

## Treasury Management Strategy Statement 2021-2022

### 1.0 Introduction

- 1.1 The Local Government Act 2003 (the Act) and supporting regulations require the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice, and to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.
- 1.2 The Act therefore requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance issued subsequent to the Act) (included as Appendix 2 of this report), which sets out the Council's policies for managing its investments and in particular for giving priority to the security and liquidity of those investments.
- 1.3 Part of the treasury management operation is to ensure that the Council's 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 approach to risk management, providing adequate liquidity initially before considering investment return.
- 1.4 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.
- 1.5 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 balance.
- 1.6 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.

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.”

- 1.7 In 2019-2020 a new requirement for a capital strategy was introduced. The capital strategy provides 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.
- 1.8 The capital strategy provides 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
- 1.9 The aim of the capital strategy is to ensure that all elected councillors on Full Council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.
- 1.10 The 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 shows:
- 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
- 1.11 The recommended strategy for 2021-2022 in respect of the following aspects of the treasury management function is based upon the Director of Finance’s views on interest rates, supplemented with leading market forecasts provided by the Council’s treasury adviser, Link Group.

The strategy covers:

- treasury limits in force which will limit the treasury risk and activities of the Council
- Prudential and Treasury Indicators
- the current treasury position
- the borrowing requirement
- prospects for interest rates
- the borrowing strategy
- policy on borrowing in advance of need
- debt rescheduling
- the investment strategy
- creditworthiness policy
- policy on use of external service providers
- the Minimum Revenue Provision (MRP) strategy

### **1.12 Balanced budget requirement**

It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 32 requires a local authority, when calculating its budget requirement for the forthcoming financial year, to include the revenue costs that result from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby increases in interest charges, MRP and other costs associated with borrowing to finance capital expenditure, as well as any increases in running costs from new capital projects, are limited to a level which is affordable within the projected income of the Council for the foreseeable future.

### **1.13 Training**

The CIPFA Code requires the Director of Finance to ensure that councillors with responsibility for treasury management receive adequate training in treasury management. The training needs of councillors and treasury management employees are periodically reviewed to ensure that they have the appropriate level of knowledge for their roles in respect of treasury management.

### **1.14 Treasury management consultants**

The Council uses Link Group, Treasury solutions as its external treasury management advisors.

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

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

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, property funds and equity investments. The commercial type investments require specialist advisers, and the Council uses a range of consultants with relevant industry knowledge, dependant on the specific commercial aspects of the project, in relation to this activity.

## **2.0 Treasury limits for 2021-2022 to 2023-2024**

2.1 It is a statutory duty under Section 3 of the Act and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The

amount so determined is termed the “Affordable Borrowing Limit”. In England and Wales, the Authorised Limit represents the legislative limit specified in the Act.

- 2.2 The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future Council tax and Council housing rent levels is ‘acceptable’.
- 2.3 Whilst termed an “Affordable Borrowing Limit”, the capital plans to be considered for inclusion incorporate financing by both external borrowing and other forms of financing such as credit arrangements. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years. Details of the Authorised Limit can be found in Appendix 3 of this report.
- 2.4 The revised Treasury Management Code of Practice has removed the interest rate exposure indicator from a formal indicator to a narrative in the Treasury Management Strategy. The Council will continue to manage and monitor its interest rate exposure against the limits set previously:

Upper limit for fixed rate                      100%  
Upper limit for variable rate                      20%

### 3.0 Current portfolio position

- 3.1 The Council’s forecast treasury portfolio position at 31 March 2021 is shown below:

	Forecast £000	Average Rate %
<b>External Debt</b>		
Fixed rate borrowing - PWLB / Local Authorities	677,513	3.6549
Fixed rate borrowing - Market	55,800	4.4700
Variable rate borrowing - Market	48,000	4.2823
<b>Total Gross Borrowing</b>	<b>781,313</b>	<b>3.7581</b>
Other Long Term Liabilities	82,238	-
<b>Total External Debt</b>	<b>863,551</b>	<b>-</b>
<b>Total Investments *</b>	<b>5,000</b>	<b>0.1913</b>

\*It is the policy to use cash balances to fund capital expenditure to avoid the need for borrowing, therefore, the level of cash investments is forecast to be minimal.

#### 4.0 Borrowing requirement

4.1 The Council's forecast borrowing requirement is summarised below. The table shows the forecast external debt against the underlying capital borrowing need (the Capital Financing Requirement), highlighting any over or under borrowing:

External Debt	2020-2021	2021-2022	2022-2023	2023-2024
	Forecast £000	Forecast £000	Forecast £000	Forecast £000
Borrowing at 1 April	732,947	781,313	925,114	964,392
Expected change in borrowing	48,366	143,801	39,278	19,952
Other long term liabilities at 1 April	86,515	82,238	79,626	79,928
Expected change in other long term liabilities	(4,277)	(2,612)	302	(2,968)
Forecast debt at 31 March	863,551	1,004,740	1,044,320	1,061,304
Capital Financing Requirement	959,261	1,070,391	1,085,971	1,102,955
Under / (over) borrowing	95,710	65,651	41,651	41,651
<b>External debt for commercial activities / non-financial investments</b>				
Forecast debt at 31 March	41,317	45,874	45,874	45,874
Percentage of total external debt	5%	5%	4%	4%

#### 5.0 Prospects for interest rates

5.1 The Council has appointed Link Group as treasury advisor to the Council and part of their service is to assist the Council to formulate a view on interest rates. A more detailed interest rate view can be found in Appendix 2. The Link Group view of the Bank Rate is that it is unlikely to rise from the current 0.10% for a considerable period at the point of writing.

## 6.0 Borrowing strategy

### 6.1 Borrowing rates

The Link forecast for the PWLB new borrowing rate is as follows:

Link Group Interest Rate View		9.11.20													
These Link forecasts have been amended for the reduction in PWLB margins by 1.0% from 26.11.20															
	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	
BANK RATE	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	
5 yr PWLB	0.80	0.80	0.80	0.80	0.80	0.90	0.90	0.90	0.90	0.90	1.00	1.00	1.00	1.00	
10 yr PWLB	1.10	1.10	1.10	1.10	1.10	1.20	1.20	1.20	1.20	1.20	1.30	1.30	1.30	1.30	
25 yr PWLB	1.50	1.50	1.60	1.60	1.60	1.60	1.70	1.70	1.70	1.70	1.80	1.80	1.80	1.80	
50 yr PWLB	1.30	1.30	1.40	1.40	1.40	1.40	1.50	1.50	1.50	1.50	1.60	1.60	1.60	1.60	

**When undertaking any new borrowing the Director of Finance will give consideration to the following to ensure the best deal is obtained for the Council:**

1. Internal / external borrowing.
2. Temporary borrowing (less than 1 year).
3. Variable / fixed rate.
4. Short / long term borrowing.
5. PWLB / market debt.

When considering the above, the balance and spread of debt in the Council's portfolio will be taken into account along with the financial implications for the medium term financial strategy.

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 has been prudent since investment returns have been low and counterparty risk is still an issue that needs to be considered, however the Director of Finance will keep this strategy under review and consider opportunities to secure higher returns on investment where the balance of risk, return, security and liquidity are considered acceptable.

6.2 Sensitivity of the forecast – In normal circumstances the main sensitivities of the forecast are likely to be the two scenarios noted below. Council employees, in conjunction with the treasury advisers, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- if it was felt that there was a significant risk of a sharp fall in borrowing rates, then borrowing will be postponed.

- if it was felt that there was a significant risk of a much sharper rise in borrowing rates than that currently forecast, perhaps arising from an acceleration 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.

### **6.3 External versus internal borrowing**

The general aim of this treasury management strategy is to maintain cash balances at a reduced level, keeping under review the level of forecast reserves and therefore anticipated cash balances and opportunities for longer term investment, whilst maintaining an appropriate level of risk; therefore keeping to a minimum the credit risk incurred by holding investments. Measures taken over the last few years have already reduced the level of credit risk and the difference between borrowing rates and investment rates has been carefully considered to ensure the Council obtains value for money once an appropriate level of risk management has been attained to ensure the security of its investments.

Where investment rates are below long term borrowing rates, the Council can minimise its overall net treasury costs in the short term by continuing to avoid new external borrowing and by using internal cash balances to finance new capital expenditure or to replace maturing external debt (this is referred to as internal borrowing).

However, short term savings by avoiding new long term external borrowing will also be weighed against the potential for incurring additional long term extra costs by delaying unavoidable new external borrowing until later years when PWLB long term rates are forecast to be higher.

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

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 approved Capital Financing Requirement estimates, will be considered carefully to ensure value for money can be demonstrated and that the Council can ensure the security of such funds.

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 costs 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 increasing investment cash balances and the consequent increase in exposure to counterparty risk, and other risks, having regard to the controls in place to minimise such risks.

## **7.0 Debt rescheduling**

- 7.1 The spread between the rates applied to new borrowing and repayment of debt has meant that PWLB to PWLB debt restructuring is now much less attractive than it was. In particular, consideration would have to be given to the large premiums which would be incurred by prematurely repaying existing PWLB loans and it is very unlikely that these could be justified on value for money grounds in using replacement PWLB refinancing. Therefore, rescheduling of current borrowing in the Council's debt portfolio is unlikely to occur.
- 7.2 If rescheduling was done, it will be reported to the Cabinet (Resources) Panel, at the earliest meeting following its action.

## **8.0 New financial institutions as a source of borrowing**

- 8.1 Currently, the PWLB Certainty Rate is set at gilts + 80 basis points for both HRA and non-HRA borrowing. However, consideration may still need to be given to sourcing funding from the sources below for the following reasons:
- Local authorities (primarily shorter dated maturities out to three years or so as can still be cheaper than the Certainty Rate)
  - Financial institutions (primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a "cost of carry" or to achieve refinancing certainty over the next few years)
  - Municipal Bond Agency (possibly still a viable alternative depending on market circumstances prevailing at the time).

Our advisors will keep us informed as to the relative merits of each of these alternative funding sources.