<table>
<tr><td>Report To:

Audit Committee</td><td>Date

4 February 2015</td><td>Classification

Unrestricted</td><td>Report No.</td><td>Agenda Item No.</td></tr>
<tr><td colspan="2">REPORT OF:

Chris Holme, Acting Corporate Director of Resources
ORIGINATING OFFICER(S):
Bola Tobun, Investment & Treasury Manager</td><td colspan="3">Treasury Management Activity for Period Ending 31 October 2014

WARD(S) AFFECTED:

N/A</td></tr>
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Lead Member	**Cllr Alibor Choudhury – Resources**
Community Plan Theme	**All**
Strategic Priority	**One Tower Hamlets**

1. SUMMARY

1.1 This report advises the Committee of treasury management activity for the current financial year up to 31 October 2014 and the continued appropriateness of the Treasury Management Strategy and Treasury Prudential Indicators, which were approved by Council on 26 February 2014 as required by the Local Government Act 2003.

1.2 The report details the current credit criteria adopted by the Acting Corporate Director of Resources, the investment strategy for the current financial year and the projected investment returns.

1.3 The current average return on investment stands at 0.72%, compared with budget set of 0.80%, whilst the budgeted cash return on assets was £1.6m for 2014/15; this has been revised to £2.7m due to large cash balances.

1.4 In accordance with regulatory requirements the Council has approved Prudential Indicators for Treasury Management. Treasury activities have not resulted in any breach of the approved limits. A Mid-Year review of the Treasury Management Strategy was presented to Council at its meeting of the 26 November 2014 to approved modification to the investment policy.

2. DECISIONS REQUIRED

2.1 Members are recommended to:

- note the contents of the treasury management activity report for period ending 31 October 2014.

3 REASONS FOR DECISIONS

3.1 Legislation requires that regular reports be submitted to Council/Committee detailing the council’s treasury management activities.

3.2 The regular reporting of treasury management activities should assist in ensuring that Members are able to scrutinise officer decisions and monitor progress on the implementation of the investment strategy as approved by Full Council.

4 ALTERNATIVE OPTIONS

4.1 The Council is bound by legislation to have regard to the Treasury Management (TM) Code. The Code requires that the Council or a sub-committee of the Council (Audit Committee) should receive regular monitoring reports on treasury management activities.

4.2 If the Council were to deviate from those requirements, there would need to be some good reason for doing so. It is not considered that there is any such reason, having regard to the need to ensure that Members are kept informed about treasury management activities and to ensure that these activities are in line with the investment strategy approved by the Council.

4.3 Within reason, the Council can vary its treasury management strategy having regard to its own views about its appetite for risk in relation to the financial returns required.

5 BACKGROUND

5.1 The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 require local authorities to have regard to the Treasury Management Code. The Treasury Management code requires that the Council or a sub-committee of the Council (Audit Committee) should receive regular monitoring reports on treasury management activities and risks.

5.2 These reports are in addition to the mid-year and annual treasury management activity reports that should be presented to Council midway through the financial year and at year end respectively.

5.3 This report details the current credit criteria/risk level adopted by the Corporate Director of Resources, the investment strategy for the current financial year and the projected investment returns.

6. TREASURY MANAGEMENT STRATEGY 2014/15

6.1 The Council's Treasury Management Strategy was approved on 26 February 2014 by Full Council. The Strategy comprehensively outlines how the treasury function is to operate over the financial year 2014-15 and it covers the following:

- Treasury limits in force which will limit the treasury risk and activities of the Council;
- Prudential and Treasury Indicators;
- The current treasury position;
- Prospects for interest rates;
- The borrowing strategy (including policy on borrowing in advance of need);
- Debt Rescheduling;
- The Investment Strategy;
- Credit Worthiness Policy'
- Policy on use of external service providers; and
- The Minimum Revenue Provision (MRP) Strategy

7. TREASURY ACTIVITY FOR PERIOD 1 April to 31 October 2014

7.1 This section of the report gives an update on the market and sets out:

- The current credit criteria being operated by the Council.
- The treasury investment strategy for the current financial year and the progress in implementing this.
- The transactions undertaken in the period and the investment portfolio outstanding as at 31 October 2014.

8 MARKET UPDATE (October 2014)

8.1 The economic outlook for the UK and US has improved, but for the Eurozone the future remains tepid at best, in spite of the recent ECB policy action. Eurozone progress will continue to be hampered by a number of fundamental issues, not least stubbornly high unemployment, in all bar one or two countries in the bloc. While the overall economy is more robust than it was in 2011, a renewal of problems within the periphery and/or elsewhere may still weigh on market sentiment in 2014.

8.2 Central bank activity continues to dominate underlying sentiment and will likely remain at the forefront in driving market confidence for some time to come. Recent market activity is another clear sign of attempts to adjust to a life beyond ultra-supportive monetary policy in the UK and US. Other recent examples have included a series of comments from Bank Governor Mark Carney and the minutes of the last three MPC meetings showing two members voting for an immediate rate hike. These have led to increased volatility in short dated money market and bond yields, as well as currency and equity markets. The signs of cooling seen in recent UK data releases would suggest that momentum in the recovery is easing, without the need for policy increases. As such, analysts have continued to push back their expectations of the first hike until at least the second quarter of 2015.

8.3 The US Federal Reserve concluded its tapering programme at the October meeting. Although the mid-month market volatility had suggested that the move could be postponed, the central bank was comforted that the economy continues to grow at a "…moderate pace". Although the accompanying statement continued to state that rates would remain unchanged for a "…considerable time" its overall tone was seen as more hawkish than expected. This was also reflected in the fact that previous "hawks" agreed with the wording, but one member voted against, highlighting suggestions that the weak inflation outlook warranted a longer time scale until rates were raised. The updated view has seen a reversal of a previous shift in forecasts towards the first move occurring in the second half of next year.

8.4 Closer to home, some commentators have cried foul at Bank of England Governor, Mark Carney, again. Just a few days after the release of a dovish Inflation Report (August), where the weakness of average earnings was suggested to hold back policy tightening, he commented in a newspaper interview that rates could yet rise, even if there is no material improvement in wages. However, he did qualify the statement by saying that there would need to be confidence that wages were going to sustainably improve, before a rate rise could be considered. Nevertheless, for a central banker who continues to place most emphasis on the long game (ie focus on where rates may head over the medium term, not when any tightening begins) his performance over the last few months has caused some consternation in markets. Perhaps, in hindsight, his most recent comments were aimed at dampening the market reaction to the two votes for an immediate rate hike at recent meetings.

8.5 For some forecasters the “No” Scottish vote did not just remove uncertainty from the timing of the initial rate rise, but also the medium term outlook. If the Union had been broken up, it would likely have had a material impact on UK plc, and thus the medium term outlook for interest rates. Nevertheless, with a General Election in May, the potential for an EU referendum thereafter and prospective changes to the political landscape in the UK, politics is likely to remain an uncertain factor for a while yet.

8.6 Through the start of 2014, emerging markets issues and more recently, geo-political concerns, have also had a major bearing on market sentiment. While the global recovery may continue, the outlook is by no means certain and markets are likely to be hit with further bouts of volatility through the remainder of the year and beyond.

8.7 Most forecasters now expect the MPC to begin raising rates in the first half of 2015 as the date when the MPC will begin raising rates. However, fine tuning of this will require a clear series of data releases, especially regarding the removal of slack in the labour market. The actions/words, or inactions, of central bankers are likely to continue to be the key themes dominating market sentiment in the coming months. They have undertaken enormous support programmes in recent years, in an effort to stabilise the world economy. However, can they be unwound without causing material market turbulence in the future? The US has started to minimise the levels of increased support through its recently-concluded tapering programme, but the full unwinding of policy support may take many years to accomplish.

8.8 Counterparty quality remains the key factor when making investment decisions. Policy rates will tighten at some stage, and this has called into question the benefits of some of the longer dated deals on offer. However, there are still some attractive rates, if the future path of rate rises is measured, as the Bank continually suggests.

9 CREDIT CRITERIA

9.1 The credit criteria for investment counterparties were amended and reported for approval to the Council in November 2014 as part of the Mid-Year review of the Treasury Management Strategy. The Council will continue to invest within the UK and its Government regardless of the country’s sovereign rating. Explanation of credit ratings criteria is attached at Appendix approve the changes to the minimum credit rating criteria; that is the removal of viability or financial strength rating and support ratings as set out in section 10 and table 1 of Appendix 3;

9.2 The Council has been advised by the treasury adviser that rating assumptions are to be updated by the three main rating agencies in order to remove the implied sovereign support embedded in the creditworthiness of an institution. The agencies are primarily reacting to the European regulatory changes which aim at ensuring the resolvability of banks without government support (e.g., resolution regimes and recovery and resolution plans).

9.3 One of the main objectives of these revisions has been to increase transparency relating to the impact of external factors on banks’ creditworthiness, such as the probability that they will receive support if they encounter difficulty. Massive government interventions during the banking crisis have indeed confirmed that government support can lower the probability that a bank will default. More recently, in the European countries at the centre of the sovereign debt tensions, the link between major banks’ creditworthiness and the perceived problems of their respective sovereign has also been evident. These regulations are due to come into effect January 2016.

9.4 The rating changes could happen before this date, as a matter of fact Fitch rating agency has reassessed their overall methodology and Capita, the Council's treasury adviser has stopped using Financial Strength Rating (FSR) and Support Ratings in computing credit worthiness of institutions. Hence we asked the Council to approved modifications the Council's basis of formulating counter party template by removing the Viability or Financial Strength Rating (FSR) and Support Rating from the template. As going forward the Financial Strength Rating (FSR) and Support Ratings will, essentially, become irrelevant.

9.5 Another key issue that faces the efficient and effective management of the Council's cash portfolio currently was that of counterparty availability. The Councils have deposit of £140m outstanding with the part nationalised banking groups and the challenge ahead will be to address the decline in the Government holding in Lloyds Banking Group and the impact that this could have on the counterparty limit that the Council currently applies to this entity.

9.6 In addressing this issue, a reduction in the nominal and duration limits has been applied to Lloyds Banking Group. The Council is struggling at the moment to place deposit with institutions as there are not many out there that meets the Council current minimum credit rating criteria. However there are some institutions that meet the Council's minimum credit criteria but offering other financial products that are not included in the Council's Investment Strategy based on the advice of the Council's treasury adviser, we asked for the Council approval to introduce new investments products as this will help with liquidity and diversification issue.

9.7 In light of the above points, approval was sought at the Council's meeting in November 2014 for the Council's Investment Policy to be modified as follows:

- *The adoption of credit rating criteria as shown at table 1 of Appendix 1 as the minimum credit rating required for an institution to be included in the Council's counterparty list.*
- *Inclusion of other financial instruments such as Certificates of Deposits, Treasury Bills, Commercial Papers and Corporate Bonds in line with the Council's credit worthiness criteria, as shown in Appendix 1; table 2 & 3; and*
- *Increase of prudential indicator limit for investments over one year but no more than three years to £50million from £25million.*

10 <u>INVESTMENT STRATEGY</u>

10.1 Capita provides cash management services to the Council, but the Council retains control of the credit criteria and the investments, so Capita's role is purely advisory.

10.2 In addition to providing cash management services, Capita also provides treasury consultancy/advisory service to the Council.

10.3 The outlook for interest rates indicates a growing belief that central banks are keen to keep rates low for a prolonged period, to encourage global growth. Forecasters are moving the date of the first projected interest rate increase in the UK forward, potentially into Q2 2015. If and when rates do start to rise, the authority will wish to be in a position to take advantage by not having too much money invested in longer term investments.

10.4 The current balance of £297.8m is £97.8m higher than the projected average cash balance of £200m. This is mainly attributable to slippage on the capital programme. It is envisaged that cash balances will reduce in the medium term as expenditure on the capital programme picks up through the remainder of the financial year.

10.5 At the end of October, the Council has £42.8m of outstanding investments of £297.8m as overnight money and £75m maturing within 3 months, £115m maturing within 3-6 months, £45m maturing within 6-9 months, no investments maturing within 9-12 months and £20m to mature after 12months.

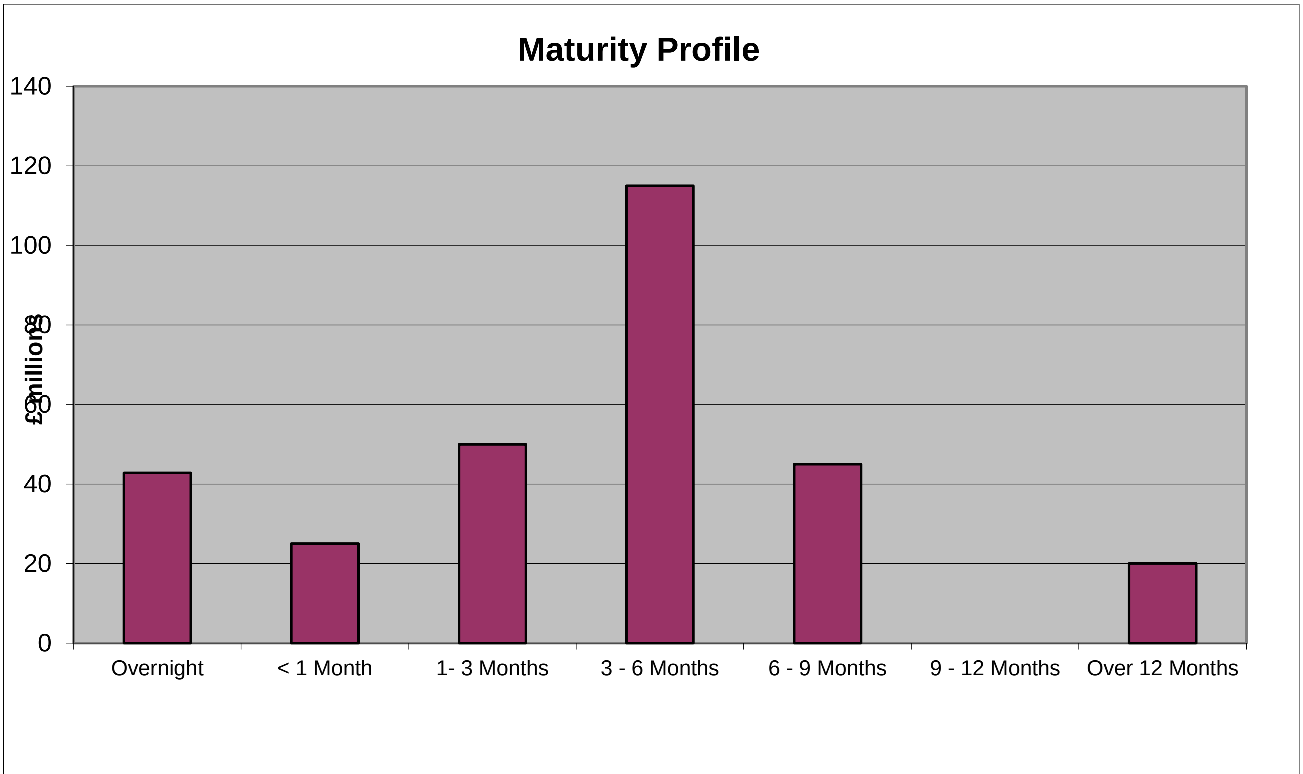
10.6 The budgeted investment return for 2014/15 was £1.6m. This target has been achieved due to large cash balances the Council has been working with; this balance has been well above the estimated budget balance of £200m. The investment return has now been revised to £2.7m with average cash balance of £325m for 2014/2015.

10.7 In response to the comments from the last meeting, the Council treasury officers investigated the issue of Lloyds paying 6% for a thirty day investment … even in the retail market, the Council's treasury adviser has been unable to confirm this. Their three year bond issue is only paying 1.70%. Their business 30 days' notice account is actually paying just 0.05%.

10.8 For 2014/15 strategy, there are institutions the Council cannot place deposits with as they are unrated institutions or institutions below the Council's minimum lending criteria. For 2015/16 Treasury management strategy the Council's treasury officers are looking for investment opportunities but have regard to security and liquidity before embracing yield.

10.9 Current investment portfolio is as set out below.

<u>Investment Portfolio at 31 October 2014</u>

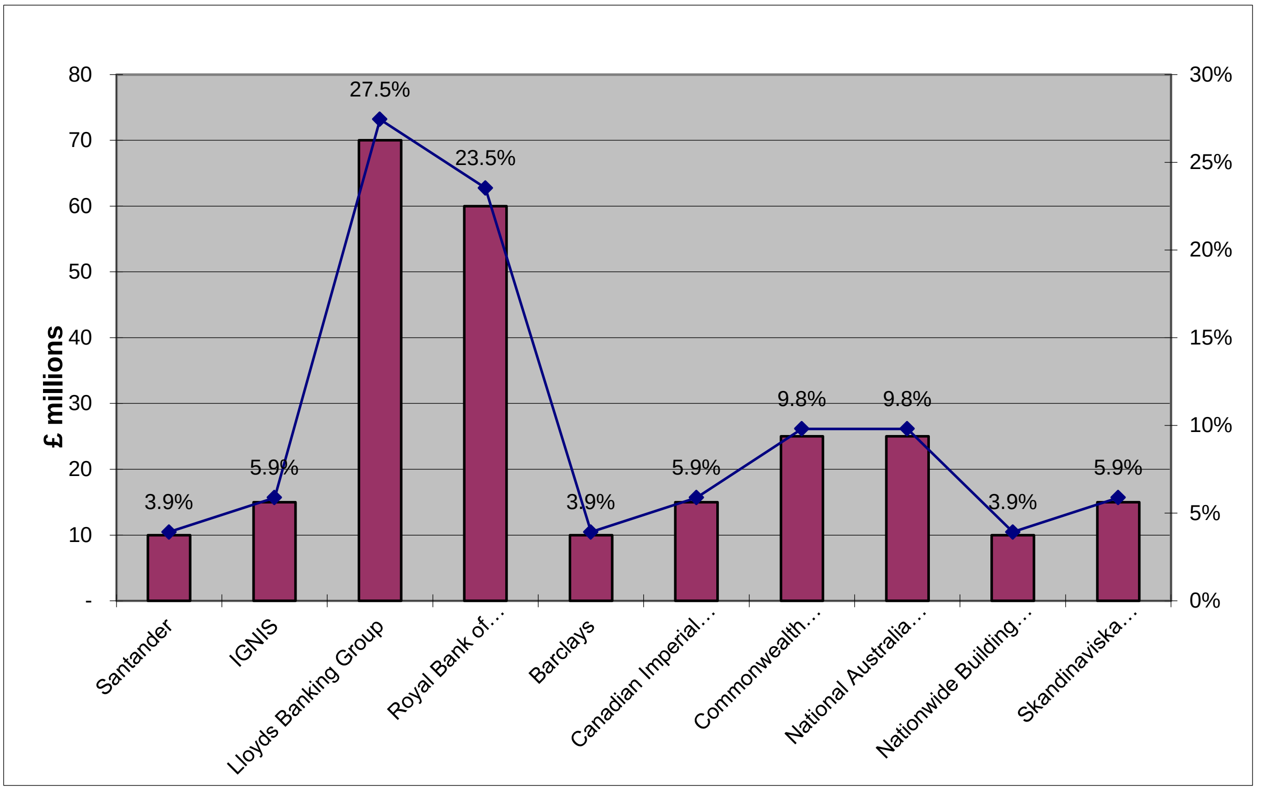


10.10 The Weighted Average Maturity for outstanding investment portfolio is 156 days. This is the average number of outstanding days to maturity of each deal from 31st October 2014.

10.11 The Council’s exposure to any one counterparty/Group is represented by the chart below including exposure as a percentage of total assets invested as at 31 October 2014.

10.12 The chart below shows the deposits outstanding with authorised counterparties as at 31 October 2014, of which 51% were with part-nationalised banks (Lloyds and RBS Groups).

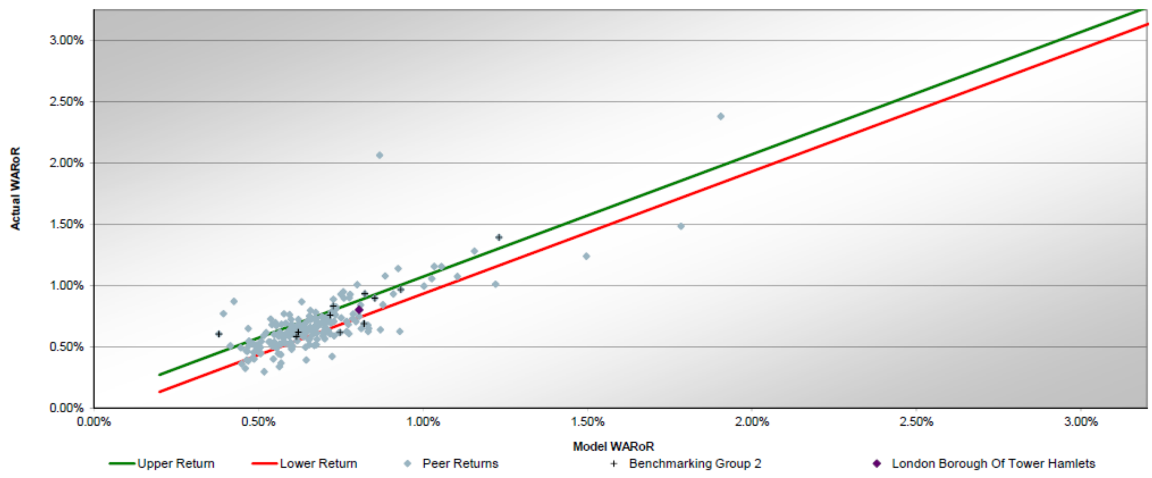
Maturity of Investment Portfolio as at 31 October 2014



11 INVESTMENT BENCHMARKING CLUB

11.1 LBTH participates in a benchmarking club to enable officers to compare the Council’s treasury management /investment returns against those of similar authorities. The model below shows the performance of benchmark club members given the various levels of risks taken as at 30 September 2014. The model takes into account a combination of credit, duration and returns achieved over the duration, and it includes data from 20 local authorities. Tower Hamlets lies close to the expected return given the council’s portfolio risk profile, which is placing deposits with institutions with the sovereign rate of AAA.

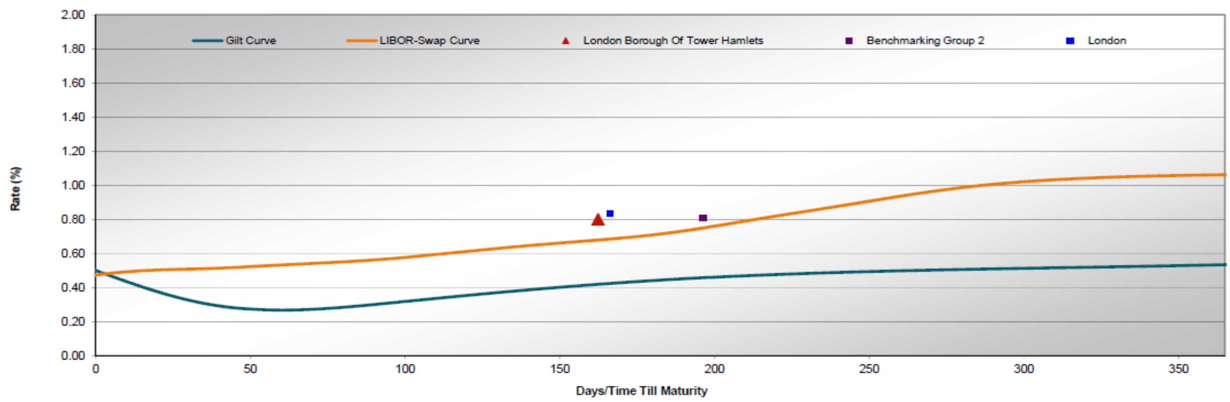
Population Returns against Model Returns



	Actual WARoR	Model WARoR	Difference	Lower Bound	Upper Bound	Performance
London Borough Of Tower Hamlets	0.80%	0.81%	-0.01%	0.74%	0.88%	Inline

11.2 The weighted average rate of return (WARoR) - this is the average annualised rate of return weighted by the principal amount in each rate. And for Tower Hamlets is 0.80% at the end of September 2014, compared to 0.81% for the benchmarking group. The return on LBTH investment is commensurate with the Council's risk appetite as set out in the Investment Strategy.

Returns Comparable Against the Risk-Free Rate and LIBOR Curve

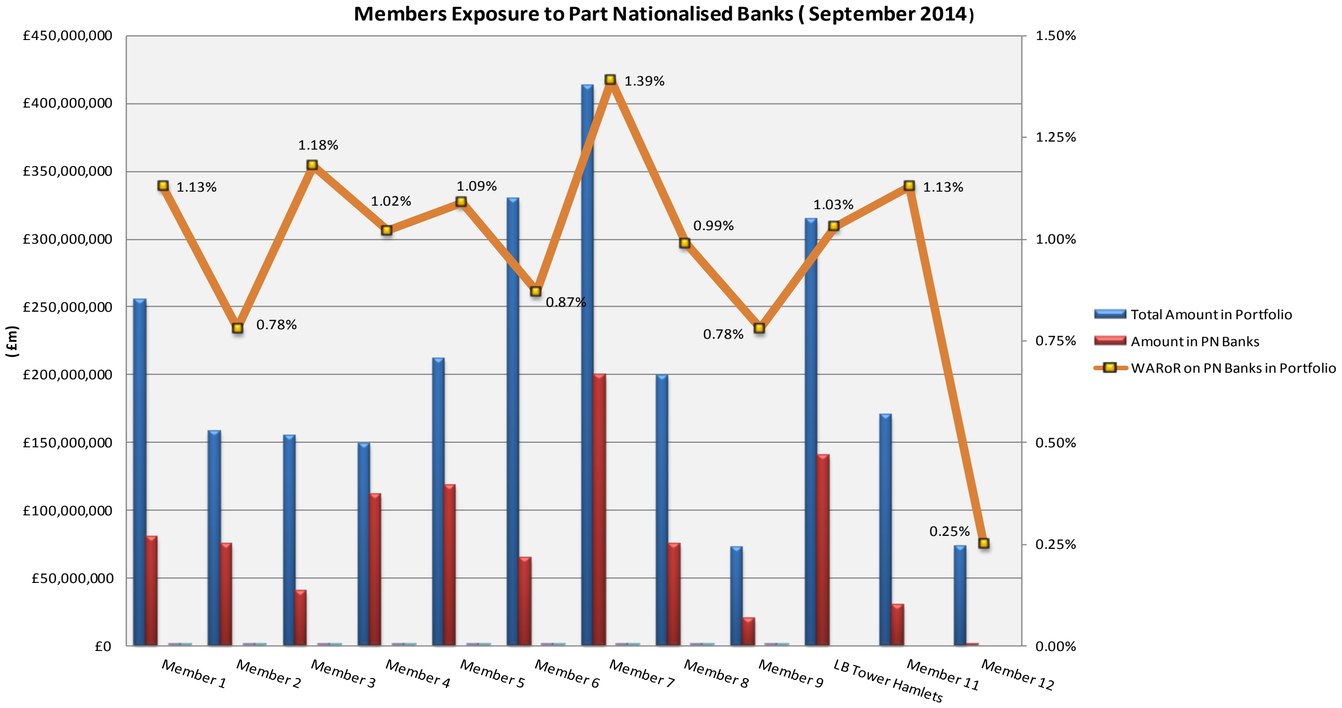


	WARoR	WAM	WATT	WARisk	Gilt	LIBOR-Swap	Difference Gilt	Difference LIBOR-Swap	Model Bands	Performance
London Borough Of Tower Hamlets	0.80%	162	309	3.3	0.42%	0.68%	0.38%	0.12%	0.74% - 0.88%	Inline
Benchmarking Group 2	0.81%	196	325	2.9	0.46%	0.75%	0.35%	0.06%	0.70% - 0.84%	Inline
London	0.83%	166	291	2.8	0.42%	0.68%	0.41%	0.15%	0.68% - 0.82%	Above

11.3 The Weighted Average Time to Maturity (WAM) - This is the average time, in days, till the portfolio matures, weighted by principal amount. At the end of September for LBTH was 162 days, compared to 196 days for the benchmarking group.

11.4 The Weighted Average Total Time (WATT) - this is the average time, in days, that deposits are lent out for, weighted by principal amount. At the end of September for LBTH was 309 days, compared to 325 days for the benchmarking group.

11.5 A further chart is set below that compares exposure to Part-Nationalised Banks (PNB) between club members as the Council currently has a significant amount of investment with PNBs. The chart shows that the Council's allocation to and returns from investment with PNBs is in line with other London boroughs as at 30 September 2014.


Members Exposure to Part Nationalised Banks (September 2014)
£450,000,000
£400,000,000
£350,000,000
£300,000,000
£250,000,000
£200,000,000
£150,000,000
£100,000,000
£50,000,000
£0
(£m)
1.50%
1.25%
1.00%
0.75%
0.50%
0.25%
0.00%
1.13%
0.78%
1.18%
1.02%
1.09%
0.87%
1.39%
0.99%
0.78%
1.03%
1.13%
0.25%
Member 1
Member 2
Member 3
Member 4
Member 5
Member 6
Member 7
Member 8
Member 9
LB Tower Hamlets
Member 11
Member 12
Total Amount in Portfolio
Amount in PN Banks
WARoR on PN Banks in Portfolio

Counterparty Exposure as at 31 October 2014

Time to Maturity	Counterparty	From	Maturity	Amount £m	Rate
Overnight	IGNIS		**MMF**	15.00	0.48%
	Blackrock		**MMF**	15.00	0.46%
	BNP Paribas		**MMF**	12.80	0.40%
	SUB TOTAL			**42.80**	
< 1 Month	Lloyds Banking Group	13/11/2013	13/11/2014	5.00	0.98%
	Skandinaviska Enskilda Banken	29/04/2014	14/11/2014	5.00	0.56%
	Canadian Imperial Bank of Commerce	18/08/2014	18/11/2014	15.00	0.42%
1 - 3 Months	Lloyds Banking Group	04/12/2013	04/12/2014	5.00	0.98%
	Royal Bank of Scotland	09/07/2013	09/01/2015	5.00	0.95%
	Santander		Call - 95N	10.00	0.45%
	Royal Bank of Scotland	27/01/2012	27/01/2015	5.00	3.35%
	Lloyds Banking Group	04/02/2014	04/02/2015	5.00	0.95%
	Lloyds Banking Group	13/02/2014	13/02/2015	5.00	0.95%
	Commonwealth Bank of Australia	15/08/2014	13/02/2015	5.00	0.48%
	DZ Bank	26/08/2014	26/02/2015	5.00	0.71%
	Skandinaviska Enskilda Banken	29/08/2014	27/02/2015	5.00	0.64%
3 - 6 Months	Lloyds Banking Group	04/09/2014	04/03/2015	5.00	0.70%
	Lloyds Banking Group	05/03/2014	05/03/2015	10.00	0.95%
	Barclays	05/09/2014	05/03/2015	10.00	0.61%
	Commonwealth Bank of Australia	15/09/2014	16/03/2015	5.00	0.53%
	National Australia Bank	18/03/2014	18/03/2015	10.00	0.57%
	Lloyds Banking Group	07/10/2014	07/04/2015	5.00	0.70%
	Lloyds Banking Group	11/04/2014	10/04/2015	5.00	0.95%
	Lloyds Banking Group	11/07/2014	13/04/2015	10.00	0.80%
	Nationwide Building Society	13/10/2014	13/04/2015	5.00	0.66%
	Lloyds Banking Group	15/04/2014	15/04/2015	5.00	0.95%
	Royal Bank of Scotland	16/04/2013	16/04/2015	5.00	0.88%
	Royal Bank of Scotland	16/04/2014	16/04/2015	5.00	0.67%
	Nationwide Building Society	16/10/2014	16/04/2015	5.00	0.66%
	Lloyds Banking Group	17/07//2014	17/04/2015	5.00	0.80%
	Skandinaviska Enskilda Banken	29/04/2014	29/04/2015	5.00	0.71%
	Lloyds Banking Group	29/10/2014	29/04/2015	5.00	0.70%
	National Australia Bank	14/05/2014	14/05/2015	10.00	0.63%
	DZ Bank	26/08/2014	26/05/2015	5.00	0.86%
6 - 9 Months	National Australia Bank	07/07/2014	07/07/2015	5.00	0.64%
	Royal Bank of Scotland	15/07/2014	15/07/2015	20.00	0.97%
	Commonwealth Bank of Australia	15/07/2014	15/07/2015	5.00	0.83%
	Commonwealth Bank of Australia	17/07/2014	17/07/2015	5.00	0.82%
	Commonwealth Bank of Australia	12/08/2014	12/08/2015	5.00	0.81%
	DZ Bank	26/08/2014	26/08/2015	5.00	0.98%
9 - 12 Months					
> 12 Months	Royal Bank of Scotland	27/02/2013	26/02/2016	10.00	1.15%
	Royal Bank of Scotland	20/03/2014	20/03/2016	5.00	1.25%
	Royal Bank of Scotland	10/01/2014	09/01/2017	5.00	1.74% *
	SUB TOTAL			**255.00**	
	TOTAL			**297.80**	

* This is a structured deal, the terms of which could change during its tenor.

INVESTMENT RETURNS

12.1 Investment returns since inception of the cash management arrangement with Capita has been consistently above the portfolio benchmark, which is 7 Day LIBID (the London Interbank Bid Rate). Performance against target which is benchmark (7 Day LIBID) plus 0.25% has been good so far, with year to date return on investment at 0.72%, which is 12 basis points above target set.

12.2 The Strategy approved at the 26 February 2014 Council allowed for more flexibility and the benefits of this Strategy is proving extremely valuable given the challenge of a counterparty list that continues to contract in the face of credit worthiness downgrades by the ratings agencies. The latest counterparty list is attached at Appendix 3.

12.3 The portfolio delivered a return which outperforms the target set, LIBID + 0.25% for the first seven months of the year. Although returns are significantly above the LIBID, which currently stands at 0.35%.

12.4 With interest rates set to remain low and provided there's no undue increase in the Council's risk, we would continually review the counter party list prudently and cautiously in order to broaden the range of counterparties and/or products in order to enhance returns of our cash holdings, giving priority to the security and liquidity of investments before yield.

12.5 Below is a table that details performance of investments. The table shows that performance has consistently outperformed LIBID.

Performance against Benchmark

Period	LBTH Performance	Target (7 Day LIBID+0.25%)	(Under)/Out Performance
Full Year 2013/14	**0.82%**	**0.60%**	**0.22%**
April 2014/15	0.70%	0.59%	0.11%
May 2014/15	0.69%	0.59%	0.10%
June 2014/15	0.68%	0.60%	0.08%
July 2014/15	0.70%	0.60%	0.10%
August 2014/15	0.73%	0.60%	0.13%
September 2014/15	0.76%	0.61%	0.16%
October 2014/15	0.77%	0.61%	0.10%
Average 2014/15	**0.72%**	**0.60%**	**0.12%**

13 DEBT PORTFOLIO

13.1 The table below sets out the Council's debt as at the beginning of the year and 31 October 2014.

	31 March 2014 Principal £'000	Average rate %	31 October 2014 Principal £'000	Average rate %
Fixed Rate Funding:				
-PWLB	12,064	7.37	12,029	7.37
-Market	13,000	4.37	13,000	4.37
Total Fixed Rate Funding	25,064	5.81	25,029	5.81
Variable Rate Funding:				
-PWLB	-		-	
-Market	64,500	4.32	64,500	4.32
Total Variable Rate Funding	64,500	4.32	64,500	4.32
Total debt	***89,564***	***4.73***	***89,529***	***4.73***
CFR	***220,720***		***235,975***	
Over/ (under) borrowing	***(131,156)***		***(146,446)***	

13.2 No borrowing has been undertaken to date in this financial year. Total debt outstanding, stands at £89.529m, against estimated CFR of £235.975m for 2014/15, resulting in an under-borrowing of £146.446m

14. INVESTMENT STRATEGY UPDATE

14.1 Full Council approved the Investment Strategy on 26 February 2014. Officers continue to look for ways to maximise returns on cash balances within the constraints of the Investment Strategy. The Investment Strategy was developed based on an improving outlook in the money markets.

14.2 Wholly or partly owned government banks offer significantly higher rates than the DMO, but have similar levels of security based on government guarantee of their credit quality. The Council already relies on this guarantee and invests with these banks, and the current strategy is to have £70m money limit for each group with an aggregate of 40% of the overall investment portfolio. This should ensure that the Council continues to receive good returns on its cash balances and that the investment strategy is optimised to support the Council's efficiency programme.

15. COMMENTS OF THE CHIEF FINANCIAL OFFICER

15.1. The comments of the Acting Corporate Director Resources are incorporated in the report.

16. LEGAL COMMENTS

16.1 Treasury management activities cover the management of the Council's investments and cash flows, its banking, money market and capital market transactions, the effective control of risks associated with those activities and the pursuit of optimum performance consistent with those risks. The Local Government Act 2003 provides a framework for the capital finance of local authorities. It provides a power to borrow and imposes a duty on local authorities to determine an affordable borrowing limit. It provides a power to invest. Fundamental to the operation of the scheme is an understanding that authorities will have regard to proper accounting practices recommended by the Chartered Institute of Public Finance and Accountancy (CIPFA) in carrying out capital finance functions.

16.2 The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 require the Council to have regard to the CIPFA publication "Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes" ("the Treasury Management Code") in carrying out capital finance functions under the Local Government Act 2003. If after having regard to the Treasury Management Code the Council wished not to follow it, there would need to be some good reason for such deviation.

16.3 The Treasury Management Code requires as a minimum that there be a practice of regular reporting on treasury management activities and risks to the responsible committee and that these should be scrutinised by that committee. Under the Council's Constitution, the audit committee has the functions of monitoring the Council's risk management arrangements and making arrangements for the proper administration of the Council's affairs.

17. ONE TOWER HAMLETS CONSIDERATIONS

17.1 Interest on the Council's cash flow has historically contributed significantly towards the budget.

18. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

18.1 There are no Sustainable Actions for A Greener Environment implications.

19. RISK MANAGEMENT IMPLICATIONS

19.1 Any form of investment inevitably involves a degree of risk. To minimise risk the investment strategy has restricted exposure of council cash balances to UK backed banks or institutions with the highest short term rating or strong long term rating.

20. CRIME AND DISORDER REDUCTION IMPLICATIONS

20.1 There are no crime and disorder reduction implications arising from this report.

21. EFFICIENCY STATEMENT

21.1 Monitoring and reporting of treasury management activities ensures the Council optimises the use of its monetary resources within the constraints placed on the Council by statute, appropriate management of risk and operational requirements.

LOCAL GOVERNMENT ACT 1972 (AS AMENDED) SECTION 100D
LIST OF "BACKGROUND PAPERS" USED IN THE PREPARATION OF THIS REPORT

Brief description of "background papers"	***Name and telephone number of holder And address where open to inspection***
September 2014 Benchmarking Report & October 2014 Investment Portfolio Analysis Report	*Bola Tobun Ext. 4733 Mulberry Place, 3rd Floor.*

Appendix 1: Creditworthiness Policy

1 Credit rating information is supplied by Capita Asset Services, our treasury advisers, 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. 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.

2 The criteria for providing a pool of high quality investment counterparties (both Specified and Non-Specified investments) is:

i. Good credit quality – the Council will only use banks which:

1. are UK banks; and/or
2. are non-UK and domiciled in a country which has a minimum sovereign long term rating of AAA; and

Where rated, have as a minimum, the following Fitch ratings, (for equivalent Moody's and Standard and Poor's credit ratings, see Table 1)

i. Short term – 'F1'

ii. Long term – 'A'

- Part nationalised/wholly owned UK banks (i.e. Lloyds Banking Group and Royal Bank of Scotland). These banks can be included if they continue to be part nationalised/wholly owned or they meet the ratings in Banks (i) above;
- The Council's own banker (The Co-operative Bank) 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;
- Building Societies – The Council will use all building societies which meet the ratings for banks outlined above;
- Money Market Funds – UK, AAA (Sterling);
- UK Government (including gilts, treasury bills and the Debt Management Account Deposit Facility);
- Local Authorities (including parish councils, Police and Fire Authorities).
- Non UK Government
- Supranational Institutions
- Corporate Bonds

3 Specified investments comprise investment instruments which the Council considers offer high security and liquidity. These instruments can be used with minimal procedural formalities. The Guidance considers that specified investments have the following characteristics: -

- denominated in Sterling and have a term of less than one year;
- have "good" credit ratings as determined by the Council itself.

4 All other investments are termed non-specified investments. These involve a relatively higher element of risk, and consequently the Council is required to set a limit on the maximum proportion of their funds which will be invested in these

instruments. The Strategy should also specify the guidelines for making decisions and the circumstances in which professional advice is obtained.

5 Investment instruments identified for use in the financial year are listed in tables 3 and 4 below under the 'Specified' and 'Non-Specified' Investments categories with the associated counterparty limits as set through the Council's Treasury Management Practices – Schedules.

Specified Investments:

6 It is recommended that the Council should make Specified investment as detailed below in Table 2.

7 All such investments will be sterling denominated, with maturities up to maximum of 1 year, meeting the minimum credit quality criteria where applicable. The Council will continue its policy of lending surplus cash to counterparties that meet the Council's minimum credit ratings as outlined in below table 1.

8 The minimum credit rating required for an institution to be included in the Council's counterparty list is as follows:

Table 1

Agency	Long-Term	Short-Term
Fitch	A	F1
Moody's	A2	P-1
Standard & Poor's	A	A-2
Sovereign Rating	AAA	
Money Market Fund	AAA	

Specified Investments:

9 The current strategy is that all such investments will be sterling denominated, with maturities up to maximum of 1 year, meeting the minimum 'high credit' quality criteria where applicable. The council will continue its policy of lending surplus cash to counterparties that have high credit ratings, defining 'high credit rating' as being F1+ Fitch short-term and AA- long-term credit rating.

Table 2

Institution	Minimum High Credit Criteria	Term Limit	Monetary Limit
Debt Management Office (DMO) Deposit Facility	Not applicable	N/A	No Limit
Local Authorities	Not applicable	1 year	£10m
Term deposits – banks and building societies	Short-term F1+, Long-term AA-	1 year	£30m
Term deposits – banks and building societies	Short-term F1, Long-term A+	1 year	£15m
Term deposits – banks and building societies	Short-term F1, Long-term A	6 months	£10m
UK Government Gilts and Treasury Bills	Long Term AAA	1 year	£50m
UK Government – Part Nationalised Banks	Per group	1 year	£70m or 30% of the portfolio
Certificates of Deposits issued by banks and building	Short-term F1+, Long-term AA-	1 year	£30m
Non-UK Government Bonds	Sovereign rating Long Term AAA	1 year	£10m
Supranational Bonds	Sovereign rating Long Term AAA	1 year	£10m
Collective Investment Schemes structured as Investment Companies (OEICs)			
Money Market Funds	AAA rated	Liquid	£15m

Definitions of credit ratings are attached at **Appendix 2**.

Non-Specified Investments:

All investments that do not qualify as specified investments are termed non-specified investments. The credit criteria for non-specified investments are detailed in the table below.

Table 3

Institution	Minimum High Credit Criteria	Time Limit	Money Limit
Term deposits – Banks and Building Societies	Sovereign rating AAA Short-term F1+, Long-term AA-	3 years	£25m or 10% of Investment Portfolio
Structured Deposits: Fixed term depos variable rate and variable maturities	Sovereign rating AAA Short-term rating F1+ Long-term rating AA-	3 years	£25m or 10%of Investment Portfolio
UK Government Gilts and treasury bill	Long Term AAA	5 years	£25m or 10% of Investment Portfolio
Certificates of Deposits issued by banl society	Sovereign rating AAA Short-term rating F1+ Long-term rating AA-	3 years	£25m or 10% of Investment Portfolio

Appendix 2: Definition of Credit Ratings

Short-term Ratings

Rating	
F1	**Highest credit quality.** Indicates the strongest capacity for timely payment of financial commitments; may have an added "+" to denote any exceptionally strong credit feature.
F2	**Good credit quality.** A satisfactory capacity for timely payment of financial commitments, but the margin of safety is not as great as in the case of the higher ratings.
F3	**Fair credit quality.** The capacity for timely payment of financial commitments is adequate; however, near-term adverse changes could result in a reduction to non-investment grade.

Long-term Ratings

Rating	Current Definition
AAA	**Highest credit quality.** 'AAA' ratings denote the lowest expectation of credit risk. They are assigned only in case of exceptionally strong capacity for timely payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.
AA	**Very high credit quality.** 'AA' ratings denote a very low expectation of credit risk. They indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A	**High credit quality.** 'A' ratings denote a low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to changes in circumstances or in economic conditions than is the case for higher ratings.
BBB	**Good credit quality.** 'BBB' ratings indicate that there is currently a low expectation of credit risk. The capacities for timely payment of financial commitments are considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity. This is the lowest investment-grade category

Individual Ratings

Rating	
A	A very strong bank. Characteristics may include outstanding profitability and balance sheet integrity, franchise, management, operating environment or prospects.
B	A strong bank. There are no major concerns regarding the bank. Characteristics may include strong profitability and balance sheet integrity, franchise, management, operating environment or

	prospects.
C	An adequate bank, which, however, possesses one or more troublesome aspects. There may be some concerns regarding its profitability and balance sheet integrity, franchise, management, operating environment or prospects.
D	A bank, which has weaknesses of internal and/or external origin. There are concerns regarding its profitability, substance and resilience, balance sheet integrity, franchise, management, operating environment or prospects. Banks in emerging markets are necessarily faced with a greater number of potential deficiencies of external origin.
E	A bank with very serious problems, which either requires or is likely to require external support.

APPENDIX 3

COUNTER PARTY LIST

NAME	FITCH RATING				MOODY RATING			S&P RATING	
	Long Term	Short Term	Viability	Support	Long Term	Short Term	FSR	Long Term	Short Term
U.K	AA+	-	-	-	Aa1	-	-	AAA	-
Abbey National Treasury Services plc	A	F1	-	-	A2	P-1	-	-	-
Bank of New York Mellon (International) Ltd	AA-	F1+	-	1	-	-	-	-	-
Barclays Bank plc	A	F1	a	1	A2	P-1	C-	A	A-1
Citibank International Plc ~	A	F1	-	1	A2	P-1	C-	A	A-1
Close Brothers Ltd	A	F1	a	5	A3	P-2	C	-	-
Clydesdale Bank	A	F1	bbb+	1	Baa2	P-2	D+	BBB+	A-2
Co-operative Bank Plc	B	B	b	5	Caa2	NP	E	-	-
Credit Suisse International ~	A	F1	-	1	A1	P-1	-	A	A-1
Goldman Sachs International ~	A	F1	-	-	A2	P-1	-	A	A-1
Goldman Sachs International Bank ~	A	F1	-	-	A2	P-1	D+	A	A-1
HSBC Bank plc	AA-	F1+	a+	1	Aa3	P-1	C	AA-	A-1+
MBNA Europe Bank	A-	F1	-	1	-	-	-	-	-
Merrill Lynch International	A	F1	-	1	-	-	-	A	A-1
Morgan Stanley & Co. International plc ~	-	-	-	-	A3	P-2	-	A	A-1
Santander UK plc	A	F1	a	1	A2	P-1	C-	A	A-1
Standard Chartered Bank	AA-	F1+	aa-	1	A1	P-1	B-	AA-	A-1+
Sumitomo Mitsui Banking Corporation Europe Ltd ~	A-	F1	-	1	Aa3	P-1	C	A+	A-1
UBS Ltd ~	A	F1	-	1	A2	P-1	-	A	A-1
Lloyds Banking Group plc	A	F1	a-	1	A2	-	-	A-	A-2
Bank of Scotland Plc	A	F1	a-	1	A1	P-1	C-	A	A-1
Lloyds Bank Plc	A	F1	a-	1	A1	P-1	C-	A	A-1
Royal Bank of Scotland Group plc	A	F1	bbb	1	Baa2	P-2	-	BBB+	A-2
National Westminster Bank Plc	A	F1	bbb	1	Baa1	P-2	D+	A-	A-2
The Royal Bank of Scotland Plc	A	F1	bbb	1	Baa1	P-2	D+	A-	A-2
Ulster Bank Ltd (Suspended)	A-	F1	ccc	1	Baa3	P-3	E+	BBB+	A-2
Coventry BS	A	F1	a	5	A3	P-2	C	-	-
Nationwide BS	A	F1	a	1	A2	P-1	C	A	A-1

NAME	FITCH RATING				MOODY RATING			S&P RATING	
	Long Term	Short Term	Viability	Support	Long Term	Short Term	FSR	Long Term	Short Term
Collateralised LA Deposit*	AA+	-	-	-	Aa1	-	-	AAA	-
Debt Management Office	AA+	-	-	-	Aa1	-	-	AAA	-
Supranationals	AAA	-	-	-	Aaa	-	-	AAA	-
UK Gilts	AA+	-	-	-	Aa1	-	-	AAA	-
Australia	**AAA**	**-**	**-**	**-**	**Aaa**	**-**	**-**	**AAA**	**-**
Australia and New Zealand Banking Group Ltd	AA-	F1+	aa-	1	Aa2	P-1	B-	AA-	A-1+
Commonwealth Bank of Australia	AA-	F1+	aa-	1	Aa2	P-1	B-	AA-	A-1+
Macquarie Bank Limited	A	F1	a	3	A2	P-1	C-	A	A-1
National Australia Bank Ltd	AA-	F1+	aa-	1	Aa2	P-1	B-	AA-	A-1+
Westpac Banking Corporation	AA-	F1+	aa-	1	Aa2	P-1	B-	AA-	A-1+
Canada	**AAA**	**-**	**-**	**-**	**Aaa**	**-**	**-**	**AAA**	**-**
Bank of Montreal	AA-	F1+	aa-	1	Aa3	P-1	C+	A+	A-1
Bank of Nova Scotia	AA-	F1+	aa-	1	Aa2	P-1	B-	A+	A-1
Canadian Imperial Bank of Commerce	AA-	F1+	aa-	1	Aa3	P-1	C+	A+	A-1
National Bank of Canada	A+	F1	a+	1	Aa3	P-1	C	A	A-1
Royal Bank of Canada	AA	F1+	aa	1	Aa3	P-1	C+	AA-	A-1+
Toronto Dominion Bank	AA-	F1+	aa-	1	Aa1	P-1	B	AA-	A-1+
Denmark	**AAA**	**-**	**-**	**-**	**Aaa**	**-**	**-**	**AAA**	**-**
Danske Bank	A	F1	a	1	Baa1	P-2	C-	A	A-1
Finland	AAA	-	-	-	Aaa	-	-	AAA	-
Nordea Bank Finland plc ~	AA-	F1+	aa-	1	Aa3	P-1	C	AA-	A-1+
Pohjola Bank	A+	F1	-	1	Aa3	P-1	C-	AA-	A-1+
Germany	**AAA**	**-**	**-**	**-**	**Aaa**	**-**	**-**	**AAA**	**-**
BayernLB	A+	F1+	bb+	1	A3	P-2	D	-	-
Commerzbank AG	A+	F1+	bbb	1	Baa1	P-2	D+	A-	A-2
Deutsche Bank AG	A+	F1+	a	1	A3	P-2	D+	A	A-1
DZ Bank AG (Deutsche Zentral-Genossenschaftsbank)	A+	F1+	-	1	A1	P-1	C-	AA-	A-1+
Landesbank Baden Wuerttemberg	A+	F1+	bbb	1	A2	P-1	D+	-	-
Landesbank Berlin AG	-	-	-	-	A1	P-1	D+	-	-
Landesbank Hessen-Thueringen Girozentrale (Helaba)	A+	F1+	-	1	A2	P-1	D+	A	A-1
Landwirtschaftliche Rentenbank	AAA	F1+	-	1	Aaa	P-1	-	AAA	A-1+
Norddeutsche Landesbank Girozentrale	A	F1	bbb-	1	A3	P-2	D	BBB+	A-2
NRW.BANK	AAA	F1+	-	1	Aa1	P-1	-	AA-	A-1+
UniCredit Bank AG (Suspended)	A+	F1+	a-	1	Baa1	P-2	D+	A-	A-2

NAME	FITCH RATING				MOODY RATING			S&P RATING	
	Long Term	Short Term	Viability	Support	Long Term	Short Term	FSR	Short Term	Long Term
Netherlands	**AAA**	**-**	**-**	**-**	**Aaa**	**-**	**-**	**AA+**	**-**
Bank Nederlandse Gemeenten	AAA	F1+	-	1	Aaa	P-1	B-	AA+	A-1+
Cooperatieve Centrale Raiffeisen Boerenleenbank BA (Rabobank Nederland)	AA-	F1+	-	1	Aa2	P-1	B-	AA-	A-1+
ING Bank NV	A+	F1+	a	1	A2	P-1	C-	A	A-1
Nederlandse Waterschapsbank N.V	-	-	-	-	Aaa	P-1	C+	AA+	A-1+
Norway	**AAA**	**-**	**-**	**-**	**Aaa**	**-**	**-**	**AAA**	**-**
DnB Bank	-	-	-	-	A1	P-1	C-	A+	A-1
Singapore	**AAA**	**-**	**-**	**-**	**Aaa**	**-**	**-**	**AAA**	**-**
DBS Bank Ltd	AA-	F1+	aa-	1	Aa1	P-1	B	AA-	A-1+
Oversea Chinese Banking Corporation Ltd	AA-	F1+	aa-	1	Aa1	P-1	B	AA-	A-1+
United Overseas Bank Ltd	AA-	F1+	aa-	1	Aa1	P-1	B	AA-	A-1+
Sweden	**AAA**	**-**	**-**	**-**	**Aaa**	**-**	**-**	**AAA**	**-**
Nordea Bank AB	AA-	F1+	aa-	1	Aa3	P-1	C	AA-	A-1+
Skandinaviska Enskilda Banken AB	A+	F1	a+	1	A1	P-1	C-	A+	A-1
Swedbank AB	A+	F1	a+	1	A1	P-1	C-	A+	A-1
Svenska Handelsbanken AB	AA-	F1+	aa-	1	Aa3	P-1	C	AA-	A-1+
Switzerland	**AAA**	**-**	**-**	**-**	**Aaa**	**-**	**-**	**AAA**	**-**
Credit Suisse AG	A	F1	a	1	A1	P-1	C-	A	A-1
UBS AG	A	F1	a	1	A2	P-1	C-	A	A-1

Appendix 4: Glossary of Investments Instruments

Certificates of Deposits	A certificate of deposit (CD) is a time deposit, a financial product. CDs are similar to savings accounts in that they are insured and thus virtually risk free; they are "money in the bank." They are different from savings accounts in that the CD has a specific, fixed term (often monthly, three months, six months, or one to five years) and, usually, a fixed interest rate. It is intended that the CD be held until maturity, at which time the money may be withdrawn together with the accrued interest.
Commercial paper	Commercial paper is a money-market security issued (sold) by large corporations to obtain funds to meet short-term debt obligations (for example, payroll), and is backed only by an issuing bank or corporation's promise to pay the face amount on the maturity date specified on the note. Since it is not backed by collateral, only firms with excellent credit ratings from a recognized credit rating agency will be able to sell their commercial paper at a reasonable price. Commercial paper is usually sold at a discount from face value, and carries higher interest repayment rates than bonds
Corporate bonds	A corporate bond is a bond issued by a corporation. It is a bond that a corporation issues to raise money effectively in order to expand its business.[1] The term is usually applied to longer-term debt instruments, generally with a maturity date falling at least a year after their issue date.
Gilt	Gilt-edged securities are bonds issued by certain national governments. The term is of British origin, and originally referred to the debt securities issued by the Bank of England, which had a gilt (or gilded) edge. Hence, they are known as gilt-edged securities, or gilts for short. Today the term is used in the United Kingdom as well as some Commonwealth nations, such as South Africa and India. However, when reference is made to "gilts", what is generally meant is "UK gilts," unless otherwise specified.
Supranational bonds	Supranational bonds are issued by institutions that represent a number of countries, not just one. Thus, organisations that issue such bonds tend to be the World Bank or the European Investment Bank. The issuance of these bonds are for the purpose of promoting economic development
Treasury bills (or T-bills)	Treasury bills (or T-bills) mature in one year or less. Like zero-coupon bonds, they do not pay interest prior to maturity; instead they are sold at a discount of the par value to create a positive yield to maturity. Many regard Treasury bills as the least risky investment available.