DEBT PORTFOLIO MANAGER

The Debt Portfolio Manager (DPM) is a passive debt management service designed to effectively manage interest rate risk in a manner appropriate to a client's individual business requirements.

The DPM service is administratively efficient, automatically allocating a client's new debt and refinancing maturing debt, within separate portfolio(s) of term fixed rate and / or term floating rate loans, in accordance with the interest rate risk management settings established by the client. WATC can also assist clients in determining the interest rate risk management settings most appropriate for their business.

Key Features

Automated Debt Management Service: automatically refinances stock lines as they mature.

Efficient: removes the need for manual client instruction, single transaction request for each drawdown, secured online transactions via the WATC Client Portal.

Portfolio Diversification / Hedging Benefits: allocates debt throughout the portfolio, hedging is done by WATC resulting in reduced interest rate volatility, without the risks and costs associated with using derivative instruments.

Minimise Risks: Refinancing and interest rate risks are kept to a minimum. Ability to match the nature of client's borrowing requirements, the term of financial assets and future cash flows.

Stability: The fixed rate debt portfolio provides stability in clients' effective interest rate from quarter to quarter.

Variability: Enables lower portfolio cost over the longer term by using term floating rate debt.

Parameters

Portfolio Maximum Term:

- Term fixed rate: 12 years
- Term floating rate: 6 years

Balance: quarterly 'stock lines' of term fixed or term floating rate loans spread evenly out to the maximum maturity.

- Term fixed rate: up to 48 stock lines
- Term floating rate: up to 24 stock lines

Interest: paid quarterly on maturity dates of the stock lines on the first month of each quarter being January, April, July and October:

- Term fixed rate: 15th of the quarter
- Term floating rate: 21st of the quarter

Repayment of Debt at Face Value: available up to the amount of the maturing stock lines on maturity dates.

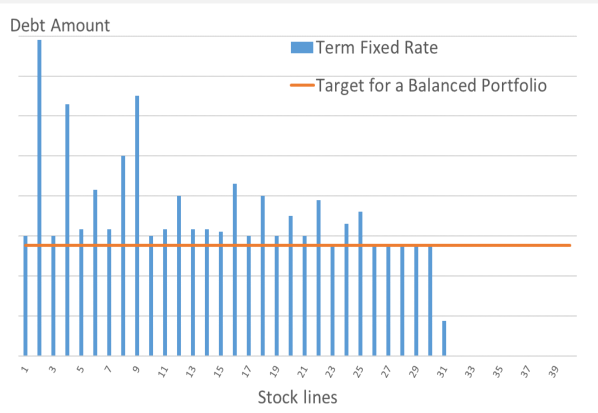
> *"The DPM is an excellent service balancing and diversifying our debt portfolio with minimal effort. It saves significant time by removing both the need to individually allocate maturities and the associated administrative effort. Using a portfolio approach, with a mix of Fixed and Floating rate debt, provides assurance of expected interest costs, as well as benefiting from lower interest rates with the use of Floating rate debt."*
>
> ***Patrice Domingue - Horizon Power***

Example

Transition from a 100% Fixed Debt Portfolio to a Balanced 70%10-year Fixed and 30% 5-year Floating DPM

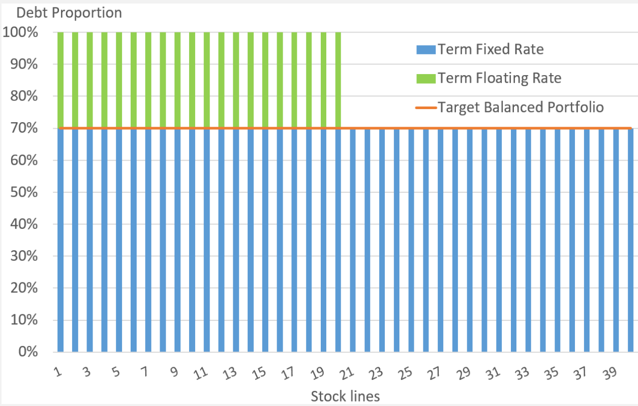
Prior to using DPM

Unbalanced portfolio with uneven maturities



Transition to DPM

Balanced portfolio, even stock lines



WESTERN AUSTRALIAN
TREASURY CORPORATION

An Efficient Debt Portfolio: The 'Efficient Frontier' Concept

"Efficient" Debt Portfolio	Efficient Frontier
Defined from a risk / return perspective, is a portfolio with a debt product combination that either: • minimises risk for an expected level of interest cost; or • minimises expected interest cost for a desired level of risk.	Defines the set of portfolio product weights that achieve either: • the lowest risk (i.e. measured by the volatility of year-on-year changes in interest costs) for a given expected cost (measured as average interest rate over the analysis period); or • the lowest expected cost for an assumed level of risk.

In the absence of a clearly defined revenue framework that has direct links to debt financing (*e.g. charging is based on weighted average cost of capital (WACC) or other contractual cost recovery principles*), an agency's debt management strategy should ideally ***target a debt portfolio mix between fixed and floating rate debt that lies on the Efficient Frontier.***

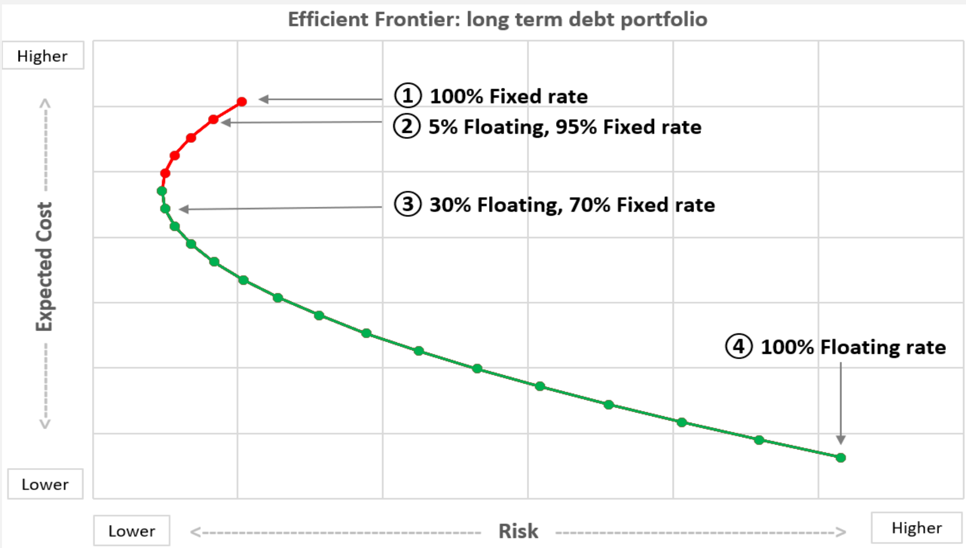
WATC Research

Applicable to Agencies with Debt Portfolios Expected to be Maintained for the Foreseeable Future

The core component of the research is the modelling of historical data on market interest rates to assess the optimal product weights between a portfolio of:

- term floating rate debt with quarterly interest rate resets out to five years maturity; and
- term fixed rate debt diversified in quarterly maturities out to a ten-year term.

Summary Outcome of Most Recent WATC Modelling – Optimal Product Weights



Plotted on the graph are portfolios with different weightings of fixed and floating rate debt:

- 'Inefficient' portfolio because for each combination represented with a red dot, there exists an alternative combination (i.e. green portion) with the same risk but lower expected cost.
- Portfolio combinations of floating and fixed rate debt that lie on the Efficient Frontier.
- ① 100% Fixed rate portfolio: highest expected cost portfolio but not lowest risk.
- ② Each successive dot reflects adding an additional 5% of floating rate debt to the portfolio leading to lower expected cost.
- ③ 30% Floating/70% Fixed is an "Efficient" portfolio: minimises expected cost at a low level of risk.
- ④ 100% Floating rate: Lower expected cost with higher level of risk.

Accessing WATC's Services

WATC's services are available to all WA State government entities and local governments. For more information on WATC services, please visit the WATC website www.watc.wa.gov.au/client-services/ or contact WATC to discuss your business requirements.

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