Appendix 10

TREASURY MANAGEMENT and INVESTMENT STRATEGY 2018/19 to 2022/23

SUMMARY

The Treasury Management and Investment Strategy represent the Council's operating guidelines on the daily management of cash, investments and borrowing. Through daily cashflow management, surplus cash is invested with security of investments being the prime consideration; only then are the yield and liquidity of investments, within the Council's risk parameters, considered.

Over the longer term, the Council considers the need to borrow money to fund its major capital projects and when the best time is to do this. The strategy aims to minimise borrowing and make use of internal funds where viable. Currently, there is an expectation that new borrowing will be required during 2018/19 of £107m. New borrowing to fund the capital financing requirement will be taken for cash flow purposes or where there is a positive budget impact in terms of the cost of carry. New debt will be a mixture of short and medium term durations designed to minimise cost without having a detrimental effect on re-financing risk.

Interest rates are forecast to stay low and investment returns will remain subdued for short-term and liquid cash.

This report details the investment instruments and counterparties in which the Council can invest. All institutions on the Counterparty List are regularly monitored assessing risk and determining the duration and value of limits on investments with counterparties.

For 2018/19, the following changes are proposed for the Treasury Management Strategy Statement (TMSS).

- Following European Money Market Fund reform, from January 2019, "Constant Net Asset Value" (CNAV) Funds will convert to "Low Volatility Net Asset Value" (LVNAV) Funds. The Council has expanded its Money Market Fund determination to accommodate the new classification.

- The European Markets in Financial Instruments Directive (MiFID II) came into force with effect from 3rd January 2018. MiFID II requires the Council to hold a minimum balance to be able to maintain its professional investor status and therefore access the services of advisers, brokers, custodians and counterparty investment vehicles. The Council has set a minimum investment level of £15m through Non-specified Pooled fund exposure which has been extended from 3 to 5 years in duration. A £15m investment into strategic and long-dated Non-specified pooled funds also aligns with the proposal to make greater use of the Council's reserves and the long-term objective of achieving £400k annual returns on this investment.

1. INTRODUCTION

1.1 Under the Local Government Act 2003 the Council has a legal obligation to have regard to both the CIPFA Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code) and DCLG Guidance on local authority investments in determining the Treasury Management Strategy Statement, Investment Strategy, Prudential Indicators and Minimum Revenue Provision Statement for the following financial year. The strategy is developed as part of the Council's MTFF process. The Council formally adopted the CIPFA Code in February 2012.

1.2 CIPFA consulted on changes to the Code and the Prudential Framework at the end of 2017. The new Code was issued in January 2018; however guidance notes are yet to be published. Following publication of the revised guidance notes any updated strategy documents will be brought to the relevant body for approval.

1.3 The Council, by having significant investments and borrowing, is exposed to financial risks, including the loss of invested funds and the revenue effect of changing interest rates. As such treasury management operations are fundamentally concerned with managing risk. Whilst there are regulations and controls in place designed to minimise or neutralise risk, some risk exposure remains due to the nature of managing loan and investment portfolios and cash flow activities. Active monitoring of the economic outlook, as well as changes in regulation, is undertaken where it impacts on the Council's treasury management strategy and risk parameters.

1.4 The major external influence on the Council's treasury management strategy for 2018/19 will be the UK's progress in negotiating its exit from the European Union and agreeing future trading arrangements. The domestic economy has remained relatively robust since the outcome of the 2016 referendum, but there are indications that uncertainty over the future is now weighing on growth. Transitional arrangements may prevent a cliff-edge, but will also extend the period of uncertainty for several years. Economic growth is therefore forecast to remain sluggish throughout 2018/19. Consumer price inflation was at 3.0% in December 2017 as the post-referendum devaluation of sterling continued to feed through to imports. However, this effect is expected to fall out of year-on-year inflation measures during 2018, removing pressure on the Bank of England to raise interest rates.

2. BALANCE SHEET AND TREASURY POSITION

1.5 The Council's borrowing strategy is driven by the estimated Balance Sheet position in the medium term and capital programme expectations. The underlying need to borrow for capital purposes is reflected by the Capital Financing Requirement (CFR) which measures the cumulative capital expenditure that has not been financed from other Council resources such as capital grants, revenue contributions or reserve financing. The CFR will generally be higher than the actual debt held due to timing requirements for cash flow purposes. This is called "internal borrowing".

1.6 Estimates of the CFR, based on the projected capital programme over the next five years are shown in Table 1. The Council's opening CFR is estimated at £421m for 2018/19, based on the closing 2017/18 figures, outstanding loans £250m and other long term liabilities of £1m, resulting in a gross borrowing requirement of £170m. Existing borrowing is identified into separate loan pools for GF and HRA. GF debt is £61m and HRA £189m.

Table 1

	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m
General Fund CFR	219	285	322	348	356	347
HRA CFR	202	193	207	201	207	205
Total CFR	**421**	**478**	**529**	**549**	**563**	**552**
Existing Borrowing *	251	234	217	203	198	185
Gross External Borrowing required to meet CFR	**170**	**244**	**312**	**346**	**365**	**367**
Projected Usable Reserves **	142	114	108	101	98	98
Projected Working Capital	38	38	38	38	38	38
Investments / (New Borrowing Required)	**10**	**(92)**	**(166)**	**(207)**	**(229)**	**(231)**

* Borrowing profile does not include potential calls on LOBO borrowing. Borrowing includes £191.6m (£130.6m balance) paid to government by the HRA as settlement on the introduction of the self financing regime in March 2012.
** Council controllable reserves only

1.7 The increasing General Fund CFR is due to the Council's programme of capital investment funded by Council resources. The Capital programme continues to focus on provision of sufficient schools places to meet rising demand across the borough. In addition there are provisions in place for major investment on the St Andrews Park site in Uxbridge, a new swimming pool in the Yiewsley/West Drayton area and improvements to the Borough's highways. The Council is forecast to require borrowing from 2018/19 to meet the current costs of the capital programme.

1.8 Under the Prudential Code for Local Authorities, the Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Council expects to comply with this, as new borrowing and existing borrow are less than the total CFR.

1.9 The Council's projected capital programme over the next five years, alongside the projected financing, is fundamental in determining a borrowing strategy. Annex A provides detail on the Prudential Indicators associated with capital expenditure projections and its incremental impact on council tax and housing rent levels.

3. BORROWING STRATEGY

1.10 The Council's external debt at 31 March 2018 will be £250.1m, a decrease of £17.3m on the previous year as a result of naturally maturing debt. There were no opportunities to repay debt in 2017/18. A further £17.3m is scheduled for repayment in 2018/19. Over 2017/18 the Council's loan portfolio had an average interest rate of 3.29%.

1.11 Projected capital expenditure levels, market conditions and interest rate levels are monitored throughout the year. This enables the Council to adapt borrowing strategies to minimise borrowing costs over the medium to longer term whilst maintaining financial stability. Table 1 above shows the Council is expecting it will need to borrow in 2018/19 based on the full capital programme and debt maturity profile.

1.12 Where prudent the Council can take short-term borrowing to offset its current internal borrowing to retain an element of cash reserves for long-term strategic investment purposes. It is forecast that over the TMSS period £15m will be sourced from other Local Authorities for this purpose. This will enable to Council to meet the MiFID II minimum investment balance criteria with the subsequent long-dated investments contributing to the income target.

1.13 Taking new fixed rate borrowing in advance of need would not normally be cost effective when compared to utilising internal balances, due to the differential between debt costs and investment earnings, despite long term borrowing rates being at low levels; however this position may change with changes in interest rates. Delaying borrowing until required for cash flow purposes allows the Council to reduce credit risk and takes pressure off the Council's Counterparty list.

1.14 If the Council takes out new borrowing the Council will consider the following approved sources of borrowing:

- Public Works Loan Board and its successor body
- UK local authorities
- Any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except Hillingdon Pension Fund)
- Capital market bond investors
- Municipal Bonds Agency (subject to Cabinet approval)
- Other special purpose companies created to enable local authority bond issues
- Leasing, Hire Purchase, Private Finance Initiative and, Sale and Leaseback

1.15 Although a mix of borrowing options will always be considered, the PWLB (or equivalent) will remain the primary source of long-term and variable rate borrowing whilst rates remain closely linked to government gilts. The Council currently has access to the preferential PWLB "certainty rate", which is 0.2% lower than normal PWLB lending rates. To cover unexpected cash flow shortages or short term borrowing requirements, the Council may borrow short term, which would mainly be sourced from other local authorities.

1.16 Where borrowing is required this will be attributed directly to either the GF or HRA loan pools. Interest costs will be separated between the two pools and allocated accordingly.

Interest Rate Risk

1.17 The Council's has fixed rate loans of £237.1m which protect against interest rate rises, whilst there are variable rate loans totalling £13m, £3m take advantage of favourably low rates and £10m are LOBO loans in their call period during 18/19. Although variable rate loans are exposed to increases in rates, any additional loan costs would be offset by a corresponding increase in investment income. Additionally, within the balance of variable rate loans, £3m is PWLB debt which can be prematurely repaid with minimal cost should the need arise.

1.18 Within the loan portfolio, the Council holds market loans of £48m of which £36m are Lender's Option Borrower's Option (LOBO) loans. The remaining £12m are classified as fixed rate debt. In 2018/19 two loans totalling £10m will be in their call period and so are reclassified for the period as variable. It is highly unlikely that the loans will be called given interest rates are now lower than those at the inception of the loan. In the event that the lender exercises the option to change the rate or terms of the loan, the Council will consider the new terms and also the option of repayment of the loan without penalty. The Council may utilise cash resources for repayment or may consider replacing the loan by borrowing from the approved sources. The default position however will be early repayment without penalty. The Council will not utilise LOBO's for any new borrowing.

Debt Rescheduling

1.19 The PWLB allows authorities to repay loans before maturity at a premium or discount. The Council may take advantage of this and replace some loans with new loans or repay early without replacement. The rationale for rescheduling is to reduce interest costs with minimal risk; balance the volatility profile (i.e. the ratio of fixed to variable rate debt); or amend the profile of maturing debt to reduce any inherent refinancing risks.

1.20 Rates and markets are regularly monitored to identify opportunities for rescheduling and any borrowing and rescheduling activity is reported monthly to Cabinet. However, current market conditions are resulting in significant early redemption costs for fixed rate debt and unless these are significantly reduced, it is unlikely any debt rescheduling will be undertaken in 2018/19.

1.21 The Council will limit and monitor large concentrations of fixed rate debt needing to be replaced through the prudential indicator in table 2. The upper and lower percentage limits are intended to control excessive exposure to volatility in interest rates on refinancing of maturing fixed rate debt by setting a structure for borrowing maturity profiles. The first scheduled LOBO call option is included as the maturity date within this indicator.

Table 2

Maturity structure of fixed rate borrowing	% PWLB maturity profile at 31/03/18	% Market LOBO 1st call option profile at 31/03/18	Lower Limit for 2018/19 %	Upper Limit for 2018/19 %
under 12 months	6.39	4.05	0	25
12 months and within 24 months	6.39	2.43	0	25
24 months and within 5 years	12.50	6.07	0	50
5 years and within 10 years	11.13	2.02	0	100
10 years and within 20 years	23.47	0	0	100
20 years and within 30 years	9.13	0	0	100
30 years and within 40 years	11.57	0	0	100
40 years and within 50 years	3.23	0	0	100
50 years and above	1.62	0	0	100
Total	**85.43**	**14.57**	**0**	**100**

1.22 Prudential indicators in relation to borrowing limits and interest rate exposure are shown in Annex A.

4. INVESTMENT STRATEGY

1.23 In accordance with Investment Guidance from DCLG and best practice, the Council's primary objectives in relation to the investment of public funds remains:

- security of the invested capital;
- liquidity of the invested capital; and
- an optimum yield which is commensurate with security and liquidity.

1.24 When investing funds the Council looks to balance risk and return, minimising the risk of incurring losses from defaults, and the risk receiving unsuitably low investment income.

1.25 Negative Interest rates: If the UK enters into a recession in 2018/19, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

1.26 The Corporate Director of Finance under delegated powers will, on a daily basis, determine the most appropriate form of investments, in keeping with investment objectives, income and risk management requirements. Investments will also be made with reference to the Prudential Indicators and from approved investments detailed in Annex B. Decisions concerning the core strategic investment portfolio will be reported monthly to Cabinet.

Bail-In Risk

1.27 Banking reform legislation was incorporated into UK law from January 2015 and exposes the Council to bail-in risk on all unsecured bank deposits. The risk of bail-in is effective at the point when banks are considered to be underperforming rather than once they have failed. With most large entities either exempt or not exposed, local authorities will be one of the primary bail-in targets with a potential loss of 100% of the deposit.

1.28 There are a number of secure deposits available to the Council to reduce bail-in exposure. Secure deposits include Covered Bonds (fixed and floating rate notes) and Repurchase Agreements (REPO's). Secure deposits are longer in duration and can be difficult to invest as a result. An element of the Councils investments must remain liquid to fund cash flow requirements, resulting in bail-in risk being inherent in the Council's investment portfolio.

1.29 Covered Bonds are bail-in exempt and are issued in their own right rather than in the name of the counterparty, with each issue having its own credit rating. The covered bond has security of underlying assets which can be called upon in the event of default of the issuing counterparty. The decision to invest in a covered bond will be based on the individual bond issue rather than an agreed list of specific counterparties, as each bond is standalone from the issuing counterparty and should be assessed individually. Duration and exposure limits will be aligned with the credit rating of the bond issue with consideration to other investment factors. The Council will only invest in a covered bond which is rated AA or above.

1.30 Repurchase Agreements (REPO's) require the use of either a tri-party facilitator to negotiate and hold the instrument or a custodian and broker if a bi-lateral arrangement is in place. REPO's are ring-fenced and not subject to the failure of the issuing counterparty, making them bail-in exempt instruments; however unlike Covered Bonds REPOs are issued in the name of the counterparty.

Funds

1.31 Money Market Funds (MMF's) remain an important vehicle for instant access deposits. Money Market Funds reduce the risk of bail-in as the funds are diversified with limits on the exposure to any specific bank. The Council also utilises more than one MMF to diversify exposure. Where MMF’s participate, the Council utilises the facilities of a MMF portal to make subscriptions and redemptions. The portal procedure involves the use of a clearing agent; however the Council’s funds are ring-fenced throughout the process. By January 2019 European Money Market Fund reform will require the conversion Constant Net Asset Value (CNAV) MMF's to Low Volatility Net Asset Value (LVNAV) funds. This change in classification has been reflected within the Specified Investment section in Annex B.

1.32 Pooled Funds provide the Council with the facility to access a diversified pool of longer duration investments which the Council could not utilise on a segregated basis. These funds have a variable net asset value and offer the potential of greater risk adjusted returns over the longer term. The Council expects to maintain its current holding of £15m within Cash-Plus and Short-Bond funds (Specified Investments) whilst placing a new allocation of £15m within Strategic & Long-Dated funds (Non-Specified Investments).

Credit Risk

1.33 Credit ratings remain an important element of assessing credit risk but they are not the sole feature in the assessment of counterparties. The Council also considers alternative assessments of credit strength and information including corporate intelligence, market sentiment and pricing as well as any overriding doubts regarding security.

1.34 The Council's in-house investments are made with reference to the outlook for the UK Bank Rate, money market rates and other macroeconomic factors. In any period of significant stress in the markets or heightened counterparty risk, the fallback position is for investments to be placed with central government's Debt Management Office (DMO) or to purchase UK Treasury Bills. The rates of interest from the DMO are below the equivalent money market rates in most cases, but this is an acceptable counterbalance for the guarantee that the Council's capital is secure.

High Credit Quality

1.35 The Council has defined "high credit quality" organisations and securities as those having a minimum credit rating of A- for UK counterparties, A+ for overseas counterparties and AA+ for non-UK sovereigns. Covered Bonds will be restricted to bond issues of AA or above. The Council's portfolio average credit rating as at 31 March 2018 is forecast at AA-.

1.36 In order to diversify investments within the portfolio, funds will be placed with a range of counterparties which meet agreed minimum credit risk requirements. Diversification will be achieved by applying individual limits with each counterparty; for unsecured deposits this is capped at 5% of the total portfolio. Varying instruments and investment periods will be utilised to meet liquidity requirements and mitigate risks. Annex B details counterparty Institutions, investment limits and allowable instruments.

Risk Assessment and Credit Ratings

1.37 Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded resulting in it failing to continue 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; and

- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

1.38 Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as “rating watch negative” or “credit watch negative”) so that it may fall below the approved rating criteria, then only new investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Liquidity Risk

1.39 The Council will ensure it has liquid funds available to settle its payment obligations when they fall due and uses cash flow modelling techniques to determine the maximum term for which funds may be prudently committed. It will utilise instant access facilities including call accounts and Money Market Funds (MMF's) for core working capital balances and structure longer term maturities to correspond to large cash outflows with reference to the Council's capital programme.

Return on Invested Sums

1.40 As interest rates are forecast to remain low on liquid balances, the investment strategy is aiming to lengthen investment periods, where cashflow and credit conditions permit, in order to lock in higher rates of acceptable risk adjusted returns. Longer term investments will typically be through deposits with local authority entities, the use of secured deposits and Strategic & Long-Dated pooled funds. For 2018/19 a new £15m allocation to Strategic and Long-Dated pooled funds is targeting excess returns of 3% and £400k income per annum over the investment period.

Council's Bank Account

1.41 The Council's bank account is held with Lloyds Bank Plc and is currently rated above the Council's agreed minimum A- rating at A. Should the credit rating fall below A- the Council may continue to deposit surplus cash providing that investments can be withdrawn on the next working day, and that the bank maintains a credit rating no lower than BBB-.

Non-Treasury Investments

1.42 Although not classed as treasury management activities and therefore not covered by the CIPFA Code or the CLG Guidance, the Council may also purchase property or set up vehicles for investment purposes. It may also make loans and investments for service purposes. Such loans and investments will be subject to the Council's normal approval processes for revenue and capital expenditure and need not comply with this treasury management strategy.

5. OTHER ITEMS

Policy on Use of Financial Derivatives

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

1.44 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 to which the Council is exposed. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

1.45 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.

Policy on Apportioning Interest to the Housing Revenue Account (HRA)

1.46 With the introduction of HRA self financing in March 2012 the Council allocated specific loans to both the General Fund and the HRA. Interest costs applicable to each loan are charged directly to the respective revenue account.

1.47 Interest earned on HRA balances will be calculated and distributed in accordance with DCLG guidelines and based on a DMADF risk free rate of return to match the risk free credit exposure applicable to the HRA.

Investment of Money Borrowed in Advance of Need

1.48 The Council may borrow in advance of need, where this is expected to provide the best long-term value for money. However, as amounts borrowed will be invested until spent, the Council is aware that it would be exposed to the risk of loss of the borrowed sums and the risk investment and borrowing interest rates may change in the intervening period. These risks would be managed as part of the Councils overall management of its treasury risks. The total amount borrowed would not exceed the authorised borrowing limit. 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.

Balanced Budget Requirement

1.49 The Council complies with the provisions of S32 of the Local Government Finance Act 1992 to set a balanced budget.

Investment Consultants

1.50 The Council has a contract in place with Arlingclose Ltd to provide treasury advisory services, which details the agreed schedule of services. Performance is measured against the schedule to ensure the services being provided are in line with the agreement.

Monitoring and Reporting

1.51 Treasury activity is monitored and reported to senior management on a daily and weekly basis. Monthly updates including compliance with Prudential Indicators are provided to Cabinet as part of the budget monitoring process.

1.52 The Treasury Management Strategy Statement is agreed by Cabinet in February prior to agreement at full Council before the start of each financial year. Amendments to the TMSS during the year are only done with Cabinet approval.

1.53 Following changes to the Code and the Prudential Framework issued in January 2018, the revised guidance is expected to follow in due course. Once issued any updated strategy documents will be brought to the relevant body for approval

Training

1.54 The CIPFA Code of Practice requires that all Members 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. The Council adopts a continuous performance and development programme to ensure officers are regularly appraised and any training needs addressed. Treasury Officers also attend regular training sessions, seminars and workshops which ensure their knowledge is up to date and relevant. Details of training received are maintained as part of the performance and development process. Council Members are provided access to additional training where required.

ANNEX A

Prudential Indicators and Estimates of Capital expenditure

The **Authorised Limit** sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) and is a statutory limit for borrowing determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).

Table 3

Authorised Limit for External Debt	**2017/18 Approved £m**	**2018/19 Estimate £m**	**2019/20 Estimate £m**	**2020/21 Estimate £m**	**2021/22 Estimate £m**	**2022/23 Estimate £m**
Borrowing	**510**	**578**	**592**	**592**	**593**	**582**
Other Long term Liabilities	1	1	1	1	0	0
Authorised Limit	**511**	**579**	**593**	**593**	**593**	**582**

The **Operational Boundary** is linked directly to the Council's estimates of the CFR and estimates of other day to day cashflow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent scenario but without the additional headroom included within the Authorised Limit. This facilitates short-term additional borrowing in the event of unforeseen adverse events.

Table 4

Operational Boundary for External Debt	**2017/18 Approved £m**	**2018/19 Estimate £m**	**2019/20 Estimate £m**	**2020/21 Estimate £m**	**2021/22 Estimate £m**	**2022/23 Estimate £m**
Borrowing	**480**	**548**	**562**	**562**	**563**	**552**
Other Long-term Liabilities	1	1	1	1	0	0
Operational Boundary	**481**	**549**	**563**	**563**	**563**	**552**

The Corporate Director of Finance has delegated authority, within the above limits, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Any such decisions will be based on the outcome of financial option appraisals and best value considerations based on current market and macroeconomic conditions. Cabinet is notified of any use of this delegated authority through monthly budget monitoring reports.

Upper Limits for Interest Rate Exposure

The following Prudential Indicators show the extent to which the Council is exposed to changes in interest rates. The upper limit for variable rate exposure has been set to ensure that the Council is not unduly exposed to interest rate rises, which could adversely impact its revenue budget. The limit allows for the use of variable rate debt to offset exposure to changes in short-term rates on investments.

Table 5

Upper Limits for Interest Rate Exposure	31/03/18 Estimate %	2017/18 Approved %	2018/19 Estimate %	2019/20 Estimate %	2020/21 Estimate %	2021/22 Estimate %	2022/23 Estimate %
Upper Limit for Fixed Interest Rate Exposure on Debt	95	100	100	100	100	100	100
Upper Limit for Fixed Interest Rate Exposure on Investments	0	(75)	(75)	(75)	(75)	(75)	(75)
Upper Limit for Variable Interest Rate Exposure on Debt	5	50	50	50	50	50	50
Upper Limit for Variable Interest Rate Exposure on Investments*	(100)	(100)	(100)	(100)	(100)	(100)	(100)

*Investments with duration less than one year are classified as variable.

Upper limits for principal over 364 days

The Council has placed an upper limit for principal sums invested for over 364 days, as required by the Prudential Code. 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. Under the Council's strategy only investments where risk is minimised, as set out in the non-specified investments in table 13, would be placed for over 1 year.

Table 6

Upper Limit for total principal sums invested over 364 days	2017/18 Approved £m	2018/19 Estimate £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m
	35	35	35	35	35	35

Estimates of Capital Expenditure and other Prudential Indicators

It is a requirement of the Prudential Code to ensure that 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. In an environment of 'low rates for longer' the Council's strategy is currently to defer external borrowing and use internal borrowing where possible, thus avoiding unnecessary interest payments and simultaneously reducing counterparty investment risks. Estimates for capital expenditure shown in Table 7 are estimates of likely capital cash outflows.

Table 7

Capital Expenditure	**2017/18 Approved £m**	**2017/18 Revised £m**	**2018/19 Estimate £m**	**2019/20 Estimate £m**	**2020/21 Estimate £m**	**2021/22 Estimate £m**	**2022/23 Estimate £m**
General Fund	66	62	108	100	72	53	40
HRA	63	73	53	51	39	44	34
Total	**129**	**135**	**161**	**151**	**111**	**97**	**74**

Capital expenditure is expected to be financed as follows:

Table 8

Capital Financing	**2017/18 Approved £m**	**2017/18 Revised £m**	**2018/19 Estimate £m**	**2019/20 Estimate £m**	**2020/21 Estimate £m**	**2021/22 Estimate £m**	**2022/23 Estimate £m**
Prudential Borrowing	37	29	69	68	38	34	10
Capital Receipts	29	36	19	19	27	26	23
Community Infrastructure Levy	5	3	5	6	6	6	6
Government Grants & External Contributions	18	21	25	41	22	11	14
Revenue Contributions	40	46	43	17	18	20	21
Total Capital Financing	**129**	**135**	**161**	**151**	**111**	**97**	**74**

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.

Table 9

Actual External Debt as at 31/03/2018	**£m**
General Fund Borrowing	61.5
HRA Borrowing	188.5
Other Long term Liabilities	1.4
Total	**251.4**

HRA Indebtedness: Following settlement and the introduction of the self-financing regime, a borrowing cap of £303.3m has been imposed by HM Treasury on HRA indebtedness. This gives the HRA potential headroom borrowing of up to £114.8m to finance future capital.

Incremental Impact of Capital Investment Decisions

As an indicator of affordability, Table 10 shows the notional impact of capital investment decisions on Council Tax and Housing Rent levels and represents the impact on these if the financing of the Capital programme were to be funded from taxes and rents.

Table 10

Incremental Impact of Capital Investment Decisions	**2017/18 Revised**	**2018/19 Estimate**	**2019/20 Estimate**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**
Increase in Band D Council Tax	£3.09	£10.09	£33.33	£18.95	£19.17	8.66
Increase in Average Weekly Housing Rents	£0.00	£0.00	£0.00	£0.00	£0.12	£0.53

The ratio of financing costs to the Council's net revenue stream is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of future revenue budgets required to meet borrowing costs. An element of the additional rents secured from new build properties within the HRA will contribute to borrowing costs linked to this investment. In terms of council tax, the incremental impact growth reflects the MTFF plan for priority growth projects in the Capital programme. There is an increase in the impact to council tax payers through to 2022/23 primarily due to the review of financing provisions during the budget setting process and an increase in financing costs due to the expectation of new borrowing mainly in support of secondary school expansion projects. These result in an increase in revenue costs that would that would ultimately fall on the local Council tax payer to fund.

Table 11

Ratio of Financing Costs to Net Revenue Stream	**2017/18 Revised**	**2018/19 Estimate**	**2019/20 Estimate**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**
General Fund	2%	3%	4%	5%	7%	7%
HRA	28%	28%	27%	27%	26%	25%

ANNEX B

Specified Investments & Non-Specified Investments

Specified investments are sterling denominated investments with a maximum maturity of one year. They also meet the “high credit quality” as decided by the Council and are not deemed capital expenditure investments under statute. Non-specified investments are those which do not meet the above criteria, for example more than 1 year in duration.

The Council defines “high credit quality” for:

- UK Organisations - The minimum credit rating is set at A- or higher
- Overseas Organisations - The minimum credit rating is set at A+ or higher
- Overseas Countries - The minimum credit rating for domiciles of overseas banks is set at AA+
- Secured Deposits - The minimum credit rating for collateral on secured deposits is set at AA.

Specified Investments identified for use by the Council

- Deposits in the DMO’s Debt Management Account Deposit Facility
- Deposits with UK local authorities
- Instant access facilities and fixed term deposits with specified banks & building societies
- Repurchase Agreements, Covered Bonds (Fixed and Floating Rate Notes))
- Gilts (bonds issued by the UK government)
- Treasury Bills (T-Bills)
- Local Authority Bonds
- Money Market Funds
- Pooled Funds

When determining the minimum acceptable credit quality the Council will not only consider the credit rating criteria above but also information on corporate developments and market sentiment towards investment counterparties, as set out in the Credit Risk indicator. For credit rated counterparties, the minimum criteria will be the lowest equivalent long term ratings assigned by Fitch, Moody’s and Standard & Poor’s (where assigned). Long-term minimum: A- (Fitch); A3 (Moody’s); A- (S&P). The Council will aim to have a weighted average credit score of A- for the whole portfolio of investments. Classification of specified and non-specified investment is made at the point of entering into the investment.

Table 12: Limits for Specified investments

Instrument	**Counterparty**	**Maximum Counterparty Limits %/£m**
Term Deposits	DMADF, DMO	No limit
Term Deposits	Other UK Local Authorities	£35m per Local Authority / No total limit
Instant Access Accounts / Notice Accounts / Term Deposits / Certificates of Deposit / REPO's	UK Banks and Building Societies - Lloyds Banking Group (Including Bank of Scotland) - Barclays Bank Plc - Close Brothers - Coventry Building Society - Goldman Sachs International Bank - HSBC Bank Plc - Leeds Building Society - Nationwide Building Society - Santander UK - Standard Chartered Bank	Unsecured Deposits Up to 5% / £7.5m (except Leeds Building Society £1m) Secured Deposit - REPO's (In addition to unsecured limits) Up to 10% / £15m
Instant Access Accounts / Notice Accounts / Term Deposits / Certificates of Deposit	Overseas Banks Australia - National Australia Bank Singapore - DBS Bank Ltd - Oversea-Chinese Banking Corporation Sweden - Svenska Handelsbanken - Nordea Bank	Unsecured Deposits 5% / £7.5m Overseas Bank Total - 50% in aggregate Secured Deposit - REPO's (In addition to unsecured limits) Up to 10% / £15m
Registered Secured Deposits (including Covered Bonds)	Bond issue minimum AA Rated	£15m / 10% (Per issue)
Gilts	DMO	No limit
Treasury Bills	DMO	No limit
Local Authority Bonds	Other UK Local Authorities	No limit
Money Market Funds	Money Market Funds (CNAV / LVNAV)	7.5%/£5m per fund. Maximum MMF exposure 50%
Pooled Funds	Pooled Funds (Cash Plus & Short-Bond Funds with investment horizons < 1year)	7.5%/£5m per fund. Maximum Pooled Fund exposure £15m

Note: The above list and limits would be amended on notification of any potential risk concerns. Cabinet will approve any additions to the above list of counterparties or investment instruments. There is no upper limit for the total of specified investments.

Non-Specified Investments (duration more than 1 year) - having considered the rational and risk associated with non-specified investments, the following have been determined for the Council's use:

Table 13

	Maximum maturity	**Max % of portfolio**
▪ Deposits and Bonds with other UK Local Authorities ▪ Deposits with UK Banks & Building Societies. ▪ Gilts ▪ Registered Secured Deposits (including Covered Bonds) AA rated or above	3 Years	40% in aggregate excluding Pooled Funds
▪ Pooled Funds (Strategic & Long-Dated Funds with investment horizons > 1year)	5 Years	£5m per fund Maximum Pooled Fund exposure £15m

In determining the period to maturity of an investment, the investment should be regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty. The Council aims to hold an investment level of £15m in strategic and long-dated pooled funds.

Appendix 10

ANNEX C

2018/19 MRP STATEMENT

Where the Council finances its capital programme through borrowing it must set aside resources annually through a Minimum Revenue Provision. This is within the revenue budget to repay the debt in later years. The Local Government Act 2003 requires the Council to have regard to Guidance on Minimum Revenue Provision issued by the Department of Communities and Local Government.

The four options available to establish a prudent amount of MRP are:

- Option 1: Regulatory Method
- Option 2: CFR Method (4%)
- Option 3: Asset Life Method (equal instalment or annuity method)
- Option 4: Depreciation Method

This does not preclude other prudent methods to provide for the repayment of debt principal.

MRP in 2018/19: Options 1 and 2 are used for GF supported borrowing prior to 31 March 2008. For capital expenditure incurred after 31 March 2008, MRP will generally be charged over the useful life of the assets, beginning in the year after the asset becomes operational. In all cases we will consider the most prudent method of providing for debt repayment. The HRA will make a form of MRP to pay down its self-financing settlement debt over the 30 year business cycle on which the settlement is based.

Capital expenditure incurred during 2018/19 is not subject to an MRP charge until 2019/20.