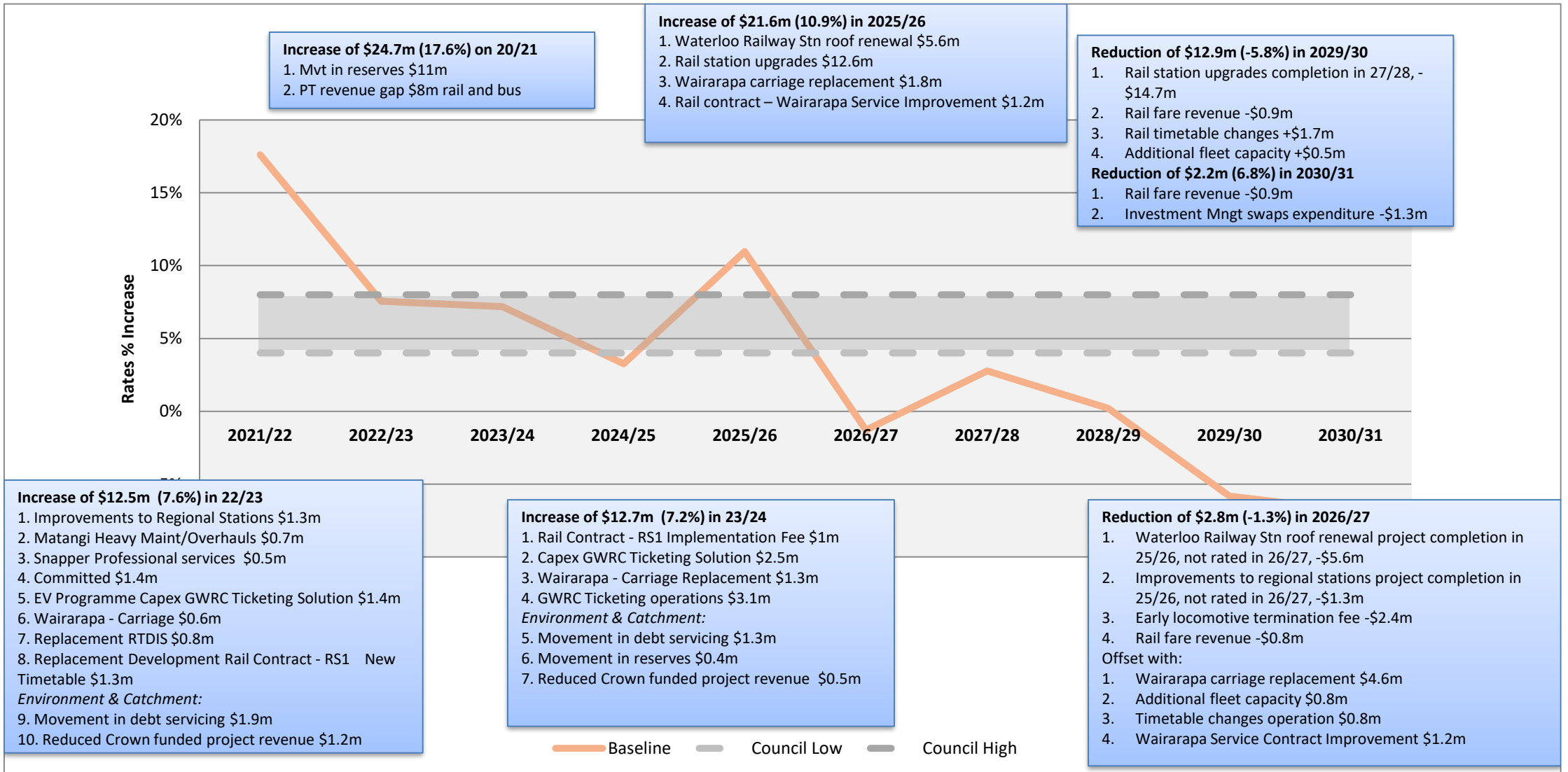


**LTP Financial Tools-
interest rates swap and reserves strategy**

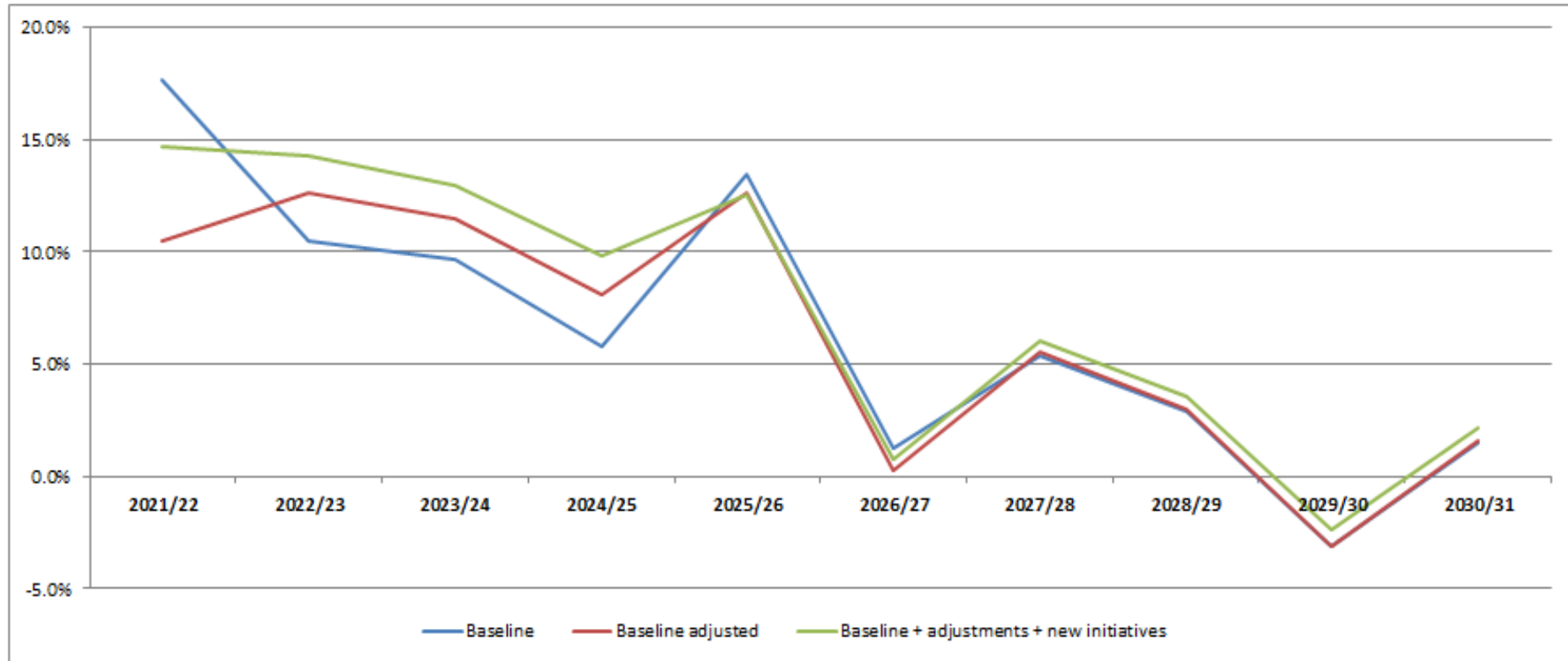
17 November 2020

Baseline without financial tools



Rates % increase without use of PT Reserve

	Excludes PT Reserve									
	Rates % increase									
	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31
Baseline	17.6%	10.5%	9.7%	5.8%	13.5%	1.2%	5.4%	2.9%	-3.1%	1.5%
Baseline adjusted	10.5%	12.6%	11.4%	8.1%	12.6%	0.3%	5.5%	3.0%	-3.1%	1.6%
Baseline + adjustments + new initiatives	14.7%	14.2%	13.0%	9.8%	12.6%	0.7%	6.0%	3.6%	-2.3%	2.2%



Environment – Regulatory Change Impact

Regulatory Initiatives:	2021/22 Yr1	2022/23 Yr2	2023/24 Yr3	2024/25 Yr4	2025/26 Yr5	2026/27 Yr6	2027/28 Yr7	2028/29 Yr8	2029/30 Yr9	2030/31 Yr10
Regional planning - implementing and responding to national direction	1,500,000	2,000,000	2,350,000	2,250,000	2,250,000	1,300,000	1,000,000	1,000,000	500,000	-
Fit for the Future	1,250,000	1,250,000	1,250,000	1,250,000	1,250,000	1,250,000	1,250,000	1,250,000	1,250,000	1,250,000
Wetland mapping and monitoring	-	-	-	140,000	140,000	140,000	80,000	80,000	80,000	80,000
Freshwater Science and monitoring	-	-	300,000	300,000	300,000	300,000	300,000	300,000	300,000	300,000
Facilitating local climate change adaptation processes	-	-	-	-	-	200,000	200,000	200,000	200,000	200,000
Completing whitua development in a more integrated way	-	250,000	250,000	250,000	250,000	250,000	-	-	-	-
Total	2,750,000	3,500,000	4,150,000	4,190,000	4,190,000	3,440,000	2,830,000	2,830,000	2,330,000	1,830,000
Indicative Rates Increase	1.9%	2.5%	2.9%	2.9%	2.9%	2.4%	2.0%	2.0%	1.6%	1.3%

Rates revenue and % increase: PT Reserve modelling

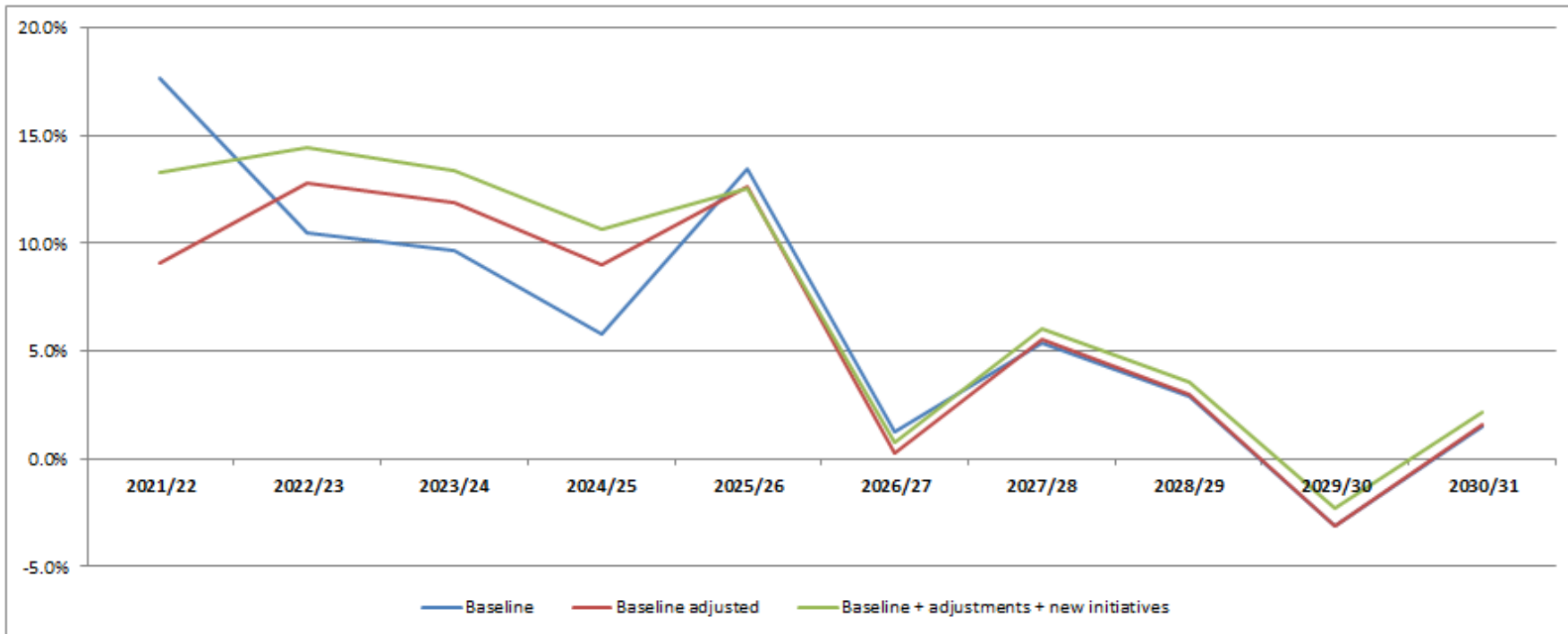
Baseline + adjustments + new initiatives	PT Reserve modelling		
	Rates revenue (Million)		
	2021/22	2022/23	2023/24
Nil reserve utilisation	161.26	179.54	198.33
20% Y1, 7% Y2 and Y3	159.21	178.85	197.63
30% Y1, 7% Y2 and Y3	158.18	178.86	197.64
40% Y1, 7% Y2 and Y3	157.16	178.87	197.66
50% Y1, 7% Y2 and Y3	156.13	178.88	197.67
60% Y1, 7% Y2 and Y3	155.11	178.90	197.68
70% Y1, 7% Y2 and Y3	154.08	178.91	197.69
80% Y1, 7% Y2 and Y3	153.06	178.92	197.70

Baseline + adjustments + new initiatives	PT Reserve modelling		
	Rates % increase		
	2021/22	2022/23	2023/24
Nil reserve utilisation	14.7%	14.2%	13.0%
20% Y1, 7% Y2 and Y3	13.3%	15.2%	13.0%
30% Y1, 7% Y2 and Y3	12.5%	16.0%	13.0%
40% Y1, 7% Y2 and Y3	11.8%	16.7%	13.0%
50% Y1, 7% Y2 and Y3	11.1%	17.5%	13.0%
60% Y1, 7% Y2 and Y3	10.3%	18.2%	13.0%
70% Y1, 7% Y2 and Y3	9.6%	19.0%	13.0%
80% Y1, 7% Y2 and Y3	8.9%	19.8%	13.0%

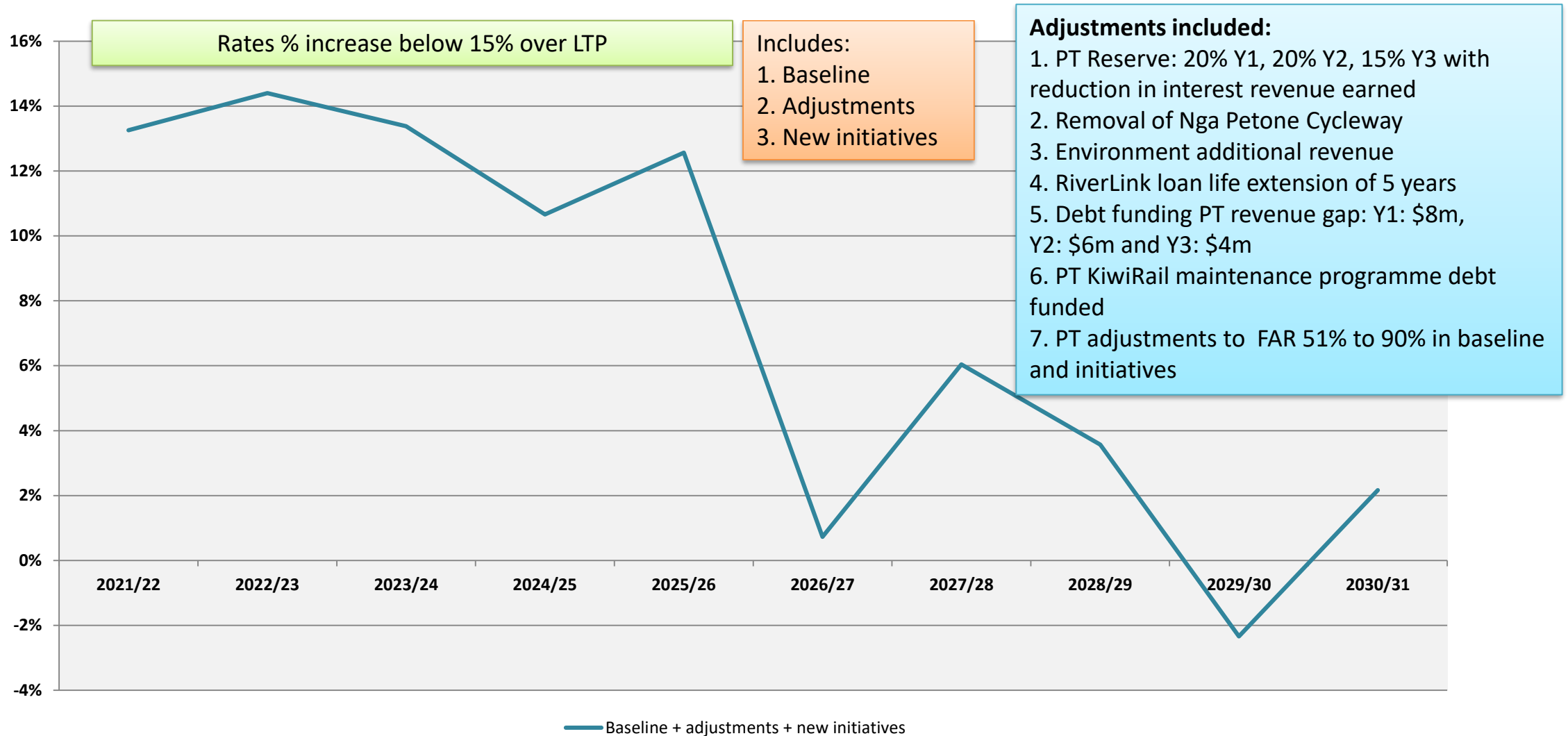
PT Reserve utilisation option: 20% Y1, 20% Y2, 15% Y3

This option keeps the rates increase % below 15% throughout the LTP

PT Reserve: Y1: 20%, Y2: 20%, Y3: 15%										
Rates % increase										
	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31
Baseline	17.6%	10.5%	9.7%	5.8%	13.5%	1.2%	5.4%	2.9%	-3.1%	1.5%
Baseline adjusted	9.0%	12.8%	11.9%	9.0%	12.6%	0.3%	5.5%	3.0%	-3.1%	1.6%
Baseline + adjustments + new initiatives	13.3%	14.4%	13.4%	10.7%	12.6%	0.7%	6.0%	3.6%	-2.3%	2.2%



Rates % increase with adjustments and initiatives



Managing Interest rate risk via Hedging

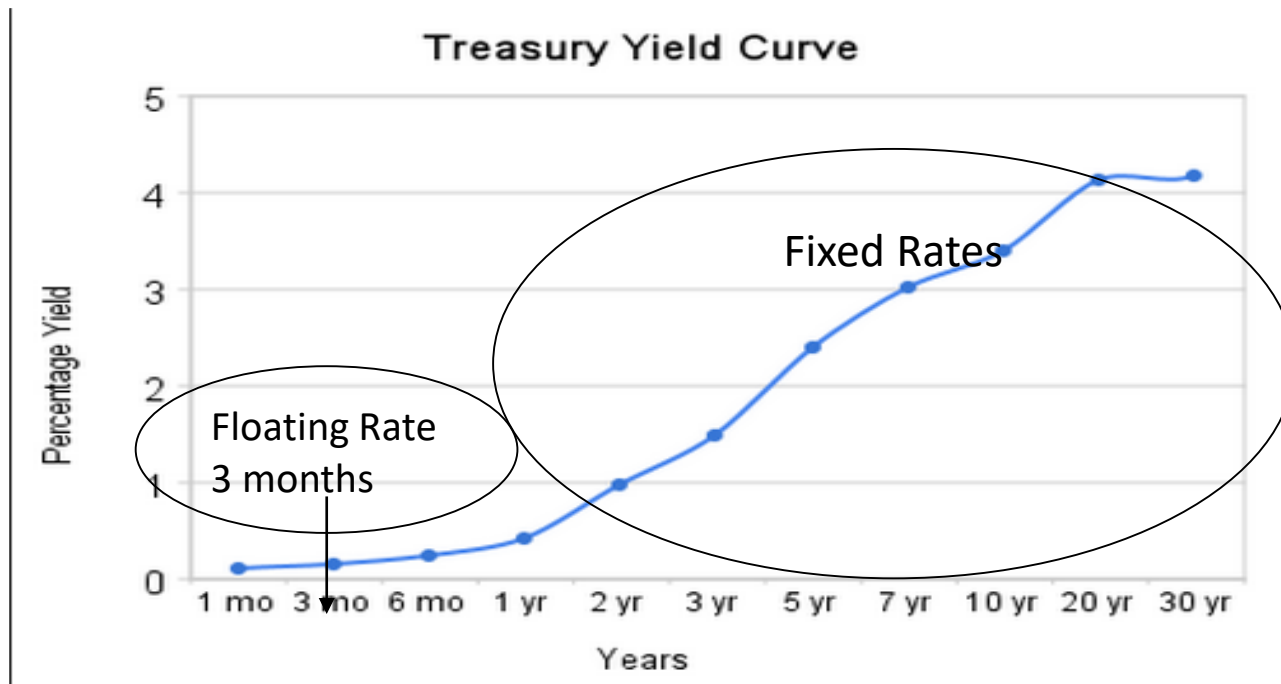


What is Hedging ?

- Hedging is designed to provide certainty
- It's a risk mitigation strategy against fluctuating interest rates, commodities, or foreign exchange movements
- Our discussion will focus on **interest rate hedging**
- What is the risk we are trying to avoid?
- There is a cost to have certainty via hedging, but there could be a even bigger one with taking a risk – i.e. uncertainty
- Finance Strategy – LTP – Financial Prudence (not taking undue risks)

Fixed or Floating rate interest cost ?

- There are two types of interest bearing debt
- **Fixed rate** - the interest rate remains constant over life of the debt
- **Floating rate** - the interest rate on the debt is re-priced generally every 90 days



- **Floating rate** is generally cheaper than **Fixed rate**
- but interest rates change over time
- 90 days is 0.25%, 10 years is 3.5%

How Council manages its Debt

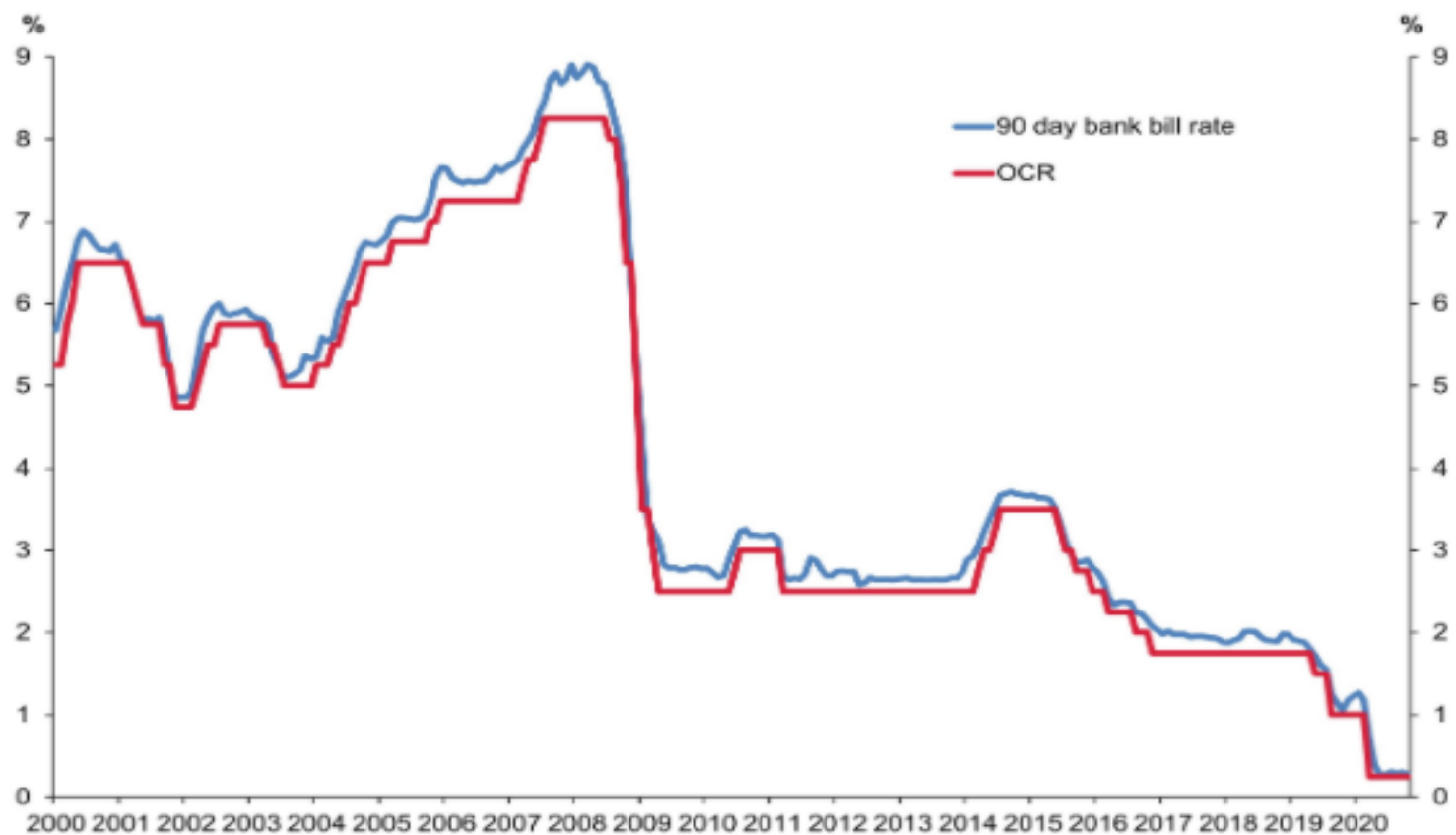
- All Council debt is borrowed at a floating interest rate i.e. re-priced every 90 days
- Funds are borrowed for various terms, overnight, 90 days to up to 17 years
- Interest rates risk on Councils debt is managed separately

Floating Rate Note Long Term Borrowing	LGFA Base Margin	Borrowing Margin AA rated Councils
May-21	13 bps	33 bps
Apr-22	23 bps	43 bps
Apr-23	21 bps	41 bps
Apr-24	23 bps	43 bps
Apr-25	28 bps	48 bps
Apr-26	30 bps	50 bps
Apr-27	37 bps	57 bps
Apr-29	45 bps	65 bps
Apr-33	64 bps	84 bps
Apr-37	73 bps	93 bps

- Our cost to borrow to April 2025 is the 90 day rate plus a fixed margin of 0.48%
- 90 day rate is 0.28% now
- i.e 0.76% for the next 90 days

Graph of 90 day Floating rate over time Current Fixed rate SWAPS 16 Nov

90-day bank bill rate & Official Cash Rate



Source: RBNZ. Monthly averages

SWAPS			16-Nov
3M	Q/Q	Act/365	0.280
6M	Q/Q	Act/365	0.255
9M	Q/Q	Act/365	0.228
1Y	Q/Q	Act/365	0.210
2Y	Q/Q	Act/365	0.205
3Y	Q/Q	Act/365	0.227
4Y	Q/Q	Act/365	0.287
5Y	Q/Q	Act/365	0.370
6Y	Q/Q	Act/365	0.462
7Y	Q/Q	Act/365	0.561
8Y	Q/Q	Act/365	0.659
9Y	Q/Q	Act/365	0.753
10Y	Q/Q	Act/365	0.833

Cost to fix via swap for 5 years to 2025 is 0.37%

Showing our Borrowing portfolio spread

30-Jun-20

Greater Wellington Regional Council

Funding Maturity Chart

0 - 3 years

15%-60%

39%

3 - 6 years

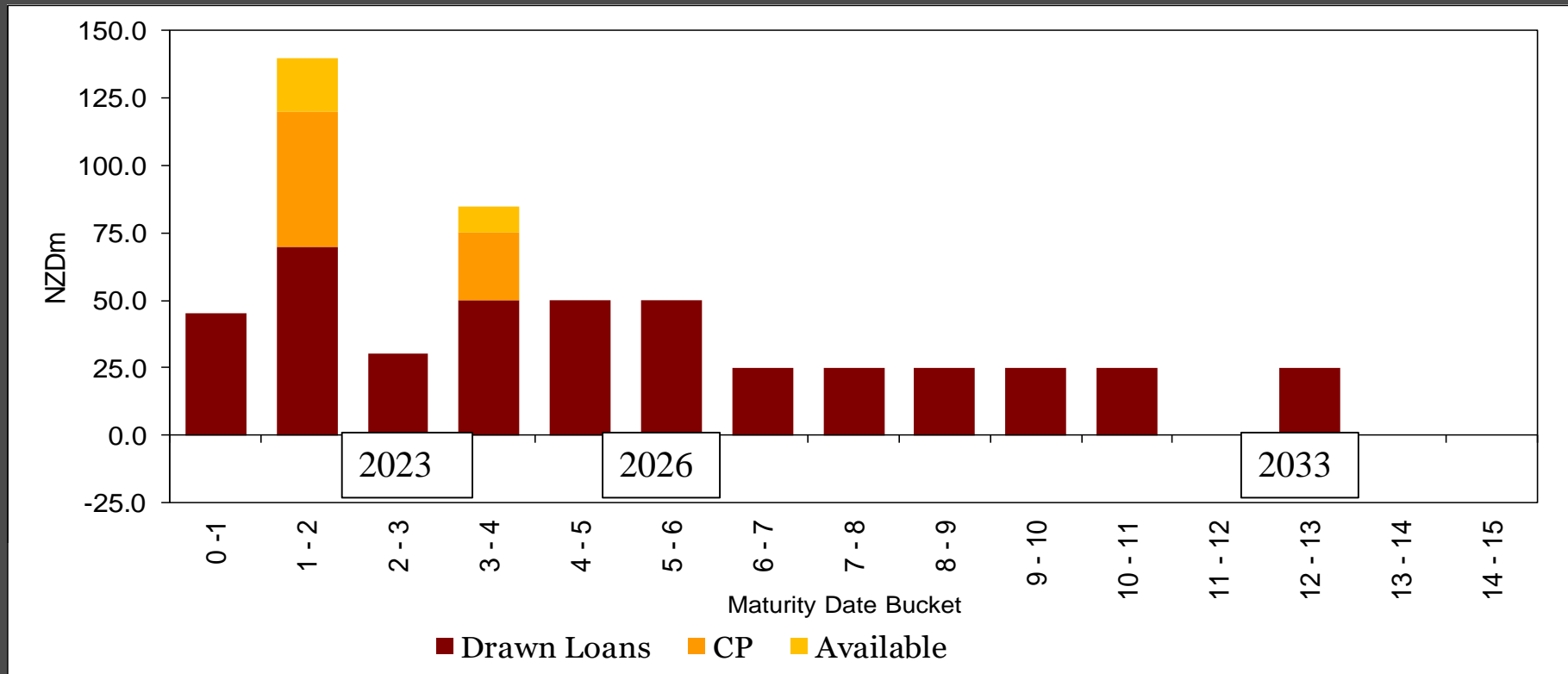
15%-60%

34%

6 years plus

10%-60%

27%



How is the councils interest rate risk managed ?

- The floating interest rate can be switched into fixed rate with an interest rate swap
- An interest rate swap can be for a short time i.e. 6 months or a long time i.e. 17 years +
- We have a portfolio of floating rate interest cost - some overlaid with fixed rate swaps
- **Interest rate swaps are flexible** they can be cancelled, they can be extended or shortened
 - .. Banks are happy to do this More on this later
- Operation of Swaps governed by our Treasury Risk Management Policy

Example of a how a SWAP works

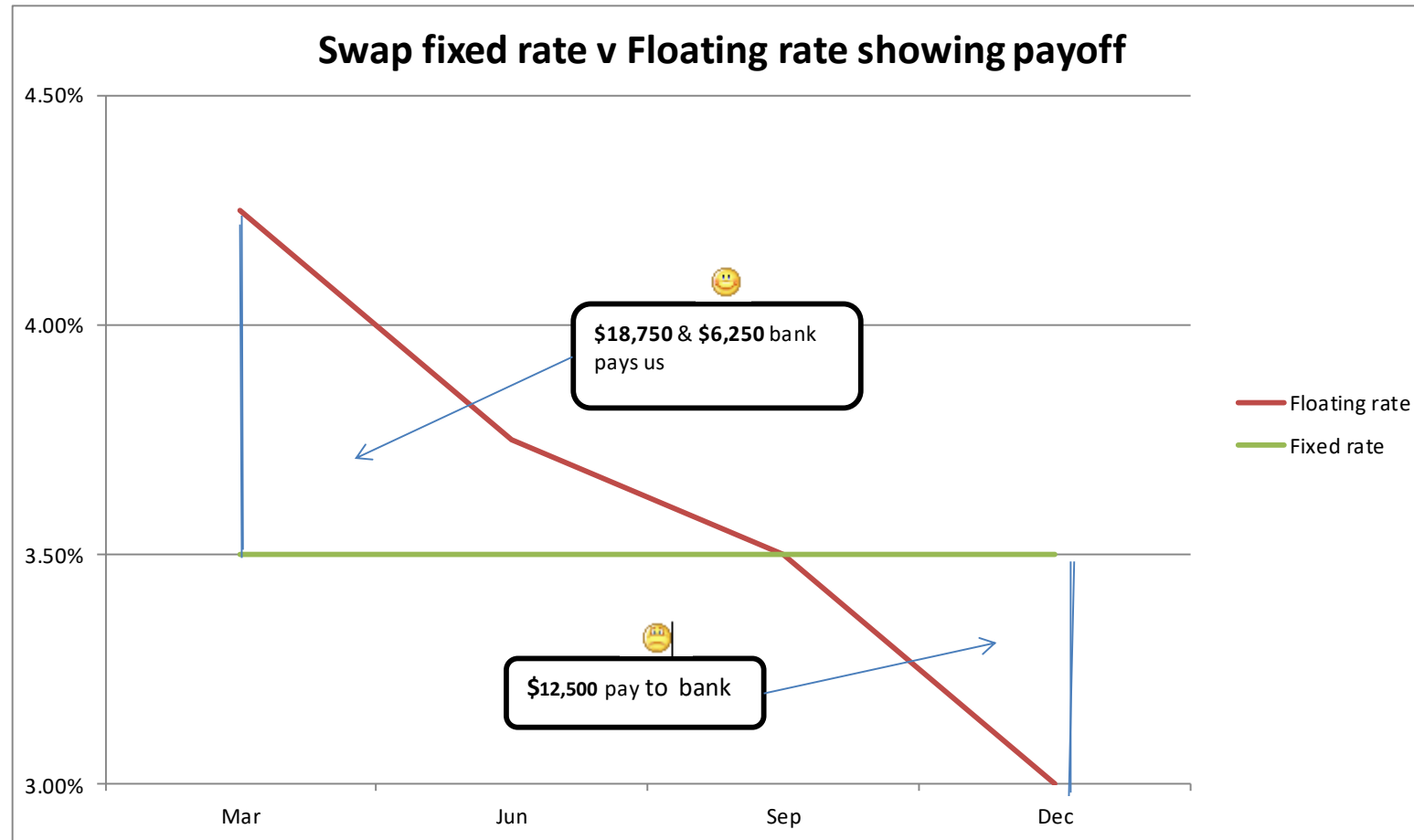
- WRC borrow funds at a floating interest rate (each 90 days the rate is re-priced) and rates determined by the market were:
 - 4.25%, 3.75%, 3.50%, 3.00% on Drawdown, March, June, September,
 - Borrowed \$10 million from LGFA on floating rate note for 1 year
- WRC enters into a swap to ensure a **fixed interest rate for 1 year at 3.50%**

Example of a SWAP

				Debt Payment		
90 day rate	Fixed wap rate	Diff	Net flow of Funds for swap		WRC pays LGFA debt interest based on 90 day rate	Net Position
4.25%	3.50%	0.75%	18,750	Bank pays WRC	106,250	87,500
3.75%	3.50%	0.25%	6,250	Bank pays WRC	93,750	87,500
3.50%	3.50%	0.00%	0	No flow of funds	87,500	87,500
3.00%	3.50%	-0.50%	-12,500	WRC pays Bank	75,000	87,500
GW Net\$ received for swap			12,500		362,500	350,000
						362,500
						12,500

$\$350,000 / \$10,000,000 = 3.5\%$

Example of a SWAP



Treasury Risk Management Policy

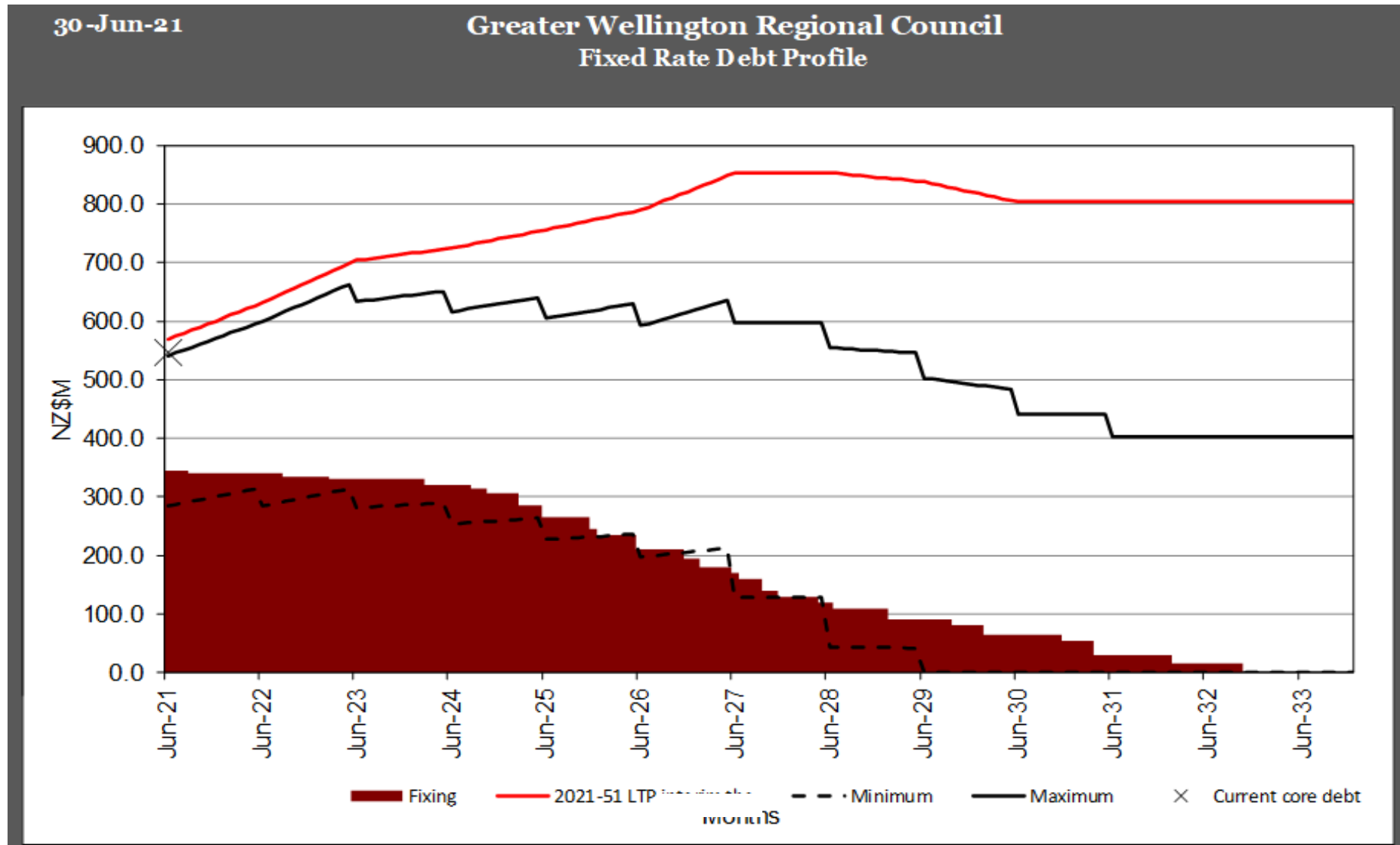
- Policy sets out the parameters under which we manage our interest rate risk
- Reviewed every 3 years, any changes are advocated/supported by our Treasury Advisors –PwC and approved by ELT, FRAC, Council
- Policy provides latitude to take some view on interest rates - reviewed at least quarterly by PwC

Interest rate Hedging Policy parameters – Fixed rate

Debt Interest Rate Policy Parameters

Rolling monthly basis	Debt Period Ending	Debt Forecast	Actual fixed	Actual %	Minimum %	Maximum %	Compliant (Y/N)
30-Jun-21	Current	569	345	59.8%	50%	95%	Yes
30-Jun-22	Year 1	631	315	53.9%	45%	95%	Yes
30-Jun-23	Year 2	704	305	46.9%	40%	90%	Yes
30-Jun-24	Year 3	725	295	44.2%	35%	85%	Yes
30-Jun-25	Year 4	756	240	35.1%	30%	80%	Yes
30-Jun-26	Year 5	789	185	26.6%	25%	75%	Yes
30-Jun-27	Year 6	853	145	19.9%	15%	70%	Yes
30-Jun-28	Year 7	854	95	14.1%	5%	65%	Yes
30-Jun-29	Year 8	838	65	10.7%	0%	60%	Yes
30-Jun-30	Year 9	803	40	8.1%	0%	55%	Yes
30-Jun-31	Year 10	803	30	3.7%	0%	50%	Yes
30-Jun-32	Year 11	803	15	1.9%	0%	50%	Yes
30-Jun-33	Year 12	803	0	0.0%	0%	50%	Yes
30-Jun-34	Year 13	803	0	0.0%	0%	50%	Yes
30-Jun-35	Year 14	803	0	0.0%	0%	50%	Yes

Hedging/Fixed interest rate graphically



SWAP valuations

- Swaps valued regularly, reported quarterly via our management reporting to Council
- Is an Accounting requirement, impact are:
- **Balance sheet** valuation reflect the current position if swaps cancelled today
- **Profit and Loss** account amounts represent the **changes** between years
- Valuations vary as interest rate move up and down and as the swaps are used-up/extinguished

Interest rate SWAPS are flexible

- Currently we have pressure with our LTP .. Can we use swaps to help us out ?
- Yes, anything is possible
- Its like your home mortgage you can easily change the rate ... but there is often a cost
- An **opportunity cost** and a **costs of the bank** to pay
- We can reduce interest costs in the next few years by extending out our swaps
- Simplistically we pay fixed rate 5% for 2 years we can extend and pay 2.5% for 4 years
- But after 2 years if we paid 5% we could pay 0.25% for the next two years instead

Interest rate swaps – Swap extensions – Simple scenario

- \$100m of Debt and a swap on this to pay 5% for 2 years and want to extend 2 years
- Current 90 day floating rate is 0.25% and same for the next 4 years

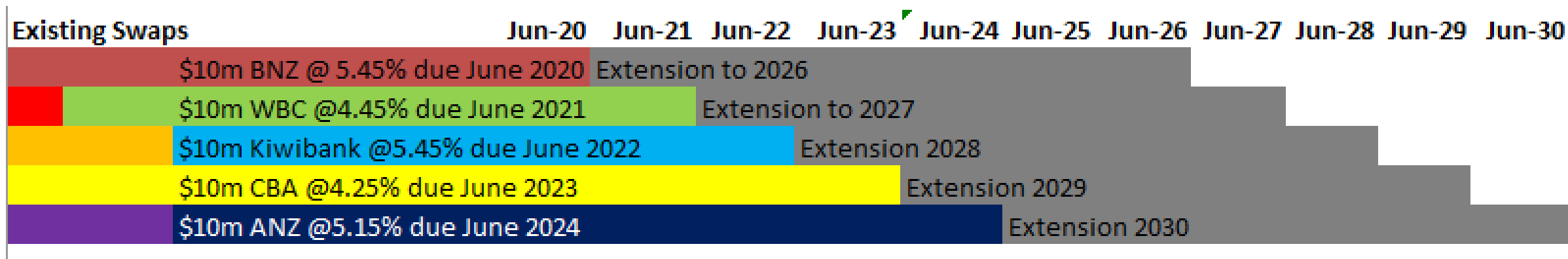
Swap Amount:	100,000,000	Year 1	Year 2	Year 3	Year 4
		Interest rate			
Let swap expire		5%	5%	0.25%	0.25%
Extend & blend swap		2.63%	2.63%	2.63%	2.63%

	Interest cost P&L				Total
Let swap expire	5,000,000	5,000,000	250,000	250,000	10,500,000
Extend & blend swap	2,630,930	2,630,930	2,630,930	2,630,930	10,523,720
P&L Saving/(Cost)	2,369,070	2,369,070	(2,380,930)	(2,380,930)	
Time value of money cost					(23,720)
Bank Fees - to be imbedded into swap	(150,000)	(150,000)	(150,000)	(150,000)	(600,000)
Total P&L cash flow & bank charges	2,219,070	2,219,070	(2,530,930)	(2,530,930)	(623,720)

Cost of transaction at 15 points (0.15%) on \$100m over 4 years in this example - typically extensions are longer

What an extension looks like

Proposed extension



Completed extension



Extension scenario 1 – Target \$2m per year over next 3 years

- Asked PwC to provide scenario of targeting saving of \$2m over first 3 years of LTP.
- Includes bank charges amounting to \$2,200,000
- Amends \$160 million of swaps
- Average extension 9 years
- Terminal interest rates 2.6%

Interest Cost Savings (Per FY)

FY 2021	1,802,925
FY 2022	3,205,849
FY 2023	1,866,944
FY 2024	1,597,126
FY 2025	646,985
FY 2026	(1,063,490)
FY 2027	(2,244,518)
FY 2028	(2,249,291)
FY 2029	(2,013,187)
FY 2030	(1,826,689)
FY 2031	(1,579,109)
FY 2032	(290,678)

Extension scenario 2 – Optimise Blend & Extend – rate reduction

- Asked PwC to provide scenario to optimise best value saving on extending high interest rate swaps
- Includes bank charges of \$650,000
- Amends \$60 million of swaps
- Average extension 7 years
- Terminal interest rates 2.5%

Interest Cost Savings (Per FY)

FY 2021	1,017,678
FY 2022	1,075,136
FY 2023	(81,126)
FY 2024	(346,750)
FY 2025	(1,033,267)
FY 2026	(910,887)
FY 2027	(458,272)
FY 2028	(56,323)

Advantages of blend and extending swaps

- Can provide immediate interest cost savings
- Lowers average interest rate in early years
- Regret factor on execution is presently low, rates can go lower but limited

Disadvantages of blend and extending swaps

- While initial saving, costs are increased in later years
- There is a cost to complete transaction – can be expensive
- There is no competitive pricing, have to take banks charges, or abandon
- Changes can range from 0.05% per annum to 0.20% depends on bank and market conditions
- Can create problems in latter years as cost reverse

Recommendation

- There is no right or wrong answer
- Economically it does not stack up because of the bank costs, these are spread.. nevertheless are to be paid
- Would not do this in the ordinary course of business unless there is an imperative
- What are our advisers recommending .. As above.