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Corporate Plan Output: Borrowing Management Policy and Investment Policy Volume I Pages 22-26	

The purpose of this report is to provide accountability for management of the debt and investment portfolios within the terms of the Council's Borrowing Management Policy and Investment Policy.

#### **REQUIREMENT TO REPORT**

In 1998 the Council adopted Borrowing and Investment policies which came into effect on 1 July 1998. This is in compliance with the requirements of the Local Government Amendment Act 1999 (No 3). The adopted policies incorporate the Financial Management Policy of the Council and set out management procedures and policies to be applied in respect of loan borrowing to fund capital expenditure and investing Council funds.

#### **Treasury Review Team**

The Treasury Review Team continues to meet on a regular basis chaired by the Director of Finance, Bob Lineham. Other members are Geoff Barnes, Funds and Financial Policy Manager; Paul Melton, Financial Services Manager and Paul Baldwin, Funds Accountant. Also a member is Peter Cavanaugh of Bancorp New Zealand Ltd, merchant bankers, who have been appointed as independent treasury advisers in terms of the policies.

#### **INVESTMENTS**

##### **General Overview**

- All external investments are made within the terms of the Investment Policy.
- The procedures for management are in compliance with the Investment Policy.
- The income performance and investment details are disclosed later in the report.

##### **Investments Report – Particular Issues**

###### *Interest Rate View*

The Investment Policy requires the Funds Manager to form an interest rate view based on professional advice. Following consultation with Bancorp and discussion by the Treasury Review Team the most recent view formed for investment purposes is shown in the following table. The general view is that with probable tightening of money supply as the economy slowly recovers from recession and as signalled by the Reserve Bank, interest rates are expected to rise in the short to medium term. The yield curve is expected to flatten as short term interest rates rise ahead of longer term rates. The curve is expected to stay positive for the foreseeable future.

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

<b>Term</b>	<b>Margin</b>	<b>Current Base Rates</b>
90 days	20–30 points over OCR*	4.5%
1 – 3 years	60–75 points over Govt bonds	Say 5.2%-6.4%
4 – 7 years	75–100 points over Govt bonds	Say 6.6%-6.9%

\* OCR – Official Cash Rate, introduced on 17 March 1999 by the Reserve Bank, fixes the bank overnight cash rate. The ORC replaced the Monetary Conditions Index (MCI) the Bank previously used to indicate “desired conditions”. The OCR is reviewable six weekly and no changes have been made to date.

#### *Use of Special Funds*

During the year the Treasury Review Team approved the use of special funds to provide temporary funding for operations. The factors taken into account were:

- Timing of special dividends and capital repayment receipts that have not passed to the Council within the timeframe originally budgeted.
- Provision being made to credit the special funds so utilised with full interest earnings by the standard formula calculated from the weighted average of Council investments.
- That this was a temporary situation and the Council will be in the position of being a net investor while debt repayment reserve fund balances are available.

#### **Short Term Liquid Investments**

The Council requires a reasonable level of short-term funds for liquidity reasons. The levels held meet the operational needs without recourse to external borrowing on a day-by-day basis.

Since July 1998 investment interest rates have diminished dramatically and this has had a significant impact on Council income for the year.

Bancorp advises that the Council’s current position is reasonable in the prevailing economic and market conditions. The mix of short and medium term investments is regularly reviewed to achieve optimum returns.

#### **Long Term Investments in Authorised Stocks and Bonds**

As the interest rates on medium to long term investments have risen the Council has increased its holdings in stocks and bonds which meet the investment criteria. The strategy adopted has been to increase yield and maintain flexibility to take advantage of expected future yield increase and match long term funding requirements.

## **Specific Measurements**

- Short term and at call investments comprised 52% of the Council's investment portfolio at 30 June 1999.
  - The amount of investments was \$34,430,000
  - No exposure to any bank exceeds 20%.
  - Interest rates range between 4.5%-4.72% p.a.
- Long term investments comprised 29% of the Council's investment portfolio as at 30 June 1999.
  - The amount of these investments at 30 June was \$18,313,000.
  - The longest maturity date is 15 March 2002.
  - Coupon interest rates range between 5.32%-10.41% p.a.
  - \$5,000,000 in corporate bonds were purchased during the last quarter at market rates.
- Loans to individuals and community organisations comprise 5% of the Council's investment portfolio.
  - All loans subject to recovery action for default have been reported to the Council.
  - Loans to individuals and community organisations total \$3,449,284.
- Shares in listed public companies comprise 1% of the Council's investment portfolio. (These shares are a specific bequest to the Council).
  - The shares are valued annually by a sharebroker.
  - The value of shares at 30 June 1999 was \$564,801.
- During the year Council loans for housing amounting to \$7.5M came due for repayment. To save on external refinancing costs the net redemption amount required to repay the loans was made available by investment of Debt Repayment Reserve funds.
  - The amount of the internal funding investment is \$6,500,000.
  - Housing operations are required to provide a return on the funds utilised at the rate of 6.46% p.a. for three years.
  - The investment comprises 10% of the Council's investment portfolio.

The attached graphs shows the Council investments by type and fund as at 30 June 1999 and 26 August 1999.

## **FUNDING**

### **General Overview**

- No long term borrowing was undertaken during the year ended 30 June 1999.
- Four short term borrowing facilities were arranged with the Council's transactional bank during the financial year.
  - The borrowing was for the purpose of funding working capital and equity investment in Council LATEs.

- The total amount of borrowing was \$1,971,250 of which \$525,000 has been repaid leaving a current balance of \$1,446,250. The maximum borrowed at any one time has been \$1,446,250. The maximum term of any borrowing has been less than three months.
- The Council specifically approved the excess of \$446,250 over the \$1M maximum bank overdraft limit set out in the Borrowing Management Policy.
- No derivative or hedging contracts were entered into during the year.
- Repayment of net housing loan debt of \$6.5M has been financed from the Debt Repayment Reserve.
- Details of repayments during the 1998-99 year and maturity profile are disclosed later in the report.

## **Borrowing Management Report – Particular Issues**

### *Council Funding Requirements*

The Council is not expected to borrow for capital works expenditure for approximately two years. However some external borrowing may be required over this period specifically related to the Council's investment in Council owned LATEs.

Short-term borrowing for cash flow purposes may be required and would normally be by bank overdraft facility. The borrowing policy approves short term borrowing of this nature up to a limit of \$1,000,000.

The Council has authorised the Director of Finance and the Legal Services Manager to approve a borrowing arrangement whereby Christchurch City Holdings Ltd will be the future provider of external funds in the first instance. The details of a funding facility are in the process of being sorted out. There are currently some issues that require resolution to ensure consistency between the funding facility between CCC and CCHL and the requirements of CCHL's lenders. The prime security will be \$350 million of uncalled capital which is the full amount of CCHL's long term funding facility and which will have capacity to meet CCC borrowing over at least the next five years.

### *Interest Rate View*

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

<b>Term</b>	<b>Margin</b>	<b>Current Base Rates</b>
Overdraft	Pre arranged rate	7.8%
Up to 90 days	Bank bill rate plus 10–20 points	Say 4.85%-4.9%
1 – 2 years	60–75 points over Govt bonds	Say 5.2%-6.0%
3 – 6 years	75-95 points over Govt bonds	Say 6.4%-6.8%
Over 6 years	100 points over Govt bonds	Say 6.9%-7.0%

The Reserve Bank has signalled that it expects 90 days bank bill rates in the open market to be closely related to the market cash rate which itself will trade within a range of .25% either side of the Official Cash Rate (OCR). The Monetary Policy Statement by the Reserve Bank in August 1999 signalled that the OCR\* is likely to rise in the short to medium term. An increase in the OCR of up to .5% is expected towards the end of the year depending on the strength of the New Zealand economy and the currency.

\* Currently the OCR is set at 4.5% p.a. Movements will be at .25% or multiples of .25%.

### *Loan Redemptions 1998-99 and Maturity Profile*

The following three tables set out loan repayments made during 1998-99 by funding source.

#### **Funded from Rates**

<b>Maturity</b>	<b>Loan</b>	<b>Amount</b>
15-Aug-98	EECA (Energy Conservation)	19,500
1-Nov-98	Works Development Loan No1 1993	4,000,000
15-Nov-98	EECA (Energy Conservation)	37,583
15-Feb-99	EECA (Energy Conservation)	19,500
15-Mar-99	Works Development Loan No 1 1993	5,000,000
15-Mar-99	Works Development Loan No 1 1993	1,000,000
15-May-99	EECA (Energy Conservation)	37,582
	<b>TOTAL</b>	<b>\$10,114,165</b>

#### **Housing Loans**

<b>Maturity</b>	<b>Loan</b>	<b>Amount</b>
15-Nov-98	Renewal Loan 1993 – Elderly Persons Housing	600,000
15-Nov-98	Renewal Loan 1993 – Public Rental Housing	1,400,000
15-Dec-98	Renewal Loan 1993 – Elderly Persons Housing	2,900,000
15-Dec-98	Renewal Loan 1993 – Public Rental Housing	1,100,000
15-Mar-99	Renewal Loan 1993 – Elderly Persons Housing	500,000
15-Mar-99	Renewal Loan 1993 – Public Rental Housing	1,000,000
1998/99	Housing Table Loans	137,718
	<b>TOTAL</b>	<b>\$7,637,718</b>

## Fully Defeased Loans

<b>Maturity</b>	<b>Loan</b>	<b>Amount</b>
1-Jul-98	Various Loans	40,400
1-Aug-98	Various Loans	387,300
1-Nov-98	Various Loans	1,583,800
1-Feb-99	Various Loans	200,200
1-Mar-99	Various Loans	70,000
1-May-99	Various Loans	<u>1,800</u>
	<b>TOTAL</b>	<u><u>\$2,283,500</u></u>
<b>GROSS LOANS REPAID in 1998-99</b>		<u><u>\$20,035,383</u></u>

The maturity profile on the Council's debt portfolio (as at 30 June 1999) is set out in the following table:

<b>Year</b>	<b>Rate Funded</b>	<b>Separately Funded</b>	<b>Defeased Loans</b>	<b>TOTAL</b>
1999-00	33,022,750	4,085,790	261,800	37,370,340
2000-01	19,675,171	1,037,432	37,400	20,750,003
2001-02	7,266,664	140,068	249,500	7,656,232
2002-03	10,000,000	141,077	82,322	10,223,399
2003-04	3,000,000	134,822	39,000	3,173,822
2004-05	0	300,664	75,000	375,664
2005-06	0	114,769	21,820	136,589
2006-07	20,000,000	87,760	0	20,087,760
Later	<u>0</u>	<u>269,071</u>	<u>0</u>	<u>269,071</u>
<b>TOTALS</b>	<u><u>\$92,964,585</u></u>	<u><u>\$6,311,453</u></u>	<u><u>\$766,842</u></u>	<u><u>\$100,042,880</u></u>

The above table represents gross debt. To offset this amount the Council holds sinking funds of \$6,566,607 and a debt repayment reserve of \$6,500,000.

The debt repayment reserve is budgeted to increase by \$132,000,000 following receipt of capital repayments via CCHL late this calendar year. Net debt also takes account of cash investments. A summary of the overall net debt position as at 30 June 1999 is:

Gross Debt 30 June 1999	\$100,042,880
less Sinking funds	(\$6,566,607)
less Debt Repayment Reserve	(\$6,500,000)
Term Debt	\$86,976,273
less Reserve Funds	(\$24,378,781)
Net Debt Pre Capital Repatriation	\$62,597,492
less Budgeted Capital Repatriation to come	(\$184,500,000)
Projected Net Debt (Post Capital Repatriation)	<u>(\$121,902,508)</u>

## Chairman's

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