For General Release

REPORT TO:	**Cabinet 20th February 2017**
AGENDA ITEM NO:	**6.2**
SUBJECT:	**Treasury Management Strategy Statement, Minimum Revenue Provision Policy Statement & Annual Investment Strategy 2017/2018**
LEAD OFFICER:	**Richard Simpson Executive Director of Resources (Section 151 Officer)**
CABINET MEMBER:	**Cllr Simon Hall , Cabinet Member for Finance and Treasury**
WARDS:	**All**

CORPORATE PRIORITY/POLICY CONTEXT:

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 initially before considering investment return.

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. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

FINANCIAL IMPACT:

This report sets out the Council's Treasury Management objectives, which are to manage the Council's cash flows, borrowing and investments minimising the level of risk exposure; maximising investment yield returns; and ensuring that capital expenditure and financing plans are prudent, affordable and sustainable. The report details the activities that will be undertaken by the Council in 2017/2018 and the capital borrowing needs of the Council for 2017/2018:-

	£m	Total £m
1. In Year Borrowing Requirement (Net)	349	
		349
2. Total Interest Payable on Debt		
- chargeable to Housing Revenue Account (HRA)	12	
- chargeable to General Fund (GF)	20	
		32

In addition the report details the investment activities and the estimated level of income earned. **Investment Income** net of interest apportioned to Non-General Fund accounts e.g. HRA and other cash balances:- (0.750)

(0.750)

KEY DECISION REFERENCE NO.:

This is not an executive key decision – this is reserved to the full Council for decision as part of the budget and policy framework.

1. RECOMMENDATIONS

1.0. The Leader of the Council has delegated to the Cabinet the power to make the decisions set out in the recommendations below.

The Cabinet is asked to recommend to Full Council that it approve:

1.1. The Treasury Management Strategy Statement 2017/2018 as set out in this report including the recommendations that:

1.1.1. The Council takes up the balance of its 2016/2017 borrowing requirement and future years' borrowing requirements, as set out in paragraph 3.6.

1.1.2. That for the reasons detailed in paragraph 3.11, opportunities for debt rescheduling are reviewed throughout the year by the Executive Director of Resources and Section 151 Officer and that, he be given delegated authority, in consultation with the Cabinet Member for Finance and Treasury and in conjunction with the Council's independent treasury advisers, to undertake such rescheduling only if revenue savings or additional cost avoidance can be achieved at minimal risk in line with organisational considerations and with regard to the Housing Revenue Account (HRA) as set out in the Council's Finance Strategy 2016-2020.

1.1.3. That delegated authority be given to the Executive Director of Resources and Section 151 Officer, in consultation with the Cabinet Member for Finance and Treasury, to make any necessary decisions to protect the Council's financial position in light of market changes or investment risk exposure.

1.2. The Annual Investment Strategy as set out in paragraph 3.14 of this report.

1.3. That the Authorised Borrowing Limits (required by Section 3 of the Local Government Act 2003) as set out in paragraph 3.7 and as detailed in **Appendix C** be as follows:

2017/2018	2018/2019	2019/2020
£1,234.442m	**£1,365.442m**	**£1,372.442m**

The Prudential Indicators as set out in **Appendix C** of this report.

1.4. The Annual Minimum Revenue Provision Policy Statement (required by SI 2008/414) as as set out in **Appendix D** of this report.

1.5. The Council's authorised counterparty lending list as at 31st December 2016 as set out in **Appendix E** of this report and the rating criteria set for inclusion onto this list.

2. EXECUTIVE SUMMARY

2.1. The Council defines its treasury management activities as:

"The management of the Council'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."

2.2. The CIPFA Code of Practice on Treasury Management in the Public Services (updated 2011) was approved and adopted by the Council on 10 February 2013 (Minute A31/13 refers).

2.3. The Code recommends that the Council approve before the commencement of each financial year:

1. A Treasury Management Strategy for borrowing;
2. An Annual Investment Strategy setting out the Council's policies for managing its investments; and
3. A statement on the Council's policy for its annual Minimum Revenue Provision (MRP) (repayment of debt).

2.4. The Local Government Act 2003 requires the Council to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities, 2011, to ensure that the Council's capital investment plans are affordable, prudent and sustainable. In particular, the Prudential Code requires the Council to set a number of Prudential Indicators for the next three financial years. This report, which incorporates these indicators, also details the expected treasury activities for the year 2017/2018, set in the context of the longer term planning forecasts for the organisation. The implications of these key indicators function as the overriding control and guidance mechanism for the future capital programme and the revenue consequences that arise for the Council in future financial years.

2.5. It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 32 requires a local authority to calculate its expenditure requirement for each financial year to include the revenue costs that flow from capital financing decisions.

3. DETAIL OF THE REPORT

3.0 The strategy for 2017/2018 covers two main areas:

Capital issues
- The capital plans and borrowing need (paragraphs 3.1 and 3.2);
- The minimum revenue provision (MRP) policy (paragraph 3.3);.

Treasury management issues
- Policy on use of external service providers paragraph 3.4);
- The Current Treasury Position (paragraph 3.5);
- Borrowing Requirement (paragraph 3.6);
- Treasury indicators which limit the treasury risk and activities of the Council (paragraph 3.7);
- Prospects for Interest Rates (paragraph 3.8) ;

- The Borrowing Strategy (paragraph 3.9);
- The policy on borrowing in advance of need (paragraph 3.10);
- Debt Rescheduling and Repayment (paragraph 3.11);
- Sources of Finance (paragraph 3.12);

Annual Investment Strategy

- The investment policy (paragraph 3.13);
- The Annual Investment Strategy (paragraph 3.14);
- Treasury Limits (paragraph 3.15) and
- Prudential Indicators (paragraph 3.16).

CAPITAL ISSUES

3.1. Capital Expentiure and borrowing need

3.1.1 The 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.

Capital expenditure

3.1.2 In order to fufil its ambitions for Croydon the Council has an extensive capital programme. This includes funding for: a Revolving Investment Fund (RIF), set up to fulfil the Council's Growth Promise and initially be principally focused on the delivery of development and regeneration on Council Land; a Development company also focused on regeneration in the borough, primarily homes; and a Growth Zone, which invests in priority infrastructure to help deliver sustainable economic growth in Croydon. The RIF, Growth Zone and Development company are expected to create their own revenue streams in order to repay the debt taken out to finance the expenditure.

3.1.3 Members are asked to note the capital expenditure forecasts given in the table below:

Table 1: Capital Expenditure Forecasts (2016 / 2020)

Capital expenditure £m	2016/2017 Estimate	2017/2018 Estimate	2018/2019 Estimate	2019/2020 Estimate
Non-HRA	127.746	386.774	148.866	28.007
HRA	25.724	27.051	27.051	27.051
Total	**153.470**	**413.825**	**175.917**	**55.058**

3.1.4 This financing need excludes other long term liabilities, such as PFI and leasing arrangements which already include borrowing instruments.

3.1.5 The Council's financing need is funded from various capital and revenue resources plus borrowing.

3.2 The Council's borrowing need (the Capital Financing Requirement)

3.2.1 The Council's Capital Financing Requirement (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 assets life. The CFR includes any other long term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes.

3.2.2 The Council's estimated CFR is detailed in the table below:

Table 2:Estimated Capital Financing Requirement 2016 / 2020

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m
	Forecast	**Estimate**	**Estimate**	**Estimate**
Capital expenditure	153.470	413.825	175.917	55.058
Less amount funded from resources	(98.748)	(58.598)	(37.345)	(39.71)
Gross In Year Borrowing Requirement (CFR)	**54.722**	**355.227**	**138.572**	**15.348**
Less In Year Minimum Revenue Provision (MRP) for debt repayment.	(5.547)	(5.993)	(7.134)	(7.895)
In Year Borrowing Requirement (Net)	**49.175**	**349.234**	**131.438**	**7.453**
2. Add previous years' outstanding borrowing requirement (not taken in that year)	0.00	0.0	0.0	0.0
3. Borrowing – to replace maturing debt	12.5	26.0	11.0	10.0
4. Less loans taken up in-year	(59)	0.0	0.0	0.0
In Year Borrowing Requirement outstanding	**2.675**	**375.234**	**142.438**	**17.453**

3.3 Minimum Revenue Provision

3.3.1 Minimum Revenue Provision (MRP), often referred to as a 'provision for the repayment of debt', is a charge to revenue in relation to capital expenditure financed from borrowing or through credit arrangements.

3.3.2 The annual MRP charge was previously determined under Regulation but is now determined under Guidance ('the Guidance') issued by the Secretary of State in February 2008. There is now a statutory duty, embodied within Statutory Instrument 2008 No.414 s 4, which lays down that:

'A local authority shall determine for the current financial year an amount of minimum revenue provision that it considers to be prudent.'

3.3.3 MRP only applies to the General Fund. There is no requirement to make a MRP charge for the Housing Revenue Account (HRA).

3.3.4 Along with the above duty, the Government issued guidance in February 2008 which requires that a statement on the Council's policy for its annual MRP should be submitted to Full Council for approval before the start of the financial year to which the provision will relate.

3.3.5 The Executive Director of Resources is responsible for ensuring that accounting policies and the MRP policy complies with the statutory Guidance in determining a prudent level of MRP.

3.3.6 As part of the mid-year review of the 2015/2016 Minimum Revenue Provision Statement, the Council's General Purposes and Audit Committee approved a revised Annual Minimum Revenue Provision Statement on 9 December 2015 (Minute A62/15). The Council's MRP Policy Statement for 2017/2018 also adopts these revisions and is attached at Appendix D.

TREASURY MANAGEMENT ISSUES

3.4 Treasury management consultants

3.4.1 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 will ensure that undue reliance is not placed upon our external service providers. It also 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.

3.5 The Current Treasury Position

3.5.1 The Council's Treasury position as at 31st December 2016 comprised:

Table 3: Borrowing by the Council as at 31 December 2016

		Principal £m	Average Rate %
Fixed Rate Funding	- PWLB[1]	614.926	3.85
	- Other [2]	0.315	3.50
	- LOBO [3]	79.500	3.91
	- Local Authorities[4]	52.500	1.10
	- Amber Green LEEF 2LLP	3.575	1.80
	- European Investment Bank	44.745	2.0
Variable Rate Funding	- LOBO [3]	60.000	4.23
Internal Loans – Trust Funds		0.006	0.23
Total External Debt as 31/12/2016		**855.567**	**3.60**
Additional			
GF borrowing requirement outstanding for 2016/2017		2.675	
HRA borrowing requirement outstanding for 2016/2017		0	
Estimated Debt as at 31/03/2017		**858.242**	**3.60**

1. PWLB is the Public Works Loan Board, the branch of Government that is the principle lender to local authorities. Included within this amount is the £223.1m borrowed for the HRA self-financing settlement made on 28/3/2012.

2. Other relates to 3 ½% Irredeemable Stock which was issued by this Authority in the past.

3. Lender's Option Borrower's Option (LOBOs) loans are commercial debts with options for the lender to vary the rate at pre-set intervals. If the option is exercised, then the Council can either accept the new rate or repay the loan with no penalty.

4. As an alternative to borrowing from the Government, several local authorities have come to the market offering loans at competitive rates.

3.5.2 The Council's debt maturity profile is included in **Appendix A**.

Table 4: Temporary Investments as at 31 December 2016

	Principal £m	Average Rate %
Temporary investments outstanding as at 31/12/2016	**127.96**	**0.47**
Estimated temporary investments outstanding as at 31/03/2017	**95.00**	**0.53**

3.6 The Borrowing Strategy and Borrowing Requirement

3.6.1 The Council's capital expenditure plans are set out in Sections 3.1.1, 3.1.2 and 3.1.3. The treasury management function ensures that the Council's cash is organised in accordance with the 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 strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

3.6.2 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.

Table 5: Borrowing and the Capital Financing Requirement 2016 / 2020

£m	2015/2016 Actual	2016/2017 Estimate	2017/2018 Estimate	2018/2019 Estimate	2019/2020 Estimate
External Debt					
Debt at 1 April	766.670	808.633	858.242	1,192.242	1,165.242
Expected change in Debt	41.963	49.609	334	131	7
Actual gross debt at 31 March	808.633	858.242	1,192.242	1,323.242	1,330.242
The Capital Financing Requirement	**880.713**	**939.34**	**1,288.58**	**1,420.01**	**1,427.47**
Under/(over) borrowing	72.08	81.098	96.338	96.768	97.228

Note: this calculation does not allow for the impact of internal borrowing which has the effect of reducing real borrowing (see Table 2, above).

3.6.3 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 2017/2018 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.

3.6.4 The Executive 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.

3.7 Treasury Indicators: limits to borrowing activity

3.7.1 **The operational boundary**. This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

Table 5: The operational boundary for 2016 / 2020

Operational boundary £m	2016/2017 Estimate	2017/2018 Estimate	2018/2019 Estimate	2019/2020 Estimate
Debt	858.242	1,192.242	1,323.242	1,330.242
Other long term liabilities	2.2	2.2	2.2	2.2
Total	860.442	1,094.442	1,325.442	1,332.442

3.7.2 **The authorised limit for external debt.** A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

3.7.3 This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

3.7.4 The Council is asked to approve the following authorised limit:

Table 6: The Authorised Limit for External Debt 2016 / 2020

Authorised Limit £m	2016/2017 Estimate	2017/2018 Estimate	2018/2019 Estimate	2019/2020 Estimate
Debt	898.242	1,232.242	1,363.242	1,370.242
Other long term liabilities	2.2	2.2	2.2	2.2
Total	900.442	1,234.442	1,365.442	1,372.442

3.8 The Prospects for Interest Rates

3.8.1 The Council has appointed Capita Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives their and our central view.

Table 7: Interest Rate Forecast December 2016 to March 2020

	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20
Bank rate	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%	0.50%	0.75%	0.75%
5yr PWLB rate	1.60%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.80%	1.80%	1.90%	1.90%	2.00%	2.00%
10yr PWLB rate	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	2.40%	2.40%	2.40%	2.50%	2.50%	2.60%	2.60%	2.70%
25yr PWLB rate	2.90%	2.90%	2.90%	2.90%	3.00%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%
50yr PWLB rate	2.70%	2.70%	2.70%	2.70%	2.80%	2.80%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%

3.8.2 Commentary on interest rate forecasts and the economy has been provided by Capital Asset Services in **Appendix G**.

3.9 The Borrowing strategy

3.9.1 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 still an issue that needs to be considered. Against this background and the risks within the economic forecast, caution will be adopted with the 2017/2018 treasury operations. The Executive Director of Resources (Section 151 Officer) 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 an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

3.9.2 Any decisions will be reported to Cabinet at the next available opportunity.

3.10 Policy on borrowing in advance of need

3.10.1 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.

3.11 Debt rescheduling and repayment

3.11.1 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).

3.11.2 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).

3.11.3 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. The forecasts under-pinning this strategy assume that cash balances will be used to repay maturing debt, at least for the short-term, i.e. the next three-year period.

3.11.4 All rescheduling will be reported to Cabinet, at the earliest meeting following its action.

3.12 Sources of finance

3.12.1 The Council's main source of finance is borrowing from the Public Works Loan Board (PWLB) where funds can be borrowed up to 50 years at both fixed and variable rates. The Council has qualified for borrowing from the PWLB at the 'certainty rate' which is the prevailing PWLB interest rate on the date of borrowing less a discount of 0.20%. This discounted rate applies for funding of capital schemes through prudential borrowing and for the refinancing of maturing long term debt. With long-term PWLB rates currently low, this 'certainty rate' now makes funding through the PWLB an attractive option. In order to reduce the risk that loans will mature when interest rates are peaking, debt is taken on in portions that mature over a spread of years. This is described as the debt maturity profile. New loans will be taken to fit into gaps in the Authority's existing debt maturity profile.

3.12.2 The Council continues to source cheaper alternatives to the PWLB in order to finance the borrowing requirement for future years. Other than the PWLB, the Council currently uses other UK local authorities willing to offer loans up to 5 years and the European Investment Bank, both of which provide financing below the PWLB certainty rate. The Council has also found and will make use of commercial lenders willing to lend at rates below the PWLB certainty rate and continues to look at options such as Local Authority Bonds and the Municipal Bond Agency. The Government is currently consulting on making debt available at a discounted rate to support investment in infrastructure. This option will be considered alongside those others listed here.

3.12.3 Long-term borrowing to support Borough regeneration will service the capital financing requirements of the Council's arms-length development company, Brick by Brick. Onwards lending will be at a margin to the cost of borrowing and interest payments together with repayment of principal will prime additional investment. Investment in the Borough's Growth Zone should generate additional business rates that can be applied to service debt funding.

ANNUAL INVESTMENTSTRATEGY

3.13 Investment policy

3.13.1 The Council's investment policy has regard to the Department for Communities and Local Government (DCLG)'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. In accordance with the above guidance from the DCLG and CIPFA, and 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. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

3.13.2 Ratings will not be the sole determinant of the quality of an institution; 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. To this end 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. 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.

3.13.3 Investment instruments identified for use in the financial year are listed in **Appendix B** under the 'specified' and 'non-specified' investments categories. Counterparty limits will be as set through the Council's treasury management practices – schedules.

3.13.4 The Council may wish, from time to time, to take advantage of financial derivative instruments in order to better manage risks, such as exposure to interest rate movements. Local authorities, including the Council, 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). However, previous legislation was understood to prevent the use of such tools where they were not embedded in other instruments. The Localism Act 2011 includes a general power of competence that removes the uncertain legal position over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment). The latest CIPFA Code requires local authorities to clearly detail their policy on the use of derivatives in their annual strategy.

3.13.5 The Council will only use financial derivatives (such as swaps, forwards, futures and options) either on a standalone, or embedded basis, where it can be clearly demonstrated that as part of the prudent management of the Council's financial affairs the use of financial derivatives will have the effect of reducing the level of 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. This will be determined in liaison with the Council's external advisors. 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 if applicable.

3.13.6 At all times the Council will comply with CIPFA advice and guidance on the use of financial derivatives and have regard to CIPFA publications on risk management.

3.14 Annual Investment Strategy

3.14.1 The investments, both specified and non-specified, that officers will be permitted to undertake in-house are summarised below. Further details are provided in **Appendix B.**

a. **Specified Investments** - All investments shall consist of investments under one year as follows:

- Debt Management Agency Deposits Facility (DMADF).
- Term deposits with UK Government or with UK local authorities.
- Term deposits with credit - rated deposit takers (banks and building societies).
- Certificate of Deposits.
- AAA rated Money Market Funds.

- Bonds issued by multinational development banks.
- Enhanced AAA rated Money Market Funds.
- UK Government Gilts.
- UK Government Treasury Bills.

b. **Non-specified investments** - Local authorities now have specific powers to invest for periods in excess of one year. It is recommended that these shall consist of:

- Term deposits with credit - rated deposit takers (banks and building societies).
- Term deposits with UK local authorities.
- Certificate of Deposits (CD).
- Callable deposits with credit rated deposit takers (banks and building societies).
- Forward deposits with credit rated banks and building societies.
- Bonds issued by multinational development banks.
- Enhanced AAA rated Money Market Funds.
- UK Government Gilts.
- Property Funds.
- Floating Rate Notes (FRNs) issued by institutions on the Council's authorised lending list.
- Investment grade Corporate Bonds issued by Corporate Institutions.
- AAA rated Covered Bonds.
- Investment in the equity of any company wholly owned by Croydon Council.

3.14.2 Investment Income Gross - Based on cash flow forecasts for 2016/2017, the Council anticipates its average cash balances for the year to be £180.0m, which includes the £210.1m of new borrowing to be undertaken in 2016/2017. The overall balances include schools balances and HRA revenue balances for which an apportionment of investment interest earned is made. The net income then due to the General Fund is estimated at £0.750m for 2017/2018.

3.14.3 All credit ratings in respect of financial institutions that the Council invests monies in will be continuously monitored together with the limits imposed on amounts that can be invested and the duration of such investments. The Council is alerted to news relating to financial institutions and changes in ratings by its treasury management advisers as these occur and is therefore in a position to take appropriate action to protect the Council's interests.

3.14.4 The Executive Director of Resources will be responsible for managing all investments within the limits as set out in **Appendix E** and in accordance with CIPFA's Treasury Management in the Public Services Code of Practice 2011 Edition.

3.14.5 Capita Asset Services have advised and assisted Council Officers in compiling and maintaining a counterparty lending list based on FITCH credit ratings and other related information in force as at 31st December 2015. This is attached at **Appendix E** and the Council is recommended to approve this list of counterparties and the criteria set for inclusion on to both List A and List B. In respect of List A the credit limits that apply range from £15m to £25m depending on the institution and the credit limit for institutions on List B is set at £10m for each institution. The maximum duration of investments in the institutions on both lists will be subject to Capita Asset Services' recommendations at the time that investments are made. Under the updated regulations the Authority is obliged to consider a range of different sources of information before taking a view on whether to invest with any counterparty. These include each of the rating agencies, the Credit Default Swap (CDS) spreads which gives early warning of likely changes in credit ratings as well as the sovereign rating for the country and other market driven information. Capita Asset Services summarise these different views in forming an overall picture of the credit-worthiness of each, which is communicated to this Authority. FITCH ratings are the most valuable in this particular case as they focus more on European banks whereas Moody's and Standard & Poor's look more at the US.

3.14.6 The principle of ensuring capital security and then of securing the best rate of return underpins all treasury investment decisions. There is a growing concern, triggered by a succession of high profile banking scandals, that the reducing pool of quality counter-parties, such as banks, is increasing the level of risk for the Authority. These risks are not simply the risk that principal sums invested might be lost but also reputational risks to the Authority. In response, the Council's Treasury team has investigated other high-grade deposit takers, to increase diversification of investments and thereby reduce the overall concentration of risk of default. As a consequence of this, the Council has put into place a Custodian agreement offered at a discount by the Bank of New York Mellon – the Custodian used by the Council's Pension Fund. This has enabled the Treasury team to diversify investments and to enhance yields by investing in those specified and unspecified investments that require custody arrangements. A list of the Specified and Non-Specified investments that Council Officers are permitted to undertake in-house is detailed in **Appendix B.** In the immediate short-term there will be no increase in returns, but the Treasury team will be better placed to exploit market opportunities in the longer term.

3.14.7 Of the two part-nationalised UK banks, the UK government's stake in the Royal Bank of Scotland (RBS) PLC group at around 72.9% makes it the majority shareholder in that bank. As such, whilst the government announced plans to sell off its stake in that bank, the size of the current equity stake makes it unlikely that the sale process will materially dilute the government's holding in RBS in the near future. The RBS Group will therefore be retained as an approved investment counterparty till such time as the situation changes. Further, as the Council banks with the National Westminster Bank PLC which is part of the RBS PLC Group, the investment limit for this counterparty will remain at £25m. The UK government's stake in the other part-nationalised bank, Lloyds Banking Group PLC, currently stands below 11% with plans to sell this stake within the coming months to bring the bank back into private ownership. For investment purposes, the Council's treasury advisers have recommended that Lloyds Banking Group should now be evaluated on a stand-alone basis and should only be included onto an approved counterparty list if the bank meets the minimum rating criteria set. At present, the bank's ratings exclude it from the Council's approved lending list but like other entities this can change over time.

3.14.8 With regard to UK Challenger banks, the majority of local authorities do not include these banks in their counterparty lists. Although at present, Challenger banks do not have credit ratings and so fall outside investment strategy criteria, it is expected that these banks may get rated in the future. The situation on Challenger banks and UK part-nationalised banks will be monitored continuously.

3.14.9 In 2014/2015, the Council had invested £20m in the Real Lettings Property Fund Limited Partnership. The property fund, which has a 7-year life, offers investors the opportunity to invest in a diversified portfolio of London residential property and aims to deliver a minimum return of 5% per annum based on the letting of the properties on 5-year lease terms. For Croydon, this investment will also provide added benefit in that the properties purchased would offer affordable accommodation for former homeless people or those at risk of homelessness, who cannot access social housing. An additional £10m was advanced to the Fund on 9 September 2015. Returns generated by the investment will serve to boost the Council's overall income in the future.

3.14.10 In the current low interest rate environment, Money Market Funds (MMFs) can also be used effectively to provide returns in excess of straight overnight bank deposits and to provide for excellent liquidity if required. The Council invests in MMFs which are AAA rated by the FITCH rating agency and at least one of the other two major ratings agencies – Moodys and Standard & Poor's.

3.14.11 In addition, the Council will continue to lend to other UK local authorities and to the Debt Management Office, which effectively is lending to the Government.

3.14.12 As at 31st December 2016, short-term investment interest rates (1-3 months) were between 0.20% and 0.40% with longer term rates (up to 1 year) between 0.45% and 0.8%. Investments will be made to take advantage of higher yields and to hedge against future decreases in bank rates. Daily liquidity requirements will be met by investing in AAA-rated MMFs. As investment rates are influenced throughout the year by the release of key items of data, there may be occasions when some investments will be pitched towards specific periods to take advantage of any unexpected higher rates resulting from data issued. In all cases investment decisions will adhere to Capita Asset Services' recommended maximum investment durations for the counterparty concerned.

3.14.13 With the introduction of the Markets in Financial Instruments Directive II from June 2017 this local authority will be classified as a retail investor. It will thence be for each counter-party to decide whether to assess the Council as a professional investor. Guidance from the Financial Conduct Authority on this process is awaited. The implications of not being reclassified are profound.

3.15 **Treasury Limits**

3.15.1 Section 3 of the Local Government Act 2003 requires the Council to set limits and to keep under review how much it can afford to borrow. The amounts so determined are to be set on a rolling basis, for the forthcoming financial year and two successive financial years, a period of three years in total from 2017/2018 to 2019/2020 and are termed:

1. The **'Operational Boundary for External Debt'**. This reflects the maximum amount of external debt according to probable events and consistent with the level of external debt projected in the estimates.

2. The **'Authorised Borrowing Limit'**. This limit represents an assessment of the maximum debt the authority may need to incur at any point throughout the year as determined in the Financial Strategy by the Executive Director of Resources.

3.15.2 The Executive Director of Resources will be responsible for setting the Council's Affordable Borrowing Limit. This limit requires the Council to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon future council tax and housing rent levels is acceptable.

3.15.3 The Council's affordable borrowing limit has been estimated to be **£900.442m** for **2016/2017**, **£1,234.442m** in **2017/2018, £1,365.442m** in **2018/2019** and £**1,372.442m** in **2019/2020** as detailed in **Appendix C**. These limits reflect the maximum amount the Council can borrow for capital and revenue purposes and allows for unexpected events for example a possible delay in the receipt of anticipated council tax, National Non-Domestic

Rates (NNDR) direct debits, housing benefit subsidy or other government grant that had been notified to Council Officers in advance. The sum of £40m has been included in respect of revenue borrowing to cover the possibility of this shortfall. The limit reflects a level of borrowing which while not desirable is affordable in the short term to fund the cash flow requirements of the organisation and to address any potential risks that may arise.

3.16 Prudential Indicators

3.16.1 The Prudential Indicators for 2017/2018 to 2019/2020 are attached in **Appendix C** in accordance with the Prudential Code for Capital Finance in Local Authorities 2011 Edition.

3.16.2 The Executive Director of Resources is responsible for setting up and monitoring the Prudential Indicators in accordance with the Council's Capital Strategy.

3.16.3 The Council is also required to indicate if it has adopted the CIPFA Code of Practice on Treasury Management. The updated 2011 Code was adopted on 26 February 2013 by Full Council (Minute A31/13).

3.16.4 The Prudential Indicators set will continue to be monitored throughout the year and will be reported to Cabinet on a regular basis.

3.16.5 The indicators break down into four blocks relating to capital expenditure; the affordability of that investment programme; debt; and treasury management as follows:

1. The capital investment indicators reflect the Authority's future plans to undertake capital works, and the extent to which these will be funded through borrowing. (**see Appendix C**).

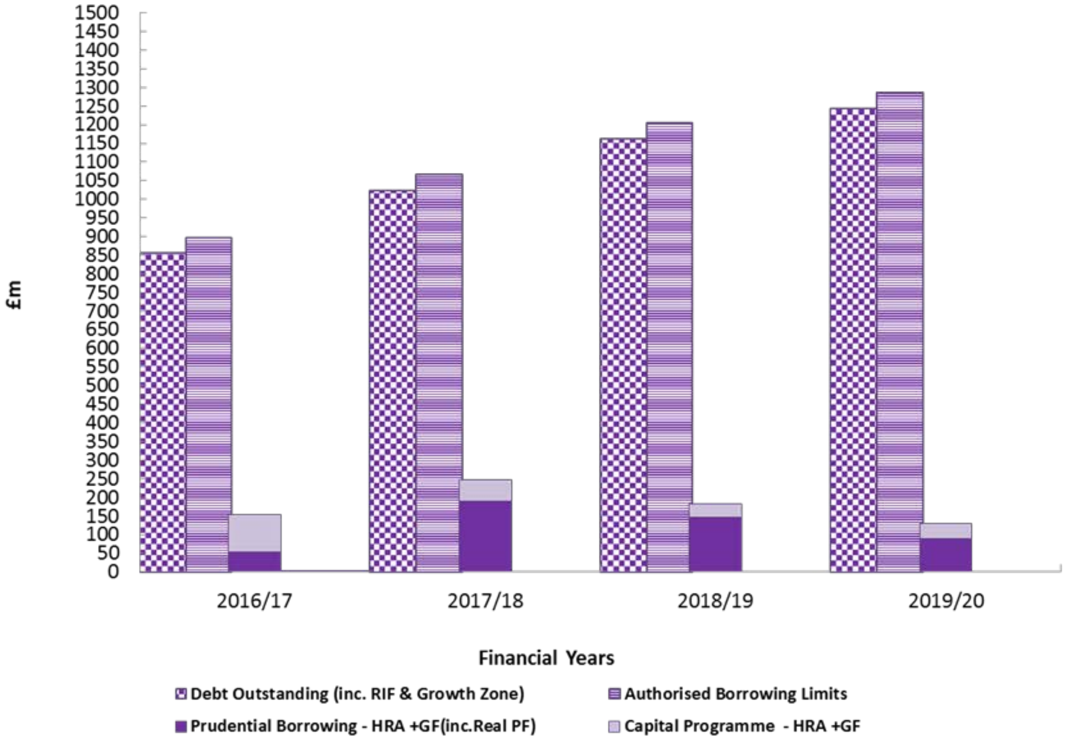
2. Apart from borrowing that is directly supported by government grant funding, the cost of new prudential borrowing to the Authority will be £14.32 per Band D council taxpayer in 2017/2018. This Prudential Indicator reflects the impact of funding decisions relating to capital investment in Croydon. The Prudential Code specifically indicates that it is not appropriate to compare this indicator with other authorities.

3. The external debt indicators illustrate the calculation of the affordable borrowing limit.

4. The treasury indicators show that the Authority will limit its exposure to variable rate debt to no more than 20% of total debt and will only invest up to 30% of the total investments for periods in excess of one year, for reasons of limiting exposure to risk and guaranteeing adequate liquidity. The final indicator sets a profile for the maturing of new debt.

3.16.6 These main indicators are featured below as follows:

Chart 1: Comparison of Debt against Prudential Limits 2016 / 2020



3.17 **Conclusion**

3.17.1 The Council's treasury advisers forecast that the bank rate, currently at 0.25%, will increase only after the UK formally leaves the European Union. The longer term (25 years) PWLB interest rates, which currently are 2.9%, are expected to increase to around 3.00% in the second half of 2017.

3.17.2 Temporary investment rates are currently between 0.40 and 0.60% for short dates and between 0.54% and 1.0% for longer periods. It is anticipated that investment rates will increase gradually next year in line with bank rate expectations.

3.17.3 A glossary of terms associated with this report is attached in **Appendix F**.

4 **CONSULTATION**

4.1 Full consultation in respect of the contents of this report has taken place with the Council's treasury management advisers Capita Asset Services in preparing this report.

5. FINANCIAL AND RISK ASSESSMENT CONSIDERATIONS

5.1 Revenue and Capital consequences of this report are dealt with within this report.

There are no additional financial considerations other than those identified in this report.

5.2 The effect of the decision

Approval to this report will ensure that the Council meets both its legal and financial management requirements in respect of Treasury Management.

5.3 Risks

There are no further risks issues other than those already detailed in this report**.**

5.4 Options

These are fully dealt with in this report.

5.5 Future savings/efficiencies

This report sets out the Treasury Strategy and identifies that new loans and debt restructuring will only be undertaken on advice from our treasury management advisers.

Approved by: Richard Simpson, Executive Director of Resources.

6. COMMENTS OF THE COUNCIL SOLICITOR AND MONITORING OFFICER

6.1 The Acting Council Solicitor comments that there are no additional legal considerations beyond those detailed in the body of the report.

Approved for and on behalf of Jacquline Harris-Baker, Acting Council Solicitor and Acting Monitoring Officer.

7. HUMAN RESOURCES IMPACT

7.1 There are no immediate HR considerations that arise from the recommendations of this strategy for Croydon Council staff or workers, other than the formation of a Development Company; HR advice will be given separately in relation to the specific people issues that will arise from that proposal.

Approved by: Jason Singh, Head of HR Employee Relations on behalf of the Director of HR.

8. EQUALITIES IMPACT

8.1 Consistent with the requirements of equal opportunities legislation including the Public Sector Equality Duty, the Council carries out an equality impact assessment on new policies, or existing policies which are the subject of major change.

8.2 The Council’s Capital and Revenue Budget 2017/2018 is not subject to an equality impact assessment. However, in those areas where the setting of the capital and revenue budget result in new policies or policy change, then it is the responsibility of the relevant service department to carry out an equality impact assessment which evaluates how the new or changed policy will impact on disadvantaged sections of the community, including disabled people. The impact assessment includes consultation with disabled people and user-led disabled people organisations.

9. ENVIRONMENTAL IMPACT

9.1 There are no Environment and Design impacts arising from this report.

10. CRIME AND DISORDER REDUCTION IMPACT

10.1 There are no Crime and Disorder reduction impacts arising from this report.

11. REASONS FOR RECOMMENDATIONS/PROPOSED DECISION

11.1 The recommendations proposed are in accordance with the Treasury Management in the Public Services Code of Practice 2011 Edition and the Prudential Code for Capital Finance in Local Authorities 2011.

12. OPTIONS CONSIDERED AND REJECTED

12.1 Consideration and evaluation of alternative options are dealt with within this report.

CONTACT OFFICER: Nigel Cook, Head of Pensions and Treasury Ext 625526

BACKGROUND DOCUMENTS:

CIPFA's Prudential Code for Capital Finance in Local Authorities – Fully Revised Second Edition 2009 and updated 2011 Edition.

CIPFA's Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes – Fully Revised Second Edition 2009 and updated 2011 Edition.

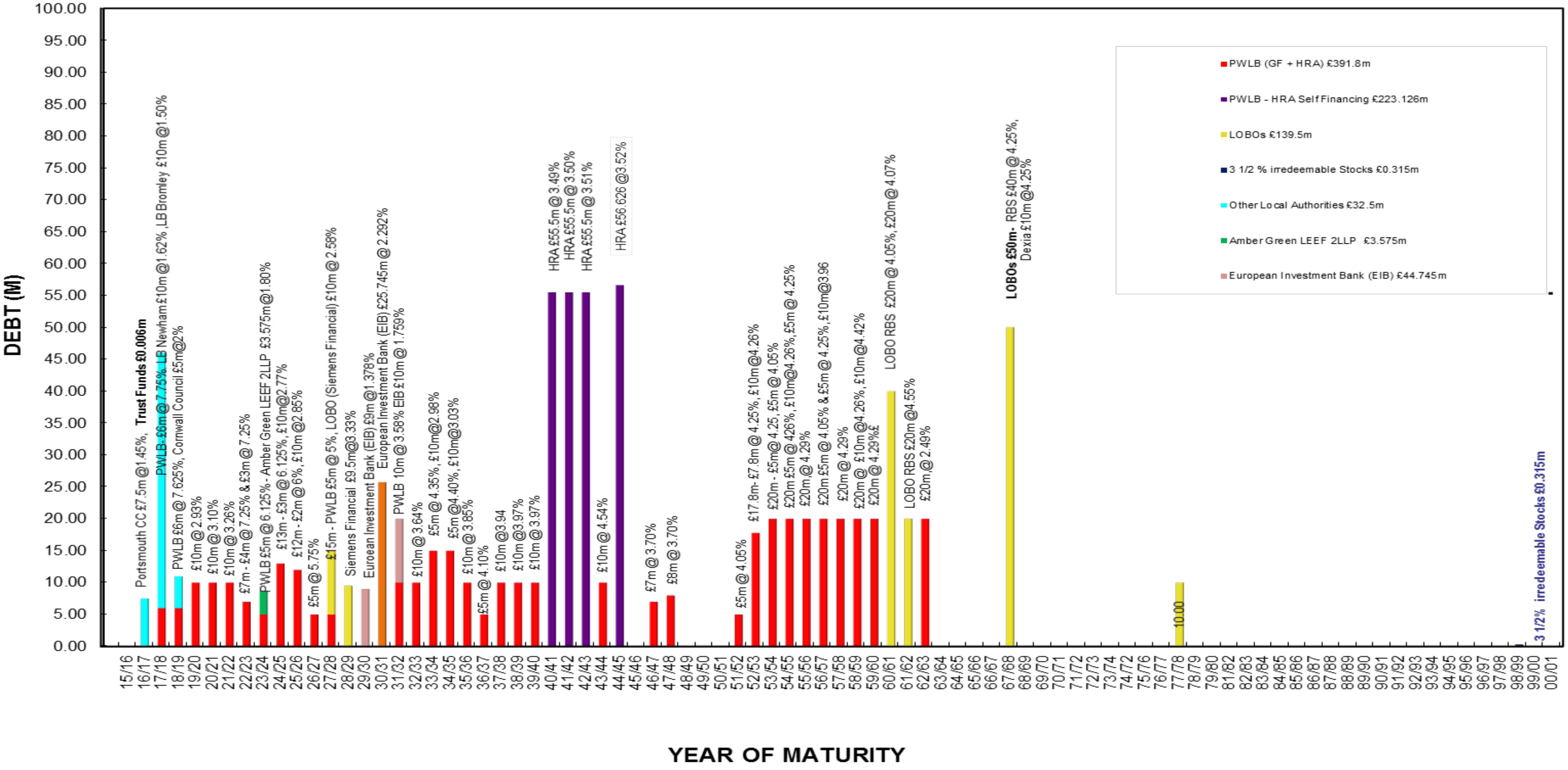
DCLG's Guidance on Local Government Investments March 2004.

Appendices

Appendix A: Long-term debt profile
Appendix B: Specified and non-specified investments
Appendix C: Prudential Indicators
Appendix D: Minimum Revenue Provision Policy
Appendix E: Authorised Lending List
Appendix F: Glossary
Appendix G: Commentary on Interest Rate Forecasts

APPENDIX A

London Borough of Croydon
Long Term Debt Profile as at 31 December 2016 £835.567m



LOCAL GOVERNMENT INVESTMENTS (ENGLAND) SPECIFIED AND NON-SPECIFIED INVESTMENTS

a. **Specified Investments** - Where there is a change in the current investment policy this is specifically noted. All investments shall consist of investments under one year as follows:

- Debt Management Agency Deposits Facility (DMADF) which is currently available for investments up to six months.

- Term deposits with the UK Government or with UK local authorities (i.e. local authorities as defined under Section 23 of the 2003 Act) with maturities up to one year.

- Term deposits with credit - rated deposit takers (banks and building societies) including callable deposits, with maturities up to one year.

- Certificate of Deposits issued by credit - rated deposit takers (banks and building societies) up to one year.

- AAA rated Money Market Funds (i.e. a collective investment scheme as defined in SI. 2004 No 534).

- Bonds issued by multinational development banks (as defined in SI 2004 No 534) with maturities under 12 months. The Council currently does not invest in this type of investment. It is recommended, however, that these can now be used and held until maturity, after consulting and taking advice from the treasury management consultants.

- Enhanced AAA rated Money Market Funds. These funds differ from traditional AAA Money Market Funds in that they take more interest rate risk by managing portfolios with a longer weighted average maturity period. They may also take greater credit risk by holding assets with lower credit ratings and / or have a longer weighted average life. Depending on whether the fund is UK or US administered, it would be rated by only one of the rating agencies. Hence, although the minimum requirement is an AAA rating, the rating need only be given by one of the agencies. Typically these funds are designed to produce an enhanced return and this requires the fund manager to take more risk (whether credit, interest rate or liquidity) than the traditional AAA Money Market Funds. The Council currently does not invest in this type of fund. It is recommended, however, that these can now be considered, after consulting and taking advice from the treasury management consultants subject to the same criteria as other investments.

- UK Government Gilts. These are bonds issued by the UK Government representing a very low credit risk with options to sell in the secondary market.

- UK Government Treasury Bills which are debt instruments issued by the Government's Debt Management Office through weekly auctions. The bills are issued with maturities of one, three and six months.

b. **Non-Specified investments -** Local authorities now have specific powers to invest for periods in excess of one year. Previously such investments were not permissible, except in respect of the Council's Pension Fund (where specific legislation exists). It is recommended that these shall consist of:

- Term deposits with credit - rated deposit takers (banks and building societies) with maturities greater than one year. As a general rule they cannot be traded or repaid prior to maturity. The risk with these is that interest rates could rise after making the investment and there is also the potential that there could be a deterioration of the credit risk over a longer period. It is recommended, therefore, that the use of this investment is limited to a maximum of five years following advice from the Council's treasury management advisers.

- Term Deposits with UK local authorities. This investment represents intra-authority loans i.e. from one local authority to another for the purpose of cash-flow management. The risk with these is that interest rates could rise after making the investment and it is therefore recommended that the use of this investment is limited to a maximum of five years following advice from the Council's treasury management advisers. This risk is common to all term deposits whether with local authorities or other counterparties.

- Certificate of Deposits (C.D.) issued by credit - rated deposit takers (banks and building societies) with maturities greater than one year. With these investments there is a market or interest risk. Yield is subject to movement during the life of the CD, which could negatively impact on the price of the CD if traded early. It is recommended, therefore, that the use of this investment is limited to a maximum of five years and sold on maturity following advice from the Council's treasury management advisers.

- Callable deposits with credit rated deposit takers (banks and building societies) with maturities greater than one year. These have the potential of higher return than using a term deposit with a similar maturity. The risk is that only the borrower has the right to pay back the deposit, the lender does not have a similar call, as although the term is fixed only the borrower has the option to repay early. There is, therefore, no guarantee that the loan will continue to its maturity. The interest rate risk is that the borrower is unlikely to pay back the deposit earlier than the maturity date if interest rates rise after the deposit is made.

- Forward deposits with credit rated banks and building societies for periods greater than one year (i.e. negotiated deal period plus period of deposit). The advantage of the investment is that there is a known rate of return over the period the monies are invested which aids forward planning. The credit risk is that if the credit rating falls or interest rate rise in the interim period the deposit period cannot be changed. It is recommended, therefore, that the use of this investment is limited to a maximum of five years following advice from the Council's treasury management advisers.

- Bonds issued by multilateral development banks (as defined by SI. 2004 No 534). These have an excellent credit quality and are relatively liquid. If they are held to maturity there is a known yield, which would be higher than that on comparable gilts.

- If traded, there could be a potential for capital gain or loss through appreciation or depreciation in value. The market or interest risk is that the yield is subject to movement during the life of the bond, which could impact on the price of the bond, i.e. if sold prior to redemption date. Given the potential for loss any investment would need to be based on the principle that they would be bought and held until maturity. It is recommended, therefore, that the use of this investment is limited to a maximum of five years following advice from the Council's treasury management advisers.

- Enhanced Money Market Funds. These funds differ from traditional AAA Money Market Funds in that they take more interest rate risk by managing portfolios with a longer weighted average maturity period. They may also take greater credit risk by holding assets with lower credit ratings and / or have a longer weighted average life. Depending on whether the fund is UK or US administered, it would be rated by only one of the rating agencies. Hence, although the minimum requirement is an AAA rating, the rating need only be given by one of the agencies. Typically these funds are designed to produce an enhanced return and this requires the fund manager to take more risk (whether credit, interest rate or liquidity) than the traditional AAA Money Market Funds. The Council currently does not invest in this type of fund. It is recommended, however, that these can now be considered, after consulting and taking advice from the treasury management consultants subject to the same criteria as other investments.

- UK Government Gilts. These are bonds issued by the UK Government representing a very low credit risk with options to sell in the secondary market. If held to maturity there is a known yield but if traded there could be a potential for capital gain or loss through appreciation or depreciation in value. Given the potential for loss, any investment would need to be based on the principle that UK government gilts would be bought and held until maturity. It is recommended, therefore, that the use of this investment is limited to a maximum of five years following advice from the Council's treasury management advisers. If held to maturity, these bonds represent the nearest to a risk-free investment.

- Property Funds. Property funds can provide stable returns in terms of fixed period rents, whether commercial or industrial rentals. Property funds can be regulated or unregulated. An investment in share or loan capital issued by a regulated property fund is not treated as capital expenditure but an investment in an unregulated fund would count as capital expenditure. Given the nature of the property sector, a longer-term time horizon will need to be considered for this type of investment. The Council currently has invested in one property fund; the Real Lettings Property Fund Limited Partnership – see 3.5.13. It is recommended, however, that any future investments in property funds should only be considered, after consulting and taking advice from the treasury management consultants.

- Floating Rate Notes (FRNs). These are typically longer term bonds issued by banks and other financial institutions which pay interest at fixed intervals. The floating rate nature of these instruments reduces the exposure to interest rate risk as the interest rate is re-fixed at the beginning of every interest rate period. The option to redeem before maturity is available through the secondary market. It is recommended that investments in FRNs be restricted to those issued by institutions on the Council's authorised lending list, after consulting and taking advice from the treasury management consultants.

- Corporate Bonds are issued by corporate institutions for example General Electric, Vodafone etc. They offer local authorities an alternative to the usual financial institutions. For Corporate Bonds, the minimum credit rating criteria of AA- should apply to fit within the Council's investment parameters. It is recommended that the use of this type of investment can now be considered, after consulting and taking advice from the treasury management consultants.

- Covered Bonds. These are a type of secured bond that is usually backed by mortgages or public sector loans. An important feature of covered bonds is that investors have dual recourse, both to the issuer and to the underlying pool of assets. It is recommended that the use of this investment can now be considered, after consulting and taking advice from the treasury management consultants.

- Investment in equity of any company wholly owned by Croydon Council.

APPENDIX C

PRUDENTIAL INDICATORS FOR 2016/17 – 2019/2020

PRUDENTIAL INDICATORS	2016/17 Forecast Outturn £m	2017/18 Forecast £m	2018/19 Forecast £m	2019/20 Forecast £m
1. Prudential Indicators for Capital Expenditure				
1.1. Capital Expenditure				
- General Fund	127.746	386.774	148.866	28.007
- HRA	25.724	27.051	27.051	27.051
Total	**153.470**	**413.825**	**175.917**	**55.058**
1.2. In year Capital Financing Requirement (see Table 2)				
- General Fund - gross of MRP costs	54.722	355.227	138.572	15.348
- HRA	0.000	0.000	0.000	0.000
Total in year Capital Financing Requirement	**54.722**	**355.227**	**138.572**	**15.348**
1.3. Capital Financing Requirement as at 31st March – **balance sheet figures**				
- General Fund (net of MRP costs)	600.653	949.887	1,081.325	1,088.778
- HRA - limit of HRA debt imposed by CLG	338.688	338.688	338.688	338.688
Total	**939.341**	**1,288.575**	**1,420.013**	**1,427.466**
2. Prudential Indicators for Affordability				
2.1. Ratio of financing costs to net revenue streams				
- General Fund	10.0%	13.0%	14.00%	14.0%
- HRA	16.00%	16.00%	16.00²	16.00%
2.2. General Fund impact of Prudential (unsupported) borrowing on Band D Council Tax levels (per annum)				
- In year increase	£4.00	£14.32	£11.00	£3.00
- Cumulative increase (includes MRP costs).		£33.00	£64.00	£82.00
2.3. HRA impact of additional borrowing (unsupported) on housing rents (per annum)	0	0	0	0
[The HRA's additional £223.1m debt costs are reflected in these ratios.]				
3. Prudential Indicators for Long External Debt				
3.1. Debt brought forward 1st April	808.633	858.242	1,192.242	1,323.242
Debt carried forward 31st March (includes the £223.1m debt for the HRA self-financing settlement sum plus RIF & Growth Zone borrowings in future years).	858.242	1,192.242	1,323.242	1,330.242
Additional Borrowing	**49.609**	**334**	**131**	**7**

APPENDIX C

PRUDENTIAL INDICATORS		2016/17 Forecast Outturn £m	2017/18 Forecast £m	2018/19 Forecast £m	2019/20 Forecast £m
3.2.	Operational boundary for external debt (excludes revenue borrowing)				
	Borrowing	858.242	1,192.242	1,323.242	1,330.242
	Other long term liabilities	2.2	2.2	2.2	2.2
3.3.	Total operational debt (excludes revenue borrowing)	858.242	1,192.242	1,323.242	1,330.242
	Add margin for cashflow contingency	40.000	40.000	40.000	40.000
	Authorised limit for external debt (includes revenue borrowing)	898.242	1,232.242	1,363.242	1,370.242
	Other long term liabilities	2.2	2.2	2.2	2.2
	Authorised Borrowing Limit	**900.442**	**1,234.442**	**1,365.442**	**1,372.442**
4.	**<u>Prudential Indicators for Treasury Management</u>**				
4.1.	Borrowing limits - upper limit for fixed interest rate exposure expressed as:-				
	Net principal re fixed rate borrowing / investments	900.442	1,234.442	1,365.442	1,372.442
4.2.	Borrowing limits - upper limit for variable rate exposure expressed as :-				
	Net principal re variable rate borrowing / investments	20%	20%	20%	20%
4.3.	Lending limits - upper limit for total principal sums invested for over 364 days expressed as a % of total investments	30%	30%	30%	30%

		Lower limit	Upper limit
4.4.	Maturity structure of new fixed rate borrowing, if taken, during 2016/17		
	- Under 12 months	0	20%
	- 12 months to 24 months	0	20%
	- 24 months to 5 years	0	30%
	- 5 years to 10 years	0	30%
	- 10 years and above	0	100%

APPENDIX D

MINIMUM REVENUE PROVISION POLICY STATEMENT FOR 2017/2018

The Council has implemented the new Minimum Revenue Provision (MRP) Guidance from 2008/09, and will continue to assess their MRP for 2017/18 in accordance with the main recommendations contained within the Guidance issued by the Secretary of State under Section 21(1A) of the Local Government Act 2003.

The Council's MRP Policy Statement for 2017/2018 is to be as follows:

1. For the proportion relating to historic debt (incurred up to 31 March 2008) and to Government-supported capital expenditure incurred since, the MRP policy will be to adapt **Option 1 - the Regulatory Method** by providing a fixed amount each financial year, calculated at 2% of the balance at 31 March 2015, reducing on a straight line basis so that the whole debt is repaid after 50 years.

2. For unsupported borrowing undertaken since 1 April 2008, reflected within the Capital Financing Requirement (CFR) debt liability at 31st March 2016, the MRP policy will be to adopt **Option 3 – Asset Life Method – Annuity method from the Guidance**. Estimated life periods will continue to be determined under delegated powers. To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the Guidance, these periods will generally be adopted by the Council. However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the Guidance would not be appropriate.

3. As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

4. Where schemes are not fully completed at the end of the financial year, MRP charges will be deferred until the schemes are complete and the assets are operational.

5. MRP on Public Finance Initiative (PFI) schemes debt is to be charged on an annuity basis over the remaining life of each scheme.

6. The Council retains the right to undertake additional voluntary payments if required (Voluntary Revenue Provision – VRP).

7. The Council's cash investment in the Real Lettings Property Fund LP under a 7 year life arrangement is due to be returned in full at maturity with interest paid annually. The cash investment will be treated as capital expenditure with the Council's Capital Financing Requirement (CFR) increasing by this amount. At maturity, the funds returned to the Council will be treated as a capital receipt and the CFR will reduce accordingly. As this is a temporary arrangement over 6 years, and as the funds are to be returned in full, there is no need to set aside prudent provision to repay the debt liability in the interim period, and therefore no MRP application is required.

8. Loans borrowed from Amber Green LEEF 2LLP or an alternative source to fund energy efficiency and carbon reduction schemes at certain educational institutions within the Borough will be recovered in full from these institutions. As such, there is no need to set aside prudent provision to repay the debt liability in the interim period, and therefore no MRP application is required.

Appendix E

LONDON BOROUGH OF CROYDON
Authorised Lending List as at 31/12/16 (Ratings as per FITCH)

LIST A

Name	Credit Limit £	Long Term Rating	Short Term Rating	Viability Rating	Support Rating	Sovereign Rating
Royal Bank Of Canada **(Canada)**	20,000,000	AA	F1+	aa	2	AAA
Morgan Stanley Money Market Fund	15,000,000	AAA				
Aberdeen Money Market Fund	15,000,000	AAA				
Goldman Sachs Money Market Fund	15,000,000	AAA				
JP Morgan Money Market Fund	15,000,000	AAA				
Royal Bank of Scotland Group Plc **(Part Nationalised) (UK)**	25,000,000	BBB+	F2	bbb+	5	AA+
Debt Management Account **(UK Government Body)**	No Limits					AA+

LIST B

Name	Credit Limit £	Long Term Rating	Short Term Rating	Viability Rating	Support Rating	Sovereign Rating
Australia & New Zealand Banking Group **(Australia)**	10,000,000	AA-	F1+	aa-	1	AAA
Bank Of Montreal **(Canada)**	10,000,000	AA-	F1+	aa-	2	AAA
Bank Of Nova Scotia **(Canada)**	10,000,000	AA-	F1+	aa-	2	AAA
Canadian Imperial Bank Of Commerce **(Canada)**	10,000,000	AA-	F1+	aa-	2	AAA
Commonwealth Bank Of Australia **(Australia)**	10,000,000	AA-	F1+	aa-	1	AAA
DBS Ltd **(Singapore)**	10,000,000	AA-	F1+	aa-	1	AAA
HSBC Bank PLC **(UK)**	10,000,000	AA-	F1+	a+	1	AA+
National Australia Bank **(Australia)**	10,000,000	AA-	F1+	aa-	1	AAA
Overseas Chinese Banking Corporation Ltd **(Singapore)**	10,000,000	AA-	F1+	aa-	1	AAA
Svenska Handelsbanken AB **(Sweden)**	10,000,000	AA-	F1+	aa-	2	AAA
Toronto-Dominion Bank **(Canada)**	10,000,000	AA-	F1+	aa-	2	AAA
United Overseas Bank Ltd **(Singapore)**	10,000,000	AA-	F1+	aa-	1	AAA
Westpac Banking Corporation **(Australia)**	10,000,000	AA-	F1+	aa-	1	AAA

Appendix E

LENDING LIST CRITERIA

LIST A

LIMITS TO INDIVIDUAL ORGANISATIONS
Maximum Investment Limit - £20m apart from the limits on the institutions noted below.

CREDIT RATINGS

FITCH Rating in each of the following categories:	F1+ on Short Term Rating AA or above Long Term Rating aa- or above Viability Rating 5 or above for Support Rating AA+ or above Sovereign Rating

APPROVED ORGANISATIONS MEETING CREDIT RATINGS
ALL NON – UK BANKS that meet the FITCH ratings set out above.
ALL UK BUILDING SOCIETIES that meet the FITCH ratings set out above.
UK BANKS that meet the FITCH ratings set out above.
AAA RATED MONEY MARKET FUNDS - £15M LIMIT
DEBT MANAGEMENT OFFICE – NO LIMIT

APPROVED ORGANISATIONS NOT MEETING THE ABOVE CREDIT RATINGS
PART NATIONALISED UK BANKS – Limits as noted below:
ROYAL BANK OF SCOTLAND GROUP PLC - £25M LIMIT

LIST B

LIMITS TO INDIVIDUAL ORGANISATIONS
Maximum Investment Limit - £10m

CREDIT RATINGS

FITCH Rating in each of the following categories:	F1+ on Short Term Rating AA- or above on Long Term Rating a+ or above Viability Rating 5 or above for Support Rating AA+ or above Sovereign Rating

APPROVED ORGANISATIONS MEETING CREDIT RATINGS
ALL NON – UK BANKS that meet the FITCH ratings set out above.
ALL UK BUILDING SOCIETIES that meet the FITCH ratings set out above.
UK BANKS that meet the FITCH ratings set out above
ALL UK LOCAL AUTHORITIES

APPENDIX F

GLOSSARY OF TERMS USED IN THE TREASURY STRATEGY STATEMENT, MINIMUM REVENUE PROVISION POLICY STATEMENT & ANNUAL INVESTMENT STRATEGY 2017/2018

"Adjustment A"	The Prudential System came into force in 2004/05. The former system relied on the maintenance of credit ceilings for both GF and HRA to determine the MRP due for both. The new Prudential system uses figures derived from the authority's consolidated balance sheet to calculate MRP due. A safeguard was built into the new system to ensure that the transition did not lead to any artificial increase in MRP liability. This was based on calculating an amount known as "Adjustment A".
Affordable Borrowing Limit and Authorised Limit for external debit	The maximum amount the Council can borrow for capital and revenue purposes, allowing for unexpected events. It reflects a level of borrowing which, while not desirable, is affordable in the short term. This limit reflects the temporary nature of the borrowing.
Borrowing for Capital Purposes - Supported	 The amount of borrowing to finance capital projects for which the Government will give revenue support and specific grants.
- Unsupported	Additional borrowing the Council may wish to undertake, but for which there will be no financial contribution through the grant system.
CIPFA Treasury Management Code of Practice	The professional code governing treasury management, which the Council has formally adopted.
Capital Financing Requirement (CFR)	The authority's underlying need to borrow to finance capital expenditure.
Consumer Price Index (CPI)	This is a measure of the general level of price changes for consumer goods and services but excludes most owner occupier housing costs such as mortgage interest payments, council tax, dwellings insurance, rents depreciation and the like.
FITCH	An internationally recognised rating agency which is used and approved by the Council's Treasury Advisers, Capita Asset Services.
Gross Domestic Product (GDP)	Gross Domestic Product (GDP) is a measure of a country's economic activity, including all the services and goods produced in a year within that country.

G7	The Group of Seven (G7) is an informal bloc of seven industrialised democracies – the USA, Canada, France, Germany, Italy, Japan and the UK that meets annually to discuss issues such as global economic governance, international security and energy policy.
Lenders Option / Borrowers Option Loans (LOBO's)	A form of long-term borrowing where loans run at a fixed rate of interest for a fixed period of time, after which the Lender has the option to ask for repayment or change the interest rate on pre-determined dates. If the Lender decides to exercise the option to change the interest rate the borrower can then decide whether to accept the new terms or repay the loan with no penalty.
London Interbank Bid Rate (LIBID)	The interest rate at which major banks in London are willing to borrow (bid for) funds from each other.
Minimum Revenue Provision (MRP)	The amount which must be set aside from revenue each year to cover future repayment of loans. There is no MRP requirement for HRA borrowing.
Net Revenue Stream (NRS)	The NRS for the General Fund is the "Amount to be met from Government Grant and Council Tax contributions", as shown in the consolidated revenue account. This represents the budget requirement for the Council. The NRS for the Housing Revenue Account is the amount to be met from net rent income as shown in the HRA accounts.
Operational boundary for external debt	The maximum amount of external debt according to probable events and consistent with the level of external debt projected in the estimates.
Public Works Loan Board (PWLB)	Part of the Government's Debt Management Office, making long-term funds available to local authorities on prescribed terms and conditions.

COMMENTARY FOR INTEREST RATE FORECASTS AND THE ECONOMY PROVIDED BY OUR TREASURY ADVISOR CAPITA ASSET SERVICES

The Bank of England's Monetary Policy Committee, (MPC), cut the Bank Rate from 0.50% to 0.25% on 4th August in order to counteract what it forecast was going to be a sharp slowdown in growth in the second half of 2016. It also gave a strong steer that it was likely to cut Bank Rate again by the end of the year. However, economic data since August has indicated much stronger growth in the second half 2016 than that forecast; also, inflation forecasts have risen substantially as a result of a continuation of the sharp fall in the value of sterling since early August. Consequently, Bank Rate was not cut again in November or December and, on current trends, it now appears unlikely that there will be another cut, although that cannot be completely ruled out if there was a significant dip downwards in economic growth. During the two-year period 2017 – 2019, when the UK is negotiating the terms for withdrawal from the EU, it is likely that the MPC will do nothing to dampen growth prospects, (i.e. by raising Bank Rate), which will already be adversely impacted by the uncertainties of what form Brexit will eventually take. Accordingly, a first increase to 0.50% is not tentatively pencilled in, as in the table above, until quarter 2 2019, after those negotiations have been concluded, (though the period for negotiations could be extended). However, if strong domestically generated inflation, (e.g. from wage increases within the UK), were to emerge, then the pace and timing of increases in Bank Rate could be brought forward.

Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The above forecasts, (and MPC decisions), will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

The overall longer run trend is for gilt yields and PWLB rates to rise, albeit gently. It has long been expected that at some point, there would be a start to a switch back from bonds to equities after a historic long term trend over about the last twenty five years of falling bond yields. The action of central banks since the financial crash of 2008, in implementing substantial quantitative easing purchases of bonds, added further impetus to this downward trend in bond yields and rising prices of bonds. The opposite side of this coin has been a rise in equity values as investors searched for higher returns and took on riskier assets. The sharp rise in bond yields since the US Presidential election, has called into question whether, or when, this trend has, or may, reverse, especially when America is likely to lead the way in reversing monetary policy. Until 2015, monetary policy was focused on providing stimulus to economic growth but has since started to refocus on countering the threat of rising inflationary pressures as strong economic growth becomes more firmly established. The expected substantial rise in the Fed. rate over the next few years may make holding US bonds much less attractive and cause their prices to fall, and therefore bond yields to rise. Rising bond yields in the US would be likely to exert some upward pressure on bond yields in other developed countries but the degree of that upward pressure is likely to be dampened by how strong, or weak, the prospects for economic growth and rising inflation are in each country, and on the degree of progress in the reversal of monetary policy away from quantitative easing and other credit stimulus measures.

PWLB rates and gilt yields have been experiencing exceptional levels of volatility that have been highly correlated to geo-political, sovereign debt crisis and emerging market developments. It is likely that these exceptional levels of volatility could continue to occur for the foreseeable future.

The overall balance of risks to economic recovery in the UK is to the downside, particularly in view of the current uncertainty over the final terms of Brexit and the timetable for its implementation.

Apart from the above uncertainties, downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- Monetary policy action by the central banks of major economies reaching its limit of effectiveness and failing to stimulate significant sustainable growth, combat the threat of deflation and reduce high levels of debt in some countries, combined with a lack of adequate action from national governments to promote growth through structural reforms, fiscal policy and investment expenditure.
- Major national polls:
- The Italian constitutional referendum in December resulted in a ‘No’ vote which led to the resignation of Prime Minister Renzi. This means that Italy needs to appoint a new government;
    - Spain has a minority government with only 137 seats out of 350 after already having had two inconclusive general elections in 2015 and 2016. This is potentially highly unstable.
    - There will be a Dutch general election in March;
    - This will be followed by the French presidential election in April/May 2017;
    - Next there is the French National Assembly election in June 2017; and finally in the annual calendar,
    - The German Federal election, in August – October 2017.
- A resurgence of the Eurozone sovereign debt crisis, with Greece being a particular problem, and stress arising from disagreement between EU countries on free movement of people and how to handle a huge influx of immigrants and terrorist threats.
- Weak capitalisation of some European banks, especially Italian.
- Geopolitical risks in Europe, the Middle East and Asia, causing a significant increase in safe haven flows.
- UK economic growth and increases in inflation are weaker than we currently anticipate.
- Weak growth or recession in the UK’s main trading partners - the EU and US.

The potential for **upside risks to current forecasts** for UK gilt yields and PWLB rates, especially for longer term PWLB rates, include: -

- UK inflation rising to significantly higher levels than in the wider EU and in the US, causing an increase in the inflation premium in gilt yields.
- A rise in US Treasury yields as a result of Fed. funds rate increases and rising inflation expectations in the USA, dragging UK gilt yields upwards.
- The pace and timing of increases in the Fed. funds rate causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.
- A downward revision to the UK’s sovereign credit rating undermining investor confidence in holding sovereign debt (gilts).

Investment and borrowing rates

- Investment returns are likely to remain low during 2017/2018 and beyond.
- 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. 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, this needs to be carefully reviewed to avoid incurring higher borrowing costs in later times when authorities will not be able to avoid new borrowing to finance capital expenditure and/or to refinance maturing debt;
- There will 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.