Presbyterian Beneficiary Fund

NEWSLETTER

MAY 2022

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If you have any questions about your savings please call the Fund's Administrator, Melville Jessup Weaver, on:

0800 266 787

Message from the Chair

Welcome to another Beneficiary Fund newsletter.

I've been fortunate to have written to you about some very good returns in past newsletters – but this time the news is not so upbeat. As you will see from your March statements, investment markets in 2022 have not been kind. The Market Update on page 2 provides some insight into what is going on, and what might happen next. No one knows, of course. Markets might soon recover, but this is by no means certain: risks remain.

However, as the chart on page 4 shows, we've already experienced more than one fall in returns in the short life of the new-look Fund – only to see them bounce back. When markets recover, they can recover very quickly. Getting out now might avoid further losses, but it might also mean missing future gains, i.e., serving to lock in losses. If you're concerned, we recommend seeing a financial adviser to discuss your position.

On a more positive note, on page 3 we highlight how Mercer is reducing carbon emissions across the investment portfolio (even if not holding oil and gas companies is hurting performance right now).

Yours in Christ

M. N. Galt

Margaret Galt

Investment Market Update

What happened?

March 2022 was a particularly tough quarter for investment assets, as both shares and bonds fell in value. Typically, when investors get nervous and sell shares, they buy safe-haven assets like bonds: but not last quarter.

The March quarter saw both global shares and global bonds fall around 5% each. NZ shares fell by 7% and NZ bonds by 4%. Add a rising NZ dollar into the mix, which erodes the returns from offshore assets, and there was nowhere to hide from market losses.

This led to losses for all the Fund's investment options, except for the Cash option. While the Balanced Fund (+3.1%) and Growth Fund (+5.0%) have still generated positive returns after fees over the year to 31 March 2022, the Conservative Fund has fallen by -0.5% over this period. While it's unusual for the Conservative Fund to post losses over 12 months (as its name would suggest), this reflects the unusually sharp increases in interest rates so far in 2022.

So, what's going on?

In our last newsletter, we highlighted the emerging problem of inflation. What we didn't predict is just how swiftly inflation would become a major headache for the global economy. Since 2020, Governments and Central Banks have pumped money into economies to avoid a Covid-induced recession. This laid a foundation for an inflationary fire, which was ignited by supply chain problems. Russia's invasion of Ukraine has only served to pour fuel on the fire.

Not that long ago, Central Banks were forecasting that low interest rates would last for several years. Fast forward and now they have been forced to raise interest rates, and raise them quickly. More increases are forecast. Sharply rising rates tend to be bad for both shares and bonds, as has been the case this year. As interest rates rise, investors sell bonds at a loss (to buy new ones that offer better rates). Share prices also fall as investors discount future earnings because of higher interest rates, and factor in the higher cost of debt for companies.

Where to from here?

What happens next all depends on whether Governments and Central Banks can engineer a soft-landing for the economy. That is, bringing inflation back under control without damaging the economy. This won't be easy, with Covid continuing to distort economic activity.

However, if the economy slows too much, it can stall or come to a standstill. If that happens, we end up with the recession we all thought was going to happen two years ago when Covid burst onto the scene. A recession is not a welcome prospect. It would likely push share prices even lower (falling earnings are seldom positive for shares).

So, is there any good news?

Maybe. While rising interest rates push the price of bonds down, they ultimately result in higher earnings. That is, bonds that were once paying around 2% interest, will soon be paying interest of 4%. And while there is a risk that share prices fall further, recent falls have made some shares look like good value. In times of trouble markets tend to be indiscriminate, pushing all prices down (just as in times of euphoria they push all prices up). Good investment managers take these opportunities to buy good companies at great prices.

Headwinds (and Tailwinds) for Responsible Investors

In addition to contributing to inflationary pressures, the war in the Ukraine has also provided another headwind for socially responsible investors. In addition to pushing up the price of petrol at the pump, it has helped push up the price of oil company shares. In fact, oil and gas share prices rose by over +30% in the March quarter and by over +50% in the 12 months to 31 March 2022.

Not investing in these companies makes it even harder for investors like the Beneficiary Fund to perform well in the current environment. We expect that excluding these companies will be positive for the Fund over the long term (after all, oil will be replaced in time by renewable energy). However, there will be periods, like now, when our responsible investment approach causes a drag on returns.

That is not to say that we are resiling from our approach. The Board continues to encourage our investment manager, Mercer, to actively position the Fund's investments to address the risks presented by climate change. We hope to both contribute to the shift to renewable energy and generate returns for members in doing so.

Reducing carbon emissions in our investment portfolio

The Board met again with Mercer earlier this month, as we do each quarter. We were pleased to hear that Mercer has just substantially reduced carbon emissions from the Listed Infrastructure portion of the Fund's investments. This part of the portfolio is made up of utility companies (e.g., water and electricity), transportation systems (e.g., rail, airport, ports, and toll roads) and communication systems (e.g., cellphone networks). As large long-term assets that generate fairly stable returns over time, they are a useful part of any long-term investment portfolio. However, they also tend to have higher emissions than other companies. By selecting a different specialist infrastructure manager with a focus on carbon reduction, emissions across the entire portfolio have fallen.

Mercer has committed to net zero carbon emissions in the portfolios it manages for clients, like the Beneficiary Fund, by 2050, and a 45% reduction by 2030. We were also pleased to hear that Mercer's parent company (Marsh McLennan) has been certified CarbonNeutral® as part of its commitment to becoming a net zero company by 2050.

How has the Beneficiary Fund performed?

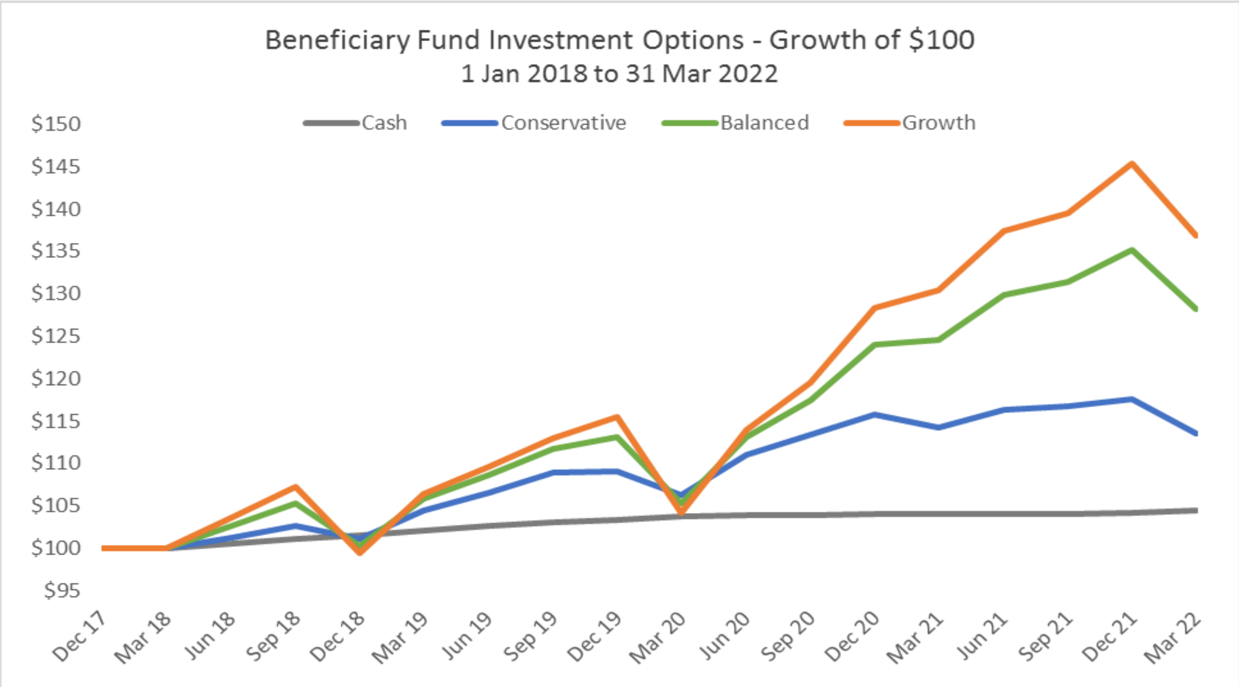
The annual returns and average annual returns for the last three years to 31 March 2022 for each investment option (net of all fees and charges) are set out in the table below.

Returns to 31 March 2022	Cash	Conservative	Balanced	Growth
1 year	0.2%	-0.5%	3.1%	5.0%
3 years (p.a.)	0.6%	2.9%	6.7%	8.8%

The chart below shows how the different investment options within the Beneficiary Fund have performed since the 1st of January 2018 through to 31 March 2022. The grey line shows that returns from the Cash Fund have plateaued with interest rates at record lows. In contrast, the orange line shows the more volatile, but substantially higher, returns from the Growth Fund.

It illustrates just how strong share prices have been, pushing up the Growth and Balanced options – and how quickly they can fall too. Markets peaked at the end of 2021, but have fallen since.

The chart also shows that it has been a struggle for the Conservative Fund of late. Even though the Conservative Fund is mostly made up of bonds and cash, these assets, like shares, can fall in value, particularly when interest rates start to rise (as investors sell bonds in favour of those paying a higher rate of return). Rising interest rates are not good for bond prices – and in this case, they have not been good for share prices either.



2022 has not been kind to investors, after a good 2021

The unit prices for each investment option are:

New Benefits and Complying Sections	Cash	Conservative	Balanced	Growth
Unit Price at 31 March 2022	1.5749	1.1354	1.3433	1.3542

Return information, along with unit price information for other periods, is available by calling the Fund's Administration Manager, Melville Jessup Weaver, on **0800 266 787**, emailing them at presbyterian@mjw.co.nz, or posting to PO Box 1096, Wellington 6140.