

## Z Energy Stakeholder Dinner

### Speech, Adrian Orr 18 October 2016

Tena kotou, tena kotou, tena kotou katoa

Talofa Lava, Kia Orana, Malo e Lelei, Ni Bula Sa Vinaka

Good evening everyone

Six years ago the Guardians of the New Zealand Superannuation Fund, together with Infratil, purchased Shell's downstream assets in New Zealand and formed what we all know today as Z Energy.

From the very beginning, the relationship between the Guardians and Z Energy was characterised by a number of commonalities. A long-term focus. A transparent style of communication. A commitment to good corporate governance.

All important. All things the market needs to see more of, by the way.

Significant progress has been made since then. In the space of six years, Z has come a long way. What was once a division of an international conglomerate has grown into an iconic Kiwi company.

The transition took courage on the part of all concerned. It required vision, conviction, and leadership across many facets. And today, Z Energy is realising some of the rewards borne of these decisions.

- In the New Zealand marketplace 'Z' is now synonymous with excellence across all sorts of fields: shareholder returns, customer relations, ESG, health and safety, sustainability, diversity...to name but a few.
- And as a result, it has built up significant reputational capital – this year it placed fourth on the New Zealand Corporate Reputation Index.

It is a company that all of us here in this room can be proud of.

And it is certainly not burying its head in the sand on the big challenges as we head into an uncertain future.

And tonight, I would like to comment on a number of these challenges. Challenges that, by virtue of our shared peculiarities, Z Energy and the New Zealand Super Fund stand poised to tackle together.

And while these challenges are formidable, they also present us with a number of opportunities. Opportunities to:

Make our capital more inclusive

Our governance structures more resilient

And our strategies more sustainable.

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*[ Z in the past - background on Z & NZSF partnership ]*

At the Guardians we see ourselves as a long-term investor. We choose to reflect this by taking a long-term perspective in our investment approach.

Importantly, long-term investing is about more than just the term over which you hold an investment. Case in point – taking a long-term perspective doesn't actually mean you have to invest for a long time.

What it does mean – is that you *can*.

The Fund's long-term horizon means we are free of artificial constraints around time.

- Our pay-outs to the Government to partially fund New Zealand Superannuation are not projected to start until 2030-32.
- And beyond this the Fund will continue to grow in size in real terms, peaking at around a third of GDP in the 2070s.

Being a large scale, long-term investor has a number of important advantages.

For one thing, we do not have to base our investment decisions solely on the returns expected over short periods of, say, a year or two.

Instead, we can look past the fluctuations and devote greater focus to the factors that are going to matter 10, 20, 50 years down the line.

In practice, this means that as asset owners:

We understand that it's about more than just the bottom line

We are able to commit the necessary time and resources up front – even amid considerable uncertainty as to when and whether our efforts will bear fruit

We can forge strong relationships with the companies we are investing in

And we can help to ensure they are in a position to leverage the strengths of their business in order to confront challenges and capitalise on emerging opportunities.

We are constantly looking for opportunities in the marketplace that will allow us to leverage these advantages to benefit our partners. We want to provide the platform that allows companies like Z Energy to get on with doing what they do best.

*[ Z today – how our partnership has paid off ]*

In 2010, when Z first embarked on its journey, there were a number of key things that it did really well.

It invested heavily in service stations and customer service. Today, Z's customer-focus is what sets it apart from its competitors. It has raised the bar for others in the industry.

## C1 - Public

As an extension of this - it applied a community focus. It gave back.

It looked closely at the health and safety of its workplace environment. After all, nothing destroys shareholder wealth faster than getting it wrong on health and safety. On the other hand, you know that if a company is managing health and safety well, chances are it is a well-managed company overall.

Z has led the way in advocating for reforms to New Zealand's health and safety legislation. It has laid down the gauntlet for others in the industry, challenging the market to reflect risks in advance, to make the necessary changes across all metrics - all elements of their operation.

And it's backed up its stance with robust health and safety risk management system. This has helped to foster a company culture in which safety and employee wellbeing is paramount.

It put in place an exceptional management team supported by a capable and well-functioning board.

It set about creating a constructive organisational culture. As part of its culture initiative, Z made a commitment to recognise diversity and equality of opportunity. It sought to access a wider pool of talent, and to create the conditions necessary to allow its talent to thrive. Today, 3 out of its 7 board members are women, and women make up significant chunk of its executive team and senior managers.

But this is not a quick-fix issue – it's not something we're going to solve overnight. As at the Guardians', diversity and inclusiveness will remain a key priority for Z as it moves toward the next stage of its journey.

It has put in place a robust and aspirational sustainability strategy. More on this later.

And it took communicating and engaging with its stakeholders seriously – right from the start. Two of its founding organisational values are “share everything” and “be straight up”. The transparency with which it operates today is distinctive - it is without parallel in its industry.

It's open and honest communication extends beyond bottom line financial metrics, and includes those measures that are less black and white.

For example, in 2015 Z moved to a reporting framework in line with international benchmarks measuring environmental, social and governance factors (or ESG).

The value in good management of ESG factors is a well-established corporate belief. In particular, there is evidence to suggest that companies that score highly on ESG measures:

- Will use resources more efficiently
- Are more likely to possess an engaged and productive workforce, and – most pertinently
- Are best placed to adapt to change.

Reflecting this, the quality of a company's non-financial reporting has become an increasingly important consideration for institutional investors. In time, we see it becoming a key reporting benchmark in the marketplace.

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At the Guardians, we believe identifying and managing ESG factors helps us to avoid the poor performance and enterprise failures that can arise from lax governance and weak environmental and social practices.

It facilitates a greater understanding of the businesses we invest in, and means we are less swayed by momentum and trends.

And as a result –

Over the long-term we expect that our returns will be higher, and our downside risks lower.

*[ Z & NZSF in the future – focus on climate change ]*

Which leads us to climate change.

There is no doubt that climate change poses a material risk to the NZ Super Fund, and to other long-term investors.

It also creates an uncertain regulatory environment, which can lead to a culture of reluctance.

This means a lot of things, but in particular, it means that efforts to release capital for climate change initiatives are impeded. In other words, concerns about regulating climate change are interfering with efforts to combat concerns about climate change.

Along with being generally pretty dispiriting – and a bit of a mouthful to say – this poses a real threat to long-term, sustainable value creation.

And to add to our woes, climate change means some assets we invest in today may become “stranded” – rendered uneconomic by proper pricing of the carbon pollution externality, made obsolete by new technologies, or face a dwindling market as consumers vote with their feet.

I hope I am conveying to you here the reality that climate change risk is not confined solely to the energy sector, or to matters of energy efficiency. It spans political, environmental and social dimensions and it encompasses a host of different industries.

At the Guardians, our climate change strategy – which we will formally announce tomorrow - aims to make the Fund's portfolio more resilient to climate change and climate change policy risk.

From our perspective, reducing exposure to these risks is good for the portfolio, and it goes to the core of our mandate – which requires us to maximise returns without undue risk to the Fund as a whole.

It is also consistent with our responsibilities as a responsible investor.

And on a wider level, it is in keeping with the nation's policy response. We note that New Zealand has just ratified the Paris agreement on climate change. Under that agreement, we have a target of reducing greenhouse gas emissions to 30% below 2005 levels by 2030.

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The strategy is timely given the investment implications of climate policy will be a key topic at this year's annual meeting of the International Forum of Sovereign Wealth Funds (IFSWFs).

The theme of the meeting, to be held in November, is "Investing in a Climate of Uncertainty: The Sovereign Wealth Fund Response".

The conference will feature leading international speakers on the global economic outlook and climate policy. About 200 leaders of global sovereign wealth funds, international financial institutions, academics and sovereign wealth experts are expected to gather together in Auckland.

The conversation is worth having in the investment industry – and although it is typically a difficult one – it is one worth having in the energy sector too.

So, in the spirit of this, I ask:

What does climate change mean for Z Energy?

Well, the reality is Z is an energy transportation company operating in a carbon constrained world.

And that world is moving to reduce its dependence on fossil fuels. It will possibly eliminate their use eventually.

This is spurring an outbreak of innovation across industries – prompting the development and uptake of new technology.

Already we are seeing passenger cars using alternative fuels on New Zealand roads.

Rapid progress in battery technology is being made – electronic vehicle manufacturers continue to announce new models with greater capabilities, including longer range.

Classic cases of disruptive innovation.

And true to form, Z has a refreshingly frank stance on the matter.

It doesn't see itself as just a fossil fuels company. It says it is not chained to the continued extraction of fossil fuels. It is a transport energy company – it gets Kiwis from A to B.

It is implementing sustainability initiatives across its entire operation.

And the efficiencies aren't confined to itself either – it's helping its customers use fuel more efficiently.

In fact, it is already helping to develop alternative, sustainable energy sources.

It is striving to become the nation's largest supplier of biodiesel. Its plant, based in Wiri, Auckland, will turn inedible tallow, a by-product of the New Zealand meat industry, into up to 20 million litres of biodiesel a year. The fuel will meet or exceed stringent New Zealand and European fuel specifications. It will be competitively priced, acting as a viable alternative for Z Energy customers.

## C1 - Public

And this is taking place without a biofuel grant – possibly a world first, and a testament to Z Energy's forward looking initiative when it comes to sustainability.

Everything that has been implemented up to this point, everything that makes Z, Z – its commitment to the well-being of New Zealanders, its focus on ESG, and its long-term outlook – place it in an excellent position to further grapple with this challenge moving forward.

As Z itself says, when it comes to climate change it's in the unique position of being able to move from being a part of the problem to being at the heart of the solution.

So too the Guardians, and other cornerstone participants and beneficiaries of the capitalist system. We all have a critical role to play in reinventing the wheel to help improve the performance of NZ business - and resolve the defining challenges of our time – climate change, environmental degradation and population ageing alike.

*[ conclusion ]*

Now the reality is, for us, opportunities like Z do not come across our desks every day. In fact, suitable opportunities of scale in New Zealand are now few and far between.

To help change this, we plan to set up an “investment hub”, leveraging our long horizon to create investment opportunities in the New Zealand market.

We want to see change, and we hope to be a part of bringing about this change. Specifically, we think

Companies and their owners must take greater notice of factors that impact long-term value. They must be less swayed by momentum and passing trends. Short-termism is the very antithesis of what we need.

Investors must take pains to understand the businesses they are investing in, and the industries within which they operate.

Companies must have conviction in their strategies. They need to back themselves in staying true to those strategies, even if it means taking risks that could impact short-term performance.

They need to communicate with their stakeholders – early and often. This means helping stakeholders to understand the implications of their choices, including, crucially, that they can sometimes lead to volatility in the short-term. This is vital in ensuring the market understands and supports their strategies.

Z's communication thus far has been nothing short of excellent. However, it takes more than just good – even excellent – communication. Words must be backed up with action. This is where a strong track record comes in, helping to reinforce confidence and trust in the marketplace.

Z is in a very fortunate position where its track record and strong execution gives its strategies credibility. As it looks to the future, it must leverage this. It must utilise its core

## **C1 - Public**

strengths, the same strengths that have allowed it to grow into the company it is today. It must be pro-active if it is to weather the harsh reality of an increasingly rapid rate of change.

And for the most part, this is not going to be easy. It takes courage to face change and to make change.

Fortunately, Z Energy is already well-versed in matters of courage.

It took courage to embark on the journey to separate the downstream assets of Shell and create Z Energy.

It took courage to list on the stock exchange, to move from answering to two shareholders to 10,000.

And it will take courage to rise to the challenge, to show leadership under changing conditions, and to move forward in an uncertain future.

Thank you