

## 14. TREASURY MANAGEMENT REPORT FOR QUARTER ENDED 30 JUNE 2004

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The purpose of this report is to advise the quarterly position relating to Council borrowing and investments and results for the 2003-04 year.

### BACKGROUND

The Local Government Act 2002 requires publication of a Liability Management Policy and an Investment Policy. These were updated and have been included as part of the Long Term Council Community Plan adopted in June 2004.

The Council's policies establish quarterly reporting requirements to the Strategy and Finance Committee.

### TREASURY REVIEW TEAM

To provide ongoing review, the Treasury Review Team which is chaired by the Director of Strategic Investment, meets on a regular basis. Bancorp Treasury Services Ltd (BTSL) has been appointed as independent treasury advisers in terms of the policies and is represented on the team.

### CAPITAL ENDOWMENT FUND

The Director of Strategic Investment is obtaining advice from external consultants on the strategy and investment of the Council's Capital Endowment Fund (CEF) which currently stands at \$80.5M. In the meantime the fund has been fully invested with a range of banks, earning income to meet the requirements for project funding and to provide for inflation protection. Interest rate earnings for the year were better than budgeted and the income account has been sufficient to meet outgoings and inflation protection of capital. Interest rates are expected to rise over 2004-05.

A Capital Endowment Fund No 2 of \$5.0M has been established this financial year from unbudgeted dividends from Council Controlled Trading Organisations (CCTOs). The purpose of the CEF No 2 is to invest in venture capital projects that may include Canterbury region ventures. A commitment has been made to invest this fund fully in a joint venture fund with Endeavour i-cap Ltd and others. A total of \$8.0M has been invested by local entities and this has attracted additional Government VIF fund contributions of \$3.0M to the joint venture fund. At 30 June 2004 \$471,335 had been called by the fund managers for venture capital investments. Further calls since have taken the investment total to \$762,921.

### LIABILITY MANAGEMENT REPORT

#### General Overview

The Council is not expected to borrow for its ordinary capital works expenditure until 2005/06. Capital expenditure is being met from the Council's Debt Repayment Reserve (DRR) in the meantime. However, some external borrowing during this period will be necessary to continue to fund the Council's investment in its CCTOs. The DRR together with accumulated balances in sinking funds and the Loan Repayment Reserve (LRR) will provide sufficient funds to repay maturing Council works loans until 2005/06.

The borrowing policy approves short term borrowing by bank overdraft up to a limit of \$2.0M. This was not exercised during the quarter under review.

The Council currently borrows from Christchurch City Holdings Ltd (CCHL) under a formal loan agreement. The loan facility has sufficient capacity to meet the Council's anticipated medium term borrowing needs. CCHL charges the Council a margin over its external borrowing costs to use the facility.

#### Interest Rate View

Based on the present market conditions and the Council's current Standard and Poor's long-term credit rating of AA+, the Council could expect to pay the following margins for any borrowing.

<b>Term</b>	<b>Current Margin</b>	<b>Current Base Rate</b>
Overdraft	Pre arranged rate	9.85% (actual)
30 to 90 days	Bank bill rate plus -1 to +1 points	6.33%-6.50%
1-2 years	+2 to +5 points over swap rates	6.61%-6.70%
3-6 years	+6 to +14 points over swap rates	6.66%-6.85%
Over 6 years	+15 to +20 points over swap rates	6.80%-7.00%

### **Liability Management and Loan Servicing Costs**

Refer to Schedule 1 attached.

### **INVESTMENTS REPORT**

#### **General Overview**

All cash investments are made within the terms of the Investment Policy and the management procedures that have been adopted by the Treasury Review Team.

Over 2003/04 interest rates generally trended upwards in line with the Reserve Bank's publicly expressed concerns over inflationary pressures within the New Zealand economy. Inflationary pressure had been moderated during the latter half of 2003 and the first quarter of this year by a higher NZ dollar exchange rate which still remains firm. Between January and July 2004 the Official Cash Rate (OCR) was increased four times. The current rate is 6.00%, from 5.00% at the beginning of the year. The financial market has accepted the probability of a further increase in September of 0.25% and the possibility of a further 0.25% by the end of the year depending on the Reserve Bank's outlook. This would take the OCR to 6.5% which is expected to be the peak in the current cycle. Investments have been made for terms that take cognisance of the outlook for higher market rates and to meet the Council's short-term and medium term funding requirements. This strategy has BTSL's support.

The OCR is the principal driver for short to medium term interest rates up to two years. Long-term rates are more influenced by overseas bond movements. Long-term bond yields overseas remain under pressure as investors continue to take a cautious approach to the expected economic recovery in the US. An economic recovery is underway in the USA albeit a modest one and the Federal Reserve has signalled intention to raise official US interest rates at a measured pace.

#### **Interest Rate View**

The Council could expect to receive the following margins for bank deposits, commercial paper and corporate bond investments complying with policy.

<b>Term</b>	<b>Current Margin</b>	<b>Current Base Rate</b>
Official Cash Rate		6.00% (actual)
30 to 90 days bank bills	+20 to +30 points over OCR	6.20%-6.30%
A-1+ commercial paper	-3 to +1 points over bank bills mid rate	6.42%-6.46%
A-1 commercial paper	+1 to +2 points over bank bills mid rate	6.46%-6.47%
A-2 commercial paper	+3 to +8 points over bank bills mid rate	6.48%-6.53%
Corporate bonds 1-3 years	+3 to +9 points over swap rates	6.61%-6.70%
Corporate bonds 4-7 years	+10 to +21 points over swap rates	6.70%-6.85%

### **Investments Management and Income**

Refer to Schedule 2 attached.

#### **Chair's**

**Recommendation:** That the information be received.