APPENDIX C

Risk Environment 2017/18	
Credit Ratings	**Local Context**
The most significant change was the downgrade by Moody's to the UK sovereign rating in September from Aa1 to Aa2 which resulted in subsequent downgrades to sub-sovereign entities including local authorities. Changes to credit ratings included Moody's downgrade of Standard Chartered Bank's long-term rating to A1 from Aa3 and the placing of UK banks' long-term ratings on review to reflect the impending ring-fencing of retail activity from investment banking (Barclays, HSBC and RBS were on review for downgrade; Lloyds Bank, Bank of Scotland and National Westminster Bank were placed on review for upgrade). Standard & Poor's (S&P) revised upwards the outlook of various UK banks and building societies to positive or stable and simultaneously affirmed their long and short-term ratings, reflecting the institutions' resilience, progress in meeting regulatory capital requirements and being better positioned to deal with uncertainties and potential turbulence in the run-up to the UK's exit from the EU in March 2019. The agency upgraded Barclays Bank's long-term rating to A from A- after the bank announced its plans for its entities post ring-fencing. Fitch revised the outlook on Nationwide Building Society to negative and later downgraded the institution's long-term ratings due to its reducing buffer of junior debt. S&P revised the society's outlook from positive to stable. S&P downgraded Transport for London to AA- from AA following a deterioration in its financial position	The Council receives monthly updates from its advisors on changes to credit ratings. Whilst the Council maintains deposits on a short-term or available instant basis the risk is reduced from failures, as the Council will be able to withdraw funds as soon as there is an indication of a credit problem. Whereas other investors with longer term fixed investments will not be able to.
Other Developments	**Local Context**
In February, Arlingclose advised against lending to Northamptonshire County Council (NCC). NCC issued a section 114 notice in the light of severe financial challenge and the risk that it would not be in a position to deliver a balanced budget. In March, following Arlingclose's advice,	The Council has not and does not intend to lend to Northamptonshire County Council. Whilst the Council uses Natwest for transactional banking (ie paying suppliers, receiving payments from customer) it is

the Authority removed RBS plc and National Westminster Bank from its counterparty list. This did not reflect any change to the creditworthiness of either bank, but a tightening in Arlingclose's recommended minimum credit rating criteria to A- from BBB+ for FY 2018-19. The current long-term ratings of RBS and NatWest do not meet this minimum criterion, although if following ring-fencing NatWest is upgraded, the bank would be reinstated on the Authority's lending list.	only keeping a minimal balance with Natwest until it again meets the requirements of Arlingclose's recommended list. Cash balances are transferred out to the Council's Money Market Funds and Call Accounts.
Regulatory Changes	
The 2017 Prudential Code introduces the requirement for a Capital Strategy which provides a high-level overview of the long-term context of capital expenditure and investment decisions and their associated risks and rewards along with an overview of how risk is managed for future financial sustainability. Where this strategy is produced and approved by full Council, the determination of the Treasury Management Strategy can be delegated to a committee. The Code also expands on the process and governance issues of capital expenditure and investment decisions In the 2017 Treasury Management Code the definition of 'investments' has been widened to include financial assets as well as non-financial assets held primarily for financial returns such as investment property. These, along with other investments made for non-treasury management purposes such as loans supporting service outcomes and investments in subsidiaries, must be discussed in the Capital Strategy or Investment Strategy. Additional risks of such investments are to be set out clearly and the impact on financial sustainability is be identified and reported.	It is expected that a Capital Strategy will be created over the summer and approved by Cabinet in the autumn. The current Treasury Management Strategy is based on the Prudential Code 2013 and the Treasury Management Code 2011. The 2019/20 Strategy which will go to Council in February 2019 will be based on the new CIPFA codes (Treasury Management Code 2017 and Prudential Code 2017).
MHCLG MRP and Investment Guidance	
In February 2018 the MHCLG published revised Guidance on Local Government and Investments and Statutory Guidance on Minimum Revenue Provision (MRP). Changes to the Investment Guidance include a wider definition of investments to	The new MHCLG investment guidance now includes the purchases made through the CIS, rather than just purely financial investments. Commercial investments should not be purely for the revenue return but should

include non-financial assets held primarily for generating income return and a new category called “loans” (e.g. temporary transfer of cash to a third party, joint venture, subsidiary or associate). The Guidance introduces the concept of proportionality, proposes additional disclosure for borrowing solely to invest and also specifies additional indicators. Investment strategies must detail the extent to which service delivery objectives are reliant on investment income and a contingency plan should yields on investments fall. The definition of prudent MRP has been changed to “put aside revenue over time to cover the CFR”; it cannot be a negative charge and can only be zero if the CFR is nil or negative. Guidance on asset lives has been updated, applying to any calculation using asset lives. Any change in MRP policy cannot create an overpayment; the new policy must be applied to the outstanding CFR going forward only.	also give a service benefit such as economic growth/development.
MiFID II	
As a result of the second Markets in Financial Instruments Directive (MiFID II), from 3rd January 2018 local authorities were automatically treated as retail clients but could “opt up” to professional client status, providing certain criteria was met which includes having an investment balance of at least £10 million and the person(s) authorised to make investment decisions on behalf of the authority have at least a year’s relevant professional experience. In addition, the regulated financial services firms to whom this directive applies have had to assess that that person(s) have the expertise, experience and knowledge to make investment decisions and understand the risks involved	The Authority has met the conditions to opt up to professional status and has done so in order to maintain its erstwhile MiFID II status prior to January 2018. The Authority will continue to have access to products including money market funds, pooled funds, treasury bills, bonds, shares and to financial advice.