Report to Council

Treasury Management Strategy Statement 2018/19

Including the Minimum Revenue Provision Policy Statement, Annual Investment Strategy and Prudential Indicators

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Reason for Decision

To present to Council, the strategy for 2018/19 Treasury Management activities including the Minimum Revenue Provision Policy Statement, the Annual Investment Strategy and Prudential Indicators.

Executive Summary

The report outlines the Treasury Management Strategy for 2018/19 including the Minimum Revenue Provision Policy Statement, Annual Investment Strategy and Prudential Indicators.

The Strategy for 2018/19 covers two main areas.

Capital Issues

- The Capital Plans and the Prudential Indicators
- The Minimum Revenue Provision (MRP) Policy Statement

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
- The Policy on Borrowing in Advance of Need
- Debt Rescheduling
- The Investment Strategy
- The Creditworthiness Policy
- The Policy regarding the use of external service providers.

The report therefore outlines the implications and key factors in relation to each of the above Capital and Treasury Management issues and makes recommendations with regard to the Treasury Management Strategy for 2018/19.

The Treasury Management Strategy for 2018/19 is based on the current guidance at the time of writing. The Chartered Institute of Public Finance and Accountancy (CIPFA) released revised and updated versions of the Prudential Code and the Treasury Management Code in early January 2018. It has not yet released guidance notes to these two Codes which would provide clarity in interpreting the new requirements. This is important as these Codes heavily influence the context of the Treasury Management Strategy.

In February 2018, the Ministry of Housing, Communities and Local Government (MHCLG) released the consultation and Government responses to the proposed changes to the prudential framework for capital finance, in particular MRP and investment guidance. Further information will be provided in the non- statutory explanatory notes, (not yet released) to clarify the MRP Guidance. This report has therefore been based on the current guidance / information available. It may be necessary to revise the Treasury Management Strategy at a later date when further clarification on new requirements becomes available.

The proposed Treasury Management Strategy was presented for scrutiny to the Overview and Scrutiny Performance and Value for Money Select Committee on 25 January 2018. The Committee was content to commend the report to Cabinet. It should be noted that the report has been subsequently updated to reflect revised Capital Expenditure projections and associated Prudential Indicators. Cabinet duly considered and approved the report at its meeting on 19 February 2018 and commended the report to Council.

Recommendation

That Council approves the:

1. Capital Expenditure Estimates as per paragraph 2.1.2;
2. MRP policy and method of calculation as per Appendix 1;
3. Capital Financing Requirement (CFR) Projections as per paragraph 2.2.4;
4. Projected treasury position as at 31/03/2018 as per paragraph 2.3.3;
5. Treasury Limit’s as per section 2.4;
6. Borrowing Strategy for 2018/19 as per section 2.6;
7. Annual Investment Strategy as per section 2.10 including non-treasury investments and the creditworthiness policy at section 2.11.
8. Level of investment in specified, non-specified and non-treasury investments detailed at Appendix 4

Treasury Management Strategy Statement 2018/19 Including the Minimum Revenue Provision Policy Statement, Annual Investment Strategy and Prudential Indicators

1 Background

1.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the Treasury Management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low investment risk appetite, providing adequate liquidity initially before considering investment return.

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

1.3 Treasury management is defined as:

"The management of the local authority's borrowing, 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. "

Source: CIPFA Treasury Management in the Public Service's Code of Practice.

Reporting Requirements

1.4 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.

a) Prudential and treasury indicators and treasury strategy (this report).

The first and most important report covers:

- the capital plans (including prudential indicators);
- 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 (the parameters on how investments are to be managed).

b) A mid-year treasury management report,

This report updates Members with the progress of the capital position, amending Prudential Indicators as necessary and revising any policies as required;

c) An annual treasury report

This report will provide details of a selection of actual Prudential and Treasury Indicators and actual treasury operations compared to the estimates within the strategy.

1.5 The above reports are required to be adequately scrutinised before being recommended to the Council. The PVFM Select Committee scrutinises the Treasury Management Strategy Statement report together with all the other reports which are presented to the annual Budget Council meeting. The Audit Committee, the body charged with the detailed scrutiny of Treasury Management activities will also consider this report and the mid-year and annual review report.

1.6 **Capital Strategy**

1.6.1 In December 2017, CIPFA issued revised Prudential and Treasury Management Codes. As from 2019/20, all Local Authorities will be required to prepare an additional report, a Capital Strategy report (currently this is not a specific requirement), which is intended to provide the following:-

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

1.6.2 The aim of the Capital Strategy will be to ensure that all Members of the Council fully understand the overall strategy, governance procedures and risk appetite entailed by this Strategy. It will include capital expenditure, investments and liabilities and treasury management in sufficient detail to allow all Members to understand how stewardship, value for money, prudence, sustainability and affordability will be secured.

1.6.3 The Council's current Capital Strategy meets many of the elements of the proposed guidance, however, some work will be needed to adapt the Strategy to ensure full compliance. This work will be undertaken so that the Capital Strategy for 2019/20 complies with the new guidance which becomes effective from April 2019.

1.7 **Treasury Management Strategy 2018/19**

1.7.1 The Strategy for 2018/19 covers two main areas, Capital issues and Treasury Management issues set out below:

1.7.2 Capital Issues:

- The Capital Plans and the Prudential Indicators
- The MRP Policy Statement

1.7.3 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
- The Policy on Borrowing in Advance of Need
- Debt Rescheduling
- The Investment Strategy
- The Creditworthiness Policy
- The Policy regarding the use of external service providers.

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

Training

1.8 The CIPFA Code requires the responsible officer to ensure that Members with responsibility for treasury management receive adequate training in treasury management. This especially applies to Members responsible for scrutiny. Training has been organised for Members of the Audit Committee during 2017/18 and Treasury Management issues are discussed in depth at each Audit Committee meeting. The key elements of the 2018/19 Treasury Management Strategy were discussed at the Audit Committee meeting of 11 January 2018.

1.9 Further training will be organised for all Council Members covering general treasury matters during 2018 with more detailed training for Members of the Audit Committee.

1.10 The training needs of treasury management officers are periodically reviewed. However the Treasury team regularly attends training organised by CIPFA and Treasury Management advisors.

Treasury Management Consultants

1.11 Oldham Council uses Link Asset Services, Treasury Solutions as its external Treasury Management advisors. The Council recognises that responsibility for Treasury Management decisions remain with the Council at all times and will ensure that undue reliance is not placed upon external service providers.

1.12 It is also recognised 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 Capital Plans & Prudential Indicators 2018/19 – 2020/21

2.1 Capital Plans

2.1.1 The Council's capital expenditure plans are the key driver of Treasury Management activity. The output of the capital expenditure plans is reflected in Prudential Indicators, which are designed to assist Members' overview and confirm capital expenditure plans. These indicators as per the Capital Programme include previous years' actual expenditure, forecast expenditure for this current year and estimates for the next three year period.

Capital Expenditure Estimates

2.1.2 This first Prudential Indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Council is asked to approve the capital expenditure forecasts included the table below:

Table 1 - Capital Expenditure Estimates

Capital Expenditure	2016/17 Actual £000	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
Corporate and Commercial Services	1,947	5,594	25,445	6,309	838
Health and Wellbeing	2,056	1,362	4,426	500	500
Economy, Skills and Neighbourhoods	37,622	27,882	52,152	97,097	22,717
Funds yet to be allocated	0	0	4,862	1,775	5,000
General Fund Services	**41,625**	**34,838**	**86,885**	**105,681**	**29,055**
Housing Revenue Account (HRA)	1,248	1,044	2,773	-	8,550
HRA	**1,248**	**1,044**	**2,773**	**-**	**8,550**
Total	**42,873**	**35,882**	**89,658**	**105,681**	**37,605**

2.1.3 The capital expenditure shown above excludes other long term liabilities, such as PFI and leasing arrangements which already include borrowing instruments. It should be noted that new expenditure commitments are likely to increase the borrowing requirement.

2.1.4 Table 2 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 need (borrowing).

2.1.5 The borrowing need for capital expenditure in 2018/19 is currently expected to be £40.664m. This will however change if there is a revision to the spending profile of the capital programme.

Table 2 - Funding of the Capital Programme

Capital Expenditure	2016/17 Actual £000	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
General Fund Services	41,625	34,838	86,885	105,681	29,055
HRA	1,248	1,044	2,773	-	8,550
Total	**42,873**	**35,882**	**89,658**	**105,681**	**37,605**
Financed by:					
Capital receipts	(8,780)	(6,037)	(17,347)	(4,258)	(1,469)
Capital grants	(17,304)	(13,859)	(28,718)	(45,816)	(15,591)
Revenue	(15,541)	(176)	(786)	(3,241)	-
HRA Resources	(1,248)	(794)	(2,143)	-	(7,300)
Net financing need for the year	**-**	**15,016**	**40,664**	**52,366**	**13,245**

2.1.6 All other prudential indicators included within this report are based on the above capital estimates.

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

2.2.1 The second Prudential Indicator is the Council's CFR. The CFR represents total historic outstanding capital expenditure which has not yet been financed 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 financed from cash backed resources, will increase the CFR.

2.2.2 The CFR does not increase indefinitely, as the Council makes 'prudent' provision for debt repayment which broadly reduces indebtedness in line with each asset's life and so charges the economic consumption of capital assets as they are used. The approach to making prudent provision is set out in the MRP Policy Statement at Appendix 1.

2.2.3 The MRP policy for 2018/19 is largely comparable to 2017/18. The only change is an amendment at 1.4.2 in Appendix 1 to clarify that the Council can adjust current and future year's calculations to recognise and take account of voluntary revenue provision in previous years. The Council recognises it has overprovided and therefore will reduce the expected MRP by this over provision of £7.465m in 2018/19. This is reflected in the 2018/19 revenue budget.

2.2.4 The CFR includes other long term liabilities (e.g. Private Finance Initiative (PFI) schemes, finance leases etc.). Whilst these arrangements increase the CFR, and therefore the Council's borrowing requirement, such schemes also include a 'loan' facility meaning the Council is not required to make separate borrowing arrangements. The Council currently has £255.971m of such schemes within the CFR for 2018/19, decreasing to £245.992m in 2019/20.

Table 3 Capital Financing Requirement (CFR)

	2016/17 Actual £000	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
Capital Financing Requirement					
CFR	521,790	520,936	542,041	572,362	561,381
Total CFR	**521,790**	**520,936**	**542,041**	**572,362**	**561,381**
Movement in CFR	**(21,442)**	**(854)**	**21,105**	**30,321**	**(10,981)**
Movement in CFR represented by					
Net financing need for the year	-	15,016	40,664	52,366	13,245
PFI Additions/Finance Leases	296				
Less MRP/VRP and other financing movements	(21,738)	(15,870)	(19,559)	(22,045)	(24,226)
Movement in CFR	(21,442)	(854)	21,105	30,321	(10,981)

2.3 Borrowing

2.3.1 The capital expenditure plans set out in section 2.1 to a large extent drive the borrowing estimates included in this report. The Treasury Management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's capital strategy. 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 and Prudential Indicators, the current and projected debt positions and the Annual Investment Strategy.

Current Borrowing Portfolio Position

2.3.2 The Council's treasury portfolio position at 31 March 2017, with forward projections is summarised below. Table 4 shows the actual external debt (the Treasury Management operations), against the underlying capital borrowing need, the CFR, highlighting any over or under borrowing.

2.3.3 Table 4 shows the forecast position of gross borrowing as at 31 March 2018 at £403.821m and an under borrowed position of £117.115m. Council is asked to note the expected year end position.

Table 4 Current and Forecast Treasury Portfolio

	2016/17 Actual £'000	Forecast position as at 31/3/18 £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000
External Debt					
Debt @ 1st April	148,113	147,866	147,850	180,350	215,850
Expected change in debt	(247)	(16)	32,500	35,500	0
Other long-term liabilities	273,009	263,947	255,971	245,992	235,245
Expected change in OLTL*	(9,062)	(7,976)	(9,979)	(10,747)	(11,270)
Actual gross debt at 31 March	**411,813**	**403,821**	**426,342**	**451,095**	**439,825**
The Capital Financing Requirement	**521,790**	**520,936**	**542,041**	**572,362**	**561,381**
Under / (over) borrowing	**109,977**	**117,115**	**115,699**	**121,267**	**121,556**

** (OLTL) - Other Long Term Liabilities*

2.3.4 Table 4 above shows the Council will need to undertake significant additional borrowing in future years if capital programme expenditure matches the anticipated spending profile. The borrowing requirement is a key driver of the borrowing strategy as set out in section 2.6 below. However, the Council has yet to draw down additional borrowing and the timing of the borrowing is being closely monitored. Members will recall that capital spending plans have been reprofiled year on year and it is possible that the trend could be repeated in 2018/19.

2.3.5 There are a number of key Prudential Indicators to ensure that the Council operates its activities within well-defined limits. The Council must ensure that gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2018/19 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 or speculative purposes. It is clear from the table above that the Council's gross borrowing position remains within these limits.

2.3.6 The Council has complied with this Prudential Indicator in the current year and does not envisage any difficulties with compliance in the future. This view takes into account current commitments, existing plans, and the proposals set out in this report.

2.4 Treasury Limits for 2018/19 to 2020/21

2.4.1 The Council is required to determine its operational boundary and authorised limit for external debt for the next three financial years.

Operational boundary

2.4.2 The forecast operational boundary for 2017/18 together with the proposed operational boundaries for 2018/19 to 2020/21 are set out in Table 5 below. The boundary reflects the maximum anticipated level of external debt which is not expected to be exceeded. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on levels of actual debt and the ability to fund under-borrowing by other cash resources. This boundary will be used as a management tool for ongoing monitoring of external debt, and may be breached temporarily due to unusual cash flow movements. However a sustained or regular trend above the operational boundary should trigger a review of both the operational boundary and the authorised limit.

Table 5 Operational Boundary

Operational boundary	2017/18 Forecast £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
Borrowing	275,000	300,000	340,000	340,000
Other long term liabilities	255,000	245,000	235,000	225,000
Total	**530,000**	**545,000**	**575,000**	**565,000**

Authorised limit

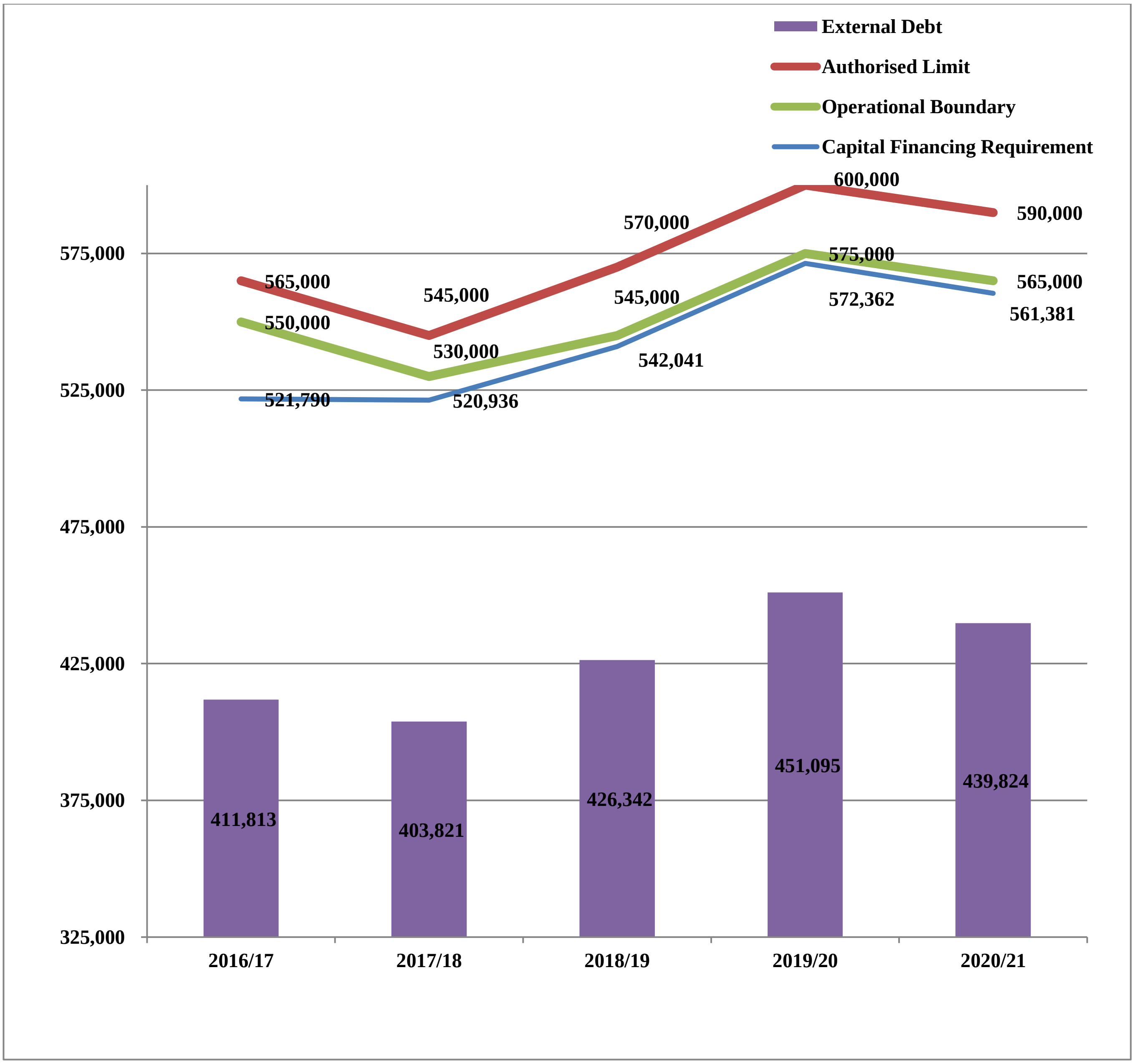
2.4.3 A further key Prudential Indicator, the Authorised Limit controls the maximum level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit may only be determined by the full Council. It reflects the level of external debt which, while not desirable, is affordable in the short term, but is not sustainable in the longer term. 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.

2.4.4 Council is asked to approve the following proposed authorised limit for each financial year from 2017/18 to 2020/21 as set out in table 5 above and 6 below:

Table 6 Authorised Limit

Authorised Limit	2017/18 Forecast £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
Borrowing	285,000	320,000	360,000	360,000
Other long term liabilities	260,000	250,000	240,000	230,000
Total	**545,000**	**570,000**	**600,000**	**590,000**

2.4.5 The graphs below disclose how the two indicators above, the Operational Boundary and the Authorised Limit compare to actual external debt and the CFR.



2.5 Prospects for Interest Rate

2.5.1 The Council has appointed Link Asset Services as its Treasury Adviser and part of its service is to assist the Council to formulate a view on interest rates. The table below gives Link Asset Services central view.

Table 7 Interest Rate Forecast

	Bank	PWLB Borrowing Rates %			
	Rate %	5 year	10 year	25 year	50 year
Mar-18	0.50	1.90	2.50	2.80	2.60
Jun-18	0.75	2.00	2.50	2.90	2.70
Sep-18	0.75	2.10	2.60	3.00	2.80
Dec-18	1.00	2.10	2.70	3.10	2.90
Mar-19	1.00	2.20	2.70	3.20	3.00
Jun-19	1.00	2.30	2.80	3.20	3.00
Sep-19	1.00	2.30	2.80	3.30	3.10
Dec-19	1.25	2.40	2.90	3.30	3.10
Mar-20	1.25	2.40	3.00	3.40	3.20
Jun-20	1.25	2.50	3.00	3.50	3.30
Sep-20	1.50	2.50	3.10	3.50	3.30
Dec-20	1.50	2.60	3.10	3.60	3.40
Mar-21	1.50	2.60	3.20	3.60	3.40

2.5.2 As expected, the Monetary Policy Committee (MPC) delivered a 0.25% increase in Bank Rate at its meeting on 2 November 2017. This removed the emergency cut in August 2016 after the European Union (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, however includes increases in Bank Rate of 0.25% in November 2018, November 2019 and August 2020.

2.5.3 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.

2.5.4 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.

2.5.5 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 Federal Reserve (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.

2.5.6 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.

2.5.7 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.

2.5.8 From time to time, gilt yields – and therefore Public Works Loan Board (PWLB) rates - can be subject to exceptional levels of volatility due to geo-political issues/ events, sovereign debt crisis and emerging market developments. Such volatility could occur at any time during the forecast period.

2.5.9 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.

2.5.10 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.

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

- The Bank of England takes action too quickly over the next three years to raise the Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than currently anticipated.
- 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 in Italy, due to its high level of government debt, low rate of economic growth and vulnerable banking system.
- Weak capitalisation of some European banks.
- Germany has just agreed a coalition Government after the inconclusive result of the general election in October. Italy is to hold a general election on 4 March and Hungary will hold a general election in April 2018. The potential changes to the political landscape could impact on overal EU leadership and direction as well as that of the individual countries.
- Rising protectionism under President Trump.
- A sharp Chinese downturn and its impact on emerging market countries.

2.5.12 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.

2.5.13 The key issues with regard to investment and borrowing rates are:

- 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 2017 and then also after the September 2017 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 if new borrowing to finance capital expenditure and/or the refinancing of maturing debt is required;
- 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. This is an important issue for the Council. There will be a need to borrow, but the timing remains uncertain requiring judgement in balancing the cost of carrying unused borrowing against locking in potentially to lower long term interest rates.

2.5.14 In the Autumn Budget 2017 the Government confirmed that it will lend Local Authorities in England up to £1 billion at a new discounted interest rate of gilts + 60 basis points accessible for three years to support infrastructure projects that are high value for money. Once the bidding process is confirmed the Council will pursue this opportunity as appropriate.

2.6 Borrowing strategy

2.6.1 The factors that influence the 2018/19 strategy are:

- The movement in CFR as set out in Table 3 above;
- Forthcoming ‘Option’ dates on £55.5m of Lender Option Borrower Option loans (LOBO’s) in 2018/19;
- The interest rate forecasts (set out in Table 7 above);
- Aiming to minimise revenue costs to reduce the impact on the Council Tax Requirement;
- The impact of the Council’s Capital and Property Investment Programmes.

2.6.2 The Council is currently maintaining an under-borrowed position. This means that the CFR 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. However, as interest rates are low, as advised in 2.5.13 consideration will be given to taking advantage of this by securing fixed rate funding and reducing the under borrowed position.

2.6.3 Against this background and the risks within the economic forecast, caution will be adopted with the 2018/19 treasury operations. The Treasury Management team will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances so that:

- if it was considered 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 borrowing will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- if it was considered that there was a significant risk of a much sharper rise in long and short term rates than that currently forecast, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are still lower than they will be in the next few years.

2.6.4 The gross borrowing requirement in Table 4 at 2.3.3 above shows, based on current estimates, that the Council will need to drawdown a significant amount of new borrowing, to support the capital programme. Any additional borrowing will be completed with regard to the limits, indicators and interest rate forecasts set out above. As noted previously, estimates of borrowing have changed due to the reprofiling of the capital programme.

2.6.5 During 2018/19, £55.5m of LOBO (Lender Option Borrower Option) debt will reach the option renewal date. Table 8 below, sets out the maturity structure of fixed rate debt. At the renewal date the loans will either:

- Move to the option rate of interest, which in all cases will be the same as the current rate or:
- Be offered at a rate above the option rate, in which case the Council has the option to repay. This would then require refinancing at the prevailing market rates.

Table 8 Maturity Structure of Fixed Rate Debt

Maturity Structure of fixed interest rate debt	2018/19
Under 12 months	37.72%
12 months and within 24 months	3.38%
24 months and within 5 years	21.54%
5 years and within 10 years	5.07%
10 years to 20 years	5.24%
20 years to 30 years	0.00%
30 years to 40 years	3.38%
40 years to 50 years	10.15%
50 years to 60 years	13.52%

2.6.6 Due to the current interest rate forecast it is not anticipated that any of these LOBO loans will be called.

2.6.7 The 2018/19 capital programme now shows anticipated prudential borrowing of £106.275m with £40.664m in 2018/19, £52.366m in 2019/20 and £13.245m in 2020/21. These figures have been reflected in this report and factored into the borrowing strategy for 2018/19 and future years.

2.6.8 Members are advised that indicators for interest rate exposure are no longer a requirement under the new Treasury Management Code however as interest rate exposure risk is an important issue. Officers will monitor the balance between fixed and variable interest rates for borrowing and investments. This will aim to ensure the Council is not exposed to adverse fluctuations in fixed or variable rate interest rate movements.

2.6.9 This is likely to reflect higher fixed interest rate borrowing if the borrowing need is high or fixed interest rates are likely to increase, or a higher variable rate exposure if fixed interest rates are expected to fall. Conversely if shorter term interest rates are likely to fall, investments may be fixed earlier, or kept shorter if short term investments are expected to rise.

2.6.10 The balance between variable rate debt and variable rate investments will be monitored as part of the overall treasury function in the context of the overall financial instruments structure and any under or over borrowing positions.

2.7 Policy on Borrowing in Advance of Need

2.7.1 The Council will not borrow more than or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved CFR 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.

2.7.2 Borrowing in advance will be made within the constraint that the Council would not look to borrow more than 24 months in advance of need.

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

2.8 Debt Rescheduling

2.8.1 As short term borrowing rates are considerably lower 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 prevailing treasury position and the size of the cost of debt repayment (premiums incurred).

2.8.2 The reasons for any rescheduling to take place will include:

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

2.8.3 Consideration will also be given to identifying if there is any residual potential for making savings by reducing investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

2.8.4 Given the current structure of the Council debt, such re-scheduling activity is unlikely however, all re-scheduling will be reported to Cabinet and Council at the earliest meeting following its action.

2.9 Local Capital Finance Company (originally Municipal Bond Agency)

2.9.1 It is possible that Local Capital Finance Company will be offering loans to Local Authorities in the future. It is also hoped that the borrowing rates will be lower than those offered by the Public Works Loan Board (PWLB).

2.9.2 The Council has currently invested £0.100m in the Company and intends to make use of this new source of borrowing as and when appropriate.

2.10 Annual Investment Strategy

Investment Policy

2.10.1 The Council's investment policy has regard to the Ministry for Housing, Communities and Local Government (MHCLG's) Guidance on Local Government Investments ("the Guidance") and the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the CIPFA TM Code"). The Council's investment priorities are:

- firstly, the security of capital;
- secondly, the liquidity of its investments;
- thirdly, the optimum return on its investments comensurate with proper levels of security and liquidity;
- finally, ethical investments.

2.10.2 In accordance with the above guidance from the MHCLG 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 avoids risk concentration. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

2.10.3 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 achieve this consideration 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

2.10.4 Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

2.10.5 Investment instruments identified for use in the financial year are listed in Appendix 4 under the 'specified' and 'non-specified' investments categories. Counterparty limits will be set through the Council's Treasury Management practices and are also included within Appendix 4.

Non Treasury Investments

2.10.6 Non-treasury investments are defined as the following categories:

- All share holding, unit holding and bond holding, including those in a Local Authority owned company
- Loans to a local authority company or other entity formed by a Local Authority to deliver services
- Loans made to third parties
- Investment property

2.10.7 The Council has an approved loan facility arrangement in place with a partner organisation to assist with payroll costs should they require it. This facility only covers payroll costs for up to 2 months. The Council currently has no other finance arrangements or loans to Local

Authority companies. Any such finance arrangements or loans would be subject to specific Cabinet approval.

2.10.8 The Council may make loans to third parties, to provide support to organisations who are contributing to the delivery of the Strategic Priorities of the Council and may encounter difficulty in securing funds from other sources at affordable interest rates. Such loans will be in line with the Councils Constitution under the Financial Procedures Rules.

2.10.9 For service reasons loans to third parties may be offered at an interest rate below the market rate. Where the loan is advanced at less than a market interest rate there is an associated loss of investment return which would otherwise have been earned on these monies. The cost to the Council in this respect would be reflected in the Council's accounts. All loans to third parties will be recognised as investments and detailed within the Annual Investment Report.

2.10.10 The Council has an approved Commercial Property Investment Strategy (CPIS). It has allocated resources and facilitated the introduction of activities required to promote the objectives of the strategy which include providing a sustainable income stream to support the Council's budget from the acquisition of property assets. Investments in property may support / provide premises to third party organisations to deliver the economic development objectives of the Council and as mentioned above to optimise the return on the property portfolio. Appendix 4 includes a section on non-treasury investments which highlights the maximum investment limits and maturity period per investment type and maximum financial limit if appropriate.

2.10.11 The Council will evaluate the CPIS Investments to understand the risks involved. It will ensure that staff have the necessary skills and knowledge required and have regard to risk management considerations so that long term financial and risk implications can be assessed and mitigated.

2.11 Creditworthiness policy

2.11.1 Oldham Council applies the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moodys and Standard and Poor. The credit ratings of counterparties are supplemented with the following 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.

2.11.2 This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the duration and maximum investment value for each counterparty.

2.11.3 Institutions are split into colour bandings and the Council will therefore use counterparties within these colours, durational bands and investment limits. Table 9 below shows these limits.

Table 9 Investment Criteria

	Link Colour Band and Long Term Rating where applicable	Maximum Duration	Maximum Principal Invested per Counterparty
Banks	Yellow (Note 1)	5 Years	£10m
Banks	Dark Pink (Note 2)	5 Years	£10m
Banks	Light Pink (Note 3)	5 Years	£10m
Banks	Purple	2 Years	£20m
Banks	Blue (Note 4)	1 Year	£20m
Banks	Orange (Note 5)	1 Year	£15m
Banks	Red	6 months	£10m
Banks	Green	100 days	£10m
Banks	No Colour	Not to be used	Not to be used
Local Authorities	Internal Due Diligence	5 Years	£10m
GMCA	Internal Due Diligence (Note 6)	5 Years	£30m
Debt Management Account Deposit Facility (DMADF)	UK Sovereign rating	6 months	£20m
	Fund Rating	**Maximum Duration**	**Maximum Principal Invested per Counterparty**
Money Market Fund - Constant	AAA	Liquid	£20m
Money Market Fund - Low Volatile	AAA	Liquid	£20m
Money Market Fund - Variable	AAA	Liquid	£20m

Note 1 – UK Government debt or equivalent

Note 2 – Enhanced money market funds (EMMF) with a credit score of 1.25

Note 3 - Enhanced money market funds (EMMF) with a credit score of 1.5

Note 4 – Blue Institutions only applies to nationalised or semi nationalised UK Banks, which currently include the RBS Group (Royal Bank of Scotland, NatWest Bank and Ulster Bank).

Note 5 - Includes the Council's banking provider (currently Barclays), if it currently falls into category below this colour band.

Note 6 – The higher maximum principal is to facilitate joint initiatives and activities related to the devolution agenda.

2.11.4 The Link 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.

2.11.5 Typically the minimum credit ratings criteria the Council uses will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of 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 this instance consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

2.11.6 All credit ratings will be monitored on a weekly basis. The Council is alerted to changes to ratings of all three agencies through its use of the Link 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 or notice given to withdraw immediately.
- In addition to the use of credit ratings the Council will be advised of information in movements in the Credit Default Swap Index against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Asset Services. Extreme market movements may result in the downgrading of an institution or its removal from the Council's lending list.

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

2.12 Country and Sector Limits

2.12.1 It is not proposed to restrict the Council's investment policy to only UK banks and building societies, however in addition to the credit rating criteria set out above consideration will be given to the sovereign rating of the country before any investment is made.

2.12.2 In February 2013 the UK lost its AAA rating and moved to an AA rating. The Council will continue to invest with UK Banks, providing the individual institutions still meet the relevant criteria.

2.12.3 The Council has determined that it will only use approved counterparties from non UK countries with a minimum sovereign credit rating of AAA from Fitch (or equivalent). The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 5. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy, therefore for illustrative purposes the appended list is extended to also show AA- i.e. the countries currently assessed to be in the rating below those that currently qualify. It is important to note that although able to, the Council has chosen not to invest overseas in recent years.

2.13 Investment Strategy

2.13.1 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). The Council currently has investments totalling £18m which span the financial year as shown in Table 10. These investments are current as at February 2018.

Table 10 Investments maturing in 2018/19

Counterparty	Amount	Maturity Date	Rate
Goldman Sachs International Bank	£5,000,000	26/04/2018	0.51%
Surrey Heath Borough Council	£3,000,000	24/05/2018	0.52%
Santander	£2,500,000	5/07/2018	0.70%
Bank of Scotland	£2,500,000	95 day notice	0.70%
Eastleigh Borough Council	£5,000,000	23/07/2018	0.55%
Total	**£18,000,000**		

2.13.2 The Bank Rate is forecast to increase steadily but slowly over the next few years to reach 1.50% by quarter 1 2021. Bank rates forecasts for financial year ends are:

- 2017/18 0.50%
- 2018/19 1.00%
- 2019/20 1.25%
- 2020/21 1.50%

2.13.3 The suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during each financial year are as follows.

- 2017/18 0.40%
- 2018/19 0.80%
- 2019/20 1.25%
- 2020/21 1.50%
- 2021/22 1.65%
- 2022/23 1.75%
- 2023/24 2.00%

2.13.4 The overall balance of risks to these forecasts is skewed to the upside and are dependent on how strong Gross Domestic Product (GDP) growth turns out, how quickly inflation pressures rise and how quickly the Brexit negotiations move forward positively.

2.13.5 The Council will maintain sufficient cash reserves to give it its necessary liquidity and may place investments for up to seven years if the cash flow forecast allows and the credit rating criteria is met.

2.13.6 The Council will avoid locking into longer term deals i.e., “more than 365 days” while investment rates are down at historically low levels unless attractive rates are available with counterparties of particularly high creditworthiness which make longer term deals worthwhile and within the risk parameters set by the Council.

2.13.7 For daily cash management, the Council will seek to utilise its business reserve instant access accounts, 15 and 30 day accounts, money market funds and short-dated deposits (overnight to 100 days) in order to benefit from the compounding of interest.

Investment Treasury Indicator and Limit

2.13.8 This indicator considers total principal funds invested for greater than 365 days. These limits have regard to the Council’s liquidity requirements and to reduce the need for the early redemption of investments, and are based on the availability of funds after each year end.

Table 13 – Maximum principal sum invested greater than 364 & 365 days

	2017/18	2018/19	2019/20	2020/21
Principal sums invested > 364 & 365 days	£50m	£50m	£50m	£50m

2.14 Investment Risk Benchmarking

2.14.1 These benchmarks provide simple guides to maximum risk, and may be breached from time to time, depending on movements in interest rates and counterparty criteria. These benchmarks provide Officers with a baseline against which current and trend positions can be monitored. It may be necessary to amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the mid-year or Annual Report.

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

- Bank overdraft facility of £0.100m
- Liquid short term deposits of at least £10m available with a week's notice.

Yield - local measures of yield benchmarks are:

- Investments – internal returns above the 7 day LIBID (London Interbank Bid Rate) rate multiplied by 5%
- Investments – internal returns above the 1 month LIBID rate multiplied by 5%
- Investments – internal returns above the 3 month LIBID rate multiplied by 5%
- Investments – internal returns above the 6 month LIBID rate multiplied by 5%
- Investments – internal returns above the 12 month LIBID rate multiplied by 5%

2.14.2 At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report, which is in accordance with required practice and is presented to Cabinet and then Council for approval.

3 Options/Alternatives

3.1 In order to comply with the CIPFA Code of Practice on Treasury Management, the Council has no option other than to consider and approve the contents of the report. Therefore no options/alternatives have been presented.

4 Preferred Option

4.1 The preferred option is that the contents of this report are approved by Council.

5 Consultation

5.1 There has been consultation with Link Asset Services, Treasury Management Advisors. Consideration of the Treasury Management Strategy for 2018/19 by the Overview and Scrutiny Performance and Value for Money Select Committee is a key strand in the consultation process. The Select Committee scrutinised the proposed Treasury Management Strategy at its meeting on 25 January 2018 and was content to commend the report to Cabinet. Cabinet also considered and approved the Strategy at its meeting on 19 February 2017 and was content to commend the report to Council.

5.2 The Audit Committee as its meeting of 11 January 2018 reviewed and considered the key features of the 2018/19 Treasury Management Strategy and were content with the issues as presented.

6 Financial Implications

6.1 Financial Implications are detailed within the report.

7 Legal Services Comments

7.1 There are no legal implications.

8 Co-operative Agenda

8.1 The Treasury Management strategy embraces the Council's cooperative agenda. The Council will develop its investment framework to ensure it complements the co-operative ethos of the Council.

9 Human Resources Comments

9.1 There are no Human Resource Implications.

10 Risk Assessments

10.1 There are considerable risks to the security of the Authority's resources if appropriate Treasury Management strategies and policies are not adopted and followed. The Council has established good practice in relation to Treasury Management which has previously been acknowledged in the Internal and External Auditors' reports presented to the Audit Committee.

11 IT Implications

11.1 There are no IT Implications

12 Property Implications

12.1 There are no Property Implications.

13 Procurement Implications

13.1 There are no Procurement Implications.

14 Environmental and Health & Safety Implications

14.1 There are no Environmental and Health & Safety Implications.

15 Equality, community cohesion and crime implications

15.1 There are no Equality, community cohesion and crime implications.

16 Equality Impact Assessment Completed?

16.1 No

17 Key Decision

17.1 Yes

18 Key Decision Reference

18.1 CFHR- 15-17

19 Background Papers

19.1 The following is a list of background papers on which this report is based in accordance with the requirements of Section 100(1) of the Local Government Act 1972. It does not include documents which would disclose exempt or confidential information as defined by the Act:

File Ref:	Background papers are provided in Appendices 1 - 7
Officer Name:	Lee Walsh / Talei Whitmore
Contact No:	0161 770 6608/ 4924

20 Appendices

Appendix 1	Minimum Revenue Provision (MRP) Policy Statement
Appendix 2	Link Asset Services - Treasury Advisor's Interest Rate Forecast 2018-2021
Appendix 3	Economic Background
Appendix 4	Treasury Management Practice (TMP1) – Credit and Counterparty Risk Management
Appendix 5	Approved Countries for Investments
Appendix 6	Treasury Management Scheme of Delegation
Appendix 7	Treasury Management Role of the Statutory Chief Finance Officer (Director of Finance)

Appendix 1 – Minimum Revenue Provision (MRP) Policy Statement

1.1 General Principles and Practices

1.1.1 Local Authorities are required to set aside 'prudent' provision for debt repayment where they have used borrowing or credit arrangements to finance capital expenditure. Ministry for Housing, Communities and Local Government (MHCLG) regulations require the full MRP Statement to be decided upon at least annually and reported to the Council Meeting. The Council has to ensure that the chosen options are prudent.

1.2 Link to Asset Life/Economic Benefit

1.2.1 Where capital expenditure on an asset is financed wholly or partly by borrowing or credit arrangements, MRP will normally be determined by reference to asset life, economic benefit or MHCLG Guidance.

1.2.3 To the extent that expenditure cannot be linked to the creation/enhancement of an asset and is of a type that is subject to estimated life periods that are referred to in the MHCLG guidance (paragraph 24), these periods will generally be adopted by the Council.

1.2.4 Where certain types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure.

1.2.5 Whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

1.3 Methods for Calculating MRP

1.3.1 Any of the methods for calculating MRP that are set out below may be used. MRP will commence in the financial year after the completion of assets rather than when expenditure is incurred. All methods, with the exception of the approach taken to Previously Supported General Fund Borrowing are based on Asset Life/Economic Benefit. These methods include but are not limited to:

The Annuity Method

1.3.2 This calculation seeks to ensure the revenue account bears an equal annual charge (for principal and interest) over the life of the asset by taking account of the time value of money. Since MRP relates only to 'principal', the amount of provision made annually gradually increases during the life of the asset. The interest rate used in annuity calculations will be referenced to either prevailing or average PWLB rates.

Equal Instalments of Principal

1.3.3 MRP is an equal annual charge calculated by dividing the original amount of borrowing by the useful life of the asset.

Previously Supported General Fund Borrowing

1.3.4 General Fund Borrowing that was previously supported through the Revenue Support Grant (RSG) system will be provided for in equal annual instalments over a 50 year period commencing 1 April 2016. As at 1 April 2016, the value of this borrowing equalled £137,119,251 and results in an equal annual minimum revenue provision of £2,742,385; the final instalment of which will be provided for by no later than 31 March 2066. In the event of:

- transfers of Capital Financing Requirement between the General Fund element and Housing element;
- additional voluntary revenue provision being made

the annual MRP charge will be adjusted to ensure that full provision will continue to be made by no later than 31 March 2066.

Bespoke Repayment Profiles:

1.3.5 With regard to credit arrangements that are implicit in Finance Lease or PFI arrangements, any 'debt' repayment element (notional or otherwise) included in charges associated with these arrangements will be classified as MRP.

1.4 Voluntary Revenue Provision

1.4.1 The Council has the option of making additional Voluntary Revenue Provision (VRP) in addition to MRP. The Council may treat VRP as 'up-front' provision (having a similar impact to the early repayment of debt) and thus recalculate future MRP charges accordingly. Where the Council has made additional VRP's for debt repayment in previous years, in year MRP charges may be adjusted to reflect this provided it does not result in a negative MRP charge. To the extent charges are adjusted, current and future year's charges will be recalculated to ensure the Council continues to make prudent provision for debt repayment in relation to historic capital expenditure. The Council may in some circumstances apply VRP to relatively short-life assets/expenditure in order to facilitate a reduction in the future base revenue budget needed to fund capital financing costs.

1.4.2 Where the Council has made additional voluntary revenue provision for debt repayment in previous years, in year MRP charges may be adjusted to reflect this provided it does not result in a negative MRP charge. To the extent charges are adjusted, current and future year's charges will be recalculated to ensure the Council continues to make prudent provision for debt repayment in relation to historic capital expenditure.

1.5 Local Exceptions to the Guidance

1.5.1 The Council reserves the right to determine useful life periods and prudent MRP in certain circumstances or where the recommendations of the MHCLG guidance are not appropriate to local circumstances. Examples include:

Assets under Construction

1.5.2 No MRP charge will be made until the financial year after that in which an item of capital expenditure is fully incurred and, in the case of a new asset, comes into service use.

Local Authority Mortgage Scheme (LAMS)

1.5.3 The Council currently operates a Local Authority Mortgage Scheme (LAMS) using the cash backed option. The mortgage lenders require a five year deposit from the Local Authority to match the five year life of the indemnity. The deposit placed with the mortgage lender provides an integral part of the mortgage lending and is treated as capital expenditure and a loan to a third party. The CFR will increase by the amount of the total indemnity. The cash advance is due to be returned in full at maturity, with interest paid annually. Once the cash advance matures and funds are returned to the Local Authority, the returned funds are classed as a capital receipt, which will be applied to reduce the CFR. As this is a temporary (five years) arrangement and the funds will be returned in full, there is no need to set aside MRP to repay the debt liability in the interim period.

Loans to third parties

1.5.4 The Council has considered the Statutory Guidance, which recommends a 25 year repayment charge for loans to third parties, and concluded that provision is not necessary. The Council considers an MRP charge is not necessary in respect of any loans made to third parties as the debt liability is covered by the existence of a debtor and the associated obligation to make repayments.

1.6 Borrowing in Lieu of Capital Receipts

1.6.1 The Council has concluded that MRP provision is not necessary for capital expenditure incurred in lieu of capital receipts. Any such schemes will be classified by the Capital Investment Programme Board (CIPB) as ‘Borrowing in Lieu of Capital Receipts’. CIPB will also determine which capital receipts will be allocated to the scheme and as the receipts are achieved they will be applied to repay the debt.

The Application of Capital Receipts in Lieu of MRP

1.6.2 Where the Council has received uncommitted and unapplied Capital Receipts, it retains the option to set aside those Capital Receipts as part of its arrangements for making ‘prudent’ provision for debt repayment rather than using them for capital financing purposes.

1.6.3 As Capital Receipts may form part of the Councils arrangements for making ‘prudent’ provision, setting aside Capital Receipts in this manner can be carried out in lieu of MRP whereby the MRP charge will be reduced by an amount equal to that set aside from Capital Receipts.

1.7 HRA Capital Financing Requirement (CFR)

1.7.1 MRP will equal the amount determined in accordance with the former regulations 28 and 29 of the 2003 Regulations (SI 2003/3146) as if they had not been revoked. This approach is consistent with paragraph 7 of the MHCLG Guidance on MRP.

1.7.2 The basic MRP charge relating to the HRA CFR is therefore nil. However, the Council may make ‘Voluntary Revenue Provision’ provided such an approach is prudent and appropriate in the context of financing the HRA capital programme and is consistent with the delivery of the HRA Business Plan.

APPENDIX 2 – Link Asset Services Interest rate forecast 2018 – 2021

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

	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21
Bank rate	0.50%	0.75%	0.75%	1.00%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%	1.50%	1.50%
5yr PWLB rate	1.90%	2.00%	2.10%	2.10%	2.20%	2.30%	2.30%	2.40%	2.40%	2.50%	2.50%	2.60%	2.60%
10yr PWLB rate	2.50%	2.50%	2.60%	2.70%	2.70%	2.80%	2.80%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%
25yr PWLB rate	2.80%	2.90%	3.00%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.50%	3.50%	3.60%	3.60%
50yr PWLB rate	2.60%	2.70%	2.80%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%

APPENDIX 3: Economic Background

Set out below is a more detailed analysis of the Economic background used to support the preparation of the 2018/19 Treasury Management Strategy Statement

Global Outlook

World growth looks to be on an encouraging trend of stronger performance, rising earnings and falling levels of unemployment. In October 2017, the International Monetary Fund (IMF) upgraded its forecast from 3.2% to 3.6% for 2017 and 3.7% for 2018.

In addition, inflation prospects are generally muted and it is particularly notable that wage inflation has been subdued despite unemployment falling to historically very low levels in the UK and US. This has led to many comments by economists that there appears to have been a fundamental shift downwards in the Phillips curve (this plots the correlation between levels of unemployment and inflation e.g. if the former is low the latter tends to be high). In turn, raising the question; what has caused this? The likely answers probably lay in a combination of a shift towards flexible working, self-employment, falling union membership and a consequent reduction in union power and influence in the economy, and increasing globalisation and specialisation of individual countries, which has meant that labour in one country is in competition with labour in other countries which may be offering lower wage rates, increased productivity or a combination of the two. In addition, technology is probably also exerting downward pressure on wage rates and this is likely to grow with an accelerating movement towards automation, robots and artificial intelligence, leading to many repetitive tasks being taken over by machines or computers. Indeed, this is now being labelled as being the start of the fourth industrial revolution.

Key risks- Central Bank Monetary Policy Measures

Looking back on nearly ten years since the financial crash of 2008 when liquidity suddenly dried up in financial markets, it can be assessed that central banks' monetary policy measures to counter the sharp world recession were successful. The key monetary policy measures they used were a combination of lowering central interest rates and flooding financial markets with liquidity, particularly through unconventional means such as Quantitative Easing (QE), where central banks bought large amounts of central government debt and smaller sums of other debt.

The key issue now is that that period of stimulating economic recovery and warding off the threat of deflation is coming towards its close and a new period has already started in the US, and more recently, in the UK, on reversing those measures i.e. by raising central rates and (for the US) reducing central banks' holdings of government and other debt. These measures are now required in order to stop the trend of an on-going reduction in spare capacity in the economy, and of unemployment falling to such low levels that the re-emergence of inflation is viewed as a major risk. It is, therefore, crucial that central banks get their timing right and do not cause shocks to market expectations that could destabilise financial markets. In particular, a key risk is that because QE-driven purchases of bonds drove up the price of government debt, and therefore caused a sharp drop in income yields, this then also encouraged investors into a search for yield and into investing in riskier assets such as equities. This resulted in bond markets and equity market prices both rising to historically high valuation levels simultaneously. This, therefore, makes both asset categories vulnerable to a sharp correction. It is important, therefore, that central banks only gradually unwind their holdings of bonds in order to prevent destabilising the financial markets. It is also likely that the timeframe for central banks unwinding their holdings of QE debt purchases will be over several years. They need to balance their timing to neither squash economic recovery by taking too rapid and too strong action, nor, alternatively, let inflation run away by taking action that was too slow and/or too weak. The potential for central banks to get this timing and strength of action wrong are now key risks.

There is also a potential key question over whether economic growth has become too dependent on strong central bank stimulus and whether it will maintain its momentum against a backdrop of rising interest rates and the reversal of QE. In the UK, a key vulnerability is the low level of productivity growth, which may be the main driver for increases in wages; and decreasing consumer disposable income, which is important in the context of consumer expenditure primarily underpinning UK GDP growth.

A further question that has come to the fore is whether an inflation target for central banks of 2%, is now realistic given the shift down in inflation pressures from internally generated inflation, (i.e. wage inflation feeding through into the national economy), given the above mentioned shift down in the Phillips curve.

- Some economists favour a shift to a lower inflation target of 1% to emphasise the need to keep inflation under control. Alternatively, it is possible that a central bank could simply 'look through' tepid wage inflation, (i.e. ignore the overall 2% inflation target), in order to take action in raising rates sooner than might otherwise be expected.
- However, other economists would argue for a shift up in the inflation target to 3% in order to ensure that central banks place the emphasis on maintaining economic growth through adopting a slower pace of withdrawal of stimulus.
- In addition, there is a strong argument that central banks should target financial market stability. As mentioned previously, bond markets and equity markets could be vulnerable to a sharp correction. There has been much commentary, that since 2008, QE has caused massive distortions, imbalances and bubbles in asset prices, both financial and non-financial. Consequently, there are widespread concerns at the potential for such bubbles to be burst by exuberant central bank action. On the other hand, too slow or weak action would allow these imbalances and distortions to continue or to even inflate them further.
- Consumer debt levels are also at historically high levels due to the prolonged period of low cost of borrowing since the financial crash. In turn, this cheap borrowing has meant that other non-financial asset prices, particularly house prices, have been driven up to very high levels, especially compared to income levels. Any sharp downturn in the availability of credit, or increase in the cost of credit, could potentially destabilise the housing market and generate a sharp downturn in house prices. This could then have a destabilising effect on consumer confidence, consumer expenditure and GDP growth. However, no central bank would accept that it ought to have responsibility for specifically targeting house prices.

United Kingdom

After the UK surprised on the upside with strong economic growth in 2016, growth in 2017 has confounded pessimistic forecasts of weak growth by coming in at 1.8%, only marginally down on the 1.9% rate for 2016, In 2017 quarter 1 came in at only +0.3% (+1.8% year on year), quarter 2 +0.3% (+1.5% year on year) and quarter 3 +0.4% (+1.5% year on year) and Q4 was +0.5% (+1.5% y/y). The outstanding performance came from the manufacturing sector which showed a 1.3% increase in Q4 and +3.1% y/y helped by an increase in exports due to the lower value of sterling over the last year and robust economic growth in our main trade partners, the EU and US. It is also notable that there has been a progressive acceleration in total GDP growth during the year which gives ground for optimism looking forward into 2018.

While the Bank of England is expected to give forward guidance to prepare financial markets for gradual changes in policy, the Monetary Policy Committee, (MPC), meeting of 14 September 2017 managed to shock financial markets and forecasters by suddenly switching to a much more aggressive tone in terms of its words around warning that Bank Rate will need to rise soon. The Bank of England Inflation Reports during 2017 have clearly flagged up that it expected Consumer Price Index (CPI) inflation to peak at just under 3% in 2017, before falling back to near to its target rate of 2% in two years' time. The Bank revised its forecast for the peak to just over 3% at the 14

September meeting. (Inflation actually came in at 3.0% in both September and October so that might prove now to be the peak). This marginal revision in the Bank's forecast can hardly justify why the MPC became so aggressive with its wording; rather, the focus was on an emerging view that with unemployment having already fallen to only 4.3%, the lowest level since 1975, and improvements in productivity being so weak, that the amount of spare capacity in the economy was significantly diminishing towards a point at which they now needed to take action. In addition, the MPC took a more tolerant view of low wage inflation as this now looks like a common factor in nearly all western economies as a result of automation and globalisation. However, the Bank was also concerned that the withdrawal of the UK from the EU would effectively lead to a decrease in such globalisation pressures in the UK, and so this would cause additional inflationary pressure over the next few years.

At its 2 November 2017 meeting, the MPC duly delivered a 0.25% increase in Bank Rate. It also gave forward guidance that it expected to increase Bank Rate only twice more in the next three years to reach 1.0% by 2020. This is, therefore, not quite the 'one and done' scenario but is, nevertheless, a very relaxed rate of increase prediction in Bank Rate in line with previous statements that Bank Rate would only go up very gradually and to a limited extent.

However, some forecasters are flagging up that they expected growth to accelerate significantly towards the end of 2017 and then into 2018. This view is based primarily on the coming fall in inflation, (as the effect of the effective devaluation of sterling after the EU referendum drops out of the CPI statistics), which will bring to an end the negative impact on consumer spending power. In addition, a strong export performance will compensate for weak services sector growth. If this scenario was indeed to materialise, then the MPC would be likely to accelerate its pace of increases in Bank Rate during 2018 and onwards.

It is also worth noting the contradiction within the Bank of England between action in 2016 and in 2017 by two of its committees. After the shock result of the EU referendum, the MPC voted in August 2016 for emergency action to cut Bank Rate from 0.50% to 0.25%, restarting £70bn of QE purchases, and also providing UK banks with £100bn of cheap financing. The aim of this was to lower borrowing costs, stimulate demand for borrowing and thereby increase expenditure and demand in the economy. The MPC felt this was necessary in order to ward off their expectation that there would be a sharp slowdown in economic growth. Instead, the economy grew robustly, although the Governor of the Bank of England strongly maintained that this was because the MPC took that action. However, other commentators regard this emergency action by the MPC as being proven by events to be a mistake. Then in 2017, we had the Financial Policy Committee (FPC) of the Bank of England taking action in June and September over its concerns that cheap borrowing rates, and easy availability of consumer credit, had resulted in too rapid a rate of growth in consumer borrowing and in the size of total borrowing, especially of unsecured borrowing. It, therefore, took punitive action to clamp down on the ability of the main banks to extend such credit. Indeed, a Price Waterhouse Cooper (PWC) report in October 2017 warned that credit card, car and personal loans and student debt will hit the equivalent of an average of £12,500 per household by 2020. However, averages belie wide variations in levels of debt with much higher exposure being biased towards younger people, especially the 25 -34 year old band, reflecting their lower levels of real income and asset ownership.

One key area of risk is that consumers may have become used to cheap rates since 2008 for borrowing, especially for mortgages. It is a major concern that some consumers may have over extended their borrowing and have become complacent about interest rates going up after Bank Rate had been unchanged at 0.50% since March 2009 until falling further to 0.25% in August 2016. This is why forward guidance from the Bank of England continues to emphasise slow and gradual increases in Bank Rate in the coming years. However, consumer borrowing is a particularly vulnerable area in terms of the MPC getting the pace and strength of Bank Rate increases right - without causing a sudden shock to consumer demand, confidence and thereby to the pace of economic growth.

Moreover, while there is so much uncertainty around the Brexit negotiations, consumer confidence, and business confidence to spend on investing, it is far too early to be confident about how the next two to three years will actually pan out.

Eurozone

Economic growth in the Eurozone (EZ), (the UK's biggest trading partner), had been lack lustre for several years after the financial crisis despite the European Central Bank (ECB) eventually cutting its main rate to -0.4% and embarking on a massive programme of QE. However, growth picked up in 2016 and has now gathered substantial strength and momentum thanks to this stimulus. GDP growth was 0.6% in quarter 1 2017 (2.1% year on year), 0.7% in quarter 2 (2.4% year on year) and +0.7% in quarter 3 (2.8% year on year). However, despite providing massive monetary stimulus, the European Central Bank is still struggling to get inflation up to its 2% target and in December 2017 inflation was 1.4%. It is therefore unlikely to start on an upswing in rates until possibly 2019. It has, however, announced that it will slow down its monthly QE purchases of debt from €60bn to €30bn from January 2018 and continue to at least September 2018.

United States

Growth in the American economy was notably erratic and volatile in 2015 and 2016. This was replicated in 2017 with quarter 1 coming in at an annualised rate of only 1.2%, quarter 2 at 2.3%, quarter 3 at 3.1%, and quarter 4 at 2.6%. This gave an overall figure for annual growth in 2017 of 2.6%, an acceleration from 1.5% in 2016. Unemployment in the US has also fallen to the lowest level for seventeen years, reaching 4.1%, while wage inflation pressures and inflationary pressures in general have been building. The Fed has started on a gradual upswing in rates with five increases in all and three increases since December 2016; a further increase in December 2017 lifted the central rate from 1.25% to 1.50%. There could then be another four increases in 2018. At its September 2017 meeting, the Fed said it would start in October to gradually unwind its $4.5 trillion balance sheet holdings of bonds and mortgage backed securities by reducing its reinvestment of maturing holdings.

China

Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems.

Japan

GDP growth has been gradually improving during 2017 to reach an annual figure of 2.1% in quarter 3. However, it is still struggling to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.

Brexit

The anticipated timetable and process is as follows;

- March 2017: UK government notifies the European Council of its intention to leave under the Treaty on European Union Article 50
- March 2019: initial two-year negotiation period on the terms of exit. In her Florence speech in September 2017, the Prime Minister proposed a two year transitional period after March 2019.

- UK continues as a full EU member until March 2019 with access to the single market and tariff free trade between the EU and UK. Different sectors of the UK economy will leave the single market and tariff free trade at different times during the two year transitional period.
- The UK and EU would attempt to negotiate, among other agreements, a bi-lateral trade agreement over that period.
- The UK would aim for a negotiated agreed withdrawal from the EU, although the UK could also exit without any such agreements in the event of a breakdown of negotiations.
- If the UK exits without an agreed deal with the EU, World Trade Organisation rules and tariffs could apply to trade between the UK and EU - but this is not certain.
- On full exit from the EU: the UK parliament would repeal the 1972 European Communities Act.

On exit, the UK will then no longer participate in matters reserved for EU members, such as changes to the EU's budget, voting allocations and policies.

Appendix 4: Treasury Management Practice (TMP1) – Credit and Counterparty Risk Management

SPECIFIED INVESTMENTS: All such investments will be sterling denominated, with **maturities up to a maximum of 1 year**, meeting the minimum 'high' quality criteria where applicable.

NON-SPECIFIED INVESTMENTS: These are any investments which do not meet the specified investment criteria. A maximum of 50% will be held in aggregate in non-specified investment

A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the above categories.

The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

Specified Investments

	Minimum credit criteria / colour band	**** Max % of total investments/ £ limit per institution**	**Max. maturity period**
DMADF – UK Government Debt Management Account Deposit Facility	N/A	100%	6 months
UK Government gilts	UK sovereign rating	£20m	12 months
UK Government Treasury bills	UK sovereign rating	£20m	12 months
Bonds issued by multilateral development banks	AAA	£10m	6 months
Money Market Funds	AAA	£20m	Liquid
Enhanced Cash Funds with a credit score of 1.25	AAA	£20m	Liquid
Enhanced Cash Funds with a credit score of 1.5	AAA	£20m	Liquid
Local authorities	N/A	£20m	12 months
Term deposits with banks and building societies	Blue Orange Red Green No Colour	£20m £15m £10m £10m Not for use	12 months 12 months 6 months 100 days Not for use
CDs or corporate bonds with banks and building societies	Blue Orange Red Green No Colour	£20m £15m £10m £10m Not for use	12 months 12 months 6 months 100 days Not for use
Gilt funds	UK sovereign rating	£10m	12 months
REPO's (Collateralised deposit)	100% Collateral	£5m	12 months
GMCA	Internal Due Diligence	£30m	12 months

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

NON-SPECIFIED INVESTMENTS: A maximum of 50% will be held in aggregate in non-specified investments

Maturities in excess of 1 year

	* Minimum Credit Criteria	Use	£ limit per institution	Max. maturity period
Term deposits – local authorities and other public institutions	--	In-house	£10m	5 years
Term deposits – banks and building societies	Yellow Purple	In-house	£10m £10m	5 years 2 years
Certificates of deposit issued by banks and building societies	Yellow Purple	In-house	£10m £10m	5 years 2 years
Certificates of deposit issued by banks and building societies	Short-term F1 Long-term AA	Fund Managers	£5m	2 years
Collateralised deposit	UK sovereign rating	In-house and Fund Managers	£5m	2 years
UK Government Gilts	UK sovereign rating	In-house and Fund Managers	£10m	5 years
Bonds issued by multilateral development banks	AAA	In-house and Fund Managers	£10m	3 years
Sovereign bond issues (other than the UK Government)	AAA	In-house and Fund Managers	£5m	2 years
Corporate bonds	Short-termF1 Long-term AA	In-house and Fund Managers	£5m	5 years
Green Energy Bonds	Internal Due Diligence	In-house and Fund Managers	£10m	10 years
Property Funds	Internal Due Diligence	In-house	£30m	10 years
Floating Rate Notes	Long Term A	In-house	£5m	5 years
REPO's (Collateralised deposit)	100% Collateral	In-house	£5m	5 years
GMCA	Internal Due Diligence	In-house	£30m	5 years
Covered Bonds	Long term A	In-house	£5m	5 years
Local Capital Finance Company (Municipal Bonds Agency)	Internal Due Diligence	In-house	£1m	10 years
Local Authority Fixed Income Fund	Internal Due Diligence	In-house	£5m	10 years
Unrated Bonds, backed by securitised Assets	Internal Due Diligence	In-house and fund managers	£5m	5 years
Asset Backed Pooled Investment Funds	Internal Due Diligence	In-house and fund managers	£5m	5 years
Fixed term deposits with variable rate and variable maturities	Internal Due Diligence	In-house and External Advice	£20m	50 years

NON-TREASURY INVESTMENTS: The Council has already or may in the future undertake investments in non-treasury activities this may be via a number of routes as outlined in the table below which considers the minimum credit criteria, a maximum financial limit per category if appropriate and a maximum maturity period.

	* Minimum Credit Criteria	Use	£ limit per category	Max. maturity period
Loans made to third parties are investments – Adhoc loans including existing long term debtors	Service Delivery objectives	In-house	N/A To be determined based on business appraisal	40 years
Loans made to third parties are investments – LAMS – The Council as guarantor.	Service Delivery objectives	In-house	£5m	5 years
Investment Property – Property Purchased for service delivery/economic regeneration	Service Delivery objectives	In-house	N/A To be determined based on business appraisal	50 years
Investment Property – Property purchased solely for the generation of income.	Appraisal Criteria in line with the Council Commercial Property Investment Strategy	In-house, external specialist.	N/A To be determined based on business appraisal	50 years

APPENDIX 5: Approved Countries for Investments (as at February 2018)

AAA

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

AA+

- Finland
- U.S.A.

AA

- France
- U.K.

AA-

- Belgium

APPENDIX 6: Treasury Management Scheme of Delegation

The scheme of delegation is as follows:

Full Council is the responsible body for:

- receiving and reviewing reports on Treasury Management policies, practices and activities;
- the approval of the annual strategy, mid-year review and outturn report.
- approval of/amendments to the organisation's 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;

Cabinet is the responsible body for:

- considering the Treasury Management Policy and Procedures and making recommendations to the responsible body.
- considering Treasury Management reports and commending to Council.

Audit Committee is responsible for scrutiny:

- reviewing the Treasury Management Policy and Procedures and making recommendations to the responsible body.
- Reviewing Treasury Management reports and making recommendations to the responsible body.

Cabinet Member for Finance and HR is responsible for:

- approving the selection of external service providers and agreeing terms of appointment

APPENDIX 7: The Treasury Management Role of the Statutory Chief Finance Officer (Director of Finance)

The Statutory Chief Financial Officer will discharge the Treasury Management role by:

- recommending 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 Treasury 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 processes, and liaising with external audit;
- recommending the appointment of external service providers.