

Chairs' Corner – May 2008
Consolidated Endowment Fund

TO: UW Foundation, Campaign Cabinet, Deans, Development & Alumni Staff
FROM: Orin C. Smith, Chair, UW Foundation
Daniel J. Evans, Vice Chair, UW Foundation
William H. Gates, Campaign Chair

Dear Friends,

Today we will explore the mysteries and delights of the Consolidated Endowment Fund (CEF). Despite what you are thinking, this will not be a trip to the dentist or a recitation of the telephone book. You might even enjoy it.

To start with the obvious and elemental: an endowment is a gift that is meant to fund its designated purpose “in perpetuity”—forever. Forever, as our astrophysicists and paleontologists would point out, is a relative term. But at a university, forever can be a long time. If you are inclined to roll your eyes at the phrase “University of a Thousand Years,” remember that Europe’s oldest university (Bologna) will turn one thousand in 2088, and there are even older ones in Fez (Morocco) and Cairo.

So universities and their donors and lawyers take “forever” very seriously, and that concept drives all the other characteristics of endowments in general and the CEF in particular. (A few endowments have designated termination dates, but those are a very small minority.)

Suppose you and your 401-K had to last “forever.” Or suppose your family fortune had to support “in perpetuity,” and with constant purchasing power, the specific interests and proclivities of almost 3,000 of your closest immortal relatives: your son Bob’s philosophical investigations, your niece Rosa’s flamenco dancing, your techie cousin John’s penchant for invention, your granddaughter Allison’s search for a cure for cancer, and so on. How would you arrange things?

The University of Washington has come relatively late to that question. The UW’s first endowed gift arrived in 1905: \$400 from one Philo Sherman Bennett (by way of his executor, William Jennings Bryan!) to fund an annual prize for the best essay about the principles of free government, now awarded by the political science department. But it was only in 1954 that all the University’s endowments—then fewer than a hundred, mainly bequests for scholarships plus the large Walker-Ames endowment, with a total value of \$3 million—were pooled into the Consolidated Endowment Fund. Not until the late 1970s, when state budget cuts led the University to step up its pursuit of private support, did the number and value of endowments really start climbing. The first two endowed chairs, in history and medicine, were established in 1980. In 1988 the CEF investment and spending policies were updated, and in 2002 the value of the CEF reached \$1 billion, an important benchmark in the investment world.

Today (as of March 31), the CEF has a market value of \$2.1 billion and comprises 2,830 separate and astonishingly varied endowments. That puts us somewhere around number 30 (depending on what and how you count) of the country's 50 largest college and university endowments, our peer group for calculating investment performance. (The 800- and 500-hundred-pound gorillas are of course Harvard, at \$34.9 billion, and Yale, at \$22.5 billion.) During fiscal-year 2008, which ends in six weeks, the CEF will have paid out more than \$93 million to support students, faculty, and activities in virtually every department of the University.

At this level, endowment policies and procedures have become fairly standard at all institutions. Here is how it works at the UW.

Endowment gifts are made through the Office of Development, almost all (more than 90 percent) directed to a very specific purpose. For \$25,000, you can create and name an endowment that supports activities in a particular program or unit of the University—for example, a lectureship, a travel fund, a research fund, or a prize. For gifts of increasing size, you can endow an undergraduate scholarship, a graduate fellowship, a professorship, or a faculty chair, all in the field or department of your choice. (Of course, your gift has to accord with the needs, purposes, and principles of the UW.)

Currently, scholarships and fellowships make up about 26 percent of the CEF, professorships and chairs are 22 percent, general academic support is 22 percent, research activities are 10 percent, and other University activities are 20 percent. These generalities, of course, conceal fascinating individual stories: the Hans G. Dehmelt Prize in Experimental Physics, funded by our Nobel laureate, for outstanding achievements in the area of “table top” physics; the Harry Bridges Endowed Chair in Labor Studies, funded mainly by gifts from hundreds of retired longshoremen; the new Gordon Stuart Peek Endowed Fund to support the change-ringing bells just installed in the Gerberding Hall bell tower; and many, many more.

Once an endowment agreement is completed (very carefully: see “forever”) and the gift (often a bequest) is made, the funds travel to the Office of the Treasurer and are deposited in the CEF. Each endowment “buys” a certain number of CEF shares, depending on the size of the gift. The CEF, in other words, is a kind of mutual fund. Its overall goal is to generate investment returns that 1) provide annual support for the designated purpose of each endowment and 2) keep the whole fund growing, so that annual payouts can keep up (at least) with inflation and maintain their original purchasing power.

As the CEF has grown, so have the diversity, complexity, and global reach of its investments. In late 2004 the Office of the Treasurer (advised by the Regents' investment committee) hired its first Chief Investment Officer, Keith Ferguson. Mr. Ferguson and his expanded investment team search out, employ, and monitor a large stable of outside investment managers—more than a hundred, at the moment. For each asset class, from domestic equity to real assets to “non-marketable alternatives” (don't ask), there is a group of specialized managers. As we all know, diversity reduces risk.

Recent returns have been good, exceeding both the S&P 500 and the median return of our college and university peers (we generally rank in the second quartile of this group of 50). In some periods, we have outperformed Harvard. For fiscal year 2007 (ending last June 30) the CEF returned 23.3 percent. Needless to say, fiscal 2008 has not been so good, but even for the quarter ending December 31 (the latest data available) we were up 1.6 percent, as against .6 percent for our peer benchmark and -3.3 percent for the S&P 500. (In fact, since 2001 the University has been parking some of its operating funds in the CEF, to maximize returns until the dollars are spent. Currently, about 20 percent of the CEF is operating funds, categorized above as “other University activities.”)

Each year, the CEF pays out to its UW “shareholders” a total of 5 percent of its market value averaged over the prior 12 quarters, a common policy. (An additional 1 percent goes for internal fees: .08 percent to the Office of Development and .02 percent to the Office of the Treasurer.) At this level of payout, the fund can meet the current needs of recipients without jeopardizing future growth and purchasing power. The 12-quarter averaging helps smooth out the erratic behavior of the market (as in 2007-2008) and gives departments a fairly predictable flow of funds.

For each endowment, of course, the amount received depends on the number of CEF shares it holds. The funds arrive as quarterly payments to the endowment administrator in each recipient department. This is the crucial person who determines how the dollars are actually spent—and who must be exceedingly careful to parse and follow the donor’s exact intent and to keep him or her (or the family or estate) apprised. For 2,830 endowments, this is a large collective effort. In addition, the Office of the Treasurer sends the donor of each endowment a short annual report showing the amount distributed from the endowment and the current balance, as well as the investment performance of the CEF.

Are endowments the best way to give to the University? Is “forever” better than “now”—a new building, a donation for urgent current needs? The truth is, both are essential. Endowments, it is true, put a lot of money in a permanent “lockbox” and come with restrictions that can tie the University’s hands. (That Endowed Chair in Ptolemaic Cosmology that looked like such a good idea in 1400 would be an albatross, requiring a trip to court, a few centuries later.) But a base of reliable, permanent support for fundamental needs like scholarships and faculty chairs is invaluable, and has been a major goal of Creating Futures.

And the campaign has delivered, especially through the Students First and Faculty-Staff-Retiree initiatives. Even in the last couple of months, there has been a huge increase in the number of endowments. If the CEF and its many moving parts continue to work as planned, these endowments will still be nourishing the UW when Creating Futures is ancient history.

Orin, Dan, and Bill

Looking Back

- **Total Campaign giving since July 1, 2000, has surpassed the \$2.5 Billion goal. As of April 30, 2008, \$2,607,349,697 has been received.** This is outstanding news!
- The April Report of Contributions Notes is attached and contains fundraising details.

Looking Ahead

- **Friday, September 26, 2008.** Foundation Board & Campaign Cabinet Meeting, and Recognition Gala & Campaign Celebration.