MoleValley District Council

Agenda Item 7

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Ward(s) affected	None specifically

Subject	**Treasury Management Strategy 2017/18 to 2019/20**

RECOMMENDATIONS

The Audit Committee is asked to :

In considering the Treasury Management Strategy, and in particular the Prudential Indicators, set out in Appendices A and B, either

- Endorse the decisions made by Council
  Or
- Suggest any final amendments, for consideration by the s151 Officer in consultation with the Chairman of the Council and the Chairman of Audit Committee

(Note: Council has already agreed, having provisionally approved this report on 21st February, that the S151 Officer, in consultation with the Chairman of the Council and the Chairman of the Audit Committee, be authorised to make any final amendments following consideration by the Audit Committee.)

CORPORATE PRIORITY OUTCOMES

Strong governance arrangements require resources to be directed in accordance with the agreed strategies and according to prudential indicators and limits as set out in the Treasury Management Strategy.

It is important that there is sound and inclusive decision making and that there is clear accountability for the use of those resources in order to achieve desired outcomes for communities and service users.

The Council's investment priorities are security (first), liquidity (second) and finally yield.

The Council has the authority to determine the Recommendations.

1. TREASURY MANAGEMENT STRATEGY - BACKGROUND

1.1 The Council's Medium Term Financial Plan, approved in 2013, sets out the need to replace reducing Government Grant by income generated through making the best use of assets. The reduction in grant announced for 2016/17 and 2017/18 has accelerated the need to pursue a policy of property investment to generate income in support of services.

1.2 Consequently, on 11th October 2016, the Council approved an Asset Investment Strategy (AIS) which approved the addition of £48.530m to the Capital Programme for the acquisition of property assets, in order to generate additional income of at least £0.75m pa by 2020 to offset likely future reductions in government funding. Currently it is anticipated that suitable properties will be purchased over a three year period.

1.3 Legislation does not permit the Council to purchase assets purely for commercial purposes, and therefore the Council has recently incorporated a holding company and subsidiary – both wholly owned by MVDC. The Council will borrow funds in order to be able to invest in these companies to facilitate the acquisition of suitable property assets.

1.4 Capital expenditure in 2016/17 has exceeded the level of reserves available to finance the capital programme. It will be necessary to borrow funds in order to fully finance both the 2016/17 capital expenditure and future year's capital programmes.

1.5 The Treasury Management Strategy sets out the appropriate indicators, authorities and limits, within the Prudential Code, to enable the Council to borrow to fund its approved capital programme. The Code requires that these indicators are set and approved before the start of the financial year.

1.6 To provide the necessary capacity to support both the AIS and the Council's approved capital programme, the Treasury Management Strategy at Appendix B provides for up to £69m of borrowing in the 2017/18. This gives full flexibility for the whole of the AIS £48m provision to be spent within one financial year, if appropriate opportunities arise.

1.7 The Treasury Management Strategy fulfils four key legislative requirements, comprising the four sections listed below.

(i) <u>10 Prudential Indicators</u> – to demonstrate overall control of capital expenditure and that the level of expenditure is sustainable and affordable. They are required by legislation to be set and approved before the start of the year, monitored during the year and reported on at year end. They address:-

1. Plans for capital expenditure – the projected capital expenditure for each of the next three years and the source of funding.

2. Capital Financing Requirement – the anticipated need for borrowing where capital cannot be financed by existing resources.

3. Affordability indicator – the ratio of capital financing costs to the net revenue budget.

4. Affordability Indicator - the impact of capital investment decisions on Council Tax.

5. Comparison of borrowing estimate and capital financing requirement, to confirm that borrowing is intended for capital purposes only.

6. Operational Boundary for external debt – is based on the Authority's estimate of most likely, ie prudent, but not worst case scenario for external debt.

7. Authorised Limit for external debt – is the maximum amount of debt that the Authority can legally owe. The Authorised Limit provides headroom over and above the Operational Boundary for unusual cash movements.

8. To preserve liquidity, the maximum value of investments for more than one year.

9. To assess interest rate exposure, the upper limit on variable, as opposed to fixed, interest rates for debt as well as investments.

10. The maturity structure of fixed interest rate borrowing, to regulate the Council's exposure to large repayment requirements.

(ii) Minimum Revenue Provision

This sets out how the Council will calculate an appropriate amount to set aside towards the principal repayment of the borrowing incurred.

(iii) Treasury Management Strategy Statement

The Council's treasury activities are strictly regulated by statutory requirements and a professional code of practice. This statement sets out the parameters of day to day treasury management and the limitations on activity determined by Prudential Indicators 5 to 10 above. It also includes the Borrowing Strategy which is set out in greater detail than in recent years, to reflect the fact that the Council is no longer debt-free.

(iv) Financial Investment Strategy

This sets out the Council's criteria for selecting investment counterparties and limiting its exposure to the risk of loss.

1.8 A requirement of the Code of Practice on Treasury Management is that the approach forms part of the Council's financial regulations. This is shown at Annex B4. The policies and parameters provide an approved framework within which the officers undertake the day-to-day capital and treasury activities.

Financial Implications – are covered in the body of this report.

Legal Implications - In addition to the statutory requirements mentioned in the report, the prudential indicators, the treasury management strategy and annual plan must be approved before the start of the new financial year, in this case, 1st April, 2017.

2. CORPORATE IMPLICATIONS

Monitoring Officer commentary – The Monitoring Officer confirms that all relevant legal implications have been taken into account.

S151 Officer commentary – The S151 Officer confirms that all financial implications have been taken into account.

Risk Implications - Risk inherent in the Council's borrowing and investment strategy have been considered throughout this report in line with statutory guidance and the requirement to set indicators that are affordable, sustainable and prudent.

Risk Management is a fundamental aspect of implementing an effective Treasury Management Strategy. The Strategy outlines the way in which the Council's investments will be managed and there is always an element of risk in these activities. This Strategy provides a framework that it considers provides a return on the Council's investments, but without placing these at undue risk.

Clearly the nature of the financial markets is such that the risks can vary throughout the year. These will be managed in line with the usual ongoing risk arrangements, although in addition the Finance Team maintain an overview of these risks and will vary the investments, in consultation with the Deputy Chief Executive (Section 151 Officer), Executive Member for Finance and Investments and Chairman of Audit Committee, as considered appropriate.

Equalities Implications

There are no equalities implications arising as a direct consequence of this report.

Employment Issues

None identified in this report.

Sustainability Issues

None identified in this report

Consultation

Capita Asset Services' (Capita Asset Services is a trading name of Capita Treasury Solutions Limited and are the Council's treasury management advisors) views have been incorporated within this report.

BACKGROUND PAPERS

CIPFA – The Prudential Code for Capital Finance in Local Authorities (2011 Edition).
CIPFA – Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes (2011 Edition).
Capita Asset Services Model Treasury Management Strategy Statement 2017/18.
The Council's latest Medium Term Financial Statement (MTFS).
DCLG - Guidance on Local Government Investments (2010).
Treasury Management (Internally Managed Funds) System Document – including Treasury Management Practices (TMPs).

List of Appendices

Appendix A	The Capital Prudential Indicators 2017/18 – 2019/20 and the Minimum Revenue Provision (MRP) Statement
Appendix B	Treasury Management Strategy 2017/18 – 2019/20 (including treasury management indicators)

List of Annexes

Annex B1	Treasury Management Practice (TMP) 1 – Credit and Counterparty Risk Management
Annex B2	Security, Liquidity and Yield Benchmarking
Annex B3	Approved countries for investments
Annex B4	Treasury Management Clauses to form part of Standing Orders / Financial Regulations / Constitution
Annex B5	The Treasury Management role of the Section 151 Officer

The Capital Prudential Indicators 2017/18 -2019/20

Introduction

1. The Local Government Act 2003 requires the Council to adopt the CIPFA Prudential Code and produce prudential indicators. Each indicator either summarises the expected capital activity or introduces limits upon that activity, and reflects the outcome of the Council's underlying capital appraisal systems. The Council is asked to approve the prudential indicators set out below for the period up to 2019/20. The prudential indicators are revised and updated annually so the figures for the second and third years are indicative at this stage.
2. Within this overall prudential framework there is an impact on the Council's treasury management activity, as it will directly impact on borrowing or investment activity. As a consequence the treasury management strategy for 2017/18 – 2019/20 is included in Appendix B to complement these indicators. Some of the prudential indicators are shown in the treasury management strategy to aid understanding.

The Capital Expenditure Plans

3. The Council's capital expenditure plans are the key driver of treasury management activity and are reflected in prudential indicators, which are designed to assist members' overview and confirm the plans.
4. The Council's capital expenditure plans are summarised overleaf and this forms the first of the prudential indicators. The figures represent forecasts of capital spend in the year and therefore differ from the Capital Programme that is set out as part of the budget report (for Council on 21st February). This shows individual capital schemes and the year in which they are scheduled to start. A certain level of capital expenditure is grant supported by the Government (ie for Mole Valley, grants towards disability adaptations). Any decisions by the Council to spend above this level will be considered unsupported capital expenditure. This unsupported capital expenditure needs to have regard to:
   - Service objectives (e.g. strategic planning);
   - Stewardship of assets (e.g. asset management planning);
   - Value for money (e.g. option appraisal);
   - Prudence and sustainability (e.g. implications for external borrowing and whole life costing);
   - Affordability (e.g. implications for the council tax and rents);
   - Practicality (e.g. the achievability of the Corporate Plan).
5. The revenue consequences of capital expenditure, particularly the unsupported capital expenditure, will need to be paid for from the Council's own resources.
6. This capital expenditure can be paid for immediately (by applying capital resources such as capital receipts, capital grants or revenue resources), but if these resources are insufficient any residual capital expenditure will add to the Council's borrowing need. From 2016/17 onwards, there are insufficient capital reserves available to fully finance capital expenditure, and the Council will borrow to fund the shortfall on an on-going basis.

7. The key risks to the plans are that the level of Government support has been estimated and therefore maybe subject to change. Similarly some estimates for other sources of funding, such as capital receipts, may also be subject to change over this timescale. For instance, slow down or a lack of developer contributions, implementation of the Community Infrastructure Levy (CIL) arrangements or due to Government legislation amendments eg a change in policy in November 2014 which reduced the developer contributions towards affordable housing on small-scale developments.

8. The Council is asked to approve the summary capital expenditure projections below. The levels of expenditure for 2016/17 to 2019/20 are higher due to the inclusion of the Asset investment Strategy, the refurbishment of Pippbrook Offices and the regeneration of the Meadowbank, Dorking football ground. This forms the first prudential indicator:

Prudential Indicator 1 – Capital Expenditure Plans

Capital	2015/16 Actual £m	2016/17 Forecast Outturn £m	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m
Capital Expenditure	6.692	18.955	24.828	22.358	18.867
Financed by:					
Capital reserves	-4.355	-5.154	-0.900	-0.900	-0.900
Government grants	-0.328	-0.606	-0.600	-0.600	-0.600
Other grants and conts	-1.854	-3.041	-0.053	0.000	0.000
Revenue	-0.155	-1.005	-2.003	-1.470	-1.270
Net financing need for the year	**0.000**	**9.149**	**21.272**	**19.388**	**16.097**

The Council’s Borrowing Need (the Capital Financing Requirement)

9. The second prudential indicator is the Council’s Capital Financing Requirement (CFR). The CFR is that element of historic capital expenditure which has not yet been paid for through capital or revenue resources. It therefore reflects the underlying need to finance capital expenditure by borrowing or other long-term liability arrangements. In Mole Valley’s case, the Council will be required to undertake borrowing of a projected £21m in 2017/18 to finance capital expenditure.

10. In addition to the proposed borrowing, some of our contract arrangements are deemed to constitute ‘finance leases’ and are therefore long-term liabilities for the purpose of these regulations.

11. The Council is asked to approve the CFR projections below:

Prudential Indicator 2 – CFR Projections

	2015/16 Actual £m	2016/17 Forecast Outturn £m	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m
Capital Financing Requirement (CFR)	2.675	10.544	31.515	50.367	65.534

Net financing need for the year (above)	0.000	9.149	21.272	19.388	16.097
Less MRP and other financing movements	-0.115	-1.280	-0.301	-0.536	-0.930
Movement in CFR	-0.115	7.869	20.971	18.852	15.167

13. The Council is required to pay off an element of the accumulated capital spend each year (the CFR) through a revenue charge (the Minimum Revenue Provision - MRP).

14. DCLG regulations have been issued which require the full Council to approve an MRP Statement in advance of each year. A variety of options are provided to councils, so long as there is prudent provision. The Council is recommended to approve the following MRP Statement which has been revised following the approval of the AIS. Changes from the previous year's version are highlighted in italics.

MRP Statement 2017/18:

- For all unsupported borrowing, the Council will use the **Asset Life Method** as its main method of applying MRP i.e. – MRP will be based on the estimated life of the assets.
- In the case of Finance Leases, the MRP requirement is regarded as met by a charge equal to the rent or charge (as applicable) element of the write down of the liability.
- *Where loans for capital purposes are made to other bodies, no MRP will be charged if the company is making annual loan repayments to MVDC. MVDC will treat these repayments as capital receipts which will be set aside to redeem debt.*

15. The application of resources (capital reserves (receipts), other reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year-end balances for each resource and anticipated day-to-day cash flow balances.

	2015/16 Actual £m	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m
Fund Balances/Reserves	5.290	1.690	1.690	1.690	1.690
Capital Reserves	5.243	0.000	0.000	0.000	0.000
Earmarked Reserves	9.384	7.899	6.496	6.346	6.196
Total Core Funds	**19.917**	**9.589**	**8.186**	**8.036**	**7.886**
Working Capital *	2.000	2.000	2.000	2.000	2.000
Expected Investments	**21.917**	**11.589**	**10.186**	**10.036**	**9.886**
Investments Change		**-10.328**	**-1.403**	**-0.150**	**-0.150**

* Working capital balances shown are estimated year end, these may be higher mid-year.

Affordability Prudential Indicators

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

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

<u>Prudential Indicator 3 – Ratio of financing costs to net revenue stream</u>

	2015/16 Actual £m	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m
Net Financing Cost (Borrowing)	0.000	0.071	0.525	0.566	0.740
Net Financings (TM Investments)	-0.480	-0.370	-0.325	-0.325	-0.325
Revenue Budget	10.060	9.972	9.430	8.616	7.947
Ratio	**-4.77%**	**-3.00%**	**2.12%**	**2.80%**	**5.22%**

18. The estimates of financing costs include current commitments and the proposals in the 2017/18 budget report.

19. **Incremental impact of capital investment decisions on the Council Tax** – This indicator identifies the revenue costs associated with changes to the three year capital programme compared to the Council's existing approved commitments and current plans.

Prudential Indicator 4 - Incremental impact of capital investment decisions on the Band D Council Tax

	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m
Interest Rate Assumption (Investments)	0.25%	0.25%	0.50%	0.50%
Interest Rate Assumption (Borrowing)	2.71%	2.70%	2.90%	3.10%
Net Increase/(Decrease) in Revenue Expenditure Arising From Capital Investment Decisions	-0.216	-0.477	-1.060	-1.063
Council Tax Base	39,884	40,257	40,358	40,459
Increase/(Decrease) in Band D Council Tax	-£5.43	-£11.85	-£26.26	-£26.26

Appendix B

Treasury Management Strategy 2017/18 – 2019/20

1. This Authority adopts the following form of words to define the policies and objectives of its treasury management activities:

   This Authority defines its treasury management activities as:

   - The management of the Authority's investments and cash flows, its banking, money market and capital market transactions. The effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks.
   - This Authority regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Authority.
   - This Authority acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

2. The treasury management service is an important part of the overall financial management of the Council's affairs. The prudential indicators in Appendix A consider the affordability and impact of capital expenditure decisions, and set out the Council's overall capital framework. The treasury service considers the effective funding of these decisions. Together they form part of the processes that ensure the Council meets its balanced budget requirement under the Local Government Act 2003.
3. The Council's treasury activities are strictly regulated by statutory requirements (the Local Government Finance Act 2003, the CIPFA Prudential Code, CLG MRP and investment guidance) and a professional code of practice (the CIPFA Code of Practice on Treasury Management – revised 2011). This Council has adopted the revised Code.
4. As a result of adopting the Code the Council also adopted a Treasury Management Policy Statement. This adoption is a requirement of one of the prudential indicators. The Treasury Management Policy Statement is appended at Annex B4.
5. The Council's Constitution requires an annual strategy to be reported to Council outlining the expected treasury activity for the forthcoming 3 years. A key requirement of this report is to explain both the risks and the management of the risks associated with the treasury service. A further treasury report is produced monitoring the mid-year position as well as a report after the year-end detailing the actual activity for the year. The above reports are required to be adequately scrutinised before being recommended to Council. The scrutiny role is undertaken by the Audit Committee.
6. This Strategy covers:
   - Debt and investment projections (including the Operational Boundary);
   - Limits to borrowing activity (including the Authorised Limit for external debt);
   - Expected movement in interest rates;
   - Borrowing strategy;

- Investment strategy;
- Economic investment considerations;
- Sensitivity to interest rate movements;
- Treasury management limits on activity;
- Additional treasury issues.

Debt and Investment Projections 2017/18 – 2019/20

<u>Prudential Indicator 5 - Gross Borrowing and Long-term Liabilities and the Capital Financing Requirement (CFR).</u>

7. In order to ensure that borrowing will only be for a capital purpose, the Council should ensure that gross external borrowing does not, except in the short-term, exceed the total CFR (ie the underlying capital borrowing need).

	2015/16 Actual £m	2016/17 Forecast Outturn £m	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m
External debt					
Debt at 1st April	0.000	0.000	9.149	30.421	49.809
Expected change in debt	0.000	9.149	21.272	19.388	16.097
Other long-term liabilities (OLTL)	2.790	2.790	1.530	1.530	1.530
Expected change in OLTL	0.000	-1.260	0.000	0.000	0.000
Actual gross debt at 31st March	**2.790**	**10.679**	**31.951**	**51.339**	**67.436**
Less Investments	**-21.917**	**-11.589**	**-10.186**	**-10.036**	**-9.886**
Net Debt	**-19.127**	**-0.910**	**21.765**	**41.303**	**57.550**
Capital Financing Requirement	2.675	10.544	31.515	50.367	65.534
Under/(over) borrowing	**21.802**	**11.454**	**9.750**	**9.064**	**7.984**

Net Debt Exceeds CFR?	**No**	**No**	**No**	**No**	**No**

Treasury Indicators: Limits to Borrowing Activity

8. Within the prudential indicators there are a number of key indicators to ensure the Council operates its activities within well-defined limits.

9. One of these is that the Council needs to ensure that its total borrowing does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2017/18 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

10. The Deputy Chief Executive (Section 151 Officer) reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in the 2017/18 budget report.

11. The borrowing requirement comprises the expected movement in the CFR and any maturing debt that will need to be re-financed. The table below shows this effect on the treasury position over the next three years. The **Operational Boundary** (Prudential Indicator 6) is an indicator based on the expected maximum external debt during the course of the year and focuses on day-to-day treasury management activity. It is not a limit in the strictest sense in that it may be breached. The Operational Boundary represents a level of short-term indebtedness that the Deputy Chief Executive (Section 151 Officer) considers would be prudent to cover any unforeseen circumstance that may arise in the management of the Council's day-to-day cash flow activities. The Council has a policy of never going into overdraft. It is advisable that this limit is set at £63.92m in 2017/18. The steep increase in this limit is to provide the authority with maximum flexibility with regard to the purchase of property assets relating to the AIS: it is possible that £48.53m of borrowing could be incurred in a single year if suitable property assets are identified. This limit is lower than the Authorised Limit (Prudential Indicator 7) which allows cash flow activities to lead to occasional, but not sustained, breaches of the Operational Boundary.

12. The Operational Boundary links directly to the Council's estimates of the CFR and estimates of other cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent, but not worst case scenario but without the additional headroom included within the Authorised Limit.

13. The Deputy Chief Executive (Section 151 Officer) has the authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on consideration of the risk the Council may be exposed to in the course of pursuing its responsibilities and it is considered the current spread of the Council's investment portfolio provides sufficient capacity to counteract any adverse economic news regarding security of financial institutions. Any movement between these separate limits would be reported to the next meeting of the Audit Committee.

Prudential Indicator 6 – Operational Boundary

Operational Boundary	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m
Debt	9.149	62.545	65.399	64.680
Other long-term liabilities	1.395	1.375	1.355	1.335
Total	**10.544**	**63.920**	**66.754**	**66.015**

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

16. This is the statutory limit determined under Section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although no control has yet been exercised.

17. The Council is asked to approve the following Authorised Limit:

Prudential Indicator 7 – Authorised Limit

Authorised Limit	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m
Debt	10.649	67.545	70.399	69.680
Other long term liabilities	1.530	1.510	1.490	1.470
Total	**12.179**	**69.055**	**71.889**	**71.150**

18. Borrowing in advance of need – The Council has some flexibility to borrow funds in year for use in future years. The Deputy Chief Executive (Section 151 Officer) may do this under delegated power where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or meet budgetary constraints. Whilst the Deputy Chief Executive (Section 151 Officer) will adopt a cautious approach to any such borrowing, where there is a clear business case for doing so borrowing may be undertaken to fund the approved capital programme. Borrowing in advance will be made within the constraints that:

- It will be limited to no more than the expected increase in borrowing need (CFR) over the three year planning period; and
- Would not look to borrow more than 18 months in advance of need.

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

Borrowing Strategy 2017/18 – 2019/20

20. The Council expects to borrow up to £10m in 2016/17 to fund the capital programme. The Council may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing in any particular year.

21. **Objectives**: The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

22. **Strategy:** Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer term stability of the debt portfolio. With interest rates currently low, the Council has fixed its borrowing for the longer term to give certainty of cost. However for future

borrowings it may be more cost effective to borrow for a shorter period and then renew or to use internal resources where available.

23. In addition, the Council may borrow short-term loans (normally for up to one month) to cover unexpected cash flow shortages.

24. **Sources**: The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB) and any successor body
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except Surrey Pension Fund)
- UK Municipal Bond agency Plc, such as the LGA bond company, created to enable local Council bond issues
- Local Enterprise Partnership

25. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- operating and finance leases
- hire purchase
- Private Finance Initiative
- sale and leaseback

26. The Council will generally raise all of its long-term borrowing from the PWLB but will continues to investigate other sources of finance, such as local Council loans and bank loans, that may be available at more favourable rates. Currently the Council has borrowed £10m from the PWLB.

27. **Short-term and Variable Rate loans**: These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators below.

28. **Debt Rescheduling**: The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

29. The Council commenced borrowing to fund the capital programme during 2016/17, and it going forward it will be necessary to fund at least part of all future capital programmes from borrowing. This is reflected in the revised Operational Boundary and Affordable Limits set out above.

Financial Investment Strategy 2017/18 – 2019/20

30. The Council’s investment strategy has regard to the Department for Communities and Local Government’s (DCLG) Guidance on Local Government Investments (‘the Guidance’) and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes (‘the CIPFA Treasury Management (TM) Code’).

31. In accordance with the above guidance from the DCLG and CIPFA, and in order to minimise the risk to investments, the Council applies minimum acceptable

credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk.

32. Continuing regulatory changes in the banking sector are designed to see greater stability, lower risk and the removal of expectations of Government financial support should an institution fail. This withdrawal of implied sovereign support is anticipated to have an effect on ratings applied to institutions. This will result in the key ratings used to monitor counterparties being the short-term and long-term ratings only. Viability, Financial Strength and Support Ratings previously applied will effectively become redundant. This change does not reflect deterioration in the credit environment but rather a change of method in response to regulatory changes.

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

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

35. Investment instruments identified for use in the financial year are listed in Annex B1 under the 'specified' and 'non-specified' investment categories.

36. **Key Objectives -** The Council's primary objectives for its investment strategy are safeguarding the repayment of the principal and interest of its investments on time first and ensuring adequate liquidity second. The investment return being a third objective. Following the economic background (Annex B6), the current investment climate has one over-riding risk consideration that of counterparty security risk.

37. **Risk Benchmarking** – A development in the revised Codes and the Department for Communities and Local Government (DCLG) consultation paper is the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance. Discrete security and liquidity benchmarks are fairly new requirements to the Member reporting, although the application of these is more subjective in nature. Additional background in the approach taken is attached at Annex B2.

38. These benchmarks are broad limits and so may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that officers' will monitor the current and trend position and amend the operational strategy depending on any changes. Any breach of the benchmarks will be reported, with supporting reasons in the Mid-Year or Annual Report.

39. **Security** - The Council's maximum security risk benchmark for the current portfolio, when compared to historic default tables, is:

    - 0.07% historic risk of default when compared to the whole portfolio.

    Note: This benchmark is an average risk of default measure, and would not constitute an expectation of loss against a particular investment.

40. **Liquidity** – In respect of this area the Council seeks to maintain:
    - Bank overdraft - £100,000
    - Liquid short-term deposits of at least £1m available with a week's notice.

41. **Yield** - Local measures of yield benchmarks are:
    - Investments – Internal returns above the 7-day LIBID (London Interbank BID) rate.

42. **Creditworthiness policy -** The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle the Council will ensure:
    - It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security and monitoring their security. This is set out in the Specified and Non-Specified investment sections below.
    - It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

43. The Deputy Chief Executive (Section 151 Officer) will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. The criteria is separate to that which chooses Specified and Non-Specified investments as it provides an overall pool of counterparties considered high quality the Council may use rather than defining what its investments are.

44. Credit rating information is supplied by our treasury consultants on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers' almost immediately after they occur and this information is considered before dealing.

45. The criteria for providing a pool of high quality investment counterparties both Specified and Non-specified investments are; (refer to Annex B1 for a definition of each)
    - Banks 1 - Good Credit Quality – the Council will only use banks which:

      (a) are UK banks (it should be noted that 'Banks 1' criteria <u>does not</u> rely upon the UK sovereign rating remaining at AA); and/or

      (b) are non-UK and domiciled in a country which has a minimum sovereign long term rating of AAA (see Annex B3).

      And have, as a minimum, the following credit ratings (where rated):

      (a) Short Term – F1/P-2/A-1 (Fitch/Moody's/Standard and Poor's)

      (b) Long Term – A/A3/A (Fitch/Moody's/Standard and Poor's)
    - Banks 2 – Guaranteed Banks with suitable Sovereign Support – In addition, the Council will use banks whose ratings fall below the criteria specified above if all of the following conditions are met:

      (a) wholesale deposits in the bank are covered by a government guarantee;

(b) the government providing the guarantee is rated ‘AAA’ by all three major rating agencies (Fitch, Moody’s and Standard & Poor’s); and

(c) the Council’s investments with the bank are limited to amounts and maturities within the terms of the stipulated guarantee.

- Banks 3 – Part nationalised UK bank – Royal Bank of Scotland. This bank can be included provided it continues to be part nationalised or it meets the ratings in Banks 1 above.
- Banks 4 – The Council’s own banker, National Westminster Bank, for transactional purposes if the bank falls below the above criteria, although in this case balances will be minimised in both monetary size and time invested.
- Building Societies – the Council may use all UK Societies which:
  - have assets in excess of £1 billion
- Money Market Funds (MMFs) – any AAA rated fund
- UK Government (including gilts and the DMADF (Debt Management Account Deposit Facility)).
- Supranational bonds
- Local Authorities, Parish Councils etc – the maximum permitted investment with any one bank/building society/fund is £7.5million (as agreed by Council – 22nd February 2011).
- Pooled property funds – up to £7.5m

A limit of 60% will be applied to the use of Non-Specified investments.

46. **Country and sector considerations** - Due care will be taken to consider the country, group and sector exposure of the Council’s investments. In part the country selection will be chosen by the credit rating of the Sovereign state in Banks 1 above. In addition:
    - no more than 20% will be placed with any non-UK country at any time;
    - limits in place above will apply to a group of companies;
    - sector limits will be monitored regularly for appropriateness.

47. **Use of additional information other than credit ratings** – Additional requirements under the Code of Practice now requires the Council to supplement credit rating information. Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information (for example Credit Default Swaps (CDS), negative rating watches/outlooks) will be applied to compare the relative security of differing investment counterparties.

48. **Time and monetary limits applying to investments** - The time and monetary limits for institutions on the Council’s Counterparty List are as follows (these will cover both Specified and Non-Specified Investments):

	Fitch (or equivalent)	Money Limit	Time Limit
Upper Limit Category – UK Banks and Building Societies	A (Minimum long-term credit rating)	£7.5m	5 years
Middle Limit Category – UK Banks and Building Societies	F1 (Minimum short-term credit rating)	£7.5m	364 days
Lower Limit Category – UK Banks and Building Societies	F1 (Minimum short-term credit rating)	£7.5m	364 days
Group Limit (Parent Companies and all subsidiaries)	F1 (Minimum short-term credit rating)	£7.5m	364 days
Other Institution Limits (see note below)	-	£7.5m	364 days
Guaranteed Organisations*	-	£7.5m	*

* Guaranteed institutions will be restricted to the terms of the guarantee.

Note: The Upper and Middle Limit categories - If these are for greater than 1 year, they will include relatively high rated institutions (A). The Lower Limit Category will normally just be used for unrated subsidiaries and building societies. In all cases building societies will have a minimum asset base of £1bn. The Other Institution Limit will be for other local authorities, the Debt Management Account Deposit Facility (DMADF), Money Market Funds and Gilt and Supranational investments. These are all considered high quality names – although not always rated – and therefore will likely have the same limit as the Upper Category.

49. The proposed criteria for Specified and Non-Specified investments are shown in Annex B1 for approval.

50. In the normal course of the Council's cash flow operations it is expected that both Specified and Non-Specified investments will be utilised for the control of liquidity as both categories allow for short-term investments.

51. The use of longer-term instruments (greater than one year from inception to repayment) will fall in the Non-Specified investment category. These instruments will only be used where the Council's liquidity requirements are safeguarded. This will also be limited by the longer-term investment limits.

52. **Country Limits** - The Council currently limits its investment criteria to entities domiciled in the UK, although the Strategy does allow use of foreign banks as long as they meet the minimum long-term credit rating of A and sovereign rating of AAA. When combined with the prudent credit criteria, this means that potential financial institutions will be limited. Given the expected total investments this means that the current £7.5m limit will force the Council to either invest with other local authority bodies or direct with the UK government via the Debt Management Office (DMO) deposit facility. Both of these options will likely act as a drag on overall investment performance.

Economic Investment Considerations

53. **In-house funds –** investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (ie rates of investments up to 12 months). During the first six months of 2016/17 funds were moved from short-term investments where interest rates were performing at historically low levels. These funds were re-invested in, better performing, property purchases that generated a rental income. This trend continued in the second half of 2016/17 and will be the case in 2017/18 leaving only a sufficient level of funds to meet day to day cash flow requirements.

54. **Investment returns expectations** - the Bank Rate is forecast to stay flat at 0.25% until quarter 2 2019 and not rise above 0.75% by quarter 1 2020. Bank Rate forecasts for financial year ends (March) are:

- 2016/17 0.25%
- 2017/18 0.25%
- 2018/19 0.25%
- 2019/20 0.50%

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

- 2016/17 0.25%
- 2017/18 0.25%
- 2018/19 0.25%
- 2019/20 0.50%
- 2020/21 0.75%
- 2021/22 1.00%
- 2022/23 1.50%
- 2023/24 1.75%
- Later years 2.75%

The overall balance of risks to these forecasts is currently probably slightly skewed to the downside in view of the uncertainty over the final terms of Brexit. If growth expectations disappoint and inflationary pressures are minimal, the start of increases in Bank Rate could be pushed back. On the other hand, should the pace of growth quicken and/or forecasts for increases in inflation rise, there could be an upside risk ie Bank Rate increases occur earlier and/or at a quicker pace.

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

<u>Prudential Indicator 8 – Principal Sums Invested > 364 days</u>

Maximum principal sums invested > 364 days			
	2017/18	**2018/19**	**2019/20**
Principal sums invested > 364 days	£12m	£12m	£12m

Sensitivity to Interest Rate Movements

56. Future Council accounts will be required to disclose the impact of risks on the Council's treasury management activity. Whilst most of the risks facing the treasury management service are addressed elsewhere in this report (credit risk, liquidity risk, market risk, maturity profile risk), the impact of interest rate risk is discussed but not quantified. The table below highlights the estimated impact of a 1% increase/decrease in all interest rates to the estimated treasury management costs/income for next year. That element of the debt and investment portfolios which are of a longer term, fixed interest rate nature, will not be affected by interest rate changes.

Revenue Budgets	**2017/18 Estimated + 1%**	**2017/18 Estimated - 1%**
Interest on borrowing	£355,545	£355,545
Investment income	£230,000	£230,000

Treasury Management Limits on Activity

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

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

58. The Audit Committee is asked to approve the limits:

<u>Prudential Indicator 9 – Interest Rate Exposures</u>

Interest rate exposures	2016/17	2017/18	2018/19
	Upper	Upper	Upper
Limits on variable interest rates:			
• Debt only	20%	20%	20%
• Investments only	50%	50%	50%
Limits on fixed interest rates:			
• Debt only	100%	100%	100%
• Investments only	100%	100%	100%

<u>Prudential Indicator 10 – Fixed Interest Rate Borrowing</u>

Maturity Structure of fixed interest rate borrowing 2017/18		
	Lower	Upper
Under 12 months	0%	25%
12 months to 2 years	0%	25%
2 years to 5 years	0%	25%
5 years to 10 years	0%	50%
10 years and above	0%	100%

Additional treasury issues

Performance Indicators

59. The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking. These are:

    - Investments – Internal returns above the 7 day LIBID rate

    The results of these indicators will be reported in the Treasury Management Annual Report.

Treasury Management Advisors

60. The Council uses Capita Asset Services as its external treasury management advisor. The company provides a range of services that include:

    - Technical support on treasury matters and capital finance issues;
    - Economic and interest rate analysis;
    - Generic investment advice on interest rates, timing and investment instruments;

- Credit ratings/market information service comprising the three main credit rating agencies;
- Attendance at Member/Officer treasury management review meetings.

61. Whilst the advisors provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice, the final decision on treasury matters remains with the Council.

62. This service is subject to regular review.

Member and Officer Training

63. The increased Member consideration of treasury management matters and the need to ensure officers dealing with treasury management are trained and kept up to date requires a suitable training process for members and officers. This Council has addressed this important issue by:

- The training needs of treasury management officers' are periodically reviewed.
- Members' attendance at meetings with our treasury advisors.

Treasury Management Practice (TMP) 1 – Credit and Counterparty Risk Management

The Council's investment policy has regard to the Department for Communities and Local Government (DCLG) Guidance on Local Government Investments ('the Guidance') issued in 2010 and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ('the CIPFA TM Code'). The Council's investment priorities will be **security** first, **liquidity** second and finally **yield**.

The Guidance forms the structure of the Council's policy below.

The key intention of the Guidance is to maintain the current requirement for Councils' to invest prudently, and that priority is given to security and liquidity before yield. In order to facilitate this objective the Guidance requires this Council to have regard to the CIPFA publication Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. This Council adopted the Code on 23rd February, 2010 and will apply its principles to all investment activity. In accordance with the Code, the Deputy Chief Executive (Section 151 Officer) has produced treasury management practices (TMPs). This part, TMP 1(1), covering investment counterparty policy requires approval each year.

Annual Financial Investment Strategy - The key requirements of both the Code and the investment guidance are to set an annual investment strategy, as part of its annual treasury management strategy for the following year, covering the identification and approval of the following:

- The strategy guidelines for choosing and placing investments, particularly non-specified investments.
- The principles to be used to determine the maximum periods for which funds can be committed.
- Specified investments the Council will use. These are high security (i.e. high credit rating, although this is defined by the Council, and no guidelines are given), and high liquidity investments in sterling and with a maturity of no more than one year.
- Non-specified investments, clarifying the greater risk implications, identifying the general types of investment that may be used and a limit to the overall amount of various categories that can be held at any time.

The investment policy proposed for the Council is:

Strategy Guidelines – The main strategy guidelines are contained in the body of the treasury strategy statement.

Specified Investments – These investments are sterling investments of not more than one-year maturity, or those which could be for a longer period but where the Council has the right to be repaid within 12 months if it wishes. These are considered low risk assets where the possibility of loss of principal or investment income is small. These would include sterling investments that would not be defined as capital expenditure with:

1. The UK Government (such as the Debt Management Account Deposit Facility, UK Treasury Bills or a Gilt with less than one year to maturity).
2. Supranational bonds of less than one year's duration.
3. A local authority, parish council or community council.
4. Pooled investment vehicles (such as money market funds) that have been AAA rated by Standard and Poor's, Moody's or Fitch rating agencies.
5. A body that is considered of a high credit quality (such as a bank or building society). Although non-rated building societies are classified as non-specified

investments. For category 5 this covers bodies with a minimum short term rating of F1/P-2/A-1 as rated by Fitch, Moody's or Standard and Poor's rating agencies.

Within these bodies, and in accordance with the Code, the Council has set additional criteria to set the time and amount of monies which will be invested in these bodies. This criterion is detailed in paragraph 39 of Appendix B.

Non-Specified Investments – Non-specified investments are any other type of investment (i.e. not defined as Specified above). The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out below. Non-specified investments would include any sterling investments with:

	Non Specified Investment Category	**Limit**
a.	**Supranational Bonds greater than 1 year but less than 5 years to maturity** **(a) Multilateral development bank bonds** - These are bonds defined as an international financial institution having as one of its objects economic development, either generally or in any region of the world (e.g. European Investment Bank etc.). **(b) A financial institution that is guaranteed by the United Kingdom Government** (e.g. The Guaranteed Export Finance Company (GEFCO)). The security of interest and principal on maturity is on a par with the Government and so very secure, and these bonds usually provide returns above equivalent gilt-edged securities. However the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.	£7.5m
b.	**Gilt edged securities** with a maturity of greater than one year. These are Government bonds and so provide the highest security of interest and the repayment of principal on maturity. Similar to category (a) above, the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.	£7.5m
c.	The **Council's own banker** (National Westminster Bank Plc) if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as is possible.	£7.5m
d.	**Building societies not meeting the basic security requirements under the specified investments**. The operation of some building societies does not require a credit rating, although in every other respect the security of the society would match similarly sized societies with ratings. The Council may use such building societies which have a minimum asset size of £1 billion, but will restrict these type of investments to £7.5 million	£7.5m
e.	Any **bank or building society** that has a minimum long-term credit rating of A for deposits with a maturity of greater than one year (including forward deals in excess of one year from inception to repayment).	£7.5m
f.	Any **non-rated subsidiary** of a credit rated institution included in the specified investment category. These institutions will be included as an investment category subject to guarantee from the parent company.	£5m
g.	**Pooled property funds** – the use of these instruments will normally be deemed to be capital expenditure. The key exception to this is an	£7.5m

	investment in the CCLA Property Fund.	

Within categories c and d, and in accordance with the Code, the Council has developed additional criteria to set the overall amount of monies that will be invested in these bodies. This criterion is detailed in Appendix B.

The Monitoring of Investment Counterparties - The credit rating of counterparties will be monitored regularly. The Council receives credit rating information (changes, rating watches and rating outlooks) from Capita Asset Services as and when ratings change and counterparties are checked promptly. On occasion ratings may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria will be removed from the list immediately by the Deputy Chief Executive (Section 151 Officer) and if required new counterparties which meet the criteria will be added to the list. Any urgent and immediate changes that are required to the Treasury Management (TM) Strategy will be directed to the Executive Member for Finance and Investments, Chairman of Audit Committee as well as the Deputy Chief Executive (Section 151 Officer). If all are in agreement the TM Strategy and Treasury Management Practices (TMP's) will be modified to reflect this change. Ultimately any change will be ratified at the next available Council meeting after having been considered at the first available meeting of the Audit Committee.

Use of External Fund Managers – It is the Council's policy to use external fund managers for part of its investment portfolio. On 30th June 2013 the Council invested £5m in the Charities, Churches and Local Authorities (CCLA) Property Fund. This is a high quality, well diversified managed property fund. To realise the full potential of this investment it should be considered as a medium to long term placement. Income is received quarterly and in the current economic climate good yields are anticipated.

The Fund Manager will use non-specified investment categories and are committed to keep to the Council's investment strategy. The performance of the Fund Manager is reviewed monthly by the Deputy Chief Executive (Section 151 Officer).

All other investments are managed by the in-house team.

Policy on the use of external service providers

The Council uses Capita Asset Services, Treasury Solutions as its external treasury management advisor.

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

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

Security, Liquidity and Yield Benchmarking

Benchmarking and Monitoring Security, Liquidity and Yield in the Investment Service - A development for Member reporting are the consideration and approval of security and liquidity benchmarks. These benchmarks are targets and so may be breached from time to time. Any breach will be reported, with supporting reasons in the Annual Treasury Report.

Yield – These benchmarks are currently widely used to assess investment performance. Local measures of yield benchmarks are:

- Investments – internal returns above the 7-day LIBID rate

Security and liquidity benchmarks are already intrinsic to the approved treasury management strategy through the counterparty selection criteria and some of the prudential indicators. Benchmarks for cash type investments are shown below and these form the basis of reporting in this area. In the other investment categories, appropriate benchmarks will be used where available.

Liquidity – This is defined as 'having adequate, though not excessive cash resources, borrowing arrangements, overdrafts or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives' (CIPFA Treasury Management Code of Practice). In respect of this area the Council seeks to maintain:

- Bank overdraft - £100,000
- Liquid short-term deposits of at least £1m available with a week's notice.

The Authority, with the help of its treasury advisor, has developed further benchmarking analysis by the monitoring of the Weighted Average Life (WAL) of the portfolio. This is done by analysing the availability of liquidity and term risk in the portfolio. A shorter WAL would embody less risk. The investment policy that is proposed for internally managed funds is shown in Annex B1.

Security of the investments – In the context of benchmarking security is a much more subjective area to assess. Security is currently evidenced by the application of minimum credit quality criteria to investment counterparties, primarily through the use of credit ratings supplied by the three main credit rating agencies (Fitch, Moody's and Standard and Poor's). Whilst this approach embodies security considerations, benchmarking levels of risk is more problematic. One method to benchmark security risk is to assess the historic level of default against the minimum criteria used in the Council's investment strategy. The table beneath shows average defaults for differing periods of investment grade products for each of the three main credit rating agencies long term rating categories over the period 1990 to 2015.

Long term rating	1 year	2 years	3 years	4 years	5 years
AAA	0.04%	0.10%	0.18%	0.27%	0.37%
AA	0.01%	0.02%	0.08%	0.16%	0.23%
A	0.07%	0.19%	0.36%	0.55%	0.77%

BBB	0.15%	0.46%	0.82%	1.26%	1.73%
BB	0.70%	2.04%	3.48%	5.21%	6.71%
B	3.04%	7.14%	11.06%	14.40%	17.24%
CCC	19.73%	28.03%	33.43%	37.39%	40.41%

The Council's minimum long term rating criteria is currently A, meaning the average expectation of default for a one year investment in a counterparty with a long term rating would be 0.07% of the total investment (eg for a £1m investment the average loss would be £700). This is only an average, any specific counterparty loss is likely to be higher, but these figures do act as a proxy benchmark for risk across the portfolio.

The Council's maximum security risk benchmark for the whole portfolio, when compared to these historic default tables is:

- **0.07% historic risk of default when compared to the whole portfolio.**

These benchmarks are embodied in the criteria for selecting cash investment counterparties and these will be monitored and reported to Members in the Treasury Management Annual Report. As this data is collated, trends and analysis will be collected and reported. Where a counterparty is not credit rated a proxy rating will be applied.

Approved countries for investments

Based on lowest available sovereign rating of;

AAA

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

AA

- UK

Treasury Management Clauses to form part of Standing Orders/Financial Regulations/Constitution

1. The Council adopts the key recommendations of the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management in the Public Services; Code of Practice.

2. The Section 151 Officer will ensure that treasury management activities are administered within the parameters defined and agreed by Council and those defined by statutory requirements and professional best practice.

3. The Section 151 Officer will define and propose for agreement by Council, a treasury management policy statement, stating the policies, objectives and approach to risk management in keeping within the above Code's recommendations and will monitor these throughout the year.

4. The Audit Committee is responsible for ensuring effective scrutiny of the treasury management strategy and activity. The Section 151 Officer will submit reports on its treasury management policies, practices and activities including an annual Treasury Management Strategy, a mid-year review and an annual report after the end of the financial year, in the form prescribed in its Treasury Management Practices (TMPs).

The Treasury Management Role of the Section 151 Officer

The Section 151 (Responsible) Officer

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