ATTACHMENT I - INVESTMENT STRATEGY

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

The current issue on COVID19 has shown severe effect on the global economy scale. The pandemic has caused restrictions on people's movements, inherently affecting the market supply chains. Countries around the world have closed their boarders, restricting tourism trade and affecting the international flow of goods and services. In Australia, we saw drastic decline in trade in the industries of airline, tourism, retail, events & hospitalities, universities; and health. Inherently affecting the Australian economy.

Interest rates is now in an all-time low, with the official cash rate at 0.10% since 04 November 2020.

Legislative Constraints

The 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 several years and the most recent Ministerial Investment Order released in January 2011 continues to limit the 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, the 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/Liquidity Dates.

Note, for the institution limits and reports, subsidiary banks will be combined with their parent companies - e.g. 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

The 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 April 2021):

Asset Group	**$**
General Fund Account	2,227,946
Current Cash on Call Group	7,675,764
Term Deposit Group	118,000,000
Floating Rate Notes	11,750,000
Mortgage Backed Securities (long term)	2,033,042
	141,686,751

In the last twelve months (as at end of April 2021), the Council has been averaging approximately $155,000,000 portfolio, with existing funds meeting all operational needs.

Liquidity, Maturity and Returns

The Council monitors cash flow on a daily basis. In managing the day-to-day cashflow requirements, Council will place sufficient funds in Call Account, strategise the maturity profile of the Investment Portfolio; while considering the times during the year that additional funding is received (such as rates instalments) or additional payments are required (such as loan repayments).

The Council's enhanced benchmark rate to measure its investment performance by exceeding the RBA cash rate, at least by 20 additional basis points (0.20% p.a.). The 20 basis point increase was based on the average increased credit spreads (or margins) over bank bill rates on offer in relation to 30–90 day investments at the time. The 30-90 bank bill rates represented a reflective benchmark for investment if the risk of long-term investment at fixed rates and margins was removed from the portfolio.

Under the current economic climate, we have seen the spread on interest rates dissipate. The Government's stimulus initiatives for authorised deposit-taking institutions (ADIs), under the Term Funding Facilities (TFF), caused the banks' appetite for investors to decline – resulting in lower interest rates being offered. For example, Council's Investment Portfolio yield pre-COVID19 (February-2020) was 1.62%; and, as at April-2021 the portfolio generated a 0.69% average return. Further contraction in the Council's Investment Portfolio return is possible despite Government efforts to support a recovery.

The uncertainty of the current and future economic outlook; and the lack of attractive interest rates in the longer term, drove most investors' strategy to be shorter term centric i.e. less than 1-year term.

The Investment Policy indicates a maximum limit of 40% for medium term investments (1-5 years), currently Council is holding 16% of funds invested in this tenor (term). The rates being offered for floating rate notes are only marginally higher than term deposit rates – e.g. Aa3 bank 3-year FRN offer 3months BBSW+42bps (or 0.46% for the initial interest rate) compared to 0.66% 3-year Term Deposit rate. At this point in time, desire for this type of product is not preferred. However, if higher interest rate spreads are offered in the future, the relevant FRN is to be considered for investments – subject to Council's risk appetite.

In addition, the Council holds two forms of Mortgage Backed Securities (MBS) which were placed in 2006 and 2007 under advice from the 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 average yield of these investments is 0.53%.

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. The 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. 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

Currently, the Council does not engage an external advisor, with the previous one being Oakvale Capital Limited up until 2011 (at $33,000 per annum). To ensure informed decisions are made in relation to the Cash and Investment functions (Treasury) of the Council, the treasury responsible officers will seek updates from the regularly received market/economy media release/conferences from various financial institutions and brokers. However, with the low interest rates currently being offered by financial institutions for term, 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.

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.