

REPORT FOR DECISION

DECISION OF:	OVERVIEW & SCRUTINY COMMITTEE CABINET COUNCIL
DATE:	13 FEBRUARY 2019 20 FEBRUARY 2019 20 FEBRUARY 2019
SUBJECT:	TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL INDICATORS 2019/20
REPORT FROM:	CABINET MEMBER FOR FINANCE & HOUSING
CONTACT OFFICER:	STEPHEN KENYON, INTERIM EXECUTIVE DIRECTOR OF RESOURCES AND REGULATION
TYPE OF DECISION:	COUNCIL
FREEDOM OF INFORMATION/STATUS:	The report is for publication
SUMMARY:	<p>The report sets out the suggested Strategy for 2019/2020 in respect of the following aspects of the Treasury Management function. It is based upon the Treasury officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury advisor. The Strategy covers:</p> <ul style="list-style-type: none"> • Capital plans and prudential indicators; • the minimum revenue provision policy; • the current treasury position; • treasury limits in force which will limit the treasury risk and activities of the Council; • prospects for interest rates; • the borrowing strategy; • policy on borrowing in advance of need • debt rescheduling; • the investment strategy; • creditworthiness policy; and • policy on use of external service providers

	<p>The primary objective of the Council's treasury management function will continue to be the minimisation of financing costs whilst ensuring the stability of the Authority's long term financial position by borrowing at the lowest rates of interest and by investing surplus cash to earn maximum interest, all at an acceptable level of risk.</p> <p>The overall strategy for 2019/20 will be to finance capital expenditure by running down cash/investment balances and using short term temporary borrowing rather than more expensive longer term loans. The taking out of longer term loans (1 to 10 years) to finance capital spending will only then be considered if required by the Council's underlying cash flow needs. Some long term loans (over 10 years) may be undertaken to replace debt which matures in the year. With the reduction of cash balances the level of short term investments will fall. Given that investment returns are likely to remain low (say) 0.75% for the financial year 2019/20, then savings will be made from running down investments rather than taking out more expensive long term loans.</p> <p>All prospects for rescheduling debt will be considered, in order to generate savings by switching from high costing long term debt to lower costing shorter term debt.</p>
<p>OPTIONS & RECOMMENDED OPTION</p>	<p>It is recommended that Overview and Scrutiny Committee notes the report;</p> <p>It is recommended that Cabinet approves, for onward submission to Council, the:</p> <ul style="list-style-type: none"> • Prudential Indicators forecast for 3 years • Treasury Management Strategy for 2019/20 • Schemes of Delegation and Responsibility attached at Appendices 2 and 6 <p>It is recommended that Council approves the report.</p> <p>Reasons for the Decision:</p> <p>It is a requirement of the CIPFA Code that the Council receives an annual treasury management strategy report.</p>
<p>IMPLICATIONS:</p>	
<p>Corporate Aims/Policy Framework:</p>	<p>Do the proposals accord with the Policy Framework? Yes</p>

Statement by the S151 Officer: Financial Implications and Risk Considerations:	Treasury Management is an integral part of the Council's financial framework and it is essential that the correct strategy is adopted in order to ensure that best value is obtained from the Council's resources and that assets are safeguarded.
Statement by Executive Director of Resources & Regulation:	There are no additional resource implications.
Health & Safety implications:	There are no direct Health & Safety implications
Equality/Diversity implications:	No
Considered by Monitoring Officer:	Yes
Wards Affected:	All
Scrutiny Interest:	Overview & Scrutiny Committee

TRACKING/PROCESS

EXECUTIVE DIRECTOR: STEVE KENYON

Chief Executive/ Senior Leadership Team	Cabinet Member/Chair	Ward Members	Partners
	Leader / Finance		
Scrutiny Committee		Committee	Council
Overview & Scrutiny 13/2/19		Cabinet 20/2/19	Council 20/2/19

1.0 BACKGROUND

- 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.
- 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, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.
- 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.
- 1.4 Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day to day treasury management activities.
- 1.5 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."
- 1.6 Revised reporting is required for 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. The capital strategy is being reported separately.

1.7 Reporting requirements

1.7.1 Capital Strategy

- 1.7.1.1 The CIPFA revised Prudential and Treasury Management Code require, for 2019/20, all local authorities to prepare an additional report, 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

- 1.7.1.2 The aim of this capital strategy is to ensure that all elected members on the full council understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.
- 1.7.1.3 This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset. The capital strategy will show:
- The corporate governance arrangements for these types of activities;
 - Any service objectives relating to the investments;
 - The expected income, costs and resulting contribution;
 - The debt related to the activity and the associated interest costs;
 - The payback period (MRP policy);
 - For non-loan type investments, the cost against the current market value;
 - The risks associated with each activity
- 1.7.1.4 Where a physical asset is being bought, details of market research, advisers used (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.
- 1.7.1.5 Where the Council has borrowed to fund any non-treasury investment, there should also be an explanation of why borrowing was required and why the MHCLG Investment Guidance and CIPFA Prudential Code have not been adhered to.
- 1.7.1.6 If any non-treasury investment sustains a loss during the final accounts and audit process, the strategy and revenue implications will be reported through the same procedure as the Capital Strategy.
- 1.7.1.7 To demonstrate the proportionality between the treasury operations and the non-treasury operation, high-level comparators are shown throughout this report.

1.7.2 Treasury Management reporting

- 1.7.2.1 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.

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 (MRP) policy (how residual capital expenditure is charged to revenue over time);
- the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

A mid year treasury management report – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether the treasury strategy is meeting the strategy or whether any policies require revision.

An annual treasury report – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

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

1.8 In Year Monitoring Arrangements

1.8.1 Budget monitoring reports are produced on a monthly basis, together with quarterly reporting to Cabinet and the Overview and Scrutiny Committee.

1.8.2 In 2018/19 the average rate of return on investments is 0.71% as at 31st December 2018.

1.9 Treasury Management Strategy for 2019/20

1.9.1 The strategy for 2019/20 covers two main areas:

Capital issues

- the capital expenditure plans and the associated prudential indicators;
- the minimum revenue provision (MRP) policy.

Treasury management issues

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

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

1.10 Training

1.10.1 The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. Training has been undertaken by members in 2017/18 and further training will be arranged as required. The training needs of treasury management officers are periodically reviewed.

1.11 Treasury Management consultants

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

1.11.2 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 our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisors.

- 1.11.3 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.
- 1.11.4 The scope of investments within the Council's operations now includes both conventional treasury investments, (the placing of residual cash from the Council's functions), and more commercial type investments, such as investment properties. The commercial type investments require specialist advisers, and the Council uses Bilfinger GVA in relation to this activity.

2.0 THE CAPITAL PRUDENTIAL INDICATORS 2019/20 – 2021/22

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

2.2 Capital expenditure

- 2.2.1 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.

Capital Expenditure	2017/18 Actual £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Non-HRA	20,100	27,857	37,254	5,311	1,200
HRA	7,371	12,015	9,830	9,830	10,000
Commercial activities / non-financial investments *	0	0	0	0	0
Total	27,471	39,871	47,084	15,141	11,200

*Commercial activities / non-financial investments relate to areas such as capital expenditure on investment properties, loans to third parties etc.

- 2.2.2 Other long-term liabilities – The above financing need excludes other long-term liabilities, such a PFI and leasing arrangements that already include borrowing instruments.
- 2.2.3 The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Financing of Capital Expenditure	2017/18 Actual £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Capital receipts	3,035	3,170	783	0	0
Capital grants	11,415	9,738	23,787	1,423	0
Capital reserves	6,945	13,837	11,190	11,018	10,000
Revenue	943	550	0	0	0
Total	22,338	27,296	35,761	12,441	10,000
Net financing need	5,133	12,575	11,323	2,700	1,200

2.3 The Council's borrowing need (the Capital Financing Requirement)

- 2.3.1 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 through a revenue or capital resource, will increase the CFR.
- 2.3.2 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, and so charges the economic consumption of capital assets as they are used.
- 2.3.3 The CFR includes any other long term liabilities (e.g. finance leases). Whilst these increase 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.

Capital Financing Requirement	2017/18 Actual £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
CFR – non HRA	119,980	128,753	136,099	134,675	141,779
CFR – HRA	118,784	118,784	118,784	118,784	108,784
CFR - Commercial activities / non-financial investments	8,313	8,313	8,313	8,313	8,313
Total CFR	247,077	255,850	263,196	261,772	258,876
Movement in CFR	1,357	8,773	7,346	-1,424	-2,896

- 2.3.4 A key aspect of the regulatory and professional guidance is that elected members are aware of the size and scope of any commercial activity in relation to the authority's overall financial position. The capital expenditure figures shown in 2.2 and the details above demonstrate the scope of this activity and, by approving these figures, consider the scale proportionate to the Authority's remaining activity.

2.4 Minimum revenue provision (MRP) policy statement

- 2.4.1 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).
- 2.4.2 MHCLG regulations have been issued which require the full Council to approve **an MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement for the year 2019/20:-
- MRP for supported borrowing will be calculated using 2% over 50 years in equal annual instalments as a variation on the 'Regulatory Method' of calculating MRP.
 - The Asset Life method of calculating repayment provision will be used for unsupported borrowing.

- The Interim Executive Director of Resources and Regulation may from time to time and when it is beneficial to the efficient financial administration of the Council, vary the amounts charged as MRP in the year by making additional and voluntary payments of MRP. In these circumstances, the amount paid would not prejudice the existing strategy or be counter to the regulatory intent of that strategy.

2.4.3 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, 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. Up until the 31st March 2019 the total VRP overpayments were £3.780m.

2.4.4 The Council has recently commissioned a MRP review from Link Consultancy. Any recommendations raised by this review will be reported once they have been assessed,

3.0 BORROWING

3.1 The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this 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.

3.2 Current portfolio position

3.2.1 To assist Members in agreeing a strategy for 2019/20 the Council's current treasury portfolio position (at nominal value) is detailed below:

		31st March 2018			Forecast 31st March 2019		
		Principal		Avg. Rate	Principal		Avg. Rate
		£0	£0		£0	£0	
Fixed rate funding							
	PWLB Bury	131,453			138,853		
	PWLB Airport	554			11,828		
	Market Bury	60,500	192,507		44,000	194,681	
Variable rate funding							
-	PWLB Bury	0			0		
	Market Bury	0	0		0	0	
Temporary Loans / Bonds		2,003	2,003		7,503	7,503	
Total Debt		194,510		3.96%	202,184		3.96%
Total Cash Investments		21,250		0.24%	7,589		0.71%
Total Investment Properties		8,313		5.10%	8,313		8.29%

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

£m	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
External Debt					
Debt at 1 April	195,682	194,510	202,184	213,507	216,207
Expected change in Debt	-1,172	7,674	11,323	2,700	1,200
Actual gross debt at 31 March	194,510	202,184	213,507	216,207	217,407
The Capital Financing Requirement	247,078	255,851	263,196	261,772	258,876
Under / (over) borrowing	-52,568	-53,667	-49,690	-45,565	-41,470

- 3.2.2 The forecast accumulated capital financing requirement at the end of 2018/19 is £255.8m. The forecast borrowing at the end of 2018/19 is £202.2m meaning that the Authority is under borrowed by £53.6 m.
- 3.2.3 The cash investment portfolio after the Capital Programme has been spent during 2018/19 is estimated to be around £5.0m. In preference to taking out long term borrowing, the Authority is taking temporary loans and running down investments to finance capital expenditure because investment returns are low at the present time. The estimated rate of interest on investments for 2018/19 is 0.71% against the 3 month LIBID investment benchmark of 0.75%.
- 3.2.4 The Council is also investing in properties that deliver a sustainable rental yield; under its "Property Investment Strategy"

3.3 Treasury Indicators: limits to borrowing activity

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

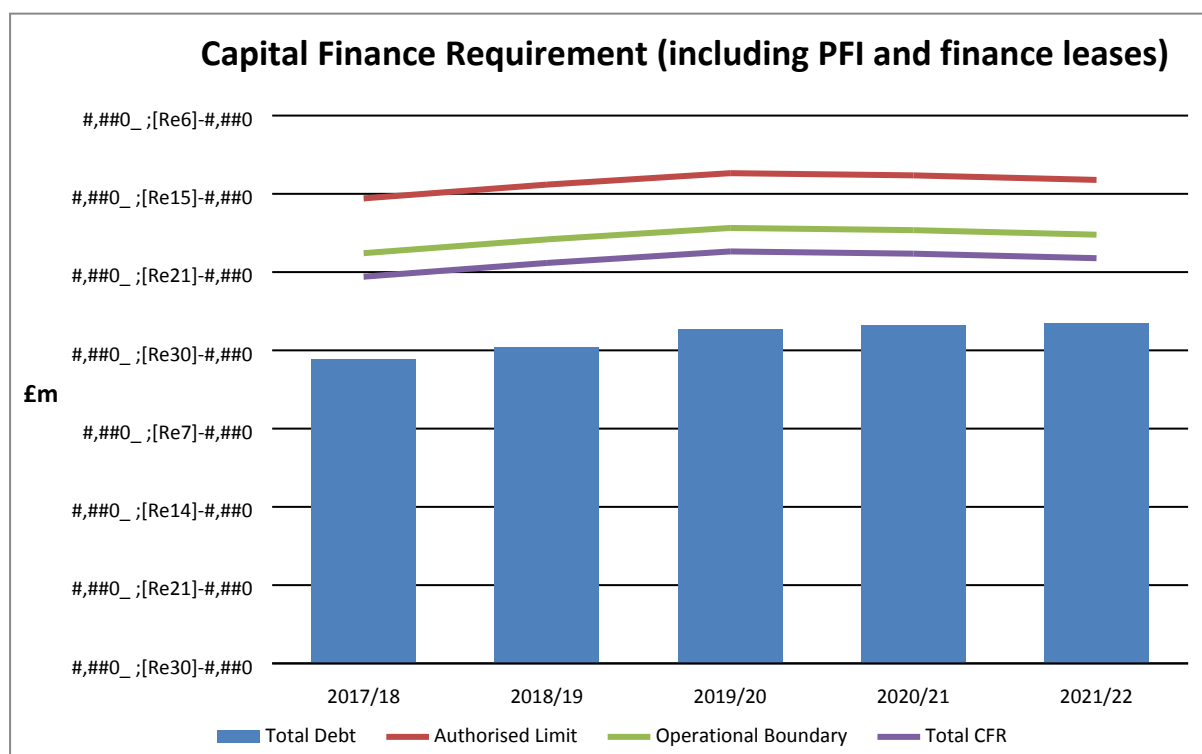
Operational boundary	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Borrowing	255,900	263,200	261,800	258,900
Other long term liabilities	5,000	5,000	5,000	5,000
Commercial activities / non - financial investments	10,000	10,000	10,000	10,000
Total	270,900	278,200	276,800	273,900

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

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

Authorised limit	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Borrowing	290,900	298,200	296,800	293,900
Other long term liabilities	5,000	5,000	5,000	5,000
Commercial activities / non - financial investments	10,000	10,000	10,000	10,000
Total	305,900	313,200	311,800	308,900

Separately, the Council is also limited to a maximum HRA CFR through the HRA self-financing regime. The HRA Debt cap was abolished from October 2018.



3.4 Prospects for interest rates

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

Link Asset Services Interest Rate View													
	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%	1.50%	1.75%	1.75%	1.75%	2.00%
3 Month LIBID	0.90%	1.00%	1.10%	1.20%	1.30%	1.40%	1.50%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%
6 Month LIBID	1.00%	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%
12 Month LIBID	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%	2.30%	2.40%
5yr PWLB Rate	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%	2.60%	2.60%	2.70%	2.80%	2.80%
10yr PWLB Rate	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%
25yr PWLB Rate	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%	3.50%	3.50%	3.60%	3.60%
50yr PWLB Rate	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.40%

- 3.4.2 Given the flow of generally positive economic statistics after the quarter ended 30th June the Monetary Policy Committee, (MPC), increased the Bank Rate on 2nd August from 0.50% to 0.75%, the first increase in Bank Rate above 0.5% since the financial crash. Growth is, however, expected to weaken during the last quarter of 2018. It is unlikely that the MPC would increase the Bank Rate in February 2019, ahead of the deadline in March for Brexit. The next increase in Bank Rate is therefore forecast to be in May 2019, followed by increases in February and November 2020, before ending up at 2% in February 2022.
- 3.4.3 The overall longer run trend is for gilt yields and PWLB rates to rise, albeit gently. The action of central banks since the financial crash of 2008, in implementing substantial Quantitative Easing, added further impetus to this downward trend in bond yields and rising bond prices. Quantitative Easing has also directly led to a rise in equity values as investors searched for higher returns and took on riskier assets.
- 3.4.4 Rising bond yields in the US have caused some upward pressure on bond yields in the UK and other developed economies. However, the degree of that upward pressure has been dampened by how strong or weak the prospects for economic growth and rising inflation are in each country, and on the degree of progress towards the reversal of monetary policy away from quantitative easing and other credit stimulus measures.
- 3.4.5 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 and emerging market developments. Such volatility could occur at any time during the forecast period.
- 3.4.6 Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The above forecasts (and MPC decisions) will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

3.5 Investment and borrowing rates

- 3.5.1 Investment returns are likely to remain low during 2019/20 but to be on a gently rising trend over the next few years.
- 3.5.2 Borrowing interest rates have been volatile so far in 2018/19 and have increased modestly since the summer. The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in the future when authorities may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.
- 3.5.3 There will remain a cost of carry (the difference between higher borrowing costs and lower investment returns), to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.

3.6 Borrowing strategy

- 3.6.1 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.
- 3.6.2 Against this background and the risks within the economic forecast, caution will be adopted with the 2019/20 treasury operations. The Interim Executive Director of Resources & Regulation will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:
- *if it was felt that there was a significant risk of a sharp FALL in long and short term rates* (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
 - *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast*, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.
- 3.6.3 Any decisions will be reported to the appropriate decision making body at the next available opportunity.

3.7 Policy on borrowing in advance of need

- 3.7.1 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.
- 3.7.2 In determining whether borrowing will be undertaken in advance of need the Council will:
- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need
 - ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets, have been considered
 - evaluate the economic and market factors that might influence the manner and timing of any decision to borrow
 - consider the merits and demerits of alternative forms of funding
 - consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use
 - consider the impact of borrowing in advance on temporarily (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk, and other risks, and the level of such risks given the controls in place to minimise them.

3.8 Debt rescheduling

3.8.1 As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

3.8.2 The reasons for any rescheduling to take place will include:

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

3.8.3 Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

3.8.4 All rescheduling will be reported to the Council, at the earliest meeting following its action.

4.0 ANNUAL INVESTMENT STRATEGY

4.1 Investment policy – management of risk

4.1.1 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, (a separate report).

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

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

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

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

- 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.
- **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..

- **Other information sources** used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.
- This authority has defined the list of **types of investment instruments** that the treasury management team are authorised to use. There are two lists in appendix 5.4 under the categories of “specified” and “non-specified” investments.
 - **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.
- This authority will set a limit for the amount of its investments which are invested for **longer than 365 days** (see paragraph 4.4.5)
- Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating** (see Appendix 3)
- This authority has engaged **external consultants** (see paragraph 1.11), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.
- All investments will be denominated in **sterling**.
- As a result of the change in accounting standards for 2018/19 under IFRS 9, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the 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.)

4.1.3 However, this authority will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investments performance (see paragraph 4.4). Regular monitoring of investment performance will be carried out during the year.

4.1.6 The above criteria are unchanged from 2018/19.

4.2 Creditworthiness policy

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

- 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.

4.2.2 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 coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands:

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

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

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

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

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

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

- 4.2.5 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 any external support for banks to help support its decision making process.

	Colour (and long term rating where applicable)	Time Limit
Banks *	yellow	5yrs
Banks	purple	2 yrs
Banks	orange	1 yr
Banks – part nationalised	blue	1 yr
Banks	red	6 mths
Banks	green	100 days
Banks	No colour	Do not use
DMADF	UK sovereign rating	6 months
Local authorities	n/a	5yrs
Housing associations	Colour bands	As per colour band
	Fund rating	Time Limit
Money Market Funds CNAV	AAA	liquid
Money Market Funds LVNAV	AAA	liquid
Money Market Funds VNAV	AAA	liquid
Ultra-Short Dated Bond Funds with a credit score of 1.25	Dark pink / AAA	liquid
Ultra-Short Dated Bond Funds with a credit score of 1.50	Light pink / AAA	liquid

4.3 Country limits

- 4.3.1 The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide). The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 3, although the Council's current approach is to use UK High Street Banks and other public bodies. The list of counterparties will be added to, or deducted from, by officers should ratings change in accordance with this policy.

4.4 Investment Strategy

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

- If it is 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.

4.4.2 **Investment returns expectations.** Bank Rate is forecast to increase steadily but slowly over the next few years to reach 2.00% by quarter 1 2022. Bank Rate forecasts for financial year ends (March) are:

- 2018/19 0.75%
- 2019/20 1.25%
- 2020/21 1.50%
- 2021/22 2.00%

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

	Now
2018/19	0.75%
2019/20	1.00%
2020/21	1.50%
2021/22	1.75%
2022/23	1.75%
2023/24	2.00%
Later years	2.50%

4.4.3 The overall balance of risks to economic growth in the UK is probably neutral.

4.4.4 The balance of risks to increases in Bank Rate and shorter term PWLB rates, are probably also even and are dependent on how strong GDP growth turns out, how quickly inflation pressures rise and how quickly the Brexit negotiations move forward positively.

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

Maximum principal sums invested > 364 & 365 days			
£m	2018/19	2019/20	2020/21
Principal sums invested > 364 & 365 days	£10m	£10m	£10m

(This takes account of the proposed change in the CIPFA Treasury Code from a 364 day limit to 365 days.)

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

4.5 End of year investment report

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

5.0 EQUALITY & DIVERSITY

- 5.1 An initial assessment has been undertaken and it is concluded that there will be no negative impact from this report.

Councillor Eamonn O'Brien
Cabinet Member for Finance and Housing

For further information on the contents of this report, please contact:

Steve Kenyon, Interim Executive Director of Resources & Regulation,
Tel: 0161 253 5002
e-mail:s.kenyon@bury.gov.uk

APPENDIX 1: Interest Rate Forecasts 2018 – 2021

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

Link Asset Services Interest Rate View													
	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%	1.50%	1.75%	1.75%	1.75%	2.00%
3 Month LIBID	0.90%	1.00%	1.10%	1.20%	1.30%	1.40%	1.50%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%
6 Month LIBID	1.00%	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%
12 Month LIBID	1.20%	1.30%	1.40%	1.50%	1.60%	1.70%	1.80%	1.90%	2.00%	2.10%	2.20%	2.30%	2.40%
5yr PWLB Rate	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%	2.60%	2.60%	2.70%	2.80%	2.80%
10yr PWLB Rate	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%
25yr PWLB Rate	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%	3.50%	3.50%	3.60%	3.60%
50yr PWLB Rate	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.40%
Bank Rate													
Link Asset Services	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%	1.50%	1.75%	1.75%	1.75%	2.00%
Capital Economics	0.75%	1.00%	1.25%	1.50%	1.70%	1.75%	2.00%	2.00%	-	-	-	-	-
5yr PWLB Rate													
Link Asset Services	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%	2.60%	2.60%	2.70%	2.80%	2.80%
Capital Economics	2.03%	2.15%	2.40%	2.65%	2.70%	2.75%	2.80%	2.85%	-	-	-	-	-
10yr PWLB Rate													
Link Asset Services	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%
Capital Economics	2.43%	2.55%	2.80%	3.05%	3.05%	3.05%	3.05%	3.05%	-	-	-	-	-
25yr PWLB Rate													
Link Asset Services	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%	3.50%	3.50%	3.60%	3.60%
Capital Economics	2.96%	3.08%	3.33%	3.58%	3.53%	3.48%	3.43%	3.38%	-	-	-	-	-
50yr PWLB Rate													
Link Asset Services	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.40%
Capital Economics	2.78%	2.90%	3.15%	3.40%	3.40%	3.40%	3.40%	3.40%	-	-	-	-	-

APPENDIX 2: Treasury Management Practice (TMP1) – Credit and Counterparty Risk Management

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

NON-SPECIFIED INVESTMENTS: These are any investments which do not meet the specified investment criteria. A maximum of 100% will be held in aggregate in non-specified investment

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

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

	Minimum credit criteria / colour band	** Max % of total investments/ £ limit per institution	Max. maturity period
DMADF – UK Government	N/A	100%	6 months
UK Government gilts	UK sovereign rating		12 months
UK Government Treasury bills	UK sovereign rating		12 months
Bonds issued by multilateral development banks	AAA		6 months
Money Market Funds CNAV	AAA	100%	Liquid
Money Market Funds LVAV	AAA		Liquid
Money Market Funds VNAV	AAA		Liquid
Ultra-Short Dated Bond Funds with a credit score of 1.25	AAA	100%	Liquid
Ultra-Short Dated Bond Funds with a credit score of 1.5	AAA	100%	Liquid
Local authorities	N/A	100%	12 months
Term deposits with housing associations	Blue Orange Red Green No Colour		12 months 12 months 6 months 100 days Not for use
Term deposits with banks and building societies	Blue Orange Red Green No Colour		12 months 12 months 6 months 100 days Not for use
CDs or corporate bonds with banks and building societies	Blue Orange Red Green No Colour		12 months 12 months 6 months 100 days Not for use
Gilt funds	UK sovereign rating		

APPENDIX 3: Approved countries for investments

This list is based on those countries which have sovereign ratings of AA- or higher and also, (except - at the time of writing - for Hong Kong, Norway and Luxembourg), have banks operating in sterling markets which have credit ratings of green or above in the Capita Asset Services credit worthiness service.

AAA

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

AA+

- Finland
- U.S.A.

AA

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

AA-

- Belgium
- Qatar

(note the Council only invests in the highest rated UK institutions)

APPENDIX 4: DELEGATION AND RESPONSIBILITY

The following personnel are involved on a regular basis in Treasury Management: -

Interim Executive Director of Resources & Regulation (Steve Kenyon)	Overall supervision of Treasury Management function and cashflow. Regular reviews of Treasury Management Strategy and monitor performance.
Head of Financial Management (Andrew Baldwin)	Deputise for the Interim Executive Director of Resources & Regulation
Head of Management Accountancy (Jane Bunn)	Manage and undertake day to day Treasury Management Activities in accordance with Treasury Strategy and Policy Statement.
Senior Accountant (Joanne McIntyre)	Deputise for Principal Accountant in her duties as required.
Senior Accountant (Angela Sozansky)	Deputise for Principal Accountant in her duties as required.
Senior Accountancy Assistant (Stephen Blake)	Deputise for Principal Accountant in her duties as required.
Accountancy Assistant (Linda Hughes)	Standby for allocation of short term business via brokers.

Please note that the Council's signatories for treasury management transactions are :-

Steve Kenyon	Interim Executive Director of Resources & Regulation
Andrew Baldwin	Head of Financial Management
Kath Pope	Principal Finance Manager
Jane Bunn	Head of Management Accountancy

APPENDIX 5: Treasury management scheme of delegation

(i) Full council

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.

(ii) Boards/committees/Council/responsible body

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
- budget consideration and approval;
- approval of the division of responsibilities;
- receiving and reviewing regular monitoring reports and acting on recommendations;
- approving the selection of external service providers and agreeing terms of appointment.

(iii) Body/person(s) with responsibility for scrutiny

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

APPENDIX 6: The treasury management role of the section 151 officer

The S151 (responsible) officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers.

The above list of specific responsibilities of the S151 officer in the 2017 Treasury Management Code has not changed. However, implicit in the changes in both codes, is a major extension of the functions of this role, especially in respect of non-financial investments, (which CIPFA has defined as being part of treasury management). (Officers are recommended to decide whether to extend this section to include the following examples): -

- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long term timeframe (say 20+ years – to be determined in accordance with local priorities. Please also note that CIPFA has provided advice that it recognises that it may be too late in the current budget round for 2018/19 for many local authorities to produce a capital strategy this year.)
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money
- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority
- ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees (*We are unclear as to whether CIPFA requires this to be implemented in 2018/19. We are concerned that many local authorities could have difficulty in complying fully with this requirement at this late stage in the 2018/19 budget cycle.*)
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following (*TM Code p54*): -
 - *Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios;*

- *Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments;*
- *Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making;*
- *Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken;*
- *Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.*