

Fiscal 2018 Endowment Report

Introduction

For the 2018 fiscal year, domestic equity markets had an outstanding year with the Russell 3000 Index returning 14.8 percent. International equities trailed the domestic equity markets with the MSCI All-country World ex U.S. Index returning 7.3 percent, and the MSCI Emerging Markets Index returning 8.2 percent. Colby's endowment returned 10.3 percent and finished the year with a market value of \$828 million (net of annuities).

Endowment Growth

During fiscal 2018, the endowment market value increased by \$53 million to \$828 million, a 7 percent increase. The total portfolio, including gift annuities, increased to \$844 million.

Figure 1 shows the endowment growth over the past 10 years. Since the beginning of fiscal 2009 the endowment has grown at a compound annual rate of increase of 3.3 which exceeds the annualized inflation rate for the past 10 years of 1.4 percent.

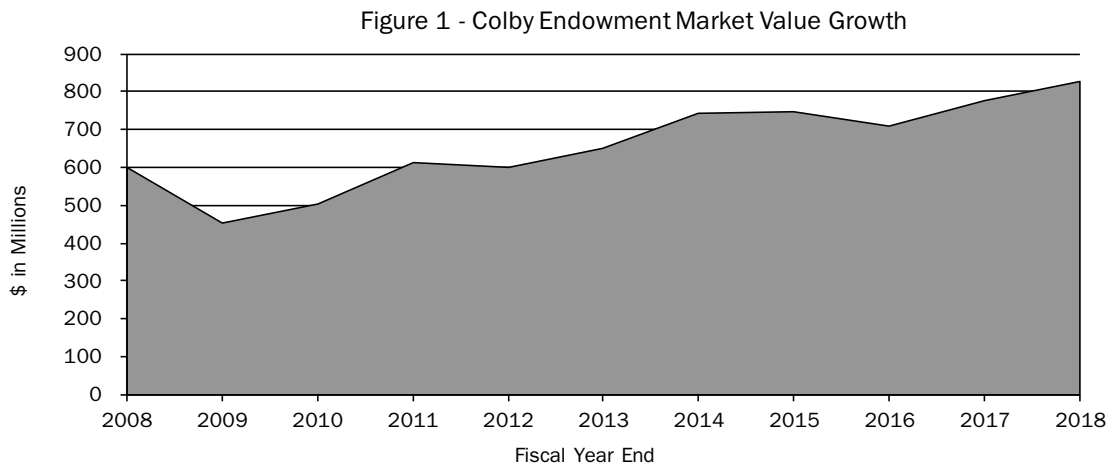


Figure 2 summarizes the sources of change in market value for the endowment for fiscal 2018 and for the last 10 years. Over the past 10 years, performance has more than offset spending and has contributed more than gifts and other additions to the increase in value. Nonetheless, new additions to the endowment from gifts and other additions continue to be an important source of endowment growth, as well as providing short-term liquidity to help fund spending.

Figure 2 - Colby Sources of Endowment Growth

	Fiscal 2018 (\$000)	Cumulative 10-Yr Totals (\$000)
Beginning Market Value	775,129	600,248
Gifts and Matured Annuities	16,883	119,756
Other Additions	3,831	25,492
Investment Performance Net of Fees	77,385	401,371
Spending	(44,065)	(301,402)
Other Deductions	(1,150)	(17,452)
Ending Market Value	<u>828,013</u>	<u>828,013</u>

Asset Allocation

Figure 3 shows a comparison of the asset allocation of the portfolio at the beginning and end of fiscal 2018.

Figure 3 - Colby Comparative Endowment Asset Allocation

	Actual June 30, 2017 <u>Allocation</u>	Actual June 30, 2018 <u>Allocation</u>	<u>Change</u>
Equities			
Marketable			
Domestic	13.9%	11.9%	(2.0%)
International Developed	9.4%	10.6%	1.2%
Emerging Markets	7.7%	8.1%	0.4%
Marketable Real Estate	0.0%	2.5%	2.5%
Marketable Natural Resources	3.0%	3.4%	0.4%
Total Marketable Equities	<u>34.0%</u>	<u>36.5%</u>	<u>2.5%</u>
Non-Marketable			
Venture Capital	13.4%	14.7%	1.3%
Private Equity	7.5%	7.3%	(0.2%)
Real Estate	3.3%	2.4%	(0.9%)
Natural Resources	2.4%	2.7%	0.3%
Total Non-Marketable Equities	<u>26.6%</u>	<u>27.1%</u>	<u>0.5%</u>
Total Equities	<u>60.6%</u>	<u>63.6%</u>	<u>3.0%</u>
Hedge Funds	27.5%	25.9%	(1.6%)
Cash and Bonds			
Cash and Receivables	8.0%	7.0%	(1.0%)
Intermediate Treasuries	3.9%	3.5%	(0.4%)
Intermediate TIPS	0.0%	0.0%	0.0%
Total Cash and Bonds	<u>11.9%</u>	<u>10.5%</u>	<u>(1.4%)</u>
Total Investments	<u>100.0%</u>	<u>100.0%</u>	<u>(0.0%)</u>

The investment office continues to monitor liquidity and new non-marketable commitments. As of June 30, 2018, the outstanding commitments to non-marketable partnerships stood at 8 percent of the portfolio.

As shown in Figure 4, the total of the illiquid non-marketable equity investments is lower than the total of their long-term targets. The investment office is aware of the near-term fluctuations in exposures and anticipates making annual adjustments to the short-term targets as the portfolio slowly moves toward its long-term targets.

Figure 4 - Asset Allocation Targets

	<u>Actual Allocation 6/30/2018</u>	<u>Short-term Target Allocation</u>	<u>Long-term Target Allocation</u>
Equities			
Marketable			
Domestic	11.9%	12.0%	
International Developed	10.6%	11.0%	
Emerging Markets	8.1%	8.0%	
Marketable Real Estate	2.5%	2.0%	
Marketable Real Assets	3.4%	3.0%	
Total Marketable Equities	<u>36.5%</u>	<u>36.0%</u>	<u>30-35%</u>
Non-Marketable			
Venture Capital	14.7%	14.0%	
Private Equity	7.3%	7.0%	
Real Estate	2.4%	4.0%	
Real Assets	2.7%	3.0%	
Total Non-Marketable Equities	<u>27.1%</u>	<u>28.0%</u>	<u>35.0%</u>
Total Equities	<u>63.6%</u>	<u>64.0%</u>	<u>65-70%</u>
Hedge Funds	25.9%	26.0%	20-25%
Cash and Bonds			
Cash and Receivables	7.0%	6.0%	
Intermediate Treasuries	3.5%	4.0%	
Intermediate TIPS			
Total Cash and Bonds	<u>10.5%</u>	<u>10.0%</u>	<u>10.0%</u>
Total Investments	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

Figure 5 shows the changes in June 30 asset allocation over the past 10 years.

Figure 5 - Ten-Year Comparative Asset Allocation

	Fiscal Year		
	2008	2013	2018
Equities			
Marketable			
Domestic	11.8%	8.8%	11.9%
International Developed	14.7%	7.4%	10.6%
Emerging Markets	5.2%	9.7%	8.1%
Marketable Real Estate	0.0%	0.0%	2.5%
Marketable Natural Resources	3.2%	2.4%	3.4%
Total Marketable Equities	<u>34.9%</u>	<u>28.3%</u>	<u>36.5%</u>
Non-Marketable			
Venture Capital	9.7%	10.3%	14.7%
Private Equity	11.2%	10.1%	7.3%
Real Estate	7.8%	8.4%	2.4%
Natural Resources	1.6%	2.6%	2.7%
Total Non-Marketable Equities	<u>30.3%</u>	<u>31.4%</u>	<u>27.1%</u>
Total Equities	<u>65.2%</u>	<u>59.7%</u>	<u>63.6%</u>
Hedge Funds	27.1%	28.0%	25.9%
Cash and Bonds			
Cash and Receivables	0.9%	8.4%	7.0%
Intermediate Treasuries	4.7%	3.9%	3.5%
Intermediate TIPS	2.1%		
Total Cash and Bonds	<u>7.7%</u>	<u>12.3%</u>	<u>10.5%</u>
Total Investments	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

At June 30, 2018 the portfolio contained commitments to 179 different investment vehicles, representing 90 investment products and 71 investment managers.

Annual Performance

The endowment outperformed at its preliminary composite benchmark by .2 percent for fiscal 2018. The following is a summary of major drivers of performance for fiscal 2018.

Passive Returns - the returns of the policy portfolio benchmarks:

- Marketable equities benchmarks combined to generate a return of 11.2 percent for the fiscal year.
- Non-Marketable equities benchmarks combined to generate a higher relative return of 15.6 percent when compared to marketable equities.
- Hedge Fund benchmarks combined to generate a return of 7.2 percent.

Active Returns - the returns of our portfolios against their portfolio benchmarks:

- The marketable equities portfolio trailed its policy benchmark by .1 percent for the fiscal year. For the one-year period only three of ten managers exceeded their policy benchmarks.
- The non-marketable equities portfolio outperformed its policy benchmark by 4.1 percent. All of the non-marketable sub-asset classes outperformed their benchmarks.
- The hedge fund portfolio generated a return of 4.6 percent which underperformed its policy benchmark by 2.6 percent. For the one-year period, six of ten managers underperformed their policy benchmarks which accounted for the underperformance. On a medium to long term, our hedge fund portfolio has met or added value above the policy benchmark.

Figure 6 shows the endowment performance for one, five and 10 year periods compared to the composite benchmark and a global 70/30 portfolio. Colby has outperformed the policy benchmark for the five and 10 year periods primarily through excellent manager selection. Colby's equity allocation features exposures that are more diverse in geography and industry than the global 70/30 portfolio.

Figure 6 - Endowment Performance

	<u>Colby</u>	<u>Colby Composite Benchmark</u>	<u>Global 70%/30% Portfolio*</u>
One-Year Return	10.3%	10.3%	8.1%
Five-Year Compound Annual Return	8.1%	7.3%	7.0%
Ten-Year Compound Annual Return	6.3%	4.5%	5.0%

* 70% MSCI ACWI Index and 30% Bloomberg Barclays Global Treasury Bond Index

Spending

The goal of a spending formula is to produce a stable flow of revenue for operations, while maintaining at a minimum the purchasing power of the principal of endowment. Colby's spending formula defines spending as a percentage of a five-year moving average of June 30 market values with adjustment for additions received in subsequent years. The use of a five-year moving average in the formula has produced a stable flow of revenue for operations.

As shown in Figure 7, endowment spending has grown at a compound annual rate of 7.5 percent over the past 10 years, assisted by an increase in the formula spending rate from 4.5 percent to 5.5 percent over the period. During this period, the spending rate was adjusted to provide additional support for financial aid, faculty growth, facilities and other key initiatives. The growth rate for spending has exceeded the rates for budgeted total operating revenue (4.6 percent) and student charges (3.8 percent). Over the past 10 years, the budgeted endowment income as a percentage of total budgeted operating revenue has increased from 15.7 percent to 21.4 percent.

Figure 7 - Comparative Compound Annual Growth Rates

	<u>Ten-Year CAGR</u>
Endowment Spending	7.5%
Budgeted Total Operating Revenue	4.6%
Student Charges	3.8%

The spending rate for fiscal 2018 was 5.5 percent of the adjusted five-year moving average market value of the endowment.

Organization

The Investment Office includes three authorized full-time positions. The non-investment manager operating costs assigned to the endowment (salaries, travel, office expenses, legal review of partnerships, consulting, custody, UBTI taxes on partnerships, and audit) amounted to approximately 16.4 basis points on average market value for fiscal year 2018.

Socially Responsible Investing

Beginning in October 2006, the Board of Trustees instituted investment policies related to direct investments in companies doing business in Sudan. The College maintains a no-purchase list that is provided to the College's managers.

As an expansion of its socially responsible investing policy, the College has begun providing a list of its direct-owned holdings (Appendix A).

Colby College
Endowment Annual Report
Direct Security Holdings as of June 30, 2018
Appendix A

Security Name	Market Value
ACTIVISION BLIZZARD INC	443,550
ADOBE SYSTEMS INC	1,166,832
ALEXION PHARMACEUTICALS INC	434,694
ALIBABA GROUP HOLDING SP ADR	1,807,869
ALIGN TECHNOLOGY INC	477,147
ALPHABET INC CL A	1,063,069
ALPHABET INC CL C	185,722
AMAZON.COM INC	2,026,276
BAIDU INC SPON ADR	965,297
BIOMARIN PHARMACEUTICAL INC	397,243
BOOKING HOLDINGS INC	946,577
COSTAR GROUP INC	555,263
EDWARDS LIFESCIENCES CORP	558,080
FACEBOOK INC A	1,270,331
ILLUMINA INC	697,439
INCYTE CORP	458,315
LOXO ONCOLOGY INC	274,465
MONSTER BEVERAGE CORP	740,870
NETFLIX INC	1,535,820
PALO ALTO NETWORKS INC	753,308
REGENERON PHARMACEUTICALS	516,540
SALESFORCE.COM INC	1,535,160
SCHWAB (CHARLES) CORP	704,970
SERVICENOW INC	1,406,325
SPLUNK INC	629,696
STARBUCKS CORP	370,496
VISA INC CLASS A SHARES	1,746,452
PPDAI GROUP	138,355
CLOUDERA INC	142,988
FORESCOUT TECHNOLOGIES INC	45,600
TREASURY SECURITIES	100,702,953
CASH AND CASH EQUIVALENTS	1,352,943
TOTAL DIRECT HOLDINGS	<u><u>126,050,644</u></u>