

Permitted Investments

Appendix 1

The Council uses the Link creditworthiness service for specific categories of permitted investments. This utilises credit ratings from the three main credit rating agencies – Fitch, Moody's and Standard & Poors, along with credit watches, outlooks, CDS spreads and country sovereign ratings in a weighted scoring system with an end product of a series of colour coded bands which indicate the relative creditworthiness of specific categories of counterparties for investment.

These colour codes are used by the Council to determine the maximum suggested duration for investment with that counterparty. These are as follows:-

Link Asset Services Colour Code	Maximum Suggested Duration for Investment
Yellow	6 years*
Dark Pink	6 years**
Light Pink	6 years**
Purple	2.5 years
Blue	1.25 years***
Orange	1.25 years
Red	7 months
Green	120 days
No colour	Not to be used

* *Note the yellow colour category is for:- UK Government Debt, or its equivalent, Money Market Funds (MMF's), and collateralised deposits where the collateral is UK Government Debt*

** *Dark Pink for Ultra Short Dated Bond Funds with a credit score of 1.25; Light Pink for Ultra Short Dated Bond Funds with a credit score of 1.5*

*** *Only applies to nationalised or semi-nationalised UK banks*

Note that the maximum suggested durations listed above have been extended by 1 year (when compared to the suggested maximum durations provided by Link) for the Yellow, Dark Pink, Light Pink categories (and so to 6 years); the Purple category by 6 months to 2.5 years; the Blue and Orange categories by 3 months to 1.25 years; the Red category by a month to 7 months, and the Green category by 20 days to 120 days. This is to allow flexibility around these durations on the margins e.g. the placement of a 13 month fixed term deposit for a counterparty rated Orange or Blue. A thorough appraisal of the additional risk involved in extending the duration of any deposit (marginally) beyond the maximum suggested by Link, against any enhanced value to the portfolio, will be undertaken prior to the placement of any deposit.

1.1 Deposits

Investment Category	Minimum Credit Criteria	Liquidity risk	Market risk	Max %/£m of total investments	Max. maturity period
Debt Management Agency Deposit Facility	--	Term	No	100%	6 months
Term deposits – local authorities	--	Term	No	100%	5 years
Call accounts – banks and building societies	Green	Instant	No	100%	1 day
Term deposits / Notice Accounts – banks and building societies	Yellow Purple Blue Orange Red Green No Colour	Term	No	100%	Up to 6 yrs Up to 2.5 yrs Up to 1.25 yrs Up to 1.25 yrs Up to 7 mths Up to 120 days Not for use
Fixed term deposits with variable rate and variable maturities: - Structured deposits	Yellow Purple Blue Orange Red Green No Colour	Term	No	100%	Up to 6 yrs Up to 2.5 yrs Up to 1.25 yrs Up to 1.25 yrs Up to 7 mths Up to 120 days Not for use

1.2 Deposits with counterparties currently in receipt of government support / ownership

Investment Category	Minimum Credit Criteria	Liquidity risk	Market risk	Max %/£m of total investments	Max. maturity period
UK nationalised banks – Call accounts	Blue	Instant	No	100%	1 day
UK nationalised banks – Term Deposits / Notice Accounts	Blue	Term	No	100%	1.25 years
UK nationalised banks – Fixed term deposits with variable rate and variable maturities: - Structured deposits	Blue	Term	No	100%	1.25 years
Non-UK (high sovereign rated country) nationalised banks – Call accounts	Green	Instant	No	100%	1 day
Non-UK (high sovereign rated country) nationalised banks:- Term Deposits / Notice Accounts	Yellow Purple Blue Orange Red Green No Colour	Term	No	100%	Up to 6 yrs Up to 2.5 yrs Up to 1.25 yrs Up to 1.25 yrs Up to 7 mths Up to 120 days Not for use
Non-UK (high sovereign rated country) nationalised banks:- Fixed term deposits with variable rate and variable maturities: - Structured deposits	Yellow Purple Blue Orange Red Green No Colour	Term	No	100%	Up to 6 yrs Up to 2.5 yrs Up to 1.25 yrs Up to 1.25 yrs Up to 7 mths Up to 120 days Not for use

If forward deposits are made, the forward period plus the deal period equate to the maximum maturity period.

1.3 Collective investment schemes structured as Open Ended Investment Companies (OEICs)

Investment Category	Minimum Credit Criteria	Liquidity risk	Market risk	Max %/£m of total investments	Max. maturity period
Government Liquidity Funds	AAA	Instant	No	100%	1 day
Money Market Funds CNAV	AAA	Instant	No	100%	1 day
Money Market Funds LVNAV	AAA	Instant	No	100%	1 day
Money Market Funds VNAV	AAA	Instant	No	100%	1 day
Ultra Short Dated Bond Funds with a credit score of 1.25	AAA	T+1 to T+5	Yes	100%	1 week
Ultra Short Dated Bond Funds with a credit score of 1.5	AAA	T+1 to T+5	Yes	100%	1 week
Bond Funds	AAA	T+2 or longer	Yes	50%	2 days
Gilt Funds	AAA	T+2 or longer	Yes	50%	2 days

1.4 Securities issued or guaranteed by governments

Investment Category	* Minimum Credit Criteria	Liquidity risk	Market risk	Max %?£m of total investments	Max. maturity period
Treasury Bills	UK sovereign rating	Sale T+1	Yes	100%	50 years
UK Government Gilts	UK sovereign rating	Sale T+1	Yes	100%	50 years
Bond issuance issued by a financial institution which is explicitly guaranteed by the UK Government e.g. National Rail	UK sovereign rating	Sale T+3	Yes	100%	50 years
Sovereign bond issues (other than the UK govt)	AAA (or state your criteria if different)	Sale T+1	Yes	100%	50 years
Bonds issued by multilateral development banks	AAA (or state your criteria if different)	Sale T+1	Yes	100%	50 years

1.5 Securities issued by corporate organisations

Investment Category	* Minimum Credit Criteria	Liquidity risk	Market risk	Max % of total investments	Max. maturity period
Certificates of deposit issued by banks and building societies	Yellow Purple Blue Orange Red Green No Colour	Sale T+0	Yes	100%	Up to 6 yrs Up to 2.5 yrs Up to 1.25 yrs Up to 1.25 yrs Up to 7 mths Up to 120 days Not for use
Commercial paper other	Yellow Purple Blue Orange Red Green No Colour	Sale T+0	Yes	100%	Up to 6 yrs Up to 2.5 yrs Up to 1.25 yrs Up to 1.25 yrs Up to 7 mths Up to 120 days Not for use
Floating rate notes	Yellow Purple Blue Orange Red Green No Colour	Sale T+2	Yes	100%	Up to 6 yrs Up to 2.5 yrs Up to 1.25 yrs Up to 1.25 yrs Up to 7 mths Up to 120 days Not for use
Corporate Bonds other	Yellow Purple Blue Orange Red Green No Colour	Sale T+2	Yes	100%	Up to 6 yrs Up to 2.5 yrs Up to 1.25 yrs Up to 1.25 yrs Up to 7 mths Up to 120 days Not for use

1.6 Other

Investment Category	Minimum Credit Criteria	Liquidity risk	Market risk	Max %/£m of total investments	Max. maturity period
Local authority mortgage guarantee scheme.	Blue	Term	No	50%	5 years
Loans to Third Parties	n/a	Term	No	£25m	25 years
Subordinated Debt Subscription to Newbattle Centre SPV	n/a	Term	No	£0.326m	22 years
Midlothian Energy Limited	n/a	Term	No	£10.2m	n/a

Treasury Risks and Mitigating Controls for each type of investment are as outlined in the Treasury Management & Annual Investment Strategy Statement – 2023/24 Detailed – Appendix 5.3. The Council's Treasury Management Practices have also been updated in line with the new CIPFA Prudential and Treasury Management Codes which were approved by Audit Committee on 6 December 2022.

2. Prudential Indicators for Capital Expenditure

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

2.1 Estimated Capital Expenditure

This indicator shows the gross capital spend included in the relevant capital plans.

Capital Expenditure						
	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
	£000's	£000's	£000's	£000's	£000's	£000's
General Services						
Children, Young People & Estates	£ 5,300	£ 29,096	£ 45,647	£ 104,189	£ 81,483	£ 8,610
Asset Management	£ 11,439	£ 14,204	£ 18,682	£ 10,597	£ 9,982	£ 5,912
Transport, Energy & Infrastructure	£ 551	£ 3,412	£ 17,122	£ 3,254	£ 425	£ 425
Regeneration & Development	£ 1,059	£ 15,380	£ 18,371	£ 721	£ 800	£ -
Other	£ 5,014	£ 3,334	£ 11,574	£ 6,104	£ 701	£ 528
Provision for return of contingencies	£ (41)	£ (506)	£ (2,539)	£ (2,890)	£ (3,627)	£ (3,347)
Total General Services	£ 23,322	£ 64,921	£ 108,857	£ 121,975	£ 89,765	£ 12,128
Total HRA	£ 51,710	£ 52,125	£ 99,585	£ 91,901	£ 36,647	£ 26,128
Combined Total	£ 75,032	£ 117,046	£ 208,442	£ 213,876	£ 126,412	£ 38,256

2.2 Financing of Capital Expenditure

This indicator shows how the Capital Expenditure forecasts are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Capital Expenditure and Available Financing						
	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
	£000's	£000's	£000's	£000's	£000's	£000's
Capital Expenditure						
General Services	£ 23,322	£ 64,921	£ 108,857	£ 121,975	£ 89,765	£ 12,128
HRA	£ 51,710	£ 52,125	£ 99,585	£ 91,901	£ 36,647	£ 26,128
Total	£ 75,032	£ 117,046	£ 208,442	£ 213,876	£ 126,412	£ 38,256
Financed by:						
Capital receipts	£ 3	£ 60	£ -	£ -	£ -	£ -
Capital grants	£ 20,203	£ 26,397	£ 38,962	£ 19,791	£ 7,231	£ 7,121
Capital reserves	£ 3,000	£ 2,473	£ 7,694	£ -	£ -	£ -
Developer/Other Contributions	£ 5,353	£ 17,935	£ 18,258	£ 14,542	£ 12,201	£ 3,772
Net financing need for the year	£ 46,473	£ 70,181	£ 143,528	£ 179,543	£ 106,980	£ 27,363

2.3 Estimated Capital Financing Requirement

This indicator measures the Council's maximum underlying need to borrow for capital purposes and other long term liabilities over the next three years.

Capital Financing Requirement (CFR)						
	2022/23 Actual £000's	2023/24 Estimate £000's	2024/25 Estimate £000's	2025/26 Estimate £000's	2026/27 Estimate £000's	2027/28 Estimate £000's
Capital Financing Requirement						
CFR – General Services	£ 138,532	£ 165,056	£ 228,109	£ 323,109	£ 389,164	£ 384,772
CFR – HRA	£ 209,129	£ 244,290	£ 317,564	£ 390,437	£ 418,804	£ 436,365
CFR – PFI Schemes	£ 92,433	£ 88,739	£ 84,815	£ 80,661	£ 76,277	£ 71,663
Total CFR	£ 440,094	£ 498,085	£ 630,488	£ 794,207	£ 884,246	£ 892,800
Movement in CFR	£ 37,230	£ 57,991	£ 132,404	£ 163,719	£ 90,039	£ 8,554
Movement in CFR represented by						
Net financing need for the year (previous table)	£ 46,473	£ 70,181	£ 143,528	£ 179,543	£ 106,980	£ 27,363
MEL Shareholder Injection	£ -	£ 710	£ 3,560	£ -	£ -	£ -
Less Scheduled Debt Amortisation	£ (5,762)	£ (9,206)	£ (10,760)	£ (11,670)	£ (12,557)	£ (14,195)
Less net PFI Finance Lease Principal Payments	£ (3,481)	£ (3,694)	£ (3,924)	£ (4,154)	£ (4,384)	£ (4,614)
Movement in CFR	£ 37,230	£ 57,991	£ 132,404	£ 163,719	£ 90,039	£ 8,554

3. Prudential Indicators for Prudence

3.1 Net Borrowing Requirement

This indicator shows the amount of external borrowing required to finance the current debt outstanding on capital projects.

Net Borrowing Requirement						
	2022/23 Actual £000's	2023/24 Estimate £000's	2024/25 Estimate £000's	2025/26 Estimate £000's	2026/27 Estimate £000's	2027/28 Estimate £000's
External Debt						
Debt at 1 April	£ 323,271	£ 321,753	£ 384,346	£ 520,674	£ 688,547	£ 782,969
Actual/Expected change in Debt	£ (1,518)	£ 62,593	£ 136,328	£ 167,873	£ 94,423	£ 13,168
Other long-term liabilities (OLTL) at 1 April	£ 95,914	£ 92,433	£ 88,739	£ 84,815	£ 80,661	£ 76,277
Actual/Expected change in OLTL	£ (3,481)	£ (3,694)	£ (3,924)	£ (4,154)	£ (4,384)	£ (4,614)
Actual/Expected Gross Debt at 31 March	£ 414,186	£ 473,085	£ 605,489	£ 769,208	£ 859,246	£ 867,800
The Capital Financing Requirement	£ 440,094	£ 498,085	£ 630,488	£ 794,207	£ 884,246	£ 892,800
Under / (over) borrowing	£ 25,908	£ 25,000	£ 25,000	£ 25,000	£ 25,000	£ 25,000
Deposits						
Cash & Cash Equivalents	£ 15,982	£ 25,000	£ 25,000	£ 25,000	£ 25,000	£ 25,000
Short-Term Investments	£ 98,000	£ 70,000	£ 57,000	£ 57,000	£ 57,000	£ 57,000
Total Deposits	£ 113,982	£ 95,000	£ 82,000	£ 82,000	£ 82,000	£ 82,000

4. Prudential Indicators for External Debt

4.1 Operational Boundary

This is the limit beyond which external debt is not normally expected to exceed and will be the focus of day to day treasury management. Typically, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

For this Council:-

- the Operational Boundary for Borrowing has been calculated to equate directly to the value of the CFR for General Services and HRA combined, over the current financial year and the following 4 financial years (2023/24 to 2027/28); and
- the Operational Boundary for Other Long-Term Liabilities has been calculated to equate directly to the in-year CFR for Other Long-Term Liabilities, given the known contractual provisions for the repayment of debt within the Council's two PPP agreements.

Operational Boundary					
	2023/24	2024/25	2025/26	2026/27	2027/28
	Estimate	Estimate	Estimate	Estimate	Estimate
	£000's	£000's	£000's	£000's	£000's
Operational Boundary - Borrowing	£ 409,346	£ 545,673	£ 713,546	£ 807,969	£ 821,137
Operational Boundary - Other long term liabilities	£ 88,739	£ 84,815	£ 80,661	£ 76,277	£ 71,663
Total	£ 498,085	£ 630,488	£ 794,207	£ 884,246	£ 892,800

Should the Operational Boundary be breached, for example as a result of a decision taken to borrow in advance (should market conditions indicate that it is prudent to do so), this will be reported to Council at the next available opportunity.

4.2 Authorised Limit of Total External Debt

This indicator sets the limit for total external debt.

The Authorised Limit for Borrowing for the 2024/25 financial year has been calculated to equate to the maximum value of the Underlying Borrowing Requirement in 2024/25. This equates to £545.673 million as outlined below.

Authorised Limit for Borrowing	
	£000's
CFR - General Services at 31 March 2025	£ 228,109
CFR - HRA at 31 March 2025	£ 317,564
Authorised Limit for Borrowing	£ 545,673

5. Prudential Indicators for Treasury Management

5.1 Upper limits on Fixed and Variable Interest Rates

This indicator limits the amount of external debt that may be held at fixed or variable rates. These limits are proposed to be as follows:-

Upper Limits on Exposure to Fixed and Variable Interest Rates 2024/25			
Interest rate exposures			Upper Limit
Limits on fixed interest rates based on gross debt			100.00%
Limits on variable interest rates based on gross debt			30.00%
Limits on fixed interest rates based on investments			100.00%
Limits on variable interest rates based on investments			100.00%

5.2 Maturity Structure of Borrowing

This indicator sets the upper and lower limits of the time scales within which external debt may be held.

The Treasury Management Code of Practice requires that LOBO's with a call date in the next 12 months are classified as short-term borrowing rather than longer-term (10 year+) borrowing.

In addition, the Code also recommends that where an authority's debt is typically very long term (i.e. for a period of greater than 10 years), that authorities should break down the period in excess of 10 years into several ranges, for example 10 to 20 years, 20 to 30 years, etc.

With the above in mind, the proposed upper and lower limits for each maturity band are shown below, with the overall aim to ensure a spreading approach to avoid a cluster of high value loans maturing/requiring refinancing within a short period of time.

Maturity Structure of Borrowing 2024/25			
Maturity structure of fixed interest rate borrowing 2024/25		Lower	Upper
Under 12 months		0.00%	50.00%
12 months to 2 years		0.00%	50.00%
2 years to 5 years		0.00%	50.00%
5 years to 10 years		0.00%	50.00%
10 years to 20 years		0.00%	50.00%
20 years to 30 years		0.00%	50.00%
30 years to 40 years		0.00%	50.00%
40 years to 50 years		0.00%	50.00%
50 years and above		0.00%	50.00%
Maturity structure of variable interest rate borrowing 2024/25		Lower	Upper
<i>Under 12 months</i>		0.00%	30.00%
<i>12 months to 2 years</i>		0.00%	30.00%
<i>2 years to 5 years</i>		0.00%	30.00%
<i>5 years to 10 years</i>		0.00%	30.00%
10 years to 20 years		0.00%	30.00%
20 years to 30 years		0.00%	30.00%
30 years to 40 years		0.00%	30.00%
40 years to 50 years		0.00%	30.00%
50 years and above		0.00%	30.00%

5.4 Total Principal Sums Invested for Periods Longer than 365 Days

This indicator relates to the total level of investments held for periods longer than 365 days.

Principal Sums Invested for > 365 Days	
Limit	£70m

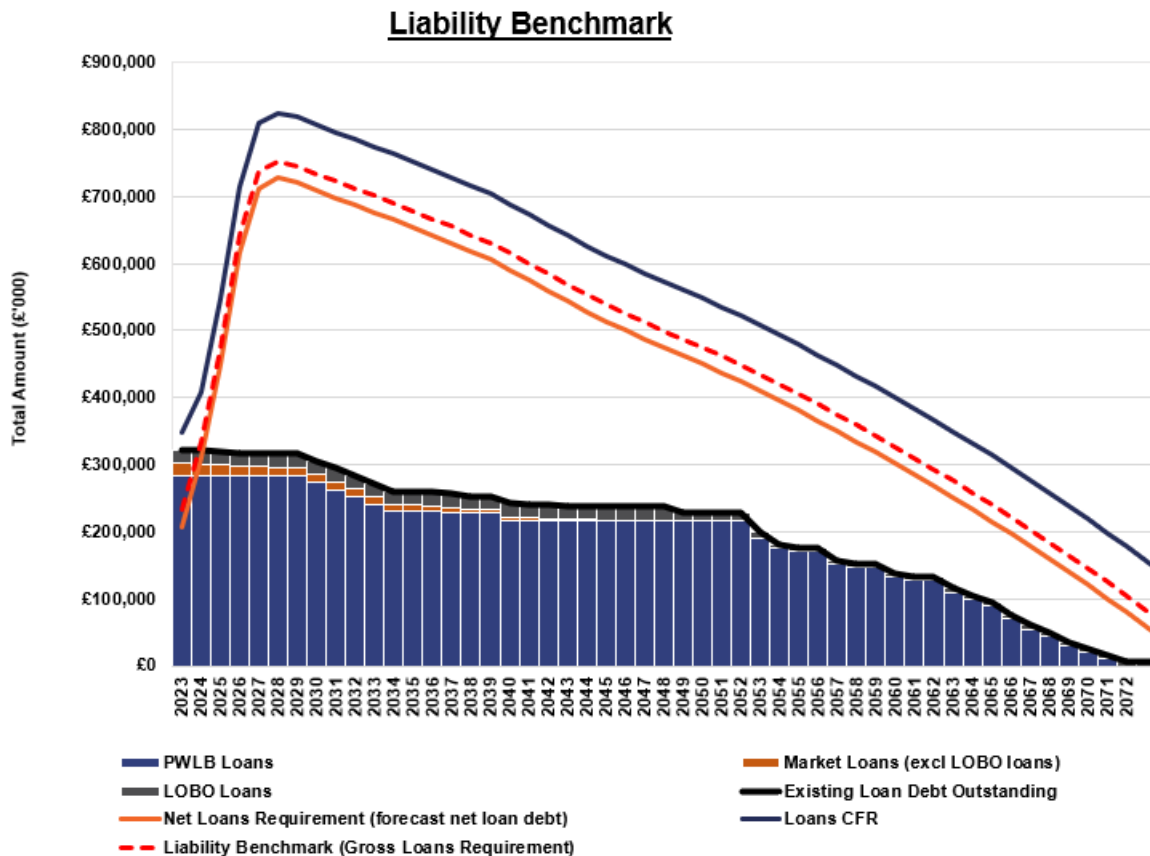
The current strategy as outlined in the body of these reports is to continue to cash-back the Council's balance sheet reserves. It is expected that the majority of this will be in the form of fixed term deposits and/or certificates of deposit. Given expected reserve forecasts and the current interest rate environment, in particular the short-medium term forecast for the Council's Capital Fund and HRA Reserve, the limit for principal sums invested for > 365 days has been retained at £70m.

For its cash flow generated balances, the Council will seek to utilise its business reserve instant access accounts and money market funds.

5.5 Liability Benchmark

The "Liability Benchmark" identifies future borrowing needs across the short, medium and longer terms, against the maturity profile of the Council's existing loan portfolio.

The Council's Liability Benchmark in graphical format is as shown below.



There are four components to the Liability Benchmark: -

- 1 **Existing loan debt outstanding:** the Council's existing loans that are still outstanding in future years – shown as the stacked bar elements of the figure above.

- 2 **Loans CFR:** this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned Loans Fund advances/Loans Fund principal repayments.
- 3 **Net loans requirement:** this shows the Council's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on its approved prudential borrowing, planned Loans Fund principal repayments and any other major cash flows (drawdowns/enhancement of reserves) forecast.
- 4 **Liability benchmark (or gross loans requirement):** this equals net loans requirement plus short-term liquidity/working capital allowance.

The Liability Benchmark Indicator identifies the Council's expected future capital financing requirement, as driven by the Council's approved Capital Plans – and therefore the Council's future borrowing needs; along with how this matches to the existing debt maturity profile. It is therefore a key tool to support the financing risk management of the capital financing requirement.

As can be noted from the figure above, the Council has a significant borrowing requirement (which equates to £478.638 million) in the short-medium term, arising as a direct result of the Council's approved Capital Plans. The proposed approach to securing this borrowing need for the 2024/25 financial year is outlined in the main body of this report, Section 4.3.

The Liability Benchmark also outlines the profile of the Council's CFR over the medium-long term, against the Council's existing debt portfolio maturity profile. As can be seen from the figure above, the profile of the CFR movements in the medium-long term broadly matches the movements in the Council's external debt portfolio over this period.

The Debt Liability Benchmark will assist the Council with plotting the tenor of borrowing to finance the Council's approved capital plans that is undertaken in the remainder of 2023/24 and the forthcoming 2024/25 period, to ensure that this aligns with the Council's future expected CFR profile and Liability Benchmark projections, taking into account the profile of existing loan maturities as identified in the figure above.