Victorian Traditional Owners Funds Limited

A Company Limited by Guarantee
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Registered name:

The Trustee for Victorian Traditional Owners Trust - Dja Dja Wurrung Clans Aboriginal Corporation for and on behalf of the Dja Dja Wurrung People

The Trustee, the Victorian Traditional Owners Funds Limited (VTOFL), presents the Report Card for the 2021 financial year for Victorian Traditional Owners Trust - Dja Dja Wurrung Clans Aboriginal Corporation for and on behalf of the Dja Dja Wurrung People (DDW Trust).

The DDW Trust was established with effect from 1 July 2018. The DDW Trust holds the funds of the Dja Dja Wurrung Clans Aboriginal Corporation Ltd (DDWCAC) which were originally held with the funds of another Traditional Owner Group in the Victorian Traditional Owners Trust (VTOT). VTOT was established under a Trust Deed signed on 13 September 2011 between Robert Clark the Attorney General of Victoria and the Trustee, VTOFL. The amendment deed creating the two separate trusts one of which is the DDW Trust was signed on 25 September 2018.

DIRECTORS

The names of each person who has been a Director of the VTOFL during the year and to the date of this report are:

Elizabeth Helen Eldridge

Glen Gerald Brennan (PSM)

Susanne Dahn

Neil Donald Westbury (PSM)

PRINCIPAL ACTIVITIES

The principal activity of the DDW Trust is to invest settlement funds received on behalf of the Dja Dja Wurrung People represented by DDWCAC. The settlement between the Dja Dja Wurrung People and the State of Victoria was under the Native Title Settlement Framework.

The State of Victoria and the Dja Dja Wurrung People reached a settlement on 28 March 2013 and the Participation Agreement was executed on 5 December 2013. In accordance with the terms of this Participation Agreement the State of Victoria paid the settlement amount of $5 million to the VTOT.

The DDW Trust (originally VTOT) has a duration of 20 years of which 12 years remain, based on a terminal date of 12 December 2033.

The costs of running VTOFL are currently met by an annual grant agreed with the Department of Justice and Community Safety.

DDW TRUST AND INVESTMENT STRATEGY

VTOFL has developed investment objectives and an investment strategy for the DDW Trust.

The objectives and the investment strategy were developed after meetings with DDWCAC where DDWCAC outlined its long term and short-term objectives and its tolerance for risk.

The DDW Trust's objectives are as follows:

- pay the minimum annual funding amount of $250,000 per annum adjusted for changes in the Consumer Price Index (CPI); and
- achieve a targeted capital sum on the termination date, 12th December 2033, of $5,000,000 (being the settlement sum) not adjusted for inflation.

The investment strategy to 30 June 2019 had a target average annual return of CPI + 3.7% (after fees) with a probability of negative returns once in 6.3 years. The average annual return target was reduced to CPI +2.4% from 1 July 2019. The reduction followed a review of the economic and financial market assumptions underpinning the investment strategy. The advice was that over the medium term (10 to 15 years) there will be lower returns due to:

- economic growth which, has been moderate since the Global Financial Crisis, is late in the economic cycle and is expected to slow and remain slow;
- asset markets are considered late in the cycle and are considered overpriced;
- bond returns are expected to remain low for some time given the level of global debt; and
- the low bond returns are the basis on which other low investment returns are set.

The reduction in the projected real return of 1.3% has implications for the DDWAC. While VTOFL still expects to meet the minimum annual funding amounts each year (assuming the return target of CPI +2.4% is achieved) it does not expect to achieve a termination amount of $5 million (not inflation adjusted) on 12th December 2033, the terminal date of the DDW Trust. Under the new assumptions there is a 50% chance that the terminal amount on 12th December 2033 will reach $3.4 million.

The DDW Trust funds are invested equally across two of the Victorian Funds Management Corporation's (VFMC) investment products, the Capital Stable Fund and the Balanced Fund.

Table 1 below sets out the value of funds invested with VFMC as at 30 June 2021 and 2020. It also reports the other assets of the Trust, which comprise franking credits receivable less accrued expenses.

Table 1 **Dja Dja Wurrung Trust**

The funds were invested and valued in the following VFMC Funds as at 30 June 2021 and 2020:

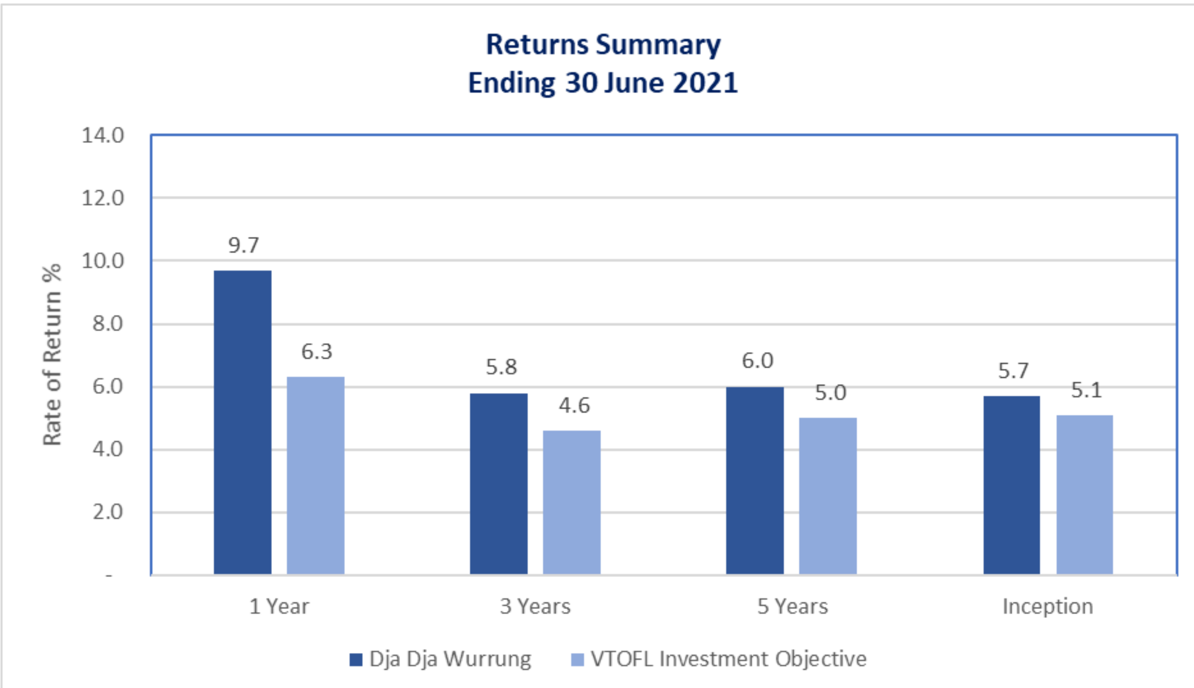
	2021	**2020**
	$	**$**
VFMC Capital Stable	2,633,996	2,546,520
VFMC Balanced	2,686,024	2,548,712
VFMC Growth	-	-
Total Invesments with VFMC	5,320,020	5,095,232
Other Assets less accrued expenses	8,193	15,156
Total Equity	5,328,213	5,110,388

REPORT ON DDW TRUST'S PERFORMANCE

The actual return of the funds will be determined by a wide range of market driven factors and will vary over time.

Chart 1 below shows the performance of the DDW Trust against its investment target since it was established. The performance includes earnings from VFMC and franking credits less expenses.

Chart 1. Performance of the Dja Dja Wurrung Trust against Target Returns



Note: Inception for the Trust is 13 December 2013. The VTOFL Investment Objective is a return of CPI + 3.7% p.a. to 30 June 2019 and CPI + 2.4% p.a. thereafter.

Table 2 below shows the actual performance of the DDW Trust against its investment target.

Table 2	Total Trust			
	CPI Growth	Margin	VTOFL Investment Objective	Investment Returns
FY Ending				
30-Jun-2014	1.3%	1.8%	3.1%	4.2%
30-Jun-2015	1.5%	3.7%	5.3%	5.5%
30-Jun-2016	1.0%	3.7%	4.8%	3.4%
30-Jun-2017	1.9%	3.7%	5.7%	6.4%
30-Jun-2018	2.1%	3.7%	5.8%	6.2%
30-Jun-2019	1.6%	3.7%	5.3%	6.4%
30-Jun-2020	-0.3%	2.4%	2.0%	1.4%
30-Jun-2021	3.8%	2.4%	6.3%	9.7%
To 30 June 2021	(cumulative %)		45.4%	51.9%
To 30 June 2021	(%p.a.)		5.1%	5.7%

For the 2021 financial year the DDW Trust outperformed its investment target of 6.3% (CPI 3.8% plus a margin of 2.4%). The actual return was 9.7%.

CPI was the highest reading since 2008 amid a rise in tobacco excise, resetting of the Medicare and Pharmaceutical Benefits, the introduction, continuation, and conclusion of a number of government schemes and home building grants.

The average annual return since the DDW Trust was established has been 5.7% compared with a target of 5.1%.

Table 3 below summarises the key changes in the balances over the past eight years.

Table 3	Total Trust					
	Opening Balance $	Net Investment Gain $	Withdrawals $	Closing Balance $	Gain in Net Assets	VTOFL Investment Objective
FY Ending						
30-Jun-2014	5,000,000	207,015	-	**5,207,015**	4.1%	3.1%
30-Jun-2015	5,207,015	285,697	(187,500)	**5,305,212**	5.5%	5.3%
30-Jun-2016	5,305,212	177,557	(375,000)	**5,107,769**	3.3%	4.8%
30-Jun-2017	5,107,769	324,552	(250,000)	**5,182,321**	6.4%	5.7%
30-Jun-2018	5,182,321	322,876	(250,000)	**5,255,197**	6.2%	5.8%
30-Jun-2019	5,255,197	335,622	(275,000)	**5,315,820**	6.4%	5.3%
30-Jun-2020	5,315,820	73,949	(279,380)	**5,110,388**	1.4%	2.0%
30-Jun-2021	5,110,388	496,035	(278,210)	**5,328,213**	9.7%	6.3%
To 30 June 2021	**5,000,000**	**2,223,304**	**(1,895,090)**	**5,328,213**	**51.8%**	**45.4%**

Since the original settlement amount of $5 million was received by the DDW Trust the cumulative earnings and franking credits after expenses have been $2,223,304. Distributions have been $1,895,090.

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Table 4 below shows the detailed movements in the DDW Trust over the last two financial years, and the distributions paid.

Table 4 **Detailed Movements Over the Past Two Years**

	2021	2020
	$	$
Trust Equity at beginning	5,110,388	5,315,819
Add		
Return from funds invested	494,788	60,964
Franking credits	5,757	12,584
Resources received free of charge	36,000	47,135
Other income		5,241
Less		
Trust's share of VTOFL expenses	(36,000)	(47,135)
Audit fees	(4,510)	(4,840)
Distributions paid	(278,210)	(279,380)
Trust Equity at end	5,328,213	5,110,388

REPORT ON SIGNIFICANT CHANGES AND LIKELY DEVELOPMENTS

During the 2021 financial year Mercer Australia (Investment) Limited (Mercer) undertook a Strategic Review of the DDW Trust's investment strategy and financial objectives. The review used Mercer's latest capital market aware assumptions (December 2020). Overall Mercer sees lower interest rates and therefore lower market returns and the risk of higher inflation. The Review indicates that the DDW Trust only has a 43% chance of achieving its current real return target of 2.4% per annum with its current investment strategy and asset allocation. For the DDW Trust to maintain a 50% chance of achieving its current investment target it would be necessary to increase the level of growth assets and hence the Trust's level of volatility. The Review indicates the DDW Trust has a 50% chance of achieving a real return of 2.2% per annum with its current investment strategy and asset allocation. After discussion with DDW, VTOFL has determined to retain the current asset allocation which has a 50% chance of achieving a real return target of 2.2% per annum and a 50% chance of having a balance of $3,544,454 in the DDW Trust when the Trust terminates. VTOFL will report against the new real return target from the start of the December Quarter 2021.

Also, during the 2021 financial year Mercer commenced reporting quarterly to VTOFL on the performance of the DDW Trust's investment portfolio.

Finally, during the 2021 financial year VTOFL carried out a selective tender seeking expressions of interest to manage the investments of the DDW Trust. Following a review of the tenders VTOFL resolved in October 2021 to transfer the management of the DDW Trust's investments to the Mercer Conservative Growth Fund (100%). The DDW Trust's investments were transferred to Mercer during October and November 2021.

REPORT ON VFMC's INVESTMENT STEWARDSHIP & ENVIRONMENTAL, SOCIAL AND GOVERNANCE INTERGRATION

VFMC reports its overarching investment stewardship approach aims to improve risk-adjusted returns by being a responsible steward of client's capital and managing Environmental, Social and Governance (ESG) risks alongside other investment factors.

VFMC's four key pillars of activity are:

- Active Ownership e.g. Proxy voting and engagement;
- ESG Integration e.g. manager selection due diligence and monitoring and direct investment due diligence;
- Major ESG Projects e.g. climate risk management plans and Modern Slavery; and
- Collaboration and Information Sharing e.g. collaborate and engage with industry and peers.

VFMC's enabling policies are:

- ESG Investments Policy;
- Proxy Voting Policy;
- Climate Change Position Statement;
- Modern Slavery Policy; and
- Exclusions Policy.

VFMC works to ensure it remains across and engages on material and emerging ESG risks and themes, many of which are also of direct relevance and interest to clients. These material issues and themes fall primarily into three categories: environmental, social, robust corporate governance and examples of each are set out below. These themes underpin its broader investment stewardship activities across ESG Integration, Major ESG Projects, and Collaboration and Knowledge Sharing.
Examples of material ESG issues and themes that VFMC engage on:

Examples of VFMC's activities during the 2021 financial year are outlined below.

Engagement with investee companies regarding modern slavery risk

In speaking with one company whose products are shipped internationally, VFMC became aware of the fact that management believed that its responsibility regarding modern slavery ceased as soon its product was loaded onto ships for export (this also being the point at which product ownership was legally transferred). VFMC communicated its view that:

- Modern slavery is a risk for which companies are responsible up and down their supply chains
- To some extent, one's responsibility follows their products
- Companies should engage with relevant stakeholders to raise awareness and drive positive change

In this instance, the nexus between the product and ship, even though legal ownership had ceased, was very close (e.g., it was not an instance in which ownership had ceased and the product had then passed through 'multiple sets of hands'). Further, their product was going directly onto ships, and the global shipping industry has been identified as being particularly susceptible to the risk of modern slavery given seafarers are often from nations with human rights, labour rights and corruption challenges.

As a result of VFMC's engagement, the company committed to evaluating how it could influence better practices with the shipping companies with whom it interacts.

Engagement regarding climate risk management

Climate change is a systemic issue, presenting a material financial risk to underlying assets and companies within VFMC's investment portfolio. VFMC and its external investment managers undertook a range of activities in FY 2021 to better understand and manage climate change risk. These have included both quantitative and qualitative evaluations of carbons emissions, understanding changes in regulatory frameworks and measuring transition risks associated with these. VFMC engages with investee companies and external fund managers regarding climate risk management and net-zero commitments to both encourage the transition to a low carbon economy and responsible allocation of capital.

In its Climate Change Position Statement issued in June 2021, VFMC supports the aim of the 2015 Paris Agreement to limit global warming to well below 2 degrees (moving toward 1.5 degrees) to minimise the worst impacts of climate change. This will require the economy to achieve net zero emissions by 2050. VFMC believe that the transition to a net zero economy needs to be carefully planned and managed to best reduce and manage the impact of potential shocks that may occur as part of this transition, as well as realise opportunities that come with this economic transformation. VFMC has, accordingly, committed to net zero portfolio greenhouse gas emissions by 2050.

Engagement regarding Cultural Heritage and First Nations communities

The destruction of the sacred Juukan Gorge caves by Rio Tinto in early 2020 elevated the need for cultural heritage to be a key consideration for all investors. VFMC is invested in Rio Tinto through its equities portfolio. Following the devastating destruction of the Juukan Gorge caves, VFMC joined with other peer investors to engage with the company to learn how the caves, with a 46,000-year history of continual occupation by Traditional Owners, had been allowed to be destroyed. VFMC spoke with Rio Tinto to encourage timely and public disclosures of the work it has been doing to improve how it operates, meet Parliamentary recommendations, and rebuild confidence – to ensure such an event never happens again. A key focus for VFMC was on ensuring executive and board accountability at Rio Tinto for the incident. VFMC collaborated with other investors to identify transparent measures for Rio Tinto to disclose against, including rebuilding trust with First Nations communities, improvements to culture and operations, and advocacy on sector-wide improvements to cultural heritage.

In addition to engagement with Rio Tinto, VFMC has also undertaken the following activities related to cultural heritage during FY 2021:

- Engaging with investment managers and underlying investee companies to better understand their relationships with First Nations groups and community as part of their ongoing ESG engagement
- Attending seminars and briefings regarding cultural heritage across various issues, including the intersection of indigenous land management and carbon farming, Australian mining and Indigenous heritage and the empowerment of Indigenous communities

VFMC voted against Rio Tinto Ltd.'s Remuneration Report due to Rio's classification of the three departing senior executives as 'good leavers' for remuneration purposes in the wake of the destruction of the Juukan Gorge caves.

Engagement with Woolworths to avoid the harmful impact of a Dan Murphy's outlet developed near three Indigenous dry communities

Alcohol consumption, and its negative health and social side-effects, are serious issues in Northern Territory, which has enacted some of Australia's strictest licensing laws. When VFMC became aware of Woolworths' application to build its first Dan Murphy's outlet in the Northern Territory on a site close to three 'dry' indigenous communities, VFMC engaged not only with Woolworths (both directly and via ACSI) but also with the owner of the land (one of our external investment managers) on which the proposed store was to be located. VFMC also participated in engagement with one of the leading opponents, the Foundation for Alcohol Research and Education (FARE), as well as Darwin's Danila Dilba Aboriginal Health Service. Subsequently, following significant investor and stakeholder pressure, in FY2021 Woolworths announced that it has disbanded the Dan Murphy's store plans at this proposed location.

VFMC REPORT ON INVESTMENT CLIMATE

VFMC advised that the 2020-21 year was a year of recovery in markets from the COVID-19 sell-off in the previous year. Equity market returns were very strong, 28.5% in Australia and 36.8% hedged internationally. Bond yields also rose, 67 bps in Australia and 80bps in the US to close at 1.53% and 1.45% respectively. The AUD appreciated 9.0% against the USD as commodity prices rebounded strongly with Oil up 87% and Iron Ore over 100%. Breakeven inflation rates (the difference between real and nominal rates) rose 147bps to 2.49%. The three Multi Strategy Funds outperformed their benchmarks over the year, with those more heavily weighted in Equities, namely the Growth and Balanced Funds, experiencing the more significant outperformance.

VFMC says it is now over a year since the COVID-19 pandemic emerged unexpectedly, creating an acute health crisis and then an overwhelming economic crisis, as policymakers adopted stringent containment measures to save lives, which plunged the global economy into a historically deep recession. Starting in the second half of 2020, the global economy rebounded more strongly than anticipated as timely, forceful and concerted fiscal and monetary policy prevented a more extended downturn.

VFMC noted that transfers, loans and guarantees shielded firms and households, giving them precious oxygen to recover. Indeed, in many countries, personal disposable income increased and, in some countries, such as the United States, at the strongest rate in decades. Saving rates also increased substantially leaving households with a large pool of “excess savings”. Widespread furlough schemes bolstered firms’ bottom lines and shored up employment. Monetary policy also played an important role. An extraordinarily accommodative policy stance underpinned exceptionally easy financial conditions. These were supported later in the period by positive news about vaccines and anticipation of the boost to the economy from fiscal stimulus in the United States. Consequently, private consumption has been the main engine of growth, allaying initial and widespread fears of lingering risk aversion and contagion worries.

VFMC says that although the recession has turned out to be less severe than initially feared with world GDP returning to near pre-crisis levels, it is important to acknowledge that this masks a clear divide between China, where GDP is now well above its pre-crisis level, and the rest of the world, where it is still generally some way below. Moreover, the recovery has been uneven across sectors, mainly reflecting the evolution of the pandemic and hence the stringency of containment measures. Manufacturing and residential construction have rebounded strongly, while services have lagged on lingering mobility restrictions.

VFMC says financial markets, the economic recovery and exceptionally accommodative financial conditions underpinned rising prices across all growth asset classes, to the point in some equity markets at least, of very stretched valuations. This environment along with a tilt toward longer-dated issuance coalesced to lift long-term sovereign bond yields, although the last few months has seen a partial reversal of this trend. However, credit spreads were compressed even for low-rated firms and corporate bond issuance remained buoyant as the confluence of positive forces supported corporate solvency and were instrumental in reducing business funding costs. House prices rose sharply in many countries.

VFMC'S THREE SCENARIO ECONOMIC AND INVESTMENT FRAMEWORK AND OUTLOOK

VFMC’s says that overall it seems the degree of uncertainty about the future is lower compared to a year ago. Economic recovery is no longer imminent but is here and now, although the risks of the pandemic remain as the rollout of global vaccinations is uneven and new waves of contagion may continue to emerge. Nevertheless, COVID-19 seems unlikely to be the primary concern for financial markets going forward. Rather they are likely to be more focused on traditional concerns around growth and inflation trends, company earnings and outlooks, the trend of interest rates and subsequent actions by central banks.

VFMC’s three scenario economic and investment framework is designed to convey possible pathways for how activity might evolve over the next 6-12 months.

The **base case macro scenario (75% probability, unchanged)** envisages a comparatively smooth, ongoing recovery where the pandemic is steadily brought under control. Monetary and fiscal policy remain broadly supportive, which ensures financial conditions do not tighten significantly. Labour markets continue to recover, which further supports private consumption and sustains the expansion. In the major developed economies, inflation rises towards targets, but any increase beyond them is temporary as the cycle transitions to one where growth will still be strong (just not as strong as the past year) and policy support will be highly accommodative (just not as ‘easy’ as the past year). This tends to be supportive of continued, albeit more moderate market expansion. However, this does not mean the market will not face difficult times or avoid corrections. Volatility will return at some point even if the macro direction remains on track.

The **upside macro scenario (15% probability, up from 10%)** is one that initially sees even stronger growth, reflecting a larger impact from fiscal policy on demand and a bigger reversal in household saving rates than assumed in the central scenario, possibly supported by better news on the pandemic front. Output gaps (the difference between actual and potential GDP growth) close faster than foreseen while unemployment rates fall rapidly. However, the swifter improvement also brings with it an increased risk that inflation exceeds expectations and financial conditions tighten as market participants anticipate a quicker and possibly more intense monetary policy tightening. Even if any increase in inflation ultimately proves transitory, markets could overreact, anticipating a more sustained inflation trajectory. Either way, the tightening could be substantial, and investors could be caught wrong-footed and be forced to unwind their positions. The prolonged and at times aggressive risk-taking that has prevailed in markets arguably increases the probability of such an outcome. Recent stress, such as the Archegos failure in April (where highly leveraged bets made by a large family investment vehicle went awry) and the losses it inflicted on banks, could turn out to be the proverbial canary in the coal mine.

The **downside scenario (10% probability, down from 15%)** sees the recovery stall, which is more plausible if the pandemic proves harder to control. Renewed lockdowns would likely blunt the impact of government spending on the economy while the deployment of excess savings by households could fall well short of expectations as renewed virus-related uncertainty induces an increase in precautionary behaviour. The retrenchment in spending would be felt most acutely in the business sector and the feared wave of firms’ insolvencies, thus far avoided, could materialise. In this alternative scenario, firms’ losses could be larger, possibly on a par with those during the Global Financial Crisis (GFC). In turn, banks could feel the strain as there is evidence suggesting some of them have released part of the provisions made earlier in 2020. Other potential pathways that could short-circuit the current recovery would be a spike in geopolitical flashpoints or aggressively premature policy tightening by central banks.

As approved by the Directors of VTOFL.

Elizabeth Eldridge	Lisa Norden
Chair	Company Secretary
15 November 2021	15 November 2021