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PRIVATE WEALTH MANAGEMENT

Topics in Wealth Strategies:

Foundation & Endowment Management: Theory and Practice

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SECTION 1

Important Disclosures

Important Disclosures (1 of 2)

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Our analysis of asset classes and their effects within a portfolio is heavily dependent on our analysis of historical data. No assurance can be given that historical parameters will accurately predict future performance. Past performance is no guarantee of future results.

Investing in the market entails the risk of principal loss as well as market volatility. The value of all types of securities may increase or decrease over varying periods.

Alternative investments often are speculative and include a high degree of risk. Investors could lose all or a substantial amount of their investment. Alternative investments are appropriate only for eligible, long-term investors who are willing to forgo liquidity and put capital at risk for an indefinite period of time. They may be highly illiquid and can engage in leverage and other speculative practices that may increase the volatility and risk of loss. Alternative Investments typically have higher fees than traditional investments. Investors should carefully review and consider potential risks before investing.

U.S. tax law may limit the ability of charitable foundations to invest in high-risk investments (such as alternative investments) and such investments may subject any such foundation to significant excise taxes. Charitable foundations are therefore strongly encouraged to consult their own accounting, tax and legal counsel prior to entering into any high-risk investment, including any alternative investment.

Tax laws are complex and subject to change. This information is based on current federal tax laws in effect at the time this was written. Morgan Stanley Smith Barney LLC, its affiliates, Financial Advisors or Private Wealth Advisors do not provide tax or legal advice. Clients should consult their tax advisor for matters involving taxation and tax planning and their attorney for matters involving trust and estate planning and other legal matters.

Important Disclosures (2 of 2)

Hypothetical performance should not be considered a guarantee of future performance or a guarantee of achieving overall financial objectives. Asset allocation and diversification do not assure a profit or protect against loss in declining financial markets.

Hypothetical performance results have inherent limitations. The past performance shown here is simulated performance based on benchmark indices, not investment results from an actual portfolio or actual trading. There can be large differences between hypothetical and actual performance results achieved by a particular asset allocation. Actual performance results of accounts vary due to , for example, market factors (such as liquidity) and client-specific factors (such as investment vehicle selection, timing f contributions and withdrawals, restrictions and rebalancing schedules). Clients would not necessarily have obtained the performance results shown here if they had invested in accordance with any asset allocation, idea or strategy for the periods indicated.

Despite the limitations of hypothetical performance, these hypothetical performance results may allow clients and Financial Advisors to obtain a sense of the risk/return trade-off of different asset allocation constructs. The hypothetical performance results in this material are calculated using returns of benchmark indices for the asset classes, and not the returns of securities, funds or other investment products.

Indices are unmanaged. They do not reflect any management, custody, transaction or other expenses, and generally assume reinvestment of dividends, accrued income and capital gains. Past performance of indices does not guarantee future results. Investors cannot invest directly in an index.

Fees reduce the performance of actual accounts: None of the fees or other expenses (e.g., commissions, mark-ups, mark-down, advisory fees) associated with actual trading or accounts are reflected in the asset allocation strategy or ideas. Fees and/or expenses would apply to clients who invest in investments in an account based on these asset allocations, and would reduce clients' returns. The impact of fees and /or expenses can be material.

SIPC insurance does not apply to precious metals, other commodities, or traditional alternative investments.

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SECTION 2

Prudent Investing

Prudent Investing – Theory

Prudent investment standards are set by state law and often vary between states, but most states have adopted some form of the Uniform Prudent Investor Act (UPIA). The UPIA serves to align the interests of investors and fiduciaries by setting criteria for prudent investing. "The standards of the act can be expected to inform the investment responsibilities of directors and officers of charitable corporations…the duties of the members of the governing board of a charitable corporation are generally similar to the duties of the trustee of a charitable trust." (UPIA)

Given these standards, institutions should consider seeking comprehensive investment advice from professional financial services firms. Such a relationship may include:

- Assistance with the development of an investment policy statement (including the specification of the spending objective and determination of an overall asset allocation)
- Assistance with the selection of appropriate individual portfolio managers (including the establishment of their respective investment guidelines)
- The aggregation of performance reporting as well as specifying appropriate benchmarks
- The establishment of ongoing institution/advisor meetings (including economic and market reviews as well as forward looking strategies)

Additionally, there are numerous tax and legal consequences that may be associated with foundation and endowment investing. As such, foundations and endowments should consult their individual accounting, tax and legal advisors when making investment decisions.

Prudent Investing – Practice

In the past, the Prudent Man Rule directed trustees on how to manage their investment portfolios. The rule required that each investment be judged individually. With rapidly growing financial instruments and sophisticated investors, the rule was revised to make decisions on investments based on the entire portfolio rather than individual securities. "This approach allows fiduciaries to utilize modern portfolio theory to guide investment decisions and requires risk versus return analysis (FDIC)." This became known as the Prudent Investor Rule. The main differences between the rules are outlined below:

Then - Prudent Man

- **Restricted Investments:** The investment horizon under Prudent Man Rule was very limited. "A prudent man would make in investing property with a view to the safety of the principal and to the securing of an income reasonable in amount and payable with regularity. This limited the investments to "government securities and 'safe' stocks" and other conservative investments.
- **Investment Guidelines:** Usually specify for only equity and fixed income the maximum weight of a security and industry within a portfolio as well as on which exchanges securities may be traded and in the case of fixed income the allowable duration and credit quality of the portfolio.
- **Individual Managers:** Given that delegation of investment and management functions may not be permitted, the institution's board is responsible for aggregating investment information (including overall portfolio market value, allocation and performance) as well as hiring and firing managers.

Now - Prudent Investor

- **Diversification:** "All categorical restrictions on types of investments have been abrogated… invest in anything that plays an appropriate role in achieving the risk/return objectives… prudent investing." (UPIA).
- **Investment Policy Statement:** Specifies the risk/return profile, objectives, time horizon, tax status, liquidity (cash flows into and out of the portfolio), restrictions, the legal investment entity and any other special considerations.
- **Advisors and Managers:** Since delegation is generally permitted, the institution may hire an advisor who may perform investment and management functions for the institution thus oftentimes utilizing more sophisticated modeling techniques and more comprehensive market data and statistics.

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SECTION 3

Setting a Return Objective

Setting a Return Objective – Theory

- *Typically, foundations and endowments have long-term return objectives.*
- *The IRS generally requires foundations to distribute 5% of their assets each year in order to maintain their tax-exempt status.*
- *Endowments aim to fund projects and programs.*
- *To do this and still maintain the long-term purchasing power of the portfolio (so the institutions may remain a going concern), their portfolios are often designed to generate a return that not only funds these required distributions but also replenishes the additional annual drain on assets due to expenses and inflation.*

Setting a Return Objective – Practice (1 of 2)

Specific Target Return Objective

- Typically, foundations and endowments specify a static target return objective.
  - For example, they may have an 8.5% return objective consisting of the 5% spending rate plus a 0.5% expense ratio plus inflation of 3%.
- While this thought process may be reasonable over very long periods of time (nearing 20 years) when the annualized inflation rate may approach 3%, in the shorter term, inflation levels may vary substantially from the longer-term annualized number.
  - If there is an inflationary environment with inflation greater (less) than the targeted 3%, then the institution will not (will more than) achieve its objective.
- While this surplus/deficit in and of itself is to be expected and over longer periods of time “average out”, it may trigger foundations and endowments to question their established investment policy by significantly changing their long-term allocation targets in order to attempt to generate additional total return.

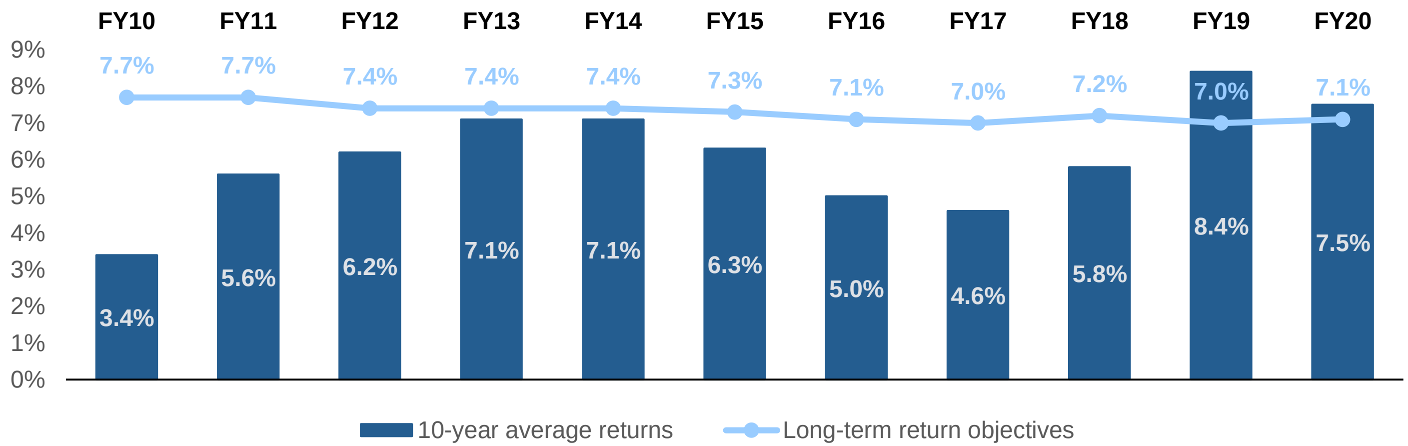
Income Matching Objective

- Oftentimes, foundations and endowments attempt to “match” the income generated by the fixed income allocation with the annual dollar payout.
- While this thought process may be reasonable over very short periods of time (1 to 3 years), in the longer-term, the significant allocation to fixed income may jeopardize the sustainability of the portfolio.
- If all the income from bonds is paid out then this portion of the portfolio may not grow over time, thus leaving a proportionately smaller part of the portfolio to bear the overwhelming burden of supplying growth for the entire portfolio.
- Additionally, another complication with this approach is that it may trigger institutions to question their established investment policy by significantly changing their long-term allocation targets in order to attempt to better “match” the income from bonds with outflows as interest rates change over time.

Setting a Return Objective – Practice (2 of 2)

- One approach to setting a return objective for foundations and endowments while maintaining the integrity of the overall portfolio in the short and longer time periods would be the following:
  - 5% spending rate + expense ratio (specified) + inflation (not specified)
- This way, the portfolios may endure the test of short and longer time horizons.
  - By not explicitly assigning an inflation rate in the objective and rather letting it “float” with changing economic environments, foundations and endowments may avoid changing their allocations in reaction to surpluses and deficits arising from inflation mismatches
  - By not matching dollar for dollar the income generated by and subsequently paid out from the portfolio and rather adopting a total return posture with respect to the overall portfolio, institutions may not feel compelled to repeatedly tweak their allocations to fixed income.
- Most importantly, by establishing a sustainable return objective, entities may be able to better avoid the increased volatility introduced to their portfolios (and not repeatedly changing their longer-term strategic allocation targets) which may substantially decrease risk adjusted returns.

Average 10-year annualized returns and long-term return targets



Source: NACUBO - TIAA Study of Endowments Report 2020

1. The data provided here is the most recent data available and is subject to change

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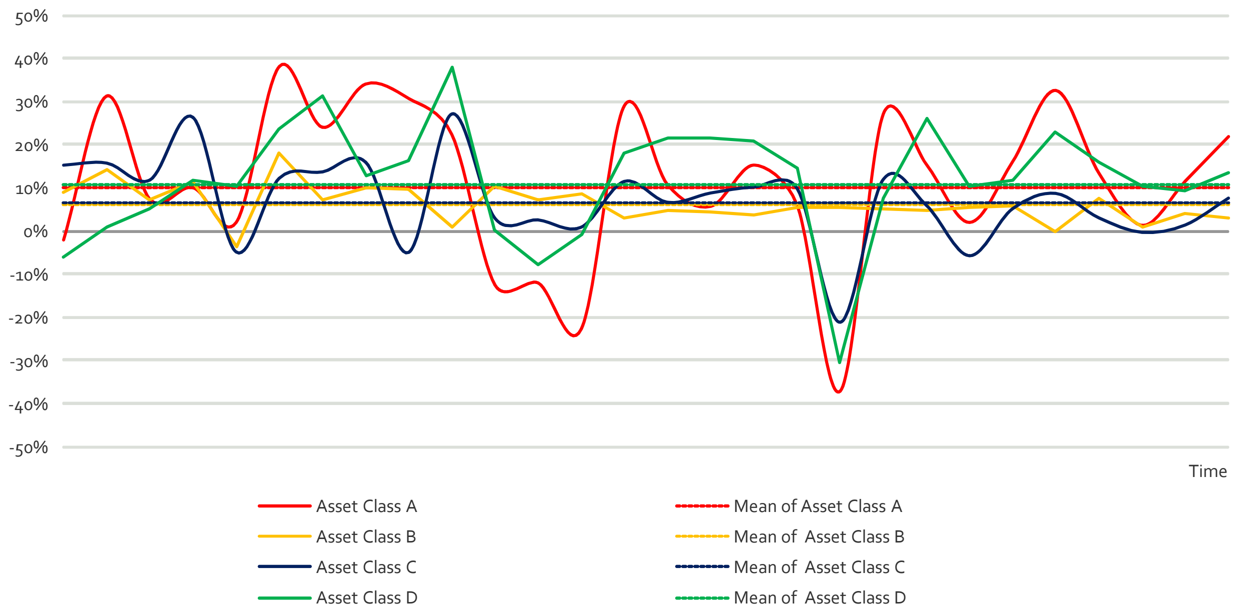
SECTION 4

Diversification

Diversification - Theory

- *By using combinations of asset classes whose return patterns differ, foundations and endowments may be able to potentially enhance their risk adjusted returns.*
- *Foundations and endowments may, however, be subject to investment restrictions imposed by Federal law that may not apply to other types of entities; foundations and endowments, therefore, are strongly urged to consult with their own advisors before entering into any alternative investment.*

Hypothetical Annual Returns of Hypothetical Asset Class A, Asset Class B, Asset Class C and Asset Class D



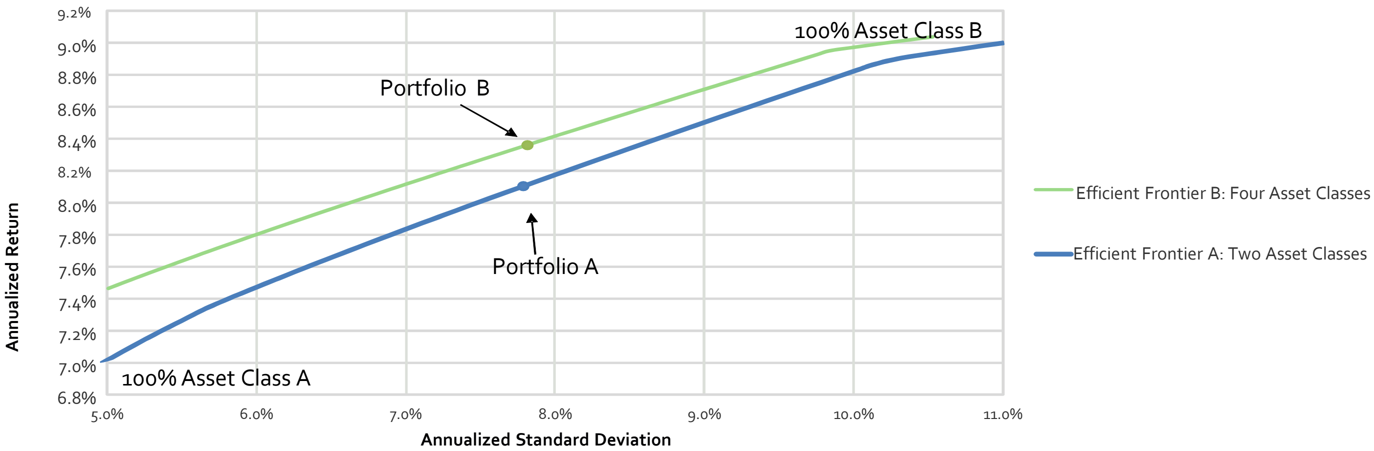
Source: Morgan Stanley Private Wealth Management

1. Past performance is no guarantee of future results.

Diversification – Practice (Hypothetical Illustration) (1 of 2)

- *Typically, foundations and endowments manage risk by restricting the inclusion of certain asset classes in their allocations.*
- *By restricting asset classes, institutions often choose among less optimal efficient frontiers rather than managing risk by choosing a portfolio from the most efficient of efficient frontiers that employs all available asset classes.*
- *The chart below shows the hypothetical efficient frontiers for different combinations of asset classes. As the number of asset classes increases, the annualized return increases due in part to diversification benefits.*
  - Portfolios A and B represent a portfolio on each of the efficient frontiers below, with similar levels of risk. The composition of these portfolios may be seen on page 16.

Comparison of Tax-Exempt Efficient Frontiers



1. Past performance is no guarantee of future results.

Diversification – Practice (Hypothetical Illustration) (2 of 2)

- *By the inclusion of additional asset classes, portfolios may experience additional return per unit of risk assumed. A risk adjusted return is a measure of how much risk a portfolio assumed to earn its returns, usually expressed as a number. This is often represented by the Sharpe Ratio.*
- *The greater the Sharpe Ratio, the greater return per unit of risk.*

Hypothetical Asset Class Performance

	Total Return	Standard Deviation	Sharpe Ratio
Asset Class A	10%	14%	0.48
Asset Class B	6%	3%	0.99
Asset Class C	7%	7%	0.53
Asset Class D	11%	6%	1.26

Source: Morgan Stanley Private Wealth Management

Hypothetical Asset Allocations with Risk and Return Metrics

	Portfolio A	Portfolio B
Global Equity	**38%**	**37%**
Asset Class A	38%	37%
Global Fixed Income	**62%**	**43%**
Asset Class B	62%	43%
Global Alternatives	**0%**	**20%**
Asset Class C	0%	7.5%
Asset Class D	0%	12.5%
Total	**100%**	**100%**
Average Annual Return	8.0%	8.3%
Annualized Std Devation	7.5%	7.5%
Sharpe Ratio	0.66	0.70

Source: Morgan Stanley Private Wealth Management

1.Past performance is no guarantee of future results.

2.Historical data is used in order to illustrate the risk/return relationships between various hypothetical portfolios. These returns and standard deviations are not forecasts and reflect only historical performance.

3.The Sharpe Ratio of an investment is defined as an investment's mean return less the risk-free rate, divided by the investment's standard deviation.

4.The returns have been adjusted to maintain the annualized standard deviation at 7.5%.

5.Please see Appendix for indices used to approximate asset classes and for other important disclosures.

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SECTION 5

Spending Instability and Return Shortfall

Spending Instability and Return Shortfall – Theory

In his book, "Pioneering Portfolio Management", David Swensen offers substantial commentary on tax-exempt investing. While his principles and tradeoffs are provided in the context of endowments, they also hold true for foundations.*

- ***Preserving purchasing power represents a long-term goal.*** *The contract that an institutions makes with donors requires that a gift to a foundation or an endowment support the designated purpose in perpetuity. Evaluating success or failure in meeting the preservation goal requires a long-term measure, spanning generations. For example, failure to maintain the institution's value might constitute losing one half of the purchasing power over fifty years.*
- ***Providing stable operating budget support represents an intermediate term goal.*** *Because operations require stable sources of support, dramatic short-term declines in income proved difficult to accommodate. Spending trauma could be defined by a one quarter reduction in real distribution over five years.*
- ***Unfortunately, a clear, direct trade off exists between preserving purchasing power and supplying stable support for operations.*** *The challenge for investors lies in selecting the portfolio best suited to satisfy, to the extent possible, both goals. Fashioning quantitative tests of performance relating to the two goals facilitates portfolio choice.*
- *Although obvious obstacles prevent reaching agreement on precise definition of failure to preserve foundation or endowment assets and failure to provide stable operating budget support, obtaining reasonable consensus on the rough equivalence of the two measures proves essential for evaluating trade offs between the two goals. The process of considering trade offs requires investors to treat the quantitatively defined goals as reasonably similar in importance.*

*The authored book covered in this material does not constitute an endorsement, authorization, sponsorship by or affiliation with Morgan Stanley. Morgan Stanley has not reviewed the books for approval and is not responsible for the information contained therein.

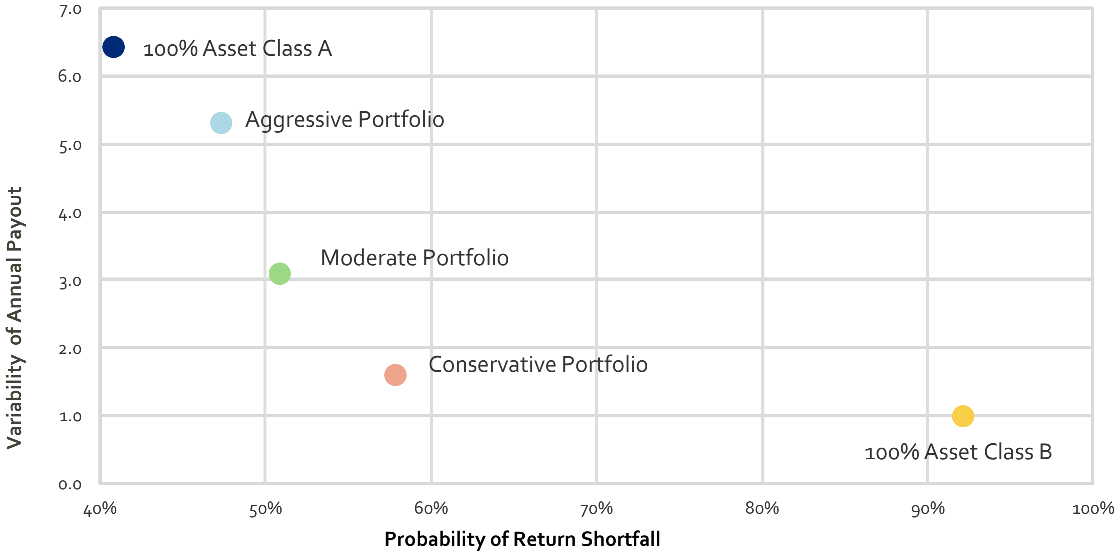
Spending Instability and Return Shortfall – Practice (1 of 2)

Return Shortfall	Spending Instability
• Typically, institutions specify a specific return objective. – For example, an institution may have a 8.5% return objective consisting of the 5% spending rate plus a 0.5% expense ratio plus inflation of 3%. – In trying to achieve this return objective, institutions may allocate a larger proportion of their assets to potentially higher returning/higher risk asset classes.	• The result of larger allocations to potentially higher returning asset classes is the potential assumption of additional risk, which can include but is not limited to portfolio return volatility. • While an institution's annualized return over time may appear acceptable, the actual dollar growth of the institution, subject to the volatility of its returns, may not keep pace with inflation – For example, if in the first couple of years of an institution's existence, it realizes negative returns, it likely will take more than a couple of years of positive returns for the institution's asset base to match its original funded dollar amount. • The result of a fixed 8.5% payout from a volatile asset base may be – A large range of dollar payments made by the institution. – Impaired dollar payments due to years of poor performance.

Spending Instability and Return Shortfall – Practice (Hypothetical Illustration) (2 of 2)

- *The chart illustrates the trade-off between the two core objectives of spending stability and institution's preservation based upon the hypothetical asset class characteristics.*
- *The risk of long-term purchasing power impairment reduces significantly when moving into additional more aggressive asset classes from a single conservative asset class portfolio.*
- *Based upon this hypothetical illustration, investing only in one aggressive asset class relative to a more diversified portfolio has a higher cost in terms of spending instability.*

Hypothetical Spending Instability and Return Shortfall



Source: Morgan Stanley Private Wealth Management

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SECTION 6

Large vs. Small Institutions

Large vs. Small Institutions – Performance

The 2020 NACUBO - TIAA Study of Endowments Report states "For the past several years, many market commentators have been predicting that markets were entering a period of lower expected returns. These predictions were made against the backdrop of a decade-long bull run in equity markets and a three-decade decline in interest rates that pushed bond prices higher. Examining endowments' returns over multiple timeframes suggests that the era of lower returns may have already arrived. Endowments' one-year returns (1.8%) are significantly lower than their five-year annualized returns (5.1%), which are significantly lower than the 10-year annualized returns (7.5%). Returns then turn lower when looking across 15 years (6.2%) and 20 years (5.5%), periods that include the global financial crisis (GFC). The longest time frame captured by the survey, 25 years, also has the highest annualized returns (7.7%); this quarter century includes multiple economic and market cycles. While one-, three- and five-year returns data are interesting, endowments are likely more concerned with their annualized returns over 10 years or more. The endowment model is designed to support institutions in perpetuity, and this makes endowments uniquely positioned among various types of investors to focus on long-term returns. This dynamic is reflected in endowments' relatively large allocations to private asset classes that often tie up liquidity for extended periods. "

Average annualized returns, FY2020

	Total Institutions	Over $1 Billion	$501 Million - $1 Billion	$251 Million - $500 Million	$101 Million - $250 Million	$51 Million - $100 Million	$25 Million - $50 Million	Under $25 Million
Total Institutions	705	111	80	83	171	134	82	44
Responded Institutions	249	40	17	28	59	55	30	20
1-year net annualized return	2%	3%	1%	1%	2%	2%	2%	2%
3-year net annualized return	5%	6%	5%	5%	5%	5%	5%	5%
5-year net annualized return	5%	6%	5%	5%	5%	5%	5%	5%
10-year net annualized return	7%	8%	7%	8%	7%	7%	8%	7%
15-year net annualized return	6%	7%	6%	6%	6%	6%	6%	5%
20-year net annualized return	6%	6%	5%	5%	5%	5%	5%	4%
25-year net annualized return	8%	8%	8%	7%	7%	8%	7%	7%

Source: NACUBO - TIAA Study of Endowments Report 2020

1. The data provided here is the most recent data available and is subject to change.

Large vs. Small Institutions – Asset Allocation

The 2020 NACUBO - TIAA Study of Endowments Report states ".Across all participating endowments, portfolio allocations as of June 30, 2020, (the end of FY2020) were 33% in public equities (U.S., non-U.S. and global), 23% in a mix of private equity and venture capital, 20% in marketable alternatives, 12% in fixed income, and 11% in real assets. Larger endowments typically exhibited less reliance on fixed income and domestic public equities, while showing greater utilization of non-U.S. stocks, private equity, venture capital, real assets and marketable alternatives. These allocations and trends, both at the total institution level and across the size cohorts, largely mirror what was seen in FY2019."

Asset Allocations for Fiscal Year 2020

Dollar Weighted

	Total Institutions	Over $1 Billion	$501 Million - $1 Billion	$251 Million - $500 Million	$101 Million - $250 Million	$51 Million - $100 Million	$25 Million - $50 Million	Under $25 Million
Total Institutions	705	111	80	83	171	134	82	44
Equities	76.3%	76.8%	76.3%	75.0%	72.6%	69.0%	66.0%	65.8%
U.S. equities active	8.8%	7.3%	14.3%	12.1%	16.6%	19.3%	21.8%	27.9%
U.S. equities passive/index	4.1%	2.7%	7.8%	8.3%	12.7%	11.6%	16.0%	14.5%
Developed non-U.S. equities active	6.4%	5.9%	8.3%	7.9%	8.5%	7.8%	7.6%	5.5%
Developed non-U.S. equities passive/index	1.0%	0.6%	2.0%	2.8%	2.6%	2.8%	3.3%	3.6%
Emerging markets active	5.6%	6.1%	4.5%	3.7%	3.4%	3.0%	2.1%	2.1%
Emerging markets passive/index	0.3%	0.2%	0.8%	0.8%	0.7%	0.8%	0.9%	0.7%
Global equities active	6.6%	6.7%	5.0%	8.0%	6.4%	7.3%	5.2%	2.8%
Global equities passive/index	0.7%	0.7%	0.6%	0.8%	1.5%	1.7%	1.1%	2.2%
Private venture capital	9.3%	10.8%	5.0%	3.4%	1.6%	0.9%	0.4%	0.5%
Private equity	13.5%	14.8%	10.6%	9.8%	5.8%	4.6%	1.8%	2.1%
Marketable alternatives	20.0%	21.1%	17.5%	17.6%	12.8%	9.1%	5.6%	4.0%
Fixed income	12.4%	11.0%	15.0%	16.6%	20.5%	25.4%	28.6%	30.9%
Investment grade active	5.0%	4.3%	4.6%	6.7%	11.1%	14.9%	16.5%	19.4%
Investment grade passive/index	1.6%	1.0%	4.0%	3.4%	3.8%	5.2%	5.8%	7.8%
Non investment grade	0.6%	0.5%	0.8%	1.0%	1.5%	1.1%	1.7%	0.6%
Private debt	1.3%	1.3%	1.9%	1.1%	0.8%	0.7%	1.1%	0.3%
Cash and equivalents <1 year	3.8%	3.9%	3.7%	4.3%	3.4%	3.5%	3.5%	2.9%
Real assets	11.4%	12.3%	8.7%	8.4%	6.9%	5.7%	5.4%	3.3%
Marketable real assets	1.2%	0.9%	1.8%	2.4%	3.0%	2.4%	1.4%	1.6%
Private real estate	5.5%	6.2%	3.4%	3.1%	2.4%	2.1%	1.9%	0.7%
Private energy and energy infrastructure	3.6%	4.1%	2.3%	1.7%	0.8%	0.8%	0.3%	0.9%
Other	1.1%	1.2%	1.2%	1.2%	0.8%	0.4%	1.7%	0.1%

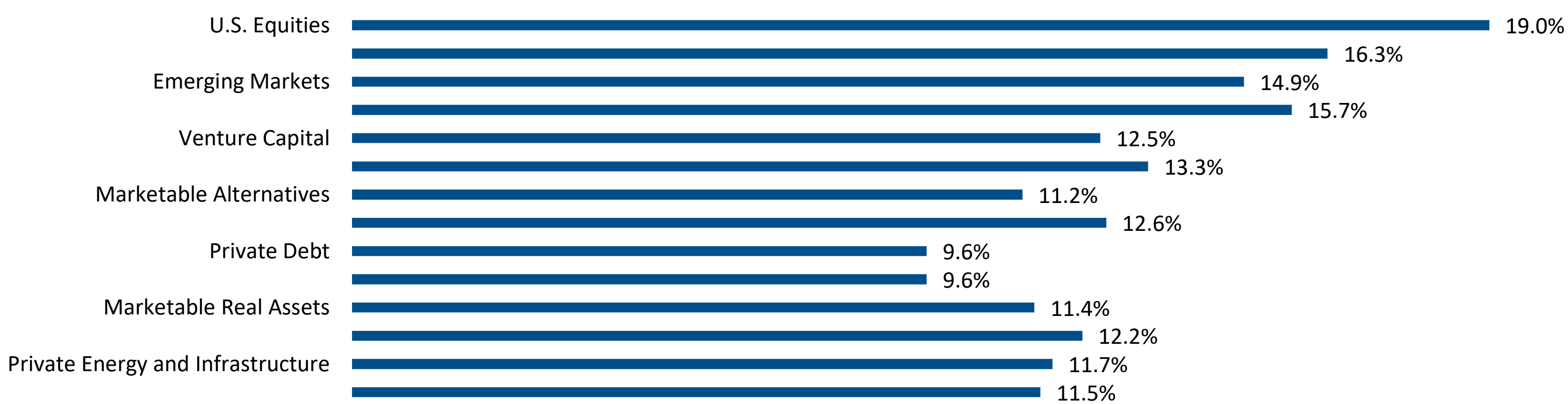
Source: NACUBO - TIAA Study of Endowments Report 2020

1. The data provided here is the most recent data available and is subject to change

Large vs. Small Institutions – Responsible Investing (1 of 2)

The 2020 NACUBO - TIAA Study of Endowments Report states "Endowments in the United States continue to take a patient, measured approach to implementing responsible investing. Many endowments recognize the investment merits of responsible investing, and this is particularly true for the largest endowments. But other endowments remain skeptical and are concerned that responsible investing may conflict with their duties as fiduciaries. In addition, practical issues related to resource limitations and the lack of standardized reporting continue to be significant barriers to adoption, especially for small and medium-sized endowments. All of these factors have contributed to limited growth in responsible investing practices among endowments. The COVID-19 pandemic and waves of social unrest expanded the ESG focus from environmental factors to social and governance factors during FY2020. And while endowments reported marginally increasing stakeholder interest in responsible investing issues in FY2020, very few reported changes to their responsible investing practices as a direct result of COVID-19. It is likely that the impacts of these events were yet to be fully realized as of the end of FY2020. This year's survey indicates that most endowments remain in the early stages of implementing responsible investing. Endowments generally don't integrate responsible investing criteria into portfolio construction in a meaningful way across asset classes. Endowments are most likely to integrate responsible investing criteria into portfolio construction in their public equity portfolios— 19% of this year's respondents incorporate responsible investing in U.S. equities and 16% in global equities."

Percent of endowments integrating responsible investing into portfolio construction by asset class, FY2020



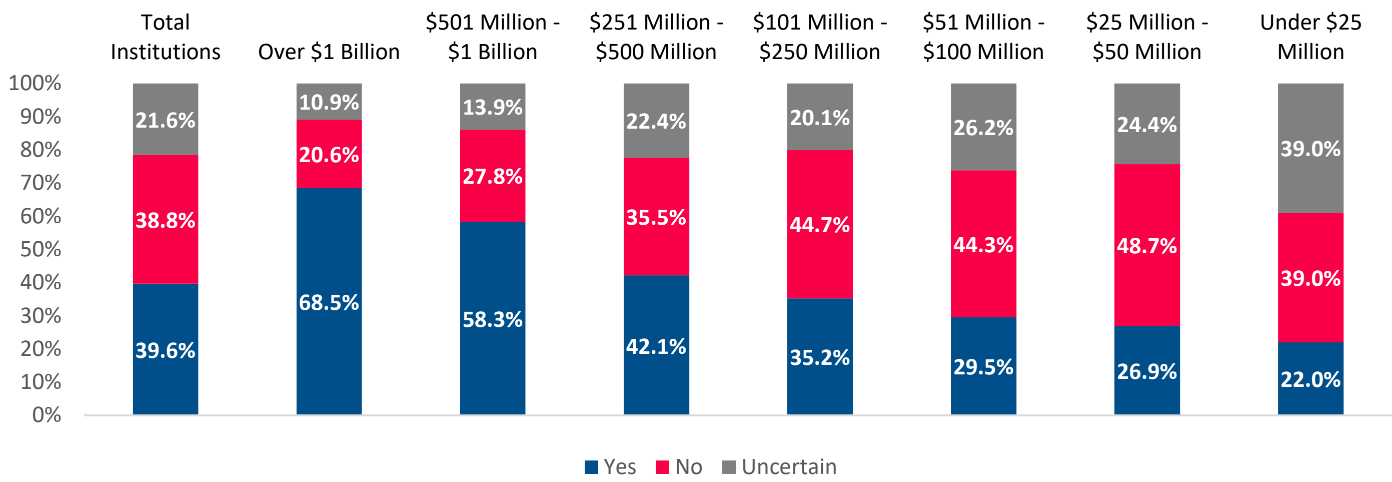
Source: NACUBO - TIAA Study of Endowments Report 2020

1. The data provided here is the most recent data available and is subject to change
2. The returns on a portfolio consisting primarily of Environmental, Social and Governance ("ESG") aware investments may be lower or higher than a portfolio that is more diversified or where decisions are based solely on investment considerations. Because ESG criteria exclude some investments, investors may not be able to take advantage of the same opportunities or market trends as investors that do not use such criteria.

Large vs. Small Institutions – Responsible Investing (2 of 2)

The 2020 NACUBO - TIAA Study of Endowments Report states "Despite the lack of consistency in responsible investing implementation in the portfolio construction process, a relatively large number of endowments reported that responsible investing considerations are a part of their investment manager due diligence and evaluation process. This is particularly true for the largest and arguably most sophisticated endowments, 60%–70% of whom said responsible investing plays a role in manager due diligence."

Does responsible investing factor into your investment manager due diligence and evaluation process?



Source: NACUBO - TIAA Study of Endowments Report 2020

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SECTION 7

Appendix

Appendix – Model Portfolio Asset Allocation

Definition of Model Portfolio Risk Profiles

- Conservative: The Investment Committee seeks a conservative approach to investing the portfolio. The Investment Committee emphasizes principal preservation over return on investment, and thus wishes only to tolerate infrequent, moderate negative returns.

- Moderate: The Investment Committee seeks a moderate approach to investing the portfolio. The Investment Committee is willing to subject a portion of their principal to increased risk in order to generate a greater rate of return. The Investment Committee understands that pursuing higher returns means that the Investment Committee may have to tolerate negative returns through phases of a market cycle.

- Aggressive: The Investment Committee seeks an aggressive but prudent approach to investing the portfolio. The Investment Committee emphasizes return on investment over principal preservation. They are willing to subject a greater portion of their principal to risk in anticipation of a greater return on investment. The Investment Committee is comfortable with fluctuations in the Portfolio, and the possibility of declines in value, in order to seek growth of the Portfolio over time.

Source: Morgan Stanley Global Investment Manager Analysis (GIMA)