

**SPEECH BY DAVID GONSKI AC, CHAIRMAN, FUTURE
FUND BOARD OF GUARDIANS, TO ASIC'S ANNUAL
DINNER**

25 MARCH 2013

IT IS AN HONOUR TO BE GIVEN THE OPPORTUNITY TO
ADDRESS YOU TONIGHT AND TO PLAY A ROLE IN ASIC'S
ANNUAL FORUM.

IN DOING SO I NOTE THAT I HAVE SPENT MOST OF MY
CAREER AS AN ADVISER AND CONSULTANT AND I
CONFESS THAT IT MAY BE A LITTLE AUDACIOUS OF ME,
AFTER ONLY 10 MONTHS IN THE ROLE OF CHAIRMAN OF
THE FUTURE FUND, TO STAND BEFORE YOU AS SOME
SORT OF EXPERT ON INSTITUTIONS, THEIR
PERSPECTIVES AND THE CHALLENGES THEY FACE.

THAT SAID, MY HOPE IS THAT MY COMMENTS TONIGHT WILL PROVOKE SOME DISCUSSION AND OFFER AT THE VERY LEAST A STARTING POINT FOR THE PANEL OF EXPERTS TO DEBATE, TEST AND ILLUMINATE THE TOPIC LATER THIS EVENING.

AUSTRALIA IN MY OPINION CAN BE PROUD OF THE POSITIVE GLOBAL REPUTATION OF ITS FINANCIAL AND INVESTMENT INSTITUTIONS. OUR FINANCIAL SYSTEM IS STRONG AND WELL REGULATED. OUR SUPERANNUATION SYSTEM IS RECOGNISED AS WORLD-CLASS AND TODAY REPRESENTS THE FOURTH LARGEST POOL OF RETIREMENT ASSETS IN THE WORLD.

THIS POSITIVE REPUTATION GLOBALLY IS IMPORTANT AND HAS BEEN ACHIEVED DESPITE THE FACT THAT AUSTRALIA ITSELF IS A COMPARATIVELY SMALL MARKET. OUR POSITIVE REPUTATION SHOULD NOT BE

TAKEN TO MEAN THAT OUR INSTITUTIONS DON'T HAVE CHALLENGES BOTH NOW AND IN THE FUTURE.

THESE CHALLENGES OFTEN ARISE FROM THE EXPECTATIONS INVESTORS AND STAKEHOLDERS GENERALLY HAVE OF THEM.

THE EXPECTATIONS FOR THE FUTURE FUND ARE WELL SET OUT IN THE MANDATES GIVEN TO US. IN PARTICULAR WE ARE EXPECTED TO ACHIEVE A LONG TERM RETURN OF CPI PLUS 4.5 – 5.5% PER ANNUM. WE ARE NOT UNIQUE WITH MOST INSTITUTIONS SEEKING TO ACHIEVE SIMILAR RESULTS. THE ISSUES THAT ARISE FROM THIS ARE LARGE AND BEAR CAREFUL THOUGHT.

THEY INCLUDE –

1. WHAT LEVEL OF RISK IS THE INSTITUTION PREPARED TO TAKE IN ORDER TO ACHIEVE THIS

SORT OF RETURN. WITH THE RISK FREE RATE BEING ABOUT 1% OVER CPI HOW DOES ONE ACHIEVE THE REMAINING PART OF THE MARGIN SOUGHT WITHOUT TAKING EXCESSIVE RISK.

AT THE SAME TIME STAKEHOLDERS RIGHTLY EXPECT INSTITUTIONS NOT TO LOSE MONEY AND TO BE CAREFUL IN THE INVESTMENTS THEY MAKE.

WE AT THE FUTURE FUND TAKE RISK VERY SERIOUSLY AS I KNOW DO OUR COLLEAGUES AT OTHER INSTITUTIONS. HOWEVER, THE ISSUE IS A FUNDAMENTAL ONE AND ONE WHICH IS DEALT WITH ON A DAILY BASIS.

2. AUSTRALIA AS I MENTIONED PREVIOUSLY IS ONLY A SMALL PART OF THE WORLD MARKET.

INSTITUTIONS INVESTING LARGE SUMS OF MONEY, AS MANY OF OUR INSTITUTIONS DO, QUITE QUICKLY

BEGIN TO RUN OUT OF TRACK WITHIN OUR BORDERS. INSTITUTIONS THEN HAVE THE ISSUE OF WHERE TO INVEST THEIR FUNDS IN OFFSHORE MARKETS.

ON THE ONE HAND THEY HAVE A CHOICE OF INVESTING IN DEVELOPED MARKETS WITH ESTABLISHED RESEARCH INSTITUTIONS TOGETHER WITH ESTABLISHED REGULATION AND LARGE AND EXPERIENCED FINANCIAL INSTITUTIONS.

UNFORTUNATELY WITH THIS OFTEN COMES THE POTENTIAL FOR LESS GROWTH.

ON THE OTHER HAND INSTITUTIONS CAN INVEST IN EMERGING MARKETS WITH THE POSSIBILITY OF GREATER GROWTH BUT WITH THE INHERENT RISK OF REGULATION AND SUPERVISION BEING NEW AND DEVELOPING AND WITH RESEARCH AND

ADVICE BEING LESS DEVELOPED AND AT TIMES
LESS RELIABLE.

THE CHOICE IS A DIFFICULT ONE. I ACKNOWLEDGE
THOUGH THAT IT IS NOT A NEW ONE – ADDITIONAL
GROWTH OFTEN BEING LINKED WITH ADDITIONAL
RISK.

3. MOST AUSTRALIAN INSTITUTIONS HAVE
AUSTRALIAN DOLLAR OBLIGATIONS AND RETURN
OBJECTIVES (PARTICULARLY IN RELATION TO
AUSTRALIAN INFLATION). THIS NATURALLY MAKES
AUSTRALIAN INVESTMENTS ATTRACTIVE BUT ALSO
MEANS THAT WHERE INVESTMENTS ARE MADE
OFFSHORE THERE IS A QUESTION OF WHETHER
THOSE INVESTMENTS SHOULD BE HEDGED BACK
INTO AUSTRALIAN DOLLARS. TO DO SO OFTEN
REQUIRES THE PROVISION OF SECURITY AND A
CONSEQUENT DRAG ON EARNINGS. A FAILURE TO

DO SO HOWEVER CAN OFTEN SEE THE INSTITUTION'S LIABILITIES NOT MATCHED WITH THEIR ASSETS.

AT THE FUTURE FUND, WE DO OPERATE A HEDGING PROGRAM, EVEN THOUGH IT REQUIRES US TO HOLD HIGHER LEVELS OF CASH.

4. THERE IS ALSO THE ONGOING DEBATE, BOTH IN AUSTRALIA AND GLOBALLY, ABOUT DIFFERENT MODELS OF INVESTING; ACTIVE VERSUS PASSIVE; IN-HOUSE VERSUS OUTSOURCED. MANY OF OUR PEERS IN CANADA, FOR EXAMPLE, FAVOUR THE USE OF IN-HOUSE TEAMS OVER THE USE OF EXTERNAL MANAGERS. THERE ARE ARGUMENTS FOR AND AGAINST EACH APPROACH.

I DO NOTE THAT OFTEN THESE DEBATES ARE FRAMED ON QUESTIONS OF FEES AND COSTS. PERSONALLY, WHILST NOTING THAT FEES AND

COSTS ARE VERY IMPORTANT, I DON'T BELIEVE THAT THEY SHOULD BE THE DECISION MAKER IN THIS AREA. THE ISSUE MUST SURELY BE WHAT IS BEST FOR ULTIMATE NET RETURNS.

I WOULD ALSO NOTE THAT AS WITH HUMANS, INSTITUTIONS MUST UNDERSTAND BOTH THEIR STRENGTHS AND THEIR WEAKNESSES. IT WOULD BE AN EXTRAORDINARY INSTITUTION THAT BELIEVED IT HAD IN-HOUSE CAPACITY TO UNDERSTAND THE ENTIRETY OF ALL MARKETS WITHIN THE WORLD. HOWEVER I DO ACCEPT THAT THERE ARE MANY JEWELS IN THE TEAMS THAT MAKE UP INVESTMENT PROFESSIONALS OF OUR INSTITUTIONS AND IT IS HIGHLY POSSIBLE THAT THE USE OF THESE CAN BE BETTER IN SOME AREAS THAN THE USE OF OUTSIDE MANAGERS.

5. THIS BRINGS ME TO, IN MY OPINION, THE GREATEST CHALLENGE OF THEM ALL.

INSTITUTIONS THAT ARE CHARGED WITH THE INVESTMENT OF FUNDS FOR THE LONG TERM HAVE TO INVEST WITH THAT IN MIND AND IN MY OPINION BE TESTED ON THAT BASIS.

SADLY IN AUSTRALIA WE LIVE IN A WORLD OF SHORT TERMISM.

OUR LISTED COMPANIES ARE GRADED SIX MONTHLY AND PERHAPS IN SOME CASES EVEN QUARTERLY AND OFTEN MAKE DECISIONS ACCORDINGLY.

SO MANY INSTITUTIONS ARE GRADED NOW ON A QUARTERLY BASIS AND RECEIVE ADVERSE

PUBLICITY IF THEY HAVEN'T PERFORMED WELL ON SHORT TERM METRICS.

COMPETING IN THE SHORT TERM CAN OFTEN BE DETRIMENTAL TO LONG TERM RESULTS AND IT IS LONG TERM RESULTS FOR SO MANY OF US THAT ARE MOST IMPORTANT.

THIS CONUNDRUM HAS TO BE DEALT WITH BY EACH INSTITUTION BUT ALSO HAS TO RECEIVE ADDED MATURITY BY THOSE IN THE MARKET WHO ARE RATING OR GRADING INSTITUTIONS AND COMMENTING THERE ON.

I SHOULD ALSO ADD THE OTHER ASPECT THAT AS LONG TERM INVESTORS, INSTITUTIONS SHOULD ENCOURAGE COMPANIES AND THE LIKE TO THINK AND ACT ACCORDINGLY. AUSTRALIAN INSTITUTIONS AS A GROUP HAVE NOT GOT THIS

MESSAGE ACROSS AND INDEED I HAVE SEEN A
BETTER UNDERSTANDING OF THIS ASPECT ON MY
TRAVELS OVERSEAS.

THERE ARE MANY OTHER CHALLENGES THAT I
BELIEVE APPLY TO INSTITUTIONS AT THIS TIME AND
I AM NOT SUGGESTING MY LIST IS A COMPLETE
ONE. WHAT I DO BELIEVE HOWEVER IS THAT THOSE
OF US INVOLVED IN RUNNING INSTITUTIONS HAVE
TO ABOVE ALL UNDERSTAND THE ISSUES AND
OFTEN TAKE A VIEW WHICH IS BEST FOR OUR FUND
DESPITE THE “SLINGS AND ARROWS” THAT MIGHT
BE SENT AGAINST US IN THE SHORT TERM FOR
TAKING THAT POSITION.

* * * * *

I WANT TO MAKE A FEW OBSERVATIONS AT THIS POINT
ABOUT HOW INSTITUTIONS IN MY VIEW SHOULD

GOVERN THEMSELVES AND HOW THEY SHOULD BEHAVE AS SHAREHOLDERS.

THE GOVERNANCE OF INSTITUTIONS IN MY OPINION IS A FUNDAMENTAL ISSUE FROM WHICH SO MUCH ELSE FLOWS. I BELIEVE STRONGLY IN THE VALUE OF GOOD GOVERNANCE.

I BELIEVE THAT THE BEST PERFORMING INSTITUTIONS ARE THOSE WHO ARE OVERSEEN BY A BOARD OF TRUSTEES OR GUARDIANS NOT INVOLVED IN THE DAY TO DAY RUNNING OF THE OPERATION.

THE FUTURE FUND WHEN IT WAS ESTABLISHED WAS IN MY VIEW CLEVERLY DESIGNED WITH A BOARD THAT IS COMPLETELY INDEPENDENT OF THE GOVERNMENT AND IS SUPPORTED BY A SEPARATE MANAGEMENT TEAM THAT CONDUCTS THE DAY TO DAY RUNNING OF THE INVESTMENT PROGRAM.

I HAVE IN THE VARIOUS ACTIVITIES IN WHICH I HAVE BEEN INVOLVED OVER A LENGTHY BUSINESS LIFE SEEN AND BEEN INVOLVED IN BOARDS WHICH ARE REPRESENTATIVE IN NATURE IN THAT THEIR VARIOUS PARTICIPANTS REPRESENT PARTICULAR INTERESTS WHO HAVE APPOINTED THEM. IN MY OPINION THE OBLIGATIONS AND THE REQUIREMENTS OF LEADING A MODERN INSTITUTION REQUIRES EACH OF THE BOARD MEMBERS TO HAVE THE SAME OBLIGATIONS AS ANY OF THE OTHERS. THIS BY ITS NATURE MEANS THAT AS IS THE CASE WITH THE FUTURE FUND EACH BOARD MEMBER HAS THE SAME OBLIGATIONS. IT FOLLOWS THAT IF ONE IS APPOINTED BY A PARTICULAR GROUP, ONCE APPOINTED HIS OR HER OBLIGATIONS ARE TO THE WHOLE ORGANISATION NOT JUST TO THAT GROUP.

I SHOULD ALSO ADD THAT I AM FIRMLY OF THE VIEW THAT THE MODERN DAY INSTITUTION WOULD PROFIT FROM A BOARD THAT ESTABLISHES A COMMITTEE

STRUCTURE SO THAT ISSUES CAN BE CONSIDERED IN
DETAIL ON A TIMELY BASIS. THE CONCEPT OF
COMMITTEES ALLOWS AMONGST OTHER THINGS BOARD
MEMBERS TO HONE AND SHOW THEIR ABILITIES TO
CHAIR MEETINGS, AS EACH OF THE COMMITTEES
WOULD HAVE ITS OWN CHAIR. IN ADDITION IT ALLOWS
DIRECTORS WITH PARTICULAR INTERESTS, SKILLS AND
EXPERIENCE TO OFFER THOSE TO THE INSTITUTION IN
A FRAMEWORK WHICH SHOULD NOT TRAVERSE THE
LINE BETWEEN EXECUTIVE AND NON-EXECUTIVE
ROLES.

A PARTICULARLY IMPORTANT COMMITTEE IN MY
OPINION OF ANY INSTITUTION IS THE RISK COMMITTEE.
RISK COMMITTEES ARE COMMON PLACE IN BANKS AND
OTHER FINANCIAL INSTITUTIONS. I BELIEVE THAT THEY
CAN OFFER REAL BENEFIT TO INVESTMENT
INSTITUTIONS. AS I HAVE PREVIOUSLY MENTIONED THE
QUESTION OF RISK IS A VERY IMPORTANT ONE AND THE

CONCEPT OF HAVING A PREORDAINED PERIOD OF TIME, WITH A DESIGNATED GROUP OF DIRECTORS WHO IN TURN HAVE A DESIGNATED FRAME OF REFERENCE AND FOCUS CAN ONLY HELP THE INSTITUTION TO COME TO TERMS WITH THE UNDERSTANDING AND POLICING OF RISK.

I SHOULD ADD THAT I SEE THIS AS A SEPARATE ROLE TO THAT OF AN AUDIT COMMITTEE. THE AUDIT COMMITTEE MAINLY HAS TO LOOK BACKWARDS WHERE AS THE ROLE OF A RISK COMMITTEE IS TO LOOK FORWARD.

I MENTIONED EARLIER THE CONCEPT OF THE BOARD LOOKING PURELY AT THE INSTITUTION AND NOT BEING BEHOLDEN TO REPRESENTATIVE INTERESTS. THIS SHOULD NOT BE READ AS A SUGGESTION THAT INSTITUTIONS TODAY CAN BE ISLANDS ON THEIR OWN

AND IGNORE THE WIDER WORLD IN WHICH THEY OPERATE.

I STRONGLY BELIEVE THAT CONSISTENT WITH BEST PERFORMANCE, IS A REQUIREMENT THAT INSTITUTIONS SEEK TO DO WHAT THEY BELIEVE IS RIGHT AND SEEK TO BE SEEN TO THINK IN A BROAD WAY AND NOT JUST ONE FOCUSED ON PROFIT.

IF ONE NEEDS TO BE CONVINCED OF THIS REMEMBER THAT THE BACKBONE OF ANY INSTITUTION IS ITS STAFF AND I HAVE NO DOUBTS THAT STAFF WHO WORK FOR ORGANISATIONS INVOLVED IN THEIR COMMUNITY WHO ARE CONCERNED ABOUT SUSTAINABILITY OF THEIR BUSINESSES AND RESPONSIBILITY IN THEIR SOCIETY ARE BOTH HAPPIER AND INDEED MORE LIKELY TO REMAIN WITH THAT ORGANISATION FOR THE LONG TERM.

IN ADDITION, I AM CONSCIOUS OF THE FACT THAT IF INSTITUTIONS DON'T HAVE AN EYE TO BEING APPROPRIATELY RESPONSIBLE THAT CAN OFTEN RESULT IN GOVERNMENTAL REGULATION.

TO ASSIST IN THIS WE AT THE FUTURE FUND HAVE ESTABLISHED A GOVERNANCE COMMITTEE WHICH SPECIFICALLY LOOKS AT QUESTIONS SUCH AS THE ONES I HAVE MENTIONED.

OUR RECENT DECISION TO EXCLUDE TOBACCO COMPANIES FOLLOWED CAREFUL DELIBERATION BY THAT COMMITTEE. AS MANY OF YOU WOULD RECOGNISE, THERE ARE WIDE RANGING VIEWS ACROSS THE COMMUNITY ABOUT WHAT SHOULD AND SHOULD NOT BE INVESTED IN, BOTH AS CONCERNS PRODUCTS BUT ALSO AS TO WHETHER ONE SHOULD PRIORITISE PARTICULAR SECTORS SUCH AS AUSTRALIAN INFRASTRUCTURE.

IN THE END, INSTITUTIONS NEED TO ESTABLISH THEIR OWN POSITIONS ON THESE ISSUES, THIS INVOLVES CONSIDERING THE MATTER AND FINDING THEIR OWN SENSE OF WHAT IS THE RIGHT THING TO DO.

IN ADDITION I BELIEVE THAT INSTITUTIONS AS PART OF BEING INVOLVED IN THEIR COMMUNITY HAVE AN OBLIGATION AT LEAST IN THEIR HOME TERRITORY TO EXERCISE THE RIGHTS THEY HOLD IN LISTED COMPANIES.

AS SOMEONE WHO CHAIRS A PUBLICLY LISTED COMPANY AND HAS BEEN ON THE BOARD OF MANY PUBLIC COMPANIES I CAN ATTEST TO HOW IMPORTANT AND VALUABLE THE EXERCISE OF VOTING RIGHTS AND DIALOGUE BETWEEN INVESTORS AND COMPANIES CAN BE.

IT DOESN'T MATTER HOW DILIGENT THE MANAGEMENT OF A LISTED COMPANY, IF ITS MAJOR SHAREHOLDERS DON'T PARTICIPATE IN VOTING ON RESOLUTIONS AND DON'T PUT THEIR VIEWS TO MANAGEMENT FROM TIME TO TIME, AN IMPORTANT PROTECTION FOR THE ONGOING GOOD OF THE COMPANY HAS BEEN REMOVED.

MY OBSERVATION IS THAT WISE COMPANIES LISTEN TO THE VIEWS OF THEIR SHAREHOLDERS AND RESPOND POSITIVELY – EITHER BY TAKING ON THE VIEWS OR EXPLAINING WHY THEY HAVE A DIFFERENT OPINION.

FINALLY, LET ME NOW TURN TO DEVELOPING CHALLENGES FOR INSTITUTIONS.

I KNOW THAT THE QUESTION IS REGULARLY POSED AS TO WHETHER THE CHALLENGES AND ENVIRONMENT IN WHICH INVESTMENT INSTITUTIONS OPERATE IS, IN

FACT, ANY MORE DIFFICULT THAN HAS BEEN FACED IN YEARS PAST.

CERTAINLY, EVERY GENERATION OF INVESTORS FACES CHANGE, BUT IT IS PERHAPS THE SPEED AND GLOBALLY INTERCONNECTED NATURE OF CHANGE TODAY THAT IS NOTE WORTHY.

THE EXISTENCE OF NEW TECHNOLOGY I FIND VERY EXCITING AND FAR FROM FEARING IT I THINK OVERALL IT ADDS ENORMOUSLY TO OUR LIVES AND TO OUR BUSINESSES. HOWEVER, THERE ARE AREAS OF THIS THAT MAKE RISK A BIT MORE DIFFICULT TO JUDGE THAN PERHAPS PREVIOUSLY.

THE CONCEPT OF LARGE AMOUNTS OF TRADING AFFECTED THROUGH ALGORITHMS AND HIGH FREQUENCY TRADING COME TO MIND. CLEARLY BOTH HAVE TO BE UNDERSTOOD WHEN CONTEMPLATING

UNIT PRICING; WHAT IS ACTUALLY HAPPENING IN THE MARKET AND THE EFFECT THAT THEY WILL HAVE ON THE LONG TERM INVESTOR. TO ME THIS IS A QUESTION VERY MUCH OF SEEKING TO UNDERSTAND THE EFFECT OF THESE SO AS TO RENDER THEM AT WORST NEUTRAL AND AT BEST TO SEEK TO OPTIMISE THE POSITION OF ONES INSTITUTION.

AS A LAWYER BY TRAINING I AM NATURALLY CONCERNED ALSO ABOUT COUNTERPARTY RISK. THE MORE THAT IS NOT DONE THROUGH A SUBSTANTIAL CLEARING HOUSE OR IN AN OPEN MANNER, THE MORE I BELIEVE INSTITUTIONS AND OTHER INVESTORS HAVE TO UNDERSTAND WHAT COULD GO WRONG IN THE PROCESS OF THEIR TRANSACTION. I SHOULD ADD HERE ABSOLUTELY A DECLARATION THAT I AM NO LONGER THE CHAIRMAN OF THE ASX!

I THINK ALSO IN CONSIDERING CHALLENGES THE CONCEPT OF INCREASED INFORMATION AVAILABLE TO THE PUBLIC GENERALLY IN CIRCUMSTANCES OF NO REAL INCREASE IN EDUCATION IN FINANCIAL MATTERS SHOULD CONCERN INSTITUTIONS. TODAY SO MANY CAN WATCH SHARE PRICES; SEE WHAT'S HAPPENING IN GREECE AND OTHER PARTS OF THE WORLD; HEAR WHAT THEIR NEIGHBOURS ARE EARNING, ETC. THIS CAN MAKE THEM START TO ACCEPT WHAT THEY EXPECT OF INSTITUTIONS AND THEIR SAVINGS GENERALLY AND THIS IS GOOD. HOWEVER I DON'T BELIEVE THAT MOST HAVE BEEN EDUCATED ENOUGH IN FINANCIAL MATTERS TO UNDERSTAND RISK AND REWARD, WHAT REALLY AFFECTS AUSTRALIA AND THEIR INVESTMENTS. THIS IS A COMPARATIVELY NEW PHENOMENON.

INSTITUTIONS CAN PLAY A PART IN FINANCIAL LITERACY AND I BELIEVE NOT ONLY NEED TO DO SO BUT ALSO TO

ENCOURAGE MORE UNDERSTANDING OF THESE MATTERS IN THE COMMUNITY GENERALLY.

DRAWING THESE POINTS TOGETHER I WOULD SAY TO YOU THAT AFTER MY LENGTHY 10 MONTH EXPERIENCE AT THE FUTURE FUND IT IS A VERY EXCITING TIME TO BE INVOLVED IN A LARGE INVESTING INSTITUTION.

HOWEVER WITH THE EXPECTATIONS OF INSTITUTIONS VERY PUBLIC AND VERY HIGH IT IS IMPERATIVE THAT THOSE OF US INVOLVED IN RUNNING THEM CLEARLY UNDERSTAND THE RISKS IN WHICH WE ARE INVOLVED; PARTICIPATE AS BEST WE CAN IN MODERATING THEM AND I BELIEVE BE INVOLVED IN OUR COMMUNITIES AND THE BUSINESSES IN WHICH WE INVEST. WE MUST SEEK TO ENSURE THAT STAKEHOLDERS EXPECTATIONS OF US ARE INFORMED AND EDUCATED AND NOT UNREALISTIC. SOCIETY'S SUPPORT FOR US MUST CONTINUE AS OURS DOES FOR THEM.