S&P Global Ratings

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Research Update:

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

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Table Of Contents

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Overview

- New Plymouth District Council's robust financial management, excellent liquidity, and high level of budgetary flexibility support its ratings.
- We expect New Plymouth's budgetary performance to weaken temporarily as capital expenditure rises during the upgrade of New Plymouth Airport's terminal. However, the increase in debt likely will be modest.
- We are affirming our 'AA' long-term and 'A-1+' short-term ratings on New Plymouth.
- The outlook on the long-term ratings is stable.

Rating Action

On Oct. 31, 2018, S&P Global Ratings affirmed its 'AA' long-term and 'A-1+' short-term issuer credit ratings on New Plymouth District Council, a New Zealand local government. The outlook on the long-term ratings is stable.

Outlook

The stable outlook reflects our expectation that our ratings on the New Zealand sovereign will continue to constrain the ratings on New Plymouth, while we see only a small likelihood that the council's own credit metrics will deteriorate substantially. While New Plymouth's budgetary performance will be temporarily weaker during the upgrade of New Plymouth Airport's terminal, we expect the council's debt burden to remain moderate compared with peers.

Downside scenario

Downward pressure on the ratings could emerge if New Plymouth's fiscal performance were to deteriorate over a prolonged period, resulting in a steep rise in the council's debt. Such developments might also cause us to lower our assessment of New Plymouth's financial management. Alternatively, we would lower our ratings on New Plymouth if we were to lower our ratings on the New Zealand sovereign.

Upside scenario

We would raise our ratings on New Plymouth if we were to raise our foreign-currency rating on the New Zealand sovereign, all else being equal. This is because the council's own credit metrics are currently stronger than those of the sovereign.

Rationale

After updating our forecasts through fiscal 2021 (i.e., the year ending June 30, 2021), we expect New Plymouth's after-capital deficit to temporarily widen in fiscal 2019 during the upgrade of the airport terminal. However, we still expect the council to maintain its excellent liquidity, high level of budgetary flexibility, and moderate debt burden. New Plymouth's relatively large Perpetual Investment Fund helps the council to sustain a significantly higher liquidity position than many domestic peers can. We expect that the council's robust financial management, and New Zealand's supportive institutional settings, will continue to underpin the ratings.

Financial management and New Zealand institutional framework support the ratings; economy sound despite potential headwinds

We continue to cap our ratings on New Plymouth at the level of our long-term foreign-currency rating on New Zealand. We believe that New Zealand local authorities cannot withstand a stress scenario better than the sovereign can, and that the council's credit metrics would deteriorate in line with those of the sovereign in a stress scenario. Meanwhile, the institutional framework in which New Zealand councils operate is a key strength supporting New Plymouth's credit profile. The framework promotes a robust management culture, fiscal discipline, and high levels of financial disclosure. It allows New Zealand councils to support higher levels of debt than some international peers can tolerate at similar ratings.

New Plymouth is governed by an elected mayor and 14 elected councilors, who together delegate day-to-day management of the council to a full-time chief executive. A new chief executive commenced in November 2017, having previously held the equivalent position at nearby South Taranaki District Council. The council's chief financial officer will also depart in December 2018, and the council is currently recruiting for a successor. New Plymouth prepares 10-year long-term plans every three years and annual plans in the intervening years, in line with New Zealand requirements. Like most of its peers, New Plymouth borrows only in local currency, and mitigates its interest-rate risk exposure through hedging. We do not expect changes in New Plymouth's executive team to lead to material shifts in its financial strategy during our forecast horizon.

New Plymouth's economy is underpinned by the large oil, gas, and dairy industries operating in the Taranaki region. The district's gross domestic product (GDP) per capita averaged about US$54,400 during fiscal years 2015 to

2017, according to data from the Ministry of Business, Innovation, and Employment. This is high by international standards, though New Plymouth's economic performance is somewhat volatile due to fluctuations in oil and dairy prices. We believe that the GDP data overstate New Plymouth's relative economic strength because profits from the oil and gas sector are mostly repatriated to equity owners outside of the district. In contrast, New Plymouth's average household income is roughly in line with the national average. In April 2018, the New Zealand central government announced a moratorium on new offshore oil and gas exploration. The moratorium is effective immediately, though it does not affect existing permits. While we do not believe these developments will have a significant impact in the short term, there may be longer-term ramifications from lower investment in the regional economy.

Fiscal performance to dip temporarily, though budgetary flexibility and liquidity remain key strengths

Like all New Zealand councils, New Plymouth has recently published its triennial long-term plan setting out its priorities for fiscal years 2019 to 2028. During the next three years, we expect New Plymouth's capital outlays to be larger than they have been in recent years. Following the council's acquisition of the Crown's 50% share of New Plymouth Airport on July 1, 2017, at a cost of NZ$3.25 million, the council is now the sole owner and we have begun consolidating the airport's financial metrics with those of the parent council. The airport is currently redeveloping its terminal at a cost of around NZ$21.7 million to NZ$28.7 million. Most of this expenditure--about NZ$18.3 million--is scheduled to take place in fiscal 2019, and will be funded by borrowing from the council. The council anticipates the new terminal being operational by the end of calendar 2019. We expect New Plymouth's after-capital deficit, as a proportion of total revenues, to widen to 20.6% in fiscal 2019 before reverting to around 5%-6% in the outer years of our forecasts. We also expect New Plymouth's operating surpluses, as a proportion of operating revenues, to remain solid, averaging about 20.9% during fiscal years 2017 to 2021.

We forecast that New Plymouth's debt burden will rise to about 107% of operating revenues by the end of fiscal 2021, up from 87% at the end of fiscal 2018. This debt burden remains moderate, in our view. We also expect the council's interest expenses to remain low, averaging about 4.4% of operating revenues. Similar to most of its domestic rated peers, New Plymouth sources the majority of its external debt through New Zealand's Local Government Funding Agency. The council intends to on-lend funds to New Plymouth Airport to fund the latter's terminal redevelopment, and we count these borrowings as part of New Plymouth's total tax-supported debt. Budgetary flexibility remains one of the council's key strengths. We estimate that about 86% of the council's operating revenues are modifiable, which means they can be raised or lowered at the council's discretion.

New Plymouth's liquidity remains excellent. Buttressing its liquidity is the council's Perpetual Investment Fund (PIF), which had a balance of about NZ$289 million as of June 30, 2018. The council has outsourced management of the PIF to Mercer (NZ) Ltd. An independent board of guardians monitors the PIF, and its assets are diversified across listed equities, fixed income, alternative assets, private equity, and cash. After applying our standard haircuts to the PIF's holdings, we estimate that New Plymouth's free cash and liquid financial assets will average about NZ$122 million during the next 12 months. We expect its debt-servicing needs to comprise NZ$15 in maturing long-term loans, NZ$39 million in short-term paper, and about NZ$7 million in interest payments, resulting in an overall debt-service coverage ratio of about 199%. New Plymouth also has access to two undrawn bank facilities totaling NZ$24 million.

The PIF aims to pay an annual "release" to the council of 3.3% of assets under management, equivalent to about NZ$8 million to NZ$9 million per annum. We treat these releases as operating revenues because they are effectively used to subsidize rates. We note that if the PIF's investment returns are below expectations, the council might reduce the annual PIF release. We consider New Plymouth's access to external liquidity to be satisfactory. While New Zealand's capital markets are comparatively liquid, they lack depth, given their relatively small size. During the severe market dislocation of 2008 and 2009, some New Zealand councils had difficulty issuing unrated commercial paper.

We assess New Plymouth's contingent liabilities as being very low. The council's insurance policies are adequate and on par with peers. New Plymouth has made provisions for potential claims under the weathertight homes resolution service. Like many of its rated domestic peers, New Plymouth is a shareholder and joint guarantor of the Local Government Funding Agency's borrowings. We consider it very unlikely that this guarantee will be activated in the near future.

Key Statistics

Table 1

Key Statistics

	--Year ended June 30--					
(mil. NZ$)	2016	2017	2018E	2019BC	2020BC	2021BC
Selected Indicators						
Operating revenues	124	123	137	140	148	155
Operating expenditures	103	101	101	112	120	120
Operating balance	21	21	36	28	28	35
Operating balance (% of operating revenues)	17.2	17.5	26.0	19.9	18.6	22.6
Capital revenues	8	7	8	10	11	13
Capital expenditures	33	34	50	68	48	58
Balance after capital accounts	-3	-6	-6	-31	-9	-9

Table 1

Key Statistics (cont.)

	--Year ended June 30--					
(mil. NZ$)	**2016**	**2017**	**2018E**	**2019BC**	**2020BC**	**2021BC**
Balance after capital accounts (% of total revenues)	-2.6	-4.3	-4.5	-20.6	-5.5	-5.5
Debt repaid	50	0	21	15	0	15
Gross borrowings	46	0	29	46	9	24
Balance after borrowings	-7	-6	2	0	0	0
Modifiable revenues (% of operating revenues)	90.0	90.2	86.6	84.4	83.7	83.0
Capital expenditures (% of total expenditures)	24.2	25.3	33.0	37.9	28.4	32.5
Tax-supported debt (outstanding at year-end)	110	110	118	149	158	167
Tax-supported debt (% of consolidated operating revenues)	88.7	89.7	86.4	106.4	106.8	107.3
Interest (% of operating revenues)	4.7	4.2	3.8	4.7	4.7	4.8
Local GDP per capita (single units)	70,219	72,942	N/A	N/A	N/A	N/A

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. dc--Downside case represents some but not all aspects of S&P Global Ratings' scenarios that could be consistent with a downgrade. uc—Upside case represents some but not all aspects of S&P Global Ratings' scenarios that could be consistent with an upgrade. N/A--Not applicable. N.A.--Not available. N.M.--Not meaningful. 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	Average
Liquidity	Exceptional
Debt burden	Moderate
Contingent liabilities	Very low

S&P Global Ratings bases its ratings on local and regional governments on the eight main rating factors listed in the table above. Section A of S&P Global Ratings' "Methodology For Rating Non-U.S. Local And Regional Governments," published on June 30, 2014, summarizes how the eight factors are combined to derive the foreign currency rating on the government.

Key Sovereign Statistics

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

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria - Governments - International Public Finance: Methodology: Rating Non-U.S. Local And Regional Governments Higher Than The Sovereign, Dec. 15, 2014
- 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, Oct. 15, 2009
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Public Finance System Overview: New Zealand's Institutional Framework For Local And Regional Governments, Dec. 11, 2016

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 agreed that all key rating factors were unchanged. Key rating factors are 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.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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