

# Corporate Policy & Resources Committee



20 February 2023

<b>Title</b>	Treasury Management Strategy Statement 2023/24
<b>Purpose of the report</b>	The Council has statutory duty to approve an annual treasury management strategy. The Council may require amendments to the strategy but must ensure that an approved strategy is in place for each financial year.
<b>Report Author</b>	Sam Masters, Treasury Management and Capital Accountant (Interim)
<b>Wards affected</b>	All Wards
<b>Exempt</b>	No
<b>Corporate Priority</b>	Community Affordable Housing Recovery Environment Service delivery
<b>Recommendations</b>	<b>Corporate Policy &amp; Resources Committee recommend to Council that it:</b> <ol style="list-style-type: none"> <li><b>1. approves the proposed Treasury Management Strategy for 2023/24 as set out in this report.</b></li> <li><b>2. notes the Treasury Management Practices (TMP) and Schedules</b></li> </ol>
<b>Reason for Recommendation</b>	<b>The Treasury Management Strategy is a statutory requirement upon the Council</b>

## 1. Introduction

- 1.1 Treasury management is the management of the Council's 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 The prime objective of the Council's investment strategy is to maintain capital security whilst ensuring that there is the necessary liquidity to carry out its business. Within these constraints, the strategy aims to maximise returns.
- 1.3 The borrowing strategy aims to minimise the revenue cost of debt whilst securing the council from revenue pressures in the event of interest rate volatility.
- 1.4 One revenue consequence of borrowing is the statutory requirement to set aside an amount for repayment of debt, known as Minimum Revenue Provision

(MRP). Regulations require the authority to determine annually a principle by which MRP will be determined.

- 1.5 The treasury management strategy aims to protect the council from market-related risks by monitoring interest rates, economic indicators, and UK and overseas government finances. A range of information sources is used to inform economic analysis and forecasts.
- 1.6 This document fulfils the Council's statutory duty under the *Local Government Act 2003* to have regard to the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2017 Edition* (the CIPFA TM Code), which requires the Council to approve a treasury management strategy before the start of each financial year.
- 1.7 This is a technical report providing necessarily detailed information that the Council is required to have due regard to. Certain key information is appended for the sake of clarity. **Appendix A** provides recent benchmarking of the investment portfolio by the Council's treasury advisors, illustrating performance reporting used by the Council. Background to this report is given at **Appendices B and C**. The MRP Statement is given at **Appendix D**. The Treasury Management Practices (TMP) and Schedules, included at **Appendix E**, set out how this Council will seek to achieve its treasury management policies and objectives and how it will manage and control those activities.

## **2. Options analysis and proposal**

- 2.1 Option 1: The Council has a statutory duty under the *Local Government Act 2003* to approve and publish a treasury management strategy before the start of each financial year. Recommended option to approve the draft Strategy as approval
- 2.2 Option 2: Committee may make recommendations to develop the strategy, as long as those recommendations comply with the CIPFA TM code and are consistent with the statutory regulatory framework, as started above the Committee must ensure a strategy is in place each year to meet its statutory duty.
- 2.3 Option 3: Not approve a Strategy. The Council does not have the option refuse to approve a strategy altogether.

## **3. Summary position**

On 31 December 2022, the Council held £1,096.5m of borrowing, £127.7m of treasury investments and £916.4m of non-treasury investment property. Overall, the Council position is £52.4m net borrowing. This detailed in Table 1 below.

**Table 1: Current Investment & Debt Portfolio Position**

As at 31.12.2022	Actual Portfolio
	£m
<b>External Borrowing:</b>	
Public Works Loan Board	(1,084.0)
Local Authorities (short term)	(12.5)
<b>Total Gross External Debt</b>	<b>(1,096.5)</b>
<b>Long-Term Investments:</b>	
Pooled Fund Investments	32.7
Funding Circle	0.4
<b>Short-Term Investments:</b>	
Local Authorities	35.0
Fixed Rate Deposits	15.0
Money Market Funds	44.6
<b>Total Investments</b>	<b>127.7</b>
Net (borrowing)/ investments	(968.8)

<b>Non-treasury investments:</b>	
<b>Investment property (as at 31Mar22)</b>	<b>916.4</b>

<b>Overall net borrowing</b>	<b>(52.4)</b>
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- 3.1 Funding Circle is a peer-to-peer lending platform which provides an alternative borrowing mechanism for small businesses. This investment was made in April 2015 to help diversify the investment portfolio, and as an economic development opportunity enabling the Council to support local businesses where demand exists. Following general review by the Funding Circle fund manager over the COVID period, fund management has changed so that sums from repaid loans are not being reinvested, so the fund is being run down.
- 3.2 **Minimum Revenue Provision (MRP):** Where the Council finances capital expenditure by debt, the Council is required to put aside resources to repay that debt. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), noting that there has been no statutory minimum since 2008. The Council's Annual MRP Statement is included at Appendix D. It should be noted that the Council repays borrowing each year, and that this is reflected in the MRP.
- 3.3 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, also known as internal borrowing. Forecast changes in the CFR, investments and borrowing are shown in Table 2 below.

**Table 2: Capital Financing Requirement**

	Actual 31.03.2022	Estimate 31.03.2023	Estimate 31.03.2024	Estimate 31.03.2025	Estimate 31.03.2026
	£m	£m	£m	£m	
Opening CFR	1,128.5	1,117.7	1,170.0	1,201.5	1,305.3
In-year movement (below)	(10.8)	52.3	31.5	103.8	142.2
<b>Closing CFR</b>	<b>1,117.7</b>	<b>1,170.0</b>	<b>1,201.5</b>	<b>1,305.3</b>	<b>1,447.5</b>
Less: External borrowing	(1,117.8)	(1,096.5)	(1,063.7)	(1,191.4)	(1,191.4)
Internal borrowing	(0.1)	73.5	137.8	113.9	256.1
<i>Capital programme:</i>					
Housing & Regeneration	4.7	63.8	51.2	146.6	162.8
Other capital expenditure	1.3	3.4	5.6	2.1	2.3
<b>Total Capital Expenditure</b>	<b>6.0</b>	<b>67.2</b>	<b>56.8</b>	<b>148.7</b>	<b>165.1</b>
<i>Financing:</i>					
Capital Receipts	(0.7)	(0.7)	(3.0)	(3.0)	(3.0)
Capital Grants and Contributions	(2.6)	(1.0)	(9.1)	(28.3)	(5.3)
Revenue Contributions	(1.2)	(0.8)	(0.8)	(0.8)	(0.8)
<b>Net Financing Need</b>	<b>1.5</b>	<b>64.7</b>	<b>43.9</b>	<b>116.6</b>	<b>156.0</b>
<i>Less: Minimum</i>					
Revenue Provision (MRP)	(12.3)	(12.4)	(12.4)	(12.8)	(13.8)
<b>In-year movement in CFR</b>	<b>(10.8)</b>	<b>52.3</b>	<b>31.5</b>	<b>103.8</b>	<b>142.2</b>

- 3.4 The Council has an increasing CFR due to planned Capital Programme expenditure, in particular on the Council's housing delivery and regeneration programme and on service projects such as the new Leisure Centre.
- 3.5 The Authorised Borrowing Limit of £1,450m and Operational Boundary of £1,350m for 2023/24, are considered appropriate for the above projections but will be reviewed and revised as needed to reflect borrowing requirements in future years. As can be seen in the above table the anticipated external borrowing figure falls below both figures.
- 3.6 CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that an authority's total debt be lower than its highest forecast CFR over the next three years. Table 2 above shows that the Council expects to comply with this recommendation for 2023/24

#### **Local context - Liability benchmark**

- 3.7 To compare the Council's actual borrowing against an alternative strategy, a liability benchmark (a measure of risk outlined in the CIPFA TM Code and now

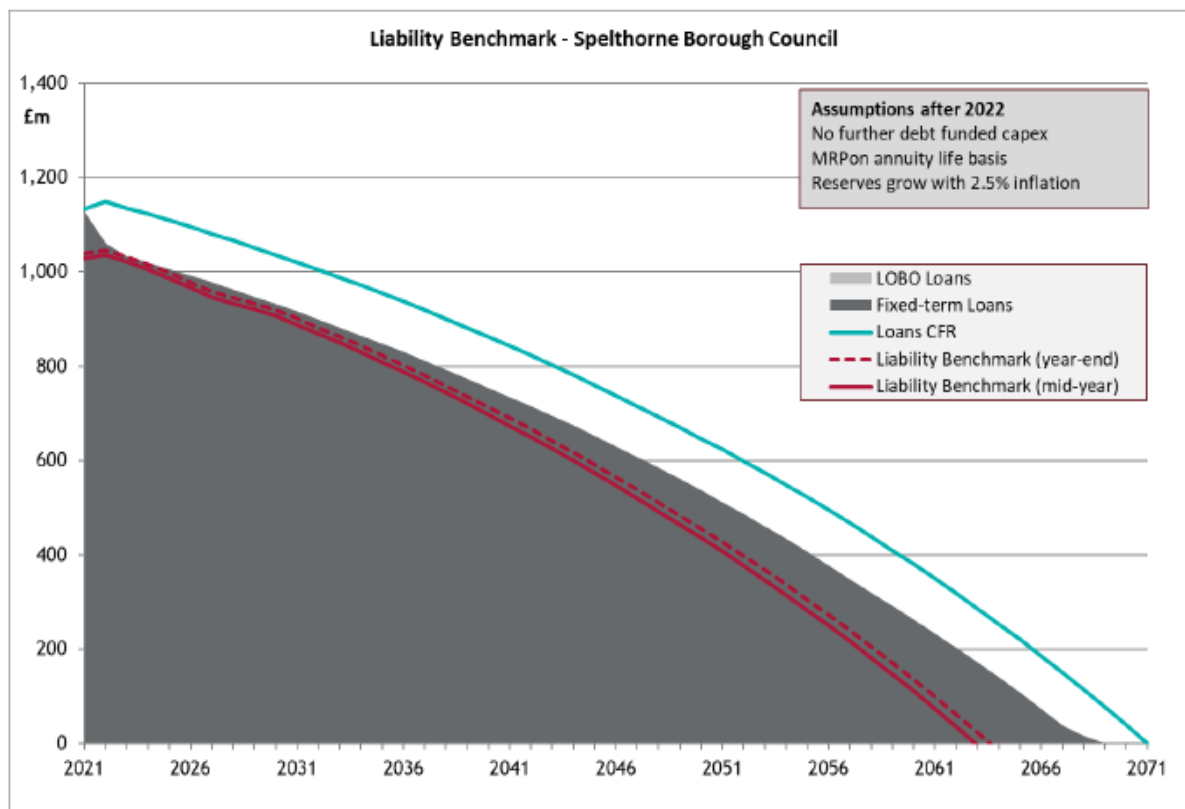
required to be reported on for future years) has been calculated showing the lowest risk level of borrowing, as shown at Table 3. This assumes the same forecasts as Table 2 above, but that cash and investment balances are kept to a minimum level of £20m at each year-end to maintain sufficient liquidity but minimise credit risk.

**Table 3: Liability benchmark**

	Actual 31.03.2022	Estimate 31.03.2023	Estimate 31.03.2024	Estimate 31.03.2025	Estimate 31.03.2026
	£m	£m	£m	£m	£m
CFR	1,117.7	1,170.0	1,201.5	1,305.3	1,447.5
Balance Sheet resources	(111.0)	(113.0)	(119.0)	(113.0)	(113.0)
Minimum investment	20.0	20.0	20.0	20.0	20.0
Liability benchmark	1,026.7	1,077.0	1,102.5	1,212.3	1,354.5

3.8 The liability benchmark indicates that the required minimum level of borrowing is forecast to be £1,077.0m as at 31 March 2023 after taking into account other resources such as usable reserves and the minimum investment of £20.0m.

3.9 Following on from the medium-term forecasts in table 2 above, the longer-term liability benchmark given next shows the level of borrowing that will be required in future years – consistently low at around £0.1m to £0.2m (the gap under the top, green line). The Council will be working with Arlingclose to further develop this modelling to help identify and apply internal resources effectively.



## 4. Borrowing and Investment Strategies

### Borrowing Strategy

- 4.1 The Council currently holds £1,096.5m of loans (Table 1) as part of its strategy for funding previous years' capital programmes. The Council was debt-free before 2016/17, when the decision was taken to make strategic property acquisitions based on the opportunities available. This continues to be the case, with the important caveat that Council has no intention to buy investment assets primarily for yield, and specifically not in the current or next two financial years. This is as set out in the Council's Capital Strategy. The Council's focus is funding its housing and regeneration programme and services expenditure.
- 4.2 The forecast in Table 2 shows that the Council expects borrowing to be a maximum of £1,063.6m in 2023/24. The Council may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the Council's Authorised Borrowing Limit. This Limit is set at £1,450m to enable the Council to fund housing developments and place-shaping within the Borough.
- 4.3 The revised draft Capital Programme budget for 2023/24 has been set at £45.2m, net of funding, although the programme has been significantly delayed because of the ongoing impact of COVID-19 and inflationary pressures on the cost of materials and borrowing. A proportion of rental income from existing investment property is set aside to increase sinking funds, which contribute towards financing of future property-related costs.
- 4.4 **Objectives:** The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty over those costs over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.
- 4.5 **Strategy:** Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio.
- 4.6 With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term either to use internal resources, or to borrow short-term loans instead of long-term. By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.
- 4.7 The benefits of internal and short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Council with this 'cost of carry' and breakeven analysis, the result of which will help determine whether the Council borrows additional sums at long-term fixed rates in 2023/24 with a view to keeping future interest costs low and gaining long term value for money even if costs are higher in the immediate to short term.
- 4.8 The Council has previously raised the majority of its long-term borrowing from the PWLB, which remains a relatively good option. The Government now prohibits authorities that have 'investments for yield' (which the Council does not intend to have) from accessing PWLB loans.

- 4.9 The Council will consider long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding, in line with the CIPFA TM Code.
- 4.10 Specifically, the Council is working with Arlingclose to identify alternative funding options for potential acquisitions and future development projects, and at options for diversifying the Council's debt to build a portfolio from a number of sources.
- 4.11 The Council will also consider forward-starting loans, where the interest rate is fixed in advance and the cash is received in later periods. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period. Forward starting loans would facilitate effective funding of major development projects such as those planned for the property portfolio.
- 4.12 In addition, the Council may borrow short-term when needed to cover unplanned cash-flow shortages.
- 4.13 **Sources of borrowing:** Approved sources of long-term and short-term borrowing are:
- HM Treasury's PWLB lending facility (formerly the Public Works Loan Board)
  - Works Loan Board (PWLB) and any successor body
  - any institution approved for investments (see below)
  - any other bank or building society authorised to operate in the UK
  - any other UK public sector body
  - UK public and private sector pension funds (except Surrey Pension Fund)
  - capital market bond investors
  - UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues
- 4.14 **Other sources of debt finance:** In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:
- leasing
  - hire purchase
  - Private Finance Initiative
  - sale and leaseback.
- 4.15 **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. The Agency plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to Council.
- 4.16 **LOBOs:** The Council does not hold and has not previously held, LOBO (Lender's Option Borrower's Option) loans, which expose borrowers to an

element of refinancing risk. A LOBO lender has the option to propose an increase in the interest rate at set dates, following which the borrower has the option to either accept the new rate or to repay the loan at no additional cost. These loans do not represent value for money and will not form part of the Council's borrowing strategy.

- 4.17 **Short-term and variable rate loans:** These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below. Financial derivatives may be used to manage this interest rate risk.
- 4.18 **Debt rescheduling:** The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

### **Investment Strategy**

- 4.19 The Council holds significant levels of invested funds representing income received in advance of expenditure plus balances and reserves held. Total long-term investments are £33.1m as at the end of December 2022 (Table 1). This includes £32.7m pooled funds, noting that the COVID-19 crisis resulted in a reduction in the capital value of these holdings as they are primarily property funds. This reduction is expected to be temporary and has since partially recovered.
- 4.20 Invested funds may be increased further if there are significant additional capital receipts and if it is agreed that these are to be invested. Total investments are higher throughout the financial year and are monitored closely and maintained at appropriate levels as part of managing short-term cash-flow requirements of the Council.
- 4.21 **Objectives:** Both the CIPFA TM Code and the DHLUC Guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest yield (rate of return). The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.
- 4.22 **Strategy:** The Council aims to maximise liquidity of funds to ensure availability for capital expenditure, in line with the Council's significant property and housing service plans.
- 4.23 **Business models:** Under the IFRS 9 standard, accounting for certain investments depends on the Council's "business model" for managing them. The Council aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.



- 4.24 **Approved counterparties:** The Council may invest its surplus funds with any of the counterparty types in Table 4 below, subject to the cash limits (per counterparty) and the time limits shown.
- 4.25 The cash limits shown have been agreed in conjunction with our treasury advisers, to enable the Council to have sufficient flexibility within the strategy being set to manage funds appropriately as they are received. This can sometimes include holding funds in advance of need in relation to making strategic acquisitions.

**Table 4: Approved investment counterparties and limits**

<b>Credit Rating</b>	<b>Government</b>	<b>Banks Secured</b>	<b>Banks Unsecured</b>	<b>Corporates</b>	<b>Registered Providers</b>
UK Gov	£ Unlimited 50 years	n/a	n/a	n/a	n/a
AAA	£10m 50 years	£10m 20 years	£10m 5 years	£5m 20 years	£5m 20 years
AA+	£10m 25 years	£10m 10 years	£10m 5 years	£5m 10 years	£5m 10 years
AA	£10m 15 years	£10m 5 years	£10m 4 years	£5m 5 years	£5m 10 years
AA-	£10m 10 years	£10m 4 years	£10m 3 years	£5m 4 years	£5m 10 years
A+	£5m 5 years	£10m 3 years	£10m 2 years	£5m 3 years	£5m 5 years
A	£5m 5 years	£10m 2 years	£10m 13 months	£5m 2 years	£5m 5 years
A-	£5m 5 years	£10m 13 months	£10m 6 months	£5m 13 months	£5m 5 years
None	£5m 25 years	n/a	£1m 6 months	£1m 5 years	£5m 5 years

Pooled funds and real estate investment trusts (REITs)	£10m per fund at point of investment
Money Market Funds	Unlimited per fund

This table must be read in conjunction with the notes below.

- 4.26 **Credit Rating:** Investment limits are set by reference to the lowest published long-term credit rating from a selection of external rating agencies. Where available, the credit rating relevant to the specific investment or class of investment is used; otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.
- 4.27 **Government:** Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years

- 4.28 **Banks Secured:** Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment-specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.
- 4.29 **Banks Unsecured:** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.
- 4.30 **Corporates:** Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in but are exposed to the risk of the company going insolvent. Loans to unrated companies would only be made either following a financial or credit assessment or as part of a diversified pool in order to spread the risk widely.
- 4.31 **Registered Providers:** Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing and Registered Social Landlords, formerly known as Housing Associations. These bodies are tightly regulated in England by the Regulator of Social Housing. As providers of public services, they retain the likelihood of receiving government support if needed.
- 4.32 **Money Market Funds:** These are pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. Although no sector limit applies to money market funds, the Council will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.
- 4.33 **Strategic Pooled Funds:** Bond, equity and property funds offer enhanced returns over the longer term but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date and are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.
- 4.34 **Real Estate Investment Trusts:** Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties. Investments in REIT shares cannot be withdrawn but can be sold on the stock market to another investor.
- 4.35 **Operational Bank Accounts:** The Council may incur operational exposures, for example through current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments but

are still subject to the risk of a bank bail-in, and balances will therefore be kept below £500,000 per bank as far as practicably possible, and, where practical issues necessitate, no more than £5m as per Table 4. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

- 4.36 **Risk Assessment and Credit Ratings:** Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria, then:
- no new investments will be made,
  - any existing investments that can be recalled or sold at no cost will be, and
  - full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.
- 4.37 Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.
- 4.38 **Other information on the security of investments:** The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis and advice from the Council's treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it might otherwise meet the above criteria.
- 4.39 When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2020, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause investment returns to fall but will protect the principal sum invested.
- 4.40 **Investment Limits:** The maximum that will be lent to any one organisation (other than the UK Government) will be £10 million, to mitigate the risk in the case of a single default. A group of entities under the same ownership will be treated as a single organisation for limit purposes.
- 4.41 Credit risk exposures arising from non-treasury investments, financial derivatives and balances greater than £500,000 in operational bank accounts count against the relevant investment limits.

- 4.42 Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as shown in Table 5 below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country since the risk is diversified over many countries.

**Table 5: Investment limits**

	<b>Cash limit Per Counterparty</b>
Any single organisation, except the UK Central Government	£10m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£25m per group
Any group of pooled funds under the same management	£25m per manager at point of investment
Negotiable instruments held in a broker's nominee account	£30m per broker
Foreign countries	£10m per country
Registered Providers	£25m in total
Unsecured investments with Building Societies	£10m in total
Loans to unrated corporates	£10m in total
Money Market Funds	£50m in total

- 4.43 **Liquidity management:** A cash flow forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. The Council has implemented a Treasury Management system and is currently developing the reporting available through that system, such as cash-flow forecasting, which will enable determination of the maximum period for which funds may prudently be committed.
- 4.44 The Council will spread its liquid cash over at least four providers (e.g. bank accounts and money market funds), where cash funds over £20 million are held, to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

### **Treasury Management Indicators**

- 4.45 The Council measures and manages its exposures to treasury management risks using the following indicators.
- 4.46 **Security:** The Council adopts a voluntary measure of its exposure to credit risk of its investment portfolio through regular rating advice from its treasury management adviser and through market information from contacts such as brokers and other councils.
- 4.47 **Liquidity:** The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period, without additional borrowing:

Liquidity risk indicator	Target
Total cash available within 3 months	£20m

- 4.48 **Interest Rate Exposures:** The Council is exposed principally to risk in terms of its exposure to interest rate movements on its borrowing and investments. The Council is heavily reliant on investment income to support expenditure and has several strategies in place for managing such risk.
- 4.49 The Council's treasury adviser provides analysis of market movements and assists in investment decisions based on their knowledge of current market conditions and interest rate forecasting.
- 4.50 The Council generally invests medium- to long-term at fixed rates. The Council currently has no variable rate investments.
- 4.51 Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. All other instruments are classified as variable rate.
- 4.52 **Maturity Structure of Borrowing:** This indicator is set to control the Council's exposure to refinancing risk. We calculate this as the amount of fixed rate borrowing we can have maturing in each period as a percentage of total projected borrowing that is at a fixed rate. The calculation takes fixed rate to be whether the borrowing was taken out at a fixed rate for a fixed period of time, regardless of that length of time. The upper and lower limits on the maturity structure of borrowing are as shown in Table 6.

**Table 6: Maturity Structure of Borrowing**

	Upper	Lower
Under 12 Months	10%	0%
1 – 2 Years	15%	0%
3 – 5 Years	20%	0%
6 – 10 Years	25%	0%
10 – 20 Years	50%	0%
20 – 30 Years	75%	0%
30 – 40 Years	90%	0%
40 – 50 Years	100%	0%

- 4.53 Time periods start on the first day of each financial year. The maturity of borrowing is the earliest date on which the lender can demand repayment. In the case of PWLB, this is the maturity date.
- 4.54 This indicator allows us to have the percentage of borrowing maturing in each time range shown above, taking into account our current debt profile and

providing an allowance for new borrowing, while having consideration to the Capital Programme.

- 4.55 **Principal Sums Invested for Periods Longer than 364 days:** The purpose of this indicator is to control the Council’s exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end are shown in Table 7 below.

**Table 7: Principal Limits – Price risk indicator**

	2023/24	2024/25	2025/26	2026/27
	£m	£m	£m	£m
Limit on principal invested beyond year end	70	70	70	70

- 4.56 **Affordable borrowing limit:** The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt). In line with statutory guidance, a lower “operational boundary” is also set as a warning level should debt approach the limit.

**Table 8: Prudential Indicators - Authorised limit and operational boundary for external debt**

	2023/24	2024/25	2025/26	2026/27
	£m	£m	£m	£m
Authorised borrowing limit	1,450	1,450	1,450	1,450
Operational boundary	1,350	1,350	1,350	1,350

- 4.57 **Estimates of financing costs to net revenue stream** shown in Table 9 is a measure of the affordability of borrowing. The Council’s financing costs relate substantially to borrowing when commercial property was acquired prior to March 2019. As the CIPFA TM Code notes, commercial investments are taken or held primarily for financial return and are not linked to treasury management activity or directly part of delivering services. However, as commercial property was directly related to borrowing costs, Table 10 also shows the net income after costs and contributions to future costs. This illustrates the affordability of the commercial investments.

**Table 9: Prudential Indicator - Financing costs to net revenue stream**

	2023/24	2024/25	2025/26	2026/27
Net Revenue Stream, £m	13.6	13.7	12.6	12.2
Financing costs, £m	39.4	39.5	39.6	39.7
Ratio	2.9	2.9	3.1	3.2

**Table 10: Commercial income, related costs and net contributions to future costs+**

	2023/24	2024/25	2025/26	2026/27
	£m	£m	£m	£m
Commercial income	(46.1)	(49.2)	(53.4)	(54.1)
Landlord costs	7.9	8.8	6.8	6.3
Contribution to sinking funds	1.0	0.8	2.9	3.7
Financing costs	39.4	39.5	39.6	39.7
<b>Net income after landlord &amp; financing costs &amp; net contributions to sinking fund</b>	<b>2.2</b>	<b>(0.02)</b>	<b>(4.1)</b>	<b>(4.5)</b>

### Related Matters

- 4.58 The CIPFA TM Code requires the Council to include the following in its treasury management strategy.
- 4.59 **Financial Derivatives:** Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the *Localism Act 2011* removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).
- 4.60 The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward-starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.
- 4.61 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.
- 4.62 In line with the CIPFA TM Code, the Council will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.
- 4.63 **Markets in Financial Instruments Directive (MIFD):** The Council has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

## 5. Financial implications

- 5.1 The budget for property investment income in 2023/24 is £46.1m (£38.2 after landlord costs), based on an investment portfolio of £1,049m (purchase cost) at an average interest rate of 4.4%. The budget for debt interest paid in 2023/24 is £25.2m, based on an average debt portfolio of £1,080.1m at an average interest rate of 2.3%. After financing costs, property costs and set asides, it is anticipated that the Council will have a net deficit. This is due to a reducing in rental income. However this appears to be an anomaly and a return to net surpluses is predicted for 2024/25 onwards.

## 6. Risk considerations

- 6.1 The DHLUC Guidance and the CIPFA TM Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. The strategy has been drawn up in consultation with the Council's independent treasury and investment advisers, to ensure a prudent and robust approach in the strategy.
- 6.2 Some alternative strategies, with their financial and risk management implications, are listed below in Table 11.

**Table 11: Alternative strategies**

<b>Alternative</b>	<b>Impact on income and expenditure</b>	<b>Impact on risk management</b>
Invest in a narrower range of counterparties and/or for shorter times	Lower investment sums resulting in less Interest income	Lower chance of losses from credit related defaults although such losses may be greater  Also, less diversity increases risk of losses
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher with increased investment sums	Increased risk of losses from credit related defaults, but any such losses may be smaller  Increased diversity also decreases the risk of significant loss
Borrow additional sums at long-term fixed interest rates (not in advance of need)	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default. However long-term interest costs may be more certain



<b>Alternative</b>	<b>Impact on income and expenditure</b>	<b>Impact on risk management</b>
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Reduced debt interest costs  Less income for funding projects  Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain  Less resources available for the Capital Programme which would need to be reduced

**7. Procurement considerations**

Not applicable

**8. Legal considerations**

The Council has a statutory obligation, under The Local Government Act 2003 to approve and publish its Treasury Management Strategy.

**9. Other considerations**

Not applicable.

**10. Equality and Diversity**

Not applicable

**11. Sustainability/Climate Change Implications**

The Corporate Policy and Resources Committee has agreed the parameters to be used in its Environmental, Social and Governance (ESG) strategy, the strategy has yet to be agreed. One of the intentions of developing and ESG strategy is to enable the Council to transition the investment portfolio to a more sustainable and environmentally sound approach.

**12. Timetable for implementation**

1<sup>st</sup> April 23

### **13. Contact**

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**Background papers:** None

**Appendices:**

TMS 2223 - Appx A - Arlingclose Benchmarking

TMS 2223 - Appx B - Context and Background v08 (5 pages)

TMS 2223 - Appx C - Arlingclose forecast (3 pages)

TMS 2223 - Appx D - Annual MRP Statement v03 (2 pages)

TMS 2223 - Appx E - TMP and Schedules (51 pages)