City of Westminster

Cabinet

Decision Maker	Cabinet
Date:	15 October 2018
Status:	General Release
Title:	Treasury Management Strategy Statement for 2019/20 to 2023/24
Wards Affected:	All
Policy Context:	To manage the Council's finances prudently and efficiently.
Cabinet Member	Cabinet Member for Finance, Property and Regeneration
Financial Summary:	The Annual Treasury Management Strategy Statement sets out the Council's strategy for ensuring that: a. its capital investment plans are prudent, affordable and sustainable; b. the financing of the Council's capital programme and ensuring that cash flow is properly planned; c. cash balances are appropriately invested to generate optimum returns having regard to security and liquidity of capital.
Report of:	Steven Mair, City Treasurer smair@westminster.gov.uk 020 7641 2904

1. EXECUTIVE SUMMARY

1.1 The Local Government Act 2003 requires the Council to ‘have regard to’ the Prudential Code for Capital Finance in Local Authorities and to set Prudential Indicators for the next three years to ensure that the Council’s capital investment plans are affordable, prudent and sustainable. These are contained within this report.

1.2 The Act also requires the Council to set out a statement of its treasury management strategy for borrowing and to prepare an Annual Investment Strategy (as shown in Appendix 1). This sets out the Council’s policies for managing its investments and for giving priority to the security and liquidity of those investments. The Treasury Management Strategy Statement and Annual Investment Strategy must both have regard to guidance issued by the DCLG and must be agreed by the full Council.

1.3 This report sets out the Council’s proposed Treasury Management Strategy Statement (TMSS) for the period 2019/20 to 2023/24, and Annual Investment Strategy (AIS) for the year ended 31 March 2020, together with supporting information.

1.4 The TMSS and AIS form part of the Council’s overall budget setting and financial framework, and will be finalised and updated as work on the Council’s 2019/20 budget is progressed in January and February 2019.

2. RECOMMENDATIONS

2.1 The Cabinet is asked to approve:

- the Treasury Management Strategy Statement;
- the borrowing strategy and borrowing limits for 2019/20 to 2023/24 set out in sections 5 to 7;
- the prudential Indicators set out in section 8;
- the Annual Investment strategy and approved investments set out in Appendix 1;
- the Minimum Revenue Provision Policy set out in Appendix 2.

3. REASONS FOR DECISIONS

3.1 To comply with the Local Government Act 2003, other regulations and guidance and to ensure that the Council’s borrowing and investment plans are prudent, affordable and sustainable and comply with statutory requirements.

4. BACKGROUND INFORMATION

4.1 The Council is required to operate a balanced budget, which broadly means that monies received during the year will cover expenditure. The function of treasury management is to ensure that:

- the Council’s capital programme and corporate investment plans are adequately funded;

- cash is available when it is needed on a day to day basis, to discharge the Council’s legal obligations and deliver Council services;

- surplus monies are invested securely and wisely.

4.2 The Council has formally adopted CIPFA's Code of Practice on Treasury Management, and follows the key requirements of the Code as set out in Appendix 3.

4.3 The TMSS covers three main areas summarised below:

4.3.1 Capital spending

- Capital spending plans
- Other investment opportunities
- Capital Finance Requirement (CFR)
- Affordability
- The Minimum Revenue Provision (MRP) policy (Appendix 2)

4.3.2 Borrowing

- Overall borrowing strategy
- Prospect for interest rates
- Limits on external borrowing
- Maturity structure of borrowing
- Policy on borrowing in advance of need
- Forward Borrowing
- Debt rescheduling

4.3.3 Managing cash balances

- The current cash position and cash flow forecast
- Prospects for investment returns
- Council policy on investing and managing risk
- Balancing short and longer term investments
- Improving investment returns

4.4 The Annual Investment Strategy (AIS) at Appendix 1 provides more detail on how the Council's surplus cash investments are to be managed in 2019/20. Approved schedules of specified and non-specified investments will be updated following consideration by Members and finalisation of 2019/20 budget plans.

TREASURY MANAGEMENT STRATEGY STATEMENT

5. SECTION 1 - CAPITAL SPENDING

Capital spending plans

5.1 Table 1 summarises the Council's capital expenditure plans, both in terms of those agreed previously, and those forming part of the current budget cycle. The table sets out the Council's current expectations reference the revenue or capital financing.

5.2 Compared with the forecast in the original 2018/19 TMSS, General Fund capital spend has slipped back by around £139m in 2018/19 revised budget and there remains an element of further slippage in future years. The risks are that:

- continued slippage in new starts will push borrowing requirements to later years when interest rates are forecast to be higher than currently;
- slippage in the programme of capital receipts may increase the need to borrow in the medium-term.

Table 1 Capital spending and funding plans

2017/18		2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	Total
Actual		Forecast	Estimate	Estimate	Estimate	Estimate	Estimate	
£m		£m	£m	£m	£m	£m	£m	£m
	Expenditure							
235	General Fund	305	344	341	329	225	132	1,676
82	HRA	126	182	151	112	134	83	788
317		**431**	**526**	**492**	**441**	**359**	**215**	**2,464**
	Funding							
	General Fund							
93	Grants & Contributions	135	71	55	20	17	12	310
23	Capital Receipts Applied	96	0	48	43	9	194	390
	HRA							
11	Grants & Contributions	24	45	28	18	40	3	**158**
32	Capital Receipts Applied	45	55	60	71	70	57	**358**
23	Major Repairs Reserve	23	23	243	23	24	23	**140**
16	Revenue Financing	34	12	15	0	0	0	**61**

198		357	206	230	175	160	289	1,417
119	Net financing need for the year	74	320	262	266	199	(74)	1,047

Other investment opportunities

5.3 As well as investing in assets owned by the Council and used in the delivery of services, the Council also invests, where appropriate, in:

- infrastructure projects, such as green energy;
- loans to third parties;
- shareholdings in limited companies and joint ventures.

5.4 Such investments are treated as expenditure for treasury management and prudential borrowing purposes even though they do not create physical assets in the Council's accounts. Appropriate budgets in respect of these activities are agreed as part of the Council's budget setting and ongoing monitoring processes and considered as part of the Investment Strategy.

5.5 In addition the Council has a substantial commercial property portfolio which forms part of the investment strategy. In previous years, the Council has invested in traditional asset classes of offices, retail and industrial/logistics, which meet the Council's requirements for the income to be secure and reliable and the investments low risk.

5.6 Following a Cabinet decision in late 2015, the Council allocated funds to invest in commercial property partnership fund that commenced in 2016/17 (£50m) and 2017/18 (£50m). The aim is to diversify the property portfolio into sectors that have historically been considered alternatives but are increasingly being viewed as mainstream. The strategy focuses on increasing the income generated by the Council from its property holdings, while also meeting statutory service requirements and improving the quality of the Council's current portfolio.

5.7 The Council has also invested £15m (2017/18), with a further £15m approved in 2018/19 within the overall context of the Council's annual investment strategy in a residential housing partnership with LB Lambeth and LB Croydon.

Capital Financing Requirement (CFR)

5.8 The CFR measures the extent to which capital expenditure has not yet been financed from either revenue or capital resources. Essentially it measures the Council's underlying borrowing need. Each year, the CFR will increase by the amounts of new capital expenditure not immediately financed.

5.9 Table 2 overleaf shows that the CFR will increase over the medium term. Consequently, the capital financing charge to revenue will increase, reflecting the capital spending plans.

Table 2 Capital Financing Requirement forecast

2017/18 Actual £m		2018/19 Forecast £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
	CFR as at 31 March						
373	General Fund	446	719	957	1,223	1,422	1,348
261	HRA	261	308	333	333	332	333
634		**707**	**1,027**	**1,290**	**1,556**	**1,754**	**1,681**
	Annual Charge						
119	General Fund	74	273	238	266	199	(74)
(0)	HRA	0	47	24	0	0	(0)
119		**74**	**320**	**262**	**266**	**199**	**(74)**
	Reason for Change						
126	Net financing	76	327	273	281	223	(49)
(7)	Less MRP	(3)	(7)	(11)	(15)	(24)	(26)
119		**74**	**320**	**262**	**266**	**199**	**(74)**

5.10 Table 3 below confirms that the Council's gross debt does not exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for current year 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.

Table 3 Borrowing compared to the Capital Financing Requirement

2017/18 Actual £m		2018/19 Forecast £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
251	Gross Projected Debt	223	223	208	448	682	672
634	Capital Financing Requirement	708	1,028	1,290	1,556	1,755	1,681
383	**Under / (over) borrowing**	**485**	**805**	**1,082**	**1,108**	**1,073**	**1,009**

Affordability

5.11 The objective of the affordability indicators is to ensure that the level of investment in capital assets proposed remains within sustainable limits and, in particular, the impact on the Council's "bottom line". Table 4 below sets out the expected ratio of capital financing costs to income for both General Fund and HRA activities:

Table 4 Ratio of capital financing costs to income

2017/18 Actual %		2018/19 Forecast %	2019/20 Estimate %	2020/21 Estimate %	2021/22 Estimate %	2022/23 Estimate %	2023/24 Estimate %
0.68	General Fund	(3.38)	(2.33)	(0.61)	5.74	15.17	17.28
30.11	HRA	30.31	30.77	31.82	31.92	30.50	31.02

5.12 For the next two years, gross capital financing charges (loan interest, MRP and finance and PFI payments) for the General Fund capital programme are largely outweighed or balanced by income from investments and the commercial property portfolio. However, in future years the Council will begin to incur increasing capital financing charges in line with the forecast increase in the General Fund CFR in Table 2.

5.13 The capital financing charges arising from the HRA capital programme increase in line with the forecast increase income, hence capital charges as a proportion of the HRA net revenue stream remain fairly steady.

6. SECTION 2 - BORROWING

Overall borrowing strategy

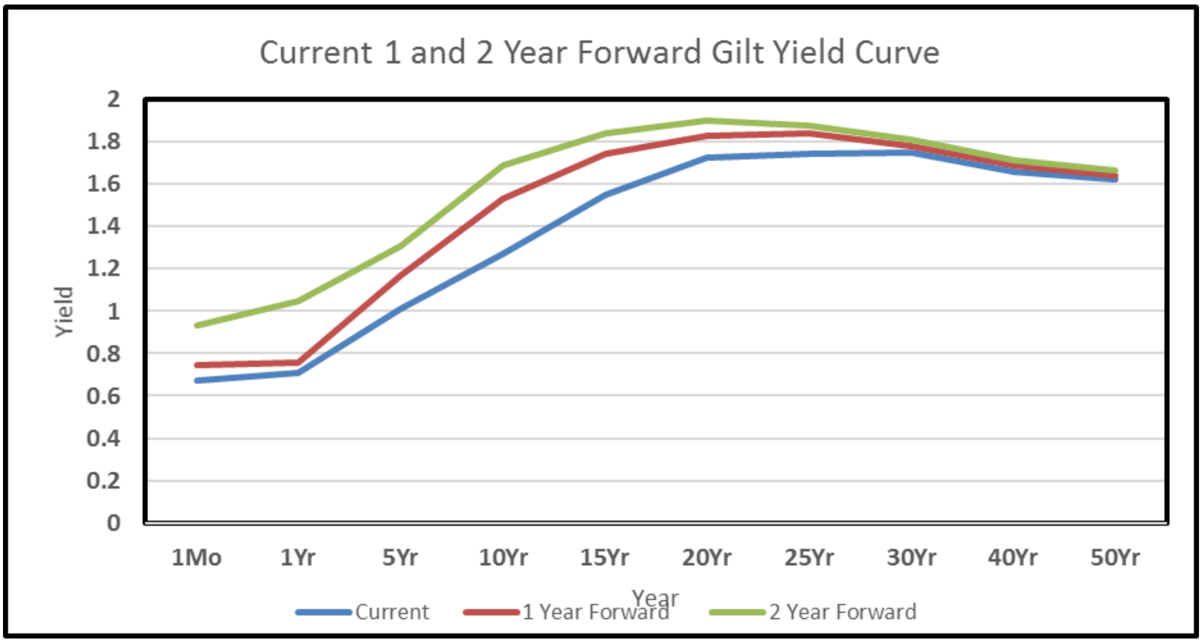
6.1 The Council's main objective when borrowing money is to strike an appropriate balance between securing low interest costs and achieving cost certainty over the period for which funds are required. Given the significant cuts to public expenditure and, in particular, to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the long-term stability of the debt portfolio. The key factors influencing the 2019/20 strategy are:

- forecast borrowing requirements,
- the current economic and market environment, and
- interest rate forecasts.

6.2 The Council is currently maintaining an under-borrowed position. This means that capital expenditure has not been fully funded from loan debt as other funding streams (such as government grants and third party contributions, use of Council reserves and cash balances and capital receipts) have been employed where available. This policy has served the Council well over the last few years while investment returns have been low and counterparty risk has been relatively high.

Prospects for Interest Rates

6. 3 The borrowing position needs to be kept under review to avoid incurring higher borrowing costs in future years when the Council may not be able to avoid new borrowing to finance capital expenditure and/or to refinance maturing debt. Market commentators are forecasting no increase in interest rates across all maturities for 12 months (see graph below). Any increase is then predicted to be gradual 0.25% increases rather than a material change. More detail on their interest rate forecasts is at Appendix 4.



Source: Bloomberg

6.4 Against this background and the risks within the economic forecast, caution will be adopted with the 2019/20 and beyond treasury borrowing decisions. The Treasury Management team will continue to monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances (within their approved remit).

6.5 If it were considered 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), long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

6.6 In the event that interest rates rose beyond the forecast used in the capital programme, the revenue interest cost to the Council would increase. A rise of an extra 1% per year during the Council's peak borrowing period of 2021/22 to 2022/23 would cost an additional £4.7m in interest payments per annum from 2023/24.

Table 5 The Council's balance sheet position at 31 March 2018

	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
	£m	£m	£m	£m	£m	£m	£m
Capital Financing Requirement (CFR)	**634**	**708**	**1,028**	**1,290**	**1,556**	**1,755**	**1,681**
Other Long term liabilities							
Service concessions	(9)	(8)	(7)	(7)	(6)	(6)	(6)
Leases	(47)	(46)	(45)	(44)	(43)	(43)	(42)
Underlying Borrowing Requirement	**578**	**654**	**976**	**1,239**	**1,507**	**1,706**	**1,633**
External Borrowing*	251	223	223	208	448	682	672
Under borrowing /Internal borrowing	**327**	**430**	**752**	**1,031**	**1,059**	**1,024**	**961**

Service concessions (note 25 2018/19 accounts). Leases relates to car parking at City Hall/Portman Square.

Limits on external borrowing

6.7 The Prudential Code requires the Council to set two limits on its total external debt, as set out in Table 6 below. The Authorised Limit has been increased in line with the CFR. The limits are:

- **Authorised Limit for External Debt (Prudential Indicator 6a)** – This is the limit prescribed by section 3(1) of the Local Government Act 2003 representing the maximum level of borrowing which the Council may incur. It reflects the level of external debt which, while not desired, could be afforded in the short term, but may not be sustainable in the longer term.

- **Operational Boundary (Prudential Indicator 6b)** – This is the limit which external debt is not normally expected to exceed. The boundary is based on current debt plus anticipated net financing need for future years.

Table 6 Overall borrowing limits

2017/18 Actual £m		2018/19 Forecast £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
	Authorised Limit:						
634	**Borrowing and other long term liabilities**	**708**	**1,028**	**1,290**	**1,556**	**1,755**	**1,681**
	Operational Boundary:						
251	Borrowing	223	223	208	448	682	672
56	Other long term liabilities	54	52	51	50	48	47
307	**Operational Boundary**	**277**	**275**	**259**	**498**	**730**	**719**

6.8 In addition, borrowing for the HRA has to remain within the HRA Debt Limit (prescribed in the HRA Self-Financing Determinations 2012) as detailed in the table below. Borrowing for the HRA is measured by the HRA CFR.

Table 7 HRA borrowing

2017/18 Actual £m		2018/19 Forecast £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
334	HRA Debt Limit	334	334	334	334	334	334
261	HRA CFR	261	308	333	333	333	333
73	**Headroom**	**73**	**25**	**1**	**1**	**1**	**1**

6.9 The City Treasurer reports that the Council complied with these indicators in the current year and does not envisage difficulties for the future.

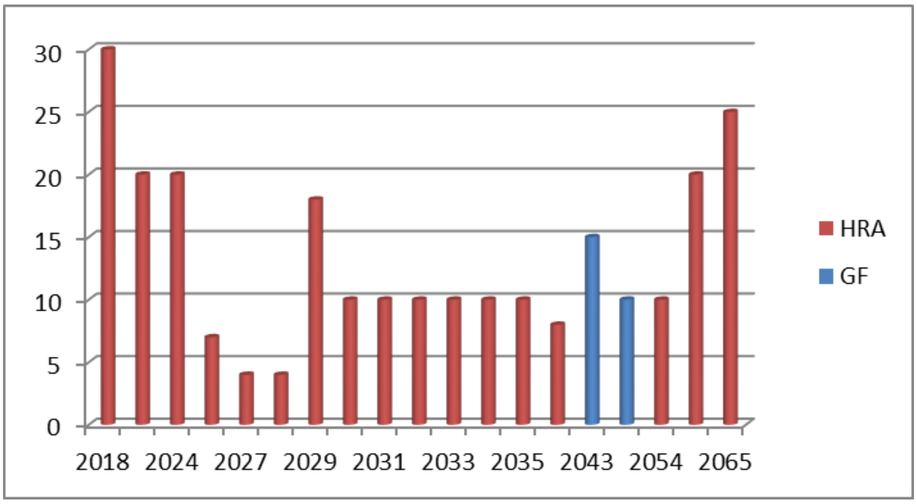
Maturity structure of borrowing (Prudential Indicator 9)

6.10 Managing the profile of when debt matures is essential for ensuring that the Council is not exposed to large fixed rate sums falling due for refinancing within a short period, and thus potentially exposing the Council to additional cost. Table 8 below sets out current upper and lower limits for debt maturity which are unchanged from 2018/19. The chart below shows the principal repayment profile for current council borrowing remains within these limits.

Table 8 Debt maturity profile limits

Actual Maturity at 31 December 2018	Duration	Upper Limit	Lower Limit
0	Under 12 months	40	0
0	12 Months and within 24 Months	35	0
9	24 Months and within 5 years	35	0
16	5 Years and Within 10 Years	50	0
100	10 Years and Above	100	35

Maturity profile of long-term borrowing



6.11 The Council has £70 million of LOBO (Lender Option Borrower Option) debt, none of which matures in the near future. Were the lender to exercise their option, officers will consider accepting the new rate of interest or repaying (with no penalty). Repayment of the LOBO may result in a need for refinancing.

6.12 In the event that there is a much sharper rise in long and short term rates than currently forecast, then the balance of the loan portfolio will be revisited with a view to taking on longer term fixed rate borrowing in anticipation of future rate rises.

Policy on Borrowing in Advance of Need

6.13 The Council has the power to borrow in advance of need in line with its future borrowing requirements under the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended. 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.

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

Forward Borrowing

6.15 The Council's net funding requirement is expected to be in the region of £1.9bn over the next ten to 15 years, due to the planned extensive capital programme (see Table

1). This requirement is net of all revenue contributions, grants and capital receipts expected to be applied. The capital programme report, elsewhere on the agenda, seeks approval to go ahead with this.

6.16 Currently, the cost of borrowing is close to all-time lows and the Council can afford to borrow at fixed interest rates. There is uncertainty about how interest rates may move in the future, with the first rate rise since 2007 having occurred on 2 November 2017 and a further rise on 2 August 2018. The current market position does not expect any dramatic interest rate movements in the short term and there is still the potential for interest rates to fall back again in the future, given economic uncertainty surrounding the UK exiting from the European Union.

6.17 The Council has the ability to borrow at a future date for an agreed price now. This is appropriate for when the Council knows that it will be required to borrow in the future and wishes to lock in certainty of interest rate cost. The reason for doing this is that the cost of borrowing can fluctuate and may increase for the Council over a period of time. The Council will incorporate this option as part of a wider borrowing strategy, and will elect to forward borrow if it deems it to be a value for money option.

6.18 A balance will need to be struck between locking in affordability over the medium term to protect against interest rate rises, but not to borrow unnecessarily early, placing undue interest expense on the general fund. The key factors will be the potential trajectory of future interest rates changes and aligning the cash flow forecast with the expected capital spend, thus looking at where future borrowing needs will arise. The net cost of the interest on any loans that are not yet deployed to funding expenditure is known as “the cost of carry” and it is the Council’s intention to minimise this as far as possible.

Debt Rescheduling

6.19 As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be 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 cost of debt repayment (premiums incurred).

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

- generating cash savings and / or discounted cash flow savings;
- helping to fulfil the treasury strategy; and
- enhancing the balance of the portfolio by amending the maturity profile and/or the balance of volatility.

6.21 Consideration will also be given to identifying the 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.

6.22 Any rescheduling will be reported.

7. SECTION 3 - MANAGING CASH BALANCES

The current cash position and cash flow forecast

7.1 Table 9 below shows that cash balances have increased by £146m in the past five months which is mainly due to income such as council tax, business rates and grants received in advance. This is expected to be closer to £1bn by year end.

Table 9 Cash position at 31 July 2018

As at 31 March 2018			As at 31 August 2018	
Principal	Average Rate		Principal	Average Rate
£m	%		0	%
		Investments		
992	0.56	Specified	1,138	0.85
0	0.00	Non-Specified	0	0
992	**1**	**Total**	**1,138**	
		Borrowing		
181	4.75	Public works loan Board	153	3.85
70	5.08	Market Loans	70	5.08
251		**Total**	**223**	

7.2 The medium-term cash flow forecast (see below) shows that the Council has a substantial positive cash flow position with an average cash position fluctuating around £500m for the medium-term. The reason for the high cash balance is largely due to capital program slippage and business rates and the amount held pending rating appeals of which are uncertain, and have been excluded from the table below.

Table 10 Medium-term cashflow forecast

	2018/19 Forecast £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
Balance at 1 April	**992**	**906**	**403**	**75**	**(3)**	**(69)**
Movement in Cash						
Capital Receipt	141	55	108	114	79	251
Grants & Contributions	159	116	83	38	57	15
Revenue Financing / MRR	57	35	39	23	24	23
Cash In	**357**	**206**	**230**	**175**	**160**	**289**
Other Cash movements	66	(175)	(45)	(149)	(52)	54
HRA cash movements	(48)	(8)	(6)	77	(14)	1
Capital Programme	(431)	(526)	(492)	(441)	(359)	(215)
Cash Out	**(413)**	**(709)**	**(543)**	**(513)**	**(425)**	**(160)**
Borrowing	0	0	0	266	199	0
Repayment of debt	(30)	0	(15)	(5)	0	(10)
Balance 31 March	**906**	**403**	**75**	**(3)**	**(69)**	**50**
Average Balance	**949**	**655**	**239**	**36**	**(36)**	**(9)**

7.3 The Council aims to manage daily cash flow peaks and troughs to achieve a nil current account balance throughout the year. As such the average yearly surplus cash balances should be fully invested throughout.

Prospects for investment returns

7.4 Investment returns on cash-based deposits are likely to increase slightly in 2019/20 and beyond, on the back drop of the bank base rate rising to 0.75% on 2 August 2018. Borrowing interest rates are on a slight increased trend over the next few years; they fell sharply to historically low levels after the EU exit referendum and then even further after the MPC meeting of August 2016 when a new package of quantitative easing purchasing of gilts was announced. As inflationary pressures have mounted in the past year, the prospect of further interest rate rises have now increased. However, despite the 2 August 2018 Bank of England increase of the base rate from 0.50% to 0.75%, the PWLB 50-year loan rate has stayed steady at around 2.50%.

7.5 Gilt yields could turn volatile over concerns around a ‘hard Brexit’ (arising from no trade deal with the EU), any resultant fall in the value of sterling, and an increase in inflation expectations. The Council is therefore committed to investigating asset backed securities (ABS) and other alternatives to cash based investments where it is considered prudent to do so.

Council policy on investing and managing risk

7.6 The aim is to manage risk and reduce the impact of any adverse movement in interest rates on the one hand but, at the same time, not setting the limits to be so restrictive that they impair opportunities to reduce costs or improve performance.

Balancing short and longer term investments

7.7 During the first half of 2018/19, there were no investment of surplus funds exceeding 364 days. This means the Council remains well within the upper limit for such investments of £450m.

Table 11 Investment limit

2017/18 Actual £m		2018/19 Forecast £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
	Upper limit for fixed interest rate exposure						
634	Net principal re fixed rate borrowing	708	1,028	1,290	1,556	1,755	1,681
	Upper Limit for variable rate exposure						
0	Net Principal for variable rate borrowing	0	0	0	0	0	0
73	Upper Limit for principal sums invested for more the 364 days	450	450	450	450	450	450

Improving Investment Returns

7.8 An Investment Executive was set up to ensure that the Council made best use of its resources and ensure value for money was being achieved in its investment strategy. The task force contains both Council Members and Officers.

7.9 The task force met on 3 September 2018 to perform an in depth review on the Council's wider investment framework document and provide suggestions improvements. The review looked at the council's property portfolio, short and long term treasury investments, governance arrangements and the impact of investing in the pension fund.

7.10 As part of the meeting, the following recommendations were made (all conform to the existing 2018/19 TMSS):

- With regard to the treasury portfolio, to agree the increased allocation to local authorities, on the basis that local authorities were more secure counterparties than UK or overseas banks. Prior to agreement with a local authority, a due diligence process will analyse the latest accounts, external audit opinion, monitoring statements and reputational issues arising from media comment or press releases.

- To agree to change the allocation (greater amount) for liquid funds (up to 12 months) and longer term cash investment (lower amount). Given the cash flow requirements dictated by the capital programme, the agreement of the Investment Executive was to move from 10% to 44% reference the more liquid aspects of the portfolio. And alternatives to move from 40% to 13%.

- To agree to proposed changes to the investment strategy using a two-year time period, with security and liquidity utmost in the investment process, prioritised over yield.

7.11 These recommendations remain under review in relation to the investment framework and investment governance arrangements going forward.

7.12 The Task Force will meet on a quarterly basis.

8. SUMMARY OF PRUDENTIAL INDICATORS (PIs)

8.1 The purpose of prudential indicators (PIs) is to provide a reference point or “dashboard” so that senior officers and Members can:

- easily identify whether approved treasury management policies are being applied correctly in practice and

- take corrective action as required.

8.2 As the Council’s S151 officer, the City Treasurer has a responsibility to ensure that appropriate PIs are set and monitored and that any breaches are reported to Members.

8.3 The City Treasurer has confirmed that the PIs set out below are all expected to be complied with in 2018/19 and he does not envisage at this stage that there will be any difficulty in achieving compliance with the suggested indicators for 2019/20.

PI ref	Para ref		2017/18 Actual	2018/19 forecast	2019/20 proposed
1	5.2	Capital expenditure	£317m	£431m	£526m
2	5.8	Capital Financing Requirement (CFR)	£634m	£707m	£1,027m
3	5.9	Net debt vs CFR	£383m underborrowing	£485m underborrowing	£805m underborrowing
4	5.10	Ratio of financing costs to revenue stream	GF 0.68% HRA 30.11%	GF (3.38)% HRA 30.31%	GF (2.33)% HRA 30.77%
5a	6.7	Authorised limit for external debt	£634m	£804m	£1,077m
5b	6.7	Operational debt boundary	£307m	£277m	£275m
5c	6.8	HRA debt limit	£334m	£334m	£334m
6	7.3	Working capital balance	£0m	£0m	£0m
7a	7.7	Upper limit for variable interest rate borrowing	£0m	£0m	£0m
7b	7.7	Upper limit for fixed interest rate borrowing	£634m	£708m	£1,028m
7c	7.7	Limit on surplus funds invested for more than 364 days (i.e. non-specified investments)	£450m	£450m	£450m
8	6.10	Maturity structure of borrowing	12% 68%	Upper limit under 12 months - 40% Lower limit 10 years and above - 35%	Upper limit under 12 months - 40% Lower limit 10 years and above - 35%

9. LEGAL IMPLICATIONS

9.1 The Director of Law comments that the legal requirements are set out in the 2003 Act, and in the subordinate legislation. The City Treasurer, as Section 151 officer, has confirmed (paragraph 8.3) that the PIs are expected to be met in the current year.

Legal comments added by Angela Hogan, Senior Solicitor, 020 7361 2211

10. APPENDICES

1 Annual Investment Strategy

2 Minimum Revenue Provision (MRP) Policy

3 CIPFA Requirements

4 Prospect for Interest Rates/ Economic Update

BACKGROUND PAPERS

Treasury Management Strategy Statement 2018/19 (Approved by Council March 2018)

1. Section 3 Local Government Act 2003

2. Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended

3. MHCLG Guidance on Minimum Revenue Provision (fourth edition) February 2018

4. MHCLG Capital Finance Guidance on Local Government Investments February 2018

5. CIPFA Prudential Code for Capital Finance in Local Authorities, 2017

6. CIPFA Treasury Management Code of Practice, 2017

If you have any queries about this Report or wish to inspect any of the Background Papers, please contact:

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APPENDIX 1

ANNUAL INVESTMENT STRATEGY

1. The Council holds significant invested funds, representing income received in advance of expenditure, balances and reserves. During the first half of the current year, the Council's average investment balance has been around £1,184m and the cash flow projections show this pattern is expected to continue in the forthcoming year. Investments are made with reference to the core balance, future cash flow requirements and the outlook for interest rates.

2. The Council's investment policy has regard to the DCLG's Guidance on Local Government Investments ("the Investment Guidance") and the 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, then yield.

3. In accordance with the above guidance and to minimise the risk to investments, the Council applies minimum acceptable credit criteria to generate a list of highly creditworthy counterparties which will provide security of investments, enable diversification and minimise risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

Investment returns expectations

4. The Bank Rate was cut in August 2016 from 0.50% to 0.25%. Subsequently the MPC has now increased the Bank Rate by 0.25% to 0.50% in November 2017 and a further 0.25% to 0.75% in August 2018. The question still remains as to whether or not they will stop at this point for a lengthy pause, or will launch into a series of further rate increases in 2019 and beyond as Brexit uncertainties remain. The Bank Rate forecasts for financial year ends (March) are:

   2018/19: 0.75%
   2019/20: 1.00%
   2020/21: 1.25%
   2021/22: 1.50%
   2022/23: 2.00%

5. The suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during each financial year are as follows

   2018/19: 0.75%
   2019/20: 0.75%
   2020/21: 1.00%
   2021/22: 1.25%
   2022/23: 1.50%

Investment time limits

6. This limit is set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment. For the year 2019/20, the proposed limit of investments for over 364 days is £450m as set out in table 11 of the TMSS.

Investment Policy

7. The Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to assess continually and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.

8. Other information sources used will include the financial press, share price and other such information pertaining to the banking sector to establish the most robust scrutiny process on the suitability of potential investment counterparties and the impact of Brexit on a potential counterparty.

Creditworthiness Policy

9. The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle, the Council will ensure that:

- it maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security and monitoring their security; and
- it has sufficient liquidity in its investments. For this purpose, it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

10. The City Treasurer will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to those which determine which types of investment instrument are either specified or non-specified as they provide an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

11. The Council takes into account the following relevant matters when proposing counterparties:

- the financial position and jurisdiction of the institution;
- the market pricing of credit default swaps[1] for the institution;
- any implicit or explicit Government support for the institution;
- Standard & Poor's, Moody's and Fitch's short and long term credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries; and
- core Tier 1 capital ratios[2].

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[1] Credit Default Swaps (CDS) are tradable instruments where the buyer receives a pay-out from the seller if the party to whom the CDS refers (often a financial institution) has a "credit event" (e.g. default, bankruptcy, etc.). The price of the CDS gives an indication to the market's view of likelihood – the higher the price the more likely the credit event.

[2] The Tier 1 capital ratio is the ratio of a bank's core equity capital to its total risk-weighted assets (RWA). Risk-weighted assets are the total of all assets held by the bank weighted by credit risk according to a formula determined by the Regulator (usually the country's central bank). Most central banks follow the Basel Committee on Banking Supervision (BCBS) guidelines in setting formulae for asset risk weights.

12. Changes to the credit rating will be monitored and in the event that a counterparty is downgraded and does not meet the minimum criteria specified in Appendix 1, the following action will be taken immediately:

- no new investments will be made;

- existing investments will be recalled if there are no penalties; and

- full consideration will be given to recall or sale of existing investments which would be liable to penalty clause.

Specified and Non-specified investments

13. The DCLG Guidance on Local Government Investments made under section 15(1) of the Local Government Act 2003, places restrictions on local authorities around the use of specified and non-specified investments. A specified investment is defined as an investment which satisfies all of the conditions below:

- the investment and any associated cash flows are denominated in sterling;
- the investment has a maximum maturity of one year;
- the investment is not defined as capital expenditure; and
- the investment is made with a body or in an investment scheme of high credit quality; or with the UK Government, a UK Local Authority or parish/community council.

14. A non-specified investment is any investment that does not meet all the conditions above. In addition to the long-term investments listed in the table at the end of Appendix 1, the following non-specified investments that the Council may make include:

- **Green Energy Bonds** - Investments in solar farms are a form of Green Energy Bonds that provide a secure enhanced yield. The investments are structured as unrated bonds and secured on the assets and contracts of solar and wind farms. Before proceeding with any such investment, internal and external due diligence will be undertaken in advance of investments covering the financial, planning and legal aspects.

- **Social Housing Bonds** – Various fund managers facilitate the raising of financing housing associations via bond issues. The investment is therefore asset backed and provides enhanced returns. Officers will need to undertake due diligence on each potential investment in order to understand the risks and likelihood of default.

- **Asset Backed Securities (ABS) / Residential Mortgage backed securities (RMBS)** – As these securities by their nature are asset backed they are regarded as low risk should a default take place, but have a higher return. These are available for direct investment, or as pooled / segregated assets managed by a third party fund manager. In the event of a fund manager option being selected, this would need to be procured through a proper procurement process.

- **Loans** - The Council will allow loans (as a form of investment) to be made to organisations delivering services for the Council where this will lead to the enhancement of services to Westminster Stakeholders. The Council will

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The Core Tier 1 ratios for the four UK banks that WCC uses are: Barclays: 12.7%, HSBC: 14.5%, Lloyds: 14.5% and RBS: 15.5%.

undertake due diligence checks to confirm the borrower's creditworthiness before any sums are advanced and will obtain appropriate levels of security or third party guarantees for loans advanced. The Council would expect a return commensurate with the type, risk and duration of the loan. A limit of £50 million for this type of investment is proposed with a duration commensurate with the life of the asset and Council's cash flow requirements. All loans will need to be in line with the Council's Scheme of Delegation and Key Decision thresholds levels

- **Shareholdings in limited companies and joint ventures** – The Council invests in three forms of company:

  - Small scale businesses funded through the Civic Enterprise Fund aimed at promoting economic growth in the area. Individual investments are no more than £0.5m and the aim is for the Fund to be self-financing over the medium-term.

  - Trading vehicles which the Council has set up to undertake particular functions. These are not held primarily as investments but to fulfil Council service objectives. For example, CityWest Homes is a company limited by guarantee to run the housing arms-length management organisation. Any new proposals will be subject to due diligence as part of the initial business case. As these are not to be held primarily as investment vehicles, then there is an expectation that they will break even.

  - Trading vehicles held for a commercial purpose where the Council is obliged to undertake transactions via a company vehicle. These will be wholly owned subsidiaries of the Council with the aim of diversifying the investment portfolio risk.

15. For any such investments, specific proposals will be considered by the Director of Treasury and Pensions, and approved by the S151 Officer after taking into account:

    - cash flow requirements
    - investment period
    - expected return
    - the general outlook for short to medium term interest rates
    - creditworthiness of the proposed investment counterparty
    - other investment risks.

16. The value of non-specified investments will not exceed their Investment allocation. The Council must now formulate a strategy that allocates its cash in the most effective manner to short, medium and long term non-specified investments.

Country of Domicile

17. The current TMSS allows deposits / investments with financial entities domiciled in the following countries: Australia, Canada, Denmark, Finland, France, Germany, Luxembourg, Netherlands, Norway, Singapore, Sweden, Switzerland, UK and USA. This list will be kept under review and any proposed changes to the policy reported to the next meeting

Schedule of investments

18. The criteria for providing a pool of high quality short, medium and long-term, cash-based investment counterparties along with the time and monetary limits for institutions on the Council's counterparty list are in the table overleaf:

19. Officers will monitor the impact of the UK's exit from the European Union on the names within the Council's counterparty list.

All investments listed below must be sterling denominated*

Investments	Minimum Credit Rating Required (S&P/Moody's/Fitch)	Maximum Individual Counterparty Investment Limit (£m)	Maximum tenor
DMO Deposits	Government Backed	Unlimited	6 months
UK Government (Gilts/T-Bills/Repos)	Government Backed	Unlimited	Unlimited
Supra-national Banks, European Agencies	LT: AA/Aa/AA	£200m	5 years
Covered Bonds	LT: AA/Aa/AA	£300m	10 years
Network Rail	Government guarantee	Unlimited	Oct 2052
TfL	LT: AA/Aa/AA	£100m	5 years
GLA UK Local Authorities (LA) Local Government Association (LGA)	N/A	GLA : £100M	5 years
		LA: £100m per LA, per criteria £500m in aggregate	3 years
		LGA: £20m	15 years
Commercial Paper issued by UK and European Corporates	ST: A-1/P-1/F-1	£40m per name, £200m in aggregate	6 months
Money Market Funds (MMF)	LT: AAA/Aaa/AAA By at least two of the main credit agencies	£70m per Fund Manager £300m in aggregate	3 day notice
Ultra Short Dated Bond Funds (USDBFs)	LT: AAA/Aaa/AAA By at least one of the main credit agencies	£25m per fund manager, £75m in aggregate	Up to 7 day notice
Collateralised Deposits	Collateralised against loan	£100m	50 years
Social Housing Bonds	Due Diligence	£200m	10 years
Asset backed securities (ABS) and Residential mortgage backed securities (RMBS)	Asset Backed / Due Diligence	£200m	10 years
UK Bank (Deposit or Certificates of Deposit)	LT: AA-/Aa3/AA- ST: F1+	£75m	5 years
UK Bank (Deposit or Certificates of Deposit)	LT: A-/A3/A ST: F1	£50m	3 years
Non-UK Bank (Deposit or Certificates of Deposit)	LT: AA-/Aa2/AA- ST: F1+	£50m	5 years
	LT: A/A2/A ST: F1	£35m	3 years
Green Energy Bonds	Internal and External due diligence	Less than 25% of the total project investment or maximum £20m per bond. £50m in aggregate	10 years
Rated UK Building Societies	LT: A-/A3/A ST: F1	£10m per Building Society, £50m in aggregate	1 year
Loans to organisations delivering services for the Council	Due diligence	£50m in aggregate	Over the life of the asset
Sovereign approved list (AA rated and above): Australia, Canada, Denmark, Finland, France, Germany, Luxembourg, Netherlands, Norway, Singapore, Sweden, Switzerland, UK and USA			

Rationale for investment limits

19. Debt Management Office (DMO): Unlimited. The DMO is an executive agency of Her Majesty's Treasury. Being fully UK government backed, the DMO is the ultimate low risk depositary. Being ultra-low risk, the investment return is very low.

20. UK Government Gilts/T-Bills/Repos: Unlimited. UK Government gilts are regarded by the market as high quality and ultra-low risk. Being ultra-low risk, the investment return is very low.

21. Supra-national Banks, European Agencies: £200m limit. A supra-national bank is a financial institution, such as the European Investment Bank or the World Bank, whose equity is owned by sovereign states. Being owned by overseas states, they are regarded as being very low risk, but not in the same safe risk category as UK. The investment return is very low.

22. Covered Bonds: £300m limit. Covered bonds are debt securities issued by a bank or mortgage institution and collateralised against a pool of assets that, in case of failure of the issuer, can cover claims at any point of time. They are subject to specific legislation to protect bond holders. With slightly more risk. the investment return is higher than UK Gilts.

23. Residential Mortgage Backed Securities (RMBS): £200m limit. A residential mortgage backed security is a pool of mortgage loans created by banks and other financial institutions. The cash flows from each of the pooled mortgages is packaged by a special-purpose entity into classes and tranches, which then issues securities and can be purchased by investors. Being asset backed, they are regarded as being reasonably low risk should a default take place, but with a higher return.

24. Network Rail: Unlimited. Network Rail is the owner and infrastructure manager of most of the rail network in England, Scotland and Wales. Having a UK government guarantee, they are regarded as being reasonably low risk with a lower investment return.

25. Transport for London (TfL): £100m limit. Transport for London is a local government body responsible for the transport system in Greater London. Its parent organisation is the Greater London Authority (GLA). Being a GLA owned entity, the investment is regarded as safe and the return is low.

26. Greater London Authority (GLA): £100m limit. The Greater London Authority is the top-tier administrative body for Greater London, consisting of a directly elected executive Mayor of London and an elected 25-member London Assembly. Being categorised alongside UK local authorities, the investment is regarded as safe and the return is low.

27. UK Local Authorities: £100 limit per authority, £500m in total. This has been increased from £200m on the basis that local authorities have always been regarded as safe counterparties. As an additional safeguard, each new local authority counterparty will be subject to checks regarding latest accounts, audit opinion, financial projections, and financial reputation. There are 326 billing authorities with tax-raising powers in England, consisting of 201 non-metropolitan district councils, 55 unitary authority councils, 36 metropolitan borough councils, 32 London borough councils, the City of London Corporation and the Council of the Isles of Scilly. Additionally, there are levying authorities, consisting of 45 police authorities, 52 fire authorities and six waste disposal authorities. Having never defaulted in history, UK

local authorities and levying authorities are regarded as safe and the return is relatively low. Each new counterparty should be subject to check of latest accounts, any audit issues reported in the latest ISA260 reports, the latest budget position reported to council (to identify if there any potential financial health issues) and officer knowledge of the authority's latest financial reputation.

28. Local Government Association: £20m. The Local Government Association (LGA) is a charitable organisation, funded largely from subscriptions, which comprises local authorities in England and Wales, representing the interests of local government to national government. 435 authorities are members of the LGA as of 2016, including 349 English councils and the 22 Welsh councils, as well number of smaller authorities including fire authorities and national parks. Despite being an entity which represents local authorities, the entity is not regarded as risk free as local authorities and therefore the limit is lower at £20m.

29. Commercial Paper issued by the UK and European Corporates: £40m per name, £200m in total. Commercial paper is an unsecured, short-term debt instrument issued by a corporation, typically for the financing of accounts receivable, inventories and meeting short-term liabilities. Investment is confined to high quality investment grade corporates. The risk and investment return are higher than the sovereign categories.

30. Money Market Funds (MMF): £70m per manager, £300m in total. Money market funds are open-ended funds that invests in short-term high quality debt securities such as Treasury bills and commercial paper. Money market funds are widely regarded as being as safe as bank deposits, yet providing a higher yield. Being well diversified but investing with higher risk counterparties and instruments, the risk and investment return are higher.

31. Ultra short dated bond funds (USDBFs): £25m per manager, £75m in total. Enhanced money market funds increase returns via increasing interest rate, credit and liquidity risk in order to enhance the return. Being well diversified reduces the impact of a single default within the portfolio.

32. Collateralised Deposits: £100m. In lending agreements, collateral is a borrower's pledge of specific property to a lender to secure repayment of a loan, serving as a lender's protection against a borrower's default. Being asset backed, they are regarded as being reasonably low risk should a default take place, but with a higher return.

33. UK Bank Deposits: £75m per bank. Banks have become a riskier counterparty since the recent bail outs of Lloyds and RBS. The Financial Services (Banking Reform) Act 2013 confers on the Bank of England a bail-in stabilisation option for the resolution for banks and building societies, ensuring that shareholders and creditors/depositors of the failed institution, rather than the taxpayer, meet the costs of the failure. Despite the bail-in risk, the return on UK bank deposits is relatively low.

34. Non-UK Bank Deposits: £50m (Sterling deposits only) per bank. Overseas banks incorporated in the UK provide a number of options for high quality institutions with returns largely similar to UK banks.

35. Green Energy Bonds: £20m per bond, £50m in total (subject to due diligence). This comprises of finance for the supply of electricity from renewable energy sources, particularly in areas such as energy storage and electric vehicle networks. This category is greater risk and will provide an enhanced return. Use should be made of

regulated markets where available in order to provide additional investment security and risk reduction.

36. Social Housing Bonds: £200m in total. Housing associations are increasingly issuing public bonds, secured against social housing assets, to meet financing requirements. This category is greater risk and will provide an enhanced return.

37. Rated Building Societies: £10m per building society, £50m in total. Same rationale as UK banks, see above.

38. Loans to organisations delivering services to the Council: £50m in total. Assessed individually and subject to due diligence. At markets rates of interest and reflecting the risk of the borrower, this will offer an enhanced rate of return.

APPENDIX 2

Minimum Revenue Provision (MRP) Policy

1. Capital expenditure is generally defined as expenditure on assets that have a life expectancy of more than one year. The accounting approach is to spread the cost over the estimated useful life of the asset. The mechanism for spreading these costs is through an annual MRP. The MRP is the means by which capital expenditure, which is financed by borrowing or credit arrangements, is funded by Council Tax.

2. Regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended (Statutory Instrument (SI) 3146/2003) requires full Council to approve a Minimum Revenue Provision (MRP) Statement setting out the policy for making MRP and the amount of MRP to be calculated which the Council considers to be prudent. In setting a level which the Council considers to be prudent, the Guidance states that the broad aim is to ensure that debt is repaid over a period reasonably commensurate with that over which the capital expenditure provides benefits to the Council.

3. The Council is recommended to approve the following MRP Statement:

   - For capital expenditure incurred before 1 April 2007, MRP will be calculated using Option 1 (the 'Regulatory Method') of the CLG Guidance on MRP. Under this option MRP will be 4% of the closing non-HRA CFR for the preceding financial year.

   - For all capital expenditure incurred after 1 April 2007 financed from unsupported (prudential) borrowing (including PFI and finance leases), MRP will be based upon the asset life method under Option 3 of the DCLG Guidance.

   - In some cases, where a scheme is financed by prudential borrowing it may be appropriate to vary the profile of the MRP charge to reflect the future income streams associated with the asset, whilst retaining the principle that the full amount of borrowing will be charged as MRP over the asset's estimated useful life.

   - A voluntary MRP may be made from either revenue or voluntarily set aside capital receipts.

   - Estimated life periods and amortisation methodologies will 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.

   - 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.

- Charges included in annual PFI or finance leases to write down the balance sheet liability shall be applied as MRP.

- Where borrowing is undertaken for the construction of new assets, MRP will only become chargeable once such assets are completed and operational.

- If property investments are short-term (i.e. no more than 4 years) and for capital appreciation, the Council will not charge MRP as these will be funded by the capital receipt on disposal.

4. There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made. For the Council this is componentised based on the life of component and the gross replacement cost within the overall existing use value – social housing of the HRA stock.

APPENDIX 3

CIPFA requirements

The Council has formally adopted CIPFA's Code of Practice on Treasury Management (updated 2017) and complies with the requirements of the Code as detailed in this appendix. There are no changes to the requirements formally adopted in the 2017 update with regard to reporting: these are listed below:

- Maintaining a Treasury Management Policy Statement setting out the policies and objectives of the Council's treasury management activities.

- Maintaining a statement of Treasury Management Practices that sets out the manner in which the Council will seek to achieve these policies and objectives.

- Presenting the Full Council with an annual TMSS statement, including an annual investment strategy and Minimum Revenue Provision policy for the year ahead (this report) a half year review report and an annual report (stewardship report) covering compliance during the previous year

- A statement of delegation for treasury management functions and for the execution and administration of statement treasury management decisions. (see below).

- Delegation of the role of scrutiny of treasury management activities and reports to a specific named body. At Westminster City Council this role is undertaken by the Housing, Finance and Corporate Services Policy and Scrutiny Committee.

Treasury Management Delegations and Responsibilities

The respective roles of the Council, Cabinet, Housing, Finance and Corporate Services Policy and Scrutiny committee and Section 151 officer are summarised below. Further details are set out in the Treasury Management Practices.

Council

Council will approve the annual treasury strategy, including borrowing and investment strategies. In doing so Council will establish and communicate their appetite for risk within treasury management having regard to the Prudential Code

Cabinet

Cabinet will recommend to Council the annual treasury strategy, including borrowing and investment strategies and receive a half-year report and annual out-turn report on treasury activities.

Cabinet also approves revenue budgets, including those for treasury activities.

Housing, Finance and Corporate Services Policy and Scrutiny Committee

This committee is responsible for ensuring effective scrutiny of the Treasury strategy and policies.

Section 151 Officer

Council has delegated responsibility for the implementation and monitoring of treasury management decisions to the Section 151 Officer to act in accordance with approved policy and practices. The s151 Officer has full delegated powers from the Council and is responsible for the following activities:

- investment management arrangements and strategy;
- borrowing and debt strategy;
- monitoring investment activity and performance;
- overseeing administrative activities;
- ensuring compliance with relevant laws and regulations;
- provision of guidance to officers and members in exercising delegated powers.

Tri-Borough Director of Treasury and Pensions

Has responsibility for the execution and administration of treasury management decisions, acting in accordance with the Council's Treasury Policy Statement and CIPFA's 'Standard of Professional Practice on Treasury Management'.

Treasury Team

Undertakes day to day treasury investment and borrowing activity in accordance with strategy, policy, practices and procedures.

Training

The CIPFA code requires the s151 officer to ensure that Members with responsibility for making treasury management decisions and for scrutinising treasury functions to receive adequate training. The training needs of all officers are reviewed periodically as part of the Learning and Development programme. Officers attend various seminars, training sessions and conferences during the year and appropriate Member training is offered as and when needs, and suitable opportunities, are identified.

Prospects for Interest Rates

1. 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 our central view.

	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21
Bank Rate	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.25%
5 yr PWLB Rate	2.00%	2.00%	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%	2.50%
10 yr PWLB Rate	2.40%	2.50%	2.50%	2.60%	2.70%	2.70%	2.80%	2.90%	2.90%	2.90%	2.90%
25 yr PWLB Rate	2.80%	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%	3.40%
50 yr PWLB Rate	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.20%	3.20%

2. Capita Asset Services undertook its last review of interest rate forecasts on 20 August 2018 after the quarterly Bank of England Inflation Report and MPC Bank Rate increase from 0.50% to 0.75% as expected. But the 9-0 outcome was a surprise. The Committee reaffirmed that further rate moves will likely be gradual though inflationary pressures will be monitored The markets are not factoring in another rate hike at any of the last three meetings this year, with December expectations being pared back below 10% following comments from the BoE Governor on Brexit. Markets are near 60% confident that there will be a hike in August 2019.

3. The overall balance of risks to economic recovery in the UK is currently to the downside but significant variables over the coming few years include just what final form Brexit will take, when finally agreed with the EU, and when.

4. Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:
   - UK economic growth and increases in inflation are weaker than we currently anticipate.
   - Weak growth or recession in the UK's main trading partners - the EU and US.
   - Geopolitical risks in Europe, the Middle East and Asia, which could lead to increasing safe haven flows.
   - A resurgence of the Eurozone sovereign debt crisis.
   - Weak capitalisation of some European banks.
   - Monetary policy action failing to stimulate sustainable growth and to get inflation up consistently to around monetary policy target levels.

5. The potential for upside risks to current forecast for UK gilt yields and PWLB rates, especially for longer term PWLB rates include:

   - The pace and timing of increases in the Fed. Funds Rate causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.

   - UK inflation returning to significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

Economic Update

6. **UK.** The first half of 2018/19 has seen UK economic growth post a modest performance, but sufficiently robust for the Monetary Policy Committee (MPC) to unanimously (9-0) vote to increase Bank Rate on 2 August from 0.5% to 0.75%. Although growth looks as if it will only be modest at around 1.5% in 2018, the Bank of England's August 2018 Quarterly Inflation Report suggested that growth will pick up to 1.8% in 2019, albeit there were several caveats, mainly related to whether or not the UK achieves an orderly withdrawal from the European Union on 29 March 2019.

7. Some MPC members have expressed concerns about a build-up of inflationary pressure, particularly with the pound falling in value again against both the US dollar and the Euro. The Consumer Price Index (CPI) measure of inflation is currently running at 2.5% but is expected to fall back towards the 2% inflation target over the next two years, given a scenario of minimal increases in Bank Rate. The MPC has indicated that the Bank Rate would need to be in the region of 1.5% by March 2021 for inflation to stay on track. Financial markets are currently pricing in the next increase in Bank Rate for the second half of 2019.

8. Re unemployment, this is now at a 43-year low of 4% on the Independent Labour Organisation measure but, despite that, wage inflation is currently weak. This is a global theme for the major economies of the world. Indeed, with UK wages running in line with the CPI measure of inflation, real earnings are, in effect, neutral. Given the UK economy is very much services sector driven, any weakness in household spending power is likely to feed through into tepid economic growth. This is another reason why the MPC will need to tread cautiously before increasing the Bank Rate again, especially given all the uncertainties around UK exit from the EU. Additionally, business sentiment surveys, such as the Purchasing Managers Index collated by Markit, suggest the UK is set for only modest GDP growth in the second half of 2018 with the monthly updated figure for annual growth being 1.5% as at the end of July 2018. The housing market is going through a weak phase, with UK wide house price growth averaging 2% to 3%, but with London and the south-east experiencing price falls.

9. As for the political arena, there is a risk that the current Conservative minority government may be unable to muster a majority in the Commons over UK exit from the EU. However, Prime Minister May's government could endure, despite various setbacks, along the route to 29 March 2019. If, however, the UK faces a general election in the next 12 months, this could result in a potential loosening of monetary policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up.

10. **EU.** Growth has undershot early forecasts for a strong economic performance in 2018. In particular, data from Germany has been mixed and it could be negatively impacted by US tariffs on a significant part of manufacturing exports, e.g., cars. For that reason, although growth is still expected to be in the region of 2% for 2018, the horizon is less clear than it seemed just a short while ago.

11. **USA.** President Trump's massive easing of fiscal policy is fuelling a (temporary) boost in consumption which has generated an upturn in the rate of strong growth to around 1% in Q2 2018, but also an upturn in inflationary pressures. With inflation moving towards 3%, the Fed has already tightened the Fed Funds interest rate to between 1.75% and 2%, and a further two increases to 2.25% to 2.5% are expected before the end of 2018 with the prospect of another increase or two next year. The dilemma, however, is what to do when the temporary boost to consumption wanes, particularly as the recent imposition of tariffs on a number of countries' exports to the US, (China in particular), could see a switch to US production of some of those goods, but at higher prices. Such a scenario would invariably make any easing of monetary policy harder for the Fed in the second half of 2019.

12. **CHINA.** Economic growth has been weakening over successive years and, despite repeated rounds of central bank stimulus, medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems.

13. **Japan** is struggling to stimulate consistent significant growth and to get inflation up to its target of 2%, despite significant monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.