REPORT FOR:	**GOVERNANCE, AUDIT, RISK MANAGEMENT AND STANDARDS COMMITTEE**
Date of Meeting:	29 January 2019
Subject:	Treasury Management Strategy Statement including Prudential Indicators, Minimum Revenue Provision Policy Statement and Annual Investment Strategy for 2019/20 and Capital Strategy
Responsible Officer:	Dawn Calvert, Director of Finance
Exempt:	No
Wards affected:	All
Enclosures:	Appendix A – Legislation and Regulations Impacting on Treasury Management Appendix B – Treasury Management Delegations and Responsibilities Appendix C – Minimum Revenue Provision (MRP) Policy Statement Appendix D –Interest Rate Forecasts 2019/22 Appendix E - Economic Background Appendix F - Counterparties Appendix G - Affordability Prudential Indicators Appendix H Draft Capital Strategy 2019/20

Summary

This report sets out the Council's Treasury Management Strategy Statement including Prudential Indicators, Minimum Revenue Provision Policy Statement and Annual Investment Strategy 2019/20 and a new requirement, the Annual Capital Strategy.

Recommendation

The Committee is asked to review and comment on the Draft Annual Capital Strategy and Treasury Management Strategy Statement for 2019/20 including:

- Prudential Indicators for 2019/20
- Minimum Revenue Provision Policy Statement for 2019/20;
- Annual Investment Strategy for 2019//20

The Committee is asked to consider the draft Capital Strategy 2019/20 with a view to a final version being brought to the Committee in April 2019.

APPENDICES

Section 2 – Report

1. INTRODUCTION

1.1 Background

1. The Chartered Institute of Public Finance and Accountancy (CIPFA) defines Treasury Management 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.""

2. The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. The first main function 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 with approved low risk counterparties or in instruments commensurate with the Council's low risk appetite current investment strategy, providing adequate liquidity initially before considering investment return.

3. The second main function of the Treasury Management service is the funding of the Council's Capital Programme. This programme provides 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.

4. The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects.

5. The Local Government Act 2003 and supporting regulations require the Council to 'have regard to' the Prudential Code (The Prudential Code for Capital Finance in Local Authorities [CIPFA 2017 Edition]) and Treasury Management Code (Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes [CIPFA 2017 Edition]), in setting Treasury and Prudential Indicators for the next three years and in ensuring that the Council's capital investment programme is affordable, prudent and sustainable.

6. The Act, the Codes and Department for Communities and Local Government Investment Guidance (2010) require the Council to set out its Treasury Strategy for Borrowing and to prepare an Annual Investment Strategy that establishes the Council's policies for managing its

investments and for giving priority to the security and liquidity of those investments. A summary of the relevant legislation, regulations and guidance is included as Appendix A.

7. The budget for each financial year includes the revenue costs that flow from capital financing decisions. Under the Treasury Management Code, increases in capital expenditure should be limited to levels whereby increases in interest charges and running costs are affordable within the projected income of the Council for the foreseeable future.

8. The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.

9. The Council recognises that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

10. Revised reporting is required for the 2019/20 reporting cycle due to revisions of the Ministry of Communities and Local Government (MHCLG), Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a Capital Strategy, to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011. The Capital Strategy is set out in Appendix H

1.2 CIPFA Requirements

11. The CIPFA revised 2017 Prudential and Treasury Management Codes require, for 2019/20, all local authorities to prepare an additional report, a Capital Strategy, which will provide the following:

- a high-level long term 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

1.3 Capital Strategy

12. The Guidance notes to the Prudential Code state that “The purpose of the Capital Strategy is to tell a story that gives a clear and concise view of how a

local authority determines its priorities for capital investment, decides how much it can afford to borrow and sets its risk appetite.

13. The Capital Strategy is reported separately from the Treasury Management Strategy Statement. (TMSS) This ensures the separation of the core treasury function set under security, liquidity and yield. Principles as set out in the TMSS. The Capital Strategy reports on the Council's policy and activity on commercial investments

14. The draft Capital Strategy is attached at Appendix H. It is draft at this stage as the final Capital Programme is being finalised for February Cabinet. A revised Capital Strategy will be presented to GARMS in April 2019.

1.4 Reporting

15. The Council has formally adopted CIPFA'S Treasury Management Code, the primary requirements of which are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

- Creation and maintenance of Treasury Management Practices ("TMPs") that set out the manner in which the Council will seek to achieve those policies and objectives.

- Receipt by the full Council and/or Cabinet of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Half-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.

- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body.

16. As introduced above, the Council and/or Cabinet are required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

Treasury Management Strategy Statement report (this report) - The first, and most important report is presented to the Council in February and covers:

- The Capital Programme (including Prudential Indicators);
- An 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).

- **Mid-year Review report** – This is presented to Cabinet in the autumn and updates Members on the progress of the capital position, reporting on Prudential Indicators and recommending amendments when necessary and identifying whether the treasury strategy is meeting the objectives or whether any policies require revision.

- **Treasury Management Outturn report** – This is presented to Cabinet in June/July and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the Strategy.

- **Scrutiny -** The above reports are required to be adequately scrutinised, normally before being recommended to Cabinet / Council, with the role being undertaken by the Governance, Audit, Risk Management and Standards Committee (GARMSC). GARMSC

17. The Council has delegated responsibility for the implementation and regular monitoring of its treasury management policies and practices to the Section 151 officer. The Section 151 Officer chairs the Treasury Management Group (TMG), which monitors the treasury management activity and market conditions.

Further details of responsibilities are given in Appendix B.

1.5 Training

18. The Treasury Management Code requires the responsible officer to ensure that Members with responsibility for treasury management receive adequate training in this area. This especially applies to Members responsible for scrutiny.

19. The training needs of Treasury Management officers are periodically reviewed as part of the Learning and Development programme with appropriate training and support provided.

1.6 Treasury Management Adviser

20. The Council has engaged Link Asset Services (was Capita Asset Services) Treasury Solutions as its external Treasury Management Adviser.

21. 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 ensures that the terms of their appointment and the methods by which their value is assessed are properly agreed and documented, and subjected to regular review.

22. However, the Council recognises that responsibility for treasury management decisions remains with itself at all times and will ensure that undue reliance is not placed upon external service providers.

1.7 Treasury Management Strategy for 2019/20

23. The Treasury Management Strategy covers:-

Capital Issues (Section 2)

- Capital Financing Summary (Sub-section 2.1)
- Capital Programme and capital prudential indicators 2017/18 to 2020/21 (Sub-section 2.2);
- Capital Financing Requirement (Sub-section 2.3);
- Minimum Revenue Provision Policy Statement (Sub-section 2.3 and Appendix C); and
- Core funds and expected investment balances (Sub-section 2.5).

- **Treasury Management Issues**
- Borrowing (Section 3)
- Current and estimated portfolio position (Sub-section 3.1);
- Treasury indicators: limits to borrowing activity (Sub-section 3.2);
- Prospects for interest rates and economic commentary (Sub-section 3.3 and Appendices D and E);
- Borrowing strategy (Sub-section 3.4);
- Treasury management limits on activity (Sub-section 3.5);
- Policy on borrowing in advance of need (Sub-section 3.6); and
- Debt rescheduling (Sub-section 3.7).

- Annual Investment Strategy (Section 4)
- Investment policy (Sub-section 4.1);
- Creditworthiness policy (Sub-section 4.2);
- Country limits (Sub-section 4.3);
- Annual Investment Strategy (Sub-section 4.4);
- Investment risk benchmarking (Sub-section 4.5); and
- End of year investment report (Sub-section 4.6).

Affordability Prudential Indicators (Section 5 and Appendix G)

24. These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, Ministry of Housing, Communities a and Local Government (MHCLG) MRP Guidance, the CIPFA Treasury Management Code and MHCLG Investment Guidance.

25. It is not considered necessary to produce a separate treasury strategy for the Housing Revenue Account (HRA) in light of the co-mingling of historic debt

and investments between HRA and the General Fund. Where appropriate, details of allocations of balances and interest to HRA are contained in this report.

1.8 Options Considered

26. No options were considered beyond those discussed in the report due to the statutory and risk management constraints inherent in treasury management.

2. Capital Issues

2.1 Capital Financing Summary

27. The Council's capital expenditure programme is the key driver of treasury management activity. The output of the programme is reflected in the Prudential Indicators, which are required by the Prudential Code and are designed to assist Members' overview. The values shown in the tables for 2017/18 and 2018/19 are actual and estimated outturn respectively and not the strategy for those years.

28. The figures and tables in this report are based on the draft Capital Programme presented to December 2018 Cabinet and will be revised to reflect the final programme which will be taken to February Cabinet.

29. In previous years the Council had deferred the requirement to take external borrowing to finance the Capital Programme by using internal borrowing; reducing cash balances to finance capital expenditure to minimise the cost of borrowing. In 2018/19 £63.750m external borrowing is required to finance the Capital Programme. As at 31 December 2018, £25m of short-term external borrowing had been taken to finance the Capital Programme. Hence £38.75m of additional borrowing will be required if the programme is spent to plan. Short-term borrowing is cost-efficient but not sustainable in the longer term and needs to be replaced by long-term borrowing.

30. The 2018/19 revenue budget, in respect of the capital financing cost of the existing Capital Programme 2018/19 to 2020/21 is £24.601m. This figure of £24.6m will also relate to the cost of historic capital programme spend prior to 2018/19. £24.6m is approximately 15% of the net revenue budget of £168.9m.

31. Shown below are the capital financing costs that are already factored into the existing MTFS from 2018/19 to 2021/22 in relation to existing and historic capital programmes again expressed as a proportion of the 2018/19 net revenue budget of £168.9m:

2018/19	£24.6m (15%)
2019/20	£32.6m (19%)
2020/21	£33.8m (20%)
2021/22	£35.7m (21%)

32. The above figures are gross capital financing costs. Where are schemes are included in the Capital Programme on a cost neutral basis (i.e. capital financing costs are covered by income generation or savings) the income or saving will be included elsewhere in the budget.

33. From 2019/20 onwards all of the capital programme will need to be financed in-year from external borrowing Wherever practical PWLB annuity loans will be taken to ensure that the loan is repaid over the lifetime of the asset to manage the on-going debt burden on the Council.

Capital Programme and Capital Prudential Indicators 2017/18 to 20/21

34. Table 1 sets out a summary of the Council's capital expenditure based on the approved Capital Programme and the way in which it will be financed. Amendments may be necessary in the light of decisions taken during the budget

Table 1 Capital Expenditure and Funding

	2017/18	2018/19	2019/20	2020/21
	Actual	**Estimate**	**Estimate**	**Estimate**
	£'000	**£'000**	**£'000**	**£'000**
Expenditure				
Community	39,158	45,347	28,160	14,373
People Services	18,098	12,841	7,200	-
Regeneration & Enterprise		183	726	201
Regeneration Programme	15,255	6,480	17,902	4,721
Resources & Commercial	9,743	11,184	5,700	4,700
HRA	11,877	9,932	34,033	44,462
Total Expenditure	**94,131**	**85,967**	**93,720**	**68,457**
Funding:-				
Capital grants	13,309	11,091	17,350	13,228
Capital receipts	8,137	3,382	1,277	7,025
Regeneration Capital Receipts			4,290	
Revenue financing	8,753	6,928	7,025	8,421
Section 106 / Section 20/ CIL	5,456	816	2,464	6,175
Total Funding	**35,655**	**22,217**	**32,407**	**34,849**
Net financing need for the year (Borrowing)	**58,476**	**63,750**	**61,313**	**33,608**

cycle:

2.3 Capital Financing Requirement

35. The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). The CFR arises directly from the capital activity of the Council and the resources applied to fund the capital spend, and represents the unfinanced element of capital expenditure. Any new capital expenditure, which has not immediately been paid for, will increase the CFR.

36. The CFR includes any other long term liabilities (e.g. finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement,

these types of scheme include a funding facility and so the Council is not required to borrow separately for them. The Council currently has £15.6 of such schemes within the CFR.

CFR projections are included in the table below.

Table 2 Capital Financing Requirement

	2017/18	2018/19	2019/20	2020/21
	Actual	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000
CFR as at 31 March				
Non – HRA	343,209	383,327	399,429	383,028
HRA	151,015	150,046	162,622	178,859
TOTAL	**494,224**	**533,373**	**562,050**	**561,887**
Movement in CFR	**34,576**	**39,149**	**28,677**	**- 164**

Movement in CFR represented by				
Net financing need for the year	58,476	63,750	61,313	33,608
Less Minimum/Voluntary revenue provision and other financing movements	**- 23,900**	**- 24,601**	**- 32,636**	**- 33,772**
Movement in CFR	**34,576**	**39,149**	**28,677**	**- 164**

37. A key aspect of the regulatory and professional guidance is that elected members are aware of the size and scope of any commercial activity in relation to the authority's overall financial position. The Councils commercial property investments made to 31 March 2019 totals £17m which represents less than 5% of the Non-HRA CFR, and shows that the scale of commercial activity is proportionate to the Authority's remaining activity.

38. The Non-HRA CFR moves from £383.327m in 2018/19 to £383.028m in 2020/21, reflecting increased MRP required to finance the Capital Programme.

2.4 Minimum Revenue Provision (MRP) Policy Statement

39. Capital expenditure is generally defined as expenditure on assets that have a life expectancy of more than one year e.g. buildings, vehicles, machinery etc. The accounting approach is to spread the cost over the estimated useful life of the asset. The mechanism for spreading these costs is through an annual MRP. The MRP is the means by which capital expenditure, which is financed by borrowing or credit arrangements, is funded by Council Tax.

40. Regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (as amended) require the Council to approve an MRP Statement setting out what provision is to be made in the General Fund for the repayment of debt, and how the provision is to be calculated. The purpose of the Statement is to ensure the provision is prudent, allowing the debt to be repaid over a period reasonably commensurate with that over which the capital expenditure benefits. The Council is recommended to approve the statement as detailed in Appendix C.

41. There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made.

42. MRP Overpayments - A change introduced by the revised MHCLG MRP Guidance was the allowance that any charges made over the statutory MRP, voluntary revenue provision or overpayments, can, if needed, be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, it is recommended to disclose the cumulative overpayment made each year in a disclosure statement to full Council.

2.5 Core funds and expected investment balances

43. The application of resources (grants, capital receipts etc.) to finance capital expenditure or budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.).

44. The Cash investment balance will be kept at approximately £30m. The working capital and borrowing position will be managed to maintain this level of cash balances.

3. BORROWING

45. The capital expenditure programme set out in Table 1 provides details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet the activities of the Council. This involves both the organisation of the cash flow and, where the Capital Programme requires it, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury indicators, the current and projected debt positions and the annual investment strategy.

3.1 Current and estimated portfolio position

46. The Council's borrowing position at 31 December 2018 is summarised below.

Table 3 Summary Borrowing and Investment Position at 31 December 2018

		Principal		Ave. rate
		£m	£m	%
Fixed rate funding	PWLB	248.4		
	Market	76.0	324.4	4.03
Temporary borrowing			25.0	0.83
Other long term liabilities (PFI & leases)			15.6	
Total Debt			**365.0**	
Total Investments at 31.12.2018			**28.5**	**0.39**

47. The Council has borrowed £20.8m under Lender Option, Borrower Option (LOBO) structures maturing in 2077. In exchange for an interest rate that was below that offered on long term debt by the PWLB, the lender has the option at the end of five years (and half yearly thereafter) to reset the interest rate. If the rate of interest changes, the Council is permitted to repay the loan at no additional cost.

48. The Council's borrowing position with forward projections is summarised below. Table 4 shows the actual external debt, against the underlying capital borrowing need, highlighting any under or over borrowing.

49.The expected change in debt in 2018/19, 2019/20 and 2020/2021 reflects the anticipated borrowing necessary to meet the Capital Programme described in Table 1.

50.Debt outstanding should not exceed CFR.

Table 4 Changes to Gross Debt

`	2017/18	2018/19	2019/20	2020/21
	Actual	**Estimate**	**Estimate**	**Estimate**
	£'000	**£'000**	**£'000**	**£'000**
External Debt				
Debt at 1 April	334,434	324,434	388,184	449,497
Expected change in Debt	- 10,000	63,750	61,313	33,608
Other long-term liabilities (OLTL) 1st April	17,032	15,600	14,168	13,736
Expected change in OLTL	- 1,032	- 1,432	- 1,432	- 432
Actual gross debt at 31 March	340,434	402,352	462,233	496,409
Capital financing requirement	494,224	533,373	562,050	561,887
Under / (Over) borrowing	**153,790**	**131,021**	**99,817**	**65,478**

51. Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2019/20 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Director of Finance reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future.

52. This view takes into account current commitments, existing programmes and the proposals in the budget report.

3.2 Treasury indicators: limits to borrowing activity

The Operational Boundary

53. This is the limit which external debt is not normally expected to exceed.

54. The boundary is based on the Council's programme for capital expenditure, capital financing requirement and cash flow requirements for the year.

The Authorised Limit for External Debt.

55. This is a further key prudential indicator which represents a control on the maximum level of borrowing. It represents a limit beyond which external debt is prohibited. It relates to the financing of the Capital Programme by both external borrowing and other forms of liability, such as credit arrangements.

56. 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' programmes, or those of a specific council, although this power has not yet been exercised.

Table 5 Operational boundary and authorised limit (Non HRA and HRA)

	2017/18	2018/19	2019/20	2020/21
	Actual	Estimate	Estimate	Estimate
	£m	£m	£m	£m
Authorised Limit for external debt				
Borrowing and finance leases	494	533	562	562
Operational Boundary for external debt				
Borrowing	340	432	492	526
Other long term liabilities	17	16	16	15
Total	357	448	508	541
Upper limit for fixed interest rate exposure				
Net principal re fixed rate borrowing	340	432	492	526
Upper limit for variable rate exposure				
Net principal re variable rate borrowing	-	-	-	-
Upper limit for principal sums invested over 364 days	60	60	60	60

57. Due to the Council's current under borrowing position it is considered sufficient to set the Authorised limit at the same level as the CFR.

58. As shown in Table 5 above and in Appendix F : Counterparties, the Council may wish to make additional investments of over 365 days. The current limit for such investments is £60m.

HRA Debt Limit

59. Separately, the Council was also limited to a maximum HRA debt through the HRA self-financing regime. This limit and the HRA CFR are shown in the table 6 below.

Table 6 HRA Debt Limit and CFR

	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
CFR as at 31 March							
Non – HRA							
HRA	151,015	150,046	162,622	178,859	201,881	231,451	230,909
TOTAL	**151,015**	**150,046**	**162,622**	**178,859**	**201,881**	**231,451**	**230,909**
Movement in CFR	**1,477**	**- 969**	**12,576**	**16,237**	**23,022**	**29,570**	**- 541**

60. In October 2018 the Government announced the abolition of the HRA debt cap. The Chancellor announced in the Budget that the applicable date was 29.10.18.

3.3 Prospects for interest rates and economic commentary

61. The Treasury Management Adviser has provided a commentary on the prospects for interest rates, (Appendix D) and an economic background, (Appendix E).

3.4 Borrowing strategy

62. As shown in Table 3 (para 46), currently the Council has a debt portfolio of £349.4m. This includes £324.4m of long-term borrowing, with an average maturity of 35 years assuming no early repayment of the LOBO loans. Adjusting LOBO loans maturity in line with the next interest reset date, reduces the average maturity to 25 years. Cash balances at 31 December 2018 were £28.5m. With the investment portfolio yielding 0.39% and the likely average cost of new long term borrowing currently at 2.6%, there is a substantial short term cost of carrying excessive debt.

63. The Council is currently maintaining an under-borrowed position. This means that the capital financing requirement has not been fully funded with loan debt as internal cash balances have been used. This strategy was prudent with investment returns low and counterparty risk is still an issue to be considered.

64. From 2018/19 all of the £63.750m Capital Programme borrowing requirement will need to be funded through external borrowing. As set out in Table 4 (para.50), current draft estimates show that £61.313m will need to be borrowed in 2019/20 and £33.608m in 2020/21.The Council will have a range of funding sources available and will need to base its decisions on optimum borrowing times and periods taking into account current interest rates and likely future movements and the “cost of carry” (difference between rates for borrowing and rates for investments).

65. It is also possible, but unlikely, that new long term borrowing in the next three years might be required if the remaining LOBO loans have to be refinanced early.

66 It may be necessary to use temporary borrowing from the money markets or other local authorities to cover mismatches in timing between capital grants and payments. However, with several Government grants now paid early in the financial year and robust daily monitoring of the cash flow position, the facility is not very likely.

67. Temporary short-term borrowing has been used to defer the higher cost of long-term borrowing. As at 31st December 2018, £25 million short-term borrowing has been used to finance the 2018/19 Capital Programme. In total up to £63.750 million capital borrowing is required in 2018/19. Short term borrowing though more cost-efficient, is not sustainable in the longer term and will need to be replaced by long-term borrowing from early in 2019/20.

68 To accelerate the repayment of debt and to reduce the CFR, PWLB annuity loans will be taken in future to ensure the equal instalment of principle over the life time of the loan.

69. Against this background and the risks within the economic forecast, caution will be adopted in the 2019/20 treasury management operations. The Treasury Management Group will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances. This incudes taking advice from Link Treasury Management Advisers.:

- If it was felt that there was a significant risk of a sharp fall in long and short term rates (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed. There is limited scope for debt rescheduling because of the high cost of early redemption of debt.

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

70. The Council has to date adopted a single pooled approach for debt. Allocations to HRA are based on its CFR, with interest charged to HRA at the average rate on all external borrowing. Longer term, the HRA's ability to repay borrowing will depend on future revenues and the capital expenditure programme. New HRA debt taken from 2019/20 will be maintained in a separate pool.

3.5 Treasury management limits on activity

71. There are three debt related treasury activity limits. The purpose of these is 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 and improve performance.

Upper limit on variable interest rate exposure

72. This identifies a maximum limit for variable interest rates based upon the debt position net of investments. As shown in Table 5 (para. 57), the Council does not expect to undertake any borrowing on this basis.

Upper limit on fixed interest rate exposure

73. This identifies a maximum limit for fixed interest rates based upon the debt position net of investments. The Council's proposed limits are shown in Table 5

Maturity Structure of Borrowing

74. 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.

75 The Council has no variable rate borrowing and the comments below relate only to its fixed rate portfolio.

76. In the table below, the maturity structure for the LOBO debt, in accordance with CIPFA Guidance, is shown as the first date that the interest rate can be increased.

Table 7 Maturity Structure of Fixed Rate Borrowing

	As at 31.12.2018 %	Upper limit %	Lower limit %
Under 12 months	13%	30	0
12 months to 23 months	0%	20	0
24 months to under 5 years	2%	30	0
5 years to under 10 years	3%	40	0
10 years and over	82%	100	30

3.6 Policy on borrowing in advance of need

77. 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 future authorised limits, 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.

78. 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 rescheduling

79. Link Asset Services currently advise that:

80. *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).

81. 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).*

82. Opportunities to reduce the cost of debt by premature repayment or to improve the maturity profile are kept under review in discussion with the Treasury Management Adviser. Early repayment of market loans is by negotiation. For PWLB loans, there are daily published prices for early repayment that allows analysis of the opportunities for restructuring. There is currently a spread which has generally made restructuring uneconomic.

83. Should the LOBO loan with interest rate reset dates in 2019/20 (£20.8m) require refinancing, the most likely source would be external borrowing.

84. All rescheduling will be reported to Cabinet at the earliest meeting following the exercise.

4. Annual Investment Strategy

4.1 Investment policy

85. MHCLG and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with financial investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy.

86. The Council's investment policy has regard to the following: -
- MHCLG's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the Code")
- CIPFA Treasury Management Guidance Notes 2018
- The Council's investment priorities will be security first, liquidity second and then return

87. The above guidance from the MHCLG and CIPFA places a high priority on the management of risk. This authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

- Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.

- **Other information:** 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.

88. This authority has defined the list of **types of investment instruments** that the treasury management team are authorised to use. There are two lists in Appendix F Counterparties, under the categories of 'specified' and 'non-specified' investments:

- **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.

- **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.

89. As a result of the change in accounting standards for 2018/19 under IFRS 9, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the Ministry of Housing, Communities and Local Government, [MHCLG], concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years commencing from 1.4.18.)

90. However, this authority will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance, (see paragraph 4.5). Regular monitoring of investment performance will be carried out during the year.

4.2 Creditworthiness policy

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

92. 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; and

93. 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.
94. The Director of Finance 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. These criteria are separate to those which determine which types of investment instrument are either specified or non-specified as they provide an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

94. The minimum rating criteria uses 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, and the institution will fall outside the lending criteria.

95 Credit rating information is supplied by the Treasury Management Adviser on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty 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 at the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions.

96. The Council's criteria for an institution to become counterparty are detailed in Appendix F.

4.3 Country Limits

97. The Council has determined that it will only use approved counterparties from the UK or from countries with a minimum sovereign credit rating of AA-. The current UK rating is the third level of AA. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

4.4 Annual Investment Strategy

98. In-house funds. The Council's funds are mainly cash derived primarily from the General Fund and HRA. Balances are also held to support capital expenditure. Investments are 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).

99.Since April 2011, pension fund cash balances have been held separately from those of the Council. However, a separate investment strategy has not been developed for the pension fund and all its cash is held on overnight call account with RBS and in separate money market funds.

100. Investment returns expectations. On the assumption that the UK and EU agree a Brexit deal in spring 2019, then Bank Rate is forecast by Link Asset Services to increase steadily but slowly over the next few years to reach 2.00% by quarter 1 2022. Bank Rate forecasts for financial year ends (March) are:

2018/19 0.75%
2019/20 1.25%
2020/21 1.50%
2021/22 2.00%

101. Link Asset Services suggest that budgeted investment earnings rates for returns on investments placed for periods of up to 100 days during each financial year are as follows:

2018/19	**0.75%**
2019/20	**1.00%**
2020/21	**1.50%**
2021/22	**1.750%**
2022/23	**1.75%**
2023/24	**2.00%**
Later years	**2.55%**

102. Link Asset Services further advise that "The overall balance of risks to economic growth in the UK is probably neutral. The balance of risks to increases in Bank Rate and shorter term PWLB rates, are probably also even and are dependent on how strong GDP growth turns out, how slowly inflation pressures subside, and how quickly the Brexit negotiations move forward positively.

103. Investment treasury indicator and limit - total principal funds invested for greater than 365 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment. The Council's limit for investments of over 365 days is currently £60m.

104. Interest rates receivable for short term investments have increased slightly since the base rate step increases in November 2017 The Council's return for the whole year is likely to be close to 0.5%. Whilst this is still above the short term LIBOR benchmark and comparable to peer authorities it represents a substantial reduction from rates earned in previous years.

105. As a result of the Council's strategy and the interest rates available the only counterparties actively in use during 2018/19 have been Lloyds, Royal Bank of Scotland Group and Svenska Handelsbanken. The investment portfolio has inevitably remained concentrated with RBS and Lloyds with 82.5% of the total portfolio invested with them on 31st December 2018. When opportunities arise consistent with the Council's policies diversification will be sought but it is not anticipated that there will be any significant change during 2019/20.

106. Authority has been given to place funds in ‘non-standard investments’ up to a value of £10m. Officers are considering what investment opportunities and counterparties should be included to utilise this facility.

4.5 Investment risk benchmarking

107. This Council uses the current LIBOR rates as a benchmark to assess the investment performance of its investment portfolio. In addition the Council is a member of a Link Asset Services investment portfolio benchmarking group through which performance is measured against peer London authorities. The risk of default attached to the Council’s portfolio is reported by Capita on a monthly basis.

4.6 End of year investment report

108. At the end of the financial year the Council will report on its investment activity as part of the Treasury Management Outturn Report.

5 Affordability Prudential Indicators

109. The previous sections cover the overall capital and control of borrowing Prudential Indicators but within this framework Prudential Indicators are also required to assess the affordability of the capital investment programme. These provide an indication of the impact of the programme on the Council’s overall finances and are shown in detail in Appendix G.

6 Implications of the recommendations

110. The recommendations primarily relate to the requirements for the Council to comply with statutory duties. However, the content of the report, covering borrowing and investment strategy, has implications for the Council’s ability to fund its capital projects and revenue activities.

111. The recommendations do not directly affect the Council’s staffing/workforce.

7 Performance issues

112. The Council meets the requirements of the CIPFA Treasury Management Code and, therefore, is able to demonstrate best practice for the Treasury Management function.

113. As part of the Code the Council must agree a series of prudential indicators and measure its performance against them. Success is measured by compliance with the indicators and the accuracy of future estimates so far as they are within the control of the Treasury Management function.

.

8 Environmental implications

114. There are no direct environmental implications.

9 Risk management implications

115. The identification, monitoring and control of risk are central to the achievement of treasury management objectives and to this report. Potential risks are identified, mitigated and monitored in accordance with Treasury Management Practice Notes approved by the Treasury Management Group.

116. Risks are included in the Directorate Risk Register as part of the overall MTFS risk.

10 Legal Implications

117. The purpose of this report is to comply with the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 and other relevant guidance referred to in the report.

11 Financial implications

118. Financial matters are integral to the report.

12 Equalities implications / Public sector equality duty

119. Officers have considered possible equalities impact and consider that there is no adverse equalities impact as there is no direct impact on individuals

13 Council priorities

120. This report deals with the Treasury Management Strategy which plays a significant part in supporting the delivery of all the Council's corporate priorities.

Section 3 - Statutory Officer Clearance

Name: Dawn Calvert Date: 25 January 2019	✓	Director of Finance
Name: Caroline Eccles Date: 25 January 2019	✓	on behalf of the Monitoring Officer

Ward Councillors notified:	**No**
EqIA carried out: **EqIA cleared by:**	**No** **N/A**

Section 4 - Contact Details and Background Papers

Contact: Iain Millar (Treasury and Pensions Manager) Tel: 020-8424-1432/ Email: iain.millar@harrow.gov.uk

Background Papers: N/A

APPENDIX A

LEGISLATION AND REGULATIONS IMPACTING ON TREASURY MANAGEMENT

The following items numbered 1 - 4 show the sequence of legislation and regulation impacting on the treasury management function. The sequence begins with primary legislation, moves through Government guidance and Chartered Institute of Public Finance and Accountancy (CIPFA) codes of practice and finishes with implementation through the Council's own Treasury Management Practices.

1. Local Government Act 2003

Link below

Local Government Act 2003

Below is a summary of the provisions in the Act dealing with treasury management.

In addition the Secretary of State is empowered to define the provisions through further regulations and guidance which he has subsequently done through statutory instruments, Department of Communities and Local Government Guidance and CIPFA codes of practice.

Power to borrow
The Council has the power to borrow for purposes relevant to its functions and for normal treasury management purposes – for example, to refinance existing debt.

Control of borrowing
The main borrowing control is the duty not to breach the prudential and national limits as described below.
The Council is free to seek loans from any source but is prohibited from borrowing in foreign currencies without the consent of Treasury, since adverse exchange rate movements could leave it owing more than it had borrowed.
All of the Council's revenues serve as security for its borrowing. The mortgaging of property is prohibited.
It is unlawful for the Council to 'securitise', that is, to sell future revenue streams such as housing rents for immediate lump-sums.

Affordable borrowing limit
The legislation imposes a broad duty for the Council to determine and keep under review the amount it can afford to borrow. The Secretary of State has subsequently defined this duty in more detail through the Prudential Code produced by CIPFA, which lays down the practical rules for deciding whether borrowing is affordable.
It is for the Council (at a meeting of the full Council) to set its own 'prudential' limit in accordance with these rules, subject only to the scrutiny of its external auditor. The Council is then free to borrow up to that limit without Government

consent. The Council is free to vary the limit during the year, if there is good reason.

Requirements in other legislation for the Council to balance its revenue budget prevent the long-term financing of revenue expenditure by borrowing.
However the legislation does confer limited capacity to borrow short-term for revenue needs in the interests of cash-flow management and foreseeable requirements for temporary revenue borrowing are allowed for when borrowing limits are set by the Council.

The Council is allowed extra flexibility in the event of unforeseen needs, by being allowed to increase borrowing limits by the amounts of any payments which are due in the year but have not yet been received.

Imposition of borrowing limits
The Government has retained reserve power to impose 'longstop' limits for national economic reasons on all local authorities' borrowing and these would override authorities' self-determined prudential limits. Since this power has not yet been used the potential impact on the Council is not known.

Credit arrangements
Credit arrangements (e.g. property leasing, PFI and hire purchase) are treated like borrowing and the affordability assessment must take account not only of borrowing but also of credit arrangements. In addition, any national limit imposed under the reserve powers would apply to both borrowing and credit.

Power to invest
The Council has the power to invest, not only for any purpose relevant to its functions but also for the purpose of the prudential management of its financial affairs.

2. Department for Communities and Local Government Investment Guidance (March 2010)

The Local Government Act 2003 requires a local authority "…..to have regard (a) to such guidance as the Secretary of State may issue…………..'' and the current guidance became operative on 1 April 2010.

The Guidance recommends that for each financial year the Council should prepare at least one investment Strategy to be approved before the start of the year. The Strategy must cover:

- **Investment security**
  Investments should be managed prudently with security and liquidity being considered ahead of yield
  Potential counterparties should be recognised as "specified" and "non-specified" with investment limits being defined to reflect the status of each counterparty

- **Investment risk**
  Procedures should be established for monitoring, assessing and mitigating the risk of loss of invested sums and for ensuring that such sums are readily accessible for expenditure whenever needed.
  The use of credit ratings and other risk assessment processes should be explained

The use of external advisers should be monitored

The training requirements for treasury management staff should be reviewed and addressed

Specific policies should be stated as regards borrowing money in advance of need

- **Investment Liquidity**
  The Strategy should set out procedures for determining the maximum periods for which funds may prudently be committed

The Strategy should be approved by the full Council and made available to the public free of charge. Subject to full Council approval, or approved delegations, the Strategy can be revised during the year.

3. Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes (CIPFA 2017)

The primary requirements of the Code are:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

- Creation and maintenance of Treasury Management Practices ("TMPs") that set out the manner in which the Council will seek to achieve those policies and objectives.

- Receipt by the full Council or Cabinet of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Half-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.

- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body.

4. CIPFA Code of Practice on Treasury Management 2017

- **CIPFA Prudential Code 2017**
- **CIPFA Treasury Management in the Public Services Guidance Notes 2018**
- **CIPFA statement 17.10.18 on borrowing in advance of need and investments in commercial properties**
- **CIPFA Bulletin 02 Treasury and Capital Management Update October 2018**
- **Statutory investment guidance where it has been updated in 2018 *(English local authorities)***
- **Statutory MRP guidance where it has been updated in 2018 *(English local authorities)***

The main objective of the above was to respond to the major expansion of local authority investment activity over the last few years into the purchase of non-financial investments, particularly property. This development has raised several concerns: -

- A local authority should define its risk appetite and its governance processes for managing risk.
- A local authority should assess the risks and rewards of significant investments over the long term, as opposed to the usual three to five years that most local authority financial planning has been conducted over, in order to ensure the long term financial sustainability of the authority. (CIPFA has not defined what longer term means but it is likely to infer 20-30 years in line with the financing time horizon and the expected life of the assets, while medium term financial planning, at a higher level of detail, is probably aimed at around a 10 year time frame and to focus on affordability in particular.)
- The Prudential Code has also expressed concern that local authorities should ensure that an authority's approach to commercial activities should be proportional to its overall resources.
- A local authority should have access to the appropriate level of expertise to be able to operate safely in all areas of investment and capital expenditure, and to involve members adequately in making properly informed decisions on such investments.

Consequently, the Prudential Code 2017 introduced a new requirement for local authorities to produce an annual Capital Strategy.

Compliance with the objectives of the Code by the Council should ensure that:

- Capital expenditure plans are affordable in terms of their implications on Council Tax and housing rents
- External borrowing and other long term liabilities are within prudent and sustainable levels
- Treasury management decisions are taken in accordance with good professional practice

As part of the two codes of practice above the Council is required to:

- agree a series of prudential indicators against which performance is measured
- produce Treasury Management Practice Notes for officers which set out how treasury management policies and objectives are to be achieved and activities controlled.

APPENDIX B

TREASURY MANAGEMENT DELEGATIONS AND RESPONSIBILITIES

The respective roles of the Council, Cabinet, GARMSC, the Section 151 officer, the Treasury Management Group the Treasury and Pensions Manager and the Treasury Team are summarised below. Further details are set out in the Treasury Management Practices.

Council

Under the Constitution, the Council is responsible for "decisions relating to the control of the Council's borrowing requirement."

It agrees the annual Treasury Management Strategy Statement including Prudential Indicators, Minimum Revenue Provision Policy Statement and Annual Investment Strategy.

Cabinet

Under the Constitution, the Cabinet "will exercise all of the local authority functions which are not the responsibility of any other part of the local authority, whether by law or under this Constitution."

It considers and recommends to Council the annual Treasury Management Strategy Statement and receives a mid-year report and annual outturn report on Treasury Management activities.

Governance, Audit, Risk Management and Standards Committee

GARMSC reviews the Treasury Management Strategy and monitors progress on treasury management in accordance with CIPFA codes of practice.

Director of Finance (Section 151 Officer)

Under S151 of the Local Government Act 1972 the Council "shall make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs." At Harrow, this responsibility is exercised by the Director of Finance.

The Director is responsibility for implementing the policies agreed by the Council and Cabinet.

Under the Local Government Finance Act 1988 and the Local Government Act 2003 the Director also has responsibilities in respect of budget arrangements and the adequacy of resources. In terms of Treasury Management this means that the financing costs of the Capital Programme are built into the Revenue Budget as are any assumptions on investment income.

The Director chairs the Treasury Management Group and agrees major treasury management decisions, specifically including any borrowing decisions, delegated to officers.

Treasury Management Group

Comprises Director of Finance, Head of Strategic and Technical Finance (Deputy S151 Officer), Treasury and Pensions Manager, Senior Finance Officer and is responsible for:

- Monitoring treasury management activity against approved strategy, policy, practices and market conditions;
- Ensuring that capital expenditure plans are continually reviewed in line with budget assumptions throughout the year to forecast when borrowing will be required.
- Approving changes to treasury management practices and procedures;
- Reviewing the performance of the treasury management function using benchmarking data on borrowing and investment provided by the Treasury Management Adviser (Link Asset Services Asset Services);
- Monitoring the performance of the appointed Treasury Management Adviser and recommending any necessary actions
- Ensuring the adequacy of treasury management resources and skills and the effective division of responsibilities within the treasury management function;
- Monitoring the adequacy of internal audit reviews and the implementation of audit recommendations

Treasury and Pensions Manager

Responsible for the execution and administration of treasury management decisions, acting in accordance with the Council's Treasury Management Strategy Statement and CIPFA's "Standard of Professional Practice on Treasury Management"

Treasury Team

Headed by Senior Finance Officer with responsibility for day-to-day treasury and investment and borrowing activity in accordance with approved Strategy, policy, practices and procedures and for recommending changes to the Treasury Management Group

APPENDIX C

Minimum Revenue Provision (MRP) Policy Statement

- For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will be the equal annual reduction of 2% of the outstanding debt at 1 April 2015 for the subsequent 50 years.

- For all capital expenditure financed from unsupported (prudential) borrowing (including PFI and finance leases), MRP will be based upon an asset life method in accordance with Option 3 of the guidance.

- In some cases where a scheme is financed by prudential borrowing it may be appropriate to vary the profile of the MRP charge to reflect the future income streams associated with the asset, whilst retaining the principle that the full amount of borrowing will be charged as MRP over the asset's estimated useful life.

- The regulations allows the Council to charge VMRP, which can be used to reduce future MRP by the same amount. A change introduced by the revised MHCLG MRP Guidance is that the voluntary MRP must be disclosed in a statement to the full council in order to reclaim it in future years as deemed necessary and prudent. Up until 31 March 2018, the total VMRP was £10.6m.

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

- Freehold land cannot properly have a life attributed to it, so for the purposes of Asset Life method it will be treated as equal to a maximum of 50 years. But if there is a structure on the land which the authority considers to have a life longer than 50 years, that same life estimate will be used for the land.

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

- Repayments included in annual PFI or finance leases are applied as MRP.

- Where borrowing is undertaken for the construction of new assets, MRP will only become chargeable once such assets are completed and operational.

- Under Treasury Management best practice the Council may decide to defer borrowing up to the capital financing requirement (CFR) and use internal resources instead. Where internal borrowing has been used, the amount chargeable as MRP may be adjusted to reflect the deferral of actual borrowing.

Provided by Link Asset Services Asset Services at January 2019

Interest Rate Forecasts 2019 - 2022

The Council has appointed Link Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives our central view.

Link Asset Services Interest Rate View	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%	1.50%	1.75%	1.75%	1.75%	2.00%
3 Month LIBID	0.90%	1.00%	1.10%	1.20%	1.30%	1.40%	1.50%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%
6 Month LIBID	1.00%	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%
12 Month LIBID	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%	2.30%	2.40%
5yr PWLB Rate	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%	2.60%	2.60%	2.70%	2.80%	2.80%
10yr PWLB Rate	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%
25yr PWLB Rate	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%	3.50%	3.50%	3.60%	3.60%
50yr PWLB Rate	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.40%

The flow of generally positive economic statistics after the quarter ended 30 June meant that it came as no surprise that the MPC came to a decision on 2 August to make the first increase in Bank Rate above 0.5% since the financial crash, from 0.5% to 0.75%. Growth became increasingly strong during 2018 until slowing significantly during the last quarter. At their November quarterly Inflation Report meeting, the MPC left Bank Rate unchanged, but expressed some concern at the Chancellor's fiscal stimulus in his Budget, which could increase inflationary pressures. However, it is unlikely that the MPC would increase Bank Rate in February 2019, ahead of the deadline in March for Brexit. On a major assumption that Parliament and the EU agree a Brexit deal in the first quarter of 2019, then the next increase in Bank Rate is forecast to be in May 2019, followed by increases in February and November 2020, before ending up at 2.0% in February 2022.

The overall longer run future trend is for gilt yields, and consequently PWLB rates, to rise, albeit gently. However, over about the last 25 years, we have been through a period of falling bond yields as inflation subsided to, and then stabilised at, much lower levels than before, and supported by central banks implementing substantial quantitative easing purchases of government and other debt after the financial crash of 2008. Quantitative easing, conversely, also caused a rise in equity values as investors searched for higher returns and purchased riskier assets. In 2016, we saw the start of a reversal of this trend with a sharp rise in bond yields after the US Presidential election in November 2016, with yields then rising further as a result of the big increase in the US government deficit aimed at stimulating even stronger economic growth. That policy change also created concerns around a significant rise in inflationary pressures in an economy which was already running at remarkably low levels of unemployment. Unsurprisingly, the Fed has continued on its series of robust responses to combat its perception of rising inflationary pressures by repeatedly increasing the Fed rate to reach 2.25 – 2.50% in December 2018. It has also continued its policy of not fully reinvesting proceeds from bonds that it holds as a result of quantitative easing, when they mature. We therefore saw US 10 year bond Treasury yields rise above 3.2% during October 2018 and also investors causing a sharp fall in equity prices as they sold out of holding riskier assets. However, by early January 2019, US 10 year bond yields had fallen back considerably on fears that the Fed was being too aggressive in raising interest rates and was going to cause a recession. Equity prices have been very volatile on alternating good and bad news during this period.

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, emerging market developments and sharp changes in investor sentiment. Such volatility could occur at any time during the forecast period.

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.

Investment and borrowing rates

- Investment returns are likely to remain low during 2019/20 but to be on a gently rising trend over the next few years.
- Borrowing interest rates have been volatile so far in 2018/19 and while they were on a rising trend during the first half of the year, they have back tracked since then until early January. 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, (the difference between higher borrowing costs and lower investment returns), to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.

APPENDIX E

Provided by Link Asset Services Asset Services at 9 January 2019

ECONOMIC BACKGROUND

GLOBAL OUTLOOK. World growth has been doing reasonably well, aided by strong growth in the US. However, US growth is likely to fall back in 2019 and, together with weakening economic activity in China and the eurozone, overall world growth is likely to weaken.

Inflation has been weak during 2018 but, at long last, unemployment falling to remarkably low levels in the US and UK has led to an acceleration of wage inflation. The US Fed has therefore increased rates nine times and the Bank of England twice. However, the ECB is unlikely to start raising rates until late in 2019 at the earliest.

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 period of stimulating economic recovery and warding off the threat of deflation, is coming towards its close. A new period is well advanced in the US, and started more recently in the UK, of 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 a 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 also encouraged investors into a search for yield and into investing in riskier assets such as equities. Consequently, prices in both bond and equity markets rose to historically high valuation levels simultaneously. This meant that both asset categories were exposed to the risk of a sharp downward correction and we have, indeed, seen a sharp fall in equity values in the last quarter of 2018. 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, or, conversely, 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.** At the time of writing, (early January 2019), financial markets are very concerned that the Fed is being too aggressive with its policy for raising interest rates and is likely to cause a recession in the US economy.

The world economy also needs to adjust to a sharp change in **liquidity creation** over the last five years where the US has moved from boosting liquidity by QE purchases, to reducing its holdings of debt (currently about $50bn per month). In addition, the European Central Bank ended its QE purchases in December 2018.

UK. The flow of positive economic statistics since the end of the first quarter of 2018 has shown that pessimism was overdone about the poor growth in quarter 1 when adverse weather caused a temporary downward blip. Quarter 1 at 0.1% growth in GDP was followed by a return to 0.4% in quarter 2 and by a strong performance in quarter 3 of +0.6%. However, growth in quarter 4 is expected to weaken significantly.

At their November quarterly Inflation Report meeting, the MPC repeated their well-worn phrase that future Bank Rate increases would be gradual and would rise to a much lower equilibrium rate, (where monetary policy is neither expansionary of contractionary), than before the crash; indeed they gave a figure for this of around 2.5% in ten years' time, but declined to give a medium term forecast. However, with so much uncertainty around Brexit, they warned that the next move could be up or down, even if there was a disorderly Brexit. While it would be expected that Bank Rate could be cut if there was a significant fall in GDP growth as a result of a disorderly Brexit, so as to provide a stimulus to growth, they warned they could also *raise* Bank Rate in the same scenario if there was a boost to inflation from a devaluation of sterling, increases in import prices and more expensive goods produced in the UK replacing cheaper goods previously imported, and so on. In addition, the Chancellor could potentially provide fiscal stimulus to support economic growth, though at the cost of increasing the budget deficit above currently projected levels.

It is unlikely that the MPC would increase Bank Rate in February 2019, ahead of the deadline in March for Brexit. Getting parliamentary approval for a Brexit agreement on both sides of the Channel will take well into spring 2019. However, in view of the hawkish stance of the MPC at their November meeting, the next increase in Bank Rate is now forecast to be in May 2019, (on the assumption that a Brexit deal is agreed by both the UK and the EU). The following increases are then forecast to be in February and November 2020 before ending up at 2.0% in February 2022.

Inflation. The Consumer Price Index (CPI) measure of inflation has been falling from a peak of 3.1% in November 2017 to 2.1% in December 2018. In the November Bank of England quarterly Inflation Report, inflation was forecast to still be marginally above its 2% inflation target two years ahead, (at about 2.1%), given a scenario of minimal increases in Bank Rate.
As for the **labour market** figures in October**,** unemployment at 4.1% was marginally above a 43 year low of 4% on the Independent Labour Organisation measure. A combination of job vacancies hitting an all-time high, together with negligible growth in total employment numbers, indicates that employers are now having major difficulties filling job vacancies with suitable staff. It was therefore unsurprising that wage inflation picked up to 3.3%, (3 month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates less CPI inflation), earnings are currently growing by about 1.2%, the highest level since 2009. This increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. This tends to confirm that the MPC was right to start on a cautious increase in Bank Rate in August as it views wage inflation in excess of 3% as increasing inflationary pressures within the UK economy.

In the **political arena**, the Brexit deal put forward by the Conservative minority government was defeated on 15 January. It is unclear at the time of writing, how this situation will move forwardHowever, our central position is that Prime Minister May's government will endure, despite various setbacks, along the route to reaching an orderly Brexit though the risks are increasing that it may not be possible to get full agreement by the UK and EU before 29 March 2019, in which case this withdrawal date is likely to be pushed back to a new date. If, however, the UK faces a general election in the next 12 months, this could result in a potential loosening of monetary and fiscal policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up.

USA. President Trump's massive easing of fiscal policy is fuelling a (temporary) boost in consumption which has generated an upturn in the rate of strong growth which rose from 2.2% (annualised rate) in quarter 1 to 4.2% in quarter 2 and 3.5%, (3.0% y/y), in quarter 3, but also an upturn in inflationary pressures. The strong growth in employment numbers and the reduction in the unemployment rate to 3.9%, near to a recent 49 year low, has fed through to an upturn in wage inflation which hit 3.2% in November, However, CPI inflation overall fell to 2.2% in November and looks to be on a falling trend to drop below the Fed's target of 2% during 2019. The Fed has continued on its series of increases in interest rates with another 0.25% increase in December to between 2.25% and 2.50%, this being the fifth increase in 2018 and the ninth in this cycle. However, they did also reduce their forecast for further increases from three to two. This latest increase compounded investor fears that the Fed is over doing the speed and level of increases in rates and that it is going to cause a US recession as a result. There is also much evidence in previous monetary policy cycles of the Fed's series of increases doing exactly that. Consequently, we have seen stock markets around the world falling under the weight of fears around the Fed's actions, the trade war between the US and China and an expectation that world growth will slow.

The tariff war between the US and China has been generating a lot of heat during 2018, but it is not expected that the current level of actual action would have much in the way of a significant effect on US or world growth. However, there is a risk of escalation if an agreement is not reached soon between the US and China.

Eurozone. Growth was 0.4% in quarters 1 and 2 but fell back to 0.2% in quarter 3, though this was probably just a temporary dip. In particular, data from Germany has been mixed and it could be negatively impacted by US tariffs on a significant part of its manufacturing exports e.g. cars. For that reason, although growth is still expected to be in the region of nearly 2% for 2018, the horizon is less clear than it seemed just a short while ago. Having halved its quantitative easing purchases of debt in October 2018 to €15bn per month, the European Central Bank ended all further purchases in December 2018. The ECB is forecasting inflation to be a little below its 2% top limit through the next three years so it may find it difficult to warrant a start on raising rates by the end of 2019 if the growth rate of the EU economy is on a weakening trend.

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. Progress has been made in reducing the rate of credit creation, particularly from the shadow banking sector, which is feeding through into lower economic growth. There are concerns that official economic statistics are inflating the published rate of growth.

Japan - has been struggling to stimulate consistent significant GDP growth and 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. It is likely that loose monetary policy will endure for some years yet to try to stimulate growth and modest inflation.

Emerging countries. Argentina and Turkey are currently experiencing major headwinds
and are facing challenges in external financing requirements well in excess of their reserves of foreign exchange. However, these countries are small in terms of the overall world economy, (around 1% each), so the fallout from the expected recessions in these countries will be minimal.

INTEREST RATE FORECASTS

The interest rate forecasts provided by Link Asset Services in paragraph 3.2 are **predicated on an assumption of an agreement being reached on Brexit between the UK and the EU.** On this basis, while GDP growth is likely to be subdued in 2019 due to all the uncertainties around Brexit depressing consumer and business confidence, an agreement is likely to lead to a boost to the rate of growth in 2020 which could, in turn, increase inflationary pressures in the economy and so cause the Bank of England to resume a series of gentle increases in Bank Rate. Just how fast, and how far, those increases will occur and rise to, will be data dependent. The forecasts in this report assume a modest recovery in the rate and timing of stronger growth and in the corresponding response by the Bank in raising rates.

- In the event of an **orderly non-agreement exit**, it is likely that the Bank of England would take action to cut Bank Rate from 0.75% in order to help economic growth deal with the adverse effects of this situation. This is also likely to cause short to medium term gilt yields to fall.
- If there was a **disorderly Brexit**, then any cut in Bank Rate would be likely to last for a longer period and also depress short and medium gilt yields correspondingly. It is also possible that the government could act to protect economic growth by implementing fiscal stimulus.

However, there would appear to be a majority consensus in the Commons against any form of non-agreement exit so the chance of this occurring has now substantially diminished.

The balance of risks to the UK

- The overall balance of risks to economic growth in the UK is probably neutral.
- The balance of risks to increases in Bank Rate and shorter term PWLB rates, are probably also even and are broadly dependent on how strong GDP growth turns out, how slowly inflation pressures subside, and how quickly the Brexit negotiations move forward positively.

One risk that is both an upside and downside risk, is that all central banks are now working in very different economic conditions than before the 2008 financial crash as there has been a major increase in consumer and other debt due to the exceptionally low levels of borrowing rates that have prevailed for ten years since 2008. This means that the neutral rate of interest in an economy, (i.e. the rate that is neither expansionary nor deflationary), is difficult to determine definitively in this new environment, although central banks have made statements that they expect it to be much lower than before 2008. Central banks could therefore either over or under do increases in central interest rates.

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

- **Brexit –** if it were to cause significant economic disruption and a major downturn in the rate of growth.
- **Bank of England monetary policy** takes action too quickly, or too far, 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.
- 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, and due to the election in March of a government which has made a lot of anti-austerity noise. The EU rejected the initial proposed Italian budget and demanded cuts in government spending which the Italian government initially refused. However, a fudge was subsequently agreed, but only by *delaying* the planned increases in expenditure to a later year. This can has therefore only been kicked down the road to a later time. The rating agencies have started on downgrading Italian debt to one notch above junk level. If Italian debt were to fall below investment grade, many investors would be unable to hold it. Unsurprisingly, investors are becoming increasingly

concerned by the words and actions of the Italian government and consequently, Italian bond yields have risen – at a time when the government faces having to refinance large amounts of debt maturing in 2019.

- Weak capitalisation of some **European banks**. Italian banks are particularly vulnerable; one factor is that they hold a high level of Italian government debt - debt which is falling in value. This is therefore undermining their capital ratios and raises the question of whether they will need to raise fresh capital to plug the gap.
- **German minority government.** In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. Then in October 2018, the results of the Bavarian and Hesse state elections radically undermined the SPD party and showed a sharp fall in support for the CDU. As a result, the SPD is reviewing whether it can continue to support a coalition that is so damaging to its electoral popularity. After the result of the Hesse state election, Angela Merkel announced that she would not stand for re-election as CDU party leader at her party's convention in December 2018, (a new party leader has now been elected). However, this makes little practical difference as she is still expected to aim to continue for now as the Chancellor. However, there are five more state elections coming up in 2019 and EU parliamentary elections in May/June; these could result in a further loss of electoral support for both the CDU and SPD which could also undermine her leadership.
- **Other minority eurozone governments.** Spain, Portugal, Ireland, the Netherlands and Belgium all have vulnerable minority governments dependent on coalitions which could prove fragile. Sweden is also struggling to form a government due to the anti-immigration party holding the balance of power, and which no other party is willing to form a coalition with. The Belgian coalition collapsed in December 2018 but a minority caretaker government has been appointed until the May EU wide general elections.
- **Austria, the Czech Republic and Hungary** now form a strongly anti-immigration bloc within the EU while **Italy,** in 2018, also elected a strongly anti-immigration government. Elections to the EU parliament are due in May/June 2019.
- Further increases in interest rates in the US could spark a **sudden flight of investment funds** from more risky assets e.g. shares, into bonds yielding a much improved yield. Throughout the last quarter of 2018, we saw sharp falls in equity markets interspersed with occasional partial rallies. Emerging countries which have borrowed heavily in dollar denominated debt, could be particularly exposed to this risk of an investor flight to safe havens e.g. UK gilts.
- There are concerns around the level of **US corporate debt** which has swollen massively during the period of low borrowing rates in order to finance mergers and acquisitions. This has resulted in the debt of many large corporations being downgraded to a BBB credit rating, close to junk status. Indeed, 48% of total investment grade corporate debt is now rated at BBB. If such corporations fail to generate profits and cash flow to reduce their debt levels as expected, this could tip their debt into junk ratings which will increase their cost of financing and further negatively impact profits and cash flow.
- **Geopolitical risks,** especially North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.

Upside risks to current forecasts for UK gilt yields and PWLB rates

- **Brexit** – if both sides were to agree by 29 March a compromise that quickly removed all threats of economic and political disruption and so led to an early boost to UK economic growth.
- **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 QE, 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.
- 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,** whether domestically generated or imported, returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

Brexit timetable and process

- March 2017: UK government notified the European Council of its intention to leave under the Treaty on European Union Article 50 on 29 March 2019.
- 25.11.18 EU27 leaders endorsed the withdrawal agreement
- Dec 2018 vote in the UK Parliament on the agreement was postponed
- 21.12.18 – 8.1.19 UK parliamentary recess
- 15.1.19 Brexit deal defeated in the Commons vote by a large margin
- By 29.3.19 second vote (?) in UK parliament
- By 29.3.19 if the UK Parliament approves a deal, then ratification by the EU Parliament requires a simple majority
- By 29.3.19 if the UK and EU parliaments agree the deal, the EU Council needs to approve the deal; 20 countries representing 65% of the EU population must agree
- 29.3.19 Either the UK leaves the EU, or asks the EU for agreement to an extension of the Article 50 period if the UK Parliament has been unable to agree on a Brexit deal.
- 29.3.19: if an agreement is reached with the EU on the terms of Brexit, then this will be followed by a proposed **transitional period ending around December 2020.**
- 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 may leave the single market and tariff free trade at different times during the 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.

APPENDIX F

Counterparties

Specified Investments
These are sterling investments of a maturity period of not more than 365 days, or those which could be for a longer period but where the lender has the right to be repaid within 365 days if it wishes. These are low risk assets where the possibility of loss of principal or investment income is negligible. The instruments and credit criteria to be used are set out in the table below.

Table 8 Specified Investments

Instrument	Minimum Credit Criteria	Use
Debt Management Agency Deposit Facility	Government backed	In-house
Term deposits – other LAs	Local Authority issue	In-house
Term deposits – banks and building societies	AA- Long Term F1 Short-term UK or AA- Sovereign	In-house
Money Market Funds (CNAV), (LVNAV) and (VNAV)	AAA	In-house

Non-Specified Investments
Non-specified investments are any other type of investment (i.e. not defined as Specified above).They normally offer the prospect of higher returns but carry a higher risk. The identification and rationale supporting the selection of these other investments are set out in the table below.

Table 9 Non - Specified Investments

	Minimum Credit Criteria	Use	Max total investment	Max. maturity period
Banks and building societies (excluding Lloyds / HBOS)	A- Long Term F1 Short-term UK or AA- Sovereign	In-house	50%	3 months
Lloyds / HBOS	A- Long Term F1 Short-term	In-house	50%	12 months
Callable Deposits	A- Long Term F1 Short term UK or AA- Sovereign	In-house	50%	3 months
Council's Bank/(RBS)	F2 Short-term	In-house	60%	36 months
Enhanced Cash Funds	AAA	In-house	25% (maximum £10 million per fund)	Minimum monthly redemption
Corporate bonds pooled funds, other non-standard investments and gilts		In house	£10m in total	Dependent on specific agreement
HB Public Law Ltd		In house	£0.1m	Dependent on specific agreement
Investment Property Strategy		In house	£17.0m	Dependent on specific agreement
Concilium Group		In house	£0.702m	60 months

	Minimum Credit Criteria	Use	Max total investment	Max. maturity period
Startup capital				
Concilium Group 5% Long Term Investment		In house	£1.5m	Dependent on specific agreement
Concilium Assets LLP		In house	£0.175m	Dependent on specific agreement
Housing Development Vehicle (LLP) – Initially on acquisition of 100 homes		In house	£30m	Dependent on specific agreement

APPENDIX G

Affordability Prudential Indicators

1 Ratio of Financing Costs to Revenue Stream

This indicator identifies the trend in the cost of capital (borrowing, depreciation, impairment and other long term obligation costs net of investment income) against the net revenue stream. Tables 10 and 11 below show the current position for the General Fund and HRA respectively.

Table 10 Ratio of Financing Costs to Revenue Stream – General Fund

	2017/18	2018/19	2019/20	2020/21
	Actual	Estimate	Estimate	Estimate
Net revenue stream (£'000)	164,987	168,917	168,780	167,760
Interest costs (£'000)	7,316	7,433	10,817	11,297
Interest costs - finance leases (£'000)	1,717	1,700	1,700	1,700
Interest and investment income (£'000)	-1,296	-1,300	-1,300	-1,300
MRP (£'000)	16,584	16,556	23,524	24,660
Total financing costs (£'000)	24,321	24,389	34,741	36,357
Ratio of total financing costs against net revenue stream (%)	14.7	14.4	20.6	21.7

The ratio of total financing costs against net revenue stream increases significantly between 2018/19 and 2021/22 due to the impact of the increased borrowing requirement to finance the Capital Programme and the required increase in MRP.

Table 11 Ratio of Financing Costs to Revenue Stream – HRA

	2017/18	2018/19	2019/20	2020/21
	Actual	Estimate, Qtr 3	Estimate	Estimate
Gross revenue stream (£'000)	32,245	31,703	31,928	32,860
Interest costs of self-funding borrowing (£'000)	6,242	6,237	6,065	6,043
Interest costs of other borrowing (£'000)	0	0	197	700
Interest and investment income (£'000)	7	1	3	3
Depreciation (£'000)	7,679	8,026	7,775	7,903
Impairment (£'000)	330	0	0	0
Total financing costs (£'000)	14,258	14,264	14,041	14,649
Ratio of total financing costs against net revenue stream (%)	44.2	45.0	44.0	44.6

The ratio of total financing costs (excluding depreciation and impairment) against net revenue stream shows a gradual increase due largely to the mandatory reduction in dwelling rent and the reduction of interest income due to reducing balances on the revenue account and Major Repairs reserve.

2 Incremental Impact of Capital Investment Decisions on Council Tax and Housing Rents

This indicator identifies the revenue costs associated with proposed Capital Programme and the impact on Council Tax and Housing Rents.

Table 12 Incremental Impact of Capital Investment Decisions – Council Tax

Incremental Impact of Capital Investment Decisions

	2017/18	2018/19	2019/20	2021/22
	Actual	Estimate	Estimate	Estimate
Net Financing need (£'000)	43,221	57,087	42,686	28,687
Borrowing @ 25-50years PWLB rate (£'000)	1,098	1,536	1,297	914
MRP @ 2% (£'000)	864	1,142	854	574
Total increased costs (£'000)	**1,962**	**2,677**	**2,150**	**1,488**
Ctax base (£'000)	82,000	83,500	84,466	85,946
% Increase	2.4	3.2	2.5	1.7
Band D Council Tax	1,348	1,395	1,464	1,493
Overall increase £ pa	**32.25**	**44.72**	**37.28**	**25.86**

Table 13 Incremental Impact of Capital Investment Decisions – Housing Rents

Incremental Impact of Capital Investment Decisions – Housing Rents

	2017/18	2018/19	2019/20	2020/21	2021/22
	Actual	Estimate, Qtr 3	Estimate	Estimate	Estimate
Net Financing need (£'000)	1,477	-	13,149	16,778	23,564
Borrowing @ 2% (25-50years PWLB rate) (£'000)	1,477	-	13,149	16,778	23,564
Depreciation @ 2% (£'000)	-	-	-	-	-
Total increased costs	1,477	-	13,149	16,778	23,564
Number of dwellings **(average)**	4,825	4,812	4,812	4,808	4,839
Increase in average housing rent per week £	£5.89	£0.00	£52.55	£67.11	£93.64

Increase required in rental income appears high due to increased borrowing required for new build. Expenditure financed from a range of sources including revenue, capital receipts, contributions and grant as well as borrowing.

3 Local HRA indicators

The Council should also be aware of the following ratios when making its treasury management decisions.

Table 14 HRA Ratios

	2017/18	2018/19	2019/20	2020/21
	Actual	**Estimate, Qtr 3**	**Estimate**	**Estimate**
Debt (CFR) @ 31 March (£m)	151.01	150.05	162.62	178.86
Gross Revenue Stream (£m)	32.24	31.70	31.93	32.86
Ratio of Gross Revenue Stream to Debt (%)	**21**	**21**	**20**	**18**
Average Number of Dwellings	4,825	4,812	4,812	4,808
Debt outstanding per dwelling (£)	**31,298**	**31,182**	**33,795**	**37,200**

Rents in the Housing Revenue Account are projected to reduce by 1% each year for four years commencing in 2016/17, in line with the provisions of the Welfare Reform and Work Act. The reduction in income is expected to be mitigated over the next two years by additional rent income generated as a result of an increase in HRA property numbers from the Council's HRA new build and purchase and repair programmes.