

Permitted Investments

Appendix 1

The Council uses the Capita creditworthiness service. 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 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:-

Capita Colour Code	Maximum Suggested Duration for Investment
Yellow	6 years*
Dark Pink	6 years**
Light Pink	6 years**
Purple	3 years
Blue	2 years***
Orange	2 years
Red	8 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 Capita) for the Yellow, Dark Pink, Light Pink, Purple, Blue and Orange categories, 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. Equally, the maximum suggested duration for the Red category has been extended by a month to 8 months, and the maximum duration for the Green category has been extended by 20 days to 120 days, on the same basis. A thorough appraisal of the additional risk involved in extending the duration of any deposit (marginally) beyond the maximum suggested by Capita, 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%	2 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 3 yrs Up to 2 yrs Up to 2 yrs Up to 8 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 3 yrs Up to 2 yrs Up to 2 yrs Up to 8 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%	2 years
UK nationalised banks – Fixed term deposits with variable rate and variable maturities: - Structured deposits	Blue	Term	No	100%	2 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 3 yrs Up to 2 yrs Up to 2 yrs Up to 8 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 3 yrs Up to 2 yrs Up to 2 yrs Up to 8 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 day
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	10)%	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+1	Yes	100%	Up to 6 yrs Up to 3 yrs Up to 2 yrs Up to 2 yrs Up to 7 mths Up to 100 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 3 yrs Up to 2 yrs Up to 2 yrs Up to 7 mths Up to 100 days Not for use
Floating rate notes	Yellow Purple Blue Orange Red Green No Colour	Sale T+0	Yes	100%	Up to 6 yrs Up to 3 yrs Up to 2 yrs Up to 2 yrs Up to 7 mths Up to 100 days Not for use
Corporate Bonds other	Yellow Purple Blue Orange Red Green No Colour	Sale T+3	Yes	100%	Up to 6 yrs Up to 3 yrs Up to 2 yrs Up to 2 yrs Up to 7 mths Up to 100 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	20 years
Subordinated Debt Subscription to Newbattle Centre SPV	n/a	Term	No	£0.5m	27 years
Property Funds	n/a	T+4	Yes	50%	15 years

Prudential Indicators

Appendix 2

1. Prudential Indicators for Affordability

These indicators provide an indication of the impact of the capital investment plans on the Council's overall finances.

1.1 Estimates of Ratio of Financing Costs to Net Revenue Stream

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

Ratio of Financing Costs to Net Revenue Stream							
%	2017/18	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
	Original	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
General Services	3.78%	3.17%	2.86%	3.04%	3.23%	3.33%	3.43%
HRA	34.14%	36.34%	37.26%	38.79%	45.31%	47.96%	52.10%

The figures above are based on the latest Capital Plans presented to Council.

1.2 HRA Ratios

The following indicator identifies the ratio of overall debt on the HRA account compared to annual house rent revenue.

Table 6: HRA Debt as a % of Gross Revenue							
	2017/18	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
	Estimate	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
HRA debt £000's	£ 166,325	£ 163,857	£ 169,011	£ 213,062	£ 285,120	£ 326,047	£ 328,252
HRA revenues £000's	£ 26,399	£ 27,798	£ 27,945	£ 29,610	£ 31,080	£ 33,670	£ 35,538
Ratio of debt to revenues %	630%	589%	605%	720%	917%	968%	924%

The following indicator identifies the ratio of overall debt on the HRA account per HRA dwelling.

Table 7: HRA Debt per Dwelling							
	2017/18	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
	Estimate	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
HRA debt £000's	£ 166,325	£ 163,857	£ 169,011	£ 213,062	£ 285,120	£ 326,047	£ 328,252
Number of HRA dwellings	6,917	6,985	6,907	6,962	7,194	7,528	£ 7,839
Debt per dwelling £	£ 24,046	£ 23,458	£ 24,470	£ 30,604	£ 39,633	£ 43,311	4187%

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						
	2017/18 Actual £000's	2018/19 Estimate £000's	2019/20 Estimate £000's	2020/21 Estimate £000's	2021/22 Estimate £000's	2022/23 Estimate £000's
General Services						
Resources	£ 8,127	£ 11,930	£ 20,874	£ 17,336	£ 12,478	£ 16,111
Education, Community & Economy	£ 8,647	£ 17,617	£ 46,516	£ 22,103	£ 9,196	£ 751
Health & Social Care	£ 170	£ 504	£ 8,416	£ 2,760	£ 397	£ 178
Business Transformation	£ 39	£ 35	£ 4	£ 10,692	£ 10,135	£ 240
Provision for Return of Contingencies	£ -	£ (372)	£ (743)	£ (1,877)	£ (1,275)	£ (773)
Total General Services	£ 16,984	£ 29,713	£ 75,067	£ 51,015	£ 30,931	£ 16,507
Total HRA	£ 10,572	£ 14,738	£ 54,519	£ 92,286	£ 51,698	£ 20,244
Combined Total	£ 27,556	£ 44,451	£ 129,586	£ 143,301	£ 82,629	£ 36,751

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					
	2018/19 Estimate £000's	2019/20 Estimate £000's	2020/21 Estimate £000's	2021/22 Estimate £000's	2022/23 Estimate £000's
Capital Expenditure					
General Services	£ 29,713	£ 75,067	£ 51,015	£ 30,931	£ 16,507
HRA	£ 14,738	£ 54,519	£ 92,286	£ 51,698	£ 20,244
Total	£ 44,451	£ 129,586	£ 143,301	£ 82,629	£ 36,751
Financed by:					
Capital receipts	£ 253	£ 900	£ 1,100	£ -	£ -
Capital grants	£ 20,339	£ 23,978	£ 36,606	£ 13,596	£ 18,784
Capital reserves	£ 750	£ 1,687	£ 2,000	£ 10,694	£ 2,000
Developer/Other Contributions	£ 11,112	£ 9,551	£ 9,624	£ 4,311	£ 2,367
Net financing need for the year	£ 11,997	£ 93,470	£ 93,971	£ 54,027	£ 13,599

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.

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 (2018/19 to 2022/23); 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						
	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
	£000's	£000's	£000's	£000's	£000's	£000's
Operational Boundary - Borrowing	£280,270	£283,930	£369,009	£452,494	£494,599	£495,135
Operational Boundary - Other long term liabilities	£53,659	£52,233	£50,683	£48,998	£47,167	£47,168
Total	£333,929	£336,163	£419,692	£501,492	£541,766	£542,303

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.

In an active Treasury Management policy it is sometimes prudent to borrow in advance of need if interest rates are expected to rise.

In order to continue to service the ongoing external debt and finance the current capital programmes the Council needs to increase its external borrowing to £523.188 million by 31 March 2023. Within the Capital Plans, there are assumptions regarding capital receipts and developer contributions which when applied to the Council's capital plans reduce the Council's borrowing requirements. However, the realisation of these capital receipts and developer contributions carry inherent uncertainty around both the timing and value of each receipt/contribution, given that they are largely dependent upon economic and market activity which are outwith the Council's control. Therefore, in order to calculate the Authorised Limit for Borrowing, these capital receipts and developer contributions have been added to the Capital Financing Requirement, to give the Council flexibility to fully borrow in advance of need (if market conditions support this action) should these receipts and contributions be unable to be realised in the short term. This therefore reflects a level of borrowing which, while not desired, could be afforded but is not sustainable.

Council is therefore asked to approve that, rather than restrict borrowing to £283.930 million for 2018/19, £369.009 million for 2019/20, £452.494 million for 2020/21, £494.599 million for 2021/22 and £495.135 million for 2022/23, that permission be granted to borrow up to the 2022/23 Authorised Limit for borrowing of £495.135 million as shown in the table below), if market conditions support this action.

Adopting this approach will secure lower costs for future years but care will be taken to ensure that the cost of carry is minimised and that the maturity structure of all debt is sufficiently robust to ensure that the Capital Financing Requirement at 31 March 2023 remains achievable.

Authorised Limit						
	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
	£000's	£000's	£000's	£000's	£000's	£000's
Authorised Limit - Borrowing	£523,188	£523,188	£523,188	£523,188	£523,188	£523,188
Authorised Limit - Other long term liabilities	£53,659	£52,233	£50,683	£48,998	£47,167	£47,168
Total Debt	£576,847	£575,421	£573,871	£572,186	£570,355	£570,356

Reconciliation of calculation of Authorised Limit for borrowing:-

Reconciliation of Authorised Limit for Borrowing	
	£000's
CFR - General Services at 31 March 2021	£168,552
CFR - HRA at 31 March 2022	£328,252
Capital Receipts 2018/19 unrealised to date	£-
Capital Receipts 2019/20 to 2022/23	£2,000
Developer/Other Contributions 2018/19 Unrealised to date	£218
Developer/Other Contributions 2019/20 to 2022/23	£24,166
Authorised Limit for Borrowing	£523,188

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 2019/20			
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 now 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 2019/20		
Maturity structure of fixed interest rate borrowing 2019/20	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 2019/20	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%
<i>10 years to 20 years</i>	0.00%	30.00%
<i>20 years to 30 years</i>	0.00%	30.00%
<i>30 years to 40 years</i>	0.00%	30.00%
<i>40 years to 50 years</i>	0.00%	30.00%
<i>50 years and above</i>	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 cash-back the Council's balance sheet reserves. It is expected that the majority of this will be in the form of 12 month fixed term deposits and/or certificates of deposit; however the Council currently have two fixed term deposits with other Local Authorities, with an original maturity period of 2 years, which offer security of funds along with a higher yield as a result of longer duration. With this in mind, the limit for principal sums invested for > 365 days has therefore been set at £70m to give the Council flexibility to extend the duration of deposits that are cash-backing the Council's reserves.