South Gloucestershire Council

Audit and Accounts Committee

22nd January 2019

TREASURY MANAGEMENT, BORROWING AND INVESTMENT STRATEGIES FOR 2019/20 AND PRUDENTIAL INDICATORS 2018/19 TO 2021/22

Purpose of report
1. To recommend the following to Council for approval: – The Treasury Management, Borrowing and Investment Strategies (Appendix A); – The Treasury Management Indicators (Appendix A); 2. To delegate authority to the Chief Finance Officer in consultation with the Chair of Audit and Accounts Committee to make amendments to this report between now and its submission to Council for approval, and to communicate these to lead members of the Audit and Accounts Committee.

Background

3. The Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code) requires the Authority to receive and approve, as a minimum, three main Treasury Management reports each year, which incorporate a range of policies, estimates and actuals. These reports are required to be adequately scrutinised by committee before being recommended to the Council. This role is undertaken by the Audit and Accounts Committee.
4. The first of these reports is the Treasury Management Strategy which must be approved before the start of each financial year (this report).
5. The other two reports which are required are a mid-year report and an annual report after the year-end.

Changes to reporting requirements for Treasury Management and Capital Reports

6. In order to align with the revised CIPFA Codes (including the Prudential Code) and revised Ministry of Housing, Communities and Local Government (MHCLG) Guidance on Local Government Investments and Minimum Revenue Provision, the content of this Treasury Management, Borrowing and Investment Strategy (TMB&IS) report to Audit and Accounts Committee has changed compared to the Treasury Management, Borrowing and Investment Strategy report for 2018/19.

7. This report now focusses on Treasury Investments (the investment of cash balances arising from income received in advance of expenditure plus balances and reserves held), the Borrowing Strategy and Treasury Management Indicators. Capital related estimates and indicators, the Minimum Revenue Provision Policy and policy for commercial investments are now reported through the Capital Strategy and Commercial and Service Investment Strategy. The changes are summarised in the table below:

Content of Treasury Management and Investment Strategy Report 2018/19	Destination Report in 2019/20
Investment Strategy - Treasury investments	TMB&IS report *(this report)*
Investment Strategy – non Treasury investments	Commercial and Service Investment Strategy *(see below)*
Borrowing strategy - general	TMB&IS report
Borrowing policy on borrowing in advance of need	Commercial and Service Investment Strategy
Minimum Revenue Provision Policy	Capital Strategy *(see below)*
Forecast interest costs and income	TMB&IS report
Interest rate forecasts	TMB&IS report
Benchmarks	TMB&IS report
Prudential Indicators (capital and borrowing): - Capital expenditure and financing - Capital financing requirement (CFR) - Affordability - Gross debt compared to CFR - Operational boundary and authorised borrowing limit	Capital Strategy
Treasury management indicators: - Interest rate exposures - Maturity structure of borrowing - Principal sums invested for period more than one year	TMB&IS report
Training Advisers	Commercial and Service Investment Strategy

8. The Commercial and Service Investment Strategy deals with the Council's policy and risk management procedures for commercial and service–related investments. It is an appendix to the Capital Strategy being reported to Cabinet and ultimately requiring Council approval. This strategy will be received as part of the 2019/20 Final Capital Programme Report in February 2019.

9. The Capital Strategy is a new strategy report introduced by the 2017 edition of CIPFA's Prudential Code. It is an overview of, and links, capital expenditure and financing, the minimum revenue provision, Treasury Management, other investments and prudential indicators. It sets out the long term context and gives due consideration to both risk and reward. It requires Council approval since it incorporates the Authorised Borrowing Limit and Minimum Revenue Provision Policy.

Other changes to the Treasury Management Investment Strategy

10. The Treasury Management Investment Strategy in Appendix A includes a new type of investment: Real Estate Investment Trusts. Further information and criteria are given in Appendix A

Amendments to this report prior to Council approval

11. Due to the Committee's timetable, this report has to be prepared before capital programme plans are finalised for 2019/20. It is proposed that the Chief Finance Officer be given delegated authority in consultation with the Chair of the Audit and Accounts Committee to make any amendments to this report as necessary between now and the submission of this report to Council for approval, and to communicate these to lead members of the Audit and Accounts Committee. Amendments may be due to updated capital programme proposals and capital financing estimates, cash flow information, interest rate estimates or other estimates used to calculate Prudential Indicators, or may be required by the newly published CIPFA Codes of Practice.

Consultation

12. In reviewing these strategies, the Chief Finance Officer has had regard to specialist advice including from the treasury management advisers Arlingclose Ltd.

Risks, mitigations and opportunities

13. Treasury management is the management of the Authority's cash flows, borrowing and investments, and the associated risks. The Authority has borrowed and invested substantial sums of money 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 Authority's prudent financial management, and Treasury risk management at the Authority is conducted within 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).

14. The Council's strategies seek to achieve a reasonable balance between risk and reward. On borrowing, this is achieved by working with specialist advisors and setting long term objectives. On investing this is achieved by working with specialist advisors, spreading risk, being aware of general market sentiment about individual institutions, and in the case of doubt, not lending to them.

15. With both borrowing and lending, there are opportunities to reduce long term costs to the Council by choosing the most appropriate strategy, and the Chief Finance Officer works with the treasury management advisers to do so.

Financial implications (Nina Philippidis 01454 865140)

16. The whole of this report is concerned with financial implications.

17. The budget for investment income in 2019/20 is £2m based on an average investment portfolio of approximately £100m at an interest rate of 1.97%. The budget for debt interest paid in 2019/20 is £5m based on an average debt portfolio of £122m at an average interest rate of 4.10%. In addition the budget includes £0.8m for interest payable to Bristol City Council in respect of ex Avon County Council debt managed by them. If actual levels of investments and borrowing, or actual interest rates, differ from those forecast, performance against budget will be correspondingly different.
18. The fields of borrowing and lending are closely governed by regulation. The CIPFA Code requires the Council to consider strategies for both each year. This report fulfils the Authority's

legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

Human resource implications (Nicola Plant, HR Business Partner, 01454 863093)

19. There are no Human Resources implications that arise directly from this report.

Legal implications (John McCormack 01454 865980)

20. Local authorities are required by the provisions of the Local Government Act 2003 and the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 to have regard to CIPFA's Treasury Management Code of Practice (the CIPFA Code).

Sustainability Implications (includes environmental, social and economic impacts)

21. None arising directly from this report.

Equality Impact Assessment

22. None arising directly from this report.

RECOMMENDATIONS

The Committee is recommended:

1. To refer the following to Council for approval:
   - The Treasury Management, Borrowing and Investment Strategies (Appendix A);
   - The Treasury Management Indicators (Appendix A),;

2. To delegate authority to the Chief Finance Officer in consultation with the Chair of Audit and Accounts Committee to make amendments to this report between now and its submission to Council for approval, and to communicate these to lead members of the Audit and Accounts

Responsible Director

Dave Perry, Director of Corporate Resources Tel: 01454 865001

Departmental contacts

Nina Philippidis, Deputy Head of Finance, Revenues and Welfare Tel: 01454 865140

Caroline Vafeas, Accountant (Technical – Treasury Management) Tel: 01454 864727

Appendices

A Treasury Management and Investment Strategy 2019/20

B Arlingclose Economic & Interest Rate Forecast December 2018

C Existing Investment & Debt Portfolio Position

D Glossary

E CDS prices 2007 to 2018 (graph)

Appendix A

Treasury Management, Borrowing and Investment Strategy 2019/20

External Context

Economic background:

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 Authority's treasury management strategy for 2019/20.

2. UK Consumer Price Inflation (CPI) for October was up 2.4% year/year, slightly below the consensus forecast and broadly in line with the Bank of England's November Inflation Report. The most recent labour market data for October 2018 showed the unemployment rate edged 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 and provide some pull on general inflation. Adjusted for inflation, real wages grew by 1.0%, a level still likely to have little effect on consumer spending.

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 horizon, providing the UK's exit from the EU is relatively smooth.

4. Following the Bank of England's decision to increase Bank Rate to 0.75% in August, no changes to monetary policy has 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 (MPC) continues to reiterate that any further increases will be at a gradual pace and limited in extent.

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.

Credit outlook:

6. The big four UK banking groups have now divided their retail and investment banking divisions into separate legal entities under ringfencing legislation. Bank of Scotland, Barclays Bank UK, HSBC UK Bank, Lloyds Bank, National Westminster Bank, Royal Bank of Scotland and Ulster Bank are the ringfenced 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 ringfenced banks generally being better rated than their non-ringfenced counterparts.

7. 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 Bank of England did not require any bank to raise additional capital.

8. 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.

Interest rate forecast:

9. Following the increase in Bank Rate to 0.75% in August 2018, the Authority's treasury management adviser Arlingclose is forecasting two more 0.25% hikes 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 horizon. 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.

10. The UK economic environment remains relatively soft, despite seemingly strong labour market data. Arlingclose's view is that the economy still faces a challenging outlook as it exits the European Union and Eurozone growth softens. While 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 mid-December).* As such, the risks to the interest rate forecast are considered firmly to the downside.

11. 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. (The main lender to local authorities is the Public Works Loans Board, which sets its rates based on gilt yields).

12. A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix B.

13. For the purpose of setting the budget for 2019/20, it has been assumed that new investments will be made at an average rate of 1.3%. There is no allowance in the 2019/20 budget for new long-term loans but the Medium Term Financial Plan assumes that in the longer term new loans will be borrowed at an average rate of 3%.

Local Context

14. On 18th December 2018, the Authority held £147m of borrowing and £127m of investments. This is set out in further detail at Appendix C. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

15. Table 1: Balance sheet summary and forecast

	31.3.18 Actual £m	**31.3.19 Estimate £m**	**31.3.20 Forecast £m**	**31.3.21 Forecast £m**	**31.3.22 Forecast £m**
General Fund CFR	203	215	284	302	314
Less: Other debt liabilities *	-25	-23	-21	-20	-18
Loans CFR	**178**	**192**	**263**	**282**	**296**
Less: External borrowing **	-123	-122	-122	-121	-111
Internal borrowing	**55**	**70**	**141**	**161**	**185**

Less: Usable reserves	-113	-70	-63	-65	-72
Less: Working capital surplus	-60	-86	-97	-86	-96
Investments/ -ve = new borrowing	**118**	**86**	**19**	**-10**	**-17**

* finance leases, PFI liabilities and transferred debt that form part of the Authority's total debt
** shows only loans to which the Authority is committed and excludes optional refinancing

16. 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. The Authority's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

17. The above forecasts show that the Authority has an increasing CFR due to the capital programme, but over time, insufficient underlying resources to continue to fund internal borrowing and therefore may be required to borrow externally up to £50m over the forecast period. (This includes an allowance for maintaining investments of £30m. See paragraph 20).

18. The Medium Term Financial Plan being proposed to Council in February includes an allowance for an additional £10m borrowing in 20/21, and assumes that £10m borrowing maturing in 21/22 will be refinanced. These assumptions are not reflected in the external borrowing figures above.

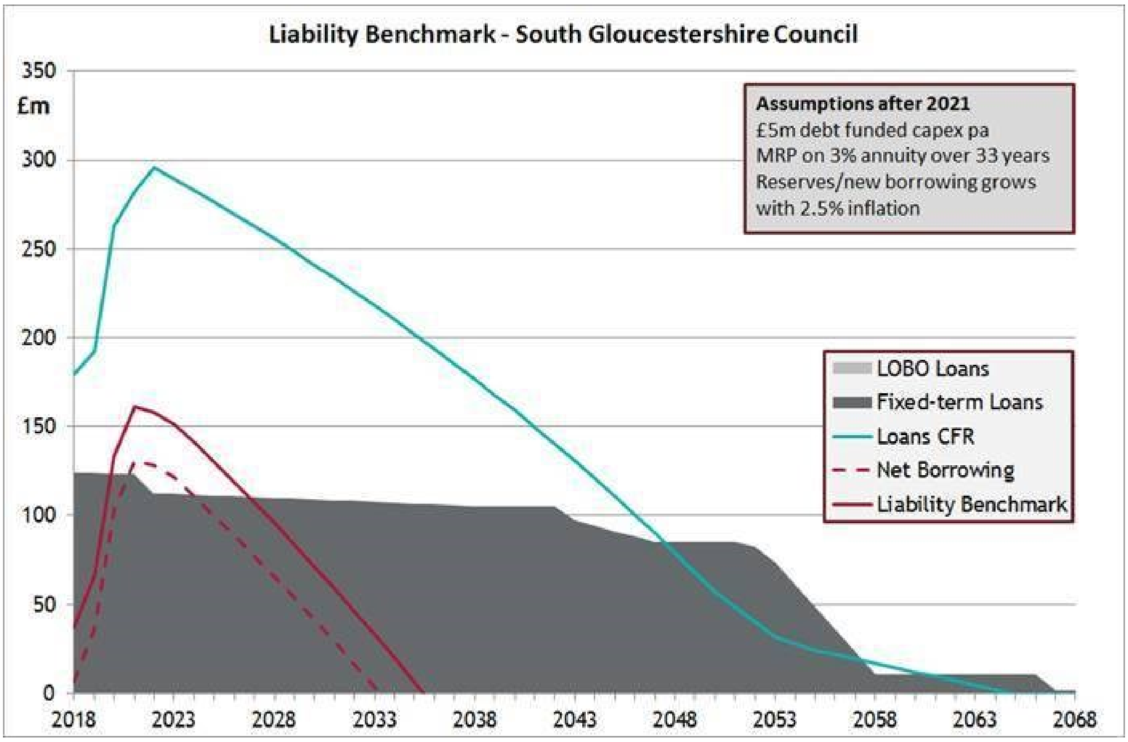
19. CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Authority expects to comply with this recommendation during 2019/20.

20. **Liability benchmark:** 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 the same forecasts as table 1 above, but that cash and investment balances are kept to a minimum level of £30m. This represents the value of the Authority's investment in a portfolio of strategic pooled funds which is a long-term investment, and which the Authority would not wish to be forced to redeem to liquidate funds.

21. Table 2: Liability benchmark

	31.3.18 Actual £m	**31.3.19 Estimate £m**	**31.3.20 Forecast £m**	**31.3.21 Forecast £m**	**31.3.22 Forecast £m**
Loans CFR	178	192	263	282	296
Less: Usable reserves	-113	-70	-63	-65	-72
Less: Working capital	-60	-86	-97	-86	-96
Plus: Minimum investments	30	30	30	30	30
Liability Benchmark	**35**	**66**	**133**	**161**	**158**

22. Liability Benchmark Chart



23. The chart indicates that based on current forecasts the Authority will need to borrow in the years from approximately 2020 to 2027, to fund the difference between the liability benchmark and the current level of external borrowing. The Medium Term Financial Plan for 2019/20 to 2022/23 allows for £10m additional borrowing in 2020/21, and for the refinancing of £10m PWLB borrowing which matures in 21/22. This budgeted borrowing is not reflected in Table 1 or the chart above.

Borrowing Strategy

24. The Authority currently holds £122m of loans, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that the Authority does not expect to need to borrow in 2019/20. The Authority may however borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £198m.

25. **Objectives:** The Authority's chief 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. The flexibility to renegotiate loans should the Authority's long-term plans change is a secondary objective.

26. **Strategy:** Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

27. By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal and/or short term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2019/20 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

28. Alternatively, the Authority may arrange forward starting loans during 2019/20, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

29. In addition, the Authority may borrow short-term loans to cover unplanned cash flow shortages.

30. **Sources of borrowing:** The approved sources of long-term and short-term borrowing are:
    a. Public Works Loan Board (PWLB) and any successor body
    b. any institution approved for investments (see below)
    c. any other bank or building society authorised to operate in the UK
    d. any other UK public sector body
    e. UK public and private sector pension funds (except Avon Pension Fund)
    f. capital market bond investors
    g. UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues
    h. Salix Energy Efficiency Loans Scheme

31. **Other sources of debt finance:** In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:
    a. leasing
    b. hire purchase
    c. Private Finance Initiative
    d. sale and leaseback

32. The Authority has previously raised the majority of its long-term borrowing from the PWLB although continues to investigate other sources of finance, such as local authority loans and bank loans that may be available at more favourable rates.

33. **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a joint and several guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to full Council.

34. **Short-term and variable rate loans**: These loans leave the Authority exposed to the risk of short-term interest rate rises. Interest rate risk is considered in the treasury management indicators below.

35. **Debt rescheduling:** The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Authority may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

Investment Strategy

36. The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Authority's investment balance has ranged between £115m and £162m, and similar levels are expected to be maintained in the forthcoming year, whilst being subject to the effects of any capital slippage, actual capital receipt dates compared to the budget assumptions and borrowing decisions, amongst other factors.

37. **Objectives:** The CIPFA Code requires the Authority 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

Authority'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 unsuitably low investment income. Where balances are expected to be invested for more than one year, the Authority will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

38. **Negative interest rates:** If the UK enters into a recession in 2019/20, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

39. **Strategy:** Given the increasing risk and very low returns from short-term unsecured bank investments, the Authority diversified into more secure and higher yielding asset classes during 2018/19. More short term lending was undertaken with other local authorities and £25m of cash that is available for longer-term investment was invested in higher yielding equity, bond and property pooled funds. Approximately two thirds of the Authority's surplus cash remains invested in short-term unsecured bank deposits and money market funds. The Authority is not seeking to further diversify into higher yielding asset classes to invest its Treasury cash in the coming year, but will continue to place deposits in the most secure counterparties.

40. **Business models:** Under the new IFRS 9 standard, the accounting for certain investments depends on the Authority's "business model" for managing them. The Authority aims to achieve value from its internally 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.

41. **Approved counterparties:** The Authority may invest its surplus funds with any of the counterparty types in table 3 below, subject to the cash limits (per counterparty) and the time limits shown.

Table 3: Approved investment counterparties and limits - This table must be read in conjunction with the notes below

<table>
<tr><th>Credit rating</th><th>Banks and building societies (secured and unsecured)</th><th>UK local authorities (excluding parish councils)</th><th>Government</th><th>Corporates</th></tr>
<tr><td>UK Govt</td><td>n/a</td><td>n/a</td><td>£ Unlimited
50 years</td><td>n/a</td></tr>
<tr><td>AAA</td><td>£15m
3 years</td><td rowspan="8">£15m
2 years
>2 years subject to further due diligence</td><td>£15m
50 years</td><td rowspan="8">Take advice on a case by case basis</td></tr>
<tr><td>AA+</td><td>£15m
3 years</td><td>£15m
25 years</td></tr>
<tr><td>AA</td><td>£15m
3 years</td><td>£0</td></tr>
<tr><td>AA-</td><td>£15m
3 years</td><td>£0</td></tr>
<tr><td>A+</td><td>£10m
1 year</td><td>£0</td></tr>
<tr><td>A</td><td>£10m
1 year</td><td>£0</td></tr>
<tr><td>A-</td><td>£10m
1 year</td><td>£0</td></tr>
<tr><td>None</td><td>£1m
100 days</td><td>£0</td></tr>
</table>

Pooled property funds and real estate investment trusts	£15m per fund or trust (but also subject to limits at Table 4 below)
Other pooled funds	£20m per fund (but also subject to limits at Table 4 below)

42. **Credit rating:** Investment limits are set by reference to the lowest published long-term credit rating from Fitch, Moody's and Standard and Poor's ratings agencies. Where available, the 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.

43. **Banks unsecured:** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. 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. See below for arrangements relating to operational bank accounts.

44. **Banks secured:** Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. 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 higher of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits.

45. **Government:** Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. 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.

46. **Corporates:** Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent.

47. **Pooled funds:** Shares or units in diversified investment vehicles consisting of any of the above investment types, plus equity shares and property. These funds have the advantage of providing 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 very low or no volatility 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.

48. Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Authority 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 Authority's investment objectives will be monitored regularly.

49. **Real estate investment trusts:** Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.

50. **Operational bank accounts:** The Authority may incur operational exposures, for example though current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but are still subject to the risk of a bank bail-in, and the Authority will aim to keep the

overnight net balance close to zero. 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 Authority maintaining operational continuity. The Authority currently banks with NatWest whose long term rating is “A-“.

51. **Risk assessment and credit ratings**: Credit ratings are obtained and monitored by the Authority’s treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be recalled or sold at no cost will be, and
- full consideration of costs and benefits and a risk assessment will be undertaken to the recall or sale of all other existing investments with the affected counterparty.

52. Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as “rating watch negative” or “credit watch negative”) so that it may fall below the approved rating criteria, then no new investments will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

53. **Other information on the security of investments**: The Authority understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis and advice from the Authority’s treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.

54. **Credit default swap (CDS) prices**: in recent years these have become more stable and much lower than during the financial crisis following 2008, and the spread between the lowest and highest priced banks has reduced. This is demonstrated in the graph at Appendix E. CDS prices of banks will be monitored for unusual fluctuations as well as against averages for similar institutions for movements that might give cause for concern.

55. When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority’s cash balances, then the surplus will be deposited with the UK Government via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

56. **Non UK Banks:** The Authority will only lend to non-UK banks which are domiciled in a country with a minimum long-term sovereign rating of AA+.

57. **Investment limits**: The Authority’s revenue reserves available to cover investment losses are forecast to be approximately £54 million on 31st March 2019. The maximum that will be lent to any one organisation (other than the UK Government) will be £15m. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers’ nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

58. <u>Table 4: Investment limits</u>

	Cash limit
Any single organisation, except the UK Central Government	£15m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£15m per group
Non UK banks	£75m in total
Unsecured investments with building societies	£15m in total
Money market funds	£90m in total

59. **Liquidity management**: The Authority produces both detailed short-term cash-flow forecasts and long-term forecasts to help determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium-term financial plan and cash flow forecast.

Treasury Management Indicators

60. The Authority measures and manages its exposures to treasury management risks using the following indicators.

61. **Security:** The Authority 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.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Credit risk indicator	Target
Portfolio average credit score	6.0

62. **Liquidity:** The Authority 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 one month period, without additional borrowing. The Council also maintains an overdraft facility with its bank.

Liquidity risk indicator	Target
Total cash available within 1 months	£17m

63. **Interest rate exposures**: In accordance with the Treasury Management Code of Practice local authorities should describe their strategy for managing interest rate risk. This is to consider and manage as far as possible the impact of changes in interest rates, taking into account their net borrowing position (borrowing less investments).

64. This Authority is in a position whereby all of its current borrowing is at long-term fixed rates, and therefore any changes in market interest rates will not impact on the cost of the current level of borrowing in the next twelve months. The majority of its investments however, other than those in strategic pooled funds, are invested for less than one year, and expected interest income over the next twelve months would be impacted by rises or falls in market rates in that period.

65. The impact of a 1% change in interest rates has been calculated based on the portfolio of borrowing and investments in December 2018. It is calculated on the assumption that maturing loans and investments will be replaced at current rates plus or minus 1%. The probability of a sudden change in interest rates of 1% is small, and therefore the impact below represents a worst case scenario in the case of a fall in rates.

Interest rate risk indicator	
One-year revenue impact of a 1% increase in interest rates (additional investment income)	£857,000
One-year revenue impact of a 1% fall in interest rates (loss of investment income)	£857,000

66. There is no allowance for new borrowing in 2019/20, but any borrowing decisions will take into account the potential impact of changes in interest rates as part of the overall consideration of the net revenue impact of the schemes being funded by borrowing. Any new short term (less than 12 months) or variable rate borrowing would have the effect of reducing the impact shown above.

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

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	0%	30%
12 months and within 24 months	0%	30%
24 months and within 5 years	0%	30%
5 years and within 10 years	0%	50%
10 years and within 20 years	0%	75%
20 years and within 30 years	0%	75%
30 years and within 40 years	0%	100%
40 years and within 50 years	0%	100%
50 years and within 60 years	0%	100%

68. 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.

69. **Principal sums invested for periods longer than a year:** The purpose of this indicator is to control the Authority'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:

Price risk indicator	2019/20	2020/21	2021/22
Limit on principal invested beyond year end	£40m	£30m	£20m

70. The Authority uses the following benchmarks to measure its performance in relation to investment returns, while recognising the overriding need for effective risk management and that priority should be given to security and liquidity.

    a. **Internally managed investments – 3 month LIBOR**

    This will cover loans to banks and building societies and investments in liquidity pooled funds.

    b. **Dividends from strategic pooled funds – 12 month LIBOR**

The Authority will also take part in its Treasury Management advisor's investment benchmarking exercises to monitor performance against other local authorities.

Related Matters

71. The CIPFA Code requires the Authority to include the following in its treasury management strategy.

72. **Financial Derivatives:** Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the *Localism Act 2011* removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

73. The Authority will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Authority is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

74. Financial derivative transactions may be arranged with any organisation that meets the 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.

75. **Markets in Financial Instruments Directive**: The Authority has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, where required to allow it access to the same range of services as previously but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

Other Options Considered

76. The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain

Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

Appendix B

Arlingclose Economic & Interest Rate Forecast December 2018

Underlying assumptions:

- Our central interest rate forecasts are predicated on there being a transitionary period following the UK's official exit from the EU.

- The MPC has a bias towards tighter monetary policy but is reluctant to push interest rate expectations too strongly. We believe that MPC members consider that: 1) tight labour markets will prompt inflationary pressure in the future, 2) ultra-low interest rates result in other economic problems, and 3) higher Bank Rate will be a more effective policy weapon if downside risks to growth crystallise.

- Both our projected outlook and the increase in the magnitude of political and economic risks facing the UK economy means we maintain the significant downside risks to our forecasts, despite the potential for slightly stronger growth next year as business investment rebounds should the EU Withdrawal Agreement be approved. The potential for severe economic outcomes has increased following the poor reception of the Withdrawal Agreement by MPs. We expect the Bank of England to hold at or reduce interest rates from current levels if Brexit risks materialise.

- The UK economic environment is relatively soft, despite seemingly strong labour market data. GDP growth recovered somewhat in the middle quarters of 2018, but more recent data suggests the economy slowed markedly in Q4. Our view is that the UK economy still faces a challenging outlook as the country exits the European Union and Eurozone economic growth softens.

- Cost pressures are easing but inflation is forecast to remain above the Bank's 2% target through most of the forecast period. Lower oil prices have reduced inflationary pressure, but the tight labour market and decline in the value of sterling means inflation may remain above target for longer than expected.

- Global economic growth is slowing. Despite slower growth, the European Central Bank is conditioning markets for the end of QE, the timing of the first rate hike (2019) and their path thereafter. More recent US data has placed pressure on the Federal Reserve to reduce the pace of monetary tightening – previous hikes and heightened expectations will, however, slow economic growth.

- Central bank actions and geopolitical risks have and will continue to produce significant volatility in financial markets, including bond markets.

Forecast:

- The MPC has maintained expectations of a slow rise in interest rates over the forecast horizon, but recent events around Brexit have dampened interest rate expectations. Our central case is for Bank Rate to rise twice in 2019, after the UK exits the EU. The risks are weighted to the downside.

- Gilt yields have remained at low levels. We expect some upward movement from current levels based on our central case that the UK will enter a transitionary period following its EU exit in March 2019. However, our projected weak economic outlook and volatility arising from both economic and political events will continue to offer borrowing opportunities.

	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Average
Official Bank Rate														
Upside risk	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.17**
Arlingclose Central Case	**0.75**	**0.75**	**1.00**	**1.00**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.13**
Downside risk	0.00	-0.50	-0.75	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	**-0.85**
3-mth money market rate														
Upside risk	0.10	0.10	0.10	0.10	0.15	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	**0.17**
Arlingclose Central Case	**0.90**	**0.95**	**1.10**	**1.30**	**1.40**	**1.40**	**1.40**	**1.35**	**1.35**	**1.35**	**1.35**	**1.35**	**1.35**	**1.27**
Downside risk	-0.20	-0.45	-0.60	-0.80	-0.90	-0.90	-0.90	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	**-0.76**
1-yr money market rate														
Upside risk	0.20	0.30	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	**0.33**
Arlingclose Central Case	**1.15**	**1.25**	**1.35**	**1.50**	**1.70**	**1.60**	**1.50**	**1.40**	**1.35**	**1.35**	**1.35**	**1.35**	**1.35**	**1.40**
Downside risk	-0.35	-0.50	-0.60	-0.80	-0.90	-0.90	-0.90	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	**-0.77**
5-yr gilt yield														
Upside risk	0.25	0.30	0.30	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.37**
Arlingclose Central Case	**1.15**	**1.25**	**1.35**	**1.50**	**1.50**	**1.40**	**1.35**	**1.35**	**1.30**	**1.30**	**1.30**	**1.30**	**1.30**	**1.33**
Downside risk	-0.50	-0.60	-0.65	-0.80	-0.80	-0.70	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	**-0.66**
10-yr gilt yield														
Upside risk	0.25	0.30	0.30	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.37**
Arlingclose Central Case	**1.50**	**1.65**	**1.70**	**1.80**	**1.80**	**1.75**	**1.75**	**1.70**	**1.70**	**1.70**	**1.70**	**1.70**	**1.70**	**1.70**
Downside risk	-0.55	-0.70	-0.70	-0.80	-0.80	-0.75	-0.75	-0.70	-0.70	-0.70	-0.70	-0.70	-0.70	**-0.71**
20-yr gilt yield														
Upside risk	0.25	0.30	0.30	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.37**
Arlingclose Central Case	**2.00**	**2.10**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.18**
Downside risk	-0.60	-0.70	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	**-0.73**
50-yr gilt yield														
Upside risk	0.25	0.30	0.30	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.37**
Arlingclose Central Case	**1.90**	**1.95**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**1.99**
Downside risk	-0.60	-0.70	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	**-0.73**

PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%

PWLB Infrastructure Rate (Maturity Loans) = Gilt yield + 0.60%

Appendix C

Existing Investment & Debt Portfolio Position

	18/12/2018 **Actual Portfolio £m**	18/12/2018 **Average Rate %**
External borrowing:		
Public Works Loan Board	-106	4.10
Other loans	-16	3.96
Total external borrowing	**-122**	**4.08**
Other long-term liabilities:		
Private Finance Initiative	-9	
Transferred Debt	-16	
Total other long-term liabilities	**-25**	
Total gross external debt	**-147**	
Treasury investments:		
Banks & building societies (unsecured)	52	0.89
Government (incl. local authorities)	17	1.01
Money Market Funds	33	0.73
Other pooled funds (property, bonds, equity)-principal value	25	3.91
Total treasury investments	**127**	**1.45**
Net debt	**-20**	

APPENDIX D

GLOSSARY

Term	Description
Authorised limit	A limit set on total external debt in a year, including borrowing and other long term liabilities such as leases and PFI. It should include headroom over and above the *operational boundary* (see definition) sufficient for unusual cash movements. This is the statutory limit of authorised external debt set by the Council and determined under s.3 (1) of the Local Government Act 2003. It represents the level of external debt which could be afforded in the short term but not sustainable in the longer term. It should not be breached.
Base Rate	Minimum lending rate of a bank or financial institution in the UK.
Basis point (bps)	1/100th of 1%, i.e. 0.01% Therefore 10 basis points is 0.10%; 50 basis points is 0.50% for example.
Benchmark	A measure against which performance can be compared.
Capital Financing Requirement (CFR)	This is the Council's borrowing need. It is the capital expenditure which has not yet been financed by capital receipts, grants or revenue, and must be funded by borrowing.
CDS *Credit Default Swap*	A contract between two parties, being a form of protection or "insurance" against the default of an institution to which the buyer of the CDS has lent money. The buyer of the CDS makes quarterly payments to the seller of the CDS, in return for the seller paying out in the event of the institution defaulting. The cost of that protection (the CDS price or "spread") varies according to the creditworthiness of the institution to whom money has been lent. If the price of a CDS to insure against loans to a particular bank, for instance, increases it is an indication that the market perceives that there is an increased likelihood of it defaulting.
Certificate of deposit (CD)	Evidence of a deposit with a specified bank or building society repayable on a fixed date. They are negotiable instruments and have a secondary market; therefore the holder of a CD is able to sell it to a third party before the maturity of the CD.
CIPFA *Chartered Institute of Public Finance and Accountancy*	A UK professional accountancy body specialising in the public sector. It issues accounting guidance and codes of practice specific to the public sector. It is responsible for the education and training of professional accountants and for their

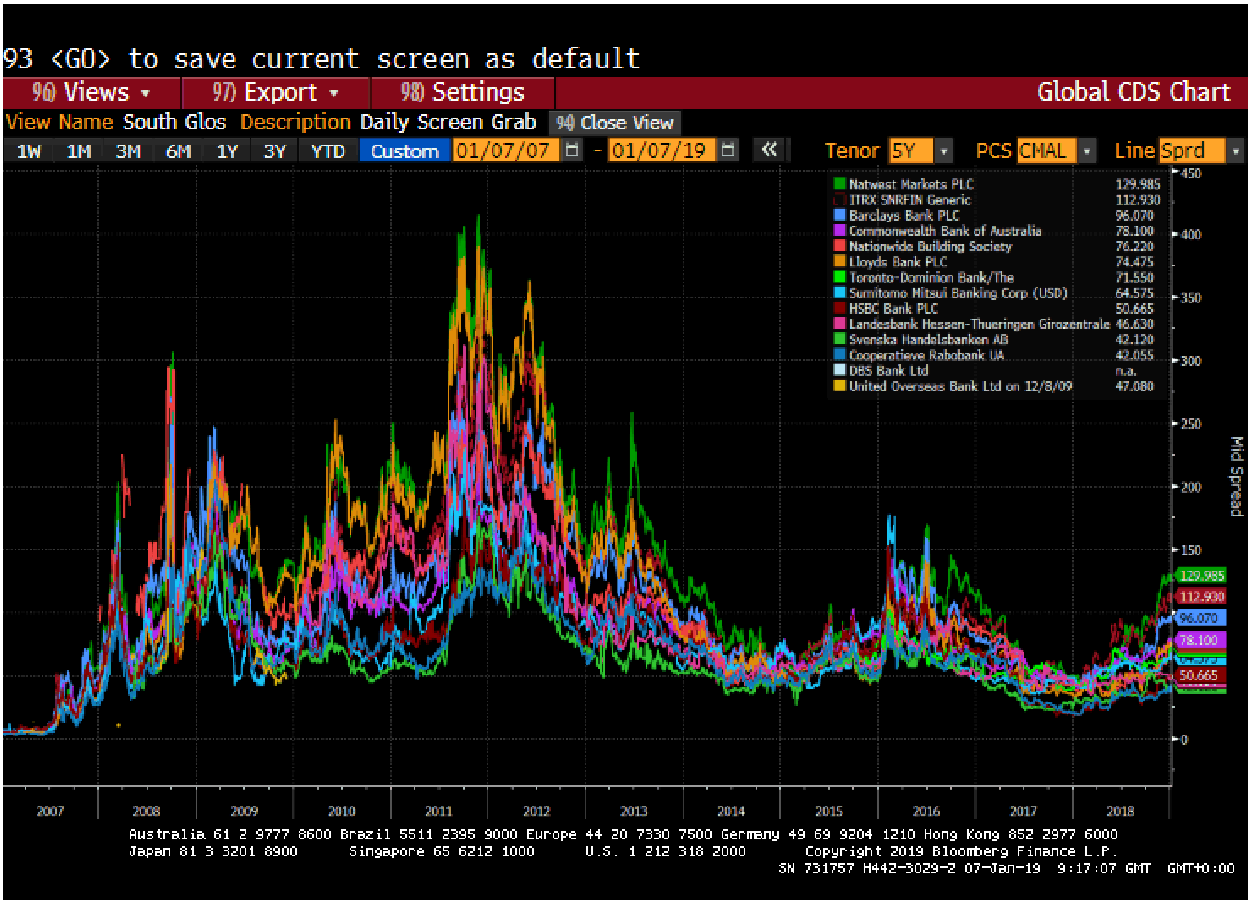
	regulation through the setting and monitoring of professional standards.
CNAV *Constant Net Asset Value*	In relation to money market funds, a constant net asset value fund seeks to maintain a constant value per share of £1 (or $1 or 1 euro for funds denominated in these currencies). Interest earned on the assets held in the fund is distributed to investors. *(Compare VNAV – variable net asset value)*
Coupon	Total annual interest paid on a gilt holding, usually in two equal, semi-annual instalments. Expressed as a percentage of a £100 nominal holding.
Corporate bond	Companies issue bonds when they wish to raise long term capital other than by the issue of shares. It is therefore a loan to a company for a fixed period of time, for a fixed interest amount (the "coupon") payable twice a year. The loan conditions are set out in a legal document.
Corporate bond fund	A collective investment scheme (similar to a money market fund - see below) but which invests in corporate bonds and possibly government bonds.
Enhanced cash funds, or enhanced money market funds	See also "Money Market Funds" below. These are pooled funds which are managed with the aim of providing an enhanced return in comparison to "liquidity" money market funds (MMFs). They do this by investing in a wider range of instruments, and for longer periods of time. For instance the weighted average maturity (WAM) of enhanced funds' investments could be as much as three years, whereas the maximum for liquidity MMFs is 60 days. The longer WAM means increased interest rate and credit risk compared to liquidity MMFs. However the fund managers seek to dilute this risk by wide diversification both in terms of counterparties, sectors, and investment types, and are required to do this in order to maintain AAA credit ratings. Usually two to three days' notice is required to redeem investments in these funds, compared to the instant access available for liquidity MMFs. Enhanced cash funds have a variable net asset value (VNAV), meaning that the value of a share is variable dependent upon the value of the assets held by the fund on a daily basis; whereas liquidity MMFs aim to maintain a constant net asset value (CNAV), meaning that the value of one share is maintained at £1 and any interest income is either paid out or used to buy more shares.
Fixed term deposit	A loan to a bank or building society for a fixed period of time at an agreed rate of interest. Premature redemption is not normally allowed, except perhaps on payment of a penalty.
Gilts (gilt edged stock)	Registered British Government securities representing money lent to the Government and giving the investor an absolute

	commitment from the Government to honour the debt that those securities represent.
iTraxx Senior Financials index	iTraxx indices comprise a "basket" of CDS prices. The Senior Financials index is based on the CDS prices of 25 European investment grade financial institutions (i.e. may include institutions other than banks).
LIBID *London Interbank Bid Rate*	The average interest rate at which banks are willing to **borrow** large deposits
LIBOR *London Interbank Offered Rate*	An interest rate at which banks can borrow from other banks, being the average interest rate at which banks are willing to **lend** to the world's most preferred borrowers. Fixed daily by the British Bankers' Association. The world's most widely used benchmark for short-term interest rates.
Liquidity	Availability of cash to meet liabilities as they fall due, or the ability to convert an asset easily into cash quickly and in large volume without substantially affecting the asset's price – for instance a Certificate of Deposit or gilts.
LOBO *Lender Option Borrower Option*	A form of borrowing, usually for a long term such as 40 to 60 years, whereby the lender has the option to re-set the interest rate at pre-determined dates (e.g. every 5 years), at which point the borrower has the option to accept the new rate, or repay the loan without incurring an early repayment penalty.
Money Market Fund (MMF)	Money market funds (MMFs) are mutual funds or pooled funds that invest in short-term money market instruments. These funds allow investors to participate in a more diverse and high-quality portfolio than if they were to invest individually. Like other mutual funds, each investor in a money market fund is considered a shareholder of the investment pool, or a part owner of the fund. All investors in a MMF have a claim on a pro-rata share of the fund's assets in line with the number of 'shares' or 'units' owned. MMFs are described as "liquidity" MMFs, and instant access to cash is possible; or "enhanced" MMFs where two or three days' notice is required to redeem a holding. See also "Enhanced Cash Funds" above.
MPC *Monetary Policy Committee*	A committee of the Bank of England which sets interest rates monthly.
MRP *Minimum Revenue Provision*	The prudent provision that local authorities must make each year for the repayment of borrowing used to finance capital expenditure (as required by Regulation under the Local Government and Public Involvement in Health Act 2007).
Net Revenue Stream	Taxation and non-specific grant income – estimates of amounts to be met from government grants (excluding capital grants) and local taxpayers.

Operational boundary	A boundary set on total external debt based on an estimate of the Council's maximum level of debt in a year. It takes into account its plans for capital expenditure and financing, and should be based on a prudent but not worst-case scenario (compare to *authorised limit)*. It is not significant if the operational boundary is breached temporarily.
Pooled fund	A type of collective investment fund, whereby the investor buys a share in a pool of investments, and receives a share of income and takes a share in the gains and losses in value of the portfolio. Different types of pooled funds exist, for instance a property fund – investing only in a property portfolio, or similarly equity fund, or bond funds. There are also multi-asset funds which aim to diversify investment into different types of asset class.
PWLB *Public Works Loans Board*	A statutory body which considers and makes loans to local authorities for capital purposes. Loans are made from the National Loans Fund. Interest rates are determined by HM Treasury and are linked to gilt yields.
Quantitative easing	If interest rates are very low and the Bank's Monetary Policy Committee expects inflation to fall below the Government's 2% target, it can inject money directly into the economy to boost spending. This is QE. The Bank of England creates new money electronically to buy financial assets like government bonds. This cash injection lowers the cost of borrowing and boosts asset prices to support spending and get inflation back to target.
Treasury bill	A zero-coupon sterling denominated instrument of up to 12 months maturity when first issued. Treasury bills are issued at a discount and redeemed at par.
VNAV *Variable net asset value*	In relation to enhanced cash funds for example, the value of a share is dependent upon the value of the assets held in the fund, which are revalued daily. As the value of the assets changes, so does the value of a share, hence the share (or unit) price is variable and can go up as well as down. The market value of the assets changes from day to day because the type and duration of assets held by an enhanced cash fund are more susceptible to the market's perceptions of interest rate risk and credit risk inherent in the asset, as compared to those held in money market funds. The return on a share in a variable net asset value fund, is the increase in the price of the share over the period. However in adverse conditions, the price could go down.
Yield	The return or interest rate earned on investments

Appendix E

CDS Prices from 2007 to 2018



Source: Bloomberg