Treasury Management Strategy Statement 2016/2017, Annual Revenue Provision Policy Statement and Annual Investment Strategy

1 Background

1.1 The Local Government Act 2003 (the Act) and the framework established by CIPFA through its Prudential Code requires the Authority to set Prudential and Treasury Indicators for each of the next three years to ensure that the Authority's capital investment plans are affordable, prudent and sustainable.

1.2 The Act also requires the Authority to set out its Treasury Strategy for borrowing and to prepare an Annual Investment Strategy that sets out the Authority's policies for managing its investments and the priority given to the security and liquidity of those investments.

1.3 The strategy for 2016/2017 covers:

- The current treasury position
- Prospects for interest rates
- Borrowing requirements and strategy
- Annual Revenue Provision policy statement
- The investment strategy
- Debt rescheduling options; and treasury management and prudential indicators for the period 2015-16 to 2018-19

1.4 As a Levying body established under the Local Government Finance Act 1985 and subsequent regulations it is a requirement for the Authority to produce a balanced budget; and in particular to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decision. This means that capital spending increases that lead to increases in revenue costs, whether from additional borrowing or running costs, must be limited to a level which is affordable within the projected income of the Authority for the foreseeable future.

2 Current Treasury position

Borrowing

2.1 At the time of writing this report the Authority currently has outstanding external borrowing of £17.1M, which includes:

Outstanding debt at 6/2/2015	Principal £M	Average rate %
Public Works Loan Board (PWLB) debt	15.116	5.22
Market Debt	2.000	4.01
Total debt	17.116	5.12

2.2 The Market Debt in the table above is held in the form of a Lender Option Borrower Option (LOBO) loan where there are options on the part of the borrower (the Authority) and the lender at specified points in the loan's existence. The maturity profile of the Authority's borrowing (both PWLB and market loans) is shown below:

Loan source	**Amount £M**	**Maturity**
LOBO	2.000	0 – 1 year
		0 – 1 year
PWLB	0.286	0 – 5 years
		5 – 10 years
PWLB	0.300	10 – 15 years
PWLB	3.000	15 – 20 years
		20 – 25 years
		25 – 30 years
PWLB	3.335	30 – 40 years
PWLB	8.195	40+ years

2.3 In line with the Prudential Code, the maturity of borrowing should be determined by reference to the earliest date on which the lender can require repayment. If the lender has the right to increase the interest rate payable (as in the case of the LOBO loan) then this should be treated as a right to require repayment. In accordance with this guidance the maturity date of the Authority's LOBO loan has been taken as the next call date for the loan. In the current interest rate climate it remains unlikely that this loan will be called immediately.

2.4 The Authority's current external debt position (together with forward projections) is shown below. The table shows total external debt against the underlying capital borrowing need (the Capital Financing Requirement – CFR), highlighting that the Authority 'under borrows' compared with the CFR.

External Debt comparison	**2015/16 Actual £M**	**2016/17 Estimate £M**	**2017/18 Estimate £M**	**2018/19 Estimate £M**
Capital financing requirement (CFR) calculation				
- Property Plant and equipment	36,308	295,421	296,951	298,481
- Investment property	0	0	0	0
- Less – revaluation reserve	-7,474	-7,474	-7,474	-7,474
- Plus – Capital Adjustment account	26,553	26,438	35,924	45,410
Capital Financing Requirement (per Prudential Code)	**55,434**	**314,385**	**325,401**	**336,417**
- Less Long Term Lease liability	-11,688	-264,224	-248,242	-232,260

External Debt comparison	**2015/16 Actual £M**	**2016/17 Estimate £M**	**2017/18 Estimate £M**	**2018/19 Estimate £M**
- Less Short term lease liability	-961	-5,052	-15,982	-15982
Total Underlying Borrowing Requirement (A)	**42,785**	**45,109**	**61,177**	**88,175**
External Borrowing				
- Short term	2,000	2,429	2,000	2,000
- Long term	15,259	14,830	14,830	14,830
- Managed by other local authorities (Merseyside Residual Debt)	2,140	1,925	1,710	1,495
Total external debt (B)	**19,399**	**19,184**	**18,540**	**18,325**
Under / (over) borrowing (A-B)	**23,386**	**25,925**	**42,637**	**69,850**

Notes:

**There is a very large increase in the value of property plant and equipment in 2016/17 as well as a similar increase in the long term lease liability. This reflects the accounting treatment required under the Resource Recovery Contract to bring the EfW and RTLS assets and their associated liabilities onto the Authority's balance sheet as required under CIPFA's Code of Practice.*

2.5 Within the prudential indicators there are a number of key indicators to ensure that the Authority operates within defined limits. One of these is that the Authority needs to ensure that its gross debt does not, except in the short term, exceed the CFR in the preceding year plus the estimates of additional CFR for 2016/17 and the following two financial years. The table above shows that the Authority's actual gross debt is comfortably lower than its CFR for the period. The variance, in part, reflects previous strategic decisions to use resources already available to the Authority to negate the need to incur additional borrowing.

2.6 The strategy adopted in previous years has been effective with relatively low long term interest rates allowing the Authority to meet its longer term borrowing requirements, as demonstrated by comparison with its Capital Financing Requirement, at an affordable cost. The Authority has also been able to meet repayment requirements on the external debt without incurring early-repayment premiums and therefore to protect is budgetary position against diminishing investment income while reducing the Treasury risk associated with investment holdings.

2.7 The Authority's use of capital receipts and other reserves to support the capital programme has been important to enable the Authority to maintain a flexible approach to the Treasury Management Strategy. When the receipts and balances have been used it is likely that any growth in the Capital Financing Requirement would need to be accompanied by an increase in the external borrowing in the same year. This need to borrow will be kept under review over the medium term and is in part dependent upon the need for further capital investment. Pressures on reserves and balances are increasingly significant and they may be less freely available to support capital programme works in future.

Investments

2.8 The Authority's funds that are not required for immediate settlement of payments are invested on behalf of the Authority by St Helens Council which provides Treasury Management services under a Service Level Agreement with the Authority. The Council are provided with information from the Authority on prospective dates for the receipt of significant amounts of income (mostly the Levy) and also about when significant payments are due to be made from the Authority (mostly the contract payments in respect of waste services). At the end of 2015/16 it is anticipated that the Authority will have almost £18M available for investment.

2.9 The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management recommends that members be updated on treasury management activities regularly. This Section therefore ensures the Council is implementing best practice in accordance with the Code.

2.10 The Authority's Annual Investment Strategy (which is incorporated into the annual Treasury Management Strategy Statement) confirms that the Authority's investment priorities are the security of capital and liquidity of funds. The Authority's investment dealings in the period therefore have been undertaken in order to achieve the optimum return on its investments commensurate with the proper levels of security and liquidity and having properly assessed all inherent risks. This activity is carried out on behalf of the Authority by St Helens Council's Treasury Managers under the terms of the Service Level Agreement.

2.11 In the current economic climate it is considered appropriate to ensure that all investments are placed with highly credit rated financial institutions in line with the Council's authorised Counterparty List (i.e. those institutions with whom we invest monies).

2.12 On behalf of the Authority the Council actively monitors the creditworthiness of its counterparties utilising information provided by our Treasury Management advisors, Capital Asset Services. During the period September to November the rating agency Fitch made the following revisions to the ratings of two institutions included on the Council's Counterparty List, the details of which are detailed below.

Institution	Aspect of Rating Altered	Old Rating	Revised Rating
Credit Suisse	Long term Short term Viability	AA- F1+ aa-	A+ F1 a+
Sumitomo Mitsui Banking Corporation	Long terms	A-	A

2.13 The Authority currently does not have investments with either institution at present, however the revisions are such that this would not preclude the Authority from investing with either Counterparty in the future.

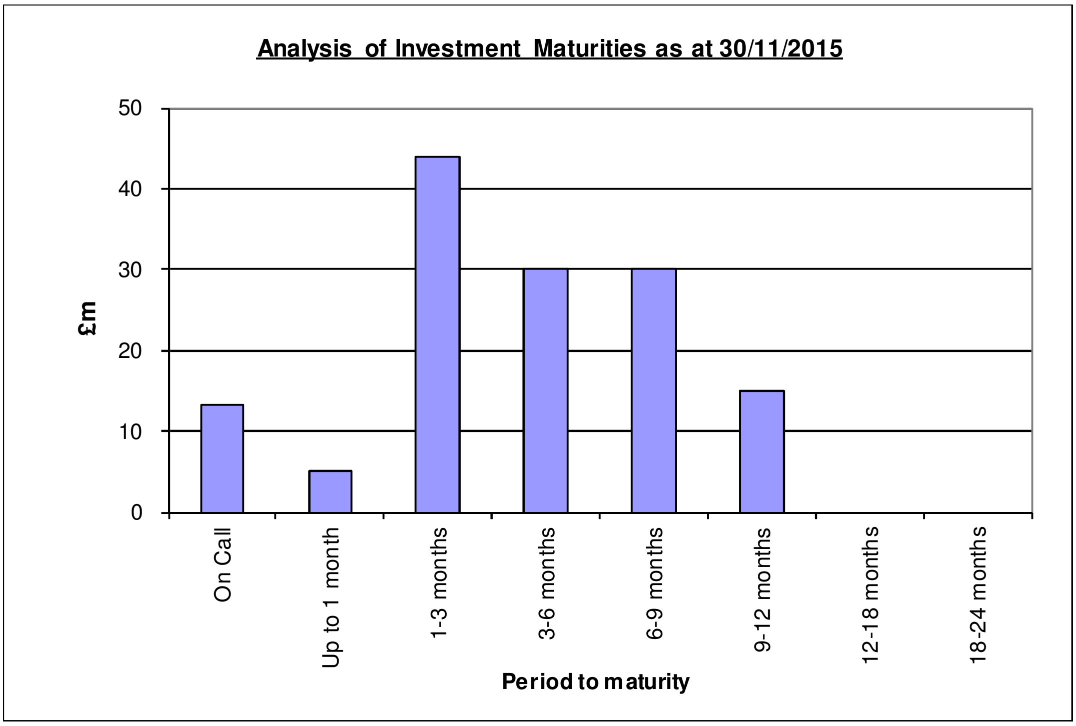
2.14 On behalf of the Authority the Council has sought to maintain a mix of investments with the Counterparties who meet the Council's criteria, however the profile of maturities have been influenced by a number of factors:

i) the availability of advantageous call rates from some high quality Counterparties;

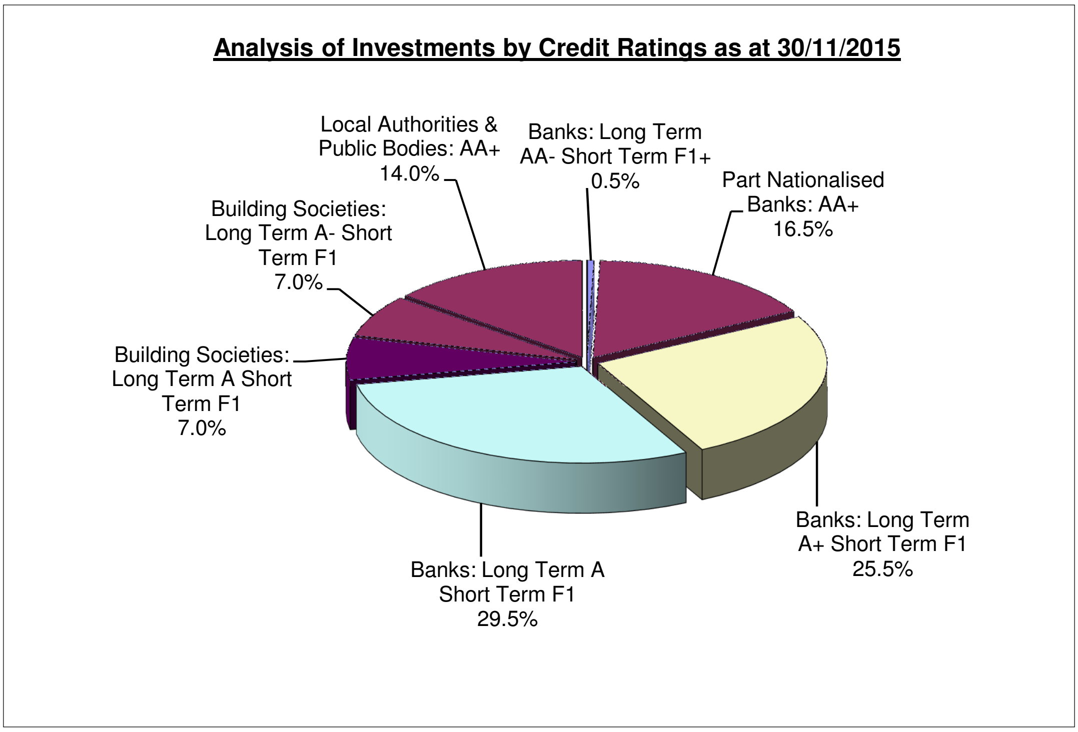
ii) limits on the duration of investments with certain counterparties;

iii) availability of investment opportunities in excess of one year with a number of Counterparties.

The chart over provides an overview of the split in the Authority's investment by maturity as at 30 November 2015.



2.15 At the time of drafting this report the Authority's share of the Council's investments of was split among the Council's investments by type and the credit rating assigned to the different groups of Counterparties.



2.16 Some 30.5% of funds are invested with Counterparties, which have a AA+ or above rating, namely part Nationalised Banks (which carry the UK Government's AA+ rating) and Local Authorities (UK Government's AA+ rating). Of the remaining investments, 62.5% are held with institutions with a Long Term credit rating of at least A with the remaining 7% being held with institutions with a rating of A-.

2.17 Despite the fact that investment rates available in the market remain low, the Council's Treasury Management of the Authority's funds has continued to outperform the benchmarks as detailed in the table below.

Investment Returns 2015/16 up to 30/11/2015

2015/16	Returns Achieved			Benchmark Returns			Performance relative to Benchmarks		
Month	Fixed Term Investments	Call Accounts	**Combined Return** *	12 Month LIBID	7 Day LIBID	**Combined LIBID**	Fixed Term / 12 Month	Call / 7 Day	**Overall +/- return**
April	1.09%	0.41%	**0.93%**	0.85%	0.36%	**0.74%**	0.24%	0.05%	**+0.19%**
May	1.08%	0.40%	**0.93%**	0.87%	0.36%	**0.76%**	0.21%	0.04%	**+0.17%**
June	1.07%	0.42%	**0.92%**	0.89%	0.36%	**0.77%**	0.18%	0.06%	**+0.15%**
July	1.08%	0.42%	**0.90%**	0.93%	0.36%	**0.77%**	0.15%	0.06%	**+0.13%**
August	1.10%	0.44%	**0.94%**	0.94%	0.36%	**0.80%**	0.16%	0.08%	**+0.14%**
September	1.09%	0.46%	**0.97%**	0.93%	0.36%	**0.82%**	0.16%	0.10%	**+0.15%**
October	1.05%	0.43%	**0.97%**	0.91%	0.36%	**0.84%**	0.14%	0.07%	**+0.13%**
November	1.08%	0.42%	**0.99%**	0.91%	0.36%	**0.84%**	0.17%	0.06%	**+0.15%**

2.10 The following table shows the level of funds expected to be available to be invested at the beginning of the year; and those anticipated at the end of the current year:

Reserves and Balances	**31/3/15 £M**	**31/3/16 £M**	**+/- £M**	**+/- %**
General Fund	15.988	16.301	+0.313	+1.95
Capital Receipts Reserve	0	0	0	0
Provisions*	0.885	0.885	0	0
Capital Fund	4.184	2.471	-1.713	-40.9
Total	21.057	19.657	-1.400	-6.64

** this represents provisions that have been set aside from revenue resources over time, not the additional 'accounting' provision set aside in respect of potential liabilities arising from closed landfill sites and for which an equal and opposite capital accounting adjustment has been made rather than charging the provision to revenue.*

2.11 The level of funds the Authority has available for longer term investments is lower than in prior years and the level of investment income will continue to be significantly lower as a result. This reduction in expected interest has been reflected in the revised estimates for the year, as well as in future projections for 2016-17 and beyond. The reduction in investment income will continue to be exacerbated by low level interest rate returns that continue to be forecast into the medium term. While the Treasury Management officers at St Helens Council seek to utilise longer-term fixed rate deposits to lock into favourable rates of return those opportunities are limited to only a small number of counterparties. In the case of the Authority as the amount available for investment reduces the opportunities for the longer term better rate investments will also continue to diminish.

3. Prospects for Interest Rates

3.1 The Authority uses the Treasury Management functions provided by St Helens Council under the SLA. As a part of that function the Council has appointed Capita Asset Services as treasury adviser for both the Council and the Authority. A part of their service is to formulate a view on interest rates.

3.2 Capita's view on interest rates is set out below in the table and the paragraphs which follow:

Annual Average %	**Bank Rate %**		**PWLB Borrowing Rates % (including certainty rate adjustment)**		
		5 year	**10 year**	**25 year**	**50 year**
Dec 2015	0.50	2.30	2.90	3.60	3.50
Mar 2016	0.50	2.40	3.00	3.70	3.60
Jun 2016	0.75	2.60	3.10	3.80	3.70
Sep 2016	0.75	2.70	3.20	3.90	3.80
Dec 2016	1.00	2.80	3.30	4.00	3.90
Mar 2017	1.00	2.80	3.30	4.10	4.00
Jun 2017	1.25	2.90	3.50	4.10	4.00
Sep 2017	1.50	3.00	3.60	4.20	4.10
Dec 2017	1.50	3.00	3.60	4.20	4.10

Mar 2018	1.75	3.30	3.80	4.30	4.20
Jun 2018	1.75	3.40	3.90	4.40	4.30
Sep 2018	2.00	3.50	4.00	4.40	4.30
Dec 2018	2.00	3.50	4.10	4.40	4.30
Mar 2019	2.00	3.60	4.10	4.50	4.40

3.3 The economic data in the table above represents the view of the Authority's Treasury Management adviser Capita, at a point in time. Other views on prospective interest rates are available. However, most are showing an increasing likelihood that there are likely to be some interest rate rises, albeit relatively modest over the short to medium term. Interestingly for the longest term borrowing the prospects for interest rates have softened slightly compared with the previous year's estimate, suggesting there is not yet a confident view that interest rate growth will be strong.

Capita's view on economic propspects

3.4 The following is a snapshot of Capita's view of national and international economic prospects which give a basis for their views on interest rates

UK

3.5 The initial reading of Quarter 3 Gross Domestic Product (GDP) confirmed a slowing of growth. Real output eased from 0.7% to 0.5%, but recovery remains driven by the services sector. Recession still holds in the manufacturing sector, as the volatile construction sector contracted, outweighing the expansion of industrial production. The October Purchasing Managers Index (PMIs), however, suggest that growth will gather pace in Q4. The composite PMI had already picked up in September, after a healthy rise in the manufacturing index and a less robust gain in services offset the decline seen in construction.

3.6 Firms' investment intentions do not appear to have been affected by the turmoil seen on the markets in August or uncertainty over the Government's promised EU referendum. Instead, they suggest that annual investment growth will remain strong in the months ahead. Actual levels of consumer spending have dipped, which is a concern, but strong gains in real earnings should support the ongoing strength of the consumer recovery.

3.7 Mortgage approvals slipped in September but, with mortgage rates remaining low, this should only prove to be a blip.

3.8 The overall trade deficit narrowed in August on strong monthly growth in goods and services exports combining with a decline in imports. The gains in goods exports do, however, have to be put in context and are a rebound from the weakness seen in the previous month. If the deficit were unchanged in September this would leave the overall Q3 deficit considerably higher than that in Q2, at about £11bn, which suggests that there has, at least, been a part reversal of the boost to Q2 growth from net trade. Sterling strength and softer overseas demand will limit export growth and, despite exporters cutting sterling prices to remain competitive, foreign currency export prices have still pushed higher.

3.9 Employment rose by 140,000 in the three months to August, pulling the unemployment rate down to 5.4%. Annualised average weekly earnings growth eased in August but the headline, annualised/three month rate, improved to a healthy 3%. There is little slack left to take up and reductions in unemployment have slowed, while some difficulties in recruiting have fed into earnings growth. Analysts are looking for further labour market improvement and private sector employment intentions remain consistent with healthy jobs growth of around 2%.

3.10 Lower fuel costs, on falling oil prices, saw CPI inflation dip into negative territory in September, at -0.1%, and that figure could weaken further in October, with education's contribution to CPI declining and petrol prices falling, as the impact of oil costs continue to feed through. Petrol's negative contribution to CPI inflation will continue to the turn of the year when oil prices are expected to pick up slightly. In the meantime, inflation will probably average just below zero in Q4. The risks of ingrained low/negative inflation are not seen as significant and households' medium term inflation expectations have flattened, with most indicators now representing steady or slightly upward domestic inflation. Food inflation will remain weak for a while yet, before picking up in later 2016, and there are upside risks to services inflation as stronger pay growth adds to demand in the sector. The benefits of past sterling strengthening should also start to fade, which should see imported goods inflation increase. While inflation is expected to be stronger in 2016, gains in productivity should ensure that the BoE's 2% target is not threatened for a while yet.

US

3.11 Overseas influences continue to impact on the factory sector, while falling mining production was partly down to declining domestic oil production. This was inevitable after drilling activity slumped recently. There was another fall in drilling activity in September but further contraction is unlikely unless oil prices dip again. Export biased manufacturers continue to be haunted by the stronger $, but those more domestically facing are faring better. The average of the ISMs remains strong and indicative of 3% annualised GDP growth, but surveys are reflective of manufacturing activity remaining subdued for the rest of the year.

3.12 Retail sales were soft in September, but this was partly a reaction to the price related fall in gasoline sales. Outside "gasoline", sales did not see spending gains except, to a degree, in auto sales. Underlying sales were flat, however, but still fairly strong over Q3 as a whole. Improved real household incomes from falling gasoline prices over the last year should result in improve real consumption. If all gains were spent it would see additional real consumption growth of 1%.

3.13 Consumer confidence levels have picked up, and indicate annualised real consumption growth of around 4%. Fresh declines in oil drilling activity means investment in mining structures could prove a drag for some time yet. Equipment investment has improved but remains significantly lower than a year ago, and survey evidence remains downbeat.

3.14 Inventory (stock) accumulation growth has slowed and this area alone could take 1.5% off Q3 GDP growth, which would reverse earlier gains. Deceleration is not expected to turn into collapse, and surveys indicate non-petroleum inventories will maintain growth.

3.15 The increased August trade deficit reflects the strength of the US $ and weaker global demand levels. Exports fell by 2% m/m, partly down to declining commodity prices. Contrastingly, levels of imports remain high. Q3 real exports are forecast to be relatively flat, whereas real imports are likely to have risen by in excess of an annualised 4%, which will result in net external trade acting as a drag of 0.7% on Q3 GDP. This spread between exports and imports is set to continue if surveys are correct.

3.16 Recent slowing in payroll growth has still left unemployment on the verge of its long run natural rate. The deceleration has been most notable in the private sector and goods production. The greatest deterioration in recent months has been in areas least affected by cyclical swings or currency shifts, but with job openings improving it suggests that a factor could be a mismatch of skills. This appears to be supported by businesses comments that labour quality is an issue, which points to further wage growth acceleration ahead. Inflation is being suppressed by the strong dollar and lower commodity prices, but there are signs of upside domestic inflationary pressures. Annualised CPI fell to 0% in September, but was a result of slumping gasoline prices. As 2014's larger energy price fall drops out of the calculation, there should be a bounce in the headline rate to around 2% in early 2016. Core prices increased 0.2% month on month, pushing the annualised rate to 1.9%. Underlying all of this, core services' inflation remains negative, but core services' prices are accelerating. Headline producer prices' growth is negative, with $ strength putting downward pressure on import prices, but the core picked up 0.3%. Domestic price pressures are, though, building as unit labour costs pick up. This suggests that core inflation will push through 2%.

3.17 Short term inflation expectations have declined, driven by crude oil price falls. However, lower longer term expectations are harder to explain, given that they are lower than the low point of the deflationary worries in 2010. Household expectations remain little changed. There are concerns, though, about the global economy slowing and its impact on the value of the $.

3.18 An interest rate move was finally made late in 2015 albeit only by 0.25% as concerns over the labour market remain .

Eurozone

3.19 The EZ economy has maintained its steady growth into Q4, if surveys are correct. The composite PMI edged higher and is consistent with quarterly growth of 0.4%, the same as Q2 and that indicated in Q3. The October Economic Sentiment Indicator also rose, for a fourth straight month, which suggests that annualised growth will improve to around 2%. This would mean a slight uplift in quarterly growth in Q3, which is better than both the PMIs and hard data have implied. German and Spanish recoveries seem to be weakening, according to the surveys, but French and Italian news appears better. Consumer spending has been helped by ongoing low inflation in Q3. With retail sales up 0.6% in July but flat-lining in August, annual growth remains above 2%. September data shows that sales strengthened in Germany and Spain, but dipped in France. Taking the weighted average of retail and car sales, which showed strong quarterly Q3 growth, household spending growth appears to have gathered pace, as has confidence among retailers, which indicates that sales may have increased as Q4 opened.

3.20 There is however, a dark cloud, in this case the fall in consumer confidence, which indicates that household spending growth could slow, with the dip in confidence most marked in Germany. The industrial sector had another poor month in August, with overall production falling by 0.5%, pulling annual growth lower to 0.9%. All four of the major economies saw production growth slow. Only Italy, among the big four economies, has seen its PMI improve since August. Nevertheless, the manufacturing PMI reflects annualised growth of 2% in the bloc for the rest of the year.

3.21 The services sector sees growth remaining strong and the PMI is reflective of quarterly growth of slightly lower than 0.5%, while the measure of confidence among services firms points to annualised growth of about 2.0%. The trade surplus has held near historical high levels, supported by the weaker €uro, but it did narrow in August, as exports slowed faster than imports. Having gathered pace early in 2015, export values' growth has been tailing off in all of the frontline economies. Indeed, export expansion has been weaker than the fall in the currency. That declining pace of growth may well be compounded if further currency depreciation is not seen. However, EC survey evidence suggests export orders should remain relatively buoyant for the coming months, and PMIs seem to support this.

3.22 The labour market continues to move in the right direction, albeit slowly. The rate of unemployment fell to 10.8% in September, as no member state saw numbers increase for the first time in eight years. Surveys are only indicating that employment growth will remain gradual, driven by the services sector. Manufacturing is recruiting far more modestly. Household unemployment expectations worsened in October with most seeing increases in the year ahead which, coupled with low inflation expectation ECB to further ease monetary policy.

3.23 Headline CPI returned to positive figures in October as goods and services inflation pushed core inflation higher. The former should ease as the impact of the weaker €uro has largely passed. Much of the previous falls in domestic cost pressures has still to filter through, while services inflation looks set to remain modest. Inflation expectations are for inflation to remain well below the ECB target level, and though energy effects will dissipate, pushing inflation higher in coming quarters, price pressures will remain at historic low levels. The prospect of monetary policy divergence is the market focus following the Fed retaining the possibility of delivering a US rate hike this year and the growing likelihood that the ECB will increase policy support, both possible in December. The €uro has lost ground to the US$, and EZ government bond yields have fallen. Additionally, equity markets bounced more strongly than those in the UK and US in October. This was on the back of investor hopes of further QE, as business and consumer sentiment improvement does not warrant such gains.

Asia

3.24 Asian economies are continuing to struggle in the wake of the weakening Chinese economy, a major trading partner in the area. The authorities there remain steadfast in their desire to rebalance the economy towards greater domestic input to growth. Whilst this is proving painful the longer term benefits should prove beneficial. In the meantime, the central bank, the People's Bank of China, cut benchmark interest rates to offer support to the ailing economy. Moreover, by removing the regulatory ceiling on banks' deposit rates they have removed the final bar to liberalising interest rates sooner than hoped. Whilst this may have little short term impact, with low benchmark rates and easy policy, current circumstances cannot last, and in time the changes will allow greater competition between banks. On the economic front, though data/surveys remain soft there are signs that there has been some stabilisation, which offers hope of a bounce in fortunes.

Summary and interest rate view

3.25 In the USA, Fed officials have finally raised interest rates this year, albeit by a relatively small amount. We still see a UK rate rise being somewhat later than that in the US, probably in the second half of 2016 but comments from Bank of England Governor, Mark Carney, continue to confuse at times, with hints that early rate hikes cannot be discounted being countered with other comments that possibly suggest otherwises,will keep wage growth subdued.

4. Borrowing requirement and strategy

4.1 The Authority's in year borrowing requirement for the next and subsequent two financial years are based on the requirements arising from the proposed Capital Programme included in the budget report and calculated as:

	2015/16 £M	**2016/17 £M**	**2017/18 £M**
Prudential borrowing	0	0	0.514
Revenue provision	(1.203)	(1.203)	(1.185)
In year capital financing requirement	(1.203)	(1.203)	(0.671)

4.2. These requirements are calculated as:

(i) that element of the proposed Capital Programme not financed by specific grant, capital receipts or earmarked balances:

(ii) less the Annual Revenue Provision, as calculated by reference to the Capital Finance and Accounting Regulations 2008 (as considered in section 5).

4.3 The table shows that the in-year capital financing requirement during the three year period is negative. This reflects the Authority's capacity to support the capital programme without the need to borrow additional amounts until 2017/18 when there is the prospect of a small additional borrowing requirement to fulfil the capital programme in that year.

4.4 The current position is a product of previous decisions to use cash arising from available reserves and balances to negate the need to borrow. With historically and abnormally low Bank Rates, the avoidance of new external borrowing has reduced costs in the short term and reduced longer term exposure to interest rate and credit risk.

4.5 The prospect of returning to borrowing during 2017/18 to fulfil the proposed capital programme in that year will be kept under review in light of changes to the requirements for capital expenditure that may be made before then. Given the likelihood of increases in borrowing rates, albeit the timing remains uncertain, there is a risk that any future borrowing may attract higher rates than are currently available.

4.6 Given the prevailing uncertainty the continuing need for caution will underpin the Authority's approach to Treasury Management via St Helens Council. Where conditions are considered to have changed so that they could have an impact on the Authority's underlying financial position Members will be advised and their views sought on which option available provides the most appropriate course of action for the Authority.

5. Annual Revenue Provision Statement

5.1 Under Regulation 27 of the Capital Finance Regulations, Local authorities are required to charge their revenue account for each financial year with a Minimum Revenue Provision (MRP) to account for the repayment of principal in that financial year. The requirement to make this statutory provision was amended under regulation 28 of the Capital Finance Regulations 2008. The current Regulation 28 sets out a duty for a Local Authority to make an amount of Minimum Revenue Provision (MRP) which it considers to be prudent.

5.2 Under Regulation 28, Authorities are provided with a number of alternative approaches, which can be adopted for the purpose of calculating a 'prudent provision'. The approach by an authority should be outlined in a Statement and submitted to the Authority for consideration. The statement below outlines the approach the Authority undertakes in the calculation of its revenue provision.

5.3 The Authority policy is to estimate MRP based on the Asset Life method. Department of Communities and Local Government (DCLG) guidance is that this method may only be used for capital expenditure incurred after 1 April 2008 (para 16); capital expenditure incurred before 1 April 2008 has to be charged based on the regulatory method ie. 2% of opening Capital Financing Requirement (para 16). For finance leases and PFI schemes, the MRP to be charged is the principal element of the contract (para 20).

5.4 Para 8 of the DCLG MRP Guidance states that for the CFR method of calculating MRP this 4% of the CFR for the preceding year. Para 16(a) of the DCLG MRP Guidance states that Options

1 and 2 can only be used for capital expenditure incurred before 1 April 2008. This has the following consequences:

- MRP for 2008/09 will be solely based on the CFR for 31/3/2008, because MRP under the Asset Life method only starts in the year following the capital expenditure being incurred (para 10 of the DCLG MRP Guidance refers);
- Because the Authority opted to use the Asset Life method for all capital expenditure incurred after 1 April 2008, it follows that the CFR method will effectively be based solely on the CFR as at 31/3/2008, because all subsequent expenditure will be on the Asset Life method and revaluations of pre 1 April 2008 capital expenditure will be neutral to the CFR, because upward asset revaluations will be equally matched by upward increases in the Revaluation Reserve for each asset (and vice versa for impairments).

5.5 Para 20 of the DCLG MRP Guidance states "In the case of finance leases and on balance-sheet PFI contracts, the MRP requirement would be regarded as met by a charge equal to the element of the rent/charge that goes to write down the balance sheet liability." The Authority has no finance leases, therefore the only MRP under this option will be the "principal" on the Veolia and on the Sita UK service concession contracts. This will be reviewed when the assets associated with the Resource Recovery Contract (RRC) are brought onto the Authority’s balance sheet and MRP calculations will be required.

6. Annual Investment Strategy

6.1 Alongside the Treasury Management Service provided by St Helens Council the Authority will have regard to the DCLG’s Guidance on Local Government Investments and CIPFA’s Code of Practice when working with the Council, which conducts investment activity on behalf of the Authority. The overriding priority of both the Authority and the Council are that security and liquidity of funds are of paramount importance.

6.2 In accordance with the above, and in order to minimise the risk to investments the Authority supports the Council’s approach to clearly stipulated minimum acceptable credit quality of Counterparties for inclusion on the Council’s lending list. The creditworthiness methodology used by the Council to create the Counterparty list takes account of ratings provided by FITCH, one of three main ratings agencies. All investments made during 2016/17 will be in accordance with the Annual Investment Strategy, which is detailed in annex 1 and mirrors the Council’s Strategy.

6.3 In keeping with previous decisions, the Authority has agreed with the Council’s strategy to seek to lock in longer period investments where opportunities and Counterparty criteria permits. At the same time the Council’s treasury managers have made maximum strategic use of its call facilities and Money Market Funds (MMFs) for cash flow generated balances and to ensure liquidity. This will continue during 2016-17, subject to:

i. The outlook for medium term interest rates (i.e. to avoid locking into deals whilst investment rates are at historically low levels and there is a forecast pick up in rates over the medium term);
ii. The management of counterparty risk
iii. Any opportunities to repay debt using available investments
iv. The Authority's liquidity requirements

7. Debt Rescheduling

7.1 Debt rescheduling has historically been undertaken in order to:

i. Generate cash savings at minimum risk;
ii. Amend debt maturity profiles and / or the balance of volatility;
iii. Aid fulfilment of the Authority's overall borrowing strategy.

7.2 Due to the expectation of short term borrowing rates being considerably cheaper than longer term rates there may be some limited opportunities to generate savings by switching from long term to short term debt. However, these potential savings will need to be considered in light of their potentially short term nature and the likely additional cost of refinancing those short term loans, once they mature, compared with the current rates of longer term debt in the existing portfolio.

7.3 Consideration will also be given to whether there is potential for making savings by running down investment balances by repaying debt prematurely (as short term investments are likely to be lower than rates paid on currently held debt). Due to the existence of higher redemption interest rates on PWLB debt premiums are highly likely to compromise such opportunity.

7.4 While the Prudential Code allows the premium costs arising from debt rescheduling to be funded from capital receipts, the Authority currently has no such receipts. There are no plans to sell any assets to generate such receipts, although in the event that such a sale took place and a receipt were to be generated the Authority would have another option to reduce liabilities arising from borrowing activity and to reduce longer term revenue costs.

7.5 Should any rescheduling opportunities arise that create potential for improvement in the Authority's financial position, prudence will be exercise and any actions will be reported as appropriate to the Authority.

8. Treasury Limits and Prudential Indicators 2015/16 to 2018/19

8.1 It is a statutory duty under Section 3 of the Local Government Act 2003 and supporting Regulations for the Authority to determine and keep under review how much it can afford to borrow. The amount so determined is the "Affordable Borrowing Limit".

8.2 The Authority must have regard to the Prudential Code when setting this limit. The Code also sets a series of limits and indicators that the Authority must consider.

8.3 The proposed limits and indicators required for approval for the period 2015/16 to 2018/19 are contained in Annex 2.

8.4 The Treasury Management and Prudential limits were not breached in the year 2015-16 up to 31 December 2015.

9. CIPFA Code of Practice: Treasury Management in the Public Services (the Code)

9.1 The Authority has affirmed annually that it continues to adopt the Code as a part of the budget reports. This year the Authority is requested to confirm formally the adoption of the Code and its relevant clauses as set out in Annex 3 and in the Treasury Management Policy Statement at Annex 4.

Annex 1

Annual Investment Strategy 2016/17

1. Purpose

1.1 This strategy is submitted to the Authority for approval in accordance with the guidance issued by the then ODPM under section 15 (1)(a) of the Local Government Act 2003.

1.2 The strategy covers the period to 31 March 2017 and complements the Treasury Management Strategy 2016/17 and the Treasury Management practices that are adopted as required by the CIPFA Code of Practice: Treasury Management in the Public Services.

1.3 In doing so the Annual Investment Strategy sets out:

- which investments the Authority (working with St Helens Council) may use for the prudent management of any surplus funds during the period, under the heads of Specified Investments and Non-Specified Investments;
- the procedures for determining the use of each asset class;
- the maximum periods for which funds may be prudently committed in each class;
- the upper limits to be invested in each class;
- the extent to which prior professional advice needs to be sought both from the Authority's Treasury Advisers and the Council Treasury Managers prior to the use of each class; and
- the minimum amount to be held in short term investments

2. Investment Objectives and Principles

2.1 The general policy objective for the Authority is the prudent investment of its surplus funds. The Authority's investment priorities are the security of capital and the liquidity of investments.

2.2 The Authority will work with St Helens Council as its investment managers to achieve the optimum return on its investments, commensurate with the proper levels of security and liquidity and having properly assessed all inherent risk, as detailed in its Treasury Management Practices.

2.3 The Authority will work with St Helens Council to ensure that temporary borrowing will not be made whilst the Authority has investment funds available and its longer term borrowing activity will have full regard to the content of CIPFA's Prudential Code and the Authority's own approved Treasury Strategy. In particular the Authority will not engage in treasury borrowing activity that is solely for the purposes of investment or on-lending to make a return.

3. Specified and Non-Specified Investment Types

3.1 Investment Instruments are broadly classified within government guidance as being Specified or Non-Specified.

3.2 An investment is a Specified Investment if:

a) the investment is denominated in sterling and any payments or repayments of the investment are only in sterling
b) the investment is not a long term investment
c) the making of the investment is not defined as capital expenditure by virtue of Regulation 25 (1)(d) of the Local Authorities (Capital Finance and Accounting) Regulation (England) Regulations 2003 (SI 3146 as amended); and
d) the investment is made with a body or investment scheme which has been awarded a high credit rating by a credit rating agency or is made with the UK Government, a Local Authority in England and Wales (as defined in Section 23 of the Act), a Parish or Community Council.

3.3 Non-Specified Investments are those investments not meeting the definition of a specified investment and, inherently, are subject to greater degrees of treasury risk. They do, however, offer some potential diversification. As a result, and as part of an overall strategy, a small number are identified via St Helens Council's Treasury Managers as being potentially suitable for use, dependent upon prior consultation and advice from the Authority and the Council's shared Treasury Management consultants.

3.4 In assessing the relative characteristics of each possible instrument type, the risk attached in their use and how their use would assist in the delivery / achievement of the Authority's investment objectives and principles, Annex A has been prepared to detail those instruments that are proposed may be used as part of the investment strategy.

4. Credit and Counterparty Policies

4.1 The Authority is guided by the Council which relies on credit ratings published by FITCH, an independent rating agency to establish the credit quality of Counterparties (issuers and issues) and investment schemes. Credit Rating lists are reviewed by the Council on a regular basis to ensure prompt action to remove institutions whose ratings fall below the Council's threshold (which safeguards the Authority). The Council's Treasury Management Practices document the approach to this review.

4.2 The Council's Treasurer has a delegated authority from the Council to establish the criteria by which the lending list is compiled for internally managed investments. The Authority is consulted on the criteria for the list, which is contained in annex B.

5. Liquidity of Investments

5.1 The need to ensure liquidity by the continuous management and monitoring of the Council and the Authority's cash transactions and resources is one of the key objectives of the

Treasury function and the approach to liquidity risk management is fully documented in the Council's Treasury Management Practices.

5.2 The limits included in Annex A are a reflection of the overriding importance of liquidity, and in addition to those, as a general rule the Council aims to ensure that it has a minimum of 15% of the investments it makes for the Authority and the Council held with a maturity of less than one week at all times. Where cash-flow expectations dictate, this general rule will be amended accordingly.

6. Investment Strategy – Internally Managed Investments

6.1 All investments made in the duration of this strategy will comply fully with the strategy.

6.2 Decisions taken within the framework, regarding the period and type of investment, will be taken having regard to future cashflow requirements and likely interest rate movements. A suitable proportion of investments will be held "at call" for contingent purposes to allow for any significant investment opportunities for longer periods that may become available.

6.3 The relatively low base rate over recent years has led the Council's treasury Managers to seek, where possible, to lock in to fixed rate deals at advantageous rates through the use of special tranche deals. This practice will continue in 2016/17, subject to:

i. The outlook for medium term interest rates (i.e. to avoid locking into deals whilst investment rates are at historically low levels and there is a forecast pick up in rates over the medium term);
ii. The management of Counterparty risk;
iii. Any opportunities to repay debt using available investments; and
iv. The Authority and the Council's liquidity requirements

6.4 working on behalf of the Authority and the Council, maximum strategic use will be made of the Council's competitive call account facilities and the AAA rated money market funds to which the Council and the Authority have access to during the period.

7. Investment Strategy – Externally Managed Funds

7.1 Neither the Authority, nor its agent the Council, currently engage any Fund Managers to invest monies on their behalf. This has been the position since a Treasury Management review of fund manager activity and the decision in 2007 to repatriate funds held by the then fund manager.

7.2 Arrangements for the re-engagement of fund managers at a future point may be considered in consultation with the Council and the appointed Treasury Management consultants. If it were to be considered that the engagement of a fund manager may be warranted, then the Authority would work with the Council to ensure that a full tender exercise be considered and a formal agreement would be entered to determine the scope of activity.

8. Reporting arrangements

8.1 The Authority will receive reports on the activities planned and undertaken at least twice each year, as part of the budget setting exercise and as part of the closedown of the Authority's year end accounts. In addition if there are any matters during the year that require the Authority to consider then reports will be made directly to the Authority.

Annex A

Local government Investments (England)
Specified versus Non-Specified Investments

The English Investment Guidance issued by the ODPM on 22 March 2004 defined Local Government investments as being either “Specified” or “Non-Specified”. The guidance was, however, non-prescriptive in classifying the various investment instruments available into either of these categories. Indeed, in a continually changing market where new innovative ‘products’ are frequently being introduced it would be extremely problematical, if not impossible to do.

Much focus and emphasis is therefore place on that element of the Guidance which states that Specified Investments should require “minimal procedural formalities”. The Authority and the Council’s Treasury Management advisers have discussed this issue directly with the DCLG, who have expressed their desire to see Local Authorities apply the spirit of the Guidance rather than focus on a legalistic approach to the meaning of words in the Guidance. The spirit of the Guidance is that investment products, which take on greater risks and therefore should be subject to greater scrutiny should be subject to more rigorous justification and agreement of their use in the Annual Investment Strategy and so should fall into the Non-Specified category.

The following tables have been drafted on that basis.

Appendix 1

Local government Investments (England)
Specified Investments

All "Specified Investments" listed below must be sterling denominated with maturities of up to 1 year

Investment	Repayable / Redeemable within 12 months?	Security / Minimum credit rating	Use for managing internal investments	Maximum period
Debt Management Agency Deposit Facility (DMADF)	Yes	Govt-backed	Yes	6 months
Term deposits with UK Government or with UK local Authorities (i.e. Local Authorities as defined under section 23 of the 2003 Act) with maturities up to 1 year	Yes	High security although local authorities are not credit rated	Yes	1 year
Term deposits with credit-rated deposit takers (Banks and Building Societies) with maturities up to 1 year	Yes	See*	Yes	1 year
Money Market Funds (i.e. a collective investment scheme as defined in SI 2004 No. 534). *These funds do not have any maturity date*	Yes	Yes: AAA	Yes	*The period of investment may not be determined at the outset but would be subject to cash flow and liquidity requirements*
Forward deals with credit rated Banks and Building Societies < 1 year (i.e. negotiated deal period plus period of deposit)	Yes	See*	Yes	1 year in aggregate
Callable deposits with credit rated Banks and Building Societies, with maturities not exceeding 1 year	Yes	See*	Yes	1 year
Call Account Facilities with credit rated deposit takers (Banks and Building Societies)	Yes	See*	Yes	n/a

**Subject to approved credit rating criteria as determined in the Annual Investment Strategy of St Helens Council as the Authority's agent, or as a result of delegation by the Council to the St Helens Treasurer in accordance with the Council's Treasury Management Practices.*

Local government Investments (England)
Non-Specified Investments

Investment	Repayable / Redeemable within 12 months?	Security / Minimum credit rating	Use for managing internal investments	Maximum maturity of Investments
Term Deposits with credit rated deposit takers (Banks and Building Societies) with maturities greater than 1 year	No	See*	Yes	3 years
Term deposits with UK Government or with UK local Authorities (i.e. Local Authorities as defined under section 23 of the 2003 Act) with maturities greater than 1 year	No	High security although local authorities are not credit rated	Yes	3 years
Certificates of Deposit with credit rated deposit takers (Banks and Building Societies) *Custodial arrangement required prior to purchase*	Yes	See*	Yes – after consultation with external Treasury Consultants	3 years
Callable deposits with credit rated deposit takers (Banks and Building Societies) with maturities greater than 1 year	Potentially	See*	Yes	3 years
Forward deposits with credit rated Banks and Building Societies for periods > 1 year (i.e. negotiated deal period plus period of investment)	No	See*	Yes – after consultation / advice from eternal Treasury Consultants	3 years in aggregate
Structured Deposits where investment returns are determinant on how specified interest rate structures move over a determined period	Potentially	n/a	Potentially – after consultation / advice from eternal Treasury Consultants	3 years

**Subject to approved credit rating criteria as determined in the Annual Investment Strategy of St Helens Council as the Authority's agent, or as a result of delegation by the Council to the St Helens Treasurer in accordance with the Council's Treasury Management Practices.*

Appendix 1

Counterparty Criteria 2015/16

Counterparty category		**Credit ratings**					**Maximum Investment (1)**	**Maximum period**
(i)	Part Nationalised banks	See below (2)					£25M £35M for RBS group	2 years including on call
(ii)	Money Market Funds (MMF)	AAA rated (3)					£25M per MMF (£100M total)	On call
(iii)	Other local authorities and public bodies	AAA rated					£50M	2 years
FITCH RATINGS		**Long term**	**Short term**	**Viability**	**Support**	**Sovereign**		
(iv)	Authorised institutions (under the Banking Act 1987) which hold a suitable credit rating	AA- and above	F1+	aa- and above	1	AA+ and above	£25M	2 years
		A and above	F1 and above	a- and above	1	AA+ and above	£20M	12 months
(v)	Call accounts held with authorised institutions (under the Banking Act 1987) which hold a suitable credit rating	AA- and above	F1+	aa- and above	1	AA+ and above	£25M	On call
		A and above	F1 and above	a- and above	1	AA+ and above	£20M	On call
(vi)	Building Societies which hold a suitable credit rating	AA- and above	F1+	aa- and above	1	AA+ and above	£15M	2 years
		A and above	F1 and above	a- and above	1	AA+ and above	£10M	12 months

Notes to Counterparty Criteria

1. For each institution meeting the criteria above and subject to the limits for maximum investments, no single investment transaction should be undertaken for more than £10M.

2. In interpreting the lending criteria detailed above it should be accepted that the part nationalised banks in the UK (Lloyds Group and Royal Bank of Scotland Group) have credit ratings that do not conform to the credit criteria used by Local Authorities to identify banks which are of high credit worthiness. In particular as they are no longer separate institutions in their own right it is impossible for Fitch to assign them an individual rating for their stand-alone financial strength. However, these institutions are recipients of an F1+ short term rating as they effectively take on the credit worthiness of the Government i.e. deposits made with them are effectively being made to the Government. They also have a support rating of 1; in other words, on both counts they have the highest ratings possible. Until such time as a decision is made by the Government to dispose of their interests in these banks, investments in these institutions can be made on the basis that they meet the highest criteria.

3. Each individual Money Market Fund (MMF) used must be separately approved by the St Helens Treasurer via a St Helens Council Administrative Decision.

Appendix 1
Annex 2

Treasury Limits and Prudential Indicators

Treasury Limits and Prudential Indicators 2015/16 to 2017/18			**2015/16 Revised**	**2016/17 Estimates**	**2017/18 Estimates**	**2018/19 Estimates**
1(i)	Proposed capital expenditure that the Authority plans to commit during the forthcoming subsequent two financial years	**Capital Expenditure (£M)**	1.478	0.100	0.100	0.100
1(ii)	Additional in year borrowing requirement for capital expenditure	**In year Capital Financing Requirement (CFR) (£M)**	(1.213)	(1.213)	(1.185)	(1.185)
2	The CFR is an aggregation of historic and cumulative capital expenditure which has yet been paid for by either revenue or capital resources	**Capital Financing Requirement as at 31 March (£M)***	55.343	314.385	325.401	336.417
3	The 'net borrowing' position represents the net of the Authority's gross external borrowing and investments sums held	**Net Borrowing requirement:** **External borrowing (£M)** **Investments held (£M)**** **Net requirement (£M)**	19.399 (19.782) **(0.383)**	19.184 (9.811) **9.373**	18.540 (0.885) **17.655**	18.325 (0.885) **17,440**
4	Identifies the impact and trend that the revenue costs of capital financing decisions will have on the General Fund budget over time	**Ratio of financing cost to net revenue stream**	2.97%	3.08%	3.11%	3.05%
5	The Authority's budget strategy has been to support capital spending from reserves set aside, in future to fund the capital programme additional borrowing is likely to be required	**Incremental impact of capital investment decisions (increase in Levy %)**	0	0	0	0
6	This represents an absolute limit on borrowing at any one	**Authorised limit for External Debt (£M)**	24.978	24.763	24.119	24.904

	point in time. It reflects the level of external debt which, while not desired, could be afforded in the short term but which is not sustainable in the longer term					
7	This is the limit beyond which external debt is not normally expected to exceed	**Operational Limit for External Debt (£M)**	21.338	21.123	20.479	20.264
8	These limits seek to ensure that the authority does not expose itself to an inappropriate level of interest rate risk, and has a suitable proportion of debt	**Upper limit for Fixed Interest Rate Exposure**	100%	100%	100%	100%
		Upper limit for Variable Interest Rate Exposure	50%	50%	50%	50%
9	This limit seeks to ensure liquidity and reduce the likelihood of any inherent or associated risk	**Upper Limit for Sums Invested over 364 days**	60%	60%	60%	60%

* *CFR calculation includes assumptions about the treatment of assets under IFRIC 12 as part of the Resource Recovery Contract (RRC), there are offsetting lease liabilities which will also feature in the authority's balance sheets in future years*

** *includes assumptions about the release of surplus funds from MWHL in 2015-16 and then again in 2017-18 but the latter funds release will depend upon the delivery of the RRC*

Appendix 1
Annex 3

Adoption of the CIPFA Treasury Management in the Public Services Code of Practice and cross sectorial-guidance notes

The 2011 revision of the CIPFA Code recommends that all public service bodies formally adopt four specific clauses as contained in the Code. All requirements of the Code are implemented through the governance frameworks, policies, systems, procedures and controls in place both in the Authority and the Council which provides Treasury Management functions, and will continue to be so. For completeness it is recommended that the Authority formally approve the following:

1 The Authority will create and maintain, as the cornerstones for effective treasury management:

- A treasury management policy statement, stating the policies, objectives and approaches to risk management of its treasury management activities. In the case of the Authority this will mirror the policy statement of St Helens Council which provides the Treasury Management function for the Authority.
- The use of suitable Treasury Management Practices (TMPs) as developed by St Helens Council, which set out the manner in which St Helens, on the Authority's behalf, will seek to achieve those policies and objectives, and prescribing how it will manage and control those objectives.

2 The Authority will receive reports on the Treasury Management policies, activities and practices carried out on its behalf, including as a minimum an annual strategy and plan in advance of the year and an annual review after the year end, together with such updates as may be required where there are unplanned changes.

3. The Authority will work with the Director of Finance in the administration of Treasury Management decisions, and in particular the Director of Finance will liaise closely with the St Helens Treasurer to whom the Authority has delegated the day to day operation of Treasury Management policy and practices on behalf of the Authority under a Service Level Agreement (SLA). The Council will act in accordance with the approved Policy Statement, and TMPs and the CIPFA Standard of Professional Practice on Treasury Management.

4. The Authority is responsible for ensuring effective scrutiny of the treasury management strategy and practices.

Annex 4

Treasury Management Policy Statement

The policies and objectives of the Treasury Management function under the SLA are defined as follows:

1. Treasury Management is ‘the management of the Authority’s investments and cash flows; its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks’.

2. The successful identification, monitoring and control of risks are the prime criteria by which the effectiveness of its Treasury Management activities will be measured. Accordingly, the analysis and reporting of Treasury Management activities will focus on their risk implications for the Authority.

3. It is acknowledged that effective Treasury Management will provide support towards the achievement of its business and service objectives and the Authority is committed to the principles of value for money in Treasury Management, and to employing suitable comprehensive performance measurement techniques within the context of effective risk management.