



Rutland County Council

Treasury Management Strategy 2018 - 19



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1 INTRODUCTION

1.1 Background to Treasury Management

1.1.1 The Council is required to operate a balanced budget, which 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 to meet day-to-day running costs and planned capital expenditure. Any surplus monies are invested in counterparties or instruments commensurate with the Council's risk appetite, providing adequate liquidity initially before considering investment return.

1.1.2 The second main function of the treasury management service is the funding of the Council's capital plans as set out in the Budget and Capital Investment Strategy (CIS). 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, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

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

1.2 Reporting Requirements

1.2.1 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.

1.2.2 The Treasury Management Strategy should be read in conjunction with the Council's CIS which covers:

- what is capital expenditure/investment and why we incur it;
- the Council's overall capital objectives, priorities and plans;
- how the Council's capital expenditure/investment will be funded/resourced;
- how the Council's capital expenditure/investment plans will be appraised including the Council's commercial investment policy;
- how capital plans will be approved, monitored and reported upon; and

- the skills and knowledge required to deliver the capital plans.

1.2.3 **Prudential and treasury indicators and treasury strategy** (this report) -
The first and most important report covers:

- the capital plans (including prudential indicators) as derived through the budget and CIS;
- a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);
- the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy for treasury investments (the parameters on how investments are to be managed).

1.2.4 **A mid-year treasury management report** – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether any policies require revision. In addition, this Council will receive an update on investment returns.

1.2.5 **An annual treasury report** – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

1.2.6 **Scrutiny** - The above reports are required to be adequately scrutinised before being recommended to Council. This role is undertaken by Cabinet and reports are also made available to Scrutiny Panels.

1.3 **Treasury Management Strategy for 2018/19**

1.3.1 The strategy for 2018/19 covers two main areas.

Capital Issues

- the capital plans and the prudential indicators;
- the minimum revenue provision (MRP) policy.

Treasury Management Issues

- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;

- the investment strategy (for treasury investments);
 - creditworthiness policy; and
 - the policy on use of external service providers.
- 1.3.2 These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, CLG MRP Guidance, the CIPFA Treasury Management Code and CLG Investment Guidance.
- 1.4 **Training**
- 1.4.1 The CIPFA Code requires the s151 Officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. Training from the Council's external treasury advisors was offered previously to Scrutiny when the Strategy was discussed in 2015/16. Further training will be arranged as required.
- 1.4.2 The training needs of treasury management officers and members are periodically reviewed.
- 1.5 **Treasury Management Consultants**
- 1.5.1 The Council uses Link Asset Services Treasury Solutions (during the current planning period Capita Asset Service has been transferred to The Link Group) as its external treasury management advisors.
- 1.5.2 The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.
- 1.5.3 It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

2 THE CAPITAL PRUDENTIAL INDICATORS 2018/19 – 2020/21

2.1 Capital Expenditure

2.1.1 The Council's capital expenditure plans as set out in the budget are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

2.1.2 The capital expenditure prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. As at 1 April 2018 the Council estimates that it will have capital projects approved of £30.938m. The details of this are shown in Budget Report (Report No: 214/2017)

2.1.3 The table below shows the indicative spend profile of approved capital projects, completed capital projects in 2016/17 and projects included in the 2018/19 Budget. Whilst the Council may have approved a project in 18/19 spending may not occur until 19/20. Members are asked to approve the capital expenditure forecasts:

| Estimated Capital Programme | Actuals | Projects | Projects | Projects | Projects |
|-----------------------------|--------------|---------------|---------------|--------------|--------------|
| | 2016/17 | 2017/18 | 2018/19 | 2019/20 | 2020/21 |
| | £000 | £000 | £000 | £000 | £000 |
| Total Projects | 5,338 | 10,924 | 14,252 | 5,713 | 2,806 |

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

| Estimated Capital Programme | Actuals | Projects | Projects | Projects | Projects |
|-----------------------------|----------------|-----------------|-----------------|----------------|----------------|
| | 2016/17 | 2017/18 | 2018/19 | 2019/20 | 2020/21 |
| | £000 | £000 | £000 | £000 | £000 |
| Grant | (3,781) | (8,983) | (1,948) | (3,497) | (2,041) |
| Prudential Borrowing | (508) | (602) | (11,600) | 0 | 0 |
| Salix Loan | (420) | 0 | 0 | 0 | 0 |
| Capital Receipts | (274) | (438) | (504) | (872) | (306) |
| RCCO | (186) | 0 | 0 | 0 | 0 |
| Oakhams North | (1) | (256) | (200) | 0 | 0 |
| S106/CIL | (168) | (645) | 0 | (1,344) | (459) |
| Total Funding | (5,338) | (10,924) | (14,252) | (5,713) | (2,806) |

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

2.2.1 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 indebtedness and its underlying borrowing need. Any capital expenditure above, which has not

immediately been paid for, will increase the CFR.

2.2.2 The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each assets life, and so charges the economic consumption of capital assets as they are used.

2.2.3 The Council is asked to approve the CFR projections below:

| | 2016/17 Actual £000 | 2017/18 Estimate £000 | 2018/19 Estimate £000 | 2019/20 Estimate £000 | 2020/21 Estimate £000 |
|--|---------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| Capital Financing Requirement | | | | | |
| CFR – 1 Apr | 22,723 | 22,335 | 22,040 | 33,011 | 32,382 |
| Movement in Year | (388) | (295) | 10,971 | (629) | (629) |
| CFR – 31Mar | 22,335 | 22,040 | 33,011 | 32,382 | 31,753 |
| Movement in CFR represented by | | | | | |
| Net financing need for the year (above) | 928 | 602 | 11,600 | - | - |
| Less MRP/VRP and other financing movements | (1,316) | (897) | (629) | (629) | (629) |
| Movement in CFR | (388) | (295) | 10,971 | (629) | (629) |

2.3 Core Funds and Expected Investment Balances

2.3.1 The application of resources (capital receipts, reserves etc) to either finance capital expenditure or 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 cash flow balances.

| Year End Resources | 2016/17 Actual £000 | 2017/18 Estimate £000 | 2018/19 Estimate £000 | 2019/20 Estimate £000 | 2020/21 Estimate £000 |
|-----------------------------|---------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| Fund balances / reserves | 25,241 | 23,989 | 20,685 | 18,347 | 17,294 |
| Capital receipts | 1,570 | 1,346 | 1,011 | 295 | 38 |
| Provisions | 265 | 265 | 265 | 265 | 265 |
| Total core funds | 27,076 | 25,600 | 21,961 | 18,907 | 17,597 |
| Working capital* | (2,000) | (2,000) | (2,000) | (2,000) | (2,000) |
| New external borrowing** | - | - | (5,000) | | |
| Expected investments | 25,076 | 23,600 | 14,961 | 16,907 | 15,597 |

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

**Prudential borrowing in line with CIS.

3 BORROWING

3.1 Borrowing objectives

3.1.1 Councils borrow to fund capital expenditure or refinance/reschedule existing borrowing e.g. replace one loan with one at a lower rate. There are 7 types of borrowing that may be considered under this strategy.

- Borrowing to fund a scheme that will reduce the Council's ongoing revenue costs in future years, or avoid increased costs in future years.
- Borrowing to fund the purchase of essential vehicles plant and equipment in order to maintain Council functions.
- Borrowing in advance of anticipated receipts to enable the Council to invest in capital expenditure before it has the income to fund the investment.
- Borrowing to enable the Council to fund a larger capital programme than it is able to do using Government grant and self-financed borrowing.
- Borrowing to fund an overspend on a large-scale capital scheme that would otherwise have to be funded from a revenue contribution to capital outlay, with major impact on the Council's revenue budget.
- Borrowing to fund a capital development which the Council believes is so essential to the transformation of Rutland, and able, within the context of setting a robust budget and medium term financial strategy, to allocate to the development a specific, ongoing, relatively secure source of funding that can clearly be seen to be able to cover the cost of debt financing for the project over its expected life.
- Borrowing to reschedule existing borrowing i.e. replace existing loans with others.

3.1.2 Effectively, the Council works out its capital expenditure plans and then calculates how much it needs to borrow having considered whether it should fund capital expenditure using other options. The Council's objectives are to:

- avoid external borrowing as far as possible (i.e. use other sources of funding first where possible) unless that borrowing yields income or deliver savings beyond the cost of borrowing;
- repay borrowing early if this is financially prudent and viable;
- reduce its borrowing charge if this represents value for money;
- ensure any new borrowing is affordable; and
- work within prudential indicator limits.

3.2 Current borrowing portfolio

3.2.1 The Council currently has loans outstanding of £22.436m of which £21.386m

are long term loans with the Public Works Loans Board (PWLB). PWLB is managed as part of the UK Debt Management Office, which is a HM Treasury Executive Agency. The remainder is a £630k Local Enterprise Partnership interest free loan which matures in 2023, and an interest free Salix loan of £420k repayable in 2020. Included within the £21.386m is £8.232m of debt that was inherited from Leicestershire in the Local Government Re-organisation in 1997.

- 3.2.2 The last time the Council actually borrowed from the PWLB was in 2008 to contribute towards funding the Oakham bypass, the value of this loan was £4m.
- 3.2.3 All PWLB loans have been borrowed on a maturity basis. Interest payments will be made every six months on equal instalments throughout the term of the loan, with the principal being re-paid on the maturity date.
- 3.2.4 The external debt projections are shown 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.

| Year End Resources | 2016/17 Actual £000 | 2017/18 Estimate £000 | 2018/19 Estimate £000 | 2019/20 Estimate £000 | 2020/21 Estimate £000 |
|-------------------------------|------------------------------------|--------------------------------------|--------------------------------------|--------------------------------------|--------------------------------------|
| External Debt | | | | | |
| Debt - 1 April | 22,016 | 22,436 | 22,394 | 27,310 | 27,226 |
| Expected Change in Debt | 420 | (42) | 4,916 | (84) | (84) |
| Actual Gross Debt 31 March | 22,436 | 22,394 | 27,310 | 27,226 | 27,142 |
| Capital Financing Requirement | 22,335 | 22,040 | 32,571 | 31,942 | 31,313 |
| Under / (Over) Borrowing* | (101) | (354) | 5,261 | 4,716 | 4,171 |

*Under Borrowing Position explained in Treasury Management Strategy 2017/18 (41/2017)

- 3.2.5 A key prudential indicator is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR. This indicator compares debt to the underlying need to borrow (measured by the CFR) to show that the borrowing is being used only to finance capital expenditure.
- 3.2.6 The s151 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.

3.3 Treasury Indicators: Limits to Borrowing Activity

3.3.1 **The operational boundary** - This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

| Operational boundary | 2017/18 Estimate £000 | 2018/19 Estimate £000 | 2019/20 Estimate £000 | 2020/21 Estimate £000 |
|-----------------------------|--------------------------------------|--------------------------------------|--------------------------------------|--------------------------------------|
| Debt | 23,000 | 28,000 | 28,000 | 28,000 |
| Other long term liabilities | - | - | - | - |
| Total | 23,000 | 28,000 | 28,000 | 28,000 |

3.3.2 The table above shows that Council are being asked to approve an operational boundary of £28.0m. This has been calculated by taking the existing debt level (£22m) and allowing head room for additional borrowing in line with the CIS.

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

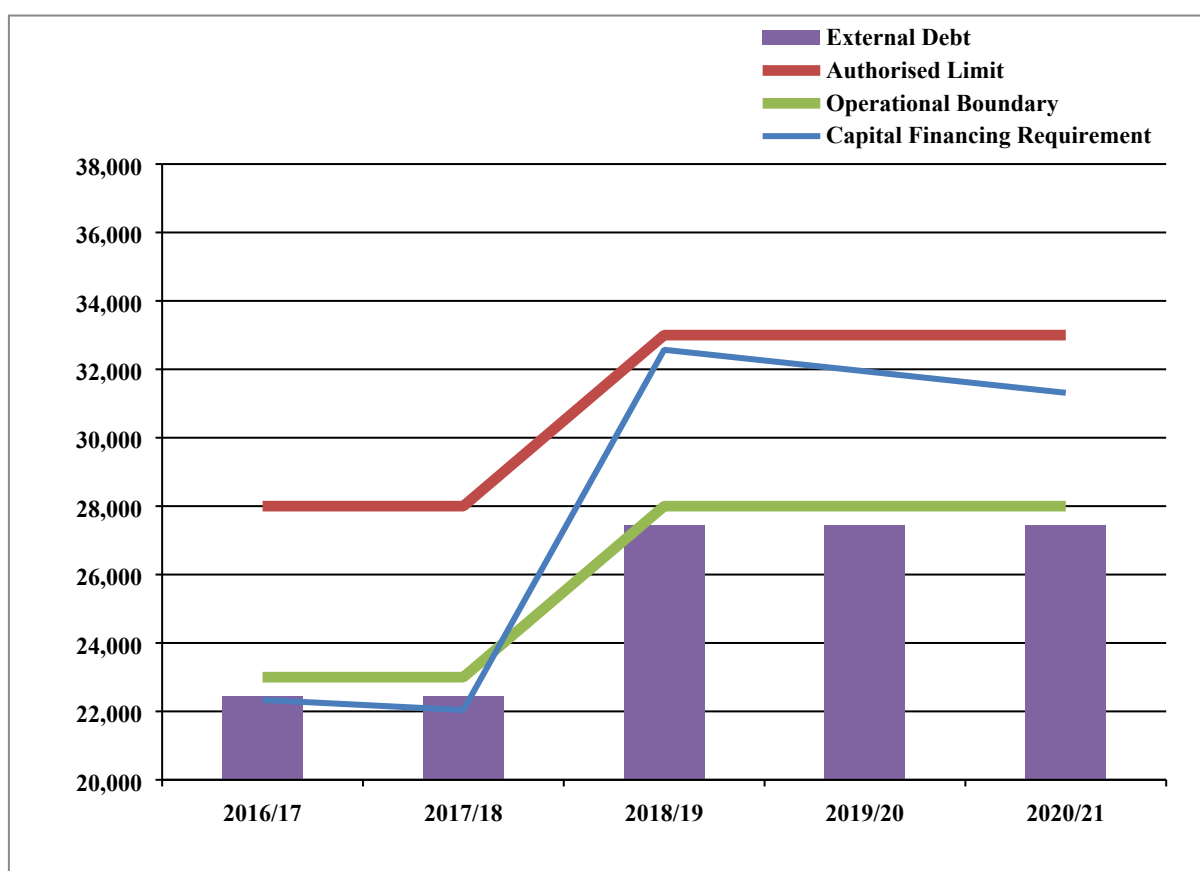
3.3.4 This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

3.3.5 The Council is asked to approve the following authorised limit:

| Authorised limit | 2017/18 Estimate £000 | 2018/19 Estimate £000 | 2019/20 Estimate £000 | 2020/21 Estimate £000 |
|-----------------------------|--------------------------------------|--------------------------------------|--------------------------------------|--------------------------------------|
| Debt | 28,000 | 33,000 | 33,000 | 33,000 |
| Other long term liabilities | - | - | - | - |
| Total | 28,000 | 33,000 | 33,000 | 33,000 |

3.3.6 The authorised limit has been increased to facilitate delivery of the CIS and other major projects in the pipeline and to support temporary cash flows which may, in the short term, push the Council above the operational boundary.

3.3.7 The graph below shows where we currently are against all of the borrowing prudential indicators.



3.4 Prospects for Interest Rates – Commentary By Link Asset Services

3.4.1 Link Asset Services have provided a view on interest rates as per the table below.

| | Dec 2017 % | Mar 2018 % | Jun 2018 % | Sep 2018 % | Dec 2018 % | Mar 2019 % | Jun 2019 % | Sep 2019 % | Dec 2019 % | Mar 2020 % |
|----------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|
| Bank Rate | 0.50 | 0.50 | 0.50 | 0.50 | 0.75 | 0.75 | 0.75 | 0.75 | 1.00 | 1.00 |
| 3 Month LIBID | 0.40 | 0.40 | 0.40 | 0.40 | 0.60 | 0.60 | 0.60 | 0.70 | 0.90 | 0.90 |
| 6 Month LIBID | 0.45 | 0.50 | 0.50 | 0.60 | 0.80 | 0.80 | 0.80 | 0.90 | 1.00 | 1.00 |
| 12 Month LIBID | 0.65 | 0.80 | 0.80 | 0.90 | 1.00 | 1.00 | 1.10 | 1.10 | 1.30 | 1.30 |
| 5 Yr PWLB | 1.50 | 1.60 | 1.60 | 1.70 | 1.80 | 1.80 | 1.90 | 1.90 | 2.00 | 2.10 |
| 10 Yr PWLB | 2.10 | 2.20 | 2.30 | 2.40 | 2.40 | 2.50 | 2.60 | 2.60 | 2.70 | 2.70 |
| 25 Yr PWLB | 2.80 | 2.90 | 3.00 | 3.00 | 3.10 | 3.10 | 3.20 | 3.20 | 3.30 | 3.40 |
| 50 Yr PWLB | 2.50 | 2.60 | 2.70 | 2.80 | 2.90 | 2.90 | 3.00 | 3.00 | 3.10 | 3.20 |

Interest rate forecast provided by Link Asset Services on 8 November 2017

- 3.4.2 As expected, the Monetary Policy Committee (MPC) delivered a 0.25% increase in Bank Rate at its meeting on 2 November. This removed the emergency cut in August 2016 after the EU referendum. The MPC also gave forward guidance that they expected to increase Bank rate only twice more by 0.25% by 2020 to end at 1.00%. The Link Asset Services forecast as above includes increases in Bank Rate of 0.25% in November 2018, November 2019 and August 2020.
- 3.4.3 The overall longer run trend is for gilt yields and PWLB rates to rise, albeit gently. It has long been expected, that at some point, there would be a more protracted move from bonds to equities after a historic long-term trend, over about the last 25 years, of falling bond yields. The action of central banks since the financial crash of 2008, in implementing substantial Quantitative Easing, added further impetus to this downward trend in bond yields and rising bond prices. Quantitative Easing has also directly led to a rise in equity values as investors searched for higher returns and took on riskier assets. The sharp rise in bond yields since the US Presidential election in November 2016 has called into question whether the previous trend may go into reverse, especially now the Fed. has taken the lead in reversing monetary policy by starting, in October 2017, a policy of not fully reinvesting proceeds from bonds that it holds when they mature.
- 3.4.4 Until 2015, monetary policy was focused on providing stimulus to economic growth but has since started to refocus on countering the threat of rising inflationary pressures as stronger economic growth becomes more firmly established. The Fed. has started raising interest rates and this trend is expected to continue during 2018 and 2019. These increases will make holding US bonds much less attractive and cause their prices to fall, and therefore bond yields to rise. Rising bond yields in the US are likely to exert some upward pressure on bond yields in the UK and other developed economies. However, the degree of that upward pressure is likely to be dampened by how strong or weak the prospects for economic growth and rising inflation are in each country, and on the degree of progress towards the reversal of monetary policy away from quantitative easing and other credit stimulus measures.
- 3.4.5 From time to time, gilt yields – and therefore PWLB rates - can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis and emerging market developments. Such volatility could occur at any time during the forecast period.
- 3.4.6 Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The above forecasts (and MPC decisions) will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.
- 3.4.7 The overall balance of risks to economic recovery in the UK is probably to

the downside, particularly with the current level of uncertainty over the final terms of Brexit. Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- Bank of England monetary policy takes action too quickly over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- Geopolitical risks, especially North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.
- A resurgence of the Eurozone sovereign debt crisis, possibly Italy, due to its high level of government debt, low rate of economic growth and vulnerable banking system.
- Weak capitalisation of some European banks.
- The result of the October 2017 Austrian general election is likely to result in a strongly anti-immigrant coalition government. In addition, the new Czech prime minister is expected to be Andrej Babis who is strongly against EU migrant quotas and refugee policies. Both developments could provide major impetus to other, particularly former Communist bloc countries, to coalesce to create a major block to progress on EU integration and centralisation of EU policy. This, in turn, could spill over into impacting the Euro, EU financial policy and financial markets.
- Rising protectionism under President Trump
- A sharp Chinese downturn and its impact on emerging market countries

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

- The Bank of England is too slow in its pace and strength of increases in Bank Rate and, therefore, allows inflation pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.
- UK inflation returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.
- The Fed causing a sudden shock in financial markets through misjudging the pace and strength of increases in its Fed. Funds Rate and in the pace and strength of reversal of Quantitative Easing, which then leads to a fundamental reassessment by investors of the relative risks of holding bonds, as opposed to equities. This could lead to a major flight from bonds to equities and a sharp increase in bond yields in the US, which could then spill over into impacting bond yields around the world.

3.4.9 Investment and borrowing rates

- Investment returns are likely to remain low during 2018/19 but to be on a gently rising trend over the next few years.
- Borrowing interest rates increased sharply after the result of the general election in June and then also after the September MPC meeting when financial markets reacted by accelerating their expectations for the timing of Bank Rate increases. Apart from that, there has been little general trend in rates during the current financial year. 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 the future when authorities may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt;
- There will remain a cost of carry to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost – the difference between borrowing costs and investment returns.

3.5 **Borrowing Strategy**

- 3.5.1 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.
- 3.5.2 Against this background and the risks within the economic forecast, caution will be adopted with the 2018/19 treasury operations. The Assistant Director - Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:
- 3.5.3 If the Council were to borrow then the Assistant Director – Finance would monitor the market to ensure that the borrowing was undertaken at the optimum time for the Council. If the Assistant Director thought rates would fall then they may choose to hold off long term borrowing. If they thought rates would rise then they may choose to borrow in advance of need (see section 3.6) to ensure borrowing is secured at a lower rate.
- 3.5.4 Any decisions will be reported to the appropriate decision making body at the next available opportunity.

3.6 **Policy on Borrowing in Advance of Need**

- 3.6.1 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. The Council has some flexibility to borrow funds in advance of need for use in future years. The Section 151 Officer may do this under delegated power where,

for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or meet budgetary constraints. Whilst the Section 151 Officer will adopt a cautious approach to any such borrowing, where there is a clear business case for doing so borrowing may be undertaken to fund the approved capital programme or to fund future debt maturities.

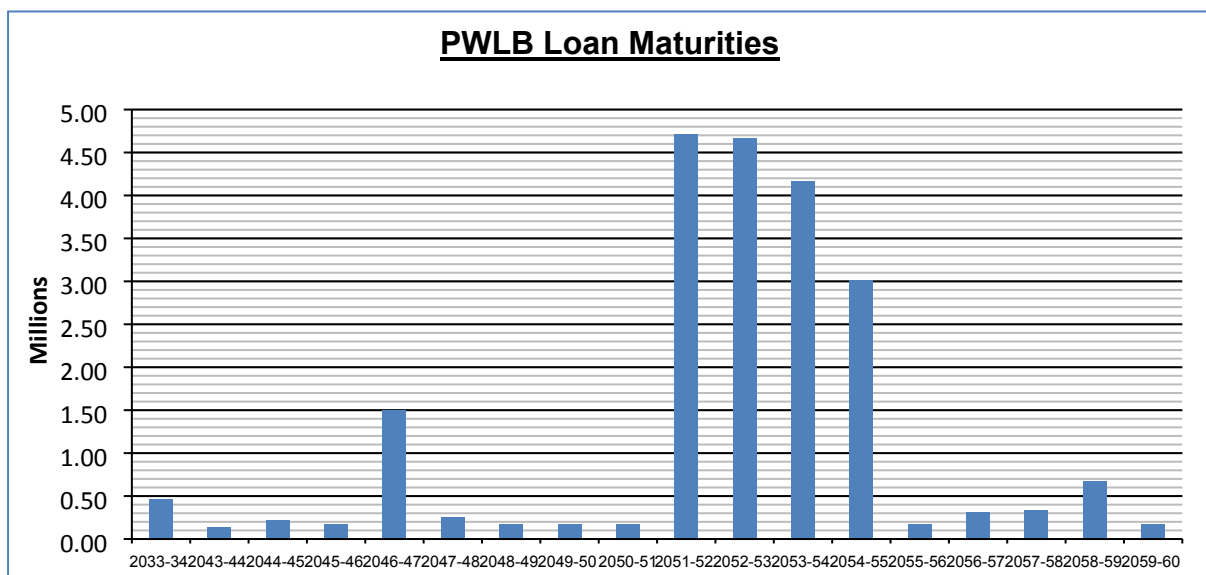
3.6.2 Borrowing in advance will be made within the constraints that:

- It will be limited to no more than 50% of the expected increase in borrowing need (CFR) over the three year planning period; and
- The authority would not look to borrow more than 18 months in advance of need.

3.6.3 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.

3.7 Debt Repayment and rescheduling

3.7.1 The table below demonstrates when PWLB debt is due to be repaid.



3.7.2 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).

3.7.3 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).
- 3.7.4 Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.
- 3.7.5 All rescheduling will be reported to the Cabinet at the earliest meeting following its action.
- 3.8 **Municipal Bond Agency**
- 3.8.1 It is possible that the Municipal Bond Agency will be offering loans to local authorities in the future. The Agency hopes that the borrowing rates will be lower than those offered by the Public Works Loan Board (PWLB). The Council may make use of this new source of borrowing as and when appropriate.

4 ANNUAL INVESTMENT STRATEGY

4.1 Investment overview

4.1.1 The Council receives substantial income from council tax, business rates and central government. The majority of council tax and business rates payments are received between April and January, with expenditure being fairly static throughout the year.

4.1.2 At any point of time in the year, the Council can have between £19m - £32m available to invest. The estimated level of investments at year end based on the current cash flow calculations and for the next few years is shown below. The Total investments at Quarter 2 show the estimated level of investment at the mid-point during the financial year.

| | 2017/18 Actual £000 | 2017/18 Forecast £000 | 2018/19 Estimate £000 | 2019/20 Estimate £000 | 2020/21 Estimate £000 |
|--------------------------------|---------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| Total Investments at Quarter 2 | 31,014 | | 18,000 | 12,100 | 8,500 |
| Total Investments at 31 March | | 25,000 | 13,500 | 8,200 | 6,100 |

4.1.3 The Council will invest surplus money in various ways to get a return on balances thus generating extra income.

4.2 Investment policy objectives

4.2.1 The Council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code").

4.2.2 This policy only covers treasury investments. The objectives of non-treasury investments are covered in the CIS.

4.2.3 The Council's investment strategy primary objectives, in order of importance are:

- safeguarding the re-payment of the principal and interest of its investments on time – losing any funds like in the case of Icelandic banks would be very significant in this financial climate;
- adequate liquidity – the Council does not want to run short of money so it cannot pay its bills or does not have money available to make investments in capital expenditure;
- maximising the investment return – this is clearly important but the Council does not want to maximise returns at the expense of the first two objectives.

4.2.4 These objectives filter through this strategy.

4.3 **Investment rules**

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

4.3.2 The Council engages with its advisors to monitor markets to support the ratings systems which ensures the Council is aware of the standing of the bank / building society.

4.3.3 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.

4.4 **Creditworthiness policy**

4.4.1 The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle the Council will ensure:

- It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the Specified and Non-Specified investment sections below.
- It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

4.4.2 The Section 151 Officer will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. This criteria is separate to that which chooses Specified and Non-Specified investments as it provides an overall pool of counterparties considered high quality the Council may use rather than defining what its investments are.

4.4.3 The rating criteria use the lowest common denominator method of selecting counterparties and applying limits. This means that the application of the Council's minimum criteria will apply to the lowest available rating for any institution. For instance if an institution is rated by two agencies, one meets the Council's criteria, the other does not, the institution will fall outside the lending criteria. This is in compliance with a CIPFA Treasury Management Panel recommendation in March 2009.

4.4.4 Credit rating information is supplied by our treasury consultants daily on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing. For instance a negative rating watch applying to counterparty will be suspended from use, with all others being reviewed in light of market.

4.4.5 The criteria for providing a pool of high quality investment counterparties (both Specified and Non-specified investments) is shown in the table below.

| | Money and / or % Limit | Time Limit |
|--|------------------------|------------|
| Banks & Rated Building Societies (Upper Limit) | £5m | 3 yrs |
| Banks & Rated Building Societies (Middle) | £5m | 364 Days |
| Banks (Council Banker) | £5m* | 3 yrs* |
| Debt Management Account Deposit Facility managed by the DMO (Debt Management Office) | £5m | 364 Days |
| Local authorities | £5m | 364 Days |
| Central Government Issued Gilts & Bonds | £5m | 3 years |
| Building Societies (not on rating list) | £1m | 6 months |
| Money Market Funds | £5m | 364 Days |
| Property Funds | £2m | ** |

*Limits will align to those of the banks

** No time limit as investment would need to be left to mature to ensure no loss on investments.

4.4.6 **Country and Sector Considerations** - Due care will be taken to consider the country, group and sector exposure of the Council's investments. In part the country selection will be chosen by the credit rating of the Sovereign state in the table above. In addition to this:

- no more than 10% (of the total investment portfolio) will be placed with any non-UK country at any time;
- limits in place above will apply to Group companies;
- Capita Asset Services limits will be monitored regularly for appropriateness.

4.4.7 **Economic Investment Considerations** - Expectations on shorter-term interest rates, on which investment decisions are based, show likelihood of the current 0.50% Bank Rate remaining for the near future. The Council's investment decisions are based on comparisons between the rises priced into market rates against the Council's and advisers own forecasts.

4.4.8 The criteria for choosing counterparties set out above provide a sound approach to investment in “normal” market circumstances. Whilst Members are asked to approve this base criteria above, under the exceptional current market conditions the Section 151 Officer may temporarily restrict further investment activity to those counterparties considered of higher credit quality than the minimum criteria set out for approval. These restrictions will remain in place until the banking system returns to “normal” conditions. Similarly the time periods for investments will be restricted.

4.5 Investment approach

4.5.1 As per our overall objectives, we ensure that these surplus balances are managed in a way to maximise the income potential whilst having regard to security risk.

4.5.2 The Council’s approach is influenced by numerous issues:

- Cash flow – when will the Council need the funds to pay general running costs of the Council or fund capital investment activity
- The vehicles allowed for investment as outlined in this strategy
- The rate of return on offer - Bank Rate is forecast to stay flat at 0.50% until quarter 4 2018 and not to rise above 1.25% by Quarter 1 2021.

4.5.3 Our focus is on traditional investments e.g. deposits for up to 12 month period – this is in line with the advice from our consultants (Link Asset Services). We will also consider longer term options (Government bonds, Property Funds etc) once the position on Commercial Investments is clear. For example, placing funds in long term investments may not be an option depending on capital expenditure and investment plans.

4.6 Investment returns expectations and benchmarking

4.6.1 Over the medium term, the Council expects to make returns as shown in the table below. The investment interest income forecast is:

| 2017/18 £000 | 2018/19 £000 | 2019/20 £000 | 2020/21 £000 | 2021/22 £000 |
|-----------------|-----------------|-----------------|-----------------|-----------------|
| 220 | 210 | 170 | 155 | 155 |

4.6.2 Security - The Council’s maximum security risk benchmark for the current portfolio, when compared to these historic default tables, is:

- 0.10% historic risk of default when compared to the whole portfolio.

4.6.3 Liquidity – in respect of this area the Council seeks to maintain:

- Bank overdraft - £0m

- Liquid short term deposits of at least £1m available with a week's notice.
- 4.6.4 Yield - local measures of yield benchmarks
- Investments – internal returns above the 6 month LIBOR rate
- 4.7 **End of Year Investment Report**
- 4.7.1 At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

5 THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2018/19 – 2020/21 AND MRP STATEMENT

5.1 Capital Expenditure

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

| Capital Expenditure | 2016/17 Actual £000 | 2017/18 Estimate £000 | 2018/19 Estimate £000 | 2019/20 Estimate £000 | 2020/21 Estimate £000 |
|---------------------|---------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| Total | 5,338 | 10,924 | 14,252 | 5,713 | 2,806 |

5.2 Minimum Revenue Provision Policy

- 5.2.1 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 - MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

- 5.2.2 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 The Council will reduce on a straight line basis over 50 years.
- From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be (either / and):
 - a) Asset life method – MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction);
 - b) Depreciation method – MRP will follow standard depreciation accounting procedures.

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

5.3 Affordability Prudential Indicators

- 5.3.1 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:

- 5.3.2 **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.

| | £000 | |
|--|---------|---|
| Capital Financing Costs | 1.644 | |
| Interest Receivable | (0.210) | |
| | 1.434 | A |
| Revenue Stream | | |
| Government Grants | 4.269 | |
| Retained Business Rates | 4.958 | |
| Council Tax | 24.563 | |
| | 33.791 | B |
| Ratio (A divided by B as a percentage) | 4.24% | |

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

- 5.3.4 **Incremental Impact of Capital Investment Decisions on Band D 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 are not published over a three year period

| | 2016/17 Actual £ | 2017/18 Estimate £ | 2018/19 Estimate £ | 2019/20 Estimate £ | 2020/21 Estimate £ |
|---------------------------------|------------------------|--------------------------|--------------------------|--------------------------|--------------------------|
| Council Tax - Band D | 0.10% | 0.34% | 0.21% | 3.84% | 0.00% |

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

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments;

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

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

| | 2018/19 | 2020/21 | 2021/22 |
|--|--------------|--------------|--------------|
| Interest rate exposures | | | |
| | Upper | Upper | Upper |
| Limits on fixed interest rates | £25.000m | £25.000m | £25.000m |
| Limits on variable interest rates | £7.500m | £7.500m | £7.500m |
| Maturity structure of fixed interest rate borrowing 2018/19 | | | |
| | | Upper | Lower |
| Under 12 months | | 25% | 0% |
| 12 months to 2 years | | 25% | 0% |
| 2 years to 5 years | | 20% | 0% |
| 5 years to 10 years | | 20% | 0% |
| 10 years and above | | 100% | 0% |
| Maximum principal sums invested > 364 days | | 25% | |

ANNEXE A1 - PUBLIC WORKS LOAN BOARD (PWLB) DEBT ANALYSIS

The table below shows the number of outstanding loans with the PWLB, the maturity date, Principal outstanding, interest rate and the premium payable if the council was to settle the outstanding loan.

| PWLB 2017-18 Loan Repayment Premiums as at 12-Dec-2017 | | | | | |
|---|-------------------|----------------------|--------------------------|------------------------|-------------------|
| Loan Reference | Start Date | Maturity Date | Principal Balance | Interest Rate % | Premium |
| 461697 | 27-Mar-1987 | 31-Dec-2043 | 132,529.13 | 9.000 | 201,316 |
| 461698 | 27-Mar-1987 | 31-Dec-2044 | 212,550.13 | 9.000 | 332,610 |
| 461699 | 27-Mar-1987 | 31-Dec-2045 | 163,500.10 | 9.000 | 264,632 |
| 461700 | 27-Mar-1987 | 31-Dec-2046 | 196,200.12 | 9.000 | 327,207 |
| 476645 | 30-Nov-1995 | 28-Jul-2053 | 163,500.10 | 8.000 | 284,175 |
| 476646 | 30-Nov-1995 | 28-Jul-2054 | 163,500.10 | 8.000 | 291,943 |
| 476647 | 30-Nov-1995 | 28-Jul-2055 | 163,500.10 | 8.000 | 298,778 |
| 476842 | 21-Dec-1995 | 13-Dec-2052 | 163,500.10 | 7.875 | 273,245 |
| 476843 | 21-Dec-1995 | 13-Dec-2051 | 163,500.10 | 7.875 | 265,695 |
| 476844 | 21-Dec-1995 | 13-Dec-2050 | 163,500.10 | 7.875 | 258,982 |
| 477672 | 05-Aug-1996 | 08-May-2048 | 163,500.10 | 8.375 | 259,006 |
| 477673 | 05-Aug-1996 | 08-May-2049 | 163,500.10 | 8.375 | 267,042 |
| 478210 | 26-Sep-1996 | 25-Sep-2047 | 217,138.76 | 8.125 | 325,907 |
| 478211 | 26-Sep-1996 | 25-Sep-2056 | 163,500.10 | 8.125 | 313,485 |
| 478214 | 26-Sep-1996 | 25-Sep-2047 | 28,111.39 | 8.125 | 42,193 |
| 479404 | 21-May-1997 | 08-May-2057 | 327,000.20 | 7.125 | 539,884 |
| 479405 | 21-May-1997 | 08-May-2056 | 147,150.09 | 7.125 | 236,735 |
| 481709 | 13-Oct-1998 | 25-Sep-2058 | 163,500.10 | 4.625 | 153,876 |
| 482002 | 14-Jan-1999 | 25-Sep-2058 | 320,460.20 | 4.375 | 277,314 |
| 482386 | 30-Mar-1999 | 25-Mar-2059 | 23,271.98 | 4.625 | 22,208 |
| 482875 | 08-Nov-1999 | 25-Mar-2059 | 163,500.10 | 4.500 | 149,764 |
| 483562 | 18-Nov-1999 | 25-Sep-2059 | 163,500.10 | 4.250 | 139,204 |
| 491043 | 19-Jan-2006 | 19-Jan-2034 | 465,521.00 | 4.000 | 161,903 |
| 491501 | 05-Mar-2006 | 03-Nov-2051 | 2,689,694.00 | 4.400 | 1,934,019 |
| 491580 | 19-May-2006 | 19-Nov-2046 | 1,303,000.00 | 4.250 | 752,847 |
| 492151 | 20-Sep-2006 | 20-Mar-2052 | 1,856,434.00 | 4.200 | 1,255,676 |
| 492927 | 19-Feb-2007 | 19-Aug-2052 | 2,000,000.00 | 4.400 | 1,478,377 |
| 492928 | 19-Feb-2007 | 19-Aug-2053 | 2,000,000.00 | 4.400 | 1,525,777 |
| 492929 | 19-Feb-2007 | 19-Aug-2054 | 1,427,410.00 | 4.400 | 1,123,138 |
| 493087 | 03-Aug-2007 | 19-Aug-2052 | 2,500,000.00 | 4.250 | 1,748,618 |
| 493088 | 03-Aug-2007 | 19-Aug-2053 | 2,000,000.00 | 4.250 | 1,444,330 |
| 493089 | 03-Aug-2007 | 19-Aug-2054 | 1,414,351.00 | 4.250 | 1,053,877 |
| | | | 21,386,323.30 | | 18,003,763 |

ANNEXE A2 TREASURY MANAGEMENT GLOSSARY OF TERMS

Authorised Limit (Also known as the Affordable Limit):

A statutory limit that sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities).

Balances and Reserves:

Accumulated sums that are maintained either earmarked for specific future costs or commitments or generally held to meet unforeseen or emergency expenditure.

Bank Rate:

The official interest rate set by the Bank of England's Monetary Policy Committee and what is generally termed at the "base rate". This rate is also referred to as the 'repo rate'.

Basis Point:

A unit of measure used in finance to describe the percentage change in the value or rate of a financial instrument. One basis point is equivalent to 0.01% (1/100th of a percent). In most cases, it refers to changes in interest rates and bond yields. For example, if interest rates rise by 25 basis points, it means that rates have risen by 0.25% percentage points. If rates were at 2.50%, and rose by 0.25%, or 25 basis points, the new interest rate would be 2.75%.

Bond:

A certificate of debt issued by a company, government, or other institution. The bond holder receives interest at a rate stated at the time of issue of the bond. The price of a bond may vary during its life.

Capital Expenditure:

Expenditure on the acquisition, creation or enhancement of capital assets.

Capital Financing Requirement (CFR):

The Council's underlying need to borrow for capital purposes representing the cumulative capital expenditure of the local authority that has not been financed.

Capital Receipts:

Money obtained on the sale of a capital asset.

Credit Rating:

Formal opinion by a registered rating agency of a counterparty's future ability to meet its financial liabilities; these are opinions only and not guarantees.

Counterparty List:

List of approved financial institutions with which the Council can place investments with.

Debt Management Office (DMO):

The DMO is an Executive Agency of Her Majesty's Treasury and provides direct access for local authorities into a government deposit facility known as the DMADF. All deposits are guaranteed by HM Government and therefore have the equivalent of a sovereign triple-A credit rating.

Gilts:

Gilts are bonds issued by the UK Government. They take their name from 'gilt-edged'. Being issued by the UK government, they are deemed to be very secure as the investor expects to receive the full face value of the bond to be repaid on maturity.

LIBID:

The London Interbank Bid Rate (LIBID) is the rate bid by banks on Eurocurrency deposits (i.e. the rate at which a bank is willing to borrow from other banks).

LIBOR:

The London Interbank Offered Rate (LIBOR) is the rate of interest that banks charge to lend money to each other. The British Bankers' Association (BBA) work with a small group of large banks to set the LIBOR rate each day. The wholesale markets allow banks who need money to be more fluid in the marketplace to borrow from those with surplus amounts. The banks with surplus amounts of money are keen to lend so that they can generate interest which it would not otherwise receive.

Maturity:

The date when an investment or borrowing is repaid.

Money Market Funds (MMF):

Pooled funds which invest in a range of short term assets providing high credit quality and high liquidity.

Minimum Revenue Provision (MRP):

An annual provision that the Council is statutorily required to set aside and charge to the Revenue Account for the repayment of debt associated with expenditure incurred on capital assets.

Non Specified Investment:

Investments which fall outside the CLG Guidance for Specified investments (below).

Operational Boundary:

This linked directly to the Council's estimates of the CFR and estimates of other day to day cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

Prudential Code:

Developed by CIPFA and introduced on 01/4/2004 as a professional code of practice to support local authority capital investment planning within a clear,

affordable, prudent and sustainable framework and in accordance with good professional practice.

Prudential Indicators:

Prudential indicators are a set of financial indicators and limits that are calculated in order to demonstrate that councils' capital investment plans are affordable, prudent and sustainable.

They are outlined in the CIPFA Prudential Code of Practice. They are indicators that must be used to cover the categories of affordability, prudence, capital spending, external debt/borrowing and treasury management. They take the form of limits, ratios or targets which are approved by Council before 1 April each year and are monitored throughout the year on an on-going basis. A council may also choose to use additional voluntary indicators.

Public Works Loans Board (PWLB):

The PWLB is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.

Revenue Expenditure:

Expenditure to meet the continuing cost of delivery of services including salaries and wages, the purchase of materials and capital financing charges.

(Short) Term Deposits:

Deposits of cash with terms attached relating to maturity and rate of return (Interest).

Specified Investments:

Term used in the CLG Guidance and Welsh Assembly Guidance for Local Authority Investments. Investments that offer high security and high liquidity, in sterling and for no more than one year. UK government, local authorities and bodies that have a high credit rating.

Supported Borrowing:

Borrowing for which the costs are supported by the government or third party.

Temporary Borrowing:

Borrowing to cover peaks and troughs of cash flow, not to fund capital spending.

Unsupported Borrowing:

Borrowing which is self-financed by the local authority. This is also sometimes referred to as Prudential Borrowing.

Yield:

The measure of the return on an investment.

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available on request**



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