Financial strategy – Draft 2024-2034

Council's Long-term plan aims to deliver the following:

- Maintaining existing infrastructure so it is fit for purpose now and into the future
- Providing infrastructure to accommodate a growing district
- Investing in the future of the district to deliver community outcomes
- Being good stewards of our assets
- Balancing delivery with affordability
- Prudent use of debt to support infrastructure and growth
- Maintaining appropriate debt headroom to respond to future opportunities or challenges

The financial strategy is underpinned by the following key elements:

- Maintain affordable rates levels
- Utilise debt to fund key projects that improve the district
- Maintain debt below 250% of revenue

The financial strategy is a cornerstone of the council achieving the goal of living within its means, and ensuring sufficient funding is available for key projects over the coming ten years.

The financial strategy outlines key financial parameters and limits which the council will operate within. It provides insight into Council's current financial health and provides clarity on how this will be managed over the next 10 years.

A short summary is provided below, however, each of the core individual components that make up the complete financial strategy is explained further in more detail.

Summary

Our Long Term Plan is supported by a Financial Strategy intended to enable Council to invest in the future of our district while also balancing delivery with affordability. Recent increases in inflation and interest rates have meant that the cost to deliver Council services has risen significantly, which has meant that Council's revenue requirement has increased in order to meet these funding challenges. Subsequently, there will need to be an approx. 10.24% rates increase in the first year which will fund the community investment throughout the district, retain and attract the best talent for pursuing and delivering our goals, financing our debt and covering depreciation, maintenance and renewal costs; invest in transforming legacy technological systems to ensure a modern and fit for purpose operating platform as well as invest in our core essential services such as Roading, Waste and 3 Waters.

Recognising that Rotorua has a shortage of housing, investment in infrastructure to enable growth and new housing opportunities within Rotorua has increased significantly, with $200m of growth capital expenditure planned over the ten years of the LTP. This is funded through increased development contributions, external funding from Central Government and a degree of investment by Council.

Debt will be increasing from a 2024 forecast year end position of $455million to over $513million in ten years. This increase does not breach any of Councils legislated covenants e.g. 2.80x revenue, and is expected to be below 2x by 2034. The increase in debt will be monitored closely and is considered financially viable not only due to the population growth expected in the district with an increase of close to 3,000 properties but also due to the stabilisation of finance costs as inflation subsides.

We are not investing just on our own, other government agencies e.g MBIE, MFE and private funders attracted by our aspirational vision and goals are willing to partner with us. By partnering with external funders who see the long term benefit that these investments will bring to our community we are able to provide a greater level of delivery and total investment than if simply only applying council funds.

Our financial strategy commits us to be prudent with ratepayer money, while ensuring that the direction of the Long Term Plan supports a better Rotorua for all. Our investment is expected to drive and cater for population growth and subsequent employment opportunities, infrastructure requirements to mitigate climate change effects and maintain a level of borrowing buffer should we need to fund emergencies or decreases in user charges over the short term. Should the consensus be that any detrimental impact is going to be over the longer term then this will necessitate a review of the financial strategy at that time.

Fees and charges

Revenue from fees and charges comes from things such as admission and hiring rates for venues and facilities, liquor licenses, dog registration, building and resource consents and parking management etc.

When budgeting for Council services and establishing how these services should be paid for, Council is required to assess who is driving the need for the service and who is the beneficiary of the service existing. For activities such as parking management, it is clear that drivers parking their vehicles within the city centre are the ones driving the need for the service, which means that we expect parking fees to cover the entire cost of the service being provided. For other services such as our venues and facilities, we recognize that there is a public good element to these services and seek to cover the costs to run these venues and facilities through a mixture of user fees and rates revenue in order to keep admission fees affordable to the community.

User fees and charges budgets are set with these principles in mind and are also subject to an affordability lens to ensure that we are setting fees and charges at a level that does not cause unintended consequences for groups within our community.

This financial strategy recognizes that there is an affordability balance between charging user fees for Council services and levying rates. We have set a target over the course of the Long Term Plan to limit rates revenue to no more than 85% of our total revenue, encouraging a balance between user fees and other revenue sources to compliment rate revenue in paying for the services that Council provides.

Rates

The council intends to provide certainty to ratepayers over their rates bills.

Rate increases will be at a rate that matches the increase to our cost base. Changes to Council's cost base are mainly driven by new or increased service levels, inflation and changes to interest expenses and depreciation resulting from the investment into capital expenditure over the 10 year plan.

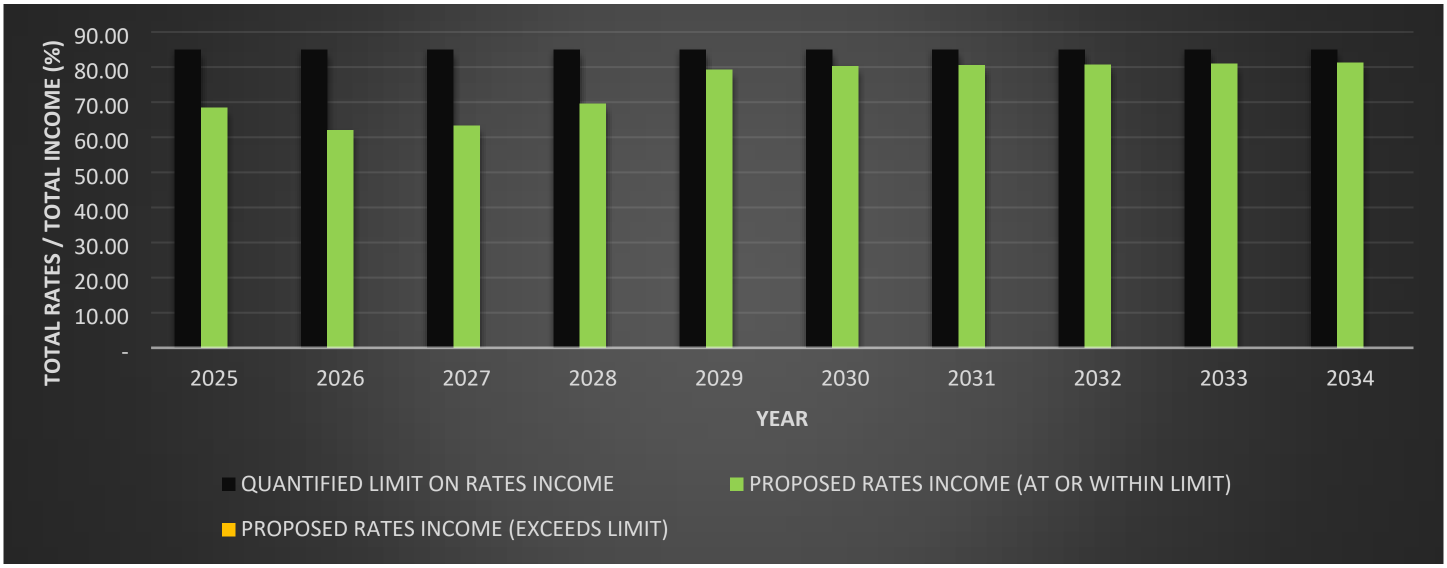
Overall rates proposed rates increases (after allowing for growth in the rating base) and the limits will be:

	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Proposed Rates increases (%)**	10.24	9.80	7.78	5.75	6.79	4.36	3.18	2.63	1.95	2.41
Quantified Limit on Rates increases (%)**	10.24	10.30	7.30	6.10	7.50	4.80	3.50	3.00	2.30	2.80

The rate limits are the proposed rate increases across existing ratepayers covering both general and targeted rates and reflecting an adjustment for future risk. Increases to individual ratepayers may be impacted by property revaluation changes and the introduction of new targeted rates such as those for new sewerage schemes.

Council will limit total rates as a proportion of total revenue to less than 85%. Council has had to maintain this limit of 85% for two reasons. Firstly, Council's increased expenditure in community facilities and infrastructure will increase the finance and depreciation costs for activities which are funded predominately from general or targeted rates and secondly, this limit provides a level of flexibility as Council activities reliant on visitor numbers for user fee revenue recover post Covid-19.

The below graph demonstrates the level that rates income will be over the period of the LTP and does not exceed our limit of 85%.

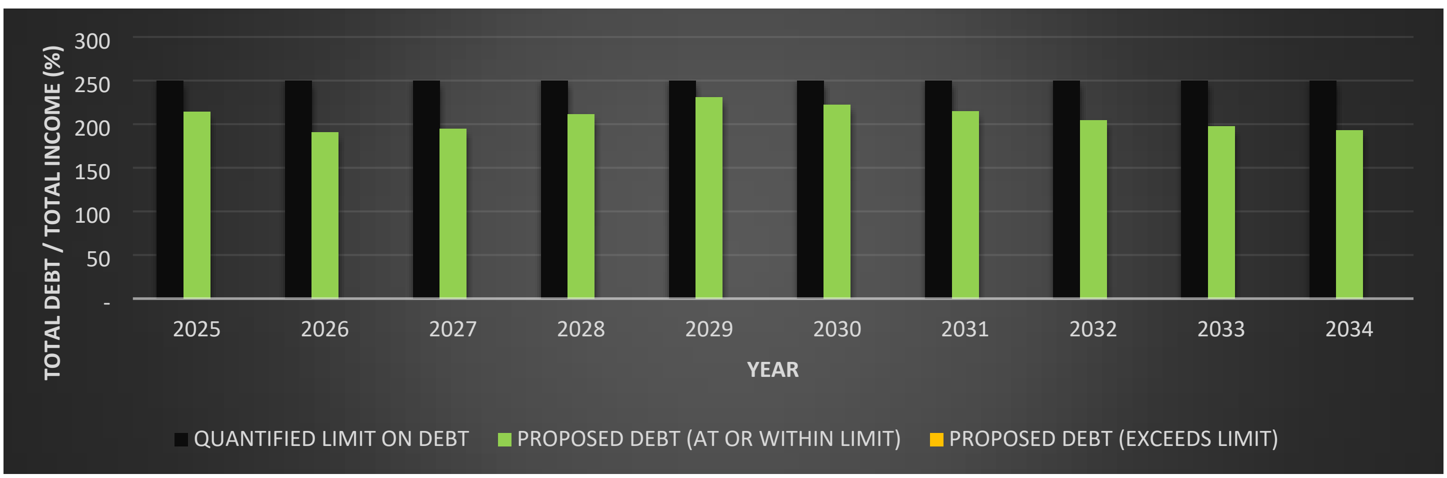


Borrowing

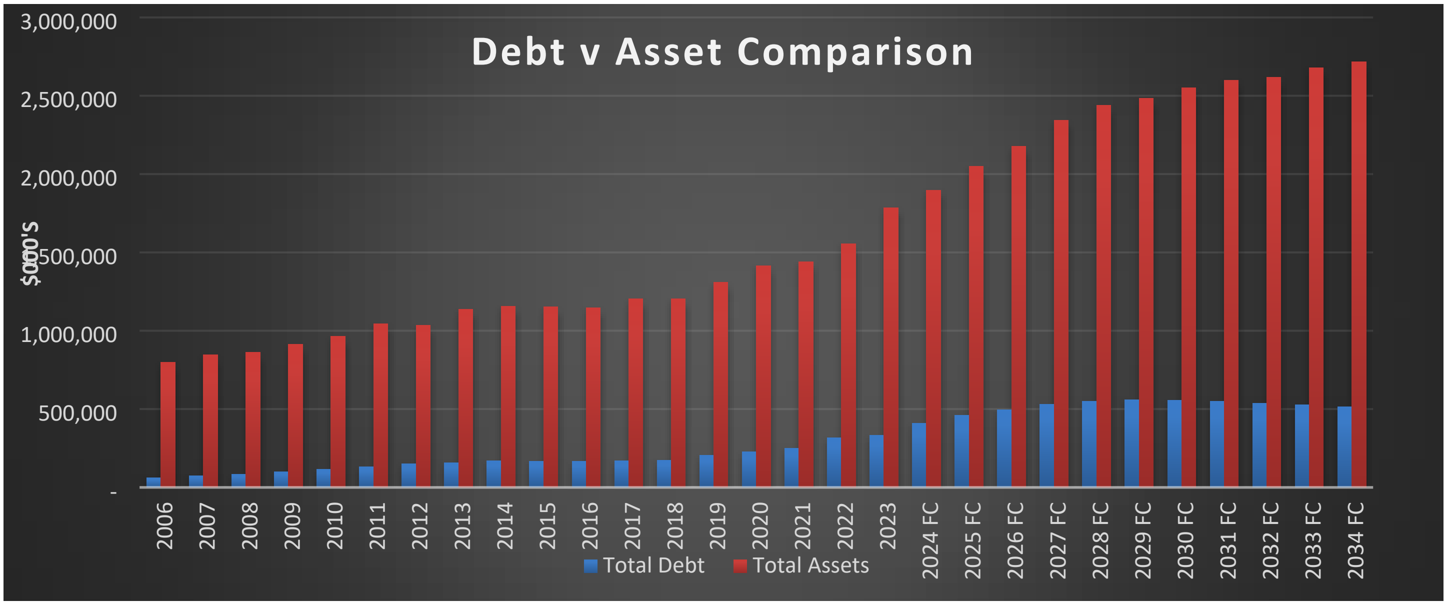
Council does not borrow to renew existing facilities and infrastructure. Borrowings are only used to grow and improve on existing facilities and infrastructure.

Unlike residential and business borrowing which is secured against assets, the Council's borrowings are secured against its revenues, in particular its ability to rate.

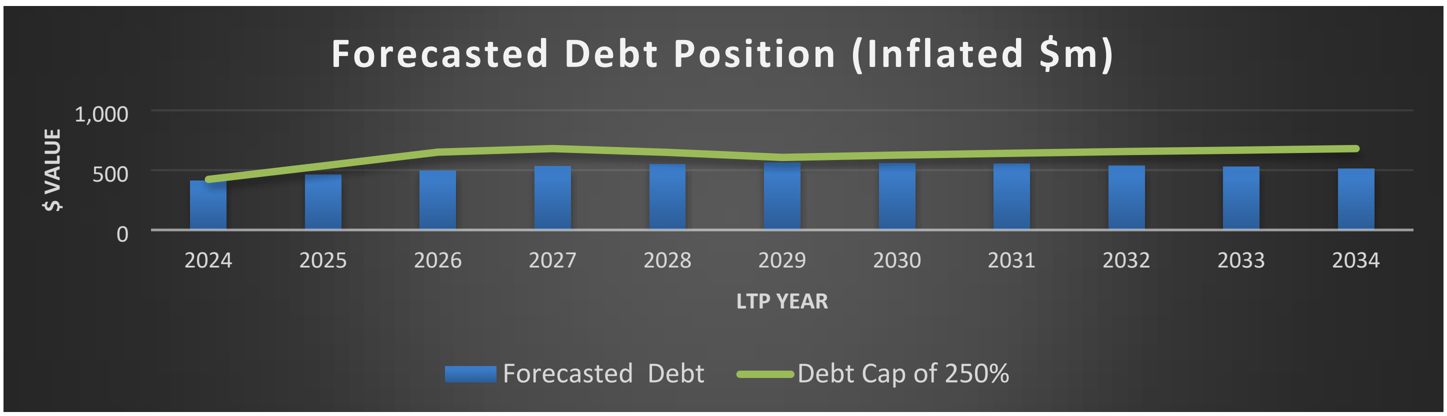
As shown by the graph below, across the profile of the LTP, debt does not exceed our limit of 250%. Debt is expected to increase from the 2024 forecasted year end position of $418million to over $513million as we invest in both essential and strategic capital programmes. The graph demonstrates that debt will be paid down towards the back end of the LTP. While this LTP includes a large capital programme, a number of significant projects attract external funding from the Central Government and other funders, enabling Council to deliver investment in the community without the need for a large borrowing programme.



In line with the above, the graph below shows that over the course of the ten years we will have increased our assets by $663 million to $2.8 billion. During the same period our debt will increase by $96 million. Despite the increase in debt we will still maintain on average 80% equity in our asset base during this time.



During the course of the ten years the increased borrowing will result in a debt profile that will peak at $557 million.



This remains within our debt limits

- Net debt to Total Revenue 231% against a limit of 250%
- Net interest to Annual Rates Income 15.8% against a limit of 25%

Council's debt level is determined by deciding on a prudent level of borrowing that can be serviced without putting pressure on Council's finances. Council has determined a prudent level based on a multiplier of not more than 2.5x (250%) revenue.

Council's debt forecast to revenue ratio as at 30 June 2023 is approximately 206% and whilst this will rise to around 231% in the year 2029, our forecast to be 193%, in 10 years' time.

The increased debt is driven in part by a significant increase in Council investment into growth related infrastructure, enabling new housing across Rotorua. While significant aspects of this investment are funded either by Central Government or development contributions, there is a timing issue where Council holds the debt until it receives the funding. Another key driver of Council's debt in the Long Term Plan is the investment in Council's wastewater treatment schemes including the Tarawera scheme and the main Treatment Plan upgrade, which supports Council's commitment to safely treating wastewater across the district.

Quantified limits on borrowing

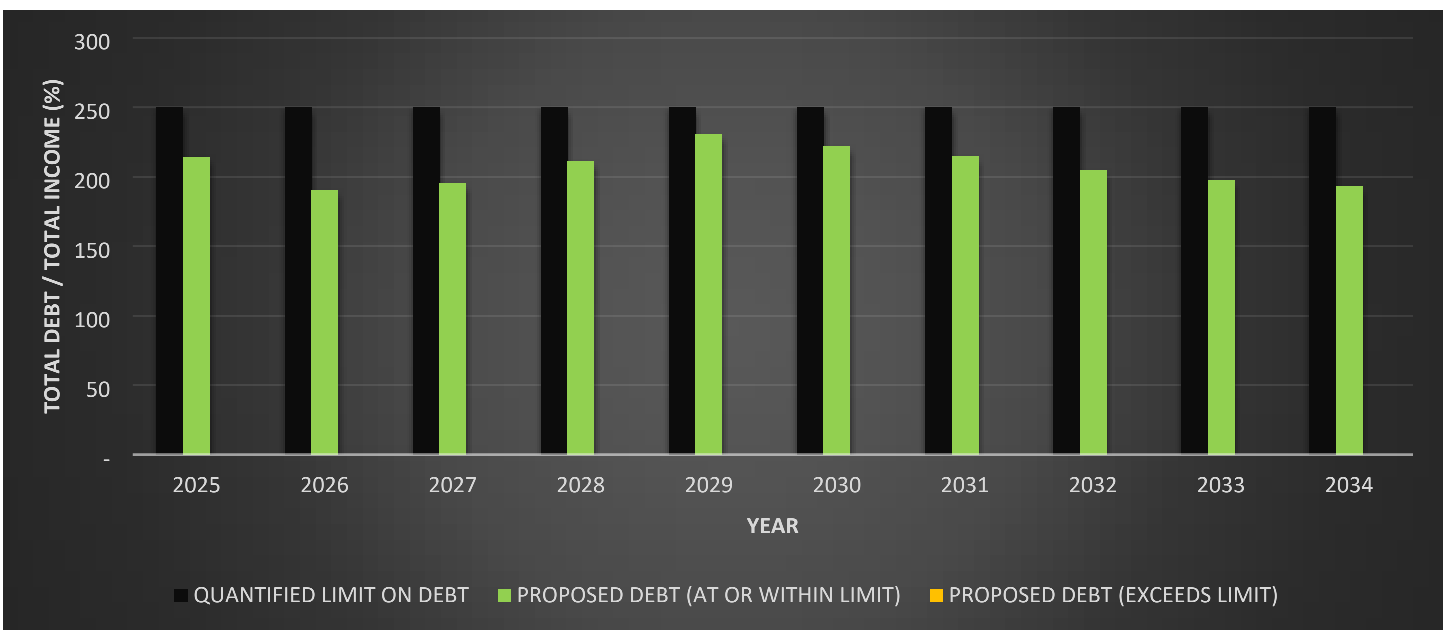
Consistent with Councils treasury policy in managing debt, Council will adhere to the following limits:

- Net interest expense on external debt as a percentage of operating revenue will not exceed 20%; and
- Net interest on external debt as a percentage of annual rates revenue will not exceed 25%; and
- Net external debt as a percentage of annual operating revenue will not exceed 250%.

As part of Councils financial strategy, to maintain debt at acceptable levels, the ratio set for this limit within this financial strategy is 250%. This is to ensure Council has adequate borrowing capacity in the future to fund unforeseen projects or be able to respond to an emergency. Council will stay below this threshold and although the debt ratio increases for periods of time to ensure sufficient investment in our community is maintained we remain within the 250x limit.

The debt to revenue ratio and external debt levels for the Long-term plan are:

	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Forecasted Debt ($m)	$ 459	$ 296	$ 531	$ 548	$ 560	$ 557	$ 551	$ 537	$ 528	$ 513
Proposed Debt / Revenue %	214%	191%	195%	211%	231%	222%	215%	205%	198%	193%
Quantified Limit on Debt %	250%	250%	250%	250%	250%	250%	250%	250%	250%	250%



Asset Sales

The Council is investigating selling some assets in order to reduce pressure on levels of debt. Council has budgeted for sales of approximately $3 million over the next ten years. These assets will only be sold if the Council gets a fair price. Council is prepared to wait until it can get a fair return.

Growth

Managing growth over the period of this plan and beyond is challenging. Our Council is investing significantly in infrastructure to enable new housing options, with several key growth projects planned over the next 10 years. In the three years to June 2023 our population grew at a compound annual growth rate of 1.3% (compared to 0.8% for the preceding 18 years). Growth is positive for Rotorua because it means people want to live here and we are attracting businesses and investment into our district.

With growth comes the need to invest in infrastructure. It is very expensive to not only put in new infrastructure but also, to renew and replace existing infrastructure. Managing the demands for growth and balancing the opportunities for future ratepayers against affordable rates and debt levels for current ratepayers is a significant challenge for our district. This investment is funded by a mixture of Central Government funding, payments from developers through Development Contributions and a small amount contributed by ratepayers.

Rotorua Council's growth assumption for LTP 2023-34 projects our population to grow from approx. 79,000 in 2023 (based on latest StatsNZ figures) to 86,000 in 2034. This increase is based on the growth projections from Infometrics and is an underlying driver for the significant investment into development over the LTP period. The Infometrics population projections have been used to help prepare demand forecasts for Councils Infrastructure Strategy and the related capital expenditure programme for the 10 year plan. The financial strategy has assumed a realistic view of the proposed population growth projections over the 10 year period. The achievability of the longer term population growth projections will require Council to ensure that land does become and is available for development. This achievability of population growth and or development is not deemed high risk given the level of funding and planning that is already taking place and will continue to take place over the short to medium term.

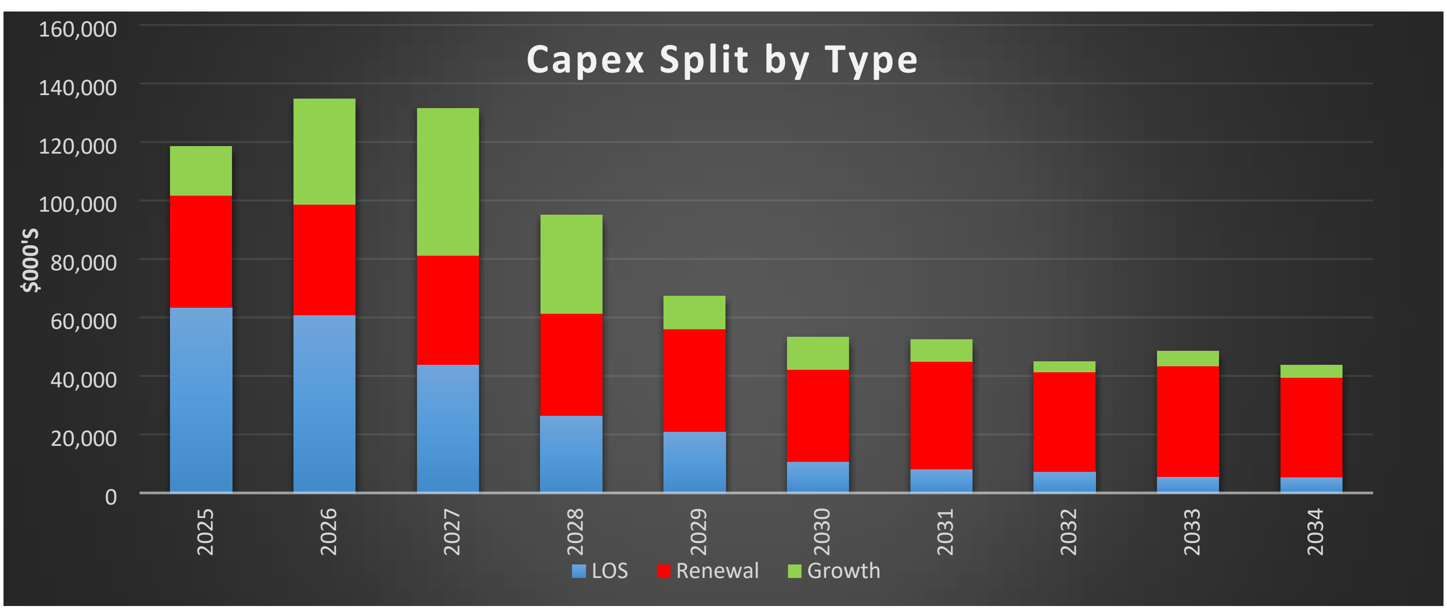
In the short term, infrastructure can accommodate the growth we are experiencing as we have capacity in our existing networks and the way growth is expected to be geographically distributed.

Funding of capital expenditure

Rates and other revenues are set to fund capital expenditure relating to the replacement of existing infrastructure, with external subsidies and borrowing used to fund capital expenditure relating to improving levels of service. External subsidies, borrowing, development and financial contributions help fund growth related capital expenditure.

Capital Expenditure

The capital expenditure within the Long Term Plan has been set to enable Council to deliver on its financial strategy, delivering core services and investing on our community while ensuring we remain prudent with ratepayer money.



Not inflated

2024-2034 Long Term Plan ($'000)			
Activity by Group	**Levels of Service**	**Growth**	**Renewals**
Wastewater	$ 87,744	$ 19,617	$ 60,000
Stormwater	$ 8,200	$ 130,971	$ 30,000
Roading	$ 29,777	$ 7,800	$ 96,141
Water	$ 19,974	$ 22,306	$ 48,665
Other	$ 106,519	$ -	$ 122,848
Total	$ 252,214	$ 180,694	$ 357,654

Not inflated

The above table shows the total cost of projects over the period of the 10 year plan categorised by type of expenditure. Growth expenditure provides new or improved assets enabling more residents to live in our city; capital expenditure to improve service levels is where we create new assets to service the existing population; and renewals restore our existing assets to their original function or capacity.

The Long-Term Plan provides for $610 million of funding for the replacement of existing assets that are near the end of their economic lives, and new assets required to improve existing levels of service. This spend is based on information developed in consultation with in-house and external experts and held in our asset management systems which groups assets, holds condition assessments, applies assumptions and averages. These in turn are used to determine estimated useful lives and expected replacement dates and values. This forms the basis of our capital expenditure program for the next 10 years and ensures that we are good custodians of the assets we already have.

Council has significantly increased its investment in growth infrastructure from the last Long Term Plan in order to enable housing supply within Rotorua. This Long Term Plan provides for $181 million of funding for growth infrastructure, including $120 million towards an Infrastructure Acceleration Fund (IAF) funded stormwater project which attracts a $85 million subsidy from Central Government. As we increase our investment in growth infrastructure, Development Contributions are an important funding tool to ensure the right groups are paying towards this investment.

Council is contributing a significant amount to improve the levels of service of existing facilities and infrastructure. Of the $252million proposed above that is going towards Level of Service projects just under $150million will be to complete significant upgrades in Rotorua's wastewater infrastructure, including Lake Tarawera, Lake Rotoiti and the main Rotorua Wastewater Treatment Plant in order to ensure that we are meeting our health and environmental obligations in the way we treat Rotorua's wastewater, and that the lake communities are connected with efficient and safe reticulation and processing capabilities eliminating the adverse effects of septic tanks leachate on the water quality of the lakes and the health of those communities and visitors. Council is nearing the completion of the Rotoiti wastewater scheme and has included a new capital rate on connected properties from 2024/25 towards this scheme. Works on the Lake Tarawera scheme are underway with further consultation on the capital contribution due through the LTP consultation process.

Our investment in levels of service also includes $80m into the Museum restoration project to enable the reopening of our iconic landmark, including strengthening for seismic risk. Council has committed to its $15 million contribution with the balance expected from external subsidies and grants. Alongside this investment in the Museum building is a $8 million investment in Museum exhibitions, ensuring that the displays in the refurbished building meet the aspirations of the community. Other improvements into the building such as the redesign of the air conditioning systems will mean that Rotorua will be able to attract a greater variety of cultural and international treasures than was previously possible. This investment will therefore continue to ensure we attract visitors and locals alike to share in our history.

Included in our level of service capital expenditure are two new projects which are subject to public consultation through our Long Term Plan Consultation document. The first is a proposed $10 million investment in our Rotorua Inner City from Yr 4 of the Plan, which includes the beautification of public infrastructure within the central city area. The second is a $3 million investment in a new stage of the Aquatic Centre redevelopment, with $2.5 million funded externally. This investment in the Aquatic Centre will create a higher quality experience for visitors to our pools. The consultation document on the Long Term Plan includes options on these projects which may alter the timing and cost, and any changes as a result of community consultation will be considered in deliberations on the final 2024-34 Long Term Plan.

In order to balance the books and deliver a Long Term Plan that is financially prudent, a number of Open Spaces projects have been deferred or cancelled. These projects include the skatepark in Kuirau Park, playground and lakes enhancements and the delivery of the Parks and Reserves Strategy (PARS) work programme. The ability of Council to reintroduce these projects will be assessed as we progress through this Long Term Plan, dependent on Council's financial operating environment.

There are additional operating costs associated with adding new assets including depreciation. These costs will be funded by increases to rates.

Policy on Securities

In order to borrow money the Council has to offer our lenders some security, just like residents do with their mortgages. Like most councils, we secure our debt against our rates income.   The council borrows the majority of its debt requirements from the Local Government Funding Agency which provides long term borrowing at favourable rates compared to commercial banks or private lenders. Rates will continue to be used as security for all borrowing. Council offers this security through a Debenture Trust Deed, lenders accept this as security and it helps keep our interest rates low.

In some circumstances Council may offer other security, however, physical assets will only be pledged in certain circumstances. The council currently has no loans secured by way of mortgage over properties but may do so if the situation arises. The full policy on securities can be found in our Treasury Policy on the council's website.

Investments

The council holds investments in companies and cash.

Investments in Companies

The council is an equity holder in eight companies. The reason for holding equity interest in the companies is principally to achieve efficiency and community outcomes, rather than to receive a financial return on investment. The council holds shares in the following companies:

Council's Shareholdings Company	Shareholding	Principal reason for Investment	Budgeted return
Rotorua Economic Development Limited	100%	Economic Development	Nil
Rotorua Regional Airport Limited	100%	Economic Development	Nil

Infracore Limited	100%	Efficient Government	Nil
Waikato Local Authority Shared Services Limited	6.14%	Efficient Government	Nil
BOP LASS Limited	16.13%	Efficient Government	Nil
Civic Financial Services Limited	<1%	Risk management	Nil
Mountain Bike Events Limited	49%	Economic Development	Nil

Cash Investments

From time-to-time the council has surplus cash. Surplus cash is invested for short periods to maximise returns. The council aims to meet the average 90 day bank bill rate.

Generally the council's cash management practice is to use surplus cash to minimise external debt. The long-term plan includes an assumption that Council holds no less than approx. $1 million in cash at any one time.

Council's Treasury

Council considers it prudent to hold cash at a level that supports the balance of restricted reserves (this amount of cash is not available to offset external debt). Any cash held above the level of restricted reserves is to ensure strong lines of liquidity and access to cash remain available to Council.

Cash is supplemented by the use of committed banking facilities. The $35 million of facilities available is based on the level of cash that Council currently holds and a further amount to ensure liquidity of funding. In present financial markets, holding cash is a cheaper option than is available through the use of committed facilities.

Other Investments

As part of borrowing from the Local Government Funding Agency, the council is required to invest in financial bonds with the agency. The council will receive interest on these bonds equivalent to the cost of borrowing.

Insurance

Council fully insures water and wastewater treatment plants, along with its buildings, plant and equipment, and vehicles.

Underground infrastructure (primarily water reticulation, waste water, and storm water networks) are insured for significant natural disasters. A key assumption is that the government will provide 60% of the funding to meet reinstatement costs following a significant natural disaster. Aon has conducted a risk assessment on the likelihood of significant natural disasters, and these were assessed as being low.

Council has tested insurance cover for infrastructural assets. This cover is currently obtained by direct placements into the London insurance markets and is based on "maximum probable loss" approach rather than reinstatement value for all assets. Maximum probably loss is the anticipate value of the biggest monetary loss that might result from a catastrophe, whether natural or otherwise. External expertise is used to complete scenario modelling and provide recommendations on the level of cover.