



## Part 2: Operations and Performance

### Operations and performance

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#### Introduction

The principal functions of the AOFM are:

- issuance of Australian Government Securities (AGS) to support the Government's financing task (including maturing debt) in accordance with broader Government policy objectives (such as promoting liquidity);
- managing the Government's daily cash balances through borrowings and investments;
- undertaking investments in financial assets according to policy directives, or as part of broader portfolio management;
- developing risk assessments that support the effective cost management of the debt and asset portfolios; and
- supporting the efficient operation of the Australian financial system through its debt issuance choices.

This section outlines the activities undertaken in 2014-15 and reports on AOFM performance against these functions.

### Treasury Bond and Treasury Indexed Bond issuance

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#### *Objective*

The main objective of Treasury Bond and Treasury Indexed Bond issuance is to raise monies to fund the Australian Government Budget.

Another objective is to support the efficient ongoing operation of Australia's financial market. This second objective is achieved in the following ways:

- Treasury Bonds, Treasury Indexed Bonds and Treasury Bond futures are used by financial market participants as benchmarks for the pricing of other capital market instruments and to manage interest rate risk; and
- the existence of active and efficient physical and futures markets for sovereign debt strengthens the robustness of the financial system and reduces its vulnerability to shocks.

#### *Achieving the objective*

The 2014-15 debt issuance programme was successfully completed. The length of the nominal yield curve was consolidated at around 20 years, and liquidity was built in several new and existing bond lines.

In 2014-15 the Reserve Bank of Australia (RBA) reduced the target cash rate by 50 basis points to a record low 2 per cent. Over the course of 2014-15, AGS yields trended lower, with the implied yield on the ten-year Treasury Bond futures contract reaching a record low in February 2015. In the last quarter of 2014-15, AGS

yields sold off sharply and the yield curve steepened in line with sovereign European and US Treasury bonds. The 2014-15 financial year ended with volatility around the Greek debt negotiations and uncertainty regarding the timing and size of the first expected US federal funds rate increase in nine years.

The higher yields on Australian bonds relative to other similarly rated sovereign bonds remained attractive to offshore investors, especially in the first three quarters of 2014-15. The steady offshore demand for AGS resulted in the ten-year spread to US Treasury yields contracting in March 2015 to the lowest level in more than a decade.

Non-resident holdings were on average around 66 per cent of the total AGS outstanding during 2014-15. The proportion of AGS held by offshore investors has declined slightly in recent years from a peak of around 76 per cent in June 2012, as illustrated in Chart 1.

**Chart 1: Non-resident holdings of Australian Government Securities**



(<http://aofm.gov.au/files/2015/10/P2->

C1.jpg)

### Treasury Bonds

Gross Treasury Bond issuance for the year totalled approximately \$74 billion. The bulk of issuance was into existing bond lines in order to enhance their liquidity and in turn, the attractiveness of the AGS market. This seems to have been particularly important to international investors. In addition, four new Treasury Bond lines were launched in 2014-15:

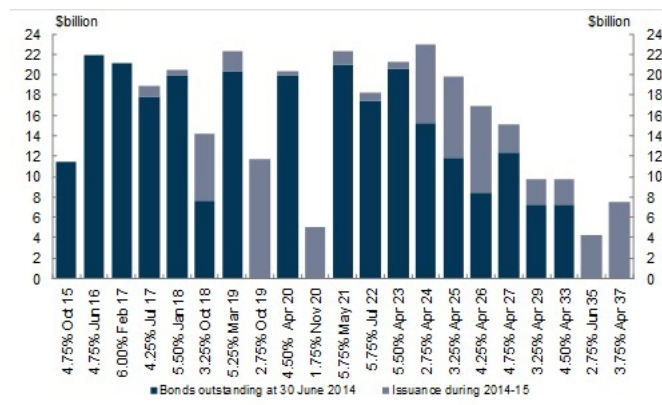
- new bond lines with maturity dates in October 2019 and November 2020 were opened to support the operation of three-year Treasury Bond futures contracts and to assist in reducing growth in the amount outstanding in surrounding bond lines, which will make it easier to manage maturity of those bonds; and
- new bond lines with maturity dates in April 2037 and June 2035 were issued to support lengthening of the yield curve to around 20 years.

In selecting the bond lines to issue each week, the AOFM took account of prevailing market conditions; information from financial market contacts about investor demand; relative value considerations; scope for increasing the liquidity of outstanding bond lines; and the need to manage the maturity structure to limit funding risk. Two tenders were held most weeks, typically comprising a tender of a long-dated bond line and a tender of a short-dated bond line, with the amount offered at each tender in the range \$500 million to \$2 billion.

Chart 2 shows Treasury Bonds outstanding as at 30 June 2015 and into which lines issuance was allocated during the 2014-15 financial year.

During the year, the total volume of Treasury Bonds outstanding increased by around \$44 billion, to \$335 billion. At the end of the year, there were 21 Treasury Bond lines with 16 of these lines having over \$10 billion on issue.

**Chart 2: Treasury Bonds outstanding as at 30 June 2015 and issuance in 2014-15**



(<http://aofm.gov.au/files/2015/10/P2->

C2.jpg)

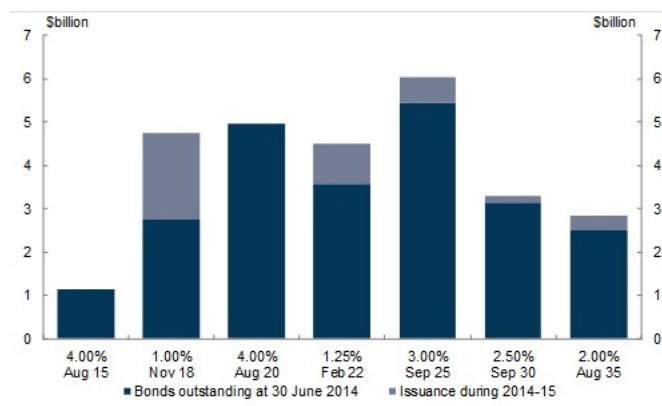
### Treasury Indexed Bonds

Treasury Indexed Bond issuance for the year totalled \$4 billion.

Tenders for the issue of Treasury Indexed Bonds were conducted twice a month, in most months. The volume of each line outstanding, relative yields and other prevailing market conditions were all considered in the selection of which line to offer.

Chart 3 shows seven Treasury Indexed Bond lines and the amounts outstanding as at 30 June 2015, together with the allocation of issuance during the 2014-15 financial year.

**Chart 3: Treasury Indexed Bonds outstanding as at 30 June 2015 and issuance in 2014-15**



(<http://aofm.gov.au/files/2015/10/P2->

C3.jpg)

## Performance

### Funding the Budget

The Government's budget financing requirement in 2014-15 was fully met.

The budget underlying cash deficit for 2014-15 was higher than estimated at the time of the 2014-15 Australian Government Budget. The resulting larger than expected budget financing task was managed primarily by increasing Treasury Bond issuance.

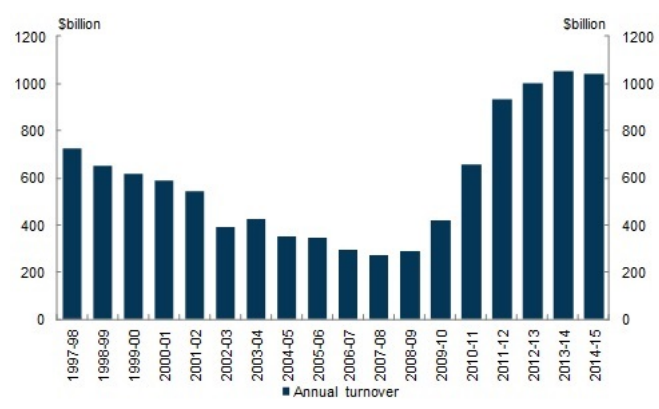
### Market liquidity and efficiency

The Treasury Bond and Treasury Indexed Bond markets operated smoothly throughout 2014-15 with liquidity again being maintained throughout the year.

Financial market liquidity has a range of interpretations, however one indicator of liquidity is turnover in the secondary market. Charts 4 and 5 show the evolution of total secondary market turnover from 1998-99 through to 2014-15. In 2014-15, turnover was around \$1 trillion for Treasury Bonds (1 per cent lower turnover

than in 2013-14) and \$50 billion for Treasury Indexed Bonds (8 per cent lower than in 2013-14). Strong liquidity is attractive to investors and reflects favourably on a sovereign bond market.

**Chart 4: Treasury Bond secondary market turnover**

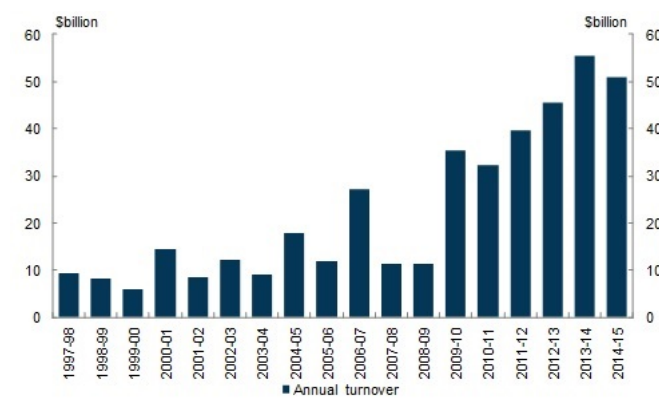


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C4.jpg)

Source: Based on data sourced from the Australian Financial Markets Association.

**Chart 5: Treasury Indexed Bond secondary market turnover**



(<http://aofm.gov.au/files/2015/10/P2->

C5.jpg)

Source: Based on data sourced from the Australian Financial Markets Association.

Turnover in the Treasury Bond futures market is significantly higher than in the underlying Treasury Bonds. The three-year Treasury Bond futures contract is amongst the ten most traded long term interest rate futures products in the world.<sup>[1]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftn1](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftn1))

Treasury Bond futures continued to display strong liquidity in 2014-15 with the turnover of three-year Treasury Bond futures contracts increasing by 4 per cent over the previous year and turnover of the ten-year contracts increasing by 16 per cent. Turnover in recent years (on a three-month moving average basis) is illustrated in Chart 6. All Treasury Bond futures contract close-outs in 2014-15 occurred smoothly.

**Chart 6: Treasury Bond Futures market turnover three-month moving average**



(<http://aofm.gov.au/files/2015/10/P2->

C6.jpg)

Source: Based on data sourced from the Australian Securities Exchange.

The AOFM's securities lending facility allows market participants to borrow Treasury Bonds and Treasury Indexed Bonds for short periods when they are not otherwise available in the secondary market. This enhances the efficiency of the market by improving the capacity of intermediaries to continuously make two-way prices, and reduces the risk of settlement failures and supports market liquidity.

There was a relatively low usage of the securities lending facility throughout the year. The facility was used 13 times for overnight borrowing in 2014-15 compared with 18 times during 2013-14. The face value amount lent in 2014-15 was approximately \$348 million.

#### Efficiency of issuance

The AOFM used competitive tenders and syndications as the means by which all issuance of AGS was undertaken in 2014-15. The use of competitive tenders remains the mainstay of AOFM's issuance operations.

Tenders held during 2014-15 were well supported. Table 1 summarises the results of Treasury Bond tenders conducted during the year. The results are shown as averages for each half-year and grouped by the maturity dates of the bonds offered.

**Table 1: Summary Treasury Bond tender results**

Period	Maturity	Face value amount allocated (\$m)	Weighted average issue yield (%)	Average spread to secondary market yield (basis points)	Average times covered
July – December 2014	Up to 2022	14,600	2.8411	-0.69	4.59
	2023 – 2037	15,900	3.5124	-0.29	3.32
January – June 2015	Up to 2022	14,800	2.1012	-0.49	3.85
	2023 – 2037	17,000	2.7006	-0.25	3.10

The average ratio of the volume of bids received to the amount of stock on offer was 3.66 for Treasury Bonds in 2014-15, a slight decrease from 3.82 in 2013-14. The average tender size in 2014-15 of \$724 million was slightly smaller than 2013-14 due to lower gross issuance in 2014-15. Shorter-dated bond tenders generally received a greater volume of bids, which reflects core investor base interest in the short-mid part of the AGS yield curve.

The strength of bidding at tenders was reflected in very competitive issue yield spreads to the secondary market. At most Treasury Bond tenders, the weighted average issue yields obtained were below prevailing secondary market yields.

The average ratio of the volume of bids received to the amount of stock on offer was 4.61 for Treasury Indexed Bonds in 2014-15, a slight increase from 4.56 in 2013-14. At all tenders, the weighted average issue yields were below prevailing secondary market yields.

Full tender details are available in Part 5 of this annual report.

## Cash management

### Objective

The AOFM manages the daily cash balances of the Australian Government in the Official Public Account (OPA).

<sup>[2]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftn2](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftn2)) The AOFM's primary objective in managing these balances is to ensure that the Government is able to meet its financial obligations as and when they fall due. Other objectives are to minimise the cost of funding and holding the daily cash balances and to invest excess cash balances efficiently. In minimising cost, the AOFM also seeks to avoid any use of the overdraft facility provided by the RBA. <sup>[3]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftn3](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftn3))

### Achieving the objective

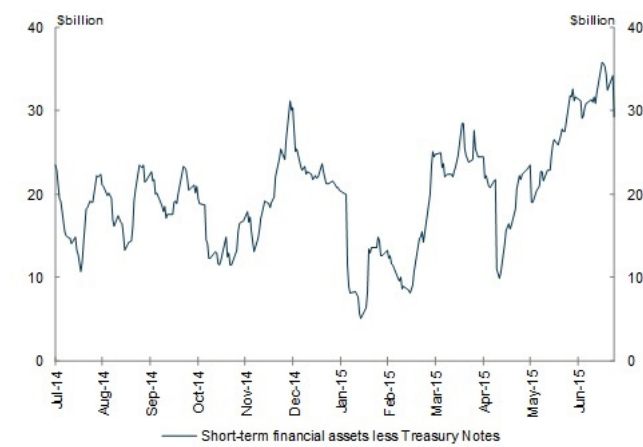
Achieving the cash management objective involves developing and implementing an appropriate strategy regarding short-term investments and debt issuance.

Cash balances not required immediately were invested in term deposits at the RBA, with the magnitudes and tenors of the term deposits determined by the AOFM. Maturity dates of term deposits were selected to most efficiently finance net outflows. Interest rates for term deposits at the RBA reflect the rates earned by the RBA in its open market operations.

Treasury Notes are issued to assist with management of the within-year funding requirement. The volume of Treasury Notes on issue ranged from \$4 billion to \$9.5 billion during 2014-15.

The size and volatility of the within-year funding requirement are reflected in changes in the short-term financial asset holdings managed by the AOFM, after deducting Treasury Notes on issue. Chart 7 shows movement in the funding requirement in 2014-15.

**Chart 7: Within-year funding requirement 2014-15**



(<http://aofm.gov.au/files/2015/10/P2-C7.jpg>)

### Performance

The task of meeting the Government's financial obligations as and when they fall due was fully met, with the overdraft facility provided by the RBA accessed only once in 2014-15 (in April 2015, with the facility cleared the next business day).

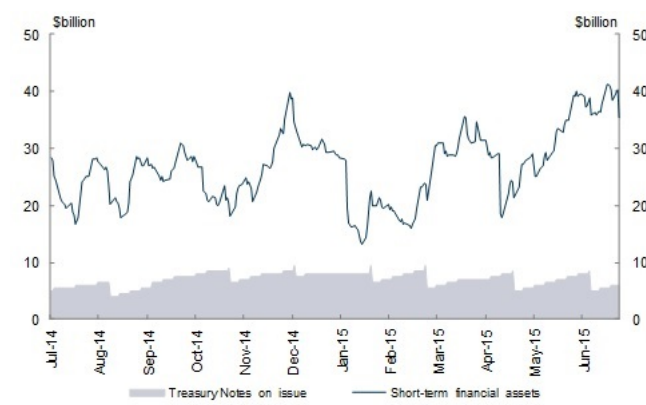
During 2014-15, the AOFM placed 326 term deposits with the RBA. The stock of term deposits fluctuated according to a range of factors influencing the AOFM's cash portfolio management needs and decisions. Term deposits ranged from a minimum of \$12.6 billion in January 2015 to a maximum of \$40.6 billion in June 2015.

The average yield obtained on term deposits during 2014-15 was 2.37 per cent, compared with 2.53 per cent in 2013-14. The decrease in average yield reflects the lower average level of interest rates that prevailed during 2014-15.

A total of \$24.5 billion of Treasury Notes were issued in 2014-15 (in face value terms). The tenders were well supported with an average coverage ratio of 3.57. Yields were on average around three basis points higher than Overnight Indexed Swap (OIS) rates for corresponding tenors (compared to around three basis points lower than OIS rates in 2013-14). Details are available in Part 5 of this annual report.

The movement in total short-term financial asset holdings managed by the AOFM (OPA cash balance plus term deposits with the RBA), together with the volume of Treasury Notes on issue, during 2014-15 are shown in Chart 8.

**Chart 8: Short-term financial asset holdings and Treasury Notes on issue 2014-15**



(<http://aofm.gov.au/files/2015/10/P2-C8.jpg>)

In undertaking its cash management activities, the AOFM was required to maintain the 91-day moving average of the daily OPA cash balance below the Ministerially approved upper limit of \$1.5 billion.

The 91-day moving average OPA cash balance was maintained below the Ministerial limit, throughout the year.

Movements in the 91-day rolling average OPA cash balance over the year is shown in Chart 9.

**Chart 9: 91-day moving average cash balance 2014-15**



(<http://aofm.gov.au/files/2015/10/P2-C9.jpg>)

C9.jpg)

## Minimising debt servicing costs subject to acceptable risk

### Objective

In managing the Commonwealth's debt portfolio, the AOFM seeks to minimise debt servicing costs over the medium term at an acceptable level of risk, by which is meant an acceptable level of variability in (interest) cost outcomes. It also seeks to maintain liquid bond lines to facilitate the issuance of debt at acceptable cost and to

manage the within year financing requirement risk that arises when bond lines mature, while also managing the impact of its issuance on the AGS market.

In order to meet its objective, the AOFM uses cost and risk measures that appropriately reflect the costs and risks faced by a sovereign debt manager. The primary cost measure used is historic accrual debt service cost. This includes interest payments made on AGS, realised market value gains and losses, capital indexation of indexed debt and the amortisation of any issuance premiums and discounts. Total accrual debt service cost can be expressed as a percentage of the stock of debt outstanding to provide the effective yield of the portfolio. This measure of cost is the most appropriate in circumstances where financial assets and liabilities are intended to be held, or in the AOFM's case, to remain on issue until maturity. The use of an historic accrual debt service cost measure excludes unrealised market value gains and losses.

An alternative measure of cost is 'fair value', which takes account of unrealised gains and losses resulting from movements in the market value of physical debt and assets. Debt service cost outcomes are presented in the AOFM's financial statements on this basis. A comprehensive income format is used that allows revenues and expenses on an historic basis to be distinguished from the effects of unrealised market value fluctuations, that is 're-measurements'. Fair value is useful in circumstances where it is possible that changes in market value may be realised in the future.

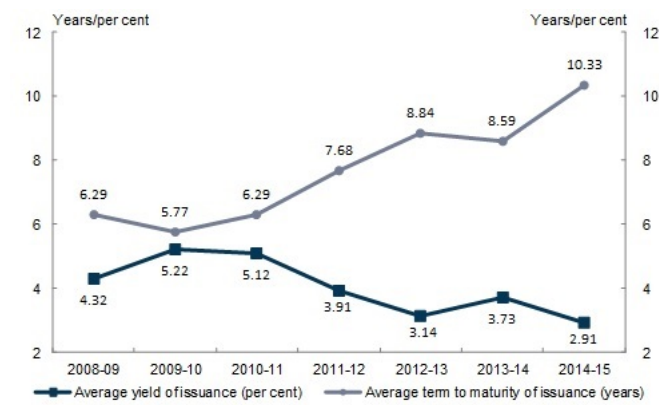
Variability in cost outcomes, or risk, can be measured in several ways. The AOFM calculates and compares several metrics to assess risk. In general, the level of risk can be characterised as a level of variation in cost outcomes over time. Debt issuance decisions made today have an impact on the variability of future cost outcomes because of their influence on the maturity profile of the portfolio and hence the amount of debt that needs to be refinanced and therefore 're-priced' through time.

### ***Achieving the objective***

The AOFM influences the cost and risk profile of the portfolio primarily through its decision making regarding the composition and maturity structure of the debt securities it issues. These decisions are framed through an annual debt issuance strategy approved by the Treasurer, which identifies the overall scale of the issuance task and its breakdown into different instrument classes. Within these broad strategy parameters approved by the Treasurer, the AOFM separately determines issuance weightings (specified as a range) applicable to different segments of the yield curve which are approved by the AOFM Chief Executive. Operational issuance decisions such as determining if, when, how much and what lines to issue each week, are made by the AOFM over the course of the year and are influenced by a range of factors including general market conditions, relative value considerations and feedback from investors. It is the AOFM's standard practice to regularly test the ongoing suitability of its overarching strategy with the AOFM Advisory Board, which is chaired by the Secretary to the Treasury. A range of specific limits, thresholds, guidelines and targets governing the AOFM's debt and investment activities through the year are separately approved by the Secretary through an Annual Remit. Strategic decision making around the portfolio is supported by an ongoing research program focused on exploring the cost and risk characteristics of alternative portfolio structures and issuance strategies. Informed by this research and feedback from the Advisory Board, the AOFM continued to lengthen the nominal debt portfolio in 2014-15.

#### **Chart 10: Treasury Bond issuance — average yield and term to maturity**



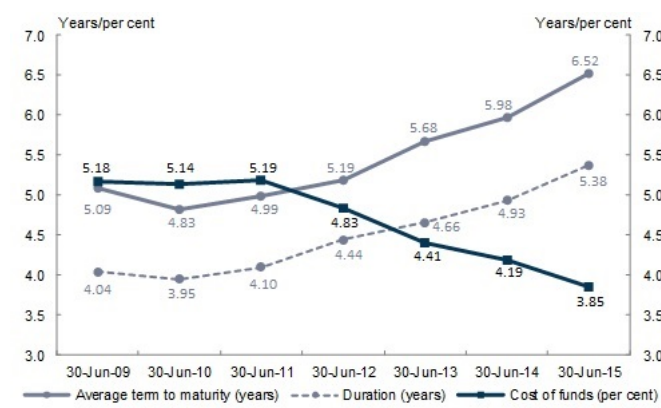


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C10.jpg)

Chart 10 shows that the average Treasury bond issued by the AOFM in 2014-15 had a term to maturity of 10.33 years and a yield of 2.91 per cent. This had the effect of lengthening duration and average term to maturity while lowering the effective cost of funds on the Treasury Bond portfolio as a whole (as shown in the next chart which shows the 'stock' analogue to the above flow information).

**Chart 11: Treasury Bond portfolio — modified duration, average term to maturity and cost of funds**

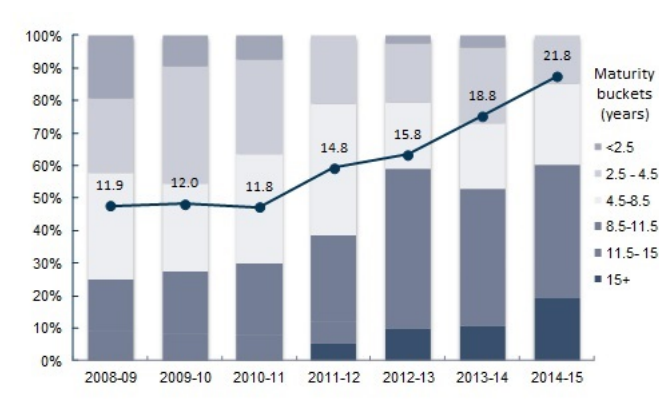


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C11.jpg)

Chart 11 shows that the average term to maturity of the Treasury Bond portfolio increased by 0.54 years to 6.52 years while duration rose by 0.45 years to 5.38 years over the course of 2014-15. Meanwhile, the effective cost of funds or yield on the Treasury Bond portfolio fell from 4.19 to 3.85 per cent in the year to 30 June 2015. This outcome was influenced by several factors, not least the continuation of low outright yields and consistent investor demand for AGS, which provided the AOFM with a favourable environment to continue with its lengthening strategy.

**Chart 12: Treasury Bond issuance distribution by financial year and term to maturity of longest line (years)**



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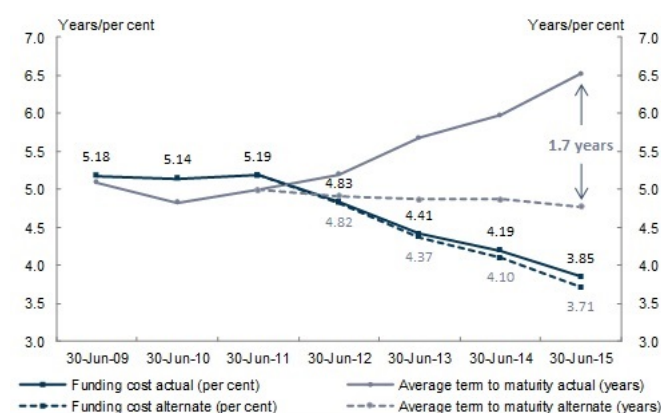
C12.jpg)

The AOFM's approach to lengthening has been twofold. Firstly, issuance has been skewed towards longer maturity bond lines. This is demonstrated in Chart 12 which shows that around 60 per cent of issuance in 2014-15 was allocated to longer bonds<sup>[4]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftn4](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftn4)) compared with around 30 per cent in 2010-11. Secondly, the AOFM has been progressively extending the length of the Treasury Bond yield curve. As at 30 June 2015 it was out to 21.8 years (up from 11.8 years as at 30 June 2011), following the establishment of the April 2037 line. The 20-year part of the yield curve was further complemented by the launch of the June 2035 line in March 2015. Combined, these new lines deliver on the AOFM's commitment to establish and maintain a 20-year curve benchmark. Extending the yield curve has facilitated portfolio lengthening by providing the AOFM with additional long issuance points to select from, while also broadening the appeal of the AGS market to include longer duration investors.

### ***Lengthening the debt portfolio – what if the AOFM had pursued a different strategy over the previous 4 years?***

Charts 10, 11, and 12 clearly demonstrate the impact of the AOFM's decision to lengthen the tenor of issuance on the duration and average term to maturity of the Treasury Bond portfolio. The success or otherwise of the lengthening strategy cannot, however, be solely judged from the outright movement in these metrics. Success must also be judged in terms of how it has helped the AOFM achieve its primary cost and risk management objective to minimise debt servicing costs over the medium term at an acceptable level of risk. A plausible counterfactual strategy against which to frame this judgement is one where the AOFM met the Government's financing requirements over the four years to 30 June 2015 without having lengthened the average term to maturity of the Treasury Bond portfolio to the extent that it has. Such a strategy has been retrospectively modelled to facilitate a comparison with the strategy the AOFM actually executed.

**Chart 13: Comparison of Treasury Bond funding costs and average term to maturity with and without lengthening and yield curve extension**

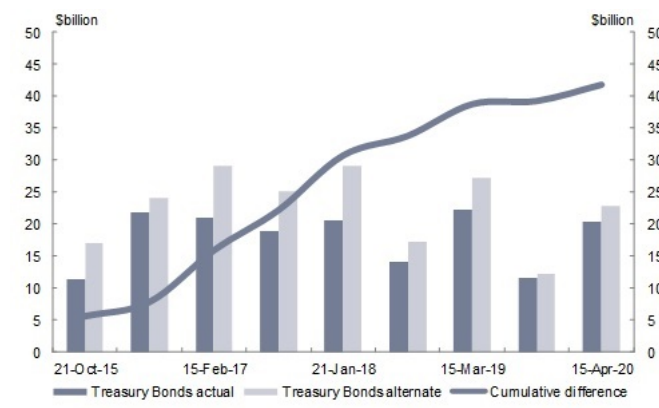


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C13.jpg)

Chart 13 shows that as at 30 June 2015, the AOFM has added about 1.7 years to the average term to maturity of the Treasury Bond portfolio (1.3 years when assessed on a duration basis) compared to the alternative of maintaining what was the pre-lengthening status quo. As yield curves have generally been upwards sloping, the AOFM's strategy of issuing more longer term debt has resulted in a slightly higher cost structure compared to the alternative shorter strategy equal to about 14 basis points as at 30 June 2015. The benefit from adopting a higher cost structure through longer issuance, however, is a significant reduction in the degree of inherent risk in the portfolio.

**Chart 14: Comparison of near maturity Treasury Bond lines on issue as at 30 June 2015 with and without lengthening (years)**



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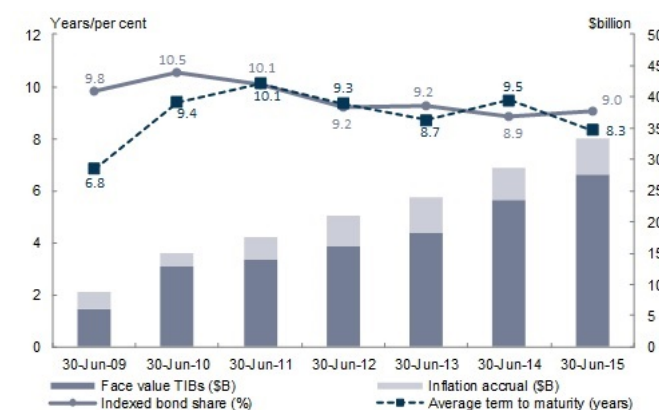
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Chart 14 demonstrates that the AOFM's gross borrowing program is reduced by about \$42 billion over the next 5 years compared to what it would otherwise have been. This is because less issuance needs to be allocated to refinancing maturing debt. The lengthening strategy has therefore reduced both refinancing and funding risk as it ensures gross issuance programs are smaller for any given fiscal path. Because gross issuance is smaller, this also means the portfolio is less exposed to future interest rate rises (which could erode or eliminate the cost advantage of the shorter alternative structure in time).

With the yield curve extended beyond 20 years, another benefit of the lengthening strategy is that the investor base for AGS is more diversified than it would otherwise have been. This is a positive for overall market liquidity and efficiency and enhances the AOFM's capacity to cost effectively meet the Government's financing requirements.

In summary, by lengthening, the AOFM now faces a lower annual refinancing task, is less exposed to future rate rises and benefits from a more diverse investor base. The additional cost of lengthening represents around 3 per cent of total interest expense on AGS. This is considered reasonable given the quantum of risk reduction and that the strategy has been executed through a period of historically low interest rates.

**Chart 15: Treasury Indexed Bonds – average term to maturity and share of the long-term funding base**



(<http://aofm.gov.au/files/2015/10/P2->

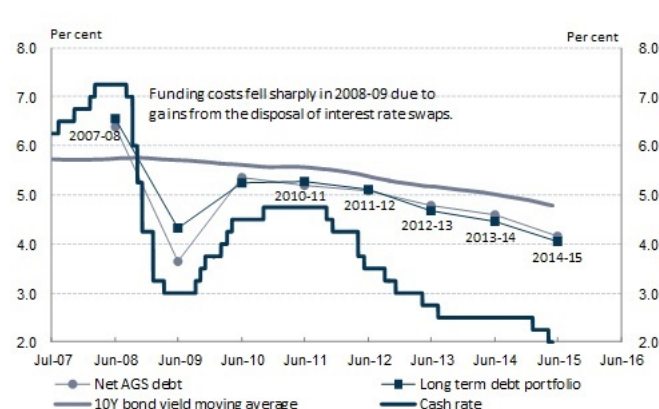
C15.jpg)

The AOFM's alternative long-term funding instrument to Treasury Bonds are Treasury Indexed Bonds. Indexed bonds, for which the capital value is adjusted periodically with changes in the Consumer Price Index, typically attract a different class of investor to nominal bonds and are thus a source of diversification in the funding base. The AOFM re-commenced issuance of indexed bonds in 2009-10 following an extended period of absence from this market and has issued regularly in the period since. While the indexed portfolio has been relatively stable as a share of the long term funding base for several years now, in absolute terms the stock of indexed bonds has continued to grow steadily (as shown in Chart 15).

### ***Minimising debt servicing cost at an acceptable level of risk***

The debt servicing cost<sup>[5]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftn5](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftn5)) of the net AGS debt portfolio managed by the AOFM in 2014-15 was \$13.59 billion on an average book volume of \$325.51 billion, representing a net cost of funds of 4.15 per cent for the financial year. The largest component of net AGS debt is the Long Term Debt Portfolio (comprised primarily of Treasury Bonds and Treasury Indexed Bonds), which incurred debt servicing costs of \$14.35 billion on an average book volume of \$353.65 billion implying a cost of funds of 4.06 per cent. The difference between net AGS debt and the Long term Debt Portfolio (LTDP) is the short term assets and liabilities the AOFM uses for liquidity management purposes (Term Deposits and Treasury Notes) and other residual assets (such as RMBS).

**Chart 16: Net AGS debt and Long Term Debt Portfolio cost of funds analysis (per cent)**



(<http://aofm.gov.au/files/2015/10/P2->

C16.jpg)

Chart 16 shows the funding cost profile of the net AGS debt portfolio and the LTDP back to 2007-08. These are contrasted with the cash rate and the 10 year moving average of the 10 year bond yield. In an environment where interest rates have been trending down, funding costs on the net debt portfolio and the LTDP have declined by 104 and 120 basis points respectively since 2010-11. This compares to declines of 275 basis points in the cash rate and 71 basis points in the ten year bond yield moving average over the same period. Given the largely fixed cost structure of the net debt portfolio and the LTDP, changes in funding cost will always lag changes in the overnight cash rate (changing only when existing debt securities or assets mature or new securities are issued/investments placed). In a comparison with the ten year bond yield moving average, funding costs have fallen further because of the relative 'over-representation' of recently issued debt in the portfolio through a period where issuance yields have been declining.<sup>[6]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftn6](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftn6))

Table 2 provides further details of the cost outcomes for the portfolio of debt and assets administered by the AOFM broken down by instrument and portfolio for 2013-14 and 2014-15.

**Table 2: Commonwealth debt and assets administered by the AOFM**

	Interest expense		Book volume		Effective yield	
	2013-14 \$million	2014-15 \$million	2013-14 \$million	2014-15 \$million	2013-14 per cent per annum	2014-15 per cent per annum
<b>Contribution by instrument</b>						
Treasury fixed coupon bonds	(11,811)	(13,078)	(274,66)	(321,839)	4.30	4.06
Treasury inflation indexed bonds	(1,650)	(1,266)	(27,661)	(31,804)	5.97	3.98
Treasury notes	(122)	(163)	(4,942)	(6,800)	2.46	2.39
Foreign loans (a)	(0)	(2)	(6)	(6)	6.89	28.39
Gross physical AGS debt	(13,583)	(14,508)	(307,275)	(360,449)	4.42	4.03
Term deposits with the RBA	608	604	23,996	25,471	2.53	2.37
RMBS investments	321	194	7,729	5,147	4.15	3.78
State Housing Advances	128	124	2,455	2,321	5.320	5.32

Gross assets	1,057	922	34,180	32,939	3.09	2.80
Net AGS debt	(12,527)	(13,586)	(273,094)	(327,510)	4.59	4.15
Contribution by portfolio						
Long-Term Debt Portfolio	(13,462)	(14,345)	(302,332)	(353,649)	4.45	4.06
Cash Management Portfolio	486	441	19,054	18,671	2.55	2.36
RMBS Portfolio	321	194	7,729	5,147	4.15	3.78
State Housing Portfolio	128	124	2,455	2,321	5.20	5.32
Total debt and assets	(12,527)	(13,586)	(273,094)	(327,510)	4.59	4.15
Re-measurements (b)	(3,671)	(7,512)				
Total after re-measurements	(16,198)	(21,098)	(273,094)	(327,510)		

Note: Sub totals and totals are actual sum results, rounded to the nearest million dollars. Effective yields are based on actual results before rounding, rounded to two decimal places. Book volume is a through the year average.

(a) Interest expense and effective yield on foreign loans incorporates foreign exchange revaluation effects.

(b) Re-measurements refer to unrealised gains and losses from changes in the market valuation of financial assets and liabilities.

The servicing cost of gross debt increased in dollar terms by \$925 million compared to the previous year. This was primarily due to an increase in the average volume of debt on issue from \$307.28 billion in 2013-14 to \$360.45 billion in 2014-15. In percentage terms however, the funding cost of gross debt declined by 40 basis points (4.42 per cent to 4.03 per cent). This improvement was driven by the issuance of new bonds through the year at yields that were below the average of pre-existing (and maturing) debt. Low rates also reduced the yield on funds invested in term deposits from 2.53 to 2.37 per cent and RMBS investments from 4.15 to 3.78 per cent.<sup>[7]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftn7](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftn7))

The return on gross assets in dollar terms for the period was \$922 million, a decrease of \$135 million compared to 2013-14. This was largely driven by a \$127 million reduction in income from RMBS resulting from the maturity of existing investments and lower interest rates. Income from term deposits was down only \$4 million despite lower investment yields due to higher average holdings through the year.

The net servicing cost of the combined portfolio of debt and assets was \$13.59 billion. This was higher in dollar terms compared to 2013-14, due to the volume of debt on issue being higher than the previous year. As a percentage of net debt, servicing costs fell from 4.59 per cent to 4.15 per cent, a product of more expensive, historically issued debt maturing and continued issuance over the year into a low interest rate environment.

The difference between the return on gross and net debt narrowed to 13 basis points in 2014-15 from 17 basis points in 2013-14. This can mainly be attributed to continued growth through the year in gross debt on issue and decline in gross assets.

Movements in market interest rates had an unfavourable impact on the market value of the portfolio in 2014-15. Unrealised losses from re-measurements amounted to \$7.51 billion. This compares to an unrealised loss of \$3.67 billion in the previous year. About 90 per cent of re-measurement losses are attributable to the higher market value of Treasury Bonds. As bond prices move in opposite directions to bond yields, it can be seen that the same favourable, lower interest rate environment responsible for driving down the AOFM's overall portfolio funding costs in 2014-15 (expressed as a percentage), were also responsible for this negative re-measurement impact.

As re-measurement items are highly volatile from one year to the next, they have no bearing on the AOFM's debt issuance strategy. Indeed were the AOFM to adopt a strategy designed to minimise the 'noise' from re-measurements, issuance would be limited to only very short-term debt securities, for example Treasury Notes and near maturity bonds, creating a portfolio structure that would maximise expected variability in debt servicing costs when measured in cash, accrual and public debt interest terms while also maximising exposure to refinancing and funding risk. In practice, the AOFM has been seeking to achieve the opposite outcome, through allocating a greater proportion of issuance to long dated lines.

## Residential mortgage-backed securities

## Objective

During the period October 2008 to April 2013, the AOFM was directed to invest up to \$20 billion in eligible RMBS to support competition in mortgage lending. In total, just under \$15.5 billion was invested.<sup>[8]</sup>  
([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftn8](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftn8))

On 10<sup>th</sup> April 2013, the Treasurer directed the AOFM to cease investment in new RMBS. On 5<sup>th</sup> May 2015, the Treasurer issued a new Direction under the PGPA Act to divest the Government's RMBS portfolio through a regular competitive process. According to this Direction, the AOFM should minimise potential market disruptions and is to exercise discretion on the timing and sale volume, subject to a \$500 million upper limit in any one month. While the Treasurer's Direction allows for sales of up to \$500 million per month in amortised face value terms, it also makes provision for periods of subdued or volatile market conditions. In the event that sales of less than \$300 million are achieved in three consecutive months because acceptable pricing cannot be met on a higher volume, the AOFM is to report back to the Treasurer with an assessment of market conditions.

## Achieving the objective

The Australian RMBS market initially strengthened in 2014-15. In the first quarter of the financial year, improving market conditions resulted in spreads on new primary transactions being at the lowest levels since before the financial crisis. While issuance volumes remained reasonably healthy throughout the financial year, spreads pushed higher as conditions deteriorated in line with a broad-based widening in credit margins globally.

Consistent with the 5 May 2015 Direction, the AOFM implemented a RMBS divestment program late in the 2014-15 financial year. The inaugural RMBS auction was held on the 24 June 2015 and over \$1.3 billion dollars of bids were received, in amortised face value terms. Around \$160.5 million was sold, or 12 per cent of bids, reflecting the AOFM exercising discretion to divest only at what it considers to be acceptable prices. The following table provides details of the first RMBS auction.

**Table 3: RMBS divestments for 2014-15**

TRANCHE	AMORTISED FV (\$m)	CLEAN VALUE (\$m)	GAIN (\$m)
Jun-15			
IDOL 2010-1 A2	74.17	74.61	0.44
PROGRESS 2011-1 A2	86.33	86.89	0.56
<b>Total</b>	<b>160.50</b>	<b>161.50</b>	<b>1.00</b>

The sales occurring at the June 2015 auction realised a gain on disposal of around \$1 million, or around 0.62 per cent of the amortised face value of the notes sold. This compares with sales between March 2010 and June 2014, in which the AOFM sold a total of around \$1.5 billion worth of notes, in amortised face value terms, with an associated gain on disposal of \$17.9 million, or 1.22 per cent of the face value of the notes sold.

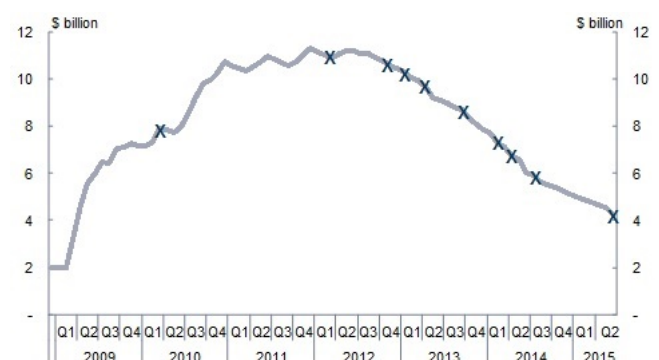
Whilst the AOFM has been directed to divest the RMBS portfolio in the entirety, the time frame over which this is achieved will be dependent on market conditions. The inaugural auction, for example, coincided with a period of market volatility in global credit markets which may have had a bearing on the outcome of the auction and, in particular, the volumes sold.

## Performance

Due to both sales and capital amortisation, the book value of the portfolio reduced in size from \$6.0 billion to \$4.3 billion over the course of the financial year. Chart 16 illustrates the evolution through time of the RMBS portfolio, in amortised face value terms, along with sales made since March 2010. As can be seen, the outstanding volume in the RMBS portfolio rose over the first two years to between \$10 billion and \$12 billion, where it remained for around two years, with new investments broadly matched by portfolio amortisation.

Between mid-2012 and mid-2014, the portfolio reduced at a relatively steady rate as a result of both amortisation and sales. The rate slowed through 2014-15 due to both a reduction in the portfolio's natural rate of amortisation and the lack of sales prior to the last week of the financial year.

**Chart 17: RMBS portfolio amortisation**



(<http://aofm.gov.au/files/2015/10/P2->

C16\_2.jpg)

#### RMBS sales (amortised face value sold)

Mar 2010	Mar 2012	Nov 2012	Feb 2013	May 2013	Oct 2013	Feb 2014	Mar 2014	Jun 2014	Jun 2015
\$73.8m	\$50.0m	\$62.8m	\$147.1m	\$300.7m	\$177.7m	\$317.1m	\$49.2m	\$341.0m	\$160.5m

The average margin over the one month bank bill rate (weighted by each of AOFM's investments) for the RMBS book remained stable over the financial year at around 127 basis points. Interest income in 2014-15 was \$193.4 million and, as noted above, sales in June 2015 contributed a further \$1 million in incremental income. Total accrual income of \$194.4 million represented an annualised return of 3.78 per cent on the portfolio average book value of \$5.1 billion. This is lower than the corresponding return in 2013-14, due largely to lower prevailing short term interest rates, but also as a result of the realisation of lower gains on disposal than in the previous financial year.

Losses or gains in the mark-to-market value of the portfolio change with prevailing conditions and therefore vary at any particular point in time. These are not realised returns and so are excluded from the accrual returns, but are included as re-measurements within the AOFM's comprehensive accounting treatment.

The RMBS securities held by the AOFM are valued using indicative 'bid' margins for secondary market trading as estimated by an independent valuation service provider. The cumulative unrealised gain on the portfolio was \$20 million as at the end of the financial year, a reduction of around \$12 million versus the year before. This reduction was due to a number of factors, including the reduction in both the size (through amortisation, and, to a lesser degree, sales) and average term to maturity of the portfolio, as well as the widening of revaluation spreads in line with the deterioration in credit conditions seen globally. The total return on the RMBS portfolio for 2014-15, including re-measurements, was around \$182.2 million, or approximately 3.54 per cent of the portfolio average book value.

Further information on the AOFM's investments in RMBS is available in Part 5 of this annual report.

## Investor relations

### Objective

The AOFM Investor Relations strategy in 2014-15 again focused on undertaking activities which encourage diversity in the investor base while maintaining and managing engagement with current key investors. Investor engagement recognises both the domestic and non-resident investor groups.

The strategy was developed further in 2014-15, this involving a more selective focus on the investor base as well as modifications to the engagement approach taken.



There were four parts to this strategy:

- A greater focus on investors from specific geographic regions, sector and type;
- A lesser (although still regular) use of direct face-to-face investor meetings;
- Presenting to bank sponsored conferences or speaking events which attract investors relevant to the AGS market; and
- enhanced uses of technology to engage with investors.

## Outcomes

The AOFM conducted fewer investor offshore roadshows this year. A similar number of large and regular conferences were again addressed by the AOFM. However a more select group of smaller events were also arranged and presented to this year as a substitute for a larger number of one-on-one meetings.

The AOFM has also engaged with a much wider spread of potential investors via a digital advertising campaign that was linked to roadshows in two targeted regions.

Although fewer investor roadshows were conducted this year, the number of face-to-face meetings were only slightly less than the year before at 117 (versus 124 for 2013-14). This was due to the greater focus on major financial centres such as Tokyo, London and Singapore where there is a very high concentration of AUD investors. Many of the investor institutions in these centres are already large, regular and long term investors in AGS however the greater pool of investors in these cities also allows for a widening number of potential investors that can be met and engaged with for the first time. For London and Tokyo in particular this includes investors with a developing interest in very long-dated AGS.

Specific regions or countries were again targeted as a part of the strategy to engage investors in locations that appeared to have a growing interest in AGS or were underweight AGS when compared to elsewhere.

Of the 117 face to face meetings undertaken this year, 40% were with accounts (47 institutions) which the AOFM had not met before. The majority of these institutions were not current although potential investors in AGS. This was an increase on the year before (34 from 124) and reflected the more targeted approach adopted in the strategy.

As well as face to face meetings and presentations, the AOFM conducted a number of phone meetings with international investors through-out the year. These were usually conducted when specific investors wished to engage in an update and they couldn't feasibly be included in upcoming roadshow plans.

The AOFM also conducted its second Australian Government Fixed Income Forum in Tokyo in June. The format was also slightly different from the first forum. Together with the AOFM CEO, the CEOs of the State Borrowing authorities of New South Wales, Victoria, Queensland and Western Australia also participated again. The Treasurers of the four major Australian banks and two Senior Managers from AMP Capital and Colonial First State Global Asset Management also participated.

Sixty four investors from 45 different institutions attended the event, compared with 33 institutions at the first forum. The increased number of attendees and positive feedback and comments received in an exit survey, suggests that this event would probably be well supported by Japanese investors in the future.

**Table 4: Summary of investor relations activities in 2014-15**

Activity	Details
Conferences, speaking engagements and investor roadshows	14 events.
Approximate total audience size: Large Presentations	420 attendees.
Individual meetings	117 investor meetings.
Hosted roundtable/small presentations	8 presentations with 66 attendees.
Individual cities visited	22 cities.
Two AOFM staff members travel on each overseas trip	CEO, Head Investor Relations, Director Financial Risk, Head Portfolio Strategy & Research, Senior Analyst, Investor Relations.
Hosting banks: Investor roadshows, conferences, roundtable	ANZ, Commonwealth Bank, Citi, Daiwa Securities, Deutsche Bank, Royal Bank of



discussions	Canada, UBS, Westpac.
Hosting banks at Australian Government Fixed Income Forum, Tokyo	ANZ, Citi, Commonwealth Bank, Daiwa Securities, Deutsche Bank, JP Morgan, NAB, Nomura, UBS, Westpac
Invited Institutions presenting at Australian Government Fixed Income Forum, Tokyo	NSW Treasury Corporation, Victorian Treasury Corporation, Queensland Treasury Corporation, Western Australian Treasury Corporation, AMP Capital, Colonial First State Global Asset Management, ANZ, Commonwealth Bank, NAB, Westpac.

## Public register of government borrowing

The *Guarantee of State and Territory Borrowing Appropriation Act 2009* requires the AOFM to publish a register recording the beneficial ownership, by country, of all CGS and any Australian State or Territory government securities guaranteed by the Commonwealth.

The Act does not contain any mechanisms to compel the provision of information to the AOFM by the beneficial owners of these securities or persons holding these securities on their behalf. Nominee and custodial services firms have not provided information to the AOFM due to their fiduciary and contractual obligations to clients. Many investors wish for their holdings to remain confidential for commercial reasons.

This situation limits the information available to the AOFM to form an opinion on the extent of beneficial ownership of the securities. Without detail on the country of beneficial ownership, information on the holdings of nominee/custodial firms alone provides a limited indicator of 'offshore' CGS ownership.

During 2014-15, the AOFM published the register each quarter and following the latest update, the register contains monthly data up to 30 June 2015. The register indicates that around \$380.4 billion of CGS, together with State and Territory securities guaranteed by the Commonwealth, were on issue at year end. Country of ownership could be identified for \$122.3 billion or 32.2 per cent, of which \$67.2 billion was identified as Australian and \$55.1 billion was recorded as held offshore. Country of beneficial ownership could not be identified for around \$258.0 billion or 67.8 per cent. Most of this unidentified component was held by nominee/custodial firms.

The Australian Bureau of Statistics (ABS) also collects and publishes information on the holdings of securities. The legal powers provided to the Australian Statistician enable the ABS to obtain information from nominee/custodial firms on security holdings; however, there are also set confidentiality requirements that can constrain how and to what extent the ABS publishes such information at the country specific level.

The quarterly ABS publication *5302.0 Balance of Payments and International Investment Position, Australia* indicates that 65.2 per cent of Commonwealth Government Securities were held by non-residents as at June 2015.<sup>[9]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftn9](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftn9))

The annual ABS publication *5352.0 International Investment Position, Australia* provides information on the country of domicile for portfolio investment in debt securities. This information covers a broader range of debt securities, issued in Australia and overseas, than that covered by the AOFM register (that is, State and Territory securities not guaranteed by the Commonwealth, as well as debt securities issued by financial intermediaries such as banks and those issued by companies).

The publication estimates that there was \$1,065.9 billion of this foreign portfolio investment in debt securities at 31 December 2014. The survey indicated the country of investor domicile breakdown as: the United States of America, \$278.3 billion; Belgium, \$220.1 billion; United Kingdom, \$178.2 billion; Japan, \$57 billion; Luxembourg, \$43.5 billion; Hong Kong, \$31.3 billion; Singapore, \$18.5 billion; Switzerland, \$17.3 billion; Malaysia, \$8.2 billion; Cayman Islands, \$6.1 billion; France, \$4.4 billion; Canada, \$4.1 billion; Netherlands, \$4.1 billion; Germany, \$3.6 billion; New Zealand, \$3.3 billion; Ireland, \$1 billion; Austria, \$0.7 billion; Papua New Guinea, \$0.3 billion and Fiji, \$0.2 billion. The remainder of holdings were attributed to international bond markets, were unspecified, or were not published for confidentiality reasons.

## Information technology operations

During 2014-15, AOFM moved to a shared services arrangement with the Treasury for all its information technology services with a Memorandum of Understanding (MOU) coming into effect on 1 July 2015. Under the MOU the Treasury provides AOFM with a secure, robust IT environment to support its business requirements. AOFM retains control over its core business specific applications.

## Enterprise risk

The AOFM's enterprise risk management (ERM) framework enables the AOFM to evaluate and monitor risks from an organisational perspective, and to provide relevant and timely information to the CEO, Executive Group and the Audit Committee in support of their governance and decision making roles.

The AOFM's enterprise risks are classified as follows:

- strategic risks are managed by the Executive Group and impact on the AOFM's medium to long term strategies;
- portfolio risks involved in debt issuance, investment and portfolio management are managed pursuant to the AOFM's financial risk management framework; and
- operational risks relate to business as usual activities of the AOFM, and generally arise when opportunities or failures present in relation to internal factors, such as business processes, and/or systems.

The AOFM manages risks subject to its risk appetite, and cognisant of its business context. The AOFM adheres to high ethical standards, which are reinforced by regular in house training and adherence to the Australian Public Service Code of Conduct.

Responsibility for risk and assurance activities resides with the Enterprise Risk and Assurance Group.

Key enterprise risk activities undertaken in 2014-15 included:

- participating in whole-of-government benchmarking via the Comcover Risk Management Benchmarking Programme, and using the results to inform the ERM framework and AOFM's risk maturity profile;
- aligning the business impact analysis process with the ERM methodology and business continuity better practice; and
- recalibration of the AOFM's risk criteria to reflect a moderate overall appetite for risk.

In 2014-15, PricewaterhouseCoopers (PwC) undertook an internal audit to assess the design and implementation of the AOFM's ERM and fraud control frameworks. The internal audit rated the frameworks as demonstrating a strong control environment, being sound in design, and aligned with better practice and current legislative requirements.

The ERM framework is supported by assurance activities (refer below).

## Assurance

The AOFM's compliance with external obligations and internal controls and procedures is monitored through a co-sourced arrangement, with in-house compliance activities complemented by the use of internal audit services.

During 2014-15, the AOFM implemented an assurance framework to provide structured assurance on the effective and/or efficient operation of its governance arrangements, risk management and internal control environment. The framework has been scaled to meet the needs of the AOFM and is modelled on better practice. Key assurance activities undertaken in 2014-15 included:

- framework reviews of enterprise risk management, fraud control, workforce planning, cash management processes and corporate performance reporting;
- project assurance for the AOFM's treasury system re-implementation;

- an internal assurance review of the AOFM's compliance with the Australian Government's Protective Security Policy Framework;
- reviews of the RMBS guiding principles and auction model;
- preparation of the annual report on compliance with the Public Governance, *Performance and Accountability Act 2013* (PGPA Act) and PGPA Rule 2014; and
- completion of an annual compliance assurance plan, with monthly reporting provided to the Executive Group and quarterly reporting provided to the Audit Committee.

Information derived from the ERM and assurance frameworks supports the CEO in meeting his obligations to maintain a sound system of risk management and internal control pursuant to the PGPA Act.

## Settlement operations

The AOFM operates in a low-volume, high-value settlement environment. The AOFM's settlement operations achieved the following during 2014-15 (all figures are face value unless otherwise stated):

- 2,066 trades totalling \$99.55 billion arising from issuance activities;
- \$60.28 billion of interest and principal payments on AGS;
- \$5.97 billion in repurchases of near-maturity AGS; and
- \$160.5 million (amortised face value) of RMBS sold by the AOFM at auction.

In 2014-15, the AOFM settled on time and in full all payment obligations resulting from its debt and investment management activities.

The AOFM also works to ensure that its counterparties settle in full and on time all administered receipts relating to AOFM's investment management activities. The AOFM did not need to seek compensation from its counterparties because of a failure to settle payment obligations in line with their contractual obligations.

The AOFM conducts its settlement operations (that is, the settlement of trades and execution of corporate actions relating to its debt and investment management activities) via the Austraclear system. The Settlements Team has in place a number of measures to ensure the continuation of settlements operations in the event of disruptions to systems, premises and personnel. One measure in place is the maintenance of a stand-in agreement for Austraclear with the RBA. The agreement enables the RBA to perform actions in Austraclear on behalf of the AOFM in the event that AOFM is unable to do so. The business continuity arrangements for settlement operations were tested during 2014-15.

## Transmutation facility

Trading of exchange-traded Australian Government Bonds ('eAGBs') commenced on the Australian Securities Exchange ('ASX') in May 2013, in the form of CHESS Depository Interests (CDIs). The creation of the eAGB market meant that there were two groups of retail investors holding Australian Government issued debt: eAGB investors and Australian Government Securities ('AGS') investors.

Upon the launch of eAGBs, AOFM advised that a facility was being developed to allow retail investors in AGS to exchange their holdings to eAGBs. The economic characteristics of an eAGB and its equivalent AGS line are identical. The process of converting an AGS to an eAGB is known as a transmutation.

There were a number of challenges in the development of this Facility. Specifically, no facility had ever been developed before in Australia allowing retail investors to exchange their holdings of a bond into a holding of CDIs.

A tax ruling was sought from the Australian Tax Office (ATO) specifically to find out whether the transmutation process would constitute a tax event under the *Income Tax Assessment Act 1997*. In July 2014, the ATO ruled that the process of transmutation would not give rise to a tax event for certain investors.

An Offer was made to all investors registered on the Inscribed Stock Register holding of AGS as at the Offer Date in February 2015. Participation in the Offer was invited on a voluntary basis. Investors who participated in the Offer did not incur any fees, commission or other costs in order to exchange their holdings.

If an investor chose to participate, they were not required to exchange their entire holdings of AGS into eAGBs. Instead, investors with multiple AGS lines could elect the lines of stock they wanted to exchange. Stock nominated for exchange, investors were required to exchange their entire holding of that line. AGS stock nominated for exchange was converted into the equivalent eAGB line. Furthermore, the exchange took place on a one-for-one basis; that is, an investor holding \$10,000 face value of an AGS line would receive \$10,000 face value of the equivalent eAGB line (or 100 units, with one unit equalling \$100 face value). In the end, 139 lines of AGS (over \$10 million face value) were exchanged for the equivalent eAGB line.

There were a range of benefits to be obtained through exchanging their AGS holdings for eAGBs. eAGB investors are able to buy or sell as little as one unit at a time (\$100 face value) of eAGBs via the ASX's electronic trading platform where buyers and sellers can have their orders executed. Market makers are required to continuously quote buy and sell prices for all eAGB lines (although market makers are not required to provide prices during certain periods including when the wholesale market is closed or during important data releases). Prices are required to be in line with prices in the wholesale AGS market.

eAGB investors have access to an online investor centre provided by Computershare (who were appointed by the AOFM as the Registrar) facilitating fast and secure access to information about their holdings and enables investors certain information pertaining to their holdings to be updated.

The full range of AGS lines currently on issue can be purchased as eAGBs by retail investors in small or large parcels. All future AGS lines issued by the Australian Government will also be available for purchase as eAGBs.

## Cooperation with other debt managers

In 2014-15 the AOFM continued to support the debt management activities of the Papua New Guinea and the Solomon Islands governments with a particular focus on capacity development. One staff member is seconded to each of these countries to help develop cash and debt management capabilities.

The sharing of information and perspectives with other sovereign debt managers has contributed positively to the AOFM's knowledge and in particular has enhanced the AOFM's portfolio research program.

## Agency financial performance

The AOFM recorded an operating surplus on agency activities of \$2.19 million for the 2014-15 financial year, comprising total revenue of \$12.34 million and expenses of \$10.15 million. The surplus in 2014-15 was largely due to lower than anticipated operating costs.

As at 30 June 2015, the AOFM was in a sound net worth and liquidity position, reporting net assets of \$28.02 million, represented by assets of \$30.66 million and liabilities of \$2.64 million.

As at 30 June 2015, the AOFM had unspent appropriations totalling \$28.74 million of which \$0.10 million was held in cash. Unspent appropriations are available to settle liabilities as and when they fall due and for future asset replacements and improvements.

<sup>[1]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftnref1](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftnref1)) Source: Australian Securities Exchange.

<sup>[2]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftnref2](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftnref2)) The Official Public Account is the collective term for the Core Bank Accounts maintained at the RBA for Australian Government cash balance management.

<sup>[3]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftnref3](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftnref3)) The overdraft facility is more costly than equivalent short-term borrowing (for example, issuance of Treasury Notes). The terms of the facility provide that it is to cover only temporary shortfalls of cash and is to be used infrequently and, in

general, only to cover unexpected events.

<sup>[4]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftnref4](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftnref4)) Defined as 8.5 years or longer. The demarcation at this point reflects the typical term of the shortest bond in the ten year Treasury Bond futures basket.

<sup>[5]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftnref5](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftnref5)) Debt servicing cost includes net interest expenses (measured on an accruals basis and includes realised gains and losses on the disposal of assets or liabilities) plus foreign exchange revaluation gains and losses (now minimal). Unrealised changes in the market valuation of domestic debt and assets are not part of this measure.

<sup>[6]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftnref6](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftnref6)) Bond issuance over the past three financial years for instance accounts for around ¾ of the LTDP as at 30 June 2015. Bond yields over this period were on average significantly lower than the preceding years which largely explains why portfolio funding costs have fallen by more than the 10 year bond yield moving average.

<sup>[7]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftnref7](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftnref7)) Additional information on the impact of re-measurements on the RMBS portfolio can be found in the Performance section under 'Residential Mortgage-Backed Securities'.

<sup>[8]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftnref8](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftnref8)) Full details of each Direction are available on the AOFM website. Note that some sponsors underwent name changes over the relevant period.

<sup>[9]</sup> ([https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#\\_ftnref9](https://aofm.tspace.gov.au/wp-admin/post.php?post=28506&action=edit#_ftnref9)) Note this does not cover Commonwealth guaranteed securities issued by the State and Territory governments under the Act.

Last updated: 28 January 2016

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← Part 1: AOFM Overview (<http://aofm.gov.au/publications/annual-reports/annual-report-2014-15-2/part-1-aofm-overview/>)

Part 3: Management and Accountability →  
(<http://aofm.gov.au/publications/annual-reports/annual-report-2014-15-2/part-3-management-and-accountability/>)

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