28 April 2024

SUBMISSION ON THE PROPOSAL FOR THE SALE OF AURORA ENERGY

SUMMARY OF SUBMISSION

1. The limited financial information included within the Consultation Document makes it difficult for submitters to determine if the sale of Aurora is in ratepayers' best interests.
2. The financial analysis, prepared using publicly available information, indicates that it is in ratepayers' best interests to retain Aurora.
3. Aurora's debt position looks manageable. The Council needs to manage its debt within policy settings and it should not be looking for a short term cash injection by selling Aurora at the expense of the long term value derived by retaining Aurora.

DETAILED SUBMISSION

The Dunedin City Council (Council) has invited submissions on the proposal to sell Aurora Energy (Aurora). The justification provided is to retire debt and to establish an investment fund which provides a cash return to Council.

The Council's Proposal Document does not provide submitters with the opportunity to compare the financial implications of selling Aurora vs the alternative of retaining Aurora. It is therefore difficult to determine if the sale of Aurora is in the long term best interests of ratepayers.

Auckland Council, for example, has included the sale of strategic assets within their draft Long Term Plan (LTP) which gives the public / ratepayers the opportunity to assess the financial implications of the proposed sale of the strategic assets. The Dunedin City Council could have deferred consideration of the sale of Aurora until its 2025 – 2034 LTP in the same way as it has with other decisions. Alternatively, if the Council wishes to proceed with the sale of Aurora, prior to releasing its LTP, it should have released some financial information in the Consultation Document, comparing the sale of Aurora with its retention.

Council will have received a significant number of reports on the proposed sale and Councilors have clearly come to the view that the sale of Aurora is in ratepayers' best interests. As noted above, the decision not to share a summary of the financial implications makes it difficult for submitters to provide constructive comments on the Proposal.

The test which I have applied in preparing this submission is – has Council established and demonstrated the case for the sale of Aurora.

The following analysis is based on publicly available information, which is limited and short term in nature.

Council and Dunedin City Holdings Ltd (DCHL) – The Council's main concern appears to be the lack of a dividend from Aurora. The proposal also implies that Council and DCHL are independent entities.

From the ratepayer perspective, however, the Council and DCHL are a Consolidated Group or single entity. The role of DCHL within the Group is to maximise the commercial value of the trading entities owned by Council. From the ratepayers' perspective, 100% of Aurora's Profit After Tax accrues to Council and ultimately to ratepayers. In completing any analysis, Aurora's Profit after Tax is more relevant to the decision on whether to sell or hold Aurora, than whether or not the Council receives a dividend.

Investment fund – Other than noting that the investment fund with be "hundreds of millions" Council has given no indication on either the likely size of the fund or the expected returns. The Proposal indicates that details on how the investment fund will be managed (within Council or by DCHL) have yet to be finalised. The investment mandate has also yet to be established. A high level of restrictions within the investment mandate will also have the potential to reduce the long term return from the Fund.

The following analysis uses an investment return of 7.5% pa. This is the return used by the Auckland Council which is considering selling strategic assets and creating an investment fund.

Aurora and the investment fund – Aurora is a regulated asset which gives a long term steady return reflecting the level of investment. Returns from Aurora will act as a natural hedge against inflation.

Returns from the investment fund will, by their nature, be more volatile. There will also be a need to retain some of the investment return to inflation proof the fund.

The expected selling price of Aurora is of critical importance. There has been some speculation in the ODT that the value of Aurora could be $1 billion. This has not been confirmed or denied by Council. In fact Council has been careful not to comment. If this consultation was part of a LTP process the Council would be required to provide an estimate of the selling price within the financial projections.

The selling price has a material impact on the size of the investment fund, as is highlighted by the following summary:

	$m	$m	$m
Aurora selling price (net of selling costs)	900	1,000	1,100
Repayment of Aurora debt	576	576	576
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Size of investment fund	324	424	524

With a 7.5% pa investment return this would give the following investment return.

Investment return p.a.	24.3	31.8	39.5
Retained in fund for inflation*	(6.5)	(8.5)	(10.5)
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Investment return available to Council	17.8	23.3	29

*based on long term inflation of 2%.

The above returns compare with Aurora's forecast Profit After Tax in the 2025/6 financial year (the first full year of the investment fund) of $31.7m*. In order for the investment fund to give an equivalent return the selling price of Aurora would need to be $1,152m.

*From Aurora's Statement of Intent

Assuming that Aurora's Profit After Tax will continue to improve, it can be expected that Aurora's Profit After Tax will exceed the return on the investment fund in each and every year. On this basis, the economic value to ratepayers will be enhanced by the retention of Aurora.

In summary, the sale of Aurora does not appear to be in ratepayers' best interest and as a result Council has yet to establish the investment case for the sale of Aurora.

The Council will need to release the investment case for selling Aurora, including the forecast selling price, if it is to demonstrate that selling Aurora is in the best interest of ratepayers.

Debt – on the information available, Aurora's debt position looks manageable. Aurora's equity position is forecast to improve and can be managed into the target range. According to the Statement of Intent, some dividend can be expected in the 2026 or 2027 financial years.

The Council needs to manage its debt within policy settings and it should not be looking for a short term cash injection by selling Aurora at the expense of the long term value derived from retaining Aurora.