OVERVIEW AND SCRUTINY ITEM, DRAFT FOR CONSIDERATION PRIOR TO FULL COUNCIL

RYEDALE DISTRICT COUNCIL

REPORT TO:	**COUNCIL**
DATE:	**20 FEBRUARY 2020**
REPORT OF THE:	**CHIEF FINANCE OFFICER (s151) ANTON HODGE**
TITLE OF REPORT:	**TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2020/21**
WARDS AFFECTED:	**ALL**

EXECUTIVE SUMMARY

1.0 PURPOSE OF REPORT

1.1 To consider the Treasury Management, Annual Investment and Capital Strategies, the Minimum Revenue Provision Policy and Prudential Indicators for 2019/20, as required by the Ministry of Housing, Communities and Local Government and CIPFA (as updated 2017)..

2.0 RECOMMENDATIONS

2.1 That Council is recommended to approve:

(i) Members receive this report;

(ii) The Operational Borrowing Limit for 2020/21 is set at £6m;

(iii) The Authorised Borrowing Limit for 2020/21 is set at £11.5m;

(iv) Councillors delegate authority to the Chief Finance Officer to effect movement within the agreed authorised boundary limits for long-term borrowing for 2020/21 onwards.

(v) Councillors delegate authority to the Chief Finance Officer to effect movement within the agreed operational boundary limits for long-term borrowing for 2020/21 onwards.

(vi) The treasury management strategy statement 2020/21 be approved.

(vii) The minimum revenue provision policy statement for 2020/21 be approved.

(viii) The treasury management investment strategy for 2020/21 be approved.

(ix) The prudential indicators for 2020/21 which reflect the capital expenditure plans which are affordable, prudent and sustainable be approved.

(x) The Capital Strategy for 2020/21 be approved

3.0 REASON FOR RECOMMENDATIONS

3.1 To ensure the Council's Treaury Management Strategy and association policies are prudent and affordable.

4.0 SIGNIFICANT RISKS

4.1 There are significant risks when investing public funds especially with unknown institutions. However, by the adoption of the CIPFA Code and a prudent investment policy, these are minimised. The employment of Treasury Advisors also helps reduce the risk.

5.0 POLICY CONTEXT AND CONSULTATION

5.1 The Council has adopted the CIPFA Code of Practice on Treasury Management in Local Authorities and this report complies with the requirements under this code and the relevant requirements of the Local Government Act 2003.

5.2 The Council use the services of Link Asset Services to provide treasury management information and advice.

REPORT

6.0 REPORT DETAILS

6.1 <u>TREASURY MANAGEMENT STRATEGY STATEMENT 2020/21</u>

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

6.1.2 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 any debt previously drawn may be restructured to meet Council risk or cost objectives.

6.1.3 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.

6.1.4 CIPFA defines treasury management as:

"The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

Reporting Requirements

6.1.5 Revised reporting is required from the 2019/20 reporting cycle due to revisions of the MHCLG Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a capital strategy, to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011.

6.1.6 **Capital Strategy**

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

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

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

6.1.7 **Treasury Management Reporting**

The 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 required to be adequately scrutinised by committee before being recommended to the Council. This role is undertaken by the Overview and Scrutiny Committee.

Prudential and Treasury Indicators and Treasury Strategy (this report) **–** The first and most important report covers:

- The capital plans (including prudential indicators);
- 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).

A Mid Year Treasury Management Report. This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether the treasury strategy or whether any policies require revision.

An Annual Treasury Report. This provides details of a selection of actual prudential treasury indicators and actual treasury operations compared to the estimates within the strategy.

Treasury Management Strategy for 2020/21

6.1.8 The strategy for 2020/21 covers two main areas

Capital Issues

- The capital plans and prudential indicators
- The MRP strategy

Treasury Management Issues

- The current treasury position;
- Treasury indicators which will limit the treasury risk and activities of the Council;
- Prospects for interest rates;
- The borrowing strategy;
- Policy on borrowing in advance of need;
- The investment strategy; and
- Creditworthiness policy.

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

6.1.9 **Training**

The CIPFA Code requires the Chief Finance Officer to ensure that members with responsibility for treasury management, particularly those with responsibility for scrutiny, receive adequate training in treasury management. Training has been provided to members by Link Asset Services and further training will be arranged as required.

6.1.10 **Treasury Management Consultants**

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

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

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

6.1.11 **Treasury Management Function & Sweeping Arrangements**

Included within the service level agreement which is currently being finalised with North Yorkshire County Council (NYCC) for the provision on s151 Officer and Finance services, there is provision for treasury management support.

Reporting and monitoring processes are already in place, along with day to day support for treasury activities. In the 2019/20 mid-year update, it was reported that discussions were underway between the Authorities' respective banks exploring the technical feasibility for Ryedale District Council to join NYCC's investment pool, and that prior to implementing such arrangements Ryedale District Council would be asked to formally adopt the Investment Strategy of NYCC.

Following on-going discussions, a solution for automated balances sweeping between banks has not been identified at present, although opportunities will continue to be investigated. It is therefore not proposed within the 2020/21 Investment strategy to adopt that of NYCC, but for Ryedale to continue with its own strategy until further updates on sweeping can be brought forward for approval.

6.2 THE CAPITAL PRUDENTIAL INDICATORS 2020/21 – 2022/23

Introduction

6.2.1 The 'Prudential Code' provides Council's with a regime of self-regulation for borrowing money for capital purposes. A local authority can borrow as much as it wishes as long as it can afford the repayments. The Code outlines four key objectives relating to the capital investment plans and treasury management procedures of local authorities. To demonstrate that these objectives are being fulfilled the Prudential Code sets out the indicators that must be used, and the factors that must be taken into account.

6.2.2 The Code prescribes how the issue of affordability is measured using a set of prudential indicators. The four key objectives of the Code are to ensure that capital investment plans of local authorities are affordable, prudent and sustainable, and to ensure that treasury management decisions are taken in accordance with good professional practice. The indicators are mandatory but the figures used in the calculations are a matter for each local authority.

6.2.3 The prudential indicators required by the Code are designed to support and record local decision-making. They are not designed to be comparative performance indicators and the use of them in this way would be likely to be misleading and counter-productive.

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

Capital Expenditure.

6.2.5 This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. These are currently based draft estimates and final budget proposals will be updated prior to Council approval.

Table 1: Capital Expenditure

Capital Expenditure	2018/19 Actual £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000
General Fund	842	6,705	1,285	1,177	811
Commercial Activites / Non Financial Investments	0	0	0	0	0
Total	**842**	**6,705**	**1,285**	**1,177**	**811**

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

Table 2: Financing of Capital Expenditure

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

Capital Expenditure	2018/19 Est. £'000	2019/20 Est. £'000	2020/21 Est. £'000	2021/22 Est. £'000	2022/23 Est. £'000
General Fund	842	6,705	1,285	1,177	811
Total	**842**	**6,705**	**1,285**	**1,177**	**811**
Financed By:					
Revenue & Reserves	-208	-5,768	-315	-315	-315
Capital Receipts	-27	-125	0	0	0
Grants	-607	-496	-496	-496	-496
Borrowing - Leases	0	-316	-474	-366	0
Net Financing Need	**0**	**0**	**0**	**0**	**0**

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

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

6.2.8 The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with each assets life. The Council is asked to approve the CFR projections below:

Table 3: Capital Financing Requirement

	2018/19 Est. £000	2019/20 Est. £000	2020/21 Est. £000	2021/22 Est. £000	2022/23 Est. £000
CFR General Fund	1,624	1,589	1,553	1,518	1,483
CFR GF Leases	240	323	609	780	590
CFR Commercial / Non-financial investments	0	0	0	0	0
Total CFR	**1,864**	**1,912**	**2,162**	**2,298**	**2,073**
Movement in CFR	-183	47	251	136	-225
Movement in CFR represented by:-					
Net Financing need for the year	0	0	0	0	0
Less MRP & Other Financing movements	-183	47	251	136	-225
Movement in CFR	**-183**	**48**	**251**	**136**	**-225**

6.2.9 The CFR includes any other long term liabilities (e.g. finance leases) brought onto the balance sheet. Whilst this increases the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes. These are also shown in Table 3.

Affordability Prudential Indicators

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

6.2.11 The indicator of actual and estimates of the ratio of financing costs to net revenue stream identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream. These are shown in Table 4. The estimates of financing costs include current commitments and the proposals in this report.

Table 4: Ratio of Financing Costs to Net Revenue Stream

	2018/19 Actual %	2019/20 Est. %	2020/21 Est. %	2021/22 Est. %	2022/23 Est. %
General Fund	2.06	1.54	1.08	1.08	0.97

6.3 MINIMUM REVENUE PROVISION POLICY STATEMENT 2020/21

Introduction

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

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

Minimum Revenue Provision Policy

6.3.2 The Council's MRP policy is based on the Governments Statutory Guidance and following a review no further changes are considered necessary and the policy for 2020/21 is therefore as follows:

(a) For all **Capital expenditure incurred before 1 April 2008** which formed the General Fund Capital Financing Requirement (CFR) that is capital expenditure funded through borrowing will be charged at 4% of the outstanding balance each year.

(b) From 1 April 2018 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be either:

- **Asset life method** – MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) (option 3);
- **Depreciation method** – MRP will follow standard depreciation accounting procedures (option 4);

These options provide for a reduction in the borrowing need over approximately the asset's life

Total MRP for 2020/21 is estimated at £0.223m, (£0.035 internal borrowing, and £0.188m for leases).

6.3.3 MRP Overpayments - A change introduced by the revised MHCLG MRP Guidance was the allowance that any charges made over the statutory minimum revenue provision (MRP), voluntary revenue provision or overpayments (VRP), can, if needed, be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. At present there are no plans to make voluntary revenue provisions (VRP).

6.4 BORROWING STRATEGY 2020/21

6.4.1 The capital expenditure plans provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet the service activity. 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.

6.4.2 The Council's treasury portfolio position at 31 December 2019, is shown in Table 1.

Table 1: Current Treasury Portfolio at 31/12/19

		Principal		Ave. Rate
		£m	£m	%
Fixed rate funding	PWLB	1.6		
	Market	0.0	1.6	3.49
Variable rate funding	PWLB	0.0		
	Market	0.0	0.0	0
Other long term liabilities	Leases	0.2	0.2	4.69
Total Debt			**1.8**	**4.19**
Total Investments			**30.95**	**0.90**

6.4.3 Forward projections are summarised in Table 2. The table shows the actual external borrowing (the treasury management operations), against the capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

Table 2: Forecasted Portfolio Position

	2019/20 F'cast £000	**2020/21 F'cast £000**	**2021/22 F'cast £000**	**2022/23 F'cast £000**
External Borrowing				
Borrowing at 1 April	1,553	1,513	1,474	1,434
Expected Change in Borrowing	-39	-39	-39	-39
Leases	323	609	780	590
Actual Borrowing at 31 March	**1,836**	**2,083**	**2,215**	**1,985**
CFR - the borrowing need	1,912	2,162	2,298	2,073
Under / (over) borrowing	**75**	**80**	**84**	**88**
Investments				
Total Investments	20,201	18,911	18,136	18,321
Investment Change	-1,759	-1,290	-776	186
Net Borrowing	**-18,365**	**-16,829**	**-15,921**	**-16,336**

Treasury Limits for 2020/21 to 2022/23

6.4.5 Ryedale District Council has, at any point in time, a number of cash flows both positive and negative, and manages its treasury position in terms of its borrowings and investments in accordance with its approved treasury management strategy and practices. In day-to-day cash management, no distinction can be made between revenue and capital cash. External borrowing arises as a consequence of all the financial transactions of the authority and not simply those arising from capital spending

6.4.6 CIPFA's Prudential code for Capital Finance in Local Authorities' includes the following 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 the next two financial years."

6.4.7 The Chief Finance Officer reports that the authority had no difficulty meeting this requirement in 2018/19, nor are any difficulties envisaged for the current (2019/20) or future years (2021/22 – 2022/23). This view takes into account current commitments, existing plans and the proposals in the budget.

6.4.8 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 levels is 'acceptable'. It reflects the level of external borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

6.4.9 Whilst termed an "Affordable Borrowing Limit", it incorporates the capital plans to be considered for inclusion in corporate financing by both external borrowing and other forms of liability, such as credit arrangements.

6.4.10 The Authorised Limit for external borrowing is a key prudential indicator and represents a control on the maximum level of borrowing. It is a limit beyond which external borrowing is prohibited, and this limit needs to be set or revised by the full Council on a rolling basis, for the forthcoming financial year and two successive financial years. This information is shown in table 3.

Table 3: Authorised Borrowing Limit

Authorised Limit	**2019/20 Estimate £'000**	**2020/21 Estimate £'000**	**2021/22 Estimate £'000**	**2022/23 Estimate £'000**
Debt	10,000	10,000	10,000	10,000
Other long term liabilities	1,000	1,500	1,500	1,500
Total	**11,000**	**11,500**	**11,500**	**11,500**

6.4.11 The Operational Boundary is the limit beyond which external borrowing is not normally expected to exceed and within which officers will manage the Council's external debt position. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual borrowing. This information is shown in table 4.

Table 4: Operational Borrowing Limit

Operational Boundary	**2019/20 Estimate £'000**	**2020/21 Estimate £'000**	**2021/22 Estimate £'000**	**2022/23 Estimate £'000**
Debt	5,000	5,000	5,000	5,000
Other long term liabilities	500	1,000	1,000	1,000
Total	**5,500**	**6,000**	**6,000**	**6,000**

6.4.12 In respect of its external debt, table 3 details the proposed authorised limits for the Council's total external debt gross of investments for the next three financial years which councillors are recommended to approve. These limits separately identify borrowing from other long-term liabilities such as finance leases. It is also recommended that members continue to delegate authority to the Chief Finance

Officer, 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 Overview & Scrutiny Committee at its next meeting following the change.

6.4.13 The Chief Finance Officer reports that these authorised limits are consistent with the authority's current commitments, existing plans and the proposals in the budget for capital expenditure and financing, and with its approved treasury management policy statement and practices. The Chief Finance Officer confirms that they are based on the estimate of the most likely, prudent but not worst-case scenario, with sufficient headroom over and above this to allow for operational management, for example unusual cash movements. Risk analysis and risk management strategies have been taken into account; as have plans for capital expenditure, estimates of the capital financing requirement and estimates of cash flow requirements for all purposes.

Prospects for Interest Rates

6.4.13 The Council has appointed Link Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Annex 1 draws together a number of current city forecasts for short term (bank rate) and longer fixed interest rates. Table 5 gives the Link central view.

Table 5: Link View interest rate forecast – January 2019

Link Asset Services Interest Rate View	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25	1.25	1.25	1.25
3 Month LIBID	0.70	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.30	1.30
6 Month LIBID	0.80	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40	1.50	1.50	1.50	1.50
12 Month LIBID	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60	1.70	1.70	1.70	1.70
5yr PWLB Rate	2.30	2.40	2.40	2.50	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.10	3.20	3.20
10yr PWLB Rate	2.60	2.70	2.70	2.70	2.80	2.90	3.00	3.10	3.20	3.20	3.30	3.30	3.40	3.50
25yr PWLB Rate	3.20	3.30	3.40	3.40	3.50	3.60	3.70	3.70	3.80	3.90	4.00	4.00	4.10	4.10
50yr PWLB Rate	3.10	3.20	3.30	3.30	3.40	3.50	3.60	3.60	3.70	3.80	3.90	3.90	4.00	4.00

Borrowing Requirement

6.4.14 The Council is currently forecasting a marginally under-borrowed position in 2019/20. This means that the Council's capital borrowing is lower than the underlying need to borrow. As a result of the capital expenditure plans set out in 6.2.2, Table 1 the Council is expected to be maintain an under-borrowed position from 2020/21 onwards as shown in Table 6 below. This is a prudent strategy as investment returns are low and counterparty risk is relatively high – this approach will be carefully monitored during 2020/21.

Table 5: Borrowing Position

Under / (Over) Borrowing	**2019/20 £000**	**2020/21 £000**	**2021/22 £000**	**2022/23 £000**
External Debt				
GF Ext Borrowing	1,513	1,474	1,434	1,395
Capital Financing Requirement	1,589	1,553	1,518	1,483
Under / (Over) Borrowing	**75**	**80**	**84**	**88**

* The table above excludes leases from the under / over borrowed position, unlike table 2 – Forecasted Portfolio Position.

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

6.4.16 The current capital programme funding forecasts for 2020/21 to 2022/23 shows there is currently no borrowing requirement. However, borrowing needs will be reviewed as the capital programmes are confirmed. Any decisions will be reported to Overview & Scrutiny committee at the next available opportunity.

Treasury Management Limits on Activity

6.4.17 There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs / improve performance. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates;
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates;
- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

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

%	**2019/20 £'000**	**2020/21 £'000**	**2021/22 £'000**
Interest Rates Exposure	**Upper**	**Upper**	**Upper**
Borrowing:			
Limits on fixed interest rates	100%	100%	100%
Limits on variable interest rates	5%	5%	5%
Investments:			
Limits on fixed interest rates	100%	100%	100%
Limits on variable interest rates	50%	50%	50%
Maturity Structure New Borrowing 2019/20		**Lower**	**Upper**
Under 12 months		0%	20%
12 Months and within 2 Years		0%	20%
2 Years and within 5 Years		0%	50%
5 Years and within 10 Years		0%	50%
10 Years and within 15 Years		0%	50%
15 Years and over		90%	20%

Policy on Borrowing in Advance of Need

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

6.5 ANNUAL INVESTMENT STRATEGY STATEMENT 2020/21

Investment Policy – management of risk

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

6.5.2 **NYCC Pooling Arrangements**

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

- MHCLG's Guidance on Local Government Investments ("the Guidance");
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the Code"); and
- CIPFA Treasury Management Guidance Notes 2018.

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

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

a) 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;

b) 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;

c) other information sources used will include the financial press, share price and other such information pertaining to the financial sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties;

d) the Council has defined the list of types of investment instruments that the treasury management team are authorised to use:-

- **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.

- **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use. Once an investment is classed as non-specified, it remains non-specified all the way through to maturity i.e. an 18 month deposit would still be non-specified even if it has only 11 months left until maturity.

e) **Non-specified investments limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being 20% of the total investment portfolio, (£4m);

f) **Lending limits**, (amounts and maturity), for each counterparty will be set;

g) the Council will set a limit for the amount of its investments which are invested for **longer than 365 days**;

h) investments will only be placed with counterparties from countries with a specified minimum **sovereign rating**;

i) the Council has engaged **external consultants**, to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of the Council in the context of the expected level of cash balances and need for liquidity throughout the year;

j) all investments will be denominated in **sterling**; and

k) as a result of the change in accounting standards for 2019/20 under IFRS 9, the Council will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the Ministry of Housing, Communities and Local Government, [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 commencing from 1.4.18.)

6.5.4 However, the Council 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.

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

Credit Worthiness Policy – Security of Capital and use of credit ratings

6.5.6 This Council applies the creditworthiness service provided by Link Asset Services (Sector). This service employs a sophisticated modelling approach utilising credit ratings from all three main credit rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings of counterparties are supplemented with the following overlays:

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

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

Colour	**Maximum Investment Duration**
Yellow	5 Years
Purple	2 Years
Orange	1 Year
Blue	1 Year (UK nationalised / semi nationalised banks only)
Red	6 Months
Green	100 Days
No Colour	No investments to be made

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

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

6.5.9 All credit ratings will be monitored daily. The Council is alerted to changes to ratings of all three agencies through its use of the Link Asset Services creditworthiness service.

- If a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be with drawn immediately;
- In addition to the use of credit ratings the Council will be advised of information in 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 lending list.

6.5.10 Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information, information on government support for banks and the credit ratings of that government support.

UK Banks – Ring-fencing

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

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

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

Country Limits

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

a) **Non-specified investment limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being 20% of the total investment portfolio.

b) **Country limit.** The Council has determined that it will only use approved counterparties from the UK and from countries with a minimum sovereign credit rating of AA- from Fitch. The list of countries that qualify using these credit criteria as at the date of this report are shown in Annex C. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

Investment Strategy

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

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

Investment returns expectations.

6.5.16 On the assumption that the UK and EU agree a Brexit deal including the terms of trade by the end of 2020 or soon after, then Bank Rate is forecast to increase only slowly over the next few years to reach 1.00% by March 2023. Bank Rate forecasts for financial year ends are:

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

6.5.17 For its cash flow generated balances, the Council will seek to utilise its notice accounts, money market funds and short dated deposits (overnight to three months) in order to benefit from the compounding of interest.

Ethical Investment Opportunities

6.5.18 Investment guidance, both statutory and from CIPFA, makes clear that all investing must adopt SLY principals – security, liquidity and yield: ethical issues must play a subordinate role to those principals. Link Asset Services is looking at ways in which Environmental, Social and Governance (ESG) metrics may be incorporated into credit rating agency assessments, and a small but growing number of financial institutions and fund managers are starting to promote ESG products. However, with a lack of consistency and coverage, Link Asset services continue to review options in this area and will update clients as progress is made, which will be brought forward in future Treasury reporting updates when available.

6.5.19 Within the Council's current lending criteria, an ethical money market fund is available to the Council for investment, (details are attached at Annex H) and will continue to be considered, should favourable return rates become available.

End of Year Investment Report

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

Scheme of Delegation

6.5.21 Please see Annex E.

Role of the section 151 officer

6.5.22 Please see Annex F.

6.6 CAPITAL STRATEGY

The Prudential Code 2017 introduced a new requirement for local authorities to produce and annual capital strategy. Please refer to Annex G.

7.0 IMPLICATIONS

7.1 The following implications have been identified:

a) Financial
The results of the investment strategy affect the funding of the Capital Programme.

b) Legal
There are no legal implications regarding this report.

c) Other (Equalities, Staffing, Planning, Health & Safety, Environmental, Crime &

Disorder)
There are no legal implications regarding this report.

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Background Papers:
None

Background Papers are available for inspection at: None