
Fitch Assigns First-Time 'AA-' Rating to Timaru District Council

Fitch Ratings has assigned Timaru District Council (TDC) a first-time Long-Term Local-Currency Issuer Default Ratings (IDR) of 'AA-' with a Stable Outlook.

The rating reflects the strong institutional framework for local and regional councils in New Zealand, TDC's sound management and fiscal performance, the stable local economic environment and moderate debt levels offset by large reserves and solid financial flexibility.

KEY RATING DRIVERS

New Zealand's institutional framework for local authorities is an important positive rating factor for TDC. transparent reporting and financial disclosure; strong controls and supervision; a high level of predictable own-source revenues (rates) with wide rate-setting powers; strong creditor protection, with borrowings generally secured over the council's rating base; and limited labour intensive responsibilities, as health and education are provided by the central government.

TDC's budgetary performance has been good with expanding revenue and controlled spending resulting in a strong operating margin of 30% for the financial year ended-June 2016 (FY16). Fitch expects TDC to maintain an operating margin of around 30% over the four years to FY20, consistent with its historic performance.

TDC has a moderate gross debt burden, with a direct debt/current revenue ratio of 132% at FYE16, which we expect to increase to 138% by FY20. This is higher than the 'AA' peer group average, but lower than for other 'AA-' rated domestic peers. However, offsetting the gross debt are some large cash and liquid investments. This brings down TDC's net overall risk/current revenue ratio to 84% at FYE16; well below a 'AA' peer group average of around 160%.

The Timaru district is a small agricultural-led economy that supports a large agricultural services and manufacturing sector. Manufacturing accounted for around 22% of the working population in 2013. Depressed dairy prices kept GDP flat in the year to September 2016, but we expect stronger prices, increased business investment and port development to support higher GDP in 2017. The district's total population of around 46,700 increased by 1% in FY16 and its GDP of around NZD2.3 billion equates to 1% of the national GDP. The unemployment rate was a low 3.3% at end-September 2016.

TDC has conservative and transparent management and governance is supported by clear policy guidelines and a rigorous planning and consultation process, which includes 10-year long-term plans that are updated every three years. Strategic goals are well articulated and council's performance relative to its budget has been good. TDC generated surpluses in excess of budget in each of the four years to FYE16.

RATING SENSITIVITIES

TDC's rating could come under pressure if its operating performance deteriorates significantly and unexpectedly, with operating margins dropping towards 15% and direct debt/current balance increasing towards ten years (five years at FYE16).

Given TDC's relatively small economy a positive rating action would require a lower debt burden, given TDC's relatively small economy, with direct debt/current balance heading towards three years.

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Summary of Data Adjustments – The financial data used in Fitch's calculations are taken from TDC's annual reports. We have made the following adjustments to the reported numbers:

- Depreciation and impairment of property, plant and equipment are excluded from capital expenses.
- Cash flow for the purchase of property, plant and equipment and intangible assets are included in capital expenses.
- Cash flow from the sale of property, plant and equipment are included in capital revenue.