



THE UNIVERSITY OF
MELBOURNE



INVESTMENT REPORT 2010

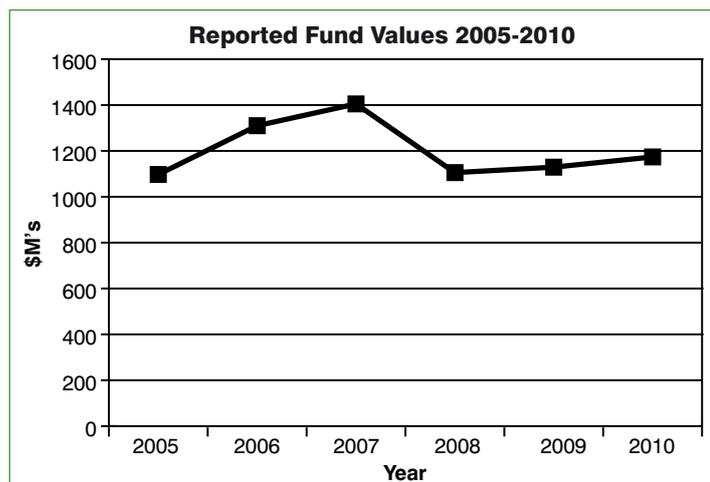
THE INVESTMENT FUND STRATEGY & AIMS

The fund is an accumulation of endowments from a significant number of trusts, and University funds surplus to immediate operating requirements.

The fund aims to meet the intergenerational requirements of the University. This includes providing funding for large capital projects or property acquisitions and to enable trust funds to fulfill obligations as per their trust deed, whilst at the same time ensuring the Fund's perpetuity. This is achieved by selecting a portfolio structure that provides long term capital growth, riding through short-medium term fluctuations, as well as reliable income streams to fulfill current obligations.

The University has outsourced its Long Term Fund management to the Victorian Funds Management Corporation (VFMC), an external "Manager of Managers".

PORTFOLIO HIGHLIGHTS

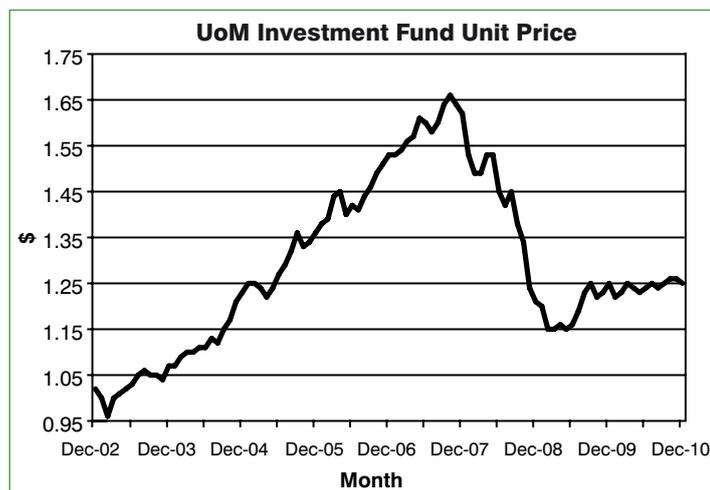


Reported Fund Values

\$m	2005	2006	2007	2008	2009	2010
Long Term Portfolio*	1094.7	1288.5	1362.15	1063.44	1128.73	1173.59
Short Term	2.5	21.3	42.76	41.91	0.41	0.19
TOTAL	1097.2	1309.9	1404.9	1105.35	1129.14	1173.78

*Includes growth and additional contributions from Trust Funds and general University.

Upon outsourcing of the Long Term Fund, the University's investment pool moved to a unitised Fund structure. On changeover date, 22nd November 2002, the units were allocated to fund holders on a one unit for each dollar invested basis. As can be seen in the graph below, the growth in the unit value of the fund has been quite steady for several years, however much of the growth was lost during 2008, reflecting Global Investment markets at the time. In 2009 the unit price began to recover and over the last 12 months, it has remained stable with the value as at 31 December 2010 at \$1.25.

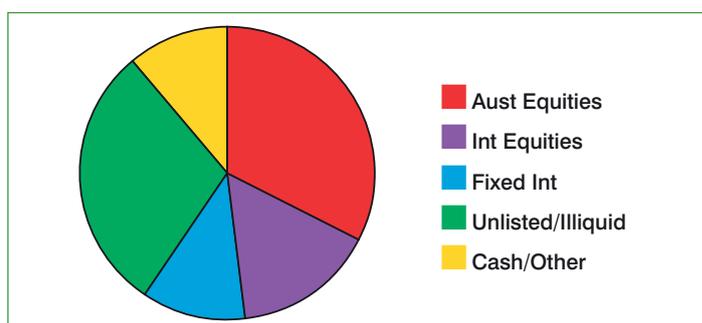


The portfolio has been a vital source of income for the University. In 2010 the Fund generated interest and dividend income of approximately \$58.12 million, all of which was distributed to unit holders (in line with the distribution cap of 5.50% for 2010). Income from the fund is key to ongoing capital works projects and the future continued support from alumni and friends is crucial.

ASSET ALLOCATION-LONG TERM PORTFOLIO

	Australian Equities	International Equities	Fixed Interest	Unlisted/Illiquid Assets	Cash/Other
	%	%	%	%	%
2005	51.90	20.80	13.90	13.29	0.10
2006	55.50	19.50	10.70	11.30	2.90
2007	45.30	20.80	9.30	24.40	0.20
2008	35.80	17.90	13.10	32.80	0.50
2009	39.00	16.40	12.80	23.10	8.70
2010	32.70	15.60	11.40	29.40	10.90

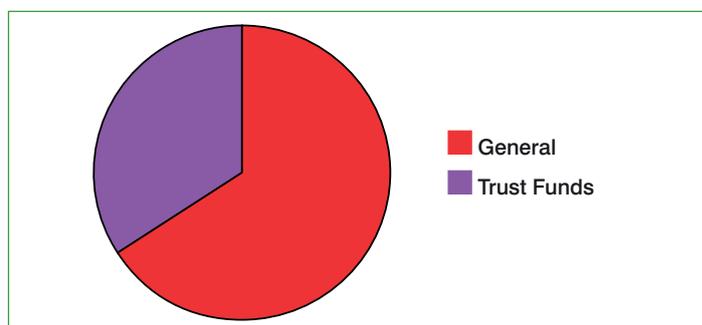
2010 ASSET ALLOCATION



As highlighted in the graph and table above, on the advice of the portfolio managers the University has continued to reduce its exposure to Australian Equities. The current target allocation for this asset class is 30%.

In line with diversification principles applicable to large investment funds, the University has continued to expand the asset classes in which it is prepared to invest. This strategy is designed to take advantage of the long term nature of the Fund and to ensure the Fund's growth and perpetuity. The result is a more balanced allocation in line with the new target weightings recommended by the advisors which is reviewed annually by the Investment Management Committee.

2010 FUND OWNERSHIP



LONG TERM FUND PERFORMANCE REVIEW

During 2010 the Long Term Fund objectives given to VFMC were:

- Outperform benchmark return by 1% p.a over a rolling 3 year period; and
- Achieve long term income yields of at least 4% p.a and growth of at least 4% p.a.

LONG TERM FUND PERFORMANCE RESULTS*

Year	2005	2006	2007	2008	2009	2010
Performance (after fees) % p.a	19.91	19.75	13.56	-21.57	8.78	4.75

* As a result of an internal process review, the University has identified that Franking Credits had not been included in Investment Portfolio earnings previously reported in prior years. These Franking Credits are a valuable source of investment Income and thus the University has moved to amend our reporting of Investment Earnings in 2010 which has been applied retrospectively to prior years.

As can be seen in the table above, the Fund has performed exceptionally well for many years. After the significant impact of the global financial crisis in 2008, the Long Term Fund has stabilised in 2010, achieving a return of 4.75% (after fees).

Since inception the long term fund has returned an average of 9.17% pa (including Franking Credits) of which 1.04% is capital growth and 8.13% income yield. This average has met its 4% income yield objective, but underperformed against its 4% growth target.

ASSET CLASS PERFORMANCE – 2010

Asset Class	Actual %	Benchmark %
Australian Equities	4.16	3.25
International Equities	0.23	0.12
Fixed Interest	5.36	6.04
Unlisted/Illiquid Assets		
Property	6.18	10.49
Private Equity	7.5	1.90
Infrastructure	109.67	1.9
Illiquid Strategies	-11.16	4.66
Liquid Strategies	16.26	0.34
Cash/Other	4.58	4.66

THE SHORT TERM FUND

VFMC invests the University's surplus cash in two cash-enhanced funds (Global and Australian). Allocations to the funds are at the University's discretion. A small portion of cash is managed in-house via an 11am facility.

The funds primary aim is to meet the short term and cyclical cash requirements of the University.

GOVERNANCE AND INVESTMENT POLICY

The Investment Fund is run using a "manager of managers" approach. The fund management contract is bound by specific performance criteria and subject to review every three years.

An Investment Management Committee exists to supervise, monitor and evaluate the investment performance of the University's funds. It ensures the stated objectives of the Fund are being met. The Committee is comprised of both University staff and industry professionals. In addition, independent asset consultants Towers Watson are engaged to provide asset allocation advice. The Committee meets six times throughout the calendar year with the second meeting of the year designed specifically to review the asset allocation strategies.

Broad objectives of the fund are to:

- provide liquidity to meet cyclic payments to beneficiaries of trusts and the possible capital expenditure requirements of the University; and
- achieve long-term growth and stability of trust and endowment funds and general funds.

These objectives are to be achieved without exposure to undue risk, including those stemming from the occurrence of a single event or the failure of any single investment.

MONITORING AND REVIEW PROCEDURES

The Investment Management Committee provides advice on investment guidelines, policies and strategies. They supervise the fund manager and custodial administrator and monitor the

performance of the portfolio. The Investment Management Committee reports through the University's Finance Committee to Council. The committee approved a Statement of Investment Objectives and Policy Document which sits alongside the University Investment Policy.

ACKNOWLEDGEMENT OF INVESTMENT RISK

The University Investment Policy sets specific objectives for volatility levels.

As part of these objectives it is acknowledged that a negative return is likely in one in every four years. Such short term fluctuations form part of the consideration of appropriate fund structure and the long term asset allocation.

INVESTMENT AND MANAGEMENT COSTS

The members of the Investment Management Committee generously donate their time and expertise in overseeing the fund.

The Long Term Fund has investment management costs of less than 0.30%. The investment returns quoted in this report are all net of fees. Endowment funds, where the University is the trustee, incur an administration fee of 2.5% of the distributed income. This amounts to less than 0.15% of the capital value of trust funds under investment. The administration fee covers a dedicated trusts office, with a full time lawyer and legal, administration and finance support staff, and a subsidy to relevant faculties and non-academic departments. The fee assists with the effective management of approximately 800 trust funds where the University is the trustee.

INVESTING IN VARIOUS ASSET CLASSES

In determining the appropriate asset classes in which to invest to achieve the Fund's objectives, the following criteria are considered:

- Access to and size of markets;
- Ability to generate income;
- Capital growth over the medium-long term; and
- Degree of liquidity.

The long term nature of the Fund and tax-free status of the University may also influence asset class decisions.

Investment activity embraces investment in physical financial securities and instruments.

The University is conscious of its responsibilities as a shareholder and actively asserts those responsibilities by voting at company meetings. Investment in physical securities must comply with the criteria set forth for each asset class. For example, the University does not wish to invest in companies involved in the production or manufacture of tobacco or tobacco related products.

Target Asset Weightings:

Class of Security	Target Allocation Range
Australian Equities	10% to 40%
Global Equities	0% to 30%
Emerging Markets	0% to 15%
Other Liquid Assets	15% to 50%
Illiquid Assets	10% to 30%

INVESTMENT INCOME RECORDING AND DISTRIBUTION

Distribution is proportionate to the unit holdings in the Fund. Income is distributed monthly subject to the maximum earnings threshold of 5.5% per annum. Income earned in excess of 5.5% is reflected in the capital holdings of the fund.

The University's Finance Committee has set a distribution cap of 5.5% in any year. This cap acts to reduce major variations in income available to trusts year to year, with any "excessive" returns in income reflected in the unit value and increasing the potential for higher income in future years. The rate of the cap is set to ensure that the annual results do not widely vary from the long term expected returns of the fund.

INVESTMENT MANAGEMENT COMMITTEE

Membership of the Committee is comprised of:

- A Chairperson nominated by Finance Committee
- The Senior Vice-Principal
- The Chief Financial Officer
- A member of Council appointed by the Finance Committee
- Up to four other members appointed by the Finance Committee, at least three of whom should have investment expertise and be external to the University.

The Committee has the power to co-opt.

Current Investment Committee

The Current Committee as at 31 December 2010 is as follows:

Mr Robert Johanson, Chairman
Director, Grant Samuel

Professor Bob Officer
Acorn Capital

Mr David White
Hawker Britton

Ms Justine Hickey
Trustee Director, Rio Tinto Staff Super Fund

Mr Ian Marshman
Senior Vice-Principal
University of Melbourne.

Mr Allan Tait
Chief Financial Officer
University of Melbourne

Professor Paul Kofman
Head of Finance,
Faculty of Business & Economics
University of Melbourne

Professor Rob Brown
Professor of Finance,
University of Melbourne

Ms Amanda Fong
Director & Client Advisor, UBS Wealth Management

EXAMPLES OF TRUST FUNDS AT WORK

Barry Taylor and David Lewis Philosophy Fund

Two outstanding contributors to the field of philosophy have been remembered through the Barry Taylor and David Lewis Philosophy Fund established at the University of Melbourne in 2010.

The late Associate Professor Barry Marshall Taylor had a distinguished 33 year career as a researcher and teacher in the philosophy department within the Faculty of Arts at the University until his retirement at the end of 2007. Commencing as a brilliant undergraduate and continuing Masters student at Melbourne, he went on to complete a PhD at Oxford before returning to join the department as a well respected lecturer in 1974.

Distinguished metaphysician, Professor David Kellogg Lewis, Doctor of Letters (Hon), FAHA was a long time friend of philosophy at the University of Melbourne, visiting from Princeton University on thirty occasions to connect with staff and students and enjoy the successes of the Essendon Football Club. Professor Lewis made ground-breaking contributions in philosophy of language, philosophy of mind, metaphysics, epistemology, and philosophical logic.

The endowed Barry Taylor and David Lewis Philosophy Fund has been established through a grant from The University of Melbourne USA Foundation. The grant was made possible through a generous gift of Stephanie Lewis to the Foundation, for the purpose of

supporting the teaching, study and research in the philosophy program at the University. Ms Lewis intends the Fund to memorialise her husband the late Professor David Kellogg Lewis and the late Associate Professor Barry Marshall Taylor.

The establishment of The Barry Taylor and David Lewis Philosophy Fund was announced at the University of Melbourne Philosophy reunion in October 2010, where alumni celebrated the contributions and lives of their former teacher, colleagues and friends. Inspired by Stephanie's wonderful generosity, many of the reunion attendees have also contributed to the fund and encourage their fellow alumni and community to do the same. Collectively, they hope to further build the fund to ensure that it provides in perpetuity broad based support for the philosophy program at the University.

The Olive Battersby Scholarship Fund

Passionate and talented future teachers are receiving support through a generous scholarship established by donors to the University of Melbourne's Graduate School of Education (MGSE).

The Olive Battersby Scholarship Fund was established in 2007 by siblings and alumni Joan Kent and John Battersby in memory of their sister, Olive Battersby (BA(Hons) 1946).

Olive worked for the University for over forty years from 1946 in the former Faculty of Education (now MGSE). Initially an Assistant to the faculty Dean, Olive went on to hold a number of positions at the University including Sub-Dean of Education and Faculty Librarian. In endowing the scholarship Joan and John hope to create a lasting commemoration of Olive's contribution to the University.

The Olive Battersby Scholarship fund annually provides financial assistance to Master of Teaching candidates.

Joan and John said they had been raised to recognise the importance of education and teachers. "[Our parents] had both left school at twelve but made sacrifices to make sure their four children had the best education possible. Our father insisted that education was the only thing that could not be taken from you."

John and Joan hope the scholarship fund will help talented students with limited resources to achieve their ambition to enter the teaching profession.

2010 recipient Balli Kaur is a perfect match for the scholarship criteria and vision. Having moved from Singapore to study the Master of Teaching (Secondary), Balli appreciates the assistance the scholarship provides.

"It was an honour to be awarded the scholarship, I felt that my academic efforts had been recognised and validated by the University" Balli said.

"The accelerated mode of the Master of Teaching course is extremely demanding and time-consuming, so finding the time to work part-time to support my studies was challenging. The scholarship helped to ease some of the costs of living and studying in Melbourne. It made it possible for me to take a bit of time off during evenings and weekends to focus on my coursework and my preparation for teaching rounds."

