EXPLANATORY STATEMENT – EDUCATION INVESTMENT FUND INVESTMENT MANDATE

Objective of the directions

As stated in the *Nation-building Funds Act 2008* (the Act), the Australian Government (the Government) has established the Education Investment Fund (EIF) to enhance the Commonwealth's ability to make payments in relation to the creation or development of higher education infrastructure, research infrastructure, vocational education and training infrastructure, eligible education infrastructure and to make transitional Higher Education Endowment Fund payments.

The EIF will be managed by the Future Fund Board of Guardians (the Board). $6.48 billion was transferred into the EIF on 2 January 2009. Decisions on further crediting will be determined by the Government in accordance with its obligations under the Act.

Directions issued under subsection 154(1) of the Act are known collectively as the investment mandate.

In setting an investment mandate, the responsible Ministers (the Treasurer and the Minister for Finance and Deregulation) must have regard to maximising the return on the EIF consistent with international best practice for institutional investment, enhancing the Commonwealth's ability to make payments, and any other matters the responsible Ministers consider to be relevant.

The investment mandate is expected to be reviewed before 1 July 2010. This reflects the Government's intention to assess whether there are marked changes in the investment environment over the next twelve to fifteen months that should be reflected in the investment mandate.

Directions

Benchmark return

For the purpose of this investment mandate, the Government has directed the Board to adopt, as the benchmark for the performance of the EIF, the Australian three month bank bill swap rate plus 0.3 per cent per annum, calculated on a rolling twelve month net-of-fee basis.

The Government has indicated its intention for funding for approved infrastructure projects to be made available to support the Government's broader economic strategy. The benchmark return has regard to this and to volatility in the financial and credit markets. These considerations are also reflected in the requirement that, in targeting the benchmark, the Board is directed to invest in such a way as to minimise the probability of capital losses over a twelve month investment horizon.

Under section 81 of the *Future Fund Act 2006*, the Chair of the Board must, as soon as practicable after the end of each financial year, prepare and give to the nominated Minister a report of the Board and Agency's operations. This includes the requirement that the report must include a report of the performance of the investments of the EIF.

Board must consider impacts from its investment strategy

The Government has an obligation to the Australian community to make decisions that are economically and fiscally responsible. It is the expectation of the Government that in managing the investments of the EIF, the Board should minimise disruption to the operation of domestic financial and credit markets and act in a manner that minimises the potential to effect any abnormal change in the volatility or efficient operation of Australian financial markets.

The Board is also required to act in a manner that is unlikely to cause any diminution of the Australian Government's reputation in Australian and international financial markets.

The Government participates in a number of international organisations which pursue high standards of conduct in financial markets. The Government recognises that the Board will potentially invest in international capital markets as part of the fulfilment of their requirements under the Act. In doing so, the Government expects that the Board will act in a manner that is unlikely to cause embarrassment for the Government.