Note regarding draft status for this Financial Strategy

This strategy underpins the proposed Long Term Plan recommended by Council. Although still subject to change by both public feedback and Council, this Strategy has been written as if the proposed policy changes and draft budget are accepted. Following consultation with the public on the key issues of our draft Long Term Plan, any significant changes may need to be reflected in an updated Financial Strategy.

Introduction

The Financial Strategy outlines the Council's overall approach to planning and managing its finances in a way that is sustainable over the long term. It is a central component of Council's Long Term Plan document. The Financial Strategy sets our limits on rates increases and debt, illustrates the overall financial implications of decisions made in the Long Term Plan and is key in demonstrating prudent financial management.

Over the next 10 years, it will cost $2.0 billion to grow and run our district. That's a huge investment of ratepayer dollars so it's important this money is spent in the context of a well-considered financial strategy. Agreed financial limits restrict what we can deliver each year but also enable delivery by ensuring we have the financial resources to do this. Project prioritisation has been the key to ensuring the community has the services it expects to have, in a way that balances affordability with delivery.

Although more difficult to predict in the current environment, growth is a key factor again in this Long Term Plan with average annual district wide growth of 3.0 percent, even when factoring in a more prudent level of growth during the economic recovery of Covid-19.

The economic recovery from the Covid-19 pandemic has been widely considered as part of this Long Term Plan; with particular attention on balancing spending required to aid economic recovery with ensuring our financial limits are conservative, particularly in the first three years.

Waipa District Council is in a very good financial position. Our draft Long Term Plan proposes an average annual rates increase of 1.8 percent over the next ten years for existing ratepayers, including volumetric and network water meter charges which are charged separately. This puts us in a good position, when we engage with the community, on a district wide spatial plan in 2020/21 which will inform investment and funding from year 4 onwards.

Our rates increases are maintained within a limit of the Local Government Cost Index (local government inflation measure) plus 2 per cent for the first three years, and the Local Government Cost Index plus 3 per cent for the remainder of the Long Term Plan. Council considers this to be a reasonable and affordable limit and has considered the economic recovery from the Covid-19 pandemic when setting these limits. We also have limited rates to a maximum of 65 per cent of our total revenue.

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Balanced Budget

Council is projecting significant surpluses throughout the ten years of the LTP, the majority of these surpluses are attributed to Development Contributions and Vested Assets. The Development Contributions are collected for investment in new, or expansion of, infrastructure and pay the interest on debt raised to fund these growth projects.

One of the prudence measures Council has is the Balanced Budget Benchmark, this benchmark checks that each year's projected operational revenue is set at a level to meet that year's operational expenditure. From Council's significant surpluses, the revenue directly relating to capital (Development Contributions and Vested Assets) has to be deducted to determine our operational result. In year 6, we are projecting a break-even position but in all other years of our draft Long Term Plan, we are projecting small operational surpluses.

Growth

District wide growth continues to remain a significant factor for Waipā, although we acknowledge that this is more difficult to predict in the current environment due to the Covid-19 pandemic. We have mitigated the risk of overcalculating our growth projections by factoring in a prudent level of growth during the first two years of the Long Term Plan during the Covid-19 recovery period.

Delays in the release of the 2018 Census information by Statistics New Zealand has meant that the Council's current population change projections are still based on the 2013 Census. Once NIDEA has the final Census information, these projections will be updated. Using 2013 Census information, Waipa is expecting an additional 25,000 people by 2050. This will take our total population to nearly 75,000.

Some of the cornerstone projects included in the Long Term Plan to unlock future growth are:

a) Cambridge Wastewater Treatment Plant $100.2m

b) Cambridge development in C2 & C3 growth cells $77.4m

c) Hautapu development including C8, C9 & C10 growth cells $69.3m

d) Further development in Cambridge C1 growth cell $33.1m

e) Picquet Hill development including T9 & T10 growth cells $22.2m

f) Te Awamutu Wastewater Treatment Plant $20.5m

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The Infrastructure Strategy details a full list of capital projects.

Growth pays for growth

A key challenge in our Long Term Plan 2021-31 is providing resilient infrastructure that meets the needs of our fast-growing district while keeping rates affordable. Our infrastructure needs to meet the service level expectations of our ratepayers and other stakeholders and the higher demands of the environmental standards set by regulatory agencies.

As well as this, we need to make sure all of the other quality services Council provides continue to be delivered at the level our residents and ratepayers expect, and enjoy – while ensuring the rates impact is contained.

Council will be taking on substantially more debt to fund growth. Catering for growth is required by the National Policy Statement on Urban Development Capacity. Council will help to ensure rates remain affordable and within our limits by ensuring 'growth pays for growth'. Under our Development Contributions Policy, developers are charged for the interest cost of new infrastructure development debt, not just the principal cost.

Service level improvements and Renewals

Growth however, is just one part of the story. Huge investment is required in service level improvements to ensure the resilience of existing infrastructure and the achievement of tougher environmental standards. There is also an ongoing need for continued investment in renewals.

The table below indicates the nature and extent of our proposed capital spend over the course of the Long Term Plan:

	Growth $000s	Improve service level $000s	Renewals $000s
Water treatment and supply	22,856	17,775	69,956
Stormwater	74,006	4,458	12,385
Wastewater treatment and disposal	146,205	1,099	17,914
Roads and footpaths	86,427	32,915	78,140
Other	16,404	81,842	35,264
Total	**345,898**	**138,089**	**213,659**

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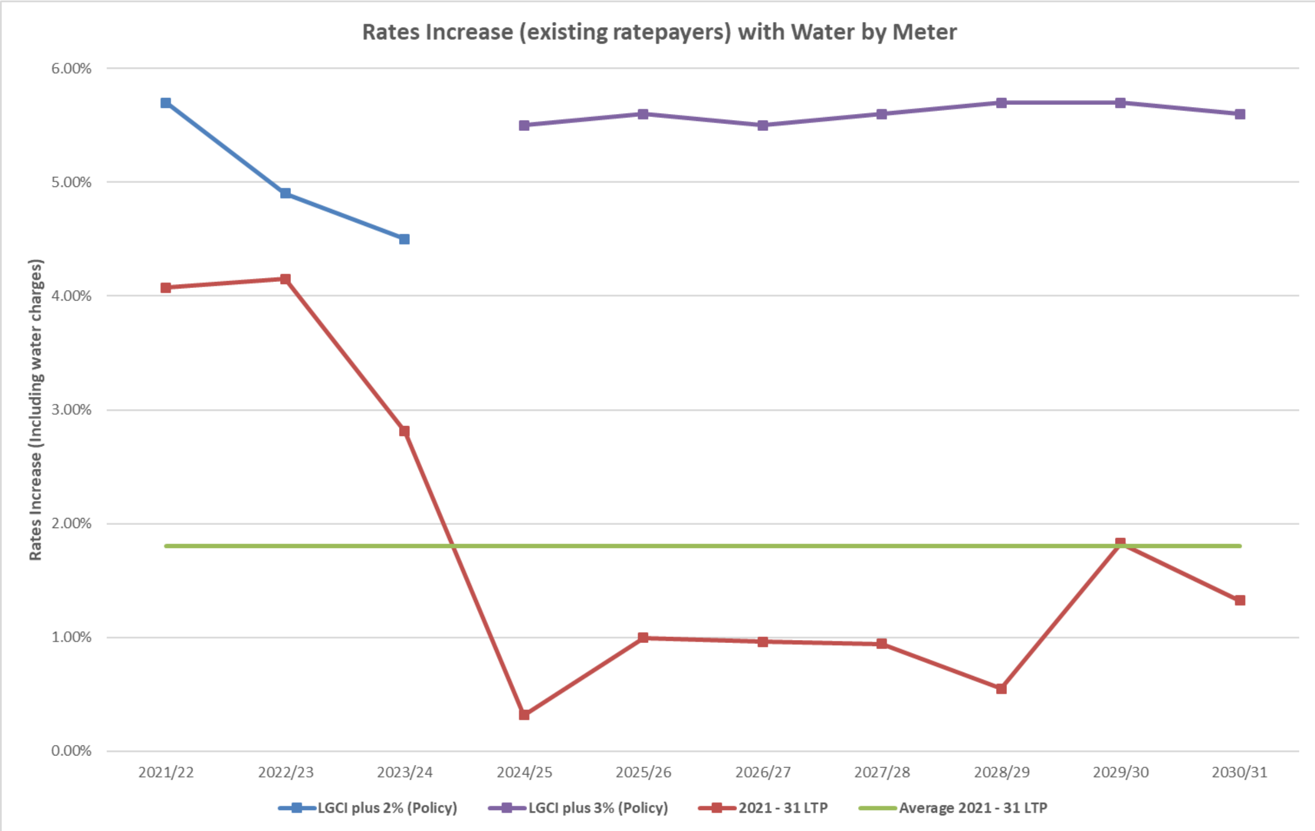
Rates

Our average rates increase over the ten years attributed to existing ratepayers, is 1.8 percent annually. This includes volumetric and network water meter charges which are billed by separate invoice as these charges are in terms of legislative definition, a rate. The annual rates increases over the ten years range between 0.5 percent and 4.1 percent.

All of the proposed rate increases are within Council's policy limit of the Local Government Cost Index plus 2% in the first three years, and Local Government Cost Index plus 3% for the remainder of the Long Term Plan, as demonstrated in the graph below:



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Setting limits on rates is a key part of ensuring financial sustainability and also ensuring rates remain affordable for our ratepayers. The economic recovery from the Covid-19 pandemic has been considered when setting these rates limits with a particular focus on ensuring the limit remains lower for the first three years of our Long Term Plan.

As well as setting limits on the level of annual rate increase we also set limits on the proportion of our income that comes from rates. This provides a focus on maximising revenue from non-rate sources and ensuring rates remain affordable. We are committed to limiting rate levels to a maximum of 65 per cent of our total revenue.

Debt

Council's debt is expected to be $177.4 million on 1 July 2021. This is a modest level of debt for a Council of Waipa's size that is set to rise steadily over the first seven years of the Long Term Plan to peak at $302 million. A significant contributor to the increase in debt is the need for infrastructure to provide for growth. The National Policy Statement for Urban Development Capacity requires high-growth Councils to have adequate land provision to accommodate development. By extension, Council must then provide infrastructure to enable this development to occur.

Council has determined that our net external debt limit is prudently set at 250 per cent of total revenue, and the gross interest expense on external debt for the year is required to equal or be less than 15 per cent of revenue (excluding development contributions, financial contributions, vested assets, gains on derivative financial instruments, and revaluations of property, plant, and equipment). We remain comfortably within these limits for the duration of the plan.

Development-driven debt is paid down as the Development Contributions are received.

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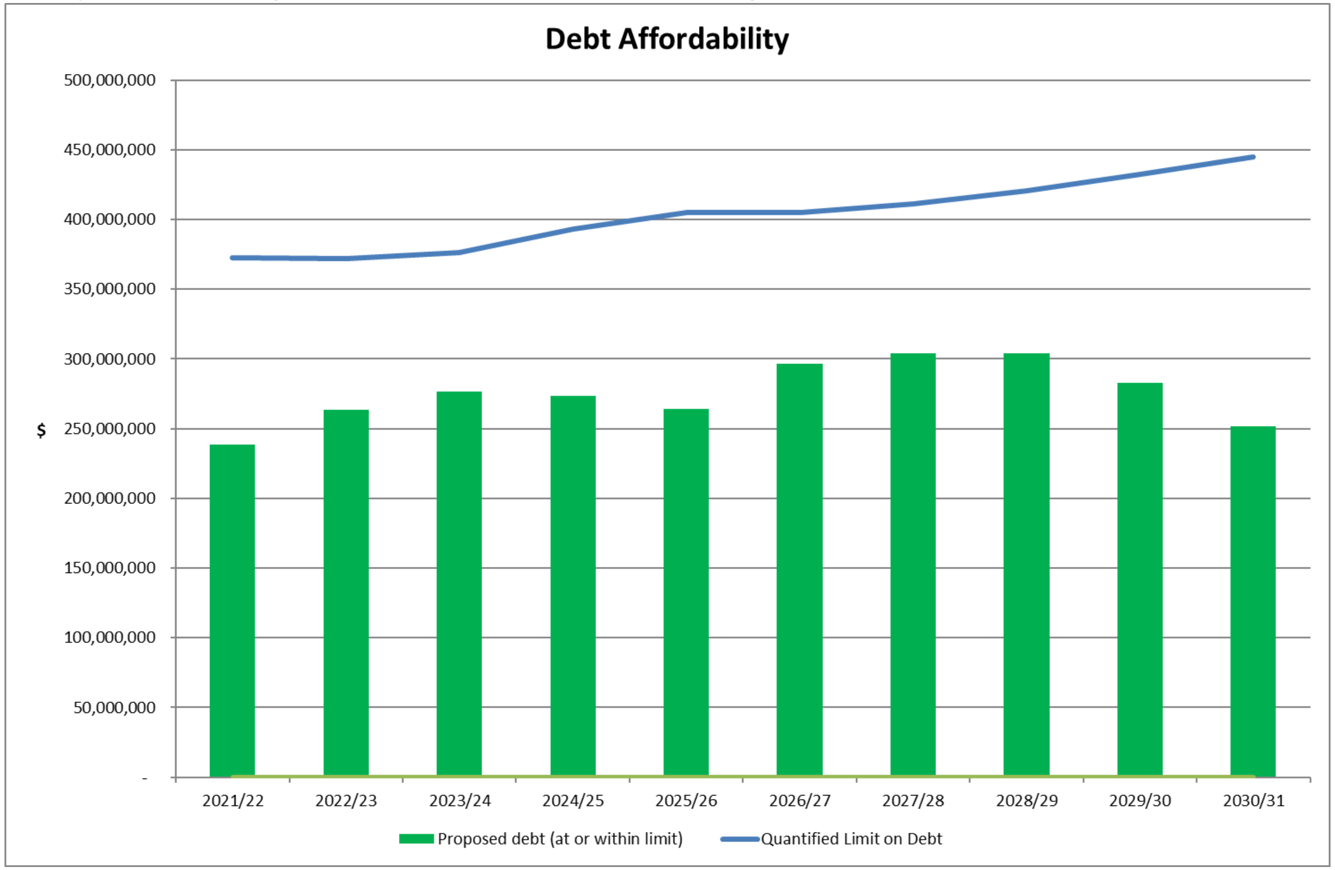
The graphs below show the anticipated results against the limits as set out in the Long Term Plan:



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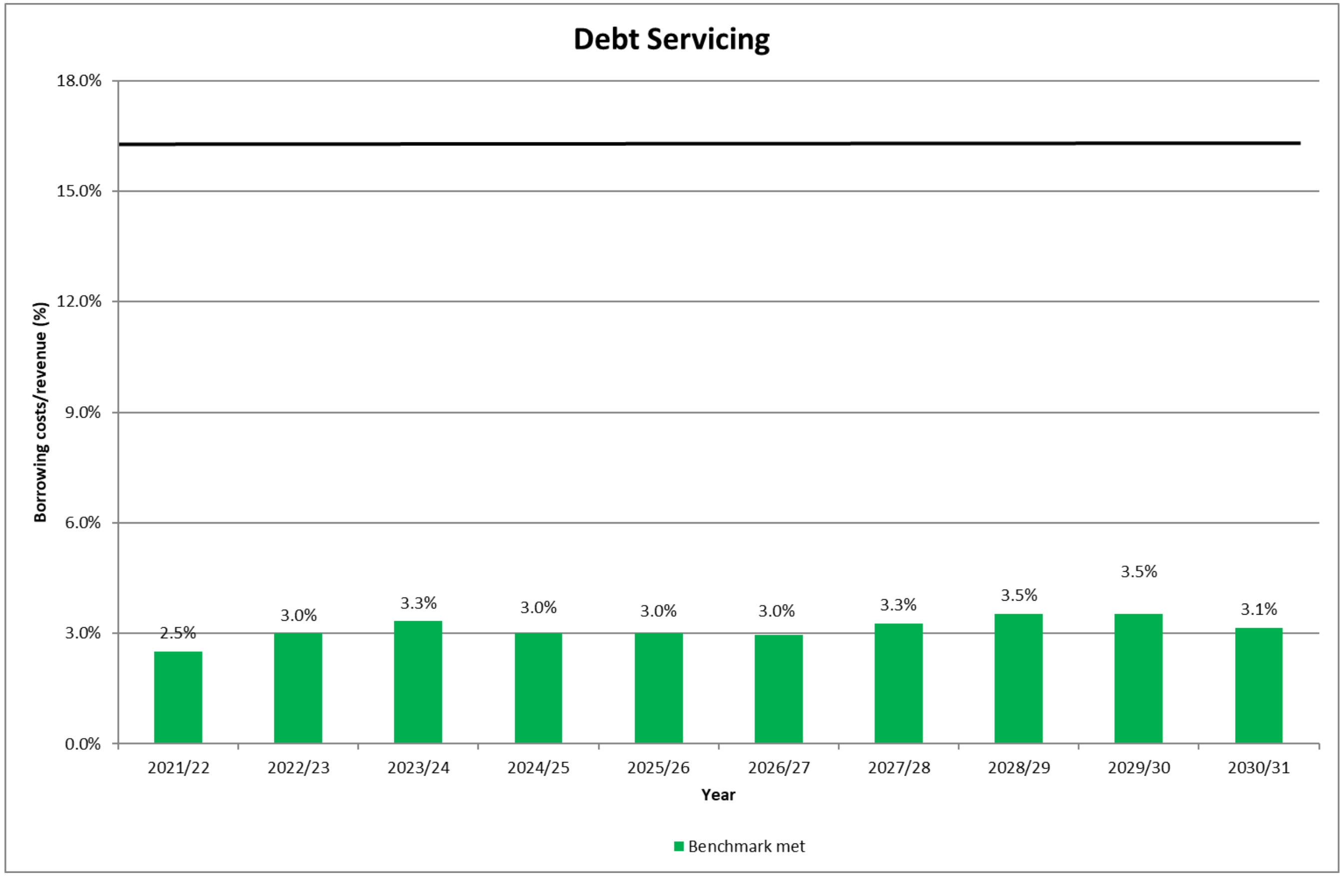

Asset Sales

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Council continues to progress the sale of surplus assets in order to fund capital projects. Council has included a total of $20.2 million of projected asset sales across years 1 to 10 of the Long Term Plan 2021 – 2031. The projects funded from these sales may be delayed or alternate interim funding might have to be sourced if there are delays in the timing of achieving these sales.

Security for borrowing

Borrowing is secured by a charge over rates by way of debenture trust deed. Generally assets are not offered as security for any loan or performance of any obligation under an incidental arrangement.

Investments

Our investment policy sets out the detail of the type of investments Council currently holds, and our objectives and risk management strategies related to holding these investments. Our approach to managing our investments is set out in our Treasury Management Policy.

Council is a shareholder in Waikato Regional Airport Limited, the New Zealand Local Government Funding Agency Limited and Local Authority Shared Services Limited. We also hold a small interest in Civic Financial Services Limited.

Other than to achieve strategic objectives, it is not our intention to undertake new equity investments. We will periodically review investments with a view to exiting at a time when market conditions are favourable and overall strategic objectives are not compromised.

Any dividend income from investments is generally included as part of general revenue.

Any purchase or disposal of equity investments not identified in this Plan is by Council resolution.

At the time of disposal, we will determine the most appropriate use of sale proceeds.

Managing financial risk

In developing this Financial Strategy Council considered how we would respond if unexpected circumstances had significant impact on our financial situation.

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Lower than expected growth

A key risk is lower than expected growth which is particularly relevant due to the difficultly in predicting growth in the current environment (due to the Covid-19 pandemic). Lower than expected growth would result in a shortfall in development contributions and a potential situation in which we have prematurely invested in infrastructure for growth that does not actually occur.

We have been conservative in our approach to this strategy and to the draft Long Term Plan. We have factored in a prudent level of growth for the duration of the Long Term Plan, with particular focus on the first two years, during the Covid-19 recovery period. We have ensured that if in fact growth does not meet expectations, there is a sufficient buffer.

We have also been conservative with our spending and capital works programme in this draft Long Term Plan. Even with significant changes to predicted growth, we will be in a good position to cover the interest cost on our debt for assets that have already been constructed. To mitigate the risk further, we will review our capital work programmes annually, amending the scale and timing of projects in response to actual or anticipated changes in growth levels.

By designing and building some of our core infrastructure, such as water and wastewater treatment plant upgrades, on a modular basis, means we can spend on an incremental basis that reduces financial outlay and the risk of underutilised assets.

Higher than expected growth

Higher than expected growth places additional demands on Council to accelerate the delivery of capital projects, this will be funded from increased or earlier development contribution revenue.

Higher than expected inflation or interest rates

If inflation and interest rates are higher than projected this will increase the overall cost of operational expenditure and capital projects. Again there is a prudent buffer in place which should allow the greater operational costs to be funded from increased rates, without unduly impacting on affordability. Council would still seek to remain within the rate limit of LGCI plus 2 per cent in the first two years, and LGCI plus 3 per cent for the remainder of the Long Term Plan. We also believe we will have sufficient capacity in our debt prudence limits to fund increased capital project costs.

Water Meter Revenue

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Lower than expected water meter revenue may create a shortfall in funding of budgeted costs, assuming levels of service are maintained, with loans required to fund the shortfall. The amount and timing of water meter revenue to be received has been calculated in line with the growth in water consumption expected due to the additional properties consistent with the development contributions model and assumptions, which is particularly relevant due to the difficultly in predicting growth in the current environment (due to the Covid-19 pandemic). We are engaging an expert to complete modelling of our water meter revenue prior to adoption of this Long Term Plan.

Any relevant adjustments will be made in our Year One estimate prior to adoption of this Long Term Plan and yearly budgets will be reviewed during each Annual Plan process.

Revaluation of non-current assets

A key risk is the revaluation of non-current assets, in particular our Infrastructure Revaluations (transportation and three waters) which are revalued every second year. These revaluations are being completed in the 2020/21 year and expected increases are consistent with the Business and Economic Research Limited inflated values. Due to the current environment with the Covid-19 pandemic and increased Central Government spending in the infrastructure area, this has increased uncertainty in the validity of the values used.

If actual valuations are different to that predicted using the Business and Economic Research Limited inflated values in both our starting position and throughout our long term plan, we will need to reflect this in our Statement of Financial Position. There will be impact on the level of depreciation in the Statement of Comprehensive Revenue and Expense and funding through rates and user fees and charges.

We will monitor value projections against actuals for the 2020/21 year and adjust when appropriate. Significant differences will be reflected in budget forecasts and annual plans.

The Assumptions section of the Long Term Plan document contains further detail of the sensitivity of our financial projections to unanticipated circumstances.

Long-term plan disclosure statement for period commencing 1 July 2021

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.

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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 increase.

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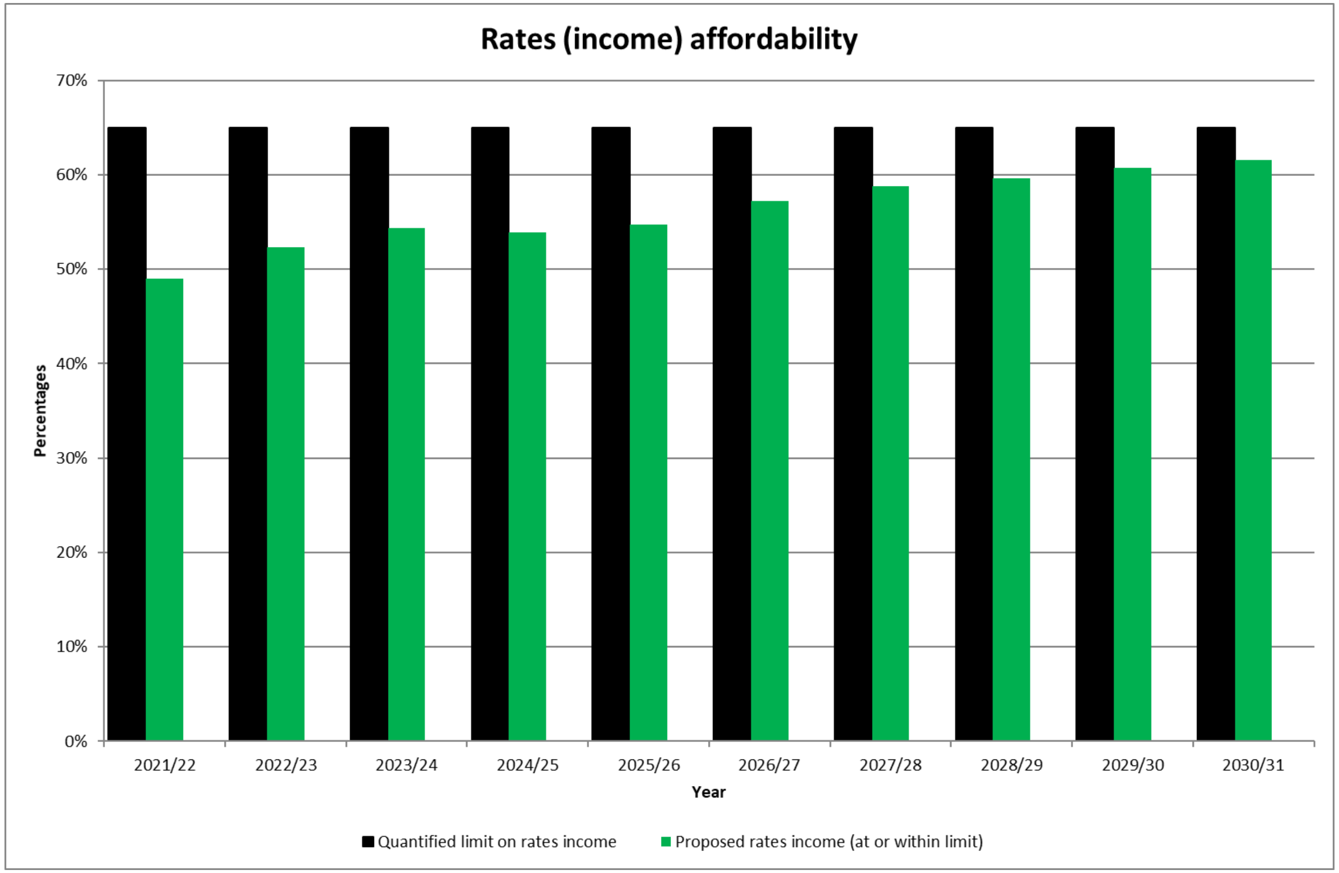
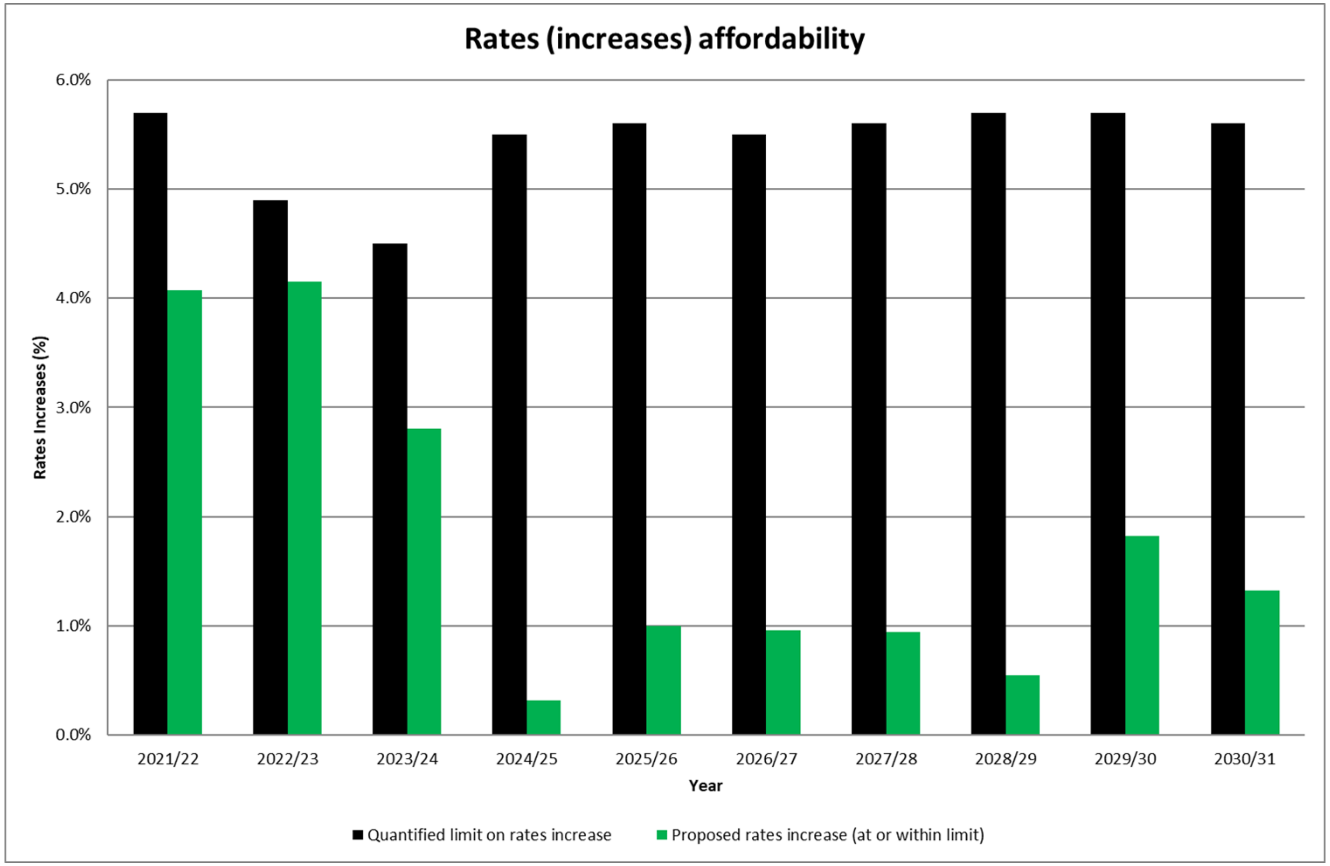
Rates (income) affordability

The following graph compares the Council's planned rates with a quantified limit on rates contained in the Financial Strategy included in this LongTerm Plan. The quantified limit is limiting rates levels to a maximum of 65% of our total revenue.



Rates (increases) affordability

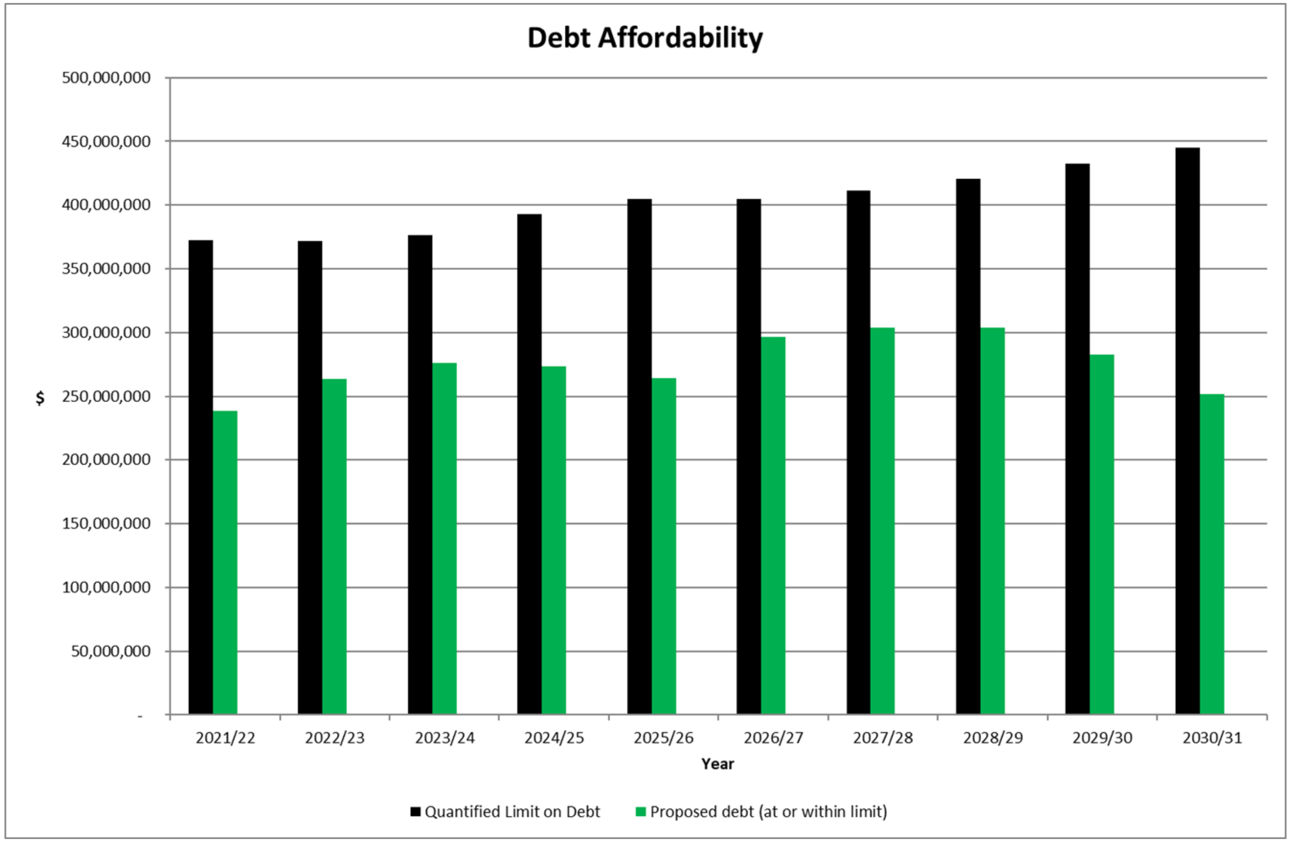
The following graph compares the Council's planned rates increases with a quantified limit on rates increases contained in the Financial Strategy included in this Long Term Plan. The quantified limit is Council will limit annual increases in the average rate requirement (after growth) to no more than the forecast Local Government Cost Index for that year plus 2% for the first three years, and Local Government Cost Index plus 3% for the remainder of the Long Term Plan.



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 contained in the Financial Strategy included in this Long Term Plan. The quantified limit is set at 250% of total revenue forecasted for each year of this plan.



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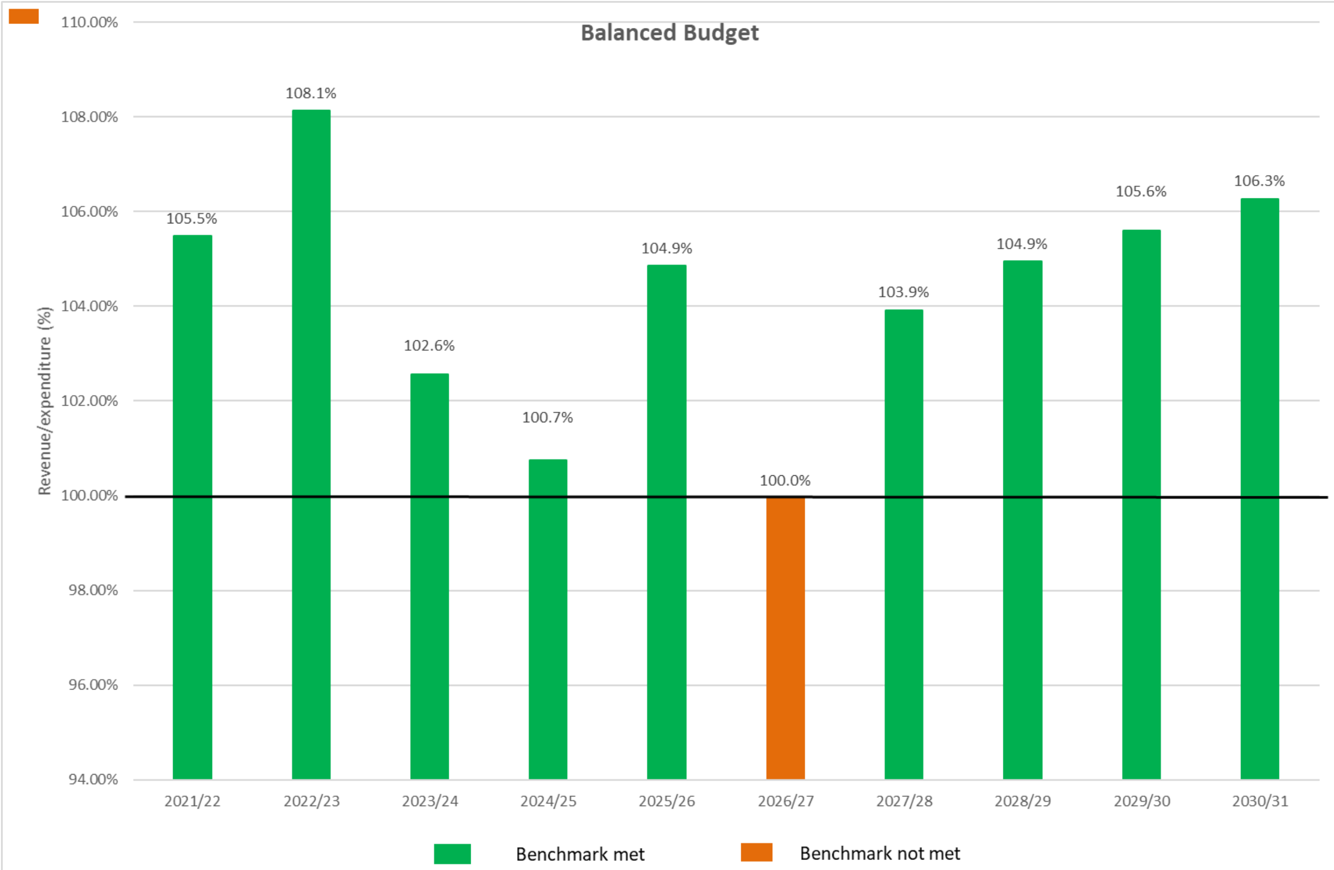
Balanced budget benchmark

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

The Council meets the balanced budget benchmark if its planned revenue equals or is greater than its planned operating expenses. Year 6 is shown as benchmark not met, being coloured orange as it is below the 100% based on the result to 2 decimal points.



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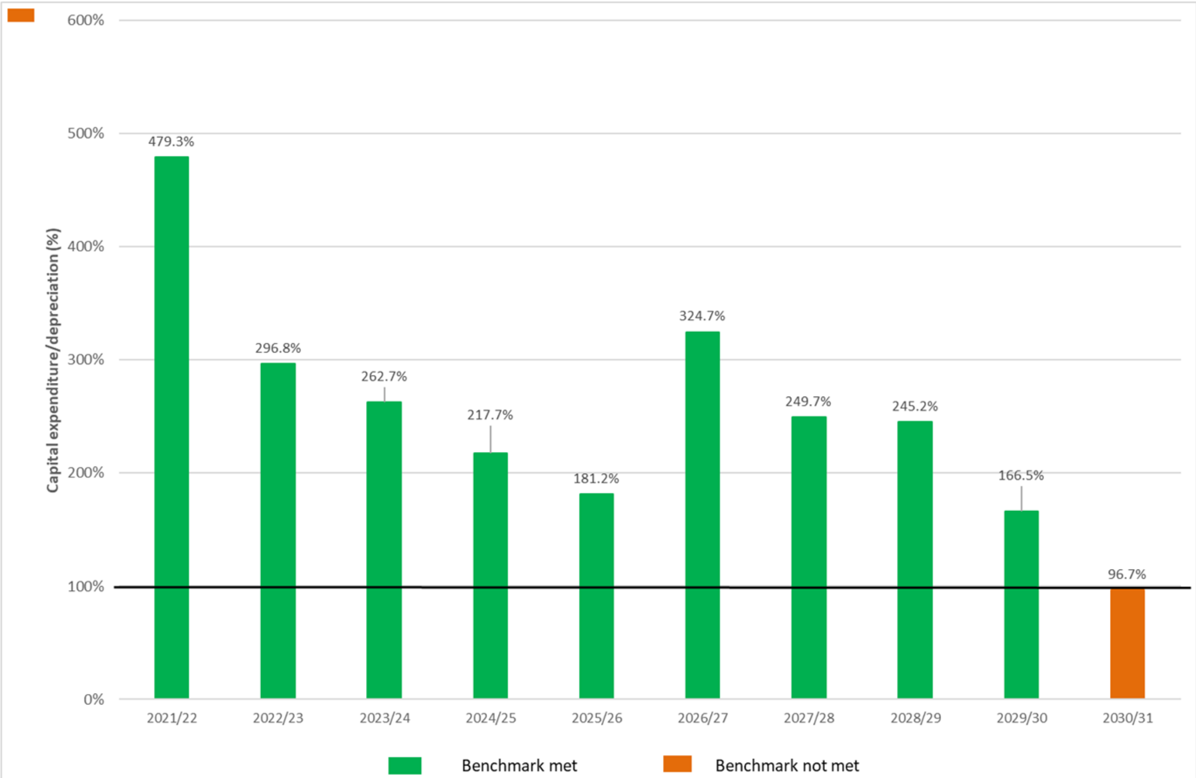
Essential services benchmark

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 the essential services benchmark if its planned capital expenditure on network services equals or is greater than expected depreciation on network services.

In year ten (2030/31), our essential services benchmark is slightly less than 100%. This is due to the required capital works being lower in 2030/31 as we have invested heavily in our capital works programme in the 2021-2030 financial years.



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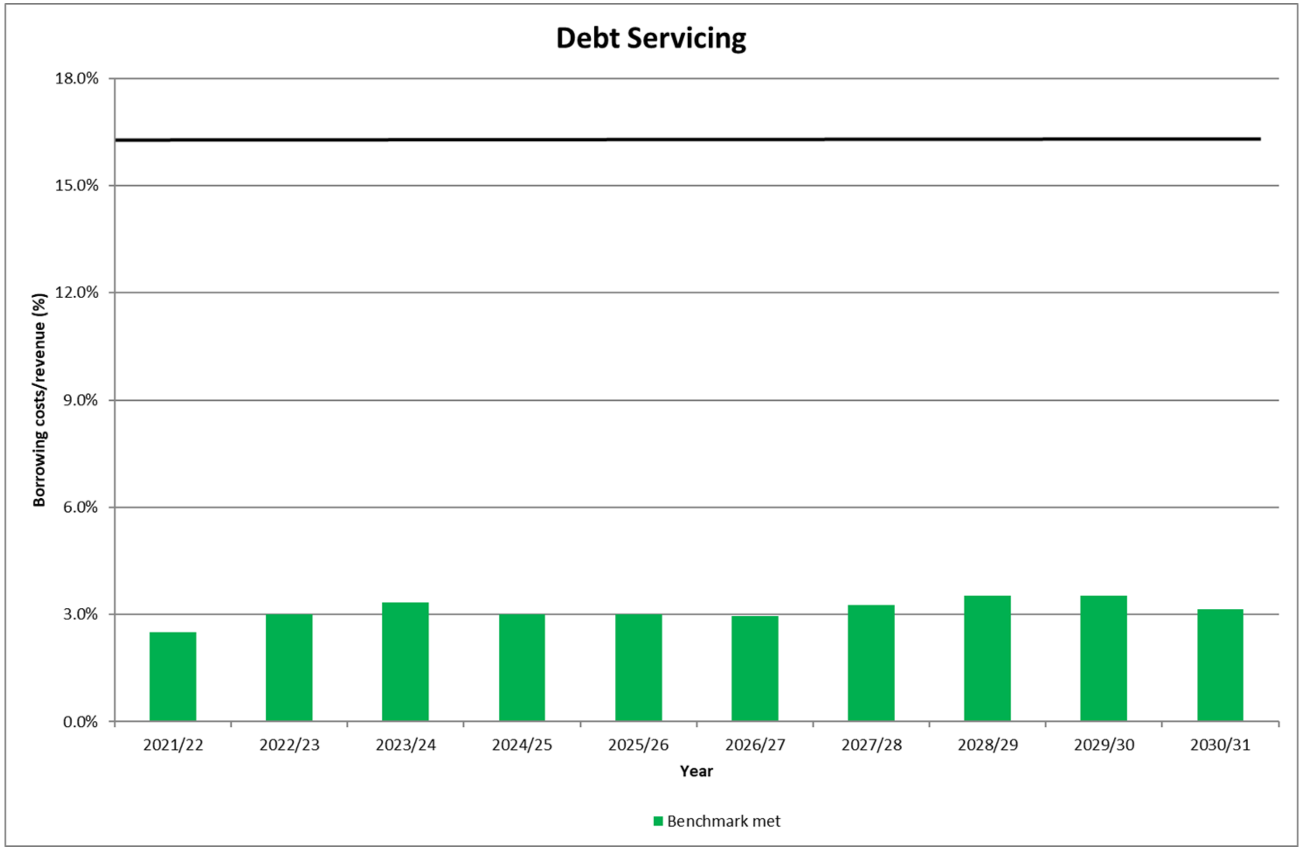
Debt servicing benchmark

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, and equipment).

Because Statistics New Zealand projects the Council's population will grow faster than the national population is projected to grow, it meets the debt servicing benchmark if its planned borrowing costs equal or are less than 15% of its planned revenue.



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