Investment and Financial Services Association 24th May 2007

Media Release

"Ready, Willing and Able"

Funds management export push begins

IFSA has released *'Policy options to increase Australia's export of funds management services',* a comprehensive policy paper that outlines future directions for the Australian financial services industry and which provides a 2020 vision to take the Australian economy beyond the resources boom.

"Australia's service industries contribute over 73% of GDP, employ 80% of the workforce and yet make up only 22% of exports. As a global leader in funds management services, Australia's reputation and growth in this sector has largely been driven by domestic opportunities, yet real potential exists to develop a substantial export market in this area", said IFSA CEO, Richard Gilbert.

"In releasing this document today, IFSA is effectively saying that the time has come for a more concerted effort by the industry and government to export our financial services capability. As an industry, we are ready, willing and able to work with government, regulators and other agencies to achieve this outcome.

"Australia's fund managers are well positioned to meet the growing demand for products, services and expertise coming from the Asian region and beyond- representing a substantial additional export opportunity for the nation.

"Costs associated with exploiting these opportunities will be minimal as much of the requisite infrastructure is already in place. Therefore, the challenge for foreign policy makers is to re-position funds management as a central platform in all WTO trade negotiations and multi-lateral and bi-lateral trade agreement negotiations.

"Financial services represents 7.2% of GDP and is the third largest sector in the Australian economy, the largest managed investment asset pool in Asia and the fourth largest managed funds market in the world.

"Our sector is asking for a 'hand up' in exploiting our export potential- not a 'hand out'. We want to play a more prominent role as an exporter so that our funds management capability and associated services can become one of the growth engines for the maintenance and enhancement of Australia's economic prosperity for future generations.

"This policy paper is a road-map and contains a number of eminently achievable objectives to facilitate the future export of Australian financial services. IFSA is a willing partner in the policy development process and we look forward to discussing these proposals with our elected representatives in the near future", Mr Gilbert concluded.

A copy of *'Policy options to increase Australia's export of funds management services'* is available on the IFSA website: www.ifsa.com.au

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IFSA represents the retail and wholesale superannuation, funds management

Investment and Financial Services Association Limited

Policy options to increase Australia's export of funds management services – May 2007

Australia's service industries contribute over 70% to GDP yet make up only 23% of exports. As a global leader in funds management services, Australia's reputation and growth in this sector has largely been driven by domestic opportunities.

This paper outlines the potential Australia has to accelerate the development of our export opportunities in funds management, making the most of one of the country's greatest assets and contributing to the ongoing employment opportunities for Australians and the growth of the Australian economy.

IFSA is the national not-for-profit organisation which represents the retail and wholesale funds management, superannuation and life insurance industries. IFSA has over 140 members who are responsible for investing over A$950 billion on behalf of more than ten million Australians. Australia has the fourth largest managed investments pool in the world and the largest in the Asian region.

Contents

Policy partnership – industry and government

One of the major challenges for Australian policy makers over the next decade will be to further the development of sustainable industry and employment opportunities that underpin the economic security and stability of Australia for future generations.

The international trade in goods and services is vital to the Australian economy. The Department of Foreign Affairs and Trade estimates that one fifth of all jobs in Australia are either directly or indirectly linked to exports - this increases to a quarter in regional and rural Australia. In the last ten years, Australia's export industries have created more than 250,000 jobs and currently provide approximately 20% of Australia's Gross Domestic Product (GDP).

Agriculture, resources and manufacturing continue to serve Australians well. However it is important to look beyond Australia's traditional export commodities, to position the nation well for any abrupt or subtle changes to:

- The global appetite for resources, or a change in pricing driven by competitive market pressure;
- The possibility of sustained periods of drought, or any further loss of competitiveness in the global agricultural products market due to continued subsidies and stalling of World Trade Organisation (WTO) negotiations on agriculture; and/or
- Australia's competitiveness in manufacturing sales to foreign markets resulting from the continued emergence of lower cost producers.

Australia's economy is now a service based one, with Axiss Australia data showing that service industries account for 73% of total gross value added and employ about 80% of the workforce.

In contrast, services only make up 22% of exports according to data from the Australian Bureau of Statistics (ABS), falling far behind resources such as agriculture and mining. By comparison, agriculture comprises around 2% of economy and 17% exports; mining comprises 5% of the economy and approximately 40% of exports.

As the third largest sector in Australia's economy, the financial sector contributes 7.2% or A$68 billion of GDP, almost as much as the agriculture, forestry, fishing and mining sectors combined.

The funds management sector is a significant asset to Australia's economy and is already a significant exporter of its services. Many of our domestic companies have developed a substantial position in the Asian region and beyond. Global financial services companies which have entered this market in the last two decades are also very comfortable using Australia as a platform for exporting funds management capability and services into the Asian region. However, those companies which have already extended their market reach into the region, feel that the rapid rate of growth in the region offers Australia more potential than has yet been realised.

It is IFSA's view that Australia's fund managers are well positioned to meet the growing demand for products, services and expertise coming from the Asian region and beyond, and that this represents a substantial additional export opportunity for the nation. Importantly any costs associated with exploiting these opportunities will be minimal as much of the requisite infrastructure is already in place.

In his speech in Singapore on 17th September 2006, the Treasurer, the Hon. Peter Costello, highlighted that the flow of international capital trebled between 1995 and 2005, demonstrating the ongoing integration of financial markets. He remarked that such flows 'can be a powerful force for the development and growth of economies. They provide resources, enhance access to technology and management skill, and lower costs by improving competitiveness'.

IFSA believes that cross-border flows will continue to increase at a greater pace over the next decade, as emerging markets such as China and India display a greater appetite for capital and encouragement of foreign investment opportunities. Diversification and the global shift to defined contribution pension policy will ensure that much of the cross-border flows will be via collective investment schemes or managed investment products.

At the end of 2006, data from the Investment Company Institute in the US (ICI) and country industry associations, suggested that there was in excess of A$1.9 trillion in funds under management within managed investment type products in Asia, excluding Australia.

It is estimated by global research house, Cerulli Associates, that the growth of the Asian market in this sector will continue at 14% per annum, exceeding that of both Europe and North America. With many countries within this region in varying stages of development, we are seeing them look to North America, Europe and Australia for leadership, know-how, human resources and support services.

Our industry is considered by most international financial services leaders as one of the most advanced in the world, with a high degree of integrity in our regulation and operational management. Australian companies are innovative in fund and product design, for example in infrastructure funding, property trusts, financial planning, investment platforms, hedge funds and retirement savings.

Australia's retail funds management market has been described by Cerulli as "the most sophisticated retail fund management marketplace outside of the US". A recent report by Boston Consulting Group (BCG) said that Australia is home to the world's fastest growing high-net-worth investor market.

Australia's managed investment asset pool is the largest in Asia and the fourth largest in the world, as shown by Axiss Australia's analysis. Diversification and the search for returns means that Australian fund managers are experienced managers of global portfolios with Chant West's December 2006 Multi-Manager Survey showing that 38% of our domestic funds are invested offshore.

Australia is politically stable, with a sound and resilient economy and is often seen to be a safe haven as well as a sensible strategic investment. The workforce is highly skilled and educated with more people working in the sector than in Hong Kong and Singapore combined. More than 850,000 Australians speak an Asian language. Australian executives with financial credentials and experience are highly sought after in this region and around the world.

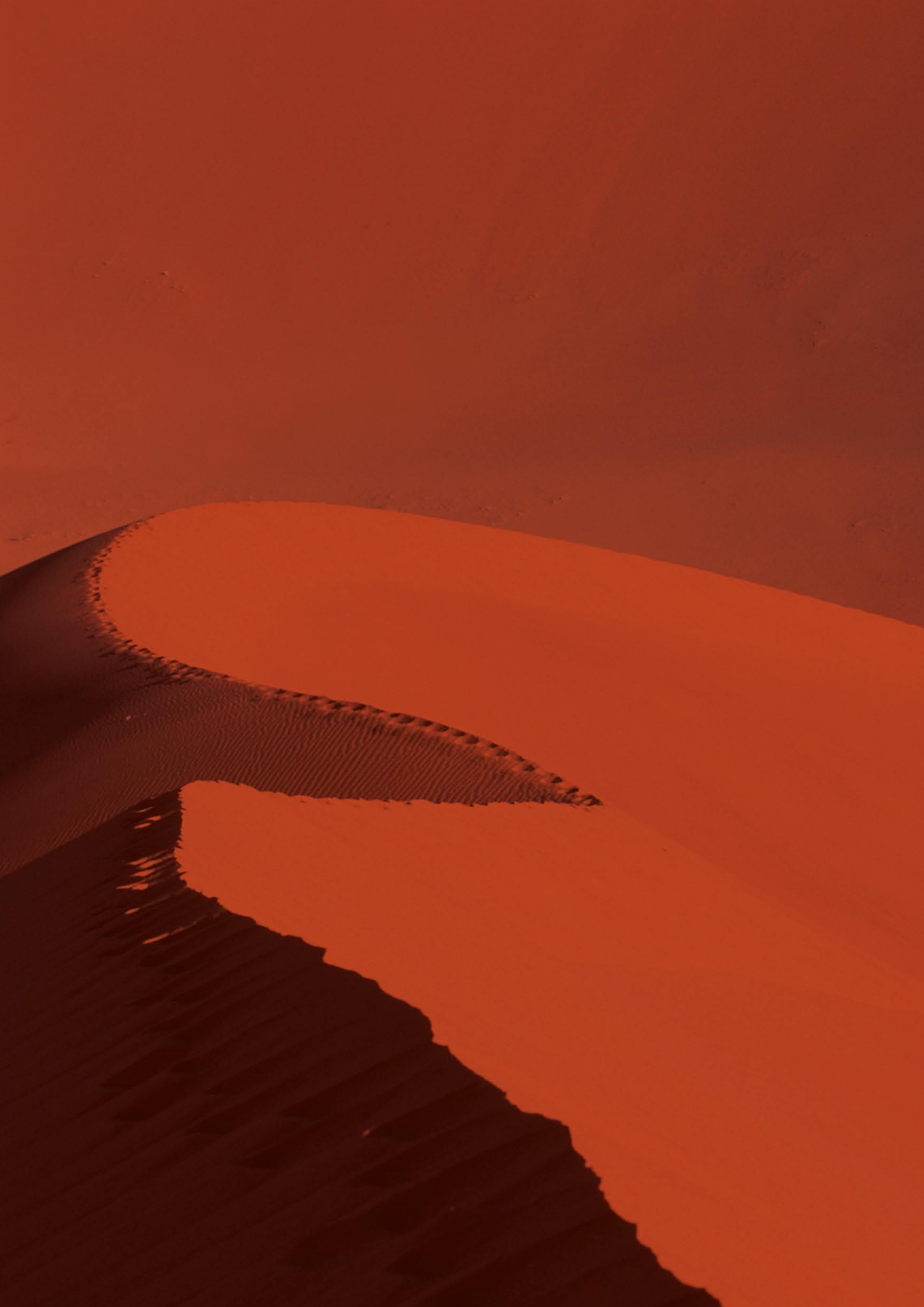
Australia is well positioned, due to experience, expertise, existing infrastructure and geography, to become the funds management hub for the Asian region. Successfully positioning Australia in this way will deliver significant positive economic benefit to Australia.

To leverage this opportunity, IFSA would welcome a partnership approach between government and industry to develop policy, prioritise the action needed and mitigate the risks. If appropriate, we would be delighted to commit IFSA and member company resources to facilitating a broad ranging inquiry to help Australia realise its potential and make the most of the assets we have. We hope to engage with government on this challenge and assist in the development of the terms of reference.

We look forward to working with government and other stakeholders in 2007 and beyond.

Richard Gilbert

IFSA Chief Executive Officer



IFSA's vision for 2020

- Australia will be the funds management hub for the Asian region. As a result of our position, the export of funds management capability and associated services will become one of the growth engines for the maintenance and enhancement of Australia's economic prosperity for future generations.

- Australian fund managers will have an enviable reputation for their expertise in managing global portfolios. They will benefit from competing with the best in the world domestically and globally.

- Australian suppliers to the funds management industry will be competitive and considered as a 'must include' in the consultation and tender process for Asian and other pension and investment funds when seeking administration, custodial and supporting services, including legal, actuarial and accounting services.

- Funds management will become a central platform in all WTO trade negotiations and multi-lateral and bi-lateral trade agreement negotiations.

- The Australian funds management industry will continue to be recognised as being one of the most innovative in the world, along with its reputation for transparency, integrity and efficiency.

- Australian universities and tertiary education institutions will continue to enhance their reputation for the delivery of the 'world's best' education and training courses for financial services, delivered in Australia and offshore.

- Next generation Australians will continue to be sought after by the financial service industry in Australia and offshore. Those with offshore experience will keenly repatriate to further build Australia's position in the global funds market.

- Domestic employment growth in semi-skilled and highly skilled roles in the financial services sector will continue to outperform other sectors.

Policy options

The following policy areas should be focused upon in order to assist Australia in positioning the funds management industry to meet increasing international demand for its services. These proposals, if adopted, would underpin the importance of exporting Australia's capability and secure the sustainability of this market over the long term.

Regulation

Reform to the Australian financial services sector over the last two decades has resulted in the funds management sector being regarded as a leader in terms of retirement savings and market conduct measures. We are now well respected globally for market integrity, efficiency and innovation.

Australia should take a more proactive approach to the harmonisation of licensing and market conduct standards across the region. We should work with foreign jurisdictions to actively pursue and support mutual recognition.

Proposal

- That the industry, government and regulators pro-actively address cross-border licensing issues and seek opportunities to take a leadership position on the harmonisation of regulation relating to market access and market conduct.

Taxation environment

It is vital that Australia's tax regime is globally competitive, as tax is a fundamental aspect of attracting and maintaining foreign capital, as well as exporting funds management services to offshore clients. Most significantly, Australia's tax laws should be responsive to developments in the global market because, as acknowledged by the Board of Taxation, "*…the competitive environment is not static.*"

Most Australian managed funds are widely-held unit trusts that distribute their income fully, and offer portfolio investments across local and overseas assets (equities, property and bonds). They are taxed on a flow-through basis, providing the ultimate beneficiary with tax treatment comparable to direct investment, but with lower tax reporting and compliance requirements. These features make them an attractive tax regime.

At both a retail and wholesale level, they are used by offshore portfolio investors who may include large institutional investors, pension funds, fund managers and global custodians. Alongside management expertise and innovative products, offshore investors are looking for tax administration that is accurate and timely, allowing them to pass on distributions quickly to their own investors.

Regardless of our many advantages, it is also important for Australia to acknowledge the need to be competitive on tax rates in order to attract and maintain offshore clients. Many of our regional competitors recognise the value of the international trade in funds management services, and have introduced more competitive withholding tax rates on distributions to non-resident investors.

Australian fund managers who invest money on behalf of both domestic and offshore clients seek to take advantage of new products and markets offshore, such as the growth of real estate investment trusts (REITs) in Asia and the UK. However, they are often constrained in their choices, despite the fact that tax complexity should not be the key driver of investment decisions.

Proposals

- That the Managed Investment Tax Regime (MITR), as advocated by IFSA in 2006, is adopted. It is intended to be revenue neutral, and will provide Australian fund managers with certainty and minimise their current compliance burden [Appendix 1].
- That a flat and final withholding tax is introduced on the non-dividend, non-interest Australian source income component of distributions, at a competitive rate of 12.5%.
- That the current rules relating to the source of particular classes of income be reviewed to ensure simple and consistent tax treatment for investors in Australian managed funds.

Measuring the impact on the economy

To date, obtaining an appreciation of how the service sector contributes to the economy has been of relatively low importance, particularly in sectors other than tourism and education. Over time, the export of services has become an increasingly important aspect of global trade and has become the main export initiative of economies such as the UK, US, Republic of Ireland, Hong Kong and Singapore.

The Australian Services Roundtable estimate that the official data on services exported, as measured by the Balance of Payments, measures less than one third of Australia's actual exports of services. This is in part because the contribution of services to the export of goods is often overlooked and the fact that official Australian Bureau of Statistics (ABS) export data only covers a handful of very broad service categories (one of which is financial services), leaving a number of types of services exports un-assessed.

The ABS produces the *Managed Funds, Australia Catalogue* which is specifically devoted to the managed funds industry. This catalogue is a good source of information on the industry as it trades within Australia but does not contain data on the export or import of funds management services.

Proposals

- That data collected on the export of services is reviewed in line with the issues identified in the Australian Services Roundtable's submission to the House Standing Committee on Economics, Finance and Public Administration Inquiry into the current and future directions of Australia's service industries [Appendix 2].
- That industry and government adopt a partnership approach to establish a system for the collection and dissemination of data that allows the development of the funds management industry to be accurately tracked over time.
- That the ABS be resourced sufficiently to enable it to establish a programme to conduct research into the funds management sector and allowing it to work constructively with the industry over the long term.

WTO and trade agreements

To date, financial services, and funds management specifically, have been a low order priority to those negotiating multi-lateral and bi-lateral trade agreements. This needs to be changed to ensure that Australia is better placed to leverage our existing capability and also ensure that we maintain the market conduct standards that we have worked hard to establish and need to protect.

Australia should also attach a higher priority to the continued liberalisation of financial services within its WTO trade negotiations. This will position Australia well to benefit from cross-border capital flows and associated services.

Proposal

- That greater consideration is given to the contribution that funds management services can make to the economy and that improved market access is a foundation for all future and renegotiated agreements.

Marketing Australia's capability

Australia's credentials in funds management services and as a financial market could be better promoted within our region and more broadly. Over the last decade we have established improved credibility with those that have had reason to deal with the Australian system. More recently we have noted that there has been an increased interest in the Australian superannuation system and regulatory framework from the Asian region and further afield.

Proposals

- That Axiss Australia is sufficiently resourced and their role is formalised to give them specific responsibility for the development and promotion of outbound trade opportunities in financial services.
- That the Department of Foreign Affairs and Trade (DFAT) is sufficiently resourced to leverage existing networks in promoting Australian funds management services, and is able to assist in the development of cross-border trade opportunities for this sector, working more closely with Axiss Australia towards this goal.

Educating for the future

The majority of today's students will be employed in the services sector, either in Australia or offshore. Many of the more highly skilled roles will be provided by the financial services sector, where the average earnings are 26% higher than the national average and many of those with funds management experience will be sought after to work in markets in Europe, Asia and the US.

It will be important, for the future growth of the industry and the economy, for Australia to continue to build our expertise and reputation in this area.

Proposals

- That a review of our secondary and tertiary education system is undertaken to ensure that we are giving adequate opportunities to next generation Australians seeking a career in financial services.
- That the financial services industry, the education sector and government work jointly to develop targeted initiatives, leverage shared networks and promote Australia's excellence in financial services education, particularly in the Asian region.
- Australia's prominent position in the Asian funds management landscape will deliver significant economic and ancillary benefits. Government revenue resulting from Australia's increasing involvement in the global funds management industry will grow at more than double the rate of other market sectors, whilst culturally, Australia will benefit from closer alignment with our neighbours in Asia.

Global trends in funds management

Size and growth of global funds under management

The United Nations paper on the Globalisation of Capital Markets estimated that the volume of mobile capital trebled in the three years to 2000.

Extract 1:

'Capital markets are in the process of rapid evolution. Electronic computerised data transmission now gives unprecedented mobility to all the financial markets on the planet. Moreover, the volume of such flows has grown — tripling or increasing tenfold in the past few years — mainly as a result of the success of mutual funds [managed investments], whose assets often exceed those of many governments.'

United Nations paper on
The Globalisation of Capital Markets.
February 2001

According to International Financial Services London (IFSL), global funds held across managed investments, pensions and insurance companies was in excess of A$71 trillion in 2005, an increase of 54% over three years.

ICI data shows that assets held specifically in global managed investment style products increased by 50% in the last five years and that Australia now has the largest pool of managed investment assets in Asia and the fourth largest in the world, as demonstrated by Table 1.

Table 1: Value of assets in managed investments at year end

Country	2001 A$ millions	2006 A$ millions	Annual Growth %
USA	8,396,428	12,535,954	10
Luxembourg	913,350	2,634,258	38
France	858,767	2,129,840	30
Australia	**402,090**	**1,040,393**	**32**
UK	381,247	946,793	30
Ireland	230,938	923,944	60
Hong Kong	204,735	759,666	54
Japan	413,997	696,862	14
Singapore	219,503	572,518	32
Korea	143,781	303,274	22
China	13,014	79,995	103
India	18,399	70,084	56
Taiwan	59,880	66,896	2
New Zealand	7,902	15,519	19
Philippines	254	1,859	126
Global	**14,262,692**	**26,853,201**	**18**

Source: ICI - Fact Book 2007. Singapore data sourced from Monetary Authority of Singapore, China data sourced from KPMG. All values converted to Australian Dollars on 8th May 2007.

Regional growth

With more than A$1.9 trillion of funds under management in Asia (excluding Australia), the region has shown the strongest growth in recent years, and most analysts agree this trend is set to continue.

Cerulli Associates have predicted that the region's managed investments will experience growth in assets of 14% per annum over the next few years, outstripping the growth rates they foresee in Europe and North America.

According to Cerulli, China's mutual fund assets are set to increase by 60% and India's by 70% in the five years to 2010. The size of these economies, their population and the will to secure the future of ageing populations, will ensure that such growth is sustainable over the long term. Charts 1 and 2 show Cerulli's projections for growth in China and India's managed investment assets.

Chart 1: China, projected investment management assets under management (AUM) through 2010E (RMB billions)

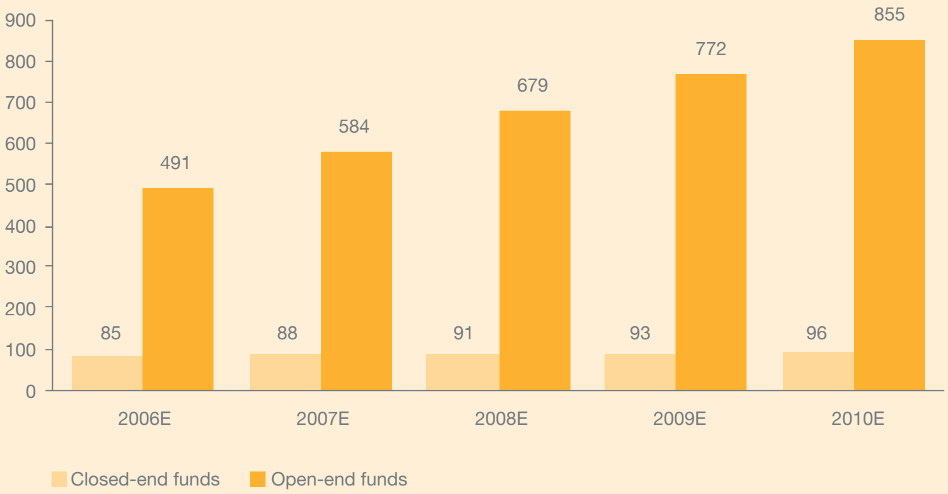
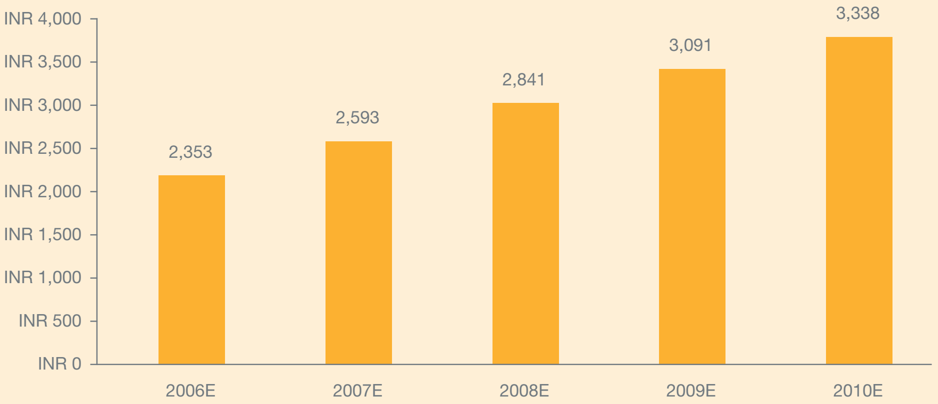


Chart 2: India, projected investment management assets under management (AUM) through 2010E (Rs billions)



Source: Cerulli Associates presentation in June 2006.

Global trends in funds management - continued

The contest for funds management services

Mercer Investment Consulting, who assist institutional investors around the world to search for funds management expertise, show the growing trend for Asian markets to seek global equity management expertise in their *2005 Global Search Activity Report*: 'There was increased interest in global equity mandates, which represented 36.4% of searches, up from 9.3% in 2005. Global equity accounted for nearly one third (31.2%) of total placements for Asia, rising from just 1.0% in the previous year.' This compares to just 21% placed in global equity, by the rest of the world.

The Australian industry has significant skills in international portfolio management. Given the industry's potential to become the region's funds management hub, it would be possible for Australia to attract global clients, investing in global assets and global strategies, managing, trading and providing custody services, all from Australia.

The markets in the Asian region are going through regulatory reform similar to that of Australia over the last two decades. In facing such growth challenges, they are seeking public policy guidance and other services such as legal, actuarial, fund administration and accounting, portfolio and product development.

Such growth means that many countries are positioning themselves to provide funds management and ancillary services to the global funds management industry, for example, Ireland, Luxembourg, Hong Kong, Singapore, Dubai and others. Australia has the capability, expertise and proximity to match these competitors.

The contest for funds management flows

Australia has a funds flow trade deficit in managed investments. This compares poorly when benchmarked against the US and the UK as illustrated in Table 2 below:

Table 2: The trade balance in managed investment US, UK and Australia

Country	Value of funds flowing into managed investments from offshore A$ billion	Value of funds flowing to foreign markets through managed investments A$ billion	Trade balance A$ billion
US	2,453	931	1,522 Surplus
UK	3,508	3,294	214 Surplus
Australia	42	231	**189 Deficit**

Source: 2006 ICI Fact Book.
ONS - 2006 Pink Book, Chapter 1, table 1.3 – portfolio investments.
ABS – Managed Funds Australia report September 2006.
All values were converted to Australian Dollars on 8th January 2007.

Considering the strength of the Australian economy, the stability of our financial markets as well as the experience of Australian funds managers, this imbalance in funds flows indicates the scale of the opportunity for Australia.

Further data from Mercer Investment Consulting suggests that only 0.6% of capital being managed through global funds managers is being placed in Australian Equity. This compares to almost 10% being placed in US Equity.

Developing Australia's potential as a regional funds management hub will not only assist the industry to export its services, but also put Australia on the world map as a home for managed investment capital.

Table 3: Extract from 2005 Global Search Activity Report, Mercer Investment Consulting.

Asset Class	Amount placed	
	A$ million	% of Total
International Equity, Balanced and Fixed Income	29,167	29.9
Europe Equity, Balanced	7,904	8.1
US Equity and Fixed Income	17,643	18.1
UK Equity, Balanced and Fixed Income	16,201	16.6
Canadian Equity, Balanced and Fixed Income	5,020	5.2
Property	2,146	2.2
Private Equity Fund of Funds	1,531	1.6
Hedge Fund of Funds	960	1.0
Alternatives	2,109	2.2
Emerging Markets Equity	2,868	2.9
Asia Pacific ex Japan	2,019	2.1
Other	9,231	9.5
Australia Equity	**614**	**0.6**
Total	**97,414**	**100**

Source: Mercer Investment Consulting, May 2006. All values were converted to Australian Dollars on 8th January 2007.

What has Australia got to offer?

Strength of the domestic industry

With just 50 years of history, Australia boasts one of the largest, fastest growing and most advanced funds management markets in the world.

Underpinned by Australia's retirement income policy, informed investor base and innovative investment products, Australia has become the fourth largest managed investment market in the world and the largest in the Asia-Pacific. Rice Warner Actuaries estimated that the market will grow by 130% in the next 10 years.

Australia's economic and industry record

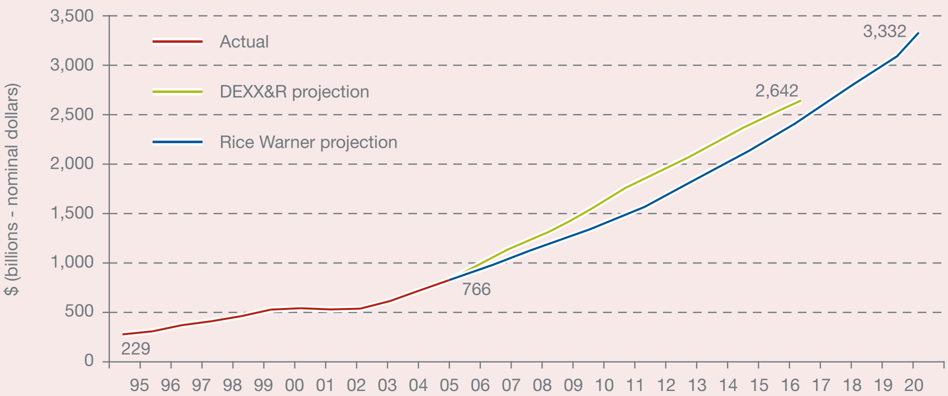
Australia's economy ranks in the top 15 in the world. It continues to be one of the strongest performing economies, with an average annual GDP growth rate of 3.6 per cent from 1996 to 2006.

The scale of the investment management industry, along with others in the financial sector, has contributed to the success of Australia's economy. As the third largest sector in Australia's economy, the financial sector contributes 7.2% or A$68 billion of GDP. In terms of output, the sector is growing more than 40% faster than nominal GDP. The finance sector is almost the same size as the agriculture, forestry, fishing and mining sectors combined. Its scale alone justifies commensurate political and trade development attention.

The size of the market has led to the development of home-grown talent as well as attracting many global funds management companies to Australia – improving competition, enhancing the talent pool and creating significant innovations. The innovations developed here are now being adopted in Europe and elsewhere and, with 38% of Australia's funds under management being invested offshore, Australia's funds managers are already recognised for their experience in managing global portfolios.

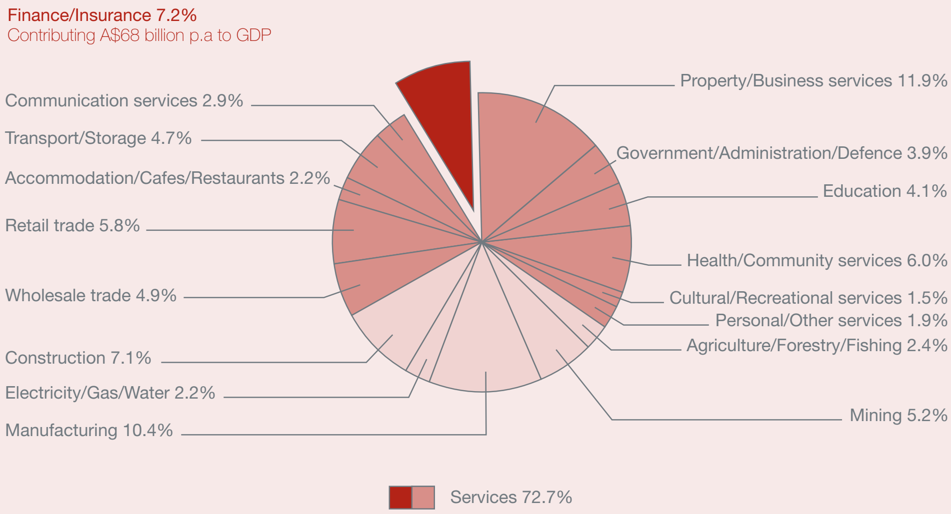
We have a highly skilled and multilingual workforce with 15.3% of the total labour force currently working in the financial service sector and related services. Of those currently enrolled in university, 27.5% are undertaking a business related course. Of the 350,000 employed in the financial services sector, 37.6% are tertiary qualified, the third highest of all industry sectors and significantly higher than the industry average of 23%.

Chart 3: Actual and projected superannuation assets 1995 - 2020



Source: APRA, ABS, Rice Warner and DEXX&R

Chart 4: Australia's real gross value added by industry – December Quarter 2006



Source: ABS, 5206.0 Australian National Accounts: National Income, Expenditure and Product, Dec Qtr 2006

The regulatory framework

Australia is very well regarded for its overarching financial services regulatory framework. This reputation reflects, to a large extent, the significant structural changes to regulatory arrangements enacted in 1997, following the Financial Systems Inquiry. Key among the developments to date has been the introduction of the Managed Investments Act (MIA).

The MIA enables a single entity to have overall responsibility for each managed investment scheme. It provides a clear framework for funds managers and investors, simplifying the investment process and the legal obligations of scheme operators.

Further reforms in the Financial Services Reform Act (FSRA) in 2002 cemented the reputation of Australia's financial services industry as being among the most efficiently regulated in the world. These reforms also ensure the industry provides a high level of consumer protection.

Australian political and legal institutions are recognised globally for their transparency, impartiality and robustness, providing a relatively safe and secure investment environment.

The right time zone

One of the world's largest funds management companies, with a base in Sydney, estimates that 15% of financial market activity occurs when the US and UK markets are closed. This suggests that there is scope for the development of a global fund hub in the Asian time zone. Such a hub would not only provide a service to those in the region but also provide European and US companies with the ability to conduct continuous running of their operational systems.

Quality of life

As highlighted by a recent *International Living* survey, the quality of life experienced by Australians is the envy of the world. Axiss Australia pin points 'Australia's climate, recreational facilities, access to healthcare, natural environment, business and political stability, cost of living and overall life style' as being powerful attractions for a skilled workforce and globally-focused companies.

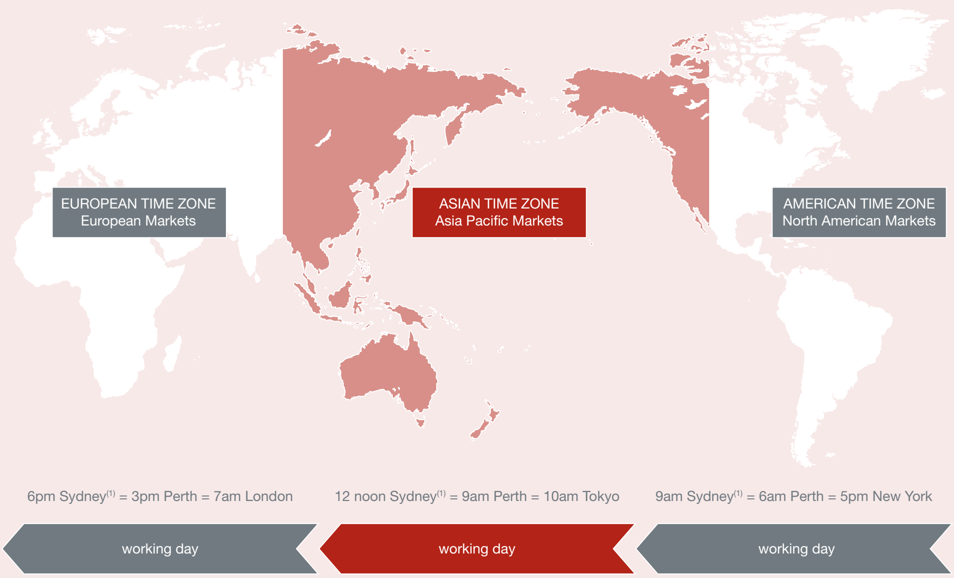
Globally competitive funds managers

Funds management is becoming an increasingly important feature of the financial services industry with almost 80 per cent of the assets of managed funds placed with specialist managers.

IFSA has over 90 funds management companies as members, just under half of which are global leaders. The openness and integrity of the market, as well as the mandated superannuation system, has proved attractive to such companies.

Australian companies are innovative in fund and product design, for example in infrastructure funding, property trusts, financial planning, investment platforms, hedge funds and retirement savings. Australia is a world leader in Real Estate Investment Trusts (REITs) and Infrastructure Investment Funds (IIFs).

Chart 5: Australia's place in the world time-zone map



(1) Australian Eastern Standard Time
Source: Axiss Australia, Benchmark Report 2006.

The benefits of managing global funds

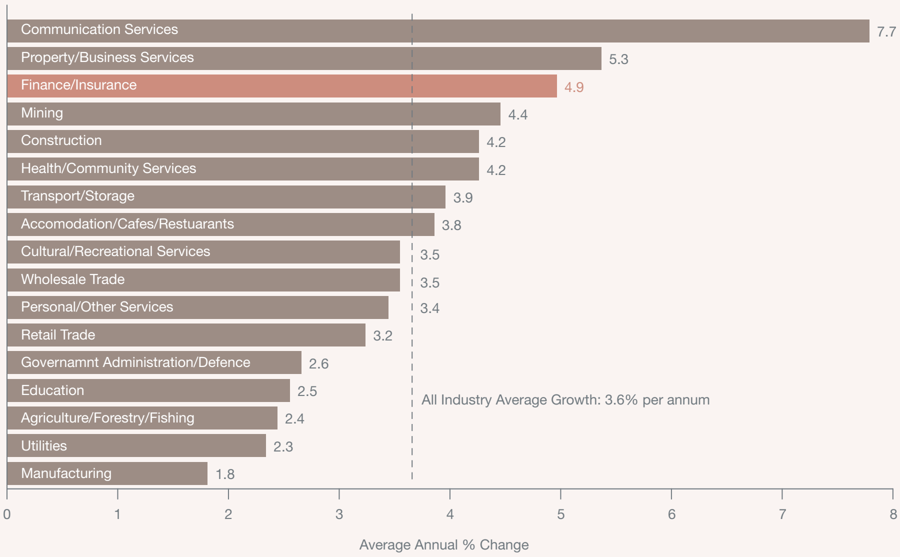
The importance of the services sector to the future growth of the Australian economy

The Australian economy has experienced strong and steady growth in GDP for a number of years. Such growth has been largely domestically driven as Australia has been a net importer of goods and services over the last five years.

Despite the recent resources boom, it is the services sector which has underpinned Australia's economic stability and growth over the last decade. The strongest industries in trend volume terms over the four quarters to December 2006 was the finance/insurance industry, contributing 0.6 percentage points to GDP, followed by the construction and property/business services industries, which both contributed 0.5 percentage points to GDP growth. Agriculture detracted 0.6 percentage points from GDP growth over the period (ABS: 5206.0 - Australian National Accounts: National Income, Expenditure and Product, December Quarter 2006).

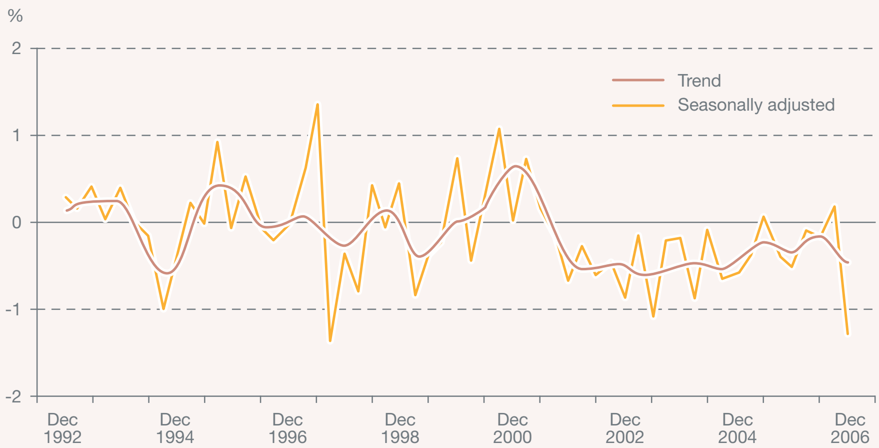
A net export position is important to the economy to secure sustainable growth over the medium to long term. Currently, despite the emphasis placed on mining and agriculture, the contribution of exports from these sectors to the growth of the economy has been minimal. As indicated below net exports contribute to GDP growth when the change in the volume of exports has been greater than the change in the volume of imports. In the December quarter 2006 net exports detracted 1.3% from GDP in seasonally adjusted terms - the largest subtraction from GDP growth since the September quarter 1997.

Chart 6: Australia's real gross value added by Industry – 1985 to 2005



Source: Axiss Australia, Benchmark Report 2006.

Chart 7: The percentage contribution to growth of net total exports contribution



Source: ABS, 5206.0 Australian National Accounts: National Income, Expenditure and Product, Dec Qtr 2006

The benefits of managing global funds - continued

OECD analysis of countries' trade to GDP ratio shows how far behind Australia is in terms of trade adding value to the country's continued growth. As highlighted, in a paper prepared for the Committee for the Economic Development of Australia (CEDA) – *Global Chains: Australia's Challenge in the Evolving Global Economy*, by Professor John Houghton, 'Australia has one of the lowest trade to GDP ratios among OECD countries, with goods trade about 20% and services trade at 5% and declining'.

In a speech to the Australian Chamber of Commerce and Industry in November 2001, the Treasurer, the Hon. Peter Costello, outlined that 'we must prepare for the real challenges ahead – drought, urban water shortages, population ageing and relentless international competition'.

Such a prospect emphasises the importance of exploring the potential for the export of services to provide support for Australia's economy in the future.

The Standing Committee on Economics, Finance and Public Administration's recent Inquiry into the current and future directions of Australia's service industries is timely and IFSA was pleased to highlight the potential contribution that the Australian funds management industry has to make.

Chart 9 is derived from OECD data on the contribution made by the finance and business services sectors to their nation's economic growth. It highlights that Australia has a significant asset in its financial services sector and the funds management industry. It is time to make the most of that asset by recognising its potential to add greater value to the future economic stability and growth of Australia.

Chart 8: Trade to GDP ratios
Difference between 2005 and 1991 ratios in percentage points

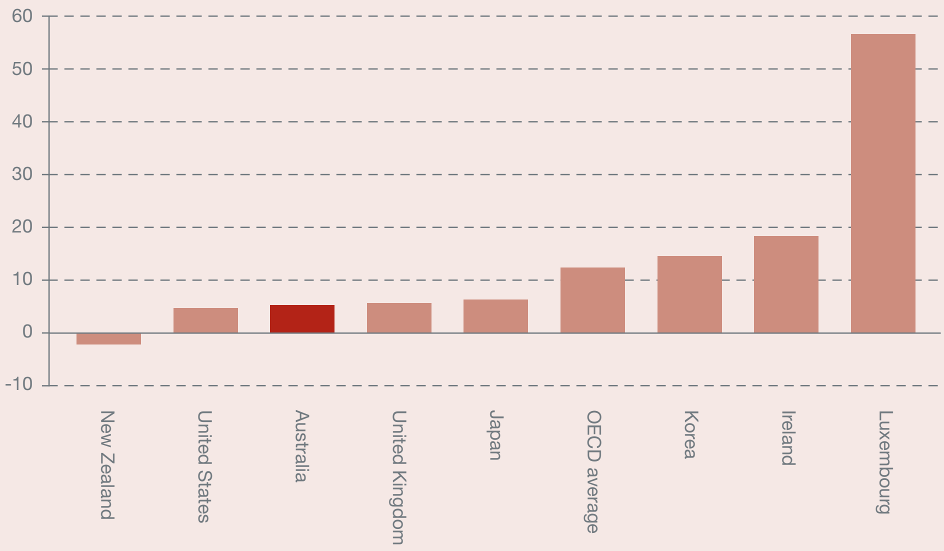
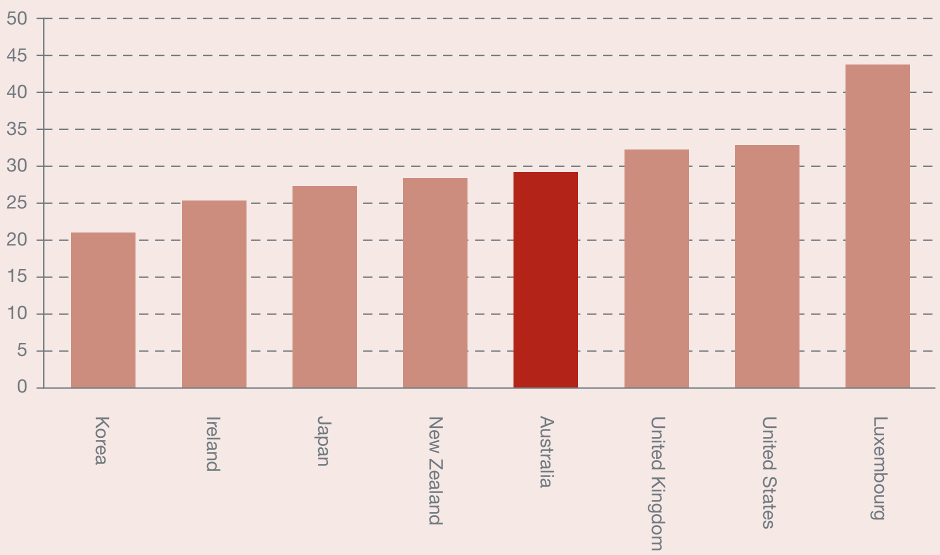


Chart 9: Value added in banks, insurance, real estate and other business services as a percentage of total value added, 2005 or latest available year



Source: OECD Online Fact Book 2007

How would Australia benefit from improving exports in financial services?

By increasing our export fund management services into Asia and beyond, Australia will benefit both economically and culturally.

There are positive corporate and personal tax benefits as a result of increased revenues. There will also be increased employment opportunities within Australia, in Asia and the broader global market for management and highly skilled staff.

Depending on the extent of services provided, management fees of approximately 1.5% of assets under management are available to companies providing them. As previously mentioned the current managed funds investment pool in Asia (excluding Australia) was A$2.1 trillion at the end of 2005 and it is growing quickly. The Australian industry will also benefit from greater economies of scale which, through better utilisation of fixed costs, will drive improved margins and overall industry productivity and profitability.

The other benefit for Australia will be the opportunity to move to a better balance of funds flow similar to the US and UK experience. This would help ensure that Australia is better positioned to access foreign capital through managed investment vehicles to stimulate Australian growth industries.

Additionally, a strong presence in the region's financial markets will enhance Australia's standing and strengthen our ties within the region.

The funds management sector services

As highlighted by the Board of Taxation's report to the Treasurer on International Tax in February 2003, 'Australia is a highly attractive location within the Asia Pacific region for financial service providers. We have a large pool of highly talented labour. We also have a maturing funds management industry which helps generate clustering of other high-end service activities — for example, business and professional services, and IT.' The services provided by the broader funds management industry in Australia include, but are not limited to, the following:

- Asset management
- Investment consulting
- Platform delivery systems, wrap accounts and master trusts
- Custodial services
- Financial service IT and software development providers
- Actuarial services
- Legal and accounting services
- Compliance and risk monitoring
- Investment performance research and reporting
- Education and training services
- Portfolio administration services
- Advice/distribution

Chart 10 indicates the approximate fees charged at each stage of the investment value chain. In such a fluid global market, the extent to which Australia will benefit from increased flows will depend on the extent to which the industry can remain globally competitive.

Chart 10: Typical funds management expenses as a percentage of funds under management

Custodial services/trading	**0.03 - 0.05%**
Asset management	**0.1 - 0.7%**
Principle investment advisory	**0.1%**
Product & servicing	**0.4 - 0.8%**
Advice/distribution	**0.4 - 0.65%**
Total Management Expense	**1.03 - 2.30%**

Source: IFSA, 2007

By being a more effective competitor, primarily in the areas of custody/trading, asset management and principle investment advisory services, Australia will be able to secure the position of a regional funds management hub. Such a prospect would be attractive for all Australian states and territories which are always actively pursuing commercial trade and employment opportunities for their cities and regional centres.

The way ahead

Highlighting Australia's reputation for being the 'lucky' country, the 2006 OECD Economic Survey said that Australia has been riding high on the global boom in commodities. It's not all luck though and the report gave Australia much credit for implementing reforms and policy which have bolstered the nation's resilience to the string of recent economic shocks. The report goes on to state however that 'A further test of this new resilience will occur at some point when the terms of trade decline,' underlining the need for further prudent policy making.

Australia's policy makers joined others at the 2006 APEC Finance Ministers' meeting to discuss financial sector reform to attract capital flows. As the joint Ministerial Statement said, 'Capital flows can provide additional resources for productive investments; enhance access to technology, management skills and international markets; and improve competitiveness and efficiency'.

The Australian funds management industry stands ready to assist policy makers in realising this potential. We have much of the infrastructure required in place and there is sustainable growth in demand for the services and capabilities we are able to offer.

Taking steps to improve the competitiveness of Australia in the global funds management market, understanding the impact of the sector to the Australian economy, seeing it as an integral part of trade negotiations and promoting its services and capabilities will only enhance the industry's ability to contribute to the ongoing stability and growth of the Australian economy. The overwhelming benefits of such an approach will be felt through the employment opportunities developed for future generations and incremental wealth that will flow from increased tax revenue.

IFSA would like to work with government on the policy areas outlined earlier in this paper, developing specific recommendations in the areas of regulation, taxation, evaluation, trade negotiations, promotion and education.

IFSA would welcome a partnership approach between government and industry to develop policy, prioritise the action needed and mitigate the risks. If appropriate, we would be delighted to commit IFSA and member company resources to facilitating a broad ranging Inquiry to help Australia realise its potential and make the most of the assets we have.

Appendix 1

Extract from IFSA's submission on Managed Investments Tax Regime (MITR) to the Treasurer, March 2006.

'In order to specifically address the stated impediments and threats to the industry, the ATO and investors, we submit that a specific tax regime should be introduced into the tax law to ensure that:

1 Complete flow through of taxable income to investors in managed investment trusts that retains its character for taxation purposes;

2 CGT be the primary taxation code for shares, property and units in unit trusts held by a managed investment trust;

3 Managed investment trust taxable income be:

   a. fully distributed by the managed investment trust to investors each year;

   b. assessed to investors for taxation purposes by reference to their economic interest in the managed investment trust. This should be determined by reference to each investor's unit holdings as a proportion of total units issued by the managed investment trust so that the concept of present entitlement will no longer be relevant for tax purposes;

   c. calculated by reference to the best information available at the time of distribution; and

   d. adjusted, by way of tax deduction or inclusion of additional assessable income, for any under or over distribution in the prior year where that under / over distribution occurred as a consequence of imperfect information available at year end; and

4 Non-resident withholding tax be simplified so that it is imposed and collected by reference to the distribution components known and made at the time liability to withholding tax arises.

We note for completeness that MITR is largely a statutory codification of the industry and ATO practices from a taxation perspective and we do not expect that the introduction of MITR will give rise to a revenue cost for the Government. We consider the value generated for the industry, its investors and the ATO with respect to MITR arises because a high degree of certainty will exist in relation to the tax treatment of managed investment trusts and their investors. This certainty will in turn generate compliance and administrative cost savings as well as certainty and confidence in financial markets.

The ATO is required to administer the taxation system as it applies to managed investment trusts in accordance with the law as it stands and this itself will give rise to a lack of consistency in tax treatment of identical products across the industry, especially under a self assessment regime. This is because different parties may have different views regarding application of the tax law given that not all taxpayers will seek to test the ATO view of the law or may not wish to depart from market practice in relation to a particular regard. Further, the ATO cannot review the tax affairs of each managed investment trust on an annual basis and thereby ATO views regarding application of the tax law to a particular arrangement will not be known for sometime after the relevant product is distributed and accepted by investors.

In an environment of increased regulatory oversight and supervision both domestically (eg financial services law) and globally (Sarbanes Oxley Act) it becomes very difficult for market participants to operate within the regulatory framework where the taxation regime applying to managed investment trusts is uncertain. Indeed certainty as to some fundamentally important tax issues ultimately may not be correctly known until many years later after taxable distributions have been made to investors whose tax affairs will ordinarily have been "finalised", should the ATO dispute the tax treatment adopted by the Managed Investment Trust.

It is submitted that such a system of taxation is most unsatisfactory and exposes investors to unwarranted tax risks. It is in this context that the need for a new managed investment trust tax regime is based, rather than by undertaking legislative amendments to the tax law on a piecemeal basis to address particular issues on a stand alone basis.

On this basis, we consider that MITR must be viewed as a "partnership" between the Government, ATO and industry whose success is ultimately in the national interest.'

For more detailed information please visit:
www.ifsa.com.au/public/content/ViewCategory.aspx?id=301

Appendix 2

Extract from the Australian Services Roundtable submission to the House Standing Committee on Economics, Finance and Public Administration Inquiry into the current and future directions of Australia's service industries:

At nearly 23 percent of exports, official estimates of Australia's services exports are now roughly on a par with manufactures exports and outdo Australia's rural exports.

But trade in services is known internationally to be notoriously difficult to measure and the official figures are likely to be significant understatements for the following reasons:

- First, Australia's services sector makes a much larger contribution to exports than its direct share, as services are often integrated with other goods; on average about one fifth of the value of Australia's goods exports is estimated to be composed of services.
- Second, the ABS compiles trade in services statistics within the framework of the System of National Accounts and the Balance of Payments (BoP). Imports are defined as services delivered by non-residents to residents of Australia; exports are services delivered by residents to non-residents. But services are traded internationally via four separate modes of delivery (see below). The BoP underestimates trade in services by omitting sales of services through Modes 3 and 4. Initial surveys of 100 percent Australian owned offshore affiliates were undertaken by the ABS in 2005 to try to get a grasp on Mode 4 services exports. The results suggest that the official data on services export as measured by the Balance of Payments has probably been measuring less than one third of Australia's actual exports of services.
- Thirdly, the only types of service exports on which official ABS export data are regularly available include passenger and freight transportation services, travel services, communication services, a range of business services such as computer and information services and financial services, and certain personal, cultural and recreational services. A number of types of services exports are not picked up in the statistics at all.
- Finally, the supplementary data available from ABS industry survey work is inadequate. Collections of selected service industries are undertaken supposedly in response to user needs but to date do not seem to reflect Australian export industry priorities. Outputs for 2003-04 included public libraries, museums, accommodation, cafes and restaurants and travel agency services. Outputs for 2004-05 are expected to cover pubs, clubs, sport and gambling services. Outputs for 2005-06 will cover retail and wholesale.

Modes in which services are exported

Mode 1: Cross-border supply is defined to cover services flows from the territory of one country (the exporter) into the territory of another (e.g. banking or architectural services transmitted via telecommunications or e-mail);

Mode 2: Consumption abroad refers to situations where a services consumer (e.g. a tourist, student or medical patient) travels temporarily into another country's territory (that of the exporter) to obtain a service abroad;

Mode 3: Commercial presence takes place where a services supplier of one country (the exporter) establishes a local presence, including through ownership or lease of premises, in another country's territory to provide a service in that market (e.g. domestic subsidiaries of foreign insurance companies or hotel chains). This activity may be picked up and measured and described as "investment" but conceptually, from an international trade policy and trade law perspective, this activity constitutes services export activity;

Mode 4: Movement of natural persons consists of services providers of one country (the exporter) travelling temporarily to the territory of another country to supply a service (e.g. accountants, lawyers, doctors, teachers).

For more information please visit:
www.aph.gov.au/house/committee/efpa/services/subs/sub044.pdf

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