10.4. Investment and Loan Borrowings Report as at 30 April 2023

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ATTACHMENTS	1. Imperium Monthly Investment Report April 2023 [**10.4.1** - 22 pages]
CSP LINK	5. Our Civic Leadership 5.2 Strong civic leadership and customer focussed services

PURPOSE:

The purpose of this report is to provide Council with the details of the performance of Council's investments and details of loans for the month of April 2023.

EXECUTIVE SUMMARY:

- This report outlines Council's investment portfolio and performance to 30 April 2023.

- All investments have been made in accordance with the Act, Regulations, Council's Investment Policy and the specific conditions of the TCorp Loan Agreement.

- For the month of April, the total portfolio (Term Deposits, Floating Rate Notes, and Bonds) provided a return of +0.22% (actual) or +2.67% p.a. (annualised), marginally under-performing the benchmark AusBond Bank Bill Index return of +0.30% (actual) or +3.77% p.a. (annualised). Council's investment adviser considers this underperformance to be temporary.

- Returns on investments exceed original YTD budget by $1.8 million due to higher than expect cash balances and higher than expected interest rates.

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

Background

Clause 212 of Local Government (General) Regulation 2021 states that The Responsible Accounting Officer must provide Council with a monthly report detailing all funds 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.

It is also prudent to report loan balances and compliance with borrowing orders issued by the Minister for Local Government and Council’s Debt Management Policy.

Investment Portfolio

The following table details the performance of Council’s investment portfolio (excluding cash deposits) to benchmark for the month of April 2023 and annualised for the year-to-date 30 April 2023 (including investments that have matured prior to that date).

	April 2023	**Annualised YTD**
Actual Return	0.22%	2.74%
Benchmark	0.30%	3.77%
Variance	-0.08%	-1.03%

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, as per 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**	**Portfolio Breakdown**
Term Deposits	$125,250,000	86.59%
Cash	$7,751,442	5.36%
Fixed Bonds	$9,000,000	6.22%
Floating Rate Notes (FRNs)	$2,647,466	1.83%
	$144,648,908	**100.00%**

Council’s average duration of term deposits, which comprise 86.92% of the investment portfolio, is approximately 339 days.

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 invested 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; $64.9 million for 2022/23 and $79.4 million in 2023/24.

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 monitor rates available from rated regional institutions (as advised by Imperium) but finds that major and large institutions tend to outperform them in the shorter terms currently required.

Summary of Returns from Investments (includes Fair Value adjustments)

The actual investment returns for the year-to-date 30 April 2023 are $531,000 more than the revised year-to-date budget. They are $1.8 million than the original YTD budget. 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. The report 10.3 Quarterly Budget Review - March 2023 proposes a further increase in forecast interest income of $550 thousand for a total projected result of $3,4 million Interest and Investment Income

Year	Original Annual Budget	Revised Annual Budget	YTD Budget (April)	YTD/ Annual Actual (April)	YTD/Annual Actual FV adjustments (April)	YTD Budget to Actual Variance (April)
2022/23	**$1,290,000**	**$2,790,000**	**$2,326,000**	**$2,852,000**	**$5,000**	**$531,000**
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 (FRNs) are required to be revalued each month using the Fair Value (FV) method, an estimate of the market value of the investment. The YTD movement of FRN's has been an increase of $5,000.

Financial Investment Policy

All categories are within the Policy limits for credit ratings. The portfolio remains well diversified, with credit quality rated as BBB or higher. The maximum holding limit in each rating category and the target credit quality weighting for Council's portfolio are:

Long Term Rating Range (Standard & Poors)	Invested	Maximum Policy Holding	Distribution
AA Category	$93,001,442	100.00%	64.29%
A Category	$33,250,453	60.00%	22.99%
BBB Category	$18,397,013	35.00%	12.72%
Unrated ADIs (NR)	$0	10.00%	0.00%

Credit Quality Limits in TCorp Loan Agreement

Council's Loan Agreement with TCorp 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 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	Maximum Allowed	Distribution
AA+ to AA-/Aa1 to Aa3 Category	$93,001,442	100%	64.29%
A+ to A/A1 to A2 Category	$33,250,453	100%	22.99%
A-/A3 Category	$0	40%	0.00%
BBB+/Baa1 Category	15,000,000	20%	10.37%
BBB/Baa2 Category	3,397,013	10%	2.35%
BBB-/Baa3 Category	$0	5%	0.00%
Unrated	$0	0%	0.00%

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

Institution	Long Term Rating Range (Standard and Poors/Moody's)	Invested	Maximum Allowed	Distribution
AMP Bank Ltd	BBB/Baa2 Category	$2,000,000	5%	1.38%
Bendigo and Adelaide Bank Ltd	BBB+/Baa1 Category	5,000,000	10%	3.46%
BOQ Ltd	BBB+/Baa1 Category	$10,000,000	10%	6.91%
Commonwealth Bank of Australia	AA+ to AA-/Aa1 to Aa3 Category	24,751,442	100%	17.11%
ICBC Sydney Branch	A+ to A/A1 to A2 Category	$17,000,000	100%	11.75%
NAB Ltd	AA+ to AA-/Aa1 to Aa3 Category	$38,000,000	100%	26.28%
Newcastle Greater Mutual Group	BBB/Baa2 Category	$1,397,013	5%	0.97%
Northern Territory Treasury	AA+ to AA-/Aa1 to Aa3 Category	$9,000,000	100%	6.22%
Suncorp Bank Ltd	A+ to A/A1 to A2 Category	16,250,453	100%	11.23%
Westpac Bank Ltd	AA+ to AA-/Aa1 to Aa3 Category	$21,250,000	100%	14.69%

Loan Borrowings

Council's Loan Borrowing Policy is the framework for Council's borrowing activities. It defines responsibilities and parameters for borrowing and related risk management activities. 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 a risk averse strategy.

Loan borrowings are 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 February 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 are to 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

Consultation requirements

Community engagement is not required.

Financial/Resource Implications

The December Quarterly Budget Review Statement increased the budgeted income from investments by $1.5 million to $2.9 million. This was due to higher-than-expected cash balances (due to delayed capital works) and interest rates greatly exceeding those available and foreseeable at the time the 2022/23 budget was made.

A further upward revision is in order. This revision of $550 thousand is included in the report 10.3 Quarterly Budget Review - March 2023 also on this agenda. The total forecast Interest and Investment Income will be $3.4 million.

Legislation

Section 625 of the Local Government Act (NSW) allows councils to invest money that is not currently required for any other purpose. It further specifies how councils may invest. It specifies investments must be in accordance with the local government minister's orders.

Clause 212 of the Local Government Regulation (NSW) 2021 requires that the Responsible Accounting Officer must make a monthly report to Council setting out all details of money invested under Section 625 of the Local Government Act.

Sections 621 to 624 of the Local Government Act give councils the ability to borrow money and specify some further regulations on that borrowing. Council's staff considers it prudent to provide monthly reporting of loans.

Monthly Investment Report

April 2023

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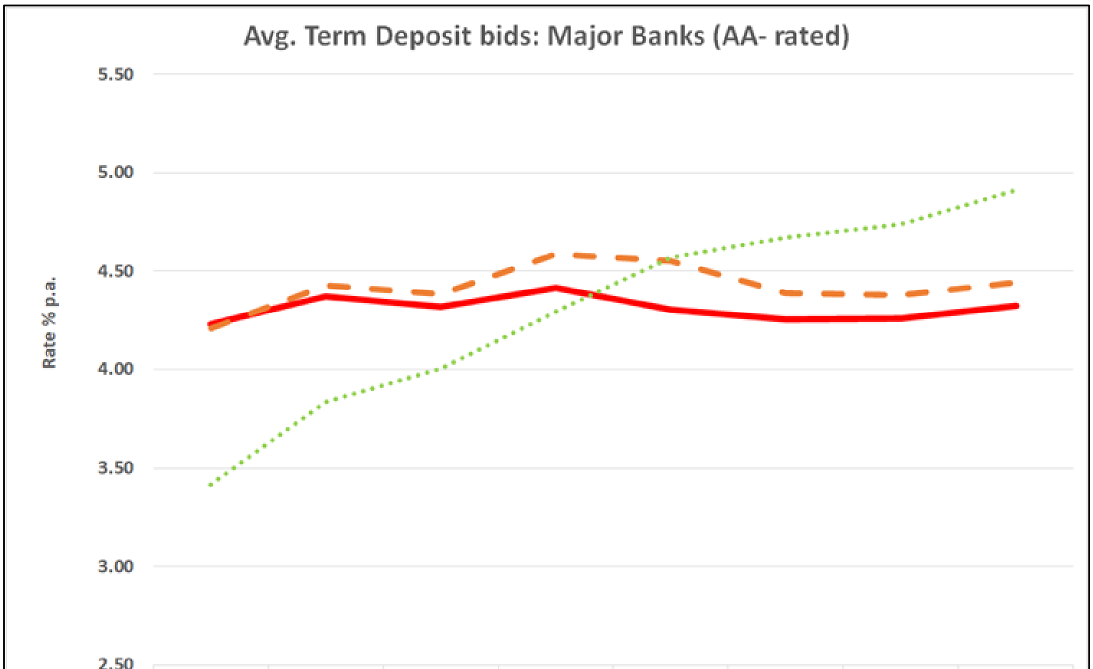
IMPERIUM MARKETS

<u>Market Update Summary</u>

Financial markets were aided in April following early signs of inflation peaking across several developed economies. Markets continue to adjust their forecasts regarding future interest rate expectations accordingly, with the peak of the interest rate cycle potentially month(s) away, as per the rhetoric from several global central banks. Domestically, the RBA paused in April but decided to lift rates in May to 3.85%, commenting "*some further tightening of monetary policy may be required*" reinforcing a continuing commitment to do what is necessary to return inflation to target and a bias that still higher interest rates might be required to return inflation to target.

Despite the aggressive rate hikes, over the past few months, the deposit market has already factored in the current rate hike cycle. Deposit rates in the long-end (12m-5yr tenors) from the major banks (rated AA-) fell around 10-20bp on average during April (compared to March), with the market starting to price in the possibility that we may have reached the peak of the interest rate cycle:



	3M	6M	9M	12M	2Y	3Y	4Y	5Y
Apr-2023	4.23	4.37	4.32	4.42	4.31	4.26	4.26	4.32
Mar-2023	4.21	4.43	4.39	4.59	4.56	4.39	4.38	4.44
Oct-2022	3.42	3.83	4.00	4.29	4.57	4.67	4.74	4.91

Source: Imperium Markets

'New' investments close to or above 4¼ - 4½% p.a. is currently available if Council can place the majority of its surplus funds for terms of 12 months to 3 years. *With recessionary fears being priced in coming years, investors may take an 'insurance policy' against future rate cuts by investing across 3-5 year fixed deposits and locking in rates above or close to 4½% p.a. (small allocation only), although this is primarily being offered by the lower rated ("BBB") ADIs.* ***<u>However due to upcoming capital outflows, this is currently restricting investments to shorter-tenors</u>****.*

Council's Portfolio & Compliance

<u>Asset Allocation</u>

As at the end of April 2023, the portfolio was mainly directed to fixed term deposits (87%). The remaining portfolio is directed to FRNs (2%), fixed bonds (6%) and overnight cash accounts (5%).

Senior FRNs remain relatively attractive as spreads have widened over the past year – new issuances should be considered again on a case by case scenario.

In the interim, fixed deposits for 12 months to 3 years remains appealing. With recessionary fears being priced in coming years, investors can choose to allocate some longer-term surplus funds and undertake an insurance policy against any potential future rate cuts by investing across 3-5 year fixed deposits, locking in and targeting yields close to or above 4½% p.a. (mainly available from the regional banks).

However, noting the significant capital outflows expected in the near term, Council is currently largely hand-cuffed to investing into very short-term investments (under 6 months). This is suitable to invest in short-dated fixed term deposits.

Term to Maturity

Overall, the portfolio remains lightly diversified from a maturity perspective. Around 19% of assets is directed to medium-term assets (2-5 years), which has resulted in strong outperformance during the challenging economic environment over longer-term time periods. There is still high capacity to invest in the short-medium term horizon (1-2 years), with approximately $71m at month-end.

Where liquidity permits (once immediate capital projects are finalised), 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	$55,751,442	38.54%	10%	100%	$88,897,466
✓	91 - 365 days	$31,250,000	21.60%	20%	100%	$113,398,908
✓	1 - 2 years	$29,647,466	20.50%	0%	70%	$71,606,770
✓	2 - 5 years	$28,000,000	19.36%	0%	50%	$44,324,454
✓	5 - 10 years	$0	0.00%	0%	25%	$36,162,227
		$144,648,908	**100.00%**			

Counterparty

As at the end of April, 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-	$24,751,442	17.11%	30.00%	$18,643,231
✓	NAB	AA-	$38,000,000	26.27%	30.00%	$5,394,672
✓	NTTC Treasury	AA-	$9,000,000	6.22%	30.00%	$34,394,672
✓	Westpac	AA-	$21,250,000	14.69%	30.00%	$22,144,672
✓	Suncorp	A+	$16,250,453	11.23%	15.00%	$5,446,883
✓	ICBC Sydney	A	$17,000,000	11.75%	15.00%	$4,697,336
✓	BOQ	BBB+	$10,000,000	6.91%	10.00%	$4,464,891
✓	Bendigo	BBB+	$5,000,000	3.46%	10.00%	$9,464,891
✓	AMP Bank	BBB	$2,000,000	1.38%	10.00%	$12,464,891
✓	Newcastle PBS	BBB	$1,397,013	0.97%	10.00%	$13,067,878
			$144,648,908	**100.00%**		

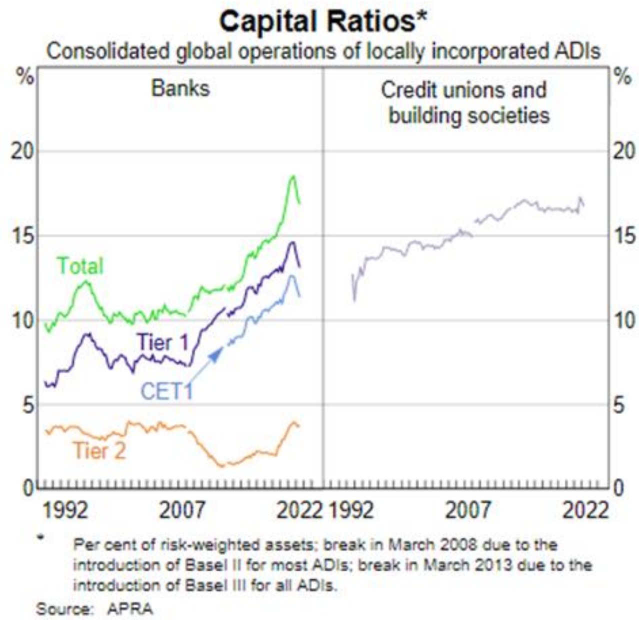
In late June 2022, Standard & Poor's downgraded Suncorp-Metway from AA- to A+ (negative watch). Suncorp recently announced that it is undertaking a strategic review of its banking operations. The downgrade reflects S&P's view that the Suncorp Group's likelihood of support for the bank had "*slightly*" 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). The financial regulator, APRA has 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

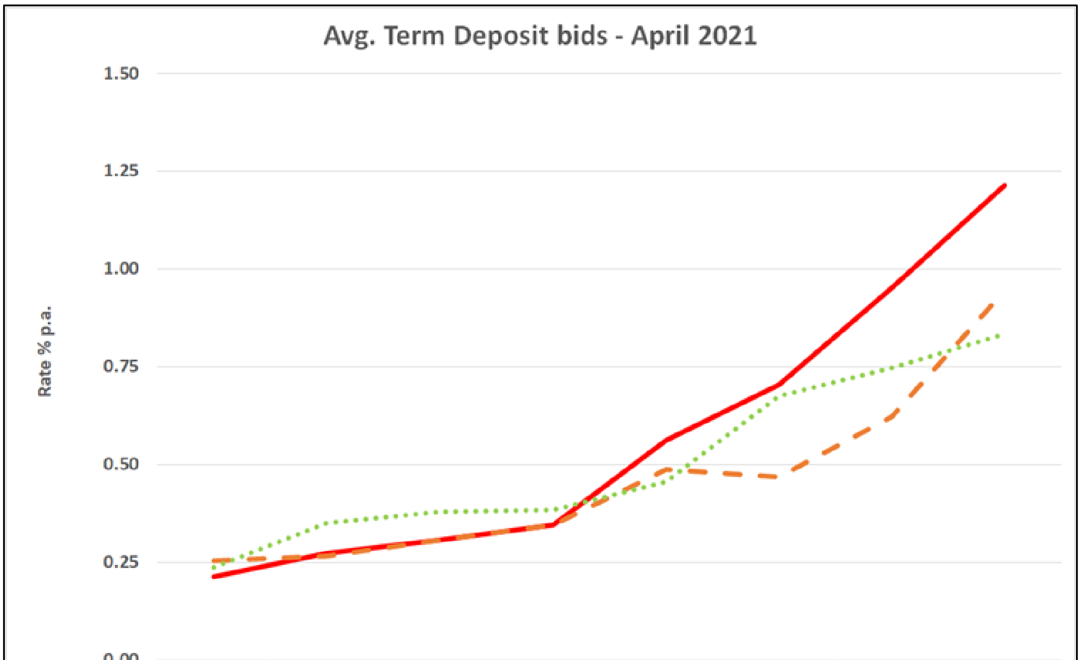
The portfolio remains well diversified from a credit ratings perspective, with all assets classified as investment grade (rated BBB- or higher). As at the end of April 2023, all categories were within the Policy limits:

Compliant	Credit Rating	Invested ($)	Invested (%)	Max. Limit (%)	Available ($)
✓	AA Category	$93,001,442	64.29%	100%	$51,647,466
✓	A Category	$33,250,453	22.99%	60%	$53,538,892
✓	BBB Category	$18,397,013	12.72%	35%	$32,230,105
✓	Unrated ADIs	$0	0.00%	10%	$14,464,891
		$144,648,908	**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.

[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

Term Deposit Rates – During Pandemic (April 2021)



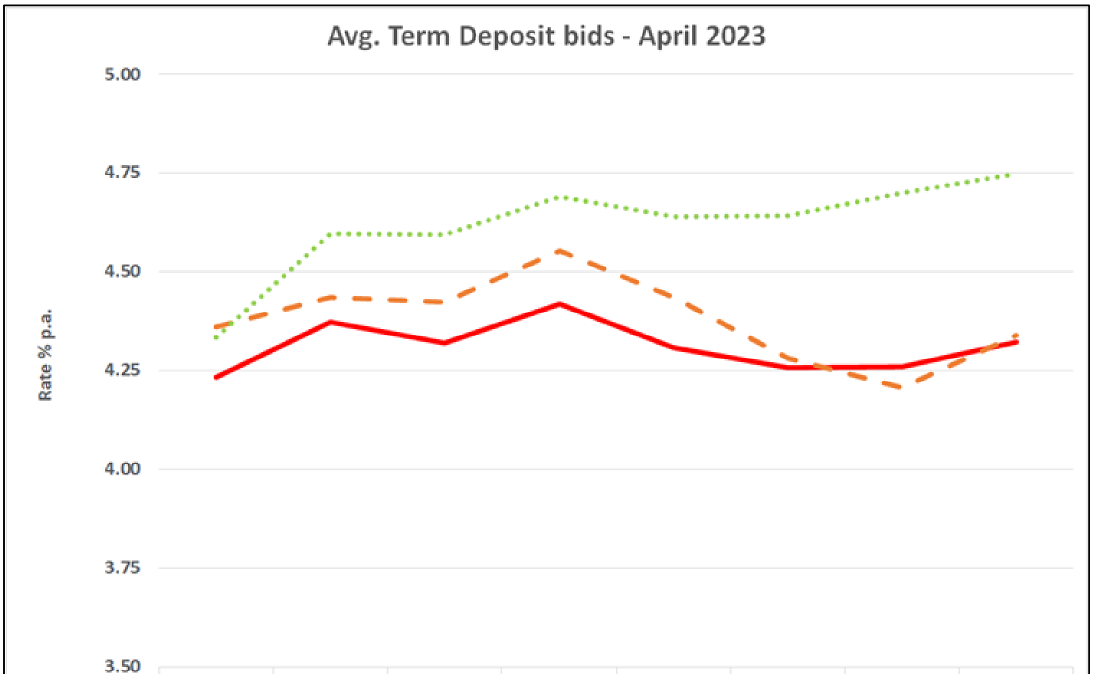
	3M	6M	9M	12M	2Y	3Y	4Y	5Y
Majors	0.21	0.27	0.31	0.34	0.56	0.71	0.95	1.21
A Rated	0.25	0.27	0.31	0.35	0.49	0.47	0.62	0.95
BBB Rated	0.24	0.35	0.38	0.38	0.46	0.68	0.75	0.84

Source: Imperium Markets

The abnormal marketplace experienced during the pandemic is starting to reverse as the competition for deposits increases. We are now starting to see some of the lower rated ADIs ("BBB" rated) offering slightly higher rates compared to the higher rated banks ("A" or "AA" rated) on different parts of the curve (i.e. pre-pandemic environment). Some of this has been attributed to lags in adjusting their deposit rates as some banks (mainly the lower rated ADIs) simply set their rates for the week.

Going forward, 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. We are slowly seeing this trend emerge, as has been the case over the past month again:

__Term Deposit Rates – Currently (April 2023)__



	3M	6M	9M	12M	2Y	3Y	4Y	5Y
Majors	4.23	4.37	4.32	4.42	4.31	4.26	4.26	4.32
A Rated	4.36	4.44	4.42	4.55	4.44	4.28	4.21	4.34
BBB Rated	4.33	4.60	4.59	4.69	4.64	4.64	4.70	4.75

Source: Imperium Markets

Performance

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

Performance (Actual)	1 month	3 months	6 months	FYTD	1 year	2 years
Official Cash Rate	0.29%	0.85%	1.61%	2.30%	2.40%	1.24%
AusBond Bank Bill Index	0.30%	0.83%	1.60%	2.28%	2.37%	1.19%
Council's T/D Portfolio	0.23%	0.66%	1.28%	1.98%	2.17%	1.74%
Council's FRN Portfolio	0.37%	1.09%	2.14%	3.22%	3.52%	2.40%
Council's Bond Portfolio	0.10%	0.28%	0.58%	0.97%	1.16%	1.13%
Council's Portfolio^	**0.22%**	**0.64%**	**1.25%**	**1.93%**	**2.13%**	**1.71%**
Outperformance	**-0.08%**	**-0.19%**	**-0.35%**	**-0.35%**	**-0.24%**	**0.52%**

^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	3.60%	3.52%	3.27%	2.77%	2.40%	1.24%
AusBond Bank Bill Index	3.77%	3.45%	3.26%	2.75%	2.37%	1.19%
Council's T/D Portfolio	2.81%	2.74%	2.61%	2.38%	2.17%	1.74%
Council's FRN Portfolio	4.63%	4.53%	4.37%	3.87%	3.52%	2.40%
Council's Bond Portfolio	1.17%	1.17%	1.17%	1.17%	1.16%	1.13%
Council's Portfolio^	**2.74%**	**2.67%**	**2.55%**	**2.33%**	**2.13%**	**1.71%**
Outperformance	**-1.03%**	**-0.78%**	**-0.71%**	**-0.42%**	**-0.24%**	**0.52%**

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

For the month of April, the total investment portfolio (excluding cash) provided a solid return of +0.22% (actual) or +2.74% p.a. (annualised), underperforming the benchmark AusBond Bank Bill Index return of +0.30% (actual) or +3.77% 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 slightly 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 April 2023, Council's deposit portfolio was yielding **2.74% p.a.** (unchanged from the previous month), with a weighted average duration of around 339 days (~11 months). We recommend Council maintains an average duration close to 12 months, should cash flows allow in future.

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:

ADI	LT Credit Rating	Term	T/D Rate
P&N Bank	BBB	5 years	4.95% p.a.
P&N Bank	BBB	4 years	4.85% p.a.
AMP Bank	BBB	2-3 years	4.85% p.a.^
P&N Bank	BBB	3 years	4.80% p.a.
P&N Bank	BBB	2 years	4.70% p.a.
Hume Bank	BBB+	2 years	4.70% p.a.
BoQ	BBB+	2 years	4.65% p.a.
ING	A	2 years	4.40% p.a.
Suncorp	A+	2 years	4.40% p.a.
Westpac	AA-	2 years	4.39% p.a.
NAB	AA-	2 years	4.35% p.a.

^Contact us to get an additional 20bp rebated commission. Aggregate limits temporarily lifted to $10m (from $5m).

The above deposits are suitable for investors looking to maintain diversification and lock-in a slight 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
AMP Bank	BBB	11-12 months	4.90% p.a.^
Hume Bank	BBB+	12 months	4.80% p.a.
P&N Bank	BBB	12 months	4.80% p.a.
BoQ	BBB+	12 months	4.65% p.a.
BoQ	BBB+	6 & 9 months	4.60% p.a.
NAB	AA-	6-12 months	4.55% p.a.
Westpac	AA-	12 months	4.51% p.a.
ING	A	12 months	4.50% p.a.
Suncorp	A+	12 months	4.48% p.a.
Suncorp	A+	3 months	4.46% p.a.

^Contact us to get an additional 20bp rebated commission. Aggregate limits temporarily lifted to $10m (from $5m).

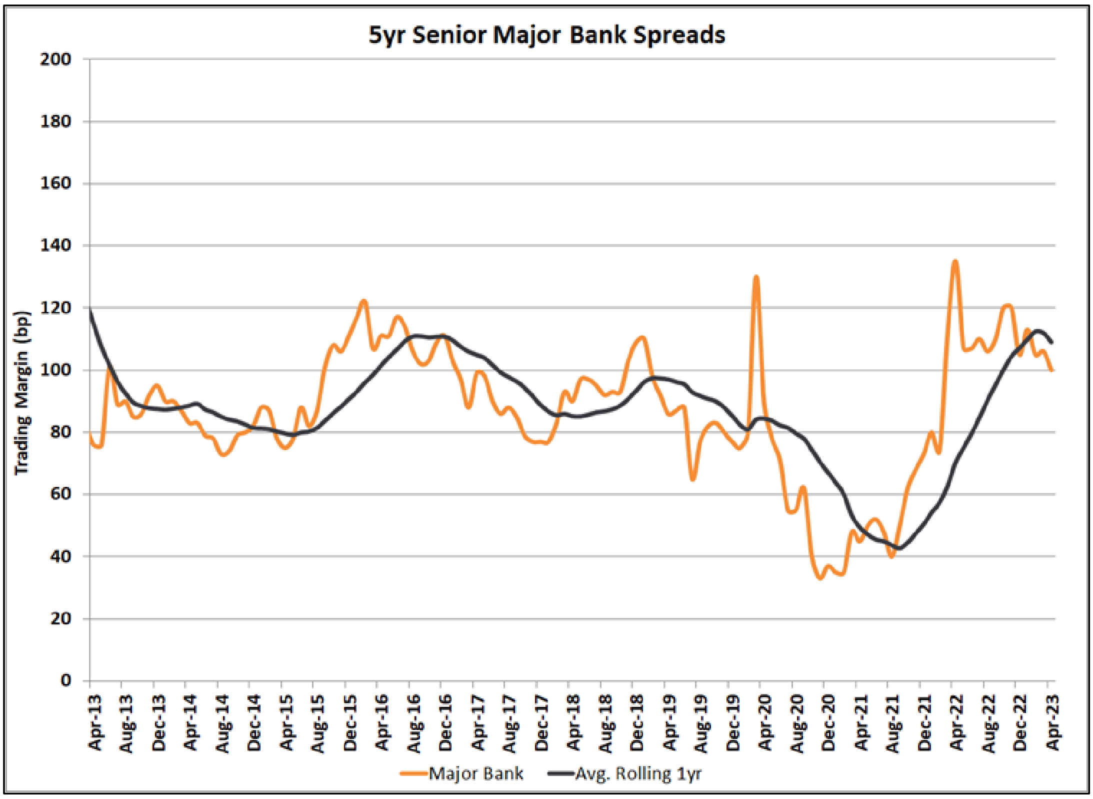
If Council does not require high levels of liquidity and can stagger its investments across the longer term horizons (1-5 years), it will be rewarded over a longer-term cycle if it can roll for an average min. term of 12 months to 3 years (this is where we current value), yielding, on average, up to ¼-½% p.a. higher compared to those investors that entirely invest in short-dated (under 6 months) deposits.

With recessionary fears being priced in coming years, Council should consider allocating some longer-term surplus funds and undertake an insurance policy by investing across 3-5 year fixed deposits and locking in rates close to or above 4½ p.a. This will provide some income protection if central banks decide to cut rates in future years, and assuming inflation has peaked and is under control.

<u>In the immediate future, given the significant outflows anticipated from capital projects, short-dated term deposits are suitable for North Sydney Council's purposes</u>.

Senior FRNs Review

Over April, amongst the senior major bank FRNs, physical credit securities tightened by around 6-8bp at the long-end of the curve. Major bank senior securities remain fairly attractive again in a rising rate environment (5 year margins above the +100bp level):



Source: IBS Capital

There was a lack of primary issuances again over the month apart from BoQ's (AAA rated) covered FRN at +120bp at month-end. Amongst the "A" rated sector, the securities were marked around 5bp tighter at the 3-5 year part of the curve, whilst the "BBB" rated sector was marked around 15bp tighter (3yrs).

Credit securities are looking much more attractive given the widening of spreads over the past year. 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)	30/04/2023	31/03/2023
"AA" rated – 5yrs	+100bp	+106bp
"AA" rated – 3yrs	+75bp	+83bp
"A" rated – 5yrs	+115bp	+120bp
"A" rated – 3yrs	+90bp	+95bp
"BBB" rated – 3yrs	+135bp	+150bp

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 mid-2025 for the "AA" rated ADIs (domestic major banks)**;
- On or before mid-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 remain, this has seen a significant lift in longer-term bond yields over the past year (valuations fell) as markets have reacted sharply.

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	0.36	3.00%	3.97%
AU3CB0258465	Westpac	AA-	Senior	16/11/2023	0.56	3.25%	4.10%
AU3CB0265403	Suncorp	A+	Senior	30/07/2024	1.27	1.85%	4.32%
AU3CB0263275	Westpac	AA-	Senior	16/08/2024	1.31	2.25%	4.10%
AU3CB0265718	ING	AAA	Covered	20/08/2024	1.32	1.45%	4.20%
AU3CB0266179	ANZ	AA-	Senior	29/08/2024	1.36	1.55%	4.10%
AU3CB0266377	Bendigo	BBB+	Senior	06/09/2024	1.39	1.70%	4.41%
AU3CB0268027	BoQ	BBB+	Senior	30/10/2024	1.52	2.00%	4.49%
AU3CB0269710	ANZ	AA-	Senior	16/01/2025	1.73	1.65%	4.08%
AU3CB0269892	NAB	AA-	Senior	21/01/2025	1.74	1.65%	4.03%
AU3CB0270387	Macquarie	A+	Senior	12/02/2025	1.81	1.70%	4.37%
AU3CB0287415	Westpac	AA-	Senior	17/03/2025	1.90	2.70%	4.08%
AU3CB0291508	Westpac	AA-	Senior	11/08/2025	2.32	3.90%	4.11%
AU3CB0291672	CBA	AA-	Senior	18/08/2025	2.32	4.20%	4.03%
AU3CB0280030	BoQ	BBB+	Senior	06/05/2026	3.03	1.40%	4.62%
AU3CB0282358	ING	AAA	Covered	19/08/2026	3.33	1.10%	4.31%
AU3CB0284149	BoQ	BBB+	Senior	27/10/2026	3.52	2.10%	4.66%
AU3CB0286037	Westpac	AA-	Senior	25/01/2027	3.77	2.40%	4.21%

Economic Commentary

International Market

Financial markets were aided in April following early signs of inflation peaking across several developed economies. Across equity markets, the S&P 500 Index gained +1.46%, whilst the NASDAQ added +0.04%. Europe's main indices also gained, led by UK's FTSE (+3.13%), France's CAC (+2.31%) and Germany's DAX (+1.88%).

US CPI showed welcome, but not overwhelming, progress. Headline CPI rose less than expected, up +0.1% m/m and +5.0% y/y, down from +6.0% previously, the first monthly decline since November 2020. Core inflation, however, was in line with expectations at +0.4% m/m and +5.6% y/y.

The US unemployment rate fell 0.1% to 3.5% (3.6% expected) and average hourly earnings rose by an as expected +0.3% to be +4.2% up on a year ago down from +4.6% and +4.3% expected.

Strong Canada jobs report showed employment up +34.7k against +5k expected and the unemployment rate remained steady at 5.0%, rather than the consensus for a rise to 5.1%. The Bank of Canada held rates for the second consecutive meeting as expected.

UK employment growth was strong at 169k vs. 50k expected, while the unemployment rate ticked up 0.1% higher to 3.8%. BoE pricing now has a 90% chance of a 25bp rate hike in May (up from a 79% previously).

UK April CPI was a shocker, headline CPI only falling from +10.3% to +10.1% against +9.8% expected and the core measure unchanged at +6.2% against expectations for a fall to +6.0%.

The RBNZ raised rates by 50bp to 5.25%, against a strong market consensus for a smaller 25bp hike.

The International Monetary Fund (IMF) downgraded global growth forecasts made three months ago by 0.1% to +2.8% for 2023 and +3.0% for next year, following the +3.4% lift last year. The IMF noted "*the risks are weighted heavily to the downside, in part because of the financial turmoil of the last month and a half*".

Chinese activity data showed GDP rebounded more quickly than expected. Q1 GDP growth beat expectations by +0.2% at +2.2% q/q vs. +2.0% expected. Strength was seen by the consumer with retail sales +10.6% y/y vs. +7.5% expected.

The MSCI World ex-Aus Index rose +1.62% for the month of April:

Index	1m	3m	1yr	3yr	5yr	10yr
S&P 500 Index	+1.46%	+2.28%	+0.91%	+12.70%	+9.50%	+10.07%
MSCI World ex-AUS	+1.62%	+2.07%	+1.66%	+11.39%	+6.45%	+6.99%
S&P ASX 200 Accum. Index	+1.85%	-0.80%	+2.83%	+13.99%	+8.26%	+7.90%

Source: S&P, MSCI

Domestic Market

The RBA decided to leave interest rates unchanged at 3.60% in April, while it assesses the outlook for the economy and the impact of previous substantial interest rate increases.

In addition, the bias to tighten further was softened with prior phrasing of further tightening will be required replaced with further tightening may well be needed. This suggests that the RBA has downgraded its forecasts for growth and/or inflation from the February Statement on Monetary Policy when a cash rate of 3.75% was seen as being required to achieve the return of inflation to 3% by mid-2025.

RBA Governor Lowe commented that "*the decision to hold rates steady this month does not imply that interest rate increases are over*" and that "*at our next meeting, we will again review the setting of monetary policy with the benefit of an updated set of forecasts and scenarios*".

Core trimmed mean Q1 CPI came in 0.2% less than market expectations at +1.2% q/q and +6.6% y/y (consensus +1.4%/+6.7%). Headline inflation was a fraction above consensus at +1.4% q/q and +7.0% y/y, (consensus +1.3%/+6.9%). Overall, the inflation figures confirmed the widely held expectation that Australian inflation peaked late last year (Q4 2022), something now becoming clearly evident in goods price pressures, a trend in place in other parts of the world as supply chain disruptions heal and freight rates fall.

Employment grew +53.0k m/m in March, more than double the consensus of +20k. The unemployment rate held steady at 3.5%, where it has been since July 2022 and it remains around its lowest levels since the 1970s. The participation rate lifted by around 0.1% to 66.74% from 66.65%.

Australian dwelling prices rose +0.6% m/m in March. That is the first nationwide increase since April 2022 and comes after declines moderated to just +0.1% in February. Meanwhile dwelling approvals rose +4.0% m/m in February (consensus +10.0%), following the sharp -27.1% fall seen in February.

The February trade surplus was $13.8bn (consensus $11.2bn) from $11.3bn, largely driven by a big fall in imports (-9.1% m/m or -$4.3bn).

The Australian dollar lost -1.52%, finishing the month at US66.10 cents (from US67.12 cents the previous month).

Credit Market

The global credit indices remained relatively flat over April. They are now back to their levels in early 2022 (prior to the rate hike cycle from most central banks):

Index	April 2023	March 2023
CDX North American 5yr CDS	79bp	78bp
iTraxx Europe 5yr CDS	86bp	88bp
iTraxx Australia 5yr CDS	91bp	92bp

Source: Markit

Fixed Interest Review

Benchmark Index Returns

Index	April 2023	March 2023
Bloomberg AusBond Bank Bill Index (0+YR)	+0.30%	+0.28%
Bloomberg AusBond Composite Bond Index (0+YR)	+0.19%	+3.16%
Bloomberg AusBond Credit FRN Index (0+YR)	+0.46%	+0.26%
Bloomberg AusBond Credit Index (0+YR)	+0.45%	+1.85%
Bloomberg AusBond Treasury Index (0+YR)	+0.01%	+3.53%
Bloomberg AusBond Inflation Gov't Index (0+YR)	+0.32%	+4.16%

Source: Bloomberg

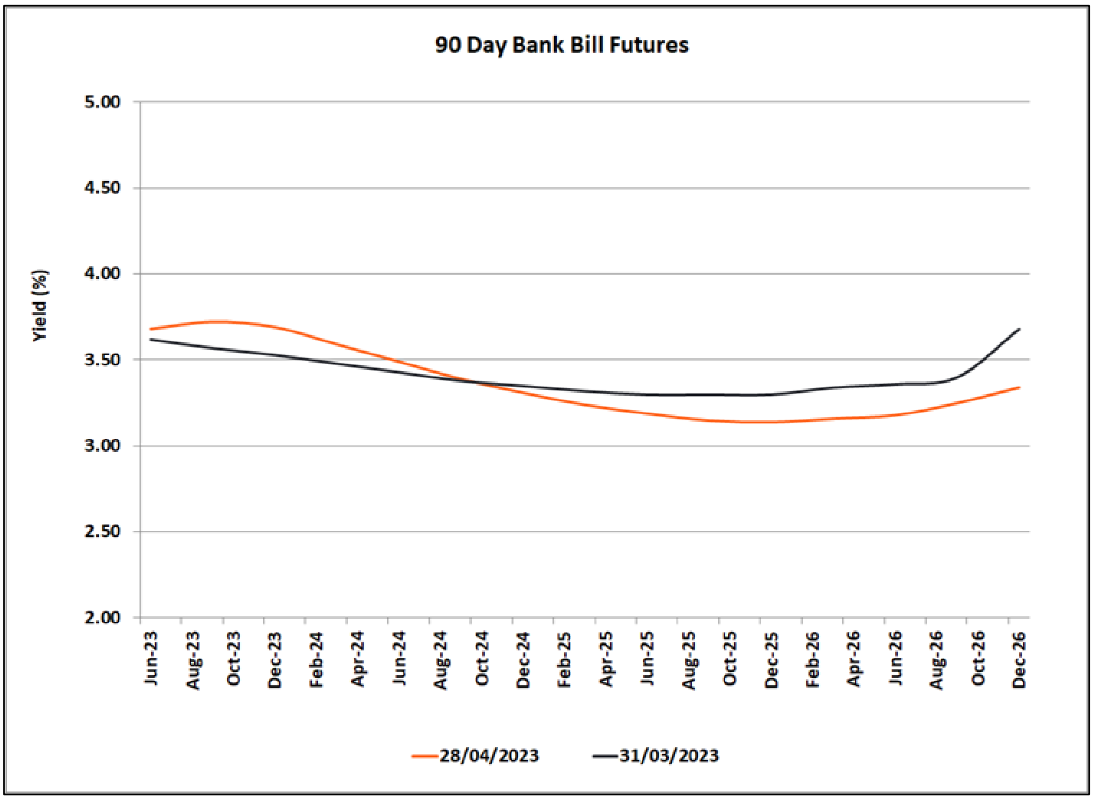
Other Key Rates

Index	April 2023	March 2023
RBA Official Cash Rate	3.60%	3.60%
90 Day (3 month) BBSW Rate	3.68%	3.72%
3yr Australian Government Bonds	3.00%	2.94%
10yr Australian Government Bonds	3.34%	3.30%
US Fed Funds Rate	4.75%-5.00%	4.75%-5.00%
2yr US Treasury Bonds	4.04%	4.06%
10yr US Treasury Bonds	3.44%	3.48%

Source: RBA, AFMA, US Department of Treasury

90 Day Bill Futures

Bill futures fell at the long-end of the curve in April, following the lower than expected inflation figures released at month-end. 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

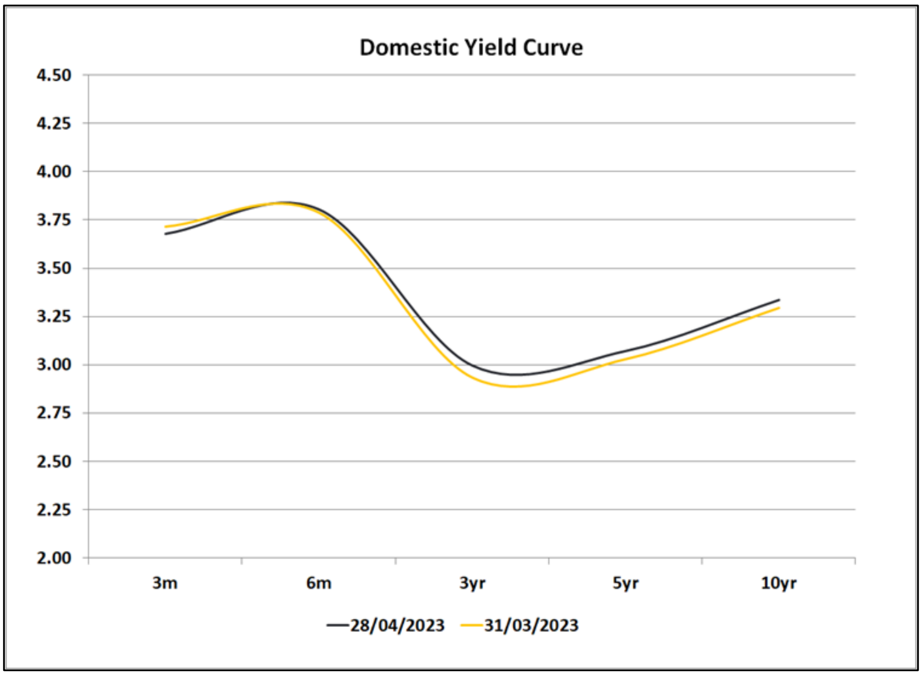
US money market rates ascribe more than an 80% probability to the Fed lifting the Funds rate by 0.25% to 5.00-5.25% on May 3 following the stronger than expected employment numbers.

Domestically, after announcing official interest rates would remain unchanged in April, the RBA's bias to tighten further was softened with prior phrasing of further tightening will be required replaced with further tightening may well be needed. With this pause, 3.60% may potentially mark the peak of interest rates for Australia this cycle as we envisage considerably slower growth in the second half of 2023, moderating inflation and an increase in the unemployment rate. But the RBA continues to suggest they will be agile and act depending on the economic data that is presented to them.

With the RBA having paused in April, the latest CPI data suggests the RBA remains on balance and is likely to pause again in May, waiting on further information on wages (WPI on 17th May and the Minimum Wage Decision) to assess whether the aim of returning inflation to 3% by mid-2025 remains plausible.

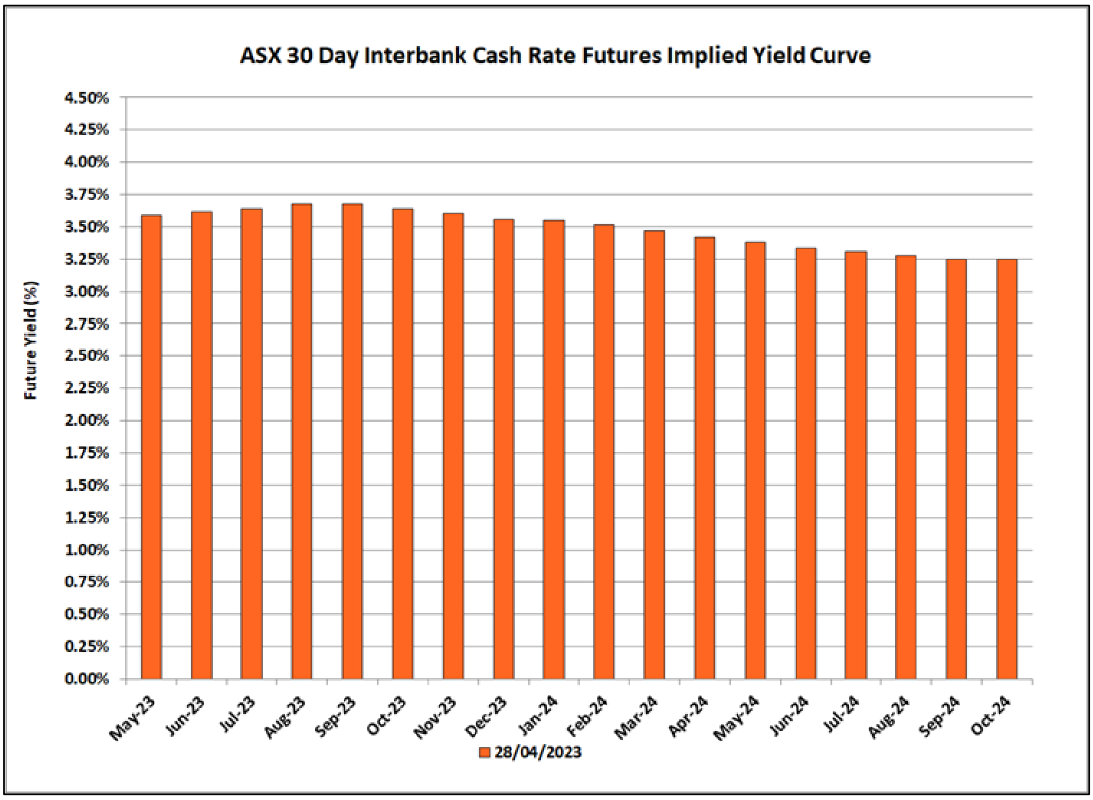
What would cause the Board to raise interest rates further? This would likely require in the near term, a significant inflation or wages shock, something that cannot be ruled out as the RBA has been quite reactive to surprises in this sense in recent months, though it also seems to have been comfortable with the prospect of a minimum wage increase as large as 7% being announced in the next few months. Medium term, further rate rises would likely require an accumulation of evidence that inflation was not tracking back towards the 2-3% target. The risk continues to be to the upside in the near term with the RBA to remain reactive to the data flow, especially around inflation and wages.

Over the month, yields remained relatively flat at the long-end of the curve:



Source: AFMA, ASX, RBA

With the RBA keeping rates on hold in April and a slightly softer inflation reading than anticipated, the market has changed its view to the next move bring a rate cut, against the RBA's rhetoric that rates may still need to move higher should inflation remain persistently high over the medium term.



Source: ASX

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