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Leeds CITY COUNCIL

Report of Chief Officer Financial Services

Report to Executive Board

Agenda Item 7(iv)

Date: 7th February 2018

Subject: TREASURY MANAGEMENT STRATEGY 2018/19

Are specific electoral Wards affected? If relevant, name(s) of Ward(s):	☐ Yes	☑ No
Are there implications for equality and diversity and cohesion and integration?	☐ Yes	☑ No
Is the decision eligible for Call-In? Except recommendation 6.3 to 6.6	☑ Yes	☐ No
Does the report contain confidential or exempt information? If relevant, Access to Information Procedure Rule number: Appendix number:	☐ Yes	☑ No

Summary of main issues

1. This report sets out for Members' approval the Treasury Management Strategy for 2018/19, and also provides an update on the implementation of the 2017/18 strategy.

2. The Council's level of net external debt is anticipated to be £1,923m by 31/03/2018, £26m below expectations in November 2017 which is as a result of rephasing the capital programme.

3. The 2018/19 strategy continues to fund the borrowing requirement from low short term interest rates, balances and reserves whilst still allowing the Council to take advantage of longer term funding opportunities. The low rate funding environment is expected to continue with rises in base rate expected to be introduced cautiously. The cost of debt is forecast to increase by £4.2m in 2018/19.

4. The Authorised Limits for both External Debt and Other Long Term Liabilities have been reviewed and it is proposed to not change them. The Operational Boundaries have also been reviewed and likewise will not be changed. The Council's Authorised Limit is set below the Capital Financing Requirement reflecting that the Council is using its balance sheet strength to fund a proportion of is borrowing requirement.

5. The strategy of defraying longer term funding will increase the amount of debt that the Council is funding from short terms loans and its balance sheet to an estimated £662m at 31/03/2018. This exposure is expected to increase if the low interest rate

environment persists. The Council is mitigating this risk by acquiring longer term loans when market opportunities arise and looking at forward funding opportunities. Against this the Council has a stable long term loan portfolio of £1.565bn that has an average maturity of just over 38 years and is funded at less than 4.0%. An increase in the short term funding costs of 0.25% would add £1.1m to the interest costs in 2018/19.

6. The report also includes an updated Treasury Management Policy Statement for approval. The main change reflects an update to the Investment counterparty selection criteria and an update to the officer scheme of delegation.

7. CIPFA codes of practice on both Treasury and Capital have been issued and updated DCLG guidance on investments and MRP are awaited. Their changes will be embedded in the Council's Capital and treasury operations and reported in an updated Capital and Treasury Strategy report to Executive Board and full Council. In addition the Council has implemented the European Union Markets in Financial Instruments Directive (MiFIDII) with effect from 03/01/2018.

8. Recommendations

That the Executive Board:

8.1 Approve the treasury strategy for 2018/19 as set out in Section 3.3 and note the review of the 2017/18 strategy and operations set out in Sections 3.1 and 3.2

8.2 Note that revised CIPFA Codes and Practice and DCLG guidance will be adopted and reported to full Council when fully issued and that the Council has implemented the European Union Markets in Financial Instruments Directive (MiFIDII) legislation with effect from 03/01/2018.

That Executive Board recommend to full Council that:

8.3 The borrowing limits for 2017/18, 2018/19, 2019/20 and 2020/21 be set as detailed in Section 3.4 and note the changes to both the Operational Boundary and the Authorised limits.

8.4 The treasury management indicators for 2017/18, 2018/19, 2019/20 and 2020/21 be set as detailed in Section 3.5.

8.5 The investment limits for 2017/18, 2018/19, 2019/20 and 2020/21be set as detailed in Section 3.6.

8.6 The revised Treasury Management Policy Statement is adopted.

1 Purpose of this report

1.1 This report sets out for approval by Members the Treasury Management Strategy for 2018/19 and the revised affordable borrowing limits under the prudential framework. It also provides Members with a review of strategy and operations in 2017/18.

2 Background information

2.1 The operation of the Treasury Management function is governed by provisions set out under part 1 of the Local Government Act 2003 whereby the Council is required to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities as amended 2011 (See note 3.8), in particular:

- The Prudential Code requires that full Council set certain limits on the level and type of borrowing before the start of the financial year together with a number of Prudential Indicators.
- Any in year revision of these limits must be set by Council.
- Policy statements are prepared for approval by the Council at least two times a year.

3 Main Issues

3.1 Review of Strategy and Borrowing Limits 2017/18

3.1.1 The current debt forecasts are given in Table 1 below, which shows that net external borrowing is now expected to be £1,923m by the end of 2017/18. This is £26m below expectations in November 2017. This is due to slippage in the capital programme of £26m. The changes in the capital programme are included as a separate agenda item.

Table 1

ANALYSIS OF BORROWING 2017/18	2017/18 Feb 17 Report £m	2017/18 Nov 17 Report £m	2017/18 This Report £m
Net Borrowing at 1 April	1,877	1,809	**1,809**
New Borrowing for the Capital Programme – General Fund	145	157	**132**
New Borrowing for the Capital Programme – HRA	15	0	**0**
Debt redemption costs charged to Revenue (Incl HRA)	(13)	(12)	**(13)**
Reduced/(Increased) level of Revenue Balances	(5)	(5)	**(5)**
Net Borrowing at 31 March*	2,019	1,949	1,923
Capital Financing Requirement			**2,207**
* Comprised as follows			
Long term borrowing Fixed	1,466	1,565	1,565
Variable (less than 1 Year)	0	0	0
New Borrowing	142	140	114
Short term Borrowing	419	252	264
Total External Borrowing	2,027	1,957	1,943
Less Investments	8	8	20
Net External Borrowing	**2,019**	**1,949**	**1,923**
% gross borrowing exposed to interest rate risk	28%	20%	19%

Note: The Capital Financing Requirement (CFR) is the maximum level of debt (i.e. borrowing and finance leasing) that the Council can hold for its current year capital purposes. The Council is also allowed to borrow in advance for up to two future years capital programmes.

3.1.2 The MPC at its meeting on 1st and 2nd of November 2017 raised its bank rate from 0.25% to 0.50% reversing the cut in bank rate following the EU referendum vote in August 2016. This move was signposted at its September meeting and reflects two main drivers. Firstly inflation forecasts are now above 3% largely driven by the fall in the value of sterling although this is expected to move back to its 2% target over the two year time horizon. Secondly Unemployment has fallen to 4.3% its lowest level since 1975 and represents a reduction in spare capacity in the economy. It should also be noted that despite this fall in unemployment, wage inflation has remained subdued at 2.2% and this trend has been seen in nearly all western economies.

3.1.3 The impact of Brexit continues to be an additional source of uncertainty to markets in forecasting GDP growth and inflation. UK GDP Growth in 2017 is still below trend levels at 1.5% for the year. Therefore it is likely that further upwards moves in the bank rate will be brought forward slowly and the Council's advisors have indicated the next increase in rates will be at the end of 2018.

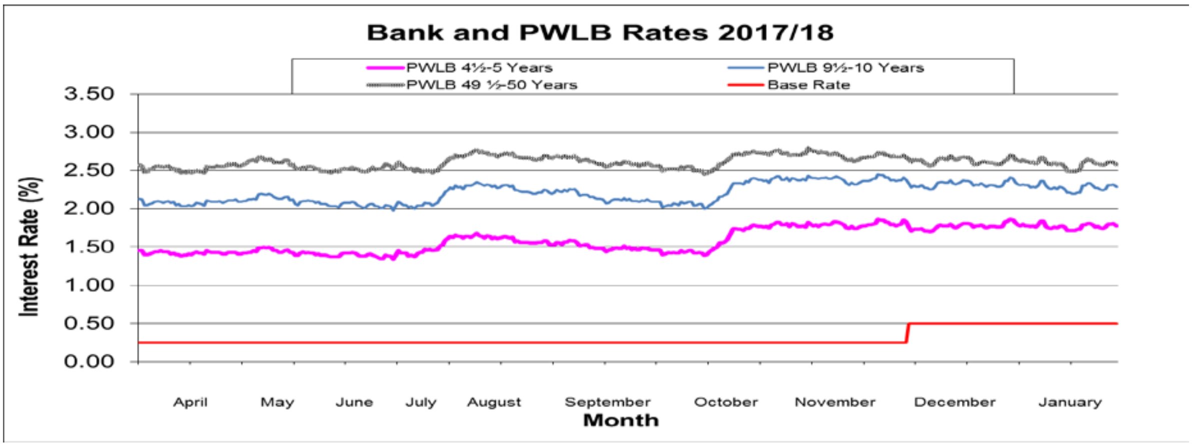
3.1.4 In the Eurozone, the ECB continues its Quantitative Easing (QE) programme but at a slower pace of €30 billion per month. Growth has picked up to 2.5% year on year, but headline inflation figures remain below the target of 2.0% at 1.4% (October 2017). Commentators therefore do not see any immediate likelihood of the European Central Bank Increasing interest rates soon and possibly not before 2019.

3.1.5 The US growth was mixed in 2017 but achieved 3.0% in Q3. Unemployment has fallen to 4.1% and the Federal Open Markets Committee (FOMC) is concerned with building inflation pressures and the FOMC has implemented 5 increases in the bank rate from its low point of near 0% to a current range of 1.25% to1.50%. Commentators are suggesting 4 more increases in 2018 and a continued unwinding of the $4.5 trillion QE which began in October 2017.

3.1.6 In Asia, Japan has been struggling to stimulate consistent significant growth and to get inflation up to its target of 2% despite sustained monetary and fiscal stimulus over a number of decades. In China, economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems.

3.1.7 The Council's treasury advisors' latest forecasts for Quarter 1, 2018 are that PWLB rates for 25 to 50 year borrowing will be around 2.60%, 10 year borrowing around 2.20% and 5 Year at 1.60%. Yields are expected to rise although the path and timing remain very uncertain.

Chart 1



3.1.8 The 2017/18 borrowing strategy continues to fund the capital programme borrowing requirement from short dated loans and internal cash balances whilst looking for opportunities to lock into attractive longer dated funding. The debt budget outturn is projected to deliver a balanced position. The ability to take longer term funding is discussed in the strategy for 2018/19 however table 2 below details the new borrowing taken during 2017/18.

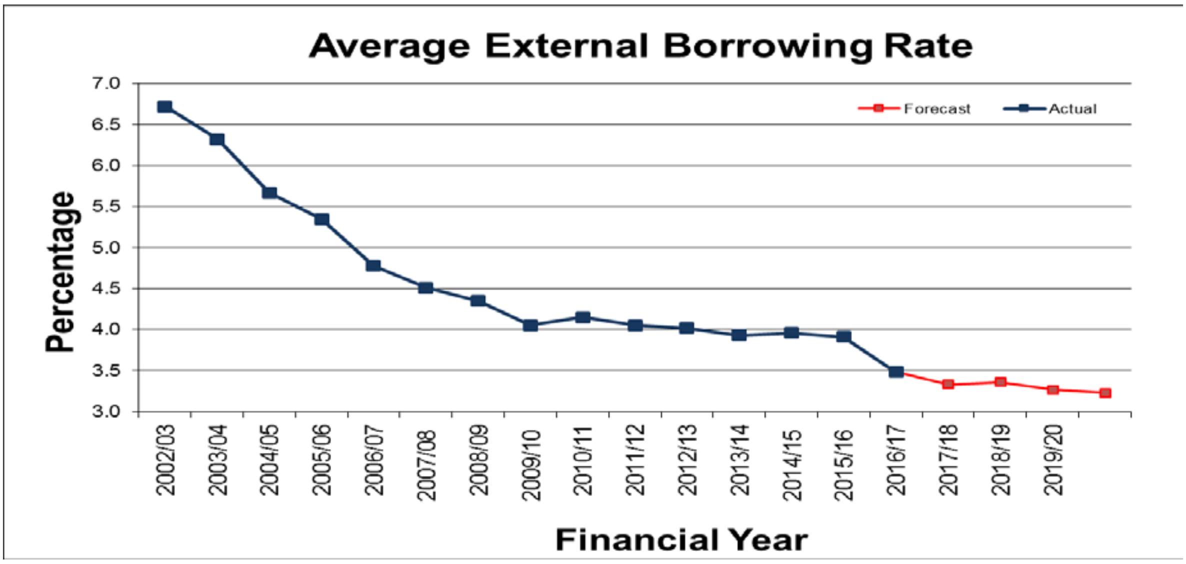
Table 2

Loan repayments and borrowing 2017/18							
Loan Repayments				New Borrowing			
Date	Amount (£m)	Original Rate (%)	Discount Rate	Date	Amount (£m)	Term (Years)	Interest Rate (%)
PWLB Loans				PWLB			
				03/04/2017	20.0	50	2.37
				19/04/2017	20.0	47	2.26
				26/06/2017	20.0	50	2.28
				15/08/2017	35.0	49	2.33
Sub Total	**0**				**95.0**		
Non PWLB Loans				Non PWLB Loans			
Sub Total	**0.0**				**0.0**		
Total	**0.0**			**Total**	**95.0**		

3.2 Interest Rate Review

3.2.1 The average rate of interest paid on the Council's external debt for 2016/17 was 3.91% as reported in the Annual Treasury Management report 2016/17 to Executive Board on 21st June 2017. This rate is forecast to fall to 3.33% for 2017/18 mainly due to the level of cheap short term borrowing that the Council has obtained. Chart 2 shows how the average, external borrowing rate has fallen from 6.72% in 2002/03. The longer term expectation is that the Councils average cost of borrowing will begin to rise as the cost of borrowing increases and short term funding is switched to more expensive longer term funding. The average rate may fall further if the rates currently available continue.

Chart 2



3.2.2 The projections for the first increase in the bank rate has moved from Q2 2019, as forecast in last year's strategy report to Q4 2018 as shown in Table 3. During August 2016 the UK had its first interest rate cut since 2009 when the bank rate was cut from 0.50% to 0.25%. This was subsequently reversed in November 2017 and it remains to be seen whether this rate increase will be made in isolation or whether it is the first on a steady path of base rate increases.

Table 3

	Bank Rate	**PWLB Borrowing Rates (including certainty rate adjustment)**			
		5 year	**10 Year**	**25 year**	**50 year**
Now	0.50	1.50	2.10	2.70	2.40
Dec 2017	0.50	1.50	2.10	2.80	2.50
March 2018	0.50	1.60	2.20	2.90	2.60
June 2018	0.50	1.60	2.30	3.00	2.70
Sept 2018	0.50	1.70	2.40	3.00	2.80
Dec 2018	0.75	1.80	2.40	3.10	2.90
March 2019	0.75	1.80	2.50	3.10	2.90
June 2019	0.75	1.90	2.60	3.20	3.00
Sept 2019	0.75	1.90	2.60	3.20	3.00
Dec 2019	1.00	2.00	2.70	3.30	3.10
March 2020	1.00	2.10	2.70	3.40	3.20
June 2020	1.00	2.10	2.80	3.50	3.30
Sept 2002	1.25	2.20	2.90	3.50	3.30
Dec 2020	1.25	2.30	2.90	3.60	3.40
March 2021	1.25	2.30	3.00	3.60	3.40

Source Council's Treasury Advisors

3.2.3 The forecast path of longer term rates is clearly dependent upon Brexit negotiations and how the economy performs both here and abroad. 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 a continuing and sustained US recovery, improvement in world economic activity or increase in inflation risks, then the strategy will be re-appraised with the likely outcome that longer term funding will be acquired. At that point the prospect of a higher debt cost would be viewed against whether:

- The forecast capital borrowing requirement had reduced or slipped into the following years,
- The levels of reserves/ balances were forecast to increase or reduce including whether the council had received up front funding for capital schemes.

3.3 Strategy for 2018/19

3.3.1 Table 4 shows that net borrowing is expected to rise by £117m to £2,040m during the course of 2018/19. This is a result of net new borrowing to fund the capital programme and a reduction in MRP chargeable in the year as a result of a review of MRP previously set aside. The Capital Programme report is presented elsewhere on this agenda.

Table 4

ANALYSIS OF BORROWING 2017/18 – 2020/21	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m
Net Borrowing at 1 April	1,809	1,923	2,040	2,147
New Borrowing for the Capital Programme – GF	132	143	106	168
New Borrowing for the Capital Programme - HRA	0	2	28	12
Debt redemption costs charged to Revenue(GF)	(13)	(22)	(20)	(50)
Reduced/(Increased) level of Revenue Balances	(5)	(6)	(7)	(7)
Net Borrowing at 31 March	1,923	2,040	2,147	2,270
* Comprised as follows				
Long term borrowing Existing Fixed	1,565	1,459	1,443	1,429
Existing Variable (Less than 1yr)	0	65	55	60
New Borrowing	114	117	107	123
Short term Borrowing	264	409	552	668
Total External Borrowing	1,943	2,050	2,157	2,280
Less Investments	20	10	10	10
Net External Borrowing	1,923	2,040	2,147	2,270
% gross borrowing exposed to interest rate risk	19%	29%	33%	37%
% gross interest rate risk exposure after £125m	19%	23%	28%	32%

Note: Borrowing exposed to interest rate risk in any one year is made up of short term borrowing, new long term borrowing and existing variable loans (i.e. LOBOs with an option falling within the year).

3.3.2 Table 4 above shows that over the 4 year time horizon the proportion of the Council's book exposed to interest rate risk is expected to rise to a maximum of 32% in 2020/21. This level is reached after taking £125m of longer term borrowing in 2018/19 to cover either new borrowing or to refinance maturities. This percentage will rise to 37% if no longer-term funding is taken. The Prudential Code specifies that the Variable Interest Rate exposure Indicator should be set in relation to net external borrowing position. This limit has been set at 40% and is recommended to be maintained at this level in 3.5.4 below. Included within the net external borrowing are two elements that are by definition variable, these are short term loans and LOBO loans with an option which falls within 12 months. No LOBO options are expected to be exercised during 2018/19. At the end of 2016/17 £215m of the Council's £445m LOBO portfolio was converted from LOBO loans to long term fixed rate loans with no options. This was as a result of one LOBO lender deciding to legally waive its options in perpetuity.

3.3.3 Alongside the prudential code structure the Council's current policy of using its balance sheet strength, reserves, provisions etc. to defray long term borrowing presents an additional risk that needs to be recognised. The Council has a forecast need to borrow, it's borrowing Capital Financing Requirement (CFR), at 31/03/2018 of £2,207m of which net external funding is expected to be £1,923m, the difference of £284m is the use of internal balance sheet strength to finance this need. The long term funding element of the external debt is forecast to be £1,565m and therefore, accepting that in current conditions LOBO options are unlikely to be exercised, the Council's gross exposure is the difference between its CFR and its current stock of long term external funding or £662m.

3.3.4 This exposure is considered manageable given historical capital programme slippage, the continued strength of the Council's balance sheet and the market for supplying short term funds remaining strong. These factors will continue to be monitored and should be considered in the context of the stability of the current debt maturity profile.

Given that short term rates continue at historical lows the Council will continue to fund the remaining borrowing requirement, if required, at short term rates.

3.3.5 This strategy is prudent as investment returns are low and counterparty risk remains a concern. This strategy is expected to continue into 2018/19 as the outlook for the bank rate remains well anchored at 0.50% with the next base rate rise not expected until late 2018. Given that further increases in the bank rate are expected to be slow and gradual, it remains prudent to continue with a strategy of financing a significant proportion of the funding requirement from short term loans. However, the 2018/19 budget strategy allows for £125m of borrowing during 2018/19 at 3% as market opportunities arise.

3.3.6 The current economic outlook and structure of market interest rates and government debt yields have several key treasury management implications:

- It is possible over the next few years that levels of government debt to GDP ratios could continue to rise to levels that could result in a loss of investor confidence in the financial viability of such countries. This could mean that sovereign debt concerns have not disappeared but, rather, have only been postponed. Counterparty risks therefore remain an ongoing concern.

- Effect of a change in US economic direction.

- Impact in the UK of Brexit negotiations and implications for trade, growth and inflation

- Investment returns are likely to remain relatively low during 2018/19 and beyond as rate rises are pushed back and the rate of increase is expected to be slow.

- Borrowing interest rates although higher than recent lows continue to be relatively cheap historically.

- If longer term borrowing is acquired before it is needed the result could be an increase in investments resulting in a revenue loss between borrowing costs and investment returns.

3.3.7 The Council’s current long term debt of £1.565bn has an average maturity of just over 38 years if all its debt runs to maturity. Approximately 15% of the Councils long term debt has options for repayment. In the unlikely event that all these options were exercised at the next option date then the average maturity would be lowered to a little under 26 years. This compares favourably with the average maturity of the UK Government debt portfolio of just over 15 years. The existing profile of the Council’s debt provides considerable certainty of funding costs. Prudential indicator 16 in Appendix A shows the maturity profile of the Council’s long term fixed debt and highlights that 75% or £1,128m matures in periods greater than 10 years.

3.3.8 The cost of debt is forecast to increase by £4.2m including MRP adjustments Forecasts for the debt budget beyond 2018/19 are dependent upon the interest rate assumptions, the likely level of capital spend and the Councils cash balances. The debt budget is currently forecast to increase by a further £7.0m in 2019/20 and £43.1m in 2020/21 including MRP costs and excluding usable capital receipts, based upon the assumptions on funding rates in Table 5. The interest rate assumptions and the borrowing requirement arising from the capital programme will be kept under review throughout 2018/19, before establishing the 2019/20 debt budget. Based upon historical performance of the capital programme the budget assumptions above allow for rephrasing of the borrowing requirement and include a reduction of £25m and £20m of borrowing in 2018/19 and 2019/20 and an increase of £45m in 2020/21.

Table 5

Assumed average funding rates	
	Average Interest Rate
2018/19	0.85%
2019/20	1.00%
2020/21	1.25%

3.3.9 These assumptions on borrowing rates have associated risks. For example in 2018/19, if the cost of borrowing was 0.25% higher than assumed, full year debt costs would increase by circa £1.1m.

3.4 Borrowing Limits for 2017/18, 2018/19, 2019/20 and 2020/21

3.4.1 The authorised limit represents the legislative limit on the Council's external debt under the Local Government Act 2003. It should be set with sufficient headroom above the operational boundary to allow flexibility for planned borrowing to be undertaken, in order for prudent treasury management decisions to be taken and temporary cash flow fluctuations to be managed. The operational boundary should reflect the maximum anticipated level of external debt consistent with budgets and cash flow forecasts. It should be seen as a management tool for on-going monitoring of external debt, and may be breached temporarily due to unusual cash flow movements.

3.4.2 Appendix B shows that the Council has kept within the operational boundary and authorised limit in 2017/18.

3.4.3 The Chief Officer Financial Services has delegated responsibility to make adjustments between the two separate limits for borrowing and other long term liabilities, provided that the overall limit remains unchanged. Any such adjustments will be reported to the next available Council meeting following the change. It is recommended that Council approve the following authorised limits for its gross external debt and other long term liabilities for the next three years.

3.4.4 After reviewing the forecast debt and borrowing position together with the forecast for revenue balances and effect of reduced MRP the Limit for borrowing is recommended to remain the same for the years 2017/18 to 2019/20 as detailed below. For 2020/21 a new limit should be set at £2,500m. The limit for Other Long Term Liabilities is recommended to remain the same for the years 2017/18 to 2019/20 as detailed below. It is further recommended that a new limit be set for the year 2019/20 of £660m to reflect the forecast decline in PFI liabilities.

Recommended: Authorised Limits as follows

Authorised Limit	**2017/18 £m**	**2018/19 £m**	**2019/20 £m**	**2020/21 £m**
Borrowing	2,450	2,450	2,500	2,500
Other Long Term Liabilities	740	720	690	660
Total	**3,190**	**3,170**	**3,190**	**3,160**

3.4.5 In line with the review of the authorised limits above it is proposed to amend the operational boundaries as detailed below. This limit will retain sufficient headroom to accommodate anticipated cashflow variances. The limit for Borrowing is recommended to remain the same for the years 2017/18 to 2019/20 as detailed below. For 2020/21, a new limit should be set at £2,350m. The limit for Other Long Term Liabilities is recommended to remain the same for the years 2017/18 to 2019/20 as detailed below. It is further recommended that a new limit be set for the year 2019/20 of £640m to reflect the forecast decline in PFI liabilities.

Recommended: Operational Boundaries as follows

Operational Boundary	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m
Borrowing	2,200	2,300	2,350	2,350
Other Long Term Liabilities	720	700	670	640
Total	**2,920**	**3,000**	**3,020**	**2990**

3.4.6 Table 6 below details the borrowing element of the Authorised limit and compares this to the projected CFR for borrowing only and does not include Other Long term liabilities. The revised Authorised limit and the Operational boundary remain below the projected CFR. The CFR is the Councils actual need to borrow based on its historic capital programme and forecast future capital programme. The lower limits reflect the significant level of balances being used internally to fund the borrowing need. These limits leave headroom for future large injections into the programme.

Table 6

year	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m	
Borrowing only					
CFR Projection.	2,223	2,330	2,451	2,536	
Authorised Limit					
Current	2,450	2,450	2,500	-	
Proposed	2,450	2,450	2,500	2,500	
Increase / (Decrease)	-	-	-	2,500	a
Operational boundary					
Current	2,200	2,300	2,350	-	
Proposed	2,200	2,300	2,350	2,350	
Increase / (Decrease)	-	-	-	2,350	a

a) Note 2020/21 has not been set previously as these limits are only set for the current +3 year time horiz

3.5 Treasury Management Indicators

3.5.1 Appendix A details the borrowing limits and other prudential indicators

3.5.2 The first prudential indicator in respect of treasury management is that the Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Services. This was adopted by the Council at the Executive Board meeting on the 13th March 2003.

3.5.3 The Council is required to set an upper limit on its fixed interest rate exposures that represents the maximum proportion of its net borrowing (i.e. measured as a percentage of its total borrowing less investments) which the Council will have at any given time during the period at fixed interest rates. The purpose of the limit is to ensure that the Council has the flexibility to take advantage of falling interest rates by ensuring a minimum level of variable rate debt. However setting a limit less than 100% can restrict the Council's ability to borrow in advance of need when long term fixed interest rates are at their low point. (This is the case since in general amounts borrowed in advance are invested, meaning that the net borrowing figure on which the limit is based will be lower than the total fixed borrowing outstanding.) Therefore to provide the Council with maximum flexibility it is recommended that the limit of 115% remains unchanged and is rolled forward into 2020/21

Recommended: Upper limit on fixed interest rate exposures for of 115% (no change)

3.5.4 The Council is required to set an upper limit on its variable interest rate exposures that represents the maximum proportion of debt the Council will have at any given time during the period at variable interest rates and exposed to interest rate rises. In evaluating this figure, LOBOs are treated as being variable in the year in which an option occurs and fixed in other years. The limit should be set in order to maintain a balance between managing the risk of rate rises and allowing sufficient flexibility to take advantage of any fall in rates. It is therefore recommended that the limit of 40% of debt remains unchanged and is rolled forward into 2020/21. It is acknowledged that unless fixed rate long term borrowing is undertaken over the 4 year timescale that by 2020/21 this limit would be approached but not broken on current forecasts.

Recommended: Upper limit on variable interest rate exposures for 2017/18, 2018/19, 2019/20 and 2020/21 of 40% (no change)

3.5.5 The Council is required to set upper and lower limits for the maturity structure of its borrowings. This is designed to limit the risk of exposure to high interest rates by restricting the level of maturing debt in any given year. The limits represent the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate. It is proposed that these limits remain unchanged.

<table>
<tr><th>Maturity structure of fixed rate borrowing</th><th>Lower Limit</th><th>Upper Limit</th></tr>
<tr><td>under 12 months</td><td>0%</td><td>15%</td></tr>
<tr><td>12 months and within 24 months</td><td>0%</td><td>20%</td></tr>
<tr><td>24 months and within 5 years</td><td>0%</td><td>35%</td></tr>
<tr><td>5 years and within 10 years</td><td>0%</td><td>40%</td></tr>
<tr><td>10 years and within 20 years</td><td rowspan="5">25%</td><td rowspan="5">90%</td></tr>
<tr><td>20 years and within 30 years</td></tr>
<tr><td>30 years and within 40 years</td></tr>
<tr><td>40 years and within 50 years</td></tr>
<tr><td>50 years and above</td></tr>
</table>

Recommended: Upper and Lower limits on fixed rate maturity structure remains unchanged as above.

3.6 Investment Strategy and Limits

3.6.1 The Council's actual external borrowing need is reduced by the availability of revenue balances. The Treasury policy allows for the external investment of these balances at advantageous rates but with due regard for security of capital invested. Investment of surplus balances in general will be limited to cash flow and liquidity management although the interest rate outlook will be kept under review to identify any opportunities for longer term investment.

3.6.2 The approved lending list is based upon the assessment of the financial standing of counterparties as determined by international credit rating agencies and further refined and updated by the Council's advisors on a continual basis. The lending list is often further restricted based upon the Council's own view of the credit worthiness of counter-parties

3.6.3 The investment strategy allows for the Council to invest in the most highly rated financial institutions around the world. The Council will only lend up to a maximum of £15m to financial institutions that are rated as excellent. There is also a limit of £5m for financial institutions that are rated as very good.

3.6.4 Any changes in the investment environment are being monitored closely as is the effect on the credit list supplied by the Council's treasury advisors. Other factors are also used in determining potential counterparties for the investment of funds over and above credit ratings

3.6.5 The Council under its existing Treasury Management Policy Statement has the authorisation to use Money Market Funds which it has not utilised to date. The rates offered on notice accounts by both the Council's bankers and by other banks offering similar products continues to be at low levels. This is thought to reflect the cost of carrying such cash on the balance sheet of these organisations under Basel III rules. As a result the levels on offer are at or below rates available from Money Market Funds which carry a higher credit worthiness rating**.** A review of the utility of these funds is being undertaken for depositing short term cash balances and any decision to utilise these accounts will be made under delegations already in place to the Chief Officer Financial Services.

3.6.6 The Prudential code requires that Councils set limits on investments for periods longer than 364 days. It is proposed to maintain the limits as outlined below and roll the limit forward into 2020/21

Recommended: Upper limit on sums invested for periods longer than 364 days (no change):

Total principal sum invested for a period longer than 364 days	**2016/17 £m**	**2017/18 £m**	**2018/19 £m**	**2019/20 £m**
Upper limit	150	150	150	150

3.7 Treasury Management Policy Statement

3.7.1 The Treasury Management Policy Statement has been updated for changes made to the Council's Investment Counterparty Criteria. These are reflected at Appendix D.

3.8 Changes to Codes, Guides and Other Market Rules.

3.8.1 During the year consultations have been undertaken by both the Department for Communities and Local Government (DCLG) and Chartered institute of Public Finance and accountancy (CIPFA) as detailed below.

3.8.2 The DCLG has undertaken a consultation on its guidance in relation to the following areas of which the council has a legal obligation to take note.

- Guidance on Investments
- Guidance on Minimum Revenue Provision (MRP)

3.8.3 CIPFA also has undertaken consultation on its codes of practice detailed below

- Treasury Management in the Public Services - Code of Practice and CS Guidance Notes – 2011
- The Prudential Code - for Capital Finance in Local Authorities - 2011

3.8.4 These revised CIPFA Codes and Practice and DCLG guidance will be adopted and reported to full Council when fully issued.

3.8.5 Additionally the European Union in summer 2017 issued a second Directive in relation to Financial Markets called Market in Financial Instruments Directive II (MiFIDII). The main change of this legislation is to change the status of all Councils from being classified as Professional to being reclassified as retail but with an option to elect up to professional status if they meet certain criteria. The Chief Financial Officer under delegated authority has elected to opt up to professional classification to allow the continued smooth operation of the treasury function with the London money markets, Brokers, banks etc. This legislation was implemented with effect from 3rd January 2018.

4 Corporate Considerations

4.1 Consultation and Engagement

4.1.1 This report sets the treasury management strategy and as such there is no need to consult the public. In establishing this strategy, consultation with the Council's treasury advisors has taken place.

4.1.2 The borrowing requirement is an outcome of the capital programme which has been the subject of consultation and engagement as outlined in the capital programme report elsewhere on this agenda.

4.2 Equality and Diversity / Cohesion and Integration

4.2.1 Equality, diversity, cohesion and integration requirements are addressed as part of individual capital scheme and programme approvals. The borrowing to deliver these capital schemes is executed through treasury strategy and as such there are no further equality diversity cohesion and integration issues. An equality screening document is attached at Appendix C.

4.3 Council policies and Best Council Plan

4.3.1 Treasury Management strategy secures funding to support the Council's Policies and City Priorities as set out in the Council capital programme and is consistent with the Best Council Plan.

4.4 Resources and Value for Money

4.4.1 This treasury strategy recognises the borrowing necessary to fund the capital programme requirements of both General Fund and HRA. The revenue costs of borrowing are included within the revenue budgets of the general fund and HRA.

4.4.2 The updated strategy 2017/18 is forecast to deliver on budget

4.5 Legal Implications, Access to Information and Call In

4.5.1 In accordance with the Council's Budget and Policy Framework, decisions on borrowing limits, treasury management indicators, investment limits and the Treasury Management Policy Statement are approved by Council. As such, recommendations 6.3 to 6.6 are not subject to call in.

4.6 Risk Management

4.6.1 This report sets out the framework for the treasury strategy for the year ahead. The execution of strategy and associated risks are kept under regular review through:

- Monthly reports to the Finance Performance Group
- Quarterly strategy meetings with the Chief Officer Financial Services and the Council's treasury advisors
- Regular market, economic and financial instrument updates and access to real time market information

5 Conclusions

5.1 The Council's level of external debt at 31st March 2018 is anticipated to be £1,923m, £26m lower than expected in November 2017, rising to £2,040m in 2018/19 and to £2,147m by 2019/20.

5.2 The cost of debt is forecast to outturn on budget in 2017/18. The impact of the capital programme and forecast interest rate increases will see an overall increase in debt costs of £4.2m in 2018/19.

5.3 The uncertainty and risks around economic forecasts will result in further caution being adopted in the management of debt and investments and the opportunity to secure longer term debt at the appropriate time will be kept under review.

5.4 The Treasury Management Policy Statement has been updated to reflect changes in how the approved investment counterparty list is compiled.

6 Recommendations

That the Executive Board:

6.1 Approve the treasury strategy for 2018/19 as set out in Section 3.3 and note the review of the 2017/18 strategy and operations set out in Sections 3.1 and 3.2

6.2 Note that revised CIPFA Codes and Practice and DCLG guidance will be adopted and reported to full Council when fully issued and that the Council has implemented the European Union Market in Financial Instruments Directive (MiFIDII) legislation with effect from 03/01/2018.

That Executive Board recommend to full Council that:

6.3 The borrowing limits for 2017/18, 2018/19, 2019/20 and 2020/21 be set as detailed in Section 3.4 and note the changes to both the Operational Boundary and the Authorised limits.

6.4 The treasury management indicators for 2017/18, 2018/19, 2019/20 and 2020/21 be set as detailed in Section 3.5.

6.5 The investment limits for 2017/18, 2018/19, 2019/20 and 2020/21be set as detailed in Section 3.6.

6.6 The revised Treasury Management Policy Statement is adopted.

7 Background documents [1]

None

[1] The background documents listed in this section are available to download from the Council's website, unless they contain confidential or exempt information. The list of background documents does not include published works.

Leeds City Council - Prudential Indicators 2017/18 - 2020/21 **Appendix A**

No.	PRUDENTIAL INDICATOR	2017/18	2018/19	2019/20	2020/21
	(1). EXTRACT FROM BUDGET AND RENT SETTING REPORTS				
	Ratio of Financing Costs to Net Revenue Stream				
1	General Fund - Excluding DSG **(Note1)**	9.94%	12.66%	12.46%	18.92%
2	HRA	11.31%	11.40%	11.61%	11.41%
	Estimates of the Incremental Impact of new capital investment decisions	£ . P	£ . P	£ . P	£ . P
3	increase in council tax B7(band D, per annum) **(Note 2)**	9.11	39.43	66.66	92.62
4	increase in housing rent per week	0.00	0.01	0.20	0.56
		£'000	**£'000**	**£'000**	**£'000**
5	**Net external borrowing requirement (Net Debt and CFR)**	1,923,000	2,040,000	2,147,000	2,270,000
	The Net Borrowing Requirement should not exceed the capital financing requirement **(Note 3)**	OK	OK	OK	OK
	Estimate of total capital expenditure	**£'000**	**£'000**	**£'000**	**£'000**
6	General Fund	258,965	288,496	223,515	292,468
7	HRA	84,292	92,387	131,000	101,188
	TOTAL	343,257	380,883	354,515	393,656
	Capital Financing Requirement (as at 31 March)	**£'000**	**£'000**	**£'000**	**£'000**
8	General Fund	2,004,600	2,121,677	2,204,014	2,317,618
9	HRA	815,075	811,599	832,842	838,597
	TOTAL	2,819,675	2,933,276	3,036,856	3,156,215
9a	**Limit of HRA Indebtedness as implemented under self financing**	721,327	721,327	721,327	721,327

No.	PRUDENTIAL INDICATOR	2017/18	2018/19	2019/20	2020/21
	(2). TREASURY MANAGEMENT PRUDENTIAL INDICATORS	**£'000**	**£'000**	**£'000**	**£'000**
10	**Authorised limit for external debt - (Note 5)**				
	borrowing	2,450,000	2,450,000	2,500,000	2,500,000
	other long term liabilities	740,000	720,000	690,000	660,000
	TOTAL	3,190,000	3,170,000	3,190,000	3,160,000
11	**Operational boundary - (Note 5)**				
	borrowing	2,200,000	2,300,000	2,350,000	2,350,000
	other long term liabilities	720,000	700,000	670,000	640,000
	TOTAL	2,920,000	3,000,000	3,020,000	2,990,000
14	**Upper limit for fixed interest rate exposure**				
	expressed as either:-				
	Net principal re fixed rate borrowing / investments OR:-	115%	115%	115%	115%
	Net interest re fixed rate borrowing / investments				
15	**Upper limit for variable rate exposure**				
	expressed as either:-				
	Net principal re variable rate borrowing / investments OR:-	40%	40%	40%	40%
	Net interest re variable rate borrowing / investments				
		£'000	**£'000**	**£'000**	**£'000**
17	**Upper limit for total principal sums invested for over 364 days (Note 5)** (per maturity date)	150,000	150,000	150,000	150,000
18	**Net Debt as a percentage of Gross debt**	98.97%	99.51%	99.54%	99.56%

16	**Maturity structure of fixed rate borrowing 2017/18**	Lower Limit	Upper Limit	Projected 31/03/2018	
	under 12 months	0%	15%	3%	
	12 months and within 24 months	0%	20%	5%	
	24 months and within 5 years	0%	35%	12%	
	5 years and within 10 years	0%	40%	5%	
	10 years and within 20 years			2%	
	20 years and within 30 years			0%	
	30 years and within 40 years	25%	90%	41%	75%
	40 years and within 50 years			24%	
	More Than 50 Years			8%	
			100%		

Notes.

1 **The indicator for the ratio of financing costs to net revenue stream for General Fund is now calculated based on the Net Revenue Charge less the Dedicated Schools Grant (DSG). The Government changed the funding of education to DSG from 2006/07.**

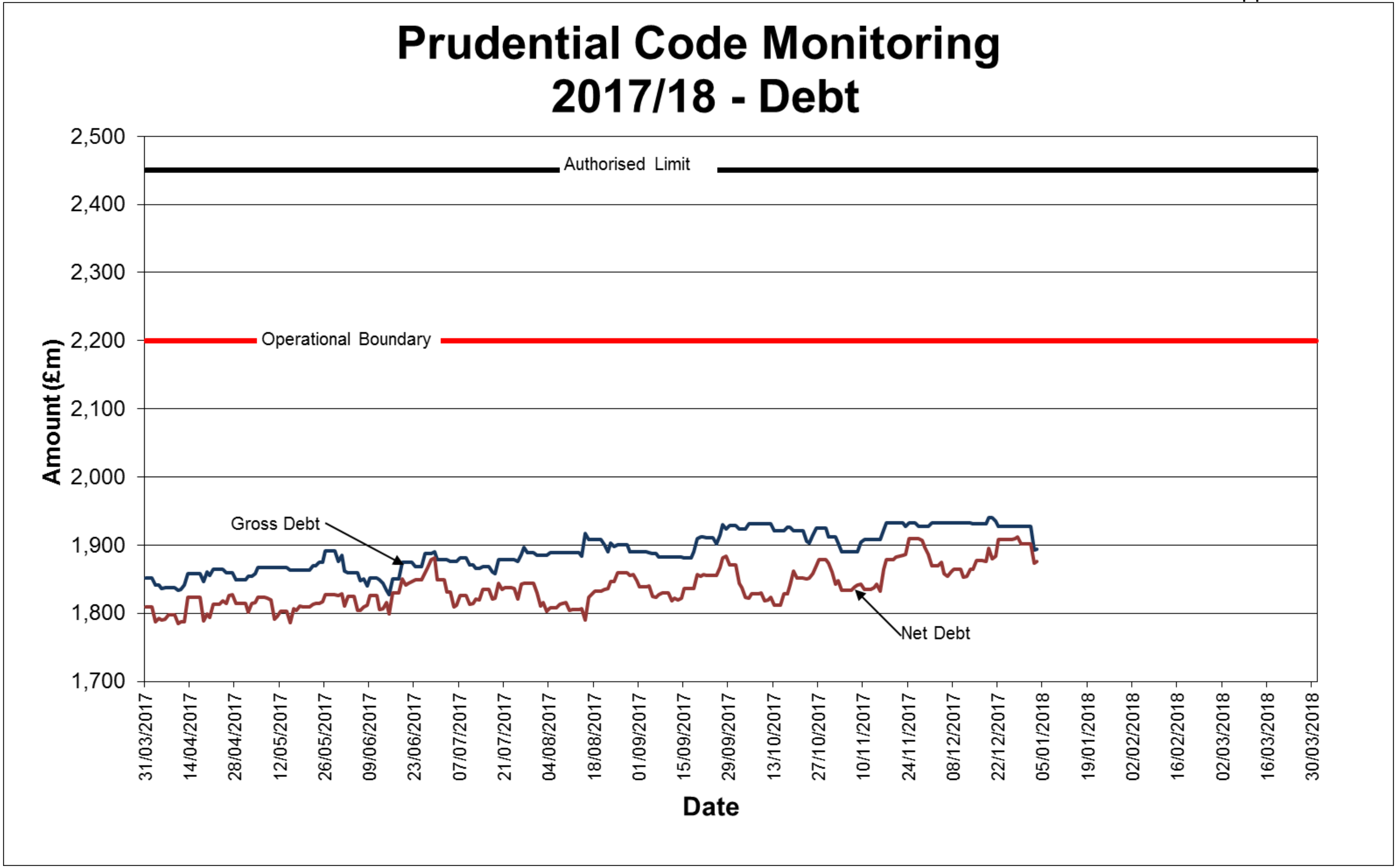
2 **The code requires that the Council identifies the capital financing costs arising from unsupported borrowing expressed as the amount per band D property.**

3 **In order to ensure that over the medium term net borrowing will only be for a capital purpose, the Council should ensure that net external borrowing does not exceed the total capital financing requirement in the preceding year plus estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence.**

4 **Prudential indicator 12 relates to actual external debt at 31st March, which will be reported in the Treasury Management Annual Report.**

5 **Prudential indicator 13 relates to the adoption of the CIPFA Code of Practice on Treasury Management. The Council formally adopted this Code of Practice in March 2003, and the revised code in 2013. The latest update will be incorporated in the next update to Executive Board**

Appendix B



Prudential Code Monitoring
2017/18 - Debt
Authorised Limit
Operational Boundary
Gross Debt
Net Debt
Amount (£m)
2,500
2,400
2,300
2,200
2,100
2,000
1,900
1,800
1,700
31/03/2017
14/04/2017
28/04/2017
12/05/2017
26/05/2017
09/06/2017
23/06/2017
07/07/2017
21/07/2017
04/08/2017
18/08/2017
01/09/2017
15/09/2017
29/09/2017
13/10/2017
27/10/2017
10/11/2017
24/11/2017
08/12/2017
22/12/2017
05/01/2018
19/01/2018
02/02/2018
16/02/2018
02/03/2018
16/03/2018
30/03/2018
Date

Appendix C
Equality, Diversity, Cohesion and Integration Screening

As a public authority we need to ensure that all our strategies, policies, service and functions, both current and proposed have given proper consideration to equality, diversity, cohesion and integration.

A **screening** process can help judge relevance and provides a record of both the **process** and **decision.** Screening should be a short, sharp exercise that determines relevance for all new and revised strategies, policies, services and functions. Completed at the earliest opportunity it will help to determine:

- the relevance of proposals and decisions to equality, diversity, cohesion and integration.
- whether or not equality, diversity, cohesion and integration is being/has already been considered, and
- whether or not it is necessary to carry out an impact assessment.

Directorate: Resources & Housing	**Service area: Capital, Insurance and Treasury Management**
Lead person: Bhupinder Chana	**Contact number: 88044**

1. Title: Treasury Management Strategy 2018/19
Is this a: [X] **Strategy / Policy** [ ] **Service / Function** [ ] **Other** **If other, please specify**

2. Please provide a brief description of what you are screening
The report sets out the treasury management strategy for 2018/19. The strategy outlines the approach to managing the Council's borrowing requirements in the light of its capital programme, cash balances and reserves and economic conditions including forecasts of interest rates.

3. Relevance to equality, diversity, cohesion and integration

All the council's strategies/policies, services/functions affect service users, employees or the wider community – city wide or more local. These will also have a greater/lesser relevance to equality, diversity, cohesion and integration.

The following questions will help you to identify how relevant your proposals are.

When considering these questions think about age, carers, disability, gender reassignment, race, religion or belief, sex, sexual orientation. Also those areas that impact on or relate to equality: tackling poverty and improving health and well-being.

Questions	Yes	No
Is there an existing or likely differential impact for the different equality characteristics?		X
Have there been or likely to be any public concerns about the policy or proposal?		X
Could the proposal affect how our services, commissioning or procurement activities are organised, provided, located and by whom?		X
Could the proposal affect our workforce or employment practices?		X
Does the proposal involve or will it have an impact on		
• Eliminating unlawful discrimination, victimisation and harassment		X
• Advancing equality of opportunity		X
• Fostering good relations		X

If you have answered **no** to the questions above please complete **sections 6 and 7**

If you have answered **yes** to any of the above and;

- Believe you have already considered the impact on equality, diversity, cohesion and integration within your proposal please go to **section 4.**
- Are not already considering the impact on equality, diversity, cohesion and integration within your proposal please go to **section 5.**

4. Considering the impact on equality, diversity, cohesion and integration
If you can demonstrate you have considered how your proposals impact on equality, diversity, cohesion and integration you have carried out an impact assessment. Please provide specific details for all three areas below (use the prompts for guidance).
• **How have you considered equality, diversity, cohesion and integration?** (**think about** the scope of the proposal, who is likely to be affected, equality related information, gaps in information and plans to address, consultation and engagement activities (taken place or planned) with those likely to be affected)
• **Key findings** **(think about** any potential positive and negative impact on different equality characteristics, potential to promote strong and positive relationships between groups, potential to bring groups/communities into increased contact with each other, perception that the proposal could benefit one group at the expense of another)

• **Actions** **(think about** how you will promote positive impact and remove/ reduce negative impact)

5. If you are **not** already considering the impact on equality, diversity, cohesion and integration you **will need to carry out an impact assessment**.	
Date to scope and plan your impact assessment:	
Date to complete your impact assessment	
Lead person for your impact assessment (Include name and job title)	

6. Governance, ownership and approval Please state here who has approved the actions and outcomes of the screening		
Name	**Job title**	**Date**
Bhupinder Chana	Head of Finance - Technical	10th January 2018
Date screening completed		10th January 2018

7. Publishing	
Though **all** key decisions are required to give due regard to equality the council **only** publishes those related to **Executive Board**, **Full Council, Key Delegated Decisions** or a **Significant Operational Decision.** A copy of this equality screening should be attached as an appendix to the decision making report: • Governance Services will publish those relating to Executive Board and Full Council. • The appropriate directorate will publish those relating to Delegated Decisions and Significant Operational Decisions. • A copy of all other equality screenings that are not to be published should be sent to equalityteam@leeds.gov.uk for record. Complete the appropriate section below with the date the report and attached screening was sent:	
For Executive Board or Full Council – sent to **Governance Services**	Date sent: 10th January 2018
For Delegated Decisions or Significant Operational Decisions – sent to appropriate **Directorate**	Date sent:
All other decisions – sent to equalityteam@leeds.gov.uk	Date sent:

Appendix D

Treasury Management Policy Statement

1 Introduction

1.1 The following document sets out the Treasury Management Policy Statement (TMPS) for the Authority, which fully complies with the requirements of the CIPFA Prudential Code and ode of Practice.

2 Background

2.1 CIPFA first published its Code of Practice on Treasury Management in May 1992. There have been subsequent revisions over the years culminating in the latest version of the code, the fully revised Third Edition 2011, which recommends that all public service organisations adopt, as part of their standing orders and financial procedures, the following four clauses.

a) This Authority adopts the key recommendations of CIPFA's *Treasury Management in the Public Services: Code of Practice* (the Code), as described in Section 4 of that Code.

b) Accordingly, this Authority will create and maintain, as the cornerstones of effective treasury management:

- A TMPS (Treasury Management Policy Statement), stating the policies and approach to risk management of its treasury management activities
- Suitable Treasury Management Practices (TMP’s), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities. A full set of TMP’s are maintained on the Treasury Section

c) The Executive Board will receive reports on its treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a half year update and an annual report after its close, in the form prescribed in its TMP’s.

d) This organisation delegates responsibility for the implementation and monitoring of its treasury management policies and practices to the Executive Board, and for the execution and administration of treasury management decisions to the Chief Finance Officer*,* who will act in accordance with the organisation's TMPS and Treasury Management Practices and, if he/she is a CIPFA member, CIPFA's *Standard of Professional Practice on Treasury Management.*

e) This organisation nominates the Corporate Governance and Audit committee to be responsible for ensuring the effective scrutiny of the treasury management strategy and Policies

2.2 CIPFA recommends that an organisation’s TMPS adopts the following forms of words to define the policies and objectives of its treasury management activities:

- This organisation defines its treasury management activities as: "The management of the organisation's 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."
- This organisation regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its

treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation and any financial instruments entered into to manage these risks.

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

2.3 These key recommendations and form of words as specified above were adopted by the Executive Board on the 12th March 2003.

2.4 The operation of the Treasury Management function is governed by provisions set out under part 1 of the Local Government Act 2003 whereby the Council is required to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities.

2.5 The Prudential Code requires that full Council set certain limits on the level and type of borrowing before the start of the financial year together with a number of Prudential Indicators. Any in year revision of these limits must similarly be set by Council.

3 Objectives of Treasury Management

3.1 The primary objective is to reduce the cost of debt management with which the other objectives are deemed to be consistent. Varying degrees of emphasis will be placed upon the “secondary objectives” at different times contingent upon prevailing market conditions.

3.2 The objectives are identified as follows:

a) To reduce the cost of debt management;

b) To ensure that the management of the HRA and general fund is treated equally and new accounting principles are examined to provide benefits where possible;

c) To effect funding at the lowest point of the interest rate cycle;

d) To maintain a flexible approach regarding any financial matters that may affect the Authority;

e) To keep under constant review advice on investment/repayment of debt policy;

f) To maintain a prudent level of volatility dependent upon interest rates;

g) To set upper and lower limits for the maturity structure of its borrowings and to maintain a reasonable debt maturity profile;

h) To specifically ensure that Leeds City Council does not breach Prudential Limits passed by the Council;

i) To ensure that the TMPS is fully adhered to in every aspect.

4 Approved Activities of the Treasury Management Operation

4.1 The approved activities of the Treasury Management operation cover:

a. borrowing;

b. lending;

c. debt repayment and rescheduling;

d. financial instruments new to the authority (including financial derivatives);

e. risk exposure; and

f. cash flow.

4.2 It is the Council's responsibility to approve the TMPS. The Executive Board will receive and consider as a minimum:

a) an annual treasury management strategy before the commencement of the new financial year (which sets out the likely operations for the forthcoming year);

b) a mid-year update on treasury strategy;

c) an annual report on the treasury management activity after the end of the year to which it relates.

4.3 The Chief Finance Officer will:

a) implement and monitor the TMPS, revising and resubmitting it for consideration to the Executive Board and the Council, periodically if changes are required;

b) draft and submit a Treasury Management Strategy to the Executive Board, in advance of each financial year;

c) draft and submit an update report on treasury management activity to the Executive Board

d) draft and submit an annual report on treasury management activity to the Executive Board; and

e) implement and monitor the Strategy, reporting to the Executive Board any material divergence or necessary revisions as and when required;

5 Formulation of Treasury Management Strategy

5.1 Whilst this TMPS outlines the procedures and considerations for the treasury function as a whole, requiring revision occasionally, the Treasury Management Strategy sets out the specific expected treasury activities for the forthcoming financial year. This strategy will be submitted to the Executive Board for approval before the commencement of each financial year.

5.2 The formulation of the annual Treasury Management Strategy involves determining the appropriate borrowing and investment decisions in the light of the anticipated movement in both fixed and shorter term variable interest rates (for instance, the Council may postpone borrowing if fixed interest rates are falling).

5.3 The Treasury Management Strategy is also concerned with the following elements:

a) the prospects for interest rates;

b) the limits placed by Council on treasury activities (per this TMPS);

c) the expected borrowing strategy;

d) the temporary investment strategy;

e) the expectations for debt rescheduling.

5.4 The Treasury Management Strategy will establish the expected move in interest rates against alternatives (using published forecasts where applicable), and highlight sensitivities to different scenarios.

6 Approved Methods and Sources of Raising Capital Finance

6.1 Under the Local Government Act 2003 a local authority may borrow money for:

a) for any purpose relevant to its functions under any enactment, or
b) for the purposes of the prudent management of its financial affairs.

A local authority may not, without the consent of the Treasury, borrow otherwise than in sterling.

6.2 Local authorities have in the past only been able to raise finance in accordance with the Local Government and Housing Act 1989, and within this limit the Council has a number of approved methods and sources of raising capital finance. These are:

		Fixed	**Variable**
	Public Works Loans Board (PWLB)	•	•
	European Investment Bank (EIB)	•	•
*	Stock Issues	•	•
	Market Long-Term	•	•
	Market Temporary	•	•
	Local Temporary	•	•
*	Local Bonds	•	
	Overdraft		•
*	Negotiable Bonds	•	•
	Internal (capital receipts & revenue balances)	•	•
*	Commercial Paper	•	
*	Medium Term Notes	•	
	Finance Leases	•	•

***** (Not used at present by this Council)

6.3 The revised treasury management code of practice (2011), through the Localism Act 2011, gave local authorities the power to use derivatives for interest rate risk Management. These instruments will only be used after a review of their appropriateness for interest rate risk management is undertaken.

7 Approved Instruments and Organisations for Investments

7.1 With effect from the 1st April 2004, to coincide with the introduction of the prudential code, new legislation has been issued to deal with the issue of Local Government Investments. This legislation lifts the restrictions on Councils with external debt to not hold investments for more than 364 days. Further freedoms are also provided which will give Councils greater flexibility and hence access to higher returns, provided that any investment strategy is consistent with the new prudential framework.

7.2 The Council will have regard to the CLG Guidance on Local Government Investments (second Edition) issued in March 2010 and CIPFAs Treasury

Management in Public Services Code of Practice and Cross Sectoral Guide. The Council's investment priorities are:

a) The security of capital

b) The liquidity of investments

c) and finally, the yield of the investment

7.3 The Council will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The Council does not have the authority to undertake borrowing purely to invest or lend and make a return as this is unlawful and will not engage in such activity.

7.4 The Chief Finance Officer will formulate suitable criteria for assessing and monitoring the credit risk of investment counterparties and shall construct a lending list comprising time, type and specific counterparty limits. This criterion is outlined below. Should any revisions occur to the criteria, they will be submitted to the Executive Board for approval. Where individual counterparties newly obtain the required criteria, they will be added to the list. Similarly, those ceasing to meet the criteria will be immediately deleted. The criteria uses ratings from the three rating agencies and those relating to Fitch are explained in Annexe A.

7.5 The Council's approved Treasury Policy is to use the recommended lending list provided by the Council's treasury advisers. This list is compiled on a matrix approach using data from recognised international credit rating agencies as well as information on individual counterparties drawn from Credit Default Swap (CDS) levels, which provide ratings of institutions across four categories. The rankings of institutions regarded as excellent is split into eight colours (yellow, dark pink, light pink, purple, blue, orange, red and green) to reflect the length of time over six months that amounts can be placed with them and to reflect the explicit support level given to UK part nationalised banks (Blue), and the special category for investment in UK gilts, UK Locals, supranational's and collateralised deposits (Yellow). Regular updates are made to this list, as institutions' credit ratings change. The use of the list was introduced and reported to Executive Board in the Treasury Strategy and Policy report of February 2002 with updates since.

The following investment limits are applied by the Council's Treasury policy:

Advisor Ranking	**Meaning**	**Limit on Amount Lent**	**Current Limits on Duration**
Green	Good	£5m	100 Days
Red	Excellent	£15m	6 Months
Orange	Excellent	£15m	1 Year
Purple	Excellent	£15m	2 Years
Other			
Blue	Excellent	£15m	1 Year
Dark Pink	Excellent	£15m	N/A
Light Pink	Excellent	£15m	N/A
Yellow	Excellent	£15m	5 Years

The CDS subjective overlay is then applied to the general banks and further reduces the suggested limits of duration as shown in the following table:

Initial Duration (Months)	Suggested Duration (watch/ outlook)	CDS Status	Suggested Adjusted Colour	Adjusted Duration (Months)
0	N/C	In Range	N/C	0
0	N/C	Monitoring	N/C	0
0	N/C	Out of Range	N/C	0
3	G	In Range	G	3
3	G	Monitoring	N/C	0
3	G	Out of Range	N/C	0
6	R	In Range	R	6
6	R	Monitoring	G	3
6	R	Out of Range	N/C	0
12	O	In Range	O	12
12	O	Monitoring	R	6
12	O	Out of Range	N/C	0
24	P	In Range	P	24
24	P	Monitoring	O	12
24	P	Out of Range	N/C	0

7.6 The Council will lend up to £15 million to an institution ranked as ‘excellent’ and up to £5 million for up to 3 months to an institution ranked as ‘good’. A number of these institutions exist within the same group of companies as parents or subsidiaries. A limit to the risk exposure of the Council for groups of banks borrowing limit has also been set of £30m. These limits do not apply to the Councils’ banker where we have an unlimited deposit facility as part of our banking arrangements. The Council's banking arrangements are the subject of a separate contract, and as such volumes and levels of transactions are not subject to the counterparty ratings and limits that are in place on external investments. Other local authorities are classified with an excellent rating and as such attract a £15m investment limit for a maximum of 5 years (Yellow classification).

7.7 Within the investment limits outlined above the Council has access to a number of investment instruments. These are listed below as specified and non-specified investment categories. Specified investments are defined as “minimal procedural formalities” under the March 2004 ODPM guidance revised 2010 under DCLG.

a) **<u>Specified Investments</u>**

(All such investments will be sterling denominated, with **maturities of any period meeting** the minimum ‘high’ rating criteria where applicable)

Fixed Term Deposits with fixed rates	**Use**
Debt Management Agency Deposit Facility	In-house
Term deposits – local authorities	In-house
Term deposits – banks and building societies	In-house and fund managers

In the following table the determination as to whether the following are specified or non-specified is at the discretion of the Authority depending on the element of the return that is fixed, **provided that the maturity of the investment falls within 1 year.**

Fixed term deposits with variable rate and variable maturities: -	
1. Callable deposits	In-house and fund managers
2. Range trade	In-house and fund managers
3. Snowballs	In-house and fund managers
Certificates of deposits issued by banks and building societies	In-house buy and hold and fund managers
UK Government Gilts	In-house buy and hold and Fund Managers
Bonds issued by multilateral development banks	In-house on a ‘buy-and-hold’ basis. Also for use by fund managers
Bonds issued by a financial institution which is guaranteed by the UK government	In-house on a ‘buy-and-hold’ basis. Also for use by fund managers
Sovereign bond issues (i.e. other than the UK government)	In house on a ‘buy and hold basis’ and Fund Managers
Treasury Bills	Fund Managers
Collective Investment Schemes structured as Open Ended Investment Companies (OEICs):	
1. Money Market Funds	In-house and fund managers
2. Enhanced cash funds	In-house and fund managers
3. Short term funds	In-house and fund managers
4. Bond Funds	In-house and Fund Managers
5. Gilt Funds	In-house and Fund Managers

Note: If forward deposits are to be made, the forward period plus the deal period should not exceed one year in aggregate.

b) **<u>Non-Specified Investments:</u>**

Non-specified investments are those where the return is uncertain.

Maturities of ANY period.

	Use
Corporate Bonds : ***the use of these investments would constitute capital expenditure***	In house on a 'buy and hold basis' and Fund Managers
Floating Rate Notes : ***the use of these investments would constitute capital expenditure unless they are issued by a multi lateral development bank***	Fund managers

All the investments in the following table are non-specified as returns could be uncertain and **the maturity of the investment is greater than 1 year.**

Fixed term deposits with variable rate and variable maturities	
1. Callable deposits	In-house and fund managers
2. Range trade	In-house and fund managers
3. Snowballs	In-house and fund managers
Certificates of deposits issued by banks and building societies	In house on a 'buy and hold basis' and Fund managers
UK Government Gilts	In house on a 'buy and hold basis' and Fund Managers
Bonds issued by multilateral development banks	In-house on a 'buy-and-hold' basis. Also for use by fund managers
Bonds issued by a financial institution which is guaranteed by the UK government	In-house on a 'buy-and-hold' basis. Also for use by fund managers
Sovereign bond issues (i.e. other than the UK govt)	In house on a 'buy and hold basis' and Fund Managers
Collateralised deposits	In house and fund managers
Property fund: ***the use of these investments would constitute capital expenditure***	Fund manager
1. Bond Funds	In-house and Fund Managers
2. Gilt Funds	In-house and Fund Managers
Collective Investment Schemes structured as Open Ended Investment Schemes	
Bond Funds	In-house and Fund Managers
Gilt Funds	In-house and Fund Managers

7.8 The Chief Finance Officer will continue to monitor the range of investment instruments available and make changes to the list as appropriate.

8 Investments on Behalf of Council Managed Charities and Trusts

8.1 The Council currently invests surplus balances on behalf of trust funds and Charities in the name of the Council and investments are within the overall counterparty limits identified in 7.6 above.

8.2 To provide the Council and Charities/Trusts with a greater degree of flexibility the Council will have the option to invest monies on behalf of charities and trusts over and above the Council's own investment limits. This additional investment will be subject to individual Charity/Trust fund Board approval.

8.3 The Council only invests in those counterparties that are on the approved list as per the investment criteria outline in 7.5 above. Investments made on behalf of Charities/Trust funds are subject to the same criteria unless there is specific Charity/Trust fund approval in place to invest in other counterparties.

9 Policy on Interest Rate Exposure

9.1 As required by the Prudential Code, the Council must approve before the beginning of each financial year the following treasury limits:

a) the overall borrowing limit;

b) the maximum proportion of interest on borrowing which is subject to variable rate interest.

9.2 The Chief Finance Officer is responsible for incorporating these limits into the Annual Treasury Management Strategy, and for ensuring compliance with the limits. Should it prove necessary to amend these limits, the Chief Finance Officer shall submit the changes for approval to the Executive Board before submission to the full Council for approval.

10 Policy on External Managers

10.1 The Council has taken the view that the appointment of external fund managers would not provide an enhanced return over what could be achieved by managing investment in house.

10.2 However, the fact that a fund manager's expertise allows for a wider investment portfolio than would be operated by Council officers may give opportunities for capital gains to supplement interest earned on investment of revenue balances.

10.3 It is felt appropriate therefore that the Policy allows for the use of external fund managers and although none are being used at present, this situation will be kept under review. Appointment of a fund manager would take place following a tender exercise and submissions on target performance.

11 Policy on Delegation and Review Requirements and Reporting Arrangements

11.1 The Council is responsible for determining the borrowing limits detailed in section 8 above. Other responsibilities and duties are delegated as follows.

11.2 The Executive Board has responsibility for determining and reviewing treasury strategy and performance. (See section 5 above).

11.3 The Chief Finance Officer and through him/her to his/her staff has delegated powers for all borrowing and lending decisions. This delegation is required in order that the authority can react immediately to market interest rate movements and therefore achieve the best possible terms. The Chief Finance Officer and staff will operate in accordance with the Code of Practice for Treasury Management in Local Authorities.

11.4 The treasury management governance framework and the delegations within the Strategy and Resources Directorate shall operate on the following basis and is summarised in Annexe B:

a) The practical organisation within the Strategy and Resources Directorate is that all aspects of borrowing/lending strategy over the year are determined or reported to regular monthly meetings of the Finance Performance Group attended by the Chief Officer (Audit and Investments), Chief Officer (Financial Services) and Heads of Finance. Quarterly, treasury strategy review meetings take place with the Chief Finance Officer, Chief Officer (Audit and Investments), Chief Officer (Financial Services), the Head of Finance (Capital Insurance and Treasury Management) and the Senior Treasury Manager.

b) Implementation of decisions at such meetings and the day to day management of the Treasury Operations are delegated without limit to the Chief Officer (Financial Services) or in his/her absence and through him her to either the Chief Officer (Audit and Investments), Head of Finance (Capital Insurance and Treasury Management) or the Senior Treasury Manager and on occasions the Assistant Finance Manager.

c) Consultations will be made by the Chief Finance Officer on Treasury Management matters with:

- The Chief Executive: so that he/she can ensure proper Treasury systems are in place and are properly resourced.

- External Treasury Advisers: so that they can advise and monitor the process of fixing strategy and policy on Treasury Matters and advise on the economic outlook, prospects for interest rates and credit worthiness

FITCH CREDIT RATING DEFINITIONS

Source: Fitch Ratings

International Short-Term Credit Ratings

A short-term rating has a time horizon of less than 12 months for most obligations, or up to three years for US public finance securities, and thus places greater emphasis on the liquidity necessary to meet financial commitments in a timely manner.

Fl *Highest credit quality*. Indicates the strongest capacity for timely payment of financial commitments; may have an added "+" to denote any exceptionally strong credit feature.

F2 *Good credit quality*. A satisfactory capacity for timely payment of financial commitments, but the margin of safety is not as great as in the case of the higher ratings.

F3 *Fair credit quality*. The capacity for timely payment of financial commitments is adequate; however, near-term adverse changes could result in a reduction to non-investment grade.

B *Speculative*. Minimal capacity for timely payment of financial commitments, plus vulnerability to near-term adverse changes in financial and economic conditions.

C *High default risk*. Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon a sustained, favourable business and economic environment.

D *Default.* Denotes actual or imminent payment default. “+” or “-“may be appended to a rating to denote relative status within major rating categories. Such suffixes are not added to the 'AAA' long-term rating category, to categories below 'CCC', or to short-term ratings other than 'Fl'.

International Long-Term Credit Ratings Investment Grade

AAA *Highest credit quality*. 'AAA' ratings denote the lowest expectation of credit risk. They are assigned only in case of exceptionally strong capacity for timely payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.

AA *Very high credit quality*. 'AA' ratings denote a very low expectation of credit risk. They indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.

A *High credit quality*. 'A' ratings denote a low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to changes in circumstances or in economic conditions than is the case for higher ratings.

BBB *Good credit quality*. 'BBB' ratings indicate that there is currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity. This is the lowest investment-grade category.

Speculative Grade

BB *Speculative*. 'BB' ratings indicate that there is a possibility of credit risk developing, particularly as the result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met. Securities rated in this category are not investment grade.

B *Highly speculative*. 'B' ratings indicate that significant credit risk is present, but a limited margin of safety remains. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favourable business and economic environment.

CCC, CC *High default risk*. Default is a real possibility. Capacity for meeting and C financial commitments is solely reliant upon sustained, favourable business or economic developments. A 'CC' rating indicates that default of some kind appears probable. 'C' ratings signal imminent default.

DDD, DD *Default*. The ratings of obligations in this category are based on and D their prospects for achieving partial or full recovery in a reorganisation or liquidation of the obligor. 'DDD' designates the highest potential for recovery of amounts outstanding on any securities involved. 'DD' indicates expected recovery of 50% **-** 90% of such out standings, and 'D' the lowest recovery potential, i.e. below 50%.

Individual Ratings

Fitch's Individual Ratings attempt to assess how a bank would be viewed if it were entirely independent and could not rely on external support. These ratings are designed to assess a bank's exposure to, appetite for, and management of risk and thus represents Fitch's view on the likelihood that it would run into significant difficulties such that it would require support.

A A very strong bank. Characteristics may include outstanding profitability and balance sheet integrity, franchise, management, operating environment, or prospects.

B A strong bank. There are no major concerns regarding the bank. Characteristics may include strong profitability and balance sheet integrity, franchise, management, operating environment or prospects.

C An adequate bank which, however, possesses one or more troublesome aspects. There may be some concerns regarding its profitability and balance sheet integrity, franchise, management, operating environment or prospects.

D A bank which has weaknesses of internal and/or external origin. There are concerns regarding its profitability and balance sheet integrity, franchise, management, operating environment or prospects .

E A bank with very serious problems which either requires or is likely to require external support.
Note: In addition, FITCH uses gradations among these five ratings, i.e AIB, BIC, CID, and DIE.

Support Ratings

Support/Legal Ratings do not assess the quality of a bank. Rather, they are Fitch's assessment of whether it would receive support in the event of difficulties. Fitch emphasises that these ratings constitute their opinions alone - although they may discuss the principles underlying them with the supervisory authorities, the ratings given to banks are Fitch's own and are not submitted to the authorities for their comment or endorsement.

1 A bank for which there is an extremely high probability of external support. The potential provider of support is very highly rated in its own right and has a very high propensity to support the bank in question. This probability of support indicates a minimum Long-term rating floor of 'A-'.

2 A bank for which there is a high probability of external support. The potential provider of support is highly rated in its own right and has a high propensity to provide support to the bank in question. This probability of support indicates a minimum Long-term rating floor of 'BBB-'.

3 A bank for which there is a moderate probability of support because of uncertainties about the ability or propensity of the potential provider of support to do so. This probability of support indicates a minimum Long-term rating floor of 'BB-'.

4 A bank for which there is a limited probability of support because of significant uncertainties about the ability or propensity of any possible provider of support to do so. This probability of support indicates a minimum Long-term rating floor of 'B'.

5 A bank for which external support, although possible, cannot be relied upon. This may be due to a lack of propensity to provide support or to very weak financial ability to do so. This probability of support indicates a Long-term rating floor no higher than 'B-' and in many cases no floor at all.

It must be emphasised that in the Support rating Fitch is not analysing how "good" or "bad" a bank is, but merely whether in Fitch’s opinion it would receive support if it ran into difficulties.

Appendix A

Treasury Management Governance Framework

FULL COUNCIL	EXECUTIVE BOARD	CORPORATE GOVERNANCE & AUDIT COMMITTEE	RESOURCES AND COUNCIL SERVICES SCRUTINY BOARD
Setting Borrowing limits	Treasury Management Strategy	Adequacy of Treasury Management policies and practices	Review / scrutinise any aspects of the Treasury management function
Changes to borrowing limits	Monitoring reports in year	Compliance with statutory guidance	
Treasury Management Policy	Performance of the treasury function		

↓DELEGATIONS TO OFFICERS

DELEGATION SCHEME	TO WHOM	FUNCTION DELEGATED
Officer delegation scheme (Executive Functions)	Chief Officer Financial Services	Making arrangements for the proper administration of the authority’s financial affairs
Executive Functions Specific Delegations Page 24 (d) Treasury Management	To Chief Officer Financial Services	The provision of financial services, including treasury management (encompassing the making of payments and borrowing of loans)
Miscellaneous Functions - Financial Regulation 20: Treasury Management Page 32	Function delegated to Chief Officer (Financial Services)	To ensure that all investment and borrowing is valid, accurate, efficient, properly accounted for and in accordance with statutory and corporate requirements

↓OPERATIONAL AUTHORITY OF OFFICERS/CONTROL FRAMEWORK

POLICY DOCUMENT	TO WHOM	OPERATIONAL AUTHORITY
Treasury Management Policy Statement (section 11) Policy on Delegation and Review Requirements and Reporting Arrangements	Chief Off. Financial Services Head of Finance - Technical Senior Treasury Manager Assistant Finance Manager	Implementation of decisions taken at Treasury strategy review meetings and day to day management of treasury operations
CIPFA: Code of Practice Prudential Code Guidance Notes	Head of Finance - Technical Senior Treasury Manager Assistant Finance Manager	Ensure compliance and that any changes are reflected in the operating framework.

POLICY DOCUMENT
TO WHOM
OPERATIONAL AUTHORITY
Treasury Management Policy Statement (section 11) Policy on Delegation and Review Requirements and Reporting Arrangements
Chief Off. Financial Services
Head of Finance - Technical
Senior Treasury Manager
Assistant Finance Manager
Implementation of decisions taken at Treasury strategy review meetings and day to day management of treasury operations
CIPFA:
Code of Practice
Prudential Code
Guidance Notes
Head of Finance - Technical
Senior Treasury Manager
Assistant Finance Manager
Ensure compliance and that any changes are reflected in the operating framework.