ENDOWMENT REPORT

2023

BROWN

Introduction

At the conclusion of the fiscal year ending June 30, 2023, Brown University's endowment and other managed assets stood at $6.6 billion, a net increase of $75 million over the previous year. The net increase accounts for gifts to the endowment of $175 million, contributions from the endowment to the University operating budget of $257 million and investment gains of $174 million. The investment gains represent an annual investment return of 2.7%.

Over the past decade the endowment has compounded investment gains at a rate of 11.3%, and more than doubled in size, from $2.9 billion to $6.6 billion. As the endowment has grown, so has the annual contribution to the University operating budget, from $137 million a decade ago to $257 million in FY23. The mandate of the endowment's investment program is to produce investment returns sufficient to maintain the size and purchasing power of the endowment such that each gift can continue to not only make contributions to its stated purpose in perpetuity, but also such that those contributions do not lose economic value over time to the pressures of inflation. Fortunately, the investment gains have been sufficient to increase the value of those gifts substantially.

As the size of the endowment grows, the investment gains — and therefore the investment strategy — increase in relative importance to Brown's mission of scholarship and research. The investment strategy can be summarized as follows:

1. Build a team of professional investors that believe in Brown's mission and pursue a culture of excellence that is consistent with the overall quality of Brown as an academic institution.

2. Guide the investment strategy with an informed and engaged Investment Committee of volunteers from the Corporation of Brown University.

3. Partner with the best professional investment managers pursuing competitively advantaged strategies.

4. Emphasize Brown's unique advantages, particularly the community of alumni, parents and scholars who represent the core constituencies of the endowment.

5. Be empirical. Be contrarian. Be long-term. Take appropriate risk.

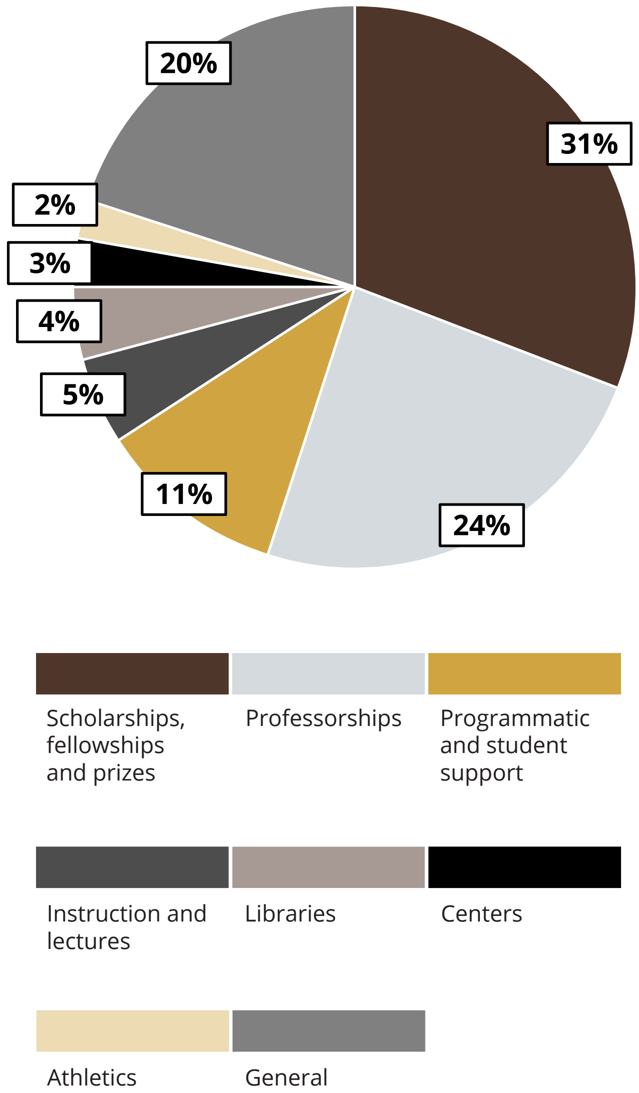
In the context of an institution in its third century, the outcomes achieved through this strategy have consistently strengthened the endowment's ability to make a significant impact on Brown's academic mission and enhance financial access for those aspiring to be part of it.

Supporting the University

The $257 million contribution to the University's operating budget in FY23 was a new all-time high. The contribution is determined annually but is always between 4.5% and 5.5% of the endowment. This payout rate is expressed as a percentage of the 12-quarter trailing average of the endowment's size. This insulates the annual budgeting of the beneficiaries of the endowment's contributions from the volatility inherent in the financial assets in which the endowment invests. As a result, the endowment's financial support for the University continues to rise to reflect the growth of the endowment in previous years. For the 2023 fiscal year, the contribution represents 4.8% of the endowment.

The University's overall operating budget received 16% of its total from the endowment's contributions in the form of financial aid, professorships, lectures and other programmatic and academic support. The providers of Brown's endowed funds have helped to shape the character of the University through these specific uses, designated to a specific purpose at the time of the original gifts that established the funds, and inextricable from the gifts. The Brown University endowment currently comprises more than 3,800 funds donated as charitable gifts to support the University since its founding.

Figure 1: Endowment Distribution by Purpose



Performance

The performance of the endowment's investment program can be assessed in multiple ways. First and foremost, the guiding principle is to ensure that the purchasing power of the endowment's financial resources is preserved for future generations in perpetuity. Another objective is that the endowment's investment performance over time should compete with market benchmarks and peer organizations pursuing similar goals of perpetual financial support to an educational mission.

This section of the endowment report will examine each of these objectives in turn, but in each case the differential between the results of FY23 and the longer-term results will merit discussion. The important context, which can be seen in the accompanying illustration (Figure 2), is that the volatility of single-year returns for the endowment has expanded in recent years. After four consecutive years of returns within 1% of one another (FY17-FY20), the returns exploded higher in FY21 (51.5%), growing the endowment by $2.4 billion in a single year.

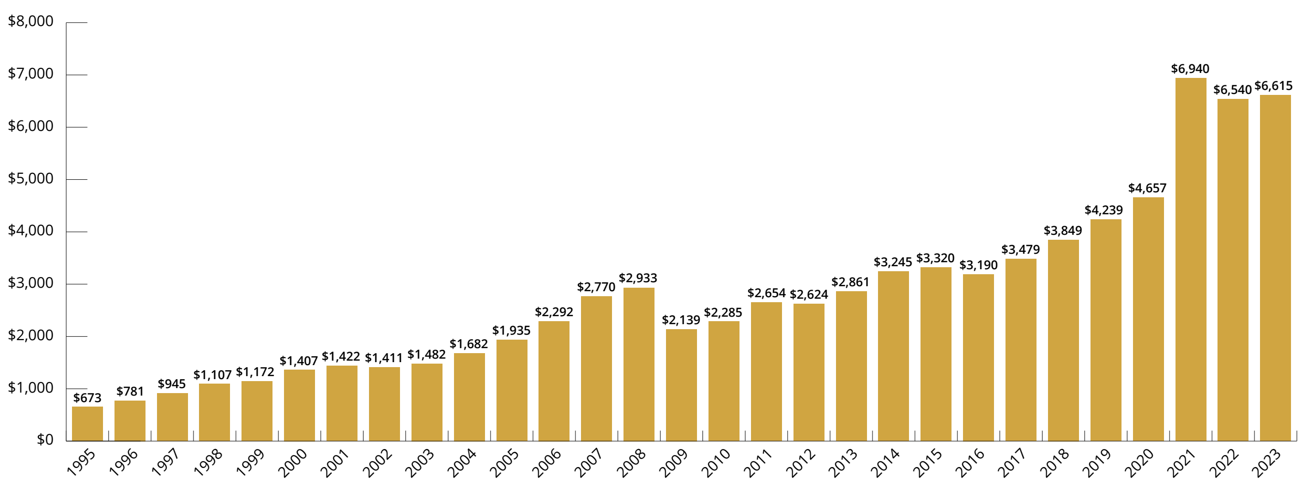
Based on the annual contribution in that year of $194 million, the investment gains from FY21 alone could theoretically account for more than 12 years of the endowment's contribution to the University's operations. That growth was, in a sense, a windfall. It was the product of significant economic distortions resulting from the pandemic and concomitant governmental fiscal policy.

Growing Brown's endowment by half in a single year was appropriately recognized as a transformational event for Brown. The annual contributions of the endowments to their designated purposes have grown rapidly as a result. However, the growth also introduced distortions to the endowment's investment program: in asset allocation, in key measures of the portfolio's liquidity, and in accurate assessments of the true value of some illiquid investments. These distortions complicated decision making for the investment portfolio.

The value of the endowment today stands slightly below its level at the conclusion of FY21. A short-term view would — accurately — identify the following two years as an unproductive stretch during which the portfolio has failed to grow at the necessary replacement rate to preserve the purchasing power of the endowment. A longer-term view would — also accurately — accede that by not relinquishing the windfall gains of FY21, the endowment's project of maintaining and growing as a financial resource for Brown's mission of scholarship and research remains on track. It is the longer-term view that carries more import.

Figure 2: Endowment Value by Fiscal Year End

dollars in millions



Performance *continued*

Spending

The investment gains of $174 million from FY23 do not entirely fund the contributions to the University. Repeating this result and extrapolating over time would quite obviously result in a deterioration and eventual depletion of the endowment's resources. Over the past decade, however, the total investment gains are $4.7 billion, while total contributions to the University are $1.8 billion, supporting a University growth strategy to increase contributions to Brown's operating budget over time. The prices for financial assets fluctuate cyclically, but the long-term growth in the endowment's financial capability to support the University has been structural in nature.

The silver lining in the category of spending is that the rate of change of Brown's most relevant measure of inflation, the Higher Education Pricing Index (HEPI), declined slightly from the prior year's measure. The 20-year average of HEPI stands at 3%.

Benchmark Comparison

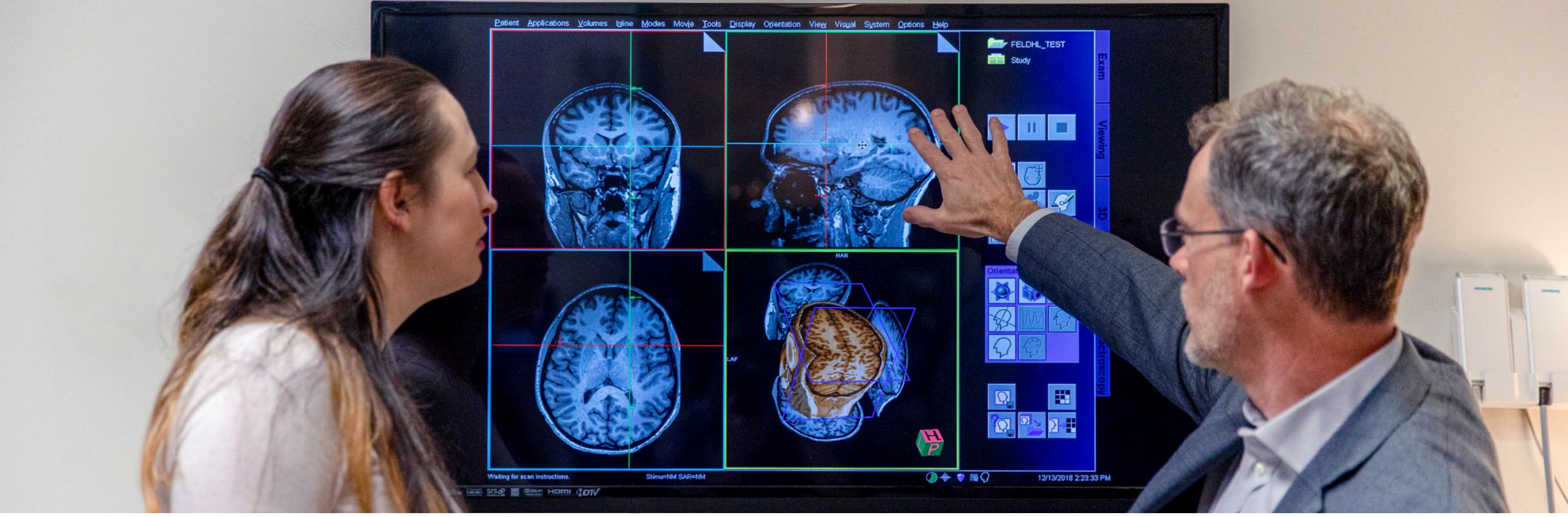
There are two essential categories of benchmarks that are useful in measuring the investment performance of the endowment: internal and external. The internal benchmark — Brown calls this the Aggregate Benchmark — combines the endowment's actual asset allocation during the year with index returns from those asset classes. The Aggregate Benchmark, in other words, does not seek to measure Brown's asset allocation; rather it seeks to measure whether, given Brown's asset class selection, Brown's investment managers added value over and above that asset allocation. External benchmarks,

Figure 3: Fiscal Year Returns
annualized returns as of June 30, 2023

	FY 2023	3-Year	5-Year	10-Year	20-Year
Brown Endowment*	2.7%	14.1%	13.3%	11.3%	9.8%
Aggregate Benchmark**	1.9%	12.8%	9.3%	8.3%	7.7%
70-30 MSCI ACWI/Barclays Global Aggregate	11.1%	6.1%	5.5%	6.3%	6.7%
70-30 S&P 500/Barclays US Aggregate	13.3%	9.0%	9.1%	9.6%	8.1%
MSCI All-Country World (ACWI)	16.5%	11.0%	8.1%	8.8%	8.2%
MSCI All-Country World (ACWI) ex-US	12.7%	7.2%	3.5%	4.7%	6.7%
S&P 500 Index	19.6%	14.6%	12.3%	12.9%	10.0%

** FY 2023 final performance includes 93.9% of private 6/30/2023 valuations, 13.4% of which are estimates.*

*** FY 2023 Aggregate Benchmark is preliminary as of 9/27/2023.*



Performance *continued*

Carney Institute for Brain Science:

The endowment-supported research at the Carney Institute for Brian Science includes the BrainGate research program, focused on developing brain-computer interface (BCI) technologies to restore the communication, mobility and independence of people with neurologic disease, injury or limb loss.

on the other hand, are market-based results that can aid in assessing the results of whether the endowment was invested appropriately overall.

In FY23, the endowment exceeded its Aggregate Benchmark but trailed most market indexes. Brown makes these data points available annually for the benefit of the endowment's stakeholders, but comparisons are most practically made over longer periods of time, which are detailed in the accompanying chart (Figure 3).

The single-year result for the Aggregate Benchmark was a gain of 1.9%, trailing the endowment's return by 80 basis points. The endowment's result has exceeded the Aggregate Benchmark in each of three-, five-, 10- and 20-year trailing periods. In the case of the 20-year measure, the endowment's result has averaged 210 basis points of outperformance. This margin indicates the value generated by Brown's external managers that invest capital on behalf of the endowment. While 210 basis points may not sound like a large number, it is very significant when compounded over 20 years. The Brown endowment has grown approximately 60% more than it would have absent this level of outperformance.

Turning to market benchmarks, Brown's 2.7% result trailed every measure of stocks and stock/bond combinations that represent appropriate measuring sticks. This is a disappointing data point. Once again, however, it is the compounded rates over longer stretches of time that best demonstrate the effectiveness of the endowment's investment program. Over three-, five-, 10- and 20-year periods (inclusive of the current year), Brown's results exceed combinations of 70% stocks and 30% bonds for both U.S.-focused and global formats, and even exceed returns generated by the MSCI All-Country World index, which is made up entirely of stocks. The sole exception is the S&P 500 index of the largest U.S.-domiciled companies, which has had an exceptionally productive decade. Even in the case of the S&P 500, however, it is worth noting that Brown has exceeded those returns on a five-year trailing basis.

Stock indexes are important benchmarks for the endowment because stocks have historically delivered a high rate of return, and access to broad market indexes like the MSCI All-Country World or the S&P 500 are liquid and available to even the smallest investors at trivial cost. Why then would Brown's endowment not pursue a highly liquid, high-returning, low-cost investment? One reason is because portfolios made up entirely of stocks tend to be highly volatile. Stock investors "earn" those high returns by enduring significant fluctuations in the value of their holdings. For an endowment with an annual payout, however, that volatility represents real risk.

Performance *continued*

The diversification that is necessary to mitigate that risk is what makes an all-stock benchmark an imperfect comparison for the endowment's investment portfolio.

A mix of stocks and bonds, such as the 70% stock and 30% bond indexes highlighted above, is a more useful comparison, not simply because a blended index mitigates the volatility of stocks, but also because it represents a simple and popular asset allocation strategy that can be easily achieved with widely available securities.

Peer Comparison

Among the universe of peers to which the endowment's investment performance should be compared, those that carried a simpler asset allocation (that is, those that owned plenty of stocks) delivered for the most part higher returns in Fiscal Year 2023. Brown's asset mix includes a significant allocation to so-called alternative investment strategies, including hedge funds and private equity. The utilization of alternative investments has been a foundational contributor to the endowment's excellent returns over the past decade, but in FY23, alternative investments mostly struggled while stocks rebounded sharply. The result of this dynamic is that Brown's FY23 investment performance trailed the majority of 161 college and university peers according to data compiled by consultancy Cambridge Associates.

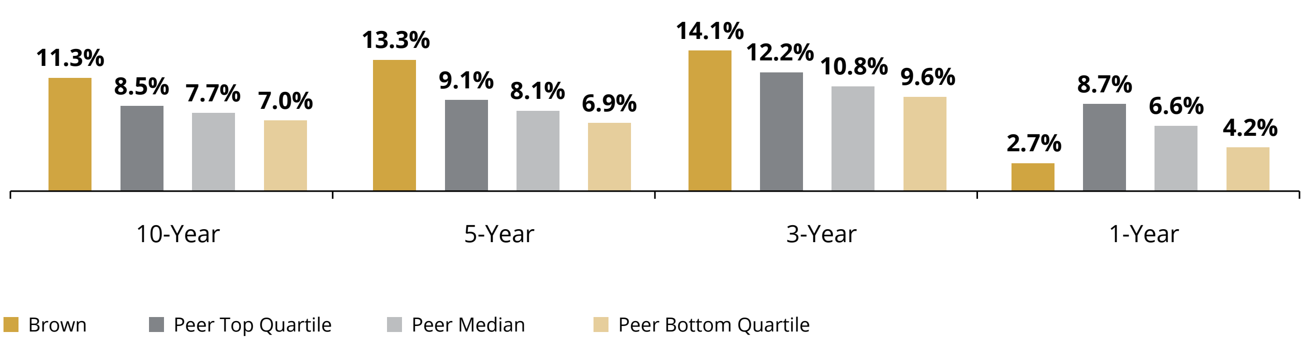
Longer-term comparisons, however, paint a brighter picture. The endowment's results rank comfortably in the first quartile for three-, five- and 10-year periods. Indeed, the endowment's margin of outperformance over a 10-year period above and beyond the threshold for inclusion in the first quartile has grown the endowment at a rate roughly 55% greater than if Brown had only achieved a first-quartile result.

In summary, the endowment's approach has generated superlative results over time, and while the current year is a disappointing result, the core strategy will remain undisturbed, albeit with necessary and ongoing minor adjustments.

Sustainable Energy Symposium:

A newly endowed gift will create the Subra Suresh Symposium at the Frontiers of Technology and Society, honoring the former National Science Foundation director and Brown professor-at-large. The symposium will bring leading scholars to campus to share their work on topics central to Brown Engineering's mission to advance technological solutions to pressing societal problems. The initial symposium in 2024 will focus on sustainable energy.

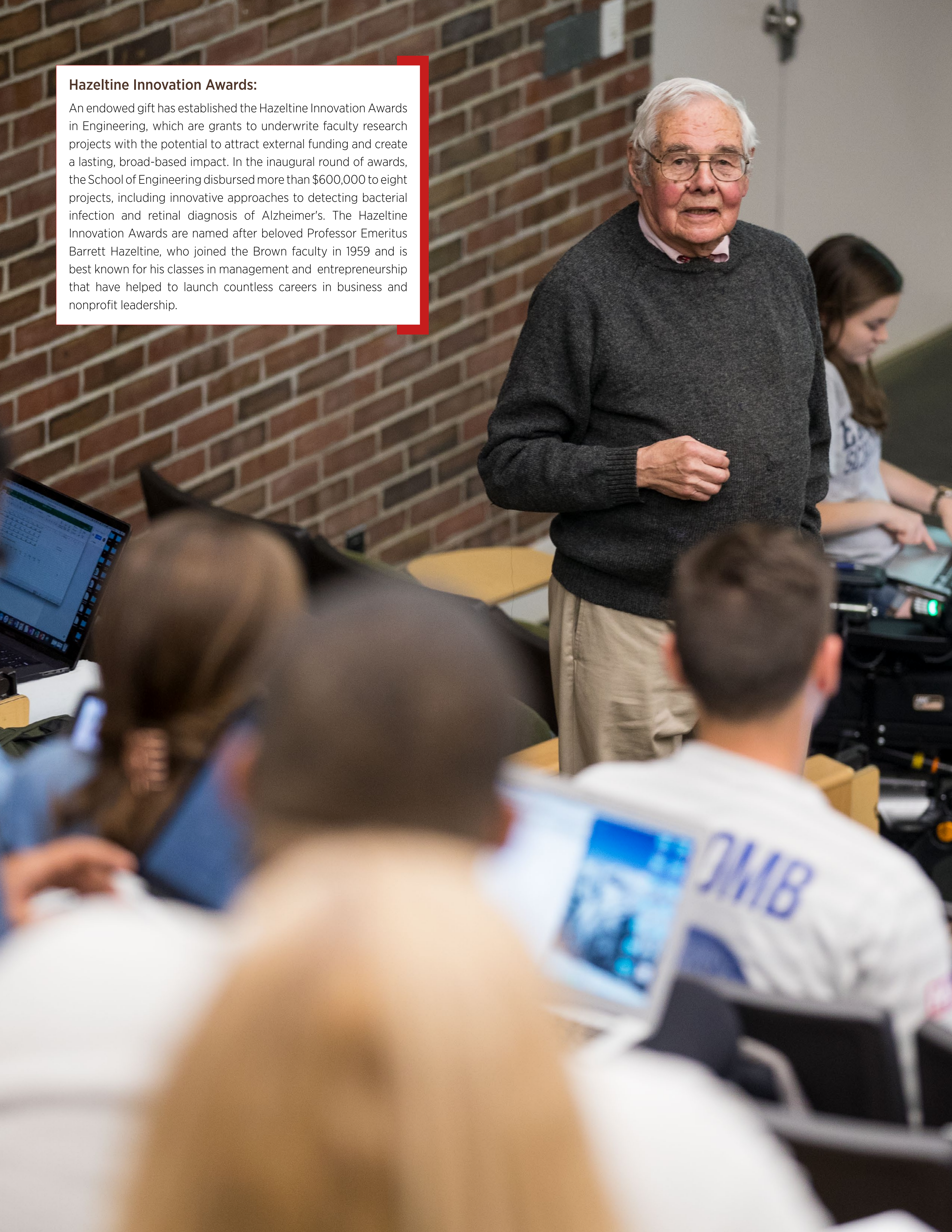
Figure 4: Brown Performance vs. Peers Through FY23
*annualized, as reported by Cambridge Associates**



**All peer quartiles calculated using Cambridge Associates preliminary data as of 10/12/2023*

Hazeltine Innovation Awards:

An endowed gift has established the Hazeltine Innovation Awards in Engineering, which are grants to underwrite faculty research projects with the potential to attract external funding and create a lasting, broad-based impact. In the inaugural round of awards, the School of Engineering disbursed more than $600,000 to eight projects, including innovative approaches to detecting bacterial infection and retinal diagnosis of Alzheimer's. The Hazeltine Innovation Awards are named after beloved Professor Emeritus Barrett Hazeltine, who joined the Brown faculty in 1959 and is best known for his classes in management and entrepreneurship that have helped to launch countless careers in business and nonprofit leadership.



Asset Allocation

In the staid world of asset allocation, this is an exciting time. Choosing the assets in which the endowment is invested is a foundational task for the investment program, and it has been animated by the return of interest rates to levels that change the fundamental arithmetic of formulating an optimal combination of assets.

Figure 5: Endowment Asset Allocation as of June 30, 2023
dollars in millions

Asset class	Market value	% of endowment
Public Equity	$968	15%
Absolute Return	1,380	21%
Private Equity	2,637	40%
Real Assets	729	11%
Asset class	**$5,715**	**86%**
Fixed Income	$466	7%
Hedges	0	0%
Cash and Receivables	434	7%
Total Endowment	**$6,615**	**100%**

In the years since the global financial crisis of 2008, the decline of interest rates to historically anomalous levels has had a broad impact. Interest payments on cash balances became trivial, and the returns on all but the riskiest of debt instruments fell to paltry levels. But the second-order effects were arguably greater: The employment of large levels of debt in the levered purchase of companies became commonplace, and assets with very long duration — meaning assets whose payoff remains far into the future, such as unprofitable growth companies — were bid up to high valuations. The largest impact of the era of low interest rates may have been that the risk of investing capital in exchange for a potentially huge but uncertain payoff far into the future became not only tolerable but increasingly attractive as prices rose ever upward.

There is virtually no financial asset that does not, in some way, derive its value from the level of interest rates. The future level and direction of interest rates will impact each of the asset classes in which Brown invests, and this section will highlight each of those in turn. As ever, the task is not to make a forecast and optimize a portfolio that will thrive in one set of future circumstances; rather, it is to construct a portfolio that can be productive regardless of any set of future circumstances.

Public Equity

Public Equity strategies comprise 15% of the endowment, or $968 million. These strategies generated profits of $133 million during the fiscal year, performing in line with benchmarks. Stock markets rebounded during the period after steep declines in the prior year, supported predominantly by steady declines in inflation readings. The performance of the S&P 500 during the year masks an unbalanced set of returns, however, as a handful of the largest technology companies posted impressive gains on the promise of productivity enhancements and new

Asset Allocation *continued*

product launches derived from advances in AI (generative artificial intelligence). For the rest of the stock market, especially smaller stocks, gains were more difficult to come by as interest rates moved steadily higher.

The endowment's opportunity set is global, and the Public Equity portfolio is split approximately evenly between U.S. markets and International Developed Markets, with a smaller allocation to Emerging Markets. Of these three, only Emerging Markets struggled during the fiscal year, as China's economy recovered more slowly than expected following the dismantling of COVID-19 pandemic restrictions. Increased political tension between the U.S. and China has manifested itself in constraints on foreign capital introduced by both parties. Although China has been a productive destination for investment opportunity historically for the endowment, the heightened uncertainty is precipitating a fundamental re-assessment of the role China can play for the portfolio — across asset classes — going forward.

Absolute Return

Absolute Return strategies represent 21% ($1.4 billion) of the endowment, and generated $48 million in profits for a 3.7% return. A portfolio of Absolute Return strategies, when working properly, should generate consistent returns with only limited correlation to broader equity markets. In recent years, the endowment's historically productive Absolute Return portfolio began to show signs of excessive correlation: to each other, to other significant asset class exposures (Venture Capital), and to broader markets. The returns generated by these strategies are valuable to a diversified portfolio precisely because of their limited correlation, so the endowment commenced a restructuring of the asset class that is now nearing completion.

The success of the actions taken will have to be judged over the coming years. But early indications suggest that the portfolio is capable of returning to its former health: steady returns, mostly independent of market direction, with sufficiently accessible liquidity. FY23's results, in fact, were held back by the decline in valuations of private, immature growth companies, which are more appropriately the domain of venture capitalists. These are precisely the type of investments the endowment has marginalized in the Absolute Return asset class. Finally, the prospect of structurally higher interest rates actually holds promise for higher returns for many of the strategies that make up the portfolio.

Private Equity

Private Equity is the largest asset class at 40% ($2.6 billion) of the endowment. There are two primary strategies within Private Equity: Buyouts and Venture Capital. Combined, these delivered losses of $81 million during the year.

Asset Allocation *continued*

Venture Capital is the larger of the two strategies, at $1.5 billion, and generated losses of $161 million as the re-pricing of young private companies continued into its second year. Brown's Venture Capital portfolio has been without peer in terms of returns for the past decade, compounding at a rate of 20% annualized. Venture Capital, in other words, grew its way to becoming the endowment's largest exposure. Valuations became unsustainably high in the wake of the distortions of the pandemic — another product of low interest rates — but signs of the return of rational capital allocation are becoming evident.

In Buyouts the focus is on mature companies. Typically, the lower growth but higher profitability of these companies is enhanced by significant amounts of borrowed money. Higher interest costs on that debt are likely to present challenges to this model. The characteristics of the endowment's Buyout portfolio, however, were selected in part to be complementary to the Venture Capital portfolio. These characteristics include lower leverage ratios, lower valuations and diverse sector exposures. As a result, in a year in which Venture Capital struggled, Buyout strategies generated $76 million in profits, an 8.2% return, and have compounded the endowment's capital at a 14.9% rate over the past 10 years.

Real Assets and Credit Strategies

Real Assets and Credit Strategies are smaller allocations, though each is growing in importance, and today they combine to be 18% of the endowment. Real Estate and Commodities are the primary components of the Real Assets portfolio, which generated $18 million in gains for the fiscal year, despite comparable benchmarks producing losses. Real Estate assets have been negatively impacted by changes in interest rates, but the endowment for the most part has refrained from investing in traditional real estate areas where the challenges currently appear steepest. Instead, Brown has opted for more niche strategies such as investing in digital infrastructure. The banking crisis that claimed several regional banks in March 2023 will only serve to exacerbate the financing challenges faced by asset owners, as regional banks provide a significant amount of commercial real estate financing.

Credit Strategies represent a broad set of potential investment opportunities, held together by the common thread that, in each case, Brown is acting ultimately as a lender. In recent years the endowment has laid the groundwork for a portfolio of managers pursuing differentiated approaches, each of which are capable of generating attractive returns at reasonable levels of risk. This is a goal that felt virtually unachievable during the period when interest rates were effectively zero. Although rising interest rates tend to drive down the prices of existing debt securities, Credit Strategies produced $47 million of profits for FY23, outperforming benchmarks.

In Closing

Despite two consecutive years of effectively flat returns, the endowment has grown dramatically over the past 10 years, and the impact on the University is significant. This was the result of prudent asset allocation and manager selection decisions, and Brown's endowment performance over that period of time ranks among the top 5% of all endowment peers.

What has worked well for the past decade, however, has no guarantee to be what continues to work well. In financial markets, as elsewhere, change is constant and adaptability is an essential characteristic of long-term success. Over the past two years, the adaptation of the stewardship of the endowment and the financial resource it represents has been a constant focus. Amid that perpetual adjustment, the foundation of that stewardship remains: a repeatable process, rooted in risk assessment, leveraging world-class partners and benefitting from expert counsel.

BROWN

Investment Office
Brown University
Box C
Providence, RI 02912
Phone: 401-867-3998

Cover Photo: Among Brown's major capital projects in FY23 was the completion of The Lindemann Performing Arts Center on Angell Street.

- Photo by Nick Dentamaro

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