

# The Treasury

## Shareholder Expectations Letters Information Release

### Release Document

May 2017

<http://www.treasury.govt.nz/statesector/commercial/reporting/strategic>

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- [1] 9(2)(a) - to protect the privacy of natural persons, including deceased people
- [2] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information
- [3] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice
- [4] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice

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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.



# Office of Hon Bill English

Deputy Prime Minister

Minister of Finance

Minister Responsible for HNZC

12 DEC 2016

Catherine McDowell  
Chair  
Board of Trustees of the National Provident Fund  
PO Box 3390  
WELLINGTON 6140

Dear Catherine

## **ANNUAL LETTER OF EXPECTATIONS**

I am writing to convey my expectations of the National Provident Fund (NPF) as it executes its business planning process for the forthcoming year.

I recognise that the NPF is not a Crown entity and therefore not required to submit a Statement of Intent or Statement of Performance Expectations, however, the Government guarantees the benefits paid by the NPF and minimum investment returns for the funds held by the NPF. Accordingly, I consider it appropriate that you are familiar with my expectations communicated to the CFIs for the development of their 2017/18 business planning documents. The general expectations applicable across all CFIs are set out below.

### **Expectations for All Crown Financial Institutions**

- *Long-Term Performance:* A prime focus for Ministers is that the Crown Financial Institutions (CFIs) achieve their long term performance objectives. The Crown has a long term perspective on returns, and acknowledges that returns will vary from year to year, sometimes due to temporary or non-controllable factors. Emphasis will continue to be placed on longer term returns. In circumstances where the longer term return is persistently below the performance objective, I expect the CFI to review the appropriateness of its investment strategy. Furthermore, where active management or other value adding strategies are employed, achieving returns in excess of benchmarks after investment management fees and other operational costs is expected.
- *Investment Management Expenses:* Notwithstanding the expectation for CFIs to outperform investment objectives after investment management costs, each CFI should also ensure that the costs incurred in implementing its investment strategy are fully transparent and appropriate in the context of managing Crown assets.

- *Risk Profile:* In the past, particular emphasis has been placed on the CFI's financial returns performance. I expect to see a greater emphasis on the risk-adjusted performance of NPF in order to better reflect the differing investment strategies that are employed to deliver these returns. Furthermore, I expect to be consulted if you are pursuing any strategic changes that may materially alter the risk profile of your entity. I also ask that you ensure that appropriate emphasis is placed both on quantifiable investment risk as well as the more qualitative non-market risks that are inherent in investment management activity.
- *Flow of Information:* Of growing importance for the Crown is the need for adequate independent analysis of financial and other investment risks at an aggregate level across the CFI portfolio and, to a certain extent, across the broader Crown balance sheet. As such, the Crown is focused on establishing a deeper and more frequent flow of information from the CFIs to the Treasury, which will then be aggregated and independently analysed by the Treasury. Some of the information obtained will also be utilised to progress the Crown Asset and Liability Management (CALM) project. Your assistance to date with the CALM project has been appreciated. I ask that you continue to engage with the Treasury in support of the Crown's broader information requirements (which will undoubtedly necessitate some dedication of additional resources).
- *Complex Products and Activities:* The aggregate funds managed within the CFI portfolio continue to grow as a percentage of the overall Crown's balance sheet. Within this portfolio there has been an increase in the complexity of the investment activity being undertaken, including an increase in the use of derivative instruments. Consistent with last year's expectations, it is my expectation that CFIs should use derivatives judiciously and that, where relevant, a strong case is made for their use relative to physical exposures. Furthermore, I expect that the CFIs will regularly assess the use of derivative instruments and the extent to which other complex investment activity is undertaken to ensure alignment with your legislative framework, including any specific approvals that have previously been issued from my office.
- *Board Relationship:* I consider it to be critical for the good stewardship of the CFIs that an open and effective dialogue is maintained between each CFI's Board and the Treasury. This should span all areas of potential shareholder interest, from strategic direction through to material operational matters, and it is my expectation that the relationships extend across the whole of the Board.
- *Collaboration:* While the individual objectives and investment strategies differ across the CFI portfolio, there is a material level of crossover in terms of operational investment activities. There is also a shared level of public scrutiny on certain investment policies, most notably relating to Responsible Investing (RI). I note that the Treasury is uniquely positioned as the Crown's agent, with oversight of each of the CFIs, to give some portfolio-level consideration to such matters. My expectation is that the CFIs will continue to identify opportunities and implement strategies to achieve operational synergies, cost efficiencies and a consistent approach to managing the public scrutiny of RI through the sharing of resources and intellectual capital, and will engage as a group inclusive of the Treasury on such matters.

- *"No surprises" policy:* I expect you to maintain a "no surprises" policy and to inform me well in advance of any material or significant events, transactions and other issues that could be considered contentious or attract wide public interest, whether positive or negative.

### **Engagement**

The Treasury is working to engage more closely with entities to gain a better understanding of the strategic issues, risks and influences on entities' financial performance. In light of this closer engagement, I would like the Board to meet with the Treasury to discuss this Letter of Expectations at an appropriate time in the New Year.

If you have any questions or require further clarification on any of my expectations, please contact Oliver Martin at the Treasury on [1] in the first instance.

Yours sincerely



Hon Bill English  
**Minister of Finance**

cc Simon Tyler  
Chief Executive  
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