



Report to General Manager

Attachments:

1. Investment Portfolio as at 28 February 2017
 2. Monthly Investment Report – February 2017
-

SUBJECT: Investments and Loan Borrowings Held as at 28 February 2017

AUTHOR: Garry Ross, Manager Financial Services (Responsible Accounting Officer)

ENDORSED BY: Sandra Moore, Acting Director Corporate Services

EXECUTIVE SUMMARY:

This report provides details of the performance of Council's investment portfolio and borrowing limits for the period ending 28 February 2017.

Investment Portfolio:

The portfolio provided an annualised return of 3.50% for the year to date as at 28 February 2017, 1.73% above the reportable benchmark (BBSW Bank Bill Index). Interest returns remain consistently above the benchmark. This was attributed to additional funds being made available for investment and prudent selection and allocation of these funds to the financial institutions which make up the investment portfolio.

Borrowing Limits:

Council has commenced a \$30 million debt facility and as at the reporting date, has drawn down \$9.5 million for capital works projects. Council continues to monitor interest rate risk whenever it borrows, regardless of whether the interest rates are fixed or variable.

FINANCIAL IMPLICATIONS:

Any surplus funds generated in excess of adopted estimates will be transferred to Council's internally restricted reserves.

Comment by Responsible Accounting Officer:

Investments and Loan borrowings funding comply with Council's Financial Management Policy.

Local Government Act 1993: Section 23A Guidelines - Council Decision Making During Merger Proposal Period

The Guidelines have been considered in the preparation of this report and are not applicable

RECOMMENDATION:

1. **THAT** the report be received.
-

LINK TO DELIVERY PROGRAM

The relationship with the Delivery Program is as follows:

- Direction: 5. Our Civic Leadership
- Outcome: 5.2 Council is financially sustainable

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.

SUSTAINABILITY STATEMENT

The following table provides a summary of the key sustainability implications:

QBL Pillar	Implications
Environment	• There are no perceived short or long-term environmental implications.
Social	• There are no perceived short or long-term social implications.
Economic	• Provides Council with a significant source of income.
Governance	• Compliance with all legislative requirements and statutory obligations.

DETAIL

Investment Portfolio

The following table provides details of the performance of Council's investment portfolio against the benchmark for the month of February 2017.

	February 2017	YTD as at 28 February 2017
Actual Return	3.50%	3.54%
Benchmark	1.77%	1.84%
Variance	1.73%	1.70%

The following table shows the actual cash inflows received from the portfolio for the month of February 2017 and for the year to date as at 28 February 2017.

	February 2017	YTD as at 28 February 2017
Capital Guaranteed	\$0.00	\$0.00
Cash Enhanced Funds	\$0.00	\$0.00
Fixed Cash Fund	\$0.00	\$0.00
Senior Bonds	\$52,415.62	\$701,725.67
Term Deposits	\$301,894.52	\$2,082,823.29
Trading Accounts	\$5,956.06	\$65,968.06
	\$360,266.20	\$2,850,517.02

Investment Performance

Investment returns continue to exceed the indicative benchmark (BBSW Bank Bill Index). All funds invested have been done so in accordance with the Act and the Regulations made thereunder and with Council's Financial Investment Policy. Further, 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. These restrictions have placed greater emphasis on obtaining competitive investment options and the need for sound investment advice from Council's independent advisor.

Council continues to seek independent advice for all investments and is actively managing the portfolio to ensure that returns are maximised, taking into account diversification and risk.

Summary of Returns from Investments:

Year	Original Budget	Revised Budget	YTD/Annual Actual (February)	YTD Budget Variance (February)
2016/17	\$2,000,000	\$3,000,000	\$2,265,830	\$265,830
2015/16	\$2,320,000	\$3,640,000	\$4,105,146	\$465,146
2014/15	\$3,400,000	\$4,150,000	\$4,414,692	\$264,692
2013/14	\$2,700,000	\$3,400,000	\$3,983,515	\$583,515
2012/13	\$2,000,000	\$2,887,751	\$4,238,785	\$1,353,069
2011/12	\$2,000,000	\$3,400,000	\$3,728,080	\$328,080

Investments held for February (Annualised):

Investment Type	%Portfolio	February 2017 (Purchase Value)	February 2017 (Market Value)	February 2017 % Return	February 2017 YTD%
Fixed Cash Fund	0.0%	\$0.00	\$0.00	0.00%	0.00%
Senior Bonds	30.0%	\$30,000,000.00	\$30,208,280.00	3.00%	3.01%
Term Deposits	61.0%	\$61,500,000.00	\$61,500,000.00	3.74%	3.75%
Trading Accounts	9.0%	\$8,636,403.93	\$8,636,403.93	1.11%	1.25%

S & P Rating	Investments Market Value	% of Portfolio (February)
AAA	\$0.00	0.00%
AA	\$0.00	0.00%
AA-	\$15,622,088.42	16.0%
	\$15,622,088.42	16.0%
A+	\$18,063,935.51	18.0%
A	\$0.00	0.0%
A-	\$27,527,780.00	27.0%
	\$45,591,715.51	45.0%
BBB+	\$27,130,880.00	27.0%
BBB	\$3,000,000.00	3.0%
BBB-	0.00	0.0%
	\$30,130,880.00	30.0%
NR	\$9,000,000.00	9.0%
	\$100,344,683.93	100.00%

Financial Investment Policy

The maximum holding limit in each rating category and the target credit quality weighting for Council's portfolio shall be:

Long Term Rating Range	Maximum Holding
AAA Category	100.00%
AA Category	100.00%
A Category	60.00%
BBB Category	35.00%
Unrated ADIs	10.00%

The policy has been independently reviewed by Council's investment advisors. Risk management guidelines and investment decision criteria have been amended. The main changes are:

- Compliance with other Council policies, those being Fraud Corruption and prevention Policy, Code of Conduct Policy and Financial Management Policy; and
- Investment decision criteria, in particular, the review mechanism associated with a rating down grade.

Loan Borrowings

Council has implemented an expanded capital works program which requires alternate sources of funding, both internal and from financial institutions. Council has been debt free for a considerable period, which has prompted the need for a loan borrowing program to ensure that there is intergenerational equity in the provision of essential infrastructure and other major capital projects.

Council's Debt Management 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 to be 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 of both in order to maintain its risk averse strategy.

Loan borrowing will be 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 the acquisition or enhancement of income producing assets;
 - To the construction and/or upgrading of buildings;
 - To infrastructure assets that have a life expectancy of greater than 10 years.

The current Debt Facility is as follows:

Bank loan via the NAB Corporate Market loan (Variable Rate Option)

Facility Limit: \$30 million (Initial offer)

Capital projects purposes only (refer to loan funded projects list)

3 year tenor with facility to be reviewed annually

Interest rate linked to 90 day BBSY index + drawn margin%

Drawn margin: 0.57%

Facility Fee: 0.24%

Facility expiry date: 28 February 2018

Facility Utilisation: 31.7% (\$9.5m of \$30m)

The estimated Debt Service Cover Ratio this financial year is approximately 24% compared to the Local Government industry benchmark of greater than or equal to 2%.

This ratio measures Council's availability of operating cash to service debt liabilities.

Council has no fixed interest rate loans. This situation will be reviewed when additional borrowings are required or when interest rates move from their current low level.

Loan Funded Capital Projects as at 28 February 2017

Project 1: Upgrading the car park in Alexander Street, Crows Nest

A \$5 million loan has been sourced to fund this project.

Current length of Loan as per LTFP: 20 years to 2035/36

Project 2: Upgrading of On-Street Parking Management System

A **\$4.5 million** loan has been sourced to fund this project.
Current length of Loan as per LTFP: 20 years to 2035/36

Loan Borrowings Summary 2016/17

	Interest & Fee Details	Amount	Applicable Dates	Rate Charge	Applicable Rate	Charge Date	Interest & Fee Charges YTD
Interest Charges	Floating Rate	\$9,500,000.00	14 June 16 - 14 Sept 16	BBSY Rate: 2.0717% Drawn Margin: 0.5700%	2.6417%	15 Sept 2016	\$63,256.05
	Floating Rate	\$9,500,000.00	14 Sept 16 - 14 Dec 16	BBSY Rate: 1.7933% Drawn Margin: 0.5700%	2.3633%	15 Dec 2016	\$55,974.60
Total							\$119,230.65
Fee and Premium Charges	Facility Fee (%)	\$30,000,000.00	14 June 16 - 14 Sept 16		0.2400%	14 Sept 2016	\$18,147.94
	Facility Fee (%)	\$30,000,000.00	14 Sept 16 - 14 Dec 16		0.2400%	14 Dec 2016	\$17,950.68
Total							\$36,098.62

The next loan repayment is due on 14 March 2017

North Sydney Council Investment Portfolio as at 28 February 2017

	Investment Face Value	Investment Market Value	%	S&P Rating #	Net Returns - 1 Month		Net Returns - FYTD		Maturity
Trading Account:					Return*	Income^	Return	Income^	
CBA Trading Account - General Fund	3,095,648.02	3,095,648.02	3%	AA-	0.80	1,267.67	1.10	11,566.95	At Call
CBA Business On-Line Saver	4,500,000.00	4,500,000.00	4%	AA-	1.05	2,953.42	1.05	28,524.12	At Call
AMP 31-day Notice Account	1,036,155.51	1,036,155.51	1%	A+	2.15	1,733.02	2.57	15,318.47	31-Mar-17
CBA Cash Management Account	4,600.40	4,600.40	0%	AA-	1.65	1.95	1.71	13.96	At Call
	8,636,403.93	8,636,403.93	9%		1.11	5,956.06	1.25	55,423.50	
Term Deposits:									
CUA @ 3.05%	2,000,000.00	2,000,000.00	2%	BBB+	3.05	4,679.45	3.05	40,610.95	23-Mar-17
Rabobank @ 5.70%	2,000,000.00	2,000,000.00	2%	A+	5.70	8,745.21	5.70	75,895.88	6-Jun-17
Auswide Bank @ 2.90%	3,000,000.00	3,000,000.00	3%	BBB	2.90	6,673.97	2.90	41,712.32	7-Jun-17
AMP @ 2.90%~	1,000,000.00	1,000,000.00	1%	A+	2.90	2,224.66	2.90	19,306.83	28-Aug-17
BoQ @ 4.90%	3,000,000.00	3,000,000.00	3%	A-	4.90	11,276.71	4.90	97,865.74	28-Aug-17
BCU @ 4.00%	2,000,000.00	2,000,000.00	2%	NR	4.00	6,136.99	4.00	53,260.27	28-Aug-17
Bendigo TD @ 2.90%	3,000,000.00	3,000,000.00	3%	A-	2.90	6,673.97	2.90	57,920.53	30-Aug-17
Bendigo TD @ 2.90%	3,000,000.00	3,000,000.00	3%	A-	2.90	6,673.97	2.90	57,920.53	4-Sep-17
CUA @ 3.75%	3,000,000.00	3,000,000.00	3%	BBB+	3.75	8,630.14	3.75	74,897.25	11-Sep-17
Bendigo TD @ 2.92%	2,000,000.00	2,000,000.00	2%	A-	2.92	4,480.00	2.92	38,880.00	15-Sep-17
BoQ @ 4.70%	1,000,000.00	1,000,000.00	1%	A-	4.70	3,605.48	4.70	31,290.40	27-Sep-17
BoQ Specialist @ 5.60%	500,000.00	500,000.00	0%	A-	5.60	2,147.95	5.60	18,641.09	2-Nov-17
AMP @ 3.20%~	4,000,000.00	4,000,000.00	4%	A+	3.20	9,819.18	3.20	85,216.43	5-Mar-18
Community Alliance CU @ 2.90%	2,000,000.00	2,000,000.00	2%	NR	2.90	4,449.32	2.90	27,013.71	13-Mar-18
RaboDirect @ 4.25%	2,000,000.00	2,000,000.00	2%	A+	4.25	6,520.55	4.25	56,589.05	20-Aug-18
Rabobank @ 4.05%	6,000,000.00	6,000,000.00	6%	A+	4.05	18,641.10	4.05	161,778.10	28-Aug-18
BCU @ 3.00%	1,000,000.00	1,000,000.00	1%	NR	3.00	2,301.37	3.00	15,123.30	29-Aug-18
Defence Bank @ 2.90%	3,000,000.00	3,000,000.00	3%	BBB+	2.90	6,673.97	2.90	41,712.32	7-Sep-18
Police CU @ 2.90%	2,000,000.00	2,000,000.00	2%	NR	2.90	4,449.32	2.90	27,808.23	7-Sep-18
Police CU @ 3.05%	1,000,000.00	1,000,000.00	1%	NR	3.05	2,339.73	3.05	20,305.48	10-Sep-18
BoQ @ 5.00%	3,000,000.00	3,000,000.00	3%	A-	5.00	11,506.85	5.00	99,863.04	29-Oct-18
WAW CU @ 3.10%	1,000,000.00	1,000,000.00	1%	NR	3.10	2,378.08	3.10	6,709.59	12-Dec-18
ME Bank @ 5.10%	3,000,000.00	3,000,000.00	3%	BBB+	5.10	11,736.99	5.10	101,860.27	14-Feb-19
ING @ 4.95%	3,000,000.00	3,000,000.00	3%	A-	4.95	11,391.78	4.95	98,864.39	18-Feb-19
Newcastle PBS @ 2.90%	2,000,000.00	2,000,000.00	2%	BBB+	2.90	4,449.32	2.90	27,808.23	6-Sep-19
NAB Flexi Deposit @ 3m BBSW +1.05%	1,000,000.00	1,000,000.00	1%	AA-	2.82	2,163.29	3.53	21,618.90	12-Dec-19
BoQ @ 3.55%	2,000,000.00	2,000,000.00	2%	A-	3.55	5,446.58	3.55	15,367.13	11-Dec-20
Expired Deposits - Financial Year	-	-	-	-	-	0.00	-	121,447.81	Expired
	61,500,000.00	61,500,000.00	61%		3.74	176,215.93	3.75	1,537,287.77	
Senior Bonds:									
CUA FRN @ 3m BBSW + 1.20%	2,000,000.00	2,013,760.00	2%	BBB+	2.99	4,595.07	3.02	40,511.80	22-Dec-17
TMB FRN @ 3m BBSW + 1.05%	2,000,000.00	2,013,200.00	2%	BBB+	3.13	4,326.58	2.88	38,076.72	4-Dec-17
Credit Suisse FRN @ 3m BBSW + 1.05%	0.00	0.00	0%	A	-	0.00	-	32,543.87	24-Aug-18
Newcastle PBS FRN @ 3m BBSW + 1.60%	5,000,000.00	5,067,850.00	5%	BBB+	3.39	13,021.92	3.42	114,594.52	22-Mar-19
CUA FRN @ 3m BBSW + 1.60%	3,000,000.00	3,030,210.00	3%	BBB+	3.40	7,824.66	3.43	68,301.38	1-Apr-19
Westpac FRN @ 3m BBSW + 1.00%	0.00	0.00	0%	AA-	-	0.00	-	1,665.75	10-May-19
CBA FRN @ 3m BBSW + 0.98%	0.00	0.00	0%	AA-	-	0.00	-	36,233.65	18-Jul-19
Bendigo FRN @ 3m BBSW + 0.93%	2,000,000.00	2,010,880.00	2%	A-	2.71	4,165.48	2.75	36,796.70	17-Sep-19
Newcastle PBS FRN @ 3m BBSW + 1.35%	2,000,000.00	2,005,860.00	2%	BBB+	3.13	4,802.19	3.18	42,510.68	7-Apr-20
NAB FRN @ 3m BBSW + 0.80%	5,000,000.00	5,007,400.00	5%	AA-	2.57	9,857.53	2.61	86,960.27	3-Jun-20
Westpac FRN @ 3m BBSW + 0.90%	2,000,000.00	2,014,440.00	2%	AA-	2.67	4,096.44	2.70	36,481.92	28-Jul-20
Bendigo FRN @ 3m BBSW + 1.10%	5,000,000.00	5,016,900.00	5%	A-	2.88	10,981.51	2.88	96,508.00	18-Aug-20
AMP FRN @ 3m BBSW + 1.35%	2,000,000.00	2,027,780.00	2%	A+	3.13	4,770.68	3.12	41,934.24	24-May-21
	30,000,000.00	30,208,280.00	30%		3.00	68,442.06	3.01	673,119.50	
TOTAL PORTFOLIO **	100,136,403.93	100,344,683.93	100%		3.50	250,614.05	3.54	2,265,830.77	
BENCHMARK					1.77		1.84		

North Sydney Council Investment Portfolio as at 28 February 2017

Term	Market Value	%	Wgt. Avg
Working Capital (0-3 Months)	10,636,403.93	11%	1.48%
Short-Term (3-12 Months)	27,526,960.00	27%	3.63%
Short-Medium Term (1-2 Years)	31,000,000.00	31%	3.88%
Medium Term (2-5 Years)	31,181,320.00	31%	3.01%
Long Term (+5 Years)	0.00	0%	0.00%
Total	100,344,683.93	100%	

Performance	Council	AusBond BBI	Outperformance
FYTD	3.54%	1.84%	1.70%
1 year	3.61%	1.98%	1.62%
2 years	3.86%	2.12%	1.75%
3 years	4.06%	2.32%	1.74%
4 years	4.32%	2.44%	1.88%
5 years	4.66%	2.70%	1.97%

Benchmark	Investments
AusBond Bank Bill Index	Cash, Term Deposits, Senior Fixed and Senior FRN's
Investment Horizon	Investments
Working Capital (0-3 Months)	At-Call Accounts, Term Deposits
Short-Term (3-12 Months)	Term Deposits
Short-Medium Term (1-2 Years)	Senior Bonds, Term Deposits
Medium Term (2-5 Years)	Senior Bonds, Term Deposits
Long Term (+5 Years)	N/A

Summary by Credit Rating #	
AAA	0%
AA+	0%
AA	0%
AA-	16%
A+	18%
A	0%
A-	27%
BBB+	27%
BBB	3%
BBB-	0%
NR	9%
100%	



Monthly Investment Report

February 2017

Market

We refer to our more detailed *Economic Commentary* for the month.

International Markets

US markets continued to rally President Trump forecasting “phenomenal” tax reform. US and global indices added 3-5%; the ASX finished over 2% higher.

US 10-year rates finished -9bp tighter at +2.36% p.a. as bond investors question how much stimulus would really affect 2017 (and whether the Federal Reserve would back away from aggressive rate increase guidance). The cash rate was unchanged in February but expected to rise 25bp in March. Local bonds were flat.

Domestic

The RBA left the cash rate unchanged at its meeting in February. Minutes revealed a positive outlook on both global and domestic economies, with 3% growth forecast for 2017 amid soaring commodity prices. A record balance of goods and services (+\$4.7bn) saw the current account improve 62% to -\$3.8bn in Q4. Inbound tourism increased +8.7% in 2016.

Corporate profits were +8.4% higher in Q4, with BHP reporting +\$3.2bn – a massive turnaround from +\$0.4bn a year earlier.

Domestically, data was mixed. Jobs rose +13,500 in January, but full-time employment fell -44,800 jobs. Unemployment was 5.7% in January (-0.1%). Retail sales contracted -0.1%. Building approvals are down -11.4% on the year, indicating another weak year after -25.5% this year.

Other Markets

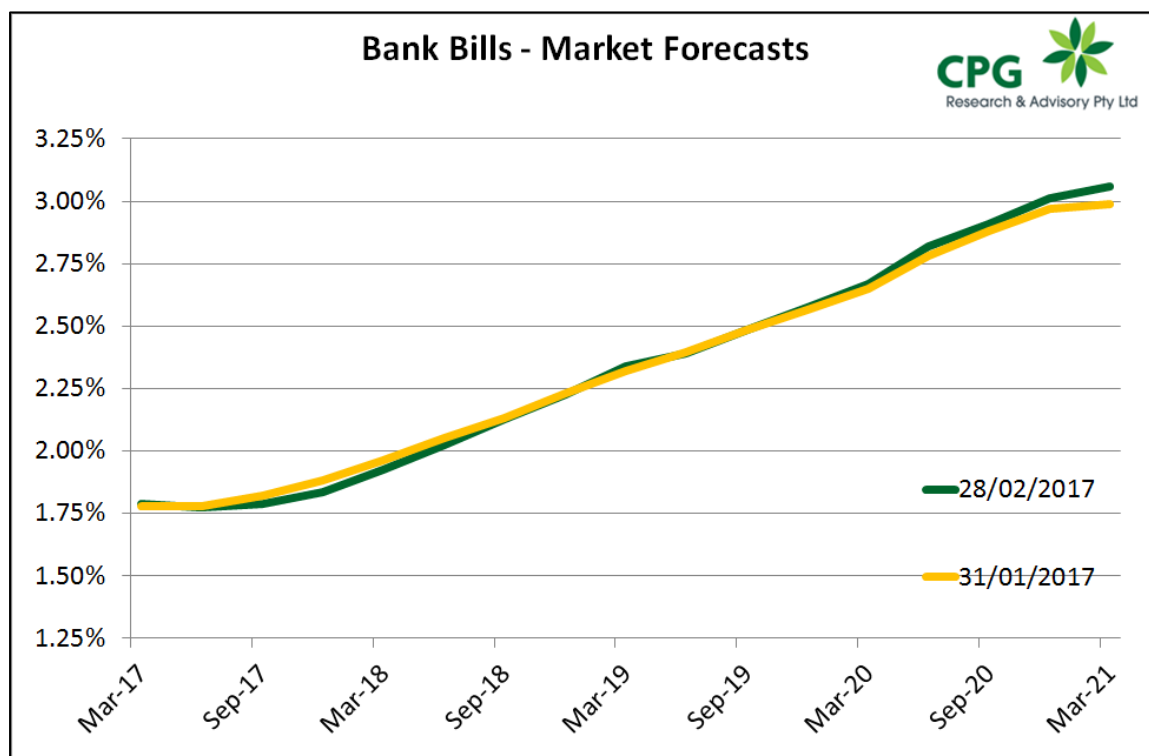
US GDP growth slowed to +1.9% in Q4 (down from +3.5% in Q3) attributable to a large reduction in exports. US Consumer spending slowed in Q4 to +2.5% despite rising auto-sales. Unemployment ticked up to 4.8%. Housing sales were off -10.4% in December.

Eurozone consumer confidence fell to -6.2, as upcoming elections bring the change of more Euro-sceptic governments in France, Netherlands and elsewhere.

WTI oil finished higher at \$54.01/bbl (+2.27%). Gold closed at US\$1257 (+3.97%). Iron Ore continued to soar, finishing at \$87.3 (+6.15%). Base metals were mixed, with Aluminium and Nickel sharply higher but Zinc and Tin weaker.

The AUD firmed +1.60% higher as commodities rallied, at US76.88 cents against a weaker \$US.

Bill futures were little changed across the curve.



Credit Market

Credit spreads narrowed again in February, following other risk assets firmer. Australia rallied, tightening 8bp. Europe and North America were 1bp and 4bp tighter respectively.

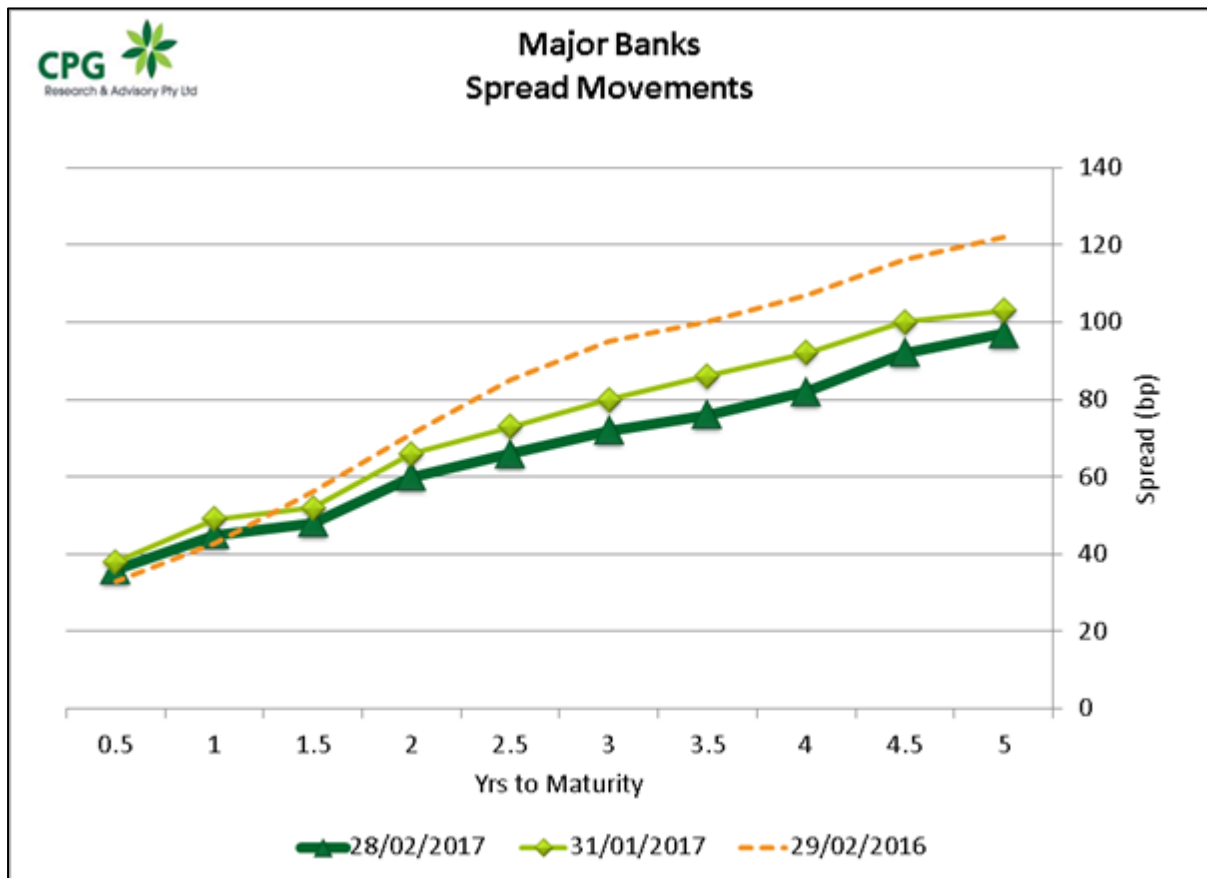
The “Trump rally” continued as President Trump forecast “phenomenal” tax reform - the US stockmarket hit record highs and the Dow Jones closed above 21,000.

Credit Indices	28 Feb 17	31 Jan 17	29 Feb 16
iTraxx Australia 5 Yr CDS	84bp	93bp	157bp
iTraxx European 5 Yr CDS	73bp	74bp	99bp
CDX North American 5 Yr CDS	62bp	66bp	108bp

Source: MarkIt

In the physical market, senior spreads tightened up to 10bp in the 3-4 year part of the curve. This was partly attributed to a new issuance by ANZ at +100bp in late February, which was well received by the market. Other issues such as hybrids have also been oversubscribed and have therefore traded well in the aftermarket.

Strong stockmarket conditions have buoyed most credit sectors.



Council's Portfolio

The portfolio has 9% of investments available at-call and a further 2% of assets maturing within 3 months. Additional short-dated funds have been gradually redeployed into a portfolio now well diversified by term – ahead of what has been a considerable decline in deposit rates.

Approximately 31% of the portfolio is represented as medium-term assets (2-5 years), with capacity now freed up after previously being close to capacity limits.

Council has a growing number of senior FRNs as additional cover for liquidity requirements (access to funds within 2 business days).

Term to Maturity	%	Maximum	Capacity
0-3 months	11%	100%	89%
3-12 months	27%	100%	73%
1-2 years	31%	70%	39%
2-5 years	31%	50%	19%
5+ years	0%	25%	25%

Council's portfolio is currently mainly directed to term deposits (61%) across a broad range of counterparties; credit assets (senior securities) are around 30% of the portfolio.

Over the past few years, our advice has focused on fixed rate deposits as the core investment theme, supplemented by other fixed rate investments. This has been justified by the downtrend in deposit yields, with 2014's longer-dated deposit investments now yielding well above market returns.

Use of FRNs reflects multiple drivers:

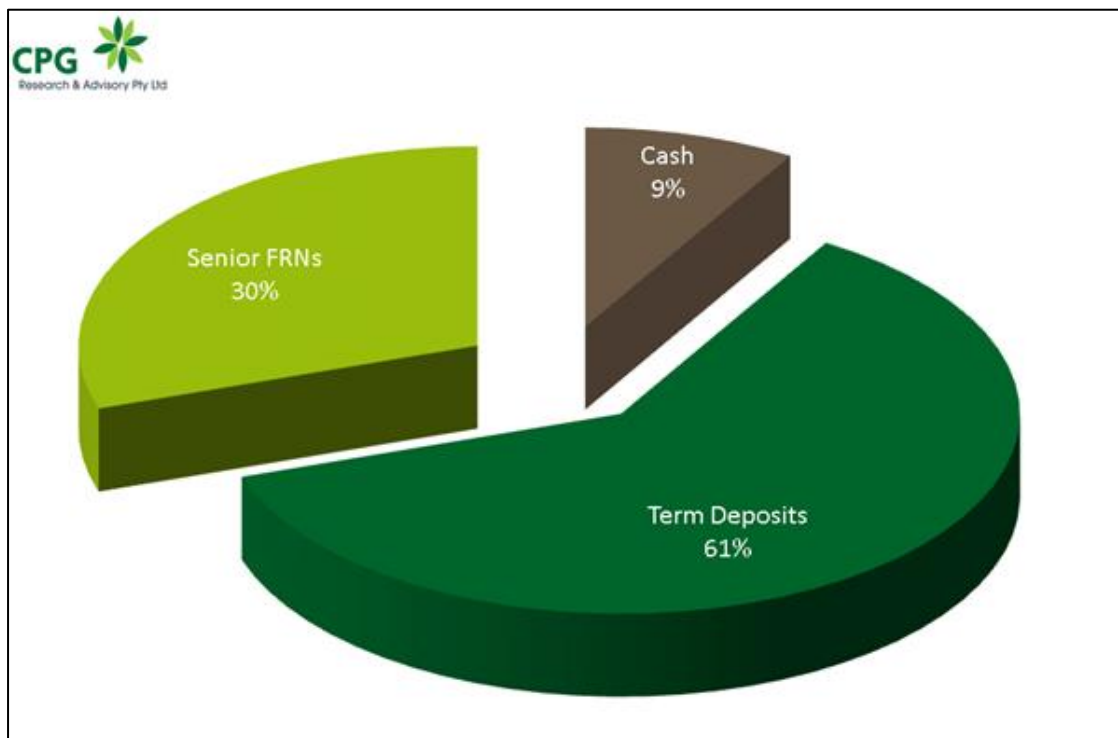
- the desire for **liquid assets** in a portfolio in case of emergency or major spending;
- a view that the **interest rate cycle was fully priced** into shorter deposits;
- **relative spreads** over the holding period (*typically 24-30 months*)

FRNs have been robust through periods of substantial weakness (such as around the Brexit referendum) **although without rallying so far that we would freeze new recommendations.**

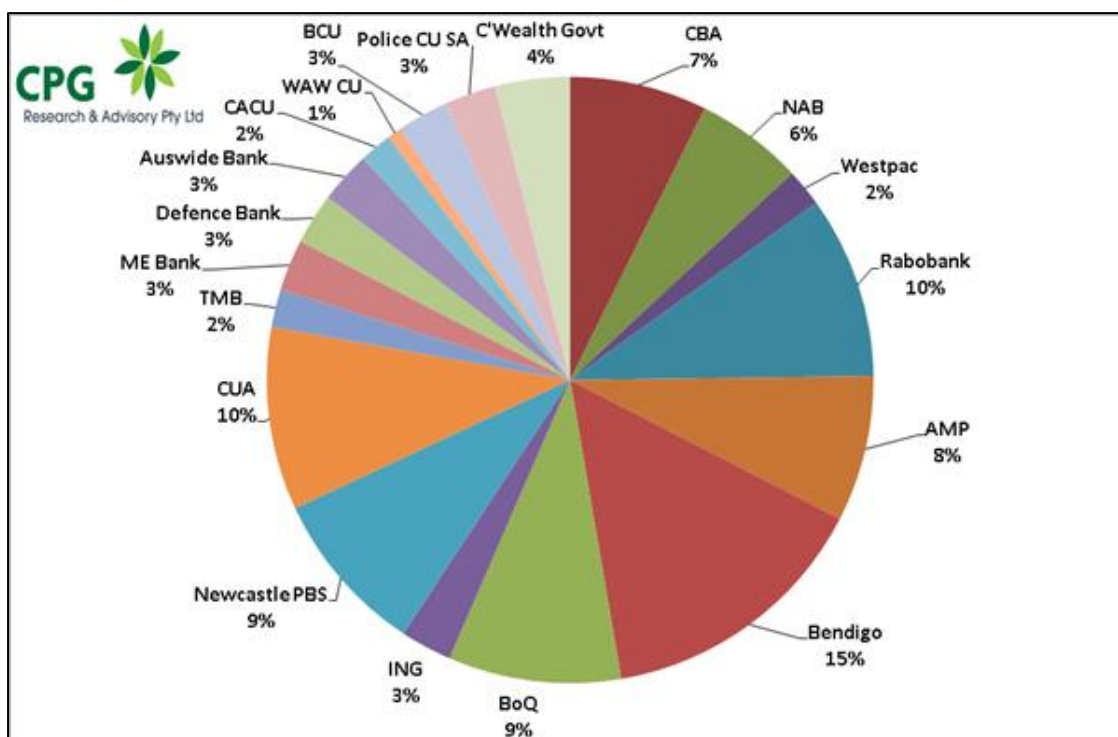
Given the significant re-rating of other risk assets (for example shares and high-yield credit), bank senior FRNs remain good relative value.

The past few months has also seen a severe sell-off in bonds, accelerating from November – with the RBA at least as responsible as the US voters. While worse at the long end, medium term bond yields are also higher, and deposits have tracked them. After we paused on longer-dated T/D recommendations in Q3, the spike in yields created a much steeper curve and rates that more clearly reward for the likely interest rate outlook.

Currently we see value in **both** longer deposits and FRNs. At the long end, rates have risen over ½% from their lows for a 5 year deposit. FRNs also offer solid initial yields with the prospect of additional gains. **We have a positive view on increasing the Medium Term allocation in either major category.**



The investment portfolio is well diversified in complying assets across the entire credit spectrum, with Bendigo, Rabobank, BoQ and CUA dominant:



Credit Quality

The portfolio is diversified from a ratings perspective. Credit quality is diversified and is predominately invested amongst the investment grade ADIs (BBB- or higher), with a slightly smaller allocation to unrated ADIs.

The aggregate allocation to BBB is now freed up after previously being close to capacity limits. The unrated ADIs however remain close to capacity limits (only 2% remaining).

These allocations will be monitored on an ongoing basis. Future investments may need to be directed to the higher rated ADIs (A or higher), although it is also dependent on the movement in the portfolio's balances.

Rating Category	Actual	Per C/Party	Aggregate	Capacity
AAA Govt	4%	100%	100%	96%
AAA	0%	40%	100%	100%
AA	15%	30%	100%	85%
A	44%	15%	60%	16%
BBB	29%	10%	35%	6%
NR ADI	8%	5%	10%	2%

All of these are well within Policy limits.

From time to time, broker specials continue to be offered with some BBB rated and unrated Credit Unions paying an additional premium above leading direct rates – **pricing is generally quite favourable, but for short terms**. This is covered in the daily emails and our advice at the time of investment.

Compliance

We have tested the portfolio provided against Council's current investment policy and report the following:

All individual counterparty exposures comply with the Policy, although Bendigo-Adelaide Bank and CUA remain very close to capacity limits.

ADI	Exposure	FCS	Net	Rating	Policy Limit	Actual	Capacity
ANZ	\$0	\$0	\$0	AA-	30%	0%	\$30,103,407
CBA	\$7,600,243	\$250,000	\$7,350,243	AA-	30%	7%	\$22,753,165
NAB	\$6,007,400	\$250,000	\$5,757,400	AA-	30%	6%	\$24,346,007
Westpac	\$2,014,440	\$0	\$2,014,440	AA-	30%	2%	\$28,088,967
Rabobank	\$10,000,000	\$250,000	\$9,750,000	A+	15%	10%	\$5,301,704
AMP	\$8,063,948	\$250,000	\$7,813,948	A+	15%	8%	\$7,237,755
Suncorp	\$0	\$0	\$0	A+	15%	0%	\$15,051,704
Bendigo	\$15,027,780	\$250,000	\$14,777,780	A-	15%	15%	\$273,924
BoQ	\$9,500,000	\$250,000	\$9,250,000	A-	15%	9%	\$5,801,704
ING	\$3,000,000	\$250,000	\$2,750,000	A-	15%	3%	\$12,301,704
Newcastle PBS	\$9,073,710	\$250,000	\$8,823,710	BBB+	10%	9%	\$1,210,759
CUA	\$10,043,970	\$250,000	\$9,793,970	BBB+	10%	10%	\$240,499
TMB	\$2,013,200	\$0	\$2,013,200	BBB+	10%	2%	\$8,021,269
ME Bank	\$3,000,000	\$250,000	\$2,750,000	BBB+	10%	3%	\$7,284,469
Defence Bank	\$3,000,000	\$250,000	\$2,750,000	BBB+	10%	3%	\$7,284,469
Auswide Bank	\$3,000,000	\$250,000	\$2,750,000	BBB	10%	3%	\$7,284,469
CACU	\$2,000,000	\$250,000	\$1,750,000	NR	5%	2%	\$3,267,235
WAW CU	\$1,000,000	\$250,000	\$750,000	NR	5%	1%	\$4,267,235
BCU	\$3,000,000	\$250,000	\$2,750,000	NR	5%	3%	\$2,267,235
Police CU SA	\$3,000,000	\$250,000	\$2,750,000	NR	5%	3%	\$2,267,235
C'wealth Govt	\$100,344,691		\$96,344,691	AAA	100%	96%	
Total	\$100,344,691	\$4,000,000	\$96,344,691	AAA	100%	4%	

^ Under the Financial Claims Scheme (FCS), the first \$250,000 is guaranteed by the Federal Government (rated AAA by S&P) per investor, per ADI.

Subsidiaries such as Bank of Queensland Specialist Bank are grouped in the exposures of the parent (Bank of Queensland, rated A-).

From May 2015, new Rabobank Australia deposits are not guaranteed by the global group, but existing deposits have their guarantee grandfathered. They are generally not accepting new investments or rollovers from institutional investors.

Performance Returns

Council's Performance as at 28 February 2017

Performance	Council	AusBond BBI	Outperformance
1 month	3.50%	1.77%	1.73%
3 months	3.46%	1.78%	1.67%
FYTD	3.54%	1.84%	1.70%
1 year	3.61%	1.98%	1.62%
2 years	3.86%	2.12%	1.75%
3 years	4.06%	2.32%	1.74%
4 years	4.32%	2.44%	1.88%
5 years	4.66%	2.70%	1.97%

The total investment portfolio had another strong month, returning **+3.50% p.a. for the month of February**, nearly doubling the benchmark AusBond Bank Bill Index¹, which returned +1.77% p.a.

Council's returns, while lower in absolute terms than historically the case, remains very strong compared to most short deposits rolling in the mid-high 2%'s. Even the highest 3-year deposit today remains around 3.2%.

The portfolio's performance continues to be anchored by the longer-dated deposits, particularly those invested above 4%. FRNs, purchased at attractive margins, have also contributed positively to overall performance.

Cash continues to be a drag on performance after the RBA cut rates twice in May and August 2016. This can be mitigated through a switch into higher yielding accounts such as AMP's 31 day notice account paying cash rate + 0.75%, which includes CPG's 10bp rebate. The account requires 31 days notice in return for the additional yield – it is not a substitute for at-call money.

¹ Previously UBS Bank Bill Index - the sale of the UBS index to Bloomberg, and subsequent change of names, is now effective.

Term Deposits

At month-end, deposits accounted for approximately 61% of the total investment portfolio. The weighted average duration of the deposit portfolio stood at approximately **1.2 years** - having been significantly lengthened (compared to benchmark) during the RBA's easing cycle over the past few years.

A longer duration will provide protection to Council's budgeted income over the coming year, which we will be looking to support over the next 12 months. ***An average yield of 3.75% p.a. (unchanged from the previous month) remains much higher than any deposit available today. It continues to yield around 2½ times the prevailing cash rate!***

It is inevitable that returns will again ease from here as prevailing reinvestment rates are much lower than preceding years.

During the month, no deposits matured and there were no newly established deposits.

Across the longer-end of the curve, the highest 4 year fixed deposit margins remains around +120bp over bank bills, while the highest 5 year fixed deposit is slightly lower at around +110bp over bank bills. Absolute terms in the long-end of the curve have risen with the rise in the bond market since the end of Q3 2016. Given the longer-term interest rate outlook, **we believe there is good value and visibility by locking in the top 4 year rate of around 3.60% p.a. offered by BoQ (A-).**

This has seen the deposit curve steepen sharply over the past few months and investors are rewarded for illiquidity, with some medium-term durations factoring in significantly more upside risk than we build into cash rate scenarios. **We recommend medium-term T/Ds at current levels, after a period of a "Neutral" view.**

Some above market rates ("specials") continue to be offered by the "BBB" and unrated ADIs, often through the broker intermediaries.

We refer to the detailed analysis in our ***February Fixed Interest Analytics***.

Securities (FRNs)

The long-end of the curve amongst the wholesale senior bank FRNs tightened by up to +10bp during February. They continued to tighten during the first week of March. Overall, they remain relatively attractive value through the cycle – around mid-range when assessed against the post-GFC trading range.

Compared to a year earlier, the new issue level is just around 10-15bp tighter.

We recommend selling any senior major bank FRNs maturing in or before 2019 as most are marked less than +70bp and the curve remains relatively steep. Lower rated institutions tend to see spreads converge only as they shorten very close to maturity – we flag the final year as the likely exit point for those. Still, switching may well be recommended opportunistically.

Apart from providing diversification and additional liquidity in a portfolio, an FRN strategy has been lucrative. Issue yields have fluctuated, but the tightening towards maturity has worked consistently.

Primary issues continue to be favoured over secondary market offers in the wholesale market.

CBA and Westpac were the first to issue a new 5 year deal this year at +111bp, which has tightened to around +95bp in the secondary market. ANZ came out with their new 5 year issue at +100bp in late February. This is currently the likely level of where a new major bank FRN would be issued at.

For new issues, the regional ADIs (rated A or BBB) naturally offer a higher spread compared to the major banks due to their lower credit rating. Our FRN analytics suggest that the respective curves are relatively fair, with higher spread but greater difficulty extracting capital gains from regional bank FRNs. However, again the new issue discount provides additional value to investors.

Private placement FRNs or secondary market ‘taps’ can sometimes be offered, usually at a premium yield to the wholesale secondary market although we note they are generally less liquid due to their smaller issue sizes and daily turnover. The most recent example was a new 3 year FRN at +145bp (\$30m printed in total) from Greater Bank (BBB+) in mid February.

Heritage retail trade in a volatile range, but **at time of writing are extremely cheap.** With around 3 months to run, brokerage knocks 10-15bp out of the return, with the bigger problem being to secure volume without unduly moving a lightly traded security. At current levels, we suggest investors buy as a higher risk-return current asset, although it is **better suited to existing holders** given the risk of being left with a small parcel if an order only partly fills. The security has swung wildly in both directions recently, on low volume, particularly during its “ex-interest” period.

We recommend that Council retain its FRN portfolio at this stage, and add to it in combination with longer deposits. In a fairly stable credit environment, we look for an exit opportunity towards the midpoint of a security’s life to maximise the potential gain, and will inform Council accordingly.

Fixed Interest Market Background

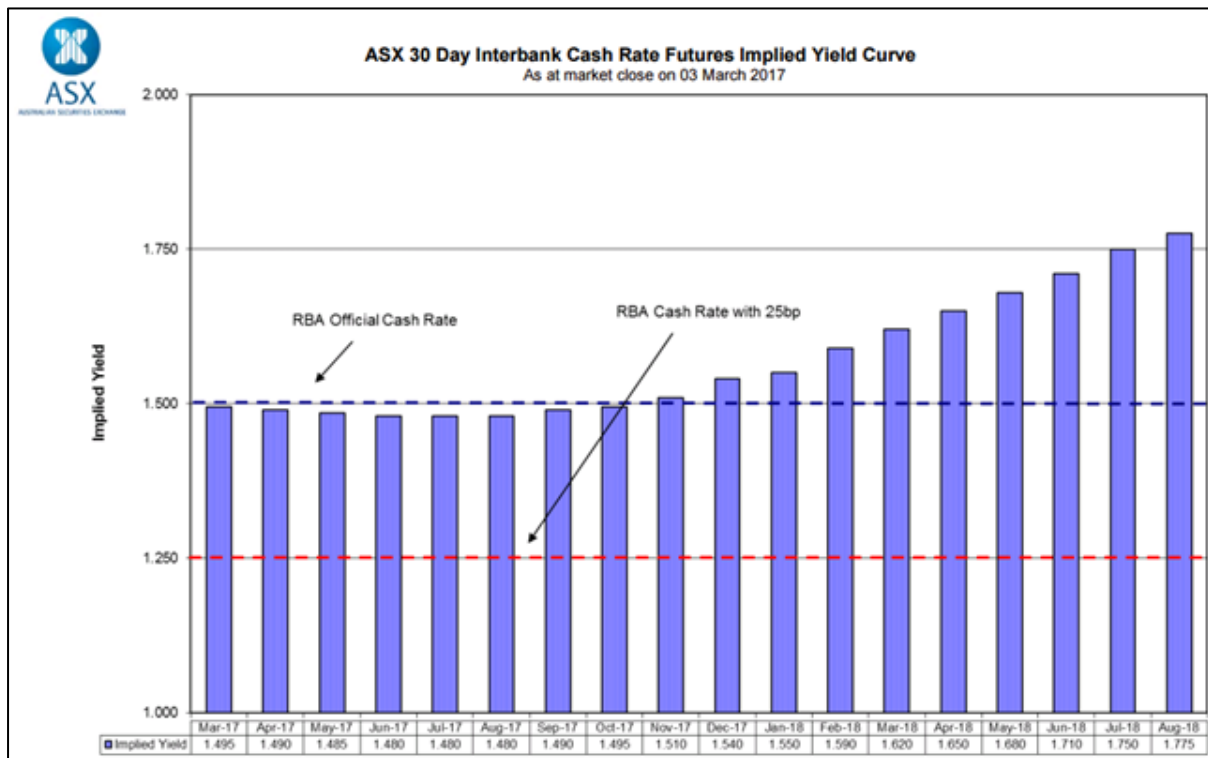
Investor sentiment strengthened, with the major US stockmarket indices recently setting new record highs.

Market pricing for a March rate hike in the US firmed, with the US Fed fund futures now pricing in around 95% chance. Fed Chair Yellen said *"At our meeting later this month, the committee will evaluate whether employment and inflation are continuing to evolve in line with our expectations, in which case a further adjustment of the federal funds rate would likely be appropriate."* She added that *"the process of scaling back accommodation likely will not be as slow as it was in 2015 and 2016."*

The RBA continued with its broadly upbeat commentary in the minutes of the RBA meeting in February. There were not many new developments to add after the Statement on Monetary Policy released earlier in the month. Indeed, the more positive outlook on the global and domestic economies was mostly repeated. The RBA's broadly upbeat tone, expectation that growth will pickup to a pace above potential and expectation that inflation will also pickup, suggests that the RBA is not in the mindset to lower official interest rates any time soon.

Domestic gross domestic product (GDP) rose by 1.1% in the December quarter of 2016. It was a sharp bounce back after GDP shrunk by -0.5% in the September quarter. The Australian economy has now notched 102 consecutive quarters of growth (or 25½ years) without a recession and this run is set to continue through 2017.

The market is still pricing in the very small possibility of a rate cut in the short-term. In contrast, a rate rise is almost fully factored in by Q3 2018. Our base case scenario is for the RBA to remain on hold over 2017.



Source: SFE / ASX

Portfolio Listing & Performance

North Sydney Council Investment Portfolio as at 28 February 2017									
Trading Account:	Investment Face Value	Investment Market Value	%	S&P Rating *	Net Returns - 1 Month Return*	Net Returns - 1 Month Income^	Net Returns - FYTD Return	Net Returns - FYTD Income^	Maturity
CBA Trading Account - General Fund	3,095,648	3,095,648	3%	AA-	0.80	\$1,268	1.10	\$10,658	At Call
CBA Business On-Line Saver	4,500,000	4,500,000	4%	AA-	1.05	\$2,953	1.05	\$28,524	At Call
AMP 31-day Notice Account	1,036,168	1,036,168	1%	A+	2.30	\$1,746	2.57	\$15,861	31-Mar-17
CBA Cash Management Account	4,600	4,600	0%	AA-	1.65	\$0	1.71	\$9	At Call
	8,636,417	8,636,417	9%		1.11	\$5,967	1.25	\$55,051	
Term Deposits:									
CUA @ 3.05%	2,000,000	2,000,000	2%	BBB+	3.05	\$4,679	3.05	\$40,611	23-Mar-17
Rabobank @ 5.70%	2,000,000	2,000,000	2%	A+	5.70	\$8,745	5.70	\$75,896	6-Jun-17
Auswide Bank @ 2.90%	3,000,000	3,000,000	3%	BBB	2.90	\$6,674	2.90	\$41,712	7-Jun-17
AMP @ 2.90%*	1,000,000	1,000,000	1%	A+	2.90	\$2,225	2.90	\$19,307	28-Aug-17
BoQ @ 4.90%	3,000,000	3,000,000	3%	A-	4.90	\$11,277	4.90	\$97,866	28-Aug-17
BCU @ 4.00%	2,000,000	2,000,000	2%	NR	4.00	\$6,137	4.00	\$53,260	28-Aug-17
Bendigo TD @ 2.90%	3,000,000	3,000,000	3%	A-	2.90	\$6,674	2.90	\$57,921	30-Aug-17
Bendigo TD @ 2.90%	3,000,000	3,000,000	3%	A-	2.90	\$6,674	2.90	\$57,921	4-Sep-17
CUA @ 3.75%	3,000,000	3,000,000	3%	BBB+	3.75	\$8,630	3.75	\$74,897	11-Sep-17
Bendigo TD @ 2.92%	2,000,000	2,000,000	2%	A-	2.92	\$4,480	2.92	\$38,880	15-Sep-17
BoQ @ 4.70%	1,000,000	1,000,000	1%	A-	4.70	\$3,605	4.70	\$31,290	27-Sep-17
BoQ Specialist @ 5.60%	500,000	500,000	0%	A-	5.60	\$2,148	5.60	\$18,641	2-Nov-17
AMP @ 3.20%*	4,000,000	4,000,000	4%	A+	3.20	\$9,819	3.20	\$85,216	5-Mar-18
Community Alliance CU @ 2.90%	2,000,000	2,000,000	2%	NR	2.90	\$4,449	2.90	\$27,014	13-Mar-18
Rabobank @ 4.25%	2,000,000	2,000,000	2%	A+	4.25	\$6,521	4.25	\$56,589	20-Aug-18
Rabobank @ 4.05%	6,000,000	6,000,000	6%	A+	4.05	\$18,641	4.05	\$161,778	28-Aug-18
BCU @ 3.00%	1,000,000	1,000,000	1%	NR	3.00	\$2,301	3.00	\$15,123	29-Aug-18
Defence Bank @ 2.90%	3,000,000	3,000,000	3%	BBB+	2.90	\$6,674	2.90	\$41,712	7-Sep-18
Police CU @ 2.90%	2,000,000	2,000,000	2%	NR	2.90	\$4,449	2.90	\$27,808	7-Sep-18
Police CU @ 3.05%	1,000,000	1,000,000	1%	NR	3.05	\$2,340	3.05	\$20,305	10-Sep-18
BoQ @ 5.00%	3,000,000	3,000,000	3%	A-	5.00	\$11,507	5.00	\$99,863	29-Oct-18
WAW CU @ 3.10%	1,000,000	1,000,000	1%	NR	3.10	\$2,378	3.10	\$6,710	12-Dec-18
ME Bank @ 5.10%	3,000,000	3,000,000	3%	BBB+	5.10	\$11,737	5.10	\$101,860	14-Feb-19
JNG @ 4.95%	3,000,000	3,000,000	3%	A-	4.95	\$11,392	4.95	\$98,864	18-Feb-19
Newcastle PBS @ 2.90%	2,000,000	2,000,000	2%	BBB+	2.90	\$4,449	2.90	\$27,808	6-Sep-19
NAB Flexi Deposit @ 3m BBSW + 1.05%	1,000,000	1,000,000	1%	AA-	2.82	\$2,163	3.53	\$22,324	12-Dec-19
BoQ @ 3.55%	2,000,000	2,000,000	2%	A-	3.55	\$5,447	3.55	\$15,367	11-Dec-20
Expired Deposits - Financial Year	-	-	-	-	-	\$0	-	\$121,889	Expired
	61,500,000	61,500,000	61%		3.74	\$176,216	3.75	\$1,538,434	
Senior Bonds:									
CUA FRN @ 3m BBSW + 1.20%	2,000,000	2,013,760	2%	BBB+	2.99	\$4,595	3.02	\$40,512	22-Dec-17
TMB FRN @ 3m BBSW + 1.05%	2,000,000	2,013,200	2%	BBB+	3.13	\$4,327	2.88	\$38,077	4-Dec-17
Credit Suisse FRN @ 3m BBSW + 1.05%	-	-	0%	A	-	\$0	-	\$31,533	24-Aug-18
Newcastle PBS FRN @ 3m BBSW + 1.60%	5,000,000	5,067,850	5%	BBB+	3.39	\$13,022	3.42	\$114,595	22-Mar-19
CUA FRN @ 3m BBSW + 1.60%	3,000,000	3,030,210	3%	BBB+	3.40	\$7,825	3.43	\$68,594	1-Apr-19
Westpac FRN @ 3m BBSW + 1.00%	-	-	0%	AA-	-	\$0	-	\$13,241	10-May-19
CBA FRN @ 3m BBSW + 0.98%	-	-	0%	AA-	-	\$0	-	\$55,273	18-Jul-19
Bendigo FRN @ 3m BBSW + 0.93%	2,000,000	2,010,880	2%	A-	2.71	\$4,165	2.75	\$36,797	17-Sep-19
Newcastle PBS FRN @ 3m BBSW + 1.35%	2,000,000	2,005,860	2%	BBB+	3.13	\$4,802	3.18	\$42,511	7-Apr-20
NAB FRN @ 3m BBSW + 0.80%	5,000,000	5,007,400	5%	AA-	2.57	\$9,858	2.61	\$86,960	3-Jun-20
Westpac FRN @ 3m BBSW + 0.90%	2,000,000	2,014,440	2%	AA-	2.67	\$4,096	2.70	\$36,482	28-Jul-20
Bendigo FRN @ 3m BBSW + 1.10%	5,000,000	5,016,900	5%	A-	2.88	\$10,982	2.88	\$96,508	18-Aug-20
AMP FRN @ 3m BBSW + 1.35%	2,000,000	2,027,780	2%	A+	3.13	\$4,771	3.12	\$41,934	24-May-21
	30,000,000	30,208,280	30%		3.00	\$68,442	3.01	\$703,016	
TOTAL PORTFOLIO **	100,136,417	100,344,697	100%		3.50	\$250,625	3.54	\$2,296,501	
BENCHMARK					1.77		1.84		

Disclaimer

The information provided in this document is intended for clients of CPG Research & Advisory only and does not constitute a recommendation or an offer to invest. Market sections of this document are descriptive and do not take into account the investment objectives, financial situation or particular needs of any particular investor. Before making an investment decision or acting on any of the information or recommendations contained in this report, the investor should consider whether such recommendation is appropriate given the investor's particular investment needs, objectives and financial circumstances. We recommend you consult your CPG adviser for updated advice that addresses your specific needs and situation before making investment decisions.

All information and recommendations expressed herein constitute judgements as of the date of this report and may change without notice. Staff and associates may hold positions in the investments discussed, and these could change without notice.