APPENDIX 1

FOREST HEATH DISTRICT COUNCIL

ANNUAL TREASURY MANAGEMENT AND INVESTMENT STRATEGY STATEMENTS 2015/2016

To be approved at Council on 27 February 2015

COU/FH/15/003

ANNUAL TREASURY MANAGEMENT AND INVESTMENT STRATEGY STATEMENTS 2015/2016

TREASURY MANAGEMENT POLICY STATEMENT

1. The Council defines its treasury management activities as:

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

2. The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council, and any financial instruments entered into to manage these risks.

3. The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

4. The Council's policies for borrowing and investments are detailed in the Treasury Management Annual Investment Strategy below.

ANNUAL INVESTMENT STRATEGY 2015/16

Introduction

5. Guidance from the Department for Communities and Local Government (CLG) on Local Government Investments in England requires that an Annual Investment Strategy be set by the Council.

6. The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management also sets out various requirements for the Council to meet. The primary requirements of the Code are as follows:

   - Receipt by the full Council of Treasury Management Statements and Reports - including the Annual Treasury Management Investment Strategy Statement & Policy Statement, Minimum Revenue Provision Policy, a Mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.
   - Creation and maintenance of Treasury Management Practices (Code of Practice) which set out the manner in which the Council will seek to achieve those policies and objectives.
   - Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
   - Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body.

7. The Council's general policy objective is to invest surplus funds prudently. The Council's investment priorities are; security and liquidity of the capital at an optimum yield which is commensurate with security and liquidity.

Risk Management

8. The Council regards the successful identification, monitoring and control of risk to be prime criteria by which the effectiveness of its Treasury Management activities will be measured. The main risks to the Council's treasury activities are:

   - Credit and Counterparty Risk – Security of the Council's Investments.
   - Market or Interest Rate Risk – Fluctuations in interest rate levels and thereby in the value of investments.
   - Liquidity Risk – Inadequate cash resources.
   - Inflation Risk – Exposure to inflation.
   - Legal and Regulatory Risk – Non compliance with Statutory and Regulatory requirements and the risk of fraud.

9. The above risks have been taken into account when setting the proposed Annual Treasury Management and Investment Strategy Statements. The risk that remains the Council's primary focus is that around the credit and counterparty risk and potential loss of its investments in a similar way to that following the Icelandic Banks collapse. The controls that the Strategy require are:

   - credit worthiness checks of counterparties through the 3 main credit rating agencies; or
   - Asset Value checks assisting the Council to manage this risk.

10. Officers also have access, through the Council's external fund managers to real time market advice and expertise.

11. Further risk centres on the loss of interest receipts through decreased interest rates which has a direct impact on the Medium Term Financial Strategy (MTFS). Should the market move in an adverse direction, the actual receipts will be lower than forecast budgets and therefore have a detrimental effect on this significant revenue income stream to the MTFS. In the current climate this is a high risk for the Council but beyond its control. The position will be monitored and actual interest receipts against forecast will be reported through Joint Leadership Team and Performance, Audit and Scrutiny Committee, the outcome of which may require the Council to revise its MTFS accordingly.

12. Given the current volatility in financial markets and the performance of institutions, it is probable that status changes may occur during the next 12 months. Accordingly it may be necessary for Officers to update Members verbally as to the impact of these changes and, if appropriate, on alternative courses of action which may have to be considered in order for the Council to have worthwhile investment opportunities during the year.

Scheme of delegation and the role of the Section 151 officer

13. The Section 151 Officer, or Deputy Section 151 Officer, has delegated responsibility under the Treasury Management Code of Practice for the execution and administration of treasury management decisions.

14. The Section 151 Officer or Deputy Section 151 Officer may delegate their treasury management responsibilities to members of their staff. The full scheme of delegation can be found in the Council's Treasury Management Code of Practice (in the section TMP5 – Organisation, Clarity and Segregation of Responsibilities, and Dealing Arrangements).

15. Staff that have responsibility for the treasury function are required to have sufficient knowledge and expertise in treasury management to be able to understand and critically consider the advice provided by the Council's treasury consultants.

16. The training needs of staff are considered on a regular basis as part of the Council's appraisal process. The Section 151 Officer or Deputy Section 151 Officer will ensure that treasury management staff receive appropriate training and have the necessary skills to be able to undertake their duties effectively.

Use of External Brokers/Advisors/Fund Managers

17. The Council will ensure, through regular meetings and discussions with their fund managers, brokers and/or advisors, that the service is tailored to the Council's needs and strategic aims, and that they appreciate the Council's position on the balance between risk and reward in its treasury activities. The Council has regard to all the advice and information provided by the external support, but responsibility for treasury decisions remains with the Council.

Creditworthiness Policy & Lending Criteria

18. The Council needs to set investment criteria for both internally and externally managed funds, based on who is an appropriate institution to hold the Council deposits. Ideally any counterparty policy should spread investments over the maximum number of counterparties, who vary in type i.e. building societies or banks. However, the key concern of the counterparty policy is to manage risk in a practical way rather than stick to a theoretical ideal. Usually those organisations or types of investments with the lower risk (best credit worthiness) are those that pay the lowest returns, those with lower credit worthiness have to pay the higher returns to attract investors. Therefore the Council must strike a balance of risk and return.

19. There are numerous ways of measuring credit worthiness, the most widely adopted are reliant on private credit rating companies, who score the worthiness of some banks and financial institutions. The companies most commonly used are Fitch, Moody's and Standard & Poor's.

20. Officers recommend the approach to use credit ratings from these 3 credit agencies and the Building Society £1bn Assets List to determine counterparty strength. The Council's counterparty policy's fundamental principle is to limit investments to UK institutions of good credit worth and where most importantly government support can be expected.

21. The Council is required to categorise the types of investments/institutions that it is delegating to officers to use. The Council will maintain a counterparty list in compliance with the following criteria:

- For short term investments (less than 1 year) – Credit rating as follows:
  - Fitch Rating – F1+, F1 of F2
  - Moody's Rating – P1 or P2
  - Standard & Poor's Rating – AAA, AA or A

Building Societies	£1bn assets or more (consideration will also be given to their credit rating, if one is available, in line with the criteria above)

  All 3 credit rating agency scores will be reviewed. Appendix 2 provides the Credit Agencies definitions.

- For long term investments (1 year or more) – Credit rating as follows:
  - Fitch Rating – AAA to BBB*
  - Moody's Rating – Aaa to Baa2*
  - Standard & Poor's Rating – AAA to BBB*

  *The Head of Resources and Performance will consult with the Portfolio Holder for Resources, Performance and Governance before an investment is made with a BBB+ or a BBB rated institution.

Building Societies	£1bn assets or more (consideration will also be given to their credit rating, if one is available, in line with the criteria above)

  All 3 credit rating agency scores will be reviewed.

- Credit worthiness check of £1bn of Assets for all Building Societies; using the Building Societies Association guide which lists the assets of UK Building Societies, ranked by group assets, taken from their latest annual reports.

- Period of Investments to be limited to 5 years maximum.

- The use of UK institutions only for internally managed funds.

- Maximum investment limit per institution of £8M (£10M Lloyds/Bank of Scotland, which is heavily government owned and the Council bank), or £6M if it is a Building Society that falls below the Top 10 listed on the Building Societies Association guide but still holds the required £1bn in assets. The limit per institution is broken down between internally managed and externally managed funds as set out in the following table:

Institution	Credit Rating Short Term (Fitch Moody's S&P)	Credit Rating Long Term (Fitch Moody's S&P)	CDCM Maximum Investment	Internally Managed Maximum Investment	Aggregated Maximum Investment per Institution
			£M	£M	£M
UK Clearing Banks (Lloyds/Bank of Scotland)	F1+, F1 or F2 P1 or P2 AAA, AA, or A	AAA to BBB* Aaa to Baa2* AAA to BBB*	6 (7)	2 (3)	8 (10)
UK Building Societies (The Top 10 & £1bn Assets)	F1+, F1 or F2 P1 or P2 AAA, AA, or A	AAA to BBB* Aaa to Baa2* AAA to BBB*	4	2	6
UK Building Societies (from Top 11 downwards & £1bn Assets)	F1+, F1 or F2 P1 or P2 AAA, AA, or A	AAA to BBB* Aaa to Baa2* AAA to BBB*	4	1	5
UK Clearing Bank Subsidiaries	F1+, F1 or F2 P1 or P2 AAA, AA, or A	AAA to BBB* Aaa to Baa2* AAA to BBB*	4	2	6
Other UK Banks (with links to overseas banks)	F1+, F1 or F2 P1 or P2 AAA, AA, or A	AAA to BBB* Aaa to Baa2* AAA to BBB*	4	1	5
Overseas Banks	F1+, F1 or F2 P1 or P2 AAA, AA, or A	AAA to BBB* Aaa to Baa2* AAA to BBB*	3	0	3
Local Authorities	N/A	N/A	7	3	10
Debt Management Office	N/A	N/A	Unlimited	Unlimited	Unlimited

* The Head of Resources and Performance will consult with the Portfolio Holder for Resources, Performance and Governance before an investment is made with a BBB+ or a BBB rated institution.

- Where banks or building societies are part of a merged group structure (jointly owned) the limits apply to the group as a whole not separately to individual banks.

- With regard to the Council's internally managed call accounts, interest receipts will not be included when considering investment limits. This is due to interest receipts being paid into the call accounts directly. Therefore until a withdrawal can be made the balance within the account may temporarily exceed the limits stated above.

22. It is proposed that the Council's current externally managed portfolio with CDCM is to continue to be invested for periods of up to 5 years, in line with the Council's overall cash flow requirements. In this way it is anticipated that a profile of maturing investments will protect the Council against the impact of low interest rates while, at the same time, allowing it to take advantage of positive changes in investment returns. Internally managed funds will continue to be placed over relatively short periods, thus ensuring that there are sufficient resources to meet all the Council's expenditure commitments throughout the year.

23. In looking for security and a return on smaller investments the Council will continue to use deposit /call accounts with major banks and building societies on its approved counterparty list. In parallel with this option, and to deal with any further uncertainties in the financial markets, it is proposed that, should the need arise the Council will place investments with the Debt Management Office through the Debt Management Agency Deposit Facility or with Local Authorities direct. Whilst the rates of interest earned are below market rates the Council's capital investments will be protected.

24. In line with the recommendations in previous strategies, the Council's investment portfolio combines a mix of banks and building societies.

Investment Security - Specified and Unspecified Investments

25. The Secretary of State requires that the Council identifies institutions which will be used for specified and unspecified investments.

26. The definitions of specified and unspecified investments are shown below:

- An investment is a *specified investment* if all of the following apply:

  (a) the investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling;
  (b) the investment is not a long-term investment (1 year or more)
  (c) the making of the investment is not defined as capital expenditure by virtue of regulation 25(1)(d) of the Local Authorities (Capital Finance and Accounting)(England) Regulations 2003 [SI 3146 as amended];
  (d) the investment is made with a body or in an investment scheme of high credit quality (see below); or with one of the following public sector bodies:
     i. the UK Government
     ii. a local authority in England & Wales (as defined in section 23 of the 2003 Act) or similar body in Scotland or Northern Ireland
     iii. a parish or community council.

  An institution is deemed to have a high credit quality if it holds a short term credit rating of at least one of the following:

Fitch	F2 or better
Standard & Poor's	A or better
Moody's	P2 or better
Building Societies	£1bn assets or more (consideration will also be given to their credit rating, if one is available, in line with the criteria above)

- An *unspecified investment* is any other investment that does not meet the definition of a specified investment. Basically these are investments with maturity dates greater than 1 year, or where no credit ratings have been awarded to the organisations concerned.
  The Council will not make unspecified investments unless the institution holds a long term credit rating of at least one of the following:

Fitch	BBB or better*
Standard & Poor's	Baa2 or better*
Moody's	BBB or better*

*The Head of Resources and Performance will consult with the Portfolio Holder for Resources, Performance and Governance before an investment is made with a BBB+ or a BBB rated institution.

Building Societies	£1bn assets or more (consideration will also be given to their credit rating, if one is available, in line with the criteria above)

Investment Liquidity - Longer Term Investments

27. The following longer term investment restrictions will apply:-

- No more than £20M (nominal) can be invested for periods of 1 year or longer.
- No investments can be made for periods longer than 5 years.
- The total value of funds controlled by any individual advisor/fund manager to the Council shall not exceed £30M (nominal).

On any day:

- No more than £15M (nominal) in total shall be held in investments where the remaining term up to the date of maturity is at least 4 years but not exceeding 5 years.
- No more than £20M (nominal) in total shall be held in investments where the remaining term up to the date of maturity exceeds 1 year.
- No more than 60% of the total value of investments held will be subject to a variable rate of return.

Borrowing/External Debt

28. The option of short or long term borrowing is available to the Council. However the Council must have regard to the Prudential Code when setting borrowing limits and must ensure that any borrowing is sustainable and affordable.

29. The Council's external debt as at 31 December 2014 was as follows:-

	£
Public Works Loan Board	0
Mortgages	0
Bonds	0
Temporary Loans	2,550
Long Term Loans	4,000,000

Council's Banker

30. Following a recent Tender process, from 1 April 2014 the Council's bank will be Lloyds Bank Plc. On adoption of this strategy, the bank meets the credit criteria of F2 or above for short term investments. It is the Council's intention to use deposit and / or call accounts provided by Lloyds for short term liquidity requirements (e.g. overnight and weekend investments) and business continuity arrangements.

Balanced Budget Requirement

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

Future Interest Rates

32. The Bank of England continues to hold the Official Base rate at 0.5%. It has remained at this rate since 5 March 2009.

33. Given the current economic situation it is difficult to forecast when the base rate will increase. The Council will work with its external fund managers to ensure that it maximises all of its returns on investments in line with the latest information available.

34. The average investment interest rates which are expected to apply to the Council's investments have been determined in consultation with the external fund managers and have been included in the MTFS interest projections are as follows:

- 2015/16 – 1.70%
- 2016/17 – 1.90%
- 2017/18 – 2.25%
- 2018/19 – 2.50%

35. Although the governments 'funding for lending' scheme has started to be scaled down, cheap funding for banks and building societies continues to be available. The effects of which are still having a major affect the rates of return, especially regarding longer term investments. Consequently the Council's interest projections have reduced.

Total Investments

36. Please see the following table for full details of the investments held by the Council as at 31 December 2014.

Counterparty Name	Value £	Interest Rate %	Date Loaned	Date of Return
BANK OF SCOTLAND ACCOUNT				
Bank of Scotland Corporate Account	221	0.400	01-Jul-13	31-Dec-14
NATWEST ACCOUNT				
NatWest Liquidity Select Account	5,052	0.250	12-Nov-14	31-Dec-14
BARCLAYS ACCOUNT				
Barclays FIBCA Account	1,996,835	0.450	12-Nov-14	31-Dec-14
TEMPORARY INVESTMENTS				
Coventry Building Society	1,500,000	0.450	03-Nov-14	19-Jan-15
Nottingham Building Society	1,200,000	0.580	01-Dec-14	23-Mar-15
Nottingham Building Society	800,000	0.450	22-Dec-14	23-Feb-15
Nationwide Building Society	1,300,000	0.480	23-Dec-14	09-Mar-15
Lloyds 95 day Account	1,500,000	0.650	19-Apr-13	31-Dec-14

Counterparty Name	Value £	Interest Rate %	Date Loaned	Date of Return
CDCM MANAGED INVESTMENTS				
Barclays Capital	3,000,000	3.500	04-Nov-11	16-Mar-15
Lloyds TSB Bank Plc	2,000,000	3.650	17-May-12	15-May-17
Nottingham Building Society	1,500,000	3.150	08-Oct-12	08-Oct-15
Close Bros	3,000,000	1.420	08-Jul-13	08-Jan-15
Progressive Building Society	2,500,000	0.960	08-Jan-14	09-Feb-15
Principality Building Society	1,500,000	1.200	10-Feb-14	10-Aug-15
Principality Building Society	1,000,000	1.150	14-Mar-14	10-Aug-15
Rothschild	3,000,000	2.450	11-Jun-14	09-Jun-17
Clydesdale Bank	3,000,000	0.800	01-Aug-14	01-May-15
TOTAL VALUE OF INVESTMENTS HELD	**28,802,108**			

Capital Finance

37. The financing of the Council's capital programme is considered by Cabinet and is ratified by Council. External financing is required to be inline with the Councils approved Treasury Management and Investment Strategy and approved Prudential Indicators.

Treasury Management Code of Practice

38. The Treasury Management Code of Practice is the subject of a separate report approved by Council. The Code of Practice underpins the Strategy and provides further details regarding the operational requirements and processes regarding treasury management

Prudential Indicators

39. The Council's overall Treasury Management Strategy and Code of Practice links into the Council's Prudential Indicators and Minimum Revenue Provision Policy which are subject to separate reports to Council. A summary of the treasury related indicators is as follows:

	2014/15	2015/16	2016/17	2017/18
TREASURY MANAGEMENT PRUDENTIAL INDICATORS	**£**	**£**	**£**	**£**
	Approved	**Estimate**	**Estimate**	**Estimate**
Authorised limit for external debt -				
Borrowing	£6,670,000	£6,670,000	£6,670,000	£6,670,000
Other long term liabilities	£0	£0	£0	£0
TOTAL	£6,670,000	£6,670,000	£6,670,000	£6,670,000
Operational boundary for external debt -				
Borrowing	£6,003,000	£6,003,000	£6,003,000	£6,003,000
Other long term liabilities	£0	£0	£0	£0
TOTAL	£6,003,000	£6,003,000	£6,003,000	£6,003,000

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	2014/15	2015/16	2016/17	2017/18
TREASURY MANAGEMENT PRUDENTIAL INDICATORS	**£**	**£**	**£**	**£**
	Approved	**Estimate**	**Estimate**	**Estimate**
Maturity Structure of Borrowing				
Upper Limit for % of borrowing maturing in:				
• Under 12 Months	33%	33%	33%	33%
• 1 - 2 years	0%	0%	0%	0%
• 2 - 5 years	0%	0%	0%	0%
• 5 - 10 years	0%	0%	0%	0%
• Over 10 years	100%	100%	100%	100%
The lower limit for all periods	0%	0%	0%	0%
Upper limit for fixed interest rate exposure				
expressed as a % of total investments	100%	100%	100%	100%
Upper limit for variable rate exposure				
expressed as a % of total investments	50%	60%	60%	60%
Upper limit for total principal sums invested for over 364 days (per maturity date)	£20,000,000	£20,000,000	£20,000,000	£20,000,000