



NZSUPERFUND

*Te Kaitiaki Tāhua Penihana
Kaumatua o Aotearoa*

TITLE:

External Manager Selection & Management

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EVENT | PRESENTATION:

Thursday 5 November 2015

Purpose of Presentation

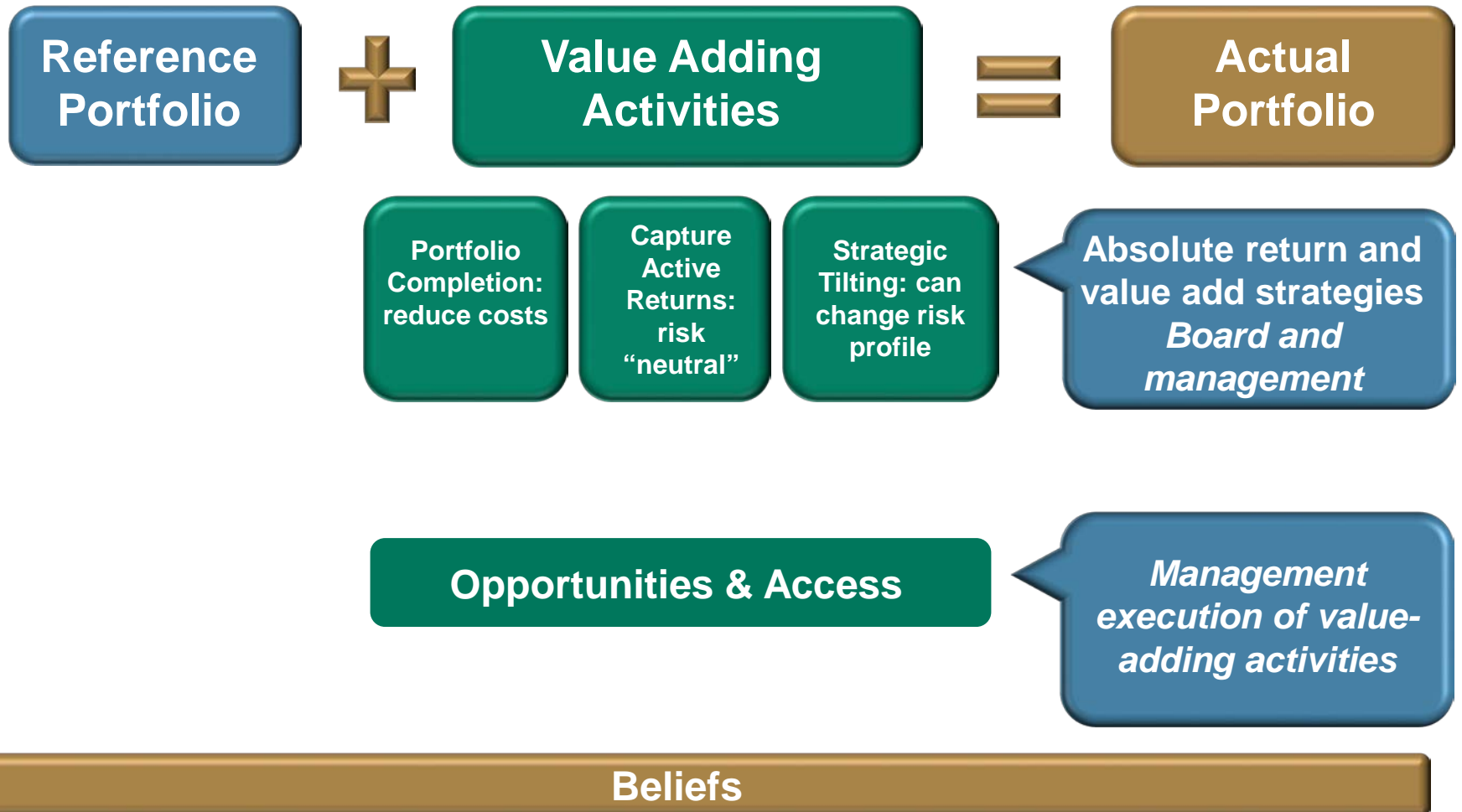
- Overview of the Super Fund's Investment Approach
- Describe how external managers fit into the Fund's overall investments
- Describe how we approach operations diligence for external managers

Our Approach: Reference Portfolio

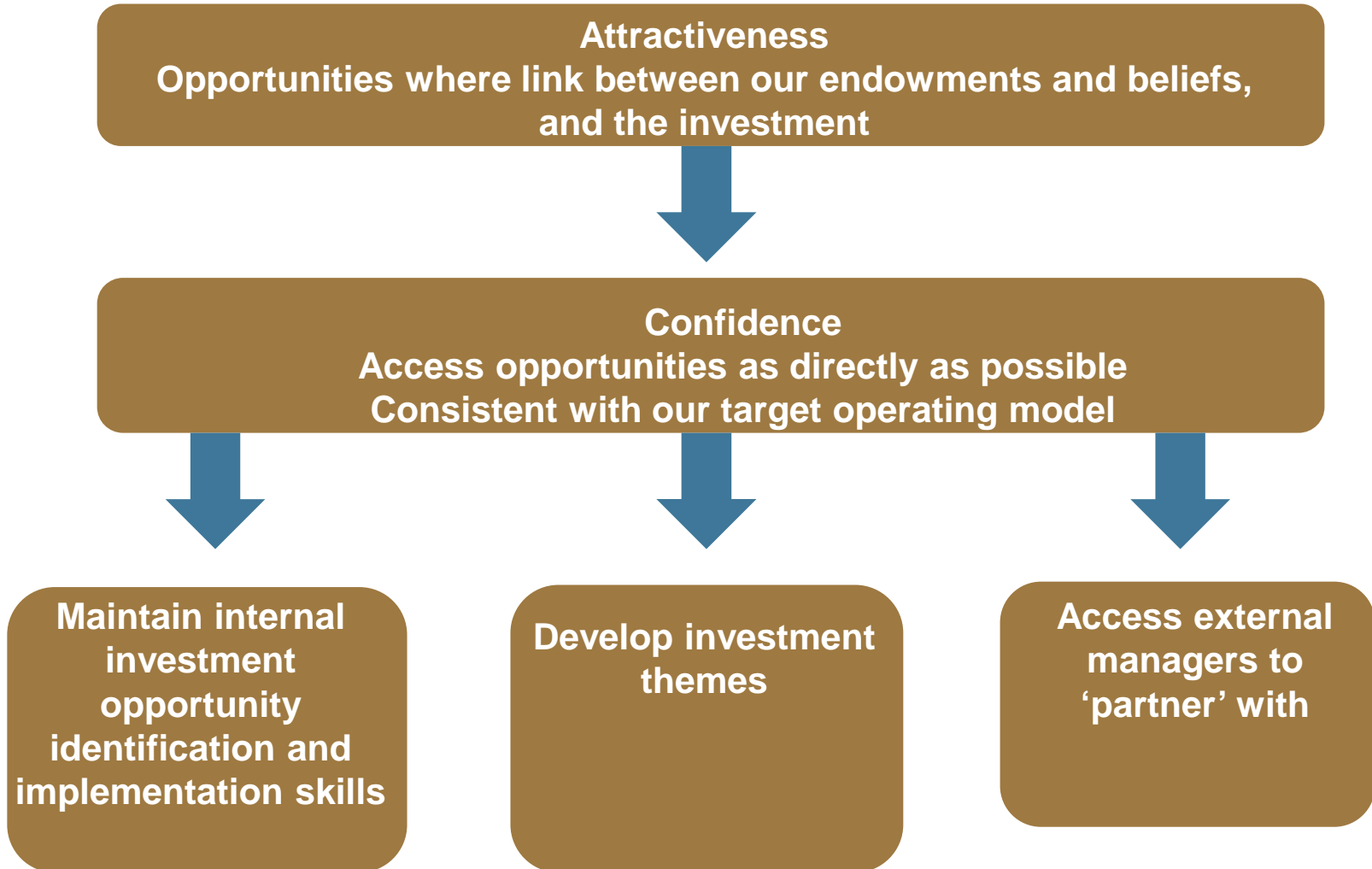
- Our Reference Portfolio
 - Low-cost, passive and implementable portfolio which is expected to achieve Fund objective
 - Degree of risk appropriate for a long-term investor
 - Chosen by the Board
- Provides a benchmark for assessment
 - Is management adding value with active strategies?

Asset class	Percentage
Global equities	75%
NZ equities	5%
Total growth	80%
Total fixed interest	20%
TOTAL PORTFOLIO	100%
Net un-hedged foreign currency exposure	0%

Building the actual portfolio: anchored to beliefs, clarity around risk, reward and responsibility

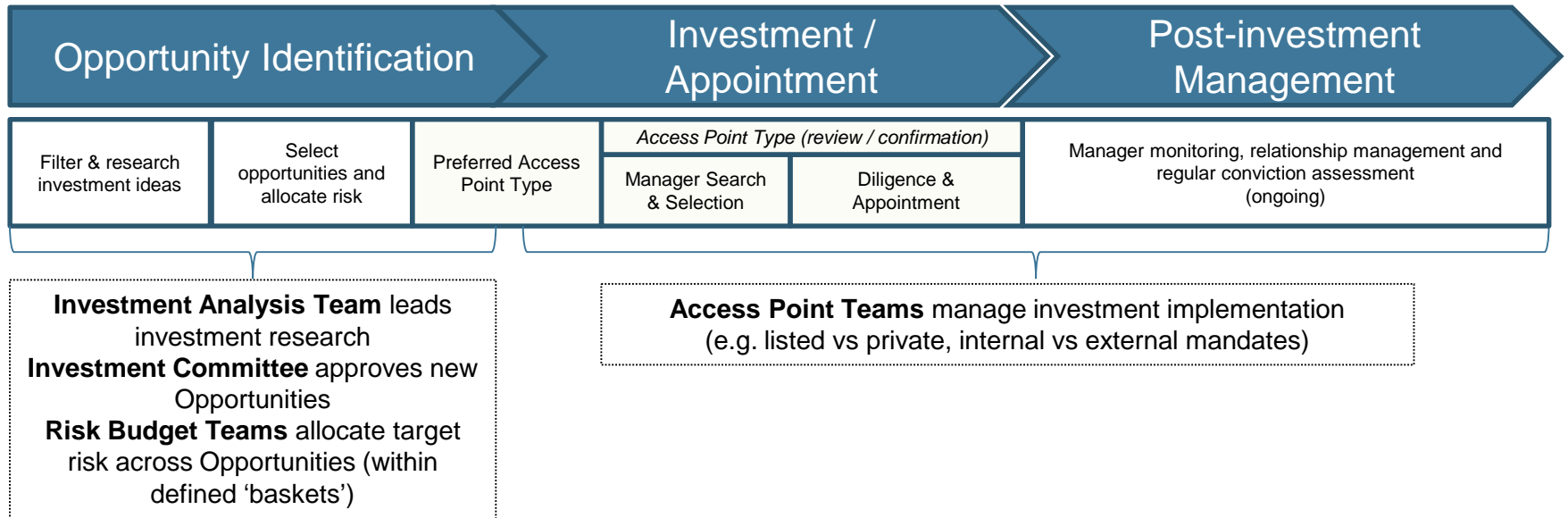


Our Investment Framework: Being Opportunistic



Active Opportunities: Our Investment Process

We separate the Investment Opportunity we are targeting, from how we access that Opportunity



Preferred Access Point Type

- Likely Access Point Type (direct, co-invest, listed, unlisted) identified during initial research
- Set access point search parameters / priorities for initial screening (test hypothesis and identify manager universe)
 - Strategy fit with opportunity (industry, value chain, geography etc)
 - Core investment focus / style needed to access opportunity (taking into account risk profile and E(r), depth and duration of opportunity, views on required flexibility/liquidity)
 - NZSF requirements (investment size/capacity, capability development etc)
- Evaluate access point types against search parameters
 - Internal discussions for direct
 - Review of existing managers (co-investment, side-car or new mandates)
 - Advisor discussions on potential universe
 - Peer discussions / recommendations
 - Attend relevant conferences plus preliminary manager meetings based on advisor/peer recommendations



Iterative process as feedback from potential access points informs thinking

Manager Search, Selection, Diligence & Appointment

- If an external manager is the preferred access point type, the Investments Team proceeds to identify and engage a specific manager

- Key steps in the Appointment process are:
 - Manager search (available universe => shortlist)
 - Manager selection (identify preferred partner)
 - Manager Diligence
 - Appointment

- Following Appointment, the Investments Team's focus shifts to monitoring / ongoing relationship management and knowledge sharing

Manager Search & Selection

- Managers assessed against selection criteria
 - Strategy fit with opportunity
 - Investment focus/style
 - Investment size/capacity
 - Capabilities
 - Performance (track record vs peers and PME cashflows – confirm returns will beat our required ‘Hurdle’)
 - Process (transparency/visibility and confidence in internal decision processes to support investment strategy; approach to RI/ESG)
 - Commercial terms (fees)
 - Alignment (ownership, economics-sharing, terms, style fit (direct-ish, flexibility)
 - Potential to become Strategic Partner (cultural/view “fit”, value-add potential beyond mandate, future investment mandate potential, willingness to engage in IP transfer etc)

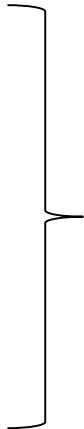
- Assessment based on direct discussions with manager (including headline terms), performance analysis, advisor recommendations, peer references
 - Follow up visits to manager by lead investment professional and Operations DD team

- Performance evaluation feedback on risk/return and opportunity attractiveness

Manager Diligence

- Once preferred partner is selected, proceed to full diligence review and finalise engagement terms

- Opportunity consistency
- Viability
- Structure & focus
- Trust
- Risk awareness & management
- People capability
- Process capability
- Performance



Satisfying these conviction criteria gives us confidence that the manager will execute on the target investment opportunity and generally conduct itself in the way we expect.

- Diligence activities involve detailed data analysis, multiple on-site visits and referencing

Manager Appointment

- In parallel with diligence, negotiate terms, finalise investment structure and documentation

- Terms: what is important (our Target Operating Model)
 - Flexibility in commitment / investment (switch on/off in line with our changing views on the opportunity)
 - Visibility – line of sight into investments and performance
 - Consistency with our investment requirements (e.g. RI)
 - Transparency in investment process / management / reporting (support our early warning system)
 - Partnership approach with IP Transfer and Fund-wide access into manager, in line with segmentation
 - Alignment with / protection of our interests (performance-oriented fees, minimise potential for conflict, Fund protections e.g. concentration limits, leverage, investment restrictions, key person etc)
 - Cost efficiency (low fees)

Manager Engagement & Monitoring

- We Segment our managers and develop a relationship plan for each, informing ongoing interaction, level and frequency of engagement, desired outcomes (e.g. collaboration, manager input into opportunity views etc)
 - Manager’s segment determined by assessment against:
 - Consistency (with investment opportunity)
 - Capability (how good they are, what we can learn)
 - Commitment (to Fund relationship)
 - Capacity (ability to help access wide range of opportunities)

- Monitoring and Conviction / ‘Scorecard’ views trigger actions at both manager and investment opportunity level
 - Scorecard-triggered → monitoring intensity, suspend/terminate or scale up/down investment, Segmentation-shift
 - Opportunity triggered → scale up/down investment, suspend/terminate mandate

Operational DD

How We Fit In

- Part of Enterprise Risk team within the Finance & Risk group
- Work closely with Investments Teams but are independent
- Active members of the New Investment Group and Operational Risk Assessment (ORA) process
- Operational DD process forms part of Scorecard Conviction and informs our confidence in a manager's Process Capabilities and Viability

Skills and Benefits

- Independence from Investments Team allows us to form our own opinion on manager operational capability
- We are often the only other team to go onsite
- We meet with staff that others may not (COO, CCO Legal, CFO, HR, IT etc.) and lower levels of staff
- Review many areas and processes that may not be reviewed otherwise
- Frequent interaction

What We Do

- Monitor firms to ensure their continuing operational capability
- Tailor a risk-based approach and rate each firm on a) their strategy / asset class and b) firm-specific risks.
- Apply risk ratings to guide frequency of interaction
- Review firms through a combination of desktop DD & onsite DD
- Review reports (Financial Statements, Regulatory Filings and Internal Controls) to identify issues, control weaknesses or anomalies (disclosure items, deviation from investment strategies)
- We have our own gate but this is not a gate to appointment. Concerns are addressed through Operational Risk Assessment if pre-investment, or via the Investment Lead Professional if post-investment

Scope

- Incumbent and potential organisations across broad array of opportunities, asset classes, services, and third parties

Operational DD

Desktop Due Diligence

- Semi-annual DDQs
- Annual Financial Statement Review
- Policies, Compliance Manual, Code of Ethics
- Offering Documents
- Internal Controls Report/ SOC1/ GS007
- Marketing Material
- Regulatory Searches
- Background Checks
- Third Party Relationships
- Internet Searches – news, Google alerts, website
- Internal GNZS Relationships

Onsite Due Diligence

- Firm Overview, AUM, Ownership, Structure
- Staffing & Culture
- Governance
- Regulatory Compliance
- Internal Compliance
- Investment Process/ Trade Lifecycle Demonstrations
- Cash Management
- Counterparties and Third Parties
- Valuation
- Systems & Service Providers
- IT, Business Continuity & Disaster Recovery

Key Outputs

- Comprehensive reporting provided on due diligence
- ORA populated for pre-investment risks identified
- Annual Financial Statement review
- Reporting to Investment and Risk Committees
- Follow up and recommendations