ASSET ALLOCATION

The asset allocation at 31 December 2008 compared to the average exposure in the SuperRatings Funds Survey is provided in the following chart. At year end the University held a higher exposure to fixed interest, cash and alternative investments and a lower exposure to overseas equities than the market.

MARKETS & STRATEGY IN 2008

World economic growth slowed dramatically in the later half of 2008 as the global financial crisis impacted real economic activity. World trade and industrial production contracted sharply leading to weaker employment markets, falling commodity prices, reduced consumption and declining investment.

Equity market investors around the world experienced the poorest investment returns since the Great Depression. Stock market indexes fell sharply in all developed and developing countries. Property investors, particularly those exposed through listed vehicles, also fared poorly.

Government bond investors benefited from falling bond yields and a flight to quality. This was reinforced by falling inflation expectations and aggressive monetary easing by central banks. Corporate bond investors did not benefit to the same extent; many lost capital as credit spreads widened and demand for these securities diminished.

Beginning in early 2008 the University actively moved to reduce risk in its investment portfolios. ANU reduced exposure to risk assets through the year with net sales of $88.6 million of domestic equities and $100.1 million of overseas equities. This action combined with falling markets reduced the allocations to these sectors from 40 per cent and 20 per cent at the beginning of the year to 30 per cent and 11 per cent by 31 December 2008. Further sales of overseas equities occurred in early 2009.

A full review of the asset allocation strategy commenced in 2008 and completed in 2009 will see the University maintaining a more defensive strategy going forward with minimal reduction to expected investment returns but with lower risk of capital losses.

Looking forward it is anticipated that investment markets will remain difficult for at least the next few years. The world has entered uncharted waters in terms of the level of fiscal and monetary stimulus that is being applied by governments and central banks in an effort to mitigate the economic fallout from the global financial crisis. Unemployment will continue to rise well into 2009 and possibly into 2010. Investment returns will likely be subdued as excess capacity is reabsorbed into the production process. Savings ratios will rise in the developed world placing more downward pressure on consumption previously funded by increasing levels of household debt. Corporate earnings and margins will remain under pressure in this environment.

Australia should endure and recover from the current world economic slump better than most developed countries due to its advantages of geographic proximity to China and India, its export mix and its relatively strong fiscal position prior to the crisis.

The LTIP has been able to recover some of its asset write downs in early 2009 through maturing securities and as a result of more stable financial markets. However risks of further valuation pressures remain in some areas of the portfolio such as in the property related exposures. Overall the LTIP is well positioned in the current difficult market environment created by the uncertainty attached to the unprecedented dislocations of markets that have unfolded since late 2007. The massive response from policy makers, while beneficial in calming worries of systemic disasters in the short-term, is adding to the uncertainties of how the stimulus policies will eventually be safely unwound.

The Investment Office, with the support of the IAC, intends to maintain a cautious approach to asset allocation with an emphasis on managing a well diversified portfolio of assets. The LTIP is designed to provide secure revenue flows and capital protection. At the same time adequate exposure to growth assets is included to provide capital appreciation over the long-term.
INTRODUCTION

The strategic goal of The Australian National University (ANU) is to advance knowledge through excellence in research, education and community engagement. The philosophy embodied in this goal is reflected in the internal management of the University’s financial assets. The assets are managed by the ANU Investment Office under advice from the Investment Advisory Committee (IAC), which includes in its membership senior industry professionals and academic experts with relevant commercial experience. The IAC reports to Finance Committee and ultimately to University Council.

INVESTMENT OBJECTIVE

The University Investment Objective is to obtain the maximum possible long term return on the available capital consistent with achieving a minimum return to the University of Consumer Price Index plus 4.0 per cent over rolling five year periods and ensuring a negative annual real return occurs less frequently than once every six years on average. Over the shorter term, it is recognised that there will be periods when investment returns do not meet this objective. Accordingly the University also aims to achieve returns (after fees and tax) that are in excess of the median return of other funds with comparable risk and return profiles as measured by independent industry surveys over three year periods. The portfolio will contain sufficient liquid assets to pay the financial obligations of the Commonwealth Superannuation Scheme, as they fall due.

FUNDS UNDER MANAGEMENT

The University’s realisable investment assets at 31 December 2008 were $1,037.9 million. Of this total $681.6 million was invested through a balanced fund known as the LTIP with exposure to all the major asset classes including domestic and overseas equities, listed property, fixed interest, alternative investments and cash. The remainder of the funds under management comprised general University funds held mainly in cash and liquid securities $220.6 million, Commonwealth Capital Grant $88.1 million, Better Universities Renewal Fund Grant $23.6 million and $24.0 million residual amount from a 2004 public market capital raising. The LTIP is administered in the same manner as a commercial unit trust with unit holders buying and selling units in the Pool at market value. Distributions to unit holders on a quarterly basis. The distribution rate for 2008 was six per cent. The difference between the distribution rate and the actual returns generated by the LTIP is captured in the market price of units in the LTIP.

MANAGEMENT OF FUNDS

The University maintains a professionally staffed Investment Office. This Office is responsible for the day-to-day management of the funds and for preparing the investment strategy recommendations and investment policy papers for consideration by the IAC.

The IAC was established in 1968 to review the management and financial performance of the University’s investment operations and to advise Finance Committee accordingly. In addition, IAC provides advice on matters of investment policy with regard to the investment funds. The IAC conducted four meetings during 2008.

Membership of the IAC comprises the Vice-Chancellor, the Chair of the Finance Committee, the Chief Finance Officer and six persons with expertise in finance and investments. The six specialists in 2008 were Emeritus Professor Allan Barton, Mr Tim Commelin (Chair, Executive Chairman Stockbroking ABN Amro Morgans), Professor Tim Braithwaite (Executive Dean Faculty of Business, Economics and Law University of Queensland), Mr Jim Service (Managing Director J.G. Service Pty Ltd), Mr Robert Ferguson (Executive Chairman IMF (Australia) Ltd) and Mr Ottmar Weiss.

INVESTMENT PERFORMANCE FOR 2008

- **2008 Return**: The investment return in 2008 was -24.6 per cent after the management expense ratio (MER) of 0.17 per cent. The benchmark return, the median return of the SuperRatings Pension Fund Crediting Rate Survey (Balanced Option), was -23.1 per cent. This ranked the University in 55th place in the SuperRatings Survey of 88 funds over one year. 2008 was only the third year in the past 10 years that the LTIP has not outperformed its benchmark.

- **Strong Long-term Performance**: SuperRatings data indicates strong longer-term performance by the ANU LTIP. Over 10 years the LTIP has provided a 7.3 per cent return net of all costs compared to the benchmark return of 4.8 per cent. In the SuperRatings Pension Crediting Rate Survey ANU has ranked third of 61 funds over five years and second of 19 funds over seven years.