AUDIT COMMITTEE	Agenda Item 64a Brighton & Hove City Council

Subject:		***Annual Investment Strategy 2010/11***		
Date of Meeting:		**30 March 2010 – Audit Committee** 18 March 2010 – Council 11 March 2010 – Cabinet		
Report of:		***Director of Finance & Resources***		
Contact Officer:	Name:	Peter Sargent	Tel:	29-1241
	E-mail:	peter.sargent@brighton-hove.gov.uk		
Key Decision:	Yes	Forward Plan No: CAB12911		
Wards Affected:	All			

FOR GENERAL RELEASE

1. SUMMARY AND POLICY CONTEXT:

1.1 The Local Government Act 2003 introduced a prudential capital finance system whereby levels of borrowing and investments are decided locally by each council.

1.2 Guidance issued under the Act requires a local authority to approve an annual investment strategy which gives priority to security and liquidity and requires the council to set out:

- its policy on determining the credit-worthiness of its investment counterparties and the frequency at which such determinations are monitored;
- its policy on holding investment instruments other than deposits held in financial institutions or government bodies;
- its policy on determining the maximum periods for which funds may be invested;
- its policy on the minimum level of investments to be held at any one time.

1.3 The purpose of this report is to seek Cabinet approval to the Annual Investment Strategy 2010/11 and to recommend the Strategy to full Council for adoption at its meeting on 18 March 2010.

2. RECOMMENDATIONS:

2.1 That Cabinet endorses the Annual Investment Strategy 2010/11 and recommends its approval to Council.

2.2 That Council approves the Annual Investment Strategy 2010/11.

2.3 That **Audit** Committee notes the report.

3. RELEVANT BACKGROUND INFORMATION/CHRONOLOGY OF KEY EVENTS:

Strategy 2010/11

3.1 The Annual Investment Strategy (AIS) for 2010/11 is set out in Appendix 1 to this report and covers investments made by the in-house treasury team and the council's external cash manager. The council uses a cash manager to take advantage of investment opportunities in specialist markets not covered by the in-house team, such as government stock. The AIS gives priority to security and liquidity.

3.2 Security is achieved by:

- selecting only those institutions that meet stringent credit rating criteria or, in the case of non-rated UK building societies, have a substantial asset base; and
- having limits on the amount invested with any one institution.

3.3 For the purpose of determining credit ratings the council uses independent credit rating agencies. Rating criteria is only one factor taken into account in determining investment counterparties. Other factors, such as articles in the financial press, will continue to be monitored and action will be taken where it is felt the risk attached to a particular counterparty has or is likely to worsen. Action will include the suspension of a counterparty in appropriate circumstances.

3.4 Liquidity is achieved by limiting the maximum period for investment.

Revisions to Strategy in 2010/11

3.5 The AIS 2010/11 continues with the policy of assessing the creditworthiness of an institution by applying the lowest rating issued by the three main rating agencies – Fitch, Moody's and Standard & Poor's. In the majority of cases the ratings issued by the three agencies are aligned but this is not always the case.

3.6 Three changes have been incorporated within the AIS 2010/11 that are aimed at enhancing security of investments. These changes will be kept under review and are considered not to be detrimental in terms of investment performance. The changes involve:

- the removal of all non-UK banks and building societies from the approved lending list,
- a reduction in the maximum period of investment for institutions with a short-term rating of "F1" or "P-1" or "A-1" from 12 months to 6 months, and
- an increase in the minimum asset base for building societies that are not rated, from £3bn to £5bn. This is to reflect the current problems being experienced in this sector.

3.7 To compensate for the reduction in investment opportunities resulting from the changes in 3.6 above the maximum percentage of investment in money market funds and local authorities have both been increased from 75% to 100%.

4. REVISED GUIDANCE FROM SECRETARY OF STATE:

4.1 The Government is reviewing the investment guidance which was published in 2004. The review has been primarily undertaken in response to the findings of the Communities and Local Government Select Committee on council investments.

4.2 The CLG Select Committee agreed that the present guidance based framework was sound but recommended some fine-tuning. The revised guidance reiterates:

- investment priorities are security and liquidity, with yield only a consideration where these two objectives have been met,
- investment strategies should be approved by full Council,
- investment strategies should be published,
- the assessment of security should not be solely based on credit ratings but should include other market intelligence,
- investment strategies should comment on the use of external consultants and
- investment strategies should comment on the investment of money borrowed in advance of need.

4.3 The requirements of the first four bullet points in 4.2 above have been included in previous years' investment strategies and are replicated in the 2010/11 AIS. The final two bullet points are new and have been incorporated in the 2010/11 AIS

5. CONSULTATION:

5.1 The council's external treasury advisor has been consulted.

6. FINANCIAL & OTHER IMPLICATIONS:

Financial Implications:

6.1 The financial implications arising from the recommendations in this report are included in the Financing Costs budget.

Finance Officer consulted: Peter Sargent *Date: 17/02/10*

Legal Implications:

6.2 The council must have regard to the guidance issued by the Secretary of State in determining its policies for investment. The Director of Finance & Resources is satisfied that the recommendations in this report are consistent with the guidance issued.

6.3 There are no direct human rights implications arising from this report.

Lawyer consulted: Abraham Ghebre-Ghiorghis *Date 18/02/10*

Equalities Implications:

6.4 None directly arising from this report.

Sustainability Implications:

6.5 The council's ethical investment statement requests that institutions apply council deposits in a socially responsible manner.

Crime & Disorder Implications:

6.6 None directly arising from this report

Risk & Opportunity Management Implications:

6.7 The investment guidance issued under the 2003 Act requires the council to assess credit worthiness by reference to an independent rating agency. The AIS 2010/11 will use the ratings assigned by Fitch, Moody's and Standard & Poor's.

6.8 The ratings provide an opinion on the relative ability of an institution to meet financial commitments, such as interest, preferred dividends, repayment of principal, insurance claims or counterparty obligations. The council uses credit ratings as an indication of the likelihood of receiving its' money back in accordance with the terms of the investment. Other sources of information are used to supplement that provided by the rating agencies.

6.9 The minimum ratings set out in the AIS have the following meaning:

	Generic criteria	Fitch	Moody's	Standard & Poor's
Short-term	Strong capacity for timely payment of financial commitments Where the credit risk is particularly strong, a "+" is added to the assigned rating	F1	P-1	A-1
Long-term	Very strong capacity for payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.	AA-	Aa3	AA-

6.10 Investment risk is managed by selecting only institutions that meet the council's stringent credit rating criteria. Liquidity risk is managed by applying maximum investment periods to institutions.

Corporate / Citywide Implications:

6.11 Investment income is a resource used by the council to fund revenue expenditure. The recommendations in this report will help to minimise capital risk whilst optimising investment returns over both the short and longer term.

7. EVALUATION OF ANY ALTERNATIVE OPTION(S):

7.1 This report sets out the council's annual investment strategy for the year commencing 1 April 2010. The AIS continues with the strong emphasis on risk management and liquidity, two cornerstones to the draft guidance issued by the Secretary of State and the impact these have on investment performance.

8. REASONS FOR REPORT RECOMMENDATIONS:

8.1 Guidance issued under the Local Government Act 2003 requires the council to approve an annual investment strategy. This report fulfils that requirement.

SUPPORTING DOCUMENTATION

Appendix:

1. Annual Investment Strategy 2010/11.

Documents in Members' Rooms:

None.

Background Documents

1. Guidance issued by the secretary of State under Section 15(1)(a) of the Local Government Act 2003 to be effective from 1st April 2010 – currently in draft form and subject to consultation.

2. The Prudential Code for Capital Finance in Local Authorities published by CIPFA – fully revised second edition 2009.