

Report 13.711
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Committee Council
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Local Government Funding Agency (LGFA) Statement of Intent & June quarter update

1. Purpose

To present the final LGFA Statement of Intent for 2013/14 and the LGFA's quarterly report for the period ending 30 June 2013.

2. The decision-making process and significance

The matter requiring decision in the report has been considered by officers against the requirements of Part 6 of the Local Government Act 2002 (the Act).

Officers have considered the significance of the matter, taking the Council's significance policy and decision-making guidelines into account. Officers recommend that the matter be considered to have low significance.

Officers do not consider that a formal record outlining consideration of the decision-making process is required in this instance.

3. Background

The LGFA was established on 6 December 2011 and being a Council Controlled Trading Organisation (CCTO), it is required to prepare a Statement of Intent to its shareholders.

Greater Wellington Regional Council (GWRC) has been a promoter of this organisation and initially held \$2 million of the \$25 million share capital, being one of the initial 18 non central government founding shareholders.

In December 2012 the Council sold down part of its shareholding (from \$2m initially down to \$1.866m) to allow 12 other councils to join the LGFA. This brought the total number of participating councils to 30.

GWRC has a representative on the Shareholders' Council, which is a group consisting of the nine Councils which originally promoted the LGFA.

The principal role of the Shareholder Council is to monitor the LGFA and to provide a focal point for LGFA communication. The Council has formal meetings and has met six times since the LGFA was established.

The Shareholders' Council has developed its own charter, provided assistance with debt settlements, developed a monitoring framework to monitor the LGFA, monitored the LGFA performance, and provided a Letter of Expectation to the LGFA in relation to its SOI and business operation.

A LGFA draft SOI was provided to Councillors via the bulletin in early April after receipt from the LGFA in late March.

The Shareholders' Council made a number of comments on the SOI, and these are recorded in a letter to the Chair of the LGFA – (refer **Attachment 1**).

4. Statement of Intent

The final Statement of Intent (refer **Attachment 2**) was received in July.

Looking at the three year plan, the following highlights are notable.

A profit forecast of \$6.64 million in the 2013/14 year climbs to \$8.34 million in 2015/16.

A flat dividend is forecast of \$1.5 million for the 3 years with equity growing from \$22 million in 2012/13 to \$40.5 million by June 2016.

Total assets (mostly lending to Council) increase from \$2,499 million in 2012/13 to \$5,358 million in 2015/16.

The performance targets have the LGFA's average cost of funds set at 0.50% above NZ Government Stock for the 2013/14 year and reducing to 0.40% for the subsequent two years. This remains 0.10% higher in the 2013/14 year than in last year's SOI, reflecting the global financial situation and the impact this is having on margins generally.

The forecasted margins charged to councils by the LGFA are reducing significantly from not more than 0.40% in last year's SOI to not more than 0.25%, 0.20% and 0.15% for the next three years respectively. This reflects the impact of the larger asset base and economies of scale and is consistent with the draft SOI.

The performance targets and objectives in this year's SOI have been amended to be more quantifiable in line with best practice.

When comparing the final SOI to the draft SOI the following variances are noted.

	Year 2013/14 \$000	Year 2014/15 \$000	2015/16 \$000
<i>Net Profit (Draft SOI)</i>	\$5.2m	\$5.8m	\$6.1m
Net Profit (Final SOI)	\$6.6m	\$7.9m	\$8.3m
Increase (Decrease)	\$1.4m	\$2.1m	\$2.2m
<i>Total Assets (Draft SOI)</i>	\$2.601b	\$2.946b	\$3.459b
Total Assets (Final SOI)	\$3.506b	\$4.351b	\$5.358b
Increase (Decrease)	\$905m	\$1,405m	\$1,899m
<i>Dividends (Draft SOI)</i>	\$1.5m	\$1.5m	\$1.5m
Dividends (Final SOI)	\$1.5m	\$1.5m	\$1.5m
Increase (Decrease)	-	-	-

These increases clearly show the conservative budget assumptions under which the draft SOI was prepared. As result of higher forecasted borrowings, the profitability of the LGFA has increased. This is not currently showing through as an increased dividend in the forecasted period, but it is likely to going forward, and is discussed under section 11 of the SOI. The dividend is based on the LGFA cost of funds plus 2%, so Council could expect to receive a dividend in the vicinity of \$100,000 later this year.

5. Shareholders' Council Quarterly report –30 June 2013

The report is report is appended (refer to **Attachment 3**). Highlights from report are noted below:

Total bonds issued were \$1.950 billion for the 2012/13 year.

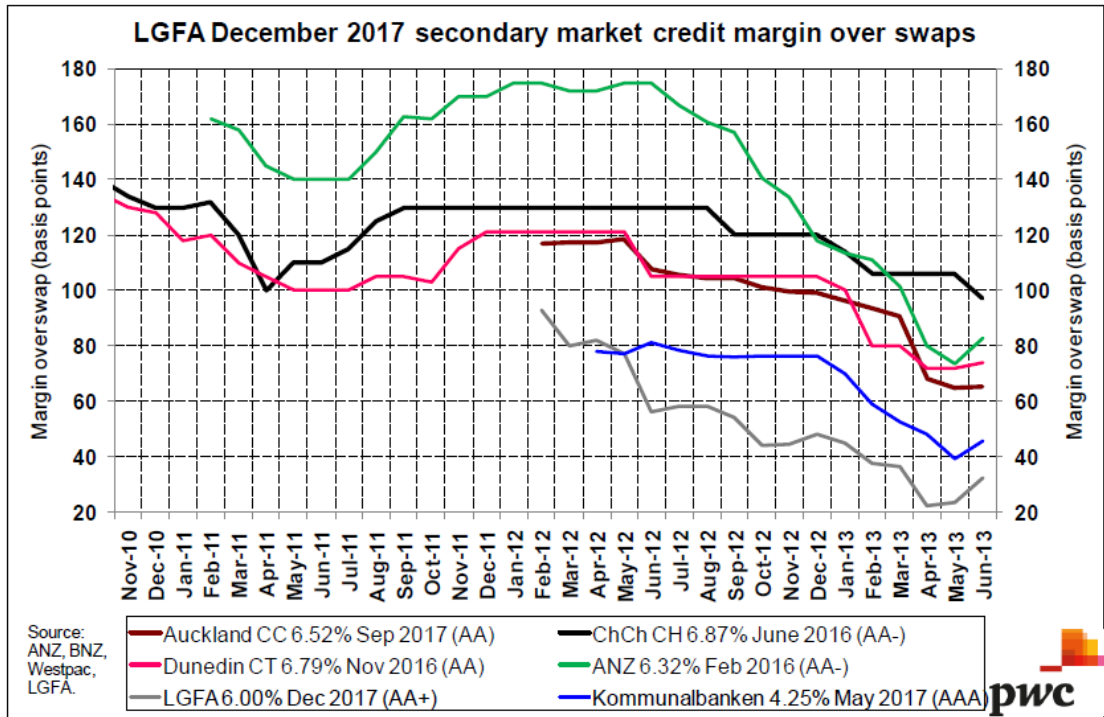
Despite market conditions weaken during the quarter with the announcement of the Federal Reserve indicating tapering of its quantitative easing (QE) programme LGFA borrowing margins were not as badly impacted as other borrowers.

The pricing of the LGFA remains favourable and their on-lending margin to Councils has reduced to 20 points from 30 points on the first issue.

The savings impact of using the LGFA compared to the Councils raising debt directly by itself is estimated in the range of 20 and 30 for a 4 to 6 year maturity respectively and is down from 40 points for a 4 year bond in the March quarter. This is connected with a general lowering of credit spreads as

they converge to lower levels. If one compares the green ANZ line to the grey LGFA line in the chart below it is easily seen.

The chart below show the pricing the LGFA receives over the swap benchmark compared to other debt issuers. It is interest to note Kommunalbanken – The Norwegian equivalent of the LGFA and better rated at AAA cannot get a finer pricing as the LGFA does with a AA+ credit rating.



LGFA overall Bond issuance is \$2.5 billion, twice that of the original business case. This has produced a net profit of \$3.5 million, exceeding the SOI forecasted by \$2.3 million!

6. Recommendations

That the Council:

1. *Notes the contents of this report*
2. *Notes the Statement of Intent from the Local Government Funding Agency for 2013/14 and the next two years.*
3. *Notes the Local Government Funding Agency Quarterly Report for the period ended 30 June 2013*

Mike Timmer
Treasurer

Warren Tocker
Chief Financial Officer

Attachment 1: Statement of Intent for 2013/14 – Comment by Shareholders Council

Attachment 2: LGFA Ltd Final Statement of Intent 2013/14

Attachment 3: LGFA Quarterly Report for the period ended 30 June 2013