AGENDA ITEM No.5(ii)

EAST RENFREWSHIRE COUNCIL

AUDIT AND SCRUTINY COMMITTEE

2 February 2017

Report by Head of Accountancy (Chief Financial Officer)

TREASURY MANAGEMENT STRATEGY REPORT FOR 2017/18

PURPOSE OF REPORT

1. To advise the Audit and Scrutiny Committee on the treasury management strategy for the financial year 2017/18.

RECOMMENDATIONS

2. It is recommended that Members:-

(a) consider the content of the Treasury Management Strategy Report for 2017/18;

(b) recommend to the Council that the Treasury Management Strategy for 2017/18 be approved, including the amendment of Treasury Management Practices in accordance with Annex E; and

(c) recommend to the Council that they approve the policy on the repayment of loans fund advances, see section 6.4.

BACKGROUND

3. In line with the revised CIPFA Treasury Management Code of Practice 2011, the Audit and Scrutiny Committee is responsible for ensuring effective scrutiny of the treasury management strategy and policies.

4. The attached Treasury Management Strategy Report for the financial year 2017/18 is submitted in accordance with this requirement.

TREASURY MANAGEMENT STRATEGY FOR 2017/18 (TMS)

5. The TMS for 2017/18 is attached (see Appendix 1).

EQUALITY IMPACT

6. A screening exercise has revealed that the Treasury Management Strategy has no direct relevance to the Council's equality duties

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Treasury Management, Interest Rates, Treasury Strategy, investment, debt rescheduling, Prudential Indicators

APPENDIX 1

EAST RENFREWSHIRE COUNCIL

TREASURY MANAGEMENT STRATEGY 2017/18

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1 Purpose and Scope

1.1 The Council is required to receive and approve, as a minimum, three main reports on treasury activity each year, which incorporate a variety of policies, estimated and actual figures. These reports are as follows:-

a) **Treasury Management Strategy 2017/18** (this report).
This report is the most important of the three reports and covers:
- The capital plans of the Council (including prudential indicators);
- The Treasury Management Strategy (how the investments and borrowings are organised). Including treasury indicators, and
- An investment strategy (investment options and limits applied).

b) **Mid-Year Treasury Management Report** – This will update members with the progress of the capital investment position, amending prudential indicators as necessary, and assess whether the actual treasury operations are adhering to the approved strategy, or whether any policies require revision.

c) **Annual Treasury Report** – This provides details of actual prudential and treasury indicators compared to the estimates within the strategy and performance of actual treasury operations.

1.2 Scrutiny
These reports are required to be adequately scrutinised by committee before being recommended to the Council. This role is undertaken by the Audit and Scrutiny Committee.

1.3 The treasury management issues covered by this report are:

Capital Issues
- The capital plans and associated prudential indicators

Treasury management issues
- The current treasury position
- Prospects for interest rates
- The borrowing strategy
- Treasury indicators which will limit the treasury risk and activities of the Council
- Policy on borrowing in advance of need
- Debt rescheduling
- The investment strategy
- Creditworthiness policy and
- Policy on use of external service providers

1.4 These elements cover the requirements of the Local Government in Scotland Act 2003, the CIPFA Prudential Code (the Prudential Code), the CIPFA Treasury Management Code (the Code) and Scottish Government Investment Regulations.

1.5 Treasury Management Consultants

The Council uses Capita Asset Services as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the Council at all times and will ensure that it does not rely solely upon information and advice from its external service providers.

It also recognises however that there is value in employing external providers of treasury management services in order to gain 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.

1.6 The Treasury Management Strategy covers the treasury management activities for the Council (including any subsidiary organisations i.e. East Renfrewshire Culture & Leisure Trust).

2 Background

2.1 The Council is required to operate a balanced budget, which broadly means that cash received during the year will meet cash expenditure. A major aspect of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, ensuring adequate liquidity before considering investment return.

2.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, being essentially longer term cash flow planning to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

2.3 The Prudential and Treasury Indicators (summarised in **Annex A**) consider the affordability and impact of capital expenditure decisions, and set out the Council's overall capital framework. These Indicators have been developed in line with both the Prudential and Treasury Codes. The treasury service considers the effective funding of these decisions. Together they form part of the process which ensures the Council meets its balanced budget requirement under the Local Government Finance Act 1992. The Treasury Management Strategy therefore forms an integral part of the Council's overall financial planning covering both its revenue and capital budgets.

2.4 CIPFA defines treasury management as:

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

3 The Capital Prudential Indicators 2017/18 – 2019/20

The Council's longer term planning for its financial management is required to:

(i) Raise the funds required by the Council to meet approved service levels in the most effective manner;

(ii) Manage the effective deployment of those funds in line with the Council's corporate objectives and priorities; and

(iii) Provide stability in resource planning and service delivery as expressed through revenue and capital budgets and approved Corporate Plans.

As part of achieving these aims the Council plans to continue to invest in infrastructure through a sustainable capital programme financed by £11.25m capital financing revenue implications per annum (increasing to £11.40m per annum from 2018/19). This creates the affordability and sustainability financial boundaries for the development of the Council's Capital Financial Plan.

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

3.1 Capital Expenditure (Prudential Indicator PI-1)

a) This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously and those forming part of this planning cycle. The indicator also includes additional expenditure which, for the purposes of financial planning and reporting, must be treated as capital expenditure. This expenditure relates to the construction of the new Barrhead High School and is the estimated investment which will be supported by the Scottish Government through ongoing revenue grant.

b) The following capital expenditure forecasts are in line with the general fund capital plan for 2017/18-2024/25 and housing capital plan 2017/18- 2021/22 which will be submitted to Council on 9 February 2017 together with the additional expenditure outlined above:

Capital Expenditure (PI-1) £'000	**2015/16 Actual**	**2016/17 Probable**	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**
General Fund					
– Capital Programme	19,151	45,134	35,369	41,666	18,996
– Other Relevant Expenditure			22,811		
General Fund Subtotal	19,151	45,134	58,180	41,666	18,996
Housing	5,529	4,884	8,281	8,122	8,054
Total	**24,680**	**50,018**	**66,461**	**49,788**	**27,050**

The increase in the housing capital plans relates to the need to achieve new energy efficiency standards and to the Council's plans to increase housing stock.

3.2 Capital Financing Assumptions

a) The table below summarises the capital expenditure plans for general fund and how these plans are being financed. Any shortfall of resources results in financial need.

General Fund £'000	**2015/16 Actual**	**2016/17 Probable**	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**
Capital Expenditure	19,151	45,134	35,369	41,666	18,996
Other Relevant Expenditure			22,811		
Total	19,151	45,134	58,180	41,666	18,996
Financed by:					
Capital Receipts	2,360	150	3,100	1,700	750
Capital Reserve	4,500	20,230	7,470	-	-
Developer Contributions	357	806	1,017	1,483	1,462
Govt. General Capital Grants	7,910	5,954	7,010	7,630	7,629
Govt. Specific Capital Grants	1,269	2,569	1,427	1,200	1,200
Other Grants & Contributions	839	568	75	75	75
Repairs & Renewals Fund/CFCR	210	790	158	-	-
Net financing need for the year	**1,706**	**14,067**	**37,923**	**29,578**	**7,880**

The 2016/17 probable capital expenditure figure of £45.134m is in line with the capital monitoring report submitted to Cabinet on 1 December 2016. However as part of the long term capital planning process the level and timing of capital receipts, developer contributions, capital reserve and borrowing has been revised. These revisions will be incorporated within the final 2016/17 monitoring report submitted to Cabinet during March 2017.

b) The table below summarises the capital expenditure plans for housing and how these plans are being financed. Any shortfall of resources results in financial need.

Housing £'000	**2015/16 Actual**	**2016/17 Probable**	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**
Capital Expenditure	5,529	4,884	8,281	8,122	8,054
Financed by:					
Capital Receipts – Right to Buy	943	800	-	-	-
Capital Receipts – Land Disposal	-	-	-	500	500
Recharges to Owners	382	462	569	365	234
Govt. Specific Capital Grants	691	34	1,865	1,810	1,810
Commuted Sums	527	96	300	300	300
Net financing need for the year	**2,986**	**3,492**	**5,547**	**5,147**	**5,210**

c) The table below summarises the financial need resulting from both the general fund and housing capital plans.

Financial Need £'000	**2015/16 Actual**	**2016/17 Probable**	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**
General Fund	1,706	14,067	37,923	29,578	7,880
Housing	2,986	3,492	5,547	5,147	5,210
Net financing need for the year	**4,692**	**17,559**	**43,470**	**34,725**	**13,090**

3.3 The Council's Borrowing Need (the Capital Financing Requirement – Prudential Indicator PI-2)

a) 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 identified above, which has not immediately been paid for (e.g. via grants), will increase the CFR. The CFR does not increase indefinitely, as scheduled debt amortisation (loans charges) broadly reduces the borrowing need in line with each asset's life.

b) The CFR includes any other long term liabilities (e.g. PPP 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 has liabilities of £78.863m relating to such schemes as at 31 March 2016.

c) The Council is asked to approve the CFR projections below:

Capital Financing Requirement (PI-2) £'000	2015/16 Actual	2016/17 Probable	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
General Fund	**152,088**	**156,309**	**183,626**	**202,085**	**198,559**
Housing	**28,255**	**28,934**	**31,495**	**33,483**	**35,349**
Total CFR (PI-2)*	**180,343**	**185,243**	**215,121**	**235,568**	**233,908**
Movement in CFR represented by:					
Net financing need for the year (above)		17,559	43,470	34,725	13,090
Less scheduled debt amortisation and other financing movements		(12,659)	(13,592)	(14,278)	(14,750)
Movement in CFR		**4,900**	**29,878**	**20,447**	**(1,660)**

**The CFR for this calculation includes capital expenditure to 31 March of each financial year.*

The significant increase between 2016/17 and subsequent years is driven by the shift in the net financing need for the year as detailed in the tables within section 3.2. The increase in the CFR is mainly related to the increased levels of expenditure within the capital plans. However two main contributors are the City Deal initiative with borrowing of £30,828,000 (over the 3 year period 2017/18 to 2019/20) and the new Barrhead High School project with debt of £22,811,000 (2017/18).

3.4 Affordability Prudential Indicators

a) Further 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 updated indicators are as follows:

Ratio of financing costs to net revenue stream (Prudential Indicator PI-3)

b) This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs, net of investment income) against the net revenue stream.

Ratio of Financing Costs to Net Revenue Stream (PI-3)	2015/16 Actual	2016/17 Probable	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
General Fund	**8.6%**	**8.5%**	**9.4%**	**10.0%**	**10.3%**
Housing	**35.3%**	**37.0%**	**38.2%**	**39.1%**	**39.4%**

The estimates of financing costs include current commitments and the proposals in the capital plans for 2016/17 to 2019/20. The increase from 2017/18 onwards within the ratio for the general fund is a result of both the increased finance costs associated with new Barrhead High School and an estimated reduction in overall government grant support. The levels of government grant support for 2018/19 and 2019/20 have not been issued and this indicator is based on estimates.

While the overall level of grant support is estimated to reduce during these years the increased financing costs associated with Barrhead High School will be covered in full by a specific revenue grant scheme provided by the Scottish Government/Scottish Futures Trust.

The increasing ratio for Housing reflects the increased investment levels in the Housing stock.

Incremental impact of capital investment decisions on council tax (Prudential Indicator PI-4a)

c) This indicator calculates the impact of capital investment decisions on council tax and takes account of the level of support provided by the Scottish Government – both capital grant support and ongoing revenue support. The impact of additional borrowing will be covered in full by corresponding revenue savings or by an additional revenue income stream (Scottish Government support for Barrhead High School). On this basis there is no impact on council tax over the three year period. As outlined above the levels of government support for 2018/19 and 2019/20 have not been issued and this indicator is also based on estimates.

Incremental Impact of Capital Investment Decisions on the Band D Council Tax (PI-4a)	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Incremental Impact on Band D Council Tax	£0.00	£0.00	£0.00

Incremental impact of capital investment decisions on rents (Prudential Indicator PI-4b)

d) This indicator calculates the impact of capital investment decisions on rents before taking into account savings which have been identified to mitigate the additional costs.

Incremental Impact of Capital Investment Decisions on Rents (PI-4b)	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Incremental Impact on Rents (52 weeks)	£0.10	£1.04	£1.26

4 Treasury Management Strategy

Section 3 provides a summary of the capital expenditure plans. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional Codes, so that sufficient cash is available to meet its liabilities as they fall due. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury/prudential indicators, the current and projected debt positions and the annual investment strategy.

4.1 Current Portfolio Position

a) The Council's actual and projected debt portfolio is summarised below. The table compares the actual and projected external debt against the Council's estimated borrowing need (the Capital Financing Requirement – CFR), highlighting any over or under borrowing.

£'000 as at 31 March	2015/16 Actual	2016/17 Probable	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Borrowing	60,597	68,510	106,755	114,147	111,994
Other Long Term Liabilities	78,863	75,949	95,293	90,984	86,252
Total Gross Debt (Prudential Indicator PI-5)	**139,460**	**144,459**	**202,048**	**205,131**	**198,246**
CFR – the borrowing need	**180,343**	**185,243**	**215,121**	**235,568**	**233,908**
(Under) / Over Borrowing (Prudential Indicator PI-6)	**(40,883)**	**(40,784)**	**(13,073)**	**(30,437)**	**(35,662)**

b) Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these (PI-6) is that the Council needs to ensure that its gross debt figure (shown above) 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 the current and following two financial years. This allows some flexibility for limited borrowing for future years, but ensures that borrowing in advance of need is not undertaken for revenue purposes.

c) The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded by external loan debt as the cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy remains both prudent and cost effective as investment returns are low and counterparty risk is relatively high

4.2 Treasury Indicators: Limits to Borrowing Activity

The Operational Boundary (Prudential Indicator PI-7)

a) This indicator takes account of capital expenditure and financing requirements and projects the expected level of external debt for operational purposes. Temporary breaches of the operational boundary are quite acceptable and the Head of

Accountancy/Chief Financial Officer has delegated authority to manage the movement between borrowing and other long term liabilities such as finance leases in accordance with option appraisal and value for money considerations. Any such movement will be reported to Council following the change.

Operational boundary for external debt (PI-7) £'000	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Borrowing	108,510	116,755	114,147
Other Long Term Liabilities	98,760	95,293	90,984
Total	207,270	212,048	205,131

The Authorised Limit for External Debt (Prudential indicator PI-8)

a) This indicator is similar to the operational boundary but includes headroom to accommodate adverse cash flow movements. It represents a limit which external debt is not expected to exceed and reflects the level of external borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. In circumstances where a breach takes place the reasons shall be reported to the next meeting of the Council and the limit revised if appropriate. The same delegated powers are in place as for the operational boundary.

b) This is the statutory limit (Affordable Capital Expenditure Limit) determined under section 35(1) of the Local Government in Scotland 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.

c) The proposed Authorised Limit for the Council is as follows:

Authorised limit for external debt (PI-8) £'000	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Borrowing	124,787	134,268	131,269
Other Long Term Liabilities	98,760	95,293	90,984
Total	223,547	229,561	222,253

4.3 Prospects for Interest Rates

a) The Council has appointed Capita Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Annex B draws together a number of current city forecasts for short term (Base Rate) and longer fixed interest rates and the following table and commentary below gives the central view of Capita Asset Services.

Annual Average %	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)			
		5 year	10 year	25 year	50 year
Dec 2016	0.25	1.6	2.3	2.9	2.7
Mar 2017	0.25	1.6	2.3	2.9	2.7
Jun 2017	0.25	1.6	2.3	2.9	2.7
Sep 2017	0.25	1.6	2.3	2.9	2.7
Dec 2017	0.25	1.6	2.3	3.0	2.8
Mar 2018	0.25	1.7	2.3	3.0	2.8
Jun 2018	0.25	1.7	2.4	3.0	2.8
Sep 2018	0.25	1.7	2.4	3.1	2.9
Dec 2018	0.25	1.8	2.4	3.1	2.9
Mar 2019	0.25	1.8	2.5	3.2	3.0
Jun 2019	0.50	1.9	2.5	3.2	3.0
Sep 2019	0.50	1.9	2.6	3.3	3.1
Dec 2019	0.75	2.0	2.6	3.3	3.1
Mar 2020	0.75	2.0	2.7	3.4	3.2

b) The Monetary Policy Committee, (MPC), cut Bank Rate from 0.50% to 0.25% on 4th August in order to counteract what it forecast was going to be a sharp slowdown in growth in the second half of 2016. It also gave a strong steer that it was likely to cut Bank Rate again by the end of the year. However, economic data since August has indicated much stronger growth in the second half 2016 than that forecast; also, inflation forecasts have risen substantially as a result of a continuation of the sharp fall in the value of sterling since early August. Consequently, Bank Rate was not cut again in November or December and, on current trends, it now appears unlikely that there will be another cut, although that cannot be completely ruled out if there was a significant dip downwards in economic growth. During the two-year period 2017 – 2019, when the UK is negotiating the terms for withdrawal from the EU, it is likely that the MPC will do nothing to dampen growth prospects, (i.e. by raising Bank Rate), which will already be adversely impacted by the uncertainties of what form Brexit will eventually take. Accordingly, a first increase to 0.50% is not tentatively pencilled in, as in the table above, until quarter 2 2019, after those negotiations have been concluded, (though the period for negotiations could be extended). However, if strong domestically generated inflation, (e.g. from wage increases within the UK), were to emerge, then the pace and timing of increases in Bank Rate could be brought forward.

c) Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The above forecasts, (and MPC decisions), will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

d) The overall longer run trend is for gilt yields and PWLB rates to rise, albeit gently. It has long been expected that at some point, there would be a start to a switch back from bonds to equities after an historic long term trend over about the last twenty five years of falling bond yields. The action of central banks since the financial crash of

2008, in implementing substantial quantitative easing purchases of bonds, added further impetus to this downward trend in bond yields and rising prices of bonds. The opposite side of this coin has been a rise in equity values as investors searched for higher returns and took on riskier assets. The sharp rise in bond yields since the US Presidential election, has called into question whether, or when, this trend has, or may, reverse, especially when America is likely to lead the way in reversing monetary policy. Until 2015, monetary policy was focused on providing stimulus to economic growth but has since started to refocus on countering the threat of rising inflationary pressures as strong economic growth becomes more firmly established. The expected substantial rise in the Federal funds rate over the next few years may make holding US bonds much less attractive and cause their prices to fall, and therefore bond yields to rise. Rising bond yields in the US would be likely to exert some upward pressure on bond yields in other developed countries but the degree of that upward pressure is likely to be dampened by how strong, or weak, the prospects for economic growth and rising inflation are in each country, and on the degree of progress in the reversal of monetary policy away from quantitative easing and other credit stimulus measures.

e) PWLB rates and gilt yields have been experiencing exceptional levels of volatility that have been highly correlated to geo-political, sovereign debt crisis and emerging market developments. It is likely that these exceptional levels of volatility could continue to occur for the foreseeable future.

f) The overall balance of risks to economic recovery in the UK is to the downside, particularly in view of the current uncertainty over the final terms of Brexit and the timetable for its implementation.

g) Apart from the above uncertainties, **downside risks to current forecasts** for UK gilt yields and PWLB rates currently include:

- Monetary policy action by the central banks of major economies reaching its limit of effectiveness and failing to stimulate significant sustainable growth, combat the threat of deflation and reduce high levels of debt in some countries, combined with a lack of adequate action from national governments to promote growth through structural reforms, fiscal policy and investment expenditure.
- Major national polls:
  - Italian constitutional referendum 04.12.16 resulted in a ‘No’ vote which led to the resignation of Prime Minister Renzi. This means that Italy needs to appoint a new government.
  - Spain has a minority government with only 137 seats out of 350 after already having had two inconclusive general elections in 2015 and 2016. This is potentially highly unstable.
  - Dutch general election 15.3.17;
  - French presidential election April/May 2017;
  - French National Assembly election June 2017;
  - German Federal election August – October 2017.
- A resurgence of the Eurozone sovereign debt crisis, with Greece being a particular problem, and stress arising from disagreement between EU countries on

free movement of people and how to handle a huge influx of immigrants and terrorist threats

- Weak capitalisation of some European banks, especially Italian.
- Geopolitical risks in Europe, the Middle East and Asia, causing a significant increase in safe haven flows.
- UK economic growth and increases in inflation are weaker than we currently anticipate.
- Weak growth or recession in the UK's main trading partners - the EU and US.

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

- UK inflation rising to significantly higher levels than in the wider EU and in the US, causing an increase in the inflation premium in gilt yields.
- A rise in US Treasury yields as a result of Federal funds rate increases and rising inflation expectations in the USA, dragging UK gilt yields upwards.
- The pace and timing of increases in the Federal funds rate causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.
- A downward revision to the UK's sovereign credit rating undermining investor confidence in holding sovereign debt (gilts).

i) The current economic outlook and structure of market interest rates and government debt yields have several key treasury management implications:-

- Investment returns are likely to remain low during 2017/18 and beyond;
- Borrowing interest rates have been on a generally downward trend during most of 2016 up to mid-August; they fell sharply to historically phenomenally low levels after the referendum and then even further after the MPC meeting of 4th August when a new package of quantitative easing purchasing of gilts was announced. Gilt yields have since risen sharply due to a rise in concerns around a 'hard Brexit', the fall in the value of sterling, and an increase in inflation expectations. The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in later times when authorities will not be able to avoid new borrowing to finance capital expenditure and/or to refinance maturing debt;
- There will remain a cost of carry to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost – the difference between borrowing costs and investment returns.

j) **Annex C** contains a more comprehensive Economic Background narrative from Capita Asset Services.

4.4 Borrowing Strategy

a) The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded by external loan debt as the cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy remains both prudent and cost effective as investment returns are low and counterparty risk is relatively high.

b) Against this background and the risks within the economic forecast, caution will be adopted with the 2017/18 treasury operations. The Chief Financial Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *If it was felt that there was a significant risk of a sharp **FALL** in long and short term rates*, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- *If it was felt that there was a significant risk of a much sharper **RISE** in long and short term rates than that currently forecast*, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed funding will be drawn whilst interest rates are lower that they are projected to be in the next few years.

c) Any decisions will be reported to Members at the next available opportunity.

Treasury Management Limits on Activity

d) There are three debt related treasury activity limits. The purpose of these is to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive, they will impair the opportunities to reduce costs / improve performance. The indicators are:

(i) **Upper limits on fixed interest rate exposure (Treasury Indicator TI-1)**

This covers a maximum limit for borrowing exposure to fixed interest rates, based on the debt position and is set at 100%.

(ii) **Upper limits on variable interest rate exposure (Treasury Indicator TI-2)**

This identified a maximum limit for borrowing exposure to variable interest rates based upon the debt position and is set at 30%.

(iii) Maturity structure of borrowing (Treasury Indicator TI-3)

Gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing. The Council has set the limit of debt maturing in any one year to 15%.

4.5 Policy on borrowing in advance of need

a) The Council will not borrow in advance of its needs, purely in order to profit from the investment of the extra sums borrowed.

b) Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

c) Borrowing in advance is defined as any borrowing undertaken by the local authority which will result in the total external debt of the local authority exceeding the capital financing requirement (CFR) of the local authority for the following twelve month period. This twelve month period is on a rolling twelve month basis.

d) The Chief Financial Officer has the authority to borrow in advance of need under delegated power where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or meet budgetary constraints. The Chief Financial Officer will adopt a cautious approach to any such borrowing and a business case to support the decision making process must consider:
   - The benefits of borrowing in advance,
   - The risks created by additional levels of borrowing and investment, and
   - How far in advance it is reasonable to borrow considering the risks identified

e) Any such advance borrowing should be reported through the mid-year or annual Treasury Management reporting mechanism.

4.6 Debt Rescheduling

a) As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

b) The reasons for any rescheduling to take place will include:

   - The generation of cash savings and/or discounted cash flow savings
   - Helping to fulfil the treasury strategy
   - Enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

c) Consideration will also be given to identify if there is any potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

d) All rescheduling will be reported to the Council at the earliest meeting following its action.

5 Investment Strategy

5.1 Investment Objectives and Policy

a) The Council’s investment policy has regard to the Scottish Government’s Investment (Scotland) Regulations (and accompanying Finance Circular) and the latest CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes (“the Code”).

b) The Council's primary investment objectives are:
   i) The safeguarding or **security** of the re-payment of principal and interest of investments on a timely basis; and
   ii) The **liquidity** of its investments

c) The council will also aim to achieve the optimum return on its investments corresponding with proper levels of security and liquidity. The risk appetite of this Council is low in order to give priority to security of its investments.

d) In accordance with the above guidance from the Scottish Government and CIPFA, and in order to minimise the risk to investments, the Council has below (see 5.3 below) clearly stipulated the minimum acceptable credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk. The intention of the approach is to provide security of investment and minimisation of risk.

e) Ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion on the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.

f) Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of the potential investment counterparties.

g) The borrowing of monies purely to invest or on-lend, without relevant Scottish Government consent, is unlawful and this Council will not engage in such activity.

h) The Council will ensure its investments have sufficient liquidity. For this purpose it will set out procedures for determining the maximum periods over which funds may prudently be committed.

5.2 Council Permitted Investments

a) The Local Government Investments (Scotland) Regulations 2010 require the Council to give approval for all the types of investments to be used and set appropriate limits for the amount that can be held in each investment type. These types of investments are termed **Permitted Investments** and any investments used which have not been approved as a permitted investment will be considered ultra vires.

b) The permitted investment instruments which may be used by the Council (and its subsidiary organisations) in the forthcoming year are detailed in **Annex D**, and include the following:

Cash type instruments

- Deposits with the Debt Management Account Facility (DMADF) (UK Government)
- Deposits with other local authorities or public bodies
- Money Market Funds
- Enhanced Cash Flows

- Call account deposit accounts with financial institutions (banks and building societies) meeting the Creditworthiness Policy
- Term deposits with financial institutions (banks and building societies) meeting the Creditworthiness Policy
- UK Government Gilts and Treasury Bills
- Certificates of Deposit with financial institutions (banks and building societies)
- Structured deposit facilities with banks and building societies
- Corporate Bonds
- Floating Rate Note

Other investments

- Investment properties
- Loans to third parties, including soft loans
- Loans to local authority companies/partnerships/ charity
- Shares in Hub schemes

c) Details of the risks, mitigating controls and limits associated with each of these permitted categories are also shown in **Annex D**.

5.3 Creditworthiness Policy

The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle, the Council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security as set out in the investment sections below; and
- It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

The Head of Accountancy will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary (see annex E). These criteria provide an overall pool of classes of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

Credit rating information is supplied by Capita Asset Services our treasury consultants, on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list, with the exception of the Council's own banker. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing. For instance, a negative rating watch applying to a counterparty at the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions. The criteria for providing a pool of high quality investment counterparties is:

- Banks 1 - good credit quality **–** the Council will only use banks which are UK banks and have, as a minimum, the following Fitch (or equivalent) ratings (where rated):
    i. Short Term – *F1*
    ii. Long Term – *A-*
- Banks 2 – Part nationalised UK bank – Royal Bank of Scotland. This bank can be included if it continues to be part nationalised or it meets the ratings in Banks 1 above.
- Banks 3 – The Council's own banker for transactional purposes if the bank falls below the above criteria, although in this case balances will be minimised in both monetary size and time invested.
- Bank subsidiary and treasury operation - The Council will use these where the parent bank has provided an appropriate guarantee or has the necessary ratings outlined above.
- Building societies - The Council will use societies which meet the ratings for banks outlined above;
- Money Market Funds
- Enhanced cash funds (ECFs)
- UK Government (including gilts and the DMADF)
- Local authorities, including Police & Fire

Use of additional information other than credit ratings. Additional requirements under the Code require the Council to supplement credit rating information. Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information (for example Credit Default Swaps, negative rating watches/outlooks) will be applied to compare the relative security of differing investment counterparties.

Time and monetary limits applying to investments. The time and monetary limits for institutions on the Council's counterparty list are as stated in Annex E.

5.4 Country and Council's Banker

Country Limits

a) The Council has determined that it will only use approved counterparties from within the United Kingdom.

Council's Own Banker

b) The Council's own banker (currently The Clydesdale bank) will be maintained on the Council's counterparty list in situations where rating changes mean this is below the above criteria. This is to allow the Council to continue to operate normal current account banking facilities overnight and short-term investment facilities.

5.5 The Monitoring of Investment Counterparties

a) All credit ratings will be monitored on a weekly basis. The Council is alerted to changes to ratings of all three agencies through its use of the creditworthiness service of Capita Asset Services.

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

b) If the Council has funds invested in an institution which is downgraded to below the acceptable rating criteria, the Council will enter discussions with the counterparty to establish if the funds can be returned early. This however will be subject to an appropriate cost versus risk assessment of the specific situation.

c) The criteria for choosing counterparties set out above provide a sound approach to investment in "normal" market circumstances. Under exceptional market conditions, the Chief Financial Officer may temporarily restrict further investment activity to those counterparties considered of higher credit quality than the minimum criteria set out in this Strategy. These restrictions will remain in place until the Chief Financial Officer is of an opinion that the banking system has returned to 'normal'. Similarly a restriction may be placed on the duration of investments.

5.6 Types of Investments

a) For institutions on the approved counterparty list, investments will be restricted to safer instruments (as listed in Annex D). Currently this involves the use of money market funds, the Debt Management Agency Deposit Facility (DMADF) and institutions with higher credit ratings than the minimum permissible rating outlines in the investment strategy, as well as the Council's own bank.

b) Where appropriate, investments will be made through approved brokers. The current list of approved brokers comprises:

- Sterling International Brokers Limited
- Tradition (UK) Limited
- Martins Brokers
- King and Shaxson Capital Limited

5.7 Investment Strategy and bank rate projections

In-house funds

a) Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

Bank Rate

b) Bank Rate is forecast to stay flat at 0.25% until quarter 2 of 2019. Bank Rate forecasts for financial year-ends (March) as at January 2017 are:

2016/2017	0.25%
2017/2018	0.25%
2018/2019	0.25%
2019/2020	0.75%

c) The overall balance of risks to these forecasts is currently probably slightly skewed to the downside in view of the uncertainty over the final terms of the Brexit. If growth expectations disappoint and inflationary pressures are minimal, the start of increases in Bank Rate could be pushed back. On the other hand, should the pace of growth quicken and/or forecasts for increases in inflation rise, there could be an upside risk i.e. Bank Rate increases occur earlier and/or at a quicker pace.

Investment Treasury Indicator And Limit (Treasury Indicator TI-4)
Total Principal Funds Invested for Greater Than 364 days

d) These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

e) The treasury indicator and limit proposed is:

Maximum principal sums invested > 364 days (TI-4)			
£m	2015/16	2016/17	2017/18
Principal sums invested > 364 days	5%	5%	5%

f) For positive cash balances and in order to maintain liquidity, the Council will seek to use overnight investment accounts, short term (< 1 month) notice accounts, money market funds and short-dated deposits (overnight to six months).

5.8 Risk Benchmarking

These benchmarks are simple guides to minimise risk, so they may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmarks is that officers will monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the mid-year or annual report.

a) Security

The Council's **maximum** security risk benchmark for the current portfolio, when compared to historic default tables, is:

0.067% historic risk of default when compared to the whole portfolio for 1 year.

b) Liquidity

In respect of this area the Council seeks to maintain:

- Bank Overdraft: £100,000

c) Yield

Local Measures of yield benchmarks are:

Investments – Internal returns above the 7 day LIBID rate

d) Activity

At the end of the financial year, the Chief Financial Officer will report on its investment activity as part of the annual treasury report.

6 Performance Indicators

6.1 The CIPFA Code requires the Council to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking.

6.2 Debt Performance Indicators

(i) Average "Pool Rate" charged by the Loans Fund compared to Scottish Local Authority average Pool Rate

Target is to be at or below the Scottish Average for 2016/17

(ii) Average borrowing rate movement year on year
Target is to maintain or reduce the average borrowing rate for the Council versus 2016/17.

6.3 Loan Charges

a) Loan Charges for 2017/18 are expected to be at or below the Revenue Budget estimate contained in the Council's Financial Plans to be approved in February 2017, which are estimated as follows:

£m	2017/18 Estimate	2018/19 Estimate
Capital Repayments	7.139	6.874
Interest on Borrowing	3.976	4.372
Expenses	0.135	0.154
Total Loan Charges*	**11.250**	**11.400**

**The Loan Charges exclude the capital element of PPP repayments*

6.4 Statutory Repayment of Loans Fund Advances

Under the Local Authority (Capital Financing and Accounting) (Scotland) Regulations 2016, the Council is required to set out its policy for the statutory repayment of loans fund advances prior to the start of the financial year. The repayment of loans fund advances ensures that the Council makes a prudent provision each year to pay off an element of the accumulated loans fund advances made in previous financial years.

A variety of options are provided to Councils so long as a prudent provision is made each year. The Council is recommended to approve the following policy on the repayment of loans fund advances:-

- For loans fund advances made before 1 April 2016, the policy will be to maintain the practice of previous years and apply the Statutory Method (in line with Schedule 3 of the Local Government (Scotland) Act 1975), with all loans fund advances being repaid by the annuity method in line with the repayment profile determined in previous years.

- Loans fund advances relating to City Deal projects which will be supported in later years by Government funding will be repaid in accordance with the funding/income profile method. This links the repayments to the project income stream.

- For loans fund advances made after 1 April 2016, excluding the above, the Council will continue to calculate loan charge repayments in line with Schedule 3 of the Local Government (Scotland) Act 1975, using an annuity rate of 4%. This rate is in keeping with the estimated loans fund rate for 2016/17 to 2020/21. The Council is permitted to use this option for new borrowing taken out over a transitional period of five years until 31 March 2021. Thereafter a new policy approach based on depreciation, asset life periods or funding/income profile must be adopted for any further new borrowing.

The Non-HRA loans fund balances are expected to be, with year 1 being 2016/17:

£'000	Year 1	Years 2-5	Years 5-10	Years 10-15	Years 15-20	etc
opening balance	73,226	80,628	113,646	90,789	51,821	22,474
advances	14,335	53,641	12,580			
repayments	6,933	20,623	35,437	38,968	29,347	22,474
closing balance	80,628	113,646	90,789	51,821	22,474	0

The HRA loans fund balances are expected to be, with year 1 being 2016/17:

£'000	Year 1	Years 2-5	Years 5-10	Years 10-15	Years 15-20	etc
opening balance	28,255	28,954	35,369	27,367	17,111	10,132
advances	3,512	15,904	8,178			
repayments	2,813	9,489	16,180	10,256	6,979	10,132
closing balance	28,954	35,369	27,367	17,111	10,132	0

7 Monitoring and Reporting

7.1 In line with the CIPFA Code the following formal reporting arrangements will be adopted:

Requirement	Purpose	Responsible Body	Frequency
Scrutiny of Treasury Management Strategy	Detailed scrutiny prior to annual approval by Council	Audit & Scrutiny Committee	Annually
Treasury Management Strategy	Reporting on Annual Strategy	Council	Annually prior to start of new financial year
Scrutiny of Treasury Management Mid-Year Report	Detailed scrutiny prior to annual approval by Council	Audit & Scrutiny Committee	Annually in October/November of the current year
Treasury Management Mid-Year Report	Mid-Year Performance Report	Council	Annually after reported to the Audit & Scrutiny Committee
Scrutiny of Treasury Management Annual Report	Detailed scrutiny prior to annual approval by Council	Audit & Scrutiny Committee	Annually in September/ October of the financial year
Treasury Management Annual Report	Annual Performance report for previous financial year	Council	Annually after reported to the Audit & Scrutiny Committee
Treasury Management Practices		Council	As appropriate
Treasury Management Policy Statement	Reviews and Revisions	Council	As required

8 Treasury Management Consultants and Advisers

8.1 The Council uses Capita Asset Services as its external treasury management consultants. The company provides a range of services which include:

- Technical support on treasury matters, capital financing issues and the drafting of Member reports
- Economic and interest rate analysis

- Debt services which includes advice on the timing of borrowing
- Debt rescheduling advice surrounding the existing portfolio
- Generic investment advice on interest rates, timing and investment instruments
- Credit ratings/market information service

8.2 As part of the service provided, Capita meet with Council officers periodically to review the current Treasury Management and Investment Strategies and also review the service provided to the Council.

8.3 The Council recognises that responsibility for treasury management decisions remains with the Council at all times and will ensure that it does not only rely upon information and advice from our external service providers.

8.4 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.

9 Member and Officer Training

9.1 The increased Member consideration of treasury management matters and the need to ensure that officers dealing with treasury management are trained and kept up to date requires a suitable training process for Members and officers. This Council will address this important issue by:

a) Elected Members
   - Working with members to identify their training needs
   - Working with Capita Asset Services to identify appropriate training provision for elected members

b) Officers dealing with treasury management matters will have the option of various levels of training including:
   - Treasury courses run by the Council's advisers
   - Attendance at CIPFA treasury management training events
   - Attendance at the CIPFA Scottish Treasury Management Forum and information exchanged via the Treasury Management Forum network
   - Training identified as part of the Council's Performance Review & Development system in line with the approved Treasury Management Practices (TMPs).

ANNEXES

ANNEX A

SUMMARY OF PRUDENTIAL AND TREASURY INDICATORS

Indicator Reference	Indicator	Page Ref.	2017/18	2018/19	2019/20
PRUDENTIAL INDICATORS					
Capital Expenditure Indicator					
PI-1	Capital Expenditure Limits General Fund Housing Total	7	£'000 58,180 8,281 66,461	£'000 41,666 8,122 49,788	£'000 18,996 8,054 27,050
PI-2	Capital Financing Requirement General Fund Housing Total	9	£'000 183,626 31,495 215,121	£'000 202,085 33,483 235,568	£'000 198,559 35,349 233,908
Affordability Indicator					
PI-3	Ratio of Financing Costs to Net Revenue Stream General Fund Housing	9	9.4% 38.2%	10.0% 39.1%	10.3% 39.4%
PI-4a	Incremental Impact of Capital Investment Decisions on Council Tax	10	£0.00	£0.00	£0.00
PI-4b	Incremental Impact of Capital Investment Decisions on Rents (52 weeks)	10	£0.10	£1.04	£1.26
External Debt Indicators					
PI-5	Gross Debt Borrowing Other Long Term Liabilities Total	11	£'000 106,755 95,293 202,048	£'000 114,147 90,984 205,131	£'000 111,994 86,252 198,246
PI-7	Operational Boundary for External Debt Borrowing Other Long Term Liabilities Total	11	£'000 108,510 98,760 207,270	£'000 116,755 95,293 212,048	£'000 114,147 90,984 205,131
PI-8	Authorised Limit for External Debt Borrowing Other Long Term Liabilities Total	12	£'000 124,787 98,760 223,547	£'000 134,268 95,293 229,561	£'000 131,269 90,984 222,253
Indicators of Prudence					
PI-6	(Under)/Over Gross Borrowing against the CFR	11	£'000 (13,073)	£'000 (30,437)	£'000 (35,662)
TREASURY INDICATORS					
TI-1	Upper Limit to Fixed Interest Rates based on Net Debt	15	100% of debt position		
TI-2	Upper Limit to Variable Interest Rates based on Net Debt	15	30% of debt position		
TI-3	Maturity Structure of Fixed Interest Rate Borrowing	15	15% maturing in any one year		
TI-4	Maximum Principal Sum invested greater than 364 days	20	5%	5%	5%

ANNEX B: INTEREST RATE FORECASTS 2017 -2020

Capita Asset Services Interest Rate View	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Dec-19	Mar-20
Bank Rate View	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%	0.75%	0.75%
3 Month LIBID	0.30%	0.30%	0.30%	0.30%	0.30%	0.30%	0.30%	0.30%	0.40%	0.50%	0.60%	0.80%	0.90%
6 Month LIBID	0.40%	0.40%	0.40%	0.40%	0.40%	0.40%	0.40%	0.40%	0.50%	0.60%	0.70%	0.90%	1.00%
12 Month LIBID	0.70%	0.70%	0.70%	0.70%	0.70%	0.70%	0.80%	0.80%	0.90%	1.00%	1.10%	1.30%	1.40%
5yr PWLB Rate	1.60%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.80%	1.80%	1.90%	2.00%	2.00%
10yr PWLB Rate	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	2.40%	2.40%	2.40%	2.50%	2.50%	2.60%	2.70%
25yr PWLB Rate	2.90%	2.90%	2.90%	2.90%	3.00%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.40%
50yr PWLB Rate	2.70%	2.70%	2.70%	2.70%	2.80%	2.80%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.20%
Bank Rate													
Capita Asset Services	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%	0.75%	0.75%
Capital Economics	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%	0.75%
5yr PWLB Rate													
Capita Asset Services	1.60%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.80%	1.80%	1.90%	2.00%	2.00%
Capital Economics	1.60%	1.70%	1.80%	1.90%	1.95%	2.05%	2.20%	2.30%	2.40%	2.60%	2.80%	3.20%	3.30%
10yr PWLB Rate													
Capita Asset Services	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	2.40%	2.40%	2.40%	2.50%	2.50%	2.60%	2.70%
Capital Economics	2.30%	2.35%	2.45%	2.50%	2.55%	2.60%	2.70%	2.70%	2.80%	3.00%	3.20%	3.60%	3.70%
25yr PWLB Rate													
Capita Asset Services	2.90%	2.90%	2.90%	2.90%	3.00%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.40%
Capital Economics	2.90%	3.00%	3.05%	3.10%	3.15%	3.25%	3.30%	3.35%	3.45%	3.55%	3.75%	4.15%	4.35%
50yr PWLB Rate													
Capita Asset Services	2.70%	2.70%	2.70%	2.70%	2.80%	2.80%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.20%
Capital Economics	2.80%	2.85%	2.95%	3.00%	3.05%	3.10%	3.15%	3.20%	3.30%	3.50%	3.70%	4.10%	4.20%

ANNEX C

CAPITA Economic Background

UK. **GDP growth rates** in 2013, 2014 and 2015 of 2.2%, 2.9% and 1.8% were some of the strongest rates among the G7 countries. Growth is expected to have strengthened in 2016 with the first three quarters coming in respectively at +0.4%, +0.7% and +0.5%. The latest Bank of England forecast for growth in 2016 as a whole is +2.2%. The figure for quarter 3 was a pleasant surprise which confounded the downbeat forecast by the Bank of England in August of only +0.1%, (subsequently revised up in September, but only to +0.2%). During most of 2015 and the first half of 2016, the economy had faced headwinds for exporters from the appreciation of sterling against the Euro, and weak growth in the EU, China and emerging markets, and from the dampening effect of the Government's continuing austerity programme.

The **referendum vote for Brexit** in June 2016 delivered an immediate shock fall in confidence indicators and business surveys at the beginning of August, which were interpreted by the Bank of England in its August Inflation Report as pointing to an impending sharp slowdown in the economy. However, the following monthly surveys in September showed an equally sharp recovery in confidence and business surveys so that it is generally expected that the economy will post reasonably strong growth numbers through the second half of 2016 and also in 2017, albeit at a slower pace than in the first half of 2016.

The **Monetary Policy Committee, (MPC), meeting of 4th August** was therefore dominated by countering this expected sharp slowdown and resulted in a package of measures that included a cut in Bank Rate from 0.50% to 0.25%, a renewal of quantitative easing, with £70bn made available for purchases of gilts and corporate bonds, and a £100bn tranche of cheap borrowing being made available for banks to use to lend to businesses and individuals.

The **MPC meeting of 3 November** left Bank Rate unchanged at 0.25% and other monetary policy measures also remained unchanged. This was in line with market expectations, but a major change from the previous quarterly Inflation Report MPC meeting of 4 August, which had given a strong steer, in its forward guidance, that it was likely to cut Bank Rate again, probably by the end of the year if economic data turned out as forecast by the Bank. The MPC meeting of 15 December also left Bank Rate and other measures unchanged.

The latest MPC decision included a forward view that **Bank Rate** could go either <u>up or down</u> depending on how economic data evolves in the coming months. Our central view remains that Bank Rate will remain unchanged at 0.25% until the first increase to 0.50% in quarter 2 2019 (unchanged from our previous forecast). However, we would not, as yet, discount the risk of a cut in Bank Rate if economic growth were to take a significant dip downwards, though we think this is unlikely. We would also point out that forecasting as far ahead as mid 2019 is highly fraught as there are many potential economic headwinds which could blow the UK economy one way or the other as well as political developments in the UK, (especially over the terms of Brexit), EU, US and beyond, which could have a major impact on our forecasts.

The pace of Bank Rate increases in our forecasts has been slightly increased beyond the three year time horizon to reflect higher inflation expectations.

The August quarterly Inflation Report was based on a pessimistic forecast of near to zero GDP growth in quarter 3 i.e. a sharp slowdown in growth from +0.7% in quarter 2, in reaction to the shock of the result of the referendum in June. However, **consumers** have very much stayed in a 'business as usual' mode and there has been no sharp downturn in spending; it is consumer expenditure that underpins the services sector which comprises about 75% of UK GDP. After a fairly flat three months leading up to October, retail sales in October surged at the strongest rate since September 2015 and were again strong in November. In addition, the GfK consumer confidence index recovered quite strongly to -3 in October after an initial sharp plunge in July to -12 in reaction to the referendum result. However, in November it fell to -8 indicating a return to pessimism about future prospects among consumers, probably based mainly around concerns about rising inflation eroding purchasing power.

Bank of England GDP forecasts in the November quarterly Inflation Report were as follows, (August forecasts in brackets) - 2016 +2.2%, (+2.0%); 2017 1.4%, (+0.8%); 2018 +1.5%, (+1.8%). There has, therefore, been a sharp increase in the forecast for 2017, a marginal increase in 2016 and a small decline in growth, now being delayed until 2018, as a result of the impact of Brexit.

Capital Economics' GDP forecasts are as follows: 2016 +2.0%; 2017 +1.5%; 2018 +2.5%. They feel that pessimism is still being overdone by the Bank and Brexit will not have as big an effect as initially feared by some commentators.

The Chancellor has said he will do 'whatever is needed' i.e. to **promote growth**; there are two main options he can follow – fiscal policy e.g. cut taxes, increase investment allowances for businesses, and/or increase government expenditure on infrastructure, housing etc. This will mean that the PSBR deficit elimination timetable will need to slip further into the future as promoting growth, (and ultimately boosting tax revenues in the longer term), will be a more urgent priority. The Governor of the Bank of England, Mark Carney, had warned that a vote for Brexit would be likely to cause a slowing in growth, particularly from a reduction in business investment, due to the uncertainty of whether the UK would have continuing full access, (i.e. without tariffs), to the EU single market. He also warned that the Bank could not do all the heavy lifting to boost economic growth and suggested that the Government would need to help growth e.g. by increasing investment expenditure and by using fiscal policy tools. The newly appointed Chancellor, Phillip Hammond, announced, in the aftermath of the referendum result and the formation of a new Conservative cabinet, that the target of achieving a budget surplus in 2020 would be eased in the Autumn Statement on 23 November. This was duly confirmed in the Statement which also included some increases in infrastructure spending.

The other key factor in forecasts for Bank Rate is **inflation** where the MPC aims for a target for CPI of 2.0%. The November Inflation Report included an increase in the peak forecast for inflation from 2.3% to 2.7% during 2017; (Capital Economics are forecasting a peak of just under 3% in 2018). This increase was largely due to the effect of the sharp fall in the value of sterling since the referendum, although during November, sterling has recovered some of this fall to end up 15% down against the dollar, and 8% down against the euro (as at the MPC meeting date – 15.12.16).This depreciation will feed through into a sharp increase in the cost of imports and materials used in production in the UK. However, the MPC is expected to look through the acceleration in inflation caused by external, (outside of the UK), influences, although it has given a clear warning that if wage inflation were to rise significantly as a result of these cost pressures on consumers, then they would take action to raise Bank Rate.

What is clear is that **consumer disposable income** will come under pressure, as the latest employers' survey is forecasting median pay rises for the year ahead of only 1.1% at a time when inflation will be rising significantly higher than this. The CPI figure has been on an upward trend in 2016 and reached 1.2% in November. However, prices paid by factories for inputs rose to 13.2% though producer output prices were still lagging behind at 2.3% and core inflation was 1.4%, confirming the likely future upwards path.

Gilt yields, and consequently PWLB rates, have risen sharply since hitting a low point in mid-August. There has also been huge volatility during 2016 as a whole. The year started with 10 year gilt yields at 1.88%, fell to a low point of 0.53% on 12 August, and hit a new peak on the way up again of 1.55% on 15 November. The rebound since August reflects the initial combination of the yield-depressing effect of the MPC's new round of quantitative easing on 4 August, together with expectations of a sharp downturn in expectations for growth and inflation as per the pessimistic Bank of England Inflation Report forecast, followed by a sharp rise in growth expectations since August when subsequent business surveys, and GDP growth in quarter 3 at +0.5% q/q, confounded the pessimism. Inflation expectations also rose sharply as a result of the continuing fall in the value of sterling.

Employment had been growing steadily during 2016 but encountered a first fall in over a year, of 6,000, over the three months to October.The latest employment data in December, (for November), was distinctly weak with an increase in unemployment benefits claimants of 2,400 in November and of 13,300 in October. **House prices** have been rising during 2016 at a modest pace but the pace of increase has slowed since the referendum; a downturn in prices could dampen consumer confidence and expenditure.

USA. The American economy had a patchy 2015 with sharp swings in the quarterly **growth rate** leaving the overall growth for the year at 2.4%. Quarter 1 of 2016 at +0.8%, (on an annualised basis), and quarter 2 at 1.4% left average growth for the first half at a weak 1.1%. However, quarter 3 at 3.2% signalled a rebound to strong growth. The Fed. embarked on its long anticipated first increase in rates at its December 2015 meeting. At that point, confidence was high that there would then be four more increases to come in 2016. Since then, more downbeat news on the international scene, and then the Brexit vote, have caused a delay in the timing of the second increase of 0.25% which came, as expected, in December 2016 to a range of 0.50% to 0.75%. Overall, despite some data setbacks, the US is still, probably, the best positioned of the major world economies to make solid progress towards a combination of strong growth, full employment and rising inflation: this is going to require the central bank to take action to raise rates so as to make progress towards normalisation of monetary policy, albeit at lower central rates than prevailed before the 2008 crisis. The Fed. therefore also indicated that it expected three further increases of 0.25% in 2017 to deal with rising inflationary pressures.

The result of the **presidential election** in November is expected to lead to a strengthening of US growth if Trump's election promise of a major increase in expenditure on infrastructure is implemented. This policy is also likely to strengthen inflation pressures as the economy is already working at near full capacity. In addition, the unemployment rate is at a low point verging on what is normally classified as being full employment. However, the US does have a substantial amount of hidden unemployment in terms of an unusually large, (for a developed economy), percentage of the working population not actively seeking employment.

Trump's election has had a profound effect on the **bond market and bond yields** rose sharply in the week after his election. Time will tell if this is a a reasonable assessment of his election promises to cut taxes at the same time as boosting expenditure. This could lead to a sharp rise in total debt issuance from the current level of around 72% of GDP towards 100% during his term in office. However, although the Republicans now have a monopoly of power for the first time since the 1920s, in having a President and a majority in both Congress and the Senate, there is by no means any certainty that the politicians and advisers he has been appointing to his team, and both houses, will implement the more extreme policies that Trump outlined during his election campaign. Indeed, Trump may even rein back on some of those policies himself.

In the first week since the US election, there was a a major shift in **investor sentiment** away from bonds to equities, especially in the US. However, gilt yields in the UK and bond yields in the EU have also been dragged higher. Some commentators are saying that this rise has been an overreaction to the US election result which could be reversed. Other commentators take the view that this could well be the start of the long expected eventual unwinding of bond prices propelled upwards to unrealistically high levels, (and conversely bond yields pushed down), by the artificial and temporary power of quantitative easing.

EZ. In the Eurozone, **the ECB** commenced, in March 2015, its massive €1.1 trillion programme of quantitative easing to buy high credit quality government and other debt of selected EZ countries at a rate of €60bn per month. This was intended to run initially to September 2016 but was extended to March 2017 at its December 2015 meeting. At its December and March 2016 meetings it progressively cut its deposit facility rate to reach -

0.4% and its main refinancing rate from 0.05% to zero. At its March meeting, it also increased its monthly asset purchases to €80bn. These measures have struggled to make a significant impact in boosting economic growth and in helping inflation to rise significantly from low levels towards the target of 2%. Consequently, at its December meeting it extended its asset purchases programme by continuing purchases at the current monthly pace of €80 billion until the end of March 2017, but then continuing at a pace of €60 billion until the end of December 2017, or beyond, if necessary, and in any case until the Governing Council sees a sustained adjustment in the path of inflation consistent with its inflation aim. It also stated that if, in the meantime, the outlook were to become less favourable or if financial conditions became inconsistent with further progress towards a sustained adjustment of the path of inflation, the Governing Council intended to increase the programme in terms of size and/or duration.

EZ GDP growth in the first three quarters of 2016 has been 0.5%, +0.3% and +0.3%, (+1.7% y/y). Forward indications are that economic growth in the EU is likely to continue at moderate levels. This has added to comments from many forecasters that those central banks in countries around the world which are currently struggling to combat low growth, are running out of ammunition to stimulate growth and to boost inflation. Central banks have also been stressing that national governments will need to do more by way of structural reforms, fiscal measures and direct investment expenditure to support demand and economic growth in their economies.

There are also significant specific political and other risks within the EZ: -

- **Greece** continues to cause major stress in the EU due to its tardiness and reluctance in implementing key reforms required by the EU to make the country more efficient and to make significant progress towards the country being able to pay its way – and before the EU is prepared to agree to release further bail out funds.
- **Spain** has had two inconclusive general elections in 2015 and 2016, both of which failed to produce a workable government with a majority of the 350 seats. At the eleventh hour on 31 October, before it would have become compulsory to call a third general election, the party with the biggest bloc of seats (137), was given a majority confidence vote to form a government. This is potentially a highly unstable situation, particularly given the need to deal with an EU demand for implementation of a package of austerity cuts which will be highly unpopular.
- The under capitalisation of **Italian banks** poses a major risk. Some **German banks** are also undercapitalised, especially Deutsche Bank, which is under threat of major financial penalties from regulatory authorities that will further weaken its capitalisation. What is clear is that national governments are forbidden by EU rules from providing state aid to bail out those banks that are at risk, while, at the same time, those banks are unable realistically to borrow additional capital in financial markets due to their vulnerable financial state. However, they are also 'too big, and too important to their national economies, to be allowed to fail'.
- **4 December Italian constitutional referendum** on reforming the Senate and reducing its powers; this was also a confidence vote on Prime Minister Renzi who has resigned on losing the referendum. However, there has been remarkably little fall out from this result which probably indicates that the financial markets had already fully priced it in. A rejection of these proposals is likely to inhibit significant progress in the near future to fundamental political and economic

reform which is urgently needed to deal with Italy's core problems, especially low growth and a very high debt to GDP ratio of 135%. These reforms were also intended to give Italy more stable government as no western European country has had such a multiplicity of governments since the Second World War as Italy, due to the equal split of power between the two chambers of the Parliament which are both voted in by the Italian electorate but by using different voting systems. It is currently unclear what the political, and other, repercussions are from this result.

- **Dutch general election 15.3.17**; a far right party is currently polling neck and neck with the incumbent ruling party. In addition, anti-big business and anti-EU activists have already collected two thirds of the 300,000 signatures required to force a referendum to be taken on approving the EU – Canada free trade pact. This could delay the pact until a referendum in 2018 which would require unanimous approval by all EU governments before it can be finalised. In April 2016, Dutch voters rejected by 61.1% an EU – Ukraine cooperation pact under the same referendum law. Dutch activists are concerned by the lack of democracy in the institutions of the EU.
- **French presidential election;** first round 13 April; second round 7 May 2017.
- **French National Assembly election June 2017.**
- **German Federal election August – 22 October 2017.** This could be affected by significant shifts in voter intentions as a result of terrorist attacks, dealing with a huge influx of immigrants and a rise in anti EU sentiment.
- The core EU, (note, not just the Eurozone currency area), principle of **free movement of people** within the EU is a growing issue leading to major stress and tension between EU states, especially with the Visegrad bloc of former communist states.

Given the number and type of challenges the EU faces in the next eighteen months, there is an identifiable risk for the EU project to be called into fundamental question. The risk of an electoral revolt against the EU establishment has gained traction after the shock results of the UK referendum and the US Presidential election. But it remains to be seen whether any shift in sentiment will gain sufficient traction to produce any further shocks within the EU.

<u>Asia.</u> Economic growth in **China** has been slowing down and this, in turn, has been denting economic growth in emerging market countries dependent on exporting raw materials to China. Medium term risks have been increasing in China e.g. a dangerous build up in the level of credit compared to the size of GDP, plus there is a need to address a major over supply of housing and surplus industrial capacity, which both need to be eliminated. This needs to be combined with a rebalancing of the economy from investment expenditure to consumer spending. However, the central bank has a track record of supporting growth through various monetary policy measures, though these further stimulate the growth of credit risks and so increase the existing major imbalances within the economy.

Economic growth in **Japan** is still patchy, at best, and skirting with deflation, despite successive rounds of huge monetary stimulus and massive fiscal action to promote consumer spending. The government is also making little progress on fundamental reforms of the economy.

Emerging countries. There have been major concerns around the vulnerability of some emerging countries exposed to the downturn in demand for commodities from China or to competition from the increase in supply of American shale oil and gas reaching world markets. The ending of sanctions on Iran has also brought a further significant increase in oil supplies into the world markets. While these concerns have subsided during 2016, if interest rates in the USA do rise substantially over the next few years, (and this could also be accompanied by a rise in the value of the dollar in exchange markets), this could cause significant problems for those emerging countries with large amounts of debt denominated in dollars. The Bank of International Settlements has recently released a report that $340bn of emerging market corporate debt will fall due for repayment in the final two months of 2016 and in 2017 – a 40% increase on the figure for the last three years.

Financial markets could also be vulnerable to risks from those emerging countries with major sovereign wealth funds, that are highly exposed to the falls in commodity prices from the levels prevailing before 2015, especially oil, and which, therefore, may have to liquidate substantial amounts of investments in order to cover national budget deficits over the next few years if the price of oil does not return to pre-2015 levels.

Brexit timetable and process

- March 2017: UK government notifies the European Council of its intention to leave under the Treaty on European Union Article 50
- March 2019: two-year negotiation period on the terms of exit. This period can be extended with the agreement of all members i.e. not that likely.
- UK continues as an EU member during this two-year period with access to the single market and tariff free trade between the EU and UK.
- The UK and EU would attempt to negotiate, among other agreements, a bi-lateral trade agreement over that period.
- The UK would aim for a negotiated agreed withdrawal from the EU, although the UK may also exit without any such agreements.
- If the UK exits without an agreed deal with the EU, World Trade Organisation rules and tariffs could apply to trade between the UK and EU - but this is not certain.
- On exit from the EU: the UK parliament would repeal the 1972 European Communities Act.
- The UK will then no longer participate in matters reserved for EU members, such as changes to the EU's budget, voting allocations and policies.
- It is possible that some sort of agreement could be reached for a transitional time period for actually implementing Brexit after March 2019 so as to help exporters to adjust in both the EU and in the UK.

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ANNEX D

Credit and Counterparty Risk Management

Permitted Investments, Associated Controls and Limits for East Renfrewshire Council and East Renfrewshire Culture & Leisure Trust

Type of Investment	Treasury Risks	Mitigating Controls	Limits
a. Deposits with the Debt Management Account Facility (UK Government) (**Very low risk**)	This is a deposit with the UK Government and, as such, counterparty and liquidity risk is very low, and there is no risk to value. Deposits can be between overnight and 6 months	Little mitigating controls required. As this is a UK Government investment, the monetary limit is £5,000,000	£5m, maximum 6 months.
b. Deposits with other local authorities or public bodies (**Very low risk**)	These are considered quasi UK Government debt and, as such counterparty risk is very low, and there is no risk to value. Liquidity may present a problem as deposits can only be broken with the agreement of the counterparty, and penalties can apply.	Little mitigating controls required for local authority deposits, as this is a quasi UK Government investment.	£5m (per body), maximum 6 months
c. Money Market Funds (MMFs) (**Very low risk**)	Pooled cash investment vehicle which provides very low counterparty, liquidity and market risk. These will primarily be used as liquidity instruments.	Funds will only be used where the MMFs use Constant Net Asset Value (CNVA) and the fund has a “AAA” rated status from either Fitch, Moody’s or Standard & Poors.	£5m per fund/£30m overall
d. Enhanced Cash Funds (ECFs) **(Low risk)**	Pooled cash investment vehicle which provides very low counterparty, liquidity and market risk. These will primarily be used as liquidity instruments.	Funds will only be used where the ECFs have a “AAA” rated status from either Fitch, Moody’s or Standard and Poor’s.	£5m per fund/£30m overall, as part of category c.
e. Call account deposit accounts with financial institutions (banks and building societies)	These tend to be low risk investments, but will exhibit higher risks than categories (a), (b) and (c) above. These type of investments have no risk to value, liquidity is high and investment can be returned at short notice	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody’s and Standard and Poor’s. The selection defaults to the lowest available	As shown in the counterparty listing (Annex E)

(**Low risk depending on credit rating**)		colour band / credit rating to provide additional risk control measures. Day to day investment dealing with the criteria will be further strengthened by use of additional market intelligence.	
f. Term deposits with financial institutions (banks and building societies) (**Low to medium risk depending on period & credit rating**)	These tend to be low risk investments, but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types of investments, liquidity is low and term deposits can only be broken with the agreement of the counterparty, and penalties may apply.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poors. The selection defaults to the lowest available credit rating to provide additional risk control measures. Day to day investment dealing with this criteria will be further strengthened by the use of additional market intelligence.	As shown in the counterparty listing (Annex E)
g. UK Government Gilts and Treasury Bills **(Very low risk)**	These are marketable securities issued by the UK Government and, as such, counterparty and liquidity risk is very low, although there is potential risk to value arising from an adverse movement in interest rates (no loss if these are held to maturity).	Little counterparty mitigating controls are required, as this is a UK Government investment. The potential for capital loss will be reduced by limiting the maximum monetary and time exposures.	£5m, maximum 6 months
h. Certificates of Deposit with Financial Institutions (Banks & Building Societies) **(Low risk)**	These are short dated marketable securities issued by financial institutions and as such counterparty risk is low, but will exhibit higher risks than categories (a), (b) and (c) above. There is risk to value of capital loss arising from selling ahead of maturity if combined with an adverse movement in interest rates (no loss if these are held to maturity). Liquidity risk will normally	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. Day to day investment dealing with this criteria will be further strengthened by the use of additional market intelligence.	Dependent on institution as listed in counterparty listing in annex E

	be low.		
i. Structured deposit facilities with banks and building societies (escalating rates, de-escalating rates etc) **(Low to medium risk depending on period & credit rating)**	These tend to be medium to low risk investments, but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types of investments, liquidity is very low and investments can only be broken with the agreement of the counterparty (penalties may apply)	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. Day to day investment dealing with this criteria will be further strengthened by the use of additional market intelligence	As shown in the counterparty listing (Annex E)
j. Corporate Bonds **(Medium to high risk depending on period and credit rating)**	These are marketable securities issued by financial and corporate institutions. Counterparty risk will vary and there is risk to value of capital loss arising from selling ahead of maturity if combined with an adverse movement in interest rates. Liquidity risk will be low.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. Fixed bonds will be restricted to those meeting the base criteria. Day to day investment dealing with this criteria will be further strengthened by the use of additional market intelligence.	Dependent on institution as listed in counterparty listing in annex E
k. Floating Rate Note **(Medium to high risk depending on period and credit rating)**	This is a money market instrument with a floating /variable rate of interest, which re-fixes over a reference rate , for example LIBOR.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. . The Floating Rate Note will be restricted to those meeting the base criteria. Day to day investment dealing with this criteria will be further strengthened by the use of additional market intelligence.	Dependent on institution as listed in counterparty listing in annex E

l. Investment properties (**Medium Risk)**	These are non-service properties which are being held pending disposal or for a longer-term rental income stream. These are highly illiquid assets with high risk to value (the potential for property prices to fall or for rental voids)	In larger investment portfolios, some small allocation of property based investment may counterbalance/compliment the wider cash portfolio.	No limit
m. Loans to third parties, including soft loans (**Low to Medium Risk depending on Credit Risk**)	These are service investments either at market rates of interest or below market rates (soft loans). These types of investments may exhibit credit risk and are likely to be highly illiquid.	Each third party loan requires Member approval and each application is supported by the service rationale behind the loan and the likelihood of partial or full default.	£0.5m
n. Loans to a local authority company/ partnership or charity (**Low Risk)**	These are service investments either at market rates of interest or below market rates (soft loans). These types of investments may exhibit credit risk and are likely to be highly illiquid	Each loan to a local authority company/LLP requires Member approval and each application is supported by the service rationale/business case behind the loan and the likelihood of partial or full default. In general these loans will involve some form of security or clear cash flow that is available to service the debt.	£1m
o. Shares in Hub Schemes (**Very Low Risk**)	These are investments that are exposed to the success or failure of individual projects and are highly illiquid.	The Council and Scottish Government (via the SFT) are participants in and party to the governance and controls within the project structure. As such they are well placed to influence and ensure the successful completion of the project's term. These projects are based on robust business cases with a cash flow from public sector organisations (i.e. low credit risk)	Investment limited to HUB schemes where the Council is a major participant

The Monitoring of Investment Counterparties

The status of counterparties will be monitored regularly. The Council receives credit rating and market information from Capita Asset Services, including when ratings change, and counterparties are checked promptly. On occasion rating may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria will be removed from the list immediately (with the exception of the Council's Bank) and if required new counterparties which meet the criteria will be added to the list with written permission of the Chief Financial Officer.

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Annex E **EAST RENFREWSHIRE COUNCIL**

ORGANISATIONS APPROVED FOR THE INVESTMENT OF SURPLUS FUNDS

		Limits	
Banking Group	**Individual Counterparty**	**Deposit**	**Transaction**
Bank of England	Debt Management Office	£5m	£5m
	UK Treasury Bills	£5m	£5m
Goldman Sachs International Bank		£5m	£5m
Lloyds Banking Group:	Bank of Scotland	£10m	£10m
Royal Bank of Scotland Group:	Royal Bank of Scotland	£5m	£5m
Barclays Banking Group	Barclays Bank	£5m	£5m
Standard Chartered Bank		£5m	£5m
Santander Group	Santander UK PLC	£5m	£5m
Clydesdale Bank		£0	£0
Building Societies			
Nationwide		£5m	£5m
Local Authorities			
All Local Authorities including Police & Fire		£5m	£5m
Money Market Funds and Enhanced Cash Funds			
Maximum limit of £5m per fund		£30m	£5m

Credit Ratings

	Fitch		Moodys		S&P	
	LT	ST	LT	ST	LT	ST
Minimum Criteria	A-	F1	A3	P-1/P-2	A	A-1/A-2

(Unless Government backed)

(please note credit ratings are not the sole method of selecting counterparty)

Limit

Investment of surplus funds is permitted in each of the above organisations, with the limits set on an individual basis by the Chief Financial Officer.

The limit may only be exceeded or another organisation approved with the written permission of the Chief Financial Officer.

Deposit Periods

The maximum period for any deposit is currently set at 6 months with the exception of the Bank of Scotland which is set at 364 days. These limits can only be exceeded with the written permission of the Chief Financial Officer.

Hub scheme deposit periods are dependent on the lifetime of the associated scheme.

GLOSSARY OF TERMS

CIPFA	Chartered Institute of Public Finance and Accountancy
CIPFA Code	Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes
CFR	Capital Financing Requirement is the estimated level of borrowing or financing needed to fund capital expenditure.
Consent to Borrow	Para 1 (1) of Schedule 3 of the Local Government (Scotland) Act 1975 (the 1975 Act) effectively restricts local authorities to borrowing only for capital expenditure. Under the legislation Scottish Ministers may provide consent for local authorities to borrow for expenditure not covered by this paragraph, where they are satisfied that the expenditure should be met by borrowing.
Gilts	A gilt is a UK Government liability in sterling, issued by HM Treasury and listed on the London Stock Exchange. The term “gilt” or “gilt-edged security” is a reference to the primary characteristic of gilts as an investment: their security. This is a reflection of the fact that the British Government has never failed to make interest or principal payments on gilts as they fall due.
LIBID	London Interbank Bid Rate The rate at which banks bid on Eurocurrency Deposits, being the rate at which a bank is willing to borrow from other banks.
MPC	Monetary Policy Committee
NHT	National Housing Trust initiative undertaken in partnership with the Scottish Futures Trust.
Other Long Term Liabilities	Balance sheet items such as Public Private Partnership (PPP), and leasing arrangements which already include borrowing instruments.
PPP	Public-Private Partnership.
Prudential Indicators	The Prudential Code sets out a basket of indicators (the Prudential Indicators) that must be prepared and used in order to demonstrate that local authorities have fulfilled the objectives of the Prudential Code.
QE	Quantitative Easing
Treasury Indicators	These consist of a number of Treasury Management Indicators that local authorities are expected to ‘have regard’ to, to demonstrate compliance with the Treasury Management Code of Practice.

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