The Treasury

Project Korimako - Release of advice

December 2022

This document has been proactively released by the Treasury/Minister of Finance (Hon Grant Robertson) on the Treasury website at

https://treasury.govt.nz/publications/information-release/project-korimako

Information Withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

Where this is the case, the relevant sections of the Act that would apply have been identified.

Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

[23] 9(2)(a) - to protect the privacy of natural persons, including deceased people

[25] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information

[26] 9(2)(ba)(i) - to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely to prejudice the supply of similar information, or information from the same source, and it is in the public interest that such information should continue to be supplied

[33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment;

[36] 9(2)(h) - to maintain legal professional privilege

[37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice

[38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice

[39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [23] appearing where information has been withheld in a release document refers to section 9(2)(a).

Reference: T2021/2632 SE-2-12-4-2-3

Date: 21 October 2021

To: Minister of Finance
(Hon Grant Robertson)

Deadline: None

Project Korimako – Potential Financial Indicator Impacts

You asked us to provide you with information regarding the impacts on the Crown balance sheet from potential changes in the shareholding arrangements for Kiwi Group Holdings (KGH). We present below financial impacts based on a spectrum of hypothetical new ownership arrangements which sit within the options you asked us to further develop [T2021/1832 refers]. These include options either for NZSF acquisition or divestment (to the Crown).

Assumptions

Transaction details would only be known following the conclusion of a transaction, so several assumptions are required to allow us to calculate potential financial impacts. The assumptions we have adopted are as follows:

- Total transaction value of KGH is $2 billion and there are no transaction costs
- Transaction settles at 30 June 2022
- New Zealand Post Limited (NZ Post) retains [25], [33], [38] of any sales proceeds it receives with the remainder distributed to the Crown as a special dividend
- Any funds released to Accident Compensation Corporation (ACC) or New Zealand Superannuation Fund (NZSF) are re-invested in non-Crown entities
- Any funds invested in KGH by NZSF are redirected from other investments
- Crown marginal 10-year financing cost of 2.1% per annum, and
- Current ownership levels are 53% NZ Post, 25% NZSF and 22% ACC.

Financial Impacts

Based on representative hypothetical new ownership arrangements, we have calculated the impacts on gross Sovereign-issued debt, net core Crown debt, and the financing costs that would be recorded in the Operating Balance before Gains and Losses (OBEGAL).

The drivers of the results are summarised on the following page.

- Gross sovereign-issued debt increases if/when the Crown purchases a direct interest in KGH and declines when the Crown receives a dividend from NZ Post, reflecting the proceeds NZ Post receives in excess of the [25], [33], [38]

- ACC and NZ Post are not included in the core Crown so financial flows between the Crown and ACC or the Crown and NZ Post have impacts on core Crown net debt.

- NZSF is included in core Crown, but is excluded from the net core Crown debt calculation so financial flows between the Crown and NZSF impact core Crown net debt.

- We are currently working through the financial reporting impacts with NZSF were it to become the majority shareholder and, once this is sufficiently progressed, we will update the impacts on the key fiscal indicators and balance sheet.

- OBEGAL financing costs relate to the interest on the change in Gross Sovereign-issued debt from the settlement date of the transaction.

- The Treasury is currently working through changes to key fiscal indicators and the effect of those changes is not yet known.

Impact on Crown debt of different transactions ($ millions)	[25], [33], [37], [38]
Gross sovereign-issued debt[1] Net core Crown debt (excluding NZSF fund and advances) OBEGAL financing cost (from FY23)[2]	

[1] Debt calculated after assumed special dividend from NZ Post

[33], [37], [38]

Note that negative figures in the debt lines in the table represent net funds coming into the Core Crown (and reducing debt)

If the Crown acquires a controlling interest, it will borrow externally to fund the acquisition from the existing KGH shareholders but, we expect, would receive a portion of the funds back from NZ Post in the form of a special dividend. The Crown would then incur funding costs on borrowings in future financial periods. Although not currently controlled by any one shareholder, because the Crown has an effective 100% interest in the company, KGH is fully consolidated into the Crown accounts. Therefore, at this stage it appears unlikely that a move to direct control by the Crown would significantly change balance sheet composition if KGH continues to be line-by-line accounted for because it is already consolidated (other than increasing total assets and liabilities by the amount borrowed). The specifics regarding accounting are being investigated and we will advise you if there is any change in this expectation.

[33], [37], [38]

If NZSF acquires a majority interest it will fund this through the divestment of other portfolio holdings or the redirection of already known inflows of funds. Thus, there is no net change from NZSF's overall funds and investment perspective. The reduction in net core Crown debt arises through the expected payment of a special dividend by NZ Post. [33], [37], [38]

Key fiscal indicators will be affected differently depending on how certain matters are accounted for. This is still being worked through with NZSF.

All scenarios are dependent on agreement being reached on a price/prices for transactions between existing KGH shareholders. It is possible that agreement cannot be reached on price. However, in the above tables we have only included one such scenario – that of ACC remaining a shareholder – where agreement on a price for a transaction with ACC is not reached and ACC therefore remains a shareholder in the meantime.

NZ Post

[25]

Treasury officials are currently engaging with NZ Post regarding appropriate capital and financial structuring arrangements going forward. These discussions include consideration of post-KGH divestment arrangements including the payment of a special dividend. For calculating the financial impact on the Crown in this report, we have simply assumed that NZ Post retains [25], [33], [38] of its investment in KGH. This is based on initial high-level discussions with the company regarding its forward capital plans (such as further investment in its parcels network), costs to restructure the mail business as the networks are integrated, and other potential investment opportunities. We note that this is an initial high-level estimate and we are engaging further with NZ Post to understand its position on the appropriate future debt levels for the company as losses from the mail business are resolved and profitability from the parcels business grows.

NZSF and ACC

[25]

[34]

KGH future capital requirements

The above calculations only allow for the next set of transactions to rearrange the ownership of already issued shares in KGH. They do not allow for the matter of additional capital that KGH is expected to require if it is to both gain market share and meet the Reserve Bank of New Zealand's (RBNZ's) new regulatory requirements for registered banks capital (which transition in over the six years to 1 July 2028).

We have undertaken estimates for additional capital requirements using the following assumptions:

- Profitability over the next few years remains at current levels
- The Te Ara Hou transformation project is completed on-time and on budget
- [25]
-

[25]

[25], [34]

Other financial reporting considerations

KGH is currently fully consolidated into the Crown accounts as it is 100% Crown-owned even though it is not controlled by any of its shareholders. In effect KGH is consolidated through the State-Owned enterprises (SOEs) segment (as the largest shareholder, NZ Post, is an SOE).

If NZSF became the majority shareholder it will need to work through whether it continues to meet the criteria to be accounted for as an investment entity (as outlined in the New Zealand equivalent to the International Financial Reporting Standard 10 for Consolidated Financial Statements (NZ IFRS 10)). We have engaged with NZSF on this matter but in the meantime, we have based the analysis of impacts on the Crown financial accounts on the assumption that separate reporting of KGH remains in place and the Crown continues to line-by-line consolidate KGH into its financial statements.

Once NZSF has sufficiently advanced its position on this matter we will update our advice to you – whether or not it results in some changes to the numbers.

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