

Chairperson and Committee Members
CORPORATE BUSINESS COMMITTEE

12 MAY 2016

Meeting Status: **Public**

Purpose of Report: For Information

**LOCAL GOVERNMENT FUNDING AGENCY HALF-YEAR
REPORT TO 31 DECEMBER 2015**

PURPOSE OF REPORT

- 1 The purpose of this report is to update the Corporate Business Committee on the Local Government Funding Agency (LGFA) Half-year Report to 31 December 2015.

DELEGATION

- 2 The Corporate Business Committee has delegated authority to consider this report under the following delegation in the Governance Structure, Section B.3.7.

Without limiting the generality of this delegation, the committee has the following functions, duties and powers.

Financial and Asset Management

7.5 Authority to monitor performance of the Council's financial activities, including income, operating and capital expenditure against budgets, remissions, key financial indicators and investment and debt/borrowings management.

BACKGROUND

- 3 The LGFA was incorporated on 1 December 2011 with the primary objective of optimising the debt funding terms and conditions for Participating Local Authorities. This includes providing savings in annual interest costs, making longer-term borrowings available and enhancing the certainty of access to debt markets.
- 4 The LGFA issues bonds to wholesale and retail investors and on-lends the funds raised to participating local authorities with borrowing needs. The quality of the LGFA's credit rating, and the liquidity created by issuing homogenous local authority paper, ensures that participating councils can raise funds on better terms than if they were issuing in their own name.
- 5 On 30 November 2012, Council became a Principal Shareholding Local Authority in the LGFA. The LGFA meets the Local Government Act (LGA) 2002 definition of a Council Controlled Organisation (CCO). As a shareholder in a CCO, the Council must regularly undertake performance monitoring of that organisation to evaluate its contribution to the achievement of the Council's desired outcomes.

ISSUES AND OPTIONS

LGFA performance for the six months to 31 December 2015

- 6 The LGFA has performed strongly for the first six months of the 2015/16 year and has continued to grow, in terms of the value, term and diversity of loans issued as well as the actual membership of the LGFA.
- 7 While the LGFA has continued to provide cost savings to councils, it acknowledges that its benchmark estimated savings for AA-rated councils has diminished during the period. Global uncertainty has resulted in reduced demand for NZD investments and for bonds issued by non-sovereign borrowers.
- 8 At 31 December 2015 the LGFA estimated that it was saving AA-rated councils approximately 11 basis points (bps) for a 2019 (four year) maturity. This compares unfavourably with the position at 30 June 2015 when it was estimating a 16 to 19 bps saving for AA-rated councils for the 2017 and 2019 dated maturities. The Kāpiti Coast District Council has a Standard and Poor's credit rating of A+, slightly lower than AA, suggesting a lower but comparable quantum of savings.
- 9 The LGFA increased its borrowings to participating councils by \$710 million during the six month period to 31 December 2015. The increased borrowings resulted in interest income of \$134 million, a 28% increase on the same period ending 31 December 2014. However increased costs mean that the net profit for the period was 3.55% (\$4.8 million) compared to a net profit for the same period ending 31 December 2014 of 4.27% (\$4.5 million).
- 10 These increased costs were a result of higher interest expense payable to investors in LGFA bonds and a 32% increase in operating expenses, largely a result of listing LGFA bonds on the NZX and higher Approved Issuer Levy payments due to increased offshore investment.
- 11 During the period the LGFA offered short dated lending for the first time. In addition the LGFA's bespoke lending service has proved popular with \$178 million (25%) of bespoke lending during the period.
- 12 The LGFA has retained its strong credit rating of AA+ from both Fitch and Standard and Poor's. In January 2016, Fitch ratings revised the Rating Outlook of LGFA from Positive to Stable; Fitch had previously made the same revision to the NZ Government.
- 13 During the period, Buller District Council and Canterbury Regional Council became members of the LGFA as Participating Local Authorities. Since 1 July 2015 the LGFA has increased its number of Directors from five to six.
- 14 Auckland Council is the LGFA's largest borrower (\$1.96 billion), followed by Christchurch City Council (\$1.05 billion). As at 31 December 2015, Kāpiti Coast District Council ranked as the 7th largest borrower with \$150 million.
- 15 The full LGFA Half-year Report to 31 December 2015 is attached as Appendix 1.

CONSIDERATIONS

Policy considerations

- 16 In accordance with the LGA 2002, the Council must provide information on all of its CCOs in its Long Term Plan (LTP). Accordingly the 2015/35 LTP contains information on the LGFA, including key performance targets and other performance metrics.

Legal considerations

- 17 There are no legal considerations arising from the matters in this report.

Financial considerations

- 18 Council is one of 30 local authority shareholders of the LGFA and has an obligation in respect of uncalled capital of \$100,000.
- 19 At 31 December 2015, the LGFA had borrowings totalling \$5.67 billion.
- 20 Council considers the risk of the LGFA defaulting on repayment of interest or capital to be very low on the basis that:
- a) The only circumstance where LGFA would default on its debt is the event where a council defaulted on a loan obligation that exceeded LGFA's available liquidity assets. As at 31 December 2015, this would need to be a single council default event that exceeded \$650 million, being the sum of:
 - cash and deposits of \$140 million, and
 - LGFA borrower notes of \$90 million, and
 - LGFA credit facility of \$400 million, and
 - uncalled share capital of \$20 million from LGFA shareholders.
 - b) In the event of an LGFA default, the call on the guarantee is made on council's proportion of their share of the underlying rate base.
 - c) In the event of a default exceeding the LGFA's available liquid assets, the council would be called for 1.2% of the overall call (less than the council's 2.6% of LGFA's loan assets).

Tāngata whenua considerations

- 21 There are no tāngata whenua considerations.

SIGNIFICANCE AND ENGAGEMENT

Degree of significance

- 22 This matter has a low level of significance under Council policy, and it is not significant.

Consultation already undertaken

- 23 There is no need to consult on the matters discussed in this report.

Engagement planning

24 An engagement plan is not needed for this report to be considered.

Publicity

25 There are no publicity considerations.

RECOMMENDATIONS

26 That the Corporate Business Committee notes the performance of the Local Government Funding Agency in its half-year Report to 31 December 2015.

Report prepared by

**Approved for
submission by**

**Approved for
submission by**

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ATTACHMENT

Appendix 1 – LGFA Half-year Report to 31 December 2015