Quarterly Report

Quarter 4: 2017 - 2018
Period ended: 30 June 2018

LGFA
NEW ZEALAND
LOCAL GOVERNMENT
FUNDING AGENCY

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A. June quarter issuance and highlights summary

Quarter	Total	Bespoke Maturity	2019	2020	2021	2022	2023	2025	2027	2033
Bonds issued $m	**490**	N/A		-	-	270	-	120	30	70
Term Loans to councils $m	**386.5**	212.7			3	52	33	65.8	20	-
Term Loans to councils #.	**37**	21			1	2	4	8	1	

Year to date	Total	Bespoke Maturity	2019	2020	2021	2022	2023	2025	2027	2033
Bonds issued $m	**1,229**	N/A	40	225	70	270	79	309	96	140
Term Loans to councils $m	**1087.9**	734.5	5	5	8	87.1	51.5	111.8	73	12
Term Loans to councils #	**129**	77	1	1	3	14	10	15	6	2

Key points and highlights for the June quarter:

- The LGFA bond curve fell over the quarter with yields declining between 5 bps (2019s) and 20 bps (2021s) while the 2033 bond yield fell 12 bps (0.12%).
- LGFA issued $490 million of bonds during the quarter across three tenders including a new April 2022 bond. The June quarter has historically been a busy quarter for issuance, averaging $461 million of issuance over the past six years. The average term of issuance during the quarter of 6.56 years was above the average term for the current year of 6.07 years but shorter than the average term for the prior year of 8.87 years. LGFA bonds outstanding as at 30 June 2018 were $8.119 billion (including $400 million of treasury stock).
- LGFA margins to swap contracted at both end points of the LGFA curve but were slightly wider in the mid curve maturities e.g. the 2033 LGFA spread to swap tightened by 13 bps while the 2025 LGFA spread to swap widened by 2 bps. Domestic investors were selling mid curve bonds to switch into a large amount of new domestic bond issuance while offshore investors were buying the longer end of the curve. LGFA Spreads to NZGB also displayed the same pattern with 2021 spreads tighter by 10 bps but 2023 spreads to NZGBs wider by 3bps.
- Long dated on-lending to council borrowers was $386.5 million including $212.7 million of bespoke maturity loans (55% of total lending) during the quarter. The average term of on-lending during the quarter was 6.18 years which was slightly shorter than the average loan term of 6.9 years for the current year and 8.1 years in the prior year.
- LGFA market share of 70% for the rolling 12-month period to June 2018 was down from 83% a year ago due to Christchurch City Holdings, Dunedin City Treasury and Auckland Council issuing in their own name over the past year.
- Short-term lending to councils remains well supported by councils with loans outstanding of $244 million as at 30 June 2018. This was a decline of $25 million over the quarter and the number of councils using this product declined by one to nineteen but this reflected a seasonal pattern.
- LGFA Net Operating Gain (unaudited) for the twelve-month period to June 2018 was $11.834 million or $0.953 million above budget.
- Stratford and Westland District Councils joined as non-guarantors during the quarter, bringing total membership to fifty-six council members. We would expect at least another five councils to join in the coming year.

B. LGFA bond tenders during quarter

LGFA held three bond tenders during the quarter.

Tender 54: 4 April 2018 $190 million

Tender 54 Tender date: 4 Apr 2018	**Apr-22**	**Apr-25**
Total amount offered $m	150	40
Total amount allocated $m	150	40
Total number bids received	34	19
Total amount of bids received $m	395.3	123.5
Total number of successful bids	6	4
Highest accepted yield %	2.805	3.410
Lowest yield accepted %	2.775	3.400
Highest yield rejected %	2.970	3.535
Lowest yield rejected %	2.805	3.410
Weighted average accepted yield %	2.786	3.410
Weighted average rejected yield %	2.860	3.456
Coverage ratio	2.64	3.09
NZGB spread at issue bps	59	83.5
Swap spread at issue bps	25.4	53.8
Swap spread: AA council bps	36.5	62.75
Swap spread: AA- council bps	41.5	67.75
Swap spread: A+ council bps	46.5	72.75
Swap spread: unrated council bps	56.5	82.75

The highlight was the debut issuance of the 14 April 2022 bond which was the first time that we have issued into a non NZGB maturity date.

We tendered only two tranches with $150 million of the 2022s and $40 million of the 2025s and these were shorter dated maturities than usual due to the soft market conditions. Price support was good with successful yields for the 2022s (at implied mid-rate) and okay for the 2025s (at 3 bps above mid- rate).

Bidding was in line with expectations with six successful bids for the 2022s and four bids for the 2025s and successful bid ranges were 2.5 bps wide on the 2022s and 1 bps wide on the 2025s.

The spread to swap compared to the previous (February 2018) tender was 1.5 bps wider on the 2025s and the spread to NZGB was 6.5 bps wider. This highlights the softening in credit markets in line with the equity market weakness over the previous seven weeks.

The average maturity of the LGFA bonds issued was very short at 4.66 years. Coverage ratio of 2.7 times was good considering the larger amount tendered and the prevailing market background. The previous two tenders had coverage ratios of 3.9 times.

While we issued $190 million of LGFA bonds we on-lent $83 million to six councils. The balance of issuance was used to cover $67 million of lending undertaken with six councils during the period since the February tender and to ensure we have sufficient cash to lend to councils over the five-week period until the May tender.

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Tender 55: 10 May 2018 $150 million

Tender 55 Tender date: 10 May 2018	**Apr-22**	**Apr-25**	**Apr-33**
Total amount offered $m	60	50	40
Total amount allocated $m	60	50	40
Total number bids received	21	20	20
Total amount of bids received $m	237	166	109
Total number of successful bids	9	5	6
Highest accepted yield %	2.800	3.425	4.265
Lowest yield accepted %	2.770	3.410	4.245
Highest yield rejected %	2.880	3.540	4.520
Lowest yield rejected %	2.800	3.430	4.270
Weighted average accepted yield %	2.790	3.415	4.263
Weighted average rejected yield %	2.833	3.467	4.339
Coverage ratio	3.95	3.32	2.73
NZGB spread at issue bps	58.5	80.5	110
Swap spread at issue bps	20	44	79
Swap spread: AA council bps	30.5	53.5	87
Swap spread: AA- council bps	35.5	58.5	92
Swap spread: A+ council bps	40.5	63.5	97
Swap spread: unrated council bps	50.5	73.5	107

We tendered three tranches with $60 million of the 2022s, $50 million of the 2025s and $40 million of the 2033s. We tendered the 2033s for the first time since December 2017 as there had been recent offshore interest to buy this maturity. Price support was very good with successful yields for all maturities at or very close to prevailing mid rates at the time of the tender.

Bidding exceeded expectations with nine, five and six successful bids for the three maturities (2022, 2025 and 2033) and tight successful bid ranges of 3 bps, 1.5 bps and 2 bps wide respectively.

The spread to NZGB compared to the previous April 2018 tender was 0.5 bps tighter on the 2022s and 1.5 bps tighter on the 2025s. The spread to swap tightened by 6 bps and 9 bps so a very pleasing outcome.

The average maturity of the LGFA bonds issued at 9.84 years was twice that of the April 2018 tender and was the longest since June 2017.

Coverage ratio of 3.4 times was very good considering the slightly larger amount tendered and the longer term of bonds issued.

While we issued $150 million of LGFA bonds we on-lent $136 million to ten councils. The balance of issuance was used to cover $10 million of lending we undertook with two councils during the period between the April and May tenders.

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Tender 56: 13 June 2018 $150 million

Tender 56 Tender date: 13 June 2018	**Apr-22**	**Apr-25**	**Apr-27**	**Apr-33**
Total amount offered $m	60	30	30	30
Total amount allocated $m	60	30	30	30
Total number bids received	13	11	9	9
Total amount of bids received $m	127	94	68	86
Total number of successful bids	3	4	1	1
Highest accepted yield %	2.730	3.440	3.635	4.235
Lowest yield accepted %	2.720	3.435	3.635	4.235
Highest yield rejected %	2.810	3.480	3.715	4.350
Lowest yield rejected %	2.730	3.440	3.680	4.250
Weighted average accepted yield %	2.723	3.440	3.635	4.235
Weighted average rejected yield %	2.770	3.457	3.691	4.270
Coverage ratio	2.12	3.13	2.27	2.87
NZGB spread at issue bps	53	81.5	82	105
Swap spread at issue bps	19.3	51	52.3	77.7
Swap spread: AA council bps	29.5	60	66.25	85
Swap spread: AA- council bps	34.5	65	71.25	90
Swap spread: A+ council bps	39.5	70	76.25	95
Swap spread: unrated council bps	49.5	80	86.25	105

We tendered four tranches comprising $60 million of the 2022s, and $30 million each of the 2025s, 2027s and 2033s. This is the second successive tender of 2033s albeit on small volume. Price support was positive with successful yields 3 to 4 bps tighter on the 2022s and 2027s relative to prevailing mid rates at the time of the tender while the 2025 and 2033s were issued at mid rates.

Bidding was mixed with only a handful of successful aggressive bids (a positive) but bid coverage ratios were soft. There were three and four successful bids for the 2022s and 2025s and one each for the 2027s and 2033s. The successful bid ranges were also tight at between zero and 1 bps wide across the four maturities.

The spread to NZGB compared to the May 2018 tender was 5 bps tighter on the 2022s and 2033s and 1 bps wider on the 2025s. The spread to swap was unchanged on the 2022s, 6.5bps wider on the 2025s and 1 bps tighter on the 2033s.

The average maturity of the LGFA bonds issued at 7.76 years was slightly longer than the annual average of 7.64 years.

Coverage ratio of 2.5 times was weak but reflects the large supply of bonds into the market since the May tender.

While we issued $150 million of LGFA bonds we on-lent $118.3 million to ten councils. The balance of issuance was used to cover $37 million of lending we undertook with three councils since the previous tender in May.

C. Key performance indicators

We have met only one of the four KPIs as at the end of the June quarter. We have maintained issuance and operating expenses below budget but were unable to meet the other three KPIs which are influenced by factors outside of our control e.g. amount of borrowing undertaken by councils and the term of borrowing.

Due to the reduction in short term lending over the quarter (and being replaced by increased longer dated lending) the average base margin widened by 0.003% to remain above 10 bps. We have lowered our base lending margin for 2018-19 to ensure we achieve this target going forward. We are struggling to improve our estimated interest cost savings due to secondary market spreads on our comparable group (Auckland and Dunedin councils) tightening more than the move in LGFA spreads to swap. This is due to LGFA issuing long dated bonds on a regular basis and a lack of issuance by the other councils. The spread will tend to narrow with the passage of time e.g. the 2019 bond was a two-year comparable bond a year ago and it is now a one-year bond, so over the past year the spread will naturally tighten. Our volume of council lending is currently below SOI forecast and this is due to the December 2017 loans rolling off, more subdued borrowing by councils relative to forecast and our largest borrower Auckland Council preferring to borrow in offshore markets and therefore did not borrow from LGFA in the past year.

Measure		**Prior full year to June 2017**	**Q1 30 Sept 2017**	**Q2 31 Dec 2017**	**Q3 31 Mar 2018**	**Q4 30 June 2018**
Average base margin over cost of funds for short term and long-term lending	Target %		< 0.10%			
	Average actual %	0.104%	0.094% (0.1086% for long term and 0.08% for short term) ✓	0.097% (0.1071% for long term and 0.09% for short term) ✓	0.102% (0.1080% for long term and 0.09% for short term) ✗	.105% (0.1082% for long term and 0.09% for short term) ✗
Estimated interest cost savings	Target Improvement on prior year as at each quarter		**Q1 30 Sept 2017**	**Q2 31 Dec 2017**	**Q3 31 Mar 2018**	**Q4 30 June 2018**
	2019 maturity At quarter end	12 bps	11 bps ✗	10 bps ✗	10 bps ✗	11 bps ✗
	2021 maturity At quarter end	20 bps	13 bps ✗	18 bps ✗	14 bps ✗	19 bps ✗
	2025 maturity At quarter end	17 bps	5 bps ✗	14 bps ✗	11 bps ✗	10 bps ✗

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Issuance and operating expenses (excluding AIL) YTD	Target ($ m)		$1.33 m (YTD as at Q1)	$2.73 m (YTD as at Q2)	$4.02 m (YTD as at Q3)	$5.45 m (FULL YEAR)
	Actual ($ m) Year to date	$4.67 m	$1.20 m ✓	$2.55 m ✓	$3.76 m ✓	$5.16 m ✓
Lending (short and long term) to participating councils	Target ($ b)		$7.834 b (YTD as at Q1)	$7.932 b (YTD as at Q2)	$8.030 b (YTD as at Q3)	$8.128 b (FULL YEAR)
	Actual ($ b) Year to date	$7.736 b	$8.101 b ✓	$7.482 b ✗	$7.595 b ✗	$7.927 b ✗

D. Summary financial information (provisional and unaudited)

Financial Year ($m)	**YTD as at Q1**	**YTD as at Q2**	**YTD as at Q3**	**YTD as at Q4**
Comprehensive income	**30-Sep-17**	**31-Dec-17**	**31-Mar-18**	**30-June-18**
Interest income	88.68	178.15	259.14	342.83
Interest expense	83.95	168.53	244.82	323.86
Net interest revenue	**4.73**	**9.62**	**14.32**	**18.97**
Issuance and On-lending costs	0.49	1.09	1.63	2.21
Approved issuer levy	0.19	1.02	1.26	1.98
Operating expenses	0.71	1.47	2.13	2.94
Issuance and operating expenses	**1.39**	**3.58**	**5.02**	**7.13**
Net Profit	**3.34**	**6.04**	**9.30**	**11.83**

Financial position ($m)	**30-Sep-17**	**31-Dec-17**	**31-Mar-18**	**30-Jun-18**
Retained earnings + comprehensive income	30.83	33.52	33.52	39.32
Total assets (nominal)	8,338.71	7,721.93	7,979.38	8453.60
Total LG loans (nominal)	8,101.05	7,488.52	7,594.67	7927.44
Total LGFA bills (nominal)	350.00	370.00	545.00	475.00
Total LGFA bonds (nominal)	7,760.00	7,109.00	7,229.00	7719.00
Total borrower notes (nominal)	124.45	114.43	117.28	123.06
Total equity	55.83	58.52	63.18	64.322

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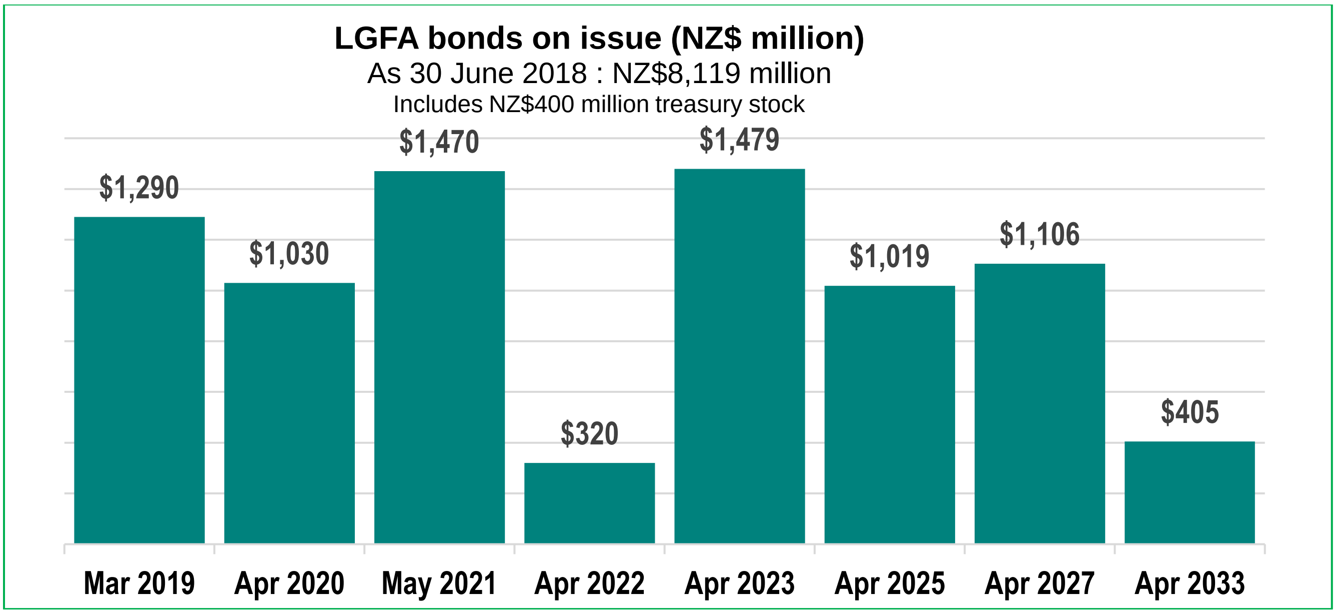


E. Quarterly compliance summary

Policy	Limit	Policy page ref	Continuous Compliance
One-month Liquidity Monitor	>120%	S1-1.1	Yes
Three Month Liquidity Monitor	>110%	S1-1.2	Yes
Twelve Month Liquidity Monitor	>110%	S1-1.3	Yes
Council Exposure (any 12-month period)	<10% of Balance Sheet	S1-1.5	Yes
Liquidity Buffer	>110%	S1-1.4	Yes
Partial Differential Hedge (PDH Interest Rate Gap Report	$40,000	S3-4.1	Yes
Value at Risk (VaR)	$250,000	S3-4.2	Yes
Council Maturity (any 12-month period)	$100m or 33% of LGFA borrowing	S1-1.6	Yes
Funding Largest Council Exposure	>100%	S1-1.7	Yes
Foreign Exchange Exposure	Nil	S7-3.1	Yes
NZDMO Facility Utilisation	Report monthly	S8-8.5	Yes
Counterparty Credit Limits	80% of Portfolio $125m Counterparty (category 3)	S4	Yes
Auckland Council Exposure (proportion of total Council exposure)	<40%	S1-1.8	Yes
Balance Sheet Maturity Mismatch	<15% of Balance Sheet	S2-2.1	Yes
Financial Covenants	Various (as set out on p13)	S9	Yes
Authorising Treasury transactions	Two approvers, one signature	S8-8.4	Yes

Details for compliance breaches over quarter.
There were no breaches over the quarter.

F. Performance against SOI objectives and performance targets

Primary objectives

1. Providing savings in annual interest costs for all Participating Local Authorities on a relative basis to other sources of financing

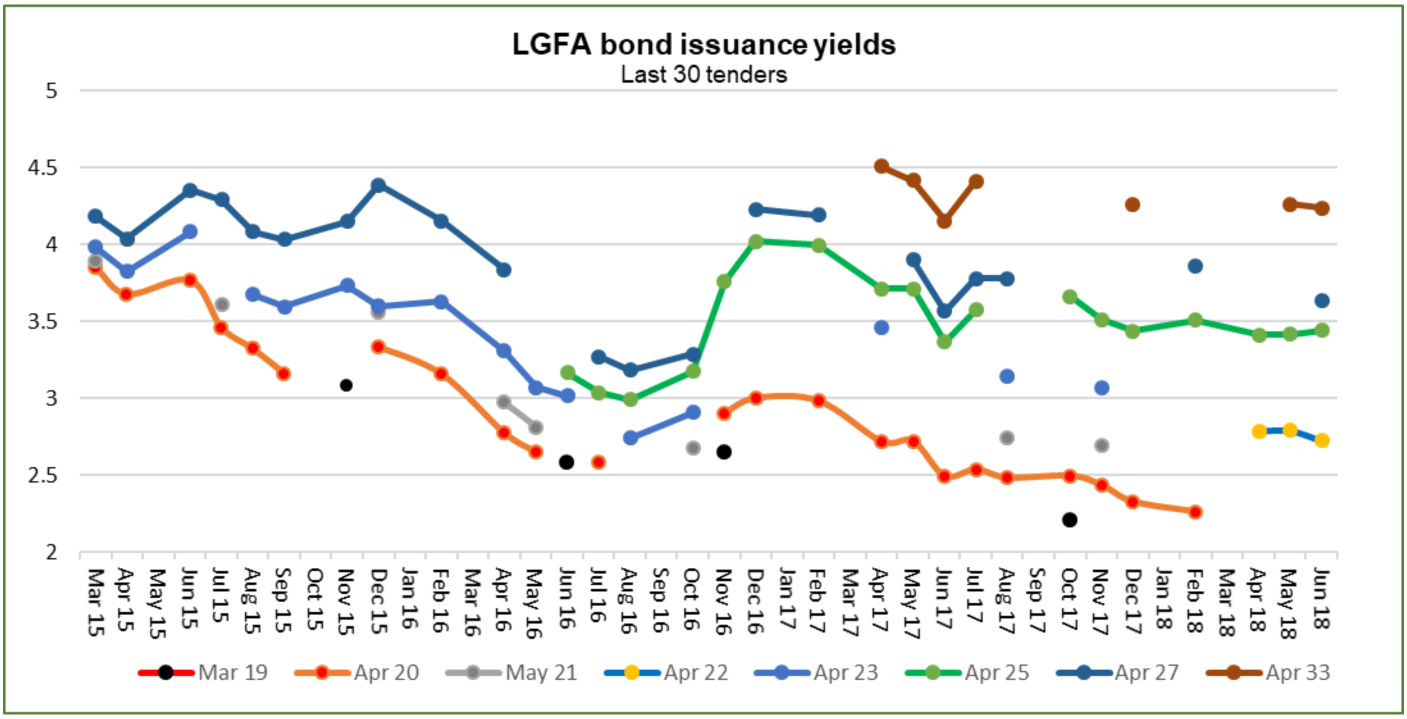
The LGFA on-lending base margins are 9 bps (terms out to 2019s), 10 bps (2020s to 2022s) and 11 bps (2023s and longer). Note that from June 2018 these margins have been simplified to an on-lending base margin of 10 bps for all maturity terms. Historically, the actual average base lending margin paid by council borrowers will depend upon the term of council borrowing but going forward it will now be a flat margin. The base margin charge covers our operating costs and provides for our capital to grow in line with the growth in our balance sheet to maintain a capital buffer.

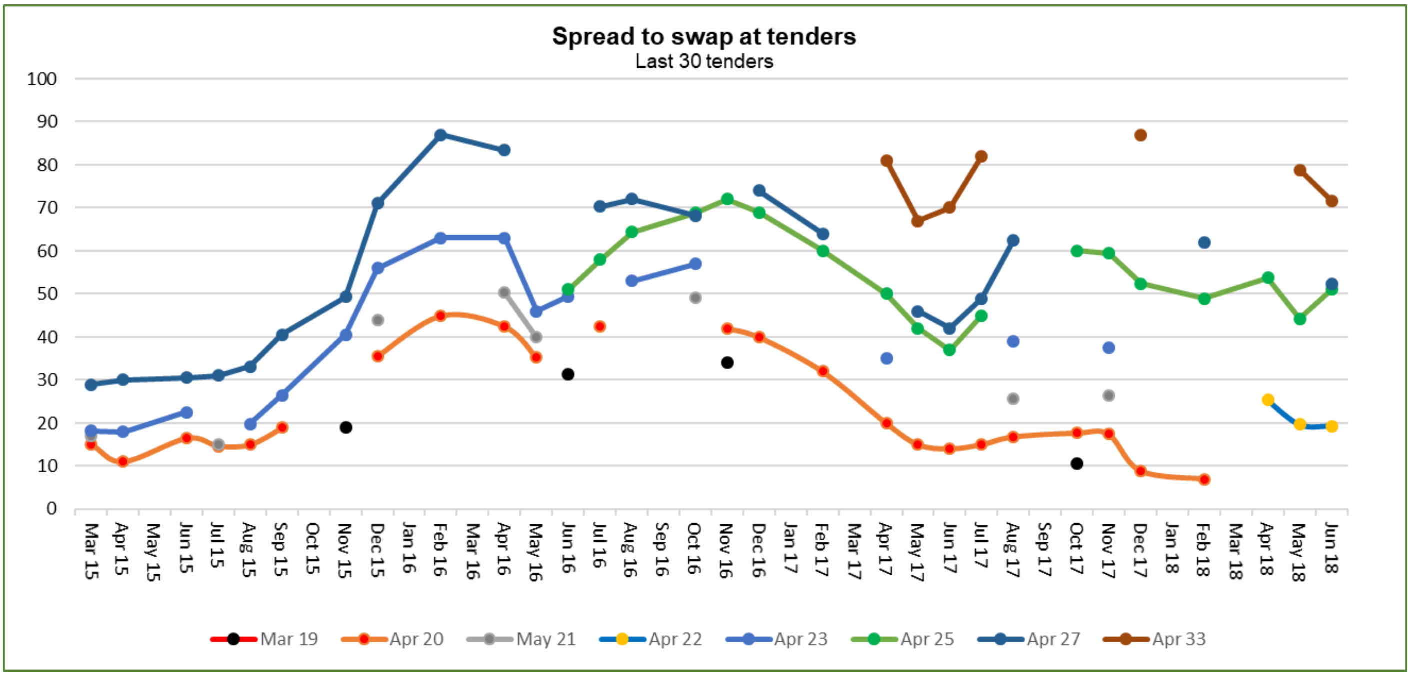
Our estimated annual savings to councils based upon the secondary market levels at 30 June 2018 of LGFA bonds compared to bonds issued by Auckland and Dunedin councils is between 10 bps and 21 bps depending upon the term of borrowing. The amount of savings has improved slightly over the past quarter as LGFA borrowing spreads have tightened slightly more than the tightening in Auckland and Dunedin borrowing margins but less so on an annual basis. Local Government sector issuance was strong during the quarter with Auckland Council issued $200 million of a June 2023 bond and Dunedin City Treasury issued $50 million of a July 2025 bond as well as LGFA issuance of $490 million.

30-Jun-18	**Savings to AA rated councils (bps)**				
	Auckland 2019	Dunedin 2020	Dunedin 2021	Auckland 2022	Auckland 2025
AA rated councils margin to swap	25	36	40	45	73
Less LGFA margin to swap	-4	-5	-11	-20	-53
LGFA Gross Funding Advantage	21	31	29	25	20
Less LGFA Base Margin	-10	-10	-10	-10	-10
Total Saving	11	21	19	15	10

Note that from 30 June 2017 we removed the implied "LGFA effect" of 10 bps of additional savings in borrowing costs from the above analysis. The LGFA effect was the assessment of immediate savings to councils when LGFA first commenced lending to councils in February 2012.

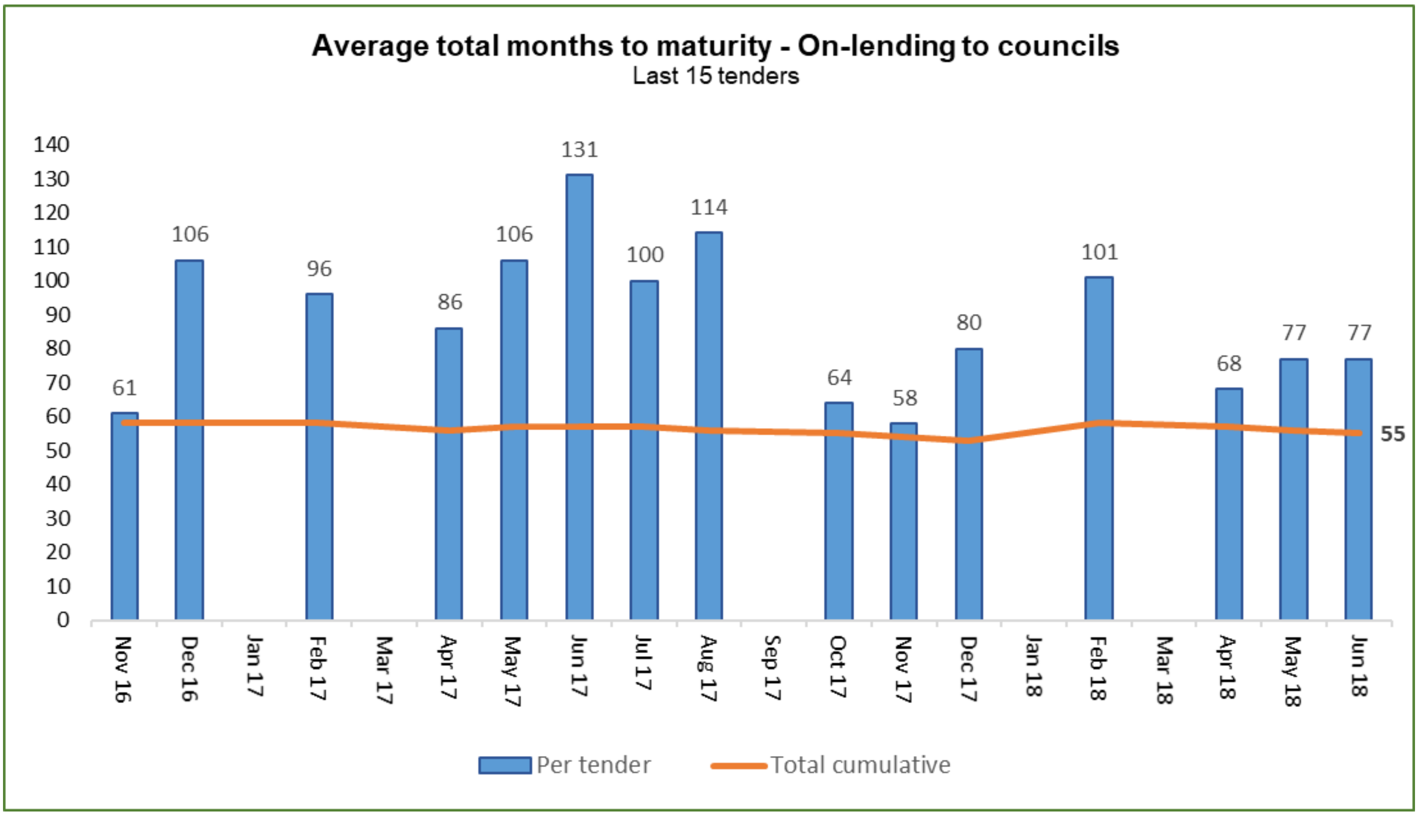
We held three tenders during the June quarter with total issuance of $490 million. This was the fifth highest quarterly issuance volume (out of twenty-six quarters) but the June quarter is seasonally the highest quarter for issuance. The annual issuance of $1.229 billion is in line with previous years issuance amounts ($1.285 billion in 2016/17 and $1.265 billion in 2015/16). Credit market sentiment was slightly more positive over the quarter with long dated spreads narrowing and yields declining as risk sentiment improved. After a record March quarter for Kauri bond issuance, there was no issuance in the June quarter as investor demand was muted and the SSA issuers could achieve their funding targets in other global markets. In general, secondary market credit spreads tightened to swap and NZGBs over the quarter. Over the past year spreads to swap and NZGB have tightened for maturities out to 2023 and widened for the longer dated LGFA maturities.





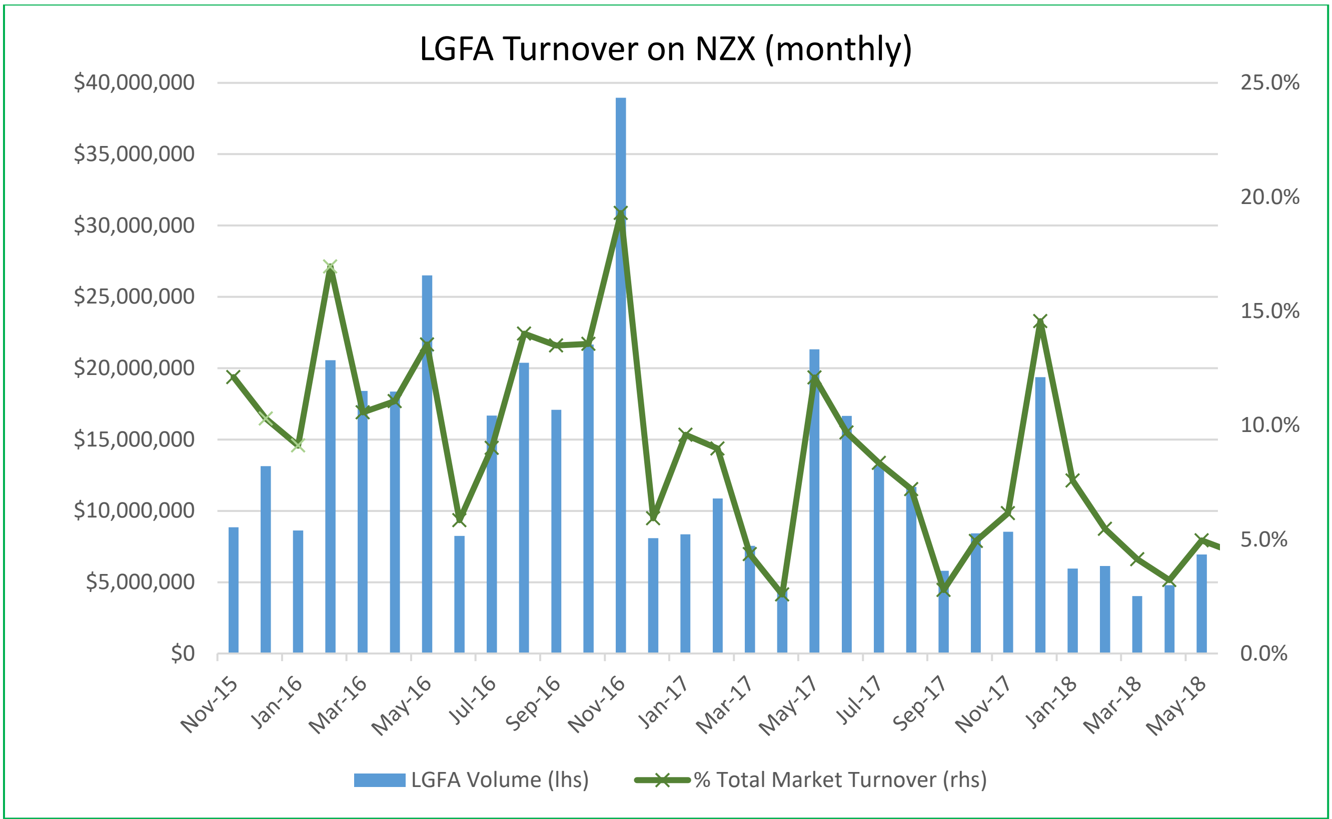
2. Making longer-term borrowings available to Participating Local Authorities

The average borrowing term (excluding short dated borrowing but including bespoke borrowing) for the June 2018 quarter by council members was 6.18 years and this was slightly shorter than the 6.9 years average term for the 2017/18 year and 8.1 years for the 2016/17 year. The shortening in borrowing term compared to the prior year was due to councils responding to the recent widening of borrowing margins in the longer dated maturities. Also, many councils had taken advantage of the tighter margins in early 2017, using the opportunity to extend longer when the 2033 maturities were first made available in April 2017.



3. Enhancing the certainty of access to debt markets for Participating Local Authorities, subject always to operating in accordance with sound business practice

The listing of LGFA bonds on the NZX Debt Market in November 2015 has led to greater investor awareness of LGFA bonds. Average turnover on the NZX Debt market since listing has been $13 million per month or 9.1% of the total turnover of the NZX Debt Market. Turnover has reduced over the past six months as retail investors are more attracted to high term deposit rates.



LGFA began issuing 3-month and 6-month LGFA Bills and commenced short dated (less than 1 year) lending to councils in late 2015. LGFA has short term loans to twenty councils of $244 million outstanding as at 30 June 2018.

LGFA documented an Australian Medium-Term Notes Programme in November 2017 to provide the ability to issue in currencies other than NZD. It is not our intention to use this programme but to have it established to provide some flexibility in case of the unlikely scenario of a significant market disrupting event in the future.

The three LGFA bond tenders during the quarter were well supported by the market with a healthy coverage ratio of between 2.5 times and 3.41 times and tight bidding ranges relative to secondary market levels at the time of each tender. We continue to offer three or four LGFA maturities at each tender and try to maintain the volume offered within the $130 million to $170 million range to ensure ongoing price tension and reduce the risk of a tender failure.

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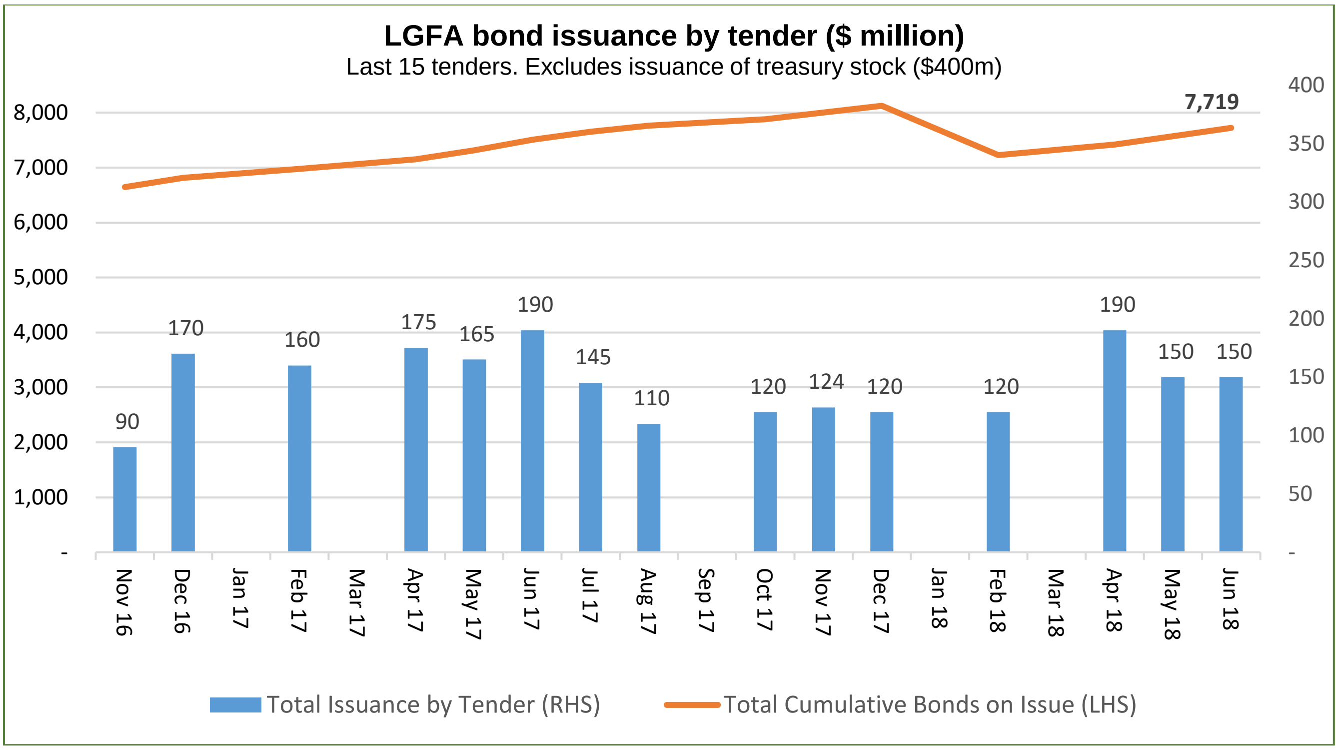
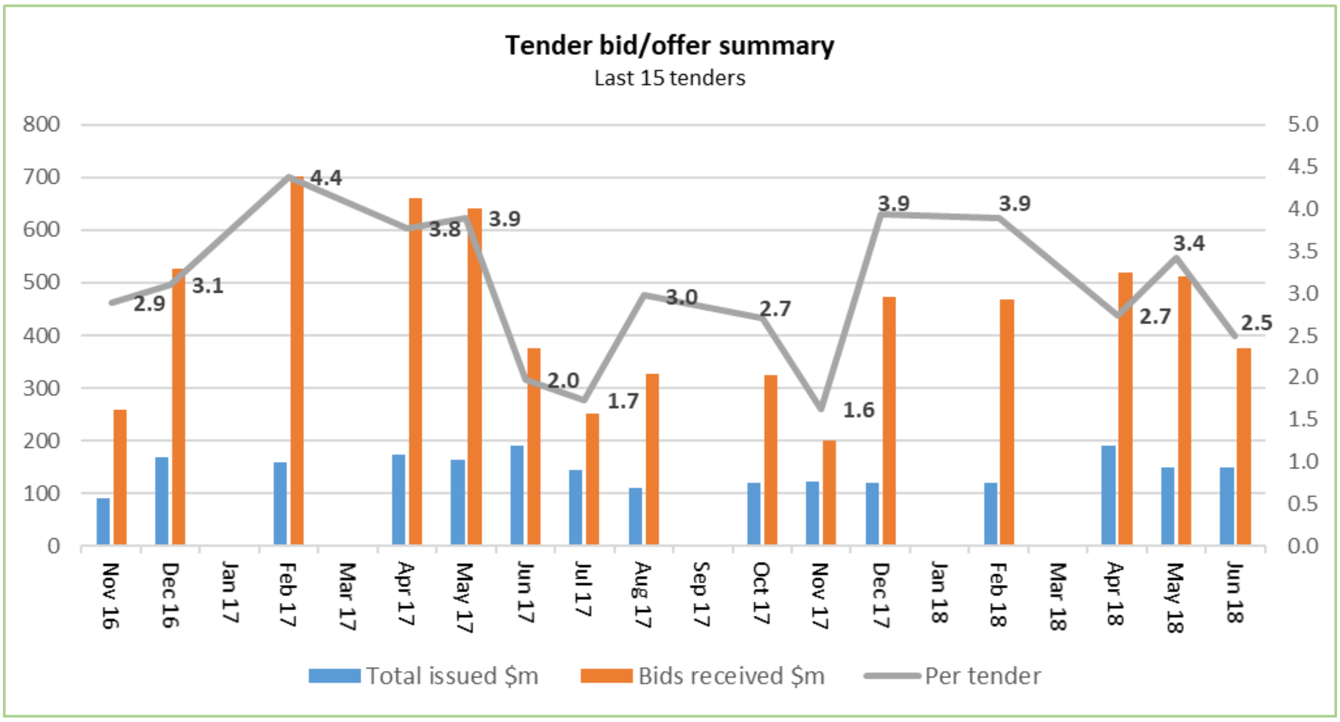




4. Offering more flexible lending terms to Participating Local Authorities

Bespoke lending continues to be a popular borrowing option for council members. During the quarter we lent $213 million on a bespoke basis to eighteen councils. This comprised 55% of total term lending by LGFA to its members during the quarter.

Short term borrowing by councils has been well received with loan terms to date of between 3 months and 12 months on $244 million of loans outstanding as at 30 June 2018. This is down from a peak of $360 million during the year as some councils have termed out their short-dated funding into longer tenors.

5. LGFA will monitor the quality of the asset book so that it remains of a high standard by ensuring it understands each Participating Local Authority's financial position and the general issues confronting the Local Government sector.

LGFA had meetings with twelve councils during the June quarter to discuss their financial performance and any developments with the underlying council operations. LGFA reviews council agendas and management reports on an ongoing basis for those councils on the LGFA borrower watch-list.

LGFA has commenced work on credit default assessment analysis of its member councils in preparation for adopting IFRS9 for accounting purposes.

LGFA management met representatives from Treasury, MBIE, S&P, OAG, Crown Infrastructure Partners, Infrastructure New Zealand, to discuss the local government sector and attended the Local Government and Central Government Forum.

LGFA presented at the LGNZ Quarterly media briefing on the sector financial position and provided an LGFA update. LGFA sponsored the SOLGM award for Transforming Service Delivery and attended three Risk and Audit Forums.

Additional objectives

6. Operate with a view to making a profit sufficient to pay a dividend in accordance with its stated Dividend Policy

LGFA’s Net Operating Gain on an unaudited management account basis of $11.834 million for the twelve-month period to 30 June 2018 exceeded the SOI forecast of $10.881 million by $953k. The average cost of funds for the 2017-18 financial year is 3.14%. This is lower than the 3.56% for the prior 2016-17 financial year due to the lower level of interest rates and much shorter term of LGFA bond issuance compared to the previous financial year. The LGFA Board has the sole discretion to set the dividend.

7. Provide at least 50% of aggregate long-term debt funding for Participating Local Authorities

LGFA estimates market share from the PwC Local Government Quarterly Debt Report and the most recent draft report is for the June 2018 quarter. LGFA market share of total sector borrowing for the June 2018 quarter was 61% and for the year to June 2018 was 70%. Our market share remains strong compared to our global peers but less than previous quarters (84%) due to both Auckland Council ($200 million) and Dunedin City Council ($50 million) borrowing in their own name during the quarter.

There are fifty-six participating local authority members of LGFA which is an increase of two over the quarter with Westland District Council and Stratford District Council both joining as non-guarantors. We are aware of at least another five councils who are working through the LTP process with an intention to join in the coming year.

8. Ensure its products and services are delivered at a cost that does not exceed the forecast for issuance and operating expenses

Expenses for the twelve-month period on an unaudited basis are $7.131 million which is $206k below budget. This variance is the consequence of:

- Issuance and on-lending costs (excluding AIL) at $2.207 million were $118k under budget. There were lower fees than budgeted relating to the NZDMO facility offset by higher registry costs and legal costs than forecast. The larger amount of short term lending and establishment of an AUD bond programme has increased legal costs.

- Operating costs at $2.948 million were $176k below budget due to lower personnel and travel costs than forecast but offset by additional legal costs relating to LGFA input regarding council borrowing into the Housing Infrastructure Fund.

- Approved Issuer Levy payments of $1.975 million were above our forecast of $1.887 million by $88k due to higher holdings of LGFA bonds by offshore investors.

9. Take appropriate steps to ensure compliance with the Health and Safety at Work Act 2015

LGFA has a Health and Safety staff committee and reporting on Health and Safety issues are made to the LGFA board on a regular basis by the Risk and Compliance Manager. There were no Health and Safety incidents during the quarter.

10. Maintain LGFA's credit rating equal to the New Zealand Government sovereign rating where both entities are rated by the same Rating Agency

LGFA has credit ratings from Standard and Poor's ("S&P") and Fitch Ratings ("Fitch") and meets with both agencies in September and October each year. Meetings were held in 2017 with both agencies and S&P

affirmed the long-term rating of LGFA at AA+ (stable outlook) on 25 September 2017 and Fitch affirmed the rating at AA+ (stable outlook) on 10 November 2017.

On 22 May 2018, S&P announced a new methodology for rating the ten entities who comprise their Public-Sector Funding Agency (PSFA) group. LGFA is a member of that group and our rating as at 30 June 2018 remained at AA+ under the old methodology but LGFA was placed on "Under Criteria Observation" (or "UCO") pending the outcome of the new methodology. [1]

11. Achieve the financial forecasts

As at the end of fourth quarter, Net Interest Income was estimated by management on an unaudited basis to be $747k above budget while expenses are $206k below budget. Net Operating Gain of $11.834 million was $953k above budget and 7.1% above the Net Operating Gain for the equivalent prior year.

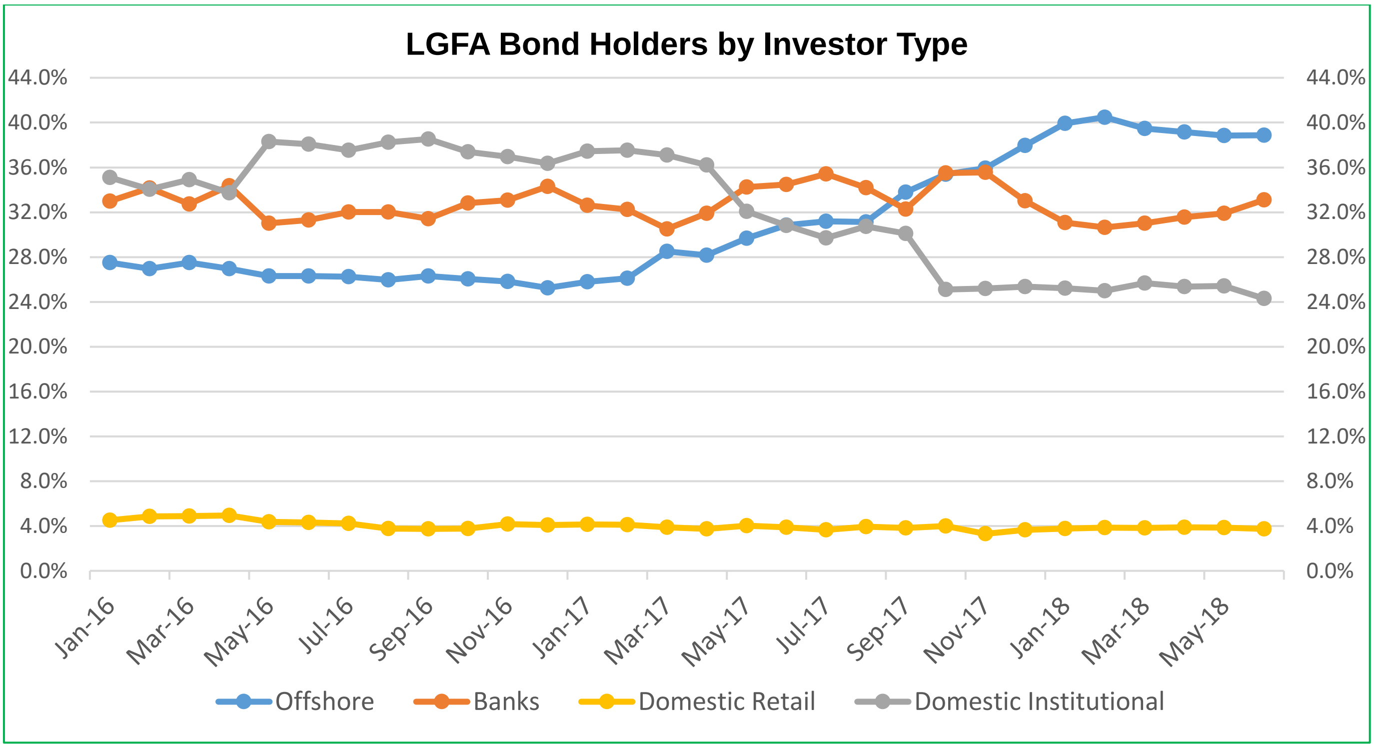
[1] Note that although outside the end of the June quarter 2018, S&P reaffirmed our AA+ credit rating under the new methodology and removed LGFA from UCO on 13th July 2018

G. Investor relations / outlook

Managing relations with our investor base is very important as the amount of LGFA bonds on issue has yet to peak and we require investors and banks to support our tender issuance. Our focus is on growing and diversifying the offshore investor group as these investors have the most growth potential given that we already receive strong support from the domestic banks and institutional investors.

All investor groups increased their holdings of LGFA bonds during the June quarter with banks the largest buyers of LGFA bonds.

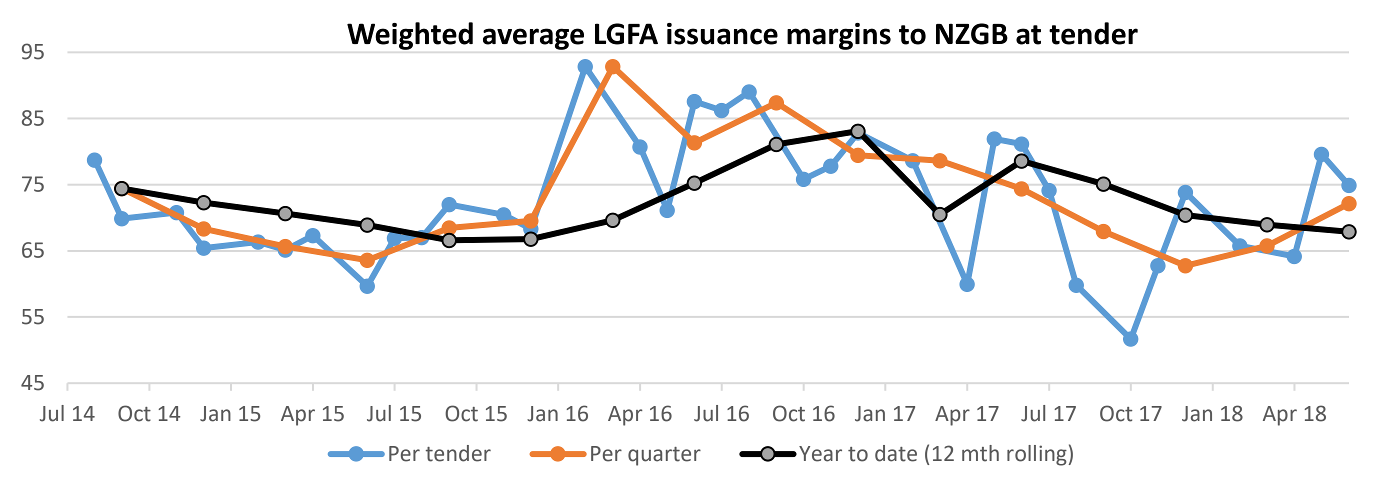
- Offshore investors increased their holdings by $146 million over the June quarter and by $700 million since June 2017. They are estimated to hold $3.002 billion (39% of outstandings) compared to $2.3 billion (30.9% of outstandings) a year ago. Offshore investor holdings are near a record high and they have become our largest investor group.
- Domestic institutional and retail investors increased their holdings by $31 million over the quarter and were estimated to hold $2.62 billion (27.9% of outstandings) compared to $2.6 billion (34.7% of outstandings) a year ago. The decline over the past year has been due to the maturing of December 2017 LGFA bonds held in money market funds and a small number of domestic investors have reduced their holdings as they are less optimistic on the credit market outlook.
- Domestic banks increased their holdings by a significant $311 million over the quarter but still hold $29 million fewer LGFA bonds than at June 2017. This reduction was due to the maturing December 2017 bond which was mainly held by banks in their liquidity portfolios and the increase in offshore investor holdings who buy from bank secondary market trading books. Bank holdings of $2.557 billion (33.1% of outstandings) compared to $2.586 billion (34.5% of outstandings) a year ago.

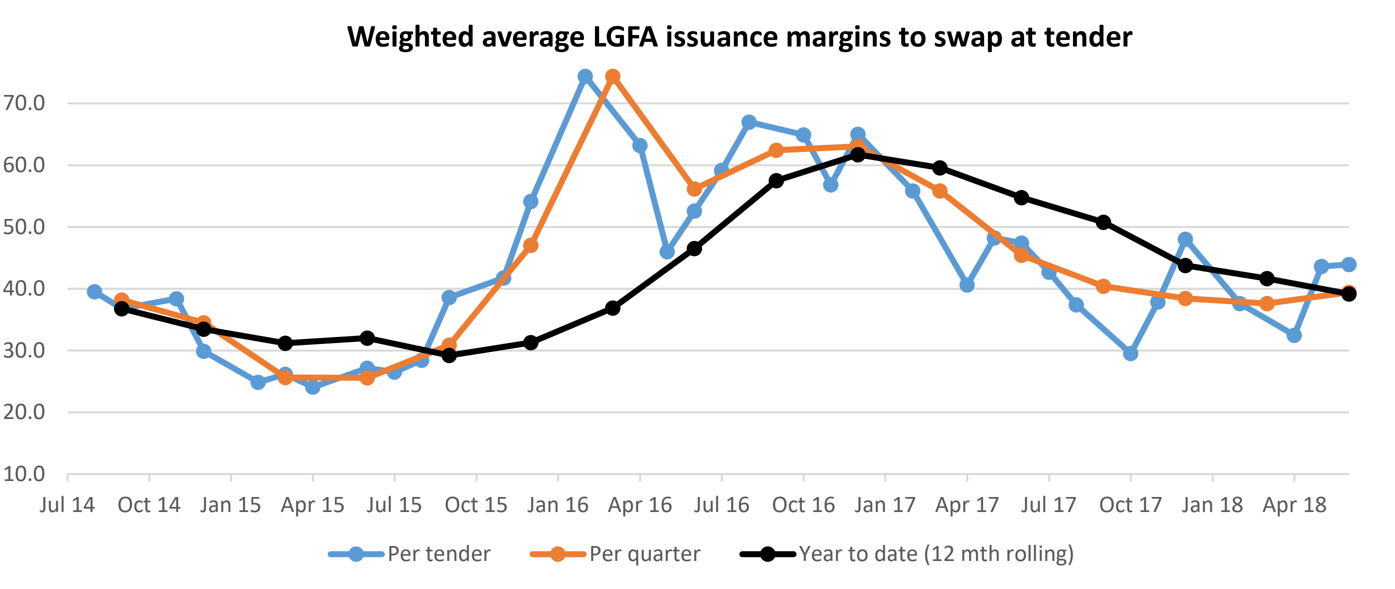


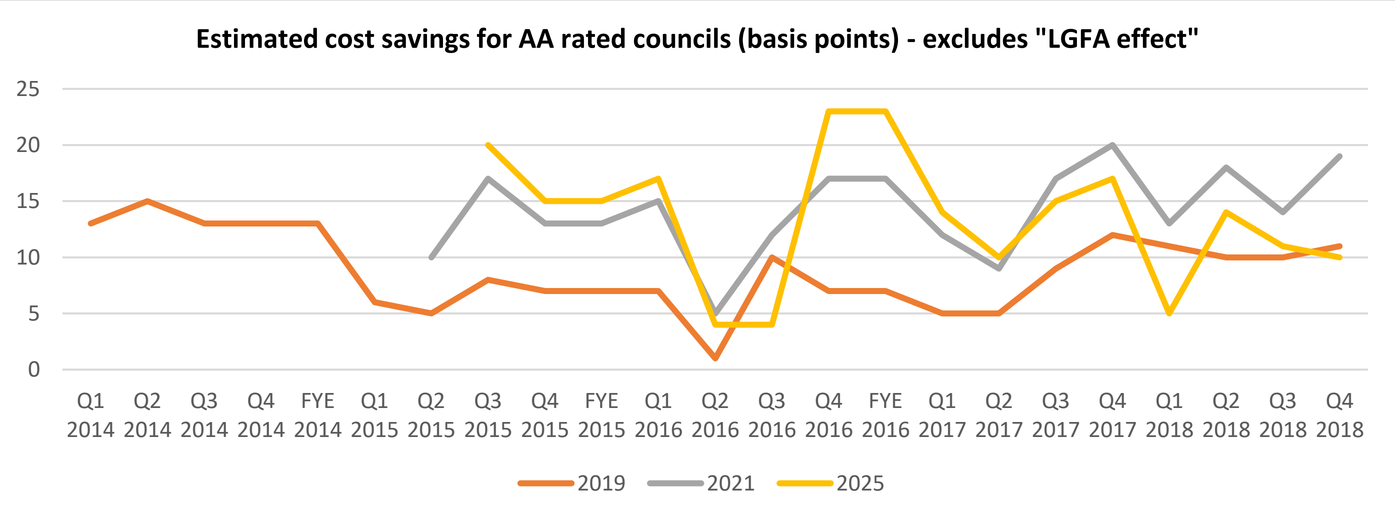
Quarterly Report

Quarter 4: 2017 - 2018
Period ended: 30 June 2018

H. Key trends







Note: Weighted average margins are a function of the term of issuance at each tender.