REPORT TITLE: TREASURY MANAGEMENT STRATEGY 2018/19

14 FEBRUARY 2018

REPORT OF PORTFOLIO HOLDER: FINANCE - Cllr. Guy Ashton

Contact Officer: Joseph Holmes Tel No: 01962 848220
Email: jholmes@winchester.gov.uk

WARD(S): ALL WARDS

PURPOSE

This report sets out the proposed Treasury Management Strategy, the Annual Investment Strategy, the Prudential Indicators and the Minimum Revenue Provision Policy Statement for the Council for 2018/19.

RECOMMENDATIONS: to Cabinet and Council:

1. That the Treasury Management Strategy Statement (TMSS) and Annual Investment Strategy for 2018/19 (and the remainder of 2017/18) including:

   - Annual Borrowing Strategy 2018/19 (see paragraph 13)
   - Prudential Indicators 2018/19 to 2020/21 (see Appendix C)
   - Minimum Revenue Provision (MRP) Policy Statement (see Appendix D)
   - That authority is delegated to the Section 151 Officer, who in turn delegates to Hampshire County Council's Director of Corporate Resources, as agreed in the Service Level Agreement, to manage all Council investments (other than the high yield investment portfolio) according to the risk assessment process in the Investment Strategy as appropriate.

2. That on an annual basis regarding MiFID II regulation, the Elective Professional Status of the Council is maintained, and that, in electing for professional client status, it acknowledges and agrees to forgo the protections available to retail clients attached at Appendix E.

IMPLICATIONS:

1 COUNCIL STRATEGY OUTCOME

1.1 Treasury management is an integral part of helping the deliver the Council Strategy and all of its outcomes.

2 FINANCIAL IMPLICATIONS

2.1 Effective treasury management ensures both the financial security and liquidity of the Council.

3 LEGAL AND PROCUREMENT IMPLICATIONS

3.1 The Council's Treasury Management Strategy follows the latest DCLG and CIPFA guidance where it is available. With effect from September 2014 Hampshire County Council (HCC) and Winchester City Council (WCC) established arrangements for the joint discharge of functions under Section (101)(1) and (5) of the Local Government Act 1972 and Section 9EA and 9EB Local Government Act 2000. Under this arrangement HCC's Investments and Borrowing Team provide a Treasury Service which includes the management of Winchester City Council's cash balances and investment of surplus cash or sourcing of short-term borrowing in accordance with the agreed TMSS.

4 WORKFORCE IMPLICATIONS

4.1 None.

5 PROPERTY AND ASSET IMPLICATIONS

5.1 None.

6 CONSULTATION AND COMMUNICATION

6.1 The Overview and Scrutiny Committee discussed the report at its meeting held on 29 January 2017 where officers and members of Cabinet responded to detailed questions. At the conclusion of questions and debate, the Committee agreed that there were no particular matters that it wished to raise for Cabinet to further consider.

7 ENVIRONMENTAL CONSIDERATIONS

7.1 None.

8 EQUALITY IMPACT ASSESSMENT

8.1 None.

9 RISK MANAGEMENT

Risk	Mitigation	Opportunities
Returns from investments are too low	A diversified strategy that attempts to manage the balance between liquidity risk, credit risk and yield within the Council's risk appetite.	
A counterparty fails	A diversified strategy that has relatively low levels of counterparty risk.	
Cash is not available	A balanced portfolio of liquid and long term funds are held to ensure cash is available to utilise. The Council also mitigates this risk through cashflow forecasting. The Council can also access intra Local Authority short term loans at very low rates (sub 0.5%) for any day to day cashflow requirements	More accurate and immediate cashflow forecasting can help improve the return on investments through more active treasury management activity.

SUPPORTING INFORMATION:

10 INTRODUCTION

10.1 Winchester City Council has historically followed the latest guidance which requires the Council to approve a treasury management strategy before the start of each financial year; the investment strategy is embedded within this Treasury Management Strategy (TMS).

10.2 CIPFA consulted on changes to the Code in 2017, and published its new 2017 edition of Treasury Management in the Public Services: Code of Practice and Cross-sectoral Notes at the end of 2017 and Prudential Code for Capital Finance in Local Authorities. These new Codes, along with the Treasury Management Code Guidance Notes which include the Treasury Management Indicators, and the new CLG Guidance (neither of which are yet available) form the new regulatory framework for treasury management. The 2018/19 Strategy has been produced with reference to these Codes; once the relevant guidance is available the 2019/20 strategy will reflect this guidance as appropriate.

10.3 This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the CLG Guidance.

10.4 Treasury management is focussed on the security and liquidity of the Council and is tailored to ensure that the Council is in a position to meet all of its financial commitments in a timely manner. Investment management concerns itself more with yield or return, balancing the risks and rewards implicit in those returns, ensuring that all such investments are within the Council's risk tolerances, including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's treasury management strategy.

11 EXTERNAL CONTEXT

11.1 The following paragraphs explain the economic and financial background against which the Treasury Management Strategy is being set.

Economic background

11.2 The major external influence on the Council's treasury management strategy for 2018/19 will be the UK's progress in negotiating its exit from the European Union and agreeing future trading arrangements. The domestic economy has remained relatively robust since the outcome of the 2016 referendum, but there are indications that uncertainty over the future is now weighing on growth. Transitional arrangements may prevent a cliff-edge, but will also extend the period of economic uncertainty further. The OECD (Organisation for Economic Co-operation and Development) has forecast economic growth to remain sluggish throughout 2018/19 compared to other nations.

11.3 Consumer price inflation (CPI) reached 3.0% in September 2017 as the post-referendum devaluation of sterling continued to feed through to imports. Unemployment continued to fall and the Bank of England's Monetary Policy Committee judged that the extent of spare capacity in the economy seemed limited and the pace at which the economy can grow without generating inflationary pressure had fallen over recent years. The Bank of England's Monetary Policy Committee raised official interest rates to 0.5% in November 2017. Since this point, CPI hit 3.1% in November 2017.

Credit outlook

11.4 High profile bank failures in Italy and Portugal have reinforced concerns over the health of the European banking sector. Sluggish economies and fines for pre-crisis behaviour continue to weigh on bank profits, and any future economic slowdown will exacerbate concerns in this regard.

11.5 Bail-in legislation, which ensures that large investors including local authorities will rescue failing banks instead of taxpayers in the future, has now been fully implemented in the European Union, Switzerland and USA, while Australia and Canada are progressing with their own plans. In addition, the largest UK banks will ringfence their retail banking functions into separate legal entities during 2018. There remains some uncertainty over how these changes will impact upon the credit strength of the residual legal entities.

11.6 The credit risk associated with making unsecured bank deposits has therefore increased relative to the risk of other investment options available to the Council; returns from cash deposits however remain very low.

Interest rate forecast

11.7 The Council's treasury adviser Arlingclose's central case is for UK Bank Rate to remain at 0.50% during 2018/19, following the rise from the historic low of 0.25%. The Monetary Policy Committee re-emphasised that any prospective increases in Bank Rate would be expected to be at a gradual pace and to a limited extent.

11.8 Future expectations for higher short term interest rates are subdued and on-going decisions remain data dependant and negotiations on exiting the EU cast a shadow over monetary policy decisions. The risks to Arlingclose's forecast are broadly balanced on both sides. The Arlingclose central case is for gilt yields to remain broadly stable across the medium term. Upward movement will be limited, although the UK government's seemingly deteriorating fiscal stance is an upside risk.

11.9 A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix A.

12 LOCAL CONTEXT

12.1 On 30 November 2017, the Council had £156.7m of borrowing and £57.1m of investments. This is set out in further detail at Appendix B. Forecast changes in these sums are shown in the balance sheet analysis in Table 1 below.

Table 1: Balance sheet summary and forecast

	31.03.17 Actual £m	**31.03.18 Estimate £m**	**31.03.19 Forecast £m**	**31.03.20 Forecast £m**	**31.03.21 Forecast £m**
General Fund CFR	8.2	12.5	47.1	75.8	86.1
HRA CFR	162.1	165.1	160.8	162.6	163.4
Total CFR	**170.3**	**177.6**	**207.9**	**238.4**	**249.5**
Less: Other debt liabilities *	(0.8)	(0.5)	(0.2)	(2.4)	(2.1)
Borrowing CFR	**169.5**	**177.1**	**207.7**	**236.0**	**247.4**
Less: External borrowing **	(156.7)	(156.7)	(156.7)	(156.7)	(156.7)
Internal (over) borrowing	**12.8**	**20.4**	**51.0**	**79.3**	**90.7**
Less: GF Usable reserves	(30.5)	(28.7)	(21.3)	(20.4)	(18.9)
Less: HRA Usable reserves	(16.9)	(13.1)	(12.1)	(8.2)	(9.1)
Less: Working capital	(12.3)	(12.3)	(12.3)	(12.3)	(12.3)
Resources for investments	**(59.7)**	**(54.1)**	**(45.7)**	**(40.9)**	**(40.3)**
New borrowing or (investments)	**(46.9)**	**(33.7)**	**5.3**	**38.4**	**50.4**

* finance leases, PFI liabilities and transferred debt that form part of the Council's total debt

** shows only loans to which the Council is committed and excludes optional refinancing

12.2 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

12.3 The Council has a forecast increasing CFR due to the planned capital programme over the coming years, and the Council's reserves will gradually reduce over the same period. If the capital programme is delivered as planned, this will require the Council to take out new borrowing during the forecast period..

12.4 CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Council expects to comply with this recommendation during 2018/19.

13 BORROWING STRATEGY

13.1 The Council currently holds £156.7 million of loans as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in Table 1 shows that the Council may need to borrow up to £5.3m in 2018/19 if it delivers its capital programme in full. The Council may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £213 million.

Objectives

13.2 The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

Strategy

13.3 Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, when the Council does borrow, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

13.4 By internally borrowing, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal and short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Council with this 'cost of carry' and breakeven analysis.

13.5 In addition, the Council may borrow (normally for up to one month) short-term loans to cover unplanned cash flow shortages.

Sources of borrowing

13.6 The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB) and any successor body
- UK local authorities
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except Hampshire Pension Fund)
- capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local Council bond issues

Other sources of debt finance:

13.7 In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- operating and finance leases
- hire purchase
- Private Finance Initiative
- sale and leaseback

13.8 The Council has previously raised all of its long-term borrowing from the PWLB but it continues to investigate other sources of finance, such as local authority loans and bank loans, that may be available at more favourable rates.

Municipal Bonds Agency

13.9 UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a joint and several guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to full Council.

Short-term and variable rate loans

13.10 These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators at Section 16 of this strategy.

Debt rescheduling

13.11 The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

14 INVESTMENT STRATEGY

14.1 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's investment balance has ranged between £45.2 and £73.9 million.

Objectives

14.2 Both the CIPFA Code and the CLG Guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

Negative interest rates

14.3 If the UK enters into a recession in 2018/19, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

Strategy

14.4 Given the increasing risk and very low returns from short-term unsecured bank investments, the Council aims to further diversify into more secure and/or higher yielding asset classes during 2018/19. This is especially the case for the estimated £20m that is available for longer-term investment. At 30 November 2017 approximately 63% (increased from 50% last year) of the Council's surplus cash was invested so that it is not subject to bail-in risk, as it was invested in local authorities, pooled property and equity funds, and secured bank bonds. Whilst the remaining cash is subject to bail-in risk, 14% is held in short-term notice accounts which produce a return commensurate with the bail-in risk, 58% is held in overnight money market funds which are subject to a reduced risk of bail in, 17% is held in certificates of deposit which can be sold on the secondary market, and the remaining 4% of cash subject to bail-in risk is held in overnight bank call accounts for liquidity purposes. Further detail is provided at Appendix B. This diversification will represent a continuation of the new strategy adopted in 2015/16.

Investment limits

14.5 The maximum that will be lent to any one organisation (other than the UK Government) will be £7 million. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, and, investments in pooled funds, as they would not count against a limit for any single foreign country, since the risk is diversified over many countries.

Table 2: Investment limits

	Cash limit
Any single organisation, except the UK Central Government	£7m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£7m per group
Any group of pooled funds under the same management	£7m per manager
Money Market Funds	50% in total

Approved counterparties

14.6 The Council may invest its surplus funds with any of the counterparty types in Table 3 below, subject to the cash limits (per counterparty) and the time limits shown.

Table 3: Approved investment counterparties and limits

Credit rating	Banks unsecured	Banks secured	Government	Corporates
UK Govt	n/a	n/a	£ Unlimited 30 years	n/a
AAA	£3.5m 5 years	£7m 20 years	£7m 50 years	£3.5m 20 years
AA+	£3.5m 5 years	£7m 10 years	£7m 25 years	£3.5m 10 years
AA	£3.5m 4 years	£7m 5 years	£7m 15 years	£3.5m 5 years
AA-	£3.5m 3 years	£7m 4 years	£7m 10 years	£3.5m 4 years
A+	£3.5m 2 years	£7m 3 years	£3.5m 5 years	£3.5m 3 years
A	£3.5m 13 months	£7m 2 years	£3.5m 5 years	£3.5m 2 years
A-	£3.5m 6 months	£7m 13 months	£3.5m 5 years	£3.5m 13 months
None	£1m 6 months	n/a	£7m 25 years	£3.5m 10 years
Pooled funds	£7m per fund			

This table must be read in conjunction with the notes below

Credit rating

14.7 Investment limits are set by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

Banks unsecured

14.8 Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

Banks secured

14.9 Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

Government

14.10 Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 30 years.

Corporates

14.11 Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made following the governance structure and process as detailed in the Treasury Management Mid-Year Review 2017/18.

Pooled funds

14.12 Shares in diversified investment vehicles consisting of any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity and very low or no volatility will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

14.13 Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council’s investment objectives will be monitored regularly.

Operational bank accounts

14.14 The Council may incur operational exposures, for example through current accounts, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but are still subject to the risk of a bank bail-in, and balances will therefore be kept low. The Council’s operational bank account is with National Westminster; therefore the Fund does not hold unsecured investments in this bank, and aims to keep the overnight balances held in current accounts positive, and as close to £0 as possible. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

Risk assessment and credit ratings

14.15 Credit ratings are obtained and monitored by the Council’s treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made;
- any existing investments that can be recalled or sold at no cost will be; and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

14.16 Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as “rating watch negative” or “credit watch negative”) so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Other information on the security of investments

14.17 The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

14.18 When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council’s cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

Specified investments

14.19 The CLG Guidance defines specified investments as those:

- denominated in pound sterling;
- due to be repaid within 12 months of arrangement; and
- not defined as capital expenditure by legislation, and invested with one of:
    - the UK Government;
    - a UK local Council, parish council or community council; or
    - a body or investment scheme of "high credit quality".

14.20 The Council defines "high credit quality" organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds "high credit quality" is defined as those having a credit rating of A- or higher.

Non-specified investments

14.21 Any investment not meeting the definition of a specified investment is classed as non-specified. The Council does not intend to make any investments denominated in foreign currencies. Non-specified investments will therefore be limited to long-term investments, (i.e. those that are due to mature 12 months or longer from the date of arrangement), pooled funds that the Council intends to hold as long-term investments (for more than one year) and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in Table 4 below.

Table 4: Non-specified investment limits

	Cash limit
Total long-term investments	£20m
Total investments without credit ratings or rated below A- (except UK Government and local authorities)	£20m
Total investments (except pooled funds) with institutions domiciled in foreign countries rated below AA+	£0m
Total non-specified investments	£30m*

* Total non-specified investments is a limit in its own right, and is not meant to equal the aggregate of the limits for total long-term investments, and investments without credit ratings or rated below A-.

14.22 Although the long-term investments limit is greater than the expected investment balance as 31 March 2019, as shown in Table 1, this limit has been set to allow for current long-term investments to mature, as well as to allow for flexibility if capital expenditure is experienced to be slower than forecast.

Liquidity management

14.23 The Council has due regard for its future cash flows when determining the maximum period for which funds may prudently be committed. Historic cash flows are analysed in addition to significant future cash movements, such as payroll, grant income and council tax precept. Limits on long-term investments are set by reference to the Council's medium term financial position (summarised in Table 1) and forecast short-term balances.

15 NON-TREASURY INVESTMENTS

15.1 Although not classed as treasury management activities and therefore not covered by the CIPFA Code or the CLG Guidance, the Council may also purchase property for investment purposes and may also make loans and investments for service purposes, for example in shared ownership housing, as loans to local businesses and landlords, or as equity investments and loans to the Council's subsidiaries.

15.2 Such loans and investments will be subject to the Council's normal approval processes for revenue and capital expenditure and need not comply with this treasury management strategy.

15.3 Further information can be found in the Council's Capital Strategy (CAB3014 refers).

15.4 The Council's existing non-treasury investments are listed in Appendix B.

16 TREASURY MANAGEMENT INDICATORS

16.1 The Council measures and manages its exposures to treasury management risks using the following indicators.

Interest rate exposures

16.2 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 amount of net principal borrowed or invested will be:

Table 5: Interest rate exposures

	2018/19	**2019/20**	**2020/21**
Upper limit on fixed interest rate investment exposure	£20m	£20m	£20m
Upper limit on variable interest rate investment exposure	£100m	£100m	£100m
Upper limit on fixed interest rate borrowing exposure	£213m	£245m	£256m
Upper limit on variable interest rate borrowing exposure	£213m	£245m	£256m

16.3 Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. All other instruments are classed as variable rate.

Maturity structure of borrowing

16.4 This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing will be:

Table 6: Maturity structure of borrowing

	Upper	**Lower**
Under 12 months	25%	0%
12 months and within 24 months	25%	0%
24 months and within 5 years	25%	0%
5 years and within 10 years	25%	0%
10 years and within 20 years	50%	0%
20 years and within 30 years	50%	0%
30 years and within 40 years	75%	0%
40 years and above	100%	0%

Principal sums invested for periods longer than 364 days

16.5 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 long-term principal sum invested to final maturities beyond the period end will be:

Table 7: Principal sums invested for periods longer than 364 days

	2018/19	**2019/20**	**2020/21**
Limit on principal invested beyond year end	£20m	£20m	£20m

17 OTHER ITEMS

17.1 There are a number of additional items that the Council is obliged by CIPFA or CLG to include in its Treasury Management Strategy.

Policy on the use of financial derivatives

17.2 Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

17.3 The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

17.4 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

Policy on apportioning interest to the HRA

17.5 The Council has adopted the "two pool approach" whereby each of its long-term loans are split into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/credited to the respective revenue account. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured each month and interest transferred between the General Fund and HRA applying the following rates:

- The PWLB 3 month variable loan rate is applied to a deficit balance
- The risk free Debt Management Office rate is applied to a surplus balance.

Investment training

17.6 The needs of the Council’s treasury management staff for training in investment management are assessed annually as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change.

17.7 Staff regularly attend training courses, seminars and conferences provided by Arlingclose and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA, and other appropriate organisations.

17.8 CIPFA’s Code of Practice requires that the Council ensures that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. All members were invited to a workshop presented by Arlingclose on 29 November 2017, which gave an update of treasury matters. A further Arlingclose workshop has been planned for November 2018.

Investment advisers

17.9 Hampshire County Council has appointed Arlingclose Limited as treasury management advisers for all Councils under the arrangement, and receives specific advice on investment, debt and capital finance issues. The quality of this service is controlled through quarterly review meetings with Arlingclose.

Investment of money borrowed in advance of need

17.10 The Council may, from time to time, borrow in advance of need, where this is expected to provide the best long-term value for money. Since amounts borrowed will be invested until spent, the Council is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Council’s overall management of its treasury risks. The total amount borrowed will not exceed the authorised borrowing limit of £213 million.

18 OTHER OPTIONS CONSIDERED AND REJECTED

18.1 The CLG Guidance and the CIPFA Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Section 151 Officer, having consulted the Portfolio Holder for Finance, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

BACKGROUND DOCUMENTS:-

Previous Committee Reports:-

CAB2898 – Treasury Management Strategy 2017/18 – 08 February 2017

Other Background Documents:-

None

APPENDICES:

Appendix A – Arlingclose Economic & Interest Rate Forecast November 2017

Appendix B – Existing Investment & Debt Portfolio Position at 30 November 2017

Appendix C – Prudential Indicators 2018/19

Appendix D – Annual Minimum Revenue Provision Statement 2018/19

Appendix A – Arlingclose Economic & Interest Rate Forecast November 2017

Underlying assumptions:

- In a 7-2 vote, the MPC increased Bank Rate in line with market expectations to 0.5%. Dovish accompanying rhetoric prompted investors to lower the expected future path for interest rates. The minutes re-emphasised that any prospective increases in Bank Rate would be expected to be at a gradual pace and to a limited extent.

- Further potential movement in Bank Rate is reliant on economic data and the likely outcome of the EU negotiations. Policymakers have downwardly assessed the supply capacity of the UK economy, suggesting inflationary growth is more likely. However, the MPC will be wary of raising rates much further amid low business and household confidence.

- The UK economy faces a challenging outlook as the minority government continues to negotiate the country's exit from the European Union. While recent economic data has improved, it has done so from a low base: UK Q3 2017 GDP growth was 0.4%, after a 0.3% expansion in Q2.

- Household consumption growth, the driver of recent UK GDP growth, has softened following a contraction in real wages, despite both saving rates and consumer credit volumes indicating that some households continue to spend in the absence of wage growth. Policymakers have expressed concern about the continued expansion of consumer credit; any action taken will further dampen household spending.

- Some data has held up better than expected, with unemployment continuing to decline and house prices remaining relatively resilient. However, both of these factors can also be seen in a negative light, displaying the structural lack of investment in the UK economy post financial crisis. Weaker long term growth may prompt deterioration in the UK’s fiscal position.

- The depreciation in sterling may assist the economy to rebalance away from spending. Export volumes will increase, helped by a stronger Eurozone economic expansion.

- Near-term global growth prospects have continued to improve and broaden, and expectations of inflation are subdued. Central banks are moving to reduce the level of monetary stimulus.

- Geo-political risks remains elevated and helps to anchor safe-haven flows into the UK government bond (gilt) market.

Forecast:

- The MPC has increased Bank Rate, largely to meet expectations they themselves created. Future expectations for higher short term interest rates are subdued. On-going decisions remain data dependant and negotiations on exiting the EU cast a shadow over monetary policy decisions.

- Our central case for Bank Rate is 0.5% over the medium term. The risks to the forecast are broadly balanced on both sides.

- The Arlingclose central case is for gilt yields to remain broadly stable across the medium term. Upward movement will be limited, although the UK government's seemingly deteriorating fiscal stance is an upside risk.

	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Average
Official Bank Rate														
Upside risk	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.19**
Arlingclose Central Case	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**
Downside risk	0.00	0.00	0.00	0.00	0.00	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	**-0.15**
3-month LIBID rate														
Upside risk	0.10	0.10	0.10	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.22**
Arlingclose Central Case	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**
Downside risk	-0.10	-0.10	-0.15	-0.15	-0.15	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	**-0.20**
1-yr LIBID rate														
Upside risk	0.15	0.15	0.20	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	**0.27**
Arlingclose Central Case	**0.70**	**0.70**	**0.70**	**0.70**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.77**
Downside risk	-0.15	-0.20	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.15	-0.15	**-0.26**
5-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	**0.32**
Arlingclose Central Case	**0.75**	**0.75**	**0.80**	**0.80**	**0.80**	**0.85**	**0.90**	**0.90**	**0.95**	**0.95**	**1.00**	**1.05**	**1.10**	**0.89**
Downside risk	-0.20	-0.20	-0.25	-0.25	-0.25	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	**-0.33**
10-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	**0.32**
Arlingclose Central Case	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.30**	**1.30**	**1.35**	**1.40**	**1.45**	**1.50**	**1.55**	**1.55**	**1.36**
Downside risk	-0.20	-0.25	-0.25	-0.25	-0.25	-0.30	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	**-0.33**
20-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	**0.32**
Arlingclose Central Case	**1.85**	**1.85**	**1.85**	**1.85**	**1.85**	**1.90**	**1.90**	**1.95**	**1.95**	**2.00**	**2.05**	**2.05**	**2.05**	**1.93**
Downside risk	-0.20	-0.30	-0.25	-0.25	-0.30	-0.35	-0.40	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.38**
50-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.25	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	**0.32**
Arlingclose Central Case	**1.70**	**1.70**	**1.70**	**1.70**	**1.70**	**1.75**	**1.80**	**1.85**	**1.90**	**1.95**	**1.95**	**1.95**	**1.95**	**1.82**
Downside risk	-0.30	-0.30	-0.25	-0.25	-0.30	-0.35	-0.40	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.39**

Appendix B – Existing Investment & Debt Portfolio Position

Table 1: Treasury investment activity in 2017/18

	Asset value on 31/08/17 £m	Asset value on 30/11/17 £m	Average Rate/Yield on 30/11/17 %	Average Life on 30/11/17 Years
Short term investments				
- Banks and Building Societies:				
- Unsecured	12.2	8.9	0.45	0.16
- Secured	5.0	4.0	0.86	0.27
- Money Market Funds	6.5	12.2	0.33	0.00
- Local Authorities	13.0	14.0	0.45	0.30
	36.7	**39.1**	**0.45**	**0.17**
Long term investments				
- Banks and Building Societies:				
- Secured	7.0	7.0	0.62	1.77
- Local Authorities	4.0	4.0	1.00	2.23
	11.0	**11.0**	**0.76**	**1.93**
High yield investments				
- Pooled Property Funds *	5.0	5.0	4.58	n/a
- Pooled Equity Funds *†	2.0	2.0	4.84	n/a
	7.0	**7.0**	**4.65**	**n/a**
TOTAL TREASURY INVESTMENTS	**54.7**	**57.1**	**1.03**	**0.56**
Increase/ (Decrease) in Investments £m		2.4		

* Yield represents the average of each investment class' most recent dividend payments as a percentage of the asset value.

† Following the reporting date, the decision has been taken to redeem the current pooled equity fund investments within the high yield investment portfolio. The Council's units have been redeemed, and the received the cash value of those units.

	£m	%
External borrowing:		
PWLB Fixed Rate	(156.7)	(3.30)
Total Gross External Debt	**(156.7)**	**(3.30)**
Investments	**57.1**	**1.03**
Net (Debt) / Investments	**(99.6)**	**(4.60)**

Non-treasury investments:	Asset value as at 31/03/17 £m	Average Rate/Yield in 2016/17 %
Investment property	46.4	4.2
Total non-treasury investments	**46.4**	**4.2**

Appendix C - Prudential Indicators 2018/19

The Local Government Act 2003 requires the Council to have regard to the Chartered Institute of Public Finance and Accountancy's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Council has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

Estimates of Capital Expenditure

The Council's planned capital expenditure and financing may be summarised as follows. Further detail is provided in the capital programme.

Capital Expenditure and Financing	**2017/18 Revised £m**	**2018/19 Estimate £m**	**2019/20 Estimate £m**	**2020/21 Estimate £m**
General Fund	8.8	**44.3**	35.2	17.4
HRA	23.0	**22.0**	22.4	17.4
Total Expenditure	**31.8**	**66.3**	**57.6**	**34.8**
Capital Receipts	4.9	**10.4**	6.4	6.5
Government Grants	2.8	**6.2**	8.6	6.9
Reserves	7.4	**9.0**	7.0	7.2
Revenue	8.9	**5.6**	6.9	2.2
Borrowing	7.8	**35.1**	28.7	12.0
Total Financing	**31.8**	**66.3**	**57.6**	**34.8**

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	**31.03.18 Revised £m**	**31.03.19 Estimate £m**	**31.03.20 Estimate £m**	**31.03.21 Estimate £m**
General Fund	12.5	**47.1**	75.8	86.1
HRA	165.1	**160.8**	162.6	163.4
Total CFR	**177.6**	**207.9**	**238.4**	**249.5**

The CFR is forecast to rise by £71.9m over the next three years as capital expenditure financed by debt outweighs resources put aside for debt repayment.

Gross Debt and the Capital Financing Requirement

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 in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence.

Debt	**31.03.18 Revised £m**	**31.03.19 Estimate £m**	**31.03.20 Estimate £m**	**31.03.21 Estimate £m**
Borrowing	(156.7)	**(156.7)**	(156.7)	(156.7)
New borrowing	-	**(5.3)**	(38.4)	(50.4)
Finance leases	(0.5)	**(0.2)**	(2.4)	(2.1)
Total Debt	**(157.2)**	**(162.2)**	**(197.5)**	**(209.2)**

Total debt is expected to remain below the CFR during the forecast period.

Operational Boundary for External Debt

The operational boundary is based on the Council's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the Council's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring. Other long-term liabilities comprise finance lease, Private Finance Initiative and other liabilities that are not borrowing but form part of the Council's debt.

Operational Boundary	**2017/18 Revised £m**	**2018/19 Estimate £m**	**2019/20 Estimate £m**	**2020/21 Estimate £m**
Borrowing	180.7	**210.5**	244.3	255.0
Other long-term liabilities	0.5	**0.2**	2.4	2.1
Total Debt	**181.2**	**210.7**	**246.7**	**257.1**

Authorised Limit for External Debt

The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Council can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

Authorised Limit	2017/18 Limit £m	2018/19 Limit £m	2019/20 Limit £m	2020/21 Limit £m
Borrowing	182.7	**212.7**	245.4	256.2
Other long-term liabilities	0.6	**0.3**	3.0	2.6
Total Debt	**183.3**	**213.0**	**248.4**	**258.8**

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	2017/18 Revised %	2018/19 Estimate %	2019/20 Estimate %	2020/21 Estimate %
General Fund	(0.82)	**2.33**	4.42	13.12
HRA	18.07	**32.94**	20.10	19.93

The General Fund Ratio of Financing Costs to Net Revenue Stream is negative in the first year as interest receivable is forecast to exceed interest payable and Minimum Revenue Provision (the statutory provision for repayment of debt; see Appendix D).

Incremental Impact of Capital Investment Decisions

This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax and housing rent levels. The incremental impact is the difference between the total revenue budget requirement of the current approved capital programme and the revenue budget requirement arising from the capital programme proposed.

Incremental Impact of Capital Investment Decisions	2018/19 Estimate £	2019/20 Estimate £	2020/21 Estimate £
General Fund - increase in annual band D Council Tax	**(0.89)**	(16.06)	(29.12)
HRA - increase in average weekly rents	**4.79**	9.04	(6.06)

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 in February 2012. It fully complies with the Codes recommendations.

Appendix D – Annual Minimum Revenue Provision Statement 2018/19

Where the Council finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Council to have regard to the Department for Communities and Local Government's Guidance on Minimum Revenue Provision (the CLG Guidance) most recently issued in 2012.

The broad aim of the CLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

The CLG Guidance requires the Council to approve an Annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP. The following statement incorporates options recommended in the Guidance as well as locally determined prudent methods.

For unsupported capital expenditure incurred after 31st March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant asset equal to the relevant PWLB rate as at 31 March for the year of expenditure, starting in the year after the asset becomes operational. MRP on purchases of freehold land will be charged over 50 years. MRP on expenditure not related to fixed assets but which has been capitalised by regulation or direction will be charged over 20 years.

For assets acquired by finance leases or the Private Finance Initiative, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.

For unsupported capital expenditure loans to third parties in respect to the Partnered Home Purchase scheme (PHP) the Council will make nil MRP, but will instead apply the capital receipts arising from when the homeowner "staircases" (purchases part or all of the Council's share of the asset) or when the asset is sold. This is considered prudent due to the fact that residential property has historically held its value over time.

No MRP will be charged in respect of assets held within the Housing Revenue Account. (England only)

Capital expenditure incurred during 2018/19 will not be subject to a MRP charge until 2019/20.

Based on the Council's latest estimate of its Capital Financing Requirement on 31st March 2017, the budget for MRP has been set as follows:

	31.03.2018 Estimated CFR £m	**2018/19 Estimated MRP £**
Unsupported capital expenditure after 31.03.2008	**12.0**	225,000
Finance leases and Private Finance Initiative	**0.5**	321,000
Total General Fund	**12.5**	**546,000**
Assets in the Housing Revenue Account	165.1	Nil
Total Housing Revenue Account	**165.1**	**Nil**
Total	**177.6**	**546,000**

Appendix E - Warnings - loss of protections as a Professional Client

Professional Clients are entitled to fewer protections under the UK and EU regulatory regimes than is otherwise the case for Retail Clients. This document contains, for information purposes only, a summary of the protections that you will lose if you request and agree to be treated as a Professional Client.

1. Communicating with clients, including financial promotions

As a Professional Client the simplicity and frequency in which the firm communicates with you may be different to the way in which they would communicate with a Retail Client. They will ensure however that our communication remains fair, clear and not misleading.

2. Information about the firm, its services and remuneration

The type of information that the firm provides to Retail Clients about itself, its services and its products and how it is remunerated differs to what the firm provides to Professional Clients. In particular,

(A) The firm is obliged to provide information on these areas to all clients but the granularity, medium and timing of such provision may be less specific for clients that are not Retail Clients; and

(B) there are particular restrictions on the remuneration structure for staff providing services to Retail Clients which may not be applicable in respect of staff providing services to Professional Clients;

(C) the information which the firm provides in relation to costs and charges for its services and/or products may not be as comprehensive for Professional Clients as it would be for Retail Clients, for example, they are required when offering packaged products and services to provide additional information to Retail Clients on the risks and components making up that package; and

(D) when handling orders on behalf of Retail Clients, the firm has an obligation to inform them about any material difficulties in carrying out the orders; this obligation may not apply in respect of Professional Clients.

3. Suitability

In the course of providing advice or in the course of providing discretionary management services, when assessing suitability for Professional Clients, the firm is entitled to assume that in relation to the products, transactions and services for which you have been so classified, that you have the necessary level of experience and knowledge to understand the risks involved in the management of your investments. The firm will assess this information separately for Retail Clients and would be required to provide Retail Clients with a suitability report.

4. Appropriateness

For transactions where the firm does not provide you with investment advice or discretionary management services (such as an execution-only trade), it may be required to assess whether the transaction is appropriate. In respect of a Retail Client, there is a specified test for ascertaining whether the client has the requisite investment knowledge and experience to understand the risks associated with the relevant transaction. However, in respect of a Professional Client, the firm is entitled to assume that they have the necessary level of experience, knowledge and expertise to understand the risks involved in a transaction in products and services for which they are classified as a Professional Client.

5. Dealing

A range of factors may be considered for Professional Clients in order to achieve best execution (price is an important factor but the relative importance of other different factors, such as speed, costs and fees may vary). In contrast, when undertaking transactions for Retail Clients, the total consideration, representing the price of the financial instrument and the costs relating to execution, must be the overriding factor in any execution.

6. Reporting information to clients

For transactions where the firm does not provide discretionary management services (such as an execution-only transactions), the timeframe for our providing confirmation that an order has been carried out is more rigorous for Retail Clients' orders than Professional Clients' orders.

7. Client reporting

Investment firms that hold a retail client account that includes positions in leveraged financial instruments or contingent liability transactions shall inform the Retail Client, where the initial value of each instrument depreciates by 10% and thereafter at multiples of 10%. These reports do not have to be produced for Professional Clients.

8. Financial Ombudsman Service

The services of the Financial Ombudsman Service may not be available to you as a Professional Client.

9. Investor compensation

Eligibility for compensation from the Financial Services Compensation Scheme is not contingent on your categorisation but on how your organisation is constituted. Hence, depending on how you are constituted you may not have access to the Financial Services Compensation Scheme.

10. Exclusion of liability

The FCA rules restrict the firm's ability to exclude or restrict any duty of liability which the firm owes to Retail Clients more strictly than in respect of Professional Clients.

11. Trading obligation

In respect of shares admitted to trading on a regulated market or traded on a trading venue, the firm may, in relation to the investments of Retail Clients, only arrange for such trades to be carried out on a regulated market, a multilateral trading facility, a systematic internaliser or a third-country trading venue. This is a restriction which may not apply in respect of trading carried out for Professional Clients.

12. Transfer of financial collateral arrangements

As a Professional Client, the firm may conclude title transfer financial collateral arrangements with you for the purpose of securing or covering your present or future, actual or contingent or prospective obligations, which would not be possible for Retail Clients.

13. Client money

The requirements under the client money rules in the FCA Handbook (CASS) are more prescriptive and provide more protection in respect of Retail Clients than in respect of Professional Clients.

It should be noted that at all times you will have the right to request a different client categorisation and that you will be responsible for keeping the firm informed of any change that could affect your categorisation as a Professional Client.