Institutional Advisors

Beyond the Market: Tailoring Benchmarks to Meet Your Foundation's Goals

Cynthia J. McDonald, CTFA, National Director of Philanthropic Advice
Kenneth F. Senvinsky Jr., National Director, Institutional Investments

The significance of benchmarking in foundation investing

Unlike for-profit entities, foundations manage their investment portfolios with a distinct mission in mind – generating returns that support their charitable endeavors.

Benchmarking is a critical tool in this context, providing a standardized basis for assessing a foundation's portfolio performance and risk-adjusted returns. Some commonly used benchmarks include the major stock indices, such as the Dow Jones Industrial Average and the S&P 500. Foundations also use asset allocations and investing by peer groups as benchmarks.

By comparing a portfolio's performance against a chosen benchmark, investment managers can gauge the portfolio's alignment with the foundation's investment objectives and risk tolerance.

Tailoring benchmarks to foundation needs

The selection of an appropriate benchmark hinges on several key factors specific to each foundation.

Investment objectives

A foundation's investment objectives should align with its spending needs and risk tolerance. A growth-oriented foundation focused on maximizing long-term returns to support future grants might choose a benchmark with a higher equity allocation. Conversely, a foundation prioritizing consistent payouts to fund ongoing programs may opt for a more conservative benchmark with a larger allocation to fixed-income securities.

Risk tolerance

Foundations must carefully consider their risk tolerance when selecting a benchmark. An aggressive benchmark that reflects a higher equity allocation may offer the potential for superior returns but also carries greater risk of principal loss. Conversely, a conservative benchmark with a significant fixed-income allocation may provide more stability but with lower potential returns.

Investment constraints

Specific limitations such as liquidity needs, spending rules, and unique investment restrictions can influence benchmark selection. Foundations with spending limitations or those restricted from investing in certain asset classes may need to customize benchmarks to accommodate their specific circumstances.

Common benchmarks for foundation investment portfolios

Foundations use several types of benchmarks to evaluate their investment portfolios:

- **Broad market indices** like the S&P 500 or MSCI All-World Index represent the overall performance of a specific market segment. These serve as valuable benchmarks for foundations seeking to track their portfolio's performance against the general market's performance.
- **Asset allocation benchmarks** embody a predetermined asset allocation, such as 60% stocks and 40% bonds. They provide a reference point for foundations with established target asset allocations and can help assess how closely the portfolio's asset class weightings align with the target.
- **Peer group benchmarks** compare a foundation's portfolio to those of similar foundations, which can offer valuable insights. However, identifying appropriate peers can be challenging due to variations in foundation size, mission, and investment strategies.

Beyond benchmarks: A holistic approach to foundation investing

Benchmarks should not be the sole determinant of a foundation's investment success. Foundations should consider these additional factors:

Mission alignment

Foundations should assess how their investments align with their philanthropic mission. Can they leverage their investments to generate positive social or environmental changes that resonate with their mission? For instance, a foundation focused on environmental sustainability might consider investing in renewable energy sources or companies committed to sustainable practices.

ESG factors

Environmental, social, and governance (ESG) factors are becoming increasingly important for foundation investors. Integrating ESG factors into the investment process allows foundations to consider financial returns and the social and environmental implications of their investments.

Total cost of ownership

Fees and expenses associated with investment management can erode returns over time. Foundations should meticulously evaluate the total cost of ownership, including investment management fees, transaction costs, and custodial fees, when making investment decisions.

For more information on these topics and how KeyBank Institutional Advisors can meet your needs, please contact:

Cynthia J. McDonald, CTFA, National Director of Philanthropic Advice, KeyBank Institutional Advisors
518-257-8745, cindy_j_mcdonald@keybank.com

Ken F. Senvisky Jr., National Director, Institutional Investments, KeyBank Institutional Advisors
216-689-5183, kenneth_f_senvisky@keybank.com

KeyBank Institutional Advisors collaboratively engages stakeholders to understand their organization's strategic mission, values, and goals. Our advisors are professionals supported by subject matter experts across client disciplines/market segments. Combining our expertise with an understanding of the client, we recommend and implement customized, coordinated financial solutions.

KeyBank

240508-2591678