

## 39. Central Finance Board of the Methodist Church

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### Summary statement of changes in unit holders' net assets

As at 28 February 2023

	<b>Net assets at 28/02/2022 £'000s</b>	<b>Net creations/ cancellations £'000s</b>	<b>Change in Net assets £'000s</b>	<b>Net assets at 28/02/2023 £'000s</b>
CFB UK Equity Fund	188,173	(113,059)	(11,724)	63,390
CFB Global Equity Fund	139,043	(84,937)	(4,317)	49,789
CFB Gilt Fund	4,849	1,457	(1,138)	5,168
CFB Corporate Bond Fund	97,150	(71,660)	(3,190)	22,300
CFB Short Fixed Interest Fund	14,959	(272)	(1,402)	13,285
CFB Managed Mixed Fund	30,709	(818)	(1,551)	28,340
CFB Methodist Council Medium Term Fund (*)	-	418	10,463	10,881
CFB Methodist Council Long Term Fund (*)	-	-	62,279	62,279
CFB Property Fund	25,764	(6,605)	(3,740)	15,419
CFB Deposit Fund	484,414	(131,197)	-	353,217
Less: CFB Deposit Fund balances in other CFB funds	(1,322)	(2,441)	-	(3,763)
<b>Total funds under management</b>	<b>983,739</b>	<b>(409,114)</b>	<b>45,680</b>	<b>620,305</b>

(\*) Excluding cross investment into other CFB Funds.

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### Chair's Report

#### Another year of change

I started this report last year with the heading "A year of change". Unfortunately, 2022/23 has also been a year of change that has seen a substantial loss of assets under management by the Central Finance Board (CFB) and a mini restructuring of the organisation in response to this. I must thank the connexional leadership and Methodist Council for their outstanding support during this period that has given us the time and space to continue our plans to replace these lost assets through the external market and Epworth Investment Management (Epworth). The year has also seen many successes which we should celebrate:

- The development of our Christian ethical presence as a witness in the Investment community, in particular the development of our Pillars document that gives a theological underpinning to our investment approach.
- The platforming of the Epworth charity clients to give them better service.
- The launch of our Christian ethical retail product so that individual Christians can invest in accordance with their values. This is a first for the UK.
- The award for Epworth of the 'Best Charity Investment Fund Management Firm' in the Wealth and Finance awards.

The Chief Executive Officer expands on these in his report.

#### A sharp decline in assets under management

I have reported previously on the Methodist pension schemes' (Schemes) long-term strategy to "de-risk" their asset portfolios by switching their equity portfolios held with the CFB into liability matching instruments managed by third parties. A recovery plan had been agreed with the lead employers in the Schemes that would lead to full disinvestment from the CFB by the Schemes by the next decade. In anticipation of this loss of assets over the next seven years, the CFB has been developing projects for new asset growth in Epworth. Members of the Schemes will be aware that the Schemes have been reporting deficits in their recent actuarial valuations – the assets that the schemes hold have been insufficient to meet the Schemes' future liabilities (ie the pensions of ministers and lay people). This has placed pressure upon the Church to finance this funding gap, something that the Connexional Treasurer addressed at the 2022 Methodist Conference. These deficits also led the Trustees of the Schemes to keep some of their investments with the CFB due to the need for investment growth to aid in the reduction of these deficits.

This financial situation changed dramatically last summer as the turmoil within the Conservative party led to a loss of confidence in the UK's investment markets and a

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sharp rise in the yield on UK Government Bonds. A key input to the actuarial valuation of the Schemes funding positions is Gilt yields as these are used to work out the present value of those future liabilities. With the surge in rates in August 2022 the net present value of these future liabilities fell sharply, meaning that the deficits in the schemes were substantially reduced. The Trustees therefore no longer needed to keep “risk on” in their asset portfolios and were able to move the substantial part of their portfolios held within CFB into liability matching assets held elsewhere. This is terrific news for the Church as a major financial concern has been addressed. Unfortunately for the CFB it meant that our assets under management fell by £382m, or 37%, during 2022.

### **Ethical exclusions hurt the CFB’s investment returns**

The extreme hardship suffered by Ukrainians continues as Putin’s War seems to be at a stalemate in the country’s east. Many sectors of the stock market have benefitted from these events; not least the oil and gas sector as Russia’s energy supplies to the West faced severe sanctions. Defence companies and high yielding sectors such as tobacco have also had good years. However, the ethical investment policies of the Joint Advisory Committee on the Ethics of Investment preclude investment from most of these sectors, leading to a difficult year for our equity portfolios. The CFB has received several emails from Church members questioning the decision to disinvest from the oil and gas sector. From an investment perspective the timing of the disinvestment was poor; from an ethics point of view the recent action of the oil and gas companies in increasing their capital expenditure on exploration for new reserves supports the decision of the Methodist Conference to disinvest. There has been a three-year long debate at Conference on the ethics of the oil and gas sector that required the CFB to undertake extensive research on the alignment of companies in this sector with a “well below two degrees” scenario. At the time, our research concluded that no oil and gas company was unambiguously aligned with the requirements of the Paris Accord; the events of the last year have confirmed this assessment.

### **The CFB’s financial position**

Last year I was reporting on a surplus in the CFB but was wary of the difficult financial markets that lay ahead after Russia’s invasion of Ukraine. I also warned of the accelerated path of disinvestment from the CFB that the Methodist pensions schemes were on following the rise in interest rates. Both of these strategic risks accelerated during 2022/23.

Ironically, Epworth received an industry award for the investment of Charity assets in the same week that it received notice from the pension schemes of their switch out

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of the majority of their risk assets with the CFB. The CFB Council reacted quickly and decisively to remediate this loss of income by entering into a period of consultation with staff that resulted in four redundancies. The costs of these redundancies are reflected in this year's trading position. Other cost cutting measures were implemented upon the withdrawal of assets by the Pension Schemes, but the CFB Council were determined to protect the resources committed to business development to ensure that the strategic plan to grow Epworth was given time to embed itself. A small fee increase was introduced on the Funds managed by the CFB but the Council limited these increases so that the Church does not pay fees any higher than those charged to third party clients by Epworth. In the CFB's "cost recovery" financial model, limiting the CFB fees in this way has contributed to the losses reported in 2022/23. I am therefore extremely grateful that, after the financial year end, the Methodist Council has confirmed to pay an additional management fee to the CFB of £500,000 to replace the lost revenue in 2022/23. This financial support is very welcome and greatly extends the window that Epworth has to grow its external business to replace the CFB's lost assets through the initiatives that the Chief Executive Officer describes in more detail in his report.

Since the difficult news of last autumn, the consolidated assets under management have shown good growth through better investment markets and new business in our Deposit Funds. We are fighting this trend as much as we can and I should express our gratitude to the custodian trustee, the Trustees for Methodist Church Purposes, in helping us maintain our position with Church clients. The CFB represents the voice of the Church in the UK's financial markets; a voice that we demonstrably use to improve the lives of individuals and the weakening of this voice is perhaps the most disappointing aspect of the last year.

### **Lending to the Church**

Last year I reported on a loan to the Methodist Council to support the financing of the purchase of new premises for the Connexional Team at Tavistock Place, London, which will become Methodist Church House. I am pleased to report that this loan was repaid without incident and that the CFB is now planning to join members of the Connexional Team in Tavistock Place next year. We were also approached by the Scheme trustees during the year who were concerned about potential liquidity risks during the extreme volatility of their leveraged Gilt positions with other managers during the market turmoil of the Truss Government. In the end, our assistance was not required but this incident was a good illustration of one of the benefits that the CFB provides to the Church is our ability to react quickly in times of financial crises.

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### **The Future**

The restructuring forced upon the CFB by the recent loss of assets and the focus upon new business growth in Epworth is the strategy for the future. A couple of years ago, the Council asked Epworth to focus its messaging on the good that investing using a Christian ethical overlay can do for the world. In the past I felt that we talked too much about what we should not do. This change of messaging has had a real impact and we regularly see Epworth and the CFB in the media and on-line feeds leading discussions on corporate behaviours. We are influencing the world for the better. While not wanting to diminish our current financial position, we have taken action to return to surplus and have an exciting growth plan. In particular, we can now not only serve the ethical needs of Charities but also serve the needs of the individual Christian investor. I am very optimistic about the future and that we will continue to be a voice in the investment community for the Methodist Church, the poor and the marginalised.

**John Sandford, Chair**

### **Chief Executive Officer's Report**

Firstly, may I express my thanks to everyone at the CFB, Council and colleagues, for their support and understanding during the difficult last year. I must also thank the broader Church which, generally, has been incredibly supportive and given us great encouragement to continue our work representing the Methodist Church in the financial markets. We are privileged to be part of this wonderful faith and I am looking forward to joining the Connexional Team in Tavistock Place next year.

### **Investment review of the year**

The last year has been a challenging one in many ways. While COVID is now largely in the rear-view mirror, there have been other challenges throughout this period which have, collectively, given people and investment markets a difficult time. Putin had just invaded Ukraine when we wrote our last report; one year on, there remains no sign of an end to the suffering created by this. Russian assets, notably fossil fuels, have been gradually removed from global supply chains as sanctions have tightened, and while this caused an acute spike in energy prices initially it has fallen back in recent months. On the positive side, global economic growth has been more resilient than expected in this environment, leading to higher than anticipated inflation in many markets. This has left many policymakers with difficult trade-offs to balance, between controlling inflation and raising interest rates while most people are feeling a cost-of-living squeeze.

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Equity markets have, against this backdrop been volatile but surprisingly resilient overall. UK equities have returned around 7% in the year to 28 Feb 2023. Our UK portfolio has struggled in this environment, particularly in the early part of the year where sectors that benefited from Putin's war effort rose and has returned 1.5% in the same period. A rotation away from growth stocks in 2022 hurt our relative performance, although this has reversed somewhat in 2023 to date. Global equities also gave a net positive return of around 2% over the twelve months. The CFB global equity fund returned -1% over the period, with similar factors impacting performance overall. Bond markets have fallen as interest rates have risen from their historic lows. This has meant we could increase the rate on the CFB Deposit Fund from its historic lows to an interest rate of over 3.60% at time of writing, but that the bond funds have achieved negative returns for the year to 28 February. Property returns started strong but became sharply negative as the year wore on and investors contemplated the impact of higher interest rates on the sector.

### **Ethical review**

Our theological motivation and focus remains at the forefront of all we do. As such, the CFB and Epworth have strengthened our theological grounding through the development of ethical pillars. These pillars underpin policies, keep the organisation grounded in its theology, and allow the CFB/Epworth to respond better to existing and emerging issues. The ethical pillars are guided by God's call to care for people and planet, and informed by the Wesleyan tradition of equality, fairness, individual responsibility, and societal care. The pillars are also linked to the United Nations Sustainable Development Goals (SDGs). CFB/Epworth supports the utilization of the SDGs, but feel that without a robust theological underpinning, they risk being misused by corporations or organizations attempting to appear ethical. By linking the theological pillars to the SDGs, the CFB/Epworth develops a common industry voice whilst better embedding theology into engagement action.

The development of these ethical pillars has enabled us to develop a more concise policy format that clearly outlines expectations we have for investee companies. This new format has already been applied and tested with the mining sector through a key collaborative activity where the CFB/Epworth serve as co-leads for Climate Action 100+'s Anglo American Engagement. Anglo American is a large, multinational diversified mining company specialising in the production of platinum, diamonds, copper, nickel and iron ore. As co-leads for Climate Action 100+ engagement with Anglo, we helped influence better climate performance at the miner. Notably, the miner has committed to reduce net emissions to zero in the long-term, publication of a detailed pathway of actions, publication of a scope 3 inventory, scenario analysis and improved governance and transparency on indirect lobbying.

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We also recognise the ongoing concerns within the Church surrounding the banking sector. From local branch closures to investment in fossil fuels, to activities with nations in violation of international law, the sector is not without its problems. We also recognise, however, the absolute importance of participating in the sector as individuals, institutions and investors, and the banks' essential role in fostering global markets. Plainly, the world simply needs banks, but it also needs banks to be better. Working alongside the Joint Advisory Committee on the Ethics of Investment, the CFB has published a sector specific policy on banks that seeks to better hold them to account and improve their practices through company engagement.

On 14 December 2022, HSBC announced it would no longer provide direct financing to new oil and gas fields, making it the world's biggest bank to do so. The CFB/Epworth felt this sent a strong market signal that banks appetite for financing new oil and gas is diminishing, as well as setting a new minimum standard for major European banks committed to net zero. HSBC's announcement was in direct response to engagement by ShareAction and investors, including the CFB/Epworth.

In the wake of HSBC's announcement to cease new fossil fuel project funding, the CFB/Epworth co-signed letters organised by ShareAction to Barclays and BNP Paribas, encouraging these banks to do the same and cease direct financing of new oil and gas fields.

We are also resolute in our commitment to play whatever part we can in supporting Ukraine during this time of illegal invasion by the Russian state. The CFB/Epworth do not hold any Russian securities directly, and both organisations have eliminated small indirect exposure to Russian companies through holdings of emerging market-focused vehicles.

We also seek to engage with investee companies where operations in Russia may still exist. After a series of engagements, the CFB was invited for high level discussion with the President of the Roman Catholic Bishops' Conference of England and Wales, Cardinal Vincent Nichols, and two of HSBC's senior advisors on human rights and policy. At the meeting with HSBC, we were able to challenge the bank on issues surrounding Hong Kong, Palestine, and Russia. Further discussion was had on the bank's approach to human rights and lending practices to the arms trade.

### **CFB Fund performance**

Where possible, the CFB funds are now all cross invested into the equivalent sub-Fund in the offering from Epworth, the Epworth Investment Fund for Charities. To show the impact of the Pension Schemes disinvestment, Fund values are shown at the end of 2021/22

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and 2022/23 in Table 1. The negative performance of the Equity funds over one year in comparison with the benchmarks, broadly reflect the impact of our ethical exclusions of companies that have benefitted from Russia's invasion of the Ukraine. The equity fund benchmarks are whole of market benchmarks, unadjusted for any ethical exclusions.

### The CFB's voting record

The CFB continues to be a very active investor. Our voting policy follows the agreed template of the Church Investors Group. Under the template most of the Christian investment bodies in the UK vote together on such issues as Executive pay and boardroom diversification. The CFB's voting record in 2022/23 is shown in Table 2.

**Table 1 - CFB fund performance summary**

To 28 February 2023

	Fund size	Fund size				
	28.02.22 £m	28.02.23 £m	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.
<b>CFB UK Equity Fund</b>	188.2	63.4	1.45	6.60	4.72	6.15
Benchmark			7.30	8.82	5.25	6.26
Excess return			-5.85	-2.22	-0.53	-0.11
<b>CFB Global Equity Fund</b>	139.0	49.8	-1.07	10.22	8.53	10.73
Benchmark			2.28	11.57	9.38	11.36
Excess return			-3.35	-1.28	-0.85	-0.63
<b>CFB Gilt Fund</b>	4.9	5.2	-21.43	-10.26	-3.87	-0.15
Benchmark			-21.24	-9.96	-3.47	0.26
Excess return			-0.19	-0.30	-0.40	-0.41
<b>CFB Corporate Bond Fund</b>	97.1	22.3	-11.67	-5.75	-1.42	1.44
Benchmark			-12.08	-5.12	-0.88	1.90
Excess return			+0.41	-0.63	-0.54	-0.46

All figures annualised and after fees

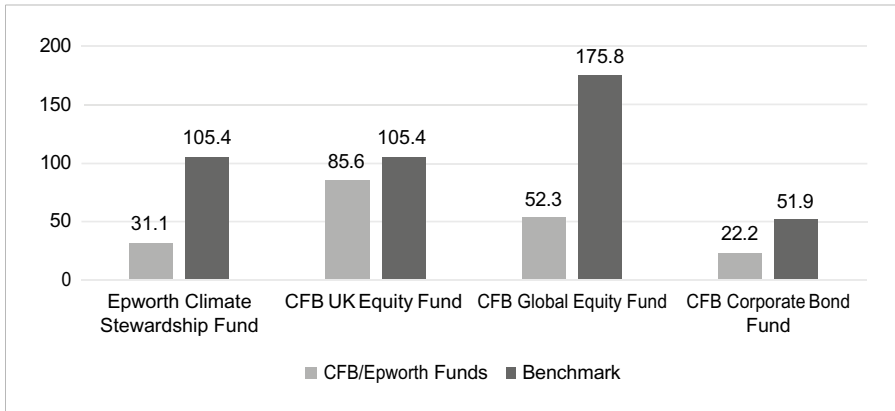


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**Table 2 - CFB voting record**  
Year to 28 February 2023

	For	Oppose	Abstain	Against or abstain
Auditors	418	2	0	0%
Directors	2,723	469	6	15%
Remuneration	129	234	4	65%
Executive Pay Scheme (UK)	29	20	0	41%
Shareholder Capital (Overseas)	108	9	0	8%
Other	1,772	129	31	8%
<b>Total</b>	<b>5,179</b>	<b>863</b>	<b>41</b>	<b>15%</b>

**Figure 1 - CFB/Epworth funds' carbon footprints (tCO2e/Mil USD)**



Sources for the above data chart - Sustainalytics for the equity funds, and Clarity AI for the Corporate Bond Fund.

### Carbon footprint

One of the other elements of fund performance that the CFB reports on is the relative carbon footprint of each fund. Figure 1 shows the latest figures on the carbon footprints of the funds, compared to the benchmark indices that they are measured against.

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### **CFB Deposit Fund**

Last year I was reflecting on the extremely low rates being paid to our Depositors by the CFB Deposit Fund. This has rapidly changed. As I write this the CFB is paying our Depositors 3.63%. The surge in inflationary pressures has led to central banks rapidly raising interest rates and we are now probably close to the top of the interest rate cycle. However, many banks are not passing the increase in wholesale rates onto their savers and hence we are seeing the CFB Deposit Fund offering a substantial uplift on the rates available from most banks' same day access accounts. In Epworth we have jumped on this opportunity to market the Epworth Cash Plus Fund to charities and this has led to some of the recovery in our assets under management reported by the Chair previously. With supply chains still imperilled and labour market struggles, we do not expect interest rates to fall significantly any time soon.

### **Portfolio clients**

Our portfolio offering to churches and charities has traditionally been based upon the Epworth funds, held in the client's own name. Whilst delivering our Christian approach to ethics, our toolbox for asset allocation decisions was relatively limited. Over the last six months we have been working with a third-party platform provider to migrate our portfolio clients onto an independent custodian and on-line valuation system. This platform greatly enhances our client experience, broadening our fund choice and giving clients daily access to their portfolio values. The Epworth Funds remain at the heart of our clients' equity exposure and any third party funds that we use undergo a stringent ethical screening before they are selected. I must extend my thanks to Sarah Bourgein, our Head of Client Relations, who has spent many hours with our clients reviewing their financial needs and appetite for risk and guiding them through the agreement and transfer process to move to the new platform. It has been a major commitment for the organization over the last year but it brings our portfolio offering into the modern world with a transparent fee structure, daily client access and active asset allocation.

### **Retail clients**

This time last year I advised that we were still waiting to hear from the UK regulator as to whether Epworth would be extended permission to handle general retail clients. I am pleased to report that this did come through and that last Autumn we formally launched our managed portfolio service (MPS) at the Association of Christian Financial Advisers. We use our Christian ethical overlay to screen potential investments and then our joint venture partner, Canaccord Genuity, manages the portfolios on various third-party platforms on our behalf.

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Currently our MPS is available to clients of Independent Financial Advisers (IFAs) on three platforms. This service is only available through IFAs due to the strict – and appropriate – rules concerning gathering of financial information, attitude to risk and understanding of a client's full financial affairs before making an investment into our MPS service. Epworth does not have the structure or staff to support a stand-alone retail offering at present. We expect this business to grow slowly but consistently; delivering us a broad client base that greatly reduces our reliance on a few core clients.

### **Taking environmental, social, and governance (ESG) thinking forward**

The ethical pillars that are described previously have been developed by our Chief Responsibility Officer, the Revd Dr Andrew Harper. He joined us in 2021 with a mandate to change our approach to ethical thinking; to change from a negative mindset to a positive one – not what we won't do, but what we can do. Andrew has delivered a foundational document for the CFB and Epworth that will be at the heart of our work for many years to come. The next challenge that I have set Andrew is to consider a new paradigm for ethical investing. ESG is in danger of becoming stale; every national and international investment firm is leading with it. The Central Finance Board was at the very forefront of ethical thinking in the 1970s when we disinvested from apartheid South Africa. Epworth kept this going in 1996 with the launch of a range of funds managed using Christian values. I am very excited to see what Andrew comes up with for the next evolution in ethical investment thinking.

### **Award**

I am delighted to announce that Epworth received the award for Best Charity Investment Fund Management Firm in the UK last year from the Wealth & Finance Awards. The judges were keen to observe that this award was made in recognition of Epworth's leading work in the field of ethical investment.

**David Palmer, Chief Executive Officer**

### **\*\*\*RESOLUTIONS**

- 39/1. The Conference adopts the Report of the Central Finance Board**
- 39/2. The Conference elects the following persons to the Central Finance Board for the period of one year from 1 September 2023:**

Dr Keith Aldred, Jennie Austin, Ruby Beech, the Revd Julian Blakemore, Graham Boyd, Julian De Garis Parker, Caroline Edwards, the Revd Anne Ellis, Ashley

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France, Bala Gnanapragasam, Anne Goodman, Alan Groves, Frank Guaschi, the Revd David Haslam, Sue Haworth, Peter Hobbs, the Revd Dr Peter Howson, Nick Moore, the Revd Leslie Newton, Colin Pearson, the Revd Jennifer Potter, Martin Rees, John Sandford, Andrew Slim, the Revd Eleanor Smith, the Revd Timothy Swindell, Matthew Tattersall, the Revd Graham Thompson, Morwenna Williams