

# GREATER LONDON AUTHORITY

## REQUEST FOR MAYORAL DECISION – MD2095

### Title: Treasury Management Strategy Statement 2017-18

#### Executive Summary:

This report sets out the GLA's Treasury Management Strategy (TMSS) for 2017-18 (including the Treasury Management Policy; Minimum Revenue Provision Policy; Investment Strategy; prudential indicators and Treasury Management Practices: Main Principles). It has been prepared in accordance with the Treasury Management in the Public Services Code of Practice (the Code), issued by the Chartered Institute of Public Finance and Accountancy (CIPFA), and relevant legislation.

Approval is also sought for the expansion of the existing GLA Group treasury management shared service provided by GLA to cover interested London Boroughs.

The previous year's outturn and the 16/17 mid year positions are also noted.

#### Decision:

That the Mayor **approves** the

1. Treasury Management Strategy Statement for 2017-18 (Appendix 1)
2. Treasury Management Policy Statement (Appendix 2)
3. Minimum Revenue Provision Policy Statement (Appendix 3)
4. Prudential Code Indicators and Treasury Management Limits including Group Borrowing Limits (Appendix 4)
5. Group Investment Syndicate (GIS) Investment Strategy (Appendix 5)
6. Treasury Management Practices: Main Principles (Appendix 6)
7. GLA entering arrangements to provide treasury services to the London Boroughs, under the Local Authorities (Goods and Services) Act 1970, subject to conclusion of negotiations to the satisfaction of the Executive Director of Resources and Chief of Staff; and

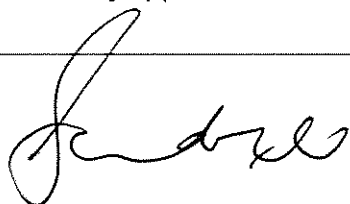
That the Mayor **notes** the 2015-16 Outturn and 2016-17 Mid Year positions (Appendix 7)

#### Mayor of London

I confirm that I do not have any disclosable pecuniary interests in the proposed decision, and take the decision in compliance with the Code of Conduct for elected Members of the Authority.

The above request has my approval.

Signature:



Date:

22/3/12

## **PART I - NON-CONFIDENTIAL FACTS AND ADVICE TO THE MAYOR**

### **Decision required – supporting report**

#### **1. Introduction and background**

The Group Treasury Management function is responsible for the management of the GLA's investments, borrowings and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; the pursuit of optimum performance consistent with those risks and the paramount issue of preserving capital.

Effective treasury management is central to the GLA's financial standing, given the £multi-billion scale of operational cash flows, assets and liabilities.

The ongoing delivery of finance for major capital projects such as Crossrail, the Northern Line Extension (NLE), the Cultural and Education District (CED) and the lending programmes for Housing Zones and the London Housing Bank means that the cost of debt service is the GLA largest single revenue expenditure and its greatest source of financial risk, alongside business rates volatility.

The GLA, through shared services arrangements for professional technical and administrative activities, undertakes the treasury management functions of the London Fire and Emergency Planning Authority (LFEPA), London Legacy Development Corporation (LLDC), London Pensions Fund Authority (LPFA), Old Oak and Park Royal Development Corporation (OPDC) and the Mayor's Office for Policing and Crime (MOPAC) (i.e. all of the GLA Group, excluding TfL). Investments are largely managed collectively through the Group Investment Syndicate (GIS), an arrangement which has proved extremely successful for delivering greater liquidity and performance than would have been achievable by the participating organisations acting individually.

This report proposes that the existing treasury management shared service be expanded to cover interested London Boroughs in order to deliver further benefits and opportunities. It is expected that all new entrants to the shared service will join the Group Investment Syndicate (GIS). London Boroughs may also wish to participate in the GIS without committing to a full shared service.

#### **2. Objectives and expected outcomes**

##### TMSS, GIS Investment Strategy and Prudential Indicators

These documents provide a strategic framework for the achievement of the following prudent objectives

##### **Borrowing**

- Proposed levels of borrowing are sustainable and affordable
- The expected costs are well-matched to the relevant revenue streams to maximise budgetary certainty
- Financing is readily available when required for major capital expenditure
- The most economical sources of borrowing for a given situation are identified and made use of.

##### **Investments**

- Public funds are not lost
- Cash is available when required for essential expenditure
- Returns are maximised, so far as the above constraints allow, to offset the impact of inflation on the spending power of public funds held by the GLA.

### Effective Balance Sheet Management

- A sustainable and prudent balance is struck between the use of cash balances in lieu of external borrowing and any potential risks of refinancing.
- Opportunities for intragroup borrowing/investment transactions are identified in order to reduce risks and/or costs.

The TMSS builds on previous years' strategies. The significant changes relate to investment strategy, introducing a new asset class (residential mortgage backed securities) as a diversification option and rationalising the credit policy to be consistent across deposits and bonds.

### Minimum Revenue Provision ("MRP") Policy

Where capital expenditure is due to be funded by future revenues, this provides a means to match those costs to the period over which the relevant benefits are enjoyed in a way that is equitable to taxpayers, e.g. avoiding the risk of taxpayers at a particular time disproportionately bearing the cost of benefits enjoyed previously or subsequently.

From a cash flow perspective, the MRP policy also ensures that a prudent amount of cash is available for the repayment of borrowings.

### Treasury Management Practices and Treasury Management Policy

These set out the high level objectives for the control and performance management of the function.

### Shared Service Expansion

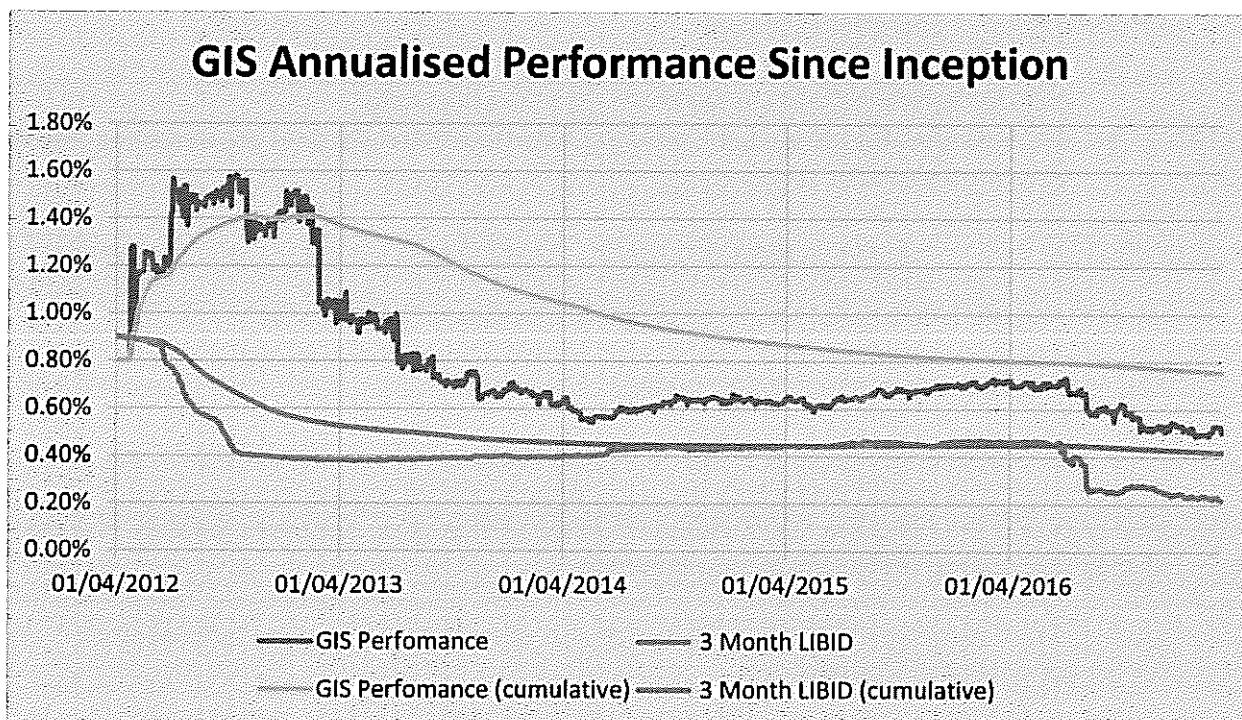
The GLA's experience of the existing shared service arrangements has been extremely positive.

Through the effects of pooling, the GIS has provided the Group Treasury Team with both greater and more stable minimum balances over 3 - 12 month periods than would generally have been the case for each organisation individually. This has provided increased opportunity for longer term investments providing greater yields.

In tandem, the overall increase in balances has provided greater bargaining power in respect of instant access accounts with banks, allowing the GIS to maintain yields for the shortest dated investments. By investing in a mix of overnight and longer dated products, the GIS has maintained a weighted average maturity (WAM) below 3 months, while maintaining excellent overnight liquidity.

The GLA now intends to create a second GIS (GIS 2) for strategic reserves, in order to extend to others the benefits it has experienced with its own longer term balances invested in Residential Mortgage Backed Securities and other longer dated assets. This will operate under identical investment guidelines, except that the WAM limit will be extended to 3 years. In order to reduce administration costs and in keeping with the intention for GIS 2 to be a home for longer-term, core balances, there will be a single agreed dealing day per month for deposits and withdrawals. The simplicity of this arrangement may enable the participation in GIS 2 of additional London Boroughs without the same resource implications for the GLA of a full shared service or the daily transactions of the original GIS.

GIS Performance since inception is shown in the chart below:



In addition to the more stable balances and improved purchasing power, the pooled GIS balances have allowed larger individual deals to be struck. The benefits of this are twofold – one transaction is made rather than a series of individual ones (saving costs) and additionally greater opportunities for diversification arise, since a number of banks in particular operate minimum deal sizes, which would be inappropriate for the participating organisations individually.

By pooling staffing and other administrative resources, the participants have been able to maintain or reduce individual expenditure on treasury management while funding a function able to operate a more sophisticated strategy than would be feasible individually. A key example of this is the expansion of the strategy to cover corporate bonds, whereby Group Treasury have been able to reduce credit risk by further diversification and in many cases obtain superior yields for identical risk.

Because of the factors above, the GIS has significantly outperformed its benchmark, ie the rate at which banks and other large organisations typically lent to each other for 3 months. As at 14 March 2017, the GIS has outperformed by 0.34% on an annualised basis since inception.

The net cash flow managed by the Group Treasury team continues to be dominated by the GLA. The introduction of a range of new organisations with different cash flow profiles has had a positive impact on relevant stability of balances, which together with scale advantages has been positive for the risk and return outcomes for all concerned.

The LPFA's balances have proved a helpful contribution. From the LPFA's perspective, access to the resources of the GLA team and the strategy it is able to deliver has improved returns significantly, with economic benefits in excess of £0.5m.

The overall increase in Group Treasury resources provided by the shared service arrangements have continued to enable the development of a resilient, well-qualified team delivering sector-leading innovations in both investment and borrowing and with the capacity to undertake major projects. As an example, the GLA's issue in May 2015 of the world's first CPI-linked Sterling bond providing

£200m for the Northern line extension, reducing inflation risks and estimated to save the taxpayer some £34m in today's prices.

For the reasons above, the GLA will continue to pursue partnerships with additional public bodies in London in a gradual fashion. In particular, developing the shared service with London Boroughs will provide an opportunity for the GLA to provide practical support, where desired, to the financing of local regeneration and infrastructure projects. The inclusion of LB Haringey has already been approved and is in train. It is proposed that the decisions to include additional London Boroughs be delegated to the Executive Director of Resources in consultation with the Chief of Staff. This delegation includes decisions to admit new participants to the GIS or GIS 2, whether or not a wider shared service is pursued (noting that any such admission is subject to agreement of *all* existing syndicate participants).

### **3. Equality comments**

None directly arising from this report

### **4. Other considerations**

Risk management is integral to the report and effective treasury management underpins the sustainability of the financing of all GLA activities.

The shared service proposal supports the corporate priority of increased budgetary efficiency and provides the opportunity to support the financing local infrastructure, housing and regeneration initiatives through the identification of financing opportunities.

There are no formal consultation requirements; however the GLA Oversight Committee has been apprised of the intention to expand the shared service to London Boroughs via Item 5 of the meeting of 10 March 2015. The committee indicated support for the direction of travel.

### **5. Financial comments**

Financial implications are largely integral to the report.

The expansion of the shared service will involve additional staffing and administrative expenditure within Group Finance; however, these additional costs will be fully recovered from the participating Boroughs.

Additionally, the fixed costs of the treasury function (inter alia, systems, advisory fees and senior management) will be shared across participants in proportion to balances managed. The addition of new participants is likely to result in a reduction in net costs to existing participants including the GLA and/or provide opportunities to mitigate the impact of additional investment in systems and compliance.

### **6. Legal comments**

Part 1 of the Local Government Act 2003 introduced a new statutory regime to regulate the borrowing and capital expenditure of local authorities. Section 23(1)(d) and (e) provides that the Greater London Authority (GLA) and the functional bodies are local authorities for this purpose.

Section 3(1) of the 2003 Act provides that all local authorities are to determine and keep under review how much money they can borrow. Section 3(2) of the Act is more specific in relation to the Mayor and functional bodies by providing that the determination is to be made by the Mayor following consultation with the Assembly, in the case of the GLA, or the relevant functional body. As

a result, borrowing limits could be changed in-year, as well as at the start of financial years. Under section 1 of that Act the GLA and the functional bodies may borrow money for any purpose relevant to their functions under any enactment or for the purposes of the prudent management of their financial affairs; they may also invest for the same purposes under section 12.

Under section 127 of the Greater London Authority Act 1999 the Authority has a duty to make arrangements for the proper administration of its affairs. Responsibility for the administration of those affairs lies with the Executive Director of Resources as the statutory chief finance officer of the Authority under section 127(2)(b) of the Act. The management of the Authority's Treasury function and the development and monitoring of the Treasury strategy fall within this responsibility of the chief financial officer.

Section 401A(2) of the Greater London Authority Act 1999, as amended, permits a shared service arrangement, by providing that any 'relevant London authority' (as defined in the GLA Act 1999) may enter into arrangements for the provision of administrative, professional or technical services by any one or more of them to any one or more of them, whether for consideration or otherwise. This enables the GLA, the Functional Bodies and the LPFA to delegate the professional technical and administrative functions involved in treasury management to the GLA and for them all to jointly participate in the GIS under their common powers to borrow and invest for the prudential management of their financial affairs.

Although London Boroughs are not covered by section 401A, they and the GLA are local authorities for the purposes of the Local Authorities (Goods and Services) Act 1970. As a result the GLA may provide the same professional technical and administrative functions involved in treasury management to boroughs, who also share the same investment and borrowing powers.

## **7. Planned delivery approach and next steps**

The TMSS will be implemented with immediate effect from 1<sup>st</sup> April 2017.

Implementation of the shared service proposals for the London Borough of Haringey is expected before end June 2017.

GIS 2 will be constituted in April 2017.

### **Appendices and supporting papers:**

#### Appendices

- Appendix 1 Treasury Management Strategy Statement for 2017-18
- Appendix 2 Treasury Management Policy Statement
- Appendix 3 Minimum Revenue Provision Policy Statement
- Appendix 4 Prudential Code Indicators and Treasury Management Limits
- Appendix 5 Group Investment Syndicate Investment Strategy
- Appendix 6 Treasury Management Practices: Main Principles
- Appendix 7 2015-16 Outturn and 2016-17 Mid Year positions

#### Supporting Papers

- Mayor's Final Draft Consolidated Budget 2017-18
- Capital Spending Plan 2017-18

**Public access to information**

Information in this form (Part 1) is subject to the Freedom of Information Act 2000 (FOI Act) and will be made available on the GLA website within one working day of approval.

If immediate publication risks compromising the implementation of the decision (for example, to complete a procurement process), it can be deferred until a specific date. Deferral periods should be kept to the shortest length strictly necessary. **Note:** This form (Part 1) will either be published within one working day after approval or on the defer date.

**Part 1 Deferral:**

**Is the publication of Part 1 of this approval to be deferred? NO**

If YES, for what reason:

Until what date: (a date is required if deferring)

**Part 2 Confidentiality:** Only the facts or advice considered to be exempt from disclosure under the FOI Act should be in the separate Part 2 form, together with the legal rationale for non-publication.

**Is there a part 2 form – NO**

**ORIGINATING OFFICER DECLARATION:**

Drafting officer to confirm the following (✓)

**Drafting officer:**

Luke Webster has drafted this report in accordance with GLA procedures and confirms the following have been consulted on the final decision.

✓

**Sponsoring Director:**

Martin Clarke has reviewed the request and is satisfied it is correct and consistent with the Mayor's plans and priorities.

✓

**Mayoral Adviser:**

David Bellamy has been consulted about the proposal and agrees the recommendations.

✓

**Advice:**

The Finance and Legal teams have commented on this proposal.

✓

**Corporate Investment Board**

This decision was agreed by the Corporate Investment Board on 20 March 2017.

**EXECUTIVE DIRECTOR, RESOURCES:**

I confirm that financial and legal implications have been appropriately considered in the preparation of this report.

**Signature**

**Date**

TOM MIDDLETON ON BEHALF OF MARTIN CLARKE 20.03.17

**CHIEF OF STAFF:**

I am satisfied that this is an appropriate request to be submitted to the Mayor

**Signature**

**Date**

D. Bellamy 20/3/2017

## **Appendix 1: Treasury Management Strategy Statement 2017-18**

### **Introduction/Background**

1. The Treasury Management Strategy Statement (TMSS) sets out the Treasury Management activities of GLA (the Authority) for the year 2017-18.
2. This TMSS has been prepared with regard to the following legislation and guidance:
  - The Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes (The Code) and associated Guidance Notes
  - The CIPFA Prudential Code for Capital Finance in Local Authorities and associated Guidance Notes
  - The Local Government Act 2003
  - The Department for Communities and Local Government (DCLG) Guidance on Local Government Investments
  - The DCLG Capital Finance Guidance on Minimum Revenue Provision
3. The Code defines treasury management activities as:

‘The management of the organisation’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.’
4. This TMSS therefore takes into account the impact of the Authority’s Revenue Budget, Medium Term Capital Programme and the Balance Sheet position and covers the following areas:
  - Economic Background
  - Prospects for Interest Rates
  - Forecast Treasury Management Position
  - Borrowing Strategy
  - Policy on Borrowing in Advance of Need
  - Debt Rescheduling
  - Investment Strategy
  - Use of External Service Providers
  - Treasury Training



- Treasury Management Policy Statement (Appendix 2)
  - Minimum Revenue Provision (MRP) Policy Statement (Appendix 3)
  - Prudential Code Indicators and Treasury Management Limits (Appendix 4)
  - Group Investment Syndicate (GIS) Investment Strategy (Appendix 5)
  - Treasury Management Practices: Main Principles (Appendix 6)
5. In covering the above areas, as per its Treasury Management Policy Statement (Appendix 2), the Authority regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Final responsibility for risk management and control resides with the Authority and cannot be delegated to any outside organisation.
6. The Treasury Management risks the Authority is exposed to are:
- Credit and counterparty risk (security of investments)
  - Liquidity risk (inadequate cash resources)
  - Interest and market risk (fluctuations in interest rate levels and thereby in the value of investments)
  - Refinancing risks (impact of debt maturing in future years) and
  - Legal and regulatory and fraud risk (non-compliance with statutory and regulatory requirements, risk of fraud)
7. These risks are further discussed in Appendix 6 (Treasury Management Practices: Main Principles)
8. The Authority formally adopts The TM Code through the following provisions
- i. The Authority will create and maintain as the cornerstones for effective treasury management:
    - a Treasury Management Policy Statement stating the policies, objectives and approach to risk management of its treasury management activities and
    - suitable Treasury Management Practices (TMPs), setting out the manner in which the Authority will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

The content of the proposed policy statement and TMPs follow the recommendations contained in Sections 6 and 7 of the TM Code, subject only to amendment where necessary to reflect the particular circumstances of the Authority. Such amendments do not result in the Authority materially deviating from the Code's key principles.

- ii. The Mayor will receive reports on its treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMPs.

- iii. The Mayor holds responsibility for the implementation and regular monitoring of its treasury management policies and practices and delegates responsibility for the execution and administration of treasury management decisions to the Executive Director of Resources. The Executive Director of Resources will act in accordance with the organisation's policy statement and TMPs and, if this officer is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.
  - iv. The Assembly has delegated to the Budget and Performance Committee the responsibility for ensuring effective scrutiny of the treasury management strategy and policies.
  - v. Should there be a need to revise the Treasury Management Strategy; the Treasury Management Policy Statement; the Minimum Revenue Provision Policy Statement; the Prudential Code Indicators and Treasury Management Limits; the GIS Investment Strategy and the Treasury Management Practices at times other than those stated above, then these updates will be submitted to the Mayor for approval. The Assembly will be fully consulted where there is any change to borrowing limits.
  - vi. Should the Executive Director of Resources wish to depart in any material respect from the main principles of the TM Code, the reason should be disclosed, in advance, in a report to the Mayor.
9. The Executive Director of Resources is required to report an annual Treasury Management Strategy to the Mayor for approval. The Executive Director of Resources is responsible for maintaining the Treasury Management Practices (TMPs) and monitoring and managing the strategy, with day to day management of this function delegated to his/her staff.

## **Economic Background**

10. Market volatility and widespread uncertainty around growth, inflation and interest rate forecasts are dominant factors in the outlook relevant to treasury management.
11. This outlook has several treasury management implications:
- Investment returns are likely to remain low for shorter term investments.
  - Borrowing interest rates have and continue to be volatile, and whilst low by historical standards are expected to continue to exceed short term cash returns. The policy of avoiding new borrowing by utilising cash balances has served well over the last few years. However, this needs to remain under careful review to avoid incurring higher borrowing costs in later times, when the organisation may not be able to avoid new borrowing to finance new capital expenditure and/or to refinance maturing debt.

## **Prospects for Interest Rates**

12. Below is a central view for short term interest rates (Bank Rate) and longer term fixed interest rates, as provided by Capita Asset Services, as at February 2017. The PWLB Rates shown are net of the 0.20% 'certainty rate' discount.

	NOW	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20
BANK RATE	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.75	0.75
3 month LIBID	0.23	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.40	0.50	0.60	0.70	0.80	0.90
6 month LIBID	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.50	0.60	0.70	0.80	0.90	1.00
12 month LIBID	0.63	0.70	0.70	0.70	0.70	0.70	0.80	0.80	0.90	1.00	1.10	1.20	1.30	1.40
5 yr PWLB	1.38	1.60	1.60	1.60	1.60	1.70	1.70	1.70	1.80	1.80	1.90	1.90	2.00	2.00
10 yr PWLB	2.11	2.30	2.30	2.30	2.30	2.30	2.40	2.40	2.40	2.50	2.50	2.60	2.60	2.70
25 yr PWLB	2.78	2.90	2.90	2.90	3.00	3.00	3.00	3.10	3.10	3.20	3.20	3.30	3.30	3.40
50 yr PWLB	2.54	2.70	2.70	2.70	2.80	2.80	2.80	2.90	2.90	3.00	3.00	3.10	3.10	3.20

## Borrowing Strategy

13. The GLA's prudent approach to borrowing is characterised by matching interest rate structures to the behaviour of the relevant revenue streams used for funding interest and repayments and close matching of maturity profiles to expected cashflows available for debt repayment.

### Delegation/Authorisation

14. The arrangements for borrowing, including the selection and the type and structure of debt instruments, are delegated to the Executive Director of Resources, provided no decision contravenes the limits set out in the prevailing TMSS.
15. On the basis of the above, the Executive Director of Resources is
- authorised to approve borrowing by the Authority, for the purposes of financing capital expenditure.
  - authorised to make use of cash balances to fund internal borrowing when it is considered advantageous.
  - authorised to borrow temporarily within the Authorised Limit, where this represents prudent management of the Authority's affairs. As an example, where a cash flow requirement is short-lived, the opportunity cost of withdrawing or otherwise liquidating investments may exceed that of temporary borrowing. In such circumstances, borrowing may be the prudent action.
  - authorised to borrow temporarily above the Authorised Limit where, and only where the amount of the increased limit represents the amount of any delayed payment which is due to the Authority and has not been received on the due date, and such delay has not already been provided for in the Authorised Limit, under the provisions of Section 5 of the Local Government Act 2003.

### Internal Borrowing Approach

16. When using cash balances in lieu of external borrowing, the Authority acknowledges that this may reduce credit risk and short term net financing costs, mindful of the following considerations:
- The Authority must maintain sufficient liquidity to be certain of meeting existing borrowing and other obligations
  - The measures set out in the investment strategy below substantially control credit risk
  - The materiality of such risks should be considered in the light of the long term financial consequences of sub-optimal borrowing decisions

- Agreements with central government specifying particular levels of borrowing
- Over the next 12 months investment rates are expected to remain significantly below borrowing rates. However, short-term avoidance of costs by postponing borrowing will also be weighed against the potential for incurring additional long-term costs by having to enter into new external borrowing in later years, when long-term rates are expected to be higher.

### **Policy on Borrowing in Advance of Need**

17. The Authority will not borrow more than or in advance of need purely to profit from the investment of the surplus borrowed. Any decision to borrow in advance will be considered carefully to ensure value for money can be demonstrated and that the Authority can ensure the security of such funds.
18. In determining whether borrowing will be undertaken in advance of need the Authority will:
  - i. Ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets are considered to be affordable and are within the forward approved Capital financing requirement estimate
  - ii. Evaluate the economic and market factors that might influence the manner and timing of any decision to borrow
  - iii. Consider the merits and demerits of alternative forms of funding , including funding from revenue, leasing and private partnerships and
  - iv. Consider the alternative interest rates bases available, the most appropriate periods to fund and repayment profiles to use.

### **Debt Rescheduling**

19. PWLB pricing policies currently impose a considerable spread between the rate of new loans and the rate used to calculate premiums or discounts on early redemption. This means that there are far fewer opportunities for restructuring than was historically the case, due to prohibitively expensive premia in relation to achievable interest savings. This emphasises the importance of attempting to optimise maturity profiles at the point of entering into borrowings.
20. The GLA continues to consider the use of intergroup transactions, to offer savings on borrowing and/or risk management opportunities.

### **Investment Strategy**

21. The GLA will continue to use the highly successful pooled approach to investment, governed by the principles of Appendix 5, noting the intention to create GIS 2 for longer term balances.
22. The investment strategy has been updated since the previous iteration in two main respects
  - a. A wider range of permissible maturities for collateral accepted by the GLA when undertaking repurchase agreements is adopted. This is in response to market conditions: the previous limits restricted maturity to less than 5 years, however competition for such assets means this needs to be reconsidered.

- b. A responsible investment statement in respect of climate change is included. This is being adopted across the GLA group in line with the Mayor's commitment to Fossil Fuel divestment.
23. Additionally, the Executive Director of Resources may from time to time instruct the Group Treasury team to invest sums independently of the GIS or GIS 2, subject to identical parameters as in Appendix 5, except that there shall be no requirement to maintain a particular weighted average maturity.
  24. Furthermore, subject to appropriate Decisions, the GLA may use treasury balances to invest on its own behalf in local projects or developments, subject to commercial returns appropriate to the relevant risks. The Chief Investment Officer will provide advice accompanying each such decision as to whether such investments materially affect the risk profile of the treasury portfolio as a whole.

### **Use of External Service Providers**

25. The Authority uses Capita Asset Services as its external treasury management advisor under a joint arrangement with other members of the GIS. Other professional advisors may be appointed to assist with particular projects. Whilst recognising the specialist skills and resources such advisors can provide, the Authority recognises that responsibility for treasury management decisions remains wholly with the organisation and will ensure that undue reliance is not placed upon external service providers. With the proposed expansion of the GIS to Boroughs who have different Treasury advisors, this contract will be exposed to competition in due course.
26. External Fund Managers will comply with this and subsequent Treasury Strategies and more detailed Investment Mandates prepared by the Chief Investment Officer. At the time of writing, such arrangements are already in place for the management of Residential Mortgage Backed Securities (24 Asset Management and Prytania).
27. RBS Plc are GLA's bankers and continue to provide a competitive service under an annual rolling contract.
28. The GLA uses King and Shaxson Limited and State Street as custodians of the Authority's tradeable instruments (such as Treasury Bills). The GLA's policy is that any custodian (or, instead, sub-custodian) shall meet the GLA's credit criteria for 12 month investments (prior to Credit Default Swaps Market or other temporary adjustments).
29. In order to facilitate the expansion of services to London Boroughs, the GLA is likely to engage the services of an FCA regulated firm to take investment decisions within the GIS (and GIS 2) in partnership with the internal team.
30. The use of external service or system providers in order to deliver the objectives of this strategy is regarded as routine expenditure and such decisions are delegated to the Executive Director or Resources.

### **Treasury Training**

31. The Code requires that Members with responsibility for treasury management receive adequate training in treasury management. Those charged with governance are also personally responsible for ensuring they have the necessary skills and training.

32. The Group Treasury Team maintains a training programme available to all senior officers and Members participating in the shared service.
33. Group Treasury officers attend national forums and practitioner groups.
34. The training needs of officers and Members are reviewed annually.

## **Appendix 2: Treasury Management Policy Statement**

### **1. Policy Statement**

1.1 This policy statement is in the form recommended by the CIPFA Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes, Section 6.

1. GLA defines its treasury management activities as:

‘The management of the Authority’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks’.

2. GLA regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the GLA, and any financial instruments entered into to manage those risks.
3. GLA acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

### **Appendix 3: Minimum Revenue Provision (MRP) Policy Statement**

*MRP is the amount out of revenues set aside each year to fund capital expenditure previously financed by borrowing or credit arrangements. Regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (as amended) provides that 'A Local Authority shall determine for the current financial year an amount of minimum revenue provision that it considers to be prudent'*

The elements of the GLA's policy are:

1. The natures of funding for the GLA's core Capital Financing Requirement (CFR) and that arising from major infrastructure projects, such as Crossrail and the Northern Line Extension, are distinct and require separate consideration from general corporate capital expenditure.
2. The policy for the MRP relating to the Crossrail CFR is 'equal to the excess of Business Rates Supplement (BRS) receipts over net financing and other revenue costs borne by the General Fund, including the making good of prior year BRS account deficits'.
3. The policy for the MRP relating to the Northern Line Extension (NLE) CFR is 'equal to the excess of NLE Enterprise Zone Revenues and Community Infrastructure Levies/ Section 106 contributions from Boroughs over net financing and other revenue costs borne by the General Fund, including the making good of prior year NLE project account deficits'.
4. This is a prudent provision for Crossrail and NLE, since it will fully fund the liability over a period of time reasonably commensurate with the benefits of the projects. Essentially, it is an amortisation of the costs with a particularly flexible profile. Other bases would cause accounting complications, inequitable to the General Fund.
5. For the MRP element arising from the GLA's non-Crossrail and non-NLE CFR, if any, the amount shall be calculated as 'the principal amount of an annuity payment based on the outstanding non-Crossrail and non-NLE CFR at 31 March of the preceding financial year, amortised over the weighted average remaining period of benefit of the capital expenditure funded by borrowing, using the GLA's aggregate rate of interest for non-Crossrail and non-NLE loans at 31 March of the preceding financial year'. 'Period of Benefit' is defined as 'asset life' (consistent with the GLA's depreciation policies) where an asset exists or, where the expenditure relates to a grant made to another body treated as capital expenditure under statute, the expected period of benefit of the capital programme the grant, to the best of the GLA's knowledge, is used to support.
6. This annuity method will provide prudent provision for capital expenditure over a period commensurate with the benefits of that expenditure in a manner which, ceteris paribus and assuming parity between CFR and external debt, would ensure equal total revenue impact (sum of MRP and interest payable) over the years in question.
7. In the case of the GLA incurring statutory capital expenditure as a result of making a loan to another entity for purposes that, had the GLA undertaken these directly, would be treated as capital expenditure, then the CFR element arising from such loans shall be excluded from MRP calculations to reflect the policy that the capital receipt arising from the repayment of the loan will be applied in full to meet the initial expenditure. The Executive Director of Resources may override this exemption on the grounds of prudence, directing a provision to be made in accordance with the methodology of (5). However, the impact of such direction on the revenue account shall be accounted for as a voluntary revenue provision (VRP). Any impairment to such loans shall be treated in accordance with proper practice.



## **Appendix 4: CIPFA Prudential Code Indicators and Treasury Management Limits**

### **1.0 Background**

- 1.1 The Prudential Code has been developed by the Chartered Institute of Public Finance and Accountancy (CIPFA). The Prudential Code has a central role in capital finance decisions, including borrowing for capital investment. Its key objectives are to provide a framework for local authority capital finance that will ensure for individual local authorities that capital expenditure plans are affordable; all external borrowing and other long-term liabilities are within prudent and sustainable levels and that treasury management decisions are taken in accordance with good professional practice.
- 1.2 The Prudential Code also has the objective of being consistent with and supporting local strategic planning, local asset management planning and proper option appraisal.
- 1.3 Any such framework for the internal control and self management of capital finance must therefore deal with all three of the following elements:
- Capital expenditure plans
  - External debt
  - Treasury Management
- 1.4 To ensure compliance with the Prudential Code in relation to the above elements, the Authority is required to set and monitor a number of Prudential Indicators. The setting of these Prudential Indicators is a circular rather than a linear process. For example, the level of external debt will follow on from the Authority's capital plans, revenue forecasts and treasury management strategy. However, if initial estimates would result in outcomes that would not be affordable or prudent, then plans for capital and/or revenue are reconsidered.
- 1.5 Prudential Indicators and Treasury Management Limits must be approved by the Authority and any subsequent changes to these Indicators and Limits must also be approved by the Authority.
- 1.6 These Prudential Indicators are set out below and reviewed for compliance.

### **2.0 Capital Expenditure**

#### **2.1 Capital Expenditure**

- 2.1.1 Capital expenditure results from the approved capital spending plan and proposed borrowing limits. It is the key driver of Treasury Management activity.
- 2.1.2 All capital expenditure is stated, not just that covered by borrowing.

<b>Capital Expenditure</b>	<b>2017/18 Estimate £m</b>	<b>2018/19 Estimate £m</b>	<b>2019/20 Estimate £m</b>
<b>Total Capital Expenditure</b>	639.2	691.0	1,006.7

## 2.2. Capital Financing Requirement (CFR)

- 2.2.1 The capital financing requirement is an indication of the underlying need to borrow for capital purposes. It is the total historical outstanding capital expenditure which has not yet been paid for from either revenue or capital resource.
- 2.2.2 Any capital expenditure above, which has not immediately been paid for, will increase the CFR.
- 2.2.3 The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual charge which broadly reduces the borrowing in line with each asset's life.
- 2.2.4 The CFR includes any other long term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Authority's borrowing requirement, these types of scheme include a borrowing facility and so the Authority is not required to separately borrow for these schemes.
- 2.2.5 This borrowing is not associated with particular items or types of capital expenditure.

Capital Financing Requirement (CFR)	2017-18 Estimate £m	2018-19 Estimate £m	2019-20 Estimate £m
Total CFR	3,731.0	3,831.0	3,910.5

## 3.0 External Debt Prudential Indicators

### 3.1 Authorised Limit for External Debt

- 3.1.1 The Authorised Limit is the expected maximum borrowing needed with some headroom for unexpected developments such as unusual cash movements.
- 3.1.2 For the purposes of the Prudential Code borrowing is distinguished from other long term liabilities.
- 3.1.3 The Authorised Limit is the statutory limit that is determined, by the Mayor in consultation with the Assembly, under section 3 (1) of the Local Government Act 2003. It is intended to be an absolute ceiling which cannot be exceeded, except as provided under section 5 of the Local Government Act 2003, where payments expected but not yet received can temporarily result in the limit being exceeded, provided the original setting of the limit had not taken into account any delay in receipt of the payment.

#### Authorised Limit for External Debt - Group

GLA	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	4,800.00	4,800.00	4,800.00
Other long term liabilities	0.00	0.00	0.00
Total	4,800.00	4,800.00	4,800.00

MOPAC	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	484.60	552.10	644.50
Other long term liabilities	79.30	76.20	71.00
Total	563.90	628.30	715.50

LFEPA	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	150.00	150.00	150.00
Other long term liabilities	75.00	75.00	75.00
Total	225.00	225.00	225.00

TfL	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	11,924.9	12,425.0	12,925.8
Other long term liabilities	303.2	268.3	198.4
Total	12,228.1	12,693.3	13,124.2

LLDC	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	500.00	555.00	750.00
Other long term liabilities	0.00	0.00	0.00
Total	500.00	555.00	750.00

GLA Group	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	17,829.90	18,452.40	19,239.80
Other long term liabilities	353.00	324.70	274.80
Total	18,182.90	18,777.10	19,514.60

## 3.2 Operational Boundary for External Debt

- 3.2.1 The Operational Boundary is based on the same estimates as the Authorised Limit. However, it reflects an estimate of the most likely prudent but not worst case scenario. It equates to the maximum level of external debt under the capital spending plans approved by the Mayor and excludes the headroom included within the Authorised Limit.
- 3.2.2 The Operational Boundary is set as a warning signal that external debt has reached a level nearing the Authorised limit and must be monitored carefully. It is probably not significant if the Operational Boundary is breached temporarily on occasions due to variations in cash flow. However, a sustained or regular trend above the Operational Boundary would be significant, requiring further investigation and action as appropriate.

Operational Boundary for External Debt – Group

GLA	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	4,300.00	4,300.00	4,300.00
Other long term liabilities	0.00	0.00	0.00
Total	4,300.00	4,300.00	4,300.00

MOPAC	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	359.60	427.10	519.50
Other long term liabilities	79.30	76.20	71.00
Total	438.90	503.30	590.50

LFEPA	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	145.00	145.00	145.00
Other long term liabilities	75.00	75.00	75.00
Total	220.00	220.00	220.00

TfL	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	10,539.8	11,339.9	11,840.7
Other long term liabilities	614.9	538.2	429.4
Total	11,154.7	11,878.1	12,270.1

LLDC	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	490.00	545.00	740.00
Other long term liabilities	0.00	0.00	0.00
Total	490.00	545.00	740.00

GLA Group	2017-18 Proposed £m	2018-19 Proposed £m	2019-20 Proposed £m
Borrowing	16,135.30	16,757.80	17,545.20
Other long term liabilities	353.00	324.70	274.80
Total	16,488.30	17,082.50	17,820.00

### 3.2.4 Gross Debt and the Capital Financing Requirement

This is a key indicator of prudence seeking to identify whether or not a Local Authority's financial strategy is prudent and sustainable by measuring the extent to which a Local Authority is using borrowing to fund revenue expenditure in the short and medium term. Since financing costs have to be repaid from revenue, borrowing to fund revenue expenditure may be affordable in the short term, but not in the medium term. It therefore follows that in the medium term borrowing should only be funding capital expenditure and this indicator seeks to check that this is so, by identifying that debt does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus the estimates of any

additional capital financing requirement for the current and next two financial years. In making this comparison between gross debt and the CFR, CIPFA guidance provides that, if in any of these years, there is a reduction in the CFR, this reduction is ignored in estimating the cumulative increase in the CFR which is used for comparison with the gross external debt.

For the purposes of the Prudential Code, gross debt refers to the sum of borrowing and other long term liabilities.

Gross Debt and the Capital Financing Requirement	2016-17 Projected £m	2017-18 Estimate	2018-19 Estimate	2019-20 Estimate £m
Gross Debt at 31 March	3,678.5	3,731.0	3,831.0	3,910.5.0
Capital Financing Requirement	3,678.5	3,731.0	3,831.0	3,910.5.0

## 4.0 Affordability Prudential Indicators

### 4.1 Ratio of Financing Costs to Net Revenue Stream

- 4.1.1 This indicator compares the total principal and net interest payments on external debt to the overall revenue spending of the authority.

Financing Costs to Net Revenue Stream	2017-18 Estimate %	2018-19 Estimate %	2019-20 Estimate %
Total	49.8	48.3	48.6

### 4.2 Incremental impact of capital investment decisions on the council tax

- 4.2.1 This indicator measures the changes in the council tax as a result of incremental changes in capital investment decisions.

Incremental Impact on Council Tax	2017/18 Estimate £	2018/19 Estimate £	2019/2020 Estimate £
Council Tax Band D	0.0	0.0	0.0

### 4.3 Local Affordability Indicators

The GLA sets two local affordability indicators to support its Standard & Poor's credit rating. This credit rating at October 2016 was AA with a negative outlook.

#### 4.3.1 Deficit after capital accounts (% of total revenues)

The GLA 'AA' credit rating has been awarded with a 'deficit balance after capital accounts ratio' of 1.4% for the year ending March 2017. The GLA will continue to target for a ratio lower than the S&P trigger ratio of 22.5%. For ratios above 22.5%, S&P may consider additional factors to support its decision.

#### 4.3.2 Interest cover ratio

Given the scaling of financing costs involved in the Crossrail borrowing and forthcoming NLE borrowing, the financing arrangements for these two projects included the requirement that the GLA will always hold the cash required to cover six months' worth of interest.

### **5.0 Treasury Management Prudential Indicator**

- 5.1 The Treasury Management Prudential Indicator requires the adoption of the latest version of the CIPFA Code of Practice for Treasury Management in the Public Services.
- 5.2 The Authority has adopted the CIPFA Code of Practice for Treasury Management in the Public Services.

### **6.0 Treasury Management Limits on Activity**

#### 6.1 Net Borrowing Upper Limits to Fixed and Variable Rate Interest Rates Exposure

- 6.1.1 The upper limit on interest rate exposure sets an upper limit to exposure to the effects of changes in interest rates. These limits are presented as a percentage of the net principal sum outstanding on the Local Authority's borrowing. The calculation formula is therefore

Total Fixed (or Variable Rate) Borrowings less Total Fixed (or Variable Rate ) Investments

Divided by

Total Borrowing less Total Investments

Fixed rate calculation:

(Fixed rate borrowing\* less Fixed rate investments\*)

Divided by

Total Borrowing less Total Investments

\*Defined as greater than 1 year to run to maturity

Variable rate calculation:

(Variable rate borrowing\*\* less Variable rate investments\*\*)

Divided by

Total Borrowing less Total Investments

\*\*Defined as less than 1 year to run to maturity or next repayment option.

Upper limit on interest rate exposure on net debt

Upper limit on interest rate exposure on net debt	2017/18 %	2018/19 %	2019/20 %
Fixed rate	150.0	150.0	150.0
Variable rate	10.0	10.0	10.0

## 6.2 Limits for Maturity Structure of Borrowing

- 6.2.1 Local Authorities are exposed to the risk of having to refinance debt at a time in the future when interest rates may be volatile or uncertain. The maturity structure of borrowing indicator is designed to assist Authorities in avoiding large concentrations of debt that has the same maturity structure and would therefore need to be replaced at the same time. The indicator is calculated as the amount of projected borrowing that is maturing in each period expressed as a percentage of total projected borrowing. For each maturity period an upper and lower limit is set.
- 6.2.2 The maturity of borrowing should be determined by reference to the earliest date on which the lender can require payment. Where the lender has the right to increase the interest rate payable without limit, such as in a LOBO loan, the maturity date will be deemed to be the next call date.

Limits for Maturity Structure of Borrowing for 2018/19	Upper Limit %	Lower Limit %
Under 12 months	10	0
12 months and within 24 months	10	0
24 months and within 5 years	10	0
5 years and within 10 years	45	15
10 years and above	100	70

## 6.3 Limits for Principal Sums Invested for Periods Longer than 364 Days

- 6.3.1 This indicator seeks to contain the risk inherent in the maturity structure of an Authority's investment portfolio, since investing too much for too long could
- adversely impact on the Authority's liquidity and in turn its ability to meet its payment obligations and
  - also lead to the loss of some of its principal if it is forced to seek early repayment or redemption of principal sums invested.
- 6.3.2 Under this indicator the Local Authority is therefore required to set an upper limit for each financial year period for the maturing of its long term investments

### Limits for Principal Sums Invested for Periods Longer than 364 days

	Maximum principal sums invested >364 days		
	2017/18 £m	2018/19 £m	2019/20 £m
Principal sums invested >364 days	250.0	250.0	250.0

- 6.3.3 This limit does not apply to externally managed funds or to pooled monies within GIS 1, providing the weighted average maturity of investments does not exceed 3 months.



# **GREATERLONDONAUTHORITY**

**Dated: 1<sup>st</sup> April 2017**

**GREATER LONDON AUTHORITY**

**and**

**LONDON FIRE AND EMERGENCY PLANNING AUTHORITY**

**and**

**LONDON LEGACY DEVELOPMENT CORPORATION**

**and**

**MAYOR'S OFFICE FOR POLICING AND CRIME**

**and**

**LONDON PENSIONS FUND AUTHORITY**

**GIS INVESTMENT STRATEGY 2017-18**

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## GIS Investment Strategy 2017-18

This investment strategy applies to investments pooled under GIS 1 (short term liquidity) and GIS 2 (strategic reserves)

### Limits and Compliance

- 1.0 All limits, unless explicitly stated otherwise, refer to the composition of the daily balance of the GIS; for compliance purposes, all limits will be assessed daily.
- 2.0 The making of any investment which causes a breach of limits is not permitted and constitutes an **active exception**.
- 3.0 **Active exceptions of any size will be reported immediately** upon identification to the CIO, Syndics and their nominated substitutes. Relevant committees or boards will be notified as specified in each Participant's TMSS.
- 4.0 Additionally, breaches of daily limits may occur due to changes in the GIS balance or the credit assessment of existing investments, including the credit status of the country of domicile. Such an occurrence constitutes a **passive exception**. Passive exceptions will be reported immediately to the CIO, the GLA's statutory CFO and his deputy. Subsequent reporting will be threshold based as follows:

Passive Exception Level (lower of)	Temporary: ≤ 3 consecutive days	Persistent: >3 days
<5% or £25m	Logged and reported quarterly to Syndics within 1 month of quarter end	Logged and reported quarterly to Syndics within 1 month of quarter end
5-10% or £50m	Logged and reported quarterly to Syndics within 1 month of quarter end	Reported to Syndics immediately
>10% or £50m	Reported to Syndics immediately	Reported to Syndics immediately

The percentage limits above apply to total daily balance of the GIS or the total number of days in the case of limits expressed as days.

- 5.0 As an additional, prudent measure, forward looking diversification limits for new, internally-managed investments shall be maintained. These limits **apply to the forecast average GIS balance over the life of the investment being considered**; for operational expediency the forecasts shall be produced up to the last day of the following maturity 'buckets' given in days and limits applied accordingly:

O/N	2	8	31	61	91	12	151-	181-	211-	241-	271-	301-	331-	398-
	-	-	-	-	-	-	180	210	240	270	300	330	397	730
	7	30	60	90	120	150								

- 6.0 If an investment is made in breach of these forward-looking limits, it is an active breach of investment strategy and will be reported per 3.0. Where changes in cash flow forecasts or counterparty and/or instrument status result in forward-looking limits being exceeded by existing investment positions, the CIO will be notified, who may then modify investment tactics to reduce the likelihood of a passive exception as defined in 4.0 occurring. Such an occurrence does not constitute an exception of any kind and need not be reported further.
- 7.0 Mitigating actions for all breaches will in the first instance be taken at the discretion of the CIO (or the GLA's statutory CFO, or his deputy). Such decisions must be supported by an analysis of the costs and benefits of attempting to reduce the overexposure in question versus tolerating it. In all cases a file note of the decision will be retained and circulated to the Syndics. A majority of the Syndics may instruct alternative action.

## **Risk Appetite Statement**

- 8.0 Capital preservation is the primary GIS objective at the portfolio level, followed by provision of liquidity to meet Participants' cash flow needs.
- 9.0 In order to deliver best value on public funds, the Participants are prepared to take some investment risk to the extent outlined below, where such risk is rewarded by yields above UK government securities held to maturity.
- 10.0 The risk of loss through default in the entire portfolio (or any subsection delegated to an external manager) should not exceed risk of loss through default equivalent to a 1 year exposure to a typical AA-rated issuer.
- 11.0 No individual instrument/investment should pose a greater risk of loss through default than a 90 day exposure to a typical BBB issuer.
- 12.0 The Participants will tolerate price volatility where there is an expectation of holding an investment to maturity; where the expectation is that sale before maturity is likely or where the investment is in a variable NAV fund, the combined risk of loss through default and crystallised falls in price should not exceed the risk tolerance specified in 10.0.
- 13.0 This strategy sets out risk controls and limits that, in the opinion of the Participants, deliver these objectives.

14.0 Alternative controls and limits, save for the overarching requirements of 15.0-17.0 and 21.0, may be used by external managers appointed in accordance with 18.0, if those limits are judged by the Syndics, on the advice of the CIO or other independent professional advice, to be appropriately effective.

## **Permissible Investments**

15.0 All investments must be Sterling-denominated financial instruments

16.0 Specified Investments (i.e. 'low risk' instruments as defined by Statutory Guidance) shall constitute at least 50% of the portfolio at any time.

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## 17.0 Approved Specified (S) and non-Specified (NS) Investments:

Investment type	Eligibility criteria	≤ 1 year to maturity at time of investment	> 1 year to maturity at time of investment	Maximum total exposure as a proportion of daily balance
<b>Senior Unsecured Debt</b> <ul style="list-style-type: none"> <li>• UK Gilts and T-Bills</li> <li>• Deposits</li> <li>• Call Accounts</li> <li>• Notice Accounts</li> <li>• Certificates of Deposit</li> <li>• Loans</li> <li>• Commercial Paper</li> <li>• All other senior unsecured bonds</li> </ul>	<p>Issuer (and security where separately rated) Investment Grade (IG) defined per 36.0</p> <p>OR</p> <p>UK Government (including the Debt Management Account Deposit Facility, Local Authorities and bodies eligible for PWLB finance)</p> <p>OR</p> <p>Issuer not meeting general criteria but instruments explicitly guaranteed by IG entity or sovereign national government meeting acceptable sovereign ratings per 32.0</p>	S	NS	100%
<b>Constant Net Asset Value Money Market Funds</b>	<p>Fitch AAA<sub>mmf</sub> or above</p> <p>See 36.0 for equivalents from other agencies.</p> <p>Daily liquidity</p>	S	N/A	<p>100%</p> <p><i>Not more than 20% per fund</i></p>
<b>Other Collective Investment Schemes structured as Open Ended Investment Companies (OEICs)</b>	<p>Fitch AAA<sub>i</sub> or equivalent from other agencies per 36.0</p>	NS	<i>Not permitted.</i>	20%



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Investment type	Eligibility criteria	≤ 1 year to maturity at time of investment	> 1 year to maturity at time of investment	Maximum total exposure as a proportion of daily balance
Senior UK Prime or Buy to Let <b>Residential Mortgage Backed Securities (RMBS)</b>	Bond rating Fitch AA <sub>+</sub> or above or equivalent from other agencies per 36.0	NS	NS	20%
<b>Covered bonds</b>	Bond rating Fitch AA <sub>+</sub> or above or equivalent from other agencies per 36.0  AND  Issuer rated Fitch A- or above or equivalent from other agencies per 36.0	NS	NS	20%
<b>Repurchase Agreements (Repo)</b>	Counterparty meets senior unsecured criteria AND proposed collateral (Min 100%) itself meets permitted investment criteria  Or  Collateralisation is >102% with UK Gilts / T-Bills	S – UK gilts or T-Bills AND  Counterparty meets senior unsecured criteria  NS – other	<i>Not permitted.</i>	S – 100%  NS – 20%, and not more than 10% with counterparties not meeting senior unsecured criteria.

18.0 The Syndics may delegate the management of a portion, not exceeding the forecast minimum GIS balance for the next 12 months, of the GIS to external fund managers if this is deemed prudent.

## Liquidity and Maturity Limits

19.0 Portfolio Weighted Average Maturity (WAM) ≤ 91 days (GIS 1) ; ≤ 3 years (GIS 2)

*[Maturity here refers to the final expected maturity or if relevant the first call option of the instrument; in the case of funds the maturity will be the redemption period; in the case of call or notice accounts, the notice period].*

## 20.0 Sub-portfolio (managed by an external manager) WAM $\leq$ 3years

Individual maturity limit, internally managed instruments:  $\leq$  2 years

*[In the exceptional event of the internal team taking possession of repo collateral, e.g. gilts that exceed this limit, the expectation is that these will be sold at the earliest opportunity, subject to market conditions]*

## 21.0 Individual maturity limit, externally managed instruments: $\leq$ 5 years

*[Note – in the case of RMBS these limits apply to the date by which all principal is expected to be received, based on analysis of the underlying mortgage pool and indicated call dates – the legal maturity date, based on the longest dated mortgage in the relevant pool, is not limited given the extremely low probability of the bond failing to be repaid by that time;*

*In the case of covered bonds, these limits apply to the expected maturity date, which may not include the exercise of the extension option]*

## 22.0 Limit for total exposure >12months: $\leq$ 25% of total daily balance.

## 23.0 Forward Dealing limit: aggregate value of outstanding forward deals $\leq$ 20% of daily balance; forward deals must not be struck with an individual counterparty if the limit forecasts defined in 5.0 indicate this is likely to cause an exception. See also 42.0 for credit risk management of forward deals.

*[The GIS defines 'forward' as negotiated more than 4 banking days in advance of delivery. The CIO may make exceptions to this limit where the counterparty is a GIS Participant and the forward period is less than 3 months]*

## 24.0 Internally managed investments should only be made where GIS cash flow forecasts or best estimates suggest the instrument may be held to maturity. Externally managed investments may be purchased with lower certainty subject to the provisions of 12.0

## Counterparty Concentration Limits

**(Apply individually and cumulatively to groups)**



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- 25.0 The total exposure to a group of companies (a parent company and any subsidiaries, i.e. companies of which it owns 20% or more of authorised share capital) shall not exceed the maximum individual exposure limit of the constituents of the group.
- 26.0 Maximum unsecured exposure to company or group: ≤5% (subject to enhancements below)
- 27.0 Enhanced limits apply for UK Government (including the Debt Management Account Deposit Facility, Local Authorities and bodies eligible for PWLB finance) and institutions covered by Capita's Colour Banding Methodology:

Cash Exposure Limits – applied to individual counterparties		
Band	Overnight	> 1 day
UK Sovereign	100%	100%
Yellow	50%	25%
Purple	50%	20%
Orange	25%	15%
Red	25%	10%
Green	10%	5%
No Colour	5%	5%

- 28.0 The Bands above are calculated based on a range of credit ratings data, including published rating Watches and Outlooks. Where the price of 5 year Credit Default Swaps for a given counterparty exceeds barrier levels proposed by Capita with regard to market history, the Band will normally be adjusted downwards. The CIO may postpone such adjustments in consultation with the Syndics, for instance, if it is felt that changes in CDS prices do not reflect an increase in the individual credit risk of a particular counterparty.
- 29.0 Additionally, an enhanced overnight limit of 100% applies to the GIS banker, RBS.
- 30.0 If, in the judgement of the Chief Investment Officer, the structure of a bond associated with a local authority is such that the credit risk is not identical to a bilateral loan with that authority, the rating of the bond itself will be used and the 5% limit will apply.
- 31.0 Maximum aggregate exposure including indirect or collateralised exposures:

Security Type	Cumulative Enhancement
Non-specified Repo	2.5%
Covered Bond	5%
RMBS	7.5%
Specified Repo	10%

*[These enhancements are cumulative so the maximum possible total enhancement is 10% above is the counterparty's senior unsecured limit]*

### Geo-political risk limits [under review]

32.0 Maximum exposures to non-UK institutions apply by country, based on the relevant sovereign ratings outlined in the table below:

Max. Aggregate Exposure (%)	Fitch Sovereign Rating	S&P Sovereign Rating	Moody's Sovereign Rating
25	AAA	AAA	Aaa
15	AA+	AA+	Aa1
5	AA	AA	Aa2

- 33.0 Where more than one rating is available the lowest common denominator will be used, unless in the opinion of the CIO there is an overriding reason to favour or disregard a particular agency's view. The use of this discretion will be reported immediately to the Syndics.
- 34.0 If 5y CDS spreads for the relevant country's central government bonds exceed barrier levels from time to time agreed by the Syndics on the advice of Capita or the CIO, the aggregate exposure limit will normally be reduced to that of the lower rating, or in the case of a AA sovereign, further investment will be suspended. The CIO may postpone such adjustments in consultation with the Syndics.
- 35.0 The Participants recognise that the approach above does not perfectly mitigate geopolitical risks, therefore the CIO is empowered to suspend investment in any particular country should concerns arise. The use of this discretion will be reported immediately to the Syndics.

## Credit Risk Limits

### 36.0 Permitted issuer credit ratings and equivalence mappings

Senior Unsecured Bond and/or Issuer Ratings					
Long term			Short term		
Fitch	Moody's	S&P	Fitch	Moody's	S&P
AAA	Aaa	AAA			
AA+	Aa1	AA+			
AA	Aa2	AA	F1+	P-1	A-1+
AA-	Aa3	AA-			
A+	A1	A+			
A	A2	A	F1	P-1	A-1
A-	A3	A-			
BBB+	Baa1	BBB+			
BBB	Baa2	BBB	F2	P-2	A-2
Structured Finance Ratings					
Fitch		Moody's		S&P	
AAA <sub>sf</sub>		Aaa (sf)		AAA (sf)	
AA+ <sub>sf</sub>		Aa1 (sf)		AA+ (sf)	
Money Market Fund Ratings					
Fitch		Moody's		S&P	
AAA <sub>mmf</sub>		Aaa-mf		AAAm	
Other Permitted Fund Ratings					
Fitch		Moody's		S&P	
AAA <sub>r</sub>		Aaa-bf		AAAf	

# GREATER LONDON AUTHORITY

- 37.0 Where more than one rating is available the lowest common denominator will be used, unless in the opinion of the CIO there is an overriding reason to favour or disregard one particular agency's view. The use of this discretion will be reported immediately to the Syndics.
- 38.0 For internally managed investments Credit Factors will also be calculated individually and Portfolio Credit Factor (PCF) on a book value weighted average basis with reference to the following tables:

Credit Factors based on Issuer Default Rating (Fitch and Fitch Equivalents) Use instrument rating or if not rated, rating of Issuer.									
Days	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB
0/N	0.01	0.01	0.01	0.01	0.02	0.03	0.04	0.07	0.10
2-7	0.02	0.04	0.06	0.10	0.15	0.20	0.30	0.50	0.80
8-30	0.10	0.15	0.25	0.40	0.60	0.75	1.30	2.10	3.50
31-60	0.20	0.30	0.50	0.80	1.20	1.50	2.60	4.20	7.00
61-90	0.25	0.50	0.75	1.25	1.50	2.50	5.00	7.50	10.00
91-120	0.35	0.65	1.00	1.50	2.30	3.30	6.60	10.00	13.50
121-150	0.40	0.80	1.25	2.10	2.90	4.20	8.30	12.50	16.50
151-180	0.50	1.00	1.50	2.50	3.50	5.00	10.00	15.00	20.00
181-210	0.60	1.20	1.75	3.00	4.00	5.80	11.70	17.50	23.50
211-240	0.70	1.30	2.00	3.30	4.70	6.60	13.30	20.00	27.00
241-270	0.75	1.50	2.25	3.75	5.25	7.50	15.00	22.50	30.00
271-300	0.80	1.70	2.50	4.20	5.80	8.30	16.70	25.00	33.50
301-330	0.90	1.85	2.75	4.60	6.50	9.20	18.50	27.50	37.00
331-397	1.00	2.00	3.00	5.00	7.00	10.00	20.00	30.00	40.00
398-730	2.70	5.30	8.00	13.00	19.00	27.00	43.00	69.00	106.00



# GREATER LONDON AUTHORITY

Other treatments	
UK Government (including the Debt Management Account Deposit Facility, Local Authorities and bodies eligible for PWLB finance)	Treat as AAA above  Except:  If, in the judgement of the Chief Investment Officer, the structure of a bond associated with a local authority is such that the credit risk is not identical to a bilateral loan with that authority, the rating of the bond itself will be used
Instruments explicitly guaranteed by IG entity or sovereign national government meeting acceptable sovereign ratings per 32.0	Use Credit Factors appropriate to guarantor strictly for the period of the guarantee, reverting to rating of issuer thereafter
Repo	Use Credit Factors appropriate to repo counterparty, not collateral;  Unrated or sub-BBB counterparty with >102% Gilt/T-bill collateralisation – treat as BBB
Approved fund, e.g. AAA <sub>mmf</sub>	Use Credit Factor of 1.5
Covered Bonds or RMBS	Use Credit Factor of 5

39.0 Where a counterparty's (or its country of domicile's) 5 year CDS spreads exceed barrier levels from time to time agreed by the Syndics on the advice of Capita or the CIO, the Credit Factor used for the PCF calculation will be from the factor set of one or more notches below the issuer or security rating (e.g. If a AA+ counterparty's CDS spread exceeds the first barrier level, AA factors will be used to the PCF).

40.0 The following limits apply at all times:

- Maximum Credit Factor of any single security: 10.00
- Maximum PCF: 5.00

41.0 The PCF will be calculated and recorded daily.

42.0 The total contractual exposure of any transaction with counterparty, i.e. in the case of a forward deal, the forward period PLUS the eventual length of the deal should be considered at the time of the transaction and compared to table 38.0 – the Credit Factor for the total exposure period at the counterparty's credit rating at the time of the deal must not exceed 10.

## **Deposit Facility of Last Resort**

- 43.0 In the circumstance of being unable to place funds with counterparties within approved limits, the Investment Manager will attempt to place the surplus funds with the Debt Management Account Deposit Facility (DMADF). This facility may, of course, also be used in other circumstances if it offers rates above equivalent market levels, though in past experience this is unlikely.
- 44.0 In the instance of technical failures or unexpected monies being received after the cut-off time for sending payments, the GLA, as the GIS Investment Manager, will have no choice but to leave the funds with the GLA's bankers, RBS. In such circumstances, the funds will be moved to the GLA's call account at RBS.

## **Custody Arrangements**

- 45.0 Internally or externally managed securities may be held by a Custodian; in such circumstances:
- a. The Custodian or any Sub-Custodian employed by the Custodian (whichever actually holds the GIS securities) must be Fitch A- rated or equivalent
  - b. Any cash held by the Custodian or any Sub-Custodian pending transactions must be properly identified as an unsecured deposit and consolidated into the PCF calculation
  - c. The Custodian or any Sub-Custodian shall not be entitled to invest such cash in any money market fund or other product without the permission of the GIS. Any such investment must meet the criteria of 17.0.
- 46.0 The above applies to any Custodian or Sub Custodian holding collateral on behalf of the GIS in respect of a Repo transaction. Note – 'Held in Custody' Repos where collateral is held at the borrower's custodian in the borrower's title are NOT permitted.

## **CIO Discretions**

- 47.0 The CIO may restrict the use of any counterparty for any reason related to the management of risk, including reputational risk to any Participant. Such restrictions may be overturned by any majority of Syndics.
- 48.0 When postponing CDS-driven adjustments to exposure limits, the Group Treasury team will notify the Syndics of the CIO's decision immediately. Syndics will have until 12pm to register concerns otherwise the decision will be implemented for that day. Any majority of Syndics may reverse the decision subsequently.
- 49.0 All above mentioned CIO discretions may also be exercised by the GLA's statutory CFO and his deputy.

## Responsible Investment

50.0 All investment will be made in accordance with the following policy with respect to fossil fuel companies:

### GLA Group Responsible Investment Statement on Climate Change

The Greater London Authority is committed to a number of principles which guide their investment decisions. The Greater London Authority will consider non-financial factors when investing, such as alignment of the activities of investment counterparties with Mayoral policy on environmental and social impact, providing no compromise of fiduciary duty arises from such considerations.

Regarding climate change in particular, the Authority will not actively invest in companies or projects ("fossil fuel companies" and "fossil fuel projects") that derive more than 10% of revenues from the extraction of fossil fuels, ignore the impact and risks associated with the use of fossil fuels, and are unable to demonstrate a commitment to achieving environmental benefits, in particular through a plan to limit climate change in line with the Paris Agreement:

[http://unfccc.int/paris\\_agreement/items/9485.php](http://unfccc.int/paris_agreement/items/9485.php)

The Authority notes a distinction between Natural Gas, which will continue to play a valuable role out to 2030, both for heating and for electricity generation, and other fossil fuels; nevertheless the Authority would expect a demonstrable commitment to achieving environmental benefits from companies involved in gas extraction.

In order to assess the level of commitment to achieving environmental benefits, the Authority will make use of the Transition Pathway Initiative, as adopted by a range of leading institutional investors:

<http://www.lse.ac.uk/GranthamInstitute/tpi/about/>

Where such investments are already in place, and opportunities for engagement and reform of the company or project do not exist, the Authority will make all reasonable efforts to divest provided that this will result in no material financial detriment (either through cost or increased investment risk).

The Authority views divestment and avoidance of any long term financial exposure to such companies or projects as entirely consistent with its fiduciary duty to protect and obtain best value from public funds. This is also consistent with the Mayor of London's climate change goals and commitment to ensuring that optimum low carbon investment decisions are taken, to help to maximise social and economic benefits.

To explain these statements concisely the Authority makes the following definitions, with examples of application:

**"invest"** – in this context, investment means the acquiring ownership of all or part of a fossil fuel company or otherwise providing financial support to such a company or any project which ignores the environmental impact and risks associated with Fossil Fuels;

**"actively"** – means making a choice to invest based on a direct assessment of that company or project or to knowingly create a long term economic interest in such companies or projects.

**"environmental benefits"** – means reducing net carbon emissions over time.

**“opportunities for engagement”** – means the ability to meaningfully influence the strategy or development of the company or project. This might be through the exercise of voting rights, either individually or alongside like-minded investors or other routes;

**“ignoring the impact and risks associated with fossil fuels”** – means continuing or developing new business activities contributing to climate change through fossil fuel emissions or environmental damage resulting from relevant fuel extraction without regard to development of new and sustainable alternatives or other transition planning towards a lower environmental impact.

**“long term financial exposure”** – means exposure for more than 12 months, either through actual investment or commitments to invest (contingent or otherwise) where the length of the commitment plus the expected duration of the investment exceeds this period.

## **Examples of application:**

- Making a loan to a fossil fuel company in order fund expansion of conventional extraction activities would meet the definition of investment for these purposes; making a loan to a fossil fuel company to develop an alternative technology would not.
- Purchasing a fossil fuel company bond, from another bond holder would not meet the definition as it does not lead to ownership or engagement, nor provide new financial assistance to the company. Participating in the purchase of newly issued long term bonds may or may not classify as investment depending on the proposed use of proceeds.
- Commercial Paper or other debt instruments with less than a year to maturity would not constitute investment in this context as there is no associated ownership or engagement, nor do the longer term risks associated with exposure to unsustainable industries (which this strategy seeks to mitigate) apply over the life of such instruments.
- Directly purchasing equity in a fossil fuel company would constitute an active investment.
- Buying units in an exchange-traded tracker fund, where the index is known to contain fossil fuel companies may or may not constitute an active investment. It would be active if the intent was for the allocation to be a permanent part of the investment portfolio *and* the composition of the index was weighted more than 10% towards fossil fuel companies; it would not if the purchase was made to maintain broad market exposure, for instance during a transition between active portfolios. In any circumstance, the Authority seeks to influence the composition of the market (reflected in passive investments) through its own active decisions and those of likeminded partners.
- Circumstances involving conglomerates with a mixture of subsidiaries, some of which may meet the fossil fuels company definition (whereas others may, for example, be focused on renewable energy), would be considered on a case-by-case basis, with investment being possible if the overall corporate strategy appears to be environmentally sustainable and offset the financial risks this statement seeks to mitigate.



## Explanatory Notes

### Background to the GIS Investment Strategy

- i. The GIS is a vehicle for investing pooled short term cash balances belonging to 'participants', currently the Greater London Authority (GLA), the London Fire and Emergency Planning Authority (LFEPA), the London Legacy Development Corporation (LLDC), the London Pensions Fund Authority (LPFA) and the Mayor's Office for Policing and Crime (MOPAC). The GLA acts as the Investment Manager under the supervision of the Syndics (the participants' respective chief financial officers).
- ii. By pooling resources, the participants can achieve economies of scale through larger individual transactions; can exploit the greater stability of pooled cash flows to obtain better returns and can achieve greater levels of diversification.
- iii. A risk sharing agreement ensures risk and reward relating to each investment within the jointly controlled portfolio are shared in direct proportion to each participant's daily investment.
- iv. The Investment manager (the GLA) operates the GIS cash balances in accordance with the GIS Investment Strategy

### 4.0

- i. Reporting thresholds are capped at £25m and £50m, these limits are conservative based on the expected scale of the GIS – based on the GIS composition as at 30 June the absolute exposure reporting thresholds for each participant would be:

£m	25	50
GLA	20.4	40.8
LFEPA	0.2	0.5
MOPAC	0.2	0.3
LPFA	2.8	5.7
LLDC	0.2	0.4

### 17.0

- i. The concept of "Specified" and "Non-Specified" Investments is defined in the DCLG Guidance on Local Government Investments (revised 2010).

#### Specified Investments

- ii. An investment is a Specified investment if all of the following apply:
  - a) The investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling;
  - b) The investment is not a long-term investment (i.e. due or required to be repaid within 12 months);

- c) The making of the investment is not defined as capital expenditure by virtue of regulation 25(1)(d) of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (SI 3146 as amended) (i.e. the investment is not share capital in a body corporate)
- d) The investment is made with a body or in an investment scheme of high credit quality (defined by the minimum credit ratings outlined in table 17.0) or with one of the following public-sector bodies:
  - The United Kingdom Government
  - A local authority in England or Wales (as defined in section 23 of the 2003 Local Government Act) or a similar body in Scotland or Northern Ireland
  - A parish council or community

## Non Specified Investments

- iii. Non-Specified Investments are defined as investments assessed by the GIS Participants to be appropriate and prudent, but not meeting the one or more of the Specified Investments criteria.

## New instruments introduced since previous strategy

- iv. Reflecting increased market risk and difficulties in diversifying, this strategy introduces the new and highly secure option of UK Residential Mortgage Backed Securities, which provides a genuine diversification away from institutional credit risk and additional options for secured lending, enabling limits to be increased with existing counterparties in exchange for security of some sort of asset in the event of the borrower becoming insolvent.
- v. RMBS
  - Since the approval of the GIS Participants' Treasury Strategies, which all set out the rationale for senior UK Prime and Buy to Let RMBS, the GLA has appointed two managers to manage £100m each of GLA core cash in this asset class.

Almost half of the investments were made prior to the market turbulence following the EU referendum, enabling the GLA to reduce its exposure to banks; additionally, this action has provided an excellent market test of extreme conditions for the asset class. Unlike a number of banks and the UK itself, the ratings of UK RMBS were untouched by the negative market perception of the UK's actions and liquidity in the asset class was no worse than any other within the current investment strategy. Yield remains higher than other available options.
  - 15 UK Banks and Building Societies have over £100bn of AAA-rated RMBS outstanding, via bankruptcy-remote issuing companies, which ensures full credit de-linkage
  - This report therefore recommends inclusion of UK RMBS in the GIS subject to the limits proposed and the overall GIS WAM limit, in order to reduce risk and improve returns. The 20% limit reflects the fact that the GIS currently has a 91 day WAM limit and most of these instruments will have a WAM > 1 year.
  - Only senior RMBS are permitted at this stage, i.e. the GIS has first priority over the cash flows from the underlying pools of thousands of diversified UK residential prime or buy-to-let mortgages. These to date have always been AAA rated at inception with some isolated cases of downgrades to AA+ due to lower ratings of associated counterparties within the

RMBS structure such as the bank servicing the mortgages, rather than the underlying mortgages, reflecting the increased risk of possible payment disruption should the servicing bank fail (though no increased risk of non-payment). The strategy does not exclude these downgraded senior notes as the risk of loss is still very low but it should be noted that changes to RMBS structures since 2008 make this circumstance very unlikely in future.

- The cash flows from RMBS are generated by both interest and principal repayments of the mortgages in the relevant pool. In particular, when homeowners refinance (or move house) the pool experiences principal inflows, which are then passed through to the RMBS bondholders (which the most senior tranches, proposed here, receive before all others). Refinancing typically occurs much earlier than the final date of the mortgage, therefore it is not proposed to limit the legal maturity of RMBS, as these are set with reference to the longest dated mortgage in the pool and do not reflect the expected maturity date. In addition, RMBS deals are structured with financial penalties for the issuer beyond the expected maturity date, to ensure that deals mature as expected.
- The strong cash flow characteristics of senior RMBS mean that principal is repaid incrementally, therefore a proposed WAM limit of 3 years per security for the whole RMBS portfolio is proposed alongside a 5 year expected final maturity limit per security.

## vi. Covered Bonds

- Covered bonds are also secured on mortgage assets, but do not depend on mortgages for the cash flows. They are more like a normal bond issued by the relevant bank or building society except that should the issuer default, the covered bond holders will have security over the banks' mortgage assets, which could be sold to another bank to meet the obligation.
- Whilst the credit risk is clearly lower than unsecured lending to the issuer, the situation is different to RMBS and when the issuer is downgraded, covered bonds are typically downgraded too. Accordingly, the strategy does not permit the use of covered bonds issued by counterparties who do not themselves meet approved investment criteria.
- Another feature of covered bonds are extension clauses, typically of 2 years. For this reason, the strategy only permits the use of counterparties of A- rating or above to allow for downgrades over the extension period, should it be invoked.
- Because they are lower risk than unsecured lending to a given counterparty, covered bond yields are generally lower. Accordingly, the main circumstance in which they would be used in the current environment is to increase exposure to a strong and well understood counterparty already at its unsecured concentration limit.

## vii. Repurchase Agreements "Repos"

- Repos are a form of secured lending whereby rather than lend directly to a counterparty, the GIS would buy from them a security e.g. a bond and agree to sell it back at an agreed (higher) price at a future date. The profit on this transaction replaces interest in a normal lending agreement but there is the additional feature that if the borrower becomes insolvent, the GIS may keep the security, which is referred to as collateral.
- For this reason, only securities that meet GIS criteria may be accepted as collateral, however the duration limits of 21.0 and 20.0 do not apply since the expectation is that the

collateral will be disposed of at the first opportunity and over-collateralisation provides mitigation for any price movement.

- Furthermore, if such a default occurred, the GIS may need to sell the collateral for cash flow reasons so there may be some price risk between the default and the sale. Therefore, minimum levels of collateral, expressed as a percentage of the market value of collateral relative to the purchase price, are proposed.
- The strategy permits very limited repo exposure (2.5% and 10% in aggregate) to counterparties not meeting unsecured investment criteria. In this case, minimum collateral is set at 102% (in line with minimum standards for repo use by AAA rated money market funds) and the provision is designed to enable transactions with pension funds engaged in liability hedging activities, to mutual advantage.
- There are a number of ways to implement a repo. This is delegated to officers and their advisors or external managers, however per 46.0, legal title to the collateral must be unequivocally obtained and safe custody arrangements be in place.
- Repos will provide a further tool for balancing GIS risk and return: the risk is very much lower than unsecured lending to banks and others, although not as low as T-bills, however repo returns are slightly higher than T-Bills and there is more flexibility with maturity dates.

## 20.0

- i. For the purposes of this limit, WAM is the sum of each expected nominal cashflow and its respective expected incidence in days from the calculation date, divided by the total nominal cashflows; the use of expectations rather than contractual maturities reflects the use of instruments like RMBS which are subject to uncertain repayments. The Syndics place reliance on the systems and investment process of appointed managers to monitor and implement this limit.

## 28.0

- i. Credit Default Swaps (CDS) are effectively insurance contracts against a given counterparty defaulting; their price (typically expressed as an additional interest cost or 'spread' in basis points – i.e. 100ths of one percent). Higher prices may therefore reflect greater market perception of risk, although other supply and demand factors can distort this, including the activity of speculators. For this reason, the CIO has discretion to propose postponements to the impact of CDS data on limits.
- ii. Although the GIS typically participates in short term investments, it refers to 5 year CDS prices as this market has higher volumes of trading and therefore more accurately reflects market sentiment.
- iii. The GIS's advisor and data provider, Capita, proposes barrier levels dependent on market conditions as indicated by one of the main CDS indices, ITRAXX 5 year senior financials.
- iv. When the ITRAXX is below 100 basis points, a counterparty's limit band will be adjusted down one notch if their CDS price is between 100 and 150 or to 'no colour' if above 150

- v. When the ITRAXX is above 100, a counterparty's limit band will be adjusted down one notch if their CDS price between 1 and 50 basis points above the ITRAXX or to 'no colour' if more than 50 basis points above.

38.0

- i. Book value weighted average here means the sum of the products of principal sums invested (plus any capitalised interest, less any impairments or partial repayments but excluding any accrued interest or unrealised gains or losses) and the respective Credit Factors at the date of calculation, divided by the sum of principal sums invested (plus any capitalised interest, less any impairments or partial repayments but excluding any accrued interest or unrealised gains or losses)

49.0

- i. In the absence of the CIO, the senior member of the Group Treasury team present should assume responsibility for reviewing circumstances where discretion might be used, and make appropriate recommendations to the CFO or deputy, who will decide whether to exercise their powers under this strategy.

**Approved by Signatories:**

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**MARTIN CLARKE**

**Syndic, GLA**

**Date:** .....

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**SUE BUDDEN**

**Syndic, LFEPA**

**Date:** .....

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**GERRY MURPHY**

**Syndic, LLDC**

**Date:** .....

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**SIOBHAN PETERS**

**Syndic, MOPAC**

**Date:** .....

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**TRICIA CLARK**

**Syndic, LPFA**

**Date:** .....

## Appendix 6: Treasury Management Practices: Main Principles

### 1.0 INTRODUCTION

- 1.1 The Treasury Management Practices (TMPs): Main Principles below set out the manner in which the Authority will seek to achieve its Treasury policies and objectives. These TMPs: Main Principles follow the wording recommended by the latest edition of the CIPFA Treasury Management Code.
- 1.2 TMPs: Main Principles are supported by TMPs: Schedules, which provide specific details of the systems and routines employed and the records to be maintained to deliver the TMPs: Main Principles. These Schedules are maintained and updated as necessary, being operational procedures and forming an integral part of the Authority's treasury management manual.
- 1.3 Approval and monitoring of TMPs is a matter for local decision. As such the TMPs: Principles will be approved by the Authority and monitored by the Executive Director of Resources and annually reviewed by the Authority before the start of the year.
- 1.4 TMPs: Schedules will be approved, monitored and annually reviewed by the Executive Director of Resources.
- 1.5 Scrutiny of the approval and monitoring of TMPs will be performed by the Budget and Performance Committee following recommendations by the Executive Director of Resources.

### 2.0 TMP1 RISK MANAGEMENT

#### 2.1 General statement

- 2.1.1 The Executive Director of Resources will design, implement and monitor all arrangements for the identification, management and control of treasury management risk, will report at least annually on the adequacy/suitability thereof, and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the Authority's objectives in this respect, all in accordance with the procedures set out in TMP6 'Reporting requirements and management information arrangements'.
- 2.1.2 In respect of each of the following risks, the arrangements which seek to ensure compliance with these objectives are set out in the TMPs: Schedules.

#### 2.2 Credit and counterparty risk management

- 2.2.1 The Executive Director of Resources regards a key objective of the Authority's treasury management activities to be the security of the principal sums it invests. Accordingly, he/she will ensure that its counterparty lists and limits reflect a prudent attitude towards organisations with whom funds may be deposited, and will limit investment activities to the instruments, methods and techniques referred to in the TMP4 Approved instruments, methods and techniques and listed in the TMPs: Schedules. The Executive Director of Resources also recognises the need to have, and will therefore maintain, a formal counterparty policy in respect of those organisations from which the Authority may borrow, or with whom it may enter into other financing arrangements.

#### 2.3 Liquidity risk management

- 2.3.1 The Executive Director of Resources will ensure the Authority has adequate though not excessive cash resources, borrowing arrangements, overdraft or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business /service objectives.
- 2.3.2 The Executive Director of Resources will only borrow in advance of need where there is a clear business case for doing so and will only do so for the current capital programme or to finance future debt maturities.
- 2.4 Interest rate risk management
- 2.4.1 The Executive Director of Resources will manage Authority exposure to fluctuations in interest rates with a view to containing its interest costs, or securing its interest revenues, in accordance with the amounts provided in its budgetary arrangements as amended in accordance with TMP6 'Reporting requirements and management information arrangements'.
- 2.4.2 The Executive Director of Resources will achieve this by the prudent use of Authority approved instruments, methods, and techniques, primarily to create stability and certainty of costs and revenues, but at the same time retaining a sufficient degree of flexibility to take advantage of unexpected, potentially advantageous changes in the level or structure of interest rates. This should be subject to the consideration and, if required, approval of any policy or budgetary implications.
- 2.5 Exchange rate risk management
- 2.5.1 The Executive Director of Resources will manage its exposure to fluctuations in exchange rates, so as to minimise any detrimental impact on its budgeted income/expenditure levels.
- 2.6 Refinancing risk management
- 2.6.1 The Executive Director of Resources will ensure that Authority borrowing, private financing and partnership arrangements are negotiated, structured and documented, and the maturity profile of the monies so raised are managed, with a view to obtaining offer terms for renewal or refinancing, if required, which are competitive and as favourable to the Authority as can reasonably be achieved in the light of market conditions prevailing at the time.
- 2.6.2 The Executive Director of Resources will actively manage Authority relationships with its counterparties in these transactions in such a manner as to secure this objective, and will avoid overreliance on any one source of funding if this might jeopardise achievement of the above.
- 2.7 Legal and regulatory risk management
- 2.7.1 The Executive Director of Resources will ensure that all Authority treasury management activities comply with statutory powers and regulatory requirements. He/She will demonstrate such compliance, if required to do so, to all parties with whom the Authority deals in such activities. In framing its credit and counterparty policy under TMP[1] 'credit and counterparty risk management', he/she will ensure that there is evidence of counterparties' powers, authority and compliance in respect of the transactions they may effect with the Authority, particularly with regard to duty of care and fees charged.
- 2.7.2 The Executive Director of Resources recognises that future legislative or regulatory changes may impact on treasury management activities and, so far as it is reasonably able to do so, will seek to minimise the risk of these impacting adversely on the Authority.



## 2.8 Fraud, error and corruption, and contingency management

- 2.8.1 The Executive Director of Resources will ensure that he/she has identified the circumstances which may expose the Authority to the risk of loss through fraud, error, corruption or other eventualities in its treasury management dealings. Accordingly, he/she will maintain effective contingency management arrangements, to these ends.

## 2.9 Market risk management

- 2.9.1 The Executive Director of Resources will seek to ensure that the Authority's stated treasury management policies and objectives will not be compromised by adverse market fluctuations in the value of the principal sums it invests, and will accordingly seek to protect the Authority from the effects of such fluctuations.

## 3.0 **TMP2 PERFORMANCE MEASUREMENT**

- 3.1 The Executive Director of Resources is committed to the pursuit of value for money in the Authority's treasury management activities, and to the use of performance methodology in support of that aim, within the framework set out in the Authority's treasury management policy statement.
- 3.2 Accordingly, the treasury management function will be the subject of ongoing analysis of the value it adds in support of the organisation's stated business or service objectives. It will be the subject of regular examination of alternative methods of service delivery, of the availability of fiscal or other grant or subsidy incentives, and of the scope for other potential improvements. The performance of the treasury management function will be measured using the criteria set out in the TMPs: Schedules.

## 4.0 **TMP3 DECISION-MAKING AND ANALYSIS**

- 4.1 The Executive Director of Resources will maintain full records of Authority treasury management decisions, and of the processes and practices applied in reaching those decisions, both for the purposes of learning from the past, and for demonstrating that reasonable steps were taken to ensure that all issues relevant to those decisions were taken into account at the time. The issues to be addressed and processes and practices to be pursued in reaching these decisions are detailed in the TMPs: Schedules.

## 5.0 **TMP4 APPROVED INSTRUMENTS, METHODS AND TECHNIQUES**

- 5.1 The Executive Director of Resources will undertake Authority treasury management activities by employing only those instruments, methods and techniques detailed in the schedule to this document, and within the limits and parameters defined in TMP1 'Risk management'.

## 6.0 **TMP5 ORGANISATION, CLARITY AND SEGREGATION OF RESPONSIBILITIES, AND DEALING ARRANGEMENTS**

- 6.1 The Executive Director of Resources considers it essential, for the purposes of the effective control and monitoring of the Authority's treasury management activities, for the reduction of the risk of fraud or error, and for the pursuit of optimum performance, that these activities are structured and managed in a fully integrated manner, and that there is at all times a clarity of treasury management responsibilities.

- 6.2 The principal on which this will be based is a clear distinction between those charged with setting treasury management policies and those charged with implementing and controlling these policies, particularly with regard to the execution and transmission of funds, the recording and administering of treasury management decisions, and the audit and review of the treasury management function.
  
- 6.3 If and when the Authority intends, as a result of lack of resources or other circumstances, to depart from these principles, the Executive Director of Resources will ensure that the reasons are properly reported in accordance with TMP6 'Reporting requirements and management information arrangements', and the implications properly considered and evaluated.
  
- 6.4 The Executive Director of Resources will ensure that there are clear written statements of the responsibilities for each post engaged in treasury management, and the arrangements for absence cover. The Executive Director of Resources will also ensure that at all times those engaged in treasury management will follow the policies and procedures. The present arrangements are detailed in the TMPs: Schedules.
  
- 6.5 The Executive Director of Resources will ensure there is proper documentation for all deals and transactions, and that procedures exist for the effective transmission of funds. The present arrangements are detailed in the TMPs: Schedules
  
- 6.6 The delegations to the Executive Director of Resources in respect of treasury management are set out in the TMPs: Schedules. The Executive Director of Resources will fulfil all such responsibilities in accordance with the Authority's policy statement and TMPs and if a CIPFA member, the 'Standard of Professional Practice on Treasury Management'.

## **7.0 TMP6 REPORTING REQUIREMENTS AND MANAGEMENT INFORMATION ARRANGEMENTS.**

- 7.1 The Executive Director of Resources will ensure that regular reports are prepared and considered on the implementation of Authority treasury management policies; on the effects of decisions taken and transactions executed in pursuit of those policies; on the implications of changes, particularly budgetary, resulting from regulatory, economic, market or other factors affecting its treasury management activities; and on the performance of the treasury management function.
  
- 7.2 As a minimum:  
  
 The Authority will receive
  - an annual report on the proposed strategy and plan to be pursued in the coming year
  - a mid-year review
  - an annual report on the performance of the treasury management function, on the effects of the decisions taken and the transactions executed in the past year, and on any circumstances of non-compliance with the organisation's treasury management policy statement and TMPs.
  
- 7.3 The GLA Audit Panel, as the body with responsibility for the scrutiny of treasury management policies and practices, will receive regular monitoring reports on treasury management activities and risks.

7.4 The GLA Audit Panel responsible for scrutiny, such as an audit or scrutiny committee, will have responsibility for the scrutiny of treasury management policies and practices.

7.5 Local authorities should report the treasury management indicators as detailed in their sector-specific guidance notes.

7.6 The present arrangements and the form of these reports are detailed in the TMPs: Schedules.

## **8.0 TMP7 BUDGETING, ACCOUNTING AND AUDIT ARRANGEMENTS**

8.1 The Executive Director of Resources will prepare, and the Authority will approve and, if necessary, from time to time will amend, an annual budget for treasury management, which will bring together all of the costs involved in running the treasury management function, together with associated income. The matters to be included in the budget will at minimum be those required by statute or regulation, together with such information as will demonstrate compliance with TMP1 'Risk management', TMP2 'Performance measurement', and TMP4 'Approved instruments, methods and techniques'.

8.2 The Executive Director of Resources will exercise effective controls over this budget, and will report upon and recommend any changes required in accordance with TMP6 'Reporting requirements and management information arrangements'.

8.3 The Executive Director of Resources will account for the Authority's treasury management activities, for decisions made and transactions executed, in accordance with appropriate accounting practices and standards, and with statutory requirements in force for the time being.

## **9.0 TMP8 CASH AND CASH FLOW MANAGEMENT**

9.1 Unless statutory or regulatory requirements demand otherwise, all monies in the hands of this Authority will be under the control of the Executive Director of Resources, and will be aggregated for cash flow and investment management purposes. Cash flow projections will be prepared on a regular and timely basis, and the Executive Director of Resources will ensure that these are adequate for the purposes of monitoring compliance with TMP1 (1.3) 'Liquidity risk management'. The present arrangements for preparing cash flow projections, and their form are set out in the TMPs: Schedules.

## **10.0 TMP9 MONEY LAUNDERING**

10.1 The Executive Director of Resources is alert to the possibility that the Authority may become the subject of an attempt to involve it in a transaction involving the laundering of money. Accordingly, it will maintain procedures for verifying and recording the identity of counterparties and reporting suspicions, and will ensure that staff involved in this are properly trained. The present arrangements, including the name of the officer to whom reports should be made, are detailed in the TMPs: Schedules.

## **11.0 TMP10 TRAINING AND QUALIFICATIONS**

11.1 The Executive Director of Resources recognises the importance of ensuring that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. He/She will therefore seek to appoint individuals who are both capable and experienced and will provide training for staff to enable them to acquire and

maintain an appropriate level of expertise, knowledge and skills. The Executive Director of Resources will recommend and implement the necessary arrangements.

- 11.2 The Executive Director of Resources will ensure that Authority members tasked with treasury management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities.
- 11.3 Those charged with governance recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively.
- 11.4 The present arrangements are detailed in the TMPs: Schedules.

## **12.0 TMP11 USE OF EXTERNAL SERVICE PROVIDERS**

- 12.1 The Authority recognises that responsibility for the treasury management decisions remains with the Authority at all times. It recognises that there may be potential value in employing external providers of treasury management services, in order to acquire access to specialist skills and resources. When it employs such service providers, it will ensure it does so for reasons which have been submitted to a full evaluation of the costs and benefits. It will also ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review. And it will ensure, where feasible and necessary, that a spread of service providers is used, to avoid overreliance on one or a small number of companies. Where services are subject to formal tender or re-tender arrangements, legislative requirements will always be observed. The monitoring of such arrangements rests with the Executive Director of Resources, and details of the current arrangements are set out in the TMPs: Schedules.

## **13.0 TMP12 CORPORATE GOVERNANCE**

- 13.1 The Authority is committed to the pursuit of proper corporate governance throughout its businesses and services, and to establishing the principals and practices by which this can be achieved. Accordingly, the treasury management function and its activities will be undertaken with openness and transparency, honesty, integrity and accountability.
- 13.2 This Authority has adopted and implemented the key principles of the TM Code. This, together with the other arrangements detailed in the TMPs; Schedules, are considered vital to the achievement of proper corporate governance in treasury management, and the Executive Director of Resources will monitor and, if and when necessary, report upon the effectiveness of these arrangements.

# Appendix 7: Treasury Management Outturn position for 2015-16 and mid-year position for 2016-17

## 1. Summary Portfolio Position

Current Treasury Management Position	Actual as at 31 March 2015		Actual as at 31 March 2016		Actual as at 30 September 2016	
	£m	Av. Rate	£m	Av. Rate	£m	Av. Rate
<b>External Borrowing</b>						
Long Term Borrowing	3,563.25	3.50%	3,595.38	3.50%	3,686.38	3.43%
Short Term Borrowing	35.00	0.75%	112.00	0.57%	116.00	0.60%
<b>Total External Borrowing (A)</b>	<b>3,598.25</b>		<b>3,707.38</b>		<b>3,802.38</b>	
<b>Other Long Term Liabilities</b>						
PFI Liability	0.00		0.00		0.00	
Finance Lease Liability	0.00		0.00		0.00	
<b>Total Other Long Term Liabilities (B)</b>	<b>0.00</b>		<b>0.00</b>		<b>0.00</b>	
<b>Total Gross Debt (A+B)</b>	<b>3,598.25</b>		<b>3,707.38</b>		<b>3,802.38</b>	
Capital Financing Requirement*	3,630.12		3,619.18		3,678.50	
Less Other Long Term Liabilities	0.00		0.00		0.00	
<b>Underlying Capital Borrowing Requirement (C)</b>	<b>3,630.12</b>		<b>3,619.18</b>		<b>3,678.50</b>	
<b>Under/(Over) Borrowing (C-A)</b>	<b>31.87</b>		<b>-88.20</b>		<b>-123.88</b>	
<b>Investments (D)</b>	<b>998.95</b>	<b>0.72%</b>	<b>1,752.59</b>	<b>0.72%</b>	<b>1,648.57</b>	<b>0.69%</b>
<b>Net Borrowing/(Investments) (A-D)</b>	<b>2,599.30</b>		<b>1,954.79</b>		<b>2,153.81</b>	

## 2. Treasury Management Budget

	2015-16 Opening Estimate £m	2015-16 Year End Actual £m	Variance between Opening Estimate and Year end Actual £m	2016-17 Opening Estimate £m	2016-17 Actual as at 30.9.15 £m	2016-17 Revised Estimate £m	Variance between Opening Estimate and Revised Estimate £m
PWLB Interest payable	125.10	125.51	0.41	125.10	63.30	126.46	1.36
Interest receivable	-8.30	-9.97	-1.67	-8.00	-6.05	-8.76	-0.76
Minimum Revenue Provision & Vol Revenue Provision	101.10	101.10	0.00	101.10	19.00	101.10	0.00
<b>Total</b>	<b>217.90</b>	<b>216.64</b>	<b>-1.26</b>	<b>218.20</b>	<b>76.25</b>	<b>218.80</b>	<b>0.60</b>

### 3. Prudential Code Indicators and Treasury Management Limits

#### i) Capital Financing Requirement

	2015-16 Original Estimate £m	2015-16 Year End Actual £m	2015-16 Variance between Original Estimate and Year End Actual £m	2016-17 Original Estimate £m	2016-17 Revised Estimate £m	2016-17 Variance between Original Estimate and Revised Estimate £m
Total CFR	3,464.40	3,619.10	154.70	3,764.00	3,678.50	(85.50)

#### ii) Authorised Limit for External Debt

	2015-16 Final Authorised Limit £m	2015-16 Actual External Debt £m	Headroom £m	2016-17 Original Authorised Limit £m	2016-17 Actual External Debt As At 30.09.15 £m	Headroom £m	2016-17 Revised Authorised Limit £m
Borrowing	4,600.00	3,707.38	892.62	4,800.00	3,802.38	997.62	4,800.00
Other long term liabilities	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Total	4,600.00	3,707.38	892.62	4,800.00	3,802.38	997.62	4,800.00

#### iii) Operational Boundary for External Debt

	2015-16 Final Operational Boundary £m	2015-16 Actual External Debt £m	Headroom £m	2016-17 Original Operational Boundary £m	2016-17 Actual External Debt As At 30.09.15 £m	Headroom £m	2016-17 Revised Operational Boundary £m
Borrowing	4,290.00	3,707.38	582.62	4,300.00	3,802.38	497.62	4,300.00
Other long term liabilities	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Total	4,290.00	3,707.38	582.62	4,300.00	3,802.38	497.62	4,300.00

iv) Net Borrowing Upper Limits to Fixed and Variable Interest Rate Exposure

	Opening 2015-16	As at 31.03.16	Opening 2016-17	As at 30.09.16
	%	%	%	%
Fixed rate	100.00	189.66	100.00	167.26
Variable rate	20.00	-89.66	0.00	-67.26

NB: when the limits were set they were set on the basis of Gross debt, whilst the definition of the indicator refers to net debt. All current long term debt is on a fixed rate basis whilst by definition investments will be variable as they are set for less than one year. The use of the net indicator therefore logically will always result in a fixed rate upper limit in excess of 100%.

v) Limits for Maturity Structure of Borrowing

	Upper Limit	Lower Limit	As at 31.03.2016
	%	%	%
Under 12 months	100.00	0.00	4.07
12 months and within 24 months	100.00	0.00	1.83
24 months and within 5 years	100.00	0.00	9.58
5 years and within 10 years	100.00	0.00	25.43
10 years and above	100.00	0.00	59.09

4. Crossrail Monitoring

	Totals as at		
	31/03/2016 £m	30/09/2016 £m	31/03/2017 £m
Total borrowing of project	3,251.25	3,226.25	3,138.00
In year interest paid	118.30	58.20	116.35
In year interest receivable	0.12	0.06	0.13
Net in year interest paid	118.18	58.14	116.22
In year BRS receipts	218.30	106.80	219.00
In year payments to TfL	-	-	-

## 5. NLE Monitoring

	Totals as at		
	31/03/2016 £m	30/09/2016 £m	31/03/2017 £m
Total borrowing of project	201.10	321.10	321.10
In year interest paid	0.38	-	2.10
In year interest receivable	- 0.71	- 0.40	- 0.68
Net in year interest paid	- 0.33	0.40	1.42
In year payments to TfL	121.00	76.30	160.50