THIS PAPER RELATES TO ITEM 04 ON THE AGENDA

CLACKMANNANSHIRE COUNCIL

Report to Special Meeting of Clackmannanshire Council

Date of Meeting: 27th March 2017

Subject: Treasury Management Strategy Statement 2017/18 and Prudential Indicators 2017/18 to 2021/22

Report by: Chief Accountant

1.0 Purpose

1.1 The purpose of this report is to present the Council's Treasury Management Strategy Statement for 2017/18 and Prudential Indicators for 2017/18 to 2021/22.

1.2 CIPFA defines treasury management 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."

2.0 Recommendations

2.1 It is recommended that Council:

2.1.1 Approve the Treasury Management Strategy Statement for 2017/18 and prudential indicators for the years 2017/18 to 2021/22 in compliance with the Prudential Code requirements attached as Appendix A.

3.0 Considerations

Background

3.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

3.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

3.3 The Prudential Indicators included in Appendix A have been determined based on the budget proposals contained in the General Services Revenue and Capital Budget 2017/18 also on this agenda and the Housing Revenue Account (HRA) Financial Business Plan 2013-18 report approved by Council on 9th February 2017. This is usually presented as a separate report however, it is intended that these are consolidated for the future to provide a more holistic view of the plans and activity.

Reporting Requirements

3.4 The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of polices, estimates and actuals.

Prudential and treasury indicators and treasury strategy - The first, and most important report covers:

- the capital plans (including prudential indicators);
- the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

A mid year treasury management report – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether the performance of the treasury function is in line with the strategy or whether any policies require revision.

An annual treasury report – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

Treasury Management Strategy for 2017/18

3.5 The strategy for 2017/18 covers two main areas:

Capital

- the capital plans and the prudential indicators

Treasury Management

- the current treasury position;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;

- statutory repayment of loans fund;
- the investment policy;
- creditworthiness policy;
- country limits; and
- the investment strategy.

These elements cover the requirements of the Local Government in Scotland Act 2003, the CIPFA Prudential Code, the CIPFA Treasury Management Code and Scottish Government Investment Regulations.

Training

3.6 The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. Regular training is held for members and the last refresher was held on the 13th December 2016. Further training will be arranged as required.

The training needs of treasury management officers are periodically reviewed.

Treasury Management Consultants

3.7 The Council uses Capita Asset Services as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the Council at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review. The current contract is in place until July 2018.

4.0 Conclusion

4.1 The Treasury Management Strategy for 2017/18 builds on and consolidates the Council's existing Investment Strategy and Prudential Borrowing framework.

4.2 The strategy supports the delivery of the Council’s capital investment plans but also remains intent on reducing the Council's overall relative level of external debt compared to Scottish Local Authority averages.

5.0 Sustainability Implications

5.1 There are no sustainability implications.

6.0 Resource Implications

6.1 Financial Details

6.2 There are no direct financial implications arising from the recommendations in this report. Yes ☑

6.3 Finance has been consulted and has agreed the financial implications as set out in the report. Yes ☑

6.4 Staffing

6.5 None

7.0 Exempt Reports

Is this report exempt? Yes ☐ (please detail the reasons for exemption below) No ☑

8.0 Declarations

The recommendations contained within this report support or implement our Corporate Priorities and Council Policies.

(1) **Our Priorities** (Please double click on the check box ☑)

The area has a positive image and attracts people and businesses	☐
Our communities are more cohesive and inclusive	☐
People are better skilled, trained and ready for learning and employment	☐
Our communities are safer	☐
Vulnerable people and families are supported	☐
Substance misuse and its effects are reduced	☐
Health is improving and health inequalities are reducing	☐
The environment is protected and enhanced for all	☐
The Council is effective, efficient and recognised for excellence	☑

(2) Council Policies (Please detail)

9.0 Equalities Impact

9.1 Have you undertaken the required equalities impact assessment to ensure that no groups are adversely affected by the recommendations?
Yes ☐ No ☑

10.0 Legality

10.1 It has been confirmed that in adopting the recommendations contained in this report, the Council is acting within its legal powers. Yes ☑

11.0 Appendices

11.1 Please list any appendices attached to this report. If there are no appendices, please state "none".

Appendix A – 2017/18 Treasury Management Strategy Statement & Annual Investment Strategy (including prudential indicators)

Appendix B - Investment Portfolio as at 31st January 2017

12.0 Background Papers

12.1 Have you used other documents to compile your report? (All documents must be kept available by the author for public inspection for four years from the date of meeting at which the report is considered)

Yes ☑ (please list the documents below) No ☐

Treasury Management in Public Service; Code of Practice and Cross Sectoral Guidance Notes 2011

The Prudential Code for Capital Finance in Local Authorities 2011

Interest rate forecasts

Economic background

Treasury management practice 1 - credit and counterparty risk management

Treasury management scheme of delegation

The treasury management role of the section 95 officer

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Appendix A

2017/18 TREASURY MANAGEMENT STRATEGY STATEMENT & ANNUAL INVESTMENT STRATEGY (including prudential indicators)

The suggested strategy for 2017/18 in respect of the following aspects of the treasury management function is based upon the Council's views on interest rates, supplemented with leading market forecasts provided by the Council's treasury adviser, Capita Asset Services.

The strategy for 2017/18 covers the following areas:

- capital expenditure;
- the current portfolio position;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- statutory repayment of loans fund;
- the investment policy;
- creditworthiness policy;
- country limits; and
- the investment strategy.

1.0 The Capital Prudential Indicators

1.1 Capital Expenditure

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

The Prudential Code requires the Council to make reasonable estimates of the total capital expenditure that it plans to incur during the forthcoming financial year and the following two financial years. The Code also requires this information to be split between General Fund Services and Housing Revenue Account (HRA).

To provide a longer term view, the estimates of gross capital expenditure to be incurred for the next five years together with the projection for the current year and actual for 2015/16 are as follows:

Table 1: Gross Capital Expenditure

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
	£000	£000	£000	£000	£000	£000	£000
	Actual	Projection	Estimate	Estimate	Estimate	Estimate	Estimate
General Fund Services	6,694	7,918	15,634	13,813	15,106	6,970	5,746
Housing Revenue Account	9,736	6,483	9,940	7,648	8,844	9,040	8,830
Total	**16,430**	**14,401**	**25,574**	**21,461**	**23,950**	**16,010**	**14,576**

The above figures are shown net of any income and are consistent with the capital programme proposals for General Services contained within the Revenue and Capital Budget report 2017/18 and the HRA Financial Business Plan 2013-18. These capital plans take full account of the requirements of the Prudential Code and levels of expenditure across the years reflect the funding envelope available consistent with the Council's Borrowing and Investment strategy to minimise increases in external borrowing. The planned spending figure of £25.574m for 2017/18 will be kept under review through the capital monitoring process and regularly reported to the Audit and Finance Committee.

1.2 Borrowing Need (Capital Financing Requirement)

Capital expenditure that is not financed upfront by the use of capital receipts, capital grants or directly from revenue will increase the capital financing requirement of the Council. The calculation of the Capital Financing Requirement is therefore intended to reflect the Council’s underlying need to borrow for a capital purpose and it is used as a key measure in treasury management decisions for this reason.

Estimates of the end of year Capital Financing Requirement for the Council for the current and future years together with the actual position last year are:

Table 2: Capital Financing Requirement as at:

	31/03/16	31/03/17	31/03/18	31/03/19	31/03/20	31/03/21	31/03/22
	£000	£000	£000	£000	£000	£000	£000
	Actual	Projection	Estimate	Estimate	Estimate	Estimate	Estimate
General Fund Services	125,041	122,454	123,640	124,546	124,636	119,003	112,272
Housing Revenue Account	28,298	26,722	25,557	24,269	22,961	21,714	20,547
Total	**153,339**	**149,176**	**149,197**	**148,815**	**147,597**	**140,717**	**132,819**

The capital financing requirement is estimated to reduce over the next five years to £132.8m by the end of March 2022. This indicates that there is no requirement for the Council to increase long term borrowing over the next five years which is in line with the approved financial strategy of minimising long term borrowing.

The financing requirement for General Fund services increases over the period 2017/18 and 2018/19. This is to accommodate investment in several significant projects including Tullibody South Campus and the carry forward from 2016/17. The requirement then reduces in 2019/20 and continues to reduce further by March 2022. The overall CFR at March 2022 is a reduction of £10.2m on the projected level at March 2017. This reduction is in line with the strategy of keeping the capital programme at a level that does not incur any net additional borrowing over the 5 year capital programme.

The financing requirement for the Housing programme is reducing over the 5 years in line with the housing business plan.

1.3 Affordability

Prudential Indicators are required to assess the affordability of capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances.

1.3.1 Ratio of financing costs to net revenue stream

The Prudential Code requires the Council to make estimates of the ratio of capital financing costs to its net revenue stream.

The indicator is intended to measure the percentage of the Council's total income that it is estimated will be committed towards meeting the costs of borrowing used to fund capital expenditure. For the General Fund this is the ratio of financing costs of borrowing against net expenditure financed by government grant and local taxpayers. For the HRA the indicator is the ratio of financing costs to gross rental income.

Estimates of the ratio of financing costs to net revenue stream for the current and future years are:

Table 3: Ratio of financing costs to net revenue stream

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
	£000	£000	£000	£000	£000	£000	£000
	Actual	Projection	Estimate	Estimate	Estimate	Estimate	Estimate
General Fund	8.12%	8.10%	8.09%	8.68%	8.92%	9.16%	9.16%
Housing Revenue Account	16.80%	16.66%	16.03%	15.33%	15.08%	15.17%	15.27%

The above figures show that for the General Fund, over the next five years, the proportion of the budget allocated to loan charges shows a modest increase which is a positive outcome over this period against a backdrop of broadly reducing levels of government grant funding, stable levels of council tax and increasing annual PPP costs. This demonstrates that capital financing costs are being controlled through the effective implementation of the Council's borrowing and investment strategy

Capital investment in Housing is in accordance with the approved Business Plan to achieve the Scottish Housing Quality Standard together with our own Clackmannanshire Standard. The ratio of capital financing costs to rental income has reduced and is projected to remain steady over the years 2018/19 to 2020/21 now that previous high reserves have been utilised as per the approved Business Plan.

1.3.2 Estimates of Incremental impact of new capital Investment decisions on Council Tax and House Rents

This indicator is intended to measure the incremental impact on the Council Tax and Housing Rents which would arise from changes to the Council's existing capital budget.

Table 4: Incremental impact of capital spending on:

	2017/18	2018/19	2019/20	2020/21	2021/22
Council Tax (Band D)	£0.17	£10.49	-£1.56	£0.31	-£4.42
Average Weekly House Rents (per week)	£1.35	£1.16	£2.03	£2.21	£2.52

The capital financing cost consequences of the general services capital proposals for the years 2017/18 to 2021/22 have been assessed against the plans approved last year. The indicator fluctuates due to reprioritisation of existing projects however overall new capital investment is restricted to the sum of capital grants and current levels of loan repayment provision over the life of the programme. Although there is no requirement to increase Council Tax to fund borrowing, the Council has the ability to increase Council Tax within policy parameters currently capped at 3% to fund other elements of revenue expenditure.

The HRA capital investment plans record slight increases in planned net borrowing requirement compared to the previous year. This is due to rephased spending in line with up-to-date condition surveys.

2.0 Borrowing

The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of approporiate borrowing facilities. The strategy covers the relevant treasury indicators, the current and projected debt positions and the annual investment strategy.

2.1 Current Portfolio Position

Within the Prudential Indicators there are a number of key indicators to ensure that the Council operates its activities within well defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the Capital Financing Requirement (CFR) in the preceding year plus the estimates of any additional CFR for 2017/18 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Council's treasury portfolio position at 31 March 2016 with forward projection are summarised in the table below. The table shows;

- the cumulative level of external debt held by the Council which represents the total amount of borrowing that has been undertaken to fund the capital programme;
- the expected change in debt which is any repayments of maturing debt less new debt undertaken in the year to fund the in-year capital programme;
- Other Long Term Liabilities which is the total of any Finance Lease or PFI arrangements;
- the expected change in Other Long Term Liabilities which refers to the repayments in the year made against this debt;
- the Capital Financing Requirement which is the cumulative amount of borrowing that the Council required to borrow to fund capital expenditure; and
- the under or over borrowing position which is the difference between the required need to borrow and the actual borrowing undertaken.

The code requires local authorities to maintain an under-borrowed position in the long term, this means that the total amount borrowed does not exceed the need to borrow. An under-borrowed position can occur where cash balances have been used to fund capital expenditure whereas, an over-borrowed position can occur where borrowing has been taken in advance of need. This is permissible in the short term to take account of timing of cash flows but the Council must return to an under-borrowed position in future years.

Table 5: External Debt

£000	2015/16 Actual	2016/17 Projected	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
External Debt							
Cumulative Debt at 1 April	118,658	102,651	103,446	107,666	108,421	108,446	102,639
Expected change in Debt	(16,007)	795	4,220	755	26	(5,807)	(6,908)
Other long-term liabilities (OLTL) at 1 April	45,005	43,715	42,404	41,342	40,374	39,147	37,845
Expected change in OLTL	(1,290)	(1,311)	(1,062)	(968)	(1,227)	(1,302)	(1,173)

£000	2015/16 Actual	2016/17 Projected	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Actual gross debt at 31 March	**146,366**	145,850	149,008	148,795	147,594	140,484	132,403
The Capital Financing Requirement	**153,339**	149,176	149,197	148,815	147,597	140,717	132,819
Under / (over) borrowing	**6,973**	3,326	189	20	3	233	416

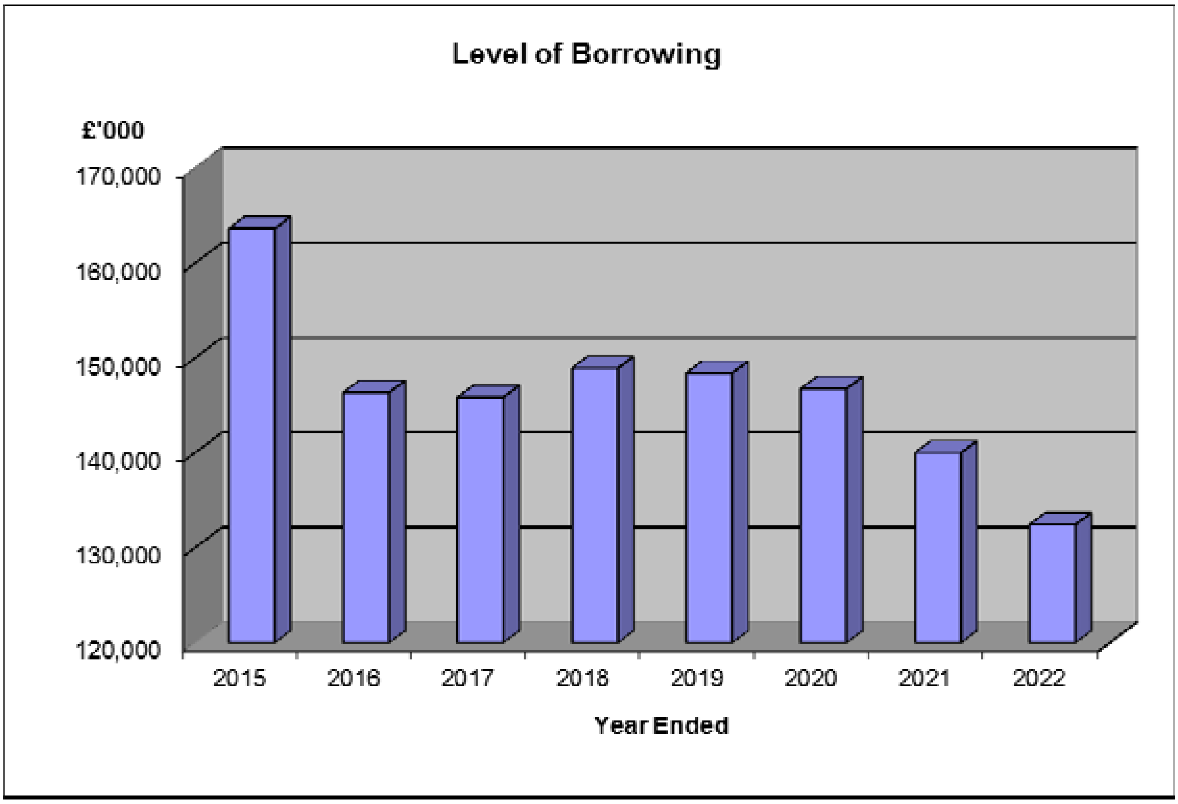
At the end of 2015/16 the Council's Gross Debt was less than the Capital Financing Requirement resulting in an under-borrowed position of £6.973m. This was as a result of internal borrowing/utilisation of cash balances to fund Capital expenditure. For all years shown in the above table the Council's Capital Financing Requirement is forecast to remain below Gross Debt maintaining a consistent under-borrowed position going forward, therefore meeting the requirement of the indicator to be in an under borrowed position over the medium term. As the level borrowing is close to the CFR particularly in 2019/20, the level of capital expenditure will be closely monitored to ensure that borrowing is only undertaken to match actual spend. This will ensure an under-borrowed position is maintained.

The Capital Programme has been set in line with the Council's strategy to reduce long term debt. Repayment profiles of debt maturity mean there are variations in annual change in debt year on year. The table below shows a projected significant reduction in cumulative external debt in 2016/17 mainly due to the repayment of a PWLB loan and a projected underspend on the capital programme within the year. External debt is forecast to increase in the next two years in line with the capital programme and no debt due to be repaid in the year that would offset the level of capital expenditure required per the capital programme. The capital programme has been set at a level in order to reduce cumulative external debt again by the end of 2019/20 and reduce further showing a reduction in loan debt of £29.97m from end of March 2015 to end of March 2022. The difference between the level of borrowing and the CFR shows the amount of internal borrowing/utilisation of cash balances to fund Capital expenditure.

The steady reduction in other long term liabilities reflects the annual repayments of the PFI debt and street lighting finance lease.

The continuing trend in reducing the Council's level of borrowing is consistent with the Treasury Strategy. This is illustrated in the following chart, demonstrating actual and forecast level of debt up to 2021/22.

Table 6: Level of Borrowing



2.2 Treasury Indicators: limits to borrowing activity

2.2.1 Operational Boundary for External Debt

This is a key management tool for in-year monitoring and is lower than the Authorised Limit as it is based on an estimate of the most likely level of external borrowing at any point in the year. In comparison, the authorised limit is the maximum allowable level of borrowing.

Table 7: Operational Boundary for external debt

	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
	£000	£000	£000	£000	£000	£000
Borrowing	109,000	110,000	110,000	110,000	105,000	98,000
Other long term liabilities	43,000	42,000	41,000	40,000	38,000	37,000
Total	**152,000**	**152,000**	**151,000**	**150,000**	**143,000**	**135,000**

This indicator is consistent with the Council's plans for capital expenditure and financing with Treasury Management policy and practice. It is sufficient to facilitate appropriate borrowing during the financial year and will be reviewed on an on-going basis.

2.2.2 Authorised Limit for External Debt

The authorised limit for external debt is required to separately identify external borrowing (gross of investments) and other long term liabilities such as finance lease obligations. The limit provides a maximum figure that the Council could borrow at any given point during each financial year.

Table 8: Authorised limit for external debt

	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
	£000	£000	£000	£000	£000	£000
Borrowing	114,000	115,000	115,000	115,000	110,000	103,000
Other long term liabilities including PFI	48,000	47,000	46,000	45,000	43,000	42,000
Total	**162,000**	**162,000**	**161,000**	**160,000**	**153,000**	**145,000**

The authorised limit set out above is consistent with approved capital investment plans and Treasury Management policy and practice but allows sufficient headroom for unanticipated cash movements. The limit has been reduced over the next five years in line with reductions in actual external borrowing. The limit will be reviewed on an on-going basis during the year. If the authorised limit is liable to be breached at any time, the Depute Chief Executive will report to the Audit and Finance Committee. It will then be open to Committee to raise the authorised limit or to take measures to ensure the limit is not breached.

3.0 Prospects for Interest Rates

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

Table 9: Forecast Interest Rates

Quarter ended	Bank Rate %	PWLB Borrowing Rates (including certainty rate adjustment)		
		5 year	25 year	50 year
March 2017	0.25	1.60	2.90	2.70
June 2017	0.25	1.60	2.90	2.70
Sept 2017	0.25	1.60	2.90	2.70
Dec 2017	0.25	1.60	3.00	2.80

Quarter ended	Bank Rate %	PWLB Borrowing Rates (including certainty rate adjustment)		
March 2018	0.25	1.70	3.00	2.80
June 2018	0.25	1.70	3.00	2.80
Sept 2018	0.25	1.70	3.10	2.90
Dec 2018	0.25	1.80	3.10	2.90
March 2019	0.25	1.80	3.20	3.00
June 2019	0.50	1.90	3.20	3.00
Sept 2019	0.50	1.90	3.30	3.10
Dec 2019	0.75	2.00	3.30	3.10
March 2020	0.75	2.00	3.40	3.20

The Bank Rate was cut from 0.50% to 0.25% on 4th August 2016 in order to counteract what it forecast was going to be a sharp slowdown in growth in the second half of 2016. It now appears that there will be no change in this rate until June 2019. During the two-year period 2017 – 2019, when the UK is negotiating the terms for withdrawal from the EU, it is unlikely that the Bank Rate will be increased. Accordingly, a first increase to 0.50% is not expected, as in the table above, until June 2019, after those negotiations have been concluded.

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

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

- The overall trend in the longer term will be for gilt yields and PWLB rates to gradually rise when economic recovery is firmly established accompanied by rising inflation and consequent increases in Bank Rate;
- Investment returns are likely to remain low during 2017/18 and beyond;
- Borrowing interest rates have generally reduced during most of 2016 falling more rapidly towards the end of the year after the referendum and the announcement of a new package of quantitative easing by the MPC. The policy of avoiding new borrowing by running down spare cash balances has had a positive impact 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; and
- There remains a cost of carrying any new borrowing which causes an increase in investments as this will continue to incur a revenue loss between borrowing costs and investment returns.

4.0 Borrowing Strategy

Over the medium term the Council is forecasted to maintain an under-borrowed position. This means that the capital borrowing need (CFR), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is relatively high.

Against this background and the risks within the economic forecast, caution will be adopted with the 2017/18 treasury operations. The Depute Chief Executive supported by the Treasury team will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in long and short term rates* (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast,* perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are still lower than they will be in the next few years.

Any decisions will be reported to the appropriate committee at the next available opportunity.

4.1 Borrowing Requirement

The Council's borrowing requirement shown in the table below is based on the in-year borrowing estimated to be needed to fund the net expenditure in the Financial Plans / Capital Budgets for both Housing and General Fund Services which were approved at meetings of the Council and Special Council in February and March 2017.

The actual timing of any borrowing will be influenced by prevailing interest rates and expectations for future movement on rates.

Over the longer term, repayments towards maturing debt should be higher than any new borrowing being undertaken to fund the Capital programme. The table below shows a reduction in external borrowing over the five years to 2021/22. This is consistent with the Council's existing strategy to reduce overall level of external debt compared to Scottish averages.

Table 10: Total Borrowing Requirement / Movement on CFR

	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
Net New External Borrowing Requirement	7,225	5,760	6,531	110	0
Repayment of Maturing Debt (Principle repayments)	(4,067)	(5,973)	(7,732)	(7,219)	(7,591)
Total Borrowing Requirement / Movement on CFR	**3,158**	**(213)**	**(1,201)**	**(7,109)**	**(7,591)**

4.2 Treasury management limits on activity

There are three debt related treasury activity limits. The purpose of these is to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs / improve performance. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments;
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates; and
- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

The Council is asked to approve the following treasury indicators and limits:

Table 11: Treasury Management Limits

£m	2017/18	2018/19	2019/20
Interest rate exposures			
	Upper	**Upper**	**Upper**
Limits on fixed interest rates based on • **Debt** • **Investments**	 90% 60%	 90% 60%	 90% 60%
Limits on variable interest rates based on • **Debt** • **Investments**	 25% 75%	 25% 75%	 25% 75%
Maturity structure of fixed interest rate borrowing 2017/18			
		Lower	**Upper**
Under 12 months		0%	25%
12 months to 2 years		0%	25%
2 years to 5 years		0%	50%
5 years to 10 years		0%	75%
10 years and above		0%	100%

Maturity structure of variable interest rate borrowing 2017/18		
	Lower	**Upper**
Under 12 months	0%	25%
12 months to 2 years	0%	25%
2 years to 5 years	0%	50%
5 years to 10 years	0%	75%
10 years and above	0%	100%

5.0 Policy on borrowing in advance of need

The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sum borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

6.0 Debt Rescheduling

As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

The reasons for any rescheduling to take place will include:

- the generation of cash savings and / or discounted cash flow savings;
- helping to fulfil the treasury strategy; or
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

All rescheduling will be reported to Council at the earliest meeting following its action.

7.0 Statutory repayment of loans fund advances

A policy for the statutory repayment of loans fund advances must be set out prior to the start of the financial year. The repayment of loans fund advances ensures that the Council makes a prudent provision each year to pay off an element of the accumulated loans fund advances made in previous financial years.

A variety of options are provided to Councils so long as a prudent provision is made each year. For loans fund advances the policy will be to maintain the practice of previous years and apply the Asset Life Method with all loans fund advances being repaid with reference to the life of an asset using the annuity method.

The annuity rate applied to the Council's loans fund is reviewed annually which is in line with the new regulation 14 (2) of SSI 2016 No 123 - to ensure that it is a prudent application. The annuity rate used provides a fair and prudent approach and generates principal repayments that are closely associated with the use of the assets. The actual annuity rate used for 2016/17 (also referred to as the Pool loan rate) is 5.05%.

8.0 Investment Policy

8.1 The aim of the strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoidance of concentration risk. The intention of the strategy is to provide security of investment and minimisation of risk

8.2 Opportunities for investment arise naturally through Treasury Management activity and in particular the management of cash flows which can result in peaks and troughs in the amount of cash required during the year. It should be noted that these cash balances currently amount to over £18.3m as at 31st January 2017. During the year the council will look to invest surplus cash balances of which the return contributes to reducing the net expenditure of the Council.

8.3 The Council's investment policy has regard to the Scottish Government's Investment (Scotland) Regulations (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 will be security first, liquidity second and then return.

8.4 In accordance with guidance from the Scottish Government and CIPFA, and in order to minimise the risk to investments, the Council applies minimum acceptable credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

8.5 The Council's officers will use ratings and other information provided by Capita Asset Services to ensure creditworthiness as detailed below.

8.6 Officers will also use other information sources which include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

9.0 Creditworthiness Policy

9.1 This Council applies the creditworthiness service provided by Capita Asset Services. This service employs a sophisticated weighted modelling approach utilising a wide array of information sources including credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's.

9.2 This approach produces a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands*:*

- Yellow 5 years
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year

- Red 6 months
- Green 100 days
- No colour not to be used

9.3 The Council will consider the ratings (Fitch or equivalents) in conjunction with other topical market information to support their use

9.4 All credit ratings of counterparties currently used will be monitored monthly. The Council is alerted to changes to ratings of all three agencies through its use of the Capita Asset creditworthiness service.

9.5 In the case where an investment is outwith the scope of the ratings agencies the Council will analyse the financial information available for that organisation such as annual accounts to assess the financial viability of the investment. Joint Venture arrangements, contractual agreements and financial guarantees from the Scottish Government are some of the elements that are used for the Council's current investments to ensure a minimal level of financial risk. For the investments listed in Appendix B, these all fall outwith the scope of the ratings agencies.

10.0 Country limits

10.1 The Council has determined that it will only use approved counterparties registered to take deposits in the United Kingdom or approved counterparties registered in other countries who have an equal or better sovereign credit rating.

11.0 Investment Strategy

11.1 **In-house funds -** Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

11.2 **Investment returns expectations -** Bank Rate is forecast to stay flat at 0.25% until quarter 2 of 2019 and not forecast to rise to 0.75% until quarter 4 of 2019. Bank Rate forecasts for financial year ends (March) are :

- 2017/18 0.25%
- 2018/19 0.25%
- 2019/20 0.75%

11.3 Taking account of the current investment returns the suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during each financial year for the next five years are as follows:

- 2017/18 0.25%
- 2018/19 0.25%
- 2019/20 0.75%

- 2020/21 0.75%
- 2021/22 1.00%

11.4 **Investment treasury indicator and limit** - total principal funds invested for greater than 364 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

11.5 The Council is asked to approve the treasury indicator and limit: -

Maximum principal sums invested > 364 days			
£m	**2017/18**	**2018/19**	**2019/20**
Principal sums invested > 364 days	£12m	£12m	£12m

11.6 For its cash flow generated balances, the Council will seek to utilise its bank instant access and notice accounts, money market funds and short-dated deposits (overnight to 100 days) in order to benefit from the compounding of interest.

Onlending to Registered Social Landlords (RSL's)

11.7 The Scottish Government has recently granted powers to enable Scottish Local Authorites to on lend to Registered Social Landlords in order to assist in the development of affordable housing. Any plans to utilise these powers will be reported for appropriate Council approval.

End of year investment report

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

APPENDIX B: Investment Portfolio as at 31st January 2017

Cash and Cash Equivalents	Principal (£000)	Interest Rate	Account Type
Bank of Scotland PLC	5,000	0.65%	Fixed Rate 6 month
Bank of Scotland PLC	5,000	0.90%	Fixed Rate 12 month
Royal Bank of Scotland PLC	8,304	0.10%	Instant Access
Total Cash and Cash Equivalents	**18,304**		

Short Term Investments	Principal (£000)
CSBP Developments	15
Total Short Term Investments	**15**

Long Term Investments	Principal (£000)
CSPB Investments	1
Clackmannanshire Regeneration	4,906
Coalsnaughton NHT Project	2,976
Total Long Term Investments	**7,883**

TOTAL INVESTMENTS	**26,294**