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INVESTMENT AND LIABILITY MANAGEMENT POLICY

Purpose and Scope

1. To comply with the Local Government Act 2002 in terms of a legislative requirement to adopt an investment policy and a liability management policy.

   To provide the framework under which council operates investment and borrowing activities.

   This policy supports council's financial strategy and Revenue and Financing Policy and is linked to the Treasury Management Policy which provides more detail for the day-to-day management of the treasury function.

2. The Council is responsible for:
   a. Approving the financial strategy in the 10-Year Plan and Annual Plans
   b. Approving new debt in the 10-year Plan, Annual Plans and specific council resolutions
   c. Ensuring that a Treasury Management Policy is adopted as a management policy
   d. Approval for one-off transactions falling outside Policy
   e. Approve the appointment of the Trustee to the Debenture Trust Deed

INVESTMENT POLICY

Principles

3. The Council will, when investing, ensure the protection of its investment capital and that a prudent approach to risk/return is always applied within the confines of this policy. Only approved creditworthy counterparties are acceptable.
   The Council will act effectively and appropriately to:

   a. Protect the Council's investments.
   b. Ensure the investments benefit the Council's ratepayers.
   c. Maintain a prudent level of liquidity and flexibility to meet both planned and unforeseen cash requirements.

Policy

4. The Council's general policy on investments is that:
   a. The Council may hold financial, property, forestry, and equity investments if there are strategic, commercial, economic, or other valid reasons (e.g. where it is the most appropriate way to administer a Council function).
   b. The Council will keep under review its approach to all major investments and the credit rating of approved financial institutions.
   c. The Council will review its policies on holding investments at least once every three years.

Acquisition and Disposal of Investments

5. With the exception of financial investments, new investments are acquired if an opportunity arises and approval is given by the Council.
6. Before approving any new investments, Council gives due consideration to the contribution the investment will make in fulfilling Council's strategic objectives, and the financial risks of owning the investment.
7. The authority to acquire financial investments is delegated to the General Manager Corporate (GMC).
8. Proceeds from the sale of assets or investments will in the first instance be used to repay outstanding borrowings unless otherwise specifically authorised by Council. The exception to this is in relation to the sale of endowment properties where any surplus cash is held in the Municipal Endowment Fund to be used to reinvest on behalf of the fund.
9. If assets are subject to legislative restrictions, the proceeds are used in accordance with the provisions of the appropriate legislation.

Investment Mix

Equity Investments

10. Equity investments, include investments held in Council Controlled Organisations (CCO), Council Controlled Trading Organisations (CCTO) and other shareholdings.
11. The Council maintains equity investments and other minor shareholdings. Council's equity investments fulfil various strategic, economic development and financial objectives as outlined in the 10-Year Plan. Equity investments may be held where the Council considers there to be strategic community value.
12. The Council seeks to achieve an acceptable rate of return on all its equity investments consistent with the nature of the investment and their stated philosophy on investments.
13. Any purchase or disposition of equity investments requires Council approval. Council may also acquire shares that are gifted or are a result of restructuring.
14. Dividends received from CCOs/CCTOs and unlisted companies are used firstly to repay debt in relation to that investment, and then used to reduce other Council debt unless otherwise directed by Council.
15. Any dividends received, and/or profit or loss arising from the sale of these investments must be recorded in accordance with appropriate accounting standards.
16. Unless otherwise directed by Council, the proceeds from the disposition of equity investments will be used firstly to repay any debt relating to the investment and then utilised to reduce other Council debt.
17. The Council recognises that there are risks associated with holding equity investments and to minimise these risks the Council, through the relevant Council committee, monitors the performance of its equity investments on a twice yearly basis to ensure that the stated objectives are being achieved. Professional advice regarding Council's equity investments is obtained when appropriate.

New Zealand Local Government Funding Agency limited investment

18. Despite anything earlier in this Policy, the Council may invest in shares and other financial instruments of the New Zealand Local Government Funding Agency Limited (LGFA), and may borrow to fund that investment to:

    a. Obtain a return on the investment.
    b. Ensure that the LGFA has sufficient capital to remain viable, meaning that it continues as a source of debt funding for the Council.
    c. Because of these dual objectives, the Council may invest in LGFA shares in circumstances in which the return on that investment is potentially lower than the return it could achieve with alternative investments. In connection with the investment, Council subscribes for uncalled capital in the LGFA and is a Guarantor.

Property investments

19. The Council will purchase property investments for strategic and commercial purposes.
20. The Council will review ownership through assessing the benefits, including financial returns, in comparison to other arrangements that could deliver similar results.
21. Surpluses generated from property investments are treated as income in the related Council activity.
22. The Council will ensure property disposals are managed to ensure compliance with statutory requirements and where appropriate consultation with the community.
23. The Council will ensure property purchases are supported by registered valuations and, where appropriate, a full business case analysis.
24. The Council will not purchase properties on a speculative basis.

Financial investments

25. The Council's primary objectives when investing is the protection of its investment capital. Accordingly, Council may only invest in approved creditworthy counterparties. Creditworthy counterparties and investment restrictions are covered in Counterparty credit risk of this policy (para. 70-74). Credit ratings are monitored and any changes are reported to Council..
26. The Council may invest in approved financial instruments as set out in the Treasury Management Policy. These investments are aligned with Council's objective of investing in high credit quality and highly liquid assets.
27. The Council's investment portfolio will be arranged to provide sufficient funds for planned expenditures and allow for the payment of obligations as they fall due.
28. The Council prudently manages liquid financial investments as follows:

    a. Any liquid investments must be restricted to a term that meets future cash flow and capital expenditure projections.
    b. Council may choose to hold specific reserves in cash and direct what happens to that investment income. In effect the income from financial investments will be an interest income stream into general funds. Interest is paid to reserves from general funds.
    c. Financial investments do not include shares.

Reserve funds

29. Liquid assets are required to be held against reserve funds.

Trust funds

30. Where the Council hold funds as a trustee, or manages funds for a trust, then such funds must be invested on the terms provided within the trust.
31. Where the trust's investment policy is not specified then this Policy should apply.

Loan Advances

32. The Council may provide advances to CCOs, CCTOs, charitable trusts and community organisations for strategic and commercial purposes.
33. New loan advances must be made by Council Resolution only. The Council will not lend money, provide any other financial accommodation, to a CCO or CCTO on terms and conditions that are more favourable than those that would apply if Council were borrowing the money or obtaining the financial accommodation. (subject to the exemption as per Section 9 of the Local Government Borrowing Act 2011, lending and financial accommodation provided to the Local Government Funding Agency).
34. Advances to charitable trusts, and community organisations from the Council do not have to be on a fully commercial basis.
35. Where the Council makes advances to charitable trusts and community organisations at below Council's cost of borrowing, the additional cost is treated as an annual grant to the organisation.
36. The Council will review performance of its loan advances on a regular basis to ensure strategic and economic objectives are being achieved.

Investment management and reporting procedures

37. The Council's investments are managed on a regular basis, with sufficient minimum immediate cash reserves and a cash buffer maintained.
38. To best manage funding gaps, Council's financial investment maturities are matched with Council's forecast cash flow requirements.
39. The performance of Council investments is regularly reviewed to ensure Council's strategic objectives are being met. Both performance and policy compliance are reviewed through regular reporting.
40. Details on the performance of investments will be reported to the Council, or the appropriate Council Committee, on a regular basis.
41. Monitoring of equity and property investments involves reviewing quarterly reports, annual reports, strategic plans, and statements of corporate intent. Members of these entities may be invited to attend and present to the appropriate Council Committee.
42. Monitoring of cash and other investments form part of the regular financial reporting to the Council and appropriate Council Committees.

LIABILITY MANAGEMENT POLICY

Introduction

43. The Council's liabilities will comprise of borrowings (external) and various other liabilities.
44. The Council maintains external borrowings in order to:

    a. Raise specific debt associated with projects and capital expenditures.

b. Fund the balance sheet as a whole, including working capital requirements.
c. Fund assets where their useful lives extend over several generations of ratepayers.
d. Fund investments in CCOs,
e. Provide funding to CCOs,
f. Fund working capital requirements.

45. Borrowing provides a basis to achieve inter-generational equity by aligning long-term assets with long-term funding sources, and ensure that the costs are met by those ratepayers benefiting from the investment.
46. Borrowing is undertaken at a whole of Council level. That is, borrowing is made as and when it is required to fund the capital and operational activities of the Council.

Borrowing Limits

47. The Council's Financial Strategy, adopted as part of the 10-Year Plan, includes borrowing limits which take account of the planning assumptions and circumstances of the City at the time the plan is adopted. The borrowing limits in this policy are the prudential limits which the Council's funders (including LGFA) and credit rating providers deem to appropriate for the City.
48. These limits are higher than the 10-Year Plan limits with the gap available for the Council to manage any unplanned events.
49. The Council will manage its debt with the following limits:

Item	**Limit**
Net External Debt / Total Revenue	<250%
Net Interest on External Debt / Total Revenue	<20%
Net Interest on External Debt / Annual Rate Income	<30%
Liquidity ratio	>110%

a. **Total revenue** is defined as total revenue less vested assets, gains and development contributions.
b. **Total external debt** is all gross debt held externally by council.
c. **Net external debt** is defined as total external debt less liquid funds and investments.
d. **Liquidity** is defined as external term debt plus committed external borrowing and liquid funds, divided by current external debt.
e. **Liquid funds** are defined as being:
  - Overnight bank cash deposits
  - Wholesale/retail bank term deposits no greater than 30 days
  - Bank issued RCD's less than 91 days
  - Wholesale/ retail bank term deposits linked to pre-funding of maturity of term debt exposures.

f. The liquidity ratio excludes encumbered cash investments, such as cash held within special / reserve funds.
g. **Net interest on external debt** is defined as the amount equal to all interest and financing costs (on external debt) less interest income for the relevant period.

h. **Annual rate income** is defined as the amount equal to the total revenue from any funding mechanism authorised by the Local Government (Rating) Act 2002 (including volumetric water charges levied) together with any revenue received from other local authorities for services provided (and for which the other local authorities rate).

50. Financial covenants are measured on Council only, not the consolidated group.
51. Disaster recovery requirements are to be met through the liquidity ratio and available debt capacity.

Security

52. The Council's external borrowings and interest rate management instruments will generally be secured by way of a charge over rates and rates revenue offered through a Debenture Trust Deed.
53. Where appropriate the Council may seek project financing, which may have a charge over the project or a specific asset(s) rather than rates.
54. The Council's utilisation of special funds, reserve funds, internal borrowing of special funds/reserve funds and other funds will be on an unsecured basis.

55. Under a Debenture Trust Deed, The Council's borrowing is secured by a floating charge over all the Council rates levied under the Local Government Rating Act.

56. The security offered by Council ranks equally or pari passu with other lenders.

57. From time to time, and with the Council approval, debt may be undertaken on an unsecured basis, or security may be offered by providing a charge over one or more of Council's assets.

58. The Councils physical assets will be charged only where:
    a. There is a direct relationship between the debt and the purchase or construction of the asset, which it funds (e.g. project finance)
    b. Council considers a charge over physical assets to be appropriate
    c. Any pledging of physical assets complies with the terms and conditions contained within the security arrangement

Borrowing mechanisms

59. The Council may externally borrow through a variety of market mechanisms including issuing stock/bonds, commercial paper (CP) and debentures, direct bank borrowing, Local Government Funding Agency (LGFA), Central Government Agencies (eg. Housing Infrastructure Fund (HIF)) accessing the short and long-term wholesale/retail debt capital markets directly or indirectly, or internal borrowing of reserve funds.
60. In evaluating strategies for new borrowing (in relation to source, term, size and pricing) the following is taken into account:

    a. Available terms from lenders.
    b. The Council's overall debt maturity profile, to ensure concentration of debt is avoided at reissue/rollover time.
    c. Prevailing interest rates and margins relative to term for loan stock issuance, LGFA, debt capital markets and bank borrowing.
    d. The market's outlook on future interest rate and credit margin movements as well as its own.

e. Legal documentation and financial covenants together with security and credit rating considerations.
f. For internally funded projects, to ensure that finance terms for those projects are at least as equitable with those terms from external borrowing.
g. Alternative funding mechanisms such as leasing should be evaluated with financial analysis in conjunction with traditional on-balance sheet funding. The evaluation should take into consideration, ownership, redemption value and effective cost of funds.

61. The Council's ability to readily attract cost effective borrowing will be determined by its ability to rate, maintain a strong financial standing and manage its relationships with its investors, LGFA, credit rating agencies and financial institutions/brokers.

Debt repayment

62. The funds from all asset sales, operating surpluses, grants and subsidies will be applied to specific projects or the reduction of debt and/or a reduction in borrowing requirements, unless the Council specifically directs that the funds will be put to another use.
63. Debt will be repaid as it falls due in accordance with the applicable borrowing arrangement.
64. Subject to the appropriate approval and debt limits, a loan may be rolled over or re-negotiated as and when appropriate.
65. The Council will manage debt on a net portfolio basis and will only externally borrow when it is commercially prudent to do so.

Interest rate risk

66. Risk recognition
    a. Interest rate risk is the risk that funding costs (due to adverse movements in market wholesale interest rates) will materially exceed or fall short of projections included in the 10-Year Plan or Annual Plan so as to adversely impact revenue projections, cost control and capital investment decisions/returns/feasibilities.
    b. The Council will ensure interest rate risk management to reduce uncertainty relating to interest rate movements through fixing/hedging of interest costs. Certainty around interest costs is to be achieved through the active management of underlying interest rate exposures.

67. Interest rate risk control limits
    a. The exposure to interest rate risk is managed and mitigated through the risk control limits below. Council's gross external debt should be within the following fixed/floating interest rate risk control limit.
    b. Forecast gross external debt is the amount of total external debt for a given period (12 month).
    c. The Council's gross external debt will allow for pre-hedging in advance of projected physical drawdown of new debt.
    d. When approved forecasts are changed (signed off by the CFO), the amount of fixed rate cover in place may have to be adjusted to ensure compliance with the Policy minimums and maximums as per the following table:

Debt Interest Rate Policy Parameters (calculated on rolling monthly basis)		
Debt Period Ending	**Minimum Fixed**	**Maximum Fixed**
0 – 1 Year	40%	95%
1 - 2 Years	35%	95%
2 - 3 Years	30%	90%
3 - 4 Years	20%	85%
4 - 5 Years	10%	80%
5 - 6 Years	0%	75%
6 - 7 Years	0%	70%
7 - 8 Years	0%	65%
8 - 9 Years	0%	60%
9 - 10 Years	0%	55%
10 - 11 Years	0%	50%
11 - 12 Years	0%	45%
12 - 13 Years	0%	40%
13 - 14 Years	0%	35%
14 - 15 Years	0%	30%

e. A fixed rate maturity profile that is outside the above limits, but self corrects in less than 90 days is not in breach of this Policy.

f. Maintaining a maturity profile outside of the above limits beyond 90 days requires Council resolution.

- "Fixed Rate" is defined as all known interest rate obligations on forecast gross external debt, including where debt is borrowed on a fixed interest rate basis and where hedging instruments have fixed movements in the applicable reset rate.
- "Floating Rate" is defined as any interest rate obligation subject to movements in the applicable reset rate.
- Fixed interest rate percentages are calculated monthly by the GMC based on the average amount of fixed interest rate obligations relative to the average forecast gross external debt amounts for the given period (as defined in the table above).
- Any interest rate fixing with a maturity beyond 15 years must be approved by the Chief Executive through a specific approval. The exception to this will be if Council raises LGFA funding as fixed rate or an interest rate swap is linked to floating rate LGFA debt and this is maturing beyond 15 years.
- Hedging outside the above risk parameters must be approved by Council.

Liquidity risk/funding risk

68. Risk recognition

a. Cash flow deficits in various future periods based on long term financial forecasts are reliant on the maturity structure of cash, short-term financial investments, loans and bank facilities. Liquidity risk management focuses on the ability to access committed funding at that future time to fund the gaps. Funding risk management centres on the ability to re-finance or raise new debt at a future time at the same or more favourable pricing (fees and borrowing margins) and maturity terms of existing loans and facilities.

b. The Council will manage funding risks where there may be adverse movement in borrowing margins, term availability and general flexibility including:

- Local Government risk is priced to a higher fee and margin level.
- Council's own credit standing or financial strength as a borrower deteriorates due to financial, regulatory or other reasons.
- A large individual lender to Council experiences its own financial/exposure difficulties resulting in Council not being able to manage their debt portfolio as optimally as desired.
- New Zealand investment community experiences a substantial "over supply" of Council investment assets.
- Financial market shocks from domestic or global events.

c. A key factor of funding risk management is to spread and control the risk to reduce the concentration of risk at one point in time so that if any of the above events occur, the overall borrowing cost is not unnecessarily increased and desired maturity profile compromised due to market conditions.

69. Liquidity/funding risk control limits

a. The Council will ensure liquid funds, term debt and committed debt facilities must be maintained at an amount exceeding 110% of existing external debt.
b. The GMC has the discretionary authority to re-finance existing external debt on more favourable terms.
c. Such action is to be reported to the Chief Executive and the appropriate Council Committee at the earliest opportunity.
d. The maturity profile of the total committed funding in respect to all external debt / loans and committed debt facilities, is to be controlled by the following system:

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

e. A funding maturity profile that is outside the above risk parameters but self corrects within 90-days is not in breach of this policy. However, maintaining a maturity profile that is outside the above risk parameters for a period greater than 90-days requires specific approval by the Council.
f. To minimise concentration risk the LGFA require that no more than the greater of NZD $100 million or 33% of the Councils borrowings from the LGFA will mature in any 12-month period.

g. The Council has the ability to pre-fund up to 18 months forecast debt requirements including re-financings. Debt refinancing that has been pre-funded will remain included within the funding maturity profile until the maturity date.

Counterparty credit risk

70. Counterparty credit risk is the risk of losses (realised or unrealised) arising from a counterparty defaulting on a financial instrument where the Council is a party. The credit risk to the Council in a default event will be weighted differently depending on the type of instrument entered into.
71. Credit risk will be regularly reviewed by the appropriate Council Committee. Treasury related transactions would only be entered into with organisations specifically approved by the (CE).
72. Counterparties and limits can only be approved on the basis of long-term Standard & Poor's (S&P) credit ratings (or equivalent Fitch or Moody's rating) being A and above and/or short term rating of A-1 or above.
73. Limits should be spread amongst a number of counterparties to avoid concentrations of credit exposure.
74. The following matrix guide will determine limits:

Counterparty/Issuer	Minimum S&P long term / short term credit rating	Total maximum per counterparty ($m)
NZ Government	N/A	Unlimited
Local Government Funding Agency (LGFA)	N/A	Unlimited
NZ Registered Bank	AA- / A-1	75.0
NZ Registered Bank	A /A-1	30.0

Guarantees/contingent liabilities and other financial arrangements

75. The Council may act as guarantor to financial institutions on loans or enter into incidental arrangements for organisations, clubs, trusts, or business units, when the purposes of the loan are in line with Council's strategic objectives.

76. When resolving to act as a guarantor, Council will ensure appropriate processes are implemented to review and monitor the performance of guarantee.

77. The Council is not allowed to guarantee loans to Council-controlled trading organisations under Section 62 of the Local Government Act.

78. Other financial arrangements may include community loans and advances.

79. Conditions to financial arrangements will be set by the Council when the arrangement is approved.

Monitoring and Implementation

80. Implementation of this policy will be monitored by the General Manager Corporate.

81. This policy will be reviewed, at the request of the Council, in response to any relevant legislative amendment, or every three years (whichever comes first)

REFERENCES

- Section 102, 104, 105, 112 to 122 and Schedule 7 Clause 32 of the Local Government Act 2002