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Future Fund assets up to $123b after strong fourth quarter

The fund's David Neal (left) and Peter Costello. The fund delivered a 4.8 per cent return over the financial year.
Wayne Taylor

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by **Jonathan Shapiro**

The Future Fund is shifting more of its $123 billion portfolio into private investments as ultra low interest rates reduce returns and raise risks in public equity and bond markets.

On Tuesday, Australia's sovereign wealth fund announced a strong 4.6 per cent quarterly performance to increase its assets to $123 billion, which managing director David Neal said was boosted by successful investments in non-listed businesses

"Private markets is an area where we continue to put a lot of focus," said Mr Neal. He explained the fund was looking to move "away from relying on market returns which are likely to be subdued [in favour] of genuine skill based opportunistic returns".

Mr Neal said markets had "broadly reflected the overarching story line" of the fund with equity market returns "lacklustre" over the past financial year. But improved market conditions helped boost portfolio returns in the final quarter of the financial year.

The fund's annual return of 4.8 per cent fell short of its 5.5 per cent return target. But over the decade the fund's annualised return of 7.7 per cent was ahead of the 6.9 per cent target as it reported its first 10-year performance figures. The fund was created in May 2006 to help the government meet its unfunded pension liabilities with $60.5 billion of capital.

The Future Fund's cash hoard fell slightly, by $185 million, but at $26.7 billion still accounts for more than a fifth of all assets.

Focus on venture capital

Holdings in alternative investments, the fund's largest asset class exposure outside of cash, and private equity increased by a combined $3.2 billion. Exposure to equities also increased by $1.2 billion, while debt securities exposure increased by $900 million.

The fund had increased its focus on venture capital and early stage growth investments to take part of the "innovation wave across technology and the disruption that is creating" and had invested in private lenders who are filling the void left by hamstrung banks.

The Future Fund has now doubled its weighting to private equity from 5 to 10 per cent over the past five years. The amount invested in the asset class has more than tripled in that period from $3.8 billion to $12.8 billion.

But as the fund has increased its allocations to private equity, it has fought hard to ensure the fees and interests of private equity managers are adequately aligned.

"[We have] worked hard to make sure the fee arrangements are as aligned as we can get them, and have rejected many private equity funds and others on the basis of their terms and conditions which don't meet our standards," Mr Neal said.

Cautious outlook

The fund had retained its cautious outlook that risks are elevated, he said, which meant it would take risks selectively and would work closely with its global networks to "seek out and access pockets of opportunity particularly in our private market and alternatives programs".

The fund says it seeks to maintain an "equivalent equity exposure"' – or sensitivity to global equity markets – of between 40 and 60 per cent of assets, with the current weighting slightly below 50 per cent. That is down from a peak of 60 per cent in December 2014.

Mr Neal said the fund was concerned that low monetary policy settings meant that not only were prospective returns low, but that central banks were ill-equipped to respond to another crisis.

"Monetary policy has been extraordinary for an extended period of time to address that, and growth has been tepid while inflation has been non-existent."

"The limited firepower is what we worry about when we look in the future," Mr Neal said.