

London Borough of Barnet

Treasury Management Strategy Statement

Minimum Revenue Provision Policy Statement and Annual Investment Strategy

2019/20

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1 INTRODUCTION

1.1 Background

The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this 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 security and 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, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

CIPFA defines treasury management as:

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

Revised reporting is required for the 2019/20 reporting cycle due to revisions of the MHCLG Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a capital strategy, to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011. The capital strategy is being reported separately.

This authority has not engaged in any commercial investments and has no non-treasury investments. However, the Council has entered into lending activity to support its priorities and the borrowing required to support this lending activity is included within this statement.

1.2 Reporting requirements

1.2.1 Capital Strategy

The CIPFA revised 2017 Prudential and Treasury Management Codes require, for 2019-20, all local authorities to prepare an additional report, a capital strategy report, which will provide the following:

- a high-level long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services

- an overview of how the associated risk is managed
- the implications for future financial sustainability

The aim of this capital strategy is to ensure that all elected members on the full council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

1.2.2 Treasury Management Reporting

The Council is currently required to receive and approve, as a minimum, three main treasury 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 is forward looking and covers:

- the capital plans (including prudential indicators);
- a 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 by which 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 whether any policies require revision.

An annual treasury report – This provides details of actual prudential and treasury indicators and treasury operations compared to the estimates within the strategy.

Scrutiny

The above reports are required to be adequately scrutinised before being recommended to the Council. The Performance and Contract Monitoring Committee and Policy and Resources Committee undertake this role.

1.3 Treasury Management Strategy for 2019/20

The strategy for 2019/20 covers two main areas:

Capital issues

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

Treasury management issues

- * the current treasury position;
- * treasury indicators which 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
- * the 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 MHCLG Investment Guidance

1.4 Training

The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. Training was provided to members of the Policy and Resources Committee on 23 October 2018. 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 Link 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 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.

1.6 Purpose

The purpose of this Treasury Management Strategy Statement is to seek approval for:

- Treasury Management Strategy for 2019/20;
- Annual Investment Strategy for 2019/20;
- Prudential Indicators for, 2019/20 to 2021/22;
- MRP statement (see Appendix para 5.1.1).

1.7 Recommendations

The main recommended revisions to the Treasury Management Strategy are:

- New external borrowing in 2018-19 has all been short-term. With interest rates of all durations expected to increase, short-term loans will be switched into longer maturities in 2019-20.

1.8 Changes between 2018-19 and 2019-20 TMSS

The Treasury Management Strategy has been updated as follows:

- The prudential indicators have been updated to reflect the Council's capital programme and future borrowing requirement; and
- The strategy has been updated to reflect the latest forecast for interest rates. Bank rate is expected to remain at 0.75% until quarter 2, 2019.
- The use of Money Market Funds as specified investments has been expanded to include LVNAV funds (see appendix 5.3).

- The mid-year change made in 2018-19 to include “loans to organisations delivering community benefits” within permitted non-specified investments is also reflected in the 2019-20 strategy.
- Permitted non-specified investments also include a new category for loans to TBG Open Door Limited.
- Capital expenditure include the proposed loans to TBG Open Door Homes Limited and Saracens Rugby Club.

1.9 Additional external Borrowing

It is anticipated that external borrowing to finance the 2019-20 and later capital programmes and lending activity will be required to taken in early to mid 2019.

1.10 Investment Policy and Instruments

The proposed criteria for specified and non-specified investments are shown in section 5.3. Further diversification of financial instruments into more secure / higher yield asset classes will be made in consultation with the Council’s investment advisor.

2 THE CAPITAL PRUDENTIAL INDICATORS 2019/20 – 2021/22

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

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. Members are asked to approve the capital expenditure forecasts:

Capital expenditure £'000	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Non-HRA	115,514	262,413	275,563	61,639	62,526
HRA	49,378	33,564	78,143	19,589	18,049
Total	164,892	295,977	353,706	81,228	80,575

Other long-term liabilities. The above financing need excludes other long-term liabilities, such as PFI and leasing arrangements, which already include borrowing instruments.

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding need.

Financing of capital expenditure £'000	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Capital receipts	32,706	25,534	60,020	467	0
Capital grants	60,886	85,248	57,956	1,190	0
Capital reserves	7,598	28,977	20,837	2,602	1,250
Revenue	29,258	25,894	26,404	19,589	18,049
Total Financing	130,448	165,653	165,217	23,848	19,299
Net capital financing need for the year	34,444	130,324	188,489	57,380	61,276

The value of capital expenditure included planned loans to TBG Open Door Homes and Saracens Rugby club.

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 historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and its underlying borrowing need. Any capital expenditure above, which has not been paid for, will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge that broadly reduces the indebtedness in line with each assets life, and so charges the economic consumption of capital assets as they are used.

The CFR includes any other long-term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility by the PFI, PPP lease provider and so the Council is not required to separately borrow for these schemes. The Council currently has £16.0m of such schemes within the CFR.

The Council is asked to approve the CFR projections below:

£'000	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Capital Financing Requirement					
CFR – non-housing	258,532	370,846	510,861	555,178	603,560
CFR – housing	200,634	207,961	243,982	243,982	243,982
Total CFR	459,166	578,807	754,843	799,160	847,542
Movement in CFR	23,515	119,641	176,036	44,317	48,382

Movement in CFR represented by					
Net financing need for the year (above)	34,444	130,324	188,489	57,380	61,276
Less MRP and other financing movements	-10,929	-10,683	-12,453	-13,063	-12,894
Movement in CFR	23,515	119,641	176,036	44,317	48,382

3 BORROWING

The capital expenditure plans set out in Section 2 provide details of the capital activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet the Council's capital strategy and day-to-day transactional needs. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate 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 overall treasury management portfolio as at 31 March 2018 and at 31 December 2018 are shown below for both borrowing and investments.

	Investments and Borrowing			
	31.3.2018		31.12.2018	
	£'000	%	£'000	%
Treasury Investments				
Money Market Funds	47,100	49.3%	23,600	61.1%
Local Authorities	23,000	24.1%	5,000	13.0%
Banks UK	20,400	21.4%	10,000	25.9%
Banks Overseas	5,000	5.2%	0	0.0%
Total treasury investments	<u>95,500</u>	<u>100.0%</u>	<u>38,600</u>	<u>100.0%</u>
Borrowing				
PWLB	241,580	79.4%	241,580	71.2%
Bank borrowing - LOBO's	<u>62,500</u>	20.6%	<u>62,500</u>	18.4%
Total long-term debt	<u>304,080</u>		<u>304,080</u>	
Short-term local authority debt	0	0.0%	35,000	10.3%
Total Treasury Borrowing	<u>304,080</u>	<u>100.0%</u>	<u>339,080</u>	<u>100.0%</u>
Net Treasury Investments / (Borrowing)	-208,580		-300,480	
Other long-term liabilities	-15,974		-15,974	
Net Investments / (borrowing)	<u>-224,554</u>		<u>-316,454</u>	

The Council's forward projections for borrowing are summarised below. The table shows the actual external debt against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

£'000	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
External Debt					
Debt at 1 April	304,080	304,080	361,521	537,857	582,474
Expected change in Debt	0	57,441	176,336	44,617	48,682
Other long-term liabilities (OLTL)	16,402	15,974	15,601	15,228	14,855
Expected change in OLTL	-428	-373	-373	-373	-373
Actual gross debt at 31 March	320,054	377,122	553,085	597,329	645,638
The Capital Financing Requirement	459,166	578,807	754,843	799,160	847,542
Under / (over) borrowing	139,112	201,685	201,758	201,831	201,904

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 2019/20 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 or speculative purposes.

The Chief Finance Officer reports that the Council complied with this prudential indicator in the current year. Previously we have reported that no difficulties were expected with this indicator in future year. However, the growth in loans will need monitoring to ensure that borrowing does not exceed the CFR. This view takes into account current commitments, existing plans, and the proposals in this 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 and the ability to fund under-borrowing by other cash resources. The limits below are based on projected CFR with a reduction of £100 million to reflect retained reserves.

Operational boundary £'000	2018/19 Projected Actuals	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Debt	361,521	639,242	683,932	732,687
Other long-term liabilities	15,974	15,601	15,228	14,855
Total	377,495	654,843	699,160	747,542

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 that, while not desired, could be afforded in the short term, but may not be sustainable in the longer term.

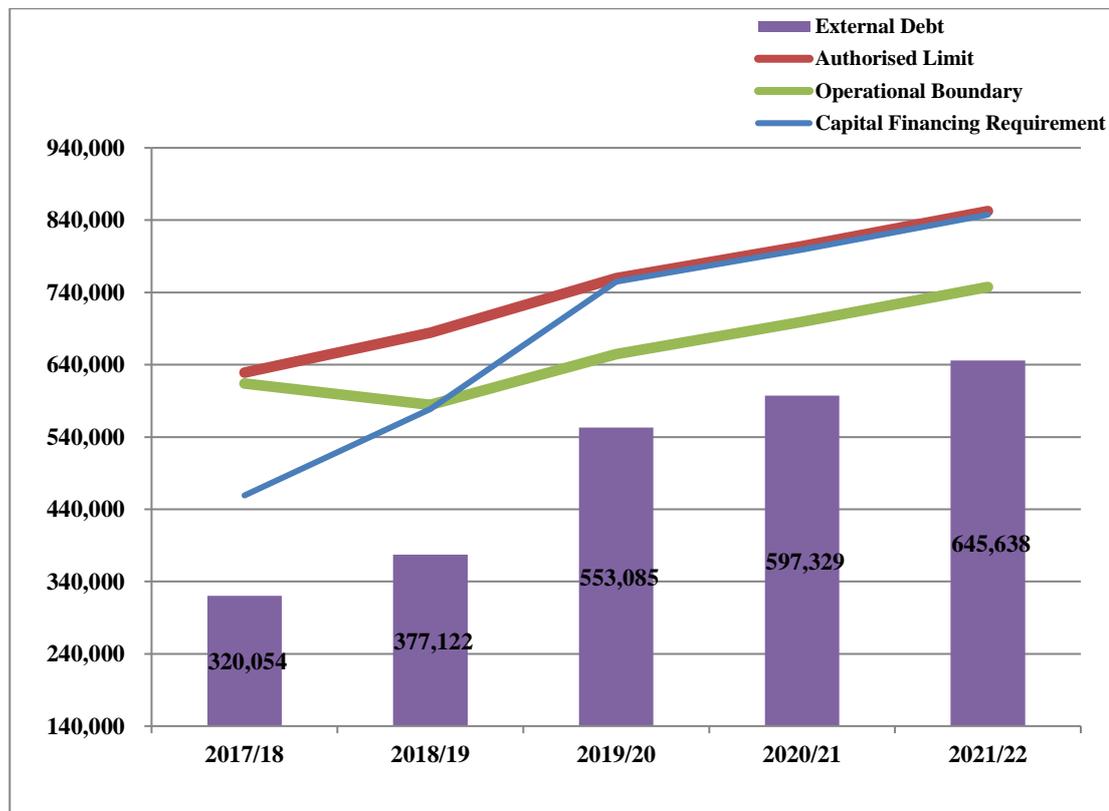
1. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.
2. The Council is asked to approve the following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

Authorised limit £'000	2018/19 Projected Actuals	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Debt	361,521	739,242	783,932	832,687
Other long-term liabilities	15,974	20,601	20,228	19,855
Total	377,495	759,843	804,160	852,542

Until recently (October 2018), the Council was limited to a maximum HRA CFR through the HRA self-financing regime. This limit was £240.043 million. HRA has replaced this limit in their business plan with a voluntary limit of £350 million.

HRA Debt Limit £'000	2018/19 Projected Actuals	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
HRA debt cap	240,043	350,000	350,000	350,000
HRA CFR	210,031	244,616	244,616	244,616
HRA headroom	30,012	105,384	105,384	105,384

The graph below illustrates the capital and borrowing position over the TMSS period. The authorised and operational limits reflect an expectation that capital expenditure levels will be below these envisaged in the plans above.



3.3 Prospects for interest rates

The Council has appointed Link Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The table in appendix 5.2 provides Link’s central view.

The flow of generally positive economic statistics after the quarter ended 30 June meant that it came as no surprise that the MPC came to a decision on 2 August to make the first increase in Bank Rate above 0.5% since the financial crash, from 0.5% to 0.75%. Growth became increasingly strong during 2018 until slowing significantly during the last quarter. At their November quarterly Inflation Report meeting, the MPC left Bank Rate unchanged, but expressed some concern at the Chancellor’s fiscal stimulus in his Budget, which could increase inflationary pressures. However, it is unlikely that the MPC would increase Bank Rate in February 2019, ahead of the deadline in March for Brexit. On a major assumption that Parliament and the EU agree a Brexit deal in the first quarter of 2019, then the next increase in Bank Rate is forecast to be in May 2019, followed by increases in February and November 2020, before ending up at 2.0% in February 2022.

The overall longer run future trend is for gilt yields, and consequently PWLB rates, to rise, albeit gently. However, over about the last 25 years, we have been through a period of falling bond yields as inflation subsided to, and then stabilised at, much lower levels than before, and supported by central banks implementing substantial quantitative easing purchases of government and other debt after the financial crash of 2008. Quantitative easing, conversely, also caused a rise in equity values as investors searched for higher returns and purchased riskier assets. In 2016, we saw

the start of a reversal of this trend with a sharp rise in bond yields after the US Presidential election in November 2016, with yields then rising further as a result of the big increase in the US government deficit aimed at stimulating even stronger economic growth. That policy change also created concerns around a significant rise in inflationary pressures in an economy which was already running at remarkably low levels of unemployment. Unsurprisingly, the Fed has continued on its series of robust responses to combat its perception of rising inflationary pressures by repeatedly increasing the Fed rate to reach 2.25 – 2.50% in December 2018. It has also continued its policy of not fully reinvesting proceeds from bonds that it holds as a result of quantitative easing, when they mature. We therefore saw US 10-year bond Treasury yields rise above 3.2% during October 2018 and investors causing a sharp fall in equity prices as they sold out of holding riskier assets. However, by early January 2019, US 10-year bond yields had fallen back considerably on fears that the Fed was being too aggressive in raising interest rates and was going to cause a recession. Equity prices have been very volatile on alternating good and bad news during this period.

From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and sharp changes in investor sentiment. Such volatility could occur at any time during the forecast period.

Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The above forecasts, (and MPC decisions), will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

Investment and borrowing rates

- Investment returns are likely to remain low during 2019/20 but to be on a gently rising trend over the next few years.
- Borrowing interest rates have been volatile so far in 2018-19 and while they were on a rising trend during the first half of the year, they have backtracked since then until early January. 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 higher borrowing costs in the future when authorities may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt;

There will remain a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.

3.4 Borrowing strategy

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

A key determinant of the timing of borrowing is certainty over the scale and timing of the capital programme. Without this certainty, there is a reluctance to enter into long-term borrowing.

Against this background and the risks within the economic forecast, caution will be adopted with the 2019/20 treasury operations. The Chief Finance Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- if it was felt that there was a significant risk of a sharp FALL in long and short-term rates (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- if it was felt that there was a significant risk of a much sharper RISE in long and short-term rates than that currently forecast, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

Any decisions will be reported to the Financial Performance and Contracts Committee at the next available opportunity.

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. The above policy permits forward funding of capital expenditure provided that current debt is below CFR (and within approved limits) i.e. reserves and working capital are mitigating borrowing requirements. Any advance funding will not exceed more than 12 months capital expenditure plans.

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

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) together with the life of assets in the capital programme and the expected cost to refinance short term borrowing in future years.

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).

Current expectations are that interest rates, both short and long term will gradually increase. Cash balances have been reduced to levels consistent with maintaining liquidity and are supported by short-term borrowing. The immediate focus is on when to switch borrowing into longer term debt to lock in rates that remain remarkably low in the longer-term context.

The Council has Lender Option Borrower Option debt of £62.5 million due to mature between 2054 and 2076. These loans carry the right of the lenders to change the interest rates and of the Council to repay without cost. The current intention is that should a change in interest rate be proposed, that the Council will exercise the option to repay.

All rescheduling will be reported to the Financial Performance and Contracts Committee at the earliest meeting following its action.

3.7 Sources of New Borrowing

The benchmark for appraising borrowing opportunities will remain the PWLB due to its transparent pricing, flexibility of terms (available maturities, fixed and variable interest rates and repayment profiles), the speed of funding, the absence of complex documentation and the known cost of early repayment. PWLB rates are offered at a fixed margin over Government gilt yields. Other borrowing avenues that may offer advantages over the PWLB are possible. The main advantage is the opportunity for lower interest rates, but others include forward pricing of loans and inflation linked interest rates. Potential lenders include institutions (via bond issues), insurance companies and the Municipal Bond Agency. When considering borrowing alternatives, all factors including price, contractual terms, flexibility etc, will be evaluated.

4 ANNUAL INVESTMENT STRATEGY

4.1 Investment policy

The Council's investment policy has regard to the following: -

- MHCLG's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the Code")
- CIPFA Treasury Management Guidance Notes 2018

The Council's investment priorities will be security first, portfolio liquidity second and then yield, (return).

In accordance with the above guidance from the MHCLG 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 that also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the Short Term and Long-Term ratings.

Ratings will not be the sole determinant of the quality of an institution; 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 achieve this consideration the Council will engage with its advisors to monitor 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.

Investment instruments identified for use in the financial year are listed in appendix 5.3 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 appendix 5.3; 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 Finance Officer will maintain a counterparty list in compliance with the criteria in appendix 5.3 and will revise the criteria and submit them to Council for approval as necessary.

Credit rating information is supplied by Link Asset Services, our treasury advisors, on all active counterparties. 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 the longer-term bias outside the central rating view) are considered before dealing. For instance, a negative rating

Watch applying to counterparty at the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions.

A limit of £100 million will be applied to the use of non-specified investments as described in appendix 5.3.

Use of additional information other than credit ratings. Additional requirements under the Code require the Council to supplement credit rating information. Whilst the selection of counterparties relies primarily on the application of credit ratings 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 and the proposed criteria for specified and non-specified investments are shown in Appendix 5.3 for approval.

4.3 Country and sector limits

Due care will be taken to consider the country, group and sector exposure of the Council's investments.

The Council has determined that it will only use approved counterparties from the United Kingdom or countries with a minimum sovereign credit rating of AA from Fitch (or equivalent). This minimum rating does not apply to the United Kingdom. The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 5.4. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

In addition:

- no more than £40 million 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.

4.4 Investment strategy

Investment returns expectations.

Bank Rate is forecast to stay flat at 0.75% until quarter 2 2019 and then to gradually increase to 2.00% by quarter 1 2022. Bank Rate forecasts for financial year ends (March) are:

- 2018/19 0.75%
- 2019/20 1.25%
- 2020/21 1.50%
- 2021/22 2.00%

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

2019/20	1.00%
2020/21	1.50%
2021/21	1.75%

The overall balance of risks to economic growth in the UK is probably neutral. The balance of risks to increases in Bank Rate and shorter term PWLB rates, are probably

also even and are dependent on how strong GDP growth turns out, how slowly inflation pressures subside, and how quickly the Brexit negotiations move forward positively.

Investment treasury indicator and limit - total principal funds invested for greater than 365 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.

The Council is asked to approve the treasury indicator and limit:

Maximum principal sums invested > 364 & 365 days			
£m	2019/20	2020/21	2021/22
Principal sums invested > 364 & 365 days	£25 million	£25 million	£25 million

For its cash flow generated balances, the Council will seek to utilise money market funds and short-dated deposits (overnight to 100 days) in order to benefit from the compounding of interest.

4.5 Investment risk benchmarking

The Council will use an investment benchmark to assess the investment performance of its investment portfolio of 7-day LIBID.

4.6 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.

4.7 Icelandic bank investments

The Council has no Icelandic bank investments.

5 APPENDICES

1. Prudential and treasury indicators and MRP statement
2. Interest rate forecasts
3. Treasury management practice 1 – credit and counterparty risk management
4. Approved countries for investments
5. Treasury management scheme of delegation
6. The treasury management role of the section 151 officer

5.1 THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2019/20 – 2021/22 AND MRP STATEMENT

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

5.1.1 Minimum revenue provision (MRP) policy statement

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

MHCLG 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 a prudent provision. The Council is recommended to approve the following MRP Statement:

For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will be:

Regulatory Method / Existing practice

MRP will follow the existing practice outlined in former CLG regulations (option 1);

These options provide for an approximate 4% reduction in the borrowing need (CFR) each year.

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

Asset life method – MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) (option 3);

These options provide for a reduction in the borrowing need over approximately the asset's life.

The Council may consider using an MRP holiday if required to match future cashflow arising from capital schemes.

Repayments included in annual PFI or finance leases are applied as MRP.

HRA

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).

The Council has not made voluntary revenue provisions.

Loan to Open Door

The Council has established a company to which it will be providing loans on a commercial basis. The cash advances will be used by the company to fund capital expenditure and should therefore be treated as capital expenditure and a loan to a third party. The Capital Financing Requirement (CFR) will increase by the amount of loans advanced and under the terms of contractual loan agreements are due to be returned in full by 2040, with interest paid. Once funds are returned to the Authority, the returned funds are classed as a capital receipt and are offset against the CFR, which will reduce accordingly. As the funds will be returned in full, there is no need to

set aside prudent provision to repay the debt liability in the interim period, so there is no MRP application.

The outstanding loan/CFR position will be reviewed on an annual basis and if the likelihood of default increases, a prudent MRP policy will commence.

5.1.2 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. The Council is asked to approve the following indicators:

a. 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.

%	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Non-HRA	4.54%	5.16%	6.40%	7.78%	8.06%
HRA	11.77%	12.82%	13.83%	14.41%	14.10%

Both ratios, in particular Non-HRA, increase substantially reflecting the scale of the capital programme and the lending activity outline in section 2.1 of the statement.

b. HRA ratios

£	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
HRA debt £'000	199,501	206,828	242,849	242,849	242,849
HRA debt cap	240,043	240,043	350,000	350,000	350,000
HRA revenues £'000	60,677	58,216	57,665	60,163	61,484
Multiple of debt to revenues	3.3	3.6	4.2	4.0	3.9

£	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
HRA debt £'000	199,501	206,828	242,849	242,849	242,849
Number of HRA dwellings	9,745	9,483	9,387	9,130	8,681
Debt per dwelling £	20,472	21,810	25,871	26,599	27,975

5.1.4 Treasury indicators for debt

There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any 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 and covers a maximum limit on fixed interest rates;
- Maturity structure 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.

The Council is asked to approve the following treasury indicators and limits:

£m	2019/20	2020/21	2021/22
Interest rate exposures			
	Upper	Upper	Upper
Limits on fixed interest rates based on net debt	100%	100%	100%
Limits on variable interest rates based on net debt	40%	40%	40%
30%			
	Current	Lower	Upper
Under 12 months	29%	0%	50%
12 months to 2 years	0%	0%	50%
2 years to 5 years	0%	0%	75%
5 years to 10 years	7%	0%	75%
10 years to 25 years	52%	0%	75%
25 years to 50 years	12%	0%	100%
Maturity structure of variable interest rate borrowing 2019/20			
	Lower	Upper	
Under 12 months	0%	50%	
12 months to 2 years	0%	50%	
2 years to 5 years	0%	75%	
5 years to 10 years	0%	75%	
10 years to 25 years	0%	75%	
25 years to 50 years	0%	100%	

The above table is based on those loans with borrower options (LOBO's) being treated as repayable at the next date the lender can alter the interest rate (and the Council can opt to repay). If these loans were shown as maturing at the contractual maturity date, the proportion maturing within 12 months would be 10% and the proportion over 25 years would be 30%. Currently the prevailing and forecast rate of interest on new debt is lower than the existing LOBO loans making any interest calls unlikely.

The variable limit has been increased from 30% to 40% to reflect the classification of LOBO loans as variable. Currently, LOBO loans and short-term borrowing represents 29% of debt balances.

5.2 INTEREST RATE FORECASTS 2019 – 2022

Link Asset Services Interest Rate View													
	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%	1.50%	1.75%	1.75%	1.75%	2.00%
3 Month LIBID	0.90%	1.00%	1.10%	1.20%	1.30%	1.40%	1.50%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%
6 Month LIBID	1.00%	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%
12 Month LIBID	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%	2.30%	2.40%
5yr PWLB Rate	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%	2.60%	2.60%	2.70%	2.80%	2.80%
10yr PWLB Rate	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%
25yr PWLB Rate	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%	3.50%	3.50%	3.60%	3.60%
50yr PWLB Rate	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.40%

5.3 CREDIT AND COUNTERPARTY RISK MANAGEMENT

The MHCLG issued Investment Guidance in 2018, and this 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 23 March 2003 and will apply its principles to all investment activity. In accordance with the Code, the Director of Finance has produced its treasury management practices (TMPs). This part, TMP 1(1), covering investment counterparty policy requires approval each year.

Annual 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 strategy for the following year, covering the identification and approval of 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 that 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 a 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 awarded a high credit rating by a credit rating agency. For category 4 this covers pooled investment vehicles, such as money market funds, rated AAA by Standard and Poor's, Moody's and / or Fitch rating agencies.
5. A body that is considered of a high credit quality (such as a bank or building society), which is defined as having a minimum Short-Term rating of F2 (or the equivalent) as rated by Standard and Poor's, Moody's and / or Fitch 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. These criteria

are a maximum of 365 days (to be classified as specified) and a counterparty limit of £25 million.

Low Volatility Net Asset Value (LVNAV) Money Market Funds

A new category of money market funds (MMF) has been introduced into the table below – low volatility net asset value. All sterling funds that do not invest mainly in government bonds are no longer able under EC regulations to be classified as constant net asset value (CNAV).

One of the characteristics of a MMF is that one pound invested is always returned (there have been no sterling exceptions) as a pound (with income distributed monthly). CNAV MMF's are able to maintain a stable net asset value provided that the market value of the underlying investments is within 0.5% of the cost.

All the existing MMF's in use by Barnet will be changing to a Low Volatility Net Asset Value structure. The rules and structure are substantially similar. LVNAV funds can only maintain a fixed value if the value of investments is within 0.2% of the cost. In order to maintain a close relationship between costs and value, it is expected that the average maturity profile of MMF's will be shortened. LVNAV funds unlike CNAV funds are allowed to impose liquidity fees and redemption gates on investors under certain circumstances. The MMF's in which we invest will continue to be AAmmf rated and we will spread our investments over more than one fund to protect against redemption restrictions and costs.

The table below provides further details on the counterparties and limits for specified investments.

Instrument	Country/ Domicile	Counterparty	Maximum Counterparty Limits £m
Term Deposits	UK	DMADF, DMO	No limit
Term Deposits/Call Accounts	UK	Other UK Local Authorities	£25 million
Term Deposits/Call Accounts	UK*	Counterparties rated at least A- Long Term)	£25 million
Term Deposits/Call Accounts	Non-UK*	Counterparties rated at least A- Long Term in select countries with a Sovereign Rating of at least AA.	£25 million
CDs and other negotiable instruments		with banks and building societies which meet the specified investment criteria (on advice from TM Adviser)	£25 million
Deposits	UK	Registered Providers (Former RSLs)	£5m per RP
Gilts	UK	DMO	No limit
T-Bills	UK	DMO	No limit
Bonds issued by multilateral development banks		(For example, European Investment Bank/Council of Europe, Inter American Development Bank)	
AAA-rated Money Market Funds		CNAV MMF's LVNAV MMF's	£25 million
	UK and EC domiciled	VNAV MMF's (where there is greater than 12 month history of a consistent £1 Net Asset Value)	
Other MMF's and CIS	UK & EC domiciled.	Collective Investment Schemes (pooled funds) which meet the definition of collective investment schemes in SI 2004 No 534 or SI 2007 No 573 and subsequent amendments	£25 million.

For Non-UK banks, a maximum exposure of £40 million per country (including any non-specified exposures) will apply to limit the risk of over-exposure to any one country.

Non-specified investments –are any other type of investment (i.e. not defined as specified above) although the counterparties can also have investments that meet the definition of specified. The identification of these other investments and the maximum limits to be applied are set out below.

The Council will have a maximum of £100 million invested in non-specified investments.

Loans to Local Organisations

The Council will allow loans (as a form of investment) to be made to organisations operating in the borough that bring community benefits. The Council will undertake due diligence checks to confirm the borrower's creditworthiness before any sums are advanced and will obtain appropriate level of security or third party guarantees for loans advanced. The Council would expect a return commensurate with the type, risk and duration of the loan. A limit of **£25 million** per counterparty (and **£50 million in aggregate**) for this type of investment is proposed with a duration commensurate with the life of the asset and Council's cash flow requirements. **All loans would need to be in line with the Council's Scheme of Delegation and Key Decision thresholds levels.**

Loans to TBG Open Door Limited

The Council is considering advancing loans to its only owned affiliate TBG Open Door Limited to fund the purchase and build of affordable homes. A provision is included below for lending up to a maximum of £300 million.

The table below details the instruments, maximum maturity and monetary limits for non-specified investments.

Instrument	Maximum maturity	Max £M of portfolio and Credit limit	Capital expenditure?	Example
Term deposits with banks, building societies which meet the specified investment criteria	10 years	£10m per counterparty	No	
Term deposits with local authorities	10 years	£25m per authority	No	
CDs and other negotiable instruments with banks and building societies which meet the specified investment criteria	10 years	£10m per counterparty	No	
Gilts	10 years	£20 million Credit limit not applicable gilts issued by UK Government	No	
Bonds issued by multilateral development banks	10 years	£20 million Minimum credit rating AA+	No	EIB Bonds, Council of Europe Bonds etc.
Sterling denominated bonds by non-UK sovereign governments	5 years	£20 million Minimum credit rating AA+	No	

Other Non-Specified investments are permitted subject to the undertaking of a credit assessment by the Council's treasury advisor (or in the case of loans to local organisations, by a suitably qualified external advisor appointed by the Council) on a case-by-case basis. These are detailed below:

Instrument	Maximum maturity	Max £M of portfolio and Credit limit	Capital expenditure?	Example
Collective Investment Schemes	N/A – these funds do not have a defined maturity date	£25 million	No	Investec Target Return Fund; Elite Charteris Premium Income Fund; LAMIT; M&G Global Dividend Growth Fund
Deposits with registered providers	5 years	£5m per registered provider/£20 million overall	No	Barnet Homes Open Door not within TMS
Corporate and debt instruments issued by corporate bodies purchased from 01/04/12 onwards	5 years	20%	No	
Collective Investment Schemes (pooled funds) which do not meet the definition of collective investment schemes in SI 2004 No 534 or SI 2007 No 573 and subsequent amendments	N/A – these funds do not have a defined maturity date	£10 million	Yes	Way Charteris Gold Portfolio Fund; Aviva Lime Fund
Bank or building societies not meeting specified criteria	3 months	£10m per counterparty	No	Bank or building societies not meeting specified criteria
Loans to organisations delivering community benefits.	Over the life of the asset.	£25 million per counterparty.	Yes	Loans to sporting clubs based in the borough.
Loans to TBG Open Door Limited	As set out in the loan agreement	£300 million	Yes	

In the tables above, the minimum credit rating will be the lowest equivalent long-term rating assigned by Fitch, Moody's and Standard and Poor's. Where the credit rating is the minimum acceptable, the Council will consider rating sentiment and market sentiment e.g. the pricing of credit default swaps.

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 Link 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 Chief Financial Officer and if required new counterparties which meet the criteria will be added to the list. The Council will not always follow the maximum maturity guidance issued by Link. However, any deposit made with a longer maturity than the Link guidance will be approved with the Chief Financial Officer.

5.4 APPROVED COUNTRIES FOR INVESTMENTS

Below is listed the domicile of the counterparties with which the Council will transact.

AAA

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

AA+

- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)
- France
- Hong Kong
- U.K.

This page is correct as at 15 January 2019. The Council will continue to utilise UK counterparties should the national rating fall below AA provided the individual counterparty restrictions are achieved.

5.5 TREASURY MANAGEMENT SCHEME OF DELEGATION

(i) Council

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.

(ii) Policy and Resources Committee

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
- budget consideration and approval;
- approval of the division of responsibilities;
- approving the selection of external service providers and agreeing terms of appointment.

(iii) The Financial Performance and Contracts Committee

- receiving and reviewing regular monitoring reports and acting on recommendations.

(iv) Audit Committee

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

5.6 THE TREASURY MANAGEMENT ROLE OF THE SECTION 151 OFFICER

The S151 (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.;
- preparation of a capital strategy to include capital expenditure, capital financing, and treasury management, with a long-term timeframe;
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money; and
- ensuring that due diligence has been carried out on all investments and is in accordance with the risk appetite of the authority.