Lake Clearwater Country
Kelly Bisset

Part 10

FINANCIAL STRATEGY

Financial Strategy

Introduction

The financial strategy outlines how Council will manage its finances over the next ten years. It sets out the general approach and principles that will be followed, and it provides a guide to assess spending proposals. The financial strategy includes limits on rates levels, rates rises and borrowing and aims to promote financial stability, affordability and value for money over the short, medium and long-term.

The strategy also helps Council to engage transparently with the community about the impact of our proposals on service levels, rates, debt and investments.

Council's financial goals for the coming ten years are to:

1. Ensure Council remains financially stable, while financing key priorities
2. Spend money prudently to deliver agreed levels of service, cater for growth and manage assets soundly.
3. Ensure rates and fees are kept to a reasonable level
4. Provide clear financial parameters for Council work programmes.

Council's funding strategy is summarised as the following

- Operational expenditure – rates are used to fund the balance of operating expenditure after all other revenue streams are accounted for, and
- Capital expenditure – rate for depreciation and then loan fund for the shortfall between capital expenditure and funded depreciation.

Ashburton District's Changing Economy

While Ashburton District's agricultural economy used to depend heavily on sheep, beef and grain, improvements in irrigation have underpinned a shift toward dairy and more specialised crops. This change in land use, along with continued growth in agricultural support businesses and primary product processing, has seen the district's economic base expand and the population grow strongly over the past 10 years.

Ashburton District's Gross Domestic Product was $1.845 billion for the year to March 2016. This was an increase of 4.0%, compared to the previous 12 months. New Zealand's gross domestic product increased by 2.5% over the same period.

Long-Term Population Projections [1]	2013	2023	2033	2043	Change
Ashburton District	32,300	36,300	39,200	41,900	9,600 (30%)

The Impacts of Change

- **Roading** - Population growth, land use changes and an increase in heavy traffic have placed significant pressure on our roads. Council recognises there is strong community demand to improve the condition of our roads, and we have increased our budget for road maintenance and upgrade expenditure accordingly. This will result in an increase in rates and loan funding for cyclic renewals.
- **Community Facilities and Services**- Catering to our growing population and changing community expectations has also led to improvements in the community services and facilities provided by Council. The last few years have seen a significant increase in the levels of service provided, including the opening of the EA Networks Centre and Ashburton Art Gallery and Heritage Centre.
- **Infrastructure** – The increased population and new developments have also created the need for infrastructure upgrades and extensions, particularly for water supply and wastewater. With changing water quality standards as a result of the Havelock North water contamination issue, Council has been proactive in planning for the anticipated legislation changes to upgrade water treatment facilities throughout the district on a cyclic basis. Details on this are contained within the Infrastructure Strategy.

The financial strategy details how Council plans to fund the additional costs and operate within limits set on rate levels, rate increases and borrowing levels.

Key Issues

Population Growth

Ashburton District is one of New Zealand's fastest growing rural districts with a population increase of 31% since 2001 (approx. 1.9% p.a.). This period of rapid but consistent growth follows an earlier period of little or no growth. Current and projected population growth impacts the way Council plans and funds services and assets.

Long-term population projections (to 2043) have been developed based on consideration of historic trends, Statistics NZ projections (to 2043), drivers of growth and constraining factors.[1]

Statistics NZ publish high, medium and low population projections. The February 2017 'high' projection suggests sustained growth at slightly lower than present rates (averaging 1.3%), while the low projection shows a population plateau at about the current level. Both the low and medium projections have been revised upwards since the previous release in 2010, while the high projection remained similar.

By 2043 the projected population is expected to be in the range of 36,000 (low growth) to 47,000 (high growth). Council has adopted the medium projections for demand planning purposes. Projections beyond 2043 are not currently published by Statistics NZ, so these need to be extended to support the 30-year Infrastructure Strategy (2018-48).

The current average number of residents per household is 2.5; however, one-person households are projected to increase by 42% by 2038. Over this same period, approximately 3,300 additional homes will need to be built.

Impact of Population Growth

Population growth leads to additional rateable properties, increased load on Council infrastructure and assets and increased service demand. If our population increases by the number forecast, we will need to cater for an additional 165 homes in the district each year. The increase in population is likely to be greatest in the towns of Ashburton, Methven and Hinds and as urban residential areas grow.

Ashburton, Methven and Hinds (particularly Lake Hood) are well served with network infrastructure and can accommodate expected population growth with additional capital for water services and increased operational expenditure.

Council plans for population growth when undertaking renewals of network infrastructure, particularly with water and wastewater. In addition to this, developers help fund additional capacity through development contributions.

Other Council services are likely to experience an increase in demand. It is expected this will be catered for with existing resources and will have little impact on Council's ability to provide services or on the cost providing the services.

The additional population and resulting households increase Council's rating base. This assists with funding the costs associated with growth and maintaining levels of service. If there were an additional 165 homes in the district in a year and each paid rates of $2,000 this would increase Council's revenue by $330,000 – currently just under 1% of Council's rate requirement.

	2018/ 19	2019/ 20	2020/ 21	2021/ 22	2022/ 23	2023/ 24	2024/ 25	2025/ 26	2026/ 27	2027/ 28
Rateable properties	16,819	16,943	17,066	17,190	17,313	17,437	17,561	17,684	17,808	17,931

Rural Land Use Changes

Most land in the Ashburton District is rural farmland. Ashburton District has the highest concentration of irrigated land in New Zealand and the area of irrigated land continues to increase. Irrigation enables land use changes, leading to a reduction in dry stock and arable farming, an increase in dairy farming and high-value cropping such as seeds.

Impact of Rural Land Use Change

The majority of land conversions to dairy farming have occurred and the rate of land change has slowed. The projected areas for future growth are in new residential developments such as Lake Hood.

Most rural properties in the district provide their own drinking water and dispose of their own wastewater which require consent from Environment Canterbury. As long as they are compliant, these practices have little impact on Council provision of these services.

Ashburton roads have seen heavy increases in daily traffic. Milk tankers and other heavy traffic has increased by 20%, causing more wear and tear on our rural road network, and some rural roads are now showing signs of premature failure. Council funds for depreciation on its roading assets for a 15 year renewal cycle, but the roads are deteriorating faster than the depreciation funding allows for and often need significant repairs within 10 years.

1 Statistics NZ, 2017 Projections

With new technology and better monitoring systems in place, Council now has a clearer picture of the conditions of the roading network. Strengthening parts of the district's road network is required, particularly for main arterial routes with heavy traffic. To maintain the current levels of service, loan funding for cyclic renewals is being used for the first three years of the Long Term Plan 2018-28 to undertake this strengthening work. However, loan funding for cyclic renewals is not the preferred option in the long-term as it is not financially prudent. To maintain the current levels of service without loan funding, Council would have to charge higher rates which may be unaffordable for the wider community. Hence, eventually, Council will have to rationalise its work program to prioritise the most critical roading issues. This will mean the focus for the roading program will be on the roads under heavy use, with lateral roads (often unsealed or sealed roads to remote rural properties) being placed lower on the priority list for renewal work.

As roading is important to the community, Council is advocating to New Zealand Transport Authority for an increase in funding to help it maintain the current levels of service. With Ashburton District roads being considered by NZTA to be one of the better maintained networks, it is unlikely the request for additional funding will be successful ahead of other districts with greater roading issues.

Urban Land Use

Ashburton, Methven and Hinds (particularly Lake Hood) are the main urban growth areas of the Ashburton District. These areas continue to have new residential developments on the urban periphery of each town, expanding the urban footprint into surrounding rural and rural-residential areas.

In the review of the District Plan, which was adopted in August 2014, areas of future growth were identified for Ashburton, Methven, Hinds and Rakaia. There are sufficient residential and commercial sites available or planned to accommodate current foreseeable growth for some years, and there may be over-capacity for residential land in the Ashburton North area. The changes and land zoning in the reviewed District Plan makes further future development in areas identified more straightforward.

New network infrastructure within a new subdivision development must be provided by the developer and vested in Council. There are normally no capital costs to Council on the development site itself. Council charges development contributions on new houses and business premises, which helps fund Council's investment in its wider network infrastructure to ensure growth is catered for.

Smaller villages in the district have some potential for growth, but this may be limited by access to network infrastructure. None of the village have reticulated wastewater schemes, instead using on-site treatment or storage and disposal of wastewater. Compliance requirements can make this a costly option, limiting growth in these villages. Council has no plans to develop wastewater schemes in any villages but will continue to talk with village communities about options and preferences for the future.

Earthquake-Prone Buildings

Ashburton District suffered less damage from the Canterbury earthquakes that occurred seven years ago than districts to the north of the Rakaia River.

Detailed engineering assessments post-quake resulted in several buildings being demolished, particularly in the Ashburton central business district. However, there are still a number of buildings that owners have yet to determine their future plans on whether they will demolish or strengthen. In the land that has become available within the CBD, new developments have started to be built and are looking for tenancies.

The Building (Earthquake-prone Buildings) Amendment Act 2016 outlines the timeframes that building owners have to strengthen their buildings to code. Within Ashburton District, 155 buildings will have "earthquake prone" placards placed on their buildings with timeframes ranging from 6-25 years to comply with the New Building Standard of 34%.

As Council does not have an adequate IL4 building to perform its Civil Defence duties in times of emergencies, a purpose-built IL4 portable building is being built to house Council Chambers and Civil Defence Emergency Operations until the new Civic Administration and Library Building is built in the next few years.

Balancing the Budget

Council is required by law to ensure that our budgeted operating revenue is enough to meet our operating expenses each year (a balanced budget).

Council may set projected operating revenues at a different level from that required, if it is financially prudent to so do, having regard to:

- The estimated cost of providing targeted levels of services, including the expected cost of maintaining asset integrity and service capacity

- The projected revenue available to fund the cost of maintaining asset integrity and service capacity
- The equitable allocation of responsibility for funding the provision and maintenance of assets and facilities throughout their useful life
- Council's funding and financial policies.

The work programmes and budgets included in this Long Term Plan 2018-28 show a balanced budget in all years.

Inflation

Council is required to budgeted for an inflation adjustment in each year of the Long Term Plan. All budgets in the Long Term Plan have been adjusted for expected price movements over the next 10 years.

Council's costs reflect the type of work it undertakes for the community and are significantly affected by the price of items such as energy, bitumen and civil contracting services. This is quite different from the average household and so using the Consumer Price Index (CPI) to forecast increased costs for Council is not appropriate.

Price level adjustments in the Long Term Plan have been derived from forecasts prepared for Local Government New Zealand by Business and Economic Research Limited (BERL) and deal primarily with areas of expenditure local authorities are exposed to through their business. These price adjusters are referred to in the strategy as the Local Government Price Index (LGPI) and have been used as part of Council's setting of limits on rates and borrowing.

For more information on the BERL local government price adjusters (LGPI) go to ***www.ashburtondc.govt.nz.***

Funding Activities Through Rates

Council allocates the cost of activities according to those who benefit (or those who have a negative impact) through the Revenue and Financing Policy, which applies appropriate funding mechanisms to suit.

Funding mechanisms relating to rates are:

- Uniform Annual General Charge (UAGC)
- General rates applied on a capital value basis
- Targeted rates applied as a Uniform Annual Charge (UAC)
- Targeted rates applied on a capital value basis.

Section 21 of the Local Government (Rating) Act 2002 states that the total amount of rates collected using a Uniform Annual General Charge and Uniform Annual Charges must not exceed 30% of the total revenue from all rates. This limit excludes Uniform Annual Charges set for water or sewerage (wastewater) disposal.

In 2017 Council collected 28% of its rates using the UAGC and UAC (excluding water and sewerage). This is forecast to increase to a maximum of 29.6% in 2019/20, which is at our rate limit for UAGC. This is primarily due to:

- The movement towards funding community-wide benefit activities from general or targeted rates towards UAGC. These include additional funding for community pools, community halls, and all community grants now being funded through the UAGC.
- The EA Networks Centre's operating and loan costs which are funded from the UAGC.
- The reduction in investment income after using reserves to fund the Civic Building upgrade. (Council investment returns are pro-rated between the UAGC and the general rate with the effect that the UAGC is normally reduced, and the general rate increased).

While Council is within the statutory limit, it is increasing the percentage of rates being collected by way of a fixed charge, which impacts on the lower valued properties.

Council believes this is an appropriate strategy, although acknowledges the potential impacts. We are aware that coming close to the 30% cap could restrict future funding mechanisms, particularly increases to the UAGC and UAC.

Rates Over the Coming 10 Years

Rates Revenue

Rates are one source of Council's revenue. Other sources include fees and charges, government transfers and investment returns. Rates are a form of property tax and must be paid by all property owners in the district.

Rates are an important source of revenue for all councils. The percentage of Ashburton

District Council's annual revenue that comes from rates varies from year to year and over time - for the 2016/17 year it was approximately 47%. Other revenue comes from fees and charges, government subsidies, investment income and a variety of other sources.

Council has kept rate increases over the 10 years covered by this Long Term Plan to a minimum, while recognising there are upward pressures on rates. These pressures include:

- Operational and loan servicing costs of the EA Networks Centre
- Capital expenditure to improve roading

Rates Limits

The Long Term Plan 2018-28 has been prepared based on the following limits on total rates and annual total rates increases:

- Total rates in any one year are to be no greater than 1% of the total capital value of the district
- Total rates increase for the 2018/19, and 2019/20 to be no greater than 6% plus LGPI each year
- Total rates increase for the years 2020/21 – 2027/28 to be no greater than 3.0% plus LGPI each year

	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28
Rates as a % of District capital Value	0.21	0.21	0.21	0.20	0.19	0.19	0.18	0.18	0.17	0.17
Rate Increase (%)	4.5	5.7	5.0	0.4	3.6	2.0	2.1	2.1	1.8	1.3
Average LGCI Adjustment (%)	2.0	2.2	2.2	2.2	2.3	2.4	2.4	2.5	2.6	2.7
Rate increase before LGCI adjustment (%)	2.5	3.5	2.8	-1.8	1.3	-0.3	-0.3	-0.4	-0.7	-1.4

Explaining Council's Rate Limits

Council has set a higher rates increase limit for the first two years of the Long Term Plan 2018-28 due in part to changes to the increased operating costs of four activities - roading, drinking water, wastewater and the EA Networks Centre.

The impact on the increase in total rates on the first four years is as follows:

	2018/19	2019/20	2020/21	2021/22
Drinking water	1.0%	1.0%	0.3%	0.1%
Roading	1.8%	0.8%	3.1%	-2.9%
EA Networks Centre	1.0%	-0.3%	0.2%	0.8%
Wastewater	0.1%	1.0%	0.6%	1.1%
Combined impact	4.0%	2.6%	4.2%	-1.0%
Residual rates Increase	0.5%	3.1%	0.8%	1.3%
Total rates increase	4.5%	5.7%	5.0%	0.4%

Please note: the table above shows total rates and does not reflect the impact on individual ratepayers.

Council has decided rate increases in total rates for each year are to be no greater than:

- **2018/19 – 2019/20**: 6% + Local Government Price Index
- **2020/21 – 2027/28**: 3% + Local Government Price Index

It is Council's view that existing levels of services can be maintained and any increases to service levels can be managed within these limits. This view is reflected by the financial projections contained in the Long Term Plan 2018-28.

Keeping Within the Rate Limits

Council is proposing some budgeting approaches to keep within the rates limits set in this strategy. Specifically, they are:

- Deferring the design of the Ashburton Resource Recovery Park compactor building from 2018/19 to 2020/21 of $200,000.
- Deferring the construction of the Ashburton Resource Recovery Park compactor building of $5.4 million from 2019/20 and 2020/21 to 2021/22 and 2022/23.
- Deferring capital works on the Ashburton Resource Recovery Park from year 1 to year 2 of $261,000, the Methven Drop-Off from year 3 to 4 of $128,000, the Rakaia Resource Recovery Park from year 1 and 2 to year 4 and 5 of $401,000 and Ashburton Recycling from years 1 and 2 to years 3 and 4 of $390,000.
- Loan funding in year 1 and 2 the shortfall on capital works programmes in Roading rather than rate funding. This amounts to $850,000 in year 1 and $900,000 in year 2.
- Removal of discretionary cyclic renewals of $150,000 in year 1 from Ashburton Water Supply.
- Deferring development of new sportsfields surrounding EA Networks Centre from year 2 and 3 to year 4 and 5 to enable sports groups to fund 50% of the development costs. The total development cost has been budgeted at $4.8 million.
- Strategic use of forestry revenue and reserves – in the past Council has used forestry revenues and reserves to offset rates. Council is proposing to continue to use this approach and sell off forestry land after the harvest of mature trees. It intends to utilise in year 1 $496,560 to offset rates.

Operating Expenditure

Services and day-to-day asset maintenance are paid for using operating expenditure. Council needs to ensure it raises enough revenue each year to cover its forecast operating expenditure (including depreciation), unless it considers it prudent not to do so.

Council's operating expenditure has risen nearly 20% in the past five years. Key drivers behind this expenditure have been:

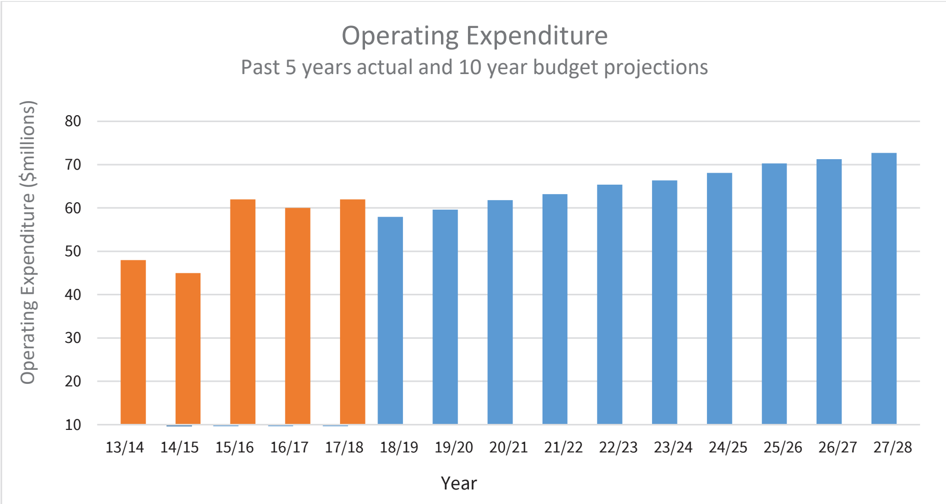
- Inflation costs
- Increased overhead costs for many Council activities (i.e. EA Networks Centre, Ashburton Museum)
- New community services and facilities.
- Servicing interest costs on debt for capital expenditure

Council has budgeted for operating expenditure to increase from $58.0 million to $72.6 million (or approximately 25%) between July 2018 and June 2028.

The increase is the result of:

- **Price increases** – contract fees and inflation mean it costs more to do business
- **Service level increases** –Council is providing a higher level of service in some areas.
- **Growth** – Council expects to cater for population growth of 9% over the next 10 years.

The following graph provides a breakdown of forecast operational expenditure.



Note: 2017/18 has been estimated based on Council's Annual Plan 2017/18.

Capital Expenditure

Capital Renewals and Depreciation

Council owns and operates significant network infrastructure assets on behalf of the community. These assets are the district's road network and the Council owned water, wastewater, stormwater and stockwater networks. To undertake this responsibility effectively, Council must:

- Invest in new assets to provide for growth
- Replace assets as they reach the end of their useful life
- Invest in new or improved assets to improve levels of service.

In general, Council looks to at least maintain current levels of service and facilities. Each year, we need to ensure enough work is done to maintain our assets and, when necessary, to rebuild or replace them.

Council has developed an Infrastructure Strategy which identifies significant infrastructure issues and outlines options for managing these over the next 30 years.

Capital renewal work programmes and budgets have been prepared based on agreed levels of service for each activity, which are set out in detail in the activity sections of the Long Term Plan. The total cost of delivering this programme is expected to be $143 million over the 10 year period. The total cost by activity group is shown below. More information on which activities are in each group and expenditure details can be found in the activity sections of the Long Term Plan.

As assets wear out, funding is put aside to pay for their eventual renewal – this is called depreciation. Depreciation is included in Council's operating expenditure. Different assets have different expected useful lives – the time you can expect them to work efficiently before they need replacing.

Depreciation funding is rated for according to the replacement value of the asset divided by the expected useful life of the asset. Over time, this builds a fund for replacing the asset. This approach to funding is fair as ratepayers who use the asset over its lifetime will fund its eventual replacement (rather than just the ratepayers at the time that the asset is replaced). This is the principle of intergenerational equity.

Council can choose the approach it will take to funding depreciation, ranging from fully funding it, to not funding it at all. In general, Council fully funds depreciation on its network infrastructure assets. Notable exceptions to this are:

- **Road formation** – the base formation of the road. This is not depreciated, and expenditure required to maintain or upgrade the road formation is rated for in the year it is to be spent
- **Stockwater races -** Depreciation is not funded and expenditure required to maintain or upgrade water races is rated for in the year it is to be spent
- **EA Networks Centre –** Depreciation is partially funded to the level of required loan repayments. Council does not believe it is appropriate to fully fund depreciation on this relatively new asset. Council is funding 100% of depreciation on items with a useful life of less than 12 years, and 50% of depreciation on those with a useful life of between 12 and 15 years. Council does not fund depreciation on anything with a useful life of greater than 15 years.

If depreciation funding is insufficient to cover the cost of asset renewal, Council will normally loan fund the asset replacement. The cost of borrowing is funded according to the funding mechanism(s) specified in Council's Revenue and Financing policy.

Council recognises that funding depreciation, as well as loan repayments and interest, is unfair on existing ratepayers, as they effectively pay for both current and future renewal at the same time. In situations like this, depreciation funding is used to pay loan principal repayments. This approach also avoids significant increases and decreases in rates as loans are raised and repaid.

The following capital renewal expenditure is budgeted for network infrastructure activities over the coming 10 years to ensure Council can continue to provide current levels of service.

Activity	2018/19 $000	2019/20 $000	2020/21 $000	2021/22 $000	2022/23 $000	2023/24 $000	2024/25 $000	2025/26 $000	2026/27 $000	2027/28 $000
Drinking Water	1,187	1,756	1,296	1,286	1,225	1,608	1,447	1,419	1,638	1,669
Wastewater	1,759	1,661	4,911	1,974	1,750	1,604	1,852	1,615	1,736	1,654
Stormwater	0	0	0	0	0	0	0	0	0	0
Stockwater	0	0	0	0	0	0	0	58	0	0
Transportation	8,894	9,086	9,282	9,461	9,667	9,905	10,128	10,238	10,459	10,832

When making renewal decisions, Council looks at the current level of service provided, what should or could be provided, and assesses these against our targeted community outcomes and priorities. Council also considers what is appropriate and affordable for the community.

New Capital Expenditure

The Long Term Plan 2018 - 28 details the levels of service Council aims to deliver over the next ten years. These levels of service are determined by considering the following:

- **Legislative compliance** – some activities have levels of service set by legislation or resource consent requirements. This includes drinking water standards, wastewater collection, treatment and disposal and solid waste disposal.
- **Community outcomes and strategic priorities** – Council identifies the goals it should work to achieve to best serve the community. This process enables levels of service to be identified.
- **Community expectations** – Council monitors community expectations in a variety of ways including an annual residents' survey, discussions with community groups and residents, and consultation processes for the Long Term Plan, the Annual Plan and specific projects.
- **Political mandate –** Councillors are elected every three years to represent the community and make decisions on their behalf. This can include decisions about levels of service that Councillors believe are in the best interests of the community, even if some people disagree. This is an essential part of the democratic process.

Capital Expenditure Requirements

Capital expenditure (including renewals) is budgeted to be $24 million in 2018/19 and $30 million in 2019/20, due primarily to investment in road improvements, water, wastewater and stormwater improvements, new Administration and Library Building and the EA Networks Centre climbing wall.

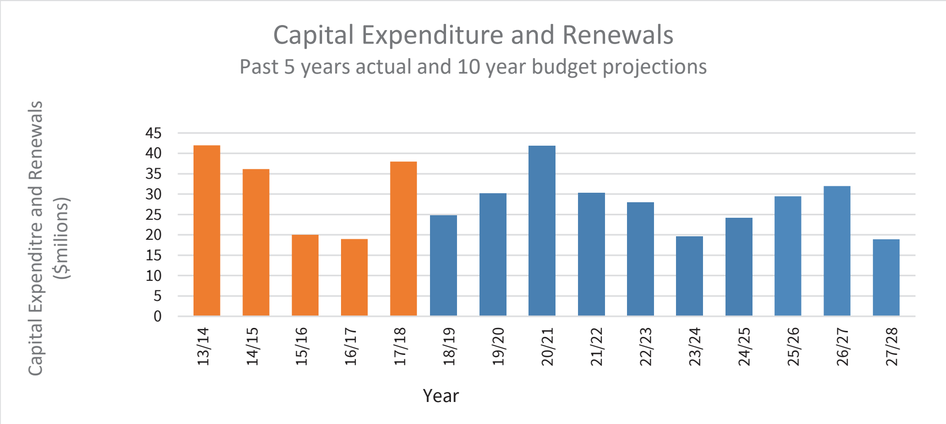
Over the next 10 years, Council has budgeted a total capital expenditure of $282 million, including capital expenditure on network infrastructure transportation, drinking water, wastewater, stormwater and stockwater.

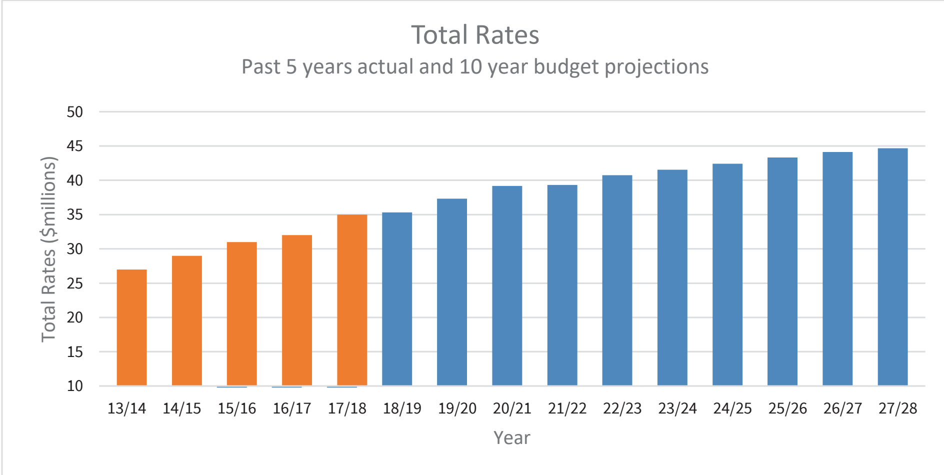
New capital expenditure is mostly budgeted to be funded from loans, with the principal and interest being funded by targeted rates over 25 years.

The following new capital expenditure is budgeted for network infrastructure activities over the coming 10 years to ensure Council can meet additional demand due to population growth or improve the level of service. The new capital costs below exclude assets vested in Council because of subdivision.

New capital expenditure for network infrastructure activities

Activity	2018/19 $000	2019/20 $000	2020/21 $000	2021/22 $000	2022/23 $000	2023/24 $000	2024/25 $000	2025/26 $000	2026/27 $000	2027/28 $000
Drinking Water	1,034	918	236	457	33	10	16	17	15	16
Wastewater	2,291	3,485	1,699	18	100	18	17	20	19	12
Stormwater	1,799	1,903	1,936	115	1,410	2,942	3,197	152	1,992	1,729
Stockwater	24	242	0	0	0	0	0	0	0	0
Transportation	2,364	2,616	2,670	3,968	3,981	1,750	1,380	14,487	14,773	238





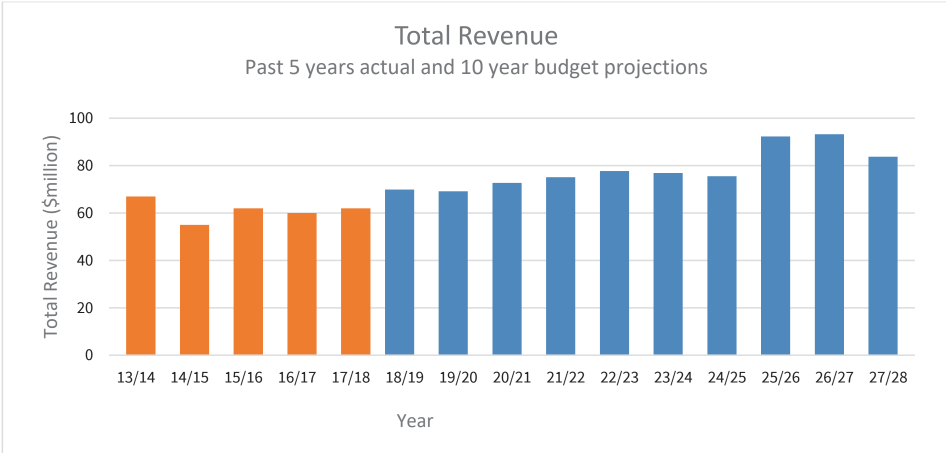
Total Rate Requirement

Total rate increases over the last 5 years have averaged 6% per year as outlined below.

The increases in overall expenditure budgeted over the coming 10 year period is driven by increased community expectations, of both the standard and quantum of infrastructure and facilities provided by Council. In addition, there has been an increasing demand for Council to become involved or increase existing levels of services in areas traditionally considered “non-core” activities such as funding for social service agencies.

The EA Networks Centre, in particular, has been extremely well supported by the community, despite the cost and consequent impact on rates.

The graphs below show the overall rate requirement and Council’s total revenue for the past 5 years and the coming 10 years covered by this Long Term Plan.



Affordability

Ashburton District's strong local economy has increased Council's rating base and the district has generally been able to absorb rate increases of the scale predicted.

However, as the proportion of rates revenue that is funded by the Uniform Annual General Charge increases, owners of lower value properties, who may have less ability to pay rates, may find the rates less affordable.

Although there may be individual cases of hardship for some ratepayers, the rating levels in Ashburton District remain affordable overall and are still comparatively low to national figures. The overall cost of rates on an average value residential property in Ashburton will be $2,105 in 2018/19, increasing to $2,497 in 2027/28.

The increasing levels of services requested and delivered are generally meeting a high level of community satisfaction, as measured in Council's Annual Residents' Survey.

Borrowing

In developing this financial strategy, Council has set limits on borrowing, to promote financial stability, affordability and value for money over the short, medium and long term.

These limits have guided the preparation of Council's work programmes and budgets set out in the Long Term Plan 2018-28 and will be used to guide the preparation of future Annual Plan work programmes and budgets. Council will review its financial strategy and the limits contained within it through the Long Term Plan 2021-31.

Council can exceed borrowing limits if it decides this is prudent; however any breach must be explained in the relevant Annual Plan, along with the reasons why a breach is considered prudent.

Council's borrowing limits have been established, recognising two major projects that are planned to be undertaken over the coming 10 years. These are:

- Construction of the Second Urban River Bridge
- Civic Administration and Library Facility renewal.

The community has been consulted extensively about the construction of the Second Urban Bridge. The Civic Administration and Library Facility has had extensive community consultation, and in 2018/19 financial year, work will commence on the design and build of the facility.

Borrowing Limits

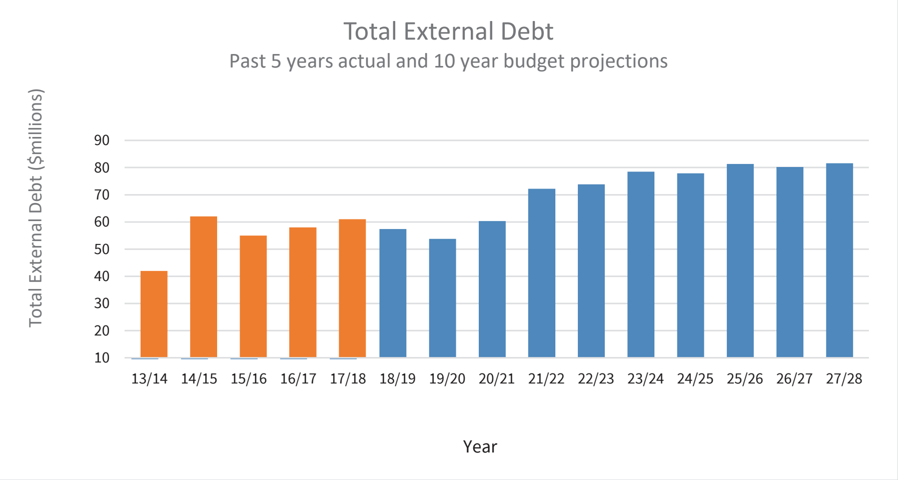
Council's position on using external debt to fund expenditure is outlined in its Revenue and Financing Policy and Liability Management Policy. By financing long-term assets through borrowing, Council allocates the cost of community assets equitably between current and future residents. This is known as the intergenerational equity principle.

The Liability Management Policy outlines external debt limits that Council believes to be prudent and sustainable over the longer term. The debt limits are considered appropriate and within commercial financial norms. In setting these limits, Council considered the financial risks associated with borrowing. Council was concerned about the impact of a significant interest rate rise, which could create higher loan servicing charges and therefore need higher rates. It also allows for market corrections without having a detrimental impact on Council activities.

During the period of this Long Term Plan, Council has budgeted to repay debt as soon as prudent to reduce finance charges.

External Debt

Council's external debt levels have increased to fund recent capital projects. Council had very low levels of external debt in 2016/17 but projects such as the Ashburton wastewater upgrade, Ashburton water supply upgrade and the Ashburton Business Estate development have seen debt levels increase significantly.



Note: 2017/18 is estimated based on the Council's Annual Plan 2017/18

Due to delays in capital projects, the 2017/18 debt projection has been recalculated and is now estimated to now be $48 million. This is the figure that has been assumed to be the opening gross debt balance for the 2018- 28 Long Term Plan.

Internal Debt

As well as external borrowing, Council has used realised investment funds to internally fund capital expenditure. Council believes it is prudent to fund debt internally, when cash reserves enable this to occur. This reduces the net cost of borrowing as Council can internalise the lender's margin.

The areas where the funds have been used are required to pay interest on these internal borrowings and capital over the life of the loans, to compensate the lost investment opportunity. As at 30 June 2017, internal loan funding was $34.2 million. If this had not taken place, Council would have $34.2 million in additional cash investments but also $34.2 million additional external debt.

Council has used internal funding from its investment pool in the past and may do so again in the future. The current strategy is to borrow externally due to favourable borrowing margins (via the Local Government Funding Agency and other sources). This will be reviewed on an ongoing basis using Council's Treasury Advisor.

External Debt Limits

The Long Term Plan 2018 - 28 has been prepared based on the following limits on external debt:

- Net interest payments to service external debt must be less than 20% of total Council revenue (excluding vested assets, infrastructure revaluations and other gains)
- Net interest payments to service external debt must be less than 25% of total rates for the year
- Net debt shall not exceed 175% of total revenue.

A limit of 10% of total Council income is widely considered to be an appropriate debt to revenue ratio. It is important to note that having debt interest that is more than 10% of total revenue does not necessarily mean debt is not sustainable, but it could limit future options and Council should be mindful of managing debt at this level. The cost of future borrowing may also increase if lenders perceive a greater risk.

	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28
Interest as a % of revenue*	1.1	1.3	1.5	2.4	2.4	2.4	1.9	1.4	1.0	0.8
Interest as a % of rates revenue	2.0	2.2	2.7	4.3	4.3	4.2	3.3	2.9	2.0	1.4

*Excluding vested assets, revaluation gains, and gains on disposal of assets.

Managing Interest Rate Risk

Interest rates are still at historically low levels. If Council was carrying high levels of external debt, any marked increase in interest rates could present difficulty in managing the increased cost of capital in the future.

Council has debt management policies that seek to minimise the impact of any such interest rate increase on Council's overall financial position.

Cash Reserves

Council's projected balance sheet shows external gross debt of $81 million by 2027/28 and a building up of cash reserves to $44 million over the same period.

Much of the cash generated is from general rate activities (such as sales in the Ashburton Business Estate) and cannot be used to repay debt funded from targeted rates (such as for water or wastewater capital expenditure). Over this period, cash reserves also increase through repayment of internal debt.

Council considers it prudent to rebuild cash holdings (primarily through land sales and depreciation funding). This will increase Council's funding flexibility by enabling cash reserves to be used, or internally borrowed against, rather than requiring external borrowing.

Council's Financial Position in 2028

Council's financial projections for the next 10 years show the following picture:

- Council's total assets in 2028 are forecast to be $1,170 million (2019: $847 million)
- Total equity is forecast to be $1,077 million (2019: $782 million)
- Debt is forecast to be $81 million ($2019: $54 million) and to be 6.9% of total assets (2019: 6.4%)
- Council's cash investments are budgeted to be $44 million, largely as a result of land sales and internal loan repayments over the 10 years
- Rates revenue is budgeted to contribute 53% of total income (2019: 51%)
- At no time over the period 20818 – 28 is Council expecting to breach its debt ratio limits
- Council will remain in a strong financial position.

Approach to Debt Security

Council provides lenders with security on its borrowings through a debenture trust deed. This gives lenders a charge over Council's rates income.

In the unlikely event of Council defaulting on a loan, the lender can ensure a rate is set to recover the outstanding amount owed. This security is attractive to lenders, which helps ensure Council has ongoing support for its debt programme, while reducing the interest rates lenders charge.

Council's Treasury Management Policy permits Council to give security over specific assets, where

a. there is a direct relationship between the debt and the asset being funded and,
b. Council considers security over the asset is preferable to security over its rates income.

Currently, Council has no securities issued over its assets and the Long Term Plan 2018-28 does not include any provision to secure debt directly over assets.

Council's approach to debt security seeks to maximise access to the capital needed for providing appropriate services to the community at the lowest cost possible.

Financial Investments and Equity Securities

Council has financial investments that generate a return, which can be used to pay for services and reduce rates. This section explains Council's objectives for holding and managing financial investments and equity securities and its targets for returns on those investments and equity securities.

Ashburton Contracting Limited

Council owns 100% of the 4,500,000 shares in Ashburton Contracting Limited (ACL).

Council's objectives in holding this investment are to:

- Ensure local capacity and capability to undertake civil works, particularly for infrastructure
- Promote competition in the district for civil construction and maintenance activities
- Form part of a balanced portfolio of investments

Council's expected rate of return on average shareholder funds is a minimum of 12% after tax, based on the rolling average of the last 5 years (excluding any tax loss offset / subvention payment or the costs of ACL's investment in the Lake Hood extension project).

This return, paid by way of dividend, is used to offset rates in the year it is received. This has been budgeted at $500,000 per year before inflation.

Transwaste Canterbury Limited

Council owns 600,000 shares in Transwaste Canterbury Limited. As at 30 June 2017, these shares had a net asset backing of $1.34 per share - $804,000.

Council's objectives in holding this investment are to:

- Provide an environmentally sustainable facility for the disposal of the district's residual solid waste
- Form part of a balanced portfolio of investments.

Dividends are determined by the board of directors and dividend returns are applied against the general rate and the uniform annual general charge as detailed in Council's Revenue and Financing Policy.

Cash

Council holds cash to operate and maintain stable cash flows. Council also holds cash in reserves, largely to fund the renewal of assets. These funds are invested in internal borrowing or deposits as provided by Council's Investment Policy. Council's target return on cash is the average 90-day bill rate. The return on net cash investments is budgeted at 4%.