TRAFFORD COUNCIL

Report to:	**Accounts & Audit Committee**
Date:	**7 February 2018**
Report for:	**Decision**
Report of:	**The Executive Member for Corporate Resources and the Chief Finance Officer**

Report Title

TREASURY MANAGEMENT STRATEGY 2018/19 – 2020/21

Summary

This report outlines the:-

- strategy to be followed during this period for investments and borrowing,
- outlook for interest rates,
- management of associated risks,
- policy to be adopted on Minimum Revenue Provision (MRP) and
- Prudential Indicators.

Recommendations

That the Accounts & Audit Committee recommend to the Executive and Council the key elements of this report for approval which are as follows:

- policy on debt strategy as set out in section 3;
- investment strategy as set out in section 5;
- Prudential Indicators and limits including the Authorised Limit (as required by section 3(1) of the Local Government Act 2003), Operational Boundary, Minimum Revenue Provision Statement and Investment criteria as detailed in Appendix 3.

Contact person for access to background papers and further information:

Name: Graham Perkins
Extension: 4017

Background papers: None

Relationship to Policy Framework / Corporate Priorities	Value for Money
Financial	The treasury management strategy will aim to maximise investment interest whilst minimising risk to the Council. The Council's debt position will be administered effectively and any new loans taken will be in-line with the Medium Term Financial Plan provision.
Legal Implications:	Actions being taken are in accordance with legislation, Ministry of Housing, Communities & Local Government (MHCLG) guidance, Chartered Institute of Public Finance & Accountancy (CIPFA) Prudential Code and Treasury Management Code of Practice.
Equality/Diversity Implications	Any equality and diversity implications are as set out in this report
Sustainability Implications	Not applicable
Staffing/E-Government/Asset Management Implications	Not applicable
Risk Management Implications	The monitoring and control of risk underpins all treasury management activities and these factors have been incorporated into the treasury management systems and procedures which are independently tested on a regular basis. The Council's in-house treasury management team continually monitor risks to ensure that the main risks associated with this function of adverse or unforeseen fluctuations in interest rates are avoided and security of capital sums are maintained at all times.
Health and Safety Implications	Not applicable

Summary

The purpose of this report, which has been prepared in accordance with the Council's Financial Procedure Rules number 8, outlines the forecasted treasury management activities for the forthcoming three years. Further reports are produced during the course of the year informing Members of the preceding financial year's actual activities together with a current mid-year update.

Economic position (Appendix 2)

Brexit negotiations between the UK Government and the European Union are set to continue to dominate the headlines during the forthcoming year and the impact these will have on both economies remains uncertain at this time. The general world economic situation is currently projecting a positive outlook with good performance and falling unemployment being reported. Appendix 2 highlights the main economic events of 2017 and projections for 2018 for reference.

Debt (Section 3)

Borrowing interest rates whilst forecasted to rise marginally from their current position are still forecast to be at historically low levels during the next 12 months. Any new external borrowing will be taken in order to assist finance the Council's capital borrowing requirement as outlined in the 2018/21 Capital Programme report with all associated costs being contained within the the Council's Medium Term Financial Plan.

Debt restructuring exercises will only be undertaken in order to produce revenue savings or lower overall treasury risk.

Investments (See Section 5 and Appendix 3)

The main objective surrounding the Council's investment criteria remains unchanged from that previously adopted of security of capital first, liquidity of its cash flows and finally yields.

The Council is required to agree the lending criteria, which is primarily determined by credit ratings issued by the 3 major credit rating agencies as detailed at Appendix 3.

Prudential Indicators and limits (Section 7 and Appendix 3)

The Council is required to approve a set of Prudential Indicators and limits which ensure the Council's capital expenditure plans and borrowing remain robust, prudent, affordable and sustainable. These are detailed at Appendix 3 for Member approval.

Medium Term Financial Plan (See Appendix 7)

Appendix 7 reflects the current forecasted financial requirements of the Council's treasury management functions during this reporting period.

Background

1.1 Treasury management as defined by the Chartered Institute of Public Finance Accountancy (CIPFA) is:

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

1.2 The main function associated with this process is to ensure that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet service activity and its approved capital strategy. This will involve both the management of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. This strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

1.3 Members are required to receive and approve, as a minimum, 3 reports annually which incorporate a variety of policies, forecasts and actuals as follows;

- **Annual treasury strategy** (issued February and includes);
  - A Minimum Revenue Provision (MRP) policy (this reflects capital expenditure previously financed by borrowing and how the principal element is charged to revenue over time),
  - The treasury management strategies (how the investments and borrowings are to be organised) including treasury indicators and
  - An investment strategy (the parameters on how investments are to be managed).
- **Mid-year update** – (issued November / December and provides an);
  - update for members with the progress of the treasury management activities undertaken for the period April to September and
  - opportunity for amending prudential indicators and any policies if necessary.
- **Annual outturn** – (June and contains);
  - details of actual treasury operations undertaken in the previous financial year.

1.4 Each of the above 3 reports are required to be adequately scrutinised before being recommended to Council for final approval and this role is undertaken by the Accounts & Audit Committee.

1.5 All treasury management transactions undertaken will comply with the statutory requirements together with MHCLG Guidance and CIPFA Treasury Management Code of Practice which the Council has previously adopted. A brief outline of these frameworks is provided at Appendix 1.

1.6 In December 2017, CIPFA issued a revised Treasury Management Code of Practice which primarily focused on non-treasury investments, particularly the purchase of property with a view to generating income. This update has clarified CIPFA's position in that it has now drawn a cleaner separation between treasury and non-treasury investments, the latter being included in the Capital Programme report.

1.7 Further consultations were also carried out by the MHCLG on both investments and MRP guidance and focused primarily on non-financial asset investments. These consultations closed on 22 December 2017 and the outcomes of which are currently awaited. Once these outcomes have been received they will be examined and where appropriate any significant amendments will be implemented and reported to Members in due course.

1.8 This report which has been prepared in accordance with the required statutory regulations and guidance includes;

- Economic & Interest Rate forecast (section 2)
- Debt Strategy (section 3)
- Minimum Revenue Provision (section 4)
- Investment Strategy (section 5)
- Investment Risk Benchmarking (section 6)
- Prudential Indicators (section 7)
- Related Treasury Issues (section 8)
- Recommendations (section 9).

1.9 The Council uses Link Asset Services (formerly Capita Asset Services) as its treasury management advisors who provide a range of services on all treasury matters from the supply of credit ratings to technical support. The Council recognises that there is value in employing external providers for this service in order to acquire access to specialist skills and resources and the provision of this service is subject to regular review.

1.10 Whilst the advisors provide support to the in-house treasury management team, the Council recognises that the final decision on all treasury management matters remains with it at all times.

1.11 The Council further acknowledges the importance of ensuring that all Members and staff involved in the treasury management function receive adequate training and are fully equipped to undertake the duties and responsibilities allocated to them.

1.12 In order to assist with this undertaking, a Member training event was provided on 30 January 2017 and similar events will be provided when required. Officers will continue to attend courses / seminars presented by CIPFA and other suitable professional organisations.

2. Economic & Interest Rate forecast

2.1 Economic and interest rate forecasting continues to be very difficult as a result of so many external influences impacting on the UK economy however it is predicted that;

- Investment returns are likely to remain low during 2018/19 rising gently over the next few years and
- Borrowing rates will continue at their current low levels with minor movements upwards expected.

2.2 The general overall world economic position looks to be on an encouraging trend of stronger performance with falling levels of unemployment and further details on the major economic events which occurred during 2017 and forecasts for 2018 are outlined at Appendix 2 for reference.

2.3 Link Asset Services produces interest rate projections periodically throughout the year and the latest forecasts (November 2017), covering the period up to March 2021, are highlighted in the table below;

Average rates	2017-18 Forecast %	2018-19 Forecast %	2019-20 Forecast %	2020-21 Forecast %
Bank Rate	0.35	0.58	0.88	1.10
Investment Rates (LIBID) 3 month 1 Year	 0.35 0.65	 0.50 0.90	 0.75 1.15	 0.70 1.15
PWLB Loan Rates 5 Year 25 Year	 1.50 2.80	 1.50 3.00	 1.95 3.25	 2.20 3.50

2.4 Over the next few years, the Council will continue to adopt a cautious approach to its treasury management activities whilst utilising the information available from both its external advisors Link Asset Services and other sources which may become available during this time.

3. Debt Strategy

3.1 In order to assist short term cash flow or finance longer term capital investment, the Council has the powers to borrow new funds from a variety of sources comprising of;

- Other local authorities,
- The Government via the Public Works Loan Board, (PWLB),
- Dedicated publicly funded companies e.g. Salix,
- Municipal Bond Agency, which is currently still in the process of being set up or
- Financial institutions within the money market.

3.2 The table below shows the level of external debt which the Council may undertake;

	2017/18	2018/19	2019/20	2020/21
	Estimate £000	**Estimate £000**	**Estimate £000**	**Estimate £000**
Debt at 1 April	105,233	406,822	430,288	438,360
External Debt maturing	(3,875)	(4,020)	(4,662)	(4,662)
Potential level of External Debt*	305,464	27,486	12,734	9,683
Debt at 31 March	406,822	430,288	438,360	443,381

*This reflects the phasing in the Capital Programme and predominatley relates to the Council's Capital Investment Property programme.

3.3 Whilst the above table reflects the Council's expected loan position, the table below details the postion of its other long term liabilities in respect to the Private Finance Initative (PFI) funding.

	2017/18	2018/19	2019/20	2020/21
	Estimate £000	**Estimate £000**	**Estimate £000**	**Estimate £000**
Other long-term liabilities – (1 April)	5,778	5,556	5,319	5,067
Expected repayment	(222)	(237)	(252)	(268)
Other long-term liabilities – (31 March)	5,556	5,319	5,067	4,799

3.4 The Council is currently maintaining an under-borrowed position and previously this was reported to be £38.8m and this is currently forecasted to be £44m by 31 March 2018. This position has arisen from decisions taken previously not to finance capital spending from new external loans but instead cash supporting the Council's reserves, balances and cash flow has been temporarily used. This strategy is prudent as investment returns are low and counterparty risk, whilst this has significantly reduced over the recent few years, remains an issue that needs to be considered.

3.5 The policy of avoiding new borrowing by running down spare cash balances has served the Council well over the last few years due to debt interest rates being consistently higher than investment returns available and this situation is forecasted to continue for the foreseeable future. Whilst the Council has no budgetary provision to cover interest costs for taking on new debt, the amount applied to finance the capital spend incurred, principal, is being reinstated via the Council's annual MRP charge.

3.6 The Chief Finance Officer will monitor the interest rate market and adopt a pragmatic approach to changing circumstances within the 2018/19 treasury operations. Any new borrowing undertaken which will be undertaken to assist finance the Council's self-financing Commercial Investment Property programme will be subject to favourable interest rates.

3.7 Appendix 6 shows the level of the Council's loans totalling £139.2m together with the average interest rate, as at 31 December 2017, and this is split between PWLB £77.4m & Market (banks & publically funded companies) £61.8m.

3.8 The Council holds, as at 31 March 2018, £61.8m of Market loans and of these £40.0m are held as variable rates of interest in the form of Lender's Option Borrower's Option (LOBO) loans. On this type of loan, the lender has the option to propose an increase in the interest rate at set dates and should this situation occur then the Council can either accept the new rate or repay the loan at no additional cost. Although the Chief Finance Officer understands that lenders are unlikely to exercise their option in the current low interest rate environment, there remains a possiblity that this could occur. In accordance with the Chief Finance Officer's delegated authority, should an opportunity present itself to repay a LOBO loan without incurring any penalty costs, then this option will be taken and a further decision will also be made at the same time as to whether it is prudent to take a replacement loan from the PWLB. The remainder of the Market loans, £21.8m are held at fixed rates of interest.

3.9 In addition to the borrowing undertaken directly, the Council is also responsible for a further £0.7m of loan debt administered by Tameside Borough Council. This follows the conversion in February 2010 of loans previously held on behalf of Manchester International Airport into an equity rated instrument.

3.10 As short term borrowing rates are cheaper than longer term fixed interest rates, there may be potential opportunities in the future to generate revenue savings by switching from long to short term debt or due to low investment returns running down investment balances to repay debt prematurely. The cost of premiums incurred however due to early repayment, will also need to be taken into account before any restructuring is undertaken.

3.11 The Council retains the flexibility to borrow funds in advance of requirement should market conditions unexpectedly change i.e. a sharp rise in interest rates is suddenly expected, and any decision to borrow in advance will ensure that funds are taken within the forward approved Capital Financing Requirement estimates. The Capital Financing Requirement (CFR) is simply the historic level of outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is a measure essentially of the Council's underlying borrowing need and is reduced from the level of Minimum Revenue Provision (MRP) provided for annually.

3.12 The Council will not borrow any funds ahead of schedule purely to profit from the investment of the extra sums borrowed and any borrowing taken by the Chief Finance Officer in advance of need will be done in accordance with delegated powers and within the constraints stated below;

- no more than 50% of the expected increase in borrowing need (CFR) over the three year planning period is to be obtained in this manner and
- the Council would not look to borrow more than 12 months in advance of need.

3.13 The Council's debt maturity profile is provided at Appendix 4 for reference which also shows, in accordance with the Code of Practice, the potential first date the lending banks could amend the rate of interest for their respective market loans.

3.14 *The Council is required to approve;*

- *the above debt strategy and*
- *as part of the Prudential Indicators and Limits requirement, the limits for external debt in accordance with the Local Government Act 2003, having regard to CIPFA's prudential code before the commencement of each financial year. These limits are detailed at Appendix 3 for Council approval.*

4. Minimum Revenue Provision Strategy

4.1 The Council is required to set aside an amount each year for the repayment of debt (by reducing the CFR), through a revenue charge called the Minimum Revenue Provision (MRP). In addition, the Council is also allowed to undertake Voluntary Revenue Payments (VRP) if required.

4.2 *The Council is requested, in accordance with MHCLG regulations, to approve an MRP Statement in advance of each year and this is detailed at Appendix 3.*

5. Investment Strategy

5.1 The Council undertakes investments, from temporary surplus income which has been received in advance of spend requirement and from its balances and reserves which it holds. The primary principle governing the Council's investment criteria is the **S**ecurity of its investments, followed by **L**iquidity whilst ensuring that a reasonable level of **Y**ield is also achieved

5.2 All of the Council's investments are undertaken in accordance with guidance issued by both the MHCLG and CIPFA. In order to minimise the risk to its investments, the Council creates and maintains a list of high creditworthy institutions which enables diversification and avoidance of concentration risk. A minimum acceptable credit criteria is applied and the key ratings used to monitor counterparties are the Short Term "F1" or equivalent and Long Term "A-" or equivalent ratings as issued by the three independent rating agencies (Fitch, Moody's and Standard and Poor's).

5.3 This approach uses real time credit rating information provided by the Council's advisors and enables an institution should they meet or no longer meet the minimum credit criteria required to be immediately included on or removed off the approved list.

5.4 Whilst investment risk will never completely be eliminated, it can be minimised and in order to reduce the risk of an institution defaulting, the Chief Finance Officer recommends that the Council continues with the current practice of institutions only being included on the Council's lending list which meet the minimum credit rating detailed in 5.2 above.

5.5 A full explanation of the credit ratings determining the institutions which the Council will use can be found at Appendix 5.

5.6 The Council's in-house treasury management team recognises ratings should not be the sole basis of determining the quality of an institution and continual assessment and monitoring of the financial sector in relation to the economic and political environments in which institutions operate will also be carried out. To achieve this, the Council will with its advisors, monitor market pricing on additional factors such as "credit default swaps" and overlay this information on top of the credit ratings. This additional market information is detailed for Members' reference at Appendix 5.

5.7 Further information will also be used to assess the credit worthiness of an institution including the financial press, share price and other such information pertaining to the financial sector in order to establish a robust scrutiny process concerning the suitability of potential investment counterparties.

5.8 Investment instruments identified for use in the financial year and counterparty limits are detailed in Appendix 3.

5.9 Members are asked to approve this base criteria, however the Chief Finance Officer may temporarily restrict further investment activity to those institutions considered of higher credit quality than the minimum criteria set out for approval should any exceptional market conditions be encountered.

5.10 Investments will continue to be placed into three categories as follows;

- Short-term – cash required to meet known cash flow outgoings in the next month, plus a contingency to cover any unexpected transaction over the same period with bank call accounts, money market funds and certificates of deposits being the main methods used for this purpose.
- Medium-term – cash required to manage the annual seasonal cash flow cycle covering the next 12 months and will generally be in the form of fixed term deposits and enhanced money market funds.
- Long-term – cash not required to meet any forthcoming cash flow requirements which can be used primarily to generate investment income by using fixed or structured term deposits, certificates of deposits, government bonds or the Local Authority Property Investment fund, after taking into consideration the forecasted interest rate yield curve.

5.11 The use of longer term instruments (greater than one year from inception to repayment) will fall in the Non-specified investment category. These instruments will only be used where the Council's liquidity requirements are safeguarded and be limited to the Prudential Indicator detailed at Appendix 3.

5.12 The level of the Council's investments together with the average interest rate, as at 31 December 2017, is provided for reference at Appendix 6.

5.13 In the continuing environment of low interest rates, the Council is not able to generate a significant return from its investments. Against this backdrop it is easy to forget recent history and search for that extra return to ease revenue budget pressures an issue recently highlighted by the Financial Conduct Authority who has stated that;

> "The main risks in the industry for the coming year are firms designing products that:

- aren’t in the long-term interest of consumers,
- contain a lack of transparency on what’s being sold,
- lead to a poor understanding by consumers of risk,
- shift toward more complex structured products that lack oversight”.

5.14 With respect to this, the Council’s in-house treasury management team will not actively seek to place funds with institutions paying considerably over and above market levels and will continue to carry out proper and full risk assessments of any new product which may come onto the market before committing funds into it.

5.15 *The Council is requested to approve;*

- *the adoption of the above Investment strategy and*
- *the minimum criteria for providing a list of high quality investment institutions, instruments and limits to be applied as set out at Appendix 3.*

6. Investment Risk Benchmarking

6.1 The CIPFA Code of Practice and MHCLG Investment Guidance require that appropriate security and liquidity benchmarks are considered and reported to Members with details of these being provided in Appendix 5.

6.2 Benchmarks are simple guides to maximum risk (not limits) for use with cash deposits and so may be breached from time to time, depending on movements in interest rates and institution criteria. The purpose of the benchmark is to assist officers to monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported to Members, with supporting reasons in the Mid-Year or Annual Report. For reference the benchmarks proposed are;

- Security - each individual year the security benchmark is:

1 year investments	2 year investments	3 year investments
0.07%	**0.02%**	**0.08%**

Note - This benchmark is an average risk of default measure and would not constitute an expectation of loss against a particular investment.

- Liquidity – Weighted Average Life (WAL) - benchmark for 2018/19 is set at 6 months, with a maximum of 3 years for cash time deposits;
  - Liquid short term deposits - at least £15m is available within a week notice;
- Yield - Internal returns are required to achieve above the 7 day London Interbank Deposit (LIBID) rate.

7. Prudential Indicators

7.1 A number of prudential indicators have been devised for the treasury management operation and these are designed to assist managing risk and reducing the impact of an adverse movement in interest rate. These indicators have been set at levels which do not restrict day to day activities being undertaken and at the same time ensure the Council’s capital expenditure plans are prudent, affordable and sustainable.

7.2 *Members are requested to approve the Prudential Indicators for Council’s treasury management activities as detailed at Appendix 3.*

8. Related Treasury Issues

8.1 Local Authority Mortgage Scheme. Under this scheme 112 first time buyers were able to purchase a property in Trafford, with the Council placing funds totalling £3m (£2m in 2012/13 & £1m 2013/14) with Lloyds bank for a period of 5 years to match the life of the indemnity. During 2017/18, £2m of the amount originally advanced was repaid back to the Council with the balance, £1m due to be repaid during 2018/19.

8.2 Greater Manchester Pension fund. During 2017/18, the Council along with several other local Councils took advantage of GMPF wider investment powers and paid over 3 years employer pension contributions at a discounted rate.

8.3 Investment Properties. During 2017/18 the Council introduced a programme to acquire suitable assets which will deliver significant economic development and regeneration benefits for the area and/or increase the Council's income generating capacity enabling it to maintain the provision of services in future years. Of the properties completed to date all spend has been financed from new external loans.

8.4 Whilst the above 3 projects are policy related activities and therefore not deemed to be treasury management, their implementation will have an impact on the Council's cash flow as well as the investing and borrowing activities which Members need to be aware of.

9. Recommendations

That the Accounts & Audit Committee recommend to the Executive and Council the key elements of this report for approval which are as follows;-

- *policy on debt strategy as set out in section 3;*
- *investment strategy as set out in section 5;*
- *Prudential Indicators and limits including the Authorised Limit (as required by section 3(1) of the Local Government Act 2003), The Minimum Revenue Provision Statement and Investment criteria as detailed in Appendix 3.*

Other Options

This report has been produced in order to comply with Financial Procedure Rules and relevant legislation. It provides a plan of action for the period 2018/19 to 2020/21, which is flexible enough to take account of changes in financial markets. There are an almost infinite number of other options that the Council could consider as part of its treasury management activities. However, this report outlines a coherent and prudent approach which is recommended by the Chief Finance Officer to the Council.

Consultation

Advice has been obtained from Link Asset Services, the Council's external advisors.

Reasons for Recommendation

The Financial Procedure Rules, incorporating the requirements of the CIPFA Treasury Management Code of Practice requires that the annual strategy report is provided to the Council as an essential control over treasury management activities. In it the Council approves the parameters under which officers will operate. In addition The Local Government Act 2003 requires that the Council approves an annual borrowing limit (the Authorised Limit) and MHCLG Guidance an annual investment strategy (setting out the limits to investment activities) prior to the commencement of each financial year.

Key Decision

This will be a key decision likely to be taken in: February 2018

This is a key decision currently on the Forward Plan: Yes

Finance Officer Clearance *…GB…*

Legal Officer Clearance *…DA….*

Director's Signature

APPENDIX 1

STATUTORY FRAMEWORK

Local Government Act 2003

In accordance with the Local Government Act 2003 (and supporting regulations and guidance) each Council must before the commencement of each financial year, produce a report fulfilling three key requirements as stipulated below;

- The debt strategy in accordance with the CIPFA Code of Practice on Treasury Management (section 3);
- The investment strategy in accordance with the MHCLG investment guidance (section 5);
- The reporting of the prudential indicators as required by the CIPFA Prudential Code for Capital Finance in Local Authorities (Appendix 3).

CIPFA Code of Practice

The Council's treasury activities are strictly regulated by statutory requirements in conjunction with a professional code of practice (the CIPFA Treasury Management Code of Practice). This Council adopted the Code of Practice on Treasury Management on 24 April 2002 and followed recommended practices by considering an annual Treasury Management Strategy before the commencement of each financial year. These Codes are revised from time to time and the Council complies with any revisions.

Investment Guidance

MHCLG issued Investment Guidance in March 2010 and this forms the structure of the Council's policy below:

- The strategic guidelines for decision making on investments, particularly non-specified investments;
- Specified investments that the Council will use. These are high security (no guidelines are given defining what this should consist of and each individual Council is required to state what this should be i.e. high credit ratings), high liquidity investments in sterling and with a maturity of no more than a year;
- Non-specified investments, clarifying the greater risk implications, identifying the general types of investment that may be used and a limit to the overall amount of various categories that can be held at any time;
- The principles to be used to determine the maximum periods for which funds can be committed.

APPENDIX 2

MAIN ECONOMIC HEADLINES DURING 2017

GLOBAL OUTLOOK-

- World growth looks to be on an encouraging trend of stronger performance, rising earnings and falling levels of unemployment. In October, the IMF upgraded its forecast for world growth from 3.2% to 3.6% for 2017 and 3.7% for 2018.
- In addition, inflation prospects are generally muted and it is particularly notable that wage inflation has been subdued despite unemployment falling to historically very low levels in the UK and US.

UK-

- After strong economic growth in 2016 of (1.8%), 2017 looks to be weaker with growth coming in at quarter 1 +0.2% (+2.0% y/y), quarter 2 +0.3% (+1.7% y/y) and quarter 3 +0.4% (+1.6% y/y);
- Consumer Price Index (CPI) opened the year at 1.8% in January 2017 rising to 3.1% in November 2017;
- The Bank of England Inflation Reports during 2017 highlighted that CPI was to peak at just under 3% in 2017, before falling back to near to its target rate of 2% in two years' time;
- At the Monetary Policy Committee, (MPC), meeting of 14 September 2017 it was announced that Bank Rate will need to rise soon. This was borne out on 2 November when the MPC announced its first rate rise in 10 years increasing the Bank Rate from 0.25% to 0.50%;
- The rate of unemployment continues to fall from 4.7% in January 2017 to 4.3% in September the lowest level since 1975;
- Due to the uncertainty around the Brexit negotiations, both consumer and business confidence to spend on investing, remains subdued and below is the proposed Brexit timetable for reference;
    - March 2017: UK government notifies the European Council of its intention to leave under the Treaty on European Union Article 50
    - March 2019: initial two-year negotiation period on the terms of exit
    - UK continues as a full EU member until March 2019 with access to the single market and tariff free trade between the EU and UK. Different sectors of the UK economy will leave the single market and tariff free trade at different times during the two year transitional period.
    - The UK and EU would attempt to negotiate, among other agreements, a bi-lateral trade agreement over that period.
    - The UK would aim for a negotiated agreed withdrawal from the EU, although the UK could also exit without any such agreements in the event of a breakdown of negotiations.
    - If the UK exits without an agreed deal with the EU, World Trade Organisation rules and tariffs could apply to trade between the UK and EU - but this is not certain.

- On full exit from the EU: the UK parliament would repeal the 1972 European Communities Act.
- The UK will then no longer participate in matters reserved for EU members, such as changes to the EU's budget, voting allocations and policies.

Eurozone –

- GDP in 2016 was (1.9%) and this positive momentum continues in 2017 with growth being reported as 0.5% in quarter 1 (2.0% y/y), 0.6% in quarter 2 (2.3% y/y) and 0.6% in quarter 3 (2.5% y/y);
- European Central Bank is still struggling to get inflation up to its 2% target and in October inflation (CPI) was 1.4%;
- Unemployment rate fell from 9.6% in January 2017 to 8.8% in October 2017;
- European Central Bank continues to hold its central policy rate at 0.00% where it has been since March 2016.

US –

- Growth in the American economy since 2015 has been inconsistent and it appears 2017 is following that path again with quarter 1 coming in at only 1.2% (2.0% y/y) with quarter 2 rebounding to 3.1% (2.2% y/y) and quarter 3 coming in at 3.0% (2.3%y/y);
- The Federal Reserve increased its interest rate from 0.75% at the beginning of the year to its current level of 1.25% in May 2017;
- Unemployment continues to fall starting at 4.8% in January 2017 falling to its lowest levels for many years, reaching 4.1% in October 2017,
- CPI fell from its starting position at 2.3% in January, to 1.8% in October 2017.

Other –

- China's economic growth appears to have slowed down from that reported in previous years with the annual growth reported in October 2017 of 6.8%.
- Japan continues to struggle to stimulate consistent significant growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus.

MAIN ECONOMIC FORECASTS FOR 2018

Producing accurate economic forecasts is difficult to do as a result of many external factors having an impact on them however forecasters are currently predicting the following levels of activity for the year ahead;

Indicator	UK	Eurozone	US	China
Growth Domestic Product	1.4%	2.3%	2.7%	6.5%
Consumer Price Index	2.4%	1.8%	2.4%	2.0%
Unemployment Rate	4.3%	8.5%	4.5%	4.3%
Bank Rate	0.75%	0.25%	1.75%	4.10%

Source - Trading Economics & Office for Budget Responsibility

APPENDIX 3

ELEMENTS FOR COUNCIL APPROVAL
(including Prudential and Treasury Indicators, Minimum Revenue Provision & Investment Criteria)

In accordance with the current MHCLG Guidance, CIPFA Treasury Management Code of Practice, each council is required to set before the commencement of each financial year Treasury Management Prudential Indicators and limits, a Minimum Revenue Provision Statement and Investment criteria.

The Accounts and Audit Committee and Executive are requested to recommend that Council approve these for the period 2018/19 – 2020/21 as detailed below.

TREASURY PRUDENTIAL INDICATORS AND LIMITS –

In accordance with the current CIPFA Prudential code, the Council is required to produce prudential indicators and limits reflecting the expected capital activity regarding its capital investment programme. These have an impact on the Council's treasury management activities and Council is required to approve the prudential indicators and limits affecting treasury management performance as shown below;

	2017/18 estimate £m	2018/19 estimate £m	2019/20 estimate £m	2020/21 estimate £m
Authorised Limit for External debt				
- External loan debt (01.04)	440.0	460.0	470.0	470.0
- Other long term Liabilities (PFI)	6.0	5.5	5.5	5.0
Total	**446.0**	**465.5**	**475.5**	**475.0**

Authorised external debt limit - maximum level of external debt that the authority will require for all known potential requirements and includes headroom to cover the risk of short-term cash flow variations that could lead to a need for temporary borrowing. This limit needs to be set or revised by Council and is the statutory limit determined under section 3(1) of the Local Government Act 2003.

	2017/18 estimate £m	2018/19 estimate £m	2019/20 estimate £m	2020/21 estimate £m
Operational Boundary for External debt				
- External loan debt (01.04)	420.0	440.0	450.0	450.0
- Other long term Liabilities (PFI)	6.0	5.5	5.5	5.0
Total	**426.0**	**445.5**	**455.5**	**455.0**

Operational boundary - calculated on a similar basis as the authorised limit but represents the likely level of external debt that may be reached during the course of the year excluding any temporary borrowing and is not a limit.

	2017/18 estimate £m	2018/19 estimate £m	2019/20 estimate £m	2020/21 estimate £m
Upper limit for Principal sums invested over 364 & 365 days	**90**	**90**	**90**	**90**

Upper Limit for sums invested for over 364 & 365 days – these limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment. Included within this limit are the Manchester Airport Shares which at 31 March 2017 were independently valued at £43.7m and the Church Commissioners Local Authorities Property Investment Fund investment of £5m. This limit also takes account of the proposed change in the CIPFA Treasury Code from a 364 day limit to 365 days.

	2017/18 estimate £m	2018/19 estimate £m	2019/20 estimate £m	2020/21 estimate £m
Upper limits on fixed interest rate exposure based on net debt	**6.1**	**13.7**	**14.2**	**14.7**
Upper limits on variable interest rate exposure based on net debt	**2.8**	**3.6**	**3.7**	**3.9**

Upper Interest Limits – identifies the maximum limit for both fixed and variable interest rates exposure based upon the Council's debt position net of investments.

Maturity structure of all external loan debt – 2018/19 to 2020/21	**Lower limit %**	**Upper limit %**
Under 12 months	0	20
12 months to 2 years	0	20
2 years to 5 years	0	20
5 years to 10 years	0	20
10 years to 20 years	0	20
20 years to 30 years	0	20
30 years to 40 years	0	20
40 years and above	0	90

Maturity Structure of Borrowing – these gross limits are set to reduce the Council's exposure to large sums falling due for refinancing and this indicator reflects the next date on which the lending bank can amend the interest rate for the Lender Option Borrower Option loans.

Gross Debt and the Capital Financing Requirement – this reflects that over the medium term, debt will only be for capital purposes. The Chief Finance Officer will ensure that all external debt does not exceed the capital financing requirement with any exceptions being reported to Council.

All the treasury prudential indicators and limits are monitored on a regular basis with any breaches being reported to Council at the earliest opportunity.

MINIMUM REVENUE PROVISION - (no change)

In accordance with the current MHCLG Guidance, the Council shall determine for the current financial year, an amount of minimum revenue provision that it considers to be prudent and submit an MRP Statement setting out its policy for its annual MRP to Council for approval. The following MRP Statement has been prepared in accordance with the Council's accounting procedures and is recommended for approval:

- Capital expenditure financed by Supported Borrowing: MRP will be calculated on a straight line basis over the expected average useful life of the assets (50yrs);
- Capital expenditure financed by Prudential Borrowing: MRP will be based on the estimated life of the assets and in accordance with MHCLG guidance;
- Expenditure incurred on the Capital Investment programme financed by Prudential Borrowing will be based on those periods outlined above stipulated within the MHCLG Guidance with annual reviews undertaken to ensure that this policy remains prudent;
- PFI schemes and leases shown on the balance sheet: MRP will be based on the amount of the principal element within the annual unitary service payment and financed from the provision set-up to cover the final bullet payment. Capital receipts are to be used to replenish this provision to ensure this final bullet payment can still be made in 2028/29
- For expenditure that does not create an asset, or following the use of a Capitalisation Direction: provision will be made over a period not exceeding 20 years, in accordance with the 2010 Guidance.
- In instances where the Council incurs borrowing and a third party is obliged to repay the principal (serviced debt arrangements): the Council will not charge MRP to the revenue account. An example of such an instance can be demonstrated when the Council participated in the national Local Authority Mortgage Scheme using the cash backed option with Lloyds bank. This involved the Council placing a five year deposit totalling £1m, in 2013/14, with the bank matching the five year life of the indemnities. This deposit provides an integral part of the mortgage lending, and is treated as capital expenditure and a loan to a third party. The CFRwill increase by the amount of the total indemnity. The deposit is due to be returned in full at maturity in 2018/19 and once received will be classed as a capital receipt, and the CFR will reduce accordingly. As this is a temporary (five years) arrangement and the funds will be returned in full, there is no need to set aside prudent provision to repay the debt liability in the interim period, so there is no MRP application.

INVESTMENT CRITERIA – (no change – Category 5)

Counterparty Selection

The Council will only use institutions which are located in a country with a minimum Sovereign Long term credit rating of AA-. The individual credit criteria, is highlighted below and for categories 1 to 4 this will be applied to both Specified and Non-specified investments. Category 5 applies only to The Church Commissioners Local Authorities Property Investment fund.

	Fitch (or equivalent) – Long Term	**Maximum Group Limit**	**Maximum Time Limit**
Category 1 – • UK & Non UK Banks (bank subsidiaries must have a parent guarantee in place), • UK Building Societies Institutions must have an individual credit rating issued by Fitch, Moody's and Standard and Poor's of: Short Term – Fitch F1 or equivalent Long Term – Fitch A- or equivalent	AA to AAA A+ to AA- A- to A	£75m £25m £10m	3yrs 1yr 1yr
Category 2 – UK Banks part nationalised - Royal Bank of Scotland. This bank or its subsidiaries can be included provided it continues to be part nationalised or meets the ratings in category1 above.	-	£20m	1yr
Category 3 – The Council's own banker for transactional purposes if the bank falls below the above criteria.	-	n/a	1day
Category 4 – • Pooled Investment Vehicles –e.g. Money Market Funds & Ultra Short Dated Bond Funds (formerly known as Enhanced Money Market Funds) - (AAA rated); • UK Government (including treasury bills, gilts and the DMO) • Local Authorities • Supranational Institutions	-	£100m	3yrs
Category 5 – • Local Authority Property Investment fund	-	£30m	10yrs

Specified and Non Specified Investments – (no change)

In accordance with the current Code of Practice, the Council is required to set criteria which identify its investments between Specified and Non Specified investments and these are classified as follows;

- Specified investments are high security and high liquidity investments with a maturity of no more than a year or those which could be for a longer period but where the Council has the right to be repaid within 12 months if it wishes. These are considered low risk assets where the possibility of loss of principal or investment income is small. All investments can be held under this definition,
- Non specified investments are any other type of investment not defined as specified above. A maximum of £90m is permitted to be held in this classification as detailed in Appendix 3, Prudential Indicator (5) Upper limit for sums invested over 364 and 365 days.

Instruments & Maximum period

All Investments will be undertaken in Sterling in the form of Term Deposits, Money Market Funds, Ultra Short Dated Bond Funds, Treasury Bills, Gilts or Certificates of Deposits unless otherwise stated below;

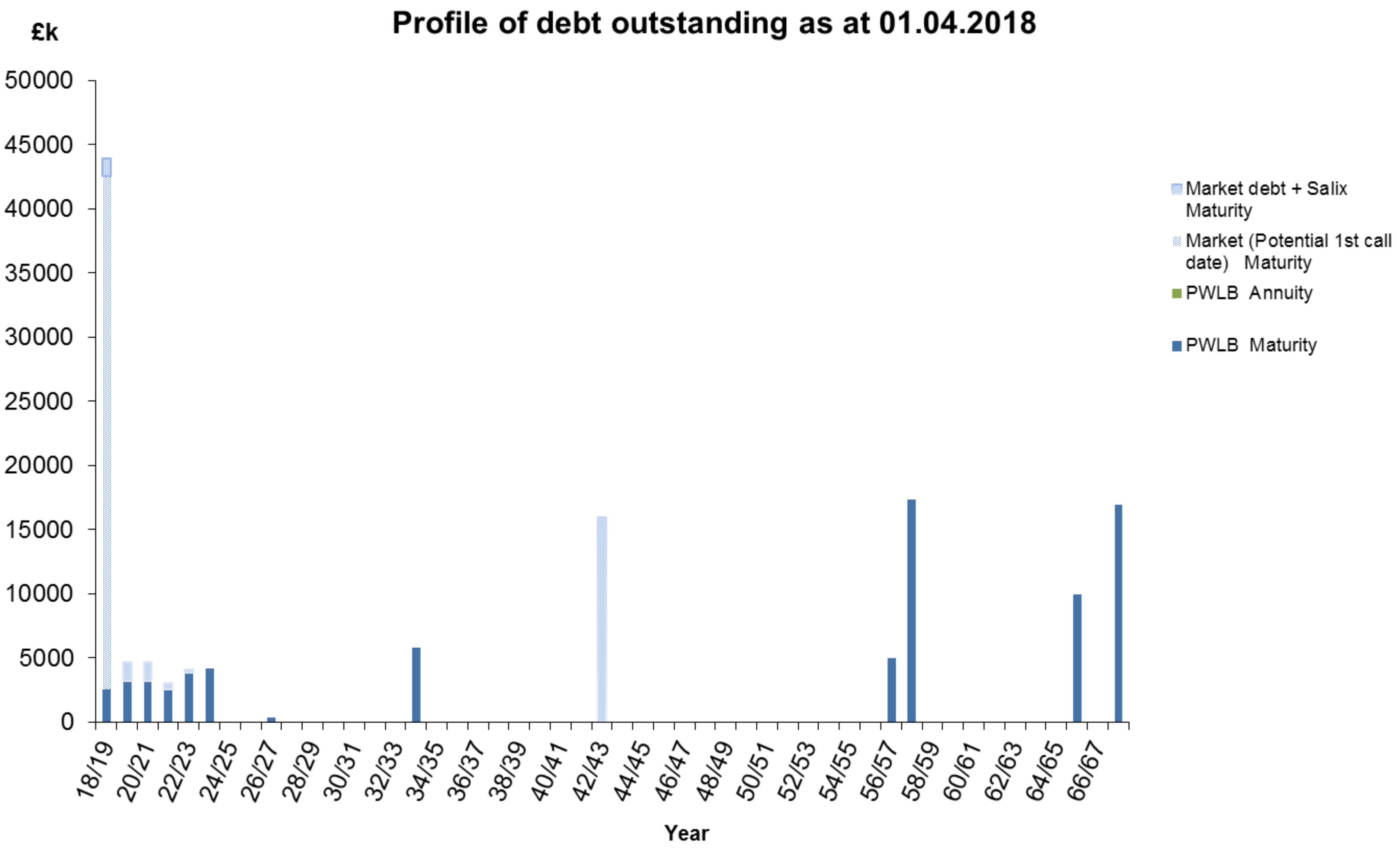
Specified Investments

Investment	Maximum Maturity
The UK Government including Local Authorities and Debt Management Office.	1 Year
Supranational bonds of less than one year duration (e.g. European Investment Bank)	1 Year
Pooled investment vehicles that have been awarded a AAA credit rating by Fitch, a credit rating agency, such as money market funds and low volatility bond funds.	1 Year
An institution that has been awarded a high short term credit rating (minimum F1 or equivalent) by a credit rating agency, such as a bank or building society.	1 Year

Non-Specified Investments

Investment	Maximum Maturity
Multilateral development bank bonds - These are bonds defined as an international financial institution having as one of its objects economic development, either generally or in any region of the world (e.g. European Investment Bank etc.). The security of principal and interest on maturity is on a par with the Government and these bonds usually provide returns above equivalent gilt edged securities. The value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.	3 Years
Gilt edged securities. These are Government bonds and provide the highest security of interest and principal. The value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.	3 Years

The Council's own bank if it fails to meet the basic credit criteria with balances being kept to a minimum.	1 Day
UK Banks which have significant Government holdings	1 Year
Any bank or building society which meets the minimum long term credit criteria detailed in Appendix 3, for deposits with a maturity of greater than one year (including forward deals in excess of 1 year from inception to repayment).	3 Years
The UK Government including Local Authorities and Debt Management Office.	3 Years
Any non-rated subsidiary of a credit rated institution included in the specified investment category. These institutions will be included as an investment category subject to being guaranteed from the parent company and is included for clarity and transparency purposes.	3 Years
Share capital or loan capital in a body corporate – The use of these instruments will be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. It is envisaged this facility will apply to the Manchester Airport share-holding which the Council holds at a historical value of £43.7m as reported in the 2016/17 Statement of Accounts. It is not envisaged that this type of investment will be undertaken in the future.	Unspecified
Manchester Airport Group – This is in response to the restructuring of the airports existing debt and is included for clarity and transparency purposes only.	Term of loans
Church Commissioners Local Authorities Property Investment Fund - This fund is aimed solely for use by public sector organisations wishing to invest in the property market whilst at the same time generating a favourable rate of return.	10 Years


Profile of debt outstanding as at 01.04.2018
£k
50000
45000
40000
35000
30000
25000
20000
15000
10000
5000
0
18/19
20/21
22/23
24/25
26/27
28/29
30/31
32/33
34/35
36/37
38/39
40/41
42/43
44/45
46/47
48/49
50/51
52/53
54/55
56/57
58/59
60/61
62/63
64/65
66/67
Year
Market debt + Salix Maturity
Market (Potential 1st call date) Maturity
PWLB Annuity
PWLB Maturity

APPENDIX 4

INVESTMENT CREDIT AND INSTITUTION RISK MANAGEMENT

The Council receives credit rating advice from its treasury management advisers, as and when ratings change and institutions are checked promptly to ensure it complies with the Council's criteria. The criteria used are such that any minor downgrading should not affect the full receipt of the principal and interest. Any institution failing to meet the criteria, or those on the minimum criteria placed on negative credit watch, will be removed from the list immediately, and if required new institutions which meet the criteria will be added to the list.

		Credit Rating Agency		
Classification	**Description**	**Fitch** **(Minimum)**	**Moody's** **(Minimum)**	**Standard & Poors (Minimum)**
Short Term	Ensures that an institution is able to meet its financial obligations within 12 months	F1 (Range **F1+, F2 A** to **D**)	P1 (Range **P1** to **P3**)	A1 (Range **A-1,** to **C**)
Long Term	Ensures that an institution is able to meet its financial obligations greater than 12 months	A- (Range **AAA** to **D**)	A3 (Range **AAA** to **C**)	A- (Range **AAA** to **CC**)

Investment Institution information.

Whilst the Council's Investment institutions list is prepared primarily using credit rating information, full regard will also be given to other available information on the credit quality of each institution in which it invests. The information below will continue to be considered when undertaking investments;

- Credit default swaps - CDS created in 1997 and are a financial instrument for swapping the risk of debt default. Essentially the owner of the position would enter into an agreement with a third party who would receive a payment in return for protection against a particular credit event – such as default. Whilst absolute prices can be unreliable, trends in CDS spreads do give an indicator of relative confidence about credit risk.
- Equity prices – like CDS prices, equities are sensitive to a wide array of factors and a decline in share price may not necessarily signal that the institution in question is in difficulty.
- Interest rates being paid - If an institution is offering an interest rate which is out of line with the rest of the market this could indicate that the investment is likely to carry a high risk.
- Information provided by management advisors – this may include some information detailed above together with weekly investment market updates.
- Market & Financial Press information – information obtained from the money market brokers used by the Council in respect of interest rates & institutions will also be considered.

No investment will be made with an institution if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

Investment Limits

In order to safeguard the Council's investments and in addition to the information shown at Appendix 3, due care will be taken to consider country, group and sector exposure as follows;

- **Country** – this will be chosen by the credit rating of the Sovereign state as shown at Appendix 3 and no more than 40% of the Council's total investments will be directly placed with non-UK counterparties at any time;
- **Group** – this will apply where a number of financial institutions are under one ownership (e.g. Royal Bank of Scotland / Nat West) and the Group limit will be the same as the individual limit for any one institution within that group;
- **Sector** limits will be monitored regularly for appropriateness.

Investment Risk benchmarking

Security and liquidity benchmarks are central to the approved treasury strategy through the institution selection criteria and proposed benchmarks for these are set out below.

Security - A method to benchmark security risk is to assess the historic level of default against the minimum criteria used in the Council's investment strategy. The table below shows average defaults for differing periods of investment grade products for each Fitch/Moody's and Standard and Poors long term rating category over the period 1981 to 2015.

Long term rating	Average 1 yr default	Average 2 yr default	Average 3 yr default	Average 4 yr default	Average 5 yr default
AAA	**0.04%**	**0.10%**	**0.18%**	**0.27%**	**0.37%**
AA	**0.01%**	**0.02%**	**0.08%**	**0.16%**	**0.23%**
A	**0.07%**	**0.19%**	**0.36%**	**0.55%**	**0.77%**
BBB	**0.15%**	**0.46%**	**0.82%**	**1.26%**	**1.73%**
BB	**0.70%**	**2.04%**	**3.48%**	**5.21%**	**6.71%**
B	**3.04%**	**7.14%**	**11.06%**	**14.40%**	**17.24%**
C	**19.73%**	**28.03%**	**33.43%**	**37.39%**	**40.41%**

The Council's minimum long term rating criteria is currently "A", meaning the average expectation of default for a one year investment in an institution with a "A" long term rating would be 0.07% of the total investment (e.g. for a £1m investment the average loss would be £700). This is only an average as any specific institution loss is likely to be higher.

Liquidity – The current CIPFA Treasury Management Code of Practice defines this as "*having adequate, though not excessive cash resources, borrowing arrangements, overdrafts or standby facilities to enable at all times to have the level of funds available which are necessary for the achievement of its business/service objectives*".

The availability of liquidity and the period of risk in the portfolio can be benchmarked by the monitoring of the Weighted Average Life (WAL) of the portfolio (shorter WAL would generally represent less risk).

APPENDIX 6

INVESTMENT & EXTERNAL DEBT POSITION AS AT 31.12.2017

	Principal £m	Average Rate %
DEBT		
Fixed rate:		
- PWLB	77.4	4.38
- Market	21.8	3.60
Sub-total	*99.2*	*4.21*
Variable rate:		
- PWLB	0.0	0.0
- Market	40.0	5.88
Sub-total	*40.0*	*5.88*
Total debt	**139.2**	**4.69**
INVESTMENTS		
- Fixed rate	(60.2)	0.54
- Variable rate	(15.3)	1.82
Total Investments	**(75.5)**	**0.80**
NET ACTUAL DEBT / (INVESTMENTS)	**63.7**	

APPENDIX 7

SUMMARY MEDIUM FINACIAL PLAN 2018/19-2020/21

	2018/19 £000	2019/20 £000	2020/21 £000
DEBT			
Interest & Premium	6,986	6,689	6,400
MRP	3,022	3,164	5,721*
Sub-total	**10,008**	**9,853**	**12,121**
INVESTMENTS			
Interest	(876)	(986)	(1,666)
MAG	(5,281)	(5,495)	(5,495)
Sub-total	**(6,157)**	**(6,481)**	**(7,161)**
RESERVES			
Contribution to Interest Smoothing Reserve **	158	200	100
Sub-total	**158**	**200**	**100**
TOTAL	**4,009**	**3,572**	**5,060**

The above figures exclude associated debt costs from any additional borrowing undertaken to fund the Councils Commercial Investment Programme as these will be self-financing.

*The increase in MRP reflects the completion of the 4 year realignment period whereby funds previously over provided are being placed into an Investment Fund.

**The estimated value of the reserve at 31 March 2018 is £492k and this is required to cover:-

- In year interest variations on the council's variable rate debt,
- Any adverse changes in investment interest rates and
- Any defaults on specific loan advances to third parties or adverse changes in value of other non-financial investments.