



Meeting of the Finance Audit & Risk Sub-committee

LATE ITEM

Date: Wednesday 22 May 2019
Time: 9.00am
Venue: Council Chamber
Hawke's Bay Regional Council
159 Dalton Street
NAPIER

Agenda

ITEM	SUBJECT	PAGE
Information or Performance Monitoring		
13.	Treasury Report	3

HAWKE'S BAY REGIONAL COUNCIL
FINANCE AUDIT & RISK SUB-COMMITTEE

Wednesday 22 May 2019

Subject: TREASURY REPORT

Item 13

Reason for Report

1. This item provides an update on the development of Council's diversified investment portfolio and application to join the Local Government Funding Agency (LGFA).

Background

2. Council has engaged PwC to provide treasury advice and reporting, their quarterly treasury report for the period ended 31 March 2019 is **attached**.
3. The last update provided to FARS on 12 February 2019, outlined the distribution of funds to dual fund managers. At this time \$15m of a total \$40m allocation pool was distributed. Staff can confirm that the full \$40m has now been fully allocated, with performance of each fund outlined in treasury report.
4. This treasury report will be further developed for future updates and will include additional analysis such as cash flow forecasting and borrowing limit covenants.

Joining LGFA

5. Authority to execute all of the documentation for joining the LGFA was resolved by Council on 19 December 2018. Staff have worked alongside Council's solicitors to complete all of the documentation, with Council successfully acceding on 29 March 2019.
6. Council has drawn down an initial \$2.5m from LGFA's recent tender on 20 May 2019, in line with approved borrowing for Year 1 of the LTP.

Decision Making Process

7. Staff have assessed the requirements of the Local Government Act 2002 in relation to this item and have concluded that as this report is for information only, the decision making provisions do not apply.

Recommendation

That the Finance Audit and Risk Sub-committee receives and notes the "*Treasury Report*".

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Approved by:

Jessica Ellerm
GROUP MANAGER CORPORATE
SERVICES

Attachment/s

[!\[\]\(5d954b3e270654ad8ab0d5913161c03c_img.jpg\) 1](#) HBRC Treasury Reporting May 2019

Hawke's Bay Regional Council

Quarterly Treasury Reporting

As at 31 March 2019

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1.0 Market Commentary

Investment markets

It was a strong start for the portfolio led by global optimism about US and China trade and accommodative central banks. Although no agreement between the US and China has been reached, the news flow was generally positive, raising hopes that more damaging tariffs can be avoided. Having previously indicated further interest rate increases, the US Federal Reserve (Fed) said it was now remaining patient in regards to any further policy changes.

The Fed's switch to an easier monetary policy stance set the tone for other central banks, notably the European Central Bank. Our own Reserve Bank (RBNZ) recently reduced interest rates by 25 basis points to an all-time low OCR of 1.50%. The Reserve Bank of Australia also hinted that interest rate cuts are likely.

The New Zealand equity market performed well as investors sought high dividend yielding shares amidst low and falling interest rates. Interest rates in NZ fell further, partly following the global trend, and partly due to the RBNZ comments. The NZ 10-year government bond yield reached a record low of 1.78% during the quarter.

Funding markets

The first quarter saw good investor interest across the spectrum of bond maturities offered at the LGFA tenders. The smaller than usual amount of high grade issuance in NZD terms (i.e. Kauri issues) offered over this time resulted in stronger than usual bid-coverage ratios and tighter credit spread to swap/NZ Government bonds. Credit market sentiment has improved slightly, commensurate with many of the global central banks / governments helping to reinvigorate global financial market conditions through 'looser' monetary policy and increased fiscal stimulus.

A positive credit rating outlook change for LGFA will also have assisted in tighter LGFA credit spreads relative to the start of the year. However, the observation is that borrowers/investors are still wary of market conditions, and still favour shorter-term bond issuances over longer-term issuances. Credit spreads have recently reversed some of their prior declines, reflecting some profit taking ahead of the RBNZ's monetary policy statement on 8 May. Over the next quarter, the expectation is that credit spreads will continue to consolidate around current levels.

Interest rate markets

Commensurate with activity evidenced across global interest rate markets, the New Zealand wholesale interest rate swap curve has moved to historically low levels over the last six months. Many of the world's largest central banks have turned increasingly dovish in their outlook for monetary policy on the back of expectations of a global growth slowdown. Importantly, the Fed changed its interest rate projections for 2019 to no rate hikes from three hikes indicated previously, and also cut the median 'longer-term neutral rate' from 3.10% to 2.60%. The current Fed Funds Rate is 2.5%.

Much of the softer global outlook has translated through to a lower wholesale interest rate curve in New Zealand with an outlook that rates will stay lower for longer as the RBNZ continues to stimulate stronger GDP growth conditions that promote higher inflation in New Zealand.

2.0 Treasury Activity Compliance Monitor

Policy document	Policy parameters	Compliance
Treasury Policy	Borrowing limits	Yes
	Funding risk control limits	Yes
	Liquidity buffer	Yes
	Interest rate risk control limits	No
	Treasury investment parameters	Yes
	Counterparty credit limits	Yes
SIPO	Asset allocations	No

3.0 Investment Management Reporting

FNZC

Market Value

Asset Class	Opening Balance	Purchases / (Sales)	Realised Gains/(Losses)	Unrealised Gains/(Losses)	Change in Accrued Interest	Closing Balance	(Fees and Taxes)	Gross Income	Total Gain/(Loss)
Cash	3,071,138	(128,604)		-		2,942,534.0		27,557.0	27,557.0
NZ Fixed Interest	811,812	9,227,157.0		7,721	52,230	10,098,920.0		14,880.0	74,831.0
Intl Fixed Interest	-	3,699,968.0		45,976		3,745,944.0			45,976.0
NZ Equities	1,133,132	344,896.0	(30)	123,950		1,601,948.0		4,780.0	128,700.0
Intl Equities	-	1,661,686.0		92,828		1,754,514.0			92,828.0
NZ Property	-	242,291.0		17,110		259,401.0		2,406.0	19,516.0
Intl Property	-					-			-
Total	5,016,082.0	15,047,394.0	(30.0)	287,585.0	52,230.0	20,403,261.0	(2,227.9)	49,623.0	389,408.0

Performance and SIPO asset allocations

Asset Class	Investment Return	Asset Allocation	SIPO Weightings		SIPO Compliant?
Cash	4.2%	14.4%	2.0%	8.0%	No
NZ Fixed Interest	1.3%	49.5%	15.0%	24.0%	No
Intl Fixed Interest	1.6%	18.4%	23.0%	28.0%	No
NZ Equities	10.4%	7.9%	13.0%	18.0%	No
Intl Equities	6.6%	8.6%	25.0%	34.0%	No
NZ Property	10.8%	1.3%	1.0%	4.0%	Yes
Intl Property	-	-	1.0%	4.0%	No
Total	3.1%	100.0%			No

We understand that the investment portfolio is not SIPO compliant as FNZC are still establishing the Fund and investment allocations.

Mercer

Market Value

Asset Class	Opening Balance	Purchases (Sales)	Realised Gains(Losses)	Unrealised Gains(Losses)	Change in Accrued Interest	Closing Balance	(Fees and Taxes)	Gross Income	Total Gain(Loss)
Operational Cash	20,004.00	-	-	-	10.5	9,692.4	-	-	-
Index Cash Portfolio	740,000.00	2,171,173	-	8,572	-	2,919,745.1	-	-	8,572.1
NZ Sovereign Bonds	700,000.00	2,120,973.0	-	60,754	-	2,881,726.6	-	-	60,753.6
Overseas Sovereign Bonds	600,000.00	1,812,394.0	-	49,935	-	2,462,329.4	-	-	49,935.4
Global Credit	449,999.00	1,358,050.0	-	35,261	-	1,843,310.2	-	-	35,261.2
Other Fixed Interest	-	-	-	-	-	-	-	-	-
Socially Responsible Trans-Tasman Shares	299,999.00	890,035.0	-	56,702	-	1,246,735.5	-	-	56,701.5
Socially Responsible Overseas Shares	1,540,000.00	4,730,131	-	137,185	-	6,407,316	-	-	137,184.9
International Listed Property	324,999.00	955,876.0	-	56,248	-	1,347,122.6	-	-	56,247.6
Unlisted Property	-	-	-	-	-	-	-	-	-
International Listed Infrastructure	324,999.00	961,375.0	-	62,706	-	1,349,079.7	-	-	62,705.7
Unlisted Infrastructure	-	-	-	-	-	-	-	-	-
Total	5,000,000.00	15,010,007.0	-	467,362.0	-	20,467,057.5	(15,737.8)	-	467,362.0

Asset Class	Investment Return	Asset Allocation	Mercer Portfolio Ranges		Portfolio Compliant?
Operational Cash					
Index Cash Portfolio	0.5%	14.3%	0.0%	20.0%	Yes
NZ Sovereign Bonds	2.7%	14.1%	5.0%	25.0%	Yes
Overseas Sovereign Bonds	2.5%	12.0%	5.0%	25.0%	Yes
Global Credit	3.6%	9.0%	5.0%	25.0%	Yes
Other Fixed Interest		-	0.0%	10.0%	No
Socially Responsible Trans-Tasman Shares	5.5%	6.1%	0.0%	18.0%	Yes
Socially Responsible Overseas Shares	4.2%	31.3%	17.0%	37.0%	Yes
International Listed Property	8.9%	6.6%	0.0%	10.0%	Yes
Unlisted Property		-	0.0%	10.0%	No
International Listed Infrastructure	8.6%	6.6%	0.0%	10.0%	Yes
Unlisted Infrastructure		-	0.0%	10.0%	No
Total	3.9%	100.0%			No

Performance and SIPO asset allocations

We understand that the investment portfolio is not SIPO compliant as Mercer are still establishing the Fund and investment allocations.

All returns presented above are before fees and inflation adjustments (i.e. are gross returns). The reported returns are lower than HBRC's net return target of 4.5% per annum. This is in part due to the staggered allotment of capital provided to the investment managers and desired strategic asset allocations continuing to be constructed over the period.

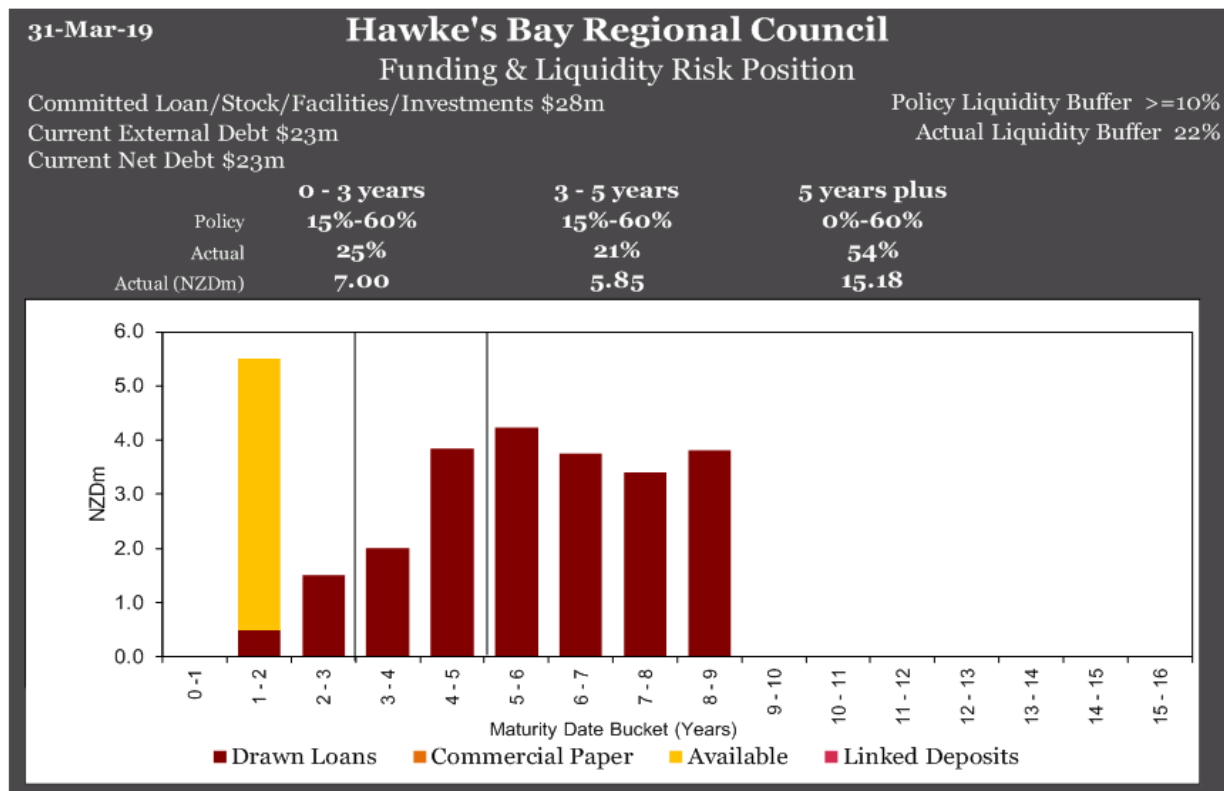
4.0 Treasury Investments

No treasury investments currently held.

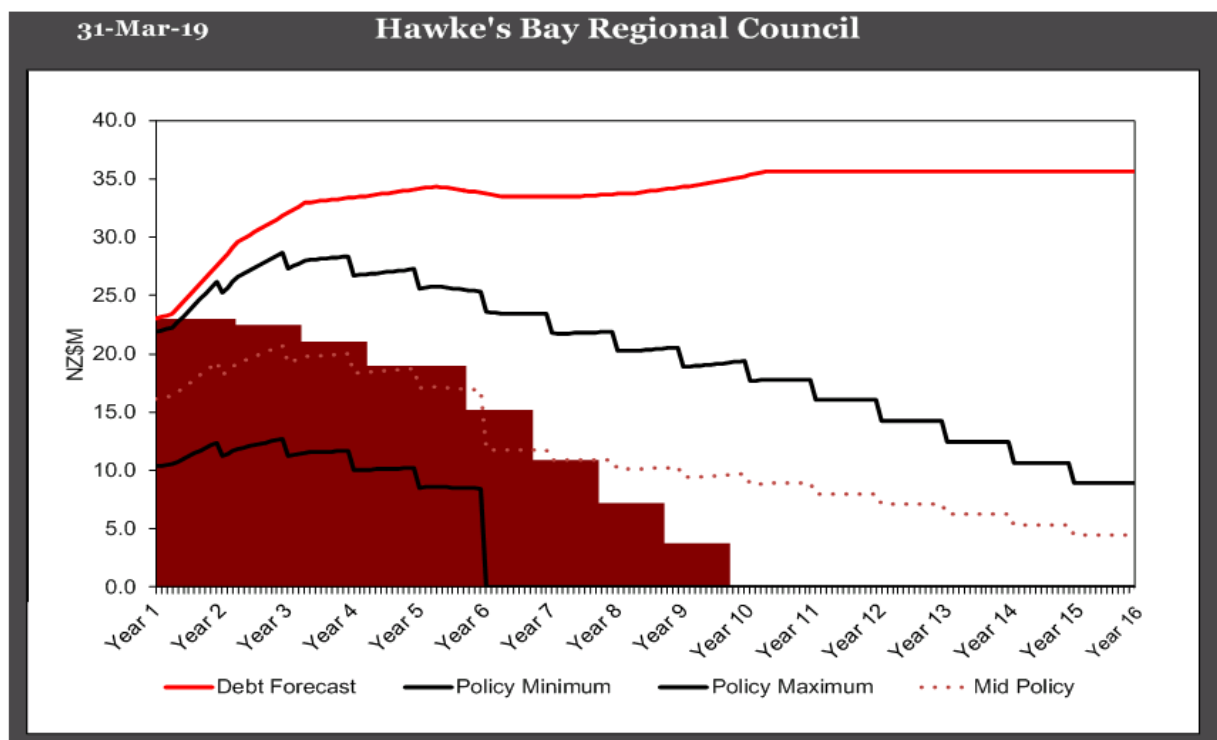
5.0 Liability Management Policy Compliance Checklist

31-Mar-19			
Liquidity Buffer:	10%		
Actual	22%		
Policy Compliance	Y		
Funding Maturity Profile:			
Years	0 - 3 years	3 - 5 years	5 years plus
Policy Limits	15% - 60%	15% - 60%	0% - 60%
Actual Hedging	25%	21%	54%
Policy Compliance	Y	Y	Y
Weighted Average Duration:			
Funding		5.22 Years	
Fixed Rate Portfolio (swaps and fixed rate loans)		6 Years	
Weighted average margin		0.00%	
Weighted average Commitment/Line Fee		0.05%	
Weighted average fixed rate (swaps & term loans/bonds)		5.44%	
All up cost of borrowing (On Drawn Debt)		5.49%	

6.0 Funding and Liquidity Risk Position



7.0 Interest Rate Risk Position



Debt Interest Rate Policy Parameters

(calculated on rolling monthly basis)

Debt Period Ending	Debt Forecast	Minimum %	Maximum %	Actual	Compliant (Y/N)
Year 1	23	45%	95%	100%	No
Year 2	28	40%	90%	82%	Yes
Year 3	32	35%	85%	70%	Yes
Year 4	33	30%	80%	63%	Yes
Year 5	34	25%	75%	56%	Yes
Year 6	34	0%	70%	45%	Yes
Year 7	34	0%	65%	33%	Yes
Year 8	34	0%	60%	21%	Yes
Year 9	34	0%	55%	11%	Yes
Year 10	35	0%	50%	0%	Yes
Year 11	36	0%	45%	0%	Yes
Year 12	36	0%	40%	0%	Yes
Year 13	36	0%	35%	0%	Yes
Year 14	36	0%	30%	0%	Yes
Year 15	36	0%	25%	0%	Yes

8.0 Funding Facility

Bank (Facility maturity date)	Maturity Date	Drawdown Amount (\$m)	Facility Limit (\$m)
BNZ	15-Jan-21	0.00	5.00
TOTAL	n/a	0.00	5.00

Available bank facility capacity (liquidity buffer)	This month (\$m)	Last month (\$m)
Gross amount	5.00	5.00
Policy liquidity buffer requirements	2.30	2.30
Excess amount	2.70	2.70

9.0 Counterparty Credit

Counterparty Credit Risk (Interest Rate Risk Management Instruments and Investments)			
Rates Revenue			\$ 19,475,000
Policy Credit Limit (NZ\$) per NZ Registered Bank (Interest rate risk management)		15%	
Policy Credit Limit (NZ\$) per NZ Registered Bank (Investments)		20-50%	
	Credit Exposure (Swaps) (\$m)	Credit Exposure (Investments) (\$m)	Compliance
WPC	0.00	0.00	Yes
ANZ	0.00	0.00	Yes
ASB	0.00	0.00	Yes
BNZ	0.00	0.00	Yes
Kiwibank	0.00	0.00	Yes
LGFA	0.00	0.00	Yes

10.0 Debt Funding Strategy

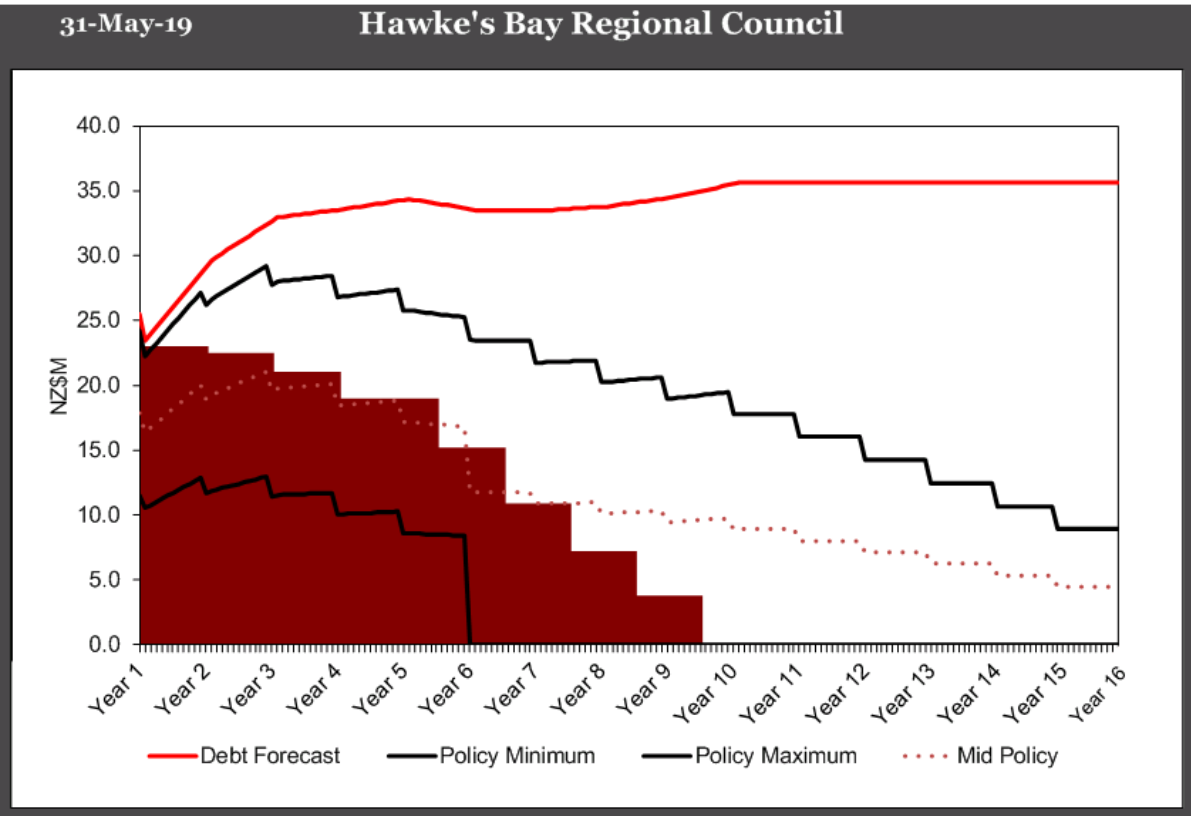
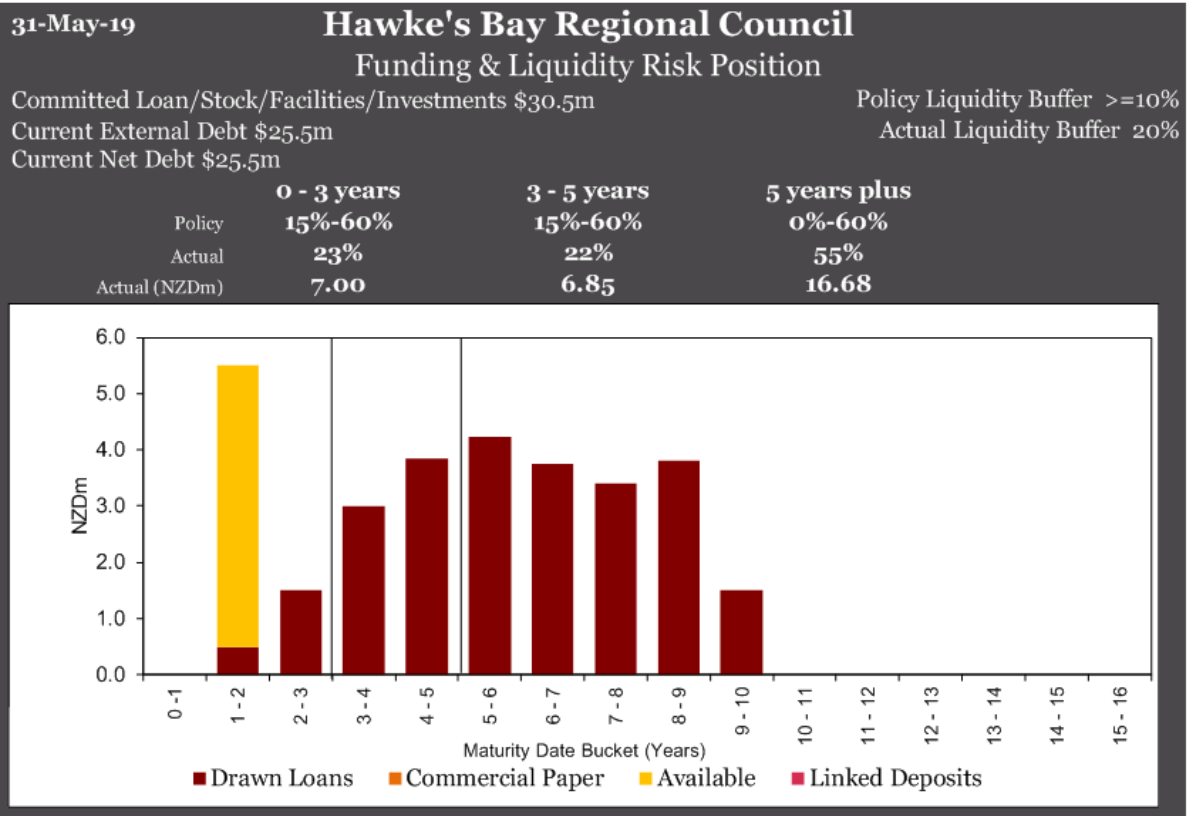
Council's cash flow and debt forecast indicate a requirement for an additional \$2.5 million of core borrowing during this financial year. It is proposed to meet this funding requirement at the 7 May 2019 Local Government Funding Agency (LGFA) bond tender as follows:

- **\$1 million floating rate note** (FRN) with a maturity date of **15 April 2023** at an indicative credit margin of 0.72%.
- **\$1.5 million floating rate note** (FRN) with a maturity date of **15 April 2029** at an indicative credit margin of 1.03%.

Borrowing is being completed on a floating interest rate basis to ensure compliance to the interest rate risk control limits within the Liability Management Policy. The borrowing tenors have been selected in order to strike an appropriate balance between long-term funding cost certainty and concentration risk spreading within funding maturity risk parameters. The resulting funding, liquidity and interest rate risk profiles following implementation of this strategy (as at 31 May 2019) are shown below:

Attachment 1

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Debt Interest Rate Policy Parameters

(calculated on rolling monthly basis)

Debt Period Ending	Debt Forecast	Minimum %	Maximum %	Actual	Compliant (Y/N)
Year 1	26	45%	95%	90%	Yes
Year 2	29	40%	90%	79%	Yes
Year 3	33	35%	85%	69%	Yes
Year 4	34	30%	80%	63%	Yes
Year 5	34	25%	75%	55%	Yes
Year 6	34	0%	70%	45%	Yes
Year 7	33	0%	65%	33%	Yes
Year 8	34	0%	60%	21%	Yes
Year 9	34	0%	55%	11%	Yes
Year 10	36	0%	50%	0%	Yes
Year 11	36	0%	45%	0%	Yes
Year 12	36	0%	40%	0%	Yes
Year 13	36	0%	35%	0%	Yes
Year 14	36	0%	30%	0%	Yes
Year 15	36	0%	25%	0%	Yes

11.0 Appendix**14.1 New Treasury Transactions up to 31 March 2019****Interest Rate Borrower Swaps**

Bank	Notional Amount (NZDm)	Deal Date	Start Date	Maturity Date	Swap Rate
n/a	n/a	n/a	n/a	n/a	n/a

Borrowing activity

Bank/LGFA	Amount (NZDm)	Borrower notes (NZDm)	Deal Date	Start Date	Maturity Date	Commitm ent Fee	Margin
Bank Facility	5.00	N/A	10-Apr- 2019	10-Apr- 2019	15-Jan-21	0.27%	1.10%