Agenda Item

WARRINGTON BOROUGH COUNCIL

COUNCIL
28 February 2022

Report of	**Lynton Green, Director of Corporate Services (Section 151 Officer)/Deputy Chief Executive**	
Report Author	**Danny Mather, Head of Corporate Finance**	
Contact Details	**Email Address: dzmather@warrington.gov.uk**	**Telephone: 01925 442344**
Ward Members:	**All**	

TITLE OF REPORT: 2022/23 TREASURY MANAGEMENT STRATEGY

1. PURPOSE OF THE REPORT

1.1 This report sets out the Council's proposed Treasury Management Strategy for 2022/23. The report was reported to the Audit and Corporate Governance Committee (A&CGC) on 10 February 2022 and scrutinised by them. The A&CGC approved the report and recommended to go to Council for approval. The report is now presented to Council for approval.

2. BACKGROUND

2.1 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 activities is to ensure that cash flow is adequately planned, with sufficient cash being available when it is required to meet payment obligations. Surplus monies are invested, in reliance upon the statutory investment power, in counterparties or instruments approved by the Council as being commensurate with their risk appetite, with a view to ensuring that adequate liquidity takes precedence over investment return.

2.2 Treasury Management activity also incorporates financing the Council's capital activity that flows from its approved capital and non-treasury management investment plans, whether through the use of available resources, or through external borrowing. This element of activity seeks to balance aggregate borrowing needs over the longer term with the Council's Capital and Investment Strategy through arranging long and short term borrowing within a balanced risk portfolio approach. It may also be appropriate for certain loans taken out to be restructured in the future where variations in interest rate levels cause this to represent an appropriate risk balancing measure.

2.3 The contribution the treasury management function makes to the Council is critical, as balancing the borrowing and investment operation ensures liquidity and the ability to meet spending commitments as they fall due, either for day-to-day revenue requirements or for larger capital transactions. The treasury operation seeks to optimise the effect of borrowing costs and investment income on the Council's resources, whilst having careful regard to inherent risks. 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.

2.4 Whilst any commercial initiatives or loans to third parties may impact on the treasury management function, these activities are referred to by CIPFA as "non-treasury management activities" and thereby considered separately from the more normal form of day to day treasury management activities.

2.5 CIPFA defines treasury management as:

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

2.6 The Treasury Management Strategy is drawn from the Council's Treasury Policy Statement and covers investments, borrowing, the outlook for interest rates, the management of associated risks, prudential indicators and the policy to be adopted on the Minimum Revenue Provision (MRP).

2.7 The Council's 2022/23 Treasury Management Strategy is attached at Appendix 1. Whilst endeavours are made to limit the technical content of the Strategy, it is by its nature necessary to include technical aspects. Additional explanations are therefore contained within the glossary of terms in Annexe A with a view to helping Members' understanding of certain technical terms contained in the Strategy.

3 CONFIDENTIAL OR EXEMPT

Not confidential.

4 FINANCIAL CONSIDERATIONS

N/A

5. RISK ASSESSMENT

5.1 The Council would be putting its financial standing at risk, as well as failing to meet the requirements of the Local Government Act 2003, should it not have regard to the recommended procedures.

5.2 The Treasury Management Strategy and Prudential and Treasury Indicators reflect various assumptions of future interest rate movements and Government support for capital expenditure. These will be continually monitored and any necessary amendments will be made in accordance with the Strategy.

6. EQUALITY AND DIVERSITY/EQUALITY IMPACT ASSESSMENT

6.1 The Finance Service undertakes an Equality Impact Assessment (EIA) in its wider functions. Service changes that emerge from proposals contained in the treasury management strategy are subject to EI Assessments.

7. CONSULTATION

7.1 Not applicable.

8. REASONS FOR RECOMMENDATIONS

8.1 To ensure the Council's Treasury Management Strategy reflects the manner in which it has had regard to the revised 2021 CIPFA Treasury Management Code of Practice and Prudential Code.

9. RECOMMENDATIONS

9.1 Council approves the 2022/23 Treasury Management Strategy.

10. BACKGROUND PAPER

10.1 Treasury Management working papers.

Contacts for Background Papers:

Name	E-mail	Telephone
Danny Mather Head of Corporate Finance	dzmather@warrington.gov.uk	01925 442344

APPENDIX 1

2022/23 COUNCIL'S TREASURY MANAGEMENT STRATEGY

1. INTRODUCTION

1.1 Chartered Institute of Public Finance and Accountancy (CIPFA) published the revised Treasury Management Code and Prudential code on 20 December 2021 and has stated that formal adoption is not required until the 2023/24 financial year. This Council has to have regard to these codes of practice when it prepares the Treasury Management Strategy Statement and Annual Investment Strategy, and also related reports during the financial year, which are taken to Full Council for approval. The Council will adopt the codes in 2022/23.

1.2 The revised codes will have the following changes:

- A recommendation for the Council to adopt a new debt liability benchmark treasury indicator to support the financing risk management of the capital financing requirement;
- Clarify what CIPFA expects a local authority to borrow for and what they do not view as appropriate. This will include the requirement to set a proportionate approach to commercial and service capital investment;
- Address Environmental, Social and Governance (ESG) issues within the Capital Strategy;
- Suggested implementation of a policy to review commercial property;
- Create new Investment Practices to manage risks associated with non-treasury investment (similar to the current Treasury Management Practices);
- Ensure that any long term treasury investment is supported by a business model;
- Amendment to Treasury Management Practice One (TMP1) – Risk Management to address ESG policy within the treasury management risk framework;
- Amendment to the knowledge and skills register for individuals involved in the treasury management function to be proportionate to the size and complexity of the treasury management conducted by each council;
- A new recommendation to clarify reporting requirements for service and commercial investment;
- In addition, all investments and investment income must be attributed to one of the following three purposes:
    - **Treasury Management** – arising from the organisation's cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.
    - **Service Delivery** – investments held primarily and directly for the delivery of public services including housing, regeneration and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in cases where the income is "either related to the financial viability of the project in question or otherwise incidental to the primary purpose".

- **Commercial Return** – Investments held primarily for financial return with no treasury management or direct service provision purpose.

1.3 As this Treasury Management Strategy Statement and Annual Investment Strategy deals solely with treasury management investments, the categories of service delivery and commercial investments will be dealt with as part of the Capital Strategy report. Members will be updated on how all these changes would impact the current approach and any recommended changes that the Council decides to adopt will be formally included within the 2022/23 Treasury Management Strategy.

1.4 The primary recommendations of the Treasury Management Code are as follows:

(i) Creation and maintenance of an annual Treasury Management Policy Statement, which sets out the policies and objectives of the Council's treasury management activities.

(ii) Creation and maintenance of Treasury Management Practices, which set out the manner in which the Council will seek to achieve those policies and objectives:

- **Reporting Requirements**
  - **Capital Strategy** – The CIPFA 2021 Prudential and Treasury Management Codes recommend that all local authorities prepare a capital strategy report which will provide the following:-
    1. A high-level long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
    2. An overview of how the associated risk is managed
    3. The implications for future financial sustainability. The aim of the capital strategy is to ensure that all elected members of the Full Council understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

- **Treasury Management Reporting**
  - The Council Committee is currently recommended to receive and approve, as a minimum, three main reports each year (strategy, mid-year review and annual report on performance, detailed below) which should incorporate appropriate Policies, together with estimates and actuals of associated activities.

  - **Prudential and Treasury Indicators and Treasury Strategy** – the first, and most important report covers:
    1. The capital plans (including prudential indictors);
    2. A Minimum Revenue Provision (MRP) Policy (how residual capital debt liability is charged to revenue over time);
    3. The Treasury Management Strategy (how the investments and borrowings are to be organised) including treasury indicators; and
    4. An Investment Strategy (the parameters on how investments are to be managed).

- **A mid-year treasury management report** – this will update members with the progress of treasury management activity, amending prudential indicators as necessary, and identifying whether any policies require revision. In addition, the Council will receive quarterly update reports.

- **An annual treasury report** – this provides details of a selection of actual prudential and treasury indicators and treasury operations compared with the estimates previously included within the strategy.

(iii) Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

(iv) Delegation by the Council of the role of scrutiny of the Treasury Management Strategy and policies to a specific named body. For this Council, the delegated body is the Audit and Corporate Governance Committee.

1.4 The Council's Capital Strategy for 2022/23 is due to be approved by Cabinet on 14 February 2022 and Full Council on 28 February 2022.

1.5 The suggested Strategy for 2022/23 in respect of the following aspects of the Treasury Management function is based upon the views of treasury officers regarding interest rates, supplemented with leading market forecasts provided by the Council's treasury advisor (Link Asset Services). The Strategy covers two main areas:

Capital Issues

- The capital investment plans and the associated prudential indicators
- The Minimum Revenue Provision (MRP) Policy.

Treasury Management issues

- The current treasury position
- Treasury indicators which limit the treasury risk arising from activities of the Council
- Prospects for interest rates
- The borrowing strategy
- Policy on borrowing in advance of need
- Debt rescheduling opportunities
- The investment strategy
- ESG Policy
- Creditworthiness policy
- Policy on use of external service providers
- Future developments.

These elements reflect the Council having had regard to the requirements and recommendations of the Local Government Act 2003, the CIPFA Prudential Code, the DLUHC MRP Guidance, the CIPFA Treasury Management Code and the DLUHC Investment Guidance.

1.6 Separately, Section 32 of the Local Government Finance Act 1992 requires the Chief Finance Officer of the Authority to calculate and report upon its budget requirement for each financial year, and the adequacy of proposed financial reserves, to include the revenue costs which flow from capital financing decisions.

1.7 Section 3 of the Local Government Act 2003 requires that the Council must determine and keep under review how much money it can afford to borrow. In order to do this, it must have regard to the Prudential Code in order to determine an Affordable Borrowing Limit.

1.8 In general, the Prudential Code recommendations provide for close scrutiny and monitoring of capital investment plans in order to achieve a balance between investment needs and associated revenue consequences.

1.9 **Training**: the CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training. This especially applies to members responsible for scrutiny. Both internal and external training courses are provided to Members. Member training is a key theme from CIPFA and the Department for Levelling Up, Housing, Communities and Local Government (DLUHC). During 2022/23 a comprehensive training programme will be offered to all members and the training needs of treasury management officers are periodically reviewed.

2. TREASURY LIMITS FOR 2022/23

2.1 It is a statutory duty, under Section 3 of LGA 2003 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'. The Authorised Limit arising under the Prudential Code is intended to enable the statutory affordability requirement to be complied with.

2.2 The Council must have regard to the Prudential Code when setting its Affordable Borrowing Limit (ABL). This 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 rent levels is 'acceptable'.

2.3 Whilst termed an "Affordable Borrowing Limit", its extent represents mainly the Council's underlying capital investment "debt" liability, whether or not this is fully financed from external borrowing at any moment in time (e.g. the Council may on occasion use its own resources to finance new capital investment liabilities, rather than investing the monies externally). This underlying capital investment liability may also include any "credit arrangements" entered into by the Council, such as arise from leases. The ABL is determined at least annually, on a rolling basis, for the forthcoming financial year and two successive financial years.

2.4 Prudential and Treasury Indicators identified at Annexe B are relevant for the purposes of setting an integrated Treasury Management Strategy.

2.5 The Council is also recommended to indicate whether it has adopted the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management in Local Authorities (the Treasury Management Code). The original Treasury Management Code was adopted in 2004 at a full meeting of the Council, and the 2009 revised Treasury Management Code was adopted at a full meeting of the Council on 1 March 2010. The latest Amendments to the Code amended in 2017 are set out in section 8 of this report. Subject to any amendments by the Committee it will be forwarded to the Council for approval at its meeting of 28 February 2022.

3. CURRENT PORTFOLIO POSITION

3.1 The Council's treasury portfolio position as at 31st January 2022 comprised of:

Current Portfolio Position	Principal £m	Total £m	Average Interest Rate %
Fixed Rate Funding			
- Public Works Loans Board	1,179.048		2.169
- Money Market	119.317		2.264
- Temporary Borrowing	207.140	1,505.505	0.223
Variable Rate Funding			
- Public Works Loans Board			
- Money Market	150.000	150.000	0.871
TOTAL BORROWING		**1,655.505**	1.909
Council Investments			
- Externally Managed	(120.190)		5.396
- Internally Managed	(0.549)		2.894
- Call Accounts	(95.188)	(215.927)	0.036
TOTAL INVESTMENTS		**(215.927)**	**3.491**
NET BORROWING		**1,439.578**	
Non-Treasury Investments			
- Group Entities	(317.363)		
- Loans to Housing Assoc. & Commercial	(439.507)		
- Investment Properties	(389.180)	**(1,146.051)**	
Indicative Net Borrowing (after deduction of non-treasury investments)		**293.528**	

BORROWING REQUIREMENT

3.2 The capital investment plans provide details of the service and non-treasury management investment activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet these activities arising under the Council's Capital Strategy. This will involve both the organisation of the cash flow and, where capital plans require, and organisation of appropriate borrowing facilities. The Strategy covers the relevant treasury/prudential indicators, the current and projected debt positions and the annual Investment Strategy. The Council's capital investment plans are the key driver of treasury management activity.

3.3 The output of the capital investment plans is reflected in prudential indicators, which are designed to assist members' overview of performance.

3.4 The table below sets out the Council's future borrowing requirement (current and previous year are shown for comparison) based on current commitments and plans.

2020/21 Actual £m	2021/22 MTFP £m	2021/22 Estimate £m	Capital Investment	2022/23 Estimate £m	2023/24 Estimate £m	2024/25 Estimate £m	TOTAL 3 Years £m
351.525	404.064	304.690	Capital Expenditure	415.399	265.464	48.110	**728.973**
			Financed By:				
14.648	12.658	18.483	Capital Grants & Reserves	35.302	16.997	2.192	**54.491**
2.954	4.861	3.106	Capital Receipts	4.490	2.000	0	**6.490**
0.329	0	0.330	Council Revenue Funding	0	0	0	**0**
15.708	13.747	9.399	External Funding	7.170	5.500	8.500	**21.170**
317.887	**372.798**	**273.372**	**Financing need for year**	**368.437**	**240.967**	**37.418**	**646.822**

4. PROSPECTS FOR INTEREST RATES – please note: the forecast interest rates and economic date has been provided as at January 2022 for the report. The information is provided to members for their general understanding when reviewing the report but members should also have regard to the continuing changes to economic data.

4.1 The Council has appointed Link Group - Treasury Solutions as its external treasury management advisor and part of their service is to assist the Council to formulate a view on interest rates.

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

4.3 The Council 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.

4.4 Over the last two years, the coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16 December 2021. The forecast for the Bank Rate to reach 1.25% in November 2022, the suggested budgeted investment earning rates for returns on investments placed for period up to about three month during each financial year are as follows:

Average earning in each year	Amended	Previously
2022/23	1.00%	0.50%
2023/24	1.25%	0.75%
2024/25	1.25%	1.00%
2025/26	1.25%	1.25%
Years 6 to 10	1.50%	-
Years 10+	2.00%	2.00%

Link Asset Services' interest rate forecast

The following table gives their view:

	Bank Rate	**PWLB Borrowing Rates**			
		5 year	**10 year**	**25 year**	**50 year**
Dec-21	0.25%	1.40%	1.60%	1.80%	1.50%
Mar-22	0.75%	2.20%	2.30%	2.40%	2.20%
Jun-22	1.00%	2.30%	2.40%	2.50%	2.30%
Sep-22	1.00%	2.30%	2.40%	2.50%	2.30%
Dec-22	1.25%	2.30%	2.40%	2.60%	2.40%
Mar-23	1.25%	2.30%	2.40%	2.60%	2.40%
Jun-23	1.25%	2.30%	2.40%	2.60%	2.40%
Sep-23	1.25%	2.30%	2.40%	2.60%	2.40%
Dec-23	1.25%	2.30%	2.40%	2.60%	2.40%
Mar-24	1.25%	2.30%	2.40%	2.60%	2.40%
Jun-24	1.25%	2.30%	2.40%	2.60%	2.40%
Sep-24	1.25%	2.30%	2.40%	2.60%	2.40%
Dec-24	1.25%	2.30%	2.40%	2.60%	2.40%
Mar-25	1.25%	2.30%	2.40%	2.60%	2.40%

4.5 The forecast for Bank Rate has increased at a much faster pace than expected even in December. The increases in Bank Rates with rises of 0.25% in March, May and November 2022 to end at 1.25% during the forecast period.

4.6 **Significant risks to forecasts –**

- **Mutations** of the virus render current vaccines ineffective, and tweaked vaccines to combat these mutations are delayed, or cannot be administered fast enough to prevent further lockdowns. A percentage of the population not being vaccinated is also a significant risk to the NHS being overwhelmed and lockdowns being the only remaining option.
- **Labour and supply shortages** prove more enduring and disruptive and depress economic activity.
- **The Monetary Policy Committee** acts 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 currently anticipated.
- **The Monetary Policy Committee** tightens monetary policy too late to ward off building inflationary pressures.
- **The Government** acts too quickly to cut expenditure to balance the national budget.
- **UK/EU trade arrangements** if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.
- **Longer term US treasury yields** rise strongly and pull gilt yields up higher than forecast.
- **Major stock markets** e.g. in the US, become increasingly judged as being over-valued and susceptible to major price corrections. Central banks become increasingly exposed to the "moral hazard" risks of having to buy shares and corporate bonds to reduce the impact of major financial market selloffs on the general economy.
- **Geopolitical risks**, for example in Ukraine, Iran, North Korea, but also in Europe and Middle Eastern countries; on-going global power influence struggles between Russia/China/US. These could lead to increasing safe-haven flows.

4.7 **The balance of risks to the UK economy** – the overall balance of risks to economic growth in the UK is now to the downside, including risks from Covid and its variants – both domestically and their potential effects worldwide.

4.8 **Forecasts for Bank Rate** – The Monetary Policy Committee is now very concerned at the way that forecasts for inflation have had to be repeatedly increased within a matter of just a few months. Combating this rising tide of inflation is now its number one priority and the 5-4 vote marginally approving only a 0.25% increase on 4 February 2022 rather than a 0.50% increase, indicates it is now determined to push up Bank Rate quickly. A further increase of 0.25% is therefore probable for March, and again in May, followed possibly by a final one in November. However, data between now and November could shift these timings or add or subtract from the number of increases. However, it is likely that these forecasts will need changing within a relatively short timeframe for the following reasons:

4.8.1 It is not known whether there will be further mutations of Covid and how severe they may be, nor how rapidly scientific advances may be made in combating them.

4.8.2 The economy was running out of steam during the second half of 2021 and Omicron will mean that economic growth in quarter 1 of 2022 is likely to be flat, though on the rise towards the end of the quarter as the economy recovers. However, 54% energy cap cost increases from April, together with 1.25% extra employee national insurance, food inflation around 5% and council tax likely to rise in the region of 5% too – these increases are going to hit lower income families hard despite some limited assistance from the Chancellor to postpone the full impact of rising energy costs.

4.8.3 Consumers are estimated to be sitting on over £160bn of excess savings left over from the pandemic so that will cushion some of the impact of the increases. But most of those holdings are held by more affluent people whereas poorer people already spend nearly all their income before these increases hit and have few financial reserves.

4.8.4 These increases are already highly disinflationary; inflation will also be on a gradual path down after April so that raises a question as to whether the MPC may shift into protecting economic growth by November, i.e. it is more debatable as to whether they will deliver another increase then.

4.8.5 The big issue is with regard to the current spike in inflation and will it lead to a second-round effect in terms of labour demanding higher wages, (and/or lots of people getting higher wages by changing jobs).

4.8.6 If the labour market remains very tight during 2022, then wage inflation poses a greater threat to overall inflation being higher for longer, and the MPC may then feel it needs to take more action.

4.8.7 If the UK were to invoke article 16 of the Brexit deal over the dislocation in trading arrangements with Norther Ireland, this would have the potential to end up in a no-deal Brexit.

4.9 In summary, with the high level of uncertainty prevailing on several different fronts, it is expected that the forecasts will be revised again, in line with whatever the news is. It should also be borne in mind that Bank Rate being cut to 0.25% and then to 0.10%, were emergency measures to deal with the Covid crisis hitting the UK in March 2020. At any time, the MPC could decide to simply take away such emergency cuts on no other grounds than they are no longer warranted, and as a step forward in the return to normalisation. In addition, any Bank Rate under 1% is both highly unusual and highly supportive of economic growth.

4.10 **Forecasts for PWLB rates and gilt and treasury yields** – since the start of 2021, there has been a lot of volatility in gilt yields, and hence PWLB rates. The forecasts show little overall increase in gilt yields during the forecast period to March 2025 but there will doubtless be a lot of unpredictable volatility during this forecast period.

4.11 While monetary policy in the UK will have a major impact on gilt yields, there is also a need to consider the potential impact that rising treasury yields in America could have on UK gilt yields. As an average since 2011, there has been a 75% correlation between movements in US 10-year treasury yields and UK 10-year gilt yields. This is a significant upward risk exposure to the forecasts for longer term PWLB rates. However, gilt yields and treasury yields do not always move in unison.

4.12 **US treasury yields** – during the first part of 2021, US President Biden's, and the Democratic party's, determination to push through a $1.9trn (equivalent to 8.8% of GDP) fiscal boost for the US economy as a recovery package from the Covid pandemic was what unsettled financial markets. However, this was in addition to the $900bn support package already passed in December 2020. This was then followed by additional Democratic ambition to spend $1trn on infrastructure, (which was eventually passed by both houses later in 2021), and an even larger sum on an American families plan over the next decade; this is still caught up in Democrat / Republican haggling. Financial markets were alarmed that all this stimulus was happening at a time when:

4.12.1 A fast vaccination programme had enabled a rapid opening up of the economy during 2021

4.12.2 The economy was growing strongly during the first half of 2021 although it has weakened overall during the second half

4.12.3 It started from a position of little spare capacity due to less severe lockdown measures than in many other countries

4.12.4 The Fed was still providing substantial stimulus through monthly QE purchases during 2021

4.13 A combination of these factors would eventually cause an excess of demand in the economy which generated strong inflationary pressures. This has been recognised by the Fed at its December meeting with an aggressive response to damp inflation down during 2022 and 2023.

4.13.1 At the November Fed meeting, the Fed decided to make a start on tapering its $120bn per month of QE purchases so that they ended next June. However, at the December meeting it doubled the pace of tapering so that they will end all purchases in February. These purchases are currently acting as downward pressure on treasury yields and so it would be expected that Treasury yields will rise over the taper period and after the taper ends, all other thing being equal.

4.13.2 The Fed also forecast that it expected there would be three rate rises in 2022 of 0.25% from near zero currently, followed by three in 2023 and two in 2024, taking rates back above 2% to a neutral level for monetary policy. It also gave up on calling the sharp rise in inflation as being 'transitory'.

4.13.3 At its January meeting, the Fed became even more hawkish following inflation rising sharply even further. It indicated that rates would begin to rise very soon, i.e. it implied at is March meeting it would increase rates and start to run down its holding of QE purchases. It also appears likely that the Fed could take action to force longer term treasury yields up by prioritising selling holdings of tis longer bonds as yields at this end have been stubbornly low despite rising inflation risks. The low level of longer dated yields is a particular concern for the Fed because it is a key channel through which tighter monetary policy is meant to transmit to broader financial conditions, particularly in the US where long rates are a key driver of household and corporate borrowing costs.

4.14 There are also possible downside risks from the huge sums of cash that the UK populace have saved during the pandemic; when savings accounts earn little interest, it is likely that some of this cash mountain could end up being invested in bonds and so push up demand for bonds and support their prices, i.e. this would help to keep their yields down. How this will interplay with the Bank of England eventually getting round to not reinvesting maturing gilts and then later selling gilts, will have to be monitored.

4.15 There is likely to be exceptional volatility and unpredictability in respect of gilt yields and PWLB rates due to the following factors:

4.15.1 How strongly will changes in gilt yields be correlated to changes in US treasury yields? As the US financial markets are, by far, the biggest financial markets in the world, any upward trend in treasury yields will invariably impact and influence financial markets in other countries. Over 10 years since 2011 there has been an average 75% correlation between movements in US treasury yields and gilt yields. However, from time to time these two yields can diverge. Lack of spare economic capacity and rising inflationary pressures are viewed as being much greater dangers in the US than in the UK. This could mean that central bank rates will end up rising higher in the US than in the UK; the consequent increases in treasury yields could well spill over to cause (lesser) increases in gilt yields. There is, therefore, an upside risk to forecasts for gilt yields due to this correlation. The Link Group forecasts have included a risk of a 75% correlation between the two yields.

4.15.2 Will the Fed take action to counter increasing treasury yields if they rise beyond a yet unspecified level?

4.15.3 Would the MPC act to counter increasing gilt yields if they rise beyond a yet unspecified level?

4.15.4 How strong and enduring will inflationary pressures actually turn out to be in both the US and the UK and so put upward pressure on treasury and gilt yields?

4.15.5 How will central banks implement their new average or sustainable level inflation monetary policies when inflation has now burst through all previous forecasts and far exceeded their target levels? Or are they going to effectively revert to their

previous approach of prioritising focusing on pushing inflation back down and accepting that economic growth will be very much a secondary priority – until inflation is back down to target levels or below?

4.15.6 How well will central banks manage the withdrawal of QE purchases of their national bonds, i.e. without causing a panic reaction in financial markets as happened in the "taper tantrums" in the US in 2013?

4.15.7 Will exceptional volatility be focused on the short or long-end of the yield curve, or both?

4.15.8 If Russia were to invade Ukraine, this would be likely to cause short term volatility in financial markets, but it would not be expected to have a significant impact beyond that.

4.16 The forecasts are also predicated on an assumption that there is no break-up of the Eurozone or EU within the forecasting period, despite the major challenges that are looming up, and that there are no major disruptions in international relations, especially between the US and Russia, China/North Korea and Iran, which have a major impact on international trade and world GDP growth.

4.17 **The balance of risks to medium to long term PWLB rates** – there is a balance of upside risks to forecasts for medium to long term PWLB rates.

4.18 **A new era – a fundamental shift in central bank monetary policy** – one of the key results of the pandemic has been a fundamental rethinking and shift in monetary policy by major central banks like the Fed, the Bank of England and the ECB, to tolerate a higher level of inflation than in the previous two decades when inflation was the prime target to bear down on so as to stop it going above a target rates. There is now also a greater emphasis on other targets for monetary policy than just inflation, especially on achieving broad and inclusive maximum employment in its entirety in the US, before consideration would be given to increasing rates.

4.18.1 The Fed in America has gone furthest in adopting a monetary policy based on a clear goal of allowing the inflation target to be symmetrical, rather than a ceiling to keep under control, so that inflation averages out the dips down and surges above the target rate, over an unspecified period of time.

4.18.2 The Bank of England has also amended its target for monetary policy so that inflation should be sustainably over 2% before starting on raising Bank Rate and the ECB now has a similar policy.

4.18.3 For local authorities, this means that investment interest rates and very short term PWLB rates will not be rising as high as in previous decades when the economy recovers from a downturn and the recovery eventually runs out of spare capacity to fuel continuing expansion.

4.18.4 Labour market liberalisation since the 1970s has helped to break the wage price spirals that fuelled high levels of inflation and has now set inflation on a lower path which makes this shift in monetary policy practicable. In addition, recent changes in flexible employment practices, the rise of the gig economy and technological changes, will all help to lower inflationary pressures once economies recover from the various disruptions caused by the pandemic.

4.18.5 Governments will also be concerned to see interest rates stay lower as every rise in central rates will add to the cost of vastly expanded levels of national debt; (in the UK this is £21bn for each 1% rise in rates). On the other hand, higher levels of inflation will help to erode the real value of total public debt.

4.19 **Investment returns** – have started improving in the second half of 21/22 and are expected to improve further during 22/23 as the MPC progressively increases Bank Rate.

4.20 **Borrowing interest rates** – fell to historically very low rates as a result of the COVID crisis and the quantitative easing operations of the Bank of England and still remain at historically low levels. The policy of avoiding new borrowing by running down spare cash balances has served local authorities well over the last few years.

4.21 November 2020 the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates which had been increased by 100 bps in October 2019. The standard and certainty margins were reduced by 100 bps but a prohibition was introduced to deny access to borrowing form the PWLB for any local authority which had purchase of assets for yield in its three-year capital programme. The current margins over gilt yields are as follows:

Type of PWLB Loan	Rate of PWLB Loan	Abbreviation
PWLB Standard Rate	Gilt plus 100 basis points	G+100bs
PWLB Certainty Rate	Gilt plus 80 basis points	G+80bs
PWLB HRA Standard Rate	Gilt plus 100 basis points	G+100bs
PWLB HRA Certainty Rate	Gilt plus 80 basis points	G+80bs
Local Infrastructure Rate	Gilt plus 60 basis points	G+60bs

4.22 **Borrowing for capital expenditure** – the long term (beyond 10 years) forecast for Bank Rate is 2.00%. As nearly all PWLB certainty rates are now above this level, borrowing strategy will need to be reviewed, especially as the maturity curve has flattened out considerably. Better value can be obtained at the very short and at the long end of the curve and longer-term rates are still at historically low levels. Temporary borrowing rates are likely, however, to remain near Bank Rate and may also prove attractive as part of a balanced debt portfolio. In addition, there are some cheap alternative sources of long-term borrowing if an authority is seeking to avoid a “cost of carry” but also wishes to mitigate future re-financing risk.

4.23 While this authority will not be able to avoid borrowing to finance new capital expenditure, to replace maturing debt and the rundown of reserves, there will be a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new borrowing that causes a temporary increase in cash balances.

5. ECONOMIC BACKGROUND - please note - the Council's Treasury Advisors provided the economic information in February 2022, however further material changes may occur before the report goes to Council.

5.1 **Covid-19 vaccines** – these were important during 2021 which raised hopes that life in the UK would be able to largely return to normal in the second half of 2021. However, the Omicron mutation at the end of November, rendered the initial two doses of all vaccines largely ineffective in preventing infection. This ~~has~~ dashed such hopes and raised major concerns that a fourth wave of the virus could overwhelm hospitals in early 2022. Although the mutation is very fast spreading, it does not cause severe illness in fully vaccinated people. Rather than go for full lockdowns which heavily damage the economy, the government strategy this time is focused on getting as many people as possible to have a third (booster) vaccination after three months from the previous last injection. The government also placed restrictions on large indoor gatherings and hospitality venues over Christmas and into January and requested workers to work from home.

5.2 With the household saving rate having been exceptionally high since the first lockdown in March 2020, there is plenty of pent-up demand and purchasing power stored up for services in sectors like restaurants, travel, tourism and hotels which had been hit hard during 2021, but could now be hit hard again by either, or both, of government restrictions and/or consumer reluctance to leave home. Growth will also have been lower due to people being ill and not working, similar to the pingdemic in July. The economy, therefore, faces significant headwinds in early 2022 although some sectors have learned how to cope well with Covid. However, the biggest impact on growth would come from another lockdown if that happened. The big question still remains as to whether any further mutations of this virus could develop which render all current vaccines ineffective, as opposed to how quickly vaccines can be modified to deal with them and enhanced testing programmes be implemented to contain their spread until tweaked vaccines become widely available.

5.3 **A summary overview of the future path of Bank Rate**

- The threat from Omicron which caused huge national concern at the time of December MPC meeting has now reduced.
- The MPC shifted up a gear last week in raising Bank Rate by another 0.25% and narrowly avoiding making it a 0.50% increase by a 5-4 voting margin.
- The forecast now expects the MPC to deliver another 0.25% increase in March, the position appears to be to go for sharp increases to get the job done.
- The March increase is likely to be followed by an increase to 1.0% in May and then to 1.25% in November.
- The MPC is currently much more heavily focused on combating inflation than on protecting economic growth.

- However, 54% energy cap cost increases from April, together with 1.25% extra employee national insurance, food inflation around 5% and council tax likely to rise in the region of 5% too – these increases are going to hit lower income families hard despite some limited assistance from the Chancellor to postpone the full impact of rising energy costs.
- Consumers are estimated to be sitting on over £160bn of excess savings left over from the pandemic so that will cushion some of the impact of the above increases. But most of those holdings are held by more affluent people whereas poorer people already spend nearly all their income before these increases hit and have few financial reserves.
- The increases are already highly disinflationary; inflation will also be on a gradual path down after April so that raises a question as to whether the MPC may shift into protecting economic growth by November, i.e. it is more debatable as to whether they will deliver another increase then.
- There is an issue of whether the current spike in inflation will lead to a second-round effect in terms of labour demanding higher wages (and/or lots of people getting higher wages by changing jobs).
- If the labour market remains very tight during 2022, then wage inflation poses a greater threat to overall inflation being higher for longer, and the MPC may then feel it need to take more action.

5.4 **PWLB Rates**

- The yield curve has flattened out considerably.
- It is considered that the markets have already built in nearly all the effects on gilt yields of the likely increases in Bank Rate.
- It is difficult to say currently what effect the Bank of England starting to sell gilts will have on gilt yields once Bank Rate rises to 1%: it is likely to act cautiously as it has already started on not refinancing maturing debt. A passive process of not refinancing maturity debt could begin in March when the 4% 2022 gilt matures; the Bank owns £25bn of this issuance. A pure roll-off of the £875bn gilt portfolio by not refinancing bonds as they mature, would see the holdings fall to about £415nb by 2031, which would be about equal to the Bank's pre-pandemic holding. Last August, the Bank said it would not actively sell gilts until the "Bank Rate had risen to at least 1%" and, "depending on economic circumstance at the time".
- It is possible that Bank Rate will not rise above 1% as the MPC could shift to relying on quantitative tightening (QT) to do the further work of taking steam out of the economy and reducing inflationary pressures.
- Increases in US treasury yield over the next few years could add upside pressure on gilt yields though, more recently, gilts have been much more correlated to movement in bund yields than treasury yields.

5.5 **Monetary Policy Committee (MPC) meetings:**

- After the Bank of England became the first major western central bank to put interest rates up in this upswing in December, it has quickly followed up its first 0.15% rise by another 0.25% rise to 0.50%, in the second of what is very likely to be a series of increases during 2022.
- The MPC voted by a majority of 5-4 to increase Bank Rate by 25bps to 0.5% with the minority preferring to increase Bank Rate by 50bps to 0.75%. The Committee also voted unanimously for the following:

- ◊ To reduce the £875bn stock of UK government bond purchases, financed by the issuance of central bank reserves, by the issuance of central bank reserves, by ceasing to reinvest maturing assets.
- ◊ To begin to reduce the £20bn stock of sterling non-financial investment-grade corporate bond purchases by ceasing to reinvest maturing assets and by a programme of corporate bond sales to be completed no earlier than towards the end of 2023.

- The Bank again sharply increased its forecast for inflation – to now reach a peak of 7.25% in April, well above its 2% target.
- The Bank estimated that UK GDP rose by 1.1% in quarter 2 of 2021 but, because of the effect of Omicron, GDP would be flat in quarter 1, but with the economy recovering during February and March. Due to the hit to households' real incomes from higher inflation, it revised down its GDP growth forecast for 2022 from 3.75% to 3.25%.
- The Bank is concerned at how tight the labour market is with vacancies at near record levels and a general shortage of workers – who are in a very favourable position to increase earnings by changing jobs.
- As in the December 2021 MPC meeting, the MPC was more concerned with combating inflation over the medium term than supporting economic growth in the short term. However, what was notable was the Bank's forecast for inflation: based on the markets' expectations that Bank Rate will rise to 1.50% by mid-2023, it forecast inflation to be only 1.6% in three years' time. In addition, if energy prices beyond the next six months fell as the futures market suggests, the Bank said CPI inflation in three years' time would be even lower at 1.25%. With calculations of inflation, the key point to keep in mind is that it is the rate of change in prices – not the level – that matters. Accordingly, even if oil and natural gas prices remain flat at their current elevated level, energy's contribution to headline inflation will drop back over the course of this year. That means the current energy contribution to CPI inflation, of 2% to 3%, will gradually fade over the next year.
- It is considered that the Bank's forecast is not expecting the Bank Rate to rise to 1.5% in order to hit their target of CPI inflation of 2%. The immediate issue is with four members having voted for a 0.50% increase in February, it would only take one member more for there to be another 0.25% increase at the March meeting.
- The MPC's forward guidance on its intended monetary policy on raising Bank Rate versus selling (quantitative tightening) holdings of bonds is as follows:
  - Raising Bank Rate as "the active instrument in most circumstance".
  - Raising Bank Rate to 0.50% before starting on reducing its holdings.
  - Once Bank Rate is at 0.50% it would stop reinvesting maturing gilts.
  - Once Bank Rate had risen to at least 1%, it would start selling its holdings.

5.6 **Bank Rate Forecast**

- Covid remains a major potential downside threat as there may be further mutations. However, their severity and impact could vary widely, depending on vaccine effectiveness and how broadly it is administered.
- If the UK invokes article 16 of the Brexit deal over the dislocation in trading arrangements with Norther Ireland, this has the potential to end up in a no-deal Brexit
- Due to the uncertainty from a number of factors it will be necessary to revise the forecasts again.

5.7 **PWLB rates and gilt and treasury yields**

- **Gilt yields** – since the start of 2021 there has been a lot of volatility in gilt yields, and hence PWLB rates. The forecasts show little overall increase in gilt yields during the forecast period to March 2025 but there will doubtless be a lot of unpredictable volatility during this forecast period.
- While monetary policy in the UK will have a major impact on gilt yields, there is also a need to consider the potential impact that rising treasury yields in America could have on gilt yields.

5.8 **US treasury yields**

- During the first part of 2021, US President Biden's, and the Democratic party's determination to push through a $1.9trn (equivalent to 8.8% of GDP) fiscal boost for the US economy as a recovery package from the Covid pandemic was what unsettled financial markets. This was in addition to the £$900bn support package previously passed in December 2020. Financial markets were alarmed that all this stimulus was happening at a time when:
  - A fast vaccination programme roll-out had enabled a rapid opening up of the economy during 2021.
  - The economy was growing strongly during the first half of 2021 although it has weakened during the second half.
  - It started from a position of little spare capacity due to less severe lockdown measures than in many other countries.
  - The Fed was still providing substantial stimulus through monthly QE purchases during 2021.

- It was not much of a surprise that a combination of these factors would eventually cause an excess of demand in the economy which generated strong inflationary pressures. This has eventually been recognised by the Fed at its recent December meeting with an aggressive response to damp inflation down during 2022 and 2023.
  - At the November Fed meeting, the Fed decided to make a start on tapering its $120bn per month of QE purchases so that they ended next June. However, at its December meeting it doubled the pace of tapering so that they will end all purchases in February. These purchases are currently acting as downward pressure on treasury yields and so it would be expected that treasury yields will rise over the taper period, all other thing being equal.
  - It also forecast that it expected there would be three rate rises in 2022 of 0.25% from near zero currently, followed by three in 2023 and two in 2024. This would take rates back above 2% to a neutral level for monetary policy. It also gave up on calling the sharp rise in inflation as being 'transitory'.
  - At the January meeting, the Fed became even more hawkish following inflation rising sharply even further. It indicated that rates would begin to rise very soon, i.e. it implied at its March meeting it would increase rates and start to run down its holdings of QE purchases. It also appears likely that the Fed could take action to force longer term treasury yields up by prioritising selling holdings of its longer bonds as yields at this end have been stubbornly low despite rising inflation risks. The low level of longer dated yields is a particular concern for the Fed because it is a key channel through which tighter

monetary policy is meant to transmit to broader financial conditions, particularly in the US where long rates are a key driver of household and corporate borrowing costs.

- There are also possible downside risks form the huge sums of cash that the UK populace have saved during the pandemic; when savings accounts earn little interest, it is likely that some of this cash mountain could end up being invested in bonds and so push up demand for bonds and support their prices i.e., this would help to keep their yields down. How this will interplay with the Bank of England eventually getting round to not reinvesting maturing gilts and then selling gilts, will be interesting to monitor.

5.9 **European Union (EU)** – the European Central Bank (ECB) joined with the Fed by announcing in December that it will be reducing its QE purchases – by half from October 2022, i.e. it will still be providing significant stimulus via QE purchases during the first half of 2022. The ECB did not change its rate at its February meeting, but it was clearly shocked by the increase in inflation to 5.1% in January. The President of the ECB, Christine Lagarde, hinted in the press conference after the meeting that the ECB may accelerate monetary tightening before long and hinted that asset purchases could be reduced more quickly than implied by the previous guidance. The ECB President refused to reaffirm officials' previous assessment that interest rate hikes in 2022 are "very unlikely". It, therefore, now looks likely that all three major western central banks will be raising rates this year in the face of sharp increases in inflation – which is looking increasingly likely to be stubbornly high and for much longer than the previous often repeated 'transitory' descriptions implied.

5.10 **China –** the pace of economic growth has now fallen back after the initial surge of recovery from the pandemic and China has been struggling to contain the spread of the Delta variant through using sharp local lockdowns – which depress economic growth. However, with Omicron having now spread to China, and being much more transmissible, lockdown strategies may not prove so successful in future. To boost flagging economic growth, The People's Bank of China cut its key interest rate in December 2021.

5.11 **Japan –** 2021 was a patchy year in combating Covid. However, recent business surveys indicate that the economy is rebounding rapidly now that the bulk of the population is fully vaccinated, and new virus cases have plunged. The Bank of Japan is continuing its very loose monetary policy but with little prospect of getting inflation back towards its target of 2% any time soon.

5.12 **World growth -** was in recession in 2020 but recovered during 2021 until starting to lose momentum more recently. Inflation has been rising due to increases in gas and electricity prices, shipping costs and supply shortages, although these should subside during 2022. It is likely that there will be a period where there will be a reversal of world globalisation and a decoupling of western countries from dependence on China to supply products, and vice versa. This is likely to reduce world growth rates from those in prior decades.

5.13 **The downside risks to the UK economy -** the overall balance of risks to economic growth in the UK is now to the downside and the downside risks to current forecasts for UK gilt yields and PWLB rates include:

- **Mutations –** of the virus render current vaccines ineffective, and tweaked vaccines to combat theses mutations are delayed or unable to be administered fast enough to stop the NHS being overwhelmed.
- **Labour and supply shortages** – prove more enduring and disruptive and depress economic activity.
- **Bank of England** – acts 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 currently anticipated.
- **The Government** – acts too quickly to increase taxes and/or cut expenditure to balance the national budget
- **UK/EU trade arrangements** – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.
- **Geopolitical risks** – for example, in Ukraine/Russia, Iran, China, North Korea and Middle Eastern countries, which could lead to increasing safe-haven flows. If Russia were to invade Ukraine, this would be likely to cause short term volatility in financial markets, but it would not be expected to have a significant impact beyond that.

5.14 **The upside risks to current forecasts for UK gilt yields and PWLB rates**:

- The Bank of England is too slow in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than currently expected.
- Longer term US treasury yields rise strongly and pull gilt yields up higher than forecast.

5.15 **Supply Shortages** – the pandemic and extreme weather events, followed by a major surge in demand after lockdowns ended, have been highly disruptive of extended worldwide supply chains. Major queues of ships unable to unload their goods at ports in New York, California and China built up rapidly during quarters 2 and 3 of 2021 but then halved during quarter 4. Such issues have led to a misdistribution of shipping containers around the world and have contributed to a huge increase in the cost of shipping. Combined with a shortage of semi-conductors, these issues have had a disruptive impact on production in many countries. The latest additional disruption has been a shortage of coal in China leading to power cuts focused primarily on producers (rather than consumers), i.e. this will further aggravate shortages in meeting demand for goods. Many western countries are also hitting up against a difficulty in filling job vacancies. It is expected that these issues will be gradually sorted out, but they are currently contributing to a spike upwards in inflation and shortages of materials and goods available to purchase.

6. BORROWING STRATEGY

6.1 The capital investment plans provide details of the anticipated spending and non-treasury investment activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to facilitate this joint nature of activity. This will involve both the organisation of the cash flow and, where capital investment plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

6.2 In general, the Council will borrow for one of two purposes – to finance cash flow in the short-term or to fund capital investment over the longer term. The Council is currently maintaining an under-borrowed position, in that it is investing some of its own resources internally. This means that the underlying capital debt liability (primarily signified by the Capital Financing Requirement), has not been fully funded through external borrowing. This strategy is considered to be prudent, as investment returns are low, whilst counterparty risk is also limited under this approach.

6.3 The Council's treasury portfolio position at 31 March 2021, with forward projections is summarised below and detailed in table 3.4. The actual external borrowing (under treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement (CFR)), highlights an underlying need to borrow £273.372m in 2021/22, £368.437m in 2022/23, £240.967m in 2023/24 and £37.418m 2024/25. There is a large requirement in the early years. This is due to the impact of new capital investment schemes in the programme and the need to replace some existing short term loans which were taken to benefit from the then existing market conditions.

6.4 A key aim of the Treasury Management Strategy is to minimise the cost of the Council's external borrowing (portfolio), through seeking to spread the period for which loans are raised so as to avoid any undue fluctuation on interest costs arising from the future need to replace earlier amounts borrowed.

6.5 Currently the average rate of interest on the Council's loan portfolio is 1.91%, which is considered to be a beneficially low rate. The achievement of such low average rate demonstrates how the Council benefits from the best value for money in terms of its borrowing. This is the result of a number of years proactively managing the portfolio on loans through restructuring and taking advantage of the best possible interest rates available. The proposed treasury management strategy aims to continue this successful approach.

6.6 The approved sources of long-term and short-term borrowing will be:

- Public Works Loan Board
- UK Local Authorities
- Municipal Bond Agency
- Any institution approved for investments including high quality supranational banks
- European Banks Green Sustainable Bond Issuances
- World Wide Banks Green Sustainable Bond Issuances

- UK public and private sector pension funds
- Insurance companies
- UK Infrastructure Bank
- Any other financial institution approved by the Prudential Regulation Authority, which is part of the Bank of England and is responsible for the regulation and supervision of banks, building societies, credit unions, insurers and major investment firms
- Capital market bond investors either over the counter or through electronic trading platforms
- Community Municipal Bonds
- Local temporary
- Local Bonds
- Local authority bills
- Overdraft
- Negotiable Bonds
- Internal (capital receipts and revenue balances)
- Commercial Paper
- Medium Term Notes
- Finance leases

6.7 New financial institutions as a source of borrowing and / or types of borrowing – currently the PWLB Certainty Rate is set at gilts+ 80bps. However, consideration may still need to be given to sourcing funding from the follow:

- Local authorities - primarily shorter dated maturities out to 3 years or so – still 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 Bonds Agency – possibly still a viable alternative depending on market circumstances prevailing at the time.

The PWLB rate forecasts are given in the table below.

	PWLB Borrowing Rates			
	5 year	**10 year**	**25 year**	**50 year**
Dec-21	1.40%	1.60%	1.80%	1.50%
Mar-22	2.20%	2.30%	2.40%	2.20%
Jun-22	2.30%	2.40%	2.50%	2.30%
Sep-22	2.30%	2.40%	2.50%	2.30%
Dec-22	2.30%	2.40%	2.60%	2.40%
Mar-23	2.30%	2.40%	2.60%	2.40%
Jun-23	2.30%	2.40%	2.60%	2.40%
Sep-23	2.30%	2.40%	2.60%	2.40%
Dec-23	2.30%	2.40%	2.60%	2.40%
Mar-24	2.30%	2.40%	2.60%	2.40%
Jun-24	2.30%	2.40%	2.60%	2.40%
Sep-24	2.30%	2.40%	2.60%	2.40%
Dec-24	2.30%	2.40%	2.60%	2.40%

6.8 These forecasts are based around an expectation that there will normally be variations of +/-25bp during each quarter around these average forecasts in the normal economic and political circumstances. However, greater variations can occur should there be any unexpected shocks to financial and/or political systems.

6.9 The PWLB has a margin over gilt yields of 80 bps on loans lent to local authorities, consideration has been given to sourcing funding at cheaper rates. The Council will evaluate the option of borrowing further from the bond markets during 2022/23. Borrowing from the bond market will take place if it offers greater value for money than borrowing from the PWLB. The degree to which any option proves cheaper than PWLB Certainty Rate and the changes to criteria is still evolving at the time of writing and further updates will be provided.

6.10 Against this background and the risks within the economic forecast, caution will be adopted with the 2022/23 treasury operations. The Section 151 Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- If it was felt that there was a significant risk of a sharp fall in long and short term rates (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- If it was felt that there was a significant risk of a much sharper rise in long and short term rates than that currently forecast, perhaps arising from an acceleration in the 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 still lower than they are projected to be in the next few years.

6.11 There will remain a cost of carry to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost – the difference between borrowing costs and investment returns. The Council's policy for 2022/23 will be to balance investments to obtain returns within the Council's risk appetite. However, an assessment of the opportunity for borrowing will be made on the cost of borrowing long-term, within forward approved Capital Financing Requirement estimates, and will be consider carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

6.12 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 in respect of known needs, having regard to the Capital Strategy, after having regard also to the need to ensure value for money and the security of such funds.

6.13 All transactions will be reported to the Audit and Corporate Governance Committee at the next available opportunity.

7. DEBT RESCHEDULING

7.1 The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt (also a further a widening of the difference between new borrowing and repayment rates from October 2010 to 2019) has generally meant that PWLB to PWLB debt restructuring is now much less attractive than before these events. In particular, consideration would have to be given to the balance to be struck between premiums incurred and benefits arising from replacement borrowing. Interest savings may also be achievable through using other local authority loans and market loans in rescheduling exercises rather than using PWLB borrowing as the source of replacement financing.

7.2 As short-term borrowing rates are generally likely to be cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term to short term borrowing. However, such savings will need to be considered in the light of the current treasury position, the cost of loan repayment (premiums incurred), and potential future fluctuation in interest rates.

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

(a) The generation of cash savings and / or discounted cash flow savings;
(b) Help fulfil the borrowing strategy outlined above;
(c) Enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

7.4 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.

7.5 All rescheduling will be reported to the Audit and Corporate Governance Committee at the earliest meeting following this action.

7.6 It is possible that the Municipal Bond Agency will be offering loans to local authorities in the future. The Agency hopes that the borrowing rates will be lower than those offered by the Public Works Loan Board (PWLB). This Authority intends to make use of this new source of borrowing as and when appropriate.

8. TREASURY POLICY STATEMENT

8.1 Treasury management within this Council is undertaken having regard to the CIPFA Code of Practice for Treasury Management in the Public Services ("the TM Code"). This Code has been reviewed and updated following recent developments in the marketplace and the introduction of the Localism Act 2011 for English local authorities.

8.2 The Council has complied with the recommendations of the TM Code and has formally adopted the key recommendations as described within Section 4.

8.3 In accordance with the TM Code, the Council defines treasury management activities as:

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

8.4 'Investments' are described within the latest Investment Guidance as covering all of the financial assets of the organisation, as well as other non-financial assets which the organisation holds primarily or partially for financial returns, such as investment property portfolios. To the extent that this recommendation includes investments which are not managed as part of normal treasury management activity, the relevant Council Policy detail is contained within their Investment Strategy.

8.5 The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Further, the Council considers both financial risks, such as credit risk, as well as non-financial risks, such as climate risk. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

8.6 The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

8.7 The Council will create and maintain, as the cornerstone for effective treasury management:

- A Treasury Policy Statement, setting out the policies, objectives and approach to risk management of its treasury management activities
- Suitable Treasury Management Practices (TMPs) setting out the manner in which the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities (reported to the Audit & Corporate Governance Committee annually)
- Treasury Management Prudential Indicators as determined by the recommendations of the CIPFA Prudential Code;
- The content of the Policy Statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the TM Code, subject only to amendment where necessary to reflect the particular circumstances of this organisation. Such amendments will not result in the organisation materially deviating from the TM Code's key principles.
- The Council will receive reports on its treasury management policies, practices and activities, including as a minimum, an annual strategy and plan in advance of the year, an annual report after its close and an half year review report.
- The Council delegates responsibility for the implementation and monitoring of its treasury management policies and practices to the Audit & Corporate Governance Committee, and for the execution and administration of treasury management decisions to the Section 151 Officer, who will act in accordance with the Council's Treasury Management Strategy and having regard to the TM Code, who is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

2022/23 COUNCIL'S ANNUAL INVESTMENT STRATEGY

9. INTRODUCTION

9.1 The aim of the Council's Investment strategy is to:

- Maintain the principal amount of sums invested;
- Maintain policy flexibility.

9.2 The Council's Section 151 Officer, under delegated powers, will undertake the most appropriate form of investments made in reliance upon S.12, Local Government Act 2003 (LGA) depending on the prevailing interest rates at the time, and taking into account the risks shown in the forecast above.

9.3 The Council invests surplus cash balances only with certain approved organisations, as security of funds is of primary importance. All investments will be made in accordance with the Council's investment policies and prevailing legislation and regulations.

10. INVESTMENT POLICY – Management of Risk

10.1 The Department of Levelling Up, Housing and Communities (DLUHC – this was formerly the Ministry of Housing, Communities and Local Government (MHCLG)) and CIPFA have extended their recommendation regarding the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with treasury (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. The Council is mindful, however, that only those non-financial investments made in reliance upon S.12 are subject to the having regard to the Guidance. Certain non-financial investments that also provide ancillary investment returns can be carried out in reliance upon other powers where achievement of profit or financial return is not the primary motive.

10.2 When making a S.12 investment, the Council will have regard to:

- The requirements and extent of the statutory power
- Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the CIPFA TM Code")
- CIPFA Treasury Management Guidance Notes 2018.

10.3 The Council's investment priorities are:

(a) The security of the principal amounts invested
(b) The liquidity of its "specified" treasury management investments (funds, reserves and cash balances)
(c) Yield
(d) Social Impact
(e) ESG Impact (covering environmental, social and governance)

10.4 The Council will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity and in line with the Council's risk appetite. In the current economic climate it is considered appropriate in general to keep treasury management investments short term to cover cash flow needs. However, where appropriate (from an internal as well as external perspective), the Council will also consider the value available in longer periods with high credit rated financial institutions, as well as wider range fund options.

10.5 The Council has reviewed its classification with financial institutions under Market in Financial Instruments Directive (MIFID II). A schedule has been included with the Treasury Management Practices document of those organisations with which it is registered as a professional client and those with which it has an application outstanding to register as a professional client.

10.6 In accordance with guidance from DLUHC and CIPFA, which places a high priority on the management of risk, the Council has stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list, which also enable diversification and thus avoidance of concentration risk.

10.7 Furthermore, the Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that 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 this end the Council will engage with its advisors to maintain and monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings. This is integrated into the credit methodology provided by the advisors, Link Asset Services in producing its colour coding which show the varying degrees of suggested creditworthiness.

10.8 The Council's officers also recognise that there are other risks of material importance to the treasury portfolio from an environmental, social and governance perspective. It is important, therefore, to assess these risks as well and to understand if these create potential longer-term financial and reputational risks for the Council, and if there are any commonalities with the Council's key objectives in this regard. To this end, the Council will use information sources and its advisors as appropriate to assist it in scrutinising and understanding if these might affect the suitability of potential counterparties.

10.9 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.

10.10 The aim of the strategy is to generate a list of highly creditworthy counterparties, which will also enable diversification and thus avoidance of concentration risk. The intention of the strategy is to provide security of investment, minimisation of all risks and alignment where possible with the Council's policy objectives.

10.11 Investment instruments identified for use in the financial year are listed below under the 'Specified' and 'Non-Specified' investments categories. Counterparty limits will be as set through the Council's Treasury Management Practices Statement.

11. SPECIFIED INVESTMENTS (MATURITIES UP TO ONE YEAR) AND COUNTERPARTY LIMITS

11.1 All such investments will be sterling denominated, with maturities up to maximum of 1 year, meeting the minimum 'high' rating criteria where applicable. The maximum limit will be applied to each account (i.e. bank, local authority, bond, etc.)

1. Specified Investments (limit per counterparty)	**Maximum Group Limit**
UK Government	Unlimited
Local Authorities	Unlimited
Money Market Funds CNAV	£75.0m
Money Market Funds LVNAV	£75.0m
Money Market Funds VNAV	£75.0m
Pooled Fund Institution with a min rating of AAA/A1	£75.0m
Institutions with a minimum rating of AAA/A1	£75.0m
Institutions with a minimum rating of AA-/A2	£30.0m
Institutions with a minimum rating of A-/A3	£20.0m
Institutions with a minimum rating of BBB/A3	£15.0m
Building Societies – assets greater than £5,000 million	£5.0m

Building Societies – assets greater than £1,000 million	£2.5m
Building Societies – assets greater than £ 250 million	£1.0m

All investments with maturities up to maximum 1 year, high credit criteria:			
	Minimum 'High' Credit Criteria	**Maximum Limit**	**Maximum Maturity Period**
Debt Management Agency Deposit Facility	UK sovereign rating	£50m	1 year
Term deposits – local authorities and other public institutions	UK sovereign rating	£20m	1 year
Term deposits – banks and building societies*	UK sovereign rating	£20m	1 year

11.2 Term deposits with nationalised banks, banks and building societies

	Minimum 'High' Credit Criteria	**Maximum Limit**	**Maximum Maturity Period**
UK part nationalised banks	UK sovereign rating	£20m	1 year
Banks part nationalised by high credit rated (sovereign rating) countries	Sovereign rating A	£20m	1 year

*The countries approved for investing with their banks: Australia, Canada, Denmark, Germany, Luxembourg, Netherlands, Norway, Singapore, Sweden, Switzerland, Finland, USA, Abu Dhabi (UAE), Hong Kong, France, UK, Belgium, and Qatar.

11.3 Other instruments

	Minimum 'High' Credit Criteria	**Max Individual Investment**	**Maximum Total Investment**	**Max Maturity Period**
Collateralised deposit	UK sovereign rating	£5m	£5m	1 year
Certificates of deposits issued by banks and building societies	UK sovereign rating	£5m	£20m	1 year
UK Government Gilts	UK sovereign rating	£10m	£50m	1 year
Bonds issued by multilateral development banks	Long term AA	£10m	£20m	1 year
Treasury Bills	UK sovereign rating	£5m	£20m	1 year
Government Liquidity Funds	Long term AA	£10m		1 year
Money Market Funds	Variable CNAV Long Term AAA	£50m per fund		1 year
Money Market Funds	Stable LNNAV Long Term AAA	£50m per fund		1 year
Money Market Funds	Stable VNAV Long Term AAA	£20m per fund		1 year
Enhanced Cash Funds	Long Term AA	£5m		1 year
Gilt Funds	Long Term AA	£5m		1 year
Bond Funds	Internal and External Due Diligence	£10m per fund		1 year / rolling
Managed Account Bond Funds	Internal and External Due Diligence	£30m per fund		1 year / rolling

12. NON-SPECIFIED INVESTMENTS (MATURITIES OVER ONE YEAR)

12.1 These are any investments which do not meet the specified investment criteria. The investments may be for periods in excess of one year, and/or more complex instruments which require greater consideration before being authorised. Non-financial investments are also likely to fall within this category, such as loans made solely the purpose of financial gain, or acquisitions of commercial property where the achievement of profit represents the primary purpose. Separate detailed consideration is given by the Council in respect of every proposal which represents these activities. Whilst these activities carried out solely for profit must necessarily rely upon the S.12 investment power, they may also have the effect of causing the Council's aggregate outstanding amount of borrowing to increase. The Investment Guidance recommends that where this is the case, appropriate quantitative indicators should be established which will allow Councillors and the general public to assess the risks and opportunities over both its payback period and period of borrowing taken out, these will be covered in the Council's Capital Strategy.

12.2 A maximum of 95% may be held in aggregate in non-specified investments. A variety of investment instruments will be used both debt and equity subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the above categories. The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

Term deposits with nationalised banks and building societies:			
	Minimum 'High' Credit Criteria	**Maximum Limit**	**Maximum Maturity Period**
UK part nationalised banks	UK sovereign rating	£20m	5 year
Banks part nationalised by high credit rated (sovereign rating) countries UK and non UK*	Sovereign rating A	£20m	5 year

12.3 Maturities of any period:

	Minimum 'High' Credit Criteria	**Maximum Individual Investment**	**Maximum Group Limit**	**Maximum Maturity Period**
Structured deposits	In accordance with Link's Credit Worthiness Criteria	£5m	£20m	5 years
Banks and Building Societies term deposits with unrated counterparties : any maturity	The top twenty building societies by total assets with a minimum asset size of £1bn and the following credit rating Fitch (or its equivalent):			
	Long term rating AA-, short term rating F2	£1m	£5m	5 years
	Non rated	£0.5m	£1m	1 year
Challenger Banks term deposits with unrated counterparties : any maturity	The non-rated bank must have a minimum asset level of £200m,	£5m	£5m	1 year
Municipal Bonds	UK sovereign rating	£10m	£10m	5 years
Commercial paper	Short-term F2, Long term A	£5m	£5m	5 years
Corporate Bonds Corporate Bond Funds / Gilt Funds	Short-term F2, Long term A	£20m	£20m	5 years
Floating Rate Notes	Long term A	£1m	£5m	5 years
Covered Bonds	Long term AA-	£10m	£10m	5 years
Un-rated bonds	Long term	£10m	£10m	5 years
Churches, Charities and Local Authorities (CCLA) Property Fund	Internal and External Due Diligence	£20m	£20m	1 year rolling

12.4 Maturities in excess of 1 year

	Minimum 'High' Credit Criteria	**Maximum Individual Limit**	**Maximum Group Limit**	**Maximum Maturity Period**
Term deposits – local authorities and other public institutions	UK sovereign rating	£20m	£20m	5 years
Term deposits – banks and building societies	Long term rating AA-, short term rating F2	£1m	£5m	5 years
Certificates of deposits issued by banks and building societies	UK sovereign rating	£5m	£20m	5 years
UK Government Gilts	UK sovereign rating	£5m	£50m	5 years
Bonds issued by multilateral development banks	AA	£5m	£20m	5 years
Green Energy Bonds	Internal and External Due Diligence	£10m	£10m	5 years
Carbon Off-set Funds	Internal and External Due Diligence	£1m	£1m	3 years
Collateralised Term Deposit	Local Authority	£5m	£20m	5 years
Sovereign bond issues (i.e. other than the UK government)	AA	£5m	£20m	5 years
Property Bonds	External Due Diligence	£20m	£20m	5 years
Property Pooled Funds	External Due Diligence	£50m	£75m	5 Years
Live Wire Community Energy	Internal Due Diligence	£1m	£1m	5 years rolling
Asset Backed Securities	Internal and External Due Diligence	£10m	£10m	5 years
Asset Backed Pooled Funds	Internal and External Due Diligence	£50m	£75m	5 years

Forest Financial Instrument	Internal and External Due Diligence	£10m	£10m	5 years
Special Purpose Acquisition Company Funds (SPAC)	Internal and External Due Diligence	£1m	£1m	2 years
Public Sector Social Impact Fund	Unrated	£30m	£30m	5 years rolling
Real Estate Investment Trusts (REITS)	Internal & External Due Diligence	£20m	£20m	5 years rolling
Bank Tier 2 Capital Both upper & lower levels	Rated & unrated Internal and External Due Diligence	£10m	£10m	10 years

12.5 As a result of the change in accounting standards for 2022/23 under IFRS 9, the Council will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. In November 2018, the MHCLG concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years commencing from 1.4.18, ending 31.3.23.

12.6 The IFRS 9 provisions are unlikely to apply to any of the Council's non-financial investments where these are separately treated as capital expenditure or for other reasons do not fall within the definition of a financial instrument. Items of capital expenditure are not considered to satisfy the asset/liability criteria that is required in order for a financial instrument to be subject to IFRS9.

12.7 **OTHER TYPES OF NON-SPECIFIED INVESTMENTS**

- Fixed term deposits with variable rate and variable maturities
- Limited Liability Partnerships
- Limited Partnerships
- Loans made for solely financial gain
- Commercial property acquisitions

12.8 **INVESTMENTS TARGETING HIGHER RETURNS**

The Council, over the last few years due to uncertainty in the world financial markets and the low returns on offer from traditional instruments and inflation eroding these returns together with a desire to invest in Environmental Social and Governance Investments (ESG), has successfully been investing in secured diversified higher yield investments. This policy will be continued into 2022/2023.

12.9 Without this allocation the weighted average return of the Council's cash investments based on investments held at 31 December 2021 would have been 0.02%; whereas the

allocation to higher yielding investments has a weighted average return of bringing the overall average return for the portfolio to 3.63%.

12.10 The latest estimated value of investment income is circa £6m for 2021/22. However, as these balances and returns do not remain constant over the course of a year the figures are indicative, and the actual returns will form part of the outturn report at the conclusion of the financial year.

12.11 Higher yields can be accessed through medium-term cash investments (although this is currently less the case as yields have declined) and investments in other assets than cash, such as pooled property, equities and bonds. Non-cash pooled investments must be viewed as medium-term investments in order that monies are not withdrawn in the event of a fall in capital values to avoid crystallising a capital loss.

12.12 Bond, equity and property funds offer enhanced returns. These allow the Council to diversify into asset classes other than cash without the need to manage the underlying investments. Depending on the type of pooled fund invested in, it may have to be classified as capital expenditure.

12.13 When the Council began to specifically target higher returns from a proportion of its investments, it also established a Commercial Risk Reserve. The reserve has never been called upon with regards to treasury investments because no treasury management losses have ever occurred.

12.14 Going forward, however, changes to IFRSs mean that capital gains and losses on investments which represent financial instruments need to be reflected in the revenue account on an annual basis. There is currently a statutory override in place for local authorities that exempts them from complying with this requirement for the next year. The Council also has more limited levels of non-treasury management activity involving this nature of transaction. However, given the greater future risk in this area it is proposed to continue to contribute towards the Commercial Risk Reserve on an on-going basis. The amount contributed each year will be determined by the Section 151 Officer when the Outturn is known each year.

13 CREDITWORTHINESS POLICY

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

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

13.2 This modelling approach combines credit Ratings, credit Watches and credit Outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments on some occasions.

13.3 The selection of counterparties with a high level of creditworthiness will be achieved by selection of institutions down to a minimum durational band within Link Asset Services weekly credit list of worldwide potential counterparties. The Council will therefore use counterparties within the following durational bands:

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

**The yellow colour category is for UK Government debt, or its equivalent, money market funds and collateralised deposits where the collateral is UK Government debt.*

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

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

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

- If a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately;
- In addition to the use of Credit Ratings the Council will be advised of information in movements in Credit Default Swap (CDS) against the iTraxx (CDS product brand name) benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Councils lending list.

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

13.8 **Creditworthiness** – significant levels of downgrades to short and long term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. However, as economies are beginning to reopen, there have been some instances of previous lowering of Outlooks being reversed.

13.9 **CDS prices** – although bank CDS prices (these are market indicators of credit risk) spiked upwards at the end of March / early April 2020 due to the heightened market uncertainty and ensuing liquidity crisis that affected financial markets, they have returned to more average levels since then. However, sentiment can easily shift, so it will remain important to undertake continual monitoring of all aspects of risk and return in the current circumstances. Link monitor CDS prices as part of their creditworthiness service to local authorities and the Council has access to this information.

14. COUNTRY LIMITS

14.1 The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide them). The list will be added to, or deducted from by officers should ratings change in accordance with this policy.

15. INVESTMENT CRITERIA

15.1 Prudence will drive the Council's approach to its treasury management investments in 2022/23 due to the volatility and uncertainty that exists in the world's financial markets. It is anticipated that these investments will generally be of a short-term nature, which may be represented by a combination of short-term loans and internal borrowing (i.e. use of the Councils own balances and reserves until required for an approved purpose). In order to minimise risk, the Council will look to diversify its investment portfolio by investing in other longer term investment vehicles such as money market funds, ESG investments and property funds. The driving force of the Council's strategy in this respect will be maintaining the security of capital (principal amount invested) and maintaining appropriate liquidity. The Council will use a combination of credit ratings, sovereign ratings, internal and external due diligence and guarantees to assess the credit quality of financial institutions before placing investments.

16. INTEREST RATE OUTLOOK

16.1 It is considered by the Council's treasury advisors that the present low level of Bank Rate will increase in May 2022 or February. This will have implications for all types of interest returns available from treasury investments.

16.2 The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are detailed below (the long-term forecast is for periods over 10 years in the future):

Average earning in each year	Now	Previously
2022/23	1.00%	0.50%
2023/24	1.25%	0.75%
2024/25	1.25%	1.00%
2025/26	1.25%	1.25%
Years 6 to 10	1.50%	-
Years 10+	2.00%	2.00%

16.3 A money market fund (MMF) is a fund that invests in highly liquid, near term instruments that offer high liquidity with a very low level of risk. The MMF's yields have continued to drift lower. Some managers have already resorted to trimming fee levels to ensure that net yields for investors remain in positive territory where possible and practical. Investor cash flow uncertainty, and the need to maintain liquidity in these unprecedented times, has meant there is a surfeit of money swilling around at the very short end of the market. This has seen a number of market operators, now including the Debt Management Account Deposit Facility (DMADF), offer nil or negative rates for very short term maturities. This is not universal, and MMFs are still offering a marginally positive return, as are a number of financial institutions for investments at the very short end of the yield curve.

16.4 Inter-local authority lending and borrowing rates have also declined due to the surge in the levels of cash seeking a short-term home at a time when many local authorities are probably having difficulties over accurately forecasting when disbursements of funds received will occur or when further large receipts will be received from the Government.

16.5 For 2022/23 the Council will budget for an investment return of 0.25% on investments placed during the financial year.

17. LIQUIDITY OF INVESTMENTS

17.1 The maximum period of investment of treasury balances will be ten years.

17.2 There will be no more than £10m of core treasury funds committed for a period over 5 years.

18. FINANCIAL DERIVATIVES

18.1 Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The GPOC arising from Section 1 of the *Localism Act 2011* May have removed some uncertainty as to whether, and to what extent, local authorities are able to enter into "stand-alone" forms of derivative contract (i.e. those that are not embedded into a loan or investment). Should any such opportunity arise, the individual conditions/circumstances would be subjected to approve consideration processes.

18.2 The Council will as a general rule only consider standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Authority is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

18.3 In line with the CIPFA Code, the Council will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.

19. ENVIRONMENTAL SOCIAL & GOVERNANCE (ESG) POLICY

19.1 The Council is committed to being a responsible investor at all times. Responsible investment means to recognise the importance of the long-term health and stability of the financial markets, and to understand that this depends on key external non-financial factors, such as the environment, social stability and strong governance. Collectively, these factors are often referred to under the umbrella of ESG (Environmental, Social and Governance).

19.2 The Council's objective is to recognise all these risks, to mitigate them where possible and thereby improve the security of its portfolio in the long-term.

19.3 Within these risks, the Council has identified climate change as a long-term, material and systemic financial risk with the potential to significantly impact the treasury portfolio and the Council's financial resilience over time. Therefore, the Council seeks to:

- Minimise exposure to counterparties and investments heavily impacted by climate change risk
- Increase exposure to sectors, counterparties and investments, such as renewables, whose activities aid the transition to a lower carbon world and economy.
- Contribute meaningfully to an improved economically sustainable future locally and nationally, without sacrificing security.

19.4 This is not to downplay other non-financial risks. The Council sees positive social impact also as a key mitigate to aid long-term financial stability, and as a meaningful contribution to the local, regional and national economy. Good governance meanwhile is also critical to safeguarding the Council's reputational risk.

19.5 The Council's core ESG principles are set out below in full:

- The Council recognises the potential impact of its counterparties and investments on the environment, workers, communities and society, as well as the potential impact of

climate change on the counterparties, businesses into which the Council invests, the Council itself and its local economy and community.

- The Council will, and seek to ensure where possible its investment counterparties will, act responsibly with respect to the environment, aiming for a sustainable approach to the use of resources, avoiding irresponsible disposal of hazardous products and unnecessary waste.
- The Council and its counterparties will be non-discriminatory (whether on grounds of gender, race or disability), and adopt equality and diversity in their employment practices
- The Council seeks to ensure it and its counterparties always respect human rights and ensure no exploitation of child labour.
- The Council and its counterparties will seek to act with integrity at all times in their dealings.
- The Council will seek to encourage positive ESG behaviour, engaging with counterparties and investments where appropriate to encourage best practice and drive change.
- The Council will comply with any industry standard ESG guidelines that may arise and otherwise, always seek to ensure best practices, actively managing ESG considerations and risks alongside its financial considerations and risks.

19.6 The Council will incorporate ESG issues into its analysis and decision making processes when considering the treasury portfolio and investments. The Council will seek to use data and analysis to determine the type and materiality of relevant issues for counterparties, and their alignment with the Council's core principles.

19.7 It is important to note that the Council shall invest on the collective basis of its investment priorities – Security, Liquidity, Yield and ESG impact – having considered all factors contributing to the risk of its counterparties and investments, including ESG factors to the extent these indirectly or directly impact on financial risk and return as well as the Council's broader policy objectives.

19.8 The Council will also seek to report progress, providing transparency on the ESG profile and impact of its portfolio investments. These will be through supporting investments and counterparties aligned with the Council's objectives, reviewing the ESG policies of funds and counterparties where appropriate, and the sourcing of suitable metrics where relevant such as for example, social impact metrics, external ratings and quantifying the investments in assets and businesses contributing to climate change reduction.

20. POLICY ON THE USE OF EXTERNAL SERVICE PROVIDERS

20.1 The Council uses Link Asset Services (previously named Capita Asset Services) as its external treasury management advisers. The Council tendered for the service in 2019 for a three year period.

20.2 The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our

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

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

20.4 The Council fully appreciates the importance of monitoring the activity and resultant performance of its appointed external fund manager. The Council's external fund managers will comply with the Annual Investment Strategy. In order to aid this assessment, the Council is provided with a suite of regular reporting from its manager. This includes quarterly/semi-annual and annual reports, statements, access to online fund reporting sites, etc.

20.5 In addition to formal reports, the Treasury Management Risk Officer Group (TMRG) meets with representatives of the fund manager on TMRG (semi-annual) basis. These meetings allow for additional scrutiny of the manager's activity as well as discussions on the outlook for the fund as well as wider markets.

20.6 Markets in Financial Instruments Directive – the Council has opted up to professional client status with its providers of financial services, including advisers, brokers, and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Section 151 Officer believes this to be the most appropriate status.

21. TREASURY MANAGEMENT SCHEME OF DELEGATION

21.1 The scheme of delegation is in the Council's Treasury Management Practices statement which will be reported to the Audit and Corporate Governance Committee on an annual basis. The Council for 2022/23 hope to report this in the autumn of 2022 because currently the CIPFA Guidance notes on new Code elements have not been published.

21.2 The Council considers it essential, for the purposes of the effective control and monitoring of its Treasury Management activities, the reduction of the risk of fraud or error, and for the pursuit of optimum performance, that these activities are structured and managed in a fully integrated manner, and that the responsibilities of Treasury Management is always clear.

21.3 **Full Council**

- Receiving and reviewing reports on treasury management policies, practices and activities
- approval of annual treasury management and investment strategies
- approval of the Mid-Year Review Report of Treasury Management

- approval of capital strategy
- monitoring of yearly Treasury Outturn Report

21.4 **Audit and Corporate Governance Committee**

- the body appointed by Council for the scrutiny of Treasury Management
- recommend the Council's Annual Treasury Management Strategy to Council
- approval of/amendments to the organisation's adopted clauses, treasury management policy and treasury management practices to Council
- receiving and reviewing regular monitoring reports and acting on recommendations
- recommending the yearly Mid-Year Review and Treasury Outturn Report to Council

21.5 **Section 151 Officer**

The Section 151 Officer (Deputy Chief Executive & Director of Corporate Services) and in their absence their appointed deputies is the delegated responsible officer by Full Council for the operation of the Council's overall borrowing and investment activities. The Section 151 Officer will implement and monitor the Treasury Management Strategy and make recommendations to the responsible body. The role of the Section 151 Officer (as detailed in the 2017 Treasury Management Code) includes:

- Recommending clauses, treasury management policy/practices for approval, reviewing the same regularly and monitoring compliance
- Submitting regular treasury management policy reports
- Submitting budgets and budget variations
- Receiving and reviewing management information reports
- Reviewing the performance of the treasury management function
- Ensuring the adequacy of treasury management function
- Ensuring the adequacy of treasury management resources and skills and the effective division of responsibilities within the treasury management function
- Ensuring the adequacy of internal audit and liaising with external audit
- Recommending the appointment of external service providers.
- 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
- 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
- Ensuring that the authority has appropriate legal powers to undertake expenditure on non-financial assets and the 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

- Ensuring that the authority has adequate expertise, whether in house or externally provided, to carry out the above
- Creation of Treasury Management Practices which specifically deal with how non-treasury investments will be carried out and managed, to include the following:
  - Risk management, including investment and risk management criteria for any material non-treasury investment portfolios
  - Performance measurement and management, including methodology and criteria for assessing the performance and success of non-treasury investments
  - Decision making, governance and organisation, including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate profession due diligence is carried out to support decision making
  - Reporting and management information, including where and how often monitoring reports are taken
  - Training and qualifications, including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.

MINIMUM REVENUE PROVISION (MRP) STRATEGY

22.1 The Council is required to make a minimum revenue provision (MRP) to a revenue account for each financial year. An earlier statutory provision contained within Regulation 28 of the 2003 Capital Finance and Accounting Regulations was replaced in 2008 by a requirement for the Council to calculate an amount of MRP each year which they consider to be prudent. In order to arrive at an annual prudent provision, the Council is required to have regard to statutory Guidance.

22.2 The statutory change in the method for assessing a prudent provision reflected in general an intention to vary the earlier annual 4% charge in respect of outstanding capital debt liability to an annual charge, assessed in equal instalments, which spread future debt liability over a period bearing some relation to that which an “associated” asset is anticipated to provide a service benefit for the Council (the asset life method).

22.3 The amount of capital debt liability that was outstanding at the time the statutory change was introduced was not subject to this revised beneficial life consideration. The MRP Guidance provided that this historic liability could either continue in accordance with the previous statutory method of assessment (referred to in the Guidance as Option 1), or be subject to local variation. The Council has approved a local variation which will result in this proportion of outstanding debt liability being charged more prudently by way of equal annual provision over a 50-year period, subject to an annual useful life assessment.

22.4 The Guidance suggests four options for charging amounts of outstanding capital debt liability:

- Option 1: Regulatory method – MRP is equal to the amount determined in accordance with the former Regulations 28 and 29 of the 2003 Regulations.
- Option 2: CFR method – MRP is equal to 4% of the non-housing CFR at the end of the preceding financial year.

- Option 3: Asset Life Method – MRP is to be determined by reference to the useful life of the asset.
- Option 4: Depreciation method – MRP is deemed to be equal to the provision required in accordance with deprecation accounting in respect of the asset on which expenditure has been financed by borrowing or credit arrangements.

22.5 As indicated, the Council has adopted a local determined option in respect of the historical element of debt liability. For most of its future capital debt liability arising from capital expenditure, the Council has determined to adopt Option 3. This reflects the asset "useful-life" approach. The Council may separately determine different approaches should this be considered appropriate, such as in the case of loans treated as capital expenditure, and certain larger schemes or transactions which warrant a more locally determined prudent approach.

22.6 The determination of which expenditure should be charged under Option 3, and the life periods considered to be applicable to these, will in general be carried out under delegated powers by the Section 151 Officer. Any variation from Guidance suggestions will be specifically considered and agreed by full Council.

22.7 A prudent provision will not be considered for new amounts of debt liability until the year following that in which the scheme or asset giving rise to the debt liability has commenced. Any deviation from this will be incorporated into the MRP Strategy.

22.8 Items of capital debt liability will only be considered for division into separate amount(s) in cases where two or more major components have substantially different useful economic lives. Assets will not be transferred into the asset register and fixed assets account until their anticipated service benefit objectives are achieved, in accordance with proper practices.

22.9 In the case of long-term debtors arising from loans or other similar types of transaction treated as capital expenditure which give rise to a capital debt liability, the Council has determined that, in general, it will reflect a prudent approach if no amount of MRP is charged where there is reasonable or actual expectation of principal repayment(s) being made either during the currency of the maximum loan period (e.g. through tranches of principal repayment) or where the maturity date offers sufficient expectation of full principal repayment within a reasonable period. MRP for loans will be equated to the principal repayment profile of the loans.

22.10 In approving this approach, and associated departure from Guidance recommendation, the Council has had regard to the fact that such loans have similar characteristics to any other loans made for treasury management purposes, whereby careful consideration is first given to security and avoidance of risk. Also, the Council recognised that the making of a prudent provision which has no regard to the likelihood of repayment would result in an unnecessary charge having been made to revenue during the intervening period once the loan is fully repaid.

22.11 The nature of security and likelihood of repayment of principal under the agreed loan terms for each individual loan will however be kept under review during its currency so that appropriate alternative approaches may be considered, either in respect of the introduction of a prudent provision, or through application of specific reserves established and set aside in a manner equivalent to an alternative MRP being made to guard against any such possibility. This form of regular reappraisal of the likelihood of loan principal repayment is considered necessary as the similar provisions that apply under IFRS9 are not apply in the case of loans treated as capital expenditure.

22.12 The Council acknowledge and agree this approach represents a departure from that suggested within the MRP Guidance, which assumes an equal annual charge spread over the life period that reflects the useful asset life of the third party which can be linked with the purpose for which the loan was granted. In general, the Council considers it unlikely that there could be any reasonable correlation between loan periods and underlying asset life periods, and that it is more prudent to determine that the principal element of loans, when repaid, should be used to write-down the debt liability that relates to the loan.

22.13 The Council has adopted a similar type of policy that will apply in the case of the Golden Square Shopping Centre. Instead of relying solely upon principal element of repayments to satisfy the MRP liability, the annual MRP charge that will be made will equate to the principal amount that has been assessed by the Council's advisers, Price Waterhouse Coopers, to be included each year within the repayments received by the Authority under the lease. Rather than resulting in a fixed annual MRP charge over the period of the lease, the nominal amount of MRP charge each year will be regarded as met by the element of the lease rental which serves to write down the outstanding long term debtor created as a consequence of the lease having been granted. The deferred capital receipt created under this arrangement will be earmarked on a yearly basis to pay off the debt liability over 200 years and will equate to the MRP charge. This approach mirrors that which is recommended within paragraph 20 of the MRP Guidance with regard to leases where the authority is a lessee.

22.14 Other finance leases and Private Finance Initiative (PFI) assets will have their MRP liability determined according to the life of the financial instrument, acting as a proxy for asset life, or in accordance with the useful life of the asset to which the PFI arrangement relates, should this be considered more appropriate to prudent provision principles. MRP on these instruments may separately be considered under IFRS accounting principles where these do not conflict with capitalisation and statutory principles. This approach is in accordance with Guidance principles.

22.15 The Council, if it considers it prudent for a particular financial year, will set aside capital receipts, either to reduce outstanding aggregate capital debt liability (such as in the case of loan principal repayments), or to reduce the aggregate level of outstanding capital debt liability by an amount up to the level of reduction that would otherwise arise from setting aside an annual amount of MRP. In such circumstances, the Council will be acknowledging that present taxpayers are most likely to have contributed to the cost of assets disposed of that are giving rise to the capital receipt, thereby allowing associated benefit to flow back to them more immediately. The present manner in which annual amounts of MRP must

be assessed does not otherwise provide for any proportion of the benefit arising from present capital receipts to be passed back to these more historic taxpayers.

22.16 After taking account of current circumstances facing them for each financial year, the Council may also, when determining an annual amount of MRP, have regard to earlier amounts of capital receipts that have been used voluntarily to reduce what would otherwise have been an ongoing amount of capital debt liability. The principle of having regard to the achievement of an earlier reduction in what would otherwise have been an ongoing level of outstanding capital debt liability has always been a recognised form of adjustment recognised by Guidance.

22.17 The Council may also consider the exercise of this option in cases where similar debt liability relief has been achieved through the voluntary use of revenue monies to finance capital expenditure. In either case where current circumstances warrant such consideration, the Council will also take account of the amount of earlier MRP that would have needed to be charged had the earlier voluntary set aside of capital receipts or revenue contributions not occurred when determining the appropriate amount of adjustment that may appropriately be made to a current year's prudent provision.

22.18 In each of these cases, any such determination by the Council will have regard to any unforeseeable changes in financial circumstance that have arisen since the earlier decisions were taken, after having regard also to what is considered to represent the most prudent outcome for both the Council and the interests of its taxpayers.

22.19 For those types of capital expenditure incurred by the Council which are not capable of being related to an individual asset (e.g. revenue expenditures treated as capital expenditure), asset lives will be assessed on a basis which 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 which 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.

22.20 Certain loans or other forms of what are termed non-financial investments made primarily for profit will necessarily be made in reliance upon the S.12 investment power. These loans do not represent capital expenditure. They will not therefore be subject to MRP. However, for reasons of prudence, any such loans are subject to separate consideration under the Council's Investment Strategy in respect of non-specified investments, and also statutory Investment Guidance.

22.21 This MRP policy will be reviewed on an annual basis. If it is proposed to vary the terms of the agreed Policy Statement during any year, a revised statement will be submitted to the Audit and Corporate Governance Committee for consideration at that time.

22.22 **Redwood Bank** - The Council has also noted that the likely life period of their equity holding in Redwood Bank will be considerably longer than might apply to more common forms of share capital acquisitions, which are likely to be more representative of investments rather than assets that provide an economic regeneration. For this reason the Council has

determined it will depart from the wording of the Guidance, which suggests a 20-year life period, and agreed that it would be prudent to determine a 50-year life period for this asset in recognition of the anticipated benefit period. The Council will thus charge MRP on the asset over 45 years to reflect the previous 5 year MRP holiday the Council have previously taken.

22.23 **Commercial Property Investment Programme** - The Council will make a voluntary MRP charge using the Annuity method which is recommended by Guidance.

22.24 **Time Square** - the nature of more locally determined approach will also be determined in the case of Time Square Town Centre redevelopment scheme. Whilst actual development works have now been completed, many of the associated occupation and income earning provisions taken into account when approving the scheme will not be received for a number of years, caused to a significant extent by the Covid restrictions. Accordingly, a prudent MRP will not be determined until the year after the envisaged service and income benefits are received, again in line with proper practice principles. It is envisaged that this could be up to 5 years after the initial year of MRP that might otherwise have been made following completion of development works. The period of MRP deferment will however be kept under regular review.

22.25 **Together Energy** -. The Council's equity stake in Together Energy will pay MRP over a 20 year period per Guidance. Together Energy entered administration in early 2022. The future of this payment is not yet known until the administration process is complete.

ANNEXE A

GLOSSARY OF TERMS

ABL	Affordable Borrowing Limit
Basis Point (BP)	1/100th of 1%, i.e. 0.01% (or 0.0001 decimal form)
Base Rate	Minimum lending rate of a bank or financial institution in the UK
Benchmark	A measure against which the investment policy or performance of a fund manager can be compared.
Bill of Exchange	A financial instrument financing trade.
Callable Deposit	A deposit placed with a bank or building society at a set rate for a set amount of time. However, the borrower has the right to repay the funds on pre agreed dates, before maturity. This decision is based on how market rates have moved since the deal was agreed. If rates have fallen the likelihood of the deposit being repaid rises, as cheaper money can be found by the borrower.
Cash Fund Management	Fund management is the management of an investment portfolio of cash on behalf of a private client or an institution, the receipts and distribution of dividends and interest, and all other administrative work in connection with the portfolio.
Certificate of Deposit (CD)	Evidence of a deposit with a specified bank or building society repayable on a fixed date. They are negotiable instruments and have a secondary market; therefore the holder of a CD is able to sell it to a third party before the maturity of the CD.
Commercial Paper	Short-term obligations with maturities ranging from 2 to 270 days issued by banks, corporations and other borrowers. Such instruments are unsecured and usually discounted, although some may be interest bearing.
Constant Net Asset Value (CNAV)	Constant Net Asset Value refers to funds which use amortised cost accounting to value all of their assets. They aim to maintain a Net Asset Value (NAV), or value of a share of the fund, at £1 and calculate their price to 2 decimal places.
Corporate Bond	Strictly speaking, corporate bonds are those issued by companies. However, the term is used to cover all bonds other than those issued by governments in their own currencies and includes issues by companies, supranational organisations and government agencies.
Counterparty	Another (or the other) party to an agreement or other market contract (e.g. lender/borrower/writer of a swap/etc.)
CDS	Credit Default Swap – a swap designed to transfer the credit exposure of fixed income products between parties. The buyer of a credit swap receives credit protection, whereas the seller of the swap guarantees the credit worthiness of the product. By doing this, the risk of default is transferred from the holder of the fixed income security to the seller of the swap.
CFR	Capital Financing Requirement
CIPFA	Chartered Institute of Public Finance and Accountancy
CLG	Department for Communities and Local Government
CPI	Consumer Price Index – calculated by collecting and comparing prices of a set basket of goods and services as bought by a typical consumer, at

	regular intervals over time. The CPI covers some items that are not in the RPI, such as unit trust and stockbrokers fees, university accommodation fees and foreign students' university tuition fees.
Derivative	A contract whose value is based on the performance of an underlying financial asset, index or other investment, e.g. an option is a derivative because its value changes in relation to the performance of an underlying stock.
DLUHC	Department for Levelling Up Housing and Communities
DMADF	Deposit Account offered by the Debt Management Office, guaranteed by the UK government.
ECB	European Central Bank – sets the central interest rates in the EMU area. The ECB determines the targets itself for its interest rate setting policy; this is to keep inflation within a band of 0 to 2%. It does not accept that monetary policy is to be used to manage fluctuations in unemployment and growth caused by the business cycle.
EIA	Equality Impact Assessment
EMU	European Monetary Union
Equity	A share in a company with limited liability. It generally enables the holder to share in the profitability of the company through dividend payments and capital gain.
EU	European Union
Fed.	Federal Reserve Bank of America – sets the central rates in the USA
Floating Rate Notes (FRN)	Bonds on which the rate of interest is established periodically with reference to short-term interest rates
Forward Deal	The act of agreeing today to deposit funds with an institution for an agreed time limit, on an agreed future date, at an agreed rate.
Forward Deposits	Same as forward dealing (above).
FCA	Financial Conduct Authority – one of the main UK regulatory bodies with three main objectives – to protect consumers, to protect and enhance the integrity of financial markets and to promote effective competition.
Fiscal Policy	The Government policy on taxation and welfare payments.
GDP	Gross Domestic Product
GF	General Fund
Gilt	Registered British government securities giving the investor an absolute commitment from the government to honour the debt that those securities represent.
Gilt Funds	Pooled fund investing in bonds guaranteed by the UK government.
Government MMF	MMFs that invest solely in government securities, or reverse repurchase agreements backed by Government Securities.
GPOC	General Power of Competence
HM Treasury	Her Majesty's Treasury
HRA	Housing Revenue Account
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IMP	Investment Management Practices for Non-Treasury Investments
iTraxx	The brand name for the group of credit default swaps index products.

LOBO's	Lenders Option Borrowers Option loans
LFS	Labour Force Survey
LGA	Local Government Association
LNAV	Low Volatility Net Asset Value (LVNAV) MMFs are short-term MMFs. Funds are primarily invested in money market instruments, deposits and other short-term assets. Units in the fund are purchased or redeemed at a constant price so long as the value of the underlying assets do not deviate by more than 0.2% (20bps) from par (i.e. 1.00).
MHCLG	Ministry of Housing, Communities and Local Government
MiFID	Markets in Financial Instruments Directive is a regulation that increases the transparency across the European Union's financial markets and standardises the regulatory disclosures required for particular markets. The directive has been in force across the European Union (EU) since 2008
Money Market Fund (MMF)	A well rated, highly diversified pooled investment vehicle whose assets mainly comprise of short term instruments. It is very similar to a unit trust, however in a MMF.
Monetary Policy committee (MPC)	Government body that sets the bank rate (commonly referred to as being base rate). Their primary target is to keep inflation within plus or minus 1% of a central target of 2% in two years' time from the date of the monthly meeting of the Committee. Their secondary target is to support the Government in maintaining high and stable levels of growth and employment.
MRP	Minimum Revenue Provision – the annual charge to the revenue account of the prudent provision for the repayment of debt, incurred in respect of capital expenditure financed from borrowing or other long-term credit arrangements.
MTFP	Medium Term Financial Plan
Open Ended Investment Companies	A diversified pooled investment vehicle, with a single purchase price, rather than a bid/offer spread.
OIS	Overnight Indexed Swap – an interest rate swap where the periodic floating payment is generally based on a return calculated from a daily compound interest investment.
Other Bond Funds	Pooled funds investing in a wide range of bonds.
PAYE	Pay As You Earn
PFI	Private Finance Initiative
PWLB	Public Works Loan Board
QE	Quantitative Easing
Reverse Gilt Repo	This is a transaction as seen from the point of view of the party which is buying the gilts. In this case, one party buys gilts from the other and, at the same time and as part of the same transaction, commits to resell equivalent gilts on a specified future date, or at call, at a specified price.
Retail Price Index (RPI)	Measurement of the monthly change in the average level of prices at the retail level weighted by the average expenditure pattern of the average person.
RPIX	As RPI but excluding mortgage interest rate movements.

RPIY	As RPI but excluding mortgage interest rate movements and changes in prices caused by changes in taxation.
SONIA	Sterling Overnight Index Average – SONIA is the effective reference overnight rate for unsecured transactions in the Sterling market
Sovereign Issues (Ex UK Gilts)	Bonds issued or guaranteed by nation states, but excluding UK government bonds.
Supranational Bonds	Bonds issued by supranational bodies, e.g. European investment bank. These bonds – also known as Multilateral Development Bank bonds – are generally AAA rated and behave similarly to gilts, but pay a higher yield ("spread") given their relative illiquidity when compared with gilts.
SORP	Statement of Recommended Practice
S151	Section 151 Officer
Term Deposit	A deposit held in a financial institution for a fixed term at a fixed rate.
TMP	Treasury Management Practice
Treasury Bill	Treasury bills are short term debt instruments issued by the UK or other governments. They provide a return to the investor by virtue of being issued at a discount to their final redemption value.
UBS	Union Bank of Switzerland
US	United States
Ultra-Short Dated Bond Fund (USDBF)	Fund designed to produce an enhance return over the above Money Market Fund (MMF). The manager may use a wide range of alternative options to try and generate excess performance.
VNAV	Variable Net Asset Value – refers to funds which use mark-to-market accounting to value some of the assets.
WARoR	Weighted Average Rate of Return is the average annualised rate of return weighted by the principal amount in each rate.
WAM	Weighted Average Time to Maturity is the average time, in days, till the portfolio matures, weighted by principal amount.
WATT	Weighted Average Total Time is the average time, in days, that deposits are lent out for, weighted by principal amount.
WA Risk	Weighted Average Credit Risk Number. Each institution is assigned a colour corresponding to a suggested duration using Sector's Suggested Credit Methodology.
Model WARoR	Model Weighted Average Rate of Return is the WARoR that the model produces by taking into account the risks inherent in the portfolio.

Annexe B - PRUDENTIAL INDICATORS

Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within defined limits.

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

A Capital Investments

For capital programme purposes, the Council makes a reasonable estimate of the capital debt liability, that it plans to incur or envisages will arise, in the following three years and after each year-end it will account for the actual capital expenditure incurred for each year.

The Council's capital programme informs the requirements of these indicators. In terms of the capital expenditure element of aggregate capital activity (which includes non- financial investments), the amounts incurred by the Council in 2020/21, the revised estimate for the current year and estimates for the future years are as follows:

2020/21	2021/22		2021/22	2022/23	2023/24	2024/25	Forecast
Actual	MTFP	Capital Expenditure	Forecast	Estimate	Estimate	Estimate	Total
£m	£m		£m	£m	£m	£m	£m
4.486	4.028	Families & Wellbeing	8.437	6.472	0.564	0.222	**15.695**
3.845	2.940	Corporate Services	5.032	3.144	2.801	1.596	**12.573**
33.969	44.511	Environment & Transport	33.722	63.173	53.922	8.500	**159.317**
5.387	17.127	Growth	10.210	22.976	3.405	1.970	**38.561**
303.839	335.458	Invest to Save Programme (ItS)	247.289	319.634	204.772	35.822	**807.517**
351.525	**404.064**	**Total Capital Expenditure**	**304.690**	**415.399**	**265.464**	**48.110**	**1033.663**

Invest to Save programme relates to areas such as capital expenditure on investment properties, loans to third parties, etc.

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

2020/21 Actual £m	2021/22 MTFP £m	Capital Financing	2021/22 Forecast £m	2022/23 Estimate £m	2023/24 Estimate £m	2024/25 Estimate £m	Forecast Total £m
317.887	372.798	Unsupported Borrowing	273.372	368.437	240.967	37.418	920.194
14.648	12.658	Capital Grants and Reserves	18.483	35.302	16.997	2.192	72.974
2.954	4.861	Capital Receipts	3.106	4.490	2.000	-	9.596
15.708	13.747	External Funding	9.399	7.170	5.500	8.500	30.569
0.329	0	Revenue Funding	0.330	-	-	-	0.330
351.525	**404.064**	**Total Capital Financing**	**304.690**	**415.399**	**265.464**	**48.110**	**1033.663**

B Capital financing cost indicators

One of the indicators of affordability is the estimated ratio of the Council's general fund capital financing costs to its net revenue stream in percentage terms. This indicator shows the proportion of the revenue budget spent on capital financing costs; if the ratio is increasing rapidly over time then a larger proportion of revenue resources is being taken up by capital financing costs, which could be used for other elements of the authority's budget.

For 2022/23, net revenue streams are based on the MTFP draft general fund (GF). For future years, the GF net revenue stream is projected in the Council's MTFP.

2020/21 Actual %	2021/22 MTFP %	2021/22 Forecast %	Ratio of financing costs to net revenue stream	2022/23 Estimate %	2023/24 Estimate %	2024/25 Estimate %
0.52	1.32	0.59	Services	1.15	0.99	0.04

C Capital Financing Requirement – the Council's borrowing need

Another prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR represents the total historic outstanding capital investment debt liability which has not yet been paid charged to revenue or otherwise financed. It is essentially a measure of the Council's indebtedness and in turn their underlying borrowing need. Any capital financing liability which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with each assets' life, and so charges the economic consumption of capital assets as they are used. It may also be reduced by the setting aside of monies achieved from asset disposals.

The CFR includes any other long term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility by the PFI, PPP lease provider and so the Council is not required to separately borrow for these schemes.

2021/22 MTFP £m	**2021/22 Forecast £m**	**Capital Financing Requirement (CFR)**	**2022/23 Estimate £m**	**2023/24 Estimate £m**	**2024/25 Estimate £m**
1945.762	**1753.074**	CFR	**2096.677**	**2316.740**	**2333.180**
353.592	**173.447**	**Movement in CFR**	**343.603**	**220.063**	**16.440**
352.237	246.746	Financing need for the year	368.437	240.967	37.418
20.561	26.626	Over borrowed from previous year			
(19.206)	(99.925)	Less MRP, other financing movements	(24.834)	(20.904)	(20.978)
353.592	**173.447**	**Net Movement in CFR**	**343.603**	**220.063**	**16.440**

A key aspect of the regulatory and professional guidance is that elected members are aware of the size and scope of any commercial activity in relation to the authority's overall financial position. The capital expenditure figures shown above demonstrate the scope of this activity and proportionality to the Council's remaining activity.

D Gross Borrowing Requirement

There is a clear linkage between the authority's capital financing requirement indicators and its gross external borrowing. Within the code there is a key indicator of prudence that ensures that, over the medium term, gross borrowing is only for a capital purpose. This can be demonstrated by comparing gross external borrowing shown in the table below to the total CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years. Gross external borrowing should not exceed this limit except in the short term. There is some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Council's treasury portfolio position at 31 March 2021, with forward projections are summarised below. The table shows the actual external debt (the treasury management operation), against the underlying capital borrowing need (the Capital Financing Requirement (CFR)), highlighting any over or under borrowing:

2020/21 Actual £m	2021/22 MTFP £m	2021/22 Forecast £m	Current Portfolio Position	2022/23 Estimate £m	2023/24 Estimate £m	2024/25 Estimate £m
1568.531	1612.731	1606.254	Debt at 1 April	1753.074	2096.677	2316.740
37.722	333.031	146.820	Expected change in Debt	343.603	220.063	16.440
1606.253	1945.762	1753.074	External Debt at 31 March	2096.677	2316.740	2333.180
1276.710	1945.762	1753.074	Capital Financing Requirement	2096.677	2316.740	2333.180
(329.544)	**0**	**0**	**Under / (Over) borrowing**	**0**	**0**	**0**

The Section 151 Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

E Impact of Capital Investment Decisions on Council Tax

The other indicator of affordability is the estimate of the incremental impact on Council Tax, over and above capital investment decisions that have previously been taken by the Council. This indicator identifies the repayment costs associated with proposed changes to the three year capital programme recommended in this budget report compared to the Council's existing approved commitments and current plans. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which are not published over a three year period. The indicator is intended to show the effect on Council Tax of approving new capital expenditure in the capital programme.

2020/21 Actual £	2021/22 MTFP £m	2021/22 Forecast £	Impact of Council capital programme for band D Council Tax	2022/23 Estimate £	2023/24 Estimate £	2024/25 Estimate £
11.21	10.82	7.56	Unsupported Borrowing	14.04	10.41	0.46

F Authorised Limit for External Debt

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

The authority has to set an Authorised Limit, which is the statutory maximum borrowing permitted, and an Operational Boundary, which is the normal level of borrowing expected, for external debt. This is a statutory limit determined under section 3(1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

The Authorised Limits set out below are consistent with the authority's current commitments, existing plans and the proposals set out in this report for the capital expenditure and financing, and with its approved treasury policy statement and practices. They are based on the most likely, prudent, but not worst case scenario, with sufficient headroom over and above this to allow for operational management recognising that during the year it may be necessary to exceed the operational boundary in order to take advantage of interest rate movements or to accommodate unusual cash flow movements.

2020/21 Actual £m	2021/22 MTFP £m	2021/22 Forecast £m	Authorised Limit for External finance	2022/23 Estimate £m	2023/24 Estimate £m	2024/25 Estimate £m
1606.253	2140.338	1928.381	Borrowing	2306.344	2548.414	2566.498
3.900	3.512	3.512	Other Long Term Liabilities	3.367	3.212	3.046
1610.153	**2143.850**	**1931.893**	**Total Authorised Limit**	**2309.711**	**2551.626**	**2569.544**

This indicator being the maximum limit the Council may borrow at any point in time in the year. If borrowing above this level were needed a report would go to Executive Board for authorisation to increase the limit.

G Operational Boundary for External borrowing and other financing

The operational boundary is a key management tool for in-year monitoring. Temporary breach of the operational boundary will not in itself be a cause for concern, although a sustained breach might indicate an underlying issue that would need investigation and action.

The Operational Boundaries below are based on the Authorised Limit, estimating the authority's most likely level of borrowing and leasing each year. It includes long term borrowing to fund capital and short term borrowing to meet day to day variations in cash flow but without the additional headroom.

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

2020/21 Actual £m	2021/22 MTFP £m	2021/22 Forecast £m	Operational Boundary	2022/23 Estimate £m	2023/24 Estimate £m	2024/25 Estimate £m
1606.253	1955.762	1763.074	Borrowing	2106.677	2326.740	2343.180
3.900	3.512	3.512	Other long term liabilities	3.367	3.212	3.046
1610.153	**1959.274**	**1766.586**	**Total**	**2110.044**	**2329.952**	**2346.226**

Treasury management indicators for debt

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

H Maturity structure of borrowing

It is recommended that the Council sets upper and lower limits for the maturity structure of its debt for the forthcoming year as follows:

Maturity Structure	Lower Limit		Upper Limit	
	Fixed	Variable	Fixed	Variable
Under 12 months	0%	0%	30%	40%
12 months to 2 years	0%	0%	30%	0%
2 years to 5 years	0%	0%	35%	0%
5 years to 10 years	0%	0%	30%	0%
10 years to 20 years	40%	0%	100%	0%
20 years to 30 years	40%	0%	100%	0%
30 years to 40 years	40%	0%	100%	0%
40 years and above	40%	0%	100%	0%

The above percentages are the ranges for the projected borrowing maturing in each year out of the total projected borrowing. The indicator is designed to be a control over the Council having large concentrations of fixed interest rate debt needing to be replaced at any one time and thus being at risk of having to borrow large amounts when interest rates may be unfavourable.

Please note that the maturity structure guidance for LOBO loans deems the maturity date to be the next call date which would account for £68.5m of the current loan portfolio. The loans have remained as the expected maturity date, however, these loans could potentially be called by the lender within the next six month period but they are unlikely to do so due to the current low interest rate environment.

I Fixed interest rate exposure

The table below shows the Council's upper limit for fixed interest rate exposure for the next three years. This indicator shows the percentage of borrowing that can be undertaken at fixed interest rates. Up to 100% of borrowing can be at fixed interest rates. Again, this indicator is set at levels to reduce the risk from interest rate movements.

Upper Limit – Fixed Interest Rate Exposure	2022/23 %	2023/24 %	2024/25 %
Fixed Interest Rates	100	100	100

J Variable interest rate exposure

The following indicator shows the percentage of borrowing that can be undertaken at variable interest rates. The purpose of the indicator is to restrict variable rate borrowing in order to reduce the risk from sudden movements in interest rates. The Council sets its upper limit for borrowing, reflecting variable interest rates less investments that are variable rate investments at 40%.

Upper Limit – Variable Interest Rate Exposure	**2022/23 %**	**2023/24 %**	**2024/25 %**
Variable Interest Rates	40	40	40

K Investment periods

It is recommended that the Council sets a limit on the amount invested for periods longer than one year of £120m in total for 2022/23, with the maximum period for any one investment being ten years. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment and are based on the availability of funds after each year-end.

Upper Limit for Total Principal Sums Invested for over 365 days	**2022/23 Estimate £m**	**2023/24 Estimate £m**	**2024/25 Estimate £m**
Investment	120	120	200