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Research Update:

New Plymouth District Council Ratings Affirmed At 'AA/A-1+'; Outlook Remains Stable

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Table Of Contents

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Overview

- The ratings on New Plymouth District Council reflect the extremely predictable and supportive institutional framework available to local and regional councils within New Zealand, combined with the council's strong financial management and economy; very strong budgetary flexibility and budgetary performance; its exceptional liquidity; moderate debt burden; and very low contingent liabilities.
- We are affirming our 'AA' long-term and 'A-1+' short-term issuer credit ratings on New Plymouth.
- The outlook on the rating remains stable, reflecting our expectations that New Plymouth would continue to prudently manage its financial metrics in line with our forecasts over the next two years, with financial management remaining strong, liquidity remaining at exceptional levels, and debt broadly stable over the next two years.

Rating Action

On Oct. 26, 2016, S&P Global Ratings affirmed its 'AA' long-term foreign currency and local currency and 'A-1+' short-term issuer credit ratings on New Plymouth District Council, a New Zealand local government. The outlook on the rating remains stable.

Rationale

The ratings on New Plymouth District Council reflect the council's strong financial management, very strong budgetary flexibility and budgetary performance, very low contingent liabilities, and its exceptional liquidity. Supporting these strengths is New Zealand's extremely predictable and supportive institutional framework, and the district's strong local economy. The council's moderate debt burden compared with peers' partially offsets these strengths.

The council's experienced and stable management is focused on prudent financial management and has contributed to the council's strong financial position. The council has undergone a management restructure that aligned its business activities and enabled better delivery of services. We consider its debt and liquidity policies prudent, as shown in its moderate level of debt and exceptional liquidity coverage. We believe its governance and oversight of its council-controlled organizations is well managed.

New Plymouth holds substantial investments in its Perpetual Investment Fund (PIF), which holds the proceeds of the 2004 sale of its shares in energy network company Powerco. From 2012 until this year, we assessed New Plymouth on a consolidated basis, incorporating the council's major investment, via the PIF, in a majority stake in Tasman Farms Ltd. The council sold Tasman Farms earlier in 2016 and, as a result, our credit analysis now focuses on New Plymouth District Council on a core-council basis (which is the approach we take for most New Zealand local governments). We believe the divestment of Tasman Farm removes the council's key off-balance-sheet risk, and therefore, an assessment on a core-council basis best reflects the credit risk of the council.

As a result of the asset sale, a number of credit factors have simultaneously improved in our view. The council's debt burden has fallen, with the council no longer exposed to the debt held by Tasman Farms. And the council's budgetary flexibility has improved significantly, with the council no longer reliant on the nonmodifiable revenues of Tasman Farms to service its (lower) debt burden, and the council being able to modify most remaining revenue sources. The council's budgetary performance, on a core-council basis, is stronger than it has been on a consolidated basis, because the council is no longer exposed to the farm's relatively weaker financial performance, which has also exhibited volatility over past years. Finally, with the PIF now likely to hold a much more liquid portfolio over the long term, we expect that the council's liquidity coverage will remain better than it has previously been.

New Plymouth's budgetary flexibility is very strong, with modifiable revenues of about 85% of operating revenues (after S&P Global Ratings' adjustments) compared with last year's figure of about 60%. We expect the council's capital expenditure to be about 25% of total expenditure between 2015 and 2019, on a cash basis. New Plymouth has some expenditure flexibility regarding the upgrade or development of infrastructure. While some projects are "lumpy" and difficult to postpone once commenced, the council can delay smaller projects if the need arises. The absence of significant population growth or an infrastructure backlog provides the council with further flexibility.

The council's stronger operating position, combined with its moderate capital-expenditure program, underpins its after-capital account surpluses and falling debt stock in 2019. The council has been scaling back its capital investment program by reducing spending on discretionary projects, while also lengthening the assumed useful life of existing assets. We forecast cash operating surpluses to average 21.6% of operating revenues in 2015-2019 and after-capital account surpluses of 1.3% of total revenues over the same period.

In addition, we expect New Plymouth's debt burden to remain moderate compared with international peers'. Total tax-supported debt is likely to remain broadly stable over the next few years, and be about 68% of operating revenues in 2019. We forecast the council's average interest expense will remain relatively low overall at 4.5% of operating revenue in 2016-2019. In addition, the interest expense is likely to gradually decline in line with the council's lower debt burden, hedging position, and from its participation in the Local Government Funding Agency (LGFA).

New Plymouth's contingent liabilities are very low. Its quantifiable contingent liabilities in 2015 were mainly for potential "weathertightness", or building moisture damage, claims of NZ$1 million. In 2016, the council made a provision for these two claims, addressing the council's quantifiable contingent liabilities.

We consider New Plymouth's economy to be strong compared with peers'. While the council's GDP per capita is high at about US$63,000 on average over 2013 to 2015, we consider that this high level largely reflects the region's significant liquefied natural gas sector, with profits mainly being repatriated outside the region. By contrast, its residents' wage and salary income, which more closely reflects the council's revenue base, is similar to the New Zealand average. The council's industry concentration in commodity-dependent sectors such as agriculture, and oil and gas, also adds some economic vulnerability in our view.

We assess the institutional framework within which New Zealand local governments operate as being one of the strongest and most predictable globally. The New Zealand local government system promotes a strong management culture and fiscal discipline among New Zealand councils. This provides a source of credit strength for New Plymouth, and allows it to support higher debt burdens than some of its international peers can tolerate.

Liquidity

New Plymouth's liquidity is exceptional, with free cash and liquid assets (after haircuts) equivalent to about 350% of the next 12 months' debt maturities and interest payments. When including unutilized bank facilities of NZ$32 million, New Plymouth's debt-servicing ratio reaches 420%. We estimate that New Plymouth will have, on average, free cash and liquid assets of about NZ$157 million (including liquid assets held in the council's investment fund) to cover its NZ$39 million of debt maturing within the next 12 months and NZ$6 million of interest repayments.

New Plymouth's debt-servicing ratio is likely to remain exceptional. With the asset sale, PIF's value has increased to NZ$270 million as at June 30, 2016. The key focus for PIF will be to rebalance the fund and return to a more diversified and liquid fund based on the strategic asset allocation policy. Under the current fund policy, no more than 10% of the fund would be invested in a single asset, to prevent future concentration and liquidity risk and to support diversification.

We consider New Plymouth's access to external liquidity as being satisfactory. New Zealand's capital markets are comparatively liquid, but, given its small size, we don't consider them as being particularly deep. During the severe market dislocation in 2008 and 2009, some New Zealand councils had difficulty issuing unrated commercial paper.

New Plymouth is participating in the New Zealand LGFA. LGFA is a mutual body representing participating New Zealand local governments, and aims to access funding at a cheaper rate than many individual New Zealand councils can. Participation in the LGFA has helped improve the council's liquidity by lengthening its maturity profile.

Outlook

The stable outlook reflects our expectations that New Plymouth will continue to prudently manage its financial metrics in line with our forecasts over the next two years, with financial management remaining strong, liquidity remaining at exceptional levels, and debt steadily declining over the next two years.

Given the current strength of New Plymouth's stand-alone credit profile, we consider downward pressure on the rating is very unlikely over the next two years. However, downward pressure could occur if there were a significant and unexpected increase in capital spending resulting in large after-capital account deficits of total revenue over a sustained period. This could weaken the council's budgetary performance over the prolonged period, leading to higher debt and interest expense; such a scenario would also include weaker liquidity coverage of upcoming debt-servicing expenses.

Likewise, we believe any upward momentum of the ratings would be linked to the New Zealand sovereign's creditworthiness.

Key Statistics

Table 1

New Plymouth District Council Key Statistics

	--Year end June 30--				
Cash basis; mil. NZ$	**2015 A**	**2016(E)**	**2017 (BC)**	**2018 (BC)**	**2019(BC)**
OPERATING RESULTS					
Council rates	74.8	77.5	80.7	81.6	84.4
User charges	33.1	34.2	29.5	33.1	33.8
Interest income	2.8	1.8	1.4	2.0	2.2
Other operating revenues	13.4	14.5	20.4	21.2	21.6
Adjusted Operating Revenues	124.0	127.9	131.9	137.9	142.0
Payments to suplliers and employees	92.5	96.8	99.4	99.3	101.8
Interest payments	6.0	5.9	6.0	5.9	5.2
Other operating expenditure	0.5	0.0	0.1	0.1	0.1
Adjusted Operating Expenditures	99.0	102.7	105.4	105.3	107.1
Operating Balance	25.0	25.2	26.5	32.6	34.8
+ Adjusted capital revenues	13.2	8.0	6.2	6.8	7.3

Table 1

New Plymouth District Council Key Statistics (cont.)					
	--Year end June 30--				
Cash basis; mil. NZ$	**2015 A**	**2016(E)**	**2017 (BC)**	**2018 (BC)**	**2019(BC)**
- Adjusted capital expenditures	37.9	36.7	33.7	37.3	29.6
Balance After Capital Accounts	0.2	(3.5)	(1.0)	2.0	12.6
FINANCIAL PERFORMANCE INDICATORS					
Operating balance (% of adj. operating revenues)	20.2	19.7	20.1	23.6	24.5
Balance after capital accounts (% of adj. total revenues)	0.2	(2.6)	(0.7)	1.4	8.4
Modifiable revenues (% of adj. operating revenues)	86.9	87.3	83.5	83.2	83.2
Capital expenditures (% of total expenditures)	27.7	26.4	24.2	26.2	21.6
FINANCIAL POSITION INDICATORS					
Tax-supported debt	113.7	110.1	111.0	109.0	96.4
Tax-supported debt (% of cons. operating revenues)	91.6	86.0	84.2	79.1	67.9
Interests (% of adj. operating revenues)	4.8	4.6	4.5	4.3	3.7

A--Actual. E--Estimate BC--Base case.

Ratings Score Snapshot

Table 2

Ratings Score Snapshot	
Key Rating Factors	
Institutional framework	Extremely predictable and supportive
Economy	Strong
Financial management	Strong
Budgetary flexibility	Very strong
Budgetary performance	Very strong
Liquidity	Exceptional
Debt burden	Moderate
Contingent liabilities	Very low

Key Sovereign Statistics

Sovereign Risk Indicators. Interactive version available at http://www.spratings.com/sri

Related Criteria And Research

Related Criteria

- Criteria - Governments - International Public Finance: Methodology: Rating Non-U.S. Local And Regional Governments Higher Than The Sovereign - December 15, 2014
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

- Criteria - Governments - International Public Finance: Methodology For Rating Non-U.S. Local And Regional Governments - June 30, 2014
- Criteria - Governments - International Public Finance: Methodology And Assumptions For Analyzing The Liquidity Of Non-U.S. Local And Regional Governments And Related Entities And For Rating Their Commercial Paper Programs - October 15, 2009

Related Research

- New Zealand Councils' High Governance Standards Ensure Strong Financial Management, Transparency, And Long-Term Planning, Nov. 30, 2015
- International Local And Regional Governments Default And Transition Study: 2012 Saw Defaults Spike, March 28, 2013

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Ratings Affirmed

New Plymouth District Council	
Issuer Credit Rating	AA/Stable/A-1+
New Plymouth District Council	
Commercial Paper	A-1+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.