TREASURY MANAGEMENT STRATEGY 2018/19

1. Introduction

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

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

This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the CLG Guidance.
The Authority has [borrowed and/or invested] substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Authority's treasury management strategy.

2. Economic Background

The major external influence on the Authority's treasury management strategy for 2018/19 will be the UK's progress in negotiating its exit from the European Union and agreeing future trading arrangements. The domestic economy has remained relatively robust since the surprise outcome of the 2016 referendum, but there are indications that uncertainty over the future is now weighing on growth. Transitional arrangements may prevent a cliff-edge, but will also extend the period of uncertainty for several years. Economic growth is therefore forecast to remain sluggish throughout 2018/19.

Consumer price inflation reached 3.1% in November 2017 as the post-referendum devaluation of sterling continued to feed through to imports. Unemployment continued to fall and the Bank of England's Monetary Policy Committee judged that the extent of spare capacity in the economy seemed limited and the pace at which the economy can grow without generating inflationary pressure had fallen over recent years. With its inflation-control mandate in mind, the Bank of England's Monetary Policy Committee raised official interest rates to 0.5% in November 2017.

In contrast, the US economy is performing well and the Federal Reserve is raising interest rates in regular steps to remove some of the emergency monetary stimulus it has provided for the past decade. The European Central Bank is yet to raise rates, but has started to taper its quantitative easing programme, signalling some confidence in the Eurozone economy.

3. Credit outlook

High profile bank failures in Italy and Portugal have reinforced concerns over the health of the European banking sector. Sluggish economies and fines for pre-crisis behaviour continue to weigh on bank profits, and any future economic slowdown will exacerbate concerns in this regard.
Bail-in legislation, which ensures that large investors including local authorities will rescue failing banks instead of taxpayers in the future, has now been fully implemented in the European Union, Switzerland and USA, while Australia and Canada are progressing with their own plans. In addition, the largest UK banks will ringfence their retail banking functions into separate legal entities during 2018. There remains some uncertainty over how these changes will impact upon the credit strength of the residual legal entities.
The credit risk associated with making unsecured bank deposits has therefore increased relative to the risk of other investment options available to the Authority; returns from cash deposits however remain very low.

4. Interest rate forecast

The Authority's treasury adviser Arlingclose's central case is for UK Bank Rate to remain at 0.50% during 2018/19, following the rise from the historic low of 0.25%. The Monetary Policy Committee re-emphasised that any prospective increases in Bank Rate would be expected to be at a gradual pace and to a limited extent.
Future expectations for higher short term interest rates are subdued and on-going decisions remain data dependant and negotiations on exiting the EU cast a shadow over monetary policy decisions. The risks to Arlingclose's forecast are broadly balanced on both sides. The Arlingclose central case is for gilt yields to remain broadly stable across the medium term. Upward movement will be limited, although the UK government's seemingly deteriorating fiscal stance is an upside risk. A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix A.

5. Balances

On 31st December 2017, the council held £64.560m of borrowing and £25m of investments. This is set out in further detail at Appendix 2. Forecast changes in these sums are shown in the balance sheet analysis in the table below.

Table 1: Balance sheet summary and forecast

	31.3.17 Actual £m	31.3.18 Estimate £m	31.3.19 Forecast £m	31.3.20 Forecast £m	31.3.21 Forecast £m
General Fund CFR	39,310	55,176	53,898	51,806	49,700
HRA CFR	44,750	44,750	44,750	44,750	44,750
Total CFR	**84,060**	**99,926**	**98,648**	**96,556**	**94,450**
Less: External borrowing	64,286	82,583	82,996	83,409	81,303

Internal borrowing	**19,774**	**17,343**	**15,652**	**13,147**	**13,147**
Less: Usable reserves	(30,150)	(30,150	(30,000)	(29,000)	(28,000)
Less: Working capital	(11,348)	(11,300)	(11,300)	(11,000)	(11,000)
Investments	**21,724**	**24,107**	**25,648**	**26,853**	**25,853**

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Authority's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing. The Authority has an increasing CFR due to the capital programme, but minimal investments and will therefore be required to borrow up to £18.5m over the forecast period.

CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Authority expects to comply with this recommendation during 2018/19.

6. Borrowing Strategy

6.1 The Authority currently holds £64.56m million of loans, a small decrease on the previous year-end balance, as part of its strategy for funding previous years' capital programmes by PWLB annuity loans.. The balance sheet forecast in table 1 shows that the Authority expects to borrow up to £17m in 2018/19 in respect of the Crematorium project and further asset purchases . The Authority may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £116m for 2018/19.

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

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

By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal or short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2018/19 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

Alternatively, the Authority may arrange forward starting loans during 2018/19, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

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

6.2 Sources of borrowing:

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

- Public Works Loan Board (PWLB) and any successor body
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except [your local] Pension Fund)
- capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues
- include any other counterparty you intend to borrow from

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

- operating and finance leases
- hire purchase
- Private Finance Initiative
- sale and leaseback

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

Municipal Bonds Agency: UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a joint and several guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to full Council.

LOBOs: The Authority holds £7m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Authority has the option to either accept the new rate or to repay the loan at no additional cost. £2m of these LOBOS have options during 2018/19, and although the Authority understands that lenders are unlikely to exercise their options in the current low interest rate environment, there remains an element of refinancing risk. The Authority will take the option to repay LOBO loans at no cost if it has the opportunity to do so

Short-term and variable rate loans: These loans leave the Authority exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators below.

Debt rescheduling: The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Authority may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

7. Investment Strategy

7.1

The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Authority's investment balance has averaged £24m, and similar levels are expected to be maintained in the forthcoming year

7.2 Objectives

Both the CIPFA Code and the CLG Guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Authority will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

7.3 Negative interest rates

If the UK enters into a recession in 2018/19, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested. Given the increasing risk and low returns from short-term unsecured bank investments, the Authority aims to carry on and diversify into more secure and/or higher yielding asset classes during 2018/19. This is especially the case for the estimated £11m that is available for longer-term investment. The majority of the Authority's surplus cash is currently invested in short-term unsecured bank deposits, certificates of deposit and money market funds. This diversification will represent a change in strategy over the coming year.

Approved counterparties: The Authority may invest its surplus funds with any of the counterparty types in table 2 below, subject to the cash limits (per counterparty) and the time limits shown.

Table 2: Approved investment counterparties and limits

Credit rating	Banks unsecured	Banks secured	Government	Corporates	Registered Providers
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£7m 5 years	£7m 20 years	£7m 50 years	£5m 20 years	£5m 20 years
AA+	£7m 5 years	£7m 10 years	£5m 25 years	£4m 10 years	£5m 10 years
AA	£7m 4 years	£7m 5 years	£5m 15 years	£4m 5 years	£5m 10 years
AA-	£7m 3 years	£7m 4 years	£5m 10 years	£3m 4 years	£5m 10 years
A+	£7m 2 years	£7m 3 years	£5m 5 years	£3m 3 years	£5m 5 years
A	£7m 13 months	£7m 2 years	£5m 5 years	£3m 2 years	£3m 5 years
A-	£7m 6 months	£7m 13 months	£5m 5 years	£2m 13 months	£3m 3 years
None	£2m 6 months	£2m 6 months	n/a	n/a	n/a
Pooled funds	£3m per fund				

7.4 Credit rating

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

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

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

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

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

Registered providers: Loans and bonds issued by, guaranteed by or secured on the assets of registered providers of social housing, formerly known as housing associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services; they retain the likelihood of receiving government support if needed.

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

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

Operational bank accounts
The Council banks with Lloyds (Lloyds Banking Group). On adoption of this Strategy, it will meet the minimum credit criteria of A- (or equivalent) long term. It is the Councils intention that even if the credit rating of Lloyds Bank falls below the minimum criteria A- the bank will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements.

Policy investments
Over the years the Authority has provided cash-flow cover for a number of third-party organisations linked to the Authority. The following limits are set for 2018/19:-

- Cheltenham Festivals - £100k up to one year duration
- The Glos Everyman Theatre - £100k up to one year duration
- Ubico Limited £500k up to one year duration
- Cheltenham Trust - £100k up to one year duration
- Publica Group - £100k up to one year duration
- Cheltenham Borough Homes - £7m Non-specified duration
- Cheltenham Borough Homes - £500k up to one year
- Glos Airport Limited - £1.75m Non-specified duration

Renewable Energy investments
Over recent years significant investments from Local Authorities in the Renewable Energy markets has occurred by way of investing in an energy bond. Currently the council has approved the use of Corporate Bonds and has used them on a regular basis but only for a maximum of two years previously. To be able to potentially invest in Green Renewable energy recommendation was made following consultation with members of the Treasury Management Panel on the 5th June 2017 and approved by Council on 24th July 2017 that up to £2m in relation to Green Investment bonds can be invested up to 5 years.

7.5 Risk assessment and credit ratings

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

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

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

7.6 Other information on the security of investments

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

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

7.7 Specified investments

The CLG Guidance defines specified investments as those:

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

The Authority defines "high credit quality" organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds "high credit quality" is defined as those having a credit rating of A- or higher.

7.8 Non-specified investments

Any investment not meeting the definition of a specified investment is classed as non-specified. The Authority does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in table 3 below.

Table 3: Non-specified investment limits

	Cash limit
Total long-term investments	£15m
Total investments without credit ratings or rated below A- (except UK Government and local authorities)	£10m
Total investments (except pooled funds) with institutions domiciled in foreign countries rated below AA+	£10m

7.9 Investment limits

The Authority's revenue reserves available to cover investment losses are forecast to be £30.15 million on 31st March 2018. In order that no more than 25% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £7 million. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Table 4: Investment limits

	Cash limit
Any single organisation, except the UK Central Government	£7m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£7m per group
Any group of pooled funds under the same	£5m per manager

management	
Foreign countries	£4m per country
Registered providers	£5m in total
Unsecured investments with building societies	£5m in total
Loans to unrated corporates – Renewable Energy	£5m in total
Money Market Funds	£10m in total

7.10 Liquidity management

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

8. Non-Treasury Investments

Although not classed as treasury management activities and therefore not covered by the CIPFA Code or the CLG Guidance, the Authority may also purchase property for investment purposes and may also make loans and investments for service purposes. Such loans and investments will be subject to the Authority's normal approval processes for revenue and capital expenditure and need not comply with this treasury management strategy.

9. Treasury Management Indicators

The Authority measures and manages its exposures to treasury management risks using the following indicators.

9.1 Security

The Authority has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

	Target
Portfolio average credit rating	***A***

Interest rate exposures: This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the proportion of net principal borrowed will be:

	2018/19	**2019/20**	**2020/21**
Upper limit on fixed interest rate exposure	100%	100%	100%
Upper limit on variable interest rate exposure	50%	50%	50%

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

Maturity structure of borrowing: This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing will be:

	Upper	**Lower**
Under 12 months	50%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	100%	0%
5 years and within 10 years	100%	0%
10 years and within 20 years	100%	0%
20 years and within 30 years	100%	0%
30 years and within 40 years	100%	0%
40 years and above	100%	0%

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

Principal sums invested for periods longer than 364 days: The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end will be:

	2018/19	2019/20	2020/21
Limit on principal invested beyond year end	£10m	£10m	£10m

10. Other Items

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

10.1 Policy on the use of financial derivatives

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

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

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

10.2 Policy on apportioning interest to the HRA

On 1st April 2012, the Authority notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/ credited to the respective revenue account. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured each year and interest transferred between the General Fund and HRA at the Authority's average interest rate on investments, adjusted for credit risk.

10.3 Investment training

The needs of the Authority's treasury management staff for training in investment management are assessed as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change.

Officers regularly attend training courses, seminars and conferences provided by Arlingclose and CIPFA.

10.4 Investment advisers

The Authority recently appointed Arlingclose Limited as treasury management advisers for three years plus the option for a further two years after a joint tender with Gloucestershire County Council, South Gloucestershire Council and the Forest of Dean District Council. The Authority receives specific advice on investment, debt and capital finance issues.

10.5 Investment of money borrowed in advance of need

The Authority may, from time to time, borrow in advance of need, where this is expected to provide the best long-term value for money. Since amounts borrowed will be invested until spent, the Authority is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Authority's overall management of its treasury risks.

The total amount borrowed will not exceed the authorised borrowing limit of £116m. The maximum period between borrowing and expenditure is expected to be two years, although the Authority is not required to link particular loans with particular items of expenditure.

10.6 Financial Implications

The budget for investment income in 2018/19 is £258.7k, based on an average investment portfolio of £21.5 million at an interest rate of 1.20%. The budget for debt interest paid in 2018/19 is £2.42 million, based on an average debt portfolio of £65.52 million at an average interest rate of 3.75%. If actual levels of investments and borrowing, and actual interest rates differ from those forecast, performance against budget will be correspondingly different.

Appendix A – Arlingclose Economic & Interest Rate Forecast November 2017

Underlying assumptions:

- In a 7-2 vote, the MPC increased Bank Rate in line with market expectations to 0.5%. Dovish accompanying rhetoric prompted investors to lower the expected future path for interest rates. The minutes re-emphasised that any prospective increases in Bank Rate would be expected to be at a gradual pace and to a limited extent.

- Further potential movement in Bank Rate is reliant on economic data and the likely outcome of the EU negotiations. Policymakers have downwardly assessed the supply capacity of the UK economy, suggesting inflationary growth is more likely. However, the MPC will be wary of raising rates much further amid low business and household confidence.

- The UK economy faces a challenging outlook as the minority government continues to negotiate the country's exit from the European Union. While recent economic data has improved, it has done so from a low base: UK Q3 2017 GDP growth was 0.4%, after a 0.3% expansion in Q2.

- Household consumption growth, the driver of recent UK GDP growth, has softened following a contraction in real wages, despite both saving rates and consumer credit volumes indicating that some households continue to spend in the absence of wage growth. Policymakers have expressed concern about the continued expansion of consumer credit; any action taken will further dampen household spending.

- Some data has held up better than expected, with unemployment continuing to decline and house prices remaining relatively resilient. However, both of these factors can also be seen in a negative light, displaying the structural lack of investment in the UK economy post financial crisis. Weaker long term growth may prompt deterioration in the UK’s fiscal position.

- The depreciation in sterling may assist the economy to rebalance away from spending. Export volumes will increase, helped by a stronger Eurozone economic expansion.

- Near-term global growth prospects have continued to improve and broaden, and expectations of inflation are subdued. Central banks are moving to reduce the level of monetary stimulus.

- Geo-political risks remains elevated and helps to anchor safe-haven flows into the UK government bond (gilt) market.

Forecast:

- The MPC has increased Bank Rate, largely to meet expectations they themselves created. Future expectations for higher short term interest rates are subdued. On-going decisions remain data dependant and negotiations on exiting the EU cast a shadow over monetary policy decisions.

- Our central case for Bank Rate is 0.5% over the medium term. The risks to the forecast are broadly balanced on both sides.

- The Arlingclose central case is for gilt yields to remain broadly stable across the medium term. Upward movement will be limited, although the UK government's seemingly deteriorating fiscal stance is an upside risk.

	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Average
Official Bank Rate														
Upside risk	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.19**
Arlingclose Central Case	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**
Downside risk	0.00	0.00	0.00	0.00	0.00	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	**-0.15**
3-month LIBID rate														
Upside risk	0.10	0.10	0.10	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.22**
Arlingclose Central Case	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**
Downside risk	-0.10	-0.10	-0.15	-0.15	-0.15	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	**-0.20**
1-yr LIBID rate														
Upside risk	0.15	0.15	0.20	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	**0.27**
Arlingclose Central Case	**0.70**	**0.70**	**0.70**	**0.70**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.77**
Downside risk	-0.15	-0.20	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.15	-0.15	**-0.26**
5-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	**0.32**
Arlingclose Central Case	**0.75**	**0.75**	**0.80**	**0.80**	**0.80**	**0.85**	**0.90**	**0.90**	**0.95**	**0.95**	**1.00**	**1.05**	**1.10**	**0.89**
Downside risk	-0.20	-0.20	-0.25	-0.25	-0.25	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	**-0.33**
10-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	**0.32**
Arlingclose Central Case	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.30**	**1.30**	**1.35**	**1.40**	**1.45**	**1.50**	**1.55**	**1.55**	**1.36**
Downside risk	-0.20	-0.25	-0.25	-0.25	-0.25	-0.30	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	**-0.33**
20-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	**0.32**
Arlingclose Central Case	**1.85**	**1.85**	**1.85**	**1.85**	**1.85**	**1.90**	**1.90**	**1.95**	**1.95**	**2.00**	**2.05**	**2.05**	**2.05**	**1.93**
Downside risk	-0.20	-0.30	-0.25	-0.25	-0.30	-0.35	-0.40	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.38**
50-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	**0.32**
Arlingclose Central Case	**1.70**	**1.70**	**1.70**	**1.70**	**1.70**	**1.75**	**1.80**	**1.85**	**1.90**	**1.95**	**1.95**	**1.95**	**1.95**	**1.82**
Downside risk	-0.30	-0.30	-0.25	-0.25	-0.30	-0.35	-0.40	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.39**

Appendix B – Existing Investment & Debt Portfolio Position

	31.12.17 Actual Portfolio £m	% Rate
External borrowing:		
Public Works Loan Board	48.660	3.67
Market Loans	15.900	4.00
Total external borrowing	**64.560**	**3.75**
Treasury Investments:		
Banks & Building Societies	17.463	0.70
Government (Incl. LA's)	1.000	1.00
Money Market Funds	2.940	0.38
Other Pooled Funds	3.00	4.6
Total treasury investments	**24.403**	**0.73**
Net Debt	**40.157**	

APPENDIX C - THE CAPITAL STRATEGY 2018/19 – 2020/21

The Council's capital expenditure plans are the key driver of treasury management activity. The outputs of the capital expenditure plans are reflected in prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

2.1 Capital expenditure

This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts:

Capital expenditure	2016/17 Actual £000	2017/18 Revised £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
General Fund	2,224	29,364	23,233	1,708	1,199
HRA	11,255	10,081	10,980	8,170	9,325
Total	**13,479**	**39,445**	**34,213**	**9,878**	**10,524**

Other long term liabilities: The above financing need excludes other long term liabilities, such as leasing arrangements which already include borrowing instruments. The authority has no finance leasing arrangements at present.

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Capital expenditure	2016/17 Actual £000	2017/18 Revised £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000
Total	**13,479**	**39,445**	**34,213**	**9,878**	**10,524**
Financed by:					
Capital receipts	3,941	8,738	3,107	1,503	1,389
Capital grants	434	2,332	21,500	500	500
Capital reserves	7,077	5,883	4,761	4,844	4,915
3rd Party Contributions	781	1,181	350	350	350
Revenue	1,246	1,918	4,082	2,268	3,370
Borrowing need for the year	**0**	**19,393**	**413**	**413**	**0**

2.2 The Council's borrowing need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic 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. Any capital expenditure above, which has not immediately been paid for, will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with each assets life.

The CFR includes any other long term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes

The Council is asked to approve the CFR projections below:

£000	2016/17 Actual	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
Capital Financing Requirement					
Total CFR	84,060	99,921	98,562	99,491	95,586
Movement in CFR	(1,356)	15,861	(1,359)	929	(3,905)

Movement in CFR represented by					
Net financing need for the year (above)	13,479	39,445	34,213	9,878	10,524
Less MRP/VRP and other financing movements	(14,835)	(23,584)	(35,572)	(8,949)	(14,429)
Movement in CFR	**(1,356)**	**15,861**	**(1,359)**	**929**	**(3,905)**

2.3 Affordability prudential indicators

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators:

2.4 Ratio of financing costs to net revenue stream

This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet borrowing costs. It would not be prudent for borrowing costs to be a significant proportion of net revenue either now or in the future. By estimating the ratio for at least the next three years the trend in the cost of capital (borrowing costs net of interest and investment income) as a proportion of revenue income can be seen.

%	2016/17 Actual	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
General Fund	3.78%	3.83%	6.06%	5.66%	5.61%
HRA	7.92%	8.07%	8.12%	8.21%	8.00%
Total	6.26%	6.36%	7.25%	7.12%	6.99%

3. BORROWING

The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of approporiate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

3.1 Current portfolio position

The Council's treasury portfolio position at 31 March 2017, with forward projections are summarised below. The table shows the actual external debt (the treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

£000	2016/17 Actual	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
External Debt					
Debt at 1 April	65,474	65,035	81,047	80,493	79,923
Expected change in Debt	(561)	16,012	(554)	(570)	(585)
Actual debt at 31 March	**65,035**	**81,047**	**80,493**	**79,923**	**79,338**
The Capital Financing Requirement	**84,060**	**99,921**	**98,562**	**99,491**	**95,586**
Under / (over) borrowing	**19,025**	**18,874**	**18,069**	**19,568**	**14,058**
Total investments at 31 March					
Investments	**22,409**	**26,015**	**25,945**	**25,945**	**24,945**
Investment change	1,867	3,606	(70)	0	(1,000)

Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within set limits. One of these is that the Council needs to ensure that its total debt, net of any investments, does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2018/19 and the following two financial years (shown as net borrowing above). This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Section 151 Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

3.2 Treasury Indicators: limits to borrowing activity

The operational boundary: This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

Operational boundary £'000	2017/18 Revised	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
Borrowing	112,000	111,000	125,000	122,000

The authorised limit for external debt: A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

The Council is asked to approve the following authorised limit:

Authorised Limit £'000	2017/18 Revised	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
Borrowing	122,000	121,000	135,000	132,000

Appendix D - Annual MRP Statement

MRP Policy for 2018/19

Background:

1. For many years local authorities have been required by Statute and associated Statutory Instruments to charge to the Revenue Account an annual provision for the repayment of debt associated with expenditure incurred on capital assets. This charge to the Revenue Account is referred to as the Minimum Revenue Provision (MRP). In practice MRP represents the financing of capital expenditure from the Revenue Account that was initially funded by borrowing.

2. In February 2008 the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [Statutory Instrument 2008/414] were approved by Parliament and became effective on 31st March 2008. These regulations replaced the formula based method for calculating MRP which existed under previous regulations under the Local Government Act 2003. The new regulations required a local authority to determine each financial year an amount of MRP which it considers to be ‘prudent’. Linked to this new regulation, the Department of Communities and Local Government (CLG) produced Statutory Guidance which local authorities are required to follow, setting out what constitutes a prudent provision.

3. The CLG Guidance recommends that, before the start of the financial year, a statement of MRP policy for the forthcoming financial year is approved by Full Council. If it is ever proposed to vary the original statement for the current year, a revised statement should be put to the council at that time.

4. The broad aim of the Policy is to ensure that MRP is charged over a period that is reasonably commensurate with the period over which the capital expenditure which gave rise to the debt provides benefits. In the case of borrowing supported by Revenue Support Grant (‘Supported Borrowing’), the aim is that MRP is charged over a period reasonably commensurate with the period implicit in the determination of that grant. MRP is not required to be charged to the Housing Revenue Account. Where a local authority’s overall underlying need to borrow for capital purposes, known as the Capital Financing Requirement (CFR), is nil or a negative amount there is no requirement to charge MRP.

MRP Options:

5. Four options for prudent MRP provision are set out in the CLG Guidance. Details of each are set out below with a summary set out in Table 1 below:

Option 1 – Regulatory Method:

6. This method replicates the position that would have existed under the previous regulatory environment. MRP is charged at 4% of the Authority's underlying need to borrow for capital purposes, the Capital Financing Requirement (CFR). The formula includes an item known as "Adjustment A" which was intended to achieve neutrality between the CFR and the former Credit Ceiling, used to calculate MRP prior to the introduction of the Prudential System on 1st April 2004. The formula also took into account any reductions relating to the commutation of capital debt made by central government.

7. The latest CLG guidance (effective from 1 April 2012) states that authorities **may** continue to use this method for capital expenditure incurred before 1 April 2008 and supported borrowing, allowing authorities to modify the method if it produces an 'anomalous and disadvantageous result'. The annual General Fund MRP charge under this method is £236,847.

8. This method (which is based on a 4% reducing balance) was used by the council up until 2015/16 for pre 1 April 2008 and supported borrowing. Under this method however, although the MRP charge reduces each year, the borrowing is never entirely paid off. Consequently, from 2016/17, the charge has been based on repaying the debt on a 'straight line' (or equal annual instalment) basis over a 35 year period. This has the advantage of a constant charge which fully repays the debt, which is more prudent. 9

Option 2 – CFR Method:

10. This method simplifies the calculation of MRP by basing the charge solely on the authority's CFR but excludes the technical adjustments included in Option 1. The annual MRP charge is set at 4% of the non-housing CFR at the end of the preceding financial year.

11. The General Fund MRP charge for this method is nil for 2017/18 and 2018/19.

Option 3 – Asset Life Method:

12. Under this method MRP is determined by the life of the asset for which the borrowing is undertaken. This can be calculated by either of the following methods:
    (a) Equal Instalments: where the principal repayment made is the same in each year, or
    (b) Annuity: where the principal repayments increase over the life of the asset.

    The annuity method has the advantage of linking MRP to the benefits arising from capital expenditure, where these benefits are expected to increase over the life of the asset.

13. MRP commences in the financial year following that in which the expenditure is incurred or, in the year following that in which the relevant asset becomes operational. This enables an MRP “holiday” to be taken in relation to assets which take more than one year to be completed before they become operational.

14. The estimated life of the asset will be determined in the year that MRP commences and will not be subsequently revised. However, additional repayments can be made in any year which will reduce the level of payments in subsequent years.

15. If no life can be reasonably attributed to an asset, such as freehold land, the life is taken to be a maximum of 50 years. In the case of freehold land on which a building or other structure is constructed, the life of the land will be treated as equal to that of the structure, where this would exceed 50 years.

16. In instances where central government permits revenue expenditure to be capitalised, the Statutory Guidance sets out the number of years over which the charge to revenue must be made. The maximum useful life for expenditure capitalised by virtue of a direction under s16(2)(b) is 20 years.

17. MRP in respect Finance Leases brought onto the Balance Sheet falls under Option 3.

18. The General Fund MRP charge using this method is £889,174 for 2017/18 and currently an estimated £1,291,885 for 2018/19.

Option 4 - Depreciation Method:

19. The depreciation method is similar to that under Option 3 but MRP is equal to the depreciation provision required in accordance with proper accounting practices to be charged to the Income and Expenditure account.

20. The General Fund MRP charge for this method is nil for 2017/18 and 2018/19.

Conditions of Use:

21. The current CLG Guidance puts the following conditions on the use of the four options:

    Options 1 and 2 can be used on all capital expenditure incurred before 1st April 2008 and on Supported Capital Expenditure on or after that date.

    Options 3 and 4 are considered prudent options for Unsupported Capital Expenditure on or after 1st April 2008. These options can also be used for Supported Capital Expenditure whenever incurred.

MRP Policy for 2018/19:

22. It is proposed that the council continues to adopt
    - the modified Option 1 – repayment over 35 years on a straight line basis - for borrowing incurred before 1 April 2008, which is Supported Borrowing
    - Option 3 for borrowing after 1 April 2008 and Unsupported Borrowing. For Option 3, the annuity method for calculating MRP will be used when appropriate as it has the advantage of linking MRP to the benefits arising from capital expenditure, where these benefits are expected to increase over the life of the asset.

Repayment of debt relating to capital loans made:

23. In recent years the council has made a number of capital loans to Gloucestershire Airport, The Everyman Theatre and Cheltenham Borough Homes (CBH) funded from prudential borrowing. Until 2016/17 the council was setting aside MRP to repay this debt over the life of the loans (equivalent to the estimated life of the capital assets) using option 3's annuity method, as permitted by the CLG guidance. The annual repayments from the borrowers (which match the MRP) must be treated as capital receipts, so were used to fund the capital programme in lieu of revenue funding. In this way the impact of these loans on the revenue account was neutral, since the additional MRP was matched by an equivalent reduction in the revenue funding for the capital programme.

24. This policy, although currently neutral on the revenue account, was however constraining the council's ability to make further capital loans should it wish, since this would increase the MRP further, whilst generating more capital receipts than required to fund the capital programme. The capital finance regulations allow the council to use capital receipts to 'repay the principal of any amount borrowed'. Therefore from 2017/18, to replace MRP provision for repaying the debt on capital loans an equivalent amount was set aside from usable capital receipts, equal to the annual repayments of principal by the borrowers. This reduces the capital receipts available to fund the capital programme, but also reduces MRP by an equivalent amount. The borrowers are contracted to fully repay the loans over their lives in annual instalments, so all of the debt will be repaid. The amount of debt to be repaid by this method in 2018/19 is approximately £243,000.

Appendix E GLOSSARY OF TERMS

Bank Rate
The rate of interest set by the Bank of England as a benchmark rate for British banks.

Bonds
A long-term debt security issued by a company, a financial institution, a local authority, national government or its affiliated agencies. It represents an undertaking to repay the holder the fixed amount of the principal on the maturity date plus a specified rate of interest payable either on a regular basis during the bond's life (coupon) or at maturity.

Borrowing
Loans taken out taken out by the authority to pay for capital expenditure or for the prudent management of the Council's financial affairs which are repayable with interest.

Capital Expenditure
Capital expenditure pays for improvements to existing and new assets used in the delivery of Council services as well as other items determined by Regulation. Capital resources are scarce, costly and also have long term revenue implications over many years and even generations where capital expenditure is funded by borrowing. Hence the requirement of the Prudential Code to ensure what is charged as Capital Expenditure is Prudent, Sustainable and Affordable.
The statutory definition of capital expenditure is given in the Local Government Act 2003, the Local Authorities (Capital Finance) Regulations 2003 and 2004 as amended. Statute relies on the accounting measurement of cost in International Accounting Standard (IAS) 16 to determine whether expenditure is eligible to be capitalised or whether it should be treated as revenue expenditure. Key to what is eligible as capitals spend, are the following words in IAS 16 -'Costs directly attributable to bringing the specific asset into working condition for its intended use'.

Capital Financing Requirement (CFR)
An authority's underlying need to borrow for a capital purpose.

Capital Market
A market for securities (debt or equity), where companies and governments can raise long-term funds (periods greater than one year). The raising of short-term funds takes place on other markets (e.g. the money market).

Capital Programme
The Capital Programme sets out the Council's capital expenditure plans for the forthcoming financial year as well as for the medium term. It is approved annually at Council and identifies the estimated cost of those schemes, their projected phasing over financial years as well as the method of funding such expenditure.

Certificates of Deposits (CDs)
A certificate issued for deposits made at a deposit-taking institution (generally a bank). The bank agrees to pay a fixed interest rate for the specified period of time, and repays the principal at maturity. CDs can be purchased directly from the banking institution or through a securities broker. An active interbank secondary market exists to buy and sell CDs.

Chartered Institute of Public Finance & Accountancy (CIPFA)
CIPFA is the professional body for people in public finance. As a specialised public services body, they provide information, guidance, and determine accounting standards and reporting standards to be followed by Local Government.

Collective Investment Scheme Structures
Schemes whereby monies from a number of investors are pooled and invested as one portfolio in accordance with pre-determined objectives.

Commercial Paper
A relatively low risk, short-term and unsecured promissory note traded on money markets issued by companies or other entities to finance their short-term cash requirements.

Corporate Bonds
Bonds that are issued by a company or other non-government issuers. They represent a form of corporate debt finance and are an alternative means of raising new capital other than equity finance or bank lending.

Counterparty
One of the parties involved in a financial transaction with which the Council may place investments.

Counterparty / Credit Risk
Risk that a counterparty fails to meet its contractual obligations to the Council to repay sums invested.

Credit Criteria
The parameters used as a starting point in considering with whom the Council may place investments, aimed at ensuring the security of the sums invested.

Credit Default Swaps
A financial transaction which the buyer transfers the credit risk related to a debt security to the seller, who receives a series of fees for assuming this risk. The levels of fees reflect the perceived level of risk.

Credit Rating
A credit rating assesses the credit worthiness of an individual, corporation, or even a country. Credit ratings are calculated from financial history and current assets and liabilities. Typically, a credit rating tells a lender or investor the probability of the subject being able to pay back a loan. Ratings usually consist of a long-term, short-term, viability and support indicators. The Fitch credit rating of F1 used by the Council is designated as “Highest Credit quality” and indicates the strongest capacity for timely payment of financial commitments.

Debt Management Account Deposit Facility (DMADF)
The Debt Management Office provides this service as part of its cash management operations and of a wider series of measures designed to improve local and central government’s investment framework and cash management. The key objective of the DMADF is to provide users with a flexible and secure facility to supplement their existing range of investment options while saving interest costs for central government.

Debt Restructuring
Debt restructuring is a process that allows an organisation to reduce, renegotiate and undertake replacement debt.

Diversification of Investments
The process of creating a portfolio of different types of financial instruments with regard to type, price, risk issuer, location, maturity, etc. in order to reduce the overall risk of the portfolio as a whole.

Duration (Maturity)
The length of time between the issue of a security and the date on which it becomes payable.

External Borrowing
Money borrowed from outside of the Council.

Financial Instrument
Any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another. Typical financial liabilities are borrowing and financial guarantees. Typical financial assets include bank deposits, amounts owed by customers, loans receivable and investments.

Fitch/Moody’s/Standard & Poors Credit Ratings
Commercial organisations providing an opinion on the relative ability of an entity to meet financial commitments, such as interest, preferred dividends, repayment of principal, insurance claims or counterparty obligations. The opinion is usually provided in the form of a credit rating.

Fixed Rate
An interest rate that does not change over the life of a loan or other form of credit.

Floating Rate Notes
A money market security paying a floating or variable interest rate, which may incorporate a minimum or floor.
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Housing Revenue Account (HRA)
The HRA is an account of expenditure and income that every local authority housing department must keep in accordance with the Local Government & Housing Act 1989. The account is kept separate or ring fenced from other Council activities. Income is primarily generated by the rents and service charges paid by tenants, while expenditure is on the management and maintenance of the housing stock, and capital financing charges on the HRA's outstanding loan debt.

Interest Rate Risk
Risk that fluctuations in interest rates could impose extra costs against which the Council has failed to protect itself adequately.

Internal Borrowing
Money borrowed from within the Council, sourced from temporary internal cash balances.

Investments
The purchase of financial assets in order to receive income and/or make capital gain at a future time, however with the prime concern being security of the initial sum invested.

Lender Option Borrower Option Loans (LOBOs)
Loans to the Council where the lender can request a change in the rate of interest payable by the Council at pre-defined dates and intervals. The council at this point has the option to repay the loan.

Liquidity
The ability of the Council to meet its financial obligations as they fall due.

Market Loans
Borrowing that is sourced from the market i.e. organisations other than the Public Works Loan Board or a Public Body.

Minimum Revenue Provision (MRP)
This is the amount which must be charged to the authority's revenue account each year and set aside as provision for repaying external loans and meeting other credit liabilities. The prudent amount is determined in accordance with guidance issued by WG. This has the effect of reducing the Capital Financing Requirement (CFR).

Money Market
The market for short-term securities or investments, such as certificates of deposit, commercial paper or treasury bills, with maturities of up to one year.

Money Market Funds
An investment fund which pools the investments of numerous depositors, spreading those investments over a number of different financial instruments and counterparties. Funds with a constant Net Asset Value (NAV) are those where any sum invested is likely to be the same on maturity. Funds with a variable Net Asset Value (NAV) are those where the sum on maturity could be higher or lower due to movements in the value of the underlying investments.

Net Asset Value (NAV)
The market value of an investment fund's portfolio of securities as measured by the price at which an investor will sell a fund's shares or units.

Pooling
The process whereby investments or loans are held corporately rather than for specific projects or parts of the Council, with recharges to those areas for their share of the relevant income and expenditure using an agreed methodology, where such a recharge is required to be made.

Pooled Funds
Investments into bond, equity and property funds offer enhanced returns over the longer term, which are managed by external fund managers with the necessary expertise and skills. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments.

Prudential Code for Capital Finance
The system introduced on 1 April 2004 by Part 1 of the Local Government Act 2003 which allows local authorities to borrow without Government consent, provided that they can afford to service the debt from their own resources and that any such borrowing is prudent and sustainable. This requires the preparation and approval of various indicators.

Public Works Loans Board (PWLB)
The Public Works Loans Board is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.

Refinancing Risk
Risk that maturing borrowing or other financing of capital projects cannot be renewed on terms that reflect existing assumptions and that the Council will suffer extra costs as a result.

Regulatory Risk
Risk that actions by the Council or by any person outside of it are in breach of legal powers or regulatory requirements resulting in losses to the Council, or the imposition of extra costs.

Security
Protecting investments from the risk of significant loss, either from a fall in value or from default of a counterparty.

Sovereign Credit Ratings
The credit rating of a country. It indicates the risk level of the investing environment of a country, taking into account political risk and other factors.

Sterling
The monetary unit of the United Kingdom (the British pound).

Term Deposits
A term deposit is a money deposit at a banking institution that cannot be withdrawn for a certain "term" or period of time.

Treasury Management
Treasury management activities are the management of an organisation'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.

Treasury Bills
Debt securities issued by a government with a short-term maturity of up to 6 months.

UK Government Gilts
Fixed-interest debt securities issued or secured by the British Government. Gilts are always denominated in sterling though the Government occasionally also issues instruments in other currencies in the Eurobond market or elsewhere.

Variable Rate
An interest rate that changes in line with market rates.

Yield
The annual rate of return paid out on an investment, expressed as a percentage of the current market price of the relevant investment.