Investment Strategy (Attachment I)

Purpose

The annual Investment Strategy sets out Council's investment goals and targets for the coming year. The aim of the strategy is to guide the management of Council's investment portfolio to:

• Preserve capital by managing the portfolio in accordance with the Investment Policy and
• Ensure liquidity when required for Council's operational and capital expenditure needs.
• Achieve an acceptable rate of return by ensuring a balanced and diversified portfolio, in terms of allowable investment products, credit ratings and maturation terms that will outperform the benchmark indices.

Scope

The *Investment Strategy* applies to all managers and employees who actively manage the investment of surplus funds or have responsibility for employees who actively manage the investment of surplus funds. This strategy should be read in conjunction with the *Investment Policy*.

Context

The City's investment strategy is determined after taking into consideration a review of the following issues:

• global and domestic economic investment environments
• investment policy and legislative constraints
• current composition of Council's investment portfolio
• short, medium and long term financial plans.

Investment environment

Financial and investment environments, both globally and domestically, continue to improve at different rates across various regions. The global financial recovery process has been aided by a more standardised international regulatory process with more stringent capital adequacy requirements for financial institutions.

In Australia, a history of prudent regulation of the financial institutions by the Australian Prudential Regulation Authority (APRA) has meant that Australian based regulated financial institutions have already operated for an extended period under stringent capital adequacy and liquidity requirements. Council's investments all fall under APRA regulation with the result that the portfolio is conservative and secure.

Interest rates have remained low, with the official cash rate at 1.5% since 3 August 2016.

Legislative Constraints

Council's investment opportunities are constrained by a combination of legislation, regulation and any directions and guidelines issued by the Minister or the Office of Local Government. There has been no change to the investment legislative environment for a number of years and the most recent Ministerial Investment Order released in January 2011 continues to limit Council's investment options to:

• term deposits with Approved Deposit-taking Institutions (ADIs)
• other ADI senior ranked securities
• investments with NSW Treasury Corporation (TCorp)
• funds or securities issued or guaranteed by the Commonwealth or any State or Territory.

Reporting of Investments to Council

As outlined in the Investment Policy, Council will report a summary of investments and a reconciliation of invested funds each month to Council. These will include summaries by Asset Group, Credit Rating, Institution Limits and Maturity Dates. Note for the institution limits and reports, subsidiary banks will be combined with their parent companies eg. Bankwest is operating under the banking licence of Commonwealth Bank, so for the purposes of reporting Bankwest will be combined with Commonwealth.

Composition of Council's Investment Portfolio

Council's investment portfolio is mainly comprised of Call Accounts, Term Deposits and Floating Rate Notes.

Council's current portfolio is as follows (as at the end of March 2019):

Asset Group	**$**
Call Account	0
TCorp Cash Fund	3,195,257
Term Deposit Group	138,500,000
Floating Rate Notes (5 years)	21,500,000
Mortgage Backed Securities (long term)	2,191,370
	165,386,627

Council has been averaging approximately $160,000,000 portfolio, with existing funds meeting all operational needs.

Liquidity, Maturity and Returns

Council monitors cash flow on a daily basis. Minimal amounts are required to be kept in call accounts/cash fund due to the strategy of ensuring term deposits mature each week, while taking into account times during the year that additional funding is received (such as rates instalments) or additional payments are required (such as loan repayments).

The current average length for a term deposit held by Council is 241 days or 8 months. In the current economic climate interest rates for term deposits longer than 12 months are similar to interest rates offered for 12 months or less, and at this time it is not advantageous to increase the maturity length invested greater than 12 months. The current yield of these investments is 2.7%.

The investment policy has implemented a maximum limit of 30% for medium term investments (1-5 years), currently Council is holding 14% of funds in floating rate notes. The rates being offered for floating rate notes are only marginally higher than term deposit rates, so at this time additional funds will not be added into this type of investment. However if high rates are offered these types of investments will be considered. Current average yield for FRNs held by Council is 2.99%.

In addition Council holds two forms of Mortgage Backed Securities (MBS) which were placed in 2006 and 2007 under advice from Councils external financial advisors. After commissioning an independent investment advisory firm, an opinion of this investment was recommended to retain the portfolio until final maturity which will be 2051 and 2057 respectively. These investments are still in compliance with the ministerial order as they were made before the current order gazetted 11 February 2011 which removed MBS as an authorised investment. The current yield of these investments is 2.43%.

Another form of investment available to Council are TCorp Growth Funds which are designed to be held for 3 to 7 years, however funds can be accessed at any time. Council investment policy has been updated in 2019 to distinguish between the different funds that TCorp offers, Cash Funds (similar to call accounts) and Growth Funds that are managed funds with a varied portfolio including cash, shares and property. The investments returns for medium growth fund as at January 2019 was 4.77% p.a. 3 years and long growth term returns were 8.06%p.a. 3 years, 7.41% p.a. 5 years and 9.86% p.a 7 years. This return is much higher than what Council can achieve currently from term deposits and floating rate notes. Future investments with TCorp Growth Funds will be considered in line with Councils Investment Policy.

Internal Loans

As stated in the current Borrowing Strategy, Council may use internal reserves and surplus funds to minimise existing or future loan liabilities. The basis of this is that interest rates on borrowings are, on average, higher than the interest income rates earned on cash investments.

Advisors

Council currently doesn't engage an external advisor, with the previous one being Oakvale Capital Limited up until 2011 (at $33,000 per annum). However with the low interest rates currently being offered by the financial institutions for term deposits (50 basis points less than January), it would be prudent to seek advice in how best to maximise returns, which may include investment in the TCorp growth facilities.

It is also a requirement under the OLG Guidelines to report monthly to Council the change in market value, as well as face value of investments. An advisor can provide this to us on a monthly basis as many also have an online platform for Councils to view and report investments being held.

Requests For Quotes are currently being received for both advisory services and use of an online investment system.

Further information about TCorp

According to TCorp 36th annual report to Parliament (for year ended 30 June 2018), TCorp currently has $94 billion of government funds under management.
From the Review of NSW Local Government Investments – Final Report, Michael Cole, April 2008, Recommendation 5 recommends that the capital growth investment option will continue to be available through the TCorp Hour-Glass Investment Facilities due to the advantages of a centralised system.

Section 6.19 A centralised system implies that investments are managed on a consolidated basis by Central Government or an established entity. The management framework requires that the central management authority is suitably qualified in investment management and has appropriate skills, expertise, systems and governance to reliably fulfil this role.

Section 6.20 Advantages of the centralised system:

- Provides the strongest controls with the associated lowest risk of unfavourable outcomes;
- Can be monitored externally by a board and external audit control procedures;
- Transaction costs are minimised as work is performed at the wholesale level. Under a decentralised system, Councils make transactions at retail margins; and
- Allows for the concentration of expertise and knowledge which is made available to all individual entities.

Section 6.21 Disadvantages of the centralised system:

- Increased cost to the incumbent management authority (either central agency or public financial institution) which must facilitate the additional account activities of Councils;
- Loss of flexibility at the individual entity level;
- Centralised policy and political accountability; and
- Focus on prescriptive regulations can create perverse behaviour and arbitrage to ensure maximum returns within the prescribed regulations.