APPENDIX N

TREASURY MANAGEMENT STRATEGY STATEMENT, TREASURY MANAGEMENT POLICY STATEMENT, MINIMUM REVENUE PROVISION POLICY STATEMENT AND ANNUAL INVESTMENT STATEMENT 2015/16

Purpose

To comply with the requirement of the Council's Treasury Management Policy in reporting to Council the proposed strategy for the forthcoming year and the Local Government Act 2003 with the reporting of the Prudential Indicators.

Executive Summary

The Local Government Act 2003 requires the Council to produce prudential indicators in line with the Prudential Code.

This report outlines the Council's prudential indicators for 2015/16 – 2017/18 and sets out the expected Treasury operations for this period. This report and associated tables fulfil the statutory requirement of the Local Government Act 2003 by:

- Reporting the prudential indicators as required by the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities;
- Setting the Council's Minimum Revenue Provision (MRP) Policy, which defines how the Council will pay for capital assets through revenue contributions each year (as required by Regulation under the Local Government and Public Involvement in Health Act 2007);
- Setting the Treasury Management Strategy in accordance with the CIPFA Code of Practice on Treasury Management;
- Adopting the Council's Treasury Management Policy Statement as recommended within the CIPFA Code of Practice 2011;
- Setting the Investment Strategy (in accordance with the Department for Communities and Local Government (DCLG) investment guidance);
- Affirming the effective management and responsibility for the control of risk and clearly identifying our appetite for risk. The Council's risk appetite is low in order to give priority to **S**ecurity, **L**iquidity then **Y**ield (or return on investments).

The main issues for Members to note are:

1. The CIPFA Code of Practice and associated Guidance Notes adopted by the Council in December 2012 require that:

   - Credit ratings should only be used as a starting point when considering risk. Use should also be made of market data and information, the quality financial press, information on government support for banks and the credit ratings of that government support;
   - There needs to be, at a minimum, a mid year review of Treasury Management Strategy and Performance. The review is intended to highlight any areas of concern that have arisen since the original strategy was approved;

- Each Council must delegate the role of scrutiny of Treasury Management Strategy and policies to a specific named body – the Audit and Governance Committee has been given this role;

- Members should be provided with access to relevant training – Members are also personally responsible for ensuring they have the necessary skills and training.

  The aim is for all Members to have ownership and understanding when making decisions on Treasury Management matters.

2. With regard to Counterparty selection for investment, rather than adopt a Lowest Common Denominator (LCD) methodology, a broader counterparty evaluation criteria is used by Capita Asset Services (the Council's Treasury Management consultants). This methodology has been progressively enhanced over the last year and now uses a sophisticated modelling approach with credit ratings from all three rating agencies forming the core element – but in line with best practice/guidance also includes the following as overlays: -

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

   The adoption of the above approach will help mitigate risks associated with the investment portfolio.

3. As agreed in past Treasury Management Strategies, it is proposed that the Council (following consultation with our advisors) will not use the approach suggested by CIPFA of using the lowest common denominator rating from all three rating agencies to determine creditworthy counterparties (as Moodys are currently very much more aggressive in giving low ratings than the other two agencies). The use of the Lowest Common Denominator rating would give the Council a very restrictive/unworkable counterparty list which would result in a disproportional (high) level of investment in a few institutions. Consequently this would increase risk as the investments would be held with a limited number of counterparties - which would be counter-productive in not allowing the sharing / spreading of risk over a higher number of counterparties. This would therefore be unworkable and leave the Council with few banks on its approved lending list.

   The Capita Asset Services creditworthiness service does though, use ratings from all three agencies, but by using a scoring system, does not give undue importance to just one agency's ratings.

   The main rating agencies (Fitch, Moody's and Standard & Poor's) have, through much of the financial crisis, provided some institutions with a ratings "uplift" due to implied levels of sovereign support. More recently, in response to the evolving regulatory regime, the agencies have indicated they may remove these "uplifts". This process may commence during 2014/15 and / or 2015/16. It is important to stress that the rating agency changes do not reflect any changes in the underlying status of the institution or credit environment, merely the implied level of sovereign support that has been built into ratings through the financial crisis.

As a result of these rating agency changes, the credit element of Capita's future methodology, adopted by the Council, will focus solely on the Short and Long Term ratings of an institution (with the introduction of a modest widening of the 'lowest band' of the 'Green – 100 days' category, to ease the effect of a potential fall in some entities ratings as a result of implied support removal). Rating Watch and Outlook information will continue to be assessed where it relates to these categories. This is the same process for Standard & Poor's that has always been taken, but a change to the use of Fitch and Moody's ratings. Furthermore, the methodology will continue to utilise CDS prices as an overlay to ratings.

4. The proposed Counterparty limits for 2015/16 have been increased, reflecting higher investment balances available at present – in line with Capita's suggested 20% maximum of investment balances deposited with any one institution.

The approach taken in item 2 and 3 above allows officers charged with the Treasury responsibilities to have the most appropriate/market assessment to aid the investment decision making process and provides a broad methodology for identifying High Credit Quality counterparties.

Equalities Implications

There are no equalities implications arising from the report.

Legal Implications

Approval of Prudential Indicators and an Annual Investment Strategy is a legal requirement of the Local Government Act 2003. Members are required under the CIPFA Code of Practice to have ownership and understanding when making decisions on Treasury Management matters.

Resource and Value for Money Implications

All financial resource implications are detailed in the body of this report which links to the Council's Medium Term Financial Strategy.

Risk Implications

Risk is inherent in Treasury Management and as such a risk based approach has been adopted throughout the report with regard to Treasury Management processes.

A Glossary of terms utilised within the report can be found at **ANNEX 8**.

Report Author

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***Background Papers**:-*	***Local Government Act 2003***
	CIPFA Code of Practice on Treasury Management in Public Services 2011
	DCLG Guidance on Local Government Investments March 2010
	Treasury Management Strategy Statement, Treasury Management Policy Statement, Minimum Revenue Provision Policy Statement & Annual Investment Statement 2014/15 Council 25/02/2014
	Annual Treasury Report 2013/14 Council, 16/09/14
	Mid-year Treasury Report 2014/15 Council, 16/12/14
	Budget & Medium Term Financial Strategy 2015/16
	Treasury Management Training slides, 4th February 2015
	Treasury Management Practices 2015/16 (Operational Detail)

1. Introduction

1.1 The Treasury Management Policy Statement

This Council defines its Treasury Management activities as:

- The management of the Council'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.

- 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 value for money in Treasury Management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

- 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.

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

1.2 Reporting Requirements

The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of polices, estimates and actuals. These reports are required to be adequately scrutinised by committee. This role is undertaken by the Audit and Governance Committee.

Prudential and Treasury Indicators and Treasury Strategy (This report – February) - The first, and most important report covers:

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

A Mid Year Treasury Management Report (by December) – This will update Members with the progress of the capital position, amending prudential indicators as necessary, and report whether the treasury strategy is meeting the strategy or whether any policies require revision.

An Annual Treasury Report (by September) – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

1.3 Treasury Management Strategy for 2015/16

The strategy for 2015/16 covers two main areas:

a) Capital Issues

- the Capital Plans and the Prudential Indicators (2.1, 2.2);
- the Minimum Revenue Provision (MRP) policy (2.3).

b) Treasury Management Issues

- the current treasury position (2.4);
- treasury indicators which will limit the treasury risk and activities of the Council (3);
- prospects for interest rates (3.3);
- the borrowing strategy (3.4);
- policy on borrowing in advance of need (3.5);
- debt rescheduling (3.6);
- the investment strategy (4);
- creditworthiness policy (4.2); and
- policy on use of external service providers (Annex 7, TMP 11).

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

1.4 Training

The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. Training was undertaken by Members on two occasions in 2010 and once in 2011 and detailed Treasury Management training was provided in both February 2014 and February 2015. Further training is planned for September 2015 but will also be provided as and when required.
The training needs of Treasury Management Officers are regularly reviewed as part of the performance development and management process.

1.5 Treasury Management Consultants

The Council uses Capita Asset Services, Treasury Solutions as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

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

2. The Capital Prudential Indicators 2015/16 – 2017/18

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.

2.1 Capital Expenditure. 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:

Capital Expenditure	2013/14 Actual £m	2014/15 Projected Outturn* £m	2015/16 Estimate** £m	2016/17 Estimate £m	2017/18 Estimate £m
Non-HRA	1.339	0.883	1.901	2.510	2.453
HRA	7.602	5.983	10.430	10.329	15.594
Total	**8.941**	**6.866**	**12.331**	**12.839**	**18.047**

** Projected at Period 9*

*** excludes projected slippage from 2014/15*

The above financing need, excludes other long term liabilities, such as PFI and leasing arrangements which already include borrowing instruments.

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

Capital Financing (GF / HRA)	2013/14 Actual £m	2014/15 Projected Outturn* £m	2015/16 Estimate** £m	2016/17 Estimate £m	2017/18 Estimate £m
Capital Receipts	0.483	0.420	0.210	0.306	0.970
Capital Grants	0.392	0.339	0.424	2.179	1.438
Capital Reserves	2.046	1.806	2.422	0.337	4.585
Revenue Reserves	6.020	4.301	8.275	7.750	6.057
Revenue Contributions	-	-	-	0.025	0.025
Net financing need for the year	**-**	**-**	**1.000**	**2.242**	**4.972**
Total	**8.941**	**6.866**	**12.331**	**12.839**	**18.047**

2.2 The Council's Borrowing Need (the Capital Financing Requirement)

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

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

The CFR includes any other long term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes. The Council currently has no such schemes within the CFR.

The Council is asked to approve the CFR projections below:

CFR Projections	2013/14 Actual £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
Capital Financing Requirement					
CFR – Non Housing	1.312	1.242	1.973	1.706	1.438
CFR - Housing	68.041	68.029	68.017	70.246	75.206
Total CFR	**69.353**	**69.271**	**69.990**	**71.952**	**76.644**
Movement in CFR*	**(0.226)**	**(0.082)**	**0.719**	**1.962**	**4.692**

Movement in CFR represented by					
Net financing need for the year (above)	-	-	1.000	2.242	4.972
Less: MRP/VRP and other financing movements **	(0.226)	(0.082)	(0.281)	(0.280)	(0.280)
Movement in CFR	**(0.226)**	**(0.082)**	**0.719**	**1.962**	**4.692**

* CFR 2012/13 £69.579m

** Potential additional MRP arising from prudential borrowing contingency

2.3 Minimum Revenue Provision (MRP) Policy Statement

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

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

For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will be:

- **Existing practice** - MRP will follow the existing practice outlined in former CLG regulations (option 1);

These options provide for an approximate 4% reduction in the borrowing need (CFR) each year.

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

- **Asset Life Method** – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) (option 3);

These options provide for a reduction in the borrowing need over approximately the asset's life.

No revenue charge is currently required for the HRA. However under HRA reform the HRA is required to charge depreciation on its assets, which will have a revenue effect. In order to address any possible adverse impact, regulations allow the Major Repairs Allowance to be used as a proxy for depreciation for five years from 2012/13.

2.4 Core Funds and Expected Investment Balances

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year end balances for each resource and anticipated day to day cash flow balances.

Year End Resources	2013/14 Actual £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
Fund Balances/Reserves	21.266	21.376	17.575	15.048	9.920
Capital Receipts	2.943	2.523	2.046	1.740	0.770
Provisions**	3.029	3.029	3.029	3.029	3.029
Other	0.048	0.048	-	-	-
Total Core Funds	**27.286**	**26.976**	**22.650**	**19.817**	**13.719**
Working Capital*	5.564	4.826	2.372	2.026	6.151
(Under)/Over Borrowing	(4.293)	(4.211)	(3.930)	(3.650)	(3.370)
Expected Investments	**28.557**	**27.591**	**21.092**	**18.193**	**16.500**

*Working capital balances shown are estimated year end; these may be higher mid year.
** Including provision for bad debts

2.5 Affordability Prudential Indicators

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

2.6 Ratio of financing costs to net revenue stream.

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

Ratio of financing costs to net revenue stream	2013/14 Actual %	2014/15 Revised Estimate %	2015/16 Estimate %	2016/17 Estimate %	2017/18 Estimate %
Non-HRA	1.22	(1.33)	1.39	(0.25)	1.67
HRA	15.39	34.97	35.67	35.53	33.73

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

2.7 Incremental impact of capital investment decisions on Council Tax.

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

Incremental impact of capital investment decisions on the Band D Council Tax

Incremental Impact on Council Tax	2013/14 Actual £:p	2014/15 Estimate £:p	2015/16 Estimate £:p	2016/17 Estimate £:p	2017/18 Estimate £:p
Band D	(0.05)	0.16	(0.36)	0.16	0.75

2.8 Estimates of the incremental impact of capital investment decisions on housing rent levels.

Similar to the council tax calculation, this indicator identifies the trend in the cost of proposed changes in the housing capital programme recommended in this budget report compared to the Council's existing commitments and current plans, expressed as a discrete impact on weekly rent levels.

Incremental impact of capital investment decisions on housing rent levels

Incremental Impact	2013/14 Actual £:p	2014/15 Estimate £:p	2015/16 Estimate £:p	2016/17 Estimate £:p	2017/18 Estimate £:p
Weekly housing rent levels	(0.01)	(0.04)	(0.01)	(0.26)	(0.24)

This indicator shows the revenue impact on any newly proposed changes, although any discrete impact will be constrained by rent controls. The additional borrowing planned for 2016/17 and 2017/18 is reflected above.

Housing Revenue Account Debt Ratios

HRA Debt to Revenue Ratio	2013/14 Actual £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
HRA Debt	**68.041**	**68.029**	**68.017**	**70.246**	**75.206**
HRA Revenues	**20.569**	**20.510**	**20.540**	**20.653**	**21.289**
Ratio of Debt to Revenues %	**30.23**	**30.15**	**30.20**	**29.40**	**28.31**

HRA Debt per Dwelling	2013/14 Actual £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
HRA Debt	**68.041**	**68.029**	**68.017**	**70.246**	**75.206**
Number of HRA Dwellings	**4,470**	**4,445**	**4,395**	**4,345**	**4,295**
Debt per Dwelling £	**15.22**	**15.30**	**15.48**	**16.17**	**17.51**

3. Borrowing

The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The Treasury Management function ensures that the Council's cash is organised in accordance with the 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 approporiate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

3.1 Current Portfolio Position

The Council's Treasury Portfolio position at 31st March 2014, 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.

Treasury Portfolio	2013/14 Actual £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
External Debt					
Debt at 1st April	65.060	65.060	65.060	66.060	68.302
Expected change in Debt	-	-	1.000	2.242	4.972
Actual gross debt at 31st March	**65.060**	**65.060**	**66.060**	**68.302**	**73.274**
The Capital Financing Requirement	**69.353**	**69.271**	**69.990**	**71.952**	**76.644**
Under / (over) borrowing	**4.293**	**4.211**	**3.930**	**3.650**	**3.370**

Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well defined limits. A key indicator is that the Council needs to ensure that its total borrowing, net of any investments, 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 2015/16 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.

The Executive Director Corporate Services 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 – compliance with the Prudential Indicator is highlighted in the table below.

Treasury Portfolio	2013/14 Actual £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
External Debt Actual gross debt at 31st March	65.060	65.060	66.060	68.302	73.274
Expected Investments	28.557	27.591	21.092	18.193	16.500
Net Borrowing	**36,503**	**37.469**	**44.968**	**50.109**	**56.774**
The Capital Financing Requirement	69.353	69.271	69.990	71.952	76.644
Under / (over) borrowing	**32,850**	**31.802**	**25.022**	**21.843**	**19.870**

3.2. Treasury Indicators: Limits to Borrowing Activity

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

Operational Boundary	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
Borrowing	72.268	73.268	75.510	80.482
Other long term liabilities	-	-	-	-
Total	**72.268**	**73.268**	**75.510**	**80.482**

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

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

2. The Council is asked to approve the following Authorised Limit:

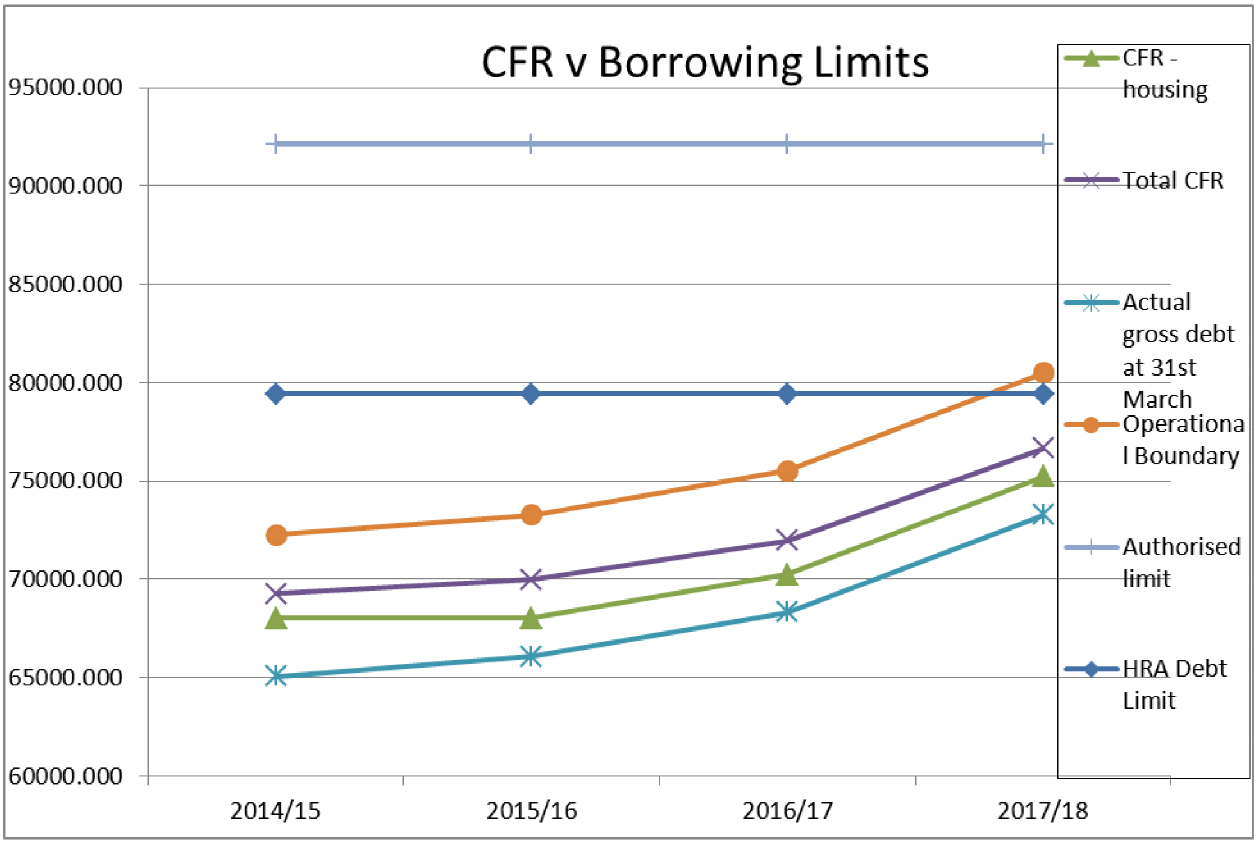
Authorised limit	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
Borrowing*	89.112	89.112	89.112	89.112
Other long term liabilities	3.000	3.000	3.000	3.000
Total	**92.112**	**92.112**	**92.112**	**92.112**

** Includes £79.407m HRA Self Financing Cap – Including Headroom of £11.344m.*

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

HRA Debt Limit	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
Total	79.407	79.407	79.407	79.407

This information summarised graphically below:



3.3. Prospects for Interest Rates

A more detailed interest rate view and economic commentary is at **Annex 5.1 and 5.2**.

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. The following table gives our central view.

Annual Average %	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)		
		5 year	25 year	50 year
Mar 2015	0.50	2.20	3.40	3.40
Jun 2015	0.50	2.20	3.50	3.50
Sep 2015	0.50	2.30	3.70	3.70
Dec 2015	0.75	2.50	3.80	3.80
Mar 2016	0.75	2.60	4.00	4.00
Jun 2016	1.00	2.80	4.20	4.20
Sep 2016	1.00	2.90	4.30	4.30
Dec 2016	1.25	3.00	4.40	4.40
Mar 2017	1.25	3.20	4.50	4.50
Jun 2017	1.50	3.30	4.60	4.60
Sep 2017	1.75	3.40	4.70	4.70
Dec 2017	1.75	3.50	4.70	4.70
Mar 2018	2.00	3.60	4.80	4.80

UK GDP growth surged during 2013 and the first half of 2014. During the second half of 2014, it has cooled somewhat but still remained strong by UK standards. Growth is likely to strengthen marginally in 2015 and 2016 under the stimulative effect of the fall in oil prices. There still needs to be a significant rebalancing of the economy away from consumer spending to manufacturing, business investment and exporting in order for this recovery to become more firmly established. One drag on the economy has been that wage inflation had only recently started to exceed CPI inflation, so enabling disposable income and living standards to start improving. The plunge in the price of oil brought CPI inflation down to a low of 0.5% in December, the lowest rate since May 2000 and it could even turn negative in the first half of 2015; this will further increase consumer disposable income and so underpin economic growth during 2015. However, labour productivity needs to improve substantially to enable wage rates to increase and further support consumer disposable income and economic growth. In addition, the encouraging rate at which unemployment has been falling must eventually feed through into pressure for wage increases, though current views on the amount of hidden slack in the labour market probably means that this is unlikely to happen early in 2015.

The US, the biggest world economy, has generated stunning growth rates of 4.6% (annualised) in Q2 2014 and 5.0% in Q3, followed by a cooler 2.6% in Q4 (overall 2.4% for 2014 as a whole). This is hugely promising for the outlook for strong growth going forwards and it very much looks as if the US is now firmly on the path of full recovery from the financial crisis of 2008. Consequently, it is now confidently expected that the US will be the first major western economy to start on central rate increases by the end of 2015.

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

- Greece: the general election on 25 January 2015 brought to power a coalition which is strongly anti EU imposed austerity. However, if this should eventually result in Greece leaving the Euro, it is unlikely that this will directly destabilise the Eurozone as the EU has put in place adequate firewalls to contain the immediate fallout to just Greece. However, the indirect effect of the likely strenthening of anti EU and anti austerity political parties throughout the EU is much more difficult to gauge;

- As for the Eurozone in general, concerns in respect of a major crisis subsided considerably in 2013. However, the downturn in growth and inflation during the second half of 2014, and worries over the Ukraine situation and the Middle East, have led to a resurgence of those concerns as risks increase that it could be heading into a prolonged period of deflation and very weak growth. Sovereign debt difficulties have not gone away and major concerns could return in respect of individual countries that do not dynamically address fundamental issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy (as Ireland has done). It is, therefore, 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. Counterparty risks therefore remain elevated. This continues to suggest the use of higher quality counterparties for shorter time periods;

- Investment returns are likely to remain relatively low during 2015/16 and beyond;

- Borrowing interest rates have been highly volatile during 2014 and early 2015 as alternating bouts of good and bad news have promoted optimism, and then pessimism, in financial markets. The opening weeks of 2015 saw gilt yields dip to historically phenominally low levels after inflation plunged, a flight to quality as a result of the Greek situation and the start of a huge programme of quantitative easing (purchase of EZ government debt), by the ECB in January 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.

3.4 Borrowing Strategy

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council’s reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is relatively high.

Against this background and the risks within the economic forecast, caution will be adopted with the 2015/16 treasury operations. The Director of Finance 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 a greater than expected increase in the anticipated rate to US tapering of asset purchases, or 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.

Any decisions will be reported to Council at the next available opportunity.

Treasury Management - Limits on Activity

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

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

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

Interest rate exposure	2015/16	2016/17	2017/18
	£m	£m	£m
	Upper	Upper	Upper
Limits on fixed interest rates based on net debt	53.515	57.094	61.184
Limits on variable interest rates based on net debt	6.556	6.718	7.080
Limits on fixed interest rates:			
• ***Debt only***	65.563	67.184	70.795
• ***Investments only***	20.558	17.760	16.061
Limits on variable interest rates			
• ***Debt only***	6.556	6.718	7.080
• ***Investments only***	8.223	7.104	6.424

Maturity structure of fixed interest rate borrowing 2015/16		
	Lower	**Upper**
Under 12 months	0%	20%
12 months to 2 years	0%	20%
2 years to 5 years	0%	25%
5 years to 10 years	0%	75%
10 years and above	0%	100%
Maturity structure of variable interest rate borrowing 2015/16		
	Lower	Upper
Under 12 months	0%	20%
12 months to 2 years	0%	20%
2 years to 5 years	0%	25%
5 years to 10 years	0%	75%
10 years and above	0%	100%

3.5 Policy on Borrowing in Advance of Need

The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

3.6. Debt Rescheduling

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

The reasons for any rescheduling to take place will include:

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

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.

All rescheduling will be reported to the Council, at the earliest meeting following its action.

4.0 Annual Investment Strategy

Introduction: changes to credit rating methodology

The main rating agencies (Fitch, Moody's and Standard & Poor's) have, through much of the financial crisis, provided some institutions with a ratings "uplift" due to implied levels of sovereign support. More recently, in response to the evolving regulatory regime, the agencies have indicated they may remove these "uplifts". This process may commence during 2014/15 and / or 2015/16.

The actual timing of the changes is still subject to discussion, but this does mean that immediate changes to the credit methodology are required and may lead to some entities seeing their ratings fall as a result of implied support removal.

It is important to stress that the rating agency changes do not reflect any changes in the underlying status of the institution or credit environment, merely the implied level of sovereign support that has been built into ratings through the financial crisis. The eventual removal of implied sovereign support will only take place when the regulatory and economic environments have ensured that financial institutions are much stronger and less prone to failure in a financial crisis.

Both Fitch and Moody's provide "standalone" credit ratings for financial institutions. For Fitch, it is the Viability Rating, while Moody's has the Financial Strength Rating. Due to the future removal of sovereign support from institution assessments, both agencies have suggested going forward that these will be in line with their respective Long Term ratings. As such, there is no point monitoring both Long Term and these "standalone" ratings.

Furthermore, Fitch has already begun assessing its Support ratings, with a clear expectation that these will be lowered to 5, which is defined as "a bank for which there is a possibility of external support, but it cannot be relied upon." With all institutions likely to drop to these levels, there is little to no differentiation to be had by assessing Support ratings.

As a result of these rating agency changes, the credit element of Capita's future methodology, adopted by the Council, will focus solely on the Short and Long Term ratings of an institution (with the introduction of a modest widening of the 'lowest band' of the 'Green – 100 days' category, to ease the effect of a potential fall in some entities ratings as a result of implied support removal). Rating Watch and Outlook information will continue to be assessed where it relates to these categories. This is the same process for Standard & Poor's that has always been taken, but a change to the use of Fitch and Moody's ratings. Furthermore, the methodology will continue to utilise CDS prices as an overlay to ratings.

4.1 Investment Policy

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 return.

In accordance with the above guidance from the Government 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.

Continuing regulatory changes in the banking sector are designed to see greater stability, lower risk and the removal of expectations of Government financial support should an institution fail. This withdrawal of implied sovereign support is anticipated to have an effect on ratings applied to institutions. This will result in the key ratings used to monitor counterparties being the Short Term and Long Term ratings only. Viability, Financial Strength and Support Ratings previously applied will effectively become redundant. This change does not reflect deterioration in the credit environment but rather a change of method in response to regulatory changes.

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

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.

Investment instruments identified for use in the financial year are listed in **ANNEX 5.3** under the 'specified' and 'non-specified' investments categories. Counterparty limits will be as set through the Council's treasury management practices – schedules.

4.2 Creditworthiness Policy

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, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:

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

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 suggested duration for investments. The Council will therefore use counterparties within the following durational bands*:*

- Yellow 5 years *
- Dark pink 5 years for Enhanced money market funds (EMMFs) with a credit score of 1.25
- Light pink 5 years for Enhanced money market funds (EMMFs) with a credit score of 1.5
- 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

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

** this category is for AAA rated Government debt or its equivalent; please also see collateralised deposits added into **ANNEX 3** as an investment instrument.*

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

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

All credit ratings will be monitored on a daily basis/as and when notified. 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. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition this Authority will also use market data and market information, information on government support for banks and the credit ratings of that government support.

4.3 Country Limits

The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA+ or higher from Fitch (or equivalent). The list of countries that qualify using this credit criteria as at the date of this report are shown in **ANNEX 4**. This list will be added to, or deducted from by officers should ratings change in accordance with this policy.

Capita Asset Services also recommends that no more than 20% of the Council's investment portfolio should be placed with an individual counterparty, in order to spread risk. The approach at the Council is to set monetary limits of up to **£5m** with individual institutions, which equates approximately to Capita's recommendation (based on current average investment levels of approximately £25m).

4.4 Investment Strategy

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).

Investment Returns Expectations. Bank Rate is forecast to remain unchanged at 0.5% before starting to rise from quarter 4 of 2015. Bank Rate forecasts for financial year ends (March) are:

- 2015/16 0.75%
- 2016/17 1.25%
- 2017/18 2.00%

There are downside risks to these forecasts (i.e. start of increases in Bank Rate occurs later) if economic growth weakens. However, should the pace of growth quicken, there could be an upside risk.

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:

Year	Up to 100 Days %
2015/16	0.60
2016/17	1.25
2017/18	1.75
2018/19	2.25
2019/20	2.75
2020/21	3.00
2021/22	3.25
2022/23	3.25
Later Years	3.50

Investment Treasury Indicator and Limit - total principal funds invested for greater than 364 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

The Council is asked to approve the treasury indicator and limit: -

Maximum principal sums invested > 364 days			
£m	**2015/16**	**2016/17**	**2017/18**
Principal sums invested > 364 days	£m 2.000	£m 2.000	£m 2.000

For its cash flow generated balances, the Council will seek to utilise its business reserve instant access and notice accounts, money market funds and short-dated deposits (overnight to100 days) in order to benefit from the compounding of interest.

4.5 Icelandic Bank Investments

Glitnir - £2.55m partial repayment of our deposits was received on the 15th March 2012. The balance due to the Council is currently being held in Icelandic Krone (ISK) but release of these funds at par is dependent on a change in Icelandic Law which currently does not allow the distribution of ISK outside Iceland.

The Central Bank of Iceland (CBI) recently held a currency auction, which gave creditors the opportunity to convert their ISK into Euros, thus allowing them to repatriate their funds. However, due to the anticipated detrimental 'Bid' level that would be set by the CBI and additional losses that would be incurred due to currency exchange rate fluctuation with the Euro, it was decided that we would not participate at this time. Interest will however continue to accrue on these funds untill the date of final settlement.

Heritable – In September 2013 the Council received what could be the final distribution from the Administrators. The total sum received is £1.415m against our claim of £1.505m, making a total recovery of 94.02%. The Administrators are witholding a sum as a contingency against disputed claims, which if rejected, could result in a further residual distribution.

Kaupthing Singer & Friedlander – At the end of December 2014, the Council had received £2.620m against our claim of £3.175m. Latest estimates given by the administrator project a total recovery of 85% to 86.5% or approximately £2.699m to £2.746m, with a future distribution estimated for mid to late 2015.

4.6 End of year investment report

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

4.7 Scheme of delegation

Please see **ANNEX 5**.

4.8 Role of the Section 151 Officer

Please see **ANNEX 6.**

10. Annex

ANNEX 1

Interest Rate Forecasts 2014 – 2017

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

Capita Asset Services Interest Rate View	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18
Bank Rate View	0.50%	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.25%	1.50%	1.75%	1.75%	2.00%
3 Month LIBID	0.50%	0.50%	0.60%	0.80%	0.90%	1.10%	1.10%	1.30%	1.40%	1.50%	1.80%	1.90%	2.10%
6 Month LIBID	0.70%	0.70%	0.80%	1.00%	1.10%	1.20%	1.30%	1.50%	1.60%	1.70%	2.00%	2.10%	2.30%
12 Month LIBID	0.90%	1.00%	1.10%	1.30%	1.40%	1.50%	1.60%	1.80%	1.90%	2.00%	2.30%	2.40%	2.60%
5yr PWLB Rate	2.20%	2.20%	2.30%	2.50%	2.60%	2.80%	2.90%	3.00%	3.20%	3.30%	3.40%	3.50%	3.60%
10yr PWLB Rate	2.80%	2.80%	3.00%	3.20%	3.30%	3.50%	3.60%	3.70%	3.80%	3.90%	4.00%	4.10%	4.20%
25yr PWLB Rate	3.40%	3.50%	3.70%	3.80%	4.00%	4.20%	4.30%	4.40%	4.50%	4.60%	4.70%	4.70%	4.80%
50yr PWLB Rate	3.40%	3.50%	3.70%	3.80%	4.00%	4.20%	4.30%	4.40%	4.50%	4.60%	4.70%	4.70%	4.80%
Bank Rate													
Capita Asset Services	0.50%	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.25%	1.50%	1.75%	1.75%	2.00%
Capital Economics	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.25%	-	-	-	-	-
5yr PWLB Rate													
Capita Asset Services	2.20%	2.20%	2.30%	2.50%	2.60%	2.80%	2.90%	3.00%	3.20%	3.30%	3.40%	3.50%	3.60%
Capital Economics	2.20%	2.50%	2.70%	3.00%	3.10%	3.20%	3.30%	3.40%	-	-	-	-	-
10yr PWLB Rate													
Capita Asset Services	2.80%	2.80%	3.00%	3.20%	3.30%	3.50%	3.60%	3.70%	3.80%	3.90%	4.00%	4.10%	4.20%
Capital Economics	2.80%	3.05%	3.30%	3.55%	3.60%	3.65%	3.70%	3.80%	-	-	-	-	-
25yr PWLB Rate													
Capita Asset Services	3.40%	3.50%	3.70%	3.80%	4.00%	4.20%	4.30%	4.40%	4.50%	4.60%	4.70%	4.70%	4.80%
Capital Economics	3.25%	3.45%	3.65%	3.85%	3.95%	4.05%	4.15%	4.25%	-	-	-	-	-
50yr PWLB Rate													
Capita Asset Services	3.40%	3.50%	3.70%	3.80%	4.00%	4.20%	4.30%	4.40%	4.50%	4.60%	4.70%	4.70%	4.80%
Capital Economics	3.30%	3.50%	3.70%	3.90%	4.00%	4.10%	4.20%	4.30%	-	-	-	-	-

Please note – The current PWLB rates and forecast shown above have taken into account the 20 basis point certainty rate reduction effective as of the 1st November 2012

Economic Background

UK. After strong UK GDP growth in 2013 at an annual rate of 2.7%, and then growth in 2014 of 0.6% in Q1, 0.8% Q2, 0.7% Q3 and 0.5% Q4 (annual rate for 2014 of 2.6%), there are good grounds for optimism that growth could pick back up again during 2015 after cooling towards the end of 2014, as the positive effects from the fall in the price of oil feeds through to consumers and other parts of the economy. For this recovery to become more balanced and sustainable in the longer term, the recovery needs to move away from dependence on consumer expenditure and the housing market to exporting, and particularly of manufactured goods, both of which need to substantially improve on their recent lacklustre performance. This overall strong growth has resulted in unemployment falling much faster than expected. The MPC is not expected to take any action for at least the first half of 2015 as inflation could even turn negative in this period. However, even if oil was to remain at around the $50-60 per barrel price throughout all of 2015, the positive effect of the initial drop in price during Q4 2014 will fall out of the twelve month calculation of CPI towards the end of the year, leaving inflation vulnerable to a sharp jump upwards. The MPC will also be keeping alert as to how quickly slack in the economy is being used up, especially as unemployment continues to fall. It will also be monitoring how strong a stimulative effect the drop in oil prices has on the economy as falling inflation will be comfortably exceeded by wage increases meaning that the disposable incomes of consumers will recover strongly during 2015. One continuing area of weakness in the UK economy is the need for a major improvement in labour productivity, which has languished at dismal levels since 2008, to support increases in pay rates after the positive effect of the fall in oil prices dissipates. Unemployment is expected to keep on its downward trend and this is likely to feed through into a return to significant increases in wage growth at some point during the next few years. However, just how much those increases in pay rates will counteract the dampening effect of stepped increases in Bank Rate, albeit at a slow rate, on consumer confidence, consumer expenditure and the buoyancy of the housing market, is open to conjecture.

Also encouraging has been the sharp fall in inflation (CPI), reaching 1.0% in November 2014 and then halving to 0.5% in December, the lowest rate since May 2000. Forward indications are that inflation could turn negative during the earlier part of 2015; however, the MPC is focused on where inflation will be over a 2 – 3 year time horizon so too much emphasis should not be placed on the short term outlook in terms of the risks around when Bank Rate is likely to start increasing. The return to strong growth has helped lower forecasts for the increase in Government debt over the last year but monthly public sector deficit figures during 2014 have disappointed, being only a fraction lower than the previous year through to December 2014. The autumn statement, therefore, had to revise the speed with which the deficit is forecast to be eliminated. The flight to quality in January 2015 has seen gilt yields fall to incredibly low levels, reducing interest costs on new and replacement government debt.

Eurozone (EZ). The Eurozone is facing an increasing threat from weak or negative growth and from deflation. In January 2015, the inflation rate fell further, to reach a low of -0.6%. However, this is an average for all EZ countries and includes some countries with even higher negative rates of inflation. Initially, the ECB took some rather limited action in June and September 2014 to loosen monetary policy in order to promote growth. As this failed to have much of a discernible effect, the ECB launched a massive €1.1 trillion programme of quantitative easing in January 2015 to buy up high credit quality government debt of selected EZ countries. This programme will run to September 2016.

Concern in financial markets for the Eurozone had subsided considerably after the prolonged crisis during 2011-2013. However, sovereign debt difficulties have not gone away and major issues could return in respect of any countries that do not dynamically address issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy, (as Ireland has done). It is, therefore, possible over the next few years that levels of government debt to GDP ratios could continue to rise for some countries. This could mean that sovereign debt concerns have not disappeared but, rather, have only been postponed. The ECB's pledge in 2012 to buy unlimited amounts of bonds of countries which ask for a bailout has provided heavily indebted countries with a strong defence against market forces. This has bought them time to make progress with their economies to return to growth or to reduce the degree of recession. However, debt to GDP ratios (2013 figures) of Greece 180%, Italy 133%, Portugal 129%, Ireland 124% and Cyprus 112%, remain a cause for concern, especially as some of these countries are experiencing continuing rates of increase in debt in excess of their rate of economic growth i.e. these debt ratios are likely to continue to deteriorate.

Any sharp downturn in economic growth would make these countries particularly vulnerable to a new bout of sovereign debt crisis. It should also be noted that Italy has the third biggest debt mountain in the world behind Japan and the US.

Greece: the general election on 25 January 2015 has brought to power a coalition which is anti EU imposed austerity. Although it is not certain that Greece will leave the Euro, the recent intractability of the troika (the EU, ECB and IMF), to finding a negotiated compromise with the new Greek government leaves this as a real possibility. However, if Greece was to leave the EZ, it is unlikely that this will directly destabilise the Eurozone as the EU has put in place adequate firewalls to contain the immediate fallout to just Greece. Nevertheless, the indirect effects of the likely strengthening of anti EU and anti-austerity political parties throughout the EU is much more difficult to gauge. There are particular concerns as to whether democratically elected governments will lose the support of electorates suffering under EZ imposed austerity programmes, especially in countries which have high unemployment rates. Of particular concern is the fact that Spain and Portugal have general elections coming up in late 2015. This will give ample opportunity for anti-austerity parties to make a big impact.

There are also major concerns as to whether the governments of France and Italy will effectively implement austerity programmes and undertake overdue reforms to improve national competitiveness. These countries already have political parties with major electoral support for anti EU and anti-austerity policies. Any loss of market confidence in either of the two largest Eurozone economies, after Germany, would present a huge challenge to the resources of the ECB to defend their debt.

USA. The U.S. Federal Reserve ended its monthly asset purchases in October 2014. GDP growth rates (annualised) for Q2 of 4.6%, Q3 of 5.0% and Q4 of 2.6%, (overall 2.4% during 2014 as a whole), provides great promise for strong growth going forward. It is confidently forecast that the first increase in the Fed. rate will occur by the end of 2015.

China. Government action in 2014 to stimulate the economy almost succeeded in achieving the target of 7.5% growth but recent government statements have emphasised that growth going forward will slow marginally as this becomes the new normal for China. There are concerns that the Chinese leadership has only just started to address an unbalanced economy, which is heavily over dependent on new investment expenditure, and for a potential bubble in the property sector to burst, as it did in Japan in the 1990s, with its consequent impact on the financial health of the banking sector. There are also concerns around the potential size, and dubious creditworthiness, of some bank lending to local government organisations and major corporates. This primarily occurred during the government promoted expansion of credit, which was aimed at protecting the overall rate of growth in the economy after the Lehmans crisis.

Japan. Japan is causing considerable concern as the increase in sales tax in April 2014 has suppressed consumer expenditure and growth to the extent that it has slipped back into recession. The Japanese government already has the highest debt to GDP ratio in the world.

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 transpires over 2015. Forecasts for average earnings beyond the three year time horizon will be heavily dependent on economic and political developments. Major volatility in bond yields is likely to endure as investor fears and confidence ebb and flow between favouring more risky assets i.e. equities, or the safe haven of bonds.

The overall longer run trend is for gilt yields and PWLB rates to rise, due to the high volume of gilt issuance in the UK, and of bond issuance in other major western countries. 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.

The interest rate forecasts in this report are based on an initial assumption that there will not be a major resurgence of the EZ debt crisis. There is an increased risk that Greece could end up leaving the Euro but if this happens, the EZ now has sufficient fire walls in place that a Greek exit would have little immediate direct impact on the rest of the EZ and the Euro. It is therefore expected that there will be an overall managed, albeit painful and tortuous, resolution of any EZ debt crisis that may occur where EZ institutions and governments eventually do what is necessary - but only when all else has been tried and failed. Under this assumed scenario, growth within the EZ will be weak at best for the next couple of years with some EZ countries experiencing low or negative growth, which will, over that time period, see an increase in total government debt to GDP ratios. There is a significant danger that these ratios could rise to the point where markets lose confidence in the financial viability of one, or more, countries, especially if growth disappoints and / or efforts to reduce government deficits fail to deliver the necessary reductions. However, it is impossible to forecast whether any individual country will lose such confidence, or when, and so precipitate a sharp resurgence of the EZ debt crisis. While the ECB has adequate resources to manage a debt crisis in a small EZ country, if one, or more, of the larger countries were to experience a major crisis of market confidence, this would present a serious challenge to the ECB and to EZ politicians.

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 strong economic growth is 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.
- Monetary policy action failing to stimulate sustainable growth and to combat the threat of deflation in western economies, especially the Eurozone and Japan.

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

- An adverse reaction by financial markets to the result of the UK general election in May 2015 and the economic and debt management policies adopted by the new government.
- The ECB severely disappointing financial markets with a programme of asset purchases which proves insufficient to significantly stimulate growth in the EZ.
- The commencement by the US Federal Reserve of increases in the Fed. funds rate in 2015, 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.

<u>Specified and Non-Specified Investments</u>:

Specified Investments:

These investments are **sterling** denominated investments of **not more than one-year maturity,** meeting the minimum 'high' quality criteria where applicable. They are of relatively high security, high liquidity and are low risk assets where the possibility of loss of principal or investment income is small, they could be for a longer period but where the Council has the right to be repaid within 12 months if it wishes. The investments could be managed In-House or by Fund Managers.

These would include investments with:

- The UK Government (such as the Debt Management Office, UK Treasury Bills or Gilts with less than one year to maturity). To facilitate use of such instruments a Custodian account was opened during 2012/13 with King & Shaxson Ltd (a primary participant authorised to bid at Treasury bill tenders on behalf of investors regulated by the Financial Services Authority (FSA) and subject to its rules and guidance in their activities);
- A Local Authority, Parish Council or Community Council;
- Pooled investment vehicles or Collective Investment Schemes structured as Open Ended Investment Companies (OEIC's) such as Money Market Funds (MMF's) Enhanced Money Market Funds, Government Liquidity Funds, Enhanced Cash Funds, Bond Funds (but not Corporate Bonds) and Gilt Funds, that have a high credit quality and been awarded a high credit rating of AAA by Standard and Poor's, Moody's or Fitch rating agencies and a Low Long Term Volatility rating;
- A body that has a high credit quality and been awarded a high credit rating by a credit rating agency (such as a bank or building society) and complies with the Capita Credit Worthiness service;
- A body which has been provided with a government issued guarantee for wholesale deposits within specific timeframes and/or is part or wholly nationalised by that Government. Where these guarantees are in place and the government has an AA+ sovereign long term rating these institutions will be included within the Council's criteria temporarily until such time as the ratings improve or the guarantees are withdrawn. Monies will only be deposited within the timeframe of the guarantee.

SPECIFIED INVESTMENTS	Minimum 'High' Credit Criteria	Limits
UK Government/ Debt Management Agency Deposit Facility	Defined by Regulation UK Treasury (AA+)	£5m
Term deposits – Local Authorities	Defined by Regulation (Sec 23 of the 2003 act)	£5m
Treasury Bills	Defined by Regulation UK Treasury (AA+)	£5m
Term deposits and Callable deposits – Banks and Building Societies	In accordance with Capita's Creditworthiness Service up to 'Orange' or 'Blue'	£5m individual institutions £8m Group limit
Pooled investment vehicles *(OEIC's, MMF's etc)	AAA (Moody's MR1, Fitch MMF and S&P M).	£5m
Banks and Building Societies – Forward deals up to 1 year from arrangement to maturity	In accordance with Capita 's Creditworthiness Service up to 'Orange 'or 'Blue'	£5m

*For pooled investment vehicles or Collective Investment Schemes (such as MMF's) that have a high credit quality and have been rated AAA by Standard and Poor's, Moody's or Fitch rating agencies and have a Constant Net Asset Value (CNAV).

Non-Specified Investments:

Non-specified investments are any other type of investment (i.e. not defined as Specified above) and could be managed In-House or by Fund Managers. The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out below. Non specified investments would include any sterling investments with:

Ref	Non Specified Investment Categories	Credit Rating	Comment
1	**Supranational Bonds greater than 1 year to maturity** • **Multilateral development bank bonds** – These are bonds defined as an international financial institution having as one of its objects economic development, either generally or in any region of the world (e.g. European Investment Bank etc.). • **A financial institution that is guaranteed by the United Kingdom Government** (e.g. The Guaranteed Export Finance Company {GEFCO}) The security of interest and principal on maturity is on a par with the Government and so very secure, and these bonds usually provide returns above equivalent gilt edged securities. However the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.	AA+	Would not use in-house due to size of investment portfolio limiting benefit to the Council.
2	**UK Gilt edged securities** with a maturity of greater than one year. These are Government bonds and so provide the highest security of interest and the repayment of principal on maturity. Similar to category (1) above, the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.	AAA Sovereign Rated (1 Rating Agency) AA+ Sovereign Rating (2 Rating Agencies)	Custodian Account held with King & Shaxson to trade on our behalf
3	**Certificates of Deposit** with credit rated deposit takers (Banks and Building Societies)	Capita Asset Services Minimum Credit Worthiness rating	Custodian Account held with King & Shaxson to trade on our behalf
4	**Term deposit with a body which has been nationalised/part nationalised** by high credit rated (sovereign rating AAA or AA+) countries and provided with a **Government issued guarantee** for wholesale deposits within specific timeframes.	AAA or AA+ Sovereign Rated Capita Asset Services Credit Worthiness rating 'Blue'	Under the current criteria this applies in the UK to Lloyds Banking Group plc and Royal Bank of Scotland Group institutions

Ref	Non Specified Investment Categories	Credit Rating	Comment
	Where these guarantees are in place and the government has an AAA or AA+ sovereign long term rating these institutions will be included within the Council's criteria temporarily until such time as the ratings improve or the guarantees are withdrawn. Monies will only be deposited within the timeframe of the guarantee.		
5	A Term Deposit with a body which is an **Eligible Institution** for the HM Treasury Credit Guarantee Scheme initially announced on 13th October 2008*(1)*. The Credit Guarantee Scheme forms part of the Government's measures to ensure the stability of the financial system and protect ordinary savers, depositors, businesses and borrowers, by; a) providing sufficient liquidity in the short term, b) making available new capital to UK banks and Building Societies to strengthen their resources c) ensuring the banking system has the funds necessary to maintain lending in the medium term.	In accordance with Capita Asset Services Credit Worthiness rating	Use restricted by Capita Asset Services Credit Worthiness rating
6	Government guarantee on ALL deposits by high credit rated (AAA sovereign rating non UK) countries.	AAA Sovereign Rated	Not in Use, currently restricting investments to UK only
7	The **Council's Own Banker** if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as possible.	Out of range	Balances reviewed and minimised on daily basis
8	Any **Bank or Building society** that has at minimum a long term credit rating of A-, a minimum short term credit rating of F1, or equivalent, for deposits with a maturity of greater than one year (including forward deals in excess of one year from inception to repayment).	In accordance with Capita Asset Services Credit Worthiness rating	Use restricted by Capita Asset Services Credit Worthiness rating
9	**Callable Deposits** with a **Bank or Building society** that has at minimum a long term credit rating of A-, a minimum short term credit rating of F1, or equivalent.	In accordance with Capita Asset Services Credit Worthiness rating	Use restricted by Capita Asset Services Credit Worthiness rating
10	**Share capital or loan capital** in a body corporate – The use of these instruments will be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. Revenue resources will not be invested in corporate bodies.	N/A	Unlikely to use due to size of portfolio and high risk associated. Also requires additional approval as deemed as capital expenditure.

Within categories 3, 4, 5 and 6, and in accordance with the Code, the Council has developed additional criteria to set the overall amount of monies which will be invested in these bodies. All investments will be made in sterling to eliminate exchange rate risk.

The criteria are detailed in the table below and will be used in conjunction withCapita's Creditworthiness service.

Counterparty Type (TBC's minimum credit ratings for approved lending list)	**Minimum Credit Criteria**	**Limits***	
Bank or Building Society (a minimum Long Term Credit Rating of AAA, a minimum short term credit rating of F1 (or equivalent))	Capita 'Yellow'	5 yrs	£5m
Bank or Building Society (a minimum Long Term Credit Rating of AA-, a minimum short term credit rating of F1 (or equivalent))	Capita 'Yellow'	4 yrs	£5m
Bank (a minimum Long Term Credit Rating of A-, a minimum short term credit rating of F1 (or equivalent))	Capita 'Yellow'	3 yrs	£5m
Banks Nationalised/Part nationalised by high credit rated (sovereign rating AAA or AA+) countries *(a)*	Capita 'Blue' (UK)	Specified in Guarantee	£5m
An Eligible Institution eligible under the HM Treasury Credit Guarantee Scheme *(c)*	Capita 'Blue'	Specified in Guarantee	£5m
Government guarantee on ALL deposits by high credit rated (AAA sovereign rating) countries *(b).*	Capita 'Blue'	Specified in Guarantee	£5m
The Council's own Banker - if it fails to meet basic criteria	n/a	Overnight	£2m
Building Society (a minimum Long Term Credit Rating of A-, a minimum short term credit rating of F1 (or equivalent /if applicable) AND assets > £4bn)	Capita 'Yellow'	3 yrs	£5m
Building Society (a Long Term Credit Rating of A- , a minimum short term credit rating of F1 (or equivalent/if applicable) AND assets < £4bn but > £1bn)	Capita 'Purple'	2 yrs	£5m
Group Limits **-** Maximum investments in Institutions within the same financial group	As above for individual investment	As above for individual investment	£8m
Territory Limits **-** Maximum investments in Institutions within the same Country (Approx 15% of investment programme) Non- UK	As above for individual investment	As above for individual investment	£3.75m
Territory Limits - Maximum investments in Institutions within the same Continent (Approx 30% of investment programme) Non UK	As above for individual investment	As above for individual investment	£7.5m

* Under current Capita Asset Services credit worthiness criteria, only institutions with a rating of 'Purple' or 'Yellow' are suggested as appropriate counterparties for investments over 1 year, with limit ranges of 2 years and 5 years respectively.

(a) **Nationalised/Part Nationalised Banks** in the UK have credit ratings which do not conform to the credit criteria usually used by local authorities to identify banks which are of high creditworthiness. In particular, as they no longer are separate institutions in their own right, it is impossible for Fitch to assign them an individual rating for their stand alone financial strength. Accordingly, Fitch has assigned an F rating which means that at a historical point of time, this bank failed and is now owned by the Government.

However, these institutions are now recipients of an F1+ short term rating as they effectively take on the creditworthiness of the Government itself i.e. deposits made with them are effectively being made to the Government. They also have a support rating of 1; in other words, on both counts, they have the highest ratings possible.

(b) **Blanket (explicit) guarantees on all deposits.** Some countries have supported their banking system by giving a blanket guarantee on ALL deposits e.g. Ireland and Singapore. Authorities may view that the sovereign rating of that country then takes precedence over the individual credit ratings for the banks covered by that guarantee.

(c) **UK banking system support package (implicit guarantee).** It should be noted that the UK Government did NOT give a blanket guarantee on all deposits but underlined its determination to ensure the security of the UK banking system by supporting eight named banks with a £500bn support package. The Council will need to decide if we wish to authorise lending to those named banks on the basis of that implicit guarantee on local authority deposits placed with these eight banks or to rely on the credit ratings of the individual banks.

The original list of banks covered when the support package was initially announced was: -

Abbey (now part of Santander)
Barclays
HBOS (now part of the Lloyds Group)
Lloyds TSB (now split into two banks)
HSBC
Nationwide Building Society
RBS
Standard Chartered

Banks eligible for support under the UK bail-out package and which have issued debt guaranteed by the Government are eligible for a continuing Government guarantee when debt issues originally issued and guaranteed by the Government mature and are refinanced. However, no other institutions can make use of this support as it closed to new issues and entrants on 28.2.10. The banks which have used this explicit guarantee are as follows: -

- Bank of Scotland
- Barclays
- Clydesdale
- Coventry Building Society
- Investec bank
- Nationwide Building Society
- Rothschild Continuation Finance plc
- Standard Life Bank
- Tesco Personal Finance plc
- Royal Bank of Scotland
- West Bromwich Building Society
- Yorkshire Building Society

(d) **Other countries.** The US, countries within the EU and Switzerland (and other countries) are currently providing major support packages to their banking systems.

Approved Countries for investments

Country	Agency		
	Fitch	Moody's	Standard & Poor
Australia	AAA	Aaa	AAA
Canada	AAA	Aaa	AAA
Denmark	AAA	Aaa	AAA
Finland	AAA	Aaa	AA+
Germany	AAA	Aaa	AAA
Luxembourg	AAA	Aaa	AAA
Netherlands	AAA	Aaa	AA+
Norway	AAA	Aaa	AAA
Singapore	AAA	Aaa	AAA
Sweden	AAA	Aaa	AAA
Switzerland	AAA	Aaa	AAA
USA	AAA	Aaa	AA+
UK*	AA+	Aa1	AAA

(Per Capita Asset Services Credit Rating List at 12th December 2014)

* At its meeting of the 15th September 2009, full Council approved a recommendation that;

'*authorises the use of institutions currently supported by the UK Government should its Sovereign rating be downgraded below the current requirement for a 'AAA' rating by all three rating agencies'*

this approval continues to form part of the strategy in 2015/16.

Treasury Management Scheme of Delegation

(i) Full Council

- receiving and reviewing reports on Treasury Management policies, practices and activities;
- approval of annual strategy;
- approval of/amendments to the organisation's adopted clauses, Treasury Management Policy statement and Treasury Management practices;
- budget consideration and approval;
- approval of the division of responsibilities;
- receiving and reviewing regular monitoring reports and acting on recommendations.

(ii) Cabinet

- receiving and reviewing Treasury Management policy statement and Treasury Management practices and making recommendations to the full Council;
- receiving and reviewing regular monitoring reports and making recommendations to the full Council;
- approving the selection of external service providers and agreeing terms of appointment.

(iii) Audit and Governance Committee

- reviewing the Treasury Management policy and procedures and making recommendations to the Cabinet;
- receiving and reviewing regular monitoring (quarterly/half yearly) and making recommendations to the Cabinet.

The Treasury Management Role of the Section 151 Officer

The S151 (responsible) Officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers.

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ANNEX 7

TREASURY MANAGEMENT PRACTICES

The Treasury Management Practices document (TMP's) forms detailed operational procedures and processes for the Treasury Management function. This document can be found on the Council's Internet by following the following link;

http://www.tamworth.gov.uk/treasury-practices

and clicking on the TMP's folder.

The items below are summaries of the individual TMP's which the Council has to produce and adopt under the Treasury Code of Practice.

TMP1 : RISK MANAGEMENT

General Statement

The Section 151 Officer will design, implement and monitor all arrangements for the identification, management and control of Treasury Management risk; will report at least annually on the adequacy / suitability of the arrangements and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the Council's objectives. The reports will be in accordance with the procedures contained in TMP6.

1.1 Credit and Counterparty Risk Management

Credit and counter-party risk is the risk of failure by a counterparty to meet its contractual obligations to the organisation under an investment, borrowing, capital project or partnership financing, particularly as a result of the counterparty's diminished creditworthiness, and the resulting detrimental effect on the organisation's capital or current (revenue) resources.

This organisation regards a key objective of its Treasury Management activities to be the security of the principal sums it invests. Accordingly, it will ensure that its counterparty lists and limits reflect a prudent attitude towards organisations with which funds may be deposited, and will limit its investment activities to the instruments, methods and techniques referred to in TMP4 Approved Instruments Methods and Techniques and detailed in the TMP Operational document.

It also recognises the need to have, and will therefore maintain, a formal counterparty policy in respect of those organisations from which it may borrow, or with whom it may enter into other financing arrangements.

1.2 Liquidity Risk Management

This is the risk that cash will not be available when it is needed, that ineffective management of liquidity creates additional unbudgeted costs, and that the organisation's business/service objectives will be thereby compromised.

This organisation will ensure it has adequate though not excessive cash resources, borrowing arrangements, overdraft or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives. This organisation will only borrow in advance of need where there is a clear business case for doing so and will only do so for the current capital programme or to finance future debt maturities.

1.3 Interest Rate Risk Management

The risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.

This organisation will manage its exposure to fluctuations in interest rates with a view to containing its interest costs, or securing its interest revenues, in accordance with the amounts provided in its budgetary arrangements as amended in accordance with TMP6 Reporting requirements and management information arrangements.
It will achieve this by the prudent use of its approved financing and investment instruments, methods and techniques, primarily to create stability and certainty of costs and revenues, but at the same time retaining a sufficient degree of flexibility to take advantage of unexpected, potentially advantageous changes in the level or structure of interest rates. This should be the subject to the consideration and, if required, approval of any policy or budgetary implications.

1.4 Exchange Rate Risk Management

The risk that fluctuations in foreign exchange rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.

It will manage its exposure to fluctuations in exchange rates so as to minimise any detrimental impact on its budgeted income/expenditure levels.

1.5 Refinancing Risk Management

The risk that maturing borrowings, capital, project or partnership financings cannot be refinanced on terms that reflect the provisions made by the organisation for those refinancing, both capital and current (revenue), and/or that the terms are inconsistent with prevailing market conditions at the time.

This organisation will ensure that its borrowing, private financing and partnership arrangements are negotiated, structured and documented, and the maturity profile of the monies so raised are managed, with a view to obtaining offer terms for renewal or refinancing, if required, which are competitive and as favourable to the organisation as can reasonably be achieved in the light of market conditions prevailing at the time.

It will actively manage its relationships with its counterparties in these transactions in such a manner as to secure this objective, and will avoid over reliance on any one source of funding if this might jeopardise achievement of the above.

1.6 Legal and Regulatory Risk Management

The risk that the organisation itself, or an organisation with which it is dealing in its Treasury Management activities, fails to act in accordance with its legal powers or regulatory requirements, and that the organisation suffers losses accordingly.

This organisation will ensure that all of its Treasury Management activities comply with its statutory powers and regulatory requirements. It will demonstrate such compliance, if required to do so, to all parties with whom it deals in such activities. In framing its credit and counterparty policy under TMP1[1] credit and counterparty risk management, it will ensure that there is evidence of counterparties' powers, Council and compliance in respect of the transactions they may effect with the organisation, particularly with regard to duty of care and fees charged.

This organisation recognises that future legislative or regulatory changes may impact on its Treasury Management activities and, so far as it is reasonably able to do so, will seek to minimise the risk of these impacting adversely on the organisation.

1.7 Fraud, Error and Corruption, and Contingency Management

The risk that an organisation fails to identify the circumstances in which it may be exposed to the risk of loss through fraud, error, corruption or other eventualities in its Treasury Management dealings, and fails to employ suitable systems and procedures and maintain effective contingency management arrangements to these ends. It includes the area of risk commonly referred to as operational risk.

This organisation will ensure that it has identified the circumstances which may expose it to the risk of loss through fraud, error, corruption or other eventualities in its Treasury Management dealings. Accordingly, it will employ suitable systems and procedures, and will maintain effective contingency management arrangements, to these ends.

The Council will therefore:-

a) Seek to ensure an adequate division of responsibilities and maintenance at all times of an adequate level of internal check which minimises such risks.
b) Fully document all its Treasury Management activities so that there can be no possible confusion as to what proper procedures are.
c) Staff will not be allowed to take up Treasury Management activities until they have had proper training in procedures and are then subject to an adequate and appropriate level of supervision.

Records will be maintained of all Treasury Management transactions so that there is a full audit trail and evidence of the appropriate checks being carried out.

1.8 Market Risk Management

The risk that, through adverse market fluctuations in the value of the principal sums an organisation borrows and invests, its stated Treasury Management policies and objectives are compromised, against which effects it has failed to protect itself adequately.

This organisation will seek to ensure that its stated Treasury Management policies and objectives will not be compromised by adverse market fluctuations in the value of the principal sums it invests, and will accordingly seek to protect its self from the effects of such fluctuations.

TMP2 : BEST VALUE AND PERFORMANCE MEASUREMENT

The Borough Council is committed to the pursuit of best value in its Treasury Management activities, and to the use of performance methodology in support of that aim, within the framework set out in the Treasury Management Policy Statement.

The Treasury Management function will be the subject of ongoing analysis of the value it adds in support of the Council's stated service objectives. It will be the subject of regular examination of alternative methods of service delivery, of the availability of fiscal, grant or subsidy incentives, and the scope for other potential improvements. The performance of the Treasury Management function will be measured using the criteria set out in the detailed TMP Operational document.

TMP3 : DECISION-MAKING AND ANALYSIS

The Council will maintain full records of its Treasury Management decisions, and of the processes and practices applied in reaching those decisions, both for the purposes of learning from the past, and for demonstrating that reasonable steps were taken to ensure that all issues relevant to those decisions were taken into account at the time. The issues to be addressed and processes and practices to be pursued in reaching decisions are set out in the detailed TMP Operational document.

TMP4 : APPROVED INSTRUMENTS, METHODS AND TECHNIQUES

The Council will undertake its Treasury Management activities by employing only those instruments, methods and techniques are set out in the detailed TMP Operational document and within the limits and parameters defined in TMP1.

TMP5 : ORGANISATION, CLARITY AND SEGREGATION OF RESPONSIBILITIES, AND DEALING ARRANGEMENTS

The Council considers it essential, for the purposes of the effective control and monitoring of its Treasury Management activities, for the reduction of risk of fraud or error, and for the pursuit of optimum performance, that these activities are structured and managed in a fully integrated manner, and that there is at all times clarity of Treasury Management responsibilities.

The principle on which this will be based is the clear distinction between those charged with setting Treasury Management policies and those charged with implementing and controlling these policies, particularly with regard to the execution and transmission of funds, the recording and administering of Treasury Management decisions and the audit and review of the Treasury Management function.

If and when this organisation intends, as a result of lack of resources or other circumstances, to depart from these principles, the Section 151 Officer will ensure that the reasons are properly reported in accordance with TMP6 and the implications properly considered and evaluated.

The Section 151 Officer will ensure that there are clear written statements of the responsibilities for each post engaged in Treasury Management, and the arrangements for absence cover. He will also ensure that at all times those engaged in Treasury Management will follow the policies and procedures set out. The present arrangements are set out in the detailed TMP Operational document.

The Section 151 Officer will ensure that there is proper documentation for all deals and transactions, and that procedures exist for the effective transmission of funds. The present arrangements are set out in the detailed TMP Operational document.
The delegations to the Section 151 Officer in respect of Treasury Management are set out in the detailed TMP Operational document. He or she will fulfil all such responsibilities in accordance with the Council's policy statement and TMP's and, if a CIPFA member, the Standard of Professional Practice on Treasury Management.

TMP6 : REPORTING REQUIREMENTS AND MANAGEMENT INFORMATION ARRANGEMENTS

The Council will ensure that regular reports are prepared and considered on the implementation of its Treasury Management policies; on the effects of decisions taken and transactions executed in pursuit of those policies; implications of changes, particularly budgetary, resulting from regulatory, economic, market or other factors affecting its Treasury Management activities; and on the performance of the Treasury Management function.

As a minimum Cabinet and Council will receive:

- An annual report on the planned strategy to be pursued in the coming year and the reporting of Prudential Indicators
- A mid-year review
- An annual report on the performance of the Treasury Management function including the performance against the Prudential Indicators, the effects of the decisions taken and the transactions executed in the past year and on any circumstances of non-compliance with the Council's Treasury Management policy statement and TMP's.

Cabinet will receive regular monitoring reports on Treasury Management activities and risks.

The Audit and Governance Committee will have responsibility for the scrutiny of Treasury Management policies and practices.

The Treasury Management indicators will be considered together with the Treasury Management indicators in the Prudential Code as part of the budget approval process.
The present arrangements and the form of these reports are set out in the detailed TMP Operational document.

TMP7 : BUDGETING, ACCOUNTING AND AUDIT ARRANGEMENTS

The Section 151 Officer will prepare and Council will approve and, if necessary, from time to time will amend, an annual budget for Treasury Management, which will bring together all of the costs involved in running the Treasury Management function together with associated income. The matters to be included will at minimum be those required by statute or regulation, together, with such information as will demonstrate compliance with TMP1, TMP2 and TMP4.

The Section 151 Officer will exercise effective controls over this budget and report upon and recommend any changes required in accordance with TMP6.

The Council will account for its Treasury Management activities, for decisions made and transactions executed in accordance with appropriate accounting practices and standards, and with statutory and regulatory requirements in force for the time being.

TMP8 : CASH AND CASH FLOW MANAGEMENT

Unless statutory or regulatory requirements demand otherwise, all monies in the hands of the Council will be under the control of the Section 151 Officer and will be aggregated for cash flow and investment management purposes. Cash flow projections will be prepared on a regular and timely basis and the Section 151 Officer will ensure that these are adequate for the purpose of monitoring compliance with TMP1. The present arrangements for preparing cash flow projections, and their form, are set out in the detailed TMP Operational document.

TMP9 : MONEY LAUNDERING

The Council is alert to the possibility that it may become the subject of an attempt to involve it in a transaction involving the laundering of money. The Council will, therefore, maintain procedures for verifying and recording the identity of counterparties and reporting suspicions, and will ensure that all staff involved are properly trained. The present arrangements, including the name of the officer to whom reports should be made, are set out in the detailed TMP Operational document.

TMP10 : TRAINING AND QUALIFICATIONS

The Council recognises the importance of ensuring that all staff involved in the Treasury Management function are fully equipped to undertake the duties and responsibilities allocated to them. It will seek to appoint individuals, who are both capable and experienced and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. The Section 151 Officer will recommend and implement the necessary arrangements.

The Section 151 Officer will ensure that Council members tasked with Treasury Management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities.

Those charged with governance recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively.

TMP11 : USE OF EXTERNAL SERVICE PROVIDERS

The Council recognises that responsibility for the Treasury Management decisions remains with the Council at all times. It recognises that there may be potential value in employing external providers of Treasury Management services, in order to acquire access to specialist skills and resources. When it employs such service providers, it will ensure it does so for reasons, which will have been submitted to a full evaluation of the costs and benefits. Terms of appointment will be properly agreed, documented and subject to regular review. It will ensure, where feasible and necessary, that a spread of service providers is used, to avoid over reliance on one or a small number of companies. Where services are subject to formal tender or re-tender arrangements, legislative requirements will always be observed. The monitoring of such arrangements rests with the Section 151 Officer, and details of the current arrangements are set out in the detailed TMP Operational document.

TMP12 : CORPORATE GOVERNANCE

The Council is committed to the pursuit of proper corporate governance throughout its services, and to establishing the principles and practices by which this can be achieved. Accordingly the Treasury Management function and its activities will be undertaken with openness, transparency, honesty, integrity and accountability.

The Council has adopted and implemented the key recommendations of the Code. This, together with the other arrangements are set out in the detailed TMP Operational document and are considered vital to the achievement of proper governance in Treasury Management, and the Section 151 Officer will monitor and, if and when necessary, report upon the effectiveness of these arrangements.

Treasury Management Glossary of Terms

Bank Rate	The Official Bank rate paid on commercial bank reserves i.e. reserves placed by commercial banks with the Bank of England as part of the Bank's operations to reduce volatility in short term interest rates in the money markets.
Base Rate	Minimum lending rate of a bank or financial institution in the UK.
Capital Financing Requirement	The Council's underlying need for borrowing for a capital purpose.
Counterparty	The organisations responsible for repaying the Council's investment upon maturity and for making interest payments.
Credit Default Swap (CDS)	A specific kind of counterparty agreement which allows the transfer of third party credit risk from one party to the other. One party in the swap is a lender and faces credit risk from a third party, and the counterparty in the credit default swap agrees to insure this risk in exchange for regular periodic payments (essentially an insurance premium). If the third party defaults, the party providing insurance will have to purchase from the insured party the defaulted asset. In turn, the insurer pays the insured the remaining interest on the debt, as well as the principal.
Credit Rating	This is a scoring system that lenders issue organisations with, to determine how credit worthy they are.
Gilts	These are issued by the UK Government in order to finance public expenditure. Gilts are generally issued for a set period and pay a fixed rate of interest for the period.
iTraxx	This is an index published by Markit who are a leading company in CDS pricing and valuation. The index is based on an equal weighting of the CDS spread of 25 European financial companies. Clients can use the iTraxx to see where an institutions CDS spread is relative to that of the market and judge its creditworthiness in that manner, as well as looking at the credit ratings.
Liquidity	An asset is perfectly liquid if one can trade immediately, at a price not worse than the uninformed expected value, the quantity one desires.
Long term	A period of one year or more.
Maturity	The date when an investment is repaid or the period covered by a fixed term investment.

Minimum Revenue Provision	Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, machinery etc. It would be impractical to charge the entirety of such expenditure to revenue in the year in which it was incurred therefore such expenditure is spread over several years in order to try to match the years over which such assets benefit the local community through their useful life. The manner of spreading these costs is through an annual Minimum Revenue Provision
Monetary Policy Committee (MPC)	Interest rates are set by the Bank's Monetary Policy Committee. The MPC sets an interest rate it judges will enable the inflation target to be met. Their primary target (as set by the Government) is to keep inflation at or around 2%.
Security	An investment instrument, issued by a corporation, government, or other organization which offers evidence of debt or equity.
Short Term	A period of 364 days or less
Supranational Bonds	A supranational entity is formed by two or more central governments with the purpose of promoting economic development for the member countries. Supranational institutions finance their activities by issuing debt, such as supranational bonds. Examples of supranational institutions include the European Investment Bank and the World Bank. Similarly to the government bonds, the bonds issued by these institutions are considered very safe and have a high credit rating.
Treasury Management	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.
Working Capital	Cash and other liquid assets needed to finance the everyday running of a business such as the payment of salaries and purchases.
Yield	The annual rate of return on an investment, expressed as a percentage.

ICELANDIC BANKING SITUATION AS AT 31/12/2014

	Deposit with;	Ref Number	Date Invested	Amount		%
1	GLITNIR	1696	10/10/2007	1,000,000		
	GLITNIR	1715	31/08/2007	1,000,000		
	GLITNIR	1754	14/12/2007	1,000,000		
	Total Principal			3,000,000		
	Estimated of Contractual or Interest due to point of administration (subject to currency exchange rate fluctuations)			155,000		
	Total of Claim			3,155,000		
	Repayments Received to date			(2,554,432)	*	*80.96*
	Outstanding at 31/12/2014			**600,568**	**	
	Estimated Remaining			**600,568**		

*Partial repayment received on the 15th March 2012 in GBP/EUR/USD/NOK. The balance is currently being held in Icelandic Krone (ISK). Release of these funds is dependent on a change in Icelandic Law which currently does not allow the distribution of ISK outside the country. **Interest will accrue on these funds untill the date of final settlement, the final payment value may also be subject to exchange rate fluctuations.
- Best case recovery 100%

	Deposit with;	Ref Number	Date Invested	Amount		%
2	Heritable Bank	1802	12/09/2008	500,000		
	Heritable Bank	1803	15/09/2008	1,000,000		
	Total Principal			1,500,000		
	Interest due at point of administration 07/10/2008			5,127		
	Total of Claim			1,505,127		
	Repayments Received to date			(1,415,080)		*94.02*
	Outstanding at 31/12/2014			**90,047**		
	Estimated Remaining			**0**		

- Final recovery received of 94.02% (declared 23/08/13, though Administrators are retaining a contingency for disputed claims that could be distributed at a later date).

	Deposit with;	Ref Number	Date Invested	Amount		%
3	Singer & Friedlander	1716	31/08/2007	1,000,000		
	Singer & Friedlander	1740	31/10/2007	1,000,000		
	Singer & Friedlander	1746	14/01/2008	1,000,000		
	Total Principal			3,000,000		
	Interest due at point of administration 08/10/2008			175,256		
	Total of Claim			3,175,256		
	Repayments Received to date			(2,619,586)		*82.50*
	Outstanding at 31/12/2014			**555,670**		
	Estimated Remaining			**87,320**		

- Current indications project an 82.5% recovery of our investments

	Summary					
	Total Principal			7,500,000		
	Interest			335,383		
	Total of Claim			7,835,383		
	Repayments Received to date			(6,589,098)		*84.09*
	Outstanding at 31/12/2014			**1,246,285**		
	Estimated Remaining			**687,888**		

1 Registered Bank in Iceland - In Administration under Icelandic Law

2 & 3 Registered Bank in UK - In Administration in UK by Ernst & Young Under English Law

Total Estimated Recovery (including Outstanding) **7,276,986**

Total Estimated % Remaining **92.87%**