

## ANNUAL INVESTMENT STRATEGY 2009/10

1. Brent Council has regard to the Department for Communities and Local Government Guidance on Local Government Investments (“Guidance”) and CIPFA’s ‘Treasury Management in the Public Services’.

### 2. Investment Principles

2.1 All investments will be in sterling. The general policy objective is the prudent investment of the council’s treasury balances. The council will aim to achieve the optimum return on its investments commensurate with the proper levels of security and liquidity.

2.3 The Guidance maintains that the borrowing of monies purely to invest or on-lend and make a return is unlawful. The council will not engage in such activity.

### 3. Specified and Non-Specified Investments

3.1 Investment instruments identified for use in the financial year are listed in Appendices N(ii) and N(iii) under the ‘Specified’ and ‘Non-Specified’ investments categories. These are defined as follows:

- a) Specified Investments (as set out in the Guidance) are those that offer high security and liquidity. Such investments will be in sterling, with a maturity of no more than one year, and will be made to bodies with high credit ratings – UK or local government, banks, building societies, money market funds, and supra-national institutions.
- b) Non-specified Investments (as set out in the Guidance) are those that may either entail more risk or are more complex, such as gilts, certificates of deposit or commercial paper. In all cases where time deposits (loans with a fixed maturity date to banks, building societies etc) are not involved, external fund managers will take investment decisions within their Investment Management Agreements.

3.2 Appendices N(ii) and N(iii) also set out:

- (a) the advantages and associated risk of investments under the category of “non-specified” category;
- (b) the upper limit to be invested in each ‘non-specified’ asset category;
- (c) which instruments would best be used by the council’s external fund managers or after consultation with the council’s treasury advisors.

### 4. Liquidity

4.1 Based on its cash flow forecasts, the council anticipates its fund balances in 2009/10 to range between £60m and £130m.

- 4.2 Giving due consideration to the council's level of balances over the next three years, the need for liquidity, its spending commitments and provisioning for contingencies, the council has determined that up to £50m may be held in 'non specified' investments during the year.
- 4.3 Appendices N(ii) and N(iii) set out the maximum periods for which funds may be prudently committed in each asset category.

## **5. Security of Capital: The Use of Credit Ratings**

5.1 Credit quality of counterparties (issuers and issues) and investment schemes will, in the first instance, be determined by reference to credit ratings published by Fitch IBCA, Standard and Poor's, and Moody's (long-term/short-term, individual, support and sovereign). The external manager will use Brent Council's Lending List to establish authorised borrowers.

5.2 Monitoring of credit ratings:

- All credit ratings will be monitored continuously. Brent Council is alerted to changes in ratings through its use of the Sector website and emails.
- If it is anticipated that a downgrading may occur following adverse economic developments; the Head of Exchequer & Investments will have discretion to remove the counterparty from the lending list.
- If a downgrade results in the counterparty/investment scheme no longer meeting the council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- If a counterparty/investment scheme is upgraded so that it fulfils the council's criteria, the Head of Exchequer & Investment will have discretion to include it on the lending list.

5.3 The council has reviewed the basis on which it uses credit ratings. Details of its revised approach are set out in the Treasury Management Strategy in Section 11 of the 2009/10 Budget Report.

## **6. Investments Defined as Capital Expenditure**

6.1 The acquisition of share capital or loan capital in any body corporate is defined as capital expenditure. Brent Council will not use or allow its external fund manager to make, any investment which will be deemed capital expenditure.

## **7. Provisions for Credit-Related Losses**

If any of the Brent Council's investments appeared at risk of loss due to default, the council will make revenue provision of an appropriate amount.

## **8. Investment Strategy to be followed In-House**

- 8.1 Investments will be made with reference to the core balance (£80m), cash flow requirements and the outlook for short and medium-term interest rates (i.e. rates for investments up to 3 years).
- 8.2 The approach that the council will take pending stability returning to the financial markets is also set out in the Treasury Management Strategy in Section 11 of the 2009/10 Budget Report.
- 8.3 Once stability has returned, the council will seek to utilise its business reserve accounts and short-dated deposits (1-3 months) in order to benefit from the compounding of interest at potentially higher rates, while looking for longer-term opportunities when the market becomes too pessimistic about rising rates. Brent Council has identified 2% as an attractive trigger rate to consider 1-year lending and 5% for 2 and 3 year lending. The 'trigger points' will be kept under review and discussed with Butlers so that investments can be made at the appropriate time.

## **9. External Cash Fund Management**

- 9.1 Brent Council's funds are managed on a discretionary basis by Aberdeen Asset Management. The fund manager is contractually required to comply with this strategy.
- 9.2 Brent Council will discuss with its external fund manager on a regular basis, instruments that they consider may be prudently used to meet the council's investment objectives. Brent Council will evaluate the risk-reward characteristics of asset categories to decide whether to permit the manager to use instruments that comply with the Guidance.

**LOCAL GOVERNMENT INVESTMENTS  
SPECIFIED INVESTMENTS**

*All "Specified Investments" listed below must be sterling-denominated.*

<b>Investment</b>	<b>Share/ Loan Capital?</b>	<b>Repayable/ Redeemable Within 12 Months?</b>	<b>Security/ Minimum Credit Rating</b>	<b>Capital Expenditure?</b>	<b>Circumstance of Use</b>	<b>Maximum Period</b>
<b>Debt Management Agency Deposit Facility</b>	No	Yes	Govt-backed	No	In-house	1 year
<b>Term or callable deposits</b> with the UK government or with UK local authorities	No	Yes	High security although local authorities are not credit rated.	No	In-house and by external fund manager	1 year
<b>Term or callable deposits</b> with credit-rated deposit takers (banks and building societies)	No	Yes	Yes-varied	No	In-house and by external fund manager	1 year
<b>Certificates of Deposit</b> issued by credit-rated deposit takers (banks and building societies)	No	Yes	Yes-varied	No	To be used by fund managers	1 year
<b>Gilts</b> : with maturities up to 1 year	No	Yes	Govt-backed	No	External cash fund manager subject to the management agreement	1 year
<b>Money Market Funds</b> (i.e. a highly rated collective investment scheme)	No	Yes	Yes- minimum : AAA	No	In-house and by external fund manager subject to the management agreement	<i>Subject to cash flow and liquidity requirements</i>

Investment	Share/ Loan Capital?	Repayable/ Redeemable Within 12 Months?	Security/ Minimum Credit Rating	Capital Expenditure?	Circumstance of Use	Maximum Period
<b>Forward deals</b> with credit rated banks and building societies	No	Yes	Yes-varied	No	In-house and fund manager	1 year in aggregate
<b>Commercial paper</b> <i>[short-term obligations generally with a maximum life of 9 months issued by banks and other issuers]</i>	No	Yes	Yes-varied	No	External fund managers subject to the management agreement	9 months
<b>Treasury bills</b> <i>[Government debt security with a maturity less than one year]</i>	No	Yes	Govt-backed	No	External fund manager subject to the management agreement	1 year
<b>Bonds issued by a financial institution that is guaranteed by the United Kingdom Government</b>	No	Yes	Govt-backed	No	External cash fund managers subject to management agreements	1 year
<b>Bonds issued by multilateral development banks</b>	No	Yes	AAA	No	External cash fund managers subject to management agreements	1 year

**LOCAL GOVERNMENT INVESTMENTS**  
**NON-SPECIFIED INVESTMENTS**

<b>Investment</b>	<b>(A) Why Use It? (B) Associated Risks?</b>	<b>Share/ Loan Capital?</b>	<b>Repayable/ Redeemable Within 12 Months?</b>	<b>Security/ Minimum Credit Rating</b>	<b>Capital Expenditure?</b>	<b>Circumstance of Use</b>	<b>Max % of Overall Investments</b>	<b>Maximum Maturity of Investment</b>
<b>Term deposits</b> with credit rated deposit takers (banks and building societies) with maturities greater than 1 year	(A) (i) Certainty of rate of return over period invested. (ii) No movement in capital value of deposit despite changes in interest rate environment. (B)(i) Liquid : as a general rule, cannot be traded or repaid prior to maturity. (ii) Return will be lower if interest rates rise after making the investment. (iii) Credit risk : potential for greater deterioration in credit quality over longer period	No	No	Yes-varied	No	In-house, authorised by senior management	100%	3 years
<b>Certificates of Deposit</b> with credit rated deposit takers (banks and building societies) with maturities greater than 1 year	(A)(i) Although in theory tradable, are relatively illiquid. (B)(i) 'Market or interest rate risk' : Yield subject to movement during life of CD which could negatively impact on price of the CD.	No	Yes	Yes-varied	No	To be used by fund manager	80%	3 years
<b>UK government gilts</b> with maturities in excess of 1 year	(A)(i) Excellent credit quality. (ii) Very Liquid. (iii) If held to maturity, known yield (rate of return) per annum ~ aids forward planning. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (v) No currency risk (B)(i) 'Market or interest rate risk' : Yield subject to movement during life of sovereign bond which could negatively impact on price of the bond i.e. potential for capital loss.	No	Yes	Govt backed	No	External cash fund manager only subject to the management agreement	50%	10 years

Investment	(A) Why Use It? (B) Associated Risks?	Share/ Loan Capital?	Repayable/ Redeemable Within 12 Months?	Security/ Minimum Credit Rating	Capital Expenditure?	Circumstance of Use	Max % of Overall Investments	Maximum Maturity of Investment
<b>Sovereign issues, excluding UK government gilts</b> : any maturity	(A)(i) Excellent credit quality. (ii) Liquid. (iii) If held to maturity, known yield (rate of return) per annum ~ aids forward planning. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (v) No currency risk  (B)(i) 'Market or interest rate risk' : Yield subject to movement during life of sovereign bond which could negatively impact on price of the bond i.e. potential for capital loss.	No	Yes	AAA	No	External cash fund manager subject to the management agreement	50%	10 years
<b>Forward deposits</b> with credit rated banks and building societies for periods > 1 year (i.e. negotiated deal period plus period of deposit)	(A)(i) Known rate of return over period the monies are invested ~ aids forward planning.  (B)(i) Credit risk is over the whole period, not just when monies are actually invested. (ii) Cannot renege on making the investment if credit rating falls or interest rates rise in the interim period.	No	No	Yes - varied	No	To be used in-house, authorised by senior management	50%	3 years
<b>Bonds issued by a financial institution that is guaranteed by the United Kingdom Government</b>	(A)(i) Excellent credit quality. (ii) Relatively liquid. (although not as liquid as gilts) (iii) If held to maturity, known yield (rate of return) per annum, which would be higher than that on comparable gilt ~ aids forward planning, enhanced return compared to gilts. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity)  (B)(i) 'Market or interest rate risk' : Yield subject to movement during life of bond which could negatively impact on price of the bond i.e. potential for capital loss.  (ii) Spread versus gilts could widen.	Yes	Yes	AAA / government guaranteed	No	External cash fund manager, subject to the management agreement	80%	3 years

Investment	(A) Why Use It? (B) Associated Risks?	Share/ Loan Capital?	Repayable/ Redeemable Within 12 Months?	Security/ Minimum Credit Rating	Capital Expenditure?	Circumstance of Use	Max % of Overall Investments	Maximum Maturity of Investment
<b>Bonds issued by multilateral development banks</b>	(A)(i) Excellent credit quality. (ii) Relatively liquid. (although not as liquid as gilts) (iii) If held to maturity, known yield (rate of return) per annum, which would be higher than that on comparable gilt ~ aids forward planning, enhanced return compared to gilts. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity). (B)(i) 'Market or interest rate risk' : Yield subject to movement during life of bond which could negatively impact on price of the bond i.e. potential for capital loss. (ii) Spread versus gilts could widen.	Yes	Yes	AAA or government guaranteed	No	External cash fund manager , subject to the management agreement	80%	3 years

\* **The prohibition on the use of derivatives** : This prohibition effectively relies on the judgement of the House of Lords in the case of *Hazell v The Council of the London Borough of Hammersmith and Fulham and Others* in 1991. Their Lordships held that local authorities have no power to enter into interest rate swaps and similar instruments.

Our treasury adviser, Butlers, believes that as this ruling still stands and was not rescinded by the introduction of the Local Government Act 2003, local authorities do not have the power to use derivative instruments.

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