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Research Update:

Tasman District Council Ratings Raised To 'AA/A-1+'; Outlook Stable

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Overview

- We expect Tasman District Council's financial position to structurally improve after the completion of the Waimea Community Dam. Tasman's budgetary performance and contingent liabilities during the next few years will be weaker while the dam is being constructed, but we expect this to be temporary.
- In September 2018, Tasman announced new funding arrangements for the Waimea Community Dam, after it revised up the total project costs. We expect contracts to be executed after a final vote of councilors due to take place around the end of November 2018.
- We are raising our long-term issuer credit rating on Tasman to 'AA' from 'AA-' and affirming our 'A-1+' short-term issuer credit rating.
- The outlook on the long-term rating is stable.

Rating Action

On Oct. 30, 2018, S&P Global Ratings revised its long-term issuer credit rating to 'AA' from 'AA-' on Tasman District Council, a New Zealand local government. At the same time, we affirmed our 'A-1+' short-term issuer credit rating. Following the upgrade, we revised the outlook to stable from positive.

Outlook

The stable outlook reflects our view that Tasman will deliver the Waimea Community Dam within our financial forecasts. We expect that budgetary performance will strengthen in the medium-term after temporarily weakening during construction of the dam. This will limit growth in the council's debt burden.

Upside scenario

Upward pressure on the ratings on Tasman would be capped by our long-term foreign-currency rating on the New Zealand sovereign. We could raise our ratings on Tasman if we raised our rating on the sovereign, and if Tasman's fiscal performance substantially improved, driving its debt levels significantly lower than we currently forecast.

Downside scenario

Downward pressure on the ratings could occur if there were a prolonged deterioration in Tasman's fiscal performance, resulting in persistently large after-capital deficits and debt rising beyond our forecasts. This could occur, for instance, if the dam incurs significant cost overruns. Alternatively, we would lower our ratings on Tasman if we were to lower the rating on the New Zealand sovereign.

Rationale

We have raised our ratings on Tasman District Council after updating our forecasts through fiscal year 2021 (i.e., the year ending June 30, 2021). We expect that Tasman's financial position will structurally improve following completion of the Waimea Community Dam. However, Tasman's budgetary performance will temporarily weaken during the construction phase, and its contingent liabilities will rise. Tasman's ratings are supported by its robust financial management, high level of liquidity, and the country's excellent institutional settings.

Waimea Community Dam to drive higher contingent liabilities and weaker fiscal position, though we expect this to be temporary

The Waimea Community Dam is the largest infrastructure project on the horizon. Tasman will establish a council-controlled organization, Waimea Water Ltd., to build and operate the dam. Tasman will hold a minimum of 51% of voting shares in Waimea Water Ltd. at all times, and appoint four of the seven board directors. Debt and equity funding for the project will be spread across three joint-venture parties: the council, Waimea Irrigators Ltd. (WIL), and Crown Irrigation Investments Ltd. (CIIL, part of the New Zealand central government).

During the next few years, we expect the council's capital contributions to Waimea Water Ltd. to comprise about NZ\$40 million of equity funding and a NZ\$5.75 million loan. We expect that the council's contributions will be partly defrayed by receipt of a NZ\$7 million grant from the Crown's Ministry of the Environment. The council has also applied for a grant from the Crown's Provincial Growth Fund, which could help to further lower its costs if successful. Nelson City Council, Tasman's neighbour, will contribute an additional NZ\$5 million to the project. The remainder of the dam's costs will be paid for by WIL through a capital raising and a loan from CIIL to Waimea Water Ltd. While this loan will be serviced by WIL, we understand that Tasman will act as guarantor, up to a maximum amount of NZ\$29 million. Of the dam's total project costs, about three-quarters has been fixed during the early contractor engagement process. This should lessen the risk of any cost overruns. The council anticipates that final contracts between all joint-venture parties will be signed and executed by mid-December 2018.

We expect Tasman to post relatively large after-capital deficits during the next two years, after which the after-capital position should revert toward balance as the dam nears completion. Like all New Zealand councils, Tasman has recently published a triennial long-term plan setting out its priorities for fiscal years 2019 to 2029. The plan calls for relatively stable levels of capital expenditure, excluding contributions for the Waimea Community Dam, and moderate annual increases in property rates, fees, and charges. The council has introduced two targeted rates to partially fund its contribution to the dam. The estimated outturn for fiscal 2018 was weaker than we expected, in part due to the cost of recovering from ex-tropical cyclones Fehi and Gita in February 2018. Some of these costs were reimbursed by way of operating grants from the New Zealand Transport Agency.

Like with most New Zealand councils, we consider budgetary flexibility to be one of Tasman's key strengths. We estimate that about 79% of its operating revenues are modifiable, which means they can be raised or lowered at the council's discretion. However, once contracts for the dam are executed, we believe that it would be difficult for Tasman to reduce or postpone its capital outlays. We expect Tasman's debt to rise during the next few years. We forecast that the council's tax-supported debt, as a proportion of operating revenues, will reach about 166% by the end of fiscal 2021, up from 142% at the end of fiscal 2018. Similar to other local authorities, Tasman sources the majority of its debt through the New Zealand Local Government Funding Agency. Tasman will also receive a one-off NZ\$10 million interest-free loan from CIIL to help finance the cost of the dam.

Tasman's free cash, liquid financial assets, and available committed bank lines stand at about 127% of the next 12 months' debt service. We expect the council's debt-servicing needs to comprise NZ\$24 million of Local Government Funding Agency loans maturing in March 2019, which the council has prefunded; NZ\$14 million in short-term paper; and about NZ\$7.7 million in interest expenses. We also expect the council to hold cash and cash equivalents averaging about NZ\$16.2 million, and access to two undrawn bank facilities totalling NZ\$42 million. We consider Tasman's access to external liquidity to be satisfactory. New Zealand's capital markets are comparatively liquid, but they lack depth, given their relatively small size. During the severe market dislocation of 2008-2009, some New Zealand councils had difficulty issuing unrated commercial paper.

We believe that Tasman's contingent liabilities are moderate, having risen from last year. As noted above, Tasman intends to provide a guarantee of up to NZ\$29 million for a CIIL loan to Waimea Water Ltd. In addition, the council will be solely responsible for funding any project cost overruns greater than NZ\$3 million. Tasman owns 50% stakes in two council-controlled trading organizations--Nelson Airport Ltd. and Port Nelson Ltd.--with Nelson City Council owning the other 50% of each. We expect both entities to increase their borrowings to finance expansion activities, and we treat Tasman's share of the debts of these self-supporting council-controlled trading organizations as contingent liabilities. We understand that the Waimea Community Dam will be designed to a level that can withstand a 1-in-10,000 year earthquake. The

council did not report any quantifiable contingent liabilities in its financial statements as of June 30, 2018.

A supportive institutional framework, robust management, and solid local economy underpin Tasman's creditworthiness

We consider Tasman's fiscal processes to be credible and well established, with the council preparing long-term plans every three years, annual plans in the intervening years, and audited annual reports, in line with New Zealand requirements. The council's treasury risk-management policy sets prudent limits on external borrowing, liquidity, and interest-rate risk. Tasman borrows only in local currency, in accordance with legislation. Like all New Zealand councils, Tasman is governed by an elected group of councilors, led by a mayor. The councilors delegate day-to-day management to a full-time chief executive. A new chief executive, Janine Dowding, commenced in May 2018. Local elections in New Zealand are held every three years, with the next due in October 2019.

The local economy has been buoyed by rising tourism numbers and construction activity. We estimate that the district's GDP per capita averaged about US\$26,720 during fiscal years 2015 to 2017, based on data from the Ministry for Business, Innovation, and Employment. This figure is lower than the national average of US\$41,300 during the same period. The local economy is somewhat concentrated in the primary sector--the largest industry by employment share (21.6%) is agriculture, forestry, and fishing, which also indirectly supports jobs in other sectors. The district's population was about 51,200 as of June 2017. The local population is aging, in part due to the region being an attractive retirement destination. However, this does not have a material impact on the council's finances as responsibility for the provision of healthcare and pensions falls on the Crown.

The institutional framework within which New Zealand local governments operate is a key factor supporting Tasman's credit profile. We believe this framework is one of the strongest and most predictable globally. It promotes a robust management culture, fiscal discipline, and high levels of financial disclosure. The framework allows New Zealand councils to support higher debt levels than some international peers can tolerate at similar ratings.

Key Statistics

Table 1

Key Statistics						
	--Year ended June 30--					
(mil. NZ\$)	2016	2017	2018E	2019BC	2020BC	2021BC
Selected Indicators						
Operating revenues	104	105	108	109	117	123
Operating expenditures	73	76	99	89	95	96

Table 1

Key Statistics (cont.)						
	--Year ended June 30--					
(mil. NZ\$)	2016	2017	2018E	2019BC	2020BC	2021BC
Operating balance	30	29	9	19	23	27
Operating balance (% of operating revenues)	29.4	27.5	8.7	17.9	19.3	21.7
Capital revenues	9	9	13	13	20	18
Capital expenditures	27	32	41	60	58	46
Balance after capital accounts	12	6	-18	-28	-15	-2
Balance after capital accounts (% of total revenues)	10.7	5.0	-14.9	-22.8	-10.9	-1.4
Debt repaid	12	7	16	49	10	25
Gross borrowings	0	0	43	77	25	27
Balance after borrowings	0	-1	9	0	0	0
Modifiable revenues (% of operating revenues)	79.9	80.7	79.4	80.8	77.9	77.2
Capital expenditures (% of total expenditures)	26.9	30.0	29.1	40.4	38.0	32.5
Tax-supported debt (outstanding at year-end)	133	126	154	187	202	204
Tax-supported debt (% of consolidated operating revenues)	128.5	120.6	141.6	172.1	172.3	165.6
Interest (% of operating revenues)	8.3	7.1	6.7	7.3	7.3	7.0
Local GDP per capita (single units)	36,962	38,321	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	Average
Financial management	Strong
Budgetary flexibility	Strong
Budgetary performance	Strong
Liquidity	Strong
Debt burden	High
Contingent liabilities	Moderate

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 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'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

Upgraded; CreditWatch/Outlook Action; Ratings Affirmed	To	From
Tasman District Council Issuer Credit Rating	AA/Stable/A-1+	AA-/Positive/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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