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focus

Auckland Future Fund: Growing the family silver is a good idea

Auckland Mayor Wayne Brown has proposed establishing a regional wealth fund, the Auckland Future Fund, to manage some of the city's assets. There are details to be worked through, but on face value we believe the idea has merit. No doubt some will say "of course Forsyth Barr is a supporter, they're an investment firm". And our response: "who would think that a fund that grows the city's wealth over the long-term, diversifies the city's assets, and provides benefits to Auckland and Aucklanders isn't a good idea?"

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The plan

Mayor Brown has proposed four options for managing two of the city's major assets, which are its 11% shareholding in Auckland International Airport and its 100% ownership of Ports of Auckland.

One option is to maintain the status quo. The others all propose establishing a Future Fund, with different choices about which assets are included in the Fund – either both the Airport shareholding and the Port, just the Airport stake, or the Airport stake plus future dividends received from the Port.

The Future Fund concept isn't novel. Many regional councils have long-term investment funds seeded by the partial or outright sale of infrastructure and property assets, including Northland, Waikato, and Bay of Plenty (just to name a few). A number of regions also have Community Trusts which were seeded by the sale of power companies, regional banks, or other assets. Their sizeable assets generate income which is invested back into those regions.

In fact, you don't have to narrow comparisons to local government. The Auckland Future Fund is not really much different to the New Zealand Super Fund investing to provide future pensions to New Zealanders, or a charity investing to grow its bequests and the future benefits it can provide, or even somebody starting to save in their 20s or 30s for their retirement.

The benefits

In New Zealand, the question of public asset sales often incites vocal opposition. In our view, some of the arguments against have merit and need to be addressed, others do not.

Often there is criticism around "selling the family silver". The case can be made that the Airport and the Port are high quality assets, but the question really should be, are these the best assets for Auckland City? The Council did not choose these assets, they inherited them from earlier councils.

A key principle of investing is diversification – not having all your eggs in one basket in order to protect yourself against future unexpected shocks. The Council's assets are not diversified. If a major economic shock or natural disaster impacted the Auckland economy, hurting Auckland ratepayers and raising the Council's need for funds, it might also impact the Airport and Port. You don't have to look back far to COVID-19 for an example.

Another claim is that private owners prioritise profits over public interests. The Maritime Union has argued privatisation of the Port could result in massive price hikes. But public ownership isn't the only way to control prices. And is it Auckland ratepayers' job to subsidise freight companies? Intense competition between New Zealand ports has limited price increases compared to what has been seen offshore. If competition isn't sufficient to adequately constrain prices then they can be regulated. This is already the case with Auckland International Airport.

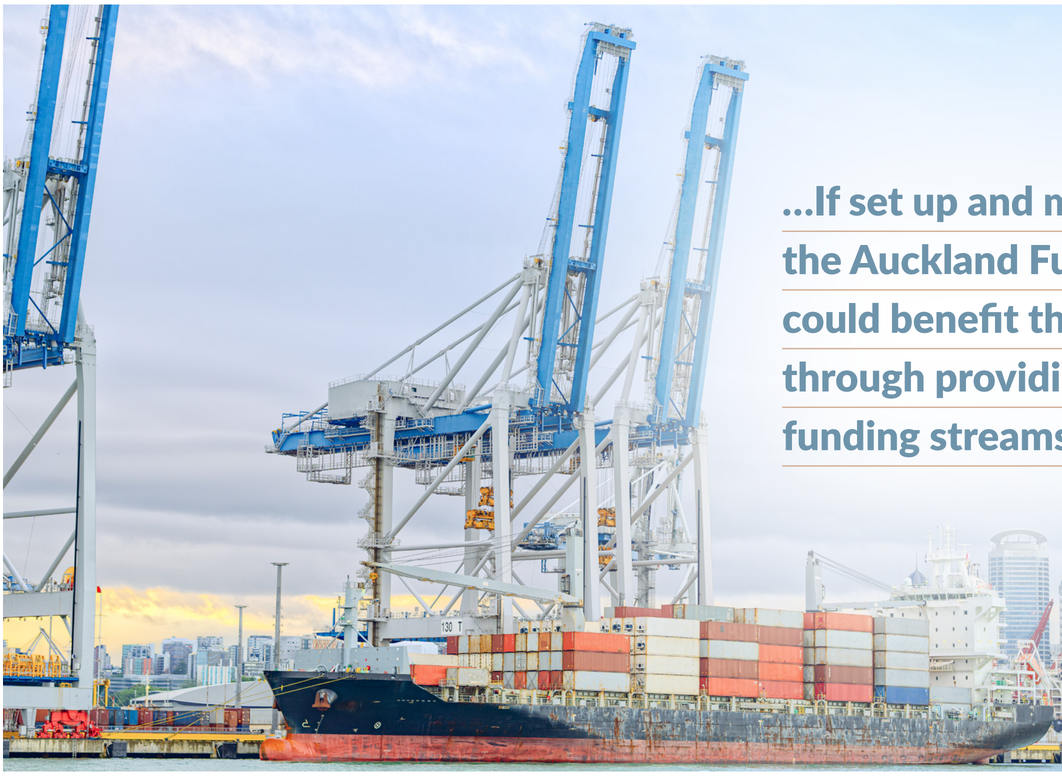
A further claim is that asset sales are a short-term gain but a long-term loss. That may or may not be true depending on how the process is managed.

History suggests that governments aren't the best owners of businesses. If you consider the Mixed Ownership Model process when Meridian Energy, Mercury Energy (then Mighty River Power), and Genesis Energy were partially floated on the NZX. Today the New Zealand government receives around $460 million in dividends a year from its 50.1% stakes in these three companies, substantially higher than the $191 million it received in 2012 when it owned 100%.

A more direct comparison may be the success story of Port of Tauranga. Quayside Holdings is the commercial investment arm of the Bay of Plenty Regional Council. It was established in 1991 with a 55% stake in Port of Tauranga (against staunch anti-privatisation opposition). That stake was originally valued at $53 million. Since then Quayside has paid out distributions of over $640 million to the Bay of Plenty Regional Council, other regional stakeholders, and local infrastructure projects. Today its asset base is valued at around $3.2 billion including $479 million of non-port assets.

The performance of Port of Tauranga contrasts sharply with a relatively sorry story for Ports of Auckland. The company was previously listed on the NZX. In 2004, the last year it was listed, it paid out $43 million in dividends. Under Auckland Council's ownership, that fell to as low as $3.7 million in 2021, and while it improved to $30 million in 2023, it remains well below the level of 20 years ago – a disappointing performance for its ultimate owners, the Auckland ratepayers.

One valid concern around asset sales is that the proceeds may be squandered. Critics point back to the $300 million-plus Diversified Asset Fund the Council inherited from the Auckland Regional



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Council. That fund was sold down between 2016 and 2018 for one-off contributions towards a number of projects and is now gone. If the Future Fund is established, it will be important that the right governance rules and structures are put in place to ensure the funds are preserved for the long-term as intended. This isn't hard to do. The New Zealand Super Fund, for example, has rules in place so governments can't tap into its funds willy-nilly. The Diversified Asset Fund had no such rules.

If set up and managed well the Auckland Future Fund could benefit the city through providing future funding streams, diversifying its asset base, and affording a buffer against economic or natural disaster shocks. This is by no means unprecedented. The success achieved by other local bodies in New Zealand shows that, with the appropriate long-term time horizon and if political ructions can be navigated, an investment fund can become a valuable asset and source of funds for a council.

If at any time you want to discuss investment options and opportunities, your Forsyth Barr Investment Adviser is available to provide you advice and assistance.

0800 367 227

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