FINANCIAL STRATEGY

DRAFT Effective from 01 July 2021

Prudent Financial Management

Prudent financial management is a legal requirement for Councils. Subpart 3 of the Local Government Act provides for a level of predictability for ratepayers, and highlights the need decisions to be made in the interest of current and future residents.

The major components of a good strategy tie in three key factors:

- Capital expenditure identified to continue to deliver sustainable levels of service. This includes:
  - costs to renew existing assets,
  - to provide for increasing levels of service where desired, and
  - to provide for growth if necessary.
- Borrowing is a rationed resource. Council does not have unlimited borrowing capacity and the ratepayers do not have unlimited resources to pay increasing rates for increased debt servicing.
- Rates are a limited resource. Council must be mindful of the impact rates has on ratepayers. It runs into two limitations. The first is ability to pay, and the second is willingness to pay. Ability to pay is addressed through the government rates rebate, but willingness to pay is harder to define.

Key challenges

Invercargill will be exposed to several challenges over the next ten years. Those challenges include:

1. A demographic change toward an ageing population with less growth than forecast.
2. Growing pressure to recognise climate change effects
3. Significant capital expenditure on existing infrastructure
4. Emerging pressure on higher standards for water, stormwater and Sewage disposal
5. Growing pressure to amalgamate Three Waters into larger service delivery entities
6. Investment in the Inner city
7. Aging Buildings needing significant upgrade or replacement (including Rugby Park, Museum, Civic Administration building among others)

However, acknowledgment of these challenges is the first hurdle to overcome. Commentary on items 1-3 is included below.

For water and sewerage reform, Council has taken an approach of business as usual. The combination of rising standards and amalgamation of waters into separate entities address problem and solution. Council approach to these is that ICC will continue to deliver water and sewerage according to our plans, and that if new entities are formed in the next 3 years as expected, then they will get assets and a revenue base that has been maintained.

Investment in the Inner city and aging buildings has been addressed through the capital work programme.

There are no other factors that are expected to impact on ICC ability to maintain existing levels of service and to meet additional demands for service.

Demographic changes

In the recent past there was a short-term trend for provincial city populations to decrease, leading some commentators to raise the spectre of “ghost towns”. This followed several years of slow decrease in population with an increased drift to major urban centres. In the past 3 years this trend of lower populations and decreasing real estate values has slowly reversed. Invercargill has seen significant lifts in property values and discussions have emerged relating to housing shortages. The recent outbreak of Covid-19 will create significant uncertainty about the near- and medium-term economic outlook and that will flow through to property and population. However, it is too early to determine whether that will be a short term “blip’ in the statistics or move provincial NZ to more growth or more retraction. That trend will take some time to determine, however analysis at this time shows that Invercargill population growth has outstripped recent StatsNZ mid-range forecasts.

While Council will be taking action to influence a positive outcome rather than a negative impact, it is worth reflecting on what the impact of change may be for Council and the community. In relation to growth the city has most of the infrastructure necessary to service a population for most of the growth in the Long Term Plan. We have already identified a need for another water supply to mitigate the risks of a single source of supply. That need would be accelerated if population rises. The costs of an emergency water supply are highlighted in the Water activity. Another effect of growth would be on the volume of sewage outfalls. An increased population may put additional pressure to improve the quality of the outlets for treated sewage, however it is expected that the standards for these will be lifted when the current consents need to be renewed. Increasing population would likely see the current increase in house prices continue, with more houses being built to cope. Subdivision capacity for growth is not unlimited but is able to respond to market demand. New subdivision are responsible for providing all of the infrastructure for new properties (roads, footpath, stormwater pipes and water and sewerage pipes) so the increase for Council is the maintenance of those assets, which is funded from the increased rates. Costs only fall to Council if the major arterials and collector pipes need to be upgraded through growth. This is not envisaged to be a factor in the next 20 years.

Major demographic “shocks” are possible through Central Government reform. Those reforms include:

- Reform of the Southland Institute of Technology will have an uncertain impact on the number of both foreign and NZ students living in Invercargill to complete their studies.
- Increasing likelihood that Water, Sewage disposal and stormwater disposal will be delivered by Central Government.
- Potential future closure of Tiwai point.

These changes are uncertain, and so cannot be planned for. The extent of the change and impact is unknown. However, it takes a significant change to significantly impact on Council services and costs. Also, it takes some time for the community to make decisions and adjust to the change. Council will need to respond to the collective impact of individuals choices.

If population reduces it can have different impacts:

- The same number of properties but a lower average persons per property.

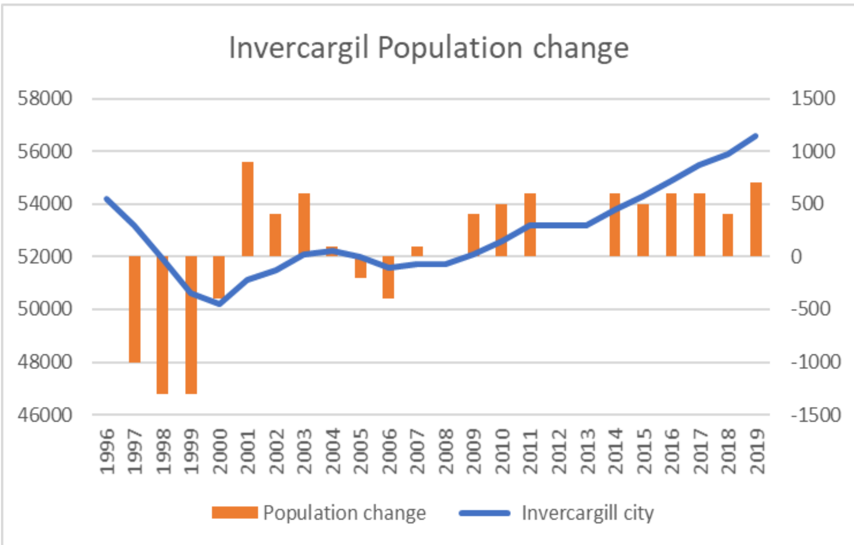
- Sales prices of properties reduce and they take longer to sell. The Market adjusts for these changes.
- Properties are unable to sell and get abandoned, and then subsequently demolished. This has occurred in NZ in past decades but typically in much smaller communities than Invercargill. A trend at this level takes time to emerge and so there is time to manage it if it emerges. Communities need to be mindful of this possibility. The sooner it is identified the better it can be managed.

Due to the significant uncertainty of the current economic outlook, Council is not planning for major changes in population. Our past observation is that the changes in recent year have been both up and down and the impact has been minor.

Changes in the composition of population by age group and ethnicity are also expected to continue. This change is not expected to have a significant change in the services provided by Council, although Council will adapt to these changes as they emerge. Changes may occur in the nature and shape of Council's activity programmes for operating activities. These changes will not be significant and will occur within the current funding envelopes.

One major composition change that may impact significantly is dependent on the economic fall-out from Covid-19. It is expected that this will have a significant impact on unemployment, although how much and where and when that may occur is extremely uncertain. Council will be monitoring unemployment levels for Invercargill/Southland and also other statistics for homelessness and crime. If necessary, Council will change its programme delivery to address these issues. Council expects that if these occur there will be Nation-wide initiatives to help address these. Council will be ready to engage in these for the benefit of Invercargill. Council will also modify its operational programmes if needed.

Information from Statistic NZ shows the population change for Invercargill since 1996. The shape of the blue line indicates why there has been significant change in the Invercargill housing market. After a long period of decline to be below the 1996 population, the population rose to be at a similar level to 1996 in 2015. Steady growth since then has put pressure on existing housing supply. That pressure has built-up and the latest Rating Values show very large rises in residential property values averaging around 50% since 2017.



An increase in population of 500-600 people per annum is around 1%. Our assessment of growth for the LTP has been included at 0.6%. The impact of growth for the City is positive for the next 10 years as it can occur with within the current and planned infrastructure so does not incur additional cost.

There is a consistent theme within the Council's Community Outcomes. The Outcomes demonstrate that the Council will maintain a strong, safe and well- utilised City with an increased, more diverse and active population who encourage the development of future technology and embrace the facilities offered to them.

The Council seeks to encourage this through the development of growth projects and sustainability of existing services. However, it is not anticipated that land use will change to an extent that would have an impact on debt over this course.

With low growth anticipated for the number of properties, the Council notes that the current infrastructure network is set to service the community, provided it is renewed when required. The Council's infrastructure network has been built to service a population much larger than that which currently resides within the City.

The historic pattern of Invercargill growth and development means that a number of the Council's assets were built at the same or a similar time, and therefore generally require renewal at a similar time. As a result there will be peaks in renewal costs which are evident within this Strategy.

Growing pressure of Climate change

Climate change has been noticeable in some forms for a number of years. There is no doubt that the weather patterns have developed more extremities. We are noticing a combination of more storms, with flooding, and more droughts. These higher extremes place more pressure on Council infrastructure services. Higher frequency of storms leads to increased costs on roads to recover from Storm damage, also the flooding frequency could lead to a need to upgrade the capacity of the stormwater network to mitigate flooding of buildings. Droughts create more frequency and longer duration of water peak use, and that puts stress on the current single source of water.

In addition to the weather pattern changes, rising sea levels are a future concern. Invercargill is a flat and low-lying city; parts of the City are likely to be impacted by rising sea levels.

While not wanting to diminish the significant future impact of these issues the timeframes for sea level rises are into the future, rather than the ten-year planning horizon of this plan. It is expected that rising sea levels will have an impact on some Invercargill properties. Those that are low lying and close to the sea. Assessment of the impact of the mid-range forecast of sea level rise for the Southland region, shows that the number of areas impacted by a 1m rise in Invercargill are very minimal. The potential impact of more significant sea level rises will emerge over time and individual property owners will become aware of the impacts well in advance. Council will be aware of future developments and will be mindful of rising sea levels when considering Resource consents for new properties and the impact on future District Plans. Council will not impact individual's property rights by taking pre-emptive action on existing properties where the current uncertainty remains. As this may have an effect of making a future possible loss for a property owner a certain current loss. At this stage that would be unfair to both the property owner and the ratepayers who may then have to fund the loss.

Significant Capital Expenditure

This Strategy operates in line with the Infrastructure Strategy and observes that over the next ten years the cost to the Invercargill Community to preserve, renew and maintain our infrastructure assets will be significantly higher than previous renewal costs. Because of this the rates increase will be higher than in previous years. When looking at this Strategy it is important to understand where we are starting from and where we want to get to in ten years. As at 30 June 2020 the financial situation of Council is one of good health, with reasonable strong capacity to invest for the future.

Council was meeting four of the six prudence benchmarks. It has a relativity low level of debt compared to other New Zealand Councils and a low level of debt compared to its rate revenue.

Council asset position showed total assets of over $1 billion and investments of $97.6 million with no significant liabilities outside of term debt. Council also had its credit rating from Fitch Rating upgraded from AA to AA+ stable, which further supports Council's strong financial position.

The ten years cover by the Long-term Plan does present the Council with challenges financially. This is in response to the Council's increasing knowledge of its infrastructural assets and the increasing demand for improving infrastructure. This is of particular importance for Water Supply and Stormwater, as communities within New Zealand are becoming more concerned about drinking water quality and reducing contaminant entering our waterways via stormwater runoff.

Invercargill City Council like many other Councils has a pattern of under delivering on its Capital spending plans. There are 2 potential methods to address this:

1. Spend more money to ensure that the capital is spent. Taking this path would require greater knowledge of the obstacles related to capital projects, and indicates a sense of certainty that does not exist in reality.
2. Recognise that there is a sense of guess work in the programme and recognise that it will not all be delivered within the arbitrary time constraints that are an integral constraint of financial planning. That constraint is the accounting concept of a financial year.

Council will take a joint approach:

- additional resource being engaged to monitor capital project delivery,
- provision of funding for a portion of the items listed in the plan.

Council does not know which projects may be delayed and Council will ensure that it does not defer projects.

The level of funding provided for the renewals component of the capital programme will gradually rise from 75% to 85% of the programme over three years. This recognises that the assessment of work and timing is uncertain. The renewal capital programme is based on average lives, and while it is supported by evidence, it clearly cannot be based on prospective asset condition.

If we resort to statistical references for averages we see:

An average life of 80 years will have a level of variation for each asset. This is called a standard deviation. Statistics tells us that there is almost certainty that an asset will need to be replaced within 3 deviations. If the variation is 5 years, which is reasonably conservative, then we have almost certainty that an assets will be replaced in one of 30 years. Being 15 years before the average and 15 years after. Not as precise as our modelling may suggest.

In regards to major projects, 85% will effectively mean that the projects will be delivered 15% later than that indicated in the plan. That is, a 2 year project will take 28 months, which is a significant improvement on our historic delivery.

Council is also focused on growing Invercargill's community assets and reinvigorating Invercargill's CBD. A number of large community projects are planned throughout the ten years, all part of making Invercargill a more desirable place to live and work. These initiatives are also designed to complement and support the Southland Regional Development Strategy. The main projects that fall within this category include a new urban play facility and art centre within the CBD and a Museum Redevelopment.

The Council via its subsidiary company, Invercargill City Holdings Limited, is taking part ownership of a company that is planning a major upgrade of the inner city area.

The end goal for Council is to provide its citizens with a City that is maintaining and improving its key infrastructure assets while understanding that a City needs to also be a vibrant, entertaining and an interesting place to live, work and play.

Financially this means that the Council will be increasing its debt over the life of the Plan in order to achieve what it has set out to do.

Depreciation is calculated on an annual basis and currently represents 27% of total operating expenditure.

Charging depreciation each year spreads the cost of an asset over its useful life.

Council is proposing to balance its budget in each year of the LTP. With Council's net debt approach and a balanced budget Council is funding depreciation at a global level. We do not fund depreciation on a service by service basis. Council does not transfer depreciation into special reserves but for some targeted rates outlined below any cash surplus after meeting all costs (excluding depreciation) and capital spending, will be placed in a targeted reserve so rates for that purpose will only be used for that purpose. Those targeted rates that will have a targeted reserve are:

Water Rates
Sewage disposal rates
Central City Coordinator
Bluff Community Board.

While depreciation is an important indicator of the true long term cost of the service, as it reflects a level of asset consumption in a particular period, it is not a panacea for the long term sustainability of a given service. Assets have been purchased by a combination of debt and annual revenue. The goal of the funding of services is that there is a level of equity between generations that is that each generation pays a fair share. Depreciation can be a proxy for this equity but there are a number of circumstances where this does not hold true. New assets that have a high debt, have the cost of debt and depreciation to meet. However, debt has a lower cost over time due to inflation, and the generation that has the debt pays interest and contributes to repayment of the debt. This reduction of debt lowers the costs for future generations through two mechanisms. The first being the inflation effect on debt and the second being the debt repayment.

The financial strategy reflects a prudent approach to debt and inter-generational equity.

Intergenerational Equity

The services that the Council provides are costly due to the value and amount of assets that are used. The Council's strategy is to ensure that both current and future ratepayers pay their fair share of the cost of providing services. Intergenerational equity is achieved through loan funding long-term assets and drawing rates to pay for the loan over an extended period of time. Also, depreciation assists in intergenerational equity by ensuring that a cost is recognised for the consumption of the assets. Where debt is low and future asset renewal is approaching, the generation that is consuming the asset should also be contributing to its replacement. For major renewal the level of service remains the same before and after replacement. This ensures that both current and future users pay for the assets. Examples of this can be found in the Invercargill City Council Infrastructure Strategy.

Replacement of an asset with a like asset should not lead to a significant increase in the funding required for a service. If that occurs it indicates that funding is not equitable, as ratepayers of the future are paying a higher cost for the same level of service enjoyed by previous ratepayers at a lower cost.

Debt Management

Net Debt

To aide understanding and predictability of funding requirements Council has introduced the concept of net debt.

Net Debt = total borrowings less cash and cash investments.

Council is able to borrow and invest money at similar interest rates. Sometimes it is slightly higher and sometimes slightly lower. Currently the interest rate we pay on debt is lower than the amount we can earn on an investment. As Council is a conservative organisation we do not borrow for the sole purpose of investing. In some years there may be financial gain from that, but in other years it will have a cost. Borrowing for the sole purpose of investing is considered to be too close to speculation, and we do not believe it is prudent to speculate with ratepayers' money. However, to gain future certainty of funding costs Council may decide to borrow in anticipation of capital spending. In such a case the funds will be invested for a short period.

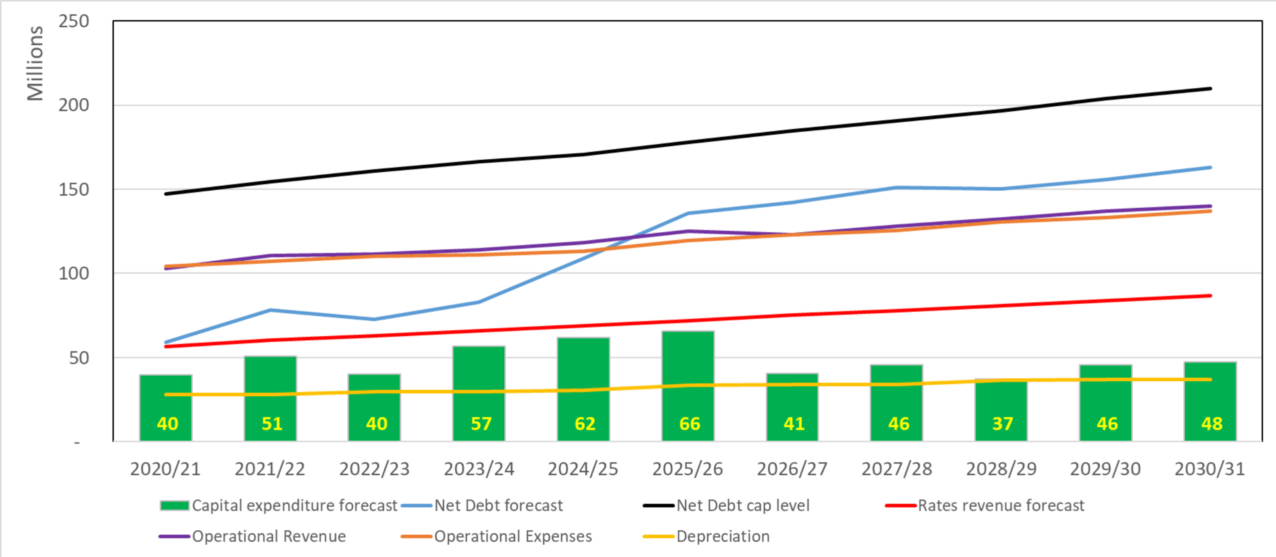
Borrowings

The Council's debt (excluding Invercargill City Holdings Limited (ICHL) bond) remains relatively low against the Council's total assets base (11.8% as at 30 June 2020). However, Council recognises that it has $100m of uncalled capital within ICHL. That capital can be called at the discretion of the directors of ICHL. Therefore in determining the maximum debt to would be prudent to incur, allowance needs to be made for the possibility of the capital to be called.

As a borrower from LGFA there is a maximum debt that Council can borrow. As a Credit rated Council that limit has been 250% of annual operating revenue. This is expected to rise to 300% before falling back to 280% over a number of years. Due the reduction to 280% being in 5 steps it would be unwise to take debt above 280%. In addition to the uncalled capital we need to make provision for unforeseen shocks. It would not be prudent to be at the maximum debt and then find a recession or natural disaster impacts on costs or revenue, with the potential to push the organisation above debt limits and therefore not able to access the necessary cash.

To be prudent Council has set a maximum debt level of 150% of revenue. This provides an increasing net debt cap over time rising from $154M to $210M

While the Council remains focused on keeping debt to a manageable level over the course of the Long-term Plan, large infrastructure projects as well as future growth projects necessitate the need for the Council to take on an increased level of debt.



Debt repayment

A significant issue for this LTP and this strategy is the increasing debt at a time when interest rates are at historic lows. This exposes the community to a significant risk of increased interest rates.

Debt is predicted to get close to the debt limits in the first 5 years of the plan. With borrowing rates as low as 1%, a rise of 1% will double the rates requirement to pay the interest. Every 1% increase in the interest rate would mean a rates rise above the forecast rates increase of about 2.5%. So a 2% rates rise would become 5%. Part of this impact can be managed through prudent borrowing, but only for a period of time.

In the interests of intergenerational equity Council should not go to the debt limits without a recognition that the debt will need to be reduced to allow future ratepayers to also undertake projects that will emerge in the future.

The funding strategy for rates will incorporate an amount of 2% of debt to go to the repayment of the debt.

Security for Borrowings

Council borrows from the Local Government Funding Agency. Part of borrowing from that source is that a standard security over rates is required. This is the most common security for Local Authority borrowing and is understood by the financial market lenders. It means that there is the ability in the event of a debt default for a security agent to set a rate to be able to pay the loan requirements.

The Council currently maintains an AA+ credit rating

Cash and Cash investments

The Council must ensure that each year's projected operating revenues are set at a level sufficient to meet that year's operating expenses, unless the local authority resolves that it is financially prudent not to do so.

The Council aims to operate a surplus for the duration of the Long-term Plan. To maintain sound treasury practice Council holds a range of investments in cash deposits. These are in two groups, funds held for restricted and non-restricted reserves.

Restricted reserves are held for a specific purpose and money is only available to be used for that purpose. In contrast a non-restricted reserve can be for a variety of reasons. These investments build up or reduce over time due to funding needs.

Holding a level of cash in investments provides a safety buffer for Council in times of uncertainty in the financial markets, as it gives us the option to use funds if the interest rates are considered to be artificially high. Having this flexibility is one factor contributing to Council's strong financial position and good credit rating. Council is targeting to maintain at least a cash investment portfolio of around $40m, this will fluctuate according to financial need.

Council limit on borrowing

Council is setting its limit on borrowing based on the Net debt measurement. The net debt limit is 150% of annual operating revenue (excluding significant one off revenue items).

Gross debt will be limited to 150% of annual operating revenue (excluding significant one off revenue items) plus the value of Cash and cash investments.

Rates

The Council will ensure that there are sufficient cash resources available to meet its obligations. The Council's current assets need to outweigh current liabilities, where current assets include cash on hand and available lines of credit

Council reviews operational expenditure for short and long-term cost savings and has established operational savings targets for the first three years of the Long- term Plan. These savings are intended to improve efficiencies within activities and services without impacting the current level of service being provided.

Rates are the "balancing factor" in the financial equations of Council. Revenue for all sources are examined on an annual basis, as are costs. Capital expenditure is evaluated for priority, need and timing for maintaining levels of service. Capital is funded from rates and, borrowing or use of investments. In the long term there is a limit on borrowing as the result of which either rates need to rise or the level of capital investment needs to reduce. This is an iterative process where the outcome is to get the service level desired by the community at a costs that is both affordable and does not hit the "willingness to pay" trigger.

Rates are set based on the factors relating to the property. One of the main factors that impacts predictability of rates is the three yearly revaluation of every property to establish the "Rateable values'. When properties are revalued it creates distortion in the rates increases each ratepayer has compared to Council stated rates rise. Unfortunately, there is very little Council can do to alleviate this effect. However, council is mindful that the rates increases should be predictable, not just in terms of total rates rise but also in impact on an individual property. For the past two years Council has set a uniform increase in rates that is each rate has risen by the same percentage. This means each ratepayer has the same increase, unless the owner has made changes to the property that trigger a need for a revaluation. It is part of this strategy that Council will maintain that practice for years that are not a Rates revaluation year.

Council limit on rates rises

In determining the impact and limits of rates rises Council has considered the level of capital spending required and also the limit on Council borrowing. To be able to undertake the capital works in the LTP the limits on rates rises are:

- The rates rise in any year will not be higher than 7.5%.

- The total rates take in any year will be no higher than a compounding annual rates rise of 7.5% per annum plus growth within the rating base.

Council in this strategy has put an emphasis on the predictability of rates. Council also recognises that the LTP is a ten year plan rather than being 10 one year plans. This means that the work programmes are established to maintain levels of service and that if work is not completed in one year it still needs to be funded over the period of the plan.

Managing Financial Investments and Equity Securities

The Council holds investments in companies, property and cash.

Investments in Companies/Trusts

The Council is an equity holder in companies and has a controlling influence over four trusts. The principal reason for holding an equity interest in the company investments is to provide a financial return on investment for ratepayers. The interests in the trusts are to enable more efficient and targeted community outcomes for the community. Trusts provide a good opportunity for community engagement with a particular outcome. Council does not seek financial return for the trusts. The Council's interest in the companies and trusts are as follows:

Company	Shareholding /Interest	Principal Reason For Investment	Budgeted Return
Invercargill City Holdings Ltd	100%	To undertake commercial opportunities and provide dividend returns to the City.	$4,886,000 for 2020/21 year
Southland Museum and Art Gallery Trust Board	Controlling interest	To provide specialised governance for the Museum.	Nil.
Bluff Maritime Museum Trust	Controlling interest	To provide specialised governance for the Museum.	Nil.
Invercargill City Charitable Trust	100%	To provide access to recreational and cultural events within the City, in line with community outcomes.	Nil.

Invercargill Community Sports and Recreation Trust	100%	To increase Invercargill residents' active participation in sports and physical activities and arts and cultural activities.	Nil.

The Council has no plans to change its shareholding, although in accordance with good practice this is reviewed regularly.

Property Investments

The Council's Investment Property Department oversees the development and undertaking of investment in property within the City. The properties are divided into two categories:

- Endowment properties which have been either allocated (per above) or purchased from endowment funds.
- Trading properties (fee simple, no classification on title, currently leased).

The Council's objective is to maximise return from endowment and trading properties, however due to historic lease arrangements (21 year Glasgow leases) the return from these properties is below market rates. The objective for the net return on investment from both endowment and trading properties is at least equal to current market interest rates.

Council also has a portfolio of operational properties and properties acquired for a strategic purpose. Where a property acquired for a strategic purpose is no longer required for that purpose, it is placed in the Trading Properties portfolio and is considered to be available for sale. Council does not see itself as a property investor for profit, with the exception of the endowment property portfolio.

Two significant properties acquired for strategic purposes are the Don Street property developed by Council

Cash Investments

The Council holds cash for two main reasons:

- To ensure strong lines of liquidity and access to cash remains available to Council.
- To support the balance of reserves through short- term investments (90 to 360 days) to maximise return on investment.

Rates and Affordability

The Council has come through a period of medium-level rates rises over the previous three years (2018/19: 4.91%, 2019/20: 3.50% and 2020/21: 2.00%). This was due to the Council focusing on ensuring that rates were low and consistent from year to year.

For future years there are some key challenges that will present themselves in relation to affordability. This will occur as the Council enters a period of accelerated capital expenditure to develop our services, whilst looking to be a growing and innovative City.

Increasing costs of providing council services is likely to intensify the affordability issues in the future. In certain years of the Long-term Plan, pressure from required infrastructure renewals has led to rates increases that are less affordable than what the Council would like.

A larger rates increase will not necessarily occur in these years as growth projects are loan-funded and will be paid back over time so as not to unfairly unburden the current ratepayers with the large costs associated with these projects.

The Council seeks to embrace innovation and change over the upcoming years, and with the constant evolution and growth of technology, we are witnessing and experiencing the change first-hand.

Invercargill City Holdings Limited (ICHL)

Invercargill City Holdings Limited is a 100% owned subsidiary of Invercargill City Council. ICHL was formed to provide a clear differentiation between Council's core ratepayers orientated activities and its commercial trading enterprises and investments. It was established for the purpose of consolidation and management of existing Council companies, with the responsibility of control and oversight of the performance of the Council Owned Companies activities on behalf of the ultimate shareholder, Invercargill City Council.

Companies that sit within the ICHL group include, Invercargill City Forests Limited (ICFL), Invercargill City Property Limited (ICPL), Invercargill Airport Limited and Electricity Invercargill Limited (EIL). Within both ICFL and ICPL sits an additional entity. Within EIL sits a number of utility based entities. One of the main purposes of ICHL is for these individual companies to trade profitably in order for ICHL to return a dividend to Council and help offset the rates demand as a result.

ICHL has historically given a dividend to Council since 1999. In order to provide predictability for rates Council has set an expectation that the dividend is set at a level that allows ICHL to be able to pay an annual dividend that will increase with inflation each year. The dividend is forecast to increase over the next ten years with $4,886,000 predicted for the 2020/21 year. Should this dividend fail to increase as predicted, Council would have less income received to minimise the impact on the general rates draw.

Council has noted that they cannot be financially reliant on an increasing dividend to match 10% of the general rates draw every year. Whilst ICHL strives to produce greater dividends year on year this is not necessarily going to be in line with the anticipated rates requirement increase.

Disclosure Statement

The purpose of this statement is to disclose the Council's planned financial performance in relation to various benchmarks to enable the assessment of whether the Council is prudently managing its revenues, expenses, assets, liabilities and general financial dealings. The Council is required to include this statement in its Long-term Plan in accordance with the Local Government (Financial Reporting and Prudence) Regulations 2014 (the regulations). Refer to the regulations for more information, including definitions of some of the terms used in this statement.

Rates Affordability Benchmark

The Council meets the rates affordability benchmark if:

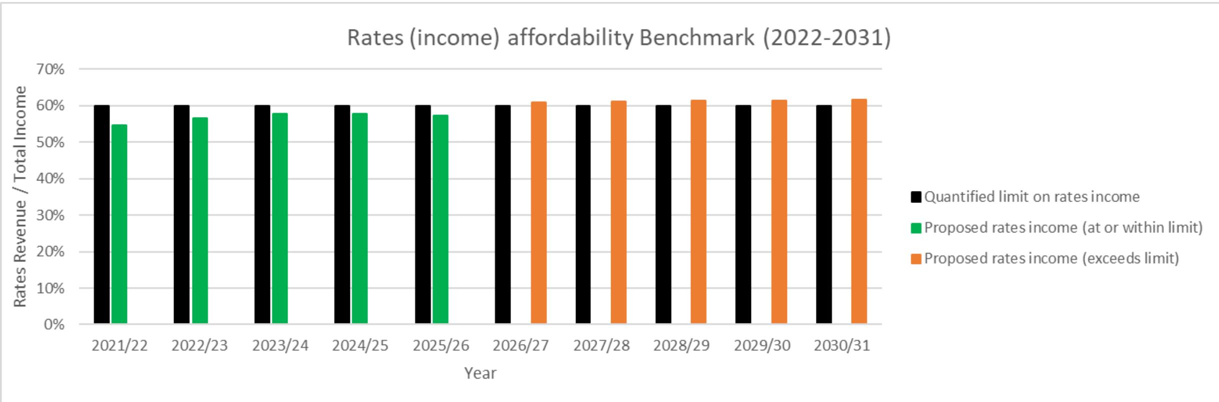
- its planned rates income equals or is less than each quantified limit on rates; and
- its planned rates increases equal or are less than each quantified limit on rates increases.

Rates (Income) Affordability

The following graph compares the council's planned rates with a quantified limit on rates. The quantified limit is rates revenue will not exceed 60% of total revenue.

The Local Government Rates Inquiry suggests that around 50% of a council's operating revenue should be taken from rates. Currently the Council draws about 55-57% of its operational revenue from rates.

The Council aims to maintain the rates collected to between the range of 50% and 60% of total Council revenue. The Council intends to increase user-pays methods to enable the income required from rates to maintain steady without significant rates increases. The Council will also seek efficiencies in how services are delivered to assist with maintaining rates revenue at a steady level.



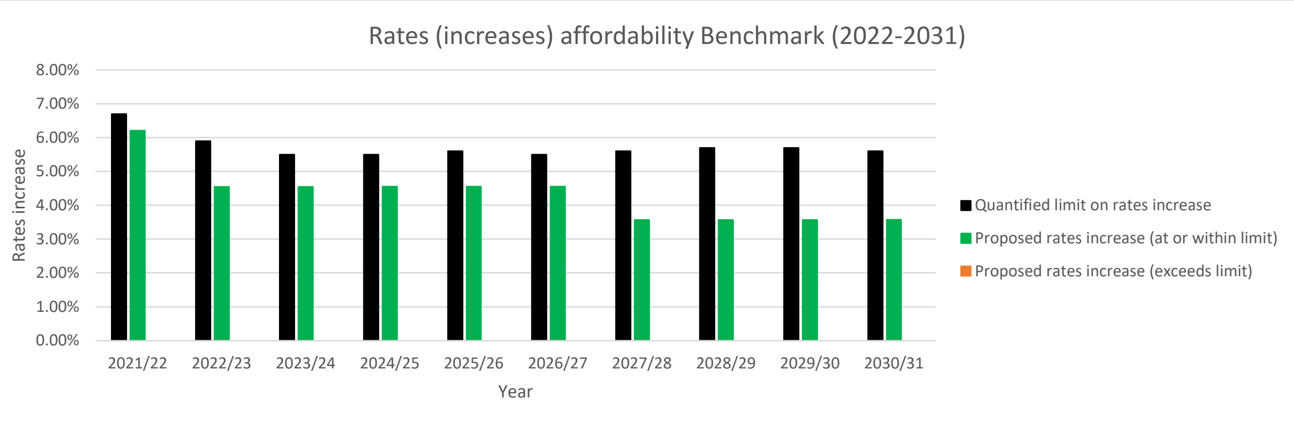
Rates are an important source of funding for the Council, but they are not the only source available. You can see more about how the Council funds its services in the Financial Management section of the Long-term Plan. The Council's Revenue and Financing Policy sets out the funding of its operational and capital expenditure and the sources of those funds on an individual activity basis.

Throughout the Long-term Plan rates fund between 55% and 62% of the Council's total revenue. The 2026/27 year has a significantly higher rates funded component due to the planned completion of the Museum. The Museum will cost roughly $2 million annually to cover the repayments and interest with no fees revenue to offset this charge to rates.

Rates (Increases) Affordability

The following graph compares the Council's planned rates increases with a quantified limit on rates increases. The quantified limit is rates increases will not exceed the Local Government Cost Index (LGCI) plus 3%. The forecast LGCI increases for the next ten years are shown in the table below, but for example, if the LGCI change was 2.20%, the Council's rates increase would be no more than 5.20%. The Council recognises that this increase could potentially be higher than household income, so although a maximum limit has been set, the Council will endeavour to achieve lower increases when planning projects and services that rely on rates revenue.

The Council recognises that the cost of providing Council services (LGCI) is rising at a higher rate than the Consumer Price Index (CPI). The Council is also mindful of affordability issues amongst our ratepayers. The Council continues to investigate cost-cutting methods to ensure that the revenue required to run the Council is kept relatively steady. The rates increases reflect the money required each year.

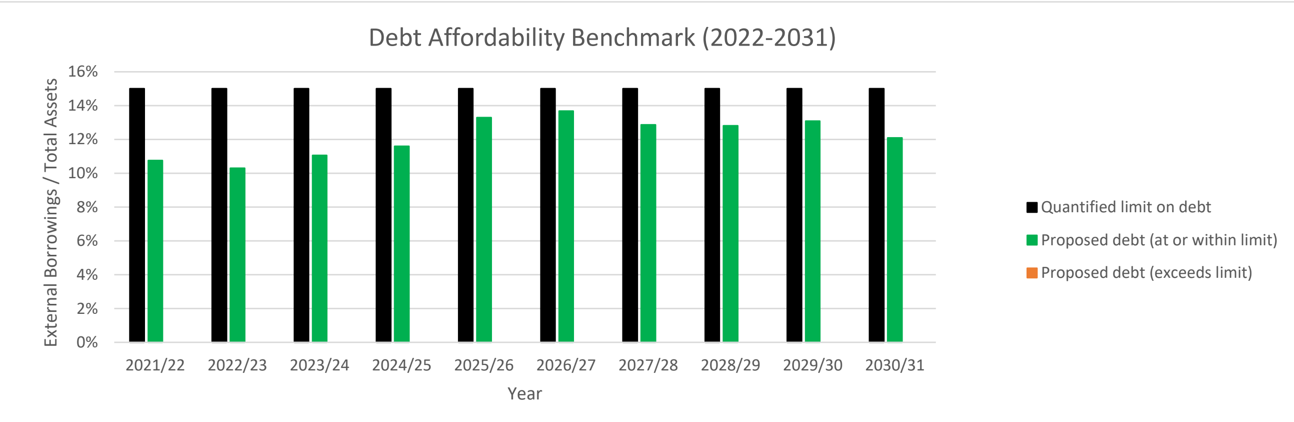


Changes in the consumer price index (CPI) are used as the basis for measuring the inflation faced by households. It gives a picture of how the prices of the goods and services purchased by the typical New Zealand household are changing over time. It is therefore heavily represented by food, accommodation and transport costs, which collectively make up over 50% of the index. The Council however purchases a different mix of goods and services. The Council's 'basket' is dominated by changes in the Local Government cost adjustors such as labour costs, land and materials associated with assets. There is therefore a difference between changes in CPI and the Council's cost (LGCI). To enable the Council to best predict what the future cost of providing its services will be, we have based future inflationary costs on the LGCI rather than CPI. The additional 3% is to allow the Council to undertake new projects, for example the Central City Master Plan, Museum and Art Centre projects.

Debt Affordability Benchmark

The Council meets the debt affordability benchmark if its planned borrowing is within each quantified limit on borrowing.

The following graph compares the Council's planned debt with a quantified limit on borrowing. The quantified limit is that debt will not exceed 15% of total assets.

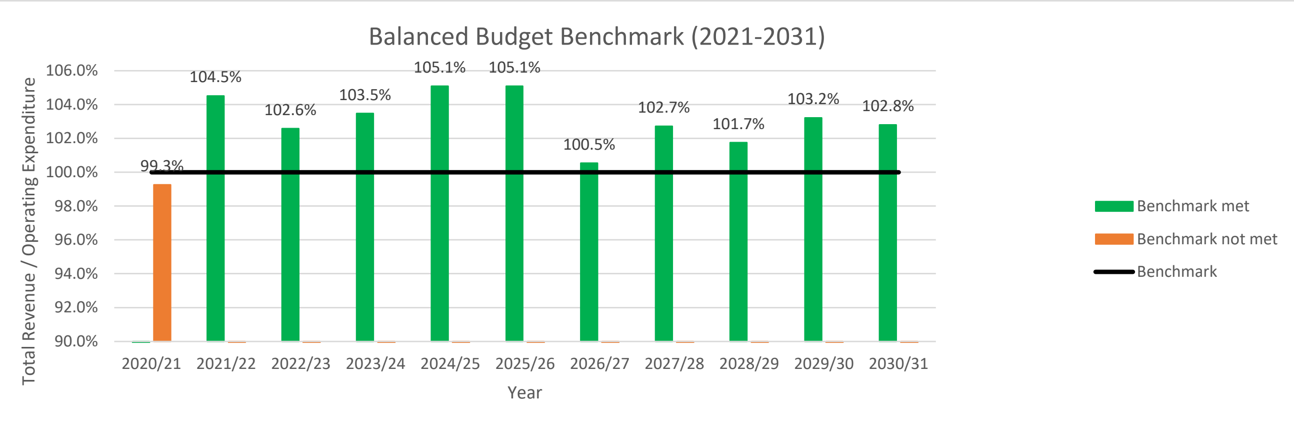


During the Long-term Plan period, the debt affordability percentage is expected to increase, peaking at 14.56% in 2026/27 before decreasing again.

The Council considers that setting a borrowing limit of 15% of assets will assist in prudently managing Council's borrowing activities to ensure the ongoing funding of Council. The Council will continue to consider and approve the borrowing requirement for each financial year in the Annual Plan or Long-term Plan recognising that borrowing capacity does not have to be fully utilised.

Balanced Budget Benchmark

The Council meets this benchmark if its revenue equals or is greater than its operating expenses.



The above graph displays the Council's planned revenue (excluding development contributions, financial contributions, vested assets, gains on derivative financial instruments, and revaluations of property, plant, or equipment) as a proportion of planned operating expenses (excluding losses on derivative financial instruments and revaluations of property, plant, or equipment).

The Council meets the balanced budget benchmark if its planned revenue equals or is greater than its planned operating expenses.

Section 100(2) of the Local Government Act 2002 (LGA) sets out the matters that Council must have regard to when determining that it is prudent to operate an unbalanced budget.

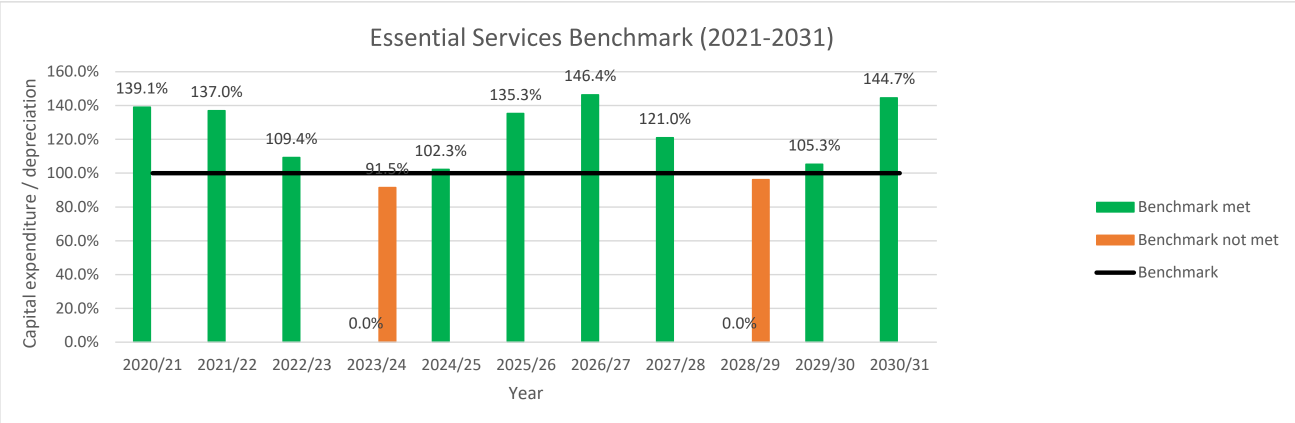
These matters are:
(a) the estimated expense of achieving and maintaining the predicted levels of service provision set out in the Long-term Plan, including estimated expenses associated with maintaining the service capacity and integrity of assets throughout their useful life; and
(b) the projected revenue available to fund the estimated expense associated with maintaining the service capacity and integrity of assets throughout their useful life; and
(c) the equitable allocation of responsibility for funding the provision and maintenance of assets and facilities throughout their useful life; and
(d) the funding and financial policies adopted under section 102.

The proposed Long-term Plan has set projected operating revenues for all years at levels that would meet the projected operating costs.

Essential Services Benchmark

The following graph displays the Council's planned capital expenditure on network services as a proportion of expected depreciation on network services.

The Council meets this benchmark if its capital expenditure on network services equals or is greater than depreciation on network services. Although not reaching the target in every financial year, over time Council's capital expenditure should equal its depreciation. This will mean Council is replacing its assets as they deteriorate, however due to some projects being large it is hard to assess this on a year by year basis.



Council does not meet this benchmark in two of the 10 years. 2023/24 and 2028-29 are lower than deprecation level due to the timing of projects which are planned in 2025/26, 2026/27 and 2030/31. Council does meet the Benchmark over the course over the combined 10 year, and exceeds in most cases.

Debt Servicing Benchmark

The following graph displays the Council's planned borrowing costs as a proportion of planned revenue (excluding development contributions, financial contributions, vested assets, gains on derivative financial instruments, and revaluations of property, plant, or equipment).

Because Statistics New Zealand projects the Council's population will grow as fast as the national population is projected to grow, it meets the debt servicing benchmark if it's planned borrowing costs equal or are less than 10% of its planned revenue.