Guardians of New Zealand Superannuation

After the Crisis – what's next for the New Zealand Superannuation Fund?

11th Annual SuperFunds Summit

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Today’s discussion

Agenda

- Why we exist and what we care about
- Maintaining focus during the crisis and capturing the rebound
- What’s next?
- The Fund and New Zealand

Why We Exist:
Our Mandate

- **Set out in section 58 of the New Zealand Superannuation Act 2001**

- **We must invest the Fund on a prudent, commercial basis consistent with:**
  - Best-practice portfolio management
  - Maximising return without undue risk
  - Avoiding prejudice to New Zealand's international reputation

- **Legislation does not prescribe what this means – it is up to the Guardians to determine**

Sets the context for all investment

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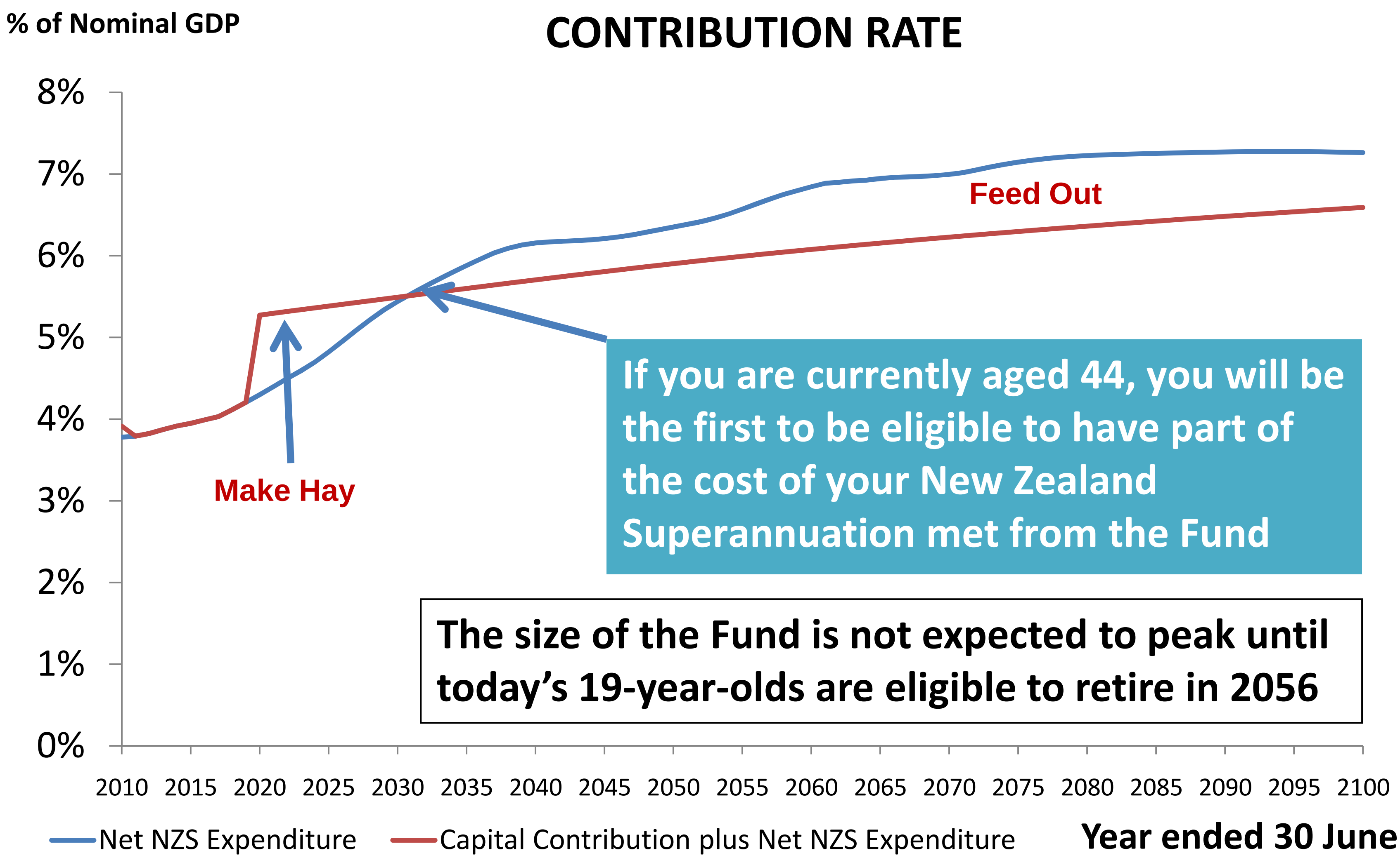
Why we exist:
Intergenerational Transfer



Source: NZ Treasury

What Matters:
The absolute return net of all costs

We think across decades

- The long-term return to the Fund net of all costs and foreign taxes is the ultimate measure of fulfilling our mission

- Current reference point is outperforming 90-day Treasury bill (T-bill) rate

- Based on our reference portfolio and our expectation of the value added in the 'actual' portfolio we expect to outperform T-bills by at least 2.5% per annum over rolling 20-year periods

- It is measured on a time-weighted basis before NZ tax, as tax is a return to the Crown

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Retaining our focus during the crisis...

A clear purpose: reducing future NZers' tax burden

Discipline to stay the course:

- Well-defined organisational and accountability structure
- Structure strategies and incentives to be invariant to short-term market-movements

Deliberate financial exposure:

- Diversification through our asset allocation
- Maintain flexibility to evaluate and buy into new investment opportunities…**ADDING VALUE**
- … while undertaking thorough diligence and maintaining risk commitments

Communication to key stakeholders

- Proactive, often, in all weathers

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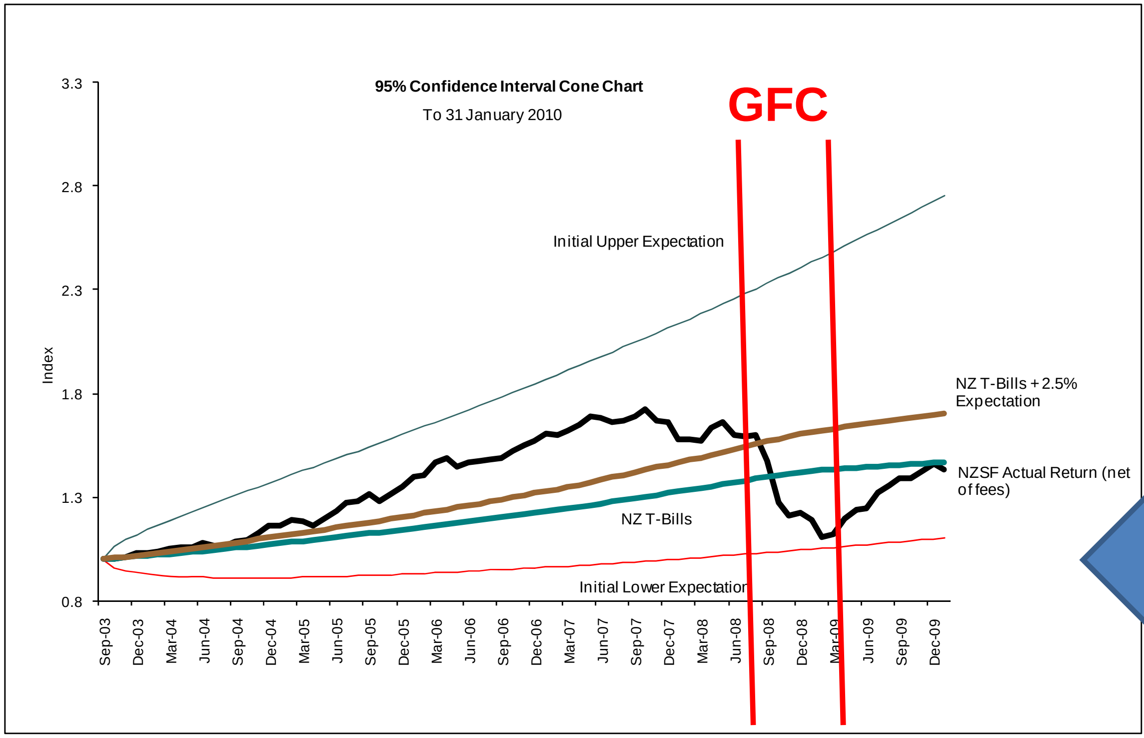
… and capturing the rebound



Returns

FYTD 28 February	Since inception to 28February
17.24% ($2.34bn)	6.04% ($2.43bn)

Impact of GFC is clear

Contributions since inception	$14.88 billion
Contributions less NZ tax paid since inception	$13.53 billion
Fund size at 31 January	$15.94 billion
Fund size relative to contributions since inception	**+$2.41 billion**

What's Next?
1 – Maintain belief-driven investment

Beliefs	Theoretical underpinnings	Investment Strategies	Organisational Capabilities
?	?	?	?

- Beliefs closely held and sternly tested
- Underpin all investment strategies and drive requirements for organisational capabilities
- If an investment opportunity is not aligned with beliefs, strategies or capabilities we do not invest

BUT

- If investment opportunity accords with beliefs and strategies it is maintained regardless of short-term 'noise'
  - As happened in GFC

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What's Next?
2 – More transparency, transparency, transparency

We are internationally recognised among SWFs for transparency

- **In <u>good</u> times we were very clear that what was up was likely to come down**
- **In <u>tough</u> times**
  - we huddled with the Board on our beliefs, strategies and capabilities
  - we kept the Minister and the public informed on what was happening and our reaction to it
- **At <u>all times</u> we make it very easy for people to understand**
  - Our purpose
  - Why our portfolio is fit for that purpose
  - Why staying our course is the best strategy

Stakeholder clarity about why we exist, what we do and why has reputation and commercial benefit

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What's Next?
3 – More opportunistic investment

This is a good time for more opportunistic investment

We have a strong team and organisation

- Clear strategies across diverse asset classes
- GFC-hardened organisational backbone
- Well placed for future and for current stressed market conditions
    - *Strategic tilting April-August 2009 was successful, will broaden our approach*
- Additional capabilities added to capture opportunities – Treasury, NZ Direct

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What's Next?
4 – Raise awareness of our NZ impacts

The Fund pays complementary present and future dividends

- One of New Zealand's few long-term savings and investment vehicles
- Primary beneficiaries are future New Zealanders

Meanwhile

- Taxpayer ($1.35 billion since inception)
- We make important additional contribution as a consequence of our activities (investment, liquidity, external relationships and skills)
    - Recognised by the Capital Markets Development Taskforce

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New Zealand's Capital Markets and Productivity

How we can contribute

- Our scale and strong commercial focus represents significant potential to add value to investments in New Zealand
- Can invest in productive assets that may struggle to attract investment from other sources
- Can build general capabilities and capacity in New Zealand capital markets through
  - Shaping governance practices
  - Relationship management
  - Creating demand for new asset classes and high-quality opportunities
  - Establishment of retail feeder fund to our joint social infrastructure investment vehicle with Morrison & Co good example of positive, present, local flow-on effects of our investment

Deepens NZ capital markets, enhances our productivity

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Exhibit 1 – NZ Expansion Capital Strategy

The Strategy reflects the Guardians' view that there is a significant pool of smaller high-growth companies in New Zealand constrained by a shortage of long-term equity and a lack of access to skilled investment management

What do we want?

- Enterprise value of $15-50 million
- Clear and credible high-growth plan typically >20% compound annual revenue growth
- Investments will primarily support expansion through strategic acquisition, technology upgrades, or market expansion
- Defensible Intellectual Property, ongoing profitability growth and positive cash flow
- Opportunity to add operational value
- Sound governance
- Genuine investment liquidity opportunities over a three-to-seven-year timeframe through Initial Public Offering, trade sale or recapitalisation

Current New Zealand investment

Approximately 15% of the Fund is invested in New Zealand (29% including cash). Does not include commitments made but not yet called (c$270 million).

Asset Classes

- **Listed equities (passive/active)**
- **Private Equity**
- **Timber**
- **Property**

Strategies

- **Direct investment**
- **Expansion Capital**
- **Infrastructure**

Existing activity includes

- **PIP Fund commitment ($100 million commitment)**
- **AMP property portfolio (c$270mm)**

Further developments

- **Assessing feasibility of global rural land strategy**
  - **Relies on sufficient yields to meet opportunity cost hurdle**
- **If strategy proceeds will include, and possibly start, with NZ**

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Appendices

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The New Zealand investment directive

What it says

- *"It is the Government's expectation, in relation to the Fund's performance, that opportunities that would enable the Guardians to increase the allocation of New Zealand assets in the Fund should be appropriately* ***identified and considered*** *by the Guardians."*

What it doesn't say

- There is no prescribed Fund minimum, as such it is not inconsistent with our mandate to invest on a prudent, commercial basis

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Impact of reduction in funding

What happened

- Government to reduce contributions to the Fund until the Crown operating balance returns to surplus sufficient to resume
- Treasury estimates this to occur in 2021
- Received a one-off $250 million contribution in July 2009 but we are assuming zero contributions until 2020

What it means

- Our investments in property and other asset classes will not be as large as they would have been

What it doesn't mean

- A change in our diversified approach to manager selection, markets and strategies

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