

**SECURITY, LIQUIDITY AND YIELD BENCHMARKING**

Member reporting on the consideration and approval of security and liquidity benchmarks will continue. These benchmarks are targets and so may be breached from time to time. Any breach will be reported, with supporting reasons in the Annual Treasury Management Report.

1. **Security**

In context of benchmarking, assessing security is a subjective area to assess. Security is currently evidenced by the application of minimum credit quality criteria to investment counterparties, primarily through the use of credit ratings supplied by the three main credit rating agencies (Fitch, Moody's and Standard and Poor's). Whilst this approach embodies security considerations, benchmarking levels of risk is more problematic. One method to benchmark security risk is to assess the historic level of default against the minimum criteria used in the Council's investment strategy.

The table below shows average defaults for differing periods of investment grade products for each Fitch/Moody's and Standard & Poor's long term rating category.

| <b>Long term rating</b>              | <b>1 year</b> | <b>2 years</b> | <b>3 years</b> |
|--------------------------------------|---------------|----------------|----------------|
| <b>AAA</b>                           | <b>0.04%</b>  | <b>0.09%</b>   | <b>0.17%</b>   |
| <b>AA<br/>(includes AA- and AA+)</b> | <b>0.02%</b>  | <b>0.04%</b>   | <b>0.09%</b>   |
| <b>A</b>                             | <b>0.05%</b>  | <b>0.14%</b>   | <b>0.26%</b>   |
| <b>BBB</b>                           | <b>0.14%</b>  | <b>0.38%</b>   | <b>0.66%</b>   |
| <b>BB</b>                            | <b>0.64%</b>  | <b>1.79%</b>   | <b>3.14%</b>   |
| <b>B</b>                             | <b>2.81%</b>  | <b>6.83%</b>   | <b>10.44%</b>  |
| <b>CCC</b>                           | <b>19.89%</b> | <b>27.52%</b>  | <b>32.84%</b>  |

The Council's minimum long term rating criteria is currently "AA-" for any investment greater than one year and "A" for any investment up to one year. The average expectation of default for a one, two or three year investment in a counterparty with a "AA-" long term rating would be approximately 0.02% of the total investment and the average expectation of default for a one year investment in a counterparty with a "A" long term rating would be 0.05% of the total investment. This is only an average, any specific counterparty loss is likely to be higher, but these figures do act as a proxy benchmark for risk across the portfolio.

The Council's maximum security risk benchmark for the whole portfolio, when compared to these historic default tables, is:

- **0.17% historic risk of default when compared to the whole portfolio.**

In addition, the security benchmark for each individual year is:

|                | <b>1 year</b> | <b>2 years</b> | <b>3 years</b> |
|----------------|---------------|----------------|----------------|
| <b>Maximum</b> | <b>0.04%</b>  | <b>0.09%</b>   | <b>0.17%</b>   |

These benchmarks are embodied in the criteria for selecting cash investment counterparties and these will be monitored and reported to Members in the Annual Treasury Management Report. As this data is collated, trends and analysis will be collected and reported. Where a counterparty is not credit rated a proxy rating will be applied in conjunction with our advisers, considering the regulatory environment and financial standing of an organisation.

## 2. **Liquidity**

This is defined as “having adequate, though not excessive cash resources, borrowing arrangements, overdrafts 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” (Revised CIPFA Treasury Management Code of Practice). In respect of this area the Council seeks to maintain:

- Bank overdraft facility - £0.5m
- Liquid short term deposits of at least £10m available immediately on call

The availability of liquidity and the term risk in the portfolio can be benchmarked by the monitoring of the Weighted Average Life (WAL) of the portfolio – shorter WAL would generally embody less liquidity risk. In this respect the proposed benchmark is to be used:

- **WAL benchmark is expected to be 0.5 years, with a maximum of 1 year.**

## 3. **Yield**

Benchmarks are widely used to assess investment performance. Previously, the “7 day LIBID rate” was the recognised rate which the Council would aim to exceed when lending money, however the LIBID rates ceased from 31<sup>st</sup> December 2021. Work is currently progressing with our Treasury advisors at Link and their clients to replace this rate with a suitable alternative for benchmarking. We will monitor the situation closely and an update will be provided in future Quarterly Reports.

Security and liquidity benchmarks are intrinsic to the approved treasury strategy through the counterparty selection criteria and some of the prudential indicators. Proposed benchmarks for the cash type investments are shown above and form the basis of reporting in this area.