TIMARU DISTRICT COUNCIL 2021-31 LONG TERM PLAN

FINANCIAL STRATEGY

Our Financial Strategy for the 2021-31 Long Term Plan (LTP) will leverage our strong financial position to meet the challenges we face over the next ten years, to continue to maintain current levels of service; enhance our community facilities; and regenerate the Timaru CBD. This is a step change for our Financial Strategy and will mean an increase in both debt and rates, but in getting the balance right we can achieve our goals of:

- Maintaining long-term financial resilience;
- Providing high-quality infrastructure and facilities;
- Ensuring our services are affordable and meet the wellbeing needs of our community.

Thriving Together

Council's Financial Strategy for the next ten years is to ensure we have the financial ability to:

- Meet the social, cultural, environmental and economic wellbeing needs of our communities, now and into the future;
- Maintain current levels of service across the core infrastructure services of roading and footpaths; drinking water; stormwater; sewage; and waste management;
- Provide for the future economic wellbeing of our District by ensuring long term water supply resilience;
- Undertake an ambitious capital work programme across our community infrastructure to provide high quality, fit-for-purpose community facilities;
- Focus investment on the rejuvenation of Timaru's CBD;
- Ensure Council has the resources to plan effectively for future environmental, legislative, and societal challenges; and
- Deliver all of this in a way that is affordable and fair to current and future communities.

Our Strategy responds to the challenges Council and our District is facing including:

- Ageing infrastructure, requiring a large capital renewal programme;
- Increasing operating costs for our activities across the board;
- Increasing regulatory requirements and community expectations;
- The need to maintain infrastructure and services that are resilient to natural disasters and the impacts of climate change[1];
- Uncertainty around the Government's Three Waters Reform Programme;[2] and
- A reduced dividend from Council's shares (held by TDHL) in Alpine Energy.

[1] For further details on how Council plans to address the impacts of climate change on Council's assets are detailed in our Infrastructure Strategy.

[2] For more detail on how the Three Waters Reform will impact Council, see our Significant Forecasting Assumptions.

This Strategy aligns with our Infrastructure Strategy and is supported by our Significant Forecasting Assumptions and our Activity Statements. These documents provide further information on Council's plans to deliver on these outcomes, and meet these challenges. However, we acknowledge that in some area, such a climate change and the Three Waters Reform, the full extent of the impact on Council is unclear.

A step-change

For the past two LTPs Council has taken a conservative, business as usual approach to the Financial Strategy. This approach has placed Council in a strong financial position with relatively low debt. But we also recognise that we have not rated to the full extent planned for in these previous LTPs. In 2020/21, for example, Council decided to reduce the total amount of rates collected by $2.99M, recognising the impact of COVID-19 on our community.

This is where the step change comes in…

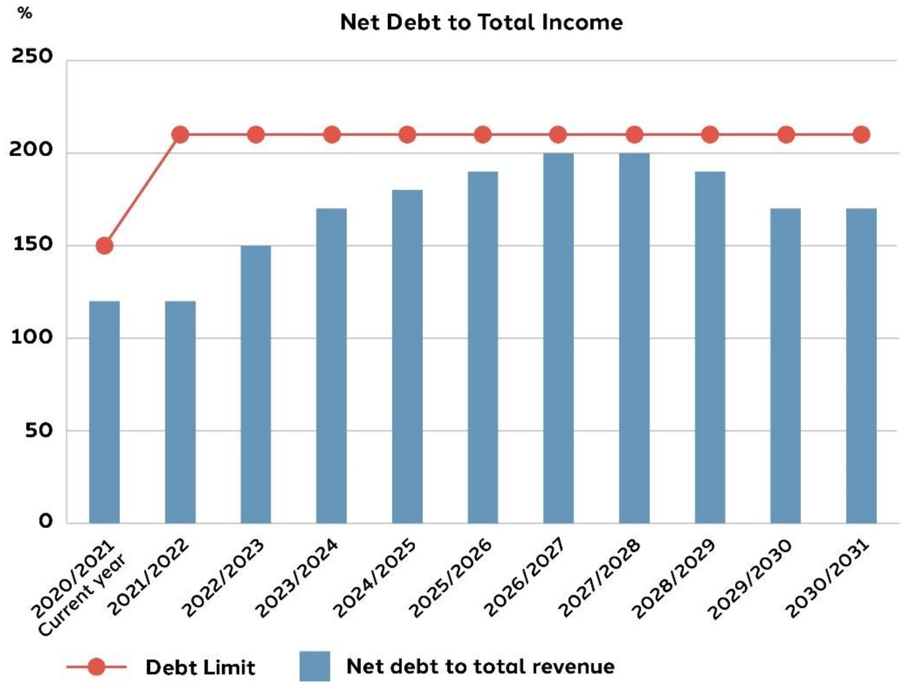
We recognise that to continue to meet levels of service we have agreed with our community, and to improve our community infrastructure (specifically the Theatre Royal and Heritage Hub, Aigantighe Art Gallery and Aorangi Park) and meet other additional demands, we need to increase our debt, and increase our rates revenue. This Strategy ensures that we will balance this step change with financial prudence, and ensure fairness between current and future ratepayers. Recognising the risks of delivery of large number of complex projects, Council is making an assumption that it will fund and deliver 90% of its planned capital work over the life of the plan.

Debt

Our large capital works programme means that our debt will increase from $120M to $279M across the life of the plan. As a result, we have to lift our debt limit. This is a change from our previous financial strategies where our debt limit was set at 150% of revenue, but Council believes lifting the debt limit is essential to the delivery of our plan and to meet our community wellbeing outcomes. Using our debt wisely also ensures that future users of new and upgraded assets will contribute appropriately.

While we have a maximum debt level of 280% of operating revenue, our Strategy sets a limit of normal operating debt at, or below, 210%. These debt limits are supported by Council's strong credit rating.

By limiting our debt in this way we are ensuring that there is still capacity to borrow in an unforeseen event (e.g. a significant natural disaster). We also know from our 30-year Infrastructure Strategy that beyond this LTP there is still significant investment required in aging infrastructure, and upgrades and replacements to community facilities (e.g CBay and the Timaru Library). This debt limit will allow headroom for the future interests of the Timaru District and give future Councils the ability to make decisions about what is important to their community.



The financial balancing act

We need to ensure that operational costs - from paying the power bill, to paying our staff - are covered by operational revenue, such as rates, fees and charges. This is called a 'Balanced Budget'. If we can't achieve this, we have to borrow to cover these costs. This means that current ratepayers are not paying the full share, and future ratepayers will have to meet those costs, and the interest. We don't believe this is fair, prudent, or sustainable.

These everyday operating costs are increasing due to a range of factors including:

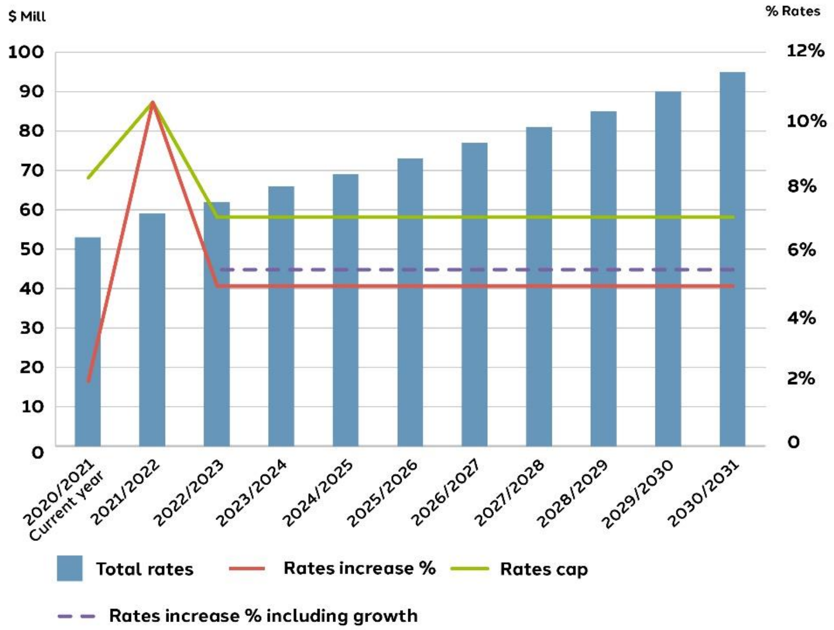
- Increasing staff costs to meet the evolving demands of local government;
- Increasing the amount we fund to replace our infrastructure assets, like roads and water networks (also referred to as funding depreciation); and
- Increased operating expenses due to inflation, the cost of carbon credits, and higher compliance standards in areas like water and sewer.

Throughout the life of this plan, Council will continue to look for ways to control expenditure and ensure efficiency across all our services.

Rates

Council has set a rate increase limit of 10.5% in 2021/22 and 7% in the following years.[3] While we don't plan to reach this limit, and are forecasting that the increase will remain at 4.9% from 2022/23 onwards, it does allow some flexibility if inflation-related costs change across the life of the plan. The graph below shows the total rate increases and the rate increase limit across the ten years.

[3] Our previous Financial Strategy set a rates increase limit of a 6% increase per annum plus CPI.



The average rates increase for 2021/22 is higher than in previous years, and also in the later years of the plan, and this reflects the step-change in our Financial Strategy and Long Term Plan. We recognise that we need to fully fund our operating costs if Council is to continue to deliver our services to a high standard, to maintain and renew our existing core infrastructure, and to invest in our community facilities.

These rates increases also form part of the balancing act. If we were to collect less rates it would reduce how much we can borrow, remembering how much we can borrow is a ratio of how much revenue we collect. This would mean that some of the projects we have planned would need to be deferred, redesigned or not completed.

Growth and Land Use Changes

Population and household growth in the Timaru District is relatively steady. We are projecting a 0.7% annual population growth and an increase of 2,267 households over the next ten years. We have factored the rates contribution of this growth into our forecast rates increases.

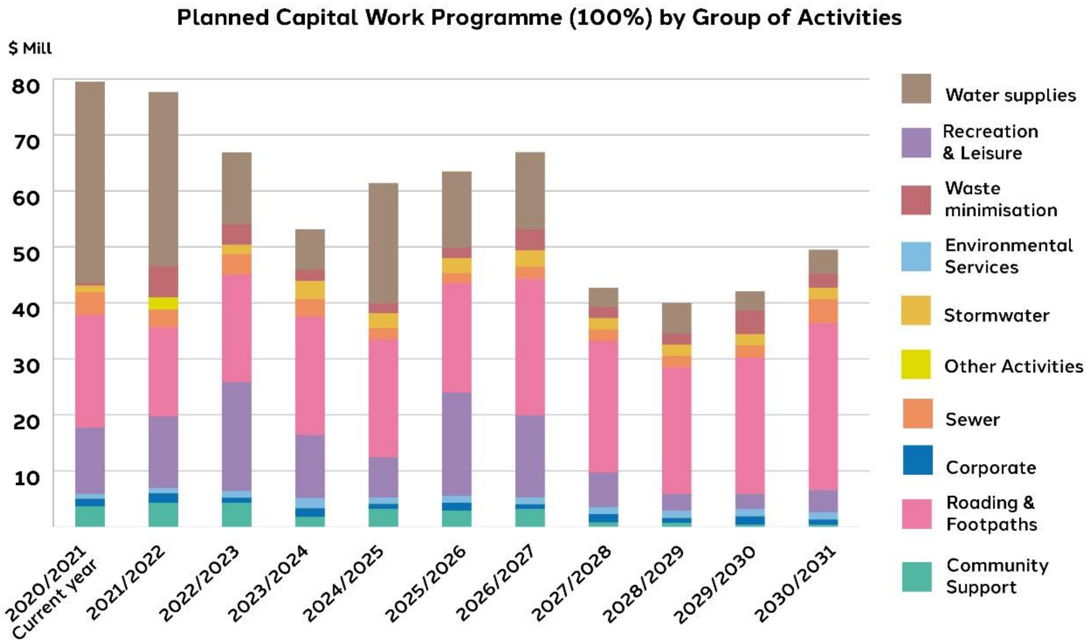
While Council is not assuming significant land-use change over the next ten years, past and future land use change has, and will continue to impact on Council's delivery of services particularly for road maintenance in rural areas and the provision of services for new development on urban fringes.

Capital Spending

Council has planned a capital works programme of $566 million over the next ten years. All project costs shown within this document are the full estimated projects cost, including inflation.

This is a significant increase on prior LTPs. The majority of this investment is in core infrastructure renewals and upgrades, like water and sewer pipes, roads and footpaths, and our landfill, and will ensure Council can continue to maintain and improve our levels of service, based on its Activity Management Plans

Council also recognises how important our community facilities, like the Aigantighe Art Gallery, the Theatre Royal and South Canterbury Museum, and Aorangi Stadium, are to supporting community wellbeing. This Strategy enables Council to fund the upgrades and development of these facilities over the next ten years, and enhance the lifestyles of our communities. The graph below shows how our Planned capital expenditure (100%) across our groups of activities.

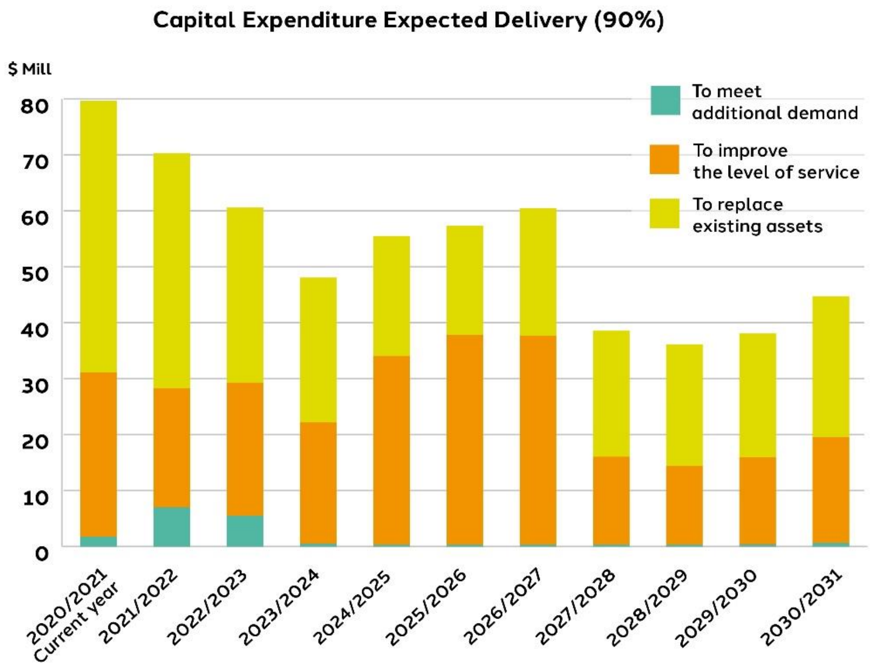


90% Delivery Assumption

The planned capital work programme is an ambitious work programme. A critical element to help deliver this programme is the change in our delivery model. The 'head start' project initiative is a change from the 'do it all in one year' as has been past practice. For example, we are awarding construction work contracts over multiple years and designing projects and awarding construction work contracts in the previous financial year for immediate start in the year allocated.

Despite this we recognise that risks outside of Council's control can impact on our ability to deliver some projects, regardless of the size of our capital work programme. For example, this includes the availability of contractors, disruption to supply chains, legislative change, resource consent delays and further project investigations that expose unknown issues. To reflect those external risks, it is assumed that Council will deliver and fund 90% of its planned capital works programme in any 12-month period and over the 10 year plan period (see Page 22). Council believes it is not fair to rate for more than it reasonably expects to deliver. Projects planned but not delivered in any one year are deferred to future years or re-prioritised (e.g. where an asset like a bridge is going to last longer or new technology provides a better solution), potentially beyond this LTP period.

The graph below shows how much we expect to spend on replacing assets, improving levels of service, and meeting additional demand, based on the 90% delivery assumption. As demonstrated in our Activity Management Plans, our assets are being enhanced over the 10-year period, which enables the levels of service to be maintained at 90% expected delivery.



Security of borrowing

Council provides security on its borrowing. This provides our lenders with a charge over the Council's rates income and means that, if we defaulted on a loan, the lender would have the ability to set a rate and recover the sums owed. In practice, it is the ability of local authorities to set rates that makes it very unlikely that a local authority would default on its obligations.

Council has obtained a credit rating from Fitch Ratings. This is currently AA- with a stable outlook. It is expected that this will be maintained as a minimum during the 10-year period.

Other revenue

Council has a number of other sources of revenue aside from rates, including fees and charges, and funding assistance from Waka Kotahi (New Zealand Transport Agency), and interest and dividend from investments. Our Revenue and Financing Policy details how these revenue streams contribute to all the services we provide. Our Financial Strategy is based on an assumption that these revenue streams will remain consistent. [4]

Investments

Our primary investments are in equity, property, and cash. We intend to maintain the value of these investments in the long term.

[4] See our Significant Forecasting Assumptions for more detail on our projected revenue from Waka Kotahi funding assistance.

Equity Investments

We have shareholdings in a number of entities primarily to achieve efficiency, to help meet our community wellbeing outcomes, and for a financial return on our investment.

The largest equity investment held by Council is its investment in Timaru District Holdings Limited (TDHL) which in turn holds the Council's interests in Alpine Energy Limited and PrimePort Timaru Limited as well as a property portfolio.

We also have a shareholding in Civic Financial Services which is a local authority collective providing insurance and Kiwisaver services to its members.

Our target for returns on these investments is a dividend of $1 million per annum from TDHL.

Property Investments

Council also owns a number of properties that we don't use for Council business. Our objective is to only own property that is required to be held or necessary to achieve our strategic objectives and meet operational requirements. We will be reviewing our property portfolio in the first three years of the LTP.

Cash Investments

Investments of cash are held for specific purposes (special funds) are usually held as short-term deposits or in bonds.

The Council maintains cash investments for the following primary reasons:

- To provide liquidity in the form of readily available cash in the event of a natural disaster. This cash is intended to bridge the gap between the disaster and the reinstatement of normal income streams;
- To invest amounts allocated to special funds, bequests, and reserves;
- To invest funds allocated for approved future expenditure, to implement strategic initiatives or to support intergenerational allocations;
- To invest proceeds from the sale of assets; and
- To invest surplus cash, and working capital funds.

Our target for return on these investments is between 1.1% and 1.5%.

Other Investments

Council also holds 235 hectares of forestry woodlots which is held as a long-term investment to support cashflow, and to help maintain the Council land where the woodlots are situated.

We assume no return on our forestry investments.