LONDON BOROUGH OF CAMDEN	WARDS: All
REPORT TITLE Treasury Management Strategy (CS/2019/01)	
REPORT OF Cabinet Member for Finance and Transformation	
FOR SUBMISSION TO Resources and Corporate Performance Scrutiny Committee Cabinet Audit and Corporate Governance Committee Council	**DATE** **19 February 2019** **20 February 2019** **21 February 2019** **25 February 2019**

SUMMARY OF REPORT

This report sets out the Treasury Management Strategy for 2019/20 including the Borrowing and Investment Strategies.

Our Camden Plan includes a commitment to "strong financial management". A robust and effective Treasury Management Strategy is crucial to enabling this ambition. This report provides a perspective on the management of investments of £267m and debt of £343m worth of Council resources, considers the Council's long term borrowing needs and updates on external factors that impact the future treasury management plans of the Council.

The report is coming to Cabinet and Council because it is a Chartered Institute of Public Finance and Accountancy (CIPFA) requirement for the Treasury Management Strategy to be agreed by those committees.

Local Government Act 1972 – Access to Information

Online documents were used in the preparation of this report which are available on the Council's website via embedded links and are cross-referenced throughout. A full list is included after the main report alongside a list of appendices.

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RECOMMENDATIONS

The Resources and Corporate Performance Scrutiny Committee is asked to consider the report and make any recommendations to the Cabinet.

The Audit and Corporate Governance Committee is asked to review the Treasury management policy statement and the risks within the debt and investment portfolios and if required make recommendations to Council.

The Cabinet is asked to endorse and recommend to **Council**, to adopt and agree the following:-

(1) the Borrowing Strategy as set out in section 2 (paragraphs 2.11 – 2.18) and Appendix 2;

(2) the operational boundaries and authorised limits in Table 1;

(3) the prudential and treasury management indicators set out in the tables presented in Appendices 1, 2 and 3;

(4) the Investment Strategy as set out in section 2 (paragraphs 2.19 – 2.27) and Appendix 3;

(5) the creditworthiness policy and credit rating criteria as set out in Appendix 3;

(6) the investment instruments categorised as specified and non-specified in Appendix 4; and

(7) the Minimum Revenue Provision (MRP) Policy for depreciating assets set out in Appendix 5.

The Council is asked to adopt and agree the following:-

(1) the Borrowing Strategy as set out in section 2 (paragraphs 2.11 – 2.18) and Appendix 2;

(2) the operational boundaries and authorised limits in Table 1;

(3) the prudential and treasury management indicators set out in the tables presented in Appendices 1, 2 and 3;

(4) the Investment Strategy as set out in section 2 (paragraphs 2.19 – 2.27) and Appendix 3;

(5) the creditworthiness policy and credit rating criteria as set out in Appendix 3;

(6) the investment instruments categorised as specified and non-specified in Appendix 4; and

(7) the Minimum Revenue Provision (MRP) Policy for depreciating assets set out in Appendix 5.

Signed: Director of Finance

Date: 8 February 2019

1. CONTEXT AND BACKGROUND

1.1. This report presents the 2019/20 Treasury Management Strategy, which remains broadly unchanged from last year, and which will govern the Council's treasury management activities for the coming year. CIPFA (the public sector accountancy body) defines treasury management as:

"The management of the organisation's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."[1]

1.2. Accordingly the report addresses a number of key concerns including:

- How the Council will fund its past and future capital plans;
- How borrowing and investments will be managed;
- How surplus cash balances will be invested to ensure cash is available when necessary and to prioritise security; and
- How the Council will use its revenue resources to pay down debt (the Minimum Revenue Provision policy)

1.3. Effective treasury management is about looking after the Council's cash and having money in the right place at the right time. A number of online documents are published on the Council's website which provide additional background information concerning the Council's treasury management activity and the issues discussed in this report.

2. PROPOSALS AND REASONS

2.1. A snapshot of the current treasury position is outlined in Table 1 which shows that the Council's debt and investment balances are significant in relation to the Council's gross revenue budget (£1.126bn) and its balance sheet (£3.345bn). It is therefore important that the Council manages the risks associated with its treasury position in order to safeguard the authority's financial robustness.

TABLE 1 - CURRENT TREASURY POSITION (30 Nov 2018)

		Principal	Average rate
Fixed rate funding	PWLB[2]	£219m	4.98%
Variable rate funding	Market	£124m	4.63%
Gross debt		**£343m**	**4.85%**
Short Term investments		**(£267m)**	**0.87%**
Net debt		**£76m**	

2.2. The Local Government Act 2003 requires the Council to 'have regard' to the CIPFA Treasury Management Code of Practice and the CIPFA Prudential Code for Capital Finance. The Code of Practice specifies that the Council should receive and approve an annual report covering its treasury management strategy. The objectives of the Prudential Code is to ensure that the Council's capital investment plans are affordable, prudent and sustainable

[1] CIPFA Treasury Management in the Public Services Code of Practice and Cross Sectoral Guidance Notes 2017

[2] The Public Works Loan Board is a statutory body operating within the UK Debt Management Office, an Executive Agency of HM Treasury

and it therefore requires the Council to annually set prudential indicators for capital finance to help the Council demonstrate that it has fulfilled these objectives.

2.3. The Council is required by Ministry of Housing, Communities and Local Government (MHCLG) guidance to set an Investment Strategy for the forthcoming year. Separate MHCLG guidance requires the Council to prepare an annual statement on its policy on making a minimum provision from revenue to repay debt (Appendix 5).

2.4. The Council has adopted the Treasury Management Policy Statement (a high level statement about the treasury management function). This forms part of our financial standing orders.

2.5. The Council uses Link Asset Services as its external treasury management consultant. Whilst this arrangement gives the Council access to specialist skills and resources, it should be remembered that the responsibility for treasury management rests with the authority and that external service providers are supporting the authority's treasury management function.

<u>Economic background and outlook for interest rates</u>

2.6. The Council's approach to treasury management is driven by its capital plans (including its capital strategy), which determines the size and nature of both the borrowing requirement and, to an extent, surplus cash balances. Aside from internal drivers, the direction of both the borrowing and the investment strategy will be influenced by the Council's view of the current economic environment and the likely direction of interest rates.

2.7. At the December Bank of England's Monetary Policy Committee meeting the Committee voted unanimously to maintain Bank Rate at 0.75%. In announcing its decision the Bank noted the further intensification of Brexit uncertainties, coupled with the slowing global economy, has also weighed on the near-term outlook for UK growth (expected to be c1.7% in 2019). These uncertainties are weighing on UK financial markets. UK financing costs have risen by more than in other advanced economies. UK-focused equity prices have fallen materially. Sterling has depreciated further, and its volatility has risen substantially. Market-based indicators of inflation expectations in the United Kingdom have risen, the decline in oil prices also means that UK CPI inflation is likely to fall below 2% in coming months. The MPC had also noted the well-documented weakness in productivity and limitations in the labour market. All members agreed that any future increases in Bank Rate would be expected to be at a gradual pace and to a limited extent. Markets had largely discounted this action although Sterling fell based on this news.

2.8. The long-term expectation is for borrowing rates to rise gradually although it is likely that we will continue to experience volatility as demand for safe haven UK gilts fluctuates in-line with investor confidence.

2.9. Our treasury consultants' interest rate forecasts are shown below. This shows the Bank of England's base rate (Bank Rate) experiencing one rise in 2019 and rising to 2% by March 2022. Rates on investments (shown as LIBID rates) are set to increase from 0.9% on very short term investments (3 months) to between 1-1.2% in 2019 in line with Base Rate expectations. Borrowing rates available from the PWLB show rates in long term debt (50 years) rising from 2.70% to 3.40% over the forecast period.

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%

2.10. The above forecasts are only one set of forecasts and there are obviously a range of scenarios either side of this. It is likely that the Bank of England will refrain from raising interest rates while economic uncertainty remains in order to avoid damaging growth. However, if inflation increases at a faster pace than currently expected, the timing of an increase in Bank Rate could be brought forward.

Borrowing Strategy

2.11. The Council's underlying need to borrow is referred to as the 'Capital Financing Requirement', or CFR. The CFR represents the total amount of capital expenditure that is yet to be financed from capital resources (made up of capital grants, capital receipts, and revenue contributions). The CFR is notionally earmarked to be financed by borrowing, but the timing and nature of this borrowing is determined by capital market factors such as availability of good interest rates, the outlook for borrowing rates and the availability of investment balances to offset borrowing in the short term.

2.12. The Council currently has external debt of £343m to meet some of its CFR. However the CFR is currently £514m and in recent years the Council has decided to fund part of its CFR by running down investment balances rather than entering into new external borrowing. As a result, the Council is presently "under-borrowed" by £171m and, if no new borrowing is undertaken, this amount is set to increase steadily over the years reaching £261m in 2021/22. (Table 1).

TABLE 1: BORROWING REQUIREMENT

	2017/18	2018/19	2019/20	2020/21	2021/22
	£m	**£m**	**£m**	**£m**	**£m**
GF debt	44	42	42	42	42
GF CFR	46	40	86	98	81
GF difference	**2**	**-3**	**43**	**56**	**39**
HRA debt	299	287	287	287	287
HRA CFR	468	479	478	485	508
HRA difference	**169**	**192**	**191**	**199**	**222**
Total debt	343	329	329	329	329
Total CFR	514	519	564	583	590
Total difference	**171**	**189**	**235**	**254**	**261**
Operational boundary	**514**	**519**	**564**	**583**	**590**
Authorised Limit	**614**	**619**	**664**	**683**	**690**

2.13. The borrowing strategy (Appendix 2) proposes that the Council continues its existing borrowing approach, based on the temporary use of internal resources (reserves) rather than new external borrowing. The authority continues to be able to meet its residual borrowing requirement from investment balances, and the medium term outlook for interest rates will accommodate this strategy, therefore this strategy remains appropriate.

2.14. If the Council did take on new borrowing now, it would immediately increase investment balances, which would expose the Council to greater credit risk, as it would need to invest these sums with banks until needed. One benefit of an internal borrowing approach is that the Council reduces its exposure to the risk of a borrower defaulting on the repayment of investment balances.

2.15. Further, as the rate of return on investments (0.84%) is significantly lower than the price of new borrowing (2.70% for 50 year borrowing), the Council would incur a "cost of carry" (i.e. the difference between the two rates, which is 1.86%). This would create a real revenue cost to the Council which at present it can avoid. To illustrate this, if the Council took on new borrowing worth £189m to meet its expected CFR in 2019/20, it would incur an additional net annual revenue cost of £3.5m (borrowing costs less investment returns).

2.16. Although the interest rate outlook noted above will accommodate this approach, there has been marked volatility in Gilt yields (which underpin PWLB rates) due primarily to an increase in inflation expectations, the weakening of sterling and uncertainty over "Brexit". Should the economic outlook and interest rate environment diverge from the expectations set out above, the Council will not be restricted from entering into new borrowing. The borrowing strategy is flexible enough to allow the Council to capitalise on advantageous borrowing opportunities or to mitigate a steep rise in borrowing costs.

2.17. Table 1 also illustrates the two debt pools that the Council operates: one for the General Fund and one for the Housing Revenue Account (HRA), alongside their respective CFRs. Currently the General Fund is fully borrowed but will have a borrowing requirement from next year due to the Town Hall refurbishment, the Highgate New Town scheme and a requirement to fund the capital programme with capital receipts. The HRA is currently under borrowed by £192m and this grows to £222m by the end of 2021/22.

2.18. The borrowing strategy (shown in more detail in Appendix 2) sets levels for the Operational Boundary and Authorised Limit on external debt (paragraphs 2.1 to 2.4), which are the key controls on external borrowing that the Council must set each year. The Operational Boundary is set at the same level as the forecast CFR, whilst the Authorised Limit is set £100m above this to allow possible debt restructuring or forward borrowing if advantageous.

Investment Strategy

2.19. The Council's investment priorities are:

(a) security of capital (primarily) and
(b) liquidity of its investments (secondly).

2.20. After these overriding priorities, the Council will aim to optimise returns on its investments commensurate with high levels of security and good liquidity. The risk appetite of the Council is low in order to give priority to security of its investments, which is paramount.

2.21. On 30 November 2018, the Council's investment balances totalled £267m. Investment balances fluctuate daily with receipts and payments cash flows. Most of the Council's investments are held with banks (£172m), although the Council continues to lend to other local authorities (£65m) too. £30m is also invested in money market funds for the purposes of managing daily cash flow.

2.22. The investment strategy has been reviewed in light of the evolving investment environment and the proposed investment strategy for 2019/20 (Appendix 3) is very similar to the existing strategy. The Council continues to invest in the most credit worthy banks globally.

2.23. The Council has some cash balances which are expected to be available for investment on a long term basis, which might help to mitigate the effects of inflation noted above. The Council already has the ability to invest with the UK Government and local authorities for up to five years and, as part of the last strategy, property funds were added to the list of eligible investments detailed in Appendix 4. The Council does not currently have any property funds and any use will be proportionate, will only follow detailed due diligence and will follow best practice. The Council is also conducting a search for an 'Ultra long dated bond fund' which runs a similar strategy to its current MMF funds, but which has slightly longer investment horizons in order to earn enhanced interest.

2.24. The credit rating criteria (the policy by which banks are selected for the Council's counterparty list) remains unchanged from the existing strategy and is detailed in the investment strategy (Appendix 3, paragraph 11). The counterparty criteria are judged to be consistent with the Council's objective of achieving best value in treasury management only after security concerns have been satisfied. However if there was a marked improvement in the financial markets and robust evidence demonstrated an easing of counterparty risk, then officers would want to reflect this in the counterparty criteria. A perceived reduction in risk in financial markets would correspond to increased time limits of investments beyond the current 12 month maximum time limit for banks. Officers have considered widening the criteria for banks on our lending list but, given the volatility in global equity markets and domestic pressures with Brexit, it has been considered sensible to leave the criteria as they are this year.

2.25. The Council continues to view the Royal Bank of Scotland as part-nationalised given the Government's continuing ownership (62%). The Government sold another tranche in RBS in June 2018 and continues to look for opportunities to return the bank to private ownership. However, the bank must still negotiate some legacy issues and the Government must decide on timing, as large losses are associated with any sales based on the current share price. Therefore it is expected that the Government will continue to be a significant shareholder in RBS for some time.

2.26. The Council uses three money market funds (MMFs): Goldman Sachs, JP Morgan and Aberdeen. These funds allow the Council to manage day-to-day liquidity requirements very effectively and their use will continue in 2019/20.

2.27. New MMF regulation means that these 'Constant Net Asset Value' (CNAV) priced funds must change after 20 January 2019. Funds on the whole are converting to a new category defined as 'Low Volatility NAV' (LVNAV) funds and all of our funds intend to make this conversion. It should be noted that many of the features of our current MMFs will be the same with the new LVNAV funds (average maturity, maximum loan period, short term cash within funds). Similar to CNAV funds, LVNAV funds will trade at a stable price per share, so as long as the shares do not deviate daily from the actual NAV by more than 0.20%. CNAV funds are currently allowed to deviate by 0.50%. The Council and our consultants remain comfortable with the operation and suitability of these MMFs.

3. OPTIONS APPRAISAL

3.1. The Council has an outstanding borrowing requirement, which is larger than its existing debt portfolio (Table 1). It has the option to either enter into new borrowing now or to continue to meet this requirement temporarily by offsetting against reserves. The Council could choose to take out new debt now and fix into relatively low interest rates. This would have the effect of reducing 'interest rate risk'. This is the risk that entering into new debt in the future will be more expensive due to higher borrowing rates. However, any new borrowing now would incur additional interest costs. Alternatively the Council could temporarily use its own resources (in the form of reserves and working capital) to offset borrowing requirements, thereby avoiding new long-term borrowing in the short to medium term.

3.2. The Council also has investments of £267m which need to be managed in-line with the treasury management strategy in order to meet the objectives of security, liquidity and yield (in that order of priority). If the Council expands its risk appetite, it will increase interest earned. However, the Council would be exposed to a greater risk of default from investments with weaker financial standings. The Council's attitude to risk is low and it has chosen to be more risk averse than standard methodology adopted by its treasury consultants.

4. **WHAT ARE THE KEY IMPACTS / RISKS? HOW WILL THEY BE ADDRESSED?**There are a number of risks inherent in treasury management and the prime objective of the Council's approach to treasury management is the effective control of such risks.

4.2. A key risk within the Council's investment activity is that an entity with whom the Council has invested in defaults on repayment and as a result the Council experiences financial loss. This risk is mitigated by a strict credit rating criteria which aims to minimise the risk of default commensurate with the Council's low appetite for risk.

4.3. There are risks around the rate at which borrowing is locked into and the interest costs associated with carrying the debt. As the Council is under-borrowed, there is a risk that it will be forced to borrow at a time when interest rates are high. The borrowing strategy is based upon interest rate views as well as detailed cash flow forecasting which indicates that the Council will have sufficient resources to pursue the proposed strategy and avoid having to borrow at any time when rates are high in future years.

4.4. Economic forecasts change and there is a risk that actual experience does not reflect predictions. The treasury strategy is monitored regularly during the year by officers and our treasury consultants to ensure the Council is best placed to manage its treasury position in an evolving economic environment.

4.5. Whilst various risks have the potential to materially affect the Council's financial position, the CIPFA Codes of Practice acknowledge that the avoidance of risk is neither appropriate nor possible. However, an effective treasury management strategy will enable the Council to manage these risks successfully.

5. **LINKS TO THE CAMDEN PLAN OBJECTIVES**Our Camden Plan includes a commitment to "strong financial management" Inappropriate management of the risks surrounding treasury management could lead to a diminishment of the Council's financial position which would significantly curtail the Council's ability to fulfil this ambition. Therefore a robust and effective treasury management strategy is crucial to enabling Our Camden Plan objectives.

6. **CONSULTATION**

6.1. There is no consultation required for this report.

7. LEGAL IMPLICATIONS

7.1. Local Authorities' powers of treasury management are governed by the Local Government Act 2003 ("the Act"). The Act sets out authorities powers to borrow (s.1 and additional provisions in Part 1 of the Act) and to invest (s.12 of the Act).

7.2. The power to borrow under the Act, up to the affordable limit, is determined by the Local Authority itself, having regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) codes of practice, "Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes".

7.3. Local Authorities also have the power to invest (s. 12 of the Act) for “any purpose relevant to their functions under any enactment or for the purposes of the prudent management of their financial affairs”. This power is subject to restrictions contained in the Local Authorities (Funds) (England) Regulations 1992/2428 (“the Regulations”).

7.4. The Act (including subordinate legislation (Local Authorities (Capital Finance and Accounting) (England) Regulations 2003) states that in carrying out its functions a Local Authority must show regard to relevant guidance, including the CIPFA codes of practice (Prudential Code for Capital Finance in Local Authorities and Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes). Local authorities must also have regard to Statutory Guidance issued by the Ministry of Housing, Communities and Local Government (MHCLG) itself (issued under s.15 of the Act).

8. RESOURCE IMPLICATIONS

8.1. The comments of the Executive Director Corporate Services have been incorporated into this report.

9. WHAT ACTIONS WILL BE TAKEN AND WHEN FOLLOWING THE DECISION AND HOW WILL THIS BE MONITORED?

9.1. The Executive Director Corporate Services will continue to operate treasury activity within parameters set out and agreed as part of this report. Once this report is agreed, all limits will become effective immediately. Activity will continue to be reported quarterly to the Audit and Corporate Governance Committee. The Annual Report and Mid-year Strategy will be reported to Cabinet and Council in the summer and will review activity over the past financial year and will update on the mid-year treasury position.

10. APPENDICES

Appendix 1 – Capital Expenditure and Prudential Indicators
Appendix 2 – Borrowing Strategy
Appendix 3 – Investment Strategy
Appendix 4 – Specified and Non-Specified Investments
Appendix 5 – Minimum Revenue Provision Policy

Online Document 1 – Treasury Management Explained
Online Document 2 – Glossary of Key Terms
Online Document 3 – Code of Practice Requirements
Online Document 4 – Credit Rating Agency definitions
Online Document 5 – Credit Rating Methodology
Online Document 6 – Lloyds and RBS Update
Online Document 7 – MMF Update
Online Document 8 – Municipal Bonds Agency
Online Document 9 – Economic Background
Online Document 10 – Illustrative Counter Party List
Online Document 11 – Treasury Management Risks

REPORT ENDS

APPENDIX 1: CAPITAL EXPENDITURE AND PRUDENTIAL INDICATORS

1.1. The Council's approach to treasury management is driven by its capital expenditure plans as the amount of capital expenditure which is not immediately financed will need to be funded by borrowing.

1.2. The overall control of the Council's capital plans is determined through a series of prudential indicators which demonstrate that total capital investment remains within sustainable limits and require Council's approval.

1.3. The prudential indicator underneath outlines the capital expenditure forecasts for this year and the next three years.

PRUDENTIAL INDICATOR 1 – CAPITAL EXPENDITURE

Capital expenditure £m	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Community Services	0	1	2	1	0
Development - CIP & Major Projects	109	98	108	80	78
ICT	2	3	1	0	0
Public Health	0	0	0	0	0
Place Management	12	13	13	1	1
Property Management	62	110	114	96	64
Regen & Planning	6	22	22	2	0
Total	**190**	**248**	**259**	**180**	**143**
GF	62	101	114	46	28
HRA	127	146	143	134	115
Total	**190**	**247**	**258**	**179**	**143**

1.4. The Council has a number of financing options available to it to resource this planned expenditure immediately including capital receipts, capital grants, contributions, reserves and direct contributions from revenue. This information is summarised in the table below, which also demonstrates a planned shortfall in each year (the net financing need).

Financing of capital expenditure £m	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Capital receipts	102	92	131	98	70
Capital grants	25	60	43	15	11
Other contributions					
Capital reserves					
Revenue	46	61	44	42	48
Net financing need for the year	**15**	**35**	**40**	**24**	**13**

1.5. The capital expenditure and financing figures above exclude the Council's PFI schemes and finance leases which already include a borrowing facility.

PRUDENTIAL INDICATOR 2 – CAPITAL FINANCING REQUIREMENT

1.6. The Capital Financing Requirement (CFR) refers simply to the total historic outstanding capital expenditure which the Council is yet to resource immediately.

1.7. The net financing need for each of the years shown above will increase the CFR. However, the CFR does not grow indefinitely as the Council is required by statute to make an annual revenue charge (the Minimum Revenue Provision) which will broadly reduce the CFR in line with the useful lives of the assets created by the Council's capital investment.

Capital Financing Requirement £m	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
GF (Excl. PFI & FL)	46	40	86	98	81
HRA (Excl. PFI & FL)	468	479	478	485	508
Total CFR (Excl. PFI & FL)	**514**	**519**	**564**	**583**	**590**
GF PFI	53	51	50	49	47
GF Finance Leases	0	0	0	0	0
HRA PFI	16	11	6	0	0
Total CFR (PFI & FL)	**69**	**63**	**56**	**49**	**47**
Total CFR	**583**	**581**	**620**	**632**	**636**
Movement in CFR	**0**	**-2**	**38**	**12**	**5**

1.8. The CFR includes the Council's other long term liabilities (PFI schemes and finances leases). Although these schemes increase the CFR they are already financed and so the Council is not required to arrange separate funding. The total balance of these liabilities is £63m at the end of 2018/19 and is predominantly comprised of three PFI schemes as well as a number of small finance leases.

PRUDENTIAL INDICATOR 3 – CAPITAL FINANCING REQUIREMENT AND GROSS DEBT

1.9. Using borrowing to support revenue expenditure is unsustainable over the medium term. In order to ensure that over the medium term debt will only be for a capital purpose, the Council should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. Gross debt includes other long time liabilities.

£m	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
GF CFR	46	40	86	98	81
HRA CFR	468	479	478	485	508
Total CFR	**514**	**519**	**564**	**583**	**590**
GF Gross Debt	97	96	94	91	89
HRA Gross Debt	315	310	305	287	287
Total Gross Debt	**412**	**406**	**399**	**378**	**376**
GF Under / (over) borrowing	(51)	(56)	(9)	7	(8)
HRA Under / (over) borrowing	153	169	173	199	221
Total Under / (over) borrowing	**102**	**113**	**165**	**205**	**213**

1.10. The Executive Director Corporate Services reports that the Council complied with this indicator in the current year and does not envisage any problems in meeting this requirement in future years with an under-borrowed position of £113m set to increase over the medium term. Although singularly the General Fund is currently over-borrowed, this position is projected to be reversed at the end of the current year, where an increase in the General Fund CFR is forecast.

PRUDENTIAL INDICATOR 4 – HRA DEBT CAP

1.11. The HRA self-financing determinations 2012 prescribe a limit on HRA debt, which was set at £525m. This limit no longer applies but is reported for completeness. Borrowing is measured with reference to the HRA CFR, excluding other long term liabilities. The Council complied with this prudential indicator in the current year.

£m	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
HRA Debt Cap *	525	525	525	525	525
HRA CFR	468	479	478	485	477
Headroom	**57**	**46**	**47**	**39**	**48**

* Abolition of HRA debt cap. In October 2018, Prime Minister Theresa May announced a policy change of abolition of the HRA debt cap. Members will be updated when information becomes available as to the detail of when and how this policy change will be implemented.

1.12. The affordability of the Council's capital plans is ultimately determined by the revenue consequences of its investment. The following indicators provide an indication of the impact of the capital plans on the Council's overall finances.

PRUDENTIAL INDICATOR 5 – RATIO OF FINANCING COSTS TO NET REVENUE STREAM

1.13. This indicator estimates the authority's capital financing costs as a percentage of overall revenue. The ratio distinguishes between the financing costs and revenues that pertain to the HRA and those that relate to the General Fund. The ratio now includes financing costs associated with the Council's PFI contracts for completeness.

%	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
GF					
HRA	9%	11%	11%	10%	10%

1.14. Financing costs for the General Fund as a proportion of net revenue are expected to rise to approximately % in later years as investment income is mitigated by low investment rates and an increase in internal borrowing, whilst revenue will reduce. The equivalent ratio for the HRA is forecast to remain fairly stable, reducing gradually as external borrowing running at a comparatively high rate matures, and PFI charges decrease.

PRUDENTIAL INDICATOR 6 – INCREMENTAL IMPACT OF CAPITAL INVESTMENT DECISIONS ON THE COUNCIL TAX AND HOUSING RENTS

1.15. A fundamental indicator of affordability for the council to consider in setting its forward plans is the impact on the council tax and housing rents that will result. Financing costs on the prudential borrowing are met by savings in expenditure or additional income associated with the new capital schemes. Therefore, the investment plans set out above do not require an increase in the council tax or council rents.

£	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
Council tax	NIL	NIL	NIL	NIL
Housing rent	NIL	NIL	NIL	NIL

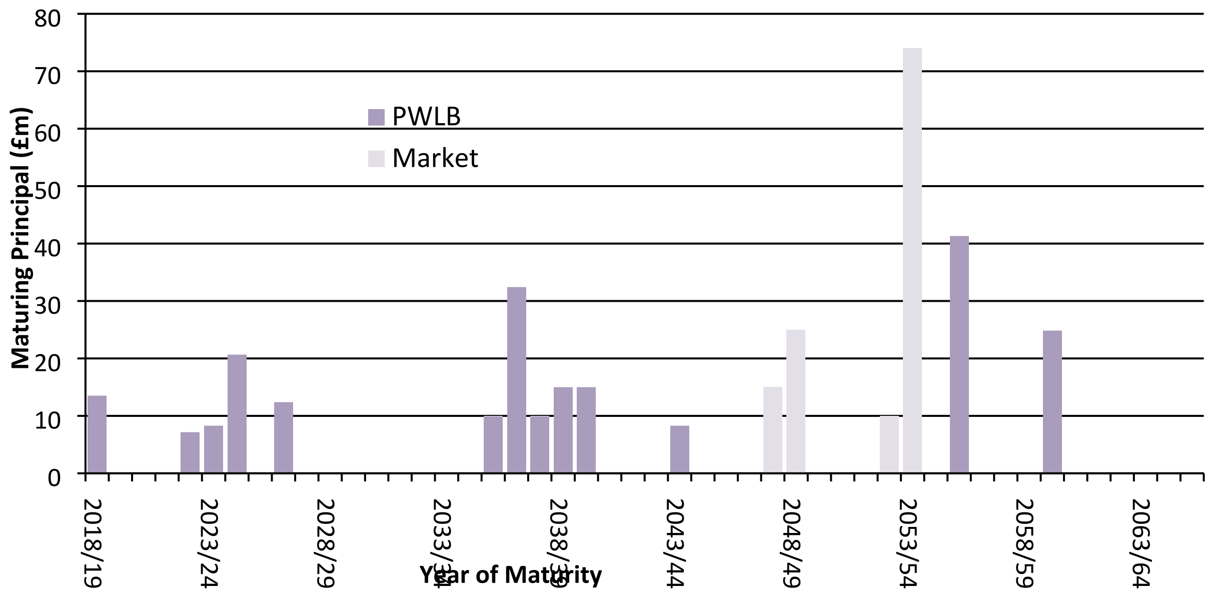
APPENDIX 2: BORROWING STRATEGY

1.1. The capital plans outlined in Appendix 1 will anchor the borrowing strategy for the forthcoming year and the Treasury Management Strategy aims to ensure that borrowing requirements flowing from these capital plans are managed so that sufficient cash is available to ensure the capital programme functions alongside normal revenue operations. This means that borrowing will be undertaken where necessary.

CURRENT DEBT PORTFOLIO

1.2. As shown in the main report, the Council has an existing debt portfolio totalling £343m which is predominantly made up of PWLB fixed rate borrowing with a significant contingent of market debt. The maturity profile of the current debt portfolio is shown below in table 1.

TABLE 1: DEBT MATURITY PROFILE



1.3. Two pools are operated, with debt attributable to the HRA and the General Fund. The last debt taken out by the Council was in March 2013 when £50m was borrowed for the HRA and £20m for the GF. £10m of this debt was subsequently transferred to the HRA.

1.4. Market debt is comprised of six ‘Lenders Option Borrowers Option’ (LOBO) loans. These loans give the lender an option to vary the loan’s interest rate every six months and when this event happens the Council has the option to either accept the revised rate or repay the loan in full. No lender has exercised their option to date and our treasury advisors continue to judge the probability of this happening as unlikely. The loans are shown at their ultimate maturity dates in the profile. However, the loans could be show as maturing in year, given the LOBO structure.

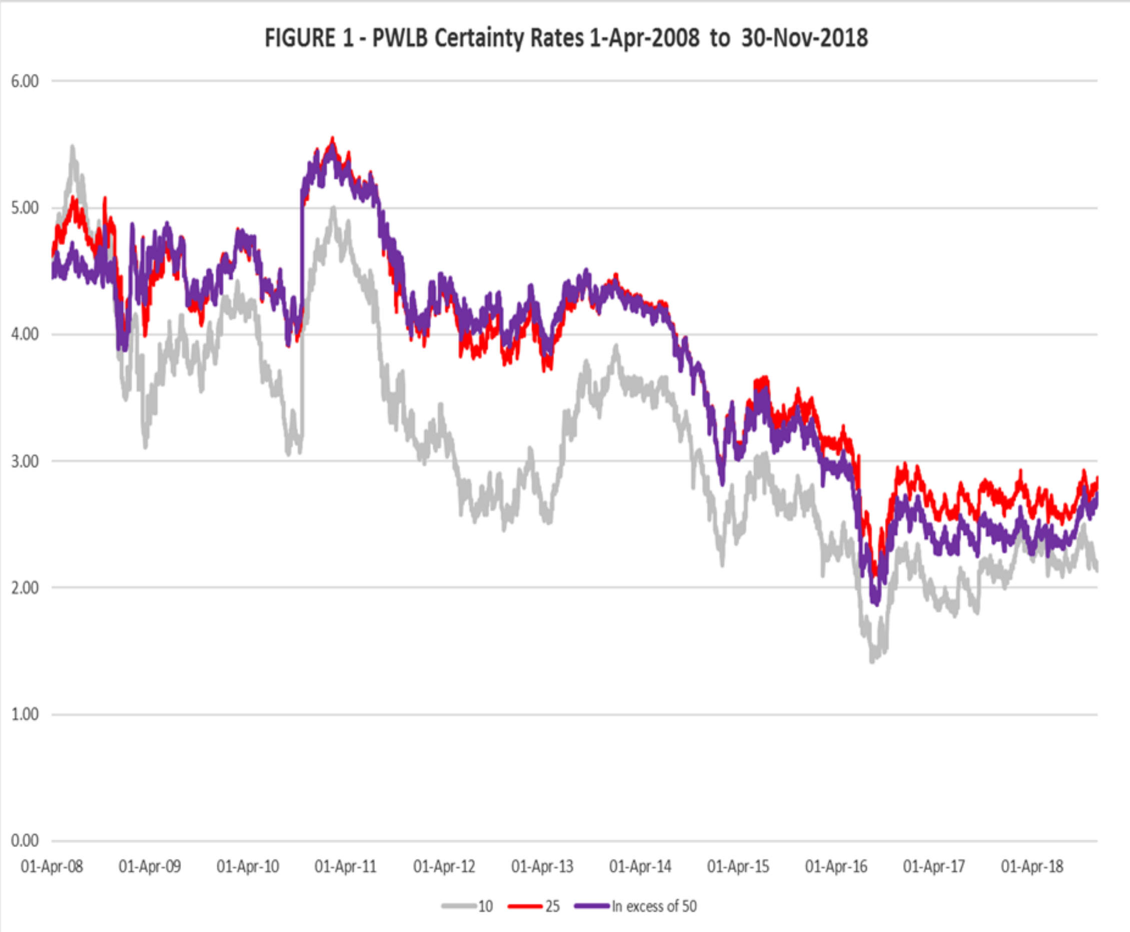
1.5. Officers will progress the restructuring of these loans, should the opportunity arise and if it is to the Council’s advantage. At present, the breakage costs incurred in restructuring any of the loans are prohibitively expensive.

1.6. The average life of the overall debt portfolio is 25 years as at 30 November 2018. Market debt has a longer life than PWLB loans. When new debt is considered, it is important that this profile is kept broadly flat and even to mitigate against refinancing risk (i.e. the risk that the Council needs to refinance debt when rates are high).

BORROWING STRATEGY

1.7. Based on the current levels of external borrowing and the medium term CFR forecast presented in Appendix 1, the Council will be under-borrowed by £189m at the end of 2018/19, and this figure will gradually increase to £261m by 2021/22.

1.8. As shown in figure 1, borrowing rates are currently low relative to their recent history and the Council could choose to take on new debt now to reduce its under-borrowed position.



1.9. Consideration has been given to possible future tranches of borrowing in the coming year. However, it is recommended that the existing internal borrowing approach is continued for 2019/20, based on the Council's financial positon as well as the outlook for interest rates (see main report, paragraph 4.4)

1.10. At present, the Council's core funds are projected to provide sufficient cover to enable the continuation of the current internal borrowing approach for the medium term. During the next few years, reserves are forecast to reduce gradually; other internal resources, including working capital, provisions and capital grants unapplied, are expected to remain relatively stable.

TABLE 2 – CORE FUNDS [needs updating]

£m	2016/17	2017/18	2018/19	2019/20	2020/21
Earmarked Reserves	76	68	56	53	52
General Balances	14	14	14	14	14
Housing Revenue Account	38	37	35	34	34
Schools Balances	16	13	9	4	4
Capital Receipts Reserve	36	54	98	63	45
Total Reserves	**179**	**185**	**212**	**168**	**149**
Provisions & Capital Grants Unapplied	30	30	30	30	30
Working Capital	178	127	127	127	127
Total Core Funds	**387**	**342**	**369**	**324**	**305**
Internal Borrowing	-164	-203	-225	-244	-263
Investments	**223**	**139**	**143**	**80**	**42**

1.11. A key benefit of using internal borrowing is the impact on revenue. The rate of return on investments is considerably lower than the rates available on new borrowing. A decision to enter into new borrowing will lead the Council to incur a “cost of carry”, which is the difference between the aforementioned rates.

1.12. A further advantage of this strategy is the reduction in the Council’s exposure to credit risk. The temporary use of cash balances to cover the remaining capital financing requirement means that cash balances held with external counterparties are smaller, which reduces the Council’s exposure to the risk of a counterparty defaulting. Conversely, if new borrowing is undertaken, cash balances will be larger.

1.13. The main risk inherent relates to interest rates. Eventually the Council will need to arrange new external borrowing to replace the temporary use of internal resources and there is a risk that it will need to source new debt at a time when interest rates are high. Officers are mindful of this risk and monitor borrowing rates on a daily basis. The latest outlook for interest rates over the medium term is relatively benign, suggesting that there is no advantage to be gained from taking on new borrowing.

1.14. Therefore the Council’s borrowing strategy will give consideration to new borrowing in the following order of priority:

i. Whilst there is the prospect of a cost of carry, with Bank Rate forecast to be significantly beneath borrowing rates (as set out above), the Council will pursue an internal borrowing strategy (reducing investments to finance capital spend). This is supported by an analysis of core funds which are forecast to reduce to £305m by the end of 2020/21 from current levels of £387m (Table 2). This core cash position will allow the Council to continue netting down debt whilst there is a cost of carry.

ii. The Council will monitor rates on borrowing from the PWLB and will continue to review with our treasury management consultants. The Executive Director

Corporate Services will make any final decision given market conditions and the latest views of officers and our treasury consultants.

iii. The Local Government Association has now established the Municipal Bond Agency (MBA) which will shortly be issuing its first bond. The Council has a £50k shareholding in the MBA and approved the Framework Agreement required for participation in the 2016/17 Treasury Management Strategy. The Council will monitor rates on borrowing from the MBA. As with PWLB borrowing, the Executive Director Corporate Services will make any final decision given market conditions and the latest views of officers and our treasury consultants.

iv. The Council could consider issuing bonds. The Council has in the past considered the concept of bond issuance but has not actively considered them due to the high cost of administration.

v. The Council will consider further use of market loans. To this end, the prudential indicator on variable rate debt was increased from 34-37% to 50% of debt in a previous TMS. Whilst these loans can introduce a degree of uncertainty as they may be 'called' and lead to a refinancing decision, they also offer structures which fix the rate in their earlier years to market rates (LIBOR) thus eradicating the cost of carry. Unlike PWLB loans they can also be forward fixed (i.e. arranged so the loan starts 2 years hence). Presently, the ratio of variable debt within the portfolio is 36% (£124m out of £343m).

1.15. Sensitivity of the forecast – In normal circumstances the main sensitivities of the forecast are likely to be the two scenarios noted below. Officers, in conjunction with the treasury consultants, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- *if it were 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 borrowing will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- *if it were 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 a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.

TREASURY INDICATORS

1.16. In order to ensure that borrowing is affordable and remains consistent with the Council's capital expenditure requirements, the Prudential Code requires local authorities to set upper limits on the total amount of external debt on the balance sheet. Council is asked to approve both the operational boundary and the authorised limit for external debt presented here.

TREASURY INDICATOR 1 – OPERATIONAL BOUNDARY FOR EXTERNAL DEBT

1.17. The operational boundary should be based on the estimate of the most likely scenario for capital expenditure and financing and should equate to the maximum level of external debt projected by this estimate. The operational boundary is therefore set to mirror the CFR.

1.18. The operational boundary is not a worst case scenario and it is possible that the limit will be breached temporarily on occasions due to variations in cash flow.

Operational boundary £m	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/2022 Estimate
Debt	518	564	583	589
Other long term liabilities	63	55	49	47
Total	**581**	**619**	**632**	**636**

TREASURY INDICATOR 2 – AUTHORISED LIMIT FOR EXTERNAL DEBT

1.19. The Council is also required to set a maximum limit for external debt for the forthcoming financial year and the following two financial years. External debt is prohibited beyond this limit. The authorised limit is set above the operational boundary to ensure that there is sufficient room to deal with unusual cash movements through debt restructuring, for example.

Authorised limit £m	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/2022 Estimate
Debt	618	664	683	689
Other long term liabilities	63	55	49	47
Total	**681**	**719**	**732**	**736**

1.20. The following two indicators are intended to help manage the Council's exposure to an adverse change in interest rates. Each indicator is set with reference to "net debt" (i.e. borrowing less investments) for existing fixed rate and variable rate principal sums outstanding, respectively.

TREASURY INDICATOR 3 – UPPER LIMITS ON FIXED RATE EXPOSURE

Net Debt Fixed Rate Exposure Limit £m	2018/19	2019/20	2020/21	2021/22
Borrowing	546	568	586	592
Investments	-114	-162	-85	-53
Net Fixed Rate Exposure	**426**	**364**	**449**	**520**

1.21. The proposed limit for fixed rate exposure provides scope for both debt and projected investment balances to be at fixed rates. To provide budget stability and reduce financial risk, the long term strategy is to have all debt at fixed rates.

TREASURY INDICATOR 4 – UPPER LIMITS ON VARIABLE RATE EXPOSURE

Net Debt Variable Rate Exposure Limit £m	2018/19	2019/20	2020/21	2021/2022
Borrowing	284	293	296	290
Investments	-100	-100	-100	-100
Net Variable Rate Exposure	**184**	**193**	**196**	**190**

1.22. Variable rate debt provides a facility to benefit from short term falls in interest rates but with the associated risk that unanticipated increases in rates will result in considerable volatility in interest costs. Conversely investments at variable rates provide flexibility to benefit from increases in interest rates. The Council's LOBO loans are classed as variable rate for the purposes of the indicator which has been set at 50% of the overall borrowing requirement to allow the Council to benefit from any future opportunities for further variable rate borrowing. The proposed indicator also enables the Council to make use of variable rate investments, should these be advantageous.

TREASURY INDICATOR 5 – MATURITY STRUCTURE OF BORROWING

1.23. The Council is exposed to the risk of having to refinance debt at a time in the future when interest rates may be volatile or uncertain. The following indicator helps the Council to manage this risk and avoid large concentrations of fixed rate debt maturing at the same time.

Maturity Structure of Borrowing for 2018/19	Lower Limit	Upper Limit	Current Position
Under 12 months	0%	20%	4%
12 months and within 24 months	0%	20%	0%
24 months and within 5 years	0%	25%	5%
5 years and within 10 years	0%	50%	10%
10 years and within 20 years	0%	50%	20%
20 years and within 30 years	0%	50%	18%
30 years and within 40 years	0%	50%	37%
40 years and within 50 years	0%	50%	7%

1.24. The debt portfolio includes £124m of LOBO loans which have been included at their ultimate maturity date. The limits have been designed to allow the Council to take advantage of any refinancing or new borrowing opportunities that may arise. There is a standard requirement for a single limit for debt maturing in 10 years and above, but the Council follows best practice by setting limits for each subsequent 10 year interval to provide a more comprehensive indication of refinancing risk.

POLICY ON BORROWING IN ADVANCE OF NEED

1.25. 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 borrowing (capital financing requirement) estimates over the three year planning period, 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.

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

DEBT RESCHEDULING

1.27. As short term borrowing rates will be considerably cheaper than longer term rates, there may be potential 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 size of premiums incurred, their short term nature, and the likely cost of refinancing those short term loans, once they mature, compared to the current rates of longer term debt in the existing debt portfolio.

1.28. 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 borrowing strategy;
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

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

1.30. The introduction in 2007 of a “spread” between the rates applied to new borrowing and the rates used to calculate premia or discounts on the early repayment of PWLB debt has served to make debt restructuring less attractive. The situation has been compounded since 2010 by a considerable further widening of the difference between these two rates and the resulting premia on PWLB debt make refinancing prohibitively expensive.

1.31. All rescheduling will be reported to the Council and the Audit and Governance Committee at the earliest meeting following its action.

MUNICIPAL BONDS AGENCY

1.32. The Municipal Bonds Agency (MBA) was set up with the purpose of offering loans to local authorities. To date they have not been able to issue loans but it is hoped that when the market is ready borrowing rates will be lower than those offered by the PWLB. The Authority will make use of this new source of borrowing as and when appropriate.

PWLB ABOLITION

1.33. With the establishment of the prudential borrowing regime in 2004, local authorities have individually taken on responsibility for determining the affordability of borrowing. As a consequence, the role of the PWLB as an independent body considering the suitability of loan applications has been reduced and the Government has recently proposed that the PWLB is abolished, and its functions are transferred to the Commissioners of the Treasury. Following a consultation exercise, the government has chosen to pursue the proposal and will use its powers in the Public Bodies Act 2011 to lay before Parliament a draft Order to implement the changes. Officers do not foresee that that the change in governance arrangements will have any discernible effect on the Council’s ability to borrow from central government. Operational activity will be delegated to the Debt Management Office, which has carried out the day-to-day responsibilities of the PWLB since 2002.

APPENDIX 3 – INVESTMENT STRATEGY

INVESTMENT POLICY

1. The Council's investment strategy has regard to the Guidance on Local Government Investments issued by the Ministry of Housing, Communities and Local Government, and the CIPFA Code of Practice on Treasury Management. The objectives for the investment strategy are security (protecting the capital sum from loss), liquidity (keeping money readily available for expenditure when needed) and yield, in order or priority.

2. In pursuing the primary goal of preserving capital from loss, the investment strategy operates a minimum level of credit quality to produce a list of highly creditworthy counterparties. Long term and short term credit ratings from the three main rating agencies will be used for this purpose.

3. Credit ratings will not be the only means by which the creditworthiness of potential and ongoing investments will be established. Officers will continue to monitor market information including the pricing of shares and "credit default swaps" as well as financial news reported in the quality press. A dialogue with relevant professionals in the financial sector, including money market brokers, is also maintained for this purpose.

4. The Council will engage its treasury management advisors, Capita Asset Services, on a regular basis to discuss its investment strategy.

5. In alignment with MHCLG's Guidance, investment instruments to be used are listed in Appendix 4 under categories of "specified" and "non-specified" investments.

6. The borrowing of monies purely to invest or on-lend and make a return is unlawful and this Council does not engage in such activity.

7. If the investment strategy is approved by the Council on 25 February, it will be used to control investment activity with immediate effect.

CREDITWORTHINESS POLICY

8. The creditworthiness policy establishes how suitable counterparties of an adequate credit standing will be selected and how their creditworthiness will be monitored.

9. The types of investments the Council will make use of are listed in Appendix 4. By engaging in an array of investment instruments the Council is able to maximise its access to high-quality counterparties. However instruments vary in their complexity, and those with a more complicated nature will only be used with the approval of the Executive Director Corporate Services. The list of specified and non-specified investment instruments is broadly unchanged from last year, with the exception of the addition of property fund investments, described underneath.

10. The Executive Director Corporate Services will maintain a list of eligible counterparties (a “counterparty list”) in compliance with the following criteria. Any proposal to alter the credit rating criteria or maximum sums invested per counterparty will need to be agreed by full Council.

11. The council will only use banks which meet the criteria outlined in table 1, and will only make investments with banks in line with the cash limits and durations specified:

TABLE 1 CREDIT RATING CRITERIA

Fitch		Moody’s		S&P		Cash limit	Maximum Duration
Long Term	Short Term	Long Term	Short Term	Long Term	Short Term		
AA-	F1+	Aa3	P-1	AA-	A-1+	£20m	1 year
AA	F1+	Aa2	P-1	AA	A-1+	£25m	1 year
AA+	F1+	Aa1	P-1	AA+	A-1+	£35m	1 year
AAA	F1+	Aaa	P-1	AAA	A-1+	£40m	1 year

12. All three rating agencies will be used and in the case of divergent opinion amongst the agencies, the lowest commonly held rating will be used to assess creditworthiness.

13. Additional requirements under the Code of Practice 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.

14. The Council is responsible for agreeing the credit rating criteria. The Executive Director Corporate Services has delegated authority to maintain banks on the counterparty list at an operational level. This may mean throughout the year that banks are removed from the list as ratings are downgraded, or their cash limits are amended. It is possible that banks are added to the list if their ratings improve (and the Executive Director Corporate Services will update the counterparty list following due diligence).

15. All credit ratings are monitored weekly. The Council is alerted to changes to ratings of all three agencies through its treasury consultants almost immediately after they occur, and so is able to act swiftly to a change affecting the lending list.

- if a downgrade results in the counterparty/ investment scheme no longer meeting the Council’s minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council is advised of information in movements in Credit Default Swap information against the iTraxx benchmark and other market data on a weekly basis. Extreme market

movements may result in downgrade of an bank or removal from the Council's lending list.

16. The Council's creditworthiness policy has regard to Link Asset Services' creditworthiness methodology. Link use a mathematical scoring system to determine appropriate investment durations for counterparties of differing credit quality. The Council operates with maximum investment durations which are stricter than this. The Executive Director Corporate Services has discretion to lengthen the maximum 6 month investment duration should conditions improve.

17. The Council no longer uses a minimum sovereign credit rating criteria due to credit rating agencies placing no value on this given banking resolution regimes across the world.

18. The Council recognises the Royal Bank of Scotland's status as a part-nationalised institution, and accordingly will make use of the bank for a maximum investment duration of 12 months, with a total investment limit of £60m at any given time.

19. The Council's main bank account for transactional purposes is held with the Royal Bank of Scotland. The Council aims to leave minimal balances overnight with its bankers.

20. The Council will continue to lend to other UK local authorities through term deposits. Lending to local authorities will be restricted to £40m per authority for a maximum of one year, although loans of up to five years may be made with the approval of the Executive Director Corporate Services.

21. From time to time the Council will invest in the UK Government itself through the use of gilts, treasury bills and the DMADF (an overnight deposit facility). Treasury bills are loans issued by the Government to fund short term liquidity. They are similar to gilts in nature, but have a term of less than 1 year, whereas gilts are issued for more than one year.

22. The Council has made use of money market funds since 2012 and will continue to use these in the year ahead. The Council uses three funds with a AAA rating and each fund has an individual cash limit of £100m. Money market funds offer access to a much larger and diverse range of the counterparties than the Council could access independently. The size of the Council's investment can be expanded or reduced on a daily basis and therefore the funds provide a very effective means of managing day-to-day liquidity. All the Funds are very large in comparison to the sums Camden has deposited with them and are monitored on a daily basis by officers.

23. Certificates of deposit (CDs) have been approved investment instruments since 2012/13 subject to sign off by the Executive Director Corporate Services and compliance with the credit rating criteria. CDs are tradable loans issued by banks and are generally issued with maturity ranging from one month to a year. Officers started using these instruments in 2015/16 and the have proved a useful means of accessing high quality counterparties. Furthermore, unlike

most investments, the Council would be able to sell out of a bank should it no longer meet the Council's risk profile or for cash flow purposes.

24. Corporate Bonds were added to the list of non-specified investments in the 2016/17 strategy. These instruments have not been used to date and will only be used in future to access banks that are eligible for inclusion on the approved lending list. They allow the Council to diversify its investments as officers may be able to use bonds when certificates of deposit or fixed term deposits are unavailable. There are also different types of bond which offer various levels of security. The Council will only use bonds that offer a level of security commensurate with traditional fixed term deposits. Any use of these instruments would need to be agreed with the Executive Director Corporate Services.

25. The Council will consider using property funds as a potential means of investing longer term cash balances. While investment in property can be made on a direct basis, the use of property funds provides a wider array of exposure to the asset class in terms of usage/type and, location, as well as efficiencies in terms of fees and maintenance and access to specialist investment managers. The authority views property as a long term investment and there are a wide range of property funds suitable for local authority investing. Appropriate due diligence will be undertaken before investment of this type is undertaken. The use of these instruments can be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. The Council will seek guidance on the status of any fund it may consider using.

TREASURY INDICATOR 6 – UPPER LIMIT FOR PRINCIPAL SUMS INVESTED FOR OVER 364 DAYS

26. A key risk inherent in investment activity is that the Council may be forced to liquidate an investment before it reaches final maturity, and thus at a time when its value may be dependent on market conditions that are unlikely to be known in advance. In order to mitigate this risk, an upper limit will be set on the total principal sums invested for periods longer than 364 days. The indicator has been calculated as 50% of expected investment balances at the end of the year (when investment balances are traditionally at the lowest level).

£m	2018/19	2019/20	2020/21
Total Investments at 31 March	114	162	85
Principal sums invested > 364 days	50	50	50

APPENDIX 4 – SPECIFIED AND NON-SPECIFIED INVESTMENTS

1. In accordance with DCLG Guidance, the investments to be used in pursuit of the investment strategy can be categorised into two types based on the following distinctions:

   - **Specified** investments will be denominated in sterling and with a maturity of no more than a year, meeting the minimum high credit quality criteria as applicable.
   - **Non-specified** investments are any investments which do not meet the specified investment criteria.

TABLE 1 – SPECIFIED INVESTMENTS

	Minimum 'High' Credit Criteria	Limit
Debt Management Agency Deposit Facility	n/a	Unlimited
Term deposits – local authorities	n/a	£40m per authority
UK Government bonds (Gilts)	UK sovereign rating	Unlimited
Treasury Bills (government bonds up to one year)	UK sovereign rating	Unlimited
Bonds issued by multilateral development banks	AAA	£40m
Certificates of deposit issued by banks and building societies	As per credit rating criteria	As per credit rating criteria
Term deposits – banks and building societies	As per credit rating criteria	As per credit rating criteria
Call accounts - banks	As per credit rating criteria	As per credit rating criteria

2. Credit rating criteria is set out in the investment strategy (table 1) along with the maximum duration of investments.

3. These limits apply to in-house investments. Should external fund managers be appointed, the same criteria will apply to funds placed under their management.

4. The following funds are also permissible under the investment strategy although they will only be used if the investment has been considered and approved by the Executive Director Corporate Services. At this stage only money market funds have been agreed for use. Any decision to invest using other funds will be reviewable by the Audit and Corporate Governance Committee and will be reported to Council as part of the Annual Report and Mid-Year Review.

TABLE 2 COLLECTIVE INVESTMENT SCHEMES STRUCTURED AS OPEN ENDED INVESTMENT COMPANIES (OEICS)

Fund Type	Minimum rating	Limit
Money market funds	Fitch AAA mmf – Stable LVNAV funds	£100m per fund
Government liquidity funds	AAA	Not set
Enhanced cash funds	AAA	Not set
Bond funds	AAA	Not set
Gilt funds	AAA	Not set

5. The below investment categories can have a time limit of any length. They have been classified as “non-specified” because of their complex nature and the level of expertise needed to enter into and monitor such transactions.

TABLE 3 Non-Specified Investments

	Minimum Credit Criteria	Cash Limit	Max. maturity period	Comment
Bank structured deposits	As per credit rating criteria	As per credit rating criteria	As per credit rating criteria	These are fixed term deposits with variable rate and variable maturities and are becoming increasingly popular. Any use will need to be sanctioned directly by the Executive Director Corporate Services.
UK Government Gilts (Primary)	As per country rating criteria	unlimited	10 years	Internally it is not expected that gilts will be used. Should a cash manager be appointed gilts would usually form part of their portfolio.
Commercial paper and corporate bonds	As per credit rating criteria	As per credit rating criteria	As per credit rating criteria	Any use of these instruments would need to be agreed with the Executive Director Corporate Services.
Certificates of deposit	As per credit rating criteria	As per credit rating criteria	As per credit rating criteria	The use of these has been agreed and they now form part of the council’s investment portfolio.
Multilateral development bank bonds	AA-, F1+ (and equivalent from other agencies)	£40m for any one counterparty	As per credit rating criteria	The use of these has been agreed and they now form part of the council’s investment portfolio.

Floating Rate Notes	As per credit rating criteria		As per credit rating criteria	Any use of these instruments would need to be agreed with the Executive Director Corporate Services.
Local authority mortgage guarantee scheme				Any use of these instruments would need to be agreed with the Executive Director Corporate Services.
Term deposits - local authorities (1 - 5 Years)	n/a	As per credit rating criteria	5 years	Any use of these instruments would need to be agreed with the Executive Director Corporate Services.
Property funds (the use of which may constitute capital expenditure)	UK property only	£20m per fund	None	Any use of these instruments would need to be agreed with the Executive Director Corporate Services.

6. The Council benchmarks its returns against other local authorities. In London the return on participating Council Treasury portfolios was 0.83% and at that time Camden had a return of 0.74%. The London group has council's which are able to take a much longer term approach to borrowing given core cash balances (an average of over 4 months duration) whereas Camden's cash flow means our average duration is 3 months. Our credit risk however is lower than the London group's.

APPENDIX 5 - MINIMUM REVENUE PROVISION POLICY

1. For local authorities depreciation on fixed assets is a notional charge which gets reversed out of the accounts and in its place a 'minimum revenue provision' is charged (MRP). Fixed assets (capital spend) are funded from a number of sources including borrowing. Traditionally MRP has been based upon depreciating the CFR (the Council's underlying need to borrow) over 25 years.

2. MRP is governed by regulations that came into force in February 2008 (for the General Fund) which give local authorities flexibility in how they calculate MRP, providing the calculation is 'prudent'. In calculating a prudent provision, local authorities are required to have regard to guidance issued by the Secretary of State. Local Authorities have a duty to "determine for the current financial year an amount of MRP which it considers prudent". In principle councils must arrange for debt liabilities to be repaid over a period commensurate with asset lives.

3. The Guidance stated that before the start of each financial year a local authority should prepare a statement of its policy on making MRP in respect of that financial year and submit it to full Council for approval. This should sit alongside reports on Prudential borrowing limits and the Treasury Management Strategy. In the guidance, options 1 and 2 deal with debt which is supported by the government through the grant system, whilst options 3 and 4 deal with new borrowing under the prudential system, for which no support is given.

Option 1: Regulatory Method

4. For debt which is supported by the government through the grant system authorities may continue to use the formula (4% on the reducing balance) in the current regulations, since the Revenue Support Grant is calculated on that basis. Although the existing regulation 28 is revoked by regulation 4(1) of the 2008 Regulations, authorities will be able to calculate MRP as if it were still in force. Regulations issued in 2007 did away with the application of the adjustment to the calculation known as Adjustment A and it is proposed to continue to exclude this factor from the MRP calculations. **Option 2** is the same as option 1 but does not deduct Adjustment A.

Option 3 – Asset Life method

5. For new borrowing under the prudential system, option 3 is to make provision over the estimated life of the asset for which borrowing is undertaken. Camden uses the equal instalment method for existing borrowing (there are options around annuity depreciation) and it is proposed that this continues. It is also intended that for future schemes funded in this way, as permitted under the regulations, that MRP will not be charged until the year after the asset comes into service. Option 4 aims to provide depreciation taking into account residual value, impairment and revaluations.

MRP Policy for Camden

6. For 2019/20 it is proposed that the Council continues its policy and adopts Option 1 for supported borrowing and Option 3 for borrowing under the prudential system. The Council will not deduct ‘Adjustment A’.

7. The Council will also continue to credit, where possible, unapplied capital receipts to the Capital Adjustment Account which has the effect of reducing the General Fund CFR until such time as the capital receipts are used to fund capital expenditure. From 2020/21 onwards, as capital receipts are needed to fund the capital programme, the MRP will rise. The estimated MRP for **2019/20**, excluding PFI and finance leases, is shown below alongside the latest estimate for 2017/18.

As at Month 8, November 2018	**2018/19 £m**	**2019/20 £m**
Supported borrowing (MRP) Prudential borrowing	0.998 2,299	0.477 2.323
Minimum Revenue Provision	**3.297**	**2.800**

As at Month 9, December 2018	**2018/19 £m**	**2019/20 £m**
Supported borrowing (MRP) Prudential borrowing	0.998 2,299	1.429 2.323
Minimum Revenue Provision	**3.297**	**3.752**

Note: mth 9 table includes MTFS investment projects that would help generate revenue savings, slippage and overall reduction in forecasted capital receipts. As the capital receipts have been delayed and ultimately reduced there will not be the same level of resources to transfer to the capital adjustment account to reduce the CFR as previously envisaged – resulting in higher MRP in future years.