



# **Waitomo District Council**

## **2018-28**

# **Financial Strategy**

# TABLE OF CONTENTS

<b>1.0 Purpose .....</b>	<b>3</b>
1.1 Guiding principles .....	3
<b>2.0 Strategic Considerations.....</b>	<b>3</b>
2.1 Population and land use changes .....	3
2.2 External Influencers .....	4
2.3 Infrastructure Strategy .....	4
2.4 Maintaining and delivering services (Levels of service) and affordability.	6
2.5 Revenue Streams.....	8
<b>3.0 Council’s planned financial future.....</b>	<b>8</b>
3.1 Rates .....	8
3.2 Balanced Budget.....	11
3.3 Borrowing .....	12
3.4 Debt Reduction.....	15
<b>4.0 Council’s policies on giving securities on its borrowing .....</b>	<b>17</b>
4.1 Financial investments and equity securities .....	17

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Responsibility	<b>Corporate Services Group</b>

## 1.0 Purpose

The purpose of the Financial Strategy (FS) is to set out Council's strategic financial direction over the horizon of the 2018-28 Long Term Plan (LTP) period and how it plans to manage its financial performance over this ten year period. The financial strategy provides some defined parameters to guide the Council in its planned journey.

The FS is an essential element of the LTP. Council must be financially sustainable to continue delivering quality services while keeping rates affordable, ensuring equity between current and future generations and sharing the costs of services across users in a fair and equitable manner.

This financial strategy is designed to provide an understanding the main factors influencing the cost and demand for Council services, the financial challenges Council is likely to face and Council's proposed financial direction.

### 1.1 Guiding principles

The Financial Strategy needs to consider financial health and robustness, the requirements of moving towards Council's vision and the needs of the community. All of these considerations are important from a sustainability perspective. The guiding principles underpinning the Financial Strategy are that Council will strive to:

- a) Provide amenities, facilities and services to the District community that contribute to and align with Council's vision
- b) Undertake good asset stewardship and management to ensure all community and infrastructure assets are fit for purpose and available for future generations
- c) Maintain affordable rates increases
- d) Ensure financial sustainability - by ensuring that our revenue is sufficient to cover an efficient operating expense base, all funding sources are being used optimally and financial management is prudent

## 2.0 Strategic Considerations

### 2.1 Population and land use changes

Planning Assumptions for the 2018-28 period show that the annualised population of Waitomo District as a whole will decline by -0.3% per year over the 2018-2048 period, from an estimated 9,810 in 2018 to 9,650 in 2028. Regarding the population structure, the district has a similar age profile to the rest of New Zealand. The proportion of people aged over 65 is projected to increase from 13% in 2013 to over 25% in 2048 and the number of people aged between 15 and 64 years of age is projected to decrease. This may have a flow-on effect to the make-up of the work force in the district. Factors such as the aging population contribute to a decline in the average household size, decreasing from around 2.6 residents per household in 2013 to under 2.3 in 2048.

In terms of geographic spread of growth, the Te Kuiti Ward is expected to experience a small growth in dwellings. The population and number of dwellings is projected to grow in the Waitomo Rural Ward. Population and dwelling growth flows through to rating units. The district's rating units are predominantly Residential and Residential Lifestyle, with nearly two thirds of the total rating units falling under these two categories. Therefore, any rating unit growth is heavily dependent on dwelling growth. The number

of Commercial and Industry rating units is projected to increase in Mokauiti, Piopio, and Te Kuiti with no growth elsewhere. No significant land use changes are expected over the 10 year planning horizon.

Population and development projections are important in the context of rating and rates affordability. Whilst a static or declining population does not necessarily translate to a reduction in the number of rateable properties (the number of rateable properties in the Waitomo District has increased despite a declining population) it can impact on a community's ability to pay and affordability concerns which Council will need to carefully manage.

It is also projected that the current pattern of limited subdivision and building development will continue over the 10 year period. Overall there is projected to be little change in demand for Council provided services through population or land use changes.

## **2.2 External Influencers**

It is important to note that projections are an indication of the future characteristics of a population, and are based on an assessment of past trends and assumptions (e.g. fertility, mortality, migration). Projections are models based on input data, available knowledge and expert assumptions. The projections represent only one possible, albeit plausible, future. Demographics and economies are complex systems characterised by multi-scale dynamic feedbacks which cannot be predicted. For this reason, it is not possible to fully quantify the uncertainty associated with the projections. The projected decline in population does not consider other factors that may well influence the future look and feel of the Waitomo Community (like Central Government policy, global and national trends) and the effective delivery of Councils own strategies can and will influence the make-up of the Waitomo Community over time.

Factors such as housing affordability in metropolitan areas, an improved national State Highway network, public transport, central government strategies around regional development and local government's efforts in the provision of networked and community services and community development could well see the smaller regions becoming more desirable places to live and work, in the future. All other factors detailed in the Planning Assumptions for the 2018-28 LTP have been considered in the development of this Financial Strategy.

## **2.3 Infrastructure Strategy**

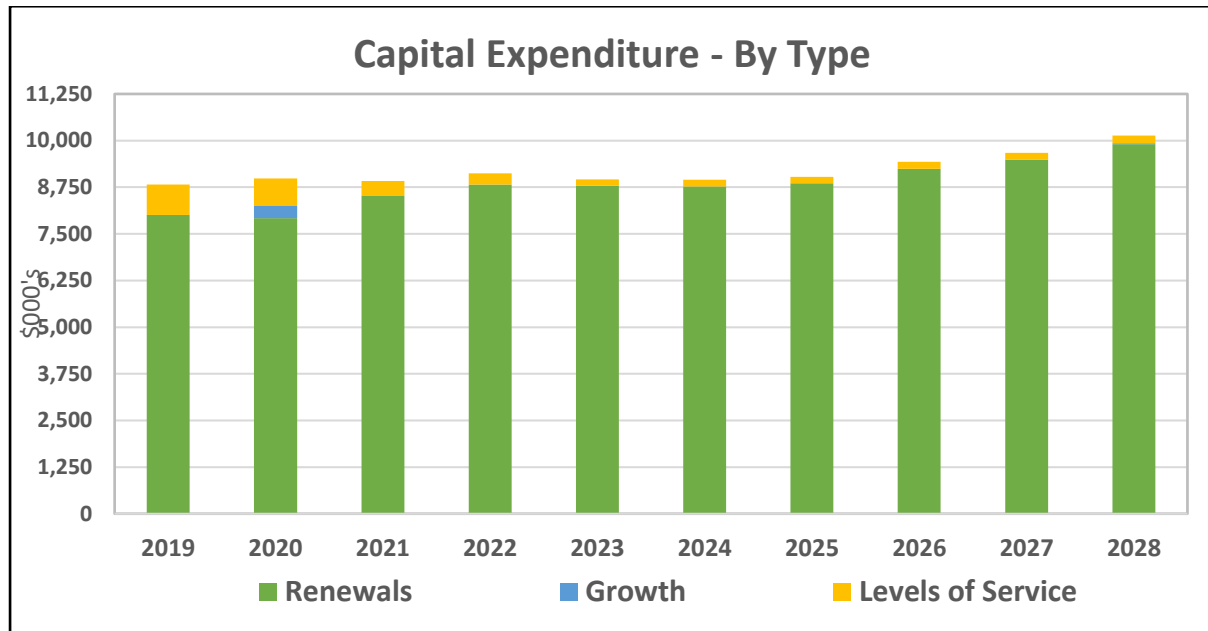
In the last 10 years, Council has made a concerted effort to invest in core infrastructure upgrades where it was essential for reasons of future proofing, for achieving public health outcomes or for reasons of environmental management. As a result, most of Council's core (above ground) assets are now in good condition. Council's piped networks, however (except for the Piopio wastewater scheme and the Benneydale water supply scheme) are characterised by ageing reticulation infrastructure. Long term asset renewal strategies take account of this aspect and respond accordingly.

A planned by-product of Council's investment in its core infrastructure over the past few years is that there is currently enough capacity in the network infrastructure for nominal growth in areas where it should occur.

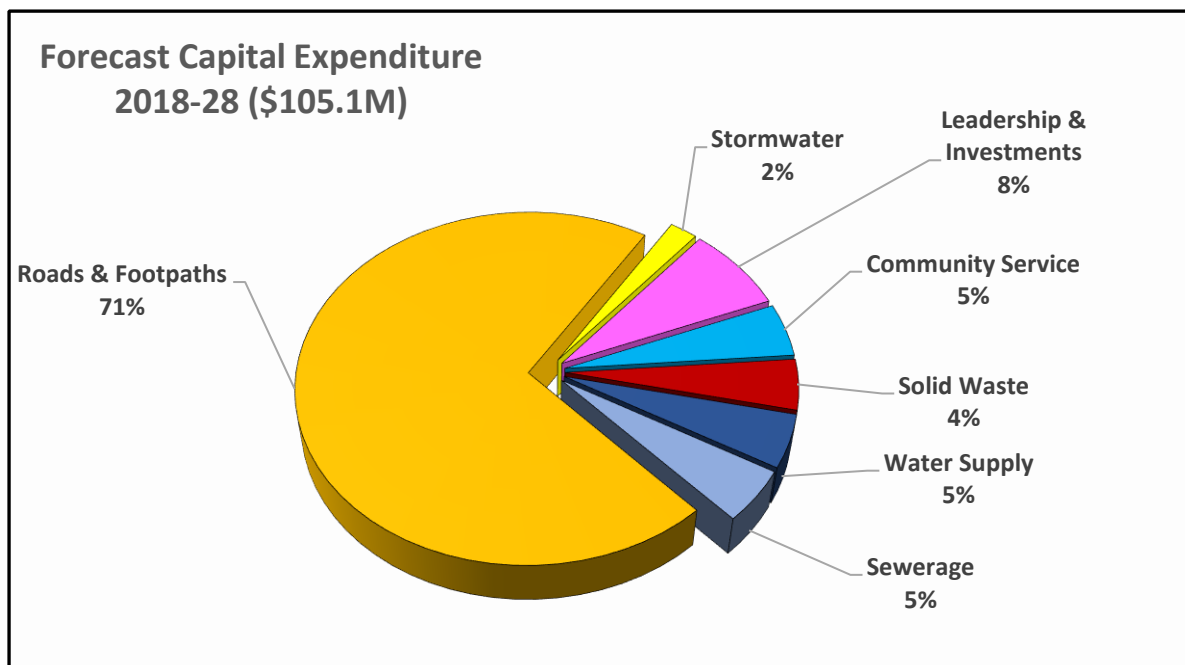
Council's Infrastructure Strategy (IS) covering a planning period of 30 years (2018-48) notes that the focus over the next 30 years for infrastructure is expected to be on maintaining it at current standards. The upgrades required are mostly related to risk mitigation and environmental reasons. The strategy asserts that asset maintenance and

essential elements of prudent asset management will continue to form a vital part of Council's future planning.

The inflated 10 year capital expenditure planned for 2018-28 period includes \$105.1 million (mostly renewals). The following graph differentiates the capital expenditure by the 'drivers'.



Over the 10 years the total planned capital expenditure by activity is shown in the following graph:



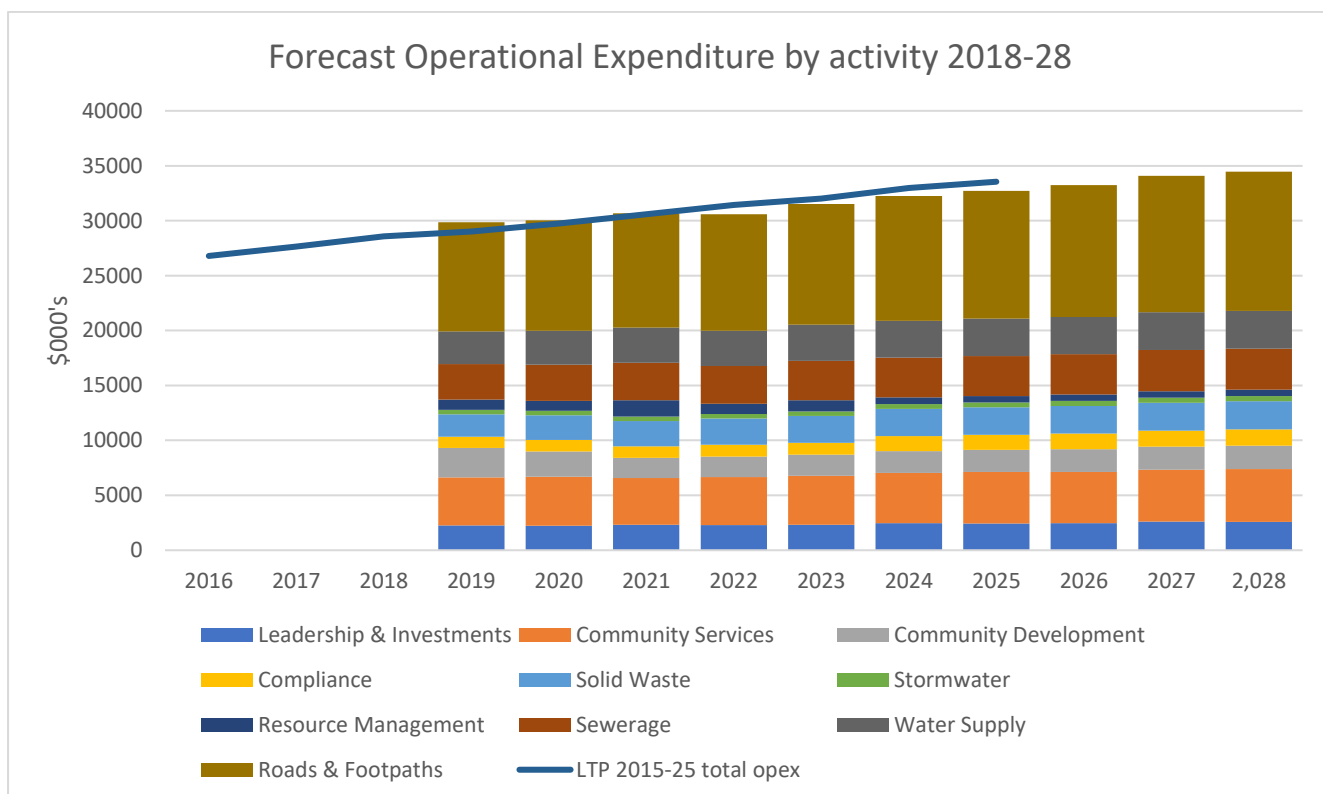
## 2.4 Maintaining and delivering services (Levels of service) and affordability

Council is clear in its vision and wants to invest in place making and place shaping initiatives; in community development and growth opportunities and also wants to deliver services that meet the current needs of the community with an eye to the future. It has been the intention of Council for some time to turn its attention to community well-being aspects and to enhance the 'liveability' of the District, once a stable and sustainable core infrastructure and financial platform was in place.

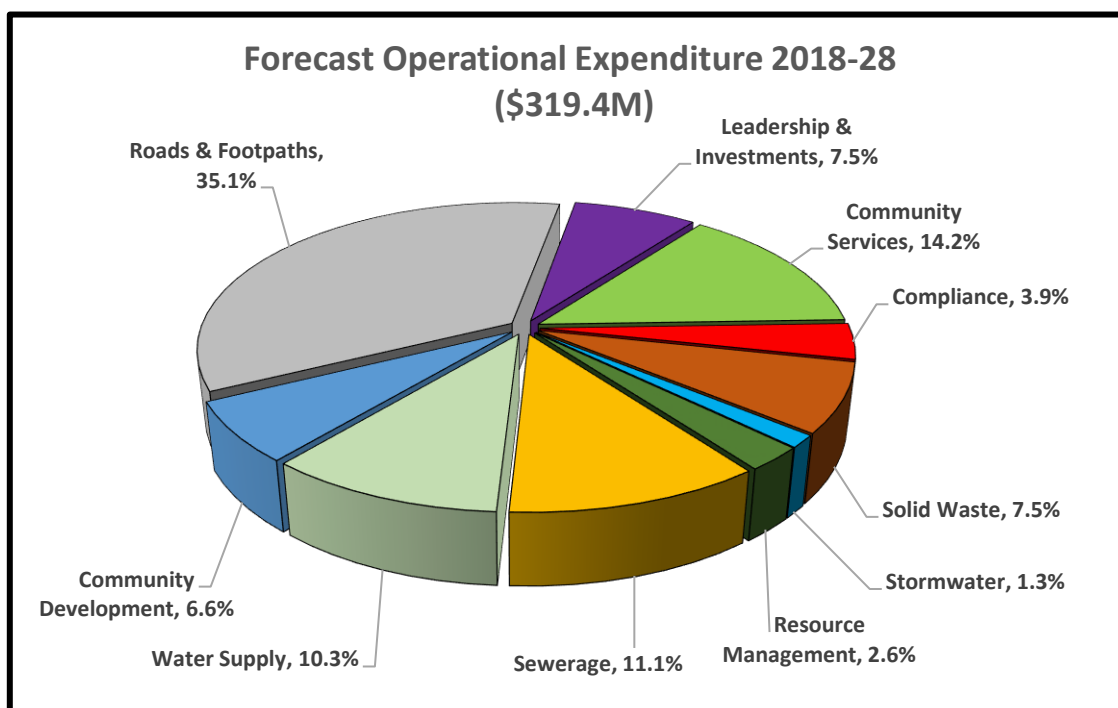
In the 2018-28 LTP, Council is proposing a change to the way it supports the development of the District community. Council proposes to take a partnership approach alongside other key stakeholders in initiatives involving community support and development (Safe Communities initiative).

Council is also clear that all this has to be done in a financially prudent and affordable manner. This is one of the guiding principles that the LTP proposals will be assessed against. Council's view is to take a 'crawl, walk, run' approach in this direction and therefore this realignment does not mean a substantial overall increase in investment in financial terms, it represents the next step in Council's journey and Council intends to make incremental gains.

The following graph shows Council's forecast levels of operating expenditure over the 2018 - 2028 period and compares it with the total operating expenditure forecast in the 2015-25 LTP.



The following graph shows the overall forecast operational expenditure over the 10 years by activity.



The service levels for all other services including core infrastructure is not expected to change over the 2018-28 period. The sealed and unsealed road network (which is the largest expenditure area for Council) is currently in reasonable condition because of current investment in maintenance, rehabilitation and reseals. Current levels of service are a minimum in terms of an effective, efficient, and safe local roading network.

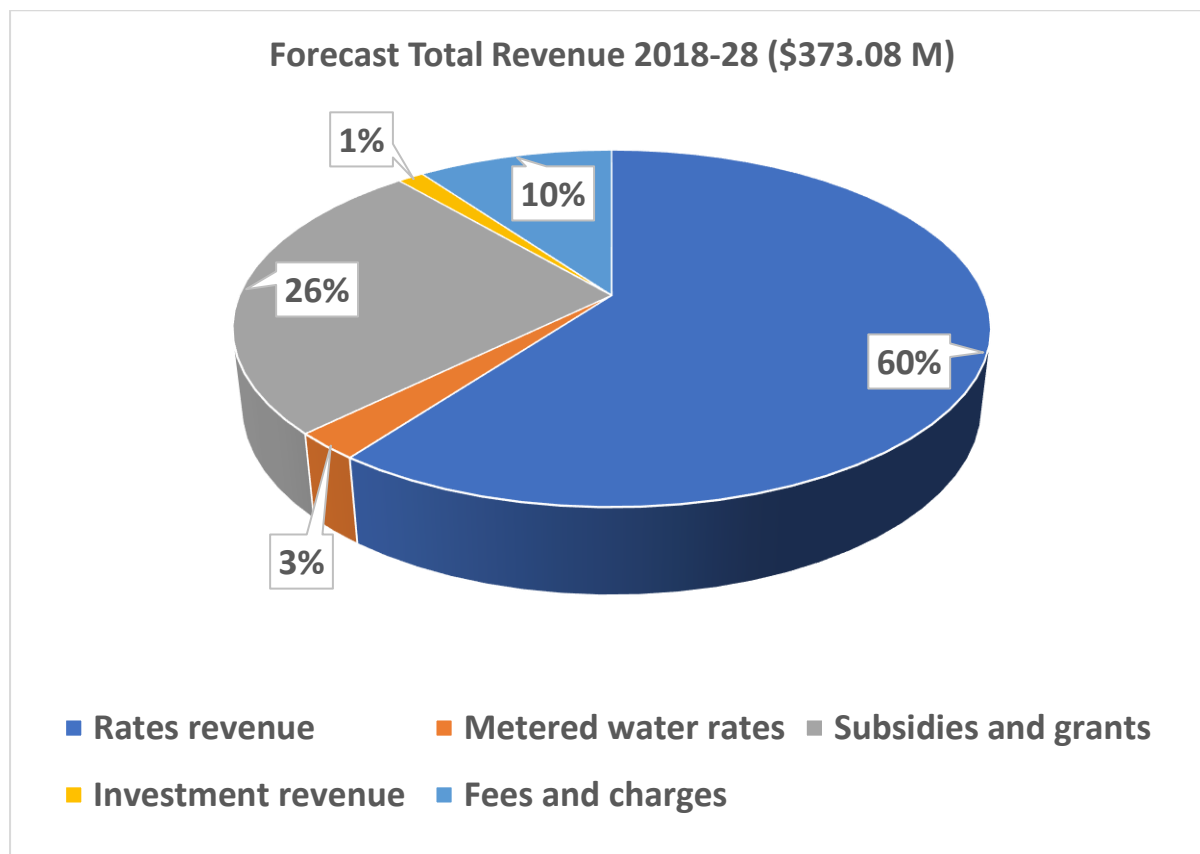
Council has been careful to invest in infrastructure upgrades for Waters where essential to give effect to public health and environmental standards. Whilst a projected decline in population is of concern in terms of affordability, there is little or perhaps no scope to scale back Council's involvement in the provision of this infrastructure. The water supply and sewerage networks have been designed to what can be termed the minimal standards required for a municipal supply in New Zealand under current legislation and regulation.

Many of the other public services provided by Council (particularly in the areas of regulation, resource management and solid waste) are also governed by legislation, regulation, and industry standards and as a result there are limited options for changes to scale and scope in response to changes in population and development.

The provision of community services such as parks and reserves, recreation and culture, community development and other public amenities are the very services that make communities desirable in terms of a place to work, live and play. Throughout the period of this LTP, Council aims to focus on community and economic development to attract more residents and visitors to the District. In short, a retraction or reduction in scope of desirable public services would work against the Council's vision of 'Creating a better future with vibrant communities and thriving business'.

## 2.5 Revenue Streams

The total revenue forecast over the 2018-28 period is \$373.08 million. Sources of funding for the planned services and operations in the 2018-2028 period are shown in the graph below. In the 2018-28 LTP, 60% of the revenue is forecast from rates and 40% from other sources.



## 3.0 Council's planned financial future

### 3.1 Rates

Council recognises the need to keep rates sustainable and increases in rates affordable over time and will endeavour to keep the income required from rates steady. Council's direction for achieving affordability of rates are:

- Limiting the level of rates income to a percentage of operating expenditure
- Managing costs through efficiency gains and increasing other revenue sources e.g. user fees and charges, subsidies
- Specific considerations for funding of depreciation (detailed in the following section)



## Funding of Depreciation

Council funds depreciation to allow for the replacement of Council's capital assets. Over the life of the Long Term Plan we are forecasting \$65.9 million of depreciation. The cost of depreciation is a substantial part of the total rates requirement over the LTP. In keeping with Council's focus on prudent financial management and ensuring that rates are affordable and sustainable, Council will apply the following regarding funding depreciation:

- a) To fund depreciation for Community Halls and Housing for Elderly only to the extent required for minor renewals. This is because Council considers that future renewals would be from community sources and/or grants and subsidies. These facilities are community occupied, have a life in excess of 50 years and renewals would be dependent on future choices.
- b) To defer depreciation or fund only to the level required to meet annual loan repayments on some newly built assets for the first 4-5 years of the asset life and fully recovering that unfunded depreciation over the life of these assets. Council does not intend to build up surplus depreciation reserves in the initial years because of the assets being brand new meaning they have extended lives and low risk of failure. Council has primarily considered this from an affordability perspective for the current ratepayers and considers this fair and equitable since the current ratepayers are carrying the debt servicing costs anyway.

Council considers that the above approach to depreciation is not likely to lead to a deferred burden on future rates caused by deferred depreciation funding as is evident from the forecast rates increase over the LTP (which is consistent).

In making these proposals (pursuant to section 100(2) of the Local Government Act 2002), Council has considered the overall impact of its financial management policies, levels of service and ensured the cash flow is positive over the life of the plan (excluding major projects).

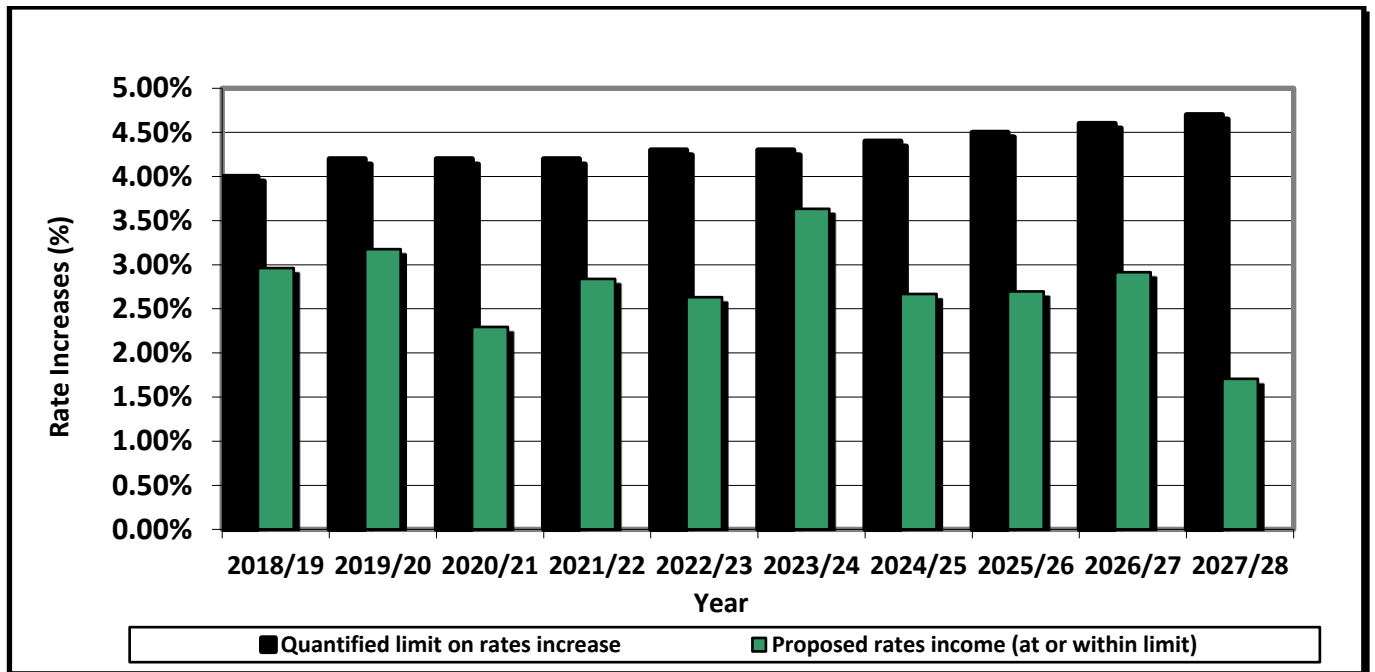
## Limits on Rates

Council has set the following limits on rates revenue and rates increases for the 2018-28 period.

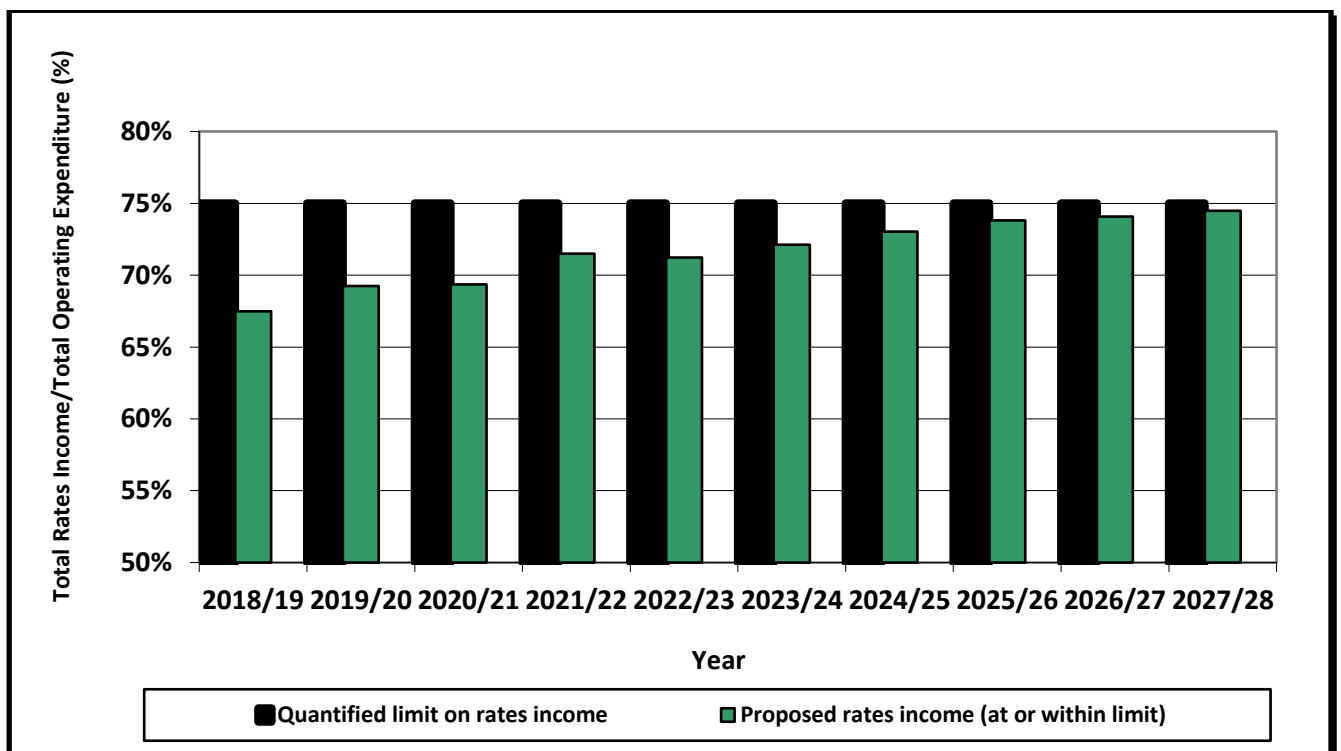
- Rates revenue will be limited to an average of 75% of total operating expenditure
- Rate increases will be limited to no more than forecast LGCI for that year + 2%

The limit on annual rate increases will not apply where there is an increase in the existing level(s) of service (LoS) of any activity in consultation with the community. This exclusion includes unforeseen events that may occur during the period of the plan.

The following graph illustrates the forecast rates increases over the 2018-28 period and tests these against the rates limit set by Council. The graph shows that Council's forecast rate increases are substantially lower than previous forecasts.



The following graph shows the planned total rates revenue is within the quantified limit that total rates revenue will be limited to an average of 75% of total operating expenditure.



## 3.2 Balanced Budget

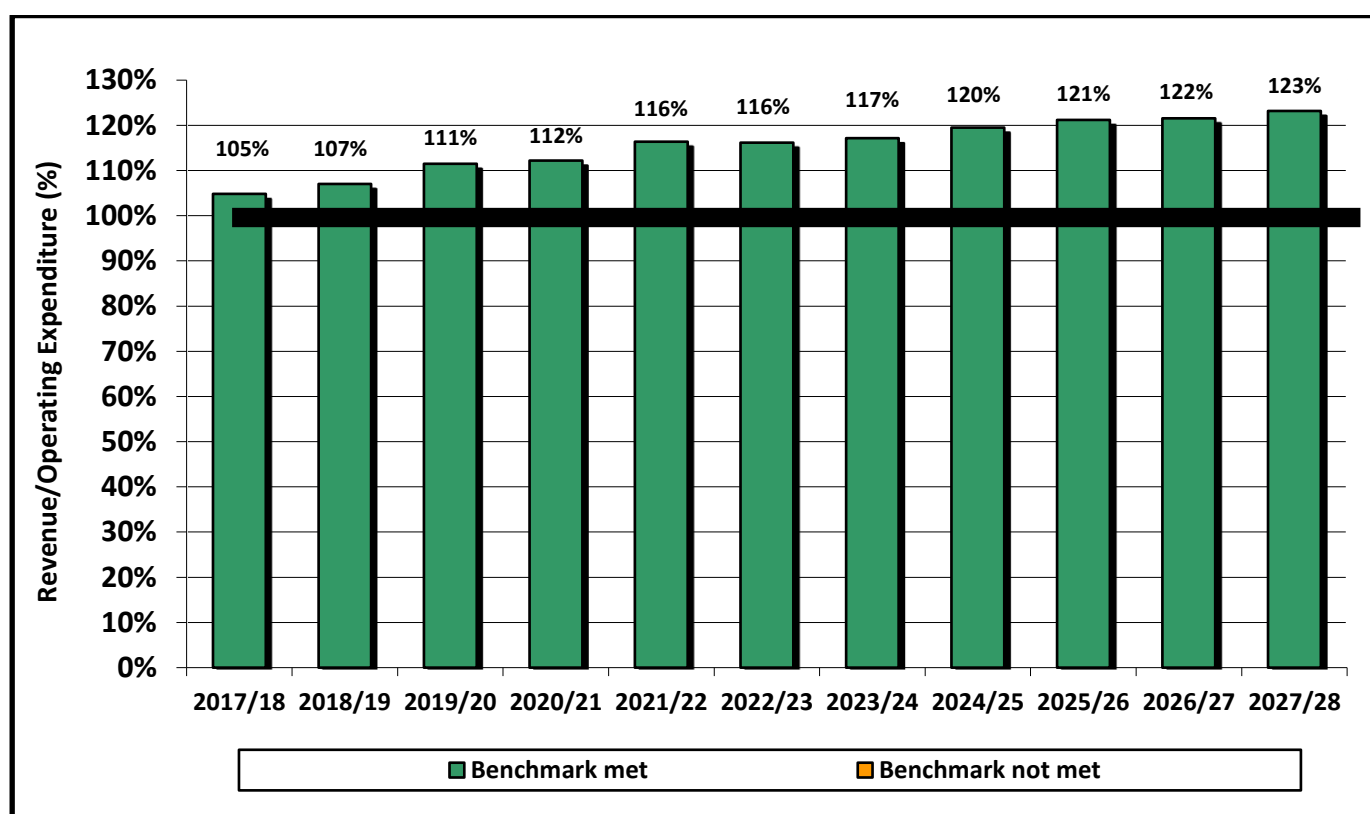
Over the life of the LTP, Council's objective is to set total operating income at a level that meets or is greater than total operating expenditure. This is to ensure that there is access to enough funding to enable the services to continue to be provided long term.

However, there are activities where this approach may not be practical or prudent on a year-by-year basis due to the activity's long term nature, e.g. wastewater, roads and footpaths, water supplies. Over the next ten years Council intends to:

- a) Temporarily run activity deficits/ surpluses in order to avoid large variations in rates increases
- b) Use operational reserves and/or activity balances to fund some specific operational expenditure where appropriate.

Council considers this to be a 'prudent' approach to financial management in that it provides for assets to be maintained and renewed, debt levels kept reasonably conservative, and rate increases limited to an affordable level now and in future.

The following graph illustrates that Council's planned expenditure as a proportion of planned operating expenses has met the balanced budget benchmark as planned revenue is greater than planned operating expenses.



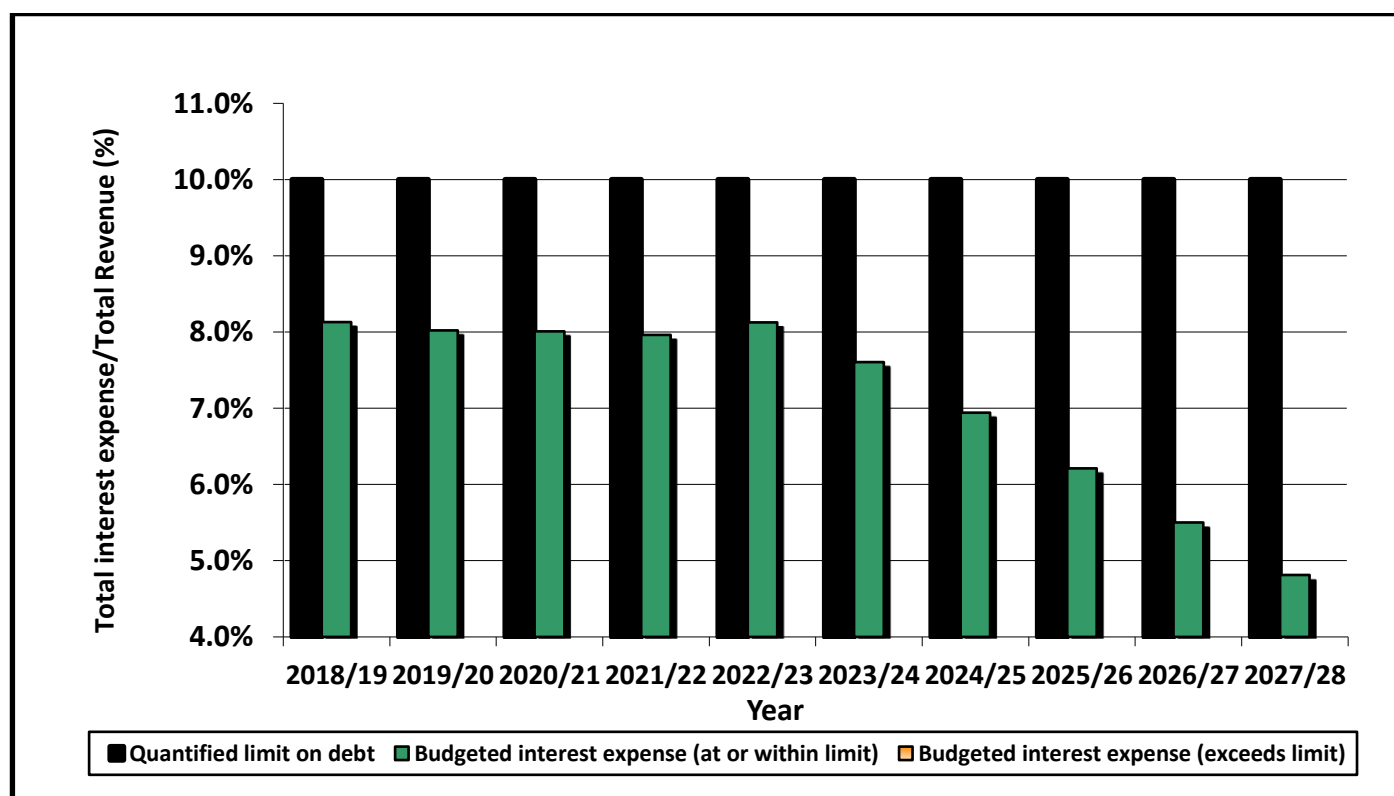
### 3.3 Borrowing

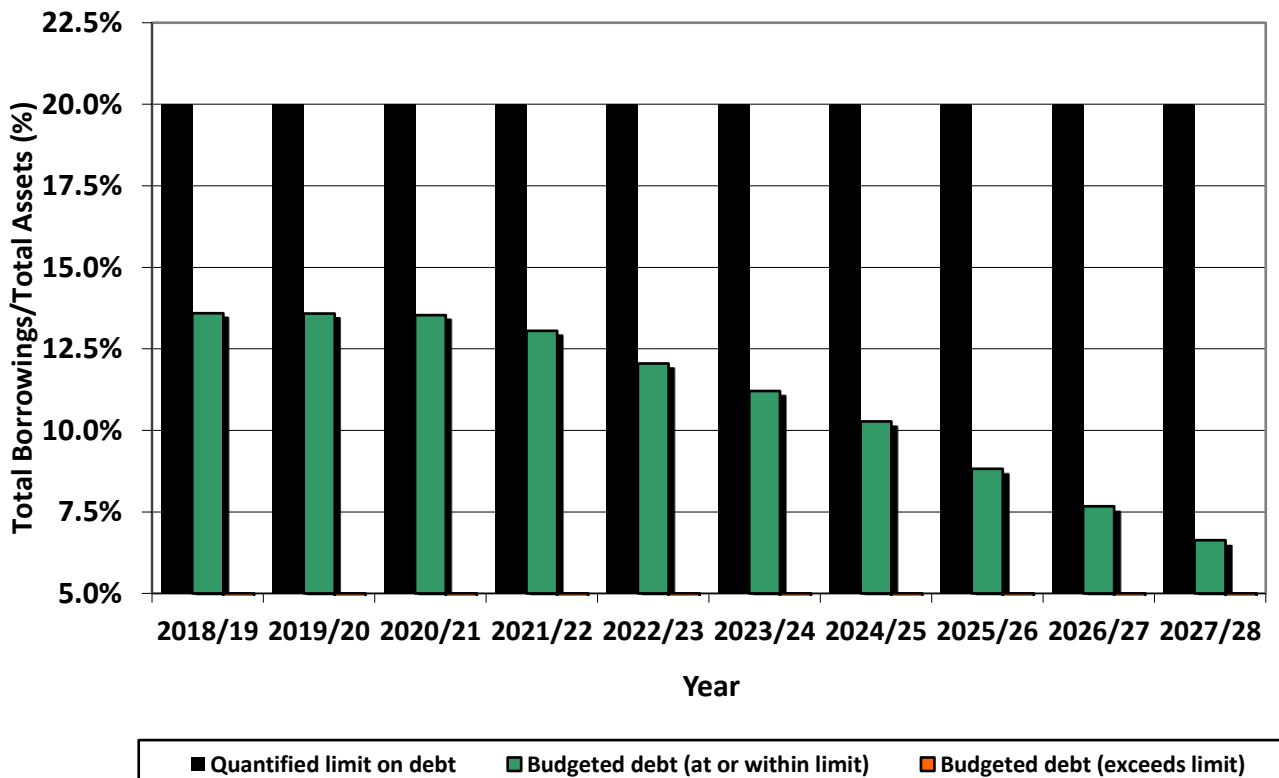
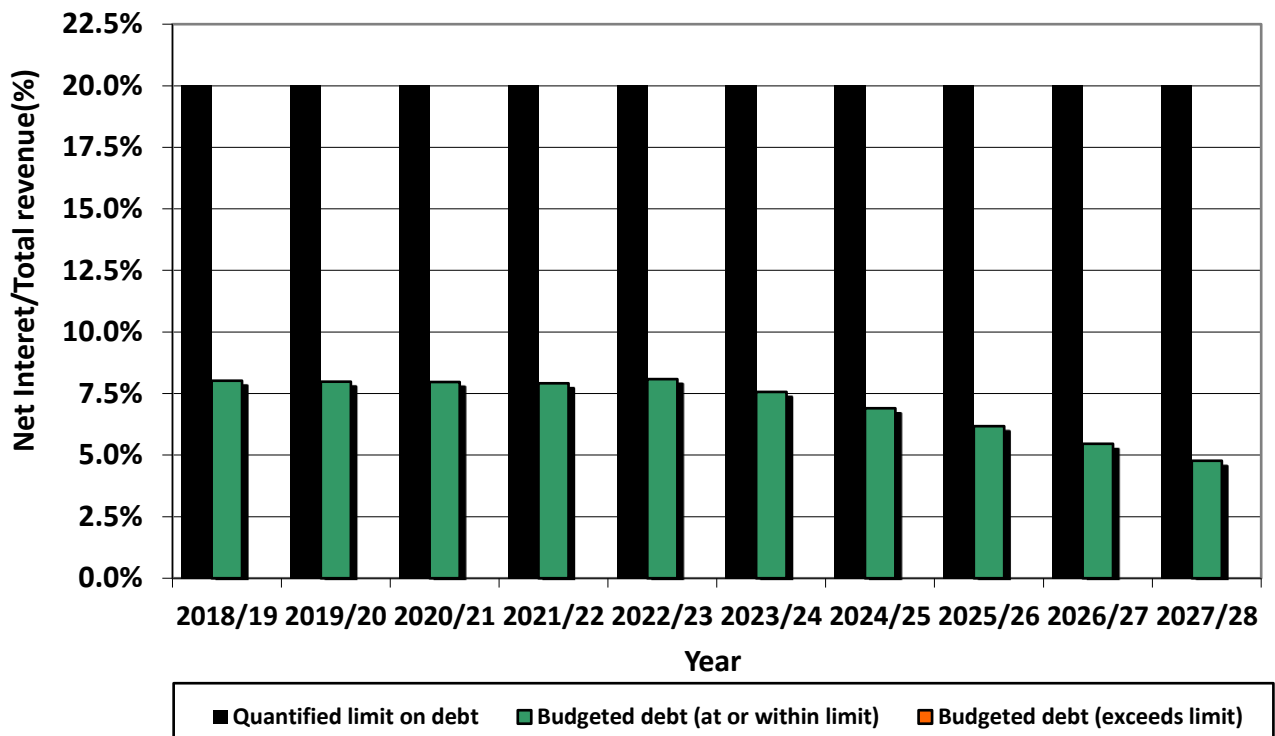
External borrowing (public debt) is used by Council to fund assets or services that will provide benefit well into the future. This is in accordance with the principle of intergenerational equity. However, the use of borrowing has to be prudent and sustainable and limited to the ability to service and repay the debt. Council approves borrowing by resolution through the Annual Plan or the LTP process.

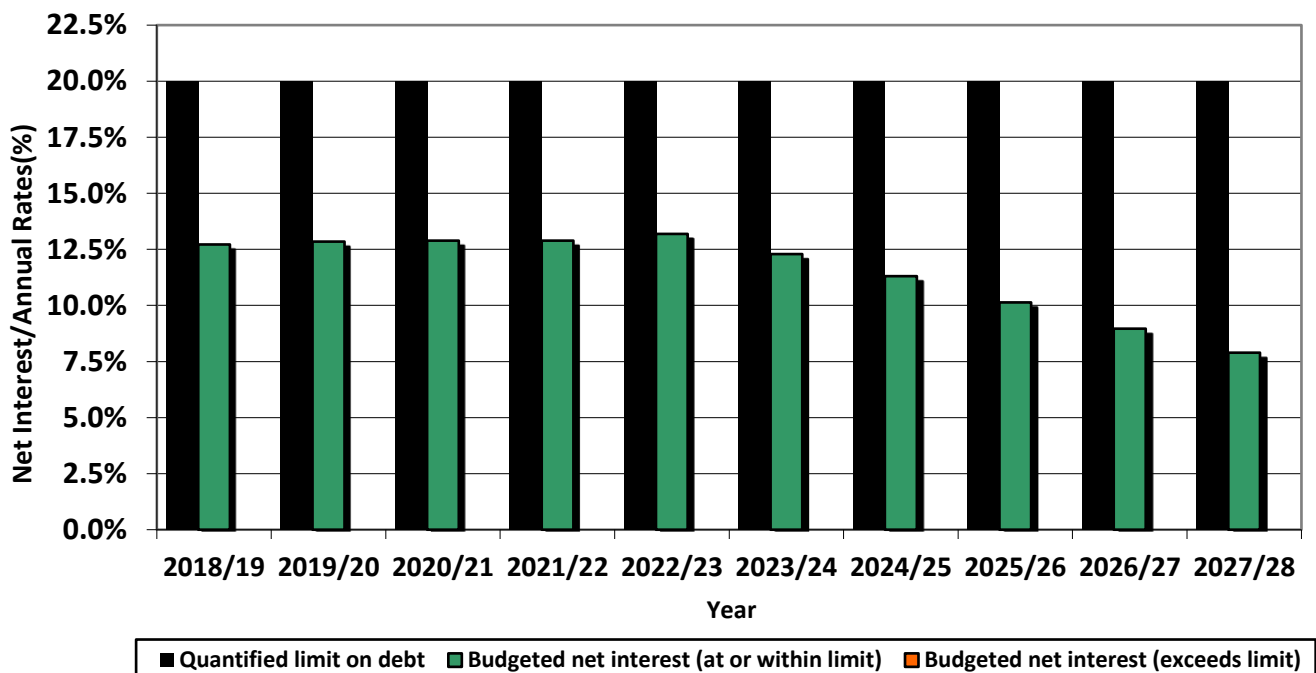
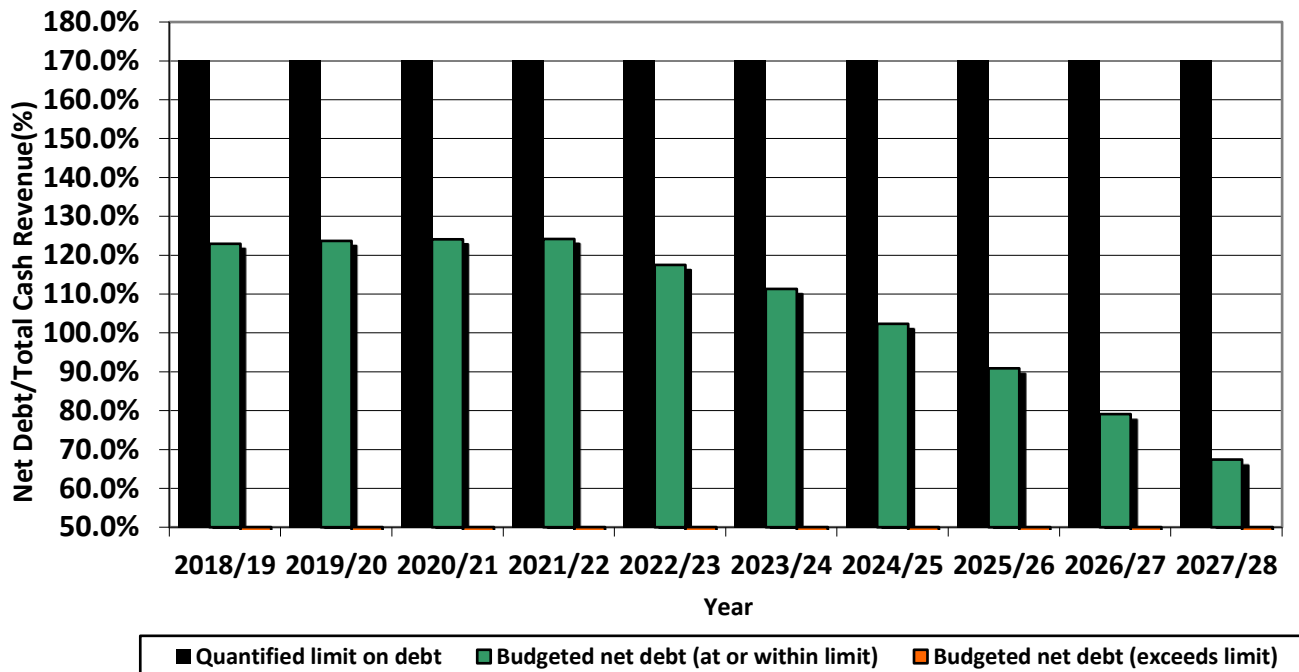
Council recognises the need to manage its finances in a sustainable and affordable manner and has therefore established borrowing parameters to ensure that investment priorities are carefully managed and affordable for the District community. Council has set the **following borrowing limits:**

- Total borrowing costs will not exceed 10% of total revenue
- The ratio of net interest to total revenue will not exceed 20%
- Total borrowings must not exceed 20% of total assets.
- The ratio of net debt to total [cash] revenue will not exceed 170%
- Net interest will not exceed 20% of annual rates

The following graphs illustrate that Council is well within these limits in the 2018-28 period.







### 3.4 Debt Reduction

Council is committed to reducing external debt over the duration of the 2018-28 LTP, in order to reduce the debt servicing burden on the District community and make headroom for investing in increasing the 'liveability' of the Waitomo district.

Council's financial performance has progressed significantly over the last 5-6 years. This is despite a significant investment programme of \$98 million (since 2008) having been undertaken. This has been the result of Council's multi-pronged approach of increasing operating income where possible (particularly from grants and subsidies), improving its reserves balance, efficiency in spending and a focus on reducing cost of borrowing.

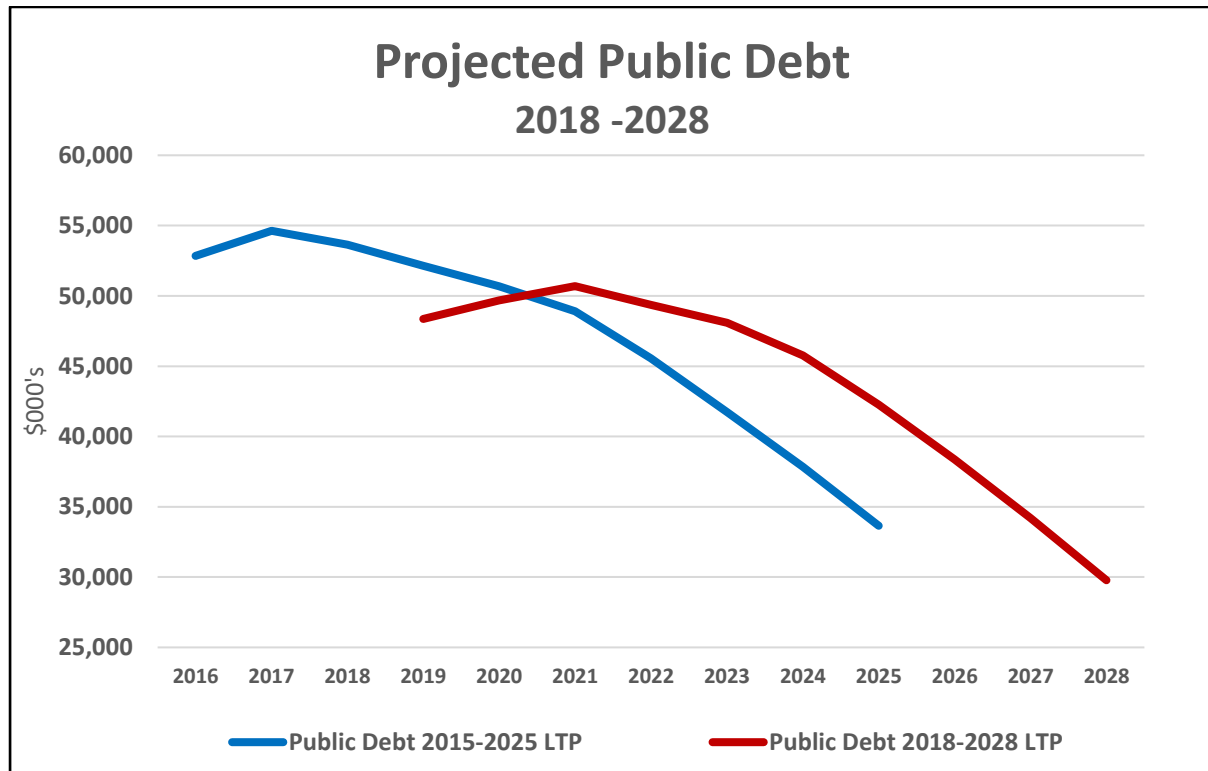
Council became a member of the Local Government Funding Agency (LGFA) in 2016 which is a big endorsement of Council's financial sustainability (Council had not been able to meet the LGFA covenants previously). Joining the LGFA has allowed Council to borrow at much lower interest rates and have easier access to long term borrowing, thereby reducing overall borrowing costs.

Changes to Council's total equity and debt levels is shown in the following table. Since 2012 Council has reduced debt by \$3.6 million and increased equity by \$29.8 million.

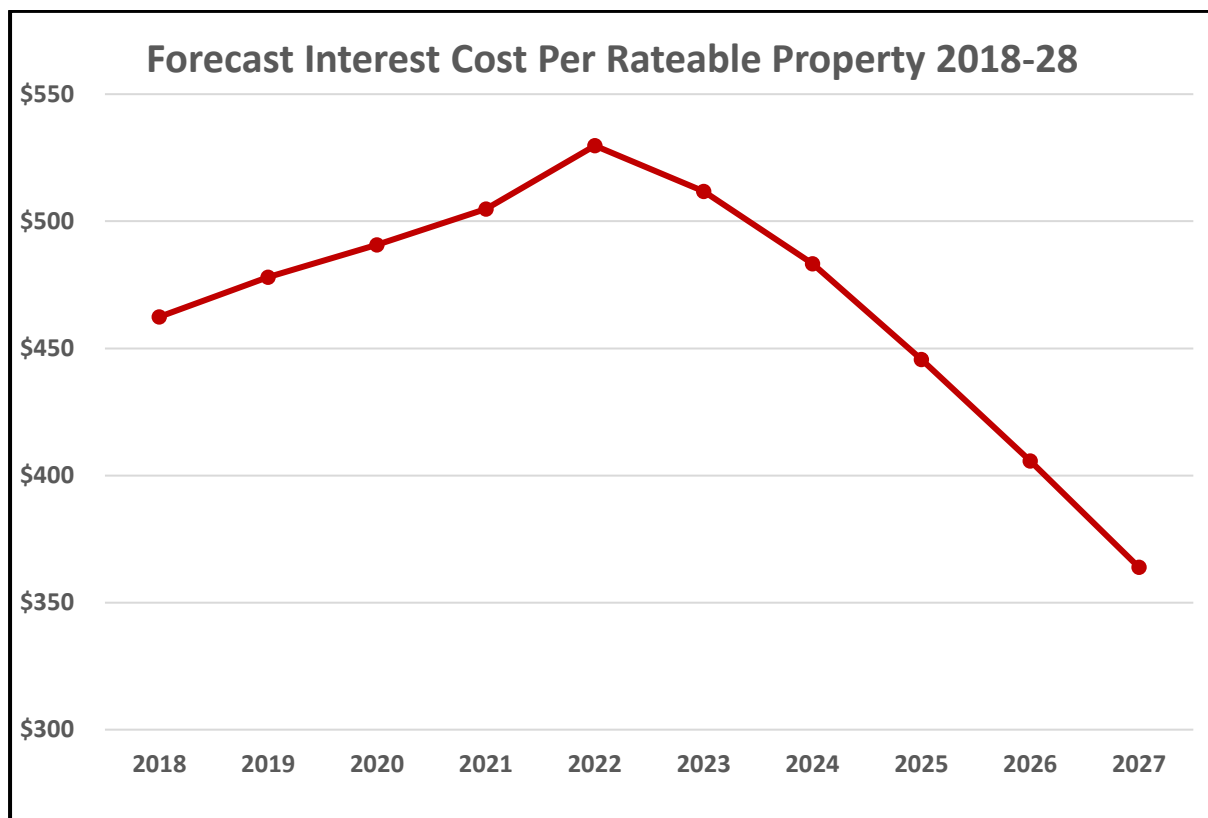
	30 June					
	2012	2013	2014	2015	2016	2017
<b>Actual Public Debt</b>	47,005	45,182	44,865	46,139	44,786	43,419
<b>Decrease</b>		-1,823	-317	1,274	-1,353	-1,367
<b>% Decrease</b>		-3.9%	-0.7%	2.8%	-2.9%	-3.1%
<b>Actual Equity</b>	264,378	270,525	277,412	287,081	289,174	294,190
<b>Increase</b>		6,147	6,887	9,669	2,093	5,016
<b>% Increase</b>		2.3%	2.5%	3.5%	0.7%	1.7%

Over the 2018-28 period Council is proposing to utilise all dividend and/or subvention income from its shareholding investment to repay debt. This income will not be used to offset rates required in any year of the 2018-2028 LTP.

Over the term of the 2018-28 LTP, public debt is forecast to decrease by \$20.9 million from a high of \$50.7 million in 2021 to \$29.8 million in 2028. There is a reduction of 38% over the 10 year period.



The borrowings cost per rateable property are forecast to reduce by 21% over this period from \$462 in 2018 to \$364 in 2028.





## 4.0 Council's policies on giving securities on its borrowing

Council borrowings are secured over annual rates on every rateable property within the Waitomo District as per section 115 of the Local Government Act 2002. From time to time, security may be offered over specific assets with Council approval or infrastructural assets where special rating provisions apply.

Council will not borrow, underwrite or guarantee loans on behalf of any other person, association or organisation except the LGFA for which, under various Deeds and a guarantee and indemnity Council guarantees the indebtedness of the LGFA and other guarantors (a requirement of joining the LGFA) and Council offers deemed rates as security for general borrowing programmes.

The 2008 amendment of the Securities Act 1978 (sections 5A to 5D) enabled Council to issue debt securities to raise funds for Capital Investment. Any issue of debt securities must be approved by Council and will be in compliance with the Securities Act 1978. Securities are not provided for Councils own internal borrowing.

### 4.1 Financial investments and equity securities

Council is a risk adverse entity and therefore takes a prudent approach to managing its investments. Council seeks to achieve an acceptable rate of return on all its investments but recognises that as a responsible local authority any investments that it does hold will be low risk and that generally lower risk means lower returns and also that sometimes investments will need to be held for purposes other than financial returns.

Council's objectives for holding investments or making any new strategic or equity investments Council are/will be (one or all of):

- a) The expected financial return
- b) Contribution of the investment in furthering the Waitomo District's community outcomes as documented in the LTP
- c) How the investment 'fits' within the existing investment portfolio in terms of Council's preference to spread and minimise risk
- d) Contribution towards the good of the local government sector either nationally, regionally or within a sub group of Councils.

The following table lists Council's shareholding investments, the objectives these align with and the target rate of return.

Investment	Objective of Holding Equity	Target rate of return
Inframax Construction Limited	<ul style="list-style-type: none"><li>• Expected financial return</li><li>• Economic benefits like job creation thereby furthering community outcomes</li></ul>	$\geq 7.5\%$
Local Authority Shared Services	To ensure LASS remains viable as a provider of shared services within the Waikato region	0%
Civic Financial Services Ltd	Contribution towards the local government sector	0%