

**Somerset Council Lending Counterparty Criteria 2024-25**

The following criteria will be used to manage counterparty risks to Somerset Council investments for new deposits / investments from 1st April 2024.

Please note that the limits in this appendix apply only to Treasury Management Investments, not to those detailed in the separate Investment Strategy.

Where deposits held were made under previous criteria, there will be no compulsion to terminate those deposits to meet new criteria, where a penalty would be incurred.

**Deposits**

Any Financial Institution that is authorised by the Prudential Regulation Authority to accept deposits in the UK or is a UK Building Society can be lent to, subject to the rating criteria below at the time of the deposit.

**Unrated Building Societies**

Unrated Building Societies as identified by Treasury Advisors can be used, with a maximum of £1m per Society and a maximum maturity of 1 year.

**Marketable Instruments** – Any bank, other organisation, or security whose credit ratings satisfy the criteria below: -

**Rating of Counterparty or Security**

Deposits or instruments of less than 13 months duration (refer to long-term ratings)

Fitch A- or above

S&P A- or above

Moody's A3 or above

The maximum deposit / investment amount for any authorised counterparty or security that has as a minimum at least two ratings of the three above will be £15m (Reduced by £5m from 2023-24). This is approximately 5.4% of average investment balances, or 9.4% of average cash balances up to 30<sup>th</sup> November. The % may be significantly less if borrowing up to the CFR is taken early in the year.

The allowed deposit amounts above are the single maximum per counterparty at any one time, and that counterparty or security must be rated as above or better by at least two of the three agencies. Short-term ratings will be monitored and considered in relative rather than absolute terms.

It remains the Council's policy to suspend or remove institutions that still meet criteria, but where any of the other factors below give rise to concern. Also, when it is deemed prudent, the duration of deposits placed is shortened or lengthened, depending on counterparty specific metrics, or general investment factors. Where deposits held were made under previous criteria, there will be no compulsion to terminate those deposits to meet new criteria, where a penalty would be incurred.

### **Operational Bank Accounts**

As the Council's current bankers, Nat West are currently within the minimum criteria. If they should fall below criteria, the instant access Call Account facility may still be used for short-term liquidity requirements and business continuity arrangements. This will generally be for smaller balances where it is not viable to send to other counterparties or in the event of unexpected receipts after the daily investment process is complete. Money will be placed in the instant access Nat West call account overnight.

### **Public Sector Bodies**

Any UK Local Authority or Public Body will have a limit of £10m (Reduced by £5m from 2023-24) and a maximum maturity of 2 years.

The UK Government, including Gilts, T-Bills, and the Debt Management Office (DMADF) will be unlimited in amount and duration.

The table below gives a definition and approximate comparison of various ratings by the three main agencies: -

## Definitions of Rating Agency Ratings

	Fitch		Moody's		S&P
Short-Term	<b>F1+</b> Exceptionally strong	<b>P-1</b>	Superior	<b>A-1+</b>	Extremely strong
	<b>F1</b> Highest quality			<b>A-1</b>	Strong
	<b>F2</b> Good quality	<b>P-2</b>	Strong	<b>A-2</b>	Satisfactory
	<b>F3</b> Fair quality	<b>P-3</b>	Acceptable	<b>A-3</b>	Adequate
	<b>B</b> Speculative	<b>NP</b>	Questionable	<b>B and below</b>	Significant speculative characteristics
	<b>C</b> High default risk				
	<b>(+) or (-)</b>	<b>(1,2, or 3)</b>		<b>(+) or (-)</b>	
Long-Term	<b>AAA</b> Highest quality	<b>Aaa</b>	Exceptional	<b>AAA</b>	Extremely strong
	<b>AA</b> V High quality	<b>Aa</b>	Excellent	<b>AA</b>	Very strong
	<b>A</b> High quality	<b>A</b>	Good	<b>A</b>	Strong
	<b>BBB</b> Good quality	<b>Baa</b>	Adequate	<b>BBB</b>	Adequate capacity
	<b>BB</b> Speculative	<b>Ba</b>	Questionable	<b>BB and below</b>	Significant speculative characteristics
	<b>B</b> Highly Speculative	<b>B</b>	Poor		
	<b>CCC</b> High default risk	<b>Caa</b>	Extremely poor		

### Financial Groups

For Financial Groups (where two or more separate counterparties are owned by the same eventual parent company) investments can be split between entities, but an overall limit equal to the highest rated constituent counterparty within the group will be used.

### Country Limits

Excluding the UK, there will be a limit of £20m collectively to all organisations domiciled in one Sovereign Country (Reduced by £10m from 2023-24). This is approximately 7.2% of average investment balances, or 12.6% of average cash balances up to 30<sup>th</sup> November. The % may be significantly less if borrowing up to the CFR is taken early in the year.

### Money Market Funds

Any LVNAV Money Market Fund used must be rated by at least two of the main three ratings agencies and must have the following ratings.

Fitch AAmmf

Moody's Aaa-mf

Standard & Poor's AAAM

Subject to the above, deposits can be made with the following limits: -

The lower of £15m or 0.5% of the total value for individual Funds.

### **VNAV and other Pooled Funds**

As a result of the review of strategic pooled funds, there will be disinvestment from this portfolio. The scale, timing, and identification of individual funds to be sold will depend on market conditions, potential gains or losses, and diversification.

It may be decided that a percentage of pooled funds are retained to provide diversification should cash interest rates fall significantly again. Whilst it is difficult to state absolute or percentage limits at present, amounts would be in relation to core balances and reserves and will be significantly below levels currently held.

### **Other Indicators**

The Council will continue to use a range of indicators, not just credit ratings. Among other indicators to be taken into account will be:

- Credit Default Swaps and Government Bond Spreads.
- GDP, and Net Debt as a Percentage of GDP for sovereign countries.
- Likelihood and strength of Parental Support.
- Banking resolution mechanisms for the restructure of failing financial institutions, i.e. bail-in.
- Share Price.
- Market information on corporate developments and market sentiment towards the counterparties and sovereigns.
- Underlying securities or collateral for covered instruments.
- Other macroeconomic factors