



Briefing from the Guardians of NZ Superannuation to the Incoming Minister of Finance

November 2023

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THE GUARDIANS OF NEW ZEALAND SUPERANNUATION AND THE NEW ZEALAND SUPERANNUATION FUND

Established by the New Zealand Superannuation and Retirement Income Act 2001 (the Act) Began Investing September 2003	Net Contributions from the Crown at 30 September 2023: \$15.7 billion (unaudited)	Current Fund Size at 30 September 2023: \$64.4 billion (unaudited)
Fund Returns since Inception	Total return: 9.5% p.a.	
Value to the NZ Taxpayer (Total Fund Return minus Cost of Crown Contributions): \$40 billion		
Growth- oriented portfolio: 80% Growth Assets		
NZ Investment		
Amount Invested in New Zealand: \$7.8 billion (12% of portfolio)		
Major NZ Assets: \$2.4 billion in NZ listed equities; 40% of Kaingaroa Forest (c\$2billion); 45% of Datacom; NZ Farm portfolio (dairy, beef, horticulture); 50% of Awanui (formerly Labtests); NZ Property investments (hotel portfolio, land development)		
Governance		
Guardians Board: Nominated via separate Nominations Committee (Nick Wells, Chair)		
Catherine Drayton (Chair)	John Williamson	Doug Pearce
Henk Berkman	David McClatchy	Fiona Oliver
External review required every five years – next one due in 2024		
CEO: Matt Whineray, finishing December 2023; Appointment process for new CEO underway		
213 staff in a single Auckland office		
Additional Mandate – Elevate Fund - \$300 million		
Increasing capital to Series A & B rounds in NZ; Develop domestic venture capital market		
Guardians' role: Oversee and administer the management of the fund by NZ Growth Capital Partners		

Material Issues for the Minister's Attention

1. Section 59 amendment	<p>A bill to repeal s59 of the Act, which prevents the NZ Super Fund from controlling any other entity, is currently awaiting its second reading.</p> <p>This change will provide the Guardians with additional investment flexibility and is consistent with global best practice.</p>
2. Board Appointments	<p>The Guardians is looking to appoint new Board members. Board fees were last reviewed in 2015 and the low level of fees is a real issue in recruiting new Board members.</p>
3. Taxation	<p>The NZ Super Fund currently pays tax. This is unusual for a sovereign wealth fund and generates deadweight costs and other economic inefficiencies. Paying tax does not increase Crown revenue, as the NZ Super Fund's assets are part of the Crown's balance sheet. Granting the NZ Super Fund tax-exempt status was recommended by the 2019 Tax Working Group.</p>
4. Elevate Funding	<p>The Elevate Fund has nearly completed the allocation of the initial fund of \$300 million to domestic venture capital managers. Significant private capital has been crowded into the market as a result of the first fund. Additional funding is required to continue to develop the domestic venture capital market and to build on the achievements of the first Fund.</p>

1. Overview

Background

The Guardians of New Zealand Superannuation (“Guardians”) is an autonomous Crown entity responsible for managing the \$64 billion New Zealand Superannuation Fund (“NZ Super Fund”) and the \$300 million Elevate NZ Venture Fund (“Elevate”). In June 2022, international sovereign wealth fund experts GlobalSWF named the NZ Super Fund the best financial performer of 50 leading sovereign wealth funds over the preceding decade, with an annualised return of 12.1 percent between FY13 and FY22.

Purpose and Vision

The Guardians’ purpose is:

Sustainable investment delivering strong returns for all New Zealanders

Kia toitū te haumi hei hua mā ngā tāngata katoa o Aotearoa

The Guardians’ vision is:

An inclusive team creating a better future through investment excellence

Mā te Kotahi ā-kapa, mā te kounga ā-haumi, ka tino eke ki tua

Statutory Context

The Guardians was established by the [New Zealand Superannuation and Retirement Income Act 2001](#) (the Act), initially with the sole function of managing the NZ Super Fund (which was also established by the Act). As an autonomous Crown entity, the Guardians is part of the public sector but legally separate from the Crown, operating at ‘double arm’s length’ from the Government. This means that, while the Guardians remains accountable to the Government, it is governed by an independent board and has operational independence regarding investment decisions.

The NZ Super Fund, a global investment fund designed to partially pre-fund the future cost of New Zealand Superannuation, began investing in 2003. Under section 58 of the Act it is the Guardians’ job to invest the NZ Super Fund on a prudent and commercial basis, in a manner consistent with:

- best practice portfolio management
- maximising return without undue risk to the Fund as a whole
- avoiding prejudice to New Zealand’s reputation as a responsible member of the world community

These three considerations are interlinked; together, they sit at the heart of our investment philosophy and practices, and are reflected in our purpose and vision.

In 2019 the Guardians was given a second mandate when the Government passed the [Venture Capital Fund Act 2019](#), which established Elevate. The Guardians governs and has overall responsibility for Elevate. Under the 2019 Act, the Guardians is required to invest Elevate in New Zealand’s venture capital markets using best-practice investment

management that is appropriate for institutional investment in those markets. The Guardians must also manage Elevate in a manner consistent with:

- a policy statement released by the Government on 19 December 2019 and updated on 4 July 2023
- avoiding prejudice to New Zealand’s reputation as a responsible member of the world community.

Under its governing legislation, Elevate doesn’t have a fixed lifetime but can be wound down once New Zealand venture capital markets are sufficiently developed and no longer require Government support. When Elevate is ultimately wound down, the funds will be returned to the Crown.

The Act specifies the Minister of Finance as the responsible Minister for Elevate; however, it also explicitly provides for these responsibilities to be delegated to another Minister.

Purpose of the Mandates

NZ Super Fund

Currently, NZ Superannuation is funded by general taxation. However, the proportion of New Zealanders receiving NZ Superannuation is expected to rise as the average age of the population increases; the NZ Super Fund is designed to meet much of the incremental cost generated by this demographic shift.

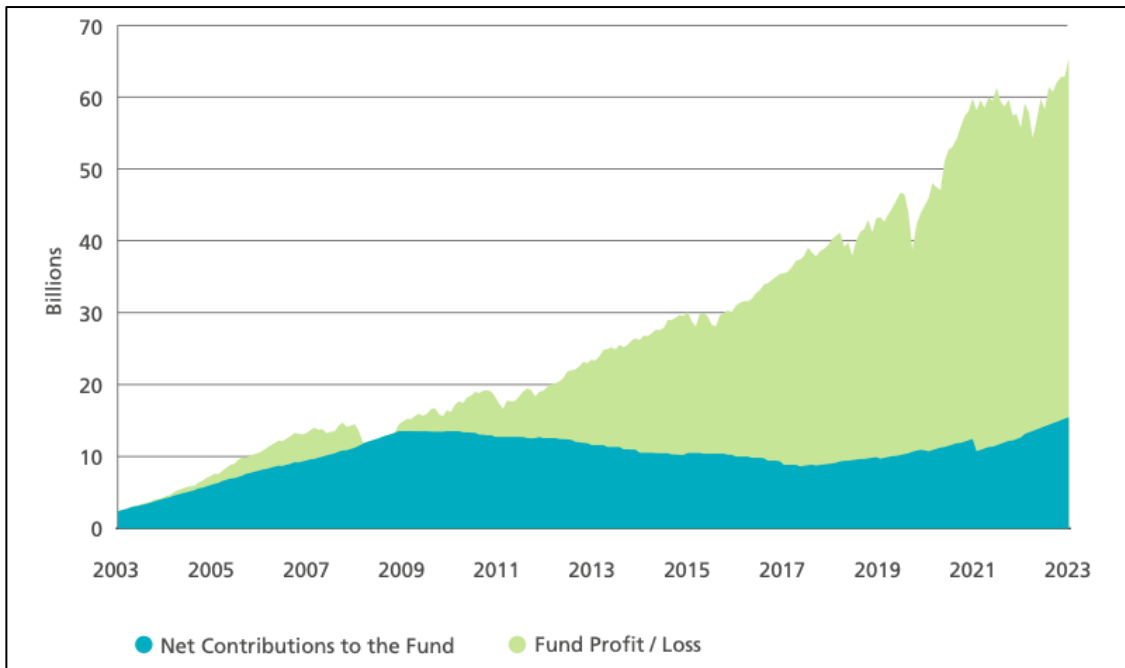
By using the NZ Super Fund to save now in order to help pre-fund the future cost of NZ superannuation, the Government aims to smooth the cost of NZ Superannuation between today’s taxpayers and future generations. This will in part offset the fiscal impact of New Zealand’s ageing population – which will see the proportion of New Zealanders who are over 65 increasing, and the proportion of taxpayers decreasing.

Sections 42 and 43 of the Act set out the process and the formula for calculating the amount of capital the Government is required to commit to the Super Fund. Section 44 sets out what the Government must do if it intends to pay less into the Super Fund than the required annual capital contribution; this includes providing a reason for the difference and setting out its intentions regarding future contributions.

The Guardians invests the capital contributions made by the Crown (net \$15.7 billion at 30 September 2023) as well as the returns generated by these investments. At the end of September 2023, the NZ Super Fund had a value of \$64.4 billion (unaudited).

Under current projections, contributions to the NZ Super Fund are expected to continue until the mid-2030s, at which time the Government will start drawing from the Fund to help fund superannuation payments. By the mid-2070s, when the NZ Super Fund is expected to be at its peak (as a percentage of GDP), withdrawals and tax payments combined will cover approximately 20% of the total annual net cost of superannuation payments. The NZ Super Fund, therefore, adds to Crown wealth, improves the ability of future Governments to pay for superannuation and ultimately reduces the tax burden of the cost of superannuation on future generations.

The graph below shows net government contributions to the NZ Super Fund (contributions less tax paid back to the government) since inception, and the investment returns the Fund has achieved on those contributions.



Elevate

Elevate is a Government initiative aimed at improving national productivity by developing more innovative knowledge-intensive industries in New Zealand by attracting private sector investors into the domestic venture capital market. Elevate is a fund of funds programme managed on behalf of the Guardians by New Zealand Growth Capital Partners (NZGCP), a Crown entity.

Elevate is designed to support investments into New Zealand companies which have moved beyond their start-up stage and require additional capital for further development. The overall aim of the Elevate programme and related initiatives is to develop the early-stage capital ecosystem in New Zealand, encourage new venture capital managers and support innovation, thereby contributing to the sustainability and productivity of the New Zealand economy.

Mandate Parameters

The Superannuation and Retirement Income Act 2001 explicitly states that there are no restrictions on the Guardians' responsibility to invest the NZ Super Fund other than:

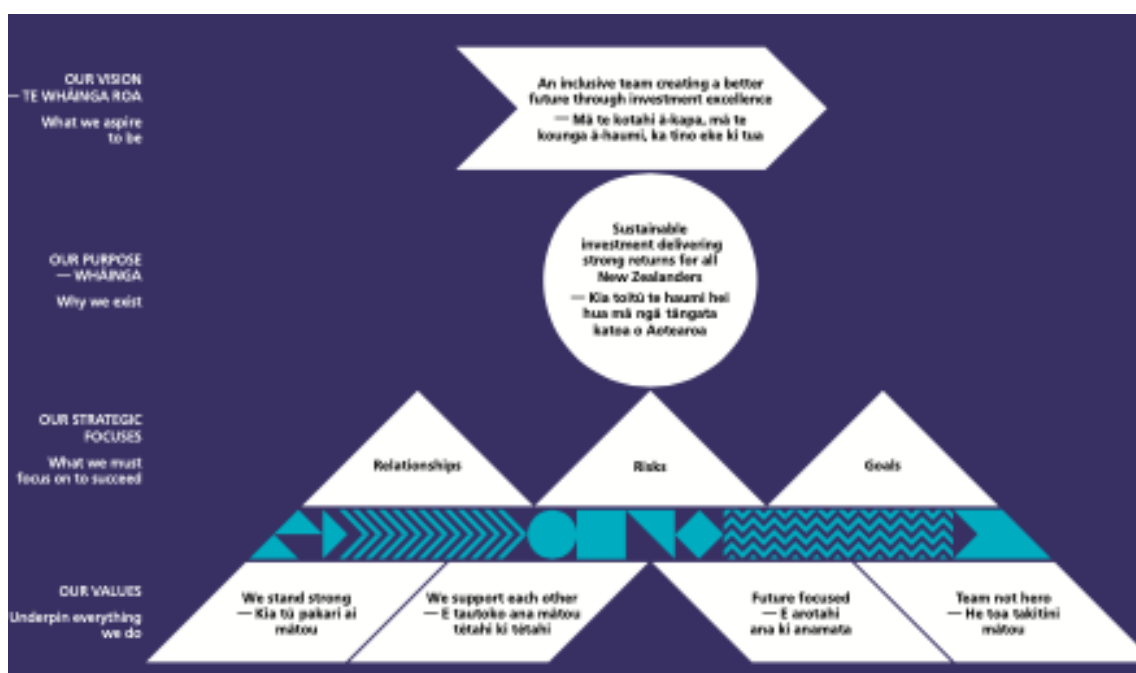
- Section 58, which sets out the investment mandate
- Section 59, which restricts the Fund from controlling another entity. A bill to repeal section 59 was introduced to Parliament on 23 February 2023. The bill has been reported back from select committee and was awaiting its second reading when Parliament was dissolved. More detail on this is provided on page 22
- Section 64, which sets out the Minister's power to issue non-binding directions as summarised above

There are also certain restrictions on the Guardians' ability to borrow in respect of the NZ Super Fund. Section 50 states the Guardians may not, except with approval of the Minister, borrow or incur contingent liabilities or mortgage or charge property of the Fund as security. The Minister has approved various types of transactions (including the use of derivatives) which would otherwise have been caught by this restriction.

Strategic Framework

The Guardians' purpose and vision, alongside the Risk Appetite (see page 11), set the scene for the strategic framework. This is shaped by three strategic focuses: Relationships, Risks, and Goals.

The strategic framework (as illustrated below) provides a guide to where the Guardians focuses its resources and thinking in the medium term. Underpinning the framework, and everything the Guardians does, are our values – which are at the heart of how the Guardians operates as a team and as an investor.



Priorities for 2023/24

Out of the above strategic framework come the Guardians' programmes of work. These activities represent large-scale and often multi-year projects.

The 2023/24 these programmes of work are:

- **Modern Workplace** - deliver improved collaboration and communication tools, including shifting to a new and improved document management system and intranet.
- **Design the Guardians of the Future** – clearly articulate how we will continue to pursue our Purpose and Vision while developing a platform to manage expected future growth. Treasury forecasts that the value of the Fund's assets will double over the coming decade.
- **Diversity, Equity, and Inclusion (DE&I); and Te Ao Māori** – implement our DE&I strategy and improve and integrate our understanding of Te Ao Māori. Current priorities include attracting and appointing more women into leadership roles, recruiting more Māori and Pacific people, and reducing our gender pay gap.
- **Investment Data and Analytics** – establish a new data platform and build data analytics, governance, and quality capabilities.
- **Human Capital Management (HCM) System** – implement Oracle HCM integrated cloud solution.

2. Governance

External

Role of Minister

The Guardians is accountable to the Government through the Minister of Finance. The Minister is responsible for overseeing and managing the Crown's interest in, and relationship with, the Guardians, and is answerable to Parliament for our performance.

The Minister also has the power to give directions to the Guardians in relation to the Fund, but only regarding the Government's expectations as to the Fund's performance, including risk and return.

The Minister cannot give a direction that is inconsistent with the Guardians' duty to invest the Fund on a prudent, commercial basis, and cannot direct the Guardians in regard to any other matter in respect of the Fund.

While the Guardians is required to 'have regard to' a Ministerial Direction, Directions are non-binding. The Guardians is required to explain how it is having regard to the Direction in its annual report.

The Minister's power of direction has been exercised once during the existence of the Guardians. In May 2009, the then-Minister of Finance, Rt Hon Sir Bill English, provided a direction setting out the Government's expectation 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"

In response, the Guardians undertook a review of domestic opportunities and identified potential to invest further into New Zealand outside of traditional listed markets. The direction was a catalyst for the establishment of the Guardians' Direct Investment team. Details of the Fund's New Zealand investments are provided on pages 12 to 15.

In short, the Guardians follows its statutory mandate, which gives it very broad investment powers, and is not required to give effect to Government policy.

Engagement with successive Ministers of Finance has typically included:

- an [annual Letter of Expectations](#) from the Minister. This is a formal but non-legislative tool which provides an opportunity for the Minister to set out the Government's expectations of the Guardians over the coming year, and to feed into the Guardians' Statement of Intent and annual Statement of Performance Expectations
- occasional enduring letters of expectations from the Minister of Finance and other Ministers. [The most recent of these](#), which set out the Government's expectations relating to responsible investment and in particular to the application of the Crown Responsible Investment Framework, was sent to all Crown Financial Institutions by the Minister of Finance and the Minister for ACC in October 2021
- a 'no surprises' protocol under which the Minister is informed as early as possible of matters that may be contentious or attract wide public interest
- an opportunity for the Minister to input into statutory reporting documents (Statement of Intent, Statement of Performance Expectations, and annual reports)

- quarterly reporting to the Minister
- periodic Board Chair and Minister calls and meetings.

Role of Treasury

Treasury is the monitoring department of the Guardians. It administers the relevant legislation and supports the Minister in exercising their responsibilities in relation to the Guardians by providing the Minister with information, analysis and advice relating to the Guardians' effectiveness and efficiency. The department has issued an 'Owner's Expectations Manual', which sets out expectations for the entities it monitors. The Chair keeps Treasury informed on appropriate aspects of the Board's governance role – including Board evaluations and progress on resulting action plans. Treasury meets at least annually with the Guardians' Board and with management at least monthly.

Five-Year Independent Review

The Act provides for a five-yearly review of the Guardians' performance against specified criteria, undertaken by an external reviewer appointed by Treasury. The next review will take place in 2024.

These reviews are published on our website, along with our response – which includes details of the actions we have taken to address any recommendations and suggestions contained in the review.

The last review was undertaken in 2019 by Willis Towers Watson. That review concluded the Guardians was operating at global best practice level, awarding ratings of "AAA" (exceptional) and "AA" (excellent) for its people and investment model respectively.

The Willis Towers Watson review found that the Guardians' "current approach to ESG integration and stewardship is impressive and, in our view, aligns with best practice in these activities". It noted, however, that "responsible investment is a developing area with positive momentum and so there is a need for the Guardians to continue to evolve and innovate to maintain their position as a leader in this area". This was a catalyst for the Guardians' shift to a sustainable finance approach (see pages 15-18).

Internal

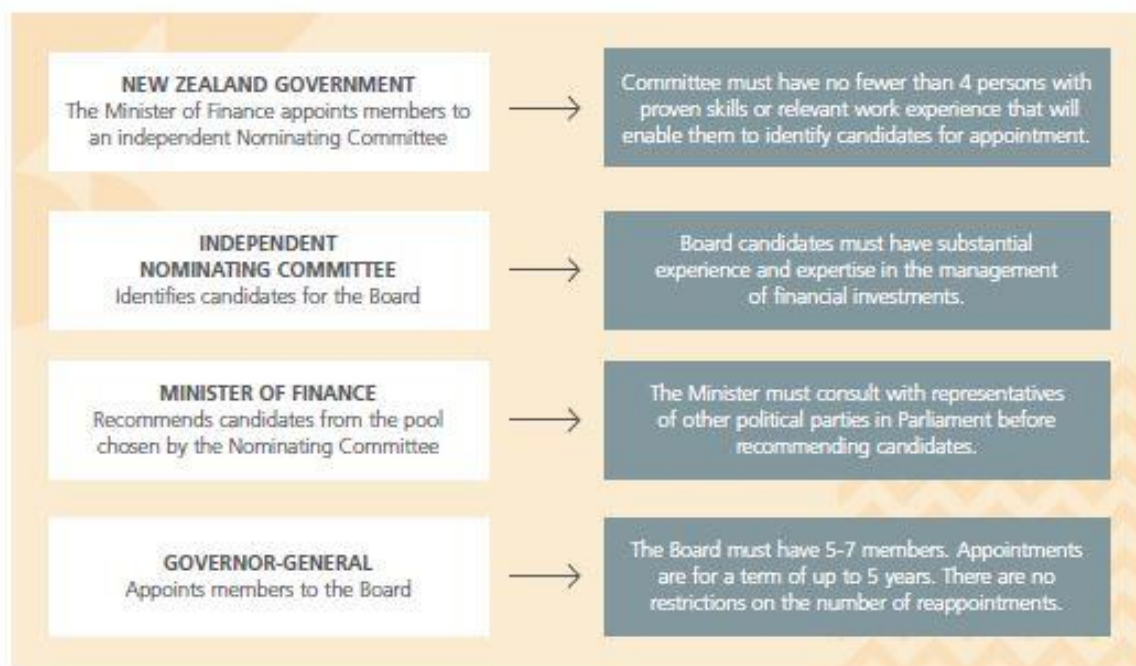
Role of the Board

The Board Charter is the principal foundation of governance at the Guardians, setting out the structure of the Board, its role and responsibilities, terms of reference and expected standards of contents. The responsibilities of the Board include:

- setting strategic direction and monitoring organisational and Fund performance
- setting and reviewing policies within which management is to operate
- oversight of risk management and effective use of Guardians resources
- promoting a culture which is aligned with the Guardians' purpose, mission, values and strategy
- setting the tone for ethical behaviour
- appointing reviewing and setting remuneration for the Chief Executive and approving the staff remuneration structure
- approving the enterprise risk appetite and risk assessment framework
- approving investment policies, beliefs, and benchmarks
- setting the risk and return profile, risk budget and investment constraints

- terminating NZGCP as manager of Elevate

The process by which Guardians Board members are appointed, which is set out below, is unique to the Guardians.



By Statute, the Board is required to consist of at least five, but no more than seven, members. It is a further statutory requirement that Board members must have substantial experience, training and expertise in the management of financial investments. Board members are generally appointed for a term of between three and five years, and may be reappointed at the expiry of their term.

The Board operates two standing committees – the Audit Committee and the Employee Policy and Remuneration Committee. The performance of the Board, its committees and its members is evaluated at regular intervals – generally annually for the Board and at least once every two years for its committees. During the previous financial year, Kerridge and Partners was engaged to undertake a full evaluation, which concluded:

“the Board of the Guardians is a well-performing board. Board members are highly engaged and motivated and have skills and experiences that are relevant to the challenges of governing the Fund.”

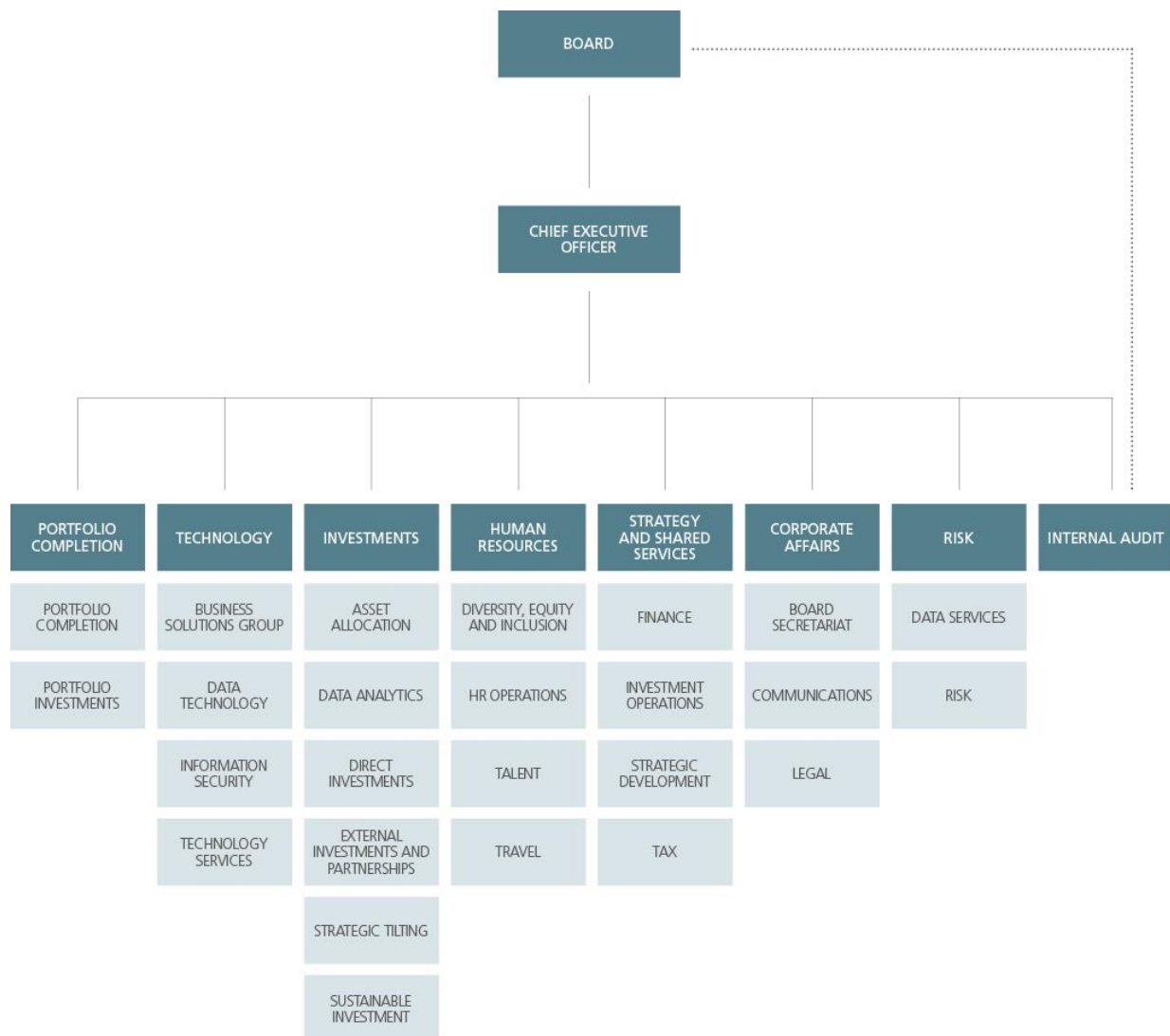
Board Members

- Catherine Drayton (Chair)
- David McClatchy
- Doug Pearce
Chair, Audit Committee
- Henk Berkman
- Fiona Oliver
- John Williamson
Chair, Employee Policy & Remuneration Committee

Role of Management

While the Board has overall responsibility for the affairs and activities of the Guardians, it has delegated authority for the day-to-day management of the Guardians to the Chief Executive and other officers, exercised within Board-approved parameters.

In general terms, the associated division of responsibilities means the Board's focus is on the governance framework, strategic direction, organisational identity, and oversight of management. Management is responsible for implementing strategy.



The Guardians does not depend on Government funding for its operating expenses. Other than a small appropriation for Board expenses and the Guardians' audit fees, organisational costs are covered by the Fund itself – another key foundation of the Guardians' operational independence.

3. Investing

Endowments (our Competitive Advantages)

As investors the Guardians considers itself to have four endowments, or competitive advantages: core features of the NZ Super Fund, derived from how it was established, that help guide investment decisions.

The four endowments are:

- **Long term horizon** – we have the ability to invest in illiquid assets and to ride out short term market movements.
- **Operational independence** – investments are made on a purely commercial basis. Independence enables the Guardians to have a stable risk appetite compared with some peer funds.
- **Sovereign status** – this is regarded favourably by other parties and investment partners and positions the NZ Super Fund as a potential co-investor of choice in New Zealand - this is one of the reasons the Fund is proportionately over-weight in terms of New Zealand assets. It also enables us to pay lower rates of tax in some jurisdictions.
- **Governance** – the Guardians is acknowledged as having developed a strong governance model, including clear delegation structures and board oversight. This is crucial in managing risk and in forming investment partnerships.

Investment Beliefs

These endowments are complemented and underpinned by our investment beliefs, which are a key driver of, and reference point for, investment decision making. The investment beliefs, outlined below, provide a clear statement of how we understand investment markets to work.

Decisions	Beliefs
Governance and investment objectives	Clear governance and decision-making structures that promote efficiency and accountability are effective and add value to the Fund.
Asset allocation	Asset allocation is the key investment decision. Investors with a long-term horizon can outperform more short-term focused investors over the long run.
Asset class strategy and portfolio structure	Asset class expected returns are partly predictable; prices tend to revert to fair value over time.
Manager and investment selection	The ability to consistently generate excess returns from skill vs an appropriate benchmark (net of fees) is rare; where this ability exists, it is hard to access. Some markets or strategies have characteristics that are conducive to a manager's ability to generate active return. These characteristics may change over time. Environmental, social and governance considerations, including climate change, are fundamental to long-term risk and return.

Total Portfolio Approach

The Guardians uses a Total Portfolio (TP) approach to invest the Fund. The Guardians has utilised this approach since 2010, before which a Strategic Asset Allocation (SAA) approach was used.

The SAA approach entails an investor setting target allocations for various asset classes, based on risk and expected return within each category. The TP approach used by the NZ Super Fund manages on a total portfolio basis as opposed to by asset class. This approach is intended to drive a collaborative cross-team approach, ensuring constant competition for capital and more nimble risk allocation.

The NZ Super Fund was one of the early adopters of the TP model and remains one of the few sovereign wealth funds (SWF) to apply it. Recent research by Global SWF (May 2023) – which ranked the Fund as the best performing SWF over the last 10 years – found that three of the top five ranked SWFs used a TP model.

Reference Portfolio

The Reference Portfolio is a shadow or notional portfolio of passive, low-cost, liquid investments suited to a long-term investment horizon and capable of meeting the Fund's objectives over time. It is a way for the Guardians to:

- estimate the Fund's expected returns
- benchmark active (value add) investment returns net of all costs
- be clear on the 'hurdles' for active investments

Currently, the Reference Portfolio is made up of 75% global equities, 5% NZX-listed stocks, and 20% fixed income assets, fully hedged to the New Zealand dollar. The 80:20 asset allocation is considered an appropriate balance between maximising return and avoiding undue risk.

The Reference Portfolio is reviewed every five years, most recently in 2020.

The composition of the Reference Portfolio is the single biggest influence on Fund returns, because it determines the overall level of market risk we take. In practice, passive exposures, in line with the reference portfolio, comprise half of the Fund's Actual Portfolio by value, with active investment strategies making up the balance.

Active Investing

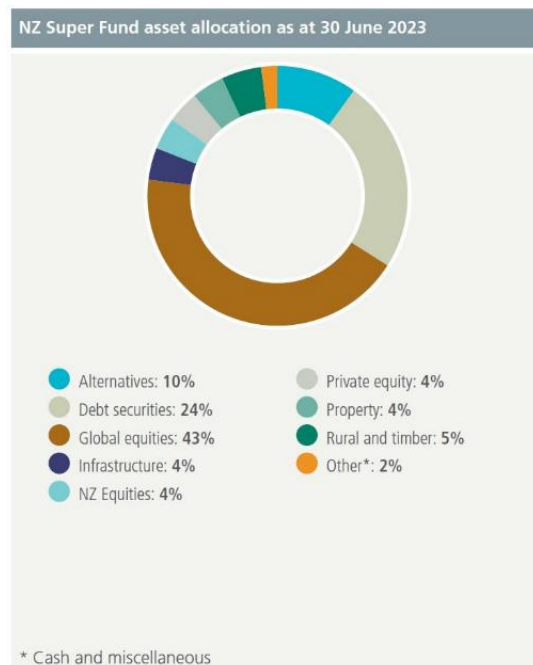
We undertake active investments to add more value after all costs to the Fund than the Reference Portfolio approach would do, using strategies based on our natural advantages as a long-term, sovereign investor with low liquidity requirements.

An active investment is only undertaken when there is a high level of confidence that, over time, it will provide greater outcomes and better value than investing passively - either by improving returns, reducing risk, or both.

Active investment strategies will not always out-perform passive results. For instance, in the 2022/23 year, actual Fund returns were 11.87% compared to Reference Portfolio returns of 12.03%.

Over the life of the NZ Super Fund, however, active investment has outperformed the reference benchmark by 1.54%, representing \$15 billion in added value. This is ahead of our long-term expectation that our active investment strategies will add 1.0% p.a. to the Fund, over and above the Reference Portfolio return.

The structure of the Fund's Actual Portfolio, by asset class, is set out in the following chart.



Externally Managed Investments

The Guardians appoints external investment managers, and invests in externally-managed collective investment vehicles, to efficiently and effectively achieve desired investment exposures. Such appointments complement our in-house expertise. External management can generate new investment opportunities and provide us with valuable information on a range of investment and operational topics.

Performance and reputational risk associated with external management is managed through annual conviction assessments, operational due diligence, and compliance monitoring. The Guardians currently works with some 50 investment and asset managers globally.

Use of Derivatives

Our default position for the Reference Portfolio is to access market exposures by funding our global passive managers. In implementing our Actual Portfolio, however, we may use derivatives when it is efficient to do so. Derivatives provide a convenient and cost-effective way to re-balance the portfolio back to its targeted risk level and to manage foreign currency risk and liquidity risk.

Our use of derivatives also reflects the Minister of Finance's 2019 letter of expectations, in which he said that where derivative instruments are employed, he expects their use to be

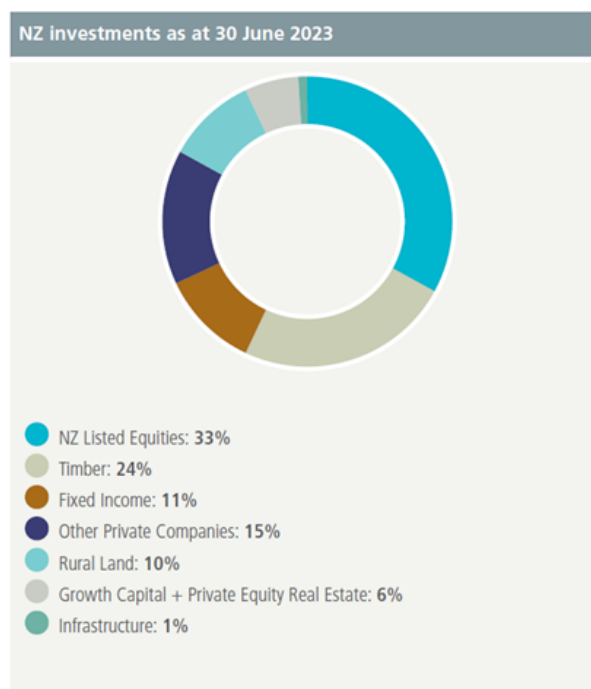
aligned to the Fund's business and expects the Guardians to be mindful of our fiduciary responsibilities and statutory duties.

NZ Investment

New Zealand is the Guardians' home, a market we understand well and one in which we, therefore, have some advantages over other investors. We are local and Crown-owned; we are relatively large in New Zealand terms; and we have a long investment horizon, which allows us to invest in illiquid assets (assets that can be hard to sell quickly) in order to earn a premium over time.

Our local advantage means that we are strongly weighted to New Zealand-based assets relative to the size of the local market. For example, some 8.5 percent of our equity investments are in NZX-listed companies; the NZX's total market value is only 0.1 percent of the total capitalisation of sharemarkets included in World Federation of Exchanges statistics.

Over time, we have grown to become one of New Zealand's largest institutional investors. Our \$7.5 billion New Zealand investment portfolio (which makes up 12% of total investments) includes more than \$2 billion in the local sharemarket, along with large investments in Kaingaroa Timberlands, Fidelity Life, NZ Gourmet, Hobsonville Development, Datacom, a portfolio of hotels and rural farmland. We are also invested, through external investment managers, in small, privately-owned companies, property developments and social infrastructure.



While the value of our investments in New Zealand has grown significantly since the 2009 Ministerial directive (by some \$2.5 billion to \$7.5 billion), the value of our New Zealand assets as a proportion of our total portfolio has decreased 10 percent during the same period. This is a function of the size of the New Zealand market and its rate of growth relative to other global markets in which we are invested. It also reflects the scale of available opportunities in New Zealand that satisfy our minimum deal size requirement, an ever-increasing constraint given our growth. We continue to actively pursue large-scale domestic investment opportunities and continue to seek out local projects that fit our commercial criteria.

Infrastructure Investment

Infrastructure is a strategic and attractive investment category for the NZ Super Fund and the Guardians is increasing its exposure to infrastructure, both domestically and internationally.

Infrastructure investment also fits with the NZ Super Fund's requirements in relation to scale. For organisational, operational and risk management reasons, funds such as ours set minimum deal sizes for direct transactions and mandates with external managers, relative to the size of the overall portfolio. The Guardians' minimum currently sits at \$200 million, but this will rise as the size of the NZ Super Fund increases. This will impact on the range of investment opportunities available to us – our investment universe.

Within New Zealand, the Guardians' interest is in pursuing large-scale domestic infrastructure investment opportunities that meet our commercial criteria, are in line with our sustainable investment approach, and allow us to bring together innovation, capital, and expert global partners to help solve New Zealand's infrastructure deficit.

The Guardians infrastructure investment model is based on long-term equity investment in large-scale infrastructure by publicly owned but commercially-run investors, in partnership with relevant jurisdictional governments, delivering both financing and funding solutions. While it shares some attributes with the 'Alliance' model increasingly used to deliver infrastructure in New Zealand, it is fundamentally different to traditional Public-Private Partnership delivery model.

SuperBuild Model

Over the past few years, with a view to making large-scale domestic investments and increasing the proportion of the NZ Super Fund that is invested in New Zealand, the Guardians has developed the SuperBuild partnership model. The model has a particular focus on investment in domestic infrastructure and real estate at scale.

The SuperBuild investment model is an equity-funded end-to-end delivery solution (i.e. planning, financing, building and operating), which provides increased financial flexibility, faster delivery and greater risk tolerance.

Under the model, once an infrastructure or urban development need is identified (whether by the Government, councils, business or other interest groups), the NZ Super Fund and its investment partner(s) jointly agree the financial and social outcomes with key stakeholders. The NZ Super Fund and partners then manage the project from end to end, with collaboration from relevant government agencies.

SuperBuild works best for projects which require long-term vision, scale, and innovation, and where partnerships with world-leading peers can add value. As with all investment decisions, SuperBuild opportunities will only be considered where they are consistent with our mandate. Examples of the SuperBuild model include:

- a partnership with Copenhagen Infrastructure Partners to explore the feasibility of offshore wind energy in South Taranaki (see case study below)
- a framework agreement with Eke Panuku Development Auckland to accelerate and scale up town centre regeneration projects
- the Beachlands South investment, with local and iwi partners, in large-scale urban development in Auckland

Investment Case Study: Taranaki Off-shore Partnership

The Guardians' partnership in a joint venture with Copenhagen Infrastructure Partners (CIP) is a useful example of our focus on domestic infrastructure and our commitment to sustainable investment. We are currently exploring the technical and commercial feasibility of a large offshore wind farm in the South Taranaki Bight. The initial proposed development of up to 1GW would equate to over 11% of New Zealand's current electricity demand capacity and could power more than 650,000 homes.

The project would see approximately 70 wind turbines installed between 23 and 30km offshore at an estimated cost of \$5 billion. The partnership believes the project could potentially later expand to 2GW, further helping to meet strong projected growth in demand for electricity in New Zealand.

Work on the project commenced in 2021 and is currently in the feasibility stage. During feasibility work, the joint venture is focusing heavily on environmental and social issues and on establishing relationships with communities and interest groups within Taranaki, with a particular focus on iwi as mana whenua and mana moana.

Creating a viable development will also require considerable work with regulators, energy users and local communities to develop a regulatory framework which supports the level of investment and development required to secure security of supply and demand. This work is at any early stage; however, the joint venture recently submitted to MBIE on Developing a Regulatory Framework for Offshore Renewable Energy.

We have also commenced preliminary work, including initial meetings with stakeholders, to explore offshore wind feasibility off the Waikato coast.

Where We Invest

While the NZ Super Fund is heavily weighted to equities, it is diversified across a range of markets and sectors globally. This diversification is in keeping with the need to invest the Fund in a manner consistent with best-practice portfolio management.

The following table sets out the geographic exposure of the NZ Super Fund's portfolio. Figures relating to the Reference Portfolio have also been included to provide an indication of the impact of the Guardians' active investment strategies.

	Reference Portfolio	Actual Portfolio
North America	59%	53%
Europe	18%	17%
Asia (excl. Japan)	10%	4%
Japan	6%	5%
New Zealand	5%	12%
Australia	1%	5%
Other	1%	4%

4. Risk Management

Taking risk is central to the work of the Guardians. The Guardians is willing to take investment risk to achieve our purpose and fulfil our mandate. Complex enterprise risks are also identified and, where possible, mitigated.

Understanding and managing risk is crucial to ensure the risk taken is appropriate for the return anticipated. Investment risk is managed by the adoption of the Reference Portfolio (as detailed above) along with approved Investment Constraints, while Enterprise Risk is managed by the Risk Assessment Framework.

The Board is responsible for setting the risk appetite, providing risk governance and oversight, and reviewing and approving the risk management framework. The Board has developed a process for delegating authority to the CEO and other officers for the day-to-day management of risk.

The Guardians believes culture, governance, people, and processes are critical to managing risk.

The Guardians has risk policies, procedures and internal controls for staff, external investment managers, and other specialist service providers.

The overall approach to managing investment risk is set out in the Statement of Investment Policies, Standards and Procedures (SIPSP) and the Investment Risk Allocation Policy.

All Policies (being Investment Policies and Enterprise Policies) are reviewed by the Board at least every five years.

A Risk Appetite Framework plays a central role in the management of risk, making it clear that accountability for risk identification and mitigation rests across all parts of the Guardians' team. Within this, the Risk Appetite Statement outlines the approach to risk the Guardians will take to achieve our strategic goals.

Alongside this, the Risk Assessment Framework helps to determine our risk appetite and how risks are responded to. This framework:

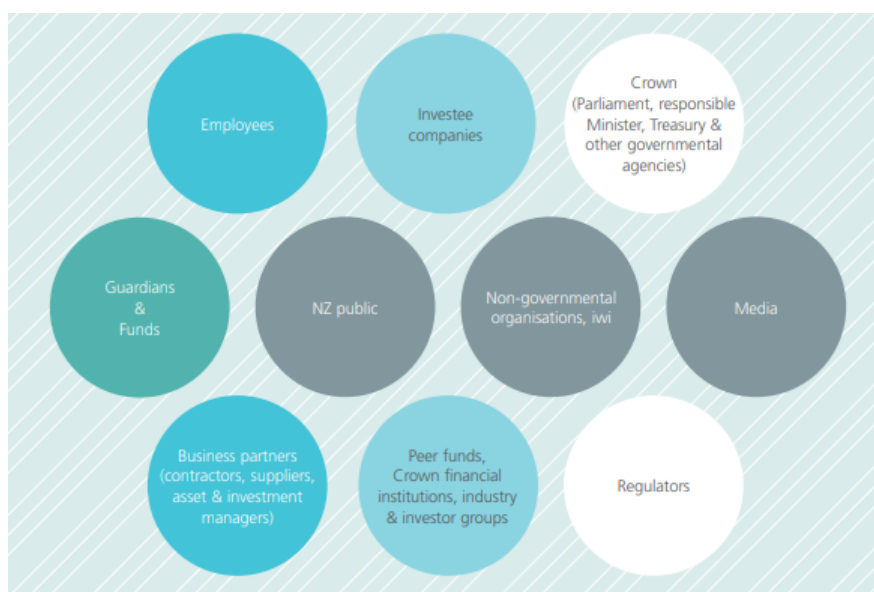
- ensures risk categories are defined
- sets out the questions which need to be asked
- defines the Guardians' core expectations
- ensures there is appropriate monitoring and reporting of risk appetite assessments

The two major investment risks for any long-term investor are loss of stakeholder support and liquidity management (being able to pay obligations as they come due).

Loss of Stakeholder Support

The key mitigant to the first of these risks is transparency. The Guardians works to ensure that stakeholders understand why and how the portfolio has been selected and understand the expected performance of the NZ Super Fund portfolio through time, including periods of negative returns.

Our stakeholders include:



Liquidity Risk

Central to liquidity risk management is ensuring there is sufficient short-term liquidity (i.e. cash and liquid securities) to cope with the expected range of short-term market movements, given the growth orientation of our portfolio and our foreign currency hedging programme. A liquidity risk appetite is established with the Board and monitored closely.

Active Investment Risks

In making active investments the Guardians takes “active risk” – the chance that the Actual Portfolio will perform better or worse than, or show more volatility than, the Reference Portfolio. It is important that active risk is prudently and commercially managed - both in total and in how it is allocated to specific investment opportunities. The total budget for active risk (i.e. the expected standard deviation of active returns) is 4%. This is an average over time as opposed to a cap; the limit for Actual Portfolio active risk is 8%.

Other Investment Risks

Other investment risks include:

- market risk - the risk that the value of an asset will fluctuate over time due to factors which effect the broader market rather than the individual asset – primarily equity price, foreign currency, and interest rate risks. Market risk is managed through diversification, investment constraints and a target hedge ratio
- credit risk – the risk a third party will default on its obligations, creating a loss for the Guardians. Exposure specifically arises from cash and cash equivalents, receivables and investments. This is mitigated through the application of specific prudential limits to any unhedged exposure in relation to any single investment manager or asset
- manager risk – risk associated with the performance or conduct of external investment managers. This is managed through annual conviction reviews and operational due diligence
- counterparty risk – the risk that a partner to an investment doesn't fulfil their obligations or role. The creditworthiness of counterparties is closely monitored by

reviewing credit ratings, credit default swap spreads, equity pricing, news flows and other indicators

5. Sustainable Finance

Over the 20 years since the Guardians was established, we have developed a strong track record and international reputation as responsible investors, including being named in the United Nations Principles for Responsible Investment Leaders Group, winning a PRI award for stewardship initiative of the year and a number of other accolades.

The Guardians' 2016 Climate Change Investment Strategy is regarded as industry-leading, and we remain at the forefront of global sustainable finance evolution and practice. We believe leadership in this area provides us with a competitive advantage and supports our social licence to operate. Our approach is aligned with the expectations relating to responsible investment and in particular to the application of the Crown Responsible Investment Framework, as set out in the Enduring Letter of Expectations sent in October 2021 to all Crown Financial Institutions by the Minister of Finance and the Minister for ACC.

Sustainable Finance Strategy

In 2020/21, in line with Willis Towers Watson's recommendations in their 2019 Independent Review, the Guardians refreshed the Fund's responsible investment strategy to ensure it would continue to remain at a best practice level over the next decade.

Our review confirmed that global best practice was moving towards 'sustainable finance', a development from the responsible investment approach which had been best practice for the previous 20 years. Responsible investment considers the impact of environmental, social and governance (ESG) risks on the various companies that make up an investment portfolio. Sustainable finance also considers the impact investee companies' activities have on global environmental and social outcomes.

Based on extensive analysis, we believe the Fund's portfolio can do a better job of achieving positive environmental and social outcomes without compromising investment returns. Since 2021, we have made several important changes to the Fund's portfolio as we move to reposition it in line with a sustainable investment approach. These have included:

- shifting our Reference Portfolio equities benchmark and associated passive equity exposure (about 40% of the Fund) to new indices that are aligned with the 2015 Paris Agreement and will require, among other-things, year-on-year decarbonisation
- improving the ESG profile of active equity (factors) mandates, which comprise about 20% of the Fund
- developing an Impact Investment Framework. This framework is based on global good practices for asset owners such as the Impact Management Projects (IMP) 'Five Dimensions of Impact'

The next area of work, being undertaken during 2023/24, will focus on improving the ESG profile of the Fund's listed fixed income holdings. We continue to integrate sustainable finance considerations into our management of our directly held and private market assets.

Climate Change Investment Strategy

Climate change has been a key focus for the Guardians over many years and the NZ Super Fund is recognised as a leader within New Zealand and globally for integrating climate change considerations into the investment process.

Our approach is based on both the significant investment implications of climate change and the New Zealand Government's net zero by 2050 commitment. We are a signatory to a global framework, the Net Zero Asset Owners Commitment, under which we have made a long-term commitment to decarbonising the NZ Super Fund, increasing investment in climate solutions, setting interim carbon reduction targets and undertaking advocacy and engagement in line with net zero goals.

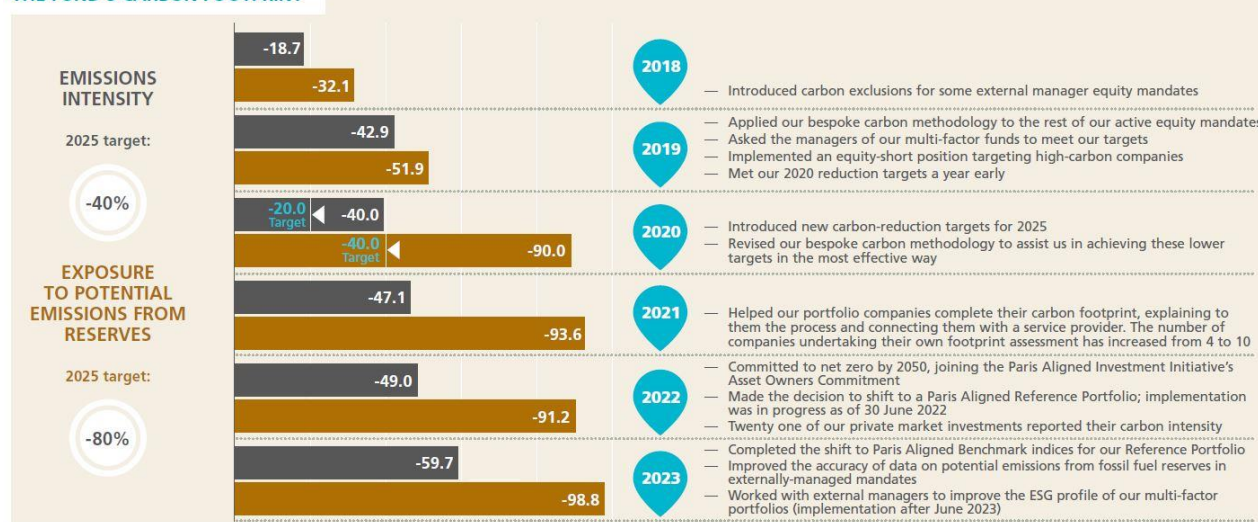
The following table summarises the progress we have made since 2016.

Workstream	Description	Progress
Reduce	Lower the entire Fund's exposure to investments most at risk from climate change policy	<p>The Guardians' short-term carbon reduction targets are to reduce the potential emissions from fossil fuel reserves held by the Fund by at least 80% and the carbon emission intensity of the Fund by at least 40%, by 2025. These targets are relative to the current year's unadjusted Reference Portfolio (baseline). We first achieved these targets in 2020.</p> <p>As at 30 June 2023, the total Fund's carbon emissions intensity was 60% lower than the baseline level, and exposure from potential emissions to reserves was 99% lower.</p> <p>The Fund no longer has any material, long-term holdings of fossil fuel reserves.</p> <p>We first implemented carbon reductions in 2017 and in the six years since then the approach has not cost the Fund anything in terms of investment returns.</p> <p>In 2025 we will set new targets for achievement by 2030.</p>
Analyse	Integrate climate change into our analysis and decision-making	We have adapted our investment decision-making framework to, where practicable, explicitly account for climate change investment risk in valuation models.
Engage	Improve the reporting and management of climate-related risks of the companies the Guardians invest in	<p>Alongside other Crown investors we are currently engaging on climate change with companies in the NZX50. This engagement aims to increase awareness about mandatory climate change disclosures and the implications of our net zero by 2050 commitment for investee companies, and communicate our expectations in terms of climate change risk management.</p> <p>Internationally, the Fund's engagement includes membership of the United Nations Principles for Responsible Investment Leaders Group; Investor Group on Climate Change; and the Carbon Disclosure Project.</p>
Search	Take advantage of investment opportunities presented by the transition to a low-carbon system	We have made substantial investments in renewable energy and low-carbon technology, particularly in the United States. These include a 17% shareholding in carbon-recycling technology company Lanzatech, a 37% shareholding in renewable energy company Longroad, a US\$100 million commitment to Wellington Management's Climate Innovation Fund I and a €125 million commitment to Copenhagen Infrastructure Partners' Energy Transition Fund I. Overall, we have committed approximately US\$470 million to Sustainable Transition opportunities.

The Guardians publishes a carbon footprint for the NZ Super Fund and a Climate Change Report annually, including an updated action plan and emission reduction targets.

The Guardians first achieved carbonZero certification from Toitū Envirocare in 2018/19 and has been successfully recertified in each of the subsequent financial years. The majority of our emissions are incurred through air travel, office electricity use and waste to landfill.

THE FUND'S CARBON FOOTPRINT



Our first carbon footprint was published in 2017.

Exclusions

1. We exclude the securities of companies whose products contravene international conventions New Zealand is party to, and/or New Zealand law; and/or significant Crown policies, from investment by the Fund. Currently, companies that are directly involved in the following activities are excluded:
 - cluster munitions
 - nuclear explosive devices
 - anti-personnel mines
 - tobacco
 - recreational cannabis
 - the manufacture of civilian automatic and semi-automatic firearms, magazines, and parts
 - the processing of whale meat
2. We may also exclude the securities of companies with practices that do not meet the standards set out in our Sustainable Investment Framework. This framework incorporates the NZSRI Act's requirement for the Guardians' statement of investment policies, standards, and procedures to cover ethical investment, including policies, standards, or procedures for avoiding prejudice to New Zealand's reputation as a responsible member of the world community. When a company's practices do not meet the standards set out in our Sustainable Investment Framework, our preference is to work with the company to remedy the issue. However, where we are unable to engage effectively with a company, or we judge that engagement is unlikely to achieve the outcome we require, we may move straight to exclusion.
3. We are legally required to comply with sanctions imposed by the New Zealand Government. Under New Zealand law, we are also required to comply with sanctions imposed by the United Nations Security Council. In line with that, we will exclude the government (sovereign) bonds of any nation state against which New Zealand has imposed meaningful diplomatic, economic or military sanctions.

4. The list of excluded securities is published six monthly. Decisions to exclude companies for breaches of standards (as opposed to excluded activities) are announced following divestment.

6. Performance

The table below sets out the NZ Super Fund's performance as at 30 September.

	Since inception (20 years - Sept 2003)	Last 15 years	Last 10 years	Last 5 years	Last 12 months	Quarter to September 2023 ¹
Actual Fund Returns (before tax, after costs)	9.53%	10.09%	10.01%	6.83%	14.52%	-1.86%
Reference Portfolio Return	7.93%	7.98%	7.85%	4.83%	13.82%	-3.41%
Value-Added (Actual Return – Reference Portfolio Return)	1.60%	2.11%	2.16%	2.01%	0.70%	1.55%
Estimated \$ earned relative to Reference Portfolio	\$15,605m	\$15,610m	\$10,807m	\$5,557m	\$399m	\$1,014m
Government contributions	\$25,344m	\$12,350m	\$10,462m	\$9,712m	\$2,322m	\$404m
NZ income tax (paid)/ recovered	(\$9,656m)	(\$8,130m)	(\$6,359m)	(\$3,332m)	(\$190m)	(\$190m)
Net Government contributions	\$15,688m	\$4,220m	\$4,103m	\$6,380m	\$2,132m	\$214m
NZ Treasury Bill (T-Bill) Return	3.42%	2.30%	2.02%	1.65%	4.63%	1.37%
Net Return (Actual Return – T-Bill Return)	6.11%	7.79%	7.99%	5.19%	9.89%	-3.23%
Estimated \$ earned relative to T- Bills	\$40,049m	\$40,989m	\$31,351m	\$13,264m	\$5,399m	(\$2,113m)
\$ change in net asset position ²	\$64,366m	\$50,787m	\$40,434m	\$23,270m	\$10,056m	(\$1,033m)

¹ Returns for periods longer than one year are annualised.

² Excludes provisions for New Zealand tax.

Net Returns (Actual Fund Returns minus Treasury Bill Returns)

The return on Treasury Bills represents the cost to the Government of contributing capital to the NZ Super Fund, instead of using the money to repay debt. Since inception in 2003, Actual Fund returns have outperformed the Treasury Bill benchmark by 6.11% p.a. (more than \$40 billion).

Reference Portfolio Return Relative to Treasury Bill Return

Our long-term expectation is that over any 20-year period the Reference Portfolio will return the 90-Day Treasury Bill rate plus 2.8% p.a. This 2.8% premium recognises that the Reference Portfolio is invested in riskier assets than Treasury Bills. Over the 20 years to 30 September 2023, Reference Portfolio returns exceeded the return on Treasury Bills by 4.51% p.a.

Value Added (Actual Fund Returns minus Reference Portfolio Returns)

This measure shows how successful the Guardians’ active investment strategies have been in adding value over and above what the Reference Portfolio achieved. Our long-term expectation is that over any 20-year period our active investment strategies will earn the Fund an extra 1% per annum. This measure is a way of evaluating how successful our active investment strategies have been in adding value above passive investments. Since inception, the Fund has beaten the Reference Portfolio by 1.6% p.a. (more than \$15 billion).

Risk-Adjusted Returns

Focusing solely on returns ignores the risk taken to achieve them. The Sharpe ratio expresses portfolio returns above a benchmark return as a ratio of the volatility of returns. The higher the ratio, the greater the return for the risk taken, and vice versa. The Sharpe ratio enables comparisons to be made between the risk-adjusted performance of the Reference Portfolio and that of the Actual Portfolio, and also against our long-term expectations. This is shown below.

30 June 2023	Reference Portfolio	Actual Portfolio
Expected Sharpe ratios	0.21	0.28
Realised Sharpe ratios		
Since introduction of Reference Portfolio (July 2010) to 30 June 2023	0.77	0.99
Since inception to 30 June 2023	0.46	0.55

The Guardians’ long-term expectation is that the Reference Portfolio will achieve a Sharpe ratio of 0.21. For the Actual Portfolio, we expect a slightly higher Sharpe ratio of 0.28, reflecting the value we expect to be able to add through active investing.

The Reference Portfolio has generated a higher Sharpe ratio than expected. Since its introduction in 2010, the Reference Portfolio has a realised Sharpe ratio of 0.77. This is because the Reference Portfolio has experienced higher-than-expected returns, and lower-than-expected volatility.

The Actual Portfolio has also generated a better Sharpe ratio than expected. Since July 2010, the Actual Portfolio's realised Sharpe ratio has been 0.99, materially exceeding our expectation of 0.28. Again, this has been driven largely by returns exceeding expectations and, to a lesser extent, lower-than-expected volatility. Since inception, the Actual Portfolio has realised a Sharpe ratio of 0.55.

Costs

Cost control is central to achieving our mission to maximise returns without undue risk. We aim to achieve the right balance between minimising cost and implementing investment

strategies that will, after adjusting for risk, add the most value to the NZ Super Fund over the long term.

CEM Benchmarking operates the world's most widely used and comprehensive cost structure benchmarking survey. CEM assesses the cost structure and value add of the NZ Super Fund against 296 funds from around the world, with a particular emphasis on a peer group of 19 similarly sized funds.

CEM's most recent report, for the five years ended 31 December 2022, found that the NZ Super Fund's net five-year value-add was approximately \$4.5 billion better than the median value-add of our peer group.

While costs had increased from 2018, they remained below both the peer group median cost and the median cost for all funds in the survey.

7. Accolades

While gathering awards is not the Guardians' purpose, recognition does provide an indication of our reputation and standing in the global investment industry. Recent accolades include:

- ranked the world's top performing sovereign wealth fund over the past 10 years by global state-owned investor think tank Global SWF
- winner, Best Asset Owner Regional Australia/New Zealand, AsianInvestor 2021 Institutional Excellence Awards
- ranked among the world's most responsible asset allocators by the Responsible Asset Allocator Initiative (RAAI).
- winner, Best Net Zero and Climate Action Investor, 2022 Mindful Money Awards
- winner, Climate Action (Top Reducer Closest to Zero) and Climate Action (Small Organisation) Awards at the 2022 Toitū Envirocare Brighter Future Awards.
- winner, Chair's Commendation Award for 10 Consecutive Gold Awards, Australasian Reporting Awards

8. Elevate

The legislation that established Elevate received broad cross-party support; the Venture Capital Fund Bill and the accompanying New Zealand Superannuation and Retirement Income Amendment Bill passed into law by 119 votes to 1.

Governance Arrangements

The Guardians is responsible for investing and managing Elevate in accordance with a legislative investment mandate. Elevate is required to invest in New Zealand's venture capital markets using best-practice investment management that is appropriate for institutional investment in those markets.

The role of the Guardians with Elevate is more limited than the NZ Super Fund mandate. Under the establishing Act, the Guardians was required to appoint NZGCP, a Crown entity, as external manager to undertake investment of the Elevate Fund.

The following table provides an overview of the resulting division of labour.

<p>Minister of Finance</p> <ul style="list-style-type: none"> • Issue a policy statement outlining the high-level requirements for Elevate, including directions on what the Guardians must give effect to and have regard to. • Revise the policy statement if required, following consultation with the Guardians. • Issue directions for the winding up of Elevate when broader market development objectives have been achieved. 	<p>Guardians</p> <ul style="list-style-type: none"> • Enter into a contract appointing NZGCP to operate the Elevate fund-of-funds. • Monitor the performance of Elevate and NZGCP, including through a Limited Partner Advisory Committee (LPAC) that reviews significant matters. • Manage and administer Elevate consistent with the Ministerial Policy Statement and legislative requirements. • Ensure Elevate is invested using best practice investment management appropriate for institutional investment in New Zealand’s venture capital markets. • Annual financial reporting for Elevate, including preparation of Statements of Intent and Performance Expectations. • Preparation of Statement of Investment Policies, Standards and Procedures for Elevate. • Report on how the Guardians have given effect of directions in the Ministerial Policy Statement.
<p>External Manager (NZGCP)</p> <ul style="list-style-type: none"> • Act as the sole manager of Elevate fund-of-funds, which is formed as a limited partnership. • Establish an Investment Committee to make decisions on investment in underlying funds. • Monitor and report on investments. • Ensure underlying funds continue to meet eligibility and other requirements. 	

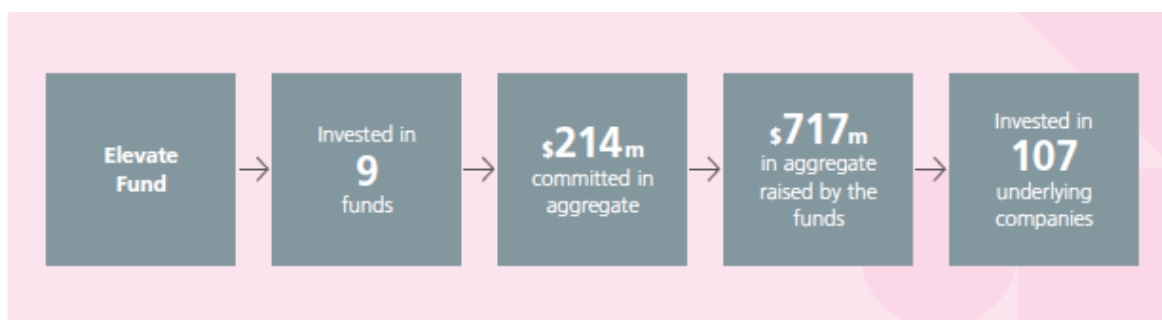
Conviction Process

The Guardians uses a conviction framework to assess all its investment managers’ capability to execute an investment opportunity on its behalf, including NZGCP. Eight factors of performance are used to assess whether managers have the necessary capabilities, specifically:

- Viability
- Structure and focus
- Trust
- Risk awareness and management
- People capabilities
- Process capabilities
- Opportunity consistency
- Performance

The Guardians undertakes an annual conviction review on NZGCP, with the most recent review occurring in September 2023. Note that the conviction framework used for NZGCP is substantially the same as the framework used for all of our other external managers; however, in the Performance factor for NZGCP we put more emphasis on venture capital market development, as well as outright investment performance.

Performance



An important measure of Elevate’s performance is its ability to catalyse private capital into the venture capital markets, supporting a wider range of managers. Earlier this year, Elevate successfully reached the mark of a billion dollars of private and public funding committed to New Zealand’s venture capital markets. This was a significant accomplishment, noting that the market prior to the inception of Elevate had an estimated \$230m of active funds under management and only a few active venture capital funds.

One performance indicator for a fund such as Elevate is ‘Total Value to Paid In’ (TVPI). While it is still very early in Elevate’s investment cycle to measure investment returns, as at 30 June 2023, TVPI gross of management fees and fund costs was 1.15, and net of costs 1.06 – meaning it is currently worth slightly more than the amount invested. This is broadly in line with what would be expected given the return profile typical of venture capital investments. In private equity there is a tendency for funds to deliver negative returns in initial years and then increasing returns as investments mature (a return profile often referred to as the j-curve).

As would be expected at this stage of Elevate’s development, there have been no investment realisations to date. It is anticipated that there will be no realisations for at least two to three years.

9. Significant Matters

We would like to draw five particular matters to the attention of the incoming Minister.

Repeal of Section 59 (Controlling entity provision)

A Bill repealing section 59 – New Zealand Superannuation and Retirement Income (Controlling Interests) Amendment Bill – was introduced to Parliament earlier this year. The Bill was considered by the Finance and Expenditure Select Committee, which recommended that the Bill be enacted. At the time of the dissolution of the 53rd Parliament the Bill was awaiting its second reading.

Under the existing legislative framework, the Fund is prohibited from taking a controlling stake in another entity. This provision was deemed appropriate for the maturity of the fund at the time (2001). Demonstrably, the Guardians’ governance has evolved, in line with the NZ Super Fund’s investment capabilities, to provide effective oversight of complex investment strategies. Alongside this, direct investment has become a much more common feature of best practice portfolio management globally.

The current prohibition constrains the Guardians from responding to the Ministerial Direction regarding domestic investment opportunities, including infrastructure investment. Additional benefits of removing the control prohibition include:

- improved investment management – by providing greater flexibility in terms of structuring and exit
- the potential to influence better ESG outcomes
- a larger addressable investment opportunity set

Concerns have been expressed that removing the prohibition may increase the possibility of political pressure and a resulting loss of independence, and that it may create a perception that investee companies would effectively be government guaranteed. The Guardians believes that existing governance and accountability mechanisms are sufficient to manage these risks. This view is consistent with the advice provided by Treasury. We understand that the Select Committee also considered these risks and how they would be managed as part of its review of the Bill and did not recommend any changes before referring the Bill back to Parliament for its second reading.

Allowing the option of taking a controlling interest simply provides the Guardians with an additional investment option and tool. It would be used only when the Guardians was convinced that it would add more value to the Fund than alternative structural and commercial options or would otherwise help the Fund to carry out its mandate.

Board Appointments, Fees and Capability

As noted on page 7, the process by which the Guardians Board is appointed is unique to the Guardians.

It is important to the success of the Guardians in managing the NZ Super Fund (which comprises a significant proportion of the assets on the Crown's balance sheet) that its Board has high calibre members with appropriate skills and expertise.

The Guardians is currently in the process of recruiting new board members.

Attracting suitable Board candidates has been made more difficult in recent years by:

- A lack of funding and resources for the nominating committee. Currently, the committee does not have sufficient funding to use search firms to help identify candidates
- The fees payable to Guardians' Board members being significantly below the market. Currently, Board members receive a fee of \$48,000 per year (\$98,000 for the Chair). These fees do not adequately reflect the workload requirements and increasing demands being made of Board members as the Fund grows in size and complexity. By way of comparison, the annual fees payable to Board members of the Future Fund (one of our peer funds) are A\$214,670 for the Chair and A\$107,340 for other members.

Elevate – Future Funding

Elevate was established based on capital commitments of \$300 million for an initial investment period, of which \$260 million was provided by the Crown in early contributions (\$240 million of which was diverted from the NZ Super Fund). The remaining \$40 million of funding was provided in Budget '23.

Further government funding will be required for Elevate until such time as it becomes self-sustaining (i.e. when distributions from the initial investments can be re-invested). NZGCP is currently modelling the venture capital market's funding requirements, and working with economic agencies to present the findings of this analysis to the incoming Government.

In venture capital, distributions from investments do not typically start to be realised until 7-10 years after the initial investment. Elevate launched in March 2020 and has committed capital progressively to managers who are building their portfolios over time.

If further funding is not provided there is a material risk that the progress made to date in strengthening New Zealand's venture capital eco-system will be lost. The availability of further funding for Elevate is also considered by us as a conviction matter in respect of our appointment of NZGCP as the manager of the mandate.

An indication of the potential opportunities available was provided by the recent Startup Advisors Council report, 'UpStart Nation', which recommended an additional \$500 million of funding be committed to Elevate over a ten-year period.

While Elevate has achieved significant success in catalysing private capital to date, current market conditions are much more challenging and NZGCP has seen established managers struggle to raise capital in recent times.

Most or all of Elevate's funds are likely to raise a further vintage during the portfolio management period. These are likely to be critical vintages for the fund managers: many of the underlying funds will still be developing and enhancing the portfolio companies in their earlier fund(s) and will not yet be able to demonstrate a track record of returns to potential investors.

Further funding for Elevate would bridge the gap until such time as Elevate began to receive realisation funds that it could continue to reinvest (i.e. essentially becoming self-sustaining). It would also enable Elevate to support underlying funds through a challenging period of the market cycle, thereby enabling those funds to complete the maturation of their businesses and teams to a stage where they can achieve exits and fund returns that can be used to attract more private capital into subsequent vintages.

Taxation

The NZ Super Fund is currently required to pay domestic income tax to the New Zealand Government. This treatment is almost unique globally in terms of sovereign wealth funds and differentiates us from the Government's other large investment funds, ACC and the Earthquake Commission, and iwi investors such as Tainui Group Holdings and Ngāi Tahu Holdings, all of which are exempt from domestic income tax.

The Guardians has consistently held the view that the NZ Super Fund should not be liable for domestic income tax, a position which was also recommended by the Government's Tax Working Group in 2019. Such a change would reduce deadweight loss, improve efficiency, and be at worst fiscally neutral for the Government.

The NZ Super Fund's assets are included on the Crown's balance sheet. As a result, Crown contributions do not increase government debt, nor does tax paid by the NZ Super Fund increase government revenue or assets.

Typically, when public policy cases are made against tax exemptions the principal argument is tax neutrality. That is not the case here, however, as neutrality is not an issue.

Policy considerations supporting the NZ Super Fund being given tax-exempt status include:

- improved efficiency and reduced compliance costs
- removing the possibility of the NZ Super Fund needing to liquidate long-term assets and positions to pay tax, for example in a year with a very large tax liability. (For example, the Fund paid \$2.2 billion in NZ tax during the 2020/21 financial year). As a result of transaction and opportunity costs this activity represents an unnecessary fiscal cost
- reduced foreign tax exposure. The NZ Super Fund's current New Zealand tax status affects its status in some foreign jurisdictions, as it is more difficult to argue the principle of sovereign immunity when liable for domestic tax
- consistency with the tax treatment of the Government's other large investment funds (ACC and EQC) and with iwi investors. This would simplify co-investment by the Fund alongside these entities
- consistency with the tax regime applied to almost all other sovereign wealth funds (the other outlier is the Korean Investment Fund)

The main argument which has been made against giving the NZ Super Fund tax exempt status is that the payment of domestic tax by the Fund creates greater flexibility for the Government to manage, and adjust, its future fiscal position.

We note that the levying of domestic tax during periods when contributions are suspended effectively constitutes a withdrawal from the Fund i.e. the effect of the suspension is not just that contributions are halted, but that through tax payments continuing, funds that were ring-fenced for future universal superannuation payments are diverted to other, short-term purposes. While this is technically possible, it is inconsistent with the inter-generational purpose of the Fund and with the express intent of the Act.

If the Government is unable to support granting the NZ Super Fund tax exempt status, we urge it to consider:

- amending the Controlled Foreign Company Rules to prevent the Fund's income from controlled foreign companies being taxed in New Zealand where this is contrary to the policy intent of the rules
- exempting the NZ Super Fund from the land tainting tax rules, as is currently done for Council Controlled Entities and Kāinga Ora where they hold land separate from any land development business, so that any proceeds the NZ Super Fund receives from the disposal of land assets not connected with any land development business (e.g. New Zealand farmland or infrastructure assets) are not subject to tax.

CEO Appointment

In May 2023, Guardians chief executive Matt Whineray announced his resignation after 15 years at the Guardians, the last five as chief executive. Mr Whineray will leave in December 2023.

Recruitment firm Johnson Partners has been appointed to assist the Board in selecting a new CEO and we expect this process to be completed by the end of the year. Under the Crown Entities Act 2004, the Public Service Commissioner agrees contractual terms including base remuneration and remuneration structure with the Board; the Commissioner

also agrees to any future changes to the Chief Executive's base remuneration. The Board will proactively work with the PSC as part of the CEO appointment process.

10. Key Person Directory

Board Members

- Catherine Drayton (Chair)
- David McClatchy
- Doug Pearce
Chair, Audit Committee
- Henk Berkman
- Fiona Oliver
- John Williamson
Chair, EPR Committee

Leadership Team

- Matt Whineray
Chief Executive
- Cristina Billett
GM Corporate Affairs
- Mark Fennell
GM Risk
- David Sara
GM Technology
- Mika Austin
GM Human Resources
- George Crosby
GM Portfolio Completion
- Stephen Gilmore
Chief Investment Officer
- Paula Steed
GM Strategy and Shared Services

Government Relations

- Catherine Etheredge
Head of Communications
- John Redwood
Senior Communications Strategist