

Flinders Council Policy Manual

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SUBJECT: <i>INVESTMENT POLICY</i>	FILE NO:	FIN/0501
ADOPTED BY COUNCIL ON: 21 May 2009	MINUTE NO:	170.05.09
AMENDED BY COUNCIL ON: 18 December 2014	MINUTE NO:	952.12.2014

1. Background

Council generally has funds in excess of those needed to meet its immediate day-to-day activities. Those funds are then available for investment until required, with the resultant investment income forming part of Council's budgeted revenue.

When exercising this policy, consideration is to be given to the preservation of capital, liquidity, and the return on the investment.

Preservation of capital and the return on investment in accordance with the parameters contained in Appendix 12, are the principal objectives of the investment portfolio ~~whilst optimising return~~. Investments are to be placed in a manner that ~~seeks to ensure security and safeguarding the investment portfolio. This includes managing credit and interest rate risk within identified thresholds is in accordance with these stated parameters~~ and parameters.

Investments should be allocated to ensure there is sufficient liquidity to meet all reasonably anticipated cash flow requirements, as and when they fall due, without incurring the risk of significant costs due to the unanticipated realisation of an investment.

Investments are expected to achieve a market average rate of return in line with the Council's risk tolerance as set out in ~~the risk assessment framework in Appendix 1 of~~ this policy.

2. Policy Objective

In accordance with legislative and common law responsibilities the objective of this Policy is to authorise and regulate the investment of Council's surplus uncommitted funds so as to maximise earnings from authorised investments whilst ensuring the security of those funds.

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3. Policy Guidelines

Funds for Investment

Any ~~uncommitted surplus~~ Council's funds are to be invested in terms of this Policy document.

Authority for Investment

Investments of Council's funds are to be in accordance with Council's power of investment under:

- *Local Government Act 1993*- Section 75.
- *The Trustee Amendment (Investment Powers) Act 1997*

Prudent Persons Standard

The investment portfolio will be managed with the care, diligence and skill that a prudent person would exercise. As trustees of public monies, officers are to manage the Council's investment portfolio to safeguard the portfolio in accordance with the spirit of this policy, and not for speculative purposes.

Ethics & Conflicts Of Interest

Officers of the Council ~~and~~, Councillors ~~and members of the Audit and Finance Special Committee~~ will not engage in personal activities that may conflict with the proper execution and management of the Council's investment portfolio. All officers ~~and Councillors~~ must disclose any actual or potential conflict of interest to the General Manager who shall disclose the interest in accordance with prescribed practice. In the case of the General Manager such a disclosure is to be made to the Mayor.

Any person from whom advice is sought in relation to investments must also declare, in writing, that they have no actual or potential conflict of interest.

4. Approved Investments

Investments made under delegation are limited to the following:-

- A. Commonwealth/State/Territory Government security (eg bonds);
- B. Interest Bearing Deposits issued by an authorised deposit taking institution (ADI);

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C. Bills of Exchange guaranteed by an authorised deposit taking institution; and

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D. Deposits with Tasmanian Public Finance Corporation.

~~E. Managed Funds with a minimum long term Standard and Poor (S&P) rating of "A" and short term rating of "A2". Recommended by Council's selected Investment Advisor - refer Clause 6.2~~

Comment [SP1]: Diversification & Risk/Return

~~E. Infrastructure for the benefit of the community.~~

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5. Prohibited Investments

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The following investments are prohibited under this policy:-

A. Derivative based financial instruments;

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B. Principal only investments or securities that provide potentially nil or negative cash flow;

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C. Investments that have underlying futures, options, forward contracts and swaps of any kind;

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D. Any type of collateralised debt obligation investment; and

E. Any financial investment that requires the Council to borrow (leverage) in order to make that investment.

6. Investment Guidelines

In order to meet the policy objectives the Council must take into consideration all of the following factors when carrying out investment functions:-

~~a) Existence of Guarantee and Security, including the Financial Claims Scheme~~

~~b)a) Risk Assessment Framework (including credit and maturity frameworks), as detailed below. The investment strategy detailed in Appendix 1.~~

~~e)b) Interest Rate; and~~

~~c) Access to, and customer service history of, the institution; and-~~

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- d) Available history of Managed Funds recommended by the Investment Advisor.

6.1 Risk Assessment Framework

Investments are expected to achieve a market average rate of return taking into consideration the following risk assessment framework.

- a) Preservation of Capital - the requirement for preventing losses in an investment portfolio's total value.
- b) Diversification - the requirement to place investments in a broad range of products so as not to be over exposed to a particular sector of the investment market, as detailed in Appendix 1.
- c) Market Risk - the risk that the fair value or future cash flows of an investment will fluctuate due to changes in market prices.
- d) Liquidity Risk - the risk an investor is unable to redeem the investment at a fair price within a timely period.
- e) Maturity Risk - the risk relating to the length of term to maturity of the investment. The larger the term, the greater the length of exposure and risk to market volatilities.
- ~~f) Leverage Risk - the magnification of an investor's risk and return that occurs when the investor takes on financial leverage through an investment product.~~

Credit and Maturity Frameworks

~~Investments are to comply with three key criteria relating to:~~

- ~~a) Overall Portfolio Credit Framework - The purpose of this is to limit the overall credit exposure of the portfolio;~~
- ~~b) Institutional Credit Framework - The purpose of this is to limit exposure to individual institutions based on their credit ratings; and~~
- ~~c) Term to Maturity Framework - The purpose of this is to limit risk based upon the time to maturity of the investment.~~

Overall Portfolio Credit Framework

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To control the credit quality on the entire portfolio, the following credit framework limits the percentage of the portfolio exposed to any particular credit rating category.

S&P Long Term Rating*	S&P Short Term Rating*	Maximum %
AAA (incl. government guaranteed deposits)	A-1+	100%
AA	A-1	80%
A	A-2	60%
BBB	A-3	20%

* or equivalents

All categories include any intermediate ratings (ie BBB includes BBB+, BBB and BBB-).

Institutional Credit Framework

Exposure to an individual institution will be restricted by their credit rating so that single entity exposure is limited, as detailed in the table below:

S&P Long Term Rating*	S&P Short Term Rating*	Maximum %
AAA (incl. government guaranteed deposits)	A-1+	45%
AA	A-1	35%
A	A-2	20%
BBB	A-3	10%

* or equivalents

All categories include any intermediate ratings (ie BBB includes BBB+, BBB and BBB-).

If any of the Council's investments are downgraded such that they no longer fall within the investment policy, they will be divested as soon as practicable. In the case of a downgrade of an investment, the General Manager is to inform the Mayor immediately of becoming aware of the event. The short-term credit rating limit will apply in the case of discrepancies between short and long-term ratings.

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~~Where a bank has a demonstrated commitment to the distribution of funds to the community within the Council municipal area the maximum amount of funds that can be deposited by the Council with that institution be increased by 5% from the benchmarks in the Institutional Credit Framework table above.~~

~~Term to Maturity Framework~~

~~The investment portfolio is to be invested within the following maturity constraints:~~

Overall Portfolio Return to Maturity		
Portfolio % <1 year	Min 40%	Max 100%
Portfolio % 1-2 years	Min 0%	Max 60%
Portfolio % 2-3 years	Min 0%	Max 20%

~~6.1(a)2 Interest Rate and Quotations on Investments~~

~~Not less than two (2) quotations shall be obtained from authorised deposit taking institutions and Managed [Funds investments](#).~~

~~6.23 Investment advisor~~

~~Where Council obtains the services of an investment advisor, the advisor must be approved by Council and licensed by the Australian Securities and Investment Commission [or operate as a corporate representative of a body and licensed](#). The advisor must [be an independent person who is free demonstrate its ability](#) to choose the most appropriate product within the terms and conditions of this policy.~~

~~The advisor will be required to provide written confirmation that [itthey does](#) not have any actual or potential conflicts of interest in relation to the -products that [itthey](#) may be reviewing or recommending, [including that they are not receiving any commissions or other benefits pertaining to the related investments and will not do so in the future](#).~~

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7. Performance Benchmarks

The Benchmark Rate for purposes of measurement of the portfolio's performance will be set in the applicable financial year's budget. This rate will be determined by reference to interest rate forecasting.

As the budget figure is based on predicted investment levels and expectations about future interest rates, using it as the sole comparison may be misleading, therefore an external benchmark may be used.

The external benchmark rate will be the Reserve Bank of Australia 90 Day Bank Accepted Bill Rate for the short term. The long term benchmark should be the composite bond index.

The investment performance will be determined on a monthly accrual basis (the income applicable for each month being determined) and compared to the above benchmark on a weighted 3 month average investment performance (the accrued interest being compared to the average investment balance for the month, averaged over 3 months).

8.7. Reporting

Documentary evidence must be held for each investment and details thereof maintained in an investment Register. The documentary evidence must provide the Council legal title to the investment. Certificates must be obtained from the financial institutions confirming the amounts of investments held on the Council's behalf as at 30 June each year and [the General Manger to ensure the confirmation is reconciled to the Investment Register.](#)

All investments are to be appropriately recorded in the Council's financial records and reconciled at least on a monthly basis.

A monthly report summarising investment performance will be provided to Council. A quarterly report detailing the investment portfolio in terms of performance, percentage exposure of total portfolio, maturity date and changes in market value will also be provided to Council.

9.8. Variations to Policy

The General Manager is authorised to approve temporary variations to this policy in exceptional circumstances, if the investment is to Council's advantage and/or also due to revised legislation.

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Such variation will be reported to the Mayor immediately. ~~All~~ major variations to this policy will be submitted to Council for approval [prior to the enactment](#).

10.9. Review

This Investment Policy will be reviewed at least every 2 years, or as required in the event of legislative changes.

Any amendment to the Investment Policy must be by way of Council resolution.

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Appendix 1 – Information about deposit and wholesale funding guarantees

~~AUSTRALIAN GOVERNMENT'S 2008 DEPOSIT AND WHOLESAL FUNDING GUARANTEES~~

~~The Australian Government's deposit and wholesale funding guarantee arrangements operate as set out below.~~

~~Purpose of the guarantees~~

~~The Prime Minister announced the deposit and wholesale funding guarantees on 12 October 2008.~~

~~The Government guarantees are designed to promote financial system stability and ensure the continued flow of credit throughout the economy at a time of heightened turbulence in international capital markets.~~

~~The guarantees apply to authorised deposit-taking institutions (ADIs) incorporated in Australia, which, as a group, are of systemic importance to the functioning of the financial system and the broader economy, and which are subject to prudential regulation by the Australian Prudential Regulation Authority (APRA) in accordance with international standards.~~

~~Recent developments in international wholesale funding markets have restricted the ability of Australian financial institutions to access funding, with potentially serious implications for liquidity and lending activity.~~

~~To address these pressures, the guarantees are designed to assist Australian banks, credit unions and building societies to continue to access funding in domestic and international credit markets. The guarantees are also designed to ensure that Australian institutions are not placed at a commercial disadvantage vis-à-vis their international competitors that have received similar government guarantees on their bank debt.~~

~~Scope of the guarantees~~

~~The guarantees are limited to Australian-owned banks, Australian ADI subsidiaries of foreign banks, credit unions and building societies ('eligible ADIs'). The guarantee applies to the foreign branches of eligible ADIs but not their foreign subsidiaries.~~

~~Wholesale funding guarantee~~

~~The guarantee will be extended on an issue by issue basis. Eligible securities will be restricted to securities issued by eligible ADIs with a term of up to 60 months with~~

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~~the guarantee to apply for the full term of the relevant security including in the period following the closure of the scheme to new issuances.~~

~~The facility is restricted to senior unsecured debt instruments. Certificates of deposit and bank bills will be covered by this facility. They will not be covered by the deposit guarantee. The guarantee will not cover structured debt.~~

~~The facility will apply to debt issuance in all major currencies including AUD, NZD, Euro, USD, Sterling, Yen and HKD. It will apply to eligible securities issued domestically or off-shore.~~

~~The Government will withdraw the facility once market conditions have normalised.~~

~~*Deposit guarantee*~~

~~The Government has guaranteed the deposits in eligible ADIs for a period of three years.~~

~~For deposits under \$1 million, the guarantee will be free. For deposits over \$1 million a fee will be charged to receive the benefit of the deposit guarantee.~~

~~**Coverage of the deposit guarantee**~~

~~The guarantee applies to deposits held in eligible ADIs by all types of legal entities, including individuals, partnerships, businesses, trusts (including in their offshore branches) and government entities.~~

~~The guarantee will not apply to products that are not deposit products with eligible ADIs. It does not apply to market-linked investment products such as share portfolios or managed funds, as these products provide an incentive for investors to pursue higher returns through investments that may involve greater risks, including the risk of making capital losses. It will also not apply to retirement income products including annuities.~~

~~The guarantee will not apply to products offered by non-ADI entities, including non-ADI subsidiaries of Australian ADIs. These entities are not subject to the prudential regulation framework that applies to ADIs, which protects the interests of depositors. Because of this, non-ADI entities are not permitted to offer deposits in Australia.~~

~~It will apply to the deposits held in eligible institutions, regardless of where the depositor resides. It will apply to deposits held in any currency.~~

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Fee Structure and level for the guarantees

Fees will be set at a single rate for all maturities for eligible securities up to 60 months, with a different rate applying to eligible ADIs based on their credit rating. The fees will apply to the wholesale guarantee and to the guarantee for deposits above the \$1 million threshold. The fees will be levied annually.

The fee scale is outlined in Table 1.

Table 1

Credit Rating	Debt Issues Up to 60 Months
AA	70bp
A	100bp
BBB and Unrated	150bp

Review of parameters

The deposit and wholesale guarantees contain features and variables that may require refinement or adjustment in light of market developments. These include the setting of the appropriate fee level and structure, the threshold for the deposit guarantee and the overall coverage of the scheme. The deposit and wholesale guarantee scheme will be reviewed on an ongoing basis and revised if necessary.

Foreign bank branches

The wholesale funding guarantee will be extended to APRA-regulated foreign bank branches in respect of their short term wholesale funding raised from Australian residents with maturities up to the end of 2009. This will be available at the same premium as applying to eligible ADIs.

Foreign bank branches will also be able to access the deposit guarantee in respect of domestic deposits held by Australian residents on the basis of the fee schedule; however, there will be no fee-free threshold.

Access to these guarantees will be subject to the following conditions:

- • The amount guaranteed be limited to 110% of the combined value of short-term wholesale liabilities and deposits held in respect of Australian residents as at 24 October 2008;
- • Branches cannot use guaranteed liabilities to support their parents; and

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- ~~The guarantee is only available if the liabilities are not guaranteed by the home authorities and the branch provides a statement from the home regulator that the parent bank is meeting relevant prudential requirements.~~

~~These requirements will ensure the funding is used for Australian operations only and that Australian taxpayer funds are protected.~~

~~The guarantees will be extended to foreign bank branches from 28 November 2008. Until that date the guarantees will not be available to foreign bank branches.~~

~~Administration of the guarantees~~

~~The Reserve Bank of Australia (RBA) will administer the guarantees as agent for the Commonwealth. The RBA will perform administrative tasks, including processing applications from institutions for coverage of liabilities and collecting fees.~~

~~The RBA will consult with APRA to ensure that the interests of the Commonwealth are protected. The Rules will allow for information sharing between the RBA, APRA and other relevant agencies. It is proposed that information and statistics about the scheme's operation will be made available on a public website.~~

~~The legal framework for the scheme will be deeds entered into by the Commonwealth and the participating institutions. The deeds will refer to scheme Rules that will be published by the Commonwealth.~~

~~Details of the scheme, including participating institutions and the liabilities that are covered will be made available on a suitable public website. The Government will provide six monthly reports to Parliament on the scheme operations.~~

~~*Wholesale funding guarantee*~~

~~Eligible ADIs must apply to the RBA for coverage of their liabilities. Eligible ADIs will be required to meet set criteria specified in Rules before they receive coverage. The Rules will be released in the near future.~~

~~*Deposit guarantee over the threshold*~~

~~Eligible ADIs will apply to the RBA for coverage of their deposits over the \$1 million threshold.~~

~~Eligible ADIs would choose whether to 'opt in' to the guarantee for their deposits above the threshold. If an eligible ADI opts in, it would be up to the ADI to determine the most suitable arrangements with its customers for those deposits it wishes to offer on a guaranteed basis~~

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~~Depending on the arrangement chosen by the ADI, depositors may need to indicate to the ADI whether they wish to receive the benefit of the guarantee for amounts over \$1 million.~~

~~If an ADI agrees to opt in, they would be required to pay the relevant fee to the RBA.~~

~~The fee would be payable on the value of the depositor's account(s) over the fee threshold.~~

~~It is expected that the ADI will pass on costs of the guarantee to depositors.~~

Commencement of guarantee arrangements

~~The guarantee scheme commenced on 28 November 2008. Up until that date deposits and wholesale funding eligible for the guarantee arrangements were guaranteed without charge. After that date, deposits over the \$1 million threshold and wholesale funding will only be guaranteed if an application has been made to the RBA and the relevant fee has been paid.~~

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Appendix 12

Flinders Council – Investment Strategy

Introduction

This investment strategy documents the intent of Flinders Council (“Council”) when purchasing, holding and selling investments pursuant to the Investment Policy of which this document forms an integral part.

The general intent is to maintain a well-diversified portfolio to support Council’s requirements for income and possible capital drawings in the both the short and long terms, but bearing in mind the need to preserve the underlying capital investment.

This strategy applies to either direct investments or those made through an Investment Advisor selected under Clause 6.2 of the Investment Policy

Investment Objectives

Council shall always act prudently to obtain the maximum rate of return within the set parameters, the need for income, access to cash and in consideration of appropriate levels of diversification.

Performance Objectives

Council has considered the current and likely expenditure and time frame needs and has determined that it is appropriate to provide a long term return on capital of a minimum of 25% per annum (net of taxes) above the underlying inflation rate.

Interest

Council at budget time shall determine the proportion of interest payments to be reinvested.

Comment [SP2]: David, are you happy with this inclusion. It seems silly to always get the interest paid out unless we need it.

Risk Profile

In light of the Investment Objectives of this document Council has determined the asset allocation and appropriate ranges to be applied, either directly or through managed funds, are:

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Asset Classes	Minimum	Maximum
Cash	5%	10%
Fixed Interest - Australian	5%	25%
Fixed Interest - International	5%	25%
Property Trusts - Australian	5%	10%
Property Trusts - International	5%	10%
Property Direct	0%	5%
Shares - Australian	15%	30%
Shares - International	10%	30%
Infrastructure	0%	5%
Alternative	0%	5%
Exotic	0%	5%

Comment [SP3]: David, could you please review the % and make any changes you see fit?

Risk Management

Property

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Property in the form of owning a direct asset is typically the least liquid form of investment. Typically, it requires a buyer at the time of offer to purchase the entire building and/or land. This can have a considerable lead time.

However property can provide a relatively secure level of income. The risk is the inability of the tenant to meet their rental obligations.

One final consideration with direct property is the capital required to purchase one asset. This may be a significant proportion of Council's assets.

Should the Investment Advisor consider investment in a direct property ~~they~~ it shall obtain appropriate valuations for the purchase price and rental income to

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satisfy themselves that the price or units of the property reflect the true value of the investment.

An investment in managed funds will generally provide more diversification through exposure to various properties across different property markets in Australia and overseas and will provide a more liquid form of investment as:

- The investment is unlikely to be more than a few percent of the total value of such a managed fund; and
- Because the managed fund is listed, there will generally be a number of potential buyers.

In terms of managed funds property ownership the Investment Advisor will have greater flexibility in their decision making.

Shares – Australian

Share investments can be made in two forms, listed or unlisted via a managed fund.

When considering investments in the form of direct shareholdings Council shall ensure the decision is based upon the anticipated longer term capital appreciation of the investment, as measured by the increase in its share price, as well as the potential dividend stream.

When investing in direct shares Council shall also give due consideration to the current exposure of the Fund to:

- The sectors of business the companies operate within (i.e. industrial, banking, retail, resources etc.);
- The manner in which the companies act and respond in various market conditions, (i.e. recession, recovery etc.); and
- The requirement for ongoing monitoring of such investments on a regular basis.

Where Council is of the opinion it does not hold or have access to the requisite skill set or experience or time to appropriately evaluate and monitor a portfolio of direct shareholdings, then the investments shall be made through managed funds recommended by the selected Investment Advisor approved and appointed by Council.

Managed funds may also be used as an investment option in conjunction with a portfolio of direct shareholdings or in isolation.

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The tax effectiveness of franking credits which are derived from holding investments may form part of the investment decision.

The Australian equity component of the portfolio is to be managed within the following guidelines:

- The majority of the exposure to Australian equities is to be held “directly” in stocks in the ASX 50 Index. The exposure to any one stock in the ASX 50 Index is limited to the greater of:
 - 5% of the value of the Australian equity component of the portfolio; or
 - 1.5 times it's weighting within the ASX 200 Index.
- The maximum aggregate exposure to Australian small/mid cap stocks is to be limited to 20% of the value of the Australian equity component of the portfolio; and
 - The exposure to any one listed investment company and/or unlisted managed fund and/or other similar investment vehicle is limited to 7.5% of the value of the Australian equity component of the portfolio; and
 - The exposure to any one small/mid cap stock (defined as any stock outside the ASX 50 Index held “directly” is limited to 2.5% of the value of the Australian equity component of the portfolio.

Shares – International

Historically this asset class has provided investors with the highest capital return. Past performance is no guarantee of future performance and this asset class must be evaluated on its merits as to its potential capacity to provide:

- Income return;
- Capital return, in excess of the prevailing inflation rate by a minimum of 2.0% per annum; and
- Volatility in the capital value.

Again this asset class can be accessed through both direct investment and managed funds.

Direct investment in international shares requires more time and administration than its counterpart. As such, Council shall generally consider investing in this asset class primarily through the use of managed funds.

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Infrastructure Investments

Infrastructure is a relatively new asset class in Australia for private investors. It comprises investments in such assets as power and water stations and associated distribution; major roads and bridges; and air and sea ports.

The way in which these assets are financed, the nature of the services they provide and the way in which those services are charged for often means an investment in infrastructure can provide reliable and tax advantaged cash flow and potential for capital growth.

In Australia, investments in infrastructure are principally available through listed unit trusts holding a number of assets. More recently, unlisted managed funds holding direct investments and listed unit trusts have become available.

Council shall consider investing in this asset class primarily through managed funds.

Alternate Investments

This category of asset class is varied. It allows for all forms of asset types not covered in the other outlined asset classes. This can include unlisted and tax advantaged investments in specialists industries; financial derivatives; and internally geared investments.

Exotic Investments

Council may consider investments in assets that may be deemed to be exotic. In considering such an asset, Council must be able to demonstrate the investment in such an asset meets one of the arms of the Objectives of the Fund as well as the risk profile of the Fund.

Risk Management

In relation to the risks involved with investing the assets of the Fund, when making an investment decision Council shall give consideration to the following range of possible risks:

Mismatch Risk – The chosen investment may not be suitable for the various needs, goals and circumstance of Council.

Inflation Risk - The real purchasing power of invested funds may not keep pace with inflation.

Reinvestment Risk – If Council relies on fixed rate investments, maturing funds may have to be reinvested at a lower rate of interest.

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Market Risk – Movements in the market mean the value of investments can go down as well as up, and sometimes suddenly.

Timing Risk – Trying to time entry to and exit from markets can involve exposure to potentially greater short-term volatility.

Risk of not diversifying - If all funds are invested into one market a fall in that market will adversely affect all of the capital

Liquidity Risk - Access to funds may not occur as quickly as required without suffering a fall in value.

Credit Risk - The institution that funds are invested with may not be able to make the required interest payments or repay capital

Legislative Risk – Investment strategies or products could be affected by changes in current laws and regulations.

Value Risk – Too much may be paid for the investment or it is sold too cheaply.

Manager Risk –The personnel or ownership of the fund manager may change so that the manager no longer has access to the skills or attitudes that contributed to earlier performance levels.

Currency Risk – Investments in assets located in other countries may rise or fall due to the relative value of the Australian currency.

Declaration

The documented Investment Strategy and its included principles, conditions and regulations are accepted by the Council.