Appendix 2 - Treasury Management Strategy - updated

Treasury Management Policy Statement, Treasury Management Strategy Statement and Annual Investment Strategy for 2017-18

1. Treasury Management Policy Statement

Chichester District Council defines its treasury management activities as:

- The management of the organisation's financial 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.

- The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

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

- The investment policy objective for this Council is the prudent investment of its treasury balances. The Council's investment priorities are security of capital and liquidity of its investments so that funds are available for expenditure when needed. Both the CIPFA Code and the DCLG guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield..

- The Council's borrowing objective, being debt free and with relatively substantial resources still available for its capital investment spending plans, means that it does not intend to borrow any monies, except for short term cash flow purposes for revenue and capital commitments.

- The generation of investment income to support the Council's spending plans is an important, but secondary objective. Other than the income from the Council's investment in the Local Authority property Fund or other long term pooled funds, returns are generally used to fund one-off expenditure or capital investment.

2. **Treasury Management Strategy Statement**

In February 2012 the Council adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2011 Edition* (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year.

The Department for Communities and Local Government (CLG) has also issued revised *Guidance on Local Authority Investments* in March 2010 that requires the Council to approve an investment strategy before the start of each financial year.

This report fulfils the Council's legal obligation under the *Local Government Act 2003* to have regard to both the CIPFA Code and the CLG Guidance.

The Treasury Management Strategy Statement including the Annual Investment Strategy are underpinned by the CIPFA Code of Practice and Treasury Management Practices (TMPs) which provide prescriptive information as to how the treasury management function should be carried out.

In accordance with CLG guidance, the Council will be asked to approve a revised Treasury Management Strategy should the assumptions on which this report is based change significantly. Such circumstances would include, for example, a large unexpected change in interest rates, or in the Council's capital programme or in the level of its investment balances.

3. **Risk Appetite Statement**

As a debt free authority with substantial balances to invest the Council's highest priority in its treasury management function is the security of those investments in accordance with the priorities set out in the CIPFA Code. However, whilst fundamentally risk adverse, the Council will accept some modest degree of risk

The use of different investment instruments and diversified high credit quality counterparties along with country, sector and group limits, as set out in this Strategy, enables the Council to mitigate the nature and extent of any risks. Relevant risks are described in Treasury Management Practices (TMP) 1.

When investing surplus cash, the Council will not necessarily limit itself to making deposits with the UK Government and local authorities, but may invest in other bodies including certain unrated building societies and money market funds. The Council may also invest surplus funds through tradable instruments such as gilts, treasury bills, certificates of deposit, corporate bonds and pooled funds. The duration of such investments will be carefully considered to limit that risk of them having to be sold (although they may be) prior to maturity, mitigating the risk of the capital sum being diminished through price movements.

4. Local Context

On 30 November 2016, the Council held £60.1m of investments, which comprised a diversified range of investments as set out in table 1, below

Table 1: Investment Portfolio Position – 30 November 2016.

Investments	£000	Annualised Return %
Short term Investments (cash, call accounts, deposits)	33,788	0.89
Money Market Funds	7,350	0.43
Corporate Bonds	3,949	0.68
Total Liquid Investments	**45,087**	**0.79**
Medium and Long term Investments	5,000	1.48
Pooled funds – Local Authority Property fund	10,000	4.86
TOTAL INVESTMENTS	**60,087**	**1.27**

The Council monitors the return on its treasury investments against that achieved by other English non-met District Councils. This information is included within the Council's performance management suite of key performance indicators (KPI) maintained on Covalent.

The figure of £60.1m is expected to fall over the next six months due to:

- The Council's projected 2016-17 capital programme (£13.1m)
- Reduced local taxation receipts in February and March.

The Council's latest resource projection (December 2016), projects the following movements in resources, including funds available for investment, over the medium term.

Table 2: Resource projection to 31 March 2021

	31.3.16 Actual £m	31.3.17 Estimate £m	31.3.18 Estimate £m	31.3.19 Estimate £m	31.3.20 Estimate £m	31.3.21 Estimate £m
Reserves:						
Earmarked and specific reserves	14.3	10.7	8.7	8.2	8.0	8.0
New Homes Bonus	6.4	9.4	9.0	8.7	8.4	8.4
Asset Replacement	7.0	4.7	4.5	4.8	4.9	4.8
General Fund	11.9	9.5	5.9	9.8	9.6	9.4
Capital Receipts	0.2	0.1	0.1	0.1	0.1	0.1
Section 106 balances	3.5	3.3	3.1	2.9	2.8	2.8
Working capital	4.7	4.1	3.4	3.7	3.7	3.7
Total Resources	**48.0**	**41.8**	**34.7**	**38.2**	**37.5**	**37.2**

Represented by:

Internal investments	43.0	31.8	24.7	28.2	27.5	27.2
Local Authority Property Fund	5.0	10.0	10.0	10.0	10.0	10.0
Total Investments	**48.0**	**41.8**	**34.7**	**38.2**	**37.5**	**37.2**

	31.3.16	31.3.17	31.3.18	31.3.19	31.3.20	31.3.21
Capital financing requirement	(1.38)	(1.41)	(1.44)	(1.47)	(1.48)	(1.48)
Debt	(0.1)	(0.1)	(0.1)	(0.05)	0	0

Apart from a small lease liability for the Council's multi-function printer/copiers, the Council is currently debt free and its capital expenditure plans do not currently imply any need to borrow over the forecast period. Investments are forecast to fall over the medium term as existing investments are used to finance capital expenditure.

For the purposes of this resource projection, Community Infrastructure Levy (CIL) receipts are not included as they are assumed to be spent in the year of receipt. For Treasury management purposes any timing differences between receipt of sum and payment of planned expenditure is included within the Council's cash-flow forecast and calculation of sums available for short term investment.

CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. As the Council does not expect to incur any debt (other than for temporary cash management purposes) over the next three years, table 2 demonstrates that the Council expects to comply with this recommendation.

5. **Borrowing Strategy**

The Council is currently debt-free and has no borrowing other than that which might occur as part of routine working capital management. This section describes the Council's policy should the need arise for any borrowing to be undertaken.

The Council's Financial Strategy confirms that:

Borrowing could be used for "invest to save" projects providing the cost of servicing the debt is contained within the revenue savings/income the project generates. The payback period for invest to save projects should be shorter than the life of the asset.

There are no plans to borrow to finance new capital expenditure in the current 5 year plan but this remains an option if deemed to be prudent. Short term internal borrowing (for schemes that pay back within the 5 year time frame of the capital programme) can be accommodated without incurring external interest charges, provided the resulting savings are recycled into reserves. Longer term pay back periods will have to accommodate both the external interest and a minimum revenue provision (MRP) in accordance with the Council's MRP policy, which links repayment of the debt to the life of the asset.

Borrowing would add pressure on the revenue budget as MRP and interest would become payable. The capacity to make these payments would need to be identified in advance, namely the further efficiency savings generated by the investment in the assets."

5.1 Borrowing Objective

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

5.2 Borrowing Sources

The Council may need to borrow money in the short term to cover unexpected cash flow shortages, (normally up to one month) within the limits shown in tables 3 and 4.

The approved sources of long-term and short-term borrowing are:

- Public Works Loans Board (PWLB) and any successor body
- Any institution approved for investments (see below)
- Any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except the West Sussex Pension Fund)

In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- Operating and finance leases
- Hire purchase
- Private Finance Initiatives
- Sale and leaseback

5.3 Operational Boundary for External Debt

The operational boundary is based on the Authority's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the Authority's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring.

Table 3: Operational boundary for external debt

Operational Boundary	2016/17 Revised £m	2017/18 Estimate £m	2018/19 Estimate £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m
Borrowing	5	5	5	5	5	5
Other long-term liabilities	0	0	0	0	0	0
Total Debt	5	5	5	5	5	5

5.4 Authorised Limit for External Debt

The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Authority can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

Table 4: Authorised limit for external debt

Authorised Limit	2016/17 Revised £m	2017/18 Limit £m	2018/19 Limit £m	2019/20 Limit £m	2020/21 Limit £m	2021/22 Limit £m
Borrowing	10	10	10	10	10	10
Other long-term liabilities	0	0	0	0	0	0
Total Debt	10	10	10	10	10	10

6. Investment Strategy

The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the 12 months to 30 November 2016, the Council's financial investment balance has ranged between £47.3m and £66.3m, but this is expected to reduce to lower levels in the forthcoming year due to the anticipated capital spending programme including any property investment commitments.

6.1 Investment Objective

The Council has a duty to safeguard the public funds and assets it holds on behalf of its community. Both the CIPFA Code, and the CLG Guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to comply with the principles stated in this strategy document, striking an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk receiving unsuitably low investment income.

6.2 2017-18 Strategy

Given the increasing risk and remaining low returns from short-term unsecured bank investments, the Council will continue to diversify using secure and/or higher yielding asset classes. To achieve this, the Council may invest its surplus funds with any of the counterparties in table 5 below, subject to the cash limits (per counterparty) and time limits shown.

Table 5: Approved Investment Counterparties

Sector Limits/ Credit Rating	Banks Unsecured £20m	Banks Secured Unlimited	Government Unlimited	Corporates £10m
UK Govt	n/a	n/a	£ Unlimited 15 years	n/a
AAA	£2.5m 5 years	£5m 10 years	£5m 10 years	£2.5m 10 years
AA+	£2.5m 5 years	£5m 7 years	£5m 7 years	£2.5m 7 years
AA	£2.5m 4 years	£5m 5 years	£5m 5 years	£2.5m 5 years
AA-	£2.5m 3 years	£5m 4 years	£5m 4 years	£2.5m 4 years
A+	£2.5m 2 years	£5m 3 years	£2.5m 3 years	£2.5m 3 years
A	£2.5m 13 months	£5m 2 years	£2.5m 2 years	£2.5m 2 years
A-	£2.5m 6 months	£5m 13 months	£2.5m 13 months	£2.5m 13 months
BBB+	£1m 100 days	£2.5m 6 months	n/a	£1m 6 months
None (excludes pooled funds)	£1m 6 months	n/a	£5m 10 years	£2m 5 or 10 years
Council's own bank	£2.5m/ 7 days	n/a	n/a	n/a
Pooled Funds	£5m per money market fund (MMF), subject to a maximum of 2% of MMF fund value and a total limit of £20m across all MMF £5m per pooled investment fund, to a maximum of £10m (excludes the Local Authority Property Fund). £10m in the Local Authority Property Fund			

This table must be read in conjunction with the details notes below and the limits stated in table 6

Credit Rating: Investment limits are set by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

Current Account Bank: The Council's current accounts are held with National Westminster Bank plc which is currently rated above the minimum rating in table 5.

Banks Unsecured: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail.

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

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

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

For corporate bonds, the limits referred to in table 5 will apply to the sum of bond principal (par value) and any premium or discount paid to acquire the bond in the secondary market. The limit will exclude the accrued interest element paid to secure a secondary bond as this is recoverable on maturity of the Bond.

Pooled Funds: Shares in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity and very low or no volatility will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

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

Where investments in pooled funds or other financial assets have prices or values that can vary according to fund performance and other factors, the investment limits in table 7 will operate to regulate the initial purchase cost (total initial investment) only.

Risk Assessment and Credit Ratings: Credit ratings are obtained and monitored by the Council's treasury advisors, who will notify changes in the ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

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

If in the case of a decision to recall or sell an investment at a cost which is over the approved virement limits, the Council's urgent action procedure in its Constitution would be invoked by officers.

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

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

When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

Specified Investments: The CLG Guidance defines specified investments as those:

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement,
- not defined as capital expenditure by legislation, and
- invested with one of:
    - the UK Government,
    - a UK local authority, parish council or community council, or
    - a body or investment scheme of "high credit quality".

The Council defines "high credit quality" organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AAA. For clarity, under this Strategy, no sovereign rating criteria for investments made with institutions domiciled in the UK is required. For money market funds and other pooled funds "high credit quality" is defined as those having a credit rating of A- or higher.

Non-specified Investments: Any investment not meeting the definition of a specified investment is classed as non-specified. The Council does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to medium and long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in table 6 below.

Table 6: Non-Specified Investment Limits

	Cash limit
Total medium and long-term investments	£35m
Total investments without credit ratings or rated below A-	£35m
Total non-specified investments	£50m

Investment Limits: The Council's uncommitted revenue reserves available to cover investment losses are forecast to be £26.5m on 31st March 2017. These uncommitted reserves include the following items; General Fund Balance (£9.5m), working capital (£4.1m) and New Homes Bonus (£9.4m). as stated in the current estimated Resources Statement. In order that no more than 25% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government and LAPF) will be £5 million. A group of banks under the same ownership or a group of funds under the same management will be treated as a single organisation for limit purposes. Limits will also be placed on investments in brokers' nominee accounts, foreign countries and industry sectors as set out in Table 7. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Table 7: Investment Limits

	Cash limit
Any single organisation, except the UK Central Government and the Local Authority Property Fund	£5m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£5m per group
Any group of pooled funds (excluding MMF and LAPF) under the same management	£5m per manager (other than the Local Authority Property Fund), to a maximum of £10m in total
Negotiable instruments held in a broker's nominee account	£10m per broker
Foreign countries	£5m per country
Unsecured investments with Building Societies	£5m in total
Loans to unrated corporates	£2m in total
Money Market Funds	£5m per money market fund (MMF), subject to a maximum of 2% of individual MMF fund value and £20m in total
Property Funds (1)	£10m in total

(1) The limit on Property Funds in table 7 does not apply to any element of a multi-asset pooled fund which is subject to the separate limit under 'any group of pooled funds'

Liquidity Management: The Council uses purpose-built cash flow forecasting software to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium term financial plan and cash flow forecast.

7. **Treasury Management Indicators**

The Council measures and manages its exposures to treasury management risks using the following indicators. All comparative data is taken from benchmarking exercises conducted by the Council's Treasury Management advisors.

7.1 Security

The Council will use the following voluntary measures of its exposure to credit risk to monitor and assess overall security

Table 8: Security management indicators

Measure	Target
Average Credit Score (time-weighted)	Less than the average of other District Councils (AAA=1, D=24)*
Average Credit Rating (time weighted)	Maintain below the time weighted average of other District Councils
Proportion Exposed to Bail-in (%)	Less than the average of other District Councils

7.2 Liquidity

The Council has in prior years adopted a voluntary measure of its exposure to liquidity risk by ensuring that £10m is available within a rolling three month period. Following the introduction of specialised treasury management software during 2015-16, this target is no longer considered necessary as the cashflow forecast identifies the Council's cash liquidity requirements.

The Council has, previously, also sought to maintain its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments and minimising the use of its overdraft facility of £350,000. Over the last 12 months, the Council has, in conjunction with its banker, implemented automated balance sweeping arrangements to ensure that, at the close of each business day, surplus funds are automatically moved into an interest bearing account or funding transferred into accounts that are overdrawn. As a result of these arrangements, the voluntary targets referred to above are obsolete when taken together with the specific limits on funds with the Council's banker set out in table 5, above.

Officers will continue to manage the Council's treasury management investments ensuring that sufficient cash is available to accommodate known payments. In the unlikely circumstance that a large unexpected cash payment is required and the

Council does not have sufficient liquidity immediately available, the Council will use its facility to borrow temporarily for cash management purposes as set out in paragraph 5.3.

The Council will use the following voluntary measures of its exposure to liquidity risk

Table 9: Liquidity management indicators

Measure	Target
Proportion of investments available within 7 days (%)	Compare and explain against the average of other District Councils
Proportion available within 100 days (%)	Compare and explain against the average of other District Councils
Average days to maturity	Compare and explain against the average of other District Councils

7.3 Interest Rate Exposures

This indicator is set to control the Council's exposure to interest rate risk. Under the TM Code the upper limits on fixed and variable rate interest rate exposures, should be expressed as the amount or proportion of net principal borrowed or interest payable, with investments counting as negative borrowing. As the Council is debt free and to provide a meaningful indicator the limits on fixed and variable rate interest rate exposures are expressed as an amount in £ and percentage of net principal invested. Any borrowing would count as negative investment. Strictly this is contrary to the TM Code definition.

Table 10: Interest rate exposure management indicators

	2017/18	2018/19	2019/20
Upper limit on fixed interest rate exposure	£28m or 40%	£24m or 40%	£22m or 40%
Upper limit on variable interest rate exposure	£70m or 100%	£60m or 100%	£55m or 100%

Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. All other instruments are classed as variable rate.

7.4 Maturity Structure of Borrowing

As the Council is debt free it currently holds no fixed long term borrowing for which a maturity profile exists.

7.5 Principal Sums Invested for Periods Longer than 364 days

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments in response to adverse economic or market conditions or credit rating downgrades. The limits on the long-term principal sum invested to final maturities beyond the period end will be:

Table 11: Limits on investment periods

	2017/18	2018/19	2019/20
Limit on principal invested beyond year end	£35m	£30m	£25m

8. Other Items

There are a number of additional items that the Council is obliged by CIPFA or CLG to include in its Treasury Management Strategy.

8.1 Policy on Use of Financial Derivatives

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

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

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

8.2 Investment Training

Member and officer training is an essential requirement in terms of understanding roles, responsibilities and keeping up to date with changes and in order to comply with the CIPFA Treasury Management Code of Practice.

The training needs of the officers involved on treasury management are identified through the annual performance and development appraisal process, and additionally when the responsibilities of individual members of staff change. Staff attend relevant training courses, seminars and conferences.

To address the training need of members, training will be provided to members of both Cabinet and the Corporate Governance and Audit Committee in advance of them considering the forthcoming year's strategies. The training was provided by the Council's treasury adviser in January 2017.

Staff regularly attend training courses, seminars and conferences provided by Arlingclose and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA, the Association of Corporate Treasurers and other appropriate organisations.

8.3 Investment Advisers

The Council currently contracts with Arlingclose Limited as its treasury management adviser and receives specific advice on investment, debt and capital finance issues. However, responsibility for final decision making remains with the Council and its officers.

The quality of this service is controlled and monitored against the contract by the Accountancy Services Manager, which is in place until the 30th June 2018.

8.4 Investment of Money Borrowed in Advance of Need

Although not envisaged at this stage, the Council may, from time to time, borrow in advance of need, where this is expected to provide the best long term value for money. Since amounts borrowed will be invested until spent, the Council is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Council's overall management of its treasury risks.

The total amount borrowed will not exceed the authorised borrowing limit of £5 million. The maximum period between borrowing and expenditure is expected to be two years, although the Council is not required to link particular loans with particular items of expenditure.

9. Financial Implications

The budget for investment income in 2017/18 is shown below.

Table 12: Investment income budget

	2017/18 average	Return %	Budget (£k)
Internally managed investments	£27.8m	0.55	153
Local Authority Property Fund	£10.0m	4.20	420
Total	£37.8m	1.38	573

The above are based on cash flow projections from the Council's resource statement and on the assumption that the base interest rate is maintained at 0.25% during the period. This assumption is the central case scenario projected by the Council's treasury management advisors. Further information about these projections can be found in Appendix 1. If actual levels of investments and actual interest rates differ from those forecast, performance against budget will be correspondingly different.

10. Reporting

The Council/Cabinet will receive as a minimum:

- An annual report on the strategy and plan to be pursued in the coming year and on the need to review the requirements for changes to be made to the Treasury Management Strategy Statement.
- A mid-year review
- An annual report on the performance of the treasury management function, on the effects of decisions taken and the transactions executed in the past year, by 30th September in the next financial year, including any circumstances of non-compliance with the organisation's treasury management policy statement and Treasury Management Practices.

The body responsible for scrutiny, Corporate Governance and Audit Committee has responsibility for the scrutiny of treasury management policies and practices. Monitoring reports on Treasury performance and compliance with this strategy will be prepared and presented to this Committee as a minimum for the half year to September and the full year to March.

The Cabinet member for Finance and Governance, and the members of the Corporate Governance & Audit Committee receive weekly monitoring reports of the investments held. Corporate Governance & Audit Committee will receive half yearly monitoring reports.

Appendix 1 – Arlingclose Economic & Interest Rate Forecast September 2016

External Context

Economic background: The major external influence on the Council's treasury management strategy for 2017/18 will be the UK's progress in negotiating a smooth exit from the European Union. Financial markets, wrong-footed by the referendum outcome, have since been weighed down by uncertainty over whether leaving the Union also means leaving the single market. Negotiations are expected to start once the UK formally triggers exit in early 2017 and last for at least two years. Uncertainty over future economic prospects will therefore remain throughout 2017/18.

The fall and continuing weakness in sterling and the near doubling in the price of oil in 2016 have combined to drive inflation expectations higher. The Bank of England is forecasting that Consumer Price Inflation will breach its 2% target in 2017, the first time since late 2013, but the Bank is expected to look through inflation overshoots over the course of the next few years when setting interest rates so as to avoid derailing the economy.

Initial post-referendum economic data showed that the feared collapse in business and consumer confidence had not immediately led to lower GDP growth. However, the prospect of a leaving the single market has dented business confidence and resulted in a delay in new business investment and, unless counteracted by higher public spending or retail sales, will weaken economic growth in 2017/18.

Looking overseas, with the US economy and its labour market showing steady improvement, the market has priced in a high probability of the Federal Reserve increasing interest rates in December 2016. The Eurozone meanwhile has continued to struggle with very low inflation and lack of momentum in growth, and the European Central Bank has left the door open for further quantitative easing.

The impact of political risk on financial markets remains significant over the next year. With challenges such as immigration, the rise of populist, anti-establishment parties and negative interest rates resulting in savers being paid nothing for their frugal efforts or even penalised for them, the outcomes of Italy's referendum on its constitution (December 2016), the French presidential and general elections (April – June 2017) and the German federal elections (August – October 2017) have the potential for upsets.

Credit outlook: Markets have expressed concern over the financial viability of a number of European banks recently. Sluggish economies and continuing fines for pre-crisis behaviour have weighed on bank profits, and any future slowdown will exacerbate concerns in this regard.

Bail-in legislation, which ensures that large investors including local authorities will rescue failing banks instead of taxpayers in the future, has now been fully implemented in the European Union, Switzerland and USA, while Australia and Canada are progressing with their own plans. The credit risk associated with making unsecured bank deposits has therefore increased relative to the risk of other investment options available to the Council; returns from cash deposits however continue to fall.

Interest rate forecast: The Authority's treasury adviser Arlingclose's central case is for UK Bank Rate to remain at 0.25% during 2017/18. The Bank of England has, however, highlighted that excessive levels of inflation will not be tolerated for sustained periods. Given this view and the current inflation outlook, further falls in the Bank Rate look less likely. A negative Bank Rate is currently perceived by some policymakers to be counterproductive but, although a low probability, cannot be entirely ruled out in the medium term, particularly if the UK enters recession as a result of concerns over leaving the European Union.

Gilt yields have risen sharply, but remain at low levels. The Arlingclose central case is for yields to decline when the Government triggers Article 50. Long-term economic fundamentals remain weak, and the quantitative easing (QE) stimulus provided by central banks globally has only delayed the fallout from the build-up of public and private sector debt. The Bank of England has defended QE as a monetary policy tool, and further QE in support of the UK economy in 2017/18 remains a distinct possibility, to keep long-term interest rates low.

Underlying assumptions:

- The economic trajectory for the UK has been immeasurably altered following the vote to leave the European Union. The long-term position of the UK economy will be largely dependent on the agreements the government is able to secure with the EU and other countries.

- The short to medium-term outlook is somewhat more downbeat due to the uncertainty generated by the result and the forthcoming negotiations (notwithstanding the Olympic and summer feel-good effects). The rapid installation of a new Prime Minister and cabinet lessened the political uncertainty, and the government/Bank of England have been proactive in tackling the economic uncertainty.

- Purchasing Managers Index data, and consumer and business confidence surveys presented a more positive picture for August following the shock-influenced data for July, in line with expectations for an initial overreaction. However, many indicators remain at lower levels than pre-Referendum.

- Over the medium term, economic and political uncertainty will likely dampen investment intentions and tighten credit availability, prompting lower activity levels and potentially a rise in unemployment. These effects will dampen economic growth through the second half of 2016 and in 2017.

- UK Consumer Price Index inflation (currently 0.6% year/year) will rise close to target over the coming year as previous rises in commodity prices and the sharp depreciation in sterling begin to drive up imported material costs for companies.

- The rise in inflation is highly unlikely to prompt monetary tightening by the Bank of England, with policymakers looking through import-led CPI spikes to the negative effects of Brexit on economic activity and, ultimately, inflation.

- There is a debatable benefit to further interest rate cuts (particularly with regard to financial stability). Negative Bank Rate is currently perceived by policymakers to be counterproductive, but there is a possibility of close-to-zero Bank Rate. QE will be used to limit the upward movement in bond yields.

- Following significant global fiscal and monetary stimulus, the short term outlook for the global economy is somewhat brighter than a few months ago. However, financial market volatility is likely at various points because the stimulus has only delayed the fallout from the build-up of public and private sector debt (particularly in developing economies, e.g. China).

Forecast:

- The likely path for Bank Rate is weighted to the downside. The Arlingclose central case is for Bank Rate to remain at 0.25%, but there is a 25% possibility of a drop to close to zero, with a very small chance of a reduction below zero

- Gilt yields will be broadly flat from current levels, although there will likely be much volatility as reports of negotiations between the UK and the remaining EU affect market perceptions of both parties' economic growth potential.

	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Aver-age
Official Bank Rate														
Upside risk	0.0	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.12
Arlingclose Central Case	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Downside risk	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.40

Appendix 2 – Benchmarking Definitions

The benchmarking compares various measures of risk and return, which are calculated as follows:

Investment Value
For most investments the value is the sum initially invested. For external pooled funds (eg; the LAPF), the value is the fund's bid price on the quarter end date multiplied by the number of units held.

Rate of Return
For most investments the return is the effective interest rate, which is also the yield to maturity for bonds. For external funds (LAPF) this is measured on an offer-bid basis less transaction fees. For external pooled funds the income only return excludes capital gains and losses.

Average returns are calculated by weighting the return of each investment by its value. All interest rates are quoted per annum.

Duration
This is the number of days to final maturity. For instant access money market funds, the number of days to final maturity is one.
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Average duration is calculated by weighting the duration of each investment by its value. Higher numbers indicate higher risk.

Credit Risk
Each investment is assigned a credit score, based where possible on its average long-term credit rating from Fitch, Moody's and Standard & Poor's. This is converted to a number, so that AAA=1, AA+=2, etc. Higher numbers therefore indicate higher risk. Unrated local authorities are assigned a score equal to the average score of all rated local authorities.

Average credit risk is measured in two ways. The value-weighted average is calculated by weighting the credit score of each investment by its value. The time-weighted average is calculated by weighting the credit score of each investment by both its value and its time to final maturity. Higher numbers indicate higher risk.