Leicester City Council

WARDS AFFECTED: ALL WARDS (CORPORATE ISSUE)

COUNCIL **21st January 2016**

TREASURY STRATEGY 2016/17

Report of the Director of Finance

1. **Purpose of Report**

1.1 This report proposes a strategy for the Council's borrowing and investments during 2016/17.

2. **Summary**

2.1 Treasury management is the process that ensures that the Council always has enough cash to make the payments that are necessary for its operations, and this involves both borrowing and investment. The Council's borrowing totals some £240 million; and its investments vary from below £190 million to over £240 million depending on circumstances.

2.2 The strategy described in this report reflects a number of factors and these are:-

(a) Current government policy is to fund capital projects by grant. This means that borrowing is only required when we are funding the costs ourselves (which is rare, given the revenue budget outlook); or when borrowing pays for itself. The vast majority of our borrowing has funded historical development. If government policy continues, we do not believe we will need to borrow money for the foreseeable future, it at all;
(b) Investment balances are high, and (at current interest rates) do not attract enough income. They continue to build up because of the lack of any borrowing requirement and the requirement to set money aside to repay debt as part of the revenue budget;
(c) Ideally we would use balances to repay existing debt, but government rules mean there is a financial disincentive to do this;
(d) Since the financial crash of 2008, our investments have been restricted to the UK government, other local authorities and substantial UK banks together with managed funds of cash invested across a diverse range of the world's strongest banks;
(e) changes to rules on bank solvency in 2015 mean that the Government will no longer bear the full cost of "bailing out" a failing bank. Banks which require

capital must first look to commercial depositors (including local authorities).This is known as “bail in”.

2.3 The consequence of the above is that the focus of our strategy is very much on investments. The strategy manages credit risk through the selection of strong counterparties, the selection of investments backed by security and by diversification. Where possible we will use investments to repay debt, but the rationale for doing so will be risk reduction rather than savings (as in the past). The strategy continues the policy, introduced in 2015, of holding up to £20m for projects that support the local economy. One scheme currently under consideration is the “Enterprising Leicester Investment Fund”.

3. **Recommendations**

3.1 The Council is recommended to approve this treasury strategy, and the authorised borrowing limit in paragraph 6.3. Other than limits which apply specifically to 2016/17, the Council is asked to give this strategy immediate effect.

4.0 **Treasury Strategy**

4.1 This document is the treasury strategy for 2016/17. At the beginning of each year the Council receives this report which identifies how it is proposed to borrow and invest in the light of capital spending requirements, interest rate forecasts and economic conditions.

4.2 The strategy covers the matters listed below:

i. the Council’s current debt and investments;
ii. prospects for interest rates;
iii. capital borrowing required;
iv. investment strategy;
v. the balance between holding investments and using them to repay debt (or as a substitute for new borrowing);
vi. debt rescheduling opportunities;

4.3 The key factors to consider are:

i. How much interest the Council can get on its investments.
ii. Ensuring the security of investments.
iii. When loans are due to be repaid and how much it is likely to cost to refinance them at that time.

4.4 The Council supports the finance function of the Leicestershire Combined Fire Authority and from 2016 this support will cover the treasury function. The advice to that authority will reflect the advice given in this report.

5. Current Portfolio Position

5.1 The Council's current debt and investment position is shown in the table below. Members are asked to note that the figures shown represent a snapshot at a single moment in time. The table excludes £26M of debt managed by the County Council on behalf of the City Council and also excludes debt instruments held by contractors for PFI schemes.

Treasury Position As At 28th November 2015	**Amount**
Fixed Rate Funding Public Works Loan Board Stock Market Loans	 £134m £9m £96m
Total Debt	£239m
Investments	£192m
Net Debt	£47m

5.2 The debt is long dated, with repayments mainly due from 37 years to 66 years.

6. Treasury Limits For 2016/2017

6.1 The treasury strategy includes a number of prudential indicators required by CIPFA's Prudential Code for capital finance, the purpose of which is to ensure that treasury management decisions are affordable and prudent. The recommended indicators and limits are shown below. One of these indicators, the "authorised limit" (para 6.3 below), is a statutory limit under the Local Government Act 2003.

6.2 The first indicator is that over the medium-term net borrowing will only be for capital purposes – i.e. net borrowing should not, except in the short-term, exceed the underlying need to borrow for capital purposes (the "capital financing requirement"). We do not anticipate any difficulties in complying with this requirement.

6.3 The Council is required to set an "authorised limit" on borrowing which cannot be exceeded. The approved limits recommended for 2016/17 are:

	£m
Borrowing	280
Other forms of liability	145
Total	425

6.4 "Other forms of liability" relates to loan instruments in respect of PFI schemes and to pre-unitary status debt managed by the County Council (and charged to the Council). The remainder, "borrowing", refers to conventional loans. In practice, the treasury strategy only manages the borrowing component.

6.5 The Council is also required to set an "operational boundary" on borrowing which requires a subsequent report to scrutiny committee if exceeded. In practice, the treasury strategy only manages the borrowing component. The approved limits recommended for 2016/17 are:

	£m
Borrowing	270
Other forms of liability	145
Total	415

6.6 Recommended upper limits on fixed and variable rate debt exposures are shown in the table below. The figures shown are the principal sums outstanding on "borrowing".

	£m
Fixed interest rate	240
Variable interest rate	60

6.7 The Council has also to set upper and lower limits for the remaining length of outstanding loans that are fixed rate as a percentage of the total of all loans. This table also excludes other forms of liability. Recommended limits are:

Upper Limit

	%
Under 12 months	30
12 months and within 24 months	40
24 months and within 5 years	60
5 years and within 10 years	60
10 years and within 25 years	100
25 years and over	100

We would not normally borrow for periods in excess of 50 years.

Lower Limit

	%
Less than 5 years	0
Over 5 years	60

7. Borrowing and Investment Levels

7.1 It appears likely that the Council's requirement to borrow is now at a peak and is likely to decline. Until 2011, the Government provided support for capital expenditure by a combination of capital grants and "supported borrowing" allocations. Supported borrowing allocations enabled the Council to borrow money, with the costs of financing the debt being met by Revenue Support Grant. Since then Government support has been wholly grant funded.

7.2 The law and codes of practice require that money must be set aside in the budget each year to repay previous years' debt. These rules, very broadly, seek to ensure that the Council's borrowing is repaid over the life of the projects which have been financed. Hence, in the absence of new borrowing, the Council's net borrowing requirement will decline.

7.3 The Council undertakes a number of projects which are not Government supported and can borrow for these – this is known as "unsupported" or "prudential" borrowing.

7.4 In practice, it has not been necessary to undertake fresh borrowing for several years. We have instead used money set aside to repay debt or other available cash.

7.5 Beyond 2016/17 the money set aside to repay debt will not be used for planned capital spending as Government grant will be used. This does not necessarily mean that we shall immediately repay debt, unless it is beneficial to do so - as noted above for a number of years we have not borrowed but have instead used cash balances as an alternative to borrowing.

7.6 The cumulative impact of these policies is that we have anticipated the need to repay debt and a cumulative total £220m of balances have been used as an alternative to external borrowing. Currently this saves the Council approximately £8m per year in interest.

7.7 Even after using balances as an alternative to borrowing, large cash balances remain. In theory at least, much of these are temporary in nature and held against commitments - for example grants received in advance of expenditure, and funds earmarked for committed capital projects. In addition the budget for 2016/17 plans for reserves to be spent. The level of balances is expected to decline over 2016/17 and later years. However, it is estimated that over the medium term we will have around £50m of investments which we will never spend (unless Government policy changes).

Interest Rates

7.8 Interest rates, both long term and short term are very low by historical standards. Our treasury advisors, Arlingclose, forecast that short term rates will rise from 2016 but that the rate of increase will be slow. By the end of 2017 they see short term rates of 1.75% and beyond that, over the medium term they do not see short term rates rising beyond 3% to 3.5%, and such rates are lower than the historical long term average. If our current position continued we would have a high level of investments earning very little in the short term with only a modest improvement over the medium term.

7.9 At the time of writing this report the interest rate on fixed rate borrowing from the PWLB for 50 year loans is 3.4% and our advisors see this rising to 4.2% by the end of 2017. This is historically extremely cheap, but we have no need to take it.

Investment Risks

7.10 Within the Eurozone, whilst economic and financial tensions have eased many underlying issues remain to be resolved. A reduction in the rate of the growth of the world economy has been a major contributor to the fall in the price of oil and other commodities with negative impacts on the economies of producer countries which may also be adversely affected by currency flows as US rates start to rise. The direct impact of these factors fall outside the UK, but due to the interconnected nature of financial markets and the world economy there could be an indirect impact on the UK and on the credit risk of investments. The most significant risk to the UK economy arising from a persistence of the recent volatility in the Chinese stock markets and Renminbi exchange rate might be a slowing of global economic growth as a result of weaker confidence.

7.11 During 2015 changes were made to reduce the need for taxpayer bailouts when banks run into trouble and these increased the risk to large investors - the deposits of small investors now take priority over the deposits of larger investors such as the Council and formal mechanisms now require that large investors are "bailed in" to any bank restructuring (i.e. a proportion of their investments will be converted into bank equity, which may have little or no value) before any taxpayer bailout takes place. However, measures are progressively being put in place to strengthen banks' balance sheets, a process that will not be complete until 2019, and this will serve to reduce the risk to investors.

7.12 Within an environment of low interest rates and in which the risk of bank failure falls on large investors, our treasury strategy should emphasise risk reduction, and an increase in investment return whilst striking a cautious balance between risk and reward.

7.13 Our advisors provide tools to help us monitor the credit risk of bank and building society investment. These include the monitoring of credit ratings and share prices coupled with an analysis of balance sheets of banks and building societies.

Investments up to One Year

7.14 Some of our investments are primarily held to manage the Council's cashflow for periods of up to one year.

7.15 We will continue to place deposits with banks and building societies. Our treasury advisors provide information and advice to monitor ‘bail in’ risk.

7.16 We propose to make greater use of overnight deposit facilities offered by our bankers, Barclays Bank, because this can be the most cost effective and operationally efficient way of dealing with day to day cashflows when these are not large. Currently the investment strategy permits a maximum investment limit for Barclays of £20M of which £10M is assigned to deposits with a further £10M assigned to longer term investments backed by security. It is proposed that the limit for longer term investments be reduced to £5M and that the limit for deposits be increased to £15M. The additional £5M could only be placed on overnight deposit, which is considered to be safer than longer deposits as the cash can be quickly withdrawn if the bank shows signs of financial stress.

7.17 We will continue to place deposits with other local authorities and with the Government through its Debt Management Office. Such investments are highly secure, although interest rates are also very low.

7.18 We propose to add repurchase agreements (‘REPO’) as an approved investment. These are short term investments akin to deposits backed by security, and are made with financial institutions. This security is achieved by the contractual arrangements which secure the investment against a government bond or other security provided by the borrower. The availability of this security enables us to lend to banks we would not otherwise chose to lend to.

7.19 We will continue to use money market funds. These are pools of highly credit rated investments such as deposits and short dated bonds which reduce risk by diversification. The funds include the strongest international banks and are actively managed preventing us having to monitor the underlying investments. Cash is repayable on demand making these useful tools for managing the Council’s short-term cashflows (particularly if we make the medium term investments described below).

7.20 We are also proposing to make use of funds similar to money market funds, often described as money market plus funds. These still pool highly credit rated investments but have a longer average maturity than money market funds. These are useful for managing cash over periods from between one month ahead to up six months ahead and offer higher returns than money market funds. Whilst the fund may under-perform if it misjudges the pace and direction of interest rates it should not under-perform because of credit losses. Such funds may make use of derivatives where this supports the objectives of the fund (in terms of security of capital and return). Importantly, however, derivatives are not used for outright speculative purposes. We will not invest in any funds where an analysis of investment objectives and prospectus indicates any significant risk to capital. The decision to invest in such a fund would be made the by the Director of Finance in consultation with the City Mayor so as to provide assurance that only appropriate funds are selected.

7.21 Another investment with a similar underlying structure is the short-dated bond fund. These funds lend less money to banks and most is invested in short-dated government bonds. The return on such funds is low because of the low interest rates on short-dated bonds and because of the fund manager's fees. This is an option that we might consider in adverse market conditions if we decided to reduce our credit exposure to banks.

Longer Term Investments

7.22 Historically, our investments represent money received in advance of need and monies set aside to repay debt or reserves. Consequentially, they are a short term resource. However, the changes described in this report suggest around £50m is now best seen as a longer term resource.

7.23 This is because, even though the Council has more debt than investments, we will continue to have £50m of investments we will not be able to use.

7.24 Over the next two years we expect our cash balances to remain high and during 2016/17 it is suggested that we may hold up to £120M in investments with a maturity in excess of one year. Over subsequent years we see these balances declining.

7.25 Conventional bank deposits with a maturity in excess of one year are not considered appropriate, even for the strongest banks. Whilst the risk of being "bailed in" is considered to be low it is real and the interest rates offered are not considered adequate to reflect this risk. We shall continue to deposit money with other local authorities for periods up to two years.

7.26 We will continue to invest in "covered bonds" . Here money is loaned to a bank for a period of between one to five years and is secured on bank assets, such as the bank's mortgage portfolio. They are similar to REPOs discussed above.

7.27 In theory, we would like to use investments to repay debt. This has always required a premium to be paid (i.e. why would a lender accept repayment of a loan paying 4% which it cannot reinvest at the same rate?). This does not necessarily make the deal uneconomic – it simply ensures debt is repaid at fair value. However rules recently imposed have increased the premium payable. Whilst we can, and should, use investments to repay some debt we will need to be selective about the loans to repay, and recognise we are primarily doing it to reduce investment risk rather than to make savings for the revenue budget. This strategy permits us to do so.

7.28 We will continue to hold cash available for a local investment fund. We can support capital projects, at a marginal cost to us of 0.5% in the short-term (i.e. what we lose on the investments), and not much more in the medium term. We would be able to fund schemes with a short life at rates exceeding what we get on our investments. The fund would be less suitable for funding longer term projects, as rates beyond 10 years' time are not knowable; however, schemes with secure longer term income streams may be viable. At the time of preparing this report proposals are in hand for an "Enterprising Leicester Investment Fund" of up to £10M. We will continue to appraise other local investment opportunities to generate future revenue income and capital growth.

7.29 Our investment strategy permits a range of bonds. These are:

(a) UK government bonds (gilts). At present these are not attractive compared to other investment options but are a very safe option in adverse market conditions and can be easily sold.

(b) Bonds issued by the new Local Authority Bond Agency, which is being set up to lend to other local authorities following an initiative of the LGA. Rates payable are likely to be good. However, we remain unconvinced that many authorities are actually going to borrow from the agency and there may therefore not be any need for our cash (many authorities are in the same position we are);

(c) We can look to lend long-term to a high quality institution (such as the European Investment Bank, Transport for London or another local authority).

7.30 It is proposed that we invest in the CCLA Local Authorities Property Fund. This fund invests in commercial property and only serves local authorities. CCLA is owned by its clients who are local authorities and charities. Its governance structure includes representatives of local authorities and other clients. In presentations it has presented a credible approach to investment and has a good track record.

7.31 The Royal Institute of Chartered Surveyors (RICS), a respected industry body which operates at arms-length from individual property funds, reports a healthy and improving property market.

7.32 It is considered that it would only be appropriate to invest in this fund if we expected to retain our holding for at least five years, and we expect this to be the case. There are two reasons for this. One is that when new funds are put into the fund new properties are bought with this investment. These purchases incur costs such as stamp duty and legal fees and these costs are passed back to new investors. The gap between the initial investment and its value is expected to close over time as income is realised and the value of the properties rise. A further consideration is that the value of property might fall and a sufficiently long investment period is required to ride out any dips in the property market,

7.33 The fund is expected to pay dividends at a rate of 4% to 4.5% and this exceeds current cash returns of 0.5%. Over the next 3-4 years we propose to apply the surplus over cash returns to firstly pay down the initial costs and also to create a buffer against any fall in property value. Thereafter we would take the full level of income.

8. <u>Debt Rescheduling & Premature Repayment of Debt</u>

8.1 This report proposes the premature repayment of debt using cash that is currently invested.

8.2 Rescheduling is also an option that may be considered. The only difference is that instead of using existing cash balances to fund the repayment we would fund it by borrowing a new loan on more attractive terms than the old loan.

8.4 In practice the premature repayment of debt will incur a premium, in which case the financial calculations become more complex, however, the principle remains the same.

8.5 In practice, debt rescheduling will be unlikely unless we successfully run down investment balances first.

9. **Managing Credit Risk and Other Risk**

9.1 This report outlines the investment strategy. Further details are given in the appendix, which sets the criteria that we apply to ensure that we only invest with borrowers of high credit worthiness. It also deals with measures to manage other key issues, for example ensuring access to liquid funds.

9.2 Investments will always comply with the minimum credit ratings specified in this strategy but other factors will be taken into account as contra-indicators and these will include share price, the cost to investors of buying insurance against default and political and economic developments (especially those to do with the Eurozone). Account will also be taken of credit worthiness opinions of our Treasury Advisors based on analyses of institutions' accounts.

9.4 This investment strategy is based on the advice of Arlingclose, our Treasury Advisors and they have consistently taken a cautious approach (for example they advised against investing in Icelandic banks).

10. **Sensitivity of This Strategy and Risk Management**

10.1 This strategy is based on the view that the economic outlook for 2016/2017 and later years carries a number of significant risks.

10.2 Short-term interest rates are expected to rise slowly over the medium term and the main risk is that they rise faster and/or sooner than expected. If this happens some individual investments may perform worse than expected, but overall the impact on the Council is likely to be that its investment income increases because most of its investments pay interest at short or variable rates.

10.3 There is a related risk that long-term rates rise faster than expected. If this happens some of the investments proposed in this report would decline in value. At the same time debt repayment and debt rescheduling options may become more financially beneficial.

10.4 If long term interest rates decrease, or rise slower than expected then some of the medium term investments proposed in this report would increase in value.

However, future debt repayment/debt rescheduling opportunities will become less favourable. Overall the short-term impact on the Council would be limited.

10.5 The main concern around lower than expected interest rates would be the underlying reason. For example the continuation of low interest rates seen during the current year reflects slower than expected growth in the world economy, something that has the potential to feed into increased credit risk.

10.6 The future level of cash balances is a material consideration. If these are higher than forecast (or decline more slowly than expected) then the Council's investments will increase, and so will investment income. The converse will be true if they are less than forecast or decline more slowly. These impacts will be limited by the low level of interest rates.

10.7 The Council has £96 million of market loans at favourable interest rates on which the lender has the right to periodically propose an interest rate increase. These loans are known as LOBOs. We have the option to refuse a proposed rate increase and to repay the loans, but would then have to borrow new loans at the prevailing interest rates. In the current interest rate environment the financial risk is believed to be low - it's unlikely that lenders will exercise their option and if they did (which we would probably welcome) the cost of replacement loans (if needed) could be kept low by borrowing short to medium term loans. We would give serious consideration to rescheduling or repaying these loans so as to reduce this risk, even if this did not generate a financial saving or came at a small cost.

10.8 Members are asked to note that LOBOs have recently received a bad press, with allegations that authorities were misled by advisors. We undertook most of this borrowing to refinance an earlier stock issues, at a time when there was limited availability of sources of borrowing. The exercise as whole saved money, and was worthwhile.

10.9 The proposed investment in the CCLA Local Authorities' Property Fund exposes the Council to declines in the value of commercial property. The fund benefits from a statutory provision such that this would not impact on the Council's revenue position (ie this would not reduce its ability to spend money on services) unless it sold its investment. These risks are mitigated by the expectation that the investment would be held for a minimum of five years over which time these risks would be lessened. These risks are further mitigated by the proposals to retain income in excess of cash returns to create a buffer.

10.10 Where, exceptionally, immediate action that does not comply with this strategy will benefit the Council such action will be taken, and will be reported to the City Mayor and the Overview Select Committee.

11. Housing Revenue Account

11.1 The Housing Revenue Account (HRA) operates under a self-financing regime in which it has earmarked debts separate from those of the General Fund. Where appropriate, a separate loans strategy should be operated for each pool. However, the requirements of the HRA for 2016/17 are straightforward in that little new borrowing is required and the strategy described in this report is appropriate for the HRA.

12. Treasury Management Advisors

12.1 Since January 2008 the Council has employed Arlingclose as treasury advisors. The service provides advice on our borrowing and investment policies and strategies. The annual fee for this service is £22,000.

12.2 There have been many challenges in 2015/16 and Arlingclose's performance has been good.

13. Leasing

13.1 The Council is likely to acquire equipment, principally vehicles, to the value of approximately £1.5 million that would be suitable for leasing.

13.2 Before leasing is pursued consideration will be given to the options of finance leasing, operational leasing, and prudential borrowing. At present prudential borrowing is more cost effective. This judgement takes into account the costs of the two forms of finance over the expected economic life of the asset. In addition, because of lease termination charges it is more expensive to dispose of a leased vehicle than an owned vehicle, and this is important because the Council is reviewing the utilisation of the existing fleet.

13.3 In practice, prudential borrowing will mean use of our cash balances.

14. Financial and Legal Implications

14.1 The proposals are in accordance with the Council's statutory duties under Local Government Act 2003 and statutory guidance, and comply with the CIPFA Code of Practice on Treasury Management. In accordance with the Council's Constitution the strategy requires full Council approval.

15. **Other Issues**

OTHER IMPLICATIONS	YES/NO	Paragraph References Within Supporting information
Equal Opportunities	No	
Policy	No	
Sustainable and Environmental	No	
Crime and Disorder	No	
Human Rights Act	No	
Elderly/People on Low Income	No	
Corporate Parenting	No	
Health Inequalities Impact	No	

16. **Background Papers**

16.1 Background information is available on the files of the Director of Finance.

17. **Consultation**

17.1 Arlingclose Ltd.

18. **Author**

18.1 The author of this report is David Janes of the Financial Services Division on extension 37 4058

Alison Greenhill
Director of Finance.

ANNUAL INVESTMENT STRATEGY 2016/2017

1. Introduction

1.1 This investment strategy complies with the DCLG's Guidance on Local Government Investments and CIPFA's Code of Practice.

1.2 The Investment Strategy states which investments the Council may use for the prudent management of its treasury balances. It also identifies other measures to ensure the prudent management of investments.

1.3 It does not cover the use of investments for local economic projects for which separate policies will be prepared.

2. Investment Objectives & Authorised Investments

2.1 All investments will be in sterling.

2.2 The overriding policy objective for the Council is the prudent investment of its balances. The Council's investment priorities are
(a) the **security** of capital and
(b) **liquidity** of its investments.

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

2.4 The Council will not borrow monies purely to invest or on-lend.

2.5 The following part of this appendix specifies how the Council may invest, with whom and the credit worthiness requirements to be applied.

2.6 The credit criteria in respect of loans to financial institutions are stated below. We only lend to banks and building societies based in the UK.

Investment Type	**Maximum Investment Period**	**Minimum Credit Rating**	**Individual Lending Limit**	**Limit for Investment Type**
Deposits – Credit Rated Banks and Building Societies	366 Days	A long term rating of A and a short term rating of F1	£10m.	£80m
	6 months	A long term rating of A- and a short term rating of F2	£10m.	
	100 days or less	A long term rating of BBB+ and a short term rating of F2	£10m Additional £5m overnight limit for Barclays Bank	
Covered Bonds	5 years	A long term rating of AA	£20m	Included in above
REPO Agreements	1 year	To be no less secure than a deposit	£20m	Included in above
Deposits – unrated building societies	6 months	N/A – Advice taken from Treasury Advisors	£1m	£10m

2.7 The credit criteria applied to other investments are as detailed in the table below. The quasi-public sector refers to such bodies as Transport for London (TFL) and the Student Loan Company which deliver public services and which are closely linked to the Government or to local government.

Investment Type	Counterparty	Maximum Investment Period	Minimum Credit Rating	Individual Lending Limit	Limit for Investment Type
Deposits	Local authority	2 Years	None required	£20m	£130M
Bonds	Local Government Bonds Agency	To be agreed	A long term rating of AA-	£30m	
Bonds, Bills and Deposits	UK Public Sector & Quasi-Public Sector	To be agreed	A long term rating of AA-	£30m	£60m
Deposits and Treasury Bills	UK Government / UK Government Guarantee	Unlimited	None required	Unlimited	Unlimited
Money Market Funds, Money Market Plus Funds and Short-Dated Bond Funds	Various Fund Managers	3 months	-	£20m	£60m
		7 days	-	£20m	£80m
Bonds	International Development Banks	5 Years	AA plus backing of one or more G7 countries.	£10m	£40m
Local Authorities' Property Fund	CCLA	-	Not Applicable	£10m	£10m

2.8 The table below specifies authorisations and consultations necessary prior to investments being added to the approved lending list.

Investment Type	Counterparty	Authorisation / Consultation
All	Quasi-UK Public Sector	Approval to named counterparty and class of investments by Director of Finance in consultation with the City Mayor.
Bond	International Development Banks	
REPO Agreements	To be agreed	
Money Market Funds, Money Market Plus Funds and Bond Funds	To be agreed	Director of Finance to consider a report recommending any new funds to be added to the approved lending list.

2.9 A 2% margin of error is permitted on the limits specified in this document when these limits are breached simply because interest has been paid and has been added to the account balance.

2.10 The following factors apply to all deposits.

i. Deposits may be for fixed terms or may be repayable at the option of the borrower and/or the lender and may or may not be negotiable
ii. Deposits or other investments may be agreed in advance that run from an agreed future date.
iii. For the purposes of applying the credit rating criteria laid down in this AIS, investments agreed in advance shall be treated as running from the date they are agreed. However, where an investment is agreed 10 or fewer working days in advance it shall be treated as running from the date the cash is deposited.
iv. Interest rates may be fixed at the outset or may be varied by agreement. They may also be varied by reference to market rates or benchmarks (eg LIBOR), provided that such rates or benchmarks are capable of independent verification.
v. An investment with an organisation with an unconditional financial guarantee from a parent organisation may be treated as if it were an investment with that parent organisation subject to consideration of any contra-indicators that such a guarantee may not be effective.
vi. Where an institution is part of a group then limits shall be set both at group level and at the level of the individual institution

3. Security of Capital

3.1 The Director of Finance will only invest with the most secure counterparties. This section of the AIS describes how these are identified.

Banks and Rated Building Societies

3.2 The Director of Finance will maintain a list of approved counterparties.

3.3 The Council utilises credit ratings published by Fitch Ratings. Investments are also permitted on the basis of equivalent ratings issued by Moody's Investors Services or Standard and Poor's. In the absence of good reasons to the contrary, decisions will be based on the lowest rating. When applying credit rating criteria it shall be assumed that investments shall be held to maturity. Where, however, the Council has an unqualified option to require the investment to be fully repaid at an earlier date, then for the purposes of applying these criteria it shall be assumed that the investment shall run until the earliest repayment date.

3.4 Credit ratings will be monitored:

i. All credit ratings for investments being actively used will be monitored monthly and credit rating alerts will be acted on as soon as practicable (the next working day or sooner);
ii. If a body is downgraded with the result that it no longer meets the Council's minimum criteria, the further use of that body will cease;
iii. A deterioration in credit ratings will not automatically lead to a decision to terminate the investment prematurely (and in many cases there will be no contractual provision to permit this).
iv. If a counterparty is upgraded so that it fulfils the Council's criteria, its inclusion will be considered and put to the Director of Finance for approval;
v. If other market intelligence suggests that credit ratings give an over-optimistic view of credit-worthiness, this will be taken into account.

Unrated Building Societies

3.5 For unrated building societies the Director of Finance will maintain a list of approved counterparties. The credit worthiness of unrated building societies will be assessed using advice from the Council's treasury advisors. This advice shall consider the risk of financial stress by reference to the most recently published accounts and by reference to any other publically available market information. In particular regard shall be had to the capital held to absorb financial shocks, liquidity and profitability. The advice shall also consider the extent of the financial loss in the event of a "bail in".

3.6 For all investments regard shall be had to the prospect of support from a parent institution or a strong government, though the role of the latter is now limited by "bail in" rules. In addition for all categories of investments regard will be had to other sources of information including (where applicable) the price of Credit

Default Swaps, share prices, developments, news, economic data and market sentiment. Regard shall be had to the likely impact of any “bail in”. Regard shall also be had to credit-worthiness assessments of the Council’s treasury advisors.

4. Investment balances / Liquidity of investments

4.1 The minimum percentage of its overall investments that the Council will hold in short-term investments is 40% and the Council will maintain liquidity by having a minimum of £30m of deposits maturing within 2 months (subject to the availability of funds to invest). There is a regular monthly cycle to the Council’s cashflow and these limits apply to the peak cash balance just ahead of the payday. These liquidity targets are guidelines and occasional and temporary deviations from these limits will be permitted on a planned basis where there are good reasons.

4.2 No more than £120m will be held in investments in excess of 366 days. For these purposes investment in money market funds, money market plus funds and short-dated bond funds shall be treated as investments held for less than 366 days and investments in the CCLA Local Authorities’ Property Fund shall be treated as an investment in excess of 366 days.