Appendix S

Treasury Management Strategy Statement

Minimum Revenue Provision Policy Statement and
Annual Investment Strategy
2016/17

1 Introduction

Background

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

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

1.3 CIPFA defines treasury management as: "The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

Reporting requirements

1.4 The Council is required to receive and approve three main reports each year, which incorporate a variety of polices, estimates and actuals. These reports are all required to be reviewed by the Council's Scrutiny Panel.

1.5 **Prudential and Treasury Indicators and Treasury Strategy** (This report) – The first, and most important report is recommended to Full Council following consideration by the Scrutiny Panel. It covers:

- the capital plans (including prudential indicators);
- a Minimum Revenue Provision (MRP) Policy (how residual capital expenditure is charged to revenue over time);
- the Treasury Management Strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

1.6 **Mid-Year Treasury Management Report** – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether any policies require revision.

1.7 **Annual Treasury Report** – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

1.8 Members will also be kept informed of any other significant matters that may occur as part of the quarterly Capital Monitoring reports to Scrutiny Panel.

Training

1.9 The CIPFA Code requires the responsible officer to ensure that Members with responsibility for treasury management or scrutiny receive adequate training in treasury management. Training has previously been undertaken by members and further training will be arranged as required. The training needs of treasury management officers are periodically reviewed.

Treasury Management Strategy for 2016/17

1.10 The strategy for 2016/17 covers the following Capital and Treasury Management issues:

- the capital plans and the prudential and treasury indicators;
- the Minimum Revenue Provision (MRP) Policy;
- the current treasury position;
- the economic background and prospects for interest rates;
- the borrowing strategy;
- the investment policy and strategy, and credit worthiness policy;
- the policy on use of external service providers.

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

Treasury management consultants

1.12 The Council uses Capita Asset Services Treasury Solutions as its external treasury management advisors. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

1.13 It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

2 The Capital Prudential Indicators 2016/17 – 2018/19

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

Capital Expenditure

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

Capital Expenditure £'000	2014/15 Actual	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
General Fund	5,898	11,485	7,221	2,721	5,800
HRA	16,188	13,849	11,899	12,443	11,407
Total	**22,086**	**25,334**	**19,120**	**15,164**	**17,207**

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

Capital Expenditure £'000	2014/15 Actual	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Total Expenditure	**22,086**	**25,334**	**19,120**	**15,164**	**17,207**
Financed by:					
Capital receipts	4,260	4,896	6,859	4,626	6,000
Capital grants	2,636	4,766	101	0	0
Reserves	9,166	5,955	5,687	5,814	6,230
Revenue	5,871	5,452	4,457	3,011	2,000
Finance leases	270	853	0	0	0
Net financing need	**(117)**	**3,412**	**2,016**	**1,713**	**2,977**

The Capital Financing Requirement

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

2.5 The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with each asset's life.

2.6 The CFR includes any other long term liabilities (e.g. finance leases) brought onto the balance sheet. Whilst this increases the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes. The Council had £3.0m of such schemes within the CFR as at 31 March 2015. The Council is asked to approve the CFR projections below:

£'000	2014/15 Actual	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
CFR – general fund	26,048	25,606	24,342	23,098	21,798
CFR - housing	125,120	128,532	130,548	132,261	135,238
Total CFR	**151,168**	**154,138**	**154,890**	**155,359**	**157,036**
Movement in CFR	(1,063)	2,970	752	469	1,677
Movement in CFR represented by					
Net financing need	(117)	3,412	2,016	1,713	2,977
Assets acquired under finance leases	270	853	0	0	0
Less MRP	1,216	1,295	1,264	1,244	1,300
Movement in CFR	**(1,063)**	**2,970**	**752**	**469**	**1,677**

Minimum revenue provision (MRP) Policy Statement

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

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

2.9 For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will follow the existing practice outlined in former CLG regulations (option 1). This option provides for an approximate 4% reduction in the borrowing need (CFR) each year.

2.10 From 1 April 2008 for all unsupported borrowing (including finance leases) the MRP policy will be the Asset Life Method (option 3) – MRP will be based on the estimated life of the assets, in accordance with the regulations. This provides for a reduction in the borrowing need over approximately the asset’s life. Repayments included in finance leases are applied as MRP.

2.11 There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made.

2.12 The Accountancy team will keep the Council’s MRP Policy under review to ensure that it remains fit for purpose in relation to its borrowing requirements.

Affordability Prudential Indicators

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

2.14 **Ratio of financing costs to net revenue stream.** This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

%	2014/15 Actual	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
General Fund	7.88%	8.05%	7.79%	7.94%	9.10%
HRA	18.36%	18.34%	18.65%	19.04%	19.35%

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

2.16 **Incremental impact of capital investment decisions on council tax**. This indicator identifies the revenue costs associated with proposed changes to the three year capital programme recommended in this report compared to the Council's existing approved commitments and current plans. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which are not published over a three year period.

£	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Council Tax - Band D	0	0	0

2.17 **Incremental impact of capital investment decisions on housing rent levels**. Similar to the council tax calculation, this indicator identifies the trend in the cost of proposed changes in the housing capital programme recommended in this report compared to the Council's existing commitments and current plans, expressed as a discrete impact on weekly rent levels. This indicator shows the revenue impact on any newly proposed changes, although any discrete impact will be constrained by rent controls.

£	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Weekly housing rents	0	0	0

3 Treasury Management Strategy

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

3.2 The Council's treasury portfolio position at 31 March 2015, with forward projections are summarised below. The table shows the actual external debt against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

£'000	2014/15 Actual	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
External debt at 1 Apr	136,094	136,094	139,506	141,522	143,235
New borrowing	0	3,412	2,016	1,713	2,977
Other long-term liabilities	2,454	2,615	2,008	1,338	738
Gross debt at 31 Mar	**138,548**	**142,121**	**143,530**	**144,573**	**146,950**
CFR	151,168	154,138	154,890	155,359	157,036
Under / (over) borrowing	**12,620**	**12,017**	**11,360**	**10,786**	**10,086**
Investments at 31 Mar	35,986	32,574	30,558	28,845	25,868
Net Debt	**102,562**	**109,547**	**112,972**	**115,728**	**121,082**

3.3 Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2016/17 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

3.4 The Chief Finance Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this report.

Treasury Indicators: Limits to Borrowing Activity

3.5 The **Operational Boundary** is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

Operational boundary £'000	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Debt	139,506	141,522	143,235	146,212
Other long term liabilities	2,615	2,008	1,338	738
Total	**142,121**	**143,530**	**144,573**	**146,950**

3.6 The **Authorised Limit** for external debt represents a control on the maximum level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

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

Authorised limit £'000	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Debt	166,723	168,182	169,421	171,898
Other long term liabilities	2,615	2,008	1,338	738
Total	**169,338**	**170,190**	**170,759**	**172,636**

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

HRA Debt Limit £'000	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
HRA debt cap	140,275	140,275	140,275	140,275
HRA CFR	128,532	130,548	132,261	135,238
HRA headroom	11,743	9,727	8,014	5,037

HRA Debt Ratios £'000	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
HRA debt	128,532	130,548	132,261	135,238
HRA revenues	30,512	30,181	29,692	29,360
Ratio of debt to revenues	4	4	4	5
Number of HRA dwellings	6,054	6,014	5,979	5,954
Debt per dwelling (£'000)	21	22	22	23

4 *Economic Outlook*

4.1 The Council has appointed Capita Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. **Appendix A** draws together current City forecasts for short term (Bank Rate) and longer fixed interest rates. The following table gives the Capita Asset Services central view:

		PWLB Borrowing Rates			
	Bank Rate	5 year	10 year	25 year	50 year
Dec-15	0.50%	2.30%	2.90%	3.60%	3.50%
Mar-16	0.50%	2.40%	3.00%	3.70%	3.60%
Jun-16	0.75%	2.60%	3.10%	3.80%	3.70%
Sep-16	0.75%	2.70%	3.20%	3.90%	3.80%
Dec-16	1.00%	2.80%	3.30%	4.00%	3.90%
Mar-17	1.00%	2.80%	3.40%	4.10%	4.00%
Jun-17	1.25%	2.90%	3.50%	4.10%	4.00%
Sep-17	1.50%	3.00%	3.60%	4.20%	4.10%
Dec-17	1.50%	3.20%	3.70%	4.30%	4.20%
Mar-18	1.75%	3.30%	3.80%	4.30%	4.20%
Jun-18	1.75%	3.40%	3.90%	4.40%	4.30%
Sep-18	2.00%	3.50%	4.00%	4.40%	4.30%
Dec-18	2.00%	3.50%	4.10%	4.40%	4.30%
Mar-19	2.00%	3.60%	4.10%	4.50%	4.40%

4.2 The UK GDP growth rate in 2014 was the strongest UK rate since 2006, and the 2015 growth rate is likely to be a leading rate in the G7 again, probably second to the US. The November Bank of England Inflation Report included a forecast for growth to remain around 2.5% over the next three years, driven mainly by strong consumer demand as the squeeze on the disposable incomes of consumers has been reversed by a recovery in wage inflation at the same time that CPI inflation has fallen to, or near to, zero since February 2015. Investment expenditure is also expected to support growth. However, since the August Inflation report was issued, most worldwide economic statistics have been weak and the November Inflation Report flagged up particular concerns for the potential impact on the UK.

4.3 The Inflation Report was also notably subdued in respect of the forecasts for inflation; this was expected to barely get back up to the 2% target within the 2-3 year time horizon. There is considerable uncertainty around how quickly pay and CPI inflation will rise in the next few years and this makes it difficult to forecast when the MPC will decide to make a start on increasing Bank Rate.

4.4 Economic forecasting remains difficult with so many external influences weighing on the UK. Bank Rate forecasts will be liable to further amendment depending on how economic data evolves over time. Capita Asset Services undertook its last review of interest rate forecasts in November 2015 shortly after the publication of the quarterly Bank of England Inflation Report. There is much volatility in rates and bond yields as news ebbs and flows in negative or positive ways. This latest forecast includes a first increase in Bank Rate in quarter 2 of 2016.

4.5 The overall trend in the longer term will be for gilt yields and PWLB rates to rise when economic recovery is firmly established accompanied by rising inflation and consequent increases in Bank Rate, and the eventual unwinding of Quantitative Easing. Increasing investor confidence in eventual world economic recovery is also likely to compound this effect as recovery will encourage investors to switch from bonds to equities.

4.6 The overall balance of risks to economic recovery in the UK is currently evenly balanced. However, the balance of risks to the Bank Rate forecast is probably to the downside, and increases may be delayed further if recovery in GDP growth, and forecasts for inflation increases, are lower than currently expected.

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

- Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.
- UK economic growth turns significantly weaker than we currently anticipate.
- Weak growth or recession in the UK's main trading partners - the EU, US and China.
- A resurgence of the Eurozone sovereign debt crisis.
- Recapitalisation of European banks requiring more government financial support.
- Emerging country economies, currencies and corporates destabilised by falling commodity prices and / or the start of Fed. rate increases, causing a flight to safe havens

4.8 The potential for upside risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates include:

- Uncertainty around the risk of a UK exit from the EU.
- The commencement by the US Federal Reserve of increases in the Fed. funds rate causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities.
- UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

5 Borrowing Strategy

5.1 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is relatively high. This means that there would be a cost of carry to any new borrowing which causes an increase in investments, as this will incur a revenue loss between borrowing costs and investment returns.

5.2 Against this background and the risks within the economic forecast, caution will be adopted with the 2016/17 treasury operations. The Chief Financial Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- if it was felt that there was a significant risk of a sharp FALL in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowing will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are still lower than they will be in the next few years.

5.3 Any decisions will be reported to the Scrutiny Panel at the next available opportunity.

Treasury Management Limits on Activity

5.4 There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs / improve performance. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates;
- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

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

Interest rate Exposures £'000	2016/17	2017/18	2018/19
Upper limit on fixed interest rates based on net debt	118,000	122,800	129,500
Upper limit on variable interest rates based on net debt	59,000	61,400	64,700

Maturity Structure of fixed interest rate borrowing	Lower	Upper
Under 12 months	0%	15%
12 months to 2 years	0%	15%
2 years to 5 years	0%	15%
5 years to 10 years	0%	15%
10 years to 20 years	0%	30%
20 years to 30 years	0%	30%
30 years to 40 years	0%	40%
40 years to 50 years	0%	40%

Policy on Borrowing in Advance of Need

5.6 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds. Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

Debt Rescheduling

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

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

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

5.9 Any rescheduling will be reported to the Scrutiny Panel at the earliest meeting following its action.

Municipal Bond Agency

5.10 It is likely that the Municipal Bond Agency, currently in the process of being set up, will be offering loans to local authorities in the near future. It is also hoped that the borrowing rates will be lower than those offered by the Public Works Loan

Board (PWLB). The Council will consider making use of this new source of borrowing as and when appropriate.

HRA borrowing

5.11 As part of the HRA reform arrangements in April 2012, the Council decided to follow the 'two pool' approach to allocating existing debt, taking into account those loans that were originally raised for a specific purpose. This assumed that the HRA would be 'fully borrowed', however the HRA is now in a position where it may need to borrow to fund the Housing Investment Programme.

5.12 As the Council is maintaining an under-borrowed position, the HRA will be recharged for the cost of any new borrowing requirement based on the average balance of unfinanced HRA borrowing during the year, using the PWLB variable rate as at 31 March of the previous year. In an environment of low investment returns and relatively stable borrowing rates, this provides a recharge that is beneficial to both the HRA and General Fund, and can be reasonably forecast from early on in the financial year. This approach will be reviewed annually in conjunction with the TMSS and projected investment returns.

6 *Annual Investment Strategy*

Investment Policy

6.1 The Council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second and then return.

6.2 In accordance with the above guidance, and in order to minimise the risk to investments, the Council applies minimum acceptable credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

6.3 Ratings will not be the sole determinant of the quality of an institution, and it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as 'credit default swaps' and overlay that information on top of the credit ratings.

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

6.5 Investment instruments identified for use in the financial year are listed in **Appendix B**, which includes Counterparty, time and monetary limits. These will cover both 'Specified' and 'Non-Specified' Investments.

6.6 Specified Investments are sterling denominated investments of not more than one-year maturity, or those which could be for a longer period but where the Council has the right to be repaid within 12 months if it wishes. These are considered low risk assets where the possibility of loss of principal or investment income is small. Non-Specified Investments are those that do not meet the specified investment criteria. A limit of £20m will be applied to the use of Non-Specified investments (this will partially be driven by the long term investment limits).

Creditworthiness policy

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

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

6.8 This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands that indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the duration for investments. The Council will therefore use counterparties within the following durational bands:

- Yellow 5 years (UK Government debt or equivalent)
- Dark Pink 5 years Enhanced money market funds (1.25 credit score)
- Light Pink 5 years Enhanced money market funds (1.5 credit score)
- Purple 2 years
- Blue 1 year (nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 100 days
- No Colour not to be used

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

6.9 The creditworthiness service uses a wider array of information than just primary ratings and by using a risk weighted scoring system, does not give undue preponderance to just one agency's ratings.

6.10 Typically the minimum credit ratings criteria the Council will use is a Short Term rating (Fitch or equivalents) of F1, and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

6.11 All credit ratings will be monitored on a monthly basis. The Council is alerted to changes to ratings of all three agencies through its use of the creditworthiness service. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- a negative rating watch applying to a counterparty at the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Capita Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

6.12 Sole reliance will not be placed on the use of this external service. In addition the Council will also use market data and market information, and information on any external support for banks to help support its decision making process.

Country limits

6.13 The Council will only use approved counterparties from countries with a minimum sovereign credit rating of AA-, based on the lowest available rating. The list of countries that qualify using this credit criteria as at the date of this report are shown in **Appendix C**. This list will be amended by officers should ratings change in accordance with this policy.

Investment strategy

6.14 The Council will manage all of its investments in-house. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

6.15 The Bank Rate is forecast to remain unchanged at 0.5% before starting to rise from quarter 2 of 2016. The suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during each financial year for the next six years are as follows:

- 2016/17 0.90%
- 2017/18 1.50%
- 2018/19 2.00%
- 2019/20 2.25%
- 2020/21 2.50%
- Later years 3.00%

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

6.17 For its cash flow generated balances, the Council will seek to utilise its business reserve instant access and notice accounts, money market funds and short-dated deposits (overnight to 100 days) in order to benefit from the compounding of interest.

Investment treasury indicator and limit

6.18 The limit for the total principal funds invested for greater than 364 days is set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end. The Council is asked to approve the treasury indicator and limit.

£'000	2016/17	2017/18	2018/19
Max. principal sums invested > 364 days	5,000	5,000	5,000

End of year investment report

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

Interest rate forecasts 2016 - 2019 **APPENDIX A**

PWLB rates and forecast shown below take into account the 20 basis point certainty rate reduction effective as of 1 November 2012.

Capita Asset Services Interest Rate View														
	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Bank Rate View	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.50%	1.50%	1.75%	1.75%	2.00%	2.00%	2.00%
3 Month LIBID	0.60%	0.70%	0.80%	0.90%	1.10%	1.30%	1.40%	1.50%	1.80%	1.90%	1.90%	2.00%	2.00%	2.10%
6 Month LIBID	0.80%	0.90%	1.00%	1.10%	1.30%	1.50%	1.60%	1.70%	2.00%	2.10%	2.10%	2.20%	2.20%	2.30%
12 Month LIBID	1.10%	1.20%	1.30%	1.40%	1.60%	1.80%	1.90%	2.00%	2.30%	2.40%	2.40%	2.50%	2.50%	2.70%
5yr PWLB Rate	2.30%	2.40%	2.60%	2.70%	2.80%	2.80%	2.90%	3.00%	3.20%	3.30%	3.40%	3.50%	3.50%	3.60%
10yr PWLB Rate	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%	3.60%	3.70%	3.80%	3.90%	4.00%	4.10%	4.10%
25yr PWLB Rate	3.60%	3.70%	3.80%	3.90%	4.00%	4.10%	4.10%	4.20%	4.30%	4.30%	4.40%	4.40%	4.40%	4.50%
50yr PWLB Rate	3.50%	3.60%	3.70%	3.80%	3.90%	4.00%	4.00%	4.10%	4.20%	4.20%	4.30%	4.30%	4.30%	4.40%
Bank Rate														
Capita Asset Services	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.50%	1.50%	1.75%	1.75%	2.00%	2.00%	2.00%
Capital Economics	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.25%	1.50%	-	-	-	-	-
5yr PWLB Rate														
Capita Asset Services	2.30%	2.40%	2.60%	2.70%	2.80%	2.80%	2.90%	3.00%	3.20%	3.30%	3.40%	3.50%	3.50%	3.60%
Capital Economics	2.40%	2.60%	2.70%	2.80%	3.00%	3.10%	3.20%	3.30%	3.50%	-	-	-	-	-
10yr PWLB Rate														
Capita Asset Services	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%	3.60%	3.70%	3.80%	3.90%	4.00%	4.10%	4.10%
Capital Economics	3.35%	3.35%	3.45%	3.45%	3.55%	3.65%	3.75%	3.85%	3.95%	-	-	-	-	-
25yr PWLB Rate														
Capita Asset Services	3.60%	3.70%	3.80%	3.90%	4.00%	4.10%	4.10%	4.20%	4.30%	4.30%	4.40%	4.40%	4.40%	4.50%
Capital Economics	3.35%	3.35%	3.45%	3.45%	3.55%	3.65%	3.75%	3.85%	3.95%	-	-	-	-	-
50yr PWLB Rate														
Capita Asset Services	3.50%	3.60%	3.70%	3.80%	3.90%	4.00%	4.00%	4.10%	4.20%	4.20%	4.30%	4.30%	4.30%	4.40%
Capital Economics	3.40%	3.40%	3.50%	3.50%	3.60%	3.70%	3.80%	3.90%	4.00%	-	-	-	-	-

Specified Investments – All such investments will be sterling denominated, with **maturities up to a maximum of 1 year**, meeting the minimum 'high' quality criteria where applicable.

Non-Specified Investments – These are investments that do not meet the specified investment criteria. A limit of the lesser of £20m or 50% of the portfolio will be held in aggregate in non-specified investments.

A variety of investment instruments may be used that will fall into one of the above categories, subject to the credit quality of the institution. The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

Organisation	Min. Credit Criteria	Money Limit	Maturity Limit
Banks and Building Societies (including term deposits, CDs or corporate bonds)	Yellow	£7.5m	5 years
	Purple	£7.5m	2 years
	Orange	£7.5m	1 year
	Blue	£7.5m	1 year
	Red	£5.0m	6 months
	Green	£2.5m	100 days
	No colour	Not to be used	
UK Government Gilts	UK sovereign rating	£10m	1 year
UK Government Treasury Bills	UK sovereign rating	£10m	1 year
UK Local & Police Authorities	N/A	Unlimited	1 year
Debt Management Agency Deposit Facility	AAA	Unlimited	6 months
Money Market Funds	AAA	£10m	Liquid
Enhanced Money Market Funds	Dark Pink / Light Pink / AAA	£10m	Liquid
Bonds issued by Multilateral Development Banks	AAA	£3m	6 months

Notes:

- Country limit of £10m
- Limit in all Building Societies of £10m

The criteria in this appendix are intended to be the operational criteria in normal times. At times of heightened volatility, risk and concern in financial markets, this strategy may be amended by temporary operational criteria further limiting investments to counterparties of a higher creditworthiness and / or restricted time limits.

Sovereign credit ratings **APPENDIX C**

This list is based on those countries that have sovereign ratings of AA- or higher and also have banks operating in sterling markets, which have credit ratings of green or above in the Capita Asset Services credit worthiness service.

AAA	Australia Canada Denmark Germany Singapore Sweden Switzerland Netherlands
AA+	Finland U.K. U.S.A.
AA	Abu Dhabi (UAE) France Qatar
AA-	Belgium