TREASURY MANAGEMENT STRATEGY STATEMENTS, MRP STRATEGY AND ANNUAL INVESTMENT STRATEGY 2019/20

INTRODUCTION

1. Background

1.1. The council is required to operate a balanced budget and in pursuit of this objective, the council operates a treasury management function which incorporates the management of the council's cash flows, lending and borrowing activities and the control management and mitigation of the risks associated with these activities. The borrowing also facilitates the funding of the council's capital programme.

1.2. The Council's 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. If the right circumstances prevail debt previously drawn may be restructured to meet Council risk or cost objectives.

1.3. 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 maintain the balance between the interest costs of debt and the investment income arising from cash deposits to manage 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

1.4. Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day to day treasury management activities.

1.5. 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."

1.6. 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 requirement for all local authorities to have 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 especially using the 'General Powers of Compentency' provision. The capital strategy is being reported separately, though the key prudential indicators will be retained within this document.

2. Reporting requirements

2.1. The CIPFA revised 2017 Prudential and Treasury Management Codes requires, 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

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

2.3. Ealing's existing Capital Strategy and Treasury Management Strategy have been reviewed to ensure compliance with the updated requirements across the two strategies.

2.4. Non-treasury investments are reported through the Capital Strategy. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset. The capital strategy shows:

- The corporate governance arrangements for these types of activities;
- Any service objectives relating to the investments;
- The expected income, costs and resulting contribution;
- The debt related to the activity and the associated interest costs;
- The payback period (MRP policy);
- For non-loan type investments, the cost against the current market value;
- The risks associated with each activity.

Of the above, the expected income, costs and resulting contribution, the debt related to the activity and the associated interest costs, and the MRP policy are included in the Treasury Management Strategy. Ealing's existing Capital Strategy has been reviewed and updated to ensure full compliance with the Codes' requirements.

2.5. Where a physical asset is being bought for investment purposes, details of market research, advisers used, (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

2.6. Where the Council has borrowed to fund any non-treasury investment, there should also be an explanation of why borrowing was required and why the MHCLG Investment Guidance and CIPFA Prudential Code have not been adhered to.

2.7. If any non-treasury investment sustains a loss during the final accounts and audit process, the strategy and revenue implications will be reported through the same procedure as the capital strategy.

2.8. To demonstrate the proportionality between the treasury operations and the non-treasury operation, high-level comparators are shown throughout this report.

3. <u>Treasury Management Reporting</u>

TREASURY MANAGEMENT STRATEGY 2019/20

3.1. The Local Government Act 2003 (the Act) and supporting regulations requires the council to 'have regard to' the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code (Prudential Code) and the CIPFA Treasury Management Code of Practice (Treasury Code) to set prudential and treasury indicators for the next three years to ensure that the council's capital investment plans are affordable, prudent and sustainable.

3.2. In pursuit of the above the council must produce as a minimum three key treasury reports:

- Treasury Strategy, prudential and treasury indicators, a requirement fulfilled by the production of this report. The report covers:
  - capital plans (including prudential indicators),
  - minimum revenue provision (MRP) policy,
  - the treasury management; and
  - an investment strategy.
- A mid-year report which updates members on treasury progress, the capital position, the prudential indicators and whether any strategies or policies require revision
- An annual treasury outturn report.

3.3. Council approves the Treasury Strategy as part of the annual budget-setting process. This appendix sets out the Treasury Strategy for 2019/20.

3.4. The scrutiny of the treasury management function within the council is undertaken by Audit Committee, which carries out quarterly reviews.

3.5. The council is also required to comply with investment guidance issued by the Department of Communities and Local Government which came into effect from 1 April 2010. The council's investment strategy is compliant with the newly revised MHCLG investment guidance.

3.6. The Treasury Code (revised November 2011) was adopted by Council on the 9 March 2010. This strategy report now complies with the revised 2017 Treasury Management Code of Practice.

3.7. In addition to the reporting schedule outlined above the code requires the:

- Creation and maintenance of a treasury management policy statement which sets out the policies and objectives of the council's treasury management activities. The Treasury Management Policy Statement is attached for reapproval as Annex 1.
- Creation and maintenance of Treasury Management Practices which set out the manner in which the council will seek to achieve those policies and objectives; these are maintained and kept under review by officers.
- Delegation by the council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions. The scheme of delegation is attached as Annex 2.

3.8. The council complies with the above and its governance process is strengthened by its Treasury Risk and Investment Board (TRIB), which meets regularly to support the Director of Finance in the execution of their delegated powers.

TREASURY MANAGEMENT STRATEGY 2019/20

1. Treasury Management Strategy for 2019/20

1.1 The Strategy for 2019/20 addresses capital plans, prudential indicators, minimum revenue provision (MRP) and other treasury management issues such as the investment strategy and creditworthiness policy.

1.2 The proposed Treasury Management Strategy and Policy for the remainder of 2018/19 and for financial year 2019/20 adheres to the council's policy on investments of "safety before returns" and investments are currently being placed with the following:

- The UK government directly (Debt Management Office)
- RBS (largely buffered by the UK government's stake in this institutions)
- The council's banker (Lloyds Bank)
- HSBC
- Nationwide
- Barclays
- Other local authorities; and
- Money Market Funds (note regulatory changes to MMFs introduced from 21 January 2019)

Money Market Funds (MMFs)

1.3 A number of MMF's faced difficulty during the global financial crisis hence the European Commission proposed new rules to safeguard investors. This process began in 2013 and was finally approved by the various regulatory bodies in November 2016 with the rules coming into effect from January 2019 for existing MMFs.

Summary of New Rules

1.4 The new regulations mainly focus on the structure, composition, liquidity requirements, Liquidity fees, redemption gates and understanding investor behaviour and information reporting. MMF's will now be categorised into (a) Short Term MMF's and Standard MMF's with three structural options within these two categories per below.

Structural Options	Short-Term Money Market Funds	Standard Money Market Funds
Government Constant Net Asset Value (CNAV)	X	
Low Volatility Net Asset Value (LVNAV) - NEW	X	
Variable Net Asset Value (VNAV)	X	X

1.5 To date European MMF's had CNAV and VNAV funds and the Council only used CNAV funds. CNAV funds have now been restricted to government portfolios while a new structural option for non government funds, the Low Volatility NET Asset Value (LVNAV) MMF has been introduced.

1.6 The LVNAV MMF still allows investors to purchase and redeem at stable NAV to two decimal places provided the fund is managed to certain maturity and liquidity constraints. If these constraints are breached the funds must be values at mark to market. The board of the MMF also have powers to take protective action in times of market stress or when more than 10% of the fund is redeemed in one day. These include gating or restricting the amount that can be drawn down in one day and levying liquidity fees on investors.

1.7 Currently the Council will restrict its use of MMF's to CNAV and LVNAV funds although the strategy gives the authority to use VNAV MMF should this be deemed appropriate at a future date.

1.8 The strategy proposed in this report will assist the council in mitigating risk in the council's treasury management activities and allow the borrowing necessary to finance the capital programme.

1.9 The proposed strategy for 2019/20 is based upon treasury officers' views on interest rates, market forecasts acquired directly by council officers and supplemented by forecasts provided by the council's treasury advisors, Link Asset Services.

1.10 The strategy report covers:

- Update on Pension Fund and West London Waste Authority cash (para 1.14 to 1.18)
- Capital Plans and Prudential Indicators (para 2 and Annex 3)
- Minimum Revenue Provision (MRP) Policy (para 3 and Annex 4)
- Borrowing (para 5)
- Treasury Limits for 2018/19 to 2020/21 (para 6)
- Economic Background (para 7)
- Borrowing Strategy including borrowing in advance of need (para 8)
- Debt Rescheduling (para 9)
- Housing Revenue Account (HRA) Self Financing (para 10)
- Annual Investment Strategy (para 11 and Annex 5)
- Financial Implications (para 12)
- Balanced Budget Requirement (para13)
- Treasury Management Policy Statement (Annex 1)
- Scheme of Delegation (Annex 2)
- Prudential Indicators (Annex 3)

1.11 These factors embrace the requirements of the Local Government Act 2003, the CIPFA Prudential Code, MHCLG MRP Guidance, the CIPFA Treasury Code and MHCLG Investment Guidance.

Training

1.12 The Treasury Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training on treasury management and related issues. This especially applies to Members responsible for scrutiny, who regularly receive training on the subject by the council. Audit Committee members are due to receive training on 6th March 2019. The training needs of treasury management officers are met through attendance at relevant courses, conferences and forums and are periodically reviewed and addressed as part of the council's appraisal scheme.

Treasury Management Consultants

1.13 The council uses Link Asset Services, 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. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers. 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.

Pension Fund Cash

1.14 The council's arrangement for pension fund cash changed from 1 April 2011 to meet the requirements of CLG regulations. In the past all pension fund transactions flowed through the Council's main bank account with monthly transfers to and from the Pension Fund Bank account to manage surplus and deficit cash positions. However, a new Pension Fund entity has now been set up on the Council's ledger system, to enable comprehensive and ring fenced use of the pension fund bank account (pension payments and income now flow through Pension Fund Account Bank Account). As part of the new process, any money due to/owed by Pension Fund to the Council is now treated as a Debtor/Creditor and cash transfers are made to/from Pension Bank Account for settlement and therefore there is no more requirement for monthly cash transfers. All surplus Pension Fund cash will continue to be transferred monthly to the Custodian's (BNY Mellon) bank account where it is swept for overnight investment into a money market bank account. Pension Fund cash retained locally to manager cash flow will be invested in either the pension fund MMF or fixed term deposits.

1.15 The council is responsible for managing the pension fund cash (that may remain in house) in accordance with this Treasury Management Strategy. The Pension Fund Panel is updated of progress on a quarterly basis.

West London Waste Authority (WLWA) Cash

1.16 From 1 April 2014, the London Borough of Ealing started to carry out treasury management services for the WLWA. There are significant benefits in the WLWA engaging with one of the boroughs to provide treasury management services on their behalf.

1.17 During 2018/19 WLWA transferred their excess funds to the council to be invested jointly. They will earn the average interest rate achieved by the council based on their average balance. The WLWA has also subscribed to Link Asset Management Services and they will mirror the council's investment strategy.

1.18 The performance of the treasury management service will be reviewed on an annual basis. The annual charge for the WLWA using Ealing's treasury management services has been agreed for 2018/19 at £7,500 and the current service contract will run to 2019/20.

MIFID II

1.19 As reported in previous year, on the 3rd of January 2018, the EU Market in Financial Instruments Directive II (MiFID II) came into effective which requires regulated bodies to classify Local Authorities as retail clients, unless they provide evidence that they should be opted up to 'professional client' status.

1.20 The council has opted up to 'professional client' categorisation with all brokers and counterparties. In order to achieve this, the authority had to provide evidence that it held an investment balance of at least £10 million and that the person(s) authorised to make investment decisions on behalf of the authority has at least one year's relevant professional experience. The London Borough of Ealing currently meets these criteria and training needs will be regularly monitored to ensure compliance

2. Prudential Indicators

2.1. The Local Government Act 2003 and supporting regulations requires the council to 'have regard to' the Prudential Code and to set Prudential Indicators for the next three years to ensure that the council's capital investment plans are affordable, prudent and sustainable.

2.2. Ealing's Prudential Indicators for the period 2019/20 – 2021/22 are set out in Annex 3 and council is asked to approve these.

2.3. The benefit of the indicators will be derived from monitoring them over time rather than from the absolute value of each. A reporting process has been established, with a mid-year report to council to highlight any significant deviations from expectations. The indicators can be amended and reported to council for approval at the earliest opportunity.

2.4. The indicators for later years are broad estimates since a number of factors including the level of government support beyond 2019/20 are unconfirmed. These estimates will be revised, as more accurate information becomes available.

3. Minimum Revenue Provision (MRP) Policy Statement

3.1. Council is recommended therefore to approve the MRP policy statement as set out in Annex 4.

4. Core funds and expected investment balances

4.1. The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Outlined below are estimates of the year end balances on investments.

Table 1 – Estimate of year End Balance

Year End Resources	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
Expected investments	127	128	117	117	117

Affordability Prudential Indicators

4.2. 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. Council is asked to approve the indicators as set out in Annex 3.

5. Borrowing

5.1. The capital expenditure plans set out in this appendix outline the service activity for the council. The treasury management function ensures that the council adheres to the relevant treasury codes of practice as well as organising the council's cash flow and borrowing needs to meet the requirements of the service activity. It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the council to produce a balanced budget. In particular, Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This therefore means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from:

- increases in interest charges caused by increased borrowing to finance additional capital expenditure, and
- any increases in running costs from new capital projects are limited to a level which is affordable, prudent and sustainable within the projected income of the council for the foreseeable future.

5.2. The strategy covers the relevant treasury/prudential indicators, the current and projected debt positions and the annual investment strategy.

5.3. The council's current treasury portfolio position is set out in table 2 below:

Table 2 – Council's treasury portfolio position at 31 December 2018

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
External Debt					
Debt at 1 April	495.438	529.045	576.311	619.609	657.880
Expected change in Debt +/-	33.607	47.266	43.298	38.271	32.266
Actual gross debt at 31 March	**529.045**	**576.311**	**619.609**	**657.880**	**690.147**
The Capital Financing Requirement (CFR)	**656.285**	**687.858**	**809.942**	**885.633**	**919.113**
Under / (Over) borrowing	**127.241**	**111.547**	**190.334**	**227.753**	**228.966**
Other long-term liabilities (OLTL)	126.059	120.136	115.185	110.505	105.463
Expected change in OLTL	- 5.924	- 4.950	- 4.681	- 5.042	- 4.944
OLTL Total	**120.136**	**115.185**	**110.505**	**105.463**	**100.519**

Note: the table shows the impact of not externally borrowing i.e. using the council's investments to internally fund the council's underlying borrowing and this policy is under constant review.

Within the above figures the level of debt relating to commercial activities / non-financial investment is:

Table 3 – External Debt for commercial activities / non-financial investments

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
Actual debt at 31 March £m	25.171	33.264	73.044	113.917	148.192
Percentage of total external debt %	5%	6%	12%	17%	21%

Within the range of 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 Director of Finance reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

6. Treasury Limits for 2019/20 to 2021/22

6.1. It is a statutory duty under Section 3 of the Act and supporting regulations for the council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the "Affordable Borrowing Limit". In England and Wales the Authorised Limit represents the legislative limit specified in the Act.

6.2. The council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax and council rent levels is 'acceptable'.

6.3. Whilst termed an "Affordable Borrowing Limit", the capital plans to be considered for inclusion incorporating financing by both external borrowing and other forms of liability, such as credit arrangements. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years, details of the Authorised Limit is set out in Annex 3.

7. Economic Background and Interest Rate Forecasts

7.1. Link Asset Services has been appointed as treasury adviser to the council and part of its service is to assist the council to formulate a view on interest rates. The following table outlines the Link view. It should be noted that the Public Works Loans Board (PWLB) offers a certainty rate discount of 0.20% to local authorities who provide specified information on their plans for capital spending and the associated longer term borrowing. The council has applied and qualifies to borrow at the certainty rate.

Table 4 – Link Interest Rate Forecast

Rate	Mar-19 %	Jun-19 %	Sep-19 %	Dec-19 %	Mar-20 %	Mar-21 %	Mar-22 %
Bank of England	0.75	1.00	1.00	1.00	1.25	1.50	2.00
5yr PWLB	2.10	2.20	2.20	2.30	2.30	2.60	2.80
10yr PWLB	2.50	2.60	2.60	2.70	2.80	3.00	3.20
25yr PWLB	2.90	3.00	3.10	3.10	3.20	3.40	3.60
50yr PWLB	2.70	2.80	2.90	2.90	3.00	3.20	3.40

7.2. The interest rate forecasts provided by Link Asset Services in Table 3 are predicated on an assumption of an agreement being reached on Brexit between the UK and the EU. In the event of an orderly non-agreement exit, it is likely that the Bank of England would take action to cut Bank Rate from 0.75% in order to help economic growth deal with the adverse effects of this situation. This is also likely to cause short to medium term gilt yields to fall. If there was a disorderly Brexit, then any cut in Bank Rate would be likely to last for a longer period and also depress short and medium gilt yields correspondingly. It is also possible that the government could act to protect economic growth by implementing fiscal stimulus.

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

7.4. One risk that is both an upside and downside risk, is that all central banks are now working in very different economic conditions than before the 2008 financial crash as there has been a major increase in consumer and other debt due to the exceptionally low levels of borrowing rates that have prevailed for ten years since 2008. This means that the neutral rate of interest in an economy, (i.e. the rate that is neither expansionary nor deflationary), is difficult to determine definitively in this new environment, although central banks have made statements that they expect it to be much lower than before 2008. Central banks could therefore either over or under do increases in central interest rates.

7.5. Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- Brexit – if it were to cause significant economic disruption and a major downturn in the rate of growth.
- Bank of England monetary policy takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- A resurgence of the Eurozone sovereign debt crisis, possibly in Italy, due to its high level of government debt, low rate of economic growth and vulnerable banking system.
- Weak capitalisation of some European banks.
- Further increases in interest rates in the US
- Concerns around the level of US corporate debt
- Geopolitical risks

7.6. Upside risks to current forecasts for UK gilt yields and PWLB rates

- Brexit – if both sides were to agree a compromise that removed all threats of economic and political disruption.
- The Fed causing a sudden shock in financial markets through misjudging the pace and strength of increases in its Fed.
- The Bank of England is too slow in its pace and strength of increases in Bank Rate and, therefore, allows inflation pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.
- UK inflation returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

8. Borrowing Strategy 2019/20

8.1. The Council's strategy is to achieve a low but stable cost of finance, but retaining flexibility to alter its plans as circumstances change. In this regards, the council is currently maintaining an under-borrowed position, hence financing schemes through internal borrowing. This means that the capital borrowing need (the Capital Financing Requirement - CFR), has not been fully funded with loan debt as cash supporting the council's reserves, balances and cash flow is being deployed in the interim. This strategy is prudent as investment returns are low and counterparty risk is relatively high.

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

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

Sensitivities of the forecast

8.4. If Officers' felt there was a significant risk of a sharp fall in long and short term interest 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. However, if there was a significant risk of a much sharper rise in long and short term rates than that currently forecast, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be raised whilst interest rates are still lower than they will be in the foreseeable years ahead. Any decisions and actions taken will be reported to Audit Committee or Council at the earliest opportunity.

8.5. The council's borrowing strategy will give consideration to new borrowing in the following order of priority:

- The cheapest borrowing will be internal borrowing by proactively using cash balances that arise through timings difference of receipts and payments plus balances for reserves and foregoing interest earned which is currently at historically low rates. However, if the overall forecast for long term borrowing rates were to be a projected increase over the next few years, consideration will also be given to weighing the short term advantage of internal borrowing against potential long term costs if the opportunity is missed for taking loans at long term rates which will be higher in future years.
- Temporary borrowing from the money markets or other local authorities
- PWLB variable rate loans for up to 10 years
- Short dated borrowing from non PWLB and other sources
- Long term fixed rate market loans at rates significantly below PWLB rates for the equivalent maturity period (where available) and to maintaining an appropriate balance between PWLB and market debt in the debt portfolio.

- PWLB borrowing for periods across all the durations when rates are seen as being at particularly good value.

8.6. The council will continue to borrow in respect of the following:

- Maturing debt (net of minimum revenue provision).
- Approved unsupported (prudential) capital expenditure.
- To finance cash flow in the short term.

8.7. The type, period, rate and timing of new borrowing will be determined by the Director of Finance under delegated powers, taking into account the following factors:

- Expected movements in interest rates as outlined above.
- Current maturity profile.
- The impact on the medium term financial strategy.
- Prudential indicators and limits.

Treasury Management Limits on borrowing Activity

8.8. There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within a flexibly set remit, to managing risk, yet not impose undue restraints that constrain cost reduction or performance improvement. The indicators are:

- Upper limits on variable interest rate exposure net of investments.
- Upper limits on fixed interest rate exposure;
- Maturity structure of borrowing to manage refinancing risk.

8.9. The proposed indicators are set out in Annex 3.

Policy on borrowing in advance of need

8.10. The council needs to ensure that its total debt, does not, except in the short term, exceed the total of the CFR in the preceding year i.e. 2018/19 plus the estimates of any additional CFR for the year 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 purposes.

8.11. Any decision to borrow in advance will be considered carefully to ensure value for money can be demonstrated and that the council can ensure the security of such funds.

8.12. Borrowing in advance of need will be limited to no more than 70% of the expected increase in borrowing need (CFR) over the three year planning period. In determining whether borrowing will be undertaken in advance of need the council will:

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow
- consider the merits and demerits of alternative forms of funding
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use
- consider the pros and cons of the impact of borrowing in advance of need at attractive rates on the available cash balances the council will hold and the risks associated with increased exposure to credit risk arising from investing this additional cash in advance of need.

9. Debt Rescheduling

9.1. 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 to be 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. Any such rescheduling and repayment of debt is likely to cause a flattening of the council's maturity profile as in recent years there has been a skew towards longer dated PWLB.

9.2. 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 strategy outlined above
- enhancing the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

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

9.4. All rescheduling will be reported to Council at the earliest meeting following its implementation.

10. Housing Revenue Account (HRA) Self Financing

10.1. The housing subsidy system was dismantled and replaced by a system of self-financing of the HRA from 1 April 2012. Since then, two separate pools are operating for the management of HRA and GF debt.

10.2. Under the two pool approach legacy loans were notionally apportioned between the HRA and general fund using the CFR split and future loans have been raised separately.

10.3. An equitable means of apportioning debt management expenses is in operation

10.4. Until October 2018, HRA borrowing was capped by the government and the HRA needed to borrow within the parameters of its existing debt and the cap known as the headroom. In October 2018, the Government approved plans to remove the HRA borrowing cap, giving local authorities the flexibility to borrow up to levels that can be supported through their revenue streams.

11. Annual Investment Strategy

11.1. The annual investment strategy is set out in Annex 5 for approval by Council. This covers:

- Overview including durations bans for counterparties and minimum credit ratings (tables 1 and 2 of Annex 5)
- Policy lending – non treasury management investments
- Investment balances / liquidity of investments
- Specified / unspecified investments

12. Financial Implications

12.1. Investment income is currently forecast to be £0.91m for 2018/19, which is higher than the budgeted £0.36m. For 2019/20 budgeted investment income is estimated at approximately £0.78m to reflect lower expected investment levels.

12.2. Savings on debt servicing costs have accrued because only a proportion of the borrowing scheduled to be made in 2018/19 was actually raised.

13. Balanced Budget Requirement

13.1. The council complies with the provisions of S32 of the Local Government Finance Act 1992 to set a balanced budget.

13.2. Risk management plays a fundamental role in treasury activities due to the value and nature of transactions involved. In order to mitigate risks on investment income the council holds a business risk reserve, which can be used to manage unforeseen volatility of investment income or borrowing costs.

13.3. Budgeting for MRP requires the council to make provision for MRP linked to the life of the assets being enhanced. This makes budgeting for MRP more complex and sensitive to changes in assets being financed and the amount on unsupported borrowing used.

13.4. MHCLG recently issued new regulations and guidance on MRP set aside:

13.5. The key changes are that:

- The option to calculate MRP in retrospect thereby creating a credit or a reduction in MRP for future years is now closed, though the ability to reset a provision prospectively still remains. Any changes should use the residual CFR at that point in time

- MRP should not be £nil in any year – unless CFR is nil or negative or a Voluntary MRP is being clawed back

- Maximum asset life is 50 years unless supported by expert opinion

- Where the asset life methodology option 3 is being used the new guidance is prescriptive on the maximum number of years over which the type of expenditure can be written off. In the absence of a quantifiable asset life 25 years is considered the reasonable default.

13.6. Loans to third parties

13.7. Expenditure on policy loans to third parties which constitute capital expenditure must have MRP set aside. In the past it was possible to justify not setting aside MRP for some investments as any borrowing would be repaid by selling the assets sometime in the future; this will not now be possible meaning MRP will need to be set aside for these assets.

13.8. As before repayments included in annual PFI or finance leases are applied as MRP. There is no requirement for the HRA to set aside MRP, although there is a requirement for depreciation to be applied.

13.9. Acquisition of share capital can be written off over a maximum of 20 years.

ANNEX 1 - TREASURY MANAGEMENT POLICY STATEMENT

The London Borough of Ealing defines the policies and objectives of its treasury management activities as follows: -

(i) This organisation defines its treasury management activities as:
"The management of the authority's 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".

(ii) This organisation regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.

(iii) This organisation acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving best value in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management."

ANNEX 2 - TREASURY MANAGEMENT SCHEME OF DELEGATION

The London Borough of Ealing's Treasury Management Scheme of Delegation is approved by Full Council annually as part of the overall Treasury Management Strategy, it was last approved by Council at its meeting of 13 February 2018 and there are no proposals for any amendments to the current scheme, which is set out below:

1. Council

- receiving and reviewing reports on treasury management policies, practices and activities
- approval of/amendments to the organisation's adopted clauses, treasury management policy statement
- approval of annual strategy.

2. Section 151 Officer/ Director of Finance

- budget consideration and approval
- approval of the division of responsibilities
- receiving and reviewing regular monitoring reports and acting on recommendations
- approving the selection of external service providers and agreeing terms of appointment.

3. Audit Committee

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

14. The treasury management role of the section 151 officer is to:

- recommend clauses, treasury management policy for approval, hold regular reviews, and monitor compliance
- formulate consulting on and approving the treasury management practices, outlining the detailed manner in which the treasury management function will operate
- submit regular treasury management policy reports
- submit budgets and budget variations
- receive and review management information reports
- review the performance of the treasury management function
- ensure the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensure the adequacy of internal audit, and liaising with external audit
- recommend the appointment of external service providers.

TREASURY MANAGEMENT STRATEGY 2019/20

ANNEX 3 - PRUDENTIAL INDICATORS

1 Capital Prudential Indicators

1.1 The council's capital expenditure plans are a key driver of treasury management activity.

Capital Expenditure

1.2 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:

Table 1: Capital Expenditure Forecast

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
Non-HRA	87.015	86.392	99.398	57.289	25.483
HRA	85.983	91.098	107.068	87.684	67.230
Commercial activities/ non-financial investments *	8.754	8.093	39.780	40.873	34.275
Total	**181.752**	**185.583**	**246.246**	**185.846**	**126.988**

* Commercial activities / non-financial investments relate to areas such as capital expenditure on investment properties, loans to third parties etc. This figure currently comprises policy loans to Broadway Living.

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

1.4 Table 2 outlines how the capital expenditure plans are proposed to be financed by capital or revenue resources. Any shortfall of resources results in a funding need i.e. borrowing.

Table 2: Capital Programme Funding Summary

Capital Expenditure	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
Non-HRA	87.015	86.392	99.398	57.289	25.483
HRA	85.983	91.098	107.068	87.684	67.23
Commercial activities/ non-financial investments *	8.754	8.093	39.78	40.873	34.275
Total	**181.752**	**185.583**	**246.246**	**185.846**	**126.988**
Financed by:					
Capital receipts					
Capital grants	47.516	39.061	26.877	15.556	8.250
Revenue Contribution	6.435	1.861	1.856	0.000	0.000
Other: Parking Reserve; Invest to Save; Partnership; S106	0.937	8.336	6.339	6.413	0.000
Finance Lease Liability					
PFI					
Total Financed	**54.888**	**49.258**	**35.072**	**21.969**	**8.25**
HRA Direct funding	**71.528**	**91.098**	**74.056**	**71.267**	**67.230**
Net Financing Need	**55.336**	**45.227**	**137.118**	**92.610**	**51.508**
TOTAL FUNDING	**181.752**	**185.583**	**246.246**	**185.846**	**126.988**

Table 3: New borrowing made up as follows:

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
New Year Borrowing HRA	14.455	0	33.012	16.417	0
New Year Borrowing GF	32.127	37.134	64.326	35.32	17.233
New Year Borrowing Commercial activities/ non-financial investments	8.754	8.093	39.780	40.873	34.275
Total borrowing	**55.336**	**45.227**	**137.118**	**92.61**	**51.508**

Table 4: Commercial activities / non-financial investments

Commercial activities / non-financial investments £m	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Capital Expenditure	8.754	8.093	39.78	40.873	34.275
Financing costs	0.223	0.327	0.949	1.998	2.975
Net financing need for the year	**55.336**	**45.227**	**137.118**	**92.610**	**51.508**
Percentage of total net financing need %	**16%**	**18%**	**29%**	**44%**	**67%**

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

1.5 This prudential indicator is the council's capital financing requirement (CFR), which is simply the total historic unfinanced capital expenditure i.e. a measure of the council's underlying borrowing need. Any capital expenditure not immediately paid for, will increase the CFR. The requirement to set aside the minimum revenue provision (MRP) reduces the council's underlying need to borrow and the ensuing CFR.

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

1.7 The CFR includes any other long-term liabilities (e.g. PFI schemes, finance leases) brought onto the balance sheet. Whilst these increase the CFR, and therefore the council's borrowing requirement, these types of scheme include a borrowing facility and so the council is not required to separately borrow for these schemes. The council currently has £120.136m of such schemes that forms part of the CFR.

1.8 The Council is asked to approve the CFR projections below:

Table 5: CFR Projections - Capital Financing Requirement

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
CFR – non housing	468.313	491.793	541.201	560.286	560.758
CFR – housing	162.801	162.801	195.813	212.230	212.230
CFR - Commercial activities/ non-financial investments	25.171	33.264	72.929	113.118	146.125
Total CFR ex OLTL	**656.285**	**687.858**	**809.942**	**885.633**	**919.113**
OLTL	120.136	115.185	110.505	105.463	100.519
Total CFR inc. OLTR	**776.421**	**803.044**	**920.447**	**991.096**	**1,019.631**
Movement in CFR	**37.646**	**26.623**	**117.403**	**70.649**	**28.536**

Table 5a: Movement in CFR inc OLTL represented by:

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
Net financing need for the year	55.336	45.227	137.118	92.61	51.508
Less MRP/VRP* and other financing movements	-17.690	-18.604	-19.715	-21.961	-22.972
Movement in CFR	**37.646**	**26.623**	**117.403**	**70.649**	**28.536**

*Voluntary Revenue Provision

1.9 A key aspect of the regulatory and professional guidance is that elected members are aware of the size and scope of any commercial activity in relation to the authority's overall financial position. The capital expenditure figures shown in 2.1 and the details above demonstrate the scope of this activity and, by approving these figures, consider the scale proportionate to the Authority's remaining activity.

1.10 Under the capital finance regulations, local authorities are permitted to borrow up to three years in advance of need. This council will only consider borrowing in advance of need if market conditions indicate that it is the best course of action. One of the reasons for borrowing in advance is to take advantage of and lock in low long term interest rates, especially if officers are of the opinion that long term rates are likely to rise. There is a short term carry cost to borrowing in advance of need as currently investment rates are considerably lower than long term borrowing rates. Borrowing in advance of need also increases the level of temporary investments and thus increases the exposure to loss of investment principal. However, the council has put in place a prudent methodology to minimise this risk.

2 Affordability Prudential Indicators

2.1 **Actual and estimates of the 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.

Table 6: Ratio of financing costs to revenue streams

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	%	%	%	%	%
Non-HRA	9.44%	11.02%	12.24%	12.30%	12.74%
HRA (inclusive of settlement)	9.05%	9.47%	9.85%	11.22%	9.95%
Commercial activities / non-financial investments	9.44%	11.02%	12.24%	12.30%	12.74%

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

Table 7: HRA Ratios

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
HRA debt (£m)	162.801	162.801	195.813	212.230	212.230
HRA debt cap* (£m)	205.076	213.116	215.010	215.010	215.010
HRA revenues (£m)	66.342	68.362	68.687	69.767	72.596
Ratio of debt to revenues %	40.75%	41.99%	35.08%	32.87%	34.21%

**The HRA debt cap was abolished from 29.10.2018. The figures included are indicative and for information only*

	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
HRA Debt (£m)	162.801	162.801	195.813	212.230	212.230
Number of HRA Dwellings	12,007	12,011	11,517	10,845	10,639
Debt per dwelling (£)	13,559	13,554	17,002	19,569	19,948

3 Treasury Indicators: Limits to Borrowing Activity

The Operational Boundary

3.1 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.

Table 8 – Treasury Indicators Limits on borrowing activity

Operational Boundary – General Fund & HRA	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	£m	£m	£m	£m
Debt	631.114	654.594	737.014	772.515	772.988
Other long term liabilities	120.136	115.185	110.505	105.463	100.519
Commercial activities/ non-financial investments	25.171	33.264	72.929	113.118	146.125
Total	**776.421**	**803.044**	**920.447**	**991.096**	**1,019.631**

The Authorised Limit for external debt

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

3.3 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.

3.4 The council is asked to approve the following Authorised Limit:

Table 9 – Authorised Limits

Authorised limit - General Fund & HRA	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	**£m**	**£m**	**£m**	**£m**
Debt	661.114	684.594	767.014	802.515	802.988
Other long term liabilities	120.136	115.185	110.505	105.463	100.519
Commercial activities/ non-financial investments	25.171	33.264	72.929	113.118	146.125
Total	**806.421**	**833.044**	**950.447**	**1021.096**	**1049.631**

3.5 Separately, the council is also limited to a maximum HRA CFR through the HRA self-financing regime. This limit is currently:

Table 10 – HRA Debt limit

HRA Debt Limit	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
	£m	**£m**	**£m**	**£m**	**£m**
HRA debt cap	205.076	213.116	215.01	215.01	215.01
HRA CFR	162.801	162.801	195.813	212.230	212.230
HRA headroom	**42.275**	**50.315**	**19.197**	**2.780**	**2.780**

The HRA debt cap was abolished from 29.10.2018. The figures included are indicative and for information only

3.6 In light of the recent changes to the HRA debt cap, the council is reviewing the HRA borrowing limits and will report back to Council at a later date.

Table 11 – Treasury Indicators and limits

	2018/19	2019/20	2020/21
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	50	50	50
Limits on fixed interest rates:			
• Debt only	100	100	100
• Investments only	100	100	100
Limits on variable interest rates			
• Debt only	50	50	50
• Investments only	100	100	100

TREASURY MANAGEMENT STRATEGY 2019/20

ANNEX 4 – MRP POLICY STATEMENT

1 The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 require the Council to determine for the current financial year an amount of minimum revenue provision which it considers to be prudent. This involves allowing the debt to be repaid over a period reasonably commensurate with that over which the capital expenditure provides benefit.

2 **Minimum Revenue Provision (MRP) Policy Statement**

3 It was agreed at the Cabinet meeting of 24 February 2009 and Council meeting of 03 March 2009 that, the council makes MRP charges to revenue in accordance with option 3, the asset life method as opposed to option 4 depreciation, which would have required the additional resource and administrative expense of tracking and revaluing assets at regular intervals. There is no basis for a change in policy and in accordance with approval sought and received in 2009 the council will continue to apply option 3.

4 **Asset Life Method** – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations (this option must be applied for any expenditure capitalised under a capitalisation direction) (option 3); this option provides for a reduction in the borrowing need over approximately the asset's life.

5 Under this Policy the total charge to the General Fund budget in 2018/19, excluding PFI and finance leases is expected to be approximately **£13.654** of which a significant element **(£4.407m)** is in relation to debt incurred prior to 1 April 2008.

6 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).

7 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*:*

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

- "the MRP policy is equal annual reduction of 2% of the outstanding debt at 1 April 2017 for the subsequent 50 years"

9 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);

10 These options provide for a reduction in the borrowing need over approximately the asset's life. There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made (although there are transitional arrangements in place). Repayments included in annual PFI or finance leases are applied as MRP.

11 **MRP Overpayments** - A change introduced by the revised MHCLG MRP Guidance was the allowance that any charges made over the statutory minimum revenue provision (MRP), voluntary revenue provision or overpayments, can, if needed, be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. No overpayment has been proposed for now but should this be deemed appropriate officers will update Members of the intention to overpay and reclaim in future years.

MRP for Loans on Commercial Activity Deemed to be Capital Expenditure

12 When making policy investments the council needs to consider the potential MRP implications should the loan be classed as capital spend. The authority will be providing loans on a commercial basis to third parties to facilitate the delivery of housing or services that advance the council's policy objectives. The cash advances will be used by the third parties 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 (under the terms of contractual loan agreements). Once funds are returned to the authority, the returned funds are classed as a capital receipt, and off-set against the CFR, which will reduce accordingly.

13 Expenditure on policy loans to third parties which constitute capital expenditure must have MRP set aside. In accordance with recent MHCLG regulations loans towards capital expenditure by third parties MRP will be based on the life of the assets to which the third party expenditure is incurred, or, over a shorter period, where it is considered to be more prudent.

14 The Council has historic commercial loans to associated organisations for which MRP treatment is in line with the associated risk and prudence considerations and regulations at the time of issue. These arrangement will continue. Full MRP provision will be made on all new prudential borrowing on long term commercial loans and financial assets held for sale, in accordance with the new regulations, over the expected life of the asset for which the loan is provided, or, over a shorter period, where it is considered to be more prudent.

TREASURY MANAGEMENT STRATEGY 2019/20

ANNEX 5 - ANNUAL INVESTMENT STRATEGY

1. OVERVIEW

1.1 The MHCLG and CIPFA have extended the meaning if 'investments' to include both financial and non financial investments. This report deals mainly with financial investments (as managed by the treasury management team) although prudential indicators in as much as it pertains to borrowing for non financial investment are outlined in this report. The purchase of income yielding assets are covered in the Capital Strategy report.

1.2 The council will have regard to the MHCLG's Guidance on Local Government Investments ("the Guidance") and the 2017 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The council's investment priorities remain: -

- security of the invested capital;
- liquidity of the invested capital; and
- an optimum yield which is commensurate with security and liquidity.
- all investments will be in sterling.

1.3 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 which also enables diversification and thus avoidance of concentration risk.

1.4 **Other information:** 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 maintain a monitor on market pricing such as **"credit default swaps"** and overlay that information on top of the credit ratings.

Creditworthiness policy

1.5 The council applies the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- CDS spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, credit Watches and credit Outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the council to determine the suggested duration for investments that exist on Capita's recommended counterparty list. The council will therefore use counterparties within the following durational (colour) bands

Colour	Suggested Duration
Yellow	5 years *
Dark Pink	5 years for Ultra-Short Dated Bond Funds with a credit score of 1.25
Light Pink	5 years for Ultra-Short Dated Bond Funds with a credit score of 1.5
Purple	2 years
Blue	1 year (only applies to nationalised or semi nationalised UK Banks)
Orange	1 year
Red	6 months
Green	100 days
No Colour	Not to be used

Table 1 – Durational bands for Counterparties

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour

	Colour (and long term rating where applicable)	Amount Limit per institution £m	TRIB Local current limit per institution £m
UK Government Debt or Equivalent *	**Yellow**	**Unlimited**	**40**
Banks	**Purple (2 years)**	**50**	**-**
Banks	**Orange (1 year)**	**50**	**30**
Banks – part nationalised	**Blue (1 year)**	**50**	**40**
Banks	**Red (6 months)**	**40**	**30**
Specific Overnight Limit with Council's Own Banker - £20m			
Banks	**Green (100 days)**	**30**	**20**
Banks	**No colour**	**Not to be used**	**-**

Limit 3 category – Council's banker (not meeting Banks 1)	**Blue**	**50**	**-**
Policy Investment lending limit	**-**	**To be determined on a case by case basis**	**-**
DMADF	**UK sovereign rating**	**Unlimited**	**120**
Local authorities	**n/a**	**15**	**10**
	Fund rating	**Money Limit £m**	
Money market funds CNAV	**AAA**	**15**	**-**
Money market funds LVNAV	**AAA**	**15**	**10**
Money market funds VNAV	**AAA**	**15**	**-**

Note: The Treasury Risk and Investment Board (TRIB) under the auspices of the Director of Finance have delegated powers to make changes to their local operational limits, but remain within the parameters of the Treasury Strategy.

1.6 The council is alerted of changes to ratings and of all three agencies through its use of its adviser's creditworthiness service. In addition to the use of credit ratings the council will be advised of information on movements in credit default swap spreads against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the council's lending list

1.7 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 except in the circumstances out lined above where TRIB determines the counterparty can remain on the councils list.

1.8 Sole reliance will not be placed on the use of this external service. In addition this council will also use market data and market information, information on government support for banks and the credit ratings of that supporting government.

Country limits

1.9 The council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating from Fitch of AA- (or equivalent from other agencies if Fitch does not provide a rating). However, it must be noted that the most likely position is that any foreign institution the council invest in should be as highly rated as the UK or better. Investments in the UK will not be subject to sovereign credit worthiness rating restriction.

1.10 The list of countries which currently meet this criterion are outlined in Annex 5 as part of the treasury strategy. The Director of Finance will monitor and update the position under delegated powers and report back to Council at the earliest opportunity.

1.11 Where Institutions are not on the council's advisers list and the council makes its own assessment, the council will only lend to counterparties using the minimum criteria specified below.

1.12 The minimum credit rating required for an institution to be included in the council's counterparty list (where Capita credit worthiness service is not being used) is as follows:

Table 2 – Minimum credit ratings

	Long-Term	**Short-Term**
Fitch	A	F1
Moody's	Baa1	P-2
Standard & Poors	A-	A-2

Sovereign Rating	Same rating as the UK or higher
Money Market Funds	AAA

Note: The above does not apply to policy investments.

1.13 As outlined above officers also take any market intelligence gleaned into consideration to further determine whether to suspend institutions from the list even though the institution meets our minimum lending criteria.

1.14 Setting and monitoring of the counterparty list and the agreed maximum limit per counterparty (and council's rating criteria) constitutes part of the execution and administration function and forms part of the authority to "determine the annual treasury strategy and carry out all treasury management activities" as per the council's scheme of delegation outlined in our financial regulations. The Director of Finance therefore has discretion to review and amend these minimum ratings in view of market conditions and report to Council at the earliest opportunity.

1.15 Officers have to respond quickly to counterparty rating changes and include or suspend institutions as their ratings fall in/out of the council's minimum rating criteria. This ensures that investment risk continues to be spread across a range of credit worthy institutions. The lending list is under ongoing review by the Director of Finance under delegated authority.

1.16 Institutions with which the council currently place funds are as follows:

- Debt Management Office (DMO). The rates of interest from the DMO are below equivalent money market rates. However, the returns are an acceptable trade-off for the guarantee that the council's capital is secure particularly in times of high market volatility.
- The British institutions where the UK has a substantial stake such as Lloyds and RBS
- Other UK institutions meeting our minimum credit rating criteria
- AAA rated money market funds.
- Other local authorities (LAs) are relatively risk free counterparties. In the CLG's own investment guidance issued to councils, LA deposits are deemed to offer high security

and liquidity. Their limit is set at £5m for district councils and £10m for other LAs, subject to a group limit of £180m.

- Foreign institutions from countries with sovereign ratings equivalent to the UK's sovereign rating or higher provided they meet our minimum criteria.
- Institutions that fall within Link Asset Services' approved lending list having met the diverse criteria and who the council assess as having sound credit worthiness.
- UK government – (gilts and treasury bills).

2. POLICY LENDING– NON TREASURY MANAGEMENT INVESTMENTS:

2.1 In some circumstances the council may have entered into a partnership arrangement with organisations or institutions for the provision of a service/facility that will directly promote the council's policy objectives which either requires the council to lend or jointly invest in a venture. Or the council may invest in a venture that furthers one or more of the council's policy objectives.

2.2 These types of policy investments do not form part of the treasury management strategy as such and are therefore not required to be included in the treasury management strategy statement.

2.3 This council has already entered into some lending activities in support of the policy objectives of the council. Four policy related investments have been made, which are shown in Table 3 below:

Table 3 – Policy investments entered into by Ealing Council

Organisation	£m	Description
West London Waste Authority (WLWA)	15.000	An Invest to Save loan granted to West London Waste Authority (WLWA) towards the project for the development of a new Energy from waste facility. Interest payments for this loan commenced January 2017.
Broadway Living Limited	8.040	Two loans have been granted to Broadway Living Limited for £1.2m and £6.8m.
Future Ealing	0.600	This is an investment that LBE made, which was part of a PFI structure
Ealing Community Resource Centre Ltd (ECRC)	0.020	This was a loan granted to ECRC in February 2014 for financial support towards the running costs of the Lido Centre in West Ealing

TREASURY MANAGEMENT STRATEGY 2019/20

3. INVESTMENT BALANCES / LIQUIDITY OF INVESTMENTS

3.1 Based on Ealing's cash flow forecasts, the council anticipates its fund balances in 2018/19 to average around £128m if no long term borrowing is raised and we persist with the internal borrowing policy to fund the Council's underlying need to borrow. Balances will be higher if we raise external borrowing. For treasury investments, it is considered that the maximum percentage of its overall investments that the council should hold for more than 365 days is £20m. (Investments with a maturity exceeding a year). The prudential indicator figure of £20m for 2019/20 is therefore recommended. It should be noted that this indicator does not apply to investments made for policy reasons.

3.2 In addition, the council may enter into forward deals, but with an exposure that does not exceed 5 years, from the date the forward deal was affected.

3.3 The actual amount available for investment in 2019/20 will fluctuate as a result of the timing of significant items such as:

- expenditure on capital projects
- council tax, business rates, council house rents income
- receipt of government grants
- long-term loans taken out to fund capital expenditure
- capital receipts in respect of major asset sales

3.4 The amounts available for investments consist of both cash flow and core balances made up of reserves not likely to be required for one to two years. It is possible for the council to invest this core cash for longer term. The strategy is flexible and allows the Director of Finance to take the decision to extend the duration of lending when market conditions are conducive to such lending.

Investment Strategy and Interest Rate Outlook

3.5 On the assumption that the UK and EU agree a Brexit deal in spring 2019, then Bank Rate is forecast to increase steadily but slowly over the next few years to reach 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%

3.6 The overall balance of risks to these forecasts is currently to the downside (i.e. start of increases in bank rate occurs later). However, should the pace of growth quicken and / or forecasts for increases in inflation rise, there could be an upside risk.

3.7 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:

2018/19	0.75%
2019/20	1.00%
2020/21	1.50%
2021/22	1.75%

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

4. SPECIFIED/ UNSPECIFIED INVESTMENTS

4.1 **SPECIFIED INVESTMENTS**: All such investments will be sterling denominated, with **maturities up to maximum of 1 year** meeting the minimum 'high' quality criteria where applicable.

4.2 **NON-SPECIFIED INVESTMENTS**: These are investments with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use. A maximum of 30% can be held in aggregate in non-specified investment.

4.3 A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the above categories.

4.4 As a result of the change in accounting standards for 2018/19 under IFRS 9, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the Ministry of Housing, Communities and Local Government, [MHCLG], concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years commencing from 1.4.18.)

4.5 The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

Table 4 – Parameters applying to institutions or investment vehicles

	Minimum credit criteria / colour band	**Max % of total investments or maximum amount of investment per institution**	**Max. maturity period**
DMADF – UK Government	N/A	**100%**	**6 months**
		£m	
UK Government gilts	UK sovereign rating	20	30 years

UK Government Treasury bills	UK sovereign rating	50	1 year
Bonds issued by multilateral development banks	UK sovereign rating	10	6 months
Money market funds CNAV	AAA	30	Liquid
Money market funds LVNAV	AAA	20	Liquid
Money market funds VNAV	AAA	10	Liquid
Ultra-Short Dated Bond funds with a credit score of 1.25	AAA	5	Liquid
Ultra-Short Dated Bond funds with a credit score of 1.5	AAA	5	Liquid
Local authorities	N/A	15	24 months
Term deposits with banks and building societies	Blue Orange Red Green No Colour	50	12 months 12 months 6 months 100 days Not for use
CDs or corporate bonds with banks and building societies	Blue Orange Red Green No Colour	40	12 months 12 months 6 months 100 days Not for use
Corporate bond funds		10	N/A Tradable
Gilt funds	UK sovereign rating	20	N/A Tradable
Property funds		10	N/A Tradable

4.6 **SPECIFIED INVESTMENTS:**

(All such investments will be sterling denominated, with **maturities up to maximum of 2 years**, meeting the minimum ‘high’ rating criteria where applicable)

Table 5 – Specified Investments

	Minimum Credit Criteria	Use	Max. maturity period
Debt Management Agency Deposit Facility	N/A	In- house	6 months
Term deposits – local authorities	N/A	In-house	2 year
Term deposits – banks and building societies	Green credit band per capita credit worthiness service	In-house	1 year

Table 6 – Term deposits with nationalised banks and banks and building societies

	Minimum Credit Criteria	Use	Max. maturity period
UK part nationalised banks	Green credit band per capita credit worthiness service	In-house	**1 year**
Banks part nationalised by high credit rated (sovereign rating) countries – non UK	Green credit band per capita credit worthiness service	In-house and Fund Managers	**1 year**

Table 7 – Other Investments Specified Investments

	Minimum Credit Criteria	Use	Max. maturity period
Collateralised deposit	Green credit band per capita credit worthiness service	In-house	**1 year**
Certificates of deposit issued by banks and building societies covered by UK Government (explicit) guarantee	Green credit band per capita credit worthiness service	In-house and Fund Managers	**1 year**
UK Government Gilts	UK Government Rating	In-house buy and hold and Fund Managers	**1year**
Treasury Bills	UK sovereign rating	In house and Fund Managers	**1 year**
Certificates of deposit issued by banks and building societies covered by UK Government (explicit) guarantee	UK sovereign rating or Green bank	In-house	**1 year**
Bond issuance issued by a financial institution which is explicitly guaranteed by the UK Government (refers solely to GEFCO - Guaranteed Export Finance Corporation)	UK sovereign rating	In-house buy and hold and Fund Managers	**1 year**
Bonds issued by multilateral development banks	Long Term AAA rating	In-house buy and hold and Fund Managers	**Liquid**
Government Liquidity Funds	UK Government liquidity funds only	In-house and Fund Managers	**Liquid**
Money Market Funds	Fitch – AAAmmf S&P – AAAm Moodys – AAAmf	In-house and Fund Managers	**Liquid**

Notes:

- *If forward deposits are to be made, the forward period plus the deal period should not exceed one year in aggregate.*
- *Buy and hold may also include sale at a financial year end and repurchase the following day in order to accommodate the requirements of SORP.*
- *As collateralised deposits are backed by collateral of AAA rated local authority LOBOs, this investment instrument is regarded as being a AAA rated investment as it is equivalent to lending to a local authority.*

LOCAL AUTHORITIES

- *Although most local authorities do not have credit ratings, investing with local authorities provides good security for the council.*

4.7 **Accounting treatment of investments.** The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this council. To ensure that the council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

4.8 **Blanket guarantees on all deposits.** Some countries may support their banking system by giving a blanket guarantee on all deposits, however; this council will generally not rely on the guarantees provided by any government unless there are overriding reasons for doing so.

4.9 **Other Countries.** At present the council will determine whether to include other countries by reference to credit rating of the sovereign together with financial news data on the sovereign. The minimum credit rating required for an institution to be included within the council's list is AA-, although the council more likely invest in sovereigns that have a rating equivalent to or better than the UK governments rating. Currently the countries falling within this are as follows:

4.10

Table 8 – Credit Rating of other countries

AAA	AA+	AA	AA-
Australia	Finland	Abu Dhabi (UAE)	Belgium
Canada	Hong Kong	France	Czech Republic
Denmark		New Zealand	Estonia
Germany		U.K	Qatar
Luxembourg			South Korea
Netherlands			Taiwan
Norway			
Singapore			
Sweden			
Switzerland			
U.S.A			

Note: Although the Director of Finance has discretion under this strategy to invest outside the UK, the current position is that investments are not currently being placed overseas. However, the position is kept under regular review.

4.11 **Non Specified Investments**

Table 9 – Non Specified Investments

A. Maturities of any period.

Fixed term deposits with variable rate and variable maturities: -	Minimum Credit Criteria	Use
Callable deposits	Falling within the council's criteria	In-house
Range trade	Falling within the council's minimum criteria	In-house
Other debt issuance by UK banks covered by UK Government guarantee	UK Government explicit guarantee	In-house and Fund Managers
Term deposits with unrated counterparties	Decision flowing through TRIB, or a delegated officer	In-house
Commercial Paper	Fitch F1, AA aa1 or equivalent.	In-house / Fund Managers
Corporate Bonds	Fitch F1, AA aa1 or equivalent.	In-house/ Fund Managers
UK Floating Rate Notes	Fitch F1, AA aa1 or equivalent.	In-house/Fund Managers
VNAV MMF's (where there is greater than 12 month history of a consistent £1 Net Asset Value)	High Credit Score	In-house and Fund Managers
Bond Funds	Long term AAA	In-house and Fund Managers
Gilt Funds	Long Term AAA	In-house and Fund managers

B. Maturities in excess of 1 year

Investments as specified above in specified investments, but for periods in excess of 1 year.

Investment Treasury Indicator and Limit

4.12 Total principal funds invested for greater than 364 days. These limits are set with regard to the council's liquidity requirements and to reduce the need for the council becoming a forced seller 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: -

Table 10 – Investment Treasury Indicator and limit to be approved

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

Note: This durational limit excludes policy investments, where the decision is made on a case by case basis.

4.13 For its cash flow generated balances, the council will seek to utilise money market funds, call accounts and short-dated deposits (overnight to three months), treasury bills and the debt management office.

Investment Risk Benchmarking

4.14 These benchmarks are simple guides to maximum risk, so they may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that officers will monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the Mid-Year or Annual Report.

Security

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

- <1% historic risk of default when compared to the whole portfolio.

Liquidity

4.16 In respect of liquidity the council seeks to maintain:

- Bank overdraft - £2m
- Liquid short term deposits of at least £5m available with a week's notice.

Yield

4.17 Local measures of yield benchmarks are:
Investments – internal returns above the 7 day LIBID rate

In addition, the security benchmark for each individual year is:

Table 11 – Security Benchmark for each individual year

	1 year	**2 years**	**3 years**	**4 years**	**5 years**
Maximum %	2%	2%	2%	2%	2%

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

Provisions for Credit-related losses

4.18 If any of the council's investments appeared at risk of loss due to default (i.e. this is a credit-related loss, and not one resulting from a fall in price due to movements in interest rates) then the council will make revenue provision of an appropriate amount.

End of year Investment Report

4.19 At the end of the financial year, the council will prepare a report on its investment activity as part of its annual treasury management report.