# Investment governance for the post-pandemic world

**ABOUT THE AUTHOR**

William F. Jarvis is a managing director and philanthropic executive at Bank of America Private Bank. Experienced with investment policy and governance for endowed nonprofit organizations, he is responsible for strategic thought leadership with institutional and private philanthropic clients.

Our investment portfolio is down — now what? Human experience, supported by behavioral finance research, teaches us that when investment portfolios have lost value because of market activity, the emotional side of investing can sometimes threaten to override the intellectual side. In times like the present, it's more important than ever to avoid making decisions driven by emotion that can, in the cold light of hindsight, seem ill-advised.

As your board or investment committee meets to consider possible responses to the market losses that you may have experienced, here for your meeting agenda are **five recommendations** that we hope will guide you to better decisions.

## 1 | Don't panic

The great majority of nonprofits are perpetual, long-term investors. This is a tremendous advantage when compared with individuals, who often let short-term market fluctuations and human emotions govern their investment decisions.

At your meeting, think in terms of decades, not days or weeks, and resist calls that urge "this time is different." Especially, don't bolt for the "safety" of cash. Going to cash in a market downturn has two disadvantages. First, it crystallizes your loss, and second — and more importantly — it requires that you have perfect foresight in determining when to get back into the market. Most organizations fail that second test, with the result that the crystallized loss can remain on their books long after a recovery has begun.

## 2 | Use your investment policy statement (IPS)

Your IPS exists for moments like this. If it was properly crafted, it represents the distillation of your team's best thought, arrived at in moments of calm. Its policies should be re-examined, but not discarded. If it truly reflects what you intended to do with the portfolio, now is the time to refresh your collective memories and recommit to the considered judgment that you used in creating it.

## 3 | Rebalance

Your IPS should contain a target — or policy — portfolio for your organization and ranges within which the various allocations are permitted to move. If market volatility has caused them to exceed these ranges, you should consider rebalancing the portfolio so it's again in compliance with the IPS. This may mean selling investments that have performed better, in relative terms, in order to purchase investments that have performed less well.

If that seems counterintuitive, think of your policy portfolio as your list of desired investments. Rebalancing presents an opportunity to purchase assets that you know you want for the portfolio at a discount. When items that they want go "on sale," most people aren't opposed to making the purchase.

## 4 | Check your liquidity

Your organization's operating or grantmaking budget may already be largely set. Where will the money come from? Your board or investment committee should meet with your organization's financial and (if appropriate) fundraising staff to determine where additional sources of liquidity might be found. For example, do you have an available line of credit that can give the organization access to funds for the near term? What are the prospects for fundraising, and how will this year's annual campaign moneys be used? Is it possible to "pull forward" a prospective gift from a potential donor? In a perfect world, these questions might already have been answered. But if not, now is a good time to reach out and start.

## 5 | Schedule an IPS review session for a future meeting

With everything else that's happening, now is not the time to try to revise your IPS. But it may be that the current market is exposing issues that merit attention and that may call for a revision to the existing document. Appoint a committee to review the IPS, in concert with your investment counselor and staff, and report back to the board at a meeting later in the year — perhaps at the midsummer session. Experience is a great teacher, and now is the time to distill and profit from its lessons.

---

## Conclusion

It's a commonplace saying that bad times can provoke bad decisions. Behavioral research tells us that humans tend to overweight recent experience — good or bad — in forming a view of what the future will hold.[1] Being able to identify and act against those innate instincts is a first step toward the more measured behavior of a prudent fiduciary. We offer these five recommendations in the hope that they'll enable you to navigate the current volatility with greater confidence and a clearer sense of how your organization could emerge stronger from this challenging time.

---

As nonprofit boards and investment committees attempt to navigate the current volatile environment, it's more important than ever to review where your organization and its investment portfolio are and where they may be headed. In this section, we propose **three actions** that nonprofit fiduciaries can take.

### 1. Know where you stand

Market downturns usually offer little advance notice of their coming.

Fortunately, for most institutional investors, it's possible to obtain an approximate view of the effect on their portfolios of positive and negative historical, or even hypothetical, market events. Today's quantitative models enable investment advisors and consultants to "stress test" portfolios and to show board and investment committee members what the results of a given event or combination of events might be.

The models on which these tests are based typically show the future in terms of probability, not certainty. They are nevertheless valuable guides to where risk lies and can help in assessing what steps to take in response to that knowledge.

There are three main ways in which nonprofit fiduciaries can make use of this information:

- Knowing the possible negative effects of market events on an institution's portfolio can significantly narrow the range of unfavorable consequences that weren't foreseen.
- Having an estimate of the consequences of certain negative events can assist in conversations with donors, who aren't infrequently acquainted with investment concepts and seek reassurance that their gift will be managed appropriately.
- Knowledge of the risks inherent in the portfolio can be very helpful in conversations with other stakeholders and the public should one of the events occur for which stress tests have been performed.

### 2. Know why you stand there

Nonprofit portfolios are all too often constructed with a view to those of other peer organizations or commonly used market benchmarks rather than with a view to the actual characteristics and needs of the specific nonprofit in question.

In an investment world that offers a very wide range of choices, it becomes imperative for the governors of an institution to be able to explain to donors, stakeholders, regulators, staff and the public why a particular set of investment strategies was viewed as optimal.

Assuming that a board or investment committee meets quarterly, a good practice is to devote at least some of each meeting to an assessment of the role played by a given allocation in the portfolio, and to the intended benefit to the portfolio of each asset class or strategy. As a result, fiduciaries should, over time, be able to internalize these lessons so that it becomes less and less likely that they'll have to answer "I don't know" to a question about the portfolio and its structure.

### 3. Know where you're going

The times we live in are characterized by the actions of complex and interconnected forces whose outcome is difficult to discern. The task of fiduciaries is to use the skills at their disposal — and those of their investment advisors — to arrive at a principled view of the shape of the political, economic and social factors that are determining what's possible for them as investors for their institution.[2]

The views in this paper should go beyond the usual market reports that focus on what may happen over the next three to six months. Augmenting that relatively short-term perspective, knowledge of the investment regime that's likely to prevail over the next 18 to 24 months (or, if appropriate, even longer)[3] can act as a powerful clarifier of discussions in meetings, helping board and investment committee members to focus on issues and forces that are material rather than those that are transient or simply topical. It can also reinforce the other two actions, giving them a strategic character that can lead to stronger governance for the investment function as a whole through a more conscious assimilation and use of the knowledge that becomes available.

**privatebank.bankofamerica.com/Nonprofits**

[1] For the classic formulation of behavioral science, see Daniel Kahneman, *Thinking, Fast and Slow*, New York: Farrar, Straus and Giroux, 2011. (Latest data available.)

[2] William F. Jarvis, *Financial regimes and nonprofit governance: Steering through the challenges*, Bank of America Corporation, December 2022.

[3] William F. Jarvis, *What to expect: The endowment model in our time*, Bank of America Corporation, December 2022.