

COMPARATIVE ANALYSIS

Waitakere City is the one of the lower rated New Zealand local governments. Waitakere City's closest rated peers in New Zealand are Hutt City Council (Hutt) (AA-/Stable) and Tauranga City Council (A+/Stable) and internationally, Penrith City Council in Australia (AA/Pos) and the City of Laval in Canada (A+/Pos).

Domestic Peers

Waitakere City is not rated at the same level as Hutt City largely due to the size of its after capital deficits and direct debt. Hutt City, in contrast to Waitakere City projects small cash deficits after capital expenditure at less than 10% of revenue compared with Waitakere City's relatively large forecast cash deficits after capital expenditure in fiscal 2006. Further, Hutt City has lower net debt than Waitakere City, with direct debt as a percentage of operating revenue at 73% compared with over 100% for Waitakere.

Waitakere City is rated at the same level as Tauranga City given its aggressive but controlled capital expenditure program and persistent cash deficits after capital spending. Unlike Tauranga City, Standard & Poor's believes that Waitakere City has higher expenditure flexibility given its persistent capital expenditure deferral and comparatively, largely discretionary capital expenditure, but shares Tauranga City's high degree of autonomy to augment its incomes given high levels of modifiable revenues.

Tauranga City's forecast financial performance is similar to Waitakere City, with accrual and cash operating surpluses, offset by large and aggressive capital expenditure programs which drive persistent and moderately large overall cash deficits. Similar to Waitakere City, the balance of risks on Tauranga City's finances tends to be positive because actual capital spending outcomes are likely to be better than expected given external and internal capacity constraints to achieve their respective capital programs.

International Peers

Waitakere City's direct debt as a percentage of operating revenue at over 100% is consistent with the international 2004 A+ median for direct debt as a percentage of operating revenue (101%).

The Canadian City of Laval (A+/Positive) is a close peer for Waitakere City with a similarly high current debt; indeed it is higher than Waitakere City's at about 112% of operating revenue. Laval's direct debt as a percentage of operating revenue could rise up to 125%, similar to Waitakere City's forecast rising debt in fiscal 2005.

Despite this higher debt, Laval has significant economic advantages, strong support from senior levels of government, strong and consistent budgetary performance and a gradually reducing debt. Laval's outlook reflects Standard & Poor's expectation that Laval will continue to enjoy both its economic advantages and substantial support from the province. The outlook also reflects Standard & Poor's expectation that economic growth in Laval is likely to accelerate as a result of these advantages.

Table 1 Peer Comparison 2005 (Core)

Council	Waitakere City Council*	Hutt City Council#	Dunedin City Council*	City of Laval#	Penrith city Council#	Tauranga City Council*
Long term Issuer credit rating	A+/Stable	AA- /Stable	AA- /Stable	A+/Positive	AA/Stable	A+/Stable
Country	New Zealand	New Zealand	New Zealand	Canada	Australia	New Zealand
<i>three-year averages</i>						
Accrual operating balance (% of operating revenue)	(14.7)	(7.1)	(0.7)	n.a	(3.6)	1.3
Operating cash balance (% of operating revenue)	9.1	22.2	28.3	22.6	9.2	19.8
Capital expenditure (% of total expenditure)	28.5	28.1	25.6	29.9	20.2	40.3
Balance after-capital-expenditure (% of operating revenue)	(10.2)	(16.7)	25.6	6.96	1.26	(24.1)
<i>2004 figure</i>						
Direct debt (% of operating revenue)	114.2	86.3	93.6	111.2	48.6	113.7

*2005, #2004, N.A not available.

SYSTEM SUPPORTIVENESS AND PREDICTABILITY

Strong Central Government Supervision. The council's rating benefits from the national government of New Zealand's (the Crown's) supervisory intervention and its operation within the Crown's mandated financial framework.

There is no formal fiscal equalization mechanism, or explicit guarantee for the debt obligations of the council, but Standard & Poor's believes that it is highly probable that the Crown would provide emergency support to local governments if required. Whilst there are no precedents of the Crown providing such support to a local government, this is because the need for such support has never arisen, not a reflection of the willingness of the Crown.

The Crown's involvement in council operations also extends to the right to dismiss the elected representatives of the local government, and to intervene in the affairs of local governments. The Crown may take supportive action before a local government's financial condition jeopardizes its solvency, positively affecting the council's credit quality.

The council's long-term financial stability is assisted through the requirement for stringent planning and reporting. In addition to an annual report and an annual plan, councils are required to prepare a 10-year long-term council community plan, asset management plans, and revenue and financing policies, at least every three years. Investment and liability management policies are also prepared, while all financial statements are presented on an accruals basis.

ECONOMY

Waitakere City's growing population, robust local economy and diverse economic structure are slightly positive factors contributing to the council's credit quality, however, the overall impact of these factors on its finances is limited, because revenue collection and expenditures are fairly insulated from changes in the economy.

Located on Auckland's periphery, which lies in the north part of the North Island. Waitakere has experienced strong population growth with its census 2001, 168 750 population expected to increase to 223 300 by fiscal 2016. In fiscal 2004, Waitakere City was ranked 13th out of 73 in relation to population growth of 73 TAs, with annual growth slightly below the Auckland region from 1994-2004 (2.7%) but significantly higher than the New Zealand average (1.4%)

About 31% of Waitakere City's GDP is from manufacturing and is also the largest employer in the region. In recent times, there has been increased diversification into the services industries and retail trade. Waitakere City experienced GDP growth of 4.8% in fiscal 2005, compared with 4.4% for the Auckland Region 4.4% and 3.6% for New Zealand. Waitakere City's employment growth also exceeded the Auckland Region at 5% compared with 3.9% respectively.

A key problem faced by Waitakere City is its lower ratio of jobs per capita. This is primarily the result of more than 50% of Waitakere's population commuting elsewhere for employment hindering the city's ability to foster sustainable economic development.

MANAGEMENT CAPACITY AND CREDIBILITY

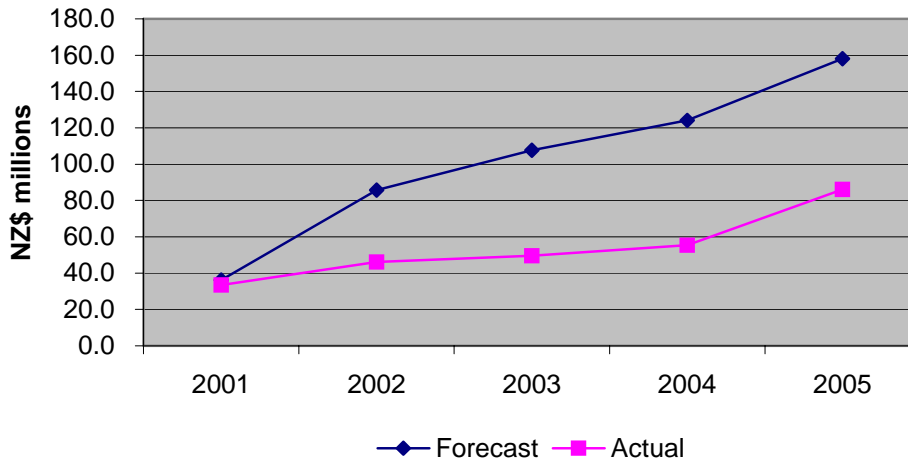
Strong. The Crown's legislative environment, which promotes a culture of planning, transparency, and consultation, ensures a very strong management culture and provides support to the rating. The preparation of a long-term council community plan at least every three years by all local governments in New Zealand ensures councils have a forward-looking approach to prudent financial management, and sets an important baseline of operating and capital spending requirements and funding strategy.

The 2006-2016-community plan development process is currently underway, with preliminary discussions not revealing any large changes.

Management's capital plan over the long-term planning period tends to be good, with budgets set to support and implement the plan. Capital spending tends to significantly lag its budget, as the council lacks capacity to meet its budgeted challenging capital expenditure program (refer chart 1)

Chart 1

Capital Expenditure Spending Lags Budget



Waitakere City has historically maintained good control over its operating expenditures relative to its operating revenues however; negative growth in fiscal 2005 has meant that operating growth rates have lagged operating expenditure growth over the three years to fiscal 2005. Following a proposed general rate increase in the 2006 Annual Plan, operating revenue growth is expected to outstrip operating expenditure growth.

FINANCIAL FLEXIBILITY

High. Similar to all New Zealand local governments, there are minimal legislative limits on council general property rates, separate rates and miscellaneous charges increases. Also, there are no restrictions on the council to levy separate rates and user charges linked to specific projects significantly, both contributing to revenue flexibility.

Waitakere City has forecast an increase in its general rate for fiscal 2006 to meet increasing council operation costs. Further, the council adopted a development contributions and financial contributions policy in fiscal 2005 to recover capital expenditure costs incurred by the council as a consequence of growth.

Although substantial grants, subsidies, and financial contributions from other levels of government can diversify a council's revenue base, they can also restrict a council's financial flexibility. In recent years, Waitakere City receives minimal revenue from the Crown in the form of grants and subsidies for operating purposes, and as such its financial flexibility has not been adversely impacted. In fiscal 2005, Waitakere City received NZ\$13.3 million or about 7.5% of total council revenue in the form of income for non-operating (capital) purposes.

Expenditure variances have historically been low because the council does not perform any significant welfare functions, which can be linked to economic cycles and are highly volatile. Similarly, the core council is not responsible for chronically expensive and high growth health, education or justice sectors.

FISCAL PERFORMANCE

Waitakere City has strong history of recording accrual operating deficits (using Standard & Poor's measures), whilst maintaining healthy operating cash flow surpluses. Persistent reported accrual operating deficits are generally uncommon for local governments in New Zealand because legislation requires councils to prepare balanced budgets; however, deficits may be budgeted in the short term if they ensure surpluses are budgeted in the medium term.

In Waitakere City's case, this difference represents the large number of revenue items that Standard & Poor's omits as part of its accounting adjustment, because this type of capital funding is not available for operating expenditure or debt servicing. The inclusion of revenue items, such as developer contributions, central government capital grants and subsidies and infrastructure assets vested in council from property developers would show Waitakere posting consistently strong accrual operating surpluses. Nevertheless, accrual-operating deficits are projected to continue over the medium term.

LIQUIDITY AND DEBT MANAGEMENT

Waitakere City has a strong liquidity position, with cash, including some holdings of sinking funds, of NZ\$2.3 million offsetting short-term debt of NZ\$16 million at fiscal 2005. Waitakere City has committed credit lines totaling NZ\$85 million to cover its liquidity needs.

The council's liability management and investment policy is clear, and enforces five key limits. Standard & Poor's does not view these limits as onerous; therefore, failure to meet these may require a reassessment of the rating. The limits are:

- Net debt not to exceed 20% of equity (forecast to increase to 16.4% by fiscal 2006 from 9.0 % in fiscal 2005)
- Net debt not to exceed 150% of income (forecast to increase to 121.1% by fiscal 2006 from 79.0% in fiscal 2005)
- Net interest not to exceed 15% of income (forecast to increase to 5.0% by fiscal 2006 from 5.2% in fiscal 2005)
- Net interest not to exceed 20% of annual rates income (forecast to increase to 10.0% by fiscal 2006 from 9.5 % in fiscal 2005)
- Liquidity (undrawn committed loan facilities as a % of next quarters maturity portion of net debt) to exceed 100%.

DEBT

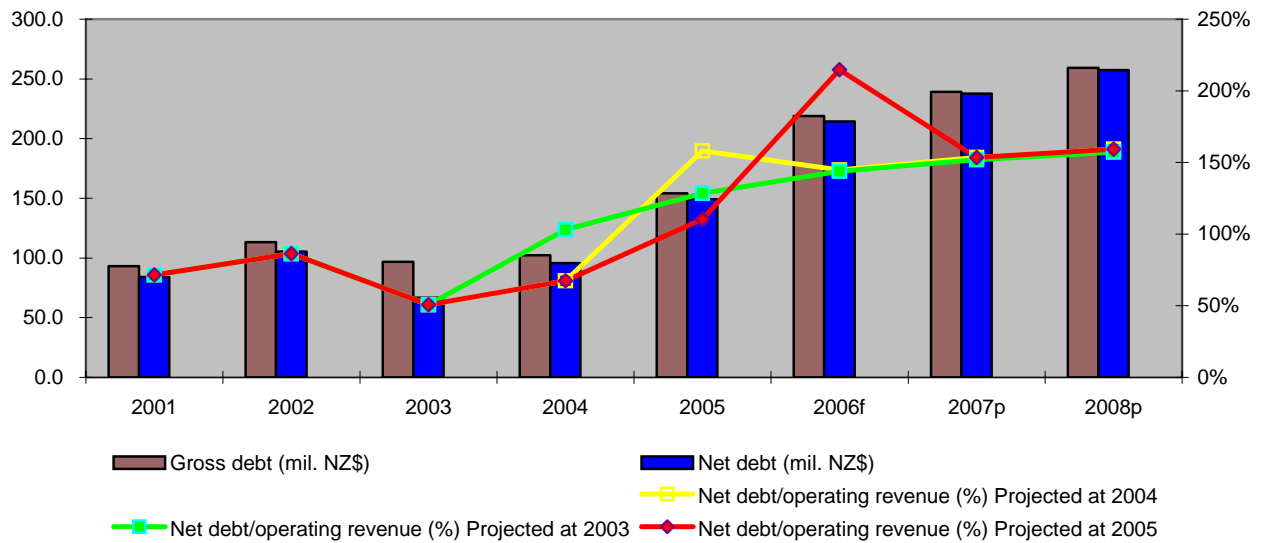
Waitakere City's fiscal 2005 debt levels are high, with net debt to operating revenue greater than 110% compared to about 68% in fiscal 2004. The council's fiscal 2005 debt is significantly lower than forecast in its 2005 Annual Plan due to internal and external capacity constraining the ability to achieve its capital expenditure program. A large component of the fiscal 2005 capital expenditure program has been brought forward into the fiscal 2006 program.

In addition to planned increases in debt over fiscal 2006 to fund both the capital expenditure program planned in the LTCCP and capital expenditure deferred from prior years, the council's 2006 Annual Plan includes new borrowings above that previously anticipated, about NZ\$40 million. This increase is primarily the result of: investments in Passenger Transport that have arisen as a result of external funding becoming available, replacement of the Council's computer systems, increased capital expenditure in roading, wastewater, stormwater and water supply and the inclusion of a contingency for strategic land purchase.

Since 2003, Waitakere City has recorded an increasing net debt to operating revenue ratio given the council's spending on its capital expenditure plan. Over the three years to fiscal 2005, the council has, on average, spend 30% of its total expenditure on capital expenditure and in fiscal 2005 the council achieved its NZ\$86million worth of capital expenditure.

Waitakere City is forecasting over NZ\$190 million capital expenditure (NZ\$130 million debt funded) in fiscal 2006. Given the council's history of capital expenditure slippage against plan (refer chart 2) and its peak capital expenditure over the last 5 years being NZ\$86 million, Standard & Poor's believes that net debt is unlikely to peak at the expected 215% of operating revenue. Despite this, net debt greater than about 120% of operating revenue would make Waitakere City council the most indebted rated council in New Zealand.'

Chart 2
Net Debt Actuals Trending Up Despite Capital Expenditure Lags



OTHER LIABILITIES

Non-debt and contingent liabilities are small and support credit quality. Direct guarantees and total contingent liabilities increased over fiscal 2005 from fiscal 2004 by 30% and 50% respectively and together totaled NZ\$18.6 million. The council's wholly owned subsidiaries and associates are debt free providing an insignificant impact on credit quality at the consolidated level. Litigation claims in respect of potential repair costs from leaky buildings also increased by 4% to NZ\$6.9 million. The council has no superannuation scheme for its employees.

Although limited at this stage, private-public partnership programs may pose some risk to Waitakere City's credit quality if pursued in the future for transport projects. Standard & Poor's will consider the political, moral, and financial incentives facing the council if a project faces financial difficulty, as the council may be required to bail out the project even though there may be no legal obligation to do so.