

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.
 - 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.
 - 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.

- 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.
- 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, Volkswagen 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.
- 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.