Appendix 2

DUBBO REGIONAL COUNCIL

March

Investment Strategy

2022

Investment Strategy

Purpose

The annual Investment Strategy sets out Council's investment goals and targets for the coming year. The aim of the strategy is to guide the management of Council's investment portfolio over the short to medium term to:

- achieve a balanced and diversified portfolio, in terms of allowable investment products, credit ratings and maturation terms that will outperform the benchmark indices; and
- ensure liquidity when required for Council's operational and capital expenditure needs.

This strategy has been prepared in consultation with Council's investment advisor, Laminar Capital Pty Ltd.

Scope

The *Investment Strategy* applies to all managers and employees who actively manage investments or have responsibility for employees who actively manage investments.

This strategy should be read in conjunction with Councils *Investment Policy*.

Effective Date

This document replaces any previous Strategy document approved by Council.

The effective date of this Strategy is 24 March 2022 and will be reviewed in March each year or when a change in either regulation or market conditions necessitates a review.

Context

Council's investment strategy is determined after taking into consideration a review of the following issues:

- global and domestic economic investment environments;
- investment policy and legislative constraints;
- current composition of Council's investment portfolio;
- long, medium and short term financial plans.

Global and domestic investment environments

As the COVID-19 pandemic began early 2020, the global economy has been struggling to regain a broad-based recovery. Through the first half of 2021, economic forecasts turned more positive based on an expected return to pre pandemic rates of growth. Nevertheless, the economic situation has remained highly fluid globally for most countries and regions. Uncertainty about the length and depth of the health crisis-related economic effects continue to influence perceptions of risk and volatility in financial markets and corporate decision making.

Progress in administering vaccines through the year 2021 raised prospects of relaxing or removing restrictions related to the pandemic, which could improve economic activity in Australia. December 2021 saw risk assets rise strongly despite the potentially growth crimping threats from rising Delta and Omicron infection rates. The most part of 2021, including December, were influenced by stronger than expected economic activity and faster than expected rise in inflation with governments and central banks barely starting to stem easy policy settings.

Whilst the RBA has maintained the cash rate target at 0.10% since their last meeting and have provided guidance that they plan to keep it at this level for the next 3 years, underlying market conditions may cause them to review their forecasts. By the end of 2021, at-call and Term Deposit rates started to pick up due to inflation concerns as well as the removal of the Total Funding Facility (TFF) which had previously resulted in excess liquidity in the cash market and hence, lower re-investment rates.

In the absence of an unforeseen factor rapidly reversing the rise in inflation and the likelihood of central bank rate hikes, 2022 will offer much smaller asset class returns to investors than 2021 and the possibility of falling returns on the most interest rate sensitive assets. Low interest rates in 2021 supported risk asset markets, however with a threat of interest rates rising in 2022 support of risk assets should reduce during the year.

Legislative environment

Council's investment opportunities are constrained by a combination of legislation, regulation and any directions and guidelines issued by the Minister or the Office of Local Government. There has been no change to the investment legislative environment for a number of years and the most recent Ministerial Investment Order released in January 2011 continues to limit Council's investment options to:

- term and at-call deposits with Approved Deposit-taking Institutions (ADIs);
- other ADI senior ranked securities;
- investments with NSW Treasury Corporation including their investment management division (TCorp and TCorpIM);
- funds or securities issued or guaranteed by the Commonwealth or any State or Territory.

Composition of Council's investment portfolio

The conservative nature of Council's Investment Strategy is clearly reflected in the structure of the portfolio, where 92% of the portfolio is invested with Australian Prudential Regulation

Authority (APRA) - regulated ADIs and 8% of the portfolio is invested in Northern Territory Government Bonds.

Council's current portfolio is as follows (as at the end of December 2021)

Investment	**Split**
Big Four banks	26.50%
Australian mid-tier banks	47.00%
Foreign controlled Australian based ADIs	10.20%
Unrated – Local ADI	1.30%
Unrated – Australian based ADI	1.30%
Unrated – Foreign controlled Australian based ADIs	5.70%
Total APRA-regulated ADIs	**92.00%**
Northern Territory Government Bonds	8.00%
Total Investment Composition	**100.00%**

Investment strategy

Council's investment portfolio will continue to be prudently managed in accordance with:

- Council's *Investment Policy* and related legislative and regulatory requirements;
- documented risk management procedures to preserve capital; and
- Council's operational and capital funding requirements.

Objectives

Council's investment strategy for the period is to maintain the highly secure profile of the portfolio, provide liquidity and deliver competitive investment returns commensurate with the portfolio structure.

Risk profile

The risk profile for Council's investment portfolio is based on the principles of being prudent, conservative and risk averse. This is achieved by managing the diversity and creditworthiness of investments in accordance with the *Investment Policy* and other relevant requirements.

Current investments are with APRA regulated financial institutions and Northern Territory Government Bonds so that credit risk remains minimal.

The maturity profile of the investments is adequately spread to ensure that liquidity and maturity risks are also kept to a minimum.

Securities are highly liquid and Council makes full use of this rather than holding at-call money. Council has historically held Floating Rate Notices (FRNs) to maturity, but is increasingly seeking to optimise the entry and exit points for these types of investments.

Liquidity / Maturity

The majority of Council's cash and investments portfolio is held as restricted reserves to satisfy legislative responsibilities and funding commitments contained within the *Dubbo 2040 Community Strategic Plan*.

To ensure Council has available funds to meet these short-term commitments, the following liquidity targets are set in accordance with the *Investment Policy*.

Investment Horizon Description	**Investment Horizon - Maturity Date**	**Minimum Allocation**	**Maximum Allocation**
Working capital funds	0-3 months	10%	100%
Short term funds	3-12 months	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%

Council's capital funding requirements will continue to increase over the next few years. Major capital expenditures in 2022 are anticipated to be approximately $75 million

Projects are being funded from either grants or restricted assets and impact the overall cash available for investment. The maturity profile of the investment portfolio has become more concentrated in the short and medium term rather than the longer term.

Council's liquidity will be monitored on an ongoing basis to ensure cash requirements are met and that liquidity parameters remain within allowable limits set out in the *Investment Policy*.

The Strategy

Investments are to be placed with the advantageous rate to Council and within the limits as set in the tables included in the *Investment Policy* and the Investment Strategy as listed below;

- Investment Policy - Performance Benchmark Table
- Investment Policy - Credit Rating Structure and Tenor Limits
- Investment Strategy – Investment Horizon Description

To maximise performance, the intention is to pursue the following actions during this strategy period;

- Reduce current cash holdings due to potential changes to cash rate forecasts from static to potentially rising.
- Increase fixed term deposits past 12 months as comparable term deposit rates have begun to improve.
- Take advantage of longer tenor specials available up to a maximum of 2 to 3 years unless an advantageous rate is available. Anything longer than 3 years should be placed in either floating rate deposits or floating rate notes.

- Take advantage of special rates being offered by banks such as Bank of Sydney, Australian Unity bank, BankVic and Auswide bank.
- Identify opportunity in Regional and Offshore names in both Senior Unsecured and Covered Bonds.
- Purchase secondary market FRNs where investment can be optimised reducing the liquidity risk and interest rate risk while having no impact on credit risk of the portfolio
- Maintain exposure to the unrated ADI category, as these issuers may enhance returns on investments.
- Maintain a well-structured portfolio with a mix of maturities laddered across tenors.
- Maintain longer term investment mix where FRN's represent 30% (currently 9.47%) is deemed appropriate.

Environmentally and Socially Responsible Investments

Council's ability to acquire environmentally and socially responsible investments within the current investment and policy environment remains limited, as:

- the structure of many of these investments remains prohibited under the current Ministerial Investment Order; and
- the global financial crisis caused significant declines in the valuation of the financial assets that comprise many of these investments.

Council will, however, continue to explore opportunities for supporting environmentally and socially responsible investments within these constraints. The investment climate is changing over time and Council notes that many large scale renewable projects are expected to evolve, which may offer sustainable investment opportunities in the future *via* co-investments. Council will continue to encourage and give preference to these investments where they comply with the Ministerial Investment Order and satisfy Council's policy and investment objectives.

References

Laws and standards	• *Local Government Act 1993;* • *Local Government (General) Regulation 2021*; • Ministerial Investment Order; • Local Government *Code of Accounting Practice and Financial Reporting;* • Australian Accounting Standards; • Office of Local Government Circulars.
Policies and procedures	• Investment Policy