EASTLEIGH BOROUGH COUNCIL

Treasury Management Strategy

2025/26

Contents

Background

Treasury Management is the management of the Council's cash flows, borrowing and investments, and the associated risks. The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Council's prudent financial management.

Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2021 Edition* (the CIPFA Code) which requires the Council to approve a Treasury Management Strategy before the start of each financial year. This report fulfils the Council's legal obligation under the *Local Government Act 2003* to have regard to the CIPFA Code.

Investments held for service and commercial purposes are considered in a different report, the Investment Strategy.

Economic Background

The impact on the UK from the government's Autumn Budget, slower than expected interest rate cuts, a short-term boost to but modestly weaker economic growth over the medium term, together with the impact from President-elect Trump's second term in office and uncertainties around US domestic and foreign policy, will be major influences on the Authority's treasury management strategy for 2025/26.

The Bank of England's (BoE) Monetary Policy Committee (MPC) held the Bank Rate at 4.75% at its December 2024 meeting, having reduced it to that level in November and following a previous 25bp cut from the 5.25% peak at the August MPC meeting. At the December meeting, six Committee members voted to maintain Bank Rate at 4.75% while three members preferred to reduce it to 4.50%.

The November quarterly Monetary Policy Report (MPR) expected Gross Domestic Product (GDP) growth to pick up to around 1.75% (four-quarter GDP) in the early period of the BoE's forecast horizon before falling back. The impact from the Budget pushes GDP higher in 2025 than was expected in the previous MPR, before becoming weaker. Current GDP growth was shown to be zero (0.0%) between July and September 2024 and 0.4% between April and June 2024, a further downward revision from the 0.5% rate previously reported by the Office for National Statistics (ONS).

ONS figures reported the annual Consumer Price Index (CPI) inflation rate at 2.5% in December 2024, down from 2.6% in the previous month and in line with expectations. Core CPI also reduced to 3.2% from 3.5% in the previous month. The outlook for CPI inflation in the November MPR showed it rising above the MPC's 2% target from 2024 into 2025 and reaching around 2.75%

by the middle of calendar 2025. This represents a modest near-term increase due to the ongoing impacts from higher interest rates, the Autumn Budget, and a projected margin of economic slack. Over the medium-term, once these pressures ease, inflation is expected to stabilise around the 2% target.

The labour market appears to be easing slowly, but the data still requires treating with some caution. The latest figures reported the unemployment rate rose to 4.3% in the three months to October 2024 and economic inactivity fell to 21.7%. Pay growth for the same period was reported at 5.2% for both regular earnings (excluding bonuses) and for total earnings. Looking ahead, the BoE MPR showed the unemployment rate is expected to increase modestly, rising to around 4.5%, the assumed medium-term equilibrium unemployment rate, by the end of the forecast horizon.

The US Federal Reserve has continued cutting interest rates, bringing down the Fed Funds Rate by 0.25% at its December 2024 monetary policy meeting to a range of 4.25%-4.50%, marking the third consecutive reduction. Further interest rate cuts are expected, but uncertainties around the potential inflationary impact of President Trump's policies may muddy the waters in terms of the pace and magnitude of further rate reductions. Moreover, the US economy continues to expand at a decent pace, rising at an annual rate of 3.1% in the third quarter of 2024, and inflation remains elevated suggesting that monetary policy may need to remain more restrictive in the coming months than had previously been anticipated.

Credit Outlook

Higher interest rates can lead to a deterioration in banks' asset quality through increased loan defaults and volatility in the value of capital investments. Fortunately, the rapid interest rate hikes during this monetary tightening cycle, while putting some strain on households and corporate borrowers, has not caused a rise in defaults, and banks have fared better than expected to date, buoyed by strong capital positions. Low unemployment and robust wage growth have also limited the number of problem loans, all of which are positive in terms of creditworthiness.

Moreover, while a potential easing of US financial regulations under a Trump Presidency may aid US banks' competitiveness compared to institutions in the UK and other regions, it is unlikely there will be any material impact on the underlying creditworthiness of the institutions on the counterparty list maintained by Arlingclose, the authority's treasury adviser.

Overall, the institutions on adviser Arlingclose's counterparty list remain well-capitalised and their counterparty advice on both recommended institutions and maximum duration remain under constant review and will continue to reflect economic conditions and the credit outlook.

Interest Rate Forecast

The Authority's treasury management adviser Arlingclose expects the Bank of England's MPC will continue reducing Bank Rate through 2025, taking it to around 3.75% by the end of the 2025/26 financial year. The effect from the Autumn Budget on economic growth and inflation has reduced previous expectations in terms of the pace of rate cuts as well as pushing up the rate at the end of the loosening cycle.

Arlingclose expects long-term gilt yields to remain broadly at current levels on average (amid continued volatility), but to end the forecast period modestly lower compared to now. Yields will continue remain relatively higher than in the past, due to quantitative tightening and significant bond supply. As ever, there will be short-term volatility due to economic and (geo)political uncertainty and events.

Considering this, for the purpose of setting the budget, the Council has opted to forecast interest rates of short-term borrowing to average 4.5% in the 2025/26 financial year, and to forecast any borrowing form the Public Works Loans Board at 4.9%. More detail can be found in the Budget Report put forward for approval by Cabinet and Council in February 2025.

Local Context

On 31 December 2024 the Council held £562M of borrowing and £31M of treasury investments, shown in table 1 below:

Table 1 – Existing Borrowing and Treasury Investment Position

Borrowing and Investments	Dec-24 Actual Portfolio £M	Dec-24 Average Rate %
External Borrowing:		
Public Works Loan Board	450	2.69
Local Authorities	112	4.62
LOBO loans from banks	0	0
Total External Borrowing	**562**	**3.07**
Other Long-Term Liabilities:		
PFI	0	0
Finance Leases	0	0
Transferred Debt	0	0
Total Gross External Borrowing	**562**	**3.07**
Investments:		
Banks and building societies (unsecured)	9	1.75
Money Market Funds	12.3	4.77
Pooled Funds	10	3.60
Total Investments	**31**	**3.52**

Net Borrowing	530.6	

Forecast changes in these sums are shown in the balance sheet analysis in table 2 below.

Table 2 - Balance Sheet Summary and Forecast

	2023/24 Actual £M	2024/25 Estimate £M	2025/26 Forecast £M	2026/27 Forecast £M	2027/28 Forecast £M
General Fund CFR	602	643	692	805	823
Less: External borrowing	(583)	(623)	(673)	(785)	(804)
Internal (over) borrowing	**19**	**20**	**19**	**20**	**19**
Less: Balance Sheet Resources	(52)	(46)	(41)	(39)	(34)
New borrowing or (treasury investments)	**(33)**	**(26)**	**(22)**	**(19)**	**(15)**

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources 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.

The Council has an increasing CFR due to the capital programme, but minimal investments and therefore borrowing will increase up to £804M over the forecast period.

CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Council's total borrowing should be lower than its highest forecast CFR over the next three years. Table 2 (above) shows that the Council expects to comply with this recommendation.

To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table 2 above, but that cash and investment balances are kept to a minimum level of £16.4M at each year-end to maintain sufficient liquidity but minimise credit risk.

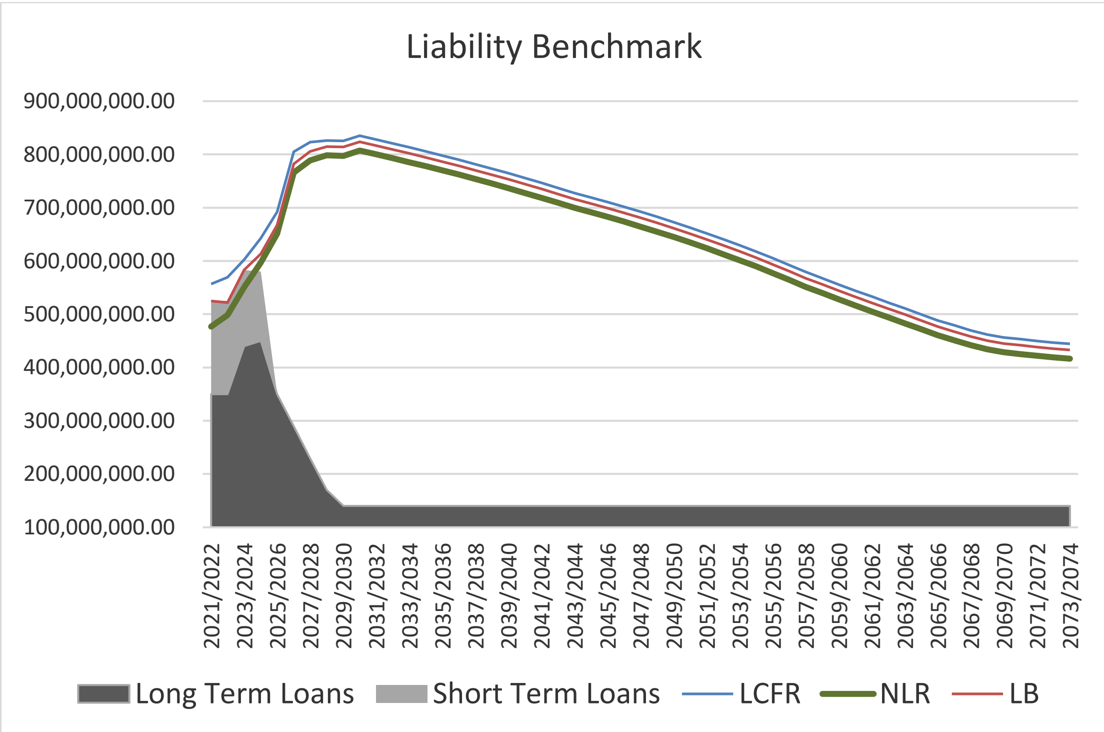
The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level required to manage day-to-day cash flow.

Table 3 – Prudential Indicator – Liability Benchmark

	2023/24 Actual £m	2024/25 Estimate £m	2025/26 Forecast £m	2026/27 Forecast £m	2027/28 Forecast £m
Loans CFR (LCFR)	602	643	692	805	823
Less: Balance Sheet Resources	(52)	(45)	(41)	(39)	(34)
Net Loans Requirement (NLR)	**550**	**597**	**651**	**766**	**789**
Plus: Liquidity Allowance	32.3	16	16	16	16
Liability Benchmark (LB)	**583**	**613**	**667**	**782**	**805**

Following on from the medium-term forecasts in table 3 above, the long-term liability benchmark looks at current approved capital expenditure, the minimum revenue provision profile of this borrowing, alongside known expenditure and reserve movements as determined from the Medium-Term Financial Plan. This is shown in the chart below:

Chart 1 – Liability Benchmark



The chart shows that the Council expects to borrow (Net Loans Requirement (NCR)) below its liability benchmark (LB), representing a need to borrow as short-term loans become due for renewal in the future. This strategy should maintain a lower cost of borrowing through the financing of short-term loans but does show the refinancing risk this presents to the Council. This risk is mitigated by the Council's ongoing access to the PWLB funds, and the liquid short term local to local borrowing market, allowing access to refinance borrowing as it becomes repayable.

The chart also shows that the Council is expecting to be a long-term borrower, although some of the borrowing within this chart is likely to be transferred from the General Fund to the Housing Revenue Account (HRA) once established. This is because a proportion of the Council's forecast borrowing will finance the building of affordable housing, that may remain in Council ownership through the HRA, rather than being sold to Registered Providers (Housing Associations).

Borrowing Strategy

The Council held £562M of loans as at the end of December 2024. The balance sheet forecast in table 2 shows that the Council expects to borrow up to a cumulative total of £673M in 2025/26. The Council may also borrow additional sums to pre-fund future year's requirements, providing this does not exceed the authorised limit for borrowing of £692M in 2025/26. This limit is reviewed quarterly as part of the monitoring of the Community Investment Programme and any change in limits will be recommended for approval.

The Council's main 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.

Given the significant cuts nationally 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 borrowing portfolio. Short-term interest rates are currently higher than in the recent past, but are expected to fall in the coming year and it is therefore likely to be more cost effective over the medium-term to either use internal resources, or to borrow short-term loans instead. The risks of this approach will be managed by keeping the Authority's interest rate exposure within the limit set in the treasury management prudential indicators.

By doing so, the Council can reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of short-term borrowing will continue to 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. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2025/26 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

The Council has previously raised all its long-term borrowing from the PWLB but will consider long-term loans from other sources including banks, pension funds, and local authorities, and will investigate the possibility of issuing bonds and similar instruments, to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield; the Authority intends to continue to avoid this activity and therefore will retain its access to PWLB loans.

Alternatively, the Council may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

In addition, the Council may borrow further short-term loans to cover unplanned cash flow shortages.

Sources of Borrowing

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

- HM Treasury’s PWLB lending facility (formerly the Public Works Loan Board)
- National Wealth Fund Ltd (formerly UK Infrastructure Bank Ltd)
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds (except Hampshire Pension Fund)
- capital market bond investors
- retail investors via a regulated peer-to-peer platform
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

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

- leasing
- hire purchase
- Private Finance Initiative
- sale and leaseback

Other sources of borrowing may include:

- **Municipal Bond Agency:** UK Municipal Bonds Agency plc. was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment if 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 Cabinet.

- **Short-term and variable rate loans**: These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below.

- **Borrowing Rescheduling:** 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. Other lenders may also be prepared to negotiate premature redemption terms. 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. The recent rise in interest rates means that more favourable borrowing rescheduling opportunities may arise than in previous years.

Treasury Investment Strategy

The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During 2024/25, the Council’s short-term investment balance has ranged between £3M and £31M, and similar levels are expected to be maintained in the forthcoming year.

The CIPFA Code requires 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. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, to maintain the spending power of the sum invested. The Council aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.

As demonstrated by the liability benchmark in Chart 1, the Council expects to be a long-term borrower and new treasury investments will therefore be made primarily to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different sectors and increase investment income.

Environmental, social and governance (ESG) considerations are increasingly a factor in global investors’ decision making, but the framework for evaluating investment opportunities is still developing. When investing in banks and funds, the Council will prioritise banks that are signatories to the UN Principles for Responsible Banking and funds operated by managers that are signatories to the UN Principles for Responsible Investment, the Net Zero Asset Managers Alliance and/or the UK Stewardship Code.

Under the IFRS 9 standard, the accounting for certain investments depends on the Council's "business model" for managing them. The Council aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

The Council may invest its surplus funds with any of the counterparty types in table 4 below, subject to the cash limits (per counterparty) and the time limits shown.

Table 4 – Approved Counterparties

Sector	Time Limit	Counterparty Limit	Sector Limit
The UK Government	3 Years	Unlimited	n/a
Local Authorities & other Government entities	364 Days	£10M	Unlimited
Secured Investments *	30 Days	£10M	Unlimited
Banks (Unsecured) *	30 Days	£10M	Unlimited
Building Societies (Unsecured) *	30 Days	£10M	£10M
Registered Providers (Unsecured) *	30 Days	£10M	£10M
Money Market Funds *	n/a	£10M	Unlimited
Strategic Pooled Funds	n/a	£10M	£10M
Real Estate Investment Trusts	n/a	£10M	£10M
Other Investments *	30 Days	£10M	£10M

This table must be read in conjunction with the notes below.

* Treasury investments in the sectors marked with an asterisk will only be made with entities whose lowest published long-term credit rating is no lower than A-. 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 considered.

UK Government: Sterling-denominated investments with or explicitly guaranteed by the UK Government, including the Debt Management Account Deposit Facility, treasury bills and gilts. These are deemed to be zero credit risk due to the government's ability to create additional currency and therefore may be made in unlimited amounts for up to 50 years.

Local authorities and other Government entities: Loans to, and bonds and bills issued or guaranteed by, other national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk.

Secured investments: Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds, secured deposits and reverse repurchase agreements with banks and building societies 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.

Banks and building societies (unsecured): 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.

Registered providers (unsecured): Loans to, and bonds issued or guaranteed by, registered providers of social housing or registered social landlords, formerly known as housing associations. These bodies are regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.

Money market funds: Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. Although no sector limit applies to money market funds, the Council will take care to diversify its liquid investments over a variety of providers to ensure access to cash.

Strategic pooled funds: Bond, equity and property funds, including exchange traded funds, that 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 can be either withdrawn after a notice period or sold on an exchange, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

Real estate investment trusts: Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.

Other investments: This category covers treasury investments not listed above, for example unsecured corporate bonds and unsecured loans to companies and universities. Non-bank companies cannot be bailed-in but can become insolvent placing the Council's investment at risk.

Operational Bank Accounts: The Council may incur operational exposures, for example through current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25billion. These are not classed as investments but are still subject to the risk of a bank bail-in, and balances will therefore be kept below £10M per bank. The Bank of England has stated that in the event of failure, banks with assets greater than £25billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

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.

Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "negative watch") 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.

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, reports in the quality financial press and analysis and advice from the Council's Treasury Management Adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.

The Authority is aware that investment with certain counterparties, while considered secure from a purely financial perspective, may leave it open to criticism, valid or otherwise, that may affect its public reputation, and this risk will therefore be taken into account when making investment decisions.

When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2020, 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, or with other local authorities. This will cause investment returns to fall but will protect the principal sum invested.

In order to limit the risk of loss, a group of Banks under the same ownership will be treated as a single organisation for limit purposes.

Table 5 – Investment limits per group

Investment Limits	Cash limit
Any group of pooled funds under the same management	£10M
Foreign countries	£10M
Negotiable Instruments held in a broker's nominee account	£10M

The Council uses purpose-built cash flow forecasting spreadsheets to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's Medium-Term Financial Plan and cash flow forecast.

Treasury Management Prudential Indicators

The Council measures and manages its exposures to treasury management risk using the following indicators:

Security: The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio.

Table 6 – Security Risk Indicator

Credit Risk Indicator	2025/26 Target
Portfolio average credit	A

Liquidity: The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount it can borrow each quarter without giving prior notice.

Table 7 – Liquidity Risk Indicator

Liquidity Risk Indicator	2025/26 Target
Total sum borrowed in past 3 months without prior notice	£0M

Interest Rate Exposures: This indicator is set to control the Council's exposure to interest rate risk. The upper limit on fixed and variable rate interest rate exposures, expressed as the proportion of net principal.

Table 8 – Interest Rate Risk Indicator

Interest Rate Risk Indicator	2025/26 Limit
Upper limit on variable interest rate exposure	90%
Upper limit on fixed interest rate exposure	100%

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

Table 9 – Refinancing Risk Indicator

Refinancing Risk Indicator	2025/26 Lower Limit	2025/26 Upper Limit
Under 12 months	0%	50%
12 months and within 24 months	0%	60%
24 months and within 5 years	10%	70%
5 years and within 10 years	10%	100%
10 years to 25 years	10%	100%
25 years and above	10%	100%

Long Term Treasury Management Investments: 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.

Table 10 – Price Risk Indicator

Price Risk Indicator	2025/26	2026/27	2027/28	No Fixed Date
Limit on principal invested beyond year end	£15M	£15M	£15M	£15M

Long term investments with no fixed maturity include strategic pooled funds and real estate investment trusts but excludes money market funds and bank accounts with no fixed maturity date as these are considered short term.

Related Matters

The CIPFA Code requires the Council to include the following in its treasury management strategy:

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).

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 considered 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.

Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for derivative exposures.

In line with the CIPFA Code, the Council will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.

The Council has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

Other Options Considered

The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer, having consulted the Treasury Management Review Group, believes that the above Strategy represents an appropriate balance between risk management and cost effectiveness given the current economic conditions. Some alternative strategies, with their financial and risk management implications, are listed below:

Table 11 – Alternative Strategies

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	Borrowing 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	Borrowing interest costs will initially be lower	Increases in borrowing 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 borrowing 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