---------- Forwarded message ---------
From: <[redacted]
Date: Mon, 8 Apr 2024 at 16:13
Subject: rate cap
To: [redacted] <[redacted]>

Please find appended.

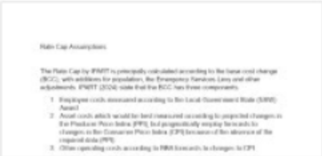
Please provide any feedback.

After considering your feedback I will provide a final note for your records.

Best Regards,

[redacted]

One attachment • Scanned by Gmail Security Sandbox



8.4.24 Rate Cap A...

Thanks for that. | Thanks for this. | Thanks, I'll take a look.

Reply | Forward

Rate Cap Assumptions.

The Rate Cap by IPART is principally calculated according to the base cost change (BCC), with additions for population, the Emergency Services Levy and other adjustments. IPART (2024) state that the BCC has three components:

1. Employee costs measured according to the Local Government State (NSW) Award
2. Asset costs which would be best measured according to projected changes in the Producer Price Index (PPI), but pragmatically employ forecasts to changes in the Consumer Price Index (CPI) because of the absence of the required data (PPI).
3. Other operating costs according to RBA forecasts to changes to CPI.

The IPART recommends that councils use 2.5 percent for the assumed rate peg. However, in the current environment our professional opinion is that this number would materially under-estimate the actual likely peg and therefore create a deficiency in revenue related to a future SRV.

For the 2024-25 financial year IPART declared rate pegs ranging from 4.5% through to 5.5%. Employee costs were expected to rise by 4.5%, asset costs were forecast to rise by 4.0% and other operating costs forecast at 3.2%.

At the time of writing (and calculating the required SRV) the RBA *Statement on Monetary Policy* (February 2024) states that 'inflation is expected to decline to the 2-3 per cent target range in 2025 and to reach the midpoint in 2026'. The graph accompanying this statement suggests that inflation would still be marginally above 3 percent in June 2025, but close to 2.5 percent in June 2026. The RBA (2024) proceeds to observe that 'services inflation is still high and is expected to decline only gradually. Goods price inflation has declined faster than expected, both here and in a number of other economies'.

Things have clearly changed since this time. For instance, according to Bloomberg, the Crude Oil price on the first of February was $US78.70. The Crude Oil price on the 8th of April was $US89.77. Oil is an important driver of inflation – especially in rural areas – because of transport costs that ultimately get passed on to consumers.

Indeed, a range of commodity prices have increased since this time – most notably copper which was $US385.35/lb on the 1st February, but is $US423.20 today.

Thus, much of the positive trends that the RBA observed in February have broken down.

Furthermore, it is a well-known fact to economists that central banks will 'jawbone' down inflation forecasts in a high inflation environment to prevent expectations from becoming un-anchored (which is counter-productive to the job of returning inflation to the legislated range). Actual 'realistic' projections might therefore be well higher than published.

In addition, few people have fully comprehended the effect of enterprise bargaining agreements in prolonging this current bout of inflation, relative to historical examples. Moreover, most *bona fide* economists agree that current geo-political risks, friendshoring, and green-shoring are all inflationary in nature.

As a professor of economics, I find it extremely doubtful that the RBA will be able to return to the legislated inflation range mandate by the stipulated period. Indeed, I expect that inflation will be persistent for many years to come, and will even increase from current levels.

The *minimum* rate peg that I would advocate for over the current LTFP is 3.5%. This is reflective of my belief that in the near-term the RBA projections will prove false - noting that they have indeed missed by a very large margin in recent years (RBA, 2024b). For the next three years I would be comfortable with Council assuming a rate cap of 4 to 4.5 percent. For the remaining seven years, I would recommend a cap no less than 3.5%. In these later years, I anticipate a positive growth factor might emerge.

Ultimately, no-one is able to precisely predict the rate cap, but it is very unlikely that 2.5 percent would prove reasonable over the entire ten years.

IPART (2024). *Rate Peg for NSW Councils for 2024-25*. IPART: Sydney.

Reserve Bank of Australia (RBA) (2024). Statement on Monetary Policy – February 2024. Available at: https://www.rba.gov.au/publications/smp/2024/feb/. Accessed 7th of April, 2024.

Reserve bank of Australia (2024b). Historical Forecasts. Available at: https://www.rba.gov.au/statistics/historical-forecasts.html