

STAFF REPORT

TO: Mayor and Councillors
FROM: Corporate Services Manager
DATE: 1 June 2010
SUBJECT: **Budgeted Interest Rate on Council Debt – RCN10-06-13**

Purpose of report

To consider the appropriate interest rate on debt to be included in Council's 2010/2011 annual plan.

Background

Council's 2009-2019 LTCCP included an interest rate on Council debt of 7.1%. This interest rate of 7.1% was included in the draft 2010/2011 annual plan.

Discussion

Council's current interest rate on external debt is 6.04%. Over the last 11 months staff have undertaken some \$35 million of swaps meaning that 50% of Council's current debt of \$109 million is protected from short term interest rate rises. In addition Council has long term debt of varying maturities in place so that over the next financial year only \$15.8 million of debt will fall due and be repriced at newer and presumably higher interest rates.

Council is budgeting in the next financial year to raise \$27.3 million of new debt. This new debt is likely to be subject to higher interest rates.

An additional risk over and above expected interest rate rises is the margins banks charge for debt. Council has two facilities falling due in the next financial year and the new bank margins are considerably higher than what we see today.

Taking into account increased bank margins and the likelihood of higher interest rates on new and repriced debt the view of staff is that the average interest rate may reach 6.4% over the next financial year. Given that the budgeted plan included an interest rate of 7.1% this provides Council with the opportunity to reduce its planned interest rate over that year.

Accordingly staff believe that the interest rate for the 2010/2011 annual plan can be reduced from 7.1 to 6.9 %. An interest rate of 6.9% still provides a .5% buffer over expected debt cost in the event that unknown events occur.

As a note of caution, while the recommendation is to reduce the interest rate for the 2010/2011 financial year depending on debt costs, the interest rate for the 2011/2012 year may have to be increased above 6.9%.

Significance

The change in interest rate is not considered significant in terms of Council's significance policy.

Options

Option 1

Accept the staff recommendation and reduce the interest rate in the 2010/2011 annual plan to 6.9%

Option 2

Reject the staff recommendation and leave the interest rate at 7.1%. If this option is preferred and a surplus is generated it would be available to be allocated the following financial year.

Recommendation

That the interest rate in the final 2010/2011 Annual Plan be 6.9%

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Corporate Services Manager