Northampton Borough Council
Treasury Management Strategy 2019-20

Contents

1. Introduction

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 borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

1.6. Revised reporting is required for 2019/20 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 reported separately.

Reporting Requirements

Capital Strategy

1.7. The CIPFA revised 2017 Prudential and Treasury Management Codes 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;

1.8. 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.

1.9. 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.

1.10. Where a physical asset is being bought, details of market research, advisors 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.

1.11. 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.

1.12. 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.

1.13. To demonstrate the proportionality between the treasury operations and the non-treasury operation, high-level comparators are shown throughout this report.

Treasury Management Reporting

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

a) **Prudential and treasury indicators and treasury strategy (this report)** - The first, and most important report is forward looking and covers:

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

b) **A mid-year treasury management report –** This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision. If applicable. In addition, this Council will receive quarterly update reports.

c) **An annual treasury report –** This is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

Treasury Management Strategy

1.15. The strategy for 2019/20 covers two main areas:

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

Treasury Management;
- 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.

1.16. 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.

Training

1.17. The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management have access to training in treasury management. The Councils treasury advisory contract includes provision for annual delivery of member training. The training needs of treasury management officers are periodically reviewed.

Treasury Advisors

1.18. The Council uses Link Asset Services (LAS) as its external treasury management advisors.

1.19. 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 advisors.

1.20. 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.

Non-treasury Investment Advise

1.21. 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. Commercial type investments may require specialist advise, and therefore the Council will undertake appropriate due-dilgence on a case-by-case basis.

2. Current Treasury Management position

2.1. The Council's projected treasury portfolio position at 31 March 2019, with forward estimates, is summarised below. Table 1 shows external borrowing against the Capital Financing Requirement (CFR) - which is a measure of the need to borrow for capital expenditure purposes - highlighting any forecast over or under borrowing.

2.2. The figures exclude any borrowing undertaken or planned for third party loans so as to focus on the Council's own cash position:

Table 1: Treasury Portfolio at 31 March 2019						
£m	**2019-20 Estimate**	**2020-21 Estimate**	**2021-22 Estimate**	**2022-23 Estimate**	**2023-24 Estimate**	**2024-25 Estimate**
External borrowing						
Borrowing at 1 April	207	202	207	206	200	192
Expected change in borrowing	(5)	5	(1)	(6)	(8)	-
Borrowing at 31 March (1)	**202**	**207**	**206**	**200**	**192**	**192**
CFR (exc 3rd Party Loans) at 31 March (2)	**299**	**326**	**331**	**336**	**333**	**330**
Under/(over) borrowing (2-1)	**97**	**119**	**125**	**136**	**141**	**138**
Investments						
Investments (exc 3rd Party Loans) at 1 April	55	45	23	19	10	6
Expected change in investments	(10)	(19)	(4)	(9)	(4)	-
Investments (exc 3rd Party Loans) at 31 March (3)	**45**	**23**	**19**	**10**	**6**	**6**
Net borrowing (exc 3rd Party Loans) (1-3)	**157**	**184**	**187**	**190**	**186**	**186**

2.3. The Council's prudential and treasury indicators for 2019-20 to 2023-24 are set out at Appendix 3.

3. Interest Rates

3.1. The Council has appointed Link Asset Services (LAS) 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 our central view.

Link Asset Services Interest Rate View	Dec-18	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%	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	0.80%	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	0.90%	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	1.10%	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	2.00%	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%	2.50%	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%	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%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.40%

3.2. The flow of generally positive economic statistics after the quarter ended 30th June meant that it came as no surprise that the Bank of England's Monetary Policy Committee (MPC) came to a decision on 2nd August to make the first increase in Bank Rate above 0.5% since the financial crash, from 0.5% to 0.75%. Growth has been healthy since that meeting, but is expected to weaken somewhat during the last quarter of 2018. At their November meeting, the MPC left Bank Rate unchanged, but expressed some concern at the Chancellor's fiscal stimulus in his Budget, which could increase inflationary pressures. However, it is unlikely that the MPC would increase 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 2.0% in February 2022.

3.3. The overall longer run future trend is for gilt yields, and consequently PWLB rates, to rise, albeit gently. However, over about the last 25 years, we have been through a period of falling bond yields as inflation subsided to, and then stabilised at, much lower levels than before, and supported by central banks implementing substantial quantitative easing purchases of government and other debt after the financial crash of 2008. Quantitative easing, conversely, also caused a rise in equity values as investors searched for higher returns and purchased riskier assets. In 2016, we saw the start of a reversal of this trend with a sharp rise in bond yields after the US Presidential election in November 2016, with yields then rising further as a result of the big increase in the US government deficit aimed at stimulating even stronger economic growth. That policy change also created concerns around a significant rise in inflationary pressures in an economy which was already running at remarkably low levels of unemployment. Unsurprisingly, the Fed has continued on its series of robust responses to combat its perception of rising inflationary pressures by repeatedly increasing the Fed rate to reach 2.00 – 2.25% in September 2018. It has also continued its policy of not fully reinvesting proceeds from bonds that it holds as a result of quantitative easing, when they mature. We have, therefore, seen US 10 year bond Treasury yields rise above 3.2% during October 2018 and also seen investors causing a sharp fall in equity prices as they sold out of holding riskier assets.

3.4. Rising bond yields in the US have also 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.

3.5. 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, emerging market developments and sharp changes in investor sentiment. Such volatility could occur at any time during the forecast period.

3.6. 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.

Investment and borrowing rates

3.7. Investment returns are likely to remain low during 2019/20 but to be on a gently rising trend over the next few years.

3.8. 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 the Council well over the last few years. However, this position will be carefully monitored to avoid incurring higher borrowing costs in the future when the Council may not be able to avoid new borrowing to finance capital expenditure or the refinancing of maturing debt.

3.9. 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.

4. Borrowing Strategy

4.1. The Council is currently maintaining an under-borrowed position against borrowing capacity. 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.

4.2. Against this background and the risks within the economic forecast, caution will be adopted with the 2019/20 treasury operations. The CFO 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 likely be postponed, and potential rescheduling from fixed rate funding into short term borrowing may 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 rate of increase in bank rate, an increase in global economic activity, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding may be drawn whilst interest rates are lower than they are projected to be in the next few years.

4.3. Any decisions will be reported to Cabinet at the next available opportunity.

Policy on Borrowing In Advance of Need

4.4. 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 CFR 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.

4.5. Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanisms.

Debt Rescheduling

4.6. 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).

4.7. 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).

4.8. 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.

4.9. All rescheduling will be reported to the Cabinet at the earliest meeting following its action.

Municipal Bonds Agency

4.10. The Municipal Bond Agency was established with the purpose of offering loans to local authorities at rates lower than those offered by the Public Works Loan Board (PWLB). To date, the Agency has not issued any bonds. In the future, the Council may make use of this new source of borrowing should it prove cost effective to do so.

Temporary Borrowing

4.11. The Council may occasionally undertake short-term temporary borrowing if this is needed to cover its cash flow position.

4.12. The CFO may also authorise the taking of short-term deposits under mutually agreed and documented terms from other local not-for-profit organisations.

5. Annual Investment Strategy (AIS)

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, (a separate report).

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");
- CIPFA Treasury Management Guidance Notes 2018 .

5.3. The Council's counterparty and credit risk management policies and its approved instruments for investments are set out in Appendix 7. The Council's investment priorities will be security first, liquidity second and then yield (return) – in that order.

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

5.4.1. 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.

5.4.2. 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.

5.4.3. 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.

5.4.4. This Council has defined the list of types of investment instruments that the treasury management team are authorised to use. There are two lists in Appendix 7 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.

5.4.5. Lending limits, (amounts and maturity), for each counterparty will be set through applying the matrix table in Appendix 7.

5.4.6. Transaction limits are set for each type of investment in Appendix 7.

5.4.7. This authority will set a limit for the amount of its investments which are invested for longer than 365 days.

5.4.8. Investments will only be placed with counterparties from countries with a specified minimum sovereign rating.

5.4.9. This authority 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 this authority in the context of the expected level of cash balances and need for liquidity throughout the year.

5.4.10. All investments will be denominated in sterling.

5.5. However, this authority will also pursue value for money in treasury management and will monitor the yield from investment income against an appropriate time-weighted benchmark for investment performance. Regular monitoring of investment performance will be carried out during the year.

Significant Changes to Risk Management Approach Since Last Approved Strategy

UK Banks – Ring-Fencing

5.6. 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.

5.7. 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.

5.8. While the structure of the banks included within this process may have changed, the fundamentals of credit assessment have not. The 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.

Approach to Investments

5.9. 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

Loans to Third Parties

5.10. The Council may make grants or loans to third parties for the purpose of capital expenditure, as allowable under paragraph 25 (1) (b) of the Local Authorities (Capital Financing and Accounting) (England) Regulations 2003 (Statutory Instrument No. 3146). This will usually be to support local economic development, and may be funded by external borrowing.

5.11. The Council also has powers to provide financial support to organisations under general powers of competence under the Localism Act 2011.

5.12. Enhancement to the governance and due diligence in respect of the awarding of grants and third party loans has been developed. This covers:

- Checklists and a manual;
- The incorporation of external independent advice as part sign-off process.

5.13. Loans of this nature that remain outstanding have been lent to Northampton Town Rugby Football Club (NTRFC), Cosworth and University of Northampton (UoN).

Enterprise Zones

5.14. The Council continues to take forward infrastructure improvements to enable development and to attract investment into the Enterprise Zone, supporting employment growth. Loans have been granted from the Government's Growing Places Fund (GPF) and Local Infrastructure Fund (LIF). The repayment of funding (principal and interest) will be met, for the most part, from business rates uplift in line with the Enterprise Zone financial model.

Tax Incremental Financing

5.15. The Government previously outlined plans to give local authorities the tools to promote growth, including giving more freedom for local authorities to make use of additional revenues to drive forward economic growth in their areas. infrastructure projects.

5.16. To this aim they are looking to introduce new borrowing powers to enable authorities to carry out Tax Incremental Financing (TIF) for infrastructure projects. This required new legislation and is closely linked to the localisation of business rates i.e. local retention of business rate income.

5.17. In determining the affordability of borrowing for capital purposes, local authorities take account of their current income streams and forecast future income. TIF will enable local authorities to borrow against a future additional uplift to their business rates base. It will be important to manage the costs and risks of this borrowing alongside wider borrowing under the Prudential Code.

5.18. The Council will continue to explore these opportunities and assess their impact on the Treasury Management Strategy, particularly in terms of risk to the sustainability, prudence and affordability to the Council's finances.

Prudential & Treasury Indicators

5.19. The Council's prudential and treasury indicators for 2019-20 to 2023-24 are set out at Appendix 3.

Outturn Report

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

6. List of appendices

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Appendix 2	Policy for attributing income and expenditure and risks between the General Fund and the HRA
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Treasury Management Strategy – Appendix 1

Treasury Management Scheme of Delegation and role of the Chief Finance Officer (Section 151 Officer)

Treasury Management Scheme of Delegation

Council

The Council is responsible for:

- Adoption of the CIPFA Code of Practice on Treasury Management in the Public Services;
- Approval of the Treasury Management Policy Statement;
- Approval of the annual Treasury Management Strategy and annual Investment Strategy;
- Setting and monitoring of the Council's prudential and treasury indicators;
- Approval of the treasury management mid-year and outturn reports;
- Approval of the debt financing revenue budget as part of the annual budget setting process.

Cabinet

The Cabinet is responsible for:

- Consideration of the all of the above and recommendation to Council;
- Receiving monitoring information on the debt financing budget as part of the revenue budget monitoring process;
- Approving the selection of external service providers and agreeing terms of appointment in accordance with the Council's procurement regulations.

Audit Committee

Audit Committee is the body responsible for scrutiny and will have responsibility for the review of treasury management policy and procedures, the scrutiny of all treasury management reports to Cabinet and Council, and for making recommendations to Cabinet and Council.

Treasury management role of the Section 151 Officer

The Council's Chief Finance Officer (CFO) is the officer designated for the purposes of Section 151 of the Local Government Act 1972 as the Responsible Officer for treasury management at the Council.

Treasury Management Strategy – Appendix 1 cont.

The Council's Financial Regulations delegates responsibility for the execution and administration of treasury management decisions to the CFO, who will act in accordance with the Council's policy statement and TMPs and CIPFA's Standard of Professional Practice on Treasury Management.

The CFO has delegated powers through this policy to take the most appropriate form of borrowing from the approved sources, and to make the most appropriate form of investments in approved instruments.

Prior to entering into any capital financing, lending or investment transaction, it is the responsibility of the responsible officer to be satisfied, by reference to the Council's legal department and external advisors as appropriate, that the proposed transaction does not breach any statute, external regulation or the Council's Financial Regulations.

The CFO may delegate his power to borrow and invest to members of his staff.

The CFO is responsible for:

- Ensuring that the schedules to the Treasury Management Practices (TMPs) are fully reviewed and updated annually and monitoring compliance to the Treasury Management in the Public Services: Code of Practice and Guidance Notes;
- Submitting regular treasury management reports to Cabinet and Council;
- Submitting debt financing revenue budgets and budget variations in line with the Council's budgetary policies;
- Receiving and reviewing treasury management information reports;
- Reviewing the performance of the treasury management function and promoting value for money;
- 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 (e.g. treasury management advisors) in line with the approval limits set out in the Council's procurement rules;
- Ensuring that the Council's Treasury Management Policy is adhered to, and if not, bringing the matter to the attention of elected members as soon as possible.
- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long term timeframe.
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money.

Treasury Management Strategy – Appendix 1 cont.

- 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.
- 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.

Treasury Management Strategy – Appendix 2

Policy for attributing income and expenditure and risks between the General Fund and the HRA

1.1 The Council is required to have a clearly agreed policy for attributing income and expenditure and risks between the General Fund and the HRA.

1.2 The Council uses a two pool approach to splitting debt between the HRA and General Fund, whereby loans are assigned to either the HRA or the General Fund.

1.3 The Council applies the requirements of the CLG Item 8 Credit and Item 8 Debit (General) Determination from 1 April 2012 in recharging debt financing and debt management costs between the HRA and the General Fund. The interest rates to be applied are determined as follows:

Principal Amount	Interest Rate
HRA Credit Arrangements CFR: concession agreements and finance leases	Average rate on HRA credit arrangements
HRA Loans CFR: long term loans (external)	Average rate on HRA external debt
HRA Loans CFR: short term loans payable (under funded CFR)	Average rate on GF external debt/or for formally agreed borrowing from GF resources an agreed PWLB equivalent rate.
HRA Loans CFR: short term loans receivable (over funded CFR)	Average rate on external investments/or for earmarked medium term reserves an actual external investment rate
HRA Cash balances: short term loans payable (cash balances overdrawn)	Average rate on external investments
HRA Cash balances: short term loans receivable (cash balances in hand)	Average rate on external investments/or for earmarked medium term reserves an actual external investment rate

1.4 For the purpose of calculating interest rates:

- HRA cash balances are based on the average of opening and closing HRA cash balances;
- HRA CFR external debt is based on actual external debt;
- Other HRA CFR balances is based on the mid year position.

1.5 Debt management costs are charged to the HRA on an apportioned basis that takes into account the weighting of time spent on managing debt and investments respectively.

Treasury Management Strategy – Appendix 2 cont.

1.6 Risk associated with external loans sit with either the GF or HRA depending on which of these the loan has been earmarked to. This will include interest rate risk, for example the risk of interest rate rises associated with variable loans.

1.7 Similarly, risk associated with any external investment of earmarked medium term HRA reserves sits with the HRA. This will include the risk of impairment, in the event of the failure of a counterparty.

1.8 Where risk cannot be earmarked specifically to either the General Fund or HRA, it is apportioned fairly between the two, using relevant available data. For example, in the event of impairment of an investment counterparty, the loss will be apportioned between the two funds based on an estimated proportion of cash balances held.

Treasury Management Strategy – Appendix 3
Prudential and Treasury Indicators

The prudential indicators for 2019-20 to 2023-24 are set out below, each one with a commentary and risk analysis.

Affordability

a) Estimate of financing costs to net revenue stream

Commentary

The indicator has been calculated as the estimated net financing costs for the year divided by the amounts to be met from government grants and local taxpayers for the non-HRA element, and by total HRA income for the HRA element. However, it should be recognised however that ultimately all debts of a local authority fall on the taxpayer. The objective is to enable trends to be identified.

The figures below reflects the cumulative impact of borrowing costs (interest and MRP where applicable) for capital programme schemes agreed each year, set against the backdrop of net revenue streams in future years.

Financing costs to net revenue stream					
	2019-20	2020-21	2021-22	2022-23	2023-24
	Estimate %	Estimate %	Estimate %	Estimate %	Estimate %
General Fund	7.82	8.42	9.03	8.96	8.89
HRA	30.13	30.28	29.43	29.08	28.88

Risk Analysis

Debt financing costs relating to past and current capital programmes have been estimated in accordance with proper practices. Actual costs will be dependent on the phasing of capital expenditure and prevailing interest rates, and will be closely managed and monitored on an ongoing basis. Carry forwards in the capital programme, whether planned or unplanned, will delay the impacts of debt financing costs to future years.

Prudence

Capital Expenditure

b) Estimates of capital expenditure

Commentary

This indicator requires reasonable estimates of the total of capital expenditure to be incurred during the forthcoming financial year and at least the following two financial years.

The draft capital programme for 2019-20 to 2023-24 for both the GF and HRA is included elsewhere on this agenda and sets out the levels of estimated capital expenditure.

Estimates include continuation schemes from previous years, new bids for the coming year, and block programmes for the coming and future years. The programme is agreed annually and will be adjusted in the context of future bids submitted and available resources when the annual programmes for the future years are agreed. Variations to the existing programme may also be agreed during the year.

Risk Analysis

There is a real risk of cost variations to planned expenditure against the capital programme, arising for a variety of reasons, including tenders coming in over or under budget, changes to specifications, and slowdown or acceleration of project phasing. There is also the possibility of needing to bring urgent and unplanned capital works into the capital programme. The risks are managed by officers on an ongoing basis, by means of active financial and project monitoring. Any significant issues are reported to Cabinet as part of the finance and performance reporting cycle.

The availability of financing from capital receipts, grants and external contributions also carries significant risk. This can be particularly true of capital receipts, where market conditions are a key driver to the flow of funds, causing particular problems in a depressed or fluctuating economic environment. The financing position of the capital programme is closely monitored by officers on an ongoing basis and any significant issues are reported to Cabinet as part of the finance and performance reporting cycle.

c) Gross debt and the capital financing requirement (CFR)

Commentary

This is a key indicator of prudence. It is intended to show that debt 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 new two financial years. This demonstrates that the Council's borrowing has only been undertaken for a capital purpose.

Gross debt and the capital financing requirement		
	2019-20 £m **Excluding** Third Party Loans	2019-20 £m **Including** Third Party Loans
Gross external debt	**202**	**272**
2018-19 Closing CFR (forecast)	268	318
Increases to CFR:		
2019-20	31	31
2020-21	27	(3)
2021-22	5	5
Adjusted CFR	**331**	**351**
Gross external debt less than adjusted CFR	**Yes**	**Yes**

Risk Analysis

Where the gross debt is greater than the capital financing requirement the reasons for this should be clearly stated in the annual strategy.

Estimates of capital financing requirement (CFR)

Commentary

External borrowing arises as a consequence of all the financial transactions of the authority and not simply those arising from capital spending. The CFR can be understood as the Council's underlying need to borrow money long term for a capital purpose – that is, after allowing for capital funding from capital receipts, grants, third party contributions and revenue contributions.

Treasury Management Strategy – Appendix 3 cont.

The Council is required to make reasonable estimates of the total CFR at the end of the forthcoming financial year and the following two years thereafter. A local authority that has an HRA must identify separately estimates of the HRA and General Fund CFR.

The CFR has been calculated in line with the methodology required by the relevant statutory instrument and the guidance to the Prudential Code. It incorporates the actual and forecast borrowing impacts of the Council's previous, current and future capital programmes.

The table below shows the impact of proposed new capital expenditure funded by borrowing ofset by annual repayments of principal (MRP – General Fund only, the HRA is not required to make an annual MRP charge). The table also splits out the impacts of loans to third party organisations funded by borrowing, where these are included in the Council's capital programme.

The changes to CFR are subject to future Council decisions in respect of the capital programme for those years.

Capital Financing Requirement (Closing CFR)					
	2019-20	2020-21	2021-22	2022-23	2023-24
	31 March £m	31 March £m	31 March £m	31 March £m	31 March £m
General Fund	84	97	96	95	92
HRA	215	229	235	241	241
Total	**299**	**326**	**331**	**336**	**333**
Loans to third parties (GF)	50	20	20	19	19
Total	**349**	**346**	**351**	**355**	**352**

Risk Analysis

The capital financing requirement will vary from the estimates if there are changes to capital programme plans that result in reduced or increased borrowing to support expenditure. This will include adjustments between years as a result of carry forwards in the capital programme, which can impact on the profile of capital expenditure and the profile of the minimum revenue provision.

All borrowing plans must be affordable in revenue terms and to this end additional borrowing to fund capital expenditure will only be approved through the normal capital project approval process and where it has been demonstrated to be prudent affordable and sustainable.

External Debt

d) Authorised limit for external debt

Commentary

For the purposes of this indicator the authorised limit for external debt is defined as the authorised limit for borrowing plus the authorised limit for other long term liabilities.

This requires the setting for the forthcoming financial year and the following four financial years of an authorised limit for total external debt (including temporary borrowing for cash flow purposes), gross of investments, separately identifying borrowing from other long term liabilities.

The authorised limit represents the maximum amount the Council may borrow at any point in time in the year. It has to be set at a level the Council considers is “prudent” and be consistent with plans for capital expenditure and financing. It contains a provision for forward funding of future years capital programmes, which may be utilised if current interest rates reduce significantly but are predicted to rise in the following year.

This limit is based on the estimate of the most likely but not worst case scenario, with in addition sufficient headroom over and above this to allow for operational management, for example unusual cash movements. It includes headroom for any planned loans to third party organisations where aplicable.

The authorised limit is set at an amount that allows a contingency for any additional unanticipated or short-term borrowing requirements over and above the operational boundary during the period (see (e) below).

Other long-term liabilities relate to finance leases and credit arrangements.

The CFO will have delegated authority to effect movement between the separately agreed figures for borrowing and other long-term liabilities. Any such changes will be reported to the Council at the next meeting following the change.

Authorised limit for external debt					
	2019-20	2020-21	2021-22	2022-23	2023-24
	Limit £m	Limit £m	Limit £m	Limit £m	Limit £m
Borrowing	330	335	335	335	335
Other long-term liabilities	5	5	5	5	5
Total	**335**	**340**	**340**	**340**	**340**

Risk Analysis

Risk analysis and risk management strategies have been taken into account in setting this indicator, as have plans for capital expenditure, estimates of the capital financing requirement and estimates of the Council's cash flow requirements.

e) Operational boundary for external debt

Commentary

The proposed operational boundary is based on the same estimates as the authorised limit. However it excludes the additional headroom included within the authorised limit to allow for unusual cash movements.

The operational boundary represents a key management tool for in year monitoring by the CFO. Within the operational boundary, figures for borrowing and other long-term liabilities are separately identified.

The borrowing element of the operational boundary has been set with reference to the maximum Capital Financing Requirement (CFR) over the coming three years. It includes headroom for any planned loans to third party organisations.

Other long-term liabilities relate to finance leases and credit arrangements.

The CFO will have delegated authority to effect movement between the separately agreed figures for borrowing and other long-term liabilities. Any such changes will be reported to the Council at the next meeting following the change.

Treasury Management Strategy – Appendix 3 cont.

Operational boundary for external debt					
	2019-20	2020-21	2021-22	2022-23	2023-24
	Limit £m	Limit £m	Limit £m	Limit £m	Limit £m
Borrowing	320	325	325	325	325
Other long-term liabilities	5	5	5	5	5
Total	**325**	**330**	**330**	**330**	**330**

Risk Analysis

Risk – Risk analysis and risk management strategies have been taken into account in setting this indicator, as have plans for capital expenditure, estimates of the capital financing requirement and estimates of the Council's cash flow requirements.

Treasury Indicators

f) Maturity structure of borrowing

This indicator sets both upper and lower limits with respect to the maturity structure of the Council's borrowing.

The indicator represents the amount of projected borrowing that is maturing in each period expressed as a percentage of total projected borrowing at the start of the period where the periods in question are:

- Under 12 months;
- 12 months and within 24 months;
- 24 months and within 5 years;
- 5 years and within 10 years;
- 10 years and within 20 years;
- 20 years and within 30 years;
- 30 years and within 40 years;
- 40 years and above.

The Treasury Management Code of Practice Guidance Notes requires that the maturity is determined by the earliest date on which the lender can require payment, which in the case of LOBO loans is the next break period. However in the current low interest rate environment the likelihood of the interest rates on these loans being raised and the loans requiring repayment at the break period is extremely low.

Treasury Management Strategy – Appendix 3 cont.

The proposed limits for the forthcoming year are:

Maturity Structure of Borrowing		
	Lower Limit %	Upper Limit %
Under 12 months	0%	50%
Between 1 and 2 years	0%	50%
Between 2 and 5 years	0%	50%
Between 5 and 10 years	0%	50%
Between 10 and 20 years	0%	50%
Between 20 and 30 years	0%	60%
Between 30 and 40 years	0%	80%
Over 40 years	0%	100%

Risk Analysis

The debt maturity profile is actively managed to ensure that debt maturity is prudently spread across future years. This ensures that the Council can properly plan for the maturity of its borrowings, and is not exposed to unmanageable risks.

g) Total principal sums invested for periods longer than 365 days

Under the Local Government Act 2003 and the MHCLG Guidance on Local Authority Investments (revised 2018), all Councils are permitted to invest for periods exceeding 1 year (or 365 days). The Council is required to set a limit to the level of such investments it might wish to make.

This limit can be expressed as a percentage or as an absolute amount (i.e. a monetary figure). The Council has chosen to work to a limit represented as an absolute amount as officers consider this to be the most transparent method and the more straightforward to monitor.

The limits have been set at a level that would allow for monies not anticipated to be spent in year to be invested for longer periods if interest rates are favourable.

Treasury Management Strategy – Appendix 3 cont.

The proposed limits for the forthcoming, and following four financial years are as follows.

Upper limit on investments for periods longer than 365 days					
	2019-20	2020-21	2021-22	2022-23	2023-24
	Upper Limit £m	Upper Limit £m	Upper Limit £m	Upper Limit £m	Upper Limit £m
Investments > 365 days	14	12	10	10	10

This upper limit has been calculated at a prudent level with regard to cashflow liquidity, capped at the maximum of 20% of forecast average (HRA & GF) cash balances in each year.

Minimum Revenue Provision Policy Statement

1.1 The Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008, which came into force in February 2008, require local authorities to make 'prudent provision' for the repayment of its General Fund debt. This debt repayment is known as the Minimum Revenue Provision (MRP).

1.2 A number of options for prudent provision are set out in the regulations. The underlying principle is that the repayment of debt should be aligned to the useful life of the asset or assets for which the borrowing has been carried out.

1.3 Since 2007-08 the Council has used the transitional measures available to calculate MRP for all capital expenditure prior to 1 April 2008 as if the previous regulations were still in force.

1.4 The authority is required, under the 2008 regulations, to prepare an annual statement of their policy on making MRP for submission to Council. The Council's policy statement on MRP for 2018-19 is set out below. The policy is considered by the Chief Finance Officer (CFO) to provide for the prudent repayment of debt.

1.4.1 The Council has implemented the 2008 CLG Minimum Revenue Provision (MRP) guidance from 2008-09 onwards, and assessed their MRP from 2008-09 onwards in accordance with the main recommendations contained within the guidance issued by the Secretary of State under section 21(1A) of the Local Government Act 2003.

1.4.2 MRP relating to the historic debt liability incurred for years up to and including 2007-08 will continue to be charged at the rate of 4% on the reducing balance, in accordance with option 1 of the guidance, the "regulatory method".

1.4.3 The debt liability relating to capital expenditure incurred from 2008-09 onwards will be subject to MRP under option 3, the "asset life method", and will be charged over a period that is reasonably commensurate with the estimated useful life applicable to the nature of expenditure, using the equal annual instalment method. For example, capital expenditure on a new building, or on the refurbishment or enhancement of a building, will be related to the estimated life of that building.

1.4.4 Estimated life periods will be determined in line with accounting guidance and regulations. To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the guidance, the Council will generally adopt these periods. However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate.

Treasury Management Strategy – Appendix 4 cont.

1.4.5 As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis that most reasonably reflects the anticipated period

of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner that reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

1.4.6 The Council will seek to spread MRP charges prudently in relation to asset lives, and with regard to the revenue impact of MRP charges. Where prudent to do so, capital receipts will be used to repay borrowing previously taken out in relation to assets with a short life. MRP on residual debt will be based on the lives of the remaining asset for which borrowing was undertaken.

1.4.7 MRP will be charged from the financial year after the asset comes into use.

1.4.8 In cases where the Council has approved the use of capital receipts to fund the asset, this funding will be assumed when the receipt is contractually certain, even if not actually received. In such cases no MRP charge will be made.

1.4.9 No MRP will be charged in respect of capital expenditure funded by borrowing where the expectation is that a future capital receipt will be applied to the CFR as a voluntary debt repayment for the borrowing - for example capital expenditure on preparing assets for sale. Where this approach is used it will be reviewed on an annual basis, in consideration of updated expectations over the timing and certainty of capital receipts, and to ensure that the latest estimate of proceeds is sufficient to cover the MRP liability.

1.4.10 Where finance leases are held on the balance sheet, the MRP will be set at a charge equivalent to the element of the annual lease charge that goes to write down the balance sheet liability, thereby applying Option 3 in a modified form.

1.4.11 The Council will take advantage of any transitional arrangements introduced to minimise or negate the impact of retrospective accounting adjustments as a result of new accounting guidance or proper practice.

1.4.12 In respect of loans to third parties supported by borrowing, where these are treated as capital expenditure, and contractual terms are in place to secure repayment over a period not exceeding the life of the asset, the Council will not charge MRP on the related expenditure; the CFR will be reduced by the third party loan repayments as and when these are received.

Treasury Management Strategy – Appendix 4 cont

1.4.13 In respect of infrastructure improvements and other capital schemes where repayment of the funding (principal and interest) will be met from business rates uplift in line with the Enterprise Zone financial model, and

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1.4.14 the repayment does not exceed the life of the asset, the Council will not charge MRP on the related expenditure; the CFR will be reduced by the amount of repayment of principal through business rates as and when these are made.

1.4.15 The Minimum Revenue Provsion Policy Statement will be continuously reviewed throughout the financial year and particularly with respect to any devlopments in the Council's Effciency Plan. Any required amendments or changes will be brought back to Council for approval.

Treasury Management Strategy – Appendix 5

Interest Rate Forecast Commentary – Link Asset Services (LAS)

The interest rate forecasts applied in this Strategy are predicated on an assumption of an agreement being reached on Brexit between the UK and the EU.

In the event of an orderly non-agreement exit, it is likely that the Bank of England would take action to cut Bank Rate in order to help economic growth deal with the adverse effects of this situation. This is also likely to cause short to medium term gilt yields to fall.

If there was a disorderly Brexit, then any cut in Bank Rate would be likely to last for a longer period and also depress short and medium gilt yields correspondingly.

It is also possible that the government could act to protect economic growth by implementing fiscal stimulus.

Balance of risks to the UK

- The overall balance of risks to economic growth in the UK is probably neutral.
- The balance of risks to increases in Bank Rate and shorter term PWLB rates, are probably also even and are broadly dependent on how strong GDP growth turns out, how slowly inflation pressures subside, and how quickly the Brexit negotiations move forward positively.

One risk that is both an upside and downside risk, is that all central banks are now working in very different economic conditions than before the 2008 financial crash as there has been a major increase in consumer and other debt due to the exceptionally low levels of borrowing rates that have prevailed for ten years since 2008.

This means that the neutral rate of interest in an economy (i.e. the rate that is neither expansionary nor deflationary) is difficult to determine definitively in this new environment, although central banks have made statements that they expect it to be much lower than before 2008. Central banks could therefore either over or under do increases in central interest rates.

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

- Brexit: if it were to cause significant economic disruption and a major downturn in the rate of growth;
- Bank of England monetary policy: MPC takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate;
- A resurgence of the Eurozone sovereign debt crisis;
- Weak capitalisation of some European banks;
- Further increases in interest rates in the US; this could spark a sudden flight of investment funds from more risky assets e.g. shares, into bonds yielding a much improved yield;

Treasury Management Strategy – Appendix 5 cont.

- Concerns around US corporate debt: levels have swollen massively during the period of low borrowing rates in order to finance mergers and acquisitions;

- Geopolitical risks: especially North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.

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

- Brexit: if both sides were to agree a compromise that removed all threats of economic and political disruption;
- Bank of England monetary policy: MPC is too slow in its pace and strength of increases in Bank Rate and, therefore, allows inflation pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect;
- The US misjudging the pace and strength of increases in interest rate: and in the pace and strength of reversal of QE, which then leads to a fundamental reassessment by investors of the relative risks of holding bonds, as opposed to equities. This could lead to a major flight from bonds to equities and a sharp increase in bond yields in the US, which could then spill over into impacting bond yields around the world;
- UK inflation: whether domestically generated or imported, inflation returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

Treasury Management Strategy – Appendix 6

Economic Commentary – Link Asset Services (LAS)

GLOBAL OUTLOOK; World growth has been doing reasonably well, aided by strong growth in the US. However, US growth is likely to fall back in 2019 and, together with weakening economic activity in China, overall world growth is likely to weaken. Inflation has been weak during 2018 but, at long last, unemployment falling to remarkably low levels in the US and UK has led to a marked acceleration of wage inflation which is likely to prompt central banks into a series of increases in central rates. The EU is probably about a year behind in a similar progression.

KEY RISKS; Looking back on nearly ten years since the financial crash of 2008 when liquidity suddenly dried up in financial markets, it can be assessed that central banks' monetary policy measures to counter the sharp world recession were successful. The key monetary policy measures they used were a combination of lowering central interest rates and flooding financial markets with liquidity, particularly through unconventional means such as quantitative easing (QE), where central banks bought large amounts of central government debt and smaller sums of other debt.

The key issue now is that that period of stimulating economic recovery and warding off the threat of deflation, is coming towards its close. A new period has already started in the US, and more recently in the UK, of reversing those measures i.e. by raising central rates and (for the US) reducing central banks' holdings of government and other debt. These measures are now required in order to stop the trend of a reduction in spare capacity in the economy, and of unemployment falling to such low levels that the re-emergence of inflation is viewed as a major risk. It is, therefore, crucial that central banks get their timing right and do not cause shocks to market expectations that could destabilise financial markets. In particular, a key risk is that because QE-driven purchases of bonds drove up the price of government debt, and therefore caused a sharp drop in income yields, this also encouraged investors into a search for yield and into investing in riskier assets such as equities. Consequently, prices in both bond and equity markets rose to historically high valuation levels simultaneously. This now means that both asset categories are vulnerable to a sharp downward correction. It is important, therefore, that central banks only gradually unwind their holdings of bonds in order to prevent destabilising the financial markets. It is also likely that the timeframe for central banks unwinding their holdings of QE debt purchases will be over several years. They need to balance their timing to neither squash economic recovery, by taking too rapid and too strong action, or, conversely, let inflation run away by taking action that was too slow and/or too weak. The potential for central banks to get this timing and strength of action wrong are now key risks.

The world economy also needs to adjust to a sharp change in liquidity creation over the last five years where the US has moved from boosting liquidity by QE purchases, to reducing its holdings of debt. In addition, the European Central Bank has cut back its QE purchases substantially and is likely to end them completely by the end of 2018.

UK; The flow of positive economic statistics since the end of the first quarter this year has shown that pessimism was overdone about the poor growth in quarter 1 when adverse weather caused a temporary downward blip. Quarter 1 at 0.1% growth in

Treasury Management Strategy – Appendix 6 cont.

GDP was followed by a return to 0.4% in quarter 2; quarter 3 is expected to be robust at around +0.6% but quarter 4 is expected to weaken from that level.

At their November meeting, the MPC reiterated that future Bank Rate increases would be gradual and would rise to a much lower equilibrium rate (where monetary policy is neither expansionary of contractionary) than before the crash; indeed they gave a figure for this of around 2.5% in ten years time but declined to give a medium term forecast. However, with so much uncertainty around Brexit, they warned that the next move could be up or down, even if there was a disorderly Brexit. While it would be expected that Bank Rate could be cut if there was a significant fall in GDP growth as a result of a disorderly Brexit, so as to provide a stimulus to growth, they warned they could also *raise* Bank Rate in the same scenario if there was a boost to inflation from a devaluation of sterling, increases in import prices and more expensive goods produced in the UK replacing cheaper goods previously imported, and so on. In addition, the Chancellor has held back some spare capacity to provide a further fiscal stimulus if needed.

It is unlikely that the MPC would increase Bank Rate in February 2019, ahead of the deadline in March for Brexit. Getting parliamentary approval for a Brexit agreement on both sides of the Channel will take well into spring next year. However, in view of the hawkish stance of the MPC at their November meeting, the next increase in Bank Rate is now forecast to be in May 2019. The following increases are then forecast to be in February and November 2020 before ending up at 2.0% in February 2022.

Inflation; The Consumer Price Index (CPI) measure of inflation fell from 2.7% to 2.4% in September. In the November Bank of England quarterly inflation report, inflation was forecast to still be marginally above its 2% inflation target two years ahead, (at about 2.1%), given a scenario of minimal increases in Bank Rate. This inflation forecast is likely to be amended upwards due to the Bank's inflation report being produced prior to the Chancellor's announcement of a significant fiscal stimulus in the Budget; this is likely to add 0.3% to GDP growth at a time when there is little spare capacity left in the economy, particularly of labour.

As for the labour market, unemployment has continued at a 43 year low of 4% on the Independent Labour Organisation measure. A combination of job vacancies hitting an all-time high in July, together with negligible growth in total employment numbers, indicates that employers are now having major difficulties filling job vacancies with suitable staff. It was therefore unsurprising that wage inflation picked up to 3.1%, (3 month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates less CPI inflation), earnings are currently growing by about 0.7%, the highest level since 2009. This increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. This tends to confirm that the MPC was right to start on a cautious increase in Bank Rate in August as it views wage inflation in excess of 3% as increasing inflationary pressures within the UK economy.

USA; The US easing of fiscal policy is fuelling a termorary boost in consumption which has generated an upturn in the rate of strong growth which rose from 2.2%

(annualised rate) in quarter 1 to 4.2% in quarter 2 and 3.5% (3.0% y/y) in quarter 3, but also an upturn in inflationary pressures. In particular, wage rates were increasing

at 3.1% y/y in October and heading higher due to unemployment falling to a 49 year low of 3.7%. With CPI inflation over the target rate of 2% and on a rising trend towards 3%, the Fed increased rates another 0.25% in September to between 2.00% and 2.25%, this being the fourth increase in 2018. They also indicated that they expected to increase rates four more times by the end of 2019. The dilemma, however, is what to do when the temporary boost to consumption wanes, particularly as the recent imposition of tariffs on a number of countries' exports to the US (China in particular) could see a switch to US production of some of those goods, but at higher prices. Such a scenario would invariably make any easing of monetary policy harder for the Fed in the second half of 2019. However, a combination of an expected four increases in rates of 0.25% by the end of 2019, together with a waning of the boost to economic growth from the fiscal stimulus in 2018, could combine to depress growth below its potential rate, i.e. monetary policy may prove to be too aggressive and lead to the Fed having to start on cutting rates. The Fed has also been unwinding its previous quantitative easing purchases of debt by gradually increasing the amount of monthly maturing debt that it has not been reinvesting.

The tariff war between the US and China has been generating a lot of heat during 2018, but it is not expected that the current level of actual action would have much in the way of a significant effect on US or world growth. However, there is a risk of escalation. The results of the mid-term elections are not expected to have a material effect on the economy.

Eurozone; Growth was 0.4% in quarters 1 and 2 but fell back to 0.2% in quarter 3, though this is probably just a temporary dip. In particular, data from Germany has been mixed and it could be negatively impacted by US tariffs on a significant part of manufacturing exports e.g. cars. For that reason, although growth is still expected to be in the region of nearly 2% for 2018, the horizon is less clear than it seemed just a short while ago. Having halved its quantitative easing purchases of debt in October 2018 to €15bn per month, the European Central Bank has indicated it is likely to end all further purchases in December 2018. Inflationary pressures are starting to build gently so it is expected that the ECB will start to increase rates towards the end of 2019.

China; Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems. Progress has been made in reducing the rate of credit creation, particularly from the shadow banking sector, which is feeding through into lower economic growth. There are concerns that official economic statistics are inflating the published rate of growth.

Japan; Japan has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy. It is likely that loose monetary policy will endure for some years yet to try to stimulate growth and modest inflation.

Emerging countries; Argentina and Turkey are currently experiencing major headwinds and are facing challenges in external financing requirements well in excess of their reserves of foreign exchange. However, these countries are small in terms of the overall world economy, (around 1% each), so the fallout from the expected recessions in these countries will be minimal.

Treasury Management Strategy – Appendix 7

Annual Investment Strategy

1 Investment policy

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 managed by the treasury management team. Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy.

1.2 The Council's appetite for risk must be clearly identified in its strategy report. The Council affirms that its investment policies are underpinned by a strategy of prudent investment of funds held on behalf of the local community. The objectives of the investment policy are firstly the security of funds (protecting the capital sum from loss) and then liquidity (keeping money readily available for expenditure when needed). Once approved levels of security and liquidity are met, the Council will seek to maximise yield from its investments, consistent with the applying of the agreed parameters. These principles are carried out by strict adherence to the risk management and control strategies set out in the TMP Schedules and the Treasury Management Strategy.

1.3 Responsibility for risk management and control lies within the Council and cannot be delegated to an outside organisation.

2 Creditworthiness policy

2.1 The Council's counterparty and credit risk management policies and its approved instruments for investments are set out below. These, taken together, form the fundamental parameters of the Council's Investment Strategy.

2.2 The Council defines high credit quality in terms of investment counterparties as those organisations that:

- Meet the requirements of the creditworthiness service provided by the Council's external treasury advisors and;
- Have sovereign ratings of AA or above, or are;
- UK banking or other financial institutions or are;
- UK national or local government bodies or are;
- Triple A rated Money Market funds.

3 Sovereign limits

3.1 The Council has determined that for 2019-20 it will only use approved counterparties from countries with a sovereign credit rating from at least one of the three main ratings agencies of at least AA-. However the limit for the amount that may be invested and the duration of the investment will be banded according to the sovereign rating. These limits are set out in the table at paragraph 7.4 below.

Treasury Management Strategy – Appendix 7 cont.

4 Investment position and use of Council's resources

4.1 The application of resources, such as capital receipts, reserves etc, to either finance capital expenditure or for other budget decisions to support the revenue budget will have an ongoing impact on investments balances and returns unless resources are supplemented each year from new sources such as asset sales. Detailed below are estimates of the Council's year end investment balances (excluding third party loans):

	2019-20 £m	2020-21 £m	2021-22 £m	2022-23 £m	2023-24 £m
Forecast Investment Balances (at 31st March)	45	23	19	10	6

4.2 Investment decisions will be made with reference to the core balance, cash flow requirements and the outlook for interest rates.

4.3 The Council is currently maintaining an under-borrowed position against its capacity to borrow. This means that the capital borrowing need (the Capital Financing Requirement) has not been fully funded with loan debt, but cash supporting the Council's reserves, balances and positive cash flows have been used to fund capital expenditure as a temporary measure. This strategy is prudent at this time as the cost of raising additional borrowing outweights the potential investment returns achievable. Furthermore, applying cash balances in this manner assists in managing counterparty risk.

5 Specified investments

5.1 Under the Local Government Act 2003 the Council is required to have regard to the CLG Guidance on Local Government Investments. This requires that investments are split into two categories:

(i) Specified investments – broadly, sterling investments, not exceeding 365 days and with a body or investment scheme of high credit quality.

(ii) Non-specified investments – do not satisfy the conditions for specified investments. This may include investment products that would normally be considered as specified investments, but are judged to have a higher level of risk than normal attached to them.

5.2 The detailed conditions attached to each of these categories are set out in the TMP Schedules.

5.3 The majority of the Council's investments in 2019-20 will fall into the category of specified investments.

6 Non-specified investments

6.1 Prior to the start of each financial year officers review which categories of non-specified investments they consider could be prudently used in the coming year.

6.2 The recommendation for 2019-20 is that the following non-specified investments may be entered into:

6.2.1 Long-term investments (those for periods exceeding 365 days), which could prudently be used where interest rates are favourable and funds are not required for short-term cashflow management. Amounts deposited for over 365 days will be determined by liquidity considerations and by whether longer term interest rates are favourable, and all deposits will be in accordance with counterparty limits. Only counterparties in the Council's current approved counterparty list that have durationlimits of over 365 days will be used for such investments. Any overall stricter limits in force in the Council's investment counterparty policies at any time will take precedence.

6.2.2 The following items, being non-specified only by virtue of the Council's lack of previous exposure to these instruments, are:

- UK Government Gilts;
- Treasury Bills;
- Bonds issued by a financial institution that is guaranteed by the UK Government and multi-lateral development banks as defined in Statutory Instrument 2004 No. 534;
- Reverse Gilt Repos;
- Commercial paper;
- Gilt funds and other bond funds;
- Enhanced money market funds;

Before proceeding with any of the above treasury management staff will take advice from the Council's external treasury advisors as appropriate, ensure that they fully understand the product and its risks, and prepare a business case to be signed off by the CFO.

7 Counterparties

7.1 Over-arching policies for the management of counterparty and credit risk are set out in the TMP Schedules. The Council's approach to counterparties for 2019-20 is set out below.

7.2 The CFO will use the recommendations of the creditworthiness service provided by the Council's external treasury advisors to determine suitable counterparties and the maximum period of investment, using the ratings assigned.

Treasury Management Strategy – Appendix 7 cont.

7.3 The CFO will determine, in the context of the above, and taking into account appropriate risk management factors:

- Any further criteria to be put in place to determine suitable counterparties;
- The maximum investment amount to be held with each type of counterparty assigned a rating;
- The maximum investment period with each type of counterparty assigned a rating.

7.4 The following table sets out the Council's counterparty criteria for 2019-20.

Investments may be placed with counterparties recommended by the Council's external treasury advisors, and which meet the following criteria			
	Counterparty Type	**Limit; per individual counterparty or banking group**	**Limits; Duration**
(1a)	UK Government	£20m	5 years
(1b)	UK nationalised or part nationalised banking institutions	£20m	1 years
(1c)	Other UK counterparties	£15m	3 years
(1d)	Other Local Authorities	£10m	3 years
(2a)	Non UK counterparties having a sovereign rating of AAA	£15m	3 years
(2b)	Non UK counterparties having a sovereign rating of AA+	£10m	2 years
(2c)	Non UK counterparties having a sovereign rating of AA	£5m	1 year
(3)	Money Market Funds (CNAV/LNAV) having a credit rating of AAA	£15m	N/A - Liquid deposits
(4)	Pooled Property Funds	£10m	5 years

Treasury Management Strategy – Appendix 7 cont.

7.5 Maximum counterparty limits may be temporarily exceeded by small amounts and for very short periods where interest is added by the counterparty to the principal investment amount, for example in the case of some call and deposit accounts. In such instances the interest amounts will be withdrawn back to the Council's main bank account as soon as reasonably practicable.

7.6 Any types of investments that fall within the category of specified investments as set out in the TMP Schedules and any types of non-specified investments approved as part of this document may be made within the bounds of the counterparty policies.

7.7 The total value of investments over 365 days at any one time is restricted by the treasury indicator for the upper limit on investments for periods longer than 365 days.

7.8 The Council may enter into forward agreements up to 3 months in advance of the investment commencing. If forward deposits are to be made, the forward period plus the deal period should not exceed the limits above.

7.9 The CFO has discretion during the financial year to lift or increase the restrictions on the counterparty list and/or to adjust the associated lending limits on values and periods should it become necessary to enable the effective management of risk in relation to investments. At all times the Council's minimum level of credit risk, as set out in the TMP Schedules, will be met.

8 Liquidity of Investments

8.1 Most short-term investments are held for cashflow management purposes and officers will ensure that sufficient levels of short-term investments and cash are available for the discharge of the Council's liabilities.

8.2 Investment periods range from overnight to 365 days as specified investments, or 5 years as non-specified investments. When deciding the length of each investment, regard is had to both cashflow needs and prevailing interest rates. As cash balances available for investment are forecast to be somewhat reduced compared to previous years, the preservation of liquidity will be a critical determinant for treasury officers when determining the value and duration of investments.

8.3 Amounts deposited for over 365 days will also be determined by liquidity considerations and by whether longer term interest rates are favourable, and all deposits will be in accordance with counterparty limits and the treasury indicator for investments over 365 days. Long term investments of over 2 years will only be made in exceptional circumstances and with approval of the CFO.

8.4 For short term and overnight investment, the Council makes full use of triple A rated Money Market Funds (CNAV and LNAV) and bank call and deposit accounts offering competitive rates and, in most instances, instant access to funds.

8.5 The Council may occasionally undertake short-term temporary borrowing if this is needed to cover its cash flow position.

9 Investments defined as capital expenditure

9.1 The acquisition of share capital or loan capital in any corporate body is defined as capital expenditure under Regulation 25(1) (d) of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003. Such investments will have to be funded from capital or revenue resources and will be classified as 'non-specified investments'.

9.2 Investments in money market funds which are collective investment schemes and bonds issued by multilateral development banks – both defined in SI 2004 No 534 – will not be treated as capital expenditure.

9.3 A loan or grant or financial assistance by this Council to another body, for capital expenditure by that body, will be treated as capital expenditure by the Council.

10 Lending to third parties

10.1 Officers will ensure that any loans to or investments in third parties comply with legislative requirements. This would normally, but not necessarily, be under one of the following Acts of Parliament:

- The Localism Act 2011 gives local authorities a general power of competence to act in the same manner as any other legal person, except where those powers are specifically limited by statute;

- The Local Government Act 2000 contains wellbeing powers for local government that allow local authorities to do anything, including to give financial assistance to any person, which they believe is likely to promote or improve the economic, social or environmental well being of their area. Certain conditions, including consultation requirements, must be complied with in order to meet the requirements allowing the local authority to use the wellbeing powers.

10.2 Loans of this nature must be approved by Cabinet. The primary aims of the Investment Strategy, in order of priority, are the security of its capital, liquidity of its capital and then to obtain a return on its capital commensurate with levels of security and liquidity. These aims are crucial in determining whether to proceed with a potential loan to a third party.

10.3 Recipients of this type of investment are unlikely to be a financial institution and therefore unlikely to be subject to a credit rating. In order to ensure security of the Council's capital, financial due-diligence must be completed prior to any loan or investment being agreed. The Council will use specialist advisors to complete financial checks to ascertain the creditworthiness of the third party. Where deemed necessary, additional guarantees will be sought. This will be via security against assets and/or through guarantees from a parent company.

11 Provisions for credit related losses

11.1 If any of the Council's investments appears at risk of loss due to default (i.e. this is a credit related loss and not one resulting from a fall in price due to movements in interest rates) the Council may make a prudent revenue provision of an appropriate amount.

12 Banking services

12.1 It is the Council's intention that, should the event of the credit rating downgrade of the provider of its banking services lead to that bank falling below the Council's minimum investment criteria, the bank may continue to be used for short-term liquidity requirements (kept under daily review).

13 End of year investment report

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