

TREASURY MANAGEMENT STRATEGY STATEMENT, TREASURY MANAGEMENT POLICY STATEMENT, MINIMUM REVENUE PROVISION POLICY STATEMENT AND ANNUAL INVESTMENT STATEMENT 2016/17

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 2016/17 – 2018/19 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); and
- Affirming the effective management and responsibility for the control of risk and clearly identify our appetite for risk. The Council's risk appetite is low in order to give priority to **Security, Liquidity then Yield** (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 requires 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 helps 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 which would as a consequence increase investment risk with the investments being 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/institutions on its approved lending list and would increase investment risk.

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. Commencing in 2015, in response to the evolving regulatory regime, all three agencies have begun removing these "uplifts" with the timing of the process determined by regulatory progress at the national level. The process has been part of a wider reassessment of methodologies by each of the rating agencies.

In addition to the removal of implied support, new methodologies take account of additional factors, such as regulatory capital levels. In some cases, these factors have “netted” each other off, to leave underlying ratings either unchanged or with little change. A consequence of these new methodologies is that they have also lowered the importance of the (Fitch) Support and Viability ratings and have seen the (Moody’s) Financial Strength rating withdrawn by the agency.

In keeping with the agencies’ new methodologies, the credit element of our own credit assessment process now focuses solely on the Short and Long Term ratings of an institution. While this is the same process that has always been used by Standard & Poor’s, this has been a change to the use of Fitch and Moody’s ratings. It is important to stress that the other key elements to our process, namely the assessment of Rating Watch and Outlook information as well as the Credit Default Swap (CDS) overlay have not been changed.

The evolving regulatory environment, in tandem with the rating agencies’ new methodologies also means that sovereign ratings are now of lesser importance in the assessment process. Where through the crisis, clients typically assigned the highest sovereign rating to their criteria the new regulatory environment is attempting to break the link between sovereign support and domestic financial institutions. While this Authority understands the changes that have taken place, it will continue to specify a minimum sovereign rating of ‘AA –’. This is in relation to the fact that the underlying domestic and where appropriate, international, economic and wider political and social background will still have an influence on the ratings of a financial institution.

It is important to stress that these rating agency changes do not reflect any changes in the underlying status or credit quality of the institution, merely a reassessment of their methodologies in light of enacted and future expected changes to the regulatory environment in which financial institutions operate. While some banks have received lower credit ratings as a result of these changes, this does not mean that they are suddenly less credit worthy than they were formerly. Rather, in the majority of cases, this mainly reflects the fact that implied sovereign government support has effectively been withdrawn from banks. They are now expected to have sufficiently strong balance sheets to be able to withstand foreseeable adverse financial circumstances without government support. In fact, in many cases, the balance sheets of banks are now much more robust than they were before the 2008 financial crisis when they had higher ratings than now. However, this is not universally applicable, leaving some entities with modestly lower ratings than they had through much of the “support” phase of the financial crisis.

4. The proposed Counterparty limits for 2016/17 have been increased, reflecting higher average investment balances available at present – but still 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**.

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Background Papers:-	<i>Budget & Medium Term Financial Strategy 2016/17</i>
	<i>Mid-year Treasury Report 2015/16 Council, 15/12/15</i>
	<i>Annual Treasury Report 2014/15 Council, 30/07/15</i>
	<i>Treasury Management Strategy Statement, Treasury Management Policy Statement, Minimum Revenue Provision Policy Statement & Annual Investment Statement 2015/16 Council 24/02/2015</i>
	<i>Treasury Management Training slides, 4th February 2015 & 7th October 2015</i>
	<i>CIPFA Code of Practice on Treasury Management in Public Services 2011</i>
	<i>DCLG Guidance on Local Government Investments March 2010</i>
	<i>Local Government Act 2003</i>
	<i>Treasury Management Practices 2016/17 (Operational Detail)</i>

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 policies, estimates and actuals. These reports are required to be adequately scrutinised by committee. This role is undertaken by the Audit and Governance Committee.

1.2.1 Prudential and Treasury Indicators and Treasury Strategy (Reported – 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).

1.2.2 A Mid Year Treasury Management Report (Reported 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.

1.2.3 An Annual Treasury Report (Reported 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.

A description of the Prudential Indicators is attached at **ANNEX 10**.

1.3 Treasury Management Strategy for 2016/17

The strategy for 2016/17 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 (3.2);
- 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 (4.1);
- creditworthiness policy (4.2); and
- policy on use of external service providers (4.10).

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

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. Detailed Treasury Management training was provided in February 2014 and February 2015 and most recently in October 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 2016/17 – 2018/19

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 member's 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	2014/15 Actual £m	2015/16 Projected Outturn* £m	2016/17 Estimate** £m	2017/18 Estimate £m	2018/19 Estimate £m
Non-HRA (GF)	0.581	1.127	4.535	2.641	0.837
HRA	4.972	6.374	10.217	16.135	12.695
Total	5.553	7.501	14.752	18.776	13.532

* Projected at Period 9

** excludes projected slippage from 2015/16

HRA – Housing Revenue Account / GF – General Fund

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 - Use of reserves)	2014/15 Actual £m	2015/16 Projected Outturn £m	2016/17 Estimate** £m	2017/18 Estimate £m	2018/19 Estimate £m
Capital Receipts	0.193	0.642	2.199	1.218	1.579
Capital Grants	0.240	0.454	3.220	1.247	0.434
Capital Reserves	0.635	2.413	1.920	6.099	6.434
Revenue Reserves	4.411	3.923	4.691	4.284	4.856
Revenue Contributions	0.074	0.069	0.480	-	-
Net financing need for the year	-	-	2.242	5.928	0.229
Total	5.553	7.501	14.752	18.776	13.532

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	2014/15 Actual £m	2015/16 Revised Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m
Capital Financing Requirement					
CFR – Non Housing	1.241	0.700	0.665	1.588	1.746
CFR - Housing	68.041	68.041	70.283	75.255	75.255
Total CFR	69.282	68.741	70.948	76.843	77.001
Movement in CFR*	(0.070)	(0.541)	2.207	5.895	0.158

Movement in CFR represented by					
Net financing need for the year (above)	-	-	2.242	5.928	0.229
Less: MRP/VRP and other financing movements **	(0.070)	(0.541)	(0.035)	(0.033)	(0.071)
Movement in CFR	(0.070)	(0.541)	2.207	5.895	0.158

* CFR 2013/14 £69.352m

** 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 DCLG 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	2014/15 Actual £m	2015/16 Revised Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m
Fund Balances/Reserves	24.946	19.048	17.874	13.186	7.791
Capital Receipts	3.898	4.583	11.338	19.074	26.649
Provisions*	4.773	4.704	4.619	4.619	4.619
Capital Grants	0.048	0.048	-	-	-
Total Core Funds	33.665	28.383	33.831	36.879	39.059
Working Capital**	2.911	7.409	5.010	7.237	10.075
(Under)/Over Borrowing	(4.222)	(3.681)	(3.646)	(3.613)	(3.542)
Expected Investments	32.354	32.111	35.195	40.503	45.592

* Including provision for bad debts

** Working capital balances shown are estimated year end; these may be higher mid year.

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	2014/15 Actual %	2015/16 Revised Estimate %	2016/17 Estimate %	2017/18 Estimate %	2018/19 Estimate %
Non-HRA	(1.19)	(2.97)	(4.91)	(8.00)	(11.54)
HRA	22.55	34.28	34.48	34.42	34.96

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	2014/15 Actual £:p	2015/16 Estimate £:p	2016/17 Estimate £:p	2017/18 Estimate £:p	2018/19 Estimate £:p
Band D	0.16	(0.27)	0.76	2.85	1.53

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	2014/15 Actual £:p	2015/16 Estimate £:p	2016/17 Estimate £:p	2017/18 Estimate £:p	2018/19 Estimate £:p
Weekly housing rent levels	(0.04)	0.02	0.00	0.04	0.01

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	2014/15 Actual	2015/16 Revised Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
HRA Debt* £m	68.041	68.041	70.283	75.255	75.255
HRA Revenues £m	22.412	21.065	21.100	21.775	22.628
Ratio of Debt to Revenues %	304%	323%	333%	346%	333%

HRA Debt per Dwelling	2014/15 Actual	2015/16 Revised Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
HRA Debt* £m	68.041	68.041	70.283	75.255	75.255
Number of HRA Dwellings	4,470	4,397	4,347	4,297	4,197
Debt per Dwelling £	15,222	15,474	16,168	17,513	17,931

* The HRA's notional debt borrowing requirement

As the level of debt increases compared to revenue income, risk increases.

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 appropriate 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 2015, with forward projections are summarised below. The table shows the actual external debt (the Treasury Management Operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

Treasury Portfolio	2014/15	2015/16	2016/17	2017/18	2018/19
	Actual £m	Revised Estimate £m	Estimate £m	Estimate £m	Estimate £m
External Debt					
Debt at 1st April	65.060	65.060	65.060	67.302	73.230
Expected change in Debt	-	-	2.242	5.928	0.229
Actual gross debt at 31st March	65.060	65.060	67.302	73.230	73.459
The Capital Financing Requirement	69.282	68.741	70.948	76.843	77.001
Under / (over) borrowing	4.222	3.681	3.646	3.613	3.542

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 2016/17 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Executive Director Corporate Services (the Section 151 Officer) reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report – compliance with the Prudential Indicator is highlighted in the table below.

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	2015/16 Revised Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m
Debt	72.268	73.268	75.510	80.482
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:

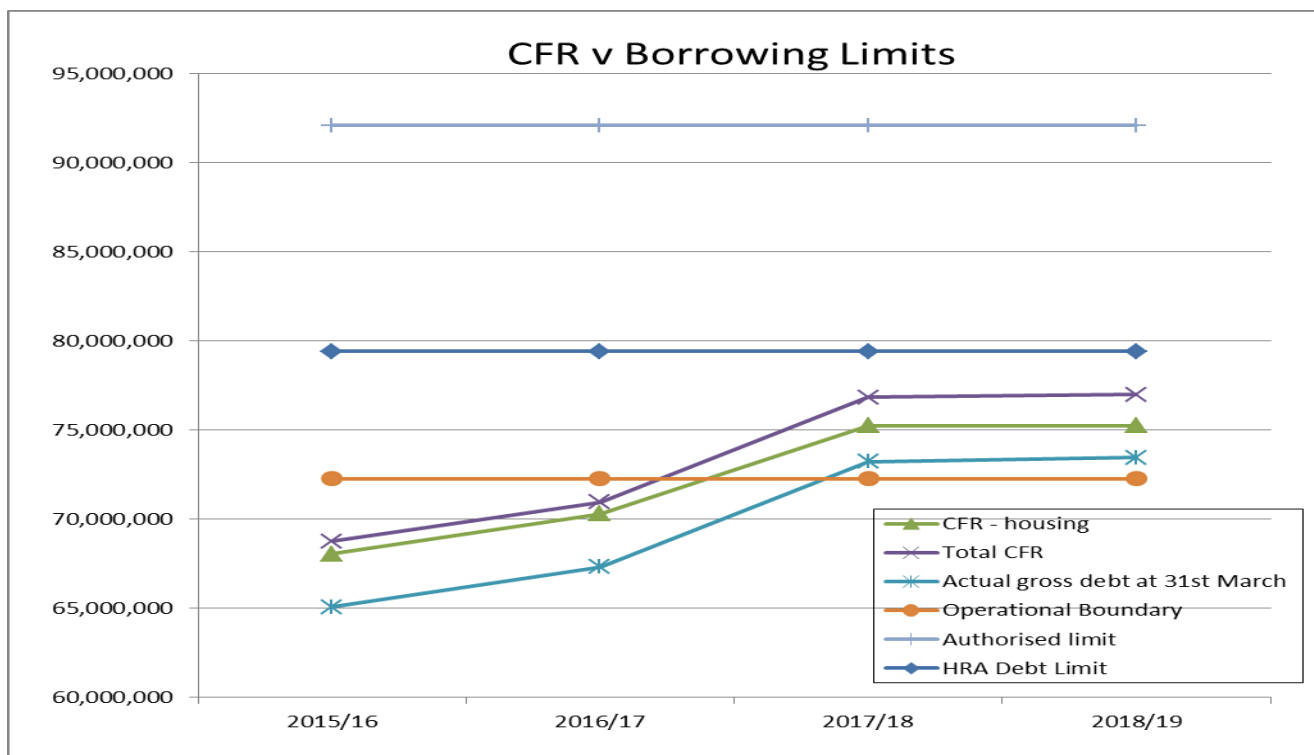
Authorised limit	2015/16 Revised Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m
Debt*	89.112	89.112	89.112	89.112
Other long term liabilities	3.000	3.000	3.000	3.000
Total	92.112	92.112	92.112	92.112

* Includes £79.407m HRA Self Financing Cap – Including initial Headroom of £11.344m at 31/03/2012

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

HRA Debt Limit	2015/16 Revised Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m	2018/19 Estimate £m
HRA Debt Cap	79.407	79.407	79.407	79.407
HRA CFR	68.041	70.283	75.255	75.255
HRA Headroom	11.366	9.124	4.152	4.152

This information summarised graphically below:



3.3. Prospects for Interest Rates

A more detailed interest rate view and economic commentary is at **ANNEX 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 their central view.

Annual Average %	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)			
		5 year	10 year	25 year	50 year
Mar 2016	0.50	2.00	2.60	3.40	3.20
Jun 2016	0.50	2.10	2.70	3.40	3.20
Sep 2016	0.50	2.20	2.80	3.50	3.30
Dec 2016	0.75	2.30	2.90	3.60	3.40
Mar 2017	0.75	2.40	3.00	3.70	3.50
Jun 2017	1.00	2.50	3.10	3.70	3.60
Sep 2017	1.00	2.60	3.20	3.80	3.70
Dec 2017	1.25	2.70	3.30	3.90	3.80
Mar 2018	1.25	2.80	3.40	4.00	3.90
Jun 2018	1.50	2.90	3.50	4.00	3.90
Sep 2018	1.50	3.00	3.60	4.10	4.00
Dec 2018	1.75	3.10	3.60	4.10	4.00
Mar 2019	1.75	3.20	3.70	4.10	4.00

UK. UK GDP growth rates in 2013 of 2.2% and 2.9% in 2014 were the strongest growth rates of any G7 country; the 2014 growth rate was also the strongest UK rate since 2006 and although the 2015 growth rate is likely to be a leading rate in the G7 again, it looks likely to disappoint previous forecasts and come in at about 2%. Quarter 1 of 2015 was weak at +0.4% (+2.9% y/y) though there was a slight increase in quarter 2 to +0.5% (+2.3% y/y) before weakening again to +0.4% (2.1% y/y) in quarter 3. The November Bank of England Inflation Report included a forecast for growth to remain around 2.5 – 2.7% over the next three years, driven mainly by strong consumer demand as the squeeze on the disposable incomes of consumers has been reversed by a recovery in wage inflation at the same time that CPI inflation has fallen to, or near to, zero since February 2015. Investment expenditure is also expected to support growth. However, since the August Inflation report was issued, most worldwide economic statistics have been weak and financial markets have been particularly volatile. The November Inflation Report flagged up particular concerns for the potential impact of these factors on the UK.

The Inflation Report was also notably subdued in respect of the forecasts for inflation; this was expected to barely get back up to the 2% target within the 2-3 year time horizon. The increase in the forecast for inflation at the three year horizon was the biggest in a decade and at the two year horizon was the biggest since February 2013. However, the first round of falls in oil, gas and food prices over late 2014 and also in the first half 2015, will fall out of the 12 month calculation of CPI during late 2015 / early 2016 but a second, more recent round of falls in fuel and commodity prices will delay a significant tick up in inflation from around zero: this is now expected to get back to around 1% by the end of 2016 and not get to near 2% until the second half of 2017, though the forecasts in the Report itself were for an even slower rate of increase. However, more falls in the price of oil and imports from emerging countries in early 2016 will further delay the pick up in inflation. There is therefore considerable uncertainty around how quickly pay and CPI inflation will rise in the next few years and this makes it difficult to forecast when the Monetary Policy Committee (MPC) will decide to make a start on increasing Bank Rate.

The weakening of UK GDP growth during 2015 and the deterioration of prospects in the international scene, especially for emerging market countries, have consequently led to forecasts for when the first increase in Bank Rate would occur being pushed back to quarter 4 of 2016. There is downside risk to this forecast i.e. it could be pushed further back.

USA. The American economy made a strong comeback after a weak first quarter's growth at +0.6% (annualised), to grow by no less than 3.9% in quarter 2 of 2015, but then pulled back to 2.0% in quarter 3. The run of strong monthly increases in nonfarm payrolls figures for growth in employment in 2015 prepared the way for the Fed. to embark on its long awaited first increase in rates of 0.25% at its December meeting. However, the accompanying message with this first increase was that further increases will be at a much slower rate, and to a much lower ultimate ceiling, than in previous business cycles, mirroring comments by our own MPC.

EZ. In the Eurozone, the ECB fired its big bazooka in January 2015 in unleashing a massive €1.1 trillion programme of quantitative easing to buy up high credit quality government and other debt of selected EZ countries. This programme of €60bn of monthly purchases started in March 2015 and it was intended to run initially to September 2016. At the ECB's December meeting, this programme was extended to March 2017 but was not increased in terms of the amount of monthly purchases. The ECB also cut its deposit facility rate by 10bps from -0.2% to -0.3%. This programme of monetary easing has had a limited positive effect in helping a recovery in consumer and business confidence and a start to some improvement in economic growth. GDP growth rose to 0.5% in quarter 1 2015 (1.3% y/y) but has then eased back to +0.4% (+1.6% y/y) in quarter 2 and to +0.3% (+1.6%) in quarter 3. Financial markets were disappointed by the ECB's lack of more decisive action in December and it is likely that it will need to boost its Quantitative Easing (QE) programme if it is to succeed in significantly improving growth in the EZ and getting inflation up from the current level of around zero to its target of 2%.

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

Portugal and Spain. The general elections in September and December respectively have opened up new areas of political risk where the previous right wing reform-focused pro-austerity mainstream political parties have lost their majority of seats. An anti-austerity coalition has won a majority of seats in Portugal while the general election in Spain produced a complex result where no combination of two main parties is able to form a coalition with a majority of seats. It is currently unresolved as to what administrations will result from both these situations. This has created nervousness in bond and equity markets for these countries which has the potential to spill over and impact on the whole Eurozone project.

In summary, the central view is that;

- Investment returns are likely to remain relatively low during 2016/17 and beyond;
- Borrowing interest rates have been highly volatile during 2015 as alternating bouts of good and bad news have promoted optimism, and then pessimism, in financial markets.

Gilt yields have continued to remain at historically phenomenally low levels during 2015. The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in later times, when authorities will not be able to avoid new borrowing to finance new capital expenditure and/or to refinance maturing debt;

- There will remain a cost of carry to any new borrowing which causes an increase in investments as this will incur a revenue loss between borrowing costs and investment returns.

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.

Use of internal funds is a more efficient use of resources as borrowing rates are significantly higher than investment returns. However, as and when resources are depleted or utilised, the opportunity to use internal balances will decrease and interest charges will increase.

Against this background and the risks within the economic forecast, caution will be adopted with the 2016/17 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	2016/17	2017/18	2018/19
	£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
<i>Limits on fixed interest rates:</i>			
• <i>Debt only</i>	65.563	67.184	70.795
• <i>Investments only</i>	20.558	17.760	16.061
<i>Limits on variable interest rates</i>			
• <i>Debt only</i>	6.556	6.718	7.080
• <i>Investments only</i>	8.223	7.104	6.424

Maturity structure of fixed interest rate borrowing 2016/17		
	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 to 20 years	0%	100%
20 years to 30 years	0%	100%
30 years to 40 years	0%	100%
40 years to 50 years	0%	100%
50 years and above	0%	100%
Maturity structure of variable interest rate borrowing 2016/17		
	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 to 20 years	0%	100%
20 years to 30 years	0%	100%
30 years to 40 years	0%	100%
40 years to 50 years	0%	100%
50 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 identifying 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. 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. Commencing in 2015, in response to the evolving regulatory regime, all three agencies have begun removing these "uplifts" with the timing of the process determined by regulatory progress at the national level. The process has been part of a wider reassessment of methodologies by each of the rating agencies. In addition to the removal of implied support, new methodologies are now taking into account additional factors, such as regulatory capital levels. In some cases, these factors have "netted" each other off, to leave underlying ratings either unchanged or little changed. A consequence of these new methodologies is that they have also lowered the importance of the (Fitch) Support and Viability ratings and have seen the (Moody's) Financial Strength rating withdrawn by the agency.

In keeping with the agencies' new methodologies, the rating element of our own credit assessment process now focuses solely on the Short and Long Term ratings of an institution. While this is the same process that has always been used for Standard & Poor's, this has been a change in the use of Fitch and Moody's ratings. It is important to stress that the other key elements to our process, namely the assessment of Rating Watch and Outlook information as well as the Credit Default Swap (CDS) overlay have not been changed.

The evolving regulatory environment, in tandem with the rating agencies' new methodologies also means that sovereign ratings are now of lesser importance in the assessment process. Where through the crisis, clients typically assigned the highest sovereign rating to their criteria, the new regulatory environment is attempting to break the link between sovereign support and domestic financial institutions. While this authority understands the changes that have taken place, it will continue to specify a minimum sovereign rating of 'AA -'. This is in relation to the fact that the underlying domestic and where appropriate, international, economic and wider political and social background will still have an influence on the ratings of a financial institution.

It is important to stress that these rating agency changes do not reflect any changes in the underlying status or credit quality of the institution. They are merely reflective of a reassessment of rating agency methodologies in light of enacted and future expected changes to the regulatory environment in which financial institutions operate. While some banks have received lower credit ratings as a result of these changes, this does not mean that they are suddenly less credit worthy than they were formerly. Rather, in the majority of cases, this mainly reflects the fact that implied sovereign government support has effectively been withdrawn from banks. They are now expected to have sufficiently strong balance sheets to be able to withstand foreseeable adverse financial circumstances without government support. In fact, in many cases, the balance sheets of banks are now much more robust than they were before the 2008 financial crisis when they had higher ratings than now. However, this is not universally applicable, leaving some entities with modestly lower ratings than they had through much of the "support" phase of the financial crisis.

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. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

Ratings will not be the sole determinant of the quality of an institution; 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 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

* Please note: the yellow colour category is for UK Government debt, or its equivalent, money market funds and collateralised deposits where the collateral is UK Government debt –see **ANNEX 3**.

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 spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Capita Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

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

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 **£7m** with individual institutions, which equates approximately to Capita's recommendation (based on average investment levels of approximately £35m).

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 Q 4 of 2016. Bank Rate forecasts for financial year ends (March) are:

- 2016/17 0.75%
- 2017/18 1.25%
- 2018/19 1.75%

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 %
2016/17	0.60
2017/18	1.25
2018/19	1.75
2019/20	2.25
2020/21	2.50
2021/22	2.75
2022/23	2.75
2023/24	3.00
Later Years	3.00

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

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	2016/17	2017/18	2018/19
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 to 100 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.

£601k is currently held in escrow in Iceland earning annual interest at a rate of c.4%.

The Council and other residual creditors have recently contracted Bevan Brittain to monitor ongoing developments in Iceland in relation to possible changes that may effect our funds held in escrow and will provide written reports on the situation as it develops.

Heritable – In September 2015 the Council received a further distribution of £60k from the Administrators taking the total received to £1.475m against our claim of £1.505m, or a recovery of 98%.

There are currently proceedings underway regarding a parent guarantee of Heritable by LBI hf. If there is no further distribution from the Heritable Administrators, the guarantee could result in potential compensation from LBI, which may result in a 100% recovery.

Kaupthing Singer & Friedlander – At the end of December 2015, 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 potential future distribution estimated for mid to late 2016.

4.6 Investment Risk Benchmarking

This Council will use an investment benchmark to assess the investment performance of its investment portfolio of 3 month LIBID.

4.7 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.

4.8 Scheme of delegation

Please see **ANNEX 5**.

4.9 Role of the Section 151 Officer

Please see **ANNEX 6**.

4.10 Policy on use of external service providers

Please see **ANNEX 7**. TMP 11

10. ANNEX

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Interest Rate Forecasts 2016 – 2019

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

Economic Background

UK. UK GDP growth rates in of 2.2% in 2013 and 2.9% in 2014 were the strongest growth rates of any G7 country; the 2014 growth rate was also the strongest UK rate since 2006 and although the 2015 growth rate is likely to be a leading rate in the G7 again, it looks likely to disappoint previous forecasts and come in at about 2%. Quarter 1 2015 was weak at +0.4% (+2.9% y/y), although there was a slight increase in quarter 2 to +0.5% before weakening again to +0.4% (+2.1% y/y) in quarter 3. The Bank of England's November Inflation Report included a forecast for growth to remain around 2.5% – 2.7% over the next three years. For this recovery, however, to become more balanced and sustainable in the longer term, it still needs to move away from dependence on consumer expenditure and the housing market to manufacturing and investment expenditure. The strong growth since 2012 has resulted in unemployment falling quickly to a current level of 5.1%.

Since the August Inflation report was issued, most worldwide economic statistics have been weak and financial markets have been particularly volatile. The November Inflation Report flagged up particular concerns for the potential impact of these factors on the UK. Bank of England Governor Mark Carney has set three criteria that need to be met before he would consider making a start on increasing Bank Rate. These criteria are patently not being met at the current time, (as he confirmed in a speech on 19 January):

- *Quarter-on-quarter GDP growth is above 0.6% i.e. using up spare capacity. This condition was met in Q2 2015, but Q3 came up short and Q4 looks likely to also fall short.*
- *Core inflation (stripping out most of the effect of decreases in oil prices), registers a concerted increase towards the MPC's 2% target. This measure was on a steadily decreasing trend since mid-2014 until November 2015 @ 1.2%. December 2015 saw a slight increase to 1.4%.*
- *Unit wage costs are on a significant increasing trend. This would imply that spare capacity for increases in employment and productivity gains are being exhausted, and that further economic growth will fuel inflationary pressures.*

The MPC has been particularly concerned that the squeeze on the disposable incomes of consumers should be reversed by wage inflation rising back above the level of CPI inflation in order to underpin a sustainable recovery. It has, therefore, been encouraging in 2015 to see wage inflation rising significantly above CPI inflation which has been around zero since February. However, it is unlikely that the MPC would start raising rates until wage inflation was expected to consistently stay over 3%, as a labour productivity growth rate of around 2% would mean that net labour unit costs would still only be rising by about 1% y/y. The Inflation Report was notably subdued in respect of the forecasts for CPI inflation; this was expected to barely get back up to the 2% target within the 2-3 year time horizon. The increase in the forecast for inflation at the three year horizon was the biggest in a decade and at the two year horizon it was the biggest since February 2013. However, the first round of falls in oil, gas and food prices in late 2014 and in the first half 2015, will fall out of the 12 month calculation of CPI during late 2015 / early 2016 but only to be followed by a second, subsequent round of falls in fuel and commodity prices which will delay a significant tick up in inflation from around zero. CPI inflation is now expected to get back to around 1% in the second half of 2016 and not get near to 2% until the second half of 2017, though the forecasts in the Report itself were for an even slower rate of increase.

However, with the price of oil having fallen further in January 2016, and with sanctions having been lifted on Iran, enabling it to sell oil freely into international markets, there could well be some further falls still to come in 2016. The price of other commodities exported by emerging countries could also have downside risk and several have seen their currencies already fall by 20-30%, (or more), over the last year. These developments could well lead the Bank of England to lower the pace of increases in inflation in its February 2016 Inflation Report. On the other hand, the start of the national living wage in April 2016 (and further staged increases until 2020), will raise wage inflation; however, it could also result in a decrease in employment so the overall inflationary impact may be muted.

Confidence is another big issue to factor into forecasting. Recent volatility in financial markets could dampen investment decision making as corporates take a more cautious view of prospects in the coming years due to international risks. This could also impact in a slowdown in increases in employment. However, consumers will be enjoying the increase in disposable incomes as a result of falling prices of fuel, food and other imports from emerging countries, so this could well feed through into an increase in consumer expenditure and demand in the UK economy, (a silver lining!). Another silver lining is that the UK will not be affected as much as some other western countries by a slowdown in demand from emerging countries, as the EU and US are our major trading partners.

There is, therefore, considerable uncertainty around how quickly pay and CPI inflation will rise in the next few years and this makes it difficult to forecast when the MPC will decide to make a start on increasing Bank Rate. There are also concerns around the fact that the central banks of the UK and US currently have few monetary policy options left to them given that central rates are near to zero and huge QE is already in place. There are, accordingly, arguments that rates ought to rise sooner and quicker, so as to have some options available for use if there was another major financial crisis in the near future. But it is unlikely that either would aggressively raise rates until they are sure that growth was securely embedded and 'noflation' was not a significant threat.

The forecast for the first increase in Bank Rate has, therefore, been pushed back progressively over the last year from Q4 2015 to Q4 2016. Increases after that are also likely to be at a much slower pace, and to much lower final levels than prevailed before 2008, as increases in Bank Rate will have a much bigger effect on heavily indebted consumers and householders than they did before 2008. There has also been an increase in momentum towards holding a referendum on membership of the EU in 2016, rather than in 2017, with Q3 2016 being the current front runner in terms of timing; this could impact on MPC considerations to hold off from a first increase until the uncertainty caused by it has passed.

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

USA. GDP growth in 2014 of 2.4% was followed by Q1 2015 growth, which was depressed by exceptionally bad winter weather, at only +0.6% (annualised). However, growth rebounded remarkably strongly in Q2 to 3.9% (annualised) before falling back to +2.0% in Q3.

Until the turmoil in financial markets in August, caused by fears about the slowdown in Chinese growth, it had been strongly expected that the Fed. would start to increase rates in September. The Fed pulled back from that first increase due to global risks which might depress US growth and put downward pressure on inflation, as well as a 20% appreciation of the dollar which has caused the Fed. to lower its growth forecasts. Although the non-farm payrolls figures for growth in employment in August and September were disappointingly weak, the October figure was stunningly strong while November was also reasonably strong (and December was outstanding); this, therefore, opened up the way for the Fed. to embark on its first increase in rates of 0.25% at its December

meeting. However, the accompanying message with this first increase was that further increases will be at a much slower rate, and to a much lower ultimate ceiling, than in previous business cycles, mirroring comments by our own MPC.

EZ. In the Eurozone, the ECB fired its big bazooka in January 2015 in unleashing a massive €1.1 trillion programme of quantitative easing to buy up high credit quality government and other debt of selected EZ countries. This programme of €60bn of monthly purchases started in March 2015 and it is intended to run initially to September 2016. At the ECB's December meeting, this programme was extended to March 2017 but was not increased in terms of the amount of monthly purchases. The ECB also cut its deposit facility rate by 10bps from -0.2% to -0.3%. This programme of monetary easing has had a limited positive effect in helping a recovery in consumer and business confidence and a start to some improvement in economic growth. GDP growth rose to 0.5% in quarter 1 2015 (1.3% y/y) but has then eased back to +0.4% (+1.6% y/y) in quarter 2 and to +0.3% (+1.6%) in quarter 3. Financial markets were disappointed by the ECB's lack of more decisive action in December and it is likely that it will need to boost its QE programme if it is to succeed in significantly improving growth in the EZ and getting inflation up from the current level of around zero to its target of 2%.

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

Portugal and Spain. The general elections in September and December respectively have opened up new areas of political risk where the previous right wing reform-focused pro-austerity mainstream political parties have lost their majority of seats. A left wing / communist anti-austerity coalition has won a majority of seats in Portugal. The general election in Spain produced a complex result where no combination of two main parties is able to form a coalition with a majority of seats. It is currently unresolved as to what administrations will result from both these situations. This has created nervousness in bond and equity markets for these countries which has the potential to spill over and impact on the whole Eurozone project.

China and Japan. Japan is causing considerable concern as the increase in sales tax in April 2014 suppressed consumer expenditure and growth. In Q2 2015 quarterly growth shrank by -0.2% after a short burst of strong growth of 1.1% during Q1, but then came back to +0.3% in Q3 after the first estimate had indicated that Japan had fallen back into recession; this would have been the fourth recession in five years. Japan has been hit hard by the downturn in China during 2015 and there are continuing concerns as to how effective efforts by the Abe government to stimulate growth, and increase the rate of inflation from near zero, are likely to prove when it has already fired the first two of its 'arrows' of reform but has dithered about firing the third, deregulation of protected and inefficient areas of the economy.

As for China, the Government has been very active during 2015 and the start of 2016, in implementing several stimulus measures to try to ensure the economy hits the growth target of about 7% for 2015. It has also sought to bring some stability after the major fall in the onshore Chinese stock market during the summer and then a second bout in January 2016. Many commentators are concerned that recent growth figures could have been massaged to hide a downturn to a lower growth figure. There are also major concerns as to the creditworthiness of much of bank lending to corporates and local government during the post 2008 credit expansion

period. Overall, China is still expected to achieve a growth figure that the EU would be envious of. Nevertheless, there are growing concerns about whether the Chinese economy could be heading for a hard landing and weak progress in rebalancing the economy from an over dependency on manufacturing and investment to consumer demand led services. There are also concerns over the volatility of the Chinese stock market, which was the precursor to falls in world financial markets in August and September and again in January 2016, which could lead to a flight to quality to bond markets. In addition, the international value of the Chinese currency has been on a steady trend of weakening and this will put further downward pressure on the currencies of emerging countries dependent for earnings on exports of their commodities.

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

The currencies of emerging countries have therefore been depressed by both this change in investors' strategy, and the consequent massive reverse cash flow, and also by the expectations of a series of central interest rate increases in the US which has caused the dollar to appreciate significantly. In turn, this has made it much more costly for emerging countries to service their dollar denominated debt at a time when their earnings from commodities are depressed by a simultaneous downturn in demand for their exports and a deterioration in the value of their currencies. There are also likely to be major issues when previously borrowed debt comes to maturity and requires refinancing at much more expensive rates.

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

CAPITA ASSET SERVICES FORWARD VIEW

Economic forecasting remains difficult with so many external influences weighing on the UK. Capita Asset Services undertook its last review of interest rate forecasts on 19 January 2016. Our Bank Rate forecasts, (and also MPC decisions), will be liable to further amendment depending on how economic data evolves over time. There is much volatility in rates and bond yields as news ebbs and flows in negative or positive ways. This latest forecast includes a first increase in Bank Rate in quarter 4 of 2016.

The overall trend in the longer term will be for gilt yields and PWLB rates to rise when economic recovery is firmly established accompanied by rising inflation and consequent increases in Bank Rate, and the eventual unwinding of QE. At some future point in time, an increase in 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 to the downside, given the number of potential headwinds that could be growing on both the international and UK scene. Only time will tell just how long this current period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.

However, the overall balance of risks to our Bank Rate forecast is probably to the downside, i.e. the first increase, and subsequent increases, may be delayed further if recovery in GDP growth, and forecasts for inflation increases, are lower than currently expected. Market expectations in January 2016, (based on short sterling), for the first Bank Rate increase are currently around quarter 1 2017.

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

- Emerging country economies, currencies and corporates destabilised by falling commodity prices and / or Fed. rate increases, causing a flight to safe havens.
- Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.
- UK economic growth and increases in inflation are weaker than we currently anticipate.
- Weak growth or recession in the UK's main trading partners - the EU and US.
- 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 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: -

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

Specified and Non-Specified Investments:**Specified Investments:**

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 Sector 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 :- <ul style="list-style-type: none"> • Debt Management Agency Deposit Facility (DMADF) • Gilts • Treasury Bills 	Defined by Regulation UK Treasury (AA-)	£7m
Bonds Issued by Multilateral Development Banks	AAA or Equivalent	£7m
Collective Investment Schemes structured as Open Ended Investment Companies (OEIC's):- <ul style="list-style-type: none"> • Government Liquidity Funds • Money Market Funds • Enhanced Money Market Funds (credit score of 1.25) • Enhanced Money Market Funds (credit score of 1.5) • Bond Funds • Gilt Funds 	AAA (Moody's MR1, Fitch MMF and S&P M).	£7m

Term deposits :- Local Authorities	Defined by Regulation (Sec 23 of the 2003 act)	£7m
Term deposits and Callable deposits :- Banks and Building Societies	In accordance with Sector's Creditworthiness Service up to 'Orange'	£7m individual institutions £10m Group limit
UK Part Nationalised Banks	In accordance with Sector's Creditworthiness Service 'Blue'	£7m individual institutions £10m Group limit
Banks and Building Societies – Forward deals up to 1 year from arrangement to maturity	In accordance with Sector's Creditworthiness Service up to 'Orange' or 'Blue'	£7m

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

Non-Specified Investments:

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	<p>Supranational Bonds greater than 1 year to maturity</p> <ul style="list-style-type: none"> 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 Royal Bank of Scotland Group
5	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

Ref	Non Specified Investment Categories	Credit Rating	Comment
6	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
7	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
8	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
9	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.
10	Property Funds – The use of these instruments can be deemed as capital expenditure and as such will be an application (spending) of capital resources. This authority will seek guidance on the status of any fund it may consider using.	N/A	Limits will be set based on levels of reserves and balances going forward and appropriate due diligence will be undertaken before investment of this type is considered.

Within categories 3, 4, and 5, 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 with Capita Asset Service'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	£7m
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	£7m
Bank (a minimum Long Term Credit Rating of A-, a minimum short term credit rating of F1 (or equivalent))	Capita 'Yellow'	3 yrs	£7m
Banks Nationalised/Part nationalised by high credit rated (sovereign rating AAA or AA+) countries	Capita 'Blue' (UK)	Specified in Guarantee	£7m
Government guarantee on ALL deposits by high credit rated (AAA sovereign rating) countries	Capita 'Blue'	Specified in Guarantee	£7m
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	£7m
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	£7m
Group Limits - Maximum investments in Institutions within the same financial group	As above for individual investment	As above for individual investment	£10m
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	£5m
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	£10m

* 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.

Approved Countries for Investment

This list is based on those countries which have sovereign ratings of AA- or higher (lowest rating from all three rating agencies) and also have banks operating in sterling markets which have credit ratings of green or above in the Capita Asset Services credit worthiness service.

AAA

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

AA+

- Finland
- U.K.*
- U.S.A.

AA

- Abu Dhabi (UAE)
- France
- Qatar

AA-

- Belgium

(Per Capita Asset Services Credit Rating List at 20/01/2016)

* 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 2016/17.

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.

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 are 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 principals, 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 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 institution's 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 31/12/2015

	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 31/12/2015			600,568 **	
	Estimated Remaining			600,568	

On the 15th March 2012, the Council received £2.554m being the majority of our deposits with the bank. The balance of our approved claim, equating to £587k, is being held in an interest bearing ESCROW account. The 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 until the date of final settlement, which is still unknown.

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			(1,475,024)	98.00
	Outstanding at 31/12/2015			30,103	
	Estimated Remaining			-	

As at the end of September the Council had received £1.475m against our claim of £1.505m, a total recovery of 98%. Negotiations are currently underway to finalise the affairs of Heritable and it is anticipated that a distribution of residual funds will be made over the next few months.

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 31/12/2015			555,670	
	Estimated Remaining			87,320	

As at the end of September the Council had received £2.620m against our claim of £3.175m. Current estimates given by the Administrator project a total recovery of 85.25% or approximately £2.707m, with the majority of repayments estimated to be received by June 2016.

Summary					
	Total Principal			7,500,000	
	Interest			335,383	
	Total of Claim			7,835,383	
	Repayments Received to date			(6,649,042)	84.86
	Outstanding at 31/12/2015			1,186,341	
	Estimated Remaining			687,888	

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

PRUDENTIAL INDICATORS – DEFINITIONS / INTERPRETATION

CIPFA's Prudential Code for Capital Finance requires local authorities to prepare Prudential Indicators of their intended capital spending plans for the forthcoming and future years. The indicators are intended to help the decision making process within an authority and must be approved by the full Council before the beginning of the financial year. The indicators are neither comparative statistics nor performance indicators. Different Councils will have different figures reflecting their history and local circumstances.

1. **Estimate of total capital expenditure to be incurred** – This summarises the Council's current plans for the total capital expenditure over the next 5 years. Details of individual schemes are contained within the capital estimate pages.
2. **Estimates of Capital Financing Summary** – Although the Prudential Code does not require this indicator, it is included so that the capital financing sources can be clearly identified.
3. **Estimated Ratio of financing costs to net revenue stream** - This indicator has been calculated as debt interest, borrowing refinancing costs, minimum revenue provision, depreciation for HRA and net of investment income and divided by the General Fund (GF) budget requirement for the GF element of costs and the total of HRA income for the HRA costs. For GF Account, the indicator has been calculated gross of government support in the form of RSG for the proportion of capital expenditure funded from supported level of borrowing.
4. **Incremental Impact on Band D Council Tax** – This represents debt charges i.e. the interest and Minimum Revenue Provision (Principal repayments) of all General Fund borrowing, gross of government support in the form of RSG. This indicator is calculated by calculating the debt charge based on the proposed capital programme and dividing the result by the tax base for Council Tax.
5. **Incremental Impact on average weekly housing rent** – For HRA capital programme, the proposed ALMO borrowing is 100% supported by government grant with the balance of the capital expenditure funded from the Major Repairs Reserve (Grant/Subsidy), revenue contributions and capital receipts and therefore will not impact the indicator for HRA.
6. **Capital Financing Requirement** – This represents the Council's underlying need to borrow to finance historic capital expenditure and is derived by aggregating specified items from the Council's balance sheet. The actual **net borrowing** is lower than this because of the reserve part of capital receipts accumulated until 31st March 2004.
7. **Actual Net Borrowing** – This is a key indicator and Section 3 of the Local Government Act 2003 requires the Council to ensure that over the medium term, the net borrowing (actual long term borrowing less temporary investments) does not exceed the sum of Capital Financing Requirement in the preceding year plus estimates of any additional capital financing requirement for the current and next two financial years.
8. **Authorised Borrowing Limit for external debt** - This indicator represents the maximum amount the Council may borrow at any point in time in the year and has to be set at a level the Council considers is **prudent**. It allows for uncertain cash flow movements and borrowing in advance for future requirements. Although the Council does not currently have any finance lease liabilities, a limit has been separately identified for potential future leasing liabilities.

The recommended authorised limits for external debt are gross of investments and are consistent with the Council's current commitments, existing plans and the current treasury management policy and strategy. The authorised limit determined for 2016- 17 is the statutory limit determined under section 3(1) of the Local Government Act 2003.

9. Operational Boundary for external debt - The proposed operational boundary for external debt is calculated on the same estimates as the authorised limit but reflects estimates of the most likely, prudent but not worst case scenario, without the additional headroom included within the authorised limit to allow for example for unusual cash movements, and equates to the maximum of external debt projected by this estimate. Within the operational boundary, figures for borrowing and other long term liabilities are separately identified.

10. Treasury Management – these indicators form part of the treasury management strategy and policy statement approved by the Council each year before the beginning of the financial year. The main indicators are:

(a) The adoption of **CIPFA Code of Practice for Treasury Management**, which the Council adopted before the current Prudential System was introduced.

(b) **Interest Rate Exposure** - The approved Treasury Policy Statement and Strategy contains upper and lower limits for fixed and variable interest rate exposure for net outstanding principal sums.

(c) **Maturity Structure of Borrowing** – The approved treasury management strategy also sets out the maturity structure of the Council's borrowing to ensure the Council is not exposed to risks of having to refinance large level of debt at a time in future when interest rates may be volatile or uncertain.

(d) **Investments longer than 364 days** – The approved treasury management strategy includes a limit of £2m for investments maturing beyond 364 days.