



DIRECTION ON INVESTMENT IN RESIDENTIAL MORTGAGE-BACKED SECURITIES 2008 (No. 2)

I, WAYNE MAXWELL SWAN, Treasurer of the Commonwealth, give this Direction under section 62A of the *Financial Management and Accountability Act 1997*. This Direction is to provide guidance to persons to whom I have delegated powers to invest under subsection 39(2) of the Act. Delegates are required to comply with this Direction, which is to be read in conjunction with my Directions of 13 July 2008 which were tabled in Parliament on 25 September 2008.

Objectives

Over the past 15 years, the market for residential mortgage-backed securities (RMBS) has provided an important source of funding for new and smaller mortgage lenders to compete with the major banks. However, developments in international capital markets since mid-2007 have reduced liquidity in the RMBS market and constrained the ability of lenders to access funding from this source.

In view of these developments, on 3 October 2008 I directed the Australian Office of Financial Management (AOFM) to invest up to \$4 billion in Australian RMBS to support competition from a diverse range of lenders during the present market dislocation.

I am now directing the AOFM to invest up to an additional \$4 billion in Australian RMBS issued by lenders other than authorised deposit-taking institutions (non-ADI lenders). The decision to direct AOFM to invest up to an additional \$4 billion aims to further support competition from non-ADI lenders in residential mortgage lending and has been made in conjunction with the Government's decision to guarantee the deposits and wholesale term funding of ADIs.

Directions

Further to my Directions of 3 October 2008 and 13 July 2008, I direct that:

1. Delegates invest up to \$4 billion in Australian residential mortgage-backed securities rated AAA or equivalent by one of the major credit rating agencies and issued by non-ADI lenders.
2. The Secretary to the Treasury may specify a cap on the total value of securities that may be purchased per originator and/or from certain classes of originators.
3. The securities accepted must meet any requirements that may be specified by the Secretary to the Treasury. Without limiting the scope of such requirements, they may include limitations on the loan valuation ratios, the proportion of low documentation loans, substitution periods and the geographical concentration of the mortgages that back the securities.
4. The Secretary to the Treasury may specify a limit on the price for the securities purchased.
5. The AOFM is to manage the investments in the residential mortgage-backed securities made under this Direction. The securities held under this Direction and my Direction of 3 October 2008 are to be held in the same portfolio, and held

separately to the AOFM's cash and long-term debt portfolios. The performance of this portfolio will be evaluated separately.

6. The AOFM may enter into repurchase arrangements using residential mortgage backed securities purchased under this Direction, or other securities purchased under my Directions of 13 July 2008, for short term financing in its management of Official Public Account balances.
7. The AOFM may adjust its holdings of securities purchased under this Direction to take account of changes in their characteristics and credit quality or to provide better balance in its holdings of these securities.
8. After conditions in the primary residential mortgage-backed securities market have improved, securities purchased under this Direction may be realised or, at the AOFM's discretion, may continue to be held as part of its total investment portfolio, taking account of the objectives of this Direction and the expected return and risk on these securities in relation to the management objectives of its total portfolio. Sales of the securities should be undertaken without causing market volatility. Note that this direction does not limit directions 6 and 7.

Pursuant to paragraph 62A(5)(b) of the Act, I direct that delegates must comply with any instructions relating to administrative arrangements, procedures, limits, controls or other matters of detail relating to investment within the framework established by this Direction and my Directions of 13 July 2008, where those instructions are given in writing by the Secretary to the Treasury or by the Chief Executive Officer of the Australian Office of Financial Management.

Dated this

16th

day of

October 2008

WAYNE MAXWELL SWAN

Treasurer of the Commonwealth of Australia