The Rise and Rise of Sovereign Wealth Funds: Long-term investing

Adrian Orr, CEO, Guardians of NZ Superannuation

Speech to the Trans-Tasman Business Circle, October 2013

Thank you very much for the privilege of speaking to the Trans-Tasman Business Circle audience today. The invitation provides me an opportunity to celebrate with you our 10th year of investing as at the end of September 2013.

It also provides me with an opportunity to outline:

- what a Sovereign Wealth Fund (SWF) is,
- why these funds are growing in size, number, and influence, and
- why the Guardians of NZ Superannuation are proud to wear the moniker SWF.

I will elaborate on these issues using our experience as a long-term investor over our first decade.

Finally, I will briefly outline the means by which we motivate our investment search activities, highlighting why we have received international acknowledgement for our governance, transparency and innovation, and how we are positioning ourselves to benefit from the anticipated and unanticipated events of the future.

Congratulations and 10 year milestone

Before going further, I do want to say I am immensely proud to be the current Chief Executive Officer of an institution that has reached its 10-year investment milestone, and which is destined to serve New Zealand's interests for decades to come.

I would like to acknowledge the exceptional efforts of the current and past Board members of the Guardians, some of who are in the audience today. I would also like to acknowledge the dedicated and exceptional staff of the Super Fund, some of whom are also in the audience today.

We have spent the last 10 years both building and operating the Fund simultaneously. I have likened it to bolting larger wings onto a plane while it is in the air.

However, 10 years on, I can confidently say the Guardians' Board and team have shown that we truly get the importance of:

- staying focused on our legislated purpose – maximising returns without undue risk, and
- using our operational independence and our endowments - of a long horizon and known liquidity - to their fullest in order to achieve sustainable success.

I also 'tip my hat' to our legislation. Our Act is 'as good as it gets' in a democracy, in terms of enabling an intergenerational investment vehicle to operate within a three-year election cycle. The so-called 'double arms length' separation between the Government of the day and the Guardians both enables the Government to delegate and monitor responsibility and accountability, and also openly discuss investment opportunities and priorities with the

Guardians. Meanwhile, the Guardians can get on and make independent, long-horizon, commercial investment decisions.

In my travels I have not seen better enabling legislation, nor better implementation. Our legislation has enabled me as a CEO to attract and retain a dedicated staff of - globally sought after - investment professionals.

As you can guess, I am very proud of our team at the Guardians. They have chosen New Zealand and its future prosperity as worth working towards, in many cases for lower personal earnings potential and - initially at least - without the well-oiled systems and process of a long established global financial institution. We can now stand beside any of our global peers.

Our performance

Of course, as CEO, I would say our team and Fund is special. However, I do have some facts and figures, and awards, to support this claim. Our awards have been celebrated well in our 2013 Annual Report released earlier this month. They include global recognition for investment innovation, responsible investing, transparency, and financial accounts and reporting.[1]

However, what matters in large part to future generations is our earnings performance, otherwise why bother taking the financial risk. September 2003 saw the first capital contribution made into the Fund. The first 10 years has been quite a ride – none of which was predicted or predictable, just like the next 10 years.

We have experienced the recovery from the 'dotcom bubble', a credit crunch, a full-blown global financial crisis, the rise and rise of Emerging and Frontier markets, a global commodity boom, the near demise of the European currency union, record low official interest rates, and we are have just recently seen some extraordinary political events in the USA.

Underlying these short-term fluctuations, and ignoring the geopolitical challenges that simmer and boil up from time to time, we are also experiencing an incredible global transformation in demographics, urban migration, rising per-capita incomes, and changing energy usage and fossil fuel wealth. These long-term and unstoppable trends are rapidly changing the fortunes of nations.

I could go on, but the list of largely unanticipated events is nearly endless – and a lot longer than the list of anticipated ones. We do not pretend to be able to predict the timing of these events. However, as a long-term investor we must understand and prepare ourselves, as best we can, to benefit from the underlying trends.

As I will outline later, throughout our initial 10 years, the Guardians have built a set of institutional disciplines and investment tools to not only withstand the inevitable short-term

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[1] Winner, most innovative sovereign wealth fund globally, 2012 AiCIO awards; Finalist, 2013 Global Responsible Investment Reporting Awards; Winner, 2012 NZICA Public Sector Annual Report of the Year; Winner, Chairman's Award for best first-time entrant, 2013 Australasian Reporting Awards.

volatility (both in rising and falling asset price markets), but to benefit from that volatility along the way.

In terms of our investment performance to date, we are pleased to say we are creating considerable wealth for future New Zealanders, and that the Fund is well ahead of its initial performance expectations.

I preface this expectations claim noting that 10 years is in fact a short period for measuring the success of a long-term investor like the Guardians. Our confidence in forecast returns peaks at periods of 20+ years ahead, when we expect to return at least the risk-free rate plus 2.5% return per annum on average.

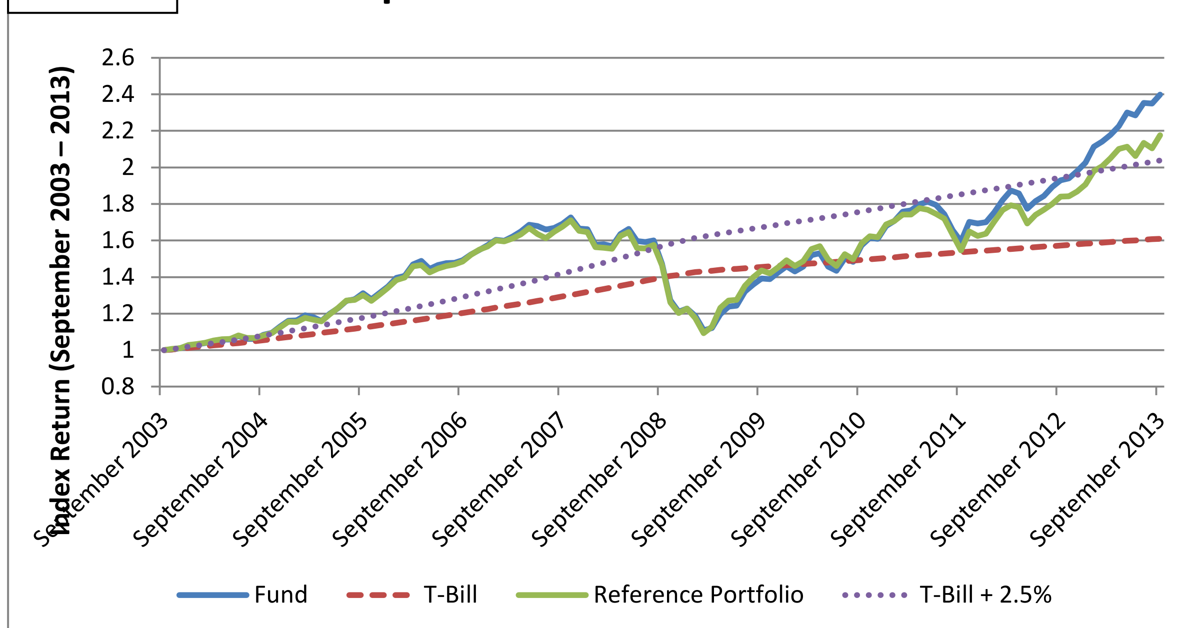
A 20+ year period is generally long enough to reap the rewards of taking on ownership (equity) risk as an investor. The rewards to owners of capital will generally outperform those of lenders (debt providers), as long as they are patient and responsible investors. This is a long time to wait however for most people, which is why the patience of the few (such as us) can be even better rewarded due to the impatience of the many.

The long-term returns' evidence can be seen looking back in economic history (subject of course to the pitfalls of looking at one draw of history). Since 1926 the returns to investors in the US equity market outperformed the US government borrowing rate (US Treasury bills) in every consecutive 20-year period, and the US borrowing rate by over 2.5 percent around 90% of the time.[2]

These historical return examples sit at the foundation of our investment structure that includes a clear investment horizon, a well diversified global portfolio, and investing disciplines to stay the course and take advantage of volatile times. For those interested, our Annual Report highlights in full our Fund construction and subsequent expected returns, annual volatility, and likely short-term gains and losses in extreme positive and negative market events.

During our first 10 years of investing we have had our return expectations sorely tested but vindicated. Despite an initial set-up phase, and then having the proverbial kitchen sink thrown at us in the GFC, our returns have remained well within the 'confidence intervals' we established initially.

[2] For further information see a discussion paper prepared by the Guardians at the request of the Commission for Financial Literacy and Retirement Income, April 2013.



Source: http://www.nzsuperfund.co.nz

During our first 10 years we have averaged a 9.13 percent annual return on our investments. This is 4.26% percent ahead of the risk-free rate of return - i.e. it's nearly double the cost of government debt[3].

In NZ dollar terms, the Fund is currently $24 billion, of which nearly $15 billion was from Crown capital contributions. We have also paid New Zealand tax of $3.3 billion. This table outlines our returns history and compares this to the risk-free rate of return and our own passive index 'benchmark', that is our Reference Portfolio.

Figure 2

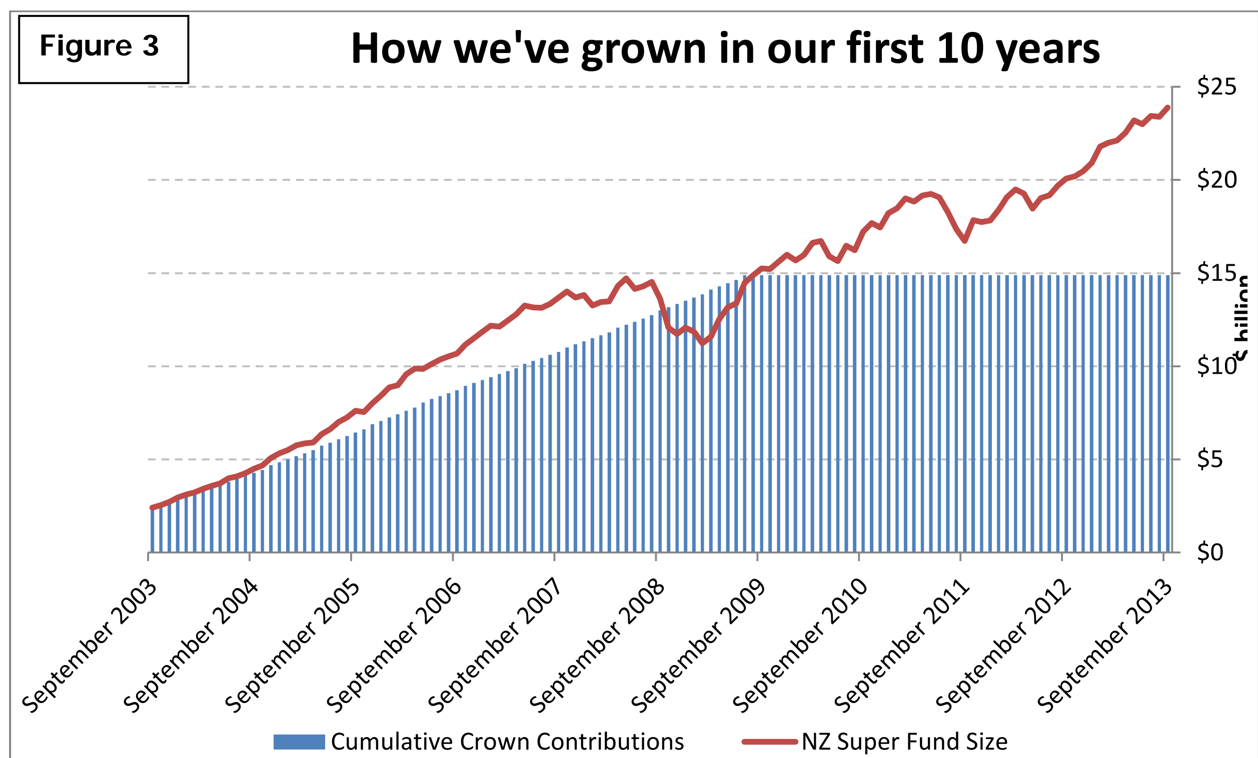
10 Years of Investing 30 September 2003 -2013		**Fund size: NZ$23.93 billion before NZ tax**		
Returns	**1 year**	**3 years**	**5 years**	**10 years**
Actual Fund Returns (before tax, after costs)	24.33%	15.08%	10.25%	9.13%
Value added by Guardians (compared to Reference Portfolio)	6.02% $1,173m	3.91% $2,464m	2.01% $1,828m	1.06% $2,220m
Net Return (returns over and above the Treasury Bill return – the Government's cost of debt)	21.95% $4,290m	12.55% $7,277m	7.38% $7,394m	4.26% $6,961m

[3] As measured by 90 day Treasury Bills.

The 10-year period averages of course mask much of the excitement of the month-to-month and year-to-year volatility a growth-oriented fund like ours experiences. As we have warned many audiences – 'kids, please don't try this at home'.

For example, the Fund lost 29.84% in the 12 months to February 2009, the depths of the GFC. The Fund troughed at $11 billion in size. Amidst this global uncertainty, Crown capital contributions were halted to the Fund as the Government turned its priority to gross government debt reduction. On the GFC itself, the news headlines from experts (mostly of the hindsight variety) were extreme – generally relating to some variant on the claim 'this time it is different'.

Fortunately, given our clear investment purpose and institutionalised long-term investment practices, the Fund benefited significantly over the years following the GFC. We have grown rapidly, returning 18.3% per annum since the trough.



Source: http://www.nzsuperfund.co.nz

We made these returns by taking advantage of global asset prices which we assessed were depressed relative to our view of their medium-term value. When you invest on that basis, you do so with the expectation that future returns will be high. Those expectations were met.

One myth we often hear that I would like to rebut is 'it doesn't make sense to borrow to invest'. Sure, for individual families with mortgages, career risk, health risk and the need to access cash for day-to-day requirements, it might not make sense. But for a long-term,

diversified and sovereign-backed investor like the Super Fund with our liquidity and horizon, long-run investment returns can and have comfortably exceeded the cost of capital.

Importantly, however, our appetite for risk – and hence returns – remained stable throughout this 10 year period. Such investment behavior is in part captured by 'rebalancing' our risk exposures to ensure we retain the targeted level of risk. For example if we want to retain at least 70% of our Fund invested in global equities, then as the value of these equities fall with a mark-to-market price decline, we will buy more (and vice versa).

However, we also introduced new contrarian investment strategies, including 'strategic tilting', selling rather than buying insurance, and being more opportunistic in direct investing when there is a clear gap between the current price and an asset's long-term value. In these simple ways we joined a minority group of disciplined 'contrarian investors'.

It is important to note that we did not purport to forecast the equity market trough. We do not believe this is possible nor a worthy exercise, as too often it leads to pro-cyclical investment behavior and missed opportunities. We simply stood firm on our horizon and liquidity, and our investment beliefs. This is the role of a long-term investor.

Again, I thank our legislation, our Board, and our wise investment staff who counseled me (and each other) throughout these exciting investment times. Suffice to say, we are now match fit, but do not take anything for granted.

An enormous amount of the Board and staff's time at the Guardians is spent discussing our robustness to financial volatility and how we can gain from the shorter-term fads, fashions, and pro-cyclical investment strategies that dominate the global financial environment.

What are Sovereign Wealth Funds (SWFs)?

Despite their supposedly 'mysterious beginnings', SWFs are simply pools of nationally-owned financial assets that are being managed (invested) for specific economic purposes. These economic purposes generally fall into one of three camps:

- Reserve funds established to retain wealth for current and future generations funded on a current – once in a generation - commodity windfall e.g. oil and gas royalties. Such funds exist in the Middle East, Norway, Azerbaijan, Nigeria, and closer to home in Timor-Leste, and soon Papua New Guinea;
- Specific purpose 'buffer funds' that are saving now for a specific purpose in the future. The savings may come from either commodity windfalls or out of the current tax base of a country. The NZ Super Fund is one of these funds. We have no explicit liability, but we have a specific purpose for our development i.e., to smooth the future tax burden of providing retirement income because of New Zealand's ageing demographic profile.[4]; or
- Stabilisation funds that are established to assist balancing short-term fiscal positions for a government. These SWFs are found in Russia, Botswana and elsewhere, and are often

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[4] For further detail see www.nzsuperfund.co.nz, in particular our April 2013 discussion paper on the role and performance of the Fund, developed at the request of Commission for Financial Literacy and Retirement Income.

an additional policy tool for meeting government payments and foreign exchange commitments in countries with less developed capital markets and/or pegged currencies.

The first two SWF types – the long-term wealth smoothing and long-term tax smoothing – provide most opportunity (and concern) globally for increased economic integration, inter-generational wealth sharing, capital market development and financial stability, and the promotion of 'responsible investment' practices.

'I work for a Sovereign Wealth Fund and am proud of it'.

There you go, I have said it. Only seven years ago I would have been far less proud to be associated as a SWF employee, that is if I had believed the global headlines and some recipient country concerns as to the purpose of these SWFs - 'barbarians at the gate coming to buy our strategic assets'.

Since then two important things have happened. One is the onset of the GFC, where SWFs suddenly became in great demand for their long-term capital for all sorts of industries in most countries. Second, there has been far more knowledge and understanding created between host and recipient nations of SWF capital.

In large part this has been assisted by the voluntary development of the 'Santiago Principles for Generally Agreed Practices and Principles' to SWF investment behavior. These published principles are championed and overseen by the International Forum of Sovereign Wealth Funds, members of which are expected to implement the Principles to the maximum extent possible.

The Guardians played a significant role in the development of the Principles, along with our peer SWFs, the IMF, OECD and other international financial organisations. We implement all of the principles that are relevant to us, and are transparent in doing so. As Deputy Chair (and in two years Chair) I also have a governance role in IFSWF, and look forward to see it grow in importance globally.

The essence of the Principles is that it is critical that SWFs are run for long-term economic purposes, with appropriate governance and investment disciplines. Why? Because it is very difficult for a current population to put wealth aside collectively for future generations.

First, it is naturally human to want 'instant gratification' and enjoy the wealth, or consume, now.

Second, future generations don't get to vote for current governments, meaning their voice is never heard. This is especially so when the capital being saved is from the current tax take - such as the NZ Super Fund - rather than some very obvious commodity boom.

Even in the latter case few countries have managed in economic history to retain 'commodity wealth' inter-generationally. Too often it has been spent by the current population (such as in part Australia), or handed out as immediate tax cuts (such as in the UK in the 1980s), or owned by a minority in countries with less robust institutional structures.

Time inconsistency, myopia, asymmetry of information, and principal-agent risks are all well understood economic concepts that drive inappropriate risk taking and rent seeking. For example, not saving now to meet a known demographic challenge implicitly assumes that it will be safer to meet that challenge by borrowing at some future unknown date and interest rate. Or, it explicitly assumes the challenge will no longer exist or that we will have decided *not* to meet it.

In short, inter-generational fairness and long-term investing are very difficult concepts to hard wire into the political economy of a society.

Even in a society with strong and sound institutions such as New Zealand, retaining consistency of policy through time is tough.

What makes a long-term investor and why do they matter?

A genuine long-term investor is an investor who has 'captured' capital and is able to do what they need to with it, to best achieve their investment purpose. The New Zealand Super Fund, and many of our peer funds and other SWFs, are long-term investors.

Capital can be 'captured', as in the case of the NZ Super Fund, through establishing an investment mandate and series of practices and principles that provide investor control. The Santiago Principles go a long way to describing the 'necessary' but not 'sufficient' tools to achieve this. The NZ Super Fund – by design – is a long-term investor. It is also one of our investment beliefs that truly long-term investors can create superior returns – they have an edge if they use this opportunity correctly.

Specifically, long-term investors can ride out much of the shorter-term volatility in financial market prices (i.e., risk premia) and not be forced to sell assets when their holdings are worth the least. Quite the opposite in fact. A long-term investor should have a much more stable 'risk appetite' and actually profit during periods of extreme risk aversion or outright panic.

The NZ Super Fund has demonstrated the ability to maintain a constant risk appetite through clarity of our passive Reference Portfolio which highlights our 'equilibrium' risk appetite, and our ability to rebalance during periods of volatility and invest in a contrarian manner when extreme risk aversion is evident in asset prices.

A long term investor can also pursue more illiquid investment opportunities, with the knowledge they have time to implement investment plans and reap the returns in time to make any future payments. Importantly, they should not be forced to sell when it is not in their interest, they can hold an asset as long as it remains sensible for them to do so.

Again, the NZ Super Fund has demonstrated our ability to take on illiquid investments with long return horizons, with the confidence we have bought into the asset at a good price and will be paid a deserved 'illiquidity premium' by owning assets more short-term investors can not manage. These assets can be readily observed in our portfolio, including our stakes in Kaingaroa, Z Energy and Datacom.

Importantly, long-term investors are not driven by reputational or career concerns derived from - irrelevant - short-term return comparisons. Instead, we have remained focused on achieving our goal and have ensured we can invest opportunistically as risk premiums fluctuate.

For example, over our short ten-year life, we have shown our capability to 'sell' insurance when other investors have not been able to manage volatility, as well as weather large positive and negative short-term deviations from our return expectations as we have increased/reduced our risk exposures as asset prices have fallen/risen. This has been demonstrated by our investments in catastrophe reinsurance, life settlements, and a variety of arbitrage strategies we have engaged in when managing our own liquidity. All of these strategies simply leverage our stable risk appetite, our investment horizon, our liquidity, and our governance and decision making capability.

As an outcome, I believe the NZ Super Fund, and other like-minded long-term investors, have provided superior risk-adjusted returns to our owners, and in doing so provided increased stability to global financial markets.

To hammer home this point, consider the alternative.

The Guardians could have chosen not to utilise the full benefits of our operational independence and investment mandate. In doing so, we could have chosen a path of less overall financial risk exposure (and by definition, lower long-term investment returns) than our growth oriented Reference Portfolio.

Likewise, we could have chosen to simply invest passively, and not look to increase our returns by exploiting an illiquidity risk premium, or investing in a contrarian manner, or actively investing outside of our Reference Portfolio at all.

Such an investment approach may have made the ride smoother for current and past Board members and staff. Sitting in risk-free government bonds, or selling equity as the global share markets declined, or hugging a benchmark we can later blame, all make for quieter life as a fund manager in the short-term.

This is especially so when investing in the deliberately transparent 'gold fish bowl' called the NZ Super Fund - with our monthly, quarterly, and annual reporting; our relative lack of local long-term investor comparisons and our Official Information Act obligations.

Believe me, there is plenty of confusing academic literature, specific time series, dramatic news headlines from experts, skeptics and vested interests, and misaligned managers to justify any investment behavior at some point in time. How else could the investment industry have grown into the heterogeneous, expensive, and jargon-filled industry it is?

In fact, the two biggest mistakes investors fall into are:

- pro-cyclical investments – selling when prices are falling and vice versa – and;
- misalignments between the managers of the investments and the owners of the capital i.e., concern for management fees and performance bonuses over and above the owner's interests.

These two factors alone help explain a considerable proportion of the turmoil we have seen in global capital markets over the last decade.

The IMF recently produced research on the pro-cyclical behavior of institutional investors, and sheeted home many of the capital market failures to 'institutional herding'.[5] They spend a considerable effort in highlighting how, as the recent GFC intensified, concerns about so-called capital preservation rose, and several institutional investor types abandoned their long-term investment strategies, reduced risk exposures, switched to supposedly safer assets, all with the intention of switching back at some later date.

Having lived through this experience ourselves, I can assure the audience that, first, markets had already plummeted in price before the decision-making capability of most institutions could have reacted, hence investors were selling pro-cyclically, locking in losses. Second, the residual fear in the market and 'blame-storming' amongst Boards, meant that many investors did not get back into 'risk assets' until well after the global recovery in asset prices was well underway.

The net outcome is that this 'institutional herding' destroyed wealth, increased financial market volatility, and led to the demise of many sensible long-term investment strategies.

Giving in to what may appear easier to explain in the short-term is a trap that significant swathes of the global investment community fall into. Fortunately for some, these two oft-repeated mistakes increase the competitive advantage of truly long-term investors.

This is why the Guardians have consciously chosen the active, opportunistic, long-term investment path. We certainly will not be guilty of underutilizing our investment mandate and endowments, nor will we bend our risk appetite to suit the current state of investor paranoia.

I am proud to be able to say that the past and present Board of the Guardians have consistently chosen not to be driven by short-term career concerns, and instead have chosen a set of investment beliefs that best leverage our mandate and our endowments.

I strongly believe the Guardians have chosen to measure the right things so that the right things can be managed. It is almost for this reason alone we are recognized globally as a leader in long-term investing, especially amongst Sovereign Wealth Funds.

What are the right things to measure for a long-term investor, and what have we measured?

There is no shortage of sound investment advice ex-ante. The difficult challenge is engineering its implementation, and having the discipline to review and learn from them over the right horizon.

The authors of the previously mentioned IMF paper advocate a framework that is designed to assist long-term institutional investors set up their investment policies so as to avoid the pro-cyclical behaviours and wealth destruction.

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[5] Reference IMF working paper 13/93

Their recipe is focused mainly on prevention and hence in the skeptical mind of this speaker will not be adopted very often. The recipe includes: forward-looking deliberate asset allocation, portfolio rebalancing, sound governance, and appropriate incentives for investment managers.

None of this is new and, no doubt, little of it will be adopted by the vast majority, since it is not fun and involves perceived career risk. It also means piercing the veil of the vested interest and asymmetric information advantages that define large parts of the investment management universe. Suffice to say, asset price and business cycles are here to stay for a long-time yet.

How has the NZSF engineered long-term investing behavior?

Future governments will begin to withdraw money from the Fund to help pay for New Zealand Superannuation from around 2030 based on current NZ Treasury forecasts. Even once withdrawals begin, the Fund is not projected to peak in size until the 2080s.

We deliberately leverage our endowments – our long-term horizon, certain cash flow, limited need for liquidity - to invest in growth assets. These endowments also allow us to invest in illiquid assets – for example, forests, infrastructure and private (unlisted) companies.

We also utilise to the full our enabling legislation that provides us operational independence and a wide investment spectrum. This provides us confidence to enter into investment arrangements that best suit the Fund's long-term purpose, with minimum so-called 'agency risk' i.e., that our owner may suddenly decide to 'pull up stumps' and force us into unanticipated liquidity situations and fire sales.

Our sovereign status is also beneficial, both in terms of our sovereign tax status in many countries, and the potential to be regarded favourably by some business partners at home and abroad.

Hence, we have deliberately thought about our purpose, who we are, and what events or investments we should be involved in that will best enable us superior returns. In doing this, we have to be honest with ourselves – what will we not do – and humble – this is a competitive industry and it is better to rely on our endowments than on our skills as investors.

Our shared investment beliefs is what gives us the confidence to choose specific investment strategies. These beliefs are the underpinning to our selection of investment strategies. Long-term and contrarian investing means we will have to allocate capital often in times of considerable uncertainty, because these are the times when expected returns, even after adjusting for the high risk, are the most attractive. The anchoring of our investment strategies to our endowments and investment beliefs enables us to stay true to our stated investment course, often when it feels the most unnatural.

I challenge everyone in the audience, once you're back in the office to, put on one sheet of paper – your purpose; endowments; beliefs; strategies; and capabilities. You should be able to fit it on one piece of paper if you have honestly thought about them. That A4 piece of

paper should be the same if I asked any member of your team or Board. It should be shared in ownership, and understood in implication and communication.

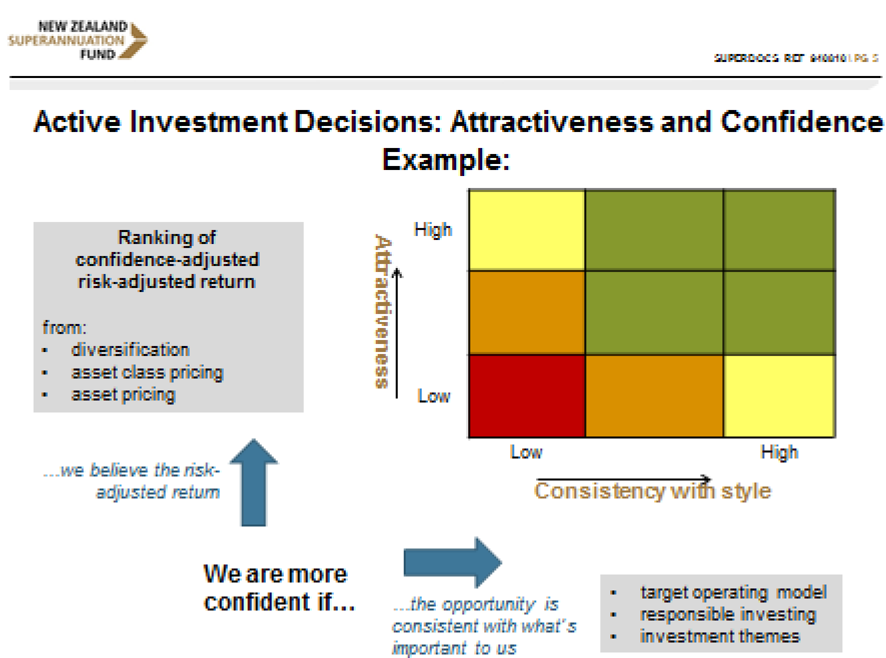
Every investment strategy the Guardians enter into is anchored to our endowments, rests on our beliefs, and we have sufficient capability – internally and externally – to manage it on a sustainable basis. When the GFC hit us, we were able to quickly debate – has our belief been challenged (e.g., markets will not normalise?); is our strategy correct (e.g., buy more when expected returns rise?); and do we have the capability to manage day-to-day financial operations in an unprecedented credit environment.

The clarity of this conversation led to our confidence to stay the course. Many of peers did not, and some no longer exist due to a lack of operational independence or governance clarity. Wealth was destroyed permanently.

We now, every six months, rank all of our investment strategies on a single 2x2 matrix of:

- Our confidence in each strategy's relative financial attractiveness;
- Each strategy's consistency with our endowments, beliefs, targeted operating capabilities, and responsible investment commitments.

Figure 4



Underlying this comparison is a common language and set of metrics on *financial attractiveness* (expected risk adjusted returns over the relevant horizon) and *consistency* with our investment beliefs (e.g. in responsible investment) and target operating model. We can then assess how much capital sits in the hot spot, and what we need to do with the rest to improve the Fund. We can also assess whether we are spending our efforts and energy in the right spots.

This simple capability is largely what has put us at the forefront of investment innovation amongst the SWFs. We have a single fund view for what will be the best investment for the Fund.

To be able to work together like this – as a single fund – is very different to most global funds that have clear asset allocations, that lead to capital allocations, that can lead to 'bucket filling' and significant remuneration complexity as each asset class expert demands a specific slice.

Instead, we have chosen the deliberate 'great team' culture to focus on the 'best portfolio'.

Our investment teams are incentivized and remunerated on how much 'value we add' relative to our Reference Portfolio (over a four-year moving average period). This is partly why we chose the simplicity of a Reference Portfolio – simple, passive, listed – over a more elaborate Strategic Asset Allocation. The latter is a mixture of passive and active investment decisions, which can blur ownership of the risk, and mask active investments that may not make economic sense. Each investment strategy has its expected return goal, net of all costs, over a relevant time horizon. It is there for all to see in our Annual Reports.

The Board own the Reference Portfolio and management implement this, as well as try to add value through our active strategies. Our Actual Portfolio is the combination of these activities. Management has a clear vested interest in only actively adding things to the Fund that will make it perform better for all, not just some.

It is almost sad to have to spell this out as an innovation. But there sits human nature. Give me my asset class, my hurdle, and my capital - now leave me alone. This approach can lead to a good asset class outcome, but it does not guarantee a good Fund outcome. It also does not assist in the ability to attract and retain the culture and talent the NZ Super Fund needs.

Finally, I have only mentioned the phrase once in passing so far – responsible investment. This is investing with concern for environmental, social, and governance (ESG) outcomes. As a long-term investor, as a SWF, and as a Guardian of NZ Superannuation, we must be committed to responsible investing. We can not ignore it, and we do take it seriously.

Our investment mandate, amongst other things, says we must… *avoid prejudice to New Zealand's reputation in the international community*.

We do not undertake responsible investing out of altruistic kindness, or purely because we are legislated to have concern. Rather, we do it because ESG issues sit firmly amongst our investment beliefs, and hence assist in underpinning our *confidence* in expected returns and *consistency* with our preferred operating style and beliefs. ESG has become part of our DNA, and again we have been recognised globally for our approach.

We believe, in establishing our investment strategies:

- Responsible asset owners who exercise best-practice portfolio management should have concern for environmental, social, and governance (ESG) issues of companies; and
- Improving ESG factors can improve the long-term financial performance of a company.

The economic benefits will come home to us directly through more consumer support of the businesses we invest in, less legal and regulatory risk, more dynamic companies, potential excess returns from investing early in the life cycle of assets, less conflict between the owners of the assets and the asset managers, and potentially leveraging our long-term investor horizon to exploit long-term trends such as resource sustainability.

As a result we have actively integrated responsible investment practices into our investment opportunity analysis and asset selection; we have made a commitment to engagement with companies in order to use our influence as a shareholder positively, and we aim to show leadership – regionally – to improve corporate governance, public reporting and overall awareness of the importance of factoring ESG concerns into investment management.[6]

We are very transparent on our responsible investment standards and practices, and will continue to aspire to lead in this area for the better of the Fund, New Zealand's reputation globally, and the wider economic environment.

To sum up – what are the secrets of the successes we have enjoyed?

Clarity of purpose, discipline to stick to it, right people to deliver it on a repeatable basis, and a frank and unapologetic approach to continuously communicating where we're headed, why and how we're making progress.

I have used a lot of numbers to support my view of the Fund and of the people working for it as long-term investors. I will leave you with just a few more which show our perspective probably better than any other. On current Treasury policy settings and projections, the Fund will begin paying out when today's 47 year olds are 65. It will hit NZD500 billion when today's three-year-olds are 65; and its size as a percentage of GDP will peak, at 34%, in 2080 – when I will be 117.

We look forward to the next 10 years, and our first '20+ year' checkpoint.

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[6] For further information see www.nzsuperfund.co.nz, in particular our Responsible Investment Framework.