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# Our 10-Year Plan

*Wellington City Council, Draft Investment and Liability Management Policy*

# Investment and Liability Management Policies

## GENERAL POLICY OBJECTIVES

The Council's general policy objectives relating to its investment and liability management are to:

- Minimise the Council's overall costs and risks associated with its borrowing activities and the general management of its other liabilities.
- Manage its borrowings and cash assets on a "net debt" basis in order to reduce the overall net cost to the Council.
- Optimise the return on its investment portfolio and other financial assets.
- Manage the Council's exposure to adverse interest rate movements.
- Borrow and invest funds and transact risk management instruments within an environment of control and compliance.
- Regularly review and consider the performance of the Council's financial assets and investments. Where appropriate, the Council will dispose of under performing assets or those assets and investments that are not essential to the delivery of services and activities set out in the Council's Long Term Plan (LTP).

More detail on the Council's investment and borrowing policies, operating procedures and associated internal controls is contained in the Treasury Management Policy.

## INVESTMENT POLICY

### Policy Statement

The Council operates on a "net debt" basis, and does not separately maintain significant long term cash investments. The general policy with respect to surplus short term cash is to invest any short term surplus cash or to utilise it to reduce borrowings.

The Council currently maintains an equity interest in Wellington International Airport Limited (WIAL) and an ownership and financial interest in ground leases and investment properties. The Council will continue to review the level of investment as well as the return it receives on these investments.

Where appropriate, the Council may choose to dispose of investments/financial assets that no longer meet our investment objectives.

## **Investment Mix and Associated Objectives**

The Council categorises its investments into 5 broad categories:

### ***Cash and Cash Equivalents***

The Council may invest funds with approved registered banking institutions. These investments generally mature in less than one year, and are held primarily for working capital/liquidity purposes or the pre-funding of debt maturing within twelve months.

### ***Income generating commercial debt instruments***

These are principally loans to other organisations (on commercial terms) which deliver a cash-flow return to the Council.

### ***Income generating commercial equity investments***

Equity investments arise from the Council owning or controlling an equity holding (e.g. shares) in another entity.

The Council currently maintains a 34 percent shareholding in Wellington International Airport Limited (WIAL).

### ***Income generating commercial property investments***

Investment properties are the Council's ground leases and land and buildings held primarily for investment purposes. The Council periodically reviews its continued ownership of investment properties by assessing the benefits of continued ownership in comparison to other arrangements that could deliver similar benefits. Any assessment is based on both the strategic benefit of the investment/ownership to the City and in terms of the most financially viable method of achieving the delivery of Council services.

### ***Non income generating investments***

This includes loans to other organisations, and equity investments in Council Controlled Organisations. The Council may consider the provision of loans to Community groups but only in exceptional circumstances. The Council's non income generating investments are held for strategic or ownership reasons.

In addition to the above investment categories, the Council may assume financial risk associated with providing contributions, guarantees and underwrites, where these meet the Council's strategic objectives and outcomes. Such undertakings require a Council resolution.

## **New Zealand Local Government Funding Agency Limited**

Despite anything earlier in this policy, the Council may invest in shares and other financial instruments (including borrower notes) of the New Zealand

Local Government Funding Agency Limited (LGFA) and may borrow to fund that investment.

The Council's objective in making any such investment is to:

- a. obtain a return on the investment; and
- b. ensure that the LGFA has sufficient capital to remain viable, meaning that it continues as a source of debt funding for the Council.

Because of this dual objective, the Council has invested in LGFA shares in circumstances in which the return on that investment is potentially lower than the return it could achieve with alternative investments. If required in connection with the investment, the Council may also subscribe for uncalled capital in the LGFA and be a Guarantor.

### **Investment Acquisition/Addition/Disposal**

With the exception of the day to day investment of short term cash and cash equivalents, all new investments, additions to existing investments, and/or disposals of existing investments must be approved by the Council. The day to day management and investment of short term cash and cash equivalents may be made by Council officers in accordance with the Treasury Management Policy.

The Council will continue to maintain its current level of investment in WIAL (being a 34 percent equity interest) until it considers that it is strategically, financially and economically prudent to dispose of the investment.

Proceeds from the sale of investments will be used to repay existing borrowings, unless the Council specifically directs that the funds be put to another use.

### **Reporting**

#### ***Investments in CCOs***

Monitoring of the Council's equity investment and ownership interest in Council Controlled Organisations (CCOs) is undertaken by the Council Controlled Organisations Subcommittee. The Subcommittee reports to the City Strategy Committee and is responsible for:

- communicating the Council's priorities and strategic outcomes to Council Controlled Organisations (CCOs)
- ensuring delivery through the development of Statements of Intent and integration of CCO outcomes with the Council's Long-term Plan and Annual Plan funding processes and decisions, and
- monitoring the financial performance and delivery on strategic outcomes of the Council's CCOs.

### ***All other investments***

The City Strategy Committee is responsible for monitoring all other investments and providing recommendations to the Council in regard to strategies, policy and guidelines in relation to those investments. The City Strategy Committee will receive and review the quarterly Treasury report contained within the consolidated quarterly report.

### **Risk Management**

The Council's principal exposure on its financial investments is credit risk. Credit risk is minimised by the Council investing in approved institutions with satisfactory credit ratings which are assessed and reviewed by independent credit rating organisations. Limits are spread amongst a number of counterparties to avoid concentrations of credit exposure.

Assessment and management of specific risks associated with the Council's investment in WIAL, LGFA and investment properties will be performed on a regular basis. Any significant changes in the risk profile for these investments will be reported to the City Strategy Committee.

### **Investment Ratios**

For the purposes of setting its Borrowing and Investment Ratios, the Council defines investments as assets which are cash or readily convertible to cash (either through fixed repayment and maturity profiles, or through sale or exchange) and assets which are held primarily for investment purposes (either for capital growth, commercial rental or interest). This is likely to include:

- Cash and cash equivalents (e.g. term deposits),
- Income generating commercial debt instruments
- Income generating commercial equity instruments
- Income generating commercial property instruments

## **LIABILITY MANAGEMENT POLICY**

In broad terms, the Council manages both current and term liabilities.

### **CURRENT LIABILITIES**

Current liabilities reflect those obligations, expressed in monetary terms, which the Council has to meet within relatively short timeframes, at a maximum within the next 12 months. In respect of its day to day obligations for both operational and capital expenditure, the Council's policy is to pay these liabilities in full by the due date. This eliminates any credit exposure or risk. Current liabilities also include the maturing portions of any term liabilities that are due for repayment within the following 12 months.

### **TERM LIABILITIES**

Term liabilities represent the Council's obligations which, in general terms, are not immediately payable, i.e. not due within the following 12 months. Borrowings comprise the majority of the Council's term liabilities.

The Council approves the borrowing programme for each financial year as part of the LTP or Annual Plan. Additional borrowings may be approved by Council on a case by case basis. The Council primarily borrows to fund its new and upgraded capital expenditure programme. In approving new borrowings the Council considers the impact of the proposed level of borrowings on its overall borrowing limits and impact on rates and rates limits.

### **POLICY OBJECTIVES**

The Council primarily borrows to pay for the upgrading of existing assets and the construction/purchase of new assets. These assets generally provide new or enhanced benefits to Wellington for many years. Borrowing is therefore considered the most cost-effective and equitable way to fund these assets as it spreads the cost of the asset over the future generations of ratepayers who will benefit from the use of the asset. In addition, Council borrows to meet the costs associated with settling liabilities arising with respect to weathertight homes issues, and the borrowings are repaid from future rates revenues. Accordingly, borrowings have a strategic benefit of making the cost of the asset investment or weathertight homes liabilities affordable to today's ratepayers. Borrowings are maintained at a prudent level, in accordance with the Council's overall financial strategy and specific borrowing limits.

### **POWER TO BORROW**

The Council borrows as it considers appropriate and in accordance with the provisions of the Local Government Act 2002 and its Treasury Management Policy. The Council approves the level of new borrowing in general terms as part of the LTP or Annual Plan. The Council delegates the authority to officers to raise the approved borrowing during the financial year as and when the funding is required. Any additional borrowing beyond that approved in the LTP or Annual Plan must be approved by the Council.

## **INTEREST RATE RISK MANAGEMENT LIMITS**

Borrowings issued at variable (floating) interest rates expose the Council to a cash flow interest-rate risk. The Council manages its cash flow interest-rate risk by using floating to fixed interest rate swaps. Such interest rate swaps have the economic effect of converting borrowings from floating rates to fixed rates.

Council debt/borrowings must be within the following fixed/floating interest rate risk control limits:

Debt Interest Rate Policy Parameters (calculated on rolling monthly basis)		
Debt Period Ending	Minimum Fixed Rate	Maximum Fixed Rate
Year 1	50%	80%
Year 2	45%	80%
Year 3	40%	80%
Year 4	35%	75%
Year 5	30%	70%
Year 6	20%	65%
Year 7	10%	60%
Year 8	0%	55%
Year 9	0%	50%
Year 10	0%	45%
Year 11	0%	40%
Year 12	0%	35%
Year 13	0%	30%
Year 14	0%	30%
Year 15	0%	30%
Year 16	0%	30%

“Fixed Rate” is defined as an interest rate repricing date beyond 3 months forward on a continuous rolling basis.

The “Fixed Rate” percentage is based on the projected gross debt level on a rolling forward basis. Gross debt is the amount of total borrowing. This allows for pre-hedging in advance of projected physical drawdowns of new debt. When forecasts are changed, the amount of fixed rate cover in place may have to be adjusted to comply with the policy minimums and maximums. In the event of one-off significant changes caused by asset sales/purchases or capital expenditure in advance of the forecast, then a 3 month period of adjustment is permitted.

## **LIQUIDITY**

The Council minimises its liquidity risk by avoiding concentration of debt maturity dates and by maintaining committed borrowing facilities at a level that exceeds 115% of the existing external net debt level. The Council will only drawdown or borrow against these facilities as required.

Where special funds are maintained to repay borrowings, these investments are held for maturities not exceeding borrowing repayment dates.

The Council avoids exposure to liquidity risk by managing the maturity of its borrowing programme within the following maturity limits:

### **BORROWING MATURITY PROFILE LIMITS**

Period	Minimum	Maximum
0 to 3 years	15%	60%
3 to 5 years	15%	60%
5 years plus	15%	60%

### **CREDIT EXPOSURE**

The Council borrows from approved institutions with satisfactory credit ratings. Borrowings are managed to ensure the Council is not exposed to material concentrations of credit risk. Limits are spread amongst a number of counterparties to avoid concentrations of credit exposure.

### **LOCAL GOVERNMENT FUNDING AGENCY**

Despite anything earlier in this Policy, the Council may borrow from the New Zealand Local Government Funding Agency Limited (LGFA) and, in connection with that borrowing, will enter into the following related transactions to the extent it considers necessary or desirable:

- a. contribute a portion of its borrowing back to the LGFA as an equity contribution to the LGFA (for example borrower notes that may convert into redeemable preference shares).
- b. provide guarantees of the indebtedness of other local authorities to the LGFA and of the indebtedness of the LGFA itself
- c. commit to contributing additional equity (or subordinated debt) to the LGFA if required
- d. secure its borrowing from the LGFA, and the performance of other obligations to the LGFA or its creditors with a charge over the Council's rates and rates revenue.
- e. Subscribe for shares and uncalled capital in the LGFA

### **BORROWING REPAYMENT**

The Council will repay borrowings from a combination of excess depreciation over and above renewals, sale of surplus or underperforming assets, operating surpluses, and any rates specifically set to repay borrowings, including those associated with settling weathertight homes liabilities, or from the renewal of borrowings.

### **SPECIFIC BORROWING LIMITS**

In determining a prudent level of borrowings the Council assesses the level of net borrowing against the Council's operating income.

Total Council Net Borrowings will be managed within the following macro limits:



<b>RATIO</b>	<b>LIMIT</b>
Net borrowing as a percentage of income	<175%
Net Interest as a percentage of income	<15%
Net Interest as a percentage of annual rates income	<20%
Liquidity (Term borrowing + committed loan facilities to existing external net debt)	>115%

### **SECURITY**

Council borrowings are secured by way of a Debenture Trust Deed (representing a charge over Council rates revenue). This security relates to any borrowing and to the performance of any obligation under any incidental arrangement. However, if it is considered advantageous, the Council's borrowings and other financial arrangements may be undertaken on an unsecured basis, or secured by way of a charge over its physical assets.

### **CREDIT RATING**

To provide an independent assessment of the Councils' credit quality, Council maintains a credit rating with an independent rating agency.

### **CARBON PRICE RISK**

Council maintains a stock of NZU credits and is projected to remain a net holder of carbon credits for the foreseeable future. Within this context, Council manages its annual carbon liabilities through surrendering existing holdings and purchasing NZUs in the spot/forward market, where required. The Treasury Management Committee is responsible for carbon strategies/decisions and the CFO has responsibility for implementing the strategies.

