Treasury Management Strategy Statement

Minimum Revenue Provision Policy Statement and Annual Investment Strategy

2019/20

1. INTRODUCTION

1.1 Background

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

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

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

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.

CIPFA defines treasury management as:

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

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

1.2 Reporting requirements

1.2.1 Capital Strategy

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

- a high-level long term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

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

This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. 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 will show:

- 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.

Where a physical asset is being bought, 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.

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. *(Note that the Council is intending to borrow for its Commercial Investment Framework and risks, mitigation and objectives are defined within the Commercial Investment Framework).*

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.

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

1.2.2 Treasury Management reporting

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

a. **Prudential and treasury indicators and treasury strategy** (this report) - The first, and most important report is forward looking and covers:
    - the capital plans, (including prudential indicators);

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

b. A mid-year treasury management report – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

c. An annual treasury report – This is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

In addition to the above reports, Cabinet will be provided with an overview of treasury return against budget and prediction of likely outturn and year-end variance as part of the financial monitoring reports presented to Members throughout the year.

1.2.3 Scrutiny

The above reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken by the Cabinet.

1.2.4 Treasury Management Strategy for 2019/20

The strategy for 2019/20 covers two main areas:

Capital issues

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

Treasury management issues

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

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

1.3 Training

The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. Training has been undertaken by members on 30 January 2018 and further training will be arranged as required. The training needs of treasury management officers are periodically reviewed.

There is a post with specific responsibility for treasury management within the accountancy team and the Council is committed to ensuring the holder has relevant qualifications and has access to the training and support required to undertake this role.

In addition, the Council's treasury management team is a member of the South West Treasury Management Benchmarking Group hosted by Link Asset Services. This group has members from approximately 14 authorities and provides a forum for interpreting Treasury Management data across the area and sharing best practice. The group also allows the opportunity to consider any potential forthcoming treasury management risks, the early identification of which can aid proactive investment management.

The Council maintains an internal audit function through the South West Audit Partnership (SWAP). SWAP undertakes a periodic internal audit review of the treasury management function. In the latest audit by SWAP, which covered the 2017/18 financial year, the treasury management function was given a Substantial Opinion, which is the highest level of assurance available.

Further review is also provided by the external audit team, who consider the reporting of treasury management data within the financial statements as part of their external audit opinion work.

1.4 Treasury management consultants

The Council uses Link Asset Services, Treasury solutions as its external treasury management advisors.

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

It is the intention that the scope of investments within the Council's operations will include both conventional treasury investments, (the placing of residual cash from the Council's functions), and more commercial type investments, such as investment properties. The commercial type investments require specialist advisers, and the Council will seek to appoint suitable specialist advisers in relation to this activity, as and when required.

1.5 IFRS 16 - Leasing

IFRS 16 Leasing requires that lessees bring leases that were previously off balance sheet onto the balance from 1 April 2019.

CIPFA has decided to recommend to the Government that implementation of IFRS 16 Leasing should be delayed by one year until 2020/21 in the public sector. This will ensure that public sector accounts will be aligned to the Whole of Government Accounts.

However, in the meantime, local authorities who are lessees need to consider what changes they will need to make to adjust their figures as at 1 April 2019 and in year, for Capital Financing Requirement, External debt (Other long-term liabilities), Authorised Limit and Operational Boundary. This is to allow for leases, previously off balance sheet, being brought onto the balance sheet from that date.

It is not currently possible to be precise about such adjustment figures until detailed data gathering has been substantially completed later in the 2019/20 financial year. Therefore, the Capital Financing Requirement, External debt (Other long-term liabilities), Authorised Limit and Operational Boundary may need to be amended mid-year, once the detailed impact is known for the Council.

1.6 Investments, Treasury Investments and Non-Treasury Investments

As explained in 1.2.1 Capital Strategy, Non-Treasury investments will be reported on through the separate Capital Strategy Statement and Treasury investments will be reported on through the Treasury Management Strategy Statement; (this document).

The following clarifies the definition of an investment and which investments are Treasury investments and which are Non-Treasury investments:

i. **Investments –** when made by local authorities, investments can be classified into one of two main categories:
    a. Treasury Investments; (sometimes referred to as Financial investments); and
    b. Non-Treasury Investments; (sometimes referred to as Other or Non-Financial investments).

    (For the avoidance of doubt, the definition of investments also covers loans made by a local authority to one of its wholly-owned subsidiaries or associates, to a joint venture or to a third party. 'Loan' for the purpose of this definition does not include a loan to another local authority, which is classified as a specified investment: (one of the types of investment instrument that the treasury management team are authorised to use). The definition of 'investments' does not include pension funds or trust fund investments).

ii. **Treasury Investments** – are those that arise from the organisation's cash flows and debt management activity, and ultimately represent balances that need to be invested until the cash is required for use in the course of business.

iii. **Non-Treasury Investments** - are investments made for policy reasons outside of normal treasury management activity. These may include:

    a. ***service investments*** - held clearly and explicitly in the course of the provision, and for the purposes, of operational services, including regeneration;

b. ***commercial investments*** - which are taken for mainly financial reasons. These may include:
   i. ***investments arising as part of business structures -*** such as shares and loans in subsidiaries or other outsourcing structures such as IT providers or building services providers;

   ii. ***investments explicitly taken with the aim of making a financial surplus for the organisation****;*

   iii. ***assets held primarily for financial benefit*** - such as investment properties.

The Capital Financing Requirement in the Treasury Management Strategy Statement, (this document), gives an holistic view of the Council's borrowing need, taking into account not only the capital expenditure planned on the Non-HRA and HRA but also the expenditure planned on Non-Treasury Investments; (i.e. service investments and commercial investments). However, as stated already, other than this, Non-Treasury Management investments are not dealt with in this document but in the separate Capital Strategy Statement.

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

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

These indicators help show the effect of the financing and borrowing strategy that the Council plans to adopt over the next three financial years.

The indicators also act as an early warning system, to flag up if the Council decides to set capital programmes without the necessary finances to fund them.

2.1 Capital expenditure

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

Capital expenditure	2017/18 Actual £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
Non-HRA	**6,864**	**16,632**	**4,279**	**1,045**	**1,051**
HRA	**10,158**	**5,241**	**4,906**	**4,906**	**4,906**
Service investments *	**600**	**1,695**	**3,335**	**1,000**	**0**
Commercial investments *	**0**	**5,000**	**10,000**	**5,000**	**0**
Total	**17,622**	**28,568**	**22,520**	**11,951**	**5,957**

** See section 1.6 for the definition of Service Investments and Commercial Investments.*

These figures show the Council's capital programme before any grants or contributions received from third parties. The total capital expenditure also includes that related to major repairs, which, for accounting purposes, is shown within the HRA.

Also included separately in the table are Service Investments and Commercial Investments, which are non-treasury investments. See section 1.6 for the definition of these.

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

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

Financing of capital expenditure	**2017/18 Actual £000**	**2018/19 Estimate £000**	**2019/20 Estimate £000**	**2020/21 Estimate £000**	**2021/22 Estimate £000**
Capital receipts	(2,399)	(700)	(8,830)	(600)	(600)
Capital grants	(1,087)	(4,410)	(3,845)	(1,760)	(1,635)
Capital reserves	(4,078)	(3,127)	(3,175)	(3,127)	(3,127)
Revenue	(7,331)	(1,879)	(1,279)	(1,279)	(1,279)
Net financing need for the year *	**2,727**	**18,452**	**5,391**	**5,185**	**(684)**

The net financing need for service investments/ commercial investments included in the above tables is shown below**:**

Service investments & Commercial investments	**2017/18 Actual £000**	**2018/19 Estimate £000**	**2019/20 Estimate £000**	**2020/21 Estimate £000**	**2021/22 Estimate £000**
Expenditure	600	6,695	13,335	6,000	0
Financing	0	(600)	0	0	0
Net financing need for the year	**600**	**6,095**	**13,335**	**6,000**	**0**
Percentage of total net financing need %	**22.0%**	**33.0%**	**247.4%**	**115.7%**	**0%**

** Capital Receipts in 2019/20 include the Non-HRA receipt of around £8m expected from the sale of Knowle. This reduces the overall net financing need for that year.*

2.2 The Council's borrowing need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so its underlying borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

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

The CFR includes any other long-term liabilities (e.g. PFI and finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility by the PFI, PPP lease provider and so the Council is not required to borrow separately for these schemes. The Council currently has no such schemes within the CFR.

(However, as reported in section 1.5 above, please note that the Capital Financing Requirement, External debt (Other long-term liabilities), Authorised Limit and Operational Boundary may need to be amended mid-year, once the detailed impact of IFRS 16 Leasing is known for the Council).

The Council is asked to approve the CFR projections below:

	2017/18 Actual £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
Capital Financing Requirement					
CFR Non-HRA	4,635	16,814	8,601	7,478	6,526
CFR HRA	80,601	79,010	77,093	74,833	72,215
CFR Service investments	3,892	4,903	8,137	6,639	6,228
CFR Commercial investments	0	5,000	14,788	19,500	19,203
Total CFR	**89,128**	**105,727**	**108,619**	**108,450**	**104,172**
Movement in CFR	**1,443**	**16,599**	**2,892**	**(169)**	**(4,278)**

Movement in CFR represented by					
Net financing need for the year (above)	2,727	18,452	5,391	5,185	(684)
Adjustment	91	0	0	0	0
Less MRP*/VRP* and other financing movements	(1,375)	(1,853)	(2,499)	(5,354)	(3,594)
Movement in CFR	**1,443**	**16,599**	**2,892**	**(169)**	**(4,278)**

** MRP = Minimum Revenue Provision; VRP = Voluntary Revenue Provision*

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 on page 9 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.

2.3 Minimum revenue provision (MRP) policy statement

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

MHCLG regulations have been issued which require the full Council to approve **an MRP Statement** in advance of each year. A variety of options is provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement:

For all unsupported borrowing, (including 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).

This option provides for a reduction in the borrowing need over approximately the asset's life. The use of this option by EDDC is consistent with the prior year.

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.

Repayments included in finance leases are applied as MRP.

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. Up until the 31 March 2019 the total VRP overpayments, (wholly in respect of the HRA), were £4,424,409; (no HRA VRP payments are scheduled for 2018/19).

3 BORROWING

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

3.1 Current portfolio position

The overall treasury management portfolio as at 31 March 2018 and for the position as at 31 December 2018 are shown below for both borrowing and investments.

A more detailed schedule of investments and borrowing may be found in Appendix 5.6

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

TREASURY PORTFOLIO				
	Actual	Actual	Current	Current
	31.3.18	**31.3.18**	**31.12.18**	**31.12.18**
Treasury investments	**£000**	**%**	**£000**	**%**
Banks	1,000	3%	2,900	6%
Building Societies - unrated	0	0%	6,000	11%
Building Societies - rated	0	0%	5,000	9%
Local Authorities	0	0%	3,000	6%
Money Market Funds	2,250	7%	5,900	11%
Total managed in house	**3,250**	**10%**	**22,800**	**43%**
Money Market Funds*	29,908	90%	29,855	57%
Property Funds	0	0%	0	0%
Total managed externally	**29,908**	**90%**	**29,855**	**57%**
Total treasury investments	**33,158**	**100%**	**52,655**	**100%**
Treasury external borrowing				
Local Authorities	4,500	5%	0	0%
PWLB	80,601	95%	88,115	100%
Total external borrowing	**85,101**	**100%**	**88,115**	**100%**
Net treasury investments / (borrowing)	**(51,943)**	**0.0%**	**(35,460)**	**0.0%**
** market value*				

	2017/18 Actual £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
External Debt					
Debt at 1 April	**84,910**	**88,242**	**94,018**	**104,274**	**104,361**
Expected change in Debt	3,332	5,776	10,256	87	(3,846)
Other long-term liabilities (OLTL) at 1 April	**0**	**0**	**0**	**0**	**0**
Expected change in OLTL	0	0	0	0	0
Actual gross debt at 31 March	**88,242**	**94,018**	**104,274**	**104,361**	**100,515**
The Capital Financing Requirement	**89,128**	**105,727**	**108,619**	**108,450**	**104,172**
Under / (over) borrowing	**885**	**11,709**	**4,345**	**4,089**	**3,657**

(As reported in section 1.5 above, please note that the Capital Financing Requirement, External debt (Other long-term liabilities), Authorised Limit and Operational Boundary may need to be amended mid-year, once the detailed impact of IFRS 16 Leasing is known for the Council).

Within the above figures, the level of debt relating to service investments/ commercial investments is:

	2017/18 Actual £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
External Debt for commercial investments / service investments					
Service Investments	1,285	2,917	6,174	4,698	4,601
Commercial Investments	0	5,000	14,788	19,500	19,203
Actual debt at 31 March	**1,285**	**7,917**	**20,962**	**24,198**	**23,804**
Percentage of total external debt %	**1.46%**	**8.42%**	**20.10%**	**23.19%**	**23.68%**

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 Section 151 Officer 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.

3.2 Treasury Indicators: limits to borrowing activity

(As reported in section 1.5 above, please note that the Capital Financing Requirement, External debt (Other long-term liabilities), Authorised Limit and Operational Boundary may need to be amended mid-year, once the detailed impact of IFRS 16 Leasing is known for the Council).

3.2.1 The operational boundary. This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

Operational boundary	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
Debt HRA/ non-HRA	87,692	86,101	83,312	80,164
Other long term liabilities	0	0	0	0
Service investments	2,917	6,174	6,174	4,698
Commercial investments	5,000	14,788	19,500	19,500
Total	**95,609**	**107,063**	**108,986**	**104,362**

3.2.2 The authorised limit for external debt. This is a key prudential indicator and 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 full Council. It reflects the level of external debt, which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

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

Authorised limit	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
Debt	97,935	97,935	97,063	96,174
Other long term liabilities	0	0	0	0
Service investments	2,917	6,174	6,174	4,698
Commercial investments	5,000	14,788	19,500	19,500
Total	**105,852**	**118,897**	**122,737**	**120,372**

The authorised limit includes an additional amount as headroom for unanticipated cash movements, including those due to slippage.

Headroom for the Non-HRA is set at £3.0m. For the HRA, a debt cap of £87.844m set by the Government as the authorised limit has been used; (but see the comment regarding abolition of the HRA debt cap, below).

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

HRA Debt Limit	**2018/19 Estimate £000**	**2019/20 Estimate £000**	**2020/21 Estimate £000**	**2021/22 Estimate £000**
HRA debt cap *	87,844	87,844	87,844	87,844
HRA CFR	79,010	77,093	74,833	72,215
HRA headroom	8,834	10,751	13,011	15,629

**** Abolition of HRA debt cap.*** *In October 2018, Prime Minister Theresa May announced a policy change of abolition of the HRA debt cap. The Chancellor announced in the Budget that the applicable date was 29.10.18.*

3.3 Prospects for interest rates

The Council has appointed Link Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Their central view is given in Appendix 5.2.

3.4 Borrowing strategy

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

Against this background and the risks within the economic forecast, caution will be adopted with the 2019/20 treasury operations. The Section 151 Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in long and short term rates,* (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast,* perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

Any decisions will be reported to the appropriate decision making body at the next available opportunity.

In practice therefore, the borrowing strategy is dependent on the amount and timing of capital expenditure, given the market conditions at the time, and the capital-financing requirement is likely to be funded via a combination of external fund disinvestment and/or loans from the PWLB.

3.5 Cash Flow or Temporary Borrowing

In addition to borrowing for capital purposes, the Council also borrows in the short-term to meet day-to-day shortages in its call account. This borrowing requirement is inherent within the operation of this account and is normally covered overnight via the call account overdraft and cleared the next day.

In some instances, particularly around the year-end, the overdraft may not provide a sufficient short-term buffer, and in these instances, the Council can borrow via the market at fixed rates for a fixed term of less than 3 months.

At the end of 2017/18, there was a requirement for short-term borrowing over the year-end, but currently there is no indication that such borrowing will be required at the end of 2018/19.

3.6 Policy on borrowing in advance of need

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

Borrowing in advance will be made within the constraints that:

- It will be limited to no more than the expected increase in borrowing need (CFR) over the three year planning period; and
- The authority would not look to borrow more than 12 months in advance of need.

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

3.7 Debt rescheduling

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

The reasons for any rescheduling to take place will include:

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

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

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

4 ANNUAL INVESTMENT STRATEGY

4.1 Investment policy – management of risk

The MHCLG and CIPFA have extended the meaning of 'investments' to include both financial (or treasury) investments and non-financial (or non-treasury/ other) investments. This report deals solely with financial investments, (as managed by the treasury management team). Non-financial (or non-treasury/ other) investments, (essentially the purchase of income yielding assets), are covered in the Capital Strategy, (a separate report).

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

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

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

The above guidance from the MHCLG and CIPFA place a high priority on the management of risk. This authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

1. Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.

2. **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.

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

4. This authority has defined the list of **types of investment instruments** that the treasury management team are authorised to use. There are two lists in appendix 5.4 under the categories of 'specified' and 'non-specified' investments.

5. **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.

6. **Non-specified investments** are those 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.

7. **Non-specified investments limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being 10% of the total investment portfolio at the point of investment, (see section 5.4).

8. **Lending limits**, (amounts and maturity), for each counterparty will be set through applying the table in section 4.3.

9. Only the Council's external funds can be invested for **longer than 365 days**, (see section 5.1.4).

10. All investments will be denominated in **sterling**.

11. As a result of the change in accounting standards for 2018/19 under IFRS 9, this authority will consider the implications of investment instruments that 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.)

However, this authority will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance, (see section 4.7). Regular monitoring of investment performance will be carried out during the year.

Changes in risk management policy from last year.
The above criteria are unchanged from last year.

4.2 Creditworthiness policy

The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle, the Council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the specified and non-specified investment section 5.4; and

- It has sufficient liquidity in its investments. For this purpose, it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

The Strategic Lead Finance will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to those that determine which types of investment instrument are either specified or non-specified as it provides an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

Counterparty ratings are monitored on a real time basis via notifications received from Link Asset Services as the agencies publish modifications. In addition a full review of the counterparty list is carried out on a regular basis.

The security of the Council's financial assets is paramount, and whilst the strategy needs to be clear in this area it also needs be sufficiently comprehensive and itterative in order to provide operational flexibility within, what at times, is a volatile macroeconomic environment. As the financial backdrop changes it is essential that the strategy is set to enable an efficient response to those changes.

The Council manages the majority of its internal investments via money market funds and a range of banks and building societies in line with the creditworthiness criteria referred to below.

In order to address the need for flexibilty, and to ensure the spread of risk, access to an investment portal has been arranged which allows officers to review and potentially transact with a small range of money market funds directly. All money market funds considered suitable with reference to the creditworthiness criteria will be approved for use by the S.151 Officer before an account is opened. The Council currently has access to four money market funds; if appropriate operationally, consideration will be given to opening an additional money market fund in the future.

This strategy was changed to include corporate bonds within its creditworthiness criteria for the first time in 2016/17. Investments in corporate bonds are limited to a duration of less than 1 year, must be AAA rated and have a maximum value of £2m per investee. The Council will not trade corporate bonds directly, but will trade via a specialist investment intermediary, whose fee is linked to the return. Given the short duration it is anticipated the majority of trades will be via the secondary market.

In the 2018/19 Treasury Management Strategy, the Council approved the inclusion of alternative investments such as Property Funds in Non-Specified Investments.

The use of these instruments can be deemed capital expenditure, and as such will be an application (spending) of capital resources. This Authority will seek guidance on the status of any fund it may consider using. Appropriate due diligence will also be carried out before investment of this type is undertaken.

4.3 Creditworthiness Criteria

The Council's proposed creditworthiness criteria are included in the table below.

Creditworthiness Criteria		
External (Long Term) Investment Fund	**Criteria**	**Maximum Money and/ or % Investment Limit**
Collective Investment Schemes (e.g. bond funds)	AAA long-term rating backed up with lowest volatility (V1/S1)	60% of External Fund total
Alternative Investment Funds e.g. property funds	The use of these instruments can be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. This Authority will seek guidance on the status of any fund it may consider using. Appropriate due diligence will also be carried out before investment of this type is undertaken.	£10m
Cash Flow/ Internal Investments		
Deposit Building Societies	With over £5 Billion in total assets	£3m
Deposit Building Societies	With over £1 Billion in total assets	£2m
Deposit with UK incorporated banks	Minimum F1, A1 or P1 short term backed up by A long term credit rating	£2m
Deposit with banks incorporated outside the UK but entitled to accept deposits in the UK	Minimum F1, A1 or P1 short term backed up by A long term credit rating	£2m
Money Market Funds	AAA Long Term Rating	£3m
UK Local, Police & Fire Authorities		£3m
UK Government Treasury Bills/ Gilts		No limit
Corporate Bonds	AAA and less than one year duration	£2m
The "deposits "referred to in the above table relate either to cash, floating rate notes or certificates of deposit.		

The Council will not invest in subsidiaries that do not have a credit rating in their own right and a separate FSA licence from the parent company.

In the event of a downgrade resulting in a counterparty or investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.

Any changes in counterparty ratings or other criteria that put the counterparty below the minimum criteria whilst the Council holds a deposit will be brought to the attention of the Strategic Lead Finance and the Portfolio Holder for Finance immediately, with an appropriate response decided on a case-by-case basis.

The Council's current counterparty list is included at section 5.5.

It is recommended that Cabinet approves the creditworthiness criteria above.

The proposed criteria for specified and non-specified investments are shown in Appendix 5.4 for approval.

4.4 UK banks – ring fencing

The largest UK banks, (those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits), are required, by UK law, to separate core retail banking services from their investment and international banking activities by 1st January 2019. This is known as "ring-fencing". Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up. Several banks are very close to the threshold already and so may come into scope in the future regardless.

Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and SME deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler, activities offered from within a ring-fenced bank, (RFB), will be focused on lower risk, day-to-day core transactions, whilst more complex and "riskier" activities are required to be housed in a separate entity, a non-ring-fenced bank, (NRFB). This is intended to ensure that an entity's core activities are not adversely affected by the acts or omissions of other members of its group.

While the structure of the banks included within this process may have changed, the fundamentals of credit assessment have not. The Council will continue to assess the new-formed entities in the same way that it does others and those with sufficiently high ratings, (and any other metrics considered), will be considered for investment purposes.

4.5 Investment strategy

In-house funds. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. While most cash balances are required in order to manage the ups and downs of cash flow where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed.

- If it is thought that Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments as being short term or variable.

- Conversely, if it is thought that Bank Rate is likely to fall within that time period, consideration will be given to locking in higher rates currently obtainable, for longer periods.

4.6 Investment returns expectations.

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%

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:

	Now
2018/19	0.75%
2019/20	1.00%
2020/21	1.50%
2021/22	1.75%
2022/23	1.75%
2023/24	2.00%
Later years	2.50%

- The overall balance of risks to economic growth in the UK is probably neutral.
- The balance of risks to increases in Bank Rate and shorter term PWLB rates, are probably also even and are dependent on how strong GDP growth turns out, how slowly inflation pressures subside, and how quickly the Brexit negotiations move forward positively.

4.7 Investment risk benchmarking

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

4.8 End of year investment report

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

4.9 External fund managers

The Council currently has the following amounts invested:

External Funds	Fitch International Fund Quality Rating	Fitch Fund Market Sensitivity Rating	Total Investment £M
Pooled Investment Vehicles, OEICS			
Royal London Asset Management - Cash Plus Fund	AAAf	S1	14.45
Payden & Rygel - Sterling Reserve Fund	AAAf	S1	15.41
			29.86

The AAAf Fund Quality Credit Rating reflects the very high credit quality of a fund, as measured by its weighted average rating factor.

The S1 Fund Market Sensitivity Rating reflects a fund's very low sensitivity to market risk factors. It also takes into account the investment advisor's strong capabilities as well as the fund's sound legal and regulatory environment.

5 APPENDICES

5.1 CAPITAL PRUDENTIAL & TREASURY INDICATORS 2019/20 – 2021/22

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

5.1.1 Capital expenditure

Capital expenditure	2017/18 Actual £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
Non-HRA	**6,864**	**16,632**	**4,279**	**1,045**	**1,051**
HRA	**10,158**	**5,241**	**4,906**	**4,906**	**4,906**
Service investments	**600**	**1,695**	**3,335**	**1,000**	**0**
Commercial activities	**0**	**5,000**	**10,000**	**5,000**	**0**
Total	**17,622**	**28,568**	**22,520**	**11,951**	**5,957**

5.1.2 Affordability prudential indicators

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

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.

Basis of Calculation for Ratio of Financing Costs to Net Revenue Stream				
General Fund (GF):				
Financing Costs	÷	**Budget Requirement**	=	**Ratio of financing costs to net revenue stream (General Fund)**
Minimum Revenue Provision		Revenue Support Grant		
+		+		
Interest charged on loans and finance leases		Council Tax		as a %
-				
Interest earned on investments				
Housing Revenue Account (HRA):				
Financing Costs	÷	**Budget Requirement**	=	**Ratio of financing costs to net revenue stream (HRA)**
Voluntary Revenue Provision		Council House tenants' income		
+		+/-		
Interest charged on loans and finance leases		Contribution to/from HRA Reserves		as a %
-				
Interest earned on investments				

The estimates of financing costs include current commitments and the proposals in this budget report. A positive figure in the table below indicates external debt.

	2017/18 Actual %	2018/19 Estimate %	2019/20 Estimate %	2020/21 Estimate %	2021/22 Estimate %
Non-HRA	(3.3)	(1.88)	0.01	0.81	(0.94)
HRA	22.57	24.97	26.55	24.46	25.10

A negative figure reflects the estimation that a higher level of investment income is received compared to that paid out in borrowing.

The HRA ratio changes are as a result of the principal associated with the HRA self-financing loans becoming due.

5.1.3 Maturity structure of borrowing

Maturity structure of borrowing. *(This is the amount of projected long-term borrowing that is due for repayment in each period expressed as a percentage of total borrowing).* These gross limits are set to reduce the Council’s exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

At any point, the actual percentages of debt projected to mature in each year will add up to 100%, but the proposed indicator is for a range of approved percentages. This gives discretion within an approved range to the treasury team. It does mean that each ‘set’ of figures will sum to more than 100%.

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

Maturity structure of fixed interest rate borrowing 2019/20			
		Lower	**Upper**
Under 12 months	2018/19	0%	20%
12 months to 2 years	2019/20	0%	20%
2 years to 5 years	2020/21 – 2023/24	0%	25%
5 years to 10 years	2024/25 – 2028/29	0%	25%
10 years to 20 years	2029/30 – 2038/39	0%	55%
20 years to 30 years	2039/40 – 2048/49	0%	20%
30 years to 40 years	2049/50 – 2058/59	0%	20%
40 years to 50 years	2059/60 – 2068/69	0%	20%

Within the HRA, the majority of the loans are over the longer term, as aligned to the HRA business plan, resulting in the upper limit being higher from year 5 onwards. Also, projected borrowing for commercial investments acts to increase the upper limit.

The upper limits on the maturity structure of borrowing will shift slightly each year as the maturity dates draw closer. However, the limits shown are in line with expectations based on the funding plans.

In addition to the above, the Council has an overdraft limit of £0.35m and can, if required, borrow for periods less than 3 months at fixed rates, in order to meet daily cash flow requirements. The Strategy is managed so as to avoid short-term fixed borrowing where possible. With the exception of the bank overdraft therefore, all borrowing the Council undertakes is at a fixed rate of interest.

The actual amounts maturing in each period are shown in the table below and reflect both the actual and potential loan commitments as referred to elsewhere within this strategy.

Based on capital borrowing plans included in the budget and plans for commercial investment (subject to approval), the current projected maturity structure of borrowing is shown below:

Maturity structure of fixed interest rate borrowing 2019/20			
		£000	%
Under 12 months	2018/19	2,112	1.87%
12 months to 2 years	2019/20	3,080	2.72%
2 years to 5 years	2020/21 – 2023/24	18,465	16.32%
5 years to 10 years	2024/25 – 2028/29	20,424	18.06%
10 years to 20 years	2029/30 – 2038/39	53,042	46.89%
20 years to 30 years	2039/40 – 2048/49	7,868	6.96%
30 years to 40 years	2049/50 – 2058/59	8,123	7.18%
40 years to 50 years	2059/60 – 2068/69	0	0%
Total		**113,114**	**100%**

5.1.4 Upper Limit for Total Principal Sums invested over 365 days

Only the Council's external funds can be invested for over 365 days and these total £29.85m. In practice, the Council can access this money with 3 days' notice.

5.2 INTEREST RATE FORECASTS 2019 – 2021

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

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%

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

The overall longer run future trend is for gilt yields, and consequently PWLB rates, to rise, albeit gently. However, over about the last 25 years, we have been through a period of falling bond yields as inflation subsided to, and then stabilised at, much lower levels than before, and supported by central banks implementing substantial quantitative easing purchases of government and other debt after the financial crash of 2008. Quantitative easing, conversely, also caused a rise in equity values as investors searched for higher returns and purchased riskier assets. In 2016, we saw the start of a reversal of this trend with a sharp rise in bond yields after the US Presidential election in November 2016, with yields then rising further as a result of the big increase in the US government deficit aimed at stimulating even stronger economic growth. That policy change also created concerns around a significant rise in inflationary pressures in an economy which was already running at remarkably low levels of unemployment. Unsurprisingly, the Fed has continued on its series of robust responses to combat its perception of rising inflationary pressures by repeatedly increasing the Fed rate to reach 2.25 – 2.50% in December 2018. It has also continued its policy of not fully reinvesting proceeds from bonds that it holds as a result of quantitative easing, when they mature. We therefore saw US 10 year bond Treasury yields rise above 3.2% during October 2018 and also investors causing a sharp fall in equity prices as they sold out of holding riskier assets. However, by early January 2019, US 10 year bond yields had fallen back considerably on fears that the Fed was being too aggressive in raising interest rates and was going to cause a recession. Equity prices have been very volatile on alternating good and bad news during this period.

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

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

Investment and borrowing rates

- Investment returns are likely to remain low during 2019/20 but to be on a gently rising trend over the next few years.
- Borrowing interest rates have been volatile so far in 2018-19 and while they were on a rising trend during the first half of the year, they have back-tracked since then until early January. The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in the future when authorities may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt;
- There will remain a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.

5.3 ECONOMIC BACKGROUND

GLOBAL OUTLOOK. World growth has been doing reasonably well, aided by strong growth in the US. However, US growth is likely to fall back in 2019 and, together with weakening economic activity in China and the eurozone, overall world growth is likely to weaken.

Inflation has been weak during 2018 but, at long last, unemployment falling to remarkably low levels in the US and UK has led to an acceleration of wage inflation. The US Fed has therefore increased rates nine times and the Bank of England twice. However, the ECB is unlikely to start raising rates until late in 2019 at the earliest.

KEY RISKS - central bank monetary policy measures
Looking back on nearly ten years since the financial crash of 2008 when liquidity suddenly dried up in financial markets, it can be assessed that central banks' monetary policy measures to counter the sharp world recession were successful. The key monetary policy measures they used were a combination of lowering central interest rates and flooding financial markets with liquidity, particularly through unconventional means such as quantitative easing (QE), where central banks bought large amounts of central government debt and smaller sums of other debt.

The key issue now is that period of stimulating economic recovery and warding off the threat of deflation, is coming towards its close. A new period is well advanced in the US, and started more recently in the UK, of reversing those measures i.e. by raising central rates and, (for the US), reducing central banks' holdings of government and other debt. These measures are now required in order to stop the trend of a reduction in spare capacity in the economy and of unemployment falling to such low levels, that the re-emergence of inflation is viewed as a major risk. It is, therefore, crucial that central banks get their timing right and do not cause shocks to market expectations that could destabilise financial markets. In particular, a key risk is that because QE-driven purchases of bonds drove up the price of government debt, and therefore caused a sharp drop in income yields, this also encouraged investors into a search for yield and into investing in riskier assets such as equities. Consequently, prices in both bond and equity markets rose to historically high valuation levels simultaneously. This meant that both asset categories were exposed to the risk of a sharp downward correction and we have, indeed, seen a sharp fall in equity values in the last quarter of 2018. It is important, therefore, that central banks only gradually unwind their holdings of bonds in order to prevent destabilising the financial markets. It is also likely that the timeframe for central banks unwinding their holdings of QE debt purchases will be over several years. They need to balance their timing to neither squash economic recovery, by taking too rapid and too strong action, or, conversely, let inflation run away by taking action that was too slow and/or too weak. **The potential for central banks to get this timing and strength of action wrong are now key risks.** At the time of writing, (early January 2019), financial markets are very concerned that the Fed is being too aggressive with its policy for raising interest rates and is likely to cause a recession in the US economy.

The world economy also needs to adjust to a sharp change in **liquidity creation** over the last five years where the US has moved from boosting liquidity by QE purchases, to reducing its holdings of debt (currently about $50bn per month). In addition, the European Central Bank ended its QE purchases in December 2018.

UK. The flow of positive economic statistics since the end of the first quarter of 2018 has shown that pessimism was overdone about the poor growth in quarter 1 when adverse weather caused a temporary downward blip. Quarter 1 at 0.1% growth in GDP was followed by a return to 0.4% in quarter 2 and by a strong performance in quarter 3 of +0.6%. However, growth in quarter 4 is expected to weaken significantly.

At their November quarterly Inflation Report meeting, the MPC repeated their well-worn phrase that future Bank Rate increases would be gradual and would rise to a much lower equilibrium rate, (where monetary policy is neither expansionary of contractionary), than before the crash; indeed they gave a figure for this of around 2.5% in ten years' time, but declined to give a medium term forecast. However, with so much uncertainty around Brexit, they warned that the next move could be up or down, even if there was a disorderly Brexit. While it would be expected that Bank Rate could be cut if there was a significant fall in GDP growth as a result of a disorderly Brexit, so as to provide a stimulus to growth, they warned they could also *raise* Bank Rate in the same scenario if there was a boost to inflation from a devaluation of sterling, increases in import prices and more expensive goods produced in the UK replacing cheaper goods previously imported, and so on. In addition, the Chancellor could potentially provide fiscal stimulus to support economic growth, though at the cost of increasing the budget deficit above currently projected levels.

It is unlikely that the MPC would increase Bank Rate in February 2019, ahead of the deadline in March for Brexit. Getting parliamentary approval for a Brexit agreement on both sides of the Channel will take well into spring 2019. However, in view of the hawkish stance of the MPC at their November meeting, the next increase in Bank Rate is now forecast to be in May 2019, (on the assumption that a Brexit deal is agreed by both the UK and the EU). The following increases are then forecast to be in February and November 2020 before ending up at 2.0% in February 2022.

Inflation. The Consumer Price Index (CPI) measure of inflation has been falling from a peak of 3.1% in November 2017 to 2.1% in December 2018. In the November Bank of England quarterly Inflation Report, inflation was forecast to still be marginally above its 2% inflation target two years ahead, (at about 2.1%), given a scenario of minimal increases in Bank Rate.
As for the **labour market** figures in October**,** unemployment at 4.1% was marginally above a 43 year low of 4% on the Independent Labour Organisation measure. A combination of job vacancies hitting an all-time high, together with negligible growth in total employment numbers, indicates that employers are now having major difficulties filling job vacancies with suitable staff. It was therefore unsurprising that wage inflation picked up to 3.3%, (3 month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates less CPI inflation), earnings are currently growing by about 1.2%, the highest level since 2009. This increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. This tends to confirm that the MPC was right to start on a cautious increase in Bank Rate in August as it views wage inflation in excess of 3% as increasing inflationary pressures within the UK economy.

In the **political arena**, the Brexit deal put forward by the Conservative minority government was defeated on 15 January. It is unclear at the time of writing, how this situation will move forward. However, our central position is that Prime Minister May's government will endure, despite various setbacks, along the route to reaching an orderly Brexit though the risks are increasing that it may not be possible to get full agreement by the UK and EU before 29 March 2019, in which case this withdrawal date is likely to be pushed back to a new date. If, however, the UK faces a general election in the next 12 months, this could result in a potential loosening of monetary and fiscal policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up.

USA. President Trump's massive easing of fiscal policy is fuelling a (temporary) boost in consumption which has generated an upturn in the rate of strong growth which rose from

2.2% (annualised rate) in quarter 1 to 4.2% in quarter 2 and 3.5%, (3.0% y/y), in quarter 3, but also an upturn in inflationary pressures. The strong growth in employment numbers and the reduction in the unemployment rate to 3.9%, near to a recent 49 year low, has fed through to an upturn in wage inflation which hit 3.2% in November, However, CPI inflation overall fell to 2.2% in November and looks to be on a falling trend to drop below the Fed's target of 2% during 2019. The Fed has continued on its series of increases in interest rates with another 0.25% increase in December to between 2.25% and 2.50%, this being the fifth increase in 2018 and the ninth in this cycle. However, they did also reduce their forecast for further increases from three to two. This latest increase compounded investor fears that the Fed is over doing the speed and level of increases in rates and that it is going to cause a US recession as a result. There is also much evidence in previous monetary policy cycles of the Fed's series of increases doing exactly that. Consequently, we have seen stock markets around the world falling under the weight of fears around the Fed's actions, the trade war between the US and China and an expectation that world growth will slow.

The tariff war between the US and China has been generating a lot of heat during 2018, but it is not expected that the current level of actual action would have much in the way of a significant effect on US or world growth. However, there is a risk of escalation if an agreement is not reached soon between the US and China.

Eurozone. Growth was 0.4% in quarters 1 and 2 but fell back to 0.2% in quarter 3, though this was probably just a temporary dip. In particular, data from Germany has been mixed and it could be negatively impacted by US tariffs on a significant part of its manufacturing exports e.g. cars. For that reason, although growth is still expected to be in the region of nearly 2% for 2018, the horizon is less clear than it seemed just a short while ago. Having halved its quantitative easing purchases of debt in October 2018 to €15bn per month, the European Central Bank ended all further purchases in December 2018. The ECB is forecasting inflation to be a little below its 2% top limit through the next three years so it may find it difficult to warrant a start on raising rates by the end of 2019 if the growth rate of the EU economy is on a weakening trend.

China. Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems. Progress has been made in reducing the rate of credit creation, particularly from the shadow banking sector, which is feeding through into lower economic growth. There are concerns that official economic statistics are inflating the published rate of growth.

Japan - has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy. It is likely that loose monetary policy will endure for some years yet to try to stimulate growth and modest inflation.

Emerging countries. Argentina and Turkey are currently experiencing major headwinds and are facing challenges in external financing requirements well in excess of their reserves of foreign exchange. However, these countries are small in terms of the overall world economy, (around 1% each), so the fallout from the expected recessions in these countries will be minimal.

INTEREST RATE FORECASTS

The interest rate forecasts provided by Link Asset Services are **predicated on an assumption of an agreement being reached on Brexit between the UK and the EU.** On this basis, while GDP growth is likely to be subdued in 2019 due to all the uncertainties around Brexit depressing consumer and business confidence, an agreement is likely to lead to a boost to the rate of growth in 2020 which could, in turn, increase inflationary pressures in the economy and so cause the Bank of England to resume a series of gentle increases in Bank Rate. Just how fast, and how far, those increases will occur and rise to, will be data dependent. The forecasts in this report assume a modest recovery in the rate and timing of stronger growth and in the corresponding response by the Bank in raising rates.

- 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 were to be 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.

However, there would appear to be a majority consensus in the Commons against any form of non-agreement exit so the chance of this occurring has now substantially diminished.

The balance of risks to the UK

- 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.

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.

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, and due to the election in March of a government which has made a lot of anti-austerity noise. The EU rejected the initial proposed Italian budget and demanded cuts in government spending which the Italian government initially refused. However, a fudge was subsequently agreed, but only by *delaying* the planned increases in expenditure to a later year. This can has therefore only been kicked down the road to a later time. The rating

agencies have started on downgrading Italian debt to one notch above junk level. If Italian debt were to fall below investment grade, many investors would be unable to hold it. Unsurprisingly, investors are becoming increasingly concerned by the words and actions of the Italian government and consequently, Italian bond yields have risen – at a time when the government faces having to refinance large amounts of debt maturing in 2019.

- Weak capitalisation of some **European banks**. Italian banks are particularly vulnerable; one factor is that they hold a high level of Italian government debt - debt which is falling in value. This is therefore undermining their capital ratios and raises the question of whether they will need to raise fresh capital to plug the gap.
- **German minority government.** In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. Then in October 2018, the results of the Bavarian and Hesse state elections radically undermined the SPD party and showed a sharp fall in support for the CDU. As a result, the SPD is reviewing whether it can continue to support a coalition that is so damaging to its electoral popularity. After the result of the Hesse state election, Angela Merkel announced that she would not stand for re-election as CDU party leader at her party's convention in December 2018, (a new party leader has now been elected). However, this makes little practical difference as she is still expected to aim to continue for now as the Chancellor. However, there are five more state elections coming up in 2019 and EU parliamentary elections in May/June; these could result in a further loss of electoral support for both the CDU and SPD which could also undermine her leadership.
- **Other minority eurozone governments.** Spain, Portugal, Ireland, the Netherlands and Belgium all have vulnerable minority governments dependent on coalitions which could prove fragile. Sweden is also struggling to form a government due to the anti-immigration party holding the balance of power, and which no other party is willing to form a coalition with. The Belgian coalition collapsed in December 2018 but a minority caretaker government has been appointed until the May EU wide general elections.
- **Austria, the Czech Republic and Hungary** now form a strongly anti-immigration bloc within the EU while **Italy,** in 2018, also elected a strongly anti-immigration government. Elections to the EU parliament are due in May/June 2019.
- Further increases in interest rates in the US could spark a **sudden flight of investment funds** from more risky assets e.g. shares, into bonds yielding a much improved yield. Throughout the last quarter of 2018, we saw sharp falls in equity markets interspersed with occasional partial rallies. Emerging countries which have borrowed heavily in dollar denominated debt, could be particularly exposed to this risk of an investor flight to safe havens e.g. UK gilts.
- There are concerns around the level of **US corporate debt** which has swollen massively during the period of low borrowing rates in order to finance mergers and acquisitions. This has resulted in the debt of many large corporations being downgraded to a BBB credit rating, close to junk status. Indeed, 48% of total investment grade corporate debt is now rated at BBB. If such corporations fail to generate profits and cash flow to reduce their debt levels as expected, this could tip their debt into junk ratings which will increase their cost of financing and further negatively impact profits and cash flow.
- **Geopolitical risks,** especially North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.

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

- **Brexit –** if both sides were to agree by 29 March a compromise that quickly removed all threats of economic and political disruption and so led to an early boost to UK economic growth.
- **The Fed causing a sudden shock in financial markets** through misjudging the pace and strength of increases in its Fed Funds Rate and in the pace and strength of reversal of QE, which then leads to a fundamental reassessment by investors of the relative risks of holding bonds, as opposed to equities. This could lead to a major flight from bonds to equities and a sharp increase in bond yields in the US, which could then spill over into impacting bond yields around the world.
- 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,** whether domestically generated or imported, returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

Brexit timetable and process

- March 2017: UK government notified the European Council of its intention to leave under the Treaty on European Union Article 50 on 29 March 2019.
- 25.11.18 EU27 leaders endorsed the withdrawal agreement
- Dec 2018 vote in the UK Parliament on the agreement was postponed
- 21.12.18 – 8.1.19 UK parliamentary recess
- 15.1.19 Brexit deal defeated in the Commons vote by a large margin
- By 29.3.19 second vote (?) in UK parliament
- By 29.3.19 if the UK Parliament approves a deal, then ratification by the EU Parliament requires a simple majority
- By 29.3.19 if the UK and EU parliaments agree the deal, the EU Council needs to approve the deal; 20 countries representing 65% of the EU population must agree
- 29.3.19 either the UK leaves the EU, or asks the EU for agreement to an extension of the Article 50 period if the UK Parliament has been unable to agree on a Brexit deal.
- 29.3.19: if an agreement is reached with the EU on the terms of Brexit, then this will be followed by a proposed **transitional period ending around December 2020.**
- UK continues as a full EU member until March 2019 with access to the single market and tariff free trade between the EU and UK. Different sectors of the UK economy may leave the single market and tariff free trade at different times during the transitional period.
- The UK and EU would attempt to negotiate, among other agreements, a bi-lateral trade agreement over that period.
- The UK would aim for a negotiated agreed withdrawal from the EU, although the UK could also exit without any such agreements in the event of a breakdown of negotiations.
- If the UK exits without an agreed deal with the EU, World Trade Organisation rules and tariffs could apply to trade between the UK and EU - but this is not certain.
- On full exit from the EU: the UK parliament would repeal the 1972 European Communities Act.

5.4 CRITERIA FOR SPECIFIED AND NON-SPECIFIED INVESTMENTS

Specified Investments are required to be in Sterling and have a maximum maturity of 1 year and be of ‘high credit quality’.

The definition of ‘high credit quality’ is set out below:

- Investments in Banks incorporated in the UK with a credit rating of at least A/F1, A1 or P1 with a limit of £2m on the amount invested.

- Investments in Banks incorporated outside of the UK but entitled to accept deposits in the UK, per the Bank of England Prudential Regulation Authority list of banks, with a credit rating of at least AA-/F1+/A1+/P1 with a limit of £2m on the amount invested.

- Investments in collective investment schemes, including money market funds, structured as Open Ended Investment Companies (OEIC’s) with a long-term rating of AAA for Constant Net Asset Value (CNAV) funds and Low Volatility Net Asset Value (LVNAV) funds and AAA V1/S1 for Variable Net Asset Values (VNAV).

- Internal Investments less than 6 months, up to agreed limits, in UK Building Societies with an asset basis of over £1 billion.

- Corporate bonds rated AAA of less than one-year duration.

- Local Authorities with a limit of £3m on the amount invested with each.

Non-Specified Investments are all investments over 1 year in duration and/or not meeting the definition of high credit quality listed above.

The Council amended its strategy in the 2018/19 Treasury Management Strategy Document to include Alternative Investment Instruments, such as Property Funds, in the Non-Specified Investment category. The use of these Alternative Investment Instruments can be deemed capital expenditure, and as such will be an application (spending) of capital resources. This Authority will seek guidance on the status of any such fund it may consider using. Appropriate due diligence will also be carried out before investment of this type is undertaken.

The Council limits non-specified treasury investments to 10% of the value of its investment portfolio at the point of investment, with the maximum amount invested being in line with criteria outlined in the Table above.

5.5 INTERNAL COUNTERPARTY LIST 2018/19 AS AT 31 DECEMBER 2018

UK High Street Banks		
UK or Irish bank with presence in UK and a short-term Fitch rating of F1 or higher	**Short-Term Fitch Rating**	**Max Investment**
		£
Lloyds Banking Group		
Lloyds Bank plc (RFB)	F1	2,000,000
Lloyds Bank Corporate Markets (NRFB)	F1	2,000,000
Bank of Scotland plc (RFB)	F1	2,000,000
Others		
Santander UK plc	F1	2,000,000
Barclays Bank UK plc (RFB)	F1	2,000,000
Barclay Bank plc (NRFB)	F1	2,000,000
HSBC UK Bank plc (RFB)	F1+	2,000,000
HSBC Bank plc (NRFB)	F1+	2,000,000

Building Societies				
		Total Assets of Building Society	**Assets > £1 Billion**	**Max Investment**
		£000		**£**
1	Nationwide	227,303,000	Yes	3,000,000
2	Yorkshire	49,063,000	Yes	3,000,000
3	Coventry	41,910,000	Yes	3,000,000
4	Skipton	19,567,000	Yes	3,000,000
5	Leeds	18,937,000	Yes	3,000,000
6	Principality	9,060,000	Yes	3,000,000
7	West Bromwich	5,794,000	Yes	3,000,000
8	Nottingham	3,915,000	Yes	2,000,000
9	Newcastle	3,776,000	Yes	2,000,000
10	Cumberland	2,522,000	Yes	2,000,000
11	National Counties	2,019,000	Yes	2,000,000
12	Progressive	1,788,000	Yes	2,000,000
13	Cambridge	1,234,000	Yes	2,000,000
14	Monmouthshire	1,059,000	Yes	2,000,000
15	Leek United	1,039,000	Yes	2,000,000
16	Saffron	1,018,000	Yes	2,000,000
17	Newbury	1,009,000	Yes	2,000,000

Non UK Banks			
	Long-Term Fitch Rating	**Short-Term Fitch Rating**	**Max Investment** **£**
Abu Dhabi (U.A.E)			
First Abu Dhabi Bank PJSC	AA-	F1+	2,000,000
Australia			
Australia and New Zealand Banking Group Ltd	AA-	F1+	2,000,000
Commonwealth Bank of Australia	AA-	F1+	2,000,000
National Australia Bank Ltd	AA-	F1+	2,000,000
Westpac Banking Corporation	AA-	F1+	2,000,000
Canada			
Bank of Montreal	AA-	F1+	2,000,000
Bank of Nova Scotia	AA-	F1+	2,000,000
Canadian Imperial Bank of Commerce	AA-	F1+	2,000,000
Royal Bank of Canada	AA	F1+	2,000,000
Toronto Dominion Bank	AA-	F1+	2,000,000
Finland			
Nordea Bank Abp	AA-	F1+	2,000,000
Germany			
DZ Bank AG (Deutsche Zentral-Genossenschaftsbank)	AA-	F1+	2,000,000
Netherlands			
Cooperatieve Rabobank U.A.	AA-	F1+	2,000,000
Singapore			
DBS Bank Ltd	AA-	F1+	2,000,000
Oversea Chinese Banking Corporation Ltd	AA-	F1+	2,000,000
United Overseas Bank Ltd	AA-	F1+	2,000,000
Sweden			
Svenska Handelsbanken AB	AA	F1+	2,000,000
Switzerland			
UBS AG	AA-	F1+	2,000,000
U.S.A			
Bank of New York Mellon, The	AA	F1+	2,000,000
Wells Fargo Bank NA	AA-	F1+	2,000,000

UK Local, Police and Fire Authorities	
	Max Investment **£**
UK Local, Police and Fire Authorities	3,000,000

Money Market Funds	Rating	Max Investment £
Amundi Money Market Fund - Short Term (GBP)	AAA	3,000,000
CCLA - Public Sector Deposit Fund	AAA	3,000,000
Goldman Sachs Sterling Liquid Reserves Fund	AAA	3,000,000
Morgan Stanley Liquidity Funds - Sterling Liquidity Fund	AAA	3,000,000

5.6 CURRENT PORTFOLIO POSITION

The overall treasury management portfolio as at 31 March 2018 and for the position as at 31 December 2018 are shown below for both borrowing and investments.

TREASURY PORTFOLIO				
	Actual	Actual	Current	Current
	31.3.18	**31.3.18**	**31.12.18**	**31.12.18**
Treasury investments	**£000**	**%**	**£000**	**%**
Banks				
Lloyds Bank Fixed Term Deposit	0	0%	1,000	2%
Bank of Scotland Fixed Term Deposit	1,000	3%	1,000	2%
Bank of Scotland Call Account	0	0%	900	2%
Building Societies - unrated				
National Counties Building Society	0	0%	2,000	4%
Nottingham Building Society	0	0%	2,000	4%
West Bromwich Building Society	0	0%	2,000	4%
Building Societies - rated				
Principality Building Society	0	0%	3,000	6%
Yorkshire Building Society	0	0%	2,000	4%
Local Authorities				
Eastleigh Borough Council	0	0%	3,000	6%
Money Market Funds				
Amundi Money Market Fund - short term	2,250	7%	3,000	6%
CCLA - Public Sector Deposit Fund	0	0%	2,900	6%
Total managed in house	**3,250**	**10%**	**22,800**	**43%**
Money Market Funds*				
Payden & Rygel Sterling Reserve Fund	15,451	47%	15,409	29%
Royal London Asset Management Cash Plus Fund	14,457	44%	14,446	27%
Property Funds	0	0%	0	0%
Total managed externally	**29,908**	**90%**	**29,855**	**57%**
Total treasury investments	**33,158**	**100%**	**52,655**	**100%**
Treasury external borrowing				
Local Authorities				
Leicester City Council	4,500	5%	0	0%
PWLB	80,601	95%	88,115	100%
Total external borrowing	**85,101**	**100%**	**88,115**	**100%**
Net treasury investments / (borrowing)	**(51,943)**	**0.0%**	**(35,460)**	**0.0%**
** market value*				

5.7 THE TREASURY MANAGEMENT ROLE OF THE SECTION 151 OFFICER

The S151 (responsible) officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers.

The above is a list of specific responsibilities of the S151 officer in the 2017 Treasury Management Code. However, implicit in the recent changes in both codes, is a major extension of the functions of this role, especially in respect of non-financial (or non-treasury/ other) investments, (which CIPFA has defined as being part of treasury management). The following are examples of the major extension in the functions of this role: -

- preparation of a capital strategy to include capital expenditure, capital financing, non-financial (or non-treasury/ other) investments and treasury management.
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money
- ensuring that due diligence has been carried out on all treasury and non-financial (or non-treasury/ other) investments and is in accordance with the risk appetite of the authority
- ensuring that the authority has appropriate legal powers to undertake expenditure on non-financial (or non-treasury/ other) assets and their financing
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial (or non-treasury/ other) investments and long term liabilities
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following*: -*
    - *Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios;*

- *Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments;*

- *Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making;*

- *Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken;*

- *Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.*