1. OVERVIEW

Philanthropic giving is essential to the fulfilment of the University of Melbourne’s purpose as articulated in *Advancing Melbourne*, “to benefit society through the transformative impact of education and research.”

Generous gifts have been used to establish scholarships and bursaries, allowing the University’s talented students to achieve their potential, regardless of personal circumstances or background; philanthropic giving also enables the University to attract academics who inspire as teachers and, as researchers, make ground-breaking discoveries addressing some of the greatest problems facing society today. Many of these gifts are placed under the long-term stewardship of the University, with annual distributions supporting the benefiting activities.

This report provides donors with an overview of the University’s investment management and the historical investment performance of those long-term gifts through to the end of the 2020 calendar year.

Further information about the uses of these long-term gifts can be found in Section 2.

Information about the University’s investment management and governance of long-term investments including philanthropic gifts can be found in Section 3.

An overview of the investment strategy for the portfolio comprising philanthropic gifts to the University is provided in Section 4.

The portfolio comprising long-term gifts to the University achieved an overall investment return of 5.3 per cent in 2020 as illustrated in Table 1 below. Information about the 2020 and historical investment performance can be found in Section 5.

Distributions from the portfolio of long-term gifts totalled c.$44.8 million in 2020, representing an enormous contribution to specific support and activities across the University; the methodology used to calculate the distribution each year is described in Section 6.

2. USES OF LONG-TERM GIFTS

Over the last ten years, the generosity of donors has resulted in more than 340 new funds being established at the University for long-term investment. These also include those established as charitable trusts, and together they extend the legacy established by those far-sighted donors who first supported the University.

The majority of the gifts managed by the University are applied for a specific purpose that honours a donor’s expressed wishes or in accordance with the trust terms at the time of making the gift. Student awards account for the greatest number and encompass scholarships, student grants, and prizes. Other gifts support academic positions, comprising chairs, fellowships, lectureships, and research assistants. Gifts towards libraries and student enrichment include gifts that support study spaces and resources as well as sport and other extracurricular activities at the University.

<table>
<thead>
<tr>
<th>TABLE 1: SUMMARY OF HISTORICAL ANNUAL INVESTMENT RETURNS &amp; DISTRIBUTIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Year End Market Value ($m)</strong></td>
</tr>
<tr>
<td>-------------------------------</td>
</tr>
<tr>
<td><strong>Return (%)</strong></td>
</tr>
<tr>
<td><strong>Trusts Distributions ($m)</strong></td>
</tr>
</tbody>
</table>
3. INVESTMENT GOVERNANCE & MANAGEMENT MODEL

GOVERNANCE

The University’s long-term investments, including long-term philanthropic gifts, are managed under the oversight of its Investment Management Committee, a sub-committee of University Council’s Finance Committee.

The Investment Management Committee is comprised of investment professionals; membership of the Committee as at the end of 2020 is listed in Table 2 above.

The Investment Management Committee meets on a quarterly basis and oversees investment strategy and performance; it also provides advice to Finance Committee and Council on investment beliefs and policy and on the appointment of fund managers.

INVESTMENT MANAGEMENT MODEL

The University does not manage its long-term investments directly, a policy that reflects both the fact that investment management is not a core function of the University and the relatively modest scale of the University’s overall long-term portfolio. Day-to-day management is therefore undertaken by two fund managers, allowing the University to benefit from the greater scale of their funds under management whilst still maintaining responsibility for investment strategy and philosophy.

Since 2002, the majority of the University’s long-term investments have been managed by the Victorian Funds Management Corporation (VFMC), an authority established in 1994 through an Act of the Victorian Parliament. VFMC is an institutional investor, responsible for investing over $64 billion of funds for 29 public authorities of the State of Victoria and related organisations, including the National Gallery of Victoria, State Library Victoria and WorkSafe Victoria.

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Table 2: Investment Management Committee Membership

<table>
<thead>
<tr>
<th>Member</th>
<th>Professional Affiliation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mr Andrew Sisson AO (Chair) 1</td>
<td>Founder, Balanced Equity Management</td>
</tr>
<tr>
<td>Ms Liliana Colla</td>
<td>Implementation Specialist, Equipsuper</td>
</tr>
<tr>
<td>Ms Amanda Fong</td>
<td>Investment Advisor/Partner, Escala Partners Ltd</td>
</tr>
<tr>
<td>Professor Paul Kofman</td>
<td>Dean, Faculty of Business and Economics, University of Melbourne</td>
</tr>
<tr>
<td>Mr Mark Leibler AC 1</td>
<td>Senior Partner, Arnold Bloch Leibler</td>
</tr>
<tr>
<td>Mr Peter Scott</td>
<td>Deputy Chairman, Gresham Partners Limited</td>
</tr>
<tr>
<td>Mr Allan Tait</td>
<td>Vice-President (Administration &amp; Finance) and Chief Operating Officer, University of Melbourne</td>
</tr>
</tbody>
</table>

1 Member, University Council
VFMC is also a leader in addressing issues relating to climate change risk in investments – an important tenet of the University’s investment philosophy.

In 2016, following a strategic decision by VFMC to exit private equity as an asset class, the University appointed ROC Partners as a separate manager for those investments to maintain that element of its strategy.

Both fund managers invest funds directly and with a range of commercial fund managers. Leading global advisory asset consultant Willis Towers Watson provides the University independent advice on investment strategy.

**FUND STRUCTURE**

The University’s long-term investments are structured as two separate portfolios: long-term gifts (including those held on trust) are thereby invested separately from the University’s other long-term assets, which comprise unutilised borrowings, income received in advance, unrestricted free reserves, and other assets.

This structure allows for the development of a distinct strategy for each portfolio reflecting its liquidity profile and therefore return expectations. The long time horizon of the portfolio comprising long-term gifts allows for investment in less liquid assets which have higher investment returns. At the same time, assets within the portfolios benefit from economies of scale in management fees and access to investment opportunities.

The portfolios operate as separate unitised fund structures. Once received, gifts intended to be invested long-term are valued and exchanged for units that represent a portion of the total portfolio.

The value of the units varies over time in accordance with the performance of the underlying investments. Units are re-valued to the market value of the underlying fund investments each month-end.

**4. INVESTMENT OBJECTIVES & STRATEGY**

The portfolio comprising long-term gifts to the University provides consistent support for the scholarship, academic, and research activities of the University. To achieve this broad objective, the portfolio is structured to achieve long-term capital growth; provide sufficient liquidity to meet the annual payments to beneficiaries of the various underlying funds; and maintain the real value of the assets into the future.

**INVESTMENT STRATEGY (ASSET ALLOCATION)**

The definition and allocation of asset classes comprises one of the central activities in strategy development and is subject to review on an annual basis by University management, Investment Management Committee, fund managers, and advisors. Adjustments to weightings and material departures from asset allocation targets or ranges are part of monthly reporting received by the University.

The portfolio comprising long-term philanthropic gifts was valued at $1,134.3 million as of end December 2020 and consisted of 12 asset classes (see Figure 1).

**INVESTMENT RISK MANAGEMENT**

As part of their investment processes, the University’s fund managers identify material risks and provide for the mitigation of these risks in investment decision-making.

One of the less well understood risks confronting all investors is presented by the accelerated change in climate conditions produced by industrial, agricultural, and other gaseous emissions; the difficulties associated with anticipating the rate and degree of change, economic impacts, and policy responses continue to create a high degree of uncertainty for investors.
The University’s awareness of and concern about the increased risk created by climate change informed a commitment in its 2017-2020 Sustainability Plan to develop a specific framework for assessing that risk and whether its fund managers were adequately factoring it into their decision-making.

The resulting Sustainable Investment Framework can be found via this link.

The University’s primary fund manager VFMC has been proactive in its approach to understanding climate change risk and has made steady progress over recent years in its investment stewardship, which takes these risks and others into consideration.

The University receives an independent assessment each year of the consistency of VFMC’s investment decision-making with the University’s Sustainable Investment Framework (SIF), and in each year since it was published in 2017, VFMC’s investments on the University’s behalf have been judged to be consistent with the SIF.
5. Investment Performance

The portfolio comprising long-term philanthropic gifts has overall performed well for many years despite periodic volatile global financial conditions. Table 3 shows the portfolio outperforming the target return over the long-term.

The COVID-19 pandemic in 2020 triggered the deepest recession since World War II. Despite this, the US equity market quickly recovered the initial 35 per cent drawdown and finished the year at record highs. The apparent disconnect between markets and fundamentals is largely explained by the unprecedented monetary and fiscal stimulus imparted by global central banks and governments. In addition, financial markets also had to absorb a turbulent US election, Brexit and quickening climate events. Efforts to contain the virus as well as late-year progress on vaccines also supported markets.

The portfolio’s positive return was driven by the strong returns in Private Equity and supported by positive returns on International Equities, Private Credit and Bonds. This helped the portfolio to exceed its target return objective of CPI + 4 per cent in 2020, despite initial losses on equities and the sell-off in infrastructure and property assets. The 2020 performance by asset class is shown in Table 4.

The University has increased the long-term target return to CPI + 4.5 per cent for 2021 onwards due to the opportunities provided by the pandemic to increase positions in higher returning asset classes.

### Table 3: Performance Over Time (At End December 2020)

<table>
<thead>
<tr>
<th>% Return per annum</th>
<th>1 Year</th>
<th>3 Year</th>
<th>5 Year</th>
<th>10 Year</th>
<th>Since Inception</th>
</tr>
</thead>
<tbody>
<tr>
<td>Portfolio Performance</td>
<td>5.3</td>
<td>6.1</td>
<td>7.1</td>
<td>11.7</td>
<td>7.9</td>
</tr>
<tr>
<td>Target Return (CPI +4%)</td>
<td>4.9</td>
<td>5.5</td>
<td>5.6</td>
<td>5.9</td>
<td>6.2</td>
</tr>
</tbody>
</table>

### Table 4: 2020 Performance by Asset Class

<table>
<thead>
<tr>
<th>Asset Class</th>
<th>Return %</th>
<th>Asset Class</th>
<th>Return %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australian Equities</td>
<td>1.7</td>
<td>Private Credit</td>
<td>7.3</td>
</tr>
<tr>
<td>International Equities</td>
<td>8.6</td>
<td>Australian Bonds</td>
<td>5.3</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>-1.7</td>
<td>Cash</td>
<td>1.0</td>
</tr>
<tr>
<td>Property</td>
<td>-1.0</td>
<td>Insurance</td>
<td>0.4</td>
</tr>
<tr>
<td>Hedge Funds</td>
<td>1.7</td>
<td>Private Equity</td>
<td>35.1</td>
</tr>
</tbody>
</table>

**Total Gift Funds Return 5.3%**
### TABLE 5: MARKET VALUE AND DISTRIBUTIONS 2018-2020 ($ IN MILLIONS)

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Year-End Market Value (M.V.)</td>
<td>909.3</td>
<td>1,024.8</td>
<td>1,134.3</td>
</tr>
<tr>
<td>Year-End Market Value (as @ Budgeting) $</td>
<td>779.2</td>
<td>900.3</td>
<td>955.4</td>
</tr>
<tr>
<td>80% of Actual Prior Year Distribution (+CPI) $</td>
<td>26.3</td>
<td>29.3</td>
<td>33.6</td>
</tr>
<tr>
<td>20% of 5% Target Rate * Year-end Market Value (as @ Budgeting) $</td>
<td>7.8</td>
<td>9.0</td>
<td>9.6</td>
</tr>
<tr>
<td>Constrained Distribution (4.5 - 5.5% of Year-end M.V. (as @ Budgeting)) $</td>
<td>35.1</td>
<td>40.5</td>
<td>43.2</td>
</tr>
<tr>
<td>Actual Distributions</td>
<td>35.7</td>
<td>41.0</td>
<td>44.8</td>
</tr>
</tbody>
</table>

## 6. DISTRIBUTIONS

Distributions for use each year from the portfolio of long-term philanthropic gifts are based on a notional rate of 5 per cent of total assets in the portfolio. To determine the exact distribution amount, the University uses a formula that adjusts for fluctuations in annual investment performance gradually. This “smoothing” formula ensures the predictability of the distribution amount without risking impairment of the portfolio corpus by, for example requiring a fixed distribution in a year of poor performance.

Calculated distributions are thus equal to the sum of (i) 80 per cent of the previous year’s distribution amount, and (ii) 20 per cent of the target distribution rate of 5 per cent of the market value of the long-term gift portfolio. To ensure that actual distributions are closely aligned to the target rate, a constraint is applied, ensuring that actual distributions cannot be lower than 4.5 per cent or higher than 5.5 per cent of the market value of the portfolio.

This calculation occurs as part of the University’s annual budgeting cycle in October each year. This means that the distribution estimate is based on the balance at the end of the year, two years prior to the distribution year.

For example, the October 2019 budget for the 2020 year was based on the market value of the portfolio as of the end of 2018. To adjust for this timing difference, the market value of the portfolio is adjusted for inflation (two years of inflation, to bring the 2018 market value into 2020 dollars for distribution). Similarly, the 4.5 - 5.5 per cent range is applied to the (inflation-adjusted) year-end market value from two years prior to the distribution year.

The actual market value and distribution figures over the past three years for the long-term gift portfolio are shown in Table 5 above. Calculation of the distribution can be illustrated using the figures in green for the 2020 distribution (calculated in October 2019):

- 80 per cent of the actual prior year (2019) distribution of $41.0m, subject to one year of inflation, equalling $33.6m; plus

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3 E.g. the “Year-End Market Value (as @ Budgeting)” in 2020 is as of 31/12/18, as the budget is created in 2019, adjusted for CPI.
• 20 per cent of the target distribution, based on the target distribution rate of 5 per cent and the most recent year-end market value (2018 year-end, being $909.3m in 2018 dollars and $955.4m in 2020 dollars, i.e. adjusted for two years of inflation) equalling $9.6m;

• This provides the constrained distribution value of $43.2m ($33.6m plus $9.6m).

The actual distribution amount in 2020 ($44.8m) slightly exceeded $43.2m due to distributions on donations received and contributed during the year.

7. ADMINISTRATION

The Vice-President (Administration & Finance) and Chief Operating Officer has management responsibility for the University’s investments, supported by the Chief Financial Officer Group. In addition, a team of Advancement, Legal, Finance Operations and Compliance staff manage the expenditure of long-term gift distributions according to the donor’s expressed wish or trust terms.

The University’s Gift Committee, a sub-committee of Council, is charged with representing donors’ interests and assists University Council in overseeing and administering philanthropic gifts from donors and partners to any part of the University. The Gift Committee ensures the appropriate and effective acceptance and use of gifts to the University. The Committee also oversees the University’s stewardship of all gifts to the University including those that are held by the University on trust.

MORE INFORMATION

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FEES

The University calculates an internal administration fee of 2.5 per cent based on distributions; this equates to roughly 0.1 per cent of the market value of the gifts invested long-term. This is below the administrative fees charged by other charitable trustees.

MAKE A DIFFERENCE

From its foundation in 1853, the University of Melbourne has been the fortunate beneficiary of generous philanthropic support from alumni, staff, students, parents and friends. The University welcomes the opportunity to discuss individual giving interests.

Gifts are accepted and administered in accordance with the University’s Gift Policy, including adhering to the commitments set out in the Donor Charter and valuing the ongoing involvement of, and relationships with, donors guided by the University’s Donations Framework.

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