Treasury Management Strategy

1 Introduction

1.1 The Local Government Act 2003 requires the Council to set out a statement of its Treasury Management Strategy. This sets out the Council's policies for managing its borrowings and investments and for giving priority to the security and liquidity of those investments.

1.2 The Strategy is prepared in compliance with the :-

1.2.1 Statutory guidance on Local Government Investments issued under section 15(1)(a) of the Local Government Act 2003.

1.2.2 CIPFA Treasury Management Code of Practice and Cross-Sectoral Guidance, 2017 edition.

1.2.3 CIPFA Prudential Code for Capital Finance in Local Authorities, 2017 edition.

1.3 **The key changes to the strategy from last year are:**

1.3.1 Removal of the prudential indicator – impact on council tax decisions (in line with the proposed new CIPFA code).

1.3.2 Inclusion of more local indicators.

1.3.3 The Treasury Management Practices (TMPs) to be approved by Members.

2 Background

2.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the Treasury Management 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.

2.2 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 CIPFA requirements

3.1 The Council has formally adopted CIPFA's Treasury Management Code of Practice and Cross-Sectoral Guidance and complies with the requirements of the Codes as detailed below:

3.1.1 Creation of Treasury Management policy statement, stating the policies, objectives and approach to risk management of its Treasury Management activities

3.1.2 A suitable Treasury Management practices (TMPs) attached at Appendix 3A, setting out the manner in which the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

3.1.3 The full Council and/or Cabinet will receive reports on its Treasury Management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMPs.

3.1.4 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 3B. The body and officers responsible will act in accordance with the organisation's policy statement and TMPs and, if he/she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

3.1.5 The Council nominates Audit Committee to be responsible for ensuring effective scrutiny of the Treasury Management strategy and policies.

3.2 **Treasury Management Strategy covers three main areas summarised below:**

- Treasury Management Policy Statement (Section 4)
- Prudential and Treasury Indicators (Section 5);
- Other matters (Section 6)

4 Treasury Management Policy Statement

4.1 Introduction

4.1.1 This section defines the policies and objectives of Treasury Management activities.

4.1.2 The Council defines its Treasury Management activities as:

> 'The management of the organisation'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.'

4.1.3 The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its Treasury Management activities will be measured. Accordingly, the analysis and reporting of Treasury Management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

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

4.2 Borrowing Policy

4.2.1 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 the 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.

4.2.2 The Capital programme for the medium to long-term is based on the key principle of zero borrowing. The policy of avoiding new borrowing by running down spare cash and reserves 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.

4.2.3 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.

4.2.4 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.

4.3 Policy on Borrowing in Advance of Need

4.3.1 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.

4.3.2 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.

4.3.3 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.

4.4 Investment Policy

4.4.1 The Council holds significant surplus funds, representing income received in advance of expenditure, plus balances and reserves. Both the CIPFA Code and the CLG Guidance require the Council to invest its funds prudently with two underlying objectives:

(i) **Security** – protecting the capital sum invested from loss; and

(ii) **Liquidity** – ensuring the funds invested are available for expenditure when needed.

4.4.2 Generation of yield is distinct from these prudential objectives. Once proper levels of security and liquidity are determined, it will then be reasonable to consider what yield can be obtained consistent with these priorities. The council must in order of importance to have regard to the security and liquidity of its treasury investments before seeking the highest rate of return, or yield.

4.5 Security

Financial Investments: These can fall into one of three categories: **Specified investments**; **Loans**; and **Other Non-specified investments**.

4.5.1 Specified Investments: An investment is a specified investment if all of the following apply:

- The investment and any associated cash-flows are denominated in sterling.
- The investment has a maximum maturity of one year.
- The making of the investment is not defined as capital expenditure.
- The investment is made with a body or in an investment scheme described as high quality or with the UK Government, a UK Local Authority or parish/community council.

4.5.2 Loans**:** A local authority may choose to make loans to local enterprises, local charities, wholly owned companies and joint ventures as part of a wider strategy for local economic growth even though those loans may not all be seen as prudent if adopting a narrow definition of prioritising security and liquidity. The financial exposure to these type of loans is proportionate.

4.5.3 Non-specified investments: A non-specified investment is any financial investment that is not a loan and does not meet the criteria to be treated as a specified investment.

4.5.4 Non-financial investments: These are Treasury investments in non-financial assets that the Council holds primarily to generate profit. It would normally be a physical asset that can be realised to recoup the capital invested when the funds are needed. When entering into these investments, the Council will consider the balance between security, liquidity and yield based on the risk appetite and the contributions of that investment activity. The Council has set a limit of £7.5m for this type of investment.

4.6 **Risks**

4.6.1 The Council is exposed to number of risks whilst carrying out the Treasury Management activities. The Council's does not have any borrowing and the medium term capital programme does not rely on any external borrowing. Based on zero borrowing position for the foreseeable future, the Council has a balanced approach to risks towards is Treasury Management activities which is mainly investment of surplus cash and the associated returns. To assist the achievement of this objective the Council will prioritise security and liquidity of investments over returns. The risks associated with investments are summarised below along with the policies in place to manage them:

4.6.2 **Credit risk**: The CIPFA Code defines this risk as :

'The risk of failure by a counterparty to meet its contractual obligations to the organisation under an investment, borrowing, capital, project or partnership financing, particularly as a result of the counterparty's diminished creditworthiness, and the resulting detrimental effect on the organisation's capital or current (revenue) resources.'

To minimise this risk to investments, the Council applies minimum acceptable credit criteria to generate a list of highly creditworthy counterparties which will provide security of investments, enable diversification and minimise risk. The creditworthiness methodology used to create the counterparty list fully accounts for the ratings, watches and outlooks published by all three ratings agencies. The Treasury Management Adviser monitors counterparty ratings on a real time basis with knowledge of any changes advised electronically as the agencies notify modifications. The creditworthiness policy along with the schedule of counter parties and the limits are detailed in Appendix 3C.

4.6.3 **Liquidity risk**: This risk can be defined as :

'The risk that cash will not be available when it is needed, that ineffective management of liquidity creates additional unbudgeted costs, and that the organisation's business or service objectives will be thereby compromised'

The Council has a comprehensive cash flow management system that seeks to ensure that cash is available as needed. The Council maintains an under borrowing position as detailed in paragraph 5.2.8, therefore if unexpected movements lead to liquidity issues then the Council has ready access to borrowing from the money markets and the Public Works Loans Board.

4.6.4 **Interest Rate Risk**: This risk is defined as the risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.

The treasury team monitors market and forecast interest rates to adjust exposures appropriately. For instance, during period of falling interest rates and where economic circumstances make it favourable, fixed rate investments may be taken for longer periods to secure better long term returns. The council does not use any hedging instruments to manage this risk.

5 Prudential & Treasury Management Indicators

5.1 Introduction

5.1.1 The objectives of the Prudential Code are to ensure, within a clear framework, that the capital expenditure plans of local authorities are affordable, prudent and sustainable.

5.1.2 To fulfil these objectives, the Prudential Code sets out the indicators that must be used and are designed to support and record local decision-making in a manner that is publicly accountable.

5.1.3 In setting prudential indicators, the Council has taken into consideration its Service objectives, Stewardship of assets, Value for money, Prudence and sustainability, Affordability and Practicality.

5.2 Prudential Indicators

5.2.1 The Council's capital expenditure plans are a key driver of Treasury Management activity. The outputs of the capital expenditure plan are reflected in prudential indicators detailed below, which are designed to assist members when making decisions.

5.2.2 **Capital Spending and funding plans**: The table 1 below summarises the Council's capital expenditure plans, and also sets out the Council's current expectations of how these plans are to be financed.

2017/18 Actual £m	Table 1	2018/19 Forecast £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m	Total £m
11.785	**Expenditure General Fund**	**21.552**	**51.745**	**25.266**	**25.088**	**10.339**	**0.303**	**134.293**
	Funding							
-5.046	Grants & Contributions	-7.214	-15.748	-7.000	-12.400	-3.666	0.000	**-46.028**
-6.739	Capital Receipts	0.000	-24.511	-17.628	-12.283	-6.069	-0.303	**-60.794**
0.000	Revenue Financing	-14.338	-11.486	-0.638	-0.405	-0.604	0.000	**-27.471**
-11.785	**Total**	**-21.552**	**-51.745**	**-25.266**	**-25.088**	**-10.339**	**-0.303**	**-134.293**

5.2.3 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.

5.2.4 **Capital Financing Requirement (CFR):** This 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.

5.2.5 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.

5.2.6 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.

5.2.7 The **Council's** Capital Financing Requirement position at 31 March 2018, with forward projections are summarised in the Table 2 below.

2017/18	Table 2	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
Actual		Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
£m		£m	£m	£m	£m	£m	£m
2.390	Gross Projected Debt	1.590	0.790	0.000	0.000	0.000	0.000
5.879	CFR 31st March	4.888	3.943	3.836	3.735	3.634	3.533
3.489	**Under borrowing**	**3.298**	**3.153**	**3.836**	**3.735**	**3.634**	**3.533**

5.2.8 **Gross Debt and the CFR**: 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.

5.2.9 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.

5.2.10 **Affordability:** The objective of the affordability indicators is to ensure that the level of investment in capital assets proposed remains within sustainable limits. Table 3 below sets out the expected ratio of capital financing costs to income for General Fund.

2017/18	Table 3	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
Actual		Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
6.02	Ratio of financing cost %	3.94	0.80	- 2.54	- 3.22	- 3.77	- 4.02

5.3 Treasury Indicators

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

5.3.1.1 **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.

5.3.1.2 **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.

2017/18 Actual £m	Table 4	2018/19 Forecast £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
	Authorised Limit for external debt						
2	Borrowing and other long term liabilities	10	9	9	9	9	9
	Operational Boundary for external debt						
0	Borrowing	3	3	4	4	4	4
2	Other long term liabilities	2	1	0	0	0	0
2	**Total**	5	4	4	4	4	4

5.3.2 **Interest rate exposure:** Due to no borrowing strategy, the council does not have significant exposure to interest rate risks. Table 5 below sets out the limits for fixed term borrowing and investments over 365 days.

2017/18 Actual £m	Table 5	2018/19 Forecast £m	2019/20 Estimate £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m
	Upper limit for fixed interest rate exposure						
0	Net principal re fixed rate borrowing	3	3	4	4	4	4
	Upper limit for variable rate exposure						
0	Net principal re variable rate borrowing	0	0	0	0	0	0
13	Upper limit for principal sums invested over 364 days	40	20	10	20	20	20

5.3.3 **Treasury Performance and Cash Position:** The return on treasury investment is benchmarked against the 3 month London Inter-bank Offered Rate (LIBOR). Table 6 below summarises the performance for the 9 months of the financial year.

Table 6	**As at 31 December 2018**		**As at 31 March 2018**	
	£m	**%**	**£m**	**%**
Specified Investments (up to 1 year)				
Banks & Building Socities	50.75	54%	39.55	49%
Local Authorities	23.00	25%	0.00	0%
Money Market Funds	9.40	10%	15.00	19%
Non - specified Investments (longer than a year)				
Local Authorities	3.00	3%	13.00	16%
Property Fund	7.50	8%	7.50	9%
Gilt	0.00	0%	4.98	7%
Total Investments	**93.65**	**100%**	**80.03**	**100%**
Benchmark 3 month LIBOR		**0.63%**		**0.41%**
Actual average return		**1.19%**		**0.73%**

5.3.4 The Council's budgeted investment return for 2019/20 is £929k, which is based on the interest rate forecast as shown in table 7 below and expected cash-flow as summarised in paragraph 5.3.5, Table 8.

Table 7	NOW	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate	0.75	0.75	1.00	1.00	1.00	1.25	1.25	1.25	1.50	1.50	1.75	1.75	1.75	2.00
5 yr PWLB	2.10	2.10	2.20	2.20	2.30	2.30	2.40	2.50	2.50	2.60	2.60	2.70	2.80	2.80
10 yr PWLB	2.50	2.50	2.60	2.60	2.70	2.80	2.90	2.90	3.00	3.00	3.10	3.10	3.20	3.20
25 yr PWLB	2.90	2.90	3.00	3.10	3.10	3.20	3.30	3.30	3.40	3.40	3.50	3.50	3.60	3.60
50 yr PWLB	2.70	2.70	2.80	2.90	2.90	3.00	3.10	3.10	3.20	3.20	3.30	3.30	3.40	3.40

5.3.5 **Core Funds and Expected Cash Flow** : 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.

Table 8

2017/18 Actual	Year End Resources	2018/19 Forecast	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
£m		£m	£m	£m	£m	£m	£m
- 9.848	General Reserves	- 9.952	- 9.952	- 9.952	- 9.952	- 9.952	- 9.952
- 40.245	Earmarked Reserves	- 25.378	- 13.514	- 13.026	- 13.354	- 13.474	- 14.602
- 16.844	Capital receipts	- 22.044	- 11.533	- 1.905	- 4.122	- 4.053	- 3.750
- 13.350	Capital Grants & Contributions	- 11.636	- 4.688	- 8.688	- 12.688	- 16.722	- 16.722
- 5.018	Provisions	- 5.018	- 5.018	- 5.018	- 5.018	- 5.018	- 5.018
- 85.305	**Total core funds**	**- 74.028**	**- 44.705**	**- 38.589**	**- 45.134**	**- 49.219**	**- 50.044**
0.459	Working capital*	5.000	5.000	5.000	5.000	5.000	5.000
3.489	Under Borrowing	3.298	3.153	3.836	3.735	3.634	3.533
80.327	Expected investments	- 65.730	- 36.552	- 29.753	- 36.399	- 40.585	- 41.511

*Working capital balances shown are estimated year end; these may be higher at certain points during the year

5.3.6 The medium-term cash flow shows that the Council has a substantial positive cash-flow position with an average cash position of just under £30m for the medium-term.

6 Other Updates

6.1 UK Banks – ring fencing

6.1.1 The largest UK banks, (those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits), are required, by UK law, to separate core retail banking services from their investment and international banking activities by 1st January 2019. This is known as "ring-fencing".

6.1.2 Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and SME deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler, activities offered from within a ring-fenced bank, (RFB), will be focused on lower risk, day-to-day core transactions, whilst more complex and "riskier" activities are required to be housed in a separate entity, a non-ring-fenced bank, (NRFB). This is intended to ensure that an entity's core activities are not adversely affected by the acts or omissions of other members of its group.

6.1.3 While the structure of the banks included within this process may change, the fundamentals of credit assessment would not. The Council will continue to assess the new-formed entities in the same way that it does others and those with sufficiently high ratings, (and any other metrics considered), will be considered for investment purposes.

6.2 Money Market Funds (MMF) Reforms

6.2.1 The MMF regulation permits four types of MMF : Public Debt Constant Net Asset Value MMF ('Public Debt CNAV MMF"); Low Volatility constant Net Asset Value MMF ("LVNAV MMF"); Short-term variable NAV MMF and Standard Variable NAV MMF.

6.2.2 The main differences between the existing CNAV MMF and the two new types of CNAV MMF are:

6.2.2.1 **Valuations**: Amortised cost still permitted and LVNAV can use amortised cost up to 75 days maturity and mark-to-market for longer asset maturities;

6.2.2.2 **Liquidity**: New daily and weekly liquidity requirements are in place;

6.2.2.3 **Diversification**: Additional more restrictive rules;

6.2.2.4 **Eligible assets**: similar to current rules and Public Debt CNAV must have 99.5% government assets, cash or reverse repo backed by government assets; and

6.2.2.5 **Redemption gates and fees**:

If weekly liquidity < 10%, then either liquidity fees or a suspension of redemption.

If weekly liquidity < 30% and net daily redemption >10% of total assets, must consider applying liquidity fees, redemption gates or a suspension of redemption.

6.2.3 The new rules will apply to all MMFs crated after 21st July 2018 and existing MMFs will have until 21 January 2019. All the Council's investments held in MMF funds fall into the LVNAV category and has been in compliance since 9th January 2019 which is before the deadline of 21 January 2019.

6.3 IFRS 9 Accounting Standard – Financial Instrument

6.3.1 This accounting standard came into effect from 1st April 2018. It means that the category of investments valued under the available for sale category will be removed from the Statutory Accounts, and any potential fluctuations in market valuations may impact onto the Surplus or Deficit on the Provision of Services, rather than being held on the balance sheet.

6.3.2 This change is unlikely to materially affect the commonly used types of Treasury Management investments but more specialist types of investments, (e.g. pooled funds, third party loans, commercial investments), are likely to be impacted. Currently the Council holds an investment of £7.5m in Property Pooled Fund which will be impacted by the new accounting standard.

6.3.3 Following the consultation by The Ministry of Housing, Communities and Local Government (MHCLG), a temporary override period for 5 years has been allowed for English local authorities to adjust their portfolio of investments. This will mean that any fluctuations in market valuation of Property Pooled Fund will not have any impact on the surplus or deficit on the provision of services.