CABINET

9 FEBRUARY 2016

TREASURY MANAGEMENT STRATEGY 2016/2017

Portfolio Holder: Councillor Alan Jarrett, Leader

Report from: Phil Watts, Chief Finance Officer

Author: Jonathan Lloyd, Principal Technical Accountant

Summary

This report presents the Council's Treasury Management Strategy for the 2016/2017 financial year. The Treasury Management Strategy incorporates within it the Treasury Management Policy Statement, Annual Investment Strategy and Minimum Revenue Provision Policy. The Cabinet is requested to consider a change to the Minimum Revenue Provision Policy for 2015/16 and beyond (see section 14).

1. Budget and Policy Framework

1.1 Audit Committee is responsible for the scrutiny of the Council's Treasury Management, Investment Strategy and Minimum Revenue Provision Policy Statement. The Constitution also specifies the role of Cabinet in implementing and monitoring treasury management policies and practices.

1.2 Cabinet is asked to consider the report, taking into account the comments from the Audit Committee. Final approval of the policy and the setting of prudential indicators is a matter for Council on 25 February 2016.

2. Background

2.1 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.

2.2 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.

2.3 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. "

2.4 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised November 2011) was adopted by this Council on 24 January 2013.

2.5 The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities
- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives
- Receipt by the full Council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year
- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices, this has been delegated to Cabinet and for the execution and administration of treasury management decisions has been delegated to the Chief Finance Officer
- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body, this has been delegated to the Audit Committee.

2.6 The suggested strategy for 2016/17 in respect of the following aspects of the treasury management function is based upon the treasury officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury adviser, Capita Asset Services.

2.7 In exercising the delegations to fulfil the responsibilities set out in the Treasury Management Strategy the Council will establish a set of standards to govern the manner in which these responsibilities are exercised. These standards are referred to as the Treasury Management Practice statements and are supported by the requisite Schedules that flow from the exercise of those Practices. These documents were approved by Cabinet on 10 February 2015, and have been updated to reflect the amendment to Treasury practices flowing from this report as well as external sources. All amendments to the practices are shown in Appendix 8 to this report.

2.8 Specifically the elements that are changing are:

- Approved Countries
- Treasury and Prudential Indicators.
- The Authorised Limit and Operational Boundary for 2012/13
- MRP Policy
- Reassignment of officer duties reflecting current departmental structure
- Removal of references to the use of external fund manager Investec

2.9 The strategy for 2016/17 covers:

- Capital plans and the prudential indicators
- The MRP strategy
- The current treasury position
- Treasury indicators which will limit the treasury risk and activities of the Council
- Prospects for interest rates
- The borrowing strategy
- Policy on borrowing in advance of need
- Debt rescheduling
- The investment strategy
- Creditworthiness policy
- Policy on use of external service providers.

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

3. The Prudential and Treasury Indicators 2016/17 – 2018/19

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

3.2 Capital prudential indicators are summarised within Appendix 3. 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. Due to uncertainties over future funding the Capital expenditure only encapsulates the Capital programme currently approved supplemented by the Council's expectations in relation to grant. It is likely that these indicators will evolve as the budget setting process progresses.

3.3 It is a statutory duty for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the "Affordable Borrowing Limit". In England and Wales the authorised Limit represents the legislative borrowing limit.

3.4 The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax and council rent levels is ‘acceptable’.

3.5 Whilst termed an “Affordable Borrowing Limit”, the capital plans to be considered for inclusion incorporate financing by both external borrowing and other forms of liability, such as credit arrangements. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years; details of the Authorised Limit can be found in Appendix 3 of this report.

3.6 The Authorised Limit and Operational Boundary for external borrowing within Appendix 3 differentiate between external borrowing and “other long term liabilities”. Other long term liabilities are other methods the authority has used to finance capital expenditure. One of the implications of the introduction of IFRS was that embedded leases should be recognised within the statement of accounts. Embedded leases are where we pay for the lease of equipment by our contractors, for example refuse collection, as these are now included within the accounts we also need to include these into both the Operational Boundary and Authorised limit. Currently our embedded leases account for £829,000. We have therefore increased the Operational Boundary for other long term liabilities by £1,000,000 and £1,100,000 for Authorised Limit in 2016/17 as well as 2017/18 and 2018/19

3.7 The Prudential and Treasury indicators are set out in Appendix 3 to this report and are relevant for the purposes of setting an integrated strategy. It is noted that since the indicators were submitted to the Audit Committee on 12 January 2016 a number of typographical errors have been identified relating to the authorised limit and operational boundary for external debt. These have been corrected in Appendix 3 to this report.

4. Treasury Management Strategy

4.1 The capital expenditure plans set out in the prudential indicators, Appendix 3, 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. These are covered in detail in paragraphs 5 to 11.

5. Borrowing requirement

5.1 No borrowing is envisaged for the foreseeable future because of the relative position of investment returns and rates for new borrowing.

6 Prospects for Interest Rates

6.1 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 2 draws together a number of current City forecasts for short term (Bank Rate) and longer fixed interest rates. The following table gives Capita Asset Services' central view.

Annual Average %	Bank Rate		PWLB Borrowing Rates (including certainty rate adjustment)		
		5 year	10 year	25 year	50 year
	%	%	%	%	%
Dec 2015	0.50	2.30	2.90	3.60	3.50
March 2016	0.50	2.40	3.00	3.70	3.60
June 2016	0.75	2.60	3.10	3.80	3.70
Sept 2016	0.75	2.70	3.20	3.90	3.80
Dec 2016	1.00	2.80	3.30	4.00	3.90
March 2017	1.00	2.80	3.40	4.10	4.00
June 2017	1.25	2.90	3.50	4.10	4.00
Sept 2017	1.50	3.00	3.60	4.20	4.10
Dec 2017	1.50	3.20	3.70	4.30	4.20
March 2018	1.75	3.30	3.80	4.30	4.20
June 2018	1.75	3.40	3.90	4.40	4.30
Sept 2018	2.00	3.50	4.00	4.40	4.30
Dec 2018	2.00	3.50	4.10	4.40	4.30
March 2019	2.00	3.60	4.10	4.50	4.40

6.2. **UK.** UK GDP growth rates in 2013 of 2.2% and 2.9% in 2014 were the strongest growth rates of any G7 country; the 2014 growth rate was also the strongest UK rate since 2006 and the 2015 growth rate is likely to be a leading rate in the G7 again, probably being second to the US. However, quarter 1 of 2015 was weak at +0.4% (+2.9% y/y) though there was a rebound in quarter 2 to +0.7% (+2.4% y/y) before weakening again to +0.5% (2.3% y/y) in quarter 3. The November Bank of England Inflation Report included a forecast for growth to remain around 2.5 – 2.7% 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 this year. Investment expenditure is also expected to support growth. However, since the August Inflation report was issued, worldwide economic statistics have distinctly weakened and the November Inflation Report flagged up particular concerns for the potential impact on the UK.

6.3 The Inflation Report was 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. However, once the falls in oil, gas and food prices over recent months fall out of the 12 month calculation of CPI, there will be a sharp tick up from the current zero rate to around 1 percent in the second half of 2016. The increase in the forecast for inflation at the three year horizon was the biggest in a decade and at the two year horizon was the biggest since February 2013. There is considerable uncertainty around how quickly 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.

6.4 **USA.** The American economy made a strong comeback after a weak first quarter's growth at +0.6% (annualised), to grow by no less than 3.9% in quarter 2 of 2015, but then weakened again to 1.5% in quarter 3. The downbeat news in late August and in September about Chinese and Japanese growth and the knock on impact on emerging countries that are major suppliers of commodities, was cited as the main reason for the Fed's decision at its September meeting to pull back from a first rate increase. However, the nonfarm payrolls figure for growth in employment in October was very strong and, together with a likely perception by the Fed. that concerns on the international scene have subsided, has supported the 0.25% rate rise in December.

6.5 **EZ.** In the Eurozone, the ECB fired its big bazooka in January 2015 in unleashing a massive €1.1 trillion programme of quantitative easing to buy up high credit quality government and other debt of selected EZ countries. This programme of €60bn of monthly purchases started in March 2015 and it is intended to run initially to September 2016. This appears to have had a positive effect in helping a recovery in consumer and business confidence and a start to a significant improvement in economic growth. GDP growth rose to 0.5% in quarter 1 2015 (1.0% y/y) but came in at +0.4% (+1.5% y/y) in quarter 2 and looks as if it may maintain this pace in quarter 3. However, the recent downbeat Chinese and Japanese news has raised questions as to whether the ECB will need to boost its QE programme if it is to succeed in significantly improving growth in the EZ and getting inflation up from the current level of around zero to its target of 2%.

6.6 **Greece**. During July, Greece finally capitulated to EU demands to implement a major programme of austerity and is now cooperating fully with EU demands. An €86bn third bailout package has since been agreed though it did nothing to address the unsupportable size of total debt compared to GDP. However, huge damage has been done to the Greek banking system and economy by the resistance of the Syriza Government, elected in January, to EU demands. The surprise general election in September gave the Syriza government a mandate to stay in power to implement austerity measures. However, there are major doubts as to whether the size of cuts and degree of reforms required can be fully implemented and so Greek exit from the euro may only have been delayed by this latest bailout.

- Investment returns are likely to remain relatively low during 2016/17 and beyond;
- Borrowing interest rates have been highly volatile during 2015 as alternating bouts of good and bad news have promoted optimism, and then pessimism, in financial markets. Gilt yields have continued to remain at historically phenomenally low levels during 2015. The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in later times, when authorities will not be able to

avoid new borrowing to finance new capital expenditure and/or to refinance maturing debt;

- There will remain 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.

7. Borrowing Strategy

7.1 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. Cash balances derived from reserves, balances and cash flow have been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is relatively high.

7.2 Against this background and the risks within the economic forecast, caution will be adopted with the 2016/17 treasury operations. The Chief Finance 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 borrowings 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.

8 Current Portfolio Position

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

	2015/2016	**2016/2017**	**2017/18**	**2018/19**
	Estimate	**Estimate**	**Estimate**	**Estimate**
	£'000	£'000	£'000	£'000
External debt				
Debt at 1 April	164,766	164,678	164,590	164,590
Other long-term liabilities (OLTL) at 1 April	829	541	265	0
Expected change in Debt	(88)	(88)	0	0
Expected change in OLTL	(288)	(276)	(265)	(0)
Actual gross debt at 31 March	165,219	164,855	164,590	164,590
The Capital Financing Requirement	237,260	234,356	231,110	227,921
Under borrowing	72,041	69,501	66,520	63,331

8.2 The general aim of this treasury management strategy is to continue to reduce the gross debt levels of the authority as and when it is prudent and economically viable to do so, due to the relationship between borrowing and investment interest rates and in order to reduce the credit risk incurred by holding investments. This policy has already been applied for a number of years resulting in a substantial reduction in credit risk and revenue interest costs.

8.3 2016/17 is expected to see only a modest rise from the historically very low Bank Rate and supports the continued strategy to resist borrowing and reduce cash balances as over the next three years, investment rates are expected to be below long-term borrowing rates. Value for money considerations would indicate that best value is obtained by avoiding new external borrowing and by using internal cash balances to finance new capital expenditure or to replace maturing external debt (this is referred to as internal borrowing). This would maximise short-term savings.

8.4 However, short term savings by avoiding new long-term external borrowing must also be weighed against the potential for incurring additional long term extra costs by delaying unavoidable new external borrowing until later years when PWLB long term rates are forecast to be significantly higher.

8.5 The Council has examined the potential for undertaking early repayment of some external debt to the PWLB in order to reduce size of the external debt position. However, large premiums would be incurred by such action and make this course of action unattractive in the short term. This situation will be monitored in case the position changes.

8.6 Against this background caution will be adopted with the 2016/17 treasury operations. The Chief Finance Officer will monitor the interest rate market and adopt a pragmatic approach to changing circumstances with decisions reported within the reviews of this strategy.

8.7 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.

8.8 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 budget report.

9. Policy on Borrowing in Advance of Need

9.1 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.

9.2 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.

10. Debt Rescheduling

10.1 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).

10.2 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).

10.3 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.

10.4 Decisions related to rescheduling will similarly be reported in reviews of this strategy.

11. Annual Investment Strategy

11.1 Investment Policy

11.1.1 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, then the return.

11.1.2 In accordance with guidance from CLG and CIPFA, 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 Short Term and Long Term ratings.

11.1.3 Ratings should not be the sole determinant of the quality of an institution and that 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. This is fully integrated into, the credit methodology provided by the advisors, Capita Asset Services in producing its colour codings which show the varying degrees of suggested creditworthiness.

11.1.4 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.

11.1.5 The aim of the strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoidance of concentration risk.

11.1.6 Investment instruments identified for use in the financial year are listed in Appendix 5 under the 'Specified' and 'Non-Specified' Investments categories. Counterparty limits will be as set through the Council's Treasury Management Practices – Schedules.

11.2 Creditworthiness policy

11.2.1 This 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, Moodys 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.

11.2.2 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 which 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
- Purple - 2 years
- Blue - 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange - 1 year
- Red - 6 months
- Green – 100 days
- No Colour - not to be used

11.2.3 The Capita Asset Services creditworthiness service uses a wider array of information than just primary. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

11.2.4 Typically the minimum credit ratings criteria the Council use will be a short term rating (Fitch or equivalents) of F1, a Long Term rating 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.

11.2.5 All credit ratings will be monitored primarily via Capita Asset Services updates by Officers on a continuous basis. The Council is alerted to changes to ratings of all three agencies through its use of the Capita Asset Services creditworthiness service.

- 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.

- In addition to the use of credit ratings the Council will be advised of information in movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly 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.

11.2.6 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, information on any external support for banks to help support its decision making process.

11.3 Counterparty Limits

11.3.1 The current counterparty limits are set as;

- in-house team £20 million limit per counterparty and £25 million for counterparties with a Capita Asset Services duration rating of 12 months or above.

11.3.2 No amendments are requested to these counterparty limits.

11.4 Country limits

11.4.1 The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch (or equivalent). The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 6. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

11.4.2 In addition

- no more than £40m will be placed with any non-UK country at any time;
- limits in place will apply to a group of companies;
- sector limits will be monitored regularly for appropriateness.

11.5 Investment Strategy

11.5.1 In-house funds. 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).

11.5.2 Investment returns expectations. Bank Rate is forecast to remain unchanged at 0.5% before starting to rise from quarter 2 of 2016. Bank Rate forecasts for financial year ends (March) are:

- 2016/17 1.00%
- 2017/18 1.75%
- 2018/19 2.00%

11.5.3 The suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during each financial year for the next eight years are as follows:

2016/17	0.90%
2017/18	1.50%
2018/19	2.00%
2019/20	2.25%
2020/21	2.50%
2021/22	3.00%
2022/23	3.00%
Later years	3.00%

11.5.4 The overall balance of risks to these forecasts is currently to the downside (i.e start of the increase 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.

11.6 Investment in Property Funds

11.6.1 Property Funds are a form of investment, comprising a portfolio of commercial properties to achieve investment returns through rental income and capital growth. However, the value of such investments may fall as well as rise. There may also be restrictions on redemption of the investment. This type of investment is regarded as a 5 to 7 year minimum timeframe.

11.6.2 Such investments would ordinarily be deemed capital expenditure, and as such would need to be accounted for as part of the capital programme, rather than through the interest and financing budget, however the Local Authorities Investment Fund is a scheme approved by HM Treasury under Section 11 of the Trustee Investments Act 1961 and is managed as an Alternative Investment Fund (AIF).

11.6.3 Such funds, comprising a strong portfolio of high quality properties with good quality, reliable tenants are generally able to provide consistent annual yields, even when capital asset values fluctuate due to market conditions. Property funds of the type approved by HM Treasury are also relatively liquid and units can be bought or sold fairly quickly to respond to significant changes in the Council's cashflow forecasts.

11.6.4 Due diligence was undertaken before the Council invested in the CCLA Property Fund and the CFO would carefully consider the Council's cash balances and cashflow projections before investing further amounts. Members are asked to note the inclusion of Property Funds on the list of non-specified investments.

11.7 End of year investment report

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

11.8 Breach of Treasury Management Practice Re Bank Overdraft

11.8.1 The treasury management practice on treasury risk management regarding liquidity risk (TMP1 paragraph 1.2.1) sets out guidance that the Council should not be overdrawn by more than £300,000.

11.8.2 On 16 December 2015 Rivermead School transferred £830,000 from its maintained school account to the new academy account. The transfer was made without informing Medway Council Finance and in breach of academy transfer instruction notes issued to the school. As a result of the un-reported transfer the Council was overdrawn on that day by £682,383.

12 Policy on the use of external service providers

12.1 The Council uses Capita Asset Services as its external treasury management advisors.

12.2 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.

12.3 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.

13. Kent County Council (KCC) Local Government Reorganisation (LGR) Debt

13.1 The charge for the share of KCC debt for which Medway Council was responsible on local government reorganisation is based on the current average cost of debt for the County Council as a whole. Whilst the County rate at a projected 5.36% remains marginally higher than our own average debt rate of 4.218% for 2016/17, the penalty involved in early repayment makes early redemption an unattractive option. The outstanding principal at 1 April 2016 will be £38.5 million.

Current and Historical Rates of Interest Charged on KCC LGR debt

Year	2009/10	2010/11	2011/12	2012/13	2013/14 Actual	2014/15 Actual	2015/16 Estimate
Rate	5.08%	5.21%	5.30%	5.44%	5.51%	5.50%	5.36%

14 Minimum Revenue Provision (MRP)

14.1 The Minimum Revenue Provision is explained and the Policy Statement for 2016/17 is set out at Appendix 1. The policy is a change from that adopted in the 2015/16 Policy Statement and Members are requested to approve adoption of the new policy for application in 2015/16 as well as for future years.

14.2 Prior to 2007/08 the basis of calculating MRP was specified in legislation. From 2007/08 under the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [SI 2008/414] the statutory minimum was removed. Councils were simply required to make prudent provision and have regard to statutory guidance.

14.3 The method adopted for providing for the element of general fund debt relating to pre 2008 expenditure was to provide for 4% of the outstanding debt after disregarding a smoothing factor (known as Adjustment A) on a reducing balance basis. Under this method, no provision was made for the amount represented by the Adjustment A factor and the operation of the reducing balance method produced a long tail of provision.

14.4 The same methodology was applied to any post 2008 general fund externally financed borrowing.

14.5 General fund financing from internal borrowing (use of cash balances to finance capital expenditure) has been provided on a straight line basis over the life of the relevant assets created or enhanced.

14.6 There is no requirement to provide MRP in respect of Housing Revenue Account (HRA) borrowing, however this has up to now been provided at 2% of the HRA Capital Financing Requirement (CFR).

14.7 It proposed that with effect from 20015/16 the council disregards Adjustment A and provides MRP on the basis of the total capital financing requirement. Furthermore the basis of provision should be based on the estimated remaining lives of the underlying assets.

14.8 It is recommended that an annuity method of allocating amounts of MRP to each year of asset life be adopted from 2015/16. This would work in a similar way to a repayment mortgage where the principal repaid in the early years is small but grows proportionally towards the end of the repayment period. Similarly the amount of MRP under this proposal would start with a small level of provision and rise over the life of the assets.

14.9 It is estimated that adoption of the proposals in paragraphs 14.7 and 14.8 would save the revenue account around £2.7m in the 2016/17 financial year. Furthermore preliminary discussions with the Council’s external auditor BDO have indicated that this approach is likely to be acceptable.

15. Audit Committee

15.1 The Audit Committee considered this report and appendices on 12 January 2016.

15.2 Members discussed the proposal to revise the Minimum Revenue Provision (MRP) Policy by changing to an annuity method of allocating amounts of MRP to each year of asset life. This would result in revenue savings of around £2.7m in 2016/17. The majority of the Council's debts matured in 50-60 years time and the proposed change would mean lower provision being set aside in early years which would increase modestly over the life of the debts. Some Members felt there was insufficient information about the consequences of this in the future to decide whether it was a reasonable and prudent approach. It was argued that the savings that would be released now were not in itself a strong enough argument for change. The Chief Finance Officer offered to provide information showing the annual revenue provision over a 40 year period as a result of the proposal compared to the existing system. A Member asked whether the annual increase in the MRP could be justified by inflation. The Chief Finance Officer explained that whilst the annuity calculation had little to do with inflation the year on year effect in cash terms was broadly similar.

15.3 It was proposed that the report be noted and further information be provided regarding the proposed changes to the Minimum Revenue Provision Policy to demonstrate the prudency of the approach. This proposal was put to the vote and lost. It was then proposed that the Committee should recommend approval of the changes to the MRP and this was agreed.

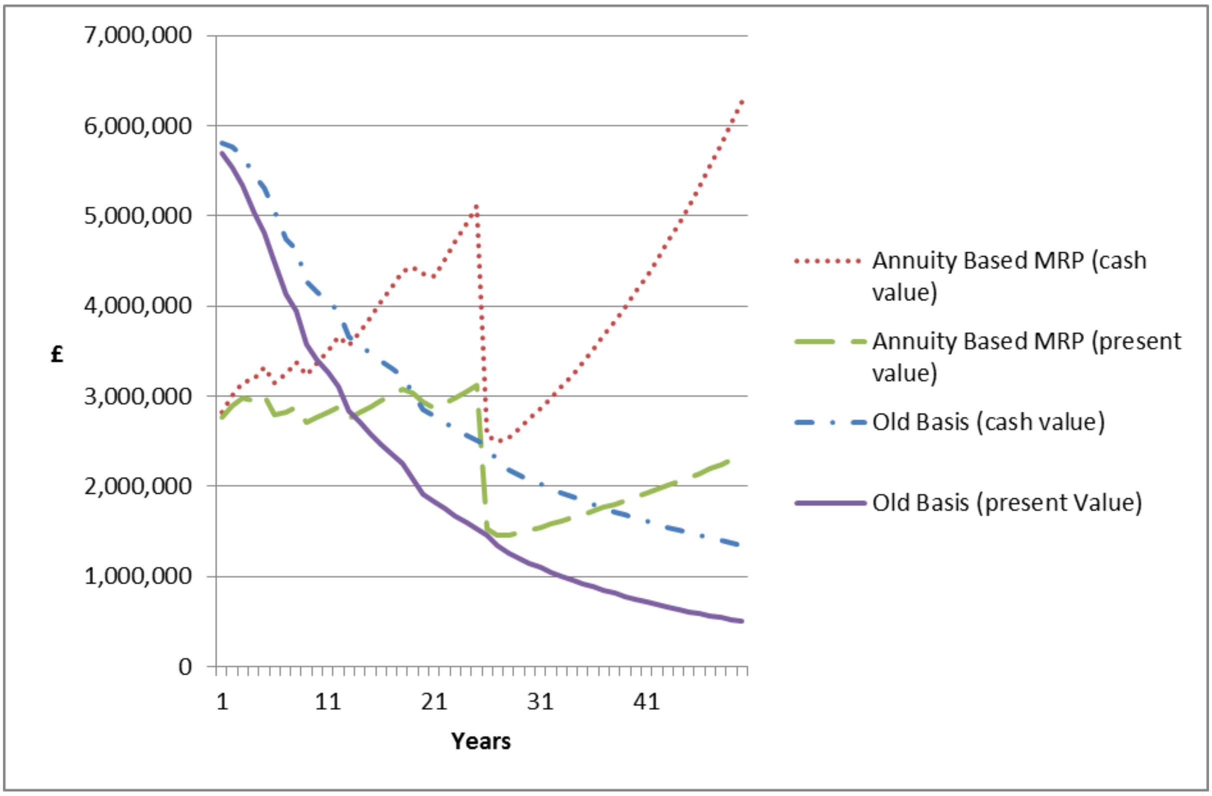
15.4 The Committee agreed to:
- (a) note the contents of the report;
- (b) recommend approval of the proposed changes in the Minimum Revenue Provision Policy, to take effect from the 2015/16 financial year onwards; and
- (c) ask for further information to be provided showing annual revenue provision over 40 years as per the proposals compared to the existing Minimum Revenue Provision policy.

Note – in accordance with Council Procedure Rule 12.6 of Chapter 4 of the Council's Constitution, Councillors Griffiths and Maple asked that it be recorded that they had voted for the proposal to note the report and that further information be provided regarding the proposed changes to the Minimum Revenue Provision Policy to demonstrate the prudency of the approach.

Chief Finance Officer's comments regarding Members' request for further information comparing old and proposed methods of calculating Minimum Revenue Provision (MRP)

15.5 The graph blow compares the estimated annual amount of MRP over the next 50 years using the existing (reducing balance) and the proposed (annuity based) methodologies. For each method both cash and inflation adjusted (present value) amounts are plotted.

15.6 Whether using the cash or the inflation adjusted basis the amounts to be provided under the proposed annuity method are lower than under the existing method for at least the next 13 years. Furthermore, throughout the 50 year period, the inflation adjusted annuity amounts do not exceed significantly the amount proposed for the current year.



16. Risk management

16.1 Risk and the management thereof is a feature throughout the strategy and in detail within the Treasury Management Practices 1.

17. Diversity Impact Assessment

17.1 The Treasury Management Strategy does not directly impact on members of the public as it deals with 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. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group.

18. Financial and legal implications

18.1 The finance and legal positions are set out throughout the main body of the report.

19. Recommendations

19.1 The Cabinet is asked to consider the comments of the Audit Committee.

19.2 The Cabinet is asked to recommend to Full Council approval of the proposed changes in the Minimum Revenue Provision Policy (Appendix 1 to the report), to take effect from the 2015/16 financial year onwards

19.3 Cabinet is asked to recommend to Full Council the Treasury Management Strategy as set out in the report and Appendices 1-6 to the report.

19.4 Cabinet is asked to approve the amendments to the Treasury Management Practices as set out in Appendix 8 to the report.

20. Suggested Reasons for Decisions

20.1 Cabinet has the responsibility to make recommendations to Full Council on the approval of the Council's Treasury Management, Investment Strategy and Minimum Revenue Provision Policy Statement and has responsibility for the implementation of the Treasury Management Practices and associated schedules.

Appendices

1. Minimum Revenue Provision Policy Statement
2. Interest rate forecasts
3. Prudential and Treasury indicators
4. Economic background
5. Specified and non specified investments
6. Approved countries for investments
7. Diversity Impact Assessment Screening Form
8. Amendments to Treasury Management Practices

Background Papers:

None

Lead officer contact
Jonathan Lloyd, Principal Technical Accountant
Telephone No: 01634 332787 Email: jonathan.lloyd@medway.gov.uk

APPENDIX 1

Minimum Revenue Provision Policy Statement 2015/16 and 2016/17

The Council implemented the new Minimum Revenue Provision (MRP) guidance in 2007/2008, and assessed MRP for 2007/2008 onwards in accordance with the main recommendations contained within the guidance issued by the Secretary of State under section 21(1A) of the Local Government Act 2003.

In setting the Minimum Revenue Provision Policy, Medway Council has regard to the guidance and will set a policy to ensure a prudent provision for the repayment of debt.

From 2015/16 MRP will be based on the estimated lives of assets funded from debt.

The Council will treat all expenditures as not ranking for MRP until the year after the scheme or asset to which they relate is completed and/or brought into use

Estimated life periods will be determined under delegated powers. To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the guidance, these periods will generally be adopted by the Council. However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate.

As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

In the case of long term debtors arising from loans or other types of capital expenditure made by the Council which will be repaid under separate arrangements (such as long term investments), or where borrowing has occurred but will be repaid by future Capital Receipts or agreed income from other source, there will be no Minimum Revenue Provision made.

There is no requirement on the HRA to make a minimum revenue provision

APPENDIX 2

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%	-	-	-	-	-

APPENDIX 3

Prudential and Treasury Indicators

PRUDENTIAL INDICATORS	2016/2017	2017/2018	2018/2019
Extract from budget and rent setting report	**estimate**	**estimate**	**Estimate**
	£'000	**£'000**	**£'000**
Capital Expenditure			
Non - HRA	23,716	21,139	8,405
HRA	7,439	4,903	4,699
TOTAL	31,155	26,042	13,104
Ratio of financing costs to net revenue stream			
Non - HRA	2.35%	2.38%	2.54%
HRA	17.24%	18.45%	19.00%
Gross borrowing requirement			
brought forward 1 April	164,766	164,678	164,590
carried forward 31 March	164,678	164,590	164,590
in year borrowing requirement	(87)	(88)	0
Capital Financing Requirement as at 31 March			
Non – HRA	189,583	187,330	185,016
HRA	44,673	43,780	42,904
TOTAL	234,256	231,110	227,920
Annual change in Cap. Financing Requirement			
Non – HRA	(9,901)	(2253)	(2314)
HRA	2143	(893)	(876)
TOTAL	(7,758)	(3,146)	(3,190)
Incremental impact of capital investment decisions	**£ p**	**£ p**	**£ p**
Increase in council tax (band D) per annum	(26.07)	0.60	1.18
Increase in average housing rent per week	0.18	0.89	0.35

TREASURY MANAGEMENT INDICATORS	2016/2017	2017/2018	2018/2019
	Estimate	Estimate	Estimate
	£'000	£'000	£'000
Authorised Limit for external debt -			
Borrowing	408,296	402,111	389,143
other long term liabilities	1,100	1,100	1,100
TOTAL	409,396	403,311	399,243
Operational Boundary for external debt -			
Borrowing	371,178	365,555	361,948
other long term liabilities	1,000	1,000	1,000
TOTAL	372,178	366,555	362,948
Actual external debt	164,678	164,590	164,590
HRA Maximum CFR Debt Limit	45,846	45,846	45,846
Upper limit for fixed interest rate exposure			
Net principal re fixed rate borrowing / investments	100%	100%	100%
Upper limit for variable rate exposure			
Net principal re variable rate borrowing / investments	40%	40%	40%
Upper limit for total principal sums invested for over 364 days (per maturity date)	£150,000	£150,000	£150,000

TABLE 5: Maturity structure of fixed rate borrowing during 2016/2017	upper limit	lower limit
under 12 months	50%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	50%	0%
10 years and above	100%	0%

Appendix 4

Economic Background

UK. UK GDP growth rates in of 2.2% in 2013 and 2.9% in 2014 were the strongest growth rates of any G7 country; the 2014 growth rate was also the strongest UK rate since 2006 and the 2015 growth rate is likely to be a leading rate in the G7 again. However, quarter 1 of 2015 was weak at +0.4%, although there was a short lived rebound in quarter 2 to +0.7% before it subsided again to +0.5% (+2.3% y/y) in quarter 3. The Bank of England’s November Inflation Report included a forecast for growth to remain around 2.5% – 2.7% over the next three years. For this recovery, however, to become more balanced and sustainable in the longer term, it still needs to move away from dependence on consumer expenditure and the housing market to manufacturing and investment expenditure. The strong growth since 2012 has resulted in unemployment falling quickly to a current level of 5.3%.

The MPC has been particularly concerned that the squeeze on the disposable incomes of consumers should be reversed by wage inflation rising back above the level of CPI inflation in order to underpin a sustainable recovery. It has, therefore, been encouraging in 2015 to see wage inflation rising significantly above CPI inflation which has been around zero since February. The Inflation Report was notably subdued in respect of the forecasts for CPI inflation; this was expected to barely get back up to the 2% target within the 2-3 year time horizon. However, once the falls in oil, gas and food prices over recent months fall out of the 12 month calculation of CPI, there will be a sharp tick up from the current zero rate to around 1% in the second half of 2016. Indeed, the increase in the forecast for inflation at the three year horizon was the biggest in a decade and at the two year horizon it was the biggest since February 2013. Nevertheless, despite average weekly earnings ticking up to 3.0% y/y in the three months ending in September, this is unlikely to provide ammunition for the MPC to take action to raise Bank Rate in the near future as labour productivity growth has meant that net labour unit costs appear to be rising by about only 1% y/y. Having said that, at the start of October, data came out that indicated annual labour cost growth had jumped sharply in quarter 2 from +0.3% to +2.2%: time will tell if this is just a blip or the start of a trend.

There is, therefore, considerable uncertainty around how quickly 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. There are also concerns around the fact that the central banks of the UK and US currently have few monetary policy options left to them given that central rates are near to zero and huge QE is already in place. There are, therefore, arguments that they need to raise rates sooner, rather than later, so as to have some options available for use if there was another major financial crisis in the near future. But it is unlikely that either would raise rates until they are sure that growth was securely embedded and ‘noflation’ was not a significant threat.

The forecast for the first increase in Bank Rate has, therefore, been pushed back progressively during 2015 from Q4 2015 to Q2 2016 and increases after that will be at a much slower pace, and to much lower levels than prevailed before 2008, as increases in Bank Rate will have a much bigger effect on heavily indebted consumers than they did before 2008.

The Government's revised Budget in July eased the pace of cut backs from achieving a budget surplus in 2018/19 to achieving that in 2019/20.

USA. GDP growth in 2014 of 2.4% was followed by Q1 2015 growth, which was depressed by exceptionally bad winter weather, at only +0.6% (annualised). However, growth rebounded very strongly in Q2 to 3.9% (annualised) before dipping again in Q3 to 1.5%.

Until the turmoil in financial markets in August, caused by fears about the slowdown in Chinese growth, it had been strongly expected that the Fed. may start to increase rates in September. However, the Fed pulled back from that first increase due to global risks which might depress US growth and put downward pressure on inflation, as well as a 20% appreciation of the dollar which has caused the Fed. to lower its growth forecasts. Although the non-farm payrolls figures for growth in employment in August and September were disappointingly weak, the October figure was stunningly strong and, underpinned the first increase (0.25%) in the Fed's funding rate for almost a decade.

Eurozone. The ECB fired its big bazooka in January 2015 in unleashing a massive €1.1 trillion programme of quantitative easing to buy up high credit quality government and other debt of selected EZ countries. This programme of €60bn of monthly purchases started in March 2015 and it is intended to run initially to September 2016. This appears to have had a positive effect in helping a recovery in consumer and business confidence and a start to a significant improvement in economic growth. GDP growth rose to 0.5% in Q1 2015 (1.0% y/y) but came in at +0.4% (+1.5% y/y) in Q2 and looks as if it may maintain this pace in Q3. However, the recent downbeat Chinese and Japanese news has raised questions as to whether the ECB will need to boost its QE programme if it is to succeed in significantly improving growth in the EZ and getting inflation up from the current level of around zero to its target of 2%.

Greece. During July, Greece finally capitulated to EU demands to implement a major programme of austerity. An €86bn third bailout package has since been agreed although it did nothing to address the unsupportable size of total debt compared to GDP. However, huge damage has been done to the Greek banking system and economy by the initial resistance of the Syriza Government, elected in January, to EU demands. The surprise general election in September gave the Syriza government a mandate to stay in power to implement austerity measures. However, there are major doubts as to whether the size of cuts and degree of reforms required can be fully implemented and so a Greek exit from the euro may only have been delayed by this latest bailout.

China and Japan. Japan is causing considerable concern as the increase in sales tax in April 2014 suppressed consumer expenditure and growth. In Q2 2015 quarterly growth shrank by -0.3% after a short burst of strong growth of 1.0% during Q1. Japan has been hit hard by the downturn in China during 2015. This does not bode well for Japan as the Abe government has already fired its first two arrows to try to stimulate recovery and a rise in inflation from near zero, but has dithered about firing the third, deregulation of protected and inefficient areas of the economy.

As for China, the Government has been very active during 2015 in implementing several stimulus measures to try to ensure the economy hits the growth target of 7% for the current year and to bring some stability after the major fall in the onshore Chinese stock market during the summer. Many commentators are concerned that recent growth figures could have been massaged to hide a downturn to a lower growth figure. There are also major concerns as to the creditworthiness of much of the bank lending to corporates and local government during the post 2008 credit expansion period. Overall, China is still expected to achieve a growth figure that the EU would be envious of. Nevertheless, concerns about whether the Chinese economy could be heading for a hard landing, and the volatility of the Chinese stock market, which was the precursor to falls in world financial markets in August and September, remain a concern.

Emerging countries. There are also considerable concerns about the vulnerability of some emerging countries and their corporates which are getting caught in a perfect storm. Having borrowed massively in dollar denominated debt since the financial crisis (as investors searched for yield by channelling investment cash away from western economies with dismal growth, depressed bond yields and near zero interest rates into emerging countries) there is now a strong flow back to those western economies with strong growth and an imminent rise in interest rates and bond yields.

This change in investors' strategy, and the massive reverse cash flow, has depressed emerging country currencies and, together with a rise in expectations of a start to central interest rate increases in the US, has helped to cause the dollar to appreciate significantly. In turn, this has made it much more costly for emerging countries to service their dollar denominated debt at a time when their earnings from commodities are depressed. There are also likely to be major issues when previously borrowed debt comes to maturity and requires refinancing at much more expensive rates.

Corporates (worldwide) heavily involved in mineral extraction and / or the commodities market may also be at risk and this could also cause volatility in equities and safe haven flows to bonds. Financial markets may also be buffeted by the sovereign wealth funds of those countries that are highly exposed to falls in commodity prices and which, therefore, may have to liquidate investments in order to cover national budget deficits.

CAPITA ASSET SERVICES FORWARD VIEW

Economic forecasting remains difficult with so many external influences weighing on the UK. Our Bank Rate forecasts, (and also MPC decisions), 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 on 9 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.

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 QE. 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.

The overall balance of risks to economic recovery in the UK is currently evenly balanced. Only time will tell just how long this current period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.

However, the overall balance of risks to our Bank Rate forecast is probably to the downside, i.e. the first increase, and subsequent increases, may be delayed further if recovery in GDP growth, and forecasts for inflation increases, are lower than currently expected. Market expectations in November, (based on short sterling), for the first Bank Rate increase are currently around mid-year 2016.

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

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 and leading to a major flight from bonds 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

Specified and Non-Specified Investments

SPECIFIED INVESTMENTS:

(All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' rating criteria where applicable)

	*** Minimum 'High' Credit Criteria**	**Use**
Debt Management Agency Deposit Facility	--	In-house and Fund Manager
Term deposits – local authorities	--	In-house and Fund Manager
Term deposits – banks and building societies	See note 1	In-house and Fund Manager
Collateralised deposit (see note 3)	UK sovereign rating	In-house and Fund Manager
Certificates of deposit issued by banks and building societies	See note 1	In-house and Fund Manager
UK Government Gilts	UK sovereign rating	In-house buy and hold and Fund Manager
Bonds issued by multilateral development banks	AAA	In-house buy and hold and Fund Manager
Bond issuance issued by a financial institution which is explicitly guaranteed by the UK Government (refers solely to GEFCO - Guaranteed Export Finance Corporation)	UK sovereign rating	In-house buy and hold and Fund Manager
Sovereign bond issues (other than the UK govt)	AAA	In-house buy and hold and Fund Manager
Treasury Bills	UK sovereign rating	In house and Fund Manager
Government Liquidity Funds	* Long-term AAA volatility rating V1+	In-house and Fund Managers
Money Market Funds	* Long-term AAA volatility rating V1+	In-house and Fund Managers

Note 1. Award of "Creditworthiness" Colour by Capita Asset Services as detailed in paragraph 11.2

Accounting treatment of investments. The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

NON-SPECIFIED INVESTMENTS: These are any investments which do not meet the Specified Investment criteria. A maximum of 70% ** will be held in aggregate in non-specified investment

1. Maturities of ANY period

	*** Minimum Credit Criteria**	**Use**	**** Max % of total investments**	**Max. maturity period**
Fixed term deposits with variable rate and variable maturities: -Structured deposits	See note 1	In-house	£10m	Lower of 5 years or Sector duration rating

2. Maturities in excess of 1 year

	*** Minimum Credit Criteria**	**Use**	**** Max % of total investments**	**Max. maturity period**
Term deposits – local authorities	--	In-house	40%	5 Years
Term deposits – banks and building societies	See note 1	In-house	40%	As per Capita duration rating
Certificates of deposit issued by banks and building societies covered by UK Government (explicit) guarantee	See note 1 and 2	In-house	40%	As per Capita duration rating and see note 3
Certificates of deposit issued by banks and building societies	See note 1 and 2	In-house	40%	As per Capita duration rating and see note 3
UK Government Gilts	UK sovereign rating	In-house	40%	see note 1
Bonds issued by multilateral development banks	AAA	In-house	20%	see note 1
Sovereign bond issues (other than the UK govt)	AAA	In-house	20%	see note 1

Note 1. Award of "Creditworthiness" Colour by Sector Treasury services as detailed in paragraph 11.2

** If forward deposits are to be made, the forward period plus the deal period should not exceed one year in aggregate.
N.B. buy and hold may also include sale at a financial year end and repurchase the following day in order to accommodate the requirements of SORP.

3 Property Funds

Investment of up to an aggregate limit of £5m may be invested in collective property funds.

APPENDIX 6

Approved countries for investments – based on lowest available rating

AAA

- Australia
- Canada
- Denmark
- Germany
- ~~Luxembourg~~
- ~~Norway~~
- Singapore
- Sweden
- Switzerland

AA+

- Finland
- Netherlands
- ~~Hong Kong~~
- U.K.
- U.S.A

AA

- Abu Dhabi (UAE)
- France
- Qatar

AA-

- Belgium
- ~~Saudi Arabia~~

Appendix 7

Diversity Impact Assessment: Screening Form

<table>
<tr><td colspan="2">Directorate

BSD</td><td colspan="3">Name of Function or Policy or Major Service Change

Treasury Management Strategy</td></tr>
<tr><td colspan="3">Officer responsible for assessment

Jonathan Lloyd</td><td>Date of assessment

31/12/2015</td><td>New or existing?

Existing</td></tr>
<tr><td colspan="5">Defining what is being assessed</td></tr>
<tr><td colspan="2">1. Briefly describe the purpose and objectives</td><td colspan="3">The Treasury Management Strategy, is the strategy that the Council applies to effectively manage it’s Treasury Function. This is defined by CIPFA 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.</td></tr>
<tr><td colspan="2">2. Who is intended to benefit, and in what way?</td><td colspan="3">All stakeholders with a safe and effective Treasury Management Strategy</td></tr>
<tr><td colspan="2">3. What outcomes are wanted?</td><td colspan="3">The successful and secure 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.</td></tr>
<tr><td colspan="2">4. What factors/forces could contribute/detract from the outcomes?</td><td colspan="2"><u>Contribute</u>
Effective Strategy,
Good planning
Effective use of information and intelligence</td><td><u>Detract</u>
Resources,
Further cuts</td></tr>
<tr><td colspan="2">5. Who are the main stakeholders?</td><td colspan="3">The Chief Finance Officer, Full Council and residents</td></tr>
<tr><td colspan="2">6. Who implements this and who is responsible?</td><td colspan="3">Chief Finance Officer, and the Treasury Team</td></tr>
</table>

Assessing impact		
7. Are there concerns that there <u>could</u> be a differential impact due to *racial/ethnic groups*?	~~YES~~ NO	Brief statement of main issue
What evidence exists for this?	The Treasury Management Strategy does not directly impact on members of the public as it deals with the Treasury management functions of the authority. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group. Hence there will not be a differential impact due racial or ethnic group membership.	
8. Are there concerns that there <u>could</u> be a differential impact due to *disability*?	~~YES~~ NO	Brief statement of main issue
What evidence exists for this?	The Treasury Management Strategy does not directly impact on members of the public as it deals with the Treasury management functions of the authority. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group. Hence there will not be a differential impact due disability.	
9. Are there concerns that there <u>could</u> be a differential impact due to *gender*?	~~YES~~ NO	Brief statement of main issue
What evidence exists for this?	The Treasury Management Strategy does not directly impact on members of the public as it deals with the Treasury management functions of the authority. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group. Hence there will not be a differential impact due gender.	
10. Are there concerns there <u>could</u> be a differential impact due to *sexual orientation*?	~~YES~~ NO	Brief statement of main issue
What evidence exists for this?	The Treasury Management Strategy does not directly impact on members of the public as it deals with the Treasury management functions of the authority. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group. Hence there will not be a differential impact due sexual orientation.	
11. Are there concerns there <u>could</u> be a have a differential impact due to *religion or belief*?	~~YES~~ NO	Brief statement of main issue
What evidence exists for	The Treasury Management Strategy does not directly	

this?	impact on members of the public as it deals with the Treasury management functions of the authority. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group. Hence there will not be a differential impact due religion or belief.	
12. Are there concerns there could be a differential impact due to people's *age*?	~~YES~~ NO	Brief statement of main issue
What evidence exists for this?	The Treasury Management Strategy does not directly impact on members of the public as it deals with the Treasury management functions of the authority. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group. Hence there will not be a differential impact due to people's age.	
13. Are there concerns that there could be a differential impact due to *being trans-gendered or transsexual*?	~~YES~~ NO	Brief statement of main issue
What evidence exists for this?	The Treasury Management Strategy does not directly impact on members of the public as it deals with the Treasury management functions of the authority. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group. Hence there will not be a differential impact due an individual's gender identity.	
14. Are there any *other* groups that would find it difficult to access/make use of the function (e.g. speakers of other languages; people with caring responsibilities or dependants; those with an offending past; or people living in rural areas)?	~~YES~~ NO	If yes, which group(s)?
What evidence exists for this?	The Treasury Management Strategy does not directly impact on members of the public as it deals with the Treasury management functions of the authority. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group. Hence there will not be a differential impact.	
15. Are there concerns there could be a have a differential impact due to *multiple discriminations* (e.g. disability and age)?	~~YES~~ NO	Brief statement of main issue
What evidence exists for	The Treasury Management Strategy does not directly	

this?	impact on members of the public as it deals with the Treasury management functions of the authority. Decisions are based upon the principles highlighted within the Strategy and have no impact on any one particular group. Hence there will not be a differential impact.

Conclusions & recommendation		
16. Could the differential impacts identified in questions 7-15 amount to there being the potential for adverse impact?	~~YES~~	Brief statement of main issue
	NO	
17. Can the adverse impact be justified on the grounds of promoting equality of opportunity for one group? Or another reason?	YES	Please explain
	NO	

Recommendation to proceed to a full impact assessment?		
NO	**This function/ policy/ service change complies with the requirements of the legislation and there is evidence to show this is the case.**	
~~**NO, BUT …**~~	~~**What is required to ensure this complies with the requirements of the legislation? (see DIA Guidance Notes)?**~~	~~Minor modifications necessary (e.g. change of 'he' to 'he or she', re-analysis of way routine statistics are reported)~~
~~**YES**~~	~~***Give details of key person responsible and target date for carrying out full impact assessment (see DIA Guidance Notes)***~~	

Action plan to make Minor modifications		
Outcome	**Actions (with date of completion)**	**Officer responsible**

Planning ahead: Reminders for the next review	
Date of next review	January 2017
Areas to check at next review (e.g. new census information, new legislation due)	
Is there *another* group (e.g. new communities) that is relevant and ought to be considered next time?	

Signed (completing officer/service manager) **Jonathan Lloyd**	**Date**	31/12/2015
Signed (service manager/Assistant Director) Phil Watts	**Date**	31/12/2015

APPENDIX 8

Amendments to the Treasury Management Practices

1. Amendment to sub-section 8 of section 1.1.1 Policy on the use of credit risk analysis techniques.

8. Diversification: this organisation will avoid concentrations of lending and borrowing by adopting a policy of diversification. It will therefore use the following: -

- Maximum amount to be placed with any one institution - £25m and for those with a sector duration of less than 12 months £20m.
- Group limits where a number of institutions are under one ownership – maximum of £25m and for those with a sector duration of less than 12 months £20m.
- Country limits – a minimum sovereign rating of AA- from Fitch Ratings (or equivalent) is required for an institution to be placed on our approved lending list, with the exception of United Kingdom, where there is no restriction on the sovereign credit rating. The maximum investment in any one country is £40m with the exception of UK which is unlimited. The list of countries which currently meet this criteria is: -

AAA	**AA+**	**AA**	**AA-**
Australia		Abu Dhabi (UAE)	Belgium
Canada	~~Hong Kong~~	Qatar	
Denmark	U.S.A.	France	~~Saudi Arabia~~
Germany	Finland		
~~Luxembourg~~	Netherlands		
~~Norway~~	U.K.		
Singapore			
Sweden			
Switzerland			

2 Amendment to paragraph 14 from Funds invested with Fund Managers within section 1.1.1

- Country limits – a minimum sovereign rating of AA- from Fitch Ratings (or equivalent) is required for an institution to be placed on our approved lending list, with the exception of United Kingdom, where there is no restriction on the sovereign credit rating. The maximum investment in any one country is £40m with the exception of UK which is unlimited. The list of countries which currently meet this criteria is: -

AAA	**AA+**	**AA**	**AA-**
Australia	Finland	Abu Dhabi (UAE)	Belgium
Canada	~~Hong Kong~~	France	~~Saudi Arabia~~
Denmark	Netherlands	Qatar	
Germany	U.K.		
~~Luxembourg~~	U.S.A.		
~~Norway~~			
Singapore			
Sweden			
Switzerland			

3 Amendment to Extract from - 1.3.1 Details of approved interest rate exposure limits

the overall borrowing limit 2016-17	£409,369

4 Property funds added to list of non- specified investments in TMP1 (paragraph 1.8.2) and related records to be kept added to TMP3 (paragraph 3.1.1)

5 Reference to accounting for funds as fair value through profit and loss in TMP1 (paragraph 1.7.1) have been deleted.

6 Reference in TMP2 to the CIPFA Benchmarking club has been deleted as the Council in no longer subscribed.

7 TMP6 reference to management information reports to the Principal Accountant have been deleted.

8 TMP 5 (paragraph 5.11) reference to £10m upper limit on total payments removes as this is out of date.