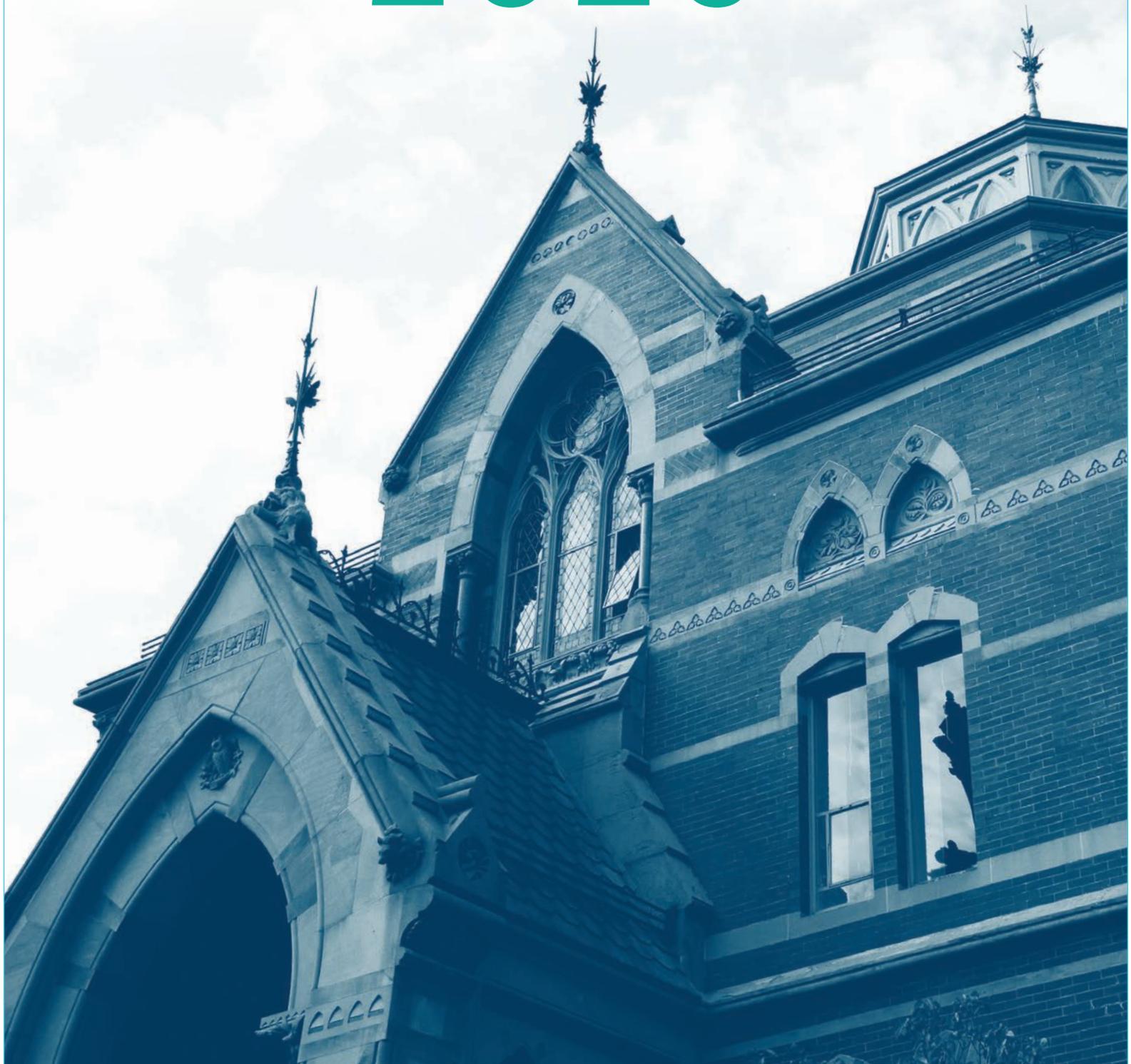


INVESTMENT OFFICE

BROWN UNIVERSITY

ENDOWMENT REPORT

2020



INTRODUCTION

During the fiscal year from July 1, 2019, to June 30, 2020, Brown University's endowment and other managed assets generated \$504 million in investment gains, equating to a 12.1% return. It was a year of economic, political and social upheaval — much arising out of the global COVID-19 pandemic — that resulted in substantial volatility in the prices of financial assets. The endowment's portfolio, managed by a group of superlative external investment managers, is diversified across asset classes, geographies and industries in order to survive and even thrive in unforeseen circumstances. Those of the preceding year certainly qualify. After accounting for investment gains and gifts of \$100 million to the endowment, and after adjusting for spending and expenses, the endowment and other managed assets totaled \$4.7 billion for Fiscal Year 2020. This total is an increase of 9.9% over the prior year and represents a high-water mark for the endowment.



BROWN

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SUPPORTING THE UNIVERSITY

The endowment is a financial resource for the University, and a fundamental measure of success is what it can sustainably contribute financially on an annual basis. This year, the endowment provided \$171 million to the overall annual operating budget. This contribution represents approximately \$17,000 per student in a diverse array of programs, many of which are supported by their specific endowed funds. Scholarships and prizes, endowed professorships, lecture programs, library resources and athletics facilities all receive support. The largest portion of these funds constitutes financial aid.

The endowment contributes between 4.5% and 5.5% of its value to the University each year. The specific percentage is determined by the Corporation of Brown University, and the value is calculated on a 12-quarter trailing basis, which serves to shield the budget from the volatility of financial markets. For FY20, spending totaled 4.9% of the endowment's value.

The initial contribution to the University's endowment was made in 1769, and its value and annual contribution have grown steadily since then, thanks primarily to gifts from benefactors that sought to shape the character of Brown and ensure its long-term financial security. When crisis occurs, as it has so often since 1769 but rarely so emergently as during the pandemic that emerged in 2020, a question invariably accompanies it: Why not spend more from the endowment to support Brown through this time of need?



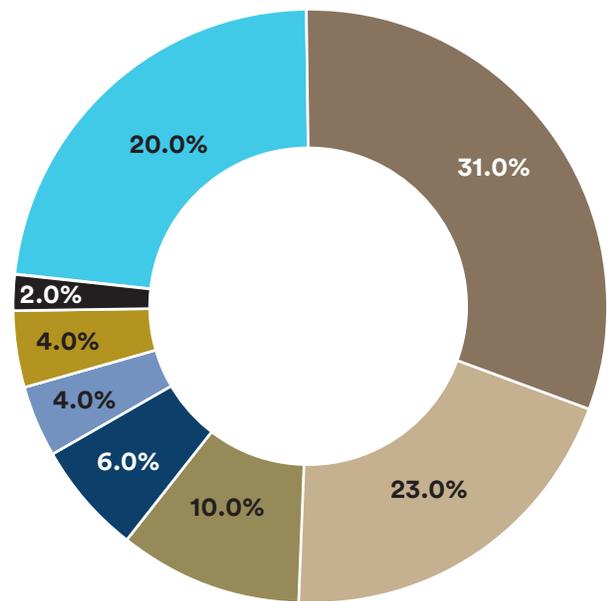
SUPPORTING THE UNIVERSITY *continued*

The primary answer to this question is that most of the endowed funds are restricted to specific purposes, so an increase in spending would not necessarily provide increased flexibility in meeting the financial needs that are most pressing for Brown today. Endowed gifts are accepted with a solemn — and legally binding — obligation to steward and spend the funds for the intended goal and over the intended duration. The fulfillment of the goal may vary (e.g., a named scholarship or an endowed faculty chair in a specific area of study), but the duration is always the same: perpetuity.

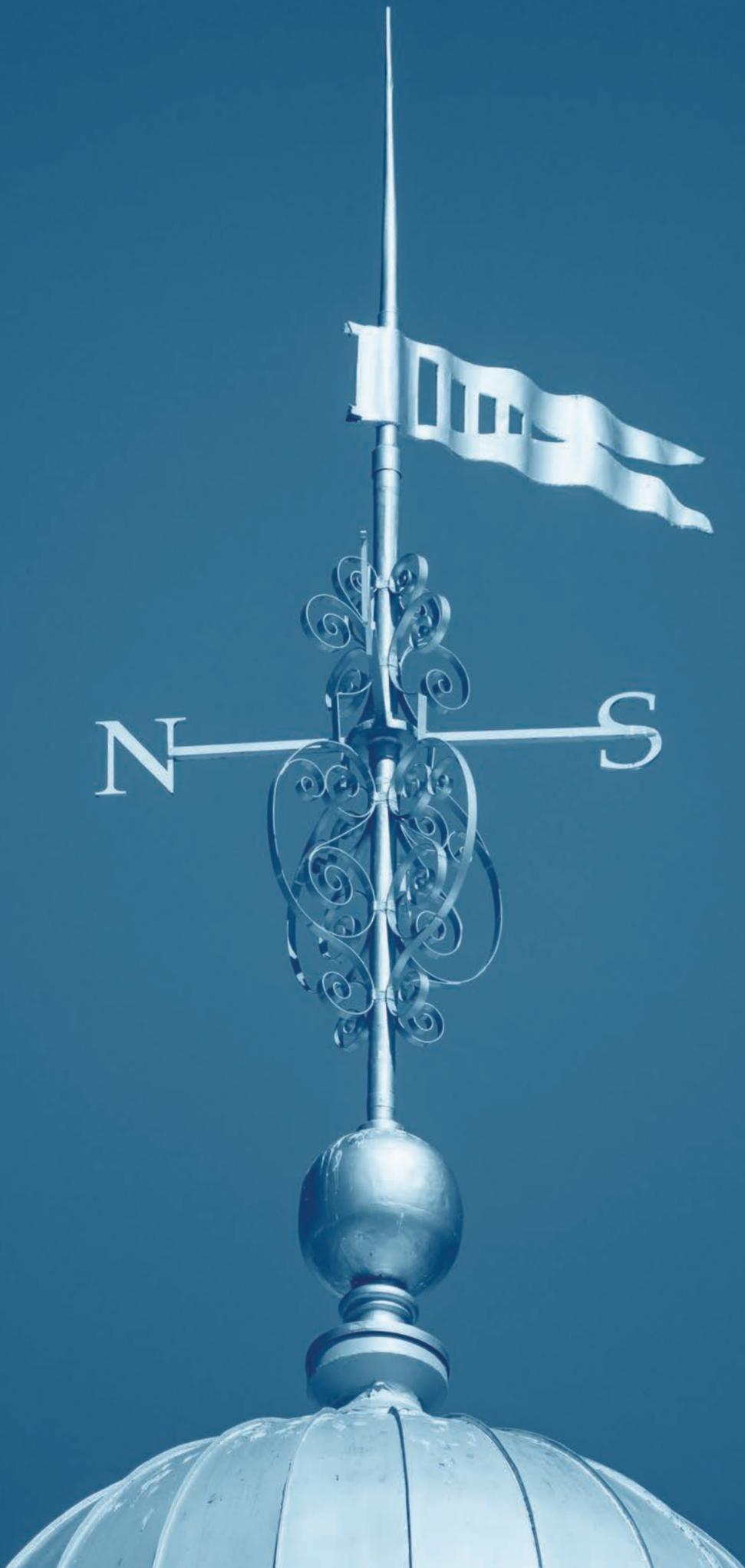
A secondary but vital answer to this question is that the endowment is not a financial resource solely for today's stakeholders in Brown's mission. It is also a resource for all of tomorrow's stakeholders. Future students, faculty, staff and alumni will face future emergencies and opportunities, and will rely on the endowment as a critical financial resource just as we do today. To represent their interests is the meaning of stewardship.

The draw on the endowment will, in fact, increase in the coming year to help alleviate the University's current financial challenges resulting from decreased revenues and increased expenses associated with operating during the global pandemic. The decision of how much to increase spending from the endowment, which is made by the Corporation of Brown University, must balance today's clear needs with tomorrow's potential needs and opportunities.

Endowment Income by Gift Purpose



- Scholarships, fellowships and prizes
- Professorships
- Programmatic and student support
- Instruction and lectures
- Centers
- Libraries
- Athletics
- Other



PERFORMANCE

In order to maintain the positive impact of the endowment on future stakeholders, the investments of the endowment must, over a long period of time, grow at a rate that exceeds the rate of spending. This growth must be in real terms, meaning it must be in excess of the rate of inflation, in order to maintain the purchasing power of the endowment. The inflation rate, as measured by Commonfund's Higher Education Price Index, totaled 2.2% for FY20, bringing the combined hurdle of spending plus inflation to 7.1%. The endowment's investment performance in FY20, as well as in all trailing time periods, exceeds this hurdle. The implication is that the impact of the endowment on Brown's educational mission is growing in importance over time.

Having achieved the paramount objective of exceeding the rate of spending, the Investment Office applies other benchmarks to the performance of the portfolio. The Aggregate Benchmark is an internally maintained measure that combines the endowment's asset allocation with the returns of market indices. Outperformance by the endowment over the Aggregate Benchmark is effectively a way to test the extent to which Brown's

external investment managers have contributed additional value through active management. That favorable gap was substantial in FY20, and has been tremendous in recent years. The Investment Office estimates that the outperformance of the endowment over the Aggregate Benchmark over just the last five years amounts to approximately \$882 million, nearly a fifth of today's total value.

The endowment's performance fares well against other relevant benchmarks. A traditional mix of 70% global stocks and 30% global bonds has underperformed Brown's endowment in all trailing time periods, as has the most commonly used measure of global stock markets, the MSCI All-Country World Index.

At the same time, a portfolio comprised entirely of stocks would not be appropriate for the Brown endowment. Despite the fact that a long time horizon confers a competitive advantage in making investment decisions, the high historical return from stocks has come with accompanying volatility that is incompatible with the University's need for a reasonably predictable stream of spending from the endowment. The endowment is

Fiscal Year Annualized Returns	FY 2020	Annualized Returns as of June 30, 2020			
	****	3-Year	5-Year	10-Year	20-Year
Brown Endowment	12.1%	12.6%	9.8%	10.2%	8.1%
Aggregate Benchmark	3.3%	6.1%	5.5%	7.0%	5.5%
70-30 MSCI ACWI/Barclays Global Aggregate	3.2%	5.7%	5.8%	7.4%	4.7%
70-30 S&P 500/Barclays US Aggregate	8.4%	9.4%	9.0%	11.1%	6.0%
MSCI All-Country World (ACWI)	2.1%	6.1%	6.5%	9.2%	5.0%
MSCI All-Country World (ACWI) ex-US	-4.8%	1.1%	2.3%	5.0%	4.1%
S&P 500 Index	7.5%	10.7%	10.7%	14.0%	5.9%

The Aggregate Benchmark performance is preliminary as of October 8, 2020.



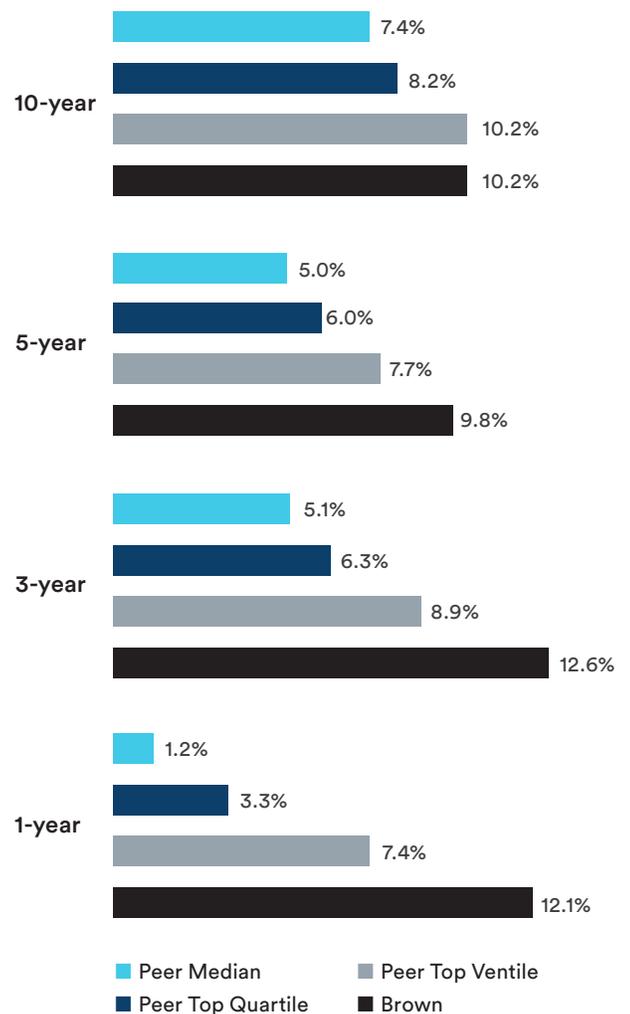
PERFORMANCE *continued*

invested in a portfolio that is diversified across asset classes and geographies in order to generate returns that are not only competitive, but sufficiently steady to avoid resulting in fluctuations in the University’s finances.

The Sharpe Ratio is a measure of a return stream adjusted to reflect the accompanying volatility, a proxy for the risk of an investment portfolio. Investment consultancy Cambridge Associates maintains a database of the Sharpe Ratios of college and university endowment portfolios. On a trailing 5-year basis, Brown’s Sharpe Ratio now ranks first out of the 140 endowment portfolios that Cambridge monitors.

The benchmarks for performance described adhere to a priority in terms of importance. Foremost is exceeding spending plus inflation, as that is imperative to the University. Second is exceeding the aggregate benchmark and other market measures, which addresses the question of whether the investment program is adding value over low-cost alternatives. Measurement against the results of peers should be considered a distant third, but a comparison is important nonetheless as an assessment of the stewardship of the endowment by the Investment Office with oversight from the Investment Committee. On this consideration the conclusion is also clearly positive: Brown’s investment returns now rank among the top 5% of college and university endowment results over trailing 1-, 3-, 5- and 10-year periods.

Brown Performance vs. Peers As of June 30, 2020



Cambridge Associates as of October 12, 2020

BROWN'S INVESTMENT RETURNS NOW
RANK AMONG THE TOP 5% OF COLLEGE AND
UNIVERSITY ENDOWMENT RESULTS OVER
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ASSET ALLOCATION

The Investment Office, with counsel from the Investment Committee, is primarily responsible for making two types of investment decisions. The first is asset allocation: the selection of a mix of productive and complementary assets in which to invest. The second is manager selection: partnering with active managers with specific expertise that can add value to the capital invested in a particular asset class. The vast majority of the endowment's portfolio is managed by external investment managers.

In Brown's portfolio construction, neither of these activities has priority over the other. Rather, assessments of the opportunities in asset classes interact and inform the evaluation of investment managers that specialize in that asset class, and vice versa. An asset class that appears otherwise unattractive for investment may in fact be an ideal hunting ground for a manager that employs contrarian or innovative techniques. Likewise, an asset class that appears attractive but yields no managers that meet Brown's qualifications for partnership may require a reassessment, or may be a candidate for investment through a low-cost alternative such as an index fund. A feedback loop encourages the investment staff to constantly examine its own assumptions.

Two features of Brown's framework for asset allocation are critical to enabling this feedback loop. The first is that the investment team is composed of generalists that research investment opportunities across asset class categorizations. This enables the team to pursue attractive opportunities or exceptionally talented investment managers without asset class constraints that feel increasingly arbitrary in today's environment. The second feature is the absence of a policy portfolio with target allocations by asset class. Brown's Investment Committee sets intentionally wide ranges for asset allocation targets, empowering the investment team to focus on the fundamental merits of an investment opportunity and its context in the portfolio without excessive regard for what category it might fall into or what label might be applied.

This framework for asset allocation is not superior to alternative frameworks. Outstanding results at other institutions have been achieved utilizing asset class specialists and the risk-mitigating effects of rebalancing. The key to how effective Brown's framework has been for the University is its integration from the Investment Committee through the Chief Investment Officer to every member of the Investment Office.



ASSET ALLOCATION REVIEW *continued*

A critical product of the asset allocation process is a diversified portfolio. The endowment's portfolio is not designed to take advantage of a particular set of future economic circumstances. Rather it is intended to fare well enough to meet the University's long-term financial goals regardless of future economic conditions. For this to be the case, investments must complement each other in terms of correlation, with strong performers compensating for those that lag in a given circumstance.

For Fiscal Year 2020, the portfolio's diversification functioned as intended, reducing overall risk. It was a difficult year for the public equity and real asset components of the portfolio, but the absolute return and private equity components generated outstanding results.

Public Equities: Brown's Public Equity strategies produced a return of 2% for FY20. This trails slightly the MSCI ACWI, a benchmark of global stock markets, which generated a return of 2.1%. As has been the case frequently in recent years, U.S. markets outperformed Global and Emerging Markets. Public Equity strategies represent 14% of the endowment's capital, a relatively low level compared to the endowment's history.

Endowment Asset Allocation as of June 30, 2020

(\$ in millions) Asset Class	Market value	% of endowment
Public equity	\$666	14%
Absolute return	\$1,542	33%
Private equity	\$1,704	37%
Real assets	\$199	4%
Brown total risk assets	\$4,111	88%
Fixed income	\$327	7%
Hedges	\$1	0%
Cash and receivables	\$219	5%
Total endowment	\$4,657	100%



ASSET ALLOCATION REVIEW *continued*

Public Equity is the asset class where the case for utilizing low-cost index funds is the most compelling. Brown's use of active managers is predicated on the existence of strategies that can add value, net of fees and expenses, in markets that are less than perfectly efficient. If there is not evidence that this is the case, the endowment will seek to achieve its exposure in the lowest-cost, most-liquid format.

The Public Equity markets, however, are diverse and complex. Indexes frequently do not capture all of the potential investment opportunities, particularly in more specialized arenas such as smaller capitalization stocks or international bourses. Capital invested in index funds, furthermore, may increasingly be contributing to distortions in pricing — though the evidence is not conclusive — which should expand the opportunity set for active managers. Brown's active managers, for the most part, fared well. In both domestic and global developed markets managers exceeded their benchmarks in FY20, but trailed in Emerging Markets.

Public Equity will continue to be a cornerstone of Brown's portfolio, and the investment team will continue to pursue partnerships with active managers that have demonstrated an ability to outperform.

Absolute Return: Absolute Return strategies, by contrast, cannot realistically be imitated by indexes. This is not because the returns generated by these strategies have been strong; indeed, industry-wide returns have been unremarkable. Rather it is because of the significant diversity of investment strategies that are grouped together in this asset class. Absolute Return encompasses a broad array of investment pursuits with varying exposures to market forces and risk appetites.

Absolute Return strategies comprise 33% of Brown's portfolio. Approximately 1/3 of that exposure is employed in strategies that endeavor to take no market risk: so-called market-neutral strategies. A market-neutral approach is fundamentally a form of arbitrage. When executed properly, it employs relatively modest risk in order to achieve an outcome akin to a classic fixed income portfolio: predictable returns with easy liquidity available for reinvestment in the event of a market decline.

The remainder of the Absolute Return asset class is predominantly in long/short equity strategies, which own the equity in public and — in some cases — private companies with collective risk exposures that result in modest correlations to the S&P 500. Brown's long/short equity managers generated impressive performance,

THE ENDOWMENT'S FORMER INVESTMENTS IN
FOSSIL-FUEL BASED ENERGY NOW ROUND TO ZERO.



ASSET ALLOCATION REVIEW *continued*

returning 24% during the year net of all fees and expenses, more than tripling the 7.5% return from the S&P 500. Every single manager outperformed the index.

Overall, the Absolute Return asset class produced a return of 13%. This is the second consecutive year that this outstanding group of investment managers has exceeded the S&P 500's return.

The relative scale of Public Equity and Absolute Return in Brown's portfolio are not a reflection of a preference for one at the expense of the other. The Investment Office seeks to generate high risk-adjusted returns by partnering with managers of exceptional skill that are focused on attractive, inefficient markets. Filters for high integrity and an alignment of incentives are also meticulously applied. The portfolio's asset allocation is better understood as a product of this manager-focused search, rather than a roadmap for it.

Private Equity: Private Equity comprises 37% of the endowment portfolio. This category describes all of Brown's partners that engage in the activity of buying or funding private companies. Here again, however, the asset class can disguise the diversity of activity taking place. Venture capital managers may provide capital to fledgling companies and continue to fund their growth for years as their scale and need for capital increases, while traditional buyout managers may buy mature companies in legacy industries in order to restructure them. Several more spheres of expertise exist between those extremes, in geographies all over the world. Brown partners with both venture and buyout managers as well as investors with more refined specialties who are often focused on a single industry. The criteria for partnership with the endowment — ability, integrity and the opportunity to create value — is the unifying thread.

Brown's Private Equity portfolio produced a return of 25% for the fiscal year, led by its venture capital investments. This is a truly phenomenal performance that reflects two factors: first, the work and care of our managers who are collectively executing their strategies at a superior level; and second, the returns from private equity, and from venture capital in particular, tend to be cyclical. The venture capital industry enjoyed a strong year of initial public offerings of stock to markets eager to award high valuations. Although the returns may be lumpy, the groundwork required to generate those returns requires persistent effort over many years. For this reason, a long time horizon is imperative in private equity investing. Brown cannot realistically expect many years of returns to rival those of FY20, but Brown's managers will be consistent in the exertion of energy that periodically culminates in an outstanding result.

The endowment also has investments in real estate, commodities and fixed income that in aggregate total 11% of the portfolio and on a combined basis delivered losses in FY20. The Investment Office has been investigating opportunities and potential partners in these asset classes, and the events of 2020 may result in new investment prospects.

The endowment's former investments in fossil-fuel based energy now round to zero. Beginning several years ago, the Investment Office undertook a review of the long-term opportunity set in fossil fuels. The conclusion of this review was that, as the world shifts to sustainable energy sources, the prospective returns from fossil-fuel investments did not sufficiently compensate the endowment for the associated risks. The Investment Office began a liquidation of existing investments which is now substantially complete, and subsequently has made no new investments in fossil fuels.



THE GREAT ACCELERATION

Good investing — good business in general — requires a focus on competitive advantage. Competitive advantage describes the basis upon which an entity can produce a consistently better result than its peers. Advantages are rare, valuable and often fleeting. Brown places competitive advantage at the center of its process in selecting investment managers. Because of its scarcity, Brown is fortunate to have access to managers that possess an advantage, and the investment team works to deepen relationships with partners that deploy such an advantage skillfully, and work to extend its life.

The Brown endowment itself enjoys two such advantages, and Brown's investment program is likewise optimized to maximize their impact. The first advantage is Brown itself: Talented and successful alumni and parents in diverse industries help Brown achieve its goals out of their love for the institution and a belief in its mission of education, scholarship and research. The investment team has benefitted from referrals, candid references and insight from the Brown network, and works to increase this engagement over time. In accounting terms, this is what would be called an "intangible asset," and it is valuable.

The second advantage is the permanent nature of the endowment and the institution for which it serves as a financial resource. This permanence enables the

endowment to make investment decisions with a horizon that extends beyond many other market participants. This advantage of duration has many manifestations, including the ability to make illiquid investments and accumulate out-of-favor assets without regard for near-term price appreciation.

The extraordinary events of 2020 have thrown a new light on the advantage of having a long investment horizon. The social and economic response to the COVID-19 health crisis stimulated demand and usage patterns for technology solutions, and the companies that are at the forefront of providing those solutions have seen their valuations soar in response, while legacy companies have lagged. The endowment's exposure to this dynamic has proven to be a significant positive this year. While few anticipated the abominable impact of the public health crisis, Brown has steadily selected investment partners with a sufficiently long-term view in order to match and maximize Brown's duration advantage. These managers disproportionately held shares of companies that were likely to be the leaders of tomorrow's increasingly digitally-oriented world. This explains a component of the endowment's strong performance and is directly attributable to Brown's competitive advantage.

IN CLOSING

The 12 months that encompass Fiscal Year 2020 witnessed significant social and economic turmoil. The pandemic has been profoundly inequitable in its impact, and long-standing inequities in our society have received renewed, overdue focus. In recent years the Investment Office and the Investment Committee have allocated significant time and energy to capturing and cataloguing data addressing the Environmental, Social and Governance implications of the investment activities of our external managers. The events of 2020, however, have injected these projects with increased meaning and urgency, and our efforts have been redoubled.

The events of 2020 also serve to underscore the inherent unpredictability of future events. The endowment manages this uncertainty by creating a portfolio of investments that can endure a broad set of economic circumstances. Sufficient liquidity ensures both the ability to steadily provide resources to the University and to adapt to a changing investment landscape. In this way, the endowment will continue to play its traditional role in supporting and shaping the character of Brown.



BROWN

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