

33. Central Finance Board of the Methodist Church

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Summary statement of change in unit holders' net assets

As at 28 February 2022

| | Net assets at 28.02.21 £'000s | Net creations/ cancellations £'000s | Change in net assets £'000s | Net assets at 28.02.22 £'000s |
|---|----------------------------------|---|--------------------------------|----------------------------------|
| CFB UK Equity Fund | 324,226 | (167,337) | 31,284 | 188,173 |
| CFB Global Equity Fund (formerly CFB Overseas Fund) | 148,910 | (29,773) | 19,906 | 139,043 |
| CFB Gilt Fund | 5,267 | (170) | (248) | 4,849 |
| CFB Corporate Bond Fund | 105,928 | (2,522) | (6,274) | 97,150 |
| CFB Short Fixed Interest Fund | 15,002 | 429 | (472) | 14,959 |
| CFB Managed Mixed Fund | 28,688 | (581) | 2,602 | 30,709 |
| CFB Property Fund | 20,673 | 1,217 | 3,874 | 25,764 |
| CFB Deposit Fund | 356,271 | 128,143 | 0 | 484,414 |
| Less: CFB Deposit Fund balances in other CFB funds | (2,144) | 822 | 0 | (1,322) |
| Total funds under management | 1,002,821 | (69,772) | 50,690 | 983,739 |

Chair's Report

A year of change

It has been another extraordinary year and a year of change for the Central Finance Board (CFB). The COVID pandemic appears to be coming to an end and our office in Bonhill Street has returned to a new hybrid work in the office/work from home model. I am very grateful to all of our staff for their professionalism and diligence during the difficult days of the pandemic. One of the features of the pandemic has been "the great resignation" as people reflect upon their priorities and career objectives. The CFB has not been immune from this, and we have seen some turnover in our management team. In my report last year, I welcomed Roz Amos as our Chief Investment Strategist and the Revd Dr Andrew Harper as our Head of Ethics. In this year's report I must also welcome Sarah Bourgein to our management team as Head of Client Relations. Sarah replaces Christophe Borysiewicz who has left us after 17 years of service. He left with our gratitude and appreciation for the service that he has given both the CFB and the Church. It is a strong management team that is outwardly focused, and I hope that the churches, Circuits and charities that we serve will have the opportunity to meet some of them at the Methodist Conference or at our own CFB conference later this year.

Our financial position

The Chief Executive Officer's report highlights the exceptional year that 2021/22 was for equity markets. This market strength helped both our funds under management and our revenue position. The combination of strong markets and cost savings on the timings of senior management recruitment meant that the CFB reported a surplus in 2021/22 of £219,733. Our regulated subsidiary, Epworth Investment Management Limited, also recorded a small profit meaning that the consolidated surplus for the financial year was £221,188.

However, the outlook for 2022/23 is more difficult. The Russian invasion of Ukraine has damaged

both geopolitical and financial confidence and we have seen sharp falls in market values at the start of our new financial year. Our Chief Executive reflects in his report on the disinvestment by the CFB from the oil and gas sector and in the short-term how this has hurt our relative investment performance as our Funds have not benefitted from the sharp rise in the price of oil that followed the invasion.

We are also seeing the climax of the disinvestment strategy from the CFB by the Methodist pension schemes. Defined benefit pension schemes have both assets and liabilities, the latter representing the future pension commitment to our Ministers and lay people. The value today of those future liabilities is greatly impacted by interest rates. With the recent rise in interest rates, today's value of those future liabilities has fallen. With this fall and the recent rise in the Schemes' asset values, the Trustees have taken the opportunity to "de-risk" those assets. In practical terms for the CFB this means that over the last year and in the next few months we will have lost a further £230m of assets under management.

Risk

The CFB prioritises a strong risk management culture. The CFB Council members recognise that risk is inherent in their business and the markets they specialise in. The organisation faces a number of business risks which are actively managed. The principal risk areas are as follows:

- Strategic risk
- Operational risk
- Regulatory risk
- Investment risk

The CFB Council members have reviewed and endorsed a robust and realistic business plan, setting the strategic direction of the CFB. Under this plan there has been substantial investment in the operational, compliance and risk functions of the organisation. The key risks are logged in a central risk register and these are reviewed regularly and adapted as appropriate.

During the COVID-19 pandemic there have been no material issues with fund liquidity or fund investment risk and the CFB Funds continued to operate normally through this period.

Raising Epworth Investment Management's profile

The Council of the CFB has asked our executive to be more vocal in our ethical engagement; to be prepared to speak up for the poor and marginalised. This has two key benefits – it fulfils our moral obligation as stewards of the assets of many faith and charity groups; it also raises the profile of Epworth. David notes in the CEO report some of the ethical activity that Epworth has undertaken in the last year. This has been noticed in the media and in ethical investment circles and we have started receiving unsolicited calls from charities seeking a strong ethical manager for their investment portfolio. For the CFB to continue in its current form we need to replace those pension scheme assets that we have lost. Epworth's increasing profile and the new business activities that David describes below leave me confident in the long-term security of the CFB.

HSBC

One issue that we have been particularly vocal on is the ethical performance of HSBC. We recognise that many treasurers within the Church are deeply unhappy with HSBC – for both their lending to the oil and gas sector and for their business practices. Over the last year we have called out HSBC very publicly for the support of the security laws in Hong Kong and for their hypocrisy in seeking to undermine the climate targets set by bodies in the financial sector. HSBC is deeply embedded in the operations of the CFB. They are not only our banker but also the custodian of our client assets and Trustee, administrator and unit registrar to Epworth's funds. We have heard the great disappointment with the performance of HSBC within the Church and in reaction to this have become one of their most vocal critics. We have a long-term project to review how we support our funds and this will include a review of the role of HSBC. This project is fraught with operational and regulatory risk and thus the review will be measured and deliberate.

Lending to the Church

The opportunity arose earlier this year for the CFB to support the Church financially in their move from Methodist Church House to 25 Tavistock Place. We were able to provide short-term, fully secured, low risk finance that resolved an issue for the Church and enhanced the rate of return to our Depositors.

The Climate Emergency

I am very keen that we work with the Church on its journey to a carbon neutral world. I have been in correspondence with the Connexional Team about practical ways to finance the investment required to reduce the Church's carbon footprint. I am very pleased to note David's report on the relatively low carbon footprint of our existing funds. However, we must do more, and it is part of my commitment as your Chair to continue the drive to consider the climate implications of every investment we make or action that we undertake.

The Future

The CFB is in a strong position to face the future and I am excited by both the developments in our portfolio management service and by the real prospect that we will be able to serve the retail Christian investor in the near future, as described in the Chief Executive Officer's report.

John Sandford, Chair

Chief Executive Officer's Report

Firstly, may I join John in welcoming the new members of our management team. Arguably one of our weaknesses in the past has been a lack of "outward facing" activity. We now have a management team that is vocal and engaging and I am confident that it will deliver the growth that John has described we need.

Investment review of the year

The last 12 months have been a rollercoaster in many ways. We started the year with many countries still in lockdown due to Covid 19. Things improved, broadly speaking, in this dimension over the year due to large scale vaccine rollouts and developments of better treatments for the disease, and although recent outbreaks tell us it is not over, the acute phase for most of the world has passed. As the year progressed attention turned to inflation and energy prices, as the pace of reopening strained supply chains and people in many countries experienced inflation in prices while growth bounced back. Most recently the world has been shaken by Russia's invasion of Ukraine, which to date shows no sign of a resolution that ends the human suffering. The economic fallout from this to date has been to put further pressure on energy supply as the rest of the world moves to exclude Russia from global markets, and forecasts for growth in the next year have fallen.

Equity markets have, against this backdrop been volatile but surprisingly resilient overall. UK equities have returned around 16% in the year to 28 Feb 2022. Our portfolio has struggled in this environment, particularly in the last couple of months, and has returned 13% in the same period. Lack of holdings in the oil and gas sector, and a rotation away from growth stocks have both hurt our relative performance. Global equities also performed well, with the CFB Global Equity Fund returning 11.3% over the period, with similar factors impacting relative performance. 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, but that the bond funds have achieved negative returns for the year to 28 February. Property returns have been positive and ahead of benchmark over the period with our exposure to Mayfair Capital's Property Income Trust for Charities rewarding us with sector leading performance.

Ethical review

Tax Justice remains an issue of importance to the Central Finance Board and Epworth Investment Management Limited. We continue our engagement with the leadership of the companies that comprise the "conviction" part of our portfolio, encouraging them to seek the accreditation of the

Fair Tax Mark. We have heard back from nearly all the companies, with encouraging responses on the need for transparent reporting. Following our engagement, we have seen several companies publish their tax strategies online, and others have committed to looking further at the Fair Tax Mark. We applaud all instances where companies take steps to be more transparent in their tax accounting and reporting. Epworth renewed its accreditation with the Fair Tax Foundation in the year. We are proud to be certified by a scheme that recognises companies which pay the right amount of tax at the right time and in the right place.

Another focus for the year has been on mining companies, where we have long term engagement projects aimed at holding these companies to account for their approaches to the environment, the welfare and safety of their employees, and the impact that their activities have on local communities in the remote areas that they operate in. We encourage companies to develop policies, to enforce these policies, and to report on them. Our ongoing engagement with these companies ensures that we can continue to influence them and to push them to continue improving on these important ethical issues. Notably, the Central Finance Board featured in a February 2021 edition of the Sunday Times as one of the only investors willing to make serious comment after the mining company Rio Tinto published a report detailing systemic workplace toxicity including incidents of criminal harassment, rape, and racism with their company. This press exposure leveraged high-level meetings for our ethics team with Rio's management and has given the Board the opportunity to interrogate policy at the company.

In accordance with the request from the Methodist Conference, the Joint Advisory Committee on the Ethics of Investment and the Central Finance Board have adopted an updated policy on Israel Palestine. This policy will better enable the Board to navigate the complexities of the region with care and compassion. It also sets a precedent on how we form policy in conflict zones; regrettably a live issue with the war in the Ukraine.

Through the Church Investors Group voting policy, in 2021 we introduced new voting on ethnic representation at board level. This year we will continue to advance our expectations of companies in this area, increasing the number of companies that this applies to. Over the year, we saw an increase in companies in both the UK and global markets putting climate related resolutions to a vote as attention to how companies are transitioning to a low carbon economy increases.

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 Funds for Charities. The CFB Overseas fund has been renamed the CFB Global Equity fund.

Until the end of 2021 all equity funds were showing strong medium term relative and absolute performances. Some of this was lost during the first two months of 2022, largely due to the exclusion of companies in the oil and gas sector:

See Table 1.

Change in the manner in which fund fees are taken

One amendment made during the year was to change the way in which the CFB collects its fees from the funds that it manages. Previously fees were charged to the "income account" of the relevant fund. Thus, fees were deducted from the dividends that were received by the Funds before a distribution was made to unit holders. From November 30, 2021, fees have been charged to the "capital account". This means that all dividends received by the Funds are distributed, improving the income received in unit holder hands. However, with fees now being charged to capital, the cost of this is reduced long term capital growth. For unitholders that reinvest their dividends, there is no overall impact upon their total return.

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. For the CFB's voting record in 2021/22 see Table 2.

Carbon footprint

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

Table 1 - CFB fund performance summary

As at 28 February 2022

| | 1 year % | 3 years % p.a. | 5 years % p.a. | 10 years % p.a. |
|--------------------------------------|-------------|-------------------|-------------------|--------------------|
| CFB UK Equity Fund | 12.95 | 5.99 | 5.46 | 7.39 |
| Benchmark | 16.03 | 5.78 | 4.68 | 6.91 |
| Excess return | -3.08 | +0.21 | +0.78 | +0.48 |
| CFB Global Equity Fund | 11.30 | 13.57 | 10.29 | 12.58 |
| Benchmark | 12.87 | 14.12 | 10.60 | 12.77 |
| Excess return | -1.57 | -0.55 | -0.31 | -0.19 |
| CFB Gilt Fund | -4.23 | 0.58 | 0.61 | 2.56 |
| Benchmark | -3.19 | 1.25 | 1.01 | 2.94 |
| Excess return | -0.96 | -0.67 | -0.40 | -0.38 |
| CFB Short Fixed Interest Fund | -2.44 | 0.32 | 0.28 | 1.43 |
| Benchmark | -2.17 | 0.30 | 0.28 | 1.40 |
| Excess return | -0.24 | +0.02 | - | +0.03 |
| CFB Corporate Bond Fund | -4.71 | 0.97 | 1.01 | 3.59 |
| Benchmark | -4.74 | 2.18 | 1.74 | 4.09 |
| Excess return | +0.03 | -1.21 | -0.73 | -0.50 |

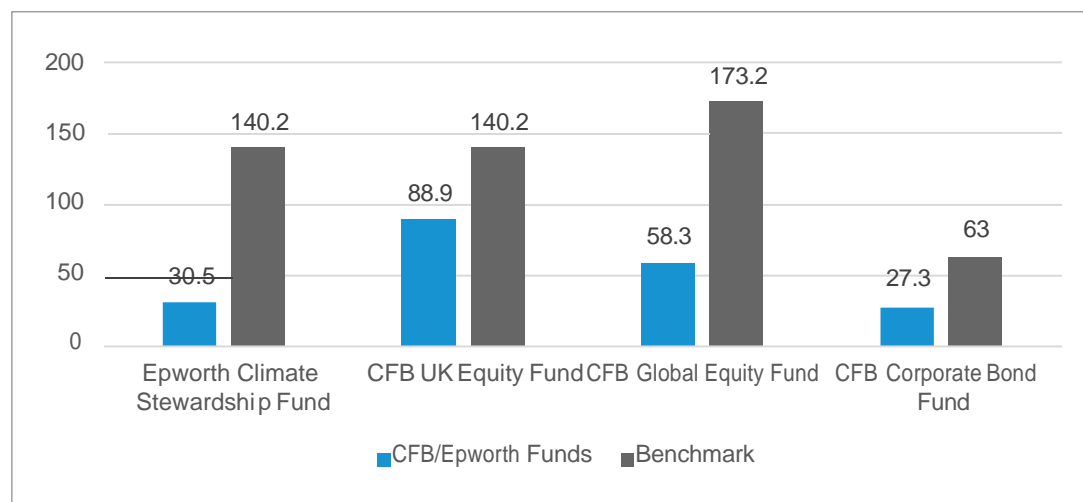
All figures annualised and after fees

Table 2 - CFB voting record

Year to 28 February 2022

| | For | Oppose | Abstain | Against or abstain |
|--------------------------------|-------|--------|---------|--------------------|
| Auditors | 326 | 2 | 0 | 1% |
| Directors | 2,773 | 444 | 24 | 14% |
| Remuneration | 156 | 263 | 5 | 63% |
| Executive Pay Scheme (UK) | 40 | 30 | 0 | 43% |
| Shareholder Capital (Overseas) | 143 | 11 | 0 | 7% |
| Other | 1,674 | 101 | 18 | 7% |
| Total | 5,112 | 851 | 47 | 15% |

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



CFB Deposit Fund

2021 was a nadir for interest rates in the United Kingdom with the CFB Deposit Fund only able to pay an interest rate of 0.01%. Even this paltry rate had to be funded from reserves as the costs of running the fund were greater than the interest we could earn from external bank deposits. However, the rising inflationary environment in the United Kingdom led to two rises in the Bank of England's base rate at the end of the year enabling us to increase the rate on the CFB Deposit Fund to 0.27% by early March. As our rolling book of deposits mature, and we are able to fund at higher rates, I anticipate that the rates declared on the CFB Deposit fund will gradually increase throughout the year; bringing some much needed support to our treasurers.

Attitude of Churches to disinvestment from oil & gas

For three years the Central Finance Board engaged with the Methodist Conference to meet its request that the Church should not be invested in any companies in the oil and gas sector that were not aligned with the Paris Accord. After three years of in-depth research, we were unable to satisfy the Joint Advisory Committee on the Ethics of Investment that any company was fully aligned with a "well below two degrees" scenario. The Board and Epworth therefore sold the last of its investments in the sector in April 2021. To my surprise this decision has been criticised by some members of the Church and we have faced challenges to our management of individual church funds due to this decision. The Central Finance Board will always comply with the directions of the Methodist Conference.

Climate Stewardship Fund

Two years ago, Epworth launched its "Climate Stewardship Fund". This fund invests in UK equities but excludes any that are involved with the oil and gas sector or have high carbon footprints (such as cement manufacturers or airline companies). It also invests in companies that are supporting the transition to a lower carbon world. We are working with the Connexional Team to replicate this fund for the Methodist Council. We also hope to launch later this year a similar fund that invests in Global equities, again supported by the Methodist Council.

CFB Conference

For the last four years we have held an annual CFB conference that updates our clients and members of the Church on our investment and ethical work. The last two conferences have been through a virtual platform, but I hope that this year we will be able to visit several locations around the country. We will be reaching out to possible locations and if you would like to host a visit from the CFB's team later this year please let me know.

Platform

In addition to its Fund offering, Epworth's investment proposition includes a portfolio management service. Because of our operational structure these portfolios can currently only consist of Epworth's own funds and an external commercial property fund. Epworth is well advanced in an operational enhancement to this portfolio offering that involves using a third-party technology provider and custodian. Once this project is completed Epworth's clients will be able to elect to hold their portfolio on a third-party platform, enabling Epworth to invest in external funds where there are gaps in our current choice of asset class. Clients on this platform will also be able to access their valuations electronically daily. We will not be able to extend this service to any portfolio clients investing in the CFB funds until we are able to improve the dealing cycle on these funds to daily.

Retail clients

Last summer Epworth applied to its regulator, the FCA, to expand its regulatory permissions to act for the general public (retail permissions). Epworth is still waiting to hear if it is being granted these extra permissions but in the meantime is working on a solution that will deliver an ethical solution based upon our Christian beliefs to the person in the pew. In the United States "biblically responsible investing" (BRI) is a well-established market; in the UK there are funds readily available for the Muslim investor. But there are no retail Christian solutions available. Epworth therefore sees this as a new business opportunity; as well as fulfilling part of our calling. The operational requirements of such a venture are substantial and Epworth has therefore partnered with a leading City investment

firm. Epworth is joining the Association of Christian Financial Advisers and will be the lead sponsor of their Autumn annual conference.

The Revd Dr Jen Smith

I would like to finish this report with my thanks to the Revd Dr Jen Smith, the Superintendent at Wesley's Chapel. Jen has supported our weekly prayer group without complaint, dialling in even when travelling to the North of Scotland where her husband currently serves. The prayer group is a time of reflection that lies at the heart of our culture. Jen's leadership has guided us through very troubling times as we have to balance our financial commitment to our clients with our ethical obligations in a dangerous and challenging world. This is at the heart of why the CFB and Epworth are different to any other investment manager and our prayer group will always be a core part of our DNA.

David Palmer, Chief Executive Officer

*****RESOLUTIONS**

33/1. The Conference adopted the Report of the Central Finance Board

33/2. The Conference elected the following persons to the Central Finance Board for the period of one year from 1 September 2022:

Dr Keith Aldred, Jennie Austin, Ruby Beech, the Revd Julian Blakemore, Graham Boyd, Caroline Edwards, the Revd Anne Ellis, Ashley France, Bala Gnanapragasam, Anne Goodman, Alan Groves, Frank Guaschi, the Revd David Haslam, Sue Haworth, Peter Hobbs, the Revd Dr Peter Howson, Theophilus Mensah, Nick Moore, the Revd Leslie Newton, John O'Brien, Julian de Garis Parker, Colin Pearson, the Revd Jennifer Potter, Martin Rees, John Sandford, Andrew Slim, the Revd Eleanor Smith, Anthea Sully, Matthew Tattersall, the Revd Graham Thompson, Morwenna Williams.