

BRIGHTON & HOVE CITY
COUNCIL

ANNUAL INVESTMENT
STRATEGY
2014/15

The Annual Investment Strategy 2014/15 is subject to approval by Policy & Resources on 20 March 2014 and full Council on 27 March 2014

Brighton & Hove City Council
Annual Investment Strategy 2014/15

This Strategy complies with guidance issued by the Secretary of State on investments and sets out the council's policy on investment criteria and counterparties. It should be noted that the minimum criteria set out in this document is only one factor taken into account for the investment of council funds. Other factors, such as Government guarantees and support and information available from the financial press and similar publications will also be taken into account when determining investment decisions. Counterparties that satisfy the minimum criteria are not automatically included on the council's approved investment list.

1 Criteria to be used for creating / managing approved counterparty lists / limits

Each counterparty included on the Council's approved lending list must meet the criteria set out below. Without the prior approval of the Council, no investment will be made in an instrument that falls outside the list below.

1.1 Capital security

Table 1 sets out the minimum capital security requirements for an investment to be made.

| <u>Table 1 – Minimum capital security requirements</u> | |
|--|--|
| Banks/building societies with a credit rating | the institution must have a minimum short term rating of good credit quality |
| Building societies that do not satisfy the minimum rating criteria above | the society must have an asset base in excess of £5 billion |
| Money market funds / CCLA Public Sector Deposit Fund | the rating of the fund meets the minimum requirement of triple A ('AAA' / Aaa) |
| Debt Management Account Deposit Facility | the deposit is made in accordance with the rules and regulations relating to such investment as issued by the Debt Management Office from time to time |

1.2 Maximum permitted investment by sector

Table 2 sets out the maximum permitted investment for each sector.

| <u>Table 2 – Maximum permitted investment by sector</u> | |
|---|---|
| <u>Sector</u> | <u>%age of total investment portfolio at the time the investment made</u> |
| Banking sector | 100% |
| Building society sector | 75% |
| Local authority sector | 100% |
| Money market funds / CCLA Public Sector Deposit Fund | 100% |
| Debt Management Account Deposit Facility | 50% |
| Maximum amount invested for | 25% (excl funds administered by external |

| <u>Table 2 – Maximum permitted investment by sector</u> | |
|---|---|
| <u>Sector</u> | <u>%age of total investment portfolio at the time the investment made</u> |
| more than 1 year | cash manager) |

1.3 Maximum permitted investment by counterparty

1.3.1 General

With the exception of money market funds, CCLA Public Sector Deposit Fund and the Debt Management Account Deposit Facility no one counterparty may have more than 75% of the relevant sector total at the time the investment is made.

1.3.2 Rated counterparties

Table 3 sets out the exposure limits and maximum periods for deposits based on various credit ratings.

| <u>Table 3 – Exposure limits and maximum periods per counterparty (with rating)</u> | | | | | |
|---|--|---------------------------------|---------------------------------|-------------------------------|--------------------------------|
| | <u>A rating of at least (lowest of Fitch (F) / Moody's (M) / Standard & Poor's (SP))</u> | | | | |
| Short-term rating | F = F1+ M = P-1 SP = A-1+ | F = F1+ M = P-1 SP = A-1+ | F = F1+ M = P-1 SP = A-1+ | F = F1 M = P-1 SP = A-1 | F = F2 M = P-2 SP = A-2 |
| Long-term rating | F = AA+ M = Aa1 SP = AA+ | F = AA- M = Aa3 SP = AA- | F = A M = A2 SP = A | F = A M = A2 SP = A | F = BBB M = Baa SP = BBB |
| Exposure Limit | £20m | £20m | £10m | £10m | £5m |
| Maximum period – fixed deposits | 3 years | 2 years | 1 year | 1 year | 6 months |
| Maximum period – negotiable instruments | 5 years | 5 years | 1 year | 1 year | 6 months |

In addition investment in money market funds and open ended investment companies with a rating of 'triple A' (i.e. AAA / Aaa) is permitted up to a value of £10 million per fund.

The exceptions to table 3 are:

- Financial institutions that have received Government support (i.e. part nationalized banks) are deemed to have the highest rating irrespective of the actual rating assigned to them. The limits on the amount advanced and length of investment will be £25 million and 1 year respectively.

Where there is a significant or sudden deterioration in one or more of the other ratings (e.g. financial strength, support) allocated to a counterparty, the Director of Finance will undertake a review and, where necessary, suspend the counterparty from the council's approved lending list.

1.3.3 Non-rated counterparties

Table 4 sets out the exposure limits and maximum periods for deposits for counterparties that are not rated.

| <u>Table 4 – Exposure limits and maximum periods per counterparty / fund (with no rating)</u> | | |
|---|-----------------------|-----------------------|
| <u>Counterparty</u> | <u>Exposure Limit</u> | <u>Maximum period</u> |
| Local authority | £10 million | 5 years |
| Non-rated building society with an asset base in excess of £5bn | £5 million | 6 months |
| Debt Management Account Deposit Facility | Unlimited | 6 months |

1.3.4 Cash manager

For the purposes of investments made by the council's external cash manager, the criteria in Table 5 will apply:

| <u>Table 5 – Exposure limits and maximum periods per counterparty (Cash manager)</u> | | |
|--|---|-----------------------|
| <u>Instrument</u> | <u>Exposure Limit</u> | <u>Maximum period</u> |
| Government stock | 100% of Fund | 10 years |
| Supra-national with minimum long-term rating of 'AA-' / Aa3 / AA- | 100% of Fund | 10 years |
| Regulation collective investment schemes | 100% of Fund | n/a |
| Fixed term investments – minimum short-term rating of 'F1 / P-1 / A-1' | 10% of Fund or £2.5m whichever is the greater | 1 year |
| Fixed term investments – minimum long-term rating of 'AA- / Aa3 / AA-' | 10% of Fund or £2.5m whichever is the greater | 5 years |

In addition to Table 5 the maximum average duration of the fund managed by the cash manager shall not exceed 4 years. All instruments used by the cash manager with a maturity of 3 months or more shall be negotiable.

1.4 Investment classification (regulatory)

The investment guidance issued by the Secretary of State requires the council to identify investments as either 'specified' or 'non-specified'. Table 6 sets out the requirements for each type.

| <u>Table 6 – Investment classification</u> | | |
|--|---------------------|----------------------|
| <u>Requirement</u> | <u>Specified</u> | <u>Non-specified</u> |
| Currency | Must be in Sterling | Any currency |
| Maturity period | Up to 12 months | Over 12 months |

| | | |
|--------------|--|-------|
| Credit worth | Counterparty with high credit rating or UK government or local authority | Other |
|--------------|--|-------|

All investments made by the council are denominated in Sterling and are made only in counterparties as set out in paragraph 1.3 above.

The maximum amount invested in non-specified investments will be 50% of the total value of investments. The use of non-specified investments is limited to:

- (a) investment in non-rated building societies with an asset base in excess of £5bn, or
- (b) investment for longer than 12 months in counterparties that meet the minimum long-term rating detailed in Tables 3 and 5 above.

2 Approved methodology for changing limits and adding / removing counterparties

A counterparty shall be removed from the Council's list where a change in their credit rating results in a failure to meet the criteria set out above.

A new counterparty may only be added to the list with the written prior approval of the Director of Finance and only where the counterparty meets the minimum criteria set out above.

A counterparty's exposure limit will be reviewed (and changed where necessary) following notification of a change in that counterparty's credit rating or a view expressed by the credit rating agency warrants a change.

A counterparty's exposure limit will also be reviewed where information contained in the financial press or other similar publications indicates a possible worsening in credit worth of a counterparty. The review may lead to the suspension of a counterparty where it is considered appropriate to do so by the Director of Finance.

3 Full individual listings of counterparties and counterparty limits

For 2014/15, with the exception of the list of high quality AA rated Non-UK banks within AAA rated countries specified below, investment by the in-house treasury team will be restricted financial institutions incorporated within the UK and regulated by the Financial Services Authority.

The in-house treasury team are able to invest in the following Non-UK banks:

- Toronto Dominion (Canada)
- Nordea (Finland)
- Commonwealth Bank of Australia
- National Australia Bank

A full list of counterparties in which the Council will invest surplus funds, together with limits and maximum investment periods is contained in Schedule 1 to this AIS.

There is no pre-determined list for investments made by the cash manager but all counterparties must meet the minimum criteria as set out in Table 5 above.

4 Details of credit rating agencies' services

Credit ratings will be based on those issued periodically by the Fitch Ratings Group, Moody's and Standard & Poor's.

5 Permitted types of investment instrument

All investments must be denominated in Sterling.

The in-house treasury team may invest in fixed term and variable term cash deposits, money market funds and open ended investment companies. The in-house treasury team may only invest in negotiable instruments (including Certificates of Deposit and Enhanced Cash Funds) where to do so offers additional value in terms of investment return and appropriate and supporting advice has been sought from the council's external treasury advisors on the suitability of such an investment.

The cash manager may invest in government stock, supranational institutions, regulation collective investment funds and fixed term instruments. All investments with a maturity of 3 months or more shall be negotiable.

6 Investment risk

6.1 Assessment of credit risk

Whilst the AIS relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for the in-house treasury team to use, additional operational market information will be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information (for example Credit Default Swaps, negative rating watches/outlooks) will be applied to compare the relative security of differing investment counterparties.

6.2 Investment risk matrix

The benchmark risk factor for 2014/15 is recommended at 0.05%, the same as 2013/14. This benchmark is a simple target (not limit) to measure investment risk and so may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that the in-house treasury team will monitor the current and trend position and amend the operational strategy depending on any changes. Any breach of the benchmarks will be reported with supporting reasons in the mid year or end of year review.

6.3 Investment advisors

The Council appoints treasury advisors through a regular competitive tendering process. One of the services provided by Capita Asset Services is the provision of updated credit ratings and “watches” issued by the three rating agencies. In addition Capita Asset Services are proactive in providing additional market information as set out in paragraph 6.1 above.

6.4 Investment training

The Council’s advisors have a wide ranging programme of training giving council officers access to seminars and printed material. The council’s in-house treasury team is experienced in dealing with investments but where necessary further training and updates will be provided. Appropriate training will be made available to all Members who are involved in the treasury management decision-making process.

6.5 Investment of money borrowed in advance

The Council has the flexibility to borrow funds in advance of need (i.e. to fund future debt maturities). The Director of Finance may do this where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial over the life of the loan or meet budgetary constraints.

Borrowing in advance will be made within the constraints set out in the treasury management strategy. The risks associated with such borrowing activity will be subject to appraisal in advance and subsequent reporting through the mid-year or end of year reviews.

6.6 Investment liquidity

Liquidity is achieved by limiting the maximum period for investment and by investing to dates where cash flow demands are known or forecast.

7 Ethical investment statement

The Council has approved the following ethical investment statement that will apply to all cash investments made by, or on behalf of, the Council

“Brighton & Hove City Council, in making investments through its treasury management function, fully supports the ethos of socially responsible investments. We will actively seek to communicate this support to those institutions we invest in as well as those we are considering investing in by:

- *encouraging those institutions to adopt and publicise policies on socially responsible investments;*
- *requesting those institutions to apply council deposits in a socially responsible manner.”*

Counterparties shall be advised of the above statement each and every time a deposit is placed with them.

8 Glossary

Long-term – period in excess of 12 months

Negotiable instrument – an investment where the council can receive back the amount invested earlier than originally agreed (subject to conditions)

Non-specified investment – see Table 6 above

Short-term – period up to and including 12 months

Specified investment – see Table 6 above

Supra-national – an organisation that encompasses more than one nation, such as the World Bank

Brighton & Hove City Council

Banks and Other Institutions
Annual Investment Strategy 2014/15
In-house Treasury Team

| <u>Counterparty</u> | <u>Specified/ Non- specified¹</u> | <u>Short-term</u> <u>F = Fitch</u> <u>M = Moody's SP =</u> <u>Standard & Poor's</u> | | | <u>Long-term</u> <u>F = Fitch</u> <u>M = Moody's</u> <u>SP = Standard & Poor's</u> | | | <u>Max amou nt</u> | <u>Max period – fixed deposits</u> |
|--|--|--|-----|------|---|------|------|----------------------------|--|
| | | F | M | SP | F | M | SP | | |
| Bank of Scotland / Lloyds TSB Bank | Specified | F1 | P-1 | A-1 | A | A2 | A | £25m | 1 year |
| Barclays Bank plc | Specified | F1 | P-1 | A-1 | A | A2 | A | £10m | 1 year |
| Close Brothers | Specified | F1 | P-2 | | A | A3 | | £5m | 6 months |
| Clydesdale Bank | Specified | F1 | P-2 | A-2 | A | Baa2 | BBB+ | £5m | 6 months |
| Crown Agents Bank Ltd | Specified | F2 | | | BBB+ | | | £5m | 6 months |
| HSBC Bank plc | Specified | F1+ | P-1 | A-1+ | AA- | Aa3 | AA- | £20m | 2 years |
| National Westminster Bank / Royal Bank of Scotland | Specified | F1 | P-2 | A-2 | A | A3 | A- | £25m | 1 year |
| NM Rothschild & Sons | Specified | F2 | | | BBB+ | | | £5m | 6 months |
| Virgin Money plc | Specified | F2 | | A-2 | BBB+ | | BBB+ | £5m | 6 months |
| Santander UK plc | Specified | F1 | P-1 | A-1 | A | A2 | A | £10m | 1 year |
| Schroders plc | Specified | F1 | | A-1 | A+ | | A+ | £10m | 1 year |
| Standard Chartered Bank | Specified | F1+ | P-1 | A-1+ | AA- | A1 | AA- | £20m | 2 years |
| <u>BUILDING SOCIETIES</u> | | | | | | | | | |
| <u>(+)</u> | | | | | | | | | |
| Coventry (3) | Specified | F1 | P-2 | | A | A3 | | £5m | 6 months |
| Leeds (5) | Specified | F2 | P-2 | | A-1 | A3 | | £5m | 6 months |
| Nationwide (1) | Specified | F1 | P-1 | A-1 | A | A2 | A | £10m | 1 year |
| Principality (6) | Specified | F2 | NP | | BBB+ | Ba1 | | £5m | 6 months |
| Skipton (4) | Specified | F3 | NP | | BBB- | Ba1 | | £5m | 6 months |
| Yorkshire (2) | Specified | F2 | P-2 | | BBB+ | Baa2 | | £5m | 6 months |
| <u>NON-UK BANKS</u> | | | | | | | | | |
| Toronto Dominion (Canada) | Specified | F1+ | P-1 | A-1+ | AA- | Aa1 | AA- | £20m | 1 year |
| Nordea bank (Finland) | Specified | F1+ | P-1 | A-1+ | AA- | Aa3 | AA- | £20m | 1 year |
| Commonwealth Bank of Australia | Specified | F1+ | P-1 | A-1+ | AA- | Aa2 | AA- | £20m | 1 year |
| National Australia Bank Ltd | Specified | F1+ | P-1 | A-1+ | AA- | Aa2 | AA- | £20m | 1 year |
| <u>OTHER</u> | | | | | | | | | |
| Other Local Authorities (per Authority) | Specified | | | | | | | £10m | 5 year |
| Debt Management Acc Deposit Facility | Specified | | | | | | | Un- limitd. | 6 months |
| Enhanced Cash Funds (Per fund) | Specified | | | | | | | £10m | Liquid |

Appendix 1

| | | | | | | | | | |
|----------------------------------|-----------|--|--|--|--|--|--|------|--------|
| Money market funds (per fund) | Specified | | | | | | | £10m | Liquid |
|----------------------------------|-----------|--|--|--|--|--|--|------|--------|

(*) Ratings as advised by Capita Asset Services February 2014

(+) UK Building Societies ranking based on Total Asset size – Source: Capita Asset Services February 2014

¹ distinction is a requirement under the investment regulations