Cabinet
18 February 2021

Treasury Management Strategy Statement
Minimum Revenue Provision Policy Statement and Annual Investment Strategy 2021/22

Cabinet Member: Councillor Andrew Moore, Cabinet Member for Finance
Responsible Officer: Andrew Jarrett, Deputy Chief Executive (S151)

Reason for Report: To agree the proposed Treasury Management Strategy and Annual Investment Strategy for 2021/22.

RECOMMENDATION(S):

1. **That the proposed Treasury Management Strategy and Annual Investment Strategy for 2021/22, including the prudential indicators for the next 3 years and the Minimum Revenue Provision Statement (Appendix 1), be approved.**
2. **That the new limit on the Council's bank account be approved as per the table of counterparty limits in paragraph 5.2.6, and narrative in section 5.3, to enable the continued administration of Covid-19 grants to businesses and to allow for the administration of future emergency grant funds should they arise.**

Relationship to the Corporate Plan: Maximising our return from all associated treasury activities enables the Council to support current levels of spending in accordance with our Corporate Plan.

Financial Implications: Good financial management and administration underpins the entire strategy.

Legal Implications: Authorities are required by regulation to have regard to the Prudential Code when carrying out their duties under Part 1 of the Local Government Act 2003.

Risk Assessment: The S151 Officer is responsible for the administration of the financial affairs of the Council. Implementing this strategy and the CIPFA Code of Practice on Treasury Management manages the risk associated with the Council's treasury management activity.

Equality Impact Assessment: No equality issues identified for this report.

Impact on Climate Change: There are no direct impacts from the content of this report.

1.0 Background

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

1.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans, or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

1.3 The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

1.4 Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities (arising usually from capital expenditure), and are separate from the day to day treasury management activities.

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

2.0 Reporting requirements

2.1 Capital Strategy

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

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

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

2.1.3 This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset. The capital strategy will show:

- the corporate governance arrangements for these types of activities;
- any service objectives relating to the investments;
- the expected income, costs and resulting contribution;
- the debt related to the activity and the associated interest costs;
- the payback period (MRP policy);
- for non-loan type investments, the cost against the current market value and
- the risks associated with each activity.

2.1.4 Where a physical asset is being bought, details of market research, advisers used (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

2.1.5 Where the Council has borrowed to fund any non-treasury investment, there should also be an explanation of why borrowing was required and why the MHCLG Investment Guidance and CIPFA Prudential Code have not been adhered to.

2.1.6 If any non-treasury investment sustains a loss during the final accounts and audit process, the strategy and revenue implications will be reported through the same procedure as the capital strategy.

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

2.2 Treasury Management reporting

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

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

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

b. A mid-year treasury management report – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

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

2.2.2 **Scrutiny.** The above reports are required to be adequately scrutinised before being recommended to the Council. The Cabinet undertakes this role.

2.3 Treasury Management Strategy for 2021/22

2.3.1 The strategy for 2021/22 covers two main areas:

2.3.2 **Capital issues**

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

2.3.3 **Treasury management issues**

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

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

2.4 Training

2.4.1 The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. Training requirements will be reviewed in 2021/22 and training will be arranged as required. The training needs of treasury management officers are periodically reviewed.

2.5 Treasury management consultants

2.5.1 The Council uses Link Asset Services, Treasury solutions as its external treasury management advisors. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the services of our external service providers.

2.5.2 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 is assessed are properly agreed and documented, and subjected to regular review.

3.0 The Capital Prudential Indicators 2021/22 – 2023/24

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

3.2 Capital expenditure

3.2.1 This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. The table below shows planned expenditure in the capital programme.

Capital expenditure £000	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Non-HRA	2,046	2,299	7,527	14,047	13,727
HRA	4,006	2,552	11,648	15,498	7,485
Commercial activities/ non-financial investments *	6,146	2,942	15,879	15,969	12,926
Total	12,198	7,793	35,054	45,514	34,138

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

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

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

Financing of capital expenditure £000	**2019/20 Actual**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**	**2023/24 Estimate**
Capital receipts	463	395	2,408	1,755	1,638
Capital grants	1,847	986	1,624	10,896	7,056
Capital reserves	0	0	90	83	41
Revenue	3,637	3,420	6,477	6,064	3,942
Net financing need for the year	**6,251**	**2,992**	**24,455**	**26,716**	**21,461**

3.2.4 The net financing need for commercial activities / non-financial investments included in the above table against expenditure is shown below:

Commercial activities / non-financial investments £000	**2019/20 Actual**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**	**2023/24 Estimate**
Capital Expenditure	6,146	2,942	15,879	15,969	12,926
Financing costs	0	0	39	96	103
Net financing need for the year	**6,146**	**2,942**	**15,918**	**16,065**	**13,029**
Percentage of total net financing need %	98.3%	98.3%	65.1%	60.1%	60.7%

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

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

3.3.2 The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each asset's life, and so charges the economic consumption of capital assets as they are used.

3.3.3 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. The Council currently has £2.532m of such schemes within the CFR.

3.3.4 The Council is asked to approve the CFR projections below:

£000	**2019/20 Actual**	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**	**2023/24 Estimate**
Capital Financing Requirement					
CFR - non housing	7,277	9,414	11,874	13,149	18,887
CFR - housing	40,431	39,607	43,406	51,202	52,398
CFR - Commercial activities / non-financial investments	8,404	9,564	25,263	39,959	38,301
Total CFR	**56,112**	**58,585**	**80,543**	**104,310**	**109,586**
Movement in CFR*		**2,473**	**21,958**	**23,767**	**5,276**

**The movement in CFR will not directly match the Net Financing Need (see 3.2.3) due to the annual MRP charge reducing the balance in line with each* *asset's expected life. The CFR is also reduced when loan repayments are received from 3 Rivers Developments Ltd, so that only outstanding loan balances are included within the CFR.*

4.0 Borrowing

4.1 The capital expenditure plans set out in section 3 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's capital strategy. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

4.2 Current portfolio position

4.2.1 The overall treasury management portfolio as at 31 March 2020, with forward projections, is summarised below. The table shows the actual external debt (the treasury management operations) against the underlying capital borrowing need (the Capital Financing Requirement – CFR), highlighting any over or under borrowing.

£000	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
External Debt					
Debt at 1 April	**40,718**	**38,937**	**37,104**	**46,234**	**70,310**
Expected change in Debt	-1,781	-1,833	9,130	24,076	8,063
Other long-term liabilities (OLTL) at 1 April	**311**	**980**	**2,532**	**2,404**	**2,004**
Expected change in OLTL	669	1,552	-128	-400	-321
Actual gross debt at 31 March	**39,916**	**39,636**	**48,638**	**72,314**	**80,056**
Capital Financing Requirement	56,114	58,586	80,543	104,310	109,586
Under / (over) borrowing	**16,198**	**18,950**	**31,905**	**31,996**	**29,530**

4.2.2 Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2021/22 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue or speculative purposes.

4.2.3 The Deputy Chief Executive (S151) 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.

4.3 Treasury Indicators: limits to borrowing activity

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

Operational boundary £000	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Debt	57,000	79,000	103,000	108,000
Other long term liabilities	3,000	3,000	3,000	2,000
Total	60,000	82,000	106,000	110,000

4.3.2 **The authorised limit for external debt.** This is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal 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.

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

Authorised limit £000	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Debt	62,000	84,000	108,000	113,000
Other long term liabilities	7,000	7,000	7,000	6,000
Total	69,000	91,000	115,000	119,000

4.4 Prospects for interest rates

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

	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Bank Rate View	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%
5yr PWLB Rate	0.80%	0.80%	0.80%	0.80%	0.90%	0.90%	0.90%	0.90%	0.90%	1.00%	1.00%	1.00%	1.00%
10yr PWLB Rate	1.10%	1.10%	1.10%	1.10%	1.20%	1.20%	1.20%	1.20%	1.20%	1.30%	1.30%	1.30%	1.30%
25yr PWLB Rate	1.50%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.70%	1.80%	1.80%	1.80%	1.80%
50yr PWLB Rate	1.30%	1.40%	1.40%	1.40%	1.40%	1.50%	1.50%	1.50%	1.50%	1.60%	1.60%	1.60%	1.60%

4.4.2 The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its subsequent meetings to 16th December, although some forecasters had suggested that a cut into negative territory could happen. However, the Governor of the Bank of England has made it clear that he currently thinks that such a move would do more damage than good and that more quantitative easing is the favoured tool if further action becomes necessary. As shown in the forecast table above, no increase in Bank Rate is expected in the near-term as economic recovery is expected to be only gradual and, therefore, prolonged.

4.4.3 A more thorough economic outlook is detailed in appendices 2 and 3.

4.5 Borrowing strategy

4.5.1 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This level of internal borrowing will increase through 2021/22 to help mitigate the impact to Council finances of low interest rates on investments (see 5.5 investment strategy for more detail). This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

4.5.2 Against this background and the risks within the economic forecast, caution will be adopted with the 2021/22 treasury operations. The Deputy Chief Executive (S151) 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 borrowing rates,* then borrowing would be postponed.
- *If it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast,* perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.
- The Council will consider all external loan options available in the market including Public Works Loans Board, Banks, Other Local Authorities and the Municipal Bond Agency. The term and repayment profile of any loans will be determined by the periods we need finance. The level of borrowing will stay within the limits.

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

4.6 Policy on borrowing in advance of need

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

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

4.7 Debt rescheduling

4.7.1 Rescheduling of current borrowing in our debt portfolio is unlikely to occur as the penalties currently being applied to premature repayments are prohibitive.

4.7.2 If rescheduling is done, it will be reported to the Cabinet at the earliest meeting following its action.

4.8 New financial institutions as a source of borrowing and / or types of borrowing

4.8.1 Currently the PWLB Certainty Rate is set at gilts + 80 basis points for both HRA and non-HRA borrowing. However, consideration may still need to be given to sourcing funding from the following sources for the following reasons:

- 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”)
- Municipal Bonds Agency (possibly still a viable alternative depending on market circumstances prevailing at the time)

4.8.2 The degree to which any of these options proves cheaper than PWLB Certainty Rate is still evolving at the time of writing but our advisors will keep us informed.

4.9 Approved Sources of Long and Short term Borrowing

On Balance Sheet	Fixed	Variable
PWLB	●	●
Municipal Bond Agency	●	●
Local Authorities	●	
Banks	●	●
Finance Leases	●	●

5.0 Annual Investment Strategy

5.1 Investment policy – management of risk

5.1.1 The Ministry of Housing, Communities and Local Government (MHCLG) and CIPFA have extended the meaning of ‘investments’ to include both financial and non-financial investments. This report deals solely with financial investments (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy (a separate report).

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

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

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

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

5.1.5 Minimum acceptable credit criteria are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.

5.1.6 **Other information:** ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets, which the Council will achieve through engaging with its advisors to maintain a monitor on market pricing.

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

5.1.8 The Council has defined the list of **types of investment instruments** that the treasury management team are authorised to use. See Appendix 4 for a list.

5.1.9 **Lending and transaction limits** (amounts and maturity) for each counterparty will be set through applying the matrix table in paragraph 5.2.6.

5.1.10 The Council will set a limit for the amount of its investments which are invested for **longer than 365 days** (see paragraph 5.5.11).

5.1.11 Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating** (see paragraph 5.4.2).

5.1.12 The Council has engaged external consultants (see paragraph 2.5.1), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of the Council in the context of the expected level of cash balances and need for liquidity throughout the year.

5.1.13 All investments will be denominated in sterling.

5.1.14 As a result of the change in accounting standards for 2019/20 under IFRS 9, the Council will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the 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 April 2018.)

5.1.15 However, this authority will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance (see section 5.6). Regular monitoring of investment performance will be carried out during the year.

5.1.16 The above criteria are unchanged from last year.

5.2 Creditworthiness policy

5.2.1 The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle, the Council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the specified and non-specified investment sections below; and
- It has sufficient liquidity in its investments. For this purpose, it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

5.2.2 The Deputy Chief Executive (S151) will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to that which determines which types of investment instrument are either specified or non-specified as it provides an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

5.2.3 Credit rating information is supplied by Link Asset Services, our treasury advisors, on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating Watches (notification of a likely change), rating Outlooks (notification of the longer-term bias outside the central rating view) are provided to officers almost immediately after they occur and this information is considered before dealing. For instance, a negative rating Watch applying to a counterparty with the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions.

5.2.4 The criteria for providing a pool of high quality investment counterparties (both specified and non-specified investments) is:

- Banks 1 - good credit quality – the Council will only use banks which:
  1. are UK banks; and/or
  2. are non-UK and domiciled in a country which has a minimum sovereign Long Term Fitch rating of AAA

and have, as a minimum, a credit rating of F1 (Fitch), with regard for Moody's and Standard & Poor's credit ratings (where rated).

- Banks 2 – Part nationalised UK bank – Royal Bank of Scotland ring-fenced operations. These banks can be included provided they continue to be part nationalised or meet the ratings in Banks 1 above.
- Banks 3 – The Council's own banker for transactional purposes if the bank falls below the above criteria, although in this case balances will be minimised in both monetary size and time invested.
- Building societies – The Council will use all societies which:
  - iii. Meet the Fitch rating for banks outlined above; and
  - iv. Have assets in excess of £1bn;
- Money Market Funds Fitch CNAV AAAmmf/AAA
- Money Market Funds LNVAV AAAmmf/AAA
- Money Market Funds VNAV AAAmmf/AAA
- UK Government (including gilts, Treasury Bills and the DMADF)
- Local authorities, Police, Fire, parish councils and other public bodies

5.2.5 **Use of additional information other than credit ratings.** Additional requirements under the Code require the Council to supplement credit rating information. Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information will be applied to compare the relative security of differing investment opportunities.

5.2.6 **Time and monetary limits applying to investments.** The time and monetary limits for institutions on the Council's counterparty list are as follows (these will cover both specified and non-specified investments):

	Fitch Short term Rating	Money and/or % Limit	Transaction Limit	Time Limit
The Council's bank* (currently NatWest)	**F1**	**£5m + balance of grant funds**	**n/a**	**n/a**
Banks 1 higher quality	**F1**	**£5m**	**£5m**	**2yr**
Banks 1 medium quality	**n/a**	**n/a**	**n/a**	**n/a**
Banks 1 lower quality	**n/a**	**n/a**	**n/a**	**n/a**
Banks 2 – part nationalised	**F1**	**£5m**	**£5m**	**1yr**
Limit 3 category – Council's banker (not meeting Banks 1)	**F2/F3**	**£5m (call account)**	**£5m (call account)**	**1 day**
Other institutions limit (including	**n/a**	**n/a**	**n/a**	**n/a**

subsidiaries)				
DMADF	**UK sovereign rating**	**unlimited**	**unlimited**	**unlimited**
Local authorities & other public bodies	**N/A**	**unlimited**	**unlimited**	**unlimited**
Other Bodies**	**N/A**	**£3m**	**£3m**	**unlimited**
	Fund Rating	**Money and/or % Limit**	**Transaction Limit**	**Time Limit**
Money Market Funds - CNAV	**AAAmmf/AAA**	**£2m**	**£2m**	**liquid**
Money Market Funds - LVNAV	**AAAmmf/AAA**	**£2m**	**£2m**	**liquid**
Money Market Funds - VNAV	**AAAmmf/AAA**	**£2m**	**£2m**	**liquid**

**This is a new limit to allow the continued administration of business grant funds – see 5.3 for further details.*
***Relates to financial investments only – non-financial investments, such as commercial loans or purchases of income yielding assets, are covered in the Capital Strategy.*

5.2.7 The proposed criteria for specified and non-specified investments are shown in Appendix 4 for approval.

5.2.8 **Creditworthiness**

5.2.9 Although the credit rating agencies changed their outlook on many UK banks from Stable to Negative during the quarter ended 30/06/2020 due to upcoming risks to banks' earnings and asset quality during the economic downturn caused by the pandemic, the majority of ratings were affirmed due to the continuing strong credit profiles of major financial institutions, including UK banks. However, during Q1 and Q2 2020, banks made provisions for expected credit losses and the rating changes reflected these provisions. As we move into future quarters, more information will emerge on actual levels of credit losses. This has the potential to cause rating agencies to revisit their initial rating adjustments earlier in the current year. These adjustments could be negative or positive, although it should also be borne in mind that banks went into this pandemic with strong balance sheets. This is predominantly a result of regulatory changes imposed on banks following the Great Financial Crisis. Indeed, the Financial Policy Committee (FPC) report on 6th August revised down their expected credit losses for the UK banking sector to "somewhat less than £80bn". It stated that in its assessment, "banks have buffers of capital more than sufficient to absorb the losses that are likely to arise under the MPC's central projection". The FPC stated that for real stress in the sector, the economic output would need to be twice as bad as the MPC's projection, with unemployment rising to above 15%.

5.2.10 All three rating agencies have reviewed banks around the world with similar results in many countries of most banks being placed on Negative Outlook, but with a small number of actual downgrades.

5.3 Change to the Council's bank limit

5.3.1 Towards the end of March 2020, approval was given by the Deputy Chief Executive (S151) and the Cabinet lead for Finance to breach the £5m counterparty limit with the Council's banking provider, NatWest, for an initial period of three months. This was to allow the administration of the business grant schemes announced by Government as part of the Covid-19 response, and to ensure sufficient funds were held whilst cash flows remained volatile. The Council received £22.732m on 1 April 2020 to fund these schemes, which ended on 28 August 2020 leaving £2.548m unspent. This continues to be held in the Council's NatWest account until repayment is required.

5.3.2 Further approval was given at the end of June for a temporary counterparty limit of £10m with NatWest for 3 months, which was extended at the start of October for a further 3 months. This allowed the administration of new business grant funds during England's second lockdown and local tiered restrictions during November & December, with £3.108m and £0.436m received respectively.

5.3.3 At the start of January a new round of business grant funds were announced to get businesses through the most recent lockdown, with this Council receiving a total of £7.307m to fund the schemes. With the grant funds from November & December still ongoing, this increased the total of grant funds being held to £12.108m, and so new temporary approval was given to replace the £10m counterparty limit with NatWest to £5m plus the balance of any grant funds being administered by the Council.

5.3.4 **Recommendation 2 proposes that this current flexible limit of £5m plus the balance of grant funds for the Council's bank, NatWest, be added to the Council's authorised counterparty limits in 5.2.6 above.** This allows the continued administration of current and future business grant funds, which are expected to continue well into 2021/22, whilst limiting the Council's own funds held with NatWest to £5m and so keeping financial risk at an acceptable level.

5.4 Other limits

5.4.1 Due care will be taken to consider the country, group and sector exposure of the Council's investments.

5.4.2 **Country limit.** The Council has determined that it will only use approved counterparties from the UK and from countries with a minimum sovereign credit rating of AAA. The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 5. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

5.4.3 **Other limits.** In addition:

- no more than 30% of overall investment balances will be placed with any non-UK country at any time;
- limits in place above will apply to a group of companies; and

- the Council will not hold more than £5m with any banking group.

5.5 Investment strategy

5.5.1 **In-house funds**

5.5.2 Over recent years, the Council has typically held upwards of £20m in short term investments with the objective of managing cash flows whilst earning a return at the same time. Before the Covid-19 pandemic hit in Q4 2019/20, interest rates had been increasing gradually, with some short term investments earning over 1% and generating a return for the Council of £238k in 2019/20. Since then, interest rates have plummeted, and with only a very limited recovery forecast during 2021/22 the expected annual return on current levels of short term investments is circa £20k. With significant levels of capital expenditure expected during 2021/22, it is recommended that the Council maximises its use of internal borrowing rather than seeking to fund projects through new external borrowing.

5.5.3 Retaining cash balances (short term investments + current account [excluding Covid-19 grant funds]) of £10m would be enough to ensure a regular turnover in short term investments to manage the fluctuations in cash flows. Therefore, internal borrowing will be used to finance capital expenditure where cash balances remain above £10m, with external borrowing only sought to keep balances above this limit. With current interest rates, this could result in net savings of around £66k per annum versus maintaining cash balances at current levels.

5.5.4 As cash balances reduce through 2021/22, there will be a need to reduce the average maturity on investments to ensure a regular turnover of maturities, which will be matched with the Council's large cash outflows. This will mean the primary consideration for investments will be the core balance and cash flow requirements, with the outlook for short-term interest rates only considered where significant changes are expected. Greater returns are usually obtainable by investing for longer periods, however this needs to be balanced with the Council's cash requirements.

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

5.5.5 **Investment returns expectations**

5.5.6 Bank Rate is unlikely to rise from 0.10% for a considerable period. It is very difficult to say when it may start rising so it may be best to assume that investment earnings from money market-related instruments will be sub 0.50% for the foreseeable future.

5.5.7 The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows (the later years forecast is for periods over 10 years in the future):

2020/21	0.10%
2021/22	0.10%

2022/23	0.10%
2023/24	0.10%
2024/25	0.25%
Later years	2.00%

5.5.8 The overall balance of risks to economic growth in the UK is probably now skewed to the upside, but is subject to major uncertainty due to the virus and how quickly successful vaccines may become available and widely administered to the population.

5.5.9 There is relatively little UK domestic risk of increases or decreases in Bank Rate and significant changes in shorter term PWLB rates. The Bank of England has effectively ruled out the use of negative interest rates in the near term and increases in Bank Rate are likely to be some years away given the underlying economic expectations. However, it is always possible that safe haven flows, due to unexpected domestic developments and those in other major economies, or a return of investor confidence in equities, could impact gilt yields (and so PWLB rates) in the UK.

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

5.5.11 The Council is asked to approve the following treasury indicator and limit:

Upper limit for principal sums invested for longer than 365 days	2020/21 (£m)	2021/22 (£m)	2022/23 (£m)
Principal sum invested for longer than 365 days but not exceeding 2 years.	5	5	5

5.5.12 For its cash flow generated balances, the Council will seek to utilise money market funds and short-dated deposits (overnight to 365 days) in order to benefit from the compounding of interest.

5.5.13 **Negative investment rates**

5.5.14 While the Bank of England said in August / September 2020 that it is unlikely to introduce a negative Bank Rate, at least in the next 6 -12 months, and in November omitted any mention of negative rates in the minutes of the meeting of the Monetary Policy Committee, some deposit accounts are already offering negative rates for shorter periods. As part of the response to the pandemic and lockdown, the Bank and the Government have provided financial markets and businesses with plentiful access to credit, either directly or through commercial banks. In addition, the Government has provided large sums of grants to local authorities to help deal with the COVID crisis; this has caused some local authorities to have sudden large increases in cash balances searching for an investment home, some of which was only very short term until those sums were able to be passed on.

5.5.15 As for money market funds (MMFs), 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 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.

5.5.16 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.

5.6 Investment performance / risk benchmarking

5.6.1 The Council will use an investment benchmark to assess the performance of its investment portfolio of 7 day LIBID.

5.7 End of year investment report

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

5.8 Commercial and Non-Financial Investments

5.8.1 **Property Investments.** A limit of £5m will be applied to the use of non-specified investments. This principally relates to property funds, which is within the Local Authorities' Property Fund via CCLA.

5.8.2 **Non-Financial Investments.** On the 30th March 2017, Cabinet approved the establishment of a Special Purpose Vehicle – 3 Rivers Developments Limited and that the Council could lend to 3 Rivers Developments Ltd. This company is a subsidiary of Mid Devon District Council and has the sole purpose of property development.

5.8.3 There is no cap on the amount of money that can be loaned to 3 Rivers Developments Ltd. However, for each new project the company takes on, there is an individual loan agreement signed by the S151 Officer prior to any lending. All project spending / borrowing requirements are approved annually by Cabinet as part of the company's Annual Report/Business Plan.

5.8.4 Please refer to the Capital Strategy for a more detailed programme and borrowing streams.

APPENDICES

1. Prudential and treasury indicators and MRP statement
2. Interest rate forecasts
3. Economic background
4. Treasury management practice 1 – credit and counterparty risk management
5. Approved countries for investments
6. Treasury management scheme of delegation
7. The treasury management role of the Section 151 Officer
8. Current list of eligible counterparties
9. Treasury Management Practices (TMPs)

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APPENDIX 1

1.0 THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2021/22 – 2023/24

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

1.1 Capital expenditure

See section 3.2 for the breakdown of capital expenditure.

1.2 Affordability prudential indicators

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

Ratio of financing costs to net revenue stream

This indicator identifies the trend in the cost of capital, (borrowing and other long-term obligation costs net of investment income), against the net revenue stream.

%	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Non-HRA	-0.13%	2.65%	8.41%	7.46%	8.40%
HRA	15.54%	15.01%	15.10%	14.49%	14.12%

The estimates of financing costs include current commitments and the proposals in this budget report.

1.3 Minimum Revenue Provision (MRP) Policy Statement

Where the Council finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Council to have regard to the Ministry of Housing, Communities & Local Government *Statutory Guidance on Minimum Revenue Provision* (the MHCLG Guidance) most recently updated in 2018.

The broad aim of the MHCLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

The MHCLG Guidance requires the Council to approve an Annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP. The Council is recommended to approve the following MRP Statement*:*

For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will be:

- **Based on CFR** – MRP will be based on the CFR.

These options provide for an approximate 4% reduction in the borrowing need (CFR) each year.

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be*:*

- **Asset life method** – MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction)

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

Finance leases will have their capital financing applied on a straight line basis over the life of the lease contract.

There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made (although there are transitional arrangements in place).

The MRP requirement for a finance lease or PFI contract is deemed to be equal to the element of the charge/rent that goes to write down the balance sheet liability.

For capital expenditure loans to third parties that are repaid in annual or more frequent instalments of principal, the Council will make nil MRP, but will instead apply the capital receipts arising from principal repayments to reduce the capital financing requirement. In years where there is no principal repayment, MRP will be charged in accordance with the MRP policy for the assets funded by the loan.

Capital expenditure incurred during 2021/22 will not be subject to a MRP charge until 2022/23.

1.4 MRP Overpayments

A change introduced by the revised MHCLG MRP Guidance was the allowance that any charges made over the statutory minimum revenue provision (MRP), voluntary revenue provision or overpayments, can, if needed, be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. Up until the 31 March 2020, the total VRP overpayments were £0m.

APPENDIX 2

2.0 INTEREST RATE FORECASTS 2021-2024

Link Asset Services Interest Rate View

	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Bank Rate View	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%
5yr PWLB Rate	0.80%	0.80%	0.80%	0.80%	0.90%	0.90%	0.90%	0.90%	0.90%	1.00%	1.00%	1.00%	1.00%
10yr PWLB Rate	1.10%	1.10%	1.10%	1.10%	1.20%	1.20%	1.20%	1.20%	1.20%	1.30%	1.30%	1.30%	1.30%
25yr PWLB Rate	1.50%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.70%	1.80%	1.80%	1.80%	1.80%
50yr PWLB Rate	1.30%	1.40%	1.40%	1.40%	1.40%	1.50%	1.50%	1.50%	1.50%	1.60%	1.60%	1.60%	1.60%

The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its subsequent meetings to 16th December, although some forecasters had suggested that a cut into negative territory could happen. However, the Governor of the Bank of England has made it clear that he currently thinks that such a move would do more damage than good and that more quantitative easing is the favoured tool if further action becomes necessary. As shown in the forecast table above, no increase in Bank Rate is expected in the near-term as economic recovery is expected to be only gradual and, therefore, prolonged.

Gilt yields / PWLB rates
There was much speculation during the second half of 2019 that bond markets were in a bubble that was driving bond prices up and yields down to historically very low levels. The context for that was a heightened expectation that the US could have been heading for a recession in 2020. In addition, there were growing expectations of a downturn in world economic growth, especially due to fears around the impact of the trade war between the US and China, together with inflation generally at low levels in most countries and expected to remain subdued. Combined, these conditions were conducive to very low bond yields. While inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation expectations, the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers. This means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc.

The consequence of this has been the gradual lowering of the overall level of interest rates and bond yields in financial markets over the last 30 years. Over the year prior to the coronavirus crisis, this has seen many bond yields up to 10 years turn negative in the Eurozone. In addition, there has, at times, been an inversion of bond yields in the US whereby 10-year yields have fallen below shorter-term yields. In the past, this has been a precursor of a recession.

Gilt yields had already been on a generally falling trend up until the coronavirus crisis hit western economies during March 2020. After gilt yields spiked up in March, we have subsequently seen these yields fall sharply to unprecedented lows as investors panicked during March in selling shares in anticipation of impending recessions in western economies, and moved cash into safe haven assets such as government bonds. However, major western central banks took rapid action to deal with excessive stress in financial markets during March, and started massive quantitative easing purchases of government bonds. Such unprecedented levels of issuance in "normal" times would have caused bond yields to rise sharply. Gilt yields and PWLB rates have been at remarkably low rates so far during 2020/21.

As the interest forecast table for PWLB certainty rates above shows, there is expected to be little upward movement in PWLB rates over the next two years as it will take economies, including the UK, a prolonged period to recover all the momentum they have lost in the sharp recession caused during the coronavirus shut down period. Gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to sharp changes in investor sentiment (as shown on 9th November when the first results of a successful Covid-19 vaccine trial were announced). Such volatility could occur at any time during the forecast period.

Investment and borrowing rates

- **Investment returns** are likely to remain exceptionally low during 2021/22 with little increase in the following two years.

- **Borrowing interest rates** fell to historically very low rates as a result of the Covid-19 crisis and the quantitative easing operations of the Bank of England. The policy of avoiding new borrowing by running down spare cash balances has served local authorities well over the last few years. The unexpected increase of 100 bps in PWLB rates on top of the then current margin over gilt yields of 80 bps in October 2019 required an initial major rethink of local authority treasury management strategy and risk management. However, in March 2020, the Government started a consultation process for reviewing the margins over gilt rates for PWLB borrowing for different types of local authority capital expenditure. It also introduced the following rates for borrowing for different types of capital expenditure: -

    - **PWLB Standard Rate** is gilt plus 200 basis points (G+200bps)
    - **PWLB Certainty Rate** is gilt plus 180 basis points (G+180bps)
    - **PWLB HRA Standard Rate** is gilt plus 100 basis points (G+100bps)
    - **PWLB HRA Certainty Rate** is gilt plus 80bps (G+80bps)
    - **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)

- Because of these increases in margins, many local authorities decided to refrain from PWLB borrowing unless it was for HRA or local infrastructure financing, until such time as the review of margins was concluded.

- On 25/11/2020, the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates; the standard and certainty margins were reduced by 1% but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three-year capital programme. The new margins over gilt yields are as follows:

    - **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)
    - **PWLB Certainty Rate** is gilt plus 80 basis points (G+80bps)
    - **PWLB HRA Standard Rate** is gilt plus 100 basis points (G+100bps)
    - **PWLB HRA Certainty Rate** is gilt plus 80bps (G+80bps)

- **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)

APPENDIX 3

3.0 ECONOMIC BACKGROUND

- **UK.** The key quarterly meeting of the Bank of England Monetary Policy Committee kept **Bank Rate** unchanged on 05/11/2020. However, it revised its economic forecasts to take account of a second national lockdown from 05/11/2020 to 02/12/2020 which is obviously going to put back economic recovery and do further damage to the economy. It therefore decided to do a further tranche of **quantitative easing (QE) of £150bn**, to start in January when the current programme of £300bn of QE, announced in March to June, runs out.
- Its forecasts appeared, at that time, to be rather optimistic in terms of three areas:
    - The economy would recover to reach its pre-pandemic level in Q1 2022.
    - The Bank also expected there to be excess demand in the economy by Q4 2022.
    - CPI inflation was therefore projected to be a bit above its 2% target by the start of 2023 and the "inflation risks were judged to be balanced".
- There was no mention of **negative interest rates** in the minutes or Monetary Policy Report, suggesting that the MPC remains some way from being persuaded of the case for such a policy, at least for the next 6 -12 months.
- If **inflation** rises to 2% in the next couple of years, it is unlikely the MPC will raise Bank Rate until they can clearly see that level of inflation is going to be persistently above target. There could well be no increase during the next five years as it will take some years to eliminate spare capacity in the economy.
- Household saving rates having been exceptionally high since the first Covid-19 lockdown in March, so there is plenty of pent-up demand and purchasing power. Effective vaccines would radically improve the economic outlook once they have been widely administered; it may allow GDP to rise to its pre-virus level a year earlier than otherwise and mean that the unemployment rate peaks at 7% in 2021 instead of 9%.
- Overall, **the pace of recovery** was not expected to be in the form of a rapid V shape, but a more elongated and prolonged one. The initial recovery was sharp after quarter 1 saw growth at -3.0% followed by -18.8% in quarter 2 and then an upswing of +16.0% in quarter 3; this still left the economy 8.6% smaller than in Q4 2019. It is likely that the one month national lockdown that started on 5th November, will have caused a further contraction of 8% m/m in November so the economy may have then been 14% below its pre-crisis level.
- There will still be some **painful longer term adjustments** as, for example, office space and travel by planes, trains and buses may not recover to their previous level of use for several years, or possibly ever, even if vaccines are fully successful in overcoming the current virus. There is also

likely to be a reversal of globalisation as this crisis has exposed how vulnerable long-distance supply chains are. On the other hand, digital services are one area that has already seen huge growth.

- **Brexit.** While the UK has been gripped by the long running saga of whether or not a deal would be made by 31/12/2020, the final agreement on 24/12/2020, followed by ratification by Parliament and all 27 EU countries in the following week, has eliminated a significant downside risk for the UK economy. The initial agreement only covers trade so there is further work to be done on the services sector where temporary equivalence has been granted in both directions between the UK and EU; that now needs to be formalised on a permanent basis.
- **EU.** In early December, the figures for Q3 GDP confirmed that the economy staged a rapid rebound from the first lockdowns. This provides grounds for optimism about growth prospects for next year. In Q2, GDP was 15% below its pre-pandemic level. But in Q3 the economy grew by 12.5% q/q leaving GDP down by “only” 4.4%.
- With inflation expected to be unlikely to get much above 1% over the next two years, **the ECB** has been struggling to get inflation up to its 2% target. It is currently unlikely that it will cut its central rate even further into negative territory from -0.5%, although the ECB has stated that it retains this as a possible tool to use.
- **World growth.** World growth will have been in recession in 2020. Inflation is unlikely to be a problem for some years due to the creation of excess production capacity and depressed demand caused by the coronavirus crisis.
- Until recent years, world growth has been boosted by increasing **globalisation** i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last thirty years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy. The Chinese government has targeted achieving major world positions in specific key sectors and products. It is achieving this by massive financial support (i.e. subsidies) to state owned firms, government directions to other firms, technology theft and restrictions on market access by foreign firms. This is regarded as being unfair competition that is putting western firms at an unfair disadvantage. It is, therefore, likely that we are heading into a period where there will be a **reversal of world globalisation and a decoupling of western countries** from dependence on China to supply products. This is likely to produce a backdrop in the coming years of weak global growth and so weak inflation.
- Central banks are likely to support growth by maintaining loose monetary policy through keeping rates very low for longer. Governments could also help a quicker recovery by providing more fiscal support for their economies at a time when total debt is affordable due to the very low rates of interest. They will also need to avoid significant increases in taxation or austerity measures that depress demand in their economies.

APPENDIX 4

4.0 TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT

Specified Investments: All investments with a high level of credit quality subject to a maturity limit of one year.

Non-Specified Investments: Any investments that do not meet the specified investment criteria. These may be of a lower credit quality, for periods in excess of one year, or are more complex instruments which require a greater consideration by members and officers before being authorised for use. A maximum of £5m will be held in aggregate in non-specified investment.

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

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

	Minimum credit criteria	Max % of total investments / £ limit per institution	Max. maturity period
DMADF – UK Government	N/A	100%	Any
UK Government gilts	UK sovereign rating	100%	Any
UK Government Treasury bills	UK sovereign rating	100%	Any
Money Market Funds CNAV	AAAmmf/AAA	100%	Liquid
Money Market Funds LNVAV	AAAmmf/AAA	£2m	Liquid
Money Market Funds VNAV	AAAmmf/AAA	£2m	Liquid
Local authorities	N/A	100%	Any
Term deposits with banks and building societies	F1 (Fitch) / £1bn asset base for building societies	£5m	2 Years

Term deposits with Non-UK banks and building societies	Sovereign Fitch rating of AAA	£3m	1 Year
Gilt funds	UK sovereign rating	100%	Any
Property funds	LA Property Fund	£5m	Ongoing

Accounting treatment of investments. The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by the Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

Non-specified investments. A maximum of £5m will be held in aggregate in non specified investments.

APPENDIX 5

5.0 APPROVED COUNTRIES FOR INVESTMENTS

AAA

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

The sovereign ratings shown above are at 5 January 2021 from Link.

APPENDIX 6

6.0 TREASURY MANAGEMENT SCHEME OF DELEGATION

(i) Full Council

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

(ii) Cabinet

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

(iii) Cabinet

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

(iv) Delegation from the Deputy Chief Executive (S151) to the nominated post(s) for the taking of the investment decisions:

- Group Manager for Finance (Deputy S151)

APPENDIX 7

7.0 THE TREASURY MANAGEMENT ROLE OF THE SECTION 151 OFFICER

The S151 (responsible) officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers;
- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long term timeframe for example 25+ years;
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money;
- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority;
- ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing;
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources;
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities;
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees;
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority;
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above;
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following
    - *Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios;*

- *Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments;*

- *Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making;*

- *Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken;*

- *Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.*

APPENDIX 8

8.0 CURRENT LIST OF ELIGIBLE COUNTERPARTIES

Counterparty Lending List as at 15/01/2021:

UK Banks **Bank**	Fitch Credit Rating **Short Term**	Moody's Rating **Short Term**	S&P Rating **Short Term**
HSBC Bank plc	F1+	P-1	A-1
Bank of Scotland Plc	F1	P-1	A-1
Barclays Bank plc	F1	P-1	A-1
Lloyds Bank Plc	F1	P-1	A-1
Goldman Sachs International	F1	P-1	A-1
Standard Chartered Bank	F1	P-1	A-1
Santander UK plc	F1	P-1	A-1
Sumitomo Mitsui Banking Corp Europe	F1	P-1	A-1
UBS	F1+	P-1	A-1
Nationalised/Part Nationalised Banks			
Royal Bank of Scotland Plc	F1	P-1	A-1
National Westminster Bank	F1	P-1	A-1

Building Societies

Group Asset Ranking		**Society Assets £m**	**Fitch Short Term**	**Year end**
1	Nationwide	238,301	F1	Apr-19
2	Coventry	46,071	F1	Dec-18
3	Yorkshire	43,055	F1	Dec-18
4	Skipton	23,204	F1	Dec-18
5	Leeds	19,390	F1	Dec-18

Note:
The above lists do not include Non-UK banks or building societies as, although being part of the Investment Strategy since 2019/20, no suitable counterparties have been found that offer competitive interest rates compared to UK banks and building societies.

APPENDIX 9

9.0 TREASURY MANAGEMENT PRACTICES (TMPs)

CIPFA lists 12 TMPSs that the council are recommended to adopt. The Deputy Chief Executive (S151) will have delegated approval over the TMPs. Any recommendations from the Deputy Chief Executive (S151) will be submitted to Cabinet for review.