



The Dartmouth College Endowment



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INTRODUCTION

Since the founding of Dartmouth College in 1769, generous alumni, parents and friends have donated financial resources to assist the College in achieving its long-term mission of providing a superb liberal arts education for undergraduates while maintaining excellent graduate programs and professional schools. Many of these gifts, as well as certain unrestricted funds designated for long-term investment by the Board of Trustees, have been invested in the College's endowment. As a result, the College's total endowment market value is among the largest college and university endowments in the United States.

Although there are several variations, in its simplest form, an endowment fund represents donated assets permanently invested to generate an annual return for the support of College operations, both currently, as well as far into the future. Dartmouth's endowment includes over 5,000 individual funds, each with its own set of instructions regarding the purpose to be supported. Funds may be established for a specific purpose or for unrestricted general support.

There are three types of endowment gifts:

▲ *True (permanent) endowment:* True endowment funds require the College to retain the original gift in perpetuity, but permit the use of investment return in support of operations.

▲ *Quasi-endowment:* Quasi-endowment funds differ from true funds in that they allow expenditure of the original principal as well as investment return at the discretion of the Board of Trustees.

▲ *Term endowment:* Term endowment funds are true endowment funds that become quasi-endowments after a specified time period or a specific event.

PURPOSES

A wide variety of instruction, research, social, cultural, athletic and recreational activities are supported by endowment funds at Dartmouth. During the year ended June 30, 2004, nearly \$113.0 million of endowment return was expended supporting such activities. This amount represented approximately 29 percent of the College's operating expenses before auxiliaries and direct research expenses. Without

endowment support many important programs and activities would not exist or would be severely limited. Figure 1, below, shows the functional areas supported and the percentage of total June 30, 2004 endowment market value represented by each.

ENDOWMENT MANAGEMENT

Over 99 percent of the College's endowment is invested in the "Total Return Pool" and virtually all new gifts are added to

the share value at the end of the preceding month. Income yield is allocated to funds using a formula employing shares and the period of the fiscal year they were owned. Capital growth is allocated to individual funds based on the number of shares "owned" by each fund.

Annual investment performance is measured based on the concept of total return. Ordinary yield (dividends, interest, rents, royalties, etc.) is combined with realized and unreal-

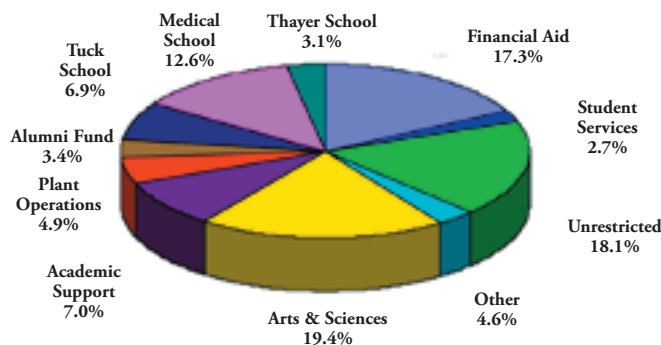


Figure 1: Endowment by area

this investment Pool. The Pool operates like a large mutual fund in that each endowment fund owns shares that represent claims on the Pool's commingled assets. Shares are valued at the end of each month based on the market value of the Pool's assets. New gifts added to the Pool "purchase" shares based on

ized capital gains (or losses) to develop a total return percentage. Investment decisions are made with a view toward maximizing long-term return opportunities while maintaining an acceptable level of investment risk.

ASSET ALLOCATION

The Investment Committee of the Board of Trustees has determined that a well-diversified mix of assets offers the best opportunity for maximum return with acceptable risk over time. Figure 2, below, reflects the asset allocation target guidelines adopted by the Investment Committee of the Board of Trustees in September 2003.

In order to achieve these targets, the College's

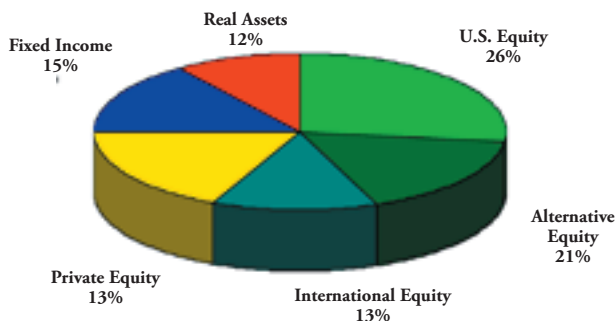


Figure 2: Endowment asset allocation targets

Investment Office contracts with professional asset managers whose expertise and demonstrated performance best match Dartmouth's investment goals in a particular asset class. The College's investment philosophy is shared with these external managers and their performance is regularly evaluated.

INVESTMENT PERFORMANCE

The College's overall performance objective is to generate sufficient returns to support current operating needs while maintaining the long-term purchasing power of the endowment fund. Historical averages indicate that an annual return between 8–10 percent is the annual return needed to provide adequate support for operations while protecting against

inflation and covering investment management fees over the long term. An additional goal is to generate return which exceeds the measure of inflation, achieving "real" growth of the endowment.

Figure 3 (next page) illustrates how successful Dartmouth has been in achieving this goal. While Dartmouth's endowment was affected by the economic recessions of the

past two decades, and most recently by the economic downturn in 2001 and 2002, prudent management and strict adherence to an overarching investment philosophy have provided long-term stability. Over the twenty-year period ended June 30, 2004, the

growth of 6.1 percent annually over these twenty years.

As of June 30, 2004, the market value of the endowment stood at \$2.454 billion. For the five years ended June 30, 2004, Dartmouth's net annualized investment return was

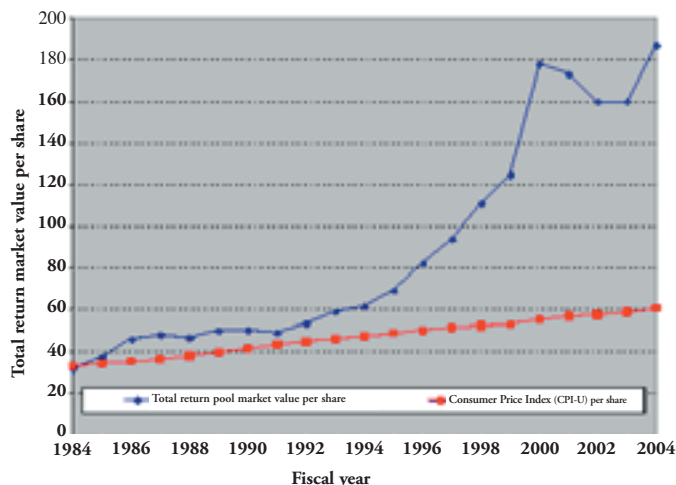


Figure 3: Total return pool market value per share vs. CPI-U inflation

Total Return Pool generated a 13.3 percent annualized total investment return net of investment management expenses. After the annual distribution to operations, the Pool's market value per share increased at a compound annual growth rate of 9.2 percent, from \$32.18 to \$187.22. Since the Consumer Price Index (CPI-U) increased by a compounded average of only 3.1 percent during this same period, Dartmouth's endowment averaged real

10.7 percent. This compares to the -2.2 percent return on the Standard & Poor's 500 equity index; 6.6 percent on the Russell 2000 small stock index; 0.4 percent return on the Morgan Stanley Capital International World Ex-U.S. equity index; 7.0 percent return on the Lehman Brothers Aggregate index and 8.9 percent on the National Council of Real Estate Investment Fiduciaries (NCREIF) index. Dartmouth's investment performance, for the

five-year period ended June 30, 2004, ranked in the top quartile of a comparative universe of college and university endowments as determined by Cambridge Associates, an independent consultant.

Figure 4 shows the Total Return Pool's five-year performance, in comparison to a diversified benchmark index that closely approximates Dartmouth's Total Return Pool asset allocation as previously defined. The diversified benchmark blends five-year investment returns according to the following percentages: 40 percent S&P 500 (domestic large stocks), 15 percent Russell 2000 (domestic small stocks), 15 percent MSCI Ex-U.S. (international stocks), 25 percent Lehman bond index (domestic bonds) and 5 percent NCREIF index (domestic real estate) to arrive at a five-year compounded growth rate of 2.8 percent. Figure 4 shows that over this five-year period, Dartmouth and its investment managers have achieved investment return in excess of comparably weighted benchmark index returns.

UTILIZATION POLICY

Dartmouth's endowment utilization policy bal-

ances support of the current generation of students and faculty with the need to preserve the College's endowment for future generations. While peer institutions have various endowment management policies, Dartmouth's is a common one, and all such policies embody the same goal of balancing current use with long-term preservation. The College's utilization policy provides that an annual amount of current and accumulated endowment investment return will be distributed from each individual endowment fund which can be utilized by the College for operations. In fiscal year 2004, the total distribution was \$114.8 million and the amount utilized was \$113.0 million. The amount of endowment return actually utilized for operations in any given fiscal year must be spent in accordance with donor restrictions, if applicable, or with Board approved directives.

To fund the annual distribution as approved by the Board and computed by the distribution formula, current yield and investment appreciation may be expended; surplus appreciation is retained in the endowment. In the event a fund has insufficient

appreciation to reach the formula amount in a given year, distribution is capped at current yield plus available appreciation. While such a limitation exists in the near-term with newly established funds, it is expected that over the long-term, positive investment performance should allow the fund to experience real growth. Beginning in fiscal year 2005, any addition

In fiscal year 2004, the College's annual distribution from endowment approved by the Board of Trustees fluctuated between a lower boundary of 4.25 percent and an upper boundary of 6.5 percent of a moving three-year average endowment market value. Beginning with the endowment distribution effective in fiscal year 2005, the Board of Trustees

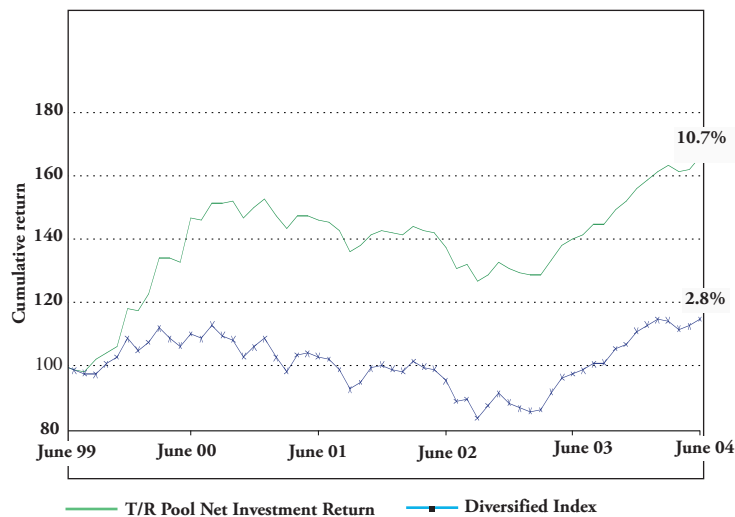


Figure 4: Five-year endowment total return vs. diversified benchmark index

to the endowment will be subject to a six-month waiting period before distributions will be allowed. The intent of this new policy is to allow these funds to retain investment growth over this six-month period to help reduce the volatility of future distributions from the funds.

approved a revised distribution formula, consistent with the College's overall endowment distribution philosophy to preserve intergenerational equity and to provide a stable distribution in support of the operating budget. This new distribution formula is designed to moderate the potential volatility of

endowment distributions during periods of large positive or negative investment returns. Specifically, the new formula requires that the distribution be calculated with 70 percent based on the prior fiscal year's distribution, adjusted by CPI; and 30 percent based on a pre-determined percentage of the four-quarter trailing average market value of the endowment.

Endowments are expected to contribute to, if not underwrite entirely, the total costs of the programs such funds support. Most of the amount utilized annually from endowment offsets direct program costs incurred. The balance (12 to 18 percent) of the amount utilized from endowment is reserved to defray associated program costs (such as space, support and oversight) which make up a significant portion of a program's total cost and represent the many dimensions of underlying support essential for any program to succeed. Since the total distribution from the endowment each year

is expected to be approximately 4 – 6 percent of average endowment market value, the amount allocated to associated program costs is expected to remain between 0.5 and 1.1 percent of average endowment market value.

CONCLUSION

Dartmouth's endowment, made up of over 5,000 individual funds, is testimony to the exceptional support the College has received over the years from donors committed to maintaining the enduring quality and value of a Dartmouth education. Continuing additions to the endowment from alumni and other friends of the College — combined with prudent oversight and investment of these funds by Dartmouth's Board of Trustees through the policies summarized in this pamphlet — help sustain an education of the highest quality for present and future generations of young women and men.