Spring Cleaning: Polishing Your Investment Portfolio

June 2011

It is that time of year again. A time when we force ourselves to address our individual "to-do" lists despite countless work and family priorities. We recognize the importance of spring cleaning tasks as they often bring our homes in order. We feel good once they are completed as we have taken needed time to strategically prepare for the coming year.

What about those organizational "To-Dos", or the strategic thinking that lingers behind priorities that tax our day-to-day work lives? Other than reacting to negative market movements, when is the last time we asked tough strategic questions about our investment portfolio?

- Do our investment outcomes truly support our broader organizational goals and objectives?
- Are there concerns about the investment portfolio's ability to withstand further volatility?
- Is our current portfolio positioning adversely influencing our long term goals and objectives?
- Will we need to alter our goals and objectives in response to the level of volatility and support provided by our investment portfolio?
- Given our acceptable level of portfolio risk are we confident that our portfolio mix has evolved with the market?

Most organizations rely on investment policy statements to articulate their investment goals and objectives as well as the strategies they expect a manager will adhere to. However, many times established goals and objectives are not well defined, well understood or remain in place because "that's the way we have always done things." Just as an organization continually pursues operational efficiencies, investment goals and objectives should also be evaluated within the context of an ever-changing economic and capital environment.

The recent economic crisis has significantly altered the investment climate. Some institutions have responded to the crisis as an opportunity to evaluate and invest in their asset management sophistication. Strategically, many are finding themselves asking more from their portfolios at a time when market complexities are increasing. However, the process by which one assesses opportunities within an investment portfolio is often as unclear as the options. In fact, in recent years, guidance from a trusted advisor ranked as one of the top institutional investor needs.[1]

This last economic crisis has taught us that an appropriate investment strategy truly supportive of the outcomes required by an organization's broader goals and objectives needs to be tailored to that organization. Standard asset allocation models may no longer be appropriate for institutions subject to varying needs and constraints.

Investment portfolios must be viewed as tools supportive of the organization, and not as stand alone capital source that functions in isolation. To illustrate, assume we have two foundations with similar asset size and cost structures. However, they have very different funding needs, board sophistication, and fundraising opportunities. These differences should result in different return objectives and risk tolerances within their investment portfolio.

In the example below, Investor ABC enjoys a steady recurring source of contributions, an established beneficiary for its funding and a board of directors that values income/return predictability from their investment portfolio.

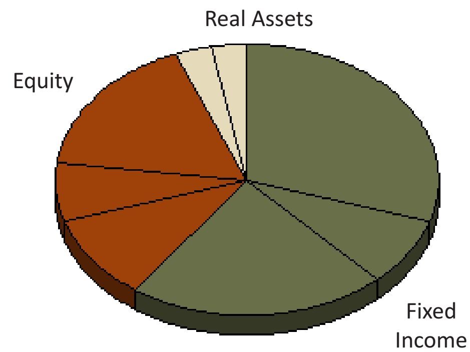
1 BNY Mellon Asset Management

Although the portfolio performed well through the crisis the board sought opportunities to further reduce volatility, while maintaining the level of portfolio income. The solution was to diversify their asset mix by including alternative investments and maintain the level of income by switching to income oriented stocks.

Investor ABC

Total Assets	$15 million
Targeted payout	5%
Required return	6%
Targeted income	3.5%
Volatility expectations	8–9%

Portfolio:
Favors consistency and conservatism

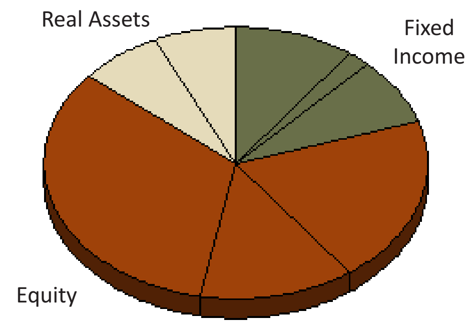


Investor XYZ has recently adopted some aggressive granting goals and wishes to support it with focused fund raising campaigns and a more aggressive investment portfolio mix. They believe a change in investment policy is supported by the commitment of some key board members and their history of delivering incremental donor support.

Investor XYZ

Total Assets	$15 million
Targeted payout	7%
Required return	8%
Targeted income	3.0%
Volatility expectations	12–13%

Portfolio:
Favors a more aggressive investment mix supported by accelerating donor support



Each of the investment strategies above began with a subjective assessment of factors influencing the organization's broader goals and objectives. Outcomes supporting those goals are then translated into income/ return targets and constrained by risk/volatility tolerances.

Making the decision to evaluate your investment strategy's effectiveness is not difficult. Lacking an investment background should not deter management or the board from engaging in a periodic review of their IPS. There are many resources, including "A Primer for Investment Trustees" published by The Research Foundation of CFA Institute, that provide a nice template.

Finally, many organizations recognize the importance of periodic review, but feel they lack the financial resources to engage consultative services. One option that far too frequently gets overlooked is leveraging the expertise of an institutional investment advisor; a premium service including partnering on periodic IPS reviews should not include too much additional expense. However, there are differences in fiduciary standards so it is appropriate to be sure your advisor is required to put your interests before their own.

A continuous process of evaluation, combined with a cost effective investment solution supportive of your evolving goals and objectives supports strategic thinking and necessitates a slot on our spring cleaning lists.

Past performance does not guarantee future results. This does not constitute an asset allocation or investment recommendation. Investors should consider investment objectives, risks and expenses carefully before investing. Investments are not FDIC insured and may lose value.