



NEW ZEALAND
LOCAL GOVERNMENT
FUNDING AGENCY



HALF YEAR REPORT

31
DECEMBER
2016



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Cover: Opening Day, Ashley Bridge (Cones Rd, Rangiora). The old bridge which has since been deconstructed is in the foreground. The bridge connects the Township of Rangiora directly with Ashley and Loburn. Waimakariri District Council. Photo: Aaron Campbell.

Left: A family ride along the new Matai Street cycleway, part of the Uni-Cycle Major Cycle Route which links the university to the city. Christchurch City Council.

CHAIRMAN'S REPORT

FOR THE SIX MONTHS ENDED 31 DECEMBER 2016

"LGFA continues to provide attractive borrowing terms to council members while providing a highly rated, liquid NZD fixed income instrument for investors."

Craig Stobo, Chairman LGFA Board



Directors would like to highlight the following developments at LGFA for the six-month period to December 2016:

Strong Financial and Operational Performance in line with the Statement of Intent (SOI) forecasts

LGFA total interest income for the six-month period of \$155.711 million was a 16.0% increase over the 2015-16 comparable period of \$134.217 million while Net Operating Profit of \$5.312 million was a 11.4% increase on the 2015-16 comparable period of \$4.769 million.

The financial strength of LGFA was reaffirmed by credit rating agencies Standard & Poor's and Fitch Ratings who maintained our credit rating at AA+. Our credit rating is the same as the NZ Government.

In October 2016, LGFA announced a bond lending programme where it would lend bonds to bank pricemakers assisting with deepening secondary market liquidity by facilitating tighter bid/offer spreads in LGFA bonds. In the first two months of this facility, LGFA has lent bonds on twelve transactions.

Borrowing activity

Over the past six months, LGFA has issued \$595 million of long-dated bonds. While this is in line with SOI forecast, it is one of the lowest issuance amounts over a six-month period, reflecting reduced borrowing demand from our council members.

LGFA has now issued \$6.815 billion of bonds on behalf of its council members across seven maturities from 2017 to 2027. LGFA is one of the largest issuers of NZD securities after the NZ Government and our bonds are amongst the largest and most liquid NZD debt instruments available for investors.

Lending to the sector

LGFA was established in late 2011 to provide long-dated borrowing, certainty of access to markets and to reduce the borrowing costs for the local government sector. It is pleasing to note the following achievements over the past six months:

- We admitted Central Hawkes Bay District Council as a new member, bringing total membership to fifty-one councils.

- Bespoke lending continues to be popular for councils in that it provides flexibility as to maturity dates of borrowing and the date of drawdown. LGFA lent \$190 million on a bespoke basis for the six-month period. This was approximately 36% of our total lending over that period. Bespoke loans outstanding are now \$676 million or 10% of our total loan book.
- Short-dated lending (less than 365 day terms) to councils, introduced in November 2015, has been very successful with outstandings now at \$240 million lent to seventeen councils. This compares to \$44 million lent to three councils as at December 2015.
- Credit quality of the sector continues to improve with all councils remaining compliant with the LGFA lending covenants and three councils in 2016 either receiving an upgrade to their credit ratings or a positive outlook change to their rating.

Finally, at this time I would like to acknowledge the support of Local Government New Zealand (LGNZ) and its chief executive Malcolm Alexander who has helped LGFA continue to provide highly valued services to the sector despite our Wellington offices being closed as a result of the Kaikoura earthquakes in November 2016. The LGFA Wellington based team are currently working from the LGNZ offices until we can safely return to our previous location.

On behalf of my fellow directors I am pleased to be part of the continued success of this organisation and wish to thank our council shareholders, guarantors and borrowers as well as our financial intermediaries and investors for their continued support.

Craig Stobo
Chairman, LGFA Board

Rauparaha Street Pump Station upgrade. Kapiti Coast District Council.





STATEMENT OF SERVICE PERFORMANCE

A stormwater mixing chamber is lowered into place as part of a comprehensive upgrade on the Little Go Stream. Nelson City Council.

Performance Against Objectives and Performance Targets

1 PRIMARY OBJECTIVES

LGFA operates with two primary objectives

1. Optimising the debt funding terms and conditions for participating local authorities.
2. LGFA will monitor the quality of the asset book so that it remains of a high standard by ensuring it understands each participating local authority's financial position and the general issues confronting the Local Government sector:

1.1 Optimising the debt funding terms and conditions for participating local authorities

(i) Providing savings in annual interest costs for all participating local authority's on a relative basis to other sources of financing

LGFA measures the pricing performance of bond tenders against two key benchmarks:

- LGFA aims to reduce its margin over New Zealand Government bonds (NZGBs)
- LGFA aims to minimise its margin over swap rates to provide cost effective funding to councils.

The LGFA margin to swap and NZGB will depend upon a number of factors including the relative demand and supply of high grade bonds, general credit market conditions, performance of NZGBs and swap rates, investor perceptions of LGFA and the issuance volume and tenor of LGFA bonds.

Given that LGFA tends to match fund its on-lending to councils, ie. tends to issue bonds in the same tenor and volume as its on-lending, then LGFA only has influence over investor perception amongst the above factors that determine LGFA spreads to NZGB and swap.

There will be periods within the interest rate and credit market cycles when LGFA bonds will outperform its benchmarks (spread narrowing) and there will be periods of time when LGFA bonds underperform (spreads widening).

LGFA spreads to its benchmarks have consistently narrowed since it first began issuing bonds in February 2012, but these spreads have widened from the historical lows over the past twelve months.

Over the course of the six-month period to 31 December 2016:

- LGFA margins to NZGB widened between 1 basis points (bps) (2021s) and 4 bps (2017s) but also narrowed between 10 bps (2023s) and 17 bps (2027s).
- LGFA margins to swap widened 2 bps on all LGFA maturities except for 2019s (unchanged) and 2017s (3 bps tighter).

These secondary market pricing movements are summarised in the following tables:

MARGINS – 15 DECEMBER 2017	As at 30 June 2016 (bps)	As at 31 Dec 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	40	44	4
NZGB margin to swap	(19)	(26)	(7)
LGFA margin to swap	21	18	(3)

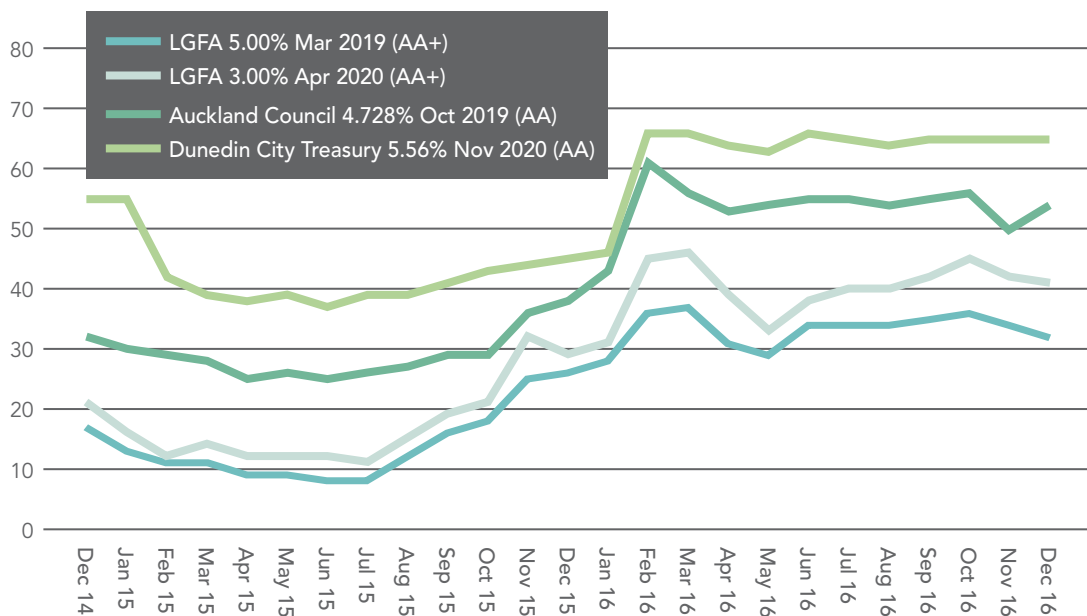
MARGINS – 15 MARCH 2019	As at 30 June 2016 (bps)	As at 31 Dec 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	54	58	4
NZGB margin to swap	(21)	(25)	(4)
LGFA margin to swap	33	33	-
MARGINS – 15 APRIL 2020	As at 30 June 2016 (bps)	As at 31 Dec 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	61	69	8
NZGB margin to swap	(23)	(29)	(6)
LGFA margin to swap	38	40	2
MARGINS – 15 MAY 2021	As at 30 June 2016 (bps)	As at 31 Dec 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	72	73	1
NZGB margin to swap	(29)	(28)	1
LGFA margin to swap	43	45	2
MARGINS – 15 APRIL 2023	As at 30 June 2016 (bps)	As at 31 Dec 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	89	79	(10)
NZGB margin to swap	(39)	(27)	12
LGFA margin to swap	50	52	2
MARGINS – 15 APRIL 2025	As at 30 June 2016 (bps)	As at 31 Dec 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	94	81	(13)
NZGB margin to swap	(37)	(15)	22
LGFA margin to swap	57	66	9
MARGINS – 15 APRIL 2027	As at 30 June 2016 (bps)	As at 31 Dec 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	106	89	(17)
NZGB margin to swap	(36)	(17)	19
LGFA margin to swap	70	72	2

The movement in LGFA bond spreads to NZGB has been largely driven by the movements in swap spreads to NZGB. Swap spreads to NZGB have been volatile and influenced by the amount of corporate fixed rate hedging and bank hedging of mortgage books over the past six months. Short-dated swap spreads have widened as banks hedge their mortgage books while the absence of corporate borrowing in the long end combined with ongoing long-dated NZ Government bond issuance has led to a contraction in long-dated swap spreads. LGFA bonds have outperformed NZGBs in the longer end of the curve and underperformed in the shorter end.

LGFA bonds have slightly widened to swap as credit spreads in general have moved slightly wider over the past six months.

LGFA continues to provide savings in borrowing cost for councils relative to other sources of borrowing. We compare our secondary market spreads on LGFA bonds to those of Auckland Council and Dunedin City Treasury. The implied pricing advantage of LGFA based upon this measure has reduced by between 1 bps (2017s) and 11 bps (2025s) over the past six months. This measure can be volatile given that it is based upon secondary market pricing estimates and LGFA is a regular issuer of bonds in the primary market whereas both Auckland and Dunedin Councils are infrequent borrowers.

LGFA March 2019 and April 2020 secondary market credit margin over swap (bps)



Source PwC and LGFA

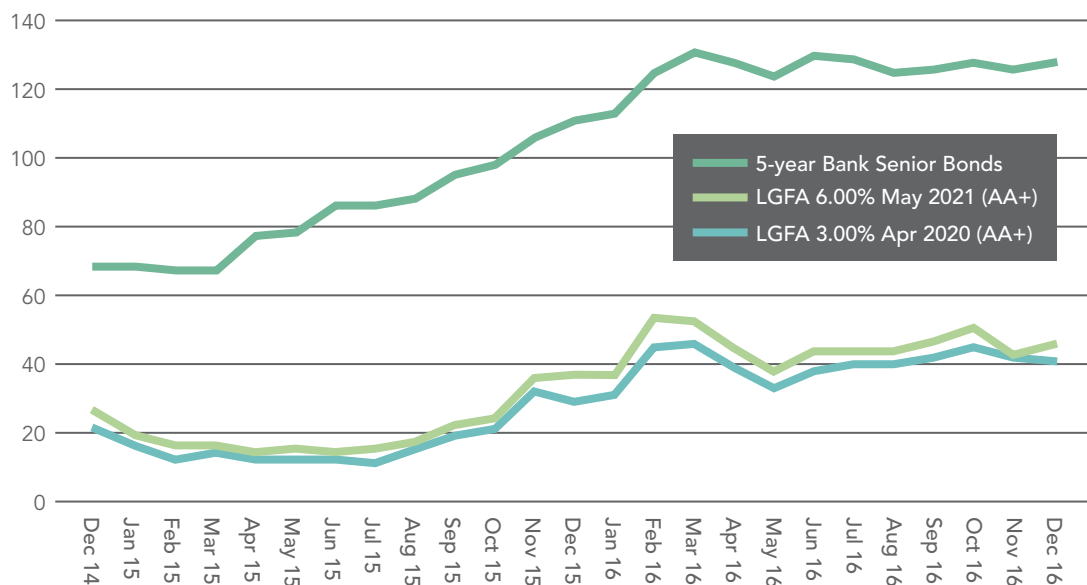
From the table below we estimate that as at 31 December 2016, LGFA was saving AA-rated councils between 15 bps for a 2019 (two and half year) maturity and 25 bps for a 2021 (five year) maturity.

30 June 2016	Auckland 2019	Dunedin 2020	Dunedin 2021	Auckland 2022	Auckland 2025
AA rated councils margin to swap	47	60	70	74	87
Less LGFA margin to swap	(33)	(40)	(45)	(49)	(66)
LGFA Gross Funding Advantage	14	20	25	25	21
Less LGFA Base Margin	(9)	(10)	(10)	(10.5)	(11)
LGFA Net Funding Advantage	5	10	15	14.5	10
Add 'LGFA Effect' *	10	10	10	10	10
Total Saving	15 bps	20 bps	25 bps	24.5 bps	20 bps

* The 'LGFA effect' represents the estimated conservative reduction in AA-rated councils' margin to swap as a result of LGFA operations. From May to June 2012, the margin to swap for AA-rated councils' fell by 10 bps, with no corresponding move in swap spreads for other borrowers. This suggests that potential access to cost-effective LGFA funding has enabled these councils to reduce their borrowing margin by around 10 bps.

LGFA remains the cheapest source of borrowing for the sector as illustrated in the chart below which shows the widening borrowing cost for banks

LGFA and bank secondary market margins over swap



Source PwC and LGFA

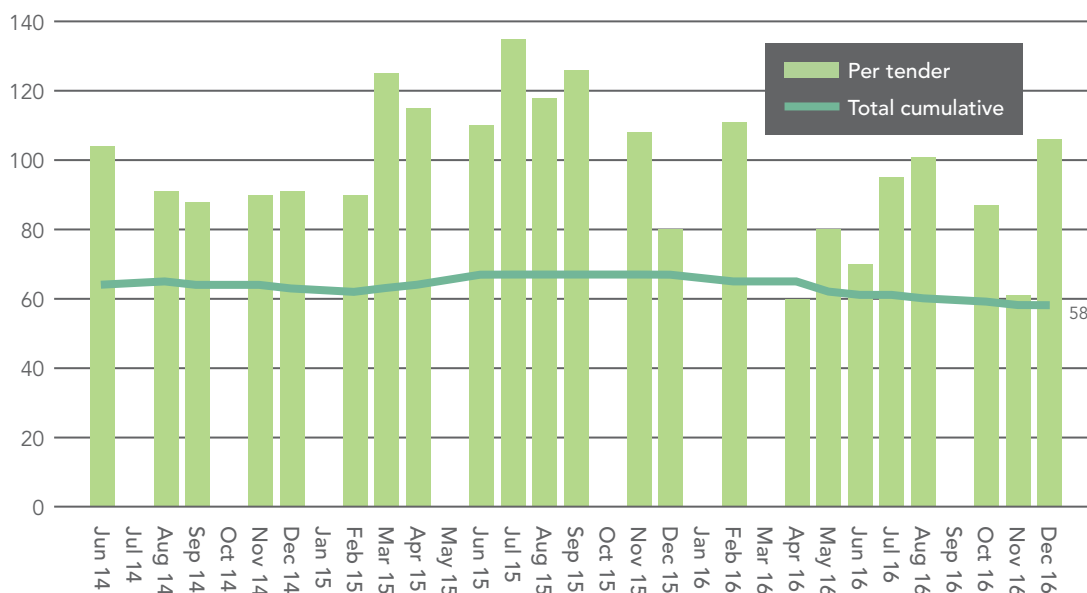
(ii) Making longer-term borrowings available to participating local authorities

Over the past six months, LGFA offered three existing maturity dates for borrowing in excess of six years to participating councils:

- 15 April 2023 bond (six and half years) and this maturity has comprised 7.6% of total issuance in the six-month period to 31 December 2016
- 15 April 2025 bond (seven and half years) and this maturity has comprised 54.6% of total issuance in the six-month period to 31 December 2016, and
- 15 April 2027 (nine and half years) and this maturity comprised 17.6% of our issuance in the six-month period to 31 December 2016.

The following chart shows the average term of lending to councils by LGFA at each tender, and the average term for all LGFA long-dated lending at each tender date. Over the past six months the average term of council lending has shortened by three months to 58 months but this must be considered in the context of a natural six month shortening in time over that period.

Average total months to maturity – On-lending to councils

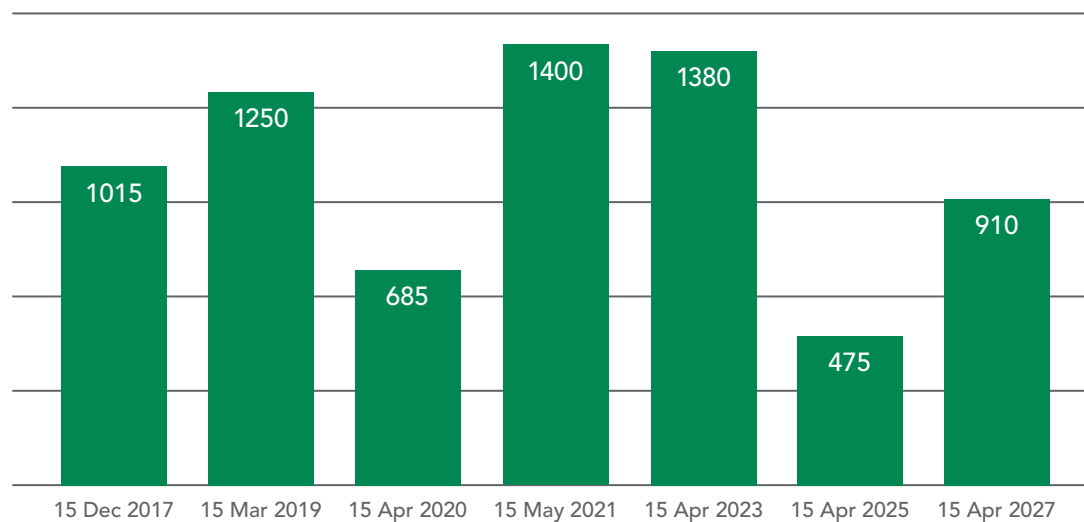


The average term of borrowing by Councils from LGFA was 7.56 years for the six-month period to 31 December 2016. This is shorter than the 8.08 years' average term for the 2015-16 year but reflects the current wider borrowing margins, higher yields and most councils had lengthened the duration of their borrowing in the prior year.

The following chart shows the total LGFA bond outstandings by maturity as at 31 December 2016

LGFA bonds outstandings as at 31 December 2016 (\$ million)

Includes \$300m treasury stock



Over the six-month period to 31 December 2016, LGFA issued \$595 million of bonds with an average term of 7.61 years. The amount of issuance is in line with the full year SOI forecast of \$1.2 billion but less than the \$710 million of issuance in the first six months of 2015-16.

2016-17 financial year issuance

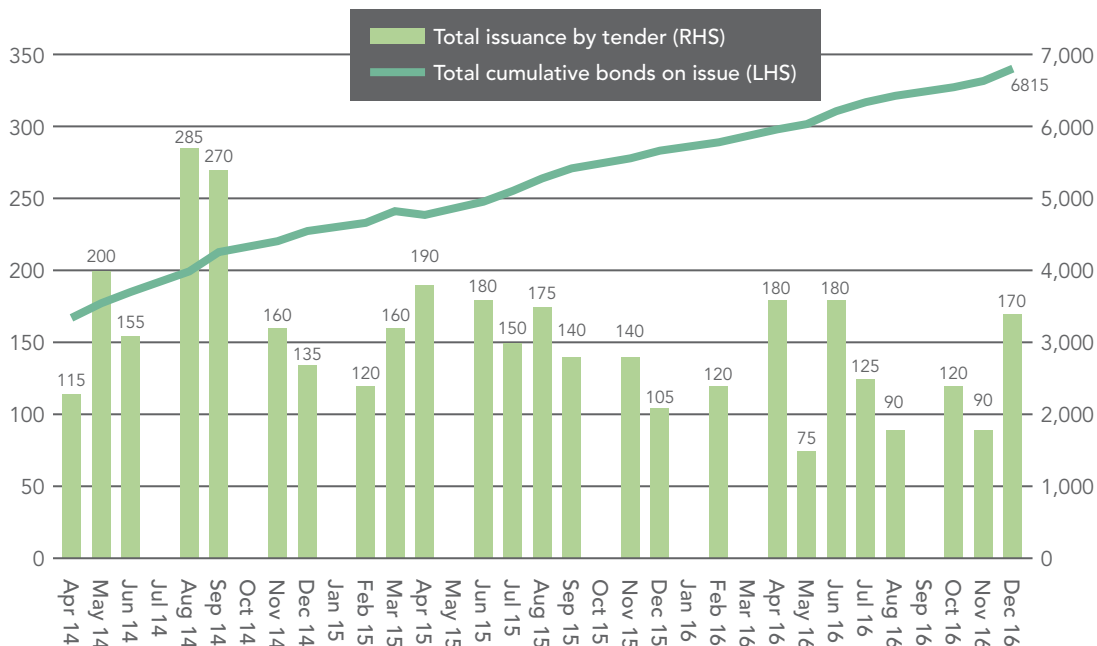
Dec-17	Mar-19	Apr-20	May-21	Apr-23	Apr-25	Apr-27	Total
-	\$20 million	\$70 million	\$30 million	\$45 million	\$325 million	\$105 million	\$595 million
-	3.4%	11.8%	5.0%	7.6%	54.6%	17.6%	100%

(iii) Enhancing the certainty of access to debt markets for participating local authorities, subject always to operating in accordance with sound business practice

LGFA held five tenders during the six-month period to 31 December 2016, with an average tender volume of \$119 million (compared to the average tender size for 2015-16 of \$141 million). The volume offered at each tender ranged from \$90 million to \$170 million and all tenders were successful and fully subscribed. Total issuance during the six-month period of \$595 million resulted in outstandings of LGFA bonds of \$6.815 billion as at 31 December 2016. This excludes the \$300 million of treasury stock held by LGFA to facilitate stock lending to banks.

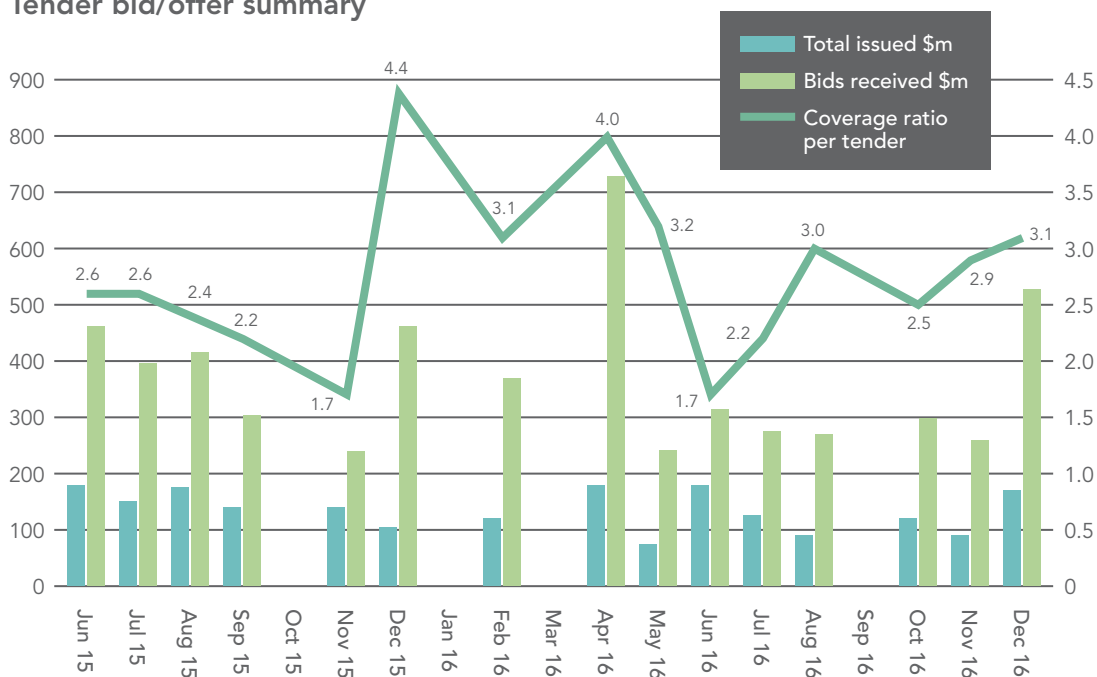
LGFA bond issuance by tender (\$ million)

Excludes issuance of treasury stock



Over the six-month period, total bids received across the five tenders was \$1.43 billion for the \$595 million of LGFA bonds offered resulting in a coverage ratio of 2.4 times. This coverage ratio is less than the 2.74 times coverage ratio for the 2015-16 year. The LGFA cover ratio for each tender and the cumulative ratio for tenders over the past two years is shown in the following chart.

Tender bid/offer summary



While the coverage ratio for the past six months is lower than the average coverage ratio of 3.1 times since LGFA first commenced issuing in February 2012, this is not surprising given the longer duration of LGFA bonds being currently tendered, the smaller tranche sizes being offered, relatively tight spreads to both NZGB and swap and low outright yields. Furthermore, offshore investor demand for LGFA securities has been noted in the secondary market rather than at LGFA tenders.

While LGFA issues fixed coupon debt to investors, Councils were provided the choice of either fixed or floating rate borrowing for their borrowing from LGFA. Councils tend to borrow on a floating rate basis from LGFA.

Improved certainty of access for councils was achieved through both bespoke lending and short-dated lending (less than one year terms).

(iv) Offering more flexible lending terms to participating local authorities

The successful introduction of bespoke lending and short-dated lending has provided councils with flexible lending conditions.

LGFA first offered bespoke lending in February 2015 where council borrowers could select their preferred borrowing maturity date and their preferred date of borrowing drawdown. In the six-month period to 31 December 2016 LGFA lent \$190 million on a bespoke basis for 14 transactions. Total bespoke lending outstanding as at 31 December 2016 was \$676 million to twenty-three councils or 10% of our loans outstanding.

LGFA first offered short-dated lending to councils in November 2015 and as at 31 December 2016 there were loans of \$240 million to seventeen councils. Councils can now borrow on attractive terms out to 364 days where previously the shortest borrowing maturity was to December 2017.

1.2 LGFA will monitor the quality of the asset book so that it remains of a high standard by ensuring it understands each participating local authority's financial position and the general issues confronting the Local Government sector. This includes:

(i) LGFA will review each participating local authority's financial position, its financial head-room under LGFA policies and visit each participating local authority on an annual basis

LGFA undertakes a detailed financial assessment on each of its borrowers and meets with all member councils on an annual basis while monitoring council performance throughout the year. LGFA reviews the Annual and Long Term Plans for each council and the annual financial statements. LGFA assigns an internal credit rating to each of its council members as part of the review exercise. All council members were compliant with LGFA covenants at June 2016.

(ii) LGFA will commence work on analysing finances at the council group level in addition to parent level. Previously the analysis was undertaken at the council parent level

LGFA reviews the financial position of each council on a Group basis where appropriate, eg. where council services are delivered through subsidiaries or holds substantial investments in subsidiaries.

(iii) LGFA will work closely with the Department of Internal Affairs (DIA), Office of the Auditor General (OAG) and Local Government New Zealand (LGNZ) on sector and individual council issues

LGFA staff and directors have met with the OAG during the past twelve months and staff have met with DIA. LGFA has presented at all LGNZ quarterly media briefings during the six-month period.

2 ADDITIONAL OBJECTIVES

LGFA has a number of additional objectives which complement the primary objective. These additional objectives are to:

2.1 Operate with a view to making a profit sufficient to pay a dividend in accordance with its stated Dividend Policy set out in section 6 of the Statement of Intent

The LGFA's policy is to pay a dividend that provides an annual rate of return to shareholders equal to LGFA cost of funds plus 2% over the medium term.

With lending volumes and financial outcomes for the six-month period close to SOI forecast, we expect profitability to be sufficient to make a dividend payment for the full year. This remains at the Board's discretion.

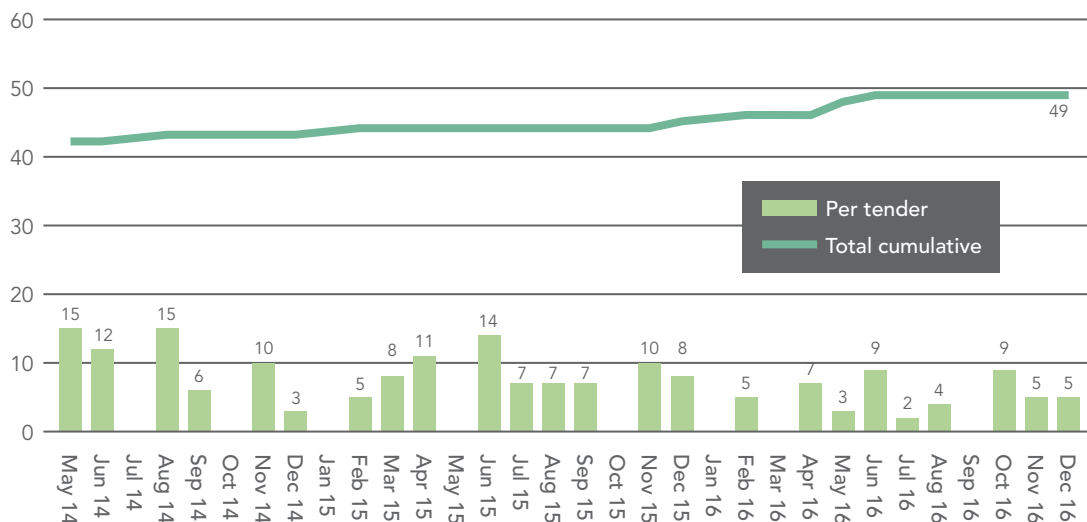
The impact from a lower interest rate environment is that LGFA has a lower cost of funds than previous years. Our cost of funds for the six-month period to 31 December 2016 is 3.31% compared to 3.57% for the 2015-16 year. While council borrowers benefit from lower borrowing costs, the dividend payment if calculated on the above cost of funds would be lower than previous years.

2.2 Provide at least 50% of aggregate long-term debt funding for Participating Local Authorities

Central Hawkes Bay District Council joined as a non-guarantor in the past six months bringing the total number of council members to 51. Councils have strongly supported LGFA and by 31 December 2016, 49 participating councils have borrowed from LGFA.

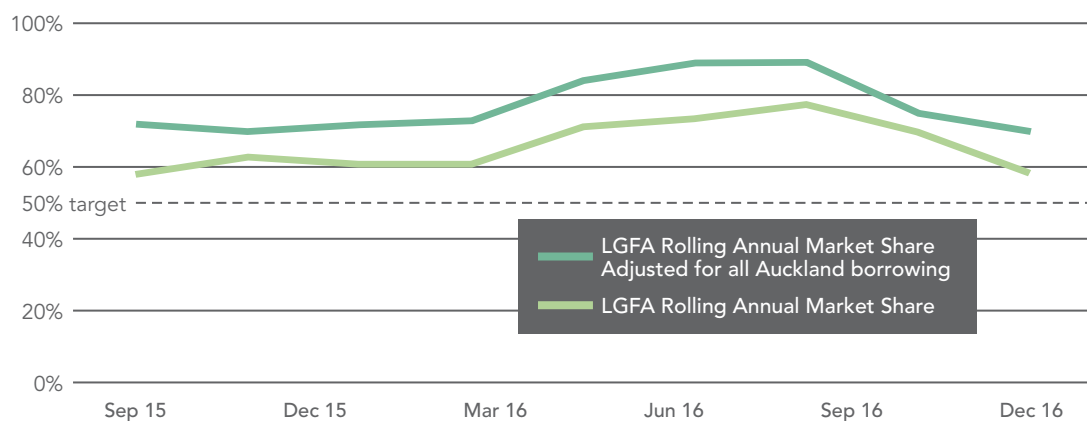
The strong council support for LGFA is demonstrated in the following chart which shows the progression of council participation

Participating councils



The following chart shows LGFA's share of new local government debt issuance and is derived from data provided by PwC. Our share of long-term borrowing by the sector including non-members of LGFA was 58% for the twelve-month period to 30 September 2016. The market share is influenced by the amount of debt issued by the sector's largest borrower, Auckland Council in its own name in the domestic market. If we exclude Auckland Council external borrowing from the data, then our estimated market share for the twelve-month period to 30 June 2016 was 69.6%.

LGFA Market Share – rolling one-year average (excluding short-term lending)



2.3 Issue a new long-dated LGFA bond (should one not be issued in the 2015/16 year)

The 2016-17 SOI was finalised before the issuance of a new April 2025 bond maturity in June 2016. Given our forecast borrowing programme we will consider issuing a further new long-dated bond maturity in the 2017 calendar year. The timing of issuance and the bond maturity will depend upon both council borrowing intentions and investor demand.

2.4 Ensure its products and services are delivered at a cost that does not exceed the forecast for issuance and operating expenses set out in section 4 of the Statement of Intent

Issuance and Operating Expenses for the six-month period to 31 December 2016 were \$3.199 million compared to a full year SOI budget of \$6.580 million. Management forecast for the six-month period was \$3.125 million.

Issuance and on-lending costs were slightly higher than budget (by \$51k) due to higher NZX listing costs relating to additional bond issuance associated with the introduction of the bond lending facility. Approved Issuer Levy (AIL) costs were slightly below budget (by \$26k). Operating costs were \$50k above budget, reflecting slightly higher treasury system and personnel costs.

2.5 Take appropriate steps to ensure compliance with the Health and Safety at Work Act 2015

In the past six months, LGFA established a Health and Safety Staff Committee and reporting on health and safety issues is made to the LGFA Board on a regular basis by the Risk and Compliance Manager. There were no health and safety incidents during the six-month period.

The Kaikoura earthquake in November impacted buildings in the Wellington CBD. While the building that LGFA occupied was not structurally affected by the earthquakes, an asbestos contamination problem was discovered. As a result, staff are currently working from the Local Government New Zealand offices until it is safe to return to the LGFA offices.

2.6 Maintain LGFA's credit rating equal to the New Zealand Government sovereign rating where both entities are rated by the same rating agency

LGFA met with both Standard & Poor's (S&P) and Fitch rating agencies in September 2016 as part of their annual review processes. S&P subsequently affirmed the long-term rating of LGFA at AA+ (stable outlook) on 20 October 2016 and Fitch affirmed the AA+ (stable outlook) on 15 November 2016.

Both the S&P and Fitch ratings reports are available on our website (lgfa.co.nz).

Both the S&P and Fitch ratings are the same as, and are capped by, New Zealand's sovereign credit ratings. Fitch has defined LGFA as a dependant Public Sector Entity and our credit rating is explicitly linked to the New Zealand Sovereign credit rating.

2.7 Achieve the Financial Forecasts (excluding the impact of AIL) set out in section 4 of the Statement of Intent

LGFA's financial results for key items set out in section 4 of the SOI for the six-month period to 31 December 2016 are:

In \$ million	31 Dec 2016 Six months actual	30 June 2017 SOI forecast
Net interest revenue	8.51	16.58
Issuance and operating expenses	(3.20)	(6.58)
Net Profit	5.31	10.00

Net interest revenue for the six month period is \$314k above management forecast due to timing issues and the early repayment of a December 2017 loan by a council borrower.

Issuance and operating expenses for the period are \$74k above management forecast.

2.8 Meet or exceed the Performance Targets outlined in section 5

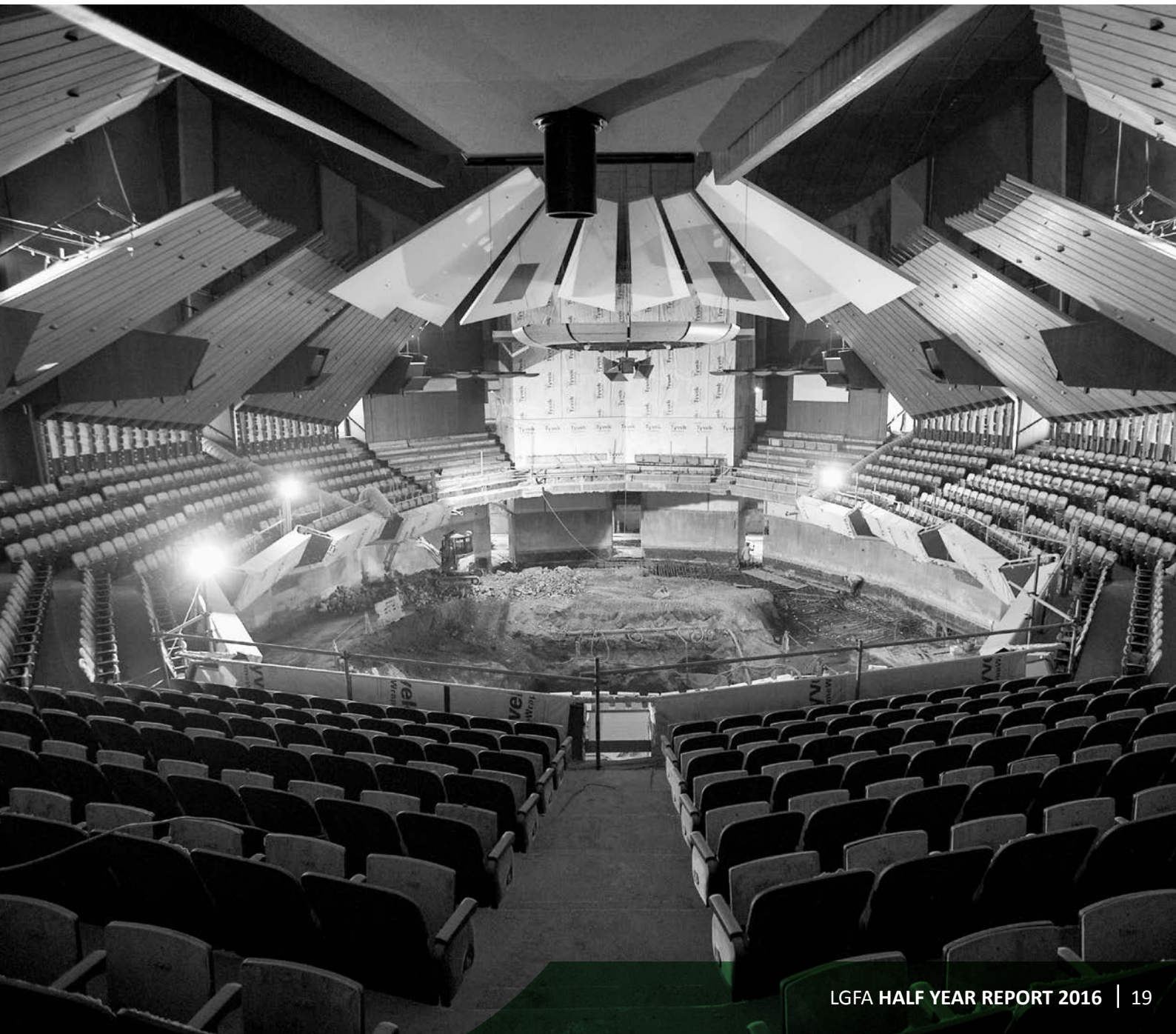
Current performance targets	Target	Result as at half year	Outcome
1 Average cost of funds on debt issued relative to New Zealand Government Securities for the 12-month period	≤0.50%	0.74%	No (i)
2 Average base on-lending margin above LGFA's cost of funds	≤0.10%	0.098%	Yes
3 Annualised issuance and operating expenses	≤\$4.80 million	\$2.260 million	Yes
4 Lending to participating councils	≥\$7,341 million	\$7,016 million	On track
5 Savings to council borrowers relative to other sources of financing and compared to previous years	Improvement	No additional savings in borrowing costs from June 2016 levels	No

- (i) The average cost of funds of all issuance for the twelve-month period ending 31 December 2016 relative to NZGS was 0.74%. This compares to a spread of 0.74% for the twelve-month period to 30 June 2016.

2.9 Comply with its Treasury Policy, as approved by the Board

LGFA was compliant at all times with the Treasury Policy for the six-month period ending 31 December 2016.

Christchurch Town Hall restoration project, scheduled for completion mid-2018. Christchurch City Council.





FINANCIAL STATEMENTS

The new library and community hub opened in Greerton last year. It is twice the size of the old library and is a modern, engaging and vibrant facility for the Greerton community.
Tauranga City Council.

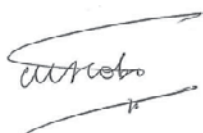
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In the opinion of the directors of the New Zealand Local Government Funding Agency Limited, the financial statements and notes on pages 24 to 38:

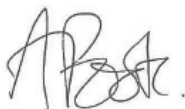
- Comply with New Zealand generally accepted accounting practice and give a true and fair view of the financial position of the Company as at 31 December 2016, and
- Have been prepared using appropriate accounting policies, which have been consistently applied and supported by reasonable judgements and estimates.
- The directors believe that proper accounting records have been kept which enables, with reasonable accuracy, the determination of the financial position of the Company and facilitates the compliance of the financial statements with the Financial Reporting Act 1993.

The directors consider that they have taken adequate steps to safeguard the assets of the Company, and to prevent and detect fraud and other irregularities. Internal control procedures are also considered to be sufficient to provide a reasonable assurance as to the integrity and reliability of the financial statements.

For and on behalf of the Board of Directors



C. Stobo, Director
24 February 2017



A. Foote, Director
24 February 2017

Statement of Comprehensive Income

For the six months ended 31 December 2016 (unaudited) in \$000s

	Note	2016 Unaudited	2015 Unaudited
Interest income from			
Cash and cash equivalents		272	635
Loans to local government		109,752	108,035
Marketable securities		1,304	598
Deposits		1,548	2,037
Derivatives		42,835	22,912
Fair value hedge ineffectiveness	2	-	-
Total interest income		155,711	134,217
Interest expense on			
Bills		2,582	542
Bonds		142,988	124,476
Borrower notes		1,584	1,606
Bond repurchases		46	-
Total interest expense		147,200	126,624
Net interest income		8,511	7,593
Operating Expenses			
Issuance and on-lending expenses	3	1,764	1,556
Operating expenses	4	1,435	1,268
Total expenses		3,199	2,824
Net operating profit		5,312	4,769
Total comprehensive income for the year		5,312	4,769

These statements are to be read in conjunction with the notes to the financial statements

Statement of Changes In Equity

For the six months ended 31 December 2016 (unaudited) in \$000s

	Note	Share capital	Retained Earnings	Total equity
Equity as at 30 June 2016	11	25,000	19,224	44,224
Net operating profit			5,312	5,312
Total comprehensive income for the year			5,312	5,312
Transactions with owners			-	-
Dividend paid on 15 October 2016			(1,392)	(1,392)
Equity as at 31 December 2016	11	25,000	23,144	48,144

For the six months ended 31 December 2015 (unaudited) in \$000s

	Share capital	Retained Earnings	Total equity
Equity as at 30 June 2015	25,000	11,287	36,287
Net operating profit		4,769	4,769
Total comprehensive income for the year		4,769	4,769
Transactions with owners			-
Dividend paid on 15 October 2015		(1,603)	(1,603)
Equity as at 31 December 2015	25,000	14,453	39,453

These statements are to be read in conjunction with the notes to the financial statements

Statement of Financial Position

As at 31 December 2016 (unaudited) in \$000s

	Note	31 December 2016 Unaudited	30 June 2016
Assets			
Financial assets			
Cash and bank balances		22,186	37,084
Borrower notes receivable		-	800
Loans to local government	5	7,064,966	6,451,332
Marketable securities		86,714	139,339
Deposits		103,745	89,828
Derivatives in gain		354,074	537,379
Non-financial assets			
Prepayments		827	535
Other assets	6	886	955
Total assets		7,633,398	7,257,252
Equity			
Share capital		25,000	25,000
Retained earnings		17,832	19,224
Total comprehensive income/ (deficit) for the period		5,312	-
Total equity		48,144	44,224
Liabilities			
Financial Liabilities			
Trade and other payables		241	182
Loans to local government not yet advanced		-	50,000
Accrued expenses		535	593
Bills		224,041	223,916
Bonds	7, 9	7,196,452	6,819,658
Borrower notes	8	118,487	108,415
Bond repurchases	9	3,714	-
Derivatives in loss		41,784	10,264
Total liabilities		7,585,254	7,213,028
Total equity and liabilities		7,633,398	7,257,252

These statements are to be read in conjunction with the notes to the financial statements

Statement of Cash Flows

For the six months ended 31 December 2016 (unaudited) in \$000s

	Note	2016 Unaudited	2015 Unaudited
Cash flow from operating activities			
Cash applied to loans to local government		(662,866)	(746,138)
Interest paid on bonds issued		(166,281)	(134,839)
Interest paid on bills issued		2,582	542
Interest paid on borrower notes		-	(57)
Interest paid on loans		-	(26)
Interest paid on bond repurchases		(44)	-
Interest received from cash & cash equivalents		271	635
Interest received from loans to local government		108,984	108,270
Interest received from marketable securities		1,142	756
Interest received from deposits		1,630	1,966
Net interest on derivatives		63,224	32,147
Payments to suppliers and employees		(3,488)	(3,051)
Net cash flow from operating activities	10	(654,846)	(739,795)
Cash flow from investing activities			
Purchase of marketable securities		52,787	(89,745)
Purchase of deposits		(14,000)	(35,000)
Purchase of plant and equipment		69	(4)
Net cash flow from investing activities		38,856	(124,749)
Cash flow from financing activities			
Dividends paid		(1,392)	(1,608)
Cash proceeds from borrower notes		9,288	11,200
Cash proceeds from bonds issued		603,386	744,807
Cash proceeds from bills issued		(5,040)	147,868
Cash applied to bond repurchases		3,712	-
Cash applied to derivatives		(8,862)	(27,022)
Net cash flow from financing activities		601,092	875,245
Net (decrease) / increase in cash		(14,898)	10,701
Cash, cash equivalents and bank overdraft at beginning of year		37,084	31,708
Cash, cash equivalents and bank overdraft at end of year		22,186	42,409

These statements are to be read in conjunction with the notes to the financial statements

1 Statement of accounting policies

A REPORTING ENTITY

The New Zealand Local Government Funding Agency Limited (LGFA) is a company registered under the Companies Act 1993 and is subject to the requirements of the Local Government Act 2002.

LGFA is controlled by participating local authorities and is a council-controlled organisation as defined under section 6 of the Local Government Act 2002. LGFA is a limited liability company incorporated and domiciled in New Zealand.

The primary objective of LGFA is to optimise the debt funding terms and conditions for participating local authorities.

The registered address of LGFA is Level 8, City Chambers, 142 Featherston Street, Wellington Central, Wellington 6011.

The financial statements are for the six-month period ended 31 December 2016.

These financial statements were authorised for issue by the Directors on 24 February 2017.

B BASIS OF PREPARATION

Measurement base

The financial statements have been prepared on a historical cost basis modified by the revaluation of certain assets and liabilities.

The financial statements are prepared on an accrual basis.

Functional and presentation currency

The financial statements are presented in New Zealand dollars rounded to the nearest thousand, unless separately identified. The functional currency of LGFA is New Zealand dollars.

Foreign currency conversions

Transactions denominated in foreign currency are translated into New Zealand dollars using exchange rates applied on the trade date of the transaction.

Changes in accounting policies

There have been no changes in accounting policies.

Early adoption standards and interpretations

NZ IFRS 9: Financial Instruments. The first two phases of this new standard were approved by the Accounting Standards Review Board in November 2009 and November 2010. These phases address the issues of classification and measurement of financial assets and financial liabilities.

Standards not yet adopted

LGFA does not consider any standards or interpretations in issue but not yet effective to have a significant impact on its financial statements. Those which may be relevant to LGFA are as follows:

- NZ IFRS 9: Financial Instruments (2014) – Effective for periods beginning on or after 1 January 2018. This standard aligns hedge accounting more closely with the risk management activities of the entity and adds requirements relating to the accounting for an entity's expected credit losses on its financial assets and commitments to extend credit.

C FINANCIAL INSTRUMENTS

Financial assets

Financial assets, other than derivatives, are recognised initially at fair value plus transaction costs and subsequently measured at amortised cost using the effective interest rate method.

Cash and cash equivalents include cash on hand, cash in transit, bank accounts and deposits with an original maturity of no more than three months.

Purchases and sales of all financial assets are accounted for at trade date.

At each balance date an assessment is made whether a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Financial liabilities

Financial liabilities, other than derivatives, are recognised initially at fair value less transaction costs and subsequently measured at amortised cost using the effective interest rate method.

Derivatives

Derivative financial instruments are recognised both initially and subsequently at fair value. They are reported as either assets or liabilities depending on whether the derivative is in a net gain or net loss position respectively.

Fair value hedge

Where a derivative qualifies as a hedge of the exposure to changes in fair value of an asset or liability (fair value hedge) any gain or loss on the derivative is recognised in profit and loss together with any changes in the fair value of the hedged asset or liability.

The carrying amount of the hedged item is adjusted by the fair value gain or loss on the hedged item in respect of the risk being hedged. Effective parts of the hedge are recognised in the same area of profit and loss as the hedged item.

D OTHER ASSETS

Property, plant and equipment (PPE)

Items of property, plant and equipment are initially recorded at cost.

Depreciation is charged on a straight-line basis at rates calculated to allocate the cost or valuation of an item of property, plant and equipment, less any estimated residual value, over its remaining useful life.

E OTHER LIABILITIES

Employee entitlements

Employee entitlements to salaries and wages, annual leave and other similar benefits are recognised in the profit and loss when they accrue to employees.

F REVENUE AND EXPENSES

Revenue

Interest income

Interest income is accrued using the effective interest rate method.

The effective interest rate exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount. The method applies this rate to the principal outstanding to determine interest income each period.

Expenses

Expenses are recognised in the period to which they relate.

Interest expense

Interest expense is accrued using the effective interest rate method.

The effective interest rate exactly discounts estimated future cash payments through the expected life of the financial liability to that liability's net carrying amount. The method applies this rate to the principal outstanding to determine interest expense each period.

Income tax

LGFA is exempt from income tax under Section 14 of the Local Government Borrowing Act 2011.

Goods and services tax

All items in the financial statements are presented exclusive of goods and service tax (GST), except for receivables and payables, which are presented on a GST-inclusive basis. Where GST is not recoverable as input tax, then it is recognised as part of the related asset or expense.

The net amount of GST recoverable from, or payable to, the IRD is included as part of receivables or payables in the statement of financial position.

The net GST paid to, or received from the IRD, including the GST relating to investing and financing activities, is classified as a net operating cash flow in the statement of cash flows.

Commitments and contingencies are disclosed exclusive of GST.

G LEASE PAYMENTS

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

H SEGMENT REPORTING

LGFA operates in one segment being funding of participating local authorities in New Zealand.

I JUDGEMENTS AND ESTIMATIONS

The preparation of these financial statements requires judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. For example, the present value of large cash flows that are predicted to occur a long time into the future depends critically on judgements regarding future cash flows, including inflation assumptions and the risk free discount rate used to calculate present values.

The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised, if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. Where these judgements significantly affect the amounts recognised in the financial statements they are described below and in the following notes.

2 Hedge accounting

LGFA is exposed to interest rate risk from fixed rate borrowing and variable rate lending to councils. LGFA manages this interest rate risk through the use of interest rate swaps. For hedge accounting purposes, LGFA has designated these swaps in fair value relationships to its fixed rate borrowing.

The gain or (loss) on the hedging instrument and the hedged item attributable to the hedged risk for fair value hedge relationships is shown in the table below.

Six months ended in \$000s	31 December 2016 Unaudited	31 December 2015 Unaudited
Hedging instruments – interest rate swaps	134,733	127,024
Hedged items attributable to the hedged risk – fixed rate bonds	(134,733)	(127,024)
Ineffectiveness recognised in profit or loss from fair value hedges	-	-

The gains or losses on the hedging instrument (interest rate swaps) and the hedged item (bonds) are mapped to the same fair value account. For this reason, the statement of comprehensive income will only report any ineffectiveness arising from the fair value hedge.

3 Issuance and on-lending expenses

Issuance and on-lending expenses are those costs that are incurred as a necessary expense to facilitate the ongoing issuance of LGFA debt securities.

Six months ended in \$000s	31 December 2016 Unaudited	31 December 2015 Unaudited
NZDMO facility fee	200	200
NZX	237	56
Rating agency fees	267	255
Legal fees for issuance	62	171
Regulatory, registry, other fees	18	14
Trustee fees	50	50
Approved issuer levy	865	751
Information services	65	59
	1,764	1,556

4 Operating expenses

Operating expenses are all other expenses that are not classified as 'Issuance and on-lending expenses.'

Six months ended in \$000s	31 December 2016 Unaudited	31 December 2015 Unaudited
Consultants	78	75
Directors' fees	174	144
Insurance	30	31
Legal fees	23	19
Other expenses	362	360
Auditor's remuneration		
Statutory audit	46	21
Advisory	4	-
Personnel	718	617
	1,435	1,268

5 Loans to local government

Includes loans and short-term loans to local government.

in \$000s	31 December 2016 Unaudited		30 June 2016	
	Short-term loans	Loans	Short-term loans	Loans
Ashburton District Council	10,008	15,756	10,006	15,820
Auckland Council	-	2,382,378	-	2,158,614
Buller District Council	-	20,003	-	20,002
Canterbury Regional Council	-	25,090	-	25,036
Christchurch City Council	71,187	1,254,483	65,177	1,209,669
Far North District Council	-	20,112	-	10,040
Gisborne District Council	4,974	17,056	4,970	17,060
Gore District Council	6,025	6,037	6,026	6,042
Greater Wellington Regional Council	-	255,741	-	255,660
Grey District Council	-	20,606	-	20,655
Hamilton City Council	-	260,765	-	230,663
Hastings District Council	4,976	50,164	-	50,175
Hauraki District Council	-	34,124	-	34,133
Horizons Regional Council	-	10,014	-	10,015
Horowhenua District Council	10,011	52,894	7,007	47,870
Hurunui District Council	-	19,068	-	17,069
Hutt City Council	-	79,653	-	79,711
Kaipara District Council	4,974	43,182	-	35,156
Kapiti Coast District Council	-	190,582	-	150,471
Manawatu District Council	-	51,059	-	51,035
Marlborough District Council	20,836	63,206	-	28,067
Masterton District Council	2,005	44,158	3,002	44,169
Matamata-Piako District Council	-	24,568	-	24,573
Nelson City Council	-	45,193	10,007	35,171
New Plymouth District Council	-	61,180	-	61,193
Opotiki District Council	-	5,196	-	5,210
Otorohanga District Council	-	9,214	-	9,246
Palmerston North City Council	-	77,276	-	77,295
Porirua City Council	9,982	23,611	9,982	23,621
Queenstown Lakes District Council	7,074	76,277	-	76,371
Rotorua District Council	-	104,991	-	100,025
Selwyn District Council	-	35,054	-	35,056
South Taranaki District Council	-	62,218	9,989	62,234
South Wairarapa District Council	-	7,537	-	7,536
Tararua District Council	1,004	10,035	-	9,033
Tasman District Council	-	90,293	-	90,314
Taupo District Council	-	125,399	-	125,431
Tauranga City Council	39,807	307,035	-	277,009
Thames-Coromandel District Council	-	35,065	-	35,069
Timaru District Council	5,106	51,312	9,737	51,325
Upper Hutt City Council	-	29,629	-	24,591
Waikato District Council	-	70,250	-	60,212
Waimakariri District Council	10,010	75,816	10,005	75,861
Waipa District Council	21,673	13,017	-	13,018
Wellington City Council	-	278,930	-	233,884
Western Bay of Plenty District Council	-	70,219	-	70,233
Whakatane District Council	-	31,093	3,015	28,076
Whanganui District Council	-	66,283	-	41,162
Whangarei District Council	9,972	122,519	9,968	122,558
	239,624	6,825,342	158,891	6,292,441

6 Other assets

in \$000s	31 December 2016 Unaudited	30 June 2016
Property, plant and equipment	50	50
Intangible assets	836	961
Total other assets	886	1,011

7 Bonds issued

As at 31 December 2016 Unaudited in \$000s		Face Value	Unamortised Premium	Accrued Interest	Fair Value Hedge Adjustment	Total
15 December 2017	6% coupon	1,015,000	16,062	2,844	-	1,033,906
15 March 2019	5% coupon	1,200,000	24,917	17,900	-	1,242,817
15 April 2020	3% coupon	635,000	(15,668)	4,082	-	623,414
15 May 2021	6% coupon	1,350,000	76,246	10,517	-	1,436,763
15 April 2023	5.5% coupon	1,330,000	72,688	15,675	-	1,418,363
15 April 2025	2.75% coupon	425,000	(19,380)	2,504	-	408,124
15 April 2027	4.5% coupon	860,000	30,039	8,293	-	898,332
Fair value hedge adjustment					134,733	134,733
Total		6,815,000	184,904	61,815	134,733	7,196,452

As at 30 June 2016 in \$000s		Face Value	Unamortised Premium	Accrued Interest	Fair Value Hedge Adjustment	Total
15 December 2017	6% coupon	1,015,000	24,292	2,662		1,041,954
15 March 2019	5% coupon	1,180,000	29,129	17,315		1,226,444
15 April 2020	3% coupon	565,000	(18,322)	3,566		550,244
15 May 2021	6% coupon	1,320,000	79,629	10,115		1,409,744
15 April 2023	5.5% coupon	1,285,000	70,428	14,869		1,370,297
15 April 2025	2.75% coupon	100,000	(3,157)	579		97,422
15 April 2027	4.5% coupon	755,000	23,373	7,148		785,521
Fair value hedge adjustment					338,032	338,032
Total		6,220,000	205,372	56,254	338,032	6,819,658

8 Borrower notes

Borrower notes are subordinated debt instruments (which are required to be held by each local authority that borrows from LGFA in an amount equal to 1.6% of the aggregate borrowings, excluding short-term loans, by that local authority).

LGFA may convert borrower notes into redeemable shares if it has made calls for all unpaid capital to be paid in full and the LGFA Board determines it is still at risk of imminent default.

9 Treasury stock and bond repurchase transactions

Periodically, LGFA subscribes for LGFA bonds as part of its tender process and holds these bonds as treasury stock. LGFA bonds held by LGFA as treasury stock are derecognised at the time of issue and no liability is recognised in the statement of financial position.

LGFA makes these treasury stock bonds available to banks authorised as its tender counterparties to borrow under short-term repurchase transactions. The objective of the bond lending facility is to assist with improving secondary market liquidity in LGFA bonds. Bonds lent to counterparties are disclosed as a separate stock lending liability on the face of the statement of financial position.

LGFA notifies the market on a monthly basis the amount of outstanding repurchase transactions and LGFA bonds held as treasury stock.

in \$000s		31 December 2016 Unaudited		30 June 2016	
		Treasury stock	Bond repurchase trades	Treasury stock	Bond repurchase trades
15 March 2019	5% coupon	46,500	3,714	-	-
15 April 2020	3% coupon	50,000	-	-	-
15 May 2021	6% coupon	50,000	-	-	-
15 April 2023	5.5% coupon	50,000	-	-	-
15 April 2025	2.75% coupon	50,000	-	-	-
15 April 2027	4.5% coupon	50,000	-	-	-
		296,500	3,714	-	-

10 Reconciliation of net profit to net cash flow from operating activities

Six months ended in \$000s	31 December 2016 Unaudited	31 December 2015 Unaudited
Net profit/(loss) for the period	5,312	4,769
Cash applied to loans to local government	(662,866)	(746,139)
Non-cash adjustments		
Amortisation and depreciation	2,999	1,261
Working capital movements		
Net change in trade debtors and receivables	59	51
Net change in prepayments	(292)	(481)
Net change in accruals	(58)	202
Net Cash From Operating Activities	(654,846)	(740,337)

11 Share capital

As at 31 December 2016 LGFA had 45 million ordinary shares on issue, 20 million of which remain uncalled. All ordinary shares rank equally with one vote attached to each ordinary share.

As at 31 December 2016, the shareholding of the New Zealand Government had been fully paid up. For all other shareholders, 50% of the shareholding had been called.

in \$000s	31 December 2016		30 June 2016	
New Zealand Government	5,000,000	11.1%	5,000,000	11.1%
Auckland Council	3,731,960	8.3%	3,731,960	8.3%
Christchurch City Council	3,731,960	8.3%	3,731,960	8.3%
Hamilton City Council	3,731,960	8.3%	3,731,960	8.3%
Bay of Plenty Regional Council	3,731,960	8.3%	3,731,960	8.3%
Greater Wellington Regional Council	3,731,960	8.3%	3,731,960	8.3%
Tasman District Council	3,731,960	8.3%	3,731,960	8.3%
Tauranga City Council	3,731,960	8.3%	3,731,960	8.3%
Wellington City Council	3,731,960	8.3%	3,731,960	8.3%
Western Bay of Plenty District Council	3,731,960	8.3%	3,731,960	8.3%
Whangarei District Council	1,492,784	3.3%	1,492,784	3.3%
Hastings District Council	746,392	1.7%	746,392	1.7%
Marlborough District Council	400,000	0.9%	400,000	0.9%
Selwyn District Council	373,196	0.8%	373,196	0.8%
Gisborne District Council	200,000	0.4%	200,000	0.4%
Hauraki District Council	200,000	0.4%	200,000	0.4%
Horowhenua District Council	200,000	0.4%	200,000	0.4%
Hutt City Council	200,000	0.4%	200,000	0.4%
Kapiti Coast District Council	200,000	0.4%	200,000	0.4%
Manawatu District Council	200,000	0.4%	200,000	0.4%
Masterton District Council	200,000	0.4%	200,000	0.4%
New Plymouth District Council	200,000	0.4%	200,000	0.4%
Otorohanga District Council	200,000	0.4%	200,000	0.4%
Palmerston North District Council	200,000	0.4%	200,000	0.4%
South Taranaki District Council	200,000	0.4%	200,000	0.4%
Taupo District Council	200,000	0.4%	200,000	0.4%
Thames-Coromandel District Council	200,000	0.4%	200,000	0.4%
Waimakariri District Council	200,000	0.4%	200,000	0.4%
Waipa District Council	200,000	0.4%	200,000	0.4%
Wanganui District Council	200,000	0.4%	200,000	0.4%
Whakatane District Council	200,000	0.4%	200,000	0.4%
	45,000,000	100%	45,000,000	100%

12 Related parties

Identity of related parties

The Company is related to the local authorities set out in the Shareholder Information by shareholding.

The Company operates under a Statement of Intent with the respective local authorities that requires the Company to optimise the debt funding terms and conditions for participating local authorities.

Shareholding local authorities, and non-shareholder local authorities who borrow more than \$20 million, are required to enter into a guarantee when they join or participate in LGFA. The guarantee is in respect of the payment obligations of other guaranteeing local authorities to the LGFA (cross guarantee) and of the LGFA itself.

Related party transactions

LGFA was established for the purpose of raising funds from the market to lend to participating councils. The lending to individual councils is disclosed in note 5, and interest income recognised on this lending is shown in the Statement of Comprehensive Income. The requirement for participating councils to subscribe to LGFA borrower notes is disclosed in note 8, and the interest expense on these is shown in the Statement of comprehensive income.

13 Subsequent events

There have been no significant events after balance date that have affected the accuracy of these financial statements.

Subsequent to balance date, LGFA has issued \$160 million in bonds through a tender on 15 February 2017



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Below: The Dive Crescent project, to replace a dilapidated seawall, also gave Council the opportunity to include a three-metre wide shared pedestrian/cycle path as part of the overall design. Tauranga City Council.

Back cover: Major capital projects for Christchurch in 2016 included the completion of many new community centres, such as the Governors Bay Community Centre. Christchurch City Council.



