

Methodist Church of New Zealand Supernumerary Fund

Statement of Investment Policy and Objectives

July 2016

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1 Introduction

1.1 Purpose of the SIPO

The purpose of this Statement of Investment Policy and Objectives (SIPO) is to document the decisions of The Methodist Church of New Zealand Supernumerary Fund (the “Fund”) has made on the management of its investment funds. In particular the SIPO:

- Specifies the overall investment objectives
- Specifies the investment beliefs and philosophy applied to the investments
- Details the investment strategy
- Details the asset sector objectives
- Allocates the responsibilities between the Trustee and the Investment Adviser
- Specifies the terms of the investment guidelines and policies and constraints to be observed by the Trustee
- Serves as a review document to support the on-going oversight of the management of the investments.

The Trustee acknowledges that achieving long term investment success requires:

- A clearly stated purpose for the investment funds
- A defined set of objectives
- An investment strategy consistent with the agreed objectives
- Adherence to the SIPO.

1.2 Background to the Fund

The purpose of the Fund is to provide retirement income benefits for Ministers of the Methodist Church of New Zealand (Church). The Fund is a defined benefit scheme and pensions are payable to retired members and may increase depending on the finances of the Fund. Benefits may be payable to members on retirement, death, disability, or when suffering financial hardship while in service or when they leave the Fund. Pensions are also payable to a surviving spouse/and or beneficiary.

The Fund is designated as a restricted legacy superannuation scheme under the Financial Markets Conduct Act 2013 (the “Act”).

The Fund was closed to new members in 2010 and is expected to reduce in size overtime.

As at 31 January 2016 the Fund was \$12.555 million. The Fund has a negative cash flow i.e. the benefits paid plus expenses exceed the contributions flowing into the Fund amounting to \$0.963 million in the 2015/16 year.

The most current version of this SIPO is available on the register entry for the Fund on the Disclose website at www.business.govt.nz/disclose.

1.3 Effective date

This SIPO takes effect on 30 September 2016.

1.4 Tax

The investments held by the Trustee are not subject to tax.

1.5 Updates to the SIPO

This SIPO is an update of the original SIPO, dated June 2011. The SIPO will be reviewed every 3 years to assess its ongoing suitability in light of the circumstances of the Fund and the prevailing economic environment, with the next review due in June 2019. In the event of a major change to the purposes of the Fund or a major event impacting the Fund's investments the Trustee may consider an earlier review. The review will be carried out by the Trustee in conjunction with the Fund's Investment Adviser.

The Trustee is responsible for approving the SIPO. Changes to the SIPO will be made by resolution of the directors of the Trustee and the updated SIPO will be lodged as required by the Act.

1.6 Responsibilities for the management of the assets

In arriving at their approach to manage the investments the Trustee has taken account of the responsibilities, functions, and duties of the Trustee under the Financial Markets Conduct Act 2013 (FMCA) (in particular, the responsibilities and duties placed on 'managers' under the FMCA) and the

the Trustee Act 1956. Accordingly the Trustee should have regard to the following matters:

- The risk of capital loss or depreciation.
- The potential for capital appreciation.
- The likely income return.
- The effect of inflation.

The responsibilities of the Trustee are:

- To agree the investment strategy.
- To manage the governance process for the investments in a manner that is consistent with the investment philosophy and other guidelines stated in this document.
- To review the performance of the Investment Advisor and Investment Manager.
- To communicate to members the results of the Fund's performance.

1.7 Investment adviser

The role of the investment adviser is to advise the Trustee on all matters as they relate to the investments and in particular:

- To assist the Trustee in achieving the investment objectives.
- To monitor and report to the Trustee quarterly on all aspects of the Fund's investments.

The Trustee shall review the performance of the investment adviser triennially with the next review due in 2019.

1.8 Investment Manager

The Investment Manager is responsible for the investment of the Fund's assets in accordance with, amongst other things, this SIPO.

The criteria for selecting or retaining a Fund Manager are:

- Business
- People
- Process
- Performance
- Fees

The criteria will be reviewed annually and on appointment the basis shall be documented.

At the date of their appointment the reasons for selecting the manager will be recorded. Each asset sector manager selected will be chosen on the basis of the role the sector is to play in the Fund's investment strategy. The manager will be selected from the universe of established NZ managers available.

Each investment manager's performance is to be continuously monitored and reviewed over rolling three-year periods.

2 Directory

2.1 Trustee

The Trustee of the Fund is Methodist Church Of New Zealand - Te Haahi Weteriana Superannuation Trustee Limited.

2.2 Investment and Administration Manager and Fund Secretary

The investment management of the Fund is undertaken by the Church's Board of Administration (Investment Manager). Amongst other things, the Investment Manager is responsible for the investment of the Fund's assets in accordance with this SIPO.

The administration of the Fund is completed by Mercer (N.Z.) Limited.

The secretary to the Fund is the Church's Board of Administration.

2.3 Investment Adviser

Melville Jessup Weaver is the investment adviser to the Fund.

3 Investment Strategy and Objectives

3.1 Strategy

The Fund pursues a diversified strategy with a relatively conservative asset allocation with assets invested in a range of asset classes. The Trustee is committed to investing in the assets in line with the beliefs stated in section 4.

3.2 Objectives

Broad objectives

The investments of the Fund are held to provide a steady return and income stream to the Fund over time. It is accepted that investment markets rise and fall and that on occasions the Fund may receive a negative return for the year. For the purpose of setting its investment strategy the Trustee considers that investing with a 10 year time horizon will provide a balance between utilising the higher return potential from the long term nature of the funds held and the need for the value of the investments held to not vary annually unduly.

The broad investment objectives are:

- To ensure the Fund's assets will be invested in a prudent manner.
- To ensure that the Fund will meet benefit entitlements and expenses when they fall due.
- To achieve, over the long term, returns greater than the risk-free rate of return.
- To maximise the real rate of return subject to the Fund's risk profile.

Quantified targets

The agreed quantified targets, against which the investment performance will be assessed, are:

- To achieve a real return (i.e. after allowance for increases in the CPI Index), net of investment fees, of 1.5% per annum
- To achieve an absolute return, net of investment fees, of 3.5% per annum.

There is a 70% chance of achieving the targets above over a 3 year period. We note here that the expected return for the Fund is 4.6% per annum pre fees. It is noted here that the Investment Manager charges the Fund between 23 basis points and 70 basis points (depending on the nature of the assets invested) for managing the investments.

While the performance is monitored quarterly the time frame for achieving the above objectives are 3 years.

Peer group measurement

The Trustee also measures the performance of the Fund against a peer group set as the MJW KiwiSaver Moderate Funds. The aim is to achieve, over a 3 year period, an above average performance against this group allowing for the fact that the allocation to growth assets is on average 40% for the peer group compared to the Fund's 35%. When making the comparison an allowance of 50 basis points will be made for the internal management costs.

3.3 Level of risk

The Trustee is mindful of the importance of achieving the objectives and has considered the matter of the level of risk it is prepared to take before arriving at the quantified objectives. In particular the

Trustee has considered the output of quantitative models provided by the investment adviser. The probabilities of the Fund having a negative return are as follows:

- 1 year 13.8%
- 3 years 1.6%
- 5 years 0.2%.

4 Investment beliefs and philosophy

4.1 Introduction

The investment philosophy of the Trustee is:

- Investment markets are broadly efficient.
- The prime driver of investment results will be the long-term (strategic) asset allocation and it is important to limit the movements around this long term position.
- The Trustee does not believe value can be added by making tactical asset allocation decisions and accordingly the asset allocation is managed on a passive basis with defined automatic rebalancing rules.
- Diversification at a sector level and across the portfolio results in a better risk/return result than otherwise.
- To pursue a strategy of buying and holding securities rather than actively trading securities.
- Value can be added by efficient implementation of investment decisions.

The Fund adheres to the philosophy of the Church in regards to ethical investments as at the date of this SIPO and as revised and amended on an ongoing basis.

4.2 How these views are expressed

The management of the assets is the responsibility of the Investment Manager.

The approach is to buy individual securities and on occasions seek exposure to a sector by investing in an established fund.

5 Investment Guidelines and Benchmarks

5.1 Investment Guidelines

The investment guidelines in regard to each of the asset sectors are set out in this section.

In the event the Fund decides to invest with a fund managed by a fund manager the Trustee shall review the terms of the fund's guidelines and in the event of any inconsistency with the Fund's guidelines these are to be noted and the Trustee to decide how to proceed.

5.2 Cash

The level of cash held by the Fund while partly dependent on the cash flow requirements will be in accordance with the benchmark asset allocations in section 5.5.

Cash may only be held at ANZ, BNZ, ASB, WESTPAC, KIWI BANK, and Taranaki Saving Bank and if such banks have a long term Standard and Poor's rating of A + or more.

NZ Bonds and Fixed Interest Portfolio

Investment may be made in New Zealand Bonds (or their equivalent); namely Fixed Interest Securities (such as Debentures) and securities issued by the New Zealand Government, State Owned Enterprises, Local Authorities and well recognised prudentially sound listed public entities. The exposure limits for the credit rating bands for the NZ bonds are shown in the table below.

Credit rating band	Permissible % of portfolio
AAA to A-	35 - 100
BBB+ to BBB-	0 - 35
Unrated	0 - 15

The maximum exposure to any one issuer for either the NZ bonds is shown in the table below:

Credit rating band	Maximum % of portfolio to any issuer
NZ Government	100
AAA to A-	25
BBB+ to BBB-	15
Unrated	10

The limits in the table above have been set to reflect the new approach adopted by the Trustee in regard to its bond holdings. Currently the securities held are of a lesser quality. During the transition to the new limits the current non-compliance is not considered to be a breach of the SIPO by the Trustee.

5.3 Global bonds

Any investment in this asset class shall be invested through a managed fund which at all times must have a minimum weighted average credit rating by Standard and Poors of A- (or other equivalent rating by another rating agency). It is noted that the Fund does not currently hold any global bonds.

5.4 Equities

The Trustee has the following guidelines:

- Investments must be confined to widely held securities trading on the main boards of relevant country.
- No investment should result in the Fund holding more than 5% of the equity in any one company.
- No direct holding in a single company should equate to over 3% of the Fund's investments.
- Holdings are not confined to ordinary shares but can be any listed hybrid equity security issued by a company in which the Trustees are able to invest and which is consistent with these investment guidelines.

5.5 Benchmark asset allocation and ranges

The benchmark asset allocation and ranges for the Fund are as follows:

	Benchmark %	Benchmark range % - %
Australasian shares	17.5	12.5 - 22.5
Global shares 50% hedged	17.5	12.5 - 22.5
Growth assets	35.0	27.5 - 42.5
NZ bonds	45.0	37.5 - 52.5
Global bonds 100% hedged	0.0	0.0 - 15.0
Cash	20.0	12.5 - 27.5
Income assets	65.0	57.5 - 72.5
Total assets	100.0	
Foreign currency exposure		
Australian shares	100.0	100.0 - 100.0
Global shares	50.0	45.0 - 55.0

The benchmark asset allocation will be reviewed as part of the SIPO review outlined in section 1.5.

5.6 Rebalancing of the portfolio and cash flow management

Rebalancing

Asset allocation ranges have been set as above and the rebalancing rules to apply are as follows:

- The allocation to each asset class will be allowed to vary within the range set.
- When the asset allocation for any asset class or for the total growth/income assets is close to the range limits the Investment Manager shall rebalance the assets back to being close to the benchmark position by realising relevant financial products and reinvesting the proceeds of

that redemption in the other asset classes. The Investment Manager will inform the Trustee accordingly.

- The rebalancing will take place within a month of the Investment Manager being aware of the need to rebalance.

In the event that the asset allocation is more than 2% over the agreed limit (considered to be a “material breach”) the Investment Manager shall notify the Trustee immediately and correct the breach within 5 working days of the Investment Manager becoming aware of the breach. In the event the rebalancing is not made within the 5 working days the Trustee must report the breach to the FMA as soon as practicable pursuant to regulation 94 of the FMC Act regulations, together with the information prescribed in regulation 96.

The Investment manager is required to monitor the asset allocation of the Fund on a monthly basis.

Cashflow

Any payments requiring the immediate cash up of investments are to be made from the cash sector.

New cash flow will be invested by the Trustee to rebalance the Fund back towards the benchmark position.

5.7 Investment targets

Benchmark outperformance targets shall be set to be achieved in each sector over rolling three-year periods. These targets are laid out below.

Sector	Value add % pa
Australasian shares	2.00
Global shares	1.25
NZ bonds	0.75
Global bonds	0.75
Cash	0.40

6 Investment policies and procedures

6.1 Introduction

This section sets out the main policies and procedures the Trustee follows in managing the Funds' investments.

6.2 Liquidity management

The Fund regularly needs cash to make benefit payments, particularly pensions. There is a risk that the Fund may not be able to redeem investments to make such payments or, if investments in only some investment sectors can be redeemed, asset allocations may deviate from the target allocations.

Accordingly the Fund invests in securities that in all but exceptional circumstances are liquid.

6.3 Currency hedging

The Fund invests offshore and the risk exists that changes in the exchange rate will reduce the value of the assets.

The hedging position adopted for each of the global assets is:

- Global equities The benchmark is 50% exposure with 5% limits on each side.
- Australian shares The benchmark is 0% hedged.
- Global bonds The benchmark is 100% hedged with a 5% limit.

6.4 Future contracts and leveraging the portfolio

Futures contracts and options are to be restricted to hedging techniques. There will be no leveraging of the portfolio.

6.5 No security lending

Securities are not to be lent to any other third party without the consent of the Trustee.

6.6 Conflicts of interest

The directors of the Trustee include beneficiaries of the Funds and board members of the Investment Manager.

Notwithstanding:

- (a) the individual interests of each director as beneficiary; and
- (b) the interests of those directors who are board members of the Investment Manager,

they each recognise their responsibility to act in the wider interests of all beneficiaries and to treat each beneficiary equitably.

Any specific conflicts of interest are managed as they arise. If a conflict arises, the process for managing the conflict will entail identifying and recording the conflict, assessing the conflict and taking appropriate measures, if required, to manage the conflict. A director shall be required to stand aside from any decisions related to a conflict involving themselves.

6.7 Investment performance monitoring

The following information is required from the Investment Manager on a monthly basis for both each asset class and the Fund for the Trustee:

- Market values as at the start and end of the month
- Contributions and withdrawals for the month
- Actual returns gross of fees, at the end of the month, rolling quarter and year to date
- Index returns for the same periods.
- Confirmation that the Fund is being managed in compliance with the SIPO.

At the end of each quarter, the Investment Adviser is to provide a report including:

- Comment on past performance and the reason for out/under performance
- Economic comment pertinent to the mandate and the outlook for future returns.

6.8 Investment mandates

Details on the benchmark of each asset sector are provided in the Appendix.

7 Risk management

7.1 Introduction

The Trustee is mindful of the need to identify risks and manage them appropriately. In addition to the matters covered in section 5 they have identified the list below. It is not meant to be exclusive but does identify some important matters. In each of the sections below we first state the risk and the response of the Trustee to managing the risk.

7.2 Market risks

Macro-economic effects, global and in New Zealand, can and do affect investment markets and hence affect overall investment returns and/or the returns of individual asset classes.

The Trustee engages the Investment Advisor who monitors macro-economic trends and advises the Trustee on changes to portfolio asset allocations and investment management appointments to take account of macro-economic trends.

7.3 Stock selection risks

The Trustee with advice from the Investment Manager pursues an active investment policy and makes decisions on which securities to purchase and hold and which funds to invest in. This policy of active management of investments may result in investments under-performing benchmark returns if the decisions made result in poor short-term stock selection outcomes.

The Trustee reviews the security selection decisions made to assess whether they need to make improvements and monitors the performance of the investments selected with advice from the Investment Advisor.

7.4 Interest and credit risks

Movements in interest rates and risks of credit defaults may adversely affect the value of securities and the return on bond investments.

When the Trustee invests in fixed interest investments and cash take account of expected movements in interest rates and credit risks.

A Investment mandates

Introduction

The investment mandates cover the following asset classes:

- Australasian Shares.
- Global Shares.
- NZ Bonds.
- Global Bonds.
- Cash.

Details on benchmark for each asset sector are provided in the following sections.

Australasian Shares

Performance Benchmark 50:50 split of the S&P NZX50 Index and the S&P ASX 200.

The benchmark split between NZ/Australia is 50%/50% with limits of 20% on either side.

Global Shares

Performance Benchmark MSCI World Index, 50% hedged to the NZ dollar.

NZ Bonds

Performance Benchmark S&P NZX NZ Government Stock Index.

Global Bonds

Performance Benchmark Barclays Global Aggregate Index.

Cash

Performance Benchmark S&P NZX NZ 90 Day Bank Bill

Hedging

The performance of the hedging policy in respect of the Australian and global shares will be monitored separately to the underlying asset class exposure and returns.