

APPENDIX N

## **TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2021/22**

### **Statement Preparation**

1. This strategy statement has been prepared in accordance with the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management in the Public Services Code of Practice (the Code). Accordingly, the Council's Treasury Management Strategy will be approved annually by the full Council and there will be quarterly reports to the Corporate Governance Committee. The Corporate Governance Committee considered the contents of the Treasury Management Strategy Statement and Annual Investment Strategy at its meeting on 29 January 2021. The aim of these reporting arrangements is to ensure that those with ultimate responsibility for the treasury management function appreciate fully the implications of treasury management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

The Council has adopted the following reporting arrangements in accordance with the requirements of the Code:

<b>Area of Responsibility</b>	<b>Council/Committee/Officer</b>	<b>Frequency</b>
Treasury Management Policy Statement	Full Council	Annually before start of financial year
Treasury Management Strategy/Annual Investment Strategy	Full Council	Annually before start of financial year
Quarterly Treasury Management updates	Corporate Governance Committee	Quarterly
Updates or revisions to Treasury Management Strategy/Annual Investment Strategy during year	Cabinet (following consideration by Corporate Governance Committee, wherever practical)	Ad hoc
Annual Treasury Outturn Report	Cabinet	Annually by end of September following year end
Treasury Management Practices	Director of Corporate Resources	
Review of Treasury Management Strategy/Annual Investment Strategy	Corporate Governance Committee	Annually before start of financial year and before consideration by full Council, wherever practical
Review of Treasury Management Performance	Corporate Governance Committee	Annually by end of September following year end

## **Treasury Management Strategy 2021/22**

2. The Local Government Act 2003 (the Act) and supporting regulations requires the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

The Act requires the Council to set its treasury strategy for borrowing and to prepare an Annual Investment strategy (for Treasury Management investments) - this is included in later paragraphs of this strategy. It sets out the Council's policies for managing its Treasury Management investments and for giving priority to the security and liquidity of those investments.

This Strategy should be read in conjunction with the Corporate Asset Investment Fund (CAIF) strategy, which sets out the Council's approach when considering the acquisition of investments for the purposes of inclusion within the CAIF, and the Capital Strategy, which sets out the Council's approach to determining its medium term capital requirements. These documents form part of the Medium Term Financial Strategy (MTFS) and together take into account the statutory guidance issued by the Secretary of State under the Local Government Act 2003.

This proposed strategy for 2021/22 in respect of the treasury management function is based upon Officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury adviser, Link Asset Services.

### **Balanced Budget Requirement**

3. It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby the increase in charges to the revenue budget from:
  - i) increase in interest charges caused by increased borrowing to finance additional capital expenditure, and
  - ii) any increases in running costs from new capital projects

are limited to a level which is affordable within the projected income of the Council for the foreseeable future.

### **Treasury Limits for 2021/22 to 2024/25**

4. It is a statutory duty under Section 3 of the Act and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the "Affordable Borrowing Limit". In England and Wales the Authorised Limit represents the legislative limit specified in the Act.

The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax level is 'acceptable'.

Whilst termed an "Affordable Borrowing Limit" the capital plans to be considered for inclusion incorporate financing by both borrowing and other forms of liability, such as credit arrangements. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and three successive financial years. Details of the Authorised Limit can be found in Annex 2 to this Strategy.

### Current Portfolio Position

5. The Council's treasury portfolio position at 31 December 2020 was:

		Principal £m	Average Rate %
Fixed Rate Funding (borrowing)	PWLB	159.6	6.22
	Market	103.5	4.37
	Total Borrowing	263.1	5.84
Total Investments		<u>287.4</u>	0.46
Net Investment		<u>24.3</u>	

The market debt relates to structures referred to as LOBOs (Lenders Option, Borrowers Option), where the lender has certain dates when they can increase the interest rate payable and, if they do, the borrower has the option of accepting the new rate or repaying the loan. All of these LOBOs have passed the first opportunity for the lender to change the rate and as a result they are all classed as fixed rate funding, even though, in theory, the rate could change in the future.

The Council's average rate of return on its treasury investments is 0.46% (as at 30 Sep 20). This compares favourably to the average of other English Counties (0.34%).

### Capital Financing Requirement

6. The Council is forecast to be overborrowed as at 31 March 2021 by £31m. There are a number of reasons that the Council is in an 'overborrowed' position but among them are the lack of unsupported borrowing within it, a move by Central Government to switch capital approvals (which required external debt to be raised) to grants and the meaningful levels of voluntary Minimum Revenue Provision (MRP) that have been applied in recent years. In essence this is a natural position to be in if new external debt is not required, as an annual provision is made to set aside cash in advance of loans maturing. The advantage this provides the County Council is flexibility in the use of cash resources in advance of the debt becoming due.

The new MTFS includes a requirement to increase the Capital Financing Requirement (CFR) by £143m by 2024/25. This will fund essential investment in service improvement, investment for growth and invest to save projects. Due to the levels of internal cash balances, which would otherwise be available to lend to banks, of c.£143m no new external loans are forecast to be required in the short to medium term. By the end of the MTFS, 2024/25, the position will move from being over-borrowed to under borrowed by £91m.

The majority of the cash requirement includes forward funding of infrastructure in advance of developer contributions through section 106 agreements or land sales, and spend to save schemes. The expectation is that this will allow cash balances to be replenished in the next 5-10 years.

7. The table below shows how the Capital Financing Requirement is expected to change over the period of the MTFS, and how this compares to the expected level of external debt. Although the level of actual debt exceeds the Capital Financing Requirement it is currently prohibitively expensive to prematurely repay existing debt. If there are cost-effective opportunities to avoid, or reduce, an overborrowed position they will be considered as long as they are in the best long-term financial interests of the Council. This will probably require both short and long-term borrowing rates to increase meaningfully from their current level.

	2021/22 £000	2022/23 £000	2023/24 £000	2024/25 £000
<b>Opening Capital Financing Requirement</b>	<b>232,480</b>	<b>226,473</b>	<b>277,297</b>	<b>320,170</b>
New Borrowing	0	56,834	50,306	35,867
Statutory Minimum Revenue Provision (MRP)	-6,007	-6,009	-7,433	-8,693
Voluntary MRP	0	0	0	0
<b>Closing Capital Financing Requirement</b>	<b>226,473</b>	<b>277,297</b>	<b>320,170</b>	<b>347,344</b>
<b>Opening external debt</b>	<b>263,100</b>	<b>262,600</b>	<b>262,100</b>	<b>261,600</b>
Loans maturing	-500	-500	-500	-5,336
<b>Closing external debt</b>	<b>262,600</b>	<b>262,100</b>	<b>261,600</b>	<b>256,264</b>
<b>Overborrowed/(borrowing requirement)</b>	<b>36,127</b>	<b>(15,197)</b>	<b>(58,570)</b>	<b>(91,080)</b>

#### Minimum Revenue Provision

8. Capital financing costs are forecast to be £19.m in 2021/22 and then rise to £23m in 2024/25, mainly as a result of increasing financing requirements for the capital requirement, partly offset by the proposed change to the minimum revenue provision (MRP) outlined below.

9. The Local Authorities (Capital Finance and Accounting) Regulations 2003 require local authorities to charge to their revenue account in each financial year a minimum amount to finance capital expenditure. This is commonly referred to as Minimum Revenue Provision.

In the context of significant medium term financial pressures the council continues to review the efficiency and effectiveness of all aspects of spend. In 2019/20 the Council reassessed the expenditure that is required under statute relating to a prudent Minimum Revenue Provision. Based on the average economic remaining life of assets held it amended the MRP calculation for supported and unsupported borrowing to a period of 40 years, which reduced the MRP charge to around £6m per annum.

The 'asset life' method is in line with the Capital Finance and Accounting Regulations 2003 and is consistent with many reviews undertaken by other Local Authorities when reviewing their MRP policy / methodology. This approach will provide for a lower charge in the earlier years and is prudent as it is built on asset life, a straight line charge, rather than reducing balance.

It should be noted that the revised approach does not change the overall amount of MRP payable; the same amount is simply repaid over a different time period, but is more aligned with the period over which the underlying assets provide benefit. Further details can be found in Annex 1 to this Strategy.

### Prudential and Treasury Indicators for 2021/22 – 2024/25

10. Prudential and Treasury Indicators (as set out in the tables in Annex 2 to this Strategy) are relevant for the purpose of setting an integrated treasury management strategy. The Council is also required to indicate that it has adopted the CIPFA Code of Practice on Treasury Management, this was adopted in February 2010.

### Prospects for Interest Rates

11. 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 11.8.20. However, following the conclusion of the review of PWLB margins over gilt yields on 25.11.20, all forecasts below have been reduced by 1%. These are forecasts for certainty rates, gilt yields plus 80bps:

Link Group Interest Rate View 9.11.20													
These Link forecasts have been amended for the reduction in PWLB margins by 1.0% from 26.11.20													
	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
5 yr PWLB	0.80	0.80	0.80	0.80	0.90	0.90	0.90	0.90	0.90	1.00	1.00	1.00	1.00
10 yr PWLB	1.10	1.10	1.10	1.10	1.20	1.20	1.20	1.20	1.20	1.30	1.30	1.30	1.30
25 yr PWLB	1.50	1.60	1.60	1.60	1.60	1.70	1.70	1.70	1.70	1.80	1.80	1.80	1.80
50 yr PWLB	1.30	1.40	1.40	1.40	1.40	1.50	1.50	1.50	1.50	1.60	1.60	1.60	1.60

12. The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its subsequent meetings to 16th December, although some forecasters had suggested that a cut into negative territory could happen. However, the Governor of the Bank of England has made it clear that he currently thinks that such a move would do more damage than good and that more quantitative easing is the favoured tool if further action becomes necessary. As shown in the forecast table above, no increase in Bank Rate is expected in the near-term as economic recovery is expected to be only gradual and, therefore, prolonged. These forecasts were based on an assumption that a Brexit trade deal would be agreed by 31.12.20: as this has now occurred, these forecasts do not need to be revised.

### **Borrowing Strategy**

13. There was much speculation during the second half of 2019 that bond markets were in a bubble which was driving bond prices up and yields down to historically very low levels. The context for that was a heightened expectation that the US could have been heading for a recession in 2020. In addition, there were growing expectations of a downturn in world economic growth, especially due to fears around the impact of the trade war between the US and China, together with inflation generally at low levels in most countries and expected to remain subdued. Combined, these conditions were conducive to very low bond yields.
14. While inflation targeting by the major central banks has been successful over the last thirty years in lowering inflation expectations, the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers. This means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. The consequence of this has been the gradual lowering of the overall level of interest rates and bond yields in financial markets over the last 30 years. Over the year prior to the coronavirus crisis, this has seen many bond yields up to 10 years turn negative in the Eurozone. In addition, there has, at times, been an inversion of bond yields in the US whereby 10 year yields have fallen below shorter term yields. In the past, this has been a precursor of a recession. The other side of this coin is that bond prices are elevated as investors would be expected to be moving out of riskier assets i.e. shares, in anticipation of a downturn in corporate earnings and so selling out of equities.
15. Gilt yields had therefore already been on a generally falling trend up until the coronavirus crisis hit western economies during March 2020. After gilt yields spiked up during the financial crisis in March, we have seen these yields fall sharply to unprecedented lows as investors panicked during March in selling shares in anticipation of impending recessions in western economies, and moved cash into safe haven assets i.e. government bonds. However, major western central banks took rapid action to deal with excessive stress in financial markets during March, and started massive quantitative easing

purchases of government bonds: this also acted to put downward pressure on government bond yields at a time when there has been a huge and quick expansion of government expenditure financed by issuing government bonds. Such unprecedented levels of issuance in “normal” times would have caused bond yields to rise sharply. Gilt yields and PWLB rates have been at remarkably low rates so far during 2020/21.

16. As the interest forecast table for PWLB certainty rates above shows, there is expected to be little upward movement in PWLB rates over the next two years as it will take economies, including the UK, a prolonged period to recover all the momentum they have lost in the sharp recession caused during the coronavirus shut down period. From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and sharp changes in investor sentiment, (as shown on 9th November when the first results of a successful COVID-19 vaccine trial were announced). Such volatility could occur at any time during the forecast period
17. On 25.11.20, the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates; the standard and certainty margins were reduced by 1% but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three year capital programme.
18. Although borrowing from the Public Works Loans Board (PWLB) is still generally the most attractive external option available to the authority, the current overborrowed position makes the use of external borrowing unlikely. Even as the position changes from overborrowed to under borrowed there is not currently a requirement to take on external debt.
19. Borrowing rates very rarely move in one direction without there being periods of volatility, and it is sensible to maintain a flexible and proactive stance towards when borrowing should be carried out (if, indeed, any borrowing is taken). Likewise it is sensible to retain flexibility over whether short, medium or long-term funding will be taken and whether some element of variable rate funding might be attractive. Any borrowing carried out will take into account the medium term costs and risks and will not be based on minimising short term costs if this is felt to compromise the medium term financial position of the Council.

### **External v Internal Borrowing**

20. The Council currently has significant cash balances invested, and at the end of December 2020 these stood at £287m. These balances relate to a number of different items – earmarked funds, provisions, grants received in advance of expenditure and simple cash flow are some of them. A growing source of cash balances relates to the overborrowed position outlined earlier.

As mentioned earlier the new MTFS capital programme includes a funding requirement of £143m. Due to the levels of internal cash balances and the

interest return compared with the cost of raising new external debt it is more economical to temporarily utilise internal cash balances

21. The Council has, since January 2009, repaid almost £95m more of external loans than has been borrowed. There has also been no new borrowing to finance the capital programme in this period. The position is that the Council has more external borrowing than is required to fund the historic capital programme. In an ideal world action would be taken to ensure that an overborrowed position does not occur, but the reality is that this could only happen by the premature repayment of existing debt and this is currently not a cost-effective option. If an opportunity to repay debt occurs that is sensible from a financial perspective, it will be taken.
22. The balance between internal and external borrowing will be managed proactively, with the intention of minimising long-term financing costs.

#### **Policy on borrowing in advance of need**

23. The Council will not borrow in advance of need simply to benefit from earning more interest on investing the cash than is being paid on the loan. Where borrowing is required in the approved capital programme and value for money can be demonstrated by borrowing in advance this option may be taken, but only if it is felt that the money can be invested securely until the cash is required. This allows borrowing to be taken out at an opportune time rather than at the time expenditure is incurred.
24. In determining whether borrowing will be taken in advance of the need the Council will;
  - ensure that there is a clear link between the capital programme and maturity profile of existing debt which supports taking financing in advance of need
  - ensure that the revenue implications of the borrowing, and the impact on future plans and budgets have been considered
  - evaluate the economic and market factors which might influence the manner and timing of any decision to borrow
  - consider the merits (or otherwise) of other forms of funding
  - consider a range of periods and repayment profiles for the borrowing.
25. The current position in respect of the level of actual borrowing in comparison to the Capital Financing Requirement, and the move by Central Government to replace borrowing approvals for capital projects with grants, and the levels of internal cash balances, makes it extremely unlikely that external borrowing will be used within the period of the MTFS.

#### **Debt Rescheduling/Premature Debt Repayment**

26. Debt rescheduling usually involves the premature repayment of debt and its replacement with debt for a different period, to take advantage of differences in the interest rate yield curve. The repayment and replacement do not necessarily have to happen simultaneously, but would be expected to have occurred within a relatively short period of time.

27. If medium and long-term loan rates rise substantially in the coming years, there may be opportunities to adjust the portfolio to take advantage of lower rates in shorter periods. It is important that the debt portfolio is not managed to maximise short-term interest savings if this is felt to be overly risky, and a maturity profile that is overly focussed into a single year will be avoided. Changes to the way that PWLB rates are set, and the introduction of a significant gap between new borrowing costs and the rate used in calculating premia/discounts for premature debt repayments, significantly reduces the probability of debt rescheduling being attractive in the future.
28. If there is a meaningful increase in medium and long-term premature repayment rates there is a possibility that premature repayment of existing debt (without any replacement) might become attractive, particularly given the current overborrowed position. This type of action would only be carried out if it was considered likely to be beneficial in the medium term.
29. All debt rescheduling or premature repayments will be reported to the Corporate Governance Committee at the earliest meeting following the action.

## **Annual Investment Strategy**

### **Investment Policy**

30. The Council will have regard to the MHCLG's Guidance on Local Authority Investments ("the Investment Guidance") and the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities are:-
  - the security of capital and
  - the liquidity of its investments
31. The Council will aim to achieve an optimal return on its investments that is commensurate with proper level of security and liquidity. The risk appetite of this Council is low in order to give priority to security of its investments.
32. The Council's policy in respect of deciding which counterparties are acceptable has always been stringent, and is one reason that the various financial organisations that have got into financial difficulties over the years (BCCI, Northern Rock, the Icelandic Banks etc.) have not been on the list of acceptable counterparties.
33. In broad terms the list of acceptable counterparties uses the list produced by Link Asset Services (the Council's treasury management advisor) but excludes any party that is included in the Link list with a maximum loan maturity period of 100 days or less. All counterparties are also restricted to a maximum loan period of one year.

### **Creditworthiness Policy**

34. Link's methodology includes the use of credit ratings from S & P, Fitch and Moody's, factors such as credit outlook reports from the credit rating agencies,

the rating of the sovereign government in which the counterparty is domiciled and the level of Credit Default Swap spreads within the market (effectively the market cost of insuring against default). The general economic climate is also considered and will, on occasions, have an impact onto the list of suggested counterparties.

35. Link Asset Services issue timely information in respect of changes to credit ratings or outlooks, and changes to their suggested counterparty list are also issued. These reports are monitored within a short time of receipt and any relevant changes to the counterparty list are actioned as quickly as is practical. A weekly summary of the credit ratings etc. of counterparties is also issued and this gives an opportunity to ensure that no important information has been missed.

### **Country Limits**

36. The Link criteria includes a requirement for the country of domicile of any counterparty to be very highly rated. This is a requirement on the basis that it will probably be the national government which will offer financial support to a failing bank, but the country must itself be financially able to afford the support. The Council's list of acceptable counterparties will include a limit on the maximum amount that can be invested in all counterparties domiciled in a single country (except for the UK) in order to mitigate sovereign risk.

### **UK Local Authorities**

37. The counterparty list from Link does not include Local Authorities, due to credit ratings not being available for the majority of organisations. Having never defaulted in history, UK Local authorities and levying authorities are and have always been regarded as safe counterparties.
38. Despite the difficult financial situation that many organisations find themselves in the legal basis underpinning local authorities and their requirement to repay loans has not changed. It is considered very unlikely that one will be allowed to collapse and default on its debt. The language used to describe the financial position of Local authorities and companies is very similar. However, the actual position is very different. Despite Government cuts to grants Local Authorities are in control of the majority of their income, due to their tax-raising powers. To regain a balanced budget service reduction can take place without a corresponding income reduction. Companies do not have this ability and if a service is cut by them, all of the related income stops. Historically when public sector re-organisations have taken place, resulting in the cessation of one or more entities, government has nominated successor organisations. These organisations take on all of the historic assets and liabilities of the original entities. If a limited company ceases trading the known liabilities can only be settled out of the assets held by the company at that time.
39. Local authorities remain very low risk counterparties and it is extremely unlikely that loans would not be repaid in full, on time and with full interest. The

Council's treasury management advisors are aware of local authorities being on the list of authorised counterparties and are supportive of it, and comfortable that they remain low-risk counterparties. There is evidence that lending between local authorities continues to happen, including to those that have been highlighted as in very difficult financial positions.

40. The combination of all these factors produces a counterparty list, for the County Council, which comprises only very secure financial institutions, and a list that is managed pro-actively as new information is available.
41. The investment instruments identified for use in the financial year are listed below. The limits for both maximum loan periods and amounts will be set in line with the criteria shown in Annex 3. This list has changed from the one that was approved as part of the 2020/21 Annual Investment Strategy; the lending limits to individual institutions have been increased and the lending limits to money market funds (MMFs) have been rationalised.
42. The council primarily uses MMFs to store its working capital (the day to day funds required to pay for services). The key benefits to using MMFs is that they satisfy the need for capital protection (providing a level of diversification the Council would be unable to achieve on its own), whilst also remaining highly liquid – usually providing instant access.
43. The current investment strategy allows a total lending limit to MMFs of £125m and an individual limit per fund of £25m. This essentially means the council can use up to five funds at any one time. Due to the nature of these funds and the regulations surrounding their underlying investments there is, inevitably, significant overlap between the counterparty exposure within these funds. Meaning the actual diversification benefit to holding more than four funds is minimal. Using four funds allows the council to focus on the funds that are most inline with our investment objectives and reduces administration time.
44. The limit for lending to an individual money market fund will be increased from £25m to £30m.
45. The limit for lending to UK institutions (that meet the counter party list requirements) and are classed as a special Institution (part nationalised) for a period of 12 months will be increased from £50m to £70m
46. The limit for lending to UK institutions (that meet the counter party list requirements) for a period of 12 months will be increased from £40m to £50m.
47. The limit for lending to UK institutions (that meet the counter party list requirements) for a period of 6 months will be increased from £25m to £30m.
48. The limit for lending to overseas institutions (that meet the counter party list requirements) for a period of 12 months will remain at £20m. The overall country limit will remain at £30m.
49. There is a requirement within the Annual Investment Strategy to state which of the approved methods of lending are specified, and which are non-specified. In

broad terms a specified investment will be capable of repayment within one year and be made to a counterparty with a high credit rating; by implication non-specified investments are more risky than specified investments as they are either for longer periods of time or to lower-quality counterparties. Anything that does not meet either of these 'tests' is, by default, non-specified and must be highlighted as such within the Strategy. The long-term nature of the 'LOBO-offset' loan to Danske Bank means that it is non-specified investment, although the off-setting nature of the borrowing and the loan actually makes it low risk. Investment in pooled private debt funds is also non-specified, primarily due to the illiquid and medium-term nature of the investment.

Investment	Repayment within 12 months	Level of Security	Maximum Period	Maximum % of Portfolio or cash sum <sup>1</sup>
Term deposits with the Debt Management Office	Yes	Government-Backed	1 year	100%
UK Government Treasury Bills	Yes	Government-Backed	1 year	100%
Term deposits with credit-rated institutions with maturities up to 1 year <sup>2</sup> (including both ring fenced and non-ring fenced banks)	Yes	Varied acceptable credit ratings, but high security	1 year	100%
Term deposits with overseas banks domiciled within a single country.	Yes	Varied acceptable credit ratings, but high security	1 year	£30m
Term deposits that are legally capable of offset against existing LOBO borrowing that the Council has <sup>3</sup>	No	Varied, but off-setting nature of borrowing against loan gives a very low risk	20 years	25%
Money Market Funds: Constant NAV <sup>4</sup> Low Volatility NAV <sup>5</sup>	Yes	At least as high as acceptable credit – rated banks	Daily, same-day redemptions and subscriptions	£125m (includes any investment in variable NAV MMFs)
Variable NAV Money Market Funds <sup>6</sup>	Yes	At least as high as acceptable credit – rated banks	Same day subscriptions, 2 – 3 day redemption period	£125m (includes any investment in other MMFs)
Pooled private debt funds	No	Diversification within pooled fund and historic loss rate suggests high security	Varies across funds – likely to be at least a three year investment period, followed by a further three years to redeem all loans	£40m (£20m plus temp £20m overlap at renewal)

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Term Deposits with UK Local Authorities up to 1 year	Yes	LA's do not have credit ratings, but high security	1 year	50%
Certificates of Deposit with credit-rated institutions with maturities of up to 1 year	Yes	Varied acceptable credit ratings, but high security	1 year	100%

- (1) As the value of the investment portfolio is variable, the limit applies at time of agreeing the investment. Subsequent changes in the level of the portfolio will not be classed as a breach of any limits.
- (2) For administrative purposes a commitment may need to be made in advance of the investment period commencing. To avoid being overexposed with a counterparty this will be kept to a few days.
- (3) Non-specified investment
- (4) Funds where the capital value of a unit will always be maintained at £1. These funds have to maintain at least 99.5% of their assets in government backed assets.
- (5) Funds are permitted to maintain the unit price at £1 as long as the net asset value does not deviate by more than 0.20% from this level.
- (6) Funds will value their units on the basis of the underlying value of the assets that they hold; the unit price will not necessarily always be exactly £1
50. Following the lasting implications of the COVID-19 pandemic, in particular, the demonstration that unforeseeable events can very quickly cause significant uncertainty and shock financial markets. It is recognised that in exceptional circumstances the Director of Corporate Resources, in order to protect capital balances and liquidity, may have to take immediate action that breaches the above policy on a temporary basis. The action will only be taken as a last resort and will be reported, along with the rationale behind it, to the Corporate Governance Committee at the first opportunity.

### **Pooled Property Fund Investment**

51. As at the end of December 2020 £25m had been invested. This is classified as a service investment, rather than a treasury management investment.

### **Investment Strategy**

52. The investment strategy shall be to only invest in those institutions and/or asset types that are included in the counterparty list, and only to lend up to the limit set for each counterparty. Periods for which loans are placed will take into account the outlook for interest rates and, to a lesser extent, the need to retain cash flows. There may be occasions when it is necessary to borrow to fund short-term cashflow issues, but there will generally be no deliberate intention to make regular borrowing necessary.

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

53. External investment managers will not be used, except to the extent that a Money Market Fund or the managers of pooled property or private debt funds can be considered as an external manager.
54. The Council uses Link Asset Services as its external treasury management adviser, but recognises that responsibility for treasury management decisions

remains with the Council at all times. Undue reliance on the Council's external advisers will be avoided, although the value of employing an external adviser and accessing specialist skills and resources is recognised.

### **Scheme of Delegation**

55. (i) Full Council
- Approval of annual strategy
  - Other matters where full Council approval is required under guidance or statutory requirement
- (ii) Cabinet
- Approval of updates or revisions to strategy during the year
  - Approval of Annual Treasury Outturn report
- (iii) Corporate Governance Committee
- Mid-year treasury management updates (usually quarterly)
  - Review of treasury management policy and procedures, including making recommendations to responsible body
  - Scrutiny of Treasury Management Strategy/Annual Investment Strategy and Annual Treasury Outturn report.
- (iv) Director of Corporate Resources
- Day-to-day management of treasury management, within agreed policy
  - Appointment of external advisers, within existing Council procurement procedures.

### **Role of Section 151 Officer**

56. The Section 151 Officer is the Director of Corporate Resources, who has responsibility for the day-to-day running of the treasury management function.

### **Pension Fund Cash**

57. The Council will comply with the requirements of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009, which were implemented on 1<sup>st</sup> January 2010, and will not pool pension fund cash with its own cash balances for investment purposes. Any investments made by the pension fund directly with the County Council after 1<sup>st</sup> April 2010 will comply with the requirements of SI 2009 No 3093. From time to time the Council will manage short term cash flow requirements for either the County Council or the Pension Fund on a non-beneficial basis.

### **Eastern Shires Purchasing Organisation (ESPO)**

58. As part of the service level agreement with ESPO, the council provides a treasury management service on behalf of ESPO for investment of surplus balances. This service is carried out with due regard to this policy and responsibility for day to day management lies with the Director of Corporate Resources. Surplus balances are invested in their own right and not pooled with the county council.

**ANNEX 1**

**ANNUAL STATEMENT FOR THE DETERMINATION OF THE  
ANNUAL MINIMUM REVENUE PROVISION (MRP)**

Statutory regulations introduced in 2008 require local authorities to make prudent provision for the repayment of debt raised to finance capital expenditure. In addition a statement of the level of MRP has to be submitted to the County Council for approval before the start of the next financial year.

**Prudent Provision.**

The definition of what is prudent provision is determined by each local authority based on guidance rather than statutory regulation

**It is proposed that provision is made on the following basis:**

**Government supported borrowing:**

Provision to be based on the estimated life of the asset to be financed from government borrowing with repayments by equal annual instalments.

The extent of borrowing required to finance the capital programme is not directly linked to any specific projects thus in determining the average life of assets an average of 40 years has been taken as a proxy for the average life of assets.

Prudential (unsupported) borrowing and expenditure capitalised by direction of the Secretary of State and certain other expenditure classified as capital incurred after 1 April 2008:

Provision to be based on the estimated life of the asset to be financed by that borrowing, with repayment by equal annual instalments.

The extent of borrowing required to finance the capital programme is not directly linked to any specific projects thus in determining the average life of assets an average of 40 years has been taken as a proxy for the average life of assets.

The County Council will also look to take opportunities to use general underspends and one-off balances to make additional (voluntary) revenue provision where possible to reduce ongoing capital financing costs. As at 31 March 2020, the cumulative amount of voluntary MRP paid in advance is £47.8m.

**Financial Implications**

MRP is a constituent of the Financing of Capital budget shown within Central Items component of the revenue budget and for 2020/21 totals £6.0m. This comprises £5.8m in respect of supported borrowing and £0.2m in respect of unsupported borrowing incurred since 2008/9.

## ANNEX 2

### PRUDENTIAL AND TREASURY INDICATORS

In line with the requirements of the CIPFA Prudential Code for Capital Finance in local authorities, the various indicators that inform authorities whether their capital investment plans are affordable, prudent and sustainable, are set out below.

A further key objective of the code is to ensure that treasury management decisions are taken in accordance with good professional practice and in a manner that supports prudence, affordability and sustainability. The indicators for Treasury management are set out in this paper.

Compliance with the Code is required under Part I of the Local Government Act 2003.

	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
Capital Expenditure	£113m	£153m	£145m	£176m	£126m	£113m
Capital financing requirement	£238m	£232m	£237m	£277m	£320m	£347m
Ratio of total financing costs to net revenue stream	4.9%	3.8%	4.1%	4.2%	4.4%	4.6%

The projected level of capital expenditure shown above differs from the total of the detailed four year programme presented in this report as an allowance has been provided to cover estimated additional expenditure that may occur during the course of a year, for instance projects funded by government grants, section 106 contributions and projects funded from the future developments programme.

The capital financing requirement (CFR) measures the Authority's need to borrow for capital purposes and as such is influenced by the availability of capital receipts and income from third parties, e.g. grants and developer contributions. The CFR is increasing during the MTFS period for essential investment in services, investment for growth and invest to save projects.

The prudential code includes the following as a key indicator of prudence:

'In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that net external borrowing does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years'. In the short term this indicator will not be met due to the reduction in the capital financing requirement in recent years and the currently prohibitively expensive premiums to repay existing debt. The Council will consider options to reduce this position where they are in the long term financial interests of the Council. Further details are included in the main Treasury Management Strategy Statement and Annual Investment Strategy 2021/22.

In respect of external debt, it is recommended that the Council approves the limits detailed in the tables below for its total external debt for the next four financial years. These limits separately identify borrowing from other long term liabilities such as finance leases. The Council is asked to approve these limits and to delegate

authority to the Director of Corporate Resources, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities. Any such changes made will be reported to the Cabinet at its next meeting following the change.

There are two limits on external debt: the 'Operational Boundary' and the 'Authorised Limit'. Both are consistent with the current commitments, existing plans and the proposals in the budget report for capital expenditure and financing, and with approved treasury management policy statement and practices. They are both based on estimates of most likely, but not worst case, scenario. The key difference is that the Authorised Limit cannot be breached without prior approval of the County Council. It therefore includes more headroom to take account of eventualities such as delays in generating capital receipts, forward borrowing to take advantage of attractive interest rates, use of borrowing in place of operational leasing, "invest to save" projects, occasional short term borrowing to cover temporary revenue cash flow shortfalls as well as an assessment of risks involved in managing cash flows. The Operational Boundary is a more realistic indicator of the likely position.

#### Operational boundary for external debt

	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m
Borrowing	263	263	262	262
Other long term liabilities	1	1	1	1
<b>Total</b>	<b>264</b>	<b>264</b>	<b>263</b>	<b>263</b>

#### Authorised limit for external debt

	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m
Borrowing	273	273	272	272
Other long term liabilities	1	1	1	1
<b>Total</b>	<b>274</b>	<b>274</b>	<b>273</b>	<b>273</b>

In agreeing these limits, the Council is asked to note that the authorised limit determined for 2021/22 will be the statutory limit determined under Section 3(1) of the Local Government Act 2003.

#### Comparison of original 2020/21 indicators with the latest forecast

In February 2020 the County Council approved certain prudential limits and indicators, the latest projections of which are shown below:

	Prudential Indicator 2020/21	Latest Projection 15/12/20
Actual Capital Financing Costs as a % of Net Revenue Stream	3.80%	3.80%
Capital Expenditure	£161m	£153m
Operational Boundary for External Debt	£265.3m	£265.3m
Authorised Limit for External Debt	£275.3m	£275.3m
Interest Rate Exposure – Fixed	50-100%	100%
Interest Rate Exposure – Variable	0-50%	0%
Capital Financing Requirement	£247m	£232m

All of the indicators are within the targets set. The latest forecast of external debt, £263.1m, shows that it is within both the authorised borrowing limit and the operational boundary set for 2020/21. The maturity structure of debt is within the indicators set. The latest projection for capital expenditure is below the indicator set, due to slippage in the current year's capital programme.

### **Treasury Management Indicators**

The Local Government Act 2003 requires the County Council to ensure that treasury management is carried out with good professional practice. The Prudential Code includes the following as the required indicators in respect of treasury management:

- a) Upper limits on fixed interest and variable rate external borrowing.
- b) Upper and lower limits for the maturity structure of borrowings.
- c) Upper limit for principal sums invested for periods longer than 364 days.

After reviewing the current situation and assessing the likely position next year, the following limits are recommended:

- a) An upper limit on fixed interest rate exposures for 2021/22 to 2024/25 of 100% of its net outstanding principal sums and an upper limit on its variable interest rate exposures for 2021/22 to 2024/25 of 50% of its net outstanding principal sums.
- b) Upper and lower limits for the maturity structure of its borrowings as follows:  
Amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate:

	Upper Limit %	Lower Limit%
under 12 months	30	0
12 months and within 24 months	30	0
24 months and within 5 years	50	0
5 years and within 10 years	70	0
10 years and above	100	25

- c) An upper limit for principal sums invested for periods longer than 364 days is 10% of the portfolio.

The County Council has adopted the CIPFA code of Practice for Treasury Management in the Public Services.

**ANNEX 3**

**POLICY ON APPROVED ORGANISATIONS FOR LENDING**

**APPROVED ORGANISATIONS/ LIMITS FOR LENDING**

<u>Institution*</u>	<u>Maximum Sum Outstanding/Period of Loan</u>
UK Clearing Banks and UK Building Societies**	£30m/6 months up to £50m/12months (Not special Institutions) £70m/12months (special Institutions) 'Special' = significant element of UK government ownership.
UK Debt Management Office	No maximum sum outstanding/12 months
UK Government Treasury Bills	No maximum sum outstanding/12 months
Overseas Banks	£10m/6 months £20m/12 months
Money Market Funds	£30m limit within any AAA-rated fund. £125m maximum exposure to all Money Market Funds
UK Local Authorities	£10m/12 months
Pooled Private Debt Funds	£40m/variable 3-6 years

\* includes ring fenced and non-ring fenced banks.

\*\*In the event that an investment is entered into which is legally offset against borrowing in the form of a LOBO (Lender's Option, Borrower's Option) from the same counterparty, the maximum period will be 20 years and the maximum sum will be the amount of the LOBO deal against which the legal offset exists.

The list of acceptable institutions will mirror the list of suggested counterparties maintained by Link Asset Services, except the maximum maturity period will be restricted to 1 year and any institution with a suggested maturity period of 100 days or less will be excluded.

Some financial institutions have both a parent company and a subsidiary that are licensed deposit takers in the UK. Where this is the case a 'group limit' will apply, and this will be the limit that is given to the parent company.

In some cases the parent company will be an overseas institution and they will have UK-registered subsidiaries. Where this is the case the parent company limit will apply at a total group level, even if this limit is less than would be given to the UK subsidiary on a stand-alone basis. Any money invested with a UK subsidiary of an overseas institution will be classed as being invested in the country of domicile of the parent, if the parent is an overseas institution for country-maximum purposes.

If the credit rating of an individual financial institution decreases to a level which no longer makes them an acceptable counterparty the Director of Corporate Resources will take action to bring this back into line at the earliest opportunity. It should be noted that there will be no legal right to cancel a loan early, and any premature repayment can only be made with the approval of the counterparty and may include financial penalties. Similar actions will be taken if a counterparty is downgraded to a level which allows them to remain on the list of acceptable counterparties, but where the unexpired term of any loan is longer than the maximum period for which a new loan could be placed with them.

In the event that the circumstances highlighted above occur, the Director of Corporate Resources will report to the Corporate Governance Committee.

## **ANNEX 4**

### **TREASURY MANAGEMENT POLICY STATEMENT (TMPS)**

1. This organisation 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”
2. This organisation 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 organisation.
3. This organisation 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 measurement techniques, within the context of effective risk management.