

## Review of the Investment Policy and Strategy

File No: X020701

### Summary

This report presents the revised Investment Policy and Investment Strategy for the Management of Council's Funds.

The Policy and Strategy are reviewed annually, as a minimum, to ensure they remain appropriate and respond to changes in economic, investment and legislative environments. The annual review of the Policy and Strategy, together with the proactive management of funds, has resulted in a secure investment portfolio that aims to continue to outperform the benchmark returns required by the policy.

The scope of the City's investments, like the wider NSW local government sector, is limited. It is mandated under the Local Government Act 1993, through a Ministerial Investment Order, that constrains council investments to deposits and / or bonds in Federal, State (including NSW TCorp) or Local Governments and in banks that are Approved Deposit Taking Institutions under the Banking Act. Councils are not permitted to invest in equities and therefore not permitted to invest directly in individual companies.

The Investment Policy sets out Council's investment objectives to safeguard the City's cash and investment portfolio, achieve appropriate rates of return and manage the portfolio to ensure sufficient liquidity to meet Council's business objectives. It includes investment criteria to frame investment decisions, risk management parameters, and investment governance standards to ensure transparency, internal controls and performance management.

The Investment Strategy outlines Council's investment intentions in light of the current economic, investment and legislative environments. The focus is on the investment opportunities available to the City, guiding investments to be maintained in the coming 12 months and the investment of new funds. The Strategy aims to accomplish a balanced and diversified portfolio in terms of investment products, credit ratings and term to maturity to ensure sufficient liquidity will be available as funds are required.

The City first formally introduced social and responsible investment criteria into its investment policy and strategy in 2008, although environmental investments were already being actively incorporated into the portfolio as appropriate instruments came onto the market. Since that time, the City has progressively strengthened its position within its allowed investment framework. In an increasingly volatile world, it should be noted that the investment policy continues to contain provisions that encourage environmentally and socially responsible investments (SRI) and seek to avoid investments in environmentally and socially harmful activities.

The City has developed good relationships with its financial institutions, partnered with them to help launch new products and continued to meet regularly with them to advocate for new investment vehicles and products that will achieve our desire to increase our commitments to social and responsible investment.

The legislative and regulatory environment for local government has remained static, and the existing Investment Policy continues to serve the City well.

The key objectives of the current Investment Strategy remain valid for the challenging economic and investment legislative requirements. The Strategy remains unchanged aside from some minor administrative adjustments as it presently meets liquidity requirements for Council's ongoing capital works program, the objectives for investment performance and continues to prudently manage credit risk.

The proposed Investment Policy and Strategy will continue to maintain an investment portfolio that is reasonably conservative; and comprise investments in institutions with high investment grade credit ratings that are all subject to APRA regulation, while at the same time allowing some flexibility for appropriate investment opportunities that enhance the City's financial returns.

### **Recommendation**

It is resolved that Council adopt the revised Investment Policy and Investment Strategy for the management and investment of Council's funds, as shown in Attachments A and B to the subject report.

### **Attachments**

**Attachment A.** 2024/25 Investment Policy

**Attachment B.** 2024/25 Investment Strategy

## Background

1. The Local Government Act 1993 (the Act) was amended in 2016 to strengthen council's fiduciary duty. The changes are intended to guide councils to carry out their functions in a way that facilitates local communities that are strong, healthy and prosperous, and include an explicit reference to councils carrying out their functions in a way that provides the best possible value for residents and ratepayers.
2. The investment policy and strategy are a key part of ensuring that the City continues to manage its finances in an effective, efficient and prudent manner. The amendments to the Local Government Act 1993, as referred to above, reinforce the City's existing underlying financial principles.
3. The Act states that councils should have effective financial and asset management, including sound policies and processes, for the following:
  - (a) performance management and reporting;
  - (b) asset maintenance and enhancement;
  - (c) funding decisions; and
  - (d) risk management practices.
4. The Local Government Code of Accounting Practice and Financial Reporting (the Code) states that Councils must maintain an investment policy that complies with the Act, Local Government (General) Regulation 2021 (NSW).
5. The Investment Policy and Strategy are reviewed annually to ensure they remain relevant to prevailing market and legislative conditions. In situations where market volatility and uncertainty arise from changes in the economic, investment and legislative environments, the review may be brought forward for adoption by Council at an earlier date so that key changes can be made to the Policy and Strategy to deal with the respective market conditions.
6. The purpose of the Policy and Strategy is to ensure the investments are secure, satisfy Council's risk / return criteria and are compliant with the Local Government Act 1993, as well as to optimise investment income from the short and long term investment of funds that are surplus to the City's present operational needs.
7. The City's investment portfolio remains conservative due to the robustness of the Australian domestic investment market under the supervision of the Australian Prudential Regulation Authority (APRA) which extends across the full range of financial institutions. The City has gradually diversified from its post 2008 GFC-focused portfolio, which was highly conservative and significantly concentrated in the 'Big 4' AA- rated domestic banks. Its current portfolio remains conservative but more diversified, as it also includes APRA-regulated A+ to A rated bank investments together with a handful of investment-grade A- to BBB+ rated investments.
8. The Policy encourages investments in environmentally and socially responsible investments provided that they meet the risk and return requirements of other investments. Investments will continue to be avoided in institutions that undertake socially harmful activities including the abuse of human rights and labour rights and the sale of armaments.

9. Two amendments were adopted in October 2016 that:
  - (a) strengthened Council's commitment to social and responsible investment where returns and risk are equivalent to other available investments; and
  - (b) expanded the definition of environmentally harmful activities to include specific reference to coal, gas and oil.
10. There are only minor administrative changes including revising the language of the definitions and formatting updates that were incorporated to the policy. The amendments above do not change the overall intent of the Policy but clarifying the City's intent and simplify the administration of the policy.
11. Council's Investment Policy and Investment Strategy continue to permit and encourage environmental and socially responsible investment activity (SRI investments). The Ministerial Investment Order limits the range of financial institutions in which NSW councils can invest and prohibits many of the available socially responsible investment products.
12. The City has good relationships with its financial institutions, and regularly meets to advocate for new investment vehicles and products that will achieve our desire to increase our commitments to social and responsible investment. In a welcome development, in November 2018, Westpac informed the City that they had created a new sustainable investment product known as a Green Tailored Deposit, which has been independently certified to meet the Climate Bonds Standard while not compromising the credit risk of the product. These deposits are associated with a defined pool of eligible assets which meet the Climate Bond Standard criteria including renewable energy, low carbon transport, low carbon intensity emitting buildings, waste and water products and are independently certified annually. Currently, the City has invested \$80 million in this Westpac product type.
13. The City currently holds \$5M in a sustainability bond/floating rate note (FRN) with Bank Australia due to mature on 24 November 2025 and an additional \$4.5M invested in February 2023 due to mature on 22 February 2027. This is based on an investment framework that is in line with the 2021 versions of the ICMA Green Bond Principles (GBP), Social Bond Principles (SBP) and Sustainability Bond Guidelines (SBG). This Socially Responsible investment opportunity meets both the credit risk and maturity profile requirement of the City.
14. The key objectives of the current Investment Strategy remain valid for the present economic, investment and legislative environments. The Strategy remains unchanged, aside from some minor administrative adjustments, as it presently meets liquidity requirements for Council's ongoing capital works program, objectives for investment performance and continues to prudently manage credit risk. Sections of the Investment Strategy that detail the current investment portfolio and its performance were amended to reflect the present results.
15. The proposed Investment Policy and Strategy continue to satisfy the compliance requirements of the Ministerial Investment Order.

16. It should be noted that the Investment Strategy is a 'guiding principles' document. As market conditions change significantly and very quickly, the Strategy may need to be amended from time to time, in which case Council would be advised through the monthly Investment Report.

### **Key Implications**

17. Council's Investment Policy and Investment Strategy direct its investments to ensure compliance with the requirements of the Local Government Act 1993 and Minister's Financial Implications.

### **Financial Implications**

18. 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. These guidelines were developed, in large part, as a response to the Global Financial Crisis and its impact on the local government sectors investments. They effectively limit the City's investment profile to something similar to a cash managed fund, which produces lower returns but provides a high level of security.
19. Annual CPI inflation was 2.8% in the September quarter, significantly down from 3.8% in the June quarter. This is the lowest annual inflation rate since the March 2021 quarter. Even though the inflation has fallen within the target range of 2% to 3%, economic forecasters remain concerned the decline may only be temporary. While global factors explain much of the variation in inflation, domestic factors also continue to play a role. Widespread upward pressures on prices remain in the economy due to strong demand, a tight labour market and capacity constraints in some sectors of the economy.
20. The Reserve Bank of Australia (RBA) board last raised the official cash rate on 7 November 2023, by 25 basis points to 4.35% a 12-year high, up from the record low of 0.10% level in May 2022. While inflation is declining, economic analysts note that the decline has been slower than anticipated, increasing the possibility of a further cash rate rise. However, the general expectation of majority of the banks is that official rates will remain on hold until late this calendar year with potential for rate cuts to follow, provided that the declining inflation trend continues.
21. The City's returns from the investment portfolio are in line with cash managed funds in the market. Past increases to official cash rates have seen improvements in rates of return offered by the market. However, in August 2024 banks began reducing term deposit rates in anticipation of a cash rate cut from the Reserve Bank of Australia, which is expected to occur early in the 2025 calendar year.
22. Annual interest earnings for the 2023/24 financial year were \$38.9M. The annual interest budget for the 2024/25 financial year is \$35.0M.

**Relevant Legislation**

23. Council is authorised to invest its surplus cash under Section 625 of the Local Government Act 1993.
24. The Local Government (General) Regulation 2021 (section 212) requires the City to provide a written monthly report of all monies invested, under Section 625 of the Act.
25. The Local Government Code of Accounting Practice and Financial Reporting (Legislative Requirements Update 10 at 11.3.5) states that Council must maintain an investment policy that complies with the Act and ensure it or its representatives exercise care, diligence and skill that a prudent person would exercise in investing council funds.

**SCOTT MCGILL**

Acting Chief Financial Officer

# **Attachment A**

**2024-25 Investment Policy**

# Investment Policy

## Purpose

The Investment Policy sets out the requirements for the management of the City of Sydney’s (“the City’s”) cash and investment portfolio. The City requires that all investment activities be exercised with the care, diligence and skill of a prudent person, and not for speculative purposes.

The policy sets the framework to:

- safeguard the City’s cash and investments portfolio
- achieve appropriate earnings on invested funds
- manage the City’s cash resources to ensure sufficient liquidity to meet the City’s business objectives over the long, medium and short term.

The policy reinforces the City’s ongoing commitment to maintain a conservative portfolio that balances risk and return, an important component of its ongoing prudent financial management practices.

The Investment Strategy supports the policy by defining investment objectives and actions for the coming year.

The City’s financial policies are developed to ensure that the City satisfies legislative requirements and follows ‘best practice’ in its business operations, with due consideration for the effective and efficient management of resources.

## Scope

This policy applies to all managers and employees who actively manage the City’s Cash and Investments or have responsibility for employees who actively manage the City’s Cash and Investments.

## Definitions

The following definitions illustrate the structure of the City’s investment portfolio and the relationship of the terms referred to in this policy:

Term	Meaning
Authorised Deposit-taking Institution (ADI)	An institution that is authorised under Section 9 of the <i>Banking Act 1959</i> to carry on banking business in Australia in accordance with that Act and under the prudential supervision of the Australian Prudential Regulation Authority (APRA).
Amortised Cost	The amount at which the financial asset is measured at initial recognition, plus or minus the cumulative amortisation of any difference between that initial amount and the maturity amount (i.e. discount or premium on acquisition). Any premium or discount on acquisition is amortised on a straight-line basis over the term of the investment. Where no premium or discount applies, amortised cost will reflect both acquisition and maturity amount of the financial asset.
Benchmark rates	Benchmark rates comprise: <ul style="list-style-type: none"> <li>• Bloomberg AusBond Bank Bill Index - The Bloomberg AusBond Bank Bill index is a widely used industry benchmark constructed to represent the performance of a passively managed short-term money market portfolio</li> <li>• 30 Day Bank Bill Index – The 30 Bank Bill Index is designed to measure the performance of the Australian short-term money market. The index is based on the calculated monthly average of Bank Accepted Bills/Negotiable Certificates of</li> </ul>



	Deposit, as issued by Reserve Bank of Australia (RBA).
<b>Term</b>	<b>Meaning</b>
Business Model	The term ‘business model’ refers to how a Council manages its financial assets in order to generate cash flows. Under AASB 9, classification of financial assets depends on whether the <i>objective</i> of the business model is to generate cash from collecting contractual cash flows over the life of the instrument or collecting contractual cash flows over the life of the instrument and selling financial assets or other.
Cash	<p>Cash comprises:</p> <ul style="list-style-type: none"> <li>• cheque and operational accounts</li> <li>• daily call accounts</li> </ul> <p>with Authorised Deposit-taking Institutions (ADIs).            Cash assets typically have a maturity term at the time of placement of being immediately available or available within 24 hours.            Cash assets are closely linked with investments but do not constitute investments.            Cash is used to meet immediate operational cash needs.</p>
Credit Ratings	Credit rating agencies (see below) assign letters to represent the risk of default and financial viability of the debt issuer, based on quantitative, qualitative, and contextual analyses.
Credit Rating Agencies (CRAs)	Credit rating agencies (CRAs) evaluate and rate the creditworthiness of debt securities and their issuers, including companies and countries. These agencies assign credit risk ratings to such entities based on quantitative and qualitative analyses. Ratings show the likelihood of a borrower to default or repay a loan with interest. Three agencies, Standard & Poor's, Moody's, and Fitch, control nearly the entire credit rating market.
Grandfathered investments	<p>Grandfathered investments are a part of total investments and comprise:</p> <ul style="list-style-type: none"> <li>• investments where additional investment activity is prohibited by regulation; or</li> <li>• other investments over which additional investment activity is temporarily prohibited due to unintentional breaches of investment thresholds and limitations arising from changes in the portfolio subsequent to the acquisition of the affected investment/s.</li> </ul>
Investments	<p>Investments comprise:</p> <ul style="list-style-type: none"> <li>• term/tailored deposits (terminology varies by institution) bonds with an active secondary market with government (including NSW T-Corp and other government treasury bodies) and Authorised Deposit-taking Institutions (ADIs).</li> <li>• Investment assets have maturities at the time of placement of 30 days or more</li> </ul>
Investment Periods	<p><i>Short-term:</i> those investments with less than 12 months to maturity date  <i>Long-term:</i> those investments with greater than 12 months to maturity date</p>
Impairment	The impairment of an investment represents the amount of the original cost of the investment that is not expected to be recovered at the investment’s maturity date due to current adverse economic or investment conditions that impact on the investment’s financial performance.

Definitions relating to statutory accounts, in accordance with Australian Accounting Standards:

Term	Meaning
Cash and cash equivalents	Investment assets that have a maturity date of 90 days or less at the time of acquisition, including: <ul style="list-style-type: none"> <li>• cash</li> <li>• call accounts</li> <li>• term/tailored deposits</li> <li>• bonds with an active secondary market.</li> </ul>
Investments	Investment assets that have a maturity date of greater than 90 days at time of acquisition, including: <ul style="list-style-type: none"> <li>• term/tailored deposits</li> <li>• bonds with an active secondary market</li> </ul> with government (including NSW T-Corp and other government treasury bodies) and Authorised Deposit-taking Institutions (ADIs).

## Policy Statement

The City’s investment objective is to ensure funds that are surplus to the City’s immediate requirements are invested within acceptable risk parameters to optimise interest income while ensuring the security of these funds and maintaining adequate liquidity to meet the City’s operational requirements.

### Legislative authority for investments

All investments are to be made in accordance with:

- Australian Accounting Standards
- Office of Local Government Investment Circulars
- Office of Local Government Investment Policy Guidelines
- Local Government (General) Regulation 2021 – Clause 212
- Local Government Act 1993 (particularly section 625)
- Local Government Code of Accounting Practice & Financial Reporting
- Minister’s Investment Order (gazetted)
- Trustee Act 1925 (NSW) (particularly sections 14A(2), 14C(1) and (2))

### Investment governance and responsibilities

The following internal control practices are in place to ensure adequate governance and allow transparent and clear performance measurement for the management of the City’s cash and investment portfolio:

- financial planning and cash-flow management
- delegated authorities and investment responsibilities
- classification of financial instruments and measurement of investment performance
- performance benchmarks
- investment criteria
- reporting and review
- audit oversight – internal/external

These internal control practices are explained in more detail below.

### **Financial planning and cash-flow management**

Funds that are surplus to the City’s immediate cash requirements will be managed in accordance

with the long, medium and short-term financial cash requirements of the City.

Long term financial plans are developed to ensure the long-term financial sustainability of the City. These plans will incorporate forecasts of cash inflows and outflows to:

- estimate cash surpluses and shortages in future periods
- identify the longer- and medium-term investment horizon for surplus funds.

Shorter term financial plans are used to predict funds availability and monitor the City's cash management needs throughout the year. These cash flow models are monitored daily to facilitate informed investment decisions and to ensure that sufficient liquidity exists to satisfy City's financial commitments.

## ***Delegated authorities and investment responsibilities***

### **Delegations**

Authority for the implementation of the Investment Policy is delegated by Council to the Chief Executive Officer in accordance with the *Local Government Act 1993*.

The Chief Executive Officer has also delegated authority to invest surplus funds to the following positions:

- Chief Operating Officer (COO)
- Chief Financial Officer (CFO)
- other senior financial officers who have the requisite skills to undertake investment functions (as per the Delegations Register).

Officers with delegated authority are required to acknowledge they have received a copy of this policy and understand their obligations in this role.

### **Investments**

The City's Financial Planning and Reporting unit prepares investment recommendations in accordance with this policy and the Investment Strategy. To achieve the best value for the City's investments, recommendations will consider:

- credit risk
- forecast cash requirements
- alternative investments with comparable risk
- liquidity and maturity profiles

A minimum of two price quotations of like or similar investments must be obtained for the acquisition of all market investments in order to verify the fairness of the purchase price.

Two authorised signatories, with appropriate delegation limits, must approve each investment recommendation. Recommendations must be retained on file as a permanent record.

Any single investment exceeding \$5M, or investments with maturity terms (or initial call dates) that exceed 5 years, require approval by any two of the CEO, COO, CFO, Financial Planning and Reporting Manager or Business Planning and Performance Manager. Where a recommendation consists of multiple investments, the amount and maturity of each investment must be considered separately.

### **Cash**

The City retains funds for daily operational payment needs in a combination of a corporate cheque account and/or daily call account/s. Transfers between these accounts are undertaken in order to ensure the cheque account has the appropriate level of funds to fulfil immediate payment obligations of the City and such transfers therefore do not constitute investments in the context of this Policy.

Delegated authority to enable transfers of call funds between the operational and call accounts is as follows:

The Chief Executive Officer has delegated authority to transfer call funds as follows:

- Chief Operating Officer (COO)
- Chief Financial Officer (CFO)
- other senior financial officers who have the requisite skills to undertake investment functions (as per the Delegations Register).

Two authorised signatories, with appropriate delegation limits, must approve each call funds transfer recommendation. Recommendations must be retained on file as a permanent record.

Any single transfer of call funds exceeding \$10M requires approval by any two of the CEO, COO, CFO, Financial Planning and Reporting Manager or Business Planning and Performance Manager.

### **Conflict of interest**

Officers shall not engage in activities that would conflict with the proper execution and management of the City's investment portfolio. Any potential conflicts of interest should be appropriately disclosed in accordance with Council's Code of Conduct.

### ***Classification of financial instruments and measurement of investment performance***

At the City, the primary objective in the purchase of financial investments is to collect contractual cashflows (i.e. interest revenue) over the life of the investment, and redeem the principal sum at maturity, rather than to regularly trade to make a profit. This constitutes a 'Held-to-Maturity business model'; one of three options described under AASB 9 – Financial Instruments. Under AASB 9, the classification and measurement of financial instruments is determined by an entity's business model.

Based upon the 'Held-to-Maturity' Model, all investments held by the City are carried at Amortised Cost. This classification requires any discounts or premiums paid on acquisition of investments to be amortised on a straight-line basis until the investment matures. Note that discounts or premiums on acquisition are only applicable to Floating Rate Note products, and have not historically been common for the City.

Since AASB 9 replaced previous applicable standard AASB 139, periodic adjustments to 'Fair Value' are not required; valuations will still be received on a quarterly basis from investment advisors, but book values will not be adjusted. This approach is more reflective of the City's historical strategy of holding investments to maturity. Any temporary gains or losses on investment values have traditionally not been realised, and investment values have returned to face value at the time of maturity.

The limited investment types permitted under the Ministerial Investment Order are not typically considered to be susceptible to default. In the unlikely event of a financial institution default on an investment held by the City, an impairment entry shall be recognised, to reflect any reduction in expected recoverable amount of the investment.

### ***Performance benchmarks***

Investment performance will be measured monthly against the chosen benchmarks in relation to both current month and 12-month rolling returns.

The City uses independently determined benchmarks. Where the City changes independently determined benchmarks, monthly reports for the month of change and the next five months thereafter shall contain reporting of investment returns against benchmark for both the following:

- the benchmark that is being replaced, and
- the new benchmark backdated on a twelve month basis.

The City currently uses two performance benchmarks:

- Bloomberg AusBond Bank Bill Index – provides a common benchmark against other councils so that the City’s investment performance can be compared on an industry basis and against other portfolios with similar or different risk and reward profiles
- 30 day Bank Bill Rate (sourced from the RBA) – provides a fair indicator of the risk free rate of return so that Council can understand the return that has been earned from diversifying its investment portfolio and accepting conservative levels of risk.

**Investment criteria**

This section sets out the criteria for investments to be considered for inclusion within the City’s portfolio. In particular, it defines the mandatory investment criteria which all investments must satisfy.

Current investment regulations require councils to invest in NSW Treasury Corporation (NSW TCorp), or securities issued by or guaranteed by the Commonwealth, any state of the Commonwealth or a Territory. Investments are also permitted with Approved Deposit-taking Institutions (ADI) such as Australian banks or branches of foreign owned banks, credit unions and/or building societies as it acknowledges the additional assurance that arises from their regulation by the Australian Prudential Regulation Authority (APRA).

**Mandatory Criteria**

**Scope**

Investments must comply with the legislative authorities as described in the *Legislative Authority for Investments* section of this policy.

**Currency**

Investments must be denominated in Australian Dollars.

**Ownership**

Investments must be held in the City of Sydney’s name.

**Term / Maturity**

The term to maturity of investments may not exceed a period of ten (10) years

**Credit rating**

The following credit rating criteria apply to City investments:

- Investments must have a credit rating. The credit rating structure of the total portfolio must comply with the following table:

Thresholds – Portfolio Percentage Limits		
Credit rating / Organisation	Direct investment products (as a % of Total Portfolio)	Exposure to a single institution (as a % of Total Portfolio)
AAA to AA-	100%	33 ⅓ %
ADIs within either the ANZ, Commonwealth Bank, NAB or Westpac Banking Groups ('Big Four')	100%	33 ⅓ %
A+ to A	60%	Maximum is the lesser of \$100M or 5% of Net Equity as per the latest published annual financial statements
A- to BBB+	25%	Maximum is the lesser of \$75M or 5% of Net Equity as per the latest published annual financial statements
BBB to BBB-	10%	Maximum is the lesser \$10M or 10% of the total portfolio

- The above table reflects the long-term credit rating scale of S&P, which is the primary rating scale used by the City. Credit risk investment parameters are based on credit rating bands as published by the credit rating agencies (e.g. S&P, Moody’s and Fitch). If an investment is rated by more than one ratings agency, the credit rating to be used will be based on the order of S&P, Moody’s and then Fitch.
- Credit ratings apply to both products and institutions. However, this policy requires the rating applicable to the institution responsible for the product (e.g. guarantor) to be taken as the relevant rating given this represents the underlying risk to the City. Where there is a disparity between the credit rating of the institution and an individual investment product, the lower of the two ratings is adopted in applying the requirements of this Policy.
- Credit ratings must be monitored regularly by Office of the CFO staff to ensure ongoing compliance. Investments with credit ratings downgraded to an extent that they no longer comply will be divested as soon as practicable, in accordance with the grandfathering provisions of this policy.
- Where the principal amount and accrued interest of any investment with a financial institution are directly guaranteed by the Australian Federal Government for full repayment, the parameters in the table above may be exceeded as follows:
  - exposure to single institutions may exceed the stated limits provided that the excess amount comprises only guaranteed investments
  - exposure of the total portfolio to credit ratings lower than AAA may be exceeded, provided that the excess amount comprises only guaranteed investments. As a result, investments directly guaranteed by the Australian Federal Government may comprise the total investment portfolio. Management should ensure that any excess of investments over the parameters specified in the table above that is comprised of Australian Federal Government guaranteed investments can be managed back to within the specified parameter levels prior to the expiration of any such guarantee.

**Portfolio liquidity parameters**

The portfolio liquidity parameters specify the maximum and minimum amounts or percentages of the City’s total investment portfolio that can be held within the various investment maturity bands.

Minimum thresholds are set to ensure adequate liquidity in earlier maturity bands before funds are committed to longer term investments. The minimum thresholds are obviously higher in the shorter term where liquidity is of greater priority. The cumulative nature of the minimum threshold limits inherently generates corresponding maximum thresholds; that is, maximum amounts that can be invested in each maturity band while remaining compliant with the minimum threshold limits. The liquidity / maturity profile of the total portfolio must comply with the parameters shown in the tables below:

	1 month	up to 12 months	up to 3 Years	up to 5 Years	up to and greater than 5 Years
Cumulative Minimum % of Total Portfolio	10% or \$50M <i>(greater of)</i>	40%	55%	90%	100%

The following example illustrates the effect of the minimum threshold for a \$700M investment portfolio size:

<b>Terms (time to maturity)</b>	<b>Parameter (minimum % cumulative)</b>	<b>Minimum Amount by category (Cumulative)</b>	<b>Maximum Amount by category</b>
1 month	10%	70,000,000	700,000,000
Up to 12 months	40%	280,000,000	630,000,000
Up to 3 Years	55%	385,000,000	420,000,000
Up to 5 Years	90%	630,000,000	315,000,000
Up to and greater than 5 Years	100%	700,000,000	70,000,000

The following example demonstrates the relationship of the maximum and cumulative minimum thresholds. Before an investment can be considered for a particular maturity band, firstly the total portfolio must comply with the cumulative minimum thresholds and secondly, the investment should then not cause the maximum thresholds to be exceeded.

Example: an investment of 2 years duration is being considered. The following thresholds must be complied with:

- First, at least 40% (or \$280M) of the total portfolio must have a maturity date of 12 months or less and 10% of the portfolio, in this case \$70M, must have a maturity date of less than 1 month.
- Secondly, once the investment is added to the portfolio, the total amount of investments maturing between 1 to 3 years must not exceed 60% of the total portfolio (i.e. \$420M).

The cumulative thresholds are primarily aimed at ensuring minimum liquidity requirements are always met while allowing an appropriate spread of investment maturity dates across the portfolio. Accordingly, if investment holdings of shorter-term investments exceed a minimum threshold for a maturity band, the excess may also be applied to the succeeding maturity band/s. For the example portfolio of \$700M above, if 40% of the portfolio (\$280M) or more has a maturity date of less than one month, the threshold level for investments of up to 12 months has also been met, and investments of greater than 12 months can be considered. Upon reinvestment, consideration must be given to ensuring that the minimum thresholds of the respective maturity bands are maintained as shorter-term investments mature.

The minimum requirement for very short term (30 days) access to investments is set at the greater of \$50M or 10% of the portfolio balance to ensure adequate liquidity to meet the City’s working capital requirements.

The City may utilise pre-approved overdraft facilities to manage short-term liquidity shortfalls where it is both prudent and financially advantageous. It is anticipated that this facility would be utilised to avoid penalties arising from early redemption of term deposits or where favourable investments arise a day or two ahead of the maturity dates of existing investments that are earmarked for future investment. Overdrafts should be limited to no more than \$10M and for a duration of no more than 2 weeks.

## Breaches of criteria

Procedures for dealing with unavoidable breaches of any particular thresholds are contained in the next section on grandfathering of investments.

## Grandfathering of Investments

This policy imposes limits and thresholds in relation to the acquisition and holding of investments. However, situations may occur where inadvertent breaches of these limitations or thresholds arise, other than from the acquisition of investments. For example:

- amendments to regulatory directives or legislation
- changes in the total value or amount of the City's investment portfolio which consequently changes any of the threshold limits so that they no longer meet the portfolio liquidity parameters.

### Breach as a result of regulatory change

When limitations or thresholds are breached due to amendments to regulatory directives or legislation, the investment portfolio must be managed in accordance with the respective amendments. Where the amendments enable retention and grandfathering of existing investments, the City may continue to actively manage those investments within the portfolio in accordance with all other regulations and policies applicable to such investments. This includes a strategy of holding or divesting such investments in accordance with regular investment considerations.

### Breach in order to meet operational requirements

Where the limitation or threshold is breached for a one-month period, in situations where short term cash is needed for urgent operational use, the breach would be authorised and no further investing activities will be made beyond 30 days.

### Breach as a result of change in total investment portfolio

Where limitations or thresholds are breached due to a change in the overall size of the total investment portfolio, the following process will apply:

- an immediate freeze is imposed on the acquisition of new investments in greater than relevant category until the portfolio can be effectively managed back to accord with the requirements of this policy;
- the relevant category of investments must be managed back in accord with the policy limits within a period that takes into account any adversity created by market liquidity, current valuations of these investments and the risks of default.

The immediate forced sale of the investments in breach of the limits or thresholds will not be required.

## Reporting and Review

The City will maintain a separate record of money it has invested under section 625 of the *Local Government Act 1993*, in accordance with the criteria defined by the *Local Government Code of Accounting Practice and Financial Reporting*.

Pursuant to the *Local Government (General) Regulation 2021* (clause 212), the City will provide a monthly report to Council on investments. The monthly report to Council will include:

- the total value of the portfolio
- a complete schedule of all investments within the total portfolio
- full disclosure of all investments by type, current credit rating and face value
- net investment income for the month (actual against budget)
- the weighted average investment returns for the current month and the last 12 months rolling period (actual against benchmark)
- informative commentary on portfolio compliance and performance, current economic investment environment, and any change to current strategy
- assurance that investments accord with the Act, regulations and Council's investment policy and



strategy.

- analysis of the portfolio's liquidity (maturity) profile
- analysis of the portfolio's risk profile (credit ratings)
- analysis of the portfolio's product diversification (investment types)
- cumulative performance over Bloomberg AusBond Bank Bill Index and 30 day Bank Bill Rate

In accordance with the Local Government Code of Accounting Practice & Financial Reporting, the City will undertake an annual review of its Investment Policy and Investment Strategy.

If there are any significant changes to the Act, regulations, issued guidelines, or if the market changes to a degree that warrants an earlier examination, the Policy and/or Strategy will be reviewed and brought back to Council for its consideration.

### **Evaluation**

The policy is evaluated through the measured results incorporated in monthly reporting of investment performance to Council.

### **Audit Oversight**

The City's external auditors will review City's investments as part of the Annual Financial Reports. This may include seeking independent certification from the relevant financial institutions (banks, fund managers, etc.) to confirm the balance of investments held on the City's behalf at the end of the financial year, and testing the adequacy of internal control procedures.

The City's Internal Audit unit will also periodically review the adequacy of the Investment Policy, Strategy and management's internal controls as part of its audit review program.

## **Investment Strategy**

The City will prepare an annual Investment Strategy to guide the management of its surplus cash and investments within the requirements of this policy.

The Investment Strategy will document all key objectives relating to management of cash and investment assets over the short to medium term in the context of prevailing market conditions at the time. The strategy will:

- consider the City's current investment portfolio, its financial position and financial commitments, current legislative constraints and the global investment environment
- specify our investment goals and targets for the forthcoming year.

Mandatory components of the City's Investment Strategy will comprise the management of the following aspects of the investment portfolio:

- risk profile
- liquidity/maturity
- return/income
- environmentally and socially responsible investments

Requirements in respect of each component are detailed below.

### **Risk Profile**

The City's risk profile in relation to investing surplus funds is prudent, conservative and risk averse. The profile will be achieved by effectively managing within the investment portfolio:

- the *diversity* of the investments
- the *creditworthiness* of the investments

*Diversity* is achieved by placing limits on the maximum exposure the City may have to individual:

- funds or financial institutions
- credit rating bands.

*Creditworthiness* of investments is primarily determined using long term industry standard credit ratings by Standard & Poors (S&P), Moody's or Fitch. The City will not invest in non-rated institutions.

### **Liquidity/Maturity**

The cash requirements of the City will be satisfied by monitoring and structuring the total maturity profile of the investment portfolio in accordance with the Investment Policy.

### **Return/Income**

Investment returns are closely correlated to the risk profile of the underlying investments. Appropriate benchmark rates of return will be set in relation to the risk profile and returns will be required to meet or exceed benchmark rates.

### **Environmentally and socially responsible investments**

Subject to compliance with legislation and investment policy objectives and parameters, the City preferences investment securities and financial institutions that meet our socially responsible investments (SRI) criteria. SRI status may be in respect of the individual investment, the issuer of the investment, or both and should be endorsed by an accredited environmentally and socially responsible industry body or institution.

Environmentally and Socially Responsible Investments will be assessed on the same basis as other investment opportunities and the City will select the investment that best meets its overall investment selection criteria.

The City's criteria relating to an SRI are those which:

- direct investment towards the socially and environmentally **productive** activities listed below
- avoid investment in the socially and environmentally **harmful** activities listed below.

The criteria for SRI are all preferred and not mandatory requirements.

Environmentally **productive** activities are considered to be:

- resource efficiency-especially water and energy
- renewable energy
- production of environmentally friendly products
- recycling, and waste and emissions reduction

Socially **productive** activities are considered to be:

- fair trade and provision of a living wage
- human health and aged care
- equal opportunity employers, and those that support the values of communities, indigenous peoples and minorities
- provision of housing, especially affordable or social housing

Environmentally **harmful** activities are considered to be:

- production of pollutants, toxins and greenhouse gases (coal, oil and gas)
- habitat destruction, especially destruction of forests and marine eco-systems.
- nuclear power
- uranium mining

Socially **harmful** activities are considered to be:

**Investment Policy** – Approved Month, Year

- abuse of Human Rights and Labour Rights
- involvement in bribery/corruption
- production or supply of armaments
- manufacture of alcohol, tobacco or gambling products

The City will continue to advocate for the further development of SRI options through engagement with financial institutions.

## References

Laws and Standards
<ul style="list-style-type: none"> <li>• Australian Accounting Standards</li> <li>• Office of Local Government – Local Government Code of Accounting Practice &amp; Financial Reporting</li> <li>• Office of Local Government Circulars</li> <li>• Office of Local Government Investment Policy Guidelines</li> <li>• Local Government (General) Regulation 2021</li> <li>• Local Government Act 1993</li> <li>• Minister’s Investment Order (gazetted)</li> <li>• Trustee Act 1925 (NSW)</li> </ul>
Policies and Procedures
<ul style="list-style-type: none"> <li>• Code of Conduct</li> <li>• Disciplinary Policy &amp; Procedures</li> <li>• Internal Reporting Policy – Corrupt Conduct and Serious Wrongdoing</li> <li>• Investment Strategy</li> </ul>

## Review period

This policy will be reviewed every year.

## Approval Status

The Council approved this policy on

## Approval History

Stage	Date	Comment	TRIM Reference
Original Policy	29 October 2018	Approved by Council	2019/018769
Reviewed	28 October 2019	Approved by Council	2019/604444, 2019/018769 (pdf)
Reviewed	26 October 2020	Approved by Council	2020/483244
Reviewed	18 October 2021	Approved by Council	2020/483244

Reviewed	31 October 2022	Approved by Council	2020/483244
Reviewed	23 October 2023	Approved by Council	2020/483244
Approval Due Date	25 November 2024		

**Ownership and approval**

<b>Responsibility</b>	<b>Role</b>
Author	Financial Planning and Reporting Manager
Owner	Chief Financial Officer
Endorser	Chief Executive Officer
Approver	City of Sydney Council

# **Attachment B**

**2024-25 Investment Strategy**

# Investment Strategy

## Purpose

The annual Investment Strategy (“the Strategy”) sets out the City of Sydney’s (“the City’s”) investment goals and targets for the coming year. The aim of the Strategy is to guide the management of the City’s investment portfolio to:

- achieve a balanced and diversified portfolio, in terms of allowable investment products, credit ratings and maturation terms that will outperform the benchmark indices
- ensure liquidity requirements are met for the City’s operational and capital expenditure needs.

## Scope

The *Investment Strategy* applies to all managers and workers who actively manage the investment of surplus funds or have responsibility for workers who actively manage the investment of surplus funds.

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

## Context

The City’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

Annual CPI inflation increased to 3.8 per cent in the June 2024 quarter, up from 3.6 per cent in the March 2024 quarter, but lower than the 4.1 per cent annual rise in the December 2023 quarter. The rate of inflation remains above the Reserve Bank of Australia’s (RBA) target range of two to three per cent. While global factors explain much of the variation in inflation, domestic factors also continue to play a role. Widespread upward pressures on prices remain in the economy due to strong demand, a tight labour market and capacity constraints in some sectors of the economy.

The Reserve Bank of Australia (RBA) board most recently raised the official cash rate on 7 November 2023, by 25 basis points to 4.35 per cent, a 12-year high, up from the record low of 0.10 per cent level in May 2022. While inflation is declining, economic analysts note that the decline has been slower than anticipated, increasing the possibility of a further cash rate rise. However, the general expectation of the majority of banks is that official rates will remain on hold until late this calendar year, provided that the declining inflation trend continues, with potential for rate cuts to follow.

In Australia, a history of judicious regulation of the financial institutions by the Australian Prudential Regulation Authority (APRA) has meant that Australian based regulated financial institutions have already operated for an extended period under stringent capital adequacy and liquidity requirements. The City’s investments all fall under APRA regulation with the result that the portfolio is conservative and secure.

**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 several years and the most recent Ministerial Investment Order released in January 2011 continues to limit Council’s investment options to:

- term deposits with Authorised Deposit-taking Institutions (ADIs)
- other ADI senior ranked securities
- investments with Australian government treasury bodies, including NSW Treasury Corporation (T-Corp)
- funds or securities issued or guaranteed by the Commonwealth or any State or Territory.

These guidelines were developed, in large part, as a response to the Global Financial Crisis and its impact on the local government sector’s investments. They effectively limit the City’s investment profile to something similar to a cash managed fund, which generally produce lower returns but provide a high level of security. The City’s returns from the investment portfolio remain in line with cash managed funds in the market.

**Composition of the City’s investment portfolio**

The conservative nature of Council’s Investment Strategy is clearly reflected in the structure of the portfolio, where 100% of the portfolio is invested with APRA-regulated ADIs.

Council’s current portfolio is as follows (as at the end of August 2024):

Investment	Split
Big Four banks	70%
Australian mid-tier banks	17%
Australian government treasury bodies	1%
Foreign controlled Australian based ADIs	12%
<b>Total</b>	<b>100%</b>

The allocation of assets within the portfolio is with very secure institutions. In the past year, the City has diversified the portfolio with further selected investment into the Australian mid-tier banks as they continue to reflect strength and stability.

## Investment strategy

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

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

## Objectives

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

As noted in the investment policy, the City's primary objective in the purchase of financial investments is to collect contractual cash flows (i.e. interest revenue) over the life of the investment, and redeem the principal sum at maturity, rather than to regularly trade to make a profit. This constitutes a 'Held-to-Maturity business model'; one of three options described under AASB 9 – Financial Instruments. Under AASB 9, the classification and measurement of financial instruments is determined by an entity's business model.

## Risk profile

The risk profile for the City'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.

The City's capital funding requirements will continue to remain high over coming years, including the funding of an expansive capital works program, potential community and commercial property acquisitions and the purchase of land for future open space. As a result, the maturity profile of the investment portfolio has generally become more concentrated in the short and medium term rather than the longer term. The maturity profile of the investments is adequately spread over those periods to ensure that liquidity and maturity risks are also kept to a minimum. All of these investments are held with APRA regulated financial institutions so that credit risk likewise remains minimal.

The most favourable market for term deposits is often with the APRA regulated Big Four Banks and Australian mid- tier banks. Accordingly, investments with these banks comprise approximately 87% of the City's total holdings at the time of writing and provide diversity within the portfolio.

## Liquidity / Maturity

A significant portion of the City's cash and investments portfolio is held as internally restricted and externally restricted cash reserves to satisfy the City's legislative responsibilities and to set aside specific funds for the City's funding commitments to the major initiatives within the Delivering Sustainable Sydney 2030-2050 Community Strategic Plan.



To ensure the City has available funds to meet these commitments and its short-term operational and capital cash commitments, the following liquidity targets are set in accordance with the Investment Policy.

Investment period	Cumulative Minimum % of total portfolio
1 month	10% or \$50M <i>(the greater of)</i>
2 to 12 months	40%
1 to 3 Years	55%
3 to 5 Years	90%
> 5 Years	100%

The City’s liquidity is monitored on a daily basis to ensure the City’s cash requirements are met and that liquidity parameters remain within allowable limits set out in the *Investment Policy*.

**Return / Income**

The City uses the following benchmarks to measure investment performance, in relation to both current month and 12-month rolling returns, against its return/income objectives:

- Bloomberg AusBond Bank Bill Index
- 30 day Bank Bill Rate as published by the Reserve Bank of Australia

The City aims to achieve portfolio returns equal to or above these benchmark rates for the period. However, this achievement remains secondary to the critical strategies of maintaining a prudent and conservative risk profile and in meeting the City’s liquidity needs. This includes immediate operational and capital commitments as well as future years’ capital commitments.

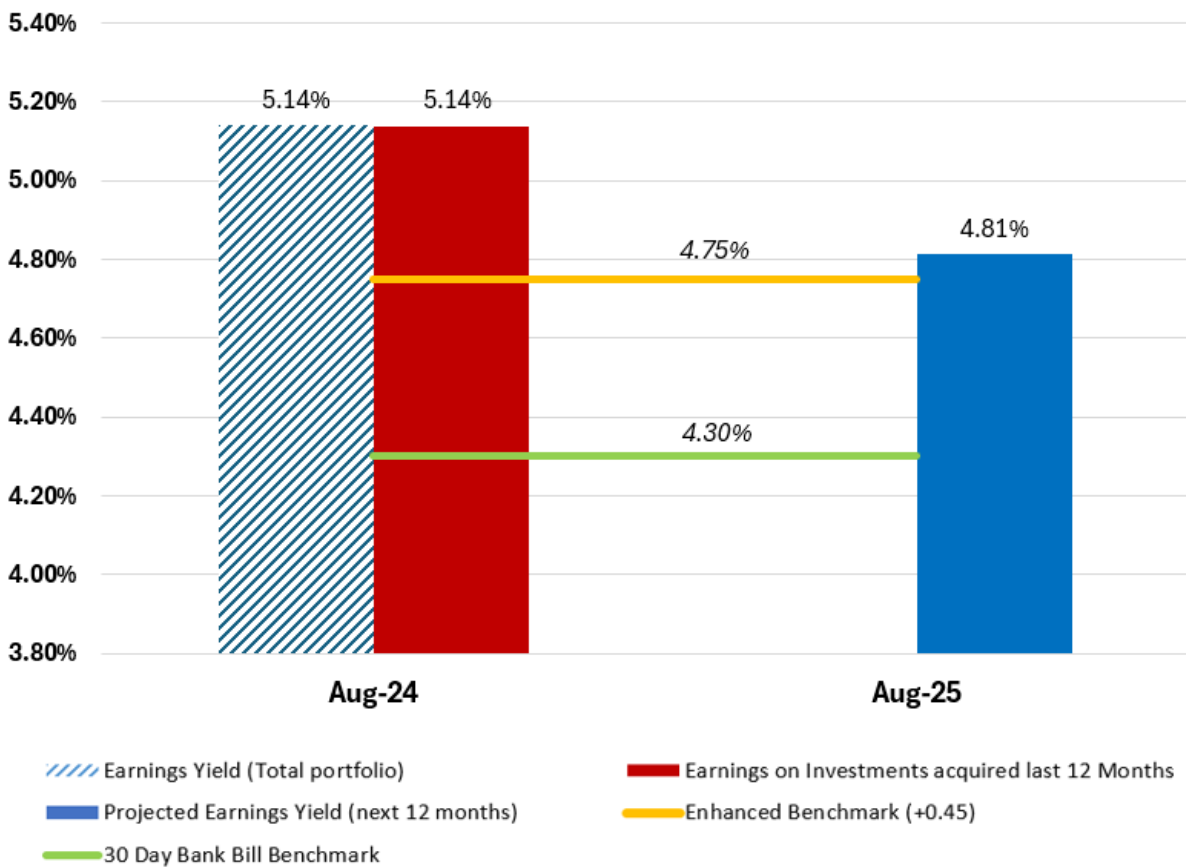
In addition, the City has utilised an additional strategic benchmark rate to measure its investment performance - exceeding the 30 day benchmark returns by at least 45 additional basis points (0.45% p.a.). The 45 basis point increase is based on observed historical average increased credit spreads (or margins) over bank bill rates on offer in relation to 30–90 day investments. The 30-90 bank bill rates represented a reflective benchmark at the time of adoption.

The City's returns from the investment portfolio are in line with cash managed funds in the market. As at August 2024 around 70 per cent of the portfolio, including at call account, is due to mature in the coming year. Past increases to official cash rates have seen improvements in rates of return offered by the market. Most banks anticipate that official rates will stay unchanged until late this year, as long as the downward trend in inflation persists, with possible rate cuts afterward. In August 2024 banks began reducing term deposit rates in anticipation of a cash rate cut from the Reserve Bank of Australia, which is expected to occur in early 2025 calendar year.

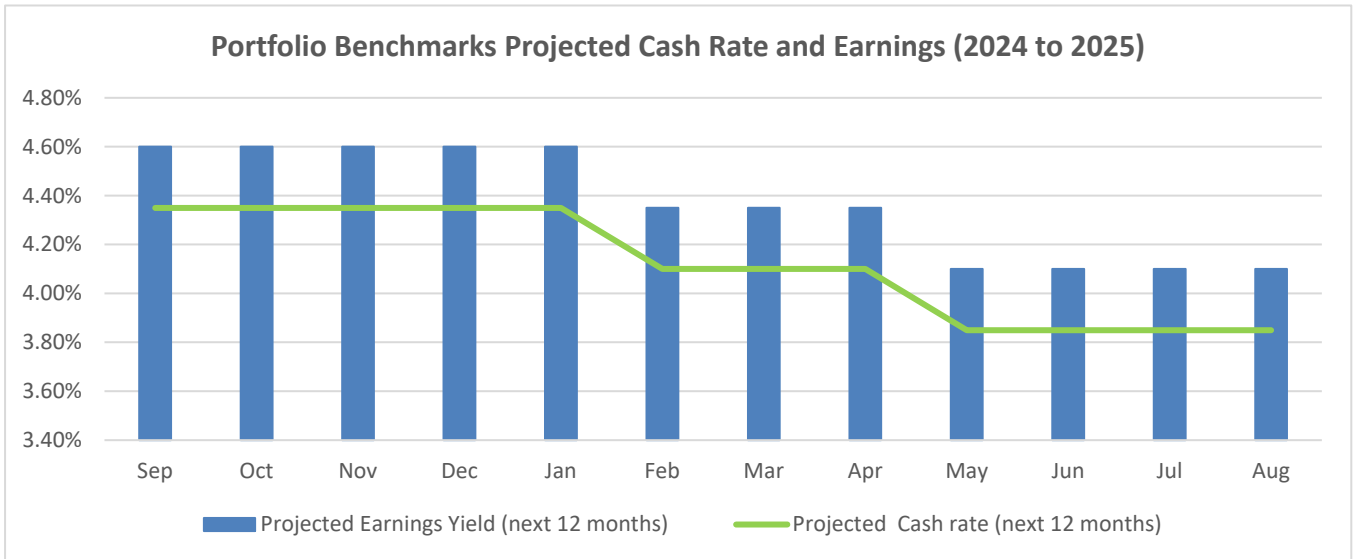
The following chart illustrates how earnings yields may potentially be impacted over the coming year as a result of the above factors. The chart assumes the re-investment of maturing deposits at prevailing rates at the time of writing.

Previous increases in official cash rates led to better rates of return available in the market. However, market expectations suggest that the RBA will first reduce interest rates by 25 basis points in February 2025, followed by three additional cuts by August 2025. This is the first forecast of multiple rate cuts since the Reserve Bank began raising rates in May 2022.

**Portfolio Performance against Benchmarks  
Current and Projected (2024 to 2025)**



This trend is anticipated to continue beyond the current financial year which is represented in the chart below. The below chart represents a correlation between the cash rate and projected earnings yield for the next 12 months.



**Environmentally and Socially Responsible Investments**

The City’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
- excess demand for environmentally and socially responsible investments has reduced market rates of return on these products.

The City will, however, continue to explore opportunities for supporting environmentally and socially responsible investments within these constraints. The investment climate is changing over time and the City notes that many large scale renewable projects are expected to evolve, which may result in additional sustainable investment offers in the medium to long term. The City has continued to strive to acquire environmentally and socially responsible investments, but opportunities to invest further are constrained by market conditions, particularly the credit rating of investments and associated investment limits under the City’s Investment Policy. The City 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.

In an increasingly volatile world, it should be noted that the investment policy continues to contain provisions that encourage environmentally and socially responsible investments (SRI) and seek to avoid investments in environmentally and socially harmful activities.

**References**

<b>Laws and standards</b>	<ul style="list-style-type: none"> <li>• Local Government Act 1993</li> <li>• Local Government (General) Regulation 2021</li> <li>• Ministerial Investment Order</li> <li>• Local Government Code of Accounting Practice and Financial Reporting</li> <li>• Australian Accounting Standards</li> <li>• Office of Local Government Circulars</li> </ul>
<b>Policies and procedures</b>	<ul style="list-style-type: none"> <li>• Investment Policy</li> </ul>

**Approval**

**Review**

Review period	Next review date	TRIM reference
The Code of Accounting Practice & Financial Reporting requires Council to undertake an annual review of its Investment Policy and Investment Strategy.	October 2024	