

Finance and Operational Performance Committee

**Thursday, 14 November 2002
Commencing at 9.30 am**

**Item 9: Borrowing and Investment
 Report**

**Item 12: First Quarter Financial
 Review**

**SUPPLEMENT TO AGENDA FOR AN ORDINARY MEETING OF THE FINANCE AND
OPERATIONAL PERFORMANCE COMMITTEE TO BE HELD IN THE CIVIC
CENTRE, 6 WAIPAREIRA AVENUE, LINCOLN, WAITAKERE CITY,
ON THURSDAY, 14 NOVEMBER 2002
COMMENCING AT 9.30 AM.**

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PART IV - FINANCE**9 BORROWING AND INVESTMENT REPORT****PURPOSE OF THE REPORT**

Waitakere City Council enters into treasury related financial contracts in the ordinary course of its business. It is the role of Council's funds management function to manage such contracts and the impact that they have on the organisation. All funds management transactions are governed by the Borrowing and Investment Policy prepared in compliance with the Local Government Act 1974. As a requirement of the Borrowing and Investment Policy, this report informs Council on the current and future movements of Council's debt and cash investments and provides a general commentary of financial market conditions.

SUMMARY OF BORROWING AND INVESTMENT MOVEMENTS, SEPTEMBER 2002

The Council's gross term debt position has decreased by \$0.576 million since August with a closing balance at September month end of \$122.6 million. Working capital borrowings of \$12.9 million as at 30 September 2002 have been funded using internal borrowings and unsecured loans.

SIGNIFICANT FUNDING TRANSACTIONS ENTERED INTO DURING SEPTEMBER 2002

- New interest rate swap. Notional value \$5 million, maturing 13 September 2012, Waitakere City Council pays fixed interest rate of 6.605% and receives floating interest rate of New Zealand Bank Bill Rate – FRA (NZD-BBR-FRA).
- Issued new floating rate note (FRN) of \$5 million, maturing 15 March 2005, at an interest rate of NZD-BBR-FRA plus 0.10%.
- Agreed to issue new FRN of \$5 million on 15 October 2002, maturing 15 April 2004 at an interest rate of NZD-BBR-FRA plus 0.10%.
- Agreed to issue new FRN of \$5 million on 15 October 2002, maturing 15 October 2004 at an interest rate of NZD-BBR-FRA plus 0.10%.
- Rolled ARST investment of \$1,099,508.43 for 60 days at an interest rate of 5.86%.
- Reinvest Sinking Fund of \$450,000 for 33 days at an interest rate of 5.86%.
- Reinvest Sinking Fund of \$1.5 million for 60 days at an interest rate of 5.86%
- Reinvest Sinking Fund of \$1,697,200 for 32 days at an interest rate of 5.85%
- Rollover Sinking Fund of \$1,667,452.73 for 60 days at an interest rate of 5.87%
- New interest rate swap. Notional value \$5 million, maturing 25 September 2010, Waitakere City Council pays fixed interest rate of 6.5% and receives floating of NZD-BBR-FRA
- New forward start interest rate swap. Notional value of \$10 million starting 1 August 2003, maturing 1 August 2012. Waitakere City Council pays fixed interest rate of 6.565% and receives floating interest rate of NZD-BBR-FRA.

UNITEDNETWORKS LIMITED SHARE SALE PROCEEDS 29 OCTOBER

Waitakere City Council received on 29 October 2002 an amount of \$56,353,589.60 representing 37.201% of the available proceeds from the shares held in trust by the UnitedNetworks Shareholders Society Inc. The Society retained \$8.9 million of the total sale proceeds for the continuation of the work to under-grounding power cables over the next two years.

The receipted funds were immediately used to offset overnight borrowing costs, with the balance invested in the interim in short-term bank deposits. While this position is not optimum, it does represent a tolerable level of risk, until limits for other institutions can be adopted. Next months report to this Committee will reflect the transactions entered into.

AMENDMENTS TO THE BORROWING AND INVESTMENT POLICY

The following amendments are proposed to the Borrowing and Investment Policy to better reflect the current and future risk profile associated with certain classes of investments.

Until now, these investment limits have not been challenged, simply because Council has not had sufficient investment funds available to consider investing in anything other than short term Bank deposits. With the early release of the UnitedNetwork Limited shares, the occasion has arisen that diminishes the possible yield that could be achieved, without incurring undue risk, simply because the limits prescribed are restrictive.

It is therefore proposed that the following new investment maximum levels be approved for inclusion in the Borrowing and Investment Policy - **Section 5.3 Counterparty Credit Risk.**

Counterparty/Issuer	Minimum long term credit rating – stated and possible	Existing Investments maximum per counterparty (\$m)	Proposed New Investment Maximum per counterparty (\$m)	Total maximum per counterparty (\$m)
NZ Government	A-	Unlimited	Unlimited	unlimited
State Owned Enterprises:	A-	5.0	5.0	5.0
- Nil approved				
NZ Registered Bank:	A-	10.0	15.0	25.0
- Bank of New Zealand				
- National Bank of NZ Ltd				
- ANZ Banking Group				
- Westpac Trust				
- ASB Bank Ltd				
- Commonwealth Bank Of Australia				
Corporate Bonds:	A-	2.0*	5.0*	5.0
- Nil approved				
LABT		2.0	5.0	5.0
Local Government Finance Corporation		2.0	5.0	5.0
Local Government Stock	A- (if rated) Unrated	2.0** 0.5**	5.0** 5.0**	5.0 5.0

* Subject to a maximum of \$20.0m investment in corporate/secured bonds at any one point in time.

** Subject to a maximum of \$30.0m investment in Local Government stock at any one point in time, including Local Government Finance Corporation.

FINANCIAL MARKET COMMENTARY

Interest Rate Overview

With the introduction to a 1% to 3% medium term inflation outlook, the Reserve Bank of New Zealand is now less likely to raise the Official Cash Rate in the short term. This was certainly the thrust of Governor Bollard's speech to the review conducted on 2 November, 2002 with a stable approach taken.

New Zealand interest rates have been extremely attractive for the past six months from overseas investors who have exited their own equity market. With US interest rates at 40 year lows, investors have been attracted to the higher yields achieved from Australian and New Zealand interest rate markets. This has made availability of quality interest rate instruments scarce. However, once the US Federal Reserve start to raise interest rates, the most likely outcome will be a sell off of the New Zealand market, effectively saturating the local market with corporate bonds, while decreasing liquidity.

News of Moody's New Zealand country credit rating being upgraded to Aaa, the highest rating of credit worthiness, achieved little in the way of media coverage, yet represents good news to New Zealand global borrowers.

Interest Rate Expectations

New Zealand short term interest rates have been edging higher over the last few weeks with the 90 day bank bill currently ranging between 5.89% to 5.94%. This suggests the markets expectation of Official Cash Rate increases in early 2003. Volatility in longer term local interest rates remains with 10 year bond swap rates ranging between 6.70% and 7.0%.

Pressure remains centred on the US economy with the likelihood of further interest cuts to US Federal Funds, with December 2002 Federal Funds futures trading at 1.40% and March 2003 at 1.275% fully supporting a 0.50% cut. The perception is that the US consumer needs a present to encourage continued expenditure throughout the holiday season.

Further offshore interest rate cuts are likely to increase the attractiveness of local returns from offshore lenders in the near term, as current interest rate spreads between the US and New Zealand at a ridiculously high 250 basis points.

It has become an increasing difficult call on what the Reserve Bank of New Zealand is likely to do. The strengthening of the New Zealand dollar over the past year decreases the cost of imports, not necessarily for the consumer, while the opposite position negatively effects exportations. Primary industry income is expected to be lower this year than last, leading through to reduced local consumer spending. Inflation remains subdued, hence the necessity to raise the Official Cash Rate in the near term appears unjustified.

Up coming dates

Monetary Policy Statement	20 November 2002.
Official Cash Rate announcement	23 January 2003

CONCLUSION

All transactions covered by this report have complied with the requirements of Council Policy. Council's current net term debt is within the limits approved in the 2002/2003 Annual Plan.

RECOMMENDATIONS

1. That the information be received.
2. That the counterparty credit risk limits presented in this report, affecting section 5.3 of the Borrowing and Investment Policy be adopted.

Report prepared by Bruce Wilkin, Funds Accountant.



12 FIRST QUARTER FINANCIAL REVIEW

PURPOSE OF THE REPORT

The purpose of the report is to inform the Finance and Operational Performance Committee of any financial issues in relation to the 2002/2003 Annual Plan as at 30 September 2002.

BACKGROUND

At each quarterly point in the year a review of revenue and expenditure against budget is undertaken including revised forecasts for the balance of the year. Any issues arising from the review are reported through to this Committee.

ISSUES

A130

Overall operational expenditure (net of revenue) is tracking within budget for the first 3 months. This is consistent with this early period in the year where some projects and programmes have yet to be commenced. Attached at page A130 is a summary of Operational and Capital expenditure for the first quarter. The forecast to year end, overall, is tracking to budget however there are a number of issues within that balanced forecast. These are commented on below:-

1. Parking Fine Revenue (net of costs) is expected to be approximately \$200,000 more than originally estimated.
2. Legal expenses are tracking high and are forecast to exceed budget by approximately \$68,000 by year end. This has been a trend over the last few years and is being monitored.
3. The Vehicle Testing Station is unlikely to meet budget projections by approximately \$100,000 due to a continued down turn in the market coupled with an inability to reduce costs without seriously effecting customer service.
4. It is expected that the dividend from Techscape will be \$80,000 short of the budget.

The proceeds from the sale of the UnitedNetwork shares is expected to produce a saving in interest in the current year of \$2.15 million. It would be appropriate for the use of this saving to be determined during the draft Annual Plan process for 2003/2004.

It should be noted that at this early stage in the year projections are preliminary and that the main focus is to identify major issues or warning signs. A clearer picture of the year end position will be established at the Half Yearly Review which will feed into the 2003/2004 Draft Annual Plan Process.

Capital Expenditure

A131 A schedule of Capital Expenditure changes is attached at page A131. The majority of the changes, along with associated issues, have already been reported through to the appropriate Committees. In effect any increases have been more than offset by the reduction in the Hobsonville Roothing Project resulting in minimal effect, at this stage, to any overall financial forecasts.

Proposed Carry Forward Projects

A132 A schedule of proposed carry forward projects is attached at page A132. These amount in total to approximately \$7 million of which \$6.3 million are related to new Library projects primarily relating to the proposed New Lynn and Glen Eden Libraries.

The level of carry forwards is likely to increase as the year progresses. There are always issues surrounding the timing of strategic land purchases and, although all infrastructure projects, other than those reported, are on track to be completed, operational issues may arise resulting in delays. Again, it is still relatively early in the year and a clearer picture will be drawn at the Half Yearly Review.

It should be noted that interest savings in respect of carry forward projects have already been factored into the current years Annual Plan and are unlikely to effect forecasts until later in the year when the timing of capital expenditure projects is more certain.

CONCLUSION

All indications at the First Quarter Review are that net expenditure overall is tracking to budget. The exception to this is the interest savings impact of the sale of the UnitedNetwork shares. Although it is too early in the year to accurately forecast the year end position, there is nothing of a material nature, at this stage, which is likely to significantly impact on these projections. The Half Yearly Review, due for completion in February 2003 will provide a clearer picture of the likely year end position.

RECOMMENDATION

That the information be received.

Report prepared by: Andrew Pollock, Director: Finance.



**Waitakere City Council
Management Report
September 2002**

Operating Costs	Actual Spent YearToDate	% Spent on Budget	Full Year Budget
Executive Suite	287,803	14%	2,073,678
Maori Issues	119,509	28%	419,729
Public Affairs	392,635	20%	1,948,639
Corporate and Civic Services	2,875,338	25%	11,392,573
Finance	304,848	22%	1,397,603
Strategic Projects	541,739	16%	3,347,232
Strategic Group	1,153,322	22%	5,172,175
City Enterprises	6,454,878	25%	25,574,388
City Services	5,887,089	18%	32,417,725
Total Operational Expenditure	18,017,161	22%	83,743,742

Capital Expenditure			
Executive Suite	0	0%	10,000
Public Affairs	0	0%	10,000
Strategic Projects	316,889	1%	35,814,364
Corporate and Civic Services			
Plant Renewal	99,477	19%	511,800
Civic and Administration	20,537	1%	1,884,000
Information Management	146,000	5%	2,661,922
Libraries	230,045	9%	2,621,514
City Enterprises			
Animal Welfare Services	0	0%	25,000
Cemetery & Crematorium	31,147	3%	1,092,900
Property Expenditure	106,289	8%	1,339,500
Aquatic and Recreation Centre	2,225,556	45%	4,968,500
Solid Waste and Baling Station	2,634	1%	300,000
Ecowater Renewals	240,041	4%	6,232,566
Ecowater Capital Works	971,071	7%	14,672,925
Ecowater Business Assets	14,310	12%	117,000
City Services			
Consent Services	0	0%	33,079
Leisure Services	1,957,521	26%	7,600,000
Aftercare and Special Projects	21,969	3%	683,793
Roading Renewals	7,483	0%	5,354,440
Roading Capital Works	372,540	3%	12,604,591
Parks and Green Assets Renewals	39,154	3%	1,300,983
Parks and Green Assets Capital Works	115,881	3%	4,155,200
Total Capital Expenditure	6,918,544	7%	103,994,077

APPROVED/PROPOSED CAPITAL EXPENDITURE FORECASTS & ADJUSTMENTS

	Budget	Forecast	Variance	Comments
Property - Glen Eden CABx	146,000	0	-146,000	Deferred indefinitely
Housing for Older Adults	0	366,000	366,000	Self Funding Account - Extra funding for renewals targeted at level of depreciation and long term program to revitalise stock.
Aquatic Centre				
- Space Frames	1,204,164	1,618,164	414,000	Extra funding approved (m3037/2002)
- Centre - Redevelopment	4,510,500	5,015,135	504,635	Extra funding approved (m3034/2002)
Road Renewal Program		645,000	645,000	Extra funding approved (m2896/2002 & 3041/2002)
Hobsonville Roading Project	8,278,825	5,278,825	-3,000,000	Budget/Carry forward overlap (m3041/2002)
Massey Community House				
- Massey Leisure Centre		-20,000	-20,000) Funding approved for alterations to the Massey
- C/fwd relocation budget	5,000	0	-5,000) Community House (former Library)
- Proposed Alterations	0	44,726	44,726) ref. m3042/2002
Libraries - Smarter Systems Project			TBA	This is a joint TLA project overseen by the CEO Forum and the Regional Shared Services group. The project will replace the Libraries Hardware & Software in conjunction with 4 other TLAs within the Auckland region.
Property Purchases				
- Property Acquisitions	23,843,750	19,993,750	-3,850,000	Transfer to Henderson Valley Rd project. (see next item)
- 40 Henderson Valley Road	0	3,850,000	3,850,000	Purchase of property as per Special Council 23 September 2002 (see previous item)
TOTAL			-1,196,639	

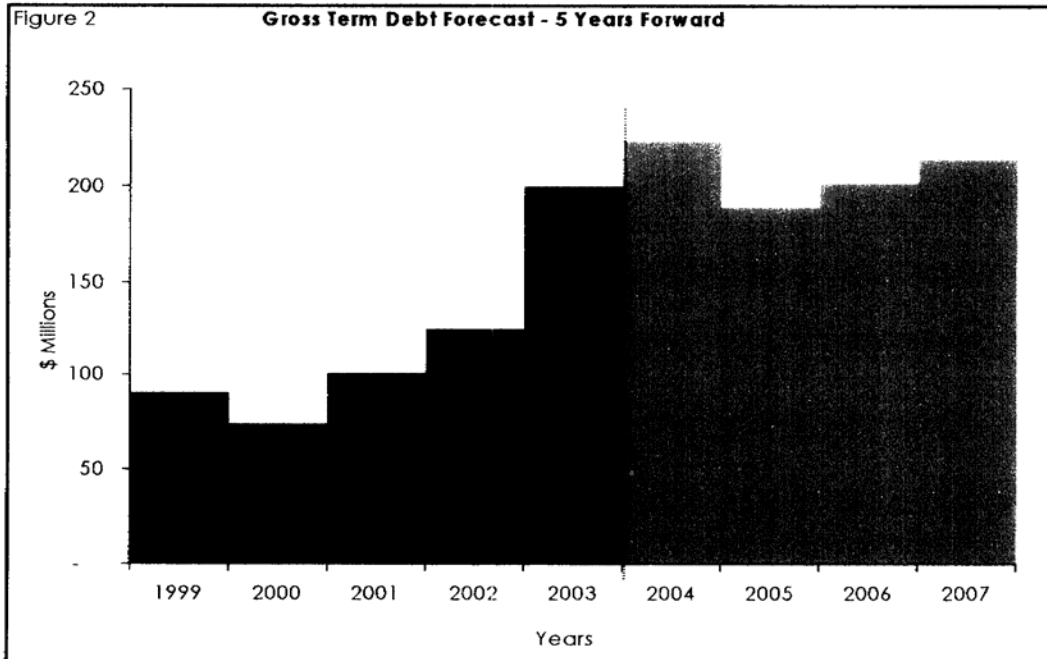
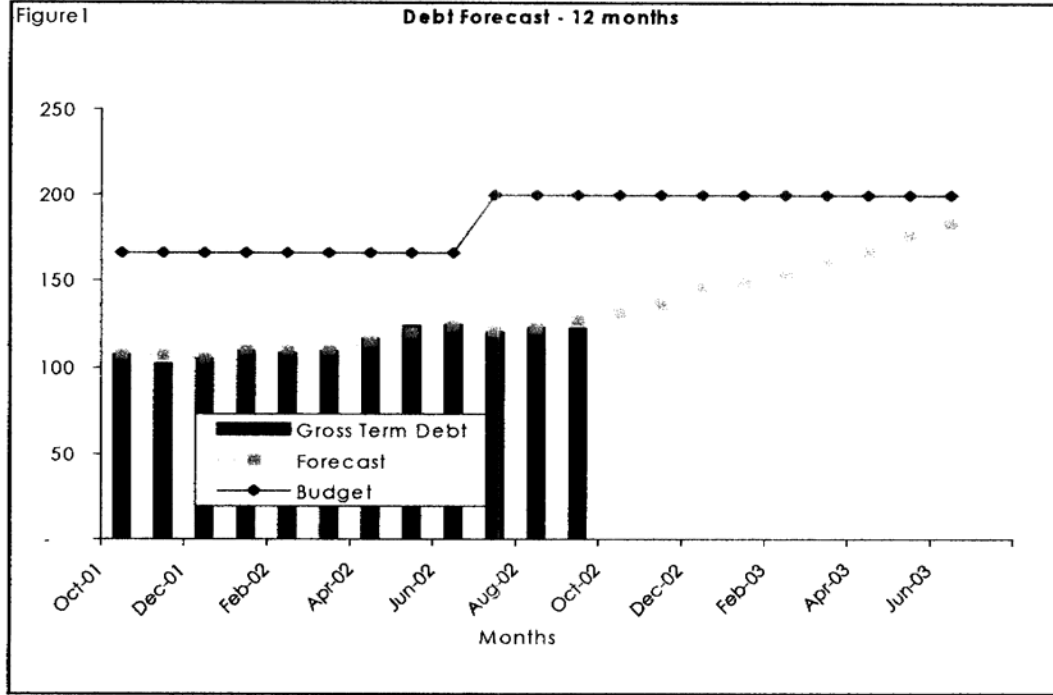
1ST QUARTER REVIEW - PROJECTED CARRY FORWARDS TO 2003/2004

Project	Budget	Forecast	Projected Carry F/wd	Completion Date	Comments
Miscellaneous Library Refurbishment	280,000	130,000	150,000	2004/05	Budget for RFID - Project deferred until 2004/5. Because of this some expenditure will be necessary to remodel Massey workroom - budget for this work will be established by Nov 2002, notional sum of \$150,000 estimated at this time
Automated Library Project	520,814	105,614	415,200	2004/5	Budget for RFID - Project deferred until 2004/5.
Patron Self-Return System	110,200		110,200	2004/5	Budget for RFID - Project deferred until 2004/5. However \$104,000 required to replace Patron Self Check in Massey and Glen Eden
New Lynn Library	3,491,114	60,000	3,431,114		Council is currently relooking at sites for the Library, pushing the project out considerably.
New Lynn Library	230,000	0	230,000	Not Known	Will be carried forward until construction is complete
Glen Eden Library Construction	1,500,000	458,400	1,041,600	Oct-04	Construction will be commencing Oct 03, Project in design phase currently
Glen Eden Library Fitout and Interior Construction	750,000	0	750,000	Oct-04	Fitout projected to commence mid 04, project in design phase currently
Glen Eden Library Fitout	195,000	0	195,000	Not Known	Will be carried forward until construction is complete
Westgate Park & Ride Land Purchase	460,000	100,000	360,000		Land purchase delayed - \$100K transferred to Ranui Project - refer Council meeting 30/10/02
Stormwater Loan programme 2002/03 - SH 16 & 18	1,000,000	700,000	300,000	2003/04	Adjust SH 16 & 18 stormwater funding to be carried over to 2003/04. Approved FOP 3043/2002 10 Oct 2002.
TOTAL			\$6,983,114		

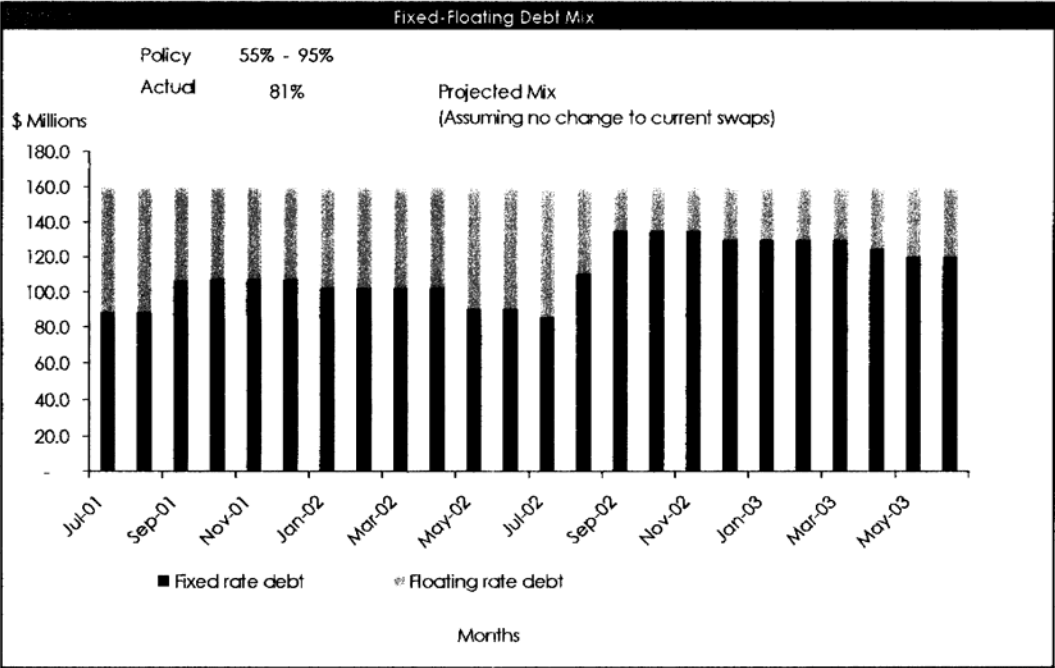
**WAITAKERE CITY COUNCIL DEBT PORTFOLIO AT
30 September 2002**

		September 02	August 02
TERM DEBT (to long term assets)			
<i>Budget year end term debt position per 2002/2003 Annual Plan</i>	Budget term debt	199,824	
	Further term debt approved by Council during 2001/2002	-	
	Budget 2002/2003 year end gross term debt	199,824	
	Forecast year end Sinking Fund Commissioner assets	5,448	
	Anticipated 2002/2003 Year End Net Term Debt	194,376	
TERM DEBT			
<i>Term debt position at 30 September 2002</i>	Term debt borrowed externally	122,599	113,503
	Special funds (used to reduce Council's external borrowing)	-	9,672
	Gross term debt	122,599	123,175
	Total Sinking Fund Commissioner assets	5,613	5,586
	Net term debt	116,986	117,589
<i>Term debt - source of funds at 30 September 2002</i>	Debenture stock - fixed rate (security: Debenture Trust Deed)	62,796	67,796
	Debenture stock - floating rate (security: Debenture Trust Deed)	40,025	35,025
	Secured bank loans (security: Debenture Trust Deed)	7,500	7,500
	Unsecured bank loans	11,903	2,800
	Finance Leases (security: associated asset)	376	382
	External borrowing	122,599	113,503
	Special funds (used to reduce Council's external borrowing)	-	9,672
	Gross term debt requirement	122,599	123,175
<i>Working capital borrowing at 30 September 2002</i>	Unsecured bank loans / (investments)	1,297	0
	Special funds (used to reduce Council's external borrowing)	11,634	2,059
	Council working capital borrowing requirement	12,931	2,059
<i>Cash investments held in trust 30 September 2002</i>	Debt repayment fund	-	-
	ARST fund (excluding fund allocations)	1,103	1,098
	Total cash investments	1,103	1,098
	Invested for 90 days - Current investment interest rate	5.86%	5.93%
	Gross Weighted Average Interest Rate	7.58%	7.50%

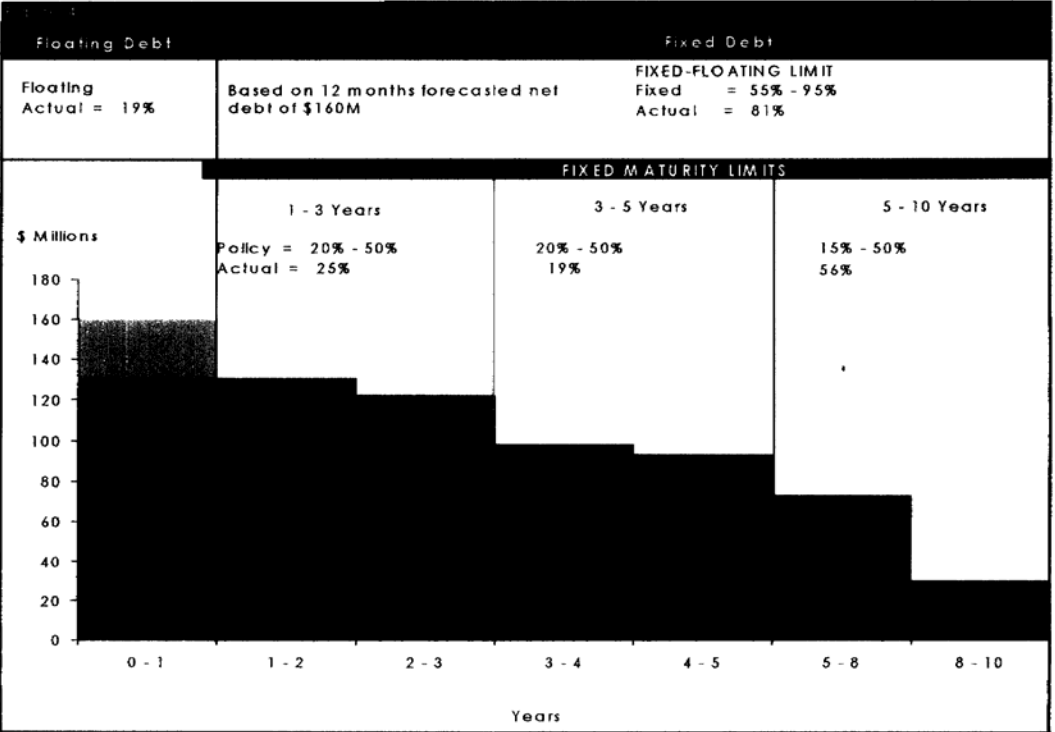
Debt Forecast

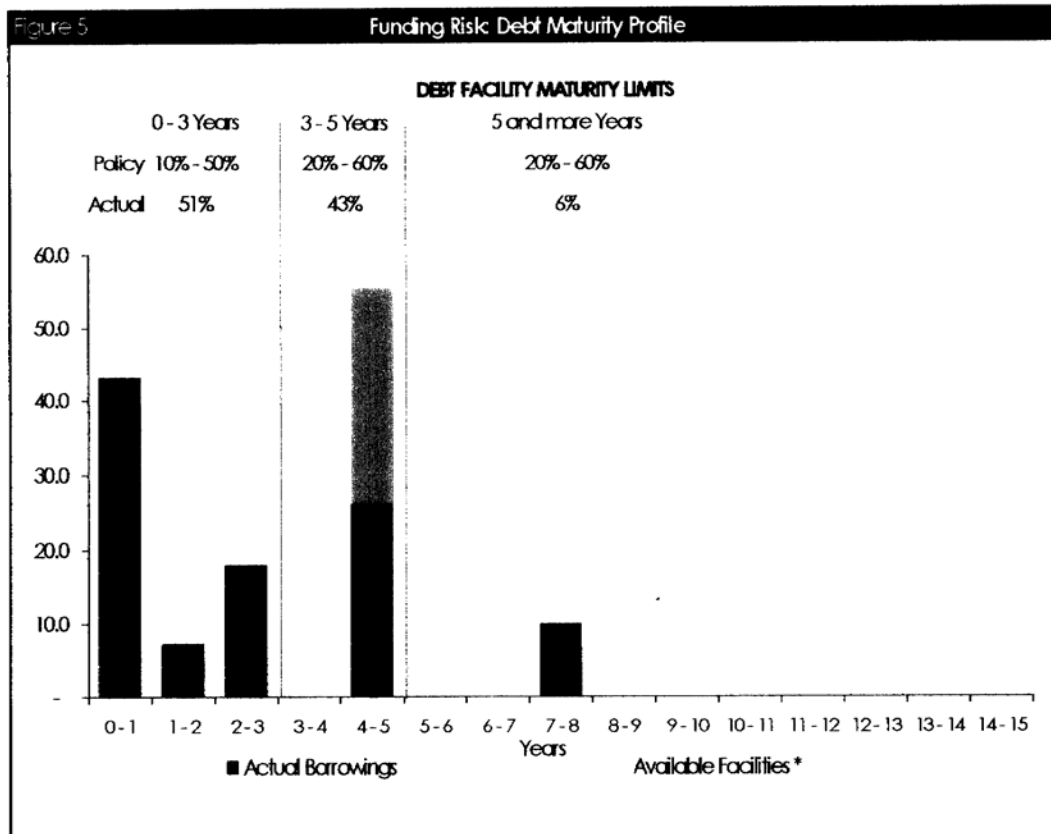


Fixed-Floating Debt Mix



Net Interest Rate Repricing Risk Profile





* Note: (1) Available facilities net of 29.3m uncommitted borrowings
 (1) Council is in the unique position of having a \$50 million committed funding facility at zero cost for the non utilised portion of the facility. The nature of this facility may, depending on the utilisation, result in a breach of the funding maturity limits. As this facility is very much in Council's favour this is an acceptable breach of policy.

Council Approved Debt Sources	Total		
	Committed Funding Sources	Usage	Available
Bank Loans			
Short Term (uncommitted)	\$0.0	\$13.2	\$0.0
Long Term (committed)	\$50.0	\$7.5	\$29.3
Commercial Paper			
Bank Overdraft	\$1.0	\$0.0	\$1.0
Senior Bonds			
Retail	\$19.7	\$19.7	\$0.0
Wholesale	\$83.2	\$83.2	\$0.0
Other	\$0.0	\$0.4	\$0.0
TOTAL	\$153.8	\$123.9	\$30.3

Notes:

Working capital borrowing is necessary due to fluctuations in the timing of operating revenue and expenditure. The working capital borrowing requirement also includes internal deficits relating to prior years. External working capital borrowing is reduced by the use of internal special funds with any surplus requirement funded by way of unsecured bank loans.

Gross Term debt is the borrowing relating to long term loan funded capital works projects. External borrowing to fund term debt is reduced by the use of internal special funds with the surplus requirement funded by way of secured or unsecured short term bank loans, fixed or floating medium or long term bonds and finance leases.

The managed debt portfolio refers to the portion of Council's total debt portfolio that is managed to reduce interest rate risk, liquidity/funding risk, counterparty risk and operational and legal risk as defined in the Borrowing and Investment Policy. The portfolio is managed on the external net term debt requirement excluding finance leases. i.e. it is net of the special funds that have been used to reduce the external term debt requirement and the sinking fund balance. Working capital is not included in the managed debt portfolio.

Special Funds are cash funds either collected through rates or vested to Council that have been 'set aside' for specific future spending. The funds are used in the interim to reduce Council's requirement to borrow externally. The fund is managed via accounting entries and a monthly interest allocation is made to the funds based on the Council's weighted average cost of borrowing for that period.

Description of Graphs:**Figure 1**

Gross term debt (blue) is the actual gross term debt position of Council as defined in the notes above. The *Forecast* (orange) is the projected gross term debt level per month in the current financial year, the figures are obtained from capital works timing forecasts (provided by budget managers on a monthly basis) and the current debt maturity profile. The *Budget* (green) line represents the gross public debt as approved in the 2002/2003 Annual Plan.

Figure 2

The prior year gross term debt figures (blue section) are obtained directly from the 'Term Liabilities' disclosure in published Annual Reports. The orange section is the projected gross term debt as forecast in the Annual and Strategic Plan 2000/2001 - 2009/2010.

Figure 3

The fixed (blue) and floating (orange) interest rate mix, both historic and projected, based on the 12 month rolling forecast net debt requirement. The Borrowing and Investment Policy minimum is 55% fixed and maximum 95% fixed. The positioning of the portfolio between policy minimum and policy maximum is dependent on the current and forecast financial market outlook.

Figure 4

Interest rate risk profile. Figure 4 shows, given the current fixed/floating rate mix and the debt forecast (assuming no changes to current swaps), the percentage of current fixed rate debt that will mature in future years. This enables Council to recognise and reduce significant concentrations of interest rate risk that may arise in future years. As debt forecasts change the amount of fixed cover in place may have to be adjusted to comply with the policy limits.

Figure 5

Funding and liquidity risk. Figure 5 varies from figure 4 in that it shows the actual maturity profile of current debt on issue as opposed to the profile of Council's exposure to interest rate risk arising when debt either reprices (in the case of floating rate debt or hedges) or matures. The debt maturity profile enables Council to identify significant concentrations of maturing debt and debt facilities. Where there are significant concentrations of debt maturing Council is at risk of not being able to re-borrow from the market at favourable rates.

Figure 6

In order to ensure Council has the ability to borrow from the market when funding is required committed funding facilities are arranged with approved debt sources. Figure 6 shows Council's committed funding sources and the current usage of these funds. In addition to the committed sources Council also uses uncommitted lines of funding as seen in short term bank loans and bonds, uncommitted funding is at times less expensive than committed funding however its availability is not guaranteed.

Wholesale Market Interest Rates and the Trade Weighted Index

