

Research Update:

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

September 29, 2020

Overview

- We expect the operating balance of New Plymouth, a New Zealand local council, to dip in 2020-2021 as a consequence of the COVID-19 economic shock. The council's debt burden will continue to rise as it pursues existing capital investment plans, too.
- New Plymouth's Perpetual Investment Fund buttresses the council's exceptional liquidity.
- We are affirming our 'AA/A-1+' long- and short-term issuer credit ratings on New Plymouth.
- The positive outlook reflects that on the New Zealand sovereign. New Plymouth's stand-alone credit profile is currently higher than New Zealand's, but we cap our ratings on New Plymouth at those on the sovereign.

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Rating Action

On Sept. 29, 2020, S&P Global Ratings affirmed its 'AA/A-1+' long- and short-term issuer credit ratings on New Plymouth District Council, a New Zealand local government. The outlook remains positive, reflecting our positive outlook on the New Zealand sovereign foreign-currency rating.

Outlook

The positive outlook on New Plymouth reflects that on the sovereign, because the ratings on the council are constrained by the long-term foreign-currency rating on New Zealand.

Upside scenario

We could raise our ratings on New Plymouth within the next two years if we were to do the same for New Zealand, all else being equal.

Downside scenario

We would revise the outlook on New Plymouth to stable if we were to do the same for the New Zealand sovereign or if New Plymouth's own creditworthiness deteriorates. The latter could occur if after-capital-account deficits are larger or more prolonged than we currently expect, resulting in a persistent rise in the council's debt burden.

Rationale

We expect a large economic shock in New Zealand during 2021 because of the effects of the COVID-19 pandemic. We have updated our analysis for New Plymouth following publication of the council's latest annual plan for fiscal 2021 (ending June 30, 2021). New Plymouth's operating deficit will dip temporarily due to the COVID-19 recession and measures rolled out by the council as part of its "Back On Our Feet" economic support package. The council's debt burden is rising, continuing its recent trend. New Plymouth's relatively large Perpetual Investment Fund helps it to sustain a very high level of liquidity.

Although New Plymouth has a stand-alone credit profile higher than that of the sovereign, we cap our ratings on New Plymouth at the level of the foreign-currency rating on New Zealand. New Plymouth does not meet the conditions to be rated above the sovereign set out in our criteria. We do not believe any New Zealand local council, including New Plymouth, could maintain stronger credit characteristics than the sovereign in a stress scenario.

Economy in recession despite COVID-19 containment

New Plymouth, along with most of New Zealand, has reverted to "Alert Level 1," under which social distancing restrictions (except for international border controls) have been removed and councils have resumed normal services. This follows the country's relative success in containing COVID-19. However, the national economy has taken a severe hit. National GDP contracted 12.2% quarter on quarter in June 2020, which is large in a historical context but comparable to the average for Organization for Economic Cooperation and Development advanced economies. The recovery will be supported by substantial Crown government stimulus and highly accommodative monetary policy.

The New Plymouth district has relatively large oil and gas and dairy sectors, resulting in a local economy that is wealthy but volatile. Oil and gas output could decline in the face of low prices and weak global energy demand, with flow-on effects to local employment. In April 2018, the Crown government announced a moratorium on new offshore oil and gas exploration, with existing permits unaffected. While we do not believe this will have a significant impact in the short term, there will be longer-term ramifications from lower new business investment. New Plymouth has a population of about 82,000, and its GDP per capita was about US\$49,800 in fiscal 2018, significantly higher than the New Zealand average of US\$42,300. However, household income is roughly in line with the national average.

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. Incumbent mayor Neil Holdom was reelected in October 2019 for another three-year term. A new chief financial officer commenced in March 2019, having held various senior roles at Auckland Council. The council prepares 10-year long-term plans every three years and annual plans in the intervening years, in line with statutory requirements. Like most of its peers, New Plymouth borrows only in local

currency, and mitigates its interest-rate risk exposure through hedging.

The institutional framework within 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 disclosure. It allows New Zealand councils to support higher levels of debt than some international peers can tolerate at similar ratings.

COVID-19-related revenue headwinds and capital expenditure (capex) are driving debt higher

We expect New Plymouth's operating balance to dip in fiscal 2021 before recovering during the next few years. The council's "Back On Our Feet" economic support package includes NZ\$8 million in rates deferrals, and commits several million dollars to home insulation loans and various grants and fee reductions. We expect New Plymouth to post moderate after-capital-account deficits, averaging about 9% of total revenues, during the next two years as it continues to roll out a program of infrastructure improvements. However, these deficits should be smaller than that recorded in fiscal 2019 during redevelopment of the terminal at New Plymouth Airport (Papa Rererangi i Puketapu Ltd., or PRIP). We consolidate the airport's financial metrics with those of the parent council, following the council's move to full ownership on July 1, 2017. In July 2020, New Plymouth injected NZ\$22 million of equity into the airport via a debt-to-equity swap. This has no immediate implications for the consolidated financial metrics.

New Plymouth should receive a NZ\$37 million capital grant from the Crown government to fund its replacement of a thermal drying facility. We haven't yet factored this grant revenue, or associated capital spending, into our base-case forecasts as there is uncertainty over timing. The council could also receive further discretionary grants for "shovel-ready" projects from Crown Infrastructure Partners.

New Plymouth has a high degree of fiscal flexibility compared with its domestic and international peers. The council's largest single source of revenue is property rates, which can be adjusted from year to year and are relatively stable through economic cycles. Unlike international peers, New Zealand councils receive little by way of intergovernmental transfers. In addition, we believe that New Plymouth could delay or reschedule nonessential capex if required. The next long-term plan, due in the second quarter of 2021, may provide further clarity on medium-term fiscal direction.

To fund its capital program, we expect New Plymouth's debt burden to rise to about 141% of operating revenues by the end of fiscal 2023, up from 97% at the end of fiscal 2019. We also expect interest expenses to remain low, averaging about 4.3% of operating revenues. New Plymouth had no reported quantifiable contingent liabilities as of June 30, 2018, the latest available data point.

New Plymouth's liquidity remains excellent. Buttressing its liquidity is the council's Perpetual Investment Fund (PIF), which had a balance of about NZ\$307 million at the time of writing. The council has outsourced management of PIF to Mercer (NZ) Ltd. An independent board of guardians monitors PIF, and its assets are diversified across listed equities, fixed income, alternative assets, private equity, and cash. 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 a year. We treat these releases as operating revenues because they are effectively used to subsidize rates.

After applying our standard haircuts to noncash assets, we estimate that New Plymouth's total free cash position--excluding NZ\$24 million of undrawn standby facilities with commercial banks Westpac New Zealand Ltd. and TSB Bank Ltd.--is sufficient to cover about 457% of debt service during the next 12 months. We expect debt-servicing needs to comprise NZ\$15 million in term

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debt maturing in May 2021, NZ\$29 million in short-dated commercial paper, and about NZ\$6 million in interest payments. In addition, the New Zealand Local Government Funding Agency (LGFA) provides New Plymouth, along with most of its domestic peers, with strong access to a well-established source of external liquidity. In our view, LGFA benefits from an extremely high likelihood of extraordinary central government support, and it has helped New Plymouth to both lengthen its maturity profile and reduce its interest expenses.

Key Statistics

Table 1

Key Statistics

(mil. NZ\$)	--Year ended June 30--				
	2019	2020e	2021bc	2022bc	2023bc
Selected Indicators					
Operating revenues	147	149	137	148	155
Operating expenditures	120	127	131	121	128
Operating balance	26	22	6	28	27
Operating balance (% of operating revenues)	17.9	14.8	4.7	18.6	17.6
Capital revenues	7	31	30	11	11
Capital expenditures	56	64	53	54	52
Balance after capital accounts	(22)	(11)	(17)	(15)	(13)
Balance after capital accounts (% of total revenues)	(14.5)	(6.2)	(10.1)	(9.3)	(8.1)
Debt repaid	15	22	15	11	15
Gross borrowings	40	53	32	26	28
Balance after borrowings	3	19	0	0	0
Tax-supported debt (outstanding at year-end)	143	174	190	205	219
Tax-supported debt (% of consolidated operating revenues)	97.5	116.5	139.0	138.4	141.1
Interest (% of operating revenues)	3.9	3.8	4.5	4.5	4.6
National GDP per capita (single units)	62,023	62,615	62,175	66,305	68,886

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. N/A--Not applicable. N.A.--Not available. N.M.--Not meaningful.

Ratings Score Snapshot

Table 2

New Plymouth District Council Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	1
Economy	2

Table 2

New Plymouth District Council Ratings Score Snapshot (cont.)

Key rating factors	Scores
Financial management	2
Budgetary performance	2
Liquidity	1
Debt burden	4
Stand-alone credit profile	aa+
Issuer credit rating	AA

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

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

Related Criteria

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- 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
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- COVID-19: Fiscal Response Will Lift Local And Regional Government Borrowing To Record High, June 9, 2020
- Ratings History List: Asia-Pacific Local And Regional Government Ratings Since 1975, May 29, 2020
- COVID-19's Effects Will Pressure New Zealand Council Ratings, May 24, 2020
- New Zealand 'AA/A-1+' FC And 'AA+/A-1+' LC Ratings Affirmed; Outlook Positive, May 3, 2020
- COVID-19: Emerging Market Local Governments And Non-Profit Public-Sector Entities Face Rising Financial Strains, April 6, 2020
- Default, Transition, and Recovery: 2018 Annual International Public Finance Default And Rating Transition Study, Aug. 19, 2019
- Institutional Framework Assessments For International Local And Regional Governments, July

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4, 2019

- Public Finance System Overview: New Zealand's Institutional Framework For Local And Regional Governments, Nov. 11, 2018

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/Positive/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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