# Lewes District Council

# Treasury Management Strategy Statement and Investment Strategy 2015/16 to 2017/18

## Contents

## 1. Executive Summary

1.1 Borrowing – the Council can borrow to finance capital expenditure in a similar way to an individual taking out a mortgage to buy a house. At 31 March 2015, total cumulative capital expenditure which will need to be funded amounts to £70.7 m. The actual long term-borrowing (the mortgage) that we have is only £56.7m because we are using the cash held in our reserves to make up the difference, rather than invest that money. (See Sections 6 and 7 for the details).

1.2 Debt rescheduling – The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall saving or reduction in risk. (See Section 8 for the details).

1.3 Accounting for debt – the Council will adopt a two-Pool approach in order to manage and account for the debt of the General Fund/Housing Revenue Account. (See Section 9 for the details).

1.4 Investing – at any given time, the Council has varying amounts of cash consisting of reserves and balances, as well as working capital, which must be held securely. The security of our investments is our highest priority. We have defined the types of investment that we will make and the criteria that those organisations with which we will deal must meet. (See Sections 10 and 11 for the details).

1.5 Providing for the repayment of debt – we will continue to make formal annual provisions to repay our long term borrowing, and will also build up a fund in the Housing Revenue Account Balance so that debt can be repaid if we choose to do so. (See Section 13 for the details).

1.6 Reporting – we will closely monitor our Treasury Management activity and make reports to every meeting of the Council's Audit and Standards Committee and Cabinet. (See Section 14 for the details).

## 2. Treasury Management Defined

2.1 The Council defines its Treasury Management activities as:

*"the management of the Council's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."*

2.2 Treasury Management is not undertaken in isolation. The Council acknowledges that effective Treasury Management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in Treasury Management and ensuring that performance is monitored and reported. All Treasury Management activity takes place within the context of effective risk management.

## 3. Scope of the Treasury Management Strategy Statement

3.1 This Strategy Statement sets out the Council's approach to financing (borrowing) and investment for the financial year but also sets the context for the following two years.

3.2 The Council has adopted the Chartered Institute of Public Finance and Accountancy's (CIPFA's) Code of Practice for Treasury Management in Public Services (the "TM Code"). This requires local authorities to determine the Treasury Management Strategy Statement (TMSS) before the start of the financial year.

3.3 This Strategy Statement also incorporates the formal Investment Strategy which is necessary to comply with guidance issued by the Department for Communities and Local Government. (DCLG) in March 2010.

3.4 The Strategy sets out the context to Treasury Management in terms of the Council's financial resources as measured in its Balance Sheet and external factors, in particular the outlook for interest rates. It considers how the Revenue Budget and Capital Programme will impact on the Balance Sheet position.

## 4. Approach to Risk

4.1 The Council has borrowed and expects to invest substantial sums of money and is therefore exposed to financial risks including the revenue effect of changing interest rates and, in the extreme, the loss of invested funds.

4.2 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 Council. No Treasury Management activity is without risk. The main risks to the Council's Treasury activities are:

- Credit and Counterparty Risk (security of investments)
- Liquidity Risk (adequacy of cash resources)
- Market or Interest Rate Risk (exposure to fluctuations in interest rate levels)
- Inflation Risk (exposure to inflation)
- Refinancing Risk (impact of debt maturing in future years)
- Legal & Regulatory Risk (compliance with statutory powers and regulatory requirements)
- Fraud, Error and Corruption and Contingency Management (maintenance of sound systems and procedures)

## 5. External Context

5.1 Economic Background

There is momentum in the UK economy, with a continued period of growth through domestically-driven activity and strong household consumption. There are signs that growth is becoming more balanced. The greater contribution from business investment should support continued, albeit slower, expansion of GDP. However, inflationary pressure is benign and is likely to remain low in the short-term. There have been large falls in unemployment but levels of part-time working, self-employment and underemployment are significant and nominal earnings growth remains weak and below inflation.

5.2 Credit Outlook

The transposition of two European Union (EU) directives into UK legislation will place the burden of rescuing failing EU banks disproportionately onto unsecured local authority investors. The Bank Recovery and Resolution Directive promotes the interests of individual and small businesses covered by the Financial Services Compensation Scheme and similar European schemes, while the recast Deposit Guarantee Schemes Directive includes large companies into these schemes. The combined effect of these two changes is to leave public authorities and financial organisations as the only senior creditors likely to incur losses in a failing bank after July 2015.

The continued global economic recovery has led to a general improvement in credit conditions since last year. However, due to the above legislative changes, the credit risk associated with making unsecured bank deposits will increase relative to the risk of other investment options available to the Council.

5.3 Outlook for Interest Rates

The detailed economic interest rate outlook provided by the Council's Treasury advisor, Arlingclose Ltd, is attached at Appendix A. In summary, Arlingclose forecasts the first rise in official interest rates in August 2015 and a gradual pace of increases thereafter, with the average for 2015/2016 being around 0.75%. However, if the negative indicators from the Eurozone become more entrenched, the Bank of England will likely defer rate rises to later in the year.

Arlingclose believes the normalised level of the Bank Rate post-crisis to range between 2.5% and 3.5%, and that the average 10 year PWLB loan rate for 2015/16 will rise to 3.40%.

5.4 Interest rates are of fundamental importance to the Council's Treasury Management operation. The ideal scenario would be to make short-duration investments if interest rates are low and are expected to rise and to invest for longer periods if interest rates are considered to be at their peak and are expected to fall. In terms of borrowing, it is preferable to borrow short-term when interest rates are high and expected to fall and to undertake long-term borrowing when interest rates are low and expected to rise.

5.5 The estimate for external interest payments in 2014/2015 is £1.73m, unchanged from 2014/2015, and for external interest receipts is £0.075m (2014/15 £0.050m).

5.6 The Council's need to borrow and its ability to invest are interrelated, as explained elsewhere in this Strategy Statement. The Council will reappraise its strategy in both of these areas from time to time and, if needs be, realign it with evolving market conditions and expectations for future interest rates. Any such changes will require the prior approval of Cabinet.

## 6. The Need to Borrow Long Term

6.1 Other than for temporary cash flow purposes, local authorities are only allowed to borrow to finance capital expenditure (eg the purchase of property, vehicles or equipment which will last for more than one year, or the improvement of such assets). The Government limits the amount borrowed by local authorities for housing purposes only by specifying ‘debt caps’. This Council’s underlying debt cap has been fixed at £72.931m. In 2014/2015 local authorities were able to bid for an increase in its housing debt cap in order to enable specific projects. A bid from this Council was successful and, should new build schemes for 30 properties across 7 sites proceed, this Council’s debt cap will increase to £75.248m.

6.2 In accounting terms, the underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. In recent years, the Council’s strategy has been to maintain borrowing and investments below their underlying levels, known as internal borrowing, and this remains the Strategy for 2015/16.

6.3 The CFR is, in simple terms, the amount of capital expenditure which has been incurred by the Council but which has not yet been paid for (by using, for example, grants, capital receipts, reserves or revenue income) and in the meantime is covered by internal or external borrowing. External borrowing is where loans are raised from the Public Works Loans Board (PWLB) or banks. Alternatively it is possible to use the significant levels of cash which has been set aside in Balances and Reserves and which would otherwise need to be invested with banks or other borrowers as a means to avoid taking on external loans.

6.4 The CFR is calculated each year in accordance with a statutory formula. As noted above, the level of CFR increases each year by the amount of capital expenditure which is yet to be financed and is reduced by the amount that the Council sets aside for the repayment of borrowing. This is illustrated in the table below. Amounts from 2015/2016 onwards are indicative. Projected capital expenditure in 2015/2016 with a financing requirement includes projects for the construction of 30 new affordable homes (£3.8m), installing PV panels on council-owned homes (£2.7m) and implementing new technology (£1.3m).

| | 2013/14 £m | 2014/15 £m | 2015/16 £m | 2016/17 £m | 2017/18 £m |
|---|---|---|---|---|---|
| Opening CFR | 71.031 | 71.448 | 70.709 | 74.034 | 72.242 |
| Capital exp in year | 10.504 | 16.594 | 15.666 | 8.140 | 6.891 |
| Less financed | -8.727 | -15.472 | -10.464 | -7.955 | -6.706 |
| Less amount set aside for debt repayment | -1.360 | -1.861 | -1.877 | -1.977 | -1.966 |
| Closing CFR | 71.448 | 70.709 | 74.034 | 72.242 | 70.461 |

6.5 The overall CFR can be split between the General Fund and Housing Revenue Account as follows:

| | 2013/14 £m | 2014/15 £m | 2015/16 £m | 2016/17 £m | 2017/18 £m |
|---|---|---|---|---|---|
| General Fund CFR | 4.652 | 5.919 | 8.421 | 8.123 | 7.837 |
| HRA CFR | 66.796 | 64.790 | 65.613 | 64.119 | 62.624 |
| Total CFR | 71.448 | 70.709 | 74.034 | 72.242 | 70.461 |

6.6 The following table compares the CFR with the amount that the Council holds in balances and reserves as well as working capital (day to day cash movements as well as grants, developer contributions and capital receipts held pending use):

| | 31/3/14 £m | 31/3/15 £m | 31/3/16 £m | 31/3/17 £m | 31/3/18 £m |
|---|---|---|---|---|---|
| (a) Capital Financing Requirement | 71.448 | 70.709 | 74.034 | 72.242 | 70.461 |
| (b) Actual external borrowing | -56.673 | -56.673 | -56.673 | -56.673 | -56.673 |
| (c) Use of Balances, Reserves and working capital as alternative to borrowing (a)–(b) | 14.775 | 14.036 | 17.361 | 15.569 | 13.788 |
| | | | | | |
| (d) Total Balances and Reserves | 16.507 | 12.758 | 10.552 | 10.417 | 10.417 |
| (e) Working capital | 3.269 | 5.730 | 10.307 | 10.284 | 11.549 |
| (f) Amount used as an alternative to borrowing (c) above | -14.775 | -14.036 | -17.361 | -15.569 | -13.788 |
| (g) Total investments (d)+(e)+(f) | 5.001 | 4.452 | 3.498 | 5.132 | 8.178 |

6.7 The table above (line b) assumes that the current external loan portfolio is unchanged across the period. There is an opportunity to repay a £5m variable rate loan to the PWLB in March 2015, utilising cash balances that would otherwise be invested. A final decision will be taken closer to the time, to take into account updated projections of working capital and reserves and balances.

6.8 Line g in the table above indicates that it will be possible to continue the current approach of internal borrowing as an alternative to raising new external loans, which remain at their current level across the period (line b). However, it will be necessary to monitor the position closely. Market conditions, interest rate expectations and counterparty and credit risk considerations will influence the Council's strategy in determining the borrowing and investment activity against the underlying Balance Sheet position. The following section explains the approach to borrowing in more depth.

## 7. Borrowing Strategy

7.1 As noted above, the Council's underlying need to borrow for capital purposes is measured by reference to its CFR. In respect of General Fund activities, local authorities are required to make a Minimum Revenue Provision for Debt Redemption (MRP) from within the Revenue budget each year in order to ensure that the underlying need to borrow is ultimately eliminated. There is no requirement to make a provision to reduce HRA borrowing, although it is prudent to do so.

7.2 Capital expenditure not paid for from internal resources (i.e. Capital Receipts, Capital Grants and Contributions, Revenue or Reserves) will produce an increase in the CFR (the underlying need to borrow) and in turn produce an increased requirement to charge MRP in the Revenue Account.

7.3 In accordance with the Prudential Code, the Council will ensure that net external borrowing does not, except in the short term, exceed its highest CFR over the next three years.

The cumulative estimate of the Council's long-term borrowing requirement in respect of historic and planned capital expenditure is shown in the table below. Increases in 2015/2016 resulting from the projects listed in paragraph 6.4 above are offset over the period though to 2017/2018 by provision being made by the HRA for the repayment of debt. The table excludes £5.7m of potential borrowing for housing projects (at 31 March 2015), permissible up to the level of the Council's underlying Housing Debt Cap.

| | 31/03/2015 Estimate £m | 31/03/2016 Estimate £m | 31/03/2017 Estimate £m | 31/03/2018 Estimate £m |
|---|---|---|---|---|
| **Capital Financing Requirement** | 70.7 | 74.0 | 72.2 | 70.5 |
| **Less:**<br>Profile of current Borrowing | -56.7 | -56.7 | -56.7 | -56.7 |
| **Cumulative Maximum External Borrowing Requirement** | 14.0 | 17.3 | 15.5 | 13.8 |

7.4 The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

7.5 Given the projected reduction in revenue funding from the Government through to 2019/2020 and the Council's General Fund savings target of £2.7m over that period, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio, With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead. By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. For example, the current rates (January 2015) available to the Council (which include a 0.2% reduction under the local authority 'certainty rate' system introduced in November 2012) for 2-year and 5-year PWLB maturity loans are 1.39% and 1.78% respectively compared with 0.25% which can be earned on a temporary deposit with the Government.

7.6 The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. At some stage the level of General Fund Reserves and Balances will become depleted (as they are used for the purpose for which the funds were set aside) restricting the ability to borrow internally. The Council's appointed Treasury advisor, Arlingclose, will assist the Council with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2015/2016 with a view to keeping future interest costs low, even if this causes additional cost in the short-term. Any decision to borrow will be confirmed with the Cabinet Member for Corporate Services and reported to the next meeting of the Cabinet.

7.7 The Council may borrow short-term loans (normally up to one month) to cover unexpected cash flow shortages should they arise.

7.8 The approved sources of new long-term and short-term borrowing will be:

- Public Works Loans Board
- UK Local Authorities
- any bank or building society approved for investments (see Section 11) below.
- LGA Bond Agency

In the event that alternative sources of borrowing are identified in the year, which are considered to be more appropriate in the context of the overall strategy, a report will be made to Cabinet and Council. Arlingclose will assist the Council with the analysis of options.

7.9 The PWLB remains an attractive source of borrowing, given the transparency and control that its facilities continue to provide. However, the Council will investigate other sources of finance, such as local authority loans and bank loans that may be available at more favourable rates.

7.10 The Local Government Association Bond Agency established the Local Capital Finance Company in 2014. The Company plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for a number of reasons including the fact that there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from this source will therefore be the subject of a separate report to full Council.

## 8. Debt Rescheduling

8.1 At the time of preparing this Strategy, the Council's loan portfolio was as shown in the table overleaf. All of the PWLB loans listed above were taken out in March 2012 in order to finance the payment to the Government needed for the national transition to self-financing for local authority housing. The Lender's Options Borrower's Option (LOBO) loan shown in the table above was taken out in April 2004 at the rate of 4.5% with a term of 50 years. Every 4 years, the Lender has the option to increase the interest rate, and if it does so, the Council has the right to repay. The next date when the rate/terms of the loan will be reviewed is April 2016.

| Lender | Interest | Amount £m | Rate % | Maturity |
|---|---|---|---|---|
| PWLB | Fixed | 4.00 | 2.7000 | 01/03/2024 |
| PWLB | Fixed | 5.00 | 3.3000 | 01/03/2032 |
| PWLB | Fixed | 2.00 | 3.0500 | 01/09/2027 |
| PWLB | Fixed | 2.00 | 2.7600 | 01/09/2024 |
| PWLB | Fixed | 4.00 | 2.9700 | 01/09/2026 |
| PWLB | Fixed | 5.00 | 3.2800 | 01/09/2031 |
| PWLB | Fixed | 4.00 | 2.6300 | 01/09/2023 |
| PWLB | Fixed | 5.00 | 3.4400 | 01/03/2037 |
| PWLB | Fixed | 6.67 | 3.5000 | 01/03/2042 |
| PWLB | Fixed | 5.00 | 3.4300 | 01/09/2036 |
| PWLB | Variable | 5.00 | 0.6200 | 28/03/2022 |
| PWLB | Fixed | 4.00 | 3.0100 | 01/03/2027 |
| | Sub-total | 51.67 | | |
| Barclays | LOBO | 5.00 | 4.5000 | 06/04/2054 |
| | Total | 56.67 | | |

8.2 The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to set a formula based on current interest rates. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall saving or reduction in risk. Any debt rescheduling activity will be confirmed with the Cabinet Member for Corporate Services and reported to the next Cabinet meeting. Reducing the level of cash held and, as a result, Credit and Counterparty risk.

## 9. The Housing Revenue Account Share of Treasury Management Costs.

9.1 Local authorities are required to recharge interest expenditure and income attributable to the HRA in accordance with Determinations issued by the Department for Communities and Local Government.

9.2 The Determinations do not set out a methodology for calculating the interest rate to use in each instance. The Council is therefore required to adopt a policy that will set out how interest charges attributable to the HRA will be determined. The CIPFA Code recommends that authorities present this policy in their Strategy Statement.

9.3 The Council has adopted a ‘2 pool’ (General Fund and HRA) approach to accounting for long-term loans, all of which were allocated to the HRA on the introduction of ‘self-financing’ Any new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/credited to the respective revenue account.

9.4 At the start of each year, an assessment will be made of the difference between the value of the HRA loans pool and the HRA’s underlying need to borrow. If the resulting cash balance is negative, an ‘internal loan’ will be advanced from the General Fund (Reserves and Balance) to the HRA and interest charged at a rate equivalent to a one-year maturity loan from the PWLB at the start of the financial year. This is a reasonable approach and reflects the fact that strategic borrowing decisions will generally be made on an annual basis, as demonstrated in this Strategy. The same approach will be adopted for any new internal borrowing required in the year to support the cost of HRA capital expenditure not anticipated in the initial annual capital programme.

## 10. The Need to Invest

10.1 As shown in the table in paragraph 6.6 the Council currently holds healthy Reserves and Balances (£12.8m projected at 31 March 2015 excluding s106 Developer Contributions and Capital Receipts which will be used to fund the Capital Programme over the next three years). In simple terms, Reserves represent amounts of money which have been set aside for use in future years for specific purposes (eg to pay for the replacement of vehicles at the end of their useful life) and Balances are cash which is retained both to ensure that the Council is able to respond effectively if an unforeseen event arises (eg the failure of a major contractor) and also to act as a buffer against unpredicted cash flow movements. Reserves and Balances are forecast to reduce over the next three years as they are called upon to support projects, services and the Council's deficit reduction programme.

10.2 Although a proportion of the Reserves and Balances are being used as an alternative to external long-term borrowing, this still leaves cash to be retained. In addition, the Council's cash flow movements fluctuate on a day to day basis, with cash received exceeding cash paid out at key points over the year. For example, at the start of 2014/2015 £11m was available for investment but the maximum amount invested at any point in the year was £28m. The purpose of the Investment Strategy is to define the conditions under which this 'surplus' cash is to be managed, with the priority being security of the sums invested.

10.3 Guidance from DCLG on Local Government Investments in England requires authorities to set an Annual Investment Strategy. The speculative procedure of borrowing purely in order to invest is unlawful. However, taking on new external loans to reduce the level of internal borrowing is permissible, and, if this takes place, the Council will place importance on the flexibility of its loan portfolio as well as the liquidity of its investments.

## 11. Investment Strategy

11.1 The Council's general policy objective is to invest its surplus funds prudently, striking a balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. The Council's investment priorities are:

| | |
|---|---|
| ***highest priority -*** | security of the invested capital; |
| ***followed by -*** | liquidity of the invested capital (this enables the Council to react to changing circumstances) |
| ***finally -*** | an optimum yield which is commensurate with security and liquidity. |

11.2 Given the increasing risk and continued low returns from short-term unsecured bank investments, the Council aims to diversify into more secure and/or higher yielding asset classes during 2015/2016 when it is appropriate to do so. This is especially the case for funds that are identified as being available for longer-term investment. This diversification will therefore represent a substantial change in strategy over the coming year.

11.3 The Council may invest its surplus funds with any of the counterparty types identified in Appendix C, subject to the cash limits (per counterparty) and the time limits shown. It is important to note that not all of the types of investment listed above will necessarily be used. Before any type of investment instrument is used for the first time (eg corporate bonds), specific Cabinet approval will be sought.

11.4 Investment decisions will be made by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used.

11.5 The Council and its advisors remain vigilant at all times, monitoring signs of credit or market distress that might adversely affect the Council.

11.6 Credit ratings are obtained and monitored by Arlingclose who will notify changes in ratings as they occur. Where a counterparty has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made
- any existing investments that can be recalled or sold at no cost, will be recalled
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty

11.7 Where a rating agency announces that a rating is on review for possible downgrade below the approved investment criteria, then only investments that can be withdrawn on the next working day will be made with that counterparty until the outcome of the review is announced. This approach will not apply to 'negative outlooks' which indicate a long-term direction of travel rather than an imminent change of rating.

11.8 The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

11.9 At times of deteriorating financial market conditions affecting the credit worthiness of all organisations (as happened in 2008 and 2011), the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments.

11.10 Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the DCLG Guidance.

Specified investments are

- o denominated in £ sterling
- o due to be repaid within 12 months of arrangement
- o not defined as capital expenditure by legislation
- o invested with the UK Government or local authority or a body or investment scheme of high credit quality'

Non specified investments are, effectively, everything else. The Council does not intend to make any investments denominated in foreign currencies nor any that are defined as capital expenditure (eg company shares). Non-specified investments will therefore be limited to long-term investments ie those that are due to mature 12 months or longer from the date of arrangement and investments with bodies and schemes not meeting the definition of 'high credit quality'.

11.11 The Council defines 'high credit quality' organisations and securities as those having a long-term credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. **Limits** on non-specified investments are shown below.

| | Cash limit |
|---|---|
| Total long-term investments | £2m |
| Total investments rated below A- | £5m |
| Total investments with institutions domiciled in foreign countries rated below AA+ | £2m |
| Total non-specified investments | £9m |

11.12 The Council's revenue reserves available to cover investment losses are forecast to be £8m on 31st March 2015. The maximum that will be lent to any one organisation (other than the UK Government) will be £2m. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below:

| | Cash limit |
|---|---|
| Any single organisation, except the UK Central Government | £2m each |
| UK Central Government | unlimited |
| Any group of organisations under the same ownership | £2m per group |
| Any group of pooled funds under the same management | £3m per manager |
| Negotiable instruments held in a broker's nominee account | £5m per broker |
| Foreign countries | £2m per country |
| Registered Providers | £4m in total |
| Money Market Funds | £6m in total |

11.13 The Director of Corporate Services will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators. Decisions taken on the investment portfolio will be reported to meetings of the Audit and Standards Committee and Cabinet.

11.14 All of the Council's investments are currently managed in-house and this approach will continue for the duration of this Strategy unless otherwise approved in advance by Cabinet.

11.15 The Council uses a spreadsheet model, updated daily, to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a pessimistic basis, with receipts under-estimated and payments over-estimated to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium term financial plan and cash flow forecast.

11.16 Investment of Money Borrowed in Advance of Need: The Council may, from time to time, borrow in advance of need, where this is expected to provide the best long term value for money. Since amounts borrowed will be invested until spent, the Council is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Council's overall management of its treasury risks. The maximum period between borrowing and expenditure is expected to be two years, although the Council is not required to link particular loans with particular items of expenditure.

## 12. The Use of Financial Instruments for the Management of Risks

12.1 Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (eg interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (ie those that are not embedded into a loan or investment).

12.2 The CIPFA Code requires authorities to clearly detail their policy on the use of derivatives in the annual strategy. The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

12.3 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

## 13. Providing for Debt Repayment - 2015/16 Minimum Revenue Provision Statement

13.1 The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (SI 2008/414) place a duty on local authorities to make a prudent provision for debt redemption. Guidance on this MRP has been issued by the Secretary of State and local authorities are required to “have regard” to such Guidance under section 21(1A) of the Local Government Act 2003.

13.2 The four MRP options available are:

Option 1: Regulatory Method Option 2: CFR Method
Option 3: Asset Life Method Option 4: Depreciation Method

13.3 Options 1 and 2 may be used only for supported non-HRA capital expenditure (ie where the Government supports the cost of financing new borrowing through a recurring grant). Methods of making prudent provision for self financed non-HRA capital expenditure include Options 3 and 4 (which may also be used for supported expenditure if the Council chooses). There is no requirement to charge MRP in respect of HRA capital expenditure funded from borrowing.

13.4 The MRP Statement will be submitted to Council before the start of the financial year. If it is ever proposed to vary the terms of the original MRP Statement during the year, a revised statement will be put to Council at that time.

13.5 The Council’s Policy for making a MRP will remain unchanged in 2015/2016 ie in respect of capital expenditure which is supported expenditure, Option 1 will apply – MRP will be equal to the amount determined in accordance with the former regulations 28 and 29 of the Local Authorities Capital Finance and Accounting (England) Regulations 2003 as if they had not been revoked. In the event that capital expenditure is incurred which is not Supported Capital Expenditure and is therefore self-financed, Option 3 will apply – MRP will be calculated according to the asset life method and will be made in equal instalments over the life of the asset.

13.6 The Housing Revenue Account 30-year Business Plan includes the principle that the long-term borrowing required on the move to self-financing will be repaid at the earliest opportunity. However, there is no requirement to do so and become ‘debt-free’. In order to maintain flexibility, resources will be set aside in the HRA balance for potential debt repayment, but formal Revenue Provisions (which cannot be reversed) will not be made other than to reduce internal borrowing from the General Fund.

## 14. Reporting on the Treasury Outturn

The Director of Corporate Services will report on Treasury Management activity/performance as follows:

| Report to/Coverage | Frequency: |
|---|---|
| Council | |
| Treasury Management Strategy/Annual Investment Strategy/MRP Policy | Annually before start of the year |
| Treasury Management Strategy/Annual Investment Strategy/MRP Policy – mid year report | Annually mid year |
| Treasury Outturn report | Annually after year end and by 30 September |
| Cabinet | |
| Receives each of the above reports in advance of Council and makes recommendations as appropriate | In advance of year/mid-year/after year end and by 30 September |
| Receives details of Treasury transactions against Strategy | Every cycle |
| Audit and Standards Committee | |
| Receives each of the above reports in advance of Cabinet and makes observations as appropriate | In advance of year/mid-year/after year end and by 30 September |
| Reviews details of Treasury transactions against Strategy and makes observations to Cabinet | Every cycle |

## 15. Training

15.1 The TM Code requires the Director of Corporate Services, as responsible officer, to ensure that all councillors tasked with Treasury Management responsibilities, including scrutiny of the Treasury Management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Arlingclose will be asked to continue the briefing programme for Councillors which has been running since 2009 (the most recent session was held in September 2014).

15.2 The training needs of the Council's Treasury Management staff will be reviewed as part of the annual corporate staff appraisal/training needs assessment process for all Council employees. The Council's contract with Arlingclose includes provision for staff to attend training seminars and workshops.

## 16. Investment Consultants

The Council has appointed Arlingclose as its financial advisers for the period 1 July 2012 to 30 June 2016. Arlingclose will be the Council's primary source of information, advice and assistance relating to investment activity. Individual investment decisions are made by the Council. Review meetings are held at least twice a year, at which the quality of the service received to date is discussed.

## 17. Publication

The Annual Treasury Management Statement and Investment Strategy, along with any in-year revisions, can be downloaded from www.lewes.gov.uk and is also available on request to the Director of Corporate Services, Southover House, Southover Road, Lewes, or by email to finance@lewes.gov.uk.

## Appendix A - Arlingclose's Economic and Interest Rate Forecast

| | Dec-14 | Mar-15 | Jun-15 | Sep-15 | Dec-15 | Mar-16 | Jun-16 | Sep-16 | Dec-16 | Mar-17 | Jun-17 | Dec-17 | Mar-18 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Official Bank Rate | | | | | | | | | | | | | |
| Upside risk | | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 |
| Arlingclose Central Case | 0.50 | 0.50 | 0.50 | 0.75 | 0.75 | 1.00 | 1.00 | 1.25 | 1.25 | 1.50 | 1.50 | 1.75 | 1.75 |
| Downside risk | | | | 0.25 | 0.25 | 0.50 | 0.50 | 0.75 | 0.75 | 1.00 | 1.00 | 1.00 | 1.00 |
| | | | | | | | | | | | | | |
| 3-month LIBID rate | | | | | | | | | | | | | |
| Upside risk | 0.05 | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 |
| Arlingclose Central Case | 0.55 | 0.60 | 0.65 | 0.85 | 1.00 | 1.15 | 1.30 | 1.45 | 1.60 | 1.75 | 1.85 | 2.05 | 2.15 |
| Downside risk | 0.10 | 0.15 | 0.20 | 0.30 | 0.40 | 0.55 | 0.65 | 0.75 | 0.85 | -0.95 | -0.95 | -0.95 | -1.00 |
| | | | | | | | | | | | | | |
| 1-yr LIBID rate | | | | | | | | | | | | | |
| Upside risk | 0.10 | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 |
| Arlingclose Central Case | 0.95 | 1.00 | 1.05 | 1.20 | 1.35 | 1.50 | 1.65 | 1.80 | 1.95 | 2.10 | 2.20 | 2.40 | 2.50 |
| Downside risk | -0.30 | -0.35 | -0.40 | -0.45 | -0.50 | -0.55 | -0.60 | -0.65 | -0.70 | -0.75 | -0.80 | -0.80 | -0.80 |
| | | | | | | | | | | | | | |
| 5-yr gilt yield | | | | | | | | | | | | | |
| Upside risk | 0.30 | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.55 | 0.55 | 0.55 |
| Arlingclose Central Case | 1.70 | 1.75 | 1.90 | 2.00 | 2.10 | 2.20 | 2.30 | 2.40 | 2.50 | 2.60 | 2.70 | 2.90 | 2.95 |
| Downside risk | -0.30 | -0.35 | -0.35 | -0.35 | -0.40 | -0.45 | -0.50 | -0.55 | -0.60 | -0.65 | -0.70 | -0.70 | -0.70 |
| | | | | | | | | | | | | | |
| 10-yr gilt yield | | | | | | | | | | | | | |
| Upside risk | 0.30 | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.55 | 0.55 | 0.55 |
| Arlingclose Central Case | 2.40 | 2.45 | 2.55 | 2.60 | 2.65 | 2.70 | 2.75 | 2.80 | 2.85 | 2.90 | 2.95 | 3.05 | 3.10 |
| Downside risk | -0.30 | -0.35 | -0.35 | -0.35 | -0.40 | -0.45 | -0.50 | -0.55 | -0.55 | -0.55 | -0.60 | -0.60 | -0.60 |
| | | | | | | | | | | | | | |
| 20-yr gilt yield | | | | | | | | | | | | | |
| Upside risk | 0.30 | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.55 | 0.55 | 0.55 |
| Arlingclose Central Case | 2.90 | 2.95 | 3.05 | 3.10 | 3.15 | 3.20 | 3.25 | 3.30 | 3.35 | 3.40 | 3.45 | 3.50 | 3.55 |
| Downside risk | -0.30 | -0.35 | -0.35 | -0.35 | -0.40 | -0.45 | -0.50 | -0.50 | -0.55 | -0.55 | -0.60 | -0.60 | -0.60 |
| | | | | | | | | | | | | | |
| 50-yr gilt yield | | | | | | | | | | | | | |
| Upside risk | 0.30 | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.55 | 0.55 | 0.55 |
| Arlingclose Central Case | 3.00 | 3.05 | 3.10 | 3.15 | 3.20 | 3.25 | 3.30 | 3.35 | 3.40 | 3.45 | 3.50 | 3.55 | 3.60 |
| Downside risk | -0.30 | -0.35 | -0.35 | -0.35 | -0.40 | -0.45 | -0.50 | -0.55 | -0.55 | -0.55 | -0.60 | -0.60 | -0.60 |

### Commentary:

### Underlying assumptions:

- The UK economic recovery has continued. Household consumption remains a significant driver, but there are signs that growth is becoming more balanced. The greater contribution from business investment should support continued, albeit slower, expansion of GDP throughout this year.
- We expect consumption growth to slow, given softening housing market activity, the muted outlook for wage growth and slower employment growth. The subdued global environment suggests there is little prospect of significant contribution from external demand.
- Inflationary pressure is currently low and is likely to remain so in the short-term. Despite a correction in the appreciation of sterling against the US dollar, imported inflation remains limited. We expect commodity prices will remain subdued given the weak outlook for global growth.
- The MPC's focus is on both the degree of spare capacity in the economy and the rate at which this will be used up, factors prompting some debate on the Committee.
- Nominal earnings growth remains weak and below inflation, despite large falls in unemployment, which poses a dilemma for the MPC. Our view is that spare capacity remains extensive. The levels of part-time, self-

employment and underemployment are significant and indicate capacity within the employed workforce, in addition to the still large unemployed pool. Productivity growth can therefore remain weak in the short term without creating undue inflationary pressure.

- However, we also expect employment growth to slow as economic growth decelerates. This is likely to boost productivity, which will bear down on unit labour costs and inflationary pressure.
- In addition to the lack of wage and inflationary pressures, policymakers are evidently concerned about the bleak prospects for the Eurozone. These factors will maintain the dovish stance of the MPC in the medium term.
- The continuing repair of public and private sector balance sheets leave them sensitive to higher interest rates. The MPC clearly believes the appropriate level for Bank Rate for the post-crisis UK economy is significantly lower than the previous norm. We would suggest this is between 2.5 and 3.5%.
- While the ECB is likely to introduce outright QE, fears for the Eurozone are likely to maintain a safe haven bid for UK government debt, keeping gilt yields artificially low in the short term.
- The probability of potential upside risks crystallising have waned a little over the past two months. The primary upside risk is a swifter recovery in the Eurozone.

**Forecast:**

- Arlingclose continues to forecast the first rise in official interest rates in Q3 2015; general market sentiment is now close to this forecast. There is momentum in the economy, but inflationary pressure is benign and external risks have increased, reducing the likelihood of immediate monetary tightening.
- We project a slow rise in Bank Rate. The pace of interest rate rises will be gradual and the extent of rises limited; we believe the normalised level of Bank Rate post-crisis to range between 2.5% and 3.5%.
- The short run path for gilt yields is flatter due to the deteriorating Eurozone situation. We project gilt yields on an upward path in the medium term.

**Appendix B – Prudential Indicators 2015/2016 to 2017/2018**

## 1. Background:

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their Prudential Indicators. Some of the Prudential Indicators relate directly to the Council's Capital Programme and are considered by Cabinet when the Capital Programme is set. These Indicators are also included below for completeness of reporting.

## 2. Net Borrowing and the Capital Financing Requirement:

2.1 This is a key indicator of prudence. In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that the net external borrowing does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.

2.2 The Director of Finance reports that the Council has had no difficulty meeting this requirement in 2014/2015, nor are there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the draft budget for 2015/2016.

## 3. Estimates of Capital Expenditure (direct link to Capital Programme)

This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax and in the case of the HRA, housing rent levels.

| No. | Capital Expenditure | 2014/15 Original £m | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|---|---|
| 1a | Non-HRA | 2.063 | 10.714 | 6.319 | 2.610 | 1.361 |
| 1b | HRA | 5.683 | 5.880 | 9.347 | 5.530 | 5.530 |
| | **Total** | **7.746** | **16.594** | **15.666** | **8.140** | **6.891** |

## 4. Ratio of Financing Costs to Net Revenue Stream (direct link to Capital Programme)

4.1 This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet borrowing costs.

4.2 The ratio is based on costs net of investment income. Where investment income exceeds interest payments, the indicator is negative.

| No. | Ratio of Financing Costs to Net Revenue Stream | 2014/15 Original % | 2014/15 Revised % | 2015/16 Estimate % | 2016/17 Estimate % | 2017/18 Estimate % |
|---|---|---|---|---|---|---|
| 2a | Non-HRA | 0.95 | To be completed | | | |
| 2b | HRA | 21.51 | | | | |

## 5. Capital Financing Requirement

5.1 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. The calculation of the CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and its financing.

| No | Capital Financing Requirement | 2014/15 Original £m | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|---|---|
| 3a | Non-HRA | 4.512 | 5.919 | 8.421 | 8.123 | 7.837 |
| 3b | HRA | 65.779 | 64.790 | 65.613 | 64.119 | 62.624 |
| | **Total CFR** | **70.291** | **70.709** | **74.034** | **72.242** | **70.461** |

5.2 The year-on-year change in the CFR is set out below.

| Capital Financing Requirement | 2014/15 Original £m | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|---|
| **Balance B/F** | 71.880 | 71.448 | 70.709 | 74.034 | 72.242 |
| Capital expenditure financed from borrowing | 0.273 | 1.122 | 5.202 | 0.185 | 0.185 |
| Revenue provision for Debt Redemption. | -1.862 | -1.861 | -1.877 | -1.977 | -1.966 |
| **Balance C/F** | **70.291** | **70.709** | **74.034** | **72.242** | **70.461** |

## 6. Actual External Debt

This indicator is obtained directly from the Council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities. This Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

| No. | Actual External Debt as at 31/03/2015 | £m |
|---|---|---|
| 4a | Borrowing | 56.673 |
| 4b | Other Long-term Liabilities | 0.000 |
| **4c** | **Total** | **56.673** |

## 7. Incremental Impact of Capital Investment Decisions Stream (direct link to Capital Programme)

This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax and Housing Rent levels. The incremental impact is calculated by comparing the total revenue budget requirement of the current approved capital programme with an equivalent calculation of the revenue budget requirement arising from the proposed capital programme.

| No. | Incremental Impact of Capital Investment Decisions | 2014/15 Original £ | 2014/15 Revised £ | 2015/16 Estimate £ | 2016/17 Estimate £ | 2017/18 Estimate £ |
|---|---|---|---|---|---|---|
| 5a | Increase in Band D Council Tax | 38.30 | To be completed | | | |
| 5b | Increase in Average Weekly Housing Rents | 8.31 | | | | |

The increase in Band D council tax/average weekly rents reflects the funding of the capital programme: for example, funding from reserves utilises resources which could have otherwise been used to fund revenue expenditure.

## 8. Authorised Limit and Operational Boundary for External Debt

8.1 The Council has an integrated Treasury Management strategy and manages its Treasury position in accordance with its approved strategy and practice. Overall borrowing will therefore arise as a consequence of all the financial transactions of the Council and not just those arising from capital spending reflected in the CFR.

8.2 The **Authorised Limit** sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities). This Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases.

8.3 The Authorised Limit has been set on the estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements.

8.4 The Authorised Limit is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).

| No. | Authorised Limit for External Debt | 2014/15 Original £m | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|---|---|
| 6a | Borrowing | 72.00 | 72.00 | 76.00 | 76.00 | 76.00 |
| 6b | Other Long-term Liabilities | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 |
| **6c** | **Total** | **72.50** | **72.50** | **76.50** | **76.50** | **76.50** |

8.5 The **Operational Boundary** links directly to the Council's estimates of the CFR and estimates of other cashflow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

8.6 The Director of Corporate Services has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next meeting of the Cabinet.

| No. | Operational Boundary for External Debt | 2014/15 Original £m | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|---|---|
| 7a | Borrowing | 66.50 | 66.50 | 70.50 | 70.50 | 70.50 |
| 7b | Other Long-term Liabilities | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 |
| **7c** | **Total** | **67.00** | **67.00** | **71.00** | **71.00** | **71.00** |

## 9. Adoption of the CIPFA Treasury Management Code

This indicator demonstrates that the Council has adopted the principles of best practice.

| No. | Adoption of the CIPFA Code of Practice in Treasury Management |
|---|---|
| 8 | The Council approved the adoption of the revised CIPFA Treasury Management Code in February 2010. The Council has incorporated the changes from the CIPFA Code of Practice and subsequent revisions into its treasury policies, procedures and practices. |

## 10. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure

10.1 These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. This Council calculates these limits on net principal outstanding sums ie fixed rate debt net of fixed rate investments.

10.2 The upper limit for variable rate exposure has been set to ensure that the Council is not exposed to interest rate rises which could adversely impact on the revenue budget.

| No. | | 2014/15 Original £m | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|---|---|
| **9** | **Upper Limit for Fixed Interest Rate Exposure** | 72.5 | 72.5 | 76.5 | 76.5 | 76.5 |
| **10** | **Upper Limit for Variable Interest Rate Exposure** | (27.5) | (27.5) | (27.5) | (27.5) | (27.5) |

10.3 The limits above provide the necessary flexibility within which decisions will be made for drawing down new loans on a fixed or variable rate basis; the decisions will ultimately be determined by expectations of anticipated interest rate movements as set out in the Council's Treasury Management Strategy.

10.4 Because the Council's investments are substantially in excess of its variable rate borrowing, the Upper Limit for Variable Interest Rate exposure is shown as a negative figure.

## 11. Maturity Structure of Fixed Rate borrowing

11.1 This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

11.2 It is calculated as the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate. The maturity of borrowing is determined by reference to the earliest date on which the lender can require payment.

| No. | Maturity structure of fixed rate borrowing | Lower Limit % | Upper Limit % |
|---|---|---|---|
| 11a | under 12 months | 0 | 70 |
| 11b | 12 months and within 24 months | 0 | 70 |
| 11c | 24 months and within 5 years | 0 | 75 |
| 11d | 5 years and within 10 years | 0 | 75 |
| 11e | 10 years and above | 0 | 100 |

## 12. Upper Limit for total principal sums invested over 364 days

The purpose of this limit is to contain exposure to the possibility of loss that may arise as a result of the Council having to seek early repayment of the sums invested.

| No. | Upper Limit for total principal sums invested over 364 days | 2014/15 Original % | 2014/15 Revised % | 2015/16 Estimate % | 2016/17 Estimate % | 2017/18 Estimate % |
|---|---|---|---|---|---|---|
| 12 | Upper limit | 50 | 50 | 50 | 50 | 50 |

## 13. HRA Limit on Indebtedness

This Prudential Indicator is associated with the introduction of self-financing for housing. It indicates the residual capacity to borrow for housing purposes, while remaining within the overall HRA Debt Cap specified by the Government.

| No | Capital Financing Requirement | 2014/15 Original £m | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|---|---|
| 13a | HRA CFR | 65.779 | 64.79 | 65.613 | 64.119 | 62.624 |
| 13b | HRA Debt Cap | 72.931 | 72.931 | 75.248 | 75.248 | 75.248 |
| | **Difference** | **7.152** | **8.141** | **9.635** | **11.129** | **12.624** |

## Appendix C – Approved Investment Counterparties and Limits

| Credit Rating | Banks Unsecured | Banks Secured | Government | Corporates | Registered Providers |
|---|---|---|---|---|---|
| UK Govt | n/a | n/a | £ Unlimited 50 years | n/a | n/a |
| AAA | £2m 5 years | £2m 20 years | £2m 50 years | £2m 20 years | £2m 20 years |
| AA+ | £2m 5 years | £2m 10 years | £2m 25 years | £2m 10 years | £2m 10 years |
| AA | £2m 4 years | £2m 5 years | £2m 15 years | £2m 5 years | £2m 10 years |
| AA- | £2m 3 years | £2m 4 years | £2m 10 years | £2m 4 years | £2m 10 years |
| A+ | £2m 2 years | £2m 3 years | £2m 5 years | £2m 3 years | £2m 5 years |
| A | £2m 13 months | £2m 2 years | £2m 5 years | £2m 2 years | £2m 5 years |
| See note below | | | | | |
| A- | £2m 6 months | £2m 13 months | No use | No use | No use |
| BBB+ | £2m 100 days | £2m 6 months | No use | No use | No use |
| BBB or BBB- | £2m next day only | £2m 100 days | No use | No use | No use |
| Pooled funds | £3m per fund | | | | |

Approved investments with institutions with credit ratings of A- or below will only be permissible in the event of rating agencies downgrading the ratings of major UK banks in response to the bail-in provisions of the EU Bank Recovery and Resolution Directive.

Further details of the counterparty types shown in the table above are as follows:

**Banks Unsecured:** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. Unsecured investment with banks rated BBB or BBB- are restricted to overnight deposits at the Council's current account bank.

**Banks Secured:** Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the highest of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

**Government:** Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.

**Corporates:** Loans and bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made as part of a diversified pool in order to spread the risk widely.

**Registered Providers:** Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services, they retain a high likelihood of receiving government support if needed.

**Pooled Funds:** Shares in diversified investment vehicles consisting of any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Money Market Funds that offer same-day liquidity and aim for a constant net asset value will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.

## Glossary of Terms

| | |
|---|---|
| Affordable Borrowing Limit | Each local authority is required by statute to determine and keep under review how much money it can afford to borrow. The Prudential Code (see below) sets out how affordability is to be measured. |
| Base Rate | The main interest rate in the economy, set by the Bank Of England, upon which others rates are based. |
| Bonds | Debt instruments issued by government, multinational companies, banks and multilateral development banks. Interest is paid by the issuer to the bond holder at regular pre-agreed periods. The repayment date of the principal is also set at the outset. |
| Capital Expenditure | Spending on the purchase, major repair, or improvement of assets eg buildings and vehicles |
| Capital Financing Requirement (CFR) | Calculated in accordance with government regulations, the CFR represents the amount of Capital Expenditure that it has incurred over the years and which has not yet been funded from capital receipts, grants or other forms of income. It represents the Council's underlying need to borrow. |
| Chartered Institute of Public Finance and Accountancy (CIPFA) | CIPFA is one of the leading professional accountancy bodies in the UK and the only one that specialises in the public services. It is responsible for the education and training of professional accountants and for their regulation through the setting and monitoring of professional standards. Uniquely among the professional accountancy bodies in the UK, CIPFA has responsibility for setting accounting standards for a significant part of the economy, namely local government. |
| Counterparty | Organisation with which the Council makes an investment |
| Credit Default Swaps | CDS are a financial instrument for swapping the risk of debt default and are effectively an insurance premium. Local authorities do not trade in CDS but trends in CDS prices can be monitored as an indicator of relative confidence about the credit risk of counterparties. |
| Credit Rating | A credit rating is an independent assessment of the credit quality of an institution made by an organisation known as a rating agency. The rating agencies take many factors into consideration when forming their view of the likelihood that an institution will default on their obligations, including the institution's willingness and ability to repay. The ratings awarded typically cover the short term outlook, the long term outlook, as well as an assessment of the extent to which the parent company or the state will honour any obligations. At present, the three main agencies providing credit |

| | |
|---|---|
| | rating services are Fitch Ratings, Moody's and Standard and Poor's. |
| Fixed Deposits | Loans to institutions which are for a fixed period at a fixed rate of interest |
| Gilts | These are issued by the UK government in order to finance public expenditure. Gilts are generally issued for set periods and pay a fixed rate of interest. During the life of a gilt it will be traded at price decided in the market. |
| Housing Revenue Account (HRA) | There is a statutory requirement for local authorities to account separately for expenditure incurred and income received in respect of the dwellings that they own and manage. |
| International Financial Reporting Standards (IFRS) | The set of accounting rules with which all local authorities have been required to comply from 1 April 2010. |
| Lenders' Option Borrower's Option (LOBO) | A long term loan with a fixed interest rate. On pre-determined dates (eg every five years) the lender can propose or impose a new fixed rate for the remaining term of the loan and the borrower has the 'option' to either accept the new imposed fixed rate or repay the loan. |
| LIBID | The rate of interest at which first-class banks in London will bid for deposit funds |
| Minimum Revenue Provision (MRP) | The minimum amount which must be charged to an authority's revenue account each year and set aside as provision for the repayment of debt. |
| Operational boundary | This is the most likely, prudent view of the level of gross external indebtedness. A temporary breach of the operational boundary is not significant. |
| Prudential Code/Prudential Indicators | The level of capital expenditure by local authorities is not rationed by central government. Instead the level is set by local authorities, providing it is within the limits of affordability and prudence they set themselves. The Prudential Code sets out the indicators to be used and the factors to be taken into account when setting these limits |
| Public Works Loan Board (PWLB) | A central government agency which provides long- and medium-term loans to local authorities at interest rates only slightly higher than those at which the Government itself can borrow. |
| Treasury Management Strategy Statement (TMSS) | Approved each year, this document sets out the strategy that the Council will follow in respect of investments and financing both in the forthcoming financial year and the following two years. |
| Treasury Bills (T-Bills) | These are issued by the UK Government as part of the Debt Management Office's cash management operations. They do not pay interest but are issued at a discount and are redeemed at par. T-Bills have up to 12 months maturity when first issued. |