For: Audit and Finance Committee Date: 21 January 2019

Treasury Management Strategy Statement 2019/20

Summary

This report presents the Treasury Management Strategy for 2019/20, including risk management, prudential indicators, and the borrowing requirement. Background information on the economic situation and the likely interest rate movements are included in the report, which informs the recommendations made.

Recommendation

Audit and Finance Committee is recommended to:

A. Scrutinise the 2019/20 Treasury Management Strategy; and

B. Note the Treasury Indicators for 2019/20 as set out in this report.

Reason

To comply with: the Local Government Act 2003 and supporting regulations, the Council's Financial Procedure Rules, CIPFA's *Treasury Management in the Public Services: Code of Practice 2017 Edition*, and *Prudential Code for Capital Finance in Local Authorities 2017 Edition* and the Ministry for Housing, Communities and Local Government's (MHCLG) *Statutory Guidance on Local Government Investments 3rd Edition (2018).*

Introduction

1. Treasury management is the management of the Council's cash flows, borrowing and investments, and the associated risks. The Council 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 risks are therefore central to the Council's prudent financial management.

2. Treasury risk management 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) which requires the Council to approve a treasury management strategy before the start of each financial year. This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

3. Investments held for service purposes or for commercial profit are considered in a different report, the Capital and Investment Strategy which is presented to Audit & Finance Committee for scrutiny in January prior to being presented to Cabinet and Full Council for approval in February.

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External Context

Economic Background

4. The Council's treasury management adviser, Arlingclose, has provided the following commentary.
5. 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.
6. 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.
7. 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 Bank of England (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.
8. Following the BoE'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.
9. 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

10. 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.

11. The BoE 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.

12. 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

13. Following the increase in Bank Rate to 0.75% in August 2018, the Council's treasury management adviser Arlingclose is forecasting two more 0.25% increases during 2019 to take official UK interest rates to 1.25%. The Bank of England's Monetary Policy Committee (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.

14. 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.

15. 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.

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

17. For the purpose of setting the budget, it has been assumed that new investments will be made at an average rate of 0.90%.

Local Context

18. On 31st December 2018, the Council held £53.4m of borrowing and £65.80m of investments. The balance held as investments is always higher than average on this date due to it being just before precepts are paid out in early January. Further detail of the investment and borrowing portfolio is set out in Appendix B.
19. Forecast changes in these sums are shown in the balance sheet analysis in the table below.

Balance Sheet Summary and Forecast	31/03/2018 Actual £m	31/03/2019 Forecast £m	31/03/2020 Estimate £m	31/03/2021 Estimate £m	31/03/2022 Estimate £m
General Fund CFR	10.5	12.2	15.5	15.4	15.2
HRA CFR	64.2	67.3	67.1	66.3	68.4
Total CFR	**74.7**	**79.5**	**82.6**	**81.7**	**83.6**
Less: External borrowing (PWLB)	-53.5	-51.2	-48.9	-46.6	-44.3
Internal borrowing	**21.2**	**28.3**	**33.7**	**35.1**	**39.3**
Less: Usable reserves	-41.5	-41.4	-41.3	-37.4	-36.7
Less: Working capital	-14.7	-14.5	-14.5	-14.5	-14.5
Investments	**35.0**	**27.6**	**22.1**	**16.8**	**11.9**

20. 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 Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing, i.e. the use of cash balances held for other purposes to delay the need to borrow from external sources.
21. The Council has an increasing CFR due to the Capital Programme. There are plans to use reserves and capital receipts for financing of some capital expenditure.
22. CIPFA's *Prudential Code for Capital Finance in Local Authorities* (2017 Edition) recommends that the Council's total external debt should be lower than its highest forecast CFR over the next three years. The table above shows that we expect to comply with this recommendation during 2019/20.

Borrowing Strategy

23. The Council currently holds £53.4 million of PWLB loans, a decrease of £0.1 million on the previous year, as part of its strategy for funding previous years' HRA capital programmes. The balance sheet forecast in the table above shows that no new external borrowing is expected in 2019/20. The Council may borrow however to externalise current internal borrowing to take advantage of rates and thus free up internal borrowing capacity to meet future years' spending at more

advantageous rates, providing this does not exceed the authorised limit for borrowing of £116 million.

24. The Council's primary 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 our long-term plans change is a secondary objective; especially given the punitive early repayment rates imposed by the PWLB.

25. Given the significant reductions in local government funding, the Council'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.

26. By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal 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 us with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council 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.

27. Alternatively, the Council 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.

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

Sources of Borrowing

29. The approved sources of long-term and short-term borrowing are as follows:
    (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; and
    (e) UK Municipal Bonds Agency Plc.

Other Sources of Debt Finance

30. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:
    (a) Operating and Finance Leases;
    (b) Hire Purchase; and
    (c) Sale and Leaseback

31. The Council has previously raised all of its long term borrowing from the PWLB but it continues to investigate other sources of finance, such as local authority loans, local government pension funds and bank loans that may be available at more favourable rates.

32. **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.

Debt Rescheduling

33. 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 Council 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.

34. Any rescheduling will be discussed with the Portfolio Holder for Finance and reported to the Cabinet, at the earliest meeting following its action.

Investment Strategy

35. The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's investment balances have ranged between £30m and £65 million and are expected to remain at similar levels in the forthcoming year.

36. 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.

37. 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 unsuitably low investment income. Where balances are expected to be invested for more than one year, the Council 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. Given the increasing risk and very low returns from short-term unsecured bank investments, the Council aims to maintain the current strategy of diversification into more secure and/or higher yielding asset classes during 2019/20. This is especially the case for the estimated £10 million that is available for longer-term investment. A proportion of the Council's surplus cash remains invested in money market funds. This diversification represents a continuation of the strategy adopted in 2018/19.

40. Under the new IFRS 9 *Financial Instruments* standard, the accounting for certain investments depends on the Council's "business model" for managing them. The Council 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.

Approved counterparties

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

Credit rating	Banks unsecured	Banks Secured	Government	Registered Providers	Wholly owned companies
UK Government	n/a	n/a	£ Unlimited	n/a	n/a
			50 years		
AAA and AA+	£3m	£5m	£7m	£3m	n/a
	5 years	10 years	25 years	5 years	
AA and AA-	£3m	£5m	£7m	£3m	
	3 years	4 years	10 years	3 years	
A+	£3m	£5m	£7m	£3m	
	2 years	3 years	5 years	2 years	
A	£3m	£5m	£7m	£3m	
	13 months	2 years	5 years	13 months	
A-	£3m	£5m	£7m	£3m	
	6 months	13 months	5 years	6 months	
None	n/a	n/a	£7m	n/a	£20m
			25 years		5 years
Pooled funds	£10m per fund				
Current Account of the Council's banker	£20m maximum but seek to keep overnight balances in a range of £1m to £15m in line with managing risk and maximising yield.				

42. The above table must be read in conjunction with the notes below.

43. **Credit rating:** Investment limits are set by reference to the lowest published long-term credit rating from a selection of external rating 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.

44. **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.

45. **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. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

46. **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 (i.e. DMADF – Debt Management Account Deposit Facility) may be made in unlimited amounts for up to 50 years.

47. **Registered Providers:** 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. 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 (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.

48. **Wholly-owned companies**: Loans and share capital in companies wholly owned by the Council.

49. **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.

50. 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.

51. **Operational bank accounts:** The Council 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. Therefore the balance in the Council's current account will be kept to the minimum required for operational purposes. Generally this will be around £1m to £3m, rising to an overnight maximum of £15m on monthly precept dates. 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.

52. **Risk assessment and credit ratings:** Credit ratings are obtained and monitored by the Council'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:

    (a) no new investments will be made;

    (b) any existing investments that can be recalled or sold at no cost will be; and

    (c) full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

53. 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 only investments that can be withdrawn on the next working day 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.

54. **Other information on the security of investments:** The Council 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 Council'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 investment criteria.

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 Council 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 Council'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.

Investment Limits

56. The Council's revenue reserves available to cover any investment losses are forecast to be £25 million on 31st March 2019. In order that no more than 20% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £5 million. 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.

Investment Limits	**Cash limit**
Any single organisation, except the UK Central Government	£5m each
UK Central Government	Unlimited
UK Local Government	£7m per local authority
Any group of organisations under the same ownership	£5m per group
Any group of pooled funds under the same management	£10m per fund manager
Negotiable instruments held in a broker's nominee account	£5m per broker
Foreign countries	£3m per country
Registered providers	£3m in total
Unsecured investments with building societies	£7m in total
Loans to unrated corporates – Wealden District Council Owned Companies only	£20m in total
Money market funds	£10m per fund

57. **Liquidity management:** The Council uses detailed cash flow forecasting analysis to 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 Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium term financial plan and cash flow forecast.

Treasury Management Indicators

58. The Council measures and manages its exposures to treasury management risks using the following indicators.

Security

59. The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating 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 rating	**A**

Liquidity

60. 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 three month period, without additional borrowing.

Liquidity Risk Indicator	Target
Total cash available within 3 months	**£10m**

Interest Rate Exposure

61. CIPFA defines interest rate risk as “the risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation’s finances, against which the organisation has failed to protect itself adequately.” In local authorities this risk is therefore commonly considered in the context of the impact of changes in interest rates on the revenue accounts.

62. In adopting a suitable indicator to measure this risk, the Council has taken advice from our treasury management advisers to use the same measure as required in the Statement of Accounts financial instruments disclosure; namely the impact over one year of a 1% change in interest rates. The disclosure in the accounts shows the actual result of this measure. For this Treasury Management Strategy, an upper limit is set in order to provide protection to the General Fund and the HRA from unexpected falls in interest rates causing a loss of investment income, and from unexpected rises in interest rates causing an increase in interest payable.

63. All of the Council’s borrowings are at fixed rates from the PWLB and therefore the risk of an increase in interest payable over a year caused by an increase in interest rates is effectively minimised.

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

Interest Rate Risk Indicator	Upper Limit
One year revenue impact of a 1% change in interest rates	**£0.6m**

Maturity Structure of Borrowing

65. 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 as shown in the following table.

Refinancing Rate Risk Indicator	Upper Limit	Lower Limit
Under 12 months	25%	0%
12 months to 2 years	50%	0%
2 years to 5 years	75%	0%
5 years to 10 years	100%	0%
10 years to 20 years	100%	0%
20 years to 30 years	100%	0%
30 years and above	100%	0%

66. 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.

Principal Sums Invested for Periods Longer Than One Year

67. 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 as set out in the following table.

Price Risk Indicator	2019/20	2020/21	2021/22
Limit on principal invested beyond year end	£8m	£6m	£6m

Related Matters

68. The Council is required by the CIPFA Code to include the following in its Treasury Management Strategy.

Financial Derivatives

69. 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).

70. The Council's policy is that it 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 Council 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.

71. 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.

Policy on Apportioning Interest to the HRA

72. All of the Council's existing long-term external borrowing relates to the HRA. In the future, new long-term loans borrowed will be assigned in their entirety to either the General Fund or the HRA as relevant. This means the Council will manage external borrowing as two pools effectively – HRA and General Fund. Interest payable and other costs / income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged / credited to the respective revenue account. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured and interest transferred between the General Fund and HRA annually at the Council's average interest rate on investments, adjusted for credit risk.

Markets in Financial Instruments Directive (MiFID)

73. The Council has opted up to 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 Chief Financial Officer believes this to be the most appropriate status. As one of the criteria for retaining this status is a minimum investment balance of £10 million, the Council's strategy includes keeping this amount invested for the longer term.

Corporate Management Team Advice

74. Audit and Finance Committee is recommended to:
    (a) Scrutinise the 2019/20 Treasury Management Strategy; and
    (b) Note the Treasury Indicators for 2019/20 as set out in this report.

Financial Implications

75. The strategy proposed in this report, together with the interest rates forecast, is in line with the assumptions made when the 2019/20 budget was prepared. The costs of treasury operations, debt management expenses and investment income are included in the 2019/20 budget.

Legal Implications

76. The Local Government Act 2003 and supporting regulations requires the Council to 'have regard to' the CIPFA *Prudential Code for Capital Finance in Local Authorities 2017 Edition* and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable. The Council also has to 'have regard' to the MHCLG's *Guidance on Local Government Investments 3rd Edition* effective for financial periods commencing on or after 1st April 2018, and to CIPFA's *Treasury Management in the Public Services: Code of Practice 2017 Edition* and *Guidance Notes for Local Authorities 2018 Edition*.

Human Resources Implications

77. None arising directly from this report.

Other Implications

78. The Treasury Strategy has been formulated to minimise risk. Risk management is embedded in treasury management operations through the adoption of the CIPFA Treasury Management Code. Credit ratings and other market intelligence are used and counterparty limits also assist to assess and mitigate risk.

Other Implications	Applies?	Other Implications	Applies?
Human Rights	No	Equalities and Diversity	No
Crime and Disorder	No	Consultation	No
Environmental	No	Access to Information	No
Sustainability	No	Exempt from publication	No
Risk Management	Yes		

Director:	Trevor Scott, Chief Executive	
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Appendices:	A	Arlingclose Interest Rate Forecast
	B	Investment and Borrowing Portfolio at 31/12/2018
Background Papers:	None	