

Report to: **Cabinet**

Date: **24 January 2023**

By: **Chief Finance Officer**

Title of report: **Treasury Management Policy and Strategy 2023/24**

Purpose of report: **This report proposes the Treasury Management Policy and Strategy for 2023/24. The Council is also required to set Prudential Indicators as set out in the Prudential Code which are included in this strategy for approval.**

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## ***RECOMMENDATIONS***

**Cabinet is recommended to recommend Council to:**

- 1) approve the Treasury Management Policy and Strategy Statement for 2023/24;**
  - 2) approve the Annual Investment Strategy for 2023/24;**
  - 3) approve the Prudential and Treasury Indicators 2023/24 to 2025/26;**
  - 4) approve the Minimum Revenue Provision (MRP) Policy Statement 2023/24 at Appendix A (Section 3).**
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### **1. Background**

1.1 A requirement under the Chartered Institute for Public Finance and Accountancy (CIPFA) Code of Practice for Treasury Management in the Public Services is to prepare a Treasury Management Policy and Strategy setting out the Council's policies for managing investments and borrowing.

1.2 The Local Government Act 2003 and supporting regulations requires the Council to 'have regard to' the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

1.3 The Treasury Management Policy and Strategy Statement (TMSS) for 2023/24 is presented in **Appendix 'A'** to this report. The strategy includes the Treasury Management Policy Statement, the Treasury Management Strategy Statement, the Annual Investment Strategy, Prudential and Treasury Indicators for the next three years and the annual Minimum Revenue Provision (MRP) Policy Statement.

1.4 The 2023/24 TMSS has been prepared within the context the financial challenge being faced by the County Council over the Medium Term Financial Plan and seeks to compliment the Council Plan by:

- utilising long term cash balances as effectively as possible by investing in longer term instruments and/or using to fund borrowing to reduce borrowing costs;
- ensuring the investment portfolio is working hard to maximise income by further use of alternative appropriate investment opportunities during 2023/24;
- ensuring effective management of the borrowing portfolio by exploring rescheduling opportunities and identifying and exploiting the most cost effective ways of funding the Council's borrowing requirement.

## **Investment Strategy**

1.5 The 2023/24 Investment Strategy has been set in the context of improved investment returns as a result of increases in the Bank of England (BoE) Base Rate as a response to global and national inflation caused by a multitude of factors. The Base Rate is currently forecast to peak during 2023/24, after which is expected to start falling again as the BoE is expected to tighten monetary policy in order to contain the impact of recession. The investment performance for 2023/24 is therefore forecast at 4.45%. The average rate of return for 2021/22 was 0.38% and for the first six months of 2022/23 was 1.08%.

1.6 Some changes in the Annual Investment Strategy are recommended as outlined in the table below:

<b>2022/23 Strategy</b>	<b>2023/24 Proposed Strategy</b>	<b>Reason for proposed change</b>
Non-UK banks – minimum criteria of AA+ banks in AA+ sovereign countries.	Non-UK banks – minimum criteria of AA- banks in AA- sovereign countries.	Whilst a reduction in the credit criteria of non-UK banks, in reality, there are no AA+ Banks that can be used under the existing criteria. The change therefore expands the list of names that the council can lend to (allowing better diversification of the investment portfolio) whilst still maintaining a high level of security.  The Approved Counterparty List at Annex A has been updated to reflect this change.
No risk benchmarking criteria.	Introduction of benchmarking the risk of the investment portfolio against historic default rates of counterparties.	To ensure that the risk of the portfolio is monitored closely and reported to members quarterly. A maximum risk indicator will be set to ensure that security is prioritised within acceptable levels.
No performance benchmarking	Introduction of benchmarking the return of the portfolio against the Sterling Overnight Interbank Average Rate (SONIA)	Monitoring the investment portfolio against market interest rates will assess whether the portfolio is maintaining its value. This will be reported to members quarterly.

1.7 Officers continue to seek out Environmental Social & Governance (ESG) investment opportunities with counterparties that meet the council's investment parameters. The council continues to invest in Standard Chartered's sustainable fixed deposits which aligns the Council's

investments with the bank's ESG strategy. The market for green and broader ESG investments is still relatively immature, which reduces the ability to actively invest in products that support the Council's aspirations. However, research and the consideration of the suitability of ESG investment products will continue into 2023/24.

### ***Borrowing Strategy***

1.8 The Borrowing Strategy and the Capital Programme identifies a borrowing need of £113m over the next 3 years (between 2023/24 and 2025/26). The Council currently has sufficient cash balances, therefore, officers will seek to use cash from the Council's own reserves to initially fund borrowing. This will decrease the Council's cash balances, reducing counterparty risk, and reduce borrowing costs. Modelling of the Council's capital plans and cashflows has identified an appropriate level of internal borrowing of around £50m. This strategy will be kept under constant review and borrowing will be undertaken where it is felt there is a significant risk of steep increases in borrowing rates.

1.9 The budget within the Medium Term Financial Plan (MTFP) is calculated using the Treasury Management Tool that reflects the costs of borrowing in support of the targeted basic need programme offset by returns on investment of the Council's balances. It is therefore reflective of a point in time. The treasury management tool, developed as part of the Capital Strategy, is reviewed regularly for reasonableness.

1.10 The introduction of the liability benchmark in Section 2.4 of Appendix A demonstrates that if the council were to internally borrow to utilise its cash-backed reserves and balances whilst maintaining a buffer for cash requirements, external borrowing could be avoided until 2026/27. This indicator will be used to assist with future borrowing decisions, in conjunction with the Treasury management Tool.

### ***Revenue impact***

1.11 The Treasury Management budget within the Medium Term Financial Plan (MTFP) supports the cost of borrowing which includes MRP provision and interest. The budget has been reviewed to take into account the impact of recent interest rate rises, which have increased returns on investments, and the impact of proposed updates to the capital strategy/programme. It is proposed that a reduction of £6m is made to the Treasury Management budget in 2023/24. With interest rates modelled to normalise at a lower level in the medium term, alongside increasing costs of capital programme borrowing, the budget reduction will be removed over 2024/25 and 2025/26.

## **Supporting Information**

### ***Treasury Management Reporting***

2.1 As well as this annual strategy, the CIPFA Code requires the Council reports as a minimum:

- A mid-year review;
- An annual report at the close of the year.

2.2 The Council meets this requirement with the Treasury Management Annual Report 2021/22 and mid-year report 2022/23 presented to Cabinet on 13 December 2022. Additionally, the treasury management monitoring position is reported to Cabinet as part of the Reconciling, Policy, Performance and Resources quarterly monitoring.

### ***Update to Treasury and Prudential CIPFA Code 2023/24***

2.3 CIPFA published the revised Treasury and Prudential codes in 2021. Full adoption of the new Codes is incorporated within this strategy. The main changes to the codes are as follows:

- Adoption of a new liability benchmark treasury indicator to support the financing risk management of the capital financing requirement. This is included in Section 2.4 of Appendix A.
- Amendment to the knowledge and skills register for officers and members involved in the Treasury management function. This will be maintained as part of the Treasury Management Team's records and Council members will be contacted in the new year to assess training requirements for delivery of training.
- Quarterly reporting to members of performance against forward looking indicators. As outlined in 1.2.2 of Appendix A, this will be built into the quarterly Council Monitoring process.
- ESG issues to be addressed within the authority's treasury management policies and practices (TMP1). This isn't a change in the council's investment strategy, but how ESG is incorporated into the monitoring of counterparties' credit standing. The Council's Treasury Management Practices (TMPs) are in the process of being updated for the new financial year to include this requirement. These will be reviewed and implemented by the Chief Finance Officer.
- An update to ensure that authorities are more transparent in their service and commercial investments. This includes a requirement that the Council acknowledges that it will not borrow to invest in the primary purpose for commercial return. These changes are reflected in the Capital Strategy.

### ***Economic Background***

2.4 The Council takes advice from Link Asset Services on its treasury management activities. A detailed view of the current economic situation and forecasts, as prepared by Link Asset Services is included in **Appendix A (Annex B)** to this report.

## **3. Conclusion and recommendations**

3.1 This policy sets out the acceptable limits on ratings, investment periods, amounts to be invested and the borrowing strategy. Cabinet will be aware that the financial position is kept under constant review and if at any time it is felt that any of these limits represent an unacceptable risk appropriate and immediate action will be taken accordingly.

3.2 Cabinet recommends the 2023/24 Treasury Management Policy and Strategy Statement for approval by Council.

## **4. Decision Maker**

4.1 The Treasury Management Strategy 2023/24 will be presented to Cabinet and approved by Full Council

**IAN GUTSELL**

**Chief Finance Officer**

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Local Member(s): All

**BACKGROUND DOCUMENTS**

CIPFA Prudential Code and CIPFA Treasury Management Code

Local Government Act 2003 – Capital Finance

DLUHC Statutory Guidance on Local Authority Investments and the Minimum Revenue Provision.

## Appendix A

# TREASURY MANAGEMENT POLICY AND STRATEGY 2023/24



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## **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 counterparties or instruments commensurate with the Council's 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 authority 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.

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 2021 Prudential and Treasury Management Codes require all local authorities to prepare a capital strategy report, to 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 the capital strategy is to ensure that all elected members on the 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.

#### **1.2.2 Treasury Management reporting**

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

- a. 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).
- b. 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.
- c. 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.

*This Council delegates responsibility for implementation and monitoring treasury management to Cabinet and responsibility for the execution and administration of treasury management decisions to the Section 151 Officer. Cabinet therefore receives the Mid-Year and Annual treasury reports in December each year.*

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

**Quarterly reports** – In addition to the three major reports detailed above, from 2023/24 quarterly reporting is also required. However, these additional reports do not have to be reported to Full Council/Board but do require to be adequately scrutinised. This role is undertaken by Cabinet, and will be incorporated into the quarterly Council Monitoring process.

### **1.3 Treasury Management Strategy for 2023/24**

The strategy for 2023/24 covers two main areas:

#### **Capital issues**

- the capital expenditure plans (section 2) and the associated prudential indicators (Annex C);
- the minimum revenue provision (MRP) policy (Section 3).

#### **Treasury management issues**

- the current treasury position (section 1.5);
- treasury indicators which limit the treasury risk and activities of the Council (Annex C);
- prospects for interest rates (Annex B);
- the borrowing strategy (section 2);
- policy on borrowing in advance of need (section 2.2);
- debt rescheduling (section 2.3);
- the investment strategy (section 4);
- creditworthiness policy (section 4.4); and
- the policy on use of external service provider (section 5.3).

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

#### 1.4 Treasury Management Policy Statement

The policies and objectives of the Council's treasury management activities are as follows:

- i) This Council defines its treasury management activities as:

*'The management of the 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'.*

- ii) This Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council, and any financial instruments entered into to manage these risks.
- iii) This Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance management techniques, within the context of effective risk management.

#### 1.5 Current Treasury Position

A summary of the Council's borrowing & investment portfolios as at 30 November 2022 and forecast at the end of the financial year is shown in **Table 1** below:

Table 1	Actual at 30 November 2022			Forecast to 31 March 2023		
	£'000	% of portfolio	Average Rate	£'000	% of portfolio	Average Rate
<b>Investments</b>						
Banks	146,000	52%	2.74%	160,000	63%	4.30%
Local Authorities	73,350	26%	1.61%	60,000	24%	4.30%
Money Market Funds	54,800	20%	3.02%	30,000	11%	4.20%
CCLA Pooled Property Fund	5,000*	2%	3.85%	5,000	2%	4.00%
<b>Total Investments</b>	<b>279,150</b>	<b>100%</b>	<b>2.56%</b>	<b>255,000</b>	<b>100%</b>	<b>4.28%</b>
<b>Borrowing</b>						
PWLB loans	215,777	97%	4.61%	214,460	97%	4.60%
Market loans	6,450	3%	4.25%	6,450	3%	4.25%
<b>Total external Borrowing</b>	<b>222,227</b>	<b>100%</b>	<b>4.60%</b>	<b>220,910</b>	<b>100%</b>	<b>4.60%</b>

\*£4,632,871 capital valuation 30 November 2022

## 2. BORROWING STRATEGY

The capital expenditure plans of the Council are set out in the Capital Strategy Report being considered by Full Council on 7 February 2023. 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 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.

Any capital investment that is not funded from these new and/or existing resources (e.g. capital grants, receipts from asset sales, revenue contributions or earmarked reserves) increases the Council's need to borrow, represented by the Capital Financing Requirement (CFR). However, external borrowing does not have to take place immediately to finance its related capital expenditure: the Council can utilise cash being held for other purposes (such as earmarked reserves and working capital balances) to temporarily defer the need for external borrowing. This is known as 'internal borrowing'.

The Council's primary objective is to strike an appropriate balance between securing cost certainty, securing low interest rates.

## **2.1 Capital Prudential Indicators**

The Authority's capital expenditure plans are a key driver for 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.

Tables 2 and 3 show the capital expenditure plans of the Authority, and the implications of these on the Capital Financing Requirement over the 3 year period to 2025/26. These indicators have been included in the Treasury Management Strategy for a number of years to demonstrate the affordability and sustainability of the Authority's capital activity.

A further prudential indicator required by the 2021 code for 2023/24 is the Liability Benchmark. This benchmark measures the authority's external debt levels net of the external investments, with the inclusion of a liquidity buffer against the Authority's CFR projection. This measure assumes that the authority will internally borrow almost all its available cash balances held in reserves and balances, with an allowance ensure it is able to meet its cash obligations.

There are four components to the Liability Benchmark: -

1. **Existing loan debt outstanding:** the Authority's existing loans that are still outstanding in future years.
2. **Loans CFR:** this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned MRP.
3. **Net loans requirement:** this will show the Authority's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on its approved prudential borrowing, planned MRP and any other major cash flows forecast.
4. **Liability benchmark (or gross loans requirement):** this equals net loans requirement plus short-term liquidity allowance.

The Liability Benchmark has been produced below in section 2.3 and notes included to explain each element and the Authority's assumptions and forward view.

## **2.2 Borrowing Strategy for 2023/24**

The Council has been carrying an internal borrowing position since 2019/20, a policy which reduces cost and reduces investment counterparty risk as the council are using cash from its own reserves to fund its borrowing requirement as opposed to entering into external borrowing.

There is £8m expected to be funded via borrowing in the 2022/23 Capital Programme. No new external borrowing is expected to be undertaken to fund this, and this will be funded through cash balances. This is expected to increase the Council's under-borrowed position compared to its CFR from £41m at 31 March 2022 to £51m by 31 March 2023 (the increase is in part as a result of repayment of borrowing during 2022/23).

The Council's Capital Programme 2023/24 to 2025/26 forecasts £260m of capital investment over the next three years with £147m met from existing or new resources. The increase in the Council's borrowing need over this period is therefore £113m as shown in **Table 2** below.

2022/23 Projected	Table 2	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	Total
£m		£m	£m	£m	£m
82	Capital Expenditure	97	102	61	260
(74)	<b>Financed by:</b> New & existing resources	(62)	(54)	(31)	(147)
<b>8</b>	<b>Borrowing Need</b>	<b>35</b>	<b>48</b>	<b>30</b>	<b>113</b>

**Table 3** below shows the actual expected external borrowing against the capital financing requirement, identifying any under or over borrowing.

2022/23 Estimate	Table 3	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
£m		£m	£m	£m
233	External Debt at 1 April	224	252	292
(9)	Expected change in Debt	27	40	20
<b>224</b>	<b>External Debt at 31 March</b>	<b>251</b>	<b>292</b>	<b>312</b>
274	CFR* at 1 April	274	302	342
8	Borrowing need (Table 2)	35	48	30
(7)	MRP	(7)	(8)	(10)
<b>275</b>	<b>CFR* at 31 March</b>	<b>302</b>	<b>342</b>	<b>362</b>
<b>51</b>	<b>Under / (Over) borrowing</b>	<b>51</b>	<b>50</b>	<b>50</b>

\*CFR in Table 3 is the underlying need to borrow and excludes PFI and lease arrangements, which are included in the CFR figure in the Prudential Indicators in Annex C

**Table 2** demonstrates that the Council has a borrowing need of £113m over the next three years. The strategy will initially focus on meeting this borrowing need from internal borrowing; avoiding external borrowing by utilising the Council's own surplus funds. Modelling of the movement of reserves and the Council's capital expenditure plans demonstrates that the Council's long term reserves can support a level of at least £50m of internal borrowing. This will mitigate the increase in the cost of borrowing and reduce counterparty risk within the Council's investment portfolio by reducing the portfolio size. The strategy and budget have been prepared based on this assumption. The Liability Benchmark, in section 2.3 below, demonstrates that if the Council were to utilise its cash-backed reserves and balances as far as possible, external borrowing can be avoided until 2028.

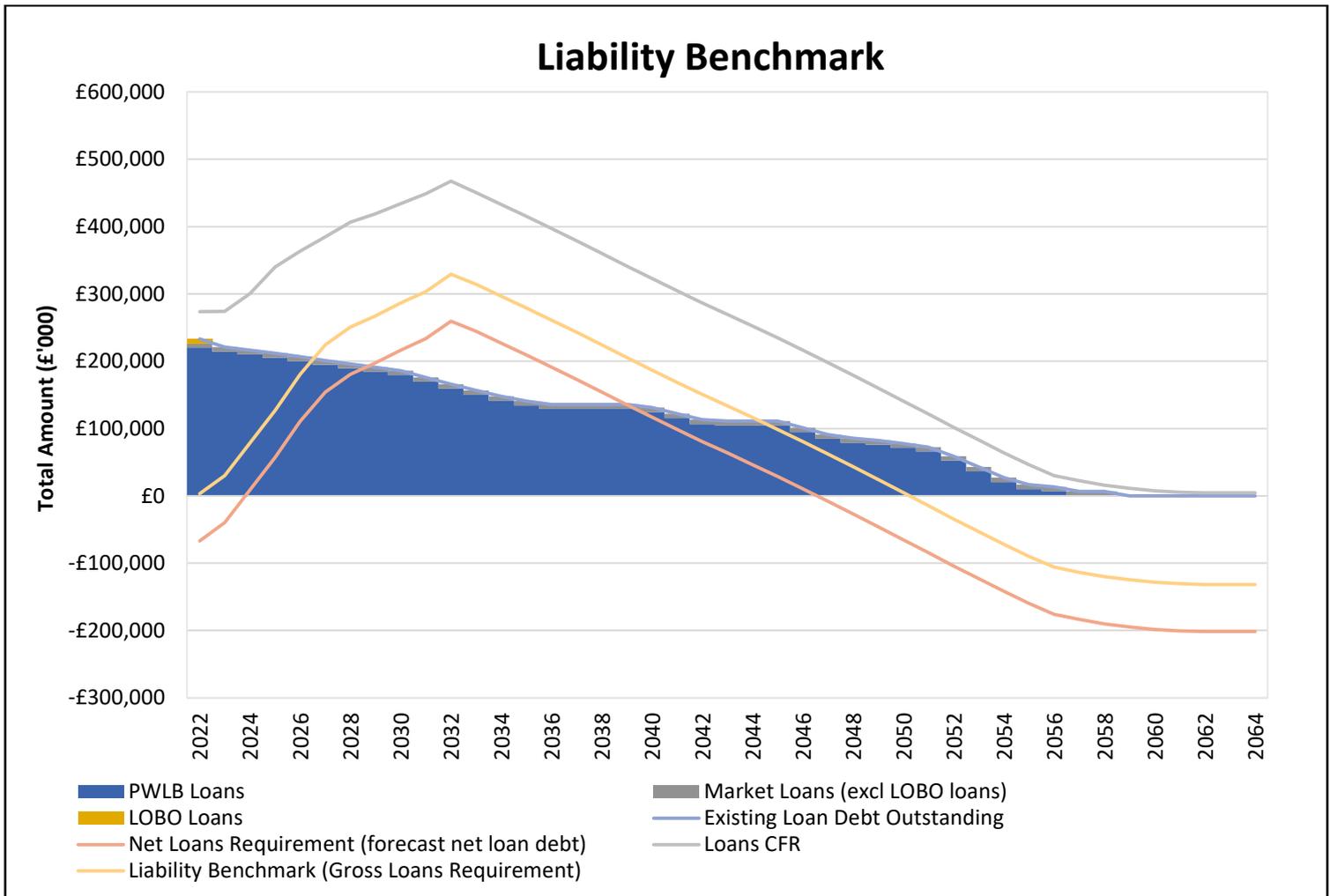
The council's priority is to strike a balance between cost and certainty, and therefore the internal borrowing position will be carefully monitored to avoid incurring higher borrowing costs in the

future at a time when the authority may not be able to avoid new borrowing to finance capital expenditure or refinance maturing debt.

### 2.3 Liability Benchmark

The Liability Benchmark is a new requirement of the 2021 Treasury Management Code. It's a measure of the Council's borrowing need were it to fully utilise its cash-backed reserves and balances to avoid external borrowing. It assumes a liquidity buffer is maintained to ensure the Council's obligations are able to be met.

The Council's liability benchmark is shown below:



- 1) **External Debt** – The maturity profile of the current portfolio of external debt is shown by the bars. The debt has a very gradual maturity profile which means that there are no requirements to pay back large amounts of debt in any one year.
- 2) **Loans CFR** – This is the projections of the Council's underlying borrowing requirement (or CFR) based on the Council's capital plans, and is shown by the top, grey line. The 2022/23 opening Loans CFR was £274m, and it is expected to peak at £467m in 2031/32. This only shows the Loans CFR projection based on the current capital programme of the council, therefore if ongoing borrowing is required beyond 2031/32 then the CFR would rise further and for longer.
- 3) **Net Loans Requirement** – The expected net treasury position is shown by the bottom orange line. This shows a projection of the loan requirements measured by opening

external debt for 2022/23 (£233m) less the opening external investments for 2022/23 (£300m). The projections are then based on the expected borrowing within the capital programme and the expected movement in reserves and balances, and shows the borrowing requirement if the Council were to utilise all of its reserves and balances for internal borrowing. This shows that the Council had more external investments than external debt as at 31/03/22, which is expected to change from 2023/24 as reserves reduce and borrowing is required in the capital programme. The Net Loans Requirement also peaks in 2031/32 as a result of the end of current capital planning period.

- 4) Liability Benchmark** – The liability benchmark shows the Net Loan Requirement, but with a buffer of £70m incorporated to ensure the Council has sufficient cash to meet its cash obligations. This measure shows the level to which the council can internally borrow based on the projection of the capital programme, movement of reserves and allowing for a liquidity buffer. Where the liability benchmark rises above the current debt portfolio, this shows a need for external borrowing, and where the benchmark reduces back below the current portfolio, it shows that the council will be over-borrowed based on current plans.

This graph demonstrates that the Council may not need to externally borrow until 2026/27, and that the external borrowing requirement will peak at £329m in 2031/32, before falling. The graph also shows that based on current plans, new borrowing will be required until 2043/44, so a shorter period than the Council historically borrows for.

Whilst the Liability Benchmark is a good indicator of the Council's direction of travel in terms of borrowing need, it assumes that capital borrowing stops after the current capital planning period, and ignores future borrowing beyond the planning period. Therefore it should not be used in isolation when making long term decisions, but as part of a range of factors.

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

The Council will not borrow purely in order to profit from investment of extra sums borrowed. Any decision to borrow in advance will be within 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.

## **2.5 Debt Rescheduling**

Officers continue to regularly review opportunities for debt rescheduling, but there has been a considerable widening of the difference between new borrowing and repayment rates, which has resulted in much fewer opportunities to realise any savings or benefits from rescheduling PWLB debt.

The reasons for any rescheduling to take place will include:

- the generation of cash savings and / or discounted cash flow savings;
- helping to fulfil the treasury strategy;
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

The strategy is to continue to seek opportunity to reduce the overall level of Council's debt where prudent to do so, thus providing in future years cost reduction in terms of lower debt repayments costs, and potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt. All rescheduling will be agreed by the Chief Finance Officer.

## 2.5 Interest Rate Risk & Continual Review

The total borrowing need in **Table 2**, as well as the debt at risk of maturity shown in **Table 4** is the extent to which the Council is subject to interest rate risk.

<b>Table 4</b>	<b>2023/24</b>	<b>2024/25</b>	<b>2025/26</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Maturing Debt	4	5	5
Debt Subject to early repayments options	0	0	0
<b>Total debt at risk of maturity</b>	<b>4</b>	<b>5</b>	<b>5</b>

Officers continue to review the need to borrow taking into consideration the potential increases in borrowing costs, the need to finance new capital expenditure, refinancing maturing debt, and the cost of carry that might incur a revenue loss between borrowing costs and investment returns.

Against this background and the risks within the economic forecast, caution will be adopted with the 2023/24 treasury operations. The Chief Finance Officer will continue to 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, 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, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

## 3. MINIMUM REVENUE PROVISION POLICY STATEMENT

The Council is required to pay off an element of the accumulated General Fund capital spend each year (the Capital Financing Requirement - CFR) through a revenue charge (the Minimum Revenue Provision - MRP). The Department for Levelling Up, Housing and Communities (DLUHC) regulations require the full Council to approve an MRP Statement in advance of each year. A variety of options are available to Councils, so long as the principle of any option selected ensures a prudent provision to redeem its debt liability over a period which is commensurate with that over which the capital expenditure is estimated to provide benefits (i.e. estimated useful life of the asset being financed).

The policy below reflects a change in the policy as approved and implemented for 2018/19 onwards; The Council is recommended to approve the following MRP Statement for 2023/24 onwards:

### **For borrowing incurred before 1 April 2008, the MRP policy will be:**

- Annuity basis over a maximum of 40 years.

### **From borrowing incurred after 1 April 2008, the MRP policy will be:**

- Asset Life Method (annuity method) – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations. A maximum useful economic life of 50 years for land and 40 years for other assets. This option will also be applied for any expenditure capitalised under a capitalisation directive.

### **For PFI schemes, leases and closed landfill sites that come onto the Balance Sheet, the MRP policy will be:**

- Asset Life Method (annuity method) - The MRP will be calculated according to the flow of benefits from the asset, and where the principal repayments increase over the life of the asset. Any related MRP will be equivalent to the “capital repayment element” of the annual charge payable.

There is the option to charge more than the prudent provision of MRP each year through a Voluntary Revenue Provision (VRP).

For loans to third parties that are being used to fund expenditure that is classed as capital in nature, the policy will be to charge an MRP over the life of the loan.

In view of the variety of different types of capital expenditure incurred by the Council, which is not in all cases capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure. This approach also allows the Council to defer the introduction of an MRP charge for new capital projects/land purchases until the year after the new asset becomes operational rather than in the year borrowing is required to finance the capital spending.

#### 4. ANNUAL INVESTMENT STRATEGY

The DLUHC and CIPFA have extended the meaning of ‘investments’ to include both financial and non-financial investments. This report deals with financial investments. Non-financial investments are covered in the Capital Strategy.

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

- DLUHC’s Guidance on Local Government Investments (the “Guidance”)
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2021 (the “Code”)
- CIPFA Treasury Management Guidance Notes 2021

***The Council’s investment priorities will be the security of capital first, portfolio liquidity second and then yield (return). The Authority will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with regard to the Authority’s risk appetite.***

##### 4.1 Annual Investment Strategy for 2023/24

Investments will be made with reference to the core balance and cash flow requirements and the outlook for interest rates.

Greater returns are usually obtainable by investing for longer periods. However, based on the forecast of Bank Rate below, it is recommended that an “agile” investment strategy is recommended as an appropriate way of optimising returns.

While most cash balances are required in order to manage the ups and downs of cash flow, 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 predicted that Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments on short term or variable terms.
- Conversely, if it is predicted that Bank Rate is likely to fall within that time period, consideration will be given to locking in the higher rates currently obtainable, for longer periods.

It is currently expected that the Bank Rate will increase further, but there is the prospect for Bank Rate to peak in the first half of 2023, and possibly reducing in the latter part of 2023. Link Asset Service's (LAS) Bank Rate forecasts for financial year ends (March) are:

Year	2022/23	2023/24	2024/25	2025/26
Bank Rate	4.25%	4.00%	3.00%	2.50%

LAS's view on the prospect for interest rates, including their forecast for short term investment rates is appended at Annex B.

The primary principle governing the Council's investment criteria is the security of its investments, although the return on the investment is also a key consideration. After this main principle, the Council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in and the criteria for choosing investment counterparties with adequate security, and monitoring their security;
- It has sufficient liquidity in its investments;
- It receives a yield that is aligned with the level of security and liquidity of its investments;
- Where possible, it actively seeks to support Environmental, Social and Governance (ESG) investment products and institutions that meet all of the above requirements.

The preservation of capital is the Council's principal and overriding priority.

#### **4.1.1 Changes from 2022/23 Strategy**

The use of Sovereign credit ratings, as outlined in paragraph 4.3, has been amended. It is recommended that the policy is amended to allow the Council to lend to Sovereign nations and their Banks that meet a minimum credit criterion of AA- (a reduction from AA+ as adopted in the 2022/23 strategy). Whilst this is a reduction in the allowable credit criteria of non-UK countries, it is consistent with the UK credit rating criteria in the strategy, and also allows a wider list of counterparties to lend to, which will help increase the diversification of the investment portfolio. The Counterparty List at Annex A has been amended to reflect the wider set of counterparties allowable under this change in strategy.

Additionally, new benchmarking criteria has been added to paragraph 4.5. Inclusion of this benchmarking within the strategy will assist in monitoring the security and performance of the investment portfolio on an ongoing basis. The benchmarking will be reported alongside the Prudential and Treasury Indicators as part of the quarterly reporting.

#### **4.2 Investment Policy – Management of risk**

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

- i) 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.
- ii) 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.

- iii) 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.
- iv) This authority has defined the list of types of investment instruments that the treasury management team are authorised to use.
  - a. **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year. The limits and permitted instruments for specified investments are listed within Table 7.
  - 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. The limits and permitted instruments for non-specified investments are listed within Table 8.
- v) Lending limits (amounts and maturity) for each counterparty will be set through applying the credit criteria matrix (within Table 7).
- vi) This authority will set a limit for the amount of its investments which are invested for longer than 365 days, detailed in the Treasury Indicators in Annex C.
- vii) Investments will only be placed with counterparties from countries with a specified minimum sovereign rating of AA- (see paragraph 4.3).
- viii) This authority has engaged external consultants, (see paragraph 5.3), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.
- ix) All investments will be denominated in sterling.
- x) As a result of the change in accounting standards for 2022/23 under IFRS 9, this Authority 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, the MHCLG, concluded a 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 ending 31.3.23. At the current juncture it has not been determined whether a further extension to the over-ride will be agreed by Government.

However, this authority will also pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year and included within the quarterly reporting.

### **4.3 Sovereign Credit Ratings**

For 2023/24 it is recommended to amend the policy of lending to sovereign nations and their banks which hold a minimum of AA-. This is a change from the 2022/23 Strategy, where the policy was to lend to Non-UK Sovereigns and their Banks that had a rating of AA+. The proposed Maximum investment limits and duration periods will remain the same as in the previous strategy at £60 million and one year respectively. The list of countries that qualify using this credit criteria (as at the date of this report) are shown below:

**AAA** Germany, Netherlands, Singapore, Sweden  
**AA+** Canada, Finland, USA

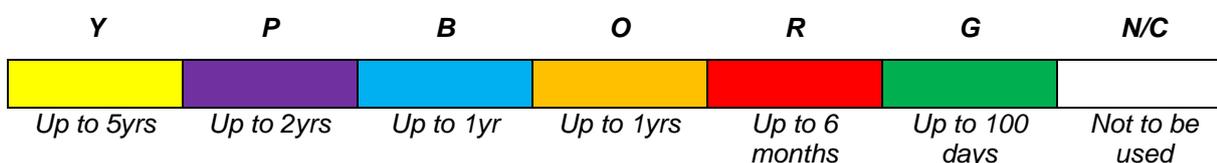
**AA** Abu Dhabi (UAE)  
**AA-** United Kingdom

#### 4.4 Creditworthiness Policy

The Council applies the creditworthiness service provided by the Link Group. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies which is then supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- credit default swap (CDS) spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

This weighted scoring system then produces an end product of 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 (in addition to other due diligence consideration) will use counterparties within the following durational bands provided they have a minimum A- (UK Banks) and AA- (Non-UK Banks) credit rating:



Typically the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A- for UK Banks. 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.

The primary principle governing the Council's investment criteria is the security of its investments, although the return on the investment is also a key consideration. After this main principle, the Council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in and the criteria for choosing investment counterparties with adequate security, and monitoring their security;
- It has sufficient liquidity in its investments.

All credit ratings are monitored daily. The Council is alerted to changes to ratings of all three agencies through its use of the LAS credit worthiness service. If a downgrade results in the counterparty or 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 is advised of information re movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list. The counterparties in which the Council will invest its cash surpluses is based on officer's assessment of investment security, risk factors, market intelligence, a diverse but manageable portfolio and their participation in the local authority market.

**Table 7** below summarises the types of specified investment counterparties available to the Council, and the maximum amount and maturity periods placed on each of these. A full list of the Council's counterparties and the current limits for 2023/24 are appended at Annex A.

## Criteria for Specified Investments

Table 7	Country/ Domicile	Instrument	Min. Credit Criteria/LAS colour band	Max. Amount	Max. maturity period
Debt Management and Deposit Facilities (DMADF)	UK	Term Deposits (TDs)	N/A	unlimited	12 Months
Government Treasury bills	UK	TDs	UK Sovereign Rating	unlimited	12 Months
UK Local Authorities*	UK	TDs	UK Sovereign Rating	£60m	12 Months
Banks – part nationalised	UK	<ul style="list-style-type: none"> <li>▪ TDs</li> <li>▪ Deposits on Notice</li> <li>▪ Certificates of Deposit (CDs)</li> </ul>	N/A	£60m	12 Months
Banks	UK	<ul style="list-style-type: none"> <li>▪ TDs</li> <li>▪ Deposits on Notice</li> <li>▪ CDs</li> </ul>	Blue	£60m	12 Months
			Orange	£60m	12 Months
			Red	£60m	6 Months
			Green	£60m	100 Days
Building Societies	UK	<ul style="list-style-type: none"> <li>▪ TDs</li> <li>▪ Deposits on Notice</li> <li>▪ CDs</li> </ul>	Blue	£60m	12 Months
			Orange	£60m	12 Months
			Red	£60m	6 Months
			Green	£60m	100 Days
Individual Money Market Funds (MMF) CNAV and LVNAV	UK/Ireland/ EU domiciled	AAA Rated Money Market Fund Rating	N/A	£60m	Liquid
VNAV MMF's and Ultra Short Dated Bond Funds	UK/Ireland/EU domiciled	AAA Rated Bond Fund Fund Rating	N/A	£60m	Liquid
Banks – Non-UK	Those with sovereign rating of at least AA-**	<ul style="list-style-type: none"> <li>▪ TDs</li> <li>▪ Deposits on Notice</li> <li>▪ CDs</li> </ul>	Blue	£60m	12 Months
			Orange	£60m	12 Months
			Red	£60m	6 Months
			Green	£60m	100 Days

\* Local Authorities appear on both Specified and Non-specified investment list – an investment with a LA for up to a year is Specified, and between 1-2 years is Non-specified. The maximum amount that can be lent to any single Local Authority is £60m across both specified and Unspecified Investments

\*\*See Paragraph 4.3 for full list of countries that meet these criteria

**Non-Specified investments** are any other types of investment that are not defined as specified. The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out in **Table 8** below:

<b>Table 8</b>	<b>Minimum credit criteria</b>	<b>Maximum investments</b>	<b>Period</b>
UK Local Authorities**	Government Backed	£60m	2 years
Corporate Bond Fund(s)	Investment Grade	£30m	2 - 5 years
Pooled Property Fund(s)	N/A	£30m	5+ years
Mixed Asset Fund(s)	N/A	£30m	2 - 5 years
Short Dated Bond Fund(s)	N/A	£30m	2 – 5 years

*\*\* Local Authorities appear on both Specified and Non-specified investment list – an investment with a LA for up to a year is Specified, and between 1-2 years is Non-specified. The maximum amount that can be lent to any single Local Authority is £60m across both specified and Unspecified Investments*

The maximum amount that can be invested will be monitored in relation to the Council’s surplus monies and the level of reserves. The approved counterparty list will be maintained by referring to an up-to-date credit rating agency reports, and the Council will liaise regularly with brokers for updates. Where Externally Managed Funds are not rated, a selection process will evaluate relative risks & returns. Security of the council’s money and fund volatility will be key measures of suitability. Counterparties may be added to or removed from the list only with the approval of the Chief Finance Officer. A full list of the Council’s counterparties and the current limits for 2023/24 are appended at Annex A.

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

The weighted average benchmark risk factor for 2023/24 is recommended to be 0.05%. This is unchanged from 2022/23. This is a measure of the percentage of the portfolio deemed to be at risk of loss by reference to the maturity date, value of investment, and credit rating of the individual investments within the portfolio compared to the historic default data for those credit ratings.

This benchmark is a simple target (not limit) to measure investment risk and so may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that the in-house treasury team can monitor the current and trend position and amend the operational strategy depending on any changes. Any breach of the benchmarks will be reported with supporting reasons in the mid-year or end of year reviews.

This matrix will only cover internally managed investments, excluding externally managed cash that has been subject to an individual selection process. It also excludes funds lent to other Local Authorities, consistent with the CIPFA Accounting Code.

#### **4.6 Investment Performance Benchmarking**

The performance of the Council’s investment portfolio will be measured against the overnight SONIA Rate.

### **5. OTHER TREASURY ISSUES**

#### **5.1 Banking Services**

NatWest, which is part Government owned, currently provides banking services for the Council.

#### **5.2 Training**

The CIPFA Treasury Management 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.

The scale and nature of this will depend on the size and complexity of the organisation's treasury management needs. Organisations should consider how to assess whether treasury management staff and board/ council members have the required knowledge and skills to undertake their roles and whether they have been able to maintain those skills and keep them up to date.

As a minimum, authorities should carry out the following to monitor and review knowledge and skills:

- Record attendance at training and ensure action is taken where poor attendance is identified.
- Prepare tailored learning plans for treasury management officers and board/council members.
- Require treasury management officers and board/council members to undertake self-assessment against the required competencies (as set out in the schedule that may be adopted by the organisation).
- Have regular communication with officers and board/council members, encouraging them to highlight training needs on an ongoing basis."

In further support of the revised training requirements, CIPFA's Better Governance Forum and Treasury Management Network have produced a 'self-assessment by members responsible for the scrutiny of treasury management', which is available from the CIPFA website to download.

Training was last provided for members of the Audit Committee on 19 November 2021 and further training will be arranged for November 2023.

The training needs of treasury management officers are periodically reviewed.

A formal record of the training received by officers central to the Treasury function and members who are responsible for decision making and scrutiny of the Treasury function will be maintained by the Principal Accountant (Treasury & Taxation).

### **5.3 Policy on the use of External Service Providers**

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

The Council recognises that responsibility for treasury management decisions remains with the Council at all times and will ensure that undue reliance is not placed upon our external service providers. 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, documented and subject to regular review.

### **5.4 Lending to Third Parties**

The Council has the power to lend monies to third parties subject to a number of criteria. These are not treasury type investments rather they are policy investments. Any activity will only take place after relevant due diligence has been undertaken.

### **5.5 Updates to Accounting Requirements**

▪ **IFRS9 – local authority override – English local authorities**

The MHCLG (DLUHC) enacted a statutory over-ride from 1.4.18 for a five-year period until 31.3.23 following the introduction of IFRS 9 in respect of the requirement for any unrealised capital gains or losses on marketable pooled funds to be chargeable in year. This has the effect of allowing any unrealised capital gains or losses arising from qualifying investments to be held on the balance sheet until 31.3.23: this was intended to allow authorities to initiate an orderly withdrawal of funds if required. In addition, IFRS9 impacts the write-down in the valuation of impaired loans.

At the time of writing, we are still waiting to hear whether the application of IFRS9 will be deferred for a further period.

▪ **IFRS 16 – Leasing**

The CIPFA LAASAC Local Authority Accounting Code Board has deferred implementation of IFRS16 until 1.4.24, the 2024/25 financial year. Once implemented, this has the following impact to the Treasury Management Strategy:

- The MRP Policy sets out how MRP will be applied for leases bought onto the balance sheet;
- The Council's Capital Financing Requirement authorised limit and operational boundary expectations for 2024/25 onwards have been increased to reflect the estimated effect of this change.

Bank with duration colour	Country	Fitch Ratings				Moody's Ratings		S & P Ratings		CDS Price	ESCC Duration	Link Duration Limit	Money Limit
Specified Investments:		L Term	S Term	Viab.	Supp.	L Term	S Term	L Term	S Term		(Months)	(Months)	(£m)
<b>UK Counterparties:</b>													
Lloyds Bank PLC (RFB)	UK	A+	F1	a	WD	A1	P-1	A+	A-1	74.27	6	6	60
Lloyds Bank Corporate Markets Plc (NRFB)	UK	A+	F1	-	WD	A1	P-1	A+	A-1	-	6	6	
Bank of Scotland PLC (RFB)	UK	A+	F1	a	WD	A1	P-1	A+	A-1	54.13	6	6	
NatWest Bank (RFB)	UK	A+	F1	a	WD	A1	P-1	A	A-1	-	12	12	60
NatWest Markets Plc (NRFB)	UK	A+	F1	WD	WD	A1	P-1	A-	A-2	-	6	6	
Royal Bank of Scotland (RFB)	UK	A+	F1	a	WD	A1	P-1	A	A-1	-	12	12	
HSBC UK Bank (RFB)	UK	AA-	F1+	a	WD	A1	P-1	A+	A-1	-	12	12	60
HSBC Bank (NRFB)	UK	AA-	F1+	a	WD	A1	P-1	A+	A-1	61.20	12	12	
Barclays Bank UK (RFB)	UK	A+	F1	a	WD	A1	P-1	A	A-1	-	6	6	60
Barclays Bank (NRFB)	UK	A+	F1	a	WD	A1	P-1	A	A-1	105.96	6	6	
Santander UK	UK	A+	F1	a	WD	A1	P-1	A	A-1	-	6	6	60
Santander Financial Services (NRFB)	UK	A+	F1	-	WD	A1	P-1	A	A-1	-	6	6	
Goldman Sachs International Bank	UK	A-	F1	-	WD	A1	P-1	A+	A-1	98.68	6	6	60
Handelsbanken PLC	UK	AA	F1+	-	WD	-	-	AA-	A-1+	-	12	12	60
SMBC Bank International Plc	UK	A-	F1	-	WD	A-	P-1	A+	A-1	59.18	6	6	60
Standard Chartered Bank	UK	A+	F1	a	WD	A1	P-1	A+	A-1	59.98	6	6	60
Close Brothers Ltd	UK	A-	F2	a-	WD	Aa3	P-1	-	-	-	6	6	60
Clydesdale Bank PLC	UK	A-	F2	bbb+	WD	A3	P-2	A-	A-2	-	3	3	60
Nationwide Building Society	UK	A	F1	a	WD	A1	P-1	A+	A-1	-	6	6	60
<b>Non UK Counterparties:</b>													
Royal Bank of Canada	Canada	AA-	F1+	aa-	WD	Aa1	P-1	AA-	A-1+	-	12	12	60
Toronto-Dominion Bank	Canada	AA-	F1+	aa-	WD	Aa1	P-1	AA-	A-1+	-	12	12	60
Nordea Bank Abp	Finland	AA-	F1+	aa-	WD	Aa3	P-1	AA-	A-1+	-	12	12	60

Landwirtschaftliche Rentenbank	Germany	AAA	F1+	-	WD	Aaa	P-1	AAA	A-1+	-	12	24	60
<b>Continued Counterparty list Bank with duration colour</b>	<b>Country</b>	<b>Fitch Ratings</b>				<b>Moody's Ratings</b>		<b>S &amp; P Ratings</b>		<b>CDS Price</b>	<b>ESCC Duration</b>	<b>Link Duration Limit</b>	<b>Money Limit</b>
		L Term	S Term	Viab.	Supp.	L Term	S Term	L Term	S Term		(Months)	(Months)	(£m)
NRW.BANK	Germany	AAA	F1+	-	WD	Aa1	P-1	AA	A-1+	-	12	24	60
Bank Nederlandse Gemeenten N.V.	Netherlands	AAA	F1+	-	WD	Aaa	P-1	AAA	A-1+	-	12	24	60
DBS Bank Ltd.	Singapore	AA-	F1+	aa-	WD	Aa1	P-1	AA-	A-1+	-	12	12	60
Oversea-Chinese Banking Corp. Ltd.	Singapore	AA-	F1+	aa-	WD	Aa1	P-1	AA-	A-1+	-	12	12	60
United Overseas Bank Ltd.	Singapore	AA-	F1+	aa-	WD	Aa1	P-1	AA-	A-1+	-	12	12	60
Svenska Handelsbanken AB	Sweden	AA	F1+	aa	WD	Aa2	P-1	AA-	A-1+	-	12	12	60
First Abu Dhabi Bank PJSC	UAE	AA-	F1+	a-	WD	Aa3	P-1	AA-	A-1+	-	12	12	60
Bank of New York Mellon	USA	AA	F1+	aa-	WD	Aa1	P-1	AA-	A-1+	-	12	12	60

<b>Yellow</b>	<b>Purple</b>	<b>Blue</b>	<b>Orange</b>	<b>Red</b>	<b>Green</b>	<b>No Colour</b>
<i>Up to 5yrs</i>	<i>Up to 2yrs</i>	<i>Up to 1yr (semi nationalised UK banks)</i>	<i>Up to 1yr</i>	<i>Up to 6 months</i>	<i>Up to 100 days</i>	<i>Not to be used</i>

<b>Non-Specified Investments:</b>			
	<b>Minimum credit Criteria</b>	<b>Maximum Investments</b>	<b>Period</b>
UK Local Authorities	Government Backed	£60m	2 years
Corporate Bond Fund(s)	Investment Grade	£30m	2 – 5 years
Pooled Property Fund(s)	N/A	£30m	5+ years
Mixed Asset Fund(s)	N/A	£30m	2 - 5 years
Short Dated Bond Fund(s)	N/A	£30m	2 - 5 years

## ECONOMIC OVERVIEW

### Provided by Link Asset Services December 2022

Against a backdrop of stubborn inflationary pressures, the easing of Covid restrictions in most developed economies, the Russian invasion of Ukraine, and a range of different UK Government policies, it is no surprise that UK interest rates have been volatile right across the curve, from Bank Rate through to 50-year gilt yields, for all of 2022.

Market commentators' misplaced optimism around inflation has been the root cause of the rout in the bond markets with, for example, UK, EZ and US 10-year yields all rising by over 200bps since the turn of the year. The table below provides a snapshot of the conundrum facing central banks: inflation is elevated but labour markets are extra-ordinarily tight, making it an issue of fine judgment as to how far monetary policy needs to tighten.

Q2 of 2022 saw UK GDP revised upwards to +0.2% q/q, but this was quickly reversed in the third quarter, albeit some of the fall in GDP can be placed at the foot of the extra Bank Holiday in the wake of the Queen's passing. Nevertheless, CPI inflation has picked up to what should be a peak reading of 11.1% in October, although with further increases in the gas and electricity price caps pencilled in for April 2023, and the cap potentially rising from an average of £2,500 to £3,000 per household, there is still a possibility that inflation will spike higher again before dropping back slowly through 2023.

	<b>UK</b>	<b>Eurozone</b>	<b>US</b>
<b>Bank Rate</b>	3.0%	1.5%	3.75%-4.00%
<b>GDP</b>	-0.2%q/q Q3 (2.4%/y/y)	+0.2%q/q Q3 (2.1%/y/y)	2.6% Q3 Annualised
<b>Inflation</b>	11.1%/y/y (Oct)	10.0%/y/y (Nov)	7.7%/y/y (Oct)
<b>Unemployment Rate</b>	3.6% (Sep)	6.6% (Sep)	3.7% (Aug)

Q2 of 2022 saw UK GDP revised upwards to +0.2% q/q, but this was quickly reversed in the third quarter, albeit some of the fall in GDP can be placed at the foot of the extra Bank Holiday in the wake of the Queen's passing. Nevertheless, CPI inflation has picked up to what should be a peak reading of 11.1% in October, although with further increases in the gas and electricity price caps pencilled in for April 2023, and the cap potentially rising from an average of £2,500 to £3,000 per household, there is still a possibility that inflation will spike higher again before dropping back slowly through 2023.

The UK unemployment rate fell to a 48-year low of 3.6%, and this despite a net migration increase of c500k. The fact is that with many economic participants registered as long-term sick, the UK labour force actually shrunk by c£500k in the year to June. Without an increase in the labour force participation rate, it is hard to see how the UK economy will be able to grow its way to prosperity, and with average wage increases running at 5.5% - 6% the MPC will be concerned that wage inflation will prove just as sticky as major supply-side shocks to food and energy that have endured since Russia's invasion of Ukraine on 22nd February 2022.

Throughout Q3 Bank Rate increased, finishing the quarter at 2.25% (an increase of 1%). Q4 has seen rates rise to 3% in November and the market expects Bank Rate to hit 4.5% by May 2023.

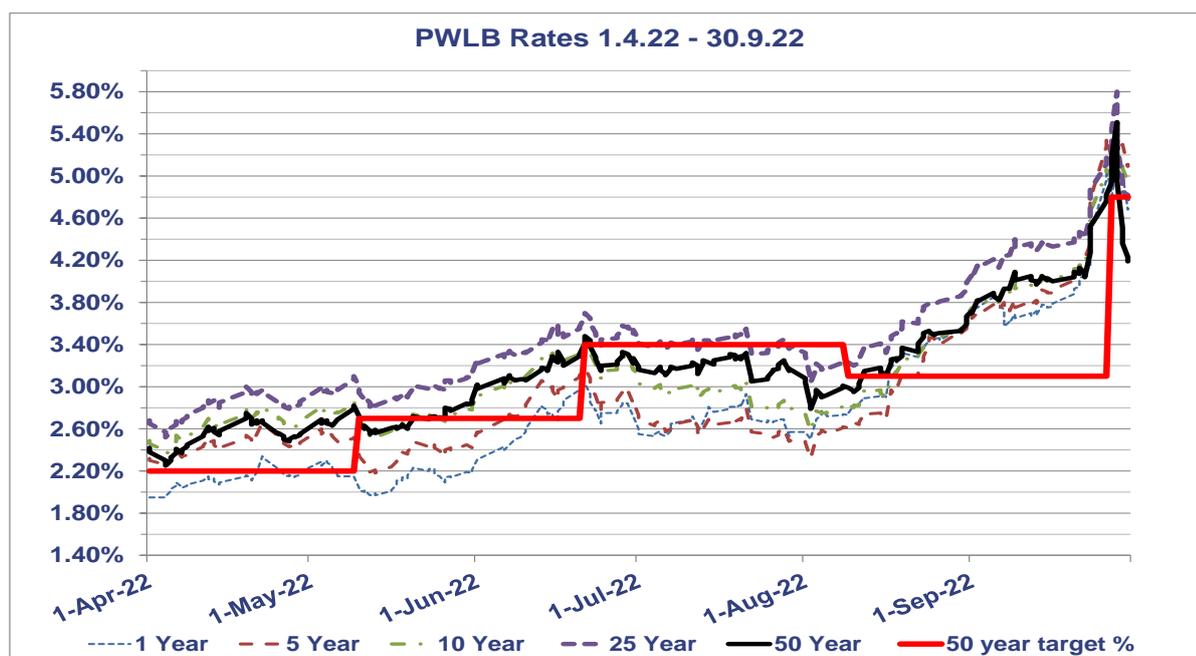
Following a Conservative Party leadership contest, Liz Truss became Prime Minister for a tumultuous seven weeks that ran through September and December. Put simply, the markets

did not like the unfunded tax-cutting and heavy spending policies put forward by her Chancellor, Kwasi Kwarteng, and their reign lasted barely seven weeks before being replaced by Prime Minister Rishi Sunak and Chancellor Jeremy Hunt. Their Autumn Statement of 17<sup>th</sup> November gave rise to a net £55bn fiscal tightening, although much of the “heavy lifting” has been left for the next Parliament to deliver. However, the markets liked what they heard, and UK gilt yields have completely reversed the increases seen under the previous tenants of No10/11 Downing Street.

Globally, though, all the major economies are expected to struggle in the near term. The fall below 50 in the composite Purchasing Manager Indices for the UK, US, EZ and China all point to at least one if not more quarters of GDP contraction. In November, the MPC projected eight quarters of negative growth for the UK lasting throughout 2023 and 2024, but with Bank Rate set to peak at lower levels than previously priced in by the markets and the fiscal tightening deferred to some extent, it is not clear that things will be as bad as first anticipated by the Bank.

The £ has strengthened of late, recovering from a record low of \$1.035, on the Monday following the Truss government’s “fiscal event”, to \$1.20. Notwithstanding the £’s better run of late, 2023 is likely to see a housing correction of some magnitude as fixed-rate mortgages have moved above 5% and affordability has been squeezed despite proposed Stamp Duty cuts remaining in place.

In the table below, the rise in gilt yields, and therein PWLB rates, through the first half of 2022/23 is clear to see.



However, the peak in rates on 28<sup>th</sup> September as illustrated in the table covering April to September 2022 below, has been followed by the whole curve shifting ever lower. PWLB rates at the front end of the curve are generally over 1% lower now whilst the 50 years is over 1.75% lower.

	1 Year	5 Year	10 Year	25 Year	50 Year
<b>Low</b>	1.95%	2.18%	2.36%	2.52%	2.25%
<b>Date</b>	01/04/2022	13/05/2022	04/04/2022	04/04/2022	04/04/2022
<b>High</b>	5.11%	5.44%	5.35%	5.80%	5.51%
<b>Date</b>	28/09/2022	28/09/2022	28/09/2022	28/09/2022	28/09/2022
<b>Average</b>	2.81%	2.92%	3.13%	3.44%	3.17%
<b>Spread</b>	3.16%	3.26%	2.99%	3.28%	3.26%

After a shaky start to the year, the S&P 500 and FTSE 100 have climbed in recent weeks, albeit the former is still 17% down and the FTSE 2% up. The German DAX is 9% down for the year.

## Prospect for Interest Rates

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Link provided the following forecasts on 19 December 22. These are forecasts for certainty rates, gilt yields plus 80 bps

Link Group Interest Rate View 19.12.22													
	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
BANK RATE	3.50	4.25	4.50	4.50	4.50	4.00	3.75	3.50	3.25	3.00	2.75	2.50	2.50
3 month ave earnings	3.60	4.30	4.50	4.50	4.50	4.00	3.80	3.30	3.00	3.00	2.80	2.50	2.50
6 month ave earnings	4.20	4.50	4.60	4.50	4.20	4.10	3.90	3.40	3.10	3.00	2.90	2.60	2.60
12 month ave earnings	4.70	4.70	4.70	4.50	4.30	4.20	4.00	3.50	3.20	3.10	3.00	2.70	2.70
5 yr PWLB	4.20	4.20	4.20	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.20	3.10
10 yr PWLB	4.30	4.40	4.40	4.30	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.30
25 yr PWLB	4.60	4.60	4.60	4.50	4.40	4.20	4.10	4.00	3.90	3.70	3.60	3.50	3.50
50 yr PWLB	4.30	4.30	4.30	4.20	4.10	3.90	3.80	3.70	3.60	3.50	3.30	3.20	3.20

Our central forecast reflects a view that the MPC will be keen to demonstrate its anti-inflation credentials by delivering a succession of rate increases. This has happened throughout 2022, but the new Government's policy of emphasising fiscal rectitude will probably mean Bank Rate does not now need to increase to further than 4.5%.

Further down the road, we anticipate the Bank of England will be keen to loosen monetary policy when the worst of the inflationary pressures have lessened – but that timing will be one of fine judgment: cut too soon, and inflationary pressures may well build up further; cut too late and any downturn or recession may be prolonged.

The CPI measure of inflation will peak at close to 11% in Q4 2022. Despite the cost-of-living squeeze that is still taking shape, the Bank will want to see evidence that wages are not spiralling upwards in what is evidently a very tight labour market. Wage increases, excluding bonuses, are currently running at 5.7%.

Regarding the plan to sell £10bn of gilts back into the market each quarter (Quantitative Tightening), this has started but will focus on the short to medium end of the curve for the present. This approach will prevent any further disruption to the longer end of the curve following on from the short-lived effects of the Truss/Kwarteng unfunded dash for growth policy.

In the upcoming months, our forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but the on-going conflict between Russia and Ukraine. (More recently, the heightened tensions between China/Taiwan/US also have the potential to have a wider and negative economic impact.)

On the positive side, consumers are still estimated to be sitting on over £160bn of excess savings left over from the pandemic so that will cushion some of the impact of the above challenges. However, most of those are held by more affluent people whereas lower income families already spend nearly all their income on essentials such as food, energy and rent/mortgage payments.

## PWLB RATES

Yield curve movements have become less volatile under the Sunak/Hunt government. PWLB 5 to 50 years Certainty Rates are, generally, in the range of 3.75% to 4.50%. The medium to longer

part of the yield curve is currently inverted (yields are lower at the longer end of the yield curve compared to the short to medium end).

We view the markets as having built in, already, nearly all the effects on gilt yields of the likely increases in Bank Rate and the poor inflation outlook but markets are volatile and further whipsawing of gilt yields across the whole spectrum of the curve is possible.

**The balance of risks to the UK economy: -**

- The overall balance of risks to economic growth in the UK is to the downside. Indeed, the Bank of England projected two years of negative growth in their November Quarterly Monetary Policy Report.

**Downside risks to current forecasts for UK gilt yields and PWLB rates include: -**

- **Labour and supply shortages** prove more enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, rising gilt yields).
- **The Bank of England** acts too quickly, or too far, over the next two years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- **UK / EU trade arrangements** – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.
- **Geopolitical risks**, for example in Ukraine/Russia, China/Taiwan/US, Iran, North Korea and Middle Eastern countries, which could lead to increasing safe-haven flows.

**Upside risks to current forecasts for UK gilt yields and PWLB rates: -**

- 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 and for a longer period within the UK economy, which then necessitates an even more rapid series of increases in Bank Rate faster than we currently expect.
- **The Government** acts too slowly to increase taxes and/or cut expenditure to balance the public finances, in the light of the cost-of-living squeeze.
- **The pound weakens** because of a lack of confidence in the UK Government's fiscal policies, resulting in investors pricing in a risk premium for holding UK sovereign debt.
- Longer term **US treasury yields** rise strongly, if inflation numbers disappoint on the upside, and pull gilt yields up higher than currently forecast.

**Borrowing advice:** Our long-term (beyond 10 years) forecast for Bank Rate stands at 2.5%. As all PWLB certainty rates are now above this level, borrowing strategies will need to be reviewed in that context. Better value can generally be obtained at the shorter end of the curve and short-dated fixed LA to LA monies should be considered. Temporary borrowing rates are likely, however, to remain near Bank Rate and may also prove attractive whilst the market waits for inflation, and therein gilt yields, to drop back later in 2023.

Our suggested budgeted earnings rates for investments up to about three months' duration in each financial year are as follows: -

Average earnings in each year	
2022/23 (remainder)	3.95%
2023/24	4.40%
2024/25	3.30%
2025/26	2.60%
2026/27	2.50%
Years 6 to 10	2.80%
Years 10+	2.80%

As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts.

Our interest rate forecast for Bank Rate is in steps of 25 bps, whereas PWLB forecasts have been rounded to the nearest 10 bps and are central forecasts within bands of + / - 25 bps. Naturally, we continue to monitor events and will update our forecasts as and when appropriate.

## PRUDENTIAL AND TREASURY INDICATORS 2023/24 to 2025/26

The Council's capital expenditure plans are a key driver of treasury management activities. The output of the capital expenditure plans is reflected in prudential indicators. Local Authorities are required to 'have regard to' the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable. The Code sets out the indicators that must be used but does not suggest limits or ratios as these are for the authority to set itself.

The Prudential Indicators for 2023/24 to 2025/26 are set out in **Table A** below:

<b>Table A</b>	<b>2023/24 Estimate</b>	<b>2024/25 Estimate</b>	<b>2025/26 Estimate</b>
<b>Capital Expenditure £m (gross)</b> Council's capital expenditure plans	£97m	£102m	£61m
<b>Capital Financing Requirement £m*</b> Measures the underlying need to borrow for capital purposes (including PFI & Leases)	£366m	£421m	£435m
<b>Ratio of financing costs to net revenue stream**</b> Identifies the trend in the cost of capital (borrowing and other long term obligation costs) against net revenue stream	3.71%	3.89%	4.50%

\* From 2024/25, the CFR includes an estimate for leases that will be bought onto the balance sheet under a change in leasing accounting regulations.

\*\* the ratio of financing costs to net revenue stream illustrates the percentage of the Council's net revenue budget being used to finance the council's borrowing. This includes interest costs relating to the council's borrowing portfolio and MRP. This was previously reported net of the investment income from the council's investment portfolio, but this is no longer allowable under the 2021 Code, and therefore the ratio is higher than previously reported.

The Treasury Management Code requires that Local Authorities set a number of indicators for treasury performance in addition to the Prudential Indicators which fall under the Prudential Code. The Treasury Indicators for 2023/24 to 2025/26 are set out in **Tables B & C** below. These have been calculated and determined by Officers in compliance with the Treasury Management Code of Practice.:

<b>Table B</b>	<b>2023/24 Estimate</b>	<b>2024/25 Estimate</b>	<b>2025/26 Estimate</b>
<b>Authorised Limit for External Debt £m*</b> The Council is expected to set a maximum authorised limit for external debt. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by Full Council.	£396m	£451m	£465m
<b>Operational boundary for external debt £m*</b> The Council is required to set an operational boundary for external debt. This is the limit which external debt is not normally expected to exceed. This indicator may be breached temporarily for operational reasons.	£376m	£431m	£445m
<b>Principal Sums invested for longer than 365 days</b>	£60m	£60m	£60m

<b>Control on interest rate exposure: Upper limit for fixed interest rate exposure</b> Identifies a maximum limit for fixed interest rates for borrowing and investments.	100%	100%	100%
<b>Control on interest rate exposure: Upper limit for variable interest rate exposure</b> Identifies a maximum limit for variable interest rates for borrowing and investments.	15%	15%	15%

*\*From 2024/25 The Authorised Limit and Operational Boundary includes an estimate for leases that will be bought onto the balance sheet under a change in leasing accounting regulations.*

<b>Table C</b>		
<b>Maturity Structure of fixed interest rate borrowing</b>		
The Council needs to set upper and lower limits with respect to the maturity structure of its borrowing.		
	Lower	Upper
Under 12 months	0%	25%
12 months to 2 years	0%	40%
2 years to 5 years	0%	60%
5 years to 10 years	0%	70%
Over 10 years	0%	90%

## SCHEME OF DELEGATION

### 1. Full Council

In line with best practice, Full Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals. These reports are:

#### i. Treasury Management Policy and Strategy Report

The report covers:

- the capital plans (including prudential indicators);
- the Capital Strategy;
- a Minimum Revenue Provision 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).

#### ii. A Mid-Year Review Report and a Year End Stewardship Report

These will update members with the progress of the capital position, amending prudential indicators as necessary, and indicating whether the treasury strategy is meeting the strategy or whether any policies require revision. The report also provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

### 2. Cabinet

- Approval of the Treasury Management quarterly update reports;
- Approval of the Treasury Management outturn report.

### 3. Audit Committee

- Scrutiny of performance against the strategy.

### 4. Role of the Section 151 Officer

The Section 151 (responsible) Officer:

- 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.

There are further responsibilities for the S151 Officer identified within the 2017 Code in respect of non-financial investments. They are identified and listed in the Capital Strategy where relevant.

## INVESTMENT PRODUCT GLOSSARY

**Bank / Building Society:** 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.

**Bank / Building Society Secured (Covered Bonds):** These investments are secured on the bank's assets, which limit the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in.

**Corporate Bonds:** Bonds 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.

**Enhanced Cash / Ultra Short Dated Bond Funds:** Funds designed to produce an enhanced return over and above a Money Market Fund. The manager may use a wider range of alternative options to try and generate excess performance. These could include different counterparties, instruments as well as longer dated investments.

**Equity Fund:** Equity funds are pooled investment vehicles that will focus investments primarily in UK equities.

**Government:** Loans, bonds and bills issued or guaranteed by UK government, local authorities and supranational banks. These investments are not subject to bail-in, and there is a minimal risk of insolvency.

**Money Market Funds:** An open ended fund that invests in short term debt securities, offers same-day liquidity and very low volatility.

**Mixed Asset Funds:** Rather than focus on a particular asset class, these funds will look to invest across a broader range of classes in an effort to provide investors with a smoother performance on a year-to-year basis. Primarily, the asset classes will be equities and fixed income, but the latter will include both corporate and government-level investments.

**Pooled Property Funds:** Shares in diversified property investment vehicles. Property funds offer enhanced returns over the longer term but are more volatile in the short term. The funds have no defined maturity date, but are available for withdrawal after a notice period

**Short Dated Bond Funds:** Funds designed to produce an enhanced return over and above an Ultra Short Dated Fund. The manager may use a wider range of alternative options to try and generate excess performance. These could include different counterparties, instruments as well as longer dated and a proportion of lower rated investments. The return on the funds are typically much higher but can be more volatile than Ultra-Short Dated bond funds, so a longer investment time horizon is recommended.