10.4. Investment and Loan Borrowings Report as at 31 January 2023

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ENDORSED BY: Margaret Palmer, Director Corporate Services

ATTACHMENTS:
1. North Sydney Monthly Investment Report January 2023 [**10.4.1** - 20 pages]

PURPOSE:

The report provides details of the performance of Council's investment portfolio and borrowing limits for the period ending 31 January 2023.

EXECUTIVE SUMMARY:

Investment Portfolio

Independent advice regarding North Sydney Council's Investments is provided by Imperium Markets. This provides a layer of governance and expert advice in addition to Council's policy and procedures.

The Investment Portfolio (excluding cash balances) held for the period ending 31 January 2023 had a market value of $138,899,262. The annualised returns were 2.50%.

Cash deposits at call were $9,641,698 with $8,800,000 of these held in interest bearing at-call accounts. $841,698 cash is held in Council's interest-bearing transaction account with the Commonwealth Bank to meet day-to-day operational needs. This amount includes deposits that settled after close of business.

The investment portfolio is managed to ensure adequate liquidity to meet operational requirements, and to fund outflows on major projects. Cashflow is monitored and assessed on an on-going basis.

Actual year to date returns for cash and investments to 31 January 2023 are $1,882,000, compared to a year-to-date budget of $753,000.

The Reserve Bank of Australia (RBA) Board continued to signal its intention to increase interest rates.

Borrowings

Loan Facility for Council Projects

Council entered into a fixed interest loan of $9.5 million with quarterly interest and principal payments on 31 July 2018. The principal outstanding as at 31 January 2023 is $5,691,792.

North Sydney Olympic Pool Redevelopment (NSOP)

In January 2022 Council established a $31 million TCorp loan facility to partially fund the redevelopment of North Sydney Olympic Pool. Drawdown on the facility was processed on 28 April 2022, with an interest rate of 4.24%. The funds were restricted and will be released as required to fund cash outflows. The principal outstanding as at 31 January 2023 is $30,499,987.

FINANCIAL IMPLICATIONS:

Council's total investment portfolio performance for the financial year to date is 2.50% annualised. The actual year to date returns for cash and investments to 31 January 2023 were $1,882,000, compared to a year-to-date budget of $753,000.

RECOMMENDATION:
1.THAT the report on Investments and Loan Borrowings held on 31 January 2023, prepared in accordance with clause 212 of the Local Government (General) Regulation 2021, be received.

LINK TO COMMUNITY STRATEGIC PLAN

The relationship with the Community Strategic Plan is as follows:

5. Our Civic Leadership
5.1 Lead North Sydney's strategic direction
5.2 Council is well governed, and customer focused

BACKGROUND

The Responsible Accounting Officer must provide Council with a monthly report detailing all funds:

a. Invested under Section 625 of the Local Government Act 1993. This report must include certification that the investments have been made in accordance with the Act and the Regulations made thereunder, the revised Investment Order issued by the Minister for Local Government and Council's Financial Investment Policy.
b. Borrowed under Section 624 of the Local Government Act. This report must comply with the borrowings Order issued by the Minister for Local Government and Council's Debt Management Policy.

CONSULTATION REQUIREMENTS

Community engagement is not required.

DETAIL

Investment Portfolio

The following table provides details of the performance of Council's investment portfolio (excluding cash deposits) against the benchmark for the month of January 2023 and annualised for the year-to-date 31 January 2023 (including investments that have matured prior to 31 January 2023).

	January 2023	Annualised YTD as at 31 January 2023
Actual Return	0.21%	2.50%
Benchmark	0.27%	3.18%
Variance	-0.06%	-0.68%

The portfolio underperformance as compared to the benchmark is due to recent sharp rises in the RBA official cash rate and long-term investments placed when inflation expectations were low, before those increases were made. Council's investment advisor, in the attached report, expects this relative underperformance to be temporary. The report further notes that North Sydney Council’s deposits portfolio ranks among the best performing when compared to other NSW councils.

Asset Type	**Market Value as at 31 January 2023**	**Portfolio Breakdown as at 31 January 2023**
Term Deposits	$127,250,000	85.67%
Cash	$9,641,698	6.49%
Fixed Bonds	$9,000,000	6.06%
Floating Rate Notes (FRNs)	$2,649,262	1.78%
	$148,540,960	**100.00%**

Council’s average duration of term deposits, which comprise 85.67% of the investment portfolio, was approximately 375 days as at 31 January 2023.

All funds have been invested in accordance with the Act and the Regulations made thereunder. Council’s investment portfolio complies with the revised Investment Order issued by the Minister for Local Government, which places restrictions on the type of investments permitted. Funds used also comply with the credit quality conditions contained in Council’s loan agreement with TCorp.

Council continues to seek independent advice for investments and is actively managing the portfolio to ensure that returns are maximised, considering diversification and risk. A complete analysis of the performance is covered in the Monthly Investment Report (Attachment 1) prepared by Council’s investment advisor Imperium Markets. The report contains advice about optimal investment options but also notes that Council’s scope to act on that advice is limited by its cash flow requirements. Council has considerable requirements for short term investments to fund its ambitious Capital Works budget ($95 million for 2022/23).

Council’s Investment Policy and the contractual requirements of the loan agreement with TCorp are biased towards major and large institutions. This limits the scope to invest in regional institutions. The loan agreement with TCorp prohibits investing with non-rated institutions. Staff monitors rates available from rated regional institutions (as advised by Imperium) but finds that major and large institutions consistently outperform them in the shorter terms that we currently require.

The actual investment returns for the year-to-date 31 January 2023 have been reviewed and are $1,129,000 more than the year-to-date budgeted estimate. This result is driven by higher-than-forecast interest rates, and a higher-than-expected cash balance due to (i) delays to capital projects caused by wet weather and (ii) Covid lockdowns in the 2021/22 Financial Year.

Summary of Returns from Investments (includes Fair Value adjustments)

Year	Original Annual Budget	Revised Annual Budget	YTD Budget (January)	YTD/Annual Actual (January)	YTD/Annual Actual FV adjustments (January)	YTD Budget to Actual Variance (January)
2022/23	**$1,290,000**	**$1,290,000**	**$753,000**	**$1,875,000**	**$7,000**	**$1,129,000**
2021/22	$1,100,000	$1,300,000		$1,244,337	-$64,865	$1,179,472
2020/21	$1,350,000	$1,350,000		$1,222,664	$93,735	-$33,601
2019/20	$1,350,000	$1,529,055		$1,896,660	-$4,944	$362,661

Floating Rate Notes (FRN's) are required to be revalued each month using the Fair Value (FV) method which is an estimate in time of the potential market value of the investment. As of 31 January 2023, the YTD movement of FRN's has been an increase of $7,000.

Financial Investment Policy

As at the end of January, all categories were within the Policy limits for credit ratings and the portfolio remains well diversified, with all asset credit quality classified as BBB or higher. The maximum holding limit in each rating category and the target credit quality weighting for Council's portfolio are as per the following table:

Long Term Rating Range (Standard & Poors)	Invested as of 31 January 2023	Maximum Policy Holding	Distribution as of 31 January 2023
AA Category	$99,391,698	100.00%	66.91%
A Category	$35,750,767	60.00%	24.07%
BBB Category	13,398,495	35.00%	9.02%
Unrated ADIs (NR)	$0	10.00%	0.00%

Credit Quality Limits in TCorp Loan Agreement

The TCorp Loan Agreement imposes credit quality limits additional to Council's Financial Investment Policy. In cases where the loan agreement imposes a credit quality limit more conservative than the Financial Investment Policy, Council's contractual obligations will prevail and the more conservative limit will be applied. The maximum holding limit in each rating category and the target credit quality weighting for Council's portfolio are as per the following table:

Long Term Rating Range (Standard and Poors/Moody's)	Invested as at 31 January 2023	Maximum Holding Allowed	Distribution as at 31 January 2023
AA+ to AA-/Aa1 to Aa3 Category	$99,391,698	100%	66.91%
A+ to A/A1 to A2 Category	$35,750,767	100%	24.07%
A-/A3 Category	$0	40%	0.00%
BBB+/Baa1 Category	$10,000,000	20%	6.73%
BBB/Baa2 Category	$3,398,495	10%	2.29%
BBB-/Baa3 Category	$0	5%	0.00%
Unrated	$0	0%	0.00%

The maximum counterparty limits and the target allowed limit are as per the following table:

Institution	Long Term Rating Range (Standard and Poors/Moody's)	Invested as at 31 January 2023	Maximum Holding Allowed	Distribution as at 31 January 2023
AMP Bank Ltd	BBB/Baa2 Category	$2,000,000	5%	1.35%
BOQ Ltd	BBB+/Baa1 Category	$10,000,000	10%	6.73%
Commonwealth Bank of Australia	AA+ to AA-/Aa1 to Aa3 Category	$40,141,698	100%	27.02%
ICBC Sydney Branch	A+ to A/A1 to A2 Category	$17,000,000	100%	11.44%
NAB Ltd	AA+ to AA-/Aa1 to Aa3 Category	$29,000,000	100%	19.52%
Newcastle Permanent	BBB/Baa2 Category	$1,398,495	5%	0.94%
Northern Territory Treasury	AA+ to AA-/Aa1 to Aa3 Category	$9,000,000	100%	6.06%
Suncorp Bank Ltd	A+ to A/A1 to A2 Category	$18,750,767	100%	12.62%
Westpac Bank Ltd	AA+ to AA-/Aa1 to Aa3 Category	$21,250,000	100%	14.31%

Loan Borrowings

Council's Loan Borrowing Policy provides the framework for Council's borrowing activities and defines key responsibilities and the operating parameters within which borrowing and related risk management activities are carried out.

The Policy's objective is to control Council's exposure to movements in interest rates through the application of fixed, floating or a combination thereof to maintain its risk averse strategy.

Loan borrowings are undertaken in line with the following principles:

a) That the capital cost of infrastructure be recognised over the period during which the benefits will be enjoyed.
b) That loan funds are a resource to fund the replacement and upgrading of existing infrastructure and fund the creation of new infrastructure.
c) That loan funds will be limited to:
   - acquisition or enhancement of income producing assets;
   - construction and/or upgrading of buildings; and
   - infrastructure assets that have a life expectancy of greater than 10 years.

Council has two debt facilities:

Alexander Street Carpark and On-street Carparking Management System Loan

This is a fixed loan financing option, fully amortising the drawn down amount of $9,500,000 over 10 years, fixed interest rate with quarterly repayments of interest and principal.

The loan details are:

Loan amount:	$ 9,500,000.00			
Loan term:	10 years			
From:	31/07/2018			
To:	31/07/2028			
Interest rate:	4.02%p.a.(fixed)			
Repayment:	**Quarterly**			
Dates	**Principal Outstanding**	**Interest**	**Principal**	**Payment**
1/07/2022	$6,373,191.95			
29/07/2022	$6,147,427.51	$63,875.10	$225,764.44	$ 289,639.54
28/10/2022	$5,921,431.53	$63,643.56	$225,995.98	$ 289,639.54
27/01/2023	$5,691,791.50	$59,999.51	$229,640.03	$ 289,639.54
28/04/2023	$5,456,690.24	$54,538.28	$235,101.26	$ 289,639.54

Loan Funded Capital Projects

Project 1: Upgrading the Car Park in Alexander Street, Crows Nest
$5 million loan was sourced to fund project.

Current length of Loan as per the Long-Term Financial Plan (LTFP): 10 years to 2028

Project 2: Upgrading of On-Street Parking Management System
$4.5 million loan was sourced to fund project.

Current length of Loan as per LTFP: 10 years to 2028

Loan for North Sydney Olympic Pool Redevelopment

In January 2022 Council established a $31 million TCorp loan facility to partially fund the redevelopment of North Sydney Olympic Pool. Drawdown on the facility was processed on 28 April 2022. The funds were restricted and will be released as required to fund project cash outflows.

This loan is a fixed loan financing option, fully amortising the drawn down amount of $31,000,000 over 20 years, fixed interest rate with semi-annual repayments of interest and principal.

The loan details are:

Loan amount:	$ 31,000,000.00			
Loan term:	20 years			
From:	28/04/2022			
To:	28/04/2042			
Interest rate:	4.24%p.a.(fixed)			
Repayment:	**Semi-Annual**			
Dates	**Principal Outstanding**	**Interest**	**Principal**	**Payment**
01/07/2022	$31,000,000			
28/10/2022	$30,499,987	$657,200	$500,013	$1,157,213
28/04/2023	$29,989,375	$646,600	$510,613	$1,157,213

Monthly Investment Report

January 2023

IMPERIUM MARKETS

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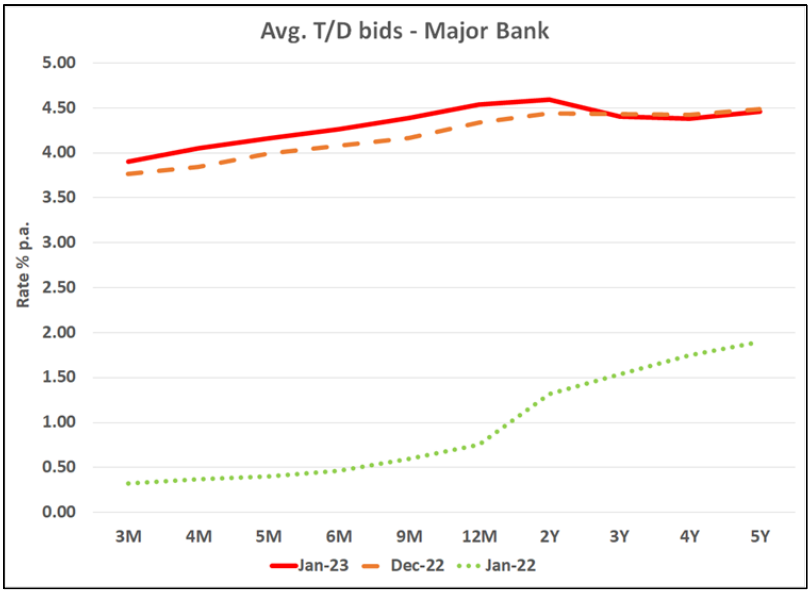
Market Update Summary

Risk markets were aided in January as recent data indicated there were signs the global economy may be weathering inflation better than previously anticipated. Several global central banks also hinted they may pause their aggressive rate hike cycles in the near future. Domestically, the labour market remains tight, but timely indicators of labour demand are off their peaks as labour supply has normalised and frictions associated with rapid employment growth out of pandemic impacts moderate. Although labour costs pressures are evident in the latest CPI figures for Q4 2022, there are reasons to be optimistic that some stabilisation in wages growth can occur without a sharply higher unemployment rate, including the normalisation in labour supply. For now, the RBA continues to signal that it expects to increase interest rates further over the period ahead, with up to 2-3 hikes already largely priced into the market by Q2-Q3 2023, taking the cash rate up to 3¾%. Thereafter, noting the lags in monetary policy, a pause around the end of Q2-Q3 is likely whilst the RBA monitors the economic data.

Despite more rate rises on the horizon, given an upward sloping deposit curve, maintaining a slightly longer average duration position on deposits will continue to outperform shorter durations. The deposit market has largely already factored in the current rate hike cycle, reflected by the flattening of the curve demonstrated by the longer-term tenors (+2yrs) over the past few months (the market is also factoring in a recession over coming years). Interestingly, amongst the major banks, some 2-5 year deposit rates are now being offered slightly below 12 month rates:



Source: Imperium Markets

'New' investments above 4¼-4½% p.a. is now possible if Council can place the majority of its surplus funds for terms of 12 months to 2 years. *With recessionary fears being priced in coming years, investors may take an insurance policy by investing across 3-5 year fixed deposits and locking in rates above 4½% p.a. (small allocation only), ahead of any potential rate cuts should inflation be under control.*

Council's Portfolio & Compliance

Asset Allocation

As at the end of January 2023, the portfolio was mainly directed to fixed term deposits (86%). The remaining portfolio is directed to FRNs (2%), fixed bonds (6%) and overnight cash accounts (6%).

Senior FRNs are now becoming more attractive as spreads have widened over the past year – new issuances should now be considered again on a case by case scenario. In the interim, fixed deposits for 12 months to 3 years appear quite appealing following the spike in medium-to longer-term yields during the rate hike cycle.

With recessionary fears being priced in coming years, those investors that can allocate longer-term surplus funds may take an insurance policy by investing across 3-5 year fixed deposits, locking in and targeting yields above 4½% p.a.

Term to Maturity

Overall, the portfolio remains lightly diversified from a maturity perspective. Around 22% of assets is directed to medium-term assets (2-5 years), which has resulted in strong outperformance during the challenging economic environment. There is still high capacity to invest in the short-medium term horizon (1-2 years), with approximately $85m at month-end.

Where liquidity permits, we recommend new surplus funds be directed to 1-2 year horizon given this is where the most attractive value can be found. We suggest this be allocated to any remaining attractive fixed term deposits.

However in the interim, given the large upcoming capital expenditure of $94.4m flagged for FY2023, Council is likely to invest across shorter-tenors to match the capital program's cash flow requirements.

Compliant	Horizon	Invested ($)	Invested (%)	Min. Limit (%)	Max. Limit (%)	Available ($)
✓	0 - 90 days	$43,641,698	29.38%	10%	100%	$104,899,262
✓	91 - 365 days	$53,250,000	35.85%	20%	100%	$95,290,960
✓	1 - 2 years	$19,250,767	12.96%	0%	70%	$84,727,905
✓	2 - 5 years	$32,398,495	21.81%	0%	50%	$41,871,985
✓	5 - 10 years	$0	0.00%	0%	25%	$37,135,240
		$148,540,960	**100.00%**			

IMPERIUM MARKETS

Counterparty

As at the end of January, all individual limits comply with the Policy. Exposures to individual ADIs are driven by the portfolio's movements throughout any month. Overall, the portfolio is well diversified across the investment grade spectrum, with no exposure to the unrated ADIs.

Compliant	Issuer	Rating	Invested ($)	Invested (%)	Max. Limit (%)	Available ($)
✓	CBA	AA-	$40,141,698	27.02%	30.00%	$4,420,590
✓	NAB	AA-	$29,000,000	19.52%	30.00%	$15,562,288
✓	NTTC Treasury	AA-	$9,000,000	6.06%	30.00%	$35,562,288
✓	Westpac	AA-	$21,250,000	14.31%	30.00%	$23,312,288
✓	Suncorp	A+	$18,750,767	12.62%	15.00%	$3,530,377
✓	ICBC Sydney	A	$17,000,000	11.44%	15.00%	$5,281,144
✓	BOQ	BBB+	$10,000,000	6.73%	10.00%	$4,854,096
✓	AMP Bank	BBB	$2,000,000	1.35%	10.00%	$12,854,096
✓	Newcastle PBS	BBB	$1,398,495	0.94%	10.00%	$13,455,601
			$148,540,960	**100.00%**		

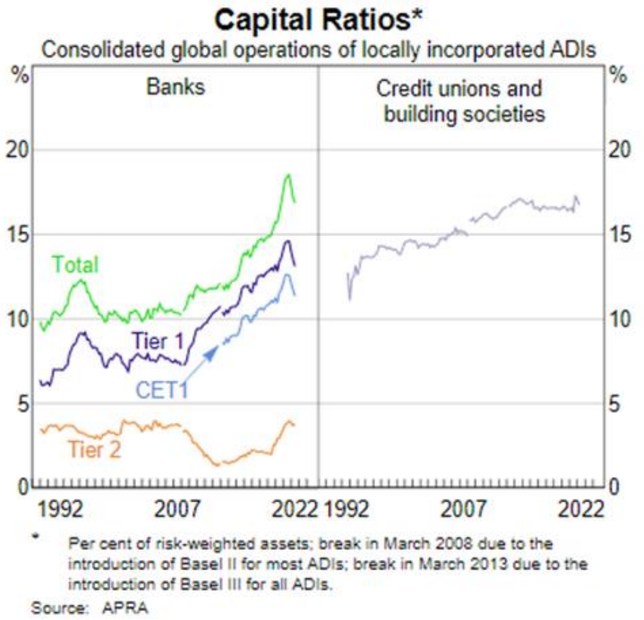
In late June 2022, Standard & Poor's downgraded Suncorp-Metway from AA- to A+ (negative watch). Suncorp recently announced that it is undertaking a strategic review of its banking operations. The downgrade reflects S&P's view that the Suncorp Group's likelihood of support for the bank had "*slightly*" diminished and that it was no longer a core part of the Group. In July 2022, ANZ (AA-) announced it was putting a bid to buy Suncorp's banking division for ~$3.9bn. Should that takeover be formalised, Suncorp-Metway's (A+) current credit rating is likely to be upgraded to ANZ's (AA-).

We remain supportive of the regional and unrated ADI sector (and have been even throughout the post-GFC period). They continue to remain solid, incorporate strong balance sheets, while exhibiting high levels of capital – typically, much higher compared to the higher rated ADIs. Some unrated ADIs have up to 25-40% more capital than the domestic major banks, and well above the Basel III requirements.

Overall, the lower rated ADIs (BBB and unrated) are generally now in a better financial position then they have been historically (see the Capital Ratio figure below). APRA's outgoing Chair Wayne Byres recently noted that the Common Equity Tier 1 capital of Australian banks now exceeds a quarter of a trillion dollars. It has increased by $110 billion, or more than 70%, over the past eight years. Over the same time, banks' assets have grown by 44%. Some of the extra capital is supporting growth in the banking system itself but clearly, there has been a strengthening in overall resilience and leverage in the system is lower.

We believe that deposit investments with the lower rated ADIs should be considered going forward, particularly when they offer 'above market' specials. Not only would it diversify the investment portfolio and reduce credit risk, it would also improve the portfolio's overall returns. The lower rated entities are generally deemed to be the more 'ethical' ADIs compared to the higher rated ADIs.

In the current environment of high regulation and scrutiny, all domestic (and international) ADIs continue to carry high levels of capital. There is minimal (if any) probability of any ADI defaulting on their deposits going forward – this was stress tested during the GFC and the pandemic period. **APRA's mandate is to "*protect depositors*" and provide "*financial stability*".**



Credit Quality

The portfolio remains well diversified from a credit ratings perspective, with all assets classified as investment grade (rated BBB- or higher). As at the end of January 2023, all categories were within the Policy limits:

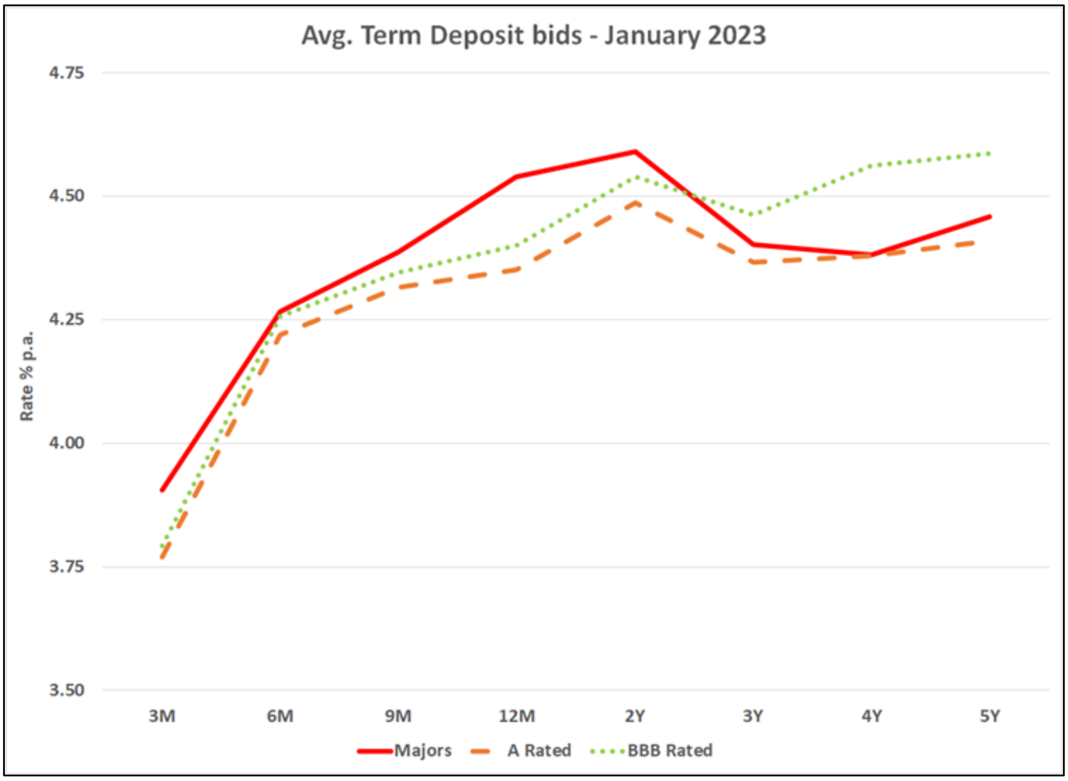
Compliant	Credit Rating	Invested ($)	Invested (%)	Max. Limit (%)	Available ($)
✓	AA Category	$99,391,698	66.91%	100%	$49,149,262
✓	A Category	$35,750,767	24.07%	60%	$53,373,809
✓	BBB Category	$13,398,495	9.02%	35%	$38,590,841
✓	Unrated ADIs	$0	0.00%	10%	$14,854,096
		$148,540,960	**100.00%**		

Pre-pandemic (March 2020), a 'normal' marketplace meant the lower rated ADIs (i.e. BBB category) were offering higher rates on term deposits compared to the higher rated ADIs (i.e. A or AA rated). But due to the cheap funding available provided by the RBA via their Term Funding Facility (TFF) since mid-2020[1], allowing the ADIs to borrow as low as 0.10% p.a. fixed for 3 years, those lower rated ADIs (BBB rated) did not require deposit funding from the wholesale deposit from the likes of Council. Given the higher rated banks had more capacity to lend (as they have a greater pool of mortgage borrowers), they subsequently were offering higher deposit rates. In fact, some of the lower rated banks were not even offering deposit rates at all. As a result, most investors placed a higher proportion of their deposit investments with the higher rated (A or AA) ADIs over the past three years.

In the interim, the ‘abnormal’ marketplace still largely exists, with the higher rated banks (majors) often paying a higher rate of return over the lower rated institutions across various parts of the curve on any particular day. Over the next few years, with the RBA now removing these cheap borrowing facilities, this should result in some of the lower rated banks (BBB rated) starting to become more competitive as the market starts to 'normalise'. Council should have a larger opportunity to invest a higher proportion of its surplus funds with the lower rated institutions (up to Policy limits), from which the majority are not lending to the Fossil Fuel industry or considered more ‘ethical’.

We are slowly seeing this trend emerge, as has been the case in recent months:

[1] The RBA’s Term Funding Facility (TFF) allowed the ADI to borrow as low as 0.10% fixed for 3 years: https://www.rba.gov.au/mkt-operations/term-funding-facility/overview.html



Source: Imperium Markets

Performance

Council's performance for the month ending 31 January 2023 is summarised as follows:

Performance (Actual)	1 month	3 months	6 months	FYTD	1 year	2 years
Official Cash Rate	0.26%	0.75%	1.32%	1.44%	1.56%	0.83%
AusBond Bank Bill Index	0.27%	0.77%	1.31%	1.44%	1.52%	0.77%
Council's T/D Portfolio	0.21%	0.62%	1.17%	1.31%	1.80%	1.59%
Council's FRN Portfolio	0.36%	1.05%	1.89%	2.11%	2.67%	2.14%
Council's Bond Portfolio	0.10%	0.29%	0.59%	0.69%	1.17%	1.11%
Council's Portfolio^	**0.21%**	**0.61%**	**1.15%**	**1.28%**	**1.77%**	**1.57%**
Outperformance	**-0.06%**	**-0.16%**	**-0.17%**	**-0.16%**	**0.26%**	**0.80%**

^Total portfolio performance excludes Council's cash account holdings. Overall returns would be lower if cash was included.

Performance (% p.a.)	1 month	3 months	6 months	FYTD	1 year	2 years
Official Cash Rate	3.10%	3.02%	2.64%	2.45%	1.56%	0.83%
AusBond Bank Bill Index	3.18%	3.08%	2.63%	2.46%	1.52%	0.77%
Council's T/D Portfolio	2.56%	2.48%	2.34%	2.23%	1.80%	1.59%
Council's FRN Portfolio	4.31%	4.21%	3.79%	3.60%	2.67%	2.14%
Council's Bond Portfolio	1.17%	1.17%	1.17%	1.17%	1.17%	1.11%
Council's Portfolio^	**2.50%**	**2.42%**	**2.29%**	**2.19%**	**1.77%**	**1.57%**
Outperformance	**-0.68%**	**-0.65%**	**-0.34%**	**-0.27%**	**0.26%**	**0.80%**

^Total portfolio performance excludes Council's cash account holdings. Overall returns would be lower if cash was included.

For the month of January, the total investment portfolio (excluding cash) provided a strong return of +0.21% (actual) or +2.50% p.a. (annualised), underperforming the benchmark AusBond Bank Bill Index return of +0.27% (actual) or +3.18% p.a. (annualised). This relative 'underperformance' has been due to the unexpected aggressive rate hikes undertaken by the RBA. Whilst this 'underperformance' may continue in the short-term, we do anticipate this to be temporary. Council should also remind itself it has consistently 'outperformed' over longer-term time periods as demonstrated by the longer-term returns of the overall investment portfolio.

We are pleased that North Sydney Council remains amongst the best performing Councils in the state of NSW where deposits are concerned. We have been pro-active in our advice about protecting interest income for many years and encouraged to maintain a long duration position. This is now reflected by the strong consistent performance of the investment portfolio over the longer term horizons.

Council's Term Deposit Portfolio & Recommendation

As at the end of January 2023, Council's deposit portfolio was yielding **2.59% p.a.** (up 10bp from the previous month), with a weighted average duration of around 375 days (~12 months). We recommend Council maintains an average duration above 12 months, should cash flows allow.

Over a longer-term cycle, investors are rewarded if they can continue to maintain a slightly longer average duration. In a 'normal' marketplace, yields at the long-end are generally offered at a slight premium over shorter tenors.

At the time of writing, we see value in:

	LT Credit Rating	Term	T/D Rate
ING	A	3 years	4.62% p.a.
ING	A	2 years	4.61% p.a.
CBA	AA-	2 years	4.64% p.a.
BoQ	BBB+	2 years	4.55% p.a.
Westpac	AA-	2 years	4.50% p.a.
NAB	AA-	2 years	4.50% p.a.
Hume Bank	BBB+	2 years	4.50% p.a.
Suncorp	A+	2 years	4.45% p.a.

The above deposits are suitable for investors looking to maintain diversification and lock-in a premium compared to purely investing short-term. For terms under 12 months, we believe the strongest value is currently being offered by the following ADIs (dependent on daily funding requirements):

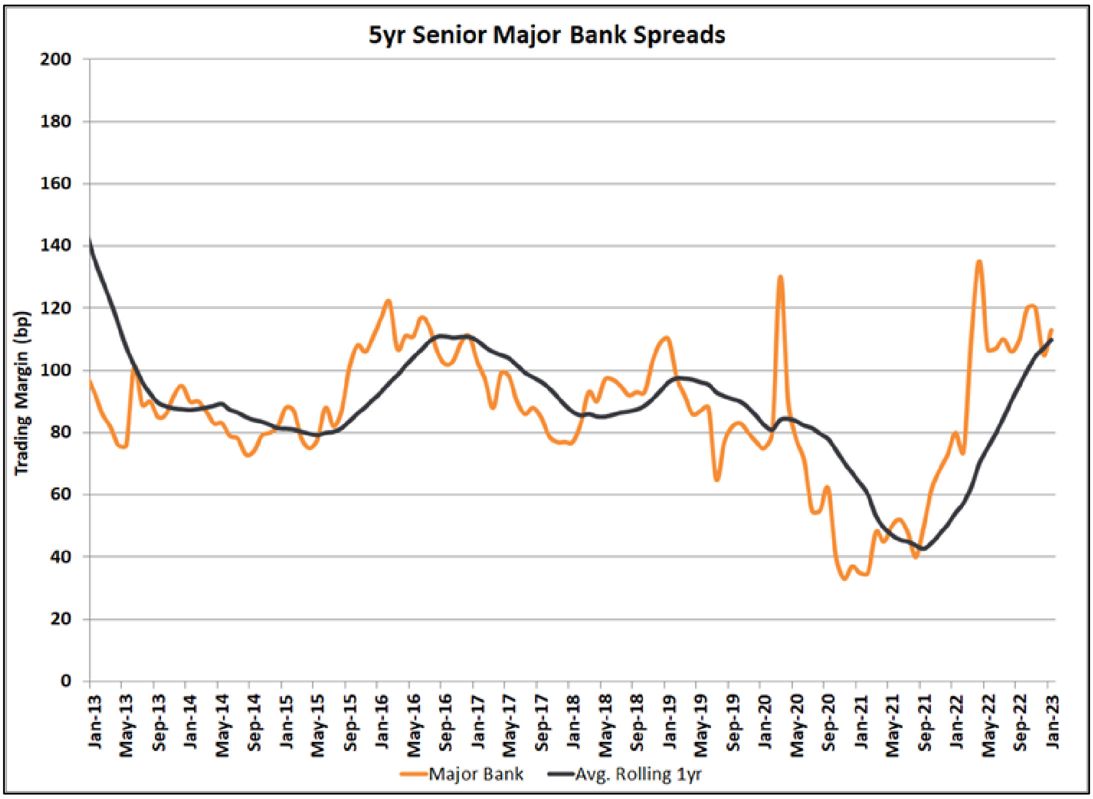
ADI	LT Credit Rating	Term	T/D Rate
CBA	AA-	12 months	4.69% p.a.
NAB	AA-	12 months	4.60% p.a.
Westpac	AA-	12 months	4.59% p.a.
ING	A	12 months	4.55% p.a.
Suncorp	A+	12 months	4.50% p.a.
BoQ	BBB+	12 months	4.50% p.a.
Hume Bank	BBB+	12 months	4.50% p.a.
CBA	A+	6 months	4.41% p.a.
BoQ	BBB+	6 months	4.40% p.a.
CBA	AA-	3 months	4.13% p.a.

If Council does not require high levels of liquidity and can stagger its investments longer-term, it will be rewarded over coming years if it can roll for an average min. term of 12 months - 2 years (this is where we see current value), yielding, on average, up to ¼% p.a. higher compared to those investors that entirely invest in short-dated deposits (under 6-9 months).

With recessionary fears being priced in coming years, assuming inflation is under control, Council may consider taking an insurance policy by investing across 3-5 year fixed deposits and locking in rates above 4½ p.a., ahead of any potential future rate cuts.

Senior FRNs Review

Over January, amongst the senior major bank FRNs, physical credit securities widened up to 10bp at the long-end of the curve. This was mainly driven by CBA's (AA-) dual 3 and 5 year primary issuance at +90bp and +115bp respectively. Major bank senior securities are now looking fairly attractive again in a rising rate environment (5 year margins above the +110bp level):



Source: IBS Capital

During January, there were other noticeable new primary issuances from:

- ICBC, Sydney Branch (A) 3 year senior 'green' FRN at 103bp
- Rabobank, Australian Branch (A+) 5 year senior FRN at +118bp
- Bendigo-Adelaide (BBB+) 4 year senior FRN at +135bp
- BoQ (BBB+) 4 year senior FRN at +135bp
- Great Southern Bank (BBB) 4 year senior FRN at +165bp

Amongst the "A" rated sector, the securities were marked up to 5bp wider at the 5 year part of the curve, whilst the "BBB" rated sector was marked up to 15bp tighter (on the 3 year part of the curve) due to recent new issuances.

Credit securities are looking much more attractive given the widening of spreads in 2022. FRNs will continue to play a role in investor's portfolios mainly on the basis of their liquidity and the ability to roll down the curve and gross up returns over ensuing years (in a relatively stable credit environment).

Senior FRNs (ADIs)	31/01/2023	31/12/2022
"AA" rated – 5yrs	+113bp	+105bp
"AA" rated – 3yrs	+88bp	+82bp
"A" rated – 5yrs	+130bp	+125bp
"A" rated – 3yrs	+103bp	+105bp
"BBB" rated – 3yrs	+150bp	+165bp

Source: IBS Capital

We now generally recommend switches ('benchmark' issues only) into new primary issues, out of the following senior FRNs that are maturing:

- **On or before early 2025 for the "AA" rated ADIs (domestic major banks)**;
- On or before early 2024 for the "A" rated ADIs; and
- Within 6-9 months for the "BBB" rated ADIs (consider case by case).

Investors holding onto the above senior FRNs ('benchmark' issues only) in their last few years are now generally holding sub-optimal investments and are not maximising returns by foregoing realised capital gains. In the current challenging economic environment, any boost in overall returns should be locked in when it is advantageous to do so, particularly as switch opportunities become available.

Primary (new) FRNs are now looking more appealing and should be considered on a case by case scenario.

Council's Senior FRNs Sale/Switch Recommendations

We recommend Council retains its remaining two FRNs at this stage. We will inform Council when there is an opportunity to sell these assets to boost the overall returns of the investment portfolio.

Council's Senior Bonds

During October 2020, Council placed two parcels of $3m (totalling $6m) with the Northern Territory Treasury Corporation (NTTC), locking in yields of 0.90% p.a. and 1.00% p.a. for a 4 and 5 year term respectively. In August 2021, it placed another $3m parcel with NTTC (AA-), locking in a yield of 1.50% p.a. for a 5 year term.

Council received the full rebated commission of 0.25% on the total face value of investments (i.e. $9m x 0.25% = $22,500) as it was introduced by Imperium Markets. We believe these investments were prudent at the time of investment especially after the rate cut delivered in early November 2020 and the RBA's forward guidance on official interest rates (no rate rises "*until at least 2024*").

The NTTC bonds are a 'retail' offering and not 'wholesale' issuances. Given the lack of liquidity and high penalty costs if they were to be sold/redeemed prior to the maturity date, they are considered to be a hold-to-maturity investment and will be marked at par value ($100.00) throughout the term of investment.

Senior Fixed Bonds – ADIs (Secondary Market)

As global inflationary pressures have escalated, this has seen a significant lift in longer-term bond yields (valuations fell) as markets have reacted accordingly.

This has resulted in some opportunities in the secondary market. We currently see value in the following fixed bond lines, with the majority now being marked at a significant discount to par (please note supply in the secondary market may be limited on any day):

ISIN	Issuer	Rating	Capital Structure	Maturity Date	~Remain. Term (yrs)	Fixed Coupon	Indicative Yield
AU3CB0255776	ING	AAA	Covered	07/09/2023	0.60	3.00%	4.21%
AU3CB0258465	Westpac	AA-	Senior	16/11/2023	0.79	3.25%	4.17%
AU3CB0265403	Suncorp	AA-	Senior	30/07/2024	1.50	1.85%	4.53%
AU3CB0265593	Macquarie	A+	Senior	07/08/2024	1.55	1.75%	4.53%
AU3CB0265718	ING	AAA	Covered	20/08/2024	1.55	1.45%	4.39%
AU3CB0266179	ANZ	AA-	Senior	29/08/2024	1.59	1.55%	4.30%
AU3CB0266377	Bendigo	BBB+	Senior	06/09/2024	1.62	1.70%	4.57%
AU3CB0268027	BoQ	BBB+	Senior	30/10/2024	1.76	2.00%	4.65%
AU3CB0269710	ANZ	AA-	Senior	16/01/2025	1.98	1.65%	4.37%
AU3CB0269892	NAB	AA-	Senior	21/01/2025	1.98	1.65%	4.32%
AU3CB0270387	Macquarie	A+	Senior	12/02/2025	2.05	1.70%	4.56%
AU3CB0287415	Westpac	AA-	Senior	17/03/2025	2.14	2.70%	4.30%
AU3CB0291508	Westpac	AA-	Senior	11/08/2025	2.54	3.90%	4.34%
AU3CB0291672	CBA	AA-	Senior	18/08/2025	2.56	4.20%	4.30%
AU3CB0280030	BoQ	BBB+	Senior	06/05/2026	3.26	1.40%	4.97%
AU3CB0234623	CBA	AA-	Senior	11/06/2026	3.35	4.20%	4.47%
AU3CB0282358	ING	AAA	Covered	19/08/2026	3.56	1.10%	4.61%
AU3CB0284149	BoQ	BBB+	Senior	27/10/2026	3.75	2.10%	4.89%
AU3CB0286037	Westpac	AA-	Senior	25/01/2027	4.00	2.40%	4.55%

Economic Commentary

Risk markets were aided in January as recent data indicated there were signs the global economy may be weathering inflation better than previously anticipated. Several global central banks also hinted they may pause their aggressive rate hike cycles in the near future.

Across equity markets, the S&P 500 Index rose +6.18%, while the NASDAQ surged +10.68%. Europe's main indices also gained, led by France's CAC (+9.40%), Germany's DAX (+8.65%) and UK's FTSE (+4.29%).

The US core CPI index, which excludes volatile food and energy items, rose +0.3% m/m, in line with the consensus. Encouragingly for the Fed, the core PCE printed +4.4% y/y, the lowest since October 2021, generating a 3-month annualised rate to +2.9% from +3.5%, the lowest read since January 2021.

US Q4 GDP beat expectations at +2.9% quarter annualised versus +2.6% expected. US headline retail was -1.1% m/m versus -0.9% expected. The important core control measure was also weak at -0.7% m/m against -0.3% expected.

The Bank of Canada (BoC) explicitly signalled a pause to the hiking cycle after hiking by 25bp during the month. Their explicit pause signal has many thinking whether other central banks will do likewise noting they were one of the first to start the initial hiking cycle. Canadian CPI data supported the theme of slower global inflationary pressure, with the headline and core measures falling to +6.3% and +5.6% respectively.

The Bank of Japan (BoJ) bought ¥5 trillion of JGBs to defend the target, its largest ever daily amount of bond buying, which followed ¥4.6 trillion of purchases earlier.

Eurozone Q4 GDP surprised at +0.1% q/q against -0.1 expected, raising hopes that a recession may be avoided. However, Italian GDP was weaker at -0.1% q/q, along with German GDP at -0.2% q/q with the possibility of downward revisions given German retail sales for December printed at -5.3% m/m against -0.2% expected.

Chinese trade data saw exports at -9.9% y/y (consensus -11.1%) and imports down -7.5% y/y (consensus -10.0%), though the impact of Covid in December clouds the numbers. China's population dropped in 2022 for the first time since 1961, by 850,000 to 1.412 billion. There are fears that as China's population declines, this will constrain potential growth. Meanwhile, China's re-opening continues to drive optimism, resulting in most commodity prices to trade higher.

The MSCI World ex-Aus Index rose +6.92% for the month of January:

Index	1m	3m	1yr	3yr	5yr	10yr
S&P 500 Index	+6.18%	+5.28%	-9.72%	+8.12%	+7.62%	+10.53%
MSCI World ex-AUS	+6.92%	+9.06%	-9.32%	+5.98%	+4.78%	+7.29%
S&P ASX 200 Accum. Index	+6.23%	+9.59%	+12.21%	+5.96%	+8.51%	+8.75%

Source: S&P, MSCI

Domestic Market

The unemployment rate in December was unchanged at 3.5% from an upwardly revised November figure. The participation rate fell 0.2% to 66.6% from 66.8%, back to its October level after the bounce in November, and has also been broadly steady at 66.6% in H2 2022.

With unemployment hovering around a 48-year low, businesses are finding it incredibly difficult to find workers. About 90% of bosses expect staffing shortages will affect their business this year, according to the Australian Industry Group's annual survey of CEO expectations.

Q4 CPI rose more than expected at +1.9% (consensus +1.5%), taking the annual rate to +7.8%, the highest peak since 1990, driven by increases in domestic holidays, international travel and higher electricity prices. The trimmed mean rose +1.7% over the quarter, with the annual rate coming in at +6.9%.

Sydney house prices have had their steepest annual fall on record, declining 10.9% last year as rising interest rates took a toll on buyer demand and spending power. House prices are now 11.3% below their early 2022 peak, but is still 24.2% higher than they were when the market troughed in mid-2020.

Dwelling approvals fell -9.0% m/m in November (consensus 0%). That's the third consecutive month of decline and follows October's 5.6% fall.

Retail sales fell a sharp -3.9% m/m in December (consensus -0.2%), following an upwardly revised November to +1.7% m/m (from 1.4%). The key implication is that we may be starting to see the first signs that monetary tightening is starting to weigh on consumption.

The November trade balance was up 0.5bn to $13.2bn from an upwardly revised October figure.

The Australian dollar gained +3.87%, finishing the month at US70.37 cents (from US67.75 cents the previous month).

Credit Market

The global credit indices tightened significantly over January in the 'risk-on' environment. They are now back to their levels in early 2022 (prior to the rate hike cycle from most central banks):

Index	January 2023	December 2022
CDX North American 5yr CDS	72bp	86bp
iTraxx Europe 5yr CDS	79bp	98bp
iTraxx Australia 5yr CDS	82bp	91bp

Source: Markit

Fixed Interest Review

Benchmark Index Returns

Index	January 2023	December 2022
Bloomberg AusBond Bank Bill Index (0+YR)	+0.27%	+0.25%
Bloomberg AusBond Composite Bond Index (0+YR)	+2.76%	-2.06%
Bloomberg AusBond Credit FRN Index (0+YR)	+0.42%	+0.34%
Bloomberg AusBond Credit Index (0+YR)	+2.19%	-0.62%
Bloomberg AusBond Treasury Index (0+YR)	+2.94%	-2.37%
Bloomberg AusBond Inflation Gov't Index (0+YR)	+4.87%	-2.74%

Source: Bloomberg

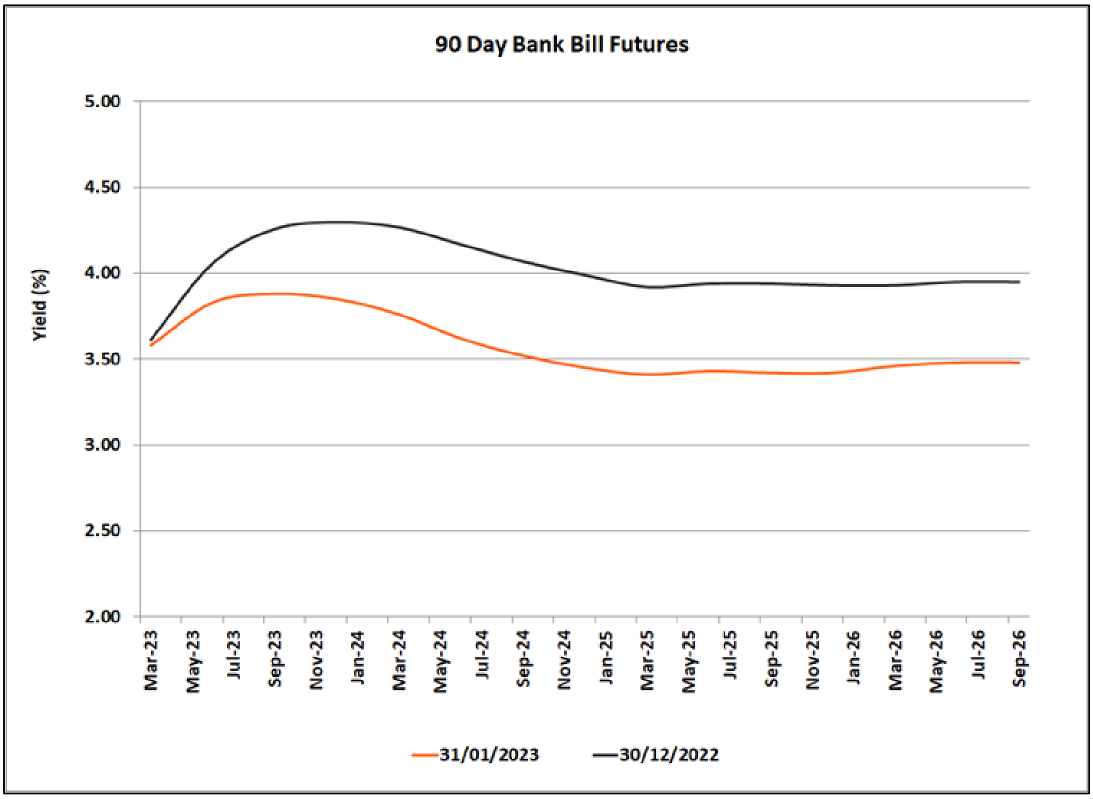
Other Key Rates

Index	January 2023	December 2022
RBA Official Cash Rate	3.10%	3.10%
90 Day (3 month) BBSW Rate	3.37%	3.26%
3yr Australian Government Bonds	3.17%	3.51%
10yr Australian Government Bonds	3.55%	4.05%
US Fed Funds Rate	4.25%-4.50%	4.25%-4.50%
3yr US Treasury Bonds	3.90%	4.22%
10yr US Treasury Bonds	3.52%	3.88%

Source: RBA, AFMA, US Department of Treasury

90 Day Bill Futures

Over January, bill futures fell across the board, with the market reacting to central bank rhetoric, hinting that a pause in the rate hike cycle was fast approaching. The markets continue to factor in the possibility of a global recession over the next few years, highlighted by the drop in the futures pricing in early 2024:



Source: ASX

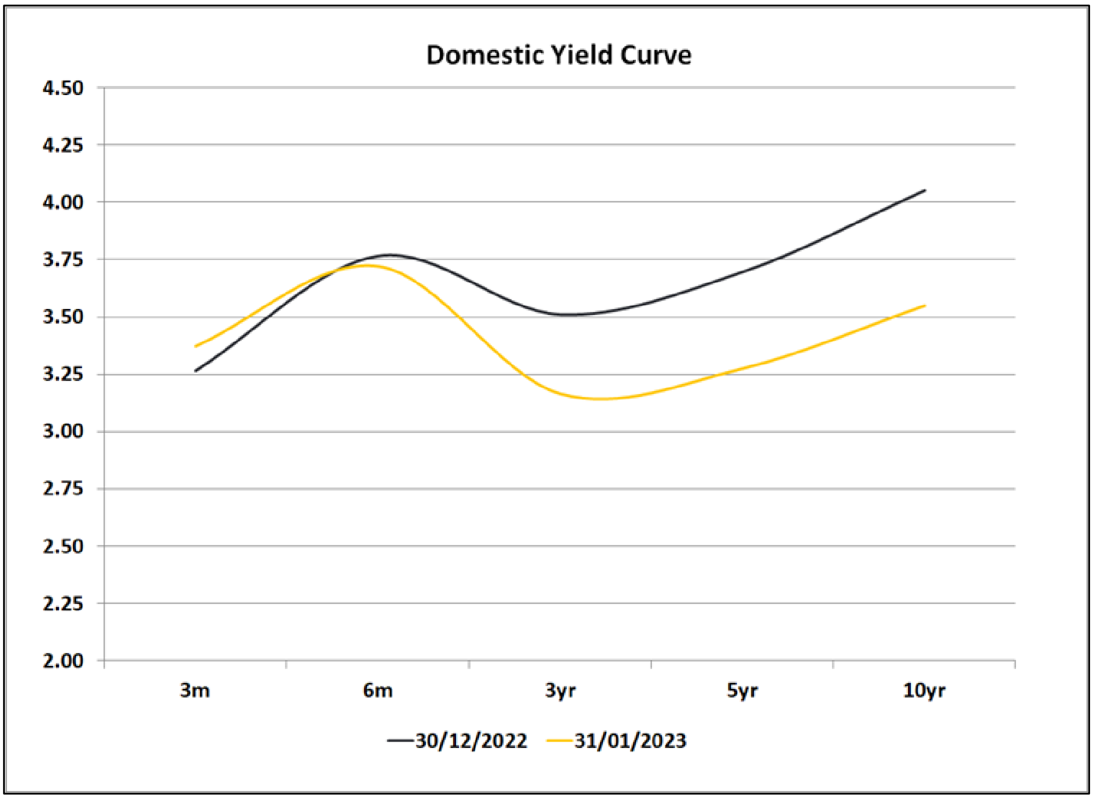
Fixed Interest Outlook

Following the recent soft inflation figures in the US, Fed Funds pricing is now expecting a 25bp hike on 1st February, with around a 40% chance they may also leave rates unchanged.

Domestically, the headline inflation outlook has somewhat receded with growing confidence that construction inflation is in retreat and signs of goods disinflation globally. The labour market remains tight, but timely indicators of labour demand are off their peaks as labour supply has normalised and frictions associated with rapid employment growth out of pandemic impacts moderate. Although labour costs pressures are evident in the latest CPI figures for Q4 2022, there are reasons to be optimistic that some stabilisation in wages growth can occur without a sharply higher unemployment rate, including the normalisation in labour supply.

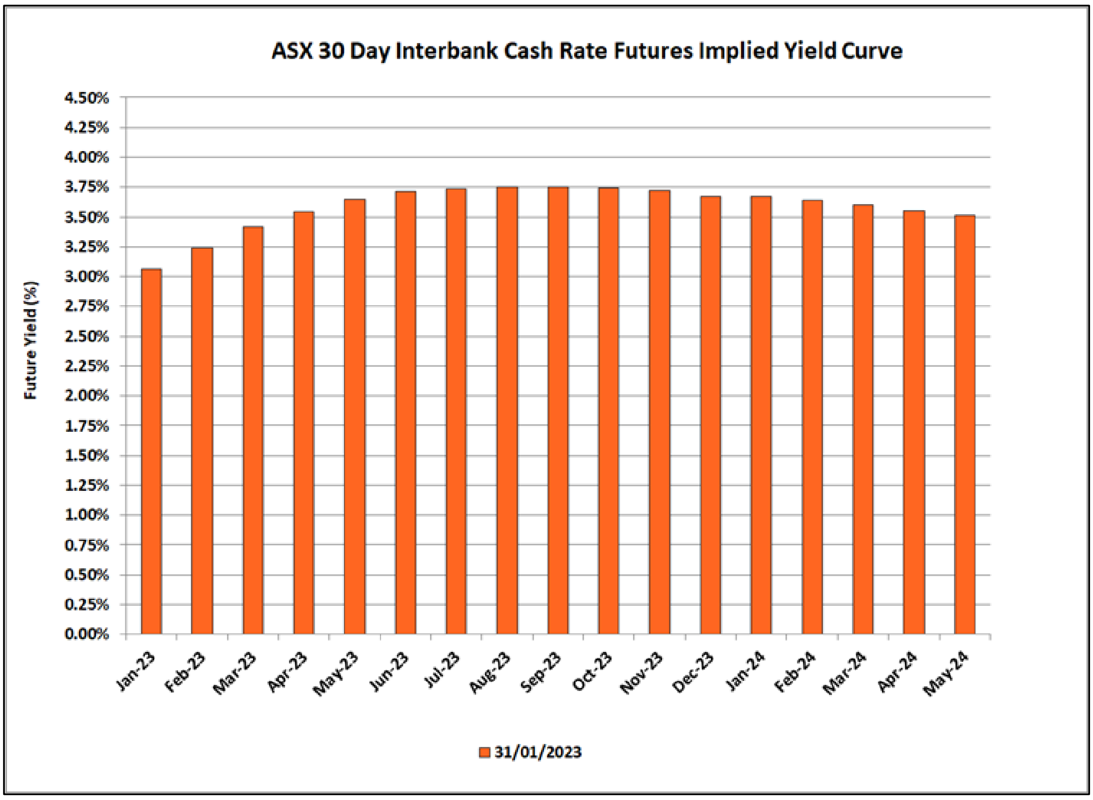
For now, the RBA continues to signal that it expects to increase interest rates further over the period ahead, with up to 2-3 hikes already largely priced into the market by Q2-Q3 2023, taking the cash rate up to 3¾%. Thereafter, noting the lags in monetary policy, a pause around the end of Q2-Q3 is likely whilst the RBA monitors the economic data.

Over the month, yields fell up to 50bp at the long-end of the curve:



Source: AFMA, ASX, RBA

Markets are currently pricing in around 2-3 additional rate rises into mid-2023 (up to 3.75%). Fears of a looming global recession have actually seen rate cuts start to be priced in towards the start of 2024, although this seems unlikely for now.



Source: ASX

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