

Finance and Operational Performance Committee

**Monday, 9 March 2009
Commencing at 9.30 am**

**Item 8: Draft Liability Management
 And Investment Policy**

SUPPLEMENT TO AGENDA OF THE FINANCE AND OPERATIONAL PERFORMANCE COMMITTEE TO BE HELD IN THE COUNCIL CHAMBER AT WAITAKERE CENTRAL, 6 HENDERSON VALLEY ROAD, HENDERSON, WAITAKERE, ON MONDAY, 9 MARCH 2009, COMMENCING AT 9.30 AM

8 DRAFT LIABILITY MANAGEMENT AND INVESTMENT POLICY

GLOSSARY

Long Term Council Community Plan 2009-2019 (LTCCP)

EXECUTIVE SUMMARY

The purpose of this report is to present the draft Liability Management and Investment Policy to be included within the Council's draft Long Term Council Community Plan 2009-2019 (LTCCP). The policy is a mandatory requirement of the LTCCP process, under the Local Government Act 2002 and is intended to provide predictability and certainty about the sources and levels of funding the Council can manage.

RECOMMENDATIONS

It is recommended that the Finance and Operational Performance Committee resolve to:

1. **Receive** the Draft Liability Management and Investment Policy Report.
2. **Agree** that it be recommended to the Council that the draft Liability Management and Investment Policy be included as part of the Long Term Council Community Plan 2009-2019.

BACKGROUND

1. The Local Government Act 2002, Section 102, requires a local authority to adopt a Liability Management Policy and an Investment Policy. Every three years as part of the LTCCP process the Council includes the policy as part of the LTCCP for public consultation. The Policy is one of several policies required under section 102 of the Act and must state the Council's policies in respect of the management of both borrowings and other liabilities. This must include specifics on:
 - interest rate exposure;
 - liquidity;
 - credit exposure;
 - debt repayment;
 - specific borrowing limits; and
 - the giving of securities.
2. At the recent deliberations of the Long Term Council Community Plan and Annual Plan Committee it was agreed that the draft Liability Management and Investment Policy be considered by the Finance and Operational Performance Committee for recommendation to the Council.

STRATEGIC CONTEXT

3. The Liability Management and Investment Policy is an overarching policy on how the Council's borrowing, investing and other liabilities will be managed. The management of these activities is the result of work undertaken in any of the Council's strategic platforms.
4. The process of amending the policy would fall under the Active Democracy platform.

DRAFT LIABILITY MANAGEMENT AND INVESTMENT POLICY

5. The draft Liability Management and Investment Policy forms a part of the Council's LTCCP. The draft policy considers the current financial market environment and provides the policy framework in how the Council will manage its borrowings, other liabilities and investments. The draft Liability Management and Investment Policy will be circulated separately.
6. The current policy has been reviewed and the draft Liability Management and Investment Policy to be consulted upon contains the following key changes:
 - Changes to reflect different job titles of staff;
 - Recognition and ability to hedge commodity exposures;
 - The addition of new interest rate risk management products;
 - The allowance to undertake treasury risk management on a scale greater than a 12 month rolling forecast;
 - Amendments to fixed and floating interest rate limits;
 - Amendments to debt maturity profiling;
 - Increases to Counter party credit limits; and
 - Amendments and deletions to certain policy ratios.

DEBT FUNDING REQUIREMENTS

7. The Council has signalled through the draft LTCCP the need to borrow funds to meet the objectives sought within the draft LTCCP. Waitakere has seen rapid growth over recent years and the consequences of this growth is that the infrastructure needs of the City must be either added or improved to meet the increasing demands. If the infrastructure needs of the City were to be funded from rating revenues, the level of rates per household would be unaffordable and the burden would also fall only on the current ratepayers. The use of borrowing for asset creation is considered appropriate because it benefits both current and future residents.
8. Major projects in the early stages of the draft LTCCP include the New Lynn transport interchange and new infrastructure around Westgate and Hobsonville, will require extensive funding. These projects are amongst the largest currently being undertaken in New Zealand by a local authority. As a result of this, the Council's debt position is expected to increase over the construction period, but will quickly decrease as alternative funds are received and applied to the repayment of debt.

9. Waitakere's proposed gross capital expenditure for the draft LTCCP is \$1.322 billion, approximately 73% of which relates to projects which, at least in part, are required to meet the demands of the city's growing population. The majority of the city's growth related projects result in the need to extend the capacity of the city's existing transportation, water supply, wastewater and storm water infrastructure assets. Many of these projects are designed to provide growth capacity for the city for beyond 10 years. In the development of the draft LTCCP, the Council has budgeted to fund the growth component of its capital projects from debt which will be repaid from development contributions charged to developers. The remainder of the Council's debt will be funded from rates and other revenue funding sources. The following table shows the Council's total capital expenditure:

Gross Capital Expenditure 2009 to 2019

Details	Total Gross Capital Expenditure (\$000's)
Transport Assets	585,741
Parks and Green Assets	161,365
Stormwater	132,739
Wastewater	122,975
Other	104,093
Water Supply	75,205
Strategic Projects	60,815
Libraries	41,103
Leisure and Community Facilities	22,113
Cemetery	16,366
Total	1,322,515

10. Asset creation is funded from various sources. These are:

Source	Utilisation
Proceeds from rating for depreciation (Rates)	Renewals
Loans	New capital expenditure and renewals where the proceeds from rating for depreciation are insufficient
Development Contributions	Growth funded capital expenditure
Financial Contributions	Reserve contributions and environmental mitigation
Subsidies	Transport for qualifying works and Stormwater for Project Twin Streams
Reserves	Where special and separate funds are available

11. The loan funded capital expenditure results in the following net debt levels: (Net debt which is defined as total debt minus investments in property acquired for development).

Details	2009/ 2010	2010/ 2011	2011/ 2012	2012/ 2013	2013/ 2014	2014/ 2015	2015/ 2016	2016/ 2017	2017/ 2018	2018/ 2019
	(\$000's)	(\$000's)	(\$000's)	(\$000's)	(\$000's)	(\$000's)	(\$000's)	(\$000's)	(\$000's)	(\$000's)
Gross Debt	590,684	694,099	801,924	903,041	986,670	1,041,142	1,051,968	1,053,071	1,034,235	978,784
Less Development Properties	63,722	63,722	63,722	63,722	63,722	63,722	63,722	63,722	63,722	63,722
Net Debt	526,962	630,377	738,202	839,319	922,948	977,420	988,246	989,349	970,513	915,062

12. This level of debt is primarily driven by the growth occurring in the City in the Northern Strategic Growth Area (Westgate and Hobsonville) and New Lynn. The draft Liability Management and Investment Policy contains detail on the approach to the management of the Council's borrowing and Investment strategies.

13. The draft policy contains the following ratios that assist in providing guidance to the management of debt at sustainable borrowing levels.

Details	2009/ 2010	2010/ 2011	2011/ 2012	2012/ 2013	2013/ 2014	2014/ 2015	2015/ 2016	2016/ 2017	2017/ 2018	2018/ 2019
Net debt as a percentage of total income	200%	213%	238%	256%	267%	259%	246%	227%	207%	179%
Net interest as a percentage of total income	12%	13%	15%	16%	17%	18%	17%	17%	16%	15%
Net interest as a percentage of rates (including water)	20%	22%	24%	26%	26%	26%	25%	23%	22%	20%

14. The Ratios are increasing in the interim years of the draft LTCCP as a result of the intensive investment in infrastructure required in the growth areas of the city. The recovery of developer contributions to repay debt is staggered over a 20 year time frame. The ratios are used as an annual guide to the management of debt. There is some uncertainty as to the precise timing of the expenditure patterns requiring external financing and therefore the ratios maybe in excess of the peak debt level reached in any given year.

CAPACITY TO BORROW

15. The Council has the benefit of having statutory powers to collect rates. Investors have a strong security as their investment is secured by the Council's rating powers. The Council has also obtained a Standard and Poor's credit rating which enables the Council to have access to a wider range of investors who can only invest in entities with an appropriate credit rating. The Council's credit rating is currently A+ long term and A-1 short term. These ratings demonstrate the Council's strong ability to meet its debt commitments.

16. In order for the Council to meet its immediate and medium term financial obligations, the Council has access to a total of \$200 million of committed standby bank facilities. These facilities provide flexibility for the management of debt as the lending margins are fixed for the duration of the facility agreement, which provides some certainty on the underlying interest rate exposure. They are also flexible in that they can be repaid immediately if an alternative and economically beneficial funding source arises.

DEBT REPAYMENT STRATEGY

17. The draft LTCCP to be considered by the Council for adoption on 20 March 2009 provides for Council controlled rate increases from 2011/2012 onwards of 7.95%. This enables from that year a debt repayment strategy that reduces reliance on loan funding of renewals. In the later years of the draft LTCCP the Council's gross borrowings peak at an estimated \$1,053,071 in 2016/2017 and then starts reducing to \$978,784 by 2018/2019. The Council does not have unlimited balance sheet capacity. The aggregate debt position relative to the size of the current and projected revenue base needs to be managed carefully.
18. This approach recognises that there may be occasions when growth related projects may need to be cut, or deferred if development revenue slows or access to loan funding is restrictive or cost prohibitive. Projects will need to be assessed on a continual basis throughout each year of the plan. The draft LTCCP provides for the loan funding for capital expenditure required to restore assets to their original condition. The reliance on this source of funding declines from 2011/2012 as more rates funding is provided.

Details	2009/ 2010 (\$000's)	2010/ 2011 (\$000's)	2011/ 2012 (\$000's)	2012/ 2013 (\$000's)	2013/ 2014 (\$000's)	2014/ 2015 (\$000's)	2015/ 2016 (\$000's)	2016/ 2017 (\$000's)	2017/ 2018 (\$000's)	2018/ 2019 (\$000's)
Loan Funding of Renewals	22,120	25,378	24,207	22,068	15,699	7,205	1,844	1,998	0	0

DECISION MAKING

19. The Finance and Operational Performance Committee needs to recommend to the Council, the draft Liability Management and Investment Policy for inclusion in the draft LTCCP for consultation.

CONSULTATION

20. The consultation on the draft Liability Management and Investment Policy forms part of the consultation process of the draft LTCCP. Consultation is scheduled to commence on 30 March 2009 and closing 30 April 2009, with hearings being conducted during May.

CONCLUSION

21. The draft Liability Management and Investment Policy which forms part of the draft LTCCP outlined in this report is required to be consulted upon. There have been some changes to the current policy to reflect the changing financial market environment and the Council's proposed expenditure programmes.

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