ITEM 12

**NORTH YORKSHIRE COUNTY COUNCIL**

**AUDIT COMMITTEE**

**3 March 2016**

**ANNUAL TREASURY MANAGEMENT STRATEGY 2016/17**

**Report of the Corporate Director – Strategic Resources**

## 1.0 PURPOSE OF REPORT

1.1 To Review the County Council's Treasury Management Policy Statement and Annual Treasury Management and Investment Strategy for 2016/17.

## 2.0 BACKGROUND

2.1 In its scrutiny role of the County Council's Treasury Management policies, strategies and day to day activities, this Committee receives regular updates on Treasury Management activities and developments, including the quarterly reports submitted to Executive. These updates and reports provide Audit Committee Members with details of the latest Treasury Management developments, both at a local and national level. They also enable Members to review Treasury Managements arrangements and consider whether they wish to make any recommendations to the Executive.

2.2 As the County Council is required to approve an up to date Annual Treasury Management and Investment Strategy before the start of the new financial year, it is not realistic for it to be reviewed by the Audit Committee in advance of its submission to Executive on 16 February and full Council on 24 February 2016.

2.3 The Annual Treasury Management documentation for 2016/17 is therefore submitted for review to this meeting of the Audit Committee. Any resulting proposals would then be considered at a subsequent meeting of the Executive. If any such proposals were accepted and required a change to the Strategies recently approved then the Executive could submit a revised version to the County Council at its meeting on 18 May 2016.

## 3.0 ANNUAL TREASURY MANAGEMENT POLICY / STRATEGY FOR 2016/17

3.1 The Full Treasury Management Documentation submitted to Executive on 16 February and full Council on 24 February 2016 is therefore attached and comprises of:

a) The Covering Report to Executive / Full Council

b) The County Council's Treasury Management Policy Statement (**Appendix A to the attached report)**

c) The Annual Treasury Management and Investment Strategy 2016/17 **(Appendix B to the attached report)** which incorporates a Minimum Revenue Provision Policy and a policy to Cap Capital Financing costs as a proportion on the annual Net Revenue Budget.

3.2 Audit Committee members are therefore invited to review this documentation and consider whether they would wish to make any proposals to be referred back to the Executive.

## 4.0 RECOMMENDATION

4.1 That Audit Committee Members review the attached 2016/17 Treasury Management documentation and consider whether they would wish to make proposals to be referred back to the Executive.

GARY FIELDING

Corporate Director – Strategic Resources

Central Services
County Hall
Northallerton

3 March 2016

APPENDIX

**NORTH YORKSHIRE COUNTY COUNCIL**

**EXECUTIVE**

**16 February 2016**

# TREASURY MANAGEMENT

**Report of the Corporate Director – Strategic Resources**

## 1.0 PURPOSE OF REPORT

1.1 To recommend to the Council an updated Annual Treasury Management Strategy for the financial year 2016/17 which incorporates:

(a) the Annual Investment Strategy;

(b) a Minimum Revenue Provision Policy;

(c) a policy to cap Capital Financing costs as a proportion of the annual Net Revenue Budget.

## 2.0 BACKGROUND

2.1 The Council is required to adopt certain procedures in relation to Treasury Management which is defined as

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

2.2 Primarily the Council is expected to comply with the terms of the **CIPFA Code of Practice on Treasury Management in the Public Services** which was last updated by CIPFA in November 2011 and adopted by the Council on 15 February 2012.

2.3 In addition, the Council must also comply with the **CIPFA Prudential Code for Capital Finance in Local Authorities** which impacts heavily on Treasury Management matters. This Code was also updated in November 2011 alongside the updated Code of Practice on Treasury Management referred to in **paragraph 2.2** above.

2.4 The Local Government Act 2003 requires the Council to have regard to the Prudential Code and set Prudential Indicators for the next three financial years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

2.5 In addition to the two CIPFA codes referred to in **paragraphs 2.2 and 2.3** above, the Government (Department of Communities and Local Government - CLG) issues statutory guidance on

(a) Local Government Investments - revised with effect from 1 April 2010, and;

(b) Minimum Revenue Provision (for debt repayment) - revised with effect from 1 April 2012

to which the Council must have regard.

2.6 A separate report on the Prudential Indicators for the three years 2016/17 to 2018/19 is also submitted to this Executive on 2 February 2016. That report should be read in conjunction with this report because of the interaction between the Prudential Indicators and the Treasury Management arrangements.

2.7 The combined effect of these Codes and other relevant Regulations is that the Council has to have in place by the start of the new financial year the following:

(a) an up to date **Treasury Management Policy Statement** - see **Section 3** below;

(b) a combined **Annual Treasury Management and Investment Strategy** and **Minimum Revenue Provision Policy** - see **Section 4**.

2.8 In addition to these Statutory Requirements, the Council also agreed an additional local policy to cap Capital Financing costs as a proportion of the annual Net Revenue Budget. This is now incorporated into the Annual Treasury Management and Investment Strategy.

2.9 This report considers the above requirements and then recommends an updated Annual Treasury Management Strategy for the financial year 2016/17 which incorporates the Annual Investment Strategy and required Minimum Revenue Provision Policy.

## 3.0 TREASURY MANAGEMENT POLICY STATEMENT

3.1 The CIPFA Code of Practice on Treasury Management (as updated in 2011) requires the Council to approve:

(a) a **Treasury Management Policy Statement** (TMPS) stating the Council's policies, objectives and approach to risk management of its Treasury Management activities;

(b) a framework of suitable **Treasury Management Practices** (TMPs) setting out the manner in which the Council will seek to achieve the policies and objectives set out in (a) and prescribing how it will manage and control those activities. The Code recommends 12 TMPs.

3.2 The TMPS referred to in **paragraph 3.1 (a)** is attached as **Appendix A** and reflects only very minor changes for 2016/17.

3.3 The 12 TMPs recommended by the code referred to in **paragraph 3.1 (b)** which were originally submitted to Members in March 2004 were updated and approved by the Audit Committee on 6 December 2012.

## 4.0 ANNUAL TREASURY MANAGEMENT AND INVESTMENT STRATEGY AND MINIMUM REVENUE PROVISION POLICY 2016/17

4.1 One of the key requirements of the CIPFA Code of Practice on Treasury Management continues to be that an Annual Treasury Management Strategy (ATMS), which incorporates a set of Borrowing Limits and Requirements for the year, is considered and approved before the start of each financial year.

4.2 The ATMS must also include reference to external debt levels, the Prudential Indicators as well as the Annual Investment Strategy (AIS) requirements.

4.3 The proposed **Annual Treasury Management Strategy for 2016/17**, incorporating the Annual Investment Strategy, is therefore attached as **Appendix B** to this report. The key elements of the Strategy are as follows:-

(a) an authorised limit for external debt of **£373.5m** in 2016/17;

(b) an operational boundary for external debt of **£353.5m** in 2016/17;

(c) a borrowing limit on fixed interest rate exposure of 60% to 100% of outstanding principal sums and a limit on variable interest rate exposure of 0% to 40% of outstanding principal sums;

(d) borrowing from the money market for capital purposes is to be limited to 30% of external debt outstanding at any one point in time;

(e) an investment limit on fixed interest rate exposure of 0% to 30% of outstanding principal sums and a limit on variable interest rate exposure of 70% to 100% of outstanding principal sums;

(f) a limit of £20m of the total cash sums available for investment (both in house and externally managed) to be invested in Non Specified Investments over 364 days;

(g) a 10% cap on Capital Financing costs as a proportion of the annual Net Revenue Budget;

(h) a Minimum Revenue Provision (MRP) policy for debt repayment to be charged to the Revenue Budget in 2016/17 as set out in **Section 11** of **Appendix B**;

(i) the Corporate Director – Strategic Resources to report to the Council if and when necessary during the year on any changes to this Strategy arising from the use of operational leasing, PFI or other innovative methods of funding not previously approved by the Council.

**Long Term Debt Position**

4.4 In **Section 10 of Appendix B**, reference is made to the long term debt position of the Council and the attempts being made to reduce the consequential interest charge impact on the annual Revenue Budget.

4.5 As previously reported to Members the long term debt position of the Council is essentially related to the level of capital expenditure undertaken. The growth of the Council's long term outstanding debt is demonstrated by the following table:-

| @ Year End | Debt Outstanding (A) | Year on Year Variation | |
|---|---|---|---|
| | **£m** | **£m** | |
| 31 March 2001 actual | 147.3 | | |
| 2002 actual | 148.9 | + 1.6 | |
| 2003 actual | 180.2 | + 31.3 | |
| 2004 actual | 215.1 | + 34.9 | |
| 2005 actual | 231.7 | + 16.6 | |
| 2006 actual | 274.4 | + 42.7 | |
| 2007 actual | 299.0 | + 24.6 | |
| 2008 actual | 328.2 | + 29.2 | |
| 2009 actual | 329.7 | + 1.5 (B) | |
| 2010 actual | 323.9 | - 5.8 (B) | |
| 2011 actual | 390.1 | + 77.6 (B) | |
| 2012 actual | 376.8 | - 13.3 (C) | |
| 2013 actual | 350.0 | - 26.8 (C) | |
| 2014 actual | 344.6 | - 5.4 (C) | |
| 2015 actual | 319.8 | - 24.8 (C) | |
| 2016 forecast | 326.0 | + 6.2 | see **paragraphs 4.6 to 4.10** |
| 2017 forecast | 320.6 | - 5.4 | |
| 2018 forecast | 311.1 | - 9.5 | |
| 2019 forecast | 302.0 | - 9.1 | |

(A) Excludes other long term liabilities such as PFI contracts and finance leases which are regarded as debt outstanding for Prudential Indicator purposes.

(B) Reflects the impact of premature repayment of external debt in 2008/09 and 2009/10 and its subsequent refinancing in 2009/10 and 2010/11, together with the capital borrowing requirement for 2009/10 being rolled forward into 2010/11.

(C) Reflects the current policy of internally financing capital expenditure from cash balances which, at some stage, will have to be reversed.

4.6 The debt outstanding forecasts for 31 March 2016 and subsequent years in the table at **paragraph 4.5** above and the Prudential Indicators relating to external debt are based on an assumption that the annual capital borrowing requirements for the years 2015/16 to 2018/19 being taken externally each year. As explained in **paragraphs 6.9 and 8.5 to 8.13** of **Appendix B**, consideration will be given however to delaying external borrowing throughout this period and funding annual borrowing requirements from revenue cash balances (i.e. running down investments). This has the potential for achieving short term revenue savings and also has the benefit of reducing investment exposure to credit risk.

4.7 Furthermore a key point in relation to debt levels is a proposal in the Revenue Budget report on today's agenda to set aside £10m in the revenue budget for debt repayment / capital financing purposes. Because of the timing and the preferred approach within the available options is not yet finalised, the impact of this is not reflected in any of the debt projections in this report and its appendices. This also applies to the various Prudential Indicators covered in **Section 3 of Appendix B** and the separate Prudential Indicators report. If implemented however the expected impact would be to reduce capital debt levels (internal and external) by £10m which would achieve recurring revenue savings in capital financing charges (repayment of principal) in subsequent years.

4.8 The above table shows the Council's external debt increased by 234% between 2001 and 2013. The increase in the years since 2002 to 2011 is particularly noticeable – this is primarily attributable to the increase in the value of annual Highways LTP allocations and the availability of Prudential Borrowing which has been deliberately used by the Council to boost capital spending and thereby invest in its asset infrastructure. The ratio of borrowing related to government borrowing approvals as opposed to being locally determined under the prudential regime has been approximately 80/20 in the period up to 31 March 2011.

4.9 A significant feature of the 2011/12 Local Government Finance Settlement, however, was that all Government capital approvals from 2011/12 were funded from capital grants rather than the previous mix of grants and borrowing approvals. This reduces annual capital borrowing and debt levels by about £33m per annum with a consequential impact on capital financing costs. The impact of this is reflected in the table in **paragraph 4.5** with forecast debt outstanding levels after 31 March 2011 starting to reduce year on year.

4.10 The change referred to in **paragraph 4.9** above has had significant implications on the future Treasury Management operations and consequential Prudential Indicators in terms of

- reduced annual borrowing requirement and consequential debt levels from 2011/12 as indicated in the table in **paragraph 4.5**
- the potential for the annual Minimum Revenue Provision (MRP) for debt repayment exceeding the actual new borrowing requirement in the year resulting in a net debt repayment required with potential early repayment penalties (premiums)
- reduced capital financing costs (interest + MRP) which were built into the 2011/12 Revenue Budget/MTFS
- significant impact on many Prudential Indicators

4.11 After reflecting the factors referred to in **paragraphs 4.9 and 4.10** above, the revenue cost of servicing the debt which impacts directly on the Revenue Budget / Medium Term Financial Strategy will be about £26.6m in 2016/17; this consists of interest payments of £13.7m and a revenue provision for debt repayment of £13.9m.

4.12 As shown in the table at **paragraph 4.5** and explained subsequently in **paragraphs 4.9** and **4.10**, the debt outstanding levels of the Council based on the current Capital Plan, start to reduce each year from 2011/12. This assumes that the Government continues to fund future capital approvals through grants rather than the previous mix of grant and supported borrowing approvals. These debt levels could be reduced further by

(a) curtailing fresh capital investment and removing/reducing Capital Plan provisions that remain funded from external prudential borrowing;

(b) significantly increasing the Revenue Budget/MTFS provision for debt repayment above the agreed Prudential policy (about 4% of debt) that is currently made;

(c) removing Capital Plan schemes funded by capital receipts and using those receipts, together with future additional receipts and the current corporate capital pot, for debt repayment, rather than new capital investment;

(d) funding total annual borrowing requirements from internal cash balances and thus running down investments. This internal capital financing option is referred to in more detail in **paragraph 4.6** above and **paragraphs 6.9 and 8.5 to 8.13** of **Appendix B**;

(e) following (d) above, external debt could also be prematurely repaid from internal cash balances and thus also running down investments.

**Age profile of the external debt**

4.13 The age profile of the Council's external debt as at 31 March 2015 is as follows:-

| Length of Period | £m |
|---|---|
| up to 1 year | 8.2 |
| 1 year to 2 years | 7.6 |
| 2 years to 5 years | 60.9 |
| 5 years to 10 years | 54.6 |
| 10 to 25 years | 34.7 |
| 25 to 40 years | 131.3 |
| above 40 years | 22.5 |
| **Total external debt at 31 March 2015** | **319.8** |

4.14 Some points to highlight in relation to the above table are as follows

(a) there is no predetermined or model age profile and decisions to borrow have been taken each year in the light of current and forecast future interest rates together with the yield curve;

(b) new borrowing in recent years has focused on longer period fixed term loans due to their historically low interest rates;

(c) a period spread of the age profile is important to avoid having to refinance loans repaid within relatively short periods;

(d) the 2016/17 Borrowing Strategy set out in **Section 8 of Appendix B** will mean that the Council should be able (in current and forecast market conditions) to undertake cost effective borrowing over markedly shorter periods than in previous years and so achieve a more even spread of the debt maturity profile. This is subject, of course, to the potential impact of delaying annual borrowing requirements to later years by utilising cash balances and running down investments. As covered elsewhere in this report, however, future new borrowing levels are significantly lower than in previous years (see **paragraphs 4.9 and 4.10**).

## 5.0 CREDIT RATING CRITERIA AND APPROVED LENDING LIST

5.1 The criteria for monitoring and assessing organisations (counterparties) to which the Council may make investments (i.e. lend) are incorporated into the detailed Treasury Management Practices (TMPs) that support the Treasury Management Policy Statement (TMPS). Applying these criteria enables the Council to produce an Approved Lending List of organisations in which it can make investments, together with specifying the maximum sum that at any time can be placed with each. The Approved Lending List is prepared, taking into account the advice of the Council's Treasury Management Advisor, Capita Asset Services – Treasury Solutions. **(See paragraph 13 of Appendix B).**

### Changes to Credit Methodology

5.2 Since the financial crisis, the main rating agencies (Fitch, Moody's and Standard & Poor's) have included an assumption, when assessing credit worthiness, that an institution would obtain support from Government should the institution fail, (i.e. implied levels of sovereign support).

5.3 Commencing in 2015, in response to the evolving regulatory regime, all three agencies have begun removing these implied "uplifts" in credit quality. The process has been part of a wider reassessment of methodologies by each of the rating agencies. In addition to the removal of implied support, new methodologies are now taking into account additional factors. In some cases, these factors have "netted" each other off, to leave underlying ratings either unchanged or little changed.
It is important to stress that the rating agency changes do not reflect any changes in the underlying status of the institution or credit environment; they are merely reflective of a reassessment of rating agency methodologies in light of changes to the regulatory environment.

5.4 As a result of these rating agency changes, the credit element of the creditworthiness methodology will focus solely on the Short and Long Term ratings of an institution. Rating Watch and Outlook information will continue to be assessed and the overlay of CDS (Credit Default Swap) prices will continue to be used.

**Lending criteria for 2016/17**

5.5 In order to minimise the risk to investments, the Council will continue to apply a minimum acceptable credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk. This approach has reflected the following:-

(a) a system of scoring each organisation using Capita's enhanced creditworthiness service. This service, revised during 2015/16 to reflect continuing regulatory changes, uses a sophisticated modelling system that includes:

- credit ratings published by the three credit rating agencies (Fitch, Moodys and Standard and Poor) which reflect a combination of components (long term and short term,)
- credit watches and credit outlooks from the rating agencies
- credit Default Swaps (CDS) spreads to give early warnings of likely changes in credit ratings
- other information sources, including, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

(b) sole reliance is not placed on the information provided by Capita. In addition the Council also uses market data and information available from other sources such as the financial press and other agencies and organisations

(c) in addition to the above, the following measures also continue to be actively taken into consideration:

- institutions will be removed or temporarily suspended from the Approved Lending List if there is significant concern about their financial standing or stability
- investment exposure will be concentrated with higher rated institutions wherever possible.

5.6 By collating and reviewing on an ongoing basis the above data, the Council aims to ensure that the most up-to-date information is used to assist in the assessment of credit quality and is seen as a practical response to the continuing money market instability and volatility.

5.7 It is, therefore, proposed that the lending criteria, as summarised in **paragraph 5.2** above, be utilised for 2016/17. These criteria are set out in full in **paragraph 12.8** of the Annual Treasury Management and Investment Strategy 2016/17 (**Appendix B**) attached and will enable the Council to continue to monitor and control its money market risk exposure whilst also ensuring that it can achieve a return that is consistent with market rates.

**Debt Management Office Deposit Account**

5.8 The Debt Management Office (DMO) Deposit Account is an investment facility introduced several years ago by the Government specifically for public authorities. This facility is AAA rated as it is part of the HM Treasury Operations and can be regarded as lending to the Government. It is, therefore, a 100% safe house lending option. Its standard interest rate however of 0.25% is below what could realistically be achieved elsewhere for similar short term investments.

5.9 This investment option is included in the Council's current approved lending list with a maximum investment limit of £100m. The facility was not utilised in 2014/15 and no investments are anticipated in 2015/16. However, The DMO account will remain on the Council's approved Lending List as a precaution.

**Approved Lending List**

5.10 The current Approved Lending List is attached to this report as **Schedule C** to the Annual Treasury Management and Investment Strategy 2016/17 (**Appendix B**). The List, however, continues to be monitored on an ongoing basis and changes made as appropriate by the Corporate Director – Strategic Resources to reflect credit rating downgrades/upgrades, mergers or market intelligence and rumours that impact on the credit 'score' and colour coding as described in **paragraph 5.8** below.

5.11 As mentioned in **paragraph 5.2 (a)** the Council evaluates an organisation's credit standing by using Capita's credit worthiness service. This service uses credit ratings and credit watch/outlook notices from all three principal market agencies overlaid by trends within the Credit Default Swap (CDS) market. All this information is then converted into a weighted credit score for each organisation and only those organisations with an appropriate score will fulfil the Council's minimum credit criteria. The score is then converted into the end product of a colour code which is used to determine the maximum investment term for an organisation. Details of this assessment criteria is included in the Annual Treasury Management and Investment Strategy 2016/17 (**paragraphs 12.8 (c) of Appendix B**).

5.12 Utilising the assessment of credit quality, the criteria and investment limits for **specified investments** (a maximum of 364 days) are:

- institutions which are partially owned by the UK Government, (Nationalised Banks), being limited to £85m
- other institutions achieving suitable credit scores and colour banding being limited to a maximum investment limit of between £20m and £75m (actual duration and investment limit dependant on final score/colour)
- all foreign bank transactions are in sterling and are undertaken with UK based offices

5.13 The criteria f**or Non Specified Investments** (for periods of more than 364 days) are:

- investments over 1 year to a maximum of 2 years with institutions which have suitable credit score

- the maximum amount for all non-specified investments is £5m with any one institution

5.14 Local Authorities will continue to be included on the Approved Lending List for 2016/17, although suitable investment opportunities with them are limited. Because of the way they are financed and their governance arrangements, Local Authorities are classed as having the highest credit rating.

5.15 The information below details all the changes reflected in the latest Approved Lending List (**Schedule C to Appendix B**) compared with that submitted for 2015/16 in February 2015. Please note that the analysis below is between the version provided last year and the proposed list for 2016/17 – it is a snapshot at a point in time. It is therefore possible that there will be in year changes that are not identified in this snapshot.

(a) organisations included on the Approved Lending List which will NOT be included for 2016/17

| **Organisation** | **Reason** |
|---|---|
| Ulster Bank Ltd | Due to fall in Credit Ratings |

(b) organisations who continue to be included on the 2016/17 Approved Lending List, but whose Maximum Investment Duration will remain as nil until Credit Ratings and market sentiment improve

| **Organisation** | **Reason** |
|---|---|
| Clydesdale Bank (Trading as the Yorkshire Bank) | Due to fall in Credit Ratings |

(c) further changes were made during the year to increase and decrease the maximum investment term for some organisations. This was the result of market movements between the Credit Default Swap and iTraxx benchmark, an early warning of likely changes to credit ratings in the future;

**Further Options**

5.16 Because of the stringent credit rating criteria being adopted (**paragraph 5.2**), there are relatively few organisations remaining on the Council's Approved Lending List (**Schedule C to Appendix B**). The impact of future downgradings, mergers and other market intelligence could, therefore, reduce the list even further and present operational difficulties in placing investments. Under these circumstances, options that could be considered at some point in the future are as follows:-

(a) continue to run down investments through taking no new borrowing (**paragraphs 8.5 to 8.13 of Appendix B**);

(b) running down investments through repaying existing debt prematurely subject to debt repayment premium constraints (**paragraphs 10.4 and 10.5 of Appendix B**);

(c) considering the addition to the Approved Lending List of further high quality, highly rated foreign banks;

(d) increasing the lending limits again for those high quality UK banks remaining on the Approved Lending List;

(e) using the Government's DMO account (**paragraphs 5.5 to 5.8**),'Triple A' rated Money Market funds or other potentially available mechanisms such as Certificates of Deposit (CD's);

(f) actively looking to invest with other local authorities although demand is very spasmodic and interest rates being offered are relatively poor;

## 6.0 REVIEW BY AUDIT COMMITTEE

6.1 In its scrutiny role of the Council's Treasury Management policies, strategies and day to day activities, the Audit Committee receives regular Treasury Management reports. These reports provide Audit Committee Members with details of the latest Treasury Management developments, both at a local and national level and enable them to review Treasury Management arrangements and consider whether they wish to make any recommendations to the Executive.

6.2 As the Council is required to approve an up to date Annual Treasury Management and Investment Strategy before the start of the new financial year, it is therefore not realistic for the Audit Committee to review this document in advance of its submission to Executive and the subsequent consideration by Council on 17 February 2016.

6.3 As in recent years it is therefore proposed that the Treasury Management Policy Statement (**Appendix A**) and updated Annual Treasury Management and Investment Strategy for 2016/17 (**Appendix B**) is submitted for review by the Audit Committee on 3 March 2016. Any resulting proposals for change would then be considered at a subsequent meeting of the Executive. If any such proposals were accepted and required a change to the (by then) recently approved Strategy document the Executive would submit a revised document to the Council at its meeting on 18 May 2016.

## 7.0 ARRANGEMENTS FOR MONITORING / REPORTING TO MEMBERS

7.1 Taking into account the matters referred to in this report, the monitoring and reporting arrangements in place relating to Treasury Management activities are now as follows:

(a) an annual (i.e. this) report to Executive and Council as part of the Budget process that sets out the Council's **Treasury Management Strategy and Policy** for the forthcoming financial year;

(b) an annual report to Executive and Council as part of the Budget process that sets the various **Prudential Indicators**, together with a mid year update of these indicators as part of the Q1 Performance Monitoring report submitted to the Executive (see **(d)** below);

(c) **annual outturn reports** to the Executive for both Treasury Management and Prudential Indicators setting out full details of activities and performance during the preceding financial year;

(d) a quarterly report on Treasury Management matters to Executive as part of the **Quarterly Performance and Budget Monitoring** report;

(e) **periodic meetings** between the Corporate Director – Strategic Resources, the Corporate Affairs portfolio holder and the Chairman of the Audit Committee to discuss issues arising from the day to day management of Treasury Management activities;

(f) reports on proposed changes to the Council's Treasury Management activities are submitted as required to the **Audit Committee** for consideration and comment; this is in addition to the arrangements referred to in **Section 6**.

## 8.0 RECOMMENDATIONS

8.1 That the Executive recommend to the Council that:

(a) the Treasury Management Policy Statement as attached as **Appendix A**;

(b) the Annual Treasury Management and Investment Strategy for 2016/17 as detailed in **Appendix B** and in particular;

(i) an authorised limit for external debt of £373.3m in 2016/17;

(ii) an operational boundary for external debt of £353.3m in 2016/17;

(iii) a borrowing limit on fixed interest rate exposure of 60% to 100% of outstanding principal sums and a limit on variable interest rate exposure of 0% to 40% of outstanding principal sums;

(iv) borrowing from the money market for capital purposes is to be limited to 30% of external debt outstanding at any one point in time;

(v) an investment limit on fixed interest rate exposure of 0% to 30% of outstanding principal sums and a limit on variable interest rate exposure of 70% to 100% of outstanding principal sums;

(vi) a limit of £20m of the total cash sums available for investment (both in house and externally managed) to be invested in Non Specified Investments over 364 days;

(vii) a 10% cap on capital financing costs as a proportion of the annual Net Revenue Budget;

(viii) a Minimum Revenue Provision (MRP) policy for debt repayment to be charged to Revenue in 2016/17 as set out in **Section 11** of **Appendix B**;

(ix) the Corporate Director – Strategic Resources to report to the Council if and when necessary during the year on any changes to this Strategy arising from the use of operational leasing, PFI or other innovative methods of funding not previously approved by the Council;

(c) that the Audit Committee be invited to review **Appendices A and B** referred to in (a) and (b) above and submit any proposals to the Executive for consideration at the earliest opportunity.

GARY FIELDING
Corporate Director – Strategic Resources

Central Services, County Hall, Northallerton
19 January 2016

**Background Documents**

CIPFA Code of Practice on Treasury Management in the Public Sector

CIPFA The Prudential Code for Capital Finance in Local Authorities

CLG Guidance on Local Government Investments

CLG Guidance on Minimum Revenue Provision

Contact: Karen Iveson (01609) 535664

**APPENDIX A**

**NORTH YORKSHIRE COUNTY COUNCIL**

**TREASURY MANAGEMENT POLICY STATEMENT**

## 1.0 BACKGROUND

1.1 The Council has adopted the **CIPFA Code of Practice on Treasury Management in the Public Services** as updated in 2011. This Code sets out a framework of operating procedures to reduce treasury risk and improve understanding and accountability regarding the Treasury position of the Council.

1.2 The CIPFA Code of Practice on Treasury Management requires the Council to adopt the following four clauses of intent:

(a) the Council will create and maintain as the cornerstone for effective Treasury Management

(i) a strategic **Treasury Management Policy Statement** (TMPS) stating the policies, objectives and approach to risk management of the Council to its treasury management activities;

(ii) a framework of suitable **Treasury Management Practices** (TMPs) setting out the manner in which the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities. The Code recommends 12 TMPs;

(b) the Council (full Council and/or Executive) will receive reports on its Treasury Management policies, practices and activities including, as a minimum, an annual strategy and plan in advance of the year, a mid year review and an annual report after its close, in the form prescribed in the TMPs;

(c) the Council delegates responsibility for the implementation and regular monitoring of its Treasury Management policies and practices to the Executive and for the execution and administration of Treasury Management decisions to the Corporate Director – Strategic Resources who will act in accordance with the Council's TMPS, TMPs, as well as CIPFA's Standard of Professional Practice on Treasury Management;

(d) the Council nominates the Audit Committee to be responsible for ensuring effective scrutiny of the Treasury Management Strategies and Policies.

1.3 The **CIPFA Prudential Code for Capital Finance in Local Authorities** (updated in 2011) and the terms of the **Local Government Act 2003**, together with 'statutory' Government Guidance, establish further requirements in relation to treasury management matters, namely

(a) the approval, on an annual basis, of a set of **Prudential Indicators**;

(b) the approval, on an annual basis, of an **Annual Treasury Management Strategy**, an **Annual Investment Strategy**, and an annual **Minimum Revenue Provision (MRP)** policy statement with an associated requirement that each is monitored on a regular basis with a provision to report as necessary both in-year and at the financial year end.

1.4 This current Treasury Management Policy Statement (TMPS) was approved by Council on 17 February 2016.

## 2.0 TREASURY MANAGEMENT POLICY STATEMENT (TMPS)

2.1 Based on the requirements detailed in **paragraph 1.2 (a) (i)** above a TMPS stating the policies and objectives of the treasury management activities of the Council is set out below.

2.2 The Council defines the policies and objectives of the treasury management activities of the Council as follows:-

(a) 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;

(b) the identification, monitoring and control of risk will be the prime criteria by which the effectiveness of the treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council and any financial instrument entered into to manage these risks;

(c) effective treasury management will provide support towards the achievement of the business and service objectives of the Council as expressed in the Council Plan. The Council is committed to the principles of achieving value for many in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

2.3 As emphasised in the Treasury Management Code of Practice, responsibility for risk management and control of Treasury Management activities lies wholly with the Council and all officers involved in Treasury Management activities are explicitly required to follow Treasury Management policies and procedures.

## 3.0 TREASURY MANAGEMENT PRACTICES (TMPs)

3.1 As referred to in **paragraph 1.2 (a) (ii)** above the CIPFA Code of Practice on Treasury Management requires a framework of Treasury Management Practices (TMPs) which:

(a) set out the manner in which the Council will seek to achieve the policies and objectives set out in **paragraph 2.2** above; and

(b) prescribe how the Council will manage and control those activities;

3.2 The CIPFA Code of Practice recommends 12 TMPs. These were originally approved by Members in March 2004 and have recently been updated in the light of the new Codes from CIPFA and Statutory Guidance from the Government. These updated documents were approved by the Audit Committee on 6 December 2012.

3.3 A list of the 12 TMPs is as follows:-

| | |
|---|---|
| TMP 1 | Risk management |
| TMP 2 | Performance measurement |
| TMP 3 | Decision-making and analysis |
| TMP 4 | Approved instruments, methods and techniques |
| TMP 5 | Organisation, clarity and segregation of responsibilities, and dealing arrangements |
| TMP 6 | Reporting requirements and management information arrangements |
| TMP 7 | Budgeting, accounting and audit arrangements |
| TMP 8 | Cash and cash flow management |
| TMP 9 | Money Laundering |
| TMP 10 | Training and qualifications |
| TMP 11 | Use of external service providers |
| TMP 12 | Corporate governance |

## 4.0 PRUDENTIAL INDICATORS

4.1 The Local Government Act 2003 underpins the Capital Finance system introduced on 1 April 2004 and requires the Council to "have regard to" the **CIPFA Prudential Code for Capital Finance in Local Authorities**. This Code which was last updated in November 2011, requires the Council to set a range of Prudential Indicators for the next three years

(a) as part of the annual Budget process, and;

(b) before the start of the financial year;

to ensure that capital spending plans are affordable, prudent and sustainable.

4.2 The Prudential Code also requires appropriate arrangements to be in place for the monitoring, reporting and revision of Prudential Indicators previously set.

4.3 The required Prudential Indicators are as follows

- estimated ratio of capital financing costs to the Net Revenue Budget
- estimates of the incremental impact of capital investment decisions on the Council Tax
- Capital Expenditure - Actual and Forecasts
- Capital Financing Requirement
- Gross Debt and the Capital Financing Requirement

- authorised Limit for External Debt

  operational Boundary for External Debt
- Actual External Debt
- Adoption of the CIPFA Code of Practice for Treasury Management
- Interest Rate Exposures
- Maturity Structure of Borrowing
- Total Principal Sums Invested for periods longer than 364 days

4.4 The Council will approve the Prudential Indicators for a three year period alongside the annual Revenue Budget/Medium Term Financial Strategy at its February meeting each year. The Indicators will be monitored during the year and necessary revisions submitted as necessary via the Quarterly Performance and Budget Monitoring reports.

4.5 In addition to the above formally required Prudential Indicators, the Council has also set two local ones as follows:

(a) to cap Capital Financing costs to 10% (11% up to 2013/14) of the net annual revenue budget; and

(b) a 30% limit on money market borrowing as opposed to borrowing from the Public Works Loan Board.

## 5.0 ANNUAL TREASURY MANAGEMENT AND INVESTMENT STRATEGY

5.1 A further implication of the Local Government Act 2003 is the requirement for the Council to set out its Treasury Management Strategy for borrowing and to approve an Annual Investment Strategy (which sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments).

5.2 The Government's guidance on the Annual Investment Strategy, updated in 2009, states that authorities can combine the Treasury Management Strategy Statement and Annual Investment Strategy into one report. The Council has adopted this combined approach.

5.3 Further statutory Government guidance, last updated with effect from April 2012, is in relation to an authority's charge to its Revenue Budget each year for debt repayment. A Minimum Revenue Provision (MRP) policy statement must be prepared each year and submitted to the full Council for approval before the start of the financial year.

5.4 The Council's Annual Treasury Management and Investment Strategy will therefore cover the following matters:

- treasury limits in force which will limit the treasury risk and activities of the Council
- Prudential and Treasury Indicators
- the current treasury position

- the Borrowing Requirement and Borrowing Limits
- borrowing Policy
- prospects for interest rates
- borrowing Strategy
- capping of capital financing costs
- review of long term debt and debt rescheduling
- minimum revenue provision policy
- annual investment strategy
- other treasury management issues
- arrangements for monitoring / reporting to Members

5.5 The Council will approve this combined Annual Strategy alongside the annual Revenue Budget/Medium Term Financial Strategy at its February meeting each year.

## 6.0 REVIEW OF THIS POLICY STATEMENT

6.1 Under Financial Procedure Rule 14, the Corporate Director – Strategic Resources is required to periodically review this Policy Statement and all associated documentation. A review of this Statement, together with the associated annual strategies, will therefore be undertaken annually as part of the Revenue Budget process, together with a mid year review as part of the Quarterly Treasury Management reporting process and at such other times during the financial year as considered necessary by the Corporate Director – Strategic Resources.

Approved by County Council February 2016

**APPENDIX B**

**NORTH YORKSHIRE COUNTY COUNCIL**

**ANNUAL TREASURY MANAGEMENT AND INVESTMENT STRATEGY 2016/17**

## 1.0 INTRODUCTION

1.1 Treasury Management is defined 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".

1.2 The Local Government Act 2003, and supporting regulations, require the Council to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

1.3 The Act also requires the Council to set out its **Annual Treasury Management Strategy** for borrowing and to prepare an **Annual Investment Strategy** (as required by Investment Guidance issued subsequent to the Act) which sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments. For practical purposes these two strategies are combined in this document.

1.4 This Strategy document for 2016/17 therefore covers the following

- treasury limits in force which will limit the treasury risk and activities of the Council (**Section 2**)
- Prudential indicators (**Section 3**)
- current treasury position (**Section 4**)
- borrowing requirement and borrowing limits (**Section 5**)
- borrowing policy (**Section 6**)
- prospects for interest rates (**Section 7**)
- borrowing strategy (**Section 8**)
- capping of capital financing costs (**Section 9**)
- review of long term debt and debt rescheduling (**Section 10**)
- minimum revenue provision policy (**Section 11**)
- annual investment strategy (**Section 12**)
- other treasury management issues (**Section 13**)
- arrangements for monitoring/reporting to Members (**Section 14**)
- summary of key elements of this strategy (**Section 15**)

- specified investments (**Schedule A**)
- non-specified investments (**Schedule B**)
- approved lending list (**Schedule C**)
- approved countries for investments (**Schedule D**)

1.5 It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced Annual Revenue Budget. In particular, Section 32 requires a local authority to calculate its Budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby additional charges to the Revenue Budget arising from:-

(a) increases in interest and principal charges caused by increased borrowing to finance additional capital expenditure, and/or;

(b) any increases in running costs from new capital projects

are affordable within the projected revenue income of the Council for the foreseeable future.

1.6 These issues are addressed and the necessary assurances provided by the Section 151 officer (the Corporate Director – Strategic Resources) in the 2016/17 Revenue Budget and Medium Term Financial Strategy report considered separately by the Executive on 2 February 2016 and approved by the Council on 17 February 2016.

1.7 This Strategy document was approved by the Council on 17 February 2016.

## 2.0 TREASURY LIMITS FOR 2016/17 TO 2018/19

2.1 It is a statutory duty under Section 3 of the Local Government Act 2003 and supporting regulations for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the **Affordable Borrowing Limit**.

2.2 The Council must have regard to the Prudential Code when setting the Affordable Borrowing Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon future Council Tax levels is acceptable. In practice, it is equivalent to the Authorised Limit as defined for the Prudential Indicators (therefore see **Section 3** below).

2.3 Whilst termed an Affordable Borrowing Limit, the spending plans to be considered for inclusion incorporate financing by both external borrowing and other forms of liability such as credit arrangements. The Affordable Borrowing Limit has to be set on a rolling basis for the forthcoming financial year and two successive financial years.

## 3.0 PRUDENTIAL INDICATORS FOR 2016/17 TO 2018/19

3.1 A separate Report incorporating an updated set of Prudential Indicators for the three year period to 31 March 2019, as required by the CIPFA Prudential Code for Capital Finance in Local Authorities, was also approved by the Council on 17 February 2016.

3.2 These Prudential Indicators include a number relating to external debt and treasury management that are appropriately incorporated into this Annual Treasury Management Strategy for 2016/17.

3.3 Full details of the Prudential Indicators listed below are contained in the separate **Revision of Prudential Indicators** report referred to in **paragraph 3.1** above.

3.4 The following Prudential Indicators are relevant for the purposes of setting an integrated Annual Treasury Management Strategy.

(a) **Estimated ratio of capital financing costs to the Net Revenue Budget**

(i) formally required indicator net of interest earned

| | |
|---|---|
| 2014/15 actual | 7.5% |
| 2015/16 probable | 7.5% |
| 2016/17 estimate | 7.1% |
| 2017/18 estimate | 6.7% |
| 2018/19 estimate | 6.1% |

(ii) Local Indicator capping capital financing costs to 10% of the annual Net Revenue Budget

| | |
|---|---|
| 2014/15 actual | 7.9% |
| 2015/16 probable | 7.8% |
| 2016/17 estimate | 7.8% |
| 2017/18 estimate | 7.7% |
| 2018/19 estimate | 7.4% |

(b) **Estimates of the incremental impact of capital investment decisions on the Council Tax requirement**

| For a Band D Council Tax | |
|---|---|
| | **£ p** |
| 2016/17 estimate | 0.80 |
| 2017/18 estimate | 1.67 |
| 2018/19 estimate | 2.11 |

(c) **Capital Expenditure - Actual and Forecasts**

| | £m |
|---|---|
| 2014/15 actual | 106.6 |
| 2015/16 probable | 112.3 |
| 2016/17 estimate | 93.6 |
| 2017/18 estimate | 87.7 |
| 2018/19 estimate | 79.3 |

(d) **Capital Financing Requirement (as at 31 March)**

| | Borrowing £m | Other Long Term Liabilities £m | Total £m |
|---|---|---|---|
| 31 March 2015 actual | 361.1 | 5.8 | 366.9 |
| 31 March 2016 probable | 346.2 | 5.5 | 351.7 |
| 31 March 2017 estimate | 336.7 | 5.3 | 342.0 |
| 31 March 2018 estimate | 326.8 | 5.1 | 331.9 |
| 31 March 2019 estimate | 316.9 | 4.7 | 321.9 |

(e) **Gross Debt and the Capital Financing Requirement**

In order to ensure that over the medium term debt will only be for Capital purposes, the Council should ensure that debt does not, except in the short term, exceed the total of the Capital Financing Requirement in the preceding year, plus the estimate of any additional capital financing requirement for 2016/17 and the next two financial years.

The Corporate Director – Strategic Resources confirms that the Council had no difficulty in meeting this requirement up to 2014/15 nor are any difficulties envisaged for the current or future financial years covered by this PI update to 2018/19. For subsequent years, however, there is the potential that the Council may not be able to comply with this requirement as a result of the potential for the annual Minimum Revenue Provision (MRP) reducing the Capital Financing Requirement below gross debt. This potential situation will be monitored closely.

(f) **Authorised Limit for external debt**

| | External Borrowing £m | Other Long Term Liabilities £m | Total Borrowing Limit £m |
|---|---|---|---|
| 2015/16 | 369.2 | 5.5 | 374.7 |
| 2016/17 | 368.2 | 5.3 | 373.5 |
| 2017/18 | 382.5 | 5.1 | 387.6 |
| 2018/19 | 344.5 | 4.7 | 349.2 |

(g) **Operational Boundary for external debt**

| | External Borrowing £m | Other Long Term Liabilities £m | Total Borrowing £m |
|---|---|---|---|
| 2015/16 | 349.2 | 5.5 | 354.7 |
| 2016/17 | 348.2 | 5.3 | 353.5 |
| 2017/18 | 362.5 | 5.1 | 367.6 |
| 2018/19 | 324.5 | 4.7 | 329.2 |

(h) **Actual External Debt**

| | Borrowing £m | Other Long Term Liabilities £m | Total £m |
|---|---|---|---|
| at 31 March 2015 actual | 319.8 | 5.8 | 325.6 |
| at 31 March 2016 probable | 326.0 | 5.5 | 331.5 |
| at 31 March 2017 estimate | 320.6 | 5.3 | 325.9 |
| at 31 March 2018 estimate | 311.1 | 5.1 | 316.2 |
| at 31 March 2019 estimate | 302.0 | 4.7 | 306.7 |

(i) **Limit of Money Market Loans** (Local Indicator)

Borrowing from the money market for capital purposes is to be limited to 30% of the Council's total external debt outstanding at any one point in time.

(j) **Adoption of CIPFA Code of Practice for Treasury Management in the Public Services**

The Council agreed to adopt the latest updated Code issued in November 2011 on 15 February 2012.

(k) **Interest Rate exposures**

| **Borrowing** | **%age of outstanding principal sums** |
|---|---|
| Limits on fixed interest rate exposures | 60 to 100 |
| Limits on variable interest rate exposures | 0 to 40 |
| **Investing** | |
| Limits on fixed interest rate exposures | 0 to 30 |
| Limits on variable interest rate exposures | 70 to 100 |
| **Combined net borrowing/investment position** | |
| Limits on fixed interest rate exposures | 160 to 210 |
| Limits on variable interest rate exposures | -60 to -110 |

(l) **Maturity Structure of borrowing**

The amount of projected borrowing maturing in each period as a percentage of total projected borrowing that is fixed rate.

| | Lower Limit % | Upper Limit % |
|---|---|---|
| under 12 months | 0 | 50 |
| 12 months and within 24 months | 0 | 15 |
| 24 months and within 5 years | 0 | 45 |
| 5 years and within 10 years | 0 | 75 |
| 10 years and within 25 years | 10 | 100 |
| 25 years and within 50 years | 10 | 100 |

(m) **Total principal sums invested for periods longer than 364 days**

Based on estimated levels of funds and balances over the next three years, the need for liquidity and day-to-day cash flow requirements, it is forecast that a maximum of £20m of 'core cash funds' available for investment can be held in aggregate in Non-Specified Investments over 364 days.

## 4.0 CURRENT TREASURY POSITION

4.1 The Council's treasury portfolio position at 31 March 2015 consisted of:

| Item | Principal £m | Average Rate at 31 March 2015 % |
|---|---|---|
| **Debt Outstanding** | | |
| Fixed Rate funding | | |
| PWLB | 299.8 | 4.47 |
| Variable Rate funding | | |
| Market LOBO's | 20.0 | 3.95 |
| Total Debt Outstanding | 319.8 | 4.44 |
| **Investments** | | |
| Managed in house | 215.2 | 0.65 |
| **Net Borrowing** | **104.6** | |

## 5.0 BORROWING REQUIREMENT AND BORROWING LIMITS

5.1 The Council's annual borrowing requirement consists of the capital financing requirement generated by capital expenditure in the year plus replacement borrowing for debt repaid less a prudent Minimum Revenue Provision charged to revenue for debt payment. These borrowing requirements are set out below.

| Year | Basis | £m | Comment |
|---|---|---|---|
| 2014/15 | actual | 0 | No actual external borrowing was undertaken in 2014/15. The total requirement was £32.5m (including the rolled forward requirement from previous years) which was all financed internally from cash balances. |
| 2015/16 | requirement | 9.4 | Includes £32.5m capital borrowing requirement rolled over from 2014/15 |
| 2016/17 | estimate | 2.2 | See **paragraphs 5.8 and 5.9**. The much higher figures for 2015/16 and 2018/19 include 'refinancing' significant PWLB and money market (LOBO) loan repayments in those years. |
| 2017/18 | estimate | 21.9 | |
| 2018/19 | estimate | -6.6 | |

5.2 The Prudential Indicators set out in **paragraph 3.4** above include an Authorised Limit and Operational Boundary for external debt for each of the three years to 2018/19. These figures are referenced at **paragraphs 3.4(f) and 3.4(g)** respectively of this Strategy.

5.3 The **Operational Boundary** reflects an estimate of the most likely, prudent but not worst case scenario of external debt during the course of the financial year. The **Authorised Limit** is based on the same estimate as the **Operational Boundary** but allows sufficient headroom (£20m) over this figure to allow for unusual cash movements.

5.4 The **Authorised Limit** therefore represents the maximum amount of external debt which the Council approves can be incurred at any time during the financial year and includes both capital and revenue requirements. It is not, however, expected that the Council will have to borrow up to the Limit agreed.

5.5 The agreed **Operational Boundary** and **Authorised Limits** for external debt up to 2018/19 are derived as follows:

| | **Item** | **2015/16 probable £m** | **2016/17 estimate £m** | **2017/18 estimate £m** | **2018/19 estimate £m** |
|---|---|---|---|---|---|
| | **Debt outstanding at start of year** | | | | |
| | PWLB | 299.8 | 326.0 | 320.6 | 311.1 |
| | Other Institutions | 20.0 | | | |
| **Sub-total** | | 319.8 | 326.0 | 320.6 | 311.1 |
| + | **External borrowing requirements** | | | | |
| | Capital borrowing requirement | -0.5 | 4.4 | 3.8 | 3.4 |
| | Replacement borrowing | 3.2 | 7.6 | 31.4 | 2.5 |
| | MRP charged to Revenue etc | 14.4 | -13.9 | -13.7 | -13.4 |
| | Borrowing rolled over from 2014/15 | 32.5 | - | - | - |
| | Internally funded variations | -11.4 | 4.1 | 0.4 | 0.9 |
| **Sub-total** | | 9.4 | 2.2 | 21.9 | -6.6 |
| - | **External debt repayment** | -3.2 | -7.6 | -31.4 | -2.5 |
| = | **Forecast debt outstanding at end of year** | **326.0** | **320.6** | **311.1** | **302.0** |
| + | **Other 'IFRS' long term liabilities which are regarded as debt outstanding for PIs** | | | | |
| | PFI | 4.4 | 4.2 | 4.0 | 3.6 |
| | Leases | 1.1 | 1.1 | 1.1 | 1.1 |
| = | **Total debt outstanding including 'other long term liabilities' (PI7)** | **331.5** | **325.9** | **316.2** | **306.7** |
| + | **Provision for** | | | | |
| | Debt rescheduling | 15.0 | 15.0 | 15.0 | 15.0 |
| | Potential capital receipts slippage | 5.0 | 5.0 | 5.0 | 5.0 |
| | New borrowing taking place before principal repayments made | 3.2 | 7.6 | 31.4 | 2.5 |
| = | **Operational Boundary for year (PI7)** | **354.7** | **353.5** | **367.6** | **329.2** |
| + | **Provision to cover unusual cash movements** | 20.0 | 20.0 | 20.0 | 20.0 |
| = | **Authorised Limit for year (PI6)** | **374.7** | **373.5** | **387.6** | **349.2** |

5.6 **Therefore the 2016/17 Limits are as follows:**

| | **£m** |
|---|---|
| Operational Boundary for external debt | 353.5 |
| + provision to cover unusual cash movements during the year | 20.0 |
| = Authorised Limit for 2016/17 | **373.5** |

5.7 All the debt outstanding estimates referred to in **paragraph 5.5** and the Prudential Indicators relating to external debt referred to in **paragraph 3.4** are based on annual capital borrowing requirements being taken externally and therefore increasing debt outstanding levels. As explained in **paragraphs 6.9 and 8.5 to 8.13**, consideration will be given however to delaying external borrowing throughout this period and funding annual borrowing requirements from revenue cash balances (i.e. running down investments). This likely outcome has the potential for achieving short term revenue savings and also has the benefit of reducing investment exposure to credit risk.

5.8 The annual borrowing requirements reported in the tables in **paragraphs 5.1 and 5.5** above £9.4m in 2015/16, £2.2m in 2016/17, £21.9m in 2017/18 and £6.6m repayment of internal borrowing in 2018/19) are much lower than about £50m per annum up to 2010/11. This is because the 2011/12 Local Government Finance Settlement reflected all Government Capital approvals from 2011/12 being funded from Capital Grants rather than the previous mix of grants and borrowing approvals.

5.9 This change has had significant implications on the Council's future Treasury Management operations and consequential Prudential Indicators in terms of:-

- reduced annual borrowing requirement and consequential debt levels from 2011/12 by about £33m per annum, which was the approximate total of such borrowing approvals in recent years
- the potential for the annual Minimum Revenue Provision (MRP) for debt repayment in the year resulting in a net debt repayment required with potential early repayments penalties (premiums)
- reduced capital financing costs (interest + MRP) from 2011/12
- significant impact on many Prudential Indicators (see **paragraph 3.4** above).

5.10 A key point in relation to debt levels is a proposal in the Revenue Budget report on today's agenda to set aside £10m in the revenue budget for debt repayment / capital financing purposes. Because the timing and which of the available options to be pursued have not been finalised the impact of this is not reflected in any of the debt projections in this strategy report. This also applies to the various Prudential Indicators covered in **section 3** of this strategy document and the separate Prudential Indicators report. If implemented in however the expected impact would be to reduce capital debt levels (internal and external) by £10m which would achieve recurring revenue savings in capital financing charges (repayment of principal) in subsequent years.

## 6.0 BORROWING POLICY

6.1 The policy of the Council for the financing of capital expenditure is set out in Treasury Management Practice Note 3 which supports the Treasury Management Policy Statement.

6.2 In practical terms the policy is to finance capital expenditure by borrowing from the Public Works Loan Board (for periods up to 50 years) or the money markets (for periods up to 70 years) whichever reflects the best possible value to the Council. Individual loans are taken out over varying periods depending on the perceived relative value of interest rates at the time of borrowing need and the need to avoid a distorted loan repayment profile. Individual loans are not linked to the cost of specific capital assets or their useful life span. Decisions to borrow are made in consultation with the Council's Treasury Management Advisor (Capita Asset Services – Treasury Solutions).

6.3 Access to PWLB loans since 1 April 2004 is based on the Prudential Indicators and approved 'borrowing requirements' of individual authorities. Loans from the PWLB used to be very competitive with other forms of borrowing as they reflected prices on the gilt market for Government securities. They became less competitive however after 20 October 2010 following the Chancellor announcing that the PWLB would increase the margin above the Government's cost of borrowing to an average of 1% with immediate effect. Borrowing costs from the PWLB thus rose by about 0.7% across all periods. From November 2012 there was however a new 0.2% discount on loans from the PWLB under the prudential regime for local authorities providing improved information and transparency on their locally determined long term borrowing and associated capital spending. The Council has provided this information each year and has qualified for the discount for any loans taken out up to 31 October 2016. Thereafter annual access to this discounted rate will be dependent on eligible local authorities providing the necessary information each year.

6.4 In addition to the PWLB the Council can borrow from the money market (principally banks and building societies) and this is usually effected via a LOBO (Lender Option, Borrower Option). Such loans feature an initial fixed interest period followed by a specified series of calls when the lender has the option to request an interest rate increase. The borrower then has the option of repaying the loan (at no penalty) or accepting the higher rate.

6.5 The time period for LOBO borrowing by the Council was increased to a maximum of 70 years (from 50 years) as part of the 2008/09 Strategy. In reality borrowing for 70 years is little different to taking a 50 year loan. The risk of taking such long period loans is that the Council could potentially be locked into paying current interest rates on a loan for up to 70 years which would be disadvantageous if medium/long term rates subsequently fell below current rates at some point in the future. In practice, however, it is highly unlikely that such loans would ever run the full period because if at some point interest rates rise above the fixed rate agreed, the lender would request an increase and the Council would have the option of repaying the loan.

6.6 Borrowing from the money market for capital purposes is limited to 30% of the Council's total external debt outstanding at any one point in time (per **Prudential Indicator 9**).

6.7 The Council will always look to borrow from the PWLB and money markets at the most advantageous rate. The Corporate Director – Finance and Central Services will monitor this situation closely throughout the year to determine whether at any stage, money market loans are more appropriate and advantageous to the Council than PWLB loans.

6.8 At present all Council long term borrowing is from the PWLB or via equally advantageous money market loans. However some short term money market borrowing may take place during the financial year in order to take advantage of low interest rates or to facilitate any debt restructuring exercise (see **paragraph 10** below).

6.9 Depending on the relationship between short term variable interest rates and the fixed term PWLB or LOBO rates for longer periods, some capital expenditure may be financed by short term borrowing from either the Council's revenue cash balances or outside sources (see **paragraphs 8.5 to 8.13**).

**Policy on borrowing in advance of need**

6.10 The Prudential Code allows external 'borrowing for capital purposes' in advance of need within the constraints of relevant approved Prudential Indicators. Thus taking estimated capital borrowing requirements up to 31 March 2019 any time after 1 April 2016 is allowable under the Prudential Code. There are risks, however, in such borrowing in advance of need and the Council has not taken any such borrowing to date and there are no current plans to do so. Furthermore the Council will not borrow more than, or in advance of, its needs purely in order to profit from the investment of the extra sums borrowed.

6.11 Any decision to borrow in advance of need will only be considered where there is

- a clear business case for doing so for the current Capital Plan
- to finance future debt maturity repayments
- value for money can be demonstrated
- the Council can ensure the security of such funds which are subsequently invested

6.12 Thus in any future consideration of whether borrowing will be undertaken in advance of need the Council will:

- ensure that there is a clear link between the Capital Plan and maturity of the existing debt portfolio which supports the need to take funding in advance of need
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow
- consider the merits and demerits of alternative forms of funding
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use.
- consider the impact of borrowing in advance (until required to finance capital expenditure) on temporarily increasing investment cash balances and the consequent increase in exposure to counter party risk and other risks, and the level of such risks given the controls in place to minimise them.

## 7.0 PROSPECTS FOR INTEREST RATES

7.1 Whilst recognising the continuing volatility and turbulence in the financial markets, the following paragraphs present a pragmatic assessment of key economic factors as they are likely to impact on interest rates over the next three years.

7.2 In terms of the key economic background and forecasts, looking ahead the current position is as follows:

### (a) The UK Economy

- **Economic Growth** UK GDP growth rates in of 2.2% in 2013 and 2.9% in 2014 were the strongest growth rates of any G7 country; the 2014 growth rate was also the strongest UK rate since 2006 and the 2015 growth rate is likely to be a leading rate in the G7 again. However, the data to quarter 3 2016 has been weak. The Bank of England's November Inflation Report included a forecast for growth to remain around 2.5% – 2.7% over the next three years. For this recovery, however, to become more balanced and sustainable in the longer term, it still needs to move away from dependence on consumer expenditure and the housing market to manufacturing and investment expenditure. The strong growth since 2012 has resulted in unemployment falling quickly to a current level of 5.2%.

- The MPC has been particularly concerned that the squeeze on the disposable incomes of consumers should be reversed by wage inflation rising back above the level of CPI inflation in order to underpin a sustainable recovery. It has, therefore, been encouraging in 2015 to see wage inflation rising significantly above CPI inflation which has been around zero since February. However, it is unlikely that the MPC would start raising rates until wage inflation was expected to consistently stay over 3%. The Inflation Report was notably subdued in respect of the forecasts for CPI inflation; this was expected to barely get back up to the 2% target within the 2-3 year time horizon. The increase in the forecast for inflation at the three year horizon was the biggest in a decade and at the two year horizon it was the biggest since February 2013. However, the first round of falls in oil, gas and food prices in late 2014 and in the first half 2015, will fall out of the 12 month calculation of CPI during late 2015 / early 2016 but only to be followed by a second, more recent, round of falls in fuel prices which will now delay a significant tick up in inflation from around zero. CPI inflation is now expected to get back to around 1% in the second half of 2016 and not get near to 2% until 2017, though the forecasts in the Report itself were for an even slower rate of increase.

- There is, therefore, considerable uncertainty around how quickly pay and CPI inflation will rise in the next few years and this makes it difficult to forecast when the MPC will decide to make a start on increasing Bank Rate. There are also concerns around the fact that the central banks of the UK and US currently have few monetary policy options left to them given that central rates are near to zero and huge QE is already in place. There are, accordingly, arguments that they need to raise rates sooner, rather than later, so as to have some options available for use if there was another major financial crisis in the near future. But it is unlikely that either would raise rates until they are sure that growth was securely embedded and zero inflation was not a significant threat.

- The forecast for the first increase in Bank Rate has, therefore, been pushed back progressively during 2015 from Q4 2015 to Q3 2016. Increases after that are also likely to be at a much slower pace, and to much lower final levels than prevailed before 2008, as increases in Bank Rate will have a much bigger effect on heavily indebted consumers and householders than they did before 2008.

**(b) Global Economy**

- **Eurozone (EZ).** The ECB released a massive €1.1 trillion programme of quantitative easing (QE) to buy up high credit quality government and other debt of selected EZ countries. This programme of €60bn of monthly purchases started in March 2015 and it is intended to run initially to September 2016. This appears to have had a positive effect in helping a recovery in consumer and business confidence and a start to an improvement in economic growth. However, more recent lacklustre progress, combined with the recent downbeat Chinese and emerging markets news, has prompted comments by the ECB that it stands ready to strengthen this programme of QE by extending its time frame and / or increasing its size in order to get inflation up from the current level of around zero towards its target of 2%. The ECB will also aim to help boost the rate of growth in the EZ.
- **USA.** Until the turmoil in financial markets in August, caused by fears about the slowdown in Chinese growth, it had been strongly expected that the Fed. would start to increase rates in September. The Fed pulled back from that first increase due to global risks, but strong employment data in October and November opened the way for the Fed. to embark on its first increase in rates of 0.25% at its December meeting. However, the accompanying message with this first increase was that further increases will be at a much slower rate, and to a much lower ultimate ceiling, than in previous business cycles, mirroring comments by our own MPC.
- **Greece.** During July, Greece finally capitulated to EU demands to implement a major programme of austerity. An €86bn third bailout package has since been agreed although it did nothing to address the unsupportable size of total debt compared to GDP. However, huge damage has been done to the Greek banking system and economy by the initial resistance of the Syriza Government, elected in January, to EU demands. The surprise general election in September gave the Syriza government a mandate to stay in power to implement austerity measures. However, there are major doubts as to whether the size of cuts and degree of reforms required can be fully implemented and so a Greek exit from the euro may only have been delayed by this latest bailout.
- **Portual and Spain.** The general elections in September and December respectively have opened up new areas of political risk where the previous right wing reform-focused pro-austerity mainstream political parties have lost power. A left wing / communist coalition has taken power in Portugal which is heading towards unravelling previous pro austerity reforms. This outcome could be replicated in Spain. This has created nervousness in bond and equity markets for these countries which has the potential to spill over and impact on the whole Eurozone project.
- **Japan.** Japan is causing considerable concern as the increase in sales tax in April 2014 suppressed consumer expenditure and growth. Japan has been hit

hard by the downturn in China during 2015 and there are continuing concerns as to how effective efforts by the Abe government to stimulate growth, and increase the rate of inflation from near zero.

- **China.** The Government has been very active during 2015 in implementing several stimulus measures to try to ensure the economy hits the growth target of 7% for the current year and to bring some stability after the major fall in the onshore Chinese stock market during the summer. Many commentators are concerned that recent growth figures could have been massaged to hide a downturn to a lower growth figure. There are also major concerns as to the creditworthiness of much of the bank lending to corporates and local government during the post 2008 credit expansion period. Overall, China is still expected to achieve a growth figure that the EU would be envious of. Nevertheless, concerns about whether the Chinese economy could be heading for a hard landing, and the volatility of the Chinese stock market, which was the precursor to falls in world financial markets in August and September, remain a concern.
- **Emerging Countries.** There are also considerable concerns about the vulnerability of some emerging countries and their corporates which are getting caught in a perfect storm. Having borrowed massively in dollar denominated debt since the financial crisis (as investors searched for yield by channelling investment cash away from western economies with dismal growth, depressed bond yields and near zero interest rates into emerging countries) there is now a strong flow back to those western economies with strong growth and an imminent rise in interest rates and bond yields.

**(c ) Capita Asset Services Forward View**

- Economic forecasting remains difficult with so many external influences weighing on the UK. Our Bank Rate forecasts, (and also MPC decisions), will be liable to further amendment depending on how economic data evolves over time. Capita Asset Services undertook its last review of interest rate forecasts on 20 December 2015. There is much volatility in rates and bond yields as news ebbs and flows in negative or positive ways.

- The overall trend in the longer term will be for gilt yields and PWLB rates to rise when economic recovery is firmly established accompanied by rising inflation and consequent increases in Bank Rate, and the eventual unwinding of QE. Increasing investor confidence in eventual world economic recovery is also likely to compound this effect as recovery will encourage investors to switch from bonds to equities.

- The overall balance of risks to economic recovery in the UK is currently evenly balanced. Only time will tell just how long this current period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.
- However, the overall balance of risks to our Bank Rate forecast is probably to the downside, i.e. the first increase, and subsequent increases, may be delayed further if recovery in GDP growth, and forecasts for inflation increases, are lower than currently expected.

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

  → Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.

  → UK economic growth is weaker than we currently anticipate.

  → Weak growth or recession in the UK's main trading partners - the EU, US and China.

  → A resurgence of the Eurozone sovereign debt crisis.

  → Recapitalisation of European banks requiring more government financial support.

  → Emerging country economies, currencies and corporates destabilised by falling commodity prices and / or the start of Fed. rate increases, causing a flight to safe havens

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

  → Uncertainty around the risk of a UK exit from the EU.

  → The commencement by the US Federal Reserve of increases in the Fed. funds rate causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities

  → UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

7.3 The Council has appointed Capita Asset Services as its treasury management advisor and part of their service is to assist in formulating a view on interest rates. By drawing together a number of current city forecasts for short term (Bank rate) and longer fixed interest rates a consensus view for bank rate, PWLB borrowing rates and short term investment rates is as follows:-

| | Bank Rate | PWLB Borrowing Rates (including 0.2% discount (para. 6.3)) | | | | Short Term Investment Rates | |
|---|---|---|---|---|---|---|---|
| | | **5 year** | **10 year** | **25 year** | **50 year** | **3 Months** | **1 Year** |
| | **%** | **%** | **%** | **%** | **%** | **%** | **%** |
| Mar 2016 | 0.50 | 2.00 | 2.60 | 3.40 | 3.20 | 0.60 | 1.00 |
| June 2016 | 0.50 | 2.10 | 2.70 | 2.40 | 3.20 | 0.60 | 1.00 |
| Sept 2016 | 0.50 | 2.20 | 2.80 | 3.50 | 3.30 | 0.60 | 1.00 |
| Dec 2016 | 0.75 | 2.30 | 2.90 | 3.60 | 3.40 | 0.80 | 1.30 |
| Mar 2017 | 0.75 | 2.40 | 3.00 | 3.70 | 3.50 | 0.80 | 1.30 |
| June 2017 | 1.00 | 2.50 | 3.10 | 3.70 | 3. 60 | 1.00 | 1.50 |
| Sept 2017 | 1.00 | 2.60 | 3.20 | 3.80 | 3.70 | 1.10 | 1.60 |
| Dec 2017 | 1.25 | 2.70 | 3.30 | 3.90 | 3.80 | 1.30 | 1.80 |
| Mar 2018 | 1.25 | 2.80 | 3.40 | 4.00 | 3.90 | 1.50 | 2.00 |
| June 2018 | 1.50 | 2.90 | 3.50 | 4.00 | 3.90 | 1.50 | 2.00 |
| Sept 2018 | 1.50 | 3.00 | 3.60 | 4.10 | 4.00 | 1.60 | 2.10 |
| Dec 2018 | 1.75 | 3.10 | 3.60 | 4.10 | 4.00 | 1.80 | 2.30 |
| Mar 2019 | 1.75 | 3.20 | 3.70 | 4.10 | 4.00 | 1.90 | 2.40 |

7.4 Thus based on **paragraphs 7.2 and 7.3** above

**Bank Rate**

- UK growth prospects remain strong looking forward into 2016 and 2017
- thus bank rate currently set at 0.5% underpins investment returns and is not expected to start increasing until late 2016
- it is then expected to continue rising by further 0.25% increases reaching 1.75% by December 2018 (0.75% in March 2017 and 1.25% in March 2018)
- as economic forecasting remains difficult with so many external influences weighing on the UK, bank rate forecasts will be liable to further amendments depending on how economic data transpires in the future
- in addition there are significant potential risks from the Eurozone and from financial flows from emerging market in particular so  continuing caution must be exercised in respect of all internet rate forecasts at present

**PWLB Rates**

- fixed interest PWLB borrowing rates are based on UK gilt yields
- the overall longer run trend for gild yields and PWLB rates is to rise due to the high volume of gilt issuance in the UK and of bond issuance in other major Western countries. Over time, an increase in investors' confidence in world economic recovery is also likely to compound this effect as recovery will further encourage investors to switch from bonds to equities

- there are however a number of downside and upside risks to UK gilt yields and PWLB rates, especially for longer term PWLB rates
- PWLB rates are seen to be on a rising trend with a forecast to rise gradually throughout the next three years in all periods as follows:-

| Period | March 2016 | March 2019 | Increase |
|---|---|---|---|
| | % | % | % |
| 5 years | 2.00 | 3.20 | + 1.20 |
| 10 years | 2.60 | 3.70 | + 1.10 |
| 25 years | 3.40 | 4.10 | + 0.70 |
| 50 years | 3.20 | 4.00 | + 0.80 |

**Short Term Investment Rates**

- investment returns are likely to remain relatively low during 2016/17 and beyond
- returns are expected to increase along with bank rate increases
- suggested returns on investments placed for periods up to 100 days are 0.90% in 2016/17, 1.50% in 2017/18 and 2.00% in 2018/19

7.5 The current economic outlook and structure of market interest rates and government debt yields have several key treasury management implications:

- Investment returns are likely to remain relatively low during 2016/17 and beyond;
- Borrowing interest rates have been highly volatile during 2015 as alternating bouts of good and bad news have promoted optimism, and then pessimism, in financial markets. Gilt yields have continued to remain at historically phenominally low levels during 2015. The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in later times, when authorities will not be able to avoid new borrowing to finance new capital expenditure and/or to refinance maturing;
- There will remain a cost of carry to any new borrowing which causes an increase in investments as this will incur a revenue loss between borrowing costs and investment returns.

8.0 **BORROWING STRATEGY 2016/17**

8.1 Based on the interest rate forecast outlined in **Section 7** above, there is a range of potential options available for the Borrowing Strategy for 2016/17. Consideration will therefore be given to the following:

(a) the Council is currently maintaining an under borrowed position. This means that the capital borrowing need (the Capital Financing Requirement) has not been fully funded with loan debt as cash supporting the authority's reserves, balances and cash flow has been used as a temporary measure. This strategy is currently prudent as investment returns are low and counterparty risk remains relatively high;

(b) thus based on the analysis presented in **paragraph 7.3**, the cheapest borrowing will be internal borrowing achieved by continuing to run down cash balances and foregoing interest earned at historically low rates (see **paragraphs 8.5 to 8.13**). However in view of the overall forecast for long term borrowing rates to increase over the next few years, consideration will also be given to weighing the short term advantage of internal borrowing against potential long term costs if the opportunity is missed for taking market loans at long term rates which will be higher in future years;

(c) long term fixed market loans at rates significantly below (0.25% to 0.5%) PWLB rates for the equivalent maturity period (where available) and to maintain an appropriate balance between PWLB and market debt in the debt portfolio. The current market availability of such loans is, however, very limited and is not expected to change in the immediate future;

(d) PWLB borrowing for periods under 10 years where rates are expected to be significantly lower than rates for longer periods. This offers a range of options for new borrowing which would spread debt maturities away from a concentration in longer dated debt. The downside of such shorter term borrowing is the loss of long term stability in interest payments that longer term fixed interest rate borrowing provides;

(e) consideration will be given to PWLB borrowing by annuity and Equal Instalments of Principal (EIP) in addition to maturity loans, which have been preferred in recent years;

(f) as indicated in the table in **paragraph 7.3** PWLB rates are expected to gradually increase throughout the financial year so it would therefore be advantageous to time any new borrowing earlier in the year;

(g) borrowing rates continue to be relatively attractive and may remain relatively low for some time, thus the timing of any borrowing will need to be monitored carefully. There will also remain a 'cost of borrowing' with any borrowing undertaken that results in an increase in investments incurring a revenue loss between borrowing costs and investment returns.

8.2 Based on the PWLB rates set out in **paragraphs 7.3 and 7.4**, suitable trigger rates for considering new fixed rate PWLB or equivalent money market borrowing will be:

| | | |
|---|---|---|
| | | **%** |
| – | 5 year period | 2.4 |
| – | 10 year period | 3.0 |
| – | 25 year period | 3.7 |
| – | 50 year period | 3.6 |

The aim however would be to secure loans at rates below these levels if available.

8.3 The forecast rates and trigger points for new borrowing will be continually reviewed in the light of movements in the slope of the yield curve, the spread between PWLB new borrowing and early repayment rates, and any other changes that the PWLB may introduce to their lending policy and operations.

8.4 It is likely that the Municipal Bonds Agency currently in the process of being set up, will be offering loans to local authorities in the near future. It is also hoped that the borrowing rates will be lower than those offered by the PWLB and the Council intends to make use of this new source of borrowing as and when appropriate.

**External -v- internal borrowing**

8.5 The Council's net borrowing figures (external borrowing net of investments) are significantly below the authority's capital borrowing need (Capital Financing Requirement – CFR) because of two main reasons

(a) a significant level of investments (cash balances – core cash plus cash flow generated) (**paragraph 8.8**);

(b) internally funded capital expenditure (**paragraph 8.6**).

The relative figures are referred to in **paragraphs 3.4 (d) and 3.4 (e)** of this report and covered in more detail in Prudential Indicators 4 and 5 in the separate Prudential Indicators report.

8.6 Such internal borrowing stood at £41.4m at 31 March 2015, principally as a result of funding company loans (see **paragraph 12.6**) from internal, rather than external borrowing, and not taking up any new debt for the 2011/12, 2012/13, 2013/14 and 2014/15 borrowing requirements. The level of this internal capital borrowing depends on a range of factors including:

(a) premature repayment of external debt;

(b) the timing of any debt rescheduling exercises;

(c) the timing of taking out annual borrowing requirements;

(d) policy considerations on the relative impact of financing capital expenditure from cash balances compared with taking new external debt with the balance of external and internal borrowing being generally driven by market conditions.

8.7 The Council continues to examine the potential for undertaking further early repayment of some external debt in order to reduce the difference between the gross and net debt position. However the introduction by the PWLB of significantly lower repayment rates than new borrowing rates in November 2007 compounded by a considerable further widening of the difference between new borrowing and repayment rates in October 2010, has meant that large premiums would be incurred by such actions which could not be justified on value for money grounds. This situation will be monitored closely in case the differential is narrowed by the PWLB at some future dates.

8.8 This internal capital borrowing option is possible because of the Council's cash balance with the daily average being £260.9m in2014/15. This consisted of cash flow generated (creditors etc), core cash (reserves, balances and provisions etc) and cash managed on behalf of other organisations. Consideration does therefore need to be given to the potential merits of internal borrowing.

8.9 As 2016/17 is expected to continue as a year of historically low bank interest rates, certainly until later in the year, this extends the current opportunity for the Council to continue with the current internal borrowing strategy.

8.10 Over the next three years investment rates are expected to be below long term borrowing rates. A value for money consideration would therefore indicate that value could be obtained by continuing avoiding/delaying some or all new external borrowing and by using internal cash balances to finance new capital expenditure or to replace maturing external debt. This would maximise short term savings but is not risk free.

8.11 The use of such internal borrowing, which runs down investments, also has the benefit of reducing exposure to low interest rates on investments, and the credit risk of counterparties.

8.12 In considering this option however, two significant risks to take into account are

(a) the implications of day to day cash flow constraints, and;

(b) short term savings by avoiding/delaying new long external borrowing in 2016/17 must be weighed against the loss of longer term interest rate stability. Thus there is the potential for incurring long term extra costs by delaying unavoidable new external borrowing until later years by which time PWLB long term rates are forecast to be significantly higher.

8.13 Borrowing interest rates are on a rising trend. The policy of avoiding new borrowing by running down cash balances has served the Council well in recent years. However this needs to be carefully reviewed and monitored to avoid incurring even higher borrowing costs which are now looming even closer for authorities who will not be able to avoid new borrowing to finance new capital expenditure and/or to refinance maturing debt in the near future.

8.14 **The general strategy for this “Internal Capital Financing” option will therefore be to continue to actively consider and pursue this approach on an ongoing basis in order to reduce the difference between the gross and net debts levels (paragraph 8.5) together with achieving short term savings and mitigating the credit risk incurred by holding investments in the market. Bearing in mind paragraph 8.12 however this policy will be carefully reviewed and monitored on an on-going basis.**

**Overall Approach to Borrowing in 2016/17**

8.15 Given the market conditions, economic background and interest rate forecasts set out in **paragraph 7** above, caution will be paramount within the Council’s 2016/17 Treasury Management operations. The Corporate Director – Strategic Resources will monitor the interest rates closely and adopt a pragmatic approach to changing circumstances – any key strategic decision that deviates from the Borrowing Strategy outlined above will be reported to the Executive at the next available opportunity.

### Sensitivity of the Strategy

8.16 The main sensitivities of the Strategy are likely to be the two scenarios below. The Corporate Director – Strategic Resources will, in conjunction with the Council's Treasury Management Advisor, continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a significant change of market view:

*(a)* *if it is felt that there was a significant risk of a sharp fall in both long and short term rates,* (e.g. due to a marked increase of risks around the relapse into recession or of risks of deflation), then long term borrowing will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered;

*(b)* *if it were felt that there was a significant risk of a much sharper rise in long and short term rates than that currently forecast* (perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks), then the portfolio position will be re-appraised with the likely action that fixed rate funding will be taken whilst interest rates are still lower than they will be in the next few years.

8.17 As mentioned, however, in **paragraphs 8.5 to 8.13**, the likely outcome will be to delay external borrowing in 2016/17 and continue to fund the year's borrowing requirement together with that for 2011/12, 2012/13, 2013/14 and 2014/15 from internal sources (ie running down the investment of cash balances). This has the potential for achieving short term revenue savings in 2016/17 and also has the benefit of reducing investment exposure to credit risk.

## 9.0 CAPPING OF CAPITAL FINANCING COSTS

9.1 During the preparation of an earlier Revenue Budget/Medium Term Financial Strategy concerns were expressed about the possible ongoing impact on the annual Net Revenue Budget of capital expenditure generated either by government borrowing approvals or approved locally under the Prudential Borrowing regime.

9.2 As a result Members approved a local policy to cap capital financing charges as a proportion of the annual Net Revenue Budget. This cap was set at 10% in 2016/17 (previously 11%) which accommodates existing Capital Plan requirements and will act as a regulator if Members are considering expanding the Capital Plan using Prudential Borrowing. Members do of course have the ability to review the cap at any time but this would have to be done in the light of its explicit impact on the Revenue Budget/Medium Term Financial Strategy.

9.3 The relationship between levels of capital expenditure and the consequential capital financing costs that they generate is demonstrated in the following table.

| Year | Forecast Annual Net Budget (ANB) £m | Budgeted Capital Financing Costs £m | Costs as a %age of ANB % | 1% of ANB £m | Potential Capital Spend from 1% on ANB £m |
|---|---|---|---|---|---|
| | (a) | (b) | (c) | (d) | (e) |
| 2015/16 | 364.2 | 28.6 | 7.8 | 3.6 | |
| 2016/17 | 356.9 | 27.8 | 7.8 | 3.6 | 43.0 |
| 2017/18 | 351.8 | 27.1 | 7.7 | 3.5 | |
| 2018/19 | 353.9 | 26.3 | 7.4 | 3.5 | |
| | | | (b÷a) | (a/100) | |

9.4 The above table reflects the following

- the impact of the Local Government Finance Settlement for 2016/17 in terms of:

  (a) a changed ‘forecast annual net budget’ since 2011/12 reflecting former specific grants being rolled into general formula grant which has the effect of increasing the ‘net budget requirement’ and continuing grant cuts which result in a reduced ‘net revenue budget’.

  (b) significantly reduced borrowing requirements and consequential reduced capital financing costs resulting from all Government capital approvals from 2011/12 being funded from grants rather than the previous mix of grant and supported borrowing approvals.

- budgeted capital financing costs include interest on external debt plus lost interest earned on internally financed capital expenditure, together with a prudent Minimum Revenue Provision for debt repayment

9.5 In addition to showing explicitly the direct link between the level of capital spend and impact on the Revenue Budget to date, the table also includes an estimate of the impact that planned levels of future capital expenditure (based on the current Capital Plan) will have on the proportion of the Annual Revenue Budget that will be required to meet the consequential capital financing costs (see **column (c)**).

9.6 The table also shows, at **column (e)**, how much additional capital spend a 1% increase in the annual Budget **(column (d)**) will support.

## 10.0 REVIEW OF LONG TERM DEBT AND DEBT RESCHEDULING

10.1 The long term debt of the Council is under continuous review.

10.2 The rescheduling of debt involves the early repayment of existing debt and its replacement with new borrowing. This can result in one-off costs or benefits called, respectively, premiums and discounts. These occur where the rate of the loan repaid varies from comparative current rates. Where the interest rate of the loan to be repaid is higher than the current rates, a premium is charged by the PWLB for repayment. Where the interest rate of the loan to be repaid is lower than the current rate, a discount on repayment is paid by the PWLB.

10.3 Discussions with the Council's Treasury Management Advisor about the long term financing strategy are ongoing and any debt rescheduling opportunity will be fully explored.

10.4 The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt, which was compounded in October 2010 by a considerable further widening of the difference between new borrowing and repayment rates, has meant that PWLB to PWLB debt restructuring is now much less attractive than it was before both of these events. In particular, consideration has to be given to the large premiums which would be incurred by prematurely repaying existing PWLB loans and it is very unlikely that these could be justified on value for money grounds if using replacement PWLB refinancing. However, some interest savings might still be achievable through using LOBO (Lenders Option Borrowers Option) loans and other market loans, in rescheduling exercises rather than using PWLB borrowing as the source of replacement financing. An issue in relation to such PWLB/LOBO rescheduling however is that only a proportion of the Council's debt portfolio should consist of money market loans (30% of total debt outstanding – see **paragraph 6.6**) which limits the extent of such rescheduling. Also unlike PWLB loans which can be rescheduled at regular intervals, once a LOBO loan has been taken, future rescheduling opportunities are more limited.

10.5 As short term borrowing rates are expected to be considerably cheaper than longer term rates throughout 2016/17, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred), their short term nature and the likely costs of refinancing those short term loans once they mature, compared to the current rates of longer term debt in the existing debt portfolio.

10.6 Consideration will also be given to indentify if there is any residual potential left for making savings by running down investment balances by repaying debt prematurely as short term rates on investments are likely to be lower than rates paid on currently held debt. However, this will need careful consideration in light of the debt repayment premiums.

10.7 The reasons for undertaking any rescheduling will include:

(a) the generation of cash savings at minimum risk;

(b) in order to help fulfil the Borrowing Strategy outlined in **Section 8** above, and;

(c) in order to enhance the balance of the long term portfolio (ie amend the maturity profile and/or the balance of volatility).

10.8 Members will appreciate that with long term debt of £319.8m at 31 March 2015 (see **paragraph 4.5** of accompanying report) and with an annual interest cost to the Revenue Budget of about £14m the savings or additional costs, attached to even a small interest rate variation can be significant. To put this into context for every 0.1% that the interest rate can be reduced it saves £0.35m on interest charges in the Revenue Budget. Any proposals to restructure debt or change the policy laid out earlier in this Strategy, therefore demand careful attention. Any debt rescheduling will, however, be in accordance with the Borrowing Strategy position outlined in **Section 8** above.

10.9 No new debt rescheduling activities have been undertaken by the Council in 2015/16 to date with none being expected during the remainder of the financial year.

## 11.0 MINIMUM REVENUE PROVISION (MRP) POLICY 2016/17

11.1 The statutory requirement for local authorities to charge the Revenue Account each year with a specific sum for debt repayment was replaced in February 2008 with more flexible statutory guidance which came into effect from 2008/09.

11.2 The new, and simpler, statutory duty (Statutory Instrument 2008) is that a local authority shall determine for the financial year an amount of minimum revenue provision (MRP) that it considers to be prudent. This replaces the previous prescriptive requirement that the minimum sum should be 4% of the Capital Financing Requirement (CFR); the CFR consists of external debt plus capital expenditure financed by borrowing from internal sources (surplus cash balances).

11.3 To support the statutory duty the Government also issued fresh guidance in February 2008 which requires that a Statement on the Council's policy for its annual MRP should be submitted to the full Council for approval before the start of the financial year to which the provision will relate. The Council are therefore legally obliged to have regard to this MRP guidance in the same way as applies to other statutory guidance such as the CIPFA Prudential Code, the CIPFA Treasury Management Code and the DCLG guidance on Investments.

11.4 The MRP guidance offers four options under which MRP might be made, with an overriding recommendation that the Council should make prudent provision to redeem its debt liability over a period which is reasonably commensurate with that over which the asset created by the capital expenditure is estimated to provide benefits (ie estimated useful life of the asset being financed). The previous system of 4% MRP did not necessarily provide that link.

11.5 The guidance also requires an annual review of MRP policy being undertaken and it is appropriate that this is done as part of this Annual Treasury Management Strategy.

11.6 The move to International Financial Reporting Standards (IFRS) from 2010/11 involves Private Finance Initiative (PFI) contracts and some leases (being reclassified as finance leases instead of operating leases) coming onto Local Authority Balance Sheets as long term liabilities. This accounting treatment impacts on the CFR mentioned in **paragraph 11.2** above with the result that an annual MRP provision is required for PFI contracts and certain leases. To ensure that this change has no overall financial impact on local authority budgets, the Government updated their "Statutory MRP Guidance" with effect from 31 March 2010. This updated Guidance allows MRP to be equivalent to the existing lease rental payments and "capital repayment element" of annual payments to PFI Operators and the implications of this are reflected in the Council's MRP policy for 2016/17 as set out in **paragraph 11.8** below.

11.7 The ‘Statutory MRP Guidance’ was again updated from 1 April 2012 but the amendments relate only to those authorities with responsibility for housing. MRP guidance remained the same for all other authorities.

11.8 The Council’s MRP policy is based on the Government’s Statutory Guidance and following a review of this policy, no changes are proposed at this time. However, a further review of the existing assumptions for prudent provision incorporated into the Council’s MRP Policy will be undertaken as part of the 2016/17 budget review and any changes will be reported to Members as part of an in-year update of this Annual Treasury Management Strategy. Until that time, the policy for 2016/17 remains as follows:-

(a) for all **capital expenditure incurred before 1 April 2008**, MRP will be based on 4% of the Capital Financing Requirement (CFR) at that date. This will include expenditure supported by Government borrowing approvals and locally agreed Prudential Borrowing up to 31 March 2008. This is in effect a continuation of the old MRP regulations for all capital expenditure up to 31 March 2008 that has been financed from borrowing;

(b) for **capital expenditure incurred after 1 April 2008 which is supported by Government Borrowing approvals**, MRP to be based on 4% of such sums as reflected in subsequent CFR updates. This reflected the principle that the Revenue Support Grant (RSG) formula for supported borrowing approvals would still be calculated on this basis. It should be noted however that as part of the 2011/12 Local Government Finance Settlement, no supported borrowing approvals have been issued for the period after 2010/11 and the RSG formula was frozen as part of the 2013/14 introduction of retained local Business Rates;

(c) for **locally agreed Prudential Borrowing on capital expenditure incurred after 1 April 2008**, MRP will be calculated based on equal annual instalments over the estimated useful life of the asset for which the borrowing is undertaken. This method is a simpler alternative to depreciation accounting.

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

The estimated life of relevant assets will be assessed each year based on types of capital expenditure incurred but in general will be 25 years for buildings, 50 years for land, and 5 to 7 years for vehicles, plant and equipment. To the extent that the expenditure does not create a physical asset (eg capital grants and loans), and is of a type that is subject to estimated life periods that are referred to in the guidance, these periods will generally be adopted by the Council.

However in the case of long term debtors arising from loans or other types of capital expenditures incurred by the Council which will be repaid under separate arrangements (eg loans to NYnet and Yorwaste), there will be no MRP made. The Council is satisfied that a prudent provision will be achieved after exclusion of these capital expenditure items.

This approach also allows the Council to defer the introduction of an MRP charge for new capital projects/land purchases until the year after the new asset becomes operational rather than in the year borrowing is required to finance the capital spending. This approach is beneficial for projects that take more than one year to complete and is therefore included as part of the MRP policy.

(d) for **"on balance sheet" PFI schemes**, MRP will be equivalent to the "capital repayment element" of the annual service charge payable to the PFI Operator and for **finance leases**, MRP will be equivalent to the annual rental payable under the lease agreement.

11.9 Therefore the Council's total MRP provision will be the sum of (a) + (b) + (c) + (d) (as defined above) which is considered to satisfy the prudent provision requirement. Based on this policy, total MRP in 2016/17 will be about £14.1m (including PFI and finance leases).

## 12.0 ANNUAL INVESTMENT STRATEGY

### Background

12.1 Under the Local Government Act 2003 the Council is required to have regard to Government Guidance in respect of the investment of its cash funds. This Guidance was revised with effect from 1 April 2010. The Guidance leaves local authorities free to make their own investment decisions, subject to the fundamental requirement of an Annual Investment Strategy being approved by the Council before the start of the financial year.

12.2 This Annual Investment Strategy must define the investments the Council has approved for prudent management of its cash balances during the financial year under the headings of **specified investments** and **non specified investments**.

12.3 This Annual Investment Strategy therefore sets out

- revisions to the Annual Investment Strategy (**paragraph 12.4**);
- the Investment Policy (**paragraph 12.5**);
- the policy regarding loans to companies in which the Council has an interest (**paragraph 12.6**);
- specified and non specified investments (**paragraph 12.7**);
- Creditworthiness Policy - security of capital and the use of credit ratings (**paragraph 12.8**);
- the Investment Strategy to be followed for 2016/17 (**paragraph 12.9**);

- investment reports to members (**paragraph 12.10**);
- investment of money borrowed in advance of need (**paragraph 12.11**);
- investment (and Treasury Management) training (**paragraph 12.12**);

**Revisions to the Annual Investment Strategy**

12.4 In addition to this updated **Investment Strategy,** which requires approval before the start of the financial year, a revised Strategy will be submitted to Council for consideration and approval under the following circumstances:

(a) significant changes in the risk assessment of a significant proportion of the Council's investments;

(b) any other significant development(s) that might impact on the Council's investments and the existing strategy for managing those investments during 2016/17.

**Investment Policy**

12.5 The parameters of the Policy are as follows:

(a) the Council will have regard to the Government's Guidance on Local Government Investments as revised with effect from 1 April 2010, and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes;

(b) the Council's investment policy has two fundamental objectives;

- the security of capital (protecting the capital sum from loss); and then
- the liquidity of its investments (keeping the money readily available for expenditure when needed)

(c) the Council will also aim to seek the highest return (yield) on its investments provided that proper levels of security and liquidity are achieved. The risk appetite of the Council is low in order to give priority to the security of its investments;

(d) the borrowing of monies purely to invest or lend and make a return is unlawful and the Council will not engage in such activity;

(e) investment instruments for use in the financial year listed under **specified** and **non-specified investment** categories (see **paragraph 12.7**);

(f) counterparty limits will be set through the Council's Treasury Management Practices Schedules.

**Policy regarding loans to companies in which the Council has an interest**

12.6 (a) the Council's general investment powers under this Annual Treasury Management and Investment Strategy come from the Local Government Act

2003 (Section 12). Under this Act a local authority has the power to invest for any purpose relevant to its functions or for the purpose of the prudent management of its financial affairs

(b) in addition to investment, the Council has the power to provide loans and financial assistance to Limited Companies under the Localisation Act 2011 (and also formally under the general power of wellbeing in the Local Government Act 2000) which introduced a general power of competence for authorities (to be exercised in accordance with their general public law duties)

(c) any such loans to limited companies by the Council, will therefore be made under these powers. They will not however be classed as investments made by the Council and will not impact on this Investment Strategy. Instead they will be classed as capital expenditure by the Council under the Local Authorities (Capital Finance and Accounting) Regulations 2003, and will be approved, financed and accounted for accordingly

(d) at present the Council has made loans to two companies in which it has an equity investment (ie Yorwaste and NYnet). In both cases loan limits are set, and reviewed periodically, by the Executive

**Specified and non-specified Investments**

12.7 Based on Government Guidance as updated from 1 April 2010.

(a) investment Instruments identified for use in the forthcoming financial year are listed in the Schedules attached to this Strategy under the **specified** and **non-specified** Investment categories;

(b) all **specified** Investments (see **Schedule A**) are defined by the Government as options with “relatively high security and high liquidity” requiring minimal reference in investment strategies. In this context, the Council has defined Specified Investments as being sterling denominated, with maturities up to a maximum of 1 year meeting the minimum high credit quality;

(c) **Non-specified** investments (see **Schedule B**) attract a greater potential of risk. As a result, a maximum local limit of 20% of “core cash” funds available for investment has been set which can be held in aggregate in such investments;

(d) for both **specified** and **non-specified** investments, the attached Schedules indicate for each type of investment:-

- the investment category
- minimum credit criteria
- circumstances of use
- why use the investment and associated risks
- maximum % age of total investments
- maximum maturity period

(Non-Specified only)

(e) there are other instruments available as Specified and Non-Specified investments which the Council will NOT currently use. Examples of such investments are:-

| | |
|---|---|
| Specified Investments | - Commercial Paper<br>- Gilt funds and other Bond Funds<br>- Treasury Bills |
| Non-Specified Investments | - Sovereign Bond issues<br>- Corporate Bonds<br>- Floating Rate notes<br>- Equities<br>- Open Ended Investment Companies<br>- Derivatives |

A proposal to use any of these instruments would require detailed assessment and be subject to approval by Members as part of this Strategy. Under existing scrutiny arrangements, the Council's Audit Committee will also look at any proposals to use the instruments referred to above.

**Creditworthiness Policy – Security of Capital and the use of credit ratings**

12.8 The financial markets have experienced a period of considerable turmoil since 2008 and as a result attention has been focused on credit standings of counterparties with whom the Council can invest funds.

It is paramount that the Council's money is managed in a way that balances risk with return, but with the overriding consideration being given to the security of the invested capital sum followed by the liquidity of the investment. The Approved Lending List will therefore reflect a prudent attitude towards organisations with whom funds may be deposited.

The rationale and purpose of distinguishing specified and non-specified investments is detailed in **paragraph 12.7** above. Part of the definition for a Specified investment is that it is an investment made with a body which has been awarded a high credit rating with maturities of no longer than 364 days.

It is, therefore, necessary to define what the Council considers to be a "high" credit rating in order to maintain the security of the invested capital sum.

The methodology and its application in practice will, therefore, be as follows:-

(a) the Council will rely on credit ratings published by the three credit rating agencies (Fitch, Moody's and Standard & Poor's) to establish the credit quality (ability to meet financial commitments) of counterparties (to whom the Council lends) and investment schemes. Each agency has its own credit rating components to complete their rating assessments. These are as follows:

**Fitch Ratings**

| | | |
|---|---|---|
| Long Term | - | generally cover maturities of over five years and acts as a measure of the capacity to service and repay debt obligations punctually. Ratings range from AAA (highest credit quality) to |

D (indicating an entity has defaulted on all of its financial obligations)

Short Term - cover obligations which have an original maturity not exceeding one year and place greater emphasis on the liquidity necessary to meet financial commitments. The ratings range from F1+ (the highest credit quality) to D (indicating an entity has defaulted on all of its financial obligations)

**Moody's Ratings**

Long Term - an opinion of the relative credit risk of obligations with an original maturity of one year or more. They reflect both the likelihood of a default on contractually promised payments and the expected financial loss suffered in the event of default. Ratings range from Aaa (highest quality, with minimal credit risk) to C (typically in default, with little prospect for recovery of principal or interest)

Short Term - an opinion of the likelihood of a default on contractually promised payments with an original maturity of 13 months or less. Ratings range from P-1 (a superior ability to repay short-term debt obligations) to P-3 (an acceptable ability to repay short-term obligations)

**Standard & Poor's Ratings**

Long Term - considers the likelihood of payment. Ratings range from AAA (best quality borrowers, reliable and stable) to D (has defaulted on obligations)

Short Term - generally assigned to those obligations considered short-term in the relevant market. Ratings range from A-1 (capacity to meet financial commitment is strong) to D (used upon the filing of a bankruptcy petition).

In addition, all three credit rating agencies produce a Sovereign Rating to select counterparties from only the most creditworthy countries. The ratings are the same as those used to measure long term credit.

(b) the Council will review the "ratings watch" and "outlook" notices issued by all three credit rating agencies referred to above. An agency will issue a "watch", (notification of likely change), or "outlook", (notification of a possible longer term change), when it anticipates that a change to a credit rating may occur in the forthcoming 6 to 24 months. The "watch" or "outlook" could reflect either a positive (increase in credit rating), negative (decrease in credit rating) or developing (uncertain whether a rating may go up or down) outcome;

(c) no combination of ratings can be viewed as entirely fail safe and all credit ratings, watches and outlooks are monitored on a daily basis. This is achieved through the use of Capita Asset Services creditworthiness service. This employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies. The credit ratings of counterparties are then supplemented with the following overlays;

- credit watches and credit outlooks from credit rating agencies
- CDS spreads to give early warning of likely changes in credit ratings
- sovereign ratings to select counterparties from only the most creditworthy countries

This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the duration for investments. The Council will therefore use counterparties within the following durational bands:-

| **Colour** | **Maximum Investment Duration** |
|---|---|
| Yellow | 5 Years |
| Purple | 2 Years |
| Orange | 1 |
| Blue | 1 Year (UK nationalised / semi nationalised banks only) |
| Red | 6 months |
| Green | 100 days |
| No colour | No investments to be made |

(d) given that a number of central banks/government have supported or are still supporting their banking industries in some way, the importance of the credit strength of the sovereign has become more important. The Council will therefore also take into account the Sovereign Rating for the country in which an organisation is domiciled. As a result, only an institution which is domiciled in a country with a minimum Sovereign Rating of AA- from Fitch or equivalent would be considered for inclusion on the Council's Approved Lending List (subject to them meeting the criteria above). Organisations which are domiciled in a Country whose Sovereign Rating has fallen below the minimum criteria will be suspended, regardless of their own individual score/colour. The list of countries that currently qualify using this credit criteria are shown in **Schedule D**. This list will be amended should ratings change, in accordance with this policy;

(e) in order to reflect current market sentiment regarding the credit worthiness of an institution the Council will also take into account current trends within the Credit Default Swap (CDS) Market. Since they are a traded instrument they reflect the market's current perception of an institution's credit quality, unlike credit ratings, which often focus on a longer term view. These trends will be monitored through the use of Capita Asset Services creditworthiness service which compares the CDS Market position for each institution to the benchmark CDS Index. Should the deviation be great, then market sentiment suggests that there is a fear that an institution’s credit quality will fall. Organisations with such deviations will be monitored and their standing reduced by one colour band (**paragraph 12.8 (c)**) as a precaution. Where the deviation is great, the organisation will be awarded ‘no colour’ until market sentiment improves. Where entities do not have an actively traded CDS spread, credit ratings are used in isolation;

(f) fully and part nationalised banks within the UK currently have credit ratings which are not as high as other institutions. This is the result of the banks having to have to accept external support from the UK Government However, due to this Central Government involvement, these institutions now effectively take on the credit worthiness of the Government itself (i.e. deposits made with them are effectively being made to the Government). This position is expected to take a number of years to unwind and would certainly not be done so without a considerable notice period. As a result, institutions which are significantly or fully owned by the UK Government will be assessed to have a high level of credit worthiness;

(g) all of the above will be monitored on a weekly basis through Capita Asset Services creditworthiness service with additional information being received and monitored on a daily basis should credit ratings change and/or watch/outlook notices be issued. Sole reliance will not be placed on the information provided by Capita Asset Services however. In addition the Council will also use market data and information available from other sources such as the financial press and other agencies and organisations;

(h) in addition, the Council will set maximum investment limits for each organisation which also reflect that institution’s credit worthiness – the higher the credit quality, the greater the investment limit. These limits also reflect UK Government involvement (i.e. Government ownership or being part of the UK Government guarantee of liquidity). These limits are as follows:-

| Maximum Investment Limit | Criteria |
| --- | --- |
| £85m | UK "Nationalised / Part Nationalised" banks / UK banks with UK Central Government involvement |
| £20m to £75m | UK "Clearing Banks" and selected UK based Banks and Building Societies |
| £20m or £40m | High quality foreign banks |

(i) should a score/colour awarded to a counterparty or investment scheme be amended during the year due to rating changes, market sentiment etc., the Council will take the following action:-

- reduce or increase the maximum investment term for an organisation dependent on the revised score / colour awarded (in line with the boundaries and colours set in **paragraph 12.8(c)**)
- temporarily suspend the organisation from the Approved Lending List should their score fall outside boundary limits and not be awarded a colour
- seek to withdraw an investment as soon as possible, within the terms and conditions of the investment made, should an organisation be suspended from the Approved Lending List
- ensure all investments remain as liquid as possible, i.e. on instant access until sentiment improves.

(j) if a counterparty / investment scheme, not currently included on the Approved Lending List is subsequently upgraded, (resulting in a score which would fulfil the Council's minimum criteria), the Corporate Director – Strategic Resources has the delegated authority to include it on the Council's Approved Lending List with immediate effect;

(k) a copy of the current Approved Lending List, showing maximum investment and time limits is attached at **Schedule C**. The Approved Lending List will be monitored on an ongoing daily basis and changes made as appropriate. Given current market conditions, there continues to be a very limited number of organisations which fulfil the criteria for non specified investments. This situation will be monitored on an ongoing basis with additional organisations added as appropriate with the approval of the Corporate Director – Strategic Resources.

**The Investment Strategy to be followed for 2016/17**

12.9 Recognising the categories of investment available and the rating criteria detailed above

(a) the Council currently manages all its cash balances internally;

(b) ongoing discussions are held with the Council's Treasury Management Advisor on whether to consider the appointment of an external fund manager(s) or continue investing in-house – any decision to appoint an external fund manager will be subject to Member approval;

(c) the Council's cash balances consist of two basic elements. The first element is **cash flow derived** (debtors/creditors/timing of income compared to expenditure profile). The second, **core element**, relates to specific funds (reserves, provisions, balances, capital receipts, funds held on behalf of other organisations etc.);

(d) having given due consideration to the Council's estimated level of funds and balances over the next three financial years, the need for liquidity and day to day cash flow requirements it is forecast that a maximum of £20m of the overall balances can be prudently committed to longer term investments (e.g. between 1 and 3 years);

(e) investments will accordingly be made with reference to this core element and the Council's ongoing cash flow requirements (which may change over time) and the outlook for short term interest rates (i.e. rates for investments up to 12 months);

(f) the Council currently has no non-specified investments over 364 days;

(g) bank rate has been unchanged at 0.5% since March 2009 and underpins investment returns. It is not expected to start increasing until mid 2016;

The Council will, therefore, avoid locking into long term deals while investment rates continue to be at historically low levels unless attractive rates are available with counterparties of particularly high creditworthiness which make longer term deals worthwhile and within a 'low risk' parameter. Thus no trigger rates will be set for longer term deposits (two or three years) but this position will be kept under constant review and discussed with the Treasury Management Advisor on a regular basis.

Based on current bank rate forecasts, as outlined above, an overall investment return of about 0.75% is likely in 2016/17, 1.25% in 2017/18 and 1.80% in 2018/19.

(h) for its cash flow generated balances the Council will seek to utilise 'business reserve accounts' (deposits with certain banks and building societies), 15, 30 and 100 day accounts and short dated deposits (overnight to three months) in order to benefit from the compounding of interest.

**Investment Reports to Members**

12.10 Reporting to Members on investment matters will be as follows:

(a) in-year investment reports will be submitted to the Executive as part of the Quarterly Performance and Budget Monitoring reports;

(b) at the end of the financial year a comprehensive report on the Council's investment activity will be submitted to the Executive as part of the Annual Treasury Management Outturn report;

(c) periodic meetings between the Corporate Director – Strategic Resources, the Corporate Affairs portfolio holder and the Chairman of the Audit Committee provide an opportunity to consider and discuss issues arising from the day to day management of Treasury Management activities.

(see **Section 14** for full details).

**Investment of Money Borrowed in Advance of Need**

12.11 The Borrowing Policy covers the Council's policy on Borrowing in Advance of Spending Needs (**paragraph 6.10**).

Although the Council has not borrowed in advance of need to date and has no current plans to do so in the immediate future, any such future borrowing would impact on investment levels for the period between borrowing and capital spending.

Any such investments would, therefore, be made within the constraints of the Council's current Annual Investment Strategy, together with a maximum investment period related to when expenditure was expected to be incurred.

**Treasury Management Training**

12.12 The training needs of the Council's staff involved in investment management are monitored, reviewed and addressed on an on-going basis and are discussed as part of the staff appraisal process. In practice most training needs are addressed through attendance at courses and seminars provided by CIPFA, the LGA and others on a regular ongoing basis.

The CIPFA Code also requires that Members with responsibility for treasury management receive adequate training in treasury management. This especially applies to Members responsible for scrutiny (i.e. the Audit Committee). An in-house training course for Members (which was also attended by officers) was provided by Capita Asset Services – Treasury Solutions on 30 September 2013. Further training will be arranged as required. The training arrangements for officers mentioned in the paragraph above will also be available to Members.

## 13.0 OTHER TREASURY MANAGEMENT ISSUES

**Policy on the use of External Treasury Management Service Providers**

13.1 The Council uses Capita Asset Services – Treasury Solutions as its external treasury management adviser. Capita provide a source of contemporary information, advice and assistance over a wide range of Treasury Management areas but particularly in relation to investments and debt administration.

13.2 Whilst the Council recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources, it fully accepts that responsibility for Treasury Management decisions remains with the authority at all times and will ensure that undue reliance is not placed upon advice of the external service provider.

13.3 Following a quotation exercise Capita Asset Services were appointed in September 2015 as a single provider of Treasury Management consultancy services for both the County Council and Selby District Council. The appointment is for three years, with the option for a further two year extension. The value and quality of services being provided are monitored and reviewed on an ongoing basis.

**The scheme of delegation and role of the section 151 officer in relation to Treasury Management**

13.4 The Government's Investment Guidance (**paragraph 12.1**) requires that a local authority includes details of the Treasury Management schemes of delegation and the role of the Section 151 officer in the Annual Treasury Management/Investment Strategy.

13.5 The key elements of delegation in relation to Treasury Management are set out in the following Financial Procedure Rules (FPR):-

(a) **14.1** The Council adopts CIPFA's "Treasury Management in the Public Services Code of Practice 2011" (as amended) as described in Section 5 of the Code, and will have regard to the associated guidance notes;

(b) **14.2** The Council will create and maintain as the cornerstone for effective Treasury Management

(i) a strategic Treasury Management Policy Statement (TMPS) stating the Council's policies, objectives and approach to risk management of its treasury management activities;

(ii) a framework of suitable Treasury Management Practices (TMPs) setting out the manner in which the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities. The Code recommends 12 TMPs;

(c) **14.3** The Executive and the full Council will receive reports on its Treasury Management policies, practices and activities including, as a minimum an Annual Treasury Management and Investment Strategy and associated report on Prudential Indicators in advance of the financial year;

(d) **14.4** The Council delegates responsibility for the implementation and regular monitoring of its Treasury Management policies and practices to the Executive, and for the execution and administration of Treasury Management decisions to the Corporate Director – Strategic Resources (CD-SR), who will act in accordance with the Council's TMPs, as well as CIPFA's Standard of Professional Practice on Treasury Management;

(e) **14.5** The Executive will receive from the CD-SR a quarterly report on Treasury Management as part of the Quarterly Performance Monitoring report and an annual report on both Treasury Management and Prudential Indicators setting out full details of activities and performance during the preceding financial year;

(f) **14.6** The CD-SR will meet periodically with the portfolio holder for financial services, including assets, IT and procurement and such other Member of the Executive as the Executive shall decide to consider issues arising from the day to day Treasury Management activities;

(g) **14.7** The Audit Committee shall be responsible for ensuring effective scrutiny of the Treasury Management process;

(h) **14.8** The CD-SR shall periodically review the Treasury Management Policy Statement and associated documentation and report to the Executive on any necessary changes, and the Executive shall make recommendations accordingly to the Council;

(i) **14.9** All money in the possession of the Council shall be under the control of the officer designated for the purposes of Section 151 of the Local Government Act 1972 (i.e. the Corporate Director - Strategic Resources).

13.6 The Treasury Management reporting arrangements in relation to the above are covered in more detail in **section 14**.

13.7 In terms of the Treasury Management role of the Section 151 officer (the Corporate Director – Strategic Resources), the key areas of delegated responsibility are as follows

- recommending clauses, treasury management policies and practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports to Members
- submitting budgets and budget variations to Members
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers

**Operational Leasing**

13.8 Up to 2004/05 the Council used operational leasing to acquire plant and vehicles. The main reason was that such financing did not impact on the level of capital resources (capital receipts and Government borrowing approvals) otherwise available to the Council. However because this rationale no longer applies under the Prudential Code there is now the option of undertaking additional unsupported borrowing to finance such items.

13.9 The option to finance by operational leasing is, of course, still available and therefore the use of leasing for periods greater than one year is approved within the schedule of Treasury Management Practices which support the Council's Treasury Management Policy Statement. Furthermore the Financial Procedure Rules of the Council require that the Corporate Director – Strategic Resources shall undertake the negotiation of all leasing arrangements.

13.10 A detailed option appraisal on whether to operationally lease, finance lease or fund from borrowing is undertaken for all plant and vehicle requirements as it may be the case that the best value option will change over time (e.g. as market conditions fluctuate). Since 2004/05, options appraisals have resulted in purchases being financed from Prudential borrowing as well as operational leasing with consequential financing costs of both methods being recharged to Directorates. In 2014/15 acquisitions totalling £0.7m were financed from Prudential borrowing. For 2015/16 the forecast outturn position is £0.3m to be financed from Prudential Borrowing.

13.11 Further option appraisals will be carried out during the year to determine whether financing should be through leasing or Prudential borrowing.

**Other Issues**

13.12 The Council continues to monitor potential PFI opportunities and assess other innovative methods of funding and the Corporate Director – Strategic Resources will report any developments to Executive at the first opportunity.

## 14.0 ARRANGEMENTS FOR MONITORING / REPORTING TO MEMBERS

14.1 Taking into account the matters referred to in this Strategy, the monitoring and reporting arrangements in place relating to Treasury Management activities are now as follows:

(a) an annual report to Executive and Council as part of the Budget process that sets out the Council's **Treasury Management Strategy and Policy** for the forthcoming financial year;

(b) an annual report to Executive and Council as part of the Budget process that sets the various **Prudential Indicators**, together with a mid year update of these indicators as part of the Q1 Performance Monitoring report submitted to the Executive (see **(d)** below);

(c) **annual outturn reports** to the Executive for both Treasury Management and Prudential Indicators setting out full details of activities and performance during the preceding financial year.

(d) a quarterly report on Treasury Matters to Executive as part of the **Quarterly Performance and Budget Monitoring** report;

(e) **periodic meetings** between the Corporate Director – Strategic Resources, the Corporate Affairs portfolio holder and the Chairman of the Audit Committee to discuss issues arising from the day to day management of Treasury Management activities;

(f) copies of the reports mentioned in (a) to (d) above are provided to the **Audit Committee** who are also consulted on any proposed changes to the Council's Treasury Management activities.

## 15.0 SUMMARY OF KEY ELEMENTS OF THIS STRATEGY

15.1 For the financial year 2016/17 the Council approves the following:-

(a) an Authorised Limit for external debt of £373.5m in 2016/17;

(b) an Operational Boundary for external debt of £353.5m in 2016/17;

(c) a borrowing limit on fixed interest exposures of between 60% to 100% of outstanding principal sums and a limit on variable interest rate exposures of between 0 to 40% of outstanding principal sums;

(d) borrowing from the money market for capital purposes is to be limited to 30% of external debt outstanding at any one point in time;

(e) an investment limit on fixed interest exposures of 0 to 30% of outstanding principal sums and a limit on variable interest rate exposure of between 70% to 100% of outstanding principal sums;

(f) a limit of £20m of the total ‘core’ cash sums available for investment (both in house and externally managed) to be invested in Non-Specified investments over 364 days;

(g) a 10% cap on capital financing costs as a proportion of the annual Net Revenue Budget;

(h) a Minimum Revenue Provision (MRP) policy for debt repayment to be charged to Revenue in 2016/17 as set out in **Section 11**;

(i) the Corporate Director – Strategic Resources to report to the Council if and when necessary during the year on any changes to this Strategy arising from the use of operational leasing, PFI or other innovative methods of funding.

GARY FIELDING
Corporate Director – Strategic Resources
19 January 2016

**SCHEDULE A**

## NORTH YORKSHIRE COUNTY COUNCIL ANNUAL INVESTMENT STRATEGY 2016/17 – SPECIFIED INVESTMENTS

| Investment | Security / Minimum Credit Rating | Circumstances of Use |
|---|---|---|
| **Term Deposits** with the UK Government or with UK Local Authorities ( as per Local Government Act 2003) with maturities up to 1 year | High security as backed by UK Government | In-house |
| **Term Deposits** with credit rated deposit takers (Banks and Building Societies), including callable deposits with maturities less than 1 year | Organisations assessed as having "high credit quality" plus a minimum Sovereign rating of AA- for the country in which the organisation is domiciled | In-house |
| **Certificate of Deposits** issued by credit rated deposit takers (Banks and Building Societies) up to 1 year | | Fund Manager or In-house "buy and hold" after consultation with Treasury Management Advisor |
| **Forward deals** with credit rated Banks and Building Societies less than 1 year (i.e. negotiated deal plus period of deposit) | | In-house |
| **Money Market Funds** i.e. collective investment scheme as defined in SI2004 No 534<br>(*These funds have no maturity date*) | Funds must be AAA rated | In-house<br>After consultation with Treasury Management Advisor<br>Limited to £20m |
| **Gilts** (with maturities of up to 1 year) | Government Backed | Fund Manager or In-house buy and hold after consultation with Treasury Management Advisor |
| **Bonds** issued by a financial institution that is guaranteed by the UK Government (as defined in SI 2004 No 534) with maturities under 12 months<br>(*Custodial arrangements required prior to purchase*) | | After consultation with Treasury Management Advisor |

**SCHEDULE B**

**NORTH YORKSHIRE COUNTY COUNCIL ANNUAL INVESTMENT STRATEGY 2016/17 – NON-SPECIFIED INVESTMENTS**

| investment | A) Why use it?<br><br>B) Associated Risks? | Security / Minimum Credit Rating | Circumstances of Use | Max % of overall investments or cash limits in cash category | Maximum investment with any one counterparty | Maximum Maturity Period |
|---|---|---|---|---|---|---|
| **Term Deposit** with credit rated deposit takers (Banks & Building Societies), UK Government and other Local Authorities with maturities greater than 1 year | A) Certainty of return over period invested which could be useful for budget purposes<br><br>B) Not Liquid, cannot be traded or repaid prior to maturity<br><br>Return will be lower if interest rates rise after making deposit<br><br>Credit risk as potential for greater deterioration of credit quality over a longer period | Organisations assessed as having "high credit quality"<br><br>Plus<br><br>A minimum Sovereign rating of AA- for the country in which an organisation is domiciled | In-house | 100% of agreed maximum proportion (20%) of core cash funds that can be invested for more than 1 year (estimated £20m) | £5m | 2 years subject to potential future review with a maximum of no longer than 5 years |
| **Certificate of Deposit** with credit rated deposit takers (Banks & Building Societies) with maturities greater than 1 year<br><br>*Custodial arrangements prior to purchase* | A) Attractive rates of return over period invested and in theory tradable<br><br>B) Interest rate risk; the yield is subject to movement during life of CD which could negatively impact on its price | | Fund Manager or In-house "buy & hold" after consultation with Treasury Management Advisor | 25% of agreed proportion (20%) of core cash funds that can be invested for more than 1 year<br>(£5m) | £3m | |
| **Callable Deposits** with credit rated deposit takers (Banks & Building Societies) with | A) Enhanced Income – potentially higher return than using a term deposit with a similar maturity | | To be used in-house after consultation with Treasury Management | 50% of agreed proportion (20%) of core cash balance that can be | £5m | |

| investment | A) Why use it?<br><br>B) Associated Risks? | Security / Minimum Credit Rating | Circumstances of Use | Max % of overall investments or cash limits in cash category | Maximum investment with any one counterparty | Maximum Maturity Period |
|---|---|---|---|---|---|---|
| maturities greater than 1 year | B) Not liquid – only borrower has the right to pay back the deposit; the lender does not have a similar call<br><br>Period over which the investment will actually be held is not known at outset<br><br>Interest rate risk; borrower will not pay back deposit if interest rates rise after the deposit is made | | Advisor | invested for more than 1 year<br>(£12.5m) | | |
| **Forward Deposits** with a credit rated Bank or Building Society > 1 year (i.e. negotiated deal period plus period of deposit) | A) Known rate of return over the period the monies are invested – aids forward planning<br><br>B) Credit risk is over the whole period, not just when monies are invested<br><br>Cannot renege on making the investment if credit quality falls or interest rates rise in the interim period | Organisations assessed as having "high credit quality" Plus A minimum Sovereign rating of AA- for the country in which an organisation is domiciled | To be used in-house after consultation with the Treasury Management Advisor | 25% of greed proportion (20%) of core cash funds that can be invested for more than 1 year<br>(£5m) | £3m | 2 years subject to potential future review with a maximum of no longer than 5 years |
| **Bonds issued by a financial institution that is guaranteed by the UK Government** (as defined in SI2004 No534) with maturities in | A) Excellent credit quality<br><br>Relatively Liquid<br><br>If held to maturity, yield is known in advance | AA or Government backed | In-house on a "buy and hold" basis after consultation with Treasury Management Advisor or use by Fund Managers | | n/a | |

| investment | A) Why use it?<br><br>B) Associated Risks? | Security / Minimum Credit Rating | Circumstances of Use | Max % of overall investments or cash limits in cash category | Maximum investment with any one counterparty | Maximum Maturity Period |
|---|---|---|---|---|---|---|
| excess of 1 year<br>Custodial arrangements required prior to purchase | Enhanced rate in comparisons to gilts<br><br>B) Interest rate risk; yield subject to movement during life off bond which could impact on price | | | | | |
| **Bonds issued by Multilateral development banks** (as defined in SI2004 No534) with maturities in excess of 1 year<br>Custodial arrangements required prior to purchase | A) Excellent credit quality<br><br>Relatively Liquid<br><br>If held to maturity, yield is known in advance<br><br>Enhanced rate in comparison to gilts<br><br>B) Interest rate risk; yield subject to movement during life off bond which could negatively impact on price | | | | £3m | |
| **UK Government Gilts** with maturities in excess of 1 year<br>Custodial arrangements required prior to purchase | A) Excellent credit quality<br><br>Liquid<br><br>If held to maturity, yield is known in advance<br><br>If traded, potential for capital appreciation | Government backed | Fund Manager | 25% of greed proportion (20%) of core cash funds that can be invested for more than 1 year (£5m) | n/a | 2 years subject to potential future review with a maximum of no longer |

| investment | A) Why use it?<br><br>B) Associated Risks? | Security / Minimum Credit Rating | Circumstances of Use | Max % of overall investments or cash limits in cash category | Maximum investment with any one counterparty | Maximum Maturity Period |
|---|---|---|---|---|---|---|
| | B) Interest rate risk; yield subject to movement during life if the bond which could impact on price | | | | | than 5 years |
| **Collateralised Deposit** | A) Excellent credit quality<br><br>B) Not liquid, cannot be traded or repaid prior to maturity<br><br>Credit risk as potential for greater deterioration of credit quality over a longer period | Backed by collateral of AAA rated Local Authority LOBO's | In-house via money market broker or direct | 100% of agreed proportion (20%) of core cash funds that can be invested for more than 1 year (£20m) | £5m | |

**SCHEDULE C**

## APPROVED LENDING LIST 2016/17

Maximum sum invested at any time (The overall total exposure figure covers both Specified and Non-Specified investments)

| | Country | Specified Investments (up to 1 year) | | Non-Specified Investments (> 1 year £20m limit) | |
|---|---|---|---|---|---|
| | | Total Exposure £m | Time Limit * | Total Exposure £m | Time Limit * |
| **UK "Nationalised" banks / UK banks with UK Central Government involvement** | | | | | |
| Royal Bank of Scotland | GBR | 85.0 | 364 days | - | - |
| Natwest Bank | GBR | | | | |
| Bank of Scotland | GBR | 85.0 | 6 months | - | - |
| Lloyds | GBR | | | | |
| **UK "Clearing Banks", other UK based banks and Building Societies** | | | | | |
| Santander UK plc (includes Cater Allen) | GBR | 40.0 | 6 months | - | - |
| Barclays Bank | GBR | 75.0 | 6 months | - | - |
| HSBC | GBR | 30.0 | 364 days | | |
| Clydesdale Bank (trading as Yorkshire Bank) | GBR | 30.0 (Shared with NAB) | Temporarily suspended | - | - |
| Goldman Sachs International Bank | GBR | 40.0 | 6 months | | |
| Nationwide Building Society | GBR | 40.0 | 6 months | - | - |
| Leeds Building Society | GBR | 20.0 | 6 months | - | - |
| **High quality Foreign Banks** | | | | | |
| National Australia Bank | AUS | 30.0 (Shared with Clydesdale) | 364 days | - | - |
| Commonwealth Bank of Australia | AUS | 20.0 | 364 days | | |
| Canadian Imperial Bank of Commerce | CAN | 20.0 | 364 days | - | - |
| Deutsche Bank | DEU | 20.0 | Temporarily suspended | - | - |
| Nordea Bank Finland | FIN | 20.0 | 364 days | - | - |
| Credit Industriel et Commercial | FRA | 20.0 | 364 days | - | - |
| BNP Paribas Fortis | FRA | 20.0 | 6 months | - | - |
| Nordea Bank AB | SWE | 20.0 | 364 days | - | - |
| Svenska Handelsbanken | SWE | 40.0 | 364 days | - | - |
| **Local Authorities** | | | | | |
| County / Unitary / Metropolitan / District Councils | | 20.0 | 364 days | 5.0 | 2 years |
| Police / Fire Authorities | | 20.0 | 364 days | 5.0 | 2 years |
| National Park Authorities | | 20.0 | 364 days | 5.0 | 2 years |
| **Other Deposit Takers** | | | | | |
| Money Market Funds | | 20.0 | 364 days | 5.0 | 2 years |
| UK Debt Management Account | | 100.0 | 364 days | 5.0 | 2 years |

* Based on data as 8 January 2016

**SCHEDULE D**

## APPROVED COUNTRIES FOR INVESTMENTS

Based on the lowest available rating

| Sovereign Rating | Country |
|---|---|
| AAA | Australia<br>Canada<br>Denmark<br>Germany<br>Netherlands<br>Singapore<br>Sweden<br>Switzerland |
| AA+ | FinlandUK<br>USA |
| AA | Abu Dhabi (UAE)<br>France<br>Qatar |
| AA- | Belgium |