Hawke’s Bay Regional Council Group

Statement of Investment

Policy and Objectives

13 December 2023

Contents

1. Investment Principles

This Statement of Investment Policy and Objectives (**SIPO**) is applicable to the Hawkes Bay Regional Council (**Council**) and the Hawkes Bay Regional Investment Company (**HBRIC**). Collectively, both organisations are the Hawkes Bay Regional Council Group (**the Group**).

<u>This SIPO is relevant to the operation and performance of the Groups Managed Fund investments only.</u>

This SIPO is not applicable to current or future subsidiaries of HBRIC, including the Port of Napier Holdings Limited (**the Port**), unless otherwise stated.

1.1 Version, Effective Date and Review Periods

This SIPO is applicable from 13 December 2023. It supersedes all prior versions of the SIPO for all entities within the Group. This includes the Council SIPO of 1 July 2018.

The SIPO is to be considered a live document, updated to reflect changes in the underlying obligations of the Group and or changes in investment market conditions. Every change in the SIPO must go through the formal approval process as outlined in this document and be reflected as a newly dated version of the SIPO.

The SIPO should be reviewed annually by HBRIC and presented to Council, allowing for the Group's Asset Allocation to reflect the annual movement in the Reserves of Council, per the Councils Annual Report. Where no change is required to the SIPO, a newly dated version must still be approved to reflect such consideration.

1.2 Investment Objectives

The Group's overarching strategic goals for its investment activities are as follows:

- The Group maintains a long-term perspective to ensure assets are protected for future ratepayer generations and over the long run will consider the impact of inflation.
- The Group ensures that the overall portfolio of investments is sufficiently liquid to meet ongoing cash flow requirements.
- The Group will ensure that investment returns are optimised within the risk management parameters specified in the SIPO.

1.3 Purpose

The purpose of this Statement of Investment Policy and Objectives (SIPO) is to assist the Group in effectively supervising, monitoring, and evaluating the management of the Groups Investment Funds (the Fund).

The SIPO defines the key responsibilities, and the operating parameters within which the investments and their ongoing management are to operate. The SIPO should always encourage the use of methodologies and processes that reflect industry best practice, encompass the principles of good governance, and reflect the Group's vision and risk tolerances.

The investment activities are defined in various sections of the SIPO by:

- Stating in a written document the Group's attitudes, expectations, objectives, and guidelines for investment.
- Recognising the underlying quantum and purpose of each of the Group's Reserves, ensuring the investment risk and return are matched to each purpose.
- Defining the operating responsibilities of HBRIC in managing the Groups investment assets.

- Define the overarching values of the Group as a Responsible Investor.
- Defining an investment parameter for managing the Funds of the Group. This structure includes various asset classes, investment management style(s), asset allocations and acceptable investment ranges that, in total, are expected to produce an appropriate level of diversification and total return over the investment time horizon.
- Establishing formal criteria to monitor, evaluate and review the performance of investments on a regular basis.
- Encouraging effective communication between the Council (and its staff and Committees), HBRIC, and the Investment Managers.
- Complying with all applicable fiduciary, prudence and due diligence requirements that experienced investment professionals would utilise, and with applicable laws, rules and regulations.
- Providing guidelines and criteria for the appointment of an Investment Managers.

1.4 Taxation

The Fund should be operated in a tax efficient manner.

The Council is zero rated for tax, while HBRIC is a subject to the company tax rate. This SIPO is for the Group, therefore assets should be managed according to their investment risk and taxation risk.

Where it is operationally efficient, market practice of investing via a Portfolio Investment Entity should be followed.

1.5 Social Responsibility

The Group recognises that Council has obligations to its community, including the delivery of social, environmental, cultural, and economic well beings. The values of the Council are similarly reflected by the Group.

The Group expects its investment portfolio to demonstrate Corporate and Social Responsibility not only in the way it is managed, but also in the way that it determines its investments. This includes ensuring any Managers apply industry standard methods and principles in the way they operate and in how underlying investments are selected.

Investments are to be thoroughly researched and screened where practical to ensure that they meet our responsible investment criteria, including consideration for mitigating and adapting to the impacts of climate change, without material negative impact on overall investment objectives. The following initiatives are to be adopted by any appointed Manager.

- Incorporate Environment, Social and Governance (ESG) considerations into investment processes to enhance understanding of the potential risk and reward of investments in the portfolio. Corporate engagement and voting encouraged where practical.
- Using data from a globally recognised ESG research agency, avoid investing in entities that exceed the ethical exclusion criteria described in Appendix 1 by prohibited activities and thresholds, as these activities are inconsistent with our values.
- The Groups management and standards on Social Responsibility will be reviewed as part of the overall SIPO review and updated as necessary to reflect changes in best practices, and to ensure continued alignment with our values and mission.

The Group excludes investment in any entity that is actively in opposition to the objectives of Council in the Hawkes Bay.

1.6 Capital Base

The Group owns, or can own, the following investment assets.

Port of Napier:	The Group, through HBRIC, holds a 55% stake in the NZX listed Port of Napier Holdings Limited. This holding is a Strategic Asset under the Local Government Act 2002.
Managed Funds:	The Group, through both HBRIC and Council, holds investments in listed and unlisted markets. This includes a selection of cash, fixed interest, equities, private equity, alternatives, and managed funds, being collectively referred to as Managed Funds. These assets reflect the proceeds of the HBRIC sale of 45% of the Port of Napier and other assets held to manage Councils reserve obligations. The proceeds of sale of the Port are a Strategic Asset under the Local Government Act 2002.
Property Assets:	The Group holds a mix of freehold property and leasehold land assets for commercial return. Property assets held by Council to achieve its wellbeing objectives are not considered part of Property Assets definition under this SIPO. The Group holds investment in residential and commercial freehold and leasehold properties in both Hawkes Bay and Wellington. Income derived on Hawkes Bay leasehold properties is subject to contractual undertakings between HBRC and Accident Compensation Corporation (**ACC**). The Group also hold Freehold property assets.
Forestry Assets:	The Group hold a range of forestry assets that consist of forestry crop for logging purposes, carbon credits, and mānuka plantings for honey.

This SIPO governs the management and operations of the Groups Managed Funds operation. Investment considerations made under this SIPO are expected to consider the broader sector exposures of the Group.

The investment base of the Managed Fund portfolio represents a combination of Group reserves for specific purpose (such as Disaster Recovery) and intergenerational reserves (such as proceeds from the Port of Napier sale).

At 30 June 2023, the value of the Groups Managed Fund portfolio was over $150,000,000.

1.7 Building a Portfolio

The Investment Portfolio is a collective pool of assets managed as one to ensure Group can achieve its future commitments, while protecting the obligations it has for the Reserves and Strategic purposes that the assets represent.

Every Reserve that is asset backed will be reviewed annually to determine the following:

Reserve Value:	The Group annually adds to Reserves or spend Reserves in accordance with the operations of the Group. The Reserves also grow by an inflation factor, being derived from the prior year's investment performance. The Reserve values will match the Council Annual Report and HBRIC Annual Report.
Reserve Duration:	The investment risk is partially determined by the expected duration of the reserve. Long term, or intergenerational reserves can tolerate higher investment risk than near term reserves. Duration is determined by the Reserve definitions in Council Plans or decisions.
Reserve Spend:	The second determination of investment risk is the level of spend likelihood. Reserves that are forecast to grow may have greater capacity for higher risk

volatility. Reserves that are forecast to be spent are focused on capital preservation. Reserves that are strategic assets and intergenerational have a higher growth focus. Council Finance team will have input into this based on Councils Annual Plan and Long Term Plan (**LTP**) cycles.

Intergenerational Reserves or Funds, such as those derived from the sale of a Strategic Asset would also apply the same test principles around duration and spend. By nature, these would likely permit greater investment risk for greater long-term benefit.

It is the combination of Reserve Duration and Reserve Spend that determines the appropriate asset allocation for a specific Reserve. The following describe is the Reserve Risk profile.

Duration \ Spend	Growing	Stable	Declining
Strategic (perpetual)/ Intergenerational		80:20	
Long Term (8 years plus)/ Low Spend certainty	80:20	60:40	40:60
Mid Term (3-7 years) / Medium Spend Certainty	60:40	40:60	20:80
Near Term (0-2 years)/ High Spend Certainty	0:100	0:100	0:100

The table above gives indicative growth to defensive splits for each Reserve in establishing a Reserve Risk.

It is the weighted average of all Reserves Risk by Reserve Value that determines the Strategic Asset Allocation.

1.8 Required Rate of Return

Investment Performance objectives are tied to the needs of Council in achieving the core responsibilities in the LTP.

For the 2024 LTP, the inflation objective is set at 2.5% per annum for each year of the LTP.

For the 2024 LTP, the cash flow requirements of Council are set at 3.0% per annum for each year of the LTP.

The Group recognises that the target rate of return (a minimum 5.5% nominal) is a long-term one and will not be achieved in every measurement period. Differences between the inflation-proofed value and the Investment Portfolio will be reflected in an Investment Volatility Reserve.

The Group expects that the Investment Manager should be able to outperform the benchmark (after fees). Nominal over or under performance will be represented in movement in the Investment Volatility Reserve.

All returns are assessed in NZD.

1.9 Strategic Asset Allocation

Based on Council and the Groups Reserves being asset backed and their respective Risk Factors required return, capacity, and willingness to accept risk, a 70% growth and 30% defensive portfolio is suitable for a **Medium/High** level of risk for the whole portfolio.

At a whole of portfolio level, tilting of plus or minus 10% is tolerated in the allocation to growth and defensive assets.

2 Risk Tolerance and Management

2.1 Approach

As entities responsible for public funds, the Group is a prudent investor and seeks to take measured risk that has adequate expected return compensation. The Groups investment framework is supportive of its inter-generational responsibilities to current and future ratepayers. The Group seek, where possible, to manage volatility or risk. Notwithstanding this risk aversion, the Group acknowledges that investing solely in capital stable investments exposes the portfolio to the risk of inflation and is willing to accept some risk to increase expected return, subject to the Group's capacity to accept risk.

Strategic, long-term asset allocation is the key to maximising investment returns while minimising risk. Fund investments should be continually monitored and adjusted relative to benchmark asset allocations.

All investments must apply a responsible and ethical investment framework filter when considering investments as outlined in the SIPO.

2.2 Risk Tolerance

The Group recognises that some risk must be assumed to achieve the long-term investment objectives. Risk tolerance is affected by three factors:

- Capacity to accept risk,
- Willingness to accept risk, and
- Required rate of return (see section 1.8 and 1.9)

<u>Capacity to Accept Risk</u>

The capacity to accept risk is tied to the Purpose for each respective reserve and a function of its investment time horizon, prospective future contributions, current financial conditions, and cash flow requirements.

Time horizon: This SIPO has been prepared on the basis that the Group is expected to exist in perpetuity. The investment time horizon of the Group is therefore long term. This increases the capacity to accept risk.

Financial capacity and cash flow requirements: The Groups ability to derive Cash flow to annually support Council imply low capacity to tolerate illiquidity, short to medium term volatility in the value of its Investment Fund. This reduces the capacity to accept risk.

Based on the combination of time horizon. financial circumstances, and the Groups high weighting to an intergeneration strategic purpose for its Port sale proceeds, the Groups implied capacity to accept risk is assessed as medium to high.

<u>Willingness to Accept Risk</u>

The Group is a prudent investor and seek to take measured risk that has adequate expected return compensation. The Group seeks, where possible, to manage volatility and risk. Notwithstanding this risk aversion, the Group is willing to accept risk to increase expected returns in line with maintaining the real value of inter-generational equity (after accounting for inflation).

The Group forecasts on a ten-year Long Term Plan basis and is an intergenerational investor. The Group accepts volatility of returns in the short term to achieve a long-term objective. Volatility is to be represented in an Investment Volatility Reserve. The Group willingness to accept risk is assessed as Medium.

2.3 Management of Risk

The Council, HBRIC, and Council Finance Team have the responsibility to develop appropriate internal controls, policies, and risk management strategies. These internal controls, policies and risk management strategies are described in this SIPO.

Identified risks include:

Credit Risk

Risk Description: Credit (or counterparty risk) is the risk of default by a counterparty to a particular transaction or an issuer of a security held in the portfolio.

Risk Managed By:

- Measuring and maintaining the credit quality of portfolios within prescribed guidelines, and
- Limiting exposure to individual issuers through issuer limits, and
- Diversification across investment type and instrument, and
- Maintaining appropriate policies and procedures relating counterparties, and
- Appointing Fund Managers with mandates consistent with prescribed risk limits

Currency Risk

Risk Description: Currency risk is the risk that foreign currency denominated assets will lose value because of an adverse exchange rate movement.

Risk Managed By:

- Maintaining a hedging policy for the portfolio and individual asset classes.

Liquidity Risk

Risk Description: Liquidity risk is the risk that a security cannot be sold when required or that the price achieved is significantly different from the quoted price.

Risk Managed By:

- Setting liquidity requirements by asset class in the SIPO, and
- Setting diversity targets by asset class in the SIPO, and
- Requiring Investment Managers to invest in accordance with the SIPO, and
- Aligning liquidity risk to the likelihood of capital spend on the investment, and
- Limiting the credit rating of the fixed interest and cash investments to approved levels.

Manager Risk

Risk Description: The Group retains professional managers to implement its investment strategy. Managers' returns may vary from expected levels.

Risk Managed By:

- Robust selection process for Fund or Private Equity Managers, and
- Appointing Managers with mandates that prescribe acceptable risk limits, and
- Appointing independent experts to the Board of HBRIC, and
- Regular assessment and review of performance against benchmark and peers.

Market Risk

Risk Description: Market risk is the risk of adverse movements in investment markets (including asset prices, volatility, changes in yield curves or other market related variables) that affect the value or income of the portfolio. The volatility of investment markets means that the return from the investment portfolio is inherently uncertain. Actual returns from each asset class may vary significantly each year from the returns assumed in determining the investment strategy appropriate for the long-term.

Risk Managed By:

- Diversifying portfolio investments, and
- Seeking professional advice, and
- Requiring Managers to manage funds to prescribed mandates.

Operational Risk

Risk Description: Operational risk is the risk of financial loss due to mismanagement, error, fraud or unauthorised transactions.

Risk Managed By:

- Having in place a robust system of internal controls at HBRIC that Regular review of reports to Council on investment portfolios, and
- Requiring a custodian to hold assets as bare trustee, record transactions and report on performance, and
- Ensuring each Investment Manager has a specific mandate, and
- Ensuring clear separation of investment management, custodial and overall supervisory functions.

3 Duties and Responsibilities

3.1 Responsibility for Investment Assets

Council has determined that the Board of HBRIC has overarching responsibility for the Investment Assets of the Group, including Managed Funds investments operated under this SIPO. This includes the safe keeping of the investment assets, and supporting Council to achieve the cash flow returns from investment assets to support the objectives set in the LTP.

This SIPO should be read in conjunction with the Council Statement of Expectations (**SOE**) and HBRIC Statement of Intent (**SOI**), as agreed annually between HBRIC and Council.

The SIPO, SOE, and SOI should be aligned in purpose and objectives, however where conflict exists the SOI takes priority in relationship matters between the Group entities, while the SIPO will take priority on investment parameters.

The core responsibilities are outlined in the table below.

Activity	Authorising Agent	Transacting Agent
SIPO Review, including • Strategic Asset Allocation and tolerances • Return Expectation • Investment Asset Classes • Responsible Investment	Council / C&S Committee	HBRIC
Investment Manager Selection, including • RFP process • Selection of Investment Manager(s) • Oversight of Investment Memorandum (‘IM') • Fee Setting • Asset Allocation by Asset Class (including rebalancing tolerance, diversity and liquidity controls)	HBRIC	Investment Manager
Custodian Selection	HBRIC	Investment Manager
Contribution and Withdrawal	HBRIC	Council Finance Team
Asset Class Manager Appointment	HBRIC	Investment Manager

3.2 Council/Corporate and Strategic Committee

The Corporate and Strategic Committee (‘C&S’) will be responsible for receiving and recommending to Council the following:

- Receiving and resolve on any change recommended by HBRIC to the review of the SIPO annually.

3.3 Council Finance Team

Many of the assets invested are intended to match Councils Reserve obligations or Strategic Asset expectations. Reserves are subject to annual movement because of funds received and Council spend.

Council Finance monitor the historic movement in such reserves and balances on an annual basis as part of their Annual Report.

Council Finance monitor the forecast movement in such reserves and balances on an annual basis through the Annual Plan.

The key contact for the Council Finance Team is the Group Manager Corporate Services (or their delegate)

Council's Finance Team will:

- Advise HBRIC of capital contributions and withdrawals from the fund annually as part of the Annual Report process.
- Advise HBRIC of capital withdrawals from the fund annually that are forecast as part of the Annual Plan process.
- Work with HBRIC on the expected timing of distributions, contributions, and withdrawals in a reasonable timeframe.
- Monitor and annually report on the value and movement in the Investment Volatility Reserve.

3.4 HBRIC Board

The responsibility for the monitoring and reviewing of The Group's investment policies is that of the Board of HBRIC, assisted by Councils Group Manager Corporate Services (or delegate), and the Investment Managers.

The Board of HBRIC may, through HBRIC policies, elect to delegate responsibilities to HBRIC resources or third parties.

The Board will:

- Recommend to C&S and then Council any amendment to the SIPO annually.
- Selection, appointment, or removal of Investment Managers.
- Formal reviewing the SIPO every three years and make recommendation to C&S and then Council. This involves a review (either in house or via third parties) of the SIPO including the investment strategy, return objective, policies and Managers configuration, and instructions to the Investment Managers.
- Monitor and ensuring that the target rate of return (section 1.8) is achievable given the risk appetite of the Group and the Strategi Asset Allocation (section 1.9). Where the Board believe the rate of return is no longer reasonable, this should be reflected in a recommendation and amendment to this SIPO.
- Provide cash flow information to the Investment Managers with respect to future deposits and redemptions. This includes following an annual review of the usage of Council Reserves with Council Finance Team.
- Ensure that the Fund has its own Investment Mandate ("IM"), which is a document, between an investor (the Group) and an Investment Managers, recording how the investor's money is to be managed. Specific information on matters such as asset allocation, risk tolerance, investment securities and liquidity requirements are included in an IM.
- Review and seek to ensure that the practices and policies set out in the SIPO and IM are adhered to.
- Regularly review Investment Manager reports, and reporting exceptions.

- Seek to ensure that all parties overseeing, advising, and managing the Group's investments disclose any potential conflicts of interest. If conflicts of interest arise, the policies and procedures for managing these are to be clearly defined, although, in principle, such conflicts should be avoided.
- Report to Council on the performance of the Fund on a basis agreed with the Council.
- Report to Council on a no surprises basis around material matters pertaining to the management of the assets.
- Confirm the management of investments complies with all applicable laws, Council's policies, risk tolerance and other supporting documents.
- Seek to ensure that contracts for the Investment Managers and Custodian are current.
- Follow formal criteria to monitor, evaluate and compare the investment performance results achieved against relevant benchmarks and objectives on a regular basis.
- Seek to ensure that all service agreements and contracts are in writing and are consistent with fiduciary standards of care.

3.5 Investment Managers

For this document the term Investment Manager, refers both to the Investment Management entity and its individual representatives.

The Investment Manager(s) is/are responsible for preparing and maintaining a written Investment Mandate (IM) or equivalent in a format consistent with, and adhering to, the SIPO.

External Investment Managers may be appointed to manage part of or all the Funds in accord with this policy.

The process for the appointment of manager is outlined in Section 5 Investment Manager Selection.

The Investment Managers roles are as follows:

Investment Strategy

- Manage investments in accordance with the guidelines and objectives as outlined in the SIPO, IM, and any respective agreements.
- Ensure investment assets are appropriately diversified and conform with the time horizon and agreed risk/return profile.
- Ensure that "expected" and "modelled" returns for asset classes are based on sound return and risk premium assumptions.
- Provide advice on, and implementation of, the SAA and where appropriate the Fund Manager selection.
- Provide advice on, and implementation of asset and sub-asset class allocation strategies.
- Rebalance individual investments and asset class groups to within agreed benchmarks as described in the rebalancing policy contained in the SIPO and IPS documents.
- Outline expected returns and risk, or volatility, within the selected strategies.

Investment Reporting and Administration

- Maintain an open 'no surprises' dialogue with the Board of HBRIC (or delegate)
- Define the procedure to be used for reporting, reviewing and possible modification of strategies from time to time.

- Ensure positions are reconciled between the Investment Manager and the Custodian.
- Provide instructions to other Fund Managers to lodge or withdraw funds.
- Deliver quarterly reports including:
  - Fund valuation,
  - Fund duration,
  - Compliance reporting (including approved exceptions),
  - Performance summary for the Fund and by asset class,
  - Performance against benchmarks,
  - Fund income,
  - Asset transactions summary,
  - Cash transactions,
  - Investment management fees,
  - Custodial fees,
  - Individual fund management fees, and
  - Brokerage and other transaction costs.
- To report at least annually the 'Total cost of Delivery' being the sum of:
  - Investment Manager fees,
  - Custodial fees,
  - Administration fees, and
  - Total Fund fees – made up of; annual management fees (including annual management fees of underlying investments) and any other fees and costs.

Professional and Social Responsibility

- Demonstrate care, skill, prudence, and due diligence that an experienced investment professional, acting in a like capacity, including compliance with all applicable laws, rules, and regulations.
- Demonstrate due care to ensure transactions for the Fund occur at the best price.
- Make available appropriate personnel to attend meetings, as agreed.
- Disclose any potential conflicts of interest and steps taken to mitigate such conflicts.
- Communicate all significant changes in ownership, organisational structure, financial condition, professional staff, and reputation are examples of changes to the firm that are material.

3.6 Fund and Private Equity Managers

To manage an allocated part of the Fund on terms and conditions consistent with their mandate. Any Fund Manager(s) chosen by an Investment Manager must be approved by the Board of HBRIC. All Fund Managers must manage in accord with the principles and policies of this SIPO.

3.7 Custodian

The Custodian holds investments as bare trustee on behalf of the Group and is responsible for the safekeeping of those investments. The specific duties and responsibilities of the Custodian are:

- Maintaining separate accounts.
- Valuation of all investment assets.
- Collection of income.
- Settlement of transactions (buy/sell orders) initiated by the Investment Managers.
- Provision of regular reports detailing transactions, cash flows, securities held and their current values, changes in value and returns.

4 Investment and Asset Class Guidelines

Specific investment policies are outlined in Council's Investment Policy. Where there is a conflict between the Councils Investment Policy and the SIPO regarding the management of Managed Funds, the SIPO shall take priority.

In general terms, when making decisions on the Fund, or a portion of the Fund, the Investment Managers will consider the overall objectives of Group and will comply with all applicable legislative requirements.

The Fund will be managed with a view to ensuring sufficient liquidity to meet expected cash flow and distribution requirements.

Investment risk will be limited by appropriate diversification both within and between asset classes as determined by the following asset allocations.

4.1 Acceptable Asset Classes

The Fund will consist of a mixture of growth and defensive assets.

The following asset classes and assets are authorised by the Group for investment.

<u>Defensive Asset Classes</u>

- Cash – term deposits, cash on call, commercial paper, bank bills.
- NZ Fixed Interest – NZD denominated bonds (domestic and foreign issuers), including sovereign and non-sovereign issuers, either directly or via Collective Investment Vehicles ("CIVs").
- International Fixed Interest – Foreign denominated (not NZD) bonds (domestic and foreign issuers), including sovereign and non-sovereign issuers, either directly or via "CIVs".

<u>Growth Asset Classes</u>

- NZ and international Equities - shares in publicly listed companies, including listed property companies, domestic and foreign, either directly or via CIVs.
- Private Equity, Mature Private Equity Direct or via Funds.
- Property, both NZ and International via managed funds indirectly or directly.
- Infrastructure via managed funds indirectly or directly.
- Alternatives, including Hedge Funds, Long / Short Funds, Inflation Linked Funds, or Venture Capital Funds.

Unlisted Growth Asset Classes can only be applied as a part of a portfolio in managing an intergenerational strategic reserve or asset of the Group.

Investment Classes not identified above are deemed to be excluded from the investment. The addition of a new investment class can only occur with a review of the SIPO and is not deemed an acceptable breach for approval by the Board of HBRIC.

4.2 Asset Allocation by Asset Class

The strategic asset allocation and tactical ranges are identified in section 1.9.

The Investment Manager is responsible for ensuring that the portfolio is rebalanced to the targeted asset allocation (see rebalancing procedures below) and kept within the tolerance ranges set below.

The Investment Manager will assist the HBRIC Board in setting and annually reviewing (or sooner if circumstances require) the sector weighting to achieve the SAA and rebalancing limits appropriate for the Group to manage its risk tolerance and income expectations.

4.3 Rebalancing

The exposures to the various asset classes will be monitored and can be rebalanced by the Investment Managers, considering the underlying exposures in any collective investment vehicles, direct investments and other material factors on an effective exposure basis.

Where an asset class allocation exceeds the benchmark asset class ranges, then the Investment Manager must inform the HBRIC Board of the breach of band and recommend a solution. Any recommendation to remain outside of benchmark asset ranges must be approved by the HBRIC Board.

Any breach outside of the Strategic Asset Allocation minimum or maximum tolerances (section 1.9) limits must be informed by HBRIC to Council, including a recommendation of a rebalance, if any.

Where a new SIPO is adopted by the Group, a period of up to three months is permitted from the adoption of the SIPO to rebalance the asset allocation.

4.4 Foreign Exchange

The fluctuation in the value of the New Zealand dollar relative to other major currencies can result in additional volatility of offshore investment returns, but can also provide an important source of diversification, given the high proportion of New Zealand dollar denominated investments across the Group's entire asset base. To strike a balance across these risks associated with having foreign currency exposure, the following policies apply:

- investments in international growth assets, a neutral currency position of being unhedged back to the New Zealand dollar is the base position, with allowance for hedging to vary between 0% to 100% within the context of the SIPO.
- Investments in international defensive assets will be fully hedged back to the New Zealand dollar to prevent currency translation volatility from impacting the returns of this conservative (stable) asset class.

The Group does not take speculative positions on Foreign Exchange or other derivates as an asset class.

4.5 Defensive Asset Class Benchmarks

<u>Cash Investments</u>

Asset Type: Defensive Asset

Benchmark: S&P/NZX 90 Day Bank Bill Index

<u>New Zealand Fixed Interest Investments</u>

Asset Type: Defensive Asset

Benchmark: S&P/NZX A-Grade Corporate Bond Index

<u>International Fixed Interest Investments</u>

Asset Type: Defensive Asset

Benchmark: Bloomberg Barclays Global Aggregate Bond Index (NZD Hedged)

4.6 Growth Asset Class Benchmarks and Rules

New Zealand Equity Investments

Asset Type: Growth Asset

Benchmark: S&P/NZX 50 Index (Gross)

Australian Equity Investments

Asset Type: Growth Asset

Benchmark: S&P/ASX200 Accumulation Index

International Equity Investments

Asset Type: Growth Asset

Benchmark: MSCI All Country World Index

Private Equity Investments

Asset Type: Growth Asset

Benchmark: S & P Listed Private Equity Index

Property Investments

Asset Type: Growth Asset

Benchmark: MSCI All Country World Index

Infrastructure Investments

Asset Type: Growth Asset

Benchmark: MSCI Australia Quarterly Unlisted Infrastructure Index

Alternate Asset Investments

- Asset Type: Growth Asset
- Benchmark: MSCI Australia Quarterly Unlisted Infrastructure Index

4.7 Selection of Portfolio Managers

Selection of Fund Managers or Private Equity, Property or Infrastructure Portfolio Managers, the Investment Managers must consider, among other criteria specific to the role:

- the skills and experience the Manager brings to the role,
- the substance and viability of the Manager,
- the costs that can be expected to be incurred,
- the existence of appropriate risk management structures, and
- whether there are any organisational or reputational issues.

Investment mandates shall include rules setting out authorised investments, performance measurements, constraints and exposure limits, use of derivatives, and reporting requirements.

Managers are regularly reviewed against the preceding criteria to determine their ongoing suitability for their role.

Where a Portfolio Manager is selected and the Investment Portfolio incurs an additional fee, the annual impact of this fee must be disclosed annually in writing to the HBRIC Board.

5 Investment Manager Selection

The HBRIC Board will be responsible for the appointment of the Investment Managers to assist with the management of the Group's Managed Funds. The HBRIC Board is responsible for applying the following due diligence criteria in selecting the Investment Managers.

Any proposed change in Investment Manager will be recommended by HBRIC to Council for approval.

5.1 Request for Proposal Process

Investment Managers roles should be tendered through a Request for Proposal (RFP) process. The HBRIC Board are responsible for the tender process and selection.

5.2 Portfolio Expenses

Total portfolio costs should be fair and reasonable. The Group preference is for a fee only service with all commissions returned to the Fund and reported to the HBRIC Board.

The Investment Manager is to report to the HBRIC Board quarterly the breakdown of the total cost of delivery including:

- Investment Management fees,
- Custodial fees,
- Individual and weighted average Funds Management fees, and
- Brokerage and other transaction costs.

The Group acknowledge that cost reductions can be achieved through scale.

Appendix 1: Responsible Investment Policy

The Group is committed to incorporating Responsible Investment into its investment decision-making processes. Our approach to Responsible Investment is to seek close alignment of the following Responsible Investment Framework with our values. The ability to implement this policy is a factor in the appointment of our investment adviser/manager.

The Group recognises New Zealand entities such as the Guardians of the New Zealand Super Fund as demonstrating a benchmark standard for Responsible Investment.

<u>Exclusions</u>

Product / Sector Exclusions

The Group has resolved to use reasonable endeavours to avoid investment in entities that meet the following criteria of ethically prohibited activities.

- the manufacture of controversial weapons including, but not limited to, cluster munitions and anti-personnel mines
- the manufacture or testing of nuclear weapons
- the manufacture of tobacco
- the processing of whale meat
- the manufacture or retail of recreational cannabis
- the manufacture of civilian automatic and semi-automatic firearms, magazines or parts.

National Exclusions

The Group resolved to use reasonable endeavours to avoid investment into the government (sovereign) bonds of any nation state where there is widespread condemnation or sanctions by the international community and New Zealand has imposed meaningful diplomatic, economic, or military sanctions aimed at that government.

Portfolio Exposure Exclusions

The Group is a majority holder of the Napier Port Holdings Limited, and is the Group is not seeking additional exposure through the Managed Funds portfolio.

<u>Implementation for Direct Security Investments</u>

Investment Manager(s) will use reasonable endeavours to screen out directly held security investments in the Discretionary Portfolio involved in the prohibited activities as described in the Ethical exclusion tables above. Investment Manager(s) may rely on data from third party agencies when screening these directly held security investments, which according to the investment guidelines agreed upon in the investment mandate, will apply to the asset classes of Cash (NZ registered banks), NZ Fixed Interest, NZ Equities and Australian Equities and Global Equities.

<u>Implementation for Indirect Pooled investments</u>

In relation to indirect pooled investments (i.e. via investment in collective investment vehicles), Investment Manager(s) will from time to time use reasonable endeavours to screen for and avoid indirect exposure to entities involved in the prohibited activities as described in the Ethical exclusion tables above. Where identified and measurable, exposure to entities involved with these prohibited activities will be limited to a materiality representation threshold of 10% of the total value of each of these pooled investment products.