Appendix 1

Draft Treasury Management Strategy 2020/21

Cardiff Council

Contents

Treasury Management

The Council carries out its treasury management activities in accordance with a Treasury Management Code of Practice for public services, updated by CIPFA in 2017. 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. The last section of this strategy includes a glossary of terms used in this document.

CIPFA has adopted the following as its definition of treasury management activities:

> *The management of the organisation's borrowing, 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 definition of 'Investments' above includes:

- Treasury Management investments (held for the prudent management of financial affairs), as well as
- Non-Treasury Investments, undertaken as part of a Capital Strategy either in the course of provision of services; or made for commercial reasons purely to make a financial gain. These are managed outside of normal treasury management activity.

Governance and Reporting

In compliance with Codes and Council policy, full Council receives a report on:

- the Treasury Management Strategy at the start of a forthcoming year
- a mid-year update and
- an outturn report.

The Council has delegated responsibility for Treasury Management to the Corporate Director of Resources and S151 Officer. The Council's Treasury Management Practices identifies specific responsibilities of officers as well as setting out schedules highlighting the way in which treasury activities are managed.

Responsibility for treasury decisions ultimately remains with the Council however, 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 by Link Asset Services, Treasury Solutions includes advice on timing of decision making, training, credit updates, economic forecasts, research, articles and advice on capital finance.

Audit Committee undertakes scrutiny of the accounting, audit and commercial issues in relation to the Council's Treasury Management Strategy and practices and various reports are produced highlighting treasury management activities in accordance with council policy.

Treasury Management Strategy

The strategy covers the following areas:

- Borrowing to finance the cash requirements arising from the Council's Capital Programme and Strategy. Costs of servicing that financing is linked to the Council's Medium Term Financial Plan.
- Treasury investments determining how short term cash flows will be safely managed to meet the Council's financial commitments and objectives.
- Highlighting the approach to Non-Treasury Management Investments. Whilst these impact on the treasury function, they arise from capital expenditure plans which are reported separately from day to day treasury management activities. Accordingly this strategy focuses on Treasury investments.

The Council accepts that no treasury management activity is without risk. However 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.

The identification, monitoring and control of risk are integral elements of treasury management activities with risks including credit and counterparty, liquidity, interest rate, refinancing, fraud and regulatory. The Council has Treasury Management Practices to address and mitigate these risks which were updated in March 2019 following a review by Internal Audit and Audit Committee.

The proposed strategy is an integrated strategy for the Council including the Housing Revenue Account (HRA). This integrated approach is proposed for review for future years, however the current strategy includes:

- the current treasury position
- economic background and prospects for interest rates
- borrowing, including:
  - policy
  - annual Minimum Revenue Provision (MRP) policy statement
  - council borrowing requirement based on its capital expenditure plans and choice between internal and external borrowing and
  - borrowing strategy
- treasury management indicators and limits for 2020/21 to 2024/25
- investment policy and strategy, including security and investments approved for use
- non treasury investments and
- training.

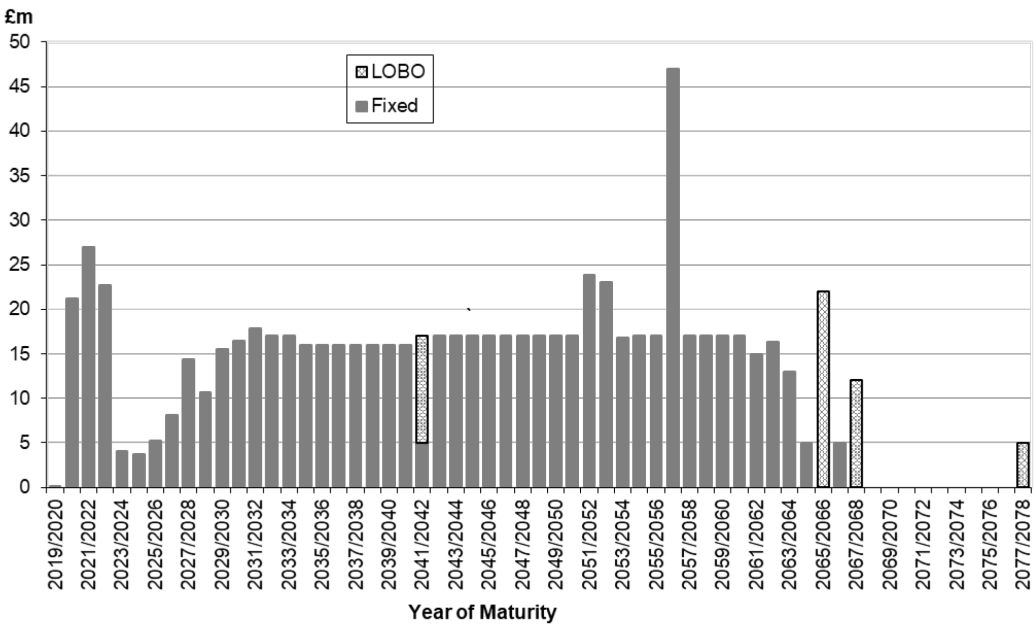
The Treasury Position

Borrowing and investments as at 10 January 2020 and at the same date in the prior year, are 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.

	10 January 2019		10 January 2020	
	Principal £m	Average Rate %	Principal £m	Average Rate %
External Borrowing				
Public Works Loan Board (PWLB)	(643.9)	4.7	(668.9)	4.6
Market (Lender Option Borrower Option)	(51.0)	4.0	(51.0)	4.0
Welsh Government	(4.5)	0	(6.1)	0
Local Authority	0	0	(58.3)	1.45
Other	(5.3)	0	(4.2)	0
Total Debt	**(704.7)**	**4.58**	**(788.5)**	**4.27**
Treasury Investments (Internally Managed)*				
Banks	34.0	0.96	89.0	0.91
Building Societies	10.0	0.84	10.0	0.75
Money Market Funds	43.9	0.75	40.3	0.71
Total Treasury Investments (Net)	**87.9**	**0.84**	**139.3**	**0.84**
Net Treasury Investments / (Borrowing)	(616.8)		(649.2)	

*Note all investments are currently managed internally and no external fund management arrangements are in place.

The Council's debt maturity profile at 10 January 2020 is shown in the following graph on the assumption that all loans run to their final maturity. This includes short term loans taken for the recent acquisition of the Red Dragon Centre site in Cardiff Bay.



LOBO products are loans to the Council where the lender can request a change in the rate of interest payable by the Council on pre-determined dates. The Council at this point has the option to repay the loan without penalty. The Council has six such loans totalling £51 million.

Apart from the option to increase rates these loans are comparable to PWLB loans and have no other complications such as variation in interest rates or complex terms. Interest rates on these loans range between 3.81% and 4.35% and are below the Council's average rate of interest payable. Details of the loans are shown in the next table.

Lender Option Borrower Option (LOBO) Loans			
Potential Next Repayment Date	**Loan Value £m**	**Option Frequency Every**	**Full Term Maturity Date**
01/03/2020	6	6 months	23/05/2067
21/05/2020	6	6 months	21/11/2041
21/05/2020	6	6 months	21/11/2041
21/05/2020	6	6 months	23/05/2067
21/11/2020	22	5 years	23/11/2065
15/01/2023	5	5 years	17/01/2078

It should be noted that £24 million of the LOBO loans are currently subject to the lender potentially requesting a change in the rate of interest payable every six months. A further £22 million and £5 million have call options in November 2020 and January 2023 respectively and every five years thereafter. The likelihood of a request for an increase in rate is negligible.

The following table gives the Council's treasury management advisor's latest forecast of interest rates taking into account the twenty basis point certainty rate reduction available for PWLB loans. It is a central forecast, acknowledging for example that there are upside and downside risks. The rates above are predicated on an assumption of a trade agreement being reached between the UK and the EU.

	Actual 31/12/2019	March 2020	March 2021	March 2022	March 2023
Bank Rate	0.75%	0.75%	1.00%	1.00%	1.25%
5yr PWLB rate	2.43%	2.40%	2.60%	2.90%	3.20%
10yr PWLB rate	2.67%	2.70%	2.90%	3.20%	3.50%
25yr PWLB rate	3.22%	3.30%	3.60%	3.90%	4.10%
50yr PWLB rate	3.05%	3.20%	3.50%	3.80%	4.00%

Forecast at December 2019

Economic and interest rate forecasting remains difficult with so many external influences on the UK economy. Growth and consumer confidence for the UK economy was dampened particularly as a result of brexit uncertainty during 2019. This uncertainty is likely to continue, limiting growth to around 1% until there is more certainty after the trade deadline is passed in December 2020.

As for inflation, the latest Monetary Policy Report issued by the Bank of England revised its inflation forecasts down to 1.5% in 2020, and 2.0% in 2021; hence, the Monetary Policy Committee views inflation as causing little concern in the near future. However it was noted that events triggering a weakening pound could change this as a result of the potential for increased import costs.

International factors also impact significantly on the UK economy. In the United States, the Federal Reserve started a series of rate reductions from its previous policy of unwinding from historic lows. Rates were set at 1.5% to 1.75% in October 2019. Trade tensions and implementation of tariffs, particularly between the United States and China, has also created uncertainty in financial markets in relation to impact on growth and risk of escalation. World central banks are, therefore, likely to come under more pressure to support growth by looser monetary policy measures and this will militate against central banks increasing interest rates. In addition they are working in very different economic conditions than before the 2008 financial crash as there has been a major increase in consumer and corporate debt due to the exceptionally low levels of borrowing rates that have prevailed since 2008. This remains a significant risk.

The above issues including growth in the UK, growth globally, price and wage inflation are key factors used by the Bank of England in determining when to change interest rates. The bank last increased the base rate by 0.25% to 0.75% on 2 August 2018. The forecasts in the table above assume a modest recovery in the rate and timing of stronger growth and in the corresponding response by the Bank in raising rates.

PWLB rates are based on Government borrowing rates (Gilts) and can be the subject of exceptional levels of volatility due to geo-political, sovereign debt crisis and emerging market developments over the forecast period. In addition we have seen from HM Treasury intervention in 2010 and more recently in 2019, a significant margin of 100 basis points each time being added in determining PWLB borrowing rates.

This makes a ‘cost of carry’, i.e. where borrowing rates are greater than investment rates even more likely to continue in the medium term. Accordingly, an approach of deferring external borrowing by using temporary cash balances will continue to result in short term savings, whilst cash balances allow. However, caution should be adopted to avoid incurring higher borrowing costs in the future when new borrowing is unavoidable.

Downside risks to PWLB rates are:

- Bank of England raises bank rate faster than anticipated causing UK economic growth and increases in inflation, to be weaker than anticipated.
- An approach to Brexit which is deemed to have a major downturn on UK economic growth.
- Geopolitical risks in Asia, Europe and the Middle East, which could lead to increasing safe haven flows to the UK.
- Resurgence of the Eurozone sovereign debt crisis due to high level of government debt, low rate of economic growth and vulnerable banking and political systems of certain countries.
- The level of debt accumulated by corporations during the decade of low interest rates.

The potential for upside risks especially for longer term PWLB rates include:

- The Bank of England is too slow in its pace and strength of increases in bank rate and, therefore, allows inflation pressures to build up too strongly within the UK economy.
- Brexit – if agreement was reached all round that removed all threats of economic and political disruption between the EU and the UK.
- UK inflation returning to sustained significantly higher levels.
- Increases in the pace and strength of reversal of quantitative easing.

Borrowing Policy

Borrowing to pay for capital investment has long-term financial consequences and risks, with decisions taken many years ago impacting currently and in the future in the form of interest and provision for repayment of capital expenditure. Expenditure decisions are assumed in the Capital Strategy and detailed programme approved by Council with the recurring cost implications factored into the Council's Medium Term Financial Plan. All borrowing is undertaken in the name of the Council and secured on all revenues of the Council.

The Council can consider various sources and debt instruments to pay for capital expenditure as well as its short term working capital requirements including unexpected cash outflows. This includes the Public Works Loan Board, the financial markets, Municipal Bond Agency, Local Authorities and other public bodies, finance leases, public private partnership models and the issuing of bonds for significant levels of funding or smaller bond schemes linked to specific themes such as green growth. These are detailed in the Council's Treasury Management Practices and the advantages and disadvantages of such products would need to be considered including risks, track record and cost of issuance, supported by external advice in respect of different options.

Best Treasury management practice is that loans are not taken on a project by project basis, however this may be a consideration for investment property purchases or similar, where there may be a need to meet specific cash flows or track performance in the short term.

The Council's currently maintains a single pool of all Council debt for all activities of the Council and the rationale for this approach was last reviewed in 2015/16. However given the changes in the last few years of the respective activities of the Housing Revenue Account and General Fund as well as some of the more complex expenditure commitments being undertaken and assumed to be paid for by borrowing, a further review will need to be undertaken. This is to ensure the current approach maintains a 'fair' interest cost for respective activities. The scope of this review will be scheduled in 2020/21, subject to the resourcing to ensure this can be undertaken effectively.

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 held 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 and so this position is kept under continuous review.

The Council's Borrowing Strategy considers 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
- ensuring borrowing plans are aligned to known capital expenditure spending plans and financial reserve levels
- achieving a balanced maturity profile
- having regard to the effects on current and future Council Tax and rent payers.

The Council does not intend to borrow in advance of need and will not do so just to gain financially. However, this option may be considered if it is felt that borrowing in advance allows opportunities to lock into favourable long-term rates. This will be limited to no more than the expected increase in the Council's borrowing requirement over a three year period.

Prudent Repayment of Capital Expenditure – Annual Minimum Revenue Provision (MRP) Policy Statement for 2019/20 and 2020/21

The Council has a statutory duty to calculate and set aside each year from its revenue budget a minimum amount 'which it considers to be prudent'. It is also allowed to undertake additional voluntary payments if required (Voluntary Revenue Provision – VRP). Voluntary provision can, if needed, be reclaimed in later years if deemed necessary or prudent.

Making MRP and VRP results in a reduction in the Council's underlying need to borrow known as the Capital Financing Requirement (CFR).

Legislation does not define what constitutes a 'prudent provision'. Instead WG has provided guidance and examples in order to interpret that term. Decisions in respect of the allocation of MRP have short, medium and very long term impacts over generations.

The previous approach to MRP was based on a reducing balance basis. This has been tested and reviewed during 2019/20 and it is recommended a change in approach is adopted whereby current and future generations who make use of assets, will pay an equal and consistent amount of MRP and there is a defined point at which debt will be fully provided.

It is proposed that the Council's MRP Policy to apply for 2019/20 and for future years is as follows, with any change in the level, timing and method of provision in year delegated to the Section 151 Officer.

- *Council expenditure undertaken based on 'supported borrowing' approved by WG is to be provided for on a straight line basis over 45 years*
- *HRA supported borrowing, which was part of the previous housing subsidy system is to be provided for at 2% on a straight line basis. MRP on the significant*

£187 million settlement buyout payment is to be on 2% straight line basis as a minimum.

- *Additional borrowing for a general increase in investment either in the Council Fund or HRA 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, 21st Century Schools etc. is to be provided for on a straight line basis, or annuity basis, 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.*
- *Voluntary Revenue Provision in excess of the above requirements can be made subject to affordability and following advice of the Section 151 Officer.*
- *Subject to agreement of the S151 Officer, MRP may be waived on expenditure recoverable within a prudent period of time through capital receipts (e.g. land purchases, loan repayments) or deferred to when the benefits from investment are scheduled to begin or when confirmed external grant payments towards that expenditure are expected.*
- *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.*

Council's Borrowing Requirement

The following table shows the actual level of external borrowing currently held by the Council including planned external borrowing in 2019/20 and scheduled loan repayments in future years. It compares this to the projected CFR i.e the need to borrow based on estimates and timing of the Council's capital expenditure, proposed MRP policy and funding plans as set out in the budget report for 2020/21. The difference between the projected CFR in 2024/25 (£1,049 million) and the actual level of external borrowing after any planned repayments (£768 million) is £281 million, i.e. there is insufficient cash held by the Council to support this projected level of under borrowing and this means there is a requirement for the Council to undertake further external borrowing over the medium term.

	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
	£m	£m	£m	£m	£m	£m	£m
External borrowing at 1 April	693	722	788	787	780	776	772
Known / New borrowing	33	70	tbc	tbc	tbc	tbc	tbc
Scheduled repayments	(4)	(4)	(1)	(7)	(4)	(4)	(4)
External Borrowing at 31 March	**722**	**788**	**787**	**780**	**776**	**772**	**768**
Capital Financing Requirement	767	844	878	966	1,049	1,055	1,049
Shortfall / (Surplus) borrowing requirement	**45**	**56**	**91**	**186**	**273**	**283**	**281**
Requirement as % of CFR	**5.9%**	**6.6%**	**10.4%**	**19.3%**	**26.0%**	**26.8%**	**26.8%**

Within the external borrowing figures above in 2019/20, short term borrowing of £58m relates to capital expenditure on the commercial investment in the Red Dragon Centre. This is just over 7% of the estimated level of actual external debt at 31 March 2020. This is made of a series of one, two and three year loans rather than long term borrowing as the acquisition is a first step in delivering arena. Accordingly the approach to future retention of the site as an investment in full or part is uncertain. Short term borrowing is cheaper but will also involve an element of refinancing risk when there is certainty of approach.

It should be noted that the borrowing requirement may increase further if the affordability envelope identified in the budget report for the indoor arena is triggered following consideration of affordability and approval of relevant business cases.

The CFR projections show a continuing increasing trend and are based on:

- agreed expenditure pre commitments in the capital programme approved in 2019/20 and prior years
- an assumption that the council has the capacity and can implement the capital programme in accordance with the timescale in which funding is requested
- an assumption that the non earmarked capital receipt target of £40 million set in 2018/19 and other capital receipts assumed are achievable and receivable in a reasonable time frame

Changes in the CFR projection compared to prior year include:

- Expansion in the HRA capital programme in respect of new build and other commitments such as cladding
- Acquisition of the Red Dragon Centre site
- A revision to the MRP policy for supporting borrowing from a reducing balance approach to a straight line approach

The CFR figures included in the above table currently assume no additional capital expenditure is approved to be paid for by borrowing as part of the updated capital programme. However, were additional expenditure commitments be deemed affordable and recommended for approval as part of the budget, then the level of such expenditure is unlikely to result in a material change to the treasury strategy proposed.

The section below sets out the approach to meeting the known borrowing requirement including use of temporary cash balances, external borrowing, sources of borrowing and timing.

Borrowing Strategy

In the short term, continuing with an approach of internal borrowing, using temporary cash balances available will continue to be a cost effective way of meeting part of the borrowing requirement. A high level balance sheet review undertaken suggests that a maximum level of internal borrowing could be circa £80 million (c9% of the 2020/21 CFR).

Whilst having regard to the risks of comparison, data was compiled by the Council's Treasury Advisors, and included as part of a Benchmarking report provided to Audit Committee in November 2019, from their Local Authority clients in 2018/19 showing internal borrowing as a percentage of their CFR. This showed that Welsh Councils averaged 11.9%; English Unitary 20.5% and 16.8% for all Authority clients. The Council will continue to undertake various benchmarking activities to support the understanding of treasury performance, position and risk.

As mentioned previously, the Council will consider various sources and debt instruments to meet the borrowing requirement. Prior to the 100 basis points increase in rates in October 2019, most local authorities preferred source of long term borrowing was the PWLB, given the transparency and control that its facilities provide. The Council continues to qualify for borrowing at the 'Certainty Rate' (0.20% below the PWLB Standard Rate). It is unclear whether the recent move by HM Treasury is one that was a short term reaction which would be reviewed. However whilst this uncertainty remains, it is very likely that alternative providers of finance will step into the market for lending to local authorities. Options will be reviewed closely as the position develops, in conjunction with the Council's treasury management advisors early in the new year, particularly given the scale of the borrowing requirement.

Given the risks within the economic forecasts, setting a fixed target for the quantum and timing of borrowing is not deemed appropriate. A pragmatic approach will be adopted by Council's Section 151 Officer due to changing circumstances with the following strategy proposed to manage the Council's Capital Financing Requirement:

- Whilst investment rates remain lower than long term borrowing rates internal borrowing will be used to minimise short-term costs
- External borrowing (short, medium and long term) will be taken for the balance of the Council's borrowing requirement, with timing delegated to the Council's Section 151 Officer. This will aim to keep internal borrowing to approximately £80 million, subject to balance sheet capacity and future interest rate forecasts.
- External borrowing is likely to be at fixed rates to meet the long term borrowing policy aims and current forecasts for rates.

If there was a significant risk of a sharp rise in long and medium-term rates than that currently forecast, then fixed rate external borrowing may be undertaken sooner to reduce the level of internal borrowing. 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.

Current interest rates on the Council's existing debt portfolio compared to new borrowing rates and penalty rates charged for early debt repayment, results in limited options for restructuring of debt. Options have previously been considered for early repayment of LOBO loans, however the penalties outweighed the benefits. This position is expected to continue to be the case in the next few years.

The Council is required to set treasury management indicators as part of the CIPFA Treasury Management Code of Practice 2017 as well as Capital expenditure indicators in the overall budget report to consider affordability indicators.

Authorised Limit

The Council must set 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 the impact upon future Council Tax payers and Council tenants is acceptable.

Based on the capital programme proposed, 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 (figures for 2019/20 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	2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m
Limit for external borrowing and other long-term liabilities	990	1,055	1,055	1,055	1,055	1,055

This limit is consistent with proposals contained within the budget for capital expenditure with the addition of financing and accounting requirements in relation to landfill obligations. The overall limit for the Council has been set at a constant level of £1,055 million for 2020/21 to 2024/25.

It should be noted that the borrowing requirement may increase further if the affordability envelope identified in the budget report for the indoor arena is triggered following consideration of affordability and approval of relevant business cases. Any increase or change in treasury indicators would be reported to Council as part of the regular reports to Council on treasury management activities.

The Government retains an option to control either the total of all council's plans, or those of a specific council, although this power has not yet been exercised.

Operational Boundary

The proposed operational boundary or projected level of external debt (excluding landfill) is set at the anticipated level of the CFR at the end of each year. This will be subject to the level and timing of borrowing decisions.

Operational boundary	2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m
Boundary for external borrowing and other long-term liabilities	788	878	966	1,049	1,055	1,049

Maturity Structure of Borrowing

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 table assumes that loans run to their final maturity, however a separate column is also included to show the maturity profile should the Council repay its LOBO loans early.

Maturity structure of borrowing in 2020/21	Upper limit %	Lower limit %	Actual to Maturity %	Actual if LOBOs Repaid Early %
Under 12 months	10	0	2.69	8.52
12 months and within 24 months	10	0	3.42	3.42
24 months and within 5 years	15	0	3.86	4.49
5 years and within 10 years	20	0	6.82	6.82
10 years and within 20 years	30	0	20.83	20.83
20 years and within 30 years	35	0	21.43	19.91
30 years and within 40 years	35	0	26.97	26.97
40 years and within 50 years	35	0	13.35	9.04
50 years and within 60 years	15	0	0.63	0.00
60 years and within 70 years	5	0	0.00	0.00

Treasury Investment Policy

The Council has regard to the CIPFA Treasury Management Code and also complies with Welsh Government guidance on investments. The Council's investments include those arising from its own temporary cash balances as well as balances held from the activities of Joint Committees for which it is the Accountable body.

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's risk appetite for treasury investments is low and its current business model for financial assets for treasury management investments is to collect contractual cash flows as part of the prudent management of its financial affairs. It aims to achieve the optimum return on investments commensurate with proper levels of security and liquidity. 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 the 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 S151 Officer.

The Markets in Financial Instruments Directive (MiFID II) was implemented from 3 January 2018. Where requested by counterparties to do so, the Council has opted up to be classed as a 'professional' client following the submission of qualitative and quantitative information on its treasury activities.

Economic, Social and Governance issues are important to the Council and can play an important part in long term investments decision making. However the key aim for the Treasury Management of temporary cash balances is Security, Liquidity and then Yield for short term cash balances. Accordingly consideration of wider ethical issues such as climate change are not currently a key factor in the options for placing of short term cash balances.

Treasury Investment Strategy

The Council will retain access to a range of products and organisations available to manage short term investment balances and to achieve diversification. It uses WG guidance and judgements to define products available for use as specified or non specified and sets credit criteria to mitigate credit risk. These are defined in the sections below. Any funds held by the Council on behalf of joint committees will be managed in accordance with this strategy.

The ability to change credit criteria and the approach to investments is delegated to the S151 Officer. This allows a prompt response to uncertainties in financial markets, with the Council being kept informed of significant changes through the various reports it receives on treasury activities during the course of the year.

The Council aims to have sufficient liquid 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. Short term cash flow forecasts and a longer term balance sheet review is undertaken as part of the calculation of Prudential Code indicators to determine maximum periods for investments.

Specified Investments

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
Term deposits – UK government and other Local Authorities	Assumed Government Guarantee
Term deposits – banks and building societies	Long-term A- /Short-term F1 or Government Equity Support

Non-Specified Investments

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 £90 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	30	2 Years
Term deposits – banks and building societies (with maturities in excess of 1 year)	Long-term AA- /Short-term F1+ or part nationalised	30	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
Certificates of Deposit	Long-term AA- /Short-term F1+	10	Maximum 2 year duration
UK Government Gilts and Gilt funds	Assumed Government Guarantee	40	Maximum 3 year duration
Treasury Bills	Assumed Government Guarantee	40	6 months
Collective Investment Scheme structures – Constant as well as Low Volatility Money Market Funds	AAA – (Fitch, Moody's or S&P)	100	Liquid
Collective Investment Scheme Structures – Ultra Short Dated Bond Funds	AAA - (Fitch, Moody's or S&P)	20	Liquid
Collective Investment Scheme Structures - Government Bond Funds, Corporate Bond Funds, Gilt Funds and Floating Rate Notes	AA-	10	Weighted Average Maturity 3 years

The Council can utilise collective investment funds which pool together investments in a diversified portfolio of products and sectors. These may include short-term money market instruments such as bank deposits, certificates of deposit, government guaranteed bonds, corporate bonds and commercial papers, together with a weighted average maturity of up to 60 days. It should be noted that any such funds are triple A rated and allow instant access.

Security / Creditworthiness Policy

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 S151 Officer. Commercial organisations (counterparties) on its approved list 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" - the strongest capacity for timely payment of financial commitments.

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 other market data.
- media reports as well as sovereign credit ratings. No minimum sovereign rating is applied to the UK, however for non UK based institutions the minimum Fitch sovereign rating is AA-
- 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.

Local authorities usually do not have a credit rating, but are expected to assume the UK Sovereign rating. In accordance with the Local Government Act 2003, a person lending money to a local authority shall not be bound to enquire whether the authority has power to borrow the money and shall not be prejudiced by the absence of any such power. All loans are secured on future revenues of local authorities and this includes the ability to take legal action if any debts are not repaid. As demonstrated in benchmarking of treasury management investments, inter local authority lending is a significant option being used for short term investment balances, and is an option that continues to be available as part of the strategy proposed.

The Council's lending list for direct investment in an organisation is based on the following credit criteria, with the maximum limit for direct investment in any one group of related companies, whether ring fenced or otherwise, being £12 million:

Fitch Ratings (minimum)	Long term	Short term	Limit £m
Overnight to three months	A-	F1	5
Overnight to one year	A	F1	10
Overnight to two years	AA-	F1+	12
UK Part Nationalised Banks overnight to two years	n/a	n/a	12

Where link recommend a shorter duration than would be allowed in accordance with Fitch criteria above, then the shorter period is adhered to.

The Council's current list of approved counterparties is shown below:

	£	Duration
Australia AAA		
Australia and New Zealand Banking Group	12m	2 years
Commonwealth Bank of Australia	12m	2 years
National Australia Bank	12m	2 years
Canada AAA		
Canadian Imperial Bank of Commerce	12m	2 years
National Bank of Canada	10m	1 Year
Toronto Dominion Bank	12m	2 years
France AA		
Credit Industriel et Commercial	10m	1 year
Societe Generale	10m	1 year

	£	Duration
Germany AAA		
DZ Bank (Deutsche Zentral-Genossenschaftsbank)	12m	2 years
Netherlands AAA		
Cooperatieve Rabobank U.A.	12m	2 years
Singapore AAA		
DBS Bank	12m	2 years
Oversea Chinese Banking Corporation	12m	2 years
United Overseas Bank	12m	2 years
Sweden AAA		
Skandinaviska Enskilda Banken	12m	2 years
Switzerland AAA		
UBS AG	12m	2 years
U.K AA*		
Barclays Bank (NRFB)	10m	1 Year
Close Brothers	10m	1 Year
Goldman Sachs International Bank	10m	1 Year
Handelsbanken	12m	2 years
HSBC Bank plc (RFB)	10m	1 year
Santander UK plc	10m	1 Year
Standard Chartered Bank	10m	1 Year
Bank of Scotland (RFB)	10m	1 Year
Lloyds Bank (RFB)	10m	1 Year
National Westminster Bank (RFB)	12m	2 Years
Royal Bank of Scotland (RFB)	12m	2 Years
Coventry BS	5m	3 Months
Leeds BS	5m	3 Months
Nationwide BS	10m	1 Year
Skipton BS	5m	3 Months
Yorkshire BS	5m	3 Months
UK Local Authority (per Authority)	12m	2 Years
Debt Management Agency Deposit Facility	n/a	6 Months
Money Market Funds		
Aberdeen Liquidity Fund	12m	Liquid
BlackRock ICS Sterling Fund	12m	Liquid
Deutsche Managed Sterling Fund	12m	Liquid
Fidelity GBP ICF	12m	Liquid
Goldman Sachs Sterling Reserves Fund	12m	Liquid
HSBC GBP Liquidity	12m	Liquid
Insight Sterling Liquidity Fund	12m	Liquid
JPMorgan	12m	Liquid
LGIM Sterling Liquidity Fund	12m	Liquid

* In respect of the Council's day to day banking provider, there is a risk that the counterparty limit would be exceeded for a short period on receipt of unexpected funds.

The above list has been determined having regard to current participation in the financial markets and brokerages, sovereign countries whose banks we would be content to use and selecting some of their highest rated organisations.

Credit ratings are monitored regularly through use of the treasury management advisor's credit service. If a downgrade results in the counterparty or investment scheme no longer meeting the Council's criteria, its further use for new investment will be withdrawn immediately. Investments already held with that counterparty will be reviewed and options to call back funds before maturity would be investigated. It should be noted that any early repayment is only at the discretion of the borrower and often at a penalty.

In addition to treasury management investment activity, local authorities can utilise their powers to borrow in order to invest in other financial assets. Such activity includes loans supporting service outcomes, investments in subsidiaries, and investment property portfolios primarily for a financial return. Whilst these impact on Treasury Management activity, they are managed outside of this Treasury Management Strategy and approved separately as part of the Council's Capital expenditure plans arising from its Capital Strategy. Regulator concerns in relation to the extent of this activity have resulted in recent updates to CIPFA professional Codes of Practice including the Treasury Management Code. Whilst no national monetary, financial or other controls or limits are in place currently, regulations have been updated to ensure the risks and implications of such activities are clearly governed and understood over a long term period.

The most significant investments currently held by the Council and managed outside of normal treasury management activity are the Council's 100% shareholding in Cardiff Bus, the Council's investment properties, which include various historic freeholds within the City held for income generation or capital appreciation. The Council has also recently secured the Red Dragon Centre site with a view to providing options for an arena and or securing future rental income.

Investment for non-treasury management purposes paid for by additional borrowing requires careful investment management. Any previous and future proposals for such investments form part of the approved Capital Strategy and Capital Programme, setting out where relevant, the risk appetite and specific policies and arrangements for non-treasury investments. This will include an appropriate investment management and risk management framework, making it explicit in any decision making:

- the powers under which investment is made
- the governance process including arrangements in place to ensure appropriate due diligence to support decision making
- the extent to which capital invested is placed at risk
- proportionality of any income to resources available to the Council
- the impact of potential losses on financial sustainability
- the methodology and criteria for assessing performance and monitoring process
- how knowledge and skills in managing such investments is arranged and that these are monitored, reported and highlighted explicitly in the decision making process and due diligence.
- creation of Treasury Management practices which specifically deal with how non treasury investments would be carried out and managed

Guidance has indicated the importance of the Council's S151 (Responsible Finance) Officer role in reviewing and informing decisions being made in relation to Non-Treasury Investments.

Treasury Management Training

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.

Audit Committee Members who are responsible for reviewing and seeking assurance on treasury management activities have also been provided with the opportunity for specific internal and external training. The development of further training will be informed by individual and collective Audit Committee self-assessments.

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 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)
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.

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 accountants in public finance. As a specialised public services body, it provides information, guidance, and determines 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.

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 (TMPs), 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 TMPs.

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, TMPs 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.

Medium Term Financial Plan

Plan outlining the financial strategies and actions that are envisaged by the Council in the medium term regarding the budget.

Markets in Financial Instruments Directive (MiFID)

EU legislation that regulates firms who provide financial instrument services. MiFID was applied in the UK from November 2007, but was revised with changes taking effect from **3 January 2018 (**MiFID II).

The aim is to ensure financial institutions undertake more extensive checks on their client's suitability for investment products. Organisations undertaking investments will be either classified as 'retail' or 'professional'.

MiFID II requires all Local Authorities to be initially treated as "retail clients" unless they "opt up" to a "professional client". The assumption being that retail clients require a greater level of due diligence and support for investment decision making. Financial institutions will owe a greater duty of care to retail clients, however, they will have no greater financial protection than professional clients.

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 having regard to 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 (CNAV) are those where the sum invested is the same on maturity, Low Volatility Net Asset Value (LVNAV) are those where any sum invested is likely to be the same on maturity. Funds with a Variable Net Asset Value (VNAV) 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 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.

Ring Fencing
The largest UK banks, (those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits), are required, by UK law, to separate core retail banking services from their investment and international banking activities. Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up. Several banks are very close to the threshold already and so may come into scope in the future regardless.

Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and SME deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler, activities offered from within a ring-fenced bank, (RFB), will be focused on lower risk, day-to-day core transactions, whilst more complex and "riskier" activities are required to be housed in a separate entity, a non-ring-fenced bank, (NRFB). This is intended to ensure that an entity's core activities are not adversely affected by the acts or omissions of other members of its group.

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

The management of the organisation's borrowing, 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.