APPENDIX C

Treasury Management Strategy 2014/15 to 2016/17

For Consideration by Council 26 February 2014

1 INTRODUCTION

1.1 Background

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

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

CIPFA defines treasury management as:

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

1.2 Reporting Requirements

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

Prudential and treasury indicators and treasury strategy (this report):

The first, and most important report covers:

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

A mid year treasury management report:

This will update Members with the progress of the capital position, amending prudential indicators as necessary, and indicating whether treasury activity is meeting objectives or whether any revisions are required. In addition, Cabinet will receive quarterly update reports.

An annual treasury report:

This provides details of various actual prudential and treasury indicators and actual treasury operations compared to the estimates within the approved Strategy.

Scrutiny

This role is undertaken primarily by Budget and Performance Panel. Where time allows, reports will be scrutinised by the Panel prior to consideration by Council. In any event, all reports are considered by Cabinet ahead of referral to Council, thereby facilitating pre-scrutiny to some extent.

1.3 Treasury Management Strategy: Scope

The strategy for 2014/15 covers two main areas:

Capital Issues

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

Treasury Management Issues

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

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

1.4 Training

The CIPFA Code requires the Chief Officer (Resources) to ensure that Members with responsibility for treasury management receive adequate training in treasury management. This especially applies to Members responsibe for scrutiny. The first training session has been arranged for Members on 04 March 2014 (linked to the Budget and Performance Panel meeting) and further training will be arranged as required.

The training needs of treasury management Officers are periodically reviewed.

1.5 Treasury Management Consultants

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

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

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

2 CAPITAL PRUDENTIAL INDICATORS 2014/15 – 2016/17

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in prudential indicators, which aim to provide Members with an overview.

2.1 Capital Expenditure

This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle.

The table below provides that summary, showing how the plans are being financed by capital or revenue resources. Any shortfall of resources results in a borrowing need.

Capital Expenditure	2012/13 Actual £M	2013/14 Estimate £M	2014/15 Estimate £M	2015/16 Estimate £M	2016/17 Estimate £M
General Fund	5.32	17.29	10.17	3.91	4.03
Housing Revenue Account (HRA)	3.59	4.87	4.79	4.93	4.66
Total	**8.91**	**22.16**	**14.96**	**8.84**	**8.69**
Financed by:					
Capital receipts	0.44	8.10	0.99	0.68	0.42
Capital grants	1.01	3.96	2.09	0.99	1.03
Capital reserves	4.45	5.72	5.24	5.08	4.68
Revenue	0.40	0.13	0.46	0.05	0.10
Net financing need for the year	**2.61**	**4.25**	**6.18**	**2.04**	**2.46**

2.2 The Council's Borrowing Need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total amount of capital expenditure (including that from prior years) that has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying need to borrow. Any capital expenditure above, which is not wholly financed in-year, will increase the CFR.

The CFR does not increase indefinitely. This is because the Minimum Revenue Provision (MRP), which is a statutory annual charge to revenue, helps offset any annual increases.

The CFR includes any other long term liabilities (e.g. finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes. The Council currently has £425K of vehicle leases within the CFR.

The Council is asked to approve the following CFR projections:

	2012/13 Actual £M	2013/14 Estimate £M	2014/15 Estimate £M	2015/16 Estimate £M	2016/17 Estimate £M
Capital Financing Requirement					
General Fund	37.57	40.28	45.10	45.65	46.55
HRA	45.51	44.47	43.43	42.39	41.35
Total CFR	**83.08**	**84.75**	**88.53**	**88.04**	**87.90**
Year on Year Movement in CFR	**-0.04**	**1.67**	**3.78**	**-0.49**	**-0.14**

Movement in CFR represented by					
Net financing need for the year (above)	2.60	4.25	6.18	2.04	2.46
Less MRP/VRP and other financing movements	-2.64	-2.57	-2.40	-2.53	-2.60
Movement in CFR	**-0.04**	**1.67**	**3.78**	**-0.49**	**-0.14**

2.3 Minimum Revenue Provision (MRP) Policy Statement

The Council is required to 'pay off' an element of the accumulated General Fund CFR each year through a revenue charge (the minimum revenue provision - MRP), and it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

Government Regulations require Council to approve **an MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision being made. In approving this Strategy, Council approves the following MRP Statement:

For capital expenditure incurred before 01 April 2008 or in subsequent years, MRP will be based on:

- **Asset life method** – MRP will be based on the estimated life of the each asset created as a result of the related capital expenditure, in accordance with the Regulations (this option must also be applied for any expenditure capitalised under a Capitalisation Direction).

This option provides for a reduction in the borrowing need over the approximate life of the asset concerned.

There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made (although there are transitional arrangements in place).

Repayments included in annual finance leases are applied as MRP.

2.4 Core Funds and Expected Investment Balances

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments, unless resources are supplemented each year from new sources (e.g. asset sales). The following table provides estimates of the year end balances for each resource and anticipated day to day cash flow balances. These could vary hugely, however, for example as a result of any successful rating appeals.

Year End Resources	2012/13 Actual £M	2013/14 Estimate £M	2014/15 Estimate £M	2015/16 Estimate £M	2016/17 Estimate £M
Fund balances/reserves	21.42	21.16	21.30	22.02	21.45
Capital receipts	0.11	0.09	0.09	0.12	0.15
Provisions	0.51	0.42	0.42	0.42	0.42
Total Core Funds	**22.04**	**21.67**	**21.81**	**22.56**	**22.02**
Working capital*	3.35	3.35	3.35	3.35	3.35
Under/over borrowing**	-6.59	-8.26	-12.04	-11.55	-11.41
Expected Investments	**18.80**	**16.76**	**13.12**	**14.36**	**13.96**

*Working capital balances shown are estimated year end; these may be higher mid year

2.5 Affordability Prudential Indicators

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

2.6 Ratio of Financing Costs to Net Revenue Stream

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

%	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
General Fund	16%	13%	12%	12%	13%
HRA	24%	23%	22%	22%	21%

The estimates of financing costs include current commitments and the proposals in this budget report.

2.7 Incremental Impact of Capital Investment Decisions on Council Tax

This indicator identifies the revenue costs associated with the five year capital programme recommended in the budget report as compared to the Council's existing approved commitments and current plans. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which are not provided for the same period of time.

Council Tax	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Band D Impact	1.46%	-3.42%	5.64%	1.71%	0.47%

2.8 Estimates of the Incremental Impact of Capital Investment Decisions on Housing Rent Levels

Similar to the council tax calculation, this indicator identifies the trend in the cost the council housing capital programme recommended in this budget report, compared to the Council's existing commitments and current plans, expressed as a discrete impact on weekly rent levels.

£	2012/13 Actual	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate	2016/17 Estimate
Weekly housing rent levels	£0.62	-£1.26	£2.17	£0.67	£0.19

3 BORROWING

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

3.1 Current Portfolio Position

The Council's treasury portfolio position at 31 March 2013 and forward projections are summarised below. The table shows the actual external debt (the treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

	2012/13 Actual £M	2013/14 Estimate £M	2014/15 Estimate £M	2015/16 Estimate £M	2016/17 Estimate £M
External Debt					
Debt at 1 April	76.11	74.58	72.59	76.94	76.63
Expected change in Debt	-0.04	1.67	3.78	-0.49	-0.14
Other long-term liabilities (OLTL)	5.49	0.42	0.24	0.13	0.04
Expected change in OLTL	-5.06	-0.19	-0.11	-0.09	-0.04
Actual gross debt at 31 March	**76.50**	**76.48**	**76.50**	**76.49**	**76.49**
The Capital Financing Requirement	**83.08**	**84.75**	**88.53**	**88.04**	**87.90**
Under- borrowing	**6.58**	**8.27**	**12.03**	**11.55**	**11.41**

Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2014/15 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Chief Officer (Resources) 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 budget report.

3.2 Treasury Indicators: Limits to Borrowing Activity

The Operational Boundary

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

Operational Boundary	2013/14 Estimate £M	2014/15 Estimate £M	2015/16 Estimate £M	2016/17 Estimate £M
Debt	84.11	88.07	88.18	87.78
Other long term liabilities	0.42	0.24	0.13	0.04
Total	**84.53**	**88.31**	**88.31**	**87.82**

The Authorised Limit for External Debt

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

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

Authorised Limit	2013/14 Estimate £M	2014/15 Estimate £M	2015/16 Estimate £M	2016/17 Estimate £M
Debt	101.00	104.00	104.00	104.00
Other long term liabilities	1.00	1.00	1.00	1.00
Total	**102.00**	**105.00**	**105.00**	**105.00**

3.3 Prospects for interest rates

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

Annual Average %	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)		
		5 year	25 year	50 year
Dec 2013	0.50	2.50	4.40	4.40
Mar 2014	0.50	2.50	4.40	4.40
Jun 2014	0.50	2.60	4.50	4.50
Sep 2014	0.50	2.70	4.50	4.50
Dec 2014	0.50	2.70	4.60	4.60
Mar 2015	0.50	2.80	4.60	4.70
Jun 2015	0.50	2.80	4.70	4.80
Sep 2015	0.50	2.90	4.80	4.90
Dec 2015	0.50	3.00	4.90	5.00
Mar 2016	0.50	3.10	5.00	5.10
Jun 2016	0.75	3.20	5.10	5.20
Sep 2016	1.00	3.30	5.10	5.20
Dec 2016	1.00	3.40	5.10	5.20
Mar 2017	1.25	3.40	5.10	5.20

Commentary:

Until 2013, the economic recovery in the UK since 2008 had been the worst and slowest recovery in recent history. However, growth has rebounded during 2013 to surpass all expectations. Growth prospects remain strong for 2014, not only in the UK economy as a whole, but in all three main sectors of services, manufacturing and construction. One downside is that wage inflation continues to remain significantly below CPI inflation so disposable income and living standards are under pressure, although income tax reductions have offset this to some extent. A rebalancing of the economy towards exports has started but as 40% of UK exports go to the Eurozone, the difficulties in this area are likely to continue to dampen UK growth. There are, therefore, concerns that a UK recovery currently based mainly on consumer spending and the housing market, may not continue much beyond 2014. The US, the main world economy, faces similar debt problems to the UK, but with reasonable growth, reductions in government expenditure and tax rises, its annual government deficit has been halved from its peak, without appearing to do too much damage to growth.

The current economic outlook and structure of market interest rates and government debt yields have several key treasury management implications:

- Although Eurozone concerns have subsided in 2013, Eurozone sovereign debt difficulties have not gone away and there are major concerns as to how these will be managed over the next few years as levels of government debt to GDP ratios, in some countries, continue to rise to levels that could result in a loss of investor confidence in the financial viability of such countries. Counterparty risks therefore remain elevated. This continues to suggest the use of higher quality counterparties for shorter time periods.
- Investment returns are likely to remain relatively low during 2014/15 and beyond.
- Borrowing interest rates have risen significantly during 2013 and are on a rising trend. The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring even higher borrowing costs, which are now looming ever closer, where authorities will not be able to avoid new

borrowing to finance new capital expenditure and/or to refinance maturing debt, in the relatively near future.

- There remains a cost of carry to any new borrowing that causes an increase in investments, as this would incur a revenue loss (the difference between higher borrowing costs and lower investment returns).

3.4 Borrowing Strategy

The Chief Officer (Resources), under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time, if need be, taking into account the risks shown in the forecast above. It is likely that shorter term fixed rates may provide lower cost opportunities in the short term.

Borrowing will only be taken on once a liability has been established although the timing of the borrowing may precede the point at which the liability actually falls due for payment. This would only be done to secure a preferential position for the Council, for example to benefit from lower interest rates.

With the likelihood of rates increasing, any debt restructuring is likely to focus on switching from longer term fixed rates to cheaper shorter term debt, although the Chief Officer (Resources) and treasury consultants will monitor prevailing rates for any opportunities during the year. The benefit of this will be balanced against the risks attached to the more frequent refinancing that would be required.

The option of postponing borrowing and running down investment balances will also continue to be considered. This has the added benefit of further reducing counterparty risk and could continue help the revenue budget, with the cost of loans currently far outweighing the return on investments.

3.5 Policy on Borrowing in Advance of Need

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

3.6 Debt Rescheduling

As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

The reasons for any rescheduling to take place will include:

- the generation of cash savings and / or discounted cash flow savings;
- helping to fulfil the treasury strategy;
- enhance the balance of the portfolio (amend the maturity profile and / or the balance of volatility).

Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

All rescheduling will be reported to Cabinet at the earliest meeting following its action.

4 ANNUAL INVESTMENT STRATEGY

4.1 Investment Policy

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

In accordance with the above, and in order to minimise the risk to investments, the Council clearly stipulates (as set out below) the minimum acceptable credit quality of counterparties for inclusion on the lending list. The creditworthiness methodology used to create the counterparty list fully accounts for the ratings, watches and outlooks published by all three ratings agencies. Using our advisor's ratings service, potential counterparty ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications.

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

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

The aim of the strategy is to generate a list of highly creditworthy counterparties, which will also enable diversification and thus avoidance of concentrated risk.

The intention of the strategy is to provide security of investment and minimisation of risk.

Investment instruments identified for use in the financial year are listed in ***Annex B*** under the 'specified' and 'non-specified' investments categories.

4.2 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 that:

- 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; and
- 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.

The Chief Officer (Resources), as s151 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. These criteria are separate to those that determine which types of investment instrument are either specified or non-specified. The following criteria provide an overall pool of counterparties considered high quality that the Council may use, rather than defining what types of investment instruments are to be used.

The minimum rating criteria use the lowest common denominator method of selecting counterparties and applying limits. This means that the application of the Council's minimum criteria will apply to the lowest available rating for any institution. For instance, if an institution is rated by two agencies, one meets the Council's criteria, the other does not, the institution will fall outside the lending criteria. Credit rating information is supplied by Capita Asset Services 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. For instance, a negative rating watch applying to a counterparty at the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions.

The criteria for providing a pool of high quality investment counterparties (both specified and non-specified investments) are:

Banks 1 - Good Credit Quality

The Council will only use banks that:

- are UK banks; or
- are non-UK but are domiciled in an EU country with a long term sovereignty rating of AAA,

and have, as a minimum, the following Fitch, Moody's and Standard and Poors credit ratings (where rated, as is consistent with the middle limit as per table 3):

i. Short Term: F1/P-1/A-1

ii. Long Term: A/A2/A

iii. Individual Viability / Financial Strength: bb+/C (Fitch / Moody's only)

iv. Support: 3 (Fitch only)

Banks 2 – Part nationalised UK banks
Lloyds Bank and Royal Bank of Scotland. These banks can be included if they continue to be part nationalised or if they meet the ratings in Banks 1 above.

Banks 3 – The Council's own Banker
The bank may be used 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.

Building Societies – all Societies that meet the ratings for banks outlined above.

Money Market Funds – AAA-rated sterling funds with constant unit value.

UK Government – Debt Management Account Deposit Facility (DMADF)

Local Authorities (including Police and Fire Authorities), Parish Councils

Supranational institutions (e.g. European Central Bank)

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 25% will be placed with any one non-UK country at any time;
- limits in place above will apply to Group companies (e.g. Natwest and RBS count as a single counterparty);
- Capita Asset Services' limits will be monitored.

Use of Additional Information other than Credit Ratings

Additional requirements under the Code require 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, negative rating watches/outlooks) will be applied to compare the relative security of differing investment counterparties.

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):

	Minimum across all three ratings			Money Limit[8]	Time Limiit[9]
	Fitch	**Moody's**	**Standard & Poors**		
Upper Limit[1]	**F1+/AA-**	**P-1/AA3**	**A-1+/AA-**	**£6M**	**Instant access only**
				£6M	**364 days**
Middle Limit[2]	**F1/A**	**P-1/A2**	**A-1/A**	**£3M**	**Instant access only**
Other Institutions[3]	**N/A**	**N/A**	**N/A**	**£6M**	**364 days**
Lancashire County Council[4]	**N/A**	**N/A**	**N/A**	**£12M**	**364 days**
Money Market Funds[5]	**AAA**	**AAA**	**AAA**	**£6M**	**Instant Access Only**
DMADF deposit[6]	**N/A**	**N/A**	**N/A**	**No limit**	**364 days**
Sovereign rating to apply to all non UK counterparties[7]	**AAA**	**AAA**	**AAA**	**N/A**	**N/A**

Notes:

1 & 2: The Upper and Middle Limits apply to appropriately rated banks and building societies.
3: The Other Institutions limit applies to other local authorities and supranational institutions (e.g. European Central Bank), and part-nationalised banks.
4: This recognises the special status of Lancashire County Council as the City Council's upper tier authority.
5: Sterling, constant net asset value funds only.
6: The DMADF facility is direct with the UK government; it is extremely low risk.
7: UK counterparties are defined as those listed under UK banks or building societies in the Capita Asset Services counterparty listing.
8: Money limits apply to principal invested and do not include accrued interest.
9: Time Limits start on the trade date for the investment.

4.3 Investment Strategy

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

Investment returns expectations: The Bank Rate is forecast to remain unchanged at 0.5% before starting to rise from Quarter 2 of 2016. Bank Rate forecasts for financial year ends (March) are:

2013/14	0.50%
2014/15	0.50%
2015/16	0.50%
2016/17	1.25%

There are upside risks to these forecasts (i.e. start of increases in Bank Rate occurs sooner) if economic growth remains strong and unemployment falls faster than expected. However, should the pace of growth fall back, there could be downside risk, particularly if the Bank of England inflation forecasts / the rate of fall of unemployment were to prove too optimistic.

The assumed investment rates for investments placed for periods up to 100 days during each financial year for the next four years are as follows:

2014/15	0.50%
2015/16	0.50%
2016/17	0.69%
2017/18	2.00%

4.4 Icelandic Bank Investments

Officers will continue to report to Cabinet on the outstanding claim balances (Glitnir escrow account, and KSF). Alternative methods for recuperating the outstanding claims, such as a sale of claim to a third party, will be considered and as required.

4.5 End of Year Investment Report

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

ANNEX A

Treasury Management Glossary of Terms

- **Annuity** – method of repaying a loan where the payment amount remains uniform throughout the life of the loan, therefore the split varies such that the proportion of the payment relating to the principal increases as the amount of interest decreases.

- **CIPFA** – the Chartered Institute of Public Finance and Accountancy, is the professional body for accountants working in Local Government and other public sector organisations, also the standard setting organisation for Local Government Finance.

- **Call account** – instant access deposit account.

- **Counterparty** – an institution (e.g. a bank) with whom a borrowing or investment transaction is made.

- **Credit Rating** – is an opinion on the credit-worthiness of an institution, based on judgements about the future status of that institution. It is based on any information available regarding the institution: published results, Shareholders' reports, reports from trading partners, and also an analysis of the environment in which the institution operates (e.g. its home economy, and its market sector). The main rating agencies are Fitch, Standard and Poor's, and Moody's. They analyse credit worthiness under four headings:

    - **Short Term Rating** – the perceived ability of the organisation to meet its obligations in the short term, this will be based on measures of liquidity.

    - **Long Term Rating** – the ability of the organisation to repay its debts in the long term, based on opinions regarding future stability, e.g. its exposure to 'risky' markets.

    - **Individual/Financial Strength Rating** – a measure of an institution's soundness on a stand-alone basis based on its structure, past performance and credit profile.

    - **Legal Support Rating** – a view of the likelihood, in the case of a financial institution failing, that its obligations would be met, in whole or part, by its shareholders, central bank, or national government.

  The rating agencies constantly monitor information received regarding financial institutions, and will amend the credit ratings assigned as necessary.

- **DMADF and the DMO –** The DMADF is the 'Debt Management Account Deposit Facility'; this is highly secure fixed term deposit account with the Debt Management Office (DMO), part of Her Majesty's Treasury.

- **EIP –** Equal Instalments of Principal, a type of loan where each payment includes an equal amount in respect of loan principal, therefore the interest due with each payment reduces as the principal is eroded, and so the total amount reduces with each instalment.

- **Gilts** – the name given to bonds issued by the U K Government. Gilts are issued bearing interest at a specified rate, however they are then traded on the markets like shares and their value rises or falls accordingly. The Yield on a gilt is the interest paid divided by the Market Value of that gilt.

E.g. a 30 year gilt is issued in 1994 at £1, bearing interest of 8%. In 1999 the market value of the gilt is £1.45. The yield on that gilt is calculated as 8%/1.45 = 5.5%.
See also PWLB.

- **LIBID** – The London Inter-Bank Bid Rate, the rate which banks would have to bid to borrow funds from other banks for a given period. The official rate is published by the Bank of England at 11am each day based on trades up to that time.

- **LIBOR** – The London Inter-Bank Offer Rate, the rate at which banks with surplus funds are offering to lend them to other banks, again published at 11am each day.

- **Liquidity** – Relates to the amount of readily available or short term investment money which can be used for either day to day or unforeseen expenses. For example Call Accounts allow instant daily access to invested funds.

- **Maturity** – Type of loan where only payments of interest are made during the life of the loan, with the total amount of principal falling due at the end of the loan period.

- **Money Market Fund (MMF)** – Type of investment where the Council purchases a share of a cash fund that makes short term deposits with a broad range of high quality counterparties. These are highly regulated in terms of average length of deposit and counterparty quality, to ensure AAA rated status.

- **Policy and Strategy Documents** – documents required by the CIPFA Code of Practice on Treasury Management in Local Authorities. These set out the framework for treasury management operations during the year.

- **Public Works Loans Board (PWLB)** – a central government agency providing long and short term loans to Local Authorities. Rates are set daily at a margin over the Gilt yield (see Gilts above). Loans may be taken at fixed or variable rates and as Annuity, Maturity, or EIP loans (see separate definitions) over periods of up to fifty years. Financing is also available from the money markets, however because of its nature the PWLB is generally able to offer better terms.

- **Sector** – Sector are the City Council's Treasury Management advisors. They provide advice on borrowing strategy, investment strategy, and vetting of investment counterparties, in addition to ad hoc guidance throughout the year.

- **Yield** – see Gilts

Members may also wish to make reference to *The Councillor's Guide to Local Government Finance.*

ANNEX B

Definitions of Specified and Non Specified Investments

See the detailed Investment Strategy included in ***Appendix C***, for the limits to be applied.

1. Specified Investments are defined as follows.

Specified Investments These are to be sterling investments of a maturity period of not more than 364 days, or those which could be for a longer period but where the Council has the right to be repaid within 364 days if it wishes. These are low risk assets where the possibility of loss of principal or investment income is considered negligible. These include investments with: (i) The UK Government (such as the Debt Management Office, UK Treasury Bills or a Gilt with less than one year to maturity). (ii Supranational bonds of less than one year's duration. (iii) A local authority, parish council or community council. (iv) An investment scheme that has been awarded a high credit rating by a credit rating agency. (v) A body with high credit quality (such as a bank or building society). For category (iv) this covers a money market fund AAA rated by Standard and Poor's, Moody's or Fitch rating agencies.

2. Non-specified Investments are defined as follows:

   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 are set out below. Non specified investments not explicitly referred to below are excluded.

Ref	Non Specified Investment Category	Limit
(i)	A body which has been provided with a government issued guarantee for wholesale deposits within specific timeframes. Where these guarantees are in place and the government has an AAA sovereign long term rating these institutions will be included within the Council's criteria temporarily until such time as the ratings improve or the guarantees are withdrawn. Monies will only be deposited within the timeframe of the guarantee.	Included as per section 4.2
(ii)	Lloyds Bank and Royal Bank of Scotland. These banks can be included if they continue to be part nationalised.	Included as per section 4.2
(iii)	The Council's own banker if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as is possible.	Included as per section 4.2

ANNEX C

Background information on credit ratings

Credit ratings are an important part of the Authority's investment strategy. The information below summarises some of the key features of credit ratings and why they are important.

What is a Credit Rating?
A credit rating is:

- An independent assessment of an organisation;
- It gauges the likelihood of getting money back on the terms it was invested;
- It is a statement of opinion, not statement of fact;
- They help to measure the risk associated with investing with a counterparty;

Who Provides / Uses Credit Ratings?
There are three main ratings agencies, all of which are used in the Authority's treasury strategy.

- Fitch
- Moody's Investor Services
- Standard & Poors

The ratings supplied by these agencies are used by a broad range of institutions to help with investment decisions, these include:

- Local Authorities;
- Other non-financial institutional investors;
- Financial institutions;
- Regulators;
- Central Banks;

Rating Criteria
There are many different types of rating supplied by the agencies. The key ones used by the Authority are ratings to indicate the likelihood of getting money back on terms invested. These can be split into two main categories:

- 'Short Term' ratings for time horizons of 12 months or less. These may be considered as the most important for local authorities.

- 'Long Term' ratings for time horizons of over 12 months. These may be considered as less important in the current climate.

In addition, the agencies issue sovereign, individual and support ratings which will also feed into the investment strategy.

Rating Scales (Fitch, Moody's and Standard & Poors)
The table below shows how some of the higher graded short and long term ratings compare across the agencies; the top line represents the highest grade possible. (There are other ratings that go much lower than those shown below, and ratings for other elements).

Short Term			**Long Term**		
Fitch	Moody's	S&P	Fitch	Moody's	S&P
F1+	P-1	A-1+	AAA	Aaa	AAA
F1	P-1	A-1	AA	Aa2	AA
F2	P-2	A-2	A	A2	A