THE LOCAL AUTHORITIES' CAPITAL MARKET IN NEW ZEALAND

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by

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CONTENTS

Preface

This thesis affords an examination of the operation of the Capital Market in New Zealand as it affects local authorities. The intention of the study is to determine and analyse the factors affecting the supply of and demand for capital, to examine the problems at present faced by the authorities in their attempts to obtain capital finance, and to conjecture as to whether or not the Market is organised in such a way that best ensures an adequate flow of capital to this sector.

The chronic difficulties experienced by many local authorities in their attempts to obtain capital finance were among the factors which induced the New Zealand Government (in 1957) to set up a Royal Commission to investigate the whole field of local authority finance and the Report of that Commission (presented in September 1958) provides the basis for much of this Thesis. Other information has been obtained from a series of personal interviews which have been scheduled as 'Appendix A'.

INTRODUCTION

A capital market is that series of institutions and practices which stands between the holders of idle funds on the one hand and the potential borrowers of capital on the other. A capital market presupposes a supply of capital awaiting investment but the mere existence of a supply of investable capital is in itself insufficient as such capital must be made available to the borrower in an acceptable form and this is the function of the capital market. The effectiveness of the market, then depends upon the extent to which it stimulates savings, makes lending terms attractive, and provides a channel through which funds are placed in convenient form and upon acceptable terms at the disposal of borrowers. For the savers there must be satisfactory methods of setting aside savings as well as a sufficient inducement to save and lend.

Different classes of lenders require different types of investments. Some, e.g. many small savers are mainly concerned with security, while others may seek a maximum return and yet at the same time be prepared to carry a degree of risk. Yet others are prepared to tie up their money for a lengthy period of time in return for a steady stable income over that period. The converse applies to the borrowers; some may require capital for a short period only, a few days maybe only a few hours, or, like some local authorities, they may float a loan with a maturity period of forty years. The institutions of the market should be sufficiently varied and adaptable to meet all requirements. An inefficient market may induce borrowers to place an undue emphasis upon the use of bank credit.

But at the same time the market must be able to give mobility to capital e.g. a Southland farmer must be able to lend to an Auckland industrialist should the need arise. If all expansion could be financed by the ploughing back of profits there would be no need for a Capital market. At the same time the market acts as a buffer and by reducing the element of risk to the lender it tends to make borrowing cheaper.

The structure of the market can, in itself, influence the volume of finance available for investment e.g. the existence of a short term money market may mean that many funds which previously were forced to remain idle through lack of investment opportunity, are utilised. The institutions of the market, by bringing together the numerous small savings of individuals into an aggregate that is profitable to lend, provide a service to the smaller savers that would not otherwise exist.

Up until the present time the New Zealand Capital Market has been somewhat undeveloped but the commencement, over the past few years, of unit trusts, and a short term money market, together with the proposed Industrial Finance Corporation has helped to add a degree of sophistication which was hitherto absent.

It is usual to divide the borrowers of capital upon a capital market into three separate categories, i.e. the Central Government, local authorities, and private borrowers. Each of these separate sectors has its own distinguishing characteristics. The Central Government is to all intents and purposes a single borrower and, generally speaking, it obtains its finance from a few clearly defined sources. It is usually a long term borrower and it is in a position to offer the maximum security. The private sector is the most diverse in composition. It is made up of innumerable borrowers ranging from house property mortgagors to insurance companies all requiring finance for widely different reasons and offering vastly different securities. The local authority sector lies somewhere between the two but in most respects tends to gravitate towards the Government Sector rather than the private. It is nevertheless possessed of several individual characteristics which clearly demarcate it from the Government Sector.

The Structure of Local Government in New Zealand

The structure of local government in New Zealand has long been a topic of considerable controversy and the diverse nature and form of the various authorities has exerted a considerable influence upon their activities on the market. Some authorities are able to obtain finance more readily than others; some need more finance than others; some are able to obtain finance more readily from one particular source than others; some lenders prefer one class of authority to another while not all authorities can offer the same degree of security.

The local authority structure at present existing in New Zealand has derived from colonial days when difficulties of transport necessitated the establishment of numerous semi-autonomous pockets of population which eventually tended to build up their own systems of government. As time passed vested interests became established in the existing order and the difficulty has been to break down this status quo. A good example of this is the number of small municipalities in the Otago and West Coast Provinces of the South Island which, although still retaining borough status, are carrying well below the minimum population required by Statute (The Municipal Corporations Act 1954) for a borough. A further example is the large number of small harbour boards which have been able to remain in existence despite greatly improved rail and road transport systems which would make the use of fewer ports more economic. The number of counties existing in New Zealand is possibly three times greater than it should be. This situation was aggravated by the incompetent arrangements which operated for the granting of Government finance to counties under the 1876 Counties Act. At the same time, however, it should be noted that in recent years considerable success, has been gained in the amalgamation of counties and their numbers are steadily decreasing.

From time to time various districts have taken it upon themselves to provide their district with a major asset and this has frequently induced the establishment of a single authority designed specifically to manage that asset. The two most notable of these are the Auckland Harbour Bridge Authority and the Christchurch Lyttelton Road Tunnel Authority.

Differing growth rates and structures and the consequent difference arising in rating demand has also been a big factor in inhibiting the amalgamation of many municipalities and this tendency is especially noticeable in the Auckland Urban Area where some twenty boroughs have defied attempts at amalgamation. Situations sometime arise where a completely built up town with a stationary or even declining population exists either entirely within or adjacent to the boundaries of a much larger and more rapidly growing city, two very good examples being Petone Borough adjacent to Lower Hutt City and Riccarton Borough situated within Christchurch City. In such a case the rating level of the smaller town will tend to be relatively low because being built up it has little to complete in the way of capital works whereas the larger town may tend to have a much higher rating level because of development requirements. This means that the ratepayers in the smaller town will generally oppose any attempt at amalgamation with the larger as it would simply mean, at least for them, increased rates with no additional benefit.

A further interesting feature of the contemporary New Zealand scene is the presence of a large number of what are commonly termed 'ad-hoc' authorities i.e. local authorities established to carry out some set purpose e.g. drainage in cities (urban drainage boards) or the eradication of rabbits (rabbit boards). These forces which have succeeded in maintaining the large number of authorities have also had the effect of making the demand for capital from the local authority sector of the market greater than what it would otherwise be. They have also had the effect of inhibiting the efficient use of capital as there can be no doubt that one large authority can use finance more efficiently than a large number of small ones. Not only can a large authority operate more effectively upon the market but it can generally put the capital which it does obtain to a more effective use.

The Control of Borrowing

An important characteristic of the market at present is the large degree of control and especially Central Government control which is exerted over the borrowing activities of the local authorities.

This control operates from several different angles. Firstly there is the Local Authorities Loans Board which was established in 1926 under the provisions of the Local Government Loans Board Act of that year. All local authorities are required to obtain the approval of this institution before going on to the market. The Loans Board exercises both long term and short term control over the borrowing activities of the authorities in that as well as having the power to refuse to sanction a loan proposal it is endowed with the power to permit or refuse the use of underwriting or procuration fees and, by the manipulation of the issue of orders in council, to control the amount of the sanction going onto the market. The rate of interest is also a very potent factor and, in accordance with the provisions of section 9(3) of the Local Authorities Loans Act 1956, the Minister of Finance has the power to set the maximum rate of interest which may be paid by local authorities on money borrowed. At the same time the Loans Board can set differential rates of interest lower than the maximum rate set by the Minister. Of course any authority could, if it could find a lender borrow free of interest or at a rate lower than that normally prescribed by the Loans Board. The power to adjust the rate of interest upon local authority stock provides the Central Government with what amounts to virtually absolute power over the market activities of the authorities because it could, if it so desired, adjust the rate of interest upon local authority stock to a figure lower than the ruling Government rate and so exclude the authorities completely from the market. The Government, has however, never adopted such a course of action.

A further method of control exercised by the Loans Board over local authority borrowing is the limitation of the issue of orders in council. This practice is usually carried out only in respect to loans of fairly large amount. Thus approval may be given by the Board to the borrowing of an amount of say, £200,000 with the stipulation that only £40,000 be raised initially. Hence a further order in council would be required before the authority could raise any further amount. On the other hand the Board could stipulate that the loan be raised over a period of say five years and that not more than £40,000 be raised in any one year. This procedure would prevent an authority from going on to the market and raising the full amount of the loan in one lump sum. But the procedure is, to some extent governed by the nature of the subject matter of the loan e.g. if the amount of £200,000 was required to purchase a building the full amount of the loan may have to be raised in one amount to meet settlement. But generally speaking most construction projects and especially road works can be spread over lengthy periods of time with payments falling due at set or irregular intervals. In such cases orders in council could be issued as the work required. This practice of limiting the issue of orders in council is of some value in times when there is considerable pressure upon the market because it has the effect of levelling out demand and preventing cycles created by the presence of one or two very large issues upon the market at the same time.

To some extent control over the market is exercised by the authorities themselves especially in the financing of projects of marginal essentiality. If the authority can see that it will experience difficulty in obtaining finance for a particular project it may well lay off the construction of that project until the market eases. As an ultimate backstop the very non-availability of finance itself will frequently act as a measure of control.

A further interesting factor which operates to control market activity is the ability of an authority to spend money over any given period. The smaller authorities in particular seem to have a fairly tight spending limit and the availability of large amounts at their disposal appears to tax their resources somewhat. In conjunction with this we could mention the point that if there is strong competition for the services of builders and other contractors from the private sector the authorities frequently experience difficulty in finding someone to do their work for them and this fact could in turn limit their capital requirements.

The Local Authorities Loans Act 1956 grants to the ratepayers the power to object and require that a poll be taken upon a proposal to borrow. As a method of control this practice has some clear disadvantages. On the one hand there is a tendency for expensive although essential projects to be rejected by the ratepayers while non-essential 'glamour projects' with widespread public appeal may be permitted to go ahead without objection. Petty politics also play a part in loan polls and the ratepayers will frequently use a loan poll to vent spleen upon an unpopular council or board irrespective of the merits of the project involved. It can be seen therefore that even at its best this method of control is ineffective and erratic.

Hence it could be said that control is both long term and short term. It can operate to prohibit initial entry on to the market, and at the same time to control the amount of demand making itself felt upon the market.

The question now arises as to the factors which have made this control necessary. These fall broadly into two categories. On the one hand there are forces inherent in the structure of local government itself, some of which have already been mentioned, while on the other hand there are factors present in the market which have made control necessary. As far as the authorities are concerned control is necessary to prevent reckless spending and to protect the ratepayers (who are ultimately called upon to foot the bill for all loan proposals) from being over committed. The authorities differ markedly in size but from a legal point of view no distinction is made between the largest and the smallest. The Municipal Corporations Act 1954, accords the Arrowtown Borough with exactly the same borrowing powers as the Auckland City but the servicing of a loan of an amount of £100,000, although likely to cause no great difficulty to the Auckland City would provide the Arrowtown Borough with serious problems. Control is therefore required to prevent the smaller authorities from over stepping themselves. But a larger authority could equally well overstep itself with reckless borrowing if it was already committed up to the hilt with the servicing of debt. If a particular authority is already spending a very large portion of its annual income upon the servicing of loan charges the borrowing of an additional £10,000 could well prove embarrassing especially if the rating level of that authority is either on or close to the maximum permitted by statute.

A further matter necessitating control is the trend of rateable values occurring in a particular locality. Some counties and boroughs (e.g. those on the West Coast and some of the Otago boroughs) are losing population fairly rapidly and in such circumstances it is reasonably certain that unless other factors intervene to compensate rateable values will decline. In such circumstances therefore, an authority could well find that, although it is rating at the legal maximum it still has insufficient income to meet its annual commitments. The Borough of Kaitangata in South Otago is in this position at the present time and some of the difficulties which this situation has created in the past are considered in the next section. Population drops generally have less effect in counties because land values in rural areas reflect agricultural productivity rather than residential demand.

A further matter which makes control desirable is that many of the smaller authorities are unable to employ staff who are competent enough to raise loans in an efficient manner. Loan raising is only one of the many tasks which the clerk of a local authority is called upon to perform and the clerk of a very small authority who is required to raise a loan once, in say every five years may obtain very little practise in the art of judging the market. The larger authorities generally find it worth their while to employ staff who specialise in this class of work and indeed many of them become highly efficient.

Consideration will now be given to a more detailed description of the two major elements of control i.e. the Local Authorities Loans Board and the rate of interest.

The Local Authorities Loans Board

A brief history of the Loans Board ind cates the intention behind the establishment of the Board and helps to show what conditions are likely to prevail if the Board did not exist.

The first restriction at all upon local authority borrowing appears to have been made by the Appropriation Act 1915 (sec 26) which required all local authorities to obtain the approval of the' Governor General in Council before going on to the market. This was purely a war time measure and indeed the section provided that it was to remain in force only so long as the War with Germany continued. The intention behind the measure seems to have been the control of interest rates so that the Government would have a free run upon the market to raise funds for its War effort. Prior to 1915 there appears to have been no restriction at all upon local authority borrowing.

In the boom years immediately following the War there was a considerable upsurge in borrowing activity and by 1926 the net debt of the local authority sector amounted to £54 m. with an amount of £6 m. raised in 1925. But it was obvious that much irresponsible borrowing had taken place in those years. (refer e.g. to Hansard Vo.209 1926 page 115 Second Reading Debate on Local Government Loans Board Bill.) The main source of trouble was apparently the raising of finance for works which were quite unnecessary and the borrowing of money upon terms which considerably outlived the lives of the assets which were the subject matter of the loan. By 1925 it was obvious that if the existing rate of borrowing continued the authorities would soon be unable to raise their demands without substantial increases in interest rates. Thus in 1926 the first overall instrument of control was introduced with the establishment of the Local Government Loans Board under legislation bearing the same name. The Parliamentary debates on this Bill (refer to Hansard Vo.209 1926, page 1155) indicate that there was no real opposition to the principle of control of local authority borrowing although some members questioned the form that the control should take and the composition of the proposed board.

Just how potent as an instrument of control the early loans Board was is somewhat difficult to ascertain but it certainly did not succeed in preventing several local authorities from getting into serious difficulties in the Depression Years of the early 1930s. A typical example is provided by the Thames Borough which in 1932 was forced to hand over the control of its affairs to the Central Government. The preamble to the Thames Borough Commissioner Act 1932 (23 Geo. 1932 Local No.1) summarised the situation in a terse but coldly accurate manner, viz:

> "Whereas the Thames Borough Council has from time to time raised certain special loans under the Local Bodies' Loans Act, 1926, or former acts by the issue of debentures or other securities secured upon the rateable property in the borough; And whereas as a result of the decrease in mining operations in the borough and the general trade and economic depression at present affecting New Zealand, the said Council has found it impossible to collect its rates in full and consequently is not at present and is not likely in the near future to be able to pay in full as they fall due the annual or other charges in respect of such loans; And whereas it has been agreed by the Council and a majority in value of the debenture holders that it is desirable that provision should be made for the temporary administration of the borough by a commissioner as hereinafter provided."

A similar situation prevailed in the Matakaoa County (refer to section 10 of the Local Legislation Act 1932). That County had apparently borrowed upon overdraft in excess of the limits permitted by the Local Bodies Finance Act of 1921-22. The Buller County also experienced financial problems largely through the necessity of having to service difficult terrain but did not require the institution of a controlling commissioner. Some general relief was afforded by the Local Authorities Interest Reduction and Loans Conversion Act of 1932.

Table No. A...1

LOANS BOARD APPLICATIONS AND SANCTIONS

Year	Total new applications	Sanctioned
1927-28	4,636,649	4,260,981
1928-29	6,007,045	4,675,772
1929-30	4,218,730	4,531,717
1930-31	3,840,505	2,605,157
1931-32	3,412,365	3,265,005
1932-33	2,951,645	2,754,752
1933-34	3,884,132	3,661,805
1934-35	3,859,363	3,965,395
1935-36	4,061,076	3,602,480
1936-37	2,804,308	2,841,671
1937-38	3,362,173	3,221,203
1938-39	5,138,917	4,201,397
1939-40	2,674,450	2,057,260
1940-41	5,336,640	4,312,175
1941-42	2,576,050	3,289,824
1942-43	2,780,270	2,618,120
1943-44	3,797,790	3,709,090
1944-45	3,242,327	2,435,927
1945-46	3,497,820	2,887,170
1946-47	9,843,543	8,295,866

Table No. A...1 (continued)

Year	Total new applications	Sanctioned
1947-48	8,724,579	7,481,914
1948-49	8,934,705	8,519,466
1949-50	8,062,758	7,364,177
1950-51	10,825,192	9,728,488
1951-52	15,092,761	14,920,543
1952-53	29,129,996	18,049,890
1953-54	24,908,485	24,282,014
1954-55	28,586,666	26,267,926
1955-56	22,503,906	15,899,655
1956-57	20,951,326	17,262,790
1957-58	31,933,906	26,649,656
1958-59	21,510,318	21,079,746
1959-60	32,847,560	29,209,597
1960-61	37,685,555	35,123,005
1961-62	30,341,386	25,843,340
1962-63	31,351,914	29,331,564

(Annual Reports of the Local Authorities Loans Board)

This situation underlined the necessity for control and indeed the existence of the Loans Board has never been seriously questioned since its institution.

The present provisions are to be found in the Local Authorities Loans Act 1956 which provides for a Board of seven members i.e. the Secretary to the Treasury, the Commissioner of Works and five other members to be appointed by the Governor General in Council. The three operative sections of the Act are 3, 8 and 9. Section 3 provides that no local authority shall borrow except with the prior approval of the Governor General in Council. Section 8 provides for the submission of all loan proposals to the Board while section 9 sets out the manner in which the Board may deal with a loan proposal.

In determining the effect which the Loans Board has had upon the operation of the market we can submit the following points. Table No. A...1 which sets out the amounts applied for (i.e. the new applications each year) against the amount sanctioned shows that theBoard has never made any really drastic reductions, as the amount sanctioned always represents a considerable proportion of the amount applied for. It will be noted that in a few instances the amount sanctioned is actually greater than the total of new applications for that year and this must mean that some amounts referred back or deferred from previous years were later sanctioned. Even in the depression years of the early thirties, or the years of extreme market stringency (1956-57) the Board apparently made little attempt to cut back applications in anything like a drastic manner. This seemingly passive policy is attributable mainly to two factors. Firstly there is a strong tendency for the Board to be subject to political pressure and this applies especially in the case of applications from the larger urban areas which are able to marshal a number of members of Parliament to their support if an application is declined. Secondly it is clear that the Board would reject an application that was obviously unnecessary or beyond the financial capacity of the particular authority and this has possibly given rise to a certain amount of caution in the submission of applications to the Board. An application that was certain to be rejected would not be submitted in the first instance. The Board has introduced a comprehensive system of technical investigation of proposals and a large percentage of rejections are upon technical rather than financial grounds.

The restriction of the issue of Orders in Council is in reality Government, rather than Loans Board control but as it operates in complement with the Board's control this is the most appropriate place to deal with it. This process is carried out in accordance with the Act (i.e. section 3) which provides that as well as the approval of the Loans Board the approval of the Governor General in Council is required before an authority can borrow upon the market. This, in effect, amounts to the control of the flow of a particular sanction on to the market and as such of course is only of relevance in the case of fairly large applications. As previously stated the practice cannot be used in those cases where the loan amount must all be paid out in one lump sum. The policy which has been adopted in those cases where the amount of the loan is required over a period of time has been to restrict the amount of each Order in Council to the amount immediately required or perhaps to the amount required in any one year. It is possible that the Board itself would adopt a policy of this nature and in some instances it has sanctioned proposals with the stipulation that only certain amounts be raised at any one time or in any one year. It is of note that in the case of hospital development, which is usually carried out over a substantial period of time, the Board has adopted a policy of limiting Orders in Council to the amount necessary to carry out two years' work. It is rather difficult to see that this practice can have any really substantial long term effect upon the demand for capital. At best it offers a slight palliative and the most immediate result is to prevent the whole loan from going on to the market at the one time.

As far as necessity is concerned the Loans Board has adopted a very liberal approach and indeed very few proposals are declined on the ground of lack of necessity. The 1963 Annual Report of the Loans Board contained the following remarks upon this question;

> "The majority of applications for new works submitted to the Board are for works which are essential for the health of the community or for the provision of services necessary for the economic development of a region. Applications which can be deferred or declined on the ground of lack of necessity are few and mainly comprise items relating to amenities and

recreational facilities. However, the development of these items has come to be regarded as a highly desirable function of local government, the effectiveness of which would be lessened if local authority activities were confined solely to work relating to health and purely economic development."

There is evidence that in the past, at least, the Loans Board has not made any concerted attempt at programming loan proposals in order of priority with the object of rationing out available finance more satisfactorily among various projects. Such a task would mean that the Board would require about three years advance knowledge of all proposals but at the present time liaison between the Board and the individual authorities is by no means systematized. There are however indications that the Board is contemplating introducing such a system and the 1963 Annual Report of the Board contained the following statement.

"The Board considers that to overcome the financial problem involved with both annual and development loans, some method of determining priorities for new works might become necessary in the next few years. It has therefore asked the major local authority organisations to examine the position with a view to obtaining a mutually satisfactory approach to the problem."

On occasions directives have been given to the Board by the Minister of Finance but evidence of direct Governmental, as distinct from political, interference with the Board is scant. Legislation passed in 1955 provided that the Board could in the exercise of its powers have regard to the interests of the national economy. The Board interpreted this legislation as imposing upon it a statutory obligation to examine priority in relation to the overall demand upon resources. Early in 1958 the Minister of Finance requested the Board to review proposals more selectively in the light of the Country's economic and financial position. According to the 1958 Annual Report of the Board this directive was implemented accordingly. However, an examination of Table A...1 reveals that sanctions in relation to applications for the year ended 31 March 1959 did not show any dramatic reduction. This appears to indicate the extreme difficulty which the Board has in declining projects which it considers at all necessary.

In January 1961 a similar directive was given to the Board and the following comment appears in the Annual Report for the year ended 31 March 1961.

> "In January 1961 the Minister of Finance asked the Board in view of the current heavy demands on available resources and the marked decline in overseas exchange reserves, to exercise its powers even more selectively. The Board has discussed ways and means of implementation without causing undue difficulties in prosecution of essential works. Most of the proposals coming before it are however, correctly regarded as being in this category. The Board considers that a closer approach to the desired objective could be achieved by local authorities themselves reviewing their programmes of

uncommitted capital expenditure and slowing expenditure by deferring the calling of tenders or reducing the scale of operations so that the programmes are spread over a longer period. The Board is endeavouring to sanction only loans for works more urgently necessary for community development. Even with that it seems the savings may not suffice to meet the demand."

In conclusion therefore, we may state that the influence of the Loans Board upon the market has been largely passive; prohibitory rather than stimulative. Its position may be likened to that of a full back in a football game in that if he plays strictly in position he can only play the ball that comes to him. The Loans Board has acted almost entirely as an instrument of control rather than direction. It has made some attempt to keep demand off the market and to ration out the available resources but it has made no effort to draw up clearly defined categories of priorities. Little conscious policy can be derived from an examination of the proposals rejected and rejections appear to have been made at random rather than in accordance with any predetermined plan. There can, however, be no doubt that the Board has had a beneficial influence in keeping the margin of completely irresponsible borrowers off the market and indeed, as stated, the very existence of the Board has probably deterred this class of borrower from appearing.

It is clear then that the Board does not look upon itself as having a central role to play in controlling the overall level of local authority capital expenditure. Its present composition indeed would be inappropriate for such a function. However, the Government's new emphasis upon the long term planning of expenditure of both Central and Local Government (refer to 1966 Economic Review page 22) to achieve a more even rate of growth will necessitate the long term programming of capital expenditure. This will possibly mean a re-organisation of the Board and more control of the factors that at present inhibit close Central Government control over local capital expenditure, i.e. the time lag between sanction and the commencement of the work, unused sanctions, and the large volume of unused loan moneys held by the National Provident Investment Pool.

The Rate of Interest

It should be said at the outset that the rate of interest does not play as potent a role in the field of local investment as it does in some other sectors of the capital market but its influence can by no means be ignored.

The rate of interest payable upon local authority stock and debentures is not free; it is set by the Minister of Finance. At the outset therefore we must endeavour to determine the policy (if such exists) behind the establishment of the rate of interest. Over the years the rate of interest payable has fluctuated considerably.
Table No. A...2 sets out the maximum rates payable over the years

since the establishment of the Loans Board in 1927. From an investors point of view, broadly speaking, local authority stock fall into the same category as Government stock as both are what is generally termed 'gilt edged' investments. Both can offer virtually the maximum in security backing as one has the financial backing of the state while the other has the rating potential of the particular local authority. Both are trustee investments in accordance with the provisions of section 4 of the Trustee Act 1956. The type of investor, then, who is attracted to local authority stock is similar to that attracted to Government Stock. Now the Government, in the interests of the national economy and the taxpayer, when borrowing endeavours to do so as cheaply as possible. Thus it has been necessary for the local authority interest rate to be set with reference to that rate of interest currently payable upon Government Stock. If the two rates happened to reach parity the local authorities would probably obtain no finance at all because of the superior security backing of the Goverr ment Stock. While on the other hand if the local authority rate was permitted to rise to any great extent above the Government rate the very slight security superiority of the Government Stock would be obliterated and the Government would find it difficult to obtain finance. The policy therefore, has been to maintain a balance between local authority and Government interest rates and this has generally necessitated setting the local authority rate at about 1/8 to 1/4% above that ruling on Government Stock. The following is a sample set of local authority interest rates showing in comparison the

Government rates at the same time;

Local Authority Rate

Year	Term	Rate
1956	5 years	4-3/8%
	8 "	$4\frac{3}{4}$%
	12 "	4-7/8%
1957	5 years	$4\frac{3}{4}$%
	6 "	5%

Government Rate

Year	Term	Rate
1956	3 years	4-3/8%
	5 "	$4\frac{1}{2}$%
	11 "	4-5/8%
1957	3 years	$4\frac{1}{2}$%
	6 "	$4\frac{3}{4}$%

(1958 Annual Report of the Local Authorities Loans Board.)

Referring again to Table No. A...2 we see that the rate of interest has fluctuated considerably over the years. The maximum rate being 6% in 1927 and the minimum rate being $3\frac{1}{4}$% in the years immediately following the Second World War. The policy therefore appears to have been to adjust the rates immediately any minor slackening or tightening of the market makes itself apparent. The excessively high rates of the depression years are clearly shown while the low rates payable after the War are accounted for by the fact the local authority activity was at a very low ebb in those years and there was therefore a very low demand for capital. In some instances as many as three adjustments to the rate of interest have taken place in the one year e.g. in the Year ended 31 March 1962. On 8 May 1961 the rate was adjusted to 5% while on 20 July 1961 the rate went to 5-1/8% and on 23 February 1962 yet a further increase took place to 5-3/8%. It would seem therefore that looked at from one point of view the rate of interest has been turned by the Government into a passive co-efficient which is automatically adjusted in accordance with the flow of capital into the sector. It has been kept at the lowest possible level that will ensure at least a minimum flow of finance into this sector. There does not appear to have been any time at which the rate was permitted to rise to such an extent that investment was directed into this sector at the expense of the private or Government sector. Thus there is no question of a rate of interest that is free to adjust itself in accordance with market forces as it is artificially adjusted to that figure which will ensure a minimum flow of capital to this sector but at the same time will not hamper the operations of the Government upon the capital market.

What influence has the rate of interest in inducing investors to put money into this sector of the capital market? In answering this question we must have regard to the nature of the investor who is

Table No. A...2

Maximum Interest Rate for Local Authority Loans

Year	Rate	Year	Rate
1927	6%	1945	3½%
1928	5¾%	1946	3½%
1929	5½%	1947	3¼%
1930	5¾%	1948	3¼%
1931	5½%	1949	3¼%
1932	5¼%	1950	3¼%
1933	4¼%	1951	3¼%
1934	4¼%	1952	4%
1935	3½%	1953	4%
1936	3½%	1954	4%
1937	3½%	1955	4¼%
1938	3½%	1956	4¾ & 4-7/8%
1939	4¼%	1957	5%
1940	4%	1958	5%
1941	4%	1959	5%
1942	3¾%	1960	5%
1943	3½%	1961	4-7/8%
1944	3½%	1962	5, 5½ & 5-3/8%

(Report of the Royal Commission on Local Authority Finance page 101 and the Annual Reports of the Local Authorities Loans Board) attracted to local authority stock. In the case of trust funds, of course, the situation is geared by the provisions of section 4 of the Trustee Act 1956, but there is still a fair range of investments set out in section 4 (e.g. first mortgages) which generally carry a higher rate of interest than local authority stock. In many instances, however, the investor is more concerned with building up a portfolio of investment rather than return and in such a case the large volume of money that can frequently be sunk into a single local authority loan, the length of term for which finance can be invested, and the ease of administering the investment, may be of importance in attracting money to this field. The Royal Commission on Local Authority Finance (see Report page 35) makes the following statement upon this matter, "We did not find that investors generally complained that interest rates were too low nor did they think that an increased rate would necessarily increase very greatly the amount of money that would be invested in local body loans." The vital point, therefore, seems to be the total volume of money available rather than the rate of interest.

Although it is very difficultto obtain any accurate information upon the matter or indeed, to make any informed conjecture, it appears probable that continual changes in the rate of interest have an adverse effect upon investment in this sector. It is reasonable to assume that if a potential investor believes that rates are at their peak he will be likely to invest whereas if he thinks that they are likely to rise he will not place his money until they have risen. But on the other hand if he just does not know what will happen he will tend to invest short term which in any event, seems to be the practice of the small investor. Frequent changes can be very difficult in those cases where a loan has not been fully sold as in such an event it is possible that one part of the loan may have to be floated upon a different interest rate from the other.

The usual procedure now is for the Loans Board to prescribe different rates of interest for different terms but although this has been the practice for the past few years it was not always the case. Until June 1956 the procedure had always been to set a single rate regardless of the term of the loan. However multiple rates are virtually imperative in those situations where some maturities are going to sell more readily than others or where you are seeking to obtain finance from a large number of different lenders. Generally speaking the open market will only accept terms of up to ten years with the most desirable term possibly five years but such a term (at least in theory) is usually much too short for the local authorities. The longer term maturities therefore, almost inevitably, command higher interest rates than the shorter terms. It is usual to set about three different rates, i.e. say, for terms of up to five years up to ten years, and above ten years. But this in turn can create some difficulties because in such an issue there would be a great tendency for the six and eleven year terms to sell very readily as these are the shortest terms at the higher rate of interest. To counter this the Loans Board frequently stipulates that only a certain portion of the issue may be sold on a six year term.

It is of some interest to conjecture upon the situation that would arise if interest rates were permitted to run free. The most immediate effect that would make itself felt would probably be a substantial rise in rates but at the same time a vast proliferation of different rates would almost certainly occur. Not only would a number of different rates appear for different terms but the smaller authorities would be forced to pay higher rates of interest than the larger ones as they would find it more difficult to obtain finance. Also it is quite possible that different rates may rule upon different projects as finance is sometimes more readily obtainable for one class of project than another. Thus a borough may find itself paying six per cent on finance for a new library but eight per cent upon money required for a sewerage scheme.

It has been suggested that one means whereby investment in this sector, and especially long term investment, may be made more attractive would be to make issues (i.e. long term issues) on the condition that the rate of interest may be adjusted at say, three yearly intervals. The difficulty with such a proposition is that if adjustments are to be made upwards then no valid argument could be made out against downward adjustments in the rate. But a provision in a loan contract to the effect that the rate of interest is subject to downward adjustments would most certainly be a deterrent to prospective investors.

THE

DEMAND FOR CAPITAL

What do the authorities want loan finance for? What are the factors which affect the demand for loan finance? Is the demand spread evenly throughout the country and among the different classes of authorities? These are the questions which this section sets out to answer.

Total Demand

As the legislation requires (with a few insignificant exceptions) that all capital borrowing by local authorities must have the prior approval of the Loans Board it is possible to assess fairly accurately the total demand which will ultimately make itself felt upon the market by considering the total volume of loan applications sanctioned by the Board. At the same time the total volume of loan applications submitted to the Board reflects the amount which the authorities would like to borrow upon the market. These figures have already been set out in Table No. A...1 in the preceding section.

Section 40 of the Local Authorities Loans Act sets out expiry dates which provide for the lapse of a loan authority after the expiration of a certain period of time. If any portion of the loan has been raised the balance of the sanction expires at the end of ten years from the date upon which the loan was sanctioned. If no part of the loan has been raised the expiry date is three years from the date of sanction. Thus it is reasonable to assume that loans sanctioned will make themselves felt as demand upon the market within a reasonable time after sanction. A consideration of loans sanctioned shows the demand that is likely to make itself felt in the future but it is also possible to make an examination of the net debt of the authorities and so derive an indication of demand which has been made in the past. This concept is used later in this section in assessing regional demand.

Referring to Table No. A...1, we see that Loans sanctioned immediately following the Second World War were at a comparatively low figure and that there was only a steady rise until 1953 when a very steep increase occurred. This higher figure has been maintained in the years following 1953. The big increase in sanctions which took place in that year appears to have been caused by the sudden release of pent up war time demand. This did not make itself felt immediately after the War largely because the activity of the Government restricted the operations of the authorities on the market until its own immediate capital requirements had been satisfied.

Table No. B...1 sets out the capital investment executed by the Government, private and local government sectors over the years shown and shows each as a percentage of total capital investment. This Table, although useful, does not show the total volume of capital investment that the market is called upon to finance because considerable amounts of capital expenditure are now met from revenue and, as will be shown later, this portion is likely to increase. The Table is of value in showing the relative share of capital expenditure as between the three sectors and this could give some indication of the portion of available capital that each of the sectors was entitled to. At the same time it could be argued that much of the capital expenditure carried out by the Government and and Local Government sector may be of greater national and local importance than much of the work carried out by the private sector; after all the basic economic framework of the country is provided by Government and local government. For reasons which will be considered more fully later the relative proportions of total capital expenditure carried out by each of the three sectors is likely to change somewhat over the next three or four decades, i.e. the proportion met by the local government sector is likely to drop.

At the same time however, we should take into consideration the point that figures for capital expenditure are very sensitive to

Table No. B...1

GROSS CAPITAL INVESTMENT (excluding changes in stocks)

Year	Private Capital Investment		Government Capital Investment		Local Government Capital Investment	
	£(m)	% Total	£(m)	% Total	£(m)	% Total
1939	17	44	16	41	6	15
1944	14	50	10	36	4	14
1947	37	58	21	33	6	9
1951	74	60	41	33	10	8
1952	91	63	41	28	12	8
1953	98	57	55	32	18	11
1954	104	57	57	31	21	11
1955	130	61	59	28	23	11
1956	128	58	67	30	26	12
1957	120	54	72	32	31	14
1958	137	56	72	30	35	14

(Report of the Royal Commission on Local Authority Finance - page 113) fluctuations in the overseas exchange position of the national economy and any drastic tightening in the exchange position could cause a sharp drop in the total volume of capital investment with a proportionately greater drop in that amount carried out by the private sector.

The Functions of Local Authorities

The demand for capital from the local authorities is, to a large extent a function of the activities carried out by the local bodies and to fully appreciate the forces affecting the demand for capital it is necessary to pay at least passing attention to the operations of the various authorities. At the outset it should be said that all local authorities are the creation of statute and their powers are closely defined in the various empowering and enabling acts. A local authority can do only that which is set out in its constituting act because they are subsidiary governmental institutions and possess no sovereign legislative powers in their own right.

In function and structure the authorities differ markedly. Municipalities (which include cities, boroughs, and town districts) derive their powers from the provisions of the Municipal Corporations Act 1954. These authorities are responsible for the internal administration of the municipal areas and their main functions are the provision of civic amenities such as sewerage and water reticulation, roading, and public transport. The demand for loan finance is generally geared to the provision of works of this nature. But considerable civic building and housing activity is also undertaken by municipalities and this has consumed substantial amounts of capital in the post war years. In recent years many boroughs have undertaken pensioner-housing schemes and for this class of work subsidies are made available to local authorities through the Department of Health. This has had a dual effect for on the one hand it has alleviated somewhat the amount which the authorities have been required to seek upon the market while on the other hand the existence of the subsidy scheme has doubtless induced many municipalities who would not otherwise have considered this work to undertake it. The provision of municipal buildings such as museums, art galleries, office accommodation and libraries is now looked upon as the legitimate prerogative of the boroughs. The construction of airports has also consumed considerable amounts of capital in the post war years and this work is also subject to a considerable amount of assistance from Government. Municipalities occasionally seek loan finance for the renewal of plant and the replacement of such items as omnibuses but these are frequently financed from depreciation and renewal funds which are built up from appropriations from rate revenue or trading profits, if such are available.

In some areas special 'ad-hoc' authorities have been established to carry out specific operations, e.g. the various transport boards, and the metropolitan drainage boards established in Dunedin, Christchurch, Auckland and upon the North Shore. These institutions are necessary in order to obtain the co-ordination of these services in those districts where several different territorial authorities exist. Authorities of this nature all derive their powers including the power to borrow, from individual empowering acts. In the Auckland Urban area the two drainage boards provide the main trunk sewers while the individual territorial authorities are responsible for installing the lateral connections. The urban drainage boards have been very heavy borrowers upon the market in the post-war years and this demand is likely to continue with the increase in population.

The following figures show the loans sanctioned for the metropolitan drainage boards over three years and give an indication of the vast amounts of finance which these bodies have consumed.

1963	
Christchurch	£600,000
Dunedin	£250,000
Hutt Valley	£210,000
	£1,060,000

1962

Auckland	£2,600,000

1961

Christchurch	£1,580,000
Auckland	£1,000,000
North Shore	£1,000,000
	£3,580,000

(The above figures were taken from the text of the Annual Reports of the Local Authorities Loans Board for the years 1961-1963.)

It should be pointed out that the figures given above do not include sanctions granted to territorial authorities in the various constituent areas to carry out lateral reticulation in conjunction with the work of the drainage boards.

Harbour Boards derive their authority from the Harbours Act 1950. Harbour works tend to be so expensive, and vital from a national as well as a local point of view, that the legislature has deemed it expedient to require that all harbour boards should have the approval of Parliament in the form of an individual empowering act as well as the approval of the Loans Board before they can go on to the market. This means that any proposal involving borrowing by a harbour board is subject to criticism in Parliament. A feature of harbour board borrowing over the past few years has been the heavy amounts demanded by the secondary boards.

The counties which, in the main are responsible for the territorial control of the rural areas of the Country, are not generally large borrowers of finance; their capital requirements being confined largely to bridge and road construction and maintenance work which is subsidised heavily from National Roads Board funds. It has been the policy of many counties to attempt to meet as much roading expenditure as possible from revenue. On the other hand there are a few heavily urbanised counties, such as Waitemata, Waimairi, and Manukau which are faced with development problems similar to those of the larger cities and, of course, have a comparable demand for capital.

Hospital boards, which are responsible for the administration of hospital districts have been very heavy borrowers over the past ten or so years. Like harbour boards, hospital board borrowing has become very subject to control by the Government and all loan proposals must have the approval of the Hospital Works Committee, as well as the sanction of the Loans Board, before market activity can be undertaken. In past years hospital boards possessed rating powers but these have now been lost and these boards are financed entirely from Government funds. Section 89(1) of the Hospitals Act 1957 provides as follows:-

"In respect of every financial year there shall be paid to the Board by way of grant, out of money appropriated by

Parliament for that purpose such sum as the Minister may determine as being necessary to enable the Board to carry out its functions having regard to the estimates for that year approved under section eighty eight of this Act."

These annual grants made to the hospital boards cover revenue expenditure including loan charges but the boards are still required to seek loan finance to meet major capital items but some very small amounts of capital expenditure are frequently met from the annual grant.

In effect, therefore, these boards could be looked upon as local spending agencies of the Central Government and it appears that the locally elected members of these boards are retained merely for the purpose of preserving some semblance of local autonomy. The peculiar position of hospital boards has had a singular effect upon their ability to obtain finance and this matter is considered later in the section dealing with the flow of capital.

From time to time individual authorities which have been designed to manage a single asset have made an appearance. The two most notable of these in recent years being the Auckland Harbour Bridge Authority and the Christchurch Lyttelton Road Tunnel Authority. Both of these authorities derive their powers from individual empowering acts. Although these two bodies have consumed considerable volumes of capital over the past few years their demand will probably not be of a continuing nature and it is unlikely that other authorities of a like nature will make an appearance in the near future.

Power reticulation is the function of the power boards but in many instances this activity (and in a very few cases power generatio is carried out by municipalities. Power boards derive their authority from the Electric Power Boards Act 1925 and these institutions have been very active upon the market in recent years.

The functions of the numerous other minor bodies such as rabbit boards and catchment boards can be readily assumed from their names and in any event they are insignificant as borrowers of capital finance.

Table No. B...2 sets out the loans sanctioned in respect to the particular class of local body. It can be seen that there is a wide variation in the amounts demanded by the different classes of bodies. It will be noted that there are six classes of local authorities whose demand figures amount to well in excess of 75% of the total figures.

Table No. B...3 sets out sanctions in accordance with the purpose of the loan. It can be seen that three of the largest items in this Table are the prerogative of separate classes of authorities i.e. hospital boards, electric power boards, and harbour boards.

The territorial local authorities derive their incomes from rates levied over either the annual, capital, or unimproved values of all the rateable property within their districts, and in some special instances, upon property outside their districts. Most municipalities rate upon the unimproved values of their property while a few rate upon the annual value system and a very few on the capital value

Table No. B...2

Loans Sanctioned by Class of Local Authority

	1960	1961	1962
Counties	1,386,340	2,262,014	2,797,112
Boroughs	8,654,557	11,726,125	11,648,740
Town Districts	4,571	84,000	114,800
Catchment Boards	138,530	235,350	337,250
Land Drainage Boards	-	14,000	-
Electric Power Boards	2,463,150	2,671,750	3,941,800
Urban Drainage Boards	742,600	2,744,700	3,044,460
Urban Transport Boards	200,000	-	200,000
Road Tunnel Authority	-	3,250,000	-
Harbour Bridge Authority	500,000	42,300	-
Rabbit Boards	9,000	11,270	23,700
Fire Boards	205,363	188,430	132,900
Harbour Boards	4,185,100	2,150,200	4,644,140
Hospital Boards	6,324,700	3,419,500	3,412,150
£	24,813,911	28,799,639	30,297,052

(Report on the Local Authority Statistics of New Zealand - Department of Statistics)

Table No. B...3

Loans Sanctioned by Subject Matter of Loan

	1960	1961	1962	1963
Waterworks	1,276,175	4,252,550	1,401,480	2,551,590
Drainage & Sewerage	2,935,719	7,043,350	6,970,200	4,455,150
Roads & Bridges	1,970,550	1,549,550	2,101,480	1,419,400
Public Buildings	987,550	2,227,800	1,470,750	1,654,650
Housing	1,255,298	1,183,866	986,350	1,179,510
Transport	1,282,230	12,000	200,000	-
Airports	497,000	3,780,000	31,500	348,925
Recreation	712,000	466,200	268,900	403,600
Electricity Supply	3,067,900	4,311,000	3,048,600	3,413,250
Hospital Works	5,542,700	5,142,000	2,384,000	3,568,000
Harbour Works	3,911,100	3,418,350	3,478,900	5,269,500
Fire Services	301,475	146,230	158,800	151,550
Gas Works	-	165,000	91,600	15,000
Abattoirs	549,650	350	31,000	42,500
Machinery	39,500	91,950	92,700	14,600
River Works	55,450	285,550	594,500	468,000
Miscellaneous	4,588,500	572,754	723,000	797,750
£	28,972,797	34,648,500	24,042,760	25,752,975

(Annual Reports of the Local
Authorities Loans Board 1961-1963)

system. The counties are divided about equally between the capital and unimproved systems while no counties rate on the annual value system. Many municipalities possess trading undertakings of some description or other from which they derive some measure of income (e.g. the supply of electricity) or which incur a loss which has to be reimbursed from some other source (e.g. public transport). Catchment and rabbit boards possess direct rating power (which is frequently exercised by the levy of a differential rate) but the major 'ad-hoc' authorities (e.g. urban drainage and transport boards) although in possession of direct rating power usually collect their rates by means of a levy over the territorial authorities within their districts. Power boards are still statutorily possessed of rating power but now derive their incomes mainly from revenue sources, i.e. from the sale of electric power frequently supplemented by the sale of electrical appliances through retail stores. It is from this income that the loan charges incurred by the authorities are met. Section 48 of the Local Authorities Loans Act 1956 provides that loan charges may be met from either the general account or the proceeds of a special rate. As the general account is financed mainly from the revenue of general rates the rate revenue is used to meet loan charges in either event.

Section 45 of the above Act sets out the security which may be pledged in respect of a loan i.e. it may be either a special rate or the property or revenue (derived from any source) of the local authority. Money received or receivable from the Crown and money already appropriated cannot be pledged as security. The different securities pledged for the loan (i.e. if there is more than one security pledged) are jointly and severally liable for the whole amount of the loan.

The Factors Affecting Demand

In some cases the topographical structure of the terrain upon which the town is situated has required the expenditure of more capital in order to effect development works than would otherwise have been the case. In the case of Wellington City, for example, very steep hill country has to be contended with and this has necessitated the use of heavy earthmoving machinery in order to install subdivisions and effect other construction works. Another problem town in this respect is the Borough of East Coast Bays in the Auckland Urban area. This Town is strung out along the coast and is divided into several semi-isolated pockets; facts which have made it very difficult to serve the Town with water and sewerage reticulation. On the other hand boroughs which are located upon dead level areas are not called upon to meet the same high cost in installing services. Construction works also tend to be somewhat more expensive in isolated towns where contractors may be required to move their men and machinery many miles before they can start work.

In some towns the residents may be continually demanding of their councils that certain works be carried out while other boroughs may possess ratepayers who are prepared to let grass grow in the main street but don't want rates raised in any circumstances. Many small country boroughs are in this latter category. In some instances councils are fired with a more progressive spirit e.g. in the case of Lower Hutt City many works, especially in the way of civic buildings have been carried out which could well have been foregone. This situation frequently arises where several towns are in close proximity with each other and there is a tendency for them to compete in the provision of civic amenities. These circumstances have involved the excessive use of capital funds while at the same time requiring the ratepayers to meet heavier rate demands.

In some cases capital demand is maintained at a high level by reason of the standard of building required. This has been an important factor in the construction of many hospital works and especially in the case of nurses' homes. It is possible that the shortage of nurses in recent years has tempted the construction of very elaborate buildings.

Government policy is also a force which has had a very potent effect upon the demand for finance. If the Government decides to offer inducements by way of subsidies upon certain works demand for loan capital to finance this class of work will almost certainly increase. A good example of this is the subsidising of pensioner housing schemes. There can be no doubt that schemes of this nature induce local authorities to indulge in these works and they generally resort to the loan market to seek the balance of the capital required.

It has largely been local pressure that has caused the development of several small harbours and this has caused a big capital demand for this type of work in recent years. If shipping in New Zealand was more centralised upon the major ports much of the heavy capital expenditure sunk into the development of secondary ports in recent years could have been avoided. But local parochialism has kept the smaller ports open. In some instances harbour boards have made play to local farmers of the fact that the closure of a small port would involve them in increased transport costs. The following is a sample of loans sanctioned for secondary harbour boards over the past few years. The schedule is by no means exhaustive.

<u>1963</u>

Gisborne	£655,000
Southland	650,000

<u>1962</u>

Whangarei	£1,500,000 (required for the oil refinery)
Southland	725,000 (required for the installation of a mechanical meat loader)

1960

Southland	£493,600
Picton	100,000
Nelson	420,000
Tauranga	500,000
Timaru	520,000

(The above figures were taken from the texts of the Annual Reports of the Local Authorities Loans Board 1960-1963)

Table No. B...4 sets out the net debts of all the harbour boards in New Zealand which handle overseas shipping as at 30 September 1961 - later figures are not available. The Table demonstrates clearly the relative dominance of the secondary boards as consumers of loan capital.

If authorities were able to meet capital works from their own revenue then it is reasonable to assume that they would refrain from seeking loan finance to satisfy their capital requirements. Now in respect to income local authorities fall into two fairly clearly defined groups. The territorial authorities, i.e. the counties and boroughs derive their income very largely from rates levied upon the land within their boundaries many of these bodies generally have other sources of income but these are usually insignificant (i.e. with a few notable exceptions e.g. the Borough of Stratford together with a few other small boroughs virtually live off their electricity undertakings). On the other hand we have the local authorities which rely mainly upon

Table No. B...4

Net Debt of New Zealand Harbour Boards

as at 30 September 1961

Auckland	£6,578,557
Whangarei	709,585
Bay of Islands	199,660
Tauranga	546,256
Napier	1,268,592
Gisborne	676,200
Taranaki	1,644,032
Wellington	1,276,039
Marlborough	308,619
Nelson	784,453
Lyttelton	2,607,560
Timaru	745,516
Otago	755,604
Southland	4,748,815

(Report of the Local Authority Statistics of New Zealand; Department of Statistics) trading income, supplemented in a few cases by limited rating power. This group includes power boards and harbour boards.

Now rating liability falls not upon the entire population but upon a relatively small group of land owners. Debate has raged as to whethe or not rates constitute an intolerable burden upon the ratepayer but it is certain that any substantial increase in rates designed for the purpose of enabling the authorities to meet more capital works from revenue would be hotly opposed. On the other hand the revenue producing authorities would be in a somewhat better position to meet capital expenditure from revenue. Before we go any further, however, it would be as well to point out that in the ultimate outcome all capital expenditure is met from revenue, whether that revenue be from rates or trading concerns. The financing of capital works from loans, however, has the effect of spreading the expenditure over a longer period of time but at the same time it is inevitably more costly in the long run because of the outlay in interest.

In some instances the use of loan finance would clearly be uneconomic; to borrow e.g. say, amounts of one hundred pounds per year over a considerable period of time, each, upon say, twenty year terms, would be unprofitable because after about the twelfth year the amount paid out annually in interest and loan charges would begin to exceed the annual amount borrowed. Thus it is usually preferable to meet the cost of many minor and continually recurring items, such as street works, from revenue. Indeed many counties and small boroughs who are faced with only this sort of expenditure hardly resort to the market at all. But when it is desired to create a durable asset which will have a long life it is frequently desirable to use loan finance rather than revenue so that the cost may be spread into the future thus enabling future ratepayers, who will also derive benefit from the project, to foot a portion of the cost.

A further point of relevance is the method of finance imposed upon the authorities by statute. The territorial authorities are required to draw up annual estimates of expenditure and then strike a rate of so much in the pound to cover that expenditure. The building up of general reserves is not permitted and as previously stated any substantial increase in rates is likely to meet with considerable opposition. But the authorities which rely mainly upon trading income, such as power and harbour boards, are usually able to appropriate large sums annually to general reserves and then, at some later date, make use of the reserves to finance capital works. If this is done the point made above about the spreading of capital cost is effected in reverse. When power reticulation has reached the saturation stage and harbour development settles down it is possible that these classes of authorities will be able to satisfy most if not all of their capital requirements from revenue.

Hence in concluding this portion of the argument we could summarise by saying that it is frequently desirable, irrespective of ability to pay, to meet the cost of capital works from revenue; that the trading authorities will probably be able to meet increasing amounts of capital expenditure from revenue; many territorial authorities who are faced only with small items will be able to meet them from revenue but that loan finance will still be required to meet the major capital works of the territorial and 'ad-hoc' authorities.

Table No. B...5 gives an indication of the relative amounts met from loan finance and from revenue. Reference to part 1 of the Table shows that there is a tendency for the older established authorities, e.g. Wairoa and Newmarket to meet proportionately larger amounts ofcapital expenditure from revenue than the newer more rapidly developing boroughs such as East Coast Bays and Tauranga. The figures for the Makara County run completely against the general trend for counties. This was brought about by the fact that the bulk of capital expenditure in that County was carried out in respect or urban development in the Porirua County Town and was secured over that Town. In effect therefore, the figures for Makara could be looked upon as the figures for a very rapidly developing borough rather than as the figures for a county. It is of interest to note that since 1962 this County has been disbanded; the rural portion being amalgamated with the Hutt County while the urban areas have been constituted into the new Porirua City. A further point of interest in the Table is the very large amount of capital expenditure met from revenue by the Southland County.

But probably the most important factor affecting the demand for capital is population growth. The demand for capital for such works

Table No. B...5

(Part 1)

A Random Sample of Local Authorities Showing the Sources of Capital Expenditure

All Figures as at 31 March 1962

Boroughs	From Revenue	From Loan
Kaitaia	20,326	16,264
Whangarei	111,859	45,104
Auckland	676,975	1,670,458
East Coast Bays	14,555	124,790
Newmarket	1,795	96
Ngaruawahia	11,417	-
Wairoa	30,991	-
Tauranga	152,813	129,066
Counties		
Mangonui	88,142	-
Waitemata	532,660	260,531
Whakatane	107,270	-
Stratford	100,006	5,420
Makara	-	54,656
Waimairi	99,739	116,629
Ashburton	164,004	-
Southland	446,272	5,545
Total Figures		
Boroughs	6,985,053	8,374,768
Counties	8,727,428	1,517,766

(Report on the Local Authority Statistics of New Zealand, Department of Statistics)

Table No. B...5

(Part 2)

Loan Receipts and Capital Expenditure

Electric Power Boards

Year	Loan Receipts	Capital Expenditure
1939	742,015	776,296
1944	86,800	337,588
1949	1,318,864	1,682,750
1954	2,435,657	4,793,206
1956	2,862,077	3,912,211
1962	3,012,340	5,030,190

Harbour Boards Capital Expenditure

Year	From Revenue	From Loan
1953	416,499	1,571,055
1954	362,259	1,102,811
1955	500,781	1,277,348
1961	792,866	3,238,292

(Report on the Local Authority
Statistics of New Zealand,
Department of Statistics)

as housing subdivisions, hospital works and power reticulation tends to be related fairly closely to population growth. It can be assumed that an area with a rapidly growing population will generally require more capital than an area with a static population.

Owing to the diverse multiplicity of factors which intervene it would be virtually impossible to derive any quantitative relationship between capital demand and population growth. But we can, by making an examination of figures for net debt per head of population, produce statistics which may help to demonstrate the position. Firstly let us take the full number of debtless boroughs and counties in New Zealand and examine their rates of population growth. The fact that a local authority is debtless indicates that its activities upon the market have been negligible for at least the past five years. Table No. B...6 excludes authorities situated in the Auckland Urban Area where net debt figures are complicated somewhat by the presence of the debt structure of the large number of 'ad-hoc' authorities meaning that territorial authorities in the Area would tend to show a smaller net debt per head of population than isolated boroughs where all the services are provided by the territorial authority.

The debtless local authorities are for the most part very low in the order of population growth but one or two notable exceptions are obvious in the table. We see that the Halswell County has, in fact, one of the highest rates of population growth in New Zealand and yet it appears in the schedule of debtless authorities. This is probably

Table No. B...6

Net Debt per Head

As at 31 March 1966

	Population	Net Debt	Debt per Head
Total Counties	879,210	10,706,831	12.17
Total Boroughs	1,578,170	66,251,766	41.98
Overall	2,457,380	76,958,597	31.31

Debtless Local Authorities

	Rate of Population Growth 1956-62	Population as at 31/3/62
Opotiki County	- 5.2	4,850
Uawa County	1.1	1,740
Eltham County	- 0.3	3,610
Waimarino County	-13.7	2,270
Oroua County	- 1.1	4,550
Wairewa County	-12.8	780
Taieri County	8.6	7,980
Tuapeka County	-37.4	4,800
Kumara Borough	- 3.1	430
Hampden Borough	- 1.3	300
Lawrence Borough	0.8	590
Halswell County	84.4	3,220

Table No. B...6 (continued)

Local Authorities with the Slowest Rate of Population Growth

	Population Growth 1956-61	Population	Net Debt	Net Debt per Head
Hokianga County	-18.0	5,920	13,202	2.23
Clifton County	- 6.2	2,580	27,156	10.52
Tuapeka County	-37.4	4,800	-	-
Waimarino County	-13.7	2,270	-	-
Buller County	-10.5	4,040	29,860	7.39
Inangahua County	- 8.2	3,060	14,472	4.72
Golden Bay County	- 9.5	3,650	19,660	5.38
Waihemo County	- 8.7	990	3,449	3.48
Palmerston Borough	- 8.7	870	13,434	15.44
Naseby Borough	-18.5	150	4,667	3.11
Vincent County	-16.5	4,010	14,838	3.70
Wairewa County	-12.8	780	-	-

(the above figures are as at 31 March 1962)

(The above figures were compiled from the Report on the Local Authority Statistics of New Zealand - Department of Statistics)

Table No. B...6 (continued)

Local Authorities with the Fastest Rate of Population Growth

	Population Growth 1956-61	Population	Net Debt	Net Debt per Head
Taupo Borough	84.7	5,760	521,899	90.60
Mt. Maunganui Borough	48.3	5,690	264,305	46.45
Taupo County	35.9	12,750	14,772	1.15
Kawerau Borough	63.9	5,390	199,636	37.03
Taradale Borough	42.6	5,250	83,850	15.97
Havelock North Borough	37.0	4,050	75,656	18.68
Tawa Borough	78.2	7,600	520,152	68.44
Hutt County	45.6	32,400	943,862	29.13
Upper Hutt Borough	37.9	17,550	1,064,483	60.65
Halswell County	84.4	3,220	-	-
Waitaki County	36.7	11,400	97,323	8.53
Mosgiel Borough	59.4	6,810	218,586	32.09

(The above figures were as at 31 March 1962)

(The above figures were compiled from the Report on the Local Authority Statistics of New Zealand - Department of Statistics) accounted for in the proximity of that County to Christchurch City. Although the County has taken some population overflow from the City considerable areas of the County have been absorbed into the City upon becoming built up, meaning that the City has been compelled to bear the cost of servicing and thus leaving the County to cope with the purely rural areas of the district. A somewhat similar situation exists in the relationship between Taieri County and the Mosgiel Borough.

A further interesting feature of the debtless local authorities is that they are nearly all counties and the three exceptions are all defunct South Island boroughs.

The local authorities with the most rapid rate of population growth, in general, exhibit net debts far in excess of the standard but here again one or two interesting exceptions occur. Waitaki County has a very low net debt but the population figures for that County have been greatly inflated by the inflow of workers required for the hydro-electric development. But the full cost of this development has been met by the Government and has therefore not reflected in the debt figures of the County.

We see also that the Taupo County exhibits an abnormally low net debt figure as compared with its rapid rate of population growth. Development problems associated with that County were considered to be of such a nature that the Government assumed virtually the full cost burden and indeed it is only in recent years that the County has assumed the status of a fully autonomous local authority. The demand for capital from this County has therefore been considerably restricted.

Local authorities with very slow rates of population growth almost without exception exhibit net debts well below the overall standard for the particular class of authority.

Thus in concluding this portion of the argument we can make the point that a local authority with a high rate of population growth will generally possess a demand for capital which is in excess of the average while the converse proposition is, in general, also true.

The figures for net debt which are given in Table No. B...6 include the full funded debt of the local authority with the amount of accumulated sinking funds deducted.

Regional Demand

We have seen that the demand for capital is not spread evenly throughout the different classes of local authorities. But at the same time demand is not spread evenly throughout the Country. Some areas demand more capital than do others. In Table No. B...7 we once again resort to the net debt figures to demonstrate capital demand. This Table sets out the debt of all the local authorities comprised in the four major urban areas. The very heavy preponderance of demand concentrated in the Auckland Area is clearly demonstrated by this Table. For reference purposes we have also included, where relevant, the population figures and these assist in showing the great

Table No. B...7

The Net Debts of the Major Urban Areas

(as at 31 March 1962)

Auckland Urban Area	Net Debt	Population
Auckland City	13,506,966	145,000
East Coast Bays Borough	462,774	10,000
Birkenhead Borough	317,420	8,030
Northcote Borough	229,974	5,780
Takapuna City	482,304	21,000
Devonport Borough	232,230	11,000
Henderson Borough	275,812	4,260
Glen Eden Borough	95,288	5,370
New Lynn Borough	325,239	9,080
Newmarket Borough	137,768	1,810
Mount Albert Borough	950,480	26,000
Mount Eden Borough	256,473	18,350
Mount Roskill Borough	1,268,055	31,000
One Tree Hill Borough	249,784	12,850
Onehunga Borough	403,308	16,300
Ellerslie Borough	111,768	4,420
Mount Wellington Borough	421,361	16,650
Howick Borough	237,795	6,940
Otahuhu Borough	244,471	8,800
Papatoetoe Borough	417,084	18,900
Manurewa Borough	397,318	12,550
Papakura Borough	167,841	8,740
Waitemata County	1,031,135	58,100
Manukau County	642,619	32,000
*Auckland Harbour Board	6,578,557	
Auckland Harbour Bridge Athy.	6,389,040	
Auckland Transport Board	2,550,470	
Auckland Electric Power Bd.	3,961,022	
Waitemata Electric Power Bd.	1,902,812	
Auckland Drainage Board	12,170,884	
North Shore Drainage Board	1,310,102	
	£58,728,154	492,930

* As at 30 September, 1961.

Table No. B...7 (continued) (as at 31March 1962)

Wellington Urban Area	Net Debt	Population
Wellington City	9,071,525	124,700
Lower Hutt City	2,645,951	54,000
Upper Hutt Borough	1,064,483	17,550
Petone Borough	136,051	9,840
Eastbourne Borough	154,400	2,640
Tawa Borough	520,152	7,600
Hutt County	943,862	32,400
Makara County	607,660	18,350
Hutt Valley Drainage Board	1,686,349	
*Wellington Harbour Board	1,276,038	
Hutt Valley Power Board	1,431,422	
	£19,537,893	267,080

Dunedin Urban Area		
Dunedin City	6,358,407	73,700
Mosgiel Borough	218,586	6,810
St. Kilda Borough	12,759	6,590
Port Chalmers Borough	88,734	3,120
West Harbour Borough	31,832	2,300
Green Island Borough	138,753	5,310
*Otago Harbour Board	755,604	
Dunedin Drainage Board	558,955	
Taieri County	-	7,980
	£8,163,630	105,830

* As at 30 September 1961.

Table No. B...7 (continued) (as at 31 March 1962)

Christchurch Urban Area	Net Debt	Population
Christchurch City	3,456,219	153,500
Riccarton Borough	86,791	7,320
Lyttelton Borough	36,525	3,380
Paparua County	201,647	16,500
Waimairi County	602,243	43,000
Heathcote County	32,586	6,470
Halswell County	-	3,220
Christchurch Transport Board	697,708	
Christchurch Drainage Board	4,736,333	
Lyttelton Harbour Board	2,607,560	
Christchurch Lyttelton Road Tunnel Authority	2,412,330	
	£14,869,642	233,390

(Report on the Local Authority Statistics of New Zealand - Department of Statistics) divergence in the sizes of the various authorities making up the different urban area.

Demand as Between Long Term and Short Term Capital

In some periods long term finance i.e. say, for terms of twenty five years and upwards, may be more readily obtainable than short term finance while at other times the converse situation may apply. Broadly speaking, however, short term capital is more readily obtainable than long term finance.

The Local Authorities Loans Board has adopted a policy of limiting the loan term to the life of the asset subject matter of the loan. But in any event it will not, except in very special circumstances, grant terms in excess of twenty-five years. These circumstances are confined to those cases where a very expensive and durable asset is to be constructed.

Ideally then, the authorities would prefer to place all of their issues at the maximum term permitted by the Loans Board but very frequently market conditions prevent them from doing this and an authority is often forced on to the market with a series of maturities carrying different rates of interest. This is designed to catch the different classes of lenders some of whom prefer long term, some medium, and some short.

Prior to about 1950 the authorities were able to raise most of the money they required from the institutions. A few, however, especially the larger bodies, explored the open market and more or less succeeded in placing their issues there without excessive advertising and without the aid of underwriting. About 1950, however a gradual tightening of the market set in and this forced many of the authorities, small and large alike, on to the open market. This meant that many of the smaller authorities were unable to raise finance at all. It also meant that maturities of a much shorter term had to be offered and this in turn gave rise to still further difficulties. Assume that there are merely two rates of interest operating i.e. a short term rate for periods up to five years and a long term rate for terms of five years and over. Now, if, in such circumstances, a loan is placed upon the open market in one issue the six year maturities will be sold first as that is the shortest term at the maximum rate of interest. After the six year maturities all the short term stock will sell and after that the maturities of up to ten years. This could mean that, after several months of intensive advertising the authorities find themselves with a heap of long term maturities upon hand which they cannot dispose of. But the Loans Board has taken action to rectify this situation and it will generally permit only a certain portion of an issue to be sold upon a six year term. At the same time it has permitted the authorities, in certain circumstances, to borrow for terms longer than the repayment table of the loan. Thus an authority may be permitted to borrow for a term of ten years upon a table of repayments based upon a term of twenty years. This means, of course, that the loan would have to be refinanced at the termination of ten years by means of a renewal loan. This practice is frequently resorted to in those times when long term finance is difficult to obtain. It has however, many inherent disadvantages, e.g. the necessity to raise renewal loans may inhibit the raising of new loans for essential construction works and may create artificial surges in the market. At the same time there is a tendency for renewal issues to be somewhat more difficult to raise than loans for new works because as they cannot be associated with some specific project they tend to lack 'glamour appeal'. The use of renewal loans is at its best merely a palliative and does not provide a sound solution to the problem of the lack of long term finance. Furthermore the overall financial structure of the local authority is not designed to borrowing upon short term.

The 1963 Annual Report of the Local Authorities Loans Board contained the following comment upon the subject of renewal loans.

> "The easing of the money market noted over the past year has undoubtedly benefited those local authorities with major works projects under way. In future years, however, the problem of raising loan money is likely to be accentuated by the necessity of many local authorities to refinance a large portion of maturing loans originally raised for six and ten years from 1952 onwards but with loan repayments or sinking fund contributions based on longer ultimate terms. The next few years should be critical ones in this respect.

"The financing of these renewal loans is an obligation which cannot be evaded and will take precedence over the financing of loans for new works. A major problem is therefore likely to arise although it may be offset to some extent by moneys available from repayment of loans after any reinvestment by holders of maturing loans. These moneys will form a pool from which local authorities will be able to draw in competition with other sections of the capital market.

The immediate problem, however, will be to obtain sufficient money to meet those balances of the maturing loans which have not been reinvested by previous holders and at the same time obtain sufficient money to enable the authorities to continue with approved capital works."

The Table No. B...8 sets out the amounts sanctioned for renewal loans together with the amount sanctioned for works loans for the respective year. We note that in the depression years of the early thirties the amounts sanctioned for renewal loans greatly exceeded that sanctioned for works loans. This indicates, firstly, the lack of capital formation in those years, secondly, the general paucity of finance and thirdly the tendency of investors to invest short term rather than long term. It should be pointed out that relatively heavy works expenditure took place in the late twenties and by the early thirties there was a need to refinance this expenditure. A somewhat analogous situation could well arise in the mid to late nineteen sixties as indicated in the tract from the Loans Board Report.

The Demand for Very Short Term Finance

As far as the demand for very short term finance is concerned we once again see that market conditions have forced doubtful practices upon the authorities. But the demand for very short term finance is really a question of the hypothecation of debentures and it is this which must now take our attention.

The hypothecation of debentures is carried out in accordance with the provisions of section 65 of the Local Authorities Loans Act 1956. In effect it is a process whereby an authority is able to mortgage debentures and thereby raise finance for a very short term before the loan itself is raised. The amount raised by way of hypothecation remains a first charge upon the loan when it is raised. Hypothecation finance is generally provided by either the trading banks or the National Provident Fund.

Now in times of market stringency there is a tendency for authorities to resort to this type of finance upon an undesirable scale and cases have occurred of the instrument of hypothecation being renewed, for what at times, amounts to an indefinite period. This means that a local authority may be using say trading bank finance to cover the cost of capital works, a situation which most would agree is quite undesirable. This condition is somewhat analogous to that which has existed in the field of company finance where companies have been forced to resort to overdraft accommodation to carry out development works because of the lack of suitable long term finance. A further disadvantage of hypothecation is the term aspect in relation to the life of the asset. Hypothecation means that the term of the loan as sanctioned by the Loans Board is extended by the amount of the period of the hypothecation. Hence it would be possible to have an asset with an anticipated life of twenty years the subject of a loan of thirty years.

Although very short term borrowing may be technically undesirable there can be no doubt that from a practical point of view it is vitally necessary that the power to hypothecate debentures should exist. A local authority is frequently called upon to meet expenditure at very short notice and may be unable to raise the necessary finance upon the market in the time available. At the same time the power to hypothecate tends to put a degree of flexibility into the market as a broker is able to make use of the process to tide him over when he sees that some suitable long term finance will be available in a few months time.

Although short term borrowing by local authorities may be undesirable the same certainly cannot be said of short term lending and indeed it is vitally necessary that there should be a repository for the funds of the authorities which are not immediately required to cover payments. A short term money market is especially necessary in those times when finance is difficult to obtain when an authority

Table No. B...8

Works and Redemption Loans Sanctioned

Year Ended 31 March	Sanctioned Works	Redemptions
1928	3,212,185	1,048,796
1929	3,866,551	809,221
1930	3,563,842	967,875
1931	1,766,256	838,901
1932	781,195	2,483,810
1933	406,521	2,348,231
1934	917,560	2,744,245
1935	1,585,440	2,379,955
1936	1,550,690	2,051,790
1937	2,411,358	430,313
1938	3,098,445	122,758
1939	3,013,872	1,188,525
1940	1,701,460	355,800
1941	2,709,505	1,602,670
1942	1,898,096	1,391,728
1943	1,497,120	1,121,000
1944	1,349,335	2,359,755
1945	1,737,807	698,120
1946	2,643,935	243,235
1947	7,289,436	1,106,430
1948	6,022,034	1,459,880
1949	6,977,289	1,542,177
1950	6,602,220	761,957
1951	9,242,938	485,550
1952	13,891,297	1,029,246
1953	17,853,560	196,330
1954	23,982,810	300,204
1955	25,818,955	448,971
1956	15,462,255	437,400
1957	17,232,790	30,000
1958	25,799,656	850,000
1959	20,537,646	542,100
1960	28,972,797	236,800
1961	34,648,500	474,505
1962	24,042,760	1,800,580
1963	25,752,975	3,578,589

(Annual Reports of the Local Authorities Loans Board) may be compelled to raise funds beyond its immediate needs simply because they happen to come along with the fear that when it does require the capital it may not be able to obtain it.

The Re-organisation of Local Authorities

The re-organisation of local authorities would possibly have some effect upon the demand for capital. This matter can be looked at from two distinct angles. Firstly there is the problem of the small local authority which cannot obtain finance. Re-organisation which had the effect of eliminating such bodies would, of course, mitigate this problem. But to be effective the re-organisation would have to do away with virtually all of the smaller authorities because if a few only were amalgamated into larger units the remainder may be compelled to compete for capital against a larger number of bigger authorities. Secondly there is the angle of total demand. Amalgamation could probably bring about some decrease in demand from the overall point of view. At present many services are duplicated and amalgamation could probably prevent such duplication. Examples of this exist in such items as administrative buildings and units of heavy plant (which frequently has to remain idle for large parts of the year) which could well serve local authorities many times the size of those which they are at present serving without the expenditure of any further capital. The best example of this exists in the Auckland Urban Area where some thirty authorities all support their own administration buildings. It must be admitted that some attempt has been made to pool items of plant so that they may be more efficiently used, but this practice has not yet been carried to any great lengths. A further example of duplication is contained in the generation of electricity. Several instances exist of small boroughs, which are completely surrounded by power boards, generating their own electricity.

A larger authority is in a position to let larger contracts and can usually effect some saving in this respect. However the use of ad-hoc authorities and in particular the Auckland Drainage Board has, in some cases, done away with the need for several small bodies to each provide themselves with the same service.

The growth of county towns over the past few years (there are now over one hundred of these bodies in New Zealand) has probably increased the demand for capital. Being a legal subdivision a debt can be centralised over a county town and many cases exist of county towns carrying net debts per head far in excess of those of their parent county. The element of local autonomy brought about by the assumption of county town status has doubtless resulted in a considerable amount of borrowing taking place which would not otherwise have occurred. Many county towns are situated on the outskirts of large urban areas and have developed along urban lines. Such a situation means a greater demand for finance than would be the case if the area of the county town had been amalgamated with the urban area. But on the other hand some saving of capital may result if some of the smaller boroughs assumed the status of county towns.

THE SUPPLY OF CAPITAL

This section considers the sources from which the local authorities obtain their capital finance. The lenders of finance to local bodies may be divided into three separate groups. On the one hand we have the open market, i.e. the small lender; the elderly widow, the family trust, the education trust, or the farmer with a few hundred pounds to spare. Secondly we have the institutions, the most notable of which are the insurance companies and the trustee savings banks. Most of these are under some degree of legislative restriction but are generally free to determine their own investment policy. Then we have the state lending institutions which play a vital role in the field of local body investment. These include the State Advances Corporation and the National Provident Fund. The investment policy of these institutions is considered in detail in this section.

These sources of supply are not static, they tend to change over the years. At one point of time the insurance companies may lead the field as investors in local authority stock while a few years later the small lender may have captured their position. Different factors have different effects upon different lenders. Thus trading banks are more likely to be affected, as lenders, by economic fluctuations than are say, insurance companies. Insurance is now socially and economically desirable and persons will take out life and fire insurance as a prime necessity in business management and irrespective of the prevailing economic conditions. Insurance companies also possess an advantage in that they can frequently exert pressure upon a potential borrower (especially a house property mortgagor) by refusing to lend money unless they have a policy as collateral security. In times of market stringency the state lending institutions, and especially the National Provident Fund, assume a greater degree of importance. The National Provident Fund is to a large extent a lender of last resort.

It has been stated elsewhere that the authorities prefer to raise loans with an amortisation period as long as possible so that the annual repayments may be kept as low as possible. Although this is the case as far as demand for capital is concerned when we come to consider the supply of capital it is desirable to have loans upon as short an amortisation period as possible.

"The Board also wishes to draw the attention of local bodies to the desirability, under present conditions, of shortening the amortisation period for their loans wherever possible. By so doing they will help to swell the volume of money becoming available from their maturing debentures or their sinking fund contributions for reinvestment in new projects."

(Annual Report of the Local Authorities Loans Board)

It is possible to visualise a permanent 'pool' of funds being established into which would be paid all local authority loan repayments and from which the authorities would draw when they required money. Such a 'pool', to borrow a term from the natural sciences, would be in a constant state of 'dynamic equilibrium'. This state would only be possible if loan repayments were equal to or exceeded borrowing and would depend upon the fund being reserved exclusively for the use of local authorities. Table No C..1 shows the amounts uplifted against the amounts repaid. In 1953 the difference between the two was about 7.6 million ; in 1958 the difference was 17.4 million while in 1963 it had risen to about 20 million. There is certainly no indication at the present time that the annual amount repaid will equate to the annual amount uplifted.

Table No C..2 (part 1) sets out in summary form the sources of funds raised. The steadily rising amount that is made available by the National Provident Fund is clearly evident while it can be seen that the amount that is coming from the State Advances Corporation, which is increasingly turning itself into a specialised lender, is tending to decline. The small lender is retaining a pre-eminent position but the insurance companies are also trending down while local authority investment in the issues of other local

Table No C..1

Amounts Uplifted As Against Amounts Repaid

£ millions

Year	Amount uplifted	Amount repaid
1953	11.6	4.0
1954	16.6	4.7
1955	12.8	5.5
1956	15.0	5.1
1957	20.4	6.6
1958	24.4	7.0
1959	22.7	7.4
1960	30.0	8.6
1961	26.9	8.7
1962	21.1	10.0
1963	29.4 *	9.5 *

* estimate only

(The above table was compiled from figures contained in the Report on the Local Authority Statistics of New Zealand - Department of Statistics; and the 1963 Report of the Local Authorities Loans Board).

authorities is remaining fairly constant. Other sources contribute little and are likely to remain small investors in the local authority sector. Thus we could summarise by saying that insurance companies and the other institutions, excluding the National Provident Fund, are declining as investors in this sector while the gap is being filled by increased investment from the National Provident Fund and the private investor.

Parts 2 to 8 of Table No C..2 show an interesting set of figures. They are, however, of limited value because they refer only to one quarter of one year. Later and more broadly based figures along the same lines have not been prepared and the figures shown seem to have been drawn up specifically for the use of the Royal Commission on Local Authority Finance. These tables are designed to show differences in the sources of supply as between authorities of differing sizes.

Looking at the figures shown for counties we find a number of significant features. One feature is the relatively small amount raised by counties as compared with other authorities. We see that counties with incomes between £100,000 and £200,000 raised an amount of £142,000 out of a total amount raised by counties of £328,000 but the great bulk of the counties would fall into this income group. Counties with incomes of less than £50,000 obtained 33% of the total amount that they raised from the State Advances Corporation; counties in the next wealthiest groups raised 8%, 32% and 16% respectively of the total amounts that they raised from this source, while counties overall gained 21% of the total amount that they raised from this source. The bulk of this finance would have been supplied for rural housing purposes which is a fairly prevailent item of expenditure especially among the smaller more rural counties. Finance for this purpose is made available by the State Advances Corporation at a reduced rate of interest.

Percentages of total amounts raised from the National Provident Fund show a steady trend downward as the counties increase in size, thus 44%, 31%, 27%, and 7% respectively. We note that there is a similar trend in the figures for boroughs and power boards. Harbour boards raised nothing at all from this source while hospital boards raised very little. This demonstrates fairly decisively the National Provident Fund's role as a lender of last resort, assisting those authorities which are unable to raise finance from other sources.

Hospital boards were successful in raising a substantial portion of their finance from private investors but harbour and power boards also obtained a fair portion of their borrowings from this source. This tends to indicate the 'glamour appeal' attached to these authorities. It is seen that the larger harbour boards tended to gain a greater portion from insurance companies while the smaller boards tended to get more from private investors. This is probably accounted for by a few very large issues from the major boards which were too big to be floated upon the open market. In the case of power boards the portion obtained from private investors increased as the power boards increased in size.

We must now go on to consider in more detail the various sources from which the authorities obtain their funds and this will involve a study of each source in turn.

THE SOURCES OF FUNDS RAISED

£ millions

Source of Funds	Amount Raised to 31 March 1960	1961	1962	1963
State Advances Corporation	2.01	1.79	0.62	0.93
National Provident Fund	2.87	3.95	4.27	6.44
Insurance Companies and Other Institutions	9.73	9.50	3.96	4.92
Other Companies	1.77	1.11	0.40	1.28
Private Investors	11.98	8.53	8.83	14.79
Local Authority Fund	1.02	1.24	1.67	1.36
Other Sources	0.78	1.03	0.50	0.45
£ millions	30.16	27.15	20.25	30.17

(Annual Reports of the Local Authorities Loans Board 1963).

Table No C..2. (part 1)

ANALYSIS OF LOANS RAISED BY LOCAL AUTHORITIES DURING SEPTEMBER QUARTER 1957

1. Local Authorities with annual revenues under £50,000 (excluding capital receipts).

Source of Funds	Borrowing Authority							(£000)
	Counties	Boroughs	Power Boards	Harbour Boards	Hospital Boards	Fire Boards	Other	Total
State Advances Cpn.	6	44	15			10	2	76
National Provident Fd.	8	137	33			7	32	267
Insurance Coys. etc.*	3	37			10	67		117
Private Investors "	1	85		1				87
Total for Quarter	18	352	48	1	10	84	34	547

* Includes savings banks, trust companies, building societies and trading banks.

" Includes some public issues where sources were not shown.

Table No. C..2. (part 2)

2. Local Authorities with Annual Revenues between £50,000 and £100,000 (excluding capital receipts)

Source of Funds	Borrowing Authority			($000)
	Counties	Boroughs	Power Boards	Total
State Advances Corporation	8	49		56
Local Authorities	3			3
National Provident Fund	30	42	55	127
Insurance Companies *	43	70		113
Other Companies		4		4
Private Investors "	11	12	6	29
Other sources		9		9
Total for Quarter	95	185	61	341

* Includes savings banks, trust companies, building societies, and trading banks.

" Includes some public issues where sources were not known.

Table No. C..2. (part 3)

3. Local Authorities with Annual Revenues between £100,000 and £200,000

Source of Funds	Borrowing Authority					(£000)
	Counties	Boroughs	Power Boards	Harbour Boards	Hospital Boards	Total
State Advances Corpn.	46		15	35		96
Local Authorities	9					9
National Provident Fund	39	87				126
Insurance Companies*		55	47		95	197
Other Companies				2		2
Private Investors "	48	52	53	193	14	360
Other Sources				17		17
Total for Quarter	142	194	115	247	109	807

* Includes savings banks, trust companies, building societies, and trading banks.
" Includes some public issues where sources were not shown.

Table No. C..2. (part 4)

4. Local Authorities with Annual Revenues between £200,000 and £500,000 (excluding capital receipts)

Source of Funds	Borrowing Authorities					(£000)
	Counties	Boroughs	Bridge Athy. & Urban Drainage Boards	Power Boards	Harbour Boards	Hospital Boards	Total
State Advances Corpn.	12	11		18			41
Local Authorities		1		3	28		32
National Provident Fund	5	1	7	45			58
Insurance Companies etc. *	48	64	632	35	285	10	1,073
Other Companies		18	47		51	16	132
Private Investors "	8	152	332	311	133	100	1,036
Other Sources			10		142		152
Total for Quarter	73	246	1,028	412	639	126	2,523

* Includes savings banks, trust companies, building societies and trading banks.

" Includes some public issues where sources were not shown.

(Note for convenience the urban drainage boards have been included in this section; their 1955-56 revenues ranged from £500 to £350,000.)

Table No. C..2. (part 5)

5. Local Authorities with Annual Revenues exceeding £500,000 (excluding capital receipts)

Source of Funds	Borrowing Authorities					(£000)
	Boroughs	Power Boards	Harbour Boards	Hospital Boards	Urban Transport Boards	Total
State Advances Corpn.	25					25
Local Authorities	177	3	20			205
National Provident Fund	22	90		15		127
Insurance Companies *	533	60	281	21	10	904
Other Companies	66	1		4		71
Private Investors "	478	253	51	376	41	1,197
Other Sources '	44	10		31		85
Total for Quarter	1,345	422	352	442	51	2,613

* Includes savings banks, trust companies, building societies, and trading banks

" Includes some public issues where sources were not shown.

Table No. C..2. (part 5)

6. All Local Authorities.

Source of Funds	Borrowing Authorities				(£000)
	Counties	Boroughs	Power Boards	Harbour Boards	Hospital Boards
State Advances Corporation	71	128	47	35	
Local Authorities	12	179	11	48	
National Provident Fund	82	339	223		15
Insurance Companies etc. *	94	758	142	566	136
Other Companies		87	1	53	18
Private Investors "	69	781	622	377	489
Other Sources		53	10	159	31
Total for Quarter	328	2,325	1,056	1,238	689

*Includes savings banks, trust companies, building societies, and trading banks.

"Includes some public issues where sources were not known.

Table No. C..2. (part 7)

6. All Local Authorities (continued)

Source of Funds	Borrowing Authorities				(£000)
	Fire Boards	Bridge Authy. & Urban Drainage Boards	Urban Transport Boards	Other	Total
State Advances Corporation	10			2	293
Local Authorities					250
National Provident Fund	7	7		32	705
Insurance Companies etc.*	67	631	10		2,404
Other Companies		47			208
Private Investors "		332	41		2,711
Other Sources		10			261
Total for Quarter	84	1,027	51	34	6,831

* Includes savings banks, trust companies, building societies, and trading banks

" Includes some public issues where sources were not shown.

Table No. C..2. (part 7) - continued

7. The total distribution according to size of local authority of the funds raised from each source was...

Size of Authority by Revenue	State Advances Corporation	Local Authorities	National Provident	Sub-total
1. £0 - £50,000	76		267	343
2. £50,000 - £100,000	56	3	127	186
3. £100,000 - £200,000	96	9	126	230
4. £200,000 - £500,000*	41	32	58	131
5. Over £500,000	25	205	127	357
	293	250	705	1,248

* Harbour Bridge Authority and urban drainage authorities included here for convenience.

Table No. C..2. (part 8)

7. The total distribution according to size of local authority of the funds raised from each source was... (continued)

Size of Authority by Revenue	Insurance Companies etc.*	Other Companies	Private Investors"	Other Sources	Total
1. £0 - £50,000	117		87		547
2. £50,000 - £100,000	113	4	29	9	341
3. £100,000 - £200,000	197	2	360	17	807
4. £200,000 - £500,000	1,073	132	1,036	152	2,523
5. Over £500,000	904	71	1,197	85	2,613
	2,404	208	2,711	261	6,831

* Includes savings banks, trust companies, building societies, and trading banks.

" Includes some public issues where source was not shown.

' Harbour Bridge Authority and urban drainage authorities included here for convenience.

(Parts 2 to 8 of Table No. C..2 were taken from the Report of the Royal Commission on Local Authority Finance.)

Table No. C..2. (part 8) - continued

The Small Lender

The small lender has retained his pre-eminent position as a contributor to local authority stock and in the year ended 31 March 1963 he contributed some 49% of the total amount raised. The other parts of Table No. C..2 show the distribution of the small lender's contribution in the September Quarter 1957. Boroughs, power boards and hospital boards obtained more finance from the small lender than from any other source in this period and the larger authorities tended to obtain a greater proportion of their finance from this source than did the smaller bodies. This latter point is probably accounted for by the fact that the larger authorities would have more reason to resort to public issues than the smaller bodies and would tend to be more successful at raising money on public issue. Unfortunately no figures are available which set out the sources of loan finance as between rural and urban authorities. It is probable, however, that such figures would show that as far as the smaller authorities are concerned it would be mainly rural bodies who drew finance from the small lender. As stated earlier many of the smaller authorities in the larger urban areas are forced to resort to the institutions to obtain finance because of opposition from the larger authorities.

In many respects the private investor does not represent a very satisfactory source of funds. Most of the finance contributed by the small lender comes from certain fairly well defined groups. The farming community provides a considerable amount of finance to the smaller counties and would doubtless figure large in the lending to the power boards (which are essentially rural) and possibly to the harbour boards. Being authorised trustee investments local authority loans attract a considerable amount of finance from such things as family trusts and education foundations. Included among the private investors would be investment from many different clubs and societies, e.g. the New Zealand Rugby Union has made some finance available for the purpose of erecting grandstands and setting out sports grounds. Quite a number of small investors prefer to purchase stock upon the stock exchange rather than invest in an initial issue. This can have the double advantage in that it may mean a shorter maturity period together with (in some instances) a higher return. This could be the case in times of great market stringency when difficulty is experienced in disposing of stock and sellers are prepared to unload at a considerable discount. But some institutions prefer to invest in initial issues merely to assist the authorities even when they could obtain a higher return by purchasing old securities.

One of the major disadvantages of the small investor from the point of view of the local authority is that generally, he is able to place only a very small amount in an issue and this tends to add somewhat to the administrative expenses involved in the issue. At the same time the open market means that expenditure will be involved in advertising but at the same time expenditure by way of procuration fees will be saved. But the biggest problem associated with raising money from the small investor is the term aspect. A small lender does not usually like to have his finance tied up for lengthy periods of time. Thus he will attempt to invest for as short a term as possible but at the same time to obtain the highest possible return. A corporation, on the other hand, has perpetual existence and does not have to be concerned with any difficulties which might arise in respect to the liquidation of long term investments upon the death of the investor.

But a further feature associated with the small lender is that he is not spread evenly throughout the country. A local authority in the Auckland or Wellington areas would probably experience considerable difficulty in raising finance from this source while a small borough set in a farming district, a rural power board, or a backwoods county would find that it could raise quite a steady amount from the small lender. In considering investment by institutions the geographical location of the borrower is not generally an important matter but the small lender is at his best in those districts where the level of individual income is higher than the national average. Table No. C..2 tends to confirm this contention. From part 7 of the Table we can calculate the amount raised from various sources as a percentage of the total amount raised for each of the various classes of authorities. We see that the hospital boards which are a combination of rural and urban bodies lead the field with 70.9% of the total amount raised coming from the small investor. They are followed by the electric power boards with a total of 58.9% raised from this source. Power Boards are essentially rural authorities.

The large amount raised from the small lender by the hospital boards leads us to a further interesting characteristic of the private investor and that is his subjection to 'glamour appeal'. A small lender is swayed by the thought of a new library or town hall while the prospect of a new sewerage system will hardly excite him at all. The security backing of a loan for sewerage works would of course be no different from that for any other loan. An institution is not subject to pressures of this nature.

Local patriotism is a feature of the private investor. Provided the investment opportunities are offering there he will tend to place funds in the area where he resides or where the bulk of his assets or interests are situated. Once again the institution is free from this characteristic. The trustee savings banks are local institutions and they certainly invest the bulk of the funds that they have available in their own areas; this indeed has been one of the major arguments advanced by those seeking to get these institutions established in the smaller areas. On the other hand the insurance companies place their investments upon a nation wide basis. Most of the investment policy of the individual insurance companies is directed from their Head Offices the bulk of which are situated in Wellington, but their investments are not by any means limited to the localities in which their offices are situated. The National Provident Fund and the' State Advances Corporation also operate upon a nation wide basis. It should be pointed out that institutions are subject to some dis-advantages not possessed by the small investor e.g. many insurance companies prefer to place their funds into the avenues from which they obtain their business. This applies also, although to a much lesser extent, to the National Provident Fund. Some institutions, e.g. the State Advances Corporation, will only lend money for certain set classes of projects.

As a large proportion of the funds contributed by the small lender are derived from the farming community this source of finance is likely to be very sensitive to changes in the prices paid for farm products. Insurance on the other hand is an economic and social necessity and people will tend to insure despite the state of the economic barometer. Thus insurance companies tend to be somewhat more immune to fluctuations in income than is the small investor. At the same time institutions such as the National Provident Fund and the State Advances Corporation, which are subject to Government control, can frequently operate against the market trends and thus help to iron out fluctuations. The small investor is of little value in this respect.

Local Authority Fund

The local authority fund figures show the volume of finance contributed to local authority loans by other local authorities, i.e. inter authority lending. This is carried out at present upon a fairly limited scale and in most cases the lender is concerned with investment mainly for the purpose of building up such things as depreciation and renewal funds. In some respects the practice of one authority investing in the stock of another is not to be commended because if it was carried out upon anything like a widespread scale it would mean that large amounts of local authority debt were secured merely upon the rating potential of other local authorities.

In the case of territorial authorities general rating revenue is assessed merely to cover the estimated expenditure of the particular authority for the year in question and a local authority could not collect rates simply for the purpose of investing the money. In respect of the trading undertakings (e.g. electrical works) of the territorial authorities it is necessary to provide for the depreciation and renewal of assets and to this end sections 133 and 140 of the Municipal Corporations Act 1954 enable the establishment of depreciation and reserve funds for each such undertaking. Sections 128 and 129 of the same Act enable a municipality to set up fire and accident insurance funds and grant a general power to invest the funds. This would almost certainly give local authorities the power to invest these moneys in local authority stock.

In the case of the revenue producing authorities the scope for the general investment of surplus funds is much wider. Thus for example section 53 of the Harbours Act 1950 grants to harbour boards a general power to invest trading profits and analogous powers have been granted to power boards.

At the present time this source of funds is very limited but as the major revenue producing authorities work off their present debt they should have increasing amounts available for investment and large amounts of this will doubtless go into the debenture and stock of other local authorities. Unlike the territorial authorities which are forced to rely mainly upon rating income there is virtually no limit to the profit which a trading authority can make and it is quite likely that in the near future we will see an increasing volume of finance flowing from the trading authorities to the territorial authorities. This could mean that other sources of funds which at present supply local authorities could be left free to invest their money in other sectors of the market.

It would be possible for a territorial authority to invest profits from its trading undertakings in its own debentures which had been issued for a loan for a general purpose, i.e. a purpose not connected with the particular trading undertaking. This would mean that the investments of the trading undertaking would be secured upon the rating potential of the same local authority. This situation would be even more undesirable than a territorial authority investing in the loan issues of another territorial authority.

The National Provident Fund

The National Provident Fund plays a vital and unique role in the field of local authority lending. Although ostensibly an independent institution, established under its own empowering act it is, in point of fact, very subject to Government policy and as such is in a position to cut across normal lending trends and to act as a lender of last resort.

The Fund was established in 1911 with a dual purpose, i.e. to provide pensions and subsidiary benefits for members of the general public and to provide superannuation schemes for members of local authorities and other statutory bodies. The Fund is administered by a Board comprising the Minister of Finance as chairman and six other members. The present legislative authority is to be found in the National Provident Fund Act 1950, section 6 of which enables the Fund to invest in local authority securities. Section 6 of the 1955 Amendment Act empowers the Fund to act as sinking fund commissioners to local authorities. The first few sections of the 1955 Act are also of vital importance to us as they establish the local authority investment 'pool' which enables authorities to invest, upon short term, those funds which they do not immediately require, e.g. surplus loan moneys. This institution of the Fund has developed into a vital component of the local authority capital market.

The investment policy of the Fund is determined by a committee of the Board known as the investment committee. The activities of the committee initially determine the flow of funds from the Fund to the local authorities. The moneys available for the Fund for investment are derived from its general superannuation activities as well as from the contributions to the 'pool account'.

The lending of the 'pool account' funds have presented the investment committee with a number of problems. Table No. C..3 (part 1) shows the composition and growth of the 'pool' over the years since its establishment in 1956. It can be seen that 'surplus loan and miscellaneous moneys' amount to more than one half of total investments in the 'pool'. Depreciation fund, sinking fund, and reserve fund moneys, are in general invested with the Fund upon a more permanent basis than are surplus loan moneys and may therefore be let out to local authorities for fairly long terms. But surplus loan moneys are frequently invested at call and are liable for heavy repayments in accordance with the constructional progress of the various loan projects. For this reason it is necessary for the Fund to invest the bulk of these moneys in readily negotiable short term securities. In 1962 there were some four hundred local authorities contributing to the 'pool' and the Fund makes a careful inspection of the accounts of all local authorities with the object of ascertaining whether they have any surplus funds (e.g. deposits with the Post Office Savings Bank) which could be diverted to the 'pool'. The sinking fund activity of the Fund is also increasing and as at the 31 March 1962 the Board had been appointed the sole commissioner of 436 different sinking funds securing the repayment of loans totalling £14.9 million.

The investment policy of the Fund is perhaps best summarised

Table No. C..3 (part 1)

The Growth and Composition of the National Provident Fund
Local Authority Pool Account 1956-63

	1956	1958	1961	1962	1963
Depreciation Funds	108,163	306,595	497,431	580,043	658,838
Sinking Funds	39,515	209,220	905,708	1,414,762	2,092,323
Reserve Funds	1,231,667	2,868,411	9,627,493	11,628,585	17,010,931
Loan & Miscellaneous Moneys	2,063,554	4,756,662	10,326,887	9,815,459	16,657,804
£	3,442,899	8,140,888	21,357,519	23,438,849	36,419,896

(Annual Reports of the National Provident Fund Board 1956-63)

Table No. C..3 (part 2)

Activities of the National Provident Fund Investment Committee for the Year Ended 31 March 1963

	Number of Applications	Amount applied for	Amount approved
Cities and Boroughs	135	5,697,685	3,171,755
Counties	60	1,842,800	1,747,300
Electric Power Boards	19	588,680	518,680
Fire Boards	8	71,900	69,450
Harbour Boards	13	1,726,940	1,529,410
Hospital Boards	13	1,227,370	1,052,370
Others	18	649,750	324,750
	266	£11,805,125	£8,413,715

(Annual Report of the National Provident Fund Board 1963)

Table No. C.,3 (part 3)

Investments of the National Provident Fund in Local Authorities Securities 1958-1963

1958	£18,461,888
1960	21,156,241
1961	23,505,052
1962	28,236,439
1963	33,297,838

(Annual Balance Sheets of the National Provident Fund Board)

Table No. C.,4

Advances upon Hypothecation made by the National Provident Fund Board

1958	£397,000
1961	260,000
1962	432,200
1963	690,000

(Annual Reports of the National Provident Fund Board 1958-1963) in the following words taken from the 1958 Annual Report of the Fund -

> "With loan applications far exceeding moneys available for lending it has been necessary for the committee to give preference to higher priority projects and in some degree to differentiate in favour of minor local authorities. Projects financed during the year cover a very wide field and include sewerage, drainage, water and electrical reticulation, streets and roads, housing and buildings, etc."

The investment committee therefore tends to accord preference to those authorities who have urgent and necessary works to carry out and who are not able to obtain the necessary finance themselves from other sources. This includes, of course, generally, the smaller authorities. Reference to Table No. C..2 will show the extent to which the Fund has been successful in implementing this policy.

There is also evidence to the effect that some preference has been accorded to authorities who support the 'pool'. The following statement appeared in the 1962 Annual Report of the Fund -

> "With loan applications exceeding moneys available for lending it was still necessary for the committee to adopt some measure of priority which was generally in the order of necessity of loan project, ability of the local authority to raise its own finance, and the degree of its investment support to the pool."

It appears that some of the larger authorities which are generally fairly successful upon the market make a point of investing available moneys with the Fund because they know that the Fund will then be more likely to take up the few maturities which they are not able to dispose of upon the open market. These are frequently those maturities for the year just below that at which a higher interest rate sets in. Thus the Fund effectively fulfills the function of a lender of last resort in that it takes up in full the issues of the smaller bodies who are unable to sell upon the open market while at the same time it takes up the unsold maturities of the larger who have succeeded in selling the rest of the issue upon the open market.

Insurance Companies

The insurance companies occupy a crucial position in the capital market. It is not possible to examine satisfactorily the investment policy of insurance companies in respect to local authorities without possessing at least some knowledge of their general investment policy. The bulk of these companies are based overseas and many of them retain only branch offices in New Zealand. Some of the larger companies possess assets worth hundreds of millions of pounds.

A major factor in the investment policy of the life companies is that they do not suffer to any great degree the fluctuating liquidy problems which have to be faced by other financial institutions e.g. trading banks. In any sophisticated society insurance, even when a state of economic depression prevails, is now a social and economic necessity and this fact together with the constant maturing of past investments has ensured a steady flow of funds into the life companies. In view of thisthere is no definite reason why the life companies should be concerned about retaining large cash reserves and this has meant that the companies tend to invest long term. But, as with other investors, the rate of interest is a fairly dominant factor in determining the period of investment. If the companies are of the opinion that the rate on local authority stock is at its maximum they will, of course, invest long term. If, however, they believe that the interest rate will trend upward they will tend to invest short term or place their funds into some other short term investments apart from local authority securities. But in general their investment in local authority stock has tended to be long term investment.

Another factor which has exerted some influence in insurance company investment has been the desire to retain custom meaning that companies will tend to invest with those authorities which do business with them. This used to be especially applicable when the life companies operated staff superannuation schemes for various local authorities but these schemes are now generally run with the National Provident Fund. However, there is still a tendency for the fire insurance companies to place their investments with those authorities which do their fire insurance with them.

It appears that direct pressure from the Government has maintained a fairly steady stream of investment in Government securities and it is possible that this has inhibited somewhat the ability of the companies to place their funds in local authority stock.

Insurance companies have made much of the 'public interest' aspect of their investment. They point out that they frequently place their funds in the manner that will best assist the national economy or the welfare of some local community. It is possible that these altruistic motives may have induced some investment in Government stock and perhaps house mortgages but it is very difficult to obtain specific examples of companies investing in local authority securities for no other reason than that that particular placement would assist the national economy or be of benefit to the local community.

In their investment pattern the companies exhibit the concept of the 'portfolio of securities' i.e. they attempt to maintain a range of investments extending from the traditional strictly gilt edged through real property mortgages to company debentures, convertible notes and loans against life interests. An examination of the balance sheet of any substantial life company almost invariably shows the familiar pattern of investment. The following is the investment range of the 'Provident Life Insurance Company' taken from that company's 1958 balance sheet. This Company is incorporated in New Zealand.

Government Stock	£1,039,658

Local Authority Stock	£1,872,645
Company Debentures	410,670
Registered Unsecured Notes	23,647
Company Shares	231,255
Loans on Mortgage	1,494,134
Loans on Policies	185,618
Loans on Life Interest	3,645

But what determines the form of this 'portfolio of investment'? The broad framework is set by the traditional investor's policy of maintaining the maximum of security with the maximum of income. Long periods of inflation and a cheap money policy have had the effect of encouraging the companies to shift from the gilt edged into the higher yield and capital gain class of investment and also into real estate. The post war years therefore have seen a steady trend away from the gilt edged investment and in this respect the local authorities have suffered somewhat more than the Government because they are not in the same position to exert pressure upon the companies. Table No. C..5 sets out this position. But although the companies would like to invest less of their current funds in local authority stock the indications are that they would not like to see this type of security deleted entirely from their balance sheets. Over the war years the amounts held in gilt edged as a percentage of total investment remained at a very high level and this raises the question of investment opportunity. Clearly the major cause of high gilt edged investment in those years was lack of opportunity and a general inability to find other more lucrative outlets for the funds.

But even if other avenues are available it is still possible that opportunity may play a part in directing investment to the gilt edged field. In terms of the New Zealand capital market the insurance companies are very large institutions and they frequently have falling due to them very substantial amounts (sometimes in excess of one million pounds) which require to be reinvested. The Government and the local authorities provide just about the only outlets in New Zealand for sums of this magnitude. It can be realised that if an amount of say, one million pounds, falls due to a company it is very much to the advantage of that company if it can reinvest that amount immediately in one particular issue as the need to break the sum up into a number of smaller investments would almost inevitably mean greater administrative expenses. The Government has taken advantage of this by making use of conversion loans which enable an investor to place his funds back into another Government loan immediately one maturity falls due. The frequent use of renewal loans in recent years could enable local authorities to take advantage of this point. Just a word in passing about administrative expenses; it is of interest to note that the expense involved in servicing the various classes of investments appears to have been a factor in inducing some of the smaller New Zealand companies to retain a greater proportion of their investments in government and local authority stock than their bigger brothers. It can be realised that in the case, of say, loans on mortgage, considerable expense is involved in such items as interviewing the applicant investigating the security, correspondence and legal fees not to mention the cost of foreclosure, should this be necessary. Lending to limited companies can also be expensive as it generally involves extensive financial investigation and legal work such as the searching of articles of association. On the other hand lending to local authorities is simple and inexpensive as with the use of inscribed stock the interest and instalments falling due are collected by the Reserve Bank and merely credited to the company's account.

Another point in respect to opportunity is the term aspect. The local authorities provide one of the few avenues for very long term placements and provided the interest rate is right this is an asset to the companies in that it affords them a stable income over a long period of time. The issues which have been put on the market with terms in excess of the normal twenty-five years have indeed proved fairly popular with insurance companies. Furthermore long term investment enables an insurance company to take the procuration fee which authorities are permitted to offer as an inducement for placements of substantial amounts for lengthy periods.

In those times when the Loans Board permits underwriting the companies rarely deal direct with individual authorities but act as sub-underwriters. This means that in return for the payment of part of the underwriting fee, calculated over the full amount of an issue, an insurance company will agree to take up that portion of an issue which cannot be disposed of on the open market. This practice has assisted in making local authority issues more attractive to the companies and indeed this could be looked upon as floating the issue at a discount.

But in spite of the several advantages which local authority investment offers to the insurance companies the higher yield security has gained ground and this raises the question of the future trend of insurance company investment in the local authority field. If present economic trends continue and investment opportunity in other fields remains at a high level it seems probable that the percentage of total investment held in local authority stock will fall still further. But the need for the companies to obtain a steady income over a long period and thus to hold a stable long term base within their portfolios of investment will ensure that investment in this field does not entirely disappear. Thus the future could see insurance company investment in this sector drop still further and then remain reasonably constant at some low level. Whether that level would be high enough to supply sufficient long term finance to the authorities will be dependant upon the trends of future capital works.

It is possible that increased investment from the Government insurance offices could at least partially offset decreased investment from the other offices. Investment by the Government Life Insurance Office in local authority securities over the past few years is as follows

(figures taken from the New Zealand Official Year Book 1964 page 834 - figures are in thousands)

1959	£8,031
1960	9,099
1961	10,834
1962	11,786
1963	12,220

It is possible that increased investment from this quarter would not come about in the absence of Government direction or pressure upon the offices concerned i.e. the State Fire Insurance Office and the Government Life Insurance Office.

Insurance company investment is of considerable importance to the authorities in that it provides the major source of large and long term placements. In some cases, because of long term investment by insurance companies, an authority which requires a very substantial amount for a lengthy period may have more chance of raising it than it would of getting a very much smaller amount upon the open market.

Table No. C..6 sets out the amounts held as investments in local authority stock by the life offices for the years shown. The downward trend over the past few years is clearly evident.

Trustee Savings Banks

New Zealand is now all but covered by a network of trustee

Table No. C..5

Life Insurance Companies - Local Authority Investment as a Percentage of Total Investment

	1938	1946	1950	1961	1962	1963
Local Authority Securities	36.2	26.70	24.92	17.77	15.94	14.44
Government Stock	18.7	42.36	40.05	18.85	17.87	18.52
Other Investments	34.1	30.94	34.93	63.38	66.19	67.04

(New Zealand Official Year Book)

Table No. C..6

Amounts Invested by Life Insurance Companies in Local Authorities Securities.

	(£000)
1937	18,201
1946	21,235
1950	26,904
1955	32,332
1960	40,621
1961	48,900
1962	48,199
1963	47,598

(New Zealand Official Year Book)

savings banks. Many of these have sprung up within the last few years. These historic institutions owe their success largely to the fact that they are locally based and sponsored. They possess the characteristic that the funds which they have available for investment can be invested in the same local district in which the bank operates. The banks have therefore been of considerable assistance to the local authorities of the areas in which they are situated. The banks have been somewhat more successful than their nearest rival, the Post Office Savings Bank, in extracting savings from the public. This has been brought about by their play upon local interest and the vigorous publicity policies which they follow. Several of the early trustee banks in New Zealand were forced into liquidation by competition from the Post Office Savings but all the banks which are in existence at the present time appear to be prospering.

The Trustee Savings Banks Act 1948 places fairly substantial restrictions upon the investment outlets of the banks. The banks have been granted a Government guarantee. This has been considered necessary to afford the small investors who deposit their savings with the banks the maximum of protection. At the same time however, the Act requires the banks to retain at least fifty per cent of their total investments in Government stock. As the banks become more securely established it is reasonable to assume that this requirement will be relaxed and this could release a fairly large volume of funds for investment in local authority stock. A further point is that at present the Act requires the banks to keep substantial cash reserves and the reduction of these could also mean that funds would be released for investment in the local authority sector. Table No. C..7 shows investment by trustee banks in Government stock and local authority stock together with the total amount held in investments. Several new banks have been established since 1963.

State Advances Corporation

The State Advances Corporation is a public corporation operating under the provisions of the State Advances Corporation Act 1934-35. In previous times it was a general lending agency for local authorities but this function has since been taken over by the National Provident Fund and the Corporation's activities are now confined to the lending of finance for housing and associated projects. The Act grants the Corporation all necessary powers and the Corporation usually lets its finance out at a rate of interest somewhat lower than the ruling market rate.

The Corporation lends for clearly defined purposes. Pensioner housing projects are a major lending avenue for Corporation funds. The local authorities are entitled to a subsidy per unit from the Department of Health and the Corporation lends the balance of the finance required to

Table No. C..7

Investments Held by the Trustee Savings Banks

(£000s) Figures as at 31 March 1963

	Government Stock	Local Authority Stock	Total Investments
Auckland	31,595	7,575	61,135
Waikato	2,955	362	4,986
New Plymouth	3,861	103	8,580
Hawkes Bay	616	16	709
Hokitika	359	31	848
Canterbury	1,500	40	1,749
Dunedin	5,371	649	12,213
Southland	5,750	2,617	12,515
Total	52,007	11,393	102,735

(New Zealand Official Year Book 1963)

complete the project. The rate at which this money is made available is at present (1964) $3\frac{1}{2}\%$.

The Corporation also provides finance for the erection of county dwellings, under the provisions of the Rural Housing Act 1939. Finance for this purpose is let out to counties at a rate (at present $4\frac{1}{4}\%$) somewhat below that ruling upon the market and the authority then relends the money to farmers for the purpose of erecting dwellings.

Community housing and slum clearance are also within the Corporation's activities but as yet only limited amounts have been invested in loans for these purposes.

National Roads Board

Section 38 of the National Roads Act 1953 enables the National Roads Board to make advances to local authorities for the purpose of providing a portion of the cost of construction of works which have been subsidised by the Roads Board.

Advances under this Section are not frequently made and the amount outstanding at any one time has never exceeded forty thousand pounds. As the making of advances under this Section means less finance available for the general activities of the Board only limited amounts have been made available.

Overseas Borrowing

Since its establishment in 1926 the Loans Board has adopted the policy of requiring all loans to be raised in New Zealand. But prior to the establishment of the Board many authorities borrowed quite freely overseas, e.g. the Dunedin City Council and the Otago Harbour Board. Even some quite small authorities tried their hand at borrowing in London, e.g. the Matamata County in 1922. Since the establishment of the Loans Board the total amount of debt domiciled outside New Zealand has steadily declined. Thus

£(m)	London	Australia
1931	17.53	8.57
1940	12.28	2.26
1950	5.03	.36
1960	1.4	.20
1961	.7	.20
1962	.5	.20
1963	.5	.20

(Annual Reports of the Local Authorities Loans Board)

It seems most unlikely that the New Zealand Government will permit local authorities to borrow overseas for some time to come at least. The disadvantages of permitting local authorities to borrow overseas may be set out as follows.

(a) Borrowing on most overseas markets is strictly controlled e.g. in the case of the United Kingdom it would be necessary to obtain the approval of the United Kingdom Treasury. A flow of applications from local bodies would mean that some order of priority would have to be set. The United Kingdom Treasury could not equitably set this and it would have the unenviable task of differentiating between the central government and the local authorities of one country. As the New Zealand Government has itself been a heavy borrower overseas in recent years it would, in effect mean that the Government and the local authorities were in competition.

(b) Servicing loans on overseas markets i.e. arranging brokers and underwriters would be very expensive.

(c) The individual authorities would hardly be known to the investors upon the overseas market and it may be very difficult to get the issues floated at par. It is of note that in the 1920s the loans of some New Zealand bodies sold for as low as £90 per £100 of face value of stock on the London market.

(d) The London market is already heavily committed and it has been called upon in recent years to supply a steady flow of capital to many Commonwealth Countries especially the newly independent African States.

(e) A fair drain upon overseas funds would be necessary to provide for the annual servicing of the loans. This could be a problem in those times when there is a downward trend in the level of export earnings.

(f) A failure by one local authority would tend to bring the New Zealand Government into disrepute with the London lender.

If authorities are to borrow overseas it would be advisable for them to borrow through the Government. On the other hand if a local authority finance corporation was established in New Zealand this could provide a channel through which overseas borrowing could be carried out as such an institution would carry much greater weight in an overseas market than any individual authority.

THE FLOW OF CAPITAL

The presence of an adequate supply of capital is no guarantee that the local authorities will, or will all, be able to borrow sufficient capital for their requirements as quite apart from the supply of capital numerous forces affect the flow of finance to the local authority sector. Opposition upon the market is one such factor that can inhibit the flow of capital and this can come from other sectors of the market as well as other local authorities. It has long been an important characteristic of the market that some types of local authorities are able to obtain finance with much greater ease than others. At the same time various devices are sometimes resorted to in order to facilitate the flow of capital. Some of these have been specifically authorised by the Loans Board while others are merely, shall we say, gimmicks used by individual authorities to assist their market activity. An ingenious town clerk can often raise finance upon a market that would deter lesser men. These matters must now be considered.

Inter Local Authority Competition

Competition for capital as between different local authorities assumes three distinct forms. Firstly there is competition as between authorities of different class, secondly there is competition as between authorities of different size and thirdly there is competition as between different projects. Considering firstly competition as between authorities of varying classes. It has long been a notable feature of the market that some types of authorities are able to obtain finance more readily than others. Probably the most attractive class of loans to the investor are those offered by the hospital boards. These institutions are in a somewhat different position from other bodies in that they are now financed almost completely by the Government. Thus from an investors point of view hospital board stock is able to offer the same security as Government stock but can offer a higher rate of interest. In fact it could almost be submitted that hospital boards are local spending agencies of the Central Government. This situation has tended to make these issues very popular upon the market especially with the insurance companies which provide sub-underwriting facilities. But at the same time these issues have also had considerable appeal to the small lender because of a certain element of 'glamour' which seems to be associated in the public mind with hospital works.

Such has been the strength of the hospital boards upon the market that the Hospital's Association of New Zealand made submissions to the Royal Commission to the effect that should any local authority finance corporation be formed it should not raise loans for hospital purposes as in its opinion doing so would,

"(a) Lose the advantages of public sentiment towards, and support of hospital enterprises.

(b) Tend towards a decline in local energies and enthusiasm in the raising of necessary finance.

(c) Result in some loss of stimulus at present gained from inter authority competition for available finance."

In fact such has been the ability of the hospital boards to gain finance in preference to other bodies that it has been suggested that the rate of interest on hospital board stock would be set at the Government rate. However this suggestion has never been seriously pursued.

On the other hand hospital boards have experienced some difficulty in floating renewal loans. These tend to present a problem for two distinct reasons. Firstly they must be raised in one full amount as they are, of course, always required to repay a parent loan and secondly they possess no 'glamour appeal' as they can rarely be associated with some particular capital work.

Harbour boards appear to stand after hospital boards at the head of the market as far as ability to attract capital is concerned. Local patriotism also plays a large part in making harbour board issues attractive to the investing public. This has been assisted in some instances, especially in the case of many secondary boards, by pointing out to the local farmers the amount that will be saved in freight costs by having a local port. Probably the best example in recent years of a harbour board playing upon the local interest to obtain finance is provided by the Southland Harbour Board which recently raised an amount of £5 million for the construction of a new harbour at Bluff. The bulk of this sum was derived from the Southland Area. These issues were accompanied by a very intensive advertising campaign.

Some secondary boards possess rating power and are therefore in a position to use a land rate as a security backing for loan charges. This situation has been brought about mainly by shear necessity as very few secondary boards (which in general, because of lack of natural harbours, have been compelled to install more expensive works than the major boards) could have afforded to finance large scale capital development purely from their revenue earnings. These rates, however, are almost invariably associated with a specific loan and the only board which has ever managed to obtain a general rating power is the Oamaru Board. As the secondary boards increase their revenue earnings these rating powers will almost certainly disappear, and the secondary boards, like the major boards, will be forced to rely upon their assets to provide security for their loans. However, this apparent advantage that the secondary boards at present possess does not appear to have given them any advantage over the major boards in gaining capital finance.

Section 4 of the Trustee Act 1956, which sets out authorised trustee investments, presents an interesting phenomena in respect to investment in harbour board investments. Section 4 (1) (d) permits the unqualified investment in the stock of seven different boards, i.e. Auckland, Wellington, Lyttelton, Otago, Napier, Timaru and Southland, while Section 4 (1)(e) permits investment in the stock of six other boards provided the particular loan has a land rate as security backing. Thus in this instance the legislature has attached some considerable importance to the land rate as a security factor. It is of note that almost all of the very small boards are omitted completely from the section (i.e. Nelson, Oamaru and Greymouth).

The Harbours Act 1950 permits all harbour boards to levy a harbour improvement rate upon the cargo which they handle and the proceeds of this could doubtless be used to pay off loan charges.

After harbour boards boroughs and counties appear to stand upon virtually an equal footing as far as the ability to raise finance is concerned. But this does not seem to apply in those cases where boroughs and counties are in competition in a large urban area (e.g. Auckland) where, provided they are roughly of equal size, the boroughs appear to have a slight advantage. Many of the backwoods counties, because of their isolated position and lack of demand, experience practically no opposition in raising capital.

Standing right at the bottom of the list as far as ability to raise capital is concerned are the urban drainage boards. These authorities appear to experience considerable difficulty in gaining finance owing largely to the unappealing nature of the works to which they are committed and to the fact that, as they are all centered in large urban areas they are subjected to intense competition from other authorities.

Looking now at the question of the ability of a local authority to gain finance in relation to its size we see that as a general proposition it is true to say that a large body can gain finance more readily than a small one. But this point is only thrown in to relief in those areas where small and large authoritiesare competing in what is virtually the same segment of the market. This situation is of considerable importance in the Auckland Area where about three individual authorities i.e. the Harbour and Hospital Boards and the Auckland City Council, dominate the market to the exclusion of the other bodies in the area. A somewhat similar situation exists in the Wellington area where the Hutt County tends to be excluded. In the strictly rural areas this problem does not arise to any notable extent and as previously stated the 'backwoods' counties, irrespective of size, seem to experience little difficulty in obtaining finance. A further good example of a small borough being excluded is provided by the West Harbour Borough which is tucked into the northern boundary of Dunedin City. This body has experienced extreme difficulty over recent years in raising sufficient finance to cope with its sewerage problems. It is possible that investment in this authority has been inhibited somewhat by the existence of continuing speculation to the effect that the borough will amalgamate with Dunedin City.

The next point is 'glamour appeal'. Some projects undertaken by local authorities seem to possess more appeal to the public than others. As already stated local patriotism is generally kindled by hospital and harbour works but new libraries and town halls also appeal to the local spirit. On the other hand an essential but mundane project such as water supply or sewerage disposal may be very difficult to finance. This means that while a body may be able to gain finance on the market for some particular project it may not be able to obtain finance for some other project of greater essentiality. It could be pointed out that in many instances these 'glamour appeal' projects have been taken up by local interests apart from the local authority who have assisted in raising money towards the completion of the asset. These interests include such concerns as local chambers of commerce, twenty thousand clubs, progressive associations and such like. Many of the tepid swimming pools which have sprung up all over the country have been assisted in this way. But how often do we hear of a local chamber of commerce conducting a mystery envelope scheme to assist a council with the financing of a new sewerage system.

The individual initiative of the secretary or clerk of the authority can also play a big part in raising finance. Thus assessing the correct time of the year to approach the market can be of considerable importance and this may vary according to the various districts, e.g. in an area with a substantial sheep farming element it would be advisable to commence advertising just after the wool cheques have come in. It is important not to advertise at a time when the local population has substantial other commitments, e.g. income tax payments to meet. The ability to assess whether money is likely to be available in other parts of the country is also of considerable assistance. Many local authorities advertise their loan issues outside their own districts and it seems that they are generally fairly successful in attracting an inward migration of capital. However, merely indiscriminate advertising throughout the length of the country on the off chance of picking up a few pounds could prove very expensive. Before a clerk went looking for finance upon the open market in another district he would have to be certain firstly, that the money was available in that area, and secondly, that there were no locally situated authorities seeking finance at the same time. It does seem that there is some drift of capital from south to north and any larger North Island authority that advertised in the more wealthy farming areas of the South Island, e.g. Canterbury, Otago or Southland would be almost certain to pick up some money.

A further matter is the judicious use of 'tap loans' which are a very satisfactory device for maintaining contact with regular investors. Some power boards in the Auckland area adopted a practice of requiring consumers to invest a few pounds in their issues before certain services would be installed in their properties. This met with considerable opposition and at least from an ethical point of view it is quite unsatisfactory.

Placement Fees

About 1957 a system of placement (sometimes called procuration) fees was introduced. This provided for the making of a payment to an individual lender who was prepared to take up a full loan, or a substantial part of a loan, upon a long term basis. This device was designed to make local authority issues more attractive to the larger investors and to encourage long term investment. The rates of placement fees permitted were as follows.

for a 20 year term 15/- per cent

for a 25 year term 20/- per cent

for a 30 year term 25/- per cent

for a 35 year term 30/- per cent

for a 40 year term 35/- per cent

The effect which the payment of these fees has had upon the volume of capital flowing into the local authority sector is difficult to ascertain exactly. The system has probably induced some of the larger investors (e.g. insurance companies, where a very small increase in return can have a substantial influence) to invest in local authority securities but any very definite effects of the system are not evident. The one interesting feature of placement fees however, is that they provided a means whereby in effect a local authority could place an issue on the market at a discount; a practice which, according to the strict letter of the law is illegal.

Tap Loans

Local authorities which are in the habit of raising most of their finance upon the open market like to maintain contact with their regular subscribers and sometimes a practice is made of circularising all subscribers to one particular issue, upon the maturity of that issue with the view to getting them to invest in further loans. But another method of maintaining contact with regular investors is by the use of 'tap loans'. This practice involves keeping an issue open upon the market for a very lengthy period of time in order to provide an investment opportunity for regular subscribers as well as anyone else who may chance along. This ensures that a steady if small stream of finance will flow into the issue. Many loans, however will not lend themselves to this e.g. in those cases where a large amount must be obtained within a very short period of time. But the system would be very satisfactory for capital works of a continuing nature e.g. road works.

Underwriting

In the mid 1950s after a period of some twenty years the Loans Board once again permitted the local authorities to underwrite their loan issues. Underwriting is a procedure whereby the local body enters into a contract with a private stockbroker, whereby for the payment of a prescribed fee the stockbroker guarantees that the issue will be filled. This practice is very common in many overseas countries and is used for private company and government as well as local government floatations. It provides a very potent weapon for marshalling the market and diverting finance into the local authority sector, and for this reason it is almost certain that it would not be permitted in times when the market is easy. Very few broking firms have taken up the business of underwriting local authorities loans and at the present time only about three are active in this field.

It is an invariable custom to include in an underwriting contract a stipulation requiring the local authority to approach the open market and attempt to raise as much finance as it can from that source before the underwriters will contribute towards the issue. As the ability to raise money varies according to the size of the body it generally comes about that the underwriters will be called upon to find a greater proportion of the issue of a smaller authority than of a larger one. To overcome the relative disadvantage of the smaller authorities in this respect, therefore, the Loans Board has adjusted the amount that may be paid in underwriting fees to accord with the size of the local authority i.e.

major local authorities	10/- per cent
secondary local authorities	12/6 per cent
strictly minor local authorities	15/- per cent

Hence the Loans Board has here seen fit to take action to remove any disability which may be suffered by the minor authorities but only in so far as actual activity upon the market is concerned because in the ultimate the smaller body is still called upon to pay a higher fee than the larger authority.

The underwriters generally arrange for a single, or number, of large investors, e.g. insurance companies to act as sub-underwriters in consideration of them receiving part or the whole of the underwriting fee in return for the money which they provide. The sub-underwriters would, of course, take up that portion of the issue not subscribed by the public. But the actual underwriting fee paid by the local authority is payable upon the full amount of the issue and the fee is usually paid in full to the sub-underwriters. Thus in the case of an issue of £100,000, one half of which is contributed by the public, the sub-underwriters could receive an amount of 30/- per cent upon the amount that they subscribed, i.e. if the fee payable is 15/- per cent. It has been contended that in effect this amounts to an increase in the rate of interest payable to these investors and that they therefore enjoy a considerable advantage over the private investor who is entitled only to the standard ruling market rate of interest. It would appear that the actual underwriter gains his profit from the transaction by retaining the 10/- per cent brokerage which the Loans Board also permits to be paid. Even so the payment of these fees has probably been a major factor in inducing insurance companies and other large investors to place funds in local authority stock.

Possibly the best way in which to continue this argument is to set out the more obvious advantages and disadvantages of the practice of underwriting.

The advantages of the system may be set out as follows:

(a) It makes certain that the issue will only be open upon the market for a limited period of time.

(b) It certifies that the local authority will obtain the full amount of the issue and within a specified time. It could be pointed out here that upon some occasions the insurance companies have not had the cash upon hand just at the particular time when it was required and in such circumstances the situation is overcome by the underwriter hypothecating debentures in order to obtain the finance immediately. When the necessary money is found by the insurance company the amount of the hypothecation is substituted therefore.

(c) It tends to induce the larger financial institutions to invest in local authority stock and as such it helps to provide long term investment for the authorities.

(d) It makes for a more orderly approach to the market as the brokers are in a position to draw up programmes for market activity thus ensuring that competition is kept to a minimum.

The disadvantages are as follows:

(a) As stated above the payment of underwriting fees could be looked upon as an increase in the effective rate of interest and as such increases the cost of loan raising to the authorities. At the same time it results in a substantial increase in income to the sub-underwriters without any additional work on their part. This point is of greater potence when issues are more readily filled upon the open market.

(b) Possibly one of the most objectional features of the system is that it throws the potential of a local authority to raise loans into the hands of a firm of private stockbrokers which is in a position to exercise discretion as to the issues which it underwrites.

(c) Now not all authorities have availed themselves of underwriting facilities and even when it is permitted many local authorities prefer to go onto the market on their own account. This can provide some problems. If the particular authority is a large one and stands a fair chance of raising money then it would incur hostility from the underwriters who were on the market at the same time as it could draw finance away from the issues which were being underwritten. In turn, of course, the brokers provide opposition to the local authority which is not making use of underwriting. This means that once underwriting is allowed there is a tendency for all to be caught up in the 'vicious circle' and it is very difficult to raise finance without the aid of the practice. Once an insurance company knows that it can obtain an underwriting fee it will be very loath to invest in local authority stock unless it knows that it will actually get that fee.

(d) Underwriting adds to the cost of raising the loan but this is offset to some extent by the reduced advertising costs as compared with those incurred in operations upon the open market.

(e) The system appears to have the tendency to induce many authorities to resort to underwriting irrespective of whether or not they could obtain the money in any other way. This is sometimes done simply because open market operations would involve the staff of the local authority in more work than would raising the issue by making use of underwriting facilities.

It was stated previously that underwriting gives a slight market advantage to the smaller authority; or would it be better to say that it helps to even out the disadvantages that the smaller authority would normally suffer, but this statement now requires some amplification. It has long been a matter of some conjecture as to whether underwriting operates to the advantage of the smaller or the larger local authority. On the one hand there are those who say that it operates to the advantage of the larger authority because, as its loans will be more readily filled, there will be a greater tendency for the brokers to take the larger authority on. This is true; the loans of the larger authorities and hospital board issues are very attractive to the insurance companies about this there can be no doubt. But insofar as a larger authority decides to go on to the market on its own the system operates to the advantage of the smaller authority. In any event the smaller body is called upon to pay a higher fee. The authority that would be at the greatest disadvantage would be the smaller authority which could not obtain access to underwriting facilities when the practice was in general use.

Broadly speaking it is the bodies in the larger urban areas and the urban drainage boards which have been forced to make use of the practice. Very few South Island local authorities have ever resorted to the use of underwriting and most of the rural bodies in the North Island have been able to raise their issues without the assistance of underwriting.

NEW PRACTICES AND INSTITUTIONS

From time to time various proposals have been put forward as providing a remedy for the defects existing in the market or as a means of streamlining or increasing the efficiency of the market. These fall roughly into three distinct categories; some involve the introduction of new practices and procedures; others involve a tighter administrative control over access to the market while others involve the establishment of entirely new institutions.

Some of these have already been touched upon (e.g. an extension of the present trustee savings bank system) and this section makes a survey of the more notable proposals which have not already been considered. Many of these were submitted to, and commented upon, by the Royal Commission on Local Authority Finance. A survey such as this lends itself to much speculation and must of necessity give rise to a considerable amount of conjecture.

Death Duty Stock

The proposal that local authorities should be permitted to issue death duty stock was submitted to the Royal Commission by the Harbours Association of New Zealand. The Commission approved the proposal in principle and the following comment appears on page 36 of the Report.

> "It was suggested that local bodies should be allowed to issue 'death duty' stock in the same way as the Government, the proposal being that the local body would redeem the stock at par in the event of the purchasor dying before the maturity date. This would probably not be advisable for smaller local bodies or even for larger ones in unlimited amounts, but we think it might with advantage be allowed for such amounts in each particular case as the Loans Board might approve."

The proposal is, therefore, that this class of stock could be taken up at par and then redeemed at par upon the death of the holder specifically for the purpose of paying death duties. The big advantage of this from the point of view of the investor is that it can be redeemed before the maturity date without loss. The intention behind the proposal is, of course, to obtain increased investment in local authority stock. This class of stock would clearly be of considerable advantage especially to elderly investors but its disadvantages from the point of view of the local authority are obvious. It would probably be necessary to establish a sinking fund or a pool account of some description to provide for repayment in cases where a very heavy commitment accrues e.g. where the whole of the loan has been taken up by the one investor. It is possible that this difficulty could be overcome if the National Provident Fund or some other institution guaranteed the redemption of the stock.

Whether the issue of death duty stock would attract any considerable volume of finance to the local authorities must remain a matter of conjecture but as yet the Government has not given any indication that it intends to introduce the practice. The proposal is only of interest to the individual investor it would clearly not apply to institutional investment and at the same time each investor would only really be concerned to invest sufficient to cover his own death duties, as presumably only sufficient to cover death duties could be redeemed at par at death. It seems probable that the issue of this class of stock would cause a small but sustained increase in the volume of funds invested in local authority stock by the small lenders.

<u>Premium Bonds</u>

Premium bonds are bonds that would be redeemed at a premium at maturity date. Suggestions that local authorities should be permitted to issue these bonds were submitted to the Royal Commission which made the following comment upon the matter:

> "The issue of premium bonds was also suggested either on the system now existing in the United Kingdom or on a system similar to that operated by building societies. We think these schemes may have some attraction for investors, and the Government might well observe the result of the experiment in England. If that seems strikingly successful it might consider the adoption of some such scheme either for its own loans or for those of local bodies or both."

The issue of premium bonds would to some extent be in the same category as the issue of stock at a discount. Devices such as these would certainly divert some finance to local authorities but they would also have the effect of increasing considerably the expense of borrowing and it is doubtful if any additional benefit which might be derived would be worth the added expense involved. The general policy of the Government has been to keep the cost of local authority borrowing as low as possible and it seems unlikely that it would permit the issue of this class of stock. This is especially so in view of the fact that the issue of premium bonds would have to be considered after the introduction of other cost increasing practices (e.g. underwriting) which have clear advantages in other directions.

Determination of Priorities

It has been suggested that the approach to the market could be made much more orderly if some system was devised whereby each loan project was accorded a rating of priority in terms of essentiality and that the more essential projects were permitted access to capital ahead of those that were less essential. The Report of the Royal Commission made the following comment upon this matter (Report paragraph (d) page 49):

> "We find that the demands of local bodies on loan funds should be regulated and controlled by the local Government Loans Board so that the market may be properly organised and priority ensured - within the capacity of the market - for the most urgent and essential works."

However the Commission did not put forward any specific proposals for a scheme of priorities and indeed it would appear that the major problem involved in implementing this proposal is, in fact, the devising of a satisfactory system of setting priorities that would be universally acceptable.

The first point to decide is who or what institution will draw up the schedule of priority. If a local authority finance corporation was ever established in New Zealand it would seem that this would be the logical body to draw up such a schedule. But in the absence of such an organisation the task would probably fall to the Loans Board. However up until the present time the Loans Board has made no attempt to introduce rigid orders of priority but has considered essentiality from a very broad point of view.

Priorities could be set by classifying all loan applications, either before or after the approval of the Loans Board had been granted, into categories (e.g. either a, b or c). Projects placed in one category could be awarded absolute or a degree of preference while those placed in the other, lower categories would be either denied access to the market or accorded limited access. A system of shifting projects from a lower to a category of higher preference in certain circumstances or upon the fulfilment of certain conditions could possibly be devised. On the other hand an even more rigid system of co-ordination could be established by according to each separate project a set time upon the market at some set date in the future.

In order to implement any system of priority at all it would be necessary for each local authority to submit details of its borrowing programme for some years ahead. The necessary information would have to comprise such matters as, the balance of loans approved but not raised, the loan moneys required for works commenced and proposed works likely to be commenced within say, each of the following three years. Figures would also have to be given for each work or group of works that would form one loan proposal. These items would give total loan requirements. The figures would also have to be broken down further into proposed expenditure for each relevant year and then further subdivided into (say) approximate quarterly or preferably monthly expenditure requirements. Relevant technical data would also have tobe submitted with each loan proposal.

The allocating authority would then be faced with the question of estimating the amount of money that is likely to be available so that priority could be established in accordance with the amount of finance that is likely to be forthcoming. This would have to include estimates of amounts available from the open market as well as that which is likely to be forthcoming from the various institutions. At the same time it would be necessary to retain a fairly substantial amount in reserve to meet possible emergency items which could not reasonably have been forecast e.g. a loan made necessary to repair damage caused by a flood.

It can therefore be seen that any system of determining priorities or attempting to co-ordinate borrowing is bound to be riddled with many problems. Firstly there is the great difficulty involved in estimating local authority loan requirements and the even greater problem in gauging the potential of the market. Secondly such a system would be cumbersome, would involve delay, would mean more control and would be bound to arouse discontent among those authorities whose works were accorded a lower priority. It would mean that the body doing the allocating would probably have to employ a number of research officers to investigate the various loan proposals and to estimate the market. Effective co-ordination would clearly require the covering of a very wide field of investment as it is doubtful if co-ordination of a part only of the entire market would be satisfactory. A priority system would mean that demand on the market would be curtailed and it is possible that this would have the effect of ultimately making less funds available to the local authority sector.

Some districts have already experimented with the idea of co-ordinating market activity. In 1955 a committee of local authorities known as the Auckland Area Joint Works Committee was established in the Auckland Area for the purpose of programming capital works in that Area. The Committee did not, however, undertake independent investigation of individual local body proposals. It received submissions from the local authorities upon their proposals and used these as a basis for its own detailed examination of the programme. This would, of course, hardly suffice for a body exercising direct and complete control on all local authority loan issues, and independent investigation of the priority claims of loan proposals would, it seems, be essential.

Optional Redemption Date Investments

The issue of optional redemption date investments would involve issuing stock which could be redeemed at the option of either the lender or the borrower, or both, at say, five or seven yearly intervals. This proposal is very closely related to that mentioned in the section dealing with the rate of interest whereby interest rates could be revised at intervals to bring them into line with current ruling rates. A proposal of this nature would operate almost completely to the disadvantage of the localauthority except possibly in that situation where interest rates were falling and finance was super abundant. If an investor decided to redeem before the full maturity date the loan would require to be refinanced and this could cause some acute administrative problems to the local authorities.

The view that local authorities should be permitted to issue optional redemption date stock was submitted to the Royal Commission on Local Authority Finance by the Electrical Supply

Authorities of New Zealand but it was not commented upon by the Commission in its Report and it appears unlikely that any such system will ever be introduced.

Municipal Bank

From time to time it has been mooted that a municipal bank should be established in New Zealand but at no point have any very specific proposals been put forward. It has been suggested that such a bank would operate in complement to a local authority finance corporation while some have believed that its functions would overlap those of a finance corporation thus rendering it unnecessary if the corporation was set up. The general intention appears to be that the bank should act essentially as a lender of short term finance while the finance corporation would be concerned mainly with the provision of long term finance i.e. the bank would be complementary to the corporation. The bank would provide overdraft accommodation to the authorities at a lower rate than that charged by the trading banks and would accept deposits upon short term. It is thus envisaged that the bank could take over some of the functions now carried out by the National Provident Fund. The bank would not act as a general savings repository accepting money from the general public. The general proposal seems to be that the bank would operate throughout New Zealand by means of agencies conducted by the Bank of New Zealand and it would operate cheque facilities. It would appear that an initial capital of at least £100,000 would be required to commence operations.

The view that a municipal bank should be set up was put to the Royal Commission by the Municipal Association of New Zealand and the Commission made the following comment thereon (Report paragraph 104 page 36):

> "The establishment of a municipal bank was another method suggested for improving the financing of local body capital projects. The suggestion was made by the Municipal Association as being complementary to a suggested Local Authority Finance Corporation (which we will presently deal with) and it was urged that while this matter should be seriously considered it should not cause delay in the provision of the Finance Corporation while the question of banking received further consideration. We find some difficulty in seeing the necessity for a municipal bank if the proposed Corporation is established and we think the proposal may well be deferred until it is decided whether or not a Corporation is to be set up and, if so, whether its operations call for any further banking facilities."

<u>Local Authority Finance Corporation</u>

The following schedule of proposed powers and functions of a possible Local Authority Finance Corporation is taken from the Report of the Royal Commission (Report paragraph 110 page 38). Several other parties have also put forward proposed sets of powers and functions but basically they all seem to conform to this one fundamental pattern.

(a) To take over those powers and functions of the National Provident Fund Board now delegated to the Investment Committee. These include.

(i) The purchase and sale of Government and local body securities.

(ii) Temporary advances upon hypothecation of securities.

(iii) Underwriting loans.

(iv) Borrowing on overdraft.

(v) Providing investment for depreciation funds, sinking funds, trust funds and loan moneys not immediately required.

(vi) Investment of surplus funds.

(b) As a primary function to lend to local authorities the funds accruing from the above activities and funds raised by Corporation borrowing.

(c) To act in an advisory capacity to local authorities and to achieve some co-ordination in local authority borrowing.

(d) To issue its own stock or debentures, which would have trustee status, against the security of debentures held from local authorities.

(e) The power to raise loans overseas for local authorities.

(f) Take over from the National Provident Fund approximately £15 million of invested funds from local authority superannuation activities plus about £5 million of local authority reserves and other moneys temporarily deposited with the Fund.

(g) Normal overdraft accommodation to enable the Corporation to keep its funds fully invested with local authorities, and any other financial assistance through the Reserve Bank as may be deemed necessary by the Bank for the implementation and extension of the Corporation's activities.

The Royal Commission went on to recommend that the Corporation should ultimately possess the sole right to raise loans and to underwrite for local authorities but with the power to contract and to pay for sub-underwriting. The Corporation should be self sufficient and self supporting and any profit which it may make should be retained by it to increase its lending resources. Care should be taken to select and maintain a skilled and experienced staff.

It would appear therefore, that what is envisaged is a highly specialised institution separated from the control of the Government but nevertheless sponsored by the Government lending institutions.

Now the question arises as to the form which the institution should take. According to the outline given above virtually all of the functions at present carried out by the National Provident Fund would be taken over by the Corporation.

In regard to (d) above it can be seen that the security backing for the Corporation's debentures would be the debentures it holds from the local authorities. Thus in the ultimate the Corporation would have the rating potential of the various local authorities as the security backing for its debentures and stock. The Corporation would not raise money except in exchange for local authority debentures. The right of persons holding debentures from the Corporation would therefore be to take over the debentures which the Corporation is holding. This raises the question of whether the Corporation would go on to the market to raise loans for each specific loans project or whether it would borrow generally. Borrowing generally may, in many cases, be a better proposition as if it attempted to obtain money for specific projects for individual local authorities its money raising potential would be considerably restricted by the nature of the particular local authority and the proposed project.

One further function which a Corporation could undertake would be a co-operative insurance scheme for local authorities. All the profits from this could be invested in local authority stock. At present the insurance companies are required to keep substantial cash reserves but if both were combined the cash reserves of insurance companies could be merged with the liquid reserves of the Corporation hence cutting the total need for reserves as there would be no need for both parties to hold reserves.

One vexed question is the initial amount of capital which the Corporation would require and the source from which it could obtain this capital. It is most unlikely that the Corporation could get any automatic access to the capital accruals of the National Provident Fund, i.e. despite the recommendations of the Royal Commission, and it would probably be necessary for it to obtain a capital structure elsewhere. The amount of initial capital that would be required would, of course, depend to a large extent upon how extensive its functions were to be. It has been submitted that £5 million would be required while others have stated that £2 million or even £1.5 million would suffice. The difficulty would be to find someone to contribute this sum. It could be put up by the National Provident Fund together with several different insurance companies in a joint effort. It is possible that this sum would remain uncalled and would act merely as a security backing for the Corporation. At the present time there does not appear to be any prospect of Reserve Bank credit being used to finance the Corporation as this could prove inflationary. The day to day operations of the Corporation would most likely be run upon the 'pool system' (similar to that at present in use by the National Providen Fund). This 'pool' would contain the surplus moneys contributed by the local authorities.

However one major problem with utilising a capital structure is that the contributors of the capital would expect a return upon their investment. It has thus been suggested that instead of relying upon contributed capital the Corporation could obtain its initial finance by means of a levy upon all New Zealand local authorities which would be made upon the rates of the territorial authorities and upon the revenues of the 'ad-hoc' authorities. A levyof 1d in the £1 upon all rateable property made annually over a period of ten years would produce an amount well in excess of £50 million.

As the Corporation would exert a very substantial influence in the market it would be necessary for it to operate in close co-operation with the Treasury and the Reserve Bank so that its activities could be harmonised with the economy of the country as a whole. To this end it is possible that the debentures of the Corporation would be issued only upon the approval of the Minister of Finance.

The next point is overdraft accommodation. It is probable that about £1 million in overdraft accommodation would be required. This would be necessary to cover fluctuations between the receipt of revenues and the payout of commitments for investments. The National Provident Fund at present maintains a system whereby it can sell Government Stock at short notice to finance unexpected liabilities but being an independent institution the Corporation could hardly operate a system such as this. Overdraft accommodation would be vital to the Corporation to enable it to keep its funds fully invested and it is possible that temporary advances could be made by the Reserve Bank i.e. the Reserve Bank could act as the Corporation's banker.

How comprehensive would the activities of the Corporation be? Would it raise the total amount of finance required by the local authority sector, would it raise loans or supply funds only to certain classes of authorities, or would any local authority be free to seek the aid of the Corporation or to make its own approach to the market as it desired? But it is certain that many of the larger bodies would still prefer to raise their own loans and even most of the smaller authorities would probably still prefer to approach the market upon their own behalf in those cases where they were sure of raising the finance. This being the case the Corporation would frequently be operating upon the market in competition with various local authorities. To overcome this difficulty a system of programming market activity would have to be devised to ensure that the Corporation was not merely taking funds away from those bodies which happened to be seeking finance at the same time as the Corporation.

An amendment to the Trustee Act 1956, would be necessary to give the securities of the Corporation trustee status. It is likely that some element of Government guarantee would be required to clinch the trustee status of the Corporation's securities.

Now we must consider the possible advantages which would accrue from such an institution. It could provide expert advice upon the raising of loans and other financial matters which would be of great assistance especially to the smaller local bodies. The Corporation could act as a buffer between Government and the local authorities At the present time available finance is not spread evenly throughout the country; this situation would be rectified. A Corporation would obtain more money for local authorities in the aggregate than all individual authorities working independently as it would have more prestige than any single local authority. By assisting the smaller local authorities it would mitigate the present disadvantageous position suffered by the smaller bodies. As the nature of the particular body would be an immaterial factor in the lending policy of the Corporation the present disadvantages suffered by some classes of authorities could largely disappear. A single type only of local body security would be on the market and this would be far more readily negotiable than the many and varied securities which are upon the market at present. It would act as a short term money market for local authorities. The debentures or stock of the Corporation would be readily marketable and since the Corporation, when well established, would have sufficient reserves (in the form of reserves made up by amortization payments or in other ways) to redeem its debentures or stock at par or thereabouts, an investor who was forced to realise before maturity date would have a smaller chance of loss through depreciation in the value of his security than in the case of debentures in a smaller body for which there was only a limited market. The securities of the Corporation could be offered to the public in varying units and in several different forms to improve their attractiveness to a wide range of investors. These bonds would be sold throughout the country, at banks, post offices, trustee companies and so on.

But two advantages which could be derived from such an institution stand out above all others. Firstly by stabilising the supply of finance to local authorities it would assist in stabilising the rate of interest. Secondly the Corporation would be in a position to borrow short and to lend long and this would mean that the authorities would not be forced to resort to rely upon short term finance to the extent which they do at present.

However, some believe that the establishment of such an institution may encourage many to enter the field for loans when the cost of the project could more readily be met from revenue. As finance would be more readily available reckless spending may be encouraged. It was previously mentioned that the Corporation would be able to raise more for local bodies than the aggregate of local authorities but this could be a major factor to operate against the Corporation as the greater power the Corporation has upon the market the more it is likely to conflict with the activities of the Government. The administration costs of the Corporation would be considerable; possibly in the vicinity of £40,000 per year. The activities of the National Provident

Fund would be seriously depleted. It would need the services of a large and highly trained staff and it is very doubtful if such a staff could be recruited in New Zealand at the present time. Could such an institution operate at a profit? It must remain a matter of some conjecture whether the Corporation would draw more savings out of the community or whether it would merely take finance away from the other sectors of the market.

It has been stated that the Corporation would issue blanket debentures and would probably not raise loans for individual projects or bodies. But if it did this the local interest in many loans would be seriously diminished and indeed it has been stated that regional loyalties based on a composite of utilitarian and prideful interest on the part of local residents, do in fact function as a benevolent underwriter of local body loans and make a valuable contribution towards their success. The Corporation may be able to overcome this by raising some issues upon a blanket basis and raising in respect of a certain project in those cases where it is obvious that local interest would be of assistance in finding the finance.

Of all the proposals which have been put forward as providing a remedy for the ills which beset the local authorities when they approach the market this is the most challenging and is the one which has received the greatest publicity. There can be no doubt that the existence of any such institution would constitute a major force within the market.

The Royal Commission approved the establishment of a Local Authority Finance Corporation and made the following comment (Report page 39 paragraph 111)

> "The Corporation would not have, initially, the sole right to raise loans for local bodies, but local bodies should be encouraged to use it and, ultimately, when fully established and operating, it could become the sole issuing authority. It should be the sole underwriter for local body loans but with power to contract and pay for sub-underwriting. We think this is necessary to protect and recognise the status of the Corporation and to prevent undue cutting and competition. We do not think it advisable to authorise the Corporation to act as an insurance company nor to empower it to make a levy on local authorities, except for the purpose of recouping losses - which should not occur. The Corporation should be self sufficient and self supporting; it should be able to make some profit but this profit would be retained by the Corporation to increase its lending resources and might well be used for making loans on especially favourable terms to needy local bodies. Particular care should be taken to select and maintain a skilled and experienced staff."

Increased Government Subvention

Conditional and unconditional grants in aid from the Central Government play a major part in the financing of local government in the United Kingdom but, except perhaps in respect to hospital boards, are not used to any great extent in New Zealand. It should be pointed out that the scope of local government activities is much wider in the United Kingdom than it is in this country.

It could well be argued that extensive Government assistance in the financing of local bodies means a negation of the whole concept of local government and implies that the authorities are merely local spending agencies of the Central Government. However, an examination of the existing situation seems to indicate that Government assistance does not bring about a weakening of the fabric of local government. Indeed the opposite appears to be the case. From time to time chairmen of various local authority organisations have commented upon the lack of financial assistance from the Government and some competition has arisen among the various classes of authorities for assistance. Financial aid in any form has been freely accepted.

Assistance which has been granted in the past has been designed largely to further Government policy rather than to provide sustenance for the authorities. Examples of this include the provision of subsidies for pensioner flats and sewerage works. Grants of this nature assist in extending the range of local activity as well as furthering Government policy.

Apart from subsidies subvention has taken the form of reduced interest rate loans and occasionally, unconditional grants. We are faced with a minor problem in definition when we come to consider subsidies paid by the National Roads Board which is now one of the major sources of subsidy finance for local government. The funds of this organisation do not have to be appropriated by Parliament. On the other hand it is financed largely by a tax on petrol.

One of the major problems involved in the granting of additional aid is the difficulty of financing it. Governments have been hesitant to take action to assist local bodies if that action is likely to prove politically inexpedient. Increased assistance to the authorities would mean increased taxation in some form or other. It is for this reason that many of the recommendations of the Royal Commission have never been implemented e.g. the local body levy of 2d in the pound on earnings, which incidentally, to make matters worse from a political point of view, it was suggested should be collected by the Central Government.

Additional Sources of Revenue

Additional sources of revenue whichwere made available to the territorial authorities could be diverted to capital uses. The political problems involved here are even more potent than those associated with Government subvention.

Rates have long been the major source of revenue for the territorial authorities and are likely to remain so if only for the reason that the limits of the property over which they are levied can be readily defined. Rates provide the basis of local body income in most Western Countries, but in some instances they are supplemented by income from such items as local income and sales taxes, citizen taxes and levies. Legislation would be necessary to implement proposals of this nature and although the revenue collected would be for local government the taxpayers would be inclined to regard the imposition as merely another tax and the brunt of the blame for its introduction would, therefore, fall upon the Central Government.

A local sales tax (i.e. a tax on retail sales) would probably have to be collected and levied on a regional basis. If such a tax was not at a uniform rate throughout the country, consumers may be induced to travel outside their district of residence in order to gain the advantage of cheaper purchases. Opposition from business interests could be expected to any proposal to introduce a local sales tax in New Zealand.

The range of local trading activities could be extended i.e. boroughs and counties could be permitted to engage in the retail selling of electrical appliances. Incidentally this practice is already carried on upon a limited scale. A proposal of this nature would also encounter opposition from the business world and it is unlikely that smaller authorities would be in a position to derive any great benefit from increased trading activities.

CONCLUSION

Having analysed the situation we conclude the study by reverting to the original question which we set out to answer: "Is the market organised in the way that best ensures an adequate flow of capital to this sector?"

It has been established that we cannot permit local authorities to compete upon a free uncontrolled market. The competitive forces operating between the authorities themselves and the overall nature of the work they are required to undertake together with the effect of the other sectors dictate a considerable degree of Government control and subvention.

A possible summary of the major problems may be as follows.

(a) Inter authority competition

(b) Competition from outside sectors

(c) Fluctuating costs of raising and servicing loans

(d) A dimunition of available sources of supply

(e) In the light of the comments made in the preceding section the fact that there is political opposition to the introduction of new institutions or additional sources of revenue to assist local authorities.

(f) Overall lack of finance coupled with a dependance upon short term finance.

These various problems are to some extent interdependent and are generally the result of each other.

As previously indicated inter local authority competition affects mainly the small boroughs with essential works who are forced to compete with larger neighbours. Even a substantial increase in the supply of capital may not wholly eliminate this problem. The fluctuating costs of raising and servicing loans also affects, in the main, the smaller bodies. The smaller authorities are already permitted to pay higher underwriting fees and it would be undesirable to allow them to pay higher interest rates thereby increasing costs still further.

Despite the recommendations of the 1958 Royal Commission to the effect that the ultimate aim should be free interest rates, this prospect could not be contemplated in present conditions.

In respect to competition from outside the sector it has been pointed out that in relation to the urgency and importance of their needs, the authorities are probably obtaining an equitable share of the overall amount of available capital. There has been little evidence that any really essential works have been either prevented from proceeding or seriously delayed through lack of finance. But this point could hardly be used as an argument against any further reform of the local authority sector of the market.

Government influence in the market makes it most unlikely that the authorities will be granted any preferences or endowed with any further devices which would enable them to gain a greater share of the market to the detriment of other sectors. The recommendation of the Royal Commission to the effect that a local authority finance corporation be established has, therefore despite frequent agitation, never been implemented. All this amounts to very little consolation for local bodies.

The gradual decline in insurance company investment in this field has resulted in the authorities turning increasingly to the small inves tor and the government institutions as sources of finance. The State Advances Corporation has ceased acting as a general lender leaving the National Provident Fund as the major state lending institution. The small investor is a fickle, and in some respects unsatisfactory lender. He is of limited use to the smaller boroughs in the large urban areas and has little value as a lender of long term finance. The authorities have tended therefore to rely more upon the Central Government as a source of capital as well as revenue finance. However the limitations involved in extending this form of assistance further have been considered in the previous section.

Possible Remedies

There is no magic remedy universally applicable which will instantly solve the existing problems and only piecemeal solutions can be submitted.

The scope and problem of local finance could be said to depend upon the position of local government within the general governmental system of the Country. Changing conditions have necessitated new distributions of functions between central and local government. No set pattern of local government central government division of responsibility has evolved; the matter rests almost entirely upon ad hoc policy considerations. The financial problems could conceivably be tackled by effecting further transfers of functions from local to Central Government. Moves in this direction would probably result in a more efficient use of available capital but at the same time would mean a weakening of the political structure of local government.

Reform is a more immediate possibility. Shifts in population have weakened the local government framework especially in the rural areas and have made reform an urgent necessity. So far however legislative incompetence has prevented any really effective reforms from taking place.

It has been pointed out that the territorial authorities are generally not permitted to build up general reserves which could be used at a later date for capital development. Section 143 of the Municipal Corporations Act grants to boroughs the power to set up funds for the renewal repair replacement or improvement of any property, plant, fixtures or appliances. The Audit Office has greatly restricted the utility of this section by requiring that any funds which are established under its provisions must be earmarked for a specific purpose. Whether this narrow interpretation was the original intention of the legislation must remain a matter of some doubt but there is no question that this provision could be used as authority for municipalities to build up reserves for a wide variety of purposes. If a reserve was established for one purpose there would probably be no restriction upon it being used later for another purpose provided it came within the scope of the section. These reserves would be financed from rating revenue. It appears therefore that if the restrictions upon the use of this section were liberalised the way would be open for municipalities to accumulate reserves which could be diverted to capital expenditure. This would mean less reliance upon the market and could be very useful, especially to smaller boroughs which had reasonably low rating levels. It must be admitted that such a practice could be open to abuse but the control exercised by the Audit Office should be able to keep any misuse of the section to a minimum.

Considerable progress towards solving the present financial problems could probably be made by introducing into New Zealand a system which has been in use in the United Kingdom for almost forty years, i.e. the "loans pool". These are somewhat analogous to the investment pool run by the National Provident Fund except that every individual authority would have its own "pool account". The great virtue of these devices is that they would do away entirely with the need for sinking and depreciation funds; or to put it more succinctly, the money which is at present invested in sinking, depreciation, and renewal funds could be made more readily available to finance capital works. It could be argued that as things stand at present there is a certain amount of double financing, i.e. simultaneous borrowing and lending. Section 9 (6) of the Local Authorities Loans Act requires that authorities when borrowing must make provision for the repayment of the loan and this is sometimes effected (although not universally by any means) by the establishment of a sinking fund. Sinking Fund Commissioners are appointed to invest these funds in trustee investments as directed by the local authority. An analogous situation exists in respect to depreciation funds.

As at 31 March 1963 local authorities had external sinking and depreciation funds totalling approximately £7.5 million and it is notable that in that same year they sought some £10 million on the market. The pool system would enable much of the money available in the sinking funds to be diverted to capital expenditure. Before pointing out the further possible advantages of the pools system we will examine the mechanism of the system in a little more detail.

As far as British practice is concerned the authority sets up a loans pool which is actually the sole borrowing and lending unit of the authority, i.e. all the authority's capital financing transactions go through the pool. The pool is financed by loan moneys received, contributions from rate income together with other miscellaneous capital receipts. The pool actually makes the capital expenditure as required and instalments of principal and interest are collected from the other departments of the authority. The pool borrows externally of course, and when external loans fall due for repayment the necessary finance is usually obtained by re-borrowing.

Now if a system such as this is to be introduced into New Zealand a few modifications would seem to be required. Firstly if each local authority is to have its own pool and external borrowing is still to be carried out, then the pool system would not go far towards solving the problems of the smaller authorities because the smaller pools would probably still experience the great difficulty in obtaining finance that the lesser local bodies do at the present time. It would appear' therefore that collective pools containing a number of different authorities would be more suitable to New Zealand conditions. These could be organised on a regional, sub-provincial, or even provincial basis but should preferably contain a good cross section of authorities of different classes and sizes both urban and rural. Coupled with the point just mentioned, provision should be made to compel the non territorial trading authorities, e.g. harbour boards, to invest in their own pool, or if no investment opportunities exist there, in some other pool. This would mean that local authority investment was kept within the local authority sector. The reserves of the trading departments of the territorial authorities could also be invested in the pools. It can be seen that the greater the number and variety of authorities in a pool, the greater would be its chances of obtaining finance. It is possible that some legislation may be needed to require authorities to invest in the pools. The attractiveness of investment in the pools would depend largely upon what was offering outside, but it would certainly be advisable to divert as much local authority investment as possible into the pools.

A further point that would have to be settled would be the avenue for the short term investment at present taken by the National Provident Fund. Should these be channelled into the pools? In view of the problems surrounding the administration of these short term investments it would appear advisable that they should, for the present at least, be left with the Provident Fund.

The administration of the pools could be placed in the hands of trustees who were appointed by the authorities and possibly containing government representatives.

Now to reiterate the advantages of the pool system. Firstly it would alleviate the need for sinking funds and would enable the moneys that are at present invested in those funds to be released for other purposes. Secondly it would provide an avenue of investment for the mounting reserves of the trading authorities, meaning that available finance from authorities with surpluses could be made available to other authorities. This would assist in providing a system of self finance for the local body sector and reduce the competition which this sector experiences from other quarters. Thirdly inter authority competition would be reduced as the pools could establish some rational method of making finance available which would not be dependent upon the size or class of authority. Fourthly as the introduction of the loans pool system would mean little disruption of the market at the expense of the other sectors it could probably be implemented without much political opposition.

APPENDIX A

SCHEDULE OF INTERVIEWS

Some of the information contained in this thesis was obtained from a series of personal interviews conducted by the writer with those individuals who appeared to be in the best position to discuss the particular aspect of the study under consideration.

Interviews were conducted with the following.

Secretary, New Zealand Harbours Association.

Accountant, Wellington Hospital Board.

Secretary, New Zealand Hospitals Association.

An Officer of the State Advances Corporation of New Zealand.

Assistant County Clerk, the Hutt County.

Treasurer, Wellington Harbour Board.

Investment Officer, Government Life Insurance Office.

An Officer of the Local Authority Section of the Audit Department.

A Borough Councillor of the Petone Borough.

A Clerk of a Firm of Wellington Stockbrokers.

Secretary, National Roads Board.