Inverclyde council

AGENDA ITEM NO: 12

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| **Report To:** | **The Inverclyde Council** | **Date:** | **9 April 2015** |
| **Report By:** | **Corporate Director Environment, Regeneration & Resources** | **Report No:** | **SL/LP/064/15** |
| **Contact Officer:** | **Sharon Lang** | **Contact No:** | **01475 712112** |
| **Subject:** | **Treasury Management Strategy Statement and Annual Investment Strategy 2015/16 – 2017/18 – Remit from Policy & Resources Committee** | | |

## 1.0 PURPOSE

1.1 The purpose of this report is to request the Council to consider a remit from the Policy & Resources Committee of 24 March 2015.

## 2.0 SUMMARY

2.1 The Policy & Resources Committee on 24 March considered a report by the Chief Financial Officer on the Treasury Management Strategy Statement and Annual Investment Strategy for 2015/18, Treasury Policy Limits, the Council's Prudential and Treasury Management Indicators for the next three years and the List of Permitted Investments. A copy of this report is attached as Appendix 1.

2.2 The Committee decided:

(1) that the following be remitted to the Inverclyde Council for approval:

(a) Treasury Management Strategy
(b) Annual Investment Strategy
(c) Treasury Policy Limits
(d) Prudential Indicators
(e) Treasury Management Indicators
(f) List of Permitted Investments (including those for the Common Good Fund); and

(2) that the Committee note the effect of banking changes and ongoing reviews of legislation on lending by the Council to other external bodies as set out in the report to the Policy & Resources Committee

## 3.0 RECOMMENDATION

3.1 The Council is asked to consider the remit from the Policy & Resources Committee.

**Gerard Malone**
**Head of Legal & Property Services**

Inverclyde council

APPENDIX
**AGENDA ITEM NO. 12**

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| **Report To:** | **Policy & Resources Committee** | **Date:** | **24 March 2015** |
| **Report By:** | **Chief Financial Officer** | **Report No:** | **FIN/18/15/AP/KJ** |
| **Contact Officer:** | **Alan Puckrin** | **Contact No:** | **01475 712223** |
| **Subject:** | **TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY - 2015/16-2017/18** | | |

## 1.0 PURPOSE

1.1 The purpose of this report is to present to Committee the Treasury Management Strategy Statement and Annual Investment Strategy for 2015/18, Treasury Policy Limits, the Council's Prudential and Treasury Management Indicators for the next 3 years, and the List of Permitted Investments.

## 2.0 SUMMARY

2.1 The report sets out the Council's proposed Treasury Management Strategy and Annual Investment Strategy for 2015/18, Treasury Policy Limits, and Prudential and Treasury Management Indicators for the next 3 years.

2.2 The report also proposes a List of Permitted Investments listing the types of investments and limits for those investments. There are no changes to the list of permitted investments from that agreed in 2014.

2.3 The Treasury Management Strategy, Annual Investment Strategy, Treasury Policy Limits, Prudential Indicators, and Treasury Management Indicators have been set based on the Council's current and projected financial position (including projected capital expenditure) and the latest estimated interest rate levels.

2.4 In addition, the report highlights the impact of the legislation which requires the ongoing strengthening of banks and the impact of those changes on future investment returns for the Council.

2.5 In line with the Council's Financial Regulations, the proposals in this report require approval by the Full Council.

## 3.0 RECOMMENDATIONS

3.1 It is recommended that the Committee remits to the Inverclyde Council, for their approval, the following, as outlined in this report:

a. Treasury Management Strategy
b. Annual Investment Strategy
c. Treasury Policy Limits
d. Prudential Indicators
e. Treasury Management Indicators
f. List of Permitted Investments (including those for the Common Good Fund).

3.2 It is also recommended that the Committee notes the effect of banking changes and ongoing reviews of legislation on lending by the Council to other external bodies, as explained in Sections 5.40 to 5.44.

Alan Puckrin
Chief Financial Officer

## 4.0 BACKGROUND

**Statutory Requirements**

4.1 The Local Government in Scotland Act 2003 (the Act) and supporting regulations require 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 three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

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 paragraphs 5.25 to 5.40 of this report) which sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

**CIPFA Requirements**

4.2 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised November 2011) was adopted by this Council on 12th April 2012.

4.3 Treasury Management is defined in the Code as:
"The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

4.4 The primary requirements of the Code are as follows:
1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
3. Receipt by the Full Council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy - for the year ahead, a Mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.
4. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
5. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is the Policy & Resources Committee.

4.5 The proposed strategy for 2015/18 in respect of the following aspects of the treasury management function is based upon the officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury advisers.

The strategy covers:
- treasury limits in force which will limit the treasury risk and activities of the Council;
- Prudential and Treasury Management Indicators;
- the current treasury position;
- the borrowing requirement;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy;
- policy on the use of external service providers; and
- any extraordinary treasury issues.

4.6 It is a statutory requirement for the Council to produce a balanced budget. In particular, a local authority must 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 are affordable within the projected income of the Council for the foreseeable future.

4.7 Treasury Management is a complex area with its own terminology and acronyms. In order to aid the Committee's understanding a Glossary of Terms is attached as Appendix 4.

## 5.0 PROPOSED TREASURY STRATEGY, PRUDENTIAL INDICATORS AND TREASURY MANAGEMENT INDICATORS

### Treasury Limits For 2015/16 To 2017/18

5.1 It is a statutory duty under part 7 of the Local Government in Scotland Act 2003 and supporting regulations for the Council to determine and keep under review how much it can afford to allocate to capital expenditure. This amount is termed the "Affordable Capital Expenditure Limit".

5.2 The Council must have regard to the Prudential Code when setting the Affordable Capital Expenditure Limit, which 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'.

5.3 Whilst termed an "Affordable Capital Expenditure Limit", the capital plans to be considered for inclusion incorporate financing by both external borrowing and other forms of liability (such as PPP and finance lease arrangements). The affordable capital expenditure limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years.

### Prudential and Treasury Management Indicators For 2015/16 To 2017/18

5.4 Inverclyde Council has adopted the CIPFA Code of Practice on Treasury Management which was last revised in November 2011.

5.5 Members should note that, due to changes in accounting rules from 2009/10 onwards, the Prudential and Treasury Management Indicators include, where required, the effect of assets being provided to the Council under PPP and finance lease arrangements.

### Current Portfolio Position

5.6 The Council's treasury portfolio position at 18/2/2015 (Number 9 – Prudential Indicator) comprised:

| | | Principal | | Average Rate |
|---|---|---|---|---|
| | | £000 | £000 | |
| Fixed rate funding | PWLB | 116,448 | | |
| | Market | 36,000 | 152,448 | 3.91% |
| Variable rate funding | PWLB | 0 | | |
| | Market | 66,942 | 66,942 | 4.81% |
| | | | 219,390 | 4.19% |
| Other long term liabilities | | | 69,684 | --- |
| **TOTAL DEBT** | | | **289,118** | |
| **TOTAL INVESTMENTS** | | | **55,381** | **0.72%** |

**Borrowing Requirement**

5.7 The Council's borrowing requirement is as follows:

| | 2013/14 | 2014/15 | 2015/16 | 2016/17 | 2016/17 |
|---|---|---|---|---|---|
| | £000 Actual | £000 Projected | £000 Estimate | £000 Estimate | £000 Estimate |
| New borrowing | 0 | 0 | 0 | 12,000 | 7,000 |
| Alternative financing arrangements | 0 | 0 | 0 | 0 | 0 |
| Replacement borrowing | 0 | 0 | 0 | 5,500 | 500 |
| TOTAL | 0 | 0 | 0 | 17,500 | 7,500 |

5.8 The Council's Gross Debt v. Capital Financing Requirement (including the effect of the proposed borrowing as shown in Section 5.7) is as follows:

| Comparison of Gross Debt and Capital Financing Requirement At Year-End | 2013/14 | 2014/15 | 2015/16 | 2016/17 | 2017/18 |
|---|---|---|---|---|---|
| | £000 Actual | £000 Projected | £000 Estimate | £000 Estimate | £000 Estimate |
| External Debt (Including PPP and Finance Leases) | 291,875 | 283,999 | 280,864 | 290,800 | 296,262 |
| Capital Financing Requirement | 304,506 | 301,840 | 301,349 | 320,317 | 319,222 |
| Under/(Over) Against Latest CFR Projection For Year | 12,631 | 17,841 | 20,485 | 29,517 | 22,960 |

5.9 The main Prudential and Treasury Management Indicators are as follows:

| | **2014/15** | **2014/15** | **2015/16** | **2016/17** | **2017/18** |
|---|---|---|---|---|---|
| | **Estimate** | **Probable Outturn** | **Estimate** | **Estimate** | **Estimate** |
| **Capital Expenditure (Number 5 - Prudential Indicator)** | £000 | £000 | £000 | £000 | £000 |
| Capital Programme | 27,872 | 25,279 | 29,486 | 46,368 | 20,617 |
| PPP Schools/Finance Leases (incl. accounting adjustments) | (2,109) | (2,080) | (1,904) | (2,035) | (1,597) |
| Total | 25,763 | 23,199 | 27,582 | 44,333 | 19,020 |
| **Ratio of financing costs (including PPP/ Finance Leases) to net revenue stream (Number 1 - Prudential Indicator)** | | | | | |
| Non – HRA | 12.27% | 11.73% | 11.90% | 13.14% | 13.95% |
| **Net external borrowing and capital financing requirement (Number 4 - Prudential Indicator)** | £000 | £000 | £000 | £000 | £000 |
| As At 31 March | (56,638) | (68,010) | (54,135) | (42,573) | (30,012) |
| **Capital Financing Requirement as at 31 March (Number 6 - Prudential Indicator)** | £000 | £000 | £000 | £000 | £000 |
| Non – HRA | 307,429 | 301,840 | 301,349 | 320,317 | 319,222 |
| **Upper limit for total principal sums invested for over 364 days (Number 14 - Treasury Management Indicator)** | £10,000,000 | £0 * | £10,000,000 | £10,000,000 | £10,000,000 |

* - This is the probable outturn of investments beyond 364 days as at 31/3/15 (against an upper limit of £10,000,000). There were no sums invested beyond 364 days during 2014/15.

| | 2014/15 | 2015/16 | 2016/17 | 2017/18 |
|---|---|---|---|---|
| | **Estimate** | **Estimate** | **Estimate** | **Estimate** |
| **Authorised limit for external debt (Number 7 - Treasury Management Indicator)** | £000 | £000 | £000 | £000 |
| Borrowing | 262,000 | 239,000 | 260,000 | 261,000 |
| Other long term liabilities | 74,000 | 68,000 | 66,000 | 65,000 |
| TOTAL | 336,000 | 307,000 | 326,000 | 326,000 |
| **Operational boundary for external debt (Number 8 - Treasury Management Indicator)** | £000 | £000 | £000 | £000 |
| Borrowing | 255,000 | 234,000 | 255,000 | 256,000 |
| Other long term liabilities | 72,000 | 68,000 | 66,000 | 65,000 |
| TOTAL | 327,000 | 302,000 | 321,000 | 321,000 |

| | 2015/16 | 2016/17 | 2017/18 |
|---|---|---|---|
| | **Estimate** | **Estimate** | **Estimate** |
| **Incremental impact of capital investment decisions** | | | |
| Incremental increase in council tax (band D) per annum (Number 2 - Prudential Indicator) | £0.10 | £0.03 | £0.08 |
| | | | |
| **Upper limit for fixed interest rate exposure (Number 11 - Treasury Management Indicator)** | 140% | 130% | 120% |
| | | | |
| **Upper limit for variable rate exposure (Number 12 - Treasury Management Indicator)** | 40% | 40% | 40% |

5.10 The limits on the maturity of fixed rate borrowing during 2015/16 (Number 13 – Treasury Management Indicator) are as follows:

| **Maturity Structure** | Upper Limit | Lower Limit | 2014/15 Probable Outturn |
|---|---|---|---|
| Under 12 months | 45% | 0% | 0.47% |
| 12 months and within 24 months | 45% | 0% | 3.75% |
| 24 months and within 5 years | 45% | 0% | 42.10% |
| 5 years and within 10 years | 45% | 0% | 20.52% |
| 10 years and within 30 years | 45% | 0% | 6.02% |
| 30 years and within 50 years | 45% | 0% | 27.14% |
| 50 years and within 70 years | 45% | 0% | 0.00% |

This Indicator has been prepared in accordance with the revised Treasury Management Code which requires that the Council's Market debt (see 5.6 above) is shown based not on when the debt is due to actually mature but on when the lender could request an increase in the interest rate (when the Council could accept the increase or repay the debt). At 31/3/2015 £66.9m of the Council's £102.9m Market Debt is treated as variable on this basis (rather than fixed rate) and so is not included in the 2014/15 Probable Outturn figures in the table above.

**Treasury Policy Limits**

5.11 In addition to the Prudential Indicators and Treasury Management Indicators, the Council has Policy Limits, as follows:

| | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2014/15 Probable Outturn at Year-End |
|---|---|---|---|---|
| **Maximum Percentage of Debt Repayable In Any Year** | 25% | 25% | 25% | 18.23% |
| **Maximum Proportion of Debt At Variable Rates** | 40% | 45% | 45% | 30.50% |
| **Maximum Percentage of Debt Restructured In Any Year** | 30% | 30% | 30% | 0.000% |

**Prospects For Interest Rates**

5.12 The Council has appointed Capita Treasury Solutions Ltd (who use the trading name "Capita Asset Services") as treasury advisers and part of their service is to assist the Council to formulate a view on interest rates. The table in Section 5.13 gives the Capita view.

5.13 Capita interest rate forecasts – 13th February 2015

| As At | Bank Rate | Investment (LIBID) Rates | | | PWLB Borrowing Rates | | | |
|---|---|---|---|---|---|---|---|---|
| | | 3 month | 6 month | 1 year | 5 year | 10 Year | 25 year | 50 year |
| | % | % | % | % | % | % | % | % |
| March 2015 | 0.50 | 0.50 | 0.70 | 0.90 | 2.10 | 2.70 | 3.30 | 3.30 |
| June 2015 | 0.50 | 0.50 | 0.70 | 1.00 | 2.20 | 2.80 | 3.40 | 3.40 |
| Sept 2015 | 0.50 | 0.50 | 0.70 | 1.00 | 2.30 | 3.00 | 3.60 | 3.60 |
| Dec 2015 | 0.50 | 0.60 | 0.80 | 1.10 | 2.50 | 3.10 | 3.80 | 3.80 |
| March 2016 | 0.75 | 0.80 | 1.00 | 1.30 | 2.60 | 3.20 | 3.90 | 3.90 |
| June 2016 | 0.75 | 0.90 | 1.10 | 1.40 | 2.70 | 3.40 | 4.00 | 4.00 |
| Sept 2016 | 1.00 | 1.10 | 1.30 | 1.60 | 2.80 | 3.50 | 4.20 | 4.20 |
| Dec 2016 | 1.25 | 1.30 | 1.50 | 1.80 | 3.00 | 3.60 | 4.30 | 4.30 |
| March 2017 | 1.25 | 1.40 | 1.60 | 1.90 | 3.10 | 3.70 | 4.40 | 4.40 |
| June 2017 | 1.50 | 1.50 | 1.70 | 2.00 | 3.20 | 3.80 | 4.50 | 4.50 |
| Sept 2017 | 1.50 | 1.80 | 2.00 | 2.30 | 3.30 | 3.90 | 4.60 | 4.60 |
| Dec 2017 | 1.75 | 1.90 | 2.10 | 2.40 | 3.40 | 4.00 | 4.60 | 4.60 |
| March 2018 | 2.00 | 2.10 | 2.30 | 2.60 | 3.50 | 4.10 | 4.70 | 4.70 |

5.14 Appendix 1 explains the Economic Background affecting the proposed Treasury Management Strategy and Annual Investment Strategy.

**Borrowing Strategy**

5.15 Capita advise that UK GDP growth increased during 2013 and the first half of 2014. During the second half of 2014, it reduced but still remained strong by UK standards. Growth is likely to strengthen marginally in 2015 and 2016 under the stimulative effect of the fall in oil prices. There still needs to be a significant rebalancing of the economy away from consumer spending to manufacturing, business investment and exporting in order for this recovery to become more firmly established. One drag on the economy has been that wage inflation had only recently started to exceed Consumer Price Inflation ("CPI"), so enabling disposable income and living standards to start improving. The plunge in the price of oil brought CPI inflation down to a low of 0.5% in December, the lowest rate since May 2000 and it could even turn negative in the first half of 2015; this will further increase consumer disposable income and so underpin economic growth during 2015. However, labour productivity needs to improve substantially to enable wage rates to increase and further support consumer disposable income and economic growth. In addition, the encouraging rate at which unemployment has been falling must eventually feed through into pressure for wage increases, though current views on the amount of hidden slack in the labour market probably means that this is unlikely to happen early in 2015.

The US, the biggest world economy, has generated growth rates of 4.6% (annualised) in Q2 2014 and 5.0% in Q3, followed by a cooler 2.6% in Q4 (overall 2.4% for 2014 as a whole). This is hugely promising for the outlook for strong growth going forwards and it very much looks as if the US is now firmly on the path of full recovery from the financial crisis of 2008. Consequently, it is now confidently expected that the US will be the first major western economy to start on central rate increases by the end of 2015.

5.16 The current economic outlook and structure of market interest rates and government debt yields have several key treasury management implications:

- Greece: the general election on 25 January 2015 brought to power a coalition which is strongly anti-EU imposed austerity. However, if this should eventually result in Greece leaving the Euro, it is unlikely that this will directly destabilise the Eurozone as the EU has put in place adequate firewalls to contain the immediate fallout to just Greece. However, the indirect effects of the likely strenthening of anti-EU and anti-austerity political parties throughout the EU is much more difficult to gauge;
- As for the Eurozone in general, concerns in respect of a major crisis subsided considerably in 2013. However, the downturn in growth and inflation during the second half of 2014 and worries over the Ukraine situation and the Middle East have led to a resurgence of those concerns as risks increase that it could be heading into a prolonged period of deflation and very weak growth. Sovereign debt difficulties have not gone away and major concerns could return in respect of individual countries that do not dynamically address fundamental issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy (as Ireland has done). It is, therefore, possible over the next few years that levels of government debt to GDP ratios could continue to rise to levels that could result in a loss of investor confidence in the financial viability of such countries. Counterparty risks therefore remain elevated. This continues to suggest the use of higher quality counterparties for shorter time periods;
- Investment returns are likely to remain relatively low during 2015/16 and beyond;
- Borrowing interest rates have been highly volatile during 2014 and early 2015 as alternating bouts of good and bad news have promoted optimism, and then pessimism, in financial markets. The opening weeks of 2015 saw gilt yields dip to historically phenominally low levels after inflation plunged, a flight to quality as a result of the Greek situation and the start of a huge programme of quantitative easing (purchase of Eurozone government debt), by the ECB in January 2015. 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 new capital expenditure and/or to refinance maturing debt;
- There will remain a cost of carry to any new borrowing which causes an increase in investments as this will incur a revenue loss between borrowing costs and investment returns.

5.17 In normal circumstances the main sensitivities of the forecast are likely to be the two scenarios noted below. Officers, in conjunction with the treasury advisers, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- 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 would be postponed, and potential rescheduling from fixed rate funding into short term borrowing would be considered.

- If it was felt that there was a significant risk of a much sharper rise in long and short term rates than that currently forecast, perhaps arising from a faster than currently anticipated unwinding of quantitative easing in the US, or an unexpected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the possibility that fixed rate funding will be drawn whilst interest rates are still lower than they will be in the next few years.

5.18 Against this background, caution will be adopted with the 2015/16 treasury operations. The Chief Financial Officer will monitor the interest rate market and adopt a pragmatic approach to changing circumstances, reporting any decisions to the Policy & Resources Committee.

5.19 Policy on Borrowing in Advance of Need

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

In determining whether borrowing will be undertaken in advance of need the Council will:

- Consider the definition of such borrowing within the Code on the Investment of Money By Scottish Local Authorities
- Ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need
- Ensure the ongoing revenue liabilities created, and the implications for the future plans and for the budgets have been considered
- Evaluate the economic and market factors that might influence the manner and timing of any decision to borrow
- Consider the merits and demerits of alternative forms of funding
- Consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use
- Consider the impact of borrowing in advance on temporarily (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk and other risks and the level of such risks given the controls in place to minimise them.

The maximum extent to which borrowing in advance would be undertaken by this Council is the borrowing requirement identified in Section 5.7 above for 2015/2018.

**Debt Rescheduling**

5.20 The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt has been compounded since 20 October 2010 by a considerable further widening of the difference between new borrowing and repayment rates. This has meant that PWLB-to-PWLB debt restructuring is now much less attractive than it was before both of these events. In particular, consideration would have to be given to the large premiums which would be incurred by prematurely repaying existing PWLB loans and it is very unlikely that these could be justified on value for money grounds if using replacement PWLB refinancing. Some interest savings might, however, still be achievable through using LOBO (Lenders Option Borrowers Option) loans and other market loans in rescheduling exercises rather than using PWLB borrowing as the source of replacement financing.

5.21 As short term borrowing rates will be considerably cheaper than longer term 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 their short term nature and the likely cost of refinancing those short term loans, once they mature, compared to the current rates of longer term debt in the existing debt portfolio.

5.22 The Council is more likely to look at 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 currently held debt.

5.23 The reasons for any rescheduling to take place will include:

- The generation of cash savings and/or discounted cash flow savings but at minimum risk;
- Helping to fulfil the strategy outlined above; and
- Enhancing the balance of the portfolio (amending the maturity profile and/or the balance of volatility).

5.24 All rescheduling will be reported to the Policy & Resources Committee and the Full Council and will be within the Treasury Policy Limits.

**Annual Investment Strategy**

5.25 Investment Policy
The Council will have regard to the Local Government Investment (Scotland) Regulations 2010 and accompanying finance circular and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross-Sectoral Guidance Notes (“the CIPFA TM Code”). The Council’s investment priorities are:

(a) The security of capital
and
(b) The liquidity of its investments.

The Council will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite of this Council is low in order to give priority to the security of its investments.

5.26 The borrowing of monies purely to invest or on-lend and make a return is unlawful and this Council will not engage in such activity.

5.27 There are a large number of investment instruments that the Council could use. The list of investment instruments proposed for possible use by the Council (including those for the Common Good Fund) are listed in Appendix 2 along with details of the risks from each type of investment. The list of proposed investments reflects a low risk appetite and approach to investments by the Council.

**There are no changes to the list of permitted investments from that agreed in 2014.**

5.28 Counterparty limits will be as set through the Council’s Treasury Management Practices.

5.29 Appendix 3 is a list of forecasts of investment balances.

5.30 Bank of Scotland – Counterparty Limit
The Council’s Counterparty Limit for investments with the Bank of Scotland is currently £60m but is due to revert back to £50m at the end of June 2015. The £50m level is the limit set in the Council’s Treasury Management Practices document.

5.31 Creditworthiness Policy

The Council uses the creditworthiness service provided by Capita Treasury Solutions Ltd. This service uses a sophisticated modelling approach using credit ratings from the three main rating agencies - Fitch, Moody's, and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- Credit watches and credit outlooks from credit rating agencies (indicating the likelihood of ratings changes for a counterparty or the expected direction of ratings for a counterparty)
- Credit Default Swap ("CDS") spreads to give early warning of likely changes in credit ratings
- Sovereign ratings to select counterparties from only the most creditworthy countries.

5.32 This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are also used by the Council to determine the duration for investments.

The approach is reviewed by Capita as required in light of banking system and regulatory changes e.g. the coming reduction in importance of support ratings for individual banks due to the removal of implied government support to banks.

5.33 The Council will use counterparties within the following durational bands and with the following limits per counterparty:

| Colour Category | Maximum Period for Individual Investments | Limit for Total Investments with Individual Counterparty |
|---|---|---|
| Purple | 2 Years | £15m |
| Blue (Nationalised or Semi-Nationalised UK Banks) | 1 Year | £15m |
| Orange | 1 Year | £15m |
| Red | 6 Months | £15m |
| Green | 100 Days | £10m |
| No Colour | Not To Be Used | £NIL |

The maximum period for individual investments with the Council's own bankers will be as in accordance with the above table whilst the limit for total investments will be £50m or as agreed by Committee.

Members should note that these are the maximum periods for which any investment with a counterparty meeting the criteria would take place but subject to the Council's policy on Investment instruments.

5.34 The Capita creditworthiness service uses a wider array of information than just primary ratings and, by using a risk weighted scoring system, does not give undue preponderance to just one agency's ratings.

Typically the minimum credit ratings criteria the Council use will be a short term rating (Fitch or equivalents) of Short Term rating of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

5.35 All credit ratings are monitored on an ongoing basis. The Council is alerted to changes to ratings of all three agencies through its use of the Capita 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.
- In addition to the use of Credit Ratings the Council will be advised of information in movements in Credit Default Swap spreads against a benchmark (the iTraxx index) and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. The Council also uses (where available) market data and market information, information on government support for banks and the credit ratings of that government support.

5.36 Country Limits
It is proposed that the Council will only use approved counterparties from the UK or from countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide). Countries currently meeting this criterion include Australia, Canada, France, Germany, Sweden, the USA, and the UK.

5.37 Investment Strategy
The Bank Rate has been unchanged at 0.50% since March 2009. It is forecast to remain at this level until quarter 4 of 2015 and then to rise gently from thereon. Bank Rate forecasts for financial year ends (March) are as follows:

- 2015/16 0.75%
- 2016/17 1.25%
- 2017/18 2.00%.

There are downside risks to these forecasts (i.e. the start of increases in Bank Rate occurs later) if economic growth weakens. However, should the pace of growth quicken, there could be an upside risk.

5.38 Capita advise that, for 2015/16, clients should budget for an investment return of 0.60% on investments placed during the financial year for periods of up to 100 days.

5.39 The Council will avoid locking into longer term deals while investment rates are down at historically low levels unless attractive rates are available with counterparties of particularly high creditworthiness which make longer term deals worthwhile and within the risk parameters set by this Council.

5.40 As part of the process of strengthening banks and the increased regulation of banks following the banking and financial crisis, the banking regulatory authorities in the UK and the EU have been introducing further directives and regulations relating to issues such as bank capital and reserves to be held in case the banks hit financial problems. The regulators also undertake stress tests of individual banks to test the resilience of their financial position if there were to be particular economic scenarios e.g. a significant drop in house prices accompanied by an increase in unemployment at the same time as an increase in interest rates/funding costs.

5.41 Members should note that the some of the changes in banking regulations being implemented in the UK and the EU to further strengthen banks will further reduce the interest rates that they are likely to see on their own bank deposit accounts as individuals (relative to the Bank Rate) and will also impact on the rates receivable by the Council on its investments. It is likely that the Council and private individuals will receive much lower rates for call monies (instant access investments) or very short term investments than it/they will for investments of 32 days and above.

5.42 At the moment the Council receives the Bank Rate of 0.50% on call monies from the Bank of Scotland under the terms of its current banking contract but we have been advised that the regulatory changes mean that the rate is likely to be reduced in the future once the current contract ends. A rate reduction will have an impact, in due course, on Council investment returns and therefore budgets and thereby making it increasingly more attractive for the Council to reduce, as far as practicable, its investment balances (whilst taking account of ongoing capital expenditure and other requirements as well as movements in borrowing costs).

5.43 The Bank of Scotland is part of the Lloyds Banking Group which is currently part owned by the UK Government. This Government ownership gives added support to the bank which means that the Bank of Scotland falls into Capita's Blue category for creditworthiness (see Section 5.33 above) allowing deals up to 1 year. The introduction of Bail In powers in the UK from 1 January 2015 (preventing Governments from stepping in to support banks, albeit banks that have recapitalised and been strengthened) and the likely future sale of the Government's shares in the Lloyds Banking Group will see the Bank of Scotland moved to another of the creditworthiness colour categories and a change to the maximum period with which the Council can invest with them.

5.44 Under the Investment Regulations, any loans that the Council provides to external bodies (such as Inverclyde Leisure) count as investments. Ongoing reviews of legislation mean that Councils may well be given additional powers to lend to other external bodies but only after appropriate due diligence is done including full financial assessments of the proposals for repaying any loan and any security to be granted whilst the loan is in place.

5.45 End of Year Investment Report
At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

**P7olicy on Use of External Service Providers**

5.46 The Council uses Capita Treasury Solutions Ltd as its external treasury management advisers and uses the services of brokers for investment deals as required. The Council's current contract with Capita finishes on 30th June 2015 but discussions have taken place with Capita towards agreeing a new contract, as approved by Committee in November 2014.

5.47 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.

5.48 The Council 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.

**Policy on Scrutiny, Monitoring and Change of Investment Policies and Practices**

5.49 The Treasury Management Practices (TMPs) of the Council set out the operational policies and procedures in place to implement the treasury management strategy and the principles set out in the treasury management policy statement. They are intended to minimise the risk to the capital sum of investments and for optimising the return on the funds consistent with those risks.

5.50 The TMPs are kept under review, with a full revision every 3 years. The last full revision was in 2014.

5.51 A copy of the TMPs may be obtained from Finance Services.

**Training for Members**

5.52 A specific training session on Treasury Management will be organised for Members in the next 12 months.

## 6.0 IMPLICATIONS

**Finance**

6.1 Adopting the Treasury Strategy and the Investment Strategy for 2015/16 and the following two years will allow a balance to be maintained between opportunities to continue to generate savings for the Council and minimising the risks involved.

**Legal**

6.2 There are no Legal implications arising from this report.

**Human Resources**

6.3 There are no HR implications arising from this report.

**Equalities**

6.4 There are no equalities implications arising from this report

**Repopulation**

6.5 There are no repopulation implications arising from this report.

## 7.0 CONSULTATIONS

7.1 This report has been produced based on advice from the Council's treasury advisers (Capita Treasury Solutions Limited).

## 8.0 LIST OF BACKGROUND PAPERS

8.1 CIPFA - Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes – 2011 Edition
CIPFA – The Prudential Code for Capital Finance in Local Authorities – 2011 Edition
Scottish Government – The Local Government Investments (Scotland) Regulations 2010 (Scottish Statutory Instrument 2010 No. 122)
Scottish Government - Finance Circular 5/2010 Investment of Money by Scottish local authorities 1.4.10.

**Appendix 1**

## ECONOMIC BACKGROUND

The following economic background is based on information from the Council's treasury advisers, Capita Treasury Solutions Ltd

1. **The UK Economy**
   a. After strong UK GDP growth in 2013 at an annual rate of 2.7%, and then growth in 2014 of 0.6% in Q1, 0.8% Q2, 0.7% Q3 and 0.5% Q4 (annual rate for 2014 of 2.6%), growth is expected to gain increased momentum during 2015 and 2016 to annual rates of 2.9%, (2017 2.7%). This will be a response to two developments; firstly, the stimulative effect of the sharp fall in oil prices in quarter 4 of 2014 and then inflation potentially falling into negative territory during 2015, but being near to zero until towards the end of the year. Secondly, due to an expected return to a significant rise in average wage rates due to the continuing fall in unemployment to about 5.5% by mid 2015, (the long run equilibrium level is 5.0%), and the further erosion of spare capacity, (slack), to about 0.5% of GDP. This is expected to lead to total consumer disposable income rising by no less than around 3.5% during quarter 3 2015. This would therefore strengthen consumer expenditure, but without much downside to the savings ratio (the proportion of disposable income that is usually put into savings accounts) .

   b. However, for this recovery to become more balanced and sustainable in the longer term, the recovery still needs to move away from dependence on consumer expenditure and the housing market to exporting, and particularly of manufactured goods, both of which need to substantially improve on their recent lacklustre performance. In addition, there has been a need for a major improvement in labour productivity, which has languished at dismal levels since 2008, to support longer term increases in pay rates and economic growth after the positive effect of the fall in oil prices dissipates. The February 2015 Inflation Report contained good news that productivity was forecast to increase by just under 0.75% in the first three quarters of 2015.

   c. The February Inflation Report also explained that the initial fall in the price of oil of over 50% would cause an overall reduction in CPI of about 0.8% in quarter 2 2015 and boost UK GDP by around 0.5% during the Monetary Policy Committee's three year forecast period. It also forecast that the sharp fall in the price of oil and its knock on effects, would start falling out of the twelve month calculation of CPI inflation in quarter 4 of 2015. This is expected to result in a sharp rise in inflation from near zero in that quarter and also onward into 2016. The report also mentioned a potential risk of deflation becoming embedded, which could then require remedial action by the Monetary Policy Committee such as a cut in Bank Rate and / or further quantitative easing. This is viewed as being a small risk given the above expected sharp increase in inflationary pressures. However, while inflation is at or near 0% for much of 2015, it is unlikely that the Monetary Policy Committee would make a start on increasing the Bank Rate. Market expectations for the first increase in the Bank Rate have therefore moved from quarter 3 2015 after the November 2014 report, to around mid year 2016 during February 2015. However, the Monetary Policy Committee is focused on where inflation will be over a 2 – 3 year time horizon so too much emphasis should not be placed on the short term inflation outlook, especially when the February report identified a slight increase in inflationary pressures on that time horizon to just above the 2% target. This treasury management report is therefore based on a forecast of a first increase in Bank Rate in quarter 1 of 2016, though it would be quite possible for it to be in quarter 4 of 2015 if events were to turn out favourably in Greece, the Eurozone as a whole and elsewhere.

   d. The return to strong growth has helped lower forecasts for the increase in Government debt over the last year but monthly public sector deficit figures during 2014 have disappointed, being only a fraction lower than the previous year through to December 2014. The Chancellor's Autumn Statement, therefore, had to revise the speed with which the deficit is forecast to be eliminated. The flight to quality in January 2015 has seen gilt yields fall to incredibly low levels, which will reduce interest costs on new and replacement government debt.

## 2. The Global Economy

Eurozone

a. The Eurozone is facing an increasing threat from weak or negative growth and from deflation. In January 2015, the inflation rate fell further, to reach a low of -0.6%. However, this is an average for all Eurozone countries and includes some countries with even higher negative rates of inflation. Initially, the European Central Bank ("ECB") took some rather limited action in June and September 2014 to loosen monetary policy in order to promote growth. As this failed to have much of a discernible effect, the ECB launched a massive €1.1 trillion programme of quantitative easing in January 2015 to buy up high credit quality government debt of selected Eurozone countries. This programme will run to September 2016.

b. Concern in financial markets for the Eurozone had subsided considerably after the prolonged crisis during 2011-2013. However, sovereign debt difficulties have not gone away and major issues could return in respect of any countries that do not dynamically address issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy, (as Ireland has done). It is, therefore, possible over the next few years that levels of government debt to GDP ratios could continue to rise for some countries. This could mean that sovereign debt concerns have not disappeared but, rather, have only been postponed. The ECB's pledge in 2012 to buy unlimited amounts of bonds of countries which ask for a bailout has provided heavily indebted countries with a strong defence against market forces. This has bought them time to make progress with their economies to return to growth or to reduce the degree of recession. However, debt to GDP ratios (2013 figures) of Greece 180%, Italy 133%, Portugal 129%, Ireland 124% and Cyprus 112%, remain a cause for concern, especially as some of these countries are experiencing continuing rates of increase in debt in excess of their rate of economic growth i.e. these debt ratios are likely to continue to deteriorate. Any sharp downturn in economic growth would make these countries particularly vulnerable to a new bout of sovereign debt crisis. It should also be noted that Italy has the third biggest debt mountain in the world behind Japan and the US.

Greece

c. The general election on 25 January 2015 has brought to power a coalition which is anti-EU imposed austerity. Although it is not certain that Greece will leave the Euro, the recent intractability of the troika (the EU, ECB and IMF), to finding a negotiated compromise with the new Greek government leaves this as a real possibility. However, if Greece was to leave the Eurozone, it is unlikely that this will directly destabilise the Eurozone as the EU has put in place adequate firewalls to contain the immediate fallout to just Greece. Nevertheless, the indirect effects of the likely strengthening of anti-EU and anti-austerity political parties throughout the EU is much more difficult to gauge. There are particular concerns as to whether democratically elected governments will lose the support of electorates suffering under Eurozone imposed austerity programmes, especially in countries which have high unemployment rates. Of particular concern is the fact that Spain and Portugal have general elections coming up in late 2015. This will give ample opportunity for anti-austerity parties to make a big impact.

d. There are also major concerns as to whether the governments of France and Italy will effectively implement austerity programmes and undertake overdue reforms to improve national competitiveness. These countries already have political parties with major electoral support for anti EU and anti-austerity policies. Any loss of market confidence in either of the two largest Eurozone economies, after Germany, would present a huge challenge to the resources of the ECB to defend their debt.

USA

e. The U.S. Federal Reserve ended its monthly asset purchases in October 2014. GDP growth rates (annualised) for Q2 of 4.6%, Q3 of 5.0% and Q4 of 2.6%, (overall 2.4% during 2014 as a whole), provides great promise for strong growth going forward. It is confidently forecast that the first increase in the Fed Rate (the US interest rate) will occur by the end of 2015.

China

f. Government action in 2014 to stimulate the economy almost succeeded in achieving the target of 7.5% growth but recent government statements have emphasised that growth going forward will slow marginally as this becomes the new normal for China. There are concerns that the Chinese leadership has only just started to address an unbalanced economy, which is heavily over dependent on new investment expenditure, and for a potential bubble in the property sector to burst, as it did in Japan in the 1990s, with its consequent impact on the financial health of the banking sector. There are also concerns around the potential size, and dubious creditworthiness, of some bank lending to local government organisations and major corporates. This primarily occurred during the government promoted expansion of credit, which was aimed at protecting the overall rate of growth in the economy after the Lehmans crisis in 2008.

Japan

g. Japan is causing considerable concern as the increase in sales tax in April 2014 has suppressed consumer expenditure and growth to the extent that it has slipped back into recession. The Japanese government already has the highest debt to GDP ratio in the world.

## 3. Capita's Forward View

a. Economic forecasting remains difficult with so many external influences weighing on the UK. The Bank Rate forecasts (and also Monetary Policy Committee decisions) will be liable to further amendment depending on how economic data transpires over 2015. Forecasts for average earnings beyond the three year time horizon will be heavily dependent on economic and political developments. Major volatility in bond yields is likely to endure as investor fears and confidence ebb and flow between favouring more risky assets i.e. equities, or the safe haven of bonds.

b. The overall longer run trend is for gilt yields and PWLB rates to rise, due to the high volume of gilt issuance in the UK, and of bond issuance in other major western countries. Increasing investor confidence in eventual world economic recovery is also likely to compound this effect as recovery will encourage investors to switch from bonds to equities.

c. There has been exceptionally high volatility in gilt yields and PWLB rates during January and February 2015. It is likely that this trend will continue through 2015 and that there could be swings of 0.50% during even one quarter.

d. The overall balance of risks to economic recovery in the UK is currently evenly balanced. Only time will tell just how long this current period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.

e. Their interest rate forecasts are based on an initial assumption that there will not be a major resurgence of the Eurozone debt crisis. There is an increased risk that Greece could end up leaving the Euro but if this happens, the Eurozone now has sufficient fire walls in place that a Greek exit would have little immediate direct impact on the rest of the Eurozone and the Euro. It is therefore expected that there will be an overall managed, albeit painful and tortuous, resolution of any Eurozone debt crisis that may occur where Eurozone institutions and governments eventually do what is necessary - but only when all else has been tried and failed. Under this assumed scenario, growth within the Eurozone will be weak at best for the next couple of years with some Eurozone countries experiencing low or negative growth, which will, over that time period, see an increase in total government debt to GDP ratios. There is a significant danger that these ratios could rise to the point where markets lose confidence in the financial viability of one, or more, countries, especially if growth disappoints and / or efforts to reduce government deficits fail to deliver the necessary reductions. However, it is impossible to forecast whether any individual country will lose such confidence, or when, and so precipitate a sharp resurgence of the Eurozone debt crisis. While the ECB has adequate resources to manage a debt crisis in a small Eurozone country, if one, or more, of the larger countries were to experience a major crisis of market confidence, this would present a serious challenge to the ECB and to Eurozone politicians.

f. Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:
   - Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.
   - UK strong economic growth is weaker than they currently anticipate.
   - Weak growth or recession in the UK's main trading partners - the EU, US and China.
   - A resurgence of the Eurozone sovereign debt crisis.
   - Recapitalisation of European banks requiring more government financial support.
   - Monetary policy action failing to stimulate sustainable growth and to combat the threat of deflation in western economies, especially the Eurozone and Japan.

g. The potential for upside risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -
   - An adverse reaction by financial markets to the result of the UK general election in May 2015 and the EU, economic and debt management policies adopted by the new government.
   - The ECB severely disappointing financial markets with a programme of asset purchases which proves insufficient to significantly stimulate growth in the Eurozone.
   - The commencement by the US Federal Reserve of increases in the Fed Rate in 2015, 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. There could also be a sharp fundamental reassessment of investments in the debt and equities of emerging countries which have chased higher yields during a prolonged period when yields and returns in western countries have been heavily suppressed; countries such as Brazil and Russia are already in recession and facing major economic and political challenges.
   - UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

**Appendix 2**

## PERMITTED INVESTMENTS

The Council approves the following forms of investment instrument for use as Permitted Investments:

| | Minimum Credit Criteria | Liquidity Risk | Market Risk | Max % of Total Investments | Max. Maturity Period |
|---|---|---|---|---|---|
| **Deposits** | | | | | |
| Debt Management Agency Deposit Facility (DMADF) | --- | Term | No | Unlimited | 6 Months |
| Term Deposits – Local Authorities | --- | Term | No | 80% | 2 Years |
| Call Accounts – Banks and Building Societies | Capita Colour Category GREEN | Instant | No | Unlimited | Call Facility |
| Notice Accounts – Banks and Building Societies | Capita Colour Category GREEN | Notice Period | No | 50% | 6 Months |
| Term Deposits – Banks and Building Societies | Capita Colour Category GREEN | Term | No | 95% | 2 Years |
| **Deposits With Counterparties Currently In Receipt of Government Support / Ownership** | | | | | |
| Call Accounts – UK Nationalised/ Part-Nationalised Banks | Capita Colour Category BLUE | Instant | No | Unlimited | Call Facility |
| Notice Accounts – UK Nationalised/ Part-Nationalised Banks | Capita Colour Category BLUE | Notice Period | No | 50% | 6 Months |
| Term Deposits – UK Nationalised/ Part-Nationalised Banks | Capita Colour Category BLUE | Term | No | 95% | 2 Years |
| **Securities** | | | | | |
| Certificates of Deposit – Banks and Building Societies | Capita Colour Category GREEN | See Note 1 Below | See Note 1 Below | 80% | 2 Years |
| **Collective Investment Schemes structured as Open Ended Investment Companies (OEICs)** | | | | | |
| Money Market Funds | AAAmmf with Fitch or equivalent with Moody's/Standard & Poors | See Note 2 Below | See Note 2 Below | 50% | Call Facility |

Notes:

1. The Liquidity Risk on a Certificate of Deposit is for the Term of the Deposit (if the Certificate is held to maturity) or the Next Banking Day (if sold prior to maturity). There is no Market Risk if the Certificate is held to maturity, only if the Certificate is sold prior to maturity (with an implied assumption that markets will not freeze up and so there will be a ready buyer).
2. The objective of Money Market Funds is to maintain the value of assets but such Funds hold assets that can vary in value. The credit ratings agencies, however, require the unit values to vary by almost zero.

Investments will only be made with banks/building societies that do not have a credit rating in their own right where the Council's treasury advisers have confirmed that any obligations of that bank/building society are guaranteed by another bank/building society with suitable ratings.

The Council will only use approved counterparties from the UK or from countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide). Countries currently meeting this criterion include Australia, Canada, France, Germany, Sweden, the USA, and the UK.

**Non-Treasury Investments**
In addition to the table of treasury investments above, the definition of "investments" under the Investment Regulations includes the following items:
"(a) All share holding, unit holding and bond holding, including those in a local authority owned company, is an investment.
(b) Loans to a local authority company or other entity formed by a local authority to deliver services, is an investment.
(c) Loans made to third parties are investments.
(d) Loans made by a local authority to another authority or harbour authority using powers contained in Schedule 3, paragraph 10 or 11 of the Local Government (Scotland) Act 1975 are not investments.
(e) Investment property is an investment."

The Council approves items in categories (a), (b), (c), and (e) above as Permitted Investments as set-out below:

| | Minimum Credit Criteria | Liquidity Risk | Market Risk | Max % of Total Investments | Max. Maturity Period |
|---|---|---|---|---|---|
| **Non-Treasury Investments** | | | | | |
| (a) Share holding, unit holding and bond holding, including those in a local authority owned company | Assessment would be made of company in which any holding was to be made | Period of holding | Yes | 10% | Unlimited |
| (b) Loans to a local authority company or other entity formed by a local authority to deliver services | Assessment would be made of company or entity to which any loan was to be made | Period of loan | No | 20% | Unlimited |
| (c) Loans made to third parties | Assessment would be made of third party to which any loan was to be made | Period of loan | No | 25% | Unlimited |
| (e) Investment property | Assessment would be made of property to be held as investment property | Period of holding | Yes | 10% | Unlimited |

In relation to the above, Members should note that the Council is unlikely to become involved with category (a), has a loan under category (b) (for the BPRA), will have loans to third parties (category (c)) arising from decisions on such loans made by the Council, and may have investment property (category (e)) should there be a reclassification, due to accounting rules, of individual properties held by the Council.

**Permitted Investments – Common Good**
The Common Good Fund's permitted investments are approved as follows:

| | Minimum Credit Criteria | Liquidity Risk | Market Risk | Max % of Total Investments | Max. Maturity Period |
|---|---|---|---|---|---|
| Funds deposited with Inverclyde Council | --- | Instant | No | Unlimited | Unlimited |
| Share holding, unit holding and bond holding, including those in a local authority owned company | Assessment would be made of company in which any holding was to be made | Period of holding | Yes | 10% | Unlimited |
| Investment property | Assessment would be made of property to be held as investment property | Period of holding | Yes | 95% | Unlimited |

**Treasury Risks Arising From Permitted Instruments**
All of the investment instruments in the above tables are subject to the following risks:

1. **Credit and counter-party risk**
   This is the risk of failure by a counterparty (bank or building society) to meet its contractual obligations to the Council particularly as a result of the counterparty's diminished creditworthiness, and the resulting detrimental effect on the Council's capital or current (revenue) resources. There are no counterparties where this risk is zero although AAA-rated organisations have a very high level of creditworthiness.

2. **Liquidity risk**
   This is the risk that cash will not be available when it is needed. While it could be said that all counterparties are subject to at least a very small level of liquidity risk as credit risk can never be zero, in this document liquidity risk has been treated as whether or not instant access to cash can be obtained from each form of investment instrument. The column in the above tables headed as 'market risk' will show each investment instrument as being instant access, notice period i.e. money is available after the notice period (although it may also be available without notice but with a loss of interest), or term i.e. money is locked in until an agreed maturity date.

3. **Market risk**
   This is the risk that, through adverse market fluctuations in the value of the principal sums that the Council borrows and invests, its stated treasury management policies and objectives are compromised, against which effects it has failed to protect itself adequately. However, some cash rich local authorities may positively want exposure to market risk e.g. those investing in investment instruments with a view to obtaining a long term increase in value.

4. **Interest rate risk**
   This is the risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the Council's finances, against which the Council has failed to protect itself adequately. This authority has set limits for its fixed and variable rate exposure in its Treasury Management Indicators in this report.

5. **Legal and regulatory risk**
   This is the risk that the Council, or an organisation with which it is dealing in its treasury management activities, fails to act in accordance with its legal powers or regulatory requirements, and that the Council suffers losses accordingly.

The risk exposure of various types of investment instrument can be summarised as:

- low risk = low rate of return
- higher risk = higher rate of return.

For liquidity, the position can be summarised as:

- high liquidity = low return
- low liquidity = higher returns.

**Controls on Treasury Risks**

1. **Credit and counter-party risk**
   This Council has set minimum credit criteria to determine which counterparties and countries are of sufficiently high creditworthiness to be considered for investment purposes.

2. **Liquidity risk**
   This Council undertakes cash flow forecasting to enable it to determine how long investments can be made for and how much can be invested.

3. **Market risk**
   The only instruments that the Council may purchase which can have market risk are Certificates of Deposit. Although they have a market value that fluctuates, the market risk does not arise if the Certificates are retained until maturity - only if they were traded prior to maturity if the need arose.

4. **Interest rate risk**
   This Council manages this risk by having a view of the future course of interest rates and then formulating a treasury management strategy accordingly which aims to maximise investment earnings consistent with control of risk or alternatively, seeks to minimise expenditure on interest costs on borrowing.

5. **Legal and regulatory risk**
   This Council will not undertake any form of investing until it has ensured that it has all necessary powers and also complied with all regulations.

**Unlimited Investments**
Investment Regulation 24 states that an investment can be shown in the above tables as being 'unlimited' in terms of the maximum amount or percentage of the total portfolio that can be put into that type of investment. However, it also requires that an explanation must be given for using that category.

The authority has given the following types of investment an unlimited category:

1. Debt Management Agency Deposit Facility (DMADF)
   This is considered to be the lowest risk form of investment available to local authorities as it is operated by the Debt Management Office which is part of H.M. Treasury i.e. the UK Government's high credit rating stands behind the DMADF. It is also a deposit account and avoids the complications of buying and holding Government issued treasury bills or gilts.

2. High Credit Worthiness Banks and Building Societies
   See paragraphs 5.31 to 5.36 for an explanation of this authority's definition of high credit worthiness. While an unlimited amount of the investment portfolio may be put into banks and building societies with high credit worthiness, the authority will seek to ensure diversification of its portfolio with the following limits:
   - Limit for any single institution (except Council's bankers): £15m
   - Limit for Council's bankers (Bank of Scotland): £50m (or as approved by the Council or Committee)
   - Limit for any one group of counterparties: £30m (£50m or as approved by the Council or Committee for the group including the Council's bankers).

3. Funds Deposited with Inverclyde Council (for Common Good funds)
   This has been included so that, under the Permitted Investments, all funds belonging to the Common Good can be deposited with Inverclyde Council (and receive interest from the Council) rather than requiring the Common Good funds to be invested under separate Treasury Management arrangements.

**Objectives of Each Type of Investment Instrument**
Investment Regulation 25 requires an explanation of the objectives of every type of investment instrument which an authority approves as being 'permitted':

1. Deposits
   The following forms of 'investments' are actually more accurately called deposits as cash is deposited in an account until an agreed maturity date, or until the end of an agreed notice period, or is held at call.

   a) Debt Management Agency Deposit Facility (DMADF)
      This offers the lowest risk form of investment available to local authorities as it is effectively an investment placed with the Government. It is also easy to use as it is a deposit account and avoids the complications of buying and holding Government issued treasury bills or gilts. As it is low risk it also earns low rates of interest. It is, however, very useful for authorities whose overriding priority is the avoidance of risk. The longest term deposit that can be made with the DMADF is 6 months.

b) Term deposits with high credit worthiness banks and building societies
See paragraphs 5.31 to 5.36 for an explanation of this authority's definition of high credit worthiness. This is the most widely used form of investing used by local authorities. It offers a much higher rate of return than the DMADF (dependent on term). The Council will seek to ensure diversification of its portfolio of deposits as practicable and as explained above. In addition, longer term deposits offer an opportunity to increase investment returns by locking in high rates ahead of an expected fall in the level of interest rates. At other times, longer term rates can offer good value when the markets incorrectly assess the speed and timing of interest rate increases. This form of investing therefore, offers a lot of flexibility and higher earnings than the DMADF. Where it is restricted is that once a longer term investment is made, that cash is locked in until the maturity date.

c) Notice accounts with high credit worthiness banks and building societies
The objectives are as for 1.b) above but there is access to cash after the agreed notice period (and sometimes access without giving notice but with loss of interest). This generally means accepting a lower rate of interest than that which could be earned from the same institution by making a term deposit.

d) Call accounts with high credit worthiness banks and building societies
The objectives are as for 1.b) above but there is instant access to recalling cash deposited. This generally means accepting a lower rate of interest than that which could be earned from the same institution by making a term deposit. Some use of call accounts is highly desirable to ensure that the authority has ready access to cash when needed to pay bills.

2. Deposits With Counterparties Currently In Receipt of Government Support/Ownership
These institutions offer another dimension of creditworthiness in terms of Government backing through either direct (partial or full) ownership or the banking support package. The view of this Council is that such backing makes these banks attractive institutions with whom to place deposits, and that will remain our view even if the UK sovereign rating were to be downgraded in the coming year.

a) Term deposits, notice accounts and call accounts with high credit worthiness banks which are fully or semi nationalised
As for 1.b), 1.c) and1.d) above but Government ownership implies that the Government stands behind this bank and will be deeply committed to providing whatever support that may be required to ensure the continuity of that bank. This Council considers that this indicates a low and acceptable level of residual risk.

3. Securities

a) Certificates of Deposit
These are shorter term securities issued by deposit taking institutions (mainly banks) so they can be sold if the need arises. However, that liquidity (and flexibility) comes at a price so the interest rate on a Certificate of Deposit is less than placing a Fixed Term Deposit with the same bank.

4. Collective Investment Schemes structured as Open Ended Investment Companies (OEICs)
   a) Money Market Funds (MMFs)
      By definition, MMFs are AAA rated and are widely diversified, using many forms of money market securities including types which this authority does not currently have the expertise or risk appetite to hold directly. However, due to the high level of expertise of the fund managers and the huge amounts of money invested in MMFs, and the fact that the weighted average maturity (WAM) cannot exceed 60 days, MMFs offer a combination of high security, instant access to funds, high diversification and good rates of return compared to equivalent instant access facilities. They are particularly advantageous in falling interest rate environments as their 60 day WAM means they have locked in investments earning higher rates of interest than are currently available in the market. MMFs also help an authority to diversify its own portfolio as e.g. a £2m investment placed directly with HSBC is a 100% risk exposure to HSBC whereas £2m invested in a MMF may end up with say £10,000 being invested with HSBC through the MMF. For authorities particularly concerned with risk exposure to banks, MMFs offer an effective way of minimising risk exposure while still getting much better rates of return than available through the DMADF. They also offer a constant Net Asset Value (NAV) i.e. the principal sum invested has high security.

5. Non-Treasury Investments
   b) Share holding, unit holding and bond holding, including those in a local authority owned company
      The objectives for the holding of shares, units, or bonds (including those in a local authority owned company) will vary depending on whether the Council wishes to undertake actual investments in the market or has the holding as a result of a previous decision relating to the management or provision of Council services. This Council will not undertake investments in the market in shares, units, or bonds but may, if required, hold shares, units, or bonds arising from any decisions taken by the Council in relation to the management or provision of Council services.

   c) Loans to a local authority company or other entity formed by a local authority to deliver services
      Having established a company or other entity to deliver services, a local authority may wish to provide loan funding to assist the company or entity. Any such loan funding would be provided only after consideration of the reasons for the loan, the repayment period for the loan, and the likelihood that the loan would be able to be repaid by the company or entity. Such loan funding would be provided from Council Revenue Reserves rather than from borrowing.

   d) Loans made to third parties
      Such loans could be provided for a variety of reasons such as economic development or to assist local voluntary groups. Any such loan funding would be provided only after consideration of the reasons for the loan, the repayment period for the loan, and the likelihood that the loan would be able to be repaid by the third party concerned. Such loan funding would be provided from Council Revenue Reserves rather than from borrowing.

   e) Investment property
      An investment in property would give the Council exposure to risks such as market risk (movements in property prices), maintenance costs, tenants not paying their rent, leasing issues, etc. This Council does not undertake investments involving property but may have investment property should there be a reclassification, due to accounting rules, of individual properties held by the Council.

## FORECASTS OF INVESTMENT BALANCES

Investment Regulation 31 requires the Council to provide forecasts for the level of investments for the next three years, in line with the time frame of our capital investment programme. These forecasts are as follows:

| INVESTMENT FORECASTS | 2015/16 | 2016/17 | 2017/18 |
|---|---|---|---|
| | Estimate | Estimate | Estimate |
| | £000 | £000 | £000 |
| **Cash balances managed in house** | | | |
| 1st April | 50,169 | 33,650 | 13,056 |
| 31st March | 33.650 | 13,056 | 7,052 |
| Change in year | (16,519) | (20,594) | (6,004) |
| Average daily cash balances | 41,910 | 23,353 | 10,054 |
| **Cash balances managed by cash fund managers** | | | |
| 1st April | 0 | 0 | 0 |
| 31st March | 0 | 0 | 0 |
| Change in year | 0 | 0 | 0 |
| Average daily cash balances | 0 | 0 | 0 |
| **TOTAL CASH BALANCES** | | | |
| 1st April | 50,169 | 33,650 | 13,056 |
| 31st March | 33,650 | 13,056 | 7,052 |
| Change in year | (16,519) | (20,594) | (6,004) |
| Average daily cash balances | 41,910 | 23,353 | 10,054 |
| **Holdings of shares, bonds, units (includes authority owned company)** | | | |
| 1st April | 2 | 2 | 2 |
| Purchases | 0 | 0 | 0 |
| Sales | 0 | 0 | 0 |
| 31st March | 2 | 2 | 2 |
| **Loans to local authority company or other entity to deliver services** | | | |
| 1st April | 0 | 590 | 555 |
| Advances | 600 | 0 | 0 |
| Repayments | 10 | 35 | 35 |
| 31st March | 590 | 555 | 520 |
| **Loans made to third parties** | | | |
| 1st April | 2,240 | 4,010 | 3,979 |
| Advances | 1,803 | 3 | 3 |
| Repayments | 33 | 34 | 34 |
| 31st March | 4,010 | 3,979 | 3,948 |
| **Investment properties** | | | |
| 1st April | 0 | 0 | 0 |
| Purchases | 0 | 0 | 0 |
| Sales | 0 | 0 | 0 |
| 31st March | 0 | 0 | 0 |

| INVESTMENT FORECASTS (Continued) | 2015/16 | 2016/17 | 2017/18 |
|---|---|---|---|
| | Estimate | Estimate | Estimate |
| | £'000 | £'000 | £'000 |
| **TOTAL OF ALL INVESTMENTS** | | | |
| 1st April | 52,411 | 38,252 | 17,592 |
| 31st March | 38,252 | 17,592 | 11,522 |
| Change in year | (14,159) | (20,660) | (6,070) |

The movements in the forecast investment balances shown above are due largely to ongoing treasury management activity in accordance with the Council's treasury management strategy or, for loans made to third parties, in accordance with Council decisions made in respect of such loans.

The "holdings of shares, bonds, units (includes authority owned company)" are for Common Good whilst the Investment properties includes Council property and Common Good property.

**TREASURY MANAGEMENT**
**GLOSSARY OF TERMS**

Affordable Capital Expenditure Limit
The amount that the Council can afford to allocate to capital expenditure in accordance with the requirements of the Local Government in Scotland Act 2003 and supporting regulations.

Authorised Limit for External Debt
This is a limit for total Council external debt as set by the Council based on debt levels and plans.

Bail In
The use of funds held by a bank or other financial institution (whether in the form of customer bank deposits or bonds) to help prevent the collapse of a bank and in place of Governments stepping in with funds/support. The introduction of Bail In powers is part of the implementation of the Bank Recovery and Resolution Directive.

Bank of England
The central bank for the UK with ultimate responsibility for setting interest rates (which it does through the Monetary Policy Committee or "MPC").

Bank Rate
The interest rate for the UK as set each month by the Monetary Policy Committee ("MPC") of the Bank of England. This was previously referred to as the "Base Rate".

Bank Recovery and Resolution Directive (BRRD)
The Bank Recovery and Resolution Directive is a European legislative requirement which sets out a common approach within the EU to how countries will deal with any banks and financial institutions that get into financial difficulty. It includes the use of Bail In powers and was implemented in the UK, Germany and Austria on 1st January 2015 with other EU countries due to implement the BRRD in 2016.

Basel III
The latest global standards relating to banks and financial institutions including the level of their capital (funds retained by banks to meet possible future losses).

Call Date
A date on which a lender for a LOBO loan can seek to apply an amended interest rate to the loan. The term "call date" is also used in relation to some types of investments with a maturity date where the investments can be redeemed on call dates prior to the maturity date.

Capita
Capita Treasury Solutions Limited who are the Council's treasury management advisers who were previously named Sector Treasury Services Limited (and were normally referred to as Sector).

Capital Expenditure
Expenditure on or for the creation of fixed assets that meets the definition of Capital Expenditure under the accounting rules as set-out in the Code of Practice on Local Authority Accounting in the United Kingdom and for which the Council are able to borrow.

Capital Financing Requirement
The Capital Financing Requirement (sometimes referred to as the "CFR") is a Prudential Indicator that can be derived from the information in the Council's Balance Sheet. It generally represents the underlying need to borrow for capital expenditure (including PPP schemes).

Capital Requirements Directives
These are European legislative requirements regarding capital, funding and other financial requirements for banks, building societies and investment firms.

CDS Spread
A CDS Spread or “Credit Default Swap” Spread is the cost of insuring against default by a Counterparty. Increases in the CDS Spread for a Counterparty may indicate concerns within the market regarding a Counterparty.

Certificates of Deposit
Certificates of Deposit (or CDs) are a form of investment and similar to Fixed Term Deposits in that the investment is with a named Bank or Financial Institution, matures on a set date, and is repaid with interest on the maturity date. Unlike a Fixed Term Deposit, a CD can also be traded in the market prior to maturity.

CIPFA
CIPFA is the Chartered Institute of Public Finance and Accountancy who produce guidance, codes of practice, and policy documents for Councils.

Consumer Prices Index
The Consumer Prices Index (“CPI”) is a means of measuring inflation (as is the Retail Prices Index or “RPI”). The Monetary Policy Committee of the Bank of England set the Bank Rate in order to try to keep CPI at or close to the target set by the Government (currently the target is 2%). The calculation of the CPI includes many items of normal household expenditure but the calculation excludes some items such as mortgage interest payments and Council Tax.

Counterparty
Another organisation involved in a deal i.e. if the Council enters a deal with a bank then the bank would be referred to as the “Counterparty”.

Credit Ratings
Credit ratings are indicators produced by a ratings provider (such as Fitch, Moody's or Standard & Poor's) that aim to give an opinion on the relative ability of a financial institution to meet its financial commitments. Credit ratings are not guarantees – they are opinions based on investigations and assessments by the ratings providers and they are regularly reviewed and updated. The Council makes use of credit ratings to determine which counterparties are appropriate or suitable for the Council to make deposits with.

The highest credit rating is AAA.

European Banking Authority
The European Banking Authority (EBA) is an independent EU Authority which works to ensure effective and consistent prudential regulation and supervision across the European banking sector.

European Central Bank
Sometimes referred to as “the ECB”, the European Central Bank is the central bank for the Eurozone and is the equivalent of the Bank of England. The European Central Bank sets interest rates for the Eurozone.

Eurozone
This is the name given to the countries in Europe that have the Euro as their currency. Interest rates in the Eurozone are set by the European Central Bank. The Eurozone is comprised of the following 19 countries: Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia, and Spain.

Fed Rate
This is the interest rate for the US. Rates for the US are set by the Federal Reserve (the central bank for the US and the equivalent of the Bank of England).

Federal Reserve
Sometimes referred to as “the Fed”, the Federal Reserve is the central bank for the US and is the equivalent of the Bank of England. The Federal Reserve sets interest rates for the US.

Fixed Rate Funding/Investments
This term refers to funding or investments where the interest rate that applies to payments or receipts of interest on the funding or investments is fixed and does not change.

Fixed Term Deposit
A Fixed Term Deposit or Fixed Term Investment is an investment with a named bank or financial institution which matures on a set date and which is repaid with interest on the maturity date. Fixed Term Deposits cannot be traded and cannot be terminated before the maturity date without the payment of a penalty (if at all).

Flat Yield Curve
A flat yield curve occurs where the yield for long-term investments is the same or similar to the yield for short-term investments – the period of the investment makes no or little difference to the yield on the investment.

G7/G8/G20
These are forums for discussions by the governments of large world economies.

The G7 is comprised of Canada, France, Germany, Italy, Japan, the UK, and the USA. The G8 is the G7 plus Russia (with the European Union also attending). The G20 is comprised of 19 countries (including the G7 and Russia) plus the European Union.

Gilt Yields
A gilt yield is the effective rate of return that someone buying a gilt at the current market price will receive on that gilt. Since the market price of a gilt can vary at any time, the yield will also vary.

Gilts
Gilts are bonds (i.e. debt certificates) that are issued (i.e. sold) by the UK Government. When they issue gilts the Government sets the interest rate that applies to the gilt, sets when they will repay the value of the gilt, and it agrees to make interest payments at regular intervals until the gilt is repaid or redeemed. Gilts are traded in the financial markets with the price varying depending on the interest rate applicable to the gilt, when the gilt will be repaid (i.e. when it will mature), on Bank Rate expectations, and on market conditions.

Gross Domestic Product
Gross Domestic Product ("GDP") is a measure of the output of goods and services from an economy.

Growth
Positive growth in an economy is an increase in the amount of goods and services produced by that economy over time. Negative growth in an economy is a reduction in the amount of goods and services produced by that economy over time.

IMF
The International Monetary Fund oversees the world financial system and seeks to stabilise international exchange rates, facilitate development, and provide resources to countries in balance of payments difficulties or to assist with poverty reduction.

Incremental Impact of Capital Investment Decisions
These are Prudential Indicators that reflect the impact on Council Tax of movements in projected and estimated capital expenditure within and between financial years.

Inflation
Inflation is the term used for an increase in prices over time. It can be measured in various ways including using the Consumer Prices Index ("CPI") or the Retail Prices Index ("RPI").

Inverted Yield Curve
An inverted or negative yield curve shows long-term investments having lower yields than short-term investments (an investor gets a better yield by investing for a shorter period).

Investment Regulations
The Local Government in Scotland Act 2003 allows the Scottish Ministers to introduce Regulations to extend and govern the rules under which Scottish Councils may invest funds. The Local Government Investments (Scotland) Regulations 2010 came into effect on 1st April 2010.

LIBID
This is the London Interbank Bid Rate – an interest rate that is used between banks when they wish to attract deposits from each other.

LIBOR
This is the London Interbank Offering Rate – an interest rate that is used as a base for setting interest rates for deals between banks.

LOBO
This is a form of loan that the Council has with some lenders. The term is short for the phrase “Lender Option/Borrower Option”.

Money Market Fund
A Money Market Fund (or MMF) is a highly regulated investment product into which funds can be invested. An MMF offers the highest possible credit rating (AAA) whilst offering instant access and the diversification of risk (due to the MMF’s balances being investing in selected and regulated types of investment product with a range of different and appropriately credit-rated counterparties).

MPC
The MPC or Monetary Policy Committee is a committee of the Bank of England that meets each month (in a meeting over 2 days) to set the Bank Rate for the UK.

Negative Yield Curve
A negative or inverted yield curve shows long-term investments having lower yields than short-term investments (an investor gets a better yield by investing for a shorter period).

Net Borrowing Requirement
This is the difference between the Council’s net external borrowing and its capital financing requirement. Under the Prudential Code the Council’s net external borrowing should not, except in the short term, exceed its capital financing requirement. The Net Borrowing Requirement should therefore normally be a negative figure.

Operational Boundary
This is a level of debt set by the Council at lower than the Authorised Limit and which Council debt levels should not normally exceed during normal operations.

Positive Yield Curve
A positive yield curve shows long-term investments having higher yields than short-term investments (an investor gets a higher rate yield for investing for longer).

PRA
The Prudential Regulation Authority which is responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms.

Prudential Code
Councils are required to comply with the CIPFA Prudential Code for Capital Finance in Local Authorities. These requirements include the production of Prudential Indicators. The Prudential Code was last revised in November 2011.

Prudential Indicators
Indicators set-out in the Prudential Code that will help Councils to meet requirements in relation to borrowing limits or which will help Councils demonstrate affordability and prudence with regard to their prudential capital expenditure.

Prudential Regulation Authority (PRA)
The PRA is responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms.

PWLB
The Public Works Loan Board is a government agency and part of the Debt Management Office. The PWLB provides loans to local authorities and other specified bodies.

PWLB Certainty Rates
In the Budget in March 2012, the Chancellor of the Exchequer announced that local authorities that provide information on their long-term borrowing and capital spending plans would be eligible for a 0.20% discount rate for new PWLB borrowing. The PWLB Certainty Rates came into effect on 1st November 2012.

PWLB Rates
These are the interest rates chargeable by the Public Works Loan Board for loans. The rates for fixed rate loans are determined by the day on which the loan is agreed. The rates to be charged by the PWLB for loans are set each day based on gilt yields at the start of business each day and then updated at least once during the day.

Quantitative Easing
This is the creation of money by a central bank (such as the Bank of England) in order to purchase assets from banks and companies and boost the supply of money in an economy.

Ratings
Ratings are indicators produced by a ratings provider (such as Fitch, Moody's or Standard & Poor's) that aim to give an indication of the financial or operational strength of entities including financial institutions and even countries. Ratings are not guarantees – they are opinions based on investigations and assessments by the ratings providers and they are regularly reviewed and updated. The Council makes use of credit ratings to determine which counterparties are appropriate or suitable for the Council to make deposits with.

Repo Rate
This is another name for the Bank Rate as set by the Monetary Policy Committee.

Retail Prices Index
The Retail Prices Index (“RPI”) is a means of measuring inflation (as is the Consumer Prices Index or “CPI”). The calculation of the RPI includes most of the same items as the CPI as well as some items not included in the CPI such as mortgage interest payments and Council Tax whilst excluding items that are in the CPI such as charges for financial services.

Ring Fencing
In banking terms, the proposal (currently expected by 2019) that those parts of a bank that undertake riskier activities (such as investment banking) be kept legally separate from those parts that undertake less risky/safer activities (such as the accepting of customer deposits).

Sector
Sector Treasury Services Limited is the former name of Capita Treasury Solutions Limited who are the Council’s treasury management advisers.

Stress Tests
Reviews of the assets and liabilities of banks and financial institutions carried out by regulators such as the European Banking Authority (EBA) and the Prudential Regulation Authority (PRA) in the UK to identify the impact of potential economic scenarios, assess the strength of those banks/financial institutions, and determine any action required by banks/financial institutions to strengthen their financial positions.

Treasury Management Code
This is the "Treasury Management in the Public Services: Code of Practice" and is a code of practice for Council treasury management activities. It is produced by CIPFA and was last revised in November 2011.

Treasury Management Indicators
These are Prudential Indicators specifically relating to Treasury Management issues.

Treasury Management Practices (TMPs)
This is a Council document that sets out Council policies and procedures for treasury management as required by the Treasury Management Code. The Council also agrees an annual treasury management strategy that is submitted to Committee in accordance with the Treasury Management Practices.

Variable Rate Funding/Investments
Funding or investments where the interest rate that applies to payments or receipts of interest on the funding or investments varies on an agreed basis.

Yield
The yield is the effective rate of return on an investment.

Yield Curve
A graph showing the yield on investments plotted against the maturity period for investments:

- A positive yield curve shows long-term investments having higher yields than short-term investments (an investor gets a higher rate yield for investing for longer).
- A negative or inverted yield curve shows long-term investments having lower yields than short-term investments (an investor gets a better yield by investing for a shorter period).
- A flat yield curve occurs where the yield for long-term investments is the same or similar to the yield for short-term investments – the period of the investment makes no or little difference to the yield on the investment.

Finance Services
Inverclyde Council
February 2015.