CT/17/08
Corporate Services Scrutiny Committee
24 January 2017

TREASURY MANAGEMENT AND INVESTMENT STRATEGY 2017-18

Report of the County Treasurer

Please note that the following recommendations are subject to consideration and determination by the Committee before taking effect.

Recommendation: That the Committee consider whether it wishes to draw to the attention of the Cabinet any observations on the proposals contained within the Treasury Management and Investment Strategy.

1. Introduction

1.1 In February 2016 the Council, in accordance with the revised CIPFA Code of Practice for Treasury Management in the Public Services, adopted a revised Treasury Management Policy Statement together with a statement of its ‘Treasury Management Practices’ (TMPs). No changes are proposed to these policies for 2017/18.

1.2 The policy requires the Council to consider a treasury strategy report, setting out the strategy and plans to be followed in the coming year, as part of the budget process.

2. Treasury Management and Investment Strategy

2.1 The Treasury Management and Investment Strategy is shown in draft at Appendix 1. It sets out the Minimum Revenue Provision (MRP) policy, capital expenditure funding, prudential indicators, the current treasury position, debt and investments; prospects for interest rates; the borrowing strategy; and the investment strategy.

2.2 The MRP policy has not been changed from that adopted for 2016/17. All borrowing (including Vehicle and Equipment Loans Pool), Capitalisation Direction and charges to other public sector bodies and PFI costs will be charged on the period of benefit of the capital investment (on a straight line basis).

2.3 Since 2009 the Council has followed a policy of containing the capital programme, taking out no new external borrowing and repaying debt whenever this can be done without incurring a financial penalty. Capital expenditure new starts have been limited to those that were financed from sources other than borrowing. To meet the need for capital expenditure, the highest priority schemes across the Authority are funded from Corporate Capital Receipts over the Capital Programme timescale.

2.4 The ability of the Council to repay further debt will depend on the cost of repayment and the availability of cash to fund the repayment. Under their current policy the Public Works Loan Board (PWLB) sets premature repayment rates, and where the interest rate payable on a current loan is higher than the repayment rate, the PWLB imposes premium penalties for early repayment. Current interest rate forecasts suggest that it is extremely unlikely that gilt yields will rise sufficiently to cancel out the premiums in the medium term. Use of revenue reserves and internal borrowing to fund the capital programme are likely to reduce the cash balance during 2017/18. As a result the availability of cash to repay external debt will be extremely limited.

2.5 Following the Bank of England's decision to reduce the base rate from 0.5% to 0.25%, in response to the European Union referendum result, the target return for deposits with banks and building societies has been reduced from 0.65% to 0.40% reflecting the current low interest rates on offer from the Council's counterparties. The target rate for the CCLA Property Fund will remain at 4.50%.

3. Conclusion

3.1 The Treasury Management and Investment Strategy will be considered by Cabinet along with the draft budget for 2017/18 on 10 February, and will become part of the budget book to be approved by Council at its budget meeting on 16 February.

3.2 The Committee is invited to make observations on these proposals prior to their consideration by the Cabinet on 10 February.

Mary Davis

Electoral Divisions: All
<u>Local Government Act 1972</u>
<u>List of Background Papers – Nil</u>
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Appendix 1

Treasury Management Strategy 2017/18 – 2019/20 and Prudential Indicators 2017/18 - 2021/22

Introduction

The Treasury Management Strategy sets out the County Council's policies in relation to: the management of the Council's cashflows, its banking, money market and capital market transactions; borrowing and investment strategies; monitoring of the level of debt and funding of the capital programme.

The County Council has adopted the CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management in the Public Services. This is one of the Prudential Indicators required by the Code. The current Code of Practice was published by CIPFA in November 2011, and requires the Council to approve a Treasury Management Policy Statement together with a statement of its 'Treasury Management Practices' (TMPs). A revised Policy Statement and TMPs were agreed by the Council in February 2016. These policies remain appropriate and no changes are proposed for 2017/18.

The County Council is required to monitor its overall level of debt in line with the national code of practice drawn up by CIPFA. Part of this code requires consideration of a set of "prudential indicators" in order to form a judgement about the affordable, prudent and sustainable level of debt.

The prudential indicators, treasury management strategy and the annual investment strategy have been reviewed in line with the Capital Programme 2017/18 – 2021/22.

This Treasury Management Strategy document sets out:

- Minimum revenue provision;
- Capital expenditure funding;
- Prudential indicators on the impact of capital financing and monitoring of the level and make-up of debt;
- The current treasury position, debt and investments;
- Prospects for interest rates;
- The borrowing strategy; and
- The investment strategy.

Minimum Revenue Provision

Minimum Revenue Provision (MRP) is a charge to the authority's revenue account to make provision for the repayment of the authority's external debt and internal borrowing. The authority has a statutory obligation to charge to the revenue account an annual amount of MRP.

The authority's MRP strategy is to charge all elements based on the period of benefit of the capital investment. All supported capital expenditure and unsupported borrowing up to 1st April 2008 and unsupported borrowing post 1 April 2008 (including Vehicle and Equipment Loans Pool), Capitalisation Direction and charges to other public sector bodies will be charged on the period of benefit of the capital investment (on a straight line basis).

We will not provide for MRP in circumstances where the relevant expenditure is intended to be financed from external contingent income, where it has not yet been received but where we conclude that it is more probable than not that the income will be collected.

Capital financing costs are also affected by PFI contracts and finance leases coming 'on Balance Sheet'. This will be charged in-line with the authority's main MRP Policy over the period of benefit of the capital investment, being the asset life.

The main Prudential Indicator to measure the acceptable level of borrowing remains the ratio of financing costs to total revenue stream. The figures for MRP shown in table 6 reflect the adoption of this strategy.

Capital Expenditure

Table 1 shown below, summarises the Capital Programme and liabilities from capital projects that will appear on the balance sheet in future years. The Capital Programme has been tested for value for money via option appraisal and for prudence, affordability and sustainability by looking at the impact that the proposed Capital Programme has on the revenue budget and through the Prudential Indicators.

Table 1 – Capital Expenditure

	2017/18 Estimate £'000	**2018/19 Estimate £'000**	**2019/20 Estimate £'000**	**2020/21 Estimate £'000**	**2021/22 Estimate £'000**
Total Capital programme	**112,050**	**97,989**	**71,423**	**59,487**	**57,945**
Funded by:					
Gross borrowing	10,312	11,055	2,967	1,200	1,218
Other capital resources	101,738	86,934	68,456	58,287	56,727
Total capital programme funding	**112,050**	**97,989**	**71,423**	**59,487**	**57,945**
Total capital expenditure	**112,050**	**97,989**	**71,423**	**59,487**	**57,945**

Prudential Indicators

Capital Financing Requirement

The Capital Financing Requirement represents the Council's underlying debt position. It shows the previous and future spend for capital purposes that has been or will be financed by borrowing or entering into other long term liabilities. The Capital Financing Requirement and debt limits will be higher than the Council's external debt, as they will be partly met by internal borrowing from the Council's internal cash resources. This reduces the cost of the required borrowing, but the Council also needs to ensure that a prudent level of cash is retained.

The forecast Capital Finance Requirement for 2017/18 and the following four years are shown in table 2 below.

Table 2 – Capital Financing Requirement

	2017/18 Estimate £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Underlying borrowing requirement	672,988	665,629	650,280	631,431	616,018
Other long-term liabilities	138,946	133,717	128,637	123,888	118,485
Capital financing requirement	**811,935**	**799,346**	**778,917**	**755,319**	**734,503**

Limits to Debt

The Authorised Limit represents the level at which the Council is able to borrow and enter into other long term liabilities. Additional borrowing beyond this level is prohibited unless the limit is revised by the Council. Table 3 details the recommended Authorised Limits for 2017/18 – 2021/22.

Table 3 – Authorised Limits

	2017/18 Estimate £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Authorised limits for borrowing	742,988	735,629	720,280	701,431	686,018
Authorised limit for other long-term liabilities	138,946	133,717	128,637	123,888	118,485
Authorised limit for external debt	**881,935**	**869,346**	**848,917**	**825,319**	**804,503**

The Operational Boundary is based on the anticipated level of external debt needed during the year. Variations in cash flow may lead to occasional, short term breaches of the Operational Boundary that are acceptable. Sustained breaches would be an indication that there may be a danger of exceeding the Authorised Limits. Table 4 details the recommended Operational Boundaries for 2017/18 and following years.

Table 4 - Operational Limits

	2017/18 Estimate £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Operational limits for borrowing	717,988	710,629	695,280	676,431	661,018
Operational limit for other long-term liabilities	138,946	133,717	128,637	123,888	118,485
Operational limit for external debt	**856,935**	**844,346**	**823,917**	**800,319**	**779,503**

The forecast opening balance for External Borrowing at 1 April 2017 is £507.85 million and remains unchanged at 31 March 2018.

The Council also needs to ensure that its gross debt does not, except in the short term, exceed the total of the Capital Financing Requirement. Table 5 details the Capital Financing Requirement against the total gross debt plus other long term liabilities. The level of under borrowing reflects the use of internal borrowing from the Council's internal cash resources.

Table 5 – Underlying Borrowing Requirement to Gross Debt

	2017/18 Estimate £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Capital financing requirement	811,935	799,346	778,917	755,319	734,503
Gross borrowing and other long-term liabilities	651,467	646,796	641,567	636,487	631,738
Under/ (over) borrowing	**160,468**	**152,551**	**137,350**	**118,832**	**102,766**

The debt management strategy and borrowing limits for the period 2017/18 to 2021/22 have been set to ensure that over the medium term net borrowing will only be for capital purposes.

Ratio of Financing Cost to Net Revenue Stream

Table 6 below shows the relationship between Capital Financing Costs and the Net Revenue Stream for 2017/18 and future years. Financing cost is affected by Minimum Revenue Provision (MRP), interest receivable and payable and reductions in other long term liabilities.

Table 6 – Ratio of Financing Costs to Net Revenue Stream

	2017/18 Estimate £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Minimum revenue provision	18,376	17,241	17,116	18,849	15,431
Interest payable	26,023	26,023	26,023	26,023	26,023
Recharges and other adjustments	(2,136)	(697)	(646)	(2,774)	(3,566)
Interest receivable	(790)	(790)	(790)	(790)	(790)
Capital financing cost (excluding other long-term liabilities)	41,473	41,777	41,703	41,308	37,098
Capital financing costs of other long-term liabilities	15,930	15,362	14,625	14,901	14,636
Capital financing costs including other long-term liabilities	57,403	57,139	56,328	56,209	51,734
Estimated net revenue stream	**492,922**	**493,262**	**510,223**	**497,163**	**497,163**
Ratio of financing costs (excluding other long term liabilities) to net revenue stream	**8.41%**	**8.47%**	**8.17%**	**8.31%**	**7.46%**
Ratio of financing costs (including other long-term liabilities) to net revenue stream	11.65%	11.58%	11.04%	11.31%	10.41%

Incremental Impact on Council Tax

The incremental impact on Council Tax of the investment decisions made in setting the 2017/18 Capital Programme is shown in table 7.

Appendix 1

Table 7 – Impact on Council Tax

	2017/18 Estimate £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Incremental impact on band D council tax payers of investment decisions funded by borrowing	(0.13)	(0.55)	(0.09)	0.08	0.08
Incremental impact on band D council tax payers of investment decisions funded by increased other long-term liabilities	0.00	0.00	0.00	0.00	0.00
Incremental impact on band D council tax payers of capital investment decisions made in setting the 2017/18 MTCP	**(0.13)**	**(0.55)**	**(0.09)**	**0.08**	**0.08**

Treasury Management Prudential Indicators

Where external borrowing is required it can either be at fixed or variable rates of interest, and can be taken out for periods from a year to 50 years. The use of prudential indicators seeks to reduce the risks associated with fixed and variable interest rate loans and with borrowing for different loan periods.

Borrowing at fixed rates of interest for long periods can give the opportunity to lock into low rates and provide stability, but means that there is a risk of missing possible opportunities to borrow at even lower rates in the medium term. Variable rate borrowing can be advantageous when rates are falling, but also means that there is a risk of volatility and a vulnerability to unexpected rate rises.

Borrowing for short periods or having large amounts of debt maturing (and having to be re-borrowed) in one year increases the risk of being forced to borrow when rates are high.

The Council’s policy has been to borrow at fixed rates of interest when rates are considered attractive.

The proposed Prudential Indicators for 2017/18 and beyond are set out in Table 8 below:

Table 8 – Treasury Management Prudential Indicators

Prudential Indicators	Upper Limit %	Lower Limit %
Limits on borrowing at fixed interest rates	100	70
Limits on borrowing at variable interest rates	30	0
Percentage of Fixed Rate Debt maturing in:		
Under 12 months	20	0
12 Months to within 24 months	25	0
24 Months to within 5 Years	30	0
5 years and within 10 Years	35	0
10 years and within 20 years	45	0
20 years and within 35 years	60	0
35 years and within 50 years	75	20

The limits have been set taking into account the CIPFA Code of Practice which requires that the maturity date for LOBO (Lender Option Borrower Option) loans is assumed to be the next call date, rather than the total term of the loan. This will apply to the Council's Money Market loans.

Monitoring the Indicators

It is important to monitor performance against forward looking indicators and the requirement that borrowing should only be for capital purposes. The total level of borrowing will be monitored daily against both the operational boundary and the authorised limit. If monitoring indicates that the authorised limit will be breached, a report will be brought to the Cabinet outlining what action would be necessary to prevent borrowing exceeding the limit and the impact on the revenue budget of breaching the limit. It will be for the Cabinet to make recommendations to the County Council to raise the limit if it is felt appropriate to do so.

The indicators for capital expenditure, capital financing requirement, capital financing costs and the treasury management indicators will be monitored monthly. Any significant variations against these indicators will be reported to the Cabinet.

Analysis of Long Term Debt

The following Table 9 shows the County Council's fixed and variable rate debt as at 31 March 2016 and 31 December 2016 (current).

The interest rates shown do not include debt management costs or premiums/discounts on past debt rescheduling.

There has been no movement in the Council's external debt over the last financial year, as no new borrowing has been required and no further opportunities have arisen to repay debt.

Table 9 – Analysis of Long Term Debt

	Actual 31.03.16 £'m	Interest Rate %	Current 31.12.16 £'m	Interest Rate %
Fixed Rate Debt				
PWLB	436.35	4.99	436.35	4.99
Money Market	71.50	5.83	71.50	5.83
Variable Debt				
PWLB	0.00		0.00	
Money Market	0.00		0.00	
Total External Borrowing	**507.85**	**5.11**	**507.85**	**5.11**

Schedule of Investments

The following schedule shows the County Council's fixed and variable rate investments as at 31 March 2016 and as at 31 December 2016 (current).

Table 10 – Schedule of Investments

	Maturing in:	Actual 31.03.16* £'m	Interest Rate %	Current 31.12.16* £'m	Interest Rate %
Bank, Building Society and MMF Deposits					
Fixed Rates					
Term Deposits	< 365 days	45.00	0.84	45.00	0.80
	365 days & >	0.00		0.00	
Callable Deposits					
Variable Rate					
Call & Notice Accounts		73.80	0.60	37.50	0.56
Money Market Funds (MMFs)		0.00		13.33	0.30
Property Fund		10.00	4.67	10.00	4.49
All Investments		**128.80**	**1.00**	**105.83**	**1.00**

The Council's cash balance available for investment varies during the year, with the balance building up during the first half of the financial year, and then tapering down towards the end of the financial year. It is anticipated that the cash balances at 31st March 2017 will have reduced from £128.8m at the start of the financial year to around £110m (£95m excluding Growing Places Fund money).

The recent investment performance of the County Council's cash has been affected by the low interest rates introduced as part of the measures used to alleviate the global credit crunch. Interest rates have also been impacted by the introduction of new banking regulations requiring banks to hold higher levels of liquidity to act as a buffer.

The rates on offer continue to be low and the returns on the County Council's cash investments are forecast to remain at the current low levels for the foreseeable future; however, the Treasury Management Strategy will continue to ensure a prudent and secure approach.

Prospects for Interest Rates

Forecasting future interest rate movements even one year ahead is always difficult. The factors affecting interest rate movements are clearly outside the Council's control. Whilst short term rates are influenced by the Bank of England's Base Rate, long term rates are determined by other factors, e.g. the market in Gilts. Rates from overseas banks will be influenced by their national economic circumstances. The County Council retains an external advisor, Capita, who forecast future rates several years forward. Similar information is received from a number of other sources.

Following the outcome of the EU referendum in June, the Bank of England decided to reduce UK interest rates from 0.5% to 0.25%, as a result of concerns about the impact of the decision on the UK economy. UK interest rates had already been held at an unprecedented low level of 0.5% since March 2009. Interest rates have also been under pressure across the world, with both the Eurozone and Japan seeing negative interest

* The figures as at 31 March 2016 and 31 December 2016 include respectively around £14.6m and £14.5m related to the Growing Places Fund (GPF). Devon County Council has agreed to be the local accountable body for the GPF, which has been established by the Department for Communities and Local Government to enable the development of local funds to address infrastructure constraints, promoting economic growth and the delivery of jobs and houses. The Council is working in partnership with the Local Economic Partnership, and interest achieved on the GPF cash, based on the average rate achieved by the Council's investments, will accrue to the GPF and not to the County Council.

rates. Quantitative Easing measures to provide liquidity have been utilised widely and remain in place in the UK, the Eurozone and Japan. The introduction of new regulations requiring banks to hold a higher cash buffer has also had the effect of reducing the rates on offer. Only in the United States have interest rates begun to rise as a result of a strengthening economy.

As a result of this and other global concerns that have impacted on banks, the rates that are now available have fallen further during 2016 from the already low rates previously available in the market.

A rise in the Bank of England Base Rate is thought unlikely during 2017/18, as a result of the uncertainty arising from the decision to leave the European Union and the nature of the UK's future relationship with the EU. The following Table 11 sets out interest rate forecasts over the next year. The forecasts from Capita and Capital Economics reflect the view that the Bank of England base rate is unlikely to increase over the next financial year. The longer-term rates available from the Public Works Loan Board (PWLB) are forecast to increase marginally from the end of 2017.

Table 11 – Base Rate Forecasts and PWLB Rates

	Dec (act) 2016	March 2017	June 2017	Sep 2017	Dec 2017	March 2018
Base Rate						
Capita	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%
Capital Economics	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%

	Dec (act) 2016	March 2017	June 2017	Sep 2017	Dec 2017	March 2018
PWLB Rates						
Capita forecast						
10 Year	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%
25 Year	2.90%	2.90%	2.90%	2.90%	3.00%	3.00%
50 Year	2.70%	2.70%	2.70%	2.70%	2.80%	2.80%

When budgeting for interest payments and receipts a prudent approach has been adopted to ensure that, as far as is possible, both budgets will be achieved.

Borrowing Strategy 2017/18 – 2019/20

The overall aims of the Council's borrowing strategy are to achieve:

- Borrowing at the lowest rates possible in the most appropriate periods;
- The minimum borrowing costs and expenses; and
- A reduction in the average interest rate of the debt portfolio.

Since 2009 the Council has followed a policy of containing the capital programme, taking out no new external borrowing and repaying debt whenever this can be done without incurring a financial penalty. Capital expenditure new starts have been limited to those that were financed from sources other than borrowing.

This strategy has worked well in a period of austerity. The Council's external borrowing level has reduced by £102m to £508m from 2008/09, resulting in reduced Capital Financing Charges.

The strategy was reviewed in 2014, in recognition of the need to invest in capital and the low level of interest rates. The review resulted in a programme of new starts funded by capital receipts but reaffirmed the policy of taking out no new external borrowing. There is no expectation that government funding will deviate from its current downward trajectory. The authority faces significant challenges in balancing its revenue budget in the coming years and it is therefore difficult to imagine how significant additional borrowing could be financed. As a result the Medium Term Financial Strategy (MTFS) continues to assume that, over the three year period, no new long-term borrowing will be required, although this will be kept under review.

The potential to repay further debt, or refinance debt at lower rates, will continue to be closely monitored. The ability of the Council to repay further debt will depend on the cost of repayment and the availability of cash to fund the repayment.

The loans in the Council's current debt portfolio all have maturity dates beyond 2027. Under their current policy the Public Works Loan Board (PWLB) sets premature repayment rates, and where the interest rate payable on a current loan is higher than the repayment rate, the PWLB imposes premium penalties for early repayment. With current low rates of interest this would be a significant cost which would impair the benefit of repayment. Therefore it will only make financial sense to repay debt early if the PWLB changes its current policy, or if interest rates rise and cancel out the repayment premiums. Current interest rate forecasts suggest that it is extremely unlikely that gilt yields will rise sufficiently to cancel out the premiums in the medium term.

It is forecast that as at 31 March 2017 the Council will have cash balances of around £95m. A prudent level of balances is required to meet cashflow. In addition, the cash balances will in part be made up of earmarked reserves and will therefore be committed to meeting Council expenditure. Use of revenue reserves and internal borrowing to fund the capital programme are likely to reduce the cash balance significantly during 2017/18. As a result the availability of cash to repay external debt will be extremely limited.

If short-term borrowing is required to aid cashflow, this will be targeted at an average rate of **0.4%**.

Investment Strategy 2016/17 – 2018/19

The County Council continues to adopt a very prudent approach to counterparties to whom the County Council is willing to lend. As a result only a small number of selected UK banks and building societies, money market funds and Non-Eurozone overseas banks in highly rated countries are being used, subject to strict criteria and the prudent management of deposits with them. In addition the CCLA (Churches, Charities and Local Authorities) Property Fund is being used. The lending policy is kept under constant review with reference to strict criteria for inclusion in the counterparty list.

The Treasury Management Strategy will continue to be set to ensure a prudent and secure approach.

The full County Council is required under the guidance in the CIPFA Treasury Management Code of Practice to approve an Annual Investment Strategy.

The overall aims of the Council's strategy continue to be to:

- Limit the risk to the loss of capital;
- Ensure that funds are always available to meet cash flow requirements;

- Maximise investment returns, consistent with the first two aims; and
- Review new investment instruments as they come to the Local Authority market, and to assess whether they could be a useful part of our investment process.

The overriding objective will be to invest prudently, with priority being given to security and liquidity before yield.

The outlook for cash investment remains challenging. Whereas in the past there has been a perception that Governments would not allow banks to fail, the current regulatory environment has put more emphasis on the requirement for investors to take a hit by funding a "bail-in". A bail-in is where the bank's creditors, including local authorities depositing money with them, bear some of the burden by having part of the debt they are owed written off. The balance of risk has therefore changed, and as a result the Council has considered alternative forms of investment in order to diversify its risk.

A variety of investment instruments are available to the Local Authority market. In addition to the notice accounts and fixed term deposits available from UK and overseas banks, it is also possible for the Council to invest, for example, in UK Government Gilts, bond funds and property funds. These alternative instruments would either require the Council to tie up its cash for significantly longer periods, thus reducing liquidity, or would carry a risk of loss of capital if markets go down.

The Council has considered these alternatives and concluded that investment in a commercial property fund would be a prudent way to diversify risk and achieve a higher yield. UK Gilts and corporate bond funds could still face a challenging environment, whereas the commercial property market stood to benefit from forecast growth in GDP. The CCLA Property Fund is therefore included as an approved counterparty.

However, the majority of the Council's investments will still be in bank deposits. Security is achieved by the creation of an 'Approved List of Counterparties'. These are the banks, building societies, money market funds and other public bodies with whom we are prepared to deposit funds. In preparing the list, a number of criteria will be used not only to determine who is on the list, but also to set limits as to how much money can be placed with them, and how long that money can be placed for.

Banks are expected to have a high credit rating. The Council uses the ratings issued by all three of the major credit rating agencies, Fitch, Moody's and Standard & Poor's, made available to the Council through its external Treasury Advisors. These are monitored daily.

The lowest rating published by any of the agencies is used to decide whether an institution is eligible for inclusion. Where the counterparty is only rated by two of the major ratings agencies the lowest rating published by either of the two is used. This rating also determines the maximum amount which can be loaned to an individual counterparty. Non-Eurozone overseas banks that meet the criteria are included from countries with a high Sovereign rating.

The time length of all deposits with financial institutions will be managed prudently, taking account of the latest advice from the Council's external advisors.

Money Market Funds have a portfolio comprised of short-term (less than one year) securities representing high-quality, liquid debt and monetary instruments. Following the financial crisis these funds were seen as higher risk and were therefore not used by the Council. However, the new regulatory environment around the concept of "bail-in" means that many money market funds are now regarded as a more secure form of investment than bank deposits, as they diversify their investments across a range of financial institutions to spread the risk, and will therefore be used where appropriate. Money market funds must have an 'AAA' rating to be included on the counterparty list.

Other public sector bodies are principally arms of Government, or other local authorities, and although not rated are deemed suitable counterparties because of their inherent low risk.

The 'Approved List of Counterparties' specifies individual institutions, and is formally reviewed at least monthly. Notification of credit rating downgrades (or other market intelligence) is acted upon immediately, resulting in any further lending being suspended.

Table 12 below summarises the current 'Approved List' criteria.

Table 12 – Counterparty Approved List Summary

Counterparty Type		Fitch	Moody's	Standard & Poor's	Credit Limit
UK Banks					
	not below	AA- & F1+	Aa3 & P-1	AA- & A-1+	£50 million
	not below	A- & F1	A3 & P-1	A- & A-1	£30 million
UK Building Societies					
	not below	AA- & F1+	Aa3 & P-1	AA- & A-1+	£50 million
	not below	A- & F1	A3 & P-1	A- & A-1	£30 million
Non-Eurozone Overseas Banks					
	Sovereign Rating of	AAA	Aaa	AAA	
	and not below	AA- & F1+	Aa3 & P-1	AA- & A-1+	£50 million
	and not below	A- & F1	A3 & P-1	A- & A-1	£30 million
UK Public Bodies					
Central Government					
	– Debt Management Office				Unlimited
Local Government					
	– County Councils				£10 million
	– Metropolitan Authorities				£10 million
	– London Boroughs				£10 million
	– English Unitaries				£10 million
	– Scottish Authorities				£10 million
	– English Districts				£5 million
	– Welsh Authorities				£5 million
Fire & Police Authorities					£5 million
Money Market Funds		AAA	Aaa	AAA	£30 million
CCLA Property Fund					£30 million

Where the short term rating of a counterparty is one notch below the stated criteria, but the counterparty meets the long term rating criteria, they may still be used subject to the advice of our external advisors (Capita) who will take into account a range of other metrics in arriving at their advice.

The credit ratings shown in the table for banks and building societies allow for greater sensitivity in recognising counterparty risk. Liquidity in investments is the second key factor in determining our strategy. Funds may be earmarked for specific purposes or may be general balances, and this will be a consideration in determining the period over which the investment will be made.

The counterparty limits shown in the table also apply at a banking group level. This ensures that the Council is not exposed to the risk of having maximum sums invested in multiple institutions owned by a group that encounters financial difficulties.

The Council has a self-imposed limit of ensuring that at least 15% of deposits will be realisable within one month.

A requirement of the Prudential Code is to establish an indicator of the total principal sum invested for a period longer than 364 days, and to state the basis used in determining the amount. The purpose of this indicator is to help the Council to contain its exposure to the possibility of loss that might arise as a result of having to seek early repayment or redemption of principal sums invested.

The limit on investments over 364 days will be set at no more than 20% of the total loans outstanding at any time or £30m whichever is the lower.

For the 2017/18 financial year it has been assumed that the average interest rate earned on lending to banks and building societies will be **0.40%** p.a. and the yield from investment in the CCLA Property Fund will be **4.50%**. The inclusion of overseas counterparties provides additional flexibility, but the rates offered by some banks have reduced over the last year. The target we have set for 2017/18 is thought to be one that is achievable.

Interest rates are forecast to remain low for the foreseeable future. MTFS forecasts have therefore been based on average rates for lending to banks and building societies continuing to be 0.40% for 2018/19 and 2019/20. However these will be reviewed in the light of changes to the rates on offer from the Council's counterparties over the MTFS period.

Performance Targets

The primary targets of the Treasury Management Strategy are to minimise interest payments and maximise interest receipts over the long term whilst achieving annual budgets, without taking undue risk. Where there are comparative statistics available for individual aspects of the Strategy (e.g. the CIPFA Treasury Management Statistics) these will be used to monitor performance.