

Annual Investment Strategy

1. Treasury Management Practice: Credit and Counterparty Risk Management

1.1 In 2010 the CLG issued Investment Guidance, which forms the structure of the Council's policy below (please note that these guidelines do not apply to trust funds or pension funds which operate under a different regulatory regime). The key intention of the Guidance is to maintain the current requirement for councils to invest prudently, and that priority is given to security and liquidity before yield.

1.2 In order to facilitate this objective the guidance requires this Council to have regard to the 2011 revised CIPFA publication Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. In accordance with the Code, the Chief Finance Officer (CFO) has produced its treasury management practices (TMPs). This part, TMP 1(5), covering investment counterparty policy requires approval each year.

1.3 Annual Investment Strategy

1.3.1 The key requirements of the Code and investment guidance are to set an annual investment strategy covering the identification and approval of the following:

- 1) The strategy guidelines for choosing and placing investments, particularly non-specified investments.
- 2) The principles to be used to determine the maximum duration for investments.
- 3) Specified investments that the Council will use. These are high security and high liquidity investments in sterling and with a maturity of no more than a year.
- 4) Non-specified investments, clarifying the greater risk implications, identifying the general types of investment that may be used and a limit to the overall amount of various categories that can be held at any time.

1.4 Specified Investments

1.4.1 Sterling investments of less than one year maturity, or those which could be for a longer period but where the Council has the right to be repaid within 12 months. These are considered low risk assets where the possibility of loss of principal or investment income is small. These would include sterling investments which would not be defined as capital expenditure with:

- 1) The UK Government (such as the Debt Management Account Deposit Facility, UK Treasury Bills or Gilts with less than one year to maturity).
- 2) Supranational bonds of less than one year's duration.
- 3) A local authority, parish council or community council.
- 4) Pooled investment vehicles (PIV) with a high credit rating. This covers PIVs such as money market funds, rated AAA by the rating agencies.
- 5) A body (i.e. bank of building society), of sufficiently high credit quality (at least a short term rating of F1 or the equivalent as rated by the three rating agencies).

1.5 Non-Specified Investments

1.5.1 Non-specified investments are any other type of investment (i.e. not defined as Specified above). The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out below. Non specified investments would include any sterling investments with:

Non Specified Investment Category (maturity greater than one year)	
a.	<p>Supranational Bonds</p> <p>(a) Multilateral development bank bonds These are bonds defined as an international financial institution having as one of its objects economic development, either generally or in any region of the world (e.g. European Investment Bank etc.).</p> <p>(b) A financial institution that is guaranteed by the UK Government The security of interest and principal on maturity is on a par with the Government and so very secure. These bonds usually provide returns above equivalent gilt edged securities. However the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.</p>
b.	<p>Gilt edged securities. Government bonds which provide the highest security of interest and the repayment of principal on maturity. Similar to category (a) above, the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.</p>
c.	<p>The Council's own bank if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as is possible. The Council's current bankers are Lloyds Banking Group which is currently supported by the UK government.</p>
d.	<p>Any bank or building society that has a minimum long term credit rating of AA- or equivalent, for deposits with a maturity of greater than one year (including forward deals in excess of one year from inception to repayment).</p>
e.	<p>Share capital or loan capital in a body corporate – The use of these instruments will be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. Revenue resources will not be invested in corporate bodies. There is a higher risk of loss with these types of instruments.</p>
f.	<p>Pooled property or bond funds– normally deemed to be capital expenditure, and as such will be an application (spending) of capital resources. Revenue resources will not be invested in corporate bodies.</p>

1.5.2 Within categories c and d, and in accordance with the Code, the Council has developed additional criteria to set the overall amount of monies which will be invested in these bodies. This criteria is set out in section 11.3 in the body of the report. In respect of categories e and f, these will only be considered after obtaining external advice and subsequent Member approval.

1.6 The Monitoring of Investment Counterparties

- 1.6.1 The credit rating of counterparties will be monitored regularly. The Council receives credit rating information from its advisor as and when ratings change, and counterparties are checked promptly. Any counterparty failing to meet the criteria will be removed from the list immediately by the CFO, and if required new counterparties which meet the criteria will be added to the list.
- 1.6.2 During 2014/15 it is possibly that the UK Government may try and sell its remaining shares in Lloyds Banking Group (Lloyds), thereby removing the support currently provided. To manage this transition it is proposed that the following procedure will be followed should this event occur:
- 1) As soon as the UK Government announces the sale of its remaining Lloyds holding, future investments will be restricted to those allowable for banks with the same credit rating as Lloyds (currently a Fitch rating of A+). Based on the current investment criteria, this would restrict investments to a maximum of 95 days but this will be subject to the credit ratings in place at this time which will continue to be monitored.
 - 2) All investments held at the time of the sale would be held to maturity, subject to agreement from the CFO, in consultation with external advisors. Whilst the UK Government continues to hold a material (>15%) equity stake in Lloyds Banking Group, Lloyds will continue to be viewed as UK Government risk and the current limits will apply.

1.7 Use of External Cash Manager(s)

- 1.7.1 The Council no longer uses an external cash manager within its investment portfolio. Were the Council to use an external cash manager in the future there would be a requirement for the Cash Manager to comply with the Annual Investment Strategy. Any agreement between the Council and the cash manager will stipulate guidelines, durations and other limits in order to contain and control risk. The investment restrictions for a cash manager have been included in the Credit Quality Criteria and Allowable Financial Instruments outlined below.

1.8 Credit Quality Criteria and Allowable Financial Instruments

- 1.8.1 The table on the following page sets out the credit quality criteria for counterparties and allowable financial instruments for Council investments:

Specified Investments: All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' quality criteria where applicable. The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

Counterparty / Financial Instrument	Minimum Credit Rating Criteria / Colour Band	Other Investment Criteria		Use	
		Maximum Duration	Counterparty Limit £m	In House	Cash Manager
Government Supported UK Bank Lloyds TSB: SIBA (Call) Accounts, Term Deposits, CDs, Structured Deposits, Corporate Bonds	Blue	Up to 1 year	£50m	Y	Y
Government Supported UK Bank - RBS SIBA (Call) Accounts Term Deposits, CDs, Structured Deposits, Corporate Bonds	Blue	Up to 1 year	£30m	Y	Y
Other UK Banks & Building Societies * SIBA (Call) Accounts Term Deposits, CDs, Structured Deposits, Corporate Bond	Orange Red Green No Colour	Up to 1 year Up to 6 Months Up to 3 months Not for use	£20m	Y	Y
Multilateral Development Banks Corporate Bonds	AAA	12 months	£10m	Y	Y
Local Authorities: Term Deposits	High Security - not credit rated	12 months	£15m per authority	Y	Y
UK Government (The in house treasury team is limited to holding and selling but not buying UK Government debt). Treasury Bills Gilts DMADF	UK Sovereign Rating	N/A	N/A	Y Y Y	Y Y Y
Money Market Funds	AAA	T+1	£15m per Manager	Y	Y
Managed Funds Gilt Funds/Bond Funds Collective Investment Schemes	Long Term rating for Fitch (AA), Moody's (Aa2), S&P (AA)	T+3	£15m	N Y	Y Y

Non-Specified Investments: These are any investments which do not meet the specified investment criteria and are held for longer than 365 days. A maximum of £55m will be held in aggregate in non-specified investments.

	Minimum Credit Rating – Based on Fitch and S&P’s Ranking			Used By	Support Rating	Maximum Maturity Period	Maximum Value (£ms) of Total Council Investment
	Short-Term	Long-Term	Viability				
Term Deposits – Local Authorities (with maturity in excess of 1 year)	High Security – although not credit rated			In House		3 years	£40m
Term deposits – Banks & Building Societies (maturity in excess of 1 year)	F1 or Equivalent	AA- or Equivalent		In-house	1	2 years	£20m
Certificates of deposit issued by banks & building societies	F1 or Equivalent	AA- or Equivalent		In-house / Cash Manager	1	2 years	£15m
UK Government Gilts with maturities in excess of 1 year	AAA			In-house / Cash Manager		5 years	£20m
Pooled Funds (Various)	F1	AAA		In-house / Cash Manager			£10m
Structured Deposits with variable rates and maturities	F1	AAA	B	In-house / Cash Manager	1	2 years	£10m
Bonds issued by: Financial Institutions with explicit UK government guarantee and Multilateral Development Banks	AAA			In-house / Cash Manager		3 years	£20m
Sovereign Bond Issues (other than UK Government)	AAA			In-house / Cash Manager		3 years	£20m
Bond Funds	AAA			In-house / Cash Manager		3 years	£20m

Key

Short Term Ratings F1 – Indicates the strongest capacity for timely repayment

Long Term Ratings A – Capacity for payment of commitments considered strong
AA – Very strong capacity for payment of commitments
AAA – Exceptionally strong capacity for payment of commitments

Individual Rating B – Strong organisation, no major concerns.
C – Adequate organisation, some concerns regarding its profitability and Balance Sheet.

Support Rating 1 – There is an extremely high probability of external support.
2 – High probability of external support
3 – Moderate probability of support