

TITLE:

Guardians and NZSF Update 2011/12 Review

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CHAIRMAN

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EVENT | PRESENTATION:

Commerce Select Committee, 21 February 2013

Agenda

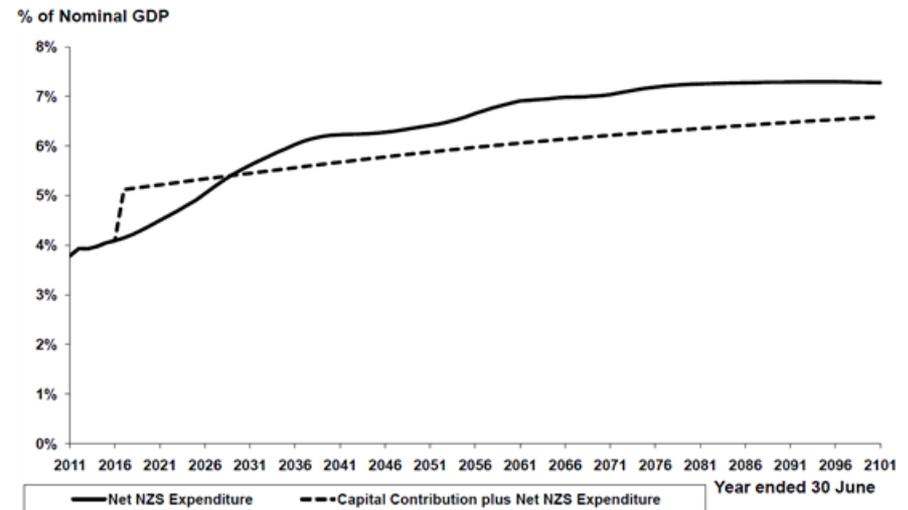
- What we do and how
- How we benchmark
- How we have performed
- Key points; priorities and challenges

What we do and how

New Zealand Superannuation Fund - Overview

- Long-term savings vehicle to partially meet the rising future cost of New Zealand Superannuation
- First withdrawals scheduled 2029/30 based on Treasury forecasts
- Commenced investing Sept 2003
- Enabling legislation - *New Zealand Superannuation and Retirement Income Act 2001*
- Double-arms'-length autonomous Crown entity

Save Now – Support Future



NZ Treasury Graph

What we do and how

■ **Mandate** (as per the Act):

- The Guardians must invest the Fund on a prudent, **commercial** basis and, in doing so, must manage and administer the Fund 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.

■ **Mission:**

- ‘Maximise the Fund’s return over the **long term, without undue risk**, so as to reduce future New Zealanders’ tax burden’

■ **Vision:**

- ‘A great team building the best portfolio’

What we do and how

Directive from the Minister of Finance – New Zealand investment –
May 2009

- “... that opportunities that would enable the Guardians to increase the allocation of New Zealand assets in the Fund should be appropriately **identified** and **considered** by the Guardians.”
- “This direction is not intended to be inconsistent with the Guardians’ duty to invest the Fund on a prudent, commercial basis, in accordance with section 58 of the Act, and the above paragraph is subject to that duty.”
- **We are actively identifying and considering, and successfully investing in, New Zealand opportunities - where they will add value to the Fund**

What we do and how

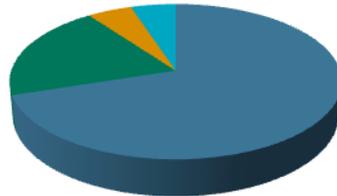
We look to fully utilise the Fund's liquidity profile, long-term investment horizon, and governance strength

- We construct a portfolio that balances our highest estimated return with financial risk → best chance of success
 - First capital withdrawal not until 2029/30
 - Strong weighting towards growth assets (which can be volatile over the short term)
- Principles of long-term investment:
 - A clear purpose
 - Discipline and capacity to stay the course
 - Transparency and clear communication to stakeholders

What we do and how

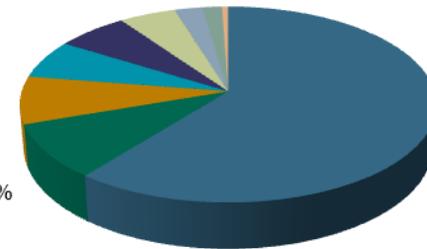
Reference Portfolio

- Global equities 70%
- Fixed interest 20%
- Global listed property 5%
- NZ equities 5%



Actual Portfolio as at 31/01/13

- Global equities 61%
- Fixed income 9%
- Infrastructure 8%
- Timber 6%
- Property 6%
- NZ equities 5%
- Other private markets 2%
- Private equity 2%
- Rural farmland 1%



Clarity around risk, reward and responsibility

Reference Portfolio



Value Adding Activities



Actual Portfolio

Low-cost, growth-oriented passive portfolio that could achieve Fund objectives; provides clear benchmark to assess the value we add as active managers

Dynamic asset allocation

Investment Strategies (e.g. PE, timber, infrastructure, rural, NZ direct)

Treasury Management (i.e. liquidity management, FX, passive market exposure)

Our Investment Beliefs

What we do and how

Clear understanding of how each investment adds to the performance of the Fund's risk and return profile, relative to all other opportunities

Developments since previous Select Committee appearance (November 2010)

- All investment opportunities can now be ranked on consistent **financial attractiveness** and **investment confidence** factors
- Confidence ranking has led to more internal management, flexible external management arrangements, and reduced costs and external agency risks
 - Recognised in reorganisation of investment teams
- Increased focus on risk management ownership and processes
- Development and integration of investment themes – emerging markets segmentation; resource sustainability; evolving demand patterns

What we do and how – Responsible Investment (RI)

- RI Centre of Excellence
 - provide research and advice on responsible investment to other CFIs
 - each CFI's Board makes decisions appropriate to their Fund
- RI Framework
 - RI integrated into all our investment activities
 - pre-investment analysis - risk assessment and due diligence
 - ownership activities e.g. voting
 - Transparent reporting and measurement via UNPRI assessments
- We exclude companies that are directly involved:
 - in the manufacture of cluster munitions;
 - in the manufacture or testing of nuclear explosive devices (not maintenance or delivery);
 - in the manufacture of anti-personnel mines;
 - in the manufacture of tobacco, and
 - in the processing of whale meat.
- We can also exclude companies for severe breaches of our responsible investment standards

How we benchmark success (global best practice)

We have chosen to benchmark against relevant global peer funds and best practice industry principles and measures

	Internal measures and mechanisms	External measures	Stakeholder engagement
Cost structure	By business unit By investment opportunity Holistic view of fees	CEM Benchmarking Hay remuneration database	Peer fund engagement: <ul style="list-style-type: none"> • 3Cs: co-operation, comparison and co-investment Global expertise
Governance	Reference Portfolio Review Internal Audit	Independent Reviews '04, '09 OAG special performance audit ('08) SWF GAAP Select Committee Reviews	
Performance	NZ T Bill rate + 2.5% Reference Portfolio + 0.5%	Performance against both measures published monthly	
Transparency	Website Annual Report OIA	Sovereign Wealth Institute's Transparency Index	
Responsible Investment		UNPRI assessments	
Risk	Risk Committee Reviews Risk Records & Registers Investment Risk Limits Target Liquidity Level	CEM Benchmarking	

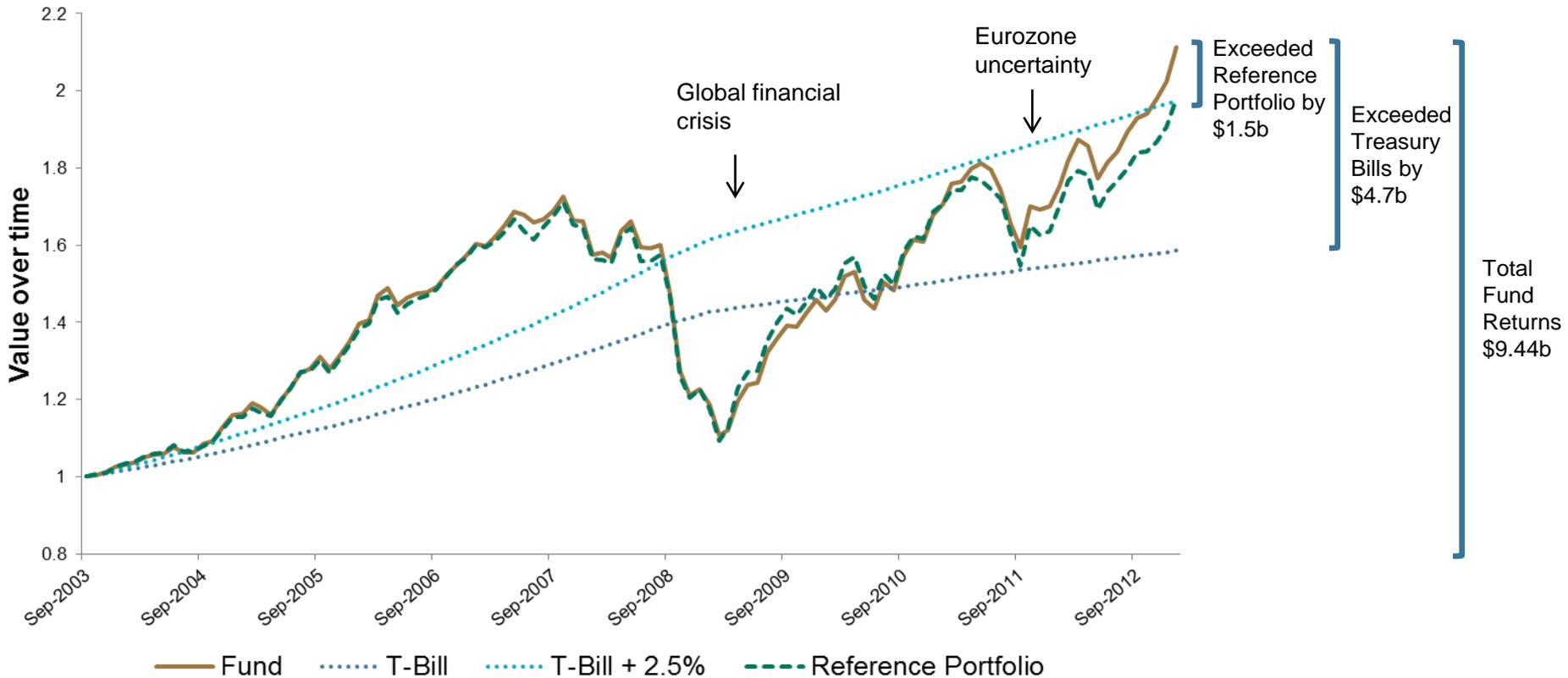
How we have performed

- Since inception, the Fund has:
 - exceeded the Treasury Bill rate by 3.28% or \$4.7 billion
 - exceeded the Reference Portfolio return by 0.74% or \$1.5 billion
- This is ahead of:
 - our expectation that we will exceed the T-Bill rate by at least 2.5% over the long term
 - our aim to exceed the Reference Portfolio by at least 0.5%

Performance as at 31 January 2013	Last 12 months	Last 3 years	Last 5 years	Since inception (Sept 2003)	Since inception (Sept 2003)
Actual Returns	20.37%	13.87%	6.04%	8.33%	\$9.44 billion
Reference Portfolio Return	16.24%	10.69%	4.84%	7.59%	Exceeded by \$1.5 billion
Treasury Bill rate	2.43%	2.60%	3.63%	5.06%	Exceeded by \$4.7 billion
Treasury Bill rate + 2.5%	4.93%	5.10%	6.13%	7.55%	Exceeded by \$1.0 billion

How we have performed

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



Fund size breakdown

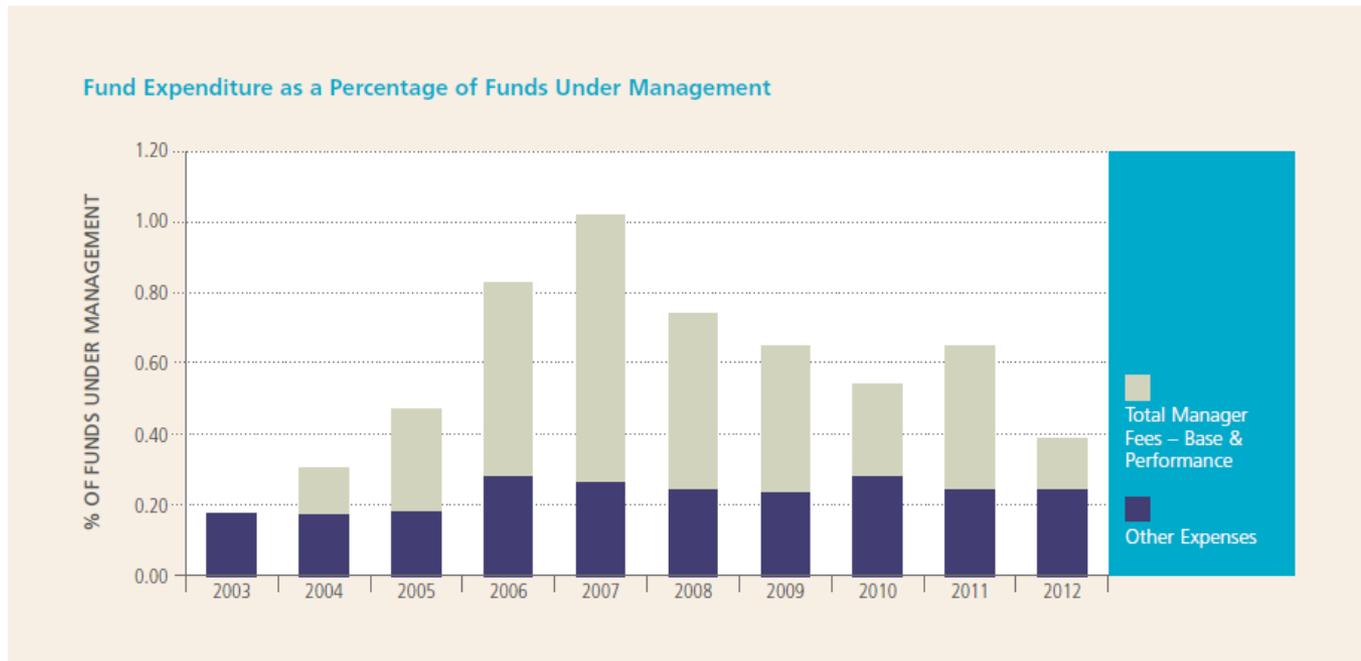
	Last 12 months	Last 3 years	Last 5 years	Since inception
Contributions received	\$0 billion	\$0 billion	\$3.5 billion	\$14.88 billion
Returns (after fees and foreign tax, and before NZ tax)	\$3.70 billion	\$7.30 billion	\$6.28 billion	\$9.44 billion
NZ tax (paid) / received*	\$(0.33) billion	\$(1.12) billion	\$(1.14) billion	\$(2.49) billion
Other movements**	\$0.00 billion	\$(0.02) billion	\$0.10 billion	\$(0.02) billion
Closing Fund balance as at 31 January 2012	\$21.81 billion			

* Tax 'received' covers any instances of refunds for overpayment of tax

** Other movements relate to transactions other than tax paid or received e.g. tax expense

How we have performed – cost control

Overall expenses down mainly due to a decrease in performance fees paid to external managers



As at 30 June 2012

Net of performance fees, expenses remained flat, at 0.45% of funds under management

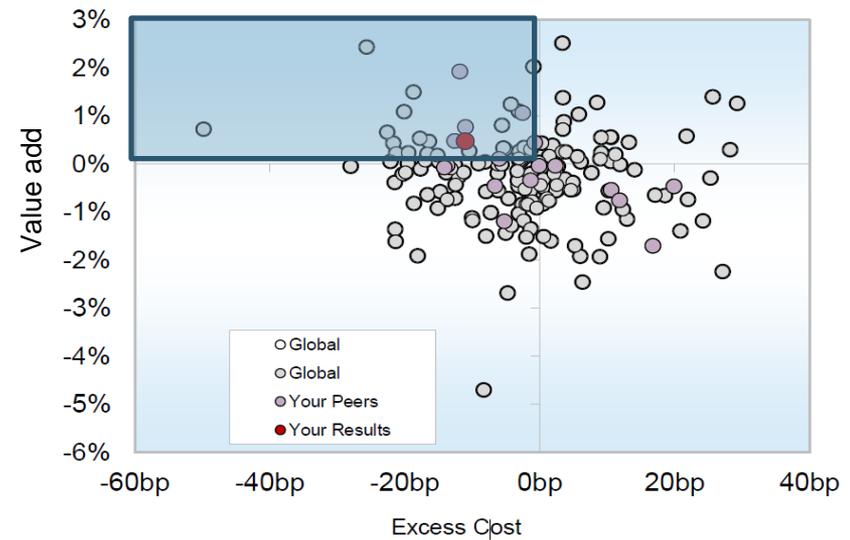
How we have performed – global cost and risk benchmarks

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

- 2012 CEM annual **cost-effectiveness** survey of more than 300 funds:
 - the NZ Superannuation Fund’s net five-year value-add of 0.5% was significantly above the median value-add of our peers
 - The NZ Superannuation Fund’s costs were well below median levels.
- 2012 CEM **risk management** survey of 27 funds considered “global leaders”:
 - found that risk management at the NZ Superannuation Fund was developing in line with best-practice standards at other funds overseas

Value added vs. excess cost

(Your 5-yr: net value added 0.5%, cost savings of 11.0bp*)



Our 5 year excess cost of -11.0bp is the average of our excess cost for the past 5 years

How we have performed

- Global Innovation
 - 2012 Asset International CIO Industry Innovation Awards – Most Innovative Sovereign Wealth Fund globally
 - (Related to our ‘single fund’, consistent ‘attractive/confidence’ value-add investing)
- Leadership
 - 2012 CIO Executive Team of the Year (NZ)
- Transparency
 - 10/10 in the Sovereign Wealth Institute’s Transparency Index, 2012
 - 1st equal for combined Transparency and Governance, and 4th equal for Transparency, out of 80 funds, by the Centre for Financial Stability, 2012
 - 2012 NZICA Public Sector Annual Report of the Year (NZ)
- 2012 INFINZ Excellence in Treasury (NZ)
- Responsible Investment (UNPRI)
 - Top quartile for all measures in most recent survey (2011)

How we have performed – NZ investments

- NZ investments currently valued at \$3.5 billion, compared to \$2.4 billion in June 2009
- An additional \$331m committed to NZ investments, but not drawn as at end Jan
- 24% of Fund investments compared to 21% in June 2009
- We are always looking to get the best return we can on our investment portfolio and to ensure that we have the right mix of investments
- We will look to sell as well as to buy NZ assets – we want the best
- All NZ investments must stack up relative to global alternatives
- We will continue to take our time and remain disciplined on price
- 2013 will see establishment of an in-house, active NZ equities team

* Figures quoted for NZ investments constitute the current value (rather than the exposures of underlying investments) and exclude cash and foreign exchange hedging instruments. Figures are as 31 January 2013.

Growth in NZ investments 2009-2012



Figures at 30 June 2012

Actively seeking and considering local investments; successfully transacting (buy and sell) as opportunities arise

■ Since last Select Committee (Nov 2010):

- Rural strategy
- Scales
- Datacom
- Kaingaroa – lifted stake
- \$90m committed to private equity funds
- AIA

Summary

- Key points:
 - Fund is exceeding its performance benchmarks and globally
 - We will continue to take our time and remain disciplined on price
- Future priorities and challenges:
 - Embedding of Target Operating Model
 - Balance between external managers and in house resource
 - Desire to invest as ‘directly’ and ‘flexibly’ as possible
 - Culture development; staff retention and motivation
 - On-going focus on responsible investment, particularly around integrating with investment analysis and identifying opportunities aligned with our investment themes