

# Chairman's Letter 2017



Dear Member

This is my first letter to you following my appointment as Chairman of the Government Superannuation Fund Authority Board (the **Board**) earlier this year.

On behalf of the Board, I am pleased to present the annual reports on the activities of the Government Superannuation Fund Authority (the **Authority**) and the Government Superannuation Fund (**GSF** or the **Fund**) for the year ended 30 June 2017.

## Features of the 2017 Year

- During the financial year to 30 June 2017, \$874 million was paid out to members of the GSF Schemes.
- All pension payments were made on time and member satisfaction is measured at 86%.
- A good year for investments with a return of 13.9% before tax and after investment fees. This was 1.4% ahead of the Reference Portfolio and well above the 0.2% return on New Zealand (**NZ**) Government Stock.
- Over the last 5 years, the Fund investment return has averaged 12.1% per annum net of fees, 0.8% per annum ahead of the Reference Portfolio and 8.3% per annum above NZ Government Stock.
- The new Business System for the administration of the GSF Schemes successfully went live on 28 November 2016. The transition from the old outdated system to the new Business System has gone seamlessly with no disruptions to key stakeholders.

## Investment Activity

The Fund's objective is to maximise the excess return above NZ Government Stock subject to limiting the chance of under-performing NZ Government Stock by more than 10% over a rolling ten year period to 25%. The Fund switched to a before NZ tax investment objective in 2015.

The Fund relies largely on equities to provide the excess return over NZ Government Stock returns but is always looking for more efficient ways to capture alternative return sources. 90% of the Fund is invested internationally. Almost 20% is invested in alternative asset classes, such as insurance-linked assets, private equity, private real estate funds and risk factors. These alternative sources of return diversify the Fund's risk, enabling higher total returns to be achieved at similar levels of risk. Active management is also used where there is a strong likelihood of added value net of any incremental costs. Nevertheless, global equity market risk remains by far the biggest investment risk to the Fund.

During the year the Board approved an increase in the Fund's commitments to global private equity. The increase will occur over the next few years and will include commitments to primary buyout and growth funds, some venture capital and secondary stakes in more mature private equity funds. The Fund's existing private equity investments are now well into their 8 - 10 year lifecycles and are producing the expected higher returns both in NZ and offshore. The Board believes better quality private equity funds will provide higher returns than the public markets sufficient to compensate for the greater risk and reduced liquidity.

Collaboration with other Crown Financial Institutions (**CFIs**) continued, notably with the Guardians of New Zealand Superannuation (**NZ Super**). As well as discussing common investment issues, the Authority with the other CFI's share the services of a global engagement service company to co-ordinate engagements with global companies that have serious issues around damage to the environment, human rights abuse and bribery and corruption. The Authority and other CFIs are members of the NZ Corporate Governance Forum which promotes good governance among listed NZ companies.

## Outlook

The economic outlook over the next year is for a modest rise in global growth and inflation. After almost a decade since the start of the global financial crisis many economies, most notably the United States of America (**USA**) are finally looking healthier. As a result, some of the extraordinary monetary stimuli that have been deployed are starting to be gradually unwound. This has begun in the USA, with other regions such as Europe expected to follow suit over the coming year.

Financial markets are currently characterised by low volatility and low yields on financial assets. This is partly due to the unprecedented monetary stimulus and the lower macro volatility this has engendered.

Low yields on financial assets point to low returns in the future, both for equities and bonds. While expected returns are low for both, the difference between the two is near the long term average which implies equity investors are being compensated for higher risk.

Of course, to the extent policy stimulus has lowered macro and financial volatility, its removal could heighten volatility in the short term. If the removal of stimulus is the result of an improving global economy, policy makers and longer term investors should 'look through' this volatility.

## Statutory Review

As mentioned last year the GSF Act provides for a statutory review to be conducted every 5 years on how effectively and efficiently the Authority is performing its functions. The third statutory review was completed by PricewaterhouseCoopers Securities Limited (**PwC**) and was tabled in Parliament in July 2016. The report can be viewed using the following link - [www.treasury.govt.nz/publications/reviews-consultation/gsf](http://www.treasury.govt.nz/publications/reviews-consultation/gsf).

The scope of PwC's assessment included a review of all relevant documentation and policies related to the investment governance and operations of the Authority.

Overall, PwC stated they believe the Authority is a sound operation, run by experienced and capable people with an appropriate investment governance framework. In addition to noting the strengths of the Authority, PwC also made some recommendations for the Authority in the statutory review which will assist in improving its operations. The Authority has considered the recommendations and developed action plans where appropriate to implement the recommendations. The action plans have been completed and are now part of the Authority's work programme. The recommendations and the Authority's responses will be published on the Authority's website.

## Communications

The Authority's website - [www.gsfa.govt.nz](http://www.gsfa.govt.nz) - continues to be an important part of our communications strategy and contains comprehensive information on both the Authority and the Fund. It explains how the Authority operates and gives all stakeholders access to member booklets and policies, together with our annual investment results and investment policies and strategy.

If your contact details change, we request and encourage you to advise the scheme administrator, Datacom, so we can contact you if required. Datacom will provide you with a personal details form on request for this purpose. Your personal information is currently maintained and stored electronically by the Authority within a cloud service in New Zealand.

## The Board

Keith Taylor retired as Chairman of the Board at the end of April 2017. Keith joined the Board in August 2008 and became Chairman 1 August 2011. The Authority and the Fund benefitted from his wide experience in investment, actuarial and governance matters. I succeeded Keith as Chairman from 1 May 2017 and I, and my fellow Board members, express our appreciation and thanks for the very significant contribution made by Keith during his time on the Board and wish him well in the future.

Dr Alison O'Connell joined the Board on 1 May 2017. Alison is also on the Board of the Education Benevolent Society Inc. and the Earthquake Commission. She is a Governor and former Director of the Pensions Policy Institute in the United Kingdom. Her background is in the financial services industry, mainly in strategic management roles including at Swiss Re and McKinsey. Alison's PhD is from Victoria University, Wellington. She has a Master of Arts in Mathematics from the University of Cambridge and a Master of Science in Gerontology from the University of London. Alison is a Fellow of the

Institute of Actuaries in the United Kingdom and of the New Zealand Society of Actuaries.

The Board has worked effectively and efficiently in 2016/17 with seven full Board meetings being held during the financial year.

The Board has two permanent committees - an Investment Committee chaired by Craig Ansley and an Audit and Risk Review Committee chaired by myself until 30 April 2017. Shelley Cave became the Chairman of the Audit and Risk Review Committee following my appointment as Chairman of the Board. The Board had also established a committee to provide governance oversight to the new Business System project. This committee was chaired by Michelle van Gaalen and dis-established in June 2017 following the successful implementation and transition to the new Business System and the completion of the project. I would like to thank all of the committee chairs for the work they undertook during the year.

## Conclusion

The Board thanks the Minister of Finance and government officials for their support, and the Management team and staff for their high level of work and commitment to meeting the Authority's objectives.

I also thank my fellow Board members for their expertise and commitment during the year.



**Cecilia Tarrant**

*Chairman*

*Government Superannuation Fund Authority Board*

6 September 2017





# GOVERNMENT SUPERANNUATION FUND AUTHORITY

## Our Mission

The Authority's mission is to use best practice to manage the Fund and administer the GSF Schemes, in accordance with the Act, with the prime objectives of enabling:

- returns to be maximised without undue risk to the Fund,
- the Crown's contribution to GSF to be minimised, and
- the needs and reasonable expectations of its stakeholders to be met.

[www.gsfa.govt.nz](http://www.gsfa.govt.nz)

## Further information

If you have any queries regarding your GSF membership or would like a free copy of the annual report, please contact Datacom Employer Services, GSF Schemes Administration, PO Box 3614, Wellington 6140, Freephone 0800 654 731.