TREASURY MANAGEMENT STRATEGY 2017/18 – 2019/20

1. INTRODUCTION

1.1. In February 2012 the Council adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year.

1.2. In addition, the Department for Communities and Local Government (CLG) issued revised Guidance on Local Authority Investments in March 2010 that requires the Council to approve an investment strategy before the start of each financial year.

1.3. This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the CLG Guidance.

1.4. The Council has potentially large exposures to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's treasury management strategy.

2. External Context

2.1. Economic background

The major external influence on the Council's treasury management strategy for 2017/18 will be the UK's progress in negotiating a smooth exit from the European Union. Financial markets, wrong-footed by the referendum outcome, have since been weighed down by uncertainty over whether leaving the Union also means leaving the single market. Negotiations are expected to start once the UK formally triggers exit in early 2017 and last for at least two years. Uncertainty over future economic prospects will therefore remain throughout 2017/18.

The fall and continuing weakness in sterling and the near doubling in the price of oil in 2016 have combined to drive inflation expectations higher. The Bank of England is forecasting that Consumer Price Inflation will breach its 2% target in 2017, the first time since late 2013, but the Bank is expected to look through inflation overshoots over the course of 2017 when setting interest rates so as to avoid derailing the economy.

Initial post-referendum economic data showed that the feared collapse in business and consumer confidence had not immediately led to lower GDP growth. However, the prospect of leaving the single market has dented business confidence and resulted in a delay in new business investment and, unless counteracted by higher public spending or retail sales, will weaken economic growth in 2017/18.

2.2. Credit outlook

Bail-in legislation, which ensures that large investors including local authorities will rescue failing banks instead of taxpayers in the future, has now been fully implemented in the European Union, Switzerland and USA, while Australia and Canada are progressing with their own plans. The credit risk associated with making unsecured bank deposits has therefore increased relative to the risk of other investment options available to the Council; returns from cash deposits however continue to fall.

2.3. Interest rate forecast

The Council's treasury adviser Arlingclose's central case is for UK Bank Rate to remain at 0.25% during 2017/18. The Bank of England has, however, highlighted that excessive levels of inflation will not be tolerated for sustained periods. Given this view and the current inflation outlook, further falls in the Bank Rate look less likely. A negative Bank Rate is currently perceived by some policymakers to be counterproductive but, although a low probability, cannot be entirely ruled out in the medium term, particularly if the UK enters recession as a result of concerns over leaving the European Union.

A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix A.

3. Balance Sheet summary and forecast

3.1. On 31st December 2016, the Council held £144.2m of borrowing and £77.8m of investments. This is set out in further detail at Appendix B. Forecast changes in these sums are shown in the balance sheet analysis in Table 1 below.

Table 1: Balance Sheet Summary and Forecast	**31/03/16 Actual £m**	**31/03/17 Estimate £m**	**31/03/18 Forecast £m**	**31/03/19 Forecast £m**	**31/03/20 Forecast £m**
General Fund (GF) CFR	3.2	3.4	3.9	4.4	5.8
Housing Revenue Account (HRA) CFR	1.9	1.9	1.9	1.9	1.9
HRA settlement	142.7	142.7	138.6	134.5	130.4
Total CFR	**147.8**	**148.0**	**144.4**	**140.8**	**138.1**
Less: External borrowing *	(144.3)	(144.1)	(139.8)	(135.5)	(131.2)
Internal (over) borrowing	**3.5**	**3.9**	**4.6**	**5.3**	**6.9**
Less: GF Usable reserves	(18.5)	(17.8)	(17.8)	(17.9)	(18.2)
Less: HRA Usable reserves	(24.0)	(26.8)	(23.6)	(14.6)	(14.3)
Less: Working capital	(13.3)	(5.4)	(1.3)	(1.3)	(1.3)
Resources for investments	**(55.8)**	**(50.0)**	**(42.7)**	**(33.8)**	**(33.8)**
New borrowing (or investments)	**(52.3)**	**(46.1)**	**(38.1)**	**(28.5)**	**(26.9)**

* shows only loans to which the Council is committed and excludes optional refinancing

3.2. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

3.3. The £77.8m investment balance referred to in para 3.1 significantly differs to the £46.1m estimated balance as at 31/03/17 predominantly because of cash flow differences to Council Tax and Business Rate Collections over the period January - March. The level of usable HRA reserves is set to decrease over the period as the Council works towards achieving its latest acquisition and development strategy, as well as commencing with principal repayments on the settlement loan. Working capital balances are estimated to decrease over the period due to the likely call on specific provisions.

3.4. CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Council expects to comply with this recommendation during 2017/18.

4. Borrowing Strategy

4.1. The Council currently holds £144.2 million of loans, a decrease of £0.2 million on the previous year, with the majority of the loan related to the HRA refinancing settlement from 2012. The balance sheet forecast in Table 1 shows that the Council does not expect to need to borrow in 2017/18. The Council may however borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £174.4 million.

4.2. Objectives

The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

4.3. Limits

The Council is required to put in place the following Prudential Indicators to control its limits on borrowing; these are operational and authorised boundaries for external debt, and the maximum HRA debt limit.

Operational Boundary for External Debt

The operational boundary is based on the Council's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the Council's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring.

Table 2: Operational Boundary	2016/17 Revised £m	2017/18 Limit £m	2018/19 Limit £m	2019/20 Limit £m
Total Debt	**163.0**	**159.4**	**155.8**	**153.1**

Authorised Limit for External Debt

The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Council can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

Table 3: Authorised Limit	2016/17 Revised £m	2017/18 Limit £m	2018/19 Limit £m	2019/20 Limit £m
Total Debt	**178.0**	**174.4**	**170.8**	**168.1**

Maximum HRA Debt Limit

The Council is also limited to a maximum HRA CFR through the HRA self-financing regime. The Council may not borrow more than this limit for HRA purposes.

This limit is dictated by the DCLG and is based on the amount of the settlement payment of £142.7m plus the old Housing Subsidy Notional Debt amount of £12.8m, plus any further borrowing approved by the DCLG. The Council is not currently planning to seek further approvals to increase HRA borrowing and therefore actual total borrowing for the HRA is currently predicted to remain at £142.7m until 2017/18.

Table 4: HRA Debt Limit	2016/17 Revised £m	2017/18 Limit £m	2018/19 Limit £m	2019/20 Limit £m
Total	**155.5**	**155.5**	**155.5**	**155.5**

4.4. Strategy

Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, if the Council does not need to borrow, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

By internally borrowing, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal and short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Council with this 'cost of carry' and breakeven analysis.

In addition, the Council may borrow short-term loans (normally for up to one month) to cover unplanned cash flow shortages.

4.5. Sources:

The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB) and any successor body
- UK local authorities
- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except Hampshire Pension Fund)

- capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- operating and finance leases
- hire purchase
- Private Finance Initiative
- sale and leaseback

The Council has previously raised all of its long-term borrowing from the PWLB but it continues to investigate other sources of finance, such as local authority loans and bank loans, which may be available at more favourable rates.

4.6. Short-term and Variable Rate loans

These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators at section 6 of this strategy.

4.7. Debt Rescheduling

The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

5. Investment Strategy

5.1. The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's investment balance has ranged between £54.7 and £86.1 million; balances are expected to reduce significantly over the next three years, mainly due to the reduction in HRA usable reserves, as shown in Table 1.

5.2. Objectives

Both the CIPFA Code and the CLG Guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

5.3. Negative Interest Rates

If the UK enters into a recession in 2017/18, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

5.4. Strategy

Given the increasing risk and falling returns from short-term unsecured bank investments, the Council aims to further diversify into more secure and/or higher yielding asset classes during 2017/18. This is especially the case for the estimated £25m that is available for longer-term investment. Approximately 59% (increased from 48% last year) of the Council's surplus cash is invested so that it is not subject to bail-in risk, as it is invested in local authorities, corporate bonds, pooled property and equity funds, and secured bank bonds. Whilst the remaining cash is subject to bail-in risk, 63% of this balance is held overnight money market funds which are subject to a reduced risk of bail-in, 29% is held in certificates of deposit which can be sold on the secondary market, and 2% is held in overnight call accounts with banks to allow for liquidity. The remaining 6% of cash subject to bail-in risk is held in short-term notice accounts which produce a significant return commensurate with the bail-in risk. This diversification will represent a continuation of the new strategy adopted in 2015/16.

5.5. Investments Targeting Higher Returns

In order to protect the Council's cash balances against the risk of negative or low interest rates, and the effect of bail-in, as well as to preserve the Council's income generated from investments, it is proposed that the Treasury Management Strategy have the flexibility to invest up to £20m targeting higher yielding investments. This amount represents the Council's core stable cash balance and is therefore an amount that can be managed appropriately as a long-term investment.

Higher yields can be accessed through long-term cash investments (although this is currently less the case as yields have declined) and investments in other assets than cash, such as pooled property, equities and bonds. Non-cash pooled investments must be viewed as long-term investments in order that monies are not withdrawn in the event of a fall in capital values to avoid crystallising a capital loss.

As shown in Appendix B of this report, as at 31 December 2016 the Council has invested £4.4m which could be classed under this allocation of investments targeting higher returns. In addition, the Council has committed a further £0.6m to investments in pooled funds. Without this allocation the weighted average return of the Council's cash investments would have been 0.58%; the higher yielding investments have added 0.27% (£210,000 based on the cash balance at 31 December 2016) to the average interest rate earned by the remainder of the portfolio.

5.6. Investment Limits

Given the impact of the Bank Reform Act, Bank Recovery and Resolution Directive, and the recast Deposit Guarantee Schemes Directive, which have increased the credit risk that unsecured bank investments could be 'bailed-in', the following investment limits are proposed to mitigate the risk whilst allowing sufficient flexibility to manage the Council's investment balances.

Table 5: Investment Limits	Cash limit
Any single organisation, except the UK Central Government	£8m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£8m per group
Any group of pooled funds under the same management	£8m per manager
Registered Providers	£6m in total
Money Market Funds	50% in total

5.7. Approved Counterparties

The Council may invest its surplus funds with any of the counterparty types in Table 6 below, subject to the cash limits (per counterparty) and the time limits shown.

Table 6: Approved Investment Counterparties and Limits						
Credit Rating	**Banks Unsecured**	**Banks Secured**	**Government**	**Corporates**	**Registered Providers Unsecured**	**Registered Providers Secured**
UK Govt	n/a	n/a	£ Unlimited 30 years	n/a	n/a	n/a
AAA	£4m 5 years	£8m 20 years	£8m 30 years	£4m 20 years	£4m 20 years	£4m 20 years
AA+	£4m 5 years	£8m 10 years	£8m 25 years	£4m 10 years	£4m 10 years	£4m 10 years
AA	£4m 4 years	£8m 5 years	£8m 15 years	£4m 5 years	£4m 10 years	£4m 10 years
AA-	£4m 3 years	£8m 4 years	£8m 10 years	£4m 4 years	£4m 10 years	£4m 10 years
A+	£4m 2 years	£8m 3 years	£4m 5 years	£4m 3 years	£4m 5 years	£4m 5 years
A	£4m 13 months	£8m 2 years	£4m 5 years	£4m 2 years	£4m 5 years	£4m 5 years
A-	£m 6 months	£8m 13 months	£4m 5 years	£4m 13 months	£4m 5 years	£4m 5 years
BBB+	£2m 100 days	£4m 6 months	£2m 2 years	£2m 6 months	£2m 2 years	£2m 2 years
None	£1m 6 months	n/a	£4m 25 years	n/a	£4m 5 years	£4m 25 years
Pooled funds	£8m per fund					

This table must be read in conjunction with the notes below

5.8. Credit Rating

Investment limits are set by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

5.9. Banks Unsecured

Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail.

5.10. Banks Secured

Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

5.11. Government

Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 30 years.

5.12. Corporates

Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent.

5.13. Registered Providers

Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services, they retain the likelihood of receiving government support if needed.

5.14. Pooled Funds

Shares in diversified investment vehicles consisting of any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity and very low or no volatility will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Depending on the type of pooled fund invested in, it may have to be classified as capital expenditure. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

5.15. Risk Assessment and Credit Ratings

Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be recalled or sold at no cost will be, and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

5.16. Other Information on the Security of Investments

The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

Based on the available information and the advice of the Council's advisers, Arlingclose, the investment limits shown in Table 5 and 6 may be reduced, and investing with certain counterparties may be suspended as necessary.

If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

5.17. Specified Investments

The CLG Guidance defines specified investments as those:

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement,
- not defined as capital expenditure by legislation, and
- invested with one of:
  - the UK Government,
  - a UK local authority, parish council or community council, or
  - a body or investment scheme of "high credit quality".

The Council defines "high credit quality" organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds "high credit quality" is defined as those having a credit rating of A- or higher.

5.18. Non-specified Investments

Any investment not meeting the definition of a specified investment is classed as non-specified. The Council does not intend to make any investments denominated in foreign currencies. Non-specified investments will therefore be limited to long-term investments, (i.e. those that are due to mature 12 months or longer from the date of arrangement), pooled funds that the Council intends to hold as long-term investments (for more than one year) and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in Table 7 below.

Table 7: Non-Specified Investment Limits	Cash limit
Total long-term investments	£25m
Total investments without credit ratings or rated below A- (excluding investments with other local authorities)	£20m
Total non-Sterling investments	£0m
Total investments in foreign countries rated below AA+	£0m
Total non-specified investments	£30m*

* Total non-specified investments is a limit in its own right, and is not meant to equal the aggregate of the limits for total long-term investments, and total investments without credit ratings or rates below A-.

5.19. Liquidity Management

The Council has due regard for its future cash flows when determining the maximum period for which funds may prudently be committed. Historic cash flows are analysed in addition to significant future cash movements, such as payroll, grant income and council tax precept. Limits on long-term investments are set by reference to the Council's medium term financial position (summarised in Table 1) and forecast short-term balances.

6. Treasury Management Indicators

6.1. The Council measures and manages its exposures to treasury management risks using the following indicators.

6.2. Interest Rate Exposures

This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the amount of principal borrowed or invested will be:

Table 8: Interest Rate Exposures	2017/18	2018/19	2019/20
Upper limit on fixed interest rate investment exposure	£25m	£25m	£25m
Upper limit on variable interest rate investment exposure	£90m	£90m	£90m
Upper limit on fixed interest rate borrowing exposure	£174.4m	£170.8m	£168.1m
Upper limit on variable interest rate borrowing exposure	£174.4m	£170.8m	£168.1m

Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. All other instruments are classed as variable rate.

6.3. Maturity Structure of Borrowing

This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing will be:

Table 9: Maturity Structure of Borrowing	Upper	Lower
Under 12 months	25%	0%
12 months and within 24 months	25%	0%
24 months and within 5 years	25%	0%
5 years and within 10 years	25%	0%
10 years and above	100%	0%

6.4. Principal Sums Invested for Periods Longer than 364 days

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end will be:

Table 10: Principal Sums Invested for Periods Longer than 364 days	2017/18	2018/19	2019/20
Limit on principal invested beyond year end	£25m	£25m	£25m

7. Other Items

7.1. There are a number of additional items that the Council is obliged by CIPFA or CLG to include in its Treasury Management Strategy.

7.2. Policy on Use of Financial Derivatives

Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

7.3. Policy on Apportioning Interest to the HRA

On 1st April 2012, the Council notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/credited to the respective revenue account. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured each month and interest transferred between the General Fund and HRA at the average % Local Authority 7 day rate.

7.4. Investment Training

The needs of Hampshire County Council's treasury management staff delivery services to New Forest District Council, for training in investment management are assessed annually as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change.

Staff members regularly attend training courses, seminars and conferences provided by Arlingclose and CIPFA. Relevant staff members are also encouraged to study professional qualifications from CIPFA, and other appropriate organisations.

CIPFA's Code of Practice requires that the Council ensures that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. All members were invited to a workshop presented by Arlingclose on 29 November 2016, which gave an update on treasury matters. A further Arlingclose workshop has been planned for 29 November 2017.

7.5. Investment Advisers

The Council has appointed Arlingclose Limited as treasury management advisers and receives specific advice on investment, debt and capital finance issues. The quality of this service is controlled through quarterly review meetings with Arlingclose.

7.6. Investment of Money Borrowed in Advance of Need

The Council may, from time to time, borrow in advance of need, where this is expected to provide the best long term value for money. Since amounts borrowed will be invested until spent, the Council is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the

Council's overall management of its treasury risks. The total amount borrowed will not exceed the authorised borrowing limit of £174.4 million.

ARLINGCLOSE ECONOMIC & INTEREST RATE FORECAST NOVEMBER 2016

Underlying assumptions:

- The medium term outlook for the UK economy is dominated by the negotiations to leave the EU. The long-term position of the UK economy will be largely dependent on the agreements the government is able to secure with the EU and other countries.

- The global environment is also riddled with uncertainty, with repercussions for financial market volatility and long-term interest rates. Donald Trump's victory in the US general election and Brexit are symptomatic of the popular disaffection with globalisation trends. The potential rise in protectionism could dampen global growth prospects and therefore inflation. Financial market volatility will remain the norm for some time.

- However, following significant global fiscal and monetary stimulus, the short term outlook for the global economy is somewhat brighter than earlier in the year. US fiscal stimulus is also a possibility following Trump's victory.

- Recent data present a more positive picture for the post-Referendum UK economy than predicted due to continued strong household spending.

- Over the medium term, economic and political uncertainty will likely dampen investment intentions and tighten credit availability, prompting lower activity levels and potentially a rise in unemployment.

- The currency-led rise in CPI inflation (currently 1.0% year/year) will continue, breaching the target in 2017, which will act to slow real growth in household spending due to a sharp decline in real wage growth.

- The depreciation in sterling will, however, assist the economy to rebalance away from spending. The negative contribution from net trade to GDP growth is likely to diminish, largely due to weaker domestic demand. Export volumes will increase marginally.

- Given the pressure on household spending and business investment, the rise in inflation is highly unlikely to prompt monetary tightening by the Bank of England, with policymakers looking through import-led CPI spikes to the negative effects of Brexit on economic activity and, ultimately, inflation.

- Bank of England policymakers have, however, highlighted that excessive levels of inflation will not be tolerated for sustained periods. Given this view and the current inflation outlook, further monetary loosening looks less likely.

Forecast:

- Globally, the outlook is uncertain and risks remain weighted to the downside. The UK domestic outlook is uncertain, but likely to be weaker in the short term than previously expected.

- The likely path for Bank Rate is weighted to the downside. The Arlingclose central case is for Bank Rate to remain at 0.25%, but there is a 25% possibility of a drop to close to zero, with a very small chance of a reduction below zero.

- Gilt yields have risen sharply, but remain at low levels. The Arlingclose central case is for yields to decline when the government triggers Article 50.

	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Ave
Official Bank Rate														
Upside risk	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	**0.12**
Arlingclose Central Case	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**
Downside risk	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	**0.40**
3-month LIBID rate														
Upside risk	0.05	0.05	0.10	0.10	0.10	0.15	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.18**
Arlingclose Central Case	**0.25**	**0.25**	**0.25**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.29**
Downside risk	0.20	0.25	0.25	0.25	0.30	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.34**
1-yr LIBID rate														
Upside risk	0.10	0.10	0.15	0.15	0.15	0.20	0.30	0.30	0.30	0.30	0.30	0.30	0.30	**0.23**
Arlingclose Central Case	**0.60**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.60**	**0.70**	**0.85**	**0.90**	**0.90**	**0.90**	**0.65**
Downside risk	0.10	0.15	0.15	0.15	0.20	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	**0.24**
5-yr gilt yield														
Upside risk	0.25	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.39**
Arlingclose Central Case	**0.50**	**0.40**	**0.35**	**0.35**	**0.35**	**0.40**	**0.40**	**0.40**	**0.45**	**0.50**	**0.55**	**0.60**	**0.65**	**0.45**
Downside risk	0.30	0.45	0.45	0.45	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	**0.47**
10-yr gilt yield														
Upside risk	0.30	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.39**
Arlingclose Central Case	**1.15**	**0.95**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.90**	**0.95**	**1.00**	**1.05**	**1.10**	**1.15**	**0.96**
Downside risk	0.30	0.45	0.45	0.45	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	**0.47**
20-yr gilt yield														
Upside risk	0.25	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.39**
Arlingclose Central Case	**1.70**	**1.50**	**1.40**	**1.40**	**1.40**	**1.40**	**1.40**	**1.45**	**1.50**	**1.55**	**1.60**	**1.65**	**1.70**	**1.75**
Downside risk	0.40	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	**0.57**
50-yr gilt yield														
Upside risk	0.25	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.39**
Arlingclose Central Case	**1.60**	**1.40**	**1.30**	**1.30**	**1.30**	**1.30**	**1.30**	**1.35**	**1.40**	**1.45**	**1.50**	**1.55**	**1.60**	**1.41**
Downside risk	0.40	0.55	0.55	0.55	0.55	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	**0.57**

EXISTING INVESTMENT & DEBT PORTFOLIO POSITION AT 31 DECEMBER 2016

Investments **Duration to maturity**	**Overnight** **£m**	**<1 year** **£m**	**>1 year** **£m**	**Total** **£m**	**Average rate/yield** **%**	**Average life** **(years)**
Subject to bail-in risk						
Bank call accounts	0.5	0.0	0.0	0.5	0.20%	0.0
Bank notice accounts	2.0	0.0	0.0	2.0	0.80%	0.3
Certificates of deposit[1]	0.0	9.0	0.0	9.0	0.40%	0.1
Money market funds[2]	20.0	0.0	0.0	20.0	0.27%	0.0
	22.5	**9.0**	**0.0**	**31.5**	**0.34%**	**0.1**
Exempt from bail-in risk						
Covered floating rate notes	0.0	12.5	6.5	19.0	0.65%	1.0
Covered fixed bonds	0.0	0.0	2.0	2.0	1.30%	1.3
Corporate floating rate notes	0.0	1.0	0.0	1.0	0.67%	0.1
Corporate fixed bonds	0.0	2.9	0.0	2.9	0.50%	0.2
Local authorities	0.0	14.0	3.0	17.0	0.87%	0.7
	0.0	**30.4**	**11.5**	**41.9**	**0.76%**	**0.8**
Targeting higher yields						
Pooled property funds[3]	0.0	0.0	3.1	3.1	4.67%	n/a
Pooled equity funds[4]	0.0	0.0	1.3	1.3	6.93%	n/a
	0.0	**0.0**	**4.4**	**4.4**	**5.35%**	**n/a**
Total	**22.5**	**39.4**	**15.9**	**77.8**	**0.85%**	**0.5**

	£m	**%**
External Borrowing:		
PWLB Fixed Rate	(144.2)	(3.12)
Total Gross External Debt	**(144.2)**	**(3.12)**
Investments	**77.8**	**0.85**
Net (Debt) / Investments	**(66.4)**	

[1] Certificates of deposit are financial instruments that have the ability of being sold on the secondary market.
[2] Money market funds have a reduced risk of bail-in due to the portfolio of investments each fund is invested in.
[3] The average rate/yield provided for the pooled property funds is the average income return per annum.
[4] The Council invested in the pooled equity funds part-way through the year, therefore the average rate/yield is the income return for the investment period, annualised. A more accurate representation of expected income return will be available once the Council are invested for a full year.