Vanguard: Can You Replicate The Results Of Top Endowments?

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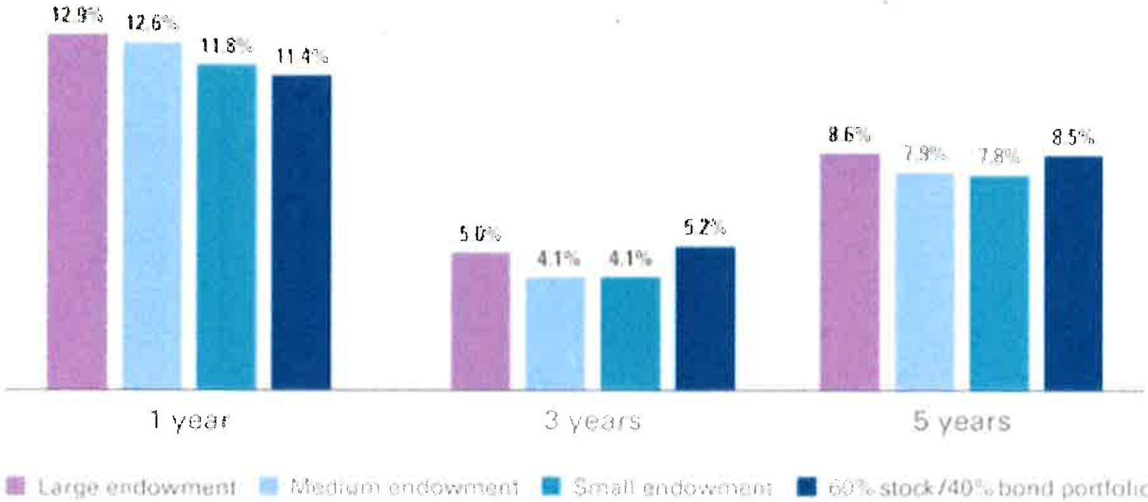
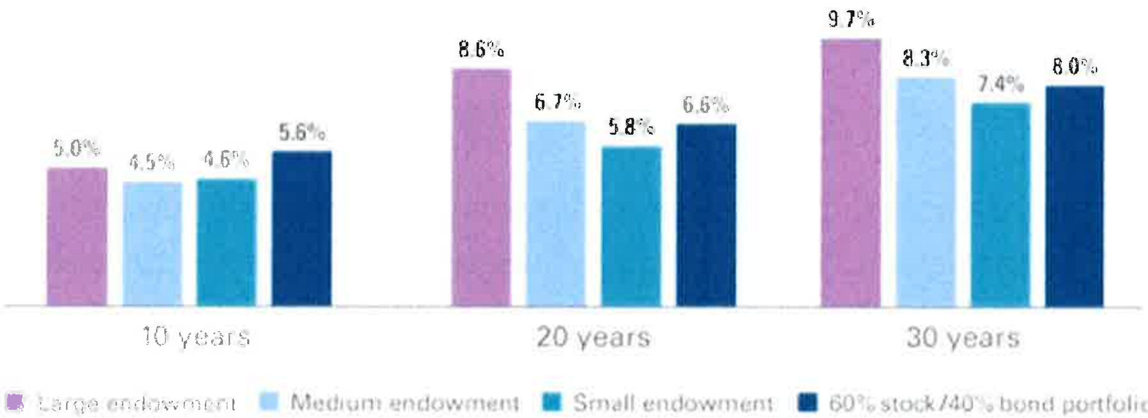
Over the past 25 years, prominent endowments have made headlines with their remarkable performance. Not surprisingly, many advisors aspire to replicate the results achieved by the top endowments for their clients. But is it realistic?

For the past 15 years, when the results from the annual NACUBO-Commonfund study become available, I've compared how a broadly diversified, low-cost balanced portfolio would have performed against the endowment universe.

The two charts below (shorter term and longer term) are the results from the 2017 NACUBO study relative to a 60% stock/40% bond portfolio.

2017 NACUBO-Commonfund study on the performance of endowment portfolios





Sources: Vanguard and 2017 NACUBO-Commonfund Study of Endowments. NACUBO stands for the National Association of College and University Business Officers. The volatility of the 60/40 benchmark is materially different from that of the NACUBO institutions' portfolios. In addition, the NACUBO institutions' portfolios may have had during the time periods noted above, and may currently have, investment objectives that are not consistent with using a 60/40 benchmark.

Data are as of June 30 for each year. Data through June 30, 2017. 60% stock/40% bond portfolio: Domestic equity (42%) is represented by the Dow Jones U.S. Total Stock Market Index (formerly known as the Dow Jones Wilshire 5000 Index) through April 22, 2005; MSCI US Broad Market Index through June 2, 2013; and CRSP US Total Market Index thereafter. Non-U.S. equity (18%) is represented by the MSCI All

Country World Index ex USA. Bonds (40%) are represented by the Bloomberg Barclays U.S. Aggregate Bond Index. The performance of an index is not an exact representation of any particular investment, as you cannot invest directly in an index. **A portfolio of actual index funds would be subject to fees and expenses that do not apply to indexes. Past performance is no guarantee of future returns.**

Two hundred and seventy-five institutions are represented in the "$101 Million to $500 Million" NACUBO cohort. The NACUBO institutions' portfolios included in this chart have the following investment allocation on average: 49% equities, 13% fixed income, 32% alternative strategies, and 6% in short-term securities/cash/other types of investments. Eighty-one percent of portfolios included in the NACUBO cohort reported rebalancing at least once in 2017. NACUBO performance data are shown net of fees. The NACUBO institutions' portfolios performance was reported to NACUBO voluntarily by NACUBO member institutions and the performance reported may have been affected by changes in conditions, objectives, or investment strategies during the time period of performance displayed above. The fees deducted from NACUBO portfolios include: (i) management fees paid to direct asset managers for investment and management services, excluding performance fees, which can vary widely and may not be indicative of expected rates for a given period; (ii) fund-of-funds fees, which represent aggregate blended management fee rates paid directly to fund-of-funds providers; (iii) advisory fees, which may include consulting fees in addition to fees for investment advisor services; (iv) fund operating expenses; and (v) custody fees. The NACUBO report notes that individual institutions may pay more or less in fees than is represented by the performance figures set forth above and that NACUBO's fee deduction method is intended to provide a representation of average fee levels rather than what any individual institution pays. Institutions in the "$101 Million to $500 Million" NACUBO cohort reported an average fee of 1.54%, excluding performance fees, as noted above.

A distinct advantage

It stands to reason that the largest endowments, here a sample size of 12%, would have some performance advantages compared with a low-cost, balanced portfolio. After all, the largest endowments have advantages that can help them succeed. They have access to top investment managers, they can leverage their size to gain lower investment fees, and they have access to investments the public does not.

Yet despite all the talent, unique access, and other potential advantages, what's interesting is how competitive a low-cost, broadly diversified, balanced portfolio could be to the endowments not in the largest cohort. During most of the time periods under evaluation, the 60/40 portfolio beat the vast majority of this sophisticated universe of active allocators.

Using technology to enhance client service

At the Inside ETFs conference in January 2018, both Vanguard CEO, Tim Buckley, and FAS head, Tom Rampulla, outlined the benefits for advisory practices to further embrace technology, while outsourcing areas such as portfolio construction, freeing up more of the advisors' time on more uniquely human tasks. The details of their talks are outlined in our recently released research paper: *The evolution of Vanguard Advisor's Alpha®: From portfolios to people.*

Advisors can easily build easy-to-implement and highly competitive investment options using ETF model portfolios or core building block ETFs or mutual funds. These approaches may seem simple at first glance, but typically, with just a few funds, your clients can own virtually the entire universe of listed stocks and bonds both domestically and internationally.

By building portfolios using low-cost, broadly diversified ETFs or mutual funds, you'll have more time to spend on behavioral coaching and relationship management. This is where you can deliver advisor's alpha and really make a difference in your clients' lives.

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Francis M. Kinniry is a principal in Vanguard Investment Strategy Group, whose primary responsibilities are capital market research, portfolio design, development and implementation of customized investment solutions, investment market commentary, and research. The group's proprietary research on investment, economic, and portfolio management issues has been published in leading academic and practitioner journals.

It also is responsible for establishing Vanguard's investment philosophy, methodology, and portfolio construction strategies. Mr. Kinniry has worked extensively with ultra high net worth families and institutional investors, creating customized portfolio solutions for their investment needs. He also initiated the Vanguard Investment Counseling & Research department and Vanguard Asset Management and Advisory Services. Before joining the company in 1997, he was a partner and senior portfolio manager for Executive Investment Advisors, Inc., an institutional asset management firm. Previously, he was a portfolio manager for H. Katz Capital, a venture capital and hedge fund manager. Mr. Kinniry has more than 20 years of experience in the industry and is a regular speaker on investment, economic, and portfolio management issues. He is a Chartered Financial Analyst® charterholder and earned his M.B.A. and bachelor's degrees from Drexel University.

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