Audit Committee	Agenda Item: A.6

Meeting Date:	22 December 2016
Portfolio:	Finance, Governance and Resources
Key Decision:	Yes: Recorded in the Notice Ref:KD21/16
Within Policy and Budget Framework	YES
Public / Private	Public

Title:	TREASURY MANAGEMENT STRATEGY STATEMENT, INVESTMENT STRATEGY AND MINIMUM REVENUE PROVISION STRATEGY 2017/18
Report of:	CHIEF FINANCE OFFICER
Report Number:	RD42/16

Purpose / Summary:

This report sets out the Council's Treasury Management Strategy Statement for 2017/18, in accordance with the CIPFA Code of Practice on Treasury Management. The Investment Strategy and the Minimum Revenue Provision (MRP) Strategy for 2017/18 are also incorporated as part of the Statement as are the Prudential Indicators as required within the Prudential Code for Capital Finance in Local Authorities.

Recommendations:

Members of the Audit Committee are asked to note and make comments on the proposed Treasury Management Strategy for 2017/18.

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# Report to Executive	Agenda Item:

Meeting Date:	19 December 2016
Portfolio:	Finance, Governance and Resources
Key Decision:	Yes: Recorded in the Notice Ref: KD21/16
Within Policy and Budget Framework	YES
Public / Private	Public

Title:	DRAFT TREASURY MANAGEMENT STRATEGY STATEMENT, INVESTMENT STRATEGY AND MINIMUM REVENUE PROVISION STRATEGY 2017/18
Report of:	CHIEF FINANCE OFFICER
Report Number:	RD42/16

Purpose / Summary:
This report sets out the Council's Draft Treasury Management Strategy Statement for 2017/18, in accordance with the CIPFA Code of Practice on Treasury Management. The Draft Investment Strategy and the Draft Minimum Revenue Provision (MRP) Strategy for 2017/18 are also incorporated as part of the Statement. So too are the Prudential Indicators as required within the Prudential Code for Capital Finance in Local Authorities.

Recommendations:
The Executive is asked to note the Draft Treasury Management Strategy Statement for 2017/18, which incorporates the Draft Investment Strategy and the Draft MRP Strategy, together with the Prudential Indicators for 2017/18 for draft budget consultation purposes as set out in Appendix A and the Treasury Management Policy Statement as set out at Appendix D.

Tracking

Executive:	**19 December 2016, 18 January 2017**
Overview and Scrutiny:	**5 January 2017**
Audit Committee:	**22 December 2016**
Council:	**7 February 2017**

1. BACKGROUND

1.1 The CIPFA Code of Practice on Treasury Management in Local Authorities was first issued in 1992 and updated in 1996 and 2001. The City Council formally adopted this Code in March 2002 and adopted the 2011 revision in February 2012. The updates made are minor, and centre around the changes in housing finance, Localism Act and the introduction of General Powers of Competence.

1.2 Under the requirements of the revised Code, the Council will receive each year the following reports:-

- Annual strategy and plan in advance of the year
- A mid year review
- Annual report after its close.

2. TREASURY MANAGEMENT STRATEGY STATEMENT

2.1 As required under the Code, the Treasury Management Strategy Statement for 2017/18, which also incorporates both the Investment Strategy for that year and the Minimum Revenue Strategy, is set out in **Appendix A**. The schedule of approved investment vehicles is contained in **Appendix B** and **Appendix C** includes a summary of current economic forecasts on interest rates that have been utilised in preparing the Strategy.

2.2 Also included within Appendix A are the **Prudential Indicators** that must be determined under the requirements of the CIPFA Prudential Code for Capital Finance in Local Authorities. These requirements came into operation on 1 April 2004 under the provisions of the Local Government Act 2003. Part 1 of the Act allows a local authority to borrow money for any purpose that is within its control or for the purposes of the prudent management of its financial affairs. The main purpose for borrowing money is to fund capital expenditure although some short-term borrowing is permitted to cover temporary cash flow needs.

2.3 Since 1 April 2004 there has been no statutory limit to the amount that can be borrowed. There is, however, a requirement for full compliance with CIPFA's Prudential Code; the key objectives of which are to demonstrate that the proposed capital investment plans have been assessed by the Council as affordable, prudent and sustainable. Section 3(1) of the Act puts a duty on the Council to determine before the start of the financial year and keep under review the maximum amount that it can afford to borrow. This amount is called the **Authorised Limit** and is discussed in Appendix A.

2.4 The Prudential Indicators will be monitored via the quarterly Treasury Management monitoring reports.

3. CONSULTATION

3.1 The Council has appointed Capita Asset Services Treasury Services as its Treasury Advisers and they have been involved in the Strategy and proposals contained within this report.

4. CONCLUSION AND REASONS FOR RECOMMENDATIONS

4.1 The Executive is asked to note the Draft Treasury Management Strategy Statement for 2017/18, which incorporates the Draft Investment Strategy and the Draft MRP Strategy, together with the Prudential Indicators for 2017/18 for draft budget consultation purposes as set out in Appendix A and the Treasury Management Policy Statement as set out at Appendix D.

5. CONTRIBUTION TO THE CARLISLE PLAN PRIORITIES

5.1 To ensure the Council's investments are in line with the appropriate policies including the Treasury Management Strategy Statement.

Contact Officer: **Steven Tickner** **Ext: 7280**

Appendices attached to report:
Appendix A – Treasury Management Strategy Statement
Appendix B – Approved Investment Instruments
Appendix C – Interest Rate Forecasts
Appendix D – Treasury Management Policy Statement

Note: in compliance with section 100d of the Local Government (Access to Information) Act 1985 the report has been prepared in part from the following papers:

- **None**

CORPORATE IMPLICATIONS/RISKS:

Chief Executive's – not applicable

Economic Development – not applicable

Governance – The Council has a fiduciary duty to manage its resources effectively for the benefit of its area and the delivery of its services. Treasury Management is an important part of this function and it is appropriate that the Council has a strategy and takes account of the available specialist internal and external advice. The Treasury Management Strategy forms part of the Budget and Policy framework and, therefore, ultimately requires approval by Council.

Resources – contained within the report.

Draft Treasury Management Strategy Statement

Minimum Revenue Provision Policy Statement and Annual Investment Statement

Carlisle City Council

2017/18

1. INTRODUCTION

1.1 The Local Government Act 2003 and supporting regulations requires the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next 3 years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

1.2 The Act therefore requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance subsequent to the Act and included as paragraph 9 of this report); these set out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

1.3 The Department of Communities and Local Government has issued revised investment guidance which came into effect from 1 April 2010. There were no major changes required over and above the changes already required by the revised CIPFA Treasury Management Code of Practice 2009 and 2011.

1.4 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised November 2011) was adopted by this Council in February 2012.

1.5 The suggested strategy for 2017/18 in respect of the following aspects of the treasury management function is based upon officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury consultants. The strategy covers the following issues:

- Treasury limits in force that will limit the treasury risk and activities of the Council;
- Prudential and Treasury Indicators;
- Current treasury position;
- Borrowing requirement;
- Prospects for interest rates;
- Borrowing strategy considerations;
- Debt rescheduling opportunities.
- Investment Strategy
- Minimum Revenue Provision Strategy

1.6 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 budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This, therefore, means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from: -

- increases in interest charges caused by increased borrowing to finance additional capital expenditure, and
- any increases in running costs from new capital projects are limited to a level which is affordable within the projected income of the Council for the foreseeable future

2. TREASURY LIMITS 2017/18 TO 2019/20

2.1 It is a statutory duty, under S.3 of the Local Government Act 2003 and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount determined is termed the 'Affordable Borrowing Limit'.

2.2 The Council must have regard to the Prudential Code when setting its Affordable Borrowing Limit. This essentially requires it to ensure that total capital investment remains within sustainable limits and in particular, that the impact upon its future council tax levels is 'acceptable'. It is important to understand, however, that the Indicators themselves, which are set out in paragraph 5, do not have an inherently right or wrong answer. They are not intended as comparator information between different authorities but are designed to support and record local decision making.

3. USE OF TREASURY CONSULTANTS

3.1 The authority has, like most other authorities, employed treasury advisers for specialist advice and assistance for many years. In the case of this authority, this role has long been fulfilled by Capita Asset Services Treasury Services.

3.2 Capita Asset Services provide specialist advice on both borrowing and investment matters. They also supply other relevant information and hold regular client seminars which help provide up to date training in what is an important and continually changing field. That said, it is important to recognise that responsibility for all treasury matters lies solely with the City Council and this responsibility is not delegated to Capita Asset Services or any other third party. The Council has regard to the advice and information supplied by Capita Asset Services along with advice and information from a variety of other sources. Such advice is valued and the authority is in frequent contact with Capita Asset Services but this does lessen the ultimate responsibility of the City Council in dealing with treasury matters and taking relevant decisions.

4. CURRENT PORTFOLIO POSITION

The Council's treasury portfolio position at 30 November 2016 comprised:

Table 1		Principal £m	£m	Ave Rate %
Fixed Rate Funding	PWLB	0		
	Market	15.0	15.0	8.76
Variable Rate Funding	PWLB	0		
	Market	0	0	0.00
Other Long Term Liabilities			0	0.00
Gross Debt			**15.0**	**8.76**
Total Investments			**23.3**	**1.13**

5. PRUDENTIAL AND TREASURY INDICATORS 2017/18 - 2019/20

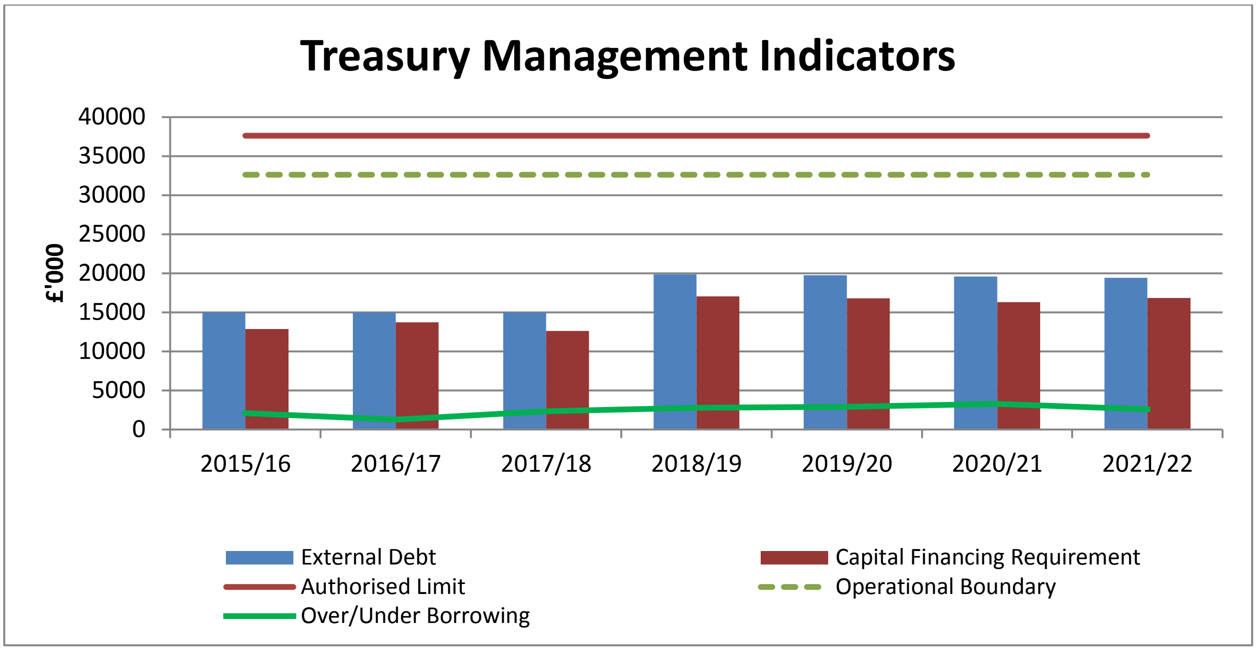
5.1 The Prudential and Treasury Indicators have been based on current projections for capital spending and resources in 2017/18 to 2019/20. The Council has ensured that future years' capital programmes have been set in accordance with the principles contained within the City Council's Capital Strategy and Asset Management Plan.

PRUDENTIAL INDICATOR AFFORDABILITY INDICATORS	2015/16 actual £000	2016/17 revised estimate £000	2017/18 estimate £000	2018/19 estimate £000	2019/20 estimate £000
Capital Expenditure	7,969	10,515	3,182	7,463	2,478
Ratio of financing costs to net revenue stream	11.74%	12.81%	13.58%	14.61%	15.48%
Net borrowing requirement in year	0	0	0	5,000	0
Capital Financing Requirement as at 31 March	12,897	13,741	12,645	17,069	16,803
Annual change in Cap. Financing Requirement	3,596	844	(1,096)	4,424	(266)
Incremental impact of capital investment decisions Increase in council tax (band D) per annum (£)	4.55	1.05	(1.36)	5.48	-0.33

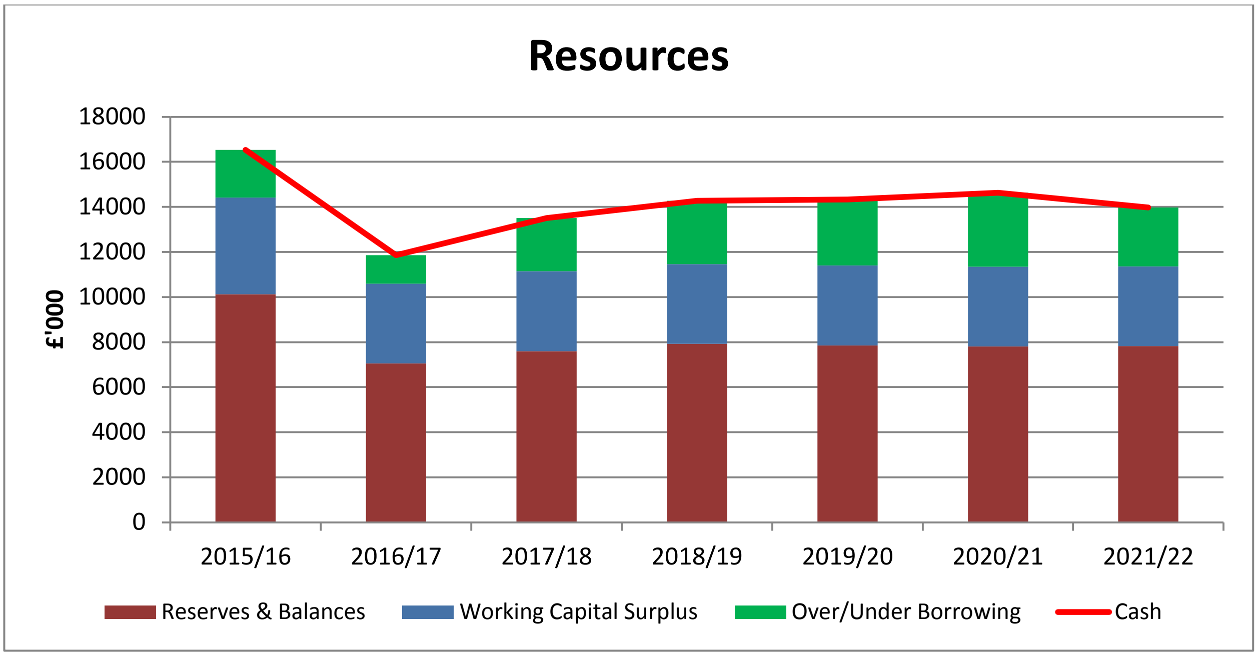
5.2 The estimates of financing costs include both current capital commitments and the draft capital programme as presented elsewhere on the agenda. In the case of this authority, it is assumed that any support from central government towards the costs of capital expenditure programmes in the next three years will be by means of a capital grant.

PRUDENTIAL INDICATOR TREASURY MANAGEMENT INDICATORS	2015/16 actual £000	2016/17 revised estimate £000	2017/18 estimate £000	2018/19 estimate £000	2019/20 estimate £000
Authorised Limit for External Debt:					
- Borrowing	37,500	37,500	37,500	37,500	37,500
- Other Long Term Liabilities	100	100	100	100	100
TOTAL	**37,600**	**37,600**	**37,600**	**37,600**	**37,600**
Operational Boundary for external debt:					
- Borrowing*	32,500	32,500	32,500	32,500	32,500
- Other Long Term Liabilities	100	100	100	100	100
TOTAL	**32,600**	**32,600**	**32,600**	**32,600**	**32,600**
Upper Limit for fixed interest rate exposure: - Net principal re. Fixed rate borrowing/investments	**100%**	**100%**	**100%**	**100%**	**100%**
Upper Limit for variable rate exposure - Net principal re. Variable rate borrowing/investments	**100%**	**100%**	**100%**	**100%**	**100%**
Upper Limit for total principal sums invested for over 1 year	**50%**	**50%**	**50%**	**50%**	**50%**

5.3 The graph below shows the level of external debt currently forecast against the Capital Financing Requirement. This shows that the Council will be in an over borrowed position for the next five years with actual debt carried being higher than the CFR.



5.4 This over-borrowed position is reflected in the level of cash resources the Council is anticipated to hold over the same period. This shows that the level of cash held as investments is as a result of the level of cash-backed reserves, working capital surpluses and the amount of over borrowing being carried.



Maturity structure of any fixed rate borrowing during 2016/17	Upper limit	Lower limit
Under 12 months	100%	0%
12 months and w ithin 24 months	100%	0%
24 months and w ithin 5 years	100%	0%
5 years and w ithin 10 years	100%	0%
10 years and above	100%	0%

5.5 In respect of its external debt, it is recommended that the Council approves the above authorised limit for its total external debt, gross of investments, for the next three financial years. The limit separately identifies borrowing from other long term liabilities such as finance leases. The Council will be asked to approve these limits and to delegate authority to the Chief Finance Officer, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities in accordance with option appraisal and best value for money. Any such change would be reported to the next available Council meeting.

5.6 The authorised limit is consistent with the authority's current commitments, plans and proposals for capital expenditure and it's financing. **However the overall authorised limit is not to be exceeded without prior Council approval.**

5.7 The operational boundary is based upon the same estimates as the authorised limit but without the headroom included within the authorised limit to allow for unusual cash movements. As with the authorised limit, the Council is asked to delegate authority to the Chief Finance Officer to effect movement between the separately agreed limits for borrowing and other long-term liabilities. The operational boundary can be exceeded in exceptional circumstances without prior Council approval providing that it remains within the authorised limit.

5.8 The City Council's current limits for maximum levels of fixed and variable rate funding are both 100% and this is as recommended by the treasury advisers.

5.9 Prudence and Sustainability
The City Council has adopted the CIPFA Code of Practice on Treasury Management in the Public Services and adopted the 2011 version of the Code in February 2012.

The current minimum level of specified investments is set at 50%. It is recommended that this level be continued into 2017/18.

5.10 Monitoring of the Prudential Indicators will be incorporated into the quarterly Treasury Transaction reports presented to the Executive.

6. PROSPECTS FOR INTEREST RATES

6.1 The Council has appointed Capita Asset Services Treasury Services as a treasury adviser to the Council and part of their service is to assist the Council to formulate a view on interest rates. The following table gives the Capita Asset Services view although it should be noted that there are some very differing views among the various economic forecasters regarding the future pattern of these rates:

	Dec'16	Mar'17	Jun'17	Sep'17	Dec'17	Mar'18	Jun'18	Sep'18	Dec'18	Mar'19	Jun'19
Bank Rate	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%

6.2 The Monetary Policy Committee, (MPC), cut 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 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:
- Italian constitutional referendum 4.12.16;
- 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.
- Dutch general election 15.3.17;
- French presidential election April/May 2017;
- French National Assembly election June 2017;
- German Federal election 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 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 2017/18 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.

7. BORROWING STRATEGY

7.1 The Capita Asset Services forecast for the PWLB new borrowing rate (repayment at Maturity) is as follows:

	Dec'16	Mar'17	Jun'17	Sep'17	Dec'17	Mar'18	Jun'18	Sep'18	Dec'18	Mar'19	Jun'19
5 Yr PWLB	1.60%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.80%	1.80%	1.90%
10Yr PWLB	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	2.40%	2.40%	2.40%	2.50%	2.50%
25Yr PWLB	2.90%	2.90%	2.90%	2.90%	3.00%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%
50Yr PWLB	2.70%	2.70%	2.70%	2.70%	2.80%	2.80%	2.80%	2.90%	2.90%	3.00%	3.00%

7.2 The Council is, as stated above, not currently expecting to have any recourse to borrowing externally in 2017/18 and although significant capital expenditure on new leisure facilities is anticipated in 2018/19 with this to be funded from borrowing, the use of internal resources, i.e. surplus investment balances may be more affordable in the short term with low investment returns forecast until 2019/20. Approval was given as part of the Capital Strategy approved in September 2016, for the Section 151 Officer to undertake external borrowing at a time it was felt to be most appropriate, taking into account forecasts for potential rises in interest rates and utilising any favourable borrowing rates. It is anticipated that a combination of capital grants and internal resources will be used to meet most, if not all, capital commitments in the new financial year. Nevertheless, the use of external borrowing is planned for future years. This is particularly the case in respect of future major capital projects which are planned to require an element of external borrowing as a part of the total funding package. The Chief Finance Officer will therefore continue to monitor the interest rate market as regards borrowing opportunities as well as in respect of investment policy.

7.3 Policy on borrowing in advance of need

7.3.1 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. As part of the Capital Strategy approved by Council in September, approval in principle was given to borrowing in advance of need for the re-financing of the stock issue loan if interest rates were favourable and would be cost effective over the term of any new loan.

7.4 External v. Internal Borrowing

7.4.1 This Council currently has a difference between gross debt and net debt (after deducting cash balances). This is shown in the graphs at 5.3 and shows an over-borrowed position with the surplus invested in cash balances.

7.4.1 The general aim of this treasury management strategy is to reduce the difference between the two debt levels over the next three years in order to reduce the credit risk incurred by holding investments. However, measures taken in the last year have already reduced substantially the level of credit risk (see paragraph 9) so another factor which will be carefully considered is the difference between borrowing rates and investment rates to ensure the Council obtains value for money once an appropriate level of risk management has been attained to ensure the security of its investments.

7.4.2 The next financial year will continue to be one of historically abnormally low Bank Rate. This provides a continuation of the current window of opportunity for local authorities to fundamentally review their strategy of undertaking new external borrowing.

7.4.3 Over the next three years, investment rates are therefore expected to be below long term borrowing rates and so value for money considerations would indicate that value could best be obtained by avoiding new external borrowing and by using internal cash balances to finance new capital expenditure or to replace maturing external debt (this is referred to as internal borrowing). This would maximise short term savings.

7.4.4 However, short term savings by avoiding new long term external borrowing in 2017/18 will also be weighed against the potential for incurring additional long term extra costs by delaying unavoidable new external borrowing until later years when PWLB long term rates are forecast to be significantly higher.

7.4.5 Against this background caution will be adopted with the 2017/18 treasury operations. The Chief Finance Officer will monitor the interest rate market and adopt a pragmatic approach to changing circumstances, reporting any decisions to the appropriate decision making body at the next available opportunity.

8. DEBT RESCHEDULING

8.1 There is unlikely to be much scope for debt rescheduling in either the current financial year or in 2017/18. Only one substantial sum of long term debt remains on the authority’s books. This is the £15m stock issue which dates from 1995 and is not due to mature until 2020. The current view is that a premature repayment is not recommended because of the size of the premium payment that would be incurred. The position remains under review, however, if circumstances should change and may become more favourable the closer it gets to natural maturity dates.

9. INVESTMENT STRATEGY

9.1 Principles

9.1.1 The City Council will have regard to CLG’s Guidance on Local Government Investments and the 2011 revised CIPFA’s Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes (“CIPFA TM Code”).

9.1.2 The Council's investment priorities are:

- The security of capital
- The liquidity of its investments

9.1.3 The Council will also endeavour to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. Security of principal will always be the primary consideration. The risk appetite of this Council is low in order to give priority to security of its investments.

9.1.4 The borrowing of monies purely to invest or to on lend and make a return is unlawful and the Council will not engage in any such activity. Any borrowing in advance of need will only be undertaken after a full financial assessment of the costs and benefits of drawing down any such funding.

9.1.5 Investment instruments identified for use in the financial year are listed below under the 'Specified' and 'Non Specified' Investment categories. Individual counterparty limits will be set through the Council's Treasury Management Practices – Schedules which will be authorised by the Chief Finance Officer.

9.1.6 Total investments with any one counterparty or group currently will not exceed £4m to ensure a reasonable spread of investments in terms of counterparties. Investments with HSBC shall not exceed £6m. However, Lloyds group and RBS Group will not exceed £8m as these establishments are currently funded by a majority shareholding by the UK Government.

9.1.7 This Annual Investment Strategy states which instruments the Council may use for the prudent management of its treasury balances during the financial year under the headings of **Specified Investments** and **Non Specified Investments**. These are listed in **Appendix B**. Essentially, specified investments are those with a maturity of up to one year which have a suitable credit rating or are otherwise guaranteed e.g. by HM Government. All other investments are non-specified.

9.1.8 Credit ratings will be used as one means of assessing the credit quality of rated counterparties although it is recognised that reliance should not be placed on credit rating alone. The minimum short term rating for a bank will be either F1 (Fitch) or P1 (Moody's). For a rated UK building society, a similar rating would be anticipated although the proposed criteria do give authority to the Chief Finance Officer to approve, if considered appropriate, the addition of other building societies with both a F2 (Fitch) and a P2 rating (Moody's). This is still a high quality credit rating but recognises the very strong record of the UK building society movement over many years in protecting the capital of all depositors. The Strategy already allows discretion to the Chief Finance Officer to include as counterparties non credit rated building societies whose assets total at least £1bn. There are some six societies in this category. Any such investment would be subject to an assessment of such a society as a suitable counterparty. There are, for example, good reasons why many building societies do not have a credit rating but there are other means of making an appropriate financial judgment.

9.1.9 Following approval in 2014/15, the Council now makes use of the CCLA Property Fund for longer term investments, and at present has invested £3m into this fund. The anticipated yield from this investment is assumed to be 4.75% in the MTFP.

9.1.10 Any investments with institutions that do not have a credit rating e.g. many smaller building societies or investments for periods over one year would be classed as non specified investments**. However it is important to stress that both the specified and non specified investments in Appendix B are perfectly legal instruments in which the City Council may invest.** This includes for example many building societies as only the larger societies have an individual credit rating although there are other criteria by which a judgement can be made as to their credit quality.

9.1.11 The minimum percentage of its overall investments that the Council will hold in specified investments is 50%.

9.2 Investment Strategy

9.2.1 With bank base rate at 0.25% and not generally expected to fluctuate significantly from this level until at least the middle of 2019, investment conditions will continue to be difficult. The view of Capita Asset Services is that bank rate will be at the following levels:

	Dec'16	Mar'17	Jun'17	Sep'17	Dec'17	Mar'18	Jun'18	Sep'18	Dec'18	Mar'19	Jun'19
Bank Rate	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%

9.2.2 Clearly, these projections can only be best estimates at this stage and the risk is to the downside i.e. if the economic recovery is slower than expected, then interest rates are like to rise more slowly. At this stage, the budget for 2017/18 has assumed an average yield of 0.46% on its investments (excluding CCLA Property Fund) in the next financial year. This allows for the fact that there are some higher value, longer term investments placed. This forecast will, however, be reviewed further during the budget cycle. Every 0.1% fall in average yield will cost the Council approximately £35,000. The anticipation of interest yielded from investing in the Property Fund is estimated at 4.75% in the MTFP.

9.2.3 In this situation, the authority will continue to try and seek value in its investments by placing them out for longer periods where possible e.g. six months to one year, to meet future cash flow needs, subject to retaining some sums for shorter periods to meet liquidity requirements and also to take advantage of any particular investment opportunities. Much of the basic framework of the authority's cash flows is already known for the next financial year and use will be made of this information in determining investment periods. The money market is monitored daily and use will be made of a plurality of sources of financial information in determining investment opportunities. All investments will be placed only with institutions that conform to the criteria set out in the Investment Strategy.

9.2.4 The investment income budget will, as ever, be carefully monitored in the coming financial year and reported to members via the regular Treasury Transactions reports.

9.3 End of Year Investment Report

In line with current practice, the Council will receive a report on its investment activity as part of the Annual Treasury Report at the end of the financial year. It should also be noted that best practice now requires a mid year report on the treasury function. This has long been the practice within the City Council where quarterly reports are presented to the Executive. In addition, the Audit Committee has taken on the role of the 'strategic committee' that oversees treasury matters.

10. THE MINIMUM REVENUE PROVISION STRATEGY

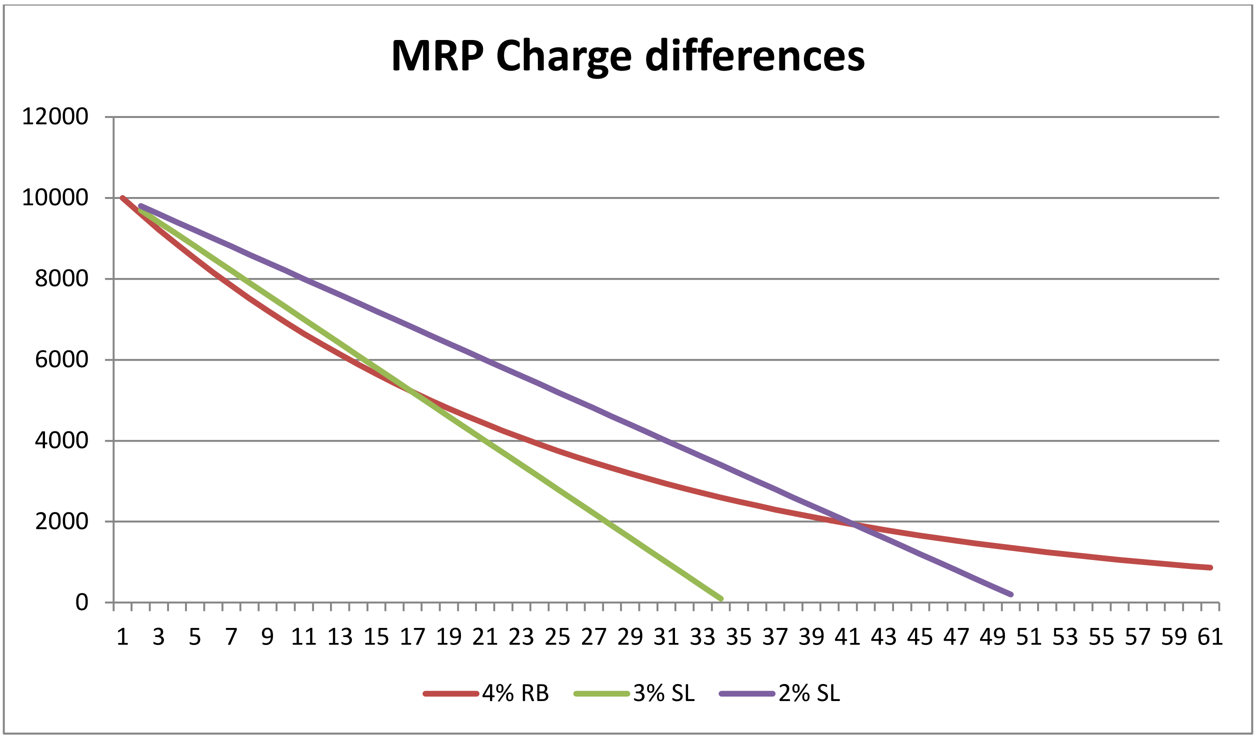
10.1 The Council implemented the new Minimum Revenue Provision (MRP) guidance in 2008/09, and will assess their MRP for 2017/18 in accordance with the main recommendations contained within the guidance issued by the Secretary of State under section 21(1A) of the Local Government Act 2003.

10.2 No requirement is currently anticipated to undertake any long term borrowing in either 2016/17 or 2017/18 although the authority will need at this stage to keep its options open and there are plans for borrowing to support future capital investment in leisure facilities in 2018/19. This is particularly so if any major capital project requires an element of long term borrowing as part of the overall funding package.

10.3 Notwithstanding this possibility, the City Council is still obliged to make proper provision for the repayment of its outstanding debt. Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. land, buildings, vehicles etc. It would usually be impractical to charge the entirety of such expenditure, which is often funded by borrowing, to the revenue account in the year it was incurred. Instead, this is spread over a longer period to try and match the years over which these assets will benefit the community. The manner of spreading these costs is through the Minimum Revenue Provision (MRP). Until recently, the MRP was calculated according to detailed and complex regulations. It is now determined under Guidance.

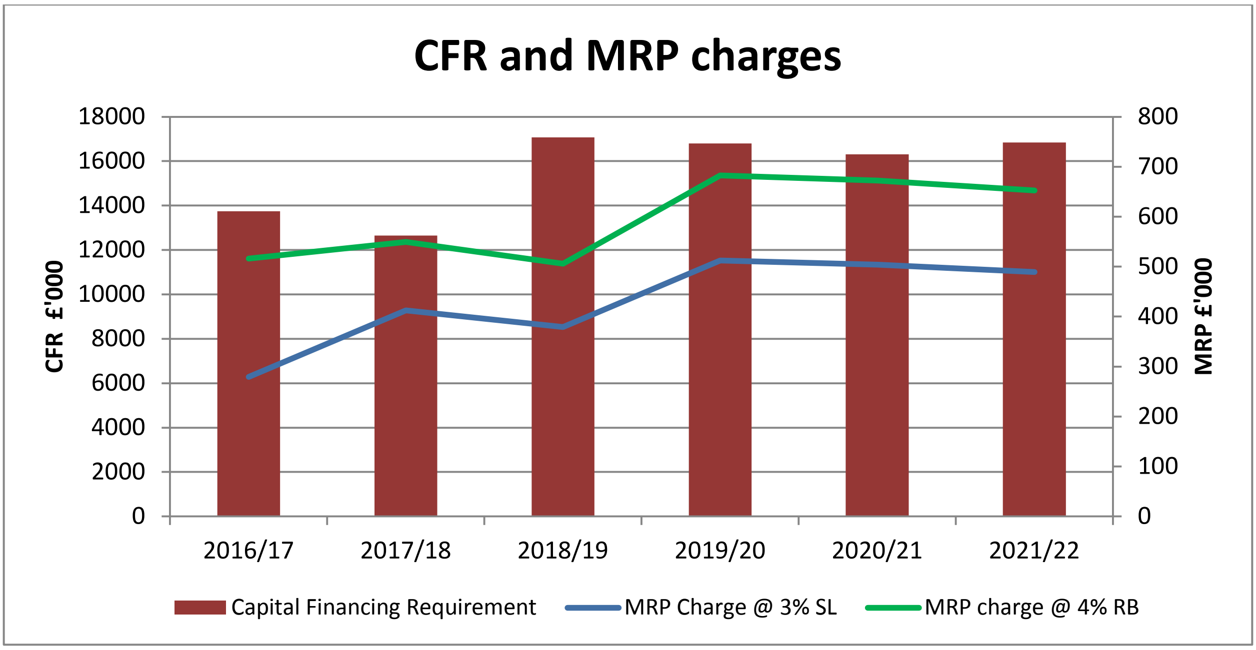
10.4 The only statutory duty that a local authority has under the new MRP regime is *'to determine for the current financial year an amount of minimum revenue provision that it considers to be prudent'*. The Guidance, which authorities must 'have regard to' provides four options for calculating the MRP as set out below. It is important to realise, however, that there is no obligation to follow any of these options and that it is up to each authority to decide upon the most appropriate method of making a prudent provision, having had regard to the Guidance.

10.5 With the guidance in mind, the Council commissioned Capita Asset Services to review its MRP policy. This was completed earlier in 2016 and the recommendation from the report is to move from a 4% reducing balance method of MRP charge to a 3% or 2% Straight Line method. One of the points highlighted in the report is that a 4% reducing balance method, never actually extinguishes the debt liability entirely, and debt is continued to be repaid even some 70 years later. Switching to a straight line method of applying MRP charges would match the debt liability to an average asset life and would see the liability repaid at a definite point in time. The differences are shown in the illustrative chart below:



10.6 A 3% charge would more reflect an average life of Council assets of 33 years and since it has a mix of short life assets such as vehicles (typical life 5-10 years) and long life assets such as land and buildings (typical life 40-50 years) this is deemed to be a prudent approach to take.

10.7 In 2016/17, the opening CFR was £12.897million which will result in an MRP of £516,000 (4% of the CFR) in this financial year. The chart below shows the anticipated CFR in future years as well as the MRP charge based on a 3% straight Line method.


CFR and MRP charges
CFR £'000
MRP £'000
18000
16000
14000
12000
10000
8000
6000
4000
2000
0
800
700
600
500
400
300
200
100
0
2016/17
2017/18
2018/19
2019/20
2020/21
2021/22
Capital Financing Requirement
MRP Charge @ 3% SL
MRP charge @ 4% RB

APPENDIX B

APPROVED INVESTMENT INSTRUMENTS

Specified Investments

All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' rating criteria where applicable. **A maximum of £4m of the investment portfolio** will be placed with any one counterparty or banking group, or a maximum of **£8m of the investment portfolio for Lloyds Group banks and RBS Group Banks and £6m with HSBC Bank (with £2m being limited to investments less than 1 month in duration)** whether by way of specified or non-specified investments except for building societies without a credit rating where **the limit will be £2m.**

Fixed Term Deposits with fixed rates and maturities:-	Minimum 'High' Credit Criteria	Use
Debt Management Agency Deposit Facility	Government backed	In-house
Term deposits – local authorities	--High level of security	In-house
Term deposits – U K banks**	Short-term F1 (Fitch) or P1(Moodys)	In-house
Term Deposits – UK building societies**	Short Term F1 (Fitch) or P1 (Moodys) or as determined by the Chief Finance Officer	In-house
Term Deposits – Non UK Banks	Sovereign Rating AAA Short Term F1 (Fitch) or P1 (Moodys) or as determined by the Chief Finance Officer	In-house
Fixed term deposits with variable rate and variable maturities: -	**Minimum 'High' Credit Criteria**	**Use**
Callable deposits	Short-term F1 (Fitch) or P1 (Moodys)	In-house
Certificates of deposits issued by UK banks and building societies	Short-term F1 (Fitch) or PI (Moodys)	In-house buy and hold
UK Government Gilts	Government backed	In-house buy and hold
Bonds issued by multilateral development banks	AAA	In-house on a 'buy-and-hold' basis.
Bonds issued by a financial institution which is guaranteed by the UK government	AAA	In-house on a 'buy-and-hold' basis.
Collective Investment Schemes structured as Open Ended Investment Companies (OEICs): -	**Minimum 'High' Credit Criteria**	**Use**
1. Money Market Funds	Short-term AAA	In-house
2. Enhanced Cash Funds	Short-term AAA	In-house
3. Government Liquidity Funds	Short-term AAA	In-house

** If forward deposits are to be made, the forward period plus the deal period should not exceed one year in aggregate.

Non-Specified Investments:

A maximum of 50% will be held in aggregate in non-specified investments

1. Maturities of ANY period.

	Minimum Credit Criteria	Use	Max % of total investments	Max. maturity period
Term deposits with non credit rated UK Building Societies	As approved by the Chief Finance Officer. Minimum asset base of £1bn	In-house	50	364 days

2. Maturities in excess of 1 year

	Minimum Credit Criteria	Use	Max % of total investments	Max. maturity period
Term deposits – local authorities	Any authority	In-house	50	3 Years
Term deposits – UK banks and building societies	Long-term A (Fitch) or A2 (Moodys)	In-house	50	3 Years
Fixed term deposits with variable rate and variable maturities	**Minimum Credit Criteria**	**Use**	**Max % of total investments**	**Max. maturity period**
Certificates of deposits issued by UK banks and building societies	Long-term A (Fitch) or A2 (Moodys)	In house on a 'buy and hold basis'	50	3 Years
UK Government Gilts	Government backed	In house on a 'buy and hold basis'	50	3 Years
Bonds issued by multilateral development banks	AAA	In-house on a 'buy-and-hold' basis.	50	3 Years
Bonds issued by a financial institution which is guaranteed by the UK government	AAA	In-house on a 'buy-and-hold' basis.	50	3 Years
Collective Investment Schemes structured as Open Ended Investment Companies (OEICs)	**Minimum Credit Criteria**	**Use**	**Max % of total investments**	**Max. maturity period**
1. Bond Funds	Long-term AAA	In-house	50	3 Years
2. Gilt Funds	Long-term AAA	In-house	50	3 Years

3. Approved Property Funds

	Use	Max % of total investments	Max. maturity period
CCLA Property Fund	In-house as determined by the Chief Finance Officer	50	No maximum

The Council uses Fitch (primarily) or Moody's ratings to derive its counterparty criteria. All credit ratings will be monitored monthly. The Council is alerted to changes in credit ratings through its use of the Sector creditworthiness service. If a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.

APPENDIX C

INTEREST RATE FORECASTS

The data below shows a variety of forecasts published by Capita Asset Services and Capital Economics. The forecast within this strategy statement has been drawn from these diverse sources and officers' own views. Revised forecasts will be provided when they become available.

1. INDIVIDUAL FORECASTS

Capita Asset Services Interest Rate View	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Dec-19	Mar-20
Bank Rate View	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%	0.75%	0.75%
3 Month LIBID	0.30%	0.30%	0.30%	0.30%	0.30%	0.30%	0.30%	0.30%	0.40%	0.50%	0.60%	0.80%	0.90%
6 Month LIBID	0.40%	0.40%	0.40%	0.40%	0.40%	0.40%	0.40%	0.40%	0.50%	0.60%	0.70%	0.90%	1.00%
12 Month LIBID	0.70%	0.70%	0.70%	0.70%	0.70%	0.70%	0.80%	0.80%	0.90%	1.00%	1.10%	1.30%	1.40%
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%	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%	2.70%
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%	3.40%
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%	3.20%
Bank Rate													
Capita Asset Services	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%	0.75%	0.75%
Capital Economics	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%	0.75%
5yr PWLB Rate													
Capita Asset Services	1.60%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.80%	1.80%	1.90%	2.00%	2.00%
Capital Economics	1.60%	1.70%	1.80%	1.90%	1.95%	2.05%	2.20%	2.30%	2.40%	2.60%	2.80%	3.20%	3.30%
10yr PWLB Rate													
Capita Asset Services	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	2.40%	2.40%	2.40%	2.50%	2.50%	2.60%	2.70%
Capital Economics	2.30%	2.35%	2.45%	2.50%	2.55%	2.60%	2.70%	2.70%	2.80%	3.00%	3.20%	3.60%	3.70%
25yr PWLB Rate													
Capita Asset Services	2.90%	2.90%	2.90%	2.90%	3.00%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.40%
Capital Economics	2.90%	3.00%	3.05%	3.10%	3.15%	3.25%	3.30%	3.35%	3.45%	3.55%	3.75%	4.15%	4.35%
50yr PWLB Rate													
Capita Asset Services	2.70%	2.70%	2.70%	2.70%	2.80%	2.80%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.20%
Capital Economics	2.80%	2.85%	2.95%	3.00%	3.05%	3.10%	3.15%	3.20%	3.30%	3.50%	3.70%	4.10%	4.20%

APPENDIX D

TREASURY MANAGEMENT POLICY STATEMENT

Carlisle City Council defines treasury management as:

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

Carlisle City Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the authority.

Carlisle City Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving best value in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.