Report of the Section 151 Officer

Council – 24 February 2015

TREASURY MANAGEMENT STRATEGY, PRUDENTIAL INDICATORS, INVESTMENT STRATEGY AND MINIMUM REVENUE PROVISION POLICY STATEMENT 2015/16

Purpose:	To recommend the Treasury Management Strategy Statement, Prudential Indicators, Investment Strategy and Minimum Revenue Provision Policy Statement for 2015/16.
Policy Framework:	None
Reason for Decision:	To allow for the proper management of the Council's borrowing and investments, to comply with statute, and the adopted CIPFA Prudential Code for Capital Finance in Local Authorities and the Revised CIPFA Treasury Management Code of Practice
Consultation:	Legal, Finance & Delivery and Access to Services.
Recommendations:	That Council approves:- (1) Treasury Management Strategy and Prudential Indicators (Sections 2-7) and (2) Investment Strategy (Section 8) and (3) Minimum Revenue Provision (MRP) Statement (Section 9)
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Legal Officer:	Tracey Meredith
Access to Services Officer:	Sherill Hopkins

1. Introduction

1.1 This strategy statement has been prepared in accordance with the revised CIPFA Treasury Management Code of Practice adopted by this Council in 2010. The Council's Treasury Management Strategy will be received and reviewed annually by Council and there will also be a mid year report providing an interim update. The aim of these reporting arrangements is to ensure that those with ultimate responsibility for the scrutiny of the Treasury Management function appreciate fully the implications of Treasury Management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

1.2 Revised CIPFA Prudential Code

CIPFA has issued a revised Prudential Code which primarily covers borrowing and the Prudential Indicators. Three of these indicators have now been moved from being Prudential Indicators to being Treasury Indicators: -

- authorised limit for external debt
- operational boundary for external debt
- actual external debt.

However, all indicators are to be presented together as one suite. In addition, where there is a significant difference between the net and the gross borrowing position, the risks and benefits associated with this strategy should be clearly stated in the annual strategy report.

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

The Council is required to formally consider the Prudential and Treasury Indicators as detailed in section 2 of this report

1.4 The Act also requires the Council to set out its Treasury Strategy for borrowing and to prepare an Annual Investment Strategy as required by Investment Guidance issued subsequent to the Act. This strategy sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments. The management of the Council's Treasury Management activities are in line with the CIPFA Treasury Management Revised Code of Practice.

1.5 The recommended strategy for 2015/16 is based upon a view on interest rates, having considered leading market forecasts provided by the Council's treasury advisor, Capita Asset Services. The overall strategy covers:

- Treasury Limits 2015/16-2018/19
- Prudential / Treasury Indicators
- The current portfolio position
- Prospects for interest rates including a summary of the economic background
- The Borrowing Requirement
- The Borrowing Strategy

    - Gross v Net Debt Position
    - Policy on Borrowing in Advance of Need
- Debt Rescheduling
- The Annual Investment Strategy
    - Investment Policy
    - Interest Rate Outlook
    - Creditworthiness Policy
    - Country Limits
    - Policy on the Use of External Advisors
    - Scheme of Delegation
    - Pension Fund Cash
- Minimum Revenue Provision (MRP) Policy Statement

1.6 A glossary of terms used within this report is attached at Appendix A.

2. Treasury Limits 2015/16 to 2018/19

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

- increases in capital finance charges (principal and net interest) caused by increased borrowing to finance additional capital expenditure and

- any increases in running costs from new capital projects

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

2.2 Under statute, the Council is required to set an Affordable Borrowing Limit i.e a limit which the Council can afford to borrow. In Wales, the Authorised Limit represents the legislative limit specified in section 3 of the Local Government Act 2003.

2.3 The Council must have regard to the Prudential Code when setting the Authorised Limit . This limit requires the Council to ensure that total capital investment remains within sustainable limits. The Authorised Limit must be set for the forthcoming financial year and the two successive financial years.

2.4 The Prudential Code for Capital Finance in Local Authorities requires Councils to calculate treasury indicators (formerly prudential indicators) which demonstrate prudence in the formulation of borrowing proposals. These are defined as:

- The Operational Boundary :
  "…is based on expectations of the maximum external debt of the authority according to probable not simply possible events and being consistent with the maximum level of external debt projected by the estimates…."

- The Authorised Limit :
  "..t*he Authorised Limit must therefore be set to establish the outer boundary of the local authority's borrowing based on a realistic assessment of the risks. The authorised limit is certainly not a limit that an authority will expect to borrow up to on a regular basis. It is crucial that it is not treated as an upper limit for borrowing for capital expenditure alone since it must also encompass borrowing for temporary purposes..."*

- Upper limits for borrowing of fixed and variable rate loans.
- Upper limit for investments for over 364 days.
- Upper and lower limits for the maturity profile of the Council's debt
- Estimates of the incremental impact of capital investment decisions on Council Tax / Housing rents
- Estimates of the ratio of financing costs to net revenue stream
- Estimates of the capital financing requirement

In setting and revising Prudential Indicators the authority is required to have regard to:-

- Affordability e.g. implications for Council Tax / Housing rents
- Prudence and sustainability e.g. implications for external borrowing
- Value for money e.g. option appraisals
- Stewardship of assets e.g. strategic planning
- Practicality e.g. achievability of forward plans

It is a requirement of the Code that Prudential / Treasury Indicators are regularly monitored and systems are in place to achieve compliance.

Treasury / Prudential Indicators						
	2013/14	**2014/15**	**2015/16**	**2016/17**	**2017/18**	**2018/19**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
	Actual	**Probable**	**Estimate**	**Estimate**	**Estimate**	**Estimate**
Capital Expenditure						
GF	59,047	89,202	43,902	31,394	19,059	17,687
HRA	24,981	26,907	136,293	44,000	41,500	42,000
TOTAL	**84,028**	**116,109**	**180,195**	**75,394**	**60,559**	**59,687**
Capital Financing Requirement ***						
GF	314,815	335,153	339,718	336,108	331,205	326,245
Credit Arrangements *	2,600	2,895	1,436	1,225	809	445
HRA	66,378	64,450	160,561	169,750	178,755	188,179
Magistrates' Court **	1,595	1,531	1,470	1,411	1,354	1,300
TOTAL	**385,388**	**404,029**	**503,185**	**508,494**	**512,123**	**516,169**
Authorised limit for external debt	£527,220	£597,269	£601,314	£605,724	£605,724	£605,724
Operational boundary for external debt	£445,829	£547,269	£551,314	£555,724	£555,724	£555,724
Upper limit for fixed interest rate exposure	100%/ £527,220	100%/ £597,269	100%/ £601,314	100%/ £605,724	100%/ £605,724	100%/ £605.724
Upper limit for variable rate exposure	40%/ £210,888	40%/ £238,908	40%/ £240,526	40%/ £242,290	40%/ £242,290	40%/ £242,290
Upper limit for total principal sums invested for over 364 days	£75,000	75,000	40,000	40,000	40,000	40,000

* The GF Capital Financing Requirements includes arrangements classified as credit arrangements (finance leases) under International Financial Reporting Standards (IFRS) requirements as of 2011/12. However these continue to be funded directly on a revenue basis and do not form part of the borrowing requirement.

** Legacy Magistrates' Court debt which is recharged is included for completeness

*** Excludes potential additional borrowing if forecast capital budget shortfalls can not be resolved in future years

Maturity structure of fixed rate borrowing during 2014/15-2018/19		
	Upper limit %	**Lower limit %**
Under 12 months	50	0
12 months and within 24 months	50	0
24 months and within 5 years	50	0
5 years and within 10 years	85	0
10 years and above	95	15

Ratio of Financing Costs to Net Revenue Stream						
	Actual 2013/14 %	**Revised 2014/15 %**	**Estimate 2015/16 %**	**Estimate 2016/17 %**	**Estimate 2017/18 %**	**Estimate 2018/19 %**
General Fund	7.24	6.58	7.00	7.26	7.47	7.67
HRA	9.04	7.96	13.39	16.98	17.57	18.20

Estimates of Incremental Impact of Capital Investment Decisions on Council Tax (Band D) and Council Housing Rents						
	Actual 2013/14 £	**Revised 2014/15 £**	**Estimate 2015/16 £**	**Estimate 2016/17 £**	**Estimate 2017/18 £**	**Estimate 2018/19 £**
General Fund*	70.50	87.23	98.02	105.87	104.81	103.23
HRA*	0.00	0.00	43.94	111.43	181.35	250.92

*It should be noted that in formulating the two above indicators it is necessary to hypothecate funding (in this case council tax and housing rents) to specific areas of capital expenditure, however in reality the complete spectrum of funding resource is utilised in funding capital expenditure as appropriate.

<u>Gross Debt v Capital Financing Requirement</u>

The gross debt position versus the capital financing requirement is detailed below. The profile below assumes progressive external funding of the internalised borrowing and the budgeted use of reserves as profiled in the revenue budget report.

Comparison of average gross debt and capital financing requirement	**2013/14**	**2014/15**	**2015/16**	**2016/17**	**2017/18**	**2018/19**
	actual	**probable**	**estimate**	**estimate**	**estimate**	**estimate**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Average debt (gross)	325,110	315,407	418,643	436,903	455,198	473,527
Capital Financing Requirement	382,788	401,134	501,749	507,269	511,314	515,724
Net Position	57,678	85,727	83,106	70,366	56,116	42,197

3 . The current portfolio position

3.1 The Council's probable debt portfolio position at 31/3/15 comprises:

	Principal outstanding 31 March 2015 £'000	Average rate of Interest %
Public Works Loan Board (fixed)	212,981	6.10
Money Market	98,000	4.10
Temporary	1,992	0.60
TOTAL	312,973	5.45

3.2 The Council's forecast investment portfolio at 31 March 2015 is as follows:

Managed investments	Investments 31 March 2015	2014/15 Estimated Investment Return	2015/16 Estimated Investment Return
	£'000	%	%
Internally Managed	105,686	0.59	0.60

4. Prospects for Interest Rates

4.1 The Council's Treasury advisers (Capita Asset Services) provided the following interest rate forecast for both short term (bank rate) and long term (PWLB) interest rates as at 16th January 2015. There is a downside risk to these forecasts if economic growth proves to be weaker and slower than currently forecast.

Annual Average %	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)		
		5 year	25 year	50 year
Mar 2015	0.50	2.20	3.40	3.40
Jun 2015	0.50	2.20	3.50	3.50
Sep 2015	0.50	2.30	3.70	3.70
Dec 2015	0.75	2.50	3.80	3.80
Mar 2016	0.75	2.60	4.00	4.00
Jun 2016	1.00	2.80	4.20	4.20
Sep 2016	1.00	2.90	4.30	4.30
Dec 2016	1.25	3.00	4.40	4.40
Mar 2017	1.25	3.20	4.50	4.50
Jun 2017	1.50	3.30	4.60	4.60
Sep 2017	1.75	3.40	4.70	4.70
Dec 2017	1.75	3.50	4.70	4.70
Mar 2018	2.00	3.60	4.80	4.80

4.2 Economic Background

Attached at Appendix B is an economic background assessment provided by our Treasury advisers, Capita Asset Services. This assessment has informed the proposed strategies .

5. The Borrowing Requirement

5.1 The Council will have the following net capital borrowing / repayment requirements for 2014/15 to 2018/19 :

	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19
Borrowing and repayment requirements	**Actual**	**Probable**	**Estimate**	**Estimate**	**Estimate**	**Estimate**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
To finance new capital expenditure by supported borrowing	6,227	6,356	6,356	6,356	6,356	6,356
To finance new capital expenditure supported by Local Authority Government Borrowing Initiative (highways)	2,648	5,861		-	-	-
To finance new capital expenditure by unsupported borrowing	8,269	23,523	12,415	4,339	3,047	2,946
To finance HRA capital expenditure/HRA Subsidy Reform 2015/16			98,000	13,000	13,000	13,000
To replace loans maturing/repaid prematurely	6,283	7,323	3,189	286	9,002	1
Less						
Repayments (MRP)	14,122	14,706	15,556	17,575	17,757	17,891
Set aside capital receipts	1,237	600	600	600	600	600
NET BORROWING /(REPAYMENT) REQUIREMENT	**8,068**	**27,757**	**103,804**	**5,806**	**13,048**	**3,812**
Principal repayment element of finance lease payments	876	915	559	288	235	240

5.2 The above table details the net borrowing requirement for each financial year. In accordance with the Prudential Code, borrowing must be undertaken in line with a funding plan informed by the projected capital financing requirement. Borrowing may be financed from one or more of Public Works Loan Board loans; Money Market loans or internal loans. The precise choice will depend on market conditions from time to time.

5.3 At time of writing, borrowing rates are materially higher then investment rates and it is projected that the remaining borrowing requirement for 2014/15 will be met from internal loans i.e it will be internalised. However, we will continue to appraise market conditions and opportunities to start to externalise debt to fund the capital programme when borrowing rates offer long term value during 2015/16 and as cashflow requirements dictate with a view to begin averaging in the total borrowing requirement in 2015/16 and the succeeding years.

Short term savings (by avoiding new long term external borrowing) will be weighed against the potential additional long term extra costs (by delaying unavoidable new external borrowing until later when PWLB long term rates are forecast to be marginally higher).

5.4 Housing Revenue Account (HRA) Subsidy Reforms - Self Financing Settlement

As outlined in the report approved by Council on 2nd Dec 2014 entitled *"Reform of the Housing Revenue Account Subsidy System"* , the Authority has entered into a Voluntary Agreement with Welsh Government to exit the current HRA subsidy system, resulting in more flexibility for the Authority in meeting affordable housing needs in the locale. In order to exit the current HRA subsidy system, a cash settlement amount must be paid over to HM Treasury equal to a sum determined by formulae agreed in the Voluntary Agreement which will result in a likely settlement figure in the range of between £70m and £100m for this Authority. The overriding principle of the HRA Reform is that all local housing authorities will be financially better off in revenue terms after the reforms.

The requirement for the HRA reform settlement to be made to the Welsh Government on 1 April 2015 will require a separate borrowing strategy dictated by the terms outlined in the Voluntary Agreement. The Council will need to have the cash settlement amount of between £70m and £100m available by the 2 April 2015, so separate borrowing solely for this purpose is anticipated. The exact structure of loans to be drawn is currently being considered by officers in consultation with Welsh Governement and HM Treasury to ensure it meets the requirements of the HRA business plan and the overall requirements of the Council.

6. Borrowing Strategy

6.1 Long term borrowing rates are expected to be significantly higher than rates available for investment deposits. It is likely that this position will continue over the short to medium term.

In addition, the continuing uncertain economic conditions has maintained the need for caution in managing credit counterparty risk. There is still a risk of a bank / institution defaulting on the payment of interest due or repayment of amounts invested.

6.2 Taking the above points together, it is not proposed to undertake any new long term external borrowing for the remainder of 2014/15. The main strategy - with a view to minimising interest costs and the risk of default by counterparties - is therefore to continue to internalise the majority of the borrowing requirement for 2015/16 with a view to begin externalising some of the borrowing requirement on a averaged basis in 2015/16 as the changing interest rates and more importantly, cashflows dictate.

Notwithstanding the general strategy above, the Authority is required to undertake the borrowing identified in 5.4 above as part of the HRA Self Financing Voluntary Agreement at pre determined rates as part of the HRA reforms in April 2015.

We will continue to monitor PWLB rates i.e if rates offer long term value in the context of market rates and the current debt portfolio, then further tranches of the identified borrowing requirement will be undertaken

6.4 Policy on borrowing in advance of need

The Council has only a limited power to borrow in advance of need.

In determining whether borrowing will be undertaken in advance of need the Council will;

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to borrow in advance of need
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow
- consider the merits and demerits of alternative forms of funding
- consider the alternative interest rate bases available, the most appropriate periods to fund and which repayment profiles to use.

7 Debt Rescheduling

7.1 The introduction of different PWLB rates on 1 November 2007 for new borrowing (as opposed to early repayment of debt) and the setting of a spread between the two rates (of about 0.4%-0.5% for the longest period loans narrowing down to 0.25%-0.30% for the shortest loans), has meant that PWLB to PWLB debt restructuring is now much less attractive than before that date.

7.2 Due to short term borrowing rates being expected to be considerably cheaper than longer term rates, there may be opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of their short term nature and the likely cost of refinancing short term loans, once they mature, compared to the current rates of longer term debt in the existing debt portfolio

7.3 In actively managing credit counterparty and interest rate risks, consideration will also be given to running down investment balances by repaying debt prematurely as short term rates on investments are likely to be significantly lower than rates paid on current debt.

However, a repayment strategy will only be considered if a loan repayment offers value in terms of discount / associated costs and does not compromise the Council's long term debt management policies. In this respect, we will need to be mindful of the potential future need to arrange new long term loans as market conditions change from time to time.

7.4 Notwithstanding the above, it is not envisaged that there will any debt rescheduling opportunities in the remainder of 2014/15 or 2015/16 in the PWLB portfolio, however there may be opportunities to review the Authority's market debt. All rescheduling decisions will be reported to the Cabinet Member for Finance & Strategy & Strategy in the quarter following action.

8. The Annual Investment Strategy

8.1 <u>Investment policy</u>

8.1.1 The Council will have regard to the National Assembly of Wales' Guidance on Local Government Investments ("the Guidance") issued in March 2004 (and subsequent amendments); CIPFA's Revised Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA Treasury Management Code") and the Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2004 SI 1010(W.107). The Council's investment priorities are: -

(a) to ensure the security of capital
(b) to ensure the liquidity of investments.
(c) to maximise interest returns (yield) commensurate with (a) and (b)

The investment strategy will be implemented with security of investment as the main consideration. The Council will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity.

8.1.2 Investment instruments identified for use in the financial year are listed in Appendix C under the 'Specified' and 'Non-Specified' Investments categories. Operational investment limits with individual institutions will be as set through the Council's Operational Treasury Management Practices.

8.1.3 Amendments to the arrangements, limits and criteria detailed in Appendix C may be made by the Head of Finance & Delivery and advised to the Cabinet Member for Finance & Strategy in the quarter following action.

Appendix G is the list of UK financial institutions (counterparties) which satisfy the Council's minimum credit criteria as at 16th January 2015.

8.1.4 The Council has retained the services of two external fund managers.. They are Investec Asset Management - who currently have no Council assets under management - and Invesco Investment Management. The fund managers will comply with the Annual Investment Strategy. The fund managers investment criteria are outlined in Appendix C. it is projected that the investments held by Invesco, approximately £22m will be fully realised by year end 2014/15.

8.1.5 It is anticipated that the Council will continue to hold internally managed funds during 2015/16 ensuring a suitable spread of investment risks. The performance of the investments will be reported. The Council has fixed benchmarks against which investment performance will be measured, i.e. 7 day LIBID rate (internally managed).

8.1.6 Interest Rate Outlook:
Bank Rate is forecast by the Council's advisors to remain unchanged at 0.5% before starting to rise in quarter 2 of 2015. Bank Rate forecasts as at 31st March are:

- 2015/16 0.75%
- 2016/17 1.25%
- 2017/18 2.00%

There are downside risks to these forecasts (i.e. start of increases in Bank Rate occurs later) if economic growth weakens. However, should the pace of growth quicken, there could be an upside risk.

8.1.7 For its cash flow generated balances, the Council will seek to utilise its business reserve accounts and short-dated deposits (1-3 months) in order to benefit from the compounding of interest. However longer dated deposits will be made with appropriate counterparties if opportunities arise.

8.1.8 During and following the end of the financial year, the Council will report on its investment activity as part of its Mid Term Treasury Management Report and its Annual Treasury Management Report.

8.2 Creditworthiness Policy
This Council uses the creditworthiness service provided by our Treasury Management Advisors. This service has been progressively enhanced over the years and now uses a sophisticated modelling approach with credit ratings from all three rating agencies. Fitch, Moodys and Standard & Poors form the core element.

Appendix D details Fitch's short and long term ratings.

The creditworthiness service does not rely solely on the current credit ratings of counterparties but also uses the following as overlays: -

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

This modelling approach combines credit ratings, credit watches, credit outlooks and CDS spreads in a weighted scoring system. The end product is a series of colour code bands which indicate the relative creditworthiness of counterparties. These colour codes are also used by the Council to determine the duration for investments.

All credit ratings will be monitored daily with reference to the credit ratings report and updates**.** The Council is alerted to changes to ratings of all three agencies through its use of the Sector creditworthiness service.

There will be no future use of a counterparty/investment scheme which fails the credit rating tests .

In addition to the use of credit ratings the Council will be advised of information in movements in Credit Default Swaps against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in the downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition the Council will also use market data, market information, information on government support for banks and the credit ratings of that government support.

8.3 <u>Country Limits</u>

The Authority has not made any new overseas deposits for several years. Going forward, extreme caution will be required when considering future opportunities to make overseas investments. There are no plans to make overseas investments at this time.

If such opportunities arise then the Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide a rating) The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix E. This list will be added to or deducted from should ratings change in accordance with this policy.

8.4 <u>Policy on the use of external advisers</u>

The Council uses the services of an external Treasury Management adviser namely - Capita Asset Services Treasury Management Advisors.

The Council recognises that responsibility for Treasury Management decisions remains with the Council at all times and as such, we will ensure that undue reliance is not placed upon external advisers.

However it is recognised that there is value in employing external advisers in relation to 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.

8.5 <u>Scheme of Delegation</u>

The role and responsibilities of the Council, Cabinet Member for Finance & Strategy and the s151 officer are as follows:

(i) Council

- to receive and review reports on Treasury Management policies, practices and activities
- to receive and review the annual strategy.
- to receive and review amendments to the Authority's adopted clauses, Treasury Management policy statement and Treasury Management practices
- to consider and approve the annual budget
- to receive and review the division of responsibilities

(ii) Cabinet Member for Finance & Strategy

- to receive and review regular briefings/reports
- to receive and review the Treasury Management policy and procedures

(iii) Section 151 Officer

- to recommend clauses, Treasury Management policy/practices for approval
- to review the same regularly and monitor compliance
- to submit regular Treasury Management policy reports
- to submit budgets and budget variations
- to receive and review management information reports
- to review the performance of the Treasury Management function
- to ensure the adequacy of Treasury Management resources and skills, and the effective division of responsibilities within the Treasury Management function
- to ensure the adequacy of internal audit, and liaise with external audit
- to recommend the appointment of external service providers.

8.6 <u>Pension Fund Cash</u>
The Council will comply with the requirements of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 which was implemented on 1st January 2010. Any investments made by the Pension Fund will comply with the requirements of SI 2009 No 393 and will comply with the prevailing City & County of Swansea Treasury Management Policies, Practices and Strategies.

9. Minimum Revenue Provision Policy Statement

9.1 Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, machinery. It is inappropriate to charge the entirety of this expenditure in the year in which it is incurred i.e the expenditure benefits more than a single year of account. As such, the resulting costs are spread over several years. The manner of spreading these costs is through an annual Minimum Revenue Provision (MRP) which was previously determined under Regulation and now is determined under Guidance.

9.2 Statutory instrument WSI 2008 no.588 section 3 states that "..a local authority must calculate for the current financial year an amount of minimum revenue provision which it considers to be prudent,,"

The previous requirement to make a 2% MRP charge for the Housing Revenue Account share of the Capital Financing Requirement (CFR) is unchanged by this instrument.

9.3 Along with the above duty, the Welsh Assembly Government issued guidance in March 2008 which requires that a Statement on the Council's Policy for its annual MRP should be submitted to the full Council for review before the start of the financial year to which the provision will relate. The Council is legally obliged to 'have regard' to the guidance.

9.4 The Welsh Assembly Government guidance outlined four broad options to adopt for the calculation of MRP. They are:

- Option 1- Regulatory Method
- Option 2 - Capital Financing Requirement Method
- Option 3 - Asset Life Method
- Option 4 – Depreciation Method

The options are detailed at Appendix F.

9.5 The Council implemented the new Minimum Revenue Provision (MRP) guidance in 2008/09 and will calculate the MRP for 2014/15 in accordance with the main recommendations contained within the guidance issued by the Secretary of State under section 21(1A) of the Local Government Act.

9.6 The major proportion of the MRP chargeable will relate to the more historic debt liability that will continue to be charged at the rate of 4%, in accordance with option 1 or 2 of the guidance.

Certain expenditure reflected within the debt liability at 31st March 2014 will under delegated powers be subject to MRP under option 3 or 4 which will be charged over a period commensurate with the estimated useful life applicable to the nature of expenditure.

Estimated life periods will be determined under delegated powers. The Section 151 Officer reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate.

Going forward, it is proposed that all debt arising from capital expenditure supported by the WG will be charged MRP in accordance with option 1 or 2 and all other capital expenditure and other 'capitalised' expenditure will be repaid under option 3 or 4 as deemed most appropriate.

10 Legal Implications

10.1 The Authority is under a duty to make arrangements for the proper administration of its financial affairs. Failure to do so will be a breach of that duty. The statutory provisions and guidance imposing such a duty on the Authority are as set out in the main body of the Report.

11. Equality Impact Implications

11.1 There are no equality impact implications arising from this report

Background papers: The revised CIPFA Treasury Management Code of Practice 2011

The revised CIPFA Prudential Code for Capital Finance in Local Authorities 2011

Appendices:
Appendix A – Glossary of Terms
Appendix B – Treasury Advisors' View On The Economic Background
Appendix C – Investment Criteria for Specified & Non Specified Investments
Appendix D – Credit Rating Agency Definitions
Appendix E – Approved Countries for Investment
Appendix F Minimum Revenue Provision Guidance
Appendix G – Approved Internal Counterparty Lending List

APPENDIX A

TREASURY MANAGEMENT – GLOSSARY OF TERMS

Annualised Rate of Return	Represents the average return which would have been achieved each year.
Authorised Limit ***(can also be considered as the affordable borrowing limit)***	The authorised limit must be set to establish the outer boundary of the local authority's borrowing based on a realistic assessment of the risks. The authorised limit is certainly not a limit that an authority will expect to borrow up to on a regular basis. It is crucial that it is not treated as an upper limit for borrowing for capital expenditure alone since it must also encompass borrowing for temporary purposes. It is the expected maximum borrowing need, with some headroom for unexpected movement.
Bank Rate	The Official Bank rate paid on commercial bank reserves i.e. reserves placed by commercial banks with the Bank of England as part of the Bank's operations to reduce volatility in short term interest rates in the money markets.
Base Rate	Minimum lending rate of a bank or financial institution in the UK.
Basis Points (bp)	A basis point is 0.01 of 1% (100 bp = 1%)
Borrowing	In the Code, borrowing refers to external borrowing. Borrowing is defined as both:- • Borrowing repayable with a period in excess of 12months • Borrowing repayable on demand or within 12months
Capital Expenditure	The definition of capital expenditure starts with all those items which can be capitalised in accordance with the Statement of Recommended Practice (SORP). To this must be added any items that have/will be capitalised in accordance with legislation that otherwise would not be capitalised. Prudential indicators for current and future years are calculated in a manner consistent with this definition.

Capital Financing Charges (see financing costs also)	These are the net costs of financing capital i.e. interest and principal, premium less interest received and discounts received.
Capital Financing Requirement	The Capital Financing Requirement is simply the total outstanding capital expenditure, which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need.
CIPFA	The Chartered Institute of Public Finance and Accountancy. One of the leading professional accountancy bodies in the UK and the only one which specialises in the public services.
Counterparty	The organisations responsible for repaying the Council's investment upon maturity and for making interest payments.
Credit Rating	This is a scoring system that lenders issue people with to determine how credit worthy they are. The Credit Rating components are as follows: 1. The AAA ratings through to C/D are long-term rating definitions and generally cover maturities of up to five years, with the emphasis on the ongoing stability of the institution's prospective financial condition. AAA are the most highly rates, C/D are the lowest. This Council does not invest with institutions lower than AA- for investments over 364 days 2. F1/A1/P1 are short-term rating definitions used by Moody's, S&P and Fitch Ratings for banks and building societies based on their individual opinion on an institution's capacity to repay punctually its short-term debt obligations (which do not exceed one year). This Council does not invest with institutions lower than F1/A1/P1 for investments under 364 days.
Debt	For the purposes of the Code, debt refers to the sum of borrowing (see above) and other long-term liabilities (see below). It should be noted that the term borrowing used with the

	Act includes both borrowing as defined for the balance sheet and other long terms liabilities defined as credit arrangements through legislation.
Discounts	Where the prevailing interest rate is higher than the fixed rate of a long-term loan, which is being repaid early, the lender can refund the borrower a discount. This is calculated on the difference between the two interest rates over the remaining years of the loan, discounted back to present value. The lender is able to offer the discount, as their investment will now earn more than when the original loan was taken out.
Financing Costs	The financing costs are an estimate of the aggregate of the following:- • Interest payable with respect to borrowing • Interest payable under other long-term liabilities • Gains and losses on the repurchase or early settlement of borrowing credited or charged to the amount to be met from government grants and local taxpayers (premiums and discounts) • Interest earned and investment income • Amounts required in respect of the minimum revenue provision plus any additional voluntary contributions plus any other amounts for depreciation/impairment that are charged to the amount to be met from government grants and local taxpayers
Financial Reporting Standards (FRSs)	These are standards set by governing bodies on how the financial statements should look and be presented.
Investments	Investments are the aggregate of:- • Long term investments • Short term investments (within current assets) • Cash and bank balances including overdrawn balances From this should be subtracted any investments that are held clearly and explicitly in the course of the provision of, and for the purposes of, operational services.

IMF	International Monetary Fund
LOBO (Lender's Option/ Borrower's Option	Money Market instruments that have a fixed initial term (typically one to ten year) and then move to an arrangement whereby the lender can decide at pre-determined intervals to adjust the rate on the loan. At this stage the borrower has the option to repay the loan.
London Inter-Bank Bid Rate (LIBID)	The interest rate at which major banks in London are willing to borrow (bid for) funds from each other.
Managed Funds	<u>In-House Fund Management</u> Surplus cash arising from unused capital receipts and working cashflows can be managed either by external fund managers or by the Council's staff in-house. The in-house funds are invested in fixed deposits through the money markets for periods up to one year. <u>Externally Management Funds</u> Fund managers appointed by the Council invest surplus cash arising from unused capital receipts in liquid instruments such as bank certificates of deposit and government stocks. The fund managers' specialist knowledge should ensure a higher rate of earnings on the managed funds than would be otherwise obtained.
Maturity	The date when an investment is repaid or the period covered by a fixed term investment.
Minimum Revenue Provision (MRP)	The amount required by statute to be principal repayment each year.
Monetary Policy Committee (MPC)	This is a body set up by the Government in 1997 to set the repo rate (commonly referred to as being base rate). Their primary target (as set by the Government) is to keep inflation within plus or minus 1% of a central target of 2% in two year time from the date of the monthly meeting of the Committee. Their secondary target is to support the Government in maintaining high and stable levels of growth and employment.
Money Market	Consists of financial institutions and deals in

	money and credit. The term applied to the institutions willing to trade in financial instruments. It is not a physical creation, but an electronic/telephone one.
Net Borrowing	For the purposes of the Code, net borrowing refers to borrowing (see above) net of investments (see above).
Net Revenue Stream	Estimates for net revenue stream for current and future years are the local authority's estimates of the amounts to be met from government grants and local taxpayers.
Operational Boundary	This is based on expectations of the maximum external debt of the authority according to probable not simply possible – events and being consistent with the maximum level of external debt projected by the estimates. It is not a limit and actual borrowing could vary around this boundary for short periods.
Other Long Term Liabilities	The definition of other long term liabilities is the sum of the amounts in the Council's accounts that are classified as liabilities that are for periods in excess of 12months, other than borrowing (see definition above).
Premature Repayment of Loans (debt restructuring/rescheduling)	A facility for loans where the Council can repay loans prior to the original maturity date. If the loan repaid has a lower interest rate than the current rate for a loan of the same maturity period the Council can secure a cash discount on the repayment of the original loan. If the loan replaced has a higher rate of interest than the current rate for a loan of the same maturity period, a cash penalty is payable to the lender.
Premia	Where the prevailing current interest rate is lower than the fixed rate of a long term loan, which is being repaid early, the lender can charge the borrower a premium. This is calculated on the difference between the two interest rates over the remaining years of the loan, discounted back to present value. The lender may charge the premium, as their investment will now earn less than when the

	original loan was taken out.
Prudential Code	The Prudential Code is the largely self regulatory framework outlined by CIPFA for managing/monitoring capital investment in local government.
Public Works Loan Board (PWLB)	A Government agency which provides loans to local authorities. Each year, it issues a circular setting out the basis on which loans will be made available. Loans can be either at a fixed rate or on a variable rate basis. They can be repaid on either an annuity, equal instalment of principal or maturity basis. The interest rate charged is linked to the cost at which the Government itself borrows.
Risk	<u>Counterparty Credit Risk</u> The risk that a counterparty defaults on its obligations. <u>Inflation Risk</u> The risk that growth in the Authority's investment income does not keep pace with the effects of inflation on its expenditure. <u>Interest Rate Risk</u> The risk that changes in rates of interest creates an unexpected or unbudgeted burden on the Council's finances. <u>Liquidity Risk</u> The risk that cash will not be available when it is needed. <u>Operational Risk</u> The risk of loss through fraud, error, corruption, system failure or other eventualities in Treasury Management dealings, and failure to maintain effective contingency management arrangements. <u>Refinancing Risk</u> The risk that the Authority is unable to replace its maturing funding arrangements on appropriate terms.
Set Aside Capital Receipts	A proportion of money received by the Council for the sale of fixed assets must be set aside to repay debt.

SORP	Statement of Recommended Practice, published by CIPFA (Local Authority Accounting Body). This sets out guidelines regarding the Council's financial matters.
Specified/Non Specified investments	Specified investments are sterling denominated investments for less than 364 days as identified in Appendix A in line with statutory investment regulations. Non-specified investments are all other investments identified in Appendix A in line with statutory investment regulations.
Supranational Bonds	These are bonds issued by institutions such as the European Investment Bank and World Bank. As with Government bonds (Gilts) they are regarded as the safest bond investments with a high credit rating.
Temporary Borrowing and Investment	Loans which are capable of being repaid within one year. The term of the loans will be negotiated from overnight to 364 days.
Treasury Management	Treasury Management has the same definition as in CIPFA's code of Practice of Treasury Management in the Public Services. "The management of the organisation's 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."
Yield Curve	The line resulting from portraying interest rate graphically for a series of periods, e.g. 7days, 1month, 3, 6, 9, and 12months. When longer-term interest rates are higher than short-term rates the yield curve slopes upwards and is described as positive. When the opposite prevails the yield curve is referred to as inverse.

APPENDIX B

TREASURY ADVISORS' VIEW ON THE ECONOMIC BACKGROUND

UK Economy

UK. After strong UK GDP growth in 2013 at an annual rate of 2.7%, and then in 2014 0.7% in Q1, 0.9% in Q2 2014 (annual rate 3.2% in Q2), Q3 has seen growth fall back to 0.7% in the quarter and to an annual rate of 2.6%. It therefore appears that growth has eased since the surge in the first half of 2014 leading to a downward revision of forecasts for 2015 and 2016, albeit that growth will still remain strong by UK standards. For this recovery to become more balanced and sustainable in the longer term, the recovery needs to move away from dependence on consumer expenditure and the housing market to exporting, and particularly of manufactured goods, both of which need to substantially improve on their recent lacklustre performance. This overall strong growth has resulted in unemployment falling much faster than expected. The MPC is now focusing on how quickly slack in the economy is being used up. It is also particularly concerned that the squeeze on the disposable incomes of consumers should be reversed by wage inflation rising back significantly above the level of inflation in order to ensure that the recovery will be sustainable. There also needs to be a major improvement in labour productivity, which has languished at dismal levels since 2008, to support increases in pay rates. Unemployment is expected to keep on its downward trend and this is likely to eventually feed through into a return to significant increases in wage growth at some point during the next three years. However, just how much those future increases in pay rates will counteract the depressive effect of increases in Bank Rate on consumer confidence, the rate of growth in consumer expenditure and the buoyancy of the housing market, are areas that will need to be kept under regular review.

Also encouraging has been the sharp fall in inflation (CPI), reaching 1.0% in November 2014, the lowest rate since September 2002. Forward indications are that inflation is likely to remain around or under 1% for the best part of a year. The return to strong growth has helped lower forecasts for the increase in Government debt over the last year but monthly public sector deficit figures during 2014 have disappointed until November. The autumn statement, therefore, had to revise the speed with which the deficit is forecast to be eliminated.

Eurozone (EZ). The Eurozone is facing an increasing threat from weak or negative growth and from deflation. In November 2014, the inflation rate fell further, to reach a low of 0.3%. However, this is an average for all EZ countries and includes some countries with negative rates of inflation. Accordingly, the ECB took some rather limited action in June and September 2014 to loosen monetary policy in order to promote growth. It now appears likely that the ECB will embark on full quantitative easing (purchase of EZ country sovereign debt) in early 2015.

Concern in financial markets for the Eurozone subsided considerably after the prolonged crisis during 2011-2013. However, sovereign debt difficulties have not gone away and major issues could return in respect of any countries that do not dynamically address fundamental issues of low growth, international un-competitiveness and the need for overdue reforms of the economy, (as Ireland has done). It is, therefore, possible over the next few years that levels of government debt to GDP ratios could continue to rise for some countries. This could mean that sovereign debt concerns have not disappeared but, rather, have only been postponed. The ECB's pledge in 2012 to buy unlimited amounts of bonds of countries which ask for a bailout has provided heavily indebted countries with a strong defence against market forces. This has bought them time to make progress with their economies to return to growth or to reduce the degree of recession. However, debt to GDP ratios (2013 figures) of Greece 180%, Italy 133%, Portugal 129%, Ireland 124% and Cyprus 112%, remain a cause of concern, especially as some of these countries are experiencing continuing rates of increase in debt in excess of their rate of economic growth i.e. these debt ratios are likely to continue to deteriorate. Any sharp downturn in economic growth would make these countries particularly vulnerable to a new bout of sovereign debt crisis. It should also be noted that Italy has the third biggest debt mountain in the world behind Japan and the US.

Greece: the general election due to take place on 25 January 2015 is likely to bring a political party to power which is anti EU and anti austerity. However, if this eventually results in Greece leaving the Euro, it is unlikely that this will directly destabilise the Eurozone as the EU has put in place adequate firewalls to contain the immediate fallout to just Greece. However, the indirect effects of the likely strenthening of anti EU and anti austerity political parties throughout the EU is much more difficult to quantify. There are particular concerns as to whether democratically elected governments will lose the support of electorates suffering under EZ imposed austerity programmes, especially in countries which have high unemployment rates. There are also major concerns as to whether the governments of France and Italy will effectively implement austerity programmes and undertake overdue reforms to improve national competitiveness. These countries already have political parties with major electoral support for anti EU and anti austerity policies. Any loss of market confidence in either of the two largest Eurozone economies after Germany would present a huge challenge to the resources of the ECB to defend their debt.

USA. The U.S. Federal Reserve ended its monthly asset purchases in October 2014. GDP growth rates (annualised) for Q2 and Q3 of 4.6% and 5.0% have been stunning and hold great promise for strong growth going forward. It is therefore confidently forecast that the first increase in the Fed. rate will occur by the middle of 2015.

China. Government action in 2014 to stimulate the economy appeared to be putting the target of 7.5% growth within achievable reach but recent data has indicated a marginally lower outturn for 2014, which would be the lowest rate of growth for many years. There are also concerns that the Chinese leadership has only started to address an unbalanced economy which is heavily over dependent on new investment expenditure, and for a potential bubble in the property sector to burst, as it did in Japan in the 1990s, with its consequent impact on the financial health of the banking sector. There are also concerns around the potential size, and dubious creditworthiness, of some bank lending to local government organisations and major corporates. This primarily occurred during the government promoted expansion of credit, which was aimed at protecting the overall rate of growth in the economy after the Lehmans crisis.

Japan. Japan is causing considerable concern as the increase in sales tax in April 2014 has suppressed consumer expenditure and growth to the extent that it has slipped back into recession in Q2 and Q3. The Japanese government already has the highest debt to GDP ratio in the world.

CAPITA ASSET SERVICES FORWARD VIEW

Economic forecasting remains difficult with so many external influences weighing on the UK. Our Bank Rate forecasts, (and also MPC decisions), will be liable to further amendment depending on how economic data transpires over 2015. Forecasts for average earnings beyond the three year time horizon will be heavily dependent on economic and political developments. Major volatility in bond yields is likely to endure as investor fears and confidence ebb and flow between favouring more risky assets i.e. equities, or the safe haven of bonds.

The overall longer run trend is for gilt yields and PWLB rates to rise, due to the high volume of gilt issuance in the UK, and of bond issuance in other major western countries. Increasing investor confidence in eventual world economic recovery is also likely to compound this effect as recovery will encourage investors to switch from bonds to equities.

The overall balance of risks to economic recovery in the UK is currently evenly balanced. Only time will tell just how long this current period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.

The interest rate forecasts in this report are based on an initial assumption that there will not be a major resurgence of the EZ debt crisis. There is an increased risk that Greece could end up leaving the Euro but if this happens, the EZ now has sufficient fire walls in place that a Greek exit would have little immediate direct impact on the rest of the EZ and the Euro. It is therefore expected that there will be an overall managed, albeit painful and tortuous, resolution of any EZ debt crisis that may occur where EZ institutions and governments eventually do what is necessary - but only when all else has been tried and failed. Under this assumed scenario, growth within the EZ will be weak at best for the next couple of years with some EZ countries experiencing low or negative growth, which will, over that time period, see an increase in total government debt to GDP ratios. There is a significant danger that these ratios could rise to the point where markets lose confidence in the financial viability of one, or more, countries, especially if growth disappoints and / or efforts to reduce government deficits fail to deliver the necessary reductions. However, it is impossible to forecast whether any individual country will lose such confidence, or when, and so precipitate a sharp resurgence of the EZ debt crisis. While the ECB has adequate resources to manage a debt crisis in a small EZ country, if one, or more, of the larger countries were to experience a major crisis of market confidence, this would present a serious challenge to the ECB and to EZ politicians.

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

- Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.
- UK strong economic growth is weaker than we currently anticipate.
- Weak growth or recession in the UK's main trading partners - the EU, US and China.
- A resurgence of the Eurozone sovereign debt crisis.
- Recapitalisation of European banks requiring more government financial support.
- Monetary policy action failing to stimulate sustainable growth and to combat the threat of deflation in western economies, especially the Eurozone and Japan.

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

- An adverse reaction by financial markets to the result of the UK general election in May 2015 and the economic and debt management policies adopted by the new government
- ECB either failing to carry through on recent statements that it will soon start quantitative easing (purchase of government debt) or severely disappointing financial markets with embarking on only a token programme of minimal purchases

which are unlikely to have much impact, if any, on stimulating growth in the EZ.

- The commencement by the US Federal Reserve of increases in the central rate in 2015 causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities, leading to a sudden flight from bonds to equities.
- A surge in investor confidence that a return to robust world economic growth is imminent, causing a flow of funds out of bonds into equities.
- UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

APPENDIX C

1. **Investment Criteria for Specified and Non Specified Investments**

1.1 Investments will be made in accordance with the following terms:

1.1.1 **<u>Specified Investments</u>:**

(All such investments will be sterling denominated, with maturities up to maximum of 1 year, meeting the minimum 'high' rating criteria where applicable and the principal sum to be repaid at maturity is the same as the initial sum invested other than investments in the UK Government.)

Instrument	**Minimum Credit Criteria**	**Use**	**Max investment**
Debt Management Agency Deposit Facility	--	In-house	£120M
Term deposits – UK government	--	In-house	£120M
Term deposits – other LAs	--	In-house	£20M with each counterparty
Term deposits – banks and building societies	Short-term F1,P1,A1, Long-term AA- or UK nationalised banks	In-house and fund managers	£20M with each counterparty/ See 2 and 3 below
Term deposits – Banks nationalised by highly credit rated sovereign countries	Short-term F1,P1,A1, Long-term AA-	In-house and fund managers	£25M with each counterparty/ See 2 and 3 below
Government guarantee on all deposits by high credit rated sovereign countries	AA-	In-house and fund managers	£20M with each counterparty/ See 2 and 3 below
UK Government supported banking sector	AA-	In-house and fund managers	£20M with each counterparty/ See 2 and 3 below

1.1.2 **Non-Specified Investments**:

A maximum of 35% will be held in aggregate of Council managed funds in non-specified investments. A maximum of 50% of aggregate funds managed by the Council's external fund managers will be held in non-specified investments.

Instrument	Min Credit/Colour Criteria	Use	Maximum Period	Maximum Investment
Term deposits – UK government (with maturities in excess of 1 year)		In-house	5 years	£30M
Term deposits – other Local Authorities (with maturities in excess of 1 year)		In-house	5 years	£20M with each counterparty
Deposits with banks and building societies covered by UK government guarantee	Short-term F1,P1,A1 Long-term AA-	Fund managers/ in-house	See 2 and 3 below	See 2 and 3 below/£25m with each counterparty
Certificates of deposits issued by banks and building societies covered by UK government guarantee	Short-term F1,P1,A1 Long-term AA-	Fund managers/in house	See 2 and 3 below	See 2 and 3 below/£20m with each counterparty
UK Government Gilts	-	Fund Managers/in house	See 2 and 3 below/5 years	See 2 and 3 below /£20M
Treasury Bills	-	Fund Managers/in house	See 2 and 3 below/5 years	See 2 and 3 below /£20M
Term deposits – banks and building societies (with maturities in excess of 1 year)	Short-term F1,P1,A1 Long-term AA-, or UK nationalised banks	In-house	5 years	£20M with each counterparty
Certificates of deposits issued by banks and building societies	Short-term F1,P1,A1 Long-term AA-,	fund managers/in -house	10 years	See 2 and 3 below/£20M with each counterparty
UK Government Gilts with maturities in excess of 1 year	AAA	Fund Managers/in house	10 years	See 2 and 3 below/£20M with each counterparty
Bonds issued by multilateral development banks	AAA	In-house on a 'buy-and-hold' basis. Also for use by fund managers	5 years 10 years	£20M with each counterparty and See 2 and 3 below
Bonds issued by a financial institution which is guaranteed by the UK government	-	In-house on a 'buy-and-hold' basis. Also for use	5 years 10 years	£20M with each counterparty See 2 and 3

		by fund managers		below
Sovereign bond issues (i.e. other than the UK govt)	AAA	In- house Fund Managers	5 years 10 years	£20M with each counterparty See 2 and 3 below
Corporate Bonds : [under SI 1010 (W.107)]	Long-term AA-	In- house Fund Managers	5 years 10years	£20M with each counterparty See 2 and 3 below
Gilt Funds and Bond Funds	Long-term AA-	In- house Fund Managers	5 years 10years	£15M See 2 and 3 below
Money Market Funds	AAA	In- house Fund Managers	n/a n/a	£20M See 2 and 3 below
Property funds	-	Fund managers	n/a	£20M See 2 and 3 below
Floating Rate Notes	Long-term AA-	Fund managers	10 years	See 2 and 3 below
Treasury Bills	N/A	Fund Managers	10 years	See 2 and 3 below
Local authority mortgage guarantee scheme	Short-term F1,P1,A1 Long-term AA-,	In-house	10 years	£20m with each counterparty
Fixed term deposits with variable rate and variable maturities				
1. Callable deposits	Short-term F1,P1,A1 Long-term AA-,	In-house and fund managers	5/10 years	£20m with each counterparty /see 2 and 3 below
2. Range trade accrual (see glossary)	Short-term F1,P1,A1 Long-term AA-,	In-house and fund managers	5/10 years	£20m with each counterparty /see 2 and 3 below
3. Snowballs (see glossary)	Short-term F1,P1,A1 Long-term AA-,	In-house and fund managers	5/10 years	£20m with each counterparty /see 2 and 3 below

1.2 The Council's external fund managers will comply with the Annual Investment Strategy. The agreements between the Council and the fund managers additionally stipulate guidelines and duration and other limits in order to contain and control risk.

1.3 The Council uses a combination of Fitch, Standard & Poor and Moody's (credit rating agency) ratings to derive its criteria. All credit ratings will be monitored daily. The Council is alerted to changes in ratings through its use of its adviser's creditworthiness service. If a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.

2. Investment Criteria - Invesco

2.1 The Fund will normally be invested in short term fixed interest rate deposits and certificates of deposit carrying interest rates of up to one year or debt instruments guaranteed by the UK government and also AAA rated money market funds. At any given time, a maximum of 50% of the portfolio by market value may be invested in negotiable securities carrying rates of interest for periods of over one year from the date of investment.

2.2 The maximum exposure to any one counter party is not to exceed 10% of the fund value or £2,000,000 whichever is the lower with the exception of money market funds where the whole balance may be invested therein. Variances to be agreed by the Head of Finance & Delivery & Delivery

2.3 The average duration of the investments for the fund shall not exceed 3 years, with the maximum maturity of any individual investment shall not exceed 10 years.

2.4 The fund will only lend to counterparties on the Invesco Standard lending list. The minimum criterion for the same is:

Short term rating of A1, F1, P1 from the credit ratings agencies Moody's Fitch and Standard and Poor.
Long term rating of AA- from Standard and Poor or equivalent from Moody's or Fitch.
Invesco reserve the right to amend the standard lending list if internal research generated supports such a move.

N.B if there is a variation in ratings between agencies for a particular counterparty the lowest rating will be applied.

APPENDIX D

Fitch International Long-Term Credit Ratings

International Long-Term Credit Ratings (LTCR) may also be referred to as Long-Term Ratings. When assigned to most issuers, it is used as a benchmark measure of probability of default and is formally described as an Issuer Default Rating (IDR). The major exception is within Public Finance, where IDRs will not be assigned as market convention has always focused on timeliness and does not draw analytical distinctions between issuers and their underlying obligations. When applied to issues or securities, the LTCR may be higher or lower than the issuer rating (IDR) to reflect relative differences in recovery expectations. The following rating scale applies to foreign currency and local currency ratings:

Investment Grade	**Definition**
AAA	Highest credit quality. 'AAA' ratings denote the lowest expectation of credit risk. They are assigned only in case of exceptionally strong capacity for payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.
AA	Very high credit quality. 'AA' ratings denote expectations of very low credit risk. They indicate very strong capacity for payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A	High credit quality. 'A' ratings denote expectations of low credit risk. The capacity for payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to changes in circumstances or in economic conditions than is the case for higher ratings.
BBB	Good credit quality. 'BBB' ratings indicate that there are currently expectations of low credit risk. The capacity for payment of financial commitments is considered adequate but adverse changes in circumstances and economic conditions are more likely to impair this capacity. This is the lowest investment grade category.
Speculative Grade	**Definition**
BB	Speculative. 'BB' ratings indicate that there is a possibility of credit risk developing, particularly as the result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met. Securities rated in this category are not investment grade.

B	Highly speculative. • For issuers and performing obligations, 'B' ratings indicate that significant credit risk is present, but a limited margin of safety remains. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favourable business and economic environment. • For individual obligations, may indicate distressed or defaulted obligations with potential for extremely high recoveries. Such obligations would possess a Recovery Rating of 'RR1' (outstanding).
CCC	For issuers and performing obligations, default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favourable business or economic conditions. • For individual obligations, may indicate distressed or defaulted obligations with potential for average to superior levels of recovery. Differences in credit quality may be denoted by plus/minus distinctions. Such obligations typically would possess a Recovery Rating of 'RR2' (superior), or 'RR3' (good) or 'RR4' (average).
CC	For issuers and performing obligations, default of some kind appears probable. • For individual obligations, may indicate distressed or defaulted obligations with a Recovery Rating of 'RR4' (average) or 'RR5' (below average).
C	• For issuers and performing obligations, default is imminent. • For individual obligations, may indicate distressed or defaulted obligations with potential for below-average to poor recoveries. Such obligations would possess a Recovery Rating of 'RR6' (poor).
RD	Indicates an entity that has failed to make due payments (within the applicable grace period) on some but not all material financial obligations, but continues to honour other classes of obligations.
D	Indicates an entity or sovereign that has defaulted on all of its financial obligations. Default generally is defined as one of the following: • Failure of an obligor to make timely payment of principal and/or interest under the contractual terms of any financial obligation; • The bankruptcy filings, administration, receivership, liquidation or other winding-up or cessation of business

	of an obligor; • The distressed or other coercive exchange of an obligation, where creditors were offered securities with diminished structural or economic terms compared with the existing obligation.

Fitch International Short-Term Credit Ratings

The following ratings scale applies to foreign currency and local currency ratings. A Short-term rating has a time horizon of less than 13 months for most obligations, or up to three years for US public finance, in line with industry standards, to reflect unique risk characteristics of bond, tax, and revenue anticipation notes that are commonly issued with terms up to three years. Short-term ratings thus place greater emphasis on the liquidity necessary to meet financial commitments in a timely manner.

Short Term Rating	**Current Definition**
F1	Highest credit quality. Indicates the strongest capacity for timely payment of financial commitments; may have an added "+" to denote any exceptionally strong credit feature.
F2	Good credit quality. A satisfactory capacity for timely payment of financial commitments, but the margin of safety is not as great as in the case of the higher ratings.
F3	Fair credit quality. The capacity for timely payment of financial commitments is adequate; however, near term adverse changes could result in a reduction to non investment grade.
B	Speculative. Minimal capacity for timely payment of financial commitments, plus vulnerability to near term adverse changes in financial and economic conditions.
C	High default risk. Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon a sustained, favourable business and economic environment.
D	Indicates an entity or sovereign that has defaulted on all of its financial obligations.

APPENDIX E

Approved Countries for Investment

AAA

- Australia
- Canada
- Denmark
- Germany
- Luxembourg
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Finland
- Hong Kong
- Netherlands
- U.K.
- U.S.A.

AA

- Abu Dhabi (UAE)
- France
- Qatar

AA-

- Belgium
- Saudi Arabia

APPENDIX F

MINIMUM REVENUE PROVISION

1. Government Guidance

The Welsh Assembly Government issued new guidance in March 2008 which requires that a Statement on the Council's policy for its annual MRP should be submitted to the full Council for approval before the start of the financial year to which the provision will relate.

The Council are legally obliged by section 21 (1b) to "have regard" to the guidance, which is intended to enable a more flexible approach to assessing the amount of annual provision than was required under the previous statutory requirements. The guidance offers four main options under which MRP could be made, with an overriding recommendation that the Council should make prudent provision to redeem its debt liability over a period which is reasonably commensurate with that over which the capital expenditure is estimated to provide benefits. The requirement to 'have regard' to the guidance therefore means that: -

Although four main options are recommended in the guidance, there is no intention to be prescriptive by making these the only methods of charge under which a local authority may consider its MRP to be prudent.

It is the responsibility of each authority to decide upon the most appropriate method of making a prudent provision, after having had regard to the guidance.

Where the CFR was nil or negative on the last day of the preceding financial year, the authority does not need to make an MRP provision. MRP in the current financial year would therefore by zero,

Option 1: Regulatory Method

Under the previous MRP regulations, General Fund MRP was set at a uniform rate of 4% of the adjusted CFR (i.e. adjusted for "Adjustment A") on a reducing balance method (which in effect meant that MRP charges would stretch into infinity). This option is available for the General Fund share of capital financing requirement which relates to capital expenditure incurred prior to 1 April 2008. It may also be used for new capital expenditure up to the amount which is deemed to be supported by the Welsh Assembly Government annual supported borrowing allocation. The use of the commutation adjustment to mitigate the MRP charge is also allowed to continue under this option.

Option 2: Capital Financing Requirement Method

This is a variation on option 1 which is based upon a charge of 4% of the aggregate CFR without any adjustment for Adjustment A, or certain other factors which were brought into account under the previous statutory MRP calculation. The CFR is the measure of an authority's outstanding debt liability as depicted by their balance sheet.

Option 3: Asset Life Method.
This method may be applied to most new capital expenditure, including where desired that which may alternatively continue to be treated under options 1 or 2.

The guidance suggests that any new borrowing which receives no Government support and is therefore self-financed would fall under option 3

Under this option, it is intended that MRP should be spread over the estimated useful life of either an asset created, or other purpose of the expenditure. There are two useful advantages of this option: -

- Longer life assets e.g. freehold land can be charged over a longer period than would arise under options 1 and 2.
- No MRP charges need to be made until the financial year after that in which an item of capital expenditure is fully incurred and, in the case of a new asset, comes into service use (this is often referred to as being an 'MRP holiday'). This is not available under options 1 and 2.

There are two methods of calculating charges under option 3:

Equal instalment method – equal annual instalments which are calculated using a simple formula set out in paragraph 9 of the MRP guidance,

under this approach, the MRP is provided by the following formula

A – B divided by C

A is the amount of capital expenditure in respect of the asset financed by borrowing or credit arrangements

B is the total provision made before the current financial year in respect of that expenditure

C is the inclusive number of financial years from the current year to that in which the estimated life of the asset expires

Annuity method – annual payments gradually increase during the life of the asset with an appropriate interest rate used to calculate the annual amount

Asset life - the MRP guidance makes it clear that the estimated life of an asset should be determined in the year MRP commences and should not subsequently be revised

Under both options, the authority may make additional voluntary revenue provision and this may require an appropriate reduction in later years' MRP

In addition adjustments to the calculation to take account of repayment by other methods (e.g. application of capital receipts) should be made as necessary.

Option 4: Depreciation Method

Under this option, MRP charges are to be linked to the useful life of each type of asset using the standard accounting rules for depreciation (but with some exceptions) i.e. this is a more complex approach than option 3.

The same conditions apply regarding the date of completion of the new expenditure as apply under option 3.

2. Date of implementation

The previous statutory MRP requirements cease to have effect after the 2006/07 financial year. However, the same basis of 4% charge in respect of the GF share of CFR may continue to be used without limit until the 2009/10 financial year, relative to expenditure incurred up to 31/3/2008.

The guidance suggests that Options 3 and 4 should be applied to any capital expenditure which results in an increase in the CFR and does not relate to the authority's Supported Capital Expenditure.

The guidance also provides the authority with discretion to apply Options 3 or 4 to all capital expenditure whether or not supported and whenever it is incurred.

Any capitalised expenditure incurred after 1 April 2008 which gives rise to an increase in the GF CFR should be repaid by using option 3 as adapted by paragraphs 23 and 24 of the guidance.

APPENDIX G

Active Internal Credit UK Counterparty List (as at 16 January 2015)

Institution	Country	Bank/BS	Fitch Ratings		
			S Term	Support	L Term
Bank of New York Mellon	UK	Bank	F1+	1	AA-
Bank of Scotland	UK	Bank	F1	1	A
Barclays	UK	Bank	F1	1	A
Citibank International plc	UK	Bank	F1	1	A
Coventry Building Society	UK	BS	F1	5	A
Credit Suisse International	UK	Bank	F1	1	A
Goldman Sachs International Bank	UK	Bank	F1		A
HSBC	UK	Bank	F1+	1	AA-
Leeds Building Society	UK	BS	F1	5	A-
Lloyds TSB	UK	Bank	F1	1	A
MBNA Europe	UK	Bank	F1	1	A-
Merrill Lynch International	UK	Bank	F1	1	A
National Westminster	UK	Bank	F1	1	A
Nationwide	UK	BS	F1	1	A
Royal Bank of Scotland	UK	Bank	F1	1	A
Santander	UK	Bank	F1	1	A
Standard Chartered Bank	UK	Bank	F1+	1	AA-
Sumitomo Mitsui Banking Corporation	UK	Bank	F1	1	A-
UBS Ltd	UK	Bank	F1	1	A
Debt Management Office	UK				
Local Authorities	UK				