STATEMENT OF INTENT

FOR THE PERIOD COMMENCING 1 JULY 2013 TO 30 JUNE 2018

Guardians of New Zealand Superannuation

WORKING FOR THE
FUTURE OF ALL
NEW ZEALANDERS

NEW ZEALAND
SUPERANNUATION
FUND

Contents

FOREWORD FROM THE

1 Board Chair

GAVIN WALKER
CHAIR

On behalf of the Guardians of New Zealand Superannuation I am pleased to present my first Statement of Intent as Chair.

It is now over a decade since the Guardians was established by the New Zealand Superannuation and Retirement Income Act 2001, and the forthcoming 2013/14 year will mark ten years since the first Fund investments were made in September 2003.

In the intervening period the Guardians has grown into a world-class investment organisation with a strong track record; strategies aligned to its long-term focus; and robust policies, processes and infrastructure.

In succeeding David May as Chairman of the Guardians, I have been conscious of the importance of continuity and of the need to take a long-term view of the Guardians and Fund.

This focus on the long-term is driven by Guardians' purpose – *to maximise the Fund's return over the long-term, without undue risk, so as to reduce New Zealanders' future tax burden.*

The 2013-2018 Statement of Intent, which is based on the third year of an established strategic plan, therefore has a high degree of continuity with previous SOIs.

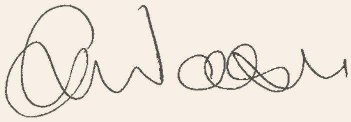
This Statement of Intent, however, also reflects the fact that we are nearing the end of the 'build' phase of the Guardians' evolution, and are shifting our focus firmly to 'operate'. Consistent with this shift, this year we have introduced 'efficiency, scalability and innovation' as a new strategic objective for the Guardians.

In line with our long-term focus and in recognition of the 10-year milestone, we have also moved to 10-year performance measures, as opposed to 5-year measures used during the Guardians' establishment phase. We remain, however, firmly focused on our long-term outcome, and committed to our preferred method of measuring our performance over rolling 20-year periods.

The Guardians' Target Operating Model, introduced in the 2012/13 year, is a key reference point for the Statement of Intent. The Target Operating Model, which established an ideal view of the activities and resources required to support our strategic objectives in the medium term (five years out), can be summed up as a "simpler and more direct approach". Under our ideal operating model, the Guardians and Fund have:

- concise investment processes that enhance our ability to consistently rank investment opportunities and prioritise our efforts;
- greater influence over the allocation of our capital to different investment risks;
- fewer, but deeper, external manager and advisor relationships, based on more of a partnership approach; and
- a more concentrated, active investment portfolio (as opportunities in which we have high confidence arise).

An overview of the Guardians' and Fund's 2013-18 strategic plan and objectives can be found on page 4. Further details of our planned activities can be found in the Forecast Statement of Service Performance (FSSP) on page 12.



GAVIN WALKER, CHAIR

INTRODUCTION TO THE

2 Guardians and Fund

The New Zealand Superannuation Fund and the Guardians of New Zealand Superannuation were established by an Act of Parliament to reduce the tax burden on future New Zealand taxpayers of the cost of New Zealand Superannuation.

Over the next few decades, the New Zealand population will age significantly. Statistics New Zealand predicts that the population aged 65 years and over will surpass one million by the late 2020s, compared with 550,000 in 2009. The 65+ age group will also grow as a proportion of New Zealand's total population, increasing from 13% in 2009 to more than 20% by the late 2020s. By the late 2050s, one in every four New Zealanders will be 65 years or older.

This means New Zealand will have:

- more people of retirement age, as a proportion of the population, than ever before; and
- fewer 'working-age' people whose productivity can be tapped, through taxation, to fund the greater cost of retirement income.

These projections have significant implications for future Governments' ability to fund other vital areas such as health, welfare, education and law enforcement. This information is therefore relevant for all New Zealanders, now and in the future.

HOW DOES THE FUND RESPOND TO NEW ZEALAND'S AGEING POPULATION?

The NZ Superannuation and Retirement Income Act 2001 (the Act) established:

- the Fund, as a pool of assets on the Government's balance sheet; and
- the Guardians, as a Crown entity charged with managing the Fund.

Together, the Fund and Guardians exist to 'smooth' the tax burden arising from the higher future cost of New Zealand Superannuation between generations of New Zealanders.

The tax smoothing occurs through the Government making contributions to the Fund. At a future date – currently in the 2029/30 financial year – the Government will begin to withdraw money from the Fund to help to meet the cost, at that time, of New Zealand Superannuation.

Saving now for this future cost is called 'pre-funding' New Zealand Superannuation. Pre-funding means that future Governments do not have to seek as much from future New Zealand taxpayers (or from other sources, such as debt) to meet the increasing cost of New Zealand Superannuation.

This is reflected in our Mission Statement: "Maximise the Fund's return over the long term, without undue risk, so as to reduce future New Zealanders' tax burden."

We believe this statement frames the purpose of the Guardians and Fund in a way that is meaningful to all New Zealanders.

HOW DO WE REFLECT THIS CONTEXT IN OUR STATEMENT OF INTENT?

We think of it this way:

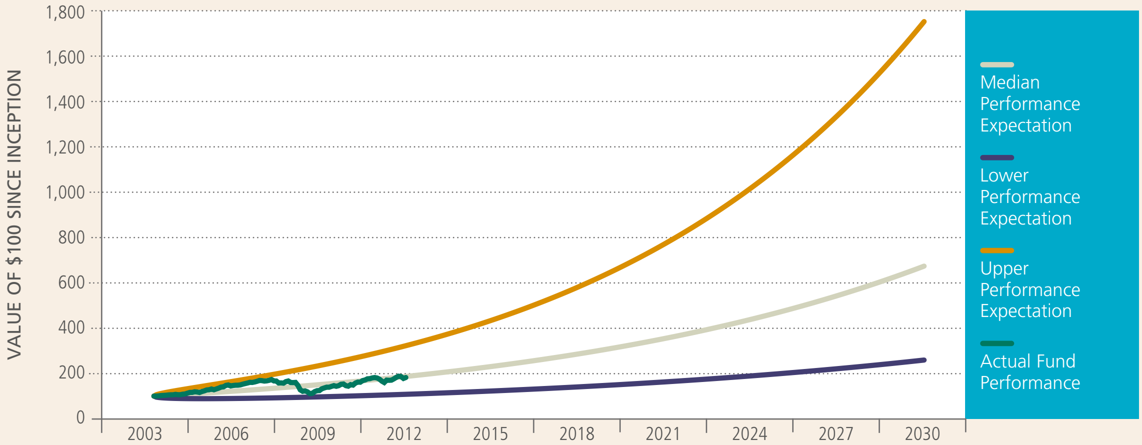
1 The Fund is a special-purpose savings vehicle giving certainty that some of the future cost of New Zealand Superannuation is covered. The Fund is also expected to add to Crown wealth over the long term by earning more for the Government in investment returns than the Government would save in debt servicing. By doing this the Fund adds to Crown wealth, improves the ability of future Governments to meet increased superannuation commitments and ultimately reduces the tax burden on future New Zealand taxpayers of the cost of superannuation. That is the Fund's long-term outcome, and we discuss how we have framed it for shorter-term measurement in our Outcome Framework on page 5.

2 Our Act requires us to manage the Fund in a commercial, prudent fashion, comprising:

  - best-practice portfolio management;
  - maximising return without undue risk; and
  - avoiding prejudice to New Zealand's reputation as a responsible member of the world community.

In our Statement of Intent we frame our output simply as 'managing the Fund' consistent with this mandate. This is also captured in the Outcome Framework on page 5.

Actual & Estimated Fund Returns to 2030 (projected commencement of withdrawals)



LONG-TERM PURPOSE

This graph plots actual and estimated Fund performance relative to our expectation that the Fund should outperform the risk-free rate of return (as measured by 90-day Treasury Bills) by 2.5% p.a. averaged over rolling 20 year periods. It shows expected returns through to 2030, when the first withdrawals are projected to take place.

As well as demonstrating that the Fund is still in its early days relative to its long-term purpose, the graph illustrates how, because of its weighting to growth assets, the Fund can experience large short-term movements. These shifts must be seen in the context of the long-term purpose of the Fund.

Upper, median and lower performance expectations, within a 95% confidence level, are shown. For the period the Fund has been invested, these expectations are based on the actual risk-free rate of return. For future periods, our projections are based on the current risk-free rate of return.

WHAT OTHER CONTEXTUAL CONSIDERATIONS ARE IMPORTANT?

Firstly, as a result of the Global Financial Crisis, in the 2009 Budget the Government decided to reduce contributions to the Fund until the Crown operating balance returns to a level of surplus that is sufficient to resume contributions. At present the Treasury estimates this will be in the 2017/18 fiscal year.

Secondly, our activities and profile in New Zealand are important for a number of reasons. We have a Directive from the Minister of Finance requiring us to actively identify and consider opportunities to increase the allocation of New Zealand assets in the Fund, subject to our mandated duty to invest on a commercial, prudent basis. From an investment perspective, we see New Zealand as a market we should have an advantage in; and it is an important part of our search for new opportunities. From an organisational perspective, it makes sense to work closely with other Crown Financial Institutions. We also see a significant benefit in ensuring our relationship with key domestic stakeholders is as transparent as possible.

Thirdly, we place a high priority on responsible investment, consistent with our mandate to adopt best practice portfolio management and avoid prejudice to New Zealand's reputation as a responsible member of the world community. We believe environmental, social and governance factors can impact on long-term financial performance. It is therefore important that our investment strategies take relevant regulatory, market, reputational and operational risks and opportunities into account. Environmental, social and governance considerations are integrated into investment decisions and our active voting and engagement programme encourages companies to apply good stewardship in these areas.

Want to know more?

If you are interested in further information about the reason why the Guardians and the Fund exist, more on the ageing population issue and how the Guardians and Fund are designed to respond to it, you can find it on our website www.nzsuperfund.co.nz.

3 Strategic Direction

The Guardians' 2013-2018 Strategic Plan was approved by the Board on 9 April 2013. The Plan sets out what success will look like for the Fund in the medium term, and includes details of key activities to be undertaken in the 2013/14 year. The Plan contains four strategic objectives: 'best portfolio'; 'collaboration with peers'; 'building & maintaining a great team'; and 'efficiency, scalability & innovation'.

'Best portfolio' combines two objectives from the previous year: 'leadership in investment search, evaluation and selection and 'significantly progress implementing value-add strategies.' 'Efficiency, scalability & innovation' is a new strategic objective. As outlined in the Chairman's Foreword, this new objective recognises a shift in the Guardians' evolution from build to operate. The Guardians' previous Strategic Plan and Statement of Intent included a fifth strategic objective, 'risk management'. After a range of initiatives to further embed risk management practices during 2012/13, we have chosen to remove it as a specific strategic plan objective this year. Risk management will continue as a key business-as-usual work programme with performance measures outlined on page 9-10 of this Statement of Intent.

2013-2018 STRATEGIC PLAN OVERVIEW

Best Portfolio

Best Portfolio means the most cost-effective and fit for purpose.

By cost-effective we mean that we pay minimum cost for pure market exposure and only pay more if we have a high level of confidence of value being added. It also means we have an efficient business model and understand the optimal trade-off between internal and external service delivery.

Fit for purpose means that the portfolio will maximise the Fund's return net of costs without undue risk and according to responsible investment principles.

High priority activities include focusing on implementation efficiency, promoting faster and more efficient deal progress and further developing the Risk Allocation Process (RAP). (See page 14 for more information).

Collaboration with peers

For a small, geographically isolated fund like ours, collaboration with peers across the world offers a range of strategic benefits. Building relationships with leading global peers has therefore been a key strategy since we started, and continues to be important.

The benefits of collaboration include leveraging these relationships to secure global and local opportunities for co-investment; exchange of best practice and knowledge; and cooperation in areas of joint interest, such as responsible investment.

Our current focus is on building relationships with peer funds identified as being most likely co-investment partners. We aim to agree areas of common interest, so that co-investment search is focused, and demonstrate that we have the capability to assess opportunities. Co-investments require an alignment of strong relationships and equally valued opportunities.

Building and maintaining a great team

Giving effect to our Statement of Intent will require strong leadership; a shared understanding among staff of our purpose and values; and talented, committed people with access to quality data, systems and tools.

In particular, being able to attract, retain and develop high calibre people in what is a global, highly competitive market is vital to the performance of the Fund.

We aim to embed the Guardians' vision, values and culture as a meaningful part of the business; translate business strategies into clear role requirements, accountabilities and competencies; and drive productivity and business performance through compensation, performance management and leadership and coaching programmes.

Efficiency, scalability & innovation

The Guardians' Target Operating Model sets out how we will continue to build operations and technology capabilities that are agile and scalable.

We seek to implement best practice investment and operational processes and workflows, and to have a high degree of transparency over our organisation and activities.

We actively seek opportunities to measurably improve our investment practices.

4 Outcome Framework

The Fund's ultimate outcome is to reduce the tax burden on future New Zealand taxpayers arising from the cost of New Zealand Superannuation.

This is a long-term outcome, the results of which will not begin to be realised until around 2029/30, when withdrawals from the Fund will begin. In the short- and medium-term, we focus on facilitating this outcome by investing the Fund on a commercial, prudent basis and 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.

Our single output is managing the Fund. This involves business-as-usual work programmes covering:

- Investment;
- Cost control;
- Risk management;
- Governance; and
- Organisational capability.

Under each work programme we have identified relevant Strategic Plan objectives and linked activities to focus and prioritise our efforts over 2013/14. Together these objectives and activities comprise our Forecast Statement of Service Performance (FSSP) at page 12.

Successfully implementing the Strategic Plan-aligned activities contained in the 2013/14 FSSP will help achieve our ultimate goal and outcome – to maximise the Fund's returns over the long term, without undue risk. It is important to understand that achieving this outcome is not a simple success/fail equation. We aim to beat our performance outcome expectations by *as much as possible*. This is why we have such a strong emphasis on innovation and on benchmarking against global best practice. Selected 2013/14 activities are highlighted on page 14.

2013-18 STRATEGIC OBJECTIVES AND ACTIVITIES:

- Forecast Statement of Service Performance 2013/14

2013/14 ACTIVITIES:

- Refine Risk Allocation Process (RAP)[1]
- Launch internal NZ active equities mandate
- Relationship management and seeking co-investment opportunities
- Implementation of performance system, education programme, central clearing
- IT roadmap
- Intranet and website redevelopment

WORK PROGRAMMES – ACTIVITIES/ OUTPUT:

- Investment
- Cost control
- Risk management
- Governance
- Organisational Capability

OUTPUT:

- Managing the Fund

OVERALL GUARDIANS' AND FUND EXPECTATIONS:

- Maximising return without undue risk, to reduce the tax burden on future New Zealand taxpayers of the cost of New Zealand Superannuation as measured, over rolling 20 year periods, by beating
  – the 90-day Treasury Bill rate by at least 2.5% p.a.;
  – the Fund's Reference Portfolio or passive benchmark.

1 See page 14 for more information about the Risk Allocation Process.

MEASURING OUR

5 Performance

We have set out on pages 6-11 a range of measures for the Fund's financial performance and for each of the work programmes listed above. We will report on progress against each measure in our Statement of Service Performance (SSP) in our Annual Reports from 2014 onward, depending on the time period of the goal.

5.1 EXPLANATION OF PERFORMANCE MEASURES

5.1.1 Outcome measures – progress towards our ultimate goal

Long-term context

On current Treasury projections the Government will not begin capital withdrawals from the Fund until 2029/30, and the Fund will not peak in size until the 2050s – some 40 years from now.

Setting targets in a five-year Statement of Intent for such a long-term outcome presents a challenge. To illustrate: at current policy settings, the Statement of Intent for the five years beginning 1 July 2025 will be the first to cover a period of actual withdrawals from the Fund.

However, the Fund has now been invested since September 2003, and there is considerable interest in its progress. This Statement of Intent sets out short, medium and long-term performance measures against which New Zealanders can track the Fund's progress.

These one, 10 and 20 year period performance measures are specific and quantitative. We will report on performance against each measure in the Statement of Service Performance (SSP) contained within the relevant period's Annual Report. These measures concern the Fund's performance and its volatility over time.

Treasury Bills measure

It is the Guardians' expectation, given our mandate and hence portfolio construction, that the Fund will return at least the Treasury Bill rate + 2.5% p.a. over any 20-year moving average period. This expectation is based on the long-run equilibrium return assumption for each asset class within the Fund.

It is important to understand that the Treasury Bill rate + 2.5% is not a target to be hit precisely – rather, it is a long-term performance expectation that we aim to beat by as much as possible.

We strongly prefer to work to an expectation rather than a target, to avoid any short-term incentive to simply add risk to the Fund if expected returns are low, i.e. increasing risk when returns are least rewarding – and vice versa.

Treasury Bills, which are wholesale debt securities issued by the Crown, are an appropriate measure of the Fund's performance. This is because they both proxy the 'opportunity cost' to the Government of contributing capital to the Fund, instead of using the money to retire debt and are seen as the most risk-free asset. Over time, the Fund is expected to earn more for the Government in investment returns than it would save in debt servicing i.e. the Fund is expected to add to Crown wealth, enhancing the ability of future governments to meet increased superannuation costs.

Reference Portfolio measure

We also use a Reference Portfolio, which is set by the Guardians' Board, to benchmark the performance of the Fund's actual investment portfolio and the value we are adding.

The Reference Portfolio, which is capable of meeting the Fund's objectives over time, is a shadow or notional portfolio of '**passive**', low-cost, listed investments suited to the Fund's long-term investment horizon and risk profile. It has an 80:20 split between growth and fixed income investments and its foreign currency exposures are 100% hedged to the New Zealand dollar.

		1-YEAR	10-YEAR	20-YEAR
Where Reported		**SSP, 2014 Annual Report**	**SSP, 2023 Annual Report**	**SSP, 2033 Annual Report**
MEASURE	Reference Portfolio Returns above Treasury Bills (per annum)			
	• expected outcome	2.5% p.a.	2.5% p.a.	2.5% p.a.
	Actual Fund Returns above Reference Portfolio (per annum, net of costs)			
	• expected outcome	1.1% p.a.	1.3% p.a.	1.3% p.a.
	In a 1-in-100 year event, potential Reference Portfolio loss			
	• expected outcome	≥ -31% p.a.	≥ -4% p.a.	≥ -3% p.a.

Predicting short-term financial market returns with useful accuracy over shorter periods is difficult. Making predictions with absolute confidence for a one-year period is impossible. We therefore employ our equilibrium expectations of the Reference Portfolio as the basis for the expected outcomes in the Statement of Intent.

What is 'passive' investment? Passive management or 'index tracking' is a style of investment management through which a fund's portfolio mirrors a market index. Stocks move in and out of the portfolio according to their market capitalisation rather than through active investment decisions.

What is 'active' investment? Active investment management is where a fund's manager attempts to beat the market through various investing strategies and buying/selling decisions. Active managers rely on analytic research, forecasts and their own judgement and experience in making investment decisions. Active investment strategies are more complex and expensive to implement than passive management.

In our actual portfolio, we also include '**active**' investment strategies – such as investing in alternative assets (e.g. timber, private equity) – in an effort to enhance our long-term performance. These activities bring a higher expected return and/or offer diversification benefits for the Fund, albeit with more complexity and cost.

These active investment strategies (such as strategic tilting and investing in private and/or illiquid assets) are consistent with our statutory duty regarding best-practice portfolio management, and are based on our investment beliefs and competitive advantages.

The Reference Portfolio (or passive benchmark) is therefore a very clear and 'pure' way for the Guardians to:

- estimate the Fund's expected returns;
- benchmark active (value-add) investment returns and costs; and
- be clear on the 'hurdles' for active investments.

The Reference Portfolio is not 'set and forget', and its asset class and risk-return composition can change over time, for example, if:

- assumptions about the long-term risk-return attributes of asset classes change; or
- aspects of the Fund's purpose or endowments (e.g. our long-term horizon) change; or
- market developments mean that a narrower or wider set of representative market exposures can be accessed passively and at a low cost.

Volatility measure – potential Reference Portfolio loss in a 1-in-100 year event

Financial market returns are inherently volatile, moving up and down over time as they are regularly re-priced. In any given period actual returns will fall somewhere within a wide range of possible returns. Over longer horizons, however, the underlying economic drivers tend to determine returns.

All investors must therefore consider the trade off between market price risk and economic return, factoring in considerations such as their particular investment timeframe and the potential need to convert assets quickly into cash (liquidity needs).

Accordingly, in establishing the Reference Portfolio, the Guardians' Board weighs up expected returns against the risks (such as equity risk and short-term price volatility) that come with different combinations of assets. The resulting combination of risk and return is that which the Board thinks best meets the Guardians' statutory obligation to maximise returns without undue risk to the Fund as a whole. As outlined above, the Board has settled on a Reference Portfolio with an 80:20 split between growth and fixed income assets.

In order to measure the market price risk carried by the Reference Portfolio, we estimate the lowest percentile expected return within different time periods. By this we mean the amount of value the Fund could lose in a 1-in-100 year event (or, to put it another way, there is a 1% chance of the Fund losing this amount of value or more within the specified time period). If losses of this magnitude were to happen more often than expected, then either a rarer-than expected event has occurred or we have taken more risk than we assumed.

When we add assets to the Fund's portfolio beyond what is in the Reference Portfolio, we fund those investments by selling 'proxies' – an equivalent mixture of equities and bonds that reflect the risk characteristics of the assets we are adding. In this way, the overall risk of the Fund's actual portfolio (before our tilting positions) is maintained at approximately the same level as the Reference Portfolio.

Want to know more?

Further detail about how we measure the Fund's performance, the internal and external influences on our management of the Fund, and detailed historical performance figures (updated monthly), can be found on www.nzsuperfund.co.nz.

Performance (continued)

5.1.2 Output measures – managing the Fund

In this section we set out how we will measure our success in delivering the five work programmes through which we manage the Fund (investment, cost control, risk, governance and organisational capability) over one, 10 and 20 year periods.

Where possible we look to obtain assessments of our performance from independent third parties and global experts in fund benchmarking.

For each work programme, we have also identified specific activities we expect to achieve in the 2013/14 financial year. These activities support the objectives we have established within our Strategic Plan.

These activities form our Forecast Statement of Service Performance (FSSP) for 2013/14, which is on page 12. We will report on our performance in the Statement of Service Performance in the 2013/14 Annual Report.

Investment Work Programme

We measure the delivery of the investment work programme via the outcome measures on page 6. Relevant FSSP activities in 2013/14 are outlined on pages 12-13.

Cost Control Work Programme

Cost control is central to the achievement of our mission to maximise returns without undue risk. Striking the right balance between minimising cost and implementing investment strategies that will add the most risk-adjusted value to the Fund over the long term is critical to achieving our mission.

	HORIZON	1-YEAR	10-YEAR	20-YEAR
	Where outcome reported	**SSP, 2014 Annual Report**	**SSP, 2023 Annual Report**	**SSP, 2033 Annual Report**
MEASURE	Costs relative to peers in CEM Benchmarking's investment management cost survey	We participate in the most widely used and comprehensive financial benchmarking available globally – the annual cost structure benchmarking survey by CEM Benchmarking Inc. (CEM). CEM assesses the cost structure of the Fund against more than 300 funds from around the world, focusing on 20 with similar risk profiles that also use active management strategies. The results of each CEM survey are published in our Annual Report and on www.nzsuperfund.co.nz. Relevant FSSP activities in 2013/14 are outlined on pages 12-13.		
MEASURE	• expected outcome	A rating of 'median cost, median-value-adding' or better. This rating provides an independent benchmark of whether we have struck a good balance between minimising costs and successfully implementing value-adding investment strategies. Succeeding in this area will result in better long-term investment returns for the Fund.		

Risk Management Work Programme

On page 2 we explained how the Act requires that the Guardians undertake best-practice portfolio management, maximise returns without undue risk, and avoid prejudice to New Zealand's reputation as a responsible member of the world community.

In order to help meet these requirements we have adopted:

- an organisational approach of being as transparent as possible about our investment process and our organisation in general;
- a commitment to exercising best practice portfolio management and to benchmarking ourselves globally; and
- a strong focus on responsible investment and the management of environmental, social and governance risks.

	HORIZON	1-YEAR	10-YEAR	20-YEAR
	Where outcome reported	**SSP, 2014 Annual Report**	**SSP, 2023 Annual Report**	**SSP, 2033 Annual Report**
MEASURE	In a 1-in-100 year event, potential Reference Portfolio loss	As per Outcome Measure – see page 7 for a full explanation.		
	• expected outcome	≥ -31% p.a.	≥ -4% p.a.	≥ -3% p.a.
	Transparency ratings over time	We strive to be a global leader in transparency. Transparency is a central compliance requirement for the Guardians, given our legal obligations under the Crown Entities Act, Official Information Act and other New Zealand legislation, together with the legislated requirement under our own Act to avoid prejudice to New Zealand's reputation as a responsible member of the world community. It is also critical to maintaining organisational credibility and stakeholder confidence in the Guardians and Fund. We therefore aim to keep our stakeholders as informed as possible about what we do and why we do it. Relevant FSSP activities in 2013/14 are outlined on page 13.		
	• expected outcome	10 out of 10 in the quarterly rating of Sovereign Wealth Fund transparency published by the Sovereign Wealth Fund Institute; top-quartile or higher ratings in other relevant rating mechanisms. Ratings published on www.nzsuperfund.co.nz		
	Best practice operations – annual updating of the Fund's response to the 'Santiago Principles'	New Zealand is a member country of the International Forum of Sovereign Wealth Funds (IFSWF), a voluntary group of sovereign wealth funds established under the auspices of the International Monetary Fund. The IFSWF's goals are for sovereign wealth funds to: • help maintain a stable global financial system and free flow of capital and investment; • comply with all applicable regulatory and disclosure requirements in the countries in which they invest; • invest on the basis of economic and financial risk and return-related considerations; and • have in place a transparent and sound governance structure that provides for adequate operational controls, risk management, and accountability. The Santiago Principles are a set of 24 voluntary IFSWF guidelines that assign best practices for the operations of sovereign wealth funds. The principles recognise that it is important for sovereign wealth funds to demonstrate to their home countries, to the countries in which they are invested and to the international financial markets in general that they are properly established and that their investments are made on a purely economic basis. The Santiago Principles monitor three important areas of operational practice for sovereign wealth funds – legal framework, institutional framework and governance framework, along with investment policies and risk management. Members of the IFSWF are required to undertake a regular review of their implementation of the Principles as a whole.		
	• expected outcome	Self-assessment of compliance with the Santiago Principles is completed and published on www.nzsuperfund.co.nz		

Performance (continued)

Risk Management Work Programme continued

	HORIZON	1-YEAR	10-YEAR	20-YEAR
	Where outcome reported	**SSP, 2014 Annual Report**	**SSP, 2023 Annual Report**	**SSP, 2033 Annual Report**
MEASURE	Responsible investment – UNPRI Assessment over time	Effective management of responsible investment issues is central to the Guardians' ability to manage both investment and reputation risk, and therefore to achieving our goal of maximising returns without undue risk. We believe environmental, social and governance factors impact investment performance over the long-term. For this reason we actively manage the long-term risks and opportunities that environmental, social and governance issues present to the Fund. We measure our performance in this area through annual United Nations Principles for Responsible Investment (UNPRI) assessments. The UNPRI is the international standard for best practice in responsible investment. Signatories are required to report on how they apply the principles. The assessment processes provide a measure of how effectively each fund is carrying out the principles relative to other signatories. The top quartile ratings that the Fund has achieved under the UNPRI assessments in past years are an indicator that we are managing responsible investment issues and risks to a high, internationally-benchmarked standard. The UNPRI is piloting a new assessment approach in the 2013/14 year, with a focus on scoring performance by asset class/business practice. Until further details of the new methodology are known it is not possible to set performance targets for the 2013/14 assessment nor for future years. We also understand that the UNPRI will restrict signatories from making assessment results relating to the pilot year public. We are participating in the 2013/14 pilot assessment and remain committed to maintaining the Fund's leadership position in responsible investment practice. We note that in recent years, investors around the world have begun to place a much higher emphasis on responsible investment and the effective management of environmental, social and governance risks. Maintaining a leadership position will therefore require constant improvement on our part. Relevant FSSP activities in 2013/14 are outlined on pages 12-13.		
	• expected outcome	Participate in pilot of new UNPRI assessment; establish performance measures for future years	Measure to be set following completion of pilot	Measure to be set following completion of pilot
	Responsible investment – Proxy voting reports	Voting rights are important for maintaining shareholder oversight of directors, boards and company policies. They are therefore central to our practice of responsible investment and to meeting our obligations under our governing legislation in relation to best practice portfolio management and managing risk. We exercise our voting rights globally across the Fund's segregated equity portfolio. Consistent with our commitment to transparency, we publish our proxy voting reports on www.nzsuperfund.co.nz on a six monthly basis. Relevant FSSP activities in 2013/14 are outlined on page 13.		
	• expected outcome	Completed and published for both six month periods on www.nzsuperfund.co.nz.		
	Annual Responsible Investment activity report	Within each year's Annual Report we publish a specific report on our responsible investment activities. This report provides a high degree of transparency and detail over our engagement programme, exclusion decisions, collaborations with other investors and internal process improvements. Relevant FSSP activities in 2013/14 are outlined on pages 12-13.		
	• expected outcome	Published		

Governance Work Programme

	HORIZON	1-YEAR	10-YEAR	20-YEAR
MEASURE	Outcome of independent reviews	An independent review of our governance of the Fund is required every five years. The terms of reference and funding for the review are provided by the Minister of Finance. The Fund has had two such reviews since inception; both are published on www.nzsuperfund.co.nz. The next review is due in 2014/15 and will be reported in the SSP, 2014/15 Annual Report.		
	• expected outcome	n/a done five yearly	On-going good reviews with the review and our response published	On-going good reviews with the review and our response published

Organisational capability

Managing the Fund, in a small country remote from the world's major financial markets and talent pools, presents the Guardians with some unique challenges. Being able to attract, retain and develop high calibre people is vital to our purpose of maximising the Fund's returns without undue risk. The global investment market is highly competitive and we can only find and enter into the best investment strategies if we have capable and experienced staff and can get the best out of their collective talent. We therefore place a high priority on attracting first-class candidates, retaining our top performers, building the capacity of our team and ensuring staff members' priorities are aligned with our organisational strategy. We also place a strong emphasis on creating a strong and collaborative working culture.

	HORIZON	1-YEAR	10-YEAR	20-YEAR
	Where outcome reported	**SSP, 2014 Annual Report**	**SSP, 2023 Annual Report**	**SSP, 2033 Annual Report**
MEASURE	Key person risks identified and covered	This measure is an indicator of how well we attract and retain the best people; and related to this, our ability to mitigate any potential loss of knowledge and expertise should key staff depart.		
	• expected outcome	Board approval received for our assessment of key person risk and our plans to mitigate that risk. 3-6 month cover in place for all critical roles and key people. Relevant FSSP activities in 2013/14 are outlined on page 13.		
	Key performance indicators achieved	Each staff member is assigned key performance indicators to work towards, including desirable behaviours and the achievement of key projects. Key performance indicators are closely linked to organisational strategy, objectives and values, and are therefore a measure of the extent to which our people are contributing to the Fund achieving its purpose.		
	• expected outcome	Staff members achieve their personal key performance indicators, with the average % achieved and trends from year-to-year reported in each year's Annual Report. Any key Strategic Plan activities for the financial year that are not achieved as planned are also reported in the Annual Report. Relevant FSSP activities in 2013/14 are outlined on page 13.		

FORECAST STATEMENT OF

6 Service Performance (FSSP)

Our FSSP frames our single output as managing the Fund. As set out in our Outcome Framework, that output comprises five work programmes covering expected investment returns; risk management; cost control; governance and organisational capability. For each work programme we have set performance measures which, collectively are performance measures for our output.

The FSSP sets out:

- objectives for the 2013-18 period as set out in our Strategic Plan together with some detail about what achieving these objectives would look like;
- key activities occurring in the 2013/14 financial year (we detail a selection of these on pages 14-15); and
- the Statement of Intent work programmes(s) toward which each strategic objective and key activity contributes, together with a reference back to the table setting out how each programme is measured and where and when it is reported (typically, in the Statement of Service Performance in the Annual Report).

The forecasted revenue that is received by the Guardians from the Fund and through parliamentary appropriation, as detailed in the prospective statement of comprehensive income (page 20), supplemented by expenses to be met directly by the Fund, will be used to implement the following strategic initiatives, and ultimately achieve the outcome of the Fund.

FOCUS OF STRATEGIC PLAN			WHERE REFLECTED IN SOI
Strategic Plan Objectives for 2013-2018	**What does success look like in 2018?**	**Key activities for 2013/14**	**Relevant work programme(s), measurements and reporting**
Best portfolio	• Single view across a wide range of opportunities • Higher reliance on internal capability to identify opportunities • Opportunistic investing in structured and consistent way • Broad assessment of access points • Systematic monitoring of strategies and managers • Fully implemented investment strategies: – Adding value net of costs to the Reference Portfolio – Improving the Sharpe ratio – Maximising cost efficiency and effectiveness • Risk taking is well aligned with risk appetite	• Refinement of RAP • Launch internal NZ active equities mandate	**Investment (pages 6-7):** • Actual Fund returns relative to Reference Portfolio **Risk (pages 9-10):** • In a 1-in-100 year event, potential Reference Portfolio loss • UNPRI assessment • Responsible Investment Activity Report **Cost control (page 8):** • Costs and value-add relative to peers in CEM Survey

	FOCUS OF STRATEGIC PLAN		WHERE REFLECTED IN SOI
Strategic Plan Objectives for 2013-2018	**What does success look like in 2018?**	**Key activities for 2013/14**	**Relevant work programme(s), measurements and reporting**
Collaboration with peers	• Co-investments alongside peers • Regular bilateral exchange of best practice alongside wider effectiveness and efficiency benchmarking • Active membership of global forums that exercise influence	• Relationship management and seeking co-investment opportunities	**Investment (pages 6-7):** • Actual Fund returns relative to Reference Portfolio **Risk (pages 9-10):** • Transparency ratings • UNPRI assessment • Voting records • Responsible Investment Activity Report **Cost control (page 8):** • Costs and value-add relative to peers in CEM Survey
Building and maintaining a great team	• Best practice across governance, enterprise risk management, and IT • Strong leadership, strong culture and values, focus on talent development and retention	• Strengthen talent management • Continue to implement culture development programme • Education Programme implementation	**Organisational capability (page 11):** • Board approval for key person risk plans and 3-6 month cover in place for all critical roles and key people • Staff achieve their KPIs **Cost control (page 8):** • Costs and value-add relative to peers in CEM Survey **Risk (pages 9-10):** • Transparency ratings • Response to best practice Santiago Principles
Efficiency, scalability and innovation	• Best practice investment and operational processes and workflows • High degree of transparency over our organisation and activities • Improvement opportunities are actively sought and measurable benefits realised	• Performance system implementation • Education Programme implementation • Central Clearing implementation • Development of IT roadmap • Intranet redevelopment • Website redevelopment	**Cost control (page 8):** • Costs relative to peers in CEM Survey **Risk (pages 9-10):** • Best practice – response to Santiago Principles • UNPRI assessment • Transparency ratings • Responsible Investment Activity Report

6.1 KEY 2013/14 ACTIVITIES

This section provides further detail about some of the key activities we plan to undertake in 2013/14.

Risk Allocation Process (RAP) Refinement and Alignment

Work programme: Investment
Strategic Plan objective: Best Portfolio

The Portfolio Risk Allocation Process, which was implemented during 2012/13, allows us to rank investment opportunities by attractiveness (expected return, adjusted for confidence and risk) and consistency with the Fund's investment style (consistency with what is important to us e.g. our long-term investment horizon, desire to invest as 'directly' as possible).

Planned refinements during 2013/14 will enable the Risk Allocation Process to better inform the sizing of investments and integrate with our Liquidity Replenishment System (a structured process for responding to extreme market volatility and ensuring the Fund has enough liquidity to meet its payment obligations as they fall due). Over time the actual portfolio will become more aligned with how the RAP determines it should look.

Performance System Implementation

Work programme: Cost control; Risk
Strategic Plan objective: Efficiency, scalability and innovation

We plan to introduce a new investment performance system during 2013/14. The Fund's shift away from a traditional asset allocation "bucket" approach to a more opportunistic investing style has increased its performance reporting needs and the new system, PEARL by Ortec Finance, was selected following a global search for a solution provider.

The new system is expected to significantly improve the quality, consistency and content of the Fund's performance reporting. PEARL provides a range of reporting features encompassing the measurement, contribution and attribution of investment performance and decision-making; the generation of ex-post risk and return analyses; and the provision of general risk statistics and risk decomposition.

Performance reporting is vital to the on-going growth and success of the Fund. PEARL is a key building block as we look to enhance and future-proof our investment performance reporting process; to build scalable systems that are at the forefront of global best practice; and in our efforts to be a global leader in transparency and public reporting.

Launch Internal Active NZ Equities Mandate

Work programme: Investment; Organisational Capability
Strategic Plan objective: Best Portfolio

Over 2013/14 the Fund will transition its passive portfolio of listed New Zealand equities to active in-house management. We believe the New Zealand equity market is conducive to active management and that establishing an internal active management function will give us the opportunity to tailor our portfolio to the Fund's investing horizon, liquidity endowments and responsible investment approach, thus maximising long-term returns. Key activities include appointing the NZ active equities team; integrating responsible investment beliefs and processes into the mandate; and building the research base.

Board and Staff Education Programme

Work programme: Organisational Capability
Strategic Plan objective: Building and maintaining a great team; Efficiency, Scalability & Innovation

Work is underway to develop a suite of educational resource material that can be accessed by Board members and staff. This initiative aims to:

- capture institutional knowledge and expertise/ avoid 'reinvention of the wheel';
- expedite the 'learning curve' for new recruits;
- ensure everyone who works at the Guardians, including non-investment professionals, have a basic knowledge of what we do and why; and the ability to articulate in simple terms key internal principles and activities;
- ensure people in roles that require a more detailed understanding of key topics can easily find the information they need;
- encourage collaboration and dialogue.

A series of education modules including video presentations and Wiki-style collaboration features will be delivered via a redeveloped Guardians intranet over 2013/14.

Central Clearing Implementation

Work programme: Risk Management
Strategic Plan objective: Efficiency, Scalability & Innovation

The passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act in the US, and the European Markets Infrastructure Regulation in Europe, are anticipated to result in the clearing of some over-the-counter derivative transactions through a central clearing counterparty (CCP). For these transactions, the CCP will stand between the Fund and the dealer we are trading with, and the CCP will become our counterparty.

As the Guardians wishes to preserve the ability to trade these products with as many counterparties as possible, a major project is underway to ensure we can successfully execute trades under the new regulatory framework. The project includes appointing and inducting clearing brokers; mapping the operational workflows from the clearing brokers to our custodian, Northern Trust; detailing selection criteria for our choice of CCP(s); and revising our approach to monitoring and managing counterparty risk.

What is a counterparty?

A counterparty is the other party that participates in a financial transaction. Every transaction must have a counterparty. More specifically, every buyer of an asset must be paired up with a seller that is willing to sell and vice versa. One of the risks involved in any transaction is counterparty risk, which is the risk that the counterparty will be unable to fulfil his or her payment obligations.

6.2 REQUIRED STATEMENT OF ESTIMATED FUND RETURNS

We are legally required to outline our expectations for the performance of the Fund over the next financial year. Predicting short-term financial market returns with any useful accuracy over such a near-term horizon is, however, impossible. We therefore show our long-term, or equilibrium, expectations for the Reference Portfolio return. To that we add our expectations of returns from added-value activities to arrive at the mid-point for the actual Fund.

Finally, we estimate a range of possible Fund returns for 2013/14, given our assumed volatility of market returns. Using this approach we have estimated as follows:

COMPONENT OF RETURN	RISK-FREE RATE **6.0%**	+	EXCESS RETURN AFTER COSTS **2.5%** (which is the reward for taking market risk above cash or the risk-free rate)	+	REWARD FOR VALUE-ADDING ACTIVITIES **1.1%**	=	**9.6%**
EXPLANATION	Our estimate of the equilibrium return on 90-day Treasury Bills.		We define the reward for market risk as the margin between the risk-free rate and the return that would be generated on the Reference Portfolio (after assumed costs of 0.3%). Although the estimates of market risk vary over time, we provide the equilibrium, or long term, expectation of the rewards for market risk on the Reference Portfolio. Our estimate of the reward for market risk has a very wide range over a one-year horizon, although this range tightens over longer horizons. Around the mid-point the 90% probability range is around +/- 20% for one year, +/- 6% for ten years and +/- 3.5% for 20 years.		Our estimation of the return from the investment activities we undertake to add value. We summarise those activities as part of the explanation of the Reference Portfolio on pages 6-7.		The mid-point of our estimated range for the Fund return over 2013/14 is 9.6%.

TRANSPARENCY AND

7 Reporting to the Minister

We strive to be as transparent as possible about our management of the Fund and how the Fund performs. Our stakeholders, including the Minister of Finance, and any other interested party, can easily access a wealth of current, detailed information on our website.

This information includes monthly performance and portfolio reports; detailed historical performance figures for the Fund since inception; copies of our media statements along with speeches and presentations given by Guardians staff.

A range of formal reporting mechanisms are also in place. A Parliamentary Select Committee, usually the Commerce Committee, reviews the Guardians' and Fund's financial statements annually. Our presentations to the Committee are published on www.nzsuperfund.co.nz. Committee reports are available on www.parliament.govt.nz.

As a Crown entity we are subject to the Official Information Act 1982 and to other Parliamentary scrutiny requirements such as Parliamentary Questions.

In addition the Guardians provide a quarterly report on the progress of the Guardians and the Fund to the Minister of Finance. This sets out the performance of the Fund and key investment and other operational developments during the preceding quarter.

Section 64 of our Act states that the Minister may, after consulting with us, give directions regarding the Government's expectations as to the Fund's performance, including the Government's expectations as to risk and return. Such a direction cannot be inconsistent with our statutory duty to invest the Fund on a prudent, commercial basis. We must have regard to any such direction and must notify the Minister how we propose to do this. We must also report how we are having regard to the direction in our Annual Report.

As part of the 2009 Budget we received a direction from the Minister on investing in New Zealand. The wording of the direction, our response, and our progress reports against it, are publicly available on www.nzsuperfund.co.nz.

In common with other Crown entities we also receive from the Minister an annual Letter of Expectations, setting out the Minister's general requirements for prudent expenditure and the importance of achieving value for costs incurred, given the broader economic and fiscal environment. A copy of the March 2013 letter and our response can be found on www.nzsuperfund.co.nz.

8 Acquisitions

We have no intention in respect of the activities of the Guardians to acquire interests in companies, trusts or partnerships for the benefit of the Guardians. We do, however, undertake such acquisitions as manager and administrator of the Fund, and those interests become the property of the Fund.

The Guardians must use its best endeavours to ensure that the Fund does not have control of entities (for example a company). This requirement is set out more fully in section 59 of the New Zealand Superannuation and Retirement Income Act 2001. Consequently, the investment guidelines we have in place with external managers and our other internal policies and procedures contain controls that ensure compliance with this requirement.

FINANCIAL

9 Projections for 2013/14

COST ALLOCATION MODEL

Our Cost Allocation Model is made up of two main components – the Guardians and the Fund.

- Fund expenses are met from the Fund and are those incurred in the establishment and implementation of investment policy and the financial and risk management of Fund assets including base fees paid to external managers.
- The Guardians' expenses – with the exception of those incurred by the Board – are met from the Fund and include remuneration, staff expenses such as office services, travel, and professional development.

The expenses of the Board are met from Parliamentary appropriation and include Board fees, the cost of travel to and from Board meetings and the cost of external audit for the Guardians.

All operating costs, irrespective of whether they are sourced from appropriations or Fund assets, are consolidated in the financial statements of the Guardians and subject to the reporting and disclosure obligations of the Crown Entities Act (2004).

We have prepared prospective financial statements for the Fund. The estimates assume that earnings will be broadly in line with the medium-term estimate (i.e. 9.6% p.a. after costs but before New Zealand tax). Some costs are fixed (e.g. audit costs) and can be easily estimated, but the majority are variable (i.e. base and performance fees paid to investment managers or transaction fees paid to the custodian). We have prepared estimates of these variable costs based on our expectations of the Fund over the year.

EXPECTED TOTAL COST OF MANAGING THE FUND IN 2013/14

The forecast cost of managing the Fund in 2013/14 – excluding performance fees – is $116.2 million or 0.52% of expected average funds under management. This is lower than forecast in the previous Statement of Intent ($125.1 million or 0.64%). Of this amount the Guardians' expenses are $35.0 million (of which $0.53 million are Board expenses met by Parliamentary Appropriation), amounting to 0.16% of expected average funds under management.

Performance fees are only paid when investment managers outperform their benchmarks and so they are better described as an offset against returns than a cost. However, if we include forecast performance fees, the forecast cost of managing the Fund in 2013/14 is $144.3 million or 0.64%. This is lower than forecast in the previous Statement of Intent ($154.0 million or 0.79%).

It is important to emphasise that these are forecast figures and that actual fees will be dependent on market conditions and the availability of suitable investment opportunities and access points. Actual performance fees paid each financial year are disclosed in our Annual Report.

EXPECTED TOTAL COST OF MANAGING THE FUND FROM 2013/14 TO 2017/18

We forecast that total costs (excluding performance fees) will remain broadly flat at around 0.52% of expected average funds under management over the five-year period covered by this SOI. This compares favourably to actual costs (excluding performance fees) over the last five years, which have averaged 0.66% of average funds under management.

If we include forecast performance fees, costs over this period are projected to increase slightly from 0.64% to 0.66% of expected average funds under management.

PROSPECTIVE

10 Financial Statements

We have prepared prospective financial statements for the Guardians (in our role as manager and administrator of the Fund) and for the Fund consistent with this Statement of Intent.

These prospective financial statements rely on assumptions with respect to unknown or uncertain future events. Assumptions represent a risk in that actual events may vary from the assumption and that all of the outcomes that may flow from actual events cannot be guaranteed.

These prospective financial statements should be read within the context of the Statement of Intent. Information in these prospective financial statements may not be appropriate for purposes other than those described.

The Board authorised the issue of these prospective financial statements at its 9 April 2013 meeting. The Board is responsible for the prospective financial statements presented, including the appropriateness of the assumptions underlying the prospective financial statements and all other required disclosures.

The assumptions used in preparing the prospective financial statements have been disclosed following the accounting policies of each entity.

Actual financial results have not been incorporated into the prospective financial statements. It is not the intent of the Board to update these prospective financial statements subsequent to presentation.

Contents

Prospective Statement of Comprehensive Income

For the year ending 30 June 2014	$000
Revenue from parliamentary appropriation	528
Revenue from New Zealand Superannuation Fund	34,312
Other income	154
Total revenue	**34,994**
Board-related expenses	(728)
Employee remuneration and related expenses	(28,258)
Depreciation	-
Other expenses	(6,008)
Total expenses	**(34,994)**
Profit/(Loss) for the year	**-**
Other comprehensive income	-
Total comprehensive income for the year	**-**

Prospective Statement of Financial Position

As at 30 June 2014	$000
ASSETS	
Current assets	
Cash and cash equivalents	975
Trade and other receivables	6,616
Non-current assets	
Property, plant and equipment	-
Total assets	**7,591**
LIABILITIES	
Current liabilities	
Trade and other payables	824
Accrued employee benefits	5,564
Lease incentive	75
Non-current liabilities	
Lease incentive	628
Total liabilities	**7,091**
Net assets	**500**
EQUITY	
Accumulated surplus	-
General equity reserve	500
Total public equity	**500**

Prospective Statement of Changes in Public Equity

For the year ending 30 June 2014	$000
Balance at 30 June 2013	**500**
Profit for the year	-
Other comprehensive income	-
Total recognised revenue and expense for the year	**-**
Balance at 30 June 2014	**500**

Prospective Statement of Cash Flows

For the year ending 30 June 2014	$000
CASH FLOWS FROM OPERATING ACTIVITIES	
Cash was provided from:	
Receipts from the Crown	528
Receipts from New Zealand Superannuation Fund	30,831
Other income	68
Interest received	64
Goods and Services Tax	708
Cash was applied to:	
Payments to suppliers	(4,433)
Payments to employees	(28,258)
Net cash provided by/(used in) operating activities	**(492)**
Net increase in cash and cash equivalents	**(492)**
Cash and cash equivalents at the beginning of the year	1,467
Cash and cash equivalents at the end of the year	**975**

Summary of significant accounting policies

GENERAL INFORMATION

These are the prospective financial statements of the Guardians of New Zealand Superannuation (Guardians), a Crown entity in terms of the Crown Entities Act 2004.

The Guardians is domiciled in New Zealand and the address of its principal place of business is 21 Queen Street, Auckland.

STATEMENT OF COMPLIANCE

The Guardians is a public benefit entity, as the primary purpose is to manage and administer the New Zealand Superannuation Fund (Fund). The prospective financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP) as it applies to prospective financial statements.

The prospective financial statements of the Guardians of New Zealand Superannuation and Subsidiaries (Group) for the year ended 30 June 2014 were authorised for issue in accordance with a resolution of the Board of Guardians of New Zealand Superannuation on 9 April 2013.

BASIS OF PREPARATION

The prospective financial statements have been prepared in accordance with the Crown Entities Act 2004 and the Public Finance Act 1989 and comply with Financial Reporting Standard No. 42: Prospective Financial Statements.

The prospective financial statements have been prepared on a historical cost basis, are presented in New Zealand dollars and all values are rounded to the nearest thousand dollars (NZ$000).

Accounting policies are selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

The following particular accounting policies which materially affect the measurement of comprehensive income and financial position have been applied:

(a) Consolidation of subsidiaries

The Group financial statements comprise the Guardians of New Zealand Superannuation and its subsidiaries.

Subsidiaries are those entities that are controlled by the Guardians. The financial statements of subsidiaries are prepared for the same reporting period as the parent entity, using consistent accounting policies.

Adjustments are made to bring into line any dissimilar accounting policies that may exist.

The results of any subsidiaries that become or cease to be part of the Group during the year are consolidated from the date that control commenced or until the date that control ceased.

All inter-entity transactions, balances and unrealised profits are eliminated on consolidation.

(b) Revenue and income

The Group primarily derives revenue through the provision of outputs to the Crown and to the Fund, and also derives income from its investments. Revenue and income is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Rendering of services

Revenue from the rendering of services is recognised by reference to the stage of completion.

New Zealand Superannuation Fund reimbursement of costs:
Stage of completion is measured by the proportion of costs incurred to date, compared to the total costs of the outputs.

Crown appropriations:
Revenue is recognised on a straight-line basis over the period the appropriations relate, because the services are performed by an indeterminate number of acts over a specified period of time.

Other service revenue:
Where outputs cannot be measured reliably, revenue is recognised only to the extent that the expenses recognised are recoverable.

Interest

Interest revenue is recognised as the interest accrues (using the effective interest method which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset).

(c) Goods and Services Tax (GST)

Revenues, expenses, assets and liabilities are recognised exclusive of GST, with the exception of receivables and payables which are stated with GST included. Where GST is irrecoverable as an input tax, it is recognised as part of the related asset or expense.

Cash flows are included in the cash flow statement on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the taxation authority are classified as operating cash flows.

(d) Taxation

The Guardians is a public authority in terms of the Income Tax Act 2007 and consequently is exempt from income tax.

(e) Receivables

Short-term receivables are stated at their estimated realisable value net of impairment allowance.

Collectibility of receivables is reviewed on an ongoing basis. Individual debts that are known to be uncollectible are written off when identified. An impairment provision is recognised when there is objective evidence that the Group will not be able to collect the receivable. Financial difficulties of the debtor, default payments or debts more than 60 days overdue are considered objective evidence of impairment. The amount of the impairment loss is the receivable carrying amount compared to the present value of estimated future cash flows, discounted at the original effective interest rate.

(f) Subsidiaries

Subsequent to initial recognition, investments in subsidiaries are measured at cost.

(g) Property, plant and equipment

Initial recording

All items of property, plant and equipment are initially recognised at cost. Cost includes the value of consideration exchanged, or fair value in the case of donated or subsidised assets, and those costs directly attributable to bringing the item to working condition for its intended use.

Subsequent expenditure

Subsequent expenditure relating to an item of property, plant and equipment is capitalised to the initial cost of the item when the expenditure increases the economic benefits over the life of the item or where that expenditure was necessarily incurred to enable the future economic benefits to be obtained and the expenditure would have been included in the initial cost of the item had the expenditure been incurred at the time of acquisition.

All other subsequent expenditure is expensed in the period in which it is incurred.

Subsequent measurement

Subsequent to initial recognition, property, plant and equipment is stated at cost less accumulated depreciation and any impairment in value.

Disposal

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset.

Any gain or loss arising on disposal of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of an item) is included in the statement of comprehensive income in the year the item is disposed of.

Impairment

All items of property, plant and equipment are assessed for indications of impairment at each balance date. If any indication of impairment exists, an estimate of the asset’s recoverable amount is calculated.

Where the carrying amount is assessed to be greater than its recoverable amount, the item is written down to its recoverable amount. The write-down is recognised in the statement of comprehensive income.

Summary of significant accounting policies (continued)

Where an impairment loss subsequently reverses, the carrying amount of the item is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the item in prior years. A reversal of an impairment loss is recognised in the statement of comprehensive income immediately.

Recoverable amount is the greater of fair value less costs to sell and value in use. The recoverable amount is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs to sell and it does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash generating unit to which the asset belongs.

In assessing value in use, the estimated pre-tax future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Held for sale

Items of property, plant and equipment classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell.

Items of property, plant and equipment are classified as 'held for sale' if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. The sale of such an asset is expected to be completed within one year from the date of classification.

(h) Depreciation

Depreciation is provided on a straight-line basis on all property, plant and equipment at a rate which will write off the cost of the assets to their estimated residual value over their useful lives.

The useful lives of major classes of assets have been estimated as follows:

Office equipment	3 years
Computer equipment	1-3 years

(i) Intangible assets

Software and licences are finite life intangibles and are recorded at cost less accumulated amortisation and impairment. Amortisation is charged on a straight-line basis over their estimated useful lives of 3 years. The estimated useful life and amortisation method is reviewed at the end of each annual reporting period.

(j) Employee benefits

Provision is made for benefits accruing to employees in respect of wages and salaries, annual leave, long service leave, incentives and sick leave when it is probable that settlement will be required and they are capable of being measured reliably.

Provisions made in respect of employee benefits expected to be settled within 12 months are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Provisions made in respect of employee benefits which are not expected to be settled within 12 months are measured at the present value of the estimated future cash outflows to be made by the Group in respect of services provided by employees up to reporting date.

(k) Operating leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Leases where the lessor effectively retains substantially all the risks and benefits of ownership of the leased items are classified as operating leases. Operating lease expenses are recognised on a straight-line basis over the period of the lease.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as deferred income in the statement of financial position. The aggregate benefits of incentives are recognised as a reduction of rental expense on a straight-line basis over the period of the lease.

(l) Foreign currency transactions

Transactions denominated in a foreign currency are converted to New Zealand dollars at the exchange rate in effect at the date of the transaction.

Monetary assets and liabilities denominated in a foreign currency at balance date are translated at the rate of exchange ruling as at that date. The resulting exchange differences are recognised in the statement of comprehensive income. Foreign exchange gains and losses for fair value through profit or loss investments are included within the change in their fair value.

(m) Financial instruments

The Group is party to financial instruments as part of its normal operations. These financial instruments include cash and cash equivalents, receivables and payables. All financial instruments are recognised in the statement of financial position and all revenues and expenses in relation to financial instruments are recognised in the statement of comprehensive income.

Financial assets and financial liabilities are recognised in the statement of financial position when the Group becomes a party to the contractual provisions of the instrument. The Group offsets financial assets and financial liabilities when the Group has a legally enforceable right to set off the recognised amounts and interests and intends to settle on a net basis.

Except for items covered by a separate accounting policy, all financial instruments are shown at their amortised cost.

(n) Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, the future sacrifice of economic benefits is probable and the amount of the provision can be measured reliably.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that recovery will be received and the amount of the receivable can be measured reliably.

(o) Payables

Short-term payables are not interest bearing and are stated at their nominal value.

(p) Equity

Equity is the Crown's interest in the Guardians and is measured as the difference between total assets and total liabilities.

(q) Statement of cash flows

The following are the definitions of the terms used in the statement of cash flows:

Operating activities include all activities other than investing and financing activities. The cash inflows include all receipts from the sale of goods and services, interest and other sources of revenue that support the Group's operating activities. Cash outflows include payments made to employees, suppliers and for taxes.

Investing activities are those activities relating to the acquisition, holding and disposal of current and non-current securities and any other non-current assets.

Financing activities are those activities relating to changes in equity and debt capital structure of the Group and those activities relating to the cost of servicing the Group's equity capital.

Cash and cash equivalents includes cash balances on hand, held in bank accounts, demand deposits and other highly liquid investments with an original maturity of three months or less.

(r) Changes in accounting policies

There have been no changes in accounting policies. The accounting policies have been applied consistently throughout these prospective financial statements.

Summary of significant accounting policies (continued)

(s) Critical accounting estimates and assumptions

In preparing these prospective financial statements the Group has made estimates and assumptions concerning the future. These estimates and assumptions may differ from the subsequent actual results. Estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are discussed below:

Employee entitlements – long-term portion of incentive

A component of the incentive scheme is based on the long-term performance of the Fund. The calculation of this portion of the incentive liability utilises assumptions regarding the future performance of the Fund, the employee's average salary over the vesting period and the percentage of service rendered. The key variable is the performance of the Fund. Should the performance of the Fund differ from the assumption utilised in the calculation of the long-term portion of the incentive liability, this will impact the employee benefits expense in the statement of comprehensive income and the carrying amount of the incentive liability in the statement of financial position. The Group manages this risk by using a medium-term expectation of Fund performance.

SIGNIFICANT ASSUMPTIONS ADOPTED IN THE PREPARATION OF PROSPECTIVE FINANCIAL STATEMENTS

The Guardians' forecast is based on the key assumption that the headcount for the Guardians will increase from 80.7 as at the end of January 2013 to 101.2 full-time equivalent employees by 30 June 2018.

The forecast increase in headcount numbers was determined from the annual business plan compiled by the Guardians senior management team.

In the event that the Guardians are unable to recruit the additional headcount as forecast, actual results may vary materially from the forecast. Any variance in actual headcount is likely to result in a material reduction of expenses, resulting in a corresponding decrease in revenue received from the Fund.

Prospective Statement of Comprehensive Income

For the year ending 30 June 2014	$000
INCOME	
Interest income	521,233
Dividend income	229,792
Timber & milk sales	25,978
Fair value changes in investments at fair value through profit or loss	1,286,041
Net foreign exchange gain/(loss)	-
Share of profit of investments accounted for using the equity method	72,222
Net operating income/(loss)	**2,135,266**
EXPENSES	
Timber expenses	(6,773)
Farm expenses	(8,761)
Depreciation and amortisation	(2,432)
Managers' fees – base	(40,830)
Managers' fees – performance	(28,057)
Custody fees	(4,218)
Other expenses	(52,545)
Profit/(Loss) for the year before income tax expense	**1,991,650**
Income tax expense	(483,779)
Profit/(Loss) for the year after income tax expense	**1,507,871**
OTHER COMPREHENSIVE INCOME	
Net fair value gains on available-for-sale financial assets	8,316
Gain on revaluation of property, plant and equipment	13,348
Income tax on items of other comprehensive income	-
Other comprehensive income for the year, net of tax	**21,664**
Total comprehensive income for the year	**1,529,535**

Prospective Statement of Financial Position

As at 30 June 2014	$000
ASSETS	
Cash and cash equivalents	2,599,231
Inventory	490
Investments	
Derivative financial instrument assets	1,280,288
Other financial assets	17,794,435
Investments accounted for using the equity method	935,027
Timber investments – forests	39,271
Total investments	**20,049,021**
Trade and other receivables	875,180
Property, plant and equipment	157,909
Total assets	**23,681,831**
LIABILITIES	
Trade and other payables	109,386
Provisions	26,744
Taxation payable	95,540
Deferred tax liability	168,796
Total liabilities	**400,466**
Net assets	**23,281,365**
EQUITY	
Retained surplus	8,350,530
Available-for-sale reserve	18,040
Land revaluation reserve	30,716
Contributed capital	14,882,079
Total public equity	**23,281,365**

Prospective Statement of Changes in Public Equity

For the year ending 30 June 2014	$000
Balance at 30 June 2013	**21,751,830**
Profit for the year	1,507,871
Other comprehensive income	21,664
Total comprehensive income for the year	**1,529,535**
Fund capital contributions from the Crown	-
Capital contributions from the Crown in respect of funding the net cost of New Zealand Superannuation entitlements	10,894,365
Capital withdrawals by the Crown in respect of funding the net cost of New Zealand Superannuation entitlements	(10,894,365)
Balance at 30 June 2014	**23,281,365**

Prospective Statement of Cash Flows

For the year ending 30 June 2014	$000
CASH FLOWS FROM OPERATING ACTIVITIES	
Cash was provided from:	
Proceeds from the sale of investments	42,497,382
Dividends received	396,163
Interest received	492,968
Receipts from customers	30,157
Cash was applied to:	
Payment for the purchase of investments	(42,571,207)
Managers' fees	(38,275)
Payments to suppliers	(84,846)
Income tax paid	(748,442)
GST paid	-
Net cash provided by/(used in) operating activities	**(26,100)**
CASH FLOWS FROM INVESTING ACTIVITIES	
Cash was provided from:	
Disposal of property, plant and equipment	-
Cash was applied to:	
Purchases of property, plant and equipment	(56,105)
Purchases of intangible assets	(1,195)
Net cash provided by/(used in) investing activities	**(57,300)**
CASH FLOWS FROM FINANCING ACTIVITIES	
Cash was provided from:	
Capital contributions from the Crown	-
Net cash provided by/(used in) financing activities	**-**
Net increase/decrease in cash and cash equivalents	**(83,400)**
Cash and cash equivalents at the beginning of the year	2,682,631
Effects of exchange rate changes on foreign currency cash	-
Cash and cash equivalents at the end of the year	**2,599,231**

Summary of significant accounting policies

GENERAL INFORMATION

These are the prospective financial statements of the New Zealand Superannuation Fund (Fund) and its subsidiaries (Group), a fund created under Section 37 of the New Zealand Superannuation and Retirement Income Act 2001 (Act). This Act commenced on 11 October 2001.

The consolidated prospective financial statements comprise the Fund and its subsidiaries.

The Fund is managed and administered by the Guardians of New Zealand Superannuation (Guardians). The Guardians were established as a Crown entity by Section 48 of the Act and became operative from 30 August 2002.

Under section 43 of the Act, the Crown is required to make capital contributions to the Fund for investment based on a percentage of GDP as set out in the Act. Capital contributions are made by the Crown into the Fund on a fortnightly basis for the purpose of investment and funding the net cost of New Zealand superannuation entitlements. Under section 44 of the Act, the Crown is entitled to contribute lesser amounts than calculated using the formula under section 43 of the Act.

The Fund is domiciled in New Zealand and the address of its principal place of business is 21 Queen Street, Auckland.

STATEMENT OF COMPLIANCE

The Fund is a profit-oriented entity. The prospective financial statements of the Group have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP).

The prospective financial statements for the year ended 30 June 2014 were authorised for issue in accordance with a resolution of the Board of the Guardians of New Zealand Superannuation on 9 April 2013.

BASIS OF PREPARATION

The prospective financial statements have been prepared in accordance with the Act and comply with Financial reporting Standard No. 42: Prospective Financial Statements.

The prospective financial statements have been prepared on a fair value basis, except for certain items as detailed in the policies below.

The prospective financial statements are presented in New Zealand dollars and all values are rounded to the nearest thousand dollars (NZ$000).

Accounting policies are selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

The following particular accounting policies which materially affect the measurement of comprehensive income and financial position have been applied:

(a) Capital contributions

(i) *Fund capital contributions*
The Crown is required to make capital contributions to the Fund in accordance with Sections 42 to 44 inclusive of the Act. Capital contributions are made by the Crown to the Fund for investment and for the purpose of contribution to the net cost of paying superannuation entitlements after 2020. These capital contributions are recorded in the statement of changes in public equity.

(ii) *Superannuation entitlement payments*
The Minister of Finance, under Section 45 of the Act, must ensure that sufficient money is transferred to the Fund in each year to meet the net cost of superannuation entitlements. These transfers are treated as capital contributions from the Crown in respect of funding the net cost of superannuation entitlements and are offset by capital withdrawals and recorded in the statement of changes in public equity.

(b) Capital withdrawals

(i) *Fund capital withdrawals*
In terms of Section 47 of the Act no withdrawals of Fund capital contributions are permitted prior to 30 June 2020.

(ii) *Superannuation entitlement payments*
The net cost of superannuation entitlements is treated as capital withdrawals by the Crown in respect of funding the net cost of superannuation entitlements and is recorded in the statement of changes in public equity.

Summary of significant accounting policies (continued)

These amounts equate to the associated capital contributions.

The payment of superannuation entitlements is an expense of the Crown and is recorded separately in the Crown's financial statements.

(c) Income tax

In accordance with Section HR 4B of the Income Tax Act 2007, the income derived by the Fund is subject to New Zealand tax determined by using the rules applying to companies.

The income tax expense recognised for the year is based on the accounting surplus, adjusted for permanent differences between accounting and tax rules.

Current tax is calculated by reference to the amount of taxes payable or recoverable in respect of the taxable profit or tax loss for the year. It is calculated using tax rates and tax laws that have been enacted or substantively enacted at balance date. Current tax for current and prior periods is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

Deferred income tax is provided on all temporary differences at balance date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

(i) except for a deferred income tax liability arising from the initial recognition of goodwill;

(ii) except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

(iii) in respect of taxable temporary differences associated with investments in subsidiaries, associates, and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, the carry-forward of unused tax assets and unused tax losses can be utilised:

(i) except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

(ii) in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except that deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at balance date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Income tax relating to items of other comprehensive income are recognised in other comprehensive income.

(d) Financial instruments

The Group is party to financial instruments as part of its normal operations. These financial instruments include cash and cash equivalents, derivatives, investments, receivables and payables. All financial instruments are recognised in the statement of financial position and all revenues and expenses in relation to financial instruments are recognised in the statement of comprehensive income.

Financial assets and financial liabilities are recognised in the statement of financial position when the Group becomes a party to the contractual provisions of the instrument. Purchases or sales of financial instruments that require delivery within the time frame generally established by regulation or convention in the marketplace are recognised on the trade date, i.e. the date that the Group commits to purchase or sell the instrument. Derivatives are recognised on a trade date basis. The Group offsets financial assets and financial liabilities when the Group has a legally enforceable right to set off the recognised amounts and interests and intends to settle on a net basis.

(e) Investments

Investments are represented by the following:

Financial instruments at fair value through profit or loss (either designated at fair value through profit or loss or held for trading):

- Equities i)
- Fixed income securities ii)
- Derivatives iii)
- Collective investment funds iv)
- Certain private equity investments v)
- Unlisted unit trusts vi)
- Insurance-linked investments vii)
- Unlisted debt instruments viii)

Available-for-sale financial instruments:

- Certain private equity investments ix)
- Other available-for-sale investments x)

Loans and receivables:

- Unlisted debt instruments xi)

Investments accounted for using the equity method (refer accounting policies (i) and (j))

Agricultural assets – forests and livestock (refer accounting policies (k) and (l))

Financial instruments at fair value through profit or loss

Initial recording
Financial instrument investments at fair value through profit or loss are initially recognised at fair value on a trade date basis. Transaction costs, for example trading commission, are expensed immediately in the statement of comprehensive income.

Subsequent measurement
Subsequent to initial recognition, these investments are recorded at fair value and are classified into the category "at fair value through profit or loss". The Guardians manage and evaluate the performance of these investments on a fair value basis in accordance with the Fund's investment strategy and information about the investments is provided internally on this basis to the Guardians' key management personnel. Changes in fair value are recognised in profit or loss in the statement of comprehensive income.

Determination of fair value
Fair value is an estimate of the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair value is determined as follows:

(i) Listed equities are valued at the last quoted bid price on the relevant exchange as of the close of business at balance date.

(ii) Highly liquid fixed income securities and equity-linked notes are valued at the last quoted bid price by a reputable pricing vendor or broker as of the close of business at balance date. Where the market for fixed income securities is illiquid, prices are determined by a reputable pricing vendor who uses models to value these securities. The models can utilise a variety of inputs including loan level data, prepayment and default assumptions and benchmark prices for similar securities. Because of the inherent uncertainty of valuation, it is possible that those values estimated for the illiquid securities may differ from those values that would have been used had a ready market for those securities existed and those differences may be significant.

(iii) Fair value for derivatives is outlined under "Derivatives" below.

(iv) Investments in collective investment funds (unlisted investment funds) are valued at the last price of the unit or security as provided by the administrators at balance date. The price is based on the fair value of the underlying net assets or securities of the relevant collective investment fund.

(v) Certain private equity investments (unlisted investment funds and unlisted equity investments), which are designated at fair value through profit or loss, are valued at the last price of the unit or security as provided by the investment managers or administrators at balance date. The price is based on the fair value of underlying net assets of the private equity investment. Fair value is determined using a variety of

Summary of significant accounting policies (continued)

methods, including independent valuations, valuation models based on the price of recent investments, earnings multiples or discounted cash flows. Certain private equity investments are classified as available-for-sale. The accounting policy for these investments is outlined under ix).

(vi) Investments in unlisted unit trusts are valued at the last bid price of the unit or security as provided by the administrators at balance date. The price is based on the fair value of the underlying net assets or securities of the relevant unlisted unit trust.

(vii) Insurance-linked investments which are catastrophe bonds are valued using prices provided by reputable pricing vendors or brokers.

(viii) Unlisted debt instruments including fixed and floating rate instruments that form part of an investment into a private equity investments may be designated at fair value through profit or loss. These assets are valued by a suitably qualified independent valuer who ascribes an enterprise value to the entire private equity investment and apportions that value across the instruments held, including the debt instruments. Any unlisted debt instruments that are not designated at fair value through profit or loss are classified as loans and receivables and are carried at amortised cost. Refer to (xi) below.

Available-for-sale financial instruments

(ix) Certain private equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured using the valuation methods outlined in v) above are classified as available-for-sale and are measured at cost less impairment. Transaction costs are included in the cost of the investment. Management has determined that fair value for these investments cannot be reliably measured where the entity's financial statements have not been prepared under either IFRS or a recognised and reliable accounting basis such as US GAAP. Subsequently, where the fair value of these investments becomes able to be reliably measured, then the investment will be measured at fair value with gains or losses being recognised in other comprehensive income (reserves) until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in reserves is reclassified to profit or loss in the prospective statement of comprehensive income.

(x) Other available-for-sale investments include investments in cooperative and processing companies. The Group is required to hold these investments to facilitate farming investment operations. As such, the Group is normally unable to sell these investments without disrupting farming investment operations. These available-for-sale investments are valued at fair value with gains or losses being recognised in other comprehensive income (reserves) until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in reserves is reclassified to profit or loss in the statement of comprehensive income.

Loans and receivables

(xi) Unlisted debt instruments including fixed and floating rate notes and redeemable preference shares are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. Where such assets are not designated at fair value through profit or loss, these assets are carried at amortised cost using the effective interest rate method. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired.

Impairment of financial assets

The Group assesses, at each reporting date, whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (an 'incurred loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Derivatives

The Group enters into a variety of derivative financial instruments to manage its exposure to foreign currency risk, interest rate risk and achieve exposure to assets and asset classes. The use of derivatives is governed by the Fund's Statement of Investment Policies, Standards and Procedures as approved by the Guardians, which provides written principles on the use of derivatives by the Group.

The fair value of forward foreign exchange contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

The fair value of cross currency swaps is determined using a discounted cash flow model.

The fair value of asset swaps is determined using a model, with the key inputs being interest rates and the pricing of inflation futures.

The fair value of interest rate swaps is determined using a model, with the key input being interest rates.

The fair value of credit default swaps is determined using a discounted cash flow model which incorporates default rate and credit spread assumptions for the reference entity or index.

The fair value of volatility swaps is determined using a discounted cash flow model with the key input being the volatility curve.

The fair value of futures contracts is calculated as being the present value of the difference between the contract price and the closing price reported on the primary exchange of the futures contract.

The fair value of index or total return swaps (commodity, equity, real estate and longevity contingent swaps) is provided by the counterparty and is calculated by reference to the movement in the underlying index or basket of securities or other contracts. Index swaps are settled net in cash.

The fair value of insurance-linked swaps is calculated using a model which incorporates the premium paid or received and a price provided by reputable pricing vendors or brokers. Premiums are recognised based on a risk dissipation schedule, derived from third party catastrophe models.

The fair value of exchange-traded insurance-linked options is the closing price as reported by the primary exchange of the contract.

The fair value of other 'over-the-counter' (OTC) swaps is determined using a model, with the key inputs being the expected future cash flows under the swap contract.

The fair value of options are calculated using a Black-Scholes option valuation model or, where the option is traded on exchange, the exchange price is used to value the option.

'Day 1' gains and losses

When the transaction price is different to the fair value from other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets, the Group immediately recognises the difference between the transaction price and fair value (a 'Day 1' gain or loss) in profit or loss in the statement of comprehensive income. In cases where the fair value is determined using data which is not observable, the difference between the transaction price and the model value is recognised on a systematic basis over the expected life of the trade.

(f) Securities lending

Securities lending transactions are collateralised by securities or cash. The transfer of the securities to counterparties is only reflected in the statement of financial position if the risks and rewards of ownership are also transferred. Collateral advanced by the borrower in the form of readily marketable securities (non-cash) is held in escrow by a third-party agent. Recourse to those securities is only available in the event of default by the borrower and, as such, the non-cash collateral is not recognised in the statement of financial position. Collateral advanced by the borrower in the form of cash is recognised in the statement of financial position as an asset, along with a corresponding liability to repay the cash collateral to the borrower, once the securities have been returned.

(g) Repurchase and reverse repurchase agreements

Securities sold under agreement to repurchase at a specified future date are not derecognised from the statement of financial position as the Group retains substantially all the risks and rewards of ownership. The corresponding cash received is recognised in the statement of financial position as an asset with a corresponding obligation to return it, including accrued interest as a liability, reflecting the transaction's economic substance as a loan to the Group. The difference between the sale and repurchase prices is treated as interest expense and is accrued over the life of the agreement using the effective interest rate.

Conversely, securities purchased under agreements to resell at a specified future date are not recognised in the statement of financial position. The consideration paid, including accrued interest, is recorded separately in the statement of financial position as an investment,

Summary of significant accounting policies (continued)

reflecting the transaction's economic substance as a loan by the Group. The difference between the purchase and resale prices is recorded in interest income and is accrued over the life of the agreement using the effective interest rate.

(h) Consolidation of subsidiaries

Subsidiaries are those entities that are controlled by the Fund.

The Group's financial statements incorporate the financial statements of the Fund and its subsidiaries, which have been consolidated. The results of any subsidiaries that become or cease to be part of the Group during the year are consolidated from the date that control commenced or until the date that control ceased.

All inter-entity transactions, balances and income and expenses are eliminated on consolidation.

The acquisition of subsidiaries is accounted for using the acquisition method of accounting. The acquisition method of accounting involves recognising at acquisition date, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. The identifiable assets acquired and the liabilities assumed are measured at their acquisition date fair values.

The difference between the above items and the fair value of the consideration (including the fair value of any pre-existing investment in the acquiree) is goodwill or a discount on acquisition.

(i) Investments in associates

An associate is an entity over which the Fund is in a position to exercise significant influence, but not control or joint control, through participation in the financial and operating policy decisions of the entity.

At inception, certain of the Fund's associates are designated at fair value through profit or loss under NZ IAS 39 Financial Instruments: Recognition and Measurement (in accordance with paragraph 1 of NZ IAS 28 Investments in Associates). All other associates are equity accounted in accordance with NZ IAS 28 Investments in Associates. The designation is made with reference to how the Guardians intends to manage the investment and the extent to which the Guardians will be involved in the management of the investment.

The results of associates which are accounted for under NZ IAS 28 Investments in Associates are incorporated in the financial statements using the equity method of accounting, except where the investment is classified as held for sale, in which case it is accounted for in accordance with NZ IFRS 5 Non-current Assets Held for Sale and Discontinued Operations. Under the equity method, investments in associates are carried at cost as adjusted for post-acquisition changes in the Fund's share of the net assets of the associate, less any impairment in the value of individual investments. Losses of an associate in excess of the Fund's interest in that associate are not recognised, unless the Fund has incurred legal or constructive obligations or made payments on behalf of the associate.

(j) Investments in joint ventures

A joint venture is a contractual arrangement whereby the Guardians and other parties undertake an economic activity that is subject to joint control, which is when the strategic financial and operating policy decisions relating to the activities of the joint venture require the unanimous consent of the parties sharing control.

At inception, certain of the Fund's joint ventures are designated at fair value through profit or loss under NZ IAS 39 Financial Instruments: Recognition and Measurement (in accordance with paragraph 1 of NZ IAS 31 Interests in Joint Ventures). All other joint ventures are equity accounted in accordance with NZ IAS 31 Interests in Joint Ventures. The designation is made with reference to how the Guardians intend to manage the investment and the extent to which the Guardians will be involved in the management of the investment.

The results of joint ventures which are accounted for under NZ IAS 31 Interests in Joint Ventures are incorporated in the financial statements using the equity method of accounting, except where the investment is classified as held for sale, in which case it is accounted for in accordance with NZ IFRS 5 Non-current Assets Held for Sale and Discontinued Operations. Under the equity method, investments in joint ventures are carried at cost as adjusted for post-acquisition changes in the Fund's share of the net assets of the joint venture, less any impairment in the value of individual investments. Losses of a joint venture in excess of the Fund's interest in that joint venture are not recognised, unless the Fund has incurred legal or constructive obligations or made payments on behalf of the joint venture.

(k) Forests

Forest assets are predominantly standing trees. These are recognised in the statement of financial position at fair value less estimated point-of-sale costs. The costs to establish and maintain the forest assets are included in profit or loss in the statement of comprehensive income together with the change in fair value for each accounting period.

The valuation of forest assets is based on discounted cash flow models. The annual harvest from forecast tree growth is multiplied by expected wood prices and the costs associated with forest management, harvesting, and distribution are then deducted to derive annual cash flows.

The fair value of the forest assets is measured as the present value of cash flows from one growth cycle based on productive forest land, taking into consideration environmental, operational and market restrictions. Forests are valued separately from the underlying freehold land.

(l) Livestock

Livestock is recorded at fair value less estimated point-of-sale costs. Fair value is determined by reference to recent comparable sales.

Changes in the value of livestock are recognised in profit or loss in the statement of comprehensive income.

(m) Inventory

All inventory items are stated at the lower of cost or net realisable value at balance date. The cost of agricultural produce transferred into inventory is measured at its fair value less estimated point-of-sale costs at the date of harvest. The net realisable value represents the estimated selling price of inventories less all estimated costs of completion and costs necessary to make the sale.

(n) Receivables

Short-term receivables are initially recorded at fair value, then subsequently at amortised cost using the effective interest rate less any impairment.

(o) Property, plant and equipment

Initial recording

All items of property, plant and equipment are initially recognised at cost. Cost includes the value of consideration exchanged, or fair value in the case of donated or subsidised assets, and those costs directly attributable to bringing the item to working condition for its intended use.

Subsequent measurement

Subsequent to initial recognition, leasehold improvements, plant and equipment are stated at cost less accumulated depreciation and any impairment in value.

Land and buildings are measured at fair value less accumulated depreciation on buildings and any impairment losses recognised after the date of revaluation. Fair value is determined on the basis of an independent valuation prepared by external valuation experts, based on discounted cash flows or capitalisation of net income (as appropriate).

Any revaluation increase arising on the revaluation of land and buildings is credited to the asset revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense in profit or loss, in which case the increase is credited to profit or loss to the extent of the decrease previously charged.

A decrease in carrying amount arising on the revaluation of land and buildings is charged as an expense in profit or loss to the extent that it exceeds the balance, if any, held in the asset revaluation reserve relating to a previous revaluation of that asset.

Independent valuations of land and buildings are performed with sufficient regularity (at least every three years) to ensure that the carrying amount does not differ materially from the asset's fair value at balance date.

Disposal

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset.

Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained surplus.

Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of an item) is included in profit or loss in the year the item is derecognised.

Impairment

All items of property, plant and equipment are assessed for indicators of impairment at each balance date. If any indication of impairment exists, an estimate of the asset's recoverable amount is calculated.

Where the carrying amount is assessed to be greater than its recoverable amount, the item is written down to its recoverable amount. The write-down is recognised in profit or loss in the statement of comprehensive income unless it

Summary of significant accounting policies (continued)

relates to land and buildings, in which case it is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the item is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the item in prior years. A reversal of an impairment loss is recognised in the statement of comprehensive income immediately unless it relates to land and buildings, in which case it is treated as a revaluation increase.

Recoverable amount is the greater of fair value less costs to sell and value in use. It is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs to sell and it does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash generating unit to which the asset belongs.

In assessing value in use, the estimated pre-tax future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

(p) Depreciation

Depreciation is provided on a straight-line basis at a rate that will write off the cost of the assets to their estimated residual value over their useful lives.

The useful lives of major classes of assets have been estimated as follows:

Land improvements	15-50 years
Buildings	25-50 years
Plant and machinery	3-17 years
Office equipment	3 years
Computer equipment	3 years
Motor vehicles	5-12 years
Office fitout	12 years

The cost of office fitout is capitalised and depreciated over the unexpired period of the lease (held by the Guardians) or the estimated remaining useful lives of the improvements, whichever is shorter.

(q) Intangible assets

Software

Software and licences are finite life intangibles and are recorded at cost less accumulated amortisation and impairment. Amortisation is charged on a straight-line basis over their estimated useful lives of 3 years. The estimated useful life and amortisation method is reviewed at the end of each annual reporting period.

Carbon credits

Allocations of New Zealand Units (NZU) and/or other carbon credits are initially recognised at fair value where they have been received, or the Group is reasonably certain that they will be received, and there is a market determined price. Other changes in the quantity of carbon credits are recognised as an operating gain or loss based on the fair value at the time of the transaction.

Subsequent to initial recognition, the carbon credits are measured at fair value at the date of revaluation less any subsequent accumulated impairment losses. Fair value for this purpose is determined by reference to an active market. If the carbon credits cannot be revalued because there is no active market, the carbon credits shall be carried at the amount initially recorded less any impairment losses. The carbon credits are assessed to have indefinite useful lives and as such are not amortised but are tested annually for impairment. An impairment loss is recognised when the carbon credits' carrying amount exceed their recoverable amount. Recoverable amount is the higher of the carbon credits fair value less costs to sell or value in use.

(r) Operating leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Leases where the lessor effectively retains substantially all the risks and benefits of ownership of the leased items are classified as operating leases. Operating lease expenses are recognised on a straight-line basis over the period of the lease.

Where there are contingent lease payments which are assessed to the closely related to the host lease contract, they are recognised as an expense as they arise.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as deferred income in the statement of financial position. The aggregate benefits of incentives are recognised as a reduction of rental expense on a straight-line basis over the period of the lease.

(s) Payables

Short-term payables are not interest bearing. They are initially recognised at fair value and subsequently at amortised cost.

(t) Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, the future sacrifice of economic benefits is probable and the amount of the provision can be measured reliably.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that recovery will be received and the amount of the receivable can be measured reliably.

(u) Income recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

For financial instruments measured at fair value, interest income is recognised on an accruals basis, either daily or on a yield to maturity basis. Interest earned on cash balances is accrued at the effective interest rate.

Dividend income is recognised when the shareholder's rights to receive payment has been established, normally the ex-dividend date. Where the Group has elected to receive dividends in the form of additional shares rather than cash, the amount of the cash dividend foregone is recognised as income. Any excess in the value of shares received over the amount of cash dividend foregone is recognised as a gain in the statement of comprehensive income.

Revenue from the sale of goods is recognised when the Group has transferred to the buyer the significant risks and rewards of ownership of the goods.

Securities lending fees are recognised as earned.

(v) Foreign currency transactions

Transactions denominated in a foreign currency are converted to New Zealand dollars at the exchange rate in effect at the date of the transaction.

Monetary assets and liabilities denominated in foreign currency at balance date are translated at the rate of exchange ruling as at that date. The resulting exchange differences are recognised separately in profit or loss in the statement of comprehensive income.

(w) Translation of the financial statements of foreign operations

Assets and liabilities of foreign operations with functional currencies other than New Zealand dollars are translated at the closing rate. Revenue and expense items are translated at a weighted average of exchange rates over the year, as a surrogate for the spot rates at transaction dates. Exchange differences arising from the foregoing are taken to the foreign currency translation reserve and recognised in the statement of changes in public equity.

Goodwill and fair value adjustments arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and translated at exchange rates prevailing at the reporting date.

On disposal of a foreign operation, the accumulated amount of the exchange differences taken to the foreign currency translation reserve that relate to the foreign operation is transferred out of the foreign currency translation reserve and recognised as income or expense in the statement of comprehensive income.

(x) Statement of cash flows

The following are the definitions of the terms used in the statement of cash flows:

Operating activities include all transactions and other events that are not investing or financing activities.

Investing activities are those activities relating to the acquisition, holding and disposal of property, plant and equipment and intangible assets.

Summary of significant accounting policies (continued)

Financing activities are those activities relating to capital contributions and to payments of superannuation entitlements (from 2020). As the current funding by the Crown of superannuation entitlements flows directly from the Treasury to the Ministry of Social Development it is not considered cash flow of the Group and is accordingly not recorded in the statement of cash flows.

Cash and cash equivalents

Cash and cash equivalents includes cash balances on hand, held in bank accounts, demand deposits and other highly liquid investments with an original maturity of three months or less, which have an insignificant risk of change in fair value.

(y) Goods and Services Tax (GST)

Revenues, expenses, assets and liabilities are recognised exclusive of GST, with the exception of receivables and payables which are stated with GST included. Where GST is irrecoverable as an input tax, then it is recognised as part of the related asset or expense.

Cash flows are included in the cash flow statement on a gross basis. The GST component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

(z) Changes in accounting policies

There have been no changes in accounting policies. The accounting policies have been applied consistently throughout these financial statements.

(aa) Significant estimates and judgements

In preparing these prospective financial statements, estimates and judgements have been made concerning the future. These estimates and judgements may differ from the subsequent actual results. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and judgements that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities are detailed within the following accounting policies and notes:

Note (e) Investments. In particular: fixed income securities where the market is illiquid; private equity funds; unlisted unit trusts; derivatives; 'day 1' gains and losses

- Note (k) Forests
- Note (l) Livestock
- Note (o) Property, plant and equipment – valuation of land and buildings
- Note (q) Intangible assets

SIGNIFICANT ASSUMPTIONS ADOPTED IN THE PREPARATION OF PROSPECTIVE FINANCIAL STATEMENTS

No capital contributions from the Government have been included in the forecast period, based on announcements made by the Government in the Budget 2009.

Investment returns for the forecast period are based on internal modelling of 20-year returns.

Management fees included in the forecast are based on investment management agreements that were in place on the date the forecast was approved by the Board. The Guardians' expenses are allocated according to the current allocation model.

The forecast has largely been based on actual experience to date with exception of the impact of foreign currency. No foreign currency impact has been forecast.

Material differences between the forecast and actual returns will occur due to two major factors:

1. investment markets generate returns at a level that is greater or lesser than the rate assumed in this forecast; and
2. foreign currency movements.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