REPORT TO	ON
Governance Committee	**13 September 2017**

Jan 2017

TITLE	AUTHOR	*Agenda item No.*
Treasury Management Activity Mid-year Review 2017/18	**M L Jackson**	

1. PURPOSE OF THE REPORT

To report on Treasury Management performance, and compliance with prudential Indicators, in financial year 2017/18 to the end of July.

2. RECOMMENDATIONS

2.1 Governance Committee is asked to note the report

3. EXECUTIVE SUMMARY

3.1 Prudential Indicators for 2017/18 will be revised when the Treasury Strategy for 2018/19 to 2020/21 is presented to Council in February 2018.

3.2 The average daily investment total for the period to 31 July 2017 was £31.841m at an average rate of 0.53%. This exceeded the target of 0.13%, and the earnings rate of 0.25% for 2017/18 suggested by Capita. The interest receivable budget for the year should be exceeded, the forecast being £116,000 compared to the budget of £69,000.

3.3 Appendix B presents an update on economic matters; and Appendix C is a commentary on interest rate forecasts.

3.5 The Markets in Financial Instruments Directive (MiFID) II is being implemented from January 2018. The Council will need to opt-up to being a Professional Client to continue using Money Market Funds, as explained in Appendix D.

3.4 CIPFA are consulting on changes to the Treasury Management Code and Prudential Code. The issues are presented in Appendix E.

3.5 IFRS 9 Financial Instruments will be adopted in the Code of Practice on Local Authority Accounting in the UK 2018/19. On adoption, certain investment types could involve annual gains or losses which would have an impact on the Council's resources.

4. CORPORATE PRIORITIES

The report relates to the following corporate priorities

Clean, green and safe		Strong and healthy communities	
Strong South Ribble in the heart of prosperous Lancashire		Efficient, effective and exceptional council	✓

5. BACKGROUND TO THE REPORT

The Code of Practice for Treasury Management specifies that Councils should review their Treasury Strategy and activity half yearly. This report meets that requirement.

6. PRUDENTIAL INDICATORS

Capital Expenditure and Capital Financing Requirement (CFR) 2017/18

6.1 The Prudential Indicators approved by Council on 1 March 2017 took account of estimated capital expenditure and sources of financing from 2016/17 to 2019/20. These will be reviewed during the year, to take account of any significant changes to the capital programme and its financing as reported in budget monitoring. Revised Prudential Indicators will be presented to the budget setting Council meeting of 28 February 2018.

6.2 The Prudential Indicators approved for 2017/18 onwards were as follows:

Prudential Indicator 1 - Capital Expenditure

Table 1 – Capital Expenditure	**2017/18 Estimate £000**	**2018/19 Estimate £000**	**2019/20 Estimate £000**
Capital expenditure incurred directly by the Council	4,404	4,762	2,379
Less Capital resources			
Capital receipts	(500)	(707)	(220)
Grants & contributions	(1,268)	(2,486)	(544)
Revenue and reserves	(1,666)	(1,271)	(410)
Unfinanced amount (affects the CFR see Prudential Indicator 2 below)	970	298	1,205
Capital expenditure under Leisure Contract – treated as a finance lease (affects the CFR see Prudential Indicator 2 below)	124	104	0
Increase in Capital Financing Requirement	**1,094**	**402**	**1,205**

Prudential Indicator 2 - Capital Financing Requirement (CFR)

Table 2 – Capital Financing Requirement (CFR)	**2017/18 Estimate £000**	**2018/19 Estimate £000**	**2019/20 Estimate £000**
Estimated CFR 1 April	**5,146**	**5,222**	**4,555**
Reasons for the annual change in the CFR			
Additional finance lease liability	124	104	0
Unfinanced capital expenditure (as above)	970	298	1,205
Increase in Capital Financing Requirement	1,094	402	1,205
Repayment of finance lease	(246)	(246)	(246)
Annual revenue charge (MRP)	(772)	(823)	(824)
Reduction in Capital Financing Requirement	(1,018)	(1,069)	(1,070)
Estimated CFR 31 March	**5,222**	**4,555**	**4,690**

6.3 The Capital Financing Requirement (CFR) measures a vital component of an authority's capital strategy: the cumulative amount of capital spending that has not yet been financed by capital receipts, capital grants and contributions, or contributions from revenue income. It measures the underlying need to borrow for a capital purpose, although this borrowing may not necessarily take place externally. An authority may judge it prudent to make use its own cash as part of an efficient and effective treasury management strategy. This practice,

which is often known as ‘internal borrowing’, is common in local authorities, and means that there is no immediate link between the need to borrow to pay for capital spending and the level of external borrowing.

6.4 The CFR increases when there is unfinanced capital expenditure and expenditure under the Leisure Contract treated as a finance lease. It reduces as a result of the annual Minimum Revenue Provision, which is a statutory charge, and the repayment of the finance lease, also referred to as voluntary MRP.

6.5 In the Balance Sheet, the CFR is broadly calculated by deducting the balance on the Revaluation Reserve and Capital Adjustment Account from the value of Long Term Assets treated as capital expenditure. However, there may be other adjustments to arrive at the CFR figure to be used for calculation of MRP.

6.6 Internal borrowing is calculated by deducting external borrowing and the finance lease liability from CFR. As there is no external borrowing at present, all of the borrowing (apart from the finance lease) is internal.

6.7 The estimated CFR of £5.222m as at 31 March 2018 represents the balance of capital spending not yet financed which has accumulated over several years. The CFR was higher in earlier years. In 2012/13 for instance, the CFR was £6.284m. This reduced to £5.691m in 2013/14, and £5.171m in 2014/15. This was because in those years the MRP and finance lease repayments exceeded the additional unfinanced capital expenditure. Currently the CFR is expected to reduce in 2018/19, but to increase by £0.135m in 2019/20. This will be reviewed to reflect changes to the capital programme and its financing, and any changes to debt repayment for instance by increasing voluntary MRP.

The CFR and Borrowing 2017/18

6.8 The Prudential Code requires that borrowing net of investments should not exceed the CFR for the preceding year plus any anticipated increase in the current and next two years. This is in order to ensure that councils borrow only for capital investment purposes. Net borrowing will not exceed the CFR in 2017/18, and the actual year-end figure will be confirmed in the Treasury Management Annual Report for the financial year in June 2018.

Operational Boundary for External Debt 2017/18

6.9 The Operational Boundary for external debt should reflect the most likely, but not worst-case, scenario consistent with the Council’s approved budgets. Gross borrowing and other long-term liabilities should not exceed the Operational Boundary. The figure approved for 2017/18 was £0.543m, being the forecast balance of other long-term liabilities as at 31 March 2018.

Table 3 – Operational Boundary	**2017/18 Estimate £000**	**2018/19 Estimate £000**	**2019/20 Estimate £000**
Borrowings	0	0	0
Other long-term liabilities	543	331	15
Operational boundary	**543**	**331**	**15**

Authorised Limit 2017/18

6.10 The Authorised Limit should allow headroom above the Operational Boundary to accommodate the fluctuations that can occur in cashflows. The figure approved for 2017/18 was £3.543m, and there is no reason to amend this at present.

Table 4 - Authorised Limit	2017/18 Estimate £000	2018/19 Estimate £000	2019/20 Estimate £000
Borrowings	3,000	3,000	3,000
Other long-term liabilities	543	331	15
Authorised limit	**3,543**	**3,331**	**3,015**

Ratio of Financing Costs to the Revenue Stream 2017/18

6.11 The Ratio of Financing Costs to the Revenue Stream shows the percentage of the Council's income from Government grants and council tax that has been used to meet interest costs and debt repayment. The actual figure for 2017/18 will be presented in the Treasury Management Annual Report 2017/18 in June 2018.

Incremental Impact of Capital Investment Decisions 2017/18

6.12 The Incremental Impact of Capital Investment Decisions measures the cumulative impact of capital expenditure on the revenue budget. It is not possible to make a meaningful comparison against this indicator other than when it is restated in the annual Treasury Strategy, which will be presented to Council in February 2018.

7. TREASURY ACTIVITY

7.1 Investment activity in year to 31 July summarised in the following table:

Table 5 - Investment Activity	Average Daily Investment £000	Earnings to 31 July 2017 £	Average Rate %
Debt Management Office	0	0	0.00
Other fixed term deposits	23,090	43,374	0.56
Notice Accounts	4,000	9,693	0.72
Call accounts	782	257	0.10
Money Market Funds	3,969	2,660	0.20
Total	**31,841**	**55,984**	**0.53**

7.2 A full list of investments currently held is shown at Appendix A. The total invested as at 4 August 2017 was £38.502m, including term deposits, notice accounts, call accounts, and money market funds. This compares to the average daily investment for the period to 31 August 2016 which was £31.392m, and the total invested at 31 August 2016 was £33.999m.

7.3 The list of investment counterparties and associated investment limits approved for 2017/18 are also presented in the same appendix.

7.4 The interest earning benchmark is the average LIBID 7-day rate plus 15%. This was 0.13% for the period reported, compared to the rate achieved of 0.53%. In addition, the rate achieved exceeded Capita's suggested earnings rate of 0.25% for 2017/18, which was based on term deposits of only three months. This Council's term deposits have been

mainly for six or twelve months, as shown in Appendix A, and these attract higher interest rates.

7.5 At this stage in 2016/17, the average rate achieved was 0.69%. All counterparties are offering lower rates of interest than they were a year ago.

7.6 The following table compares the budgets for interest receivable against the latest projection. A low average rate was assumed when the Treasury Strategy was prepared, and the average rate achieved to date has exceeded it. This means that an increase in the forecast as shown in Table 6 is possible. At present it is assumed that when current investments mature they will be reinvested at a lower rate that achieved in the period to 31 July.

Table 6 - Interest Receivable Budget	Budget for 2017/18 £000	Actual to 31 July 2017 £000	Forecast for year £000
Interest earned	69	56	116
Heritable repayment	0	0	0
Total	**69**	**56**	**116**

Investment Options

7.7 Banks and building societies currently approved for use as investment counterparties, together with Capita's recommended investment durations, are as follows:

Suggested Investment Durations as at 30 August 2017			
Country	**Counterparty**	**Suggested Duration**	**Limit per institution**
United Kingdom	Royal Bank of Scotland Plc	12 mths	£5m per group
	National Westminster Bank Plc	12 mths	
	Bank of Scotland Plc	6 mths	£5m per group
	Lloyds Bank Plc	6 mths	
	Barclays Bank Plc	6 mths	£5m
	Coventry Building Society	6 mths	£5m
	Goldman Sachs International Bank	6 mths	£5m
	HSBC Plc	12 mths	£5m
	Leeds Building Society	100 days	£5m
	Nationwide Building Society	6 mths	£5m
	Santander UK Plc	6 mths	£5m
	Skipton Building Society	100 days	£5m
	Yorkshire Building Society	100 days	£5m
Germany	Landesbank Hessen-Thuringen Girozentrale (Helaba)	12 mths	£4m

7.8 In practice, several of these institutions cannot be used by this council. Some of the banks do not require investments from local authorities; some only accept minimum deposits greater than our strategy allows; and some accept deposits for minimum periods greater than we can invest for, such as two or three years. Finally interest rates offered by some banks are so low that there is little or no advantage in using them instead of the DMO. The banks and building societies that have accepted investments from the council are as listed in Appendix A.

Icelandic Investment Claim

7.9 So far in 2017/18 there have been no repayments in respect of the Heritable investment claim. The balance of the claim remaining to be recovered is still £40,000. In total, £1.974m of the original £2m investment has been recovered. Recovery to date is around 98% of the claim value, which has exceeded expectations.

7.10 On 30 August 2017, the Heritable administrators Ernst & Young LLP notified all creditors of the bank that they propose to apply for a further extension to the Administration of one year. No further repayment is due in the near future.

8. TREASURY CONSULTANTS' ADVICE

8.1 Appendix B presents the advice of Capita Asset Services and their economic research consultants Capital Economics in respect of economic matters in the first quarter of 2017/18. In addition, a detailed commentary on interest rate forecasts is presented as Appendix C. Bank rate and PWLB borrowing rate forecasts are given from September quarter 2017 through to March quarter 2020.

8.2 An increase in Bank Rate from 0.25% to 0.50% is still expected in the June quarter of 2019. So far the Bank Rate forecast remains unchanged from that included in the Treasury Strategy for 2017/18.

8.3 Capita's suggested budgeted investment earning rates for investments up to about three months duration in each financial year for the next seven years are as follows:

Table 7 - Average Earnings in each financial year		
	Revised August 2017	**Original March 2017**
2017/18	0.25%	0.25%
2018/19	0.25%	0.25%
2019/20	0.50%	0.50%
2020/21	0.75%	0.75%
2021/22	1.00%	1.00%
2022/23	1.50%	1.50%
2023/24	1.75%	1.75%
Later years	2.75%	2.75%

8.4 The most recent estimate is compared to the estimated earnings rate available at the time the Treasury Management Strategy was presented for approval in March 2017. The suggested earnings rates are unchanged so far this financial year.

8.5 Compared to the previous interest rates forecast, PWLB borrowing rates are currently a little lower than expected. Gradually increases through to March quarter of 2020 are still forecast.

9. MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE (MiFID) II

9.1 Appendix D presents an update on the implementation of MiFID II in the United Kingdom. In brief, to continue using regulated products such as money market funds this Council would have to opt-up to Professional Client status. At present it is expected that qualification as a Professional Client will be achieved so that use of Money Market Funds will continue. However, the process has not yet commenced so progress will be reported at the earliest opportunity.

10. CIPFA CONSULTATIONS ON THE TREASURY MANAGEMENT CODE AND PRUDENTIAL CODE

10.1 A summary of the proposed changes to CIPFA's Treasury Management Code and Prudential Code is presented as Appendix E. Several of the proposed changes are inevitably of a technical nature, and those incorporated into the Codes will be explained when implemented.

10.2 It is clear that some of the changes are intended to address concerns expressed in the media in recent months about the extent to which local authorities have been incurring capital expenditure on income-generating properties to meet budget shortfalls following cuts in government funding. The changes to the Prudential Code should not affect this Council's existing capital expenditure plans, though there would be a specific requirement to report on risks associated with the capital strategy.

11. CIPFA CONSULTATION ON ADOPTION OF IFRS 9 FINANCIAL INSTRUMENTS IN CODE OF PRACTICE ON LOCAL AUTHORITY ACCOUNTING IN THE UNITED KINGDOM 2018/19

11.1 The CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 will adopt the IFRS 9 accounting rules for Financial Instruments. The changes could have an impact on councils which invest in companies, or place deposits in enhanced money market funds.

11.2 Any investments which would be accounted for as "available for sale" at present would move into the "fair value through profit or loss" category. This would mean that gains or losses from changes in the fair value of financial assets would be reflected in the surpluses or deficits in the Provision of Services in local authorities' accounts, rather than being held in a reserve until realised on sale of the assets. It is not clear whether the DCLG will introduce a statutory override to reverse the impact of the gains or losses.

11.3 At present the proposed change would not affect this Council, though it may be desirable to delete enhanced MMFs from the investment counterparties list in the Treasury Strategy for 2018/19 onwards.

12. WIDER IMPLICATIONS AND BACKGROUND DOCUMENTATION

12.1 Comments of the Statutory Finance Officer

The report meets the requirement of the Treasury Management Code of Practice that the Treasury Strategy and activity should be reviewed half-yearly.

12.2 Comments of the Monitoring Officer
The purpose of the Report is to comply with various guidance including the Code of Practice for Treasury Management.

Other implications: • **Risk** • **Equality** • **HR**	The Council's treasury management strategy and policies are designed to ensure the effective control and management of the risks associated with such activities.

8. BACKGROUND DOCUMENTS (or there are no background papers to this report)

Treasury Management in the Public Services: Code of Practice (2011)
CIPFA Prudential Code for Capital Finance in Local Authorities (2011)
DCLG Guidance on Local Government Investments (2010)

Appendix A

Investments as at 4 August 2017

Counterparty	Type	Amount £000	Rate %	Date of investment	Date of Maturity
Salford City Council	Term	2,000	0.45	09/03/2017	09/08/2017
Goldman Sachs International Bank	Term	2,000	0.75	14/03/2017	14/09/2017
Plymouth City Council	Term	2,000	0.32	16/06/2017	18/09/2017
Salford City Council	Term	2,000	0.45	29/03/2017	29/09/2017
Goldman Sachs International Bank	Term	1,000	0.76	30/03/2017	29/09/2017
Goldman Sachs International Bank	Term	1,000	0.77	03/04/2017	29/09/2017
Bank of Scotland	Term	1,000	0.55	04/03/2017	06/11/2017
Goldman Sachs International Bank	Term	1,000	0.66	04/05/2017	06/11/2017
Bank of Scotland	Term	2,000	0.55	08/05/2017	08/11/2017
Thurock Borough Council	Term	1,000	0.35	22/05/2017	22/11/2017
Helaba	Term	2,000	0.55	14/12/2016	14/12/2017
Bank of Scotland	Term	1,000	0.55	14/06/2017	14/12/2017
Bank of Scotland	Term	1,000	0.36	13/07/2017	15/01/2018
Lancashire County Council	Term	1,000	0.53	16/05/2017	16/05/2018
Lancashire County Council	Term	3,000	0.53	06/06/2017	05/06/2018
Lancashire County Council	Term	1,000	0.55	28/06/2017	27/06/2018
Fixed Term Deposits sub total		**24,000**		**Listed in order of maturity**	
Santander UK - 180 Day	Notice	4,000	0.55		
Notice Accounts sub total		**4,000**			
Barclays (deposit account)	Call	3,001	0.20 (1)		
Barclays (current account)	Call	1			
Call Accounts sub total		**3,002**			
Federated MMF	MMF	1,500	0.17 (2)		
Standard Life MMF	MMF	3,000	0.18 (2)		
BlackRock MMF	MMF	3,000	0.20 (2)		
Money Market Funds sub total		**7,500**			
Total		**38,502**			

Notes:

(1) Includes 0.20% annual bonus.

(2) MMF rates are variable. This is the calculated average for the year to July

Summary of Term Deposits by Counterparty	Type	Amount £000	Limit £000
Bank of Scotland	Term	5,000	5,000
Goldman Sachs International Bank	Term	5,000	5,000
Helaba	Term	2,000	4,000
Lancashire County Council	Term	5,000	5,000
Plymouth City Council	Term	2,000	5,000
Salford City Council	Term	4,000	5,000
Thurock Borough Council	Term	1,000	5,000
Fixed Term Deposits sub total		24,000	

Investment Counterparties 2017/18

Category	Institutions	CAS Colour Code	Maximum Period	Limit per Institution
Banks & Building Societies: Call Accounts /Term Deposits / Certificates of Deposit (CDs)				
Government related/guaranteed	DMADF (DMO) UK Local Authority	Yellow Yellow	6 months 2 years	Unlimited £5m per LA
UK part-nationalised institutions	Royal Bank of Scotland group	Blue	1 year	£5m per group
UK-incorporated Institutions	UK banks and building societies of high credit quality	Orange Red Green	1 year 6 months 3 months	£5m per group (or independent institution)
Non-UK Banks	Non-UK banks of high credit quality	Orange Red Green	1 year 6 months 3 months	£4m per group (or independent institution); £8m in total for this category
Money Market Funds				
Money Market Funds (CNAV) **	MMFs of high credit quality - AAA rated		Instant access	£5m per fund
Enhanced Money Market Funds (VNAV)	EMMFs of high credit quality - AAA rated		T+2 or T+3	£3m per fund; £6m in total for this category

Appendix B

Economic Background

The UK GDP annual growth rates in each calendar year 2013 – 2016 of 1.9%, 3.1%, 2.2% and 1.8%, have all been the top rate, or near top rate, of any of the G7 countries in every year. It is particularly notable that the UK performance was repeated in 2016, a year in which the Bank of England had forecast in August 2016 that growth would be near to zero in the second half of the year due to the economic shock it expected from the result of the Brexit referendum in June. However, it has had to change its mind and in its February and May 2017 Inflation Reports, the Bank upgraded its forecasts for growth (May Report - 2017 1.9%, 2018 and 2019 1.9%). However over these years, it also expects inflation to accelerate towards nearly 3% as increases in costs as a result of the fall in the value of sterling since the referendum, gradually feeds through into the economy, though it should fall back to 2.2% in 2019. Provided those cost pressures do not feed through into significantly higher domestically generated inflation within the UK, the MPC is expected to 'look though' this one off blip upwards in inflation. Wage inflation, which is a key driver of domestically generated price pressures, is currently subdued. There is, though, a potential risk that the MPC might muster a majority to reverse the emergency 0.25% rate cut before embarking on a progressive trend of increases in Bank Rate at a later time.

GDP growth in the US has been highly volatile in 2016 but overall mediocre, at an average of 1.6% for the year. Quarter 1 in 2017 has also been mediocre at 1.4% but current indications are that growth could rebound strongly in quarter 2. The disappointment so far has been the lack of decisive action from President Trump to make progress with his promised fiscal stimulus package. The Fed has, therefore, started on the upswing in rates now that the economy is at or around "full employment" and inflationary pressures have been building to exceed its 2% target. It has, therefore, raised rates four times, with the last three following quickly on one another in December 2016 and March and June 2017. One or two more increases are expected in 2017 and possibly four in 2018.

Growth in the EU improved in 2016, to 1.7%, after the ECB cut rates into negative territory and embarked on massive quantitative easing during the year. The ECB is now forecasting growth of 1.9% in 2017, 1.8% in 2018 and 1.7% in 2019. It has committed to continuing major monthly quantitative easing purchases of debt instruments, though in April 2017 it reduced the rate from €80bn per month to €60bn, to continue until the end of 2017, in order to stimulate growth and to get inflation up to its 2% target.

There are major concerns about various stresses within the EU; these could even have the potential to call into question the EU project. The Dutch and French elections passed off without creating any waves for the EU but we still have a national election in Germany on 22 October; this is not currently expected to cause any significant change. What could be more problematic is the general election in Austria on 15 October where a major front runner is the Freedom Party which is strongly anti-immigration and anti EU. There is also a risk of a snap general election in Italy before the final end possible date of 20 May 2018. A continuing major stress point is dealing with the unsustainable level of national debt in Greece in the face of implacable opposition from Germany to any further bail out. High levels of unemployment in some EU countries and the free movement of people within the EU, together with the EU's fraught relationship with Turkey in controlling such people movements, are also major stress issues. On top of which the EU also now has to deal with Brexit negotiations with the UK.

China is expected to continue with reasonably strong growth, (by Chinese standards), of 6.5% in 2017. However, medium term risks are increasing. Japan has only achieved 1% growth in 2016 and is struggling to get inflation to move from around 0%, despite massive fiscal stimulus and monetary policy action by the Bank of Japan.

Detailed economic commentary on developments during quarter ended 30 June 2017

This section has been provided by **Capital Economics** and therefore includes their views and opinions of future trends and events.

- During the quarter ended 30 June 2017:

- The economy showed signs of re-accelerating;

- There was an intensifying squeeze on households' real earnings;

- The MPC took a more hawkish turn, with 3 members voting to raise interest rates;

- A snap General Election delivered a hung Parliament;

- Face-to-face negotiations with the EU began.

- After sluggish growth of 0.2% in Q1, the early indications are that the economy has re-gained some momentum in Q2. Indeed, the quarterly average of the Markit/CIPS all-sector PMI points to GDP growth of about 0.5% or so. Admittedly, the PMI pointed to a similar rate of growth in Q1, which didn't materialise. However, this is partly because the service sector PMI excludes the retail sector, which performed poorly in Q1 – sales volumes fell by a quarterly 1.6%. On the basis of the survey data and hard evidence released so far, retail sales look to have rebounded by over 1% in Q2.

- There is some concern, however, about the sustainability of consumer spending. After all, Q1's National Accounts showed that the 0.4% quarterly rise in spending was entirely funded through households reducing the proportion of their income that they save to just 1.7%, the lowest level since comparable records began. What's more, unsecured consumer borrowing has been rising at an annual rate of over 10%, prompting the Bank of England's Financial Policy Committee to bring forward its stress tests of UK banks' consumer loan books to July. It also increased the counter cyclical capital buffer that banks are required to hold from 0% to 0.5% and intends to increase that further to 1.0% in November. This will have little immediate impact on overall lending as most banks already hold capital in excess of the overall minimum required. However, the FPC also signalled that it is likely to take targeted action specifically on falling consumer credit quality at its next meeting in September after it has the results of its stress tests.

- That said, it could be argued that the drop in saving is an entirely rational response to what households perceive to be a temporary squeeze on their real incomes. Annual growth in the headline measure of average weekly earnings was just 2.1% in the three months to April, down from the 2.3% rate recorded in Q1 and below CPI inflation of 2.4% over the same period. Given that inflation picked up to 2.9% in May, the squeeze on real earnings is likely to have intensified since then.

- The weakness of wage growth still looks hard to square with the performance of the labour market. Employment growth has held up at an annual rate of 1.2% in April and the unemployment rate has continued to drift lower, reaching a new post-crisis low of 4.6%.

- Inflation has risen faster than expected. But this appears to be because the impact of the drop in the pound is feeding through faster than in previous depreciations, rather than by a larger amount. Note that price pressures at the beginning of the production pipeline are already beginning to fade. Producer input price inflation has fallen from a peak of almost 20% in January, to 11.6% in May. And output price inflation – which did not rise as far as its past relationship with input price inflation would have suggested anyway – has stood at 3.6% for three consecutive months now.

- Accordingly, inflation still looks set to peak before the end of this year, at around 3.2% in Q4. Given that it has accelerated more quickly than anticipated, it should fall back quicker as well. We think that inflation should be close to 2% by the end of 2018.

- Given the continued weakness in wage growth, and the fact that inflation's rise is set to be only temporary, it is perhaps surprising that the Monetary Policy Committee appeared to take a more hawkish stance in the second quarter.

- The Committee came its closest to voting for a rate hike since 2007 at its June meeting, with three out of eight members (Kristin Forbes, Michael Saunders and Ian McCafferty) voting to increase Bank Rate by 0.25%. There have been some indications that the rift between MPC members has grown since then, with Bank of England Chief Economist, Andy Haldane, also giving a relatively hawkish speech in which he indicated that he would probably vote to raise interest rates in the second half of 2017. This is particularly symbolic given that he is a Bank "insider" and has typically been quite dovish.

- However, Kristin Forbes term came to an end on 30th June – she will be replaced by Silvana Tenreyro at the next meeting in August. However, we do not know much about Ms Tenreyro's views on UK monetary policy. As a result, the next meeting could see a 5-3 split once again though a 4-4 split with Carney voting for a rise, would put him in the deciding vote hot seat, (until the MPC is restored to its full nine person membership by filling one vacancy).

- However, despite the media reporting that Carney had shifted his view to a more hawkish position between his two speeches in June, it is not at all clear that he is on the cusp of voting to raise interest rates. In particular, his list of specific conditions, including signs that wage growth is firming, and that business investment and net trade pick up the slack from slower consumer spending growth, may not be met.

- One possibility is that the MPC could vote to simply reverse the emergency cut in interest rates that took place following the EU referendum, but then leaves rates on hold for a while thereafter. This appears to be an argument that one or two MPC members are sympathetic to. That said, markets still expect rates to remain on hold until August 2018, around six months earlier than they thought at the end of Q1.

- Meanwhile, the public finances started the fiscal year on a fairly solid footing, with borrowing in April and May in line with last year's outturn. Note, however, that the Office for Budget Responsibility expects borrowing to rise this fiscal year as a whole by £7bn, as a number of temporary factors – including income shifting related to the rise in the dividend tax rate – unwind.

- What's more, borrowing could increase further if the Government is forced to ease back on austerity at the autumn Budget. The snap general election on June 8th saw the Conservatives fail to gain an overall majority, and instead the party has had to agree a confidence and supply agreement with the Northern Irish Democratic Unionist Party (DUP). The fact that votes on the Queen's Speech were passed without too much difficulty suggests this should be able to function for a while. But the fragile nature of the arrangement could see the Government soften its stance on Brexit and austerity, in order to ensure legislation is passed.

- Face-to-face negotiations with the EU started in June. The Government capitulated on day one to the EU's demand that the withdrawal and future arrangements occur in sequence, rather than in parallel. What's more, the Government appeared to concede some ground to the EU in its initial offer on citizens' rights, including allowing the exporting of EU citizens' child benefits. We have not learnt much in terms of what Brexit will ultimately look like from the initial exchanges, although it still looks likely that the UK will leave the single market and customs union.

- Finally, in financial markets, the FTSE 100 index and FTSE UK Local Index (which only includes firms that make 70% of their sales domestically) have fallen by 0.4% and 0.1% respectively. Most of this decline occurred in June, and probably reflects a combination of election uncertainty as well as the prospect of higher interest rates. Meanwhile, 10-year gilt yields rose by 12bp between end-Q1 and end-Q2. However, there was significant variation within the quarter, with yields falling to as low as 0.9%, before picking up following a more hawkish turn by the MPC.

About Capital Economics

Capital Economics is one of the leading independent economic research companies in the world. Its large team of more than 60 experienced economists provides award-winning macroeconomic, financial market and sectoral analysis, forecasts and consultancy, from offices in London, New York, Toronto, Sydney and Singapore.

Founded in 1999, it has gained an enviable reputation for original and insightful analysis, and has built up a diverse and distinguished client base. The majority are in the financial sector, including some of the world's largest investment banks and wealth managers, as well as smaller and more specialist firms. But it also have a growing number of corporate clients from a wide range of sectors and industries, and many relationships with governments and central banks, both in advanced and emerging economies.

Appendix C

Detailed commentary on interest rate forecasts

Capita Asset Services have provided us with the following update to their interest rate forecasts.

May quarterly inflation report review

- Following the latest Bank of England quarterly Inflation Report on 11 May, we have reviewed the forecasts we did on 8 February after the previous quarterly Inflation Report for February 2017. However, we would draw your attention to our newsflash on 3 April where we made an interim adjustment to our forecasts for PWLB rates by reducing our forecasts for quarter 2 2017 by 20 bps to reflect the fact that gilt yields had settled lower since February. Today's forecasts incorporate that interim adjustment and we have lowered following quarters in keeping with the continuing lower gilt yields. We have also made some minor adjustments by lowering a few 25 and 50 year PWLB rate forecasts by 10 bps in later quarters. We have left our forecasts for Bank Rate unchanged.

- The key points from the latest Inflation Report are as follows: -

- Forecast for GDP growth for 2017 shaved from 2.0% to 1.9% to reflect a weak start in quarter 1 of only +0.3%, (but the Bank expects that figure to be revised to +0.4%); 2018 and 2019 upped from 1.8% to 1.9%. (2016 was 1.8%.)

- Little change in inflation forecasts; inflation to fall back to 2.2% in just over 2 years' time and to pick up slightly going into 2020.

- In February, the Bank cut the equilibrium rate of unemployment from 5.0% to 4.5%. This potentially means that the MPC could wait longer before taking action to combat rising inflation.

- Some MPC members were clearly more concerned about the degree to which they could look through increases in inflation caused by the effective devaluation of the pound since the referendum and the consequent feed through into the CPI measure on inflation.

· Our forecasts assume that there is no cancellation of the emergency cut in Bank Rate in August 2016 from 0.50% to 0.25% and a stop to the Quantitative Easing (QE) programme in the shorter-term. There is a potential risk that the MPC could muster a majority to reverse both before reaching a time when there is a progression to a sustained trend of gentle increases in Bank Rate. Our forecasts for both Bank Rate and PWLB rates would then need revision if both were to occur.

· Our overall view is that there is now need for some caution over forecasts for GDP growth as quarter 1 2017 GDP growth was noticeably weaker; this can be explained by the rise in inflation eating into consumers' disposable income and spending power. The Inflation Report stated that the Bank expected a continuation of strong growth near to 2% on the assumption that foreign trade and business investment would counteract a fall back in consumer spending. The Bank also made a major assumption that there would be a smooth adjustment of the UK's relationship with the EU. Again, we feel some caution around both assumptions.

· The Bank also warned that markets were too pessimistic in thinking Bank Rate would not start rising until towards the end of 2019 as the Bank expects wage growth to accelerate

due to continuing falls in unemployment and rising vacancy levels. Again, we do feel some caution on this area as wage growth has been remarkably benign despite continuing falls in unemployment; this may reflect hidden levels of unemployment e.g. people wanting to move from part time to full time employment. We do feel that the MPC will focus on inflation risks, ahead of protecting growth, if inflation looks like rising to levels significantly above current forecasts. However, it is very difficult to be at all certain about risks around this, especially when currency movements in the pound, dollar and euro will be very hard to predict and are subject to major unknowns. It is notable that sterling has now recovered from around $1.20 to the pound after the referendum to around $1.30. However, the Fed is expected to embark on quarterly increases in interest rates and this should cause the dollar to strengthen, i.e. the value of sterling against the dollar is likely to fall back again over the next couple of years.

- Capital Economics' forecasts for UK economic growth are as follows: 2017 +2.0%; 2018 +2.3%; 2019 +2.0%. They feel that pessimism is still being overdone by the Bank and Brexit will not have as big an effect as initially feared by some commentators. They are forecasting that the first increase in Bank Rate will occur in quarter 2 2018 whereas our first increase is in quarter 2 2019 - after the end of Brexit negotiations.

- One major uncertainty is the degree to which there will be a major financial stimulus programme in the US - depending on the degree of agreement, or otherwise, between President Trump and Congress. If this stimulus programme is substantial, this is likely to have, in turn, a significant impact on the rise in inflation pressures and the speed of increases in the Fed. Rate. There are also concerns as to whether the US will enter into a trade and currency value conflict with other major trading nations. The value of the dollar against other currencies has been subject to major volatility since the Presidential election and this is likely to continue. It is to be noted that after 6 months of Trump's presidency, there has been little substantial progress on a fiscal stimulus so this will weaken world growth expectations in the near future. In addition, it now appears there is a significant weakening in Chinese economic growth. However, the risk of a trade war between America and China appears to have evaporated as China has become a vital partner to the US in curbing North Korea's nuclear ambitions.

- **Rising EU and geopolitical risks e.g.**

  - Greece continues to cause major stress in the EU due to its tardiness and reluctance in implementing key reforms required by the EU to make the country more efficient and to make significant progress towards the country being able to pay its way – and before the EU is prepared to agree to release further bail out funds. A crunch point is imminent this summer when Greece needs to make major repayments it will not be able to make unless there is a new bail out which is very unlikely ahead of the general election due in Germany before late October. However, in the usual EU approach, another fudge looks probable so as to avoid a crisis ahead of the imminent German general election.

  - Spain has had two general elections in 2015 and 2016, both of which failed to produce a workable government with a majority of the 350 seats. At the eleventh hour on 31 October, before it would have become compulsory to call a third general election, the party with the biggest bloc of seats (137), was given a majority confidence vote to form a government. This is potentially a highly unstable situation,

particularly given the need to deal with an EU demand for implementation of a package of austerity cuts which will be highly unpopular.

- The under capitalisation of Italian banks poses a major risk with state aid firmly ruled out by the EU as a potential way out. Progress has been made in sorting out the dire under capitalisation of a few very small banks but this leaves major issues still to be dealt with.

- Italian general election; the latest possible date for a general election in Italy is 20 May 2018. The constitutional referendum last December, on reforming the Senate and reducing its powers, became a confidence vote on Prime Minister Renzi who duly resigned when he lost the vote. The rejection of these proposals stopped progress to fundamental political and economic reform which is urgently needed to deal with Italy's core problems, especially low growth. They were also intended to give Italy more stable government as no western European country has had such a multiplicity of governments since the Second World War, due to the equal split of power between the two chambers of the Parliament which are both voted in by the Italian electorate but by using different voting systems. This means there is now major uncertainty about the road ahead for Italy and its ability to tackle the needed major reform. Italy has the third biggest government debt mountain in the world.

- German Federal election 22 October 2017. Chancellor Merkel currently looks in a strong position to retain power. However, this could be affected by significant shifts in voter intentions as a result of terrorist attacks, dealing with a huge influx of immigrants, and a rise in anti EU sentiment.

- Austria general election 15 October. What could be more problematic is this general election in Austria where a major front runner is the Freedom Party which is strongly anti-immigration and anti EU. If it gains substantial power, or influence in a coalition, this could create waves for the core EU policy, (note, not just the Eurozone currency area), of free movement of people – which is also a key issue for Brexit negotiations and with the Visegrad bloc of former communist states.

- Economic growth in the EU, (the UK's biggest trading partner), has been lacklustre for a long time despite the ECB cutting its main policy rate to -0.4% and embarking on a massive programme of quantitative easing during 2016. However, growth has picked up during 2016 to reach an overall figure of 1.7% for the year for the Eurozone. Current forecasts are for growth to improve to 1.9% in 2017.

- US. GDP growth has been highly volatile in 2016 but overall mediocre, at an average of 1.6% for the year. Quarter 1 in 2017 has also been mediocre at 1.4% but current indications are that growth could rebound strongly in quarter 2. The disappointment so far has been the lack of decisive action from President Trump to make progress with his promised fiscal stimulus package. The Fed has, therefore, started on the upswing in rates now that the economy is at or around "full employment" and inflationary pressures have been building to exceed its 2% target. It has, therefore, raised rates four times, with the last three following quickly on one another in December 2016 and March and June 2017. One or two more increases are expected in 2017 and possibly four in 2018.

- Japan is struggling to stimulate consistent significant growth to get inflation up to its target of 2% despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.

- Chinese economic growth has been weakening despite successive rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems.

CAPITA ASSET SERVICES' FORWARD VIEW

Economic forecasting remains difficult with so many external influences weighing on the UK. Our Bank Rate forecasts, (and also MPC decisions), will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Forecasts for average earnings beyond the three year time horizon will be heavily dependent on economic and political developments. Major volatility in bond yields is likely to endure as investor fears and confidence ebb and flow between favouring more risky assets i.e. equities, or the safe haven of bonds.

The overall longer run trend is for gilt yields and PWLB rates to rise, albeit gently. A world economic recovery will likely see investors switching from the safe haven of bonds to equities.

We have pointed out consistently that the Fed. Rate is likely to go up more quickly and more strongly than Bank Rate in the UK and recent events have not changed that view, just that the timing of such increases may well have been deferred somewhat during 2016. While there is normally a high degree of correlation between the two yields, we would expect to see a growing decoupling of yields between the two i.e. we would expect US yields to go up faster than UK yields. We will need to monitor this area closely and the resulting effect on PWLB rates.

- The overall balance of risks to economic recovery in the UK remains to the downside, particularly with the current uncertainty over the final terms of Brexit.

- The balance of risks to increases in Bank Rate and shorter term PWLB rates are to the upside and are dependent on how quickly inflation pressures rise and how high the peak will be.

- Our forecasts are predicated on an assumption that there is no break-up of the Eurozone or EU, (apart from the departure of the UK), within our forecasting time period despite the major challenges that are looming up, and that there are no major ructions in international relations, especially between the US and China, which have a major impact on international trade and world GDP growth.

We would, as always, remind clients of the view that we have expressed in our previous interest rate revision newsflashes of just how unpredictable PWLB rates and bond yields are at present. We are experiencing exceptional levels of volatility which are highly correlated to geo-political and sovereign debt crisis developments. Our revised forecasts are based on the Certainty Rate (minus 20 bps) which has been accessible to most authorities since 1st November 2012.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- Geopolitical risks in Europe, the Middle East and Asia, which could lead to increasing safe haven flows.
- UK economic growth and increases in inflation are weaker than we currently anticipate.
- Weak growth or recession in the UK's main trading partners - the EU and US.
- A resurgence of the Eurozone sovereign debt crisis.
- Weak capitalisation of some European banks.
- Monetary policy action failing to stimulate sustainable growth and combat the threat of deflation in western economies, especially the Eurozone and Japan.

The potential for upside risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -

- The pace and timing of increases in the Fed. Funds Rate causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.
- UK inflation returning to significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

Borrowing advice: although yields have risen from their low points, yields are still at historic lows and borrowing should be considered if appropriate to your strategy. We still see value in the 40yr to 50yr range at present but that view would be negated if Bank Rate does not climb to at least 2.5% over the coming years. Accordingly, clients will need to review and assess their risk appetite in terms of any underlying borrowing requirement they may have, and also project forward their position in respect of cash backed resources.

Any new borrowing should also take into account the continuing cost of carry, the difference between investment earnings and borrowing rates, especially as our forecasts indicate that Bank Rate may not rise from 0.25% until quarter 2 2019 and then will only rise slowly.

As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts. The general expectation for an eventual trend of gently rising gilt yields and PWLB rates is expected to remain unchanged. Negative, (or positive), developments could significantly impact safe-haven flows of investor money into UK, US and German bonds and produce shorter term movements away from our central forecasts.

Our interest rate forecast for Bank Rate is in steps of 25 bps whereas PWLB forecasts have been rounded to the nearest 10 bps and are central forecasts within bands of + / - 25 bps.

Naturally, we continue to monitor events and will update our forecasts as and when appropriate.

	Bank Rate %		PWLB Borrowing Rates % (including 0.20% certainty rate adjustment)							
			5 year		10 year		25 year		50 year	
	Aug 17	Mar 17	Aug 17	Mar 17	Aug 17	Mar 17	Aug 17	Mar 17	Aug 17	Mar 17
Sep-17	0.25	0.25	1.40	1.60	2.10	2.30	2.80	2.90	2.80	2.70
Dec-17	0.25	0.25	1.50	1.60	2.20	2.30	2.90	3.00	2.70	2.80
Mar-18	0.25	0.25	1.60	1.70	2.30	2.30	2.90	3.00	2.70	2.80
Jun-18	0.25	0.25	1.70	1.70	2.30	2.40	3.00	3.00	2.80	2.80
Sep-18	0.25	0.25	1.70	1.70	2.40	2.40	3.00	3.10	2.90	2.90
Dec-18	0.25	0.25	1.80	1.80	2.40	2.40	3.10	3.10	2.90	2.90
Mar-19	0.25	0.25	1.80	1.80	2.50	2.50	3.10	3.20	2.90	3.00
Jun-19	0.50	0.50	1.90	1.90	2.50	2.50	3.20	3.20	3.00	3.00
Sep-19	0.50	0.50	1.90	1.90	2.60	2.60	3.30	3.30	3.00	3.10
Dec-19	0.75	0.75	2.00	2.00	2.60	2.60	3.30	3.30	3.10	3.10
Mar-20	0.75	0.75	2.00	2.00	2.70	2.70	3.30	3.40	3.10	3.20

Markets in Financial Instruments Directive (MiFID) II

The Financial Conduct Authority (FCA) explains that the Markets in Financial Instruments Directive is the EU legislation that regulates firms who provide services to clients linked to 'financial instruments' (shares, bonds, units in collective investment schemes and derivatives), and the venues where those instruments are traded.

The Markets in Financial Instruments Directive (MiFID) is the framework of European Union (EU) legislation for:

• investment intermediaries that provide services to clients around shares, bonds, units in collective investment schemes and derivatives (collectively known as 'financial instruments'), and

• the organised trading of financial instruments

MiFID was applied in the UK from November 2007, but is now being revised to improve the functioning of financial markets in light of the financial crisis and to strengthen investor protection.

The changes are currently set to take effect from 3 January 2018, with the new legislation being known as MiFID II - this includes a revised MiFID and a new Markets in Financial Instruments Regulation (MiFIR).

The FCA released a new Policy Statement on 3 July 2017. This included a finalised position for the client categorisation of Local Authorities, which will come into effect as part of the full introduction of MiFID II on 3 January 2018.

MiFID II does not cover simple term deposits. It is only focussed on regulated products, which would include direct investments such as Certificates of Deposit, Gilts, Corporate Bonds, and investment funds (including Money Market Funds - MMFs).

Under MiFID II, the FCA is obliged to treat by default all Local Authorities as "retail clients" under EU legislation. However, the regulator does offer the option to "opt up" to being an Elective Professional Client if the authority meets certain criteria.

Opt-Up Process under MiFID II

To be considered as a Professional Client, an authority will now need to make that choice in writing and meet requirements set by the FCA.

Qualitative criteria will be set by the counterparties and will be tailored to the specific products. It is unlikely that a client authority could produce one document that it could use to satisfy all potential requirements. Each firm will present their clients with slightly different forms and content as they will be drafted to the specific products being offered. This introduces a new administrative burden to the treasury management function.

The quantitative test includes a minimum financial instrument portfolio size of £10 million. Previously limits of £15m or even £20m had been considered, which would have prevented many local authorities from opting up to Professional Client status. The portfolio size is likely to be measured at the point at which the authority requests to opt up, rather than at the balance sheet date.

If local authorities do not meet the minimum portfolio size requirement, the biggest potential consequence could be that they may no longer be able to use MMFs.

In addition to passing the £10m portfolio size test, a local authority would need to satisfy one of the following criteria to opt-up:

- Ten transactions per quarter in a relevant market in the past four quarters; or
- At least one year experience in a professional position in financial markets which requires knowledge of transactions or services envisaged.

The advice of Capita Asset Services is that because opting-up would be product by product, it would be better to prioritise applications to concentrate on those products used most frequently.

Appendix E

CIPFA Consultations on the Prudential and Treasury Management Codes

The Chartered Institute of Public Finance and Accountancy (CIPFA) have issued consultations on proposed changes to the Code of Practice on Treasury Management and the Prudential Code. Responses to CIPFA are required by 30 September 2017.

The proposed changes would be made either in the Codes or the sector-related guidance. The proposals and questions in the consultation documents are as follows.

Treasury Management Code

Treasury Management Indicators

- Change the principal invested for longer than 364 days indicator to principal invested over 365 days in line with financial reporting definitions,
- Remove the interest rate exposure indictor and require TM Strategy to state how interest rate exposure is managed and monitored, and
- Extend the maturity structure of borrowing indicator to cover variable as well as fixed rate debt.

Do you agree with the proposed indicator changes?

Non Treasury Investments

It is intended to clarify that the Code does cover all investments held primarily for financial returns, which may include some service investments. The annex to the consultation contains an extract of the substantive changes proposed to the code and in respect of non-treasury investments; attention is drawn to the introduction, policy statement and the new TMP 13 along with a requirement to maintain a schedule of non-treasury management investments alongside the treasury management strategy.

Do you agree with the clarification that the Code should cover all investments held primarily for financial returns and the proposed amendments to the Code set out in the Annex?

Reporting

It is proposed to allow some reporting of detailed indicators and monitoring information to a committee or sub-committee whilst making clear that responsibility remains with the board/full council.

Do you agree with the proposal to allow some delegation of reporting to a committee/sub-committee in order to promote more active engagement and with the subsequent changes proposed to the Code?

Other changes

A number of general suggestions were made by respondents to consultation earlier in the year as to areas which are not fully covered by the current principles, including borrowing coverage, MiFID II, Cost of Carry indicator, Liquidity measure, TM Policy being part of TMSS, Diversification Policy, and Housing Association Guidance. These areas will all be picked up in future updates of sector specific guidance, and references have been updated as necessary.

Are there any other comments you wish to make, including on the proposed substantive changes set out in the Annex?

Prudential Code

Objectives of the Prudential Code

Objective iii) is that treasury management decisions are taken in accordance with good professional practice, and a number of respondents to earlier consultation queried whether the Prudential Code was the appropriate place for the “Adoption of the Treasury Management Code” prudential indicator, especially given that local authorities are statutorily required to “have regard” to both Codes.

It is therefore proposed that objective iii) be deleted and the requirement of the Prudential Code to adopt CIPFA's Treasury Management Code is removed.

Do you agree that the requirement of the Prudential Code to adopt CIPFA's Treasury Management Code is removed?

Mayors, Combined Authorities and the Group Entity

It is proposed that the revised code confirm that the underlying principles apply to mayors and combined authorities and the group entity, but that the use of local indicators is encouraged to recognise the differing impact of residual liabilities on the individual local authority.

It is proposed that a requirement to consider the affordability of borrowing in respect of ring-fenced borrowing in addition to overall resources is introduced. This requirement can be met through the use of local indicators. Given that the HRA is effectively such a separate ring-fenced fund, the specific requirements in respect of the HRA have been removed as it is considered that the previous requirements will be met by the new requirement.

Do you agree that the Code confirm that the underlying principles apply to mayors and combined authorities and the group entity?

Do you agree that the impact of such structures is best dealt with through the use of local indicators?

Do you agree with the requirement to consider explicitly separate ring-fenced funding streams and that this requirement removes the need to specify separate requirements for the HRA?

Ensuring Prudence

It is proposed to introduce a requirement to report on the overall capital strategy to full council in order to demonstrate that the authority takes capital expenditure and investment decisions in line with service objectives; and properly takes account of stewardship, value for money, prudence, sustainability, and affordability. The capital strategy should sets out the long term context in which capital expenditure and investment decisions are made; and give due consideration to both risk and reward, and impact on the achievement of priority outcomes.

In developing the capital strategy authorities are encouraged to strike a balance between the amount of detail included and accessibility to the key audience. Links should be made where appropriate to the Treasury Management Strategy.

The capital strategy also allows borrowing for capital investment to be considered alongside more commercial type and third party investment so that the overall impact on affordability and risk on the financial sustainability of the authority can be identified and understood. This is particularly important as with increasing commercialisation it is vital that authorities identify all potential liabilities and risks, and consider the combined impact on the overall financial position of the authority to ensure such activity remains proportionate.

In order to support an effective approach to risk management, and in line with the requirement for the Revenue Budget, it is proposed that the Chief Finance Officer should report explicitly on the deliverability, affordability and risk associated with the capital strategy. It is also proposed that the code recognises explicitly that the Chief Finance Officer may need access to specialised advice to enable them to reach their conclusions.

It is proposed to remove the indicator relating to council tax impact to allow focus on a longer term and more informed view of affordability rather than relying upon a slightly contrived indicator.

Do you agree with the proposal to introduce the requirement for a capital strategy to be formally reported?

Do you agree with a principles based approach and that the key matters to be taken into account are reflected in the proposed wording within the annex?

Do you agree with the proposal to require the chief financial officer to report explicitly on the risks associated with the capital strategy?

Do you agree with the proposal to delete the council tax indicator?