For General Release

REPORT TO:	**Cabinet 22 February 2016**
AGENDA ITEM NO:	**8.2**
SUBJECT:	**Treasury Management Strategy Statement, Minimum Revenue Provision Policy Statement & Annual Investment Strategy 2016/17**
LEAD OFFICER:	**Assistant Chief Executive (Corporate Resources and Section 151 Officer)**
CABINET MEMBER:	**Cllr Simon Hall , Cabinet Minister for Finance and Treasury**
WARDS:	**All**

CORPORATE PRIORITY/POLICY CONTEXT:

Improving corporate capacity ensures that the Council delivers effective services contributing to the achievement of the Council's visions and corporate priorities. An effective and efficient Treasury Management Strategy linked to a Minimum Revenue Provision Policy Statement and an Annual Investment Strategy ensures that the Council's capital and investment plans are affordable, prudent and sustainable.

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FINANCIAL IMPACT:

This report sets out the Council's Treasury Management objectives, which are to manage the Council's cash flows, borrowing and investments minimising the level of risk exposure; maximising investment yield returns; and ensuring that capital expenditure and financing plans are prudent, affordable and sustainable. The report details the activities that will be undertaken by the Council in 2016/17 and the capital borrowing needs of the Council for 2016/17:-

	£m	Total £m
1. In Year Borrowing Requirement (Gross)	203.800	
		203.800
2. Total Interest Payable on Debt		
- chargeable to Housing Revenue Account (HRA)	12.535	
- chargeable to General Fund (GF)	19.554	
		32.089

In addition the report details the investment activities and the estimated level of income earned. **Investment Income** net of interest apportioned to Non-General Fund accounts e.g. HRA and other cash balances:- (0.971)

(0.971)

KEY DECISION REFERENCE NO.:

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

1. RECOMMENDATIONS

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

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

1.1. The Treasury Management Strategy Statement 2016/17 as set out in paragraphs 3.1 to 3.3 of this report including the recommendations that:

1.1.1. The Council takes up the balance of its 2015/16's borrowing requirement and future years' borrowing requirements, as set out in paragraph 3.3.

1.1.2. That for the reasons detailed in paragraph 3.7, opportunities for debt rescheduling are reviewed throughout the year by the Assistant Chief Executive (Corporate Resources and Section 151 Officer) and that, he be given delegated authority, in conjunction with the Council's independent treasury advisers, to undertake such rescheduling only if revenue savings or additional cost avoidance can be achieved at minimal risk in line with organisational considerations and with regard to the Housing Revenue Account (HRA) as set out in the Council's Finance Strategy 2015-2019.

1.1.3. That delegated authority be given to the Assistant Chief Executive (Corporate Resources and Section 151 Officer) to make any necessary decisions to protect the Council's financial position in light of market changes or investment risk exposure.

1.2. The Annual Investment Strategy as set out in paragraph 3.5 and as detailed in **Appendix B** of this report.

1.3. That the Affordable Borrowing Limits (required by Section 3 of the Local Government Act 2003) as set out in paragraph 3.6 and as detailed in **Appendix C** be as follows:

2016/17	**2017/18**	**2018/19**
£1,132.6m	**£1,216.0m**	**£1,267.1m**

1.4. The Prudential Indicators as set out in paragraph 3.8 and in **Appendix D** of this report.

1.5. The Annual Minimum Revenue Provision Policy Statement (required by SI 2008/414) as set out in paragraph 3.9 and as detailed in **Appendix E** of this report.

1.6. The Council's authorised counterparty lending list as at 31st December 2015 as set out in **Appendix F** of this report and the rating criteria set for inclusion onto this list.

2. EXECUTIVE SUMMARY

2.1. The Council defines its treasury management activities as:

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

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

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

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

2.4. The Local Government Act 2003 requires the Council to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities 2011, to ensure that the Council's capital investment plans are affordable, prudent and sustainable. In particular, the Prudential Code requires the Council to set a number of Prudential Indicators for the next three financial years. This report, which incorporates these indicators, also details the expected treasury activities for the year 2016/17, set in the context of the longer term planning forecasts for the organisation. The implications of these key indicators function as the overriding control and guidance mechanism for the future capital programme and the revenue consequences that arise for the Council in future financial years.

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

3. DETAIL OF THE REPORT

These strategy policies and statements cover:-

- The Current Treasury Position;
- The Borrowing Strategy and Borrowing Requirement;
- Prospects for Interest Rates and the Economic Outlook;
- The Annual Investment Strategy;
- Treasury Limits (as specified by the Local Government Act 2003);
- Debt Rescheduling and Repayment;
- Prudential Indicators;
- The Minimum Revenue Provision Policy Statement.

3.1. The Current Treasury Position

The Council's Treasury Management Strategy Statement for 2016/17, which is set out in paragraphs 3.1 to 3.3, incorporates the current treasury position and the overall borrowing strategy that is being recommended.

The Council's treasury position as at 31st December 2015 comprised:

Table 1: Borrowing by the Council

		Principal £m	Average Rate %
Fixed Rate Funding	- PWLB[1]	574.926	3.95
	- Other [2]	0.315	3.50
	- LOBO [3]	79.500	3.91
	- Local Authorities[4]	42.500	1.50
	- Amber Green LEEF 2LLP[5]	3.575	1.80
	- European Investment Bank	25.745	2.292
Variable Rate Funding	- LOBO [3]	60.000	4.23
Internal Loans – Trust Funds		0.023	0.25
Total External Debt as 31/12/15		**786.584**	**3.70**
Additional			
GF borrowing requirement outstanding for 2015/16		103.270	
HRA borrowing requirement outstanding for 2015/16		5.217	
Estimated Debt as at 31/03/16 [6]		**895.071**	**3.70**

1. PWLB is the Public Works Loan Board, the branch of Government that is the principle lender to local authorities. Included within this amount is the £223.1m borrowed for the HRA self-financing settlement made on 28/3/12.
2. Other relates to 3 ½% Irredeemable Stock which was issued by this Authority in the past.
3. Lender's Option Borrower's Option (LOBOs) loans are commercial debts with options for the lender to vary the rate at pre-set intervals. If the option is exercised, then the Council can either accept the new rate or repay the loan with no penalty.
4. As an alternative to borrowing from the Government, several local authorities have come to the market offering loans at competitive rates.
5. Amber Green LEEF (London Energy Efficiency Fund) 2LLP acts as an intermediary for the advancement of funding from the European Investment Bank (EIB).
6. Note that this amount represents the maximum and the actual figure is likely to be lower as internal balances and maturing investments may be used for funding purposes.

Table 2: Temporary Investments

	Principal £m	Average Rate %
Temporary investments outstanding as at 31/12/15	**125.435**	**0.71**
Estimated temporary investments outstanding as at 31/03/16	**100.000**	**0.71**

3.2. The Borrowing Strategy

3.2.1. The cost of taking up borrowing is reflected in the budgets set for the year and is therefore affordable. There will be no Housing Revenue Account (HRA) supported borrowing allocations for 2016/17 or for future years. The HRA operates within a limit on the amount of borrowing that can be accessed; this limit is set by the government. As at 1 April 2015, the HRA had headroom against this limit for an additional £11.409m of further borrowing. All of this additional borrowing would be unsupported. Of this amount, **£5.217m** will be taken up in 2015/16 with the balance being borrowed in future years as set out in Table 3 below. The cost of additional debt has been factored into the Authority's Financial Strategy planning assumptions and forecasts. With the Bank of England continuing to keep the base rate at historically low levels the Authority will seek to access the best opportunities to secure financing for the Capital Strategy at an affordable cost. The capital programme recommends the borrowing amounts detailed in 3.3 should be taken over the future three financial years; this recognises the strategic nature of the Council's infrastructure requirements. This, in turn, is partly in response to the current economic climate, which has seen a reduction in the ability of the private sector to invest in the Borough and partly as a result of the financial position the Council finds itself in which allows it to make this change in the capital programme.

3.2.2. Cabinet has agreed to set up a Revolving Investment Fund (RIF) to support the delivery of the Council's Growth Promise. The RIF will be an internal fund within the Council where funding is provided to schemes that support the Growth promise and also deliver a financial return. The focus will initially be principally on the delivery of a programme of development and regeneration on Council land. These will be funded outside the capital programme and be based on the projects delivering a return and therefore there should be no negative impact on the revenue budget. In fact there may be some positive impact from income streams such as rent. A sum of £100m has been included within the Council's overall borrowing headroom in 2016/17 to allow for the capacity to borrow for this purpose.

3.2.3. The Council has also formed a wholly owned Development company which will also be focused on regeneration in the borough, primarily relating to providing homes. The Council, as the main founder of the company, will provide loan facilities to the company which will count as capital investment in the project. There will also be a provision made for making equity investments in the company in the future. The appropriate changes have been made to the schedule of permitted investments to allow for this to take place – see 3.5.5. The company will be operated commercially and over time it is intended to deliver a financial return to the Council.

3.2.4. The Council has been working with the Greater London Authority (GLA) and Department for Communities and Local Government (DCLG) on a Growth Zone for the Croydon Opportunity Area (COA). The proposal has received support from the government and the Council is in the final stages of getting sign off for the business plan from CLG. The concept of the Growth Zone is that the Council invests in priority infrastructure to help deliver sustainable economic growth in Croydon, including increased homes and jobs. The debt taken out by the Council will be repaid from future business rates uplift in the COA. The GLA element of business rates uplift is also ring-fenced for debt repayment alongside the Council's. An allowance has been made in the borrowing assumptions for the expected investment over the next 3 years based on the business case being approved.

3.3. Borrowing Requirement

Table 3: Borrowing Requirement

	2015/16 £m	2016/17 £m	2017/18 £m	2018/19 £m	Total
		Estimate	Estimate	Estimate	£m
1. GF Prudential borrowing – funded through council tax.	51.4	82.6	60.7	9.3	204.0
2. HRA additional borrowing – unsupported by any grant funding.	5.2	6.2	0.0	0.0	11.4
3. Revolving Investment Fund (RIF)	0.0	100.0	0.0	0.0	100.0
4. Growth Zone	0.0	15.0	30.0	50.0	95.0
In Year Borrowing Requirement (Gross)	**56.6**	**203.8**	**90.7**	**59.3**	**410.4**
5. Less In Year Minimum Revenue Provision (MRP) for debt repayment.	(5.5)	(6.2)	(7.3)	(8.2)	(27.2)
In Year Borrowing Requirement (Net)	**51.1**	**197.6**	**83.4**	**51.1**	**383.2**
6. Add previous years' outstanding borrowing requirement (not taken in that year)	83.1	0.0	0.0	0.0	83.1
7. Borrowing – to replace maturing debt	5.0	12.5	26.0	11.0	54.5
8. Less loans taken up in-year	(25.7)	0.0	0.0	0.0	(25.7)
In Year Borrowing Requirement outstanding	**113.5**	**210.1**	**109.4**	**62.1**	**495.1**

3.3.1. The gross in year borrowing requirement for 2016/17 has been estimated to be £203.8m. Of this, £82.6m relates to borrowing to fund the GF capital programme, £6.2m relates to borrowing for HRA projects, £100.0m is for RIF and £15.0m will be for the Growth Zone. The Council will continue to use cash balances where this can be done prudently to reduce the amount of borrowing that it undertakes.

3.3.2. The Council's budget report elsewhere on the Cabinet agenda provides details of the full Capital Programme requirements including RIF and the Growth Zone. In order to take advantage of any low long term interest rates, part of the following two years' borrowing requirement may also be taken in advance in 2016/17. Under CIPFA's Treasury Management Code of Practice 2011, local authorities are permitted to borrow in advance of their capital requirement where there is a clear business case for doing so and where this will only be for the current capital programme or to finance future debt maturities. The Assistant Chief Executive (Corporate Resources and Section 151 Officer) will be responsible for managing the borrowing requirement and for ensuring that borrowing decisions are taken as part of the Council's Capital Strategy.

3.3.3. The borrowing requirement takes account of two of the main objectives of the Prudential Code which are:

a. That capital expenditure plans are affordable; and
b. That all external borrowing and other long term liabilities are within prudent and sustainable limits.

3.3.4. The total interest payable on the Council's long term GF and HRA debt in 2016/17 is estimated to be £32.089m of which £12.535m relates to borrowing undertaken for HRA schemes and for the HRA self financing settlement and is charged to the HRA with the balance of £19.554m being charged to the General Fund (GF).

3.3.5. The alternatives available to finance the balance of 2016/17's borrowing requirement and future borrowing requirements are:

The Public Works Loan Board (PWLB)

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

The Money Markets

Loans obtained through the Money Markets are generally at rates higher than the PWLB because commercial debt providers factor in risk and the government does not need to as local authorities are treated effectively as government backed and so much less likely to default on any debt. In recent years a form of borrowing known as Lenders Option Borrowers Option (LOBO) loans have become a more popular option for local authorities. These loans are at a fixed rate of interest for an initial fixed period of time after which the lender has the option to vary the interest rate at pre-determined intervals. If the lender decides to exercise this option, then the borrower can decide whether to accept the new terms or to repay the loan with no penalties. Generally this form of borrowing is cheaper in the initial fixed period of the loan as interest rates are held lower in this period to attract borrowers. Advice will be sought from Capita Asset Services, the Council's independent treasury advisers before any new LOBO loans are taken up for future funding.

UK Local Authorities

As UK local authorities struggle to identify approved counterparties to invest with and with low rates of returns being achieved as a result of this risk-adverse approach, the market has recently become more active in local authority to local authority lending for periods in excess of one year. The interest rates quoted would always need to be below the PWLB's certainty rate to attract bids. Loans offered are up to the 5 year period as local authorities generally are reluctant to tie up funds any further than this period.

European Investment Bank (EIB) Funding

In September 2013, the Council was successful in bidding for £20m of funding for energy efficiency and carbon reduction schemes within its capital programme. The funding will be advanced from the EIB through Amber Green LEEF 2LLP in two tranches. The first tranche was for up to £6m to be drawn down before 31 December 2014 at a rate of 1.80% over 9 years. Of this tranche, £3.575m was taken on 31 December 2014. The second tranche is for up to £14m to be taken up between 1 August 2015 and 31 July 2016 at an agreed rate of 2.50%. The comparable PWLB maturity certainty rate at the time that the agreement was signed was 3.39%

A separate credit facility has been set up with the EIB to fund capital schemes within the Council's Education Capital Strategy. This facility will allow the Council to access up to £102m in loans from the EIB for these capital projects over the next few years. To date, a maturity loan of £25.745m has been taken on 1 December 2015 over 15 years at a rate of 2.292% - the comparable PWLB loan interest rate on the day was 3.14%. The Council is therefore expected to make substantial savings of interest on this and future loans taken from the EIB.

Local Authority Bonds

The increased divergence between PWLB and gilt rates coupled with inflexible market borrowing opportunities have created the conditions necessary to make the issue of local authority bonds, at a rate higher than the gilt rate but lower than the cost of PWLB borrowing, an attractive proposition. The Council has already undertaken extensive initial exploratory work on this subject and will continue to explore this option and to take advice from Capita Asset Services on all aspects of this type of funding.

Municipal Bond Agency

The UK Municipal Bond Agency has been established to provide an alternate source of financing for local authorities. Authorities will be required to agree to a joint and several guarantee and be subject to the Agency's credit checks. Currently 58 local authorities are shareholders of the Agency.

Temporary Borrowing

Temporary borrowing (up to 1 year) can be used as short-term finance in order to manage the capital cash flow requirement pending a more advantageous time to borrow long term.

Temporary Investments

The next financial year is expected to be a time of continuing historically low bank rates. Currently, long-term borrowing rates are higher than rates achievable on investments and this situation is likely to continue throughout 2016/17. Therefore, as an alternative to taking up new external loans, consideration will be given to the use of temporary investments, as they mature, to fund the borrowing requirement. Council Officers, in conjunction with Treasury advisers, will continually monitor both the prevailing interest rates and the market forecasts, adopting the most suitable strategies to likely movements.

3.3.6. Any borrowing undertaken will need to fit into the Council's existing debt maturity profile to ensure an even distribution of maturities in future years. A prudent target for debt maturing in any single year in line with best practice is considered to be a maximum of 15% of total outstanding debt. In terms of cost, the Council's overall external debt interest rate has remained consistently below the average of all London boroughs. This has been verified by CIPFA and the data is detailed below.

Average Interest Rate payable on long term external debt

	Financial Year ending 31 March								
	2007	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
	%	%	%	%	%	%	%	%	%
Croydon	4.64	4.77	4.60	4.42	4.32	4.36	4.06	3.97	3.84
London Boroughs (Average)	5.66	5.90	5.82	5.65	5.11	4.39	4.55	4.49	4.51

The above data is attached as a chart in **Appendix G**.

3.3.7. The Authority's long-term debt profile as at 31st December 2015 is set out in **Appendix A**. The level of additional debt proposed within this report positions the Authority comparable to other boroughs of a similar profile facing similar challenges. As set out by this report and illustrated by the Prudential Indicators shown in full in **Appendix D**, the proposed level of debt meets the affordability criteria.

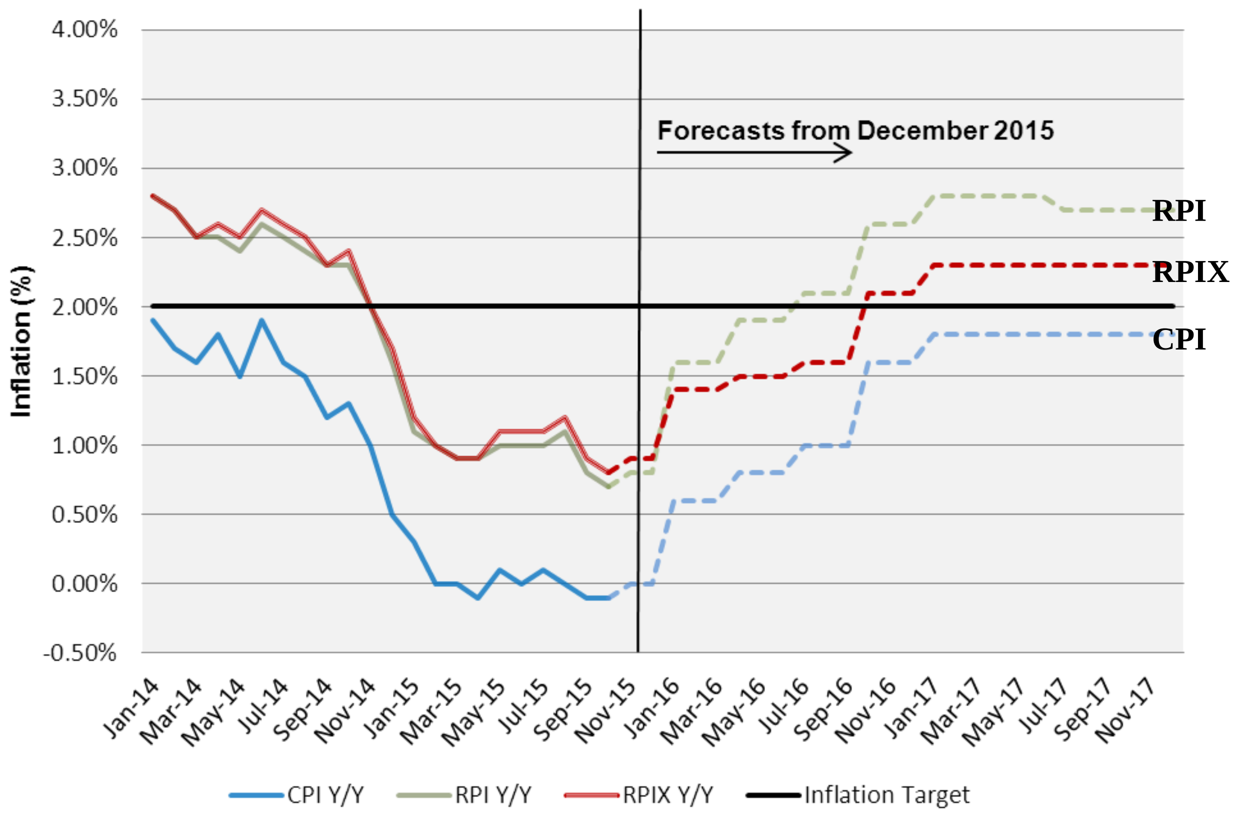
3.4. **Prospects for Interest Rates and the Economic Outlook**

3.4.1. To effectively manage the risks inherent in treasury management the team needs a clear understanding of the macro-economic factors that influence returns, the security of sums invested and the outlook for the markets. The Council has appointed Capita Asset Services as its external treasury management advisers. Part of the service provided by Capita is to advise the Council on economic matters and in formulating a view on interest rates as detailed below.

3.4.2. Inflation is an important factor that determines movements in interest rates in the UK. The Consumer Price Index (CPI), which is a key measure of inflation, hovered around the zero mark throughout the year 2015. It is forecast to increase to 1% in 2016 but not to get near the Government's target of 2% till 2017. The Bank of England's Monetary Policy Committee's (MPC) primary remit is to control inflation and this it achieves in the main by controlling interest rate movements. The MPC appears to show a consolidation of support for holding off on increasing the Bank Rate from 0.50% due to persistent low inflation. The MPC face the task of balancing the pros and cons of when to start on increasing Bank Rates, especially as many consumers are still heavily indebted and very vulnerable to increases in borrowing rates. The current Bank Rate of 0.50% has been in force since 5th March 2009 and is the lowest that it has been since the creation of the Bank of England. The UK's quantitative easing (asset purchase) target remains unchanged at £375bn.

Historical data together with forecasts on future UK inflation are detailed in **Chart 1** below.

Chart 1: UK Inflation Forecasts (Year on Year) January 2014 to December 2017



Notes to Chart 1:

- Retail Price Index (RPI) is a measure of inflation and represents the change in the prices of goods and services bought for the purpose of consumption in the UK.
- Underlying Rate of Inflation (RPIX) is the RPI excluding mortgage interest payments.
- Consumer Price Index (CPI) is a measure of the general level of price changes for consumer goods and services but excludes most owner/occupier housing costs such as council tax, dwelling insurance, rents, depreciation and the like. The Government has set a target for the twelve month increase in the CPI of 2% with a tolerance of ± 1% either way.

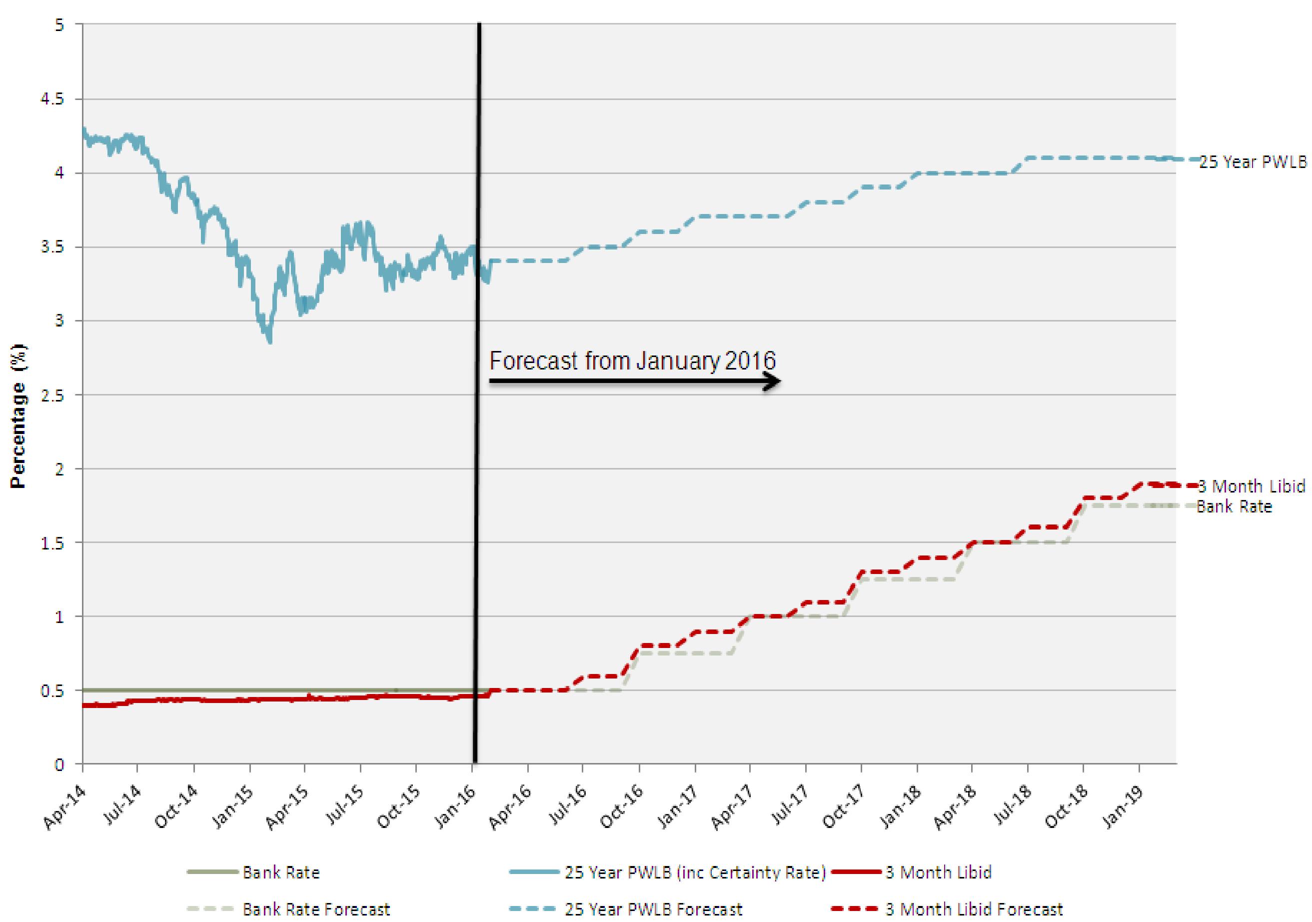
3.4.3. The market's view on interest rates for the UK as assessed by Capita Asset Services, the Council's independent treasury advisers is as follows:

	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Bank rate	0.50%	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.25%	1.50%	1.50%	1.75%	1.75%
5yr PWLB rate	2.00%	2.10%	2.20%	2.30%	2.40%	2.50%	2.60%	2.70%	2.80%	2.90%	3.00%	3.10%	3.20%
10yr PWLB rate	2.60%	2.70%	2.80%	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%	3.60%	3.60%	3.70%
25yr PWLB rate	3.40%	3.40%	3.50%	3.60%	3.70%	3.70%	3.80%	3.90%	4.00%	4.00%	4.10%	4.10%	4.10%
50yr PWLB rate	3.20%	3.20%	3.30%	3.40%	3.50%	3.60%	3.70%	3.80%	3.90%	3.90%	4.00%	4.00%	4.00%

a. On **shorter-term interest rates**, the general opinion is that the current bank rate of 0.50% is expected to increase to 0.75% by December 2016 and to remain at this level for the rest of the financial year.

b. On **longer-term interest rates**, the Public Works Loan Board (PWLB) rates for 25-year loans, currently at 3.29% are expected to increase to around 3.50% in the first half of 2016/17 and to be 3.70% at the end of 2016/17. The 50-year PWLB rate, which is currently at 3.11%, is expected to increase to 3.30% in the first half of 2016/17 and to be 3.50% by the end of the financial year. **Chart 2** below graphically illustrates Capita's view on interest rates.

Chart 2: UK Interest Rates April 2014 to January 2019



Notes to Chart 2:

- London Interbank Bid Rate (LIBID) is the average rate of interest at which a bank is willing to borrow from other banks in the wholesale money markets in London. The 3 Month LIBID rate reflects the interest rate that is bid by banks to borrow cash for 3 months

- Bank Rate is the official rate as set periodically by the Bank of England Monetary Policy Committee.

- Public Works Loan Board (PWLB) rate for 25 years is the interest rate at which local authorities can borrow from the PWLB over a term of 25 years

3.4.4. There remain huge uncertainties in economic forecasts for the 2016/17 financial year due to:

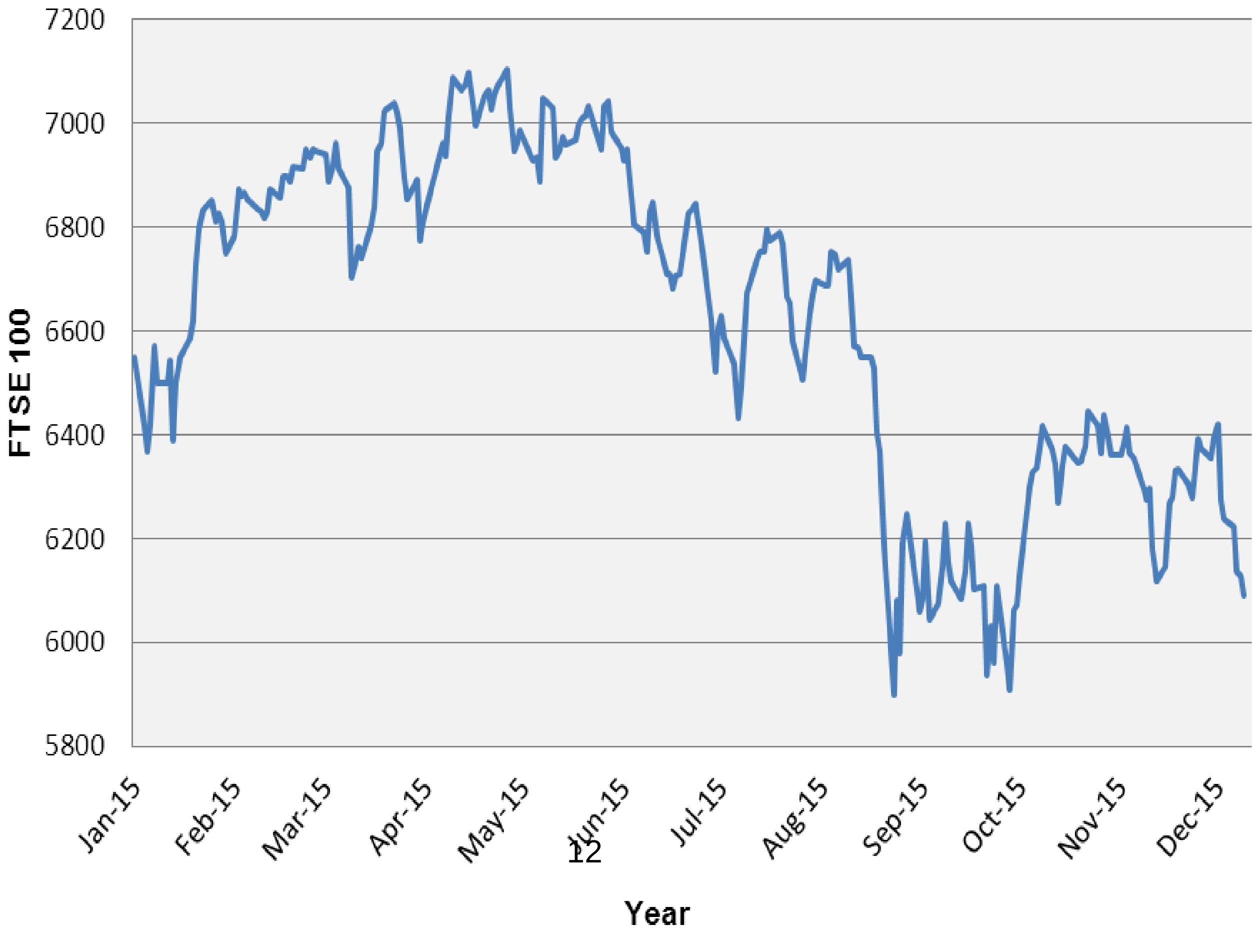
- The rise in geopolitical concerns principally in Eastern Europe, the Middle East and Asia.

- Uncertainty around the risk of a UK exit from the European Union following the referendum.
- The risk of deflation in the Eurozone and the potential for a significant increase in negative reaction to austerity measures in Eurozone countries, especially in those countries with high levels of unemployment.
- A resurgence of the Eurozone's sovereign debt crisis.
- Weak growth or recession in the UK's main trading partners – the EU, US and China.

3.4.5. At the start of 2015, the FTSE 100 opened over the 6,000 level and rose strongly in the first half of 2015, with market activity appearing strong and consumer confidence in stocks high. The index peaked at 7,103 on 27 April 2015 as markets reacted to a rise in banking and mining shares along with positive developments in Greece on that particular day. The FTSE 100 rallied on UK's General Election result of May 2015 which saw the Conservatives securing an overall majority. However, the index had a major setback in July and August as volatility in the Chinese stock market emerged. The crash of the Chinese stock market on 24 August 2015 triggered a £74bn sell off in the FTSE 100, as markets experienced the biggest fall in China's stock market in eight years. Towards the end of 2015, the strength of the pound combined with falling oil prices in the UK saw a further sell off in the FTSE 100 with oil and commodity companies suffering most as the price of Brent crude dipped below $40 a barrel. The index hit a low of 5,874 on 14 December 2015 which was the lowest level it has reached since December 2012. The US Federal Reserve Bank's decision of 16 December 2015 to raise their interest rate for the first time in nine years saw all the world's major indices, including the FTSE 100, reacting positively. The FTSE 100 closed at 6,242 at the end of December 2015.

Chart 3 below tracks the FTSE 100 on a monthly basis over the course of 2015.

Chart 3: FTSE100 January 2015 to December 2015



3.5. **Annual Investment Strategy**

3.5.1. When deciding on its investment strategy, the Council will have regard to the Department for Communities and Local Government's (the DCLG) Guidance on Local Government Investments issued in March 2004 and CIPFA's updated Treasury Management in Public Services Code of Practice and Cross-Sectoral Guidance Notes 2011 in formulating the Council's investment strategy for 2016/17. This will broadly follow the same lines adopted for 2015/16 as detailed in the paragraphs below and in **Appendix B**.

3.5.2. All investments will be in sterling. The overriding policy objective for the Council is the prudent investment of its treasury balances. The Council's investment priorities are:

a. The security of capital; and
b. The liquidity of its investments.

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

3.5.4. The Council will not engage in the borrowing of monies purely to invest or to lend in order to make a return as this is unlawful.

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

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

- Debt Management Agency Deposits Facility (DMADF).
- Term deposits with UK Government or with UK local authorities.
- Term deposits with credit - rated deposit takers (banks and building societies).
- Certificate of Deposits.
- AAA rated Money Market Funds.
- Bonds issued by multinational development banks.
- Enhanced AAA rated Money Market Funds.
- UK Government Gilts.
- UK Government Treasury Bills.

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

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

- Investment grade Corporate Bonds issued by Corporate Institutions.
- AAA rated Covered Bonds.
- Investment in the equity of any company wholly owned by Croydon Council.

3.5.6. Investment Income Gross - Based on cash flow forecasts for 2016/17, the Council anticipates its average cash balances for the year to be £180.0m, which includes the £210.1m of new borrowing to be undertaken in 2016/17. The overall balances include schools balances and HRA revenue balances for which an apportionment of investment interest earned is made. The net income then due to the General Fund is estimated at £0.971m for 2016/17.

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

3.5.8. The Assistant Chief Executive (Corporate Resources & Section 151 Officer) will be responsible for managing all investments within the limits as set out in **Appendix F** and in accordance with CIPFA's Treasury Management in the Public Services Code of Practice 2011 Edition.

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

3.5.10. The principle of ensuring capital security and then of securing the best rate of return underpins all treasury investment decisions. There is a growing concern, triggered by a succession of high profile banking scandals, that the reducing pool of quality counter-parties, such as banks, is increasing the level of risk for the Authority. These risks are not simply the risk that principal sums invested might be lost but also reputational risks to the Authority. In response, the Council's Treasury team has investigated other high-grade deposit takers, to increase diversification of investments and thereby reduce the overall concentration of risk of default. As a consequence of this, the Council has put into place a Custodian agreement offered at a discount by the Bank of New York Mellon – the Custodian used by the Council's Pension Fund. This has enabled the Treasury team to diversify investments and to enhance yields by investing in those specified and unspecified investments that require custody arrangements. A list of the Specified and Non-Specified investments that Council Officers are permitted to undertake in-house is detailed in

Appendix B. In the immediate short-term there will be no increase in returns, but the Treasury team will be better placed to exploit market opportunities in the longer term.

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

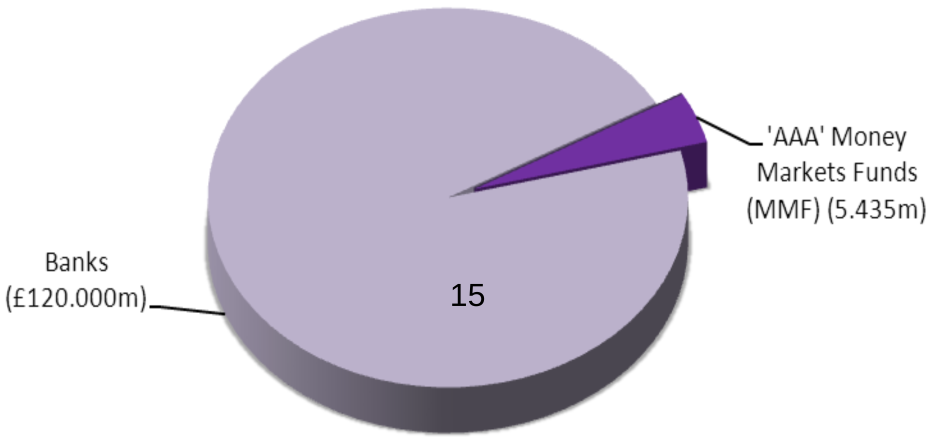
3.5.12. With regard to UK Challenger banks, the majority of local authorities do not include these banks in their counterparty lists. Although at present, Challenger banks do not have credit ratings and so fall outside investment strategy criteria, it is expected that these banks may get rated in the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

3.5.13. In 2014/15, the Council had invested £20m in the Real Lettings Property Fund Limited Partnership. The property fund, which has a 7-year life, offers investors the opportunity to invest in a diversified portfolio of London residential property and aims to deliver a minimum return of 5% per annum based on the letting of the properties on 5-year lease terms. For Croydon, this investment will also provide added benefit in that the properties purchased would offer affordable accommodation for former homeless people or those at risk of homelessness, who cannot access social housing. An additional £10m was advanced to the Fund on 9 September 2015. Returns generated by the investment will serve to boost the Council's overall income in the future.

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

3.5.15. In addition, the Council will continue to lend to other UK local authorities and to the Debt Management Office, which effectively is lending to the Government. The Council's investments outstanding as at 31st December 2015 are detailed graphically as follows:

Temporary Investments as at 31st December 2015 (£125.435m)



3.5.16. As at 31st December 2015, short-term investment interest rates (1-3 months) were between 0.40% and 0.60% with longer term rates (up to 1 year) between 0.54% and 1.0%. Investments will be made to take advantage of higher yields and to hedge against future decreases in bank rates. Daily liquidity requirements will be met by investing in the AAA rated MMFs. As investment rates are influenced throughout the year by the release of key items of data, there may be occasions when some investments will be pitched towards specific periods to take advantage of any unexpected higher rates resulting from data issued. In all cases investment decisions will adhere to Capita Asset Services' recommended maximum investment durations for the counterparty concerned.

3.6. Treasury Limits

3.6.1. Section 3 of the Local Government Act 2003 requires the Council to set limits and to keep under review how much it can afford to borrow. The amounts so determined are to be set on a rolling basis, for the forthcoming financial year and two successive financial years, a period of three years in total from 2016/17 to 2018/19 and are termed:

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

2. The **'Affordable Borrowing Limit'**. This limit represents an assessment of the maximum debt the authority may need to incur at any point throughout the year as determined in the Financial Strategy by the Assistant Chief Executive (Corporate Resources and Section 151 Officer).

3.6.2. The Assistant Chief Executive (Corporate Resources and Section 151 Officer) will be responsible for setting the Council's Affordable Borrowing Limit. This limit requires the Council to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon future council tax and housing rent levels is acceptable.

3.6.3. The Council's affordable borrowing limit has been estimated to be **£1,132.6m** for **2016/17**, **£1,216.0m** in **2017/18** and **£1,267.1m** in **2018/19** as detailed in **Appendix C**. These limits reflect the maximum amount the Council can borrow for capital and revenue purposes and allows for unexpected events for example a possible delay in the receipt of anticipated council tax, National Non-Domestic Rates (NNDR) direct debits, housing benefit subsidy or other government grant that had been notified to Council Officers in advance. The sum of £40m has been included in respect of revenue borrowing to cover the possibility of this shortfall. The limit reflects a level of borrowing which while not desirable is affordable in the short term to fund the cash flow requirements of the organisation and to address any potential risks that may arise.

3.7. Debt Repayment and Rescheduling

3.7.1. The Public Works Loan Board will allow authorities to reschedule debt and award a discount or charge a premium as appropriate.

3.7.2. The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt, has meant that PWLB to PWLB debt restructuring is now much less attractive than it was before. In particular, consideration will 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 if replacement PWLB refinancing is taken.

3.7.3. Financially, the optimum time to repay debt is when discounts on early repayment have reached a maximum or premiums a minimum and this will depend on the prevailing long-term interest rates. Officers will monitor interest rates throughout the year to identify rescheduling opportunities.

3.7.4. This report proposes that the Assistant Chief Executive (Corporate Resources and Section 151 Officer) be given delegated authority to undertake necessary debt rescheduling following advice from the Council's independent treasury advisers and after taking into account the organisational considerations with regard to the HRA as set out in the Council's Finance Strategy 2015-2019.

3.8. **Prudential Indicators**

3.8.1. The Prudential Indicators for 2015/16 to 2018/19 are attached in **Appendix D** in accordance with the Prudential Code for Capital Finance in Local Authorities 2011 Edition.

3.8.2. The Assistant Chief Executive (Corporate Resources and Section 151 Officer) is responsible for setting up and monitoring the Prudential Indicators in accordance with the Council's Capital Strategy.

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

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

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

1. The capital investment indicators reflect the Authority's future plans to undertake capital works, and the extent to which these will be funded through borrowing. Hence for 2016/17, £176.185m of GF and HRA capital investment is planned, £88.867m of which is to be financed from borrowing. Further borrowing of £100.0m for RIF and £15.0m for the Growth Zone will be undertaken in 2016/17 resulting in a total level of debt of £1,092.666m that supports past investment in the infrastructure of the Borough (**see Appendix D**).

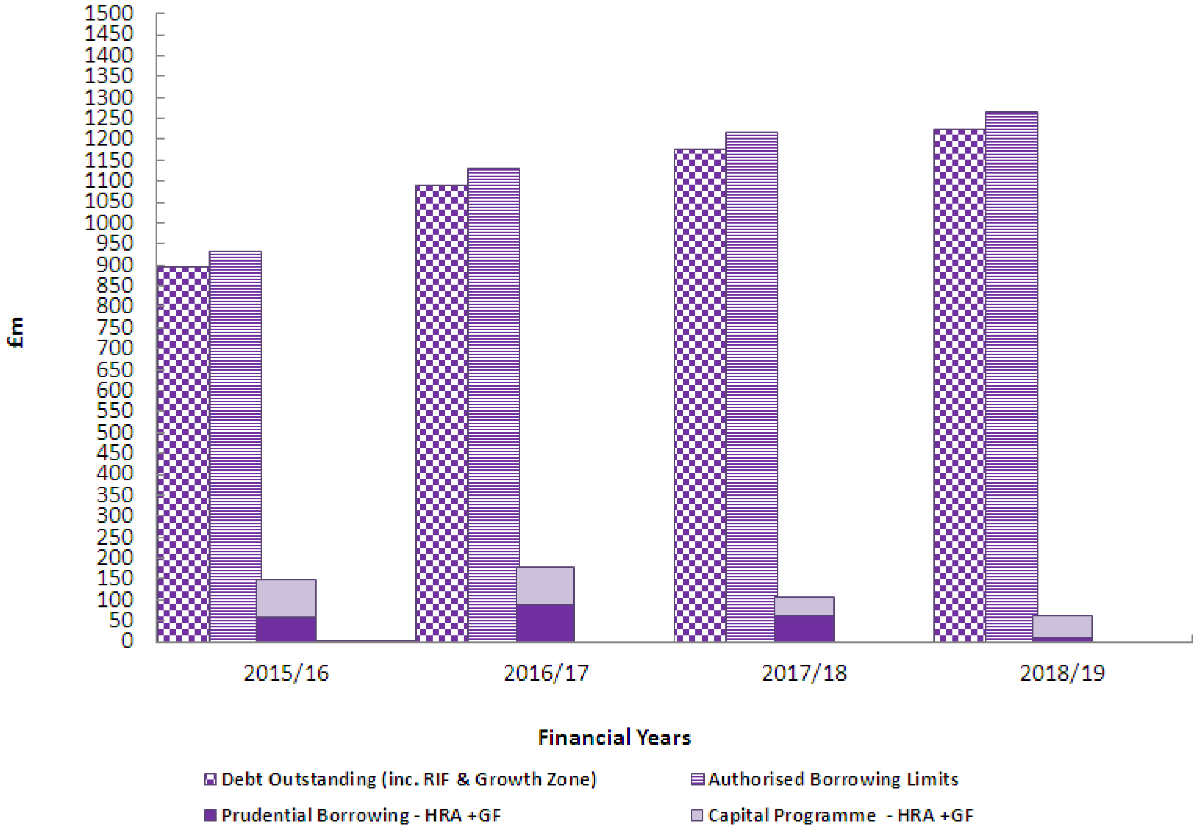
2. Apart from borrowing that is directly supported by government grant funding, the cost of new prudential borrowing to the Authority will be £14.00 per Band D council taxpayer in 2016/17. This Prudential Indicator reflects the impact of funding decisions relating to capital investment in Croydon. The Prudential Code specifically indicates that it is not appropriate to compare this indicator with other authorities.

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

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

These main indicators are featured below as follows:

Chart 4: Prudential Indicators for 2015/16 to 2018/19



3.9. Minimum Revenue Provision

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

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

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

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

3.9.3. Along with the above duty, the Government issued guidance in February 2008 which requires that a statement on the Council's policy for its annual MRP should be submitted to Full Council for approval before the start of the financial year to which the provision will relate.The Guidance offers four options under which MRP could be made although it makes clear that these options are by no means prescriptive. The options are:

Option 1: Regulatory Method.
MRP was set at a uniform rate of 4% on the General Fund's (GF) Capital Financing Requirement's (CFR) historic debt (incurred up to 31 March 2008) and for Government supported capital expenditure incurred since, adjusted for Adjustment 'A' – see Glossary of Terms at **Appendix H**.

Option 2: Capital Financing Requirement Method.
This is a variation on Option 1 and is based on 4% of the aggregate GF's CFR without any adjustment for 'Adjustment A'.

Option 3: Asset Life Method.
Under this option, for unsupported borrowing, MRP is spread over the estimated useful life of the asset created with two methods of calculating charges being available namely through the equal instalments method or on an annuity basis.

Option 4: Depreciation Method.
Under this option, MRP charges are linked to the useful life of each type of asset using the standard accounting rules for depreciation.

3.9.4 Given that the Guidance states that the four MRP options (as listed above in 3.9.3) are by no means prescriptive provided that an authority complies with the statutory duty to make prudent provision for the repayment of debt, there is freedom for authorities to consider an annual profiling of MRP that best fits the prudent management of their own financial circumstances.

3.9.5 The Assistant Chief Executive (Corporate Resources and Section 151 Office) is responsible for ensuring that accounting policies and the MRP policy complies with the statutory Guidance in determining a prudent level of MRP.

3.9.6 As part of the mid-year review of the 2015/16 Minimum Revenue Provision Statement, the Council's General Purposes and Audit Committee approved a revised Annual Minimum Revenue Provision Statement on 9 December 2015 (Minute A62/15). The Council's MRP Policy Statement for 2016/17 also adopts these revisions and is attached at **Appendix E.**

3.10 Conclusion

3.10.1 The Council's treasury advisers forecast that the bank rate, currently at 0.50%, will increase to 0.75% in December 2016 and to remain at this level for the rest of the financial year. The longer term (25 years) PWLB interest rates, which currently are 3.29%, are expected to increase to around 3.50% in the first half of 2016 and to be 3.70% at the end of 2016/17.

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

3.10.3 As indicated above, UK growth remains strong although continuing debt worries in the

Eurozone, who are the UK's biggest trading partner, may serve to dampen future economic growth. Another factor which could affect financial markets and the confidence of UK producers may be the result of the forthcoming UK referendum on whether to stay in the European Union, the outcome of which appears difficult to predict. Inflation, the Eurozone debt issues and the UK Government's plans to maintain the economic recovery momentum will continue to have a significant impact on the future direction of the Council's policies and finances. The Assistant Chief Executive (Corporate Resources and Section 151 Officer) will continue to monitor interest rates with the aim of taking advantage of any opportunities to borrow and invest after taking advice from the Council's independent treasury advisers in order to achieve the Council's long term Financial Strategy.

3.10.4 A glossary of terms associated with this report is attached in **Appendix H**.

4 **CONSULTATION**

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

5 FINANCIAL AND RISK ASSESSMENT CONSIDERATIONS

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

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

5.2 **The effect of the decision**

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

5.3 **Risks**

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

5.4 **Options**

These are fully dealt with in this report.

5.5 **Future savings/efficiencies**

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

Approved by: Richard Simpson, Assistant Chief Executive (Corporate Resources and Section 151 Officer).

6 **COMMENTS OF THE COUNCIL SOLICITOR AND MONITORING OFFICER**

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

Approved by: Gabriel MacGregor, Head of Corporate Law on behalf of the Council Solicitor and Monitoring Officer.

7 HUMAN RESOURCES IMPACT

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

Approved by: Michael Pichamuthu, HRBP, on behalf of Heather Daley, Director of HR.

8 EQUALITIES IMPACT

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

8.2 The Council's Capital and Revenue Budget 2016/17 is not subject to an equality impact assessment. However, in those areas where the setting of the capital and revenue budget result in new policies or policy change, then it is the responsibility of the relevant service department to carry out an equality impact assessment which evaluates how the new or changed policy will impact on disadvantaged sections of the community, including disabled people. The impact assessment includes consultation with disabled people and user-led disabled people organisations.

9 ENVIRONMENTAL IMPACT

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

10 CRIME AND DISORDER REDUCTION IMPACT

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

11 REASONS FOR RECOMMENDATIONS/PROPOSED DECISION

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

12 OPTIONS CONSIDERED AND REJECTED

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

CONTACT OFFICER: Derick Fernandes, Treasury Manager Ext 62526

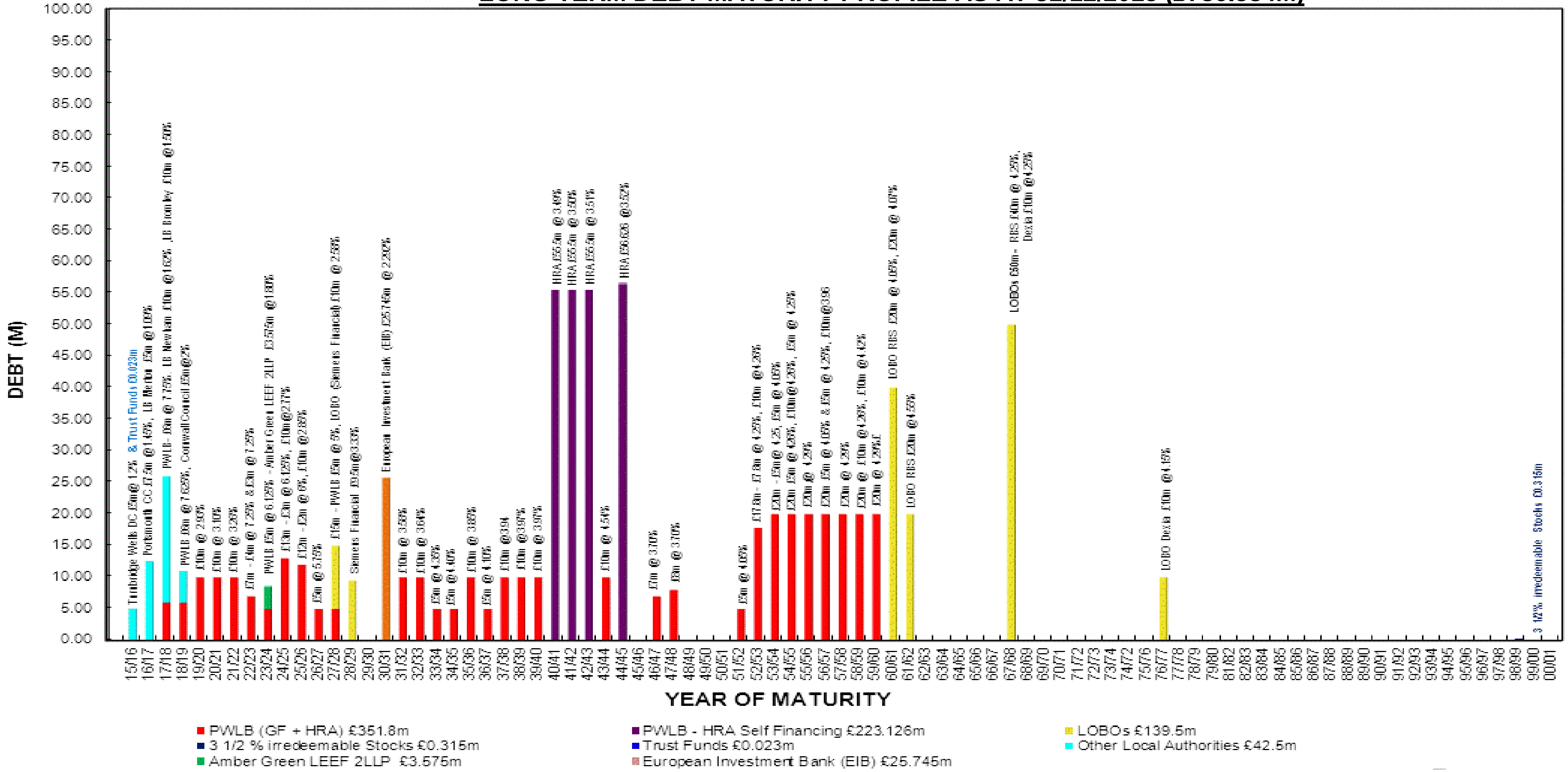
BACKGROUND DOCUMENTS:

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

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

DCLG's Guidance on Local Government Investments March 2004.

LONDON BOROUGH OF CROYDON
LONG TERM DEBT MATURITY PROFILE AS AT 31/12/2015 (£786.584M)



Appendix A

APPENDIX B

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

-

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

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

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

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

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

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

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

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

APPENDIX C

AFFORDABLE BORROWING LIMITS 2016/17 TO 2018/19

	£m	£m	Limit £m
2016/17			
Estimated borrowing as at 31st March 2016 (see Note 1 below)		**895.0**	
Allowance for temporary revenue borrowing (see Note 2 below)		**40.0**	
Revolving Investment Fund (RIF) borrowing		**100.0**	
Growth Zone borrowing		**15.0**	
Additional Borrowing 2016/17	**82.6**		
Maturities 2016/17	**(12.5)**		
Maturities refinance 2016/17	**12.5**		
Additional borrowing	**82.6**	**82.6**	
Affordable borrowing limit 2016/17		**1,132.6**	**1,132.6**
2017/18			
Additional Borrowing 2017/18	**53.4**		
Maturities 2017/18	**(26.0)**		
Maturities refinance 2017/18	**26.0**		
Additional borrowing	**53.4**	**53.4**	
Growth Zone borrowing		**30.0**	
Affordable borrowing limit 2017/18		**1,216.0**	**1,216.0**
2018/19			
Additional Borrowing 2018/19	**1.1**		
Maturities 2018/19	**(11.0)**		
Maturities refinance 2018/19	**11.0**		
Additional borrowing	**1.1**	**1.1**	
Growth Zone borrowing		**50.0**	
Affordable borrowing limit 2018/19		**1,267.1**	**1,267.1**

Note

1. **The external debt outstanding as at 31/3/2016 includes the £223.126m that was borrowed from the PWLB for the HRA Self Financing settlement on 28/3/12 and the balance of 2015/16's borrowing requirement which was outstanding as at 31/12/15 (see 3.1).**

2. **This is the upper limit which assumes a worst case scenario for example in the event of the unexpected late receipt of major income such as Council Tax, NNDR, Housing Benefit subsidy or other government grants. The £40m represents the maximum in short term borrowing that is affordable and which could be undertaken to ease cash flow difficulties in such instances.**

APPENDIX D

PRUDENTIAL INDICATORS FOR 2015/16 – 2018/19

PRUDENTIAL INDICATORS	2015/16 Probable Outturn £m	2016/17 Forecast £m	2017/18 Forecast £m	2018/19 Forecast £m
1. Prudential Indicators for Capital Expenditure				
1.1. Capital Expenditure (includes £10m advanced to Real Property Lettings Fund – see 3.5.13)				
- General Fund estimate as at 31/12/15	111.388	142.564	72.584	26.610
- HRA as at 31/12/15	37.552	33.621	33.621	33.621
Total as at 31/12/15	**148.940**	**176.185**	**106.205**	**60.231**
1.2. In year Capital Financing Requirement (see Table 3)				
- General Fund - gross of MRP costs(includes £10m advanced to Real Property Lettings Fund)	51.431	82.676	60.723	9.374
- HRA	5.217	6.191	0.000	0.000
Total in year Capital Financing Requirement	**56.648**	**88.867**	**60.723**	**9.374**
1.3. Capital Financing Requirement as at 31st March – **balance sheet figures**				
- General Fund (net of MRP costs)	570.000	650.000	710.000	710.000
- HRA- [1] limit of HRA debt imposed by CLG	333.905[1]	333.905[1]	333.905[1]	333.905[1]
Total	**903.905**	**983.905**	**1,043.905**	**1,043.905**
2. Prudential Indicators for Affordability				
2.1. Ratio of financing costs to net revenue streams				
- General Fund	10.0%	13.0%	14.00%	14.0%
- HRA	16.00%[2]	16.00%[2]	16.00%[2]	16.00%[2]
2.2. General Fund impact of Prudential (unsupported) borrowing on Band D Council Tax levels (per annum)				
- In year increase	£4.00	£14.00	£11.00	£3.00
- Cumulative increase (includes MRP costs).		£33.00	£64.00	£82.00
2.3. HRA impact of additional borrowing (unsupported) on housing rents (per annum)	0	0	0	0
[2]The HRA's additional £223.1m debt costs are reflected in these ratios.				
3. Prudential Indicators for Long External Debt				
3.1. Debt brought forward 1st April	760.839	895.071	1092.666	1,176.036
Debt carried forward 31st March (includes the £223.1m debt for the HRA self-financing settlement sum plus RIF & Growth Zone borrowings in future years).	895.071	1092.666	1,176.036	1,227.173
Additional Borrowing	**134.232**	**197.595**	**83.370**	**51.137**

APPENDIX D

PRUDENTIAL INDICATORS	2015/16 Probable Outturn £m	2016/17 Forecast £m	2017/18 Forecast £m	2018/19 Forecast £m
3.2. Operational boundary for external debt (excludes revenue borrowing)				
Borrowing	895.071	1,092.666	1,176.036	1,227.173
Other long term liabilities	0	0	0	0
3.3. Total operational debt (excludes revenue borrowing)	895.071	1,092.666	1,176.036	1,227.173
Add margin for cashflow contingency	40.000	40.000	40.000	40.000
Affordable Borrowing Limit (includes revenue borrowing)	935.071	1,132.666	1,216.036	1,267.173
Authorised limit for external debt (includes revenue borrowing)				
Borrowing	935.071	1,132.666	1,216.036	1,267.173
Other long term liabilities	0	0	0	0
Authorised Borrowing Limit	**935.071**	**1,132.666**	**1,216.036**	**1,267.173**
4. <u>Prudential Indicators for Treasury Management</u>				
4.1. Borrowing limits - upper limit for fixed interest rate exposure expressed as:-				
Net principal re fixed rate borrowing / investments	935.071	1,132.666	1,216.036	1,267.173
4.2. Borrowing limits - upper limit for variable rate exposure expressed as :-				
Net principal re variable rate borrowing / investments	20%	20%	20%	20%
4.3. Lending limits - upper limit for total principal sums invested for over 364 days expressed as a % of total investments	30%	30%	30%	30%

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

APPENDIX E

MINIMUM REVENUE PROVISION POLICY STATEMENT FOR 2016/17

The Council has implemented the new Minimum Revenue Provision (MRP) Guidance from 2008/09, and will continue to assess their MRP for 2016/17 in accordance with the main recommendations contained within the Guidance issued by the Secretary of State under Section 21(1A) of the Local Government Act 2003.

The Council's MRP Policy Statement for 2016/17 is to be as follows:

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

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

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

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

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

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

7. The Council's cash investment in the Real Lettings Property Fund LP under a 7 year life arrangement is due to be returned in full at maturity with interest paid annually. The cash investment will be treated as capital expenditure with the Council's Capital Financing Requirement (CFR) increasing by this amount. At maturity, the funds returned to the Council will be treated as a capital receipt and the CFR will reduce accordingly. As this is a temporary arrangement over 6 years, and as the funds are to be returned in

full, there is no need to set aside prudent provision to repay the debt liability in the interim period, and therefore no MRP application is required.

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

Appendix F

LONDON BOROUGH OF CROYDON
Authorised Lending List as at 31/12/15 (Ratings as per FITCH)

LIST A

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

LIST B

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

Appendix F

LENDING LIST CRITERIA

LIST A

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

CREDIT RATINGS

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

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

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

LIST B

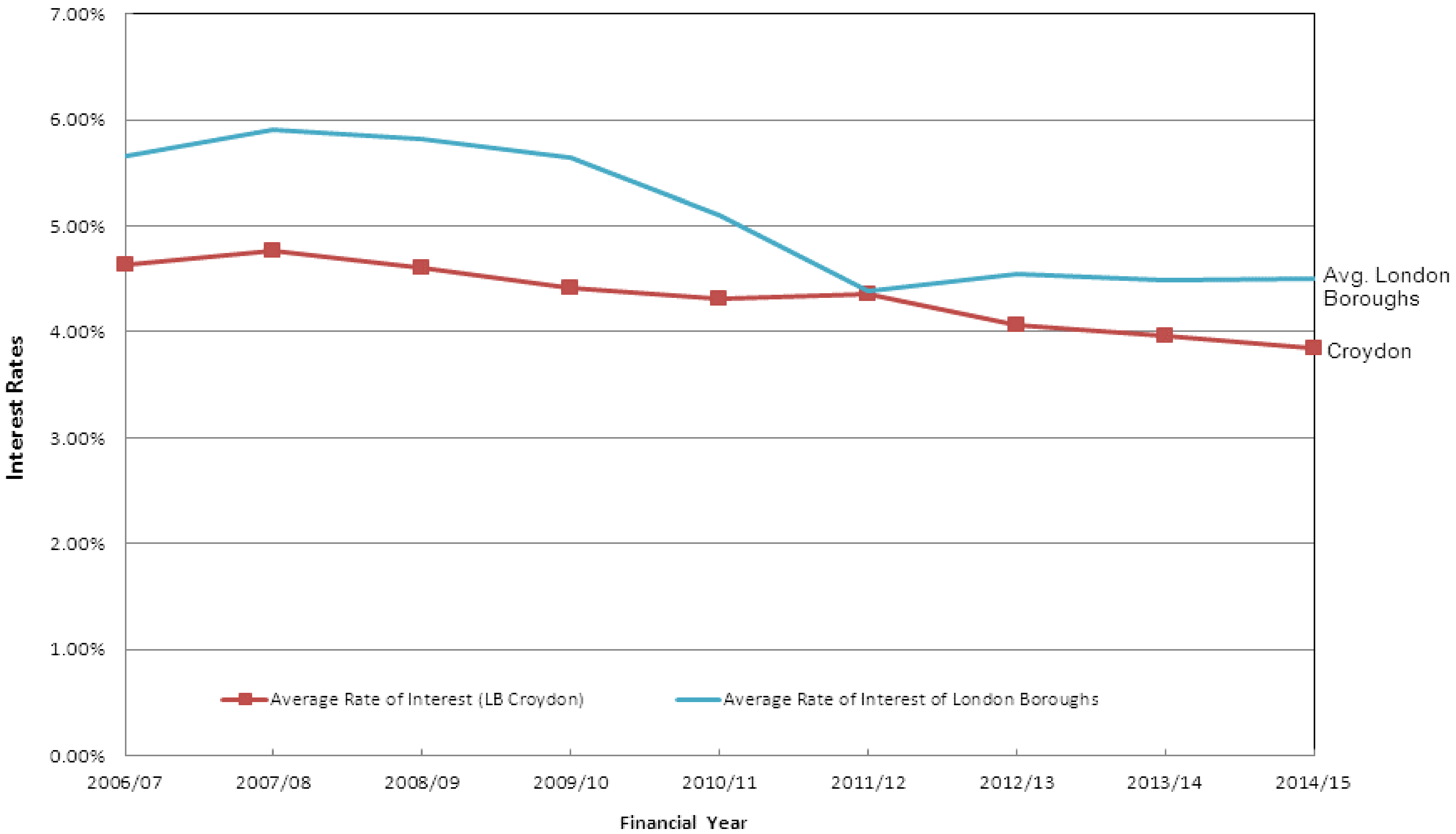
LIMITS TO INDIVIDUAL ORGANISATIONS
Maximum Investment Limit - £10m

CREDIT RATINGS

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

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

Average Rate of Interest on External Debt
Comparison between LB Croydon and London Boroughs' Average



Appendix G

APPENDIX H

GLOSSARY OF TERMS USED IN THE TREASURY STRATEGY STATEMENT, MINIMUM REVENUE PROVISION POLICY STATEMENT & ANNUAL INVESTMENT STRATEGY 2016/17

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

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