



STATEMENT OF INVESTMENT POLICY AND OBJECTIVES (SIPO)

Dated: 1 April 2024

MIDLANDS FUNDS MANAGEMENT LIMITED

Statement of Investment Policy and Objectives (“SIPO”) for the Midlands Smarter PIE Fund (the “Fund”)

EFFECTIVE DATE: 1 April 2024

The most current version of the SIPO is available on the *Disclose* register at www.business.govt.nz/disclose, and on the Manager's website at www.midlandsfundsmanagement.co.nz.

DESCRIPTION OF THE FUND

The Fund is a trust established under the Trustee Companies Act 1967 by a trust deed dated 1 October 2004 between Trustees Executors Limited (“Supervisor”) and Midlands Funds Management Limited (“Manager”), and is currently governed by an amended and restated trust deed dated 1 March 2024 (“Trust Deed”).

Roles and Responsibilities

The Manager is, among other things, responsible for managing the Fund’s investments and must ensure that the Fund has a statement of investment policy and objectives that provides adequately for the following matters:

- the nature or type of investments that may be made, and any limits on those;
- any limits on the proportion of each type of asset invested in; and
- the methodology used for developing and amending the investment strategy and for measuring performance against the investment objectives of the Fund.

The Supervisor is, among other things, responsible for holding the Fund’s assets and for supervising the performance by the Manager of its functions and obligations.

The Fund invests in loans secured by first mortgages of land and buildings in New Zealand, within defined lending ratios. The Fund also invests in cash and cash equivalents with registered banks. The Manager generally has the discretion as to which authorised investments are acquired, held or disposed of in and for the Fund.

INVESTMENT OBJECTIVES

Investment objective

The investment objective is to provide investors with an income return pre-tax (but after fees and expenses) at a level which exceeds the average of the four main New Zealand registered banks’ 90-day term deposit rates.

Investment policy

The policy of the Manager in relation to mortgage lending is to establish and maintain a broad range of mortgage investments with a mix of mortgage types, interest rates, maturity dates and physical locations of the mortgaged properties.

Cash and cash equivalents may be held with any registered bank (as defined under the Banking (Prudential Supervision) Act 1989). The policy of the Manager in relation to investing in cash and cash equivalents is to have a minimum of 5% held in cash and cash equivalents, as determined in accordance with GAAP, (target range is 5% - 25%) for the purpose of managing liquidity and pending investment in loans, and to have a variety of short term deposits up to 90 days to provide a balance between greater liquidity and higher interest returns.

INVESTMENT PHILOSOPHY

The Manager’s investment style and philosophy should be regarded as active. The Manager’s investment strategy is to balance the competing objectives of optimising returns versus operating within acceptable risk and liquidity parameters (as outlined elsewhere in this SIPO). The Manager’s belief when executing the strategy is that a conservative approach is preferred.

INVESTMENT STRATEGY

Authorised investments

There are restrictions on the types of investments the Fund can make, as set out in its Trust Deed and includes cash and cash equivalents and loans secured by a first-ranking mortgage.

Under the Trust Deed, the Fund must always be invested in “authorised investments” (as defined) and may only be invested in investments in which a group investment fund is permitted to invest in order to fall within the definition of a "designated group investment fund" as defined in section YA 1 of the Tax Act. In addition, for so long as the Fund is a PIE, and until such time as the Manager and Supervisor agree otherwise, the Fund shall only be invested in investments permitted for a PIE under section HM 11 of the Income Tax Act 2007 (or such other investments as may otherwise be permitted from time to time for eligibility to be a PIE under the PIE Rules).

Notwithstanding the range of authorised investments described in the Trust Deed, the Manager shall only invest the Fund pursuant to the specific policy guidelines, benchmark asset allocations, and lending limits described further below.

Specific policy guidelines

The specific investment policy guidelines determined by the Manager in relation to the Fund are as follows:

- **Interest rates and payment** - most investments by the Fund will be in mortgages with mostly floating interest rates but the Manager may maintain some fixed rate mortgages. Most borrowers pay interest on the first of each month. It is not the Manager's general practice to permit borrowers to capitalise the interest for the term of the loan, however, for certain projects and subject to specific lending criteria it may be allowed from time-to-time.
- **Lending Limits** - as set out below.
- **Cash and Cash Equivalents held for Operational Liquidity** - The Fund also holds cash and cash equivalents within the range of 5% – 25% of the Fund Value. The Manager shall maintain at least 5% of the Fund value in cash and cash equivalents to meet redemption requests and for the payment of the Fund's running expenses. Greater amounts of cash and cash equivalents may be held in times when the Manager determines that the Fund requires greater liquidity. The Fund's cash and cash equivalents (term deposits of up to 90 days) holdings may only be invested with registered banks.
- **Participating loans** - The Manager may invite third parties to participate in lending opportunities identified by the Manager, on terms agreed with the Supervisor. This could include the Manager participating in loans in its personal capacity, subject to compliance with the Trust Deed, the Financial Markets Conduct Act 2013 ("FMCA"), and any other relevant requirements. All such loans must fall within the guidelines set out above, except that the maximum exposure limits will be assessed by reference to the Fund's portion of the loan, not the full loan value.

Limitation on borrowings

The Fund may borrow, if the Manager (with the permission of the Supervisor) believes it is appropriate. The aggregate of the principal moneys borrowed and outstanding in respect of the Fund or secured against the investments of the Fund may not exceed 25% of the Fund's fund value.

Benchmark Asset Allocation Ranges - Mortgage Types and Cash and Cash Equivalents

The Fund will be spread between first mortgages against residential, commercial and rural properties, and cash and cash equivalents, within the following proportions (as to value) of the Fund value:

| | RESIDENTIAL | COMMERCIAL | RURAL | CASH AND CASH EQUIVALENTS |
|--------------------------|-------------|------------|----------|---------------------------|
| Limits of the Fund value | 10% - 75% | 15% - 75% | 0% - 50% | 5% - 25% |

Lending Limits (Valuation)

The Fund has Loan to Value ("LVR") lending limits, based on the amount of the loan when compared with the value of the mortgage security property at the time of loan approval, as follows:

| RESIDENTIAL MORTGAGES | COMMERCIAL MORTGAGES | RURAL MORTGAGES |
|---|---|--|
| Fee simple and cross lease land and buildings: up to 75% LVR | Fee simple and cross lease land and buildings: up to 66.7% LVR | Fee simple and cross lease: up to 60% LVR |
| | | Property used for dairy farming (fee simple and cross lease): up to 66.67% LVR provided collateral security is obtained over co-operative shares |
| Leasehold: up to 50% LVR | Leasehold: up to 50% LVR | Leasehold: up to 50% LVR |
| Vacant land: up to 50% LVR | Vacant land: up to 50% LVR | Vacant land: up to 50% LVR |

In addition, at the time of lending the following maximum exposure limits must be met:

- ▷ No more than 5% of the Fund value will be invested in any one mortgage or advanced to any one borrower or related group of borrowers.
- ▷ The total of the six largest exposures (including loans to a related group of borrowers) will not exceed 20% of the Fund value.

Registered valuations are required for all loans in excess of 50% of the rating valuation of a property. The rating valuation is only relied on when the property is inspected by the Manager (or their nominee). Where a registered valuation is required, it must be no older than 90 days prior to the date of loan approval.

As referred to above, all lending limits are determined and are solely applicable as at the initial loan approval date and at the date of any renewal of a loan. The value of any individual loan or the proportionate value of a loan in relation to the

Fund value may change subsequent to initial approval or renewal and, as a result, the above limits may sometimes be exceeded after those dates. This will not constitute a breach of this SIPO.

Appropriate benchmark index

The Fund is an exempt fund under the Financial Markets Conduct (Market Index) Exemption Notice 2023. That exemption notice exempts the Manager from providing market index comparisons to returns for the Fund if an appropriate market index is not available.

In addition, there is no peer group index for mortgage funds in New Zealand. Overseas indexes are not considered appropriate given the differences between New Zealand and overseas mortgage lending markets.

OTHER INVESTMENT POLICIES

Rebalancing policy

The assets of the Fund should be invested in line with its benchmark asset allocation. New lending determinations take these allocations into account. However, the allocation to each asset class will vary, due primarily to market movements, within the ranges set.

Given the relatively illiquid nature of mortgage loans, cash flow (either to or from the Fund) is the primary mechanism for ensuring that the asset allocation is maintained broadly in line with the benchmark asset allocation weightings for each asset class.

The exposure to the various asset classes is monitored monthly by the Manager's senior leadership team. If, at the end of a month, the allocation to a particular class has moved outside the ranges set out for that class, steps will be taken to bring back the asset allocation within the permitted ranges. This will typically occur through new lending in other asset classes, meaning there can be some lag in completing the rebalancing. A practical approach is taken to any rebalancing, with one of the objectives being to minimise transaction costs.

Hedging policy

The Manager does not hedge the Fund's interest rate exposures.

Conflict of interest policy

The Manager will only enter into transactions with related parties with the consent of the Supervisor and if the Manager certifies that any such transaction is on arm's length terms.

Liquidity and cash flow management policy

The Manager will maintain at least 5% of the Fund value in cash and cash equivalents to meet redemption requests and for the payment of the Fund's running expenses.

METHODOLOGY FOR MONITORING, AMENDING AND DEVELOPING INVESTMENT STRATEGY

Monitoring of underlying securities

The Manager closely reviews the loans once they are made to ensure that borrowers pay interest and principal as scheduled. Credit control and recovery functions are undertaken if payments are not made.

The Manager makes appropriate general and specific provisions for loss on the mortgage portfolio and these provisions are discussed with and reviewed annually by the auditor of the Fund.

Investment performance monitoring

The Manager monitors the Fund's investment performance as a continuous process and at least monthly. The Manager monitors the Fund's absolute performance, as well as its quarterly performance against the stated investment objective.

The Manager gives monthly reports to the Supervisor. The monthly reports include confirmation that all investments have been properly applied in accordance with the authorised investments of the Fund, that all calculations of the entitlements of investors and the valuation of units have been carried out in accordance with the Trust Deed provisions and that all proper accounting and internal control procedures have been maintained. In addition, it specifies the unit value, the aggregate number of units in the Fund on issue and such other information as the Supervisor may request.

The Manager also gives quarterly reports to the Supervisor on the performance of the Fund and adherence with the SIPO, including whether there have been any limit breaks. A limit break is a material breach of any limits set out in this SIPO in relation to the nature or type of investment that may be made or the proportion of each type of asset in which the fund is invested.

In accordance with the requirements of the FMCA and the Financial Markets Conduct Regulations 2014, the Manager will report to the Supervisor, as soon as is practicable, any limit breaks that have not been corrected within 5 business days after the date that the Manager became aware of the limit break.

Investment strategy review and amendment

This SIPO is formally reviewed by the directors of the Manager annually and may also be reviewed at any other time if the Manager considers that a review is required as a result of the prevailing market conditions or for any other reason.

In the course of the review the Manager's executive team will consider whether the Fund's benchmark asset allocations remain appropriate given the prevailing market conditions. Consideration will also be given as to whether the Fund's liquidity policy remains appropriate once again given prevailing market and economic conditions. The Manager's executive team will make recommendations to the Manager's directors, who will then consider such recommendations and implement as necessary.

In accordance with the FMCA, the Manager may amend or replace this SIPO only with the consent of the Supervisor. If the Manager proposes to alter the SIPO in a manner which materially affects existing investors then the Manager must, prior to effecting any such alteration, give at least 30 days' written notice to investors.



MIDLANDS



Midlands Funds Management Limited

P. 0800 870 326 / 06 870 3260 E. investments@mmt.net.nz

1/111 Karamu Road North, Hastings 4122 | PO Box 609 Hastings 4156 New Zealand

midlandsfundsmangement.co.nz

