Report to: Cabinet **Date of Meeting:** 14 February 2013
Council 28 February 2013

Subject: Treasury Management Policy & Strategy 2013/2014

Report of: Head of Corporate Finance & ICT

Wards Affected: All

Is this a Key Decision? No

Is it included in the Forward Plan? No

Exempt/Confidential No

Purpose/Summary

To advise Cabinet of the proposed procedures and strategy to be adopted in undertaking the Treasury Management Function in 2013/2014.

Recommendation(s)

Council be recommended that: -

a) The Treasury Management Policy Document for 2013/2014 (Annex A) be agreed; and
b) The Treasury Management Strategy Document for 2013/2014 (Annex B) be agreed.

How does the decision contribute to the Council's Corporate Objectives?

	Corporate Objective	Positive Impact	Neutral Impact	Negative Impact
1	Creating a Learning Community		√	
2	Jobs and Prosperity		√	
3	Environmental Sustainability		√	
4	Health and Well-Being		√	
5	Children and Young People		√	
6	Creating Safe Communities		√	
7	Creating Inclusive Communities		√	
8	Improving the Quality of Council Services and Strengthening Local Democracy		√	

Reasons for the Recommendation:
To enable the Council to effectively manage its treasury activities..

What will it cost and how will it be financed?

(A) Revenue Costs
There are no financial implications as a result of this report.

(B) Capital Costs
None.

Implications:

The following implications of this proposal have been considered and where there are specific implications, these are set out below:

Legal	Local Authorities are required to have regard to the Code of Practice on Treasury Management under the provisions of the Local Government Act 2003	
Equality		
1.	No Equality Implication	√
2.	Equality Implications identified and mitigated	
3.	Equality Implication identified and risk remains	

Impact on Service Delivery:
None.

What consultations have taken place on the proposals and when?
The Head of Corporate Finance and ICT has no comments on this report because the contents of the report have no financial implications (FD2095/13:)

The Head of Corporate Legal Services has been consulted and comments have been incorporated into the report (LD2095/13 /13:).

Are there any other options available for consideration?
None.

Implementation Date for the Decision
With effect from 1 April 2013.

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Background Papers:
None

1. Background

1.1. The Council has previously adopted CIPFA's revised 2001 Code of Practice on Treasury Management in the Public Services which recommends the production of annual Treasury Management Policy and Strategy Documents, and the revision to The Code in 2009 following the Icelandic bank collapse. The Council has also adopted the revisions contained within the 2011 Code.

1.2. In addition, the Council has also adopted, and incorporated into both documents:

a) The requirements of the 2003 Prudential Code for Capital Finance in Local Authorities; and,
b) An Investment Strategy produced in line with guidance from the then Office of the Deputy Prime Minister concerning the investment of surplus funds. This sets out the manner in which the Council will manage its investments, giving priority to the security and liquidity of those investments.

2. Treasury Management Policy and Strategy Documents

2.1. The Code requires the Council to produce:

a) A Treasury Management Policy Document – which outlines the broad policies, objectives and approach to risk management of its treasury management activities;
b) A Treasury Management Strategy Document – This sets out specific treasury activities which will be undertaken in compliance with the Policy in 2013/2014; and
c) Suitable treasury management practices, setting out the manner in which the organisation will seek to achieve these policies and objectives, prescribing how it will manage and control those activities.

The content of the policy statement and the treasury management practices will follow the recommendations contained in sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of the Council. Such amendments will not result in the Council materially deviating from the Codes key principles.

2.2. The proposed Policy and Strategy Documents are attached at **Annex A and B** respectively.

2.3. Economic conditions have been difficult since the onset of the credit crunch in August 2007. This caused all major economies to enter into recession caused by a reduction in lending as banks attempted to repair their balance sheets, with concerns being raised over the financial health of many institutions. The wider economic position has meant that a continuing review of the Treasury Management Policy and Strategy documents has been undertaken to identify whether any improvements can be made.

All investments are made in accordance with the Council's Investment Criteria. This takes account of market and risk conditions at the time the investment is made, with security being assessed over liquidity, and liquidity being assessed over return.

2.4. In view of the complex nature of Treasury Management, regular treasury update reports will be presented to the Audit and Governance Committee.

3. Financial Procedure Rules – Banking Arrangements

3.1. The Treasury Management Policy Document at **Annex A** delegates certain responsibilities to the Head of Corporate Finance and ICT, including all executive decisions on borrowing, investment or financing, in line with the Constitution of the Council.

4. Minimum Revenue Provision (MRP) for Debt Repayment Policy Document

4.1. The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 introduced changes to the calculation of the MRP.

4.2. As a transitional arrangement for 2008/09, authorities were able to continue to calculate MRP as in previous years i.e. 4% of the underlying need to borrow for capital purposes, as measured at 31 March 2008. The Council's revenue budget for 2008/09 was constructed on this basis.

4.3. To comply with the legislative changes, the Council has, from 2009/10, retained this calculation for borrowing supported through the Revenue Support Grant but for unsupported prudential borrowing, MRP will be calculated using the estimated life method. This links the charges to revenue more closely to the life of the asset. The Council's Revenue Budget for 2013/14 to 2015/16 has been constructed on this basis.

4.4. The change in legislation also allows councils to apply an MRP "Holiday" on large projects, the costs of which span a number of financial years. Rather than starting to charge MRP as the expenditure is incurred, the option is given to apply MRP only when the scheme becomes operational. The total level of MRP remains unchanged, only the timing of the charge is altered. This option is considered to be the most appropriate for use within Sefton.

ANNEX A

SEFTON COUNCIL

TREASURY MANAGEMENT

POLICY

2013/2014

CORPORATE FINANCE AND ICT

1. **Treasury Management Policy**

1.1. The Council defines Treasury Management as:

The management of the 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.

1.2. The Council's Statement of Treasury Management Policy is:

a) Effective Treasury Management is acknowledged as providing support towards the achievement of the Council's 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;
b) The successful identification, monitoring and control of risk is regarded as being the prime criteria by which the effectiveness of the Council's Treasury Management activities will be measured. Accordingly, the analysis and reporting of Treasury Management activities will focus on their risk implications for the organisation.

1.3 A dedicated team of three officers carries out the day-to-day treasury management activities. Two of the current officers are qualified accountants, whilst the third is a qualified accounting technician. The Treasury Group Accountant has obtained the CIPFA/Association of Corporate Treasurers sponsored qualification CertITM-PF, which is aimed at giving a solid grounding in treasury management and which is tailored to the public sector.

1.3.1 Members should receive training in the Treasury Management function, in order to assist in the understanding of this relatively complex area. This will be addressed via the provision of regular reporting to Cabinet, Corporate Services Cabinet Member Meeting and the Audit and Governance Committee, and the provision of specific training on Treasury Management.

2. **Treasury Management Strategy**

2.1. The Annual Strategy Document sets out in detail how the Treasury Management Activities are to be undertaken in a particular financial year to comply with the Council's Policy. The strategy for 2013/2014 is attached at **Annex B**.

3. **Delegated Powers**

3.1. The Head of Corporate Finance and ICT, under the Council's Constitution, is given the following authority:

a) All money in the hands of the Council shall be aggregated for the purposes of Treasury Management and shall be under the control of the Head of Corporate Finance and ICT, the Officer designated for the purposes of Section 151 of the Local Government Act, 1972;

b) All executive decisions on borrowing, investment or financing shall be delegated to the Head of Corporate Finance and ICT (or in his/her absence the Deputy Section 151 Officer) who shall be required to act in accordance with the Council's Treasury Policy, Treasury Management Practices and CIPFA's Standard of Professional Practice on Treasury Management.

4. Reporting Requirements/Responsibilities

4.1. Council

Council will approve, prior to each financial year, the Treasury Management Policy and Strategy Documents. Also, an annual outturn report on Treasury Management activity will be presented before 30 June following the end of the previous financial year.

4.2. Cabinet

Cabinet will:

a) Consider, prior to each financial year, Treasury Management Policy and Strategy Documents and refer them to Council for approval;
b) Monitor these documents and approve any in-year amendments necessary to facilitate continued effective Treasury Management;
c) Receive an annual outturn report on Treasury Management activity prior to the 30 June following each financial year; and

4.3. Audit and Governance Committee

Audit and Governance Committee will:

a) Implement and monitor performance on at least a quarterly basis necessary to facilitate continued effective Treasury Management;
b) Receive an annual outturn report on Treasury Management activity prior to the 30 June following each financial year; and
c) Will be responsible for ensuring effective scrutiny of treasury management and policies.

4.4. Head of Corporate Finance and ICT

The Head of Corporate Finance and ICT will:

a) Draft and submit to Cabinet and Council prior to each financial year, Treasury Management Policy and Strategy Documents;
b) Implement and monitor these documents resubmitting any necessary in-year revisions/amendments (at least on a quarterly basis) to Cabinet for approval;
c) Draft and submit an annual outturn report on Treasury Management activity to Cabinet and Council by the 30 June following each financial year-end;

d) Draft and submit an annual outturn report (and quarterly performance reports) on Treasury Management activity to the Audit & Governance Committee by the 30 June following each financial year-end;
e) Maintain suitable Treasury Management Practices (TMP), setting out the manner in which the Council will seek to achieve its objectives. The TMP's will also prescribe how the treasury activities will be managed and controlled;
f) Be responsible for the execution and administration of treasury management decisions; and
g) Act in accordance with the Council's policy statement and treasury management practices, and also in accordance with CIPFA's Standard of Professional Practice on Treasury Management.

4.5 Borrowing and investments

The Council's borrowing will be affordable, sustainable and prudent and consideration will be given to the management of interest rate risk and refinancing risk. The source from which the borrowing is taken and the type of borrowing should allow the Council transparency and control over its debt.

The Council's primary objective in relation to investments remains the security of capital. The liquidity or accessibility of the Authority's investments followed by the yield earned on investments remain important but are secondary considerations.

ANNEX B1

SEFTON COUNCIL

TREASURY MANAGEMENT

STRATEGY

2013/2014

CORPORATE FINANCE AND ICT

SEFTON COUNCIL

Treasury Management Strategy

1. Introduction

1.1. The Treasury Management Strategy Document sets out in detail how the Treasury Management Activities are to be undertaken in a particular financial year to comply with the Council's Treasury Management Policy.

1.2 The Strategy had been produced to incorporate the requirements of the CIPFA Code of Practice on Treasury Management, the 2011 revised Prudential Code for Capital Finance, and the revised Treasury Management in the Public Services code of Practice and Cross-Sectoral Guidance Notes (2011).

2. Treasury Management Strategy 2013/2014

2.1. The Strategy for 2013/2014 covers:

a) Treasury Limits in force which will limit the borrowing activity of the Council (2.2);
b) Prudential Indicators 2013/2014 to 2015/2016 (2.3);
c) Interest Rates (2.4);
d) Capital Borrowing (2.5);
e) Debt Rescheduling opportunities (2.6);
f) Borrowing in advance of need (2.7);
g) Investment Strategy (2.8).

2.2. Treasury Limits for 2013/2014

The Treasury Limits set by Council in respect of its borrowing activities are:

The overall or Affordable Borrowing Limit (authorised limit as per Prudential Indicators 2013/2014).	Maximum £200.500m

It is a statutory duty under S.3 of the Local Government Act 2003 and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the 'Affordable Borrowing Limit'. The Affordable Borrowing Limit takes into account the Council's current debt, an assessment of external borrowing to fund the Capital Programme in 2013/2014, the need to fund capital expenditure previously met from internal funding, and cash flow requirements.

The amount of overall borrowing, which maybe outstanding by way of short-term borrowing.	Maximum £15m

The Short – Term Borrowing limit takes into account an assessment of any potential short-term financing the Council may need (e.g. bank overdraft, short-term funding in anticipation of grant receipts). Short-Term Borrowing is defined as being for less than 12 months.

The proportion of external borrowing which is subject to variable rate interest.	Maximum 33%

The limit on variable rate borrowing gives the Council flexibility to finance expenditure at favourable market rates, but ensures Council exposure to variable interest commitments is within prudent levels.

2.3. Prudential Indicators

The following prudential indicators are considered relevant by CIPFA for setting an integrated Treasury Management Strategy.

2.3.1 Interest Rate Exposure Indicators

Fixed rate borrowing and investment has the benefit of reducing the uncertainty surrounding future interest rate changes. However, in looking to improve performance best practice recommends retaining a degree of flexibility through the use of variable rates on at least part of the Treasury Management Activity.

To ensure that the risk associated with improved performance which may be achieved by using variable loans and investments is minimised, it is necessary to establish indicators to control the position. The control is based on setting an upper limit for both fixed and variable interest rate exposures expressed as a percentage of the Council's net outstanding principal sum. The following indicators are to be used:

Upper Limit for Interest Rate Exposures	**2013/14 %**	**2014/15 %**	**2015/16 %**
Upper limit for fixed interest rate exposure expressed as a percentage of net outstanding principal sum	340	340	340
Upper limit for variable interest rate exposure expressed as a percentage of net outstanding principal sum	-20	-20	-20

2.3.2 Non Specified Investment Indicator

The Investment Strategy (Para 2.9) allows non-specified investments (see paragraph 2.9.3 for definition) to be made using funds managed by the Council. The indicator is designed to control the level of such non-specified investments when compared to the overall investments of the Council.

Upper Limit on Non-Specified Investments	**2013/14 %**	**2014/15 %**	**2015/16 %**
Upper limit on the value of non-specified investments as a percentage of total investments	40	40	40

2.3.4 Debt Maturity Indicators

The indicators are designed to be a control over an authority having large concentrations of fixed rate debt needing to be replaced at times of high interest rates. The control is based on the production of a debt maturity profile, which measures the amount of borrowing that is fixed rate that will mature in each period as a percentage of total projected borrowing that is fixed rate. Any borrowing decision and related maturity dates will be taken by the Council mindful of maturity profile limits set out below to ensure large concentrations of debt do not fall due for repayment in any one future financial year. The profile reflects borrowing advice provided by Arlingclose, the Council's Treasury Management Advisors, and has been noted by them.

Maturity Structure of Fixed Rate Borrowing During 2013/2014	**Upper Limit %**	**Lower Limit %**
Under 12 month	35%	0%
12 months and within 24 months	40%	0%
24 months and within 5 years	40%	0%
5 years and within 10 years	40%	0%
10 years and above	90%	25%

Policy on the use of external service providers

The Council employs Arlingclose as its treasury consultants. Arlingclose were engaged for the first time with effect from 01/04/2011, replacing Sector, following a tendering exercise for the contract. The Council recognises that responsibility for treasury management decisions rests with the Council at all times. It also recognises that there is value in such arrangements in order to acquire access to specialist skills, knowledge, and advice. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly documented, and subjected to regular review.

2.3.5 Credit risk

Virtually any investment involves risk. The Council will consider the credit ratings supplied by a variety of recognised money market organisations, as part of the process to determine the list of Banks where the level of risk is acceptable, with security, then liquidity, being the key aims. As part of this process advice from Arlingclose will be considered, both in terms of maximum duration and level of investment.

The Council also considers alternative assessments of credit strength, and information on corporate developments and of market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution (minimum A- or equivalent) and its sovereign (minimum AA+ for non-UK sovereigns);
- Sovereign support mechanisms;
- Credit default swaps (where quoted);
- Share prices (where available);
- Economic fundamentals, such as a country's net debt as a percentage of its GDP);
- Corporate developments, news, articles, markets sentiment and momentum;
- Subjective overlay.
- Background research in the financial press
- Discussion with our treasury consultants
- Internal discussion with Head of Corporate Finance and ICT

As a means of clarifying the level of acceptable risk, the Risk Matrix at **Annex B3** will be used. The Council will only invest in institutions that have a Risk Matrix scoring of long term A- (or equivalent).

The Council maintains a full record of each investment decision taken, each of which is authorised by an appropriate level of signatory.

2.4. Interest Rates

2.4.1 Arlingclose provide regular forecasts of interest rates to assist decisions in respect of:

a) Capital Borrowings (2.5);
b) Debt Rescheduling opportunities, (2.6)
c) Temporary borrowing for cash flow; and
d) Investments strategy (2.8).

2.4.2. **Annex B2** gives details of Arlingclose's central view regarding interest rate forecasts. Arlingclose's forecast is for official interest rates to remain at 0.5% until 2016.

2.4.3. The advice from Arlingclose takes into account financial activity both in the UK and world economies and the impact of major national and international events. It is essential that borrowing and investment decisions are taken mindful of independent forecasts as to interest rate movements. The Council will continue to take account of the advice of Arlingclose.

2.5. Capital Borrowing

2.5.1 The Council's debt portfolio as at 31st January 2013 is as set out below:

Debt Portfolio	
Average Interest Rate	4.51%
Debt Outstanding – Fixed Rate	£m
PWLB	130.465
Other Borrowing	19.770
Other Long Term Liabilities	5.907
Total Debt	156.142

The category of other borrowing (£19.770m) represents finance lease liabilities.

Other long term liabilities (£5.907m) represent transferred debt from the Merseyside Residuary Body.

2.5.2 The Council will raise its required finance, following advice from Arlingclose, from the Public Works Loan Board (PWLB), or other local authorities.

The Council's forecast borrowing requirement for 2013/2014 is as follows:

Borrowing Requirement	Estimate £m
New Borrowing	14.345
Replacement Borrowing	7.173
Total Borrowing	21.518

The new borrowing represents the unsupported borrowing as required by the Capital Programme in 2013/14. As noted in 2.5.4 below the Council is internally borrowed, and may take additional borrowing if required in order to reverse this position.

2.5.3. The Arlingclose forecast for Gilt interest rates (as set out at **Annex B2**). This would suggest that the following strategy is followed:

- The cheapest borrowing will be internal borrowing, which involves running down cash balances and foregoing interest earned at historically low rates. Consideration will always be given to long term borrowing rates and the possibility of rates rising, which could mean borrowing at future higher rates which could erode the advantages of internal borrowing
- Temporary borrowing from money markets or other local authorities.

2.5.4. The authority borrows from the PWLB in order to fund part of the capital programme, the maximum that we can borrow being the Capital Financing Requirement (CFR). PWLB borrowing as at 31 January 2013, plus lease liabilities and other long term liabilities, is £156.142m, as against a CFR of £220.500m for 2013/14. This position is classed as being internally borrowed which does have the advantage of reducing exposure to interest rate and credit risk. To be internally borrowed is a conscious decision to use cash balances to fund capital expenditure, rather than borrow from the PWLB. This position can be reversed at any time by borrowing from the PWLB.

2.5.5. 2013/14 is expected to experience a continuation of a low bank rate. Hence, internal borrowing is a sensible option where interest rates on deposits are much lower than the current PWLB borrowing rates.

2.5.6. However, as noted in 2.5.3, savings have to be weighed against the potential for incurring long term extra costs by delaying unavoidable new borrowing until later years when PWLB rates are forecast to be higher.

2.5.7. Against this background, caution will be adopted in undertaking borrowing in 2013/2014. The Head of Corporate Finance and ICT will monitor the interest rate market and following advice from Arlingclose, adopt a pragmatic approach to changing circumstances during the year.

2.5.8. External v Internal Borrowing

2.5.9. The Council currently has a difference between gross debt and net debt (gross debt net of cash balances) of £72m. The general aim of the strategy would be to reduce the difference between the two in order to reduce the credit risk of holding investments.

2.5.10. As noted in 2.5.4 above the Council is internally borrowed. If this continues this will reduce the difference between gross and net debt. Early repayment of debt is, however, not a realistic option since the introduction by the PWLB of significantly lower rates on 1 November 2007, which has now been compounded by a considerable further widening of the difference between new borrowing and repayment has meant that large premiums would be incurred.

2.6. Debt Rescheduling Opportunities

2.6.1. As noted in 2.5.10 above, restructuring with the PWLB is now much less attractive than before due to the potentially large premiums that would be incurred.

The lower interest rate environment and changes in the rules regarding the premature repayment of PWLB loans has adversely affected the scope to undertake meaningful debt restructuring. However, the situation will be monitored and the Council will consider the option of debt restructuring during 2013/2014, should the financial circumstances change.

2.7 Borrowing in advance of need

The Council will not borrow more than, or in advance of, its needs purely to profit from the investment income made on the extra sums borrowed. Any decision to borrow in advance of need will be considered carefully to ensure value for money can be demonstrated and that the Council can ensure the security of such funds.

In determining whether to borrow in advance of need the Council will;

- Ensure that there is a direct link between the capital programme and maturity profile of the existing debt portfolio which supports the need to borrow in advance of need;
- Ensure that the revenue implications of such borrowing have been considered in respect of future plans and budgets; and
- Consider the merits of other forms of funding.

2.8 The Use of Financial Instruments for the Management of Risks

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

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

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

The Council will only use derivatives after seeking expertise, a legal opinion and ensuring officers have the appropriate training for their use.

2.9. Investment Strategy

2.9.1. The Council manages the investment of its surplus funds internally, and operates in accordance with the Guidance on Local Government Investments issued by CLG, and the 2011 CIPFA Treasury Management in Public Services and Cross Sectoral Guidance Notes.

2.9.2 The Council's investment priorities are, in order of priority:

- The security of capital
- The liquidity of capital

The Council will aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity.

2.9.3. Under the system of guidance investments are classified as Specified or Non Specified.

Specified Investments are those which satisfy the following conditions:

a) The investment and all related transactions are in sterling;
b) The investment is short-term i.e. less than 12 months;
c) The investment does not involve the acquisition of share or loan capital; Either:
   i) The investment is made with the UK Government or local authority; OR
   ii) The investment is made with a body or scheme, which has been awarded a high credit rating by a credit rating agency.

Non Specified Investments are those that do not meet the above definition.

2.9.4 The Council's investment portfolio as at 31st January 2013 is set out below:

Investments Portfolio	**£m**
Specified Investments Non-Specified Investments	70.930 0 .700
Total	71.630

2.9.5 The Council banks with National Westminster, which is part of the Royal Bank of Scotland Group. It is currently a part government-owned institution. At the present time, it does meet the minimum credit criteria of A- (or equivalent) long term. If the credit rating falls below the Authority's minimum criteria the Bank will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements when no other options are available.

2.9.6 The Council Strategy will be:

a) To make Specified Investments in line with the above conditions;
b) To make Non Specified Investments which satisfy all of the above with the exception of 2.9.3 b) which is extended to a period of less than 2 years or fixed term deposits, and a maximum of 5 years for negotiable instruments such as CDs;

It is suggested that the following investment vehicles should be made available to the authority:

Investment	**Reason**	**Risk**
Term deposits made with banks as listed in annexe B5, following the investment criteria as listed in annexe B4. Deposits also acceptable on an overnight call basis. Can also deposit with Local Authorities.	Certainty of rate of return and repayment of capital	Liquid, with potential for deterioration in credit risk. Most Local Authorities are not credit rated.
Certificates of Deposit with Banks and Bullding Societies	Certainty of rate and liquid	If not held until maturity, can be sold for a capital loss on the secondary market
Supra-national bonds	Greater levels of security of investment. A fairly liquid investment, though not as liquid as Gilts	High credit rating as placed with EIB and World Bank (AAA rated). Bond price may vary if sold early

Investments with Registered Providers	Certainty of rate of return and repayment of capital	Most Registered Providers are not credit rated.
Investments with organisations that do not meet the Council's specified investment criteria (subject to an external credit review and specific advice from TM advisor).	Greater diversification and allows a small portion of the portfolio to be invested at higher rates of retrurn	Investments may not be with credit rated organisations
AAA rated Money Market Fund (MMF)	Same day liquidity and high credit worthiness due to considerable diversification	High credit rating via the International Money Market Fund Association or IMMFA (AAA rated)
Other Money Market and Collective Investment Schemes	Stromng portfolio diversification	Variable Net Asset Value VNAV funds – potential for receving less than paid in. Plus long lead time for return of investment.
Corporate Bonds	Can be sold on the secondary market	Can be sold for a capital loss
Gilts	Liquid and very secure. Interest paid every six months	High credit rating as Government backed (AAA rated). Bond price may vary if sold early
Treasury Bills	Liquid and very secure. Duration of < 1year	No interest paid – they are zero-coupon rated, but are typically bought at a discount.
Debt Management Agency Account Deposit Facility (DMADF)	Secure investment	High credit rating as Government backed (AAA rated). Interest earned low. Investment cannot be repaid early

The maximum that can be invested in any of the above vehicles is £25m, except for term deposits and MMF's for which no limit is set. The maximum maturity period in any is 2 years for non-tradeable deposits, and 5 years for deposits that are tradeable on the secondary market. However, advice from Arlingclose will be taken into account in determining whether shorter maximum investment period is more appropriate during the year.

It is NOT proposed that the Council will be making any Non Specified Investments in 2013/2014 that do not comply with the above, however, should the situation change, the Head of Corporate Finance and ICT will report to Cabinet requesting appropriate approval to amend the Strategy before any such investments are made.

2.9.7 The Bank of England Base Rate has remained significantly low at 0.5%. Arlingclose's project of interest rates is to remain at 0.5% to 2016 **Annex B2**. Given the volatility of the market, the forecasts can only be used as a general guide to the future position. Consequently for 2013/14, the Authority has taken a prudent view and budgeted for an investment return based upon Arlingclose's base rate projection during 2013/14.

2.9.9. In order to pursue the strategy of maximising returns from surplus funds at an acceptable level of security and liquidity, the following Brokers will be utilised for investments of over one month:

ii) Sterling International Brokers Limited;
iii) Tradition UK Limited;
iv) Tullet Prebon Limited.

2.9.10 As noted in previous year's report, Cabinet agreed that the limit of investments that can be made to any UK or international banking institution was raised from £15m to £25m. This reflected the fact that our counterparty list became drastically reduced following the downgrading of many banks by the credit rating agencies following the credit crunch. However, now that stability has now entered the banking sector, on an operational basis we are using an institutional or group limit of £15m in order to increase security of capital by spreading risk. However, the overall limit of £25m will be maintained as a maximum, should conditions change.

It should be noted that an operational limit of £22.5m applies to Banking Groups, reflecting the fact that it represents two institutions (e.g. Natwest and RBS), as advised by Arlingclose. This represents 1.5 times the operational limit. The potential investment is apportioned between the institutions so that the maximum investment in either of the institutions is £15m.

2.9.11 The current list of Banks at **Annex B5** has been produced for information; this takes account of the most up-to-date credit ratings available in respect of the Banks and Building Societies named, and utilising Arlingclose's creditworthiness advice. It has also been rationalised to only include institutions that are backed by a no-UK sovereign rating of AA+, which implies that national Governments would support the Banks if they were facing financial difficulties. The organisations listed will be monitored daily with the assistance of Arlingclose to ensure they continue to meet the requirements outlined at **Annex B4**. In the event of a change in credit rating or outlook, the Council, with advice from Arlingclose, will evaluate its significance and determine whether to include (subject to Cabinet approval) or remove the organisation from the approval list.

2.9.14 If any of the Council's investments appear at risk of loss due to default (ie this is a credit related loss, and not one resulting from a fall in price due to movements in interest rates) the Council will make an assessment of whether a revenue provision of an appropriate amount is required.

2.9.15 Performance monitoring

a) Compliance with investment strategy (i.e level of risk is not exceeded).

b) The performance of the Council's investment strategy will be assessed by monitoring the average interest rate earned against the average 7 day LIBID on a monthly basis.

This will be reported to the Audit and Governance Committee on a quarterly basis, with outturn reports also presented to Cabinet and Council.

2.10 Member and Officer training

CIPFA's Code of Practice requires the Head of Corporate Finance and ICT to ensure that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities.

In order to address this, the Treasury Group Accountant has obtained the CIPFA/Association of Corporate Treasurers sponsored qualification CertITM-PF, which is aimed at giving a solid grounding in treasury management and which is tailored to the public sector. Training was provided for Members of the Audit & Governance Committee on 12 December 2012 and it is intended for such training to occur at least annually.

ANNEX B2

ARLINGCLOSE INTEREST

RATE FORECAST

Arlingclose's Interest Forecast as at 31 January 2012

	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15
Official Bank Rate													
Upside risk				0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50
Central case	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
3-month LIBID													
Upside risk	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Central case	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
1-yr LIBID													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	1.50	1.40	1.50	1.50	1.60	1.60	1.70	1.70	1.70	1.80	1.80	1.80	1.80
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
5-yr gilt													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	0.60	0.60	0.70	0.70	0.70	0.80	0.80	0.90	0.90	0.90	0.90	0.90	0.90
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
10-yr gilt													
Upside risk	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	1.50	1.40	1.50	1.60	1.60	1.70	1.70	1.80	1.80	1.80	1.90	1.90	1.90
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
20-yr gilt													
Upside risk	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	2.50	2.40	2.40	2.40	2.50	2.50	2.60	2.50	2.50	2.60	2.60	2.60	2.60
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
50-yr gilt													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	3.00	2.90	2.90	3.00	3.10	3.10	3.20	3.20	3.20	3.20	3.20	3.30	3.30
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50

RISK ASSESSMENT MATRIX - FITCH RATINGS

High

INCREASING YIELD

PROBABLITY of DEFAULT

High

F1 A +- 6	F2 12	F3 18	B 24	C 30	D 36
F1 A+ 5	F2 10	F3 15	F3 20	B 25	C 30
F1+/AA- 4	F1 A 8	F2 12	F3 16	F3 20	B 24
F1+/AA 3	F1 A+ 6	F1 A- 9	F2 12	F3 15	F3 18
F1+/AA+ 2	F1+/AA- 4	F1 A+ 6	F1 A 8	F2 10	F2 12
F1+/AAA 1	F1+/AA+ 2	F1+/AA 3	F1+/AA- 4	F1 A+ 5	F1 A +- 6

Low

High

SEVERITY of CONSEQUEN

SEFTON RISK TOLERANCE	**4**	
LOW RISK	**1 - 4**	Investment Grade
LOW - MEDIUM RISK	**5 - 9**	Investment Grade
MEDIUM RISK	**10 - 20**	Investment Grade
HIGH RISK	**21 - 36**	Speculative Grade

ANNEX B4

FITCH RATING EXPLANATION

Short term rating
This places greater emphasis on the liquidity necessary to meet financial commitments.

F1 – highest credit quality - + denotes exceptionally strong
F2 – good credit quality
F3 – fair credit quality

Long term rating
AAA – highest credit quality – lowest expectation of credit risk and exceptionally strong capacity to pay financial commitments
AA - very high credit quality – very low credit risk and very strong capacity to pay financial commitments
A - high credit quality – low credit risk and considered to have strong capacity to pay financial commitments, but may be vulnerable

Viability rating
This assesses how a bank would be viewed if it were entirely independent and could not rely on external support.

Aaa – highest fundamental credit quality
aa – very high fundamental credit quality
a – high fundamental credit quality
bbb – good fundamental credit quality
bb - speculative fundamental credit quality
b – highly speculative fundamental credit quality
ccc – substantial fundamental risk
cc – very high levels of fundamental credit risk
c – exceptionally high levels of fundamental credit risk
f - failed

Support rating
Judgement of a potential supporter’s (either sovereign state of parent) propensity to support the bank and it’s ability to support it.

1 – extremely high probability of external support
2 – extremely high probability of external support
3 – moderate probability
4 – limited probability
5 – cannot rely on support

Investments with UK and International Banks (including the Nationwide Building Society) are limited by the Head of Corporate Finance and ICT to a maximum principal sum of £25m with any of the institutions listed above.

Investment with the Government’s Debt Management Account Deposit Facility (DMADF), local authorities or any AAA rated or equivalent Money Market Fund will be limited to a maximum principal sum of £25m. However, the Head of Corporate Finance and ICT can decide day to day maximum sums lower than this; an operational limit of £15m is currently in place.

A group limit of 1.5 times the above limit will also be applied to institutions that are part of a group. This would allow, for example in the case of the RBS/Natwest Group, £15m to be invested with Natwest, and £7.5m with RBS.

SEFTON COUNCIL - STANDARD LENDING LIST

ANNEX B5

Counterparty Name	COUNTRY	Fitch Long-Term Issuer Default	Fitch Short Term Rating	Fitch Viability Rating	Fitch Support Ratin	Moody's Long-term	MDY ST	Moody's Financial Strength Rating	S&P Long-term	S&P Short-term	Banking Group	Maximum Recommended Duration (where TMSS permits)
COMMONWEALTH OF AUSTRALIA	AU	AAA	F1+			Aaa			AAAu	A-1+u		
AUST AND NZ BANKING GROUP	AU	AA-	F1+	aa-	1	Aa2	P-1	B-	AA-	A-1+		12 Months
COMMONWEALTH BANK OF AUSTRAL	AU	AA-	F1+	aa-	1	Aa2	P-1	B-	AA-	A-1+		12 Months
NATIONAL AUSTRALIA BANK LTD	AU	AA-	F1+	aa-	1	Aa2	P-1	B-	AA-	A-1+	National Australia Bank Group	12 Months
WESTPAC BANKING CORP	AU	AA-	F1+	aa-	1	Aa2	P-1	B-	AA-	A-1+		12 Months
GOVERNMENT OF CANADA	CA	AAA	F1+			Aaa			AAA	A-1+		
BANK OF MONTREAL	CA	AA-	F1+	aa-	1	Aa2 *-	P-1	B- *-	A+	A-1		12 Months
BANK OF NOVA SCOTIA	CA	AA-	F1+	aa-	1	Aa1 *-	P-1	B *-	A+	A-1		12 Months
CAN IMPERIAL BK OF COMMERCE	CA	AA-	F1+	aa-	1	Aa2 *-	P-1	B- *-	A+	A-1		12 Months
ROYAL BANK OF CANADA	CA	AA	F1+	aa	1	Aa3	P-1	C+	AA-	A-1+		12 Months
TORONTO-DOMINION BANK	CA	AA-	F1+	aa-	1	Aaa *-	P-1	B+ *-	AA-	A-1+		12 Months
REPUBLIC OF FINLAND	FI	AAA	F1+			Aaa	P-1		AAA	A-1+		
NORDEA BANK FINLAND PLC	FI	AA-	F1+	WD	1	Aa3	P-1	C	AA-	A-1+	Nordea Group	12 Months
FRENCH REPUBLIC	FR	AAA	F1+			Aa1			AA+u	A-1+u		
BNP PARIBAS	FR	A+	F1+	a+	1	A2	P-1	C-	A+	A-1	BNP Paribas Group	100 Days
CREDIT AGRICOLE CIB	FR	A+	F1+	#N/A N.A	1	A2	P-1	D-	A	A-1	Credit Agricole Group	100 Days
CREDIT AGRICOLE SA	FR	A+	F1+	a	1	A2	P-1	D	A	A-1	Credit Agricole Group	100 Days
SOCIETE GENERALE	FR	A+	F1+	a-	1	A2	P-1	C-	A	A-1		100 Days
UNITED KINGDOM	GB	AAA	F1+			Aaa			AAAu	A-1+u		
SANTANDER UK PLC	GB	A	F1	a	1	A2	P-1	C-	A	A-1	Santander Group	100 Days
BANK OF SCOTLAND PLC	GB	A	F1		1	A2	P-1	D+	A	A-1	Lloyds Banking Group	6 Months
BARCLAYS BK PLC-ADR C	GB	A	F1	a	1	A2	P-1	C-	A+	A-1		12 Months
HSBC BANK PLC	GB	AA-	F1+	a+	1	Aa3	P-1	C	AA-	A-1+	HSBC Group	12 months
LLOYDS TSB BANK PLC	GB	A	F1	bbb	1	A2	P-1	C-	A	A-1	Lloyds Banking Group	6 Months
NATIONAL WESTMINSTER BANK	GB	A	F1		1	A3	P-2	D+	A	A-1	RBS Group	6 Months
NATIONWIDE BUILDING SOCIETY	GB	A+	F1	a+	1	A2	P-1	C	A+	A-1		12 Months
ROYAL BANK OF SCOTLAND PLC	GB	A	F1	bbb	1	A3	P-2	D+	A	A-1	RBS Group	6 Months
STANDARD CHARTERED BANK	GB	AA-	F1+	aa-	1	A1	P-1	B-	AA-	A-1+		12 Months
FEDERAL REPUBLIC OF GERMANY	GE	AAA	F1+			Aaa			AAAu	A-1+u		
DEUTSCHE BANK AG-REGISTERED	GE	A+	F1+	a	1	A2	P-1	C-	A+	A-1		12 Months
KINGDOM OF THE NETHERLANDS	NE	AAA	F1+			Aaa	P-1		AAAu	A-1+u		
ING BANK NV	NE	A+	F1+		1	A2	P-1	C-	A+	A-1		100 Days
BANK NEDERLANDSE GEMEENTEN	NE	AAA	F1+		1	Aaa	P-1	A	AAA	A-1+		12 Months
COOPERATIEVE CENTRALE RAIFFE	NE	AA	F1+		1	Aa2	P-1	B-	AA-	A-1+		12 Months
KINGDOM OF SWEDEN	SW	AAA	F1+			Aaa	P-1		AAA	A-1+		
SVENSKA HANDELSBANKEN-A SHS	SW	AA-	F1+	aa-	1	Aa3	P-1	C	AA-	A-1+		12 Months
SWISS CONFEDERATION	SZ	AAA	F1+			Aaa			AAAu	A-1+u		
CREDIT SUISSE	SZ	A	F1	a	1	A1	P-1	C-	A+	A-1	Credit Suisse Group	100 Days
UNITED STATES (GOVT OF)	US	AAA	F1+			Aaa			AA+u	A-1+u		
JPMORGAN CHASE BANK NA	US	A+	F1	a+	1	Aa3	P-1	C	A+	A-1		12 Months
Supranationals and multi-lateral												
EUROPEAN INVESTMENT BANK	LX	AAA	F1+			Aaa			AAA	A-1+		
EUROPEAN BANK FOR RECONSTRUC	GB	AAA	F1+			Aaa			AAA	A-1+		
COUNCIL OF EUROPE DEVELOPMNT	FR	AA+	F1+			Aaa			AA+	A-1+		
INTL BANK RECON & DEV	US	AAA	F1+			Aaa			AAA	A-1+		
NORDIC INVESTMENT BANK	FI					Aaa			AAA	A-1+		
INTER-AMERICAN DEV BANK	US	AAA	F1+			Aaa			AAA	A-1+		
KREDITANSTALT FUER WIEFERAUF	GE	AAA	F1+			Aaa			AAA	A-1+		