

Aalto University Foundation Endowment Spending Policy

Effective Date of Policy: January 1st, 2022

Introduction

The **Aalto University endowment** consist of assets of different types of equity funds, formed from the capital received from the founders of the foundation, donors and government. In addition, the Board of the foundation may form funds from the accumulated profit.

The **endowment spending policy** sets principles for defining the level of spending from the endowment towards the university operations. The predefined spending policy provides a clear and transparent way to estimate future endowment spending that will support the annual operative planning of the University, donor communications and sets a clear target for the endowment strategy, including a strategic risk/return profile of the investment portfolio.

The assets of the equity funds are pooled to one endowment portfolio for investment management purposes, each having their distinct pre-defined spending rules. Currently, these funds are of four different types:

- **General Endowment Fund**, consisting of capitalizing donations received towards the overall long-term development of the University, including the matching capital from the Finnish government. The investment horizon of the fund is perpetual.
- **Restricted Donation Funds (capitalizing)**, consisting of donations received towards the long-term development of activities in single study field / school / department or unit (i.e. earmarking or limitations on the use given by the donor). The investment horizon of the funds is perpetual.
- **Restricted Donation Funds (hybrid)**, consisting of donations received towards the development of activities for a pre-defined duration in single study field / school / other university unit (i.e. earmarking or limitations on the use given by the donor). The investment horizon of the funds is typically 5-20 years and fund capital is used during this period.
- **Unrestricted Funds (hybrid)**, consisting of capital transferred by Board decision from accumulated operative profit to form a hybrid fund. The investment horizon of the funds is typically 5-20 years and fund capital is used during this period.

Updates for the endowment spending policy are approved by the University Board, and the implementation of the spending is managed by the University CFO.

Spending from the general endowment fund

The spending rule for the general endowment fund has two potentially conflicting **goals**: i) to preserve and accumulate the real value of the endowment in the long run and ii) maximize stability of the endowment spending in the medium term to limit disruptions of university operations.

The real value preservation is essential to ensure that the same amount of activities can be supported by the endowment returns over time. Preserving the real value of the endowment requires accumulating the endowment with investment return at a minimum with the rate of university inflation, which comprises of 64% of Finland's wage and salary earnings index, 21% of Finland's consumer price index and 15% of Finland's producer price index.

Aalto University **general spending rule** consists of two components:

1. Maximum spending rate (2.5 %) times general endowment market value (30% weight)
2. Previous year maximum spending + university inflation (70% weight)

The maximum spending rate is set at 2.5%. Since the real return target is 3.0%, the policy targets a long-term capital real value accumulation of 0.5% per annum. The long-term real value appreciation target improves the probability of real value preservation.

Maximum amount of general spending is approved for **two years in advance** and is guaranteed by endowment liquidity buffers. In addition, spending estimate for years 3 and 4 are set as year 2 spending $\pm 10\%$.

In a **funding risk scenario** where university funding drops significantly e.g. due to political risk materializing, endowment spending may be increased by up to 20% over two years. This provides the university time to adjust its operations to lower funding level. This additional spending is only available outside endowment crisis scenario and is subject to endowment accumulated real return staying positive.

In an **endowment crisis scenario**, where the endowment market value drops at minimum 15% below previous peak, spending for years 1 and 2 will remain fixed, guaranteed by liquidity buffers. Spending for years 3 and 4 will be reset with general spending rule, based on the lower endowment market value. In this scenario, Aalto University may utilize short to medium term debt to provide university time to adjust its operations to lower funding level.

Spending from the other funds

Aalto University spending rules for other funds are defined as follows:

- **Restricted Donation Funds (capitalizing)** spending by fixed real return rule: fixed return of 5%, where the capital is protected against inflation with adjustment of 2.5% and 2.5% of the fund value is available for use
- **Restricted Donation Funds (hybrid)** spending by fixed nominal return rule: use of fixed nominal return of 5% of the capital as well as the capital itself during the pre-defined duration
- **Unrestricted Funds (hybrid)** spending by fixed nominal return rule: use of fixed nominal return of 5% of the capital as well as the capital itself during the pre-defined duration.