

**TREASURY MANAGEMENT STRATEGY STATEMENT, TREASURY MANAGEMENT POLICY STATEMENT, MINIMUM REVENUE PROVISION POLICY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2020/21**

**Purpose**

To comply with the requirement of the Council's Treasury Management Policy in reporting to Council the proposed strategy for the forthcoming year and the Local Government Act 2003 with the reporting of the Prudential Indicators.

**Executive Summary**

The Local Government Act 2003 requires the Council to produce prudential indicators in line with the Prudential Code.

This report outlines the Council's prudential indicators for 2020/21 – 2022/23 and sets out the expected Treasury operations for this period. This report and associated tables fulfil the statutory requirement of the Local Government Act 2003 by:

- Reporting the prudential indicators as required by the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities;
- Setting the Council's Minimum Revenue Provision (MRP) Policy, which defines how the Council will pay for capital assets through revenue contributions each year (as required by Regulation under the Local Government and Public Involvement in Health Act 2007);
- Setting the Treasury Management Strategy in accordance with the CIPFA Code of Practice on Treasury Management;
- Adopting the Council's Treasury Management Policy Statement as recommended within the CIPFA Code of Practice 2017;
- Setting the Investment Strategy (in accordance with the Ministry of Housing, Communities and Local Government (MHCLG) investment guidance); and
- Affirming the effective management and responsibility for the control of risk and clearly identifying our appetite for risk. The Council's risk appetite is low in order to give priority to **S**ecurity, **L**iquidity then **Y**ield (or return on investments).

Under the requirements of the CIPFA Code of Practice and associated Guidance Notes 2017, the following four clauses have been adopted:

- a) This Council 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 organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

- b) This Council 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.
- c) This Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Cabinet, and for the execution and administration of treasury management decisions to the Executive Director Finance, who will act in accordance with the organisation's policy statement and TMPs.
- d) This Council nominates the Audit and Governance Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

### **Equalities Implications**

There are no equalities implications arising from the report.

### **Legal Implications**

Approval of Prudential Indicators and an Annual Investment Strategy is a legal requirement of the Local Government Act 2003. Members are required under the CIPFA Code of Practice to have ownership and understanding when making decisions on Treasury Management matters.

### **Resource and Value for Money Implications**

All financial resource implications are detailed in the body of this report which links to the Council's Medium Term Financial Strategy and Capital Strategy.

### **Risk Implications**

Risk is inherent in Treasury Management and as such a risk based approach has been adopted throughout the report with regard to Treasury Management processes.

A Glossary of terms utilised within the report can be found at **ANNEX 9**.

**Report Author** Please contact Jo Goodfellow, Head of Finance, ext 241 or Stefan Garner, Executive Director Finance, ext 242

<b>Background Papers:-</b>	<b><i>Budget &amp; Medium Term Financial Strategy 2020/21</i></b>
	<b><i>Mid-year Treasury Report 2019/20 Council, 10/12/19</i></b>
	<b><i>Annual Treasury Report 2018/19 Council, 10/09/19</i></b>
	<b><i>Treasury Management Strategy Statement, Treasury Management Policy Statement, Minimum Revenue Provision Policy Statement &amp; Annual Investment Statement 2019/20 Council 26/02/19</i></b>
	<b><i>Treasury Management Training slides 20<sup>th</sup> November 2019</i></b>
	<b><i>CIPFA Code of Practice on Treasury Management in Public Services 2017</i></b>
	<b><i>DCLG Guidance on Local Government Investments March 2010</i></b>
	<b><i>Local Government Act 2003</i></b>
	<b><i>Treasury Management Practices 2020/21 (Operational Detail)</i></b>

## 1. INTRODUCTION

### 1.1 Background

The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the Treasury Management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

The second main function of the Treasury Management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

The contribution the treasury management function makes to the Council is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day to day treasury management activities.

CIPFA defines treasury management as:

*The management of the local authority's borrowing, 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.*

### 1.2 Reporting Requirements

#### 1.2.1 Capital Strategy

The CIPFA 2017 Prudential and Treasury Management Codes require all local authorities to prepare a capital strategy report which will provide the following:

- a high-level long term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

The aim of this capital strategy is to ensure that all elected members on the full council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset. The capital strategy will show:

- The corporate governance arrangements for these types of activities;
- Any service objectives relating to the investments;
- The expected income, costs and resulting contribution;
- The debt related to the activity and the associated interest costs;
- The payback period (MRP policy);
- For non-loan type investments, the cost against the current market value;
- The risks associated with each activity.

Where a physical asset is being bought, details of market research, advisers used, (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

Where the Council has borrowed to fund any non-treasury investment, there should also be an explanation of why borrowing was required and why the MHCLG Investment Guidance and CIPFA Prudential Code have not been adhered to.

If any non-treasury investment sustains a loss during the final accounts and audit process, the strategy and revenue implications will be reported through the same procedure as the capital strategy.

To demonstrate the proportionality between the treasury operations and the non-treasury operation, high-level comparators are shown throughout this report.

### **1.2.2 Treasury Management Reporting**

The Council is currently required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

#### **Prudential and Treasury Indicators and Treasury Strategy** (this report) –

The first, and most important, report is forward looking and covers:

- the capital plans (including prudential indicators);
- a Minimum Revenue Provision (MRP) Policy (how residual capital expenditure is charged to revenue over time);

- the Treasury Management Strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an Investment Strategy (the parameters on how investments are to be managed).

### **A Mid Year Treasury Management Report**

This is primarily a progress report and will update Members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

### **An Annual Treasury Report**

This is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

### **Scrutiny**

The above reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken by the Audit and Governance Committee.

### **1.3 Treasury Management Strategy for 2020/21**

The strategy for 2020/21 covers two main areas:

#### **Capital Issues**

- the capital expenditure plans and the associated Prudential Indicators;
- the Minimum Revenue Provision (MRP) policy.

#### **Treasury Management Issues**

- the current treasury position;
- treasury indicators which will limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- policy on use of external service providers.

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the MHCLG MRP Guidance, the CIPFA Treasury Management Code and MHCLG Investment Guidance.

### **1.4 Training**

The CIPFA Code requires the responsible officer to ensure that Members with responsibility for treasury management receive adequate training in treasury management. This especially applies to Members responsible for scrutiny. Detailed Treasury Management training was most recently provided in November 2019, and will be provided as and when required.

The training needs of Treasury Management officers are regularly reviewed.

## 1.5 Treasury Management Consultants

The Council uses Link Asset Services, Treasury Solutions as its external treasury management advisors.

The Council recognises that responsibility for Treasury Management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisors.

It also recognises that there is value in employing external providers of Treasury Management services in order to acquire access to specialist skills and resources. The Council will 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.

## 2. THE CAPITAL PRUDENTIAL INDICATORS 2020/21 – 2022/23

The Council's Capital Expenditure plans are the key driver of Treasury Management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

### 2.1 Capital Expenditure

This prudential Indicator is a summary of the Council's Capital Expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts:

Capital Expenditure £m	2018/19 Actual	2019/20 Predicted Outturn*	2019/20 Re- profiling	2020/21 Estimate**	2021/22 Estimate	2022/23 Estimate
<b>Non-HRA</b>	3.376	3.781	1.816	1.579	1.356	0.831
<b>HRA</b>	9.266	26.897	2.453	10.246	9.502	8.377
<b>Commercial Activities/Non- Financial Investments ***</b>	7.139	4.135	8.726	-	-	-
<b>Total</b>	<b>19.781</b>	<b>34.812</b>	<b>12.995</b>	<b>11.825</b>	<b>10.858</b>	<b>9.208</b>

\* Actual Projected at Period 9

\*\* excludes projected slippage from 2019/20

\*\*\* commercial activities/non-financial investments relate to areas such as capital expenditure on investment properties & investments in property funds.

The projected slippage into 2020/21 of £12.995m relates mainly to Gungate development, Gateways projects, Castle Mercian Trail, Amington Woodland & Cycleway, Property Fund investments and Solway LATC, High Rise lifts and Tinkers Green and Kerria redevelopment.

Other long-term liabilities - the above financing need excludes other long-term liabilities, such as PFI and leasing arrangements which already include borrowing instruments.

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding (borrowing) need.

<b>Capital Financing (GF/HRA)</b>	<b>2018/19</b>	<b>2019/20</b>	<b>2019/20</b>	<b>2020/21</b>	<b>2021/22</b>	<b>2022/23</b>
	<b>Actual</b>	<b>Predicted Outturn*</b>	<b>Re-profiling</b>	<b>Estimate**</b>	<b>Estimate</b>	<b>Estimate</b>
Capital Receipts	8.198	9.095	8.923	1.533	1.230	1.410
Capital Grants	2.822	0.659	0.113	0.424	0.424	0.424
Capital Reserves	3.605	13.310	0.534	6.010	5.442	4.306
Revenue Reserves	5.061	5.391	0.853	3.015	3.005	2.816
Revenue Contributions	0.095	0.118	0.300	-	-	-
<b>Net financing need for the year</b>	-	6.24	2.27	0.84	0.76	0.25
<b>Total</b>	<b>19.781</b>	<b>34.812</b>	<b>12.995</b>	<b>11.825</b>	<b>10.858</b>	<b>9.208</b>

\* Actual Projected at Period 9

\*\* excludes projected slippage from 2019/20

However, it should be noted that due to receipt of Homes England grant of c.£5m, it is likely that the planned borrowing for the Regeneration of Tinkers Green and Kerria will be reduced to c.£2m.

The net financing need for commercial activities/non-financial investments included in the above table against expenditure is shown below:

<b>Commercial Activities/Non-Financial Investments</b>	<b>2018/19</b>	<b>2019/20</b>	<b>2019/20</b>	<b>2020/21</b>	<b>2021/22</b>	<b>2022/23</b>
	<b>Actual</b>	<b>Predicted Outturn*</b>	<b>Re-profiling</b>	<b>Estimate**</b>	<b>Estimate</b>	<b>Estimate</b>
Capital Expenditure	7.139	4.135	8.726	-	-	-
Financing Costs	(7.139)	(4.135)	(8.726)	-	-	-
<b>Net financing need for the year</b>	-	-	-	-	-	-
Percentage of total net financing need %	-	-	-	-	-	-



## 2.2 The Council's Borrowing Need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so its underlying borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

The CFR does not increase indefinitely, as the Minimum Revenue Provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each asset's life, and so charges the economic consumption of capital assets as they are used.

The CFR includes any other long term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility by the PFI lease provider and so the Council is not required to separately borrow for these schemes. The Council currently has no such schemes within the CFR.

The Council is asked to approve the CFR projections below:

£m	2018/19 Actual	2019/20 Revised Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
<b>Capital Financing Requirement</b>					
CFR – non housing	0.828	1.986	2.806	3.373	3.380
CFR - housing	68.041	73.065	75.255	75.255	75.255
CFR - commercial activities/non-financial investments	-	-	-	-	-
<b>Total CFR</b>	<b>68.869</b>	<b>75.052</b>	<b>78.061</b>	<b>78.628</b>	<b>78.634</b>
<b>Movement in CFR</b>	<b>(0.057)</b>	<b>6.182</b>	<b>3.010</b>	<b>0.567</b>	<b>0.006</b>

<b>Movement in CFR represented by</b>					
Net financing need for the year (above)	-	6.239	3.116	0.757	0.252
Less MRP/VRP and other financing movements	<b>(0.057)</b>	<b>(0.056)</b>	<b>(0.106)</b>	<b>(0.189)</b>	<b>(0.246)</b>
<b>Movement in CFR</b>	<b>(0.057)</b>	<b>6.182</b>	<b>3.010</b>	<b>0.567</b>	<b>0.006</b>

\* CFR 2017/18 £68.926m

A key aspect of the regulatory and professional guidance is that elected members are aware of the size and scope of any commercial activity in relation to the Council's overall financial position. The capital expenditure figures shown in 2.1 and the details above demonstrate the scope of this activity and, by approving these figures, consider the scale proportionate to the Council's remaining activity.

## 2.3 Core Funds and Expected Investment Balances

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year end balances for each resource and anticipated day to day cash flow balances.

Year End Resources £m	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
Fund Balances/Reserves	35.009	23.861	18.055	14.078	10.205
Capital Receipts	23.409	15.356	6.637	6.774	6.882
Provisions*	1.815	1.815	1.815	1.815	1.815
Other	-	-	-	-	-
<b>Total Core Funds</b>	<b>60.233</b>	<b>41.032</b>	<b>26.507</b>	<b>22.666</b>	<b>18.903</b>
Working Capital**	14.337	12.375	15.691	18.197	20.855
(Under)/Over Borrowing	(5.809)	(11.991)	(15.001)	(15.568)	(15.574)
<b>Expected Investments</b>	<b>68.761</b>	<b>41.415</b>	<b>27.197</b>	<b>25.295</b>	<b>24.184</b>

\* Includes full provision for NNDR appeals

\*\* Working capital balances shown are estimated year end; these may be higher mid year.

## 2.4 Minimum Revenue Provision (MRP) Policy Statement

The Council is required to pay off an element of the accumulated General Fund Capital spend each year (the CFR) through a revenue charge (the Minimum Revenue Provision – MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

MHCLG Regulations have been issued which require the full Council to approve **an MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement:

For Capital Expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will be:

- **Existing practice** - MRP will follow the existing practice outlined in former MHCLG regulations (option 1);

This option provides for an approximate 4% reduction in the borrowing need (CFR) each year.

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

- **Asset Life Method** – MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) (option 3);

This option provides for a reduction in the borrowing need over approximately the asset's life.

There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made (although there are transitional arrangements in place).

Repayments included in annual PFI or finance leases are applied as MRP.

**MRP Overpayments** – a change introduced by the revised MHCLG MRP Guidance was the allowance that any charges made over the statutory minimum revenue provision (MRP), voluntary revenue provision or overpayments, can, if needed, be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. The Council has made no VRP overpayments.

### 3. BORROWING

The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The Treasury Management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's capital strategy. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

#### 3.1 Current Portfolio Position

The overall Treasury Management portfolio as at 31<sup>st</sup> March 2019 and for the position as at 31<sup>st</sup> December 2019 are shown below for both borrowing and investments.

	TREASURY PORTFOLIO			
	ACTUAL AT 31/3/19		CURRENT AT 31/12/19	
	£m	%	£m	%
<b>Treasury Investments</b>				
Banks	50.520	73.47	33.000	47.21
Building Societies	-	-	-	-
Local Authorities	-	-	21.000	30.04
DMADF (H M Treasury)	-	-	-	-
Money Market Funds	4.421	6.43	6.124	8.76
Certificates of Deposit	10.000	14.54	6.002	8.59
<b>Total Managed in-House</b>	<b>64.941</b>	<b>94.445</b>	<b>66.126</b>	<b>94.61</b>
<b>Property Funds</b>	3.820	5.56	3.770	5.39
<b>Total Managed Externally</b>	<b>3.820</b>	<b>5.56</b>	<b>3.770</b>	<b>5.39</b>
<b>Total Treasury Investments</b>	<b>68.761</b>	<b>100</b>	<b>69.896</b>	<b>100</b>
<b>Treasury External Borrowing</b>				
PWLB	63.060	100	63.060	100
<b>Total External Borrowing</b>	<b>63.060</b>	<b>100</b>	<b>63.060</b>	<b>100</b>
<b>Net Treasury Investments/(Borrowing)</b>	<b>5.701</b>		<b>6.836</b>	

The Council's forward projections for borrowing are summarised below. The table shows the actual external debt, against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

<b>Treasury Portfolio</b>	<b>2018/19 Actual £000's</b>	<b>2019/20 Estimate £000's</b>	<b>2020/21 Estimate £000's</b>	<b>2021/22 Estimate £000's</b>	<b>2022/23 Estimate £000's</b>
<b>External Debt</b>					
Debt at 1st April	63.060	63.060	63.060	63.060	63.060
Expected change in Debt	-	-	-	-	-
<b>Actual gross debt at 31st March</b>	<b>63.060</b>	<b>63.060</b>	<b>63.060</b>	<b>63.060</b>	<b>63.060</b>
<b>The Capital Financing Requirement</b>	<b>68.869</b>	<b>75.052</b>	<b>78.061</b>	<b>78.628</b>	<b>78.634</b>
<b>Under / (over) borrowing</b>	<b>5.809</b>	<b>11.991</b>	<b>15.001</b>	<b>15.568</b>	<b>15.574</b>

Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2020/21 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue or speculative purposes.

The Executive Director Finance (the Section 151 Officer) reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

### 3.2. Treasury Indicators: Limits to Borrowing Activity

**The Operational Boundary** - This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

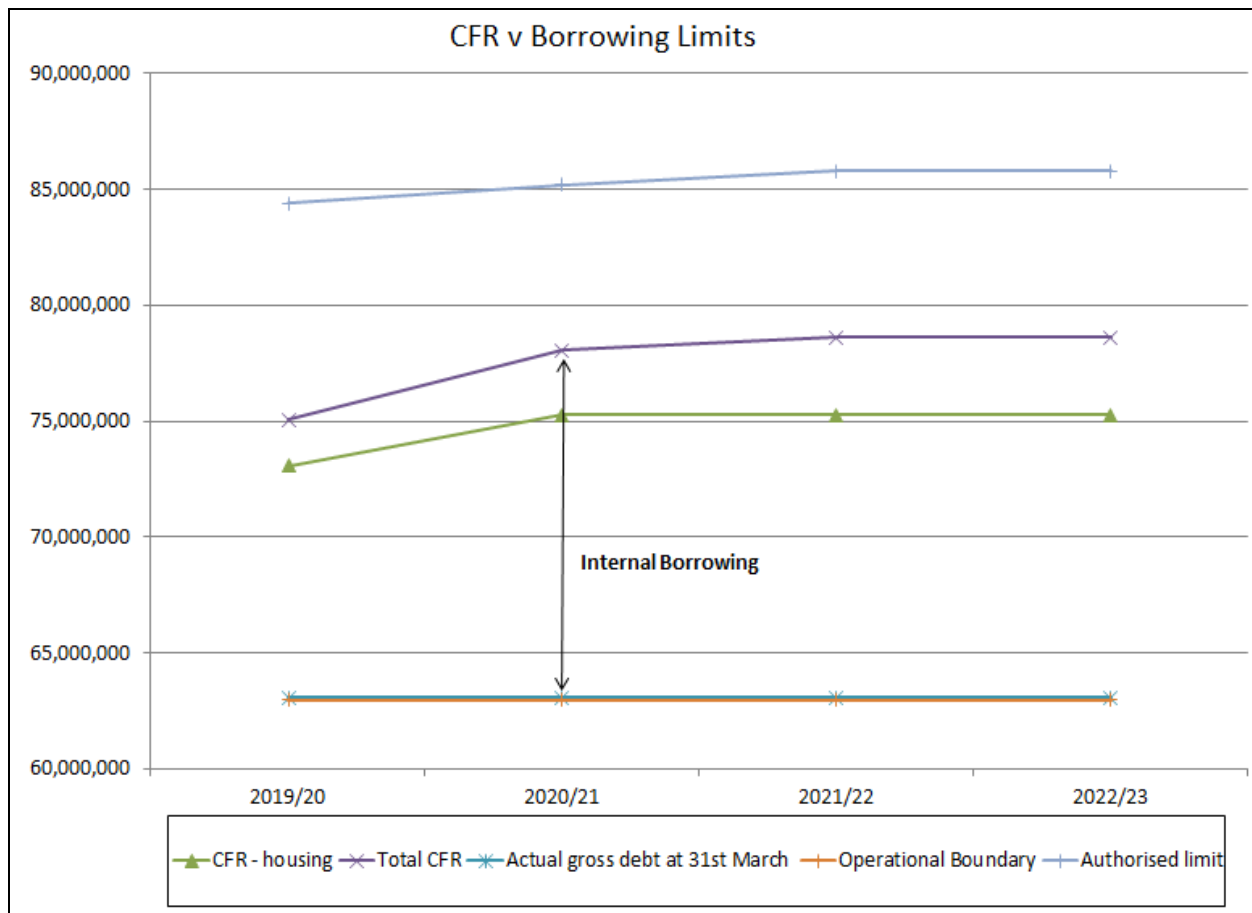
<b>Operational Boundary</b>	<b>2019/20 Estimate £m</b>	<b>2020/21 Estimate £m</b>	<b>2021/22 Estimate £m</b>	<b>2022/23 Estimate £m</b>
Borrowing	63.060	63.060	63.060	63.060
Other long term liabilities	-	-	-	-
Commercial Activities/non-financial Investments	-	-	-	-
<b>Total</b>	<b>63.060</b>	<b>63.060</b>	<b>63.060</b>	<b>63.060</b>

**The Authorised Limit for external debt** – This is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

The Council is asked to approve the following Authorised Limit:

Authorised limit	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m
Borrowing	84.393	85.213	85.780	85.787
<b>Total</b>	<b>84.393</b>	<b>85.213</b>	<b>85.780</b>	<b>85.787</b>



### 3.3. Prospects for Interest Rates

A more detailed interest rate view and economic commentary are at **ANNEXES 2 & 3**.

The Council has appointed Link Asset Services as its Treasury Advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives their central view.

Link Asset Services Interest Rate View													
	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25	1.25	1.25	1.25
3 Month LIBID	0.70	0.70	0.80	0.80	0.90	1.00	1.00	1.10	1.20	1.30	1.30	1.30	1.30
6 Month LIBID	0.80	0.80	0.90	1.00	1.00	1.10	1.20	1.30	1.40	1.50	1.50	1.50	1.50
12 Month LIBID	0.90	0.90	1.00	1.10	1.20	1.30	1.40	1.50	1.60	1.70	1.70	1.70	1.70
5yr PWLB Rate	2.30	2.30	2.40	2.40	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.00	3.10
10yr PWLB Rate	2.50	2.50	2.60	2.60	2.70	2.80	2.90	3.00	3.10	3.10	3.20	3.20	3.30
25yr PWLB Rate	3.00	3.00	3.10	3.20	3.30	3.40	3.50	3.60	3.70	3.80	3.80	3.90	3.90
50yr PWLB Rate	2.90	2.90	3.00	3.10	3.20	3.30	3.40	3.50	3.60	3.70	3.70	3.80	3.80

The above forecasts have been based on an assumption that there is an agreed deal on Brexit, including agreement on the terms of trade between the UK and EU, at some point in time. The result of the general election has removed much uncertainty around this major assumption. However, it does not remove uncertainty around whether agreement can be reached with the EU on a trade deal within the short time to December 2020, as the prime minister has pledged.

2019 was a year of weak UK economic growth as political and Brexit uncertainty depressed confidence. It was therefore little surprise that the Monetary Policy Committee (MPC) left Bank Rate unchanged at 0.75% during the year. However, during January 2020, financial markets were predicting a 50:50 chance of a cut in Bank Rate at the time of the 30 January MPC meeting. Admittedly, there had been plenty of downbeat UK economic news in December and January which showed that all the political uncertainty leading up to the general election, together with uncertainty over where Brexit would be going after that election, had depressed economic growth in quarter 4 of 2019. However, that downbeat news was backward looking; more recent economic statistics and forward-looking business surveys, all pointed in the direction of a robust bounce in economic activity and a recovery of confidence after the decisive result of the general election removed political and Brexit uncertainty. The MPC clearly decided to focus on the more recent forward-looking news, rather than the earlier downbeat news, and so left Bank Rate unchanged. Provided that the forward-looking surveys are borne out in practice in the coming months, and the March Budget delivers with a fiscal boost, then it is expected that Bank Rate will be left unchanged until after the December trade deal deadline. However, the MPC is on alert that if the surveys prove optimistic and/or the Budget disappoints, then they may still take action and cut Bank Rate in order to stimulate growth.

**Bond yields / PWLB rates.** There had been much speculation during 2019 that the bond market had gone into a bubble, as evidenced by high bond prices and remarkably low yields. However, given the context that there have been heightened expectations that the US was heading for a recession in 2020, and a general background of a downturn in world economic

growth, together with inflation generally at low levels in most countries and expected to remain subdued, conditions were ripe for low bond yields. While inflation targeting by the major central banks has been successful over the last thirty years in lowering inflation expectations, the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last thirty years. We have therefore seen over the last year, many bond yields up to ten years in the Eurozone actually turn negative. In addition, there has, at times, been an inversion of bond yields in the US whereby ten-year yields have fallen below shorter-term yields. In the past, this has been a precursor of a recession. The other side of this coin is that bond prices are elevated, as investors would be expected to be moving out of riskier assets i.e. shares, in anticipation of a downturn in corporate earnings and so selling out of equities. However, stock markets are also currently at high levels as some investors have focused on chasing returns in the context of dismal ultra-low interest rates on cash deposits.

During the first half of 2019-20 to 30 September, gilt yields plunged and caused a near halving of longer term PWLB rates to completely unprecedented historic low levels. There is though, an expectation that financial markets have gone too far in their fears about the degree of the downturn in US and world growth. If, as expected, the US only suffers a mild downturn in growth, bond markets in the US are likely to sell off and that would be expected to put upward pressure on bond yields, not only in the US, but also in the UK due to a correlation between US treasuries and UK gilts; at various times this correlation has been strong, but at other times weak. However, forecasting the timing of this, and how strong the correlation is likely to be, is very difficult with any degree of confidence. Changes in UK Bank Rate will also impact on gilt yields.

One potential danger that may be lurking in investor minds is that Japan has become mired in a twenty-year bog of failing to get economic growth and inflation up off the floor, despite a combination of massive monetary and fiscal stimulus by both the central bank and government. Investors could be fretting that this condition might become contagious to other western economies.

Another danger is that unconventional monetary policy post 2008, (ultra-low interest rates plus quantitative easing), may end up doing more harm than good through prolonged use. Low interest rates have encouraged a debt-fuelled boom that now makes it harder for central banks to raise interest rates. Negative interest rates could damage the profitability of commercial banks and so impair their ability to lend and / or push them into riskier lending. Banks could also end up holding large amounts of their government's bonds and so create a potential doom loop. (A doom loop would occur where the credit rating of the debt of a nation was downgraded which would cause bond prices to fall, causing losses on debt portfolios held by banks and insurers, so reducing their capital and forcing them to sell bonds – which, in turn, would cause further falls in their prices etc.). In addition, the financial viability of pension funds could be damaged by low yields on holdings of bonds.

The overall longer run future trend is for gilt yields, and consequently PWLB rates, to rise, albeit gently. From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and sharp changes in investor sentiment. Such volatility could occur at any time during the forecast period.

In addition, PWLB rates are subject to ad hoc decisions by **H.M. Treasury** to change the margin over gilt yields charged in PWLB rates: such changes could be up or down. It is not clear that if gilt yields were to rise back up again by over 100bps within the next year or so, whether H M Treasury would remove the extra 100 bps margin implemented on 9.10.19.

Economic and interest rate forecasting remains difficult with so many influences weighing on UK gilt yields and PWLB rates. The above forecasts, (and MPC decisions), will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

### **Investment and borrowing rates**

- Investment returns are likely to remain low during 2020/21 with little increase in the following two years. However, if major progress was made with an agreed Brexit, then there is upside potential for earnings.
- Borrowing interest rates were on a major falling trend during the first half of 2019-20 but then jumped up by 100 bps on 9.10.19. The policy of avoiding new borrowing by running down spare cash balances has served local authorities well over the last few years. However, the unexpected increase of 100 bps in PWLB rates requires a major rethink of local authority treasury management strategy and risk management. As Link Asset Services' long-term forecast for Bank Rate is 2.25%, and all PWLB certainty rates are close to or above 2.25%, there is little value in borrowing from the PWLB at present. Accordingly, the Council will reassess its risk appetite in terms of either seeking cheaper alternative sources of borrowing or switching to short term borrowing in the money markets until such time as the Government might possibly reconsider the margins charged over gilt yields. Longer term borrowing could also be undertaken for the purpose of certainty, where that is desirable, or for flattening the profile of a heavily unbalanced maturity profile.
- While this Council will not be able to avoid borrowing to finance new capital expenditure, there will be a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new short or medium-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.



### **3.4 Borrowing Strategy**

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

Against this background and the risks within the economic forecast, caution will be adopted with the 2020/21 treasury operations. The Executive Director Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- \* *if it was felt that there was a significant risk of a sharp FALL in borrowing rates (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then borrowing will be postponed.*
- \* *if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast, perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.*

Any decisions will be reported to Council at the next available opportunity.

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

The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

### **3.6. Debt Rescheduling**

Rescheduling of current borrowing in our debt portfolio is unlikely to occur as the 100 bps increase in PWLB rates only applied to new borrowing rates and not to premature debt repayment rates. If rescheduling was done, it will be reported to the Council at the earliest meeting following its action.

### **3.7 New Financial Institutions as a Source of Borrowing**

Following the decision by the PWLB on 9 October 2019 to increase their margin over gilt yields by 100 bps to 180 basis points on loans lent to local authorities, consideration will also need to be given to sourcing funding at cheaper rates from the following:

- Local authorities (primarily shorter dated maturities)
- Financial institutions (primarily insurance companies and pension funds but also some banks, out of spot or forward dates)
- Municipal Bonds Agency

The degree which any of these options proves cheaper than PWLB Certainty Rate is still evolving at the time of writing but our advisors will keep us informed.

### 3.8 Approved Sources of Long and Short term Borrowing

<b>On Balance Sheet</b>	<b>Fixed</b>	<b>Variable</b>
PWLB	●	●
Municipal bond agency	●	●
Local authorities	●	●
Banks	●	●
Pension funds	●	●
Insurance companies	●	●
Market (long-term)	●	●
Market (temporary)	●	●
Market (LOBOs)	●	●
Stock issues	●	●
Local temporary	●	●
Local Bonds	●	
Local authority bills	●	●
Overdraft		●
Negotiable Bonds	●	●
Internal (capital receipts & revenue balances)	●	●
Commercial Paper	●	
Medium Term Notes	●	
Finance leases	●	●

## 4. ANNUAL INVESTMENT STRATEGY

### 4.1 Investment Policy – Management of Risk

The MHCLG and CIPFA have extended the meaning of ‘investments’ to include both financial and non-financial investments. This report deals solely with financial investments (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy.

The Council’s investment policy has regard to the following:-

- MHCLG’s Guidance on Local Government Investments (“the Guidance”)
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 (“the Code”)
- CIPFA Treasury Management Guidance Notes 2018

The Council’s investment priorities will be security first, portfolio liquidity second, and then yield (return).

The above guidance from the MHCLG and CIPFA places a high priority on the management of risk. This Council has adopted a prudent approach to managing risk and defines its risk appetite by the following means:-

- 1) Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.
- 2) **Other Information:** Ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as “credit default swaps” and overlay that information on top of the credit ratings.
- 3) **Other information sources** used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.
- 4) This Council has defined the list of **types of investment instruments** that the Treasury Management team, are authorised to use. There are two lists in Annex 4 under the categories of ‘specified’ and ‘non-specified’ investments.
  - a) **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.

- b) **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use. Once an investment is classed as non-specified, it remains non-specified all the way through to maturity ie an 18 month deposit would still be non-specified even if it has only 11 months left until maturity.
- 5) **Non-specified investments limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being 25% of the total investment portfolio (see paragraph 4.3)
- 6) **Lending limits** (amounts and maturity) for each counterparty will be set though applying the matrix table in paragraph 4.2
- 7) **Transaction limits** are set for each type of investment in 4.2
- 8) This Council will set a limit for the amount of its investments which are invested for **longer than 365 days** (see paragraph 4.4)
- 9) Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating** (see paragraph 4.3)
- 10) This Council has engaged **external consultants** (see paragraph 1.5) to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this Council in the context of the expected level of cash balances and need for liquidity throughout the year.
- 11) All investments will be denominated in **sterling**.
- 12) As a result of the change in accounting standards for 2019/20 under IFRS 9, this Council will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. In November 2018, MHCLG concluded consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years commencing 1<sup>st</sup> April 2018.

This Council will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance (see paragraph 4.5). Regular monitoring of investment performance will be carried out during the year.

**Changes in risk management policy from last year.** The above criteria are unchanged from last year.

#### **4.2 Creditworthiness Policy**

This Council applies the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- 'watches' and 'outlooks' from credit rating agencies;

- CDS spreads that may give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, and any assigned watches and outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads. The end product of this is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands:

- Yellow 5 years \*
- Dark pink 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.25
- Light pink 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.5
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 100 days
- No colour not to be used

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour

The Link Asset Services' creditworthiness service uses a wider array of information other than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

Typically the minimum credit ratings criteria the Council uses will be a short term rating (Fitch or equivalents) of F1 and a Long Term rating of A -. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored on a daily basis/as and when notified. The Council is alerted to changes to ratings of all three agencies through its use of the Link Asset Services' creditworthiness service:

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately;
- in addition to the use of credit ratings the Council will be advised of information in movements in Credit Default Swap spreads against the iTraxx European Financials benchmark and other market data on a daily basis via its Passport website, provided

exclusively to it by Link Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information, as well as information on any external support for banks, to help support its decision making process.

<b>Counterparty</b>	<b>Colour (and long term rating where applicable)</b>	<b>Money and/or % Limit</b>	<b>Time Limit</b>
<b>Banks/Building Societies *</b>	<b>Yellow</b>	<b>£10m</b>	<b>5yrs</b>
<b>Banks/Building Societies</b>	<b>Purple</b>	<b>£10m</b>	<b>2 yrs</b>
<b>Banks/Building Societies</b>	<b>Orange</b>	<b>£10m</b>	<b>1 yr</b>
<b>Banks – part nationalised</b>	<b>Blue</b>	<b>£10m</b>	<b>1 yr</b>
<b>Banks/Building Societies</b>	<b>Red</b>	<b>£10m</b>	<b>6 mths</b>
<b>Banks/Building Societies</b>	<b>green</b>	<b>£10m</b>	<b>100 days</b>
<b>Banks/Building Societies</b>	<b>No colour</b>	<b>Not to be used</b>	
<b>Council's banker (where "No Colour")</b>	<b>No colour</b>	<b>£2m</b>	<b>1 day</b>
<b>DMADF</b>	<b>UK sovereign rating</b>	<b>£10m</b>	<b>6 months</b>
<b>Local authorities</b>	<b>n/a</b>	<b>£10m</b>	<b>5yrs</b>
	<b>Fund Rating **</b>	<b>Money and/or % Limit</b>	<b>Time Limit</b>
<b>Money Market Funds CNAV</b>	<b>AAA</b>	<b>£10m</b>	<b>Liquid</b>
<b>Money Market Funds LVNAV</b>	<b>AAA</b>	<b>£10m</b>	<b>Liquid</b>
<b>Money Market Funds VNAV</b>	<b>AAA</b>	<b>£10m</b>	<b>Liquid</b>

*\* The yellow colour category is for UK Government debt, or its equivalent, money market funds and collateralised deposits where the collateral is UK Government debt – see Annex 4.*

*\*\* 'Fund' ratings are different to individual counterparty ratings, coming under either specific 'MMF' or 'Bond Fund' rating criteria.*

## **UK banks – ring fencing**

The largest UK banks, (those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits), are required, by UK law, to separate core retail banking services from their investment and international banking activities by 1st January 2019. This is known as “ring-fencing”. Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up. Several banks are very close to the threshold already and so may come into scope in the future regardless.

Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and SME deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler activities offered from within a ring-fenced bank (RFB), will be focused on lower risk, day-to-day core transactions, whilst more complex and “riskier” activities are required to be housed in a separate entity, a non-ring-fenced bank (NRFB). This is intended to ensure that an entity’s core activities are not adversely affected by the acts or omissions of other members of its group.

While the structure of the banks included within this process may have changed, the fundamentals of credit assessment have not. The Council will continue to assess the new-formed entities in the same way that it does others and those with sufficiently high ratings, (and any other metrics considered), will be considered for investment purposes.

## **4.3 Country Limits**

Due care will be taken to consider the exposure of the Council’s total investment portfolio to non-specified investments, countries, groups and sectors.

- a) **Non-specified investment limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being 25% of the total investment portfolio.
- b) **Country limit.** The Council has determined that it will only use approved counterparties from the UK and from countries with a minimum sovereign credit rating of ‘AA-’ from Fitch. The list of countries that qualify using this credit criteria as at the date of this report are shown in Annex 5. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.
- c) **Other limits. In addition:-**
  - no more than 25% will be placed with any non-UK country at any time;
  - a limit of £14m per group will apply to a group of companies;
  - sector limits will be monitored regularly for appropriateness.

## 4.4 Investment Strategy

**In-house funds.** Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. While most cash balances are required in order to manage the ups and downs of cash flows, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed.

- If it is thought that Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments as being short term or variable.
- Conversely, if it is thought that Bank Rate is likely to fall within that time period, consideration will be given to locking in higher rates currently obtainable, for longer periods.

### Investment Returns Expectations.

On the assumption that the UK and EU agree a Brexit deal including the terms of trade by the end of 2020 or soon after, then Bank Rate is forecast to increase only slowly over the next few years to reach 1.25% by quarter 1 2023. Bank Rate forecasts for financial year ends (March) are:

- Q1 2021 0.75%
- Q1 2022 1.00%
- Q1 2023 1.25%

The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows:

2019/20	0.75%
2020/21	0.75%
2021/22	1.00%
2022/23	1.25%
2023/24	1.50%
2024/25	1.75%
Later years	2.25%

- The overall balance of risks to economic growth in the UK is probably relatively even due to the weight of all the uncertainties over post-Brexit trade arrangements and the impact of an expansionary government spending policy (as expected in the Budget on 11<sup>th</sup> March).
- The balance of risks to increases or decreases in Bank Rate and shorter term PWLB rates are also broadly even.



**Investment Treasury Indicator and Limit** - total principal funds invested for greater than 365 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

The Council is asked to approve the treasury indicator and limit: -

<b>Upper limit for principal sums invested for longer than 365 days</b>			
	<b>2020/21 £m</b>	<b>2021/22 £m</b>	<b>2022/23 £m</b>
Principal sums invested > 365 days	6.799	6.324	6.046
Current investments as at 31.12.19 in excess of 1 year maturing in each year	5.000	-	-

For its cash flow generated balances, the Council will seek to utilise its business reserve instant access and notice accounts, money market funds and short-dated deposits (overnight to 100 days) in order to benefit from the compounding of interest.

#### **4.5 Investment Risk Benchmarking**

This Council will use an investment benchmark to assess the investment performance of its investment portfolio of 3 month LIBID.

#### **4.6 End of year investment report**

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

## 5. ANNEXES

1. Prudential and Treasury Indicators
2. Interest Rate Forecasts
3. Economic Background
4. TMP 1 Credit & Counterparty Risk Management
5. Approved Countries for investments
6. Treasury Management Scheme of Delegation
7. The Treasury Management Role of the Section 151 Officer
8. Treasury Management Practices
9. Treasury Management Glossary of Terms
10. Prudential Indicators – Definitions/Interpretation

## ANNEX 1

### THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2020/21 – 2022/23

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

#### 1 Capital expenditure

A breakdown of capital expenditure by Directorate is detailed within the Performance Healthcheck reported quarterly to Cabinet.

#### 2 Affordability Prudential Indicators

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators:

##### a) Ratio of financing costs to net revenue stream.

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream (net cost of services).

Ratio of financing costs to net revenue stream.	2018/19 Actual %	2019/20 Estimate %	2020/21 Estimate %	2021/22 Estimate %	2022/23 Estimate %
Non-HRA	(5.42)%	(5.82)%	(2.17)%	(0.84)%	(1.43)%
HRA	29.17%	29.10%	28.24%	27.21%	26.38%
Commercial Activities / non-financial Investments	(2.60)%	(2.71)%	(4.44)%	(6.45)%	(6.16)%

The estimates of financing costs include current commitments and the proposals in this budget report.

Commercial Activities/non-Financial Investments includes investments in property funds and the return on the Gungate Site purchase.

## b) Housing Revenue Account Debt Ratios

HRA Debt to Revenues Ratio	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
HRA Debt £m	68.041	73.065	75.255	75.255	75.255
HRA Revenues £m	18.046	18.006	18.783	19.411	19.883
Ratio of Debt to Revenues %	377	406	401	388	378

HRA Debt per Dwelling	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
HRA Debt £m	68.041	73.065	75.255	75.255	75.255
Number of HRA Dwellings	4,206	4,160	4,120	4,090	4,060
Debt per Dwelling £'000	16.177	17.564	18.266	18.400	18.536

## 4 Maturity Structure of Borrowing

These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

The Council is asked to approve the following treasury indicators and limits:

<b>Maturity structure of Fixed Interest Rate borrowing 2020/21</b>		
Timeline	Lower	Upper
Under 12 months	0%	20%
12 months to 2 years	0%	20%
2 years to 5 years	0%	25%
5 years to 10 years	0%	75%
10 years and above	0%	100%

<b>Maturity structure of Variable Interest Rate borrowing 2020/21</b>		
Timeline	Lower	Upper
Under 12 months	0%	20%
12 months to 2 years	0%	20%
2 years to 5 years	0%	25%
5 years to 10 years	0%	75%
10 years and above	0%	100%

## 5. Control of Interest Rate Exposure

Please see paragraphs 3.3, 3.4 and 4.4

## ANNEX 2 Interest Rate Forecasts 2020 – 2023

PWLB rates and forecast shown below have taken into account the 20 basis point certainty rate reduction effective as of the 1st November 2012.

Link Asset Services Interest Rate View													
	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25	1.25	1.25	1.25
3 Month LIBID	0.70	0.70	0.80	0.80	0.90	1.00	1.00	1.10	1.20	1.30	1.30	1.30	1.30
6 Month LIBID	0.80	0.80	0.90	1.00	1.00	1.10	1.20	1.30	1.40	1.50	1.50	1.50	1.50
12 Month LIBID	0.90	0.90	1.00	1.10	1.20	1.30	1.40	1.50	1.60	1.70	1.70	1.70	1.70
5yr PWLB Rate	2.30	2.30	2.40	2.40	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.00	3.10
10yr PWLB Rate	2.50	2.50	2.60	2.60	2.70	2.80	2.90	3.00	3.10	3.10	3.20	3.20	3.30
25yr PWLB Rate	3.00	3.00	3.10	3.20	3.30	3.40	3.50	3.60	3.70	3.80	3.80	3.90	3.90
50yr PWLB Rate	2.90	2.90	3.00	3.10	3.20	3.30	3.40	3.50	3.60	3.70	3.70	3.80	3.80
<b>Bank Rate</b>													
Link Asset Services	0.75%	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.25%
Capital Economics	0.75%	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	-	-	-	-	-
<b>5yr PWLB Rate</b>													
Link Asset Services	2.30%	2.30%	2.40%	2.40%	2.50%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%
Capital Economics	2.40%	2.50%	2.50%	2.60%	2.60%	2.80%	2.80%	2.90%	-	-	-	-	-
<b>10yr PWLB Rate</b>													
Link Asset Services	2.50%	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%
Capital Economics	2.70%	2.70%	2.80%	2.80%	2.90%	3.00%	3.00%	3.10%	-	-	-	-	-
<b>25yr PWLB Rate</b>													
Link Asset Services	3.00%	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%	3.60%	3.70%	3.80%	3.80%	3.90%	3.90%
Capital Economics	3.10%	3.10%	3.20%	3.20%	3.20%	3.30%	3.30%	3.40%	-	-	-	-	-
<b>50yr PWLB Rate</b>													
Link Asset Services	2.90%	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%	3.60%	3.70%	3.70%	3.80%	3.80%
Capital Economics	3.10%	3.10%	3.20%	3.20%	3.30%	3.40%	3.40%	3.50%	-	-	-	-	-

## ANNEX 3 ECONOMIC BACKGROUND

**UK. Brexit.** 2019 was a year of upheaval on the political front as Theresa May resigned as Prime Minister to be replaced by Boris Johnson on a platform of the UK leaving the EU on 31 October 2019, with or without a deal. However, MPs blocked leaving on that date and the EU agreed an extension to 31 January 2020. In late October, MPs approved an outline of a Brexit deal to enable the UK to leave the EU on 31 January. The Conservative Government gained a large overall majority in the **general election** on 12 December; this ensured that the UK left the EU on 31 January. However, there will still be much uncertainty as the detail of a comprehensive trade deal will need to be negotiated by the current end of the transition period in December 2020, which the Prime Minister has pledged he will not extend. This could prove to be an unrealistically short timetable for such major negotiations that leaves open three possibilities; a partial agreement on many areas of agreement and then continuing negotiations to deal with the residual areas, the need for the target date to be put back, probably two years, or, a no deal Brexit in December 2020.

**GDP growth took** a big hit from both political and Brexit uncertainty during 2019; quarter three 2019 surprised on the upside by coming in at +0.4% q/q, +1.1% y/y. However, the peak of Brexit uncertainty during the final quarter appears to have suppressed quarterly growth to probably around zero. The forward-looking surveys in January have indicated that there could be a significant recovery of growth now that much uncertainty has gone. Nevertheless, economic growth may only come in at about 1% in 2020, pending the outcome of negotiations on a trade deal. Provided there is a satisfactory resolution of those negotiations, which are in both the EU's and UK's interest, then growth should strengthen further in 2021.

At its 30 January meeting, the Monetary Policy Committee held Bank Rate unchanged at 0.75%. The vote was again split 7-2, with two votes for a cut to 0.50%. The financial markets had been predicting a 50:50 chance of a rate cut at the time of the meeting. Admittedly, there had been plenty of downbeat UK economic news in December and January which showed that all the political uncertainty leading up to the general election, together with uncertainty over where Brexit would be going after the election, had depressed economic growth in quarter 4. In addition, three members of the MPC had made speeches in January which were distinctly on the dovish side, flagging up their concerns over weak growth and low inflation; as there were two other members of the MPC who voted for a rate cut in November, five would be a majority at the January MPC meeting if those three followed through on their concerns.

However, that downbeat news was backward looking; more recent economic statistics and forward-looking business surveys, have all pointed in the direction of a robust bounce in economic activity and a recovery of confidence after the decisive result of the general election removed political and immediate Brexit uncertainty. In addition, the September spending round increases in expenditure will start kicking in from April 2020, while the Budget in March is widely expected to include a substantial fiscal boost by further increases in expenditure, especially on infrastructure. The Bank of England cut its forecasts for growth from 1.2% to 0.8% for 2020, and from 1.8% to 1.4% for 2021. However, these forecasts could not include any allowance for the predicted fiscal boost in the March Budget. Overall, the MPC clearly decided to focus on the more recent forward-looking news than the earlier downbeat news.

The quarterly Monetary Policy Report did, though, flag up that there was still a risk of a Bank Rate cut; "Policy may need to reinforce the expected recovery in UK GDP growth should the more positive signals from recent indicators of global and domestic activity not be sustained or should indicators of domestic prices remain relatively weak." Obviously, if trade negotiations

with the EU failed to make satisfactory progress, this could dampen confidence and growth. On the other hand, there was also a warning in the other direction, that if growth were to pick up strongly, as suggested by recent business surveys, then "some modest tightening" of policy might be needed further ahead. It was therefore notable that the Bank had dropped its phrase that tightening would be "limited and gradual", a long-standing piece of forward guidance; this gives the MPC more room to raise Bank Rate more quickly if growth was to surge and, in turn, lead to a surge in inflation above the 2% target rate.

As for **inflation** itself, CPI has been hovering around the Bank of England's target of 2% during 2019, but fell again in both October and November to a three-year low of 1.5% and then even further to 1.3% in December. It is likely to remain close to or under 2% over the next two years and so, it does not pose any immediate concern to the MPC at the current time. However, if there was a hard or no deal Brexit, inflation could rise towards 4%, primarily because of imported inflation on the back of a weakening pound.

With regard to the **labour market**, growth in numbers employed has been quite resilient through 2019 until the three months to September, where it fell by 58,000. However, there was an encouraging pick up again in the three months to October to growth of 24,000 and then a stunning increase of 208,000 in the three months to November. The unemployment rate held steady at a 44-year low of 3.8% on the Independent Labour Organisation measure. Wage inflation has been steadily falling from a high point of 3.9% in July to 3.4% in November (3-month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates higher than CPI inflation), earnings grew by about 2.1%. As the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. The other message from the fall in wage growth is that employers are beginning to find it easier to hire suitable staff, indicating that supply pressure in the labour market is easing.

**Coronavirus.** The recent Coronavirus outbreak could cause disruption to the economies of affected nations. The Chinese economy is now very much bigger than it was at the time of the SARS outbreak in 2003 and far more integrated into world supply chains. However, a temporary dip in Chinese growth could lead to a catch up of lost production in following quarters with minimal net overall effect over a period of a year. However, no one knows quite how big an impact this virus will have around the world; hopefully, the efforts of the WHO and the Chinese authorities will ensure that the current level of infection does not multiply greatly.

**USA.** After growth of 2.9% y/y in 2018 fuelled by President Trump's massive easing of fiscal policy, growth has weakened in 2019. After a strong start in quarter 1 at 3.1%, (annualised rate), it fell to 2.0% in quarter 2 and then 2.1% in quarters 3 and 4. This left the rate for 2019 as a whole at 2.3%, a slowdown from 2018 but not the precursor of a recession which financial markets had been fearing earlier in the year. Forward indicators are currently indicating that growth is likely to strengthen somewhat moving forward into 2020.

**The Fed** finished its series of increases in rates to 2.25 – 2.50% in December 2018. In July 2019, it cut rates by 0.25% as a 'midterm adjustment'. It also ended its programme of quantitative tightening in August 2019, (reducing its holdings of treasuries etc.). It then cut rates by 0.25% again in September and by another 0.25% in its October meeting to 1.50 – 1.75%. It left rates unchanged at its December meeting. Rates were again left unchanged at its end of January meeting although it had been thought that as the yield curve on Treasuries had been close to inverting again, (with 10 year yields nearly falling below 2 year yields - this is often viewed as being a potential indicator of impending recession), that the Fed could have

cut rates, especially in view of the threat posed by the coronavirus. However, it acknowledged that coronavirus was a threat of economic disruption but was not serious at the current time for the USA. In addition, the phase 1 trade deal with China is supportive of growth. The Fed though, does have an issue that despite reasonably strong growth rates, its inflation rate has stubbornly refused to rise to its preferred core inflation target of 2%; it came in at 1.6% in December. It is therefore unlikely to be raising rates in the near term. It is also committed to reviewing its approach to monetary policy by midyear 2020; this may include a move to inflation targeting becoming an average figure of 2% so as to allow more flexibility for inflation to under and over shoot.

**“The NEW NORMAL.”** The Fed chairman has given an overview of the current big picture of the economy by summing it up as **A NEW NORMAL OF LOW INTEREST RATES, LOW INFLATION AND PROBABLY LOWER GROWTH.** This is indeed an affliction that has mired Japan for the last two decades despite strenuous efforts to stimulate growth and inflation by copious amounts of fiscal stimulus and cutting rates to zero. China and the EU are currently facing the same difficulty to trying to get inflation and growth up. Our own MPC may well have growing concerns and one MPC member specifically warned on the potential for a low inflation trap in January.

It is also worth noting that no less than a quarter of total world sovereign debt is now yielding negative returns.

**EUROZONE. Growth** has been slowing from +1.8% during 2018 to nearly half of that in 2019. Growth was +0.4% q/q in quarter 1, +0.2% q/q in quarters 2 and 3; it then fell to +0.1% in quarter 4 for a total overall growth rate of only 1.0% in 2019. Recovery from quarter 4 is expected to be slow and gradual. German GDP growth has been struggling to stay in positive territory in 2019 and grew by only 0.6% in 2019, with quarter 4 potentially being a negative number. Germany would be particularly vulnerable to a no deal Brexit depressing exports further and if President Trump imposes tariffs on EU produced cars.

**The European Central Bank (ECB)** ended its programme of quantitative easing purchases of debt in December 2018, which then meant that the central banks in the US, UK and EU had all ended the phase of post financial crisis expansion of liquidity supporting world financial markets by quantitative easing purchases of debt. However, the downturn in EZ growth in the second half of 2018 and in 2019, together with inflation falling well under the upper limit of its target range of 0 to 2%, (but it aims to keep it near to 2%), has prompted the ECB to take new measures to stimulate growth. At its March 2019 meeting, it said that it expected to leave interest rates at their present levels “at least through to the end of 2019”, but that was of little help to boosting growth in the near term. Consequently, it announced a **third round of TLTROs**; this provides banks with cheap borrowing every three months from September 2019 until March 2021 that means that, although they would have only a two-year maturity, the Bank was making funds available until 2023, two years later than under its previous policy. As with the last round, the new TLTROs will include an incentive to encourage bank lending, and they will be capped at 30% of a bank’s eligible loans. However, since then, the downturn in EZ and world growth has gathered momentum; at its meeting on 12 September, it cut its deposit rate further into negative territory, from -0.4% to -0.5%, and announced a **resumption of quantitative easing purchases of debt for an unlimited period.** At its October meeting it said these purchases would start in November at €20bn per month - a relatively small amount compared to the previous buying programme. It also increased the maturity of the third round of TLTROs from two to three years. However, it is doubtful whether this loosening of monetary policy will have much impact on growth and, unsurprisingly, the ECB stated that governments



would need to help stimulate growth by 'growth friendly' fiscal policy. There have been no changes in rates or monetary policy since October. In January, the ECB warned that the economic outlook was 'tilted to the downside' and repeated previous requests for governments to do more to stimulate growth by increasing national spending. The new President of the ECB, Christine Lagarde, who took over in December, also stated that a year long review of monetary policy, including the price stability target, would be conducted by the ECB.

On the political front, Austria, Spain and Italy have been in the throes of **forming coalition governments** with some unlikely combinations of parties i.e. this raises questions around their likely endurance. The most recent results of German state elections has put further pressure on the frail German CDU/SDP coalition government and on the current leadership of the CDU.

**CHINA.** Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and shadow banking systems. In addition, there still needs to be a greater switch from investment in industrial capacity, property construction and infrastructure to consumer goods production.

**JAPAN** - has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.

**WORLD GROWTH.** Until recent years, world growth has been boosted by increasing **globalisation** i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last thirty years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy. The Chinese government has targeted achieving major world positions in specific key sectors and products, especially high tech areas and production of rare earth minerals used in high tech products. It is achieving this by massive financial support, (i.e. subsidies), to state owned firms, government directions to other firms, technology theft, restrictions on market access by foreign firms and informal targets for the domestic market share of Chinese producers in the selected sectors. This is regarded as being unfair competition that is putting western firms at an unfair disadvantage or even putting some out of business. It is also regarded with suspicion on the political front as China is an authoritarian country that is not averse to using economic and military power for political advantage. The current trade war between the US and China therefore needs to be seen against that backdrop. It is, therefore, likely that we are heading into a period where there will be a **reversal of world globalisation and a decoupling of western countries** from dependence on China to supply products. This is likely to produce a backdrop in the coming years of weak global growth and so weak inflation. **Central banks are, therefore, likely to come under more pressure to support growth by looser monetary policy measures and this will militate against central banks increasing interest rates.**

The trade war between the US and China is a major concern to **financial markets** due to the synchronised general weakening of growth in the major economies of the world, compounded by fears that there could even be a recession looming up in the US, though this is probably overblown. These concerns resulted in **government bond yields** in the developed world falling significantly during 2019. If there were a major worldwide downturn in growth, central

banks in most of the major economies will have limited ammunition available, in terms of monetary policy measures, when rates are already very low in most countries, (apart from the US). There are also concerns about how much distortion of financial markets has already occurred with the current levels of quantitative easing purchases of debt by central banks and the use of negative central bank rates in some countries.

## INTEREST RATE FORECASTS

The interest rate forecasts provided by Link Asset Services in paragraph 3.3 are **predicated on an assumption of an agreement being reached on Brexit between the UK and the EU**. On this basis, while GDP growth is likely to be subdued in 2019 and 2020 due to all the uncertainties around Brexit depressing consumer and business confidence, an agreement on the detailed terms of a trade deal is likely to lead to a boost to the rate of growth in subsequent years. This could, in turn, increase inflationary pressures in the economy and so cause the Bank of England to resume a series of gentle increases in Bank Rate. Just how fast, and how far, those increases will occur and rise to, will be data dependent. The forecasts in this report assume a modest recovery in the rate and timing of stronger growth and in the corresponding response by the Bank in raising rates.

- In the event of an **orderly non-agreement exit in December 2020**, it is likely that the Bank of England would take action to cut Bank Rate from 0.75% in order to help economic growth deal with the adverse effects of this situation. This is also likely to cause short to medium term gilt yields to fall.
- If there were a **disorderly Brexit**, then any cut in Bank Rate would be likely to last for a longer period and also depress short and medium gilt yields correspondingly. Quantitative easing could also be restarted by the Bank of England. It is also possible that the government could act to protect economic growth by implementing fiscal stimulus.

### The balance of risks to the UK

- The overall balance of risks to economic growth in the UK is probably relatively even due to the weight of all the uncertainties over post-Brexit trade arrangements and the impact of an expansionary government spending policy (as expected in the Budget on 11th March).
- The balance of risks to increases or decreases in Bank Rate and shorter term PWLB rates are also broadly even.

One risk that is both an upside and downside risk, is that all central banks are now working in very different economic conditions than before the 2008 financial crash as there has been a major increase in consumer and other debt due to the exceptionally low levels of borrowing rates that have prevailed since 2008. This means that the neutral rate of interest in an economy, (i.e. the rate that is neither expansionary nor deflationary), is difficult to determine definitively in this new environment, although central banks have made statements that they expect it to be much lower than before 2008. Central banks could therefore either over or under do increases in central interest rates.

## Downside risks to current forecasts for UK gilt yields and PwLB rates currently include:

- **Post Brexit trade negotiations** – if it were to cause significant economic disruption and a major downturn in the rate of growth.
- **Bank of England** takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- A resurgence of the **Eurozone sovereign debt crisis**. In 2018, Italy was a major concern due to having a populist coalition government which made a lot of anti-austerity and anti-EU noise. However, in September 2019 there was a major change in the coalition governing Italy which has brought to power a much more EU friendly government; this has eased the pressure on Italian bonds. Only time will tell whether this new coalition based on an unlikely alliance of two very different parties will endure.
- Weak capitalisation of some **European banks**, particularly Italian banks.
- **German minority government**. In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. The CDU has done badly in recent state elections but the SPD has done particularly badly and this has raised a major question mark over continuing to support the CDU. Angela Merkel has stepped down from being the CDU party leader but she intends to remain as Chancellor until 2021.
- **Other minority EU governments**. Austria, Finland, Sweden, Spain, Portugal, Netherlands and Belgium also have vulnerable minority governments dependent on coalitions which could prove fragile.
- **Austria, the Czech Republic, Poland and Hungary** now form a strongly anti-immigration bloc within the EU. There has also been rising anti-immigration sentiment in Germany and France.
- In October 2019, the IMF issued a report on the World Economic Outlook which flagged up a synchronised slowdown in world growth. However, it also flagged up that there was **potential for a rerun of the 2008 financial crisis**, but this time centred on the huge debt binge accumulated by corporations during the decade of low interest rates. This now means that there are corporates who would be unable to cover basic interest costs on **some \$19trn of corporate debt in major western economies**, if world growth was to dip further than just a minor cooling. This debt is mainly held by the shadow banking sector i.e. pension funds, insurers, hedge funds, asset managers etc., who, when there is \$15trn of corporate and government debt now yielding negative interest rates, have been searching for higher returns in riskier assets. Much of this debt is only marginally above investment grade so any rating downgrade could force some holders into a fire sale, which would then depress prices further and so set off a spiral down. The IMF's answer is to suggest imposing higher capital charges on lending to corporates and for central banks to regulate the investment operations of the shadow banking sector. In October 2019, the deputy Governor of the Bank of England also flagged up the dangers of banks and the shadow banking sector lending to corporates, especially highly leveraged corporates, which had risen back up to near pre-2008 levels.
- **Geopolitical risks**, for example in North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.

## Upside risks to current forecasts for UK gilt yields and PWLB rates

- **Brexit** – if a comprehensive agreement on a trade deal was reached that removed all threats of economic and political disruption between the EU and the UK.
- The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.
- **UK inflation**, whether domestically generated or imported, returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

## **ANNEX 4 TREASURY MANAGEMENT PRACTICE (TMP1) CREDIT AND COUNTERPARTY RISK MANAGEMENT**

**SPECIFIED INVESTMENTS:** All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum ‘high’ quality criteria where applicable.

**NON-SPECIFIED INVESTMENTS:** These are any investments which do not meet the specified investment criteria. A maximum of 25% will be held in aggregate in non-specified investments.

A variety of investment instruments will be used, subject to the credit quality of the institution, and, depending on the type of investment made, it will fall into one of the above categories.

The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

<b>Counterparty</b>	<b>Minimum credit criteria / colour band</b>	<b>£ limit per institution</b>	<b>Max. maturity period</b>
DMADF – UK Government	Yellow	£10m	6 months (max is set by the DMO*)
UK Government gilts	Yellow	£10m	5 years
UK Government Treasury bills	Yellow	£10m	364 days (max is set by the DMO*)
Bonds issued by multilateral development banks	Yellow	£10m	5 years
Money Market Funds CNAV	AAA	£10m	Liquid
Money Market Funds LVNAV	AAA	£10m	Liquid
Money Market Funds VNAV	AAA	£10m	Liquid
Local authorities	Yellow	£10m	5 years
Term deposits with banks and building societies	Blue	£10m	12 months
	Orange		12 months
	Red		6 months
	Green		100 days

Counterparty	Minimum credit criteria / colour band	£ limit per institution	Max. maturity period
	No Colour		Not for use
CDs or corporate bonds with banks and building societies	Blue	£10m	12 months
	Orange		12 months
	Red		6 months
	Green		100 days
	No Colour		Not for use
Gilt funds	UK sovereign rating	£10m	
<b>Non-Specified Investments</b>			
Property Funds - the use of these instruments can be deemed as capital expenditure and as such will be an application (spending) of capital resources		£10m	Limit will be set based on level of reserves and balances going forward and appropriate due diligence will be undertaken before investment of this type
Wider Investment Funds - the use of these instruments can be deemed as capital expenditure and as such will be an application (spending) of capital resources		£10m	Limit will be set based on level of reserves and balances going forward and appropriate due diligence will be undertaken before investment of this type

\* DMO – is the Debt Management Office of HM Treasury

**Accounting treatment of investments.** The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

## ANNEX 5 APPROVED COUNTRIES FOR INVESTMENT

This list is based on those countries which have sovereign ratings of AA- or higher (showing the lowest rating from Fitch, Moody's and S&P) and also (except - at the time of writing – for Hong Kong, Norway and Luxembourg) have banks operating in sterling markets which have credit ratings of green or above in the Link Asset Services credit worthiness service.

### ***Based on lowest available rating***

#### AAA

- Australia
- Canada
- Denmark
- Germany
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

#### AA+

- Finland
- U.S.A.

#### AA

- Abu Dhabi (UAE)
- France
- Hong Kong
- U.K.\*

#### AA-

- Belgium
- Qatar

(Per Link Asset Services 3/1/20)

\* At its meeting of the 15<sup>th</sup> September 2009, full Council approved a recommendation that;

***‘authorises the use of institutions currently supported by the UK Government should its Sovereign rating be downgraded below the current requirement for a ‘AAA’ rating by all three rating agencies’***

this approval continues to form part of the strategy in 2020/21.

## **ANNEX 6 TREASURY MANAGEMENT SCHEME OF DELEGATION**

### **(i) Full Council**

- receiving and reviewing reports on Treasury Management policies, practices and activities.
- approval of annual strategy.
- approval of/amendments to the organisation's adopted clauses, Treasury Management Policy statement and Treasury Management practices.
- budget consideration and approval.
- approval of the division of responsibilities.
- receiving and reviewing regular monitoring reports and acting on recommendations.

### **(ii) Cabinet**

- receiving and reviewing Treasury Management policy statement and Treasury Management practices and making recommendations to the full Council.
- receiving and reviewing regular monitoring reports and making recommendations to the full Council.
- approving the selection of external service providers and agreeing terms of appointment.

### **(iii) Audit and Governance Committee**

- reviewing the Treasury Management policy and procedures and making recommendations to the Cabinet.
- receiving and reviewing regular monitoring and making recommendations to the Cabinet.



## **ANNEX 7 THE TREASURY MANAGEMENT ROLE OF THE SECTION 151 OFFICER**

### **The S151 (responsible) Officer is responsible for**

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers
- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long term timeframe
- ensuring that the capital strategy is sustainable, affordable and prudent in the long-term and provides value for money
- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority
- ensuring that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following -
  - Risk management (TMP1), including investment and risk management criteria for any material non-treasury investment portfolios;
  - Performance measurement and management (TMP2), including methodology and criteria for assessing the performance and success of non-treasury investments;
  - Decision making, governance and organisation (TMP5), including a statement of the governance requirements for decision making in relation to non-treasury

investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making;

- Reporting and management information (TMP6), including where and how often monitoring reports are taken;
- Training and qualifications (TMP10), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.

## **TREASURY MANAGEMENT PRACTICES**

The Treasury Management Practices document (TMPs) forms detailed operational procedures and processes for the Treasury Management function. This document can be found on the Council's Internet by following the following link;

<http://www.tamworth.gov.uk/treasury-practices>

and clicking on the TMPs folder.

The items below are summaries of the individual TMPs which the Council has to produce and adopt under the Treasury Code of Practice.

### **TMP1 : RISK MANAGEMENT**

#### **General Statement**

The Section 151 Officer 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 of the arrangements and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the Council's objectives. The reports will be in accordance with the procedures contained in TMP6.

#### **1.1 Credit and Counterparty Risk Management**

*Credit and counter-party risk is the risk of failure by a counterparty to meet its contractual obligations to the organisation under an investment, borrowing, capital project or partnership financing, particularly as a result of the counterparty's diminished creditworthiness, and the resulting detrimental effect on the organisation's capital or current (revenue) resources.*

This organisation regards a key objective of its Treasury Management activities to be the security of the principal sums it invests. Accordingly, it will ensure that its counterparty lists and limits reflect a prudent attitude towards organisations with which funds may be deposited, and will limit its investment activities to the instruments, methods and techniques referred to in TMP4 Approved Instruments Methods and Techniques and detailed in the TMP Operational document.

It also recognises the need to have, and will therefore maintain, a formal counterparty policy in respect of those organisations from which it may borrow, or with whom it may enter into other financing arrangements.

#### **1.2 Liquidity Risk Management**

*This is the risk that cash will not be available when it is needed, that ineffective management of liquidity creates additional unbudgeted costs, and that the organisation's business/service objectives will be thereby compromised.*

This organisation will ensure it 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. This organisation 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.

### **1.3 Interest Rate Risk Management**

*The risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.*

This organisation will manage its 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.

It will achieve this by the prudent use of its approved financing and investment 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.

### **1.4 Exchange Rate Risk Management**

*The risk that fluctuations in foreign exchange rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.*

The Council will manage its exposure to fluctuations in exchange rates so as to minimise any detrimental impact on its budgeted income/expenditure levels.

### **1.5 Inflation Rate Risk Management**

*Inflation risk, also called purchasing power risk, is the chance that cash flows from an investment won't be worth as much in the future because of changes in purchasing power due to inflation.*

The Council will keep under review the sensitivity of its treasury assets and liabilities to inflation, and will seek to manage the risk accordingly in the context of the whole organisation's inflation exposures.

### **1.6 Refinancing Risk Management**

*The risk that maturing borrowings, capital, project or partnership financings cannot be refinanced on terms that reflect the provisions made by the organisation for those refinancings, both capital and current (revenue), and/or that the terms are inconsistent with prevailing market conditions at the time.*

The Council will ensure that its borrowing, private financing and partnership arrangements are negotiated, structured and documented, and the maturity profile of the monies so raised is managed, with a view to obtaining offer terms for renewal or refinancing, if required, which are competitive and as favourable to the organisation as can reasonably be achieved in the light of market conditions prevailing at the time.

It will actively manage its relationships with its counterparties in these transactions in such a manner as to secure this objective, and will avoid over reliance on any one source of funding if this might jeopardise achievement of the above.

### **1.7 Legal and Regulatory Risk Management**

*The risk that the organisation itself, or an organisation with which it is dealing in its Treasury Management activities, fails to act in accordance with its legal powers or regulatory requirements, and that the organisation suffers losses accordingly.*

The Council will ensure that all of its Treasury Management activities comply with its statutory powers and regulatory requirements. It will demonstrate such compliance, if required to do so, to all parties with whom it deals in such activities. In framing its credit and counterparty policy under TMP1[1] credit and counterparty risk management, it will ensure that there is evidence of counterparties' powers, and compliance in respect of the transactions they may effect with the organisation, particularly with regard to duty of care and fees charged.

This organisation recognises that future legislative or regulatory changes may impact on its 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 organisation.

### **1.8 Fraud, Error and Corruption, and Contingency Management**

*The risk that an organisation fails to identify the circumstances in which it may be exposed to the risk of loss through fraud, error, corruption or other eventualities in its Treasury Management dealings, and fails to employ suitable systems and procedures and maintain effective contingency management arrangements to these ends. It includes the area of risk commonly referred to as operational risk.*

This organisation will ensure that it has identified the circumstances which may expose it to the risk of loss through fraud, error, corruption or other eventualities in its Treasury Management dealings. Accordingly, it will employ suitable systems and procedures, and will maintain effective contingency management arrangements, to these ends.

The Council will therefore:-

- a) Seek to ensure an adequate division of responsibilities and maintenance at all times of an adequate level of internal check which minimises such risks.
- b) Fully document all its Treasury Management activities so that there can be no possible confusion as to what proper procedures are.
- c) Ensure that staff will not be allowed to take up Treasury Management activities until they have had proper training in procedures and are then subject to an adequate and appropriate level of supervision.

Records will be maintained of all Treasury Management transactions so that there is a full audit trail and evidence of the appropriate checks being carried out.

## **1.9 Price Risk Management**

*The risk that, through adverse market fluctuations in the value of the principal sums an organisation borrows and invests, its stated Treasury Management policies and objectives are compromised, against which effects it has failed to protect itself adequately.*

The Council will seek to ensure that its 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 itself from the effects of such fluctuations.

### **TMP2 : PERFORMANCE MEASUREMENT**

The Council is committed to the pursuit of best value in its Treasury Management activities, and to the use of performance methodology in support of that aim, within the framework set out in the Treasury Management Policy Statement.

The Treasury Management function will be the subject of ongoing analysis of the value it adds in support of the Council's stated service objectives. It will be the subject of regular examination of alternative methods of service delivery, of the availability of fiscal, grant or subsidy incentives, and the scope for other potential improvements. The performance of the Treasury Management function will be measured using the criteria set out in the detailed TMP Operational document.

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

The Council will maintain full records of its 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 decisions are set out in the detailed TMP Operational document.

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

The Council will undertake its Treasury Management activities by employing only those instruments, methods and techniques set out in the detailed TMP Operational document and within the limits and parameters defined in TMP1.

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

The Council considers it essential, for the purposes of the effective control and monitoring of its Treasury Management activities, for the reduction of 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 clarity of Treasury Management responsibilities.

The principle on which this will be based is the 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.

If and when this organisation intends, as a result of lack of resources or other circumstances, to depart from these principles, the Section 151 Officer will ensure that the reasons are properly reported in accordance with TMP6 and the implications properly considered and evaluated.

The Section 151 Officer will ensure that there are clear written statements of the responsibilities for each post engaged in Treasury Management, and the arrangements for absence cover. He will also ensure that at all times those engaged in Treasury Management will follow the policies and procedures set out. The present arrangements are set out in the detailed TMP Operational document.

The Section 151 Officer will ensure that there is proper documentation for all deals and transactions, and that procedures exist for the effective transmission of funds. The present arrangements are set out in the detailed TMP Operational document.

The delegations to the Section 151 Officer in respect of Treasury Management are set out in the detailed TMP Operational document. He will fulfil all such responsibilities in accordance with the Council's policy statement and TMPs and, if a CIPFA member, the Standard of Professional Practice on Treasury Management.

#### **TMP6 : REPORTING REQUIREMENTS AND MANAGEMENT INFORMATION ARRANGEMENTS**

The Council will ensure that regular reports are prepared and considered on the implementation of its Treasury Management policies; on the effects of decisions taken and transactions executed in pursuit of those policies; 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.

As a minimum Cabinet and Council will receive:

- An annual report on the planned strategy to be pursued in the coming year and the reporting of Prudential Indicators.
- A mid-year review
- An annual report on the performance of the Treasury Management function including the performance against the Prudential Indicators, the effects of the decisions taken and the transactions executed in the past year and on any circumstances of non-compliance with the Council's Treasury Management policy statement and TMPs.

Cabinet will receive regular monitoring reports on Treasury Management activities and risks.

The Audit and Governance Committee will have responsibility for the scrutiny of Treasury Management policies and practices.

The Treasury Management indicators will be considered together with the Treasury Management indicators in the Prudential Code as part of the budget approval process.

The present arrangements and the form of these reports are set out in the detailed TMP Operational document.

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

The Section 151 Officer will prepare and Council 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 will at minimum be those required by statute or regulation, together with such information as will demonstrate compliance with TMP1, TMP2 and TMP4.

The Section 151 Officer will exercise effective controls over this budget and report upon and recommend any changes required in accordance with TMP6.

The Council will account for its Treasury Management activities, for decisions made and transactions executed in accordance with appropriate accounting practices and standards, and with statutory and regulatory requirements in force for the time being.

### **TMP8 : CASH AND CASH FLOW MANAGEMENT**

Unless statutory or regulatory requirements demand otherwise, all monies in the hands of the Council will be under the control of the Section 151 Officer 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 Section 151 Officer will ensure that these are adequate for the purpose of monitoring compliance with TMP1. The present arrangements for preparing cash flow projections, and their form, are set out in the detailed TMP Operational document.

### **TMP9 : MONEY LAUNDERING**

The Council is alert to the possibility that it may become the subject of an attempt to involve it in a transaction involving the laundering of money. The Council will, therefore, maintain procedures for verifying and recording the identity of counterparties and reporting suspicions, and will ensure that all staff involved are properly trained. The present arrangements, including the name of the officer to whom reports should be made, are set out in the detailed TMP Operational document.

### **TMP10 : TRAINING AND QUALIFICATIONS**

The Council 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. It will 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 Section 151 Officer will recommend and implement the necessary arrangements.



The Section 151 Officer will ensure that Council members tasked with Treasury Management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities.

Those charged with governance recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively.

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

The Council recognises that responsibility for the Treasury Management decisions remains with the Council 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 will have been submitted to a full evaluation of the costs and benefits. Terms of appointment will be properly agreed, documented and subject to regular review. It will ensure, where feasible and necessary, that a spread of service providers is used, to avoid over reliance 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 Section 151 Officer, and details of the current arrangements are set out in the detailed TMP Operational document.

### **TMP12 : CORPORATE GOVERNANCE**

The Council is committed to the pursuit of proper corporate governance throughout its services, and to establishing the principles and practices by which this can be achieved. Accordingly the Treasury Management function and its activities will be undertaken with openness, transparency, honesty, integrity and accountability.

The Council has adopted and implemented the key recommendations of the Code. This, together with the other arrangements are set out in the detailed TMP Operational document and are considered vital to the achievement of proper governance in Treasury Management, and the Section 151 Officer will monitor and, if and when necessary, report upon the effectiveness of these arrangements.

### **TMP 13: MANAGEMENT PRACTICES FOR NON-TREASURY INVESTMENTS**

This Council recognises that investment in other financial assets and property primarily for financial return, taken for non-treasury management purposes, requires careful investment management. Such activity includes loans supporting service outcomes, investments in subsidiaries, and investment property portfolios.

The Council will ensure that all of its investments are covered in the capital strategy and/or investment strategy, and will set out, where relevant, the Council's risk appetite and specific policies and arrangements for non-treasury investments. It will be recognised that the risk appetite for these activities may differ from that for treasury management.

The Council maintains a schedule setting out a summary of existing material investments, subsidiaries, joint ventures and liabilities including financial guarantees and the Council's risk exposure.

The following TMPs will apply with regard to non-treasury management investments:-

**TMP1 - Risk management** - including investment and risk management criteria for material non-treasury investment portfolios

**TMP2 - Performance measurement and management** - including methodology and criteria for assessing the performance and success of non-treasury investments

**TMP5 - Decision making and analysis** - including a statement of the governance requirements for decision-making in relation to non-treasury investments, and arrangements to ensure that appropriate professional due diligence is carried out to support decision making

**TMP6 - Reporting and management information** - including where and how often monitoring reports are taken

**TMP10 - Training and qualifications** - including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.

## ANNEX 9

### Treasury Management Glossary of Terms

Bank Rate	The Official Bank rate paid on commercial bank reserves i.e. reserves placed by commercial banks with the Bank of England as part of the Bank's operations to reduce volatility in short term interest rates in the money markets.
Base Rate	Minimum lending rate of a bank or financial institution in the UK.
Capital Financing Requirement	The Council's underlying need for borrowing for a capital purpose.
Counterparty	The organisations responsible for repaying the Council's investment upon maturity and for making interest payments.
Credit Default Swap (CDS)	A specific kind of counterparty agreement which allows the transfer of third party credit risk from one party to the other. One party in the swap is a lender and faces credit risk from a third party, and the counterparty in the credit default swap agrees to insure this risk in exchange for regular periodic payments (essentially an insurance premium). If the third party defaults, the party providing insurance will have to purchase from the insured party the defaulted asset. In turn, the insurer pays the insured the remaining interest on the debt, as well as the principal.
Credit Rating	This is a scoring system that lenders issue organisations with, to determine how credit worthy they are.
Gilts	These are issued by the UK Government in order to finance public expenditure. Gilts are generally issued for a set period and pay a fixed rate of interest for the period.
iTraxx	This is an index published by Markit who are a leading company in CDS pricing and valuation. The index is based on an equal weighting of the CDS spread of 25

	<p>European financial companies.</p> <p>Clients can use the iTraxx to see where an institution's CDS spread is relative to that of the market and judge its creditworthiness in that manner, as well as looking at the credit ratings.</p>
Liquidity	An asset is perfectly liquid if one can trade immediately, at a price not worse than the uninformed expected value, the quantity one desires.
Long term	A period of one year or more.
Maturity	The date when an investment is repaid or the period covered by a fixed term investment.
Minimum Revenue Provision	Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, machinery etc. It would be impractical to charge the entirety of such expenditure to revenue in the year in which it was incurred therefore such expenditure is spread over several years in order to try to match the years over which such assets benefit the local community through their useful life. The manner of spreading these costs is through an annual Minimum Revenue Provision.
Monetary Policy Committee (MPC)	Interest rates are set by the Bank's Monetary Policy Committee. The MPC sets an interest rate it judges will enable the inflation target to be met. Their primary target (as set by the Government) is to keep inflation at or around 2%.
Security	An investment instrument, issued by a corporation, government, or other organization which offers evidence of debt or equity.
Short Term	A period of 364 days or less
Supranational Bonds	A supranational entity is formed by two or more central governments with the purpose of promoting economic development for the member countries. Supranational institutions finance their activities by issuing debt, such as supranational bonds. Examples of supranational institutions include the

	<p>European Investment Bank and the World Bank.</p> <p>Similarly to the government bonds, the bonds issued by these institutions are considered very safe and have a high credit rating.</p>
Treasury Management	<p>The management of the local 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.</p>
Working Capital	<p>Cash and other liquid assets needed to finance the everyday running of a business such as the payment of salaries and purchases.</p>
Yield	<p>The annual rate of return on an investment, expressed as a percentage.</p>

## ANNEX 10

### PRUDENTIAL INDICATORS – DEFINITIONS / INTERPRETATION

CIPFA's Prudential Code for Capital Finance requires local authorities to prepare Prudential Indicators of their intended capital spending plans for the forthcoming and future years. The indicators are intended to help the decision making process within an authority and must be approved by the full Council before the beginning of the financial year. The indicators are neither comparative statistics nor performance indicators. Different Councils will have different figures reflecting their history and local circumstances.

1. **Estimate of total capital expenditure to be incurred** – This summarises the Council's current plans for the total capital expenditure over the next 3 years. Details of individual schemes are contained within the capital estimate pages.

2. **Estimates of Capital Financing Summary** – This details the capital financing sources for the next 3 years.

3. **Estimated Ratio of financing costs to net revenue stream** - This indicator has been calculated as debt interest, borrowing refinancing costs, minimum revenue provision, depreciation for HRA, net of investment income and divided by the General Fund (GF) budget requirement for the GF element of costs and the total of HRA income for the HRA costs. For GF Account, the indicator has been calculated gross of government support in the form of RSG for the proportion of capital expenditure funded from supported level of borrowing.

4. **Capital Financing Requirement** – This represents the Council's underlying need to borrow to finance historic capital expenditure and is derived by aggregating specified items from the Council's balance sheet. The actual **net borrowing** is lower than this because of the current strategy to use internal borrowing rather than replace maturing debt.

5. **Actual External Debt** – This is a key indicator and Section 3 of the Local Government Act 2003 requires the Council to ensure that gross external debt does not, except in the short term, exceed the total of the Capital Financing Requirement in the preceding year plus estimates of any additional capital financing requirement for the current and next two financial years.

6. **Authorised Borrowing Limit for external debt** - This indicator represents the maximum amount the Council may borrow at any point in time in the year and has to be set at a level the Council considers is **prudent**. It allows for uncertain cash flow movements and borrowing in advance for future requirements. The Council does not currently have any finance lease liabilities.

The recommended authorised limits for external debt are gross of investments and are consistent with the Council's current commitments, existing plans and the current treasury management policy and strategy. The authorised limit determined for 2018- 19 is the statutory limit determined under section 3(1) of the Local Government Act 2003.

7. **Operational Boundary for external debt** - The proposed operational boundary for external debt is calculated on the same estimates as the authorised limit but reflects estimates of the most likely, prudent but not worst case scenario, without the additional headroom included within the authorised limit to allow for example for unusual cash movements, and equates to

the maximum of external debt projected by this estimate. Within the operational boundary, figures for borrowing and other long term liabilities are separately identified.

**8. Treasury Management** – these indicators form part of the treasury management strategy and policy statement approved by the Council each year before the beginning of the financial year. The main indicators are:

(a) The adoption of **CIPFA Code of Practice for Treasury Management**, which the Council adopted before the current Prudential System was introduced.

(b) **Interest Rate Exposure** - The approved Treasury Policy Statement and Strategy contains upper and lower limits for fixed and variable interest rate exposure for net outstanding principal sums.

(c) **Maturity Structure of Borrowing** – The approved treasury management strategy also sets out the maturity structure of the Council's borrowing to ensure the Council is not exposed to risks of having to refinance large level of debt at a time in future when interest rates may be volatile or uncertain.

(d) **Investments longer than 365 days** – The approved treasury management strategy includes a limit of £20m for investments maturing beyond 365 days.

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