Treasury Management Strategy Statement (Revised June 2016)

Minimum Revenue Provision Policy Statement and Annual Investment Strategy

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1 INTRODUCTION

1.1 Background

The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

CIPFA defines treasury management as:

> *"The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."*

1.2 Reporting requirements

The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

Prudential and treasury indicators and treasury strategy (this report) - The first, and most important report covers:

- the capital plans (including prudential indicators);
- a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);
- the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

A mid year treasury management report – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether any policies require revision

An annual treasury report – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

Scrutiny

The above reports are required to be adequately scrutinised before being recommended to Full Council. This role is undertaken by the Corporate Governance and Finance Committee.

1.3 Treasury Management Strategy for 2016/17

The strategy for 2016/17 covers two main areas:

Capital issues

- the capital plans and the prudential indicators;
- the minimum revenue provision (MRP) policy.

Treasury management issues

- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- the investment strategy;
- creditworthiness policy; and
- policy on use of external service providers.

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, CLG MRP Guidance, the CIPFA Treasury Management Code and CLG Investment Guidance.

1.4 Training

The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsibe for scrutiny.

The training needs of treasury management officers are periodically reviewed.

1.5 Treasury management consultants

The Council uses Capita Asset Services, Treasury solutions as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

2 THE CAPITAL PRUDENTIAL INDICATORS 2016/17 – 2018/19

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

2.1 Capital expenditure

This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts: (note these include the loan financing of up to £5 million for the LATC, and full funding for the leisure centre project).

Capital expenditure £'000	2015/16 Actual	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Total	**1,051**	**8,397**	**12,721**	**490**

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Capital expenditure £'000	2015/16 Actual	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Total	**1,051**	**8,397**	**12,721**	**490**
Financed by:				
Capital grants	260	473	1,700	200
Capital reserves / receipts	688	2,906	1,057	261
Revenue	103	735	29	29
Net financing need for the year	**0**	**4,283**	**9,935**	**0**

2.2 The Council's borrowing need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with estimated life of each individual asset.

The CFR includes any other long term liabilities. Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes.

The Council is being requested to approve the capital scheme to develop a new district wide leisure facility. The implications of both of these projects are incorporated into this revised Treasury Management Strategy.

The Council is asked to approve the CFR projections below:

£'000	2015/16 Actual	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Total CFR	**(2)**	**4,281**	**14,216**	**13,781**
Movement in CFR	**(22)**	**4,283**	**9,935**	**(435)**

Net financing need for the year (above)	0	4,283	9,935	0
Less MRP/VRP and other financing movements	(22)	0	0	435
Movement in CFR	**(22)**	**4,283**	**9,935**	**(435)**

2.3 Minimum revenue provision (MRP) policy statement

In most cases, the Council is required to pay off an element of the accumulated capital spend each year (the CFR) through a revenue charge (the minimum revenue provision - MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

CLG regulations have been issued which require Full Council to approve **an MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement.

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

- **Asset life method** – MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction)

These options provide for a reduction in the borrowing need over approximately the asset's life. With regard to the Council's new Leisure Centre, the minimum estimated life is projected to be 25 years; with the fixtures and fittings at 10 years. The Council will therefore adapt these periods for the Leisure Centre. If it becomes apparent that the minimum life of the assets exceeds these, consideration will be given to a longer MRP period.

Repayments included in annual finance leases are applied as MRP.

With regard to the loan to the LATC, as the capital spend relates to a short-term loan arrangement to the LATC, the policy will be to not charge any MRP to the revenue account as the full repayment of the loan will be received from the LATC within five years.

2.4 Core funds and expected investment balances

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.).

Projected level of cash balances (at the end of each financial year) are set out below

£'000	2015/16 Actual	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Revenue Reserves	8,119	7,902	7,163	5,480
S106 / CIL	5,450	5,644	5,644	5,644
Capital Receipts reserves	2,722	16	64	3
Cash (Debtor / Creditors)	3,400	3,400	3,400	3,400
Internal borrowings	0	(4,283)	(14,218)	(13,795)
Total Investments	**19,691**	**12,679**	**2,053**	**732**

In as much as the table shows the Council having funds to invest, this will gradually reduce over the years as the reserves and receipts are utilised, there are strong internal balances to fund all known capital costs from internal cash balances.

The above projections include full funding of the leisure centre, and the LATC up to a maximum value of £5 million. Projections show that cash balances will become minimal, and although the Leisure Centre will be repaying its loan (at £423,000 per annum) this is likely to be offset by further use of revenue reserves to fund the MTFS.

The loan to the LATC is repayable in full in FY 2021/22, so this will increase cash balances at that time by a further £5 million.

2.5 Affordability prudential indicators

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators:

2.6 Ratio of financing costs to net revenue stream

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

%	2015/16 Actual	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Net Revenue Budget	£8,553k	£8,331k	£9,056k	£9,284k
Ratio	0.27%	-0.46%	-0.65%	-0.08%

The estimates of financing costs include current commitments and the proposals in this budget report, which does include the LATC funding interest payments on the loan and the interest costs for internal borrowing to fund the leisure centre..

2.7 Incremental impact of capital investment decisions on Council Tax

This indicator identifies the revenue costs associated with proposed changes to the capital programme recommended in this budget report compared to the Council's existing approved commitments and current plans. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support.

Incremental impact of capital investment decisions on the band D council tax

£	2015/16 Actual	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Council tax band D – tax base	28,263.0	28,682.1	29,107.4	29,539.1
Change in Council Tax – Band D	-82p	134p	201p	25p

3 BORROWING

The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

3.1 Current portfolio position

The Council's treasury portfolio position at 31 March 2016, with forward projections, are summarised below. The table shows the actual external debt (the treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

£'000	2015/16 Actual	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Debt at 1 April	0	0	0	0
Expected change in Debt	0	0	0	0
Other long-term liabilities (OLTL)	22	0	0	0
Expected change in OLTL	22	0	0	0
Actual gross debt at 31 March	**0**	**0**	**0**	**0**
The Capital Financing Requirement	**(2)**	**4,281**	**14,216**	**13,781**
Under / (over) borrowing	**(24)**	**4,281**	**14,216**	**13,781**

Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2016/17 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Chief Finance Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

3.2 Treasury Indicators: limits to borrowing activity

The Operational boundary: This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

Operational boundary £'000	2015/16 Actual	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Debt	0	0	0	0
Other long term liabilities	(2)	0	0	0
Total	(2)	0	0	0

The authorised limit for external debt A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

1. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.
2. The Council is asked to approve the following authorised limit:

Authorised limit £'000	2015/16 Actual	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Debt	5,000	5,000	5,000	5,000
Other long term liabilities	(2)	0	0	0
Total	4,998	5,000	5,000	5,000

3.3 Prospects for interest rates

The Council has appointed Capita Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives our central view.

UK Interest Rate Forecast

Bank Rate	NOW	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Capita Asset Services	0.50%	0.50%	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.25%	1.50%	1.50%	1.75%
Capital Economics	0.50%	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	-	-	-	-	-

5yr PWLB Rate	NOW	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Capita Asset Services	1.52%	1.90%	2.00%	2.10%	2.20%	2.30%	2.40%	2.60%	2.70%	2.80%	2.90%	3.00%	3.10%
Capital Economics	1.52%	1.85%	2.10%	2.35%	2.80%	2.80%	3.15%	3.15%	-	-	-	-	-

10yr PWLB Rate	NOW	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Capita Asset Services	2.11%	2.40%	2.50%	2.60%	2.70%	2.80%	2.90%	3.00%	3.10%	3.30%	3.40%	3.50%	3.60%
Capital Economics	2.11%	2.30%	2.55%	2.80%	3.05%	3.05%	3.30%	3.30%	-	-	-	-	-

25yr PWLB Rate	NOW	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Capita Asset Services	2.89%	3.20%	3.30%	3.30%	3.50%	3.50%	3.60%	3.60%	3.70%	3.70%	3.70%	3.80%	3.80%
Capital Economics	2.89%	3.15%	3.30%	3.40%	3.50%	3.50%	3.65%	3.65%	-	-	-	-	-

50yr PWLB Rate	NOW	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Capita Asset Services	2.63%	3.00%	3.10%	3.10%	3.30%	3.30%	3.40%	3.40%	3.50%	3.60%	3.60%	3.70%	3.70%
Capital Economics	2.63%	3.30%	3.45%	3.55%	3.65%	3.65%	3.80%	3.80%	-	-	-	-	-

3.4 Capita Asset Services Forward View

Market expectations for the first increase in Bank Rate moved considerably during the last year, with bank rate not forecast to rise until early-2017. There are continuing fears that any increase could be pushed further back into 2018 due to market concerns regarding global economic growth, uncertainty around the UK economy ahead of the EU Referendum, continuing Eurozone growth uncertainties and few signs of inflationary pressures in the wider global economy.

Economic growth projections have recently been downgraded and these concerns have caused sharp market volatility in equity prices during the year with corresponding impacts on bond prices and bond yields due to safe haven flow. The overall dominant trend in bond yields since July 2015 has been for yields to fall to historically low levels as forecasts for inflation have repeatedly been revised downwards and expectations of increases in central rates have been pushed back. In addition, a notable trend was that several European central banks introduced negative interest rates as a measure to stimulate the creation of credit and hence economic growth. The European Central Bank commenced a full blown quantitative easing programme of purchases of Eurozone government and other bonds starting in March at €60bn per month. This put downward pressure on Eurozone bond yields. There was a further increase in this programme of quantitative easing announced in December 2015.

As for the America, the economy has continued to grow on the back of resilient consumer demand. The first increase in the central bank rate occurred in December 2015, since when there has been a return to caution as to the speed of further rate increases, due to concerns around the risks to world growth. Expectations of a further two or three interest rises in the US during 2016 have now been deferred, with the next increase likely to be pushed back to September 2016, if at all.

From a borrowing perspective, the recent flows of investor funds to safe havens has seen UK gilt yields fall to record lows, with consequential reductions in PWLB borrowing rates. As at mid-June, 50-year borrowing rates were down as low as 2.58%, ahead of the EU Referendum decision. The referendum vote places further uncertainty on the economic outlook for the UK and this is likely to lead to continued volatility in PWLB rates which the Council, with support from its treasury management advisors Capita Asset Services, will continue to monitor. If suitable opportunities arise to borrow externally and lock in to historic low rates, then the Council may borrow accordingly, in line with the Treasury Management Strategy outlined within this report.

However, due to the current low level of investment rates and the potential additional cost of borrowing, in the short-term the Council will continue to borrow internally as outlined in the Treasury Management Strategy Statement approved in February 2016.

3.5 Borrowing Strategy

Previously, it has been assumed that funding the LATC will be done via external debt. However, due to the significant improvement in the Council's cash position, it is projected that external debt can be avoided.

In using internal cash balances to fund the full borrowing requirements for the Council, the Council will be in an under-borrowed postion. This means that the Council has not exposed itself to external debt- with potentially higher rates of interest. However, should the level of cash balances reduce further, then the Council will consider raising debt externally. Such a decision will be made based on the projections at the time.

There will essentially be two funding options when the Council makes its decision>

- Raise funding externally : Interest rates are currently low but predicted to rise in the coming years. Any borrowing cost will exceed interest earned on cash investment, so will only be undertaken with clear cash projections and full Council approval.

- Alternatively the council could use the combination of both internal and external funding: by using core internal funds to finance the Leisure centre and LATC, with both paying back the borrowed funds with interest to an agreed time frame.

Treasury management limits on activity

There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs / improve performance. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates;
- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

The Council is asked to approve the following treasury indicators and limits:

£million	**2016/17**	**2017/18**	**2018/19**
Interest rate exposures			
	Upper	**Upper**	**Upper**
Limits on fixed interest rates based on net debt	25	25	25
Limits on variable interest rates based on net debt	25	25	25
Maturity structure of fixed interest rate borrowing 2016/17			
		Lower	**Upper**
Under 12 months		0%	100%
12 months to 2 years		0%	100%
2 years to 5 years		0%	100%
5 years to 10 years		0%	100%
10 years to 20 years		0%	100%
20 years to 30 years		0%	100%
30 years to 40 years		0%	100%
40 years to 50 years		0%	100%
Maturity structure of variable interest rate borrowing 2016/17			
		Lower	Upper
Under 12 months		0%	100%
12 months to 2 years		0%	100%
2 years to 5 years		0%	100%
5 years to 10 years		0%	100%
10 years to 20 years		0%	100%
20 years to 30 years		0%	100%
30 years to 40 years		0%	100%
40 years to 50 years		0%	100%

3.6 Policy on borrowing in advance of need

The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

4 ANNUAL INVESTMENT STRATEGY

Introduction: changes to credit rating methodology

The main rating agencies (Fitch, Moody's and Standard & Poor's) have, through much of the financial crisis, provided some institutions with a ratings "uplift" due to implied levels of sovereign support. Commencing in 2015, in response to the evolving regulatory regime, all three agencies have begun removing these "uplifts" with the timing of the process determined by regulatory progress at the national level. The process has been part of a wider reassessment of methodologies by each of the rating agencies. In addition to the removal of implied support, new methodologies are now taking into account additional factors, such as regulatory capital levels. In some cases, these factors have "netted" each other off, to leave underlying ratings either unchanged or little changed. A consequence of these new methodologies is that they have also lowered the importance of the (Fitch) Support and Viability ratings and have seen the (Moody's) Financial Strength rating withdrawn by the agency.

In keeping with the agencies' new methodologies, the rating element of our own credit assessment process now focuses solely on the Short and Long Term ratings of an institution. While this is the same process that has always been used for Standard & Poor's, this has been a change in the use of Fitch and Moody's ratings. It is important to stress that the other key elements to our process, namely the assessment of Rating Watch and Outlook information as well as the Credit Default Swap (CDS) overlay have not been changed.

The evolving regulatory environment, in tandem with the rating agencies' new methodologies also means that sovereign ratings are now of lesser importance in the assessment process. Where through the crisis, clients typically assigned the highest sovereign rating to their criteria, the new regulatory environment is attempting to break the link between sovereign support and domestic financial institutions. While this authority understands the changes that have taken place. This is in relation to the fact that the underlying domestic and where appropriate, international, economic and wider political and social background will still have an influence on the ratings of a financial institution.

It is important to stress that these rating agency changes do not reflect any changes in the underlying status or credit quality of the institution. They are merely reflective of a reassessment of rating agency methodologies in light of enacted and future expected changes to the regulatory environment in which financial institutions operate. While some banks have received lower credit ratings as a result of these changes, this does not mean that they are suddenly less credit worthy than they were formerly. Rather, in the majority of cases, this mainly reflects the fact that implied sovereign government support has effectively been withdrawn from banks. They are now expected to have sufficiently strong balance sheets to be able to withstand foreseeable adverse financial circumstances without government support. In fact, in many cases, the balance sheets of banks are now much more robust than they were before the 2008 financial crisis when they had higher ratings than now. However, this is not universally applicable, leaving some entities with modestly lower ratings than they had through much of the "support" phase of the financial crisis.

4.1 Investment policy

The Council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second, then return.

In accordance with the above guidance from the CLG and CIPFA, and in order to minimise the risk to investments, the Council applies minimum acceptable credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

Ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.

Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

Investment instruments identified for use in the financial year are listed in appendix 5.3 under the 'specified' and 'non-specified' investments categories. Counterparty limits will be as set through the Council's treasury management practices – schedules.

4.2 Creditworthiness policy

This Council applies the creditworthiness service provided by Capita Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- CDS spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, credit Watches and credit Outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands

- Yellow 5 years
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 100 days
- No colour not to be used

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour

The Capita Asset Services' creditworthiness service uses a wider array of information than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

Typically the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored **weekly**. The Council is alerted to changes to ratings of all three agencies through its use of the Capita Asset Services' creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Capita Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information, information on any external support for banks to help support its decision making process.

4.3 Counterparty Limits

The following counterparty limits were agreed on 26th February 2016.

- £6m with counterparties rated 6 months to 1 year (Orange) durational limit
- £5m with Money market Funds
- £4m with counterparties rated 3-months (green) durational limit on the approved weekly list

4.4 Country and sector limits

The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch or equivalent. The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 5.2. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

4.5 Investment strategy

The Council continues to hold cash balances and is able to meet the loan requirements of the LATC and the leisure centre without recourse to external borrowing. The cashflow projection of the LATC and the leisure centre enables the council to make investments in fixed terms deposits, which generates greater investment interest.

Previously, it had been assumed that the Council would raise funds through external debt. With the cash projections improving, then this is not required. However, it will mean that cash balances will reduce to minimal levels, and as such, the ability to invest sizeable sums in longer term deposits will cease.

In-house funds. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

Investment returns expectations. Bank Rate is forecast to remain unchanged at 0.5% before starting to rise in quarter 1 of 2017. Bank Rate forecasts for financial year ends (March) are:

- 2016/17 0.75%
- 2017/18 1.25%
- 2018/19 1.75%

The suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during each financial year for the next eight years are as follows:

2016/17 0.60%
2017/18 1.25%
2018/19 1.75%
2019/20 2.00%
2020/21 2.25%
2021/22 2.50%
2022/23 2.75%
2023/24 2.75%
Later years 3.00%

The overall balance of risks to these forecasts is currently to the downside (i.e. start of increases in Bank Rate occurs later). However, should the pace of growth quicken and / or forecasts for increases in inflation rise, there could be an upside risk.

Investment treasury indicator and limit - total principal funds invested for greater than 364 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

The Council is asked to approve the treasury indicator and limit: -

Maximum principal sums invested > 364 days			
£m	**2016/17**	**2017/18**	**2018/19**
Principal sums invested > 364 days	£3m	£3m	£3m

For its cash flow generated balances, the Council will seek to utilise its business reserve instant access and notice accounts, money market funds and short-dated deposits (overnight to100 days) in order to benefit from the compounding of interest.

4.6 Investment risk benchmarking

This Council will use an investment benchmark to assess the investment performance of its investment portfolio of 3 month LIBID compounded

4.7 End of year investment report

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

APPENDIX

1. Treasury management practice 1 – credit and counterparty risk management
2. Approved countries for investments
3. Treasury management scheme of delegation
4. The treasury management role of the Section 151 officer

APPENDIX 1

Treasury Management Practice (TMP1) – Credit and Counterparty Risk Management

SPECIFIED INVESTMENTS: All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' quality criteria where applicable.

NON-SPECIFIED INVESTMENTS: These are any investments which do not meet the specified investment criteria. A maximum of 75% will be held in aggregate in non-specified investment

A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the above categories.

The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

	Minimum credit criteria / colour band	**Max % of total investments/ £ limit per institution**	**Max. maturity period**
DMADF – UK Government	N/A	**100%**	**6 months**
Money market funds	AAA	100%	Liquid
Local authorities	N/A	100%	12 months
Term deposits with banks and building societies	Blue Orange Red Green No Colour		12 months 12 months 6 months 100 days Not for use

SPECIFIED INVESTMENTS:
(All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' rating criteria where applicable)

	Minimum 'High' Credit Criteria	**Use**
Debt Management Agency Deposit Facility	--	In-house
Term deposits – local authorities	--	In-house
Term deposits – banks and building societies	Green	In-house

Term deposits with nationalised banks and banks and building societies

	* Minimum Credit Criteria	Use	Max % of total investments	Max. maturity period
UK part nationalised banks	Blue	In-house	100%	1 year
Banks part nationalised by high credit rated (sovereign rating) countries – non UK	Sovereign rating or Short-term F1, Long-term A-, Sovereign rating AA	In-house	3m	1 year

Collective Investment Schemes structured as Open Ended Investment Companies (OEICs): -		
Money Market Funds	MMF rating	In-house and Fund Managers

Accounting treatment of investments: The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

NON-SPECIFIED INVESTMENTS: A maximum £3 million will be held in aggregate in non-specified investment

1. Maturities of ANY period

	Minimum Credit Criteria	Use	Max % of total investments	Max. maturity period
Fixed term deposits with variable rate and variable maturities: - Structured deposits	See note 1	In-house	3m	2 Years

2. Maturities in excess of 1 year

	Minimum Credit Criteria	Use	Max % of total investments	Max. maturity period
Term deposits – local authorities	--	In-house	3m	Unlimited
Term deposits – banks and building societies	Purple	In-house	3m	2 Years

APPENDIX 2 : Approved countries for investments

AAA

- Australia
- Canada
- Denmark
- Germany
- Singapore
- Sweden
- Switzerland
- Netherlands

AA+

- Finland
- U.K.
- U.S.A.

AA

- Abu Dhabi (UAE)
- France
- Qatar

AA-

- Belgium

APPENDIX 3

Treasury management scheme of delegation

(i) Full board/council

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.

(ii) Corporate Governance & Finance Committee

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
- budget consideration and approval;
- approval of the division of responsibilities;
- receiving and reviewing regular monitoring reports and acting on recommendations;
- approving the selection of external service providers and agreeing terms of appointment.

(iii) Chief Finance Officer

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

APPENDIX 4

The treasury management role of the Section 151 officer

The Chief Finance Officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers.