REFERRAL FROM THE AUDIT COMMITTEE

Treasury Management Strategy Statement 2018/19, Annual Investment Strategy 2018/19 and Minimum Revenue Provision Policy Statement 2018/19

Chairman of the Committee: Councillor Mike Appleyard

Officer Contact: David Skinner: David.Skinner@wycombe.gov.uk

Proposed recommendation to Council

To approve**:**

- The Treasury Management Strategy Statement (TMSS) and Prudential Indicators for 2018/;
- Annual Investment Strategy (AIS) for 2018/19 at Appendix A;
- Minimum Revenue Provision Policy Statement for 2018/19 at Appendix B; and

1. Reason

To comply with the Local Government Act 2003, other regulations and guidance and to ensure that the Council's investment plans are prudent, affordable, sustainable and comply with statutory requirements.

The Committee is responsible for ensuring effective scrutiny of the Treasury Management Strategy.

Corporate Implications

The Treasury Management Strategy plays a significant part in supporting the delivery of the Council's vision and corporate priorities.

2. Executive Summary

2.1. The Local Government Act 2003 requires the Council to set out a statement of its treasury management strategy for borrowing and to prepare an Annual Investment Strategy. This sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

2.2. This report sets out the Council's proposed Treasury Management Strategy Statement (TMSS) and Annual Investment Strategy (AIS) for the year 2018/19.

3. Background

3.1. 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.

3.2. 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.

3.3. Treasury management is defined 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."

3.4. CIPFA requirements - The Council has formally adopted CIPFA's Code of Practice on Treasury Management and complies with the requirements of the Codes as detailed below:

a. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
b. Creation and maintenance of Treasury Management Practices ("TMPs") that set out the manner in which the Council will seek to achieve those policies and objectives.
c. Receipt by the full Council and/or Cabinet of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Half-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.
d. 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. The details of delegations and responsibilities are summarised in Appendix C.
e. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For the Council this role is undertaken by Audit Committee.

3.5. **Training -** 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. The training needs of treasury management officers are periodically reviewed as part of the Learning and Development programme. The officers attend various seminars and conferences throughout the year. As part of developing financial management training programme Members will be provided training as and when required.

3.6. **Treasury management consultants**

a. Link Asset Services (The Link Group has acquired Capita Asset Services formerly part of Capita plc) are Wycombe District Council's 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 our external service providers.

b. 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.

3.7. Markets in Financial Instruments Directive (MiFID II)

c. The Markets in Financial Instruments Directive, or MiFID II, is an EU regulation designed to offer greater protection for investors and inject more transparency into all asset classes: from equities to fixed income, exchange traded funds and foreign exchange.

d. The EU has now set a deadline of 3 January 2018 for the introduction of regulations under MIFID II. These regulations will govern the relationship that financial institutions conducting lending and borrowing transactions will have with local authorities from that date. The Directive will result in the automatic reclassification of local authorities as retail clients unless they choose to elect to professional client status. The Council is electing to professional client status in order to preserve the range of financial instruments, advice and services that it currently accesses.

3.8. Treasury Management Strategy covers three main areas summarised below:

i. <u>Capital Strategy (Section 4)</u>
   a) Capital expenditure plans;
   b) Capital Financing Requirement (CFR);
   c) Affordability – Ratio of Financing cost;
   d) Affordability – Incremental impact of capital investment decisions on Council Tax; and
   e) The Minimum Revenue Provision (MRP) policy (Appendix B).

ii. <u>Borrowing strategy (Section 5);</u>
   a) Current borrowing position;
   b) Indicators : Limits on External Borrowing;
   c) Borrowing Strategy; and
   d) Policy on borrowing in advance of need.

iii. <u>Treasury Management (Section 6)</u>
   a) Current treasury position;
   b) Core funds and expected investment balances;
   c) Expected return on investments and benchmarking; and
   d) Investment Limits

3.9. The Annual Investment Strategy (AIS) at Appendix A provides more detail on how the Council will manage its risks and liquidity in 2018/19.

Treasury Management Strategy Statement

4. Capital Strategy

Capital Spending and funding plans

4.1. 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.

4.2. Table 1 summarises the Council's capital expenditure plans, both in terms of those agreed previously, and those forming part of the current budget cycle. The table also sets out the Council's current expectations of how these plans are to be financed.

2016/17 Actual £m		2017/18 Forecast £m	2018/19 Estimate £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	Total £m
14.017	**Expenditure General Fund**	**17.176**	**45.358**	**37.812**	**31.353**	**29.458**	**6.758**	**167.915**
	Funding							
-2.214	Grants & Contributions	-3.946	-19.495	-7.261	-6.189	-6.815	-3.990	**-47.696**
-4.899	Capital Receipts	-13.230	-20.720	-9.000	-9.800	-5.000	-2.768	**-60.518**
-6.904	Revenue Financing	0.000	-5.143	-20.933	-0.532	-0.304	0.000	**-26.912**
0.000	Borrowing	0.000	0.000	-0.618	-14.832	-17.339	0.000	**-32.789**
-14.017	**Total**	**-17.176**	**-45.358**	**-37.812**	**-31.353**	**-29.458**	**-6.758**	**-167.915**

4.3. The Department for Communities and Local Government (DCLG) have consulted on the proposed changes to the prudential framework of capital finance. The proposals fore for Local Authorities Investment Code and Minimum Revenue Provision Guidance. The outcome of the consultation is still awaited, however the proposed changes are incorporated within the strategy as detailed in paragraphs 4.4 to 4.7.

4.4. The prudential code on capital finance requires Council's to ensure that the capital investment plans are prudent, sustainable and affordable in the long term. In considering the capital programme, in addition to the initial investments, the financing, ongoing repairs and maintenance costs should be considered to ensure these are sustainable and affordable in the medium to long term.

4.5. As well as investing in assets owned by the Council and used in the delivery of services, the Council also invests, where appropriate, in commercial properties which generates revenue to support the delivery of service to the local community within the district.

4.6. Over the years the Council has organically grown its commercial portfolio and invested in traditional asset classes of offices, retail and industrial/logistics, which meet the Council requirements of sustainable economic growth within the district and the income to be secure and reliable and the investments low risk.

4.7. The current capital strategy includes proposals for strategic land acquisition and housing development to deliver Local Plan. These are long-term prudent proposals which will deliver the Council ambition of economic development for the district by investing in assets in such a way that not only delivers regeneration and growth in a sustainable way, but also generates annual revenue to support our services for the local residents.

4.8. As part of the due diligence process and risk assessment, consideration is given to the inherent nature of risks around valuations, volatility of property markets, sustainability of rental income and Council's dependence on this income stream to deliver services.

Capital Financing Requirement (CFR)

4.9. The CFR measures the extent to which capital expenditure has not yet been financed from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so it's underlying borrowing need. Any capital expenditure, which has not immediately been financed or paid for, will increase the CFR.

4.10. 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 assets life, and so charges the economic consumption of capital assets as they are used.

4.11. The CFR includes other long-term liabilities such as embedded lease included within the Chiltern Waste contract. Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of contracts include a borrowing facility by the lease provider and so the Council is not required to separately borrow for these leases.

4.12. The Council's Capital Financing Requirement position at 31 March 2017, with forward projections are summarised on the following page in Table 2.

2016/17	Table 2	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Actual		Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
£m		£m	£m	£m	£m	£m	£m
3.206	Gross Projected Debt	2.406	1.606	1.418	15.450	32.789	32.789
6.908	CFR 31st March	5.901	4.894	4.505	18.413	35.342	34.686
3.702	**Under borrowing**	**3.495**	**3.288**	**3.087**	**2.963**	**2.553**	**1.897**

4.13. The above projections confirms that the Council's gross debt does not exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for current year and the following two financial years. This allows some flexibility for limited early borrowing for future years if required, but ensures that borrowing is not undertaken for revenue purposes.

4.14. The Head of Finance and Commercial reports that the Council complied with this indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing programme and the proposals in the budget report.

Affordability

4.15. The objective of the affordability indicators is to ensure that the level of investment in capital assets proposed remains within sustainable limits, and in particular, the impact on the Council's "bottom line" as reflected in the impact on council tax. Table 3 below sets out the expected ratio of capital financing costs to income for General Fund. There is a significant increase in this ratio for 2018/19 resulting mainly form revenue reserves being used to fund the Capital Programme.

4.16. The Council's financial strategy is based on the premise that the capital programme is fully funded from various sources and does not require borrowing. Which means that the new programme does not have any incremental impact on council tax levels.

2016/17	Table 3	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Actual		Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
47%	Ratio of financing cost	-2%	34%	-150%	-3%	4%	8%

5. Borrowing

5.1. 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 the day to day requirement for service delivery and also capital strategy. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities.

Borrowing Limits

5.2. The Code requires the Council to set two limits on its total external debt, as set out in Table 4 below. The limits are:

a. **Authorised Limit for External Debt** – This is the limit prescribed by section 3(1) of the Local Government Act 2003 representing the maximum level of borrowing which the Council may incur. It reflects the level of external debt which, while not desired, could be afforded in the short term, but may not be sustainable in the longer term.

b. **Operational Boundary** – This is the limit which external debt is not normally expected to exceed. The boundary is based on current debt plus anticipated net financing need for future years.

2016/17	Table 4	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Actual		Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
£m		£m	£m	£m	£m	£m	£m
	Authorised Limit for external debt						
3	Borrowing and other long term liabilities	11	10	10	23	40	40
	Operational Boundary for external debt						
0	Borrowing	4	3	4	19	36	36
3	Other long term liabilities	2	2	1	0	0	0
3	**Total**	6	5	5	19	36	36
	Upper limit for fixed interest rate exposure						
0	Net principal re fixed rate borrowing	4	3	4	19	36	36
	Upper limit for variable rate exposure						
0	Net principal re variable rate borrowing	0	0	0	0	0	0
6	Upper limit for principal sums invested over 364 days	40	40	40	40	40	40

Prospects for Interest Rates

5.3. 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. Further Economic Background is provided at Appendix D by Link Asset Services. The table on the next page gives the advisor's central view.

	Now	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21
Bank Rate	0.50	0.50	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.25	1.25	1.25
5 yr PWLB	1.50	1.50	1.60	1.60	1.70	1.80	1.80	1.90	1.90	2.00	2.10	2.10	2.20	2.30	2.30
10 yr PWLB	2.10	2.10	2.20	2.30	2.40	2.40	2.50	2.60	2.60	2.70	2.70	2.80	2.90	2.90	3.00
25 yr PWLB	2.70	2.80	2.90	3.00	3.00	3.10	3.10	3.20	3.20	3.30	3.40	3.50	3.50	3.60	3.60
50 yr PWLB	2.40	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.00	3.10	3.20	3.30	3.30	3.40	3.40

5.4. Borrowing interest rates increased sharply after the result of the general election in June and then also after the September MPC meeting when financial markets reacted by accelerating their expectations for the timing of Bank Rate increases. Since then, borrowing rates have eased back again somewhat. Apart from that, there has been little general trend in borrowing rates during the current financial year.

5.5. After a decade, Bank Rate was increased from 0.25% to 0.50% in November 2017. As detailed in the table above the current forecast is a gradual increase in base rates over time with the next increase of 0.25% is expected in the last quarter of 2018.

Borrowing strategy

5.6. The Council is currently maintaining an under-borrowed position due to healthy cash balance and this seems likely to continue for the next two or three years at least. This position is measured against the Capital Financing Requirement which is a technical calculation and takes account of cash-flow timing difference. This puts council in a good position as the capital borrowing need, 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 has served well especially in the recent years with low interest rates and high counter party risks.

5.7. The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in the future when the Council may not be able to avoid new borrowing to finance capital expenditure.

5.8. If borrowing is undertaken in this environment there will be a net cost of holding this money until it is used, sometimes called the "cost of carry". As borrowing is often for longer dated periods (anything up to 60 years) the cost of carry needs to be considered against a backdrop of uncertainty and affordability constraints in the Council's wider financial position.

5.9. The Council will adopt a flexible approach to any future long-term borrowing in consultation with, Link Asset Services. Affordability and interest rate risk will be considered prior to undertaking any external borrowing.

Policy on Borrowing in Advance of Need

5.10. The Council has the power to borrow in advance of need in line with its future borrowing requirements under the Local Authorities (Capital Finance and Accounting)(England) Regulations 2003, as amended.

5.11. 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.

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

6. Treasury Management

Current cash position

6.1. Table 5 below shows the cash balance position as at December 2017.

	As at 31 March 2017		As at 31 December 2017	
	Principal £m	Average Rate %	Principal £m	Average Rate %
Investments				
Specified	63.6		80.7	
Non - specified	11.0		13.0	
Total Investments	**74.6**	**0.67%**	**93.7**	**0.65%**

Core Funds and expected Cash Flow

6.2. The application of resources to either finance capital expenditure or revenue budget will have an ongoing impact on investments. Detailed below are estimates of the year end balances for each resource.

2016/17 Actual	Year End Resources	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
£m		£m	£m	£m	£m	£m	£m
- 9.739	General Reserves	- 9.739	- 9.739	- 9.739	- 9.739	- 9.739	- 9.739
- 35.360	Earmarked Reserves	- 35.768	- 29.506	- 7.787	- 6.937	- 6.287	- 5.637
- 18.329	Capital receipts	- 9.420	-	-	-	-	- 5.232
- 12.227	Capital Grants & Contributions	- 13.081	- 6.600	- 5.989	- 8.600	- 11.155	- 10.965
- 3.261	Provisions	- 3.261	- 3.261	- 3.261	- 3.261	- 3.261	- 3.261
- 78.916	**Total core funds**	**- 71.269**	**- 49.106**	**- 26.776**	**- 28.537**	**- 30.442**	**- 34.834**
- 0.457	Working capital*	5.000	5.000	5.000	5.000	5.000	5.000
3.702	Under Borrowing	-	-	-	-	-	-
75.401	Expected investments	66.269	44.106	21.776	23.537	25.442	29.834
*Working capital balances shown are estimated year end; these may be higher at certain points during the year							

6.3. The medium-term cash flow shows that the Council has a substantial positive cash-flow position with an average cash position of more than £25m for the medium-term.

6.4. Council policy is to set aside £5m to provide working capital and cover day to day contingencies. Therefore an average of £40m is available to be invested over the longer-term without impacting on the Council's need for liquidity.

Background Papers

Treasury Management Strategy Statement 2017/18 (Approved by Council February 2017)

1. Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended

2. DCLG Guidance on Minimum Revenue Provision 2012

3. DCLG Guidance on Local Government Investments – March 2010

4. CIPFA Prudential Code for Capital Finance in Local Authorities, 2011

5. CIPFA Treasury Management Code of Practice, 2011