Date:	**Tuesday, 6 August 2024**
Time:	**12:30 pm**
Location:	**Council Chamber, Wairoa District Council, Coronation Square, Wairoa**

AGENDA

Late Reports

Finance, Assurance & Risk Committee Meeting

6 August 2024

MEMBERSHIP: His Worship the Mayor Craig Little, Cr Jeremy Harker, Cr Denise Eaglesome-Karekare, Mr Philip Jones, Cr Benita Cairns, Cr Melissa Kaimoana

The agenda and associated papers are also available on our website: www.wairoadc.govt.nz

For further information please contact us 06 838 7309 or by email info@wairoadc.govt.nz

Order Of Business

8 GENERAL ITEMS

8.1 LONG-TERM PLAN 2024-27 DRAFT FINANCIAL STRATEGY

Author: **Gary Borg, Pouwhakarae - Putea Tautawhi Rangapu | Group Manager Finance and Corporate Support**

Authoriser: **Kitea Tipuna, Tumu Whakarae Chief Executive**

Appendices:
1. **Draft Financial Strategy ⇩**
2. **Prospective Prudence Benchmarks ⇩**

1. PURPOSE

1.1 This report provides information for Committee on the Draft Financial Strategy 2024-27. No decisions are required by Committee at this stage.

1.2 Presentation of this information supports the Committee in fulfilling its Terms of Reference

RECOMMENDATION

The Pouwhakarae - Putea Tautawhi Rangapu | Group Manager Finance and Corporate Support RECOMMENDS that Committee receive the report and endorses the Financial Strategy for inclusion in the Long-term Plan 2024-27.

2. BACKGROUND

2.1 Council is in the final throes of preparing its Long-term Plan (LTP) 2024-27 under Severe Weather Emergency Legislation Act – Order in Council provisions.

2.2 The Financial Strategy, attached as **Appendix 1**, is integral to the LTP, setting a framework for how Council will raise revenue and meet its financial obligations in delivering Levels of Service whilst, in this instance, undertaking Emergency Recovery activities.

2.3 Council completed its LTP consultation from mid-June 2024 and received submissions on 1 August 2024.

2.4 The final and complete LTP will be presented to Council for adoption on 8 August 2024.

2.5 In addition, and to aid interpretation, the prospective financial prudence graphs, prepared in accordance with the Local Government (Financial Reporting and Prudence) Regulations 2014 are attached as **Appendix 2**.

INTRODUCTION

This Financial Strategy sets out how Council intends to fund its activities and projects, to deliver sustainable service levels and achieve the community objectives contained in its Long- term Plan (LTP) 2024-27 and the corresponding three years of its infrastructure strategy.

The Wairoa district has experienced two major natural emergency events in the past 18 months. Cyclone Gabrielle, February 2023, was the most severe weather event in 40 years and caused considerable damage to our roading and 3 water networks. In June 2024, another weather event caused a significant event with flooding experienced in a different part of the township than was flooded during Cyclone Gabrielle.

The recovery from these events will take a number of years and its effects have been considered as part of this strategy.

This strategy will guide Council on the use of appropriate funding tools to pay for this expenditure, so that it can continue to deliver effective and affordable services to the community now and into the future.

It examines the key drivers that will affect Council's funding and expenditure, the risks associated with the assumptions it has made, and the use of available tools to deliver its outcomes and allow for changing circumstances.

Council continues to face significant challenges to deliver desired levels of service within an affordable funding envelope. We will continue to strive to deliver effective services at an affordable cost. Despite this we also need a reset, to respond to events of the past 3 years and reposition the Council to a sustainable financial footing.

Council has historically had been able to keep rates increases below 5%. It achieved this primarily by not rating for depreciation, selling surplus assets, and deferring expenditure. These measures are not sustainable and since 2021, from the effects of Covid19 through to the recent weather events on our costs means these levers are not even available in the short-term. Council acknowledges minimal rates increase are desirable, but this is not achievable unless levels of service are reduced.

Over the next 3 years, Council forecasts that a total of over $135 million in operating costs and $141 million in capital expenditure. Natural emergency event recovery will make up $3 million of operating costs and $20 million of capital expenditure.

We project rates increases averaging 10% over the next three years while we project debt to increase by an average of $10 million per year. This is within our available debt covenants, but we are conscious that it adds to the affordability challenges for future generations.

BACKGROUND

What hasn't changed….

Wairoa's low population density and the large remote expanse of land over which Council delivers infrastructure and services present continuing affordability challenges. Our remoteness and landscape, whilst presenting wonderful lifestyle benefits, adds to this.

The costs of meeting increasing compliance requirements and the community's desired levels of service in all areas will continue to rise.

Council is heavily dependent on Waka Kotahi subsidies to maintain its roading network and, at 75%, receives the highest funding assistance rate in the country.

Due to significant increase in contract prices, we have become more reliant on borrowing to undertake essential upgrades to infrastructure and facilities. The weather events experienced by the region mean this trend is forecast to continue over the three years of the LTP.

What has changed……

Post COVID-19, Wairoa and the Hawke's Bay Region has proved its resilience with a strong primary economy, we are mindful of the lingering effects the pandemic has had on the global, national, and local economies.
We are also aware of the region's reliance on sheep and beef farming.

OUR FINANCIAL OBJECTIVES

Our mission in this strategy is financial sustainability, our financial objectives are:

Objective	Simple	Affordable	Appropriate
Certainty of Rates Increases		✓▪	✓▪
Optimise External Revenue	✓▪	✓▪	✓▪
Value for Money		✓▪	✓▪
Intergenerational Equity	✓▪	✓▪	✓▪
Debt Remains Manageable	✓▪	✓▪	✓▪

These objectives are the pillars upon which we will seek to build a financial framework to enable us to deliver effective services and infrastructure now and into the future, as economically as possible. We may not achieve them all at the same time and sometimes they will conflict. There will need to be a balance. It is a long road with many turns ahead.

Council has adopted a range of benchmarks to assess how we are progressing. These are illustrated throughout this strategy.

ASSUMPTIONS - WHAT WE ARE PLANNING FOR

This section discusses the key factors that will affect Council's ability to achieve its objectives in this strategy. For each area, a table is presented showing Council's assessment of the risks that the area presents to achieving these objectives and the degree to which opportunities may be developed to contribute to favourable outcomes. More detail is provided in the Overall Assessment.

The key factors that will influence Council's ability to achieve its financial objectives are:

i. Population
ii. Economic factors (local growth rate, cost of borrowing, inflation)
iii. Land Use
iv. Maintaining Levels of Service – Ageing Infrastructure

POPULATION

At the 2023 census Wairoa had a population of 8826 residents, 69% of whom identified as being of Māori descent.

The graph below base based on 2018 census data projects the population to increase to 9200 by 2033. The 2023 starting point of 9040 residents has not eventuated but the graph is helpful to understand the potential growth the district is forecast to experience. The data indicates overall growth in the district will be minimal with the current infrastructure, facilities, housing stock being sufficient to meet the district's needs.

It is hoped that potential population growth will stimulate economic growth that will improve household incomes and make Council activities, as part of the general cost of living, more affordable.

Therefore, the main challenge that Wairoa's population presents to achieving these financial objectives remains spreading the cost over a small base.

Wairoa's population is expected to remain approximately 2/3 Māori. This presents no implications for Council's financial strategy, but alongside its new Revenue and Financing Policy Council has adopted updated Rates Remission and Postponement policies, with particular attention to the prospective growth of Papakāinga and the progression of the Local Government (Rating of Whenua Māori) Amendment Bill.

The table below summarises Council's assessment of the Risks and Opportunities that Population factors represent for the Financial Strategy.

	Population	
	Risk	**Opportunity**
Certainty of Rates Increases	**High** – small population and large geographical spread provides a small funding base for escalating costs	**Low** – growth would need to be high percentages to make a significant difference to spreading the load
Optimise External Revenue	**Low** – our diversity is a strength and does attract external funding	**High** – our community was an important factor in the amount of PGF funding we were able to attract
Value for Money	**High** – cost increases always likely to exceed rate of population growth	**Medium** – cost of service discussion with an engaged community improves transparency
Intergenerational Equity	**Low** – shared objectives with regards to future generations	**High** – involving the community in future planning helps preserve sustainable services
Debt Remains Manageable	**Medium** – must maintain borrowing within prudent limits so that debt servicing does not become a large part of day-to-day expense	**Low** – limited scope for targeted rates for specific projects

These objectives are not a means to themselves, they are the pillars upon which we will seek to build a financial framework to enable us to economically deliver effective services and infrastructure now and into the future. We may not achieve them all at the same time and sometimes they will conflict. There will need to be a balance. It is a long road with many turns ahead.

Council has adopted a range of benchmarks to assess how we are progressing. These are illustrated throughout this strategy.

ECONOMIC FACTORS

The Local Economy

Wairoa has a strong primary industry and Local GDP, and employment are trending modestly upwards, but below regional and national averages.

There are a concentration of employment remains focused around the Wairoa township, with the district's largest single employer accounting for the equivalent of approximately 12% of the town's population and making a significant contribution to export GDP. The three largest employers combined make up roughly 16%.

The rural economy has traditionally been dominated by pastoral farming, which also makes a substantial contribution to export GDP, but there is a concern that substitution into forestry will dilute this, and the wealth retained in the district.

We envisage longer-term opportunities for the district relating to tourism and hospitality, with regular launches by Rocket Lab in Māhia becoming a draw. If the district can maintain its robust core industries this will be a valuable addition for growth and diversification.

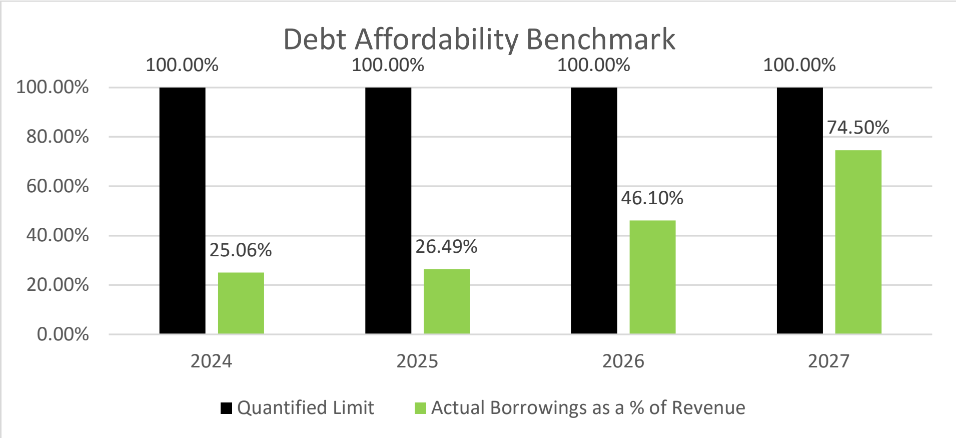
In June 2024 the average house price was $379,893. Comparable to the national average of $916,285, Wairoa continues to be an inexpensive place to buy property, but supply is severely limited and the district's remoteness and small population mean it is not necessarily cheap to live and play. The post Covid property boom has seen property prices remain static or fall across the country with Wairoa also experiencing this with the average price in July 2021 being $424,973. This along with the cost-of-living crisis means residents are more likely spend less and focus on core essentials putting pressure on businesses to stay open.

Macronomics

Challenge 1 – Ability to Borrow

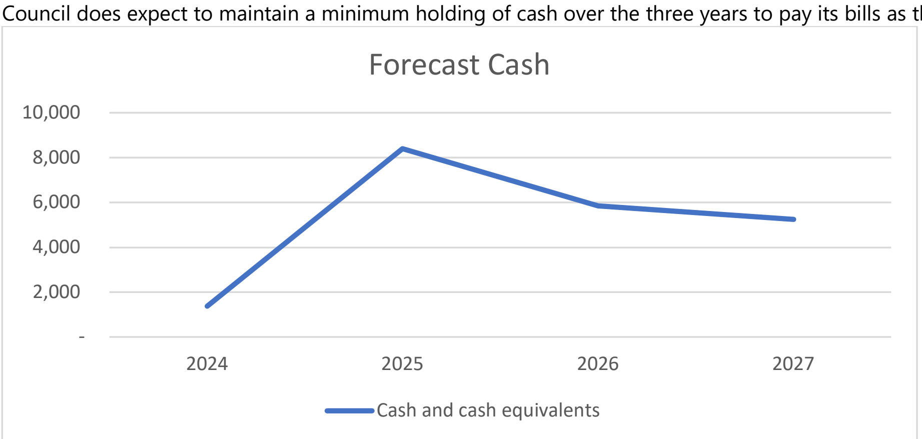
To meet it's the costs of disaster recovery and its capital works programme Council will need to borrow, on average, $10 million extra over the three years of the LTP. On 1 July 2024 Council's total external borrowing was $10.938 million and is forecast to have debt of $41.4 million by 30 June 2027.

Council has a self-imposed debt limit of 100% of total revenue. The graph below illustrates that council forecasts to peak at 74.5% of total revenue which is within its limit. Over the LTP council forecasts to have headroom to borrow more in the case of unexpected events such as natural disasters.



As a member of the Local Government Funding Agency (LGFA) Council can borrow up to 175% of its revenue. Council considers this to be high risk and views 100% of revenue as an important affordability threshold for its community. This is reflected in our Liability Management Policy. Council is not a guarantor to LGFA but with forecast debt levels exceeding $20 million, it will need to review the benefits and costs of becoming a guarantor to secure cheaper debt.

Council does expect to maintain a minimum holding of cash over the three years to pay its bills as they fall due.



Our Response
Borrowing is an appropriate funding tool for long-term assets. Council will use borrowing prudently to fund the infrastructure that delivers core services now and into the future, without creating an unmanageable affordability challenge. Council has been forced to borrow to cover the costs of replacing assets affected by Cyclone Gabrielle and the June floods. Due to the uncertainty associated with the Recovery programme Council's will need to hold cash levels sufficient to meet its commitments which may vary considerably. To make good use of these cash holding we will place funds in short-term deposits and investments until it is needed to pay the bills.

To fund improvements in infrastructure sustainably and maintain levels of service, Council will borrow up to the levels that it considers prudent - 100% of revenue. It will rate for the repayment of this debt over the life of the corresponding assets, in lieu of rating for depreciation. This will ensure that each year the community that benefits from this infrastructure pays its share.

Challenge 2 – Cost of Borrowing
The other half of the borrowing equation is the cost of borrowing. Interest rates have been low for many years and Council has made use of this to borrow for essential capital works at competitive rates. Post Covid has seen an increase in the OCR rate, but current Reserve Bank projections indicate these will fall from their current peak in late 2024, early 2025. There is always a risk that rates will increase in the future, but council tries to mitigate this through its liability management policy. We are in the same waka as every other council, with a large works programme to catch up on and limited reserves available to pay for them.

As previously stated, Council's membership with the LGFA enables us to borrow at competitive rates. Our financial forecasts assume these rates will be available throughout this strategy. However, we also recognise the risk that economic pressures will cause interest rates to rise in the future.

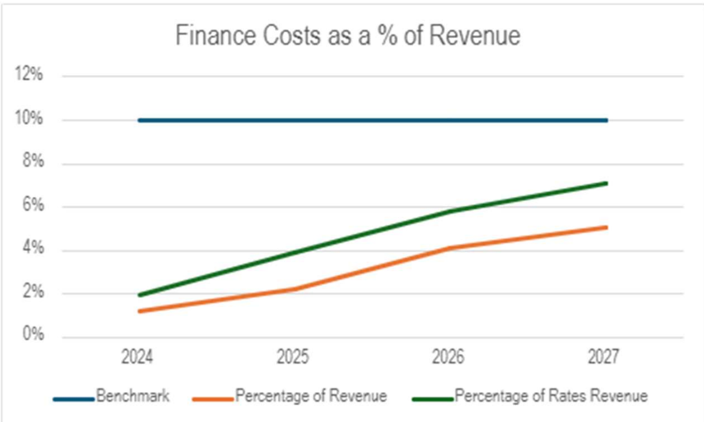
Council has a statutory limit of Finance Costs being less than 10% of Revenue which it forecasts to stay within over the life of the LTP.

Council has considered a tighter assessment, considering the following:

- The ability to service debt also includes the ability to meet repayments.
- Total revenue includes subsidies, primarily from Waka Kotahi

Which are specifically intended for maintaining and improving our roads. This revenue is not to be used to cover interest and debt repayments.

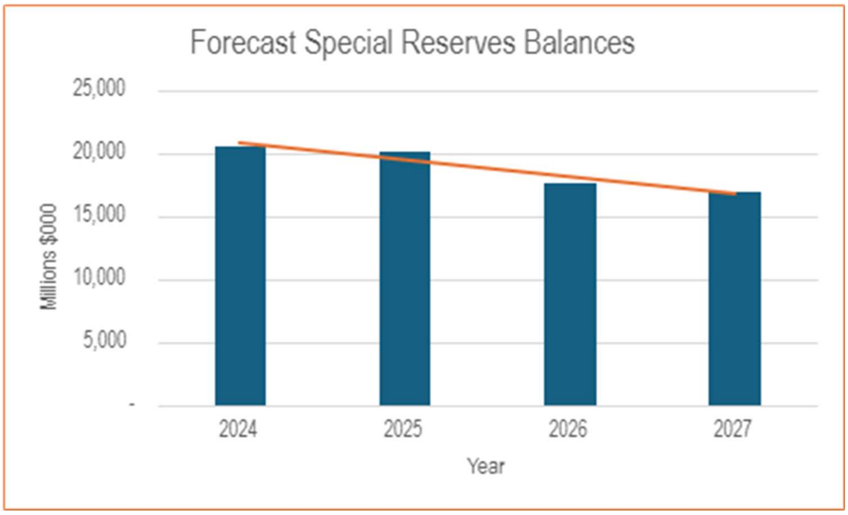
Council has modelled its own debt servicing measure to ensure that the scale of borrowing will continue to be affordable. In the graph below, Forecast Debt Servicing includes interest expenses, and the amount required to be rated for loan repayments and is expressed as a percentage of revenue excluding subsidies. This is the annual cost that the community will bear. Council will maintain a limit of 10%, but it will be based on this adjusted revenue figure. This shows that debt remains affordable throughout the plan.



Challenge 3 – Inflation
In our financial forecasts we have applied the nationally recognised inflation rates provided by Business and Economic Research Ltd (BERL). The table below shows the estimated inflation rates that we have used as inflators for this LTP, and Council's Infrastructure Strategy

BERL (Business and Economic Research Ltd) Local Government Cost Adjusters					
Cumulative change (since 2023)					
Year	Planning & Regulation	Roading	Transport	Community	Water & environment
2024	3.4%	3.8%	3.4%	3.5%	5.0%
2025	2.6%	2.9%	2.6%	2.7%	3.6%
2026	2.1%	2.0%	2.1%	2.0%	2.5%
2027	2.2%	2.3%	2.2%	2.2%	2.7%
2028	2.1%	2.3%	2.2%	2.2%	2.6%
2029	2.0%	2.2%	2.1%	2.1%	2.5%
2030	1.9%	2.1%	2.0%	2.0%	2.3%
2031	1.9%	2.0%	2.0%	1.9%	2.3%
2032	1.9%	2.0%	1.9%	1.9%	2.2%
2033	1.9%	2.0%	1.9%	1.9%	2.1%
2034	1.9%	1.9%	1.9%	1.8%	2.1%
20 Year Average	2.4%	2.6%	2.4%	2.4%	3.1%

Council will use its reserves to fund some of the costs but over the three years the balances are forecast to reduce. In general, these have built up over time by council putting away funds over time accumulating to the point when they are needed. The level of renewals required over the three years of the LTP will result in lower balances held.



For the year ended 30 June 2025 we have applied known contract rates. Prices rarely decrease and in the public sector they often go up more than normal. This has been experienced In Wairoa we have the added challenge of remoteness and size, making the local market less competitive due to the small number of suppliers. Noting that these are averages applied across the entire country, the Wairoa experience may be quite different.

Council rates for approximately 60% of its operating costs, which means a 1% variation in inflation would increase rates by 0.6%. However, this assumes that nothing else will change. In the LTP 2021-31 we applied the corresponding inflation rates in our forecasts. Since the sector has seen large increases in the costs of building and maintaining network infrastructure. As well as the factors peculiar to Wairoa, increasing requirements for safety and regulatory compliance continue to affect the cost of provision. Furthermore, the economic stimulus packages have been beneficial to the local and national economy, but there is a real prospect of the demand from this causing upward price pressure in the market, placing Wairoa at a potential disadvantage.

In addition, due to its dependency on subsidies from Waka Kotahi, significant price changes may limit the amount of work that can be completed without additional input from Council.

Our Response
Council's ability to insulate against future price increases is restricted to developing smart collaborative procurement techniques, careful contract management and disciplined budgeting.

Costs are far more likely to increase due to changes in the safety, regulatory and compliance areas for all activities. If these activities become unaffordable Council will need to review its levels of service with the community.

The table below summarises Council's assessment of the Risks and Opportunities that Economic factors represent for the Financial Strategy.

	Economic Factors	
	Risk	**Opportunity**
Certainty of Rates Increases	**Medium** – population size presents an exposure to extreme changes in inflation or interest rates	**Low** – limited investment holdings and modest returns
Optimise External Revenue	**Low** – subsidies set at co-contribution rates, some exposure on what can be delivered	**Medium** – strong relationships with funders have seen Wairoa achieve above average investment
Value for Money	**Medium** – some revenue lines may not increase at the same rate as costs	**Low** – already benefiting from low interest rates
Intergenerational Equity	**Low** – funding plans in place to deliver the same levels of service in the future	**High** – economic recovery stimulus packages have delivered improvements to long-term infrastructure and facilities
Debt Remains Manageable	**Low** – debt used as part of a balanced funding approach and repayments included in funding plans	**Medium** – capacity built in to take advantage of refinancing options

LAND USE

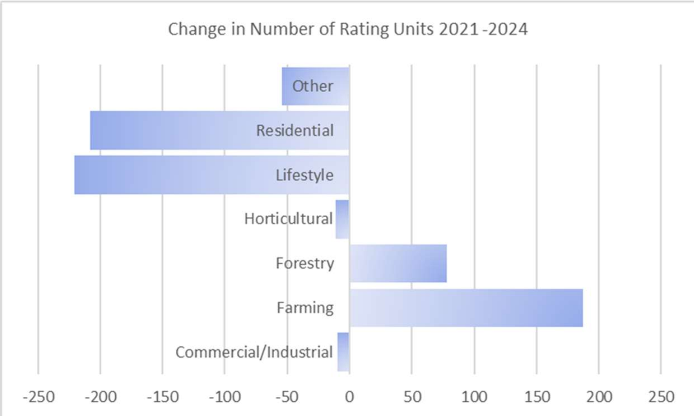
Council's Infrastructure Strategy refers to:

- Anticipated transfer of land use from farming to forestry and horticulture.
- Expected increase in Rocket Lab operations and tourism possibilities.
- Increase in residential building in Māhia and Wairoa.

The first two items will specifically affect the consumption and cost of maintaining and improving the roading network.

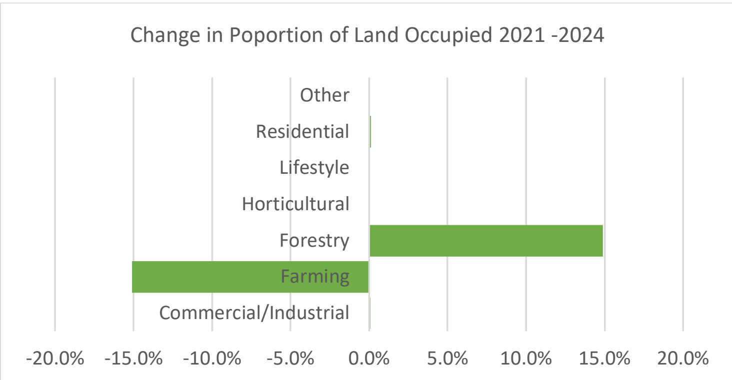
With regards to residential growth, improvements to the stormwater network are specifically anticipated, particularly in Māhia.

The graphs below illustrate what changes have occurred with regards to land use since the 2021 LTP:



The total number of rating units has reduced by 239 since 2021. This is mostly because of the amalgamation of rural titles, with lifestyle and residential units associated with farms being reclassified or combined into single titles.
There is some modest development of housing stock, but this is way below the demand for affordable housing, especially after the impacts of the weather events.

Conversely the number of rating units whose main use is forestry has virtually doubled as farm conversions continue to be an attractive proposition. In 2021 for every hectare of land planted in forestry there were 2.4 ha of land used for farming. Today that ratio is 1.2.



Our Response

Due to financial constraints and the total amount of approved funding we are likely to receive from Waka Kotahi, there is limited capacity to augment the land transport management programme. It is more likely that work will need to be prioritised to meet this change in demand unless funding becomes available.

In the future Council will need to maintain these assets to a higher standard so that they remain serviceable to the users.

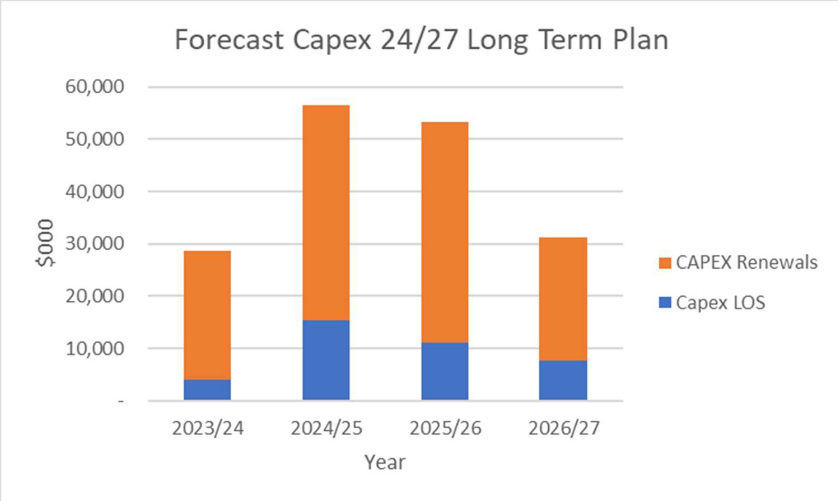
Our main lever is therefore seeking to ensure an appropriate distribution of funding needs, primarily through rates. In 2021 Council completed its rating review and adopted an updated methodology. Specific features that addressed the impact of land use changes included:

- Transitioning to a general rate assessed on capital value, partly on the basis that development drives the cost of infrastructure;
- Incorporating the forestry roading differential into the streamlined capital value rating system and applying a differential factor of four overall to reflect the relative impact on community wellbeing outcomes;
- Moving 10% of the rates for all water activities to the general rate, recognising the community benefit from healthy water systems.

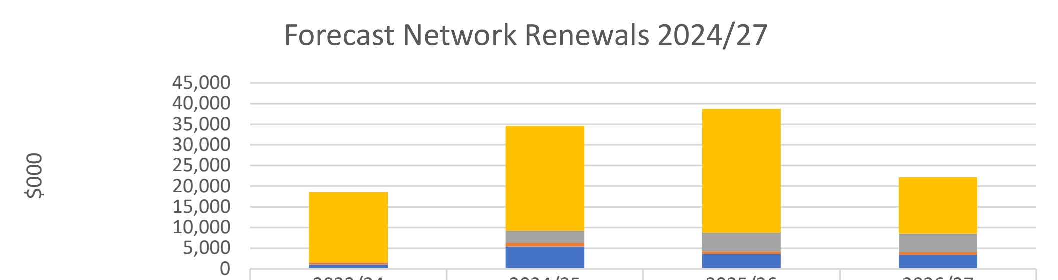
The table below summarises Council's assessment of the Risks and Opportunities that Land Use changes represent for the Financial Strategy.

	Land Use	
	Risk	**Opportunity**
Certainty of Rates Increases	**Medium** – significant changes may affect demand and cost effectiveness of services	**Medium** –new rating policy enables Council to respond with greater agility and consistency
Optimise External Revenue	**Low** – observed trends in land use are more likely to justify continuation of high subsidy rates	**Medium** – link to economic development, options to explore financial contributions may arise
Value for Money	**Medium** – changes in land use may affect demand for Council activities which are planned over the long- term	**Medium** – new development may create sufficient demand to increase fees and charges
Intergenerational Equity	**Medium** – rapid change may create redundancy or deficiencies in infrastructure	**Medium** – co-design with community partners to support sustainable outcomes
Debt Remains Manageable	**Low** – the only risk would be redundant capacity and a need to finance significant unexpected changes to assets	**Low** – unlikely that co-funding opportunities would supersede existing arrangements

MAINTAINING LEVELS OF SERVICE THROUGH AGEING INFRASTRUCTURE



Council forecasts spending $141 million over the three years of the LTP. $107 million of this relates to maintaining the current asset base with the remainder invested in improving the level of service. $95 million of the renewals relates to maintaining the council's infrastructure network as illustrated below. Transport is responsible for $17 million of the LOS improvement forecast to be undertaken over the three years.

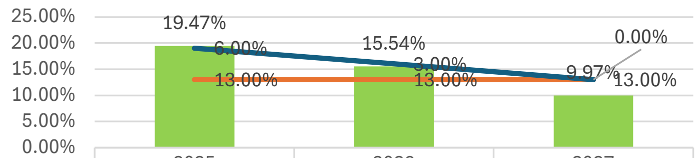


	2023/24	2024/25	2025/26	2026/27
Transport Renewals	16,937	25,403	29,891	13,586
Wastewater Renewals	80	2,910	4,548	4,526
Stormwater Renewals	418	965	588	603
Water Renewals	1,072	5,353	3,645	3,428

LEVELS OF SERVICE - AFFORDABILITY AND BALANCING THE BOOKS

Council funds its infrastructure activities through a mixture of rates, subsidies, grants and other fees and charges, seeks central government funding, and potentially development contributions.
Most funding comes from rates, with land transport heavily subsidised by Waka Kotahi NZ Transport Agency (Waka Kotahi). Council also uses debt and reserves to spread the funding of large costs, especially capital expenditure, over the life of the asset.
Over the period of this Strategy, Council will be exploring alternative funding sources to maintain its current levels of service to the district.
Council has adopted a funding approach that it considers prudent and sustainable. As part of this approach, it takes an activity-by-activity approach to depreciation rating for renewals. Depreciation is rated in ranges from 0% to 100% and council will not rate for depreciation in circumstances where other funding is available.

We have set a rates increases affordability quantified limit of 13% over the life of the plan. With forecast increases of 19.47% and 15.54% we acknowledge breach the limit in years one and two but believe it is prudent to do so. The breach of the limits is attributable to the ongoing costs of recovery being 6% in 2024/25 and 3% in 2025/26. We forecast a rates increase of 9.97% in 2026/27 which is within the limit.



	2025	2026	2027
% Increase	19.47%	15.54%	9.97%
Recovery	6.00%	3.00%	0.00%
Rates Affordability	13.00%	13.00%	13.00%

OTHER POLICY CONDITIONS

BORROWING

Council's primary security for borrowing is its ability to set rates. We do not currently offer assets as security but will consider alternatives if it is prudent to do so. This may require an update to our Liability Management Policy.

INVESTMENTS

Council will not speculate on the securities or other financial markets but will invest where there is clear economic benefit to the district, where the risk is within the parameters of the investment policy and where such investment contributes to the achievement of community outcomes.

Council owns 100% of the equity in Quality Roading and Services (Wairoa) Ltd (QRS). The main purpose of this investment is to maintain and enhance competition for local infrastructure contracts issued by Council. QRS is a significant employer in the district and its presence in Wairoa also ensures resources are available to respond to emergencies. QRS distributes a percentage of its profit to Council. The targets for QRS are set out in the company's Statement of Intent that is agreed with Council annually.

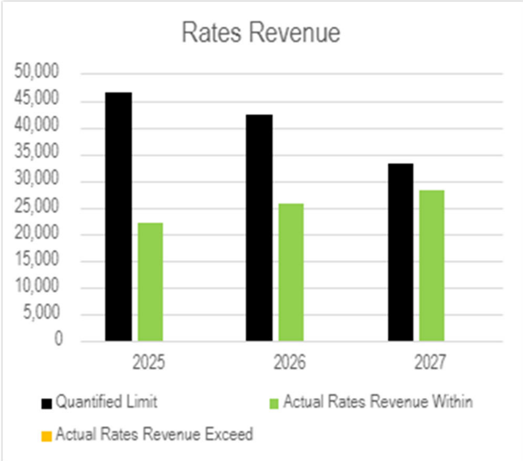
Council's portfolio of bonds and other liquid investments is held to:

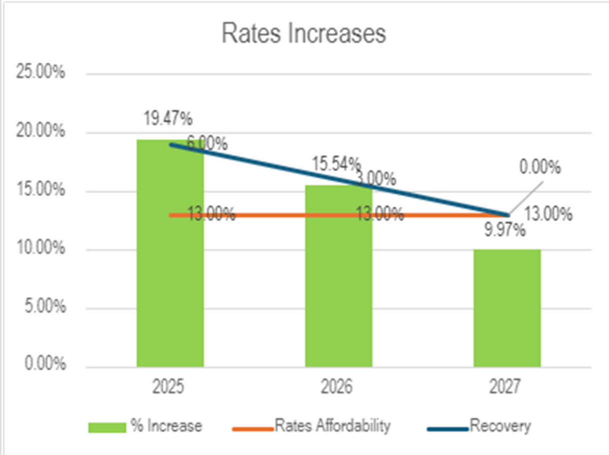
- Provide emergency funds.
- Represent reserves accumulated for asset renewals.
- Earn a return on surpluses, windfalls, and deposits.

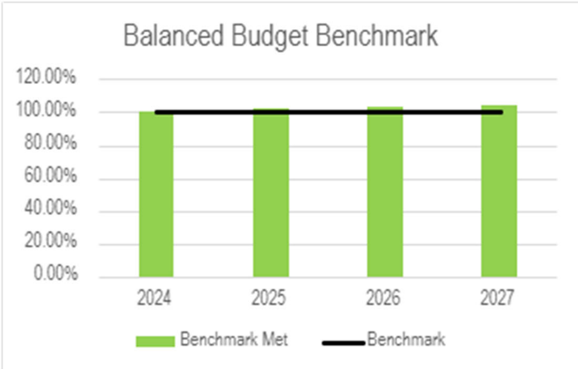
Our current average return on these investments is 4%. We have maintained this in our financial forecasts, although since they will be expended by 2024 this is of limited relevance. As a minimum, we expect a return of 0.75% above our cost of borrowing, which is currently 3.5% As described in economic factors earlier in this strategy, future decisions between repaying loans or increasing investments will be made based on the cost of borrowing versus available returns on bonds.

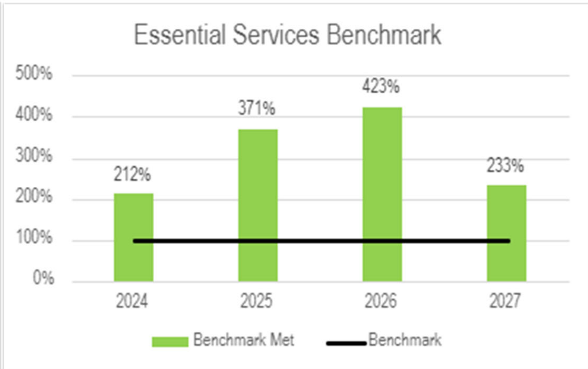
Council owns a minority shareholding in Civic Financial Services Ltd. The sole purpose of this is by virtue of Council's membership of the mutual insurance funds that the company administers. No return is anticipated on this investment.

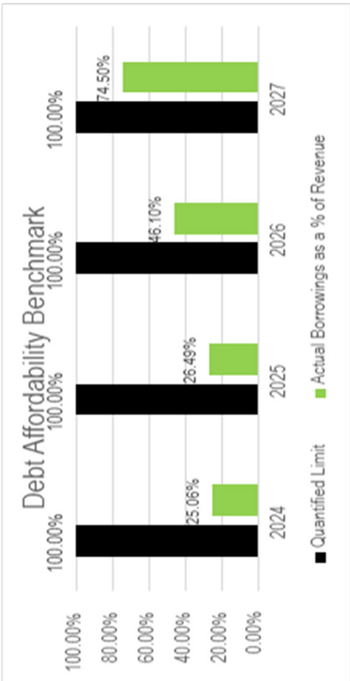
LTP 2024-27 – Draft Prudence Benchmarks

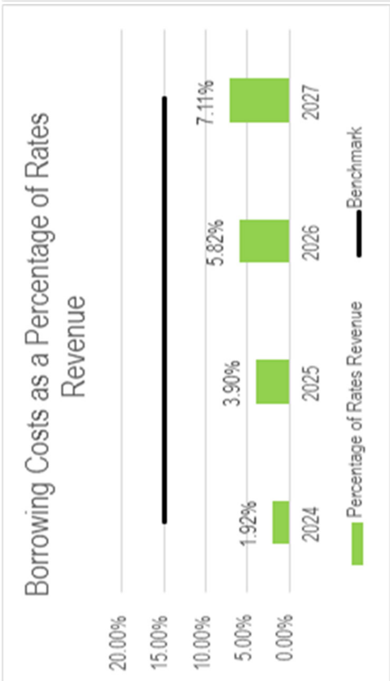


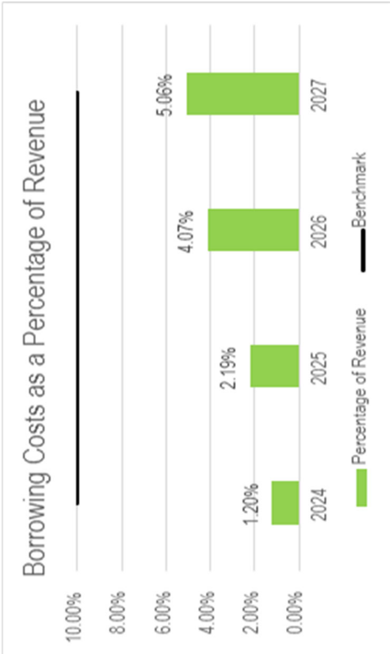







Debt Affordability Benchmark
100.00%
80.00%
60.00%
40.00%
20.00%
0.00%
100.00%
25.06%
100.00%
26.49%
100.00%
46.10%
100.00%
74.50%
2024
2025
2026
2027
Quantified Limit
Actual Borrowings as a % of Revenue


Borrowing Costs as a Percentage of Rates Revenue
20.00%
15.00%
10.00%
5.00%
0.00%
1.92%
3.90%
5.82%
7.11%
2024
2025
2026
2027
Percentage of Rates Revenue
Benchmark


Borrowing Costs as a Percentage of Revenue
10.00%
8.00%
6.00%
4.00%
2.00%
0.00%
1.20%
2.19%
4.07%
5.06%
2024
2025
2026
2027
Percentage of Revenue
Benchmark