Policy

Investment Policy

Responsible Manager (Title)	Manager Finance & Supply		
Adopted by Council	Date:	Minute Number:	
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Community Plan Linkage	**5 Leadership**		
	5.2 We will have an effective and efficient organisation		
	5.2.1 Operates in a financially responsible and sustainable manner		

1 Purpose

The purpose of this document is to establish the framework within which investment principles are to apply to the investment of Council funds. It details:

1. Council Funds covered by this Investment Policy Statement;
2. Council's objectives for its investment portfolio/s;
3. How investments are to be undertaken;
4. The applicable risks to be managed;
5. Any constraints and other prudential requirements to apply to the investments of Funds having regard to the applicable legislation and regulations governing Council investment;
6. The manner in which compliance with the Policy will be monitored and reported; and
7. Appropriate benchmarks for each category of investments.

2 Definitions

Act	*Local Government Act 1993 (NSW)*.
ADI	Authorised Deposit-Taking Institutions (ADIs) are corporations that are authorised under the *Banking Act 1959* (C'wlth) to take deposits from customers and regulated by APRA.
AusBond BBI	The Bank Bill Index represents the performance of a notional rolling parcel of bills averaging 45 days and is the widely used benchmark for local councils and other institutional cash investments.
Bill of Exchange	A bill of exchange is an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand, or at a fixed or determinable future time, a sum certain in money to or to the order of a specified person, or to bearer. These can be underwritten by banks, to become "bank bills" on which the benchmark return is calculated.
BBSW	The Bank Bill Swap reference rate (BBSW) is the average of mid-rate bank-bill quote from brokers on the BBSW Panel. The BBSW is calculated daily. Floating rate securities are most commonly reset quarterly to the 90-day BBSW.
Council Funds	Surplus monies that are invested by Council in accordance with section 625 of the Act.
Debenture	A debenture is a document evidencing an acknowledgement of a debt, which a company has created for the purposes of raising capital. Debentures are issued by companies in return for medium and long-term investment of funds by lenders.
FRN	A Floating Rate Note (FRN) is a medium to long term fixed interest investment where the coupon is a fixed margin ("coupon margin") over a benchmark, also described as a "floating rate". The benchmark is usually the BBSW and is reset at regular intervals – most commonly quarterly.
Grandfathered	Investments held by Council that were previously allowed under the Minister's Order but were Grandfathered (*i.e.* eligible to retain but not add to or restructure existing investments) when the NSW State Government changed the list of Approved Investments as a result of the Cole enquiry reflected in the Ministerial Order dated 31/7/2008 and the revised order dated 12/1/2011. (It would also apply to any future similarly structured regulatory change, or any assets that do not comply by virtue of a Policy change.)
LGGR	*Local Government (General) Regulation 2005 (NSW)*.
OLG	NSW Office of Local Government (Department of Planning, Industry and Environment), including historical references to previous Divisions or Departments.
TCorp/TCorpIM	New South Wales Treasury Corporation (NSW TCorp), including the TCorp Investment Management arm which manages the TCorpIM Funds.

3 Background/legislative requirements

All investments are to comply with the following:

1. *Local Government Act 1993 (NSW);*
2. *Local Government (General) Regulation 2005 (NSW);*
3. Ministerial Investment Order;
4. *Trustee Amendment (Discretionary Investments) Act (1997)* – Section 14;
5. Local Government Code of Accounting Practice and Financial Reporting;
6. Australian Accounting Standards;
7. Office of Local Government Investment Policy Guidelines; and
8. Office of Local Government Circulars.

4 Policy statement

Investment Objective

The purpose of this Policy is to provide a framework for the optimum investment of Clarence Valley Council's Funds at the most favourable terms and rates of return available to it at the time to maximise returns, whilst having due consideration of risk, liquidity and security for its investments.

While exercising the power to invest, consideration is to be given to the preservation of capital, liquidity and the return of investment. Council therefore has several primary objectives for its investment portfolio:

1. Compliance with legislation, regulations, the prudent person tests of the Trustee Act and best practice guidelines;
2. The preservation of the amount invested;
3. To ensure there is sufficient liquid funds to meet all reasonably anticipated cash flow requirements; and
4. To generate income from the investment that exceeds the performance benchmarks mentioned later in this document.

5 Implementation

5.1 Effective Date and Investment Strategy

The effective date of this Investment Policy is the date it is adopted by Council and will be reviewed at regular twelve monthly intervals, or when either changes in regulation or market conditions necessitate a review.

Council's Investment **Strategy** will run in conjunction (a separate document) with its Investment **Policy** and will outline:

1. Councils current cash flow expectations and the implications for deviations from a long-term liquidity profile;
2. Diversification: the allocation of investment type, credit quality, counterparty exposure and term to maturity profile;
3. Market conditions and the appropriate responses – particularly relative positioning within the limits outlined in this policy;
4. Relative return outlook, risk-reward considerations, assessment of the market cycle and hence constraints on risk; and
5. Appropriateness of overall investment types for Council's portfolio.

The Investment Strategy will be reviewed at regular twelve monthly intervals, or as required in the event of legislative change or as a result of significantly changed economic/market conditions.

Council is in regular contact with its advisors and is able to adjust strategy as market conditions dictate.

5.2 Prudent Person Standard

The investments will be managed with the care, diligence and skill that a prudent person would exercise. As trustees of public monies, officers are to manage Council's investment portfolios to safeguard the portfolio in accordance with the spirit of this Investment Policy and not for speculative purposes.

5.3 Ethics and Conflicts of Interest

Officers shall refrain from personal activities that would conflict with the proper execution and management of Council's investment portfolio. This policy requires officers to disclose any conflict of interest to the General Manager.

Independent advisors are also to declare that they have no actual or perceived conflicts of interest and receive no inducements in relation to Council's investments, as outlined more fully in section 5.8 *Investment Advisor*.

5.4 Authorised Investments

All investments must be denominated in Australian Dollars. Authorised Investments are limited to those allowed by the Ministerial Investment Order and include:

1. Commonwealth / State / Territory Government securities *e.g.* bonds;
2. Interest bearing deposits / senior securities issued by an eligible ADI;
3. Bills of Exchange (< 200 days duration) guaranteed by an ADI;
4. Debentures issued by a NSW Council under Local Government Act 1993 (NSW);
5. Deposits with NSW TCorp &/or Investments in NSW TCorpIM Funds;
6. Existing investments grandfathered under the Ministerial Investment Order; and
7. Any investment in TCorpIM Funds other than Cash and Short-Term Income, while permitted by the Order, can only be made after Council approval – reflecting the greater risk of moving outside traditional bank and government fixed interest.

5.5 Prohibited Investments

This investment policy prohibits the following types of new investment[1]:

1. Derivative based instruments;
2. Principal only investments or securities that provide potentially nil or negative cash flow;
3. Stand alone securities issued that have underlying futures, options, forwards contracts and swaps of any kind;
4. Investment trusts other than TCorpIM Funds, even where the trusts adhere to the Minister's Order fully; and
5. Any other investment written out of the Minister's Order.

This policy also prohibits the use of leveraging (borrowing to invest) of an investment. However, nothing in the policy shall prohibit the short-term investment of loan proceeds where the loan is raised for non-investment purposes and there is a delay prior to the expenditure of loan funds.

[1] Prohibited investments are not limited to the list above and extend to any investment carried out for speculative purposes.

5.6 Risk Management Guidelines

Investments obtained are to be considered in light of the following key criteria:

1. **Preservation of Capital** – the requirement for preventing losses in an investment portfolio's total value;
2. **Legal/Fidelity** – avoiding loss of title through failure of internal action or inaction;
3. **Credit Risk** – the risk that a party or guarantor to a transaction will fail to fulfil its obligations. In the context of this document it relates to the risk of loss due to the failure of an institution/entity with which an investment is held to pay the interest and/or repay the principal of an investment;
4. **Diversification** – the requirement to place investments in a broad range of products so as not to be over exposed to a particular sector of the investment market;

8. **Liquidity Risk** – the risk an institution runs out of cash, is unable to redeem investments at a fair price within a timely period, and thereby Council incurs additional costs (or in the worst case is unable to execute its spending plans);
9. **Market Risk** – the risk that fair value or future cash flows will fluctuate due to changes in market prices, or benchmark returns will unexpectedly overtake the investment's return;
10. **Maturity Risk** – the risk relating to the length of term to maturity of the investment. The longer the term, the greater the length of exposure and risk to market volatilities; and
11. **Rollover Risk** – the risk that income will not meet expectations or budgeted requirement because interest rates are lower than expected in future.

5.7 Third Party Suppliers and Dealers

Council will structure its affairs in order to be economical in its investment management costs, favouring dealing direct in its fixed interest (or, where intermediated, arrangements that result in a rebate of brokerage) where possible.

At times, it will be advantageous to deal with third parties that are remunerated on a transaction rather than retainer basis. Council will use such suppliers where to its advantage, and have regard to the "best execution" test in its Investment Policy. Specifically, Council will have regard to:

1. Administrative cost savings;
2. Ability to access higher (retail) rates where exceeding the direct transaction costs;
3. Access to ADIs that would not normally have an institutional direct channel;
4. Limited access or IPO deals, or other secondary market opportunities that are only available from specific sources; and
5. The costs of other distribution channels that do not involve transaction remuneration.

Council will take steps to ensure that:

6. Any suppliers used are appropriately licensed, reputable and capable;
7. Funds and identification data are sufficiently secured;
8. Third party arrangements do not materially worsen Council's credit risks by creating exposure to the dealer as counterparty; and

9. Remuneration arrangements are reasonable and transparent, whether paid by Council or by the issuer directly.

5.8 Investment Advisor

An investment advisor engaged by the Council must be licensed by the Australian Securities and Investment Commission. The advisor must be independent and must confirm in writing that they have no actual or potential conflict of interest in relation to investment products being recommended and is free to choose the most appropriate product within the terms and conditions of investment policy. This includes receiving no commissions or other benefits in relation to the investments being recommended or reviewed, unless such remuneration is rebated 100% to Council.

5.9 Accounting

Council will comply with appropriate accounting standards in valuing its investments and quantifying its investment returns.

In addition to recording investment income according to accounting standards, published reports may show a break-down of its duly calculated investment returns into realised and unrealised capital gains and losses, and interest.

Other relevant issues will be considered in line with relevant Australian Accounting Standards, such as discount or premium, designation as held-to-maturity or on a fair value basis and impairment.

5.10 Safe Custody Arrangements

Where necessary, investments may be held in safe custody on Council's behalf, as long as the following criteria are met:

1. Council must retain beneficial ownership of all investments;
2. Adequate documentation is provided, verifying the existence of the investments at inception, in regular statements and for audit;
3. The Custodian conducts regular reconciliation of records with relevant registries and/or clearing systems; and
4. The Institution or Custodian recording and holding the assets will be:
    a. The Custodian nominated by NSW TCorp for NSW TCorpIM Funds;
    b. Austraclear;
    c. An institution with an investment grade Standard and Poor's, Moody's or Fitch rating; or
    d. An institution with adequate insurance, including professional indemnity insurance and other insurances considered prudent and appropriate to cover its liabilities under any agreement.

5.11 Investments in Financial Institutions which Support the Fossil Fuel Industry

Subject to consideration of the Risk Management Guidelines of this Policy, preference may be given to financial institutions that publicly state that they do not invest in or finance the fossil fuel industry if:

1. The investment is compliant with Council's Investment Policy;
2. The investment rate of return is equivalent to or more favourable to Council relative to other similar investments that may be offered to Council at the time of investment;
3. It does not increase the overall risk of Council's investment portfolio and reduce the diversification with regards to counterparty, credit quality and its maturity profile.

5.12 Credit Quality Limits

The portfolio credit guidelines to be adopted will reference the Standard & Poor's (S&P) ratings system criteria and format - however, references to the Minister's Order also recognises Moody's and Fitch Ratings and any of the three ratings may be used where available. During "split ratings" (different agencies assigning different rating bands), existing investments are assessed at the highest rating, but new investments must be tested against the lower rating.

However, the primary control of credit quality is the prudential supervision and government support and explicit guarantees of the ADI sector, not ratings.

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

Long Term Rating Range (or Moody's equivalent)	**Maximum Holding**
AAA Category	100%
AA Category or major banks*	100%
A Category	60%
BBB Category	50%

*For the purpose of this Policy, "major banks" are currently defined as:

The ADI deposits or senior guaranteed principal and interest ADI securities issued by the major Australian banking groups:

1. Australia and New Zealand Banking Group Limited
2. Commonwealth Bank of Australia
3. National Australia Bank Limited
4. Westpac Banking Corporation

including ADI subsidiaries whether or not explicitly guaranteed, and brands (such as St George).

Council may ratify an alternative definition from time to time.

Products with a guarantor or security can have a higher rating than the issuer.

Rating categories may be deduced from a parent where a subsidiary is not explicitly rated. Where appropriate, such as TCorpIM fixed interest funds, rating quality is based on the underlying investment mix. TCorpIM Cash is treated as AA+ category, and Short Term Income Fund as AA-.

Credit ratings are monitored regularly by Finance staff to ensure ongoing compliance. Investments with credit ratings downgraded to an extent that they no longer comply will be assessed for divestment as soon as practicable, in accordance with the grandfathering provisions of this policy.

In the event of disagreement between agencies as to the rating ("split ratings") Council shall use the higher in assessing compliance with portfolio Policy limits, but for conservatism shall apply the lower in assessing new purchases.

5.13 Counterparty Limits

Exposure to individual counterparties/financial institutions will be restricted by their rating so that single entity exposure is limited, as detailed in the table below. It excludes any government guaranteed investments.

This table does not apply to any managed fund or structured investment where it is not possible to identify a single counterparty exposure.

Individual Institution or Counterparty Limits

Long Term Rating Range (or Moody's equivalent)	**Limit**
AAA Category[2]	40%
AA Category or major banks*	30%
A Category	15%
BBB Category	15%

The definitions are as in the previous section.

[2] Commonwealth Government and Government-guaranteed deposits are included in this category to the extent of the guarantee and not according to the bank's actual rating, but without any upper limit applying to the government as counterparty.

5.14 Investment Horizon Limits

Council's investment portfolio shall be structured around the time horizon of investment to ensure that liquidity and income requirements are met.

"Horizon" represents the intended minimum term of the investment, which can be designated as shorter than the legal maturity in case of an expectation of earlier call or the intention to sell the investment. (Such a designation may have accounting implications which must be taken into account.)

Once the primary aim of liquidity is met, Council will ordinarily diversify its maturity profile as this will ordinarily be a low-risk method of obtaining additional return as well as reducing the risks to Council's income. However, Council always retains the flexibility to invest as short as required by internal requirements or the economic outlook.

The factors and/or information used by Council to determine minimum allocations to the shorter durations include:

1. Council's liquidity requirements to cover both regular payments as well as sufficient buffer to cover reasonably foreseeable contingencies;
2. Medium term financial plans and major capex forecasts;
3. Known grants, asset sales or similar one-off inflows; and
4. Seasonal patterns to Council's investment balances.

Investment Horizon - Description	Investment Horizon - Maturity Date	Minimum Allocation	Maximum Allocation
Working capital funds	0-3 months	20% Previously 10%	100%
Short term funds	3-12 months	0% Previously 20%	100%
Short-Medium term funds	1-2 years	0%	70%
Medium term funds	2-5 years	0%	50%
Long term funds	5-10 years	0%	25%

Within these broad ranges, Council relies upon assumptions of expected investment returns and market conditions that have been examined with its investment advisor.

5.15 Performance Benchmarks

The performance of each investment will be assessed against the benchmarks listed in the table below.

It is Council's expectation that the performance of each investment will be greater than or equal to the applicable benchmark by sufficient margin to justify the investment taking into account its risks, liquidity and other benefits of the investment.

It is also expected that Council will take due steps to ensure that any investment is executed at the best pricing reasonably possible.

Investment	Performance Benchmark	Time Horizon
11 am Account including TCorpIM Cash Fund, short dated bills, deposits issued by financial institutions of appropriate term.	AusBond Bank Bill Index (BBI)	3 months or less
Term Deposits of appropriate remaining term, FRN's nearing maturity, TCorpIM Short Term Income Fund.	AusBond Bank Bill Index (BBI)	3 months to 12 months
Term Deposits with a maturity date between 1 and 2 Years, FRN's designated for sale.	AusBond Bank Bill Index (BBI)	1 to 2 years
FRN's, Bonds, Term deposits with a longer maturity date not intended for sale.	AusBond Bank Bill Index (BBI)	2 to 5 Years
TCorpIM Managed Funds (Diversified or growth asset sectors).	Fund's Internal Benchmark	3 Years (M/T Growth) 5+ Years (L/T Growth or Growth Sector Funds)

5.16 Grandfathering

Grandfathered investments (managed funds or securities) are allocated to the appropriate horizon based on expected or average maturity date and should be taken into account when allocating the rest of the portfolio. Note, Council does not currently hold Grandfathered investments.

The decision on when to exit such investments are based on a range of criteria specific to the investments – including but not limited to factors such as:

1. Returns expected over the remaining term;
2. Fair values;
3. Competing investment opportunities;
4. Costs of holding;
5. Liquidity and transaction costs
6. Outlook for future investment values; and
7. Risk of defaulting payment.

In general, it is expected that professional advice will be sought before transacting in "grandfathered" investments. This policy does not presume disposal; however, the removal of an asset from the Minister's Order or under a new Policy would warrant a review of its suitability for retention.

5.17 Reporting

Council will maintain a separate record of money it has invested under section 625 of the Act, in accordance with the criteria defined by the Local Government Code of Accounting Practice and Financial Reporting. Documentary evidence must be held for each investment and details thereof maintained in an investment register. The documentary evidence must provide Council legal title to the investment.

For audit purposes, certificates must be obtained from the banks/fund managers/custodian confirming the amounts of investment held on Council's behalf at the 30th of June each year.

All investments are to be appropriately recorded in Council's financial records and reconciled at least on a monthly basis.

A monthly report will be provided to Council. The report will detail the investment portfolio in terms of holdings and impact of changes in market value since the previous report. The monthly report will also detail the investment performance against the applicable benchmark, investment income earned versus budget year to date and confirm compliance of Council's investments within legislative and policy limits. Council may nominate additional content for reporting.

6 Related Documents

Investment Strategy.

Policy

Investment Strategy

Responsible Manager (Title)	Manager Finance & Supply		
Adopted by Council	Date:	Minute Number:	
File Reference Number	DWS	Version 15.0	Review Due: June 2022
Document(s) this policy Supersedes	V14.0 – 23/06/2020 – 6c.20.085		
Community Plan Linkage	**5 Leadership**		
	5.2 We will have an effective and efficient organisation		
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1 Purpose

Having outlined the framework for investment in the **Investment Policy**, this document sets out:

1. current market conditions;
2. how Council is responding to structure its investment portfolio;
3. realistic objectives for the investment portfolio;
4. risk management.

2 Investment Strategy

2.1 Strategy

Council's Investment Strategy is set in relation to the following parameters:

Diversification

Council's investments are diversified only within the fixed interest sector: cash and term deposits (fixed and floating). It has recently disposed of its assets held in senior floating rate notes (FRNs) at a premium given they are sub-optimal investments. It has not been Council's practice to diversify further across other riskier asset classes.

The Policy and Minister's Order permits investment in the TCorpIM Funds; TCorpIM as a business decision excluded sector funds from Councils from 2019, and this is not expected to change for all but the largest investors. Currently the only viable path to higher risk-returns is with the Long-Term Growth Fund – approximately 65-70% shares, or the Medium-Term Growth Fund which invests approximate

20-40% in shares. Fundamentally, growth funds including TCorp remain expensive on a historical basis, as measured by the current price-to-earnings (P/E) ratios and dividend yields.

Long-term growth assets are risky and would only be used to back long-term liabilities specifically designated of appropriate funding horizon. Risky assets would only be used with specific Council approval.

COVID-19: Impact

The pandemic has adversely impacted financial markets, which in turn, has also affected Council's investment portfolio. We provide a quick summary in this section.

With regards to financial markets, shares (equities) experienced a significant correction in March 2020 but have since, recovered substantially due to the unprecedented fiscal and monetary policy support from global central banks and governments. The RBA cut official interest rates to record lows on 3rd November 2020 to 0.10%. Equities continued their rally in April 2021 with the accelerated rollouts of multiple vaccines and ongoing fiscal stimulus. Longer-term bond yields have also risen over the past few months on the prospects of higher inflation over coming years.

With regards to the medium-longer term outlook for financial markets, of importance is the RBA's outlook and stance on the current situation:

1. The RBA's official cash rate will remain unchanged at its emergency level of 0.10% until its objectives of full employment and inflation are reached.
2. They suggested the non-accelerating inflation rate of unemployment (NAIRU) could be in the low 4s, or even the high 3s, well below the current unemployment rate of 5.6%;
3. The RBA reiterated that it was prepared to do more quantitative easing (QE) after the second $100bn round ends in September 2021;
4. Inflation is not expected to reach their 2-3% target band until at least mid-2023;
5. The Board does not expect the conditions for a rate hike "*to be met until 2024 at the earliest*".

The largest impact to Council's investment portfolio is with regards to its largest exposure being assets held in bank term deposits (fixed and floating), which accounts for around ~71% of the total portfolio. The biggest risk that Council faces over the medium-longer term in this environment is not the potential loss of capital (given all the banks are well capitalised and regulated by APRA), but the rapid loss of interest income as interest rates have plummeted.

Given official rates have fallen to record lows, Council is likely to see a rapid decline in interest income over future financial years. Its budgeted income over the medium-longer term needs to be revised to reflect the low interest rate environment. Returns between 0.40%-0.80% p.a. for new investments and rollovers may potentially be the "norm" over the next few financial years, especially if placing the majority of surplus funds for terms less than 2-3 years. Yields are in fact likely to be lower if electing to invest for terms under 12 months.

Market & Economic Background

US core CPI inflation printed triple the market consensus at +0.9% m/m (consensus +0.3%) over April 2021, while the annual rate came in at +3.0% y/y, the highest since 1996. Headline CPI inflation was also strong at +0.8% m/m and +4.2% y/y. US Fed speak post the CPI report repeated the familiar lines that the spike in inflation is likely to be transitory.

The US payroll numbers in April 2021 disappointed, coming in at 266k against expectation of 1 million. The unemployment rate unexpectedly ticked up from 6.0% to 6.1% against expectations of a fall to 5.8%.

The US Treasury announced its expectations to borrow US$463bn in April through June 2021, an increase of about US$368bn compared to the numbers projected in February.

The UK economy contracted by -1.5% q/q in Q1 2021, but the monthly track showed a decent pick-up in growth in March, confirming that a strong rebound is underway as lockdown restrictions ease.

European GDP data confirmed their recession with Q1 GDP at -0.6% q/q. With the vaccination programme back on track in the region and restrictions likely to ease, Q2 is expected to be much better.

The Bank of England kept all its policy settings unchanged, including its £875bn government bond buying target.

Domestically, the RBA kept its rates and guidance unchanged at its meeting in May 2021, however it upgraded its baseline forecasts for economic growth and substantially reduced its unemployment forecasts. The RBA has lowered its unemployment rate forecasts to 4.5% by the end of 2022 (previously 5.5%), which is at the bottom end of model-based NAIRU estimates (NAIRU is pegged around 4.5-5.0%). The unemployment rate was at 5.6% in March 2021.

The RBA has indicated it will not extend their 3yr yield target from the April 2024 bond to the November 2024 bond, which could signal their intention to announce a tapered QE3.

The Federal Government announced the underlying cash deficit for 2020-21 was revised almost $40bn lower to $161bn (7.8% of GDP) from $213.7bn (11%) at the previous budget in October 2020, on the back of the better-than-expected labour market recovery and elevated iron ore price.

However, the 2021-22 deficit is only slightly lower, $106.6bn from $112bn, much higher than market expectations for a deficit around $80bn. Deficits are forecast all the way to 2031-32. Gross debt is expected to be $829bn (40.2% of GDP) in 2020-21 before stabilising at around 51% of GDP in the medium term.

In terms of spending, the largest item was the Government’s aged care package – at around $17.7bn over the forward estimates. But there were other big spends in the areas of Infrastructure ($15bn) and NDIS ($13.2bn). The Low and Middle-Income tax offset was extended a year ($7.8bn) and the Investment Asset Write Off also was extended.

Interest Rate Outlook

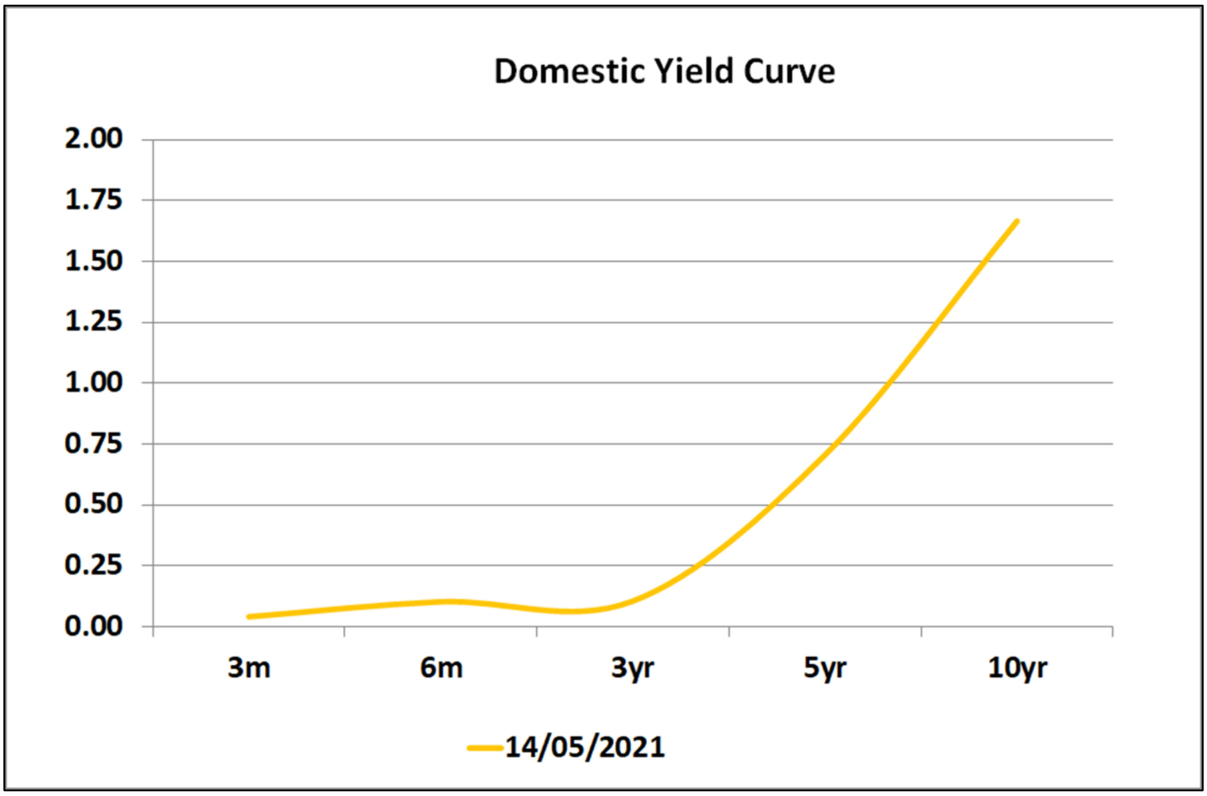
The unprecedented fiscal support for the global economy and the evident determination of the US Biden administration to accelerate the vaccine rollout has aided financial markets. Further significant stimulus packages are also being proposed to expediate the recovery.

US Fed Chair Powell appeared to be more optimistic on the outlook, saying "*we feel like we're at a place where the economy's about to start growing much more quickly and job creation coming much more quickly*". Powell remains cautious and has made it clear that it was "*not time yet*" to have a conversation about tapering its US$120bn monthly QE bond buying programme. He emphasised that the US was "*not close to*" the substantial progress toward its employment and price stability goals that has been set as the condition for contemplating its first steps of tapering.

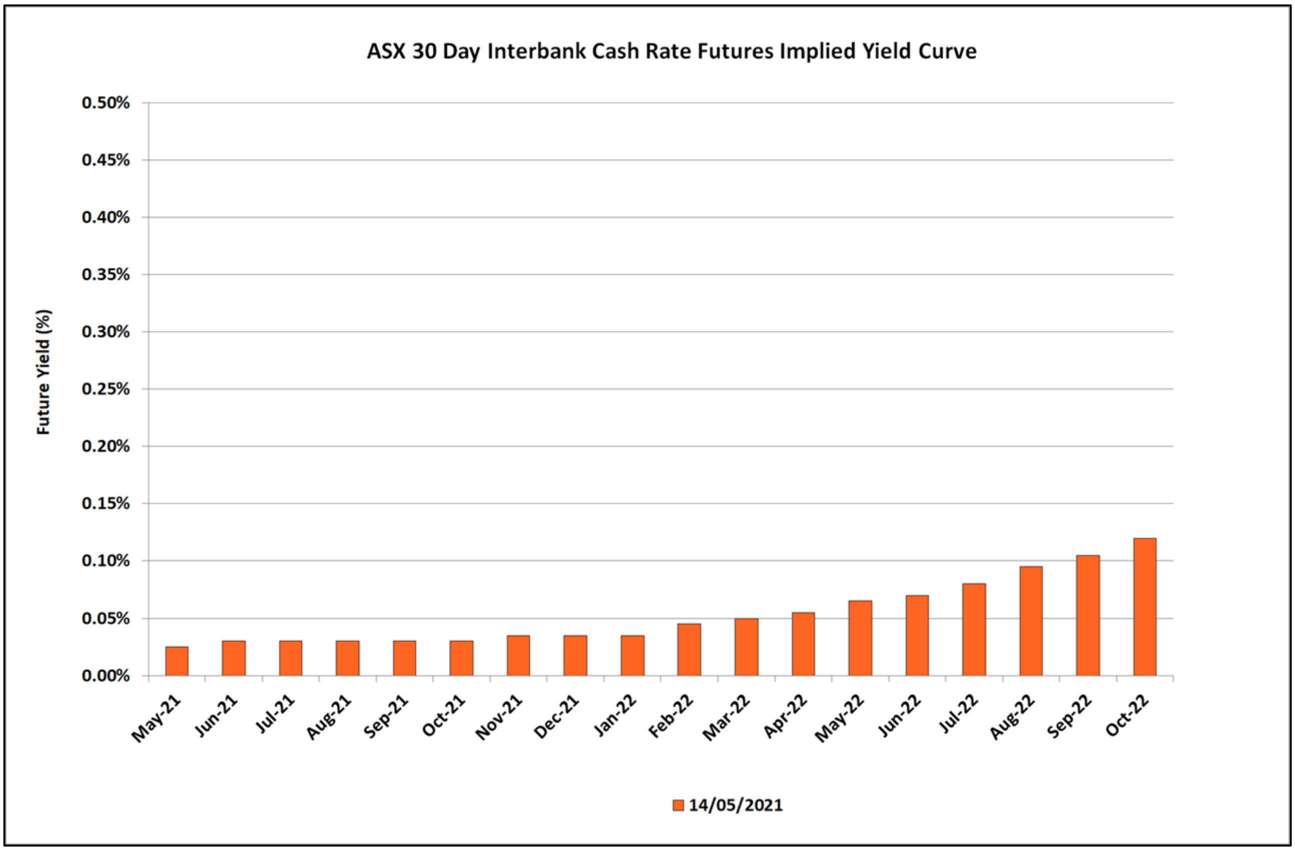
Global central banks (including the RBA) have stressed that they will look through temporary increases in inflation from base effects and supply chain disruptions.

Domestically, the RBA is of the view that "*a materially lower unemployment rate*" (NAIRU of low 4s or even 3s) is needed to generate wages growth in excess of 3%, which is the level the RBA thinks is needed to deliver inflation sustainably within the 2-3% inflation target. The Bank does not see this occurring "***until 2024 at the earliest***", which underpins their rates guidance.

The domestic bond market continues to suggest a prolonged low period of interest rates, with 10-yr government bond yields still yielding under 1.75%. A flat curve is still largely priced in for at least the next 3 years:



RBA Governor Lowe has pushed back on market pricing of rate hikes as early as late 2022. Dr Lowe reiterated his 'best guidance' was that it is "*unlikely to see wages growth consistent with the inflation target before 2024. This is the basis for our assessment that the cash rate is very likely to remain at its current level until at least 2024*":

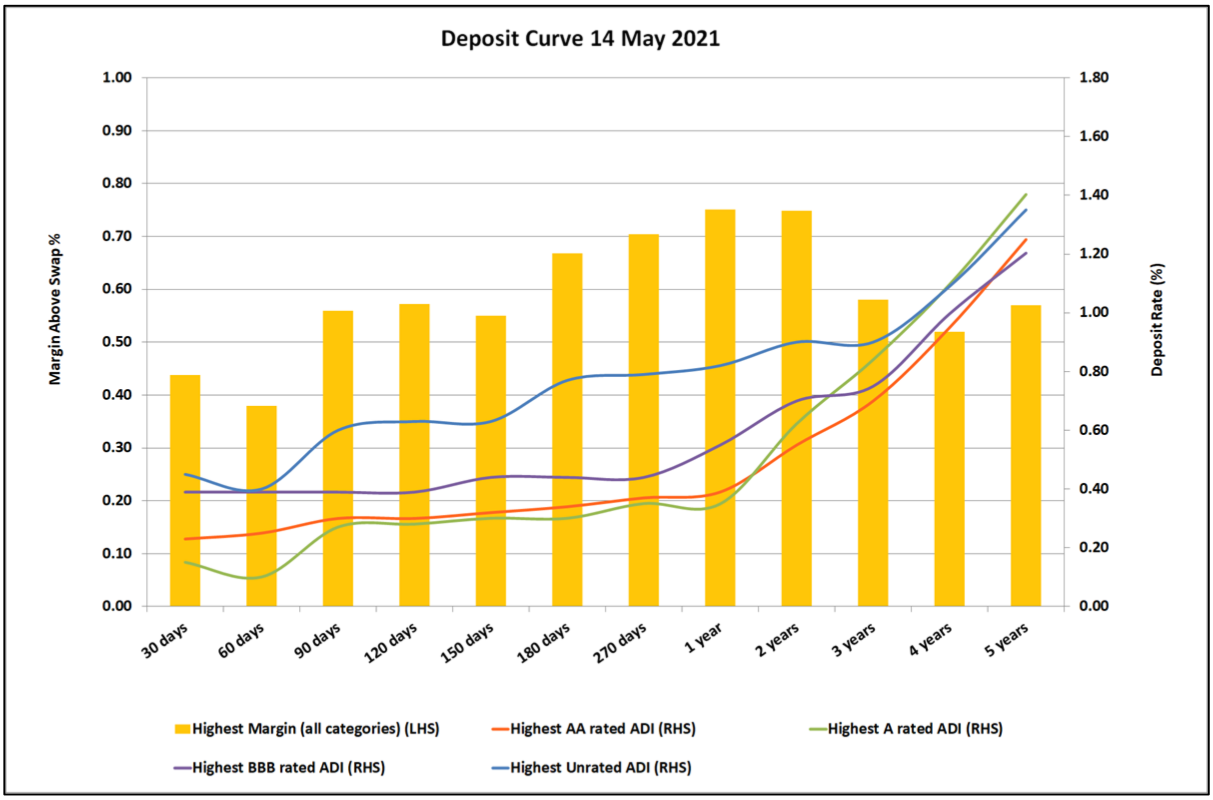


Term Deposits

Council should remain prudent and be aware of their cash flow requirements throughout the various stages of the pandemic. Strategically, any funds excess to liquidity requirements should be diversified across different maturity horizons, potentially taking advantage of higher yields on offer at the longer end of the curve to address reinvestment risk and compressed margins.

The combination of high unemployment, soft credit growth and cheap funding for the banks via the RBA's term funding facility (TFF) and Quantitative Easing (QE) program has resulted in excess liquidity in the marketplace. Margins continue to squeeze on the back of excess liquidity provided by unprecedented fiscal and monetary policy support.

The retail deposit market has been flooded with cash on the back of increased government payments, superannuation withdrawals, and repayment deferrals, which have offset the hit to household incomes in aggregate. As a result, several ADIs have been selective in seeking 'new' wholesale funding, often only looking to roll existing deposits, whilst some are simply redeeming all deposits at maturity.



Amongst the investment grade sector, outside of AMP Bank (BBB), short-dated term deposits (maturing less than 12 months) are yielding under 0.50% p.a. (most are under 0.40% p.a.). We believe there is not much value being offered in short-dated deposits.

In contrast, there is an upward pick-up in yield for Council if it can take advantage of 2-5 year fixed T/Ds whilst official rates are stuck at depressed levels for the foreseeable future. Given Council does not require high levels of liquidity and can stagger its investments longer-term, it will be rewarded over coming years if it reinvests for a minimum term of 2 years (we note other Councils have been able to roll for 3-5 years). Such a strategy is potentially yield, on average, more than double the return compared to those Councils that purely invest in short-dated deposits.

Floating Rate Notes (FRNs)

Credit spreads have tightened significantly since the RBA stepped in and reduced the cash rate to emergency levels. The RBA then followed up by offering their $200bn term funding facility (TFF) to the ADIs, allowing them to borrow directly at 0.10% p.a. fixed for 3 years, as well as launching Quantitative Easing (QE), whereby they continue to buy bonds in the secondary market to target a 3-year bond rate of 0.10%, effectively keeping longer-term interest rates low.

These factors have resulted in an overly liquid market with little FRN supply in the primary market from the ADIs. FRNs are now trading at pre-GFC tights and look expensive. For example:

- For a new 5 year senior FRN issued by a regional / "BBB" rated bank, the most attractive issuances in recent months were CUA (BBB) at +68bp and BoQ (BBB+) at 63bp. Over a 4yr holding period and once factoring in potential capital gains, the net (outright) return for any "BBB" rated FRN is likely to be under 0.80% p.a. These FRNs are currently not that attractive compared to fixed bond or fixed term deposits where Council is able to lock in rates between 0.80%-1.35% p.a. for 3-5 years and most likely, with a higher rated/lower risk bank.

- For a new 5 year senior FRN issued by a higher rated bank, there is currently very little supply as the higher rated domestic banks are not issuing securities (they have option of cheap funding from the RBA's TFF i.e. they are in no rush to receive wholesale funding by issuing new FRNs).

Given the above factors, unless there is significant widening of credit spreads, there is currently not much value being offered in senior FRNs relative to medium-longer dated fixed assets (term deposits and bonds). In fact, Council disposed of all its FRNs between February – April 2021 at a significant premium, from which it realised capital gains of $141,320.

Should market conditions change, Council may look at purchasing new FRNs in the future but in the interim, it will focus on other higher yielding complying asset classes (namely fixed term deposits and potentially, fixed bonds).

Fixed Bonds – Northern Territory Treasury Corporation (NTTC)

We are aware of the following senior retail bond offering from Northern Territory Treasury Corporation (NTTC) effective 12th April 2021, and available until the end of May 2021:

Maturity Date	Rate % p.a.^	Interest Paid
15/06/2024	0.80%	Annually
15/06/2025	1.10%	Annually
15/06/2026	1.30%	Annually

If interested in this product, Council should avoid placing through the broker channel and contact Imperium Markets to receive the full commission of 0.25% (plus GST) on the face value of the investment, in the form of an additional rebate. If placed through the brokers, they are likely to keep the 0.25% commission (on the face value of the investment).

Overview	Description
Issuer	Northern Territory Government
Credit Rating	Aa3 (Moody's), which is AA- equivalent (S&P)
Type	Fixed senior (retail) bonds
Program	Territory Bonds Issue 110
Date for applications	**01/01/2021 – 31/05/2021**
Liquidity	Weekly redemptions available, subject to the prevailing market rate and administration costs^^

The product should be viewed as a hold-to-maturity product, noting there are significant penalty costs including admin fees, the prevailing market interest rate, and factors in any associate commissions that were previously paid. Given the longer-term outlook for official interest rates, Council should strongly consider placing small parcels (up to $5m) in the 15/06/2024, 15/06/2025 and 15/06/2026 maturities through Imperium Markets to receive an effectively higher rate, once factoring in the rebated commission.

2.2 Existing Portfolio Status

As at the end of April 2021, the deposit portfolio had a weighted average yield of 1.37% p.a., which is still yielding higher than any deposit in the marketplace out to 5 years. It compares to a benchmark bank bill rate that has traded to lows between 0.01%-0.10% p.a.

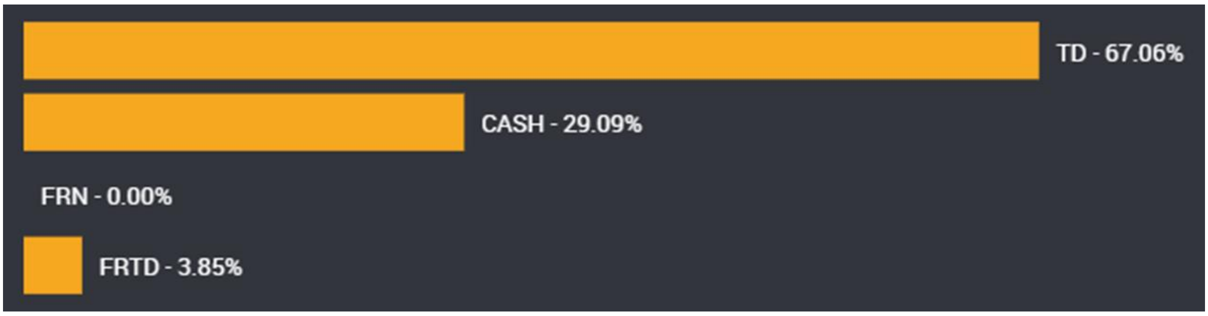
Council has not invested in TCorpIM's Growth strategies, which can be volatile during times of stress given their exposure to shares.

The Strategy throughout the past few years has been to prioritise long-dated deposits - ahead of significant cuts to interest rates. This has been extremely successful over a long period and continues to dominate portfolio returns today.

The portfolio continues to be dominated by term deposits (fixed and floating). Future reinvestments on term deposits will likely be locked in at lower prevailing rates. Reinvestment rates are now generally under ½% for terms under 12 months, and between ½% to 1¼% for 2-5 terms.

Medium-Term fixed bonds issued by the Northern Territory Treasury Corporation (NTTC), rated Aa3 by Moody's (AA- equivalent from S&P) is yielding between 0.80%-1.30% p.a., available until the end of May 2021. An additional 0.25% rebated commission can be achieved through Council's investment advisor if placed through them.

Council's Investment Portfolio 30/04/2021



2.3 Proposed Actions

For the reinvestment of maturing assets, Council will need to assume returns yielding between 0.50%-1.00% p.a. on average, at least for the next few financial years. Note if a larger proportion of assets are reinvested for terms less than 12 months, returns on these investments may in fact likely be placed at yields less than 0.50% p.a.

Only the higher-risk Growth Funds at TCorpIM have the potential to offer higher returns. This is a topic for consultation, but no investment in risk assets is intended at this time, given the high volatility and potential for capital losses.

To maximise performance, the intention is to pursue the following actions during this strategy period (subject to conditions broadly outlined in this document):

New Investments

1. Consider placing new investments in NTTC (AA-) fixed bonds and lock-in rates between 0.80%-1.30% p.a. for 3-5 year terms prior to 31/05/2021 when the offer closes. (Note an additional 0.25% rebated commission will gross up overall returns).
2. Take advantage of the upward sloping deposit curve and place a mixture of 2-5 year fixed deposits with the likes of NAB (AA-) or another major bank to lock in rates between 0.55%-1.25% p.a. (or potentially higher).
3. Consider opening up a term deposit account with an international bank such as the Industrial and Commercial Bank of China (A) to lock in fixed deposit rates yielding between 0.60%-1.40% p.a. for 2-5 year terms with a higher rated bank.
4. For any short-term requirements (should be kept at a minimum), place in a mixture of 6-12 month deposits from any of the investment grade (BBB- or higher) rated banks.
5. Switch out of low yielding overnight cash accounts (including the withdrawal of the TCorpIM Cash Fund) and switch into the Macquarie Bank (A+) accelerator cash account currently offering 0.40% p.a. for balances up to $10m and 0.20% p.a. for balances greater than $10m.

Council will conduct stakeholder consultation on the applicability of the higher risk TCorpIM investments should there be any risk appetite in the future.

Risk Management Guidelines

The strategy addresses risk management as outlined below:

Preservation of Capital

Council has already enacted major strategies to manage capital risk given the portfolio remains 100% compliant with the Minister's Order. All are 'senior-ranked' assets, considered extremely low risk and rank highest in the bank capital structure.

Over the short term, growth assets would be inconsistent with this objective.

Credit Risk

S&P continues to officially rate the domestic major banks at AA- with a negative outlook. This has no impact under the current Policy given the protections in place with the maximum limits permitted in the event of a downgrade.

The credit rating profile is currently acceptable, well within Policy limits, as all assets in the portfolio are investment grade (rated "BBB-" or higher).

Given the credit downgrades of several banks over the past few years, it is expected that Council will prioritise careful management of credit quality during the term of this Strategy, but no sectors or counterparties are currently outside Policy limits.

Diversification

Investments are currently diversified within the fixed interest sector – term deposits (fixed and floating), at-call cash and cash notice accounts. Diversification outside the fixed interest sector would require broad-based buy-in and there is no current intention to diversify into other asset classes.

Liquidity Risk

Council's portfolio is highly liquid from at-call accounts and near-term maturities. Approximately 67% matures within 12 months; unusually high. A larger proportion of assets should be diversified across the 2-5 year horizon to address rollover risk.

Market Risk

Along with credit risk, market risk has now been substantially minimised given all investments are directed to conservative, senior fixed interest assets.

Market risk would significantly increase from any growth assets.

Maturity Risk

Council's longer-term investments are entirely directed to term deposits and cash accounts, minimising the effect of maturity risk as there is a regular maturity pattern and spread of maturity dates.

Rollover Risk

Council has reduced some of its risk through the term deposit portfolio's weighted average duration being at ~12½ months, considerably longer than the 45-day benchmark. This is considered a safe level of protection, deferring rollover risk for a full reporting cycle. Given the depressed state of interest rates, it should look to extend the average duration further to protect income from falling more rapidly over future financial years.

Protection is against economic shocks causing a radical change in monetary policy, but also against lower spreads. There has been a long-term trend for deposit margins to fall post-GFC; this has been especially pronounced in shorter deposits.

Medium and longer term holdings are lightly utilised, and there is capacity for liquid investments should they become more attractive.

2.4 Performance Benchmarks

Council's portfolio returned an annualised yield of 1.56% for the latest quarter ending April 2021. This is supported by high yields on deposits placed in earlier years, and well above bank bills at close to zero percent and the cash rate return of 0.10%.

This yield is considered very strong given the high credit ratings targeted, but is no longer possible to maintain. Yield is facing further pressure over time, as official interest rates are expected to remain lower for much longer based on the RBA's guidance over the next few years.

2.5 Delegations/Responsibilities

Within the constraints of the Policy, strategic or execution decisions are delegated to the General Manager, Director Corporate & Governance and the Manager Finance & Supply. While Council is notified of significant strategy updates and the reasons for them, implementation of investments optimised within the approved Policy is part of management's operational responsibilities.

2.6 Effective Date and Review of Strategy

The effective date of this Investment Strategy is the date it is adopted by Council and will be reviewed at regular twelve monthly intervals, or as required in the event of legislative change or as a result of significantly changed economic/market conditions.

Council is in regular contact with its advisors and is able to adjust strategy as market conditions dictate.

3 Related Documents

This Strategy relates to implementation of the portfolio within the constraints set out in the **Investment Policy**.