Quarterly REPORT

31 March 2014

INVESTMENT MANAGEMENT

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1 Executive summary for Risk and Assurance Committee

1.1 Group overview

Business as usual activities and functions carried out by the Investment Management Group included:

- Investing surplus funds and contingency funds
- Managing GWRC's debt portfolio and interest rate risk, ensuring adequate cash is available, relationships with bankers and rating agencies
- Monitoring CentrePort and the Stadium Trust and completing the WRC Holdings Group Statement of Intent and reporting to its Board
- Managing the Council's Treasury function, interest rate risk and FX risk
- Co-ordinating the Council's risk management, and management of the policy on project management
- Managing and coordinating the Council's Insurance programme.

1.2 Executive Summary

Investment Management has seen interest rates rise at a slower pace than anticipated. This has impacted on our investments which show slightly lower returns. Our borrowings have had limited impact as most of our debt is fixed.

Debt has increased by $8.7 million since the beginning of the year. We are anticipating most of the budgeted borrowing to occur late in the year to pay for the Matangi upgrades. The future Matangi debt interest rate risk has been covered (converted to fixed rate) with 53% of the peak borrowings covered for an average term of about 5 years.

1.3 Key results for the quarter

Further Hedging for Matangi

We completed $25 million of hedging for the quarter in relation to the Matangi bringing the total hedged amount to 53% of the total peak debt requirements.

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1.4 Achievement/s during the quarter

Market rates and hedging – Changes during the quarter

The Official Cash Rate (OCR) moved to 2.75% from 2.50% on 13 March after no change since March 2011. This is the beginning of a series of rate increases forecast for the coming year. The 90 day rate ranged from 2.90% to 3.15%, currently it is at 3.25%.

The 5 year interest rate swap ranged from 4.40% to 4.75% and is currently at 4.60%.

The 10 year swap ranged from 4.77% to 4.90% and is currently at 5.05%.

The price of Singapore Gas oil (Diesel) in NZ Dollars per barrels was:

31 December 12	$151
31 March 13	$142
30 June 13	$155
30 September 13	$144
31 December 13	$154
31 March 14	$140

The price of Diesel in New Zealand dollars decreased over the quarter to around $140 per barrel and is trading at around $142 per Barrel as we write this report, the same level as in March 2013.-

The proportion of Diesel in the index, under which we pay the service providers, is approximately 15%, which leaves us with a relatively small risk exposure.

The valuation of swaps was $965,000 positive (June 2013: -$3.81m negative) in the Council and about $33,000 positive (June 2013: -$260,000 negative) in WRC Holdings (WRCH). The positive valuation is due to our contract swap rates being slightly lower than the equivalent actual market rates. Our average borrowing swap rate per end of March is about 4.83% for the 2013/14 year and 4.80% for the 2014/15 year. The big movement in the valuation reflects the general upward movement in term interest rates, particularly in the last quarter.

During the quarter we entered in the following borrower swaps:

$15 million @ 5.2475% from 15.02.16 to 15.02.20 (4.0 years) with ANZ

$10 million @ 5.4000% from 15.04.16 to 15.10.23 (7.5 years) with BNZ

We continue to look for opportunities to add some additional cover, and remain close to our Treasury Advisors' target levels.

The Council has approved the hedging of the Interest rate risk more than one year out. This is prudent given that our debt levels are forecasted to increase significantly, mainly due to the purchase of the new Matangi 2 trains in the coming years, which are estimated to cost around $175 million. After the contract for the new Matangi trains was signed the interest rates

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moved up significantly. This limited our ability to cover this interest rate risk at levels under our 5% target.

Nevertheless we have now covered $85 million (53%) of the peak $160 million debt requirement. This provides an average hedge rate for the new Matangi trains of 4.89% for a weighted average period of 4.9 years.

We continue to face a number of challenges; firstly, cash flows are uncertain; secondly, there is a large premium to hedge forward and thirdly, the forecasted peak for the 90 day rate is below the current rates we can hedge at.

We were fully compliant with our Treasury Management Policy in March 2014.

Investments

The $33 million liquid deposits were invested during the quarter on average at about 4.34%.

The contingency funds for the Water group, The Flood group and the newly established Property fund collectively amounting to $25.1 million were invested on average at 4.05%, comparing favourably to the 90 day bill rate of around 2.90% over the period.

We have $30 million of short term money market funds invested. These funds are averaging a return of about 4.03% and compares to short term borrowing costs of around 3.21% and is discussed further below.

Debt

The $44 million of WRCH debt was rolled over at a margin of 12 points (0.12%). WRCH received $65 million ($60 million December 2013) in bids and settled with a weighted average interest cost of 3.19% which is $211,000 per annum cheaper than direct bank borrowing.

At the end of March we had $39 million of Commercial Paper issued of which $30 million related to the prefunding of working capital requirements and $9 million related to the share investment into Greater Wellington Rail Limited (GWRL) for the new Matangi trains.

The Gross Debt Level of GWRC (incl. WRCH) per 31 March was $259.4 million (June 2013: $220.7 million). After deducting money market and short term investments, as well as $33 million Liquid Financial Deposits, but not the contingency investments and LGFA borrower notes, the Net Debt is $196.4 million (June 2013:$187.7 million). This is an increase of $8.7 million when compared to 30 June 2013.

This increase was mainly due to funding the new Matangi trains and the old Matangi retrofits, offset by increases in working capital.

Local Government Funding Agency (LGFA)

The LGFA has just completed its nineteenth debt issuances since its inaugural issuance in February 2012.

Appetite for non–sovereign bonds has surged recently. This is most likely due to the “carry trade” where foreign investors borrow cheaply in low interest rate currencies and invest in

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New Zealand. They benefit from a significant yield pick-up and in many cases enjoy a currency gain as well.

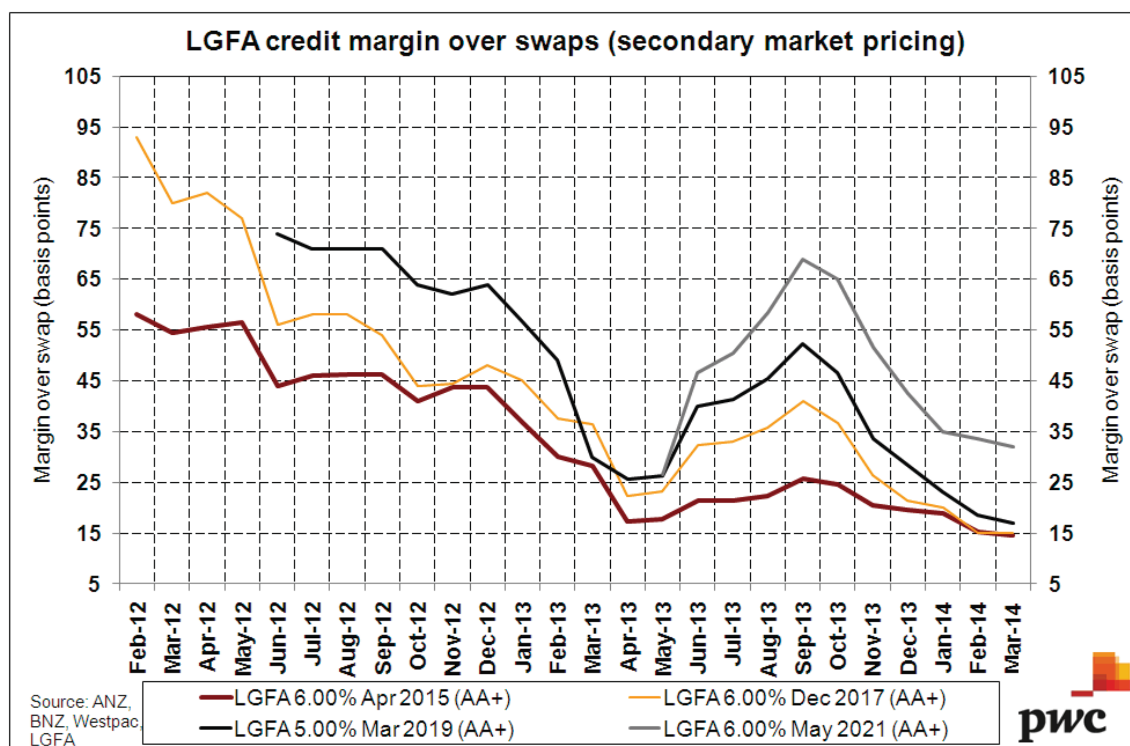
The charts below show how margins had increased but then recovered.

Overseas investors have been specifically targeted and they are beginning to have a greater share of the LGFA bonds.

The greater the volume of bonds on issues the more attractive the LGFA becomes to these investors. Overseas investors will assist with reducing the LFGA margin as it is seen as very close to Government risk, with quite a large premium.

The second chart shows a narrowing of the credit margins between bank lending (green) and the LGFA (grey). This makes the bank more competitive.

We recently completed a paper for the Shareholders Council, about the LGFA and the need for the LGFA to become more borrower focused now that it has become well established. The topics covered include the Number of maturities offered by the LGFA, Refinancing of the sectors debt, the LGFA offering Promissory notes (Commercial Paper) and Tenders.



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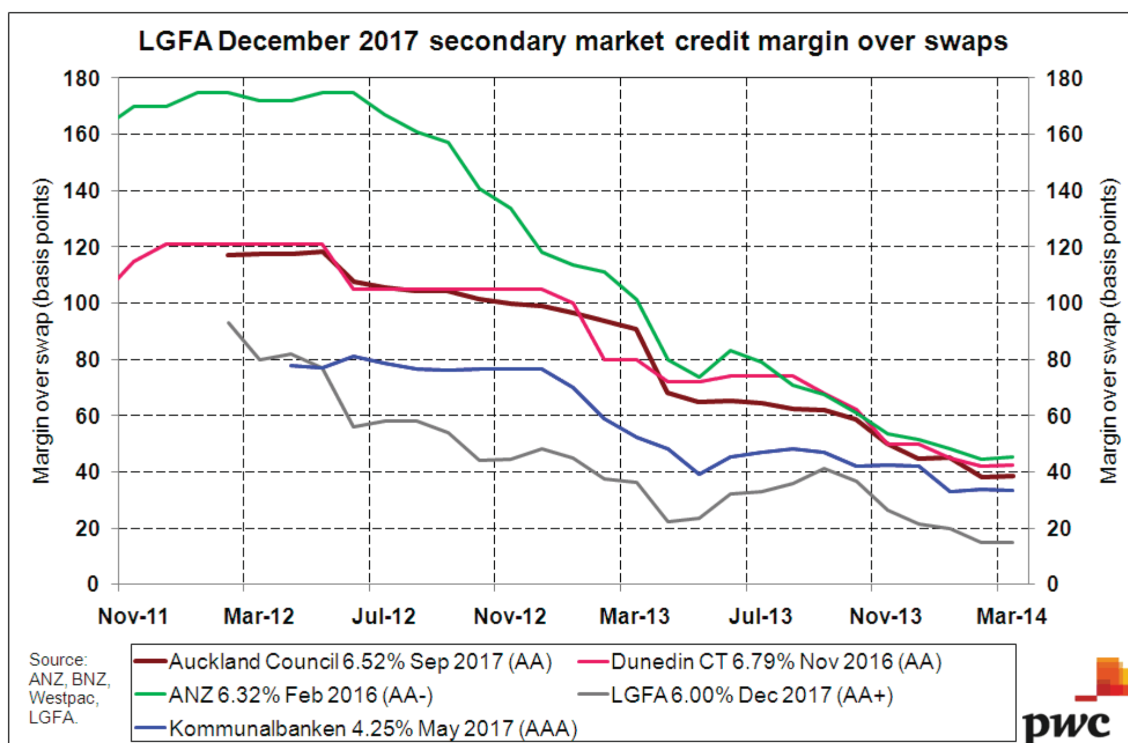

Insurance

Local Government New Zealand is progressing work with a sector approach to potentially buying insurance collectively and dealing with related issues such as Government support, and risk management strategies around a seismic response. GWRC is keen to be part of this working group.

We began a review of our liability insurance cover and the first step in this process is to collect information on the clauses we have in our contracts.

There is concern that some contractual clauses may limit our ability and our insurers to sue and for us to be covered under our liability policy.

Once we have collected this information we will work with our broker Aon to review and possibly reword our Insurance policy to better respond to any claim we might make.

We have just begun the annual insurance renewal process, which involves completing the insurance proposals, updating our valuations and collecting various bits of data to provide to our insurers.

Risk Management

The Council's risks were presented to ELT in late March for review, with a view to modify them and provide a consistent approach. The Chief Executive and the Treasurer have worked up an updated format which will incorporate the 11 new risk categories into the current reporting template.

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Project Management

The groups are now reporting projects with their quarterly reporting through to the Chief Executive. Work is being progressed towards receiving the post project reviews at the next quarterly round of reporting.

Subsidiary companies

A letter of reply to CentrePort has been sent to them in relation to their draft Statement of Intent (SOI). The letter addressed the separation of the Property and Port functions which our Directors were keen to see more of. The dividend was raised and while it could be accommodated relatively easily within existing financial covenants it was noted that the Board of CentrePort had also reduced their capital expenditure programme and was suffering from expenditure shocks from the Seddon Earthquakes. It was noted that a dividend was important and the Council’s expectation was that it be the maximum practical amount given the anticipated business needs.

1.5 Looking ahead

The next quarters will continue to focus on raising further debt and managing our interest rate risk.

2 GROUP FINANCIAL SUMMARY

2.1 Financial summary to date

Investment Management is showing a $9.7 million surplus, which is $70,000 unfavourable to budget.

Total income is $784,000 favourable to budget, mainly due $1,488,000 higher interest revenue from investments which is offset by $704,000 lower interest revenue from internal loans.

Total direct expenditure is $159,000 above budget which is mainly due to higher expenditure for contractors and consultants.

Total indirect expenditure was $695,000 above budget with finance costs being $666,000 higher than budget due to the prefunding of debt.

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2.2 Group consolidated financial statements

Investment Management Income Statement 9 months ending 31 March 2014	YTD as at 31 March Actual $000	 Budget $000	 Variance $000	Full Year Forecast $000	 Budget $000	 Variance $000	Last Year YTD Actual $000	 FY Actual $000
Rates & Levies	2,007	2,007	-	2,676	2,676	-	2,007	2,676
Investment Revenue	5,263	3,775	1,488	6,035	4,378	1,658	4,371	5,106
Internal Debt Interest Recovery	10,374	11,077	(704)	14,119	14,770	(651)	10,667	14,532
Internal Revenue	455	455	(0)	607	607	-	154	206
TOTAL INCOME	**18,099**	**17,315**	**784**	**23,437**	**22,430**	**1,007**	**17,199**	**22,520**
Materials,Supplies & Services	63	99	36	119	137	18	62	88
Travel & Transport Costs	0	0	-	0	0	-	0	0
Contractor & Consultants	332	137	(195)	462	183	(279)	149	212
Internal Charges	304	304	-	406	406	0	301	402
Total Direct Expenditure	**700**	**541**	**(159)**	**987**	**726**	**(261)**	**513**	**703**
External Finance Costs	6,984	6,319	(666)	9,516	8,750	(766)	5,820	7,921
Bad Debts	0	0	-	0	0	-	0	0
Internal Reserve Investment Cost	688	623	(65)	931	831	(100)	766	1,044
Depreciation	16	52	36	69	69	(0)	18	24
Loss(Gain) on Assets / Investments	0	0	-	0	0	-	(29)	(29)
Total Indirect Expenditure	**7,689**	**6,994**	**(695)**	**10,516**	**9,650**	**(866)**	**6,574**	**8,960**
TOTAL OPERATING EXPENDITURE	**8,389**	**7,535**	**(854)**	**11,503**	**10,377**	**(1,127)**	**7,087**	**9,663**
OPERATING SURPLUS/(DEFICIT)	**9,710**	**9,780**	**(70)**	**11,934**	**12,053**	**(120)**	**10,112**	**12,857**
Unrealised Revaluation Gains / (Loss)	0	0	-	735	735	-	0	4,712
Grants and Subsidies - Revenue	0	0	-	0	0	-	(2)	8,531
Surplus / (Deficit) after non operating items	**9,710**	**9,780**	**(70)**	**12,668**	**12,788**	**(120)**	**10,110**	**26,100**

Investment Management Capital Expenditure Statement For the 9 months ending 31 March 2014	YTD as at 31 December Actual $000	 Budget $000	 Variance $000	Full Year Forecast $000	 Budget $000	 Variance $000	Last Year YTD Actual $000	 FY Actual $000
Total Asset Acquisitions	-	-	-	-	-	-	-	-
Capital Project Expenditure	2,237	2,500	263	2,438	2,500	62	259	309
Asset Disposal Cash Proceeds	-	-	-	-	-	-	-	-
Net Capital Expenditure	**2,237**	**2,500**	**263**	**2,438**	**2,500**	**62**	**259**	**309**

2.3 Departmental financial summary and variance analysis

Total income is $784,000 favourable to budget, which is mainly due to $1.5 million higher interest revenue from investments. This is offset by $704,000 lower interest revenue from internal loans due to slower capex spending.

Investment Revenue is $1.49 million favourable to budget. This is mainly due to $1.08 million higher interest on money market investments as we received more interest due to the prefunded debt. Revenue from the guarantee fee for CentrePort's debt is $72,000 higher than budget as the Facility limit, on which the guarantee is calculated, has increased by $25 million since the budget was set. We received a $266,000 unbudgeted subvention payment from Pringle House which relates to the last financial year. Investment revenue (in the budget & actual) includes a dividend of $2.3 million from WRC Holdings Ltd which was declared post June 2013. No further dividend is forecasted or budgeted for this financial year.

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Total direct expenditure is $159,000 unfavourable to budget, mainly due to $195,000 higher expenditure for contractors and consultants emanating from moving costs relating to shed 39, offset by $36,000 of various other costs.

Total indirect expenditure is $695,000 unfavourable to budget. External finance costs are the main contributor at $666,000 unfavourable to budget. This is made up of interest expenditure on external debt being $566,000 above budget, mainly as a result of prefunding of debt. The costs for our swaps are $108,000 above budget due to actual lower floating rates compared to higher fixed rate swap rates.

Internal Reserve Investment costs where Treasury pays the business interest on its reserve funds were $65,000 unfavourable to budget due to the reserve opening balance and transfers to reserves being higher than budgeted.

As a result of the above variances the operating surplus before non-operating items is $70,000 below the budgeted amount of $9.8 million.

Capital expenditure, all relating to Shed 39, is $2.2 million for the year to date, which is $263,000 unfavourable to budget. This favourable variance results from the timing of payments relating to the work on shed 39.

2.4 Forecast

The forecast is for a year end surplus of $12.67 million which is $120,000 unfavourable to budget of $12.79 million.

Total Income is forecasted to be $1.0 million above budget, with Investment Revenue forecasted to be higher by $1.66 million, offset by $651,000 lower interest revenue from internal loans due to the timing of capital expenditure and overall lower Capex by the Council.

Investment Revenue is forecasted to be $1.66 million favourable. This is mainly due to $1.34 million higher interest revenue from term deposits resulting from prefunding debt and investing the proceeds. The guarantee fee from CentrePort is expected to be $98,000 more due to higher borrowings by CPL (which the fee is calculated on). We received a $266,000 unbudgeted subvention payment from Pringle House which relates to last financial year. This is offset by lower returns on our $33m contingency funds due to lower interest rates compared to budget.

Internal Debt Interest Recovery is forecasted to be $651,000 unfavourable to budget due to lower forecast capex spend from the business units and is offset by equal lower interest costs in the business units. Large capital expenditure costs are expected to happen just before year end, and therefore reducing the internal loan interest income significantly as an even expenditure pattern is the underlying assumption in the budget.

Total Direct Expenditure is forecasted to be $261,000 above budget. This is predominantly due to costs relating to the unscheduled move after the first earthquake and the final move to shed 39.

Finance costs are forecasted to be $766,000 unfavourable to budget, mainly due to the prefunding of debt. This is offset by lower levels of borrowing due to slower capex spend by the business.

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Internal Reserve Investment costs are adverse to budget by $100,000 due to a higher opening balance of Reserves at 30 June 2013 than budget, consequently Investment management pays more interest to the business.

3 KEY PERFORMANCE INDICATORS

3.1 Key performance indicators as at 31 March 2014

See attachment 1.

The financial covenants of the LGFA and those in our Treasury Management Policy are as follows:

- Net Interest Expense / Total Revenue < 20%
- Net Debt / Total Revenue < 250%
- Net interest / Annual Rates and Levies < 30%

As per 31 March we were fully compliant in all three ratios, with ample head room.

Fixed Rate Debt Maturity profile

At the end of March we are fully compliant with our Treasury Risk Management Policy. In terms of the policy we are required to have a spread of maturities for our fixed rate debt and swaps. The one to three year maturity band has 18% maturing, which is slightly above the minimum of 15% required by the policy. In the three to five year band 32% mature, which is within the 15% - 60% range of policy. After five years 50% of all fixed debt and swaps mature, this is inside the 0% to 60% range set by the policy.

Our fixed/floating fix is now at 94% and compares favourably with a policy maximum of 95%.

Net External debt per Capita and Net External Debt / Rates & Levies

Although not required under the Treasury Management Policy, we continued to calculate these ratios. The net external debt per capita is $255, which is $12 higher than in June. The “Net External Debt / Rates & Levies” ratio stayed reasonably unchanged at 104.5% when compared 101.9% at the end of June 2013.

Historical benchmark rate by APRM – no margin

The APRM benchmark rate increased slightly from 3.99% to 4.06% during the quarter, an upward movement of 0.07%. During the same period the Council's cost of funds increased by 0.23% from 3.90% to 4.13%, mainly due to the OCR having been increased by 0.25% and by having a lower proportion of CP debt.

3.2 Historic key performance indicators

See attachment 2.

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Key Performance Indicators
As at 31 March 2014

	Benchmark/ Limits Per TMP.	Actual Mar-14	Actual Dec-13	Actual Nov-13	Actual Oct-13	Actual Sep-13	Actual Aug-13	Actual Jul-13	Actual Jun-13	Actual Mar-13	Actual Dec-12	Actual Sep-12	Benchmark/ Limits Per TMP up to 30.06.12	Actual Jun-12	Actual Jun-11	Actual Jun-10	Actual Jun-09
Debt - Interest Rate Risk Control limits																	
Fixed net interest rate debt and swaps to the total forecasted debt in 12 month time	**40% - 95%**	94%	90%	91%	93%	95%	96%	94%	85%	84%	69%	74%	**40% - 95%**	76%	69%	83%	102%
Debt - Fixed Rate Maturity Profile Limits																	
1 - 3 years	**15 - 60%**	18%	15%	15%	11%	11%	11%	12%	13%	15%	20%	23%	**15 - 60%**	20%	19%	16%	26%
3 - 5 years	**15 - 60%**	32%	40%	38%	43%	43%	36%	38%	41%	49%	37%	41%	**15 - 60%**	44%	27%	25%	4%
> 5 years	**0 - 60%**	50%	44%	43%	46%	46%	53%	51%	46%	36%	43%	36%	**10 - 60%**	36%	54%	59%	70%
Funding and Liquidity risk																	
0 - 3 years	**15 - 60%**	25%	23%	36%	34%	40%	23%	44%	44%	47%	50%	41%	**10 - 60%**	30%	38%	28%	86%
3 - 5 years	**15 - 60%**	53%	43%	30%	31%	28%	53%	32%	32%	36%	35%	27%	**20 - 60%**	32%	18%	50%	0%
> 5 years	**10 - 60%**	23%	35%	34%	35%	32%	24%	24%	24%	17%	16%	32%	**15 - 60%**	37%	44%	22%	14%
Investing - Repricing liquid financial investments																	
0 - 1 years	**40 - 100%**	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	**40 - 100%**	100%	100%	100%	35%
1 - 3 years	**0 - 60%**	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0 - 60%**	0%	0%	0%	65%
3 - 5 years	**0 - 40%**	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0 - 40%**	0%	0%	0%	0%
5 - 10 years	**0 - 20%**	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0 - 20%**	0%	0%	0%	0%
Borrowing Limit compliance under new treasury policy - starting 01.07.12																	
Net Interest Expense / Total Revenue	< 20%	3%	3%	3%	3%	2%	2%	3%	2%	2%	2%	1%	**n / a**	1%	1%		
Net Debt / Total Revenue	< 250%	57%	55%	58%	54%	60%	59%	52%	55%	47%	47%	33%	**n / a**	18%	14%		
Net interest / Annual rates and levies	< 30%	5%	5%	5%	5%	4%	4%	5%	4%	3%	3%	3%	**n / a**	3%	3%		
Liquidity Ratio	**> 110%**	132%	134%	137%	140%	135%	126%	133%	135%	139%	143%	149%	**> 110%**	152%	162%	139%	163%
Debt ratios under expired treasury policy																	
Net External Debt per Capita	**$400**	$255	$243	$257	$242	$268	$262	$233	$243	$215	$216	$152	**$400**	$113	$85	$104	$88
Net External Debt / Rates & Levies	**210%**	105%	102%	108%	101%	113%	110%	98%	104%	92%	93%	65%	**210%**	50%	39%	48%	41.4%
Net Interest Expense / Rates & Levies	**25%**	5%	5%	5%	5%	4%	4%	5%	4%	3%	3%	3%	**25%**	3%	1%	0.7%	0.8%

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History of Key Performance Indicators

	Benchmark/ Limits Per old TMP	Actual Mar-14	Actual Dec-13	Actual Sep-13	Actual Jun-13	Actual Mar-13	Actual Dec-12	Actual Jun-12	Actual Jun-11	Actual Jun-10	Actual Jun-09	Actual Jun-08	Actual Jun-07	Actual Jun-06	Actual Jun-05	Actual Jun 04	Actual June 03	Actual June 02	Actual June 01	Actual June 00
Core Council																				
Net External Debt per Capita	**$400**	$255	$243	$268	$243	$215	$216	$113	$85	$104	$88	$55	$48	$11	$4	$11	$24	$49	$66	$83
Net External Debt / Rates & Levies	**210%**	105%	102%	113%	104%	92%	93%	50%	39%	48%	41%	27%	26%	5.8%	2.0%	6.5%	13.9%	28.5%	38.8%	56.5%
Net Interest Expense / Rates & Levies	**25%**	4.6%	4.8%	4.0%	3.5%	3.3%	3.1%	2.6%	1.0%	0.7%	0.8%	0.2%	1.1%	0.3%	0.8%	2.4%	3.6%	5.1%	4.9%	7.4%
Average Interest Rate on Debt (WACD) (includes Crown Loans)		4.3%	4.0%	4.1%	4.3%	4.1%	4.1%	4.5%	4.8%	4.6%	4.6%	6.0%	7.1%	7.5%	7.5%	7.2%	7.3%	7.7%	7.8%	7.8%

3.3 Project Report

There are no projects to report in Treasury.

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