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Treasury Management Strategy

The County Council of the City and County of Cardiff

2015/16

CARDIFF
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CONTENTS

FOREWORD

Treasury Management activities are the management of an organisation'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.

The Council carries out its treasury management activities in accordance with a code developed for public services in 2011 by the Chartered Institute of Public Finance and Accountancy (CIPFA). This publication provides information on the Council's proposed Treasury Management Strategy to be adopted during 2015/16. The strategy is to be included in the Budget Proposals Report 2015/16 to be recommended for approval by Council, then published in accordance with Welsh Government Guidance. A glossary of terms is included at Appendix 1.

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Treasury Management

1. Treasury management involves ensuring cash is available when needed; investing temporary cash balances and ensuring appropriate borrowing facilities to pay for the Council's capital expenditure plans and for the prudent management of its financial affairs.

2. The Council carries out its treasury management activities in accordance with the revised treasury management code of practice developed for public services in 2011 by the Chartered Institute of Public Finance and Accountancy (CIPFA). This requires the Council to set out the policies and objectives of its treasury management activities and adopt four Clauses of Treasury Management. These were formally adopted by the Council in February 2010.

3. The Council's Audit Committee undertakes scrutiny of the accounting, audit and commercial issues in relation to the Council's Treasury Management Strategy and practices.

4. During the course of each year, a number of reports are produced in relation to the Council's treasury management activities including a strategy at the start of the year, performance reports during the year, a mid year report and an outturn report.

Treasury Management Strategy

5. It is accepted that no treasury management activity is without risk. In undertaking its treasury management activities, the overriding objective is to minimise the risk of adverse consequences or loss, whilst at the same time not unduly constraining investment returns or unnecessarily incurring interest costs.

6. The successful identification, monitoring and control of risk are integral elements of treasury management activities. Risks include credit and counterparty, liquidity, interest rate, refinancing, fraud and regulatory. The Council has Treasury Management Practices to address and mitigate these risks. The practices were last updated in April 2014 following a review by Internal Audit and Audit Committee

7. The Council recognises the value in the use of treasury advisors to support the management of risk and to access specialist skills and resources. Support provided includes advice on timing of decision making, training, credit updates, economic forecasts, research, articles and advice on capital finance, with the terms of appointment reviewed periodically. Responsibility for treasury decisions ultimately remains with the Council.

8. The following paragraphs set out the integrated strategy for borrowing and investments for 2015/16. The strategy covers:

- The current treasury position.
- Economic background and prospects for interest rates.
- Borrowing, including:-
    - Policy
    - Annual Minimum Revenue Provision (MRP) Policy Statement
    - Housing Finance Reform Settlement Amount (Self Financing Buyout) and Treasury Management Implications
    - Council borrowing requirement and choice between internal and external borrowing and
    - Borrowing Strategy
- Treasury management indicators and limits for 2015/16 to 2017/18
- Investment policy and strategy, including security and investments approved for use.
- Training.

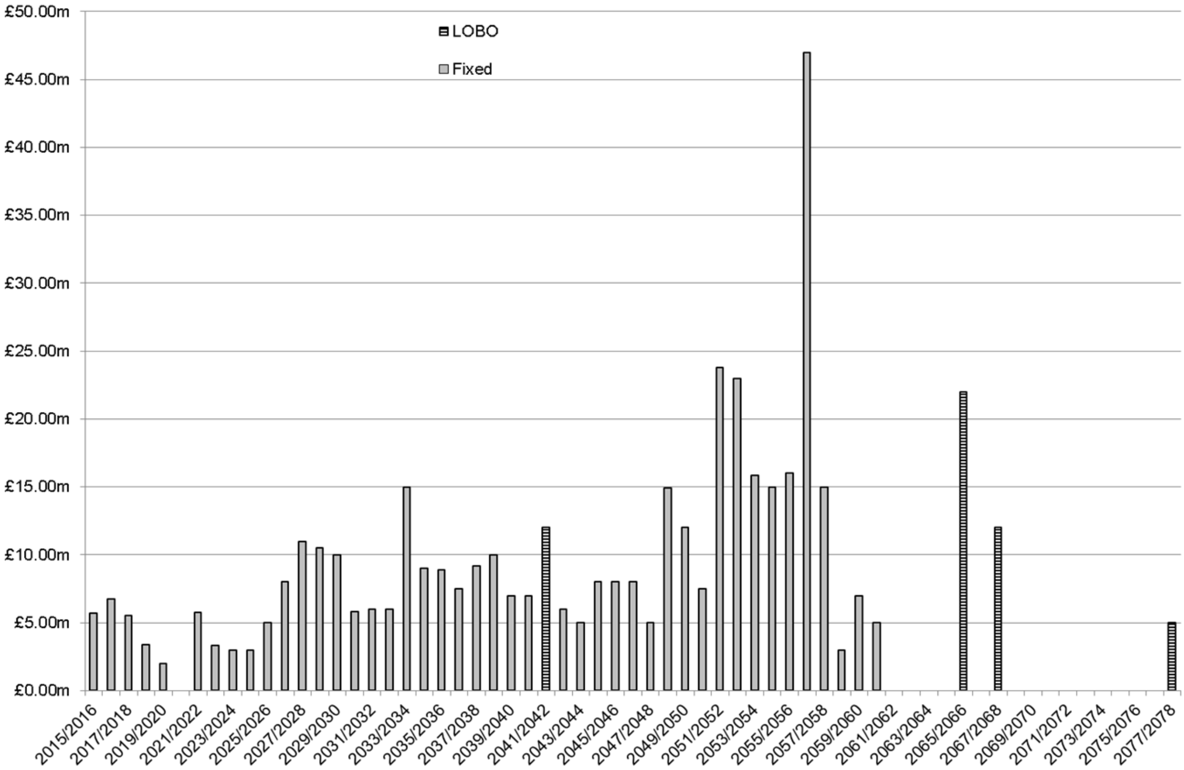
9. The proposed strategy is based on information known at the time of writing this report. Significant changes are to occur in 2015/16 in relation to additional borrowing, circa £222 million, required to meet obligations of Housing Finance Reform. There are unlikely to be significant changes in the proposed Capital Programme. However, whilst the principle of Housing Finance Reform has been agreed, the settlement value is to be based on interest rates at 31 March 2015. Any changes will be reported in future scheduled reports to Council, Cabinet and Audit Committee on Treasury Management during the course of the year.

The Treasury Position

10. The treasury position as at 31 December 2014 is shown in the following table. Borrowing is predominantly made up of fixed interest rate loans payable on maturity. Investments fluctuate daily and are represented by fixed term deposits, notice deposit accounts and money market funds. These balances arise due to the timing of cash flows and working capital as well as the existence of reserves, provisions and balances required for future use.

	Principal £m	**Average Rate %**
External Borrowing		
- Public Works Loan Board	423.7	5.35
- Market Loans	52.0	4.10
- Other	0.4	0.00
Total Debt	**476.1**	**5.21**
Treasury Investments	**70.9**	**0.66**

11. The Council's current debt maturity profile is shown in the following graph on the assumption that all loans run to their final maturity.



12. It should be noted that £24 million of the Lender Option Borrower Option loans (LOBOs) are currently subject to the lender potentially requesting a change in the rate of interest payable every six months, with a further £22 million having its five year call option which could trigger early repayment and possible need to borrow to refinance in 2015/16.

Lender Option Borrower Option (LOBO) Loans			
Potential Next Repayment Date	**Loan Value £m**	**Option Frequency Every**	**Full Term Maturity Date**
01/03/2015	6	6 months	23/05/2067
21/05/2015	6	6 months	21/11/2041
21/05/2015	6	6 months	21/11/2041
21/05/2015	6	6 months	23/05/2067
21/11/2015	22	5 years	23/11/2065
05/01/2018	5	5 years	17/01/2078

13. Risk of early repayment is deemed to be low, however in the longer-term, options will need to be considered to reduce any potential large repayments in a single year.

Economic background and prospects for Interest Rates

14. The following table gives the Council's treasury management advisors latest forecast of interest rates taking into account the 20 basis point certainty rate reduction available for PWLB loans to eligible local authorities. It is a central

forecast, acknowledging for example that the bank rate may rise sooner if there is sustained and robust UK growth, employment and inflation expectations.

	January 2015	March 2015	March 2016	March 2017	March 2018
Bank Rate	0.50%	0.50%	0.75%	1.25%	2.00%
5yr PWLB rate	2.00%	2.20%	2.60%	3.20%	3.60%
10yr PWLB rate	2.60%	2.80%	3.30%	3.80%	4.20%
25yr PWLB rate	3.30%	3.40%	4.00%	4.50%	4.80%
50yr PWLB rate	3.30%	3.40%	4.00%	4.50%	4.80%

Forecast at 5 January 2015

15. Whilst sentiment in financial markets has improved considerably during 2014, geopolitical events, political changes given the forthcoming UK general election and resurfacing of concerns of EU member states indebtedness are concerns. Growth in the UK economy has strengthened, inflation has fallen and credit conditions remain eased primarily due to the Funding for Lending Scheme. However there are concerns that any recovery based mainly on consumer spending and the housing market may not be sustainable.

16. The bank rate, which is unchanged since March 2009, is currently forecast to rise towards the end of 2015. Future borrowing costs are forecast to rise as a result of higher levels of UK Government borrowing and any reversal in quantitative easing undertaken by the Bank of England in the UK resulting in higher longer term revenue budget costs for the Council.

Borrowing

Policy

17. Borrowing has long-term financial consequences and risks, with decisions taken many years ago impacting currently and in the future. The costs of servicing borrowing is included in the Council's Capital Financing revenue budgets.

18. Borrowing is not undertaken for specific schemes or directorates. All loans are taken in the name of the Council and secured on all revenues of the Council. Loans and investments are pooled. The Council will aim to manage its debt portfolio on a long-term basis with a high regard to the effects on current and future Council Tax and Rent Payers.

19. The Council's borrowing strategy for 2015/16 and the capital financing revenue budgets included in the MTFP will consider all options to meet the long-term aims of:

- Promoting revenue cost stability to aid financial planning and avoid a stop-start approach to service delivery, although it is recognised that this may have a financial impact.

- Pooling borrowing and investments to ensure the whole Council shares the risks and rewards of treasury activities.
- Meeting the Council's commitment to Housing Finance Reform by paying a settlement amount to WG
- Reduction over time in the average rate of interest on overall Council borrowing.
- Ensuring any refinancing risk is manageable each financial year, using opportunities to re-profile borrowing where cost effective to do so both in the short and long term.
- Ensuring borrowing plans are aligned to known capital expenditure spending plans, the useful life of assets created and consistent with the prudent provision for the repayment of any such expenditure paid for by borrowing.

20. The Council will not borrow in advance of need, purely to profit from any investment of the extra sums borrowed. However, if it is felt that by borrowing in advance of need up to a maximum of three years, opportunities exist to lock into favourable long-term rates and the credit risks associated with this can be managed, then this is an option that will be considered.

Prudent Repayment of Capital Expenditure – Annual Minimum Revenue Provision (MRP) Policy Statement

21. Capital expenditure is budgeted expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, machinery. Such expenditure is spread over several years so as to try to match the benefits such assets provide over their useful life. The manner of spreading these costs over years is through an annual charge to the Council's revenue account known as MRP. The level of the MRP is determined using WG guidance and the judgement of the Section 151 Officer.

22. The WG requires that: - "A local authority must calculate for the current financial year an amount of MRP which it considers to be prudent." A statement on the Council's policy for its annual MRP is required to be submitted to full Council for approval before the start of the financial year to which the provision will relate.

23. It is proposed that the Council MRP Policy will be as follows with any change in the level, timing and method of provision in year delegated to the Section 151 Officer :

    - General Fund historic expenditure prior to 1 April 2004 as well as subsequent supported borrowing approved by the WG is to be provided for at 4.5% on a reducing balance basis. This is in excess of the WG minimum of 4%, but will continue to be reviewed for ongoing affordability.
    - HRA supported borrowing prior to self financing on 1 April 2015 is to be provided for at 2% on a reducing balance basis. MRP on the housing settlement payment to be made in 2015/16 is to be at 2% straight line basis as a minimum.

- Additional borrowing for a general increase in investment to balance the Capital Programme in a year is to be provided for on a straight line basis over the estimated average life of the assets created.
- Any additional expenditure linked to specific schemes e.g. Invest to Save, SOP etc. is to be provided for on a straight line basis, or over the estimated useful life of assets being created or a shorter period as determined by the Section 151 Officer or suggested periods determined by WG as is the case with Local Government Borrowing Initiative (LGBI).
- Revenue Provision in excess of minimum requirements can be made subject to affordability and following advice of the S151 officer. Where any additional voluntary revenue provision has been made from 2015/16 onwards, the Council may make an appropriate reduction in later years' levels of MRP after consideration of prudence and affordability.
- The MRP charged against liabilities under finance leases, or contracts that have the characteristics of finance leases, shall be equal to the principal element of the lease repayment, calculated on an annual basis.

Housing Finance Reform Settlement Amount (Self Financing Buyout)

<u>Agreed Position</u>

24. Currently, all eleven Welsh landlord authorities operate within a centralised HRA Subsidy system which is complex, out dated and where a "negative subsidy" is paid to the UK Treasury each year, circa £73.1 million. Cardiff's share of this is £14.9 million (20.4%) based on 2013/14 audited figures.

25. The UK and Welsh Government have reached an agreement that will allow Wales and the 11 Councils to leave the Subsidy system through a one off loan settlement payment to HM Treasury. This is to be based on an agreed interest figure of £40 million using PWLB rates applicable on 31 March 2015.

26. The overriding principle of subsidy reform is that no Welsh Authority will be worse off under the new Self Financing arrangements. The new arrangements will mean that from April 2015, the City of Cardiff Council will no longer have to pay a negative subsidy. Instead it will make a single one off settlement payment as a "buy out" to the UK Treasury on 2 April 2015.

27. Based on current interest rates, the all Wales settlement payment could be £1.090 billion with Cardiff's share of this total settlement figure at 20.4% being £222 million and circa £8.15 million in interest.

28. The agreement imposes a limit of indebtedness for each authority on HRA borrowing in accordance with the requirements of HM Treasury. This has been accepted by the Council in accordance with a Voluntary Agreement signed in January 2015.

29. The move to self financing offers the opportunity for authorities to use their role as a landlord to help achieve their wider priorities and ambitions within the context of the ring-fenced HRA. These could include economic regeneration, improving health and well being, improving community safety

and helping vulnerable people to live independently in the community. It will mean councils will retain all revenue and capital income and become responsible for financing their landlord services and housing investment from their income. English Authorities moved to self financing in April 2012.

30. Previous reports to Cabinet and Council during 2014/15 have provided members with information on housing reform including the treasury management implications. Council approved a delegation to officers in consultation with the Cabinet Members for Health, Housing and Wellbeing and for Corporate Services and Performance to conclude the appropriate detail within the voluntary agreement and sign on behalf of the Council.

<u>Treasury Management Implications - Borrowing</u>

31. Using the PWLB 30 year Maturity Rate loan interest rate (over 30 not over 30 ½ years) on the 31 March 2015, the WG will determine the value of loans (settlement amount) which notionally equates to an interest payment of £8.155 million The interest payment share remains constant irrespective of interest rates. A basket of PWLB loans will then be undertaken by the Council at various maturities to pay the settlement amount over to WG on 2 April 2015. It is proposed that these loans would be a spread of loan maturities, having consideration of existing Council loan maturities, as shown in the previous borrowing maturity chart, to ensure re-financing risk is not increased. This would also allow benefit from reduced interest costs as loans mature.

32. As the settlement amount will depend on interest rates on 31 March 2015, there is risk of fluctuation in interest rates which are outside of the Council's control.

33. Based on an interest rate of 3.67%, the settlement payment would be £222 million and this is what has been assumed in the Treasury Strategy and the indicators included in the strategy that follows. If the interest rate fell by half percent, the settlement payment would be higher at £257 million and if rates rose by half percent the settlement will be lower at £195 million. The risk to the Council is if interest rates fall significantly as if this were to be the case, a higher settlement amount would impact on the level of debt repayment (Prudent Minimum Revenue Provision (MRP)) on loans undertaken.

<u>Treasury Management Implications – Impact on HRA Revenue Budget</u>

34. WG and Treasury are discussing opportunities for taking loans at concessionary rates which could result in greater financial benefit to the Council, however the Council has included prudent assumptions for capital financing, to ensure any such changes in settlement amount and costs for HRA recharges of Capital Financing costs can be accommodated and are affordable.

35. The estimated financial impact in the initial year of self financing for the Housing Revenue Account is shown in the table below and is deemed affordable. With interest costs reducing over time, the financial benefit will increase.

	£m
Subsidy no longer paid over to WG (13/14 data)	(14.9)
Maximum interest cost on loans	8.2
Assumed Provision for debt repayment	5.0
Net benefit to Housing Revenue Account	1.7

Treasury Management Implications – Impact on HRA Limit to Indebtedness

36. As mentioned earlier in the report, HM Treasury has insisted that the local authorities adhere to a limit to indebtedness i.e. a debt ceiling. This is measured using the Housing Capital Financing Requirement (CFR). The Council will use existing prudential indicators to monitor the limit closely to ensure there is no breach and risk of any penalties from WG of any breach. Based on the estimated settlement amount, the HRA limit to indebtedness is £351 million as shown in the table below:-

HRA Capital Financing Requirement	£m
Estimated 31.03.2015	96
Add estimated settlement amount	222
Add headroom for new build	33
Estimated limit to indebtedness (subject to final settlement amount)	**351**

Treasury Management Implications – Pooling of debt

37. In determining the approach to managing the Council's debt, consideration has to be given as to whether HRA debt is notionally split from the rest of the Council debt, which would necessitate two different strategies being prepared, or whether the Council continues with the current integrated single strategy and loans pool. In determining the approach to managing the Council's debt, the Council has also sought advice from its treasury management advisors and considered guidance from CIPFA.

38. Local authorities are required to deliver a solution that is broadly equitable between the HRA and the Council Fund; and future charges to the HRA in relation to borrowing are not influenced by Council Fund decisions, giving a greater degree of independence, certainty and control. However it is a local authority's choice as to how it treats both HRA and General Fund debt.

39. Whilst there are advantages and disadvantages of various options, the view of the Section 151 Officer and Officers is to maintain a single pool for all Council debt. The reasoning for this includes consideration of the following:-

- One pool is consistent with pooling of treasury management activities for effective management of risk and control

- The Council is ultimately responsible for all debt, including debt undertaken by the HRA. HRA is a Service in the same way as education. Interest costs are recharged to HRA, in the same way as to directorates who take invest to save schemes.
- All loans are charged indifferently on all the revenues of the authority in accordance with the Local Government Act 2003.
- Specific loans are not taken out for specific purposes in accordance with good treasury management practice.
- The Section 151 Officer is ultimately responsible for all Council debt, including that funding HRA capital expenditure.
- There is no mechanism to charge HRA for risks of default on Investments. This is all borne by the General Fund so it is deemed inconsistent to treat debt and investments separately
- This avoids the requirement for two separate Treasury Strategies and documents at all current reporting meetings. The extent of additional work in administration, management and reporting of maintaining two pools should not be underestimated.
- Planned loan maturities for HRAS exit are taken with regard to existing debt maturity profile to smooth the historic debt maturity profile to minimise overall re-financing risk to Council.
- Potentially a short term revenue budget benefit to the General Fund, whilst the Council's capital programme in respect of 21st Century schools is implemented, at which point increased benefit to HRA.
- The Prudential Code still requires indicators to be aggregated and Treasury risk is managed as a whole / corporately.
- De-pooling is a one off exercise which ignores the historic benefit which may have accrued to HRA / cost to GF.
- One pool avoids risk of over borrowing. If HRA pays off debt quicker than anticipated, allows flexibility to transfer loans at nil cost to GF. HRA can secure a long term stable / flexible portfolio.

Council's borrowing requirement

40. The following table compares the projected level of external borrowing currently held by the Council, taking into account any scheduled loan repayments and committed new borrowing arising from Housing reform. It compares this to the projected CFR** based on current, known estimates of the Council's capital expenditure plans, subject to approval of the Council's budget in February 2015. The difference between the projected CFR in 2017/18 (£786 million) and the level of external borrowing after any planned repayments and borrowing required to be undertaken for self financing (£674 million) is £112 million, i.e. there will be a requirement for additional borrowing over the medium term.

41. Some of this requirement may be covered by internal borrowing in the short term, dependent on the sustainability and risks of any internal borrowing position. The table demonstrates that over the medium term, borrowing is undertaken only for a capital purpose and it is not borrowing in advance of need.

Gross Debt compared to Capital Financing Requirement					
	2013/14 Actual £m	**2014/15 Estimate £m**	**2015/16 Estimate £m**	**2016/17 Estimate £m**	**2017/18 Estimate £m**
External Borrowing at 1 April	455	473	470	687	680
New borrowing undertaken	20	5			
Housing Settlement commitment			222		
Scheduled repayments	(2)	(8)	(5)	(7)	(6)
External Borrowing at 31 March	**473**	**470**	**687**	**680**	**674**
Capital Financing Requirement **	485	495	743	779	786
Under / (Over) borrowing	**12**	**25**	**56**	**99**	**112**

** The definition of the CFR in accordance with the current Prudential Code for Capital Finance in local authorities is an authority's underlying need to borrow for a capital purpose. It measures capital expenditure incurred but not yet financed by the receipt of grants, contributions or charges to the revenue account. To be meaningful for treasury management purposes, the CFR figures in this strategy exclude the accounting provisions for the management and aftercare of landfill sites which may not be incurred for many years to come. Accordingly, when setting the treasury indicators, landfill provision is excluded from the calculations, except for the setting of the Authorised Limit for external debt, which is required to be set under statute.

External versus Internal borrowing

42. Whilst interest rates for borrowing are greater than interest rates the Council receives for investments (the 'cost of carry'), it makes financial sense to use any internal cash balances in the short-term to pay for capital expenditure and minimise costs (Internal Borrowing), rather than undertake external borrowing. However, there is a risk that the Council may have to borrow at higher rates when it does actually need to borrow in future.

43. A high level balance sheet review undertaken at a point in time suggests that a maximum level of internal borrowing is circa £70 million. However this is dependent on cash flows, the use the Council makes of General and Earmarked Reserves and longer term pressures in the Medium Term Financial Plan.

Borrowing Strategy

44. Based on the analysis above the Council's borrowing strategy for 2015/16 is as follows.

45. Borrowing for the payment of the settlement amount for Housing finance reform buy out will be undertaken on 2 April 2015 in accordance with the agreement with HM Treasury and WG. This will be a basket of loans, with a spread of maturities over time having regard to existing Council debt maturities and resulting in reducing interest cost to the Council over time.

46. Whilst investment rates remain lower than long term borrowing rates internal borrowing will be used to minimise short-term costs where possible. The forecast level of internal borrowing at 31 March 2015 as a percentage of the CFR is deemed manageable. However, based on the current forecasts of future capital expenditure plans and high level analysis of the sustainability of

internal borrowing from the Council's balance sheet position for future years, external borrowing will be required to be undertaken in the medium term.

47. Any borrowing is to be a balance between temporary borrowing on a short term basis to minimise revenue costs (the cost of carry) where possible, with options considered to take an element of the Council's borrowing requirement with loans of longer periods. This strategy should help to mitigate against the risk of borrowing rates rising faster than currently anticipated.

48. If it were felt that there was a significant risk of a sharp rise in long and medium-term rates, then fixed rate borrowing may be undertaken whilst rates were still relatively cheap. If there was a significant risk of a sharp fall in rates, then long-medium term borrowing would be deferred, following consideration of internal borrowing capacity.

49. Current interest rates on the Council's existing debt portfolio compared to new borrowing rates and the high penalty rates charged by the PWLB for early debt repayment, results in limited options for restructuring of debt. Options have been considered but these have resulted in very short term financial gains outweighed by the risk of higher longer term costs. Opportunities will continue to be reviewed to determine whether options exist to generate long term interest savings at minimum risk and minimise refinancing risk.

Treasury Management Indicators and limits for 2015/16 – 2017/18

50. The Council is required to set its treasury management indicators for the years 2015/16 - 2017/18. Appendix 2 gives further background in respect of the Prudential Indicators. Any indicators relevant to treasury are included in this report with additional indicators to be included in the Budget Proposals 2015/16 Report that considers the Capital Programme.

51. The Council must determine and keep under review how much it can afford to borrow from debt or other long-term liabilities for the forthcoming year and the following two financial years (the Affordable Borrowing Limit). It must have regard to the Prudential Code and locally determined indicators when setting this limit and be content that capital investment plans are within sustainable limits and that the impact upon future Council Tax/Rent levels is acceptable.

52. It is recommended that the Council approve the following authorised limits (Statutory limit under Section 3(1) of the Local Government Act 2003) and operational boundaries for the next three years (figures for 2014/15 are for comparison only). The undertaking of other long-term liabilities, within the overall limit, is delegated to the Section 151 Officer based on the outcome of financial option appraisals and best value considerations.

Authorised limit for external debt

	2014/15 £m	2015/16 £m	2016/17 £m	2017/18 £m
Limit for external borrowing and other long-term liabilities	593	812	812	812

53. These limits are consistent with known commitments, existing plans and proposals contained within the budget for capital expenditure, financing and revised accounting requirements. They include landfill provision and are based on the estimated and prudent, but not worst case scenario and in addition with sufficient headroom over and above this to allow for operational management and unforeseen cash movements. The limit has been set at a constant level of £812 million for 2015/16 to 2017/18, with the main reason for the increase from 2014/15 being the housing settlement payment required to be paid to WG.

Operational boundary for external debt

54. The proposed operational boundary for external debt (excluding landfill) is based on the same estimates as the authorised limit, but without the additional headroom for unusual and unexpected cash movements. It is set at the projected level of external debt at the end of the year this being the level of anticipated capital financing requirement. This is clearly subject to the timing of borrowing decisions.

	2014/15 £m	**2015/16 £m**	**2016/17 £m**	**2017/18 £m**
Boundary for external borrowing and other long-term liabilities	470	743	779	786

55. The Council's actual external debt represented by borrowing at 31 March 2014 was £473 million, with no significant other long-term liabilities.

Limits for fixed and variable interest rate exposure

56. Various upper limits are required to be set in order to manage risk and reduce the financial impact on the Council of any adverse movement in interest rates. The limits below reflect that whilst the majority of Council borrowing is currently at long term fixed rates, there could be exposure to variable rates. This is in the form of interest on LOBO loans being changed early, the strategy to utilise internal borrowing where possible and short term external borrowing when required to manage cash flow.

	2014/15 %	**2015/16 %**	**2016/17 %**	**2017/18 %**
Upper limit for fixed interest rate exposure:-	100	100	100	100
Upper limit for variable rate exposure:-	25	25	25	25

Maturity structure of fixed rate borrowing

57. Limits are set to guard against a large element of the Council's debt maturing and having to be refinanced in a very short space of time, when it may not be economically favourable to do so. The limits have been set to reflect the current debt portfolio, and to allow enough flexibility to enable new borrowing

to be undertaken for the optimum period. The actual maturity profile of existing borrowing is included on the assumption that loans run to their final maturity and a separate column is also included to show the maturity profile should the Council be required to repay its LOBOs early.

Maturity structure of borrowing in 2015/16	**Upper limit %**	**Lower limit %**	**Actual to Maturity %**	**Actual if LOBOs Repaid Early %**
Under 12 months	10	0	0.83	7.47
12 months and within 24 months	10	0	0.97	0.97
24 months and within 5 years	15	0	4.18	4.90
5 years and within 10 years	15	0	7.24	7.24
10 years and within 20 years	30	0	20.41	20.41
20 years and within 30 years	35	0	20.30	18.57
30 years and within 40 years	35	0	23.54	23.54
40 years and within 50 years	35	0	16.90	16.90
50 years and within 60 years	15	0	4.91	0
60 years and within 70 years	5	0	0.72	0

Investments

Policy

58. The Council has regard to the WG Guidance on Investments issued in 2004 and its subsequent amendments, as well as the 2011 revised CIPFA's Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes (the CIPFA Treasury Management Code).

59. The Council recognises that given the nature of investments, a trade-off between security, liquidity and yield cannot be avoided i.e. there is risk of default. The Council will aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity, however the level of risk will be contained by ensuring:-

- All investments and repayments are in sterling.
- Investment instruments identified for use in the financial year are listed under 'Specified' investments and 'Non-Specified' investment categories, dependant on their complexity and risk.
- A list of highly credit worthy counterparties with whom to invest is created and monitored.
- Diversification of approach, investment product and counterparties are sought where possible to avoid concentration of risk.
- Any set limits are implemented with immediate effect following approval of this Treasury Management Strategy by Council.

- Continual monitoring of treasury activities with the categories of investments that may be used, the credit criteria and associated limits in determining with whom to invest and timing of decisions being delegated to the Section 151 Officer.

Specified Investments

60. A specified investment is defined as one :

- being for a period up to one year.
- which is in straightforward easily understood low risk products.
- not involving corporate share or loan capital.
- where the principal sum to be repaid at maturity is the same as the initial principal sum invested.

Specified investments may comprise up to 100% of the Council's total investments.

Instruments approved for use	Minimum Credit Criteria
Debt Management Agency Deposit Facility	Assumed Government Guarantee
Term deposits – UK government and other Local Authorities	Assumed Government Guarantee
Deposits with the Council's banking services provider	Long-term A /Short-term F1
Term deposits – banks and building societies	Long-term A /Short-term F1
Term deposits with variable rate and variable maturities up to one year e.g. structured investment products	Long-term A /Short-term F1
Deposits with banks wholly or partly nationalised or where guaranteed by high credit rated (sovereign rating) countries	Long-term A /Short-term F1 Assumed Government Guarantee

Non-Specified Investments

61. These are all other investments not meeting the definition of a specified investment which could be used in order to achieve diversification and manage liquidity needs. A maximum upper level of £60 million is to be set for non-specified investments including investments for greater than one year.

Instruments approved for use	Min Credit Criteria	Max % of total investments	Max. maturity period
Term deposits with Local Authorities (with maturities in excess of 1 year)	Assumed Government Guarantee	15	2 Years
Term deposits – banks and building societies (with maturities in excess of 1 year)	Long-term AA-/Short-term F1+	15	2 Years

Deposits over one year with banks wholly or partly nationalised institutions where guaranteed by high credit rated (sovereign rating) countries	Long-term A /Short-term F1 Government Guarantee	20	2 Years
Term deposits with variable rate and variable maturities in excess of 1 year e.g. structured investment products	Long-term AA- /Short-term F1+	10	2 Years
Term deposit with Financial institutions in accordance with the Council's Local Authority Mortgage Scheme	Long Term A / Short Term F1	Budget approved limit for scheme	5 years
Certificates of Deposit (In-house)	Long-term AA- /Short-term F1+	10	Maximum 2 year duration
UK Government Gilts and Gilt funds (In-house)	Assumed Government Guarantee	40	Maximum 3 year duration
Treasury Bills (In-house)	Assumed Government Guarantee	40	6 Months
Collective Investment Scheme structures - Money Market Funds	AAA Constant Net Asset Value	60	Weighted Average Maturity 60 days
Other Collective Investment Schemes structures - e.g. enhanced cash funds, Government and Corporate Bond, Gilt or Liquidity Funds and floating rate notes	AAA Variable Net Asset Value	20	Weighted Average Maturity 3 years

62. The Council uses money market funds and other collective investment funds which pool together investments in a diversified portfolio of products and sectors mainly high quality, short-term money market instruments such as bank deposits, certificates of deposit, government guaranteed bonds, corporate bonds and commercial paper.

Security

63. Credit and fraud risk are managed through procedural requirements and controls. The Council uses Fitch Credit ratings as a basis for assessment of credit worthiness of institutions it will invest with. Changes in the criteria and decisions with whom to invest are delegated to the Section 151 Officer. Commercial organisations on its approved list (See Appendix 3) will have at least the short-term credit rating of F1 and be authorised institutions within the meaning of the Financial Services and Markets Act 2000. The rating F1 infers "Highest Credit Quality" and indicates the strongest capacity for timely payment of financial commitments.

64. For internally managed investments provided by the private sector, the lending list for any new direct investment in an organisation is based on the following credit criteria:

Fitch Ratings (minimum)	Long-term	Short-term	Limit £m
Overnight to one year	A	F1	10
Overnight to two years	AA-	F1+	12
UK Part Nationalised Banks overnight to two years	A	F1	15

65. For internally managed funds the maximum limit for direct investment in any one group of related companies is £15 million.

66. Credit ratings are monitored regularly through use of the treasury management advisor's credit service. If a downgrade results in the counterparty/investment scheme no longer meeting the Council's criteria, its further use for new investment will be withdrawn immediately.

67. Where investments are held with a counterparty which falls below the Council's approved criteria for new investment, the investments will be reviewed and options to call back funds before the maturity date would be investigated. It should be noted that any early repayment is only at the discretion of the borrower and often at a penalty.

68. Whilst Fitch ratings form the basis of the Council's threshold criteria, the Council will also have regard to the following when determining with whom to invest:

- Rating updates provided by treasury advisors in respect of all three credit rating agencies, as well as credit default swaps, support ratings and other market data.
- Media reports as well as sovereign credit ratings with the minimum requirement being a Fitch sovereign rating of AA for non UK based institutions.
- The informed judgement of treasury staff and treasury management advisors after consideration of wider economic factors.
- Financial sector and country exposure.
- The extent to which organisations who do not meet the above criteria, are nationalised.

Liquidity

69. The Council aims to have sufficient funds to ensure it does not become a forced borrower for a significant period of time at rates in excess of what may be earned on such investments. In determining the maximum periods for which funds may be available and can be invested, short term cash flow forecasts are undertaken and a longer term balance sheet review is undertaken as part of the calculation of Prudential Code indicators.

Investment Strategy

70. Given uncertainty of financial markets, the Specified and Non Specified investments above allow for a range of products to be available to manage short term investment balances and diversification.

71. Given the likelihood of internal borrowing and the interest rate forecasts identified above, longer term investments above one year will be unlikely. The Debt Management Agency Deposit Facility will be used only as a last resort.

72. The investment strategy for 2015/16 will continue to adapt to changing circumstances and market sentiment, with a pragmatic approach taken. Credit criteria changes delegated to the Section 151 Officer, which allows a prompt response to uncertainties with the Council being kept informed of significant changes through the various reports it receives on treasury activities during the course of the year.

Treasury Management Training

73. Treasury staff directly and regularly involved in borrowing and lending activities are provided access to a wide range of training. This includes seminars and workshops organised by treasury advisors bringing together practitioners from different authorities; seminars organised by CIPFA and other national bodies, regular contact with a client relationship manager as well as their briefing notes and articles. Staff responsible for treasury activity on a day to day basis have a recognised accountancy qualification and are encouraged to undertake relevant treasury management training.

74. The Council's Audit Committee Members who are responsible for scrutiny of treasury management activities have also been provided with training in order to support their role.

APPENDIX 1 - Glossary of Terms

Bank Rate
The rate of interest set by the Bank of England as a benchmark rate for British banks.

Bonds
A long-term debt security issued by a company, a financial institution, a local authority, national government or its affiliated agencies. It represents an undertaking to repay the holder the fixed amount of the principal on the maturity date plus a specified rate of interest payable either on a regular basis during the bond's life (coupon) or at maturity.

Borrowing
Loans taken out taken out by the authority to pay for capital expenditure or for the prudent management of the Council's financial affairs, which are repayable with interest.

Capital Expenditure
Capital expenditure pays for improvements to existing and new assets used in the delivery of Council services as well as other items determined by Regulation. Capital resources are scarce, costly and also have long term revenue implications over many years and even generations where capital expenditure is funded by borrowing. Hence the requirement of the Prudential Code to ensure what is charged as Capital Expenditure is Prudent, Sustainable and Affordable.

The statutory definition of capital expenditure is given in the Local Government Act 2003, the Local Authorities (Capital Finance) Regulations 2003 and 2004 as amended. Statute relies on the accounting measurement of cost in International Accounting Standard (IAS) 16 to determine whether expenditure is eligible to be capitalised or whether it should be treated as revenue expenditure. Key to what is eligible as capital spend are the following words in IAS 16 - 'Costs directly attributable to bringing the specific asset into working condition for its intended use'.

Capital Financing Requirement (CFR) (Real and Notional)
An authority's underlying need to borrow for a capital purpose. It measures capital expenditure incurred but not yet financed by the receipt of grants, contributions and charges to the revenue account. This is termed the Real CFR.
Revised accounting guidance from Wales Audit Office on accounting for Landfill Obligations requires a provision to created and charged to capital. As this is for future spend, this is not incurred expenditure, hence caution needs to adopted when comparing the latter figure compared to external borrowing to ensure borrowing in advance of need does not take place.

Capital Market
A market for securities (debt or equity), where companies and governments can raise long-term funds (periods greater than one year). The raising of short-term funds takes place on other markets (e.g. the money market).

Capital Programme
The Capital Programme sets out the Council's capital expenditure plans for the forthcoming financial year as well as for the medium term. It is approved annually at Council and identifies the estimated cost of those schemes, their projected phasing over financial years as well as the method of funding such expenditure.

Certificates of Deposits (CDs)
A certificate issued for deposits made at a deposit-taking institution (generally a bank). The bank agrees to pay a fixed interest rate for the specified period of time, and repays the principal at maturity. CDs can be purchased directly from the banking institution or through a securities broker. An active interbank secondary market exists to buy and sell CDs.

Chartered Institute of Public Finance & Accountancy (CIPFA)
CIPFA is the professional body for people in public finance. As a specialised public services body, they provide information, guidance, and determine accounting standards and reporting standards to be followed by Local Government.

Collective Investment Scheme Structures
Schemes whereby monies from a number of investors are pooled and invested as one portfolio in accordance with pre-determined objectives.

Commercial Paper
A relatively low risk, short-term and unsecured promissory note traded on money markets issued by companies or other entities to finance their short-term cash requirements.

Corporate Bonds
Bonds that are issued by a company or other non-government issuers. They represent a form of corporate debt finance and are an alternative means of raising new capital other than equity finance or bank lending.

Counterparty
One of the parties involved in a financial transaction with whom the Council may place investments.

Counterparty / Credit Risk
Risk that a counterparty fails to meet its contractual obligations to the Council to repay sums invested.

Credit Criteria
The parameters used as a starting point in considering with whom the Council may place investments, aimed at ensuring the security of the sums invested.

Credit Default Swaps
A financial transaction which the buyer transfers the credit risk related to a debt security to the seller, who receives a series of fees for assuming this risk. The levels of fees reflect the perceived level of risk.

Credit Rating
A credit rating assesses the credit worthiness of an individual, corporation, or even a country. Credit ratings are calculated from financial history and current assets and liabilities. Typically, a credit rating tells a lender or investor the probability of the subject being able to pay back a loan. Ratings usually consist of a long-term, short-term, viability and support indicators. The Fitch credit rating of F1 used by the Council is designated as "Highest Credit quality" and indicates the strongest capacity for timely payment of financial commitments.

Debt Management Account Deposit Facility (DMADF)
The Debt Management Office provides this service as part of its cash management operations and of a wider series of measures designed to improve local and central government's investment framework and cash management. The key objective of the DMADF is to provide users with a flexible and secure facility to supplement their existing range of investment options while saving interest costs for central government.

Debt Restructuring
Debt restructuring is a process that allows an organisation to reduce, renegotiate and undertake replacement debt.

Diversification of Investments
The process of creating a portfolio of different types of financial instruments with regard to type, price, risk issuer, location, maturity, etc. in order to reduce the overall risk of the portfolio as a whole.

Duration (Maturity)
The length of time between the issue of a security and the date on which it becomes payable.

External Borrowing
Money borrowed from outside of the Council.

Financial Instrument
Any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another. Typical financial liabilities are borrowing and financial guarantees. Typical financial assets include bank deposits, amounts owed by customers, loans receivable and investments.

Fitch Credit Ratings
A commercial organisation providing an opinion on the relative ability of an entity to meet financial commitments, such as interest, preferred dividends, repayment of principal, insurance claims or counterparty obligations. The opinion is usually provided in the form of a credit rating.

Fixed Rate
An interest rate that does not change over the life of a loan or other form of credit.

Floating Rate Notes
A money market security paying a floating or variable interest rate, which may incorporate a minimum or floor.

Four Clauses of Treasury Management
In compliance with the First Clause, this Council will create and maintain, as the cornerstones for effective treasury management:

- A treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities.
- Suitable Treasury Management Practices (TMP's), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

In compliance with the Second Clause, this Council will receive reports on its treasury management policies, practices and activities, including, as a minimum, an annual strategy in advance of the year, a mid year review and an annual report after its close, in the form prescribed in its TMP's.

In compliance with the Third Clause, this Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to the Cabinet, and for the execution and administration of treasury management decisions to the Corporate Director Resources in accordance with existing delegations, who will act in accordance with the organisation's policy statement, TMP's and CIPFA's Standard of Professional Practice on Treasury Management.

In compliance with the Fourth Clause, this Council requires the scrutiny of the accounting, audit and commercial issues of its Treasury management Strategy and Practices to be undertaken by the Council's Audit Committee due to the technical nature of the documents.

Fraud / Error Risk
Risk of losses being incurred as a result of fraud, error or corruption in treasury management and failure to institute adequate systems, procedures and other arrangements to prevent irregularities.

Housing Revenue Account (HRA)
The HRA is an account of expenditure and income that every local authority housing department must keep in accordance with the Local Government & Housing Act 1989. The account is kept separate or ring fenced from other Council activities. Income is primarily generated by the rents and service charges paid by tenants, while expenditure is on the management and maintenance of the housing stock, and capital financing charges on the HRA's outstanding loan debt.

Interest Rate Risk
Risk that fluctuations in interest rates could impose extra costs against which the Council has failed to protect itself adequately.

Internal Borrowing
Money borrowed from within the Council, sourced from temporary internal cash balances.

Investments
The purchase of financial assets in order to receive income and/or make capital gain at a future time, however with the prime concern being security of the initial sum invested.

Lender Option Borrower Option Loans (LOBOs)
Loans to the Council where the lender can request a change in the rate of interest payable by the Council at pre-defined dates and intervals. The council at this point has the option to repay the loan.

Liquidity
The ability of the Council to meet its financial obligations as they fall due.

Market Loans
Borrowing that is sourced from the market i.e. organisations other than the Public Works Loan Board or a Public Body.

Minimum Revenue Provision (MRP)
This is the amount which must be charged to the authority's revenue account each year and set aside as provision for repaying external loans and meeting other credit liabilities. The prudent amount is determined in accordance with guidance issued by WG. This has the effect of reducing the Capital Financing Requirement (CFR).

Money Market
The market for short-term securities or investments, such as certificates of deposit, commercial paper or treasury bills, with maturities of up to one year.

Money Market Funds
An investment fund which pools the investments of numerous depositors, spreading those investments over a number of different financial instruments and counterparties. Funds with a constant Net Asset Value (NAV) are those where any sum invested is likely to be the same on maturity. Funds with a variable Net Asset Value (NAV) are those where the sum on maturity could be higher or lower due to movements in the value of the underlying investments.

Net Asset Value (NAV)
The market value of an investment fund's portfolio of securities as measured by the price at which an investor will sell a fund's shares or units.

Pooling
The process whereby investments or loans are held corporately rather than for specific projects or parts of the Council, with recharges to those areas for their share of the of relevant income and expenditure using an agreed methodology, where such a recharge is required to be made.

Prudential Code for Capital Finance
The system introduced on 1 April 2004 by Part 1 of the Local Government Act 2003 which allows local authorities to borrow without Government consent, provided that they can afford to service the debt from their own resources and that

any such borrowing is prudent and sustainable. This requires the preparation and approval of various indicators.

Public Works Loans Board (PWLB)
The Public Works Loans Board is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.

Refinancing Risk
Risk that maturing borrowing or other financing of capital projects cannot be renewed on terms that reflect existing assumptions and that the Council will suffer extra costs as a result.

Regulatory Risk
Risk that actions by the Council or by any person outside of it are in breach of legal powers or regulatory requirements resulting in losses to the Council, or the imposition of extra costs.

Security
Protecting investments from the risk of significant loss, either from a fall in value or from default of a counterparty.

Sovereign Credit Ratings
The credit rating of a country. It indicates the risk level of the investing environment of a country, taking into account political risk and other factors.

Sterling
The monetary unit of the United Kingdom (the British pound).

Term Deposits
A term deposit is a money deposit at a banking institution that cannot be withdrawn for a certain "term" or period of time.

Treasury Management
Treasury management activities are the management of an organisation'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.

Treasury Bills
Debt securities issued by a government with a short-term maturity of up to 6 months.

UK Government Gilts
Fixed-interest debt securities issued or secured by the British Government. Gilts are always denominated in sterling though the Government occasionally also issues instruments in other currencies in the Eurobond market or elsewhere.

Variable Rate
An interest rate that changes in line with market rates.

Yield
The annual rate of return paid out on an investment, expressed as a percentage of the current market price of the relevant investment.

APPENDIX 2 - Prudential Indicators

The Prudential Code

The current system of capital finance is CIPFA's Prudential Code.

It is a professional Code of practice to support the decisions local authorities have to make to plan for capital investment at a local level. Authorities are required by regulation to have regard to the Prudential Code when carrying out their duties under Part I of the Local Government Act 2003 i.e. compliance with the Code is a statutory requirement.

Objectives of the Code

The key objectives of the Code are:-

- To ensure within a clear framework that capital expenditure plans are affordable, prudent and sustainable
- That Treasury Management decisions are taken in accordance with good professional practice
- That local strategic planning, asset management planning and proper option appraisal are supported
- To provide a clear and transparent framework to ensure accountability

Prudential Indicators

The indicators required are shown below, with further explanation as to their meaning:

1(a). External Debt - Operational Boundary

The most likely, prudent view of the level of gross external indebtedness. External debt includes both borrowing and long term liabilities (e.g. finance leases). It encompasses all borrowing, whether for capital or revenue purposes.

1(b). External Debt - The Authorised Limit

The upper limit on the level of gross external indebtedness, which must not be breached without Council approval. It is the worst-case scenario. It reflects the level of borrowing which, while not desired, could be afforded but may not be sustainable. Any breach must be reported to the executive decision making body, indicating the reason for the breach and the corrective action undertaken or required to be taken.

1(c). External Debt - Actual External Debt

The indicator for actual external debt will not be directly comparable to the operational boundary and authorised limit, since the actual external debt will reflect the actual position at one point in time.

2. Financing cost to Net Revenue Stream

The percentage of revenue budget set aside each year to service debt financing costs

3. Capital Financing Requirement (CFR)

The Capital Financing requirement (CFR) replaced the ‘Credit Ceiling’ measure of the 1989, Local Government and Housing Act. It measures an authority’s underlying need to borrow or use other long-term liabilities, to pay for capital expenditure.

4. Capital Expenditure

The level of capital expenditure incurred and likely to be incurred in future years. This is to be based on an accruals basis and on the definition of capital expenditure.

5. Incremental impact of Capital Investment decisions on Council Tax / Average weekly Housing Rents

This shows the impact of new capital investment decisions included in the budget on the Council Tax and average weekly rent for HRA.

6. Gross External Borrowing and the Capital Financing Requirement

The level of external borrowing is required to be compared to the Capital Financing Requirement which represents the underlying need to borrow. Requires that borrowing in the medium term can only be for capital purposes.

7. Adoption of CIPFA’s Treasury Management Code of Practice

CIPFA’s Code of Practice for Treasury Management in the Public Services (the CIPFA Code) primary aim is to ensure that public services manage and control the risks attached to its treasury functions in an efficient effective and economic manner.

Accordingly the adoption of the Code has been encapsulated in Local Authorities (Capital Finance and Accounting) Regulations that call for explicit compliance with the CIPFA Code.

8. Interest Rate Exposures

Recognition of the impact on revenue budgets of changes in interest rates as well as the need to ensure that local authorities maintain flexibility in their treasury strategy has resulted in the adoption of an interest rate exposure indicator.
This indicator sets out for the following three years an upper limit for both fixed rate and variable rate exposure.

9. Maturity Structure of Borrowing

Local Authority debt portfolios consist of a number of loans with differing maturities. Setting limits assists in ensuring any new borrowing in particular when combined with existing borrowing does not result in large concentrations of borrowing maturing in a short period of time.

10. Principal sums invested for greater than 364 days

This indicator measures the exposure of a local authority to investing for periods of greater than one year.

APPENDIX 3 – Approved list of Counterparties (@ 31/12/14)

	£	Duration
Australia		
Australia and New Zealand Banking Group	12m	2 years
Commonwealth Bank of Australia	12m	2 years
National Australia Bank	12m	2 years
Canada		
Canadian Imperial Bank of Commerce	12m	2 years
Toronto Dominion Bank	12m	2 years
France		
Credit Industriel et Commercial	10m	1 Year
Societe Generale	10m	1 Year
Germany		
Deutsche Bank	10m	1 Year
DZ Bank (Deutsche Zentral-Genossenschaftsbank)	10m	1 Year
Landesbank Baden Wuerttemberg	10m	1 Year
Netherlands		
Cooperatieve Centrale Raiffeisen Boerenleenbank (Rabobank Nederland)	12m	2 years
Singapore		
DBS Bank	12m	2 years
Oversea Chinese Banking Corporation	12m	2 years
United Overseas Bank	12m	2 years
Sweden		
Skandinaviska Enskilda Banken	10m	1 Year
Svenska Handelsbanken		
Switzerland		
UBS AG	10m	1 Year
U.K		
Barclays Bank	10m	1 Year
Close Brothers	10m	1 Year
Goldman Sachs International Bank	10m	1 Year
HSBC Bank plc	12m	2 years
Santander UK plc	10m	1 Year
Standard Chartered Bank	12m	2 years
Bank of Scotland	15m	2 Years
Lloyds Bank	15m	2 Years
Royal Bank of Scotland	15m	2 Years
Coventry BS	10m	1 Year
Nationwide BS	10m	1 Year
Local Authorities	15m	2 Years
Debt Management Agency Deposit Facility	n/a	6 Months
Money Market Funds		
BlackRock ICS Sterling Fund	12m	Instant Access
Deutsche Managed Sterling Fund	12m	Instant Access
Fidelity GBP ICF	12m	Instant Access
Goldman Sachs Sterling Reserves Fund	12m	Instant Access
Ignis Sterling Liquidity	12m	Instant Access
Insight Sterling Liquidity Fund	12m	Instant Access

LGIM Sterling Liquidity Fund	12m	Instant Access
Northern trust sterling Government Liquidity Fund	12m	Instant Access
Royal Bank of Scotland Global Treasury Fund	12m	Instant Access