Kaipara District Council
Treasury management

Presentation by PwC Treasury Advisory
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11 June 2020

Introduction

Introduction

Thank you for the opportunity to present

- Independent and impartial treasury adviser to Council.
- We've been providing independent and tailored treasury advice to the sector since 1997.
- We are presently retained by 35 council clients.

Structure of presentation

This presentation sets out:

- Considerations relating to external credit ratings.
- Funding and interest rate risk positions.
- Key Treasury Policy changes.

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External credit ratings

Credit rating considerations

- In considering the use of a credit rating, there are two main considerations for Council:
  - Will economies of scale relating to new debt refinancing activities outweigh the cost of the credit rating?
  - Are the disciplines of increased management, governance, public scrutiny and reporting associated with the ongoing maintenance of a credit rating justified?
- Currently, 29 New Zealand Councils are formally credit rated, of which 23 are rated by Standard and Poor's (S&P) and 6 by Fitch Ratings.
- **Key benefits**:
  - The LGFA differentiates lending margins between councils that are credit rated and those that are not.

Rated AA	0 basis points p.a.
Rated AA-	5 basis points p.a.
Rated A+	10 basis points p.a.
Unrated	20 basis points p.a.

  - Provides an independent opinion of credit worthiness, financial strengths and weaknesses
  - A credit rating can promote greater financial discipline and awareness of Council's risk appetite
  - Provides a framework and boundary for risk tolerance (i.e. if a certain decision is made, will this have an adverse impact on Council's credit rating?)
  - Help Council to focus on risks and behaviours such as forecasting achievability of budgets

Credit rating considerations (cont.)

- Consideration should be whether the cost of a rating can be offset by the savings achieved within the funding portfolio.

Rating agency	Current approximate initial rating fees	Current approximate ongoing annual analytical surveillance fees
S&P	AUD51.25k / NZD55k	AUD51.25k / NZD55k
Fitch	~NZD45k	NZD45k

- **Scenario example to demonstrate cost savings**
  - Council will obtain at least a 0.10% p.a. benefit on new term borrowings with the LGFA through obtaining a credit rating (i.e. as per the table on the previous page).
  - Based on $50 million of term borrowings, this would result in a $50,000 p.a. benefit.
  - The above demonstrates the minimum saving if Council were to achieve a A+ rating.
  - If Council were to achieve a AA rating, a 0.20% p.a. benefit would be achieved providing an annual interest cost saving of $100,000.
  - The above example is for illustrative purposes only and the actual realised benefits would depend on Council's actual rating outcome.
- Council has a $25 million borrowing maturity in May 2021 which requires refinancing which would be able to be obtained at a lower cost of borrowing through the LGFA were a credit rating obtained.
- **Note that to achieve a break even cost and assuming a Fitch credit rating of AA- is achieved, a minimum amount of new and or refinanced debt of $30 million in the 12-months post obtaining the credit rating is required.**

Credit rating considerations (cont.)

- In making a decision as to whether to progress the process to obtain a credit rating or otherwise, Council must also be cognisant of the $220 million of 'shovel-ready' projects which have been put forward for consideration with Crown Infrastructure Partners (CIP).
- Where these projects are able to be financed through a grant or debt which remains on the Crown's balance sheet, Council's need for external debt raising will be reduced.
- Council should also contemplate the possibility that only a portion of the $220 million requested will be funded by CIP and further external borrowings will be required to obtained through the LGFA.
- These potential impacts on external debt financing requirements could mitigate or enhance the financial benefits which can be procured were Council to obtain a credit rating.
- The credit ratings process (a 4 - 8 week timeframe):
    - A lead analyst will be assigned to Council who will evaluate Council's creditworthiness.
    - Information will be obtained by published information, from interviews and discussions with management and Councilors.
    - The information received will be assessed against the ratings criteria relevant for the sector.
    - The analyst will take the information gathered to a rating committee and recommend a rating. The rating committee will assess the recommendation and vote on a credit rating.
    - This will then be fed back to Council who will have a chance to correct any false information.
    - Once this is complete, the rating will be published and Council can use this to source more attractive funding costs for long term debt.

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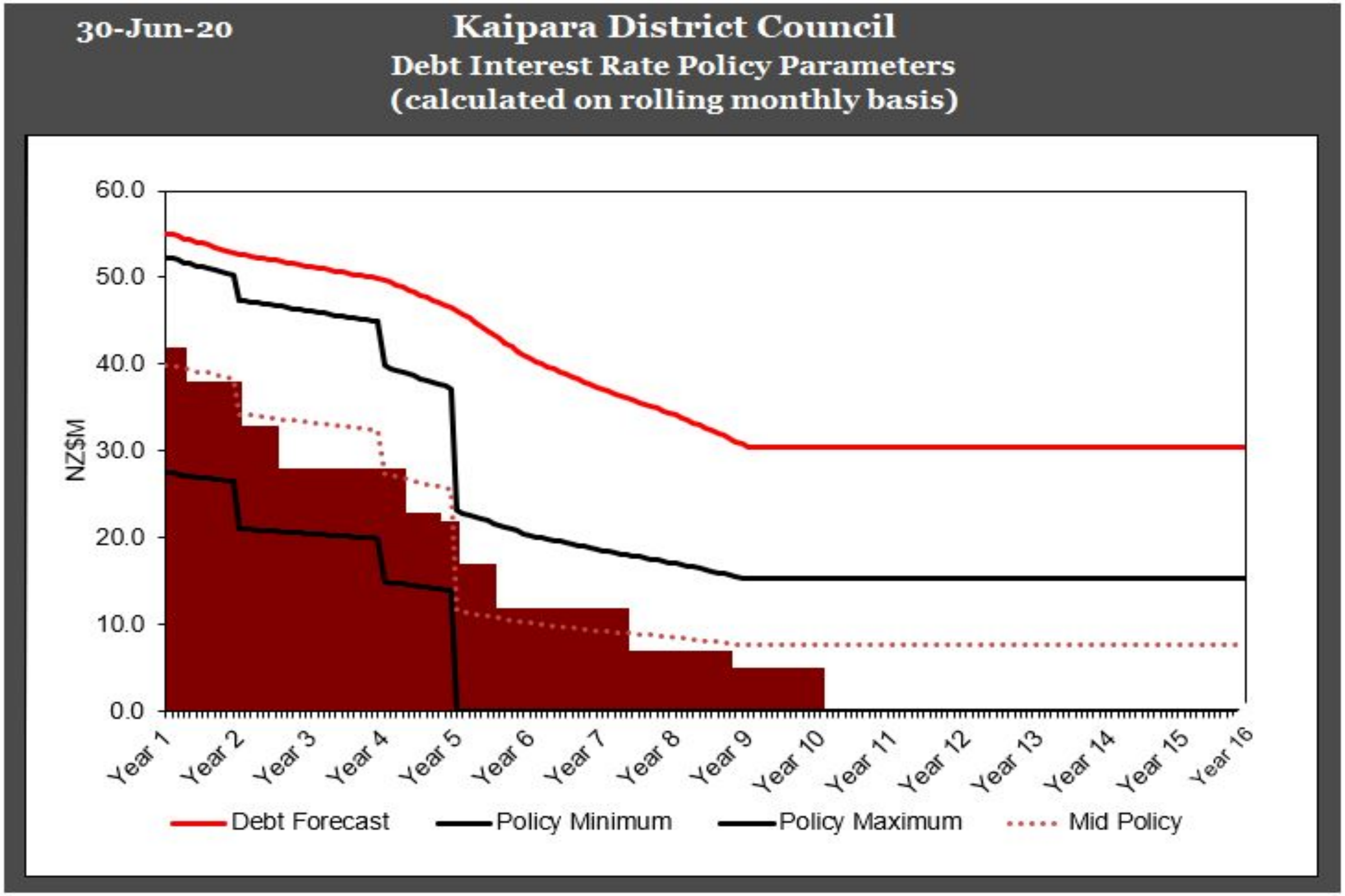
Funding and interest rate risk positions

Interest rate risk position



Funding and liquidity position

30-Jun-20

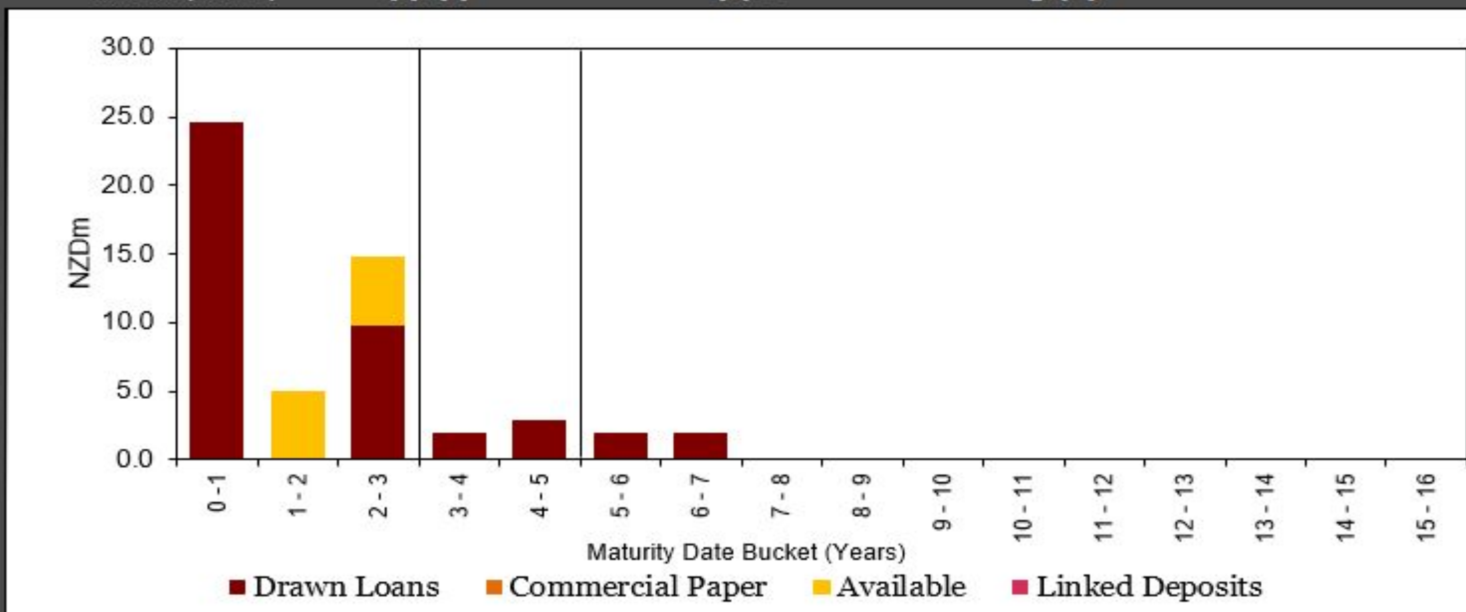
Kaipara District Council

Funding & Liquidity Risk Position

Committed Loans/Stock/Facilities/Investments $53.3m
Current External Debt $43.3m
Current Net Debt $43.3m

Policy Liquidity Ratio >=110%
Actual Liquidity Ratio 123%

	0 - 3 years	3 - 5 years	5 years plus
Policy Target Band	15%-60%	15%-60%	10%-60%
Actual	83%	9%	7%
Actual (NZDm)	44.44	4.92	3.94



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Key Treasury Policy Changes

Key Treasury Policy Changes

- Two main amendments recommended:
  - Updated interest rate risk control limits
  - More flexible funding maturity control limits

- Rationale for proposed changes:
  - Greater level of flexibility in the management of interest rate risks and debt refinancings
  - Recognition of structural shift lower in interest rate settings
  - Increased access to long dated financing and with greater ease
  - Ensuring economic decision making is fully supported

- Areas considered when recommending changes:
  - Council is a prudent financial manager.
  - Governance and oversight of intergenerational assets.
  - Statutory and financial objectives
  - Avoiding adverse interest rate related increases to rates and desire to maintain overall interest costs within budgets.
  - Stress-test scenario modelling to identify the best “all-weather” policy framework

Thank you.