Annex A

Working Document

Treasury Management Strategy Statement

Minimum Revenue Provision Policy Statement and
Annual Investment Strategy

London Borough of Tower Hamlets
2017/18

1. **BACKGROUND**

1.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part 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, providing adequate liquidity primarily before considering investment return.

1.2 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, essentially the 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.

1.3 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."

1.4 **REPORTING REQUIREMENTS** -The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

I. **An annual treasury management strategy statement** (this report) – it covers:
   - a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);
   - the capital plans (including prudential indicators);
   - the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
   - an investment strategy (the parameters on how investments are to be managed).

II. **A mid year treasury management report** – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether any policies require revision.

III. **A treasury outturn report** – This provides details of annual actual prudential and treasury indicators and annual actual treasury operations compared to the annual estimates within the strategy.

1.5 **SCRUTINY** - The above reports are required to be adequately scrutinised before being recommended to the Council. This role is being undertaken by the Auditee Committee and or Cabinet.

1.6 **Treasury management consultants** - The Council uses Capita Asset Services, Treasury solutions as its external treasury management advisors. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and officers will ensure that undue reliance is not placed upon the external service providers.

1.7 **Training** - The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsibe for scrutiny. Training will be arranged as required. The training needs of treasury management officers are periodically reviewed.

1.8 **TREASURY MANAGEMENT STRATEGY FOR 2017/18**

The strategy for 2017/18 covers two main areas:

Capital issues

- the minimum revenue provision (MRP) policy;
- the capital plans and the prudential indicators.

Treasury management issues

- prospects for interest rates;
- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Council;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy;
- service/policy investments.

1.9 These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, CLG MRP Guidance, the CIPFA Treasury Management Code and CLG Investment Guidance.

2. MINIMUM REVENUE PROVISION (MRP) POLICY STATEMENT

2.1 The Council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the minimum revenue provision - MRP).

2.2 The Department of Communities and Local Government (DCLG) require Councils to establish a policy statement on the MRP and has published guidance on the four potential methodologies to be adopted.

2.3 The guidance distinguishes between supported borrowing which relates to assumed borrowing which is incorporated into the Government's Formula Grant calculation and consequently has an associated amount of government grant and unsupported borrowing. Unsupported borrowing is essentially prudential borrowing the financing costs of which have to be met by the Council locally.

2.4 There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made pending finalisation of transitional arrangements following introduction of Self-Financing.

2.5 The DCLG guidance provides two options for the calculation of the MRP associated with each classes of borrowing.

2.6 The two options for the supported borrowing are variants of the existing statutory calculation which is based on 4% of the aggregate assumed borrowing for general fund capital investment - termed the Capital Financing requirement (CFR). The two options are:

- **Option 1** (Regulatory Method): To continue the current statutory calculation based on the gross CFR less a dampening factor to mitigate the impact on revenue budgets of the transition from the previous system. This calculation is further adjusted to repay debt transferred to the Council when the Inner London Education Authority (ILEA) was abolished.
- **Option 2** (Capital Financing Requirement Method): The statutory calculation without the dampener which will increase the annual charge to revenue budget.

2.7 The options purely relate to the timing of debt repayment rather than the gross amounts payable over the term of the loans. The higher MRP payable under option 2 will accelerate the repayment of debt.

2.8 It is recommended that because of budget constraints in the medium term the existing statutory calculation with the ILEA adjustment be adopted as the basis of the Councils MRP relating to supported borrowing.

2.9 The guidance provides two options for the MRP relating to unsupported borrowing. The options are:-

- **Option 3** (Asset Life Method): To repay the borrowing over the estimated life of the asset with the provision calculated on either an equal instalment or annuity basis. This method has the advantage of simplicity and relating repayments to the period over which the asset is providing benefit.
- **Option 4** (Depreciation Method): A calculation based on depreciation. This is extremely complex and there are potential difficulties in changing estimated life and residual values.

2.10 It is recommended that option 3 is adopted for unsupported borrowing.

2.11 The Council is required under regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 to determine for each financial year an amount of minimum revenue provision which it considers to be prudent.

2.12 **It is proposed that the Council makes Minimum Revenue Provision using Option 1 (Regulatory Method) for supported borrowing and Option 3 (Asset Life Method) for unsupported borrowing.**

THE CAPITAL PRUDENTIAL INDICATORS 2017/18 – 2019/20

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

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

Capital expenditure £m	2015/16 Actual	2016/17 Revised Estimate	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Adults' Services	0.202	7.442	7.018	1.591	0.000
Children's Services	13.893	17.749	28.259	25.445	17.250
Communities, Localities & Culture	6.673	8.691	20.054	12.883	16.393
Building Schools for the Future	(0.058)	0.290	0.977	0.000	0.000
Development & Renewal (Non Housing)	2.328	3.310	4.778	0.321	0.000
Corporate	2.393	7.783	11.335	15.000	0.000
Housing – Non HRA	1.189	1.307	1.757	1.757	1.257
Total Non-HRA	**26.620**	**46.572**	**74.178**	**56.997**	**34.900**
Housing - HRA	66.359	89.345	77.720	83.444	0.000
Total HRA	**66.359**	**89.345**	**77.720**	**83.444**	**0.000**
Total	**92.979**	**135.917**	**151.898**	**140.441**	**34.900**

3.3 **Other long term liabilities** - The above financing need excludes other long term liabilities, such as PFI and leasing arrangements which already include borrowing instruments.

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

Capital expenditure £m	2015/16Actual	2016/17 Revised Estimate	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Non-HRA	26.620	46.572	74.178	56.997	34.900

HRA	66.359	89.345	77.720	83.444	0.000
Total	**92.979**	**135.917**	**151.898**	**140.441**	**34.900**
Capital expenditure £m	**2015/16 Actual**	**2016/17 Revised Estimate**	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**
Financed by:					
Grant	(50.986)	(23.619)	(32.480)	(22.680)	(28.150)
Major Repairs Allowance	(28.319)	(40.161)	0.000	0.000	0.000
Schools Contribution	0.000	(0.969)	(1.192)	0.000	0.000
Capital Receipts	(0.841)	(23.321)	(21.150)	(15.568)	0.000
S106 (Developers Contributions)	(6.087)	(16.943)	(35.812)	(26.817)	0.000
Direct Revenue Financing	(6.600)	(20.312)	(56.943)	(0.750)	0.000
Total Financed	**(92.833)**	**(125.325)**	**(147.577)**	**(65.815)**	**(28.150)**
Prudential Borrowing	**0.145**	**10.592**	**4.321**	**74.626**	**6.750**

3.5 **The Council's borrowing need (the Capital Financing Requirement)** - The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR. The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with each asset's life.

The Council is asked to approve the CFR projections below:

£m	**2015/16 Actual**	**2016/17 Revised Estimate**	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**
Capital Financing Requirement					
CFR – housing	75.583	83.266	83.533	148.858	146.309
CFR – non housing	187.005	181.143	176.459	177.063	177.699
Total CFR	**262.588**	264.408	**259.993**	**325.921**	**324.008**
Movement in CFR		**1.820**	**(4.416)**	**65.929**	**(1.914)**

Movement in CFR represented by					
Net financing need for the year (above)	0.145	10.592	4.321	74.626	6.750
Less MRP/VRP and other financing movements	(0.145)	(8.772)	(8.737)	(8.697)	(8.664)
Movement in CFR	**0.000**	**1.820**	**(4.416)**	**65.929**	**(1.914)**

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

3.7 The Council has set the following **affordability prudential indicators** as prescribed by the code and these are set out below and detailed in Appendix 1.

3.8 **Ratio of financing costs to net revenue stream -** 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. The estimates of financing costs include current commitments and the proposals in this budget report.

	2015/16 Actual	2016/17 Revised Estimate	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Non-HRA	0.84%	0.82%	0.79%	0.92%	1.02%
HRA	4.02%	5.23%	6.12%	10.30%	10.77%

3.9 **Incremental impact of capital investment decisions on council tax** - This indicator identifies the revenue costs associated with proposed changes to the three year capital programme recommended in this budget report compared to the Council's existing approved commitments and current plans. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which are not published over a three year period.

£	2015/16 Actual	2016/17 Revised Estimate	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Council Tax - Band D (per annum)	24.055	29.224	32.537	31.224	30.074

3.10 **Estimates of the incremental impact of capital investment decisions on housing rent levels** - Similar to the Council tax calculation, this indicator identifies the trend in the cost of proposed changes in the housing capital programme recommended in this budget report compared to the Council's existing commitments and current plans, expressed as a discrete impact on weekly rent levels. This indicator shows the revenue impact on any newly proposed changes, although any discrete impact will be constrained by rent controls.

£	2015/16 Actual	2016/17 Revised Estimate	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Weekly housing rent levels	0.00	2.123	1.458	6.397	0.923

4. PROSPECTS FOR INTEREST RATES

4.1 The borrowing and investment strategy is in part determined by the economic environment within which it operates. The treasury advisor to the Council is Capita Asset Services and part of their service is to assist the Council to formulate a view on interest rates. The following table gives Capita's overall view on interest rates for the next three years.

Annual Average %	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)			
		5 year	10 Year	25 year	50 year
Dec 2016	0.25	1.60	2.30	2.90	2.70
Mar 2017	0.25	1.60	2.30	2.90	2.70
Jun 2017	0.25	1.60	2.30	2.90	2.70
Sep 2017	0.25	1.60	2.30	2.90	2.70
Dec 2017	0.25	1.60	2.30	3.00	2.80
Mar 2018	0.25	1.70	2.30	3.00	2.80
Jun 2018	0.25	1.70	2.40	3.00	2.80
Sep 2018	0.25	1.70	2.40	3.10	2.90
Dec 2018	0.25	1.80	2.40	3.10	2.90
Mar 2019	0.25	1.80	2.50	3.20	3.00
Jun 2019	0.50	1.90	2.50	3.20	3.00
Sep 2019	0.50	1.90	2.60	3.30	3.10
Dec 2019	0.75	2.00	2.60	3.30	3.10
Mar 2020	0.75	2.00	2.70	3.40	3.20

4.2 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.

4.3 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.

4.4 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.

4.5 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.

4.6 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.

4.7 The latest MPC decision included a forward view that Bank Rate could go either up or down depending on how economic data evolves in the coming months. The 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, the Council’s treasury adviser would not, as yet, discount the risk of a cut in Bank Rate if economic growth were to take a significant dip downwards, though they think this is unlikely. They 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 their forecasts.

4.8 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.

4.9 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 3.2% in 2018). This increase was largely due to the effect of the sharp fall in the value of sterling since the referendum, (16% down against the US dollar and 11% down against the Euro); this 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.

4.10 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 for October surprised by under shooting forecasts at 0.9%. However, producer output prices rose at 2.1% and core inflation was up at 1.4%, confirming the likely future upwards path.

4.11 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 have hit a peak on the way up again of 1.46% on 14 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.

4.12 Employment has been growing steadily during 2016, despite initial expectations that the referendum would cause a fall in employment. However, the latest employment data in November, (for October), showed a distinct slowdown in the rate of employment growth and an increase in the rate of growth of the unemployment claimant count. House prices have been rising during 2016 at a modest pace but the pace of increase has been slowing since the referendum; a downturn in prices could dampen consumer confidence and expenditure.

4.13 The American economy had a patchy 2015 with sharp swings in the growth rate leaving the overall growth for the year at 2.4%. Quarter 1 of 2016 disappointed at +0.8% on an annualised basis while quarter 2 improved, but only to a lacklustre +1.4%. However, forward indicators are pointing towards a pickup in growth in the rest of 2016. 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 which is now strongly expected in December 2016.

4.14 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 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 from around zero towards the target of 2%. GDP growth rose by 0.6% in quarter 1 2016 (1.7% y/y) but slowed to +0.3% (+1.6% y/y) in quarter 2. This has added to comments from many forecasters that central banks around the world are running out of ammunition to stimulate economic growth and to boost inflation. They stress that national governments will need to do more by way of structural reforms, fiscal measures and direct investment expenditure to support demand in the their economies and economic growth.

4.15 Japan is still bogged down in anaemic growth and making little progress on fundamental reform of the economy while Chinese economic growth has been weakening and medium term risks have been increasing.

4.16 In conclusion investment returns are likely to remain low during 2017/18 and beyond;

a) 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.

b) 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, we need to carefully review this to avoid incurring higher borrowing costs in later times when the Council will not be able to avoid new borrowing to finance capital expenditure and/or to refinance maturing debt;

c) There still 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.

5. TREASURY MANAGEMENT CONSIDERATIONS AND DEVELOPMENT

5.1 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 this service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The Council anticipates its fund balances in 2017/18 to average around £350m, if we persist with the policy of internal borrowing to fund the Council's underlying need to borrow.

5.2 The Pension Fund surplus cash will continue to be invested in accordance with the Council's Treasury Management Strategy agreed by Full Council, under the delegated authority of the Corporate Director Resources to manage within agreed parameters.

5.3 The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

5.4 **Core funds and expected investment balances** – The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales, etc.).

Detailed below are estimates of the year end balances of investments.

Year End Resources	2015/16 Actual	2016/17 Projected Outturn	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Expected Investments	£381.4m	£400m	£350m	£300m	£300m

5.5 **Current portfolio position** - The Council's treasury portfolio position at 31 March 2016, with forward projections are summarised below. The table shows the actual external debt (the treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

£m	2015/16 Actual	2016/17 Projected Outturn	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
External Debt					
Debt at 1 April	87.825	85.936	94.888	98.206	161.236
Expected change in Debt	(0.842)	(1.889)	(1.639)	(1.004)	(1.004)
New borrowing		10.592	4.321	74.626	6.750
Other long-term liabilities (OLTL)	38.472	37.509	36.304	34.957	33.415
Expected change in OLTL	(0.963)	(1.205)	(1.347)	(1.542)	(1.931)
Actual gross debt (Inc. PFI) at 31 March	**124.492**	**130.943**	**132.527**	**205.243**	**198.466**
The Capital Financing Requirement (Inc. PFI)	**262.588**	**264.408**	**259.993**	**325.921**	**324.008**
Under / (over) borrowing	***138.096***	***133.465***	***127.466***	***120.678***	***125.541***

5.6 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 is that the Council needs to ensure that its gross debt 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 2016/17 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

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

5.8 **Treasury Indicators: limits to borrowing activity for 2016-17 to 2019-20** Treasury indicators are about setting parameters within which within which officers can take treasury management decisions. The Council has set the following treasury indicators as prescribed by the Code and these are set out below and also detailed in Appendix 1:

- **Authorised Limit for External Debt** – The upper limit on the level of gross external debt permitted. It must not be breached without Full Council approval.

The Council is asked to approve the following authorised limit:

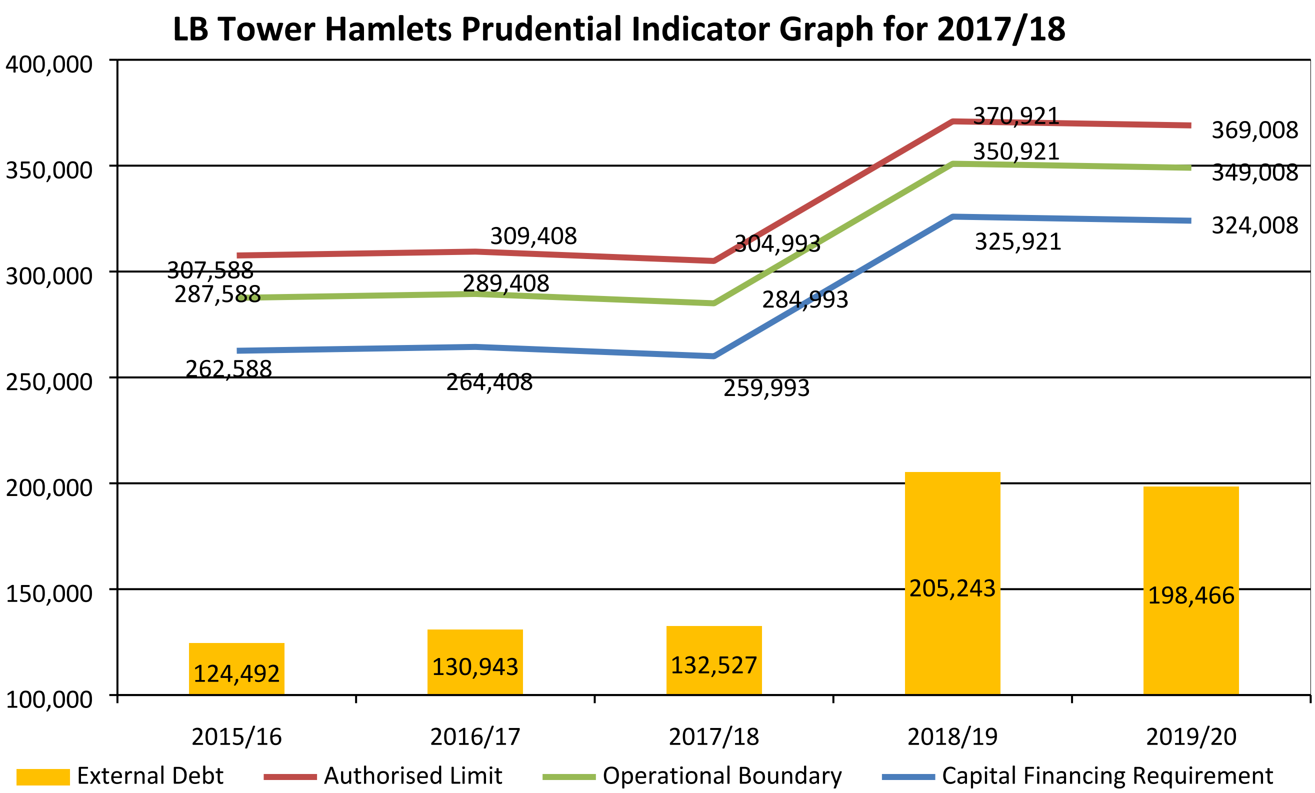
Authorised limit £m	2016/17 Projected Outturn	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Borrowing & OLTL	289.408	284.993	350.921	349.008
Headroom	20.000	20.000	20.000	20.000
Total	**309.408**	**304.993**	**370.921**	**369.008**

- **Operational Boundary for External Debt** – Most likely and prudent view on the level of gross external debt requirement. Debt includes external borrowings and other long term liabilities.

Operational Boundary £m	2016/17 Projected Outturn	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
Debt	251.899	248.689	315.964	315.593
Other long term liabilities	37.509	36.304	34.957	33.415
Total	**289.408**	**284.993**	**350.921**	**349.008**

- **HRA Debt Limit** – The HRA Self Financing regime came into effect on 1 April 2012. The new regime imposes a maximum HRA CFR on the Council. For this Council this has been set at £184m following repayment of HRA debt totalling £236.2m by the Government as part of debt settlement that preceded the implementation of the HRA Self Financing regime. In 2014, as part of the Local Growth Fund LBTH was awarded £8.225m of additional HRA borrowing capacity, so in effect the HRA debt cap is currently £192m.

HRA Debt Limit £m	2016/17 Projected Outturn	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate
HRA debt cap	192.000	192.000	192.000	192.000
HRA CFR	83.266	83.533	148.858	146.309
HRA Headroom	**108.734**	**108.467**	**43.142**	**45.691**



Investment returns expectations

5.9 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).

5.10 Policy Rate is forecast to remain flat at 0.25% until quarter 2 of 2019. Bank Rate forecasts for financial year ends (March) are:

- 2017/18 0.25%
- 2018/19 0.25%
- 2019/20 0.50%

5.11 There are downside risks to these forecasts (i.e. further reduction in Bank Rate) if economic growth weakens. However, 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.

5.12 Stated below are the estimated average investment earnings rates for investments placed during each financial year for the next three years:

- 2016/17 0.65%
- 2017/18 0.45%
- 2018/19 0.40%
- 2019/20 0.50%

5.13 **Investment treasury indicator and limit** - total principal funds invested for greater than 1 year. 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.

5.14 **Investments Longer than a Year:** The Code of Practice requires the Council to give consideration to longer-term investment and set an upper limit for principal sums to be invested for longer than one year. The Council currently has £50m limit for investments invested for longer than one year.

5.15 Therefore taking all of the abovementioned into consideration, in order for the Council to have flexibility in investing in high quality counterparties, such as the UK Government, it is recommended that the Council set an upper limit for principal sums to be invested for longer than one year at £100 million for 2017/18, £100 million for 2018/19, £100 million for 2019/20 and £100m for 2020/21.

The Council is asked to approve the treasury indicator and limit: -

Maximum principal sums invested > 1 year					
£m	**2016/17**	**2017/18**	**2018/19**	**2019/20**	**2020/21**
Principal sums invested > 1 year	£50m	£100m	£100m	£100m	£100m

5.16 For its cash flow generated balances, the Council will seek to utilise money market funds and short-dated deposits (overnight to100 days),such as its Santander 95 days call account in order to benefit from the compounding of interest.

5.17 **Provision for Credit-related Losses** - If any of the Council's investments appear at risk of loss due to default, provision would need to be made from revenue for the appropriate amount. The Council has no exposure to any banking failure.

6. BORROWING STRATEGY

6.1 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 with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is relatively high.

6.2 Against this background and the risks within the economic forecast, caution will be adopted with the 2017/18 treasury operations. The Corporate Director Reources 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 a greater than expected increase in the anticipated rate to US tapering of asset purchases, or in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are still lower than they will be in the next few years.

6.3 Any decisions will be reported to the Cabinet and the full Council at the next available opportunity.

6.4 The Council's borrowing strategy will give consideration to new borrowing in the following order of priority: -

- The cheapest borrowing will be internal borrowing by running down cash balances and foregoing interest earned at historically low rates. However, in view of the overall forecast for long term borrowing rates to increase over the next few years, consideration will also be given to weighing the short term advantage of internal borrowing against potential long term costs if the opportunity is missed for taking loans at long term rates which will be higher in future years.
- Temporary borrowing from the money markets or other local authorities
- PWLB variable rate loans for up to 10 years
- Short dated borrowing from non PWLB below sources
- Long term fixed rate market loans at rates significantly below PWLB rates for the equivalent maturity period (where available) and to maintaining an appropriate balance between PWLB and market debt in the debt portfolio.
- PWLB borrowing for periods under 10 years where rates are expected to be significantly lower than rates for longer periods. This offers a range of options for new borrowing which will spread debt maturities away from a concentration in longer dated debt

6.5 The Council will continue to borrow in respect of the following:

- Maturing debt (net of minimum revenue provision).

- Approved unsupported (prudential) capital expenditure.
- To finance cash flow in the short term.

6.6 The type, period, rate and timing of new borrowing will be determined by the Corporate Director Resources under delegated powers, taking into account the following factors:

- Expected movements in interest rates as outlined above.
- Current maturity profile.
- The impact on the medium term financial strategy.
- Prudential indicators and limits.

6.7 **Treasury management limits on borrowing activity** - There are three debt related treasury activity limits. The purpose of these are 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:

- **Upper limits on variable interest rate exposure** - This identifies a maximum limit for variable interest rates based upon the debt position net of investments
- **Upper limits on fixed interest rate exposure** - This is similar to the previous indicator and covers a maximum limit on fixed interest rates;
- **Maturity structure of borrowing** - These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

The Council is asked to approve the following treasury indicators and limits:

	2017/18	2018/19	2019/20
Interest rate exposures			
	Upper %	**Upper %**	**Upper %**
Limits on fixed interest rates based on net debt	100	100	100
Limits on variable interest rates based on net debt	75	75	75
Limits on fixed interest rates:			
• ***Debt only***	*100*	*100*	*100*
• ***Investments only***	*100*	*100*	*100*
Limits on variable interest rates			
• ***Debt only***	*90*	*90*	*90*
• ***Investments only***	*50*	*50*	*50*

Maturity structure of fixed interest rate borrowing 2017/18		
	Lower	**Upper**
Under 12 months	0%	10%
12 months to 2 years	0%	30%
2 years to 5 years	0%	40%
5 years to 10 years	0%	80%

10 years and above	0%	100%
Maturity structure of variable interest rate borrowing 2017/18		
	Lower	**Upper**
Under 12 months	0%	100%
12 months to 2 years	0%	100%
2 years to 5 years	0%	100%
5 years to 10 years	0%	100%
10 years and above	0%	100%

6.8 **Policy on borrowing in advance of need** - The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. 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.

6.9 Borrowing in advance will be made within the constraints that:

- It will be limited to no more than 75% of the expected increase in borrowing need (CFR) over the three year planning period; and
- Would not look to borrow more than 18 months in advance of need.

6.10 Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual outturn reporting mechanism.

6.11 **Debt rescheduling** - 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 the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

6.12 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).

6.13 Consideration will also be given to identify if there is any residual 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.

6.14 All rescheduling will be reported to the Cabinet and Council, at the earliest meeting following its implementation.

7. ANNUAL INVESTMENT STRATEGY

7.1 **Investment policy -** The Council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second, then return.

7.2 In order to minimise the risk to investments, the Council applies minimum acceptable credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk.

7.3 Ratings will not be the sole determinant of the quality of an institution as 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 of the markets. 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.

7.4 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 potential investment counterparties.

7.5 Investment instruments identified for use in the financial year are listed in section 7.15 and 7.16-7.21, under the 'specified' and 'non-specified' investments categories.

7.6 **In summary –** considering the factors set out in Paragraphs 4-7, the recommended Investment Strategy is that:

I. The cash balances, not immediately required to finance expenditure, are lent to the money market for the most appropriate periods as indicated by the cash flow model and current market and economic conditions;
II. Liquidity is maintained by the use of overnight deposits, MMF and call accounts;
III. The minimum amount of short-term cash balances required to support monthly cash flow management is £75 million;
IV. The upper limit for investments longer than one year is £100 million;
V. The maximum period for longer term lending is 5 years;
VI. All investment with institutions and investment schemes is undertaken in accordance with the Council's creditworthiness criteria as set out at section 7;
VII. More cautious investment criteria are maintained during times of market uncertainty;
VIII. All investment with institutions and investment schemes is limited to the types of investment set out under the Council's approved "Specified" and "Non-Specified" Investments detailed at section 7, and that professional advice continues to be sought where appropriate;
IX. All investment is managed within the Council's approved investment/asset class limits.

Creditworthiness Policy

7.7 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. This is set out in the specified and non-specified 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.

7.8 The Corporate Director Resources 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. These criteria are separate to that which determines which types of investment instrument are either specified or non-specified as it provides an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

7.9 The minimum rating criteria uses the lowest common denominator method of selecting counterparties and applying limits. This means that the application of the Council's minimum criteria will apply to the lowest available rating for any institution. For instance, if an institution is rated by two agencies, one meets the Council's criteria, the other does not, and consequently this institution will fall outside the Council's lending criteria.

7.10 Credit rating information is supplied by Capita Asset Services, the Council 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. 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. This does not apply to the unrated building societies or banks whereby they are selected based on enhanced credit analysis.

7.11 The criteria for providing a pool of high quality investment counterparties (both specified and non-specified investments) are:

1) Banks with good credit quality **–** the Council will only use banks which:

    i. are UK banks; and/or

    ii. are non-UK and domiciled in a country which has a minimum sovereign Long Term rating of AAA

    And have, as a minimum, the following Fitch, Moody's and Standard and Poor's credit ratings (where rated):

    i. Short Term – 'F1'

    ii. Long Term – 'A-'

(N.B. Viability, Financial Strength and Support ratings have been removed and will not be considered in choosing counterparties.)

2) Part nationalised UK banks – Lloyds Banking Group and Royal Bank of Scotland. These banks can be included if they continue to be part nationalised or they meet the ratings in Bank above.

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.

4) 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.

5) Unrated/Challengers Banks – The Council will use unrated banks with assets in excess of £1.5bn. When investing with such institution, the Council will carry out an enhanced credit analysis in understanding the institution, its financials and credit capabilities.

    I. The "RAG" framework will be used for Building societies as well as Banks, for the Council to evaluate and compare security and liquidity of investment opportunities.
    II. The "RAG" (Red, Amber or Green) indicator framework is generally used to identify the strength of a company's financial numbers.
    III. For example, all the financials there will be pre-set categories which will classify institutions outcomes as Red, Amber or Green. These pre-set categories are industry dependent; e.g. a retail company is expected to generate higher cash flow than a bank.

6) Building societies - The Council will use all building societies in the UK which:

    iii. Meet the ratings for banks outlined above;

    iv. Have assets in excess of £1.5bn;

    or meet both criteria.

7) Money Market Funds (MMF) – AAA

8) Enhanced Money Market Funds (EMMFs) – AAA

9) Certificates of Deposits (CDs)

10) Corporate Bonds

11) Covered Bonds

12) Property Funds

13) Equity Funds

14) UK Government (including gilts, treasury bills and the Debt management Account Deposit Facility, (DMADF))

15) Local authorities, parish councils, Police and Fire Authorities

16) Supranational institutions

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

Agency	Long-Term	Short-Term
Fitch	A-	F1
Moody's	A3	P-1
Standard & Poor's	A-	A-1
Sovereign Rating	AAA	
Money Market Fund	AAA	

7.13 **Country and Product considerations** - Due care will be taken to consider the country, group and sector exposure of the Council's investments. In part, the country selection will be chosen by the credit rating of the sovereign state in Banks above. In addition:

- No more than a maximum amount of £75m or 25% of the investments portfolio will be placed with any individual non-UK country with AAA sovereign rating at any time;
- limits in place above will apply to a group of institutions within a non UK country;
- Product limits will be monitored regularly for appropriateness.

7.14 **Use of additional information other than credit ratings –** Additional requirements under the Code requires 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 are for example Credit Default Swaps, negative rating watches/outlooks, these will be applied to compare the relative security of differing investment counterparties.

Time and monetary limits applying to investments

7.15 **Specified Investments:** It is recommended that the Council should make Specified investment as detailed below, 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 A- long-term credit rating or equivalent Moody's or Standard and Poor's rating.

Specified Investments	**Fitch Long term Rating (or equivalent)**	**Money Limit**	**Time Limit**
Term Deposits (Banks - higher quality)	*Short-term F1+,* *Long-term AA*	£30m	1 year
Term Deposits (Banks – medium (high) quality)	*Short-term F1,* *Long-term A+*	£25m	1 year
Term Deposits (Banks – medium (low) quality)	*Short-term F1,* *Long-term A*	£20m	1 year
Term Deposits (Banks - lower quality)	*Short-term F1,* *Long-term A-*	£10m	6 months
Banks - part nationalised (per group)	N/A	£70m	1 year
Council's banker (not meeting lending criteria)	XXX	£25m	1 day
DMADF	N/A	unlimited	6 months
Local authorities	N/A	£20m	1 year
Treasury Bills	Long Term AAA	No Limit	1 year
UK Government Gilts	N/A	No Limit	1 year
Covered Bonds	Long Term AAA	£25m	1 year
Non-UK Government Bonds	Sovereign AAA Long Term AAA	£25m	1 year
Certificates of Deposits	As Term Deposits above	As Term Deposits above	As Term Deposits above
Corporate Bond Funds	As Term Deposits above	As Term Deposits above	As Term Deposits above
Collective Investment Schemes structured as Open Ended Investment Companies (OEICs)			
	Fund rating	**Money Limit (per fund)**	**Time Limit**
Money market funds (Sterling)	AAA	£25m	liquid
Enhanced Cash Funds	AAA/V1	£20m	liquid
Cash Funds	AAA	£20m	liquid
Bond Funds	AAA	£20m	liquid

<u>Non-Specified Investments:</u>

7.16 All investments that do not qualify as specified investments are termed non-specified investments. The table below details the total percentage of the Annual Principal Sums that can be Invested for more than 1 year and can be held in each category of investment, for example 100% of the Principal Sums limit can be held with the UK Government at any one time.

7.17 **Unrated banks, building societies and other institutions** are classed as non-specified investments irrespective of the investment period. When investing with this institution, the Council will carry out an enhanced credit analysis in understanding the institution, its financials and credit capabilities.

7.18 The "RAG" (Red, Amber or Green) framework will be used by the Council to evaluate and compare the security and liquidity elements of investment opportunities with unrated institutions as deemed appropriate.

7.19 The "RAG" indicator framework is generally used to identify the strength of a company's financial numbers. For example, all for the financial sector there will be pre-set categories which will classify institutions outcomes as Red, Amber or Green. These pre-set categories are industry dependent; e.g. a retail company is expected to generate higher cash flow than a bank.

In assessing investment opportunities with unrated UK Banks, Building Societies and other Institutions the Council will look at the following metrics:

Ratio	Red	Amber	Green
Total Debt / Equity	<5	5-10	>10
Net Interest Margin	<0	0-1.5	>1.5
CET1 Ratio	<9	9-13%	>13%
Capital Adequacy Ratio	<0	10-12%	>12%
Total Capital Ratio	<8	8-14%	>14%

Ratio	Red	Amber	Green
Tangible Equity Ratio	<3	3-5	>5
Loan to Deposit Ratio	>110	100-110	<100
Non-performing loan Ratio	>5	2-5	<2
Return on Equity	<0%	0-10%	>10%
Dividend yield	0-8%	8-12%	>12%
P/E Ratio	<0	0-10	>10%

7.20 Whilst the Council look for as many 'greens' as possible, a balance of ratios that indicate long-term solvency and ability for the institution to service and repay debts is most important.

Minimum Criteria for considering Unrated Institutions with money and time limits:

	Institution Assets Value	Money Limit	Time Limit
Unrated UK Building Societies & Challenger Banks with assets in excess of:	£1.5bn £2.0bn	£3m £5m	6 months 12 months

7.21 It is considered that the maximum nominal value of overall investments that the Council should hold for more than one year and less than 5 years is £100m. (Investments with maturity over one year) **The prudential indicator figure of £100m is therefore recommended.**

The credit criteria for non-specified investments are detailed in the table below:

Non-Specified Investments	Fitch Long term Rating (or Equivalent)	Time Limit	Monetary Limit
Term deposits – Banks and Building Societies	Short-term F1+, Long-term AA-	5 years	£25m
Structured Deposits: Fixed term deposits with variable rate and variable maturities	Short-term F1+, Long-term AA-	5 years	£25m
Part Nationalised or Wholly Owned UK Banks	N/A	5 years	£25m
Certificates of Deposits	Short-term F1+, Long-term AA-	5 years	£25m
Corporate Bonds	Short-term F1+, Long-term AA-	5 years	£25m
Covered Bonds	Long Term AAA	5 years	£25m
Equity Funds	N/A	5 years	£25m
Property Funds	N/A	5 years	£25m
UK Government Gilts	N/A	5 years	100% of Investment Portfolio

The Council is asked to approved the above criteria for specified and all non-specified investments.

7.22 Country limits - The Council has determined that it will only use approved counterparties from non UK countries with a minimum sovereign credit rating of AAA from Fitch (or equivalent). A counterparty list will be compiled based on this sovereign rating of AAA and in accordance with the Council's minimum credit rating criteria policy for institutions and qualified institutions will be added to this list, and unqualified institutions will be removed from the list, by officers as deemed appropriate. Please see Appendix 3 for qualified countries and their institutions as of 03/01/2017.

APPENDICES

Appendix 1 – Prudential and Treasury Indicators

Appendix 2 – Definition of Credit Ratings

Appendix 3 – Counter Party Credit Rating List

Appendix 4 – Treasury Management Policy Statement

Appendix 5 – Treasury Management Scheme of Delegation

Appendix 6 – Treasury Management Reporting Arrangement

Appendix 7 - Glossary

Local Government Act, 1972 Section 100D (As amended)

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.**
	Bola Tobun, x4733, Mulberry Place

APPENDIX 1

PRUDENTIAL AND TREASURY MANAGEMENT INDICATORS FOR 2017/18

Prudential Indicators	**2015/16**	**2016/17**	**2016/17**	**2017/18**	**2018/19**	**2019/20**
Extract from Estimate and rent setting reports	**Actual**	**Original Estimate**	**Projected Outturn**	**Estimate**	**Estimate**	**Estimate**
	£m	£m	£m	£m	£m	£m
Capital Expenditure						
Non – HRA	26.620	89.475	46.572	74.178	56.997	34.900
HRA	66.359	138.315	89.345	77.720	83.444	0.000
TOTAL	**92.979**	**227.790**	**135.917**	**151.898**	**140.441**	**34.900**
Ratio of Financing Costs to Net Revenue Stream						
Non – HRA	0.84%	1.09%	0.82%	0.79%	0.92%	1.02%
HRA	4.02%	5.94%	5.23%	6.12%	10.30%	10.77%
	£m	£m	£m	£m	£m	£m
Gross Debt and Capital Financing Requirement						
Gross Debt	124.492	133.361	130.943	132.527	205.243	198.466
Capital Financing Requirement	262.588	287.173	264.408	259.993	325.921	324.008
Over/(Under) Borrowing	(138.096)	(153.812)	(133.465)	(127.466)	(120.678)	(125.541)
In Year Capital Financing Requirement						
HRA	5.908		0.355	1.500	6.750	6.750
Non – HRA	(6.980)	21.804	10.237	2.821	67.876	0.000
TOTAL	**(1.072)**	**21.804**	**10.592**	**4.321**	**74.626**	**6.750**
Capital Financing Requirement as at 31 March						
Non - HRA	187.005	192.310	181.143	176.459	177.063	177.699
HRA	75.583	94.864	83.266	83.533	148.858	146.309
TOTAL	**262.588**	**287.173**	**264.408**	**259.993**	**325.921**	**324.008**
Incremental Impact of Financing Costs (£)						
Increase in Council Tax (band D) per annum	24.055	24.458	29.224	32.537	31.224	30.074
Increase in average housing rent per week	5.615	2.855	2.123	1.458	6.397	0.923

Treasury Management Indicators	2015/16	2016/17	2016/17	2017/18	2018/19	2019/20
	Actual	Original Estimate	Projected Outturn	Estimate	Estimate	Estimate
	£m	£m	£m	£m	£m	£m
Authorised Limit For External Debt -						
Borrowing & Other long term liabilities	287.588	312.173	289.408	284.993	350.921	349.008
Headroom	20.000	20.000	20.000	20.000	20.000	20.000
TOTAL	**307.588**	**332.173**	**309.408**	**304.993**	**370.921**	**369.008**
Operational Boundary For External Debt -						
Borrowing	87.825	274.664	251.899	248.689	315.964	315.593
Other long term liabilities	38.472	37.509	37.509	36.304	34.957	33.415
TOTAL	**126.297**	**312.173**	**289.408**	**284.993**	**350.921**	**349.008**
Gross Borrowing	**124.492**	**133.361**	**130.943**	**132.527**	**205.243**	**198.466**
HRA Debt Limit*	**184.381**	**192.000**	**192.000**	**192.000**	**192.000**	**192.000**
Upper Limit For Fixed Interest Rate Exposure						
Net principal re fixed rate borrowing / investments	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**
Upper Limit For Variable Rate Exposure Net interest payable on variable rate borrowing / investments	**20%**	**20%**	**20%**	**20%**	**20%**	**20%**
Upper limit for total principal sums invested for over 12 months (per maturity date)	**£50m**	**£50m**	**£100m**	**£100m**	**£100m**	**£100m**

Maturity structure of new fixed rate borrowing during 2017/18	Upper Limit	Lower Limit
under 12 months	10%	0%
12 months and within 24 months	30%	0%
24 months and within 5 years	40%	0%
5 years and within 10 years	80%	0%
10 years and above	100%	0%

Appendix 2 *Definition of Fitch Credit Ratings*

Support Ratings

Rating	Current Definition (December 2014)
1	A bank for which there is an extremely high probability of external support. The potential provider of support is very highly rated in its own right and has a very high propensity to support the bank in question. This probability of support indicates a minimum Long-term rating floor of 'A-'.
2	A bank for which there is a high probability of external support. The potential provider of support is highly rated in its own right and has a high propensity to provide support to the bank in question. This probability of support indicates a minimum Long-term rating floor of 'BBB-'.
3	A bank for which there is a moderate probability of support because of uncertainties about the ability or propensity of the potential provider of support to do so. This probability of support indicates a minimum Long-term rating floor of 'BB-'.
4	A bank for which there is a limited probability of support because of significant uncertainties about the ability or propensity of any possible provider of support to do so. This probability of support indicates a minimum Long-term rating floor of 'B'.
5	A bank for which external support, although possible, cannot be relied upon. This may be due to a lack of propensity to provide support or to very weak financial ability to do so. This probability of support indicates a Long-term rating floor no higher than 'B-' and in many cases no floor at all.

Short-term Ratings

Rating	Current Definition (December 2014)
F1	**Highest short-term 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 short-term 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 short-term 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 (December 2014)
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 capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions is more likely to impair this capacity. This is the lowest investment-grade category.
BB	**Speculative** - 'BB' ratings indicate an elevated vulnerability to default risk, particularly in the event of adverse changes in business or economic conditions over time; however, business or financial flexibility exists which supports the servicing of financial commitments.
B	**Highly speculative -** 'B' ratings indicate that material default risk is present, but limited margin of safety remains. Financial commitments are currently being me however, capacity for continued payment is vulnerable to deterioration in th business and economic environment.
CCC	**Substantial credit risk – '**CCC' Default is a real possibility.
CC	**Very high levels of credit risk –** 'CC' Default of some kind appears probable
C	**Exceptionally high levels of credit risk** Default is imminent or inevitable, or the issuer is in standstill. Conditions that are indicative of a 'C' category rating for an issuer include: a. the issuer has entered into a grace or cure period following non-payment of a material financial obligation; b. the issuer has entered into a temporary negotiated waiver or standstill agreement following a payment default on a material financial obligation; or c. Fitch Ratings otherwise believes a condition of 'RD' or 'D' to be imminent or inevitable, including through the formal announcement of a distressed debt exchange. (RD – stands for restricted default and D – default).

Note:

The modifiers "+" or "-" may be appended to a rating to denote relative status within major rating categories. Such suffixes are not added to the 'AAA' Long-Term IDR category, or to Long-Term IDR categories below 'B'.

Appendix 3

London Borough of Tower Hamlets

Counterparty Credit Rating List as at 03/01 2017

		Fitch Ratings				Moodys Ratings				S&P Ratings			
Counterparty		Long Term		Short Term		Long Term		Short Term		Long Term		Short Term	
Australia		SB	AAA			SB	Aaa			NO	AAA		
Banks	Australia and New Zealand Banking Group Ltd.	SB	AA-		F1+	NO	Aa2		P-1	NO	AA-		A-1+
	Commonwealth Bank of Australia	SB	AA-		F1+	NO	Aa2		P-1	NO	AA-		A-1+
	Macquarie Bank Ltd.	SB	A		F1	SB	A2		P-1	NO	A		A-1
	National Australia Bank Ltd.	SB	AA-		F1+	NO	Aa2		P-1	NO	AA-		A-1+
	Westpac Banking Corp.	SB	AA-		F1+	NO	Aa2		P-1	NO	AA-		A-1+
Canada		SB	AAA			SB	Aaa			SB	AAA		
Banks	Bank of Montreal	SB	AA-		F1+	NO	Aa3		P-1	SB	A+		A-1
	Bank of Nova Scotia	SB	AA-		F1+	NO	Aa3		P-1	SB	A+		A-1
	Canadian Imperial Bank of Commerce	SB	AA-		F1+	NO	Aa3		P-1	SB	A+		A-1
	National Bank of Canada	SB	A+		F1	NO	Aa3		P-1	SB	A		A-1
	Royal Bank of Canada	NO	AA		F1+	NO	Aa3		P-1	NO	AA-		A-1+
	Toronto-Dominion Bank	SB	AA-		F1+	NO	Aa1		P-1	SB	AA-		A-1+
Denmark		SB	AAA			SB	Aaa			SB	AAA		
Banks	Danske A/S	SB	A		F1	PO	A1		P-1	SB	A		A-1
Germany		SB	AAA			SB	Aaa			SB	AAA		
Banks	DZ BANK AG Deutsche Zentral-Genossenschaftsbank	SB	AA-		F1+	SB	Aa1		P-1	SB	AA-		A-1+
	Landesbank Berlin AG					PO	Aa3		P-1				
	Landesbank Hessen-Thueringen Girozentrale	SB	A+		F1+	SB	Aa3		P-1	SB	A		A-1
	Landwirtschaftliche Rentenbank	SB	AAA		F1+	SB	Aaa		P-1	SB	AAA		A-1+
	NRW.BANK	SB	AAA		F1+	SB	Aa1		P-1	SB	AA-		A-1+
Netherlands		SB	AAA			SB	Aaa			SB	AAA		
Banks	ABN AMRO Bank N.V.	SB	A+		F1	SB	A1		P-1	SB	A		A-1
	Bank Nederlandse Gemeenten N.V.	SB	AA+		F1+	SB	Aaa		P-1	SB	AAA		A-1+
	Cooperatieve Rabobank U.A.	SB	AA-		F1+	NO	Aa2		P-1	SB	A+		A-1
	ING Bank N.V.	SB	A+		F1	SB	A1		P-1	SB	A		A-1
	Nederlandse Waterschapsbank N.V.					SB	Aaa		P-1	SB	AAA		A-1+
Singapore		SB	AAA			SB	Aaa			SB	AAA		
Banks	DBS Bank Ltd.	SB	AA-		F1+	SB	Aa1		P-1	SB	AA-		A-1+
	Oversea-Chinese Banking Corp. Ltd.	SB	AA-		F1+	SB	Aa1		P-1	SB	AA-		A-1+

	United Overseas Bank Ltd.	SB	AA-		F1+	SB	Aa1		P-1	SB	AA-		A-1+
Sweden		SB	AAA			SB	Aaa			SB	AAA		
Banks	Nordea Bank AB	SB	AA-		F1+	SB	Aa3		P-1	NO	AA-		A-1+
	Skandinaviska Enskilda Banken AB	SB	AA-		F1+	SB	Aa3		P-1	SB	A+		A-1
	Svenska Handelsbanken AB	SB	AA		F1+	SB	Aa2		P-1	NO	AA-		A-1+
	Swedbank AB	SB	AA-		F1+	SB	Aa3		P-1	NO	AA-		A-1+
Switzerland		SB	AAA			SB	Aaa			SB	AAA		
Banks	Credit Suisse AG	SB	A		F1	SB	A1		P-1	SB	A		A-1
	UBS AG	SB	A+		F1	SB	Aa3		P-1	SB	A+		A-1
United Kingdom		NO	AA			NO	Aa1			NO	AA		
AAA rated and Government backed securities	Debt Management Office												
Banks	Bank of Scotland PLC	SB	A+		F1	SB	A1		P-1	NO	A		A-1
	Close Brothers Ltd	SB	A		F1	SB	Aa3		P-1				
	Co-operative Bank PLC (The)	SB	B		B	PO	Caa2		NP				
	Goldman Sachs International Bank	SB	A		F1	SB	A1		P-1	SB	A+		A-1
	HSBC Bank PLC	SB	AA-		F1+	NO	Aa2		P-1	NO	AA-		A-1+
	Lloyds Bank Plc	SB	A+		F1	SB	A1		P-1	NO	A		A-1
	Santander UK PLC	PO	A		F1	NO	Aa3		P-1	NO	A		A-1
	Standard Chartered Bank	SB	A+		F1	NO	Aa3		P-1	SB	A		A-1
	Sumitomo Mitsui Banking Corporation Europe	NO	A		F1	SB	A1		P-1	PO	A		A-1
	UBS Ltd.	SB	A+		F1	SB	A1		P-1	SB	A+		A-1
	Ulster Bank Ltd	SB	BBB+		F2	PO	A3		P-2	SB	BBB		A-2
Building Society	Coventry Building Society	SB	A		F1	NO	A2		P-1				
	Cumberland Building Society												
	Leeds Building Society	SB	A-		F1	NO	A2		P-1				
	National Counties Building Society												
	Nationwide Building Society	PO	A		F1	NO	Aa3		P-1	NO	A		A-1
	Newcastle Building Society	SB	WD		WD								
	Nottingham Building Society					NO	Baa1		P-2				
	Principality Building Society	SB	BBB+		F2	SB	Baa3		P-3				
	Progressive Building Society												
	Skipton Building Society	SB	A-		F1	PO	Baa2		P-2				
	West Bromwich Building Society					SB	B1		NP				
	Yorkshire Building Society	SB	A-		F1	SB	A3		P-2				
Nationalised and Part	National Westminster Bank PLC	SB	BBB+		F2	PO	A3		P-2	SB	BBB+		A-2

Nationalised Banks	The Royal Bank of Scotland Plc	SB	BBB+		F2	PO	A3		P-2	SB	BBB+		A-2

Appendix 4

Treasury Management Policy Statement

The London Borough of Tower Hamlets defines the policies and objectives of its treasury management activities as follows: -

1. This organisation defines its treasury management activities as:

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

2. This organisation 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 organisation.

3. This organisation 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 best value in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management."

Policy on use of an External Treasury Advisor

The Council shall employ an external treasury advisor to provide treasury management advice and cash management support services. However, the Council shall control the credit criteria and the associated counter-party list for investments.

The Council recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

Appendix 5

Treasury Management Scheme of Delegation

1. Full Council / Cabinet

- receiving and reviewing reports on treasury management policies. practices and activities
- receiving the mid-year and annual (outturn) reports
- approval of annual strategy.

2. Cabinet /Section 151 Officer

- approval of/amendments to the organisation's adopted clauses and treasury management policy statement
- budget consideration and approval
- approval of the division of responsibilities
- approving the selection of external service providers and agreeing terms of appointment.

3. Audit Committee

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.
- receiving and reviewing regular monitoring reports and acting on recommendations

Appendix 6

Treasury Management Reporting Arrangement

Area of Responsibility	Council/Committee/ Officer	Frequency
Treasury Management Strategy Statement/ Annual Investment Strategy/ Minimum Revenue Provision Policy	Full Council	Annually before the start of the financial year to which policies relate
Mid-Year Treasury Management Report	Full Council	Semi-Annually in the financial year to which policies relate
Updates or revisions to the Treasury Management Strategy Statement/ Annual Investment Strategy/ Minimum Revenue Provision Policy	Audit Committee or Full Council	As necessary
Annual Treasury Outturn Report	Audit Committee and Full Council	Annually by 30 September after the year end to which the report relates
Treasury Management Practices	Corporate Director-Resources	N/A
Scrutiny of Treasury Management Strategy Statement	Overview and Scrutiny Committee (if called in) / Audit Committee	Annually before the start of the financial year to which the report relates
Scrutiny of Treasury Management Performance	Audit Committee	Quarterly

Appendix 7 - GLOSSARY

Asset Life	How long an asset, e.g. a Council building is likely to last.
Borrowing Portfolio	A list of loans held by the Council.
Borrowing Requirements	The principal amount the Council requires to borrow to finance capital expenditure and loan redemptions.
Capitalisation direction or regulations	Approval from central government to fund certain specified types of revenue expenditure from capital resources.
CIPFA Code of Practice on Treasury Management	A professional code of Practice which regulates treasury management activities.
Capital Financing Requirement (CFR)	Capital Financing Requirement- a measure of the Council's underlying need to borrow to fund capital expenditure.
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
Counterparties	Organisations or Institutions the Council lends money to e.g. Banks; Local Authorities and MMF.
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. The term is usually applied to longer-term debt instruments, generally with a maturity date falling at least a year after their issue date.
Covered bonds	A covered bond is a corporate bond with one important enhancement: recourse to a pool of assets that secures or "covers" the bond if the originator (usually a financial institution) becomes insolvent. These assets act as additional credit cover; they do not have any bearing on the contractual cash flow to the investor, as is the case with Securitized assets.

Consumer Prices Index & Retail Prices Index (CPI & RPI)	The main inflation rate used in the UK is the CPI. The Chancellor of the Exchequer bases the UK inflation target on the CPI. The CPI inflation target is set at 2%. The CPI differs from the RPI in that CPI excludes housing costs. Also used is RPIX, which is a variation of RPI, one that removes mortgage interest payments.
Credit Default Swap (CDS)	A kind of protection that can be purchased by MMF companies from insurance companies (for their investment) in exchange for a payoff if the organisation they have invested in does not repay the loan i.e. they default.
Credit watch	Variety of special programs offered by credit rating agencies and financial institutions to monitor organisation/individual's (e.g. bank) credit report for any credit related changes. A credit watch allows the organisation/individuals to act on any red flags before they can have a detrimental effect on credit score/history.
Credit Arrangements	Methods of Financing such as finance leasing
Credit Ratings	A scoring system issued by credit rating agencies such as Fitch, Moody's and Standard & Poors that indicate the financial strength and other factors of a bank or similar Institution.
Creditworthiness	How highly rated an institution is according to its credit rating.
Debt Management Office (DMO)	The DMO is an agency of the HM Treasury which is responsible for carrying out the Government's Debt Management Policy.
Debt Rescheduling	The refinancing of loans at different terms and rates to the original loan.
Depreciation Method	The spread of the cost of an asset over its useful life.
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.
Interest Rate exposures	A measure of the proportion of money invested and what impact movements in the financial markets would have on them.
The International Monetary Fund (IMF)	is an intergovernmental organisation which states its aims as to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world.
Impaired investment	An investment that has had a reduction in value to reflect

	changes that could impact significantly on the benefits expected from it.
LIBID	The London Interbank Bid Rate – it is the interest rate at which major banks in London are willing to borrow (bid for) funds from each other.
Market Loans	Loans from banks available from the London Money Market including LOBOS (Lender Option, Borrowing Option) which enable the authority to take advantage of low fixed interest for a number of years before an agreed variable rate comes into force.
Money Market Fund (MMF)	A 'pool' of different types of investments managed by a fund manager that invests in lightly liquid short term financial instruments with high credit rating.
Monetary Policy Committee (MPC)	Committee designated by the Bank of England, whose main role is to regulate interest rates.
Minimum Revenue Provision (MRP)	This is the amount which must be set aside from the revenue budget each year to cover future repayment of loans.
Non Specified Investments	Investments deemed to have a greater element of risk such as investments for longer than one year
Premium	Cost of early repayment of loan to PWLB to compensate for any losses that they may incur
Prudential Indicators	Set of rules providing local authorities borrowing for funding capital projects under a professional code of practice developed by CIPFA and providing measures of affordability and prudence reflecting the Council's Capital Expenditure, Debt and Treasury Management.
PWLB	Public Works Loan Board, a statutory body whose function is to lend money to Local Authorities (LAs) and other prescribed bodies. The PWLB normally are the cheapest source of long term borrowing for LAs.
Specified Investments	Investments that meet the Council's high credit quality criteria and repayable within 12 months.
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.
Unrated institution	An institution that does not possess a credit rating from one of the main credit rating agencies.
Unsupported Borrowing	Borrowing where costs are wholly financed by the Council.