INTEGRATED PLAN

PART D – TREASURY MANAGEMENT STRATEGY

Contents

1. Background

1.1 Treasury management is the management of the Council's cash flows, borrowing and investments, and the associated risks. The Council has significant investment and borrowing balances and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Council's prudent financial management.

1.2 Under the Local Government Act 2003, local authorities must have regard to statutory proper practices in their treasury management and borrowing activities.

1.3 These are set out in the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code)

1.4 This report demonstrates that the Council has fulfilled its legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

1.5 As in previous years, this report proposes the 2019/20 Treasury Management Strategy, Borrowing Strategy, and Treasury Management indicators that will be set and monitored throughout 2019/20.

2. External Context for the Treasury Management Strategy

The Council's independent Treasury Advisors, Arlingclose, have provided the following information on the external context for the TMSS.

2.1. Economic Background - Provided by Arlingclose

2.1.1. The UK's progress negotiating its exit from the European Union, together with its future trading arrangements, will continue to be a major influence on the Council's treasury management strategy for 2019/20.

2.1.2. UK Consumer Price Inflation (CPI) for October was up 2.4% year on year, slightly below the consensus forecast and broadly in line with the Bank of England (BoE)'s November Inflation Report. The most recent labour market data for October 2018 showed the unemployment rate up slightly to 4.1% while the employment rate of 75.7% was the joint highest on record. The 3-month average annual growth rate for pay excluding bonuses was 3.3% as wages continue to rise steadily. Adjusted for inflation, real wages grew by 1.0%, a level still likely to have little effect on consumer spending.

2.1.3. The rise in quarterly GDP growth to 0.6% in Q3 from 0.4% in the previous quarter was due to weather-related factors boosting overall household consumption and construction activity over the summer following the weather-related weakness in Q1. At 1.5%, annual GDP growth continues to remain below trend. Looking ahead, the BoE, in its November Inflation Report, expects GDP growth to average around 1.75% over the forecast period, providing the UK's exit from the EU is relatively smooth.

2.1.4. Following the Bank of England's decision to increase Bank Rate to 0.75% in August, no changes to monetary policy have been made since. However, the Bank expects that should the economy continue to evolve in line with its November forecast, further increases in Bank Rate will be required to return inflation to the 2% target. The Monetary Policy Committee continues to reiterate that any further increases will be at a gradual pace and limited in extent.

2.1.5. While US growth has slowed over 2018, the economy continues to perform robustly. The US Federal Reserve continued its tightening bias throughout 2018, pushing rates to the current 2%-2.25% in September. Markets continue to expect one more rate rise in December, but expectations are fading that the further hikes previously expected in 2019 will materialise as concerns over trade wars drag on economic activity.

2.2. Interest Rate Forecast - Provided by Arlingclose

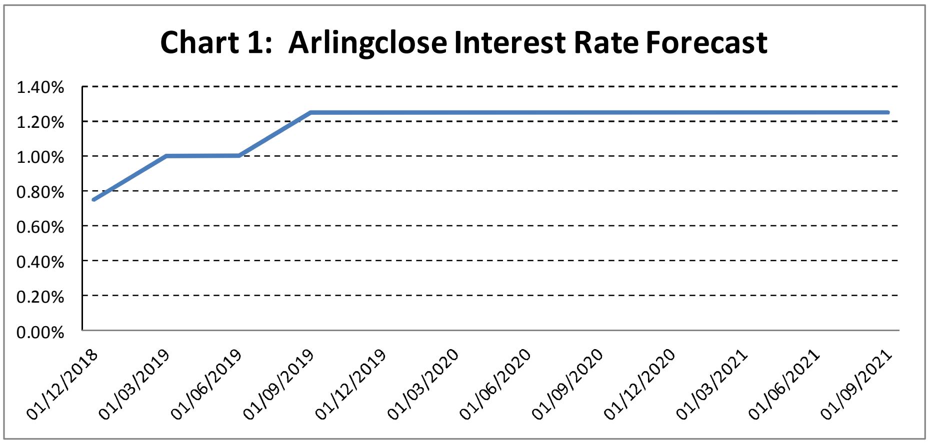
2.2.1. Following the increase in Bank Rate to 0.75% in August 2018, the Council's treasury management adviser Arlingclose is forecasting two further 0.25% increases during 2019 to take official UK interest rates to 1.25%. The Bank of England's MPC has maintained expectations for slow and steady rate rises over the forecast period. The MPC continues to have a bias towards tighter monetary policy but is reluctant to push interest rate expectations too strongly. Arlingclose believes that MPC members consider both that ultra-low interest rates result in other economic problems, and that higher Bank Rate will be a more effective policy weapon should downside Brexit risks crystallise when rate cuts will be required.

2.2.2. The UK economic environment remains relatively soft, despite seemingly strong labour market data. The Arlingclose view is that the economy still faces a challenging outlook as it exits the European Union and Eurozone growth softens.

2.2.3. Whilst assumptions are that a Brexit deal is struck and some agreement reached on transition and future trading arrangements before the UK leaves the EU, the possibility of a "no deal" Brexit still hangs over economic activity *(at the time of writing this commentary in early December 2018).* As such, the risks to the interest rate forecast are considered firmly to the downside.

2.2.4. Gilt yields and hence long-term borrowing rates have remained at low levels but some upward movement from current levels is expected based on Arlingclose's interest rate projections, due to the strength of the US economy and the ECB's forward guidance on higher rates. 10-year and 20-year gilt yields are forecast to remain around 1.7% and 2.2% respectively over the interest rate forecast horizon, however volatility arising from both economic and political events are likely to continue to offer borrowing opportunities.

2.2.5. Chart 1 (overleaf), shows Arlingclose's central case for UK Bank Rate during 2019/20. This illustrates their view that rates are likely to rise twice during the year, in line with the Bank of England's forecasts.



2.2.6. For the purpose of setting the budget, it has been assumed that new investments will be made at an average rate of 0.82%, and that new long-term loans will be borrowed at an average rate of 2.82%.

2.3. **Credit Outlook - Provided by Arlingclose**

2.3.1. The big four UK banking groups have now divided their retail and investment banking divisions into separate legal entities under ring-fencing legislation. Bank of Scotland, Barclays Bank UK, Lloyds Bank, National Westminster Bank, Royal Bank of Scotland and Ulster Bank are the ring-fenced banks that now only conduct lower risk retail banking activities. Barclays Bank, HSBC Bank, Lloyds Bank Corporate Markets and NatWest Markets are the investment Banks. Credit rating agencies have adjusted the ratings of some of these banks with the ring fenced banks generally being better rated than their non-ring fenced counterparts.

2.3.2. The Bank of England released its latest report on bank stress testing, illustrating that all entities included in the analysis were deemed to have passed the test once the levels of capital and potential mitigating actions presumed to be taken by management were factored in. The BoE did not require any bank to raise additional capital.

2.3.3. European Banks are considering their approach to Brexit, with some looking to create new UK subsidiaries to ensure they can continue trading here. The credit strength of these new banks remains unknown, although the chance of parental support is assumed to be very high if ever needed. The uncertainty caused by protracted negotiations between the UK and EU is weighing on the creditworthiness of both UK and European banks with substantial operations in both jurisdictions.

3. Local Context for Treasury Management Strategy

The following information outlines the background to the Council's existing and planned activities for 2019/20.

3.1. **Current Treasury Position for Borrowing**

3.1.1. Table 1 (overleaf) shows the borrowing position at 31 March 2018 and the estimated position at 31 March 2019. No additional long term borrowing was undertaken in 2018/19 since cash balances were used to fund capital expenditure in the short-term.

3.1.2. Table 1 also shows the sources of borrowing and the maturity structure of the loans. Borrowing is sourced from the UK Government's Public Works Loans Board [PWLB] and commercial banks. PWLB loans have a fixed maturity date. Commercial bank loans are a mixture of fixed term borrowing and Lender's Option, Borrower's Option [LOBO] loans.

3.1.3. The Options on LOBO loans represent an inherent risk that the loan may be called for repayment earlier than the ultimate maturity date of the loan. During 2018/19, two LOBO loans with a total value of £30m held with RBS were refinanced under a prepayment agreement. Replacement borrowing was sourced from the PWLB at a lower interest rate, resulting in an overall cost saving.

3.1.4. As a result of the refinancing action taken, the Council's exposure to this risk is now £19.4m.

Table 1: Treasury Position for Borrowing

Maturity Analysis as at 31 March	2017/18 Sources of Borrowing				2018/19 Sources of Borrowing			
	Actual	PWLB	LOBO	Commercial	Estimated	PWLB	LOBO	Commercial
	£m	£m	£m	£m	£m	£m	£m	£m
Under 2 years	**0.25**	0.25			**6**	6.00		
2 to 10 years	**19.90**	19.90	-	-	**36.9**	36.93	-	-
10 to 30 years	**43.93**	43.93	-	-	**51.2**	51.15	-	-
30 years or later	**194.70**	39.20	49.40	106.10	**164.70**	39.20	19.40	106.10
Total:	**258.78**	**103.28**	**49.40**	**106.10**	**258.78**	**133.28**	**19.40**	**106.10**

3.1.5. Charts 2 and 3 (overleaf) show the maturity profile of the Council's existing PWLB, LOBO and commercial loans.

3.1.6. Chart 2 reflects the current maturity profile, while Chart 3 shows the profile were the LOBO loans to be called at the next option date.

3.1.7. Chart 3 highlights the inherent uncertainty around the existing terms of the remaining LOBO loans and the risk of early repayments. The Council's treasury advisor predicts that LOBOs are very unlikely to be called in the short to medium term based on current interest rate forecasts.

3.1.8. In the event that LOBOs were to be called, the Council would seek to replace borrowing from sources listed in section 4.1.9 at the most economic rate.

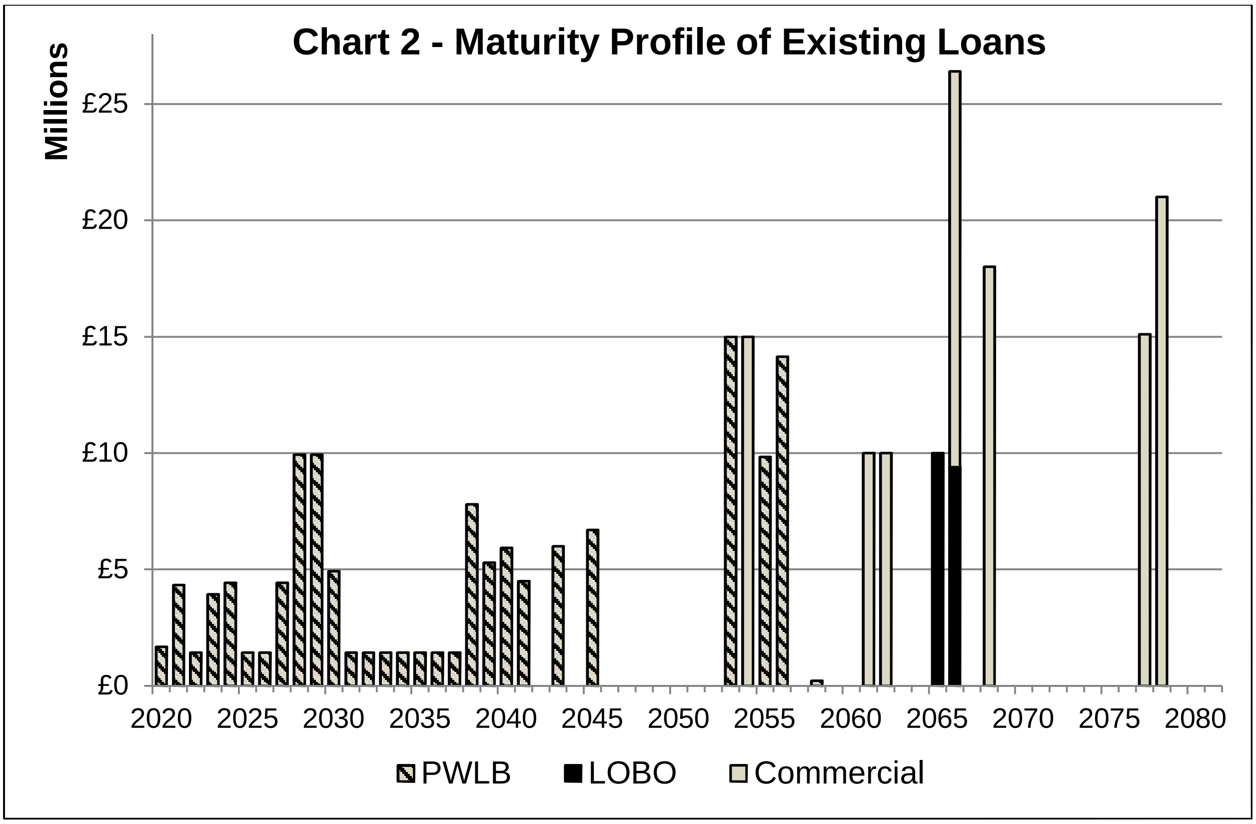


Chart 2 - Maturity Profile of Existing Loans
Millions
£25
£20
£15
£10
£5
£0
2020
2025
2030
2035
2040
2045
2050
2055
2060
2065
2070
2075
2080
PWLB
LOBO
Commercial

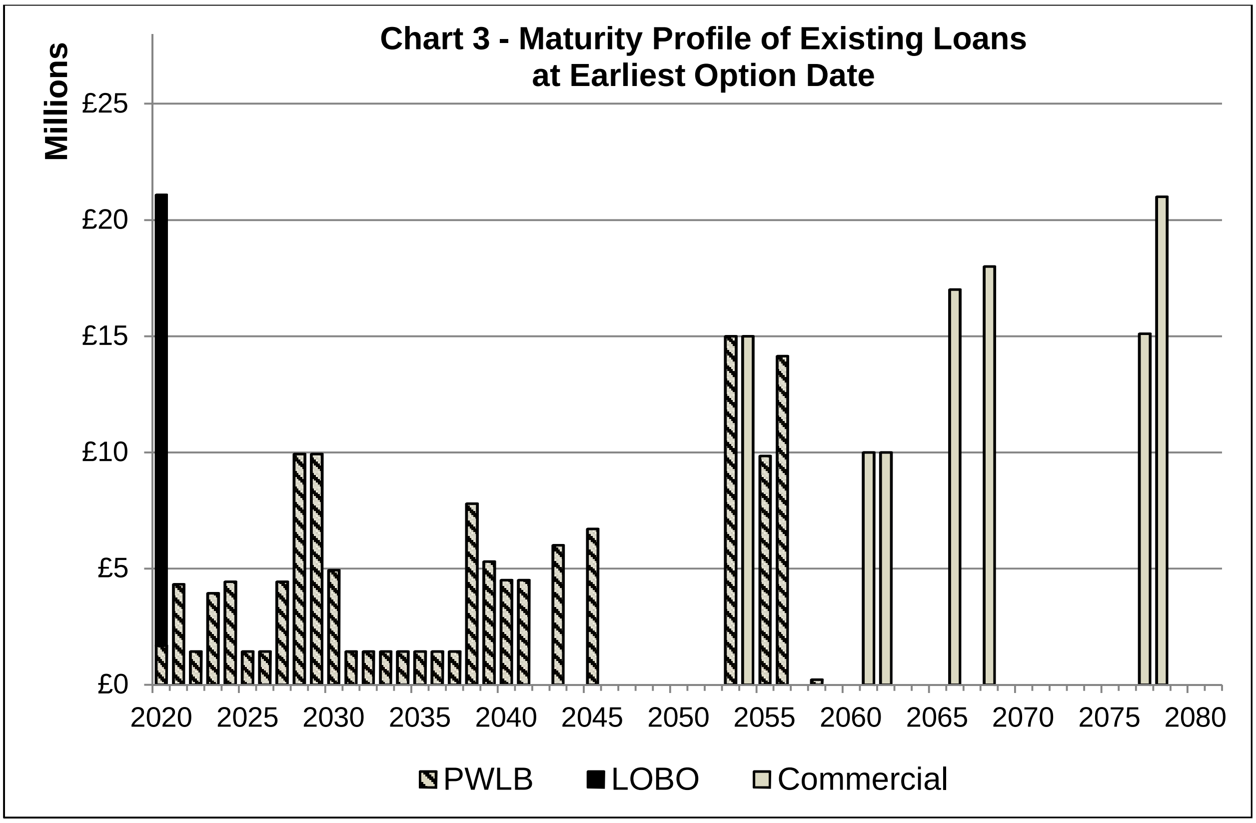


Chart 3 - Maturity Profile of Existing Loans
at Earliest Option Date
Millions
£25
£20
£15
£10
£5
£0
2020
2025
2030
2035
2040
2045
2050
2055
2060
2065
2070
2075
2080
PWLB
LOBO
Commercial

3.2. **Current Treasury Position for Investments**

3.2.1. Table 2 shows the investment position at 31 March 2018 and the estimated position at 31 March 2019.

Table 2: Treasury Position for Investment

	2017/18 Actual £000	2018/19 Estimated £000
Iceland Investments	612	601
Instant Access	70,993	28,782
95 Day Notice Account	0	10,000
Long Term MMFs	17,500	17,500
Fixed Term	23,000	20,000
Pooled Funds	30,000	30,000
Total Lending at 31 March	**142,105**	**106,883**

3.3. **Capital Financing Requirement**

3.3.1. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement [CFR], while usable reserves and working capital are the underlying resources available for investment.

3.3.2. The Council has an increasing CFR due to the capital programme, and overall investment balances are expected to reduce to a minimal level over the forecast period. As a result borrowing of up to £300m will be required over the forecast period.

3.3.3. The Council's current strategy is to maintain borrowing and investments below their underlying levels. This approach is referred to as 'Internal Borrowing'. Further detail about Internal Borrowing is included in Section 4.

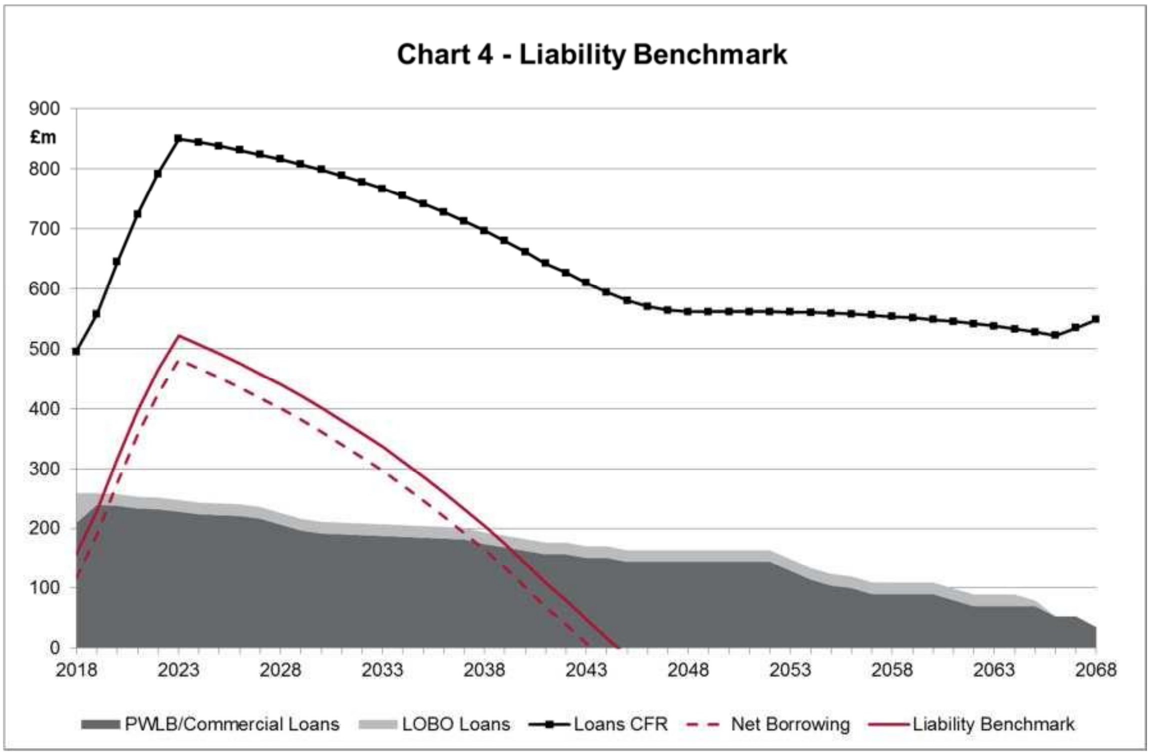
3.4. **Liability benchmark**

3.4.1. To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes that a minimum level of investments is reached during 2019/20 and maintained thereafter, and that the overall levels of reserves and working capital remain broadly stable.

Table 3 – Liability Benchmark

	2017/18 Actual £000	2018/19 Forecast £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000	2022/23 Estimate £000
Loans CFR	503,887	566,330	646,430	729,845	794,869	837,430
Projected Borrowing	258,779	258,779	320,478	414,177	496,733	553,105
Liability benchmark	156,592	229,869	316,794	396,477	464,241	522,027

3.4.2. Following on from the medium term forecasts in table 3 above, the long-term liability benchmark assumes capital expenditure funded by borrowing in each year, minimum revenue provision on new capital expenditure based on a 25 year asset life, and income, expenditure and reserves all increasing by inflation of 2.5% a year. This is illustrated in chart 4, below.



3.4.3. In this chart, the Council's borrowing need is illustrated by the clear area between the Liability Benchmark and the shaded area representing existing loans.

3.4.4. Actual borrowing arranged is likely to differ from the liability benchmark depending on actual cash balances, the rate at which the capital programme is delivered, and actual use of reserves and working capital.

4. Proposed Treasury Management Strategy

4.1. Borrowing Strategy

4.1.1. The Council's objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required.

4.1.2. The Capital Programme for 2019/20 – 2022/23 includes a requirement for additional borrowing funded capital expenditure of £300m. As Capital Assets by nature bring benefits over multiple years, their financing is long-term in nature.

4.1.3. In recent years the Council followed a policy of using internal borrowing where possible to finance unfunded elements of the capital programme. Internal Borrowing is the use of short-term cash surpluses (represented primarily by the council's reserves and provisions) to fund Capital Projects. This is a prudent approach which reduces the cost of interest paid on borrowing in the short term.

4.1.4. In the long term, as reserves and provisions are used it will be necessary to meet the accumulated borrowing requirement using long-term loans from external sources such as the PWLB,

4.1.5. Whilst the Bank of England is expected to increase interest rates during 2019/20, as noted in section 3, the interest rate environment is expected to remain at levels which are low by historical standards for the foreseeable future. In this environment, where short term borrowing is available at lower cost than long term loans, internal borrowing delivers value to the council.

4.1.6. The risk of this approach is that future interest rate increase result in a higher long term borrowing cost, relative to the cost of borrowing at current long-term rates. Officers will monitor interest rates in conjunction with its treasury advisor to ensure that an efficient balance of risk and cost is achieved.

4.1.7. Accordingly it is proposed that the cost of long-term financing will be managed by meeting the council's borrowing requirement from a combination of rolling shorter term loans (0-5 years duration), combined with long term borrowing (20+ years duration).

4.1.8. This strategy meets the primary aim of security by limiting the value of surplus cash available for deposits.

4.1.9. The approved sources of long term and short term borrowing will be:

- Public Works Loan Board (PWLB)
- Any institution approved for investments in the Lending Policy
- Any other bank or building society authorised to operate in the UK
- Any Other UK Public Sector Body
- Capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues
- UK public and private sector pension funds (except for Hertfordshire Pension Fund)

4.1.10. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- Leasing
- Private Finance Initiatives
- Hire purchase
- Sale and leaseback

4.2. Treasury Investment Strategy

4.2.1. The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. The Council also holds funds on behalf of the Hertfordshire Local Enterprise Partnership, in its capacity as the Accountable Body. These are managed alongside the Council's own cash.

4.2.2. In the past 12 months, the Council's investment balance has ranged between £75m and £212m, and although balances are expected to reduce over the course of the year a similar level of variability is expected.

4.2.3. The CIPFA Code requires the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving low investment income.

4.2.4. Whilst currently deemed unlikely, were an economic downturn to occur in 2019/20 the Bank of England could choose to set a bank rate at or below zero. This would likely feed through to negative rates on all low-risk short-term investment options. In this event, security would be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

4.2.5. No changes are proposed to the list of approved counterparties for 2019/20 and the Council will continue to pursue the strategy of a diversified investment portfolio, in order to manage its credit risk exposure and liquidity requirements.

4.2.6. The use of long-term investments as part of a diversified portfolio which addresses a range of credit and counterparty risks may, when the impact of the uncertain timing of receipts and payments are considered, give rise to short-term borrowing requirements to provide required liquidity.

4.2.7. With due regard to this risk, £50m is deemed to be available for long-term investment and £30m has been invested in a range of pooled funds. These funds are subject to market value fluctuations and are therefore intended to be held for the long-term to generate income and mitigate the risk of capital value variation. The target for these investments was to generate a yield of 4% per annum. During 2018/19 the overall return on these funds exceeded 4.50%. It is intended that these investments will continue to be held throughout 2019/20.

4.2.8. Under the new IFRS9 accounting standard, the accounting for certain investments depends on the Council's "business model" for managing them. The Council aims to achieve value from its internal managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost

4.2.9. Further information on the approved instruments is set out in Appendix 2, including specific limits linked to credit ratings.

4.3. Liquidity Management

4.3.1. The Council creates an annual cash-flow forecast based on known and estimated patterns of income and expenditure drawn from a variety of internal and external sources. The forecast is based on prudent assumptions, to identify periods of liquidity pressure or surplus cash.

4.3.2. The forecast allows the Council to estimate durations for which surplus cash may prudently be committed and/or the likely short-term borrowing requirement for the year ahead. This minimises the risk that borrowing for liquidity purposes has to be arranged at short notice and on unfavourable terms, and allows officers to balance security and liquidity risks to use cash resources efficiently.

4.4. Investment Limits

4.4.1. Overall investment limits are set with regard to the council's forecast cash balances and forecast revenue reserves. This restricts the Council's exposure to credit risk in the event of a single default. The Council's investment limits are set out in Appendix 2: 2019/20 Lending Policy.

4.4.2. The proposed 2019/20 Treasury Management Strategy has considered a full range of risks, including credit ratings, exposure to bail-in, market conditions and the outlook for interest rates, and Officers will apply the strategy to ensure that security of deposits is the prime consideration.

4.4.3. In agreeing the proposed strategy, Members should be aware that there is always a risk of default of counterparties other than the Debt Management Office which is guaranteed by the government.

4.5. Security

4.5.1. Specific investment limits are set by reference to the lowest published long-term credit rating from a selection of external rating agencies. Where available, credit rating relevant to the specific investment or class of investment is used; otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors, including external advice, will be taken into account

4.5.2. The Council understands that credit ratings are a good indicator of investment default risk, but are rating agencies' expressed opinions and not a perfect prediction. Therefore, Officers will use other sources of information; including credit default swap ratings and equity prices, to determine the credit quality of an organisation. These are detailed in Appendix 2, section 4 of the proposed Lending Policy.

4.5.3. No investments will be made with an organisation if there are substantive doubts about its credit quality even though it may meet the Lending Policy criteria. This means the Lending Policy applied operationally may at times be more restrictive than is formally stated

5. Treasury Management Indicators and Reporting

5.1. Treasury Management Indicators

5.1.1. The CIPFA Code requires the Council to set performance indicators to assess the treasury function over the year.

5.1.2. The indicators, which will set limits against specific criteria, are outlined overleaf. Further detail, including a description of how 2019/20 indicators differ from previous years is provided in Appendix 4.

Ref	Category	Description
TM1	Security of Investments	Weighted Average Credit Score
TM2	Liquidity	Total Cash available with 1 month
TM3	Interest Rate Exposure	Upper limits on the revenue cost impact of a +/- 1% change in interest rates
TM4	Maturity Structure of Borrowing	Upper and lower limits on the proportion of the loan portfolio maturing by time period
TM5	Price Risk	Upper limits on the amount which may be invested for periods over 1 year

5.2. Other Indicators

5.2.1. In addition to the indicators listed above, the following indicators will also be used to provide additional context and performance measures.

Indicator	Category	Presentation
Weighted Average Maturity of Investment Portfolio	Liquidity	X Days to Maturity
Return on Lending vs 7 Day LIBID Rate	Yield	Actual %, Benchmark %, Variance %
Average rate payable on borrowing portfolio	Cost	Interest Paid/Average Borrowing *100 = Actual %
Breaches of Lending Policy	Compliance	Number & Narrative Explanation
Types of Instruments Used (Excludes MMF Funds)	Compliance	Number and value of new investments and maturities by instrument type.

5.3. Treasury Management Reporting

5.3.1. Officers provide a quarterly monitoring report to Cabinet which is included as part of the budget monitoring process.

5.3.2. The Audit Committee will receive a mid-year report and a report at the end of the financial year on treasury management activities and performance.

5.3.3. These reports will incorporate the Treasury Management Indicators outlined above and the Prudential Indicators set out in Appendix A to the Council's Capital Strategy 2019/20. A summary statement of the indicators to be reported is provided in Appendix 4.

6. Financial Implications and Sensitivity to Interest Rates

6.1.1. The financial implications of treasury management activity are included in the Capital Financing and Interest on Balances budget which is part of the Council's overall budget being considered elsewhere in this IP pack. This section highlights the financial implications of the Treasury Management Strategy described in section 4.

6.1.2. Table 5 (overleaf) shows forecasts of interest payable on borrowing split between existing commitments and a forecast of additional interest expected to be paid as a result of the proposed new borrowing requirement set out in section 2.

Table 5: Forecasts of interest payable on borrowing

	2018/19 Forecast £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000	2022/23 Estimate £000
Cumulative Additional borrowing	0	63,377	159,722	239,383	298,255
Funded by:					
Long-term Borrowing	0	0	31,688	111,550	199,553
Short-term Borrowing	0	63,377	128,034	127,833	98,702
Interest Cost of Borrowing:					
Interest committed as at 31/3/2017	12,106	11,770	11,711	11,515	11,455
From additional long-term borrowing	0	0	922	3,296	5,957
From additional short-term borrowing	0	397	841	1,889	934
Total Estimated Interest Payable	**12,106**	**12,167**	**13,473**	**16,700**	**18,345**

6.1.3. Table 6 shows the interest the Council expects to earn on investments in the forthcoming four financial years. The Council will continue to diversify the risk of managing an investment portfolio by maintaining low investment balances. Cashflow will be maintained on a short term basis to meet known cash outflows in the next month, plus a contingency to cover unexpected cash flows over the same period.

Table 6: Forecasts of Interest on Investments

	2018/19 Forecast £000's	2019/20 Estimate £000's	2020/21 Estimate £000's	2021/22 Estimate £000's	2022/23 Estimate £000's
Forecast Average Balance	110,000	96,000	82,500	72,000	69,000
Forecast Interest Rate Short-term	0.79%	0.82%	1.06%	1.15%	1.15%
Forecast Interest Rate Long-term	4.70%	4.50%	4.50%	4.25%	4.00%
Short-term interest earned	866	542	554	485	448
Long-term interest earned	1,410	1,350	1,350	1,275	1,200
Total Interest earned forecast	**2,276**	**1,892**	**1,904**	**1,760**	**1,648**

6.1.4. Changes to interest rates have an impact on treasury management activity. Table 7 (overleaf) demonstrates the impact of a 1% rise or fall in interest rates, based on budgeted activity levels.

Table 7 Sensitivity to a 1% Increase/Decrease in Interest Rates

	2018/19 Estimated Impact 1% Rate Increase Cost / (Saving) £000	**2018/19 Estimated Impact 1% Rate Decrease Cost / (Saving) £000**
Interest on borrowing	316	(286)
Investment income	(1,505)	698
Total Revenue Impact	**(1,189)**	**412**

6.1.5. The saving resulting from a reduction in interest rates are not equal to the cost of an increase in rates because there is a presumed minimum interest rate payable on borrowing, below which rates will not fall. At prevailing low rates a 1% increase rate reduction would result in a reduction of less than 1% in new borrowing rates.

6.1.6. The Council seeks to minimise the interest rate risk by agreeing fixed rates for new long term borrowing in the majority of cases, however in the current financial climate, as outlined in section 4.1.5, there are opportunities for cost savings by taking advantage of lower rates on short term borrowing. In setting the budget for short term interest earned or paid the Council takes advice about the likely pattern of interest rates over the coming financial year and models the impact of a change in rates as shown in Table 7 to illustrate the risk.

7. Treasury Management Training and Advice

MHCLG investment guidance requires the Council to note the following matters each year as part of the annual strategy:

7.1. Treasury Management Advisers

7.1.1. The Council contracts with Arlingclose to provide advice and information relating to its investment and borrowing activities. This contract began in February 2017, following a competitive tender process.

The services provided are reviewed through quarterly meetings and include:

- Advice and guidance on relevant policies, strategies and reports
- Advice on investment decisions
- Notification of credit ratings and changes
- Other information on credit quality
- Advice on debt management decisions
- Technical accounting advice
- Reports on treasury performance
- Forecasts of interest rates; and
- Training courses.

7.2. **Investment training**

7.2.1. Training on treasury management will be provided in 2019/20 by the Council's treasury advisors and other professional bodies. Training will be provided to induct new members and to ensure that members continuing in their roles in relation to treasury management keep their knowledge and skills up to date.

7.2.2. All treasury management Officers are required to attend an introductory course run by the treasury advisors. Officers new to treasury management are shadowed by more experienced Officers until they are judged to be competent to undertake transactions themselves and demonstrate a good understanding of the Council's treasury policies. To keep Officers' knowledge up to date, the Council is a member of the CIPFA Treasury Management Network which provides information and training to its members. In addition the Council's advisers provide continuous guidance, updates and training and Officers will attend conferences and courses related to the treasury function.

7.2.3. Treasury Officers will maintain Continuing Professional Development records in order to allow the Council to maintain its Professional Client status under MiFID II regulations (see section 8 for details).

8. Markets in Financial Instruments Directive

8.1. The Council maintains Professional Client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Director of Resources believes this to be the most appropriate status.

8.2. The following indicators will be reported to allow the Audit Committee to monitor the ongoing eligibility of the Council for elective professional status and that meets the criteria set by the FCA to elect to be a professional investor:

TM6 MiFID Compliance Indicators

TM6 (a) Investment Balance at Reporting Date	
Minimum Balance Limit	£10m
TM6 (b) Number of Officers with at least 1 Year relevant experience	
Regulatory Minimum	1

9. Treasury Management for Other Organisations

9.1. HCC currently provides treasury management services for three other organisations, the Hertfordshire Pension Fund, the Hertfordshire Police and Crime Commissioner (PCC) and the Hertfordshire Local Enterprise Partnership (LEP).

9.2. Hertfordshire PCC and the Pension Fund cash balances are held in separate bank accounts and separate investments are maintained for each in accordance with their respective cash flows. These investments are made in accordance with their own Treasury Management Strategies which are maintained separately and agreed by the PCC and the Pensions Committee respectively. Reporting arrangements are similar to the Council's with a mid-year and end of year report being provided on activity within the year in addition to the Strategy.

9.3. The Hertfordshire LEP is not yet a separate legal entity and HCC is the Accountable body. Currently LEP balances are held with the Council's and invested as part of the wider pool. Separate information is maintained on LEP cash flows, and appropriate interest is paid over to the LEP annually. Any specific investments made on behalf of the LEP are therefore covered by the HCC Treasury Management Strategy. The Treasury Management Strategy was amended in 2016/17 is to enable investments in instruments linked to economic growth but which do this in such a way to manage risk.

9.4. In line with government guidance, Hertfordshire LEP is pursuing a process of independent incorporation. This will not change the Council's Accountable Body status, and so the current arrangements set out above will continue. If new guidance emerges to the effect that fully separate treasury arrangements are required, these will be set up in parallel to those for the Pension Fund and PCC.

APPENDIX 1 TREASURY MANAGEMENT POLICY STATEMENT

The Council's financial regulations require it to create and maintain a Treasury Management Policy statement, stating the policies, objectives and approach to risk management of its treasury activities, as a cornerstone for effective treasury management.

1. Definition

1.1. The Council defines its treasury management activities as the:

- Management of the Council's investments and cash flows; its banking arrangements; money market and capital market transactions
- Effective control of the risks associated with those activities
- Pursuit of optimum performance consistent with those risks

2. Risk management

2.1. The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

3. Value for money

3.1. The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

4. Borrowing policy

4.1. The Council values revenue budget stability and will therefore borrow the majority of its long term funding needs at long term fixed rates of interest. Short term and variable rate loans will only be borrowed to the extent that they either offset short term and variable rate investments or can be shown to produce revenue savings.

4.2. The Council will set an affordable borrowing limit each year in compliance with the Local Government Act 2003, and will have regard to the CIPFA Prudential Code for Capital Finance in Local Authorities when setting that limit. It will also set limits on its exposure to changes in interest rates and limits on the maturity structure of its borrowing in the Treasury Management Strategy report each year.

4.3. Borrowing will be undertaken only to fund capital expenditure and when it is necessary to manage short term cashflow requirements. The Chief Financial Officer, in consultation with the Council's treasury management advisers, will take the most appropriate form of borrowing depending on prevailing interest rates. The maturity profile of the borrowing portfolio will also be taken into consideration when deciding the duration of borrowing to ensure an even spread of loans and avoid a concentration of loans maturing at the same time requiring refinancing in a high interest rate environment.

4.4. The borrowing portfolio will be continually monitored in consultation with the Council's treasury management advisers to identify rescheduling opportunities which could reduce interest costs. The potential refinancing and interest rate risks arising from rescheduling would be considered at the same time to determine whether it is appropriate.

5. Treasury Investment Policy

5.1. The Council's primary objectives for the investment of its surplus funds are to protect the principal sums invested from loss, and to ensure adequate liquidity so that funds are available for expenditure when needed. The generation of investment income to support the provision of local authority services is an important, but secondary, objective.

5.2. The Council will have regard to the Ministry of Housing, Communities and Local Government Guidance on Local Government Investments and will approve a Lending Policy each year as part of the Treasury Management Strategy. The strategy will set criteria to determine suitable organisations with which cash may be invested, limits on the maximum duration of such investments and limits on the amount of cash that may be invested with any one organisation.

6. Policy on Use of Financial Derivatives

6.1. The CIPFA Code requires local authorities to clearly detail their policy on the use of derivatives in the annual strategy.

6.2. Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans).

6.3. The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) to manage specific risks such as currency or interest rate risk and where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, through entering into such contracts, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Officers will seek professional advice and opinion from the Treasury advisers and legal services on proposals to use any form of derivative contracts.

6.4. Financial derivative transactions that are arranged will only be with organisations that meet the Council's approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

APPENDIX 2 2019/20 LENDING POLICY

1. Background

1.1. The Council's Lending Policy seeks to address Treasury Management risks by setting criteria such as:

- Monetary limits on terms of investment with any one single counterparty;
- Monetary and time limits for investment with counterparty sectors or countries;
- Group limits on counterparty sectors;
- Diversifying investments across a number of different financial instruments and asset classes;
- Maximum value as a single transaction for fixed term investments; and
- Using financial data such as credit ratings to assess the creditworthiness of counterparties.

1.2. No changes are proposed to the approved list of financial instruments for investment purposes for the 2019/20 Lending Policy. These are as follows:

- Call and notice accounts
- Fixed Term deposits and loans
- Treasury Bills
- Certificate of deposits
- Shares in Money Market Funds – short and long term duration
- Commercial Paper
- Other Pooled Funds (including bond, equity and property funds)
- Loan Agreements with UK Registered Providers of social housing
- Government and Corporate Bonds
- Covered Bonds
- Reverse Repurchase Agreements
- Other collateralised arrangements
- Equity shares in the Local Capital Finance Company
- Investments in small corporates via peer to peer lending through on-line portals or specialist lending vehicles.

1.3. Further information on the approved instruments is set out in Appendix 3. Investment limits are set according to approved instrument type, with additional counterparty limits set in the next section.

2. Investment Limits

2.1. Overall Investment Limits

2.1.1. Table A provides details of the overall investment limits which have been set for the Council. The limits in table A have been set with regard to the council's balance sheet and cashflow forecasts. The aim of the following limits is to limit the proportion of the council's available reserves at risk in the event of a single default, and the maximum amount that may be lent to any one organisation (other than the UK government) is £15m.

Table A – Overall Investment Limits

	Cash limit
UK Central Government	Unlimited
Any single organisation (Except UK Central Government)	£15m each
Any group of organisations under the same ownership	£15m per group
Any group of pooled funds under the same management	£15m Per Fund £35m per manager
Negotiable instruments held in a broker's nominee account	£20m per broker
Foreign countries	£10m per country
Registered providers and registered social landlords	£30m in total
Unsecured investments with building societies	£2m in total
Loans to unrated corporates	£5m in total
Low Volatility Net Asset Value (LVNAV) Money market funds	£15m per fund £100m in total

2.1.2. Money Market and Pooled Fund investments have an individual limit of £15m per fund. Whilst these are unsecured investments, the higher limit is appropriate because the diversified nature of the underlying investments of the fund limit the Council's exposure to the default of a single entity.

2.2. Approved Counterparties and Limits

2.2.1. The Council may invest in any of the counterparty types in Table B (overleaf), subject to the cash limits (per counterparty) and the time limits shown. The credit rating criteria in Table B is based on Fitch's long term credit ratings.

Definitions to support reading of Table B may be found in section 2.4, below.

Table B: Approved Investment Counterparties and Limits

Credit Rating	Banks Unsecured		Banks Secured		Government / Sovereign		Corporates		Registered Providers	
	Value	Time	Value	Time	Value	Time	Value	Time	Value	Time
UK Govt	N/A	N/A	N/A	N/A	Unlimited	10 years	N/A	N/A	N/A	N/A
UK Local Authorities[1]	N/A	N/A	N/A	N/A	£10m	10 years	N/A	N/A	N/A	N/A
AAA	£10m	5 years	£15m	10 years	£10m	10 years	£10m	10 years	£10m	10 years
AA+	£10m	5 years	£15m	5 years	£10m	10 years	£10m	10 years	£10m	10 years
AA	£10m	4 years	£15m	5 years	£10m	10 years	£10m	5 years	£10m	10 years
AA-	£10m	3 years	£15m	4 years	£10m	5 years	£10m	4 years	£10m	10 years
A+	£10m	2 years	£15m	3 years	£5m	5 years	£10m	3 years	£10m	5 years
A	£10m	13 months	£15m	2 years	£5m	5 years	£10m	2 years	£10m	5 years
A-	£10m	6 months	£15m	13 months	£5m	5 years	£10m	13 months	£10m	5 years
None	£1m	6 months	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

Pooled Funds and AAA rated Money Market Funds	£15m per fund[2]
Peer to Peer Lending	Total for LEP and HCC - £5m
Note 1: For UK Local Authorities without a credit rating, a maximum of £10m per local authority will apply. For UK Local Authorities with credit ratings, the relevant Government/Sovereign for that rating will apply.	
Note 2: AAA rated funds may have exposure to underlying investments with lower credit ratings than the overall fund rating; a fund's AAA rating is assessed based on a number of factors, including the use of asset diversification to mitigate the credit risk of individual underlying investments, and the risk tolerance and fund management policies in place.	

2.2.2. The limits in table B are a guide and can change in periods of market stress. The Council's advisers provide counterparty updates monthly, and in response to new information or changing market conditions. Where these differ from the above officers will adhere to the lower of the limits set out in the table, or according to the latest advice.

2.2.3. The Council will continue to invest in UK institutions, e.g. banks, central government and pooled funds, even if the UK was not rated AA+.

2.2.4. Overseas subsidiaries of foreign banking groups will normally be assessed according to the country of domicile of the parent organisation. For the avoidance of doubt, Santander UK plc (a subsidiary of Spain's Banco Santander) will be classed as a UK bank due to its substantial UK franchises and the arms-length nature of the parent-subsidiary relationship.

2.2.5. Sovereign credit rating criteria will not apply to investments in multilateral development banks (e.g. the European Investment Bank and the World Bank) or other supranational organisations.

2.2.6. When deteriorating financial market conditions affect the creditworthiness of all organisations but these are not generally reflected in credit ratings, then the Council will restrict its investments in those organisations to maintain the required level of security. These restrictions may mean that insufficient commercial organisations of "high credit quality" are available for investment and so any cash surplus will be deposited with the government's Debt Management Office or with other local authorities. This may result in a reduction in the level of investment income earned but will protect the principal sums invested.

2.2.7. Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

2.2.8. No investments will be made with an organisation if there are substantive doubts about its credit quality even though it may meet the Lending Policy criteria. This means the Lending Policy applied operationally may at times be more restrictive than is formally stated.

2.3. Credit Ratings

2.4. Investment decisions are made by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment issued, otherwise the counterparty credit rating is used. If an agency removes one of the set of ratings it issues for a bank or building society, the institution will be removed from the list.

2.4.1. Table C provides a comparison of long term credits ratings issued by the major rating agencies.

Table C Comparison of Credit Ratings by Agency

<table>
<tr><th>Fitch</th><th>Moody’s</th><th>S&P</th><th>Definition</th></tr>
<tr><td>AAA</td><td>Aaa</td><td>AAA</td><td>Prime</td></tr>
<tr><td>AA+</td><td>Aa1</td><td>AA+</td><td rowspan="3">High Grade
High Quality</td></tr>
<tr><td>AA</td><td>Aa2</td><td>AA</td></tr>
<tr><td>AA-</td><td>Aa3</td><td>AA-</td></tr>
<tr><td>A+</td><td>A1</td><td>A+</td><td rowspan="3">Upper Medium Grade</td></tr>
<tr><td>A</td><td>A2</td><td>A</td></tr>
<tr><td>A-</td><td>A3</td><td>A-</td></tr>
<tr><td>BBB+</td><td>Baa1</td><td>BBB+</td><td rowspan="3">Adequate Grade</td></tr>
<tr><td>BBB</td><td>Baa2</td><td>BBB</td></tr>
<tr><td>BBB-</td><td>Baa3</td><td>BBB-</td></tr>
</table>

3. Changes in Credit Ratings

3.1. Credit rating updates, in responses to a change in the credit rating of a counterparty are provided by Arlingclose, along with any changes to advice and recommended actions.

3.2. Credit rating updates will be discussed at the weekly Treasury Management Update meeting.

3.3. On receipt of a credit rating update, or other substantive information about an counterparty, officers will consider the advice and actions in line with the following policy:

3.4. Negative Watch

3.4.1. This is a status that credit rating agencies apply while they are deciding whether to lower that organisation's credit rating.

3.4.2. If an institution is on negative rating watch the Council will treat it as one credit rating lower than it is currently rated.

3.4.3. If an institution is at the bottom of the Council’s credit rating criteria and is placed on negative watch, the Council will consider the advice of Arlingclose and if necessary stop investing and attempt to call back any money which is currently invested, depending on the economic viability of withdrawing the investment.

3.4.4. This policy does not apply to a **negative outlook** on a credit rating. In the case of a negative outlook any investment decision will be considered in line with all other information available but will not prompt immediate action to review existing investments.

3.5. Downgrading

3.5.1. If an institution is downgraded below the minimum credit rating criteria, then it will be removed from the list with immediate effect, along with any subsidiaries, and no new investments will be made.

3.5.2. If funds are on call with an institution when a downgrade happens, they will be withdrawn or the balance reduced as appropriate, at the earliest possible opportunity, which may be the following working day.

3.5.3. If there are outstanding fixed term deposits with an institution which has been removed from the list, terms for repayment will be sought and, if offered, fully considered and documented by Officers.

3.5.4. Downgrading and the action taken will be reported in the weekly treasury management meetings and quarterly reports to members.

3.5.5. If the Council's own bank were to be downgraded, officers would reduce balances according to the strategy. In the event of a significant downgrading of Barclays, where the bank's credit rating fell below investment grade, officers would reduce balances to minimum operational levels, but it would not be possible to eliminate all exposure to the bank.

3.6. Other matters to be considered by Officers

3.6.1. In applying the policy set out above, Officers will refer to the following sources of market information on a regular basis:

- Credit Default Swap Rates
- Equity Prices
- Economic data
- Financial statements
- Outlook reports from credit agencies
- Financial Times and other financial news sources
- Professional journals and other publications

3.6.2. A regular briefing will be provided for all Officers involved in the dealing function, the Head of Finance – Pensions and Treasury and/or the Assistant Director of Finance. This will provide all relevant information to enable decisions to be taken about treasury activity to ensure it remains within the policy. By its very nature the information will not be definitive and Officers will do all they can to react to these sources of information with the primary objective of security. The briefings will generally be delivered by weekly meetings. If for any reason, a meeting cannot be convened, all relevant information will be circulated to Officers and the Assistant Director of Finance.

3.6.3. Officers maintain an overview of prevailing market rates in their regular contact with brokers. When considering fixed term deposits, Officers will consider quotes from brokers for a range of periods before making decisions.

4. Definitions – Table B

4.1. Banks Unsecured

4.1.1. Accounts, deposits, certificates of deposit, and senior unsecured bonds with banks and building societies, other than multilateral development banks.

4.1.2. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail.

4.1.3. The Council may incur operational exposures to the banking sector through, for example, current accounts, collection accounts and merchant acquiring services. These are not classed as investments, but are still subject to the risk of a bank bail-in. Officers will seek to minimise operational exposure by keeping total operational balances as close to zero as possible. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

4.2. Banks Secured

4.2.1. Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies.

4.2.2. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the highest of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

4.3. Government

4.3.1. Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks.

4.3.2. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.

4.4. Corporates

4.4.1. Loans, bonds and commercial paper issued by companies other than banks and registered providers.

4.4.2. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made as part of a diversified pool in order to spread the risk widely.

4.5. Registered Providers

4.5.1. Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing and Registered Social Landlords, formerly known as Housing Associations.

4.5.2. These bodies are tightly regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department for Communities (Northern Ireland). As providers of public services, they retain a high likelihood of receiving government support if needed.

4.6. Pooled Funds

4.6.1. Shares or units in diversified investment vehicles consisting of any of the investment types above, as well as equity shares and property.

4.6.2. These funds provide wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity and aim for a constant net asset value will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

4.6.3. Bond, Equity and Property Funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

APPENDIX 3 FINANCIAL INSTRUMENTS GLOSSARY

Call Account
A bank account that pays a higher rate of interest than an ordinary account. These investments are subject to the risk of credit loss as a result of a bail-in should the regulator determine that the bank is failing or likely to fail.

Certificates of Deposit (CDs)
CDs are negotiable term deposits made with a bank or a building society. They are bearer instruments which can be issued at a discount and without a coupon (interest payment), however, more typically they pay either a fixed or a variable coupon; with variable rates of interest being fixed semi-annually against a reference rate such as LIBOR. The coupon is closely related to the current market deposit rate from the same counterparty for a corresponding maturity. Large issues will typically be issued at par and are actively traded on a secondary market meaning that they can be acquired and sold on a daily basis. CDs are a money market instrument and therefore the credit ratings will be the same as those for term deposits. CDs offer the same credit quality as term deposits, but due to their liquidity there is an active secondary market and therefore the rate of interest paid is typically slightly lower than the rate earned on a term deposits of the same duration.

Commercial papers
An unsecured, short-term debt instrument issued by a corporation, typically for the financing of accounts receivable, inventories and meeting short-term liabilities. Maturities on commercial paper rarely range any longer than 270 days. The debt is usually issued at a discount, reflecting prevailing market interest rates.

Corporate bonds
These are issued by companies that are looking to raise capital and are seen as riskier than gilts, as companies are likelier to default on debt than governments. You generally get a higher rate of interest for taking on this risk. A corporate bond is a loan made to a company for a fixed period by an investor, for which they receive a defined return. Investors usually receive annual payments for their cash (which are normally expressed as a percentage) as well receiving the principal sum back at the end of the term. Investment grade corporate bonds are usually issued by established companies which are deemed less likely to default on their obligations. Corporate bonds can be traded on a secondary market.

Covered Bonds, Reverse Repurchase Agreements and other Collateralised Agreements
These investments are secured on a bank or building societies' assets, which limits the potential losses in the event of insolvency which means that they are exempt from bail in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the highest of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

Fixed Term Deposits
A deposit held at a financial institution that has a fixed term. These are generally short-term with maturities ranging anywhere from a month to a few years. When a term deposit is purchased, the lender (the customer) understands that the money can only be withdrawn after the term has ended or by giving a predetermined number of days' notice.

These investments are subject to the risk of credit loss as a result of a fail-in should the regulator determine that the bank is failing or likely to fail.

Government Bonds (Gilts)
This type of fixed interest security is issued by the British government if it wants to raise money and is generally seen as very low risk. This is because it is highly unlikely that the British government would go bankrupt and therefore be unable to pay the interest due or repay the loan in full. Government bonds are traded on a secondary market and therefore seen to be very liquid.

Index linked gilts pay interest linked to the Retail Price Index (RPI) so their value rises with inflation.

Loans to Local Authorities or Companies
This type of investment is an arrangement under which an amount is lent for a fixed period of time to a counterparty for which a rate of interest is receivable either at intervals during the loan or on maturity.

Local Capital Finance Company (LCFC) Equity
LCFC was established in 2014 by the Local Government Association (LGA) Municipal Bond Agency. Its aim is to provide local authorities with an alternative form of borrowing to supplement current lenders such as the PWLB and banks. The LCFC plans to issue bonds on the capital markets and lend proceeds to local authorities. The LGA is seeking to raise equity of £10m from local authorities and in September 2014 the LGA had raised £4.5m from 38 councils. A mid-year change to the 2014/15 Treasury Management Strategy was agreed by Council on 25 November 2014 to enable investment in the LCFC.

Local Government Bonds
A loan raised by a local authority in the form of a fixed-interest bond, repayable at a specific date. Local Government Bonds are tradable but the market is less establish as with other bond markets.

Money Market Funds
A Money Market Fund is an open-ended mutual fund that invests in a diversified pool of securities short-term debt securities such as Treasury bills and commercial paper. Money Market Funds are widely regarded as being as safe as bank deposits yet providing a higher yield.

Notice accounts
Accounts on which the account holder is required to give a notice of withdrawal a specified number of days before making the withdrawal to avoid penalties. These investments are subject to the risk of credit loss as a result of a bail-in should the regulator determine that the bank is failing or likely to fail.

Peer to Peer Lending
Peer to peer lending (P2PL) is a method of lending money to unrelated individuals, or "peers", without going through a traditional financial intermediary such as a bank or other financial institution. Typically these investment vehicles offer higher rates of return commensurate with the underlying risk of unsecured investments. In addition, this form of investment may provide a means of stimulating economic development within a corporate rather than financial risk profile and may be particularly suitable for the Local Enterprise Partnership

Pooled Funds
Pooled funds include pooled bond, equity and property funds. They provide enhanced returns over the longer period, but are, potentially, more volatile in the shorter term. These funds would enable the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

Registered Providers of Social Housing
Formerly known as Housing Associations, Registered Providers for social housing are tightly regulated by the Homes and Communities Agency. They retain a high likelihood of receiving government support if needed. The Council will consider investing with unrated Registered Providers with adequate credit safeguards, subject to receiving independent advice.

Supranational Bonds
A supranational entity is formed by two or more central governments with the purpose of promoting economic development for the member countries. Supranational institutions finance their activities by issuing debt, such as supranational bonds. Examples of supranational institutions include the European Investment Bank and the World Bank.

Similarly to the government bonds, the bonds issued by these institutions are considered very safe and have a high credit rating.

Treasury Bills (T-Bills)
Treasury Bills are short term Government debt instruments. They are issued by the Debt Management Office and are an eligible sovereign instrument, meaning they have an AAA rating. T-Bills are issued on a zero-coupon, i.e. they are issued at a discount to their par nominal value whereupon maturity the par value redemption will be higher than the purchase price reflecting an income return alongside the return of the initial capital outlay. T-Bills are actively traded on a secondary market meaning that they can be acquired and sold on a daily basis.

APPENDIX 4 TREASURY MANAGEMENT INDICATORS SUMMARY

1. Background

1.1. The following tables set out the Prudential and Treasury Management Indicators that will be monitored and reported on during the 2019/20 Financial Year.

1.2. The Treasury Management Indicators are outlined in Section 5 IP PART Treasury Management Strategy and details are given in section 2 , below

1.3. The Prudential Indicators are set in the IP PART C Capital Strategy 2019, Appendix A

2. Treasury Management Indicators

2.1. Security

2.1.1. The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit score of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.[1]) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

TM1 - Credit risk indicator	Target
Portfolio average credit score	6.0

1 The Council's minimum lending criteria is BBB- which has a score of 10.

2.1.2. This is an existing indicator which is unchanged from 2018/19

2.2. Liquidity

2.2.1. The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling 1 month period, without additional borrowing.

TM2 - Liquidity risk indicator	Target
Total cash available within 1 months	£10m

2.2.2. This is a new indicator which has not previously been required.

2.3. Interest rate exposures

2.3.1. This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

TM3 - Interest rate risk indicator	Limit
Upper limit on one-year revenue impact of a 1% rise in interest rates	£45,000
Upper limit on one-year revenue impact of a 1% fall in interest rates	£90,000

2.3.2. The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates.

2.3.3. This is a new indicator, which replaces the old Net Limit on Fixed and variable interest rates indicators, which was mandatory under the old code. This is a local indicator for interest rate risk recommended for inclusion by Arlingclose.

2.4. Maturity structure of borrowing

2.4.1. This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

TM4 - Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	30%	0%
12 months and within 24 months	20%	0%
24 months and within 5 years	20%	0%
5 years and within 10 years	20%	0%
10 years and within 20 years	20%	0%
20 years and within 30 years	30%	0%
30 years and above	60%	0%

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

2.4.2. This indicator has changed from the 2018/19 version. Previously only Long-Term loans were reported – for 2019/20 it is required to capture all loans in this table

2.5. Principal sums invested for periods longer than a year

2.5.1. The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end will be:

TM5 - Price risk indicator	2019/20	2020/21	2021/22	2022/23
Limit on principal invested beyond year end	£50m	£50m	£50m	£50m

2.5.2. This is an existing indicator which is unchanged from 2018/19

2.6. MIFID II Compliance Indicators

2.6.1. The purpose of this indictor is to confirm that the Council has met the minimum requirements required to be considered a Professional Investor under the Markets in Financial Instruments Directive (ii) [MiFID II].

2.6.2. The Council holds elective professional status under MiFID II. Professional status is required in order to maintain access to the full range of approved instruments and counterparties set out in the Lending Policy.

2.6.3. The indicators to be monitored during 2019/20 are:

TM6 (a) Investment Balance at Reporting Date	
Minimum Balance Limit	£10m
TM6 (b) Number of Officers with at least 1 Year relevant experience	
Regulatory Minimum	1

3. Prudential Indicators

3.1. The CIPFA Prudential Code for Capital Finance requires the Council to set and monitor performance against as number of Prudential Indicators [PIs]. Changes to the code in 2018 mean that with effect from 2019/20 these indicators will be set within the Capital Strategy, whereas in previous years his was a part of the Council's Treasury Management Strategy.

3.2. As there are no required changes to reporting arrangements, the PIs will continue to be reported alongside the Treasury Management indicators. The PIs therefore are included in the summary of indicators shown in the next section

3.3. Full details of the PIs can be found in IP Part C – 2019/20 Capital Strategy, appendix A.

4. Summary of Indicators

4.1. The tables on the following page set out a summary of the Treasury Management and Prudential Indicators for the IP period, and which will be reported in 2019/20

4.2. Treasury Management Indicators

Treasury Management Indicators		All Years 2019/20 to 2022/23	
		Values are £000 unless stated	
TM1	Portfolio Average Credit Score	Value Weighted Average of 6.0	
TM2	Cash Available within 1 month (Minimum)	10,000	
TM3	Upper limit on one-year revenue impact of a 1% rise in interest rates	450,000	
	Upper limit on one-year revenue impact of a 1% fall in interest rates	900,000	
TM4	Maturity Structure of fixed rate borrowing	Upper Limit	Lower Limit
	Under 12 months	30%	0%
	12 months to 2 years	20%	0%
	2 years to 5 years	20%	0%
	5 years to 10 years	20%	0%
	10 years to 20 years	20%	0%
	20 years to 30 years	30%	0%
	30 years and above	60%	0%
TM5	Price Risk – Maximum principal invested >1 Year	50,000	
TM6	MIFID II Compliance Indicators **a)** Minimum Investment Balance	10,000	
	b) Officers with 1 year relevant experience	1	
Treasury Performance Indicators – Additional Indicators			
Weighted average maturity of the investment portfolio			
Return on lending compared to 7 day LIBID rate			
Average rate payable on the borrowing portfolio			
Any breaches of the Lending Policy			
Types of financial instruments used			

4.3. Prudential Indicators

	Prudential Indicators – Limits and Comparators	2019/20	2020/21	2021/22	2022/23
Ref	**Indicator**	**Values are £000 unless stated**			
PI1	Estimates of Capital Expenditure	242,783	248,919	210,445	155,361
PI2	Estimates of Capital Financing Requirement (CFR)	697,363	778,793	841,774	882,276
PI3	Gross Borrowing	371,412	463,124	543,638	597,951
	Gross Borrowing less than CFR	Y	Y	Y	Y
PI4	Liability Benchmark	316,794	396,477	464,241	522,027
PI5	Authorised Limit for external debt	545,000	620,000	720,000	810,000
	Loans Outstanding less than Authorised Limit	Y	Y	Y	Y
PI6	Operational Boundary for external debt	515,000	590,000	690,000	780,000
PI7	Loans Outstanding less than Operational Boundary	Y	Y	Y	Y
	Ratio of financing costs to net revenue stream (%)	3.75%	4.25%	4.75%	5..25%