# Quarterly Report

Quarter 4: 2018 - 2019
Period ended: 30 June 2019

NEW ZEALAND
LOCAL GOVERNMENT
FUNDING AGENCY

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## A. June quarter issuance and highlights summary

| Quarter | Total | Bespoke Maturity | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2027 | 2033 |
|---|---|---|---|---|---|---|---|---|---|---|
| Bonds issued $m | **331** | N/A | - | - | 100 | 21 | - | 100 | - | 110 |
| Term Loans to councils $m | **617.4** | 280.5 | - | - | 4.5 | 37.5 | 187 | - | 16.5 | 35 |
| Term Loans to councils #. | **38** | 20 | - | - | 2 | 6 | 5 | - | 5 | 2 |

| Year to date | Total | Bespoke Maturity | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2027 | 2033 |
|---|---|---|---|---|---|---|---|---|---|---|
| Bonds issued $m | **2456** | N/A | - | 30 | 440 | 21 | 950 | 410 | 220 | 385 |
| Term Loans to councils $m | **2,446.3** | 1,344.5 | 38.5 | 10.5 | 350 | 131.5 | 452 | 223 | 72.5 | 66.5 |
| Term Loans to councils # | **236** | 125 | 7 | 5 | 22 | 20 | 27 | 23 | 17 | 4 |

**Key points and highlights for the June quarter:**

- The LGFA bond curve continued to flatten and fall over the quarter with yields declining between 20 bps (2020s) and 36 bps (2025s and longer). Over the past year the yield on the 2020 LGFA bond has declined 63 bps while the 2033 LGFA bond yield has declined 140 bps closing at historic lows.
- LGFA issued $331 million of bonds during the quarter via one tender of $171 million and a tender of $160 million. The financial year issuance of $2.456 billion was a record and compares to the average annual issuance of $1.4 billion. The average term of issuance during the quarter of 7.52 years was longer than both the previous quarter and the average term of 6.62 years for the 2018-19 year. The past year issuance was dominated by the jumbo 2024 syndicated issue.
- LGFA margins to swap were either unchanged or slightly wider by between 2 bps and 4 bps over the quarter. The large amount of issuance and narrowing in swap spreads to NZGB were the major influences. LGFA spreads to NZGB narrowed between 3 bps (2020s) and 14 bps (2033s) over the quarter.
- Long dated on-lending to council borrowers during the quarter was another strong amount of $617.4 million including $280.5 million of bespoke maturity loans (45% of total lending). The average term of on-lending during the quarter at 5.55 years was shorter than the 2018-19 financial year average of 6 years and 7.04 years for the 2017-18 financial year.
- LGFA has market share of 92.3% of total council borrowing for the rolling twelve-month period to June 2019 (up 69.9% from June 2018). We provided 100% of council borrowing during the June 2019 quarter.
- Short-term lending to councils remains supported by councils with loans outstanding of $362 million as at 30 June 2019. This was a decrease of $132 million over the quarter (due to councils repaying before the end of financial year) and the number of councils using this product was unchanged at thirty.
- LGFA Net Operating Gain (unaudited) for the twelve-month period was $11.201 million or $326k above budget with Net Interest Income $151k above budget and expenses $175k below budget.
- One new council joined LGFA over the quarter (Invercargill City Council), increasing the number of councils over the past twelve months by eight to sixty-four councils. There are fifty-two council guarantors as at 30 June 2019. We are expecting a further two councils to join over the next twelve months.

## B. LGFA bond tenders during quarter

LGFA held two bond tenders during the quarter.

Tender 63: 07 May 2019 $160 million

| Tender 63 | Apr-22 | Apr-25 | Apr-33 |
|---|---|---|---|
| Total amount offered $m | 50 | 50 | 60 |
| Total amount allocated $m | 50 | 50 | 60 |
| Total number bids received | 11 | 23 | 27 |
| Total amount of bids received $m | 93 | 189 | 125 |
| Total number of successful bids | 1 | 1 | 8 |
| Highest accepted yield % | 1.845 | 2.290 | 3.145 |
| Lowest yield accepted % | 1.845 | 2.290 | 3.114 |
| Highest yield rejected % | 1.940 | 2.450 | 3.320 |
| Lowest yield rejected % | 1.860 | 2.300 | 3.145 |
| Weighted average accepted yield % | 1.845 | 2.290 | 3.127 |
| Weighted average rejected yield % | 1.891 | 2.331 | 3.190 |
| Coverage ratio | 1.86 | 3.78 | 2.08 |
| NZGB spread at issue bps | 39 | 71 | 106 |
| Swap spread at issue bps | 21 | 45.8 | 72 |
| Swap spread: AA council bps | 32.75 | 57.75 | 87 |
| Swap spread: AA- council bps | 37.75 | 62.75 | 97 |
| Swap spread: A+ council bps | 42.75 | 67.75 | 102 |
| Swap spread: unrated council bps | 52.75 | 77.75 | 112 |

Tender 63 achieved a very strong outcome with good demand for the three bond maturities offered. Spreads to both NZGB and swap were generally tighter by 7 bps to 10 bps, yields were at historic lows and successful bids at prevailing secondary market mid-levels.

The three-month gap from the previous February tender (excluding the March syndication), improving global credit market sentiment helped, recent offshore investor buying, the positive ratings outlook from S&P and only one Kauri issue since March helped improve sentiment.

The tender size of $160 million was in line with the historical average tender size ($163 million). Council borrowing demand remained strong with new borrowing the key driver rather than refinancing.

Bidding volume was good with the overall bid coverage ratio of 2.6x the second highest for over a year. Bidders were aggressive with only one successful bid for the 2022s and 2025s.

The average maturity of the LGFA bonds issued at 8.01 years was the longest since the August 2018 tender. The average for the financial year to date was 6.59 years (albeit dominated by the 2024 syndication).

While we issued $160 million of LGFA bonds we on-lent $211 million to thirteen councils with an average term of lending at 6.58 years.

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Tender 64: 12 June 2019 $171 million

| Tender 64 | Apr-22 | Apr-23 | Apr-25 | Apr-33 |
|---|---|---|---|---|
| Total amount offered $m | 50 | 21 | 50 | 50 |
| Total amount allocated $m | 50 | 21 | 50 | 50 |
| Total number bids received | 9 | 8 | 18 | 23 |
| Total amount of bids received $m | 79 | 59 | 124 | 69 |
| Total number of successful bids | 4 | 2 | 6 | 20 |
| Highest accepted yield % | 1.665 | 1.780 | 2.065 | 2.910 |
| Lowest yield accepted % | 1.650 | 1.780 | 2.050 | 2.835 |
| Highest yield rejected % | 1.700 | 1.820 | 2.120 | 2.930 |
| Lowest yield rejected % | 1.665 | 1.780 | 2.065 | 2.910 |
| Weighted average accepted yield % | 1.658 | 1.780 | 2.062 | 2.878 |
| Weighted average rejected yield % | 1.681 | 1.793 | 2.079 | 2.922 |
| Coverage ratio | 1.58 | 2.81 | 2.48 | 1.38 |
| NZGB spread at issue bps | 39 | 48 | 70 | 100 |
| Swap spread at issue bps | 22.8 | 29.0 | 45.8 | 75.35 |
| Swap spread: AA council bps | 34.5 | 41 | 58 | 92 |
| Swap spread: AA- council bps | 39.5 | 46 | 63 | 97 |
| Swap spread: A+ council bps | 44.5 | 51 | 68 | 102 |
| Swap spread: unrated council bps | 54.5 | 61 | 78 | 112 |

Tender 64 achieved an average result with only good demand for the last issuance of the 2023s but lower bid volumes, bonds issued 3 bps above mid rates and wider spreads to both NZGB and swaps on the other three bonds tendered. The larger tender size and yields at historic lows had dampened investor sentiment. The record $2.4 billion of issuance over the past year has also left the market slightly overweight LGFA bonds.

The tender size of $171 million was in line with the historic average tender size.

We tendered the current issuance maturities of 2022s,2025s and 2033s but increased the 2023s by $21 million to reach the $1.5 billion cap on that bond.

Bidding volume were light with the overall bid coverage ratio of 1.9x the lowest since October 2018. The successful bid ranges ranged between nil for the 2023s and 7.5 bps for the 2033s.

Spread to NZGB were tighter but spreads to swap wider compared to the May 2019 tender. The spread movements had already partially occurred prior to the tender in response to the higher projected issuance of NZGBs by Central Government.

The average maturity of the LGFA bonds issued was 7.06 years.

While we issued $171 million of LGFA bonds we on-lent $174 million to ten councils and the average term of lending at 6.83 years was slightly above the recent lending term and our 4.8-year average

## C. Key performance indicators

We have met one KPI and did not meet three KPIs as at the end of the June 2019 quarter.

Issuance and operating expenses (excluding AIL) are above budget by approximately $180k for the twelve-month period to 30 June 2019. Higher legal and NZX listing costs associated with larger bond issuance than forecast (due to higher council lending than forecast) have contributed to these costs exceeding budget. Net Operating Gain is however above budget by $88k.

We changed our base lending margin for long dated lending to a standard 10 bps margin regardless of the borrowing term from 1 July 2018. The average base margin target of 10.1 bps is not achieved when we combine the long-dated lending margin across the 12-month period to 30 June 2019 with our short-dated lending outstanding as at 30 June 2019. The short-dated lending margins are higher than 10 bps because it is an all-in borrowing margin over BKBM (including LGFA cost of borrowing).

We have been unable to improve our estimated interest cost savings for council borrowing through LGFA compared to councils borrowing in their own name compared to the levels at the start of the financial year. This objective remains difficult to achieve as the spread between what councils borrow at over LGFA borrowing cost will naturally narrow as the borrowing term approaches maturity. The record volume of council borrowing has led to LGFA issuing a record amount of bonds in the financial year so while borrowing spreads have narrowed, they have not narrowed as much as the spread for other borrowers.

Our volume of council lending is above the SOI forecast by $1.157 billion due to both the larger amount of short-term lending and Auckland Council resuming borrowing through LGFA. The loan book is near historic highs.

| **Measure** | | **Prior full year to June 2018** | **Q1 30 Sept 2018** | **Q2 31 Dec 2018** | **Q3 31 Mar 2019** | **Q4 30 June 2019** |
|---|---|---|---|---|---|---|
| Average base margin over cost of funds for short term and long-term lending | Target % | | < 0.10% | | | |
| | Average actual % | 0.105% | 0.095% (0.10% for long term and 0.09% for short term) ✓ | 0.095% (0.10% for long term and 0.09% for short term) ✓ | 0.10% (0.10% for long term and 0.104% for short term) ✓ | 0.101% (0.10% for long term and 0.106% for short term) ✗ |
| Estimated interest cost savings to AA rated councils | Target Improvement on prior year as at each quarter | | **Q1 30 Sept 2018** | **Q2 31 Dec 2018** | **Q3 31 Mar 2019** | **Q4 30 June 2019** |
| | 2019 maturity At quarter end | 11 bps | 8 bps ✗ | 2 bps ✗ | n/a | n/a |
| | 2021 maturity | 19 bps | 20 bps | 17 bps | 20 bps | 9 bps |

| | | | | | | |
|---|---|---|---|---|---|---|
| | At quarter end | | ✓ | ✗ | ✓ | ✗ |
| | 2025 maturity<br>At quarter end | 10 bps | 20 bps<br>✓ | 15 bps<br>✓ | 14 bps<br>✓ | 7 bps<br>✗ |
| Issuance and operating expenses (excluding AIL) YTD | Target ($) | | **$1.42 m<br>(YTD as at Q1)** | **$2.84 m<br>(YTD as at Q2)** | **$4.16 m<br>(YTD as at Q3)** | **$5.67 m<br>(FULL YEAR)** |
| | Actual ($) | $5.16 m | $1.36 m<br>✓ | $2.81 m<br>✓ | $4.33 m<br>✗ | $5.85m<br>✗ |
| Lending (short and long term) to participating councils | Target ($) | | **$8.378 b<br>(YTD as at Q1)** | **$8.818 b<br>(YTD as at Q2)** | **$7.898 b<br>(YTD as at Q3)** | **$8.105 b<br>(FULL YEAR)** |
| | Actual ($) | $7.927 b | $8.641 b<br>✓ | $9.268 b<br>✓ | $8.812 b<br>✓ | $9.262 b<br>✓ |

## D. Summary financial information (provisional and unaudited)

| **Financial Year ($m)** | **YTD as at Q1** | **YTD as at Q2** | **YTD as at Q3** | **YTD as at Q4** |
|---|---|---|---|---|
| **Comprehensive income** | **30-Sep-18** | **31-Dec-18** | **31-Mar-19** | **30-June-19** |
| Interest income | 88.71 | 180.89 | 273.13 | 361.08 |
| Interest expense | 83.43 | 171.12 | 258.56 | 342.32 |
| **Net interest revenue** | **5.29** | **9.77** | **14.57** | **18.76** |
| | | | | |
| Issuance and On-lending costs | 0.57 | 1.17 | 1.90 | 2.58 |
| Approved issuer levy | 0.19 | 0.89 | 1.00 | 1.71 |
| Operating expenses | 0.79 | 1.64 | 2.43 | 3.27 |
| **Issuance and operating expenses** | **1.55** | **3.70** | **5.33** | **7.56** |
| | | | | |
| **Net Profit** | **3.74** | **6.08** | **9.24** | **11.20** |

| **Financial position ($m)** | **30-Sep-18** | **31-Dec-18** | **31-Mar-19** | **30-Jun-19** |
|---|---|---|---|---|
| Retained earnings + comprehensive income | 41.74 | 44.05 | 47.24 | 49.17 |
| Total assets (nominal) | 8,857.01 | 9,434.82 | 9,402.11 | 9708.03 |
| Total LG loans (nominal) | 8,631.65 | 9,276.43 | 8,811.97 | 9,262.86 |
| Total LGFA bills (nominal) | 470.00 | 485.00 | 545.00 | 505.00 |
| Total LGFA bonds (nominal) | 8,104.00 | 8,704.00 | 8,604.00 | 8935.00 |
| Total borrower notes (nominal) | 131.20 | 139.86 | 133.12 | 142.43 |
| Total equity | 66.74 | 69.05 | 72.24 | 74.17 |

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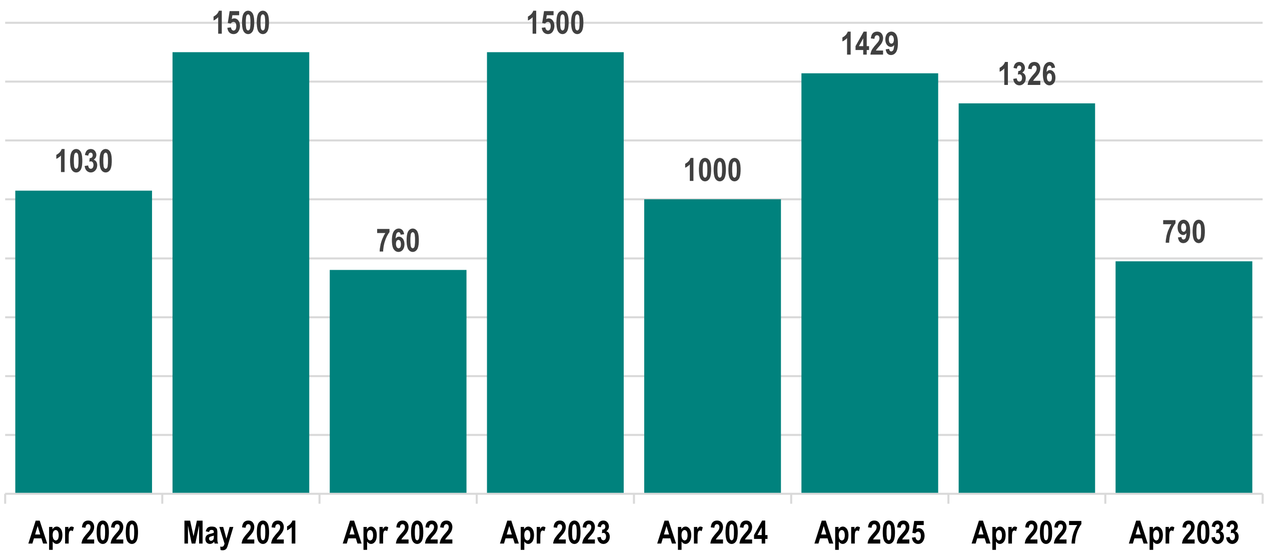
LGFA bonds on issue (NZ$ million)
As at 30 June 2019 : NZ$ 9,335 million
Includes NZ$400 million treasury stock




## E. Quarterly compliance summary

| Policy | Limit | Policy page ref | Continuous Compliance |
|---|---|---|---|
| One-month Liquidity Monitor | >120% | S1-1.1 | Yes |
| Three Month Liquidity Monitor | >110% | S1-1.2 | Yes |
| Twelve Month Liquidity Monitor | >110% | S1-1.3 | Yes |
| Council Exposure (any 12-month period) | <10% of Balance Sheet | S1-1.5 | Yes |
| Liquidity Buffer | >110% | S1-1.4 | Yes |
| Partial Differential Hedge (PDH Interest Rate Gap Report | $40,000 | S3-4.1 | Yes |
| Value at Risk (VaR) | $250,000 | S3-4.2 | Yes |
| Council Maturity (any 12-month period) | $100m or 33% of LGFA borrowing | S1-1.6 | No |
| Funding Largest Council Exposure | >100% | S1-1.7 | Yes |
| Foreign Exchange Exposure | Nil | S7-3.1 | Yes |
| NZDMO Facility Utilisation | Report monthly | S8-8.5 | Yes |
| Counterparty Credit Limits | 80% of Portfolio<br>$125m Counterparty (category 3) | S4 | Yes |
| Auckland Council Exposure (proportion of total Council exposure) | <40% | S1-1.8 | Yes |
| Balance Sheet Maturity Mismatch | <15% of Balance Sheet | S2-2.1 | Yes |
| Financial Covenants | Various (as set out on p13) | S9 | Yes |
| Authorising Treasury transactions | Two approvers, one signature | S8-8.4 | Yes |

**Details for compliance breaches over quarter.**

There was a compliance breach where a council had inadvertently breached the following limit in late 2018

> To minimise concentration risk, the LGFA will require that no more than the greater of $NZD100 million or 33% of a council’s borrowings from the LGFA will mature in any 12-month period.

The limit breach was discovered and then escalated to both the LGFA Board and Shareholder Council in May 2019. The breach occurred because the council had borrowed 100% of its financing through LGFA in short dated loans (less than one year) and the LGFA management process had not picked up short dated borrowing within this limit. This limit when established in 2012 was originally intended to monitor long dated borrowing. It should be noted that the limit breach was the not the fault of the council. LGFA worked with the council to extend some of their short term borrowing into long dated funding to resolve the breach in early June.

## F. Performance against SOI objectives and performance targets

### Primary objectives

#### 1. Providing savings in annual interest costs for all Participating Local Authorities on a relative basis to other sources of financing

LGFA on-lending base margins are 10 bps for all terms between April 2020 and April 2033 following our change to a flat margin structure in June 2018. The base margin charge covers our operating costs and provides for our capital to grow in line with the growth in our balance sheet to maintain a capital buffer.

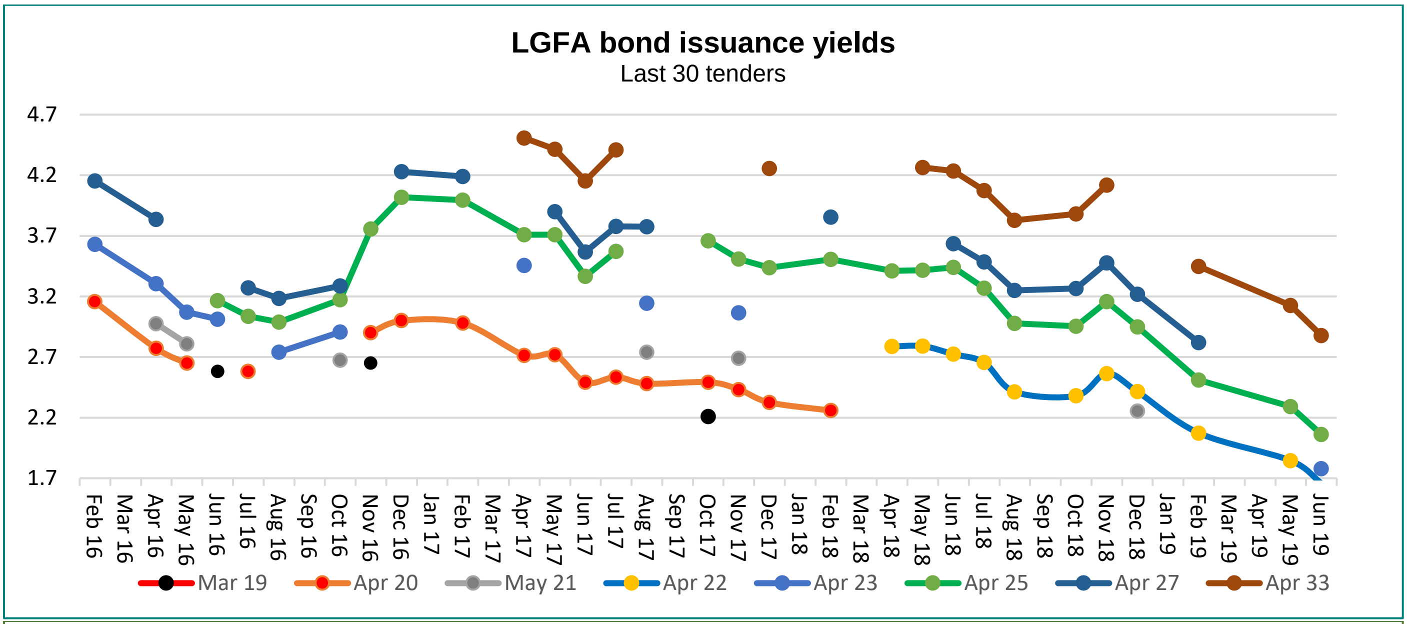
Our estimated annual savings to councils that are based upon the secondary market levels at 30 June 2019 of LGFA bonds compared to bonds issued by Auckland and Dunedin councils are between 7 bps and 9 bps depending upon the term of borrowing. The amount of savings has reduced over the past quarter by between 7 bps and 11 bps and reduced by between 3 bps and 13 bps over the past year. The LGFA borrowing margins to swap have moved out over the past twelve months on our record issuance volume while both Auckland Council and Dunedin City Treasury have issued relatively small amounts of bonds in their own name. LGFA borrowing spreads have narrowed to both swap and NZGB over the past year between 2 bps to 18 bps.

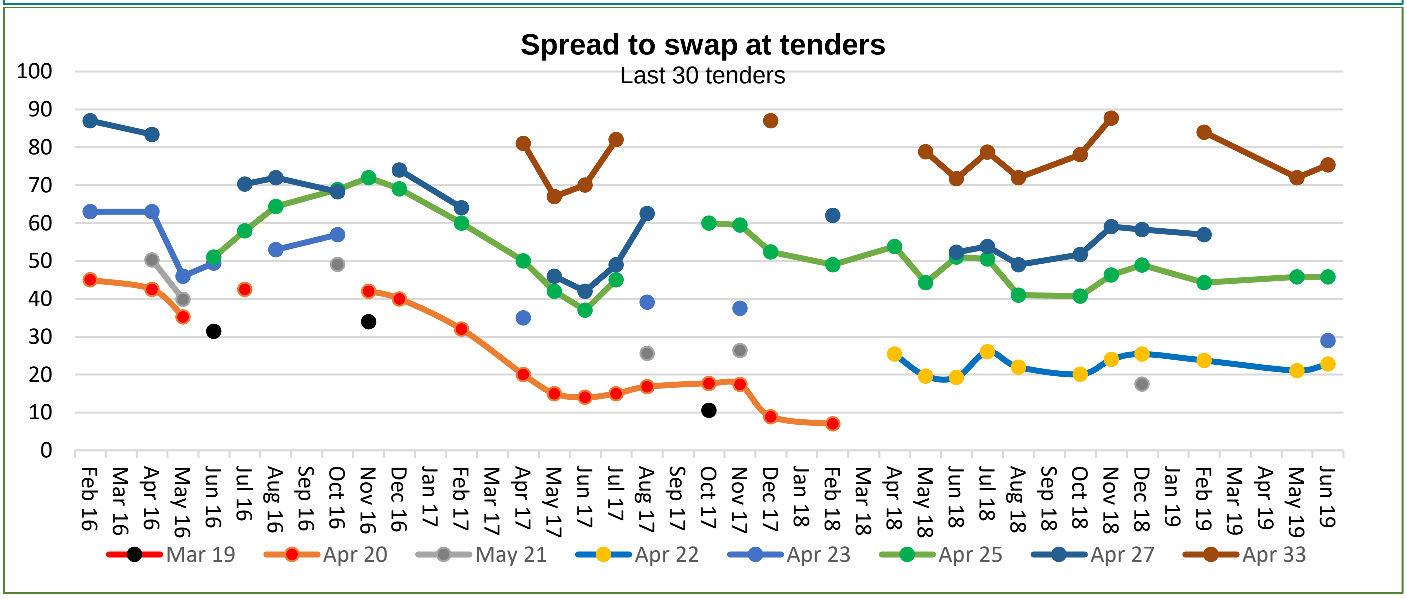
| 30-Jun-19 | Savings to AA rated councils (bps) | | | |
|---|---|---|---|---|
| | Dunedin 2020 | Dunedin 2021 | Auckland 2022 | Auckland 2025 |
| AA rated councils' margin to swap (bps) | 29 | 34 | 39 | 58 |
| Less LGFA margin to swap (bps) | -11 | -15 | -22 | -41 |
| LGFA gross funding advantage (bps) | 18 | 19 | 17 | 17 |
| Less LGFA base margin (bps) | -10 | -10 | -10 | -10 |
| **Total savings (bps)** | 8 | 9 | 7 | 7 |

Note that from 30 June 2017 we removed the implied "LGFA effect" of 10 bps of additional savings in borrowing costs from the above analysis. The LGFA effect was the assessment of immediate savings to councils when LGFA first commenced lending to councils in February 2012.

Outright yields declined to historic lows as global central banks (including the RBNZ) softened monetary policy either through lowering interest rates or forecasting additional stimulus. The interest rate curve continued to flatten with yields on short dated LGFA bond yields (2020s) declining by 20 bps over the quarter while long dated LGFA bond yields (2033s) declined by 36 bps. Over the past year the respective yields have declined by 63 bps (0.63%) and 140 bps (1.4%).

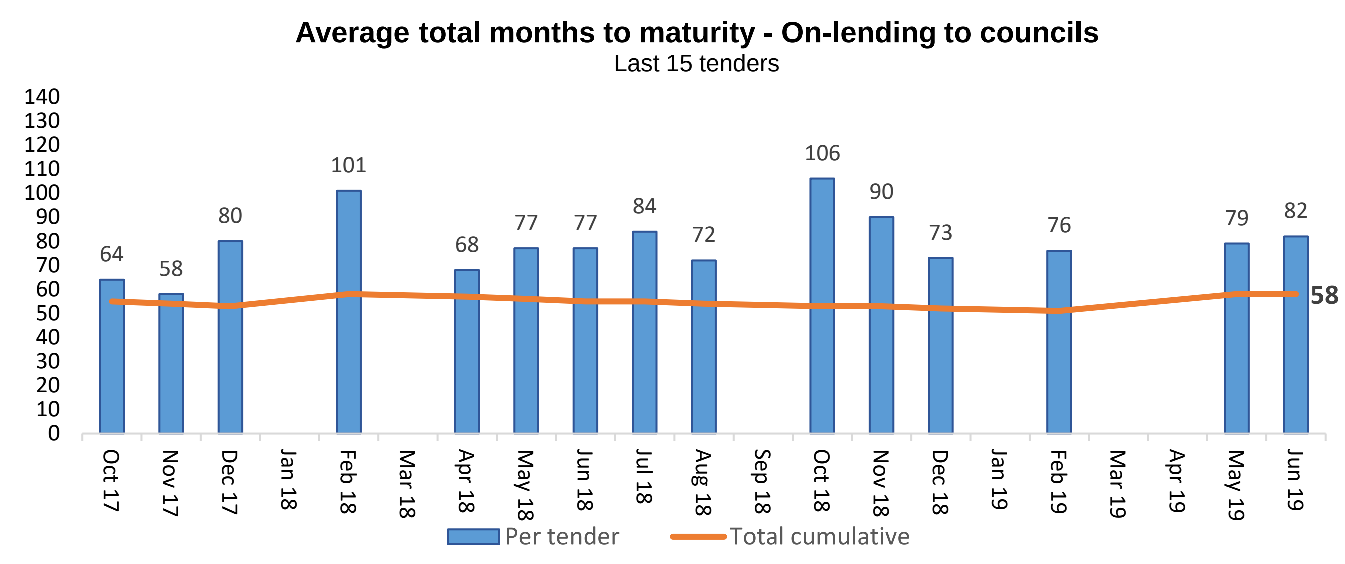
We closely monitor the Kauri market for ongoing supply and price action as this other high-grade issuance by "AAA" rated Supranational issuers such as the World Bank (IBRD), Nordic Investment Bank (NIB) and the Asian Development Bank (ADB) influences LGFA demand and pricing. These borrowers are our peer issuers in the NZD market and have the most influence on our pricing. The June quarter was very quiet for Kauri issuance with a $200 million issue of seven-year bonds undertaken by Asian Development Bank. The same theme continues of reduced offshore investor demand for NZD product as well as more attractive borrowing spreads for issuers in the US and European markets has led to the fall in issuance activity. This has assisted LGFA to issue a greater volume but has not led to significant margin improvement.



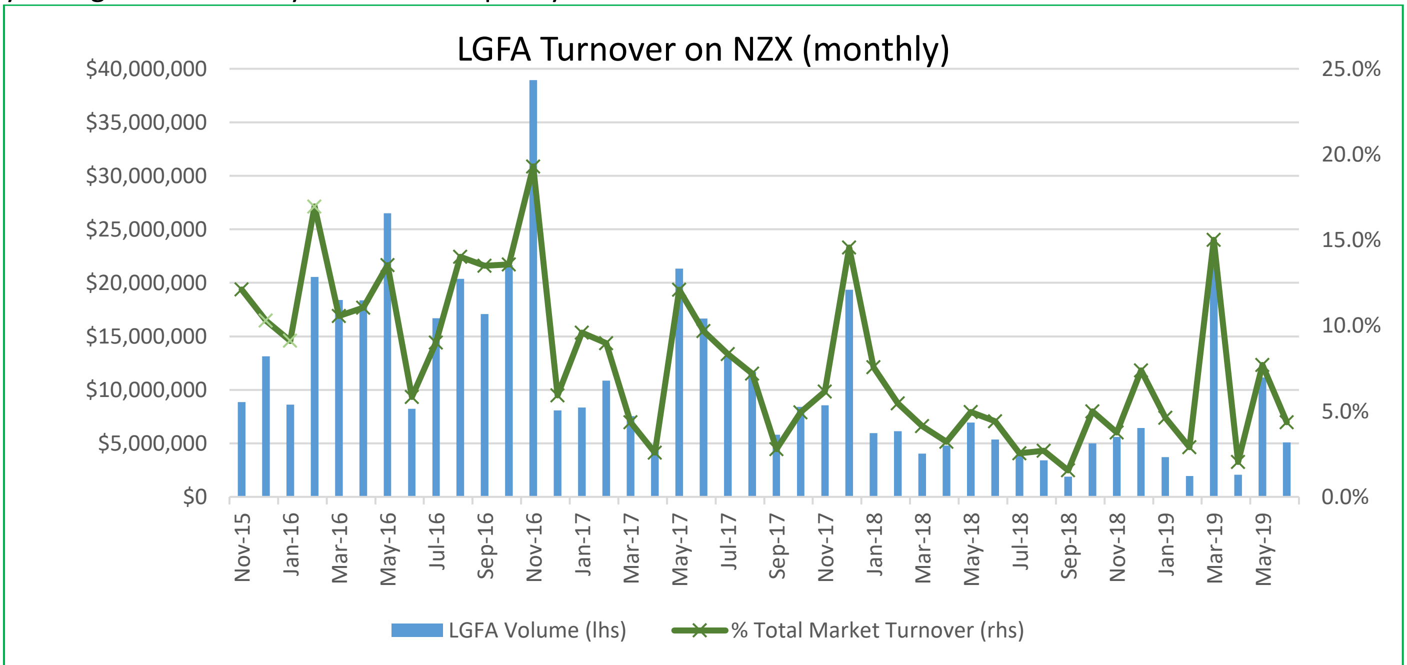

## 2. Making longer-term borrowings available to Participating Local Authorities

The average borrowing term (excluding short dated borrowing but including bespoke borrowing) for the June 2019 quarter by council members was 5.55 years and this was slightly shorter than the 6.0 years average term for 2018-19 year and shorter compared to the 7.04 average term for the 2017-18 prior year. The shortening in average borrowing term is explained by councils accessing the new April 2022 and April 2024 maturities.




**3. Enhancing the certainty of access to debt markets for Participating Local Authorities, subject always to operating in accordance with sound business practice**

LGFA bonds were listed on the NZX Debt Market in November 2015 and average turnover on the NZX Debt market has been $11.1 million per month or 8.1% of the total turnover of the NZX Debt Market. Turnover on the NZX remains light as retail investors are more attracted to high term deposit rates and higher yielding bond issues by lower credit quality borrowers.



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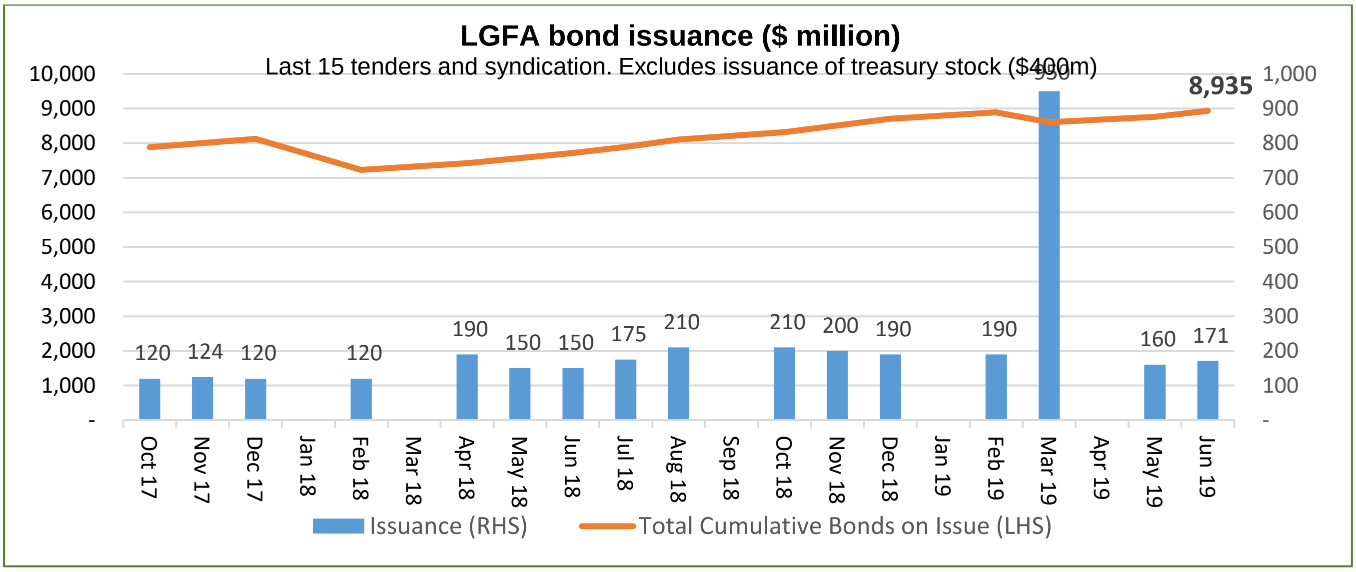
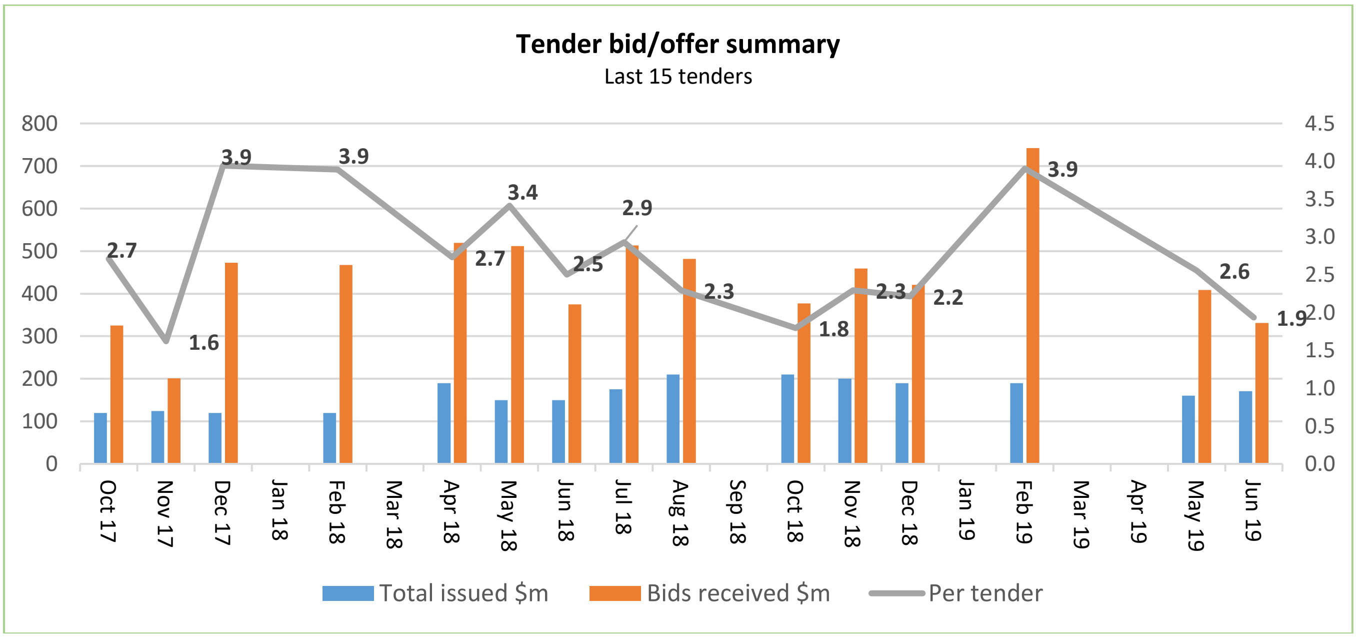
NEW ZEALAND LOCAL GOVERNMENT FUNDING AGENCY

LGFA started issuing LGFA Bills and short dated (less than 1 year) lending to councils in late 2015. As at June 2019 there were LGFA Bills of $505 million on issue and short-term loans of $362 million.

LGFA documented an Australian Medium-Term Notes Programme in November 2017 to provide the ability to issue in currencies other than NZD. We have no immediate intention to use this programme, but it provides flexibility in case of the unlikely scenario of a significant market disrupting event in the future.

We held two LGFA bond tenders during the quarter and market support was average with overall tender coverage ratios of 1.9x and 2.6x and support for the individual maturities between 1.38x and 3.78x.



**4. Offering more flexible lending terms to Participating Local Authorities**

Bespoke lending continues to be a popular borrowing option for council members. During the quarter we lent $280.5 million into bespoke maturity dates (non LGFA bond dates) and the amount of bespoke maturity loans in the 12-month period to 30 June 2019 was $1.344.5 billion. Bespoke lending comprised 45% of total term lending by LGFA to its members during the June quarter and 55% for the 12-month period to 30 June 2019.

Short term borrowing by councils has been well received with loan terms to date of between one month and 12 months on $362 million of loans outstanding as at 30 June 2019 to thirty councils. This is a significant increase compared to June 2018 where we had lent $244 million to nineteen councils and has led us to issue $545 million of LGFA bills.

**5. 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.**

LGFA had meetings with thirty councils during the June quarter (fifty-nine for the twelve-month period to June 2019) to discuss their financial performance and any developments with the underlying council operations. LGFA reviews council agendas and management reports on an ongoing basis for those councils on the LGFA borrower watch-list.

LGFA has commenced work on credit default assessment analysis of its member councils in preparation for adopting IFRS9 for accounting purposes.

LGFA management met representatives from Morrison Low to discuss the local government sector, presented at the Bancorp Local Authority Day and attended the Department of Internal Affairs Workshop on Local Government Financing and Funding.

## Additional objectives

**6. Operate with a view to making a profit sufficient to pay a dividend in accordance with its stated Dividend Policy**

LGFA’s Net Operating Gain on an unaudited management account basis of $11.201 million for the twelve-month period to 30 June 2019 exceeded the SOI forecast of $10.875 million by $326k. The average cost of funds for the 2018-19 financial year to date is 2.78%. This is lower than the 3.14% for the prior 2017-18 financial year due to the lower outright level of interest rates. The LGFA Board has the sole discretion to set the dividend.

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

LGFA derives market share estimates from the PwC Local Government Quarterly Debt Report. The LGFA market share of total sector borrowing for the June 2019 quarter was 100% and for the twelve-month period to June 2019 was 92.3%. Adjusting for Auckland Council borrowing in its own name our market share for the year to June 2019 was also 92.3%. Our market share remains strong compared to our global peers.

As at 30 June 2019, there are sixty-four participating local authority members of LGFA and we estimate a further two councils could become members in the next twelve months.

**8. Ensure its products and services are delivered at a cost that does not exceed the forecast for issuance and operating expenses**

Expenses for the twelve-month period on an unaudited, management basis were $7.558 million which is $175k below budget. This variance is the consequence of:

- Issuance and on-lending costs (excluding AIL) at $2.579 million were $263k above budget. Lower fees than budgeted relating to the NZDMO facility were offset by higher NZX costs and legal costs. A larger amount of bond issuance and short-term lending increased these costs relative to budget.

- Operating costs at $3.271 million were $76k below budget due to lower travel, governance and overhead costs offset by additional legal costs relating to LGFA progressing its work on the ability to lend to CCOs.

- Approved Issuer Levy payments of $1.708 million were less than our forecast of $2.070 million by $362k due to a lower level of LGFA bonds holdings by offshore investors relative to budget.

**9. Take appropriate steps to ensure compliance with the Health and Safety at Work Act 2015**

LGFA has a Health and Safety staff committee and reporting on Health and Safety issues are made to the LGFA board on a regular basis by the Risk and Compliance Manager. There were no Health and Safety incidents during the quarter.

**10. Maintain LGFA's credit rating equal to the New Zealand Government sovereign rating where both entities are rated by the same Rating Agency**

LGFA has an annual review process regarding our credit ratings from Standard and Poor's ("S&P") and Fitch Ratings ("Fitch") and meets with both agencies at least annually. Meetings were held in July 2018 with S&P and in September 2018 with Fitch.

On 4 February 2019, S&P placed our long-term credit rating on positive outlook, following their decision to place the long-term credit rating of the New Zealand Government on positive outlook the previous week.

On 18 November 2018, Fitch reaffirmed our long-term credit rating as AA+ and classified LGFA as a corporate mission, government related entity (GRE) under its GRE rating criteria. Fitch equalises our ratings with those of the New Zealand Government.

**11. Achieve the financial forecasts**

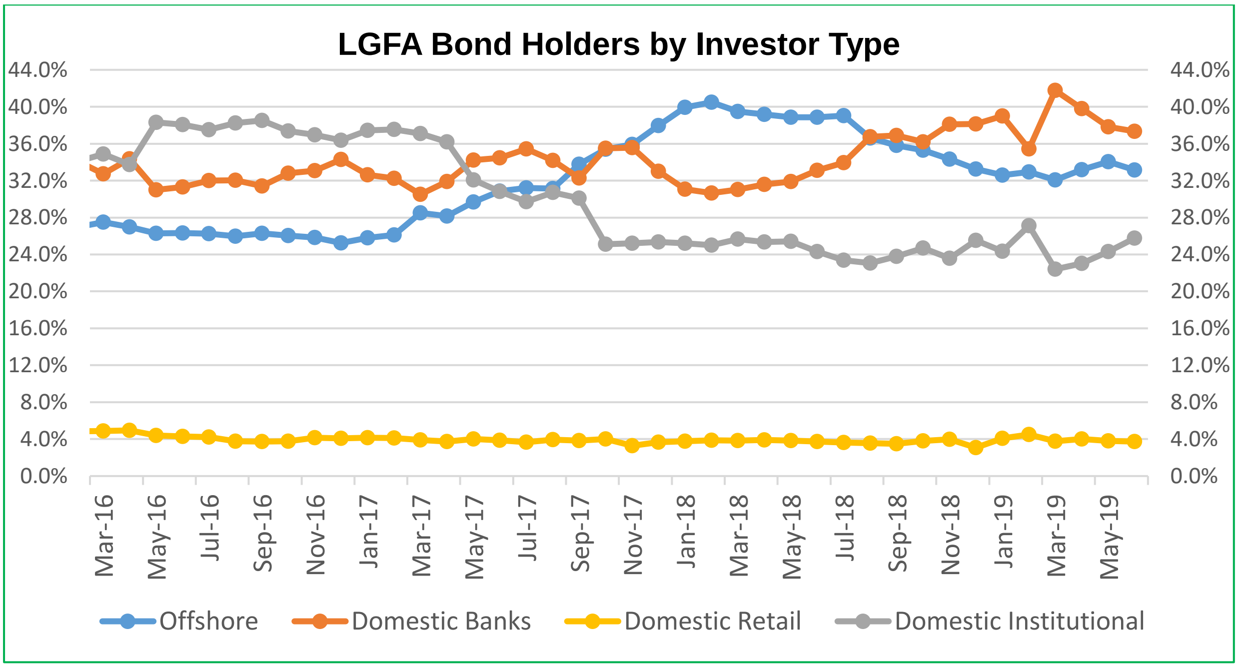
As at the end of the fourth quarter, Net Interest Income was estimated by management on an unaudited basis to be $151k above budget while expenses are $175k below budget. Net Operating Gain of $11.201 million was $326k above budget but $601k (5.1%) below the Net Operating Gain for the equivalent prior period.

## G. Investor relations / outlook

Managing relations with our investor base is very important as the amount of LGFA bonds on issue has yet to peak and we require investors and banks to support our tender issuance. Our focus is on growing and diversifying the offshore investor group as these investors have the most growth potential given that we already receive strong support from the domestic banks and institutional investors.

Offshore and domestic institutional investors increased their holdings over the quarter as LGFA bonds remain attractive on a spread to underlying NZGBs and investors chasing yield in the current low interest rate environment. By our estimates

- Offshore investors increased their holdings of LGFA bonds by $203 million over the quarter (but reduced by $33 million over the past twelve months). NZ bond yields remain unattractive relative to other global markets and there has been a subsequent decline in the holdings of NZ Government Bonds (NZGB), Kauri bonds and LGFA bonds. While low interest rates are a positive for our council borrowers, it is more difficult to encourage offshore investors to buy LGFA bonds. They are estimated to hold $2.97 billion (33.1% of outstandings) compared to $3.0 billion (38.9% of outstandings) a year ago.
- Domestic institutional and retail investors increased their holdings by $390 million over the quarter and were estimated to hold $2.64 billion (29.62% of outstandings) compared to $2.17 billion (28.0% of outstandings) a year ago.
- Domestic banks holdings have reduced by $265 million over the quarter as the other investor groups have bought from the bank trading books. Bank holdings of $3.34 billion (37.3% of outstandings) are just below their record highs in March 2019 and compare favourably to $2.56 billion (33.1% of outstandings) a year ago.



# Quarterly Report

Quarter 4: 2018 - 2019
Period ended: 30 June 2019

## H. Key trends