Appendix A

Economic Background 1 April 2017 to 30 September 2017

Growth in the UK expanded at a much slower pace as evidenced by Q1 and Q2 Gross Domestic Product (GDP) growth of 0.2% and 0.3% respectively, leading to a 1.5% year-on-year rate (as at the end of June 2017). The annual Consumer Price Index (CPI) measure of inflation increased to 3.0% as at the end of September 2017, its highest since June 2013 as the lower level of sterling continues to boost consumer prices. Inflation is likely to remain above the Bank of England's Monetary Policy Committee (MPC) 2.0% target over much of the next three years. The labour market saw the unemployment rate for the three months to 31 August 2017 remain unchanged at 4.3% from the previous quarter, down from 5.0% a year earlier and joint lowest since 1975.

The movement in rates at which local authorities can borrow from the Public Works Loan Board (PWLB) is set out in the table below.

Period	1 April 2017	30 September 2017
1 year	0.9%	0.8%
3 year	1.0%	1.0%
5 year	1.3%	1.2%
10 year	1.9%	1.9%
25 year	2.6%	2.5%
50 year	2.4%	2.3%

* These borrowing rates are at the 'Certainty Rate' (0.20% below the PWLB standard rate).

The outlook for the six-month period ending 31 March 2018 continues to remain muted as uncertainty over the UK's future trade relations with the EU and the rest of the world will weigh on economic activity and business investment, dampen investment intentions and tighten credit availability, prompting lower activity levels and potentially a rise in unemployment.

The Bank of England's MPC made no change to monetary policy at its meetings in the first half of the financial year and at its meeting in September 2017 voted 7-2 in favour of keeping the Base Rate unchanged at 0.25%. However, the MPC recently changed their rhetoric, implying a rise in Base Rate in "the coming months". The Council's treasury adviser, Arlingclose Ltd, is not convinced that the UK's economic outlook justifies such a move at this stage, but the Bank's interpretation of the data seems to have shifted.

Regulatory Updates

MiFID II:

Local authorities are currently treated by regulated financial services firms as professional clients who can “opt down” to be treated as retail clients instead. But from 3 January 2018, as a result of the second Markets in Financial Instruments Directive (MiFID II), local authorities will be treated as retail clients who can “opt up” to be professional clients, providing that they meet certain criteria. Regulated financial services firms include banks, brokers, advisers, fund managers and custodians, but only where they are selling, arranging, advising or managing designated investments. In order to opt up to professional, the authority must have an investment balance of at least £10 million and the person authorised to make investment decisions on behalf of the authority must have at least one year’s relevant professional experience. In addition, the firm must assess that that person has the expertise, experience and knowledge to make investment decisions and understand the risks involved.

The main additional protection for retail clients is a duty on the firm to ensure that the investment is “suitable” for the client. However, local authorities are not protected by the Financial Services Compensation Scheme nor are they eligible to complain to the Financial Ombudsman Service whether they are retail or professional clients. It is also likely that retail clients will face an increased cost and potentially restricted access to certain products including money market funds, pooled funds, treasury bills, bonds, shares and to financial advice. The Authority has declined to opt down to retail client status in the past as the costs were thought to outweigh the benefits.

The Council meets the conditions to opt up to professional status and intends to do so in order to maintain its current MiFID status.

CIPFA Consultation on Prudential and Treasury Management Codes:

In February 2017 CIPFA canvassed views on the relevance, adoption and practical application of the Treasury Management and Prudential Codes.

The proposed changes to the Prudential Code include the production of a new high-level Capital Strategy report to full Council which will cover the basics of the capital programme and treasury management. The prudential indicators for capital expenditure and the authorised borrowing limit would be included in this report but other indicators may be delegated to another committee. There are plans to drop certain prudential indicators, however local indicators are recommended for ring fenced funds (including the HRA) and for group accounts. Other proposed changes include applying the principles of the Code to subsidiaries.

Proposed changes to the Treasury Management Code include the potential for non-treasury investments such as commercial investments in properties in the definition of “investments” as well as loans made or shares brought for service purposes. Another proposed change is the inclusion of financial guarantees as instruments requiring risk management and addressed within the Treasury Management Strategy. Approval of the technical detail of the Treasury Management Strategy may be delegated to a committee rather than needing approval of full Council. There are also plans to drop or alter some of the current treasury management indicators.

CIPFA intends to publish the two revised Codes towards the end of 2017 for implementation in 2018/19, although CIPFA plans to put transitional arrangements in place for reports that are required to be approved before the start of the 2018/19 financial year. The Department of Communities and Local Government (DCLG) and CIPFA wish to have a more rigorous framework in place for the treatment of commercial investments as soon as is practical. It is understood that DCLG will also be revising its Investment Guidance (and its MRP guidance) for local authorities.

Appendix B

Debt Management Activities from 1 April 2017 to 30 September 2017

	Balance on 01/04/2017 £M	Debt Maturing £M	New Borrowing £M	Balance on 30/09/2017 £M
Capital Financing Requirement (CFR)	**524.4**			
Short Term Borrowing[1]	72.2	228.2	213.0	57.0
Long Term Borrowing	275.6	0.0	0.0	275.6
TOTAL BORROWING	**347.8**	**228.2**	**213.0**	**332.6**
Other Long Term Liabilities	17.2	0.0	0.0	17.2
TOTAL EXTERNAL DEBT	**365.0**	**228.2**	**213.0**	**349.8**

At 30 September 2017, the Council had in place £349.8M of external borrowing to finance its previous years' capital programmes. With short term interest rates being much lower than long term rates, it continues to be more cost effective in the short term to use a combination of internal resources and short term borrowing, rather than undertake further long term borrowing. By doing so, the Council is able to minimise net borrowing costs and reduce overall treasury risk.

No debt rescheduling has been undertaken during the financial year as present discount rates make the costs involved unattractive.

[1] Loans with maturities less than 1 year.

Budgeted Expenditure and Outturn

The interest payable in the year is forecast to be £0.2M less than the budget of £5.5M. This budget underspend is due to a combination of:

- new borrowing being taken from local authorities and other public sector bodies such as Police and Crime Commissioners on a short-term temporary basis at lower than budgeted rates; and
- Capital Programme slippage which has been higher than originally assumed in the interest payable budget, leading to a lower level of overall borrowing being required than assumed in the 2017/18 budget.

Appendix C

<u>Investment Activities from 1 April 2017 to 30 September 2017</u>

The Council gives priority to security and liquidity and aims to achieve a yield commensurate with these principles.

	Balance on 01/04/2017 £M	**Investments Made / Capital Appreciation £M**	**Investments Repaid / Capital Depreciation £M**	**Balance on 30/09/2017 £M**
Short Term Investments	3.2	48.8	45.3	6.7
Money Market Funds	6.0	182.5	176.1	12.4
Investments in Pooled Funds (Lime Fund)	5.3	0.1	0.0	5.4
TOTAL INVESTMENTS	**14.5**	**231.4**	**221.4**	**24.5**

Security of capital has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2017/18. New investments were made with the following classes of institutions:

- BBB+ rated banks and building societies;
- AAA rated Money Market Funds.

Counterparty credit quality was assessed and monitored with reference to credit ratings (the Council's minimum long-term counterparty rating of BBB+ or equivalent across rating agencies Fitch, Standard & Poors and Moody's), share prices, credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

The average cash balance the Council held was £22.9M over the 6-month period to 30 September 2017, compared to £19.6M for the comparable period in the previous year. Currently, the Council has money market funds and bank deposits placed on varying interest rates ranging between 0.1% and 0.6%.

The Council continues to adhere to its long-standing strategy of holding low cash balances to reduce investment counterparty risk and contain its borrowing costs by utilising cash balances in lieu of borrowing externally.

The Council may invest its surplus funds with any of the counterparties in the table below:

Approved Investment Counterparties

Counterparty	
Banks and other organisations and securities whose lowest published long-term credit rating from Fitch, Moody's and Standard & Poor's is:	AAA
	AA+
	AA
	AA-
	A+
	A
	A-
	BBB+
UK Central Government (irrespective of credit rating)	
UK Local Authorities, Police Authorities, Police & Crime Commissioners and Fire Authorities (irrespective of credit rating)	
Money Market Funds and other pooled funds	

In addition, the Council may invest with organisations and pooled funds without credit ratings, following an external credit assessment and advice from its treasury management advisers, Arlingclose Ltd.

Counterparty Investment Limits

The cash limit for any single organisation or any group of organisations under the same ownership is outlined in the following table.

	Cash limit
Any single organisation, except the UK Central Government	£7M each
UK Central Government	unlimited
UK Local Authorities	unlimited
Any group of organisations under the same ownership	£7M per group
Any group of pooled funds under the same management	£10M per manager
Negotiable instruments held in a broker's nominee account	£10M per broker
Foreign countries	£10M per country
Registered Providers	£10M in total
Unsecured investments with Building Societies	£10M in total
Loans to small businesses	£10M in total
Money Market Funds	70% in total

Budgeted Income and Outturn

The investment interest receivable in the year is forecast to be in line with the budget at £0.3M.

Appendix D

<u>Compliance with Prudential Indicators</u>

The Council has complied with its prudential indicators during the period 1 April – 30 September 2017. The indicators were set in February 2017 as part of the Council's Treasury Management Strategy Statement.

Borrowing in Comparison to the Capital Financing Requirement

Estimates of the Council's cumulative maximum external borrowing requirement for 2017/18 to 2019/20 are shown in the table below.

	31/03/2017 Actual £M	**31/03/2018 Estimate £M**	**31/03/2019 Estimate £M**	**31/03/2020 Estimate £M**
Gross CFR	524.4	541.3	564.0	573.7
Less: PFI liabilities	(17.2)	(16.5)	(15.7)	(15.3)
Borrowing CFR	**507.2**	**524.8**	**548.3**	**558.4**
Less: Existing profile of long term borrowing	(275.6)	(275.6)	(275.6)	(275.6)
Gross Borrowing Requirement/Internal Borrowing	**231.6**	**249.2**	**272.7**	**282.8**

These forecast borrowing figures are based on the full Capital Programme being achieved.

(a) Estimates of Capital Expenditure

This indicator is set to ensure that the level of capital expenditure remains within sustainable limits. The Council's planned capital expenditure and financing, as approved by Council in February 2017, can be summarised as follows.

Capital Expenditure and Financing	**2016/17 Actual £M**	**2017/18 Estimate £M**	**2018/19 Estimate £M**	**2019/20 Estimate £M**
General Fund	103.0	94.9	91.0	96.8
HRA	10.2	14.6	22.3	21.9
Total Expenditure	**113.2**	**109.5**	**113.3**	**118.7**
Capital receipts	(6.9)	(12.0)	(10.0)	(10.0)
Grants and contributions	(42.4)	(43.0)	(46.4)	(63.5)
Revenue contributions	(3.5)	-	-	-
Minimum Revenue Provision (MRP) / PFI	(1.6)	(9.5)	(10.3)	(10.7)
Borrowing	(48.6)	(30.4)	(24.3)	(12.6)
General Fund sub-total	**(103.0)**	**(94.9)**	**(91.0)**	**(96.8)**
Capital receipts	(3.4)	(4.0)	(4.7)	(10.2)
Reserves	(4.6)	(6.2)	(14.5)	(11.4)
Revenue contributions	(2.2)	(2.3)	(2.1)	-
Grants and contributions	-	(2.1)	(1.0)	(0.3)
HRA sub-total	**(10.2)**	**(14.6)**	**(22.3)**	**(21.9)**
Total Financing	**(113.2)**	**(109.5)**	**(113.3)**	**(118.7)**

(b) Estimates of Capital Financing Requirement

The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose.

Capital Financing Requirement	**31/03/2017 Actual £M**	**31/03/2018 Estimate £M**	**31/03/2019 Estimate £M**	**31/03/2020 Estimate £M**
General Fund	359.4	377.8	402.0	414.6
HRA	165.0	163.5	162.0	159.1
Total CFR	**524.4**	**541.3**	**564.0**	**573.7**

The CFR is forecast to rise by £49.3M over the next three years as capital expenditure financed by debt outweighs resources put aside for debt repayment.

(c) Gross Debt and the Capital Financing Requirement

This is a key indicator of prudence. In order to ensure that over the medium term debt will only be for a capital purpose, the Council should ensure that debt does not, except in the short term, exceed the total of Capital Financing Requirement (CFR) in the preceding year plus the estimates of any additional CFR for the current and next two financial years.

The Council has had no difficulty meeting this requirement nor are any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

	31/03/2017 Actual £M	31/03/2018 Estimate £M	31/03/2019 Estimate £M	31/03/2020 Estimate £M
CFR	**524.4**	**541.3**	**564.0**	**573.7**
Borrowing	347.8	407.1	432.9	454.0
PFI liabilities	17.2	16.5	15.7	15.3
Gross Debt	**365.0**	**423.6**	**448.6**	**469.3**
Usable reserves	102.7	92.7	90.4	79.4
Working capital	56.7	25.0	25.0	25.0
Borrowed in excess of CFR? (Yes/No)	**No**	**No**	**No**	**No**

(d) Authorised Limit and Operational Boundary for External Debt

The Local Government Act 2003 requires the Council to set an affordable borrowing limit, irrespective of their indebted status, referred to as the Authorised Limit. It is the maximum amount of debt that the Council can legally owe. This is a statutory limit which should not be breached.

The Operational Boundary is based on the same estimates as the Authorised Limit but reflects the most likely, prudent but not worst case scenario without the additional headroom included within the Authorised Limit for unusual cash movements.

The Council confirms that there were no breaches in either the Authorised Limit or the Operational Boundary during the first six months of 2017/18, where the maximum extent of external borrowing was £363.8M (as at 24 April 2016).

	Authorised Limit for 2017/18 £M	**Operational Boundary for 2017/18 £M**	**Actual External Debt as at 30/09/2017 £M**
Borrowing	559.2	549.2	332.6
Other long-term liabilities	18.2	17.7	17.2
Total	**577.4**	**566.9**	**349.8**

(e) Ratio of Financing Costs to Net Revenue Stream:

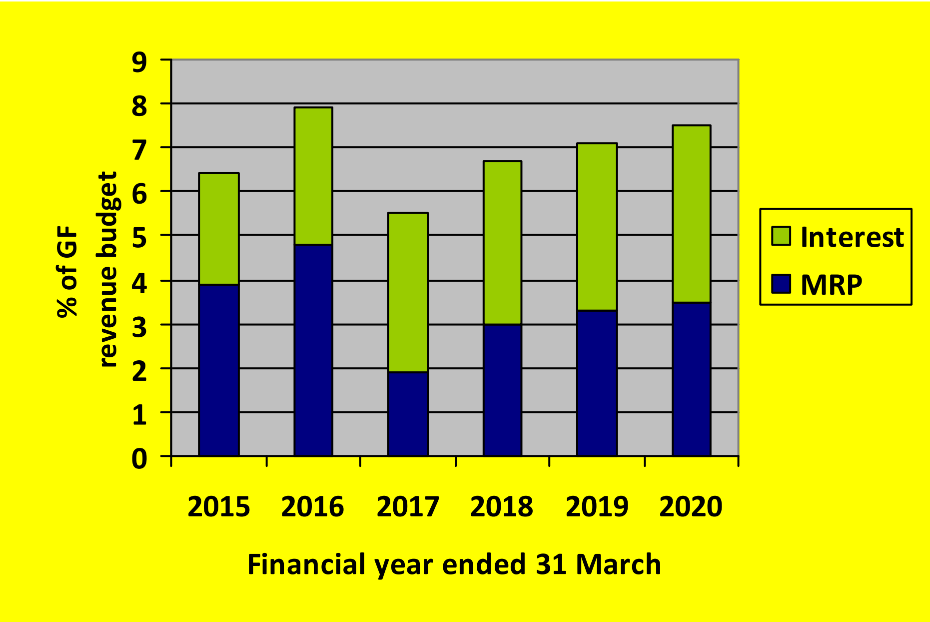
This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

Ratio of Financing Costs to Net Revenue Stream	**2016/17 Actual %**	**2017/18 Estimate %**	**2018/19 Estimate %**	**2019/120 Estimate %**
General Fund	5.3	6.6	7.0	7.4
HRA	13.2	13.7	13.7	13.7

It measures the proportion of the revenue budget that is required to meet the ongoing financing costs of past capital expenditure which was funded from borrowing. Future year estimates incorporate the additional financing costs of planned capital expenditure to be funded from borrowing. It is important that the total capital investment of the Council remains within sustainable limits. However, the level of capital investment that can be supported will be a matter for local decision.

Central Bedfordshire's ratio is expected to increase given the Council's significant commitment to capital investment over the next few years.

The impact of the recent change in methodology for calculating the Council's Minimum Revenue Provision (MRP) is shown by the reduction in 2016/17 relative to previous years. However, the growing impact of borrowing to fund new capital expenditure is illustrated from 2016/17 onwards, with MRP and interest costs taking up an increasingly greater proportion of the Council's net revenue budget over time:



The figures in the above chart are based on the current Medium Term Financial Plan. The Council will need to carefully consider this increasing cost when determining its future plans for capital expenditure.

(f) Incremental Impact of Capital Investment Decisions:

This is an indicator of affordability that shows the incremental impact of new capital investment decisions included in the current approved capital programme on Council Tax and housing rent levels.

Incremental Impact of Capital Investment Decisions	2017/18 Estimate £	2018/19 Estimate £	2019/20 Estimate £
General Fund – increase in annual band D Council Tax	11.87	20.03	25.67
HRA – increase in average weekly rents	0.12	0.32	0.52

(g) Adoption of the CIPFA Treasury Management Code

This indicator demonstrates that the Council has adopted the principles of best practice.

Adoption of the CIPFA Treasury Management Code
The Council adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2011 Edition* at its Full Council meeting on 29 November 2012.

(h) Housing Revenue Account (HRA) Debt

The purpose of this limit is to report the level of debt imposed on the Council at the time of the implementation of self-financing by the Department for Communities and Local Government (CLG).

	31/03/2017 Actual £M	31/03/2018 Estimate £M	31/03/2019 Estimate £M	31/03/2020 Estimate £M
HRA Debt Cap (as prescribed by the DCLG)	165.0	165.0	165.0	165.0
HRA CFR	165.0	163.5	162.0	159.1
Difference	**0.0**	**1.5**	**3.0**	**5.9**

(i) Interest Rate Exposures

This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the proportion of net principal borrowed, are outlined in the table below.

The Council confirms that there were no breaches to either of the upper limits during the first six months of 2017/18, where the upper limit of variable rate exposure was 37% (as at 24 April 2017).

	2017/18 %	2018/19 %	2019/20 %
Upper limit on fixed rate exposure	100	100	100
Actual exposure as at 30/09/2017	**68**		
Upper limit for variable rate exposure	50	50	50
Actual exposure as at 30/09/2017	**32**		

(j) Maturity Structure of Fixed Rate Borrowing

This indicator is to limit large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates.

Maturity Structure of Fixed Rate Borrowing	Upper Limit %	Lower Limit %	Actual Fixed Rate Borrowing as at 30/9/2017 %	Compliance with Set Limits?
Under 12 months	20	0	5	Yes
12 months - 24 months	20	0	0	Yes
24 months - 5 years	60	0	0	Yes
5 years - 10 years	100	0	36	Yes
10 years - 20 years	100	0	36	Yes
20 years - 30 years	100	0	0	Yes
30 years - 40 years	100	0	23	Yes
40 years - 50 years	100	0	0	Yes
50 years and above	100	0	0	Yes

(The 2011 revision to the CIPFA Treasury Management Code requires the Prudential Indicator relating to Maturity of Fixed Rate Borrowing to reference the maturity of LOBO loans to the earliest date on which the lender can require payment, i.e., the next call date).

(k) Principal sums invested for periods longer than 364 days

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total principal sum invested to final maturities beyond the period end are outlined in the table below.

The Council confirms that there was no breach in the £10M limit during the first six months of 2017/18, given that no investments for a period of longer than 364 days were entered into.

	2017/18 £M	**2018/19 £M**	**2019/20 £M**
Upper limit for total principal sums invested over 364 days	10	10	10
Actual as at 30 September 2017	0		

*

* The Council holds an investment in Aviva Investors' Lime Property Fund Unit Trust (valued at £5.4m as at 30 September 2017). This investment has delivered a reasonably stable income return of around 5% p.a. over recent years and the Council intends to retain this investment for the long term. However, it does not feature in the above Actual column on the basis that it does not have a specified maturity date and could be liquidated within an estimated 3-month timescale if necessary.