HAWKE'S BAY FOUNDATION

Hawke's Bay Foundation Statement of Investment Policies and Objectives

Adopted: 1 April 2020

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Statement of investment policies and objectives

This statement summarises the investment policies of the Trustees. It is the intention of the Trustees to review and update, as appropriate, the policies to reflect the changing investment markets, Foundation characteristics and the Trustees' requirements.

The statement is set out as follows:

History

Version	Adopted	Comment
1.0	28 October 2014	Initial Sipo
2.0	9 April 2019	General update & strengthening of RI policy
2.1	1 April 2020	General update

1. Introduction

1.1 Background

The Foundation is registered as a charity with the Charities Commission.

The Foundation is a community foundation with the underlying principle that responsibility begins at the local level. It provides a vehicle for individuals, families, companies and groups to endow local community causes and organisations. It also acts as an investment vehicle for other charities and organisations.

Donations and legacies given to the Foundation will be invested in perpetuity with income being distributed to the designated causes and organisations and, as appropriate, the wider community.

Where other charities and organisations use the Foundation as an investment vehicle, the Trustees will determine whether:

- The assets of the charity will be invested as part of the Foundation's standard assets and receive the earning rate of those assets.
- The assets of the charity will be subject to the "short-term income strategy" as detailed under the short-term income strategy attachment.
- The assets of the charity will be subject to the "long-term growth strategy" as detailed under the long-term growth strategy attachment.

The Trustees can also determine that the assets will be split between 2 or more of the above options.

1.2 Capital base

In terms of the assets of the Foundation, the "capital base" will include the capital donated and gifted to the Foundation that is not for immediate distribution.

The capital base figure will be adjusted each year by an amount to calculate the equivalent real value to allow for the effects of the CPI inflation rate. The objective is to build and maintain assets above this level.

1.3 Current assets

The Foundation is a new community foundation and is expected to grow overtime. The initial target is to build a capital base of $10m over the first ten years.

1.4 Taxation

The Foundation's investment income is subject to normal taxation rules for charitable Foundations. Therefore, the Foundation does not expect to pay income tax on the investment income earned on the assets. This is important for investments that are taxed at source, for example New Zealand shares, where the imputation credits associated with dividends do not boost the return to the Foundation.

The balance date of the Foundation is 31 December.

1.5 **Primary objectives**

The primary objectives underlying the investment policies for the Foundation are:

- to ensure that the assets of the Foundation are invested prudently, consistent with the Foundation's purposes;
- to maintain the value of the assets above the Foundation's capital base and to grow such value at such level above the inflation rate as determined by the Trustees;
- to ensure that money is available for distribution, as required, to meet the granting policies; and
- to maximise the funds available for distribution over the long-term.

1.6 The primary objectives translate into investment objectives of:

(a) to generate income from the investment of the assets consistent with the intended short-term distributions.

(b) subject to (a), to maximise the return available to support the work of the Foundation, both in the long and short-term;

(c) to grow the assets of the Foundation, over the medium-term (5 to 10 years);

(d) within (c), to maximise the long-term value of the assets in real terms.

1.7 **Investment beliefs**

The investment beliefs of the Trustees that have determined the investment policies for the Foundation are summarised in appendix A.

1.8 **Income requirements/grants policy**

The initial grants policy of the Foundation is to target distributions each year at 4.0% of the capital base, subject to a minimum of 3.0%, at the start of the year.

The targeted level of distributions will be reviewed from time to time, as market conditions vary, the priorities of the Foundation change and opportunities to meet the Foundation's purpose arise.

1.9 **Smoothing policy**

The Trustees recognise the risks associated with fluctuations in the underlying values of the different investments. Accordingly, the Trustees will operate a policy to smooth out the impact of temporary short-term asset value fluctuations, on the year-by-year distributions. The smoothing policy forms part of the Trustees' risk management policies. The current smoothing policy is set out in section 5.

1.10 **Non-traditional investments**

The Foundation may, with the prior unanimous approval of the Trustees, invest in assets outside the traditional asset classes of cash/bank deposits, bonds, property and listed shares. Such assets may include private equity, venture capital and special opportunity investments.

1.11 Management

The responsibility for the oversight of the Trustees' investment policies shall be that of the Trustees' Investment Committee and the investment consultant. Initially, all Trustees will be on the Investment Committee.

The Investment Committee's role includes:

- implementing the Trustees' investment policies;
- liaison with the Foundation's investment consultant;
- advising the Trustees of required changes or issues regarding the Foundation's assets;
- reporting to the Trustees on the performance of the Foundation's assets on a basis agreed with the Trustees.

1.12 Responsible investment policy

The Trustees recognise that they have a fiduciary responsibility to seek to maximise the investment returns on the Foundation's assets, subject to appropriate risk constraints. As a general policy, the Foundation will not invest in any entity or product where it is expected that in doing so would have a significant detrimental impact on the Foundation's investment reputation.

The Trustees acknowledge that they are acting as trustees for beneficiaries of Hawke's Bay Foundation, being the community within the boundaries of our region, and therefore should always endeavour to ensure the funds of the Foundation are invested in a manner that is consistent with the values of the community.

In this context, the Trustees recognise that there may be some circumstances in which it is appropriate to consider exclusions of a sector or a specific stock. In particular, the Trustees expect any appointed manager to avoid investing in any company whose activities would be deemed to be unlawful under New Zealand law, notwithstanding that the investment might be domiciled in another country.

2. Performance objectives

2.1 Return requirements

The return requirements of the Trustees are to achieve:

Long term (20+ years)

- a real return after investment and other expenses, on average, of at least 3.0% per annum, and

Short term

- an income cash flow return, of 4.0% of the capital base each financial year.
- a total return that is positive over the short-term (2 to 3 years).

2.2 Risk profile

The risk profile of the investment strategy of the Foundation will be set to maximise the long-term return within the context of the market environment and risk levels to look to achieve:

- to achieve the long-term objective with 99% confidence (i.e. the rate of failure to meet objectives is 1 long-term period in 100 such periods), and

- to achieve an actual 4% income-return over the short-term (1 year) with 95% confidence (i.e. the risk of failure to meet the short-term objective is 1 period in 20) such periods,

and to

- maintain liquidity equal to 5% of the capital base.

2.3 Special strategies

The Trustees also operate two special strategies:

Strategy	**Objective**
Short-term income	To maximise the income available for distribution over the next 12 months while minimising, to the extent possible, the risk of capital loss (negative market movement).
Long-term growth	To capture the long-term return available from a diversified portfolio of share and property assets.

Details of the strategies and policies of the above policies are set out in the attachments.

3. Investment strategy

3.1 Given the objectives and nature of the Foundation, the assets will be invested based on the following long-term benchmark allocation and will generally be maintained within the ranges indicated. The benchmark and ranges will be reviewed as circumstances change and will be reassessed as appropriate. The next review is due on or prior to 30 June 2021.

Long-term investment strategy		
Asset class	**Benchmark allocation**	**Allowable range**
Liquidity Cash	5.0%	0% - 15%
Income Cash/bonds	15.0%	0% - 50%
Growth Property/shares	80.0%	35% - 90%

3.2 In respect of the above strategy, subject to the prudential investment guidelines set out in section 4 and the risk management policy in section 5, it is noted:

- current assets, equal to any grants approved but not paid, will be held in cash or fixed interest, as appropriate, outside the above investment strategy.
- it is intended that the assets will be managed relative to the benchmark with appropriate rebalancing back to benchmark as required, in the context of the risk management policy.
- shares and property will initially focus on the Australasia markets and the Trustees will only look to diversify into the wider overseas markets when the capital base is above $5m.
- the NZ bond, property and share assets, and Australian share assets will be managed on predominately a “buy and hold” basis. The long-term aim is to construct portfolios of 15 to 25 shares which will be generally “equally” weighted, and 10 to 20 corporate bonds.
- the NZ bond assets will focus on investment grade corporate debt.
- until the exposure to overseas shares is above $5m and 25% of the assets, the risks arising from currency movements on overseas shares shall be unhedged. Prior to the exposure to overseas shares reaching $5m and 25% of the assets a formal currency hedging management policy will be developed.
- the risks arising from currency associated with overseas bond investments, if any, shall normally be fully hedged. This will mean that it will be managed within a hedging range of 95% to 105%.
- the property assets will be a combination of listed securities in the NZ and Australian markets together with direct property investments as appropriate.

4. Investment guidelines and requirements

4.1 The following investment guidelines and requirements have been set for prudential reasons to ensure there is an adequate level of security in the investments. They relate to the day-to-day management of the assets and in each case can be deviated from, as appropriate, by a unanimous decision of the Trustees.

4.2 **Shares**

- Investments must be confined to publicly listed, widely-held securities trading in recognised markets. For clarification, in New Zealand and Australia this would mean securities listed on the "main boards" of the NZ or Australian Stock Exchanges.

- Except where there is a clear strategic advantage, the Foundation should not hold more than 5% of the equity of any one company and no direct holding in a single company should equate to over 5% of the market value of the Foundation's assets.

4.3 **Property**

- Direct property investments may only be made with the unanimous consent of the Trustees.

4.4 **Bonds**

- Bond investments are not limited to government guaranteed investments and in New Zealand should focus on non-government guaranteed securities where appropriate.

- The overall average credit grade of the portfolio should be equivalent to at least a Standard & Poors BBB credit rating.

- When a bond is not formally rated by Standard & Poors, the level of security must be assessed by two brokers/consultants to have a level of security equal to the relevant investment grade rating. All such security holdings must be notified to the Trustees.

- No holding of a single government issue should exceed 10% of the market value of the Foundation's assets.

- No holding in a single non-government entity should exceed 3% of the market value of the Foundations' assets.

4.5 **Cash**

- Cash and cash equivalent investments, with a maximum duration of 365 days, shall be invested with organisations with a level of security equal to, or better than, a Standard & Poors A1 rating or a Moody's P1 rating.

4.6 **Currency**

- Where risks arising from currency associated with overseas investments where managed will be managed by 90-day forward currency hedging contracts.

4.7 General

- All investments must be prudent investments and shall be made in accordance with the requirements of the applicable legislation.

- No constraints are placed on an appointed manager's ability to raise cash for the management of short-term cash flow transactions that relate to the Foundation, provided that borrowing for this purpose in any investment sector may not without the approval of the Trustees:

  - Exceed 5% of the market value of the assets of that sector held by that manager,

  - Be for a period greater than one week.

- Borrowing for other purposes is prohibited.

- Investments in assets other than those contemplated by this policy statement are not permitted.

- Total holdings (bonds and shares) in any one organisation, other than government bonds, shall not exceed 7.5% of the market value of the Foundation's assets.

- Futures and options may be used for the prudential investment management of the Foundation's assets, provided that such investments are not used for gearing purposes.

4.8 Pooled investments

Where the Trustees determine that an appropriate investment vehicle is a pooled investment arrangement, they recognise that the strict application of the investment guidelines and requirements may not be possible or be in the overall best interests of the Foundation. Where a pooled vehicle is used, the manager of the pooled arrangement shall be required to disclose to the Trustees, as soon as practicable, details of any investment that materially falls outside the guidelines and requirements so that the Trustees, can continually reassess the overall suitability of such an investment vehicle.

5. Risk management and asset allocation

5.1 It is noted that the Foundation's assets are exposed to different investment risks that will lead to variations in the actual short-term return versus expected average return. To reduce the potential negative effects of these risks on the Foundation's distribution policies, the Trustees have put in place risk and management policies and principles. Current details of the risks and management policies and principles are set out in appendix B.

5.2 In addition, the following policies apply:

- The Trustees meet regularly and investment performance and investment outlook is a specific agenda item where appropriate;
- A comprehensive investment reporting process applies;
- An independent investment consultant is used;
- Professional investment managers are used, where appropriate;
- The strategic investment policies are subject to a three-yearly review;
- The movement of money between managers and investments requires two authorised signatures.

5.3 The risk management policies will be reviewed from time to time in light of the Foundation's overall strategies, to confirm their ongoing appropriateness.

Asset allocation policy (AA policy)

5.4 The purpose of the AA policy is to identify times and events when the Trustees should instigate a discussion process to potentially adopt a short-term departure from the standard benchmark investment strategy. The outcome of the review is to identify actions, if any, that will help protect the ability of the Foundation to maintain its distribution policy over the short and long term, given the market environment and outlook. The focus is not to "second guess" the markets solely to enhance the return.

5.5 The normal framework for the AA policy review will be for the investment consultant:

- in the first instance to raise with the Foundation Chairman the event or environment that triggered the AA policy review process and discuss the need for a "special meeting" of the Trustees. Where it is decided such a meeting is required, the normal procedures for that meeting will take over;
- to collate the information, if any, required by the Trustees to assist them formulate recommendations as to what action may be required to be taken;
- to instigate such action.

5.6 It is recognised that the scenarios that will arise where action will need to be taken, will be unusual. Where actions are required, they will be tailored to the specific circumstances. The Trustees will set from time to time "triggers" that will potentially lead to a AA policy review. Details of the current triggers are set out in appendix B.

5.7 The investment monitoring and reporting will include analysis that captures the performance relative to the hurdles.

Currency management policy

5.8 As part of the Foundation's risk management policy, where the Foundation invests in markets outside Australasia, the Trustees operate a currency management policy. Details of the current currency policy are set out in appendix B.

Smoothing policy

5.9 The Trustees recognise that the Foundation's investment policies contemplate an asset allocation across market areas which are likely to demonstrate short-term volatility from time to time. Accordingly, to help protect the "capital base" from these fluctuations, the Trustees will seek to build and then maintain a level of assets over and above the "capital base". The Foundation will seek to build and maintain an "optimal level" of assets that is 20% above the "capital base".

5.10 Each year the Trustees will review the current level of assets relative to the capital base:

- Where at any time the assets are below the level of the capital base of the Foundation (measured at the end of the previous year) specific advice will be taken on the investment outlook to determine what, if any, action needs to be taken in terms of either the investment strategy or the distribution policy to protect the capital base.
- Where, at the end of a financial year, the assets exceed the capital base by 25% or more, then such surplus shall be taken into account by the Trustees in applying their distribution policy or in building up the capital base by more than CPI.

6. Monitoring and review

6.1 The overall performance of the Foundation will be evaluated on an ongoing basis in terms of return and volatility against:

- the Foundation's overall performance objectives, as identified in section 2, and
- the return, after expenses, of a portfolio with the benchmark asset allocation invested in the market indices used to review the individual asset sector returns.
- the risk-free rate of return as measured by the S&P/NZX Bank Bills 90-Day Index.
- such other objectives as determined by the Trustees from time-to-time.

6.2 The performance of each sector will be evaluated on a return and volatility basis over the period indicated against the return of the appropriate market index.

Sector	Market index#	Evaluation period
Fixed income		
Cash	S&P/NZX Bank Bills 90-Day Index	1 year
Overseas bonds	FTSE World Government Bond Index (hedged)	3 years
NZ bonds	S&P/NZX NZ Government Bond Index	3 years
Shares		
NZ	S&P/NZX 50 Index	5 years
Australian	S&P/ASX 200 (NZD) Index	5 years
Overseas	MSCI appropriately adjusted for hedging	5 years
Property	S&P/NZX All Real Estate Index	5 years

 # Each index will be adjusted for tax slippage as appropriate (e.g. imputation credits) to make the comparison fair.

7. Investment consultant

7.1 Appointment of investment consultant

The Trustees believe that an investment consultant should be appointed to assist the Trustees develop their investment policies, to help evaluate the performance of the Foundation and the investment managers, and to provide strategic research and market information. The investment consultant is MCA NZ Limited. The roles of the investment consultant are set out below.

7.2 The appointed investment consultant, in terms of clause 7.1, shall be responsible to the Trustees for:

- assisting the Trustees review and develop the Foundation's investment policies;
- evaluating the ongoing appropriateness of the long-term investment strategy relative to the investment objectives;
- monitoring the Foundation's progress towards achieving its overall investment objectives over the long term;
- monitoring the investment manager's performance in terms of the Trustees' evaluation policy and the investment managers' mandates;
- advising the Trustees in the way in which the Foundation's assets should be invested given market changes, including legislation changes and trends;
- ensuring that any appointed investment manager manages the assets under their care in terms of the mandate given;
- advising the Trustees on the need for changes to their policies or the implementation of their policies;
- monitoring the Foundation's risk management policy including currency policy;
- providing Trustee education and training as requested.

7.3 Reports

In terms of its responsibilities the investment consultant is expected to provide independent reports:

- as requested:
  - a consolidated report showing asset levels, returns and strategies of the managers.
  - attribution analysis which shows where the Foundation added value for the period, year-to-date and recent history;
  - a risk management report showing the current position of the overseas markets, interest rates and exchange rate;

  - any relevant commentaries from investment managers and consultants in the market.

  - "market intelligence" in terms of changes to the manager that may have an impact on the quality of the future performance.

- as required or requested:

  - reports or letters addressing topical issues and any questions raised by the Trustees.

7.4 Performance evaluation

The investment consultant shall be formally evaluated, as required, by the Trustees in terms of the advice and service given and the suitability of the resources available to continually assist the Trustees. It is expected that such evaluation will occur, in the absence of an earlier specific need, on a five-yearly basis. The first review will be targeted to take place in 2022.

8. Investment managers

8.1 Appointment of investment managers

The Trustees' policy is that external investment professionals ("investment managers") should be appointed to undertake the day-to-day management of the investments for both the domestic and overseas markets.

Where investment managers are appointed, a mandate will document the requirements of the manager in terms of performance evaluation, reporting, and the investment guidelines and requirements appropriate to that manager, within the guidelines of the Trustees as a whole.

No investment manager appointed by the Trustees may:

(a) hold, without prior disclosure to the Trustees, any investment in its own company, its parent or any subsidiary and must disclose any investment in associated companies;

(b) delegate to another investment manager on terms other than in accordance with these guidelines.

Where appropriate, investment managers will be delegated full discretion to exercise all voting rights, including, but not limited to, voting proxies. Investment managers must exercise these voting rights in the best interests of the Foundation.

The Trustees may change investment manager(s) from time-to-time as they see fit at their sole discretion.

8.2 Performance evaluation

Each investment manager's performance will be monitored quarterly and formally evaluated annually against:

(a) the performance objectives set out in the manager's mandate and the evaluation criteria, and

(b) such other objectives as agreed between the Trustees and the investment manager from time-to-time.

8.3 Investment manager reporting

Each investment manager will be required to prepare and submit written and verbal reports as follows:

(a) the reporting requirements as set out in the manager's mandate as appropriate, and

(b) as requested by the Trustees:

- details of the manager's investment management structure, decision making process, investment philosophy, and investment personnel;
- recommendations on the manager's mandate;
- such other information that is required by the Trustees in their day-to-day activities which it is reasonable to ask the manager to provide.

Appendix A – Investment beliefs

The beliefs of the Trustees that underpin the investment policies to achieve the primary objectives include:

1. The long-term return is determined primarily by the investment strategy (mix of cash, bonds, property and shares).
2. The short-term return is primarily driven by market events.
3. Markets are generally efficient.
4. There exists an equity, property and bond risk premium and the risk premium is material. The true risk premium only emerges over the long term.
5. The value of an asset returns to its fair value over time, but actual values may be away from fair values for long periods of time. "Fair" value is driven long-term by fundamentals.
6. You are not rewarded long-term for something that can be diversified away.
7. Some investors have specific and inflexible time frames. It is possible to exploit these.
8. Currency rates are not predictable in the short term. Currency trends around a long-term equilibrium unless there is a fundamental market change.
9. Most managers do not add value after costs and relative to the third-party risk.
10. Differences in returns relative to benchmarks are explained more often by policy and not manager skill and judgement.
11. Managers depend on people. Few managers have a concentration of smart people.
12. Managers will not generally outperform the market in the long term. There are some active managers who may outperform the market in the short term where they have an information advantage and the costs of management and third-party risks do not negate the benefit.
13. The only returns that matter are the after-costs-net-return. Costs matter.
14. We get a better return over time by:
    i. Taking a long-term view
    ii. But being willing to make decisions
    iii. Focusing on managing costs
    iv. Keeping things simple and avoiding complex investments
    v. Managing risks.
15. The alignment of the income and growth with the needs of the Foundation is important.
16. Risk leads to short term volatility. Risk is best managed by diversification. Diversification lowers risk.
17. Illiquidity is a risk that is compensated by the market.
18. Risk and return are related in the long term.
19. Risk factors are not constant over time.

Appendix B - risk management

B.1 Details of the Trustees' risk management policies in respect of the risks noted are:

Type of risk	Definition	Foundation's management policies
Interest rate risk	The risk that the value of a security, particularly a bond, will temporarily decrease in value as a result of a rise in interest rates.	• Bonds are generally held to maturity. Such temporary decreases are therefore unrealised and reversed prior to maturity. • Bond holdings are diversified by maturity date. • The cash levels are set to minimise the potential to be forced to realise a bond to meet distribution needs.
Re-investment risk	The risk that interest, or dividends, received from an investment may not be able to be re-invested in such a way that they earn the same or higher rate of return as the investment that generated them. Also, that at the time an investment matures, interest rates have fallen preventing the capital to be re-invested at the same yield.	• Interest and dividends are generally paid to the Foundation's cash portfolio for distribution, not re-investment, purposes. • Bonds are structured to diversify by duration and minimise the level of investments that mature at any point in time. • New investments can be deferred if interest rates are low.
Default risk	The possibility that an issuer of a bond will fail to make a principal and/or interest payment in a timely manner on the due date.	• Bond investments are restricted to investment grade or better, or their equivalent. • Investments are diversified over a range of companies, industries and maturities. • Exposure to any one issuer is limited. • The reporting requirements require commentary on the potential for default.
Currency risk	The risk that changes in exchange rates will reduce the value of the assets.	• Currency risks from shares are hedged within controlled limits and managed with a currency policy. • Where the outlook is uncertain and negative, currency risks are fully hedged as part of the Foundation's currency policy. • Currency risks from bond investments are fully hedged.

Type of risk	Definition	Foundation policies
Inflation risk	The risk that inflation increases the size of the targeted distributions. The risk that a high level of inflation makes unexpected significant demands for capital base increases.	• Part of the assets are invested in shares that provide a potential hedge against inflation. • Part of the assets are unhedged, this provides a potential hedge against imported inflation.
Market volatility	The risk that the investments will decrease in value with general market movements over the short-term.	• Investments are spread across the asset classes, countries, industries and companies. • Cash holdings are set to limit the need to realise assets and therefore market volatility, does not impact on short-term distributions. • The smoothing policy helps minimise the impact of market volatility on distributions. • Cash holdings are increased as opportunities arise to ensure that assets need not be sold for distributions.
Market downturn risk	The risk that the markets suffer a severe and prolonged period of negative performance.	• Cash and bonds assets are held to ensure that distributions can be maintained short-term. • Share assets are diversified across the economic regions of the world. • Interest and dividends are taken as cash and not automatically reinvested. • The Trustees seek specific independent advice on the market outlook as required but at least annually. • The Trustees have a AA policy in place as part of its Risk Management policy.

Type of risk	Definition	Foundation policies
Manager risk	The risk that the discretionary active decisions of a single manager prove to be wrong or that the manager fails.	• Where discretionary decisions are delegated, a specific mandate documents their application. • The exposure to any single manager is limited. • Assets are always held separate to a manager's own assets and held under Foundation.
Timing risk	The risk that investments are made as the market is about to fall or sold as the markets are about to rise.	• Money is moved into new investments of volatile asset classes over time in multiples typically no more than 5%.

AA policy triggers

B.2 Instances that will trigger a AA policy review process include:

- a rise in global equity markets generally, or the New Zealand or Australian markets specifically, by more than 25% over a 12-month period.
- a fall in global equity markets generally by more than 15% on a rolling year basis or 20% from a peak (in the last 5 years), or more than 10% in a quarter.
- if New Zealand short (90-day) or long (10-year) interest rates rise or fall by more than 1% over a 3-month period.
- if the NZ : US dollar exchange rate moves by more than 15% in a 12 month period, or falls below 60 cents or rises above 90 cents.
- if there is serious concern expressed by any of the Trustees about the outlook of the markets.
- if a significant market opportunity is identified and raised by any of the Trustees.
- such other event as the investment consultant may in its opinion (acting as the investment consultant and in the best interests of the Foundation) consider as an event warranting a short-term asset allocation review.

where

"equity markets" in this context means the global equity as a whole, and the Australia and NZ markets individually.

"interest rate" in this context means the market interest rates/yields in the US and NZ markets.

Appendix C - Temporary departures from this statement

- The Trustees recognise that from time to time circumstances will occur which require a departure from the guidelines set out in this statement. Any such departure requires the prior approval of the Trustees. Current temporary departures are:
    - Nil