

TELFORD & WREKIN COUNCIL

AUDIT COMMITTEE – 26 JANUARY 2016

CABINET – 25 FEBRUARY 2016

COUNCIL – 3 MARCH 2016

2016/17 TREASURY STRATEGY AND TREASURY UPDATE REPORT

REPORT OF THE CHIEF FINANCE OFFICER (ASSISTANT DIRECTOR: FINANCE & HUMAN RESOURCES)

LEAD CABINET MEMBER – CLLR LEE CARTER

PART A – SUMMARY REPORT

1. SUMMARY OF MAIN PROPOSALS

The report updates members on Treasury Management activities during 2015/16 and details the Treasury Strategy recommended to be adopted for 2016/17

2015/16 Treasury Management Update

The treasury portfolio at the end of December showed overall net indebtedness of £130.4m (borrowing: £159.0m less investments: £28.6m). Base rates have remained at 0.5% all year with the next move expected to be upwards, perhaps in the second half of 2016.

The borrowing strategy for 2015/16 is to use maturing investments to reduce borrowing and then start to take new borrowing within shorter maturities before gradually lengthening maturities. To date, part of our 2 EIP PWLB loans have matured and no new loans have been taken out. Short term borrowing has been used to fund short term cash flow requirements and take advantage of low interest rates.

Commercial Schemes within External Borrowing

	31/03/15 Actual £m	31/03/16 Estimate £m	31/03/17 Estimate £m	31/03/18 Estimate £m	31/03/19 Estimate £m
External Borrowing from 5.1.3	116.613	167.129	220.190	232.288	232.680
Housing Investment programme - Houses	0.000	10.332	40.358	45.742	45.742
Housing Investment programme - PIP	0.025	0.075	6.180	6.180	6.180
Solar Farm	3.692	3.719	3.719	3.719	3.719
PIP	1.611	2.500	14.021	19.021	24.021
External Borrowing excluding Commercial Schemes	111.285	150.503	155.912	157.626	163.018

The investment strategy for 2015/16 is to gain maximum benefit with security of principal sum invested being the primary consideration. The weighted average

return on internal investments at the end of December 2015 was 0.43% compared to a benchmark return for the period of 0.30%. A schedule of short-term investments is shown at Appendix F.

TREASURY STRATEGY

The Council's Treasury Management Strategy is set within the parameters of the relevant statute, guidance and accounting standards which include the Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services and the Prudential Code.

The Council is currently expected to be required to borrow up to £53.1m in 2016/17 based on the current capital programme plans and will adopt a flexible approach to borrowing. In consultation with its treasury management advisors consideration will be given to affordability, maturity profile of existing debt, interest rate and refinancing risk as well as borrowing source, which is primarily expected to be the Public Works Loan Board, but may also include the LGA Municipal bonds Agency, European Investment Bank or commercial sources.

The strategy for any investments will generally be to reduce investments in order to reduce counter-party risk and to reduce net interest costs as longer-term borrowing rates will tend to be greater than we are able to earn on new investments, but we will look to lengthen investment periods, where cash flow permits, to achieve higher interest rates within acceptable risk parameters. Maximum investment levels with counterparties will be set to ensure prudent diversification is achieved whilst recognising that strict investment criteria that the Council applies severely reduces the number of suitable available counterparties and therefore sums with individual counterparties may be up to £15m at any one time. Reduced from £20m in view of the lower level of investment fund and to spread risk.

The report also includes the Council's Minimum Revenue Provision Statement, this has been updated to state the exact policy in use for each borrowing type and will apply from 2015/16. Overall the policy is broadly in line with that previously agreed, however it is being extended to include the Public Finance Initiative (PFI) Agreement and we have changed the way we are charging MRP in respect of historic borrowing. This includes backdating of the adjustments back to the start of the prudential regime. This will produce net savings in 2015/16 of £5.3m, 2016/17 of £5.7m, 2017/18 £5.3m, 2018/19 £2.4m and 2019/20 £2.4m, these remain at broadly this level until 2033/34 before ultimately becoming a cost. If a net present value calculation is done to the savings using the government's green book discount rate, then the present value of the saving is over £50m. This change and saving reflects the time value of money.

The change, particularly in relation to the PFI MRP, will increase the level of borrowing over the medium term as MRP is not set aside out of the revenue budget. By the end of the life of the asset the impact on borrowing is nil.

The report also sets the Prudential Indicators associated with Treasury for 2016/17.

It should be noted that there may be some changes to the Treasury Strategy before it is presented to Cabinet on 26 February as further information becomes available. The final strategy will be circulated to Audit Committee Members for information with any significant changes highlighted.

2. RECOMMENDATIONS

Members are asked to

1. Note the treasury management activities for the first half year,
2. Note the Treasury Management Policy Statement (Appendix A) and
3. Approve the Treasury Strategy, including the Annual Investment Strategy for 2016/17 together with the associated treasury Prudential Indicators and the Minimum Revenue Provision Statement, which will apply from 2015/16 onwards.

3. SUMMARY IMPACT ASSESSMENT

COMMUNITY IMPACT

Do these proposals contribute to specific priority plan objectives?

Yes/ No Maximisation of investment income whilst managing risks and minimising borrowing costs whilst also managing risks helps to support the council's overall financial position and therefore the delivery of all policy objectives.

Will the proposals impact on specific groups of people?

Yes/
No

TARGET COMPLETION / DELIVERY DATE

Part of ongoing Treasury Management Activities within the Treasury Management Strategy and Policy approved by Council.

FINANCIAL/VALUE FOR MONEY IMPACT

Yes/ No Where appropriate these are detailed in the body of the report.

LEGAL ISSUES

Yes/ No The Council's Treasury Strategy has to comply with the relevant statute, codes and guidance which are set out both in the main body of this report and Appendices A and C of the strategy itself (Attached).

The Assistant Director: Finance & Human Resources (Section 151 Officer) has responsibility for the administration of the financial affairs of the Council. In providing this report the Assistant Director: Finance & Human Resources is meeting one of the responsibilities of the post contained within the Council's Constitution at Part 2, Article 12, paragraph 12.04(f) which states "The Chief financial Officer will contribute to the promotion and maintenance of high standards of governance, audit, probity and propriety, risk management and the approval of the statement of accounts through provision of support to the Audit Committee."

OTHER IMPACTS, RISKS AND OPPORTUNITIES

Yes/ No The key opportunities and risks associated with treasury management activities are set out in the body of the report and in the Treasury Management Strategy and Policy approved by Council and will be regularly monitored throughout the year.

IMPACT ON SPECIFIC WARDS

Yes/
No

PART B – ADDITIONAL INFORMATION

4. 2015/16 TREASURY MANAGEMENT UPDATE

4.1 CURRENT PORTFOLIO POSITION

	31 March 15	31 Dec 15
	Principal	Principal
	£m	£m
Fixed Rate Borrowing - PWLB	28.520	28.020
Fixed Rate Borrowing - LOBO	60.000	60.000
Variable Rate Borrowing - market	<u>28.093</u>	<u>71.000</u>
Total Debt	116.613	159.020
Investments - in-house	<u>3.778</u>	<u>28.601</u>
Total Investments	3.778	28.601
Net Indebtedness	112.835	130.419

4.2 INTEREST RATES

Base rates began the year at 0.5% and have remained unchanged all year. The Bank of England Quantitative Easing programme remained at £375bn. The next move in the base rate is expected to be upwards, some time in the second half of 2016 and will be strongly linked to the recovery of the economy.

4.3 BORROWING & RESCHEDULING

The borrowing strategy for the current year has been to borrow temporarily to take advantage of low interest rates where possible and to undertake new longer term borrowing initially in shorter maturities before gradually extending maturities.

Rescheduling

During 2015/16 no rescheduling has taken place as market conditions have not been favourable, however the scope for opportunities is regularly monitored.

New Borrowing

Between the period 1 June 2015 (previous Member update) and 31 December 2015, £199.8m of temporary loans have been raised in order to fund short-term cash flow requirements at various points. Interest rates have ranged from 0.28% to 0.53% - interest rates have remained fairly low during this time. £71.0m of this temporary borrowing was outstanding at 31 December 2015. No long term borrowing has been undertaken in the year to date.

4.4 INVESTMENTS

The strategy for the current year is: The Authority's objective when investing money is to strike an appropriate balance between risk and return.

4.4.1 In-House Investments

The majority of the Council's investments are internally managed – currently just temporary investments for cash flow purposes.

Temporary Investments

All the funds are invested by the Council's own officers in order to maximise returns from day to day cash flows

In total £1,443m of investments were placed between 1 June and 31 December. Interest rates have ranged from 0.35% to 0.45% and periods ranged from overnight deposits to 38 days. £28.601m in house temporary investments were held at 31 December 2015.

Longer Term Investments

A number of internally managed deposits have been made previously. We currently hold no longer term investments.

It should be noted that under the current guidance from our Treasury Advisors our investment policy would mean that new investments should not be placed for longer than 13 months.

Overall the weighted average return on all internal investments for the year to date was 0.43% compared to a benchmark return for the period of 0.30%.

4.4.2 Overall Position and Exposure

A full analysis of all Council investments at the end of December is shown in Appendix F.

Our current counterparty limit and maximum exposure is £20.0m for the current year with any one counterparty. At the end of December the greatest exposure with a single counterparty was £10.7m with Lloyds Bank (37% of the total portfolio).

The Council is guided by its Treasury advisers, Arlingclose, in assessing investments.

4.5 LEASING

Each year the Council arranges operating and finance leases for assets such as vehicles, computers and equipment. This helps to spread the cost over a number of years.

The first drawdown for 2015/16 was completed in October. The drawdown from both Lloyds Bank and Cranmer Lawrence totalled £0.439m and funded the purchase of equipment over three and five years at interest rates of 1.20% and 1.42% respectively. A further lease drawdown is anticipated in March.

5. TREASURY STRATEGY FOR 2016/17 to 2018/19

5.1 BACKGROUND

5.1.1 The CIPFA Treasury Management Code of Practice

The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators on an annual basis. The TMSS also incorporates the Annual Investment Strategy as required under the CLG's Investment Guidance.

The purpose of this TMSS is, therefore, to approve the:

- Treasury Management Strategy for 2016/17
- Annual Investment Strategy for 2016/17
- Prudential Indicators for 2016/17, 2017/18, 2018/19 and 2019/20
- MRP Statement.

Treasury Management is about the management of risk. The Authority is responsible for its treasury decisions and activity. No treasury management activity is without risk.

The Authority has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Authority's treasury management strategy.

As per the requirements of the Prudential Code, the Authority adopted the CIPFA TM Code at a meeting of Full Council on 4 March 2010. In addition, the Department for Communities and Local Government (CLG) issued revised Guidance on Local Authority Investments in March 2010 that requires the Authority to approve an investment strategy before the start of each financial year.

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

All treasury activity will comply with relevant statute, guidance and accounting standards.

The strategy takes into account the impact of the Council's Revenue Budget and Capital Programme on the Balance Sheet position, the current and projected Treasury position (Appendix B), the Prudential Indicators (Appendix C) and the outlook for interest rates (Appendix D).

5.1.2 External Context

Economic background: Domestic demand has grown robustly, supported by sustained real income growth and a gradual decline in private sector savings. Low oil and commodity prices were a notable feature of 2015, and contributed to annual CPI inflation falling to 0.1% in October. Wages are growing at 3% a year, and the unemployment rate has dropped to 5.4%. Mortgage approvals have risen to over 70,000 a month and annual house price growth is around

3.5%. These factors have boosted consumer confidence, helping to underpin retail spending and hence GDP growth, which was an encouraging 2.3% a year in the third quarter of 2015. Although speeches by the Bank of England's Monetary Policy Committee (MPC) members sent signals that some were willing to countenance higher interest rates, the MPC held policy rates at 0.5% for the 81st consecutive month at its meeting in November 2015. Quantitative easing (QE) has been maintained at £375bn since July 2012.

The outcome of the UK general election, which was largely fought over the parties' approach to dealing with the deficit in the public finances, saw some big shifts in the political landscape and put the key issue of the UK's relationship with the EU at the heart of future politics. Uncertainty over the outcome of the forthcoming referendum could put downward pressure on UK GDP growth and interest rates.

China's growth has slowed and its economy is performing below expectations, reducing global demand for commodities and contributing to emerging market weakness. US domestic growth has accelerated but the globally sensitive sectors of the US economy have slowed. Strong US labour market data and other economic indicators however suggest recent global turbulence has not knocked the American recovery off course. The Federal Reserve increased its policy rates at its meeting in December 2015. In contrast, the European Central Bank finally embarked on QE in 2015 to counter the perils of deflation.

Credit outlook: The varying fortunes of different parts of the global economy are reflected in market indicators of credit risk. UK Banks operating in the Far East and parts of mainland Europe have seen their perceived risk increase, while those with a more domestic focus continue to show improvement. The sale of most of the government's stake in Lloyds and the first sale of its shares in RBS have generally been seen as credit positive.

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 UK, USA and Germany. The rest of the European Union will follow suit in January 2016, while Australia, Canada and Switzerland are well advanced with their own plans. Meanwhile, changes to the UK Financial Services Compensation Scheme and similar European schemes in July 2015 mean that most private sector investors are now partially or fully exempt from contributing to a bail-in. The credit risk associated with making unsecured bank deposits has therefore increased relative to the risk of other investment options available to the Authority; returns from cash deposits however remain stubbornly low.

Interest rate forecast: The Authority's treasury advisor Arlingclose projects the first 0.25% increase in UK Bank Rate in the third quarter of 2016, rising by 0.5% a year thereafter, finally settling between 2% and 3% in several years' time. Persistently low inflation, subdued global growth and potential concerns over the UK's position in Europe mean that the risks to this forecast are weighted towards the downside.

A shallow upward path for medium term gilt yields is forecast, as continuing concerns about the Eurozone, emerging markets and other geo-political events weigh on risk appetite, while inflation expectations remain subdued. Arlingclose projects the 10 year gilt yield to rise from its current 2.0% level by around 0.3% a year. The uncertainties surrounding the timing of UK and US interest rate rises are likely to prompt short-term volatility in gilt yields.

5.1.3 Local Context

The Authority's current level of debt and investments is set out at Appendix B.

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). The CFR, together with Usable Reserves, are the core drivers of the Authority's Treasury Management activities.

The Authority is able to borrow funds in excess of the current level of its CFR up to the projected level in 2019/20. The Authority is likely to only borrow in advance of need if it felt the benefits of borrowing at interest rates now compared to where they are expected to be in the future, outweighs the current cost and risks associated with investing the proceeds until the borrowing was actually required.

The forecasted movement in the CFR in coming years is one of the Prudential Indicators (PIs). The movement in actual external debt and usable reserves combine to identify the Authority's borrowing requirement and potential investment strategy in the current and future years.

The estimates, based on the current Revenue Budget and Capital Programmes, are:

	31/03/15 Actual £m	31/03/16 Estimate £m	31/03/17 Estimate £m	31/03/18 Estimate £m	31/03/19 Estimate £m
Capital Financing Requirement	295.535	351.956	407.229	421.653	421.824
Less: Other long term liabilities (e.g. PFI)	-58.964	-57.813	-58.260	-56.408	-54.167
Borrowing CFR	236.571	294.143	348.969	365.245	367.657
Less: External Borrowing	-116.613	-167.129	-220.190	-232.288	-232.680
Internal Borrowing	119.958	127.014	128.779	132.957	134.977
Less: Usable reserves	-63.343	-63.343	-63.343	-63.343	-63.343
Less: Working capital	-52.837	-63.671	-65.436	-69.614	-71.634
Investments	3.778	0.000	0.000	0.000	0.000

Commercial Schemes within External Borrowing

External Borrowing from Above	116.613	167.129	220.190	232.288	232.680
Housing Investment programme - Houses	0.000	10.332	40.358	45.742	45.742
Housing Investment programme - PIP	0.025	0.075	6.180	6.180	6.180
Solar Farm	3.692	3.719	3.719	3.719	3.719
PIP	1.611	2.500	14.021	19.021	24.021
External Borrowing excluding Commercial Schemes	111.285	150.503	155.912	157.626	163.018

The table above shows an increasing Capital Financing Requirement and will require the Council to undertake additional longer term borrowing as well as converting from temporary borrowing we currently hold to fixed borrowing at the best time for the Council dependent on market conditions.

The row relating to external borrowing includes debt associated with funding the Council's proposed Housing Investment Programme together with associated PIP development and other commercial investments in 2015/16. The projected income from these projects is projected to generate a surplus after funding the debt and operational costs. The outstanding debt relating to the Housing Investment Programme will be repaid by the eventual sale of some or all of the properties held by the Council's wholly owned company. The proceeds of any partial disposals will be used to reduce the outstanding debt until the whole amount of debt used to fund the investment has been repaid.

5.1.4 Borrowing Strategy

The Authority currently holds £159.020 million of loans, an increase of £42.4 million on the previous year end. The Council also holds £57.813 million of other longer term liabilities (mainly PFI). The balance sheet forecast in the above table shows that the Authority expects borrowing to increase by year end and continue to increase over the next few years until capital receipts are realised. The Authority may however borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing.

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

Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow using short-term loans instead.

By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. Whilst such a strategy is most likely to be beneficial over the next 1-2 years as official interest rates remain low, it is unlikely to be sustained in the medium-term. The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. Arlingclose will assist the Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2016/17 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

The Authority will also evaluate forward-fixing long-term loans which start at a date in the future, say 12-36 months ahead. Such loans benefit the Authority by fixing a known rate for future borrowing commitments without incurring the funding cost in the intervening period.

In addition, the Authority may borrow short-term loans to cover exceptional cash flow shortages.

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

- Public Works Loan Board and any successor body
- LGA Bond Agency
- UK local authorities, including Fire and Police Authorities
- any institution approved for investments (see below)
- any other bank or building society authorised by the Prudential Regulation Authority to operate in the UK
- UK public and private sector pension funds
- capital market bond investors
- European Investment Bank
- Local Authority Capital Finance Company and other special purpose companies created to enable joint local authority bond issues.

The Authority has previously raised a significant part of its long-term borrowing from the Public Works Loan Board, but it continues to investigate other sources of finance, such as local authority loans and bank loans, that may be available at more favourable rates.

LGA Bond Agency: UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities may be required to provide bond investors with a joint and several guarantee over the very small risk that other local authority borrowers default on their loans; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to full Council.

LOBOs: The Authority holds £60m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate as set dates, following which the Authority has the option to either accept the new rate or to repay the loan at no additional cost. £55m of these LOBOS have options during 2016/17, and although the Authority understands that lenders are unlikely to exercise their options in the current low interest rate environment, there remains an element of refinancing risk, which will arise at some point in the future when interest rates increase. The Authority will take the option to repay LOBO loans at no cost if it has the opportunity to do so. Total borrowing via LOBO loans will be limited to £60m. Short-term and variable rate loans leave the Authority exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators below.

Debt Rescheduling: The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Some bank lenders may also be prepared to negotiate premature redemption terms. The Authority may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall saving or reduction in risk. Treasury management and borrowing strategies in particular continue to be influenced not only by the absolute level of borrowing rates but also the relationship between short and long term interest rates. The interest rate forecast provided in Appendix D indicates that an acute difference between short and longer term interest rates is expected to continue. This difference creates a "cost of carry" for any new longer term borrowing where the proceeds are temporarily held as investments because of the difference between what is paid on the borrowing and what is earned on the investment. Whilst the cost of carry can be assumed to be a reasonably short-term issue since borrowing is often for longer dated periods (anything up to 50 years) it cannot be ignored against a backdrop of uncertainty and affordability constraints in the Authority's wider financial

position.

5.2 Investment Strategy

The Authority holds invested funds, representing income received in advance of expenditure plus balances and reserves. In the past 12 months, the Authority's investment balance has ranged between £4 million and £38 million, and levels are expected to reduce in the forthcoming year now that long term investments have matured and been used to avoid/reduce borrowing.

Both the CIPFA Code and the CLG Guidance require the Authority 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 Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

The Authority may invest its surplus funds with any of the counterparties in table 2 below, subject to the cash and time limits shown.

Approved Investment Counterparties

Credit Rating	Banks Unsecured	Banks Secured	Government	Corporates	Registered Providers
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£15m 5 years	£15m 20 years	£15m 50 years	£7.5m 20 years	£15m 20 years
AA+	£15m 5 years	£15m 10 years	£15m 25 years	£7.5 m 10 years	£15m 10 years
AA	£15m 4 years	£15m 5 years	£15m 15 years	£7.5m 5 years	£15m 10 years
AA-	£15m 3 years	£15m 4 years	£15m 10 years	£7.5m 4 years	£15m 10 years
A+	£15m 2 years	£15m 3 years	£15m 5 years	£7.5m 3 years	£15m 5 years
A	£15m 13 months	£15m 2 years	£15m 5 years	£7.5m 2 years	£15m 5 years
A-	£15m 6 months	£15m 13 months	£15m 5 years	£7.5m 13 months	£15m 5 years
BBB+	£7.5m 100 days	£7.5m 6 months	£7.5m 2 years	£4m 6 months	£7.5m 2 years
BBB	£4m next day only	£4m 100 days	n/a	n/a	n/a
None	£0m 6 months	n/a	£4m 25 years	£1,000 5 years	£0m 5 years
Pooled funds	£10m per fund				

There is no intention to restrict investments to bank deposits, and investments may be made with any public or private sector organisations that meet the above credit rating criteria. The table reflects a lower likelihood that the UK and other governments will support failing banks as the bail-in provisions in the Banking Reform Act 2015 and the EU Bank Recovery and Resolution Directive are implemented.

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

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

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

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

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

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

Pooled Funds: Shares in diversified investment vehicles consisting of any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Money Market Funds that offer same-day liquidity and 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 may 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 Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.

Risk Assessment and Credit Ratings: Credit ratings are obtained and monitored by the Authority's treasury advisers, who will notify changes in 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.

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 on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Other Information on the Security of Investments: The Authority understands that credit ratings are good, but not perfect, predictors of investment default. Regard will therefore be given to other available information on the credit quality of the organisations in which it invests as advised by our treasury advisors, 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 our Treasury Advisors have raised 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 Authority 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 Authority’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 Authority defines “high credit quality” organisations 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 AA+ or higher. 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 Authority 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 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 3 below.

The Council's purchase of shares in the Housing Wholly Owned Company (and any other wholly owned company) and subsequent loans to the company are service-related and are not included in the annual investment strategy.

Table 3: Non-Specified Investment Limits

	Cash limit
Total long-term investments	£25m
Total investments without credit ratings or rated below A-	£5m
Total investments (except pooled funds) in foreign countries rated below AA+	£5m
Total non-specified investments	£30m

It should be noted that the authority has an historic investment in Shropshire Waste Management shares totalling £33k which was transferred when the Unitary authority was created in 1998.

Investment Limits: The Authority has revenue reserves, which could be used to cover investment losses and are forecast to be £63 million on 31st March 2016 although not all of these are available. In order that no more than 50% of reserves (as recommended by the code) 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) will be £15 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 (e.g. King & Shaxson), foreign countries and industry sectors as below:

Approved Instruments: The Authority may lend or invest money using any of the following instruments:

- interest-bearing bank accounts,
- fixed term deposits and loans,
- callable deposits and loans where the Authority may demand repayment at any time (with or without notice),
- callable deposits and loans where the borrower may repay before maturity, but subject to a maximum of £5 million in total,
- certificates of deposit,
- bonds, notes, bills, commercial paper and other marketable instruments, and
- shares in money market funds and other pooled funds.

Investments may be made at either a fixed rate of interest, or at a variable rate linked to a market interest rate, such as LIBOR, subject to the limits on interest rate exposures below.

Liquidity management: The Authority uses cash flow forecasting to determine the maximum period for which funds may prudently be committed. The forecast

is compiled on a prudent basis, with receipts under-estimated and payments over-estimated to minimise the risk of the Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium term financial plan and cash flow forecast.

5.3 Ethical Investment

The Council will not knowingly directly invest in organisations whose activities include practices which directly pose a risk of serious harm to individuals or groups, or whose activities are inconsistent with the mission and values of the Council. At the same time the Council will take full responsibility for proper management of risk and safeguarding its investments by ensuring that they are diversified and made with organisations suitably credit assessed.

The Council's lending activity will be subject to (in order of rank)

- The assessment of meeting the minimum lending criteria as specified in the current Treasury Management Strategy and the minimum credit ratings as outlined in the Strategy;
- Meeting the Security, Liquidity & Yield criteria as set out in the current Treasury Management Strategy and Compliance with the Treasury Management Practice Statements;
- And investments are not contrary to the values outlined in the Ethical Investment Framework (Appendix G)

5.4 The Use of Financial Instruments for the Management of Risks

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 Authority 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 Authority 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 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.

5.5 Balanced Budget Requirement

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

5.6 2016/17 MRP Statement

5.6.1 The Local Authorities (Capital Finance and Accounting)(England)(Amendment)

Regulations 08 (SI 08/414) place a duty on local authorities to make a prudent provision for debt redemption. Guidance on Minimum Revenue Provision has been issued by the Secretary of State and local authorities are required to “have regard” to such Guidance under section 21(1A) of the Local Government Act 2003.

5.6.2 The four MRP options available are:

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

NB This does not preclude other prudent methods.

5.6.3 MRP in 2016/17: Options 1 and 2 may be used only for supported expenditure. Methods of making prudent provision for self financed expenditure include Options 3 and 4 (which may also be used for supported expenditure if the Council chooses).

5.6.4 The MRP Statement will be submitted to Council before the start of the 2016/17 financial year. If it is ever proposed to vary the terms of the original MRP Statement during the year, a revised statement should be put to Council at that time.

5.6.5 The Council will calculate MRP by the following methods.

Historic MRP (re pre 2007/08 borrowing). This will be calculated by dividing the balance at 31/3/07 (calculated in accordance with regulations) by 50 for an annual charge that charges over a finite period rather than a 4% reducing balance.

MRP in respect of prudential borrowing, government supported allocations since 2007/08 and PFI will be charged over the life of the asset on an annuity basis (option 3 in the regulations).

The policy in respect of historic borrowing and PFI is a change from current practice and will be applied from 2015/16 onwards. The calculation includes backdating of the adjustments back to the start of the prudential regime. This will produce a net savings in 2015/16 of £5.3m, 2016/17 of £5.7m, 2017/18 £5.3m, 2018/19 £2.4m and 2019/20 £2.4m, these remain at broadly this level until 2033/34 before ultimately becoming a cost. If a net present value calculation is done to the savings using the government’s green book discount rate, then the present value of the saving is over £50m. This change and saving reflects the time value of money.

Also MRP in respect of leases brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability which is broadly in line with the life of the asset.

5.7 Monitoring and Reporting on the Treasury Outturn and Prudential Indicators

The Assistant Director: Finance & Human Resources will report to the Audit Committee on treasury management activity / performance and Performance Indicators as follows:

- half yearly against the strategy approved for the year. The Authority will produce an outturn report on its treasury activity no later than 30th September after the financial year end and an updated report alongside the Treasury Strategy in the last quarter of the financial year.
- Audit Committee will be responsible for the scrutiny of treasury management activity and practices rather than the Budget and Finance Scrutiny Committee.

6 Other Items

6.1 Training

CIPFA's Code of Practice requires the responsible officer to ensure that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Full training will be made available for any new members following Annual Council in May 2016.

Reviewing and addressing training needs: The authority regularly reviews the training needs of its staff involved with treasury management and ensures that staff are appropriately trained.

6.2 Investment Consultants/Treasury Advisors

The Council uses Arlingclose as its external treasury management advisers.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review to ensure the quality of any such service is controlled. During 2015/16 the Council re-tendered the contract for the provision of this service and Arlingclose were successful for a further 3 years, with an extension option.

7. BACKGROUND PAPERS

CIPFA Code of Practice for Treasury Management in Local Authorities
 Temporary Borrowing Records
 PWLB records
 Investment records
 Draft Treasury Strategy provided by Arlingclose
 Local Government Act 2003
 CLG Guidance on Local Authority Investments
 Audit Commission – Risk and Return

Report prepared by
 Bernie Morris, Finance Manager (01952) 383702
 Ken Clarke, Assistant Director: Finance & Human Resources (01952)
 383100.

TREASURY MANAGEMENT POLICY STATEMENT

1. INTRODUCTION AND BACKGROUND

1.1 The Council adopts the key recommendations of CIPFA's Treasury Management in the Public Services: Code of Practice (the Code), as described in Section 5 of the Code.

1.2 Accordingly, the Council will create and maintain, as the cornerstones for effective treasury management:-

- A treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities
- 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.

1.3 The Council 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 its TMPs.

1.4 The Council delegates responsibility for the implementation and monitoring of its treasury management policies and practices to Audit Committee and for the execution and administration of treasury management decisions to Assistant Director: Finance & Human Resources, who will act in accordance with the organisation's policy statement and TMPs and CIPFA's Standard of Professional Practice on Treasury Management.

1.5 The Council nominates Audit Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

2. POLICIES AND OBJECTIVES OF TREASURY MANAGEMENT ACTIVITIES

2.1 The Council defines its treasury management activities as:

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

2.2 This 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.

2.3 This 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 performance measurement techniques, within the context of effective risk management."

2.4 The Council's borrowing will be affordable, sustainable and prudent and consideration will be given to the management of interest rate risk and refinancing risk. The source from which the borrowing is taken and the type of borrowing should allow the Council

transparency and control over its debt. The Council will look to minimise borrowing through the use of maturing investments to fund capital expenditure rather than reinvestment.

2.5 The Council's primary objective in relation to investments remains the security of capital. The liquidity or accessibility of the Authority's investments followed by the yield earned on investments remain important but are secondary considerations. Generally as investments mature they will not be reinvested but be used to minimise borrowing.

APPENDIX B

EXISTING PORTFOLIO PROJECTED FORWARD

	Current Portfolio £m	%	31/3/16 Estimate £m	31/3/17 Estimate £m	31/3/18 Estimate £m	31/3/19 Estimate £m	31/3/20 Estimate £m
External Borrowing:							
Fixed Rate – PWLB	28.0	13	47.1	110.2	122.3	122.7	98.4
Fixed Rate – Market	60.0	28	60.0	60.0	60.0	60.0	60.0
Variable Rate – PWLB	0.0	0	0.0	0.0	0.0	0.0	0.0
Variable Rate – Market	71.0	33	50.0	50.0	50.0	50.0	50.0
Total External Borrowing	159.0	74	167.1	220.2	232.3	232.7	208.4
IFRS Long Term Liabilities:							
PFI	56.9	26	57.3	55.5	53.3	50.9	49.7
Finance Leases	0.9	0	0.9	0.9	0.9	0.9	0.9
Total Gross External Debt	216.8	100	225.3	276.6	286.5	284.5	259.0
Investments:							
<i>Managed in-house</i>							
Short-term monies (Deposits/ monies on call /MMFs)	28.6	100	0.0	0.0	0.0	0.0	0.0
Long-term investments (maturities over 12 months)	0.0	0	0.0	0.0	0.0	0.0	0.0
Total Investments	28.6	100	0.0	0.0	0.0	0.0	0.0
(Net Borrowing Position)/ Net Investment position	(188.2)		(225.3)	(276.6)	(286.5)	(284.5)	(259.0)

Appendix C
Prudential Indicators 2016/17 – 2019/20

1 Background:

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA’s Prudential Code for Capital Finance in Local Authorities (the “CIPFA Prudential Code”) when setting and reviewing their Prudential Indicators.

2. Gross debt and the Capital Financing Requirement:

This is a key indicator of prudence. In order to ensure that over the medium term debt will only be for a capital purpose, the local authority 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 estimates of any additional increases to the capital financing requirement for the current and next two financial years.

The Assistant Director: Finance & Human Resources reports that the authority had no difficulty meeting this requirement in 2015/16, nor are there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

3. Estimates of Capital Expenditure:

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

Capital Expenditure	15/16 Approved £m	15/16 Revised £m	16/17 Estimate £m	17/18 Estimate £m	18/19 Estimate £m	19/20 Estimate £m
Total	110.380	92.469	88.522	37.597	15.293	6.256

**if applicable*

3.2 Capital expenditure will be financed or funded as follows:

Capital Financing	15/16 Approved £m	15/16 Revised £m	16/17 Estimate £m	17/18 Estimate £m	18/19 Estimate £m	19/20 Estimate £m
Capital receipts	25.752	2.868	5.814	7.037	10.810	25.000
Government Grants	25.334	30.332	21.508	15.162	4.091	5.556
Revenue / External contributions	3.879	4.975	8.139	3.300	0.000	0.000
Total Financing	54.965	38.175	35.461	25.499	14.901	30.556
Supported borrowing	1.268	1.398	0.000	0.000	0.000	0.000
Unsupported borrowing	54.147	52.896	53.061	12.098	0.392	-24.300
Total Funding	55.415	54.294	53.061	12.098	0.392	-24.300
Total Financing and Funding	110.380	92.469	88.522	37.597	15.293	6.256

4. Ratio of Financing Costs to Net Revenue Stream:

4.1 This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs. The definition of financing costs is set out in the Prudential Code.

4.2 The ratio is based on costs net of investment income.

Ratio of Financing Costs to Net Revenue Stream	15/16 Approved %	15/16 Revised %	16/17 Estimate %	17/18 Estimate %	18/19 Estimate %	19/20 Estimate %
Total	4.78	4.11	4.89	5.23	5.22	5.19

5. Capital Financing Requirement:

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

Capital Financing Requirement	15/16 Approved £m	15/16 Revised £m	16/17 Estimate £m	17/18 Estimate £m	18/19 Estimate £m	19/20 Estimate £m
Total CFR	363.131	351.956	407.229	421.653	421.824	397.577

6. Actual External Debt:

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

Actual External Debt as at 31/03/15	£m
Borrowing	116.613
Other Long-term Liabilities	58.964
Total	175.577

7. Incremental Impact of Capital Investment Decisions:

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

Incremental Impact of Capital Investment Decisions	15/16 Approved £	16/17 Estimate £	17/18 Estimate £	18/19 Estimate £	19/20 Estimate £m	20/21 Estimate £m
Increase in Band B Council Tax	22.08	25.65	59.06	62.04	54.63	42.36

7.2 The increase in Band B council tax reflects the increases in the provision for Capital Financing Charges of £2.547m by 2020/21 to undertake additional borrowing of £45.304m arising from the proposed capital programme.

8. Authorised Limit and Operational Boundary for External Debt:

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

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

identifies borrowing from other long term liabilities such as finance leases. It is consistent with the Council's existing commitments, its proposals for capital expenditure and financing and its approved treasury management policy statement and practices.

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

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

Authorised Limit for External Debt	15/16 Approved £m	15/16 Revised £m	16/17 Estimate £m	17/18 Estimate £m	18/19 Estimate £m	19/20 Estimate £m
Borrowing	327	327	330	340	340	310
Other Long-term Liabilities	63	63	62	61	60	59
Total	390	390	392	401	400	369

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

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

Operational Boundary for External Debt	15/16 Approved £m	15/16 Revised £m	16/17 Estimate £m	17/18 Estimate £m	18/19 Estimate £m	19/20 Estimate £m
Borrowing	309	309	310	320	320	290
Other Long-term Liabilities	61	61	60	60	59	58
Total	370	370	310	380	379	348

9. Adoption of the CIPFA Treasury Management Code:

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

Adoption of the CIPFA Code of Practice in Treasury Management
--

The Council approved the adoption of the CIPFA Treasury Management Code at its Council meeting on 4 March 2010.

The Council has incorporated the changes from the revised CIPFA Code of Practice into its treasury policies, procedures and practices.

10. Gross Debt and the Capital Finance Requirement

10.1 The purpose of this treasury indicator is to highlight a situation where the Council is planning to borrow in advance of need. If these figures exceed CFR (which they don't) they would indicate we are borrowing in advance of need.

Gross and Net Debt	15/16 Estimated £m	16/17 Authorised £m	17/18 Authorised £m	18/19 Authorised £m	19/20 Authorised £m
Outstanding Borrowing (at nominal value)	167.129	220.190	232.288	232.680	208.380
Other Long-term Liabilities (at nominal value)	57.813	58.260	56.408	54.167	51.848
Gross Debt	224.942	278.450	288.696	286.847	260.228

11. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure:

11.1 These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. This Council calculates these limits on net principal outstanding sums, (i.e. fixed rate debt net of fixed rate investments / total debt net of total investments)

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

Guidance note on quantum of acceptable volatility...

	Existing level (or Benchmark level) at 31/03/15 %	15/16 Approved %	15/16 Revised %	16/17 Estimate %	17/18 Estimate %	18/19 Estimate %	19/20 Estimate %
Upper Limit for Fixed Interest Rate Exposure	100	100	100	100	100	100	100
Upper Limit for Variable Interest Rate Exposure	30	30	30	30	30	30	30
Local Indicator – Upper limit for net variable rate exposure. (Net principal re gross variable rate borrowing and investments divided by gross borrowing plus investments)	70	70	70	70	70	70	70

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

12. Maturity Structure of Fixed Rate borrowing:

12.1 This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to

protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

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

Maturity structure of fixed rate borrowing	Existing level (level at 31/03/15) %	Lower Limit for 16/17 %	Upper Limit for 16/17 %
under 12 months	46 (25)	0	70
12 months and within 24 months	1 (1)	0	30
24 months and within 5 years	1 (3)	0	50
5 years and within 10 years	0 (0)	0	75
10 years and within years	0 (0)	0	75
years and within 30 years	0 (0)	0	75
30 years and within 40 years	9 (13)	0	100
40 years and within 50 years	11 (15)	10	100
50 years and above	31 (43)	15	100

13. Credit Risk:

13.1 The Council considers security, liquidity and yield, in that order, when making investment decisions.

13.2 Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in the Council's assessment of counterparty credit risk.

13.3 The Council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution (minimum A- or equivalent) and its sovereign (minimum AA+ or equivalent for non-UK sovereigns);
- Sovereign support mechanisms;
- Credit default swaps (where quoted);
- Share prices (where available);
- Economic fundamentals, such as a country's net debt as a percentage of its GDP);
- Corporate developments, news, articles, markets sentiment and momentum;
- Subjective overlay.

13.4 The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

14. Upper Limit for total principal sums invested over 364 days:

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

Upper Limit for total principal sums invested over 364 days	15/16 Approved %	15/16 Revised %	16/17 Estimate %	17/18 Estimate %	18/19 Estimate %	19/20 Estimate %
	95	95	95	95	95	95

Appendix D – Arlingclose Economic & Interest Rate Forecast December 2015**Underlying Assumptions:**

- Underlying assumptions:
 - UK economic growth softened in Q3 2015 but remained reasonably robust; the first estimate for the quarter was 0.5% and year-on-year growth fell slightly to 2.3%. Negative construction output growth offset fairly strong services output, however survey estimates suggest upwards revisions to construction may be in the pipeline.
 - Household spending has been the main driver of GDP growth through 2014 and 2015 and remains key to growth. Consumption will continue to be supported by real wage and disposable income growth.
 - Annual average earnings growth was 3.0% (including bonuses) in the three months to August. Given low inflation, real earnings and income growth continue to run at relatively strong levels and could feed directly into unit labour costs and households' disposable income. Improving productivity growth should support pay growth in the medium term. The development of wage growth is one of the factors being closely monitored by the MPC.
 - Business investment indicators continue to signal strong growth. However the outlook for business investment may be tempered by the looming EU referendum, increasing uncertainties surrounding global growth and recent financial market shocks.
 - Inflation is currently very low and, with a further fall in commodity prices, will likely remain so over the next 12 months. The CPI rate is likely to rise towards the end of 2016.
 - China's growth has slowed and its economy is performing below expectations, which in turn will dampen activity in countries with which it has close economic ties; its slowdown and emerging market weakness will reduce demand for commodities. Other possible currency interventions following China's recent devaluation will keep sterling strong against many global currencies and depress imported inflation.
 - Strong US labour market data and other economic indicators suggest recent global turbulence has not knocked the American recovery off course. Although the timing of the first rise in official interest rates remains uncertain, a rate rise by the Federal Reserve seems significantly more likely in December given recent data and rhetoric by committee members.
 - Longer term rates will be tempered by international uncertainties and weaker global inflation pressure.

Forecast:

- Arlingclose forecasts the first rise in UK Bank Rate in Q3 2016. Further weakness in inflation, and the MPC's expectations for its path, suggest policy tightening will be pushed back into the second half of the year. Risks remain weighted to the downside. Arlingclose projects a slow rise in Bank Rate, the appropriate level of which will be lower than the previous norm and will be between 2 and 3%.

- The projection is for a shallow upward path for medium term gilt yields, with continuing concerns about the Eurozone, emerging markets and other geo-political events, weighing on risk appetite, while inflation expectations remain subdued.
- The uncertainties surrounding the timing of UK and US monetary policy tightening, and global growth weakness, are likely to prompt short term volatility in gilt yields.

	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18
Official Bank Rate													
Upside risk		0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50	1.75	1.75
Downside risk				-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-1.00	-1.00	-1.25	-1.25
3-month LIBID rate													
Upside risk	0.20	0.30	0.30	0.30	0.35	0.35	0.35	0.35	0.40	0.40	0.40	0.40	0.40
Arlingclose Central Case	0.55	0.60	0.70	0.80	0.95	1.05	1.15	1.30	1.40	1.55	1.65	1.80	1.85
Downside risk		-0.20	-0.30	-0.45	-0.55	-0.65	-0.80	-0.90	-1.05	-1.10	-1.20	-1.20	-1.20
1-yr LIBID rate													
Upside risk	0.25	0.35	0.35	0.35	0.40	0.40	0.40	0.40	0.45	0.45	0.45	0.45	0.45
Arlingclose Central Case	1.10	1.20	1.35	1.45	1.55	1.70	1.80	1.95	2.00	2.10	2.15	2.15	2.15
Downside risk	-0.15	-0.25	-0.35	-0.50	-0.60	-0.70	-0.85	-0.95	-1.10	-1.15	-1.25	-1.25	-1.25
5-yr gilt yield													
Upside risk	0.40	0.50	0.50	0.50	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60
Arlingclose Central Case	1.50	1.55	1.60	1.70	1.80	1.90	2.00	2.10	2.20	2.25	2.30	2.35	2.35
Downside risk	-0.35	-0.45	-0.55	-0.60	-0.70	-0.80	-0.90	-1.00	-1.10	-1.15	-1.20	-1.25	-1.25
10-yr gilt yield													
Upside risk	0.40	0.50	0.50	0.50	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60
Arlingclose Central Case	2.00	2.05	2.10	2.20	2.30	2.40	2.50	2.60	2.65	2.70	2.75	2.80	2.80
Downside risk	-0.35	-0.45	-0.55	-0.60	-0.70	-0.80	-0.90	-1.00	-1.10	-1.15	-1.20	-1.25	-1.25
20-yr gilt yield													
Upside risk	0.40	0.50	0.50	0.50	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60
Arlingclose Central Case	2.45	2.50	2.55	2.55	2.60	2.65	2.70	2.75	2.80	2.85	2.90	2.95	2.95
Downside risk	-0.30	-0.40	-0.50	-0.55	-0.65	-0.75	-0.85	-0.95	-1.05	-1.10	-1.15	-1.20	-1.20
50-yr gilt yield													
Upside risk	0.40	0.50	0.50	0.50	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60
Arlingclose Central Case	2.45	2.50	2.55	2.60	2.65	2.70	2.75	2.80	2.85	2.90	2.95	3.00	3.00
Downside risk	-0.25	-0.35	-0.45	-0.50	-0.60	-0.70	-0.80	-0.90	-1.00	-1.05	-1.10	-1.15	-1.15

Appendix E – Recommended Sovereign and Counterparty List (Section 8)

- **Group Limits** - For institutions within a banking group, the authority executes a limit at the highest of any of the single banks within that group.
- **Sovereign Limit** – The Council will only invest a maximum of £15m of the portfolio with non UK sovereigns. This is a reduction of the limit from £20m and will only apply from 2016/17 onwards.

Instrument	Country/ Domicile	Counterparty	Maximum Counterparty Limit %/£m	Maximum Group Limit (if applicable) %/£m	Council Holding At 31/12/15 £m
Term Deposits / CDs / Call Accounts	UK	Santander UK Plc (Banco Santander Group)	15	15	6.00
Term Deposits / CDs / Call Accounts	UK	Bank of Scotland (Lloyds Banking Group)	15	15	0
Term Deposits / CDs / Call Accounts	UK	Lloyds (Lloyds Banking Group)	15	15	10.74
Term Deposits / CDs / Call Accounts	UK	Barclays Bank Plc	15	15	0
Term Deposits / CDs / Call Accounts	UK	HSBC Bank Plc	15	15	2.75
Term Deposits / CDs / Call Accounts	UK	Nationwide Building Society	15	15	0
Term Deposits / CDs / Call Accounts	UK	NatWest (RBS Group)	15	15	0
Term Deposits / CDs / Call Accounts	UK	Royal Bank of Scotland (RBS Group)	15	15	0
Term Deposits / CDs / Call Accounts	UK	Standard Chartered Bank	15	15	0
Term Deposits / CDs / Call Accounts	UK	Close Brothers Limited	15	15	0
Term Deposits / CDs / Call Accounts	UK	Goldman Sachs International Bank	15	15	0
Term Deposits / CDs / Call Accounts	UK	Leeds Building Society	15	15	0
Term Deposits / CDs / Call Accounts	Australia	Australia and NZ Banking Group	15	15	0

Term Deposits / CDs / Call Accounts	Australia	Commonwealth Bank of Australia	15	15	0
Term Deposits / CDs / Call Accounts	Australia	National Australia Bank Ltd (National Australia Bank Group)	15	15	0
Term Deposits / CDs / Call Accounts	Australia	Westpac Banking Corp	15	15	0
Term Deposits / CDs / Call Accounts	Canada	Bank of Montreal	15	15	0
Term Deposits / CDs / Call Accounts	Canada	Bank of Nova Scotia	15	15	0
Term Deposits / CDs / Call Accounts	Canada	Canadian Imperial Bank of Commerce	15	15	0
Term Deposits / CDs / Call Accounts	Canada	Royal Bank of Canada	15	15	0
Term Deposits / CDs / Call Accounts	Canada	Toronto-Dominion Bank	15	15	0
Term Deposits / CDs / Call Accounts	Finland	Nordea Bank Finland	15	15	0
Term Deposits / CDs / Call Accounts	Finland	Pohjola Bank	15	15	0
Term Deposits / CDs / Call Accounts	Germany	Deutsche Bank AG	15	15	0
Term Deposits / CDs / Call Accounts	Germany	Landesbank Hessen – Thuringen (Helaba)	15	15	0
Term Deposits / CDs / Call Accounts	Netherlands	ING Bank NV	15	15	0
Term Deposits / CDs / Call Accounts	Netherlands	Rabobank	15	15	0
Term Deposits / CDs / Call Accounts	Netherlands	Bank Nederlandse Gemeenten	15	15	0
Term Deposits / CDs / Call Accounts	Singapore	DBS Bank Ltd	15	15	0
Term Deposits / CDs / Call Accounts	Singapore	Oversea-Chinese Banking Corporation (OCBC)	15	15	0
Term Deposits / CDs / Call Accounts	Singapore	United Overseas bank (UOB)	15	15	0

Term Deposits / CDs / Call Accounts	Sweden	Svenska Handelsbanken	15	15	9.12
Term Deposits / CDs / Call Accounts	Switzerland	Credit Suisse	15	15	0
Term Deposits / CDs / Call Accounts	US	JP Morgan Chase Bank	15	15	0

***Please note this list could change if, for example, a counterparty/country is upgraded, and meets our other creditworthiness tools. Alternatively, if a counterparty is downgraded, this list may be shortened. The counterparty list was correct as at 31 December 2015.*

SUMMARY OF INVESTMENTS**TOTAL RISK PER COUNTERPARTY AS AT 31 DECEMBER 2015**

	CREDIT RATING			TOTAL £000
<u>Fixed Deposits</u>				
HSBC	UK AAA	F1+ AA-	1	2,746
Svenska Handelsbanken	Sweden AAA	F1+ AA-	2	9,115
Lloyds	UK AAA	F1 A+	5	10,740
Santander	UK AAA	F1 A	2	6,000
TOTAL- FIXED TERM AND CASH DEPOSITS				28,601

<u>SUMMARY BY SOVEREIGN RATING</u>	<u>£000</u>	<u>%</u>
UK AAA	19,486	68
Sweden AAA	9,115	32
Total	28,601	100

Ethical Investment Framework – Telford and Wrekin Council

At the current time the Council's treasury activity consists principally of making short-dated loans to the UK Government (through the Debt Management Agency Deposit Facility) and to banks and building societies which adheres to the S-L-Y principles of (Security, Liquidity and Yield, in that order).

The preservation of capital is the Council's principal and overriding priority. The banks and building societies on the Council's lending list are selected only if the institutions and the sovereign meet a minimum credit criteria. In accordance with its social and corporate governance responsibilities, the Council seeks to support institutions which additionally have an ethical and responsible approach to environmental and social issues including employment and global trade. These "ethical" criteria and their basis are described below.

1. Environmental and Social Standards

Equator Principles

The Equator Principles are a voluntary set of guidelines based on the environmental and social standards practiced by the International Finance Committee when evaluating financing projects. Financial institutions that adopt the Principles agree to use a screening process aiming to ensure that environmental and social assessments help inform decisions to finance development projects. This allows signatories to engage proactively with their stakeholders on environmental and social policy issues.

The Equator Principles (EPs) are a screening framework for determining, assessing and managing environmental and social risk in project finance transactions for major infrastructure and industrial projects. The EPs are adopted voluntarily by financial institutions and are applied where total project capital costs exceed US\$10 million. The EPs are primarily intended to provide a minimum standard for due diligence to support responsible risk decision-making. They are based on the International Finance Corporation's performance standards on social and environmental sustainability and on the World Bank Group Environmental Health and Safety Guidelines.

Financial institutions which are signatories to the EPs commit to not providing loans to projects where the borrower will not or is unable to comply with their respective social and environmental policies and procedures that implement the EPs.

The following banks relating to institutions on the Council's lending list have adopted the Equator Principles :

- Barclays Bank
- HSBC Bank plc
- Lloyds Banking Group (parent of Bank of Scotland and Lloyds TSB Bank)
- Royal Bank of Scotland
- Standard Chartered
- Banco Santander (parent of Santander UK plc).

<http://www.equator-principles.com/index.php/members-reporting>

2. Human Rights, Labour and Environment

The **UN Global Compact** is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption.

Corporations which sign up to the UN Global Compact are encouraged to themselves embrace and in turn, support and enact, within their sphere of influence, a set of core values which are derived from:

- The Universal Declaration of Human Rights
- The International Labour Organization's Declaration on Fundamental Principles and Rights at Work
- The Rio Declaration on Environment and Development
- The United Nations Convention Against Corruption

Human Rights

- Principle 1: Businesses should support and respect the protection of internationally proclaimed human rights; and
- Principle 2: make sure that they are not complicit in human rights abuses.

Labour

- Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;
- Principle 4: the elimination of all forms of forced and compulsory labour;
- Principle 5: the effective abolition of child labour; and
- Principle 6: the elimination of discrimination in respect of employment and occupation.

Environment

- Principle 7: Businesses should support a precautionary approach to environmental challenges;
- Principle 8: undertake initiatives to promote greater environmental responsibility; and
- Principle 9: encourage the development and diffusion of environmentally friendly technologies.

Anti-Corruption

- Principle 10: Businesses should work against corruption in all its forms, including extortion and bribery.

The following banks relating to institutions on the Council's lending are participants/stakeholders of the UN Global Compact :

- HSBC
- Royal Bank of Scotland
- Standard Chartered
- Grupo Santander (ultimate parent of Santander UK plc).

<http://www.unglobalcompact.org/ParticipantsAndStakeholders/index.html>

Limitations to ethical policies :

It should be noted here that the individual institutions which have signed up to the Equator Principles and to the Global Compact screen borrowers before lending for infrastructure and industrial projects.

However, financial institutions also engage daily in money market and interbank lending transactions; the criteria for such lending is based primarily on credit risk assessment (i.e. the assessment of their lending being repaid in full and on time when it is due). Being a signatory to the EPs will not necessarily be a critical feature of such credit assessment and the Council is not in a position to monitor interbank lending. The same applies to an individual financial signing up to the UN Global Compact.

It should also be noted that becoming a signatory of voluntary guidelines (Equator Principle or Global Compact) does not guarantee that that institution's policies and practices are of a better standard than those institutions which are not signatories to the voluntary guidelines.

Activist investment : The Council does not invest directly in shares or in corporate bonds. Not only are such investments inherently higher risk investments, and requires a distinct and separate set of fund management expertise. Under current legislation (SI 2003 No 3146) the purchase of share capital or loan capital of a body corporate is a capital expenditure investment which, on sale or maturity, becomes a capital receipt and is unsuitable for the Council's treasury investments which are primarily the cash management of its operating surpluses and reserves. Corporate bond and equity investments would however be made by the Council's pension fund (run by Shropshire Council).

Other than through its pension fund (which is measured by Shropshire Council), the Council cannot seek to influence decision making at a company by voicing concerns, engaging in a dialogue with management, or lobbying other shareholders for support. Activist investors attempt to purchase sufficient shares or obtain seats on the board with the goal of effecting major change in the company to make the company more valuable financially or socially (for example to change management policies and adopt better governance; optimise shareholder value through acquisitions/divestitures, be more socially responsible etc).

Credit Ratings – A Guide.

Long-term credit ratings and Sovereign Ratings

Fitch Rating' long-term credit ratings are set up along a scale from 'AAA' to 'D', first introduced in 1924 and later adopted and licensed by Standard & Poors (S&P). Moody's also uses a similar scale, but names the categories differently. Like S&P, Fitch also uses intermediate modifiers for each category between AA and CCC (i.e., AA+, AA, AA-, A+, A, A-, BBB+, BBB, BBB- etc.).

Investment grade

- **AAA** : the best quality, reliable and stable
- **AA** : good quality, a bit higher risk than AAA
- **A** : economic situation can affect finance
- **BBB** : medium class counterparties, which are satisfactory at the moment

Non-investment grade

- **BB** : more prone to changes in the economy
- **B** : financial situation varies noticeably
- **CCC** : currently vulnerable and dependent on favourable economic conditions to meet its commitments
- **CC** : highly vulnerable, very speculative bonds
- **C** : highly vulnerable, perhaps in bankruptcy or in arrears but still continuing to pay out on obligations
- **D** : has defaulted on obligations and Fitch believes that it will generally default on most or all obligations
- **NR** : not publicly rated

Short-term credit ratings

Fitch's short-term ratings indicate the potential level of default within a 12-month period.

- **F1+** : best quality grade, indicating exceptionally strong capacity of obligor to meet its financial commitment
- **F1** : best quality grade, indicating strong capacity of obligor to meet its financial commitment
- **F2** : good quality grade with satisfactory capacity of obligor to meet its financial commitment
- **F3** : fair quality grade with adequate capacity of obligor to meet its financial commitment but near term adverse conditions could impact the obligor's commitments
- **B** : of speculative nature and obligor has minimal capacity to meet its commitment and vulnerability to short term adverse changes in financial and economic conditions
- **C** : possibility of default is high and the financial commitment of the obligor are dependent upon sustained, favourable business and economic conditions
- **D** : the obligor is in default as it has failed on its financial commitments.

Support Ratings (1 – 5)

The Purpose and Function of Support Ratings

Support Ratings are Fitch Ratings' assessment of a potential supporter's propensity to support a bank and of its ability to support it. Its propensity to support is a judgment made by Fitch Ratings. Its ability to support is set by the potential supporter's own Issuer Default Ratings, both in foreign currency and, where appropriate, in local currency. Support Ratings do not assess the intrinsic credit quality of a bank. Rather they communicate the agency's judgment on whether the bank would receive support should this become necessary. These ratings are exclusively the expression of Fitch Ratings' opinion even though the principles underlying them may have been discussed with the relevant supervisory authorities and/or owners.

Timeliness and Effectiveness Requirements

Fitch Ratings' Support Rating definitions are predicated on the assumption that any necessary "support" is provided on a timely basis. The definitions are also predicated on the assumption that any necessary support will be sufficiently sustained so that the bank being supported is able to continue meeting its financial commitments until the crisis is over.

Obligations and Financial Instruments Covered

In terms of these definitions, unless otherwise specified, "support" is deemed to be in terms of foreign currency. It is assumed that typically the following obligations will be supported: senior debt (secured and unsecured), including insured and uninsured deposits (retail, wholesale and interbank); obligations arising from derivatives transactions and from legally enforceable guarantees and indemnities, letters of credit, and acceptances; trade receivables and obligations arising from court judgments.

Likewise, the agency does not assume that the following capital instruments will be supported when sovereign support is involved: preference/preferred shares or stock; hybrid capital (tier 1 and upper tier 2), including reserve capital instruments (RCIs) and variations upon RCIs; and common/ordinary equity capital. It is also assumed that there will be no support for any moral obligation on securitizations. The sovereign support status of subordinated debt is difficult to categorize in advance; it is assessed on a case by case basis, distinguishing among different jurisdictions.

Definitions:

- 1: A bank for which there is an extremely high probability of external support. The potential provider of support is very highly rated in its own right and has a very high propensity to support the bank in question. This probability of support indicates a minimum Long-Term Rating floor of 'A-'.
- 2: A bank for which there is a high probability of external support. The potential provider of support is highly rated in its own right and has a high propensity to provide support to the bank in question. This probability of support indicates a minimum Long-Term Rating floor of 'BBB-'.
- 3: A bank for which there is a moderate probability of support because of uncertainties about the ability or propensity of the potential provider of support to do so. This probability of support indicates a minimum Long-Term Rating floor of 'BB-'.
- 4: A bank for which there is a limited probability of support because of significant uncertainties about the ability or propensity of any possible provider of support to do so. This probability of support indicates a minimum Long-Term Rating floor of 'B'.

- 5:** A bank for which external support, although possible, cannot be relied upon. This may be due to a lack of propensity to provide support or to very weak financial ability to do so. This probability of support indicates a Long-Term Rating floor no higher than 'B-' and in many cases no floor at all.

GLOSSARY

Term	Meaning
Affordable Borrowing Limit	The amount the authority would normally borrow at any point of time in the year. This boundary might be exceeded temporarily but only in exceptional circumstances. The limit is set by Full Council at the beginning of March and is a prudential indicator.
Authorised Borrowing Limit	The maximum amount the authority can borrow at any point of time in the year. This limit should never be exceeded. The limit is set by Full Council at the beginning of March and is a prudential indicator.
Capital Financing Requirement (CFR)	This represents the underlying need for the authority to borrow and represents the assets of the authority less the long term capital liabilities.
Credit Default Swaps (CDS)	CDS are bought by investors to insure against defaults (i.e. the counterparty not being able to repay). The higher the cost/premium then the higher the risk – CDS therefore given a market view of the credit worthiness of an organisation.
Credit Ratings	Rating on the ability of an organisation to meet its obligations; ratings are assigned by independent, specialist companies, such as Fitch and Moodys using market intelligence they gather.
Credit Risk	The risk that the debtor will default on their obligations
Counterparty	The organisation that you are conducting your business with.
Debt Management Account Deposit Facility	Provided by the <u>Debt Management Office</u> , users can place cash in secure fixed-term deposits. Deposits are guaranteed by the government and therefore have the equivalent of a sovereign triple-A credit rating.
Derivative Instruments	A security whose price is dependent upon or derived from one or more underlying assets. The derivative itself is merely a contract between two or more parties. Its value is determined by fluctuations in the underlying asset. The most common underlying assets include stocks, bonds, commodities, currencies, interest rates and market indexes. Most derivatives are characterized by high leverage. For example, a stock option is a derivative because it derives its value from the value

	of a stock. An interest rate swap is a derivative because it derives its value from one or more interest rate indices.
Discounts	These relate to Public Works Loans Board loans. If rates have increased since the borrowing was undertaken then part of the benefit that PWLB will achieve from being able to loan out at that higher rate are passed back to an authority if they repay the loan early.
Fund Managers	Independent investment managers who work to a specific mandate and invest funds on behalf of the Council
Inflation	The rise in prices of goods and services over a period of time.
Interest Rate Risk	The risk that the value of an investment will change due to changes to the interest rate.
Internal Borrowing	This is where the amount of an authority's borrowing is less than its CFR or underlying need to borrow and represents the use of internal balances rather than borrowing from the market.
LIBID	London inter-bank bid rate. Interest rate at which prime banks will borrow money in the London inter-bank market.
LIBOR	London inter-bank offer rate. Interest rate at which prime banks will lend money in the London inter-bank market. Fixed every day by the British Bankers Association to five decimal places.
Liquidity Risk	The risk of not being able to trade an investment quickly to release cash.
Minimum Revenue Provision (MRP)	This is the amount charged against the Income and Expenditure Account for the year in relation to the repayment of debt on borrowing in order to fund capital expenditure.
Obligor	An individual or company that owes debt to another individual or company (the creditor), as a result of borrowing or issuing bonds.
Premia	This is the penalty applied to the early redemption of PWLB loans where rates have fallen since the loan was undertaken.
Prudential Code	A professional code of practice which provides regulatory framework to local authorities on capital expenditure, investments and borrowing activities.
Prudential Indicators	A set of indicators developed within the Prudential Code which define thresholds for investment and borrowing within a local authority.

PWLB	Public Works Loans Board – a Government agency providing long and short term loans to local authorities. Interest rates are generally lower than the private sector and slightly higher than the rates at which the Government themselves may borrow.
Re-scheduling	This relates to repaying existing borrowing early and replacing it with borrowing for a different period usually, but not necessarily, at lower rates
Return	The gain from holding an investment over a given period
Security	An investment instrument, other than an insurance policy or fixed annuity, issued by a corporation, government or other organisation which offers evidence of debt or equity.
Sovereign Exposure	Risk of exposure to one particular country.
Supranational Bonds	These are bonds (similar to gilts) issued by multi government development organisations and are supported by all of the governments who form part of the organisation. E.g. European Investment Bank and are usually very secure.
Quantative Easing	This is where the government buy back there own gilt issuance to effectively pump money into the financial markets of the economy.