Presbyterian
Investment Fund

Annual Report
Year ended 30 June 2022

Together we can generate returns to support mission

Key points from the 2021 / 2022 year

- Account balances have grown to over $185 million
- Over $43 million in the new Long Term Fund
- Average On Call interest rate of 1.3%
- Long Term Interest of 3.0%
- Long Term Inflation Interest of 7.3%
- Long Term Reserve Interest of -15.5%
- $4.8m of Reserves used to support interest payments
- Expenses fell by 2.5%

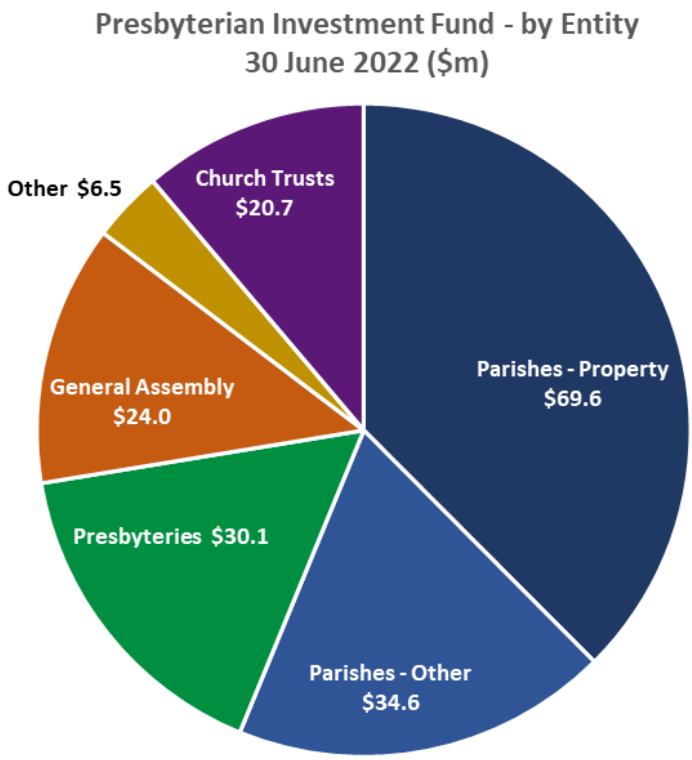
- ✓ Together we benefit from investing as a group
- ✓ Two investment options
- ✓ Online access to funds without notice
- ✓ Attractive ‘on call’ interest rates
- ✓ Low operating expenses – less than 0.40% of funds

Who makes up the PIF?

The Presbyterian Investment Fund (PIF) holds funds on behalf of parishes, Presbyteries, the General Assembly, The Presbyterian Church Property Trustees, and other entities associated with the Presbyterian Church of Aotearoa New Zealand. Property funds held on behalf of parishes are primarily held for property-related use.

Chart 1 provides a breakdown of the various groups that hold funds in the PIF. It shows that $69.6m is held as Property Capital (generated from the sales of properties) on behalf of parishes (last year $65.3m). Parishes hold a further $34.6m in the PIF (last year $37.9m), Presbyteries hold $30.1m (last year $26.5m), and the General Assembly $24.0m (last year $22.6m). The Trustees hold $20.7m on behalf of the various trusts they administer (last year $25.2m). A further $6.5m is held on behalf of related entities.

Chart 1



Parish balances make up 55% of the PIF

Account holders can invest in either or both the On Call Fund and the Long Term Fund. Table 1 below provides a breakdown of the balances between the On Call and Long Term Funds this year and last year.

Table 1: Account balance comparison

	30 June 2021	30 June 2022
On Call Fund	$140.12m	$141.88m
Long Term Fund	$38.43m	$43.52m
Total Accounts held	$178.55m	$185.40m
Reserves	$8.62m	$3.85m
Total Assets	$187.17m	$189.25m

The PIF grew again this year with more funds invested in the Long Term Fund

PIF Interest Rates

Interest from the PIF is credited to accounts each quarter (calculated on daily balances). Reserves (which are invested in the On Call Fund) are used to smooth returns over time and insulate the PIF from extreme market events where possible.

Table 2 below details the changes in rates over the course of the year. It highlights just how quickly the Reserve Bank of New Zealand raised the Official Cash Rate, how strong inflation was over the period, and how much investment markets fell in 2022.

Table 2: PIF Rate Changes Over the year

	On Call Fund p.a.	Official Cash Rate p.a.	Long Term Fund p.a.	Quarterly Inflation	Reserve Interest
As at 30 June 2021	1.00%	0.25%	3.00%		
September 2021				2.22%	
October 2021		0.50%			
November 2021		0.75%			
December 2021				1.45%	
January 2022	1.50%				
February 2022		1.00%			
March 2022				1.78%	-7.50%
April 2022	1.75%	1.50%			
May 2022		2.00%			
June 2022				1.66%	-8.00%
				7.30%*	-15.50%
As at 30 June 2022	1.75%	2.00%	3.00%		

* Compound interest

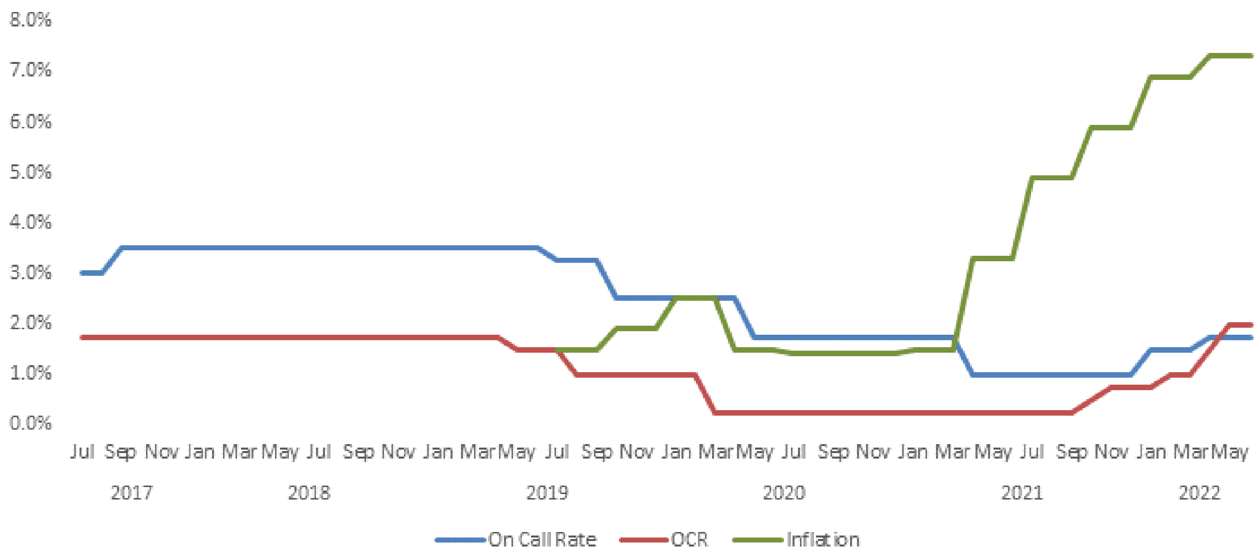
The Official Cash Rate rose from its record low of 0.25% to 2.0% by year end as inflation spiked dramatically, which led to sharp losses for the Long Term Fund

On Call Interest Rates

The PIF On Call rate started at 1.00% p.a. and ended the year at 1.75%. After keeping the Official Cash Rates at record lows in order to support the economy through the Covid pandemic, the RBNZ commenced a series of rate increases in an effort to curb price rises. The dramatic re-appearance of inflation surprised everyone, a function of record low interest rates, Covid-related government spending and global supply issues caused first by Covid and then the war in Ukraine.

Chart 2 below tracks the PIF On Call Interest Rate with the Official Cash Rate (OCR) over the last five years, and inflation over the last three years.

Chart 2: Annual PIF Interest Rates versus the Official Cash Rate and Inflation



Interest rates have started to rise again as inflation surges

The On Call PIF rate, which remained well above the Official Cash Rate (OCR) throughout the pandemic period, also increased over the course of the year, although by year-end, the OCR was just ahead.

Long Term Interest Rates

The PIF Long Term regular interest rate remained at 3.0% p.a. for the year (the same as last year). Inflation Interest, based on Statistics New Zealand's Consumer Price Index, was paid quarterly. This compounded to 7.30% for the year, significantly higher than the 3.30% paid last year.

In an ideal world, the investments that underpin the Long Term Fund would have generated 10.30%, to match the total of regular Interest and Inflation Interest paid for the year. Unfortunately, after generating strong returns through the period of the pandemic, the aftermath has been a different story. Surging inflation and rising interest rates resulted in sharp losses for both shares and bonds, delivering some of the worst losses ever experienced by diversified investment funds.

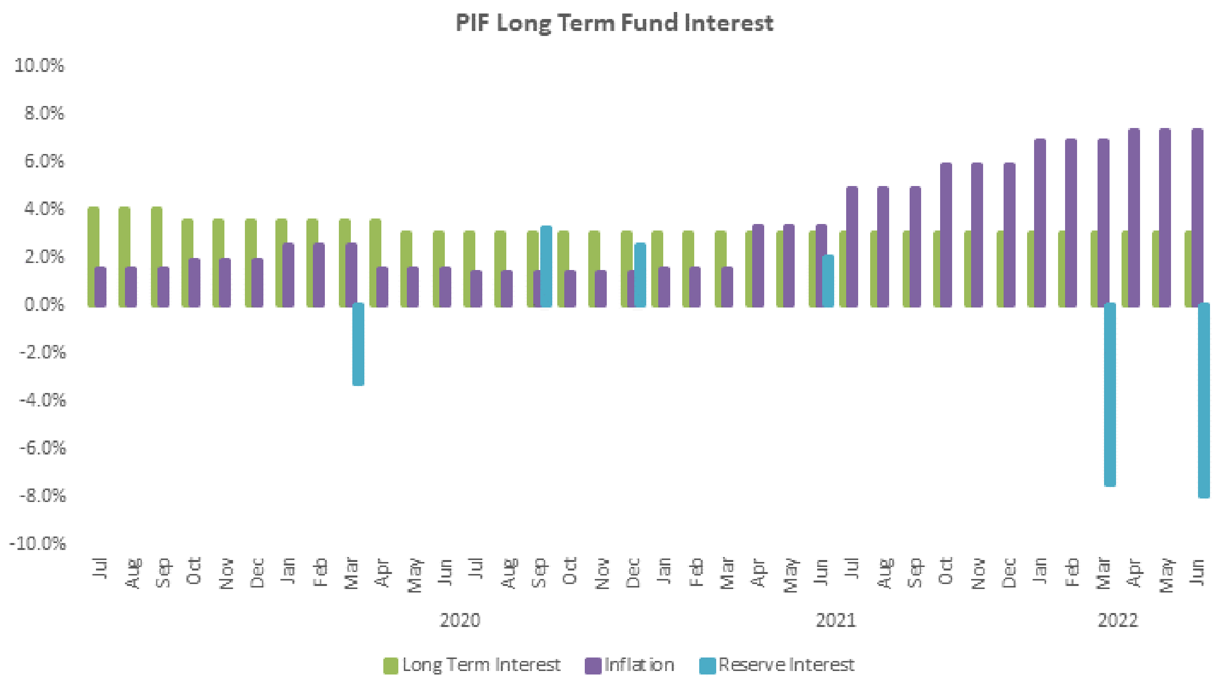
Last year, investment returns were higher than the total of regular Interest and Inflation Interest, leading to positive Reserve Interest. However, this year, the Long Term Fund's investments fell by around 8%, most of which occurred in the first six months of 2022. As a result, the PIF posted negative Reserve Interest for the year of -15.50% (with some reserves being used to soften the impact of falling markets).

Table and Chart 3 below show the breakdown of PIF Long Term Interest over the last three years

Table 3: Long Term Interest Paid for years to 30 June

	Regular Interest	Inflation Interest	Reserve Interest	Total Interest
2020	3.50%	1.50%	(3.25%)	1.75%
2021	3.00%	3.30%	7.75%	14.35%
2022	3.00%	7.30%	(15.50%)	(5.20%)

Chart 3: Long Term Interest Paid over time



Investment returns have been quite variable over the last three years

Why does the Long Term Fund have three different types of interest?

The Long Term Fund provides three different types of interest to help account-holders manage the natural variability of returns from this type of investment.

Because the Fund is invested in a diversified fund, investment returns will vary quarter to quarter and year to year. If the PIF was to provide a single interest amount each quarter, this would also vary, making it difficult for parishes to know how much of the interest they could spend.

So, the PIF breaks down Long Term Interest into:

1. Inflation Interest – by separating this amount out, we know how much we need to increase the balance by to maintain the real spending power of the capital. As the capital balance increases over time, so does the regular Interest.
2. Regular Interest – is set at 3%, which is the expected average return (after inflation) from the Long Term Fund's investments over the long term (at least 7 years). This is the amount we believe parishes can spend each year.
3. Reserve Interest – is the difference between what the investments deliver and how much is paid out in regular Interest and Inflation Interest. When market returns are higher, Reserve Interest will be positive. When market returns are lower, Reserve Interest will be negative. We recommend parishes treat this movement much like an unrealised gain or loss: it is only really relevant if and when the parish decides to withdraw the balance.

The Long Term Fund requires patient investing.

There will be ups and downs along the way,

But we expect account-holders will be rewarded for their patience.

Where to from here for interest rates?

In last year's report we noted that markets expected interest rates to continue to climb above 1% in 2022 and above 2% in 2023. So much for the experts! Markets are now forecasting that the Official Cash Rate could reach 5.5% in 2023. The exact path will depend on inflation.

The PIF On Call Fund interest rate is inextricably linked to short-term interest rates. It is therefore likely that the PIF On Call interest rate will follow cash rates up, albeit with a lag (in the same way that the PIF rate lagged the Official Cash Rate on the way down).

Higher PIF On Call rates might sound like good news for parishes, but while the rate of inflation exceeds interest rates, balances are actually going backwards in real (inflation-adjusted) terms.

The Long Term regular interest rate will likely remain at 3% plus inflation. The key question for Long Term Fund account-holders is, what will investment returns do? This will determine whether or not Reserve Interest will be positive or negative. While inflation remains high, the hurdle for the Long Term Fund remains high. Just as we didn't expect 2022 to deliver the same high return achieved in 2021, we don't expect 2023 to be quite as tough as this year. This is due, in part, to the fact that we are starting with higher interest rates, which means that bond returns will likely not be as poor. On the other hand, while share prices have fallen, they could fall further if we enter a recession.

The average total Long Term Fund return over the long term is expected to be 5% p.a. (3% interest plus 2% inflation).

PIF Loans

The PIF introduced loans to parishes (secured against a mortgage) two years ago. This year we introduced the ability for parishes to borrow secured by a guarantee from their presbytery. This facility requires less administration and as a result, allows the PIF to make smaller loans.

As at 30 June the PIF had one loan of $2m to a parish secured by a mortgage and one loan of $500,000 secured by a presbytery guarantee. Loan interest rates are set quarterly. The average rate at 30 June 2022 was 4.57%. After year end, two further loans have been advanced and interest rates have climbed further.

Service Providers

The Trustees have outsourced the provision of various PIF services to a range of specialist organisations. Harbour Asset Management (HAM) has managed the PIF's On Call Fund investment assets since July 2016 under a 'segregated mandate', which is tailored to our specific requirement that a high level of security and liquidity in the PIF's assets be maintained (along with our responsible investment requirement). Assets in the Long Term Fund are managed by Mercer. Trustees Executors Limited acts as custodian for the PIF, holding the investment assets in safekeeping, and providing accounting services. Booster provides account administration and online access for parishes and other account holders from the Presbyterian family. Ernst and Young are the Fund's auditors.

The Trustees are pleased to report that Administration expenses fell slightly for the year (from $705,899 to $688,026), despite an increase in the size of the Fund.

Expenses fell for the second year in a row.

Thank you to all the account holders and our service providers for another successful year for the Presbyterian Investment Fund.

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Full accounts are available at:
The Presbyterian Church Property Trustees: www.presbyterian.org.nz