

STATEMENT OF INVESTMENT POLICY AND OBJECTIVES

FOR

Lifestages Australasian Equity Portfolio

**Manager:
Funds Administration New Zealand Limited (FANZ)**

**Supervisor:
Trustees Executors Limited**

Effective Date: 30 November 2016

Introduction and description of Fund

This statement of investment policy and objectives ("**SIPO**") takes effect from 30 November 2016 and has been prepared for the Lifestages Australasian Equity Portfolio (the "**Fund**"). This SIPO replaces the previous SIPO for the Fund dated 1 October 2015.

The Fund is a registered managed investment scheme under the Financial Markets Conduct Act 2013 ("**Act**"). It forms part of the Lifestages Investment Funds, a suite of registered managed investment schemes, governed by a master trust deed, and managed by Funds Administration New Zealand Limited (referred to as "**we**", "**our**", and "**us**" in this SIPO).

The Supervisor of the Fund is Trustees Executors Limited ("**Supervisor**").

Within our organisation, the Executive Director is responsible for ensuring the SIPO is implemented and monitoring that implementation during the investment cycle (see section 8).

This SIPO sets out the following details with respect to the Fund:

| | |
|---|----|
| 1. Benchmarks and Investment Objectives | 3 |
| 2. Investment Philosophy | 3 |
| 3. Eligible Investments..... | 3 |
| 4. Investment Guidelines..... | 4 |
| 5. Authorised Investments..... | 4 |
| 6. Authorised Activities | 5 |
| 7. Investment policies | 5 |
| 8. Monitoring..... | 6 |
| 9. Review and update of SIPO | 7 |
| 10. Useful definitions | 10 |

Our Investment Strategy for the Fund is contained in sections 3 to 7.

In the event of conflict between the provisions of this SIPO and the master trust deed ("**Trust Deed**") or deed of establishment ("**Establishment Deed**") for the Fund, the provisions of the Trust Deed or Establishment Deed (as applicable) will prevail.

An explanation of the terms used in this SIPO is provided in the final section of this SIPO.

1. Benchmarks and Investment Objectives

- 1.1. **Benchmark:** The benchmark asset allocations and indices for the Fund (“**Benchmark**”) are:
- (a) **5% NZ Cash:** NZX NZ 90 Day Bank Bill Index
 - (b) **65% New Zealand Equities:** S&P/NZX 50 Gross Index
 - (c) **30% Australian Equities:** S&P/ASX 300 Accumulation Index in NZD.
- 1.2. **Investment objectives:**
- The Fund’s investment objectives are:
- (a) To achieve capital growth and returns over the long-term.
 - (b) To provide a gross return above the return of the composite Benchmark, with net dividends reinvested, on a rolling three-year basis i.e. before tax, fees, and other expenses.
 - (c) To produce a competitive investment return relative to the relevant peer group (see ‘Monitoring’ below).
- 1.3. **General description of investments:** The Fund will invest primarily in a broad spread of New Zealand and Australian equities.

2. Investment Philosophy

- 2.1. We have developed the investment strategy for the Fund with reference to investors who are seeking a fund that aims to achieve capital growth and returns over the long-term through investment in New Zealand and Australian equities. The Fund invests in large cap New Zealand and Australian equities and is designed to provide investors with a core holdings of equities in these markets. We believe that markets are largely efficient, and engaging in active management or speculating in concentrated positions is only likely to increase volatility and costs.
- 2.2. The level of investment risk accepted will be in line with the overall risk profile of the leading indices of the New Zealand and Australian equity markets which will be reflected in the selection of securities within the Fund.
- 2.3. The Fund is designed to provide investors with a core risk exposure to Australasian equities. The Fund is designed to be consistent with our overall investment philosophy and approach to equity investing.
- 2.4. The Fund offers a multi-manager approach to equity investing by providing access to a number of Australasia’s most experienced equity investment teams.

3. Eligible Investments

As at the date of this SIPO, the Fund (through its underlying managers) will only invest in the following security types

- 3.1. Deposits, transferable obligations or other debt obligations of or guaranteed by a ‘registered bank’ under the Reserve Bank of New Zealand Act 1989 whose short term rating is at least A1 with a maturity of no more than 180 days at time of purchase. Floating rate notes with a final maturity of more than 180 days are not authorised (irrespective of the frequency of rate setting).

- 3.2. Shares issued under New Zealand or Australian legal jurisdiction of companies listed and traded on a recognised stock exchange or other trading system.
- 3.3. Derivative contracts, where the underlying risk relates to the shares referred to in 3.2. Eligible derivative contracts include interest rate futures, options, interest rate swaps, and credit default swaps. Options, swaps and credit default swaps must be entered with a counterparty with a minimum long-term credit rating of AA- and a current industry standard (International Swaps and Derivatives Agency) agreement must be in place between the counterparty and us or the underlying manager. The market value of the exposure must be fully covered by cash or backed by liquid physical assets.

Derivatives are to be measured on a notional face value basis and may not exceed 100% of the net market value of the Fund's investment portfolio.

Investment in collateralised debt obligations and collateralised loan obligations are not permitted.

Where an entity or an issuer is rated, that rating shall be by an internationally approved rating agency such as Standard & Poor's (or other rating agency acceptable to the Supervisor).

The eligible investments may change in the future (see section 5 below).

4. Investment Guidelines

- 4.1. **Liquidity:** A minimum 2% of total assets must be held in highly liquid securities. Highly liquid securities are on-call Cash, NZ Government securities with less than 5 years to maturity and Bank Reverse Convertible Debentures with less than 6 months to maturity.
- 4.2. **Ranges:** The benchmark asset allocation ranges outlined in Table 1 are not to be exceeded.
- 4.3. **Hedging:** The Fund's Australian dollar exposure is not hedged to the New Zealand dollar (although this can change in the future).
- 4.4. **Derivatives:** Derivatives may be used as a risk management tool where underlying investments create an overall portfolio exposure that we determine to be undesirable. It is envisaged that derivatives will not be used in the normal course of business. While derivatives may be used at our sole discretion, we will advise the Supervisor of any decision to do so, explaining the investment rationale and anticipated duration of the holding period of derivative contracts entered into.

5. Authorised Investments

The universe of authorised investments for the Fund is set out in its consolidated Establishment Deed dated 1 November 2016, as amended from time to time. Investments may be made by direct investment or by investments in underlying funds.

The underlying managers currently accessed are available in the most current Fund Update on the Fund's managed investment schemes register entry with the Registrar of Financial Service Providers at www.companiesoffice.govt.nz/disclose.

5.1. Exposure

Table 1. Benchmark asset allocations and ranges

| | Benchmark asset allocation % | Usual range % |
|----------------------|-------------------------------------|----------------------|
| New Zealand Cash | 5 | 2 – 10 |
| New Zealand Equities | 65 | 55 – 75 |
| Australian Equities | 30 | 20 – 40 |

Other than as outlined in the table above, there are no limits on the nature or type of investments that may be made, or on the proportion of each type of asset invested in. However any breaches of these limits will result in breach of the Limit Breaks Policy and require action as provided by section 167 of the Financial Markets Conduct Act.

5.2. **Managed Funds.** Investment in managed funds which achieve essentially the same ultimate exposure as would have been achieved by directly held securities, with the relevant benchmark asset allocation and ranges flowed through to any managed fund exposure.

5.3. **Cash.** Cash is generally held in the Fund's bank account, for cashflow management. Any other cash investments will be made by way of direct investment in unsecured deposits with SBS Bank, or with other registered banks or financial institutions pending investment into other assets.

All transactions will be undertaken through recognised market participants. For domestic transactions no settlement risk will be taken. For international transactions dealing only with entities whose short-term credit rating is at least A1 will minimise settlement risk.

6. Authorised Activities

The Fund may undertake the following other activities in carrying out its investment strategy:

- 6.1. **Securities Lending.** The Fund is authorised to lend up to 20% of its Gross Asset Value (as defined in the Trust Deed) to 'A' rated counterparties.
- 6.2. **New Issues.** Underwriting new issues of authorised debt and share issues.
- 6.3. **Borrowing.** As provided by clause 23.12 of the Trust Deed, the Fund is authorised to borrow up to 25% of its Gross Asset Value to invest in Authorised Investments, subject to the consent of the Supervisor.

7. Investment policies

7.1. Liquidity

Sufficient liquidity will be held to cover reasonably anticipated redemptions of units in the Fund and, if necessary, there is a general authorisation to borrow up to 5% of the market value of the Fund to cover settlement requirements. Such borrowing will be for a maximum period of 15 business days and in each instance the Supervisor will be advised. The

Supervisor may at any time require that no further borrowing shall be undertaken in respect of the Fund.

7.2. Valuation

The purchase price of securities entering the Fund will include purchase brokerage and sale values will be after brokerage has been deducted.

For assets under outside management, periodic valuation will be based on latest market prices (for equities the last sale and for bonds the mid-price). Deposits with banks and building societies will be valued at book value plus accrued interest. In the case of securities whose latest market price or yield is more than 5 business days old at least two broker opinions will be sought and the average of these will be the price for valuation purposes.

The valuation formula will include a provision for tax, supervisor fees, management fees, an estimate of other ongoing fees, costs and expenses, any exceptional fees and estimated disposal costs in order to establish the true 'cash' value of the Fund. For exiting and new unit holders this will be the basis of their exit and issue unit price respectively.

7.3. Derivatives

Derivatives may not be used to leverage the Fund, or if the effect is to increase the portfolio risk beyond what it would have been had the Fund comprised only directly held securities. That is, there will be no gearing effect and any derivative positions will be backed by physically held positions at the time that the risk on any derivative arrangement commences. It is accepted that during the term of a derivative arrangement some mismatch may occur between the value of the derivative and the value of its underlying security or portfolio position (up to a maximum of 10% either side of the market price).

7.4. Tax

The Fund is currently taxed as a Portfolio Investment Entity ("PIE") and as such complies with the relevant tax rules for PIEs.

7.5. Related Party Transactions

Transactions with related parties of us or the Supervisor are permitted, provided such transactions are permitted under the Trust Deed and the Act (where applicable). The key constraint is that such transactions must be entered into on ordinary commercial arm's-length terms. The Supervisor may also impose other terms on related party transactions from time to time.

7.6. Hedging

The purpose of Australian investment is diversification of markets rather than diversification of currencies. It is accepted that international market diversification will entail additional risk arising from foreign currency exposure. As practicable, the foreign currency risk will not be removed by currency hedging.

8. Monitoring

8.1. We will review the performance of the Fund and the underlying investment managers quarterly. This review will compare the return of the Fund and each component of its portfolio against the relevant Benchmark over the quarter. There will also be a Fund

review, at least annually, against its peers as determined by the FANZ Investment Committee, with input from the Supervisor where appropriate.

- 8.2. The performance standard expected to be observed is that the Fund's return over the period will be within the top two quartiles based on its respective universe of funds (i.e. the range of funds identified as peers of the Fund).
- 8.3. If performance does not meet this standard, the reason for the under-performance will be identified and appropriate action recommended.
- 8.4. Where two or more managers are responsible for the investment management of a specific part of the Fund, rebalancing between them will be through cash flows rather than from a periodic formal rebalancing.

9. Review and update of SIPO

The SIPO will be reviewed and updated from time to time. The most current version of the SIPO is available on the Fund's managed investment schemes register entry with the Registrar of Financial Service Providers at www.companiesoffice.govt.nz/disclose.

9.1. Review of the SIPO and investments generally

The SIPO will be reviewed from time to time by us and the Supervisor, and at least annually. An ad hoc review of the overall SIPO may be triggered by any of the below events occurring.

We review all investments on a quarterly basis. Performance is measured against appropriate benchmark indices. Where an underlying fund's performance is consistent with its mandate and in line with broad style and/or asset class returns, no further action will generally be taken.

However, an investment/underlying fund may be flagged for 'enhanced due diligence', and subjected to a higher degree of scrutiny for any one or more of the following reasons, where applicable:

- A change in the primary underlying manager/issuer
- A significant change in an underlying manager's or issuer's majority owner or ownership structure
- A greater than 25% fall in the investment/underlying fund's assets under management over a rolling one year period (due to redemptions, not market movements) or total investment/underlying fund assets falling below \$25 million at any time
- A change in the investment/underlying fund's investment style, diversification and/or risk factor tilting
- An increase in the investment/underlying fund's fees
- The investment/underlying fund shows persistent underperformance against a relevant benchmark. Persistent underperformance is defined as performance below benchmark on a three year basis minus fees, and a volatility measure appropriate for each investment/underlying fund

- An extraordinary event which we consider has impacted or may interfere with the investment/underlying manager/fund's ability to act in the future within the established fund mandate

Each quarter, we will review all recommended investments to ensure no investment/underlying fund has breached its own limits.

In general, if an investment/underlying fund has breached any threshold, we will undertake an analysis and written review. Depending on the nature and seriousness of the breach, the written review will include some or all of the following features:

- Review of the investment mandate
- Explanation of the breach and analysis of its seriousness
- Investigation with the investment/underlying fund management team
- Regression analysis and/or attribution analysis
- Peer review
- Reconfirmation, if the investment/underlying fund is still the preferred choice relative to other alternatives

If the investment/underlying fund requires enhanced due diligence due to underperformance, we will attempt to ascertain whether this underperformance is the result of the underlying manager taking mandated risks, which are acceptable, or non-mandated risks, which are generally unacceptable.

The decision to retain or terminate an investment/underlying fund cannot be determined by a simple formula. Selecting investment/underlying funds with above average performance over previous periods provides no increased likelihood of improving performance over subsequent periods. Our confidence in the underlying manager's ability to consistently deliver in accordance with the investment/underlying fund mandate in the future will play a part in the decision to retain or replace an investment/underlying fund.

Once an investment/underlying fund has been reviewed in relation to a specific threshold breach, then, assuming the investment/underlying fund retains its recommended status, it will only be re-reviewed with respect to that breach in 12 months' time (not every subsequent quarter). However, if the investment/underlying fund subsequently breaches any other threshold in the interim, this will prompt a new review in relation to the new breach.

9.2. Review of the investment strategy and underlying manager selection

FANZ undertakes a review of the investment strategy, the appropriateness of the benchmark asset allocations and ranges, and the performance and risk profiles of the asset class on a regular basis. This is a qualitative review and forms part of the manager review of the managers used in the Fund.

We follow a due diligence process for selecting the underlying managers within each Fund, applying a combination of three primary filters.

Exclusionary filters

- **Investment style and philosophy** – investments should be non-speculative and compatible with an asset class investment philosophy. This philosophy is based on the assumption that markets are largely efficient, and engaging in active management or speculating in concentrated positions is only likely to increase volatility and costs.
- **Representation** – an investment must broadly represent the risk and return characteristics contained in a fair sample of an asset class or sub-asset class so that effective asset class and portfolio construction can be achieved.
- **Fund size** – an underlying recommended unit trust or exchange traded fund should have assets of \$25 million or more, unless there are exceptional circumstances.
- **Liquidity** – investments should be able to be redeemed for cash within one week.
- **Excluded investments** – none of the Fund's investments have exposure to cluster munitions, anti-personnel mines, or nuclear armament manufacturers.

Quantitative filters

- **Fees and expenses** – the Management Expense Ratio (MER) or Investment Cost Ratio (ICR) should be lower than average for the available funds in the relevant asset class.
- **Quality of execution** – a managed fund should demonstrate low turnover and light market impact of trading.
- **Diversification** – a fund should own the majority of available securities within its defined asset class or sub-asset class.
- **Consistency of risk exposure** - a fund should demonstrate consistency in the application of risk exposures, regardless of market or economic conditions.
- **Tax efficiency** – investments should be managed sensitive to the underlying taxable consequences of transacting.
- **Track record** – the fund should typically have a minimum track record of at least 12 months.
- **Performance since inception vs benchmark** – the fund should demonstrate that it is capturing the return of the asset class. In some cases, suitable benchmarks may not be available, and the adviser will take that into consideration.

Qualitative filters

For all managers recommended, we undertake a qualitative review of information every three years, focusing on items such as:

- **Ownership structure/major shareholders** – the company should demonstrate a consistent and stable ownership structure. Mergers and acquisitions should provide benefit to investors.
- **Staff** – the company should demonstrate low turnover of professional and service staff and long running tenure of key investment managers running the fund.

- **Services provided** – the company should provide the same or better level of service than is available in the marketplace for investment alternatives.
- **Business strength** – the company should be a growing and viable business. Growth in investment assets would be one indicator of this.
- **Reports** – the reports should contain all of the information that is necessary and useful to enable regular due diligence, and should consistently be provided on a timely basis.
- **Requests for information** – the company should consistently respond to requests for information in a timely manner with information given in a way that is easily understood.
- **Investment education** – the company should provide adequate explanation of and education around its investment decisions, and the evidence it considered in making decisions.

9.3. Changes to the SIPO

Both we and the Supervisor must agree in writing any changes or replacements to this SIPO. Any changes must be approved by our Board.

For material changes, we must provide 30 days' notice in advance to all existing unit holders of the proposed change. The decision as to whether or not a change is material rests with the Supervisor.

Each updated or amended SIPO will contain an effective date. Any changes to this SIPO will be lodged with the Registrar of Financial Service Providers in accordance with the Act.

10. Useful definitions

For the purposes of this SIPO:

“Benchmark” means the asset allocations and indices against which we measure the performance of the Fund as outlined at section 1.1 of this SIPO.

“Benchmark asset allocation” means the Fund's long-term average expected weighting for each type of asset (i.e. the proportion of the Fund's assets that we target to have invested in each type of asset). This is also referred to in other documents as its 'target asset allocation'. We invest within ranges agreed with the Supervisor, and actual exposures will vary over time.

“Credit Ratings” are ratings of the debtor's ability to pay back the debt by making timely interest payments and of the likelihood of default. An agency may rate the creditworthiness of issuers of debt obligations, the debt instruments, and/or in some cases, the servicers of the underlying debt, but not individual consumers. A poor credit rating indicates a credit rating agency's opinion that the company or government has a high risk of defaulting, based on the agency's analysis of the entity's history and analysis of long term economic prospects.

“Derivatives” means any financial arrangement traded on a recognised market or market system (and specifically not 'over the counter' securities) whose contribution to portfolio risk, after taking into account any gearing element within the derivative, is essentially no more than that of the security from which it is derived had that security been held ungeared.

“Equities” means shares of companies listed and traded on a recognised stock exchange or other trading system and any traded derivative of those shares whose contribution to portfolio risk, after taking into account any gearing element within the derivative, is essentially no more than that of the security from which it is derived had that security been held ungeared.

“Cash” means deposits guaranteed by entities whose short term rating is at least A1 with a maturity of no more than 180 days at the time of purchase. Floating rate notes with a final maturity of more than 180 days are not authorised (irrespective of the frequency of rate setting).

“Managed Funds” means units in a pooled arrangement or managed fund, which achieve essentially the same ultimate exposure as would have been achieved by directly held securities.

“Preference Shares” are a type of stock which may have any combination of features not possessed by common stock including properties of both equity and a debt instrument, and is generally considered a hybrid instrument.

Preference shares are senior (i.e., higher ranking) to common stock, but subordinate to bonds in terms of claim (or rights to their share of the assets of the company) and may have priority over common stock (ordinary shares) in the payment of dividends and upon liquidation. Terms of the preferred stock are described in the articles of association. Similar to bonds, preferred stocks are rated by the major credit-rating companies. The rating for preference shares are generally lower than for bonds because preferred dividends do not carry the same guarantees as interest payments from bonds and because preferred stock holders' claims are junior to those of all creditors.

“Underlying managers” are the underlying fund managers that we have appointed in respect of the Fund. The underlying managers are named in the most current Fund Update.

STATEMENT OF INVESTMENT POLICY AND OBJECTIVES

FOR

Lifestages Corporate Bond Portfolio

Manager:
Funds Administration New Zealand Limited (FANZ)

Supervisor:
Trustees Executors Limited

Effective Date: 30 November 2016

Introduction and description of Fund

This statement of investment policy and objectives (“**SIPO**”) takes effect from 30 November 2016 and has been prepared for the Lifestages Corporate Bond Portfolio (the “**Fund**”). This SIPO replaces the previous SIPO for the Fund dated 1 October 2015.

The Fund is a registered managed investment scheme under the Financial Markets Conduct Act 2013 (“**Act**”). It forms part of the Lifestages Investment Funds, a suite of registered managed investment schemes, governed by a master trust deed, and managed by Funds Administration New Zealand Limited (referred to as “**we**”, “**our**”, and “**us**” in this SIPO).

The Supervisor of the Fund is Trustees Executors Limited (“**Supervisor**”).

Within our organisation, the Executive Director is responsible for ensuring the SIPO is implemented and monitoring that implementation during the investment cycle (see section 8).

This SIPO sets out the following details with respect to the Fund:

| | |
|---|----|
| 1. Benchmark and Investment Objectives..... | 3 |
| 2. Investment Philosophy | 3 |
| 3. Eligible Investments..... | 3 |
| 4. Investment Guidelines | 4 |
| 5. Authorised Investments..... | 5 |
| 6. Authorised Activities | 6 |
| 7. Investment policies | 7 |
| 8. Monitoring..... | 8 |
| 9. Review and update of SIPO | 8 |
| 10. Useful definitions | 12 |

Our Investment Strategy for the Fund is contained in sections 3 to 7.

In the event of conflict between the provisions of this SIPO and the master trust deed (“**Trust Deed**”) or deed of establishment (“**Establishment Deed**”) for the Fund, the provisions of the Trust Deed (or Establishment Deed, as applicable) will prevail.

An explanation of the terms used in this SIPO is provided in the final section of this SIPO.

1. Benchmark and Investment Objectives

- 1.1. **Benchmark:** The benchmark asset allocation and index for the Fund is 100% S&P/NZX A-Grade Corporate Bond Index (“**Benchmark**”).
- 1.2. **Investment objectives:**
The Fund’s investment objectives are:
 - (a) Aim to provide a core and low risk exposure to New Zealand fixed interest debt securities;
 - (b) To provide a gross return above the return of the Benchmark on a rolling three-year basis i.e. before tax, fees, and other expenses; and
 - (c) To produce a competitive investment return relative to the relevant peer group (see ‘Monitoring’ below).
- 1.3. **General description of investments:** The Fund will invest in low to medium risk investments consisting of a broad spread of government and non-government securities primarily of investment grade quality. Any unrated securities will comply with our strict risk policy criteria through the underlying manager’s internal credit ratings process.

2. Investment Philosophy

- 2.1. We have developed the investment strategy for the Fund with reference to investors who are seeking a fund that aims to capture the yield premium attached to NZD-denominated government stock, corporate bonds and other non-Government fixed or floating rate securities. We believe that markets are largely efficient, and engaging in active management or speculating in concentrated positions is only likely to increase volatility and costs.
- 2.2. Duration management and tactical positioning will only be used to the extent that it results in the Fund’s duration being plus or minus two years either side of the Benchmark index position.
- 2.3. The level of investment risk accepted will be low to medium which will be reflected in the selection of securities within the Fund.
- 2.4. The Fund is designed to provide investors with a core and low risk exposure to New Zealand Fixed interest debt securities. The Fund is designed to be consistent with our overall investment philosophy and approach to low risk fixed interest investing. This approach aims to provide our clients with “no surprises” in terms of their fixed interest investments.
- 2.5. The Fund offers a multi manager approach to fixed interest investing by providing access to some of New Zealand’s most experienced fixed interest investment teams.

3. Eligible Investments

As at the date of this SIPO, the Fund (through its underlying managers) will only invest in the following cash, deposit or other security types denominated in New Zealand Dollars:

- 3.1. On-call cash or bank deposits at a 'registered bank' under the Reserve Bank of New Zealand Act 1989 with a minimum long-term credit rating of BBB- from the Fitch ratings agency.
- 3.2. Debt securities denominated in New Zealand Dollars that have a long-term credit rating of not less than BBB-, or a short-term rating of not less than A3 from the Standard & Poor's ratings agency.
- 3.3. Preference shares denominated in New Zealand Dollars and issued under New Zealand or Australian legal jurisdiction with a long-term credit rating of not less than BBB- from the Standard & Poor's ratings agency.
- 3.4. Securities that qualify as Tier 1 capital for registered banks in New Zealand with a long-term credit rating of not less than BBB- from the Standard & Poor's ratings agency.
- 3.5. Unrated securities provided the underlying manager, in their judgement, determines that the issue would have a rating of not less than BBB- from Standard & Poor's rating agency, if a rating was sought.
- 3.6. Derivative contracts, where the underlying risk relates to New Zealand interest rates or credit risk. Eligible derivative contracts include interest rate futures, options, and interest rate swaps. Options, swaps and credit default swaps must be entered with a counterparty with a minimum long-term credit rating of AA- (Standard & Poor's rating) and a current industry standard (International Swaps and Derivatives Agency) agreement must be in place between the counterparty and us or the underlying manager. The market value of the exposure must be fully covered by cash or backed by liquid physical assets.

Derivatives are to be measured on a notional face value basis and may not exceed 100% of the net market value of the Fund's investment portfolio.

Investment in collateralised debt obligations, collateralised loan obligations or credit default swaps are not permitted.

The eligible investments may change in the future (see section 5 below).

4. Investment Guidelines

- 4.1. **Duration:** The duration of the Fund is to be kept within two years of the duration of the Benchmark. The duration implications of derivative products are to be considered included when calculating the Fund's weighted average duration.
- 4.2. **Yield Curve:** The underlying managers shall monitor the maturity bucket exposure of the portfolio to ensure no excessive yield curve exposures exist. A 'laddered' approach is sought.
- 4.3. **Liquidity:** A minimum 2% of total assets must be held in highly liquid securities. Highly liquid securities are on-call Cash, NZ Government securities with less than 5

years to maturity and Bank Reverse Convertible Debentures with less than 6 months to maturity.

- 4.4. **Credit Exposures:** The credit exposures outlined in Table 1 are not to be exceeded.
- 4.5. **Unrated security assessments:** are to be reviewed at least six monthly.
- 4.6. **Derivatives:** Derivatives may be used as a risk management tool where underlying investments create an overall portfolio exposure that we determine to be undesirable. It is envisaged that derivatives will not be used in the normal course of business. While derivatives may be used at our sole discretion, we will advise the Supervisor of any decision to do so, explaining the investment rationale and anticipated duration of the holding period of derivative contracts entered into.

5. Authorised Investments

The universe of authorised investments for the Fund is set out in its Establishment Deed dated 1 April 2002, as amended from time to time. The Fund's New Zealand fixed interest investments may be made by direct investment or by investments in underlying funds.

The underlying managers currently accessed are available in the most current Fund Update on the Fund's managed investment schemes register entry with the Registrar of Financial Service Providers at www.companiesoffice.govt.nz/disclose.

5.1. Credit Exposure

Table 1. Credit Exposure Limits

| | <i>Max % of Total Fund with Single Issuer</i> | <i>Max% of total Fund with Class of Issue</i> | <i>Credit Rating</i> |
|--|--|--|--|
| New Zealand Government Bonds | 100% | 100% | |
| Investment Grade Corporate Bonds (AAA to A-) | 10% | 60% | A- or better, A-2 or better Commercial Paper |
| Investment Grade Corporate Bonds (BBB+ to BBB-) | 3% | 15% (including unrated bonds that are not Local Authority) | BBB-, BBB and BBB+, A-3 Commercial Paper |
| NZ Local Government Funding Authority (LGFA) | 50% | 50% | |
| Other Local Authority Stock | 10% | 30% | if not rated, issue must be secured by rates |
| Registered Banks, including subordinate securities issued by bank-owned entities | 12% | 60% | A- or better |
| State Owned Enterprise Bonds | 10% | 40% | BBB+ or better |

| | <i>Max % of Total Fund with Single Issuer</i> | <i>Max% of total Fund with Class of Issue</i> | <i>Credit Rating</i> |
|--|--|--|-----------------------------|
| Unrated Corporate Bonds (Excluding Local Authority Stock) | 3% | 5% | Unrated with IC approval |
| Subordinate Debt, including Capital Notes and Bank Tier1 and Tier 2 securities, including Perpetual Debt | 3% | 20% | BBB- or better |
| Perpetual Debt | 2.5% | 10% | BBB- or better |

There are no specific benchmark asset allocations or minimum exposures for any of the specified types of investment, but the overall neutral benchmark asset allocation for this component of the Fund is 95%, with a maximum of 98% and a minimum of 87.5%. However any breaches of these limits will result in breach of the Limit Breaks Policy and require action as provided by section 167 of the Financial Markets Conduct Act.

- 5.2. **Managed Funds.** Investment in managed funds that meet or exceed in part or in full the objectives and risk characteristics of the Fund, with the relevant credit exposure limits flowed through to any managed fund exposure.
- 5.3. **Income Strategies.** Any other income strategies approved by the Supervisor which we consider fall within the parameters of the Fund's Authorised Investments (as set out in the Establishment Deed), appropriately reflect the risk profile of the Fund, and will contribute towards achieving its investment objectives. There are no limits on the extent to which the Fund's investment exposure may be obtained through Income Strategies.
- 5.4. **Cash.** Cash is generally held in the Fund's bank account, for cashflow management, and is limited to a maximum of 12.5% of the Fund's portfolio, a neutral benchmark of 5% of the portfolio and a minimum of 2% of the portfolio. Any other cash investments will be made by way of direct investment or by investments in unsecured deposits with SBS Bank, or with other registered banks or financial institutions pending investment into other assets.

All transactions will be undertaken through recognised market participants. For domestic transactions no settlement risk will be taken. For international transactions dealing only with entities whose short-term credit rating is at least A1 will minimise settlement risk.

6. Authorised Activities

The Fund may undertake the following other activities in carrying out its investment strategy:

- 6.1. **Securities Lending.** The Fund is authorised to lend up to 20% of its Gross Asset Value (as defined in the Trust Deed) to 'A' rated counterparties.

- 6.2. **New Issues.** Underwriting new issues of authorised debt and share issues.
- 6.3. **Borrowing.** As provided by clause 23.12 of the Trust Deed the Fund is authorised to borrow up to 25% of its Gross Asset Value to invest in Authorised Investments, subject to the consent of the Supervisor.

7. Investment policies

7.1. Liquidity

Sufficient liquidity will be held to cover reasonably anticipated redemptions of units in the Fund and, if necessary, there is a general authorisation to borrow up to 5% of the market value of the Fund to cover settlement requirements. Such borrowing will be for a maximum period of 15 business days and in each instance the Supervisor will be advised. The Supervisor may at any time require that no further borrowing shall be undertaken in respect of the Fund.

7.2. Valuation

The purchase price of securities entering the Fund will include purchase brokerage and sale values will be after brokerage has been deducted.

For assets under outside management, periodic valuation will be based on latest market prices (for equities the last sale and for bonds the mid-price). Deposits with banks and building societies will be valued at book value plus accrued interest. In the case of securities whose latest market price or yield is more than 5 business days old at least two broker opinions will be sought and the average of these will be the price for valuation purposes.

The valuation formula will include a provision for tax, supervisor fees, management fees, an estimate of other ongoing fees, costs and expenses, any exceptional fees and estimated disposal costs in order to establish the true 'cash' value of the Fund. For exiting and new unit holders this will be the basis of their exit and issue unit price respectively.

7.3. Derivatives

Derivatives may not be used to leverage the Fund, or if the effect is to increase the portfolio risk beyond what it would have been had the Fund comprised only directly held securities. That is, there will be no gearing effect and any derivative positions will be backed by physically held positions at the time that the risk on any derivative arrangement commences. It is accepted that during the term of a derivative arrangement some mismatch may occur between the value of the derivative and the value of its underlying security or portfolio position.

7.4. Tax

The Fund is taxed as a Portfolio Investment Entity and as such complies with the relevant legislation.

7.5. Related Party Transactions

Transactions with related parties of us or the Supervisor are permitted, provided such transactions are permitted under the Trust Deed and the Act (where applicable). The key constraint is that such transactions must be entered into on ordinary commercial arm's-length terms. The Supervisor may also impose other terms on related party transactions from time to time.

8. Monitoring

- 8.1. We will review the performance of the Fund and the underlying investment managers quarterly. This review will compare the return of the Fund and each component of its portfolio against the relevant index over the quarter. There will also be a Fund review, at least annually, against its peers as determined by the FANZ Investment Committee, with input from the Supervisor where appropriate.
- 8.2. The performance standard expected to be observed is that the Fund's return over the period will be within the top two quartiles based on its respective universe of funds (i.e. the range of funds identified as peers of the Fund).
- 8.3. If performance does not meet this standard, the reason for the under-performance will be identified and appropriate action recommended.
- 8.4. Where two or more managers are responsible for the investment management of a specific part of the Fund, rebalancing between them will be through cash flows rather than from a periodic formal rebalancing.

9. Review and update of SIPO

The SIPO will be reviewed and updated from time to time. The most current version of the SIPO will be available on the Fund's managed investment schemes register entry with the Registrar of Financial Service Providers at www.companiesoffice.govt.nz/disclose.

9.1. Review of the SIPO and investments generally

The SIPO will be reviewed from time to time by us and the Supervisor, and at least annually. An ad hoc review of the overall SIPO may be triggered by any of the below events occurring.

We review all investments on a quarterly basis. Performance is measured against appropriate benchmark indices. Where an underlying fund's performance is consistent with its mandate and in line with broad style and/or asset class returns, no further action will generally be taken.

However, an investment/underlying fund may be flagged for 'enhanced due diligence', and subjected to a higher degree of scrutiny for any one or more of the following reasons, where applicable:

- A change in the primary underlying manager/issuer
- A significant change in an underlying manager's or issuer's majority owner or ownership structure
- A greater than 25% fall in the investment/underlying fund's assets under management over a rolling one year period (due to redemptions, not market movements) or total investment/underlying fund assets falling below \$25 million at any time
- A change in the investment/underlying fund's investment style, diversification and/or risk factor tilting
- An increase in the investment/underlying fund's fees

- The investment/underlying fund shows persistent underperformance against a relevant benchmark. Persistent underperformance is defined as performance below benchmark on a three year basis minus fees, and a volatility measure appropriate for each investment/underlying fund
- An extraordinary event which we consider has impacted or may interfere with the investment/underlying manager/fund's ability to act in the future within the established investment/underlying fund mandate

Each quarter we will review all recommended investments to ensure no investment/underlying fund has breached its own limits.

In general, if an investment/underlying fund has breached any threshold, we will undertake an analysis and written review. Depending on the nature and seriousness of the breach, the written review will include some or all of the following features:

- Review of the investment mandate
- Explanation of the breach and analysis of its seriousness
- Investigation with the investment/underlying fund management team
- Regression analysis and/or attribution analysis
- Peer review
- Reconfirmation, if the investment/underlying fund is still the preferred choice relative to other alternatives

If the investment/underlying fund requires enhanced due diligence due to underperformance, we will attempt to ascertain whether this underperformance is the result of the underlying manager taking mandated risks, which are acceptable, or non-mandated risks, which are generally unacceptable.

The decision to retain or terminate an investment/underlying fund cannot be determined by a simple formula. Selecting investment/underlying funds with above average performance over previous periods provides no increased likelihood of improving performance over subsequent periods. Our confidence in the underlying manager's ability to consistently deliver in accordance with the investment/underlying fund mandate in the future will play a part in the decision to retain or replace an investment/underlying fund.

Once an investment/underlying fund has been reviewed in relation to a specific threshold breach, then, assuming the investment/underlying fund retains its recommended status, it will only be re-reviewed with respect to that breach in 12 months' time (not every subsequent quarter). However, if the investment/underlying fund subsequently breaches any other threshold in the interim, this will prompt a new review in relation to the new breach.

9.2. Review of the investment strategy and underlying manager selection

FANZ undertakes a review of the investment strategy, the appropriateness of the credit exposure limits, the performance and risk profiles of the asset class on a regular basis.

This is a qualitative review and forms part of the manager review of the managers used in the Fund.

We follow a due diligence process for selecting the underlying managers within each Fund, applying a combination of three primary filters.

Exclusionary filters

- **Investment style and philosophy** - investments should be non-speculative and compatible with an asset class investment philosophy. This philosophy is based on the assumption that markets are largely efficient, and engaging in active management or speculating in concentrated positions is only likely to increase volatility and costs.
- **Representation** - an investment must broadly represent the risk and return characteristics contained in a fair sample of an asset class or sub-asset class so that effective asset class and portfolio construction can be achieved.
- **Fund size** – an underlying recommended unit trust or exchange traded fund should have assets of \$25 million or more, unless there are exceptional circumstances.
- **Liquidity** - investments should be able to be redeemed for cash within one week.
- **Excluded investments** – none of the Fund's investments have exposure to cluster munitions, anti-personnel mines, or nuclear armament manufacturers.

Quantitative filters

- **Fees and expenses** - the Management Expense Ratio (MER) or Investment Cost Ratio (ICR) should be lower than average for the available funds in the relevant asset class.
- **Quality of execution** – a managed fund should demonstrate low turnover and light market impact of trading.
- **Diversification** - a fund should own the majority of available securities within its defined asset class or sub-asset class.
- **Consistency of risk exposure** - a fund should demonstrate consistency in the application of risk exposures, regardless of market or economic conditions.
- **Tax efficiency** - investments should be managed sensitive to the underlying taxable consequences of transacting.
- **Track record** - the fund should typically have a minimum track record of at least 12 months.
- **Performance since inception vs benchmark** - the fund should demonstrate that it is capturing the return of the asset class. In some cases, suitable benchmarks may not be available, and the adviser will take that into consideration.

Qualitative filters

For all managers recommended, we undertake a qualitative review of information every three years, focusing on items such as:

- **Ownership structure/major shareholders** - the company should demonstrate a consistent and stable ownership structure. Mergers and acquisitions should provide benefit to investors.
- **Staff** - the company should demonstrate low turnover of professional and service staff and long running tenure of key investment managers running the fund.
- **Services provided** – the company should provide the same or better level of service than is available in the marketplace for investment alternatives.
- **Business strength** – the company should be a growing and viable business. Growth in investment assets would be one indicator of this.
- **Reports** - the reports should contain all of the information that is necessary and useful to enable regular due diligence, and should consistently be provided on a timely basis.
- **Requests for information** - the company should consistently respond to requests for information in a timely manner with information given in a way that is easily understood.
- **Investment education** – the company should provide adequate explanation of and education around its investment decisions, and the evidence it considered in making decisions.

9.3. Changes to the SIPO

Both we and the Supervisor must agree in writing any changes or replacements to this SIPO. Any changes must be approved by our Board.

For material changes, we must provide 30 days' notice in advance to all existing unit holders of the proposed change. The decision as to whether or not a change is material rests with the Supervisor.

Each updated or amended SIPO will contain an effective date. Any changes to this SIPO will be lodged with the Registrar of Financial Service Providers in accordance with the Act.

10. Useful definitions

For the purposes of this SIPO:

“Benchmark” means the asset allocation and index against which we measure the performance of the Fund as outlined at section 1.1 of this SIPO.

“Benchmark asset allocation” means the Fund’s long-term average expected weighting for each type of asset (i.e. the proportion of the Fund’s assets that we target to have invested in each type of asset). This is also referred to in other documents as its ‘target asset allocation’. We invest within ranges agreed with the Supervisor, and actual exposures will vary over time.

“Cash” means deposits with the SBS Bank, or any other registered bank, with a maturity of no more than 180 days at the time of purchase. Floating rate notes with a final maturity of more than 180 days are not authorised (irrespective of the frequency of rate setting).

“Credit Ratings” are ratings of the debtor's ability to pay back the debt by making timely interest payments and of the likelihood of default. An agency may rate the creditworthiness of issuers of debt obligations, the debt instruments, and/or in some cases, the servicers of the underlying debt, but not individual consumers. A poor credit rating indicates a credit rating agency's opinion that the company or government has a high risk of defaulting, based on the agency's analysis of the entity's history and analysis of long term economic prospects.

“Derivatives” means any financial arrangement traded on a recognised market or market system (and specifically not ‘over the counter’ securities) whose contribution to portfolio risk, after taking into account any gearing element within the derivative, is essentially no more than that of the security from which it is derived had that security been held ungeared.

“Managed Funds” means units in a pooled arrangement or managed fund, which achieve essentially the same ultimate exposure as would have been achieved by directly held securities.

“Preference Shares” are a type of stock which may have any combination of features not possessed by common stock including properties of both equity and a debt instrument, and is generally considered a hybrid instrument.

Preference shares are senior (i.e., higher ranking) to common stock, but subordinate to bonds in terms of claim (or rights to their share of the assets of the company) and may have priority over common stock (ordinary shares) in the payment of dividends and upon liquidation. Terms of the preferred stock are described in the articles of association. Similar to bonds, preferred stocks are rated by the major credit-rating companies. The rating for preference shares are generally lower than for bonds because preferred dividends do not carry the same guarantees as interest payments from bonds and because preferred stock holders' claims are junior to those of all creditors.

“Underlying managers” are the underlying fund managers that we have appointed in respect of the Fund. The underlying managers are named in the most current Fund Update.

STATEMENT OF INVESTMENT POLICY AND OBJECTIVES

FOR

Lifestages World Bond Portfolio

Manager:
Funds Administration New Zealand Limited (FANZ)

Supervisor:
Trustees Executors Limited

Effective Date: 30 November 2016

Introduction and description of Fund

This statement of investment policy and objectives ("**SIPO**") takes effect from 30 November 2016 and has been prepared for the Lifestages World Bond Portfolio (the "**Fund**"). This SIPO replaces the previous SIPO for the Fund dated 1 October 2015.

The Fund is a registered managed investment scheme under the Financial Markets Conduct Act 2013 ("**Act**"). It forms part of the Lifestages Investment Funds, a suite of registered managed investment schemes, governed by a master trust deed, and managed by Funds Administration New Zealand Limited (referred to as "**we**", "**our**", and "**us**" in this SIPO).

The Supervisor of the Fund is Trustees Executors Limited ("**Supervisor**").

Within our organisation, the Executive Director is responsible for ensuring the SIPO is implemented and monitoring that implementation during the investment cycle (see section 8).

This SIPO sets out the following details with respect to the Fund:

| | |
|---|----|
| 1. Benchmark and Investment Objectives..... | 3 |
| 2. Investment Philosophy | 3 |
| 3. Eligible Investments..... | 4 |
| 4. Investment Guidelines | 4 |
| 5. Authorised Investments..... | 5 |
| 6. Authorised Activities | 7 |
| 7. Investment policies | 7 |
| 8. Monitoring..... | 8 |
| 9. Review and update of SIPO | 9 |
| 10. Useful definitions | 12 |

Our Investment Strategy for the Fund is contained in sections 3 to 7.

In the event of conflict between the provisions of this SIPO and the master trust deed ("**Trust Deed**") or deed of establishment ("**Establishment Deed**") for the Fund, the provisions of the Trust Deed or Establishment Deed (as applicable) will prevail.

An explanation of the terms used in this SIPO is provided in the final section of this SIPO.

1. Benchmark and Investment Objectives

- 1.1. **Benchmark:** The benchmark asset allocations and indices for the Fund are:
- (a) **5% NZ Cash:** NZX NZ 90 Day Bank Bill Index
 - (b) **95% International Fixed Interest:** Bloomberg Barclays Global Aggregate Index hedged into New Zealand dollars ("**Benchmark**").
- 1.2. **Investment objectives:**
- The Fund's investment objectives are:
- (a) To provide investors with a broadly diversified portfolio of international investment grade income securities;
 - (b) To provide a gross return in line with or greater than the Benchmark over a rolling three-year basis i.e. before tax, fees, and other expenses; and
 - (c) To produce a competitive investment return relative to the relevant peer group (see 'Monitoring' below)
- 1.3 **General description of investments:** The focus of the Fund is investment in international investment grade income securities.

2. Investment Philosophy

- 2.1. We have developed the investment strategy for the Fund with reference to investors who are seeking a fund that aims to provide investors with a broadly diversified portfolio of global fixed interest through investment in international investment grade income securities.

The Lifestages World Bond Portfolio is designed to provide investors with access to a large pool of offshore income producing investments. Investors can access a wider pool of fixed interest investments by investment internally which also reduces the risk and volatility of their overall investment portfolio.

To protect investors from concentration risk the Fund is subject to strict rules about diversification. These involve limits on the proportion of the Fund to be allocated at time of purchase to the paper of any single issuer.

The addition of global fixed interest has the benefit of increasing diversification within the portfolio, which reduces overall volatility. It also provides exposure to the expected returns of multiple yield curves, rather than a single domestic curve. Investing in hedged global fixed interest, along with domestic fixed interest, allows the flexibility to create a more diversified and less risky fixed interest portfolio. It is a transparent strategy that is designed to fit well into an overall portfolio.

- 2.2. We believe that markets are largely efficient, and engaging in active management or speculating in concentrated positions is only likely to increase volatility and costs.
- 2.3. Duration management and tactical positioning will only be used to the extent that it results in the Fund's duration being plus or minus five years either side of the Benchmark index position.
- 2.4. The level of investment risk accepted will be low to medium which will be reflected in the selection of securities within the Fund.
- 2.5. The Fund is designed to provide investors with exposure to a diversified portfolio of international investment grade income securities, hedged into New Zealand dollars. A

portion will be held in cash for liquidity. The Fund is designed to be consistent with our overall investment philosophy and approach to low to medium risk fixed interest investing. This approach aims to provide our clients with “no surprises” in terms of their fixed interest investments.

- 2.6. The Fund offers a multi manager approach to fixed interest investing, providing access to experienced fixed interest investment teams.

3. Eligible Investments

As at the date of this SIPO, the Fund (through its underlying managers) will only invest in the following cash, deposit or other security types:

- 3.1. On-call cash or bank deposits at a ‘registered bank’ under the Reserve Bank of New Zealand Act 1989 with a minimum long-term credit rating of BBB- from the Fitch ratings agency.
- 3.2. Fixed or floating rate debt and bond issues denominated in foreign currencies. These issues may include but are not limited to inflation indexed bonds, municipal and government bonds, mortgage related debt and corporate debt, and that are listed, traded or dealt in on regulated markets in the OECD and which may have fixed or floating interest rates. FX exposures are to be hedged back to NZD.
- 3.3. Derivative contracts, where the underlying risk relates to foreign currency-denominated interest rates or credit risk. Eligible derivative contracts include interest rate futures, options, interest rate swaps, and credit default swaps. Options, swaps and credit default swaps must be entered with a counterparty with a minimum long-term credit rating of AA- (Standard & Poor’s rating) and a current industry standard (International Swaps and Derivatives Agency) agreement must be in place between the counterparty and us or the underlying manager. The market value of the exposure must be fully covered by cash or backed by liquid physical assets.
- 3.4. Any other income strategies approved by the Supervisor and by the Board of FANZ.

Derivatives are to be measured on a notional face value basis and may not exceed 100% of the net market value of the Fund’s investment portfolio.

Investment in collateralised debt obligations is not permitted.

The eligible investments may change in the future (see section 5 below).

4. Investment Guidelines

- 4.1. **Duration:** The duration of the Fund is to be kept within +/- five years of the duration of the Benchmark.
- 4.2. **Yield Curve:** The underlying managers shall monitor the maturity bucket exposure of the portfolio to ensure no excessive yield curve exposures exist.
- 4.3. **Liquidity:** A minimum 2% of total assets must be held in highly liquid securities. Highly liquid securities are on-call Cash, NZ Government securities with less than 5 years to maturity and Bank deposits with less than 6 months to maturity.

- 4.4. **Credit Exposures:** The credit exposures outlined in 5.1 are not to be exceeded. The Fund is constructed to achieve a weighted average credit rating of A- on capital invested.
- 4.5. **Hedging:** The Fund's foreign currency exposure will be hedged back to the New Zealand dollar 100%.
- 4.6. **Derivatives:** Derivatives may be used as a risk management tool where underlying investments create an overall portfolio exposure that we determine to be undesirable. It is envisaged that derivatives will not be used in the normal course of business. While derivatives may be used at our sole discretion, we will advise the Supervisor of any decision to do so, explaining the investment rationale and anticipated duration of the holding period of derivative contracts entered into.

5. Authorised Investments

The universe of authorised investments for the Fund is set out in its consolidated Establishment Deed dated 1 November 2016, as amended from time to time. The Fund's New Zealand fixed interest investments may be made by direct investment or by investments in underlying funds.

The underlying managers currently accessed are available in the most current Fund Update on the Fund's managed investment schemes register entry with the Registrar of Financial Service Providers at www.companiesoffice.govt.nz/disclose.

5.1. Credit Exposure Limits

a. Risk Limits

Duration +/- 5 years versus the Benchmark

b. Credit Quality Minimums

The underlying managers will apply quality ratings using the higher of Moody's, Standard & Poor's or Fitch. If an issue is not rated by one of these rating agencies, then a rating will be determined within any parameters agreed with the Supervisor.

| | |
|------------------------------------|-----------|
| Minimum Average Portfolio Quality: | A- Rating |
| Minimum Issue Quality: | B- Rating |
| Minimum Commercial Paper Quality: | A2/P2 |

Should an issue be downgraded below these minimums, the underlying manager will determine the appropriate action (sell or hold) based on the perceived risk and expected return.

c. Concentration Limits

Concentrations within the Fund's portfolio will be limited to the following:

| | |
|--|-----------------------|
| Issue/Issuer: <ul style="list-style-type: none">- Sovereign debt of OECD governments and US agencies:- Supranational issuers:- Any others: | No limit 25% 5% |
| High Yield Securities (rated below BBB-): | 10% |
| Emerging Market Securities: (We use the World Bank definition for emerging markets which is based on GNP per capita calculation) | 20% |
| Mortgage Derivatives: | 10% |
| Structured Notes: | 5% |
| Preferred Securities: | 5% |
| Bank Loans: | 10% |

The percentages set out above are maximums. There are no specific benchmark asset allocations or minimum exposures. However any breach of these limits will result in a breach of the Limit Breaks Policy and require action as provided by section 167 of the Financial Markets Conduct Act.

- 5.2. **Managed Funds.** Investment in managed funds that meet or exceed in part or in full the objectives and risk characteristics of the Fund, with the relevant credit exposure limits flowed through to any managed fund exposure.
- 5.3. **Income Strategies.** Any other income strategies approved by the Supervisor which we consider fall within the parameters of the Fund's Authorised Investments (as set out in the Establishment Deed), appropriately reflect the risk profile of the Fund, and will contribute towards achieving its investment objectives. There are no limits on the extent to which the Fund's investment exposure may be obtained through Income Strategies.
- 5.4. **Cash.** Cash is generally held in the Fund's bank account, for cashflow management and is limited to a maximum of 12.5% of the Fund's portfolio, a neutral benchmark of 5% of the portfolio and a minimum of 2% of the portfolio. Any other cash investments will be made by way of direct investment or by investments in unsecured deposits with SBS Bank, or with other registered banks or financial institutions pending investment into other assets.

All transactions will be undertaken through recognised market participants. For domestic transactions no settlement risk will be taken. For international transactions dealing only with entities whose short-term credit rating is at least A1 will minimise settlement risk.

6. Authorised Activities

The Fund may undertake the following other activities in carrying out its investment strategy:

- 6.1. **Securities Lending.** The Fund is authorised to lend up to 20% of its Net Tangible Assets (“NTAs”) ‘A’ rated counterparties, with a counterparty credit limit of no more than 20% with any one party or 5% net risk exposure.
- 6.2. **New Issues.** Underwriting new issues of authorised debt.
- 6.3. **Borrowing.** As provided by clause 23.12 of the Trust Deed the Fund is authorised to borrow up to 25% of its Gross Asset Value to invest in Authorised Investments, subject to the consent of the Supervisor. The Fund is not permitted to borrow money to invest in securities for leverage and or for shorting purposes.

7. Investment policies

7.1. Liquidity

Sufficient liquidity will be held to cover reasonably anticipated redemptions of units in the Fund and, if necessary, there is a general authorisation to borrow up to 5% of the market value of the Fund to cover settlement requirements. Such borrowing will be for a maximum period of 15 business days and in each instance the Supervisor will be advised. The Supervisor may at any time require that no further borrowing shall be undertaken in respect of the Fund.

7.2. Valuation

The purchase price of securities entering the Fund will include purchase brokerage and sale values will be after brokerage has been deducted.

For assets under outside management, periodic valuation will be based on latest market prices (for equities the last sale and for bonds the mid-price). Deposits with banks and building societies will be valued at book value plus accrued interest. In the case of securities whose latest market price or yield is more than 5 business days old at least two broker opinions will be sought and the average of these will be the price for valuation purposes.

The valuation formula will include a provision for tax, supervisor fees, management fees, an estimate of other ongoing fees, costs and expenses, any exceptional fees and estimated disposal costs in order to establish the true ‘cash’ value of the Fund. For exiting and new unit holders this will be the basis of their exit and issue unit price respectively.

7.3. Derivatives

Derivatives may not be used to leverage the Fund, or if the effect is to increase the portfolio risk beyond what it would have been had the Fund comprised only directly held securities. That is, there will be no gearing effect and any derivative positions will be backed by physically held positions at the time that the risk on any derivative arrangement commences. It is accepted that during the term of a derivative arrangement some mismatch may occur between the value of the derivative and the value of its underlying security or portfolio position.

7.4. Hedging

The Fund's foreign currency exposure will be hedged back to the New Zealand dollar 100%.

7.5. Tax

The Fund is taxed as a Portfolio Investment Entity and as such complies with the relevant legislation.

7.6. Related Party Transactions

Transactions with related parties of us or the Supervisor are permitted, provided such transactions are permitted under the Trust Deed and the Act (where applicable). The key constraint is that such transactions must be entered into on ordinary commercial arm's-length terms. The Supervisor may also impose other terms on related party transactions from time to time.

8. Monitoring

- 8.1. We will review the performance of the Fund and the underlying investment managers quarterly. This review will compare the return of the Fund and each component of its portfolio against the relevant index over the quarter. There will also be a Fund review, at least annually, against its peers as determined by the FANZ Investment Committee, with input from the Supervisor where appropriate.
- 8.2. The performance standard expected to be observed is that the Fund's return over the period will be within the top two quartiles based on its respective universe of funds (i.e. the range of funds identified as peers of the Fund).
- 8.3. If performance does not meet this standard, the reason for the under-performance will be identified and appropriate action recommended.
- 8.4. Where two or more managers are responsible for the investment management of a specific part of the Fund, rebalancing between them will be through cash flows rather than from a periodic formal rebalancing.

9. Review and update of SIPO

The SIPO will be reviewed and updated from time to time. The most current version of the SIPO is available on the Fund's managed investment schemes register entry with the Registrar of Financial Service Providers at www.companiesoffice.govt.nz/disclose.

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The SIPO will be reviewed from time to time by us and the Supervisor, and at least annually. An ad hoc review of the overall SIPO may be triggered by any of the below events occurring.

We review all investments on a quarterly basis. Performance is measured against appropriate benchmark indices. Where an underlying fund's performance is consistent with its mandate and in line with broad style and/or asset class returns, no further action will generally be taken.

However, an investment/underlying fund may be flagged for 'enhanced due diligence', and subjected to a higher degree of scrutiny for any one or more of the following reasons, where applicable:

- A change in the primary underlying manager/issuer
- A significant change in an underlying manager's or issuer's majority owner or ownership structure
- A greater than 25% fall in the investment/underlying fund's assets under management over a rolling one year period (due to redemptions, not market movements) or total investment/underlying fund assets falling below \$25 million at any time
- A change in the investment/underlying fund's investment style, diversification and/or risk factor tilting
- An increase in the investment/underlying fund's fees
- The investment/underlying fund shows persistent underperformance against a relevant benchmark. Persistent underperformance is defined as performance below benchmark on a three year basis minus fees, and a volatility measure appropriate for each investment/underlying fund
- An extraordinary event which we consider has impacted or may interfere with the manager/fund's ability to act in the future within the established investment/underlying fund mandate

Each quarter, we will review all recommended investments to ensure no investment/underlying fund has breached its own limits.

In general, if an investment/underlying fund has breached any threshold, we will undertake an analysis and written review. Depending on the nature and seriousness of the breach, the written review will include some or all of the following features:

- Review of the investment mandate
- Explanation of the breach and analysis of its seriousness
- Investigation with the investment/underlying fund management team
- Regression analysis and/or attribution analysis
- Peer review

- Reconfirmation, if the investment/underlying fund is still the preferred choice relative to other alternatives

If the investment/underlying fund requires enhanced due diligence due to underperformance, we will attempt to ascertain whether this underperformance is the result of the underlying manager taking mandated risks, which are acceptable, or non-mandated risks, which are generally unacceptable.

The decision to retain or terminate an investment/underlying fund cannot be determined by a simple formula. Selecting investment/underlying funds with above average performance over previous periods provides no increased likelihood of improving performance over subsequent periods. Our confidence in the underlying manager's ability to consistently deliver in accordance with the investment/underlying fund mandate in the future will play a part in the decision to retain or replace an investment/underlying fund.

Once an investment/underlying fund has been reviewed in relation to a specific threshold breach, then, assuming the investment/underlying fund retains its recommended status, it will only be re-reviewed with respect to that breach in 12 months' time (not every subsequent quarter). However, if the investment/underlying fund subsequently breaches any other threshold in the interim, this will prompt a new review in relation to the new breach.

9.2. Review of the investment strategy and underlying manager selection

FANZ undertakes a review of the investment strategy, the credit limit exposures, duration risk and how the asset class fits into our portfolios, the performance and risk profiles of the asset class on a regular basis. This is a qualitative review and forms part of the manager review of the managers used in the Fund.

We follow a due diligence process for selecting the underlying managers within each Fund, applying a combination of three primary filters.

Exclusionary filters

- **Investment style and philosophy** - investments should be non-speculative and compatible with an asset class investment philosophy. This philosophy is based on the assumption that markets are largely efficient, and engaging in active management or speculating in concentrated positions is only likely to increase volatility and costs.
- **Representation** - an investment must broadly represent the risk and return characteristics contained in a fair sample of an asset class or sub-asset class so that effective asset class and portfolio construction can be achieved.
- **Fund size** - an underlying recommended unit trust or exchange traded fund should have assets of \$25 million or more, unless there are exceptional circumstances.
- **Liquidity** - investments should be able to be redeemed for cash within one week.
- **Excluded investments** – none of the Fund's investments have exposure to cluster munitions, anti-personnel mines, or nuclear armament manufacturers.

Quantitative filters

- **Fees and expenses** - the Management Expense Ratio (MER) or Investment Cost Ratio (ICR) should be lower than average for the available funds in the relevant asset class.

- **Quality of execution** - a managed fund should demonstrate low turnover and light market impact of trading.
- **Diversification** - a fund should own the majority of available securities within its defined asset class or sub-asset class.
- **Consistency of risk exposure** - a fund should demonstrate consistency in the application of risk exposures, regardless of market or economic conditions.
- **Tax efficiency** - investments should be managed sensitive to the underlying taxable consequences of transacting.
- **Track record** - the fund should typically have a minimum track record of at least 12 months.
- **Performance since inception vs benchmark** - the fund should demonstrate that it is capturing the return of the asset class. In some cases, suitable benchmarks may not be available, and the adviser will take that into consideration.

Qualitative filters

For all managers recommended, we undertake a qualitative review of information every three years, focusing on items such as:

- **Ownership structure/major shareholders** - the company should demonstrate a consistent and stable ownership structure. Mergers and acquisitions should provide benefit to investors.
- **Staff** - the company should demonstrate low turnover of professional and service staff and long running tenure of key investment managers running the fund.
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- **Business strength** - the company should be a growing and viable business. Growth in investment assets would be one indicator of this.
- **Reports** - the reports should contain all of the information that is necessary and useful to enable regular due diligence, and should consistently be provided on a timely basis.
- **Requests for information** - the company should consistently respond to requests for information in a timely manner with information given in a way that is easily understood.
- **Investment education** - the company should provide adequate explanation of and education around its investment decisions, and the evidence it considered in making decisions.

9.3. Changes to the SIPO

Both we and the Supervisor must agree in writing any changes or replacements to this SIPO. Any changes must be approved by our Board.

For material changes, we must provide 30 days' notice in advance to all existing unit holders of the proposed change. The decision as to whether or not a change is material rests with the Supervisor.

Each updated or amended SIPO will contain an effective date. Any changes to this SIPO will be lodged with the Registrar of Financial Service Providers in accordance with the Act.

10. Useful definitions

For the purposes of this SIPO:

“Benchmark” means the asset allocations and indices against which we measure the performance of the Fund as outlined at section 1.1 of this SIPO.

“Benchmark asset allocation” means the Fund’s long-term average expected weighting for each type of asset (i.e. the proportion of the Fund’s assets that we target to have invested in each type of asset). This is also referred to in other documents as its ‘target asset allocation’. We invest within ranges agreed with the Supervisor, and actual exposures will vary over time.

“Cash” means deposits with the SBS Bank, or any other registered bank, with a maturity of no more than 180 days at the time of purchase. Floating rate notes with a final maturity of more than 180 days are not authorised (irrespective of the frequency of rate setting).

“Credit Ratings” are ratings of the debtor's ability to pay back the debt by making timely interest payments and of the likelihood of default. An agency may rate the creditworthiness of issuers of debt obligations, the debt instruments, and/or in some cases, the servicers of the underlying debt, but not individual consumers. A poor credit rating indicates a credit rating agency's opinion that the company or government has a high risk of defaulting, based on the agency's analysis of the entity's history and analysis of long term economic prospects.

“Derivatives” means any financial arrangement traded on a recognised market or market system (and specifically not ‘over the counter’ securities) whose contribution to portfolio risk, after taking into account any gearing element within the derivative, is essentially no more than that of the security from which it is derived had that security been held ungeared.

“Managed Funds” means units in a pooled arrangement or managed fund, which achieve essentially the same ultimate exposure as would have been achieved by directly held securities.

“Underlying managers” are the underlying fund managers that we have appointed in respect of the Fund. The underlying managers are named in the most current Fund Update.

STATEMENT OF INVESTMENT POLICY AND OBJECTIVES

FOR

Lifestages World Equity Portfolio

Manager:
Funds Administration New Zealand Limited (FANZ)

Supervisor:
Trustees Executors Limited

Effective Date: 30 November 2016

Introduction and description of Fund

This statement of investment policy and objectives (“**SIPO**”) takes effect from 30 November 2016 and has been prepared for the Lifestages World Equity Portfolio (the “**Fund**”). This SIPO replaces the previous SIPO for the Fund dated 1 October 2015.

The Fund is a registered managed investment scheme under the Financial Markets Conduct Act 2013 (“**Act**”). It forms part of the Lifestages Investment Funds, a suite of registered managed investment schemes, governed by a master trust deed, and managed by Funds Administration New Zealand Limited (referred to as “**we**”, “**our**”, and “**us**” in this SIPO).

The Supervisor of the Fund is Trustees Executors Limited (“**Supervisor**”).

Within our organisation, the Executive Director is responsible for ensuring the SIPO is implemented and monitoring that implementation during the investment cycle (see section 8).

This SIPO sets out the following details with respect to the Fund:

| | |
|---|----|
| 1. Benchmarks and Investment Objectives | 3 |
| 2. Investment Philosophy | 3 |
| 3. Eligible Investments..... | 3 |
| 4. Investment Guidelines | 4 |
| 5. Authorised Investments | 4 |
| 6. Authorised Activities | 5 |
| 7. Investment policies | 5 |
| 8. Monitoring..... | 7 |
| 9. Review and update of SIPO | 7 |
| 10. Useful definitions | 11 |

Our Investment Strategy for the Fund is contained in sections 3 to 7.

In the event of conflict between the provisions of this SIPO and the master trust deed (“**Trust Deed**”) or deed of establishment (“**Establishment Deed**”) for the Fund, the provisions of the Trust Deed (or Establishment Deed, as applicable) will prevail.

An explanation of the terms used in this SIPO is provided in the final section of this SIPO.

1. Benchmarks and Investment Objectives

- 1.1. **Benchmark:** The benchmark asset allocations and indices for the Fund (“**Benchmark**”) are:
 - (a) **5% NZ Cash:** NZX NZ 90 Day Bank Bill Index
 - (b) **95% International Equities:** MSCI World Index in NZD with net dividends reinvested (50% hedged to the NZD).
- 1.2. **Investment objectives:**

The Fund’s investment objectives are:

 - (a) To achieve capital growth and returns over the long-term.
 - (b) To provide a gross return above the return of the composite Benchmark on a rolling three-year basis i.e. before tax, fees, and other expenses.
 - (c) To produce a competitive investment return relative to the relevant peer group (see ‘Monitoring’ below).
- 1.3. **General description of investments:** The Fund will invest primarily in a broad spread of international equities.

2. Investment Philosophy

- 2.1. We have developed the investment strategy for the Fund with reference to investors who are seeking a fund that aims to achieve capital growth and returns over the long-term through investment in international equities. The Fund provides access for investors to a portfolio of large cap stocks with a portion of the portfolio hedged back to the New Zealand dollar for risk management and volatility purposes.
- 2.2. We believe that markets are largely efficient, and engaging in active management or speculating in concentrated positions is only likely to increase volatility and costs.
- 2.3. The level of investment risk accepted will be largely in line with the Benchmark (50% hedged to the New Zealand dollar) which will be reflected in the selection of securities within the Fund.
- 2.4. The Fund is designed to provide investors with a core and large cap risk exposure to international equities. The Fund is designed to be consistent with our overall investment philosophy and approach to equity investing.
- 2.5. The Fund offers a multi manager approach to equity investing by providing access to a number of experienced international equity investment teams.

3. Eligible Investments

As at the date of this SIPO, the Fund (through its underlying managers) will only invest in the following security types:

- 3.1. Deposits, transferable obligations or other debt obligations of or guaranteed by a ‘registered bank’ under the Reserve Bank of New Zealand Act 1989 whose short term rating is at least A1 with a maturity of no more than 180 days at time of purchase. Floating rate notes with a final maturity of more than 180 days are not authorised (irrespective of the frequency of rate setting).

- 3.2. Shares issued in any jurisdiction of companies listed and traded on a recognised stock exchange or other trading system.
- 3.3. Derivative contracts, where the underlying risk relates to the shares referred to in 3.2. Eligible derivative contracts include interest rate futures, options, interest rate swaps, and credit default swaps. Options, swaps and credit default swaps must be entered with a counterparty with a minimum long-term credit rating of AA- and a current industry standard (International Swaps and Derivatives Agency) agreement must be in place between the counterparty and us or the underlying manager. The market value of the exposure must be fully covered by cash or backed by liquid physical assets.

Derivatives are to be measured on a notional face value basis and may not exceed 100% of the net market value of the Fund's investment portfolio.

Investment in collateralised debt obligations or collateralised loan obligations are not permitted.

Where an entity or an issuer is rated, that rating shall be by an internationally approved rating agency such as Standard & Poor's or AM Best.

The eligible investments may change in the future (see section 5 below).

4. Investment Guidelines

- 4.1. **Liquidity:** A minimum 2% of total assets must be held in highly liquid securities. Highly liquid securities are on-call Cash, NZ Government securities with less than 5 years to maturity and Bank Reverse Convertible Debentures with less than 6 months to maturity.
- 4.2. **Ranges:** The benchmark asset allocation ranges outlined in Table 1 are not to be exceeded.
- 4.3. **Hedging:** Foreign currency exposure is approximately 50% hedged to the New Zealand dollar, generally through the underlying investments.
- 4.4. **Derivatives:** Derivatives may be used as a risk management tool where underlying investments create an overall portfolio exposure that we determine to be undesirable. It is envisaged that derivatives will not be used in the normal course of business. While derivatives may be used at our sole discretion, we will advise the Supervisor of any decision to do so, explaining the investment rationale and anticipated duration of the holding period of derivative contracts entered into.

5. Authorised Investments

The universe of authorised investments for the Fund is set out in its consolidated Establishment Deed dated 1 November 2016, as amended from time to time. Investments may be made by direct investment or by investments in underlying funds.

The underlying managers currently accessed for the Fund's international equity investments are available in the most current Fund Update on the Fund's managed investment schemes register entry with the Registrar of Financial Service Providers at www.companiesoffice.govt.nz/disclose.

5.1. Exposure

Table 1. Benchmark asset allocations and ranges

| | Benchmark asset allocation % | Usual range % |
|------------------------|-------------------------------------|----------------------|
| New Zealand Cash | 5 | 2 – 10.0 |
| International Equities | 95 | 90 – 98 |

Other than as outlined in the table above, there are no limits on the nature or type of investments that may be made, or on the proportion of each type of asset invested in. However any breaches of these limits will result in breach of the Limit Breaks Policy and require action as provided by section 167 of the Financial Markets Conduct Act.

5.2. **Managed Funds.** Investment in managed funds which achieve essentially the same ultimate exposure as would have been achieved by directly held securities, with the relevant benchmark asset allocation and ranges flowed through to any managed fund exposure.

5.3. **Cash.** Cash is generally held in the Fund's bank account for cashflow management. Any other cash investments will be made by way of direct investment in unsecured deposits with SBS Bank, or with other registered banks or financial institutions pending investment into other assets.

All transactions will be undertaken through recognised market participants. For domestic transactions no settlement risk will be taken. For international transactions dealing only with entities whose short-term credit rating is at least A1 will minimise settlement risk.

6. Authorised Activities

The Fund may undertake the following other activities in carrying out its investment strategy:

6.1. **Securities Lending.** The Fund is authorised to lend up to 20% of its Gross Asset Value (as defined in the Trust Deed) to 'A' rated counterparties.

6.2. **New Issues.** Underwriting new issues of share issues.

6.3. **Borrowing.** As provided by clause 23.12 of the Trust Deed, the Fund is authorised to borrow up to 25% of its Gross Asset Value to invest in Authorised Investments, subject to the consent of the Supervisor.

7. Investment policies

7.1. Liquidity

Sufficient liquidity will be held to cover reasonably anticipated redemptions of units in the Fund and, if necessary, there is a general authorisation to borrow up to 5% of the market value of the Fund to cover settlement requirements. Such borrowing will be for a maximum period of 15 business days and in each instance the Supervisor will be advised. The Supervisor may at any time require that no further borrowing shall be undertaken in respect of the Fund.

7.2. Valuation

The purchase price of securities entering the Fund will include purchase brokerage and sale values will be after brokerage has been deducted.

For assets under outside management, periodic valuation will be based on latest market prices (for equities the last sale and for bonds the mid-price). Deposits with banks and building societies will be valued at book value plus accrued interest. In the case of securities whose latest market price or yield is more than 5 business days old at least two broker opinions will be sought and the average of these will be the price for valuation purposes.

The valuation formula will include a provision for tax, supervisor fees, management fees, an estimate of other ongoing fees, costs and expenses, any exceptional fees and estimated disposal costs in order to establish the true 'cash' value of the Fund. For exiting and new unit holders this will be the basis of their exit and issue unit price respectively.

7.3. Derivatives

Derivatives may not be used to leverage the Fund, or if the effect is to increase the portfolio risk beyond what it would have been had the Fund comprised only directly held securities. That is, there will be no gearing effect and any derivative positions will be backed by physically held positions at the time that the risk on any derivative arrangement commences. It is accepted that during the term of a derivative arrangement some mismatch may occur between the value of the derivative and the value of its underlying security or portfolio position.

7.4. Tax

The Fund is currently taxed as a Portfolio Investment Entity ("PIE") and as such complies with the relevant tax rules for PIEs.

7.5. Related Party Transactions

Transactions with related parties of us or the Supervisor are permitted, provided such transactions are permitted under the Trust Deed and the Act (where applicable). The key constraint is that such transactions must be entered into on ordinary commercial arm's-length terms. The Supervisor may also impose other terms on related party transactions from time to time.

7.6 Hedging

The purpose of international investment is diversification of markets rather than diversification of currencies. It is accepted that international market diversification will entail additional risk arising from foreign currency exposure. As practicable, this foreign currency risk will be removed by currency hedging. A complete hedge is not totally practical or cost efficient.

In view of this the policy position is that total foreign currency exposures will be approximately 50% hedged based on a periodic review with the 50% hedge ratio applied at the start of each period and applied to the then New Zealand dollar market value of the assets to be hedged. Hedging is generally through the underlying investments. Any hedges put in place at the most recent review, except in exceptional circumstances, will be left in place until the next review irrespective of interim movements in the prices of the underlying assets. For these purposes hedge rebalancing will be quarterly. In between times the hedge ratio will be allowed to move between 40% and 60%.

The approach to currency hedging is passive and there is no expectation or intention to actively manage currency exposures.

It is recognised that closing out currency hedge positions may involve payments from the funds whose currency exposure is hedged. Because there may be difficulty in controlling cash movements and recognising that it is overall portfolio currency exposure which is relevant, where possible hedged offshore investment management options will be taken within the overall 50% (approximately) guideline. It is further recognised that where the manager of an offshore investment hedges the foreign currency exposure only to Australian dollars putting in place a further hedge between Australian and New Zealand dollars may be both costly and logistically difficult. Given the relatively high correlation between Australian and New Zealand dollars it is considered that any exposure from holding uncovered Australian dollars is acceptable.

8. Monitoring

- 8.1. We will review the performance of the Fund and the underlying investment managers quarterly. This review will compare the return of the Fund and each component of its portfolio against the relevant index over the quarter. There will also be a Fund review, at least annually, against its peers as determined by the FANZ Investment Committee, with input from the Supervisor where appropriate.
- 8.2. The performance standard expected to be observed is that the Fund's return over the period will be within the top two quartiles based on its respective universe of funds (i.e. the range of funds identified as peers of the Fund).
- 8.3. If performance does not meet this standard, the reason for the under-performance will be identified and appropriate action recommended.
- 8.4. Where two or more managers are responsible for the investment management of a specific part of the Fund, rebalancing between them will be through cash flows rather than from a periodic formal rebalancing.

9. Review and update of SIPO

The SIPO will be reviewed and updated from time to time. The most current version of the SIPO is available on the Fund's managed investment schemes register entry with the Registrar of Financial Service Providers at www.companiesoffice.govt.nz/disclose.

9.1. Review of the SIPO and investments generally

The SIPO will be reviewed from time to time by us and the Supervisor, and at least annually. An ad hoc review of the overall SIPO may be triggered by any of the below events occurring.

We review all investments on a quarterly basis. Performance is measured against appropriate benchmark indices. Where an underlying fund's performance is consistent with its mandate and in line with broad style and/or asset class returns, no further action will generally be taken.

However, an investment/underlying fund may be flagged for 'enhanced due diligence', and subjected to a higher degree of scrutiny for any one or more of the following reasons, where applicable:

- A change in the primary underlying manager/issuer
- A significant change in an underlying manager's or issuer's majority owner or ownership structure
- A greater than 25% fall in the investment/underlying fund's assets under management over a rolling one year period (due to redemptions, not market movements) or total investment/underlying fund assets falling below \$25 million at any time
- A change in the investment/underlying fund's investment style, diversification and/or risk factor tilting
- An increase in the investment/underlying fund's fees
- The investment/underlying fund shows persistent underperformance against a relevant benchmark. Persistent underperformance is defined as performance below benchmark on a three year basis minus fees, and a volatility measure appropriate for each investment/underlying fund
- An extraordinary event which we consider has impacted or may interfere with the investment/underlying manager/fund's ability to act in the future within the established fund mandate

Each quarter, we will review all recommended investments to ensure no investment/underlying fund has breached its own limits.

In general, if an investment/underlying fund has breached any threshold, we will undertake an analysis and written review. Depending on the nature and seriousness of the breach, the written review will include some or all of the following features:

- Review of the investment mandate
- Explanation of the breach and analysis of its seriousness
- Investigation with the investment/underlying fund management team
- Regression analysis and/or attribution analysis
- Peer review
- Reconfirmation, if the investment/underlying fund is still the preferred choice relative to other alternatives

If the investment/underlying fund requires enhanced due diligence due to underperformance, we will attempt to ascertain whether this underperformance is the result of the underlying manager taking mandated risks, which are acceptable, or non-mandated risks, which are generally unacceptable.

The decision to retain or terminate an investment/underlying fund cannot be determined by a simple formula. Selecting investment/underlying funds with above average performance over previous periods provides no increased likelihood of improving performance over subsequent periods. Our confidence in the underlying manager's ability to consistently

deliver in accordance with the investment/underlying fund mandate in the future will play a part in the decision to retain or replace an investment/underlying fund.

Once an investment/underlying fund has been reviewed in relation to a specific threshold breach, then, assuming the investment/underlying fund retains its recommended status, it will only be re-reviewed with respect to that breach in 12 months' time (not every subsequent quarter). However, if the investment/underlying fund subsequently breaches any other threshold in the interim, this will prompt a new review in relation to the new breach.

9.2. Review of the investment strategy and underlying manager selection

FANZ undertakes a review of the investment strategy, the appropriateness of the benchmark asset allocations and ranges, and the performance and risk profiles of the asset class on a regular basis. This is a qualitative review and forms part of the manager review of the managers used in the Fund.

We follow a due diligence process for selecting the underlying managers within each Fund, applying a combination of three primary filters.

Exclusionary filters

- **Investment style and philosophy** – investments should be non-speculative and compatible with an asset class investment philosophy. This philosophy is based on the assumption that markets are largely efficient, and engaging in active management or speculating in concentrated positions is only likely to increase volatility and costs.
- **Representation** – an investment must broadly represent the risk and return characteristics contained in a fair sample of an asset class or sub-asset class so that effective asset class and portfolio construction can be achieved.
- **Fund size** – an underlying recommended unit trust or exchange traded fund should have assets of \$25 million or more, unless there are exceptional circumstances.
- **Liquidity** – investments should be able to be redeemed for cash within one week.
- **Excluded investments** – none of the Fund's investments have exposure to cluster munitions, anti-personnel mines, or nuclear armament manufacturers.

Quantitative filters

- **Fees and expenses** – the Management Expense Ratio (MER) or Investment Cost Ratio (ICR) should be lower than average for the available funds in the relevant asset class.
- **Quality of execution** – a managed fund should demonstrate low turnover and light market impact of trading.
- **Diversification** – a fund should own the majority of available securities within its defined asset class or sub-asset class.
- **Consistency of risk exposure** – a fund should demonstrate consistency in the application of risk exposures, regardless of market or economic conditions.

- **Tax efficiency** – investments should be managed sensitive to the underlying taxable consequences of transacting.
- **Track record** – the fund should typically have a minimum track record of at least 12 months.
- **Performance since inception vs benchmark** - the fund should demonstrate that it is capturing the return of the asset class. In some cases, suitable benchmarks may not be available, and the adviser will take that into consideration.

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“Derivatives” means any financial arrangement traded on a recognised market or market system (and specifically not ‘over the counter’ securities) whose contribution to portfolio risk, after taking into account any gearing element within the derivative, is essentially no more than that of the security from which it is derived had that security been held ungeared.

“Equities” means shares of companies listed and traded on a recognised stock exchange or other trading system and any traded derivative of those shares whose contribution to portfolio risk, after taking into account any gearing element within the derivative, is essentially no more than that of the security from which it is derived had that security been held ungeared.

“Cash” means deposits guaranteed by entities whose short term rating is at least A1 with a maturity of no more than 180 days at the time of purchase. Floating rate notes with a final maturity of more than 180 days are not authorised (irrespective of the frequency of rate setting).

“Managed Funds” means units in a pooled arrangement or managed fund, which achieve essentially the same ultimate exposure as would have been achieved by directly held securities.

“Preference Shares” are a type of stock which may have any combination of features not possessed by common stock including properties of both equity and a debt instrument, and is generally considered a hybrid instrument.

Preference shares are senior (i.e., higher ranking) to common stock, but subordinate to bonds in terms of claim (or rights to their share of the assets of the company) and may have priority over common stock (ordinary shares) in the payment of dividends and upon liquidation. Terms of the preferred stock are described in the articles of association. Similar to bonds, preferred stocks are rated by the major credit-rating companies. The rating for preference shares are generally lower than for bonds because preferred dividends do not carry the same guarantees as interest payments from bonds and because preferred stock holders’ claims are junior to those of all creditors.

“Underlying managers” are the underlying fund managers that we have appointed in respect of the Fund. The underlying managers are named in the most current Fund Update.