TITLE:

Guardians of New Zealand Superannuation

2021/22 Review

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CHAIR

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EVENT | PRESENTATION:

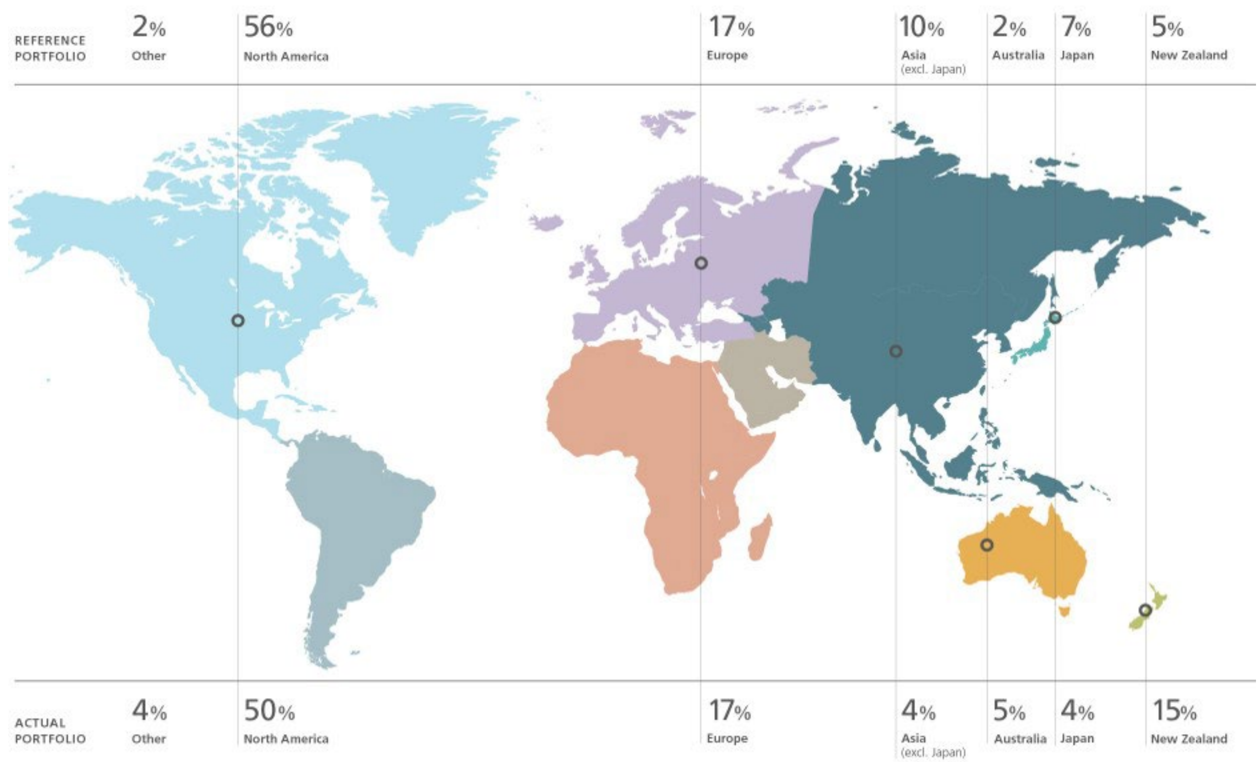
Finance & Expenditure Select Committee, 8 February 2023

#3138337

Agenda

- Our role and mandate
- Investment approach
- Investing in New Zealand
- Benchmarking
- Performance
- ESG
- Reset of RI Strategy
- Climate Change
- Outlook

Where we invest



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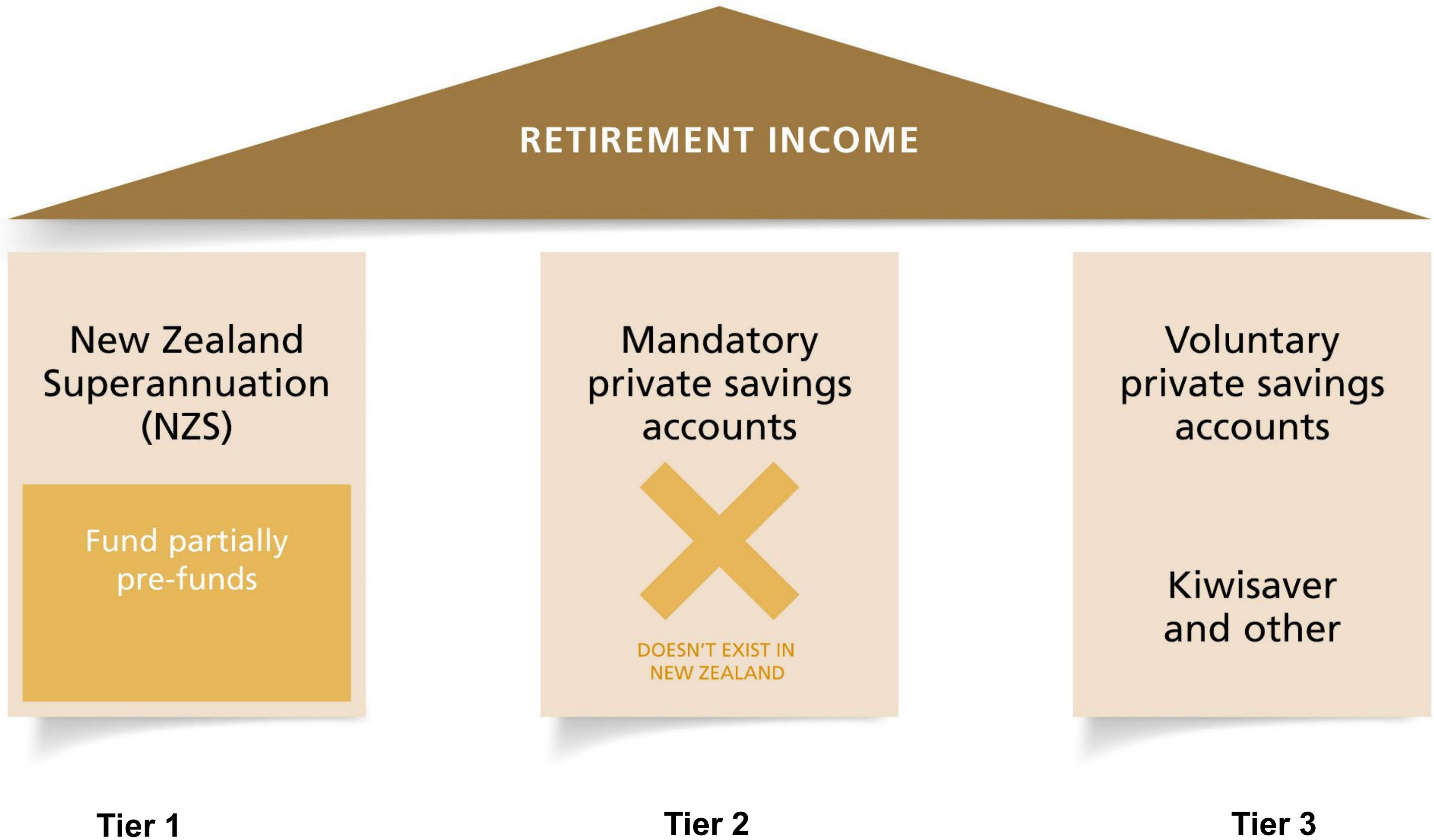
Where we fit in – part prefunding Tier 1

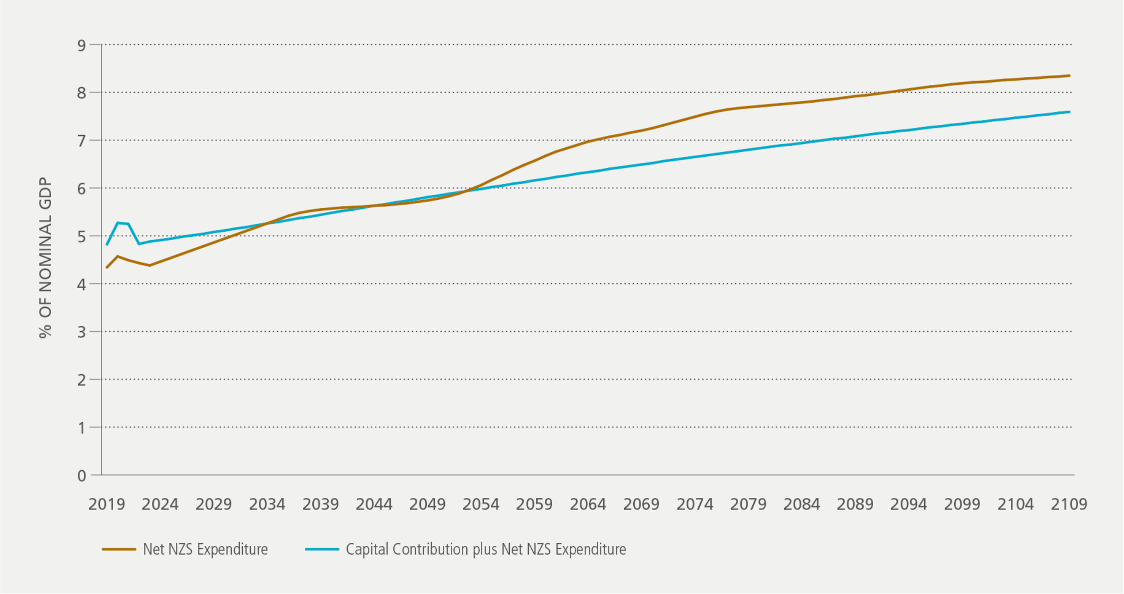


- The NZ Super Fund is expected to pre-pay approximately 20% of NZ superannuation costs by 2040
- Contributions were suspended from July 2009 and restarted in December 2017

NZ Super Fund’s role

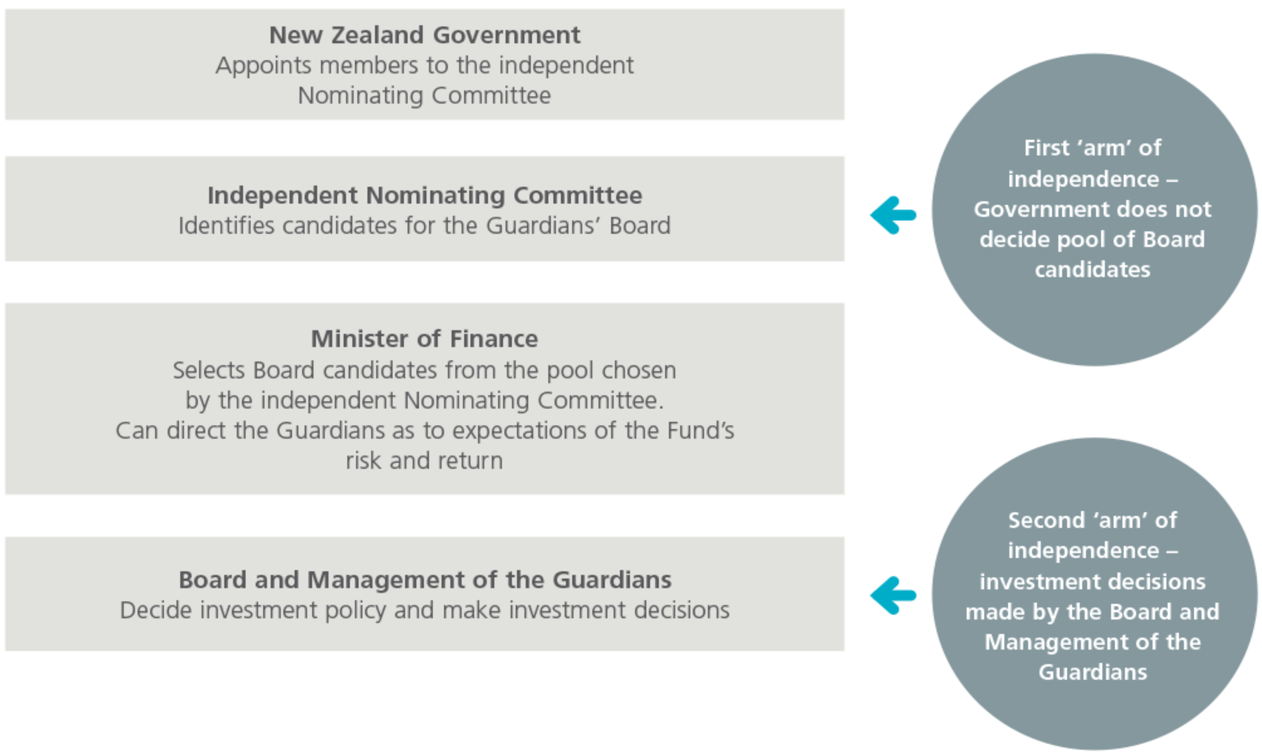
- The NZ Super Fund exists to ‘smooth out’ the increasing cost of government-provided superannuation. By contributing to the Fund out of current taxes, a pool of wealth (the Fund) is created that can be used to partially pay for superannuation, reducing the need for future generations of workers to see taxes rise or government spending cuts.
- At a future date, dependent on the growth of superannuation costs versus that of the economy and the Fund’s performance, the government of that time will be able to receive funds each year from the Fund, rather than provide it with funds (contributions). This will help future taxpayers partially cover the costs of superannuation, which will have risen not just in nominal terms but, more significantly, as a share of the economy.

Contribution rate graph



Governance framework

- The Guardians of New Zealand Superannuation is an autonomous Crown entity, legally separate from the Crown, and operates at double arms' length from Government.
- The Guardians manages and administers the NZ Super Fund. The Fund is a pool of Crown assets.



Mandates

- **NZ Super Fund Mandate** (Act of Parliament, 2001):
  - The Guardians must invest the NZ Super Fund on a prudent, **commercial** basis and must manage it in a manner consistent with:
    - Best-practice portfolio management;
    - **Maximising return without undue risk** to the Fund as a whole; and
    - Avoiding prejudice to New Zealand's reputation as a responsible member of the world community.

- **Venture Capital Fund Mandate** (Act of Parliament, 2019):
  - The Guardians must invest the venture capital fund in New Zealand's venture capital markets using best-practice investment management that is appropriate for institutional investment in those markets. It must manage and administer the fund in a manner consistent with:
    - The policy statement; and
    - Avoiding prejudice to New Zealand's reputation as a responsible member of the world community.

Our purpose and vision

Our purpose:

Sustainable investment delivering strong returns for all New Zealanders

Kia toitu- te haumi hei hua ma- ngata- ngata katoa o Aotearoa

Our vision:

An inclusive team creating a better future through investment excellence

Ma- te kotahi a - -kapa, ma - te kounga a - -haumi, ka tino eke ki tua

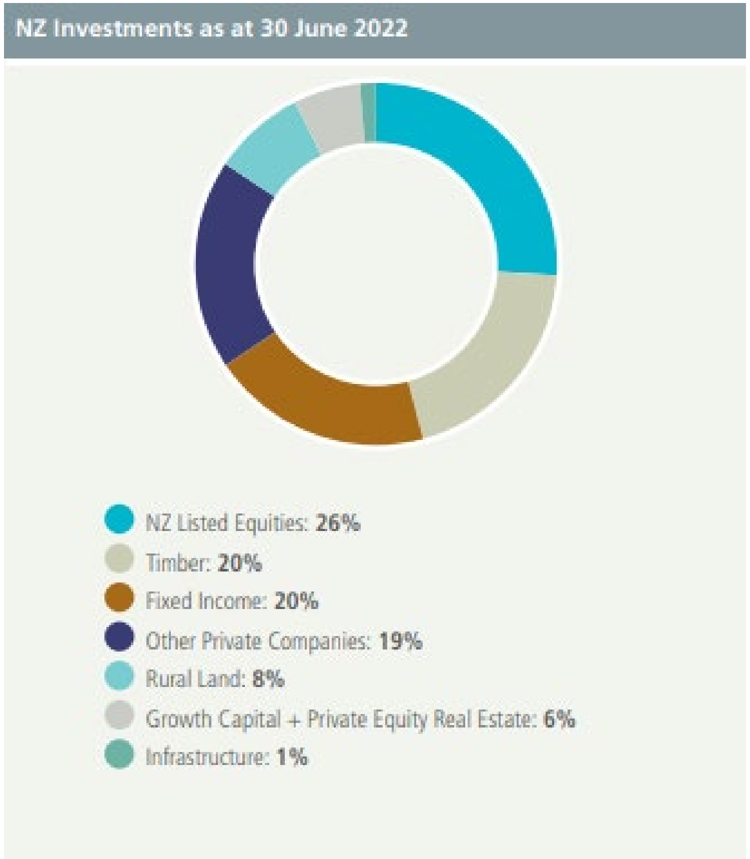
Investment approach

We look to utilise the NZ Super Fund's liquidity profile, long-term investment horizon and governance strength

- We construct a portfolio that balances our highest estimated return with financial risk → the best likelihood of success:
  - First capital withdrawals not currently scheduled until 2034-35;
  - Strong weighting towards growth assets (because we can ride out short-term volatility).
- Principles and advantages of long-term investment:
  - A clear purpose + long horizon, highly liquid, operationally independent;
  - Discipline and capacity to stay the course – governance;
  - Transparency and clear communication with stakeholders;
  - Focus on best-practice, including environmental, social and governance (ESG) factors.

Investing in New Zealand

- Ministerial Directive (2009)
  - "…that opportunities that would enable the Guardians to increase the allocation of New Zealand assets in the Fund should be appropriately **identified** and **considered**…"
  - "This direction is not intended to be **inconsistent** with the Guardians' duty to invest the Fund on a prudent commercial basis, in accordance with section 58 of the Act, and the above paragraph is subject to that duty."
- As at 30 June 2022, the Fund had $8.5 billion invested in New Zealand.
- In the 11 years since we received the Directive, the proportion of the overall Fund that is invested in New Zealand (in value terms) has dropped from 21% to 15%. The proportional drop reflects the strong performance of global equities in recent years, even after significant new investments in New Zealand.
- The Fund is one of the largest institutional investors in New Zealand and plays a significant role in New Zealand's capital markets
- Investments include Datacom, Fidelity Life, NZ Gourmet, Kaingaroa Timberlands, Asia Pacific Health Group (APHG), NZ dairy farms, housing, NZ equities and (via external managers) in growth capital and infrastructure.



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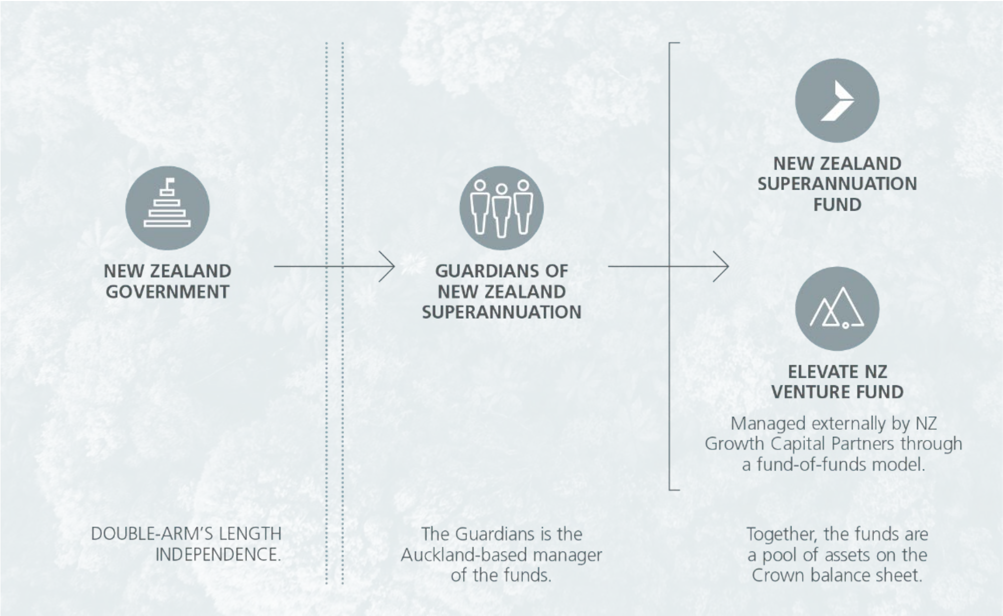
Investing in NZ: Developing NZ’s venture capital market

- The Elevate NZ Venture Fund consists of $260 million of initial Crown commitments, expected to reach $300 million over time.
- Guardians oversees NZ Growth Capital Partners (NZGCP) management of Elevate Fund’s investment into a fund of venture capital funds.



ELEVATE
NZ VENTURE FUND

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Elevate NZ Venture Fund - Framework

- Venture Capital Fund Act 2019
  - **Purpose**: of Elevate NZ Venture Fund a) capital to NZ companies; b) develop NZ venture capital markets
  - **Our mandate:** to apply best practice investment management appropriate for institutional investment in context of NZ venture capital markets
  - **Benchmark:** no financial return benchmark
  - **NZGCP:** appointed external manager
  - **Fund of funds model**: NZGCP allocates capital to fund managers who can attract matching private sector capital; fund managers deploy capital to investee companies

- Market Development: NZGCP tasked with wider market development
- Elevate NZ Venture Fund launched in March 2020
- Legislation supported by Policy Statement
  - Sets broad investment parameters to ensure capital deployment aligns with policy intention
  - Elevate NZ Venture Fund capital to be “wholly or substantially” invested in NZ entities and through NZ connected funds

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Offshore wind in the South Taranaki Blight

In March 2022 we announced our partnership with Copenhagen Infrastructure Partners (CIP) to explore the potential for large-scale offshore wind energy in the South Taranaki Bight. Subject to feasibility, an initial planned 1GW development would represent over 11% of New Zealand's current electricity demand capacity and could power over 650,000 homes. We believe the project could later expand to 2GW, helping to meet strong projected growth in demand for electricity in New Zealand.

Benchmarks

We benchmark against best practice industry principles, measures and relevant global peer funds

	Internal measures and mechanisms	External measures	Stakeholder engagement
Cost structure	By business unit By investment opportunity Holistic view of fees	CEM Benchmarking Survey Hay remuneration database	Peer fund engagement: • 3Cs: Comparison, collaboration and co-investment Global expertise
Governance	Reference Portfolio Review Internal Audit	Independent Reviews ‘04, ’09, ’14, ‘19 OAG special performance audit (‘08) SWF GAAP Select Committee Reviews	
Performance	NZ T Bill rate + 2.8% Reference Portfolio + 1.0%	Performance against both measures published monthly	
Transparency	Website Annual Report OIA	Sovereign Wealth Institute’s Transparency Index	
Responsible Investment		UNPRI assessments	
Risk	Risk Committee Reviews Risk Registers Investment Risk Limits Target Liquidity Level	CEM Benchmarking Survey	

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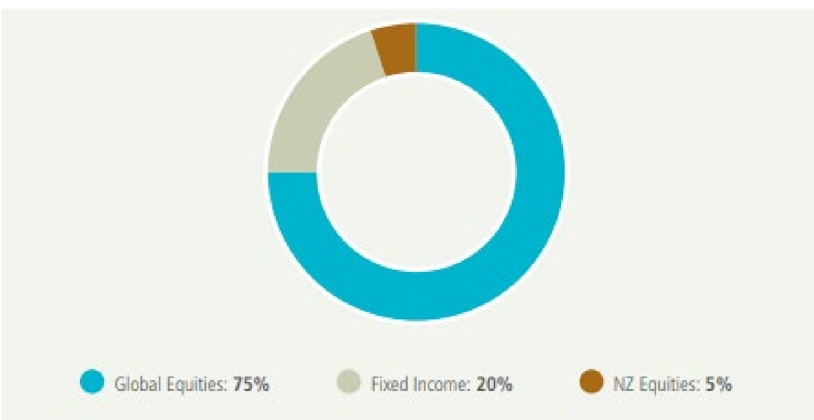
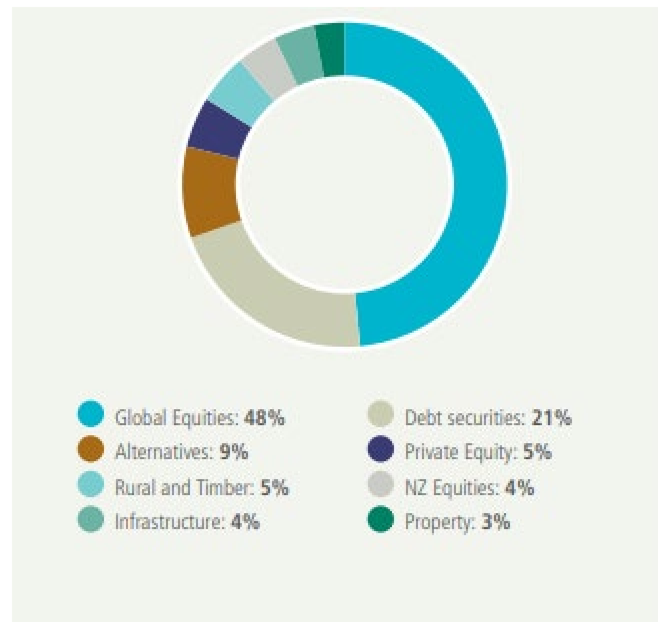
Reference portfolio + active investments = Actual Portfolio

Growth-oriented portfolio, majority passive, highly diversified

Reference Portfolio as at 30 June 2022



Actual Portfolio as at 30 June 2022



* Excludes the impact of any strategic tilts. Totals do not add to 100% due to rounding.

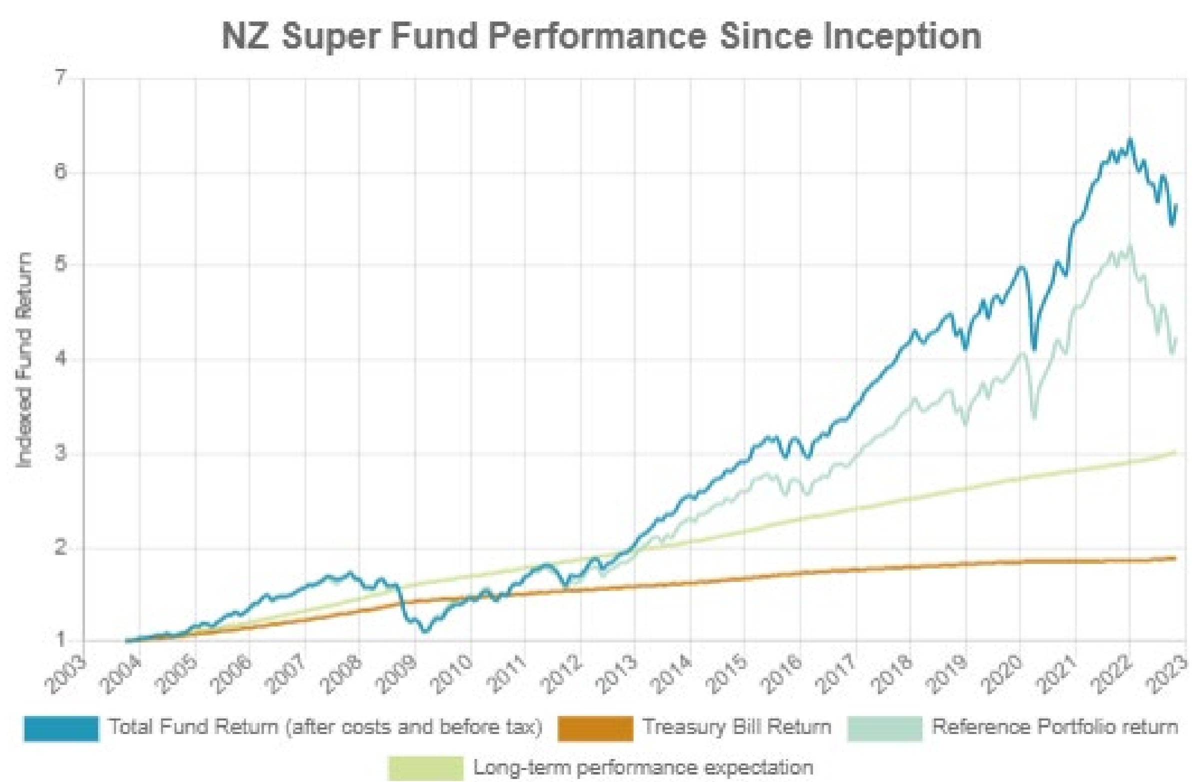
Performance

Despite a negative return, the NZ Super Fund proved resilient to ongoing volatility and added a record $4.5 billion in value above its Reference Portfolio benchmark this year.

In 2021/22 the impact of the challenging market conditions was cushioned by a highly successful year for active investment strategies. Strategies ranging from strategic tilting to timber, global macro, tactical credit and equity factors mandates did well during what was a volatile period, delivering very strong returns.

Performance

This graph shows what has happened to the first dollar invested in the Fund over time.



Exceeded Reference Portfolio by $13.29 billion (1.63% pa)

Exceeded Treasury Bills by $34.61 billion (6.28% pa)

Total Fund Return 9.65%

Reference Portfolio return - the best **passive**, list "market" return that would achieve the Fund's objectives over time

Treasury Bill return - a measure of the cost to the Government of contributing to the Fund instead of paying down debt

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Performance (as at 30 June 2022)

	Quarter to June 2022	Last 12 months	Last 5 years	Last 10 years	Since inception
Contributions received	$605m	$2.4b	$7.5b	$7.5b	$22.4b
Actual Fund Return	-7.26%	-6.99%	8.09%	12.06%	9.65%
Reference Portfolio Return	-12.64%	-14.24%	5.98%	9.41%	8.02%
Value-Added (Actual return less Reference Portfolio return)	5.39%	7.25%	2.11%	2.65%	1.63%
NZ tax (paid) / received*	$145m	$(2.12)b	$(4.19)b	$(7.57)b	$(9.75)b
Closing Fund balance			**$55.7b**		

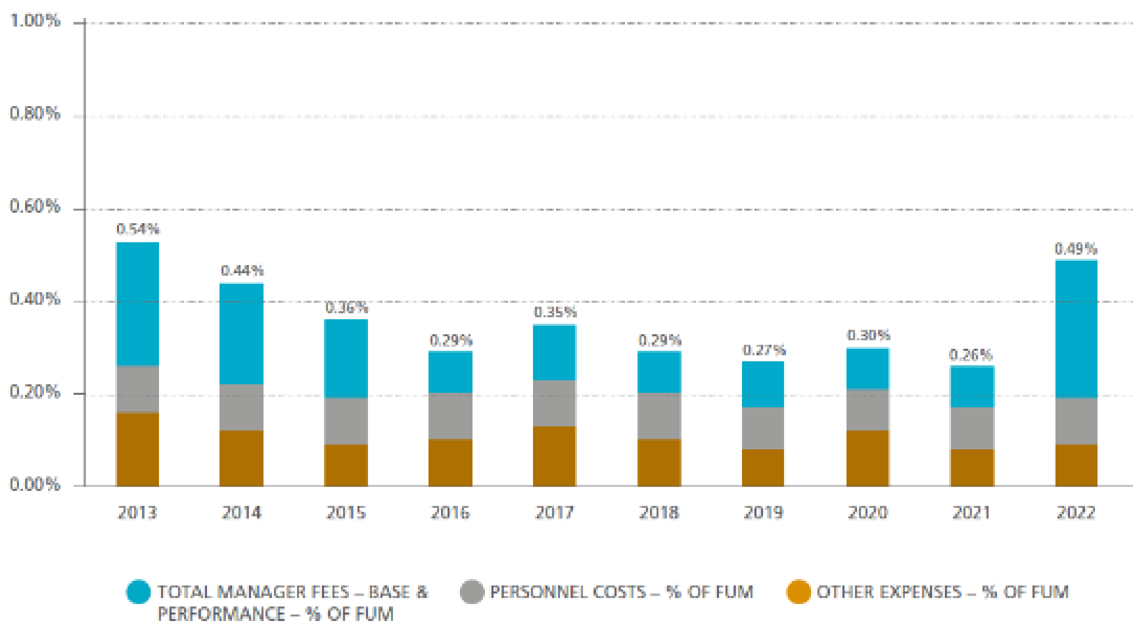
Cost

CEM (Cost Effectiveness Management) Benchmarking is the global leader in benchmarking pension and sovereign wealth funds

- CEM's latest report found our net value-add was above the median of our peers and costs were below the median over the relevant five-year period

- The Fund is described as "low cost" because it had a lower cost implementation style and paid less than peers for similar services

Fund Expenditure as a Percentage of Funds Under Management (10 Years)
as at 30 June 2022



ESG integrated into the investment process

Environmental, social and governance factors, including climate change, are integrated into the investment process

As share owners, we manage ESG through collaboration, engagement and, in some cases, exclusions

Our performance on ESG is measured through global benchmarking

Climate change is an investment risk

As a Fund with a very long horizon, we believe climate change is one of the Fund's most critical investment risks and opportunities.

WORKSTREAMS

REDUCE decreases the transition risk of the portfolio. We do this by:
- measuring our carbon footprint;
- setting a target to reduce our portfolio's emissions intensity and our holdings of potential emissions from reserves; and
- applying a bespoke carbon methodology to our equity portfolio and our benchmark.

ANALYSE integrates climate change considerations into our assessment of potential new investments and when we review our existing holdings. We do this by building climate change scenarios into our valuation framework.

ENGAGE influences the companies we own an interest in to continuously mitigate and improve resilience to climate-related risks. We do this by being an active owner, including prioritising engagement and voting in accordance with our climate change views.

SEARCH focuses us on finding companies that will thrive during the low-carbon transition. We do this by actively searching for new opportunities in the areas such as alternative energy, energy efficiency and transformational infrastructure

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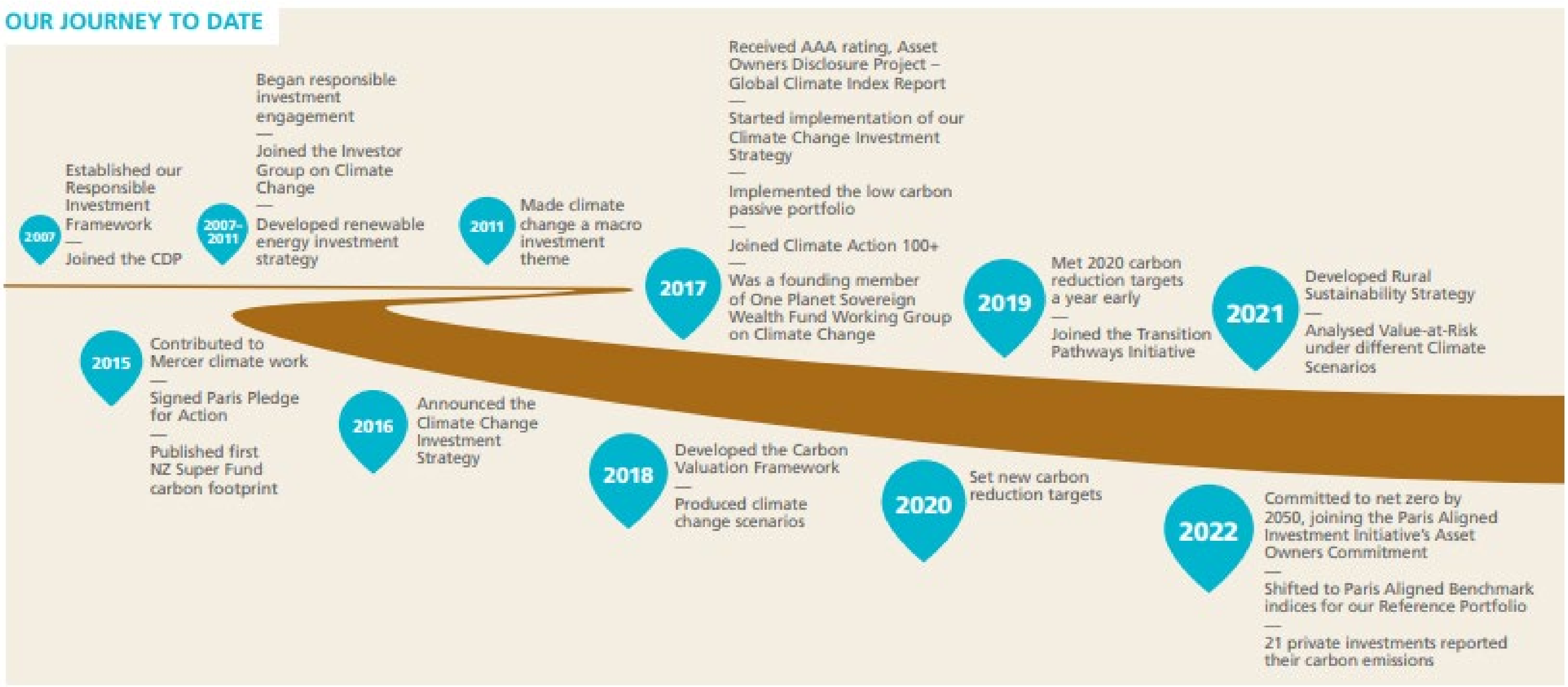
Climate strategy implementation

Reduce, Analyse, Engage, Search



Net zero alignment

- The NZ Super Fund has met its 2025 targets for reducing its carbon emissions and exposure to reserves. Carbon intensity has been reduced by 49% and fossil fuel reserves by 91%, compared to market levels.
- We are now moving to align the Fund’s carbon reduction targets with the goal of net zero by 2050.
- This year, as part of our Reference Portfolio Review, the Board elected to change the ACWI IMI building block of our Reference Portfolio to the MSCI World Climate Paris Aligned Index and the MSCI EM Climate Paris Aligned Index.
- As well as improving the overall ESG profile of the Fund, these indices will ensure that the Fund’s passive equity positions are better aligned with net zero objectives.

Climate Action Plan

Sustainable Finance Framework

RI COMPASS REVIEW PHASE 1 – 2020/21

Changing Mindsets
- Emerging trends & stakeholder research
- Review of policy & regulatory trends, our mandate
- Willis Towers Watson & best practice review
- Sustainable Finance Strategy developed & approved

Transforming Finance
- Research on ESG, best practice, peer practice
- Research on improving ESG performance (equities)
- CFIs & Net-Zero/Paris alignment methods

Financing transformation
- Link between Positive (Impact) Investment & our mandate;
- Impact investment research, review of peers & market
- Understanding internal barriers
- Options to increase number & scale of impact investments

RI COMPASS PHASE 2 – CAPACITY BUILDING 2021/22

Changing Mindsets
- Sustainable Finance reflected in Guardians' Mission/ Vision
- SIPSP updated
- Join Centre for Sustainable Finance
- UNPRI sustainability outcomes
- CFI Framework/Net Zero commitment; engagement

Transforming Finance
- Test, approve, apply ESG performance methodologies for equities, ESG in private markets; improve ESG data
- ESG in Risk Budget Review
- CCIS: Net Zero alignment
- Engage/exclude review

Financing transformation
- Deepen PI integration & resourcing; experiment
- Sustainable financial system engagement (external)
- Impact measures

RI COMPASS PHASE 3 – SCALING UP 2022/23

Changing Mindsets
- SF in personal objectives; build capability
- SF in SOI & SIPSP
- Measurement, reporting

Transforming Finance
- ESG equity portfolio established, monitored
- Improving ESG across other investments
- ESG data platform & research deepened
- CCIS/Net-Zero alignment
- External engagement
- Engage/exclude review

Financing transformation
- Increased impact AUM and scale of impact; climate solutions a focus
- Refining definitions, measurement, reporting
- Options for mapping impact

MATURING 2023-2025

Changing Mindsets
- SF reporting
- 5-yearly Independent Review

Transforming Finance
- Mature ESG performance strategy
- Mature data
- ESG consideration in 5-yearly Reference Portfolio review
- Review CCIS Targets

Financing transformation
- Mature Impact strategy
- Assess, review and adjust as needed
- Mapping impact where appropriate

IN OUR DNA 2026-30...

Changing Mindsets
- 5-yearly Independent Review (2029)

Transforming Finance
- ESG embedded – building best practice standards
- Outcomes mapped to SDGs (if appropriate)

Financing transformation
- Impact core to investment strategy
- Accounts for significant part of AUM
- Outcomes mapped to SDGs

Outlook

- The Fund's advantages (our endowments) – long-term horizon, known liquidity, operational independence and Crown ownership – give us important advantages as an investor.
- The Fund continues to be strongly weighted to growth assets – we are prepared to weather short-term volatility for a better long-term return.
- We remain interested in investing in large-scale infrastructure and real estate projects (both in New Zealand and internationally), which we see as attractive investment opportunities because of their consistent, competitive returns and yields, and diversification benefits.
- 2022 was a volatile year for financial markets, and we expect this to continue into 2023 as the economic and market implications of policy decisions by central banks to manage inflation are navigated. As a long-term investor we are prepared to weather the ups and downs of the market.
- Operationally, we are focused on:
  - Fewer, deeper relationships with external investment managers
  - Increased direct investment where we have an advantage, including in NZ
  - Scalability and efficiency as the Fund continues to grow – maturing the organisation to manage a much larger Fund over time
  - Implementing the Crown Responsible Investment Framework alongside fellow Crown investors