first news
Issue 92
December 2022

first mortgage trust

Annualised pre-tax return for the quarter ending 31 December 2022.

6.07% p.a. Group Investment Fund and PIE Fund

Past returns are not a reliable indicator of future performance.

From the CEO

Hello and welcome to our last newsletter of the year.

2022 has been a busy year and if you are like me and the rest of the FMT team, you will be looking forward to spending some time relaxing with family and friends over the festive season.

We are pleased to announce the annualised pre-tax return for the December quarter is 6.07%. In keeping with our philosophy of careful and managed growth the return rates have increased consecutively each quarter this year. This growth shows the resilience of the Fund especially considering the uncertainty and volatility that other asset classes have experienced over the past 24 months due to local and global market factors.

Our lending team are doing a great job in identifying high quality lending opportunities and achieving growth in our lending rates at the same time, which filters through to our investor returns. We have a strong pipeline of loans with no current loans where we are anticipating a capital loss. This, combined with increasing lending rates, means we are expecting further growth in investor returns in 2023.

As an active manager our philosophy is to optimise return rather than maximise return, and we believe this is what drives our success.

Here are some of our highlights and successes from 2022:

- The Fund stands at over $1.56 billion in FUM.
- We welcomed over 1,000 new investors this year with investor numbers now over 6,000.
- Our loan portfolio grew to $1.39 billion, secured by over 1,350 first mortgages on properties located primarily in NZ's five main centres.
- Key lending metrics have tracked in line with our 5-year averages despite the tougher economic conditions.
- Lending ratios remain significantly lower than the ratios permitted in our governing documents.
- We opened a new office in Christchurch.
- We were announced as one of the Top Mortgage Employers for 2022.
- Over $130,000 was invested into our communities through our sponsorships.
- Investor Meetings were reinstated after a two-year hiatus.

Our conservative lending approach is reflected in our loan book statistics. Our average loan to value ratio across our loan book is less than 50% and over 99% of lending is less than a 70% loan to value ratio. This means our borrowers must have significant equity in the lending transaction before we lend to them, which provides a substantial buffer to adverse property market movements.

Looking ahead to 2023

Over the course of 2022 the Fund has performed extremely well in a challenging economic environment. We see further headwinds going into 2023 with the continued increase in the cost of living, rising interest rates, the impact of inflation and geo-political tensions.

Despite these headwinds, we look forward to 2023 with confidence as the Fund remains in a strong financial position.

Over the coming months we will be planning Investor Meetings for 2023 and we are looking to add additional locations. Updates on venues and dates will be available in future newsletters and on our website.

Developments will see our investment offering enriched, including the delivery of an online investor portal together with further enhancements to our cyber security platform through the introduction of new technology. Our primary focus for 2023 will continue to be the active management of the Fund.

Thank you to those who completed our online Client Feedback Survey, we genuinely appreciate the feedback you provide. The Senior Leadership Team including myself thoroughly review the survey findings to ensure we are providing the best possible customer service to our investors.

In closing, on behalf of all the team at First Mortgage Trust, thank you for your continued support. We wish you and your families a safe and enjoyable Christmas and New Year.

Paul Bendall, CEO

Seasons Greetings from our Chair, Michael Smith

It is that time of year when many of us wind down for some much needed rest and relaxation and a chance to spend time with family and friends over the festive season.

On behalf of the Board of Directors I would like to take this opportunity to wish both you and your families a Merry Christmas.

The Board is pleased with how First Mortgage Trust has navigated the economic climate this year, continuing to deliver steady returns to our investors.

We know you have a choice on where to invest your money and we genuinely appreciate your support and the trust you place in us.

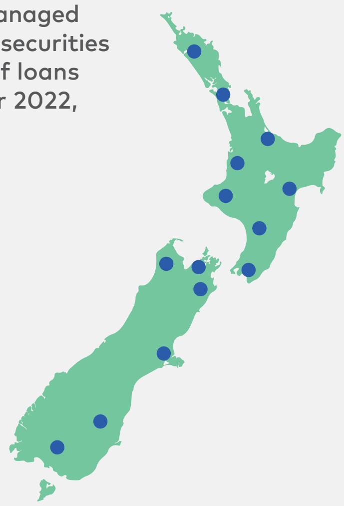
Wishing you a Merry Christmas and a safe, relaxing holiday season.

Michael Smith, Chair

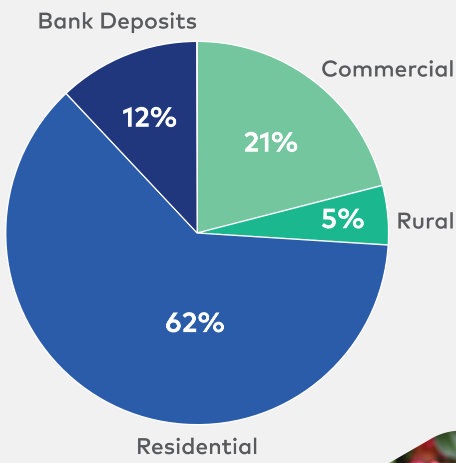
As the Manager of the Fund we have aimed to continue our relatively conservative position. The Fund has been managed to maintain a spread and mix of quality properties as securities for our loans. The map and graph, providing details of loans by region and investments by type as at 2 December 2022, demonstrates the diversity of First Mortgage Trust.

Loans by Region

- Northland 0.5%
- Auckland 61.0%
- Bay of Plenty 6.5%
- Waikato 5.2%
- Taranaki 0.1%
- Hawkes Bay 0.5%
- Manawatu-Wanganui 0.5%
- Wellington 9.2%
- Nelson 0.2%
- Tasman 0.0%
- Marlborough 0.2%
- Canterbury 11.5%
- Otago 4.3%
- Southland 0.3%



Investments by Type



Gardening this Summer

Water and mulching for a successful summer garden: Even though the sun is shining, January is not an easy month for the home garden. Lack of attention due to holidays, high temperatures, low rainfall and often strong winds all make it a tough time for plants. Sustaining soil moisture becomes a gardener's greatest challenge this month. Mulching is the magic word and will help reduce water loss alongside regular, consistent watering.

In the veggie garden: Vegetables going to seed or 'bolting' can happen easily in summer when plants have been stunted or stressed during the growing period. This is usually caused by a lack of or inconsistent watering. Maintain strong healthy growth with regular, deep watering and applications of fresh compost around maturing vegetables. Always increase watering during any periods of drought and mulch with bark or pea straw to significantly reduce water loss from your garden.

Roses: As temperatures and humidity increase, the successful cultivation of healthy roses becomes increasingly difficult. The early season flush of flowers has finished, and now the battle with rust and black spot commences! Some regions have even reported seeing these diseases starting to take hold in December! Spray plants every two weeks throughout summer to treat any disease or pests. Water regularly and apply Daltons Premium Mulch & Grow to keep moisture and nutrients in. Pay special attention to potted roses to ensure they don't dry out. Dead head plants once a week to encourage repeat flowering.

Daltons™ Keeping New Zealand Growing

With thanks to Daltons
www.daltons.co.nz

The Changing Landscape of Inheritance Law

New Zealand's current inheritance law (formally known as succession law) is observed by many as being piecemeal and disjointed. There are a number of different pieces of legislation covering succession law and these date back to 1949, a time when family dynamics and relationships generally reflected the nuclear family model. With New Zealand's developing social landscape, which includes new types of family relationships and changing views on what constitutes a family/whanau, the proposal for change is welcomed.

From 2019 to 2021 the Law Commission reviewed New Zealand's inheritance laws and has recommended that the law be streamlined into a new Act – the Inheritance (Claims against Estates) Act (proposed Act).

How may these recommendations affect us?

Partners

For partners (including spouses, civil union and de facto) the proposed Act would remove the current option A/B process which requires partners to choose either a 50/50 division of relationship property or what is left to them under their partner's Will. The proposed Act would give the partner what they were left under the Will, plus a claimable top up. The Court would also have the flexibility to replace property the surviving partner is to receive under the Will with relationship property.

Partners will be less able to make family protection claims (claims against an estate that they have not received an adequate share). They will need to prove they have 'insufficient resources to maintain a reasonable, independent standard of living'.

However, where a partner dies intestate (without a Will), the surviving partner will receive a greater share of their estate than they do under the existing law.

Children and Grandchildren

Whāngai children and grandchildren (persons adopted according to tikanga Māori) will be eligible to make a Family Protection Act (FPA) claim. However, stepchildren remain ineligible.

The Commission has offered two options for the ability of children and grandchildren to make an FPA claim:

- The first option is to enable all children and grandchildren to claim where the deceased has 'unjustly failed' to provide for a child or grandchild who is in financial need, or to recognise them. This is like the existing law. However, when assessing whether there is a valid claim, in addition to current considerations, the Court would have regard to tikanga.
- The second option is to limit those eligible to claim to persons under 25 (ages 18 or 20 are also being considered for the threshold). Currently, a child of any age can make a claim. Disabled children and grandchildren who were wholly or partially reliant on the deceased immediately prior to their passing or whose disability occurred when they were adults, would not be subject to the age limit. This option would see a more narrowed set of circumstances to be considered by the Courts.

Attacks on Trusts

The proposed Act will likely see an increase in attacks on Family Trusts. It is recommended that the Court have the power to recover property that has been transferred to a Trust to defeat an entitlement or claim. This will make Trusts more vulnerable to claims, but their success will largely depend on sufficient proof of the intention to defeat a claim.

Other noteworthy recommendations

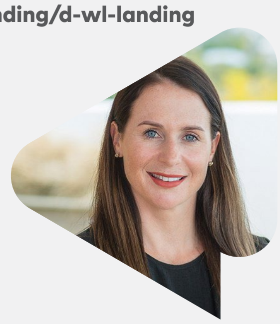
- Greater recognition of tikanga Māori and in particular determining succession matters for Māori;
- Replacing and clarifying the law on testamentary promises (promise that someone will leave a gift in their Will) and contributory claims;
- Enabling persons to contract out of their entitlements to provide for their children/stepchildren (similar to the 'prenup' model for relationships);
- Increasing the prescribed amount for a probate application, which is currently $15,000;
- Including audio visual recordings as 'documents' which record the intent of the deceased (where the deceased fails to leave a Will); and
- Preventing Wills from being automatically revoked on marriage or civil union.

We wait in anticipation to see a draft of the proposed Act, noting that if it is anything like the Trusts Act 2019, it may be several years away.

For the basics of what you need to think about when preparing or updating your Will try out the Holland Beckett Will questionnaire on their website – **https://hobec.wills.settify.co.nz/willslanding/d-wl-landing**

HOLLAND BECKETT
LAW

Article provided by Rebecca Steens, Holland Beckett Law



Our very own Dame Jane!

Jane Swainson from our investment team was recently promoted within The Most Venerable Order of the Hospital of St John of Jerusalem to the rank of Dame of Grace.

She was invested by John Whitehead (CNZM, KStJ), Chancellor of the Priory in New Zealand. Jane is the first woman in St John to be dubbed by sword in New Zealand, and she was one of 22 postulants who were honoured at this service, whose awards were some of the last to be signed off by the late Queen Elizabeth II.

Congratulations Jane, we are all very proud of you and this is a great acknowledgement of the amazing work you do with St John.

Investor Meetings 2022

We recently concluded our Investor Meetings for 2022. For those who were unable to attend we have included the key points discussed.

Michael Smith, Chair and Paul Bendall, CEO

As a business what do we focus on?

We focus on risk and return or put another way – resilience and performance. When making decisions the first question we always ask ourselves is – "Is this in the best interest of our investors?" If the answer isn't an emphatic yes, we move on. It has been this way for over 26 years and it won't be changing.

Where is FMT positioned today?

The Fund is in a strong financial position and has performed well over the last 12 months, even in the current economic climate.

FMT Fund stats

- **$1.55 billion** FUM
- **Est. in 1996** & **NZ owned**
- **6,000+** investors
- The Manager is **100% NZ owned**
- **Team of 50+**, based in Auckland, Tauranga, Wellington & Christchurch
- **NZ's largest non-bank property lender** secured by first mortgages
- A trust structure with **strong governance** across Board, teams & processes

FMT Loan Book of $1.38 billion

50% average LVR	**$1 billion** of new loans in 2022	**16 months** average loan term
1350 first mortgages	**$1.8m** average loan	**Less than 1%** loans arrears

One of our strengths is our extensive loan origination capability driven by highly experienced property finance experts.

Why is being an active fund manager important?

We are an active manager which means that we decide which loans to invest in; ensuring the loans comply with the Funds' investment guidelines and policies. We manage these loans on behalf of you – our investors.

A key part of being an active manager is making lending decisions based on our skills and knowledge as a specialist property lender and this includes:

- Continuously assessing and monitoring the market;
- Using the skills and experience of the team to identify and structure the best possible lending opportunities; and
- Managing these loans through to successful completion.

There's a saying "that lending money is the easy part, it's getting the money back that takes skill" – we focus heavily on getting the money back!

We have continued to provide consistent returns, even during challenging economic times

We've managed to increase our quarterly rate each quarter this year – which is impressive when you look at other markets.

What makes the Fund so resilient is our strong loan book. We are conservative in our lending and this is reflected by our lending statistics.

Who do we lend to?

We often get asked "do you lend to people that the banks say no to", in part yes, we do, but we believe the banks should be lending to these people. Many of these prospective borrowers are business owners with strong asset positions who want to invest in their business. Many are aged over 50 who on the bank models can't demonstrate how they can repay the loan from their primary income source by the time they reach the age of 65, despite having strong assets and diverse income sources; and some people are just fed up with dealing with the banks and are prepared to pay a bit extra for the service we provide.

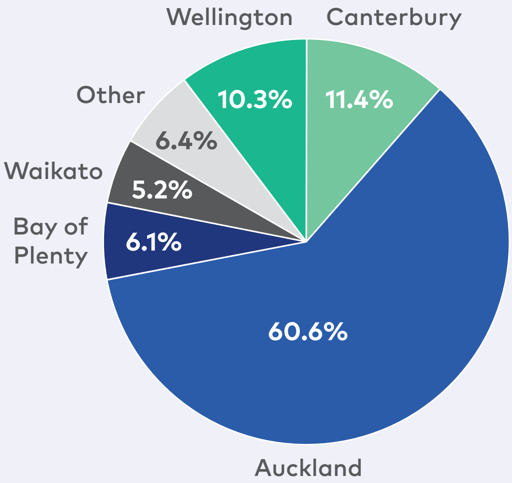
Where do we see future opportunities?

The NZ non-bank sector is growing year-on-year and we are seeing a structural shift in the funding landscape with more people moving towards non-banks, and this reflects what is happening overseas. This move will create more lending opportunities for us in the future. Since 2019 bank mortgage lending has grown 25% and the non-bank sector which we operate in has grown 152%. (Source: Reserve Bank, October 2022).

Where are our loans and what type of loans are they?

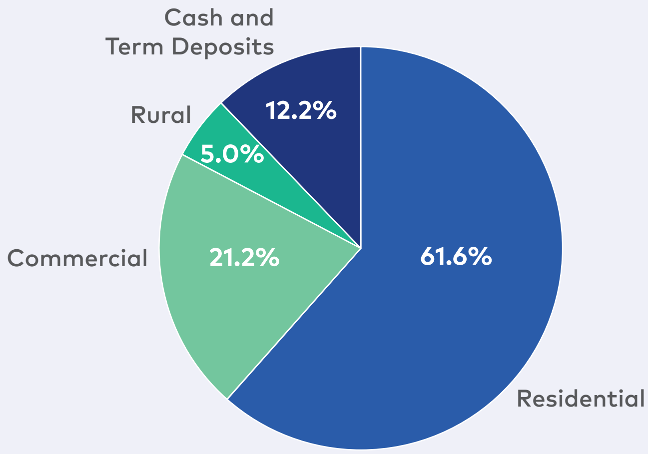
We have a diverse loan book, with different asset types and geographical locations across NZ.

The below diagram shows where our loans are located.



Over 90% of our loan book is located in New Zealand's five main regions. The reason we focus almost entirely on these key markets is, historically, they have performed well from a property value perspective and because they are regions with growth, employment opportunities and strong GDP.

Geographical diversification is not our only consideration for lending. We also evaluate different asset types to lend against. The chart shows the asset types of our loans, as you can see the majority of these are in the residential and commercial markets.



We assess the portfolio to an even more granular level and monitor how much of our lending is investment, development or land only. At any given time, our development exposures generally range between 20%-25% of our lending, with our current level close to 20%. Land is similar and generally ranges between 15%-20% and we are currently closer to 15%.

All figures in this article are at 30 September 2022.

Our Future Focus

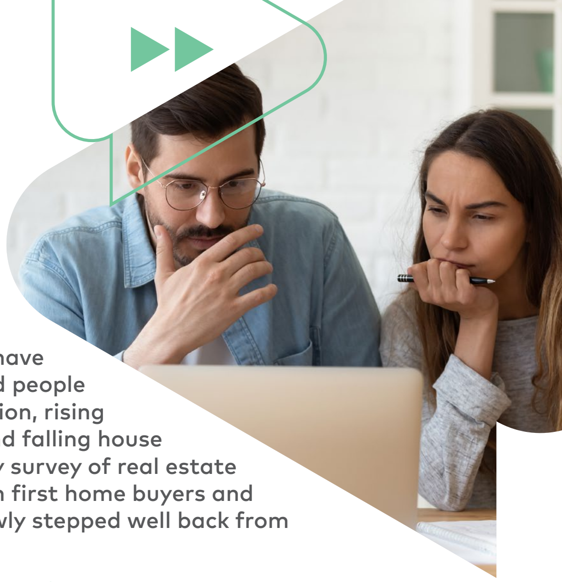
We look ahead with confidence. We have over 26 years of continuous success behind us. There is invaluable knowledge built up within the business. The Fund continues to grow and we continue to invest in the business.

Our commitment to you, we will:

- Continue to strive to provide our investors with consistent returns.
- Maintain steady, sustainable growth.
- Always focus on having leading-edge cyber security technology – our cyber security partner uses best in class technology to ensure systems and data are continuously monitored and protected.
- Provide our investors with a client portal so they can access their account 24-7 from any device.
- Ensure we always comply with all relevant regulatory requirements.
- Always act in the best interest of our investors.
- Strive to keep our record of never missing a payment to our investors and never losing a cent of investor capital in our history.
- And of course, ensure we continue to provide you with great customer service.

Thanks to those that attended the Investor Meetings and also to our guest speakers – Dane and Quinn. To view a video of our Investor Meeting held in Tauranga, visit our website – **fmt.co.nz/events**

Monetary Policy Over-tightening Risk



In the middle of October, we learnt that New Zealand's inflation rate was 7.2% in the year to September rather than the 6.6% rate commonly expected. That piece of unwelcome news led to a lift in expectations for the extent to which monetary policy would have to be tightened and banks responded to borrowing cost increases with a round of 0.5% fixed mortgage rate rises.

Things then generally settled down and we could see some stepping back of buyers in the residential real estate industry. But despite increasing their interest rates, bank margins for fixed rate loans remained well below average. Then the Reserve Bank tightened monetary policy on November 23.

The Reserve Bank lifted their predicted peak for the official cash rate from 4.1% to 5.5% and warned that the economy would need to go into recession with unemployment rising from 3.3% to 5.7% in order to get inflation back towards 2%.

Their scary comments and media focus on future mortgage rate rises have been enough to encourage banks to raise their interest rates by another 0.5% or so. Now, here is where things get interesting. Margins for fixed rate lending are now roughly back at their two year averages. How can this be if monetary policy has tightened and presumably bank funding costs for fixed rate loans have jumped higher?

Actually, they haven't. Banks have simply taken the opportunity provided by the official tightening of monetary policy via a record 0.75% rise in the official cash rate to 4.15% to finally get margins back to average levels.

Consider the one year swap rate which is the cost to banks of borrowing at a fixed rate for one year in the wholesale markets to on-lend to you and I at a fixed mortgage rate for one year. Shortly before the mid-October inflation shock this rate was near 4.8%. After the inflation outcome it jumped to almost 5.3% and banks raised their lending rates about 0.5%.

Following the 0.75% official cash rate rise on November 23 the one year swap rate settled at 5.2%. It is now actually lower than it was just after the inflation outcome. The markets had already priced in an expectation of the cash rate going to 5.5%, so confirmation of this by the Reserve Bank has not altered the wholesale borrowing costs of the banks.

Consider also the three year swap rate. It was 4.8% before the inflation number, rose to 5.15% shortly after, and now sits near 4.8%. It has fallen most recently. This reflects an expectation that monetary policy will successfully get inflation down and there will likely be rate cuts through 2024 if not before the end of 2023.

Helping to propel expectations that monetary policy will work was the ANZ Business Outlook survey for November released after the monetary policy decision. It showed a new decline in business sentiment and plans for cutting staff numbers and capital spending levels. The survey was taken almost entirely before November 23 and raises the possibility that by leaving its harshest warning words until now and its biggest one-off increase to late in the cycle, the Reserve Bank may in fact now be over-tightening monetary policy.

This would be consistent with their habit of moving too late with easing and tightening then going too far and causing things to whiplash back the other way.

What are the housing market implications?

In the short-term – as in over summer – negative.

The Reserve Bank have successfully scared people with talk of recession, rising unemployment, and falling house prices. My monthly survey of real estate agents shows both first home buyers and investors have newly stepped well back from the market.

But will prices fall as far as some are newly predicting?

Probably not. Within a few weeks the discussions about interest rates are likely to start shifting from rates rising further to them not going as high as earlier expected and in fact falls becoming probable in a few months for the 3 - 5 year fixed rates. This is because we are only four months away from the predicted peak in the cash rate, forecasts of inflation and peak interest rates offshore are both falling as inflationary pressures are seen to be easing, and NZ data suggest our central bank has over-egged its pessimism.

Once buyers can see their worst case scenario for borrowing costs, some will start returning to the market assisted by rising incomes and high job security. Another supporting factor as we head into autumn looks like being better than expected migration flows.

Just as tourist numbers have so far surprised on the strong side, so too have inflows of migrants been higher than expected recently. One analyst is even predicting a net gain over 2023 of just under 40,000 people from a net loss of 8,500 in the year to October.

Worth keeping an eye on also are the political opinion polls. It is looking increasingly like there will be a change in government at next year's general election and that means restoration of interest expense deductibility for investors.

At the same time however we need to be aware that chickens are coming home to roost in the home construction sector. As noted here and in my other writings for the past two years, too many over-optimistic, under-capitalised, inexperienced people have become property developers. They have paid too much for the land and their projects are no longer financially viable.

Already the newspapers contain stories of builders failing and home buyers losing hundreds of thousands of dollars. We are unfortunately going to see more such stories for the next 1 - 2 years as the level of house building falls back towards more sustainable levels. The good side of that however is that buyers will increasingly look to purchase an existing dwelling rather than a newly constructed one from other than the well-established larger building groups.

Article by Tony Alexander,
Independent Economist

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FMT Investor Prize Draw

Each quarter First Mortgage Trust investors have a chance at winning a $250 voucher, choosing from petrol or supermarket gift cards.

This quarter's prize winners are located in:

- 1 individual Northcote, Auckland
- 1 individual Mount Maunganui
- 1 individual Papamoa
- 2 individuals Tauranga
- 1 trust Tauranga

Congratulations to our winners!

The prize draw is held under supervision and winnings are paid for by the Manager of the Fund, meaning it has no effect on the return to investors.

Terms and conditions apply.

Making a Withdrawal

To make a withdrawal from your First Mortgage Trust investment you must complete a Notice of Withdrawal.

A Notice of Withdrawal form is available on our website for you to complete and return to us (it is also sent on the rear of our postal correspondence and as an attachment to our email correspondence).

Withdrawals are normally actioned twice a week (on Monday and Thursday). We generally action withdrawals within four business days of receiving your completed Notice of Withdrawal.

Last date for processing withdrawals for March quarter: Monday 27 March 2023.

We will need to receive completed and signed Notices of Withdrawal on or before Friday 24 March 2023.

Next processing date for withdrawals: Monday 3 April 2023.

We will need to receive completed and signed Notices of Withdrawal on or before Friday 31 March 2023.

Christmas Hours

The offices of First Mortgage Trust will close on Thursday 22 December 2022 and will reopen on Monday 9 January 2023 at 9.00am.

Spiced Christmas Cake with Candied Orange, Cranberries and Rum-Soaked Sultanas

FOR THE CAKE

- 100g sultanas
- 80ml rum
- 150g butter, softened
- 125g coconut sugar or soft brown sugar
- 1 tsp vanilla extract
- 3 organic eggs
- 150g plain flour
- 50g ground almonds
- 1 tsp cinnamon
- 1 tsp nutmeg
- 1 tsp cloves
- 1 tsp allspice
- 1 tsp ginger
- 2 tsp baking powder
- ½ cup whole milk
- 3 tbsp candied orange peel
- 80g dried cranberries

FOR THE ICING

- 150g butter, softened
- 2 cups icing sugar
- 125g cream cheese
- 1 tsp vanilla extract with seeds
- 2 tbsp rum

TO DECORATE

- handful dried cranberries
- 20g finely chopped pistachios
- 1 candied orange slice (optional)

METHOD

1. In a small bowl, combine sultanas and rum and microwave for one minute until sultanas are plump and juicy. Set aside to cool.
2. Preheat oven to 175°C fan bake. Line 2 x 22cm tins with baking paper.
3. In the bowl of an electric mixer, cream butter and sugar until pale, light and fluffy. Add vanilla and then eggs, one at a time. In two batches add flour, ground almonds, spices and baking powder, alternating with milk. Stop mixing once combined.
4. Fold through dried fruit including rum-soaked sultanas (and any excess rum in the bowl).
5. Pour batter into two lined tins and spread out to the sides. Bake for about 30 minutes or until golden in colour. Allow cakes to cool for 10 minutes before turning onto a cooling rack.
6. Meanwhile, make icing. In the bowl of an electric mixer, beat butter and icing sugar until smooth, and then gradually add cream cheese and vanilla. The icing should be smooth, creamy and thick. Stir through rum at the end.
7. Once cake is cool, apply a generous amount of icing to one layer. Place other cake layer on top and ice it generously. Decorate with dried cranberries, pistachios and candied orange slice.

Source: the-caker.com

FMT in the Community

At FMT we believe it is important to support our local communities.

Our purpose is to create a better New Zealand, which we keep front of mind when we partner with charities, communities and clubs. In 2022 we have invested over $130,000 into New Zealand by supporting many worthwhile organisations and events.

Below are some of the charities, organisations and clubs we've supported during 2022.

It gives us great pride to partner with these worthy causes.

Save the Kiwi

Can you imagine a world without the kiwi? We can't! That's why we are one of the main sponsors of this charity which does an amazing job of protecting and rebuilding the kiwi population. To read more on how they do this, visit **savethekiwi.nz**

Bowling clubs

We're a proud sponsor of several bowling clubs, having partnered with some for a number of years, with many of the members being FMT clients. Bowling clubs form a key part of our communities, both for fitness and social connection.

FMT Youth Sponsorship Grant

The Youth Sponsorship Grant was established 17 years ago and is open to young people aged between 16 and 25. The successful sponsorship recipient receives a grant of $3,500 to put towards helping them succeed in their chosen field. Over the years recipients have been involved in music and drama, sailing, clay shooting, swimming, lacrosse and athletics. This year's recipient was open water swimmer Quinn Boyle. We were really impressed with Quinn, not only his swimming achievements, but also with his attitude and values.

We will be looking for our next recipient in early 2023, see our website – in our communities page for more information, **fmt.co.nz/in-our-communities**

Hanmer Clinic

Hanmer Clinic is an Outpatient Addiction Treatment Centre, which has provided alcohol and drug addiction treatment services in Tauranga since 1999. We are their first corporate sponsor. Our sponsorship makes a difference, helping people on their road to recovery. To learn more visit **hanmerclinic.co.nz**

Coastguard

The Coastguard is a charity which does an impressive job keeping people safe on the water. We have partnered with the Tauranga Volunteer Coastguard for five years, the last four as their premier sponsor. Coastguard are always on the lookout for volunteers – see their website **coastguard.co.nz** for contact details.

GoGenerosity

GoGenerosity began during Covid when many businesses and kiwis were struggling. The concept is all about paying-it-forward to help those in need. As a corporate sponsor we pay-it-forward by way of a monthly donation which is distributed to local businesses who then produce goods and services for local charities to help those in the community that are in need. To learn more visit **gogenerosity.com**

To learn more about our sponsorships, visit **fmt.co.nz/in-our-communities**

*NB Where sponsorship funds or donations are made by the Manager, these do not come out of investor funds. Funds or donations are paid for by the Manager although in the name of First Mortgage Trust.