Doncaster Council

Report

Date: 16th February 2021

To the Chair and Members of Cabinet

THE TREASURY MANAGEMENT STRATEGY STATEMENT 2021/22 – 2024/25

EXECUTIVE SUMMARY

1. This report details the strategy for management of the council finances and provides a framework for the operation of the treasury management function within the Council. Treasury management seeks to optimise the council's cash flow and secure the most effective arrangements to support long term funding requirements. Key prudential indicators relating to borrowing limits are contained in the body of the report, with the prudential indicators relating to affordability in **Appendix A**. The key messages are: -

   a. Borrowing – total borrowing requirement will increase during the period covered by this report but the Council will remain under-borrowed against its total borrowing requirement to avoid the higher cost of carrying debt (Capital Financing Requirement 2021/22 £617m). As borrowing rates are forecast to rise gently over the next 3 years, the primary borrowing strategy for new and replacement debt will be to take cheaper short-term loans to maximise interest savings over the period of the report. The borrowing strategy is detailed in **paragraphs 26 – 70**.

   b. Investments – securing the return of investment funds remains paramount when selecting counterparties and the strategy reflects this. The Investment Strategy will continue to manage the balances available and support cash flow requirements. The Investment Strategy is a low risk policy with minimal returns in value; this protects the Council from losses caused by financial institutions failing to repay investments when due. This policy allows the Council to spread the risk amongst a number of approved lenders, and financial instruments as outlined in **paragraphs 71 – 110.**

2. The Council has to approve the local policy for approach to debt repayment (Minimum Revenue Provision – MRP) which is detailed in **Appendix B**.

EXEMPT REPORT

3. Not applicable.

RECOMMENDATIONS

4. Cabinet is asked to recommend to Council, the Treasury Management Strategy Statement 2021/22 – 2024/25 report and the Prudential Indicators included.
5. Cabinet is asked to recommend to Council the Minimum Revenue Provision (MRP) policy as set out in paragraphs 39 - 40 (details in **Appendix B**).

WHAT DOES THIS MEAN FOR THE CITIZENS OF DONCASTER?

6. This Strategy ensures that the Council's Capital Programme borrowing requirement is affordable and takes advantage of low short-term interest rates to deliver savings for the Council. By ensuring that the treasury management function is effective, we can ensure that the right resources are available at the right time to enable the delivery of services.

BACKGROUND

7. 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 function is to ensure that this cash flow is planned, with cash being available when it is needed. Surplus monies are invested in low risk financial institutions and instruments in line with the Council's low risk appetite, providing liquidity before considering investment return. 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.
8. The second main function of treasury management is the funding of the Council's Capital Programme. The Capital Programme provides a guide to the borrowing need of the Council and 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 existing debt may be restructured to reduce Council risk or generate savings.
9. 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.
10. Chartered Institute of Public Finance and Accounting (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".

11. For the Council to produce a strategy that is compliant with the statutory guidelines, a number of acts and guidance have to be taken into account.

12. 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;
    - The implications for future financial stability.

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

14. There are five reports containing treasury information 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 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. **Finance and Performance Improvement Report** – Quarterly report presented to Directors, Executive Board and Cabinet.

       - Details Treasury Management position at the end of each quarter
       - Interest rate levels
       - Under/Over borrowing position
       - Associated risks
       - Investment profile

15. All the above reports are scrutinised by the Overview and Scrutiny Management Committee.

16. The Treasury Management strategy for 2021/22 – 2024/25 covers two main areas: -

    Capital Issues
    a) the capital expenditure plans and the associated prudential indicators;
    b) MRP policy.

    Treasury Management Issues
    a) the current treasury position;
    b) treasury indicators which limit treasury risk and activities of the Council;
    c) prospects for interest rates;
    d) the borrowing strategy;

e) policy on borrowing in advance of need;
f) debt rescheduling;
g) the investment strategy;
h) creditworthiness policy; and
i) policy on use of external service providers.

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

Training

18. 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. No training has taken place during 2020/21 but sessions will be held in 2021/22.

19. The training needs of treasury management officers are periodically reviewed.

Treasury management consultants

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

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

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

The Capital Programme Prudential Indicators 2021/22 – 2024/25

23. The Council's Capital Programme is the key driver of treasury management activity. The Prudential Indicators are designed to assist members' overview and confirm capital expenditure plans.

Capital Expenditure

24. The first prudential indicator is a summary of the Council's Capital Programme expenditure plans and funding. It includes existing expenditure commitments, and those included in the 2021/22 – 2024/25 budget cycle.

	Actual	Estimates				
	2019/20 £k	2020/21 £k	2021/22 £k	2022/23 £k	2023/24 £k	2024/25 £k
Capital Expenditure						
General Fund (GF)	**63,913**	**63,274**	**68,281**	**42,074**	**19,955**	**14,446**
HRA	**22,988**	**20,181**	**39,446**	**62,790**	**47,463**	**46,827**
Total	**86,901**	**83,455**	**107,727**	**104,864**	**67,418**	**61,273**

25. The following table summarises the above capital expenditure plans and how capital or revenue resources are financing these plans. Any shortfall of resources results in a funding borrowing need.

	Actual	Estimates				
	2019/20 £k	2020/21 £k	2021/22 £k	2022/23 £k	2023/24 £k	2024/25 £k
Financing of Capital Expenditure						
Capital Receipts	8,047	7,198	19,173	7,054	4,320	3,140
Capital Grants	30,334	35,719	33,428	28,856	9,005	3,773
Capital Reserves	965	810	380	0	0	0
Revenue	24,251	20,111	28,829	33,940	25,157	25,300
Sub Total	**63,597**	**63,838**	**81,810**	**69,850**	**38,482**	**32,213**
Net Financing Need	**23,304**	**19,617**	**25,917**	**35,014**	**28,936**	**29,060**

Borrowing

26. The capital expenditure plans set out below 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.

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

27. The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply total historic outstanding capital expenditure that has not been fully funded. It is a measure of the Council's underlying borrowing need.

28. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

29. The CFR does not increase indefinitely, as 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.

30. The CFR includes any other long-term liabilities (e.g. Private Finance Iiniative (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, Purchasing Power Parity (PPP) lease provider and so the Council is not required to borrow separately for these schemes. As at 31/03/20, the Council had £46.7m of such schemes within the CFR:

	Actual	**Estimates**				
	2019/20 £k	**2020/21 £k**	**2021/22 £k**	**2022/23 £k**	**2023/24 £k**	**2024/25 £k**
Capital Financing Requirement						
GF	316,754	329,959	336,481	348,124	353,945	359,940
HRA	267,069	267,428	280,416	296,416	312,416	328,416
Total CFR	**583,823**	**597,387**	**616,897**	**644,540**	**666,361**	**688,356**
Movement in CFR	**15,640**	**13,564**	**19,510**	**27,643**	**21,821**	**21,995**
Represented by						
Net Financing Need (table above)	23,304	19,617	25,917	35,014	28,936	29,060
Less MRP/Other financing adjustment	**(7,664)**	**(6,053)**	**(6,407)**	**(7,371)**	**(7,115)**	**(7,065)**
Movement in CFR	**15,640**	**13,564**	**19,510**	**27,643**	**21,821**	**21,995**

31. The Council is forecast to have borrowed £521.3m as at 31/03/21 against a CFR (borrowing requirement) of £597.4m which means that the Council is currently forecast to be under-borrowed (see paragraphs 32 to 35) by £76.2m. This minimises external interest costs but may not be sustainable long term.

Under- Borrowing

32. As detailed above, the Council is currently maintaining an under-borrowed position. This means that the level of actual debt is below the Capital Financing Requirement (the amount the authority needs to borrow for capital purposes) and therefore the Council has to use internal resources such as earmarked reserves, unapplied grants and capital receipts, cash balances, etc. to fund some of its unfinanced capital expenditure.

33. This strategy is beneficial because external debt interest payments are minimised and funds available for investments are reduced at a time when investment returns remain low.

34. This position cannot be sustained in the long term. The reserves and balances may be needed and consequently the need to borrow will increase. This could be short-term or long-term borrowing. The Council have used short-term borrowing opportunities from other authorities as they have restricted lending lists which means they lend at rates lower than the Public Works Loan Board (PWLB) rates.

35. The Council has decided to pre-pay its future service rate pension liabilities, at a discounted rate, for 2020/21 to 2022/23. The prepayment has been funded through borrowing. This has reduced the under borrowed position until the pension prepayment loans are repaid.

Short-Term Borrowing

36. The use of short-term borrowing can make the borrowing portfolio volatile in terms of interest rate and refinancing risk. The benefit to the Council is low interest costs which has enabled the treasury management function to generate savings, which have been re-prioritised to service delivery. The risk inherent to using this

approach has to be balanced against the need to find savings and produce a balanced budget.

37. There is a risk associated with a short-term borrowing strategy. As interest rates are likely to rise in future years, long-term borrowing will be more expensive than it is currently. By deferring long-term borrowing until later years, it is likely that additional costs will be incurred. We are balancing long term stable interest costs against short-term interest savings.

38. Unless new resources are identified, e.g. grants, asset sales, etc. funding the Capital Programme from balances will decrease investment balances and hence reduce investment income levels but the loss, currently, is more than offset by the interest savings generated by not taking on the full borrowing requirement.

The Minimum Revenue Provision (MRP)

39. The Council is required by statute to charge MRP to the General Fund Revenue Account each year for the repayment of debt. The MRP charge is the means by which capital expenditure, which has been funded by borrowing, is paid for by council taxpayers.

40. The Council's MRP policy is detailed at **Appendix B**. The selected methods are those that are most beneficial in each case and comply with Ministry of Housing, Communities & Local Government (MHCLG) regulations.

Core funds and expected investment balances

41. The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year-end balances for each resource and anticipated day-to-day cash flow balances. It should be noted that the use of resources is difficult to predict and a cautious approach is taken.

Year End Resources	Actual	Estimates				
	2019/20 £k	2020/21 £k	2021/22 £k	2022/23 £k	2023/24 £k	2024/25 £k
Reserves balances	84,435	122,435	103,335	84,435	84,435	84,435
Capital receipts	17,348	14,664	15,358	15,950	15,603	16,037
Provisions	14,609	14,609	14,609	14,609	14,609	14,609
Capital Grants Unapplied	19,572	19,572	19,572	19,572	19,572	19,572
Total core funds	**135,964**	**171,280**	**152,874**	**134,566**	**134,219**	**134,653**
Working capital	8,485	8,485	8,485	8,485	8,485	8,485
Under/over borrowing	81,121	76,234	69,827	62,456	55,341	48,276
Expected investments	**46,358**	**86,561**	**74,562**	**63,625**	**70,393**	**77,892**

Current Portfolio Position

42. There are a number of key prudential indicators to ensure that the Council operates within well-defined limits. One of these is that the Council needs to

ensure that its total borrowing does not, except in the short term, exceed the total of the CFR. This helps to ensure that over the medium term borrowing is not undertaken for revenue purposes.

43. The Chief Financial Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this report. As previously stated the Council's external borrowing at 31st March 2021 is expected to be £521.2m. This is split across two pools as shown in the table below. The borrowing need (total CFR) is £597.4m, which highlights that the Council will be under-borrowed by £76.2m (see paragraphs 32 to 35 above).

44. The Council's forward projections for borrowing are summarised below. The table shows the actual external debt, against the underlying capital borrowing need, (the CFR), highlighting any over or under borrowing.

Portfolio Position	Actual	Estimates				
	2019/20 £k	2020/21 £k	2021/22 £k	2022/23 £k	2023/24 £k	2024/25 £k
CFR General Fund	**315,588**	**329,959**	**336,481**	**348,124**	**353,945**	**359,940**
External Borrowing	235,473	254,731	267,660	286,674	299,610	312,670
Under-borrowed Position	80,114	75,228	68,821	61,450	54,335	47,270
Ave. Interest Rate	2.87%	2.61%	2.34%	2.32%	2.26%	2.23%
CFR HRA	**267,069**	**267,428**	**280,416**	**296,416**	**312,416**	**328,416**
External Borrowing	266,063	266,422	279,410	295,410	311,410	327,410
Under-borrowed Position *	1,006	1,006	1,006	1,006	1,006	1,006
Average Interest Rate	4.66%	4.63%	4.40%	4.25%	4.06%	4.21%
Total CFR	**582,657**	**597,387**	**616,897**	**644,540**	**666,361**	**688,356**
Total External debt	**501,536**	**521,153**	**547,070**	**582,084**	**611,020**	**640,080**
Total Under-borrowing	**81,121**	**76,234**	**69,827**	**62,456**	**55,341**	**48,276**

*As there is no requirement to apply MRP to the Housing Revenue Account (HRA) borrowing, its under-borrowed position would only change because of a strategic change in the Council's borrowing pool makeup or external borrowing position, e.g. increase/decrease in external debt.

45. Both debt pools have relatively low interest rates, which are expected to rise gently between 2021/22 and 2024/25. The average interest rate on HRA debt is higher than the GF debt as the pool contains a higher proportion of older or longer term, debt taken out at higher interest rates.

46. Treasury management decisions on the structure and timing of borrowing will be made independently for the general fund (GF) and HRA. Interest on loans will be calculated in accordance with proper accounting practices. This will require interest expenditure on external borrowing attributed to HRA loans being allocated to the HRA. Interest expenditure on external borrowing attributed to the GF will be allocated to the GF.

47. Following changes to the MHCLG guidance, the council needs to report debt relating to commercial activities/non-financial investments separately. The Council confirms that we do not currently have any debt relating to commercial activities/non-financial investments and there are no plans for this to change during the term of this report.

Treasury Indicators: Limits to Borrowing Activity

48. These are the 2 overall controls for treasury management external borrowing: -

- The 'operational boundary' for external borrowing; and
- The 'authorised limit' for external borrowing.

Operational Boundary for external borrowing

49. This is the normally expected limit for external borrowing. For 2021/22, the limit is **£616.9m**. In most cases, this would be a similar figure to the CFR. However, Doncaster Council's operational boundary adds in our 'other long term liabilities' (which is Metropolitan Debt transferred from South Yorkshire County Council, the final repayment is due to be made in 2020/21).

Operational Boundary	Actual	Estimates				
	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
	£k	£k	£k	£k	£k	£k
CFR/Borrowing	583,823	597,387	616,897	644,540	666,361	688,356
Other long-term liabilities Met. Debt	4,762	2,381	0	0	0	0
Total	**588,585**	**599,768**	**616,897**	**644,540**	**666,361**	**688,356**

The Authorised Limit for external borrowing

50. A further key prudential indicator is a control on the maximum level of borrowing. This represents the statutory legal limit, determined under section 3 of the Local Government Act 2003, beyond which external borrowing is prohibited and this limit needs to be set or revised by the full Council.

51. It reflects the level of external borrowing, which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

52. This allows the Council to borrow in advance (up to 3 years) of need for future planned expenditure – relating solely to unfinanced capital expenditure in any future 3-year period. The Council does not borrow in advance and this would only be considered where interest rates were preferential and to avoid future interest rate risk. This would mean that the council would incur additional interest costs and principal repayments before benefiting from a developed asset. For 2021/22, the limit is **£706.8m.**

Authorised limit	Actual	Estimates				
	2019/20 £k	2020/21 £k	2021/22 £k	2022/23 £k	2023/24 £k	2024/25 £k
Borrowing	583,823	597,387	616,897	644,540	666,361	688,356
Other long-term liabilities – 'Met. Debt'	4,762	2,381	0	0	0	0
Theoretical amount	0	80,548	89,867	93,010	0	0
Total	**588,585**	**680,316**	**706,764**	**737,550**	**666,361**	**688,356**

Treasury Management Limits on activity

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

Prospects for Interest Rates

54. Part of the service provided by the council's treasury advisors is to assist the Council to formulate a view on interest rates. **Appendix D** draws together a number of current City forecasts for short term (Bank Rate) and longer term fixed interest rates.

55. Economic and interest rate forecasting remains difficult with so many external influences weighing on the United Kingdom (UK). The Link forecasts will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Within a benign interest rate environment, the overall balance of risks to economic recovery in the UK is probably to the downside, particularly with the current level of uncertainty over the speedy completion of new trade deals as part of the Brexit transition period.

56. There are a number of downside risks to current forecasts for UK gilt yields and PWLB rates, e.g. an increase in the Bank Rate causes UK economic growth and increases in inflation, to be weaker than we currently anticipate.

57. There is also the potential for upside risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates, e.g. the bank rate raises too slowly and therefore, allows inflation pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.

Borrowing Strategy

58. The borrowing strategy is a continuation of the recent successful strategy that has generated large interest savings. The savings are generated in two ways, being under-borrowed (see paragraphs 32 to 35) and borrowing short term (see paragraphs 36 to 38). As interest rates are forecast to increase gently over the term of this strategy we propose to continue to borrow short term rather than lock into the historically low long term interest rates. Where the Chief Financial Officer considers it is prudent to do so borrowing may be taken over a longer period.

59. The savings, which are very sensitive to a movement in interest rates, assume that the under-borrowing will continue. There remains risks associated with the under-borrowing but these will probably be eroded over time through the application of MRP.

60. The strategy delays some borrowing as long as possible to generate interest saving. For example at today's interest rates, if we were to borrow the £76.2m (forecast under-borrowed amount as at 31st March 2021) from the PWLB over 5 years interest would cost £0.8m per annum and over 25 years to 50 years it would cost £1.3m per annum.

61. It is normally prudent to borrow long term to support the Capital Programme; however, we have had unusual market conditions that we have used to generate short-term savings. Those market conditions are forecast to continue to normalise gradually during the strategy term, however, the new normal is forecast to be much lower borrowing rates than in previous economic cycles. Also, 48% of the

Councils borrowings are for terms between 30 and 50 years, which brings certainty of cost and minimises interest rate risk on almost half the portfolio.

62. The Council's current Loans and Investment portfolios are shown in **Appendix C.**

Transfer of Loans between Debt Pools

63. The Council's policy on transferring loans between the HRA and GF debt pools is as follows: -

    - In the case of the HRA/GF having a requirement to fund its CFR, then one debt pool may be used to subsidise another to reduce either the GF or the HRA external borrowing requirement.
    - If this happens, then loans will be transferred between the pools without the need to recognise an internal premium or discount.
    - Similarly, if the HRA and GF wish to swap loans as a result of strategic decisions, this loan swap would also be undertaken at no internal premium or discount.

64. Where the HRA or GF has surplus cash balances, which allow either account to fund internal, the rate charged on this internal borrowing will be based on the average external rate of interest on the applicable pool at the end of the financial year. This is a reasonable approach providing certainty of charging, protection against short-term increases in market rates and reflects the fact that strategic borrowing decisions will generally be made on an annual basis.

Policy on Borrowing in Advance of Need

65. 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. At present, the Council does not borrow in advance.

66. Borrowing in advance will be made within the constraints that: -

    - It will be limited to no more than 100% of the expected increase in borrowing need (CFR) over a three year planning period; and
    - Would not look to borrow more than 36 months in advance of need.

67. 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.

Debt Rescheduling

68. Any rescheduling activity will be reported in the next Finance and Performance Improvement Report to Cabinet.

Approved Sources of Long and Short term Borrowing

69. The Chief Financial Officer, under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time taking into account the relevant risks. It is likely shorter term fixed rates may provide lower cost opportunities in the short to medium term.

70. Our advisors will keep us informed as to the relative merits of available funding sources.

Annual Investment Strategy

Investment Policy

71. The Council's investment policy has regard to the Government MHCLG's Guidance on Local Government Investments ("the Guidance"), the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the CIPFA Code") and the CIPFA Treasury Management Guidance Notes 2018. The Council's investment priorities will be security first, portfolio liquidity second, then return.

72. In order to minimise the risk to investments, the Council has stipulated the minimum acceptable credit quality of financial institutions for inclusion on its lending list. The methodology used to create the lending list takes account of the ratings and watches published by all three ratings agencies, Fitch, Moody's and Standard & Poor's, with a full understanding of what the ratings reflect in the eyes of each agency. Using the Link Asset Services Treasury Solutions, ratings service, banks' ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications.

73. The aim of the policy is to generate a list of highly creditworthy financial institutions/products, which will also enable diversification, and thus avoidance of concentration risk.

74. The primary intention of the policy is to provide security of investment and minimisation of risk.

75. Where the HRA or GF has surplus cash balances invested the interest shall be credited based on the relative proportions of the balances. Where an investment is impaired, the charge shall also be shared based on the relative proportions of the balances.

76. Investment instruments identified for use within the financial year are listed in **Appendix E** under the "Specified" and "Non-specified" investment categories.

77. The MHCLG Guidance defines Specified Investments as those: -

    - Denominated in sterling;
    - Due to be repaid within 12 months of the arrangement;
    - Not defined as Capital Expenditure by legislation and invested with one of:-

        I. The UK Government
        II. A UK local authority, parish council, or community council, or
        III. A body or investment scheme of "high credit quality"

78. Non-Specified Investments are any that do not meet the above criteria.

79. The above criteria is unchanged from last year.

Credit Risk Policy

80. The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating equal to the UK's sovereign rating (minimum rating as confirmed by at least two agencies). The list of countries that qualify using this credit criteria as at the date of this report are shown in **Appendix E**. This list will be amended by officers should ratings change in accordance with this policy. Any changes will be approved by the Chief Financial Officer. Not all counterparties will be active in the market at all times, therefore, it is important to have a good spread of available organisations.

81. The Council applies the credit risk assessment service provided by Link Asset Services Treasury Solutions.

82. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies. The credit ratings of financial institutions are supplemented with the following overlays: -

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

83. The end product of this is a series of bands, which indicate the relative creditworthiness of financial institutions. This is used by the Council to determine the duration of investments. The model will also be used to select institutions with a high level of creditworthiness, based on the following bands. The Council will therefore use financial institutions within the following durational bands.

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour

Colour	Maximum Term
Yellow	5 Years
Dark pink	5 years for Enhanced money market funds (EMMFs) with a credit score of 1.25
Light Pink	5 years for Enhanced money market funds (EMMFs) with a credit score of 1.5
Purple	2 Years
Blue	1 year (applies to nationalised or semi nationalised UK Banks)
Orange	1 Year
Red	6 Months
Green	100 Days
No Colour	Not to be used

84. **Appendix E** contains a table showing the relative credit worthiness of different financial institutions, maximum terms and maximum investment limits.

85. This methodology is even more cautious than the approach suggested by CIPFA of using the lowest rating from all three rating agencies to determine creditworthy financial institutions. The Link Asset Services Treasury Solutions, creditworthiness service uses a wider array of information in addition to the primary ratings and by using a risk weighted scoring system, does not give undue weighting to one agency's ratings.

86. Typically the minimum credit ratings criteria the Council use will be a short term rating (Fitch or equivalents) of F1 and a long-term rating of A-. There may be occasions when another rating agency's counterparty ratings may be used that are marginally lower than Fitch's counterparty ratings but in such instances consideration will be given to the whole range of ratings available or other topical market information, to support their use.

87. All credit ratings are monitored daily and changes to ratings are notified to us by Link Asset Services Treasury Solutions, creditworthiness service.

88. If a downgrade results in the financial institution / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.

89. In addition to the use of credit ratings the Council will be advised of information in movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

UK banks – ring-fencing

90. The largest UK banks, (those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits), were 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". Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up. Several banks are very close to the threshold already and so may come into scope in the future regardless.

91. 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.

92. While the structure of the banks included within this process may have changed, the fundamentals of credit assessment have 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.

Investment Strategy

93. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

94. The bank rate is currently 0.1% and forecast to stay at 0.1% until at least March 2024.

95. The suggested budgeted investment earnings rates for returns on investments placed for periods of up to 3 months during each financial year for the next 3 years are as above. These rates, plus a small margin to stretch performance, have been used to estimate investment interest, over the strategy term.

96. The Council will pursue value for money with its investments and to measure this will use the 7 day London Interbank Bid Rate (LIBID) as its investment benchmark. We will also continue to use the investment benchmarking service offered by Link Asset Services Treasury Solutions, to compare our performance against our peers.

97. The overall balance of risks to economic growth in the UK is probably to the downside due to the weight of all the uncertainties over Brexit, as well as a softening global economic picture.

98. The balance of risks to increases in Bank Rate and shorter-term PWLB rates are broadly similarly to the downside. The Bank of England's forward guidance should be a good indicator of where interest rates are going.

99. To bring balance to the portfolio funds generated through the Council's cash flow will be invested on the following basis:-

Liquid Funds (approx. £15m)

100. This part of the portfolio should be managed at around £15m. This allows for the payment of payroll on dates within the year when grants are delayed due to the 15th being on a weekend (May 2021, August 2021and January 2022).

101. For example, this part of the portfolio should be invested in: -

- bank deposits (main accounts, call accounts, notice accounts); and
- potentially Money Market Funds (subject to due diligence and selection process).

Other Specified Investments (approx. £25m)

102. Once the liquid funds are in place the Council should continue to invest in other slightly less liquid but still secure assets, up to a maximum of 1 year. Examples of these assets are: -

- UK Government Treasury Bills, which will have a maturity date of less than 6 months (the maximum term).
- High quality Certificates of Deposit (rank equally with bank deposits re: bail in) which provides access to a wider range of higher rated banks.
- High quality bonds issued by banks, with a maturity date of less than 1 year.
- Other Corporate Bonds that meet its minimum investment criteria, with a maturity of less than 1 year.
- Collateralised Deposits (repurchase/Reverse Repurchase) arrangements utilising its existing custodial arrangements with King & Shaxson brokers. This is a method of secured deposit with a bank.

103. Repo/Reverse Repo is accepted as a form of securitised lending and should be based on the GMRA 2000 (Global Master Repo Agreement). Should the counterparty not meet our senior unsecured rating then a 102% collateralisation would be required. The acceptable collateral is as follows:

  - Index linked Gilts
  - Conventional Gilts
  - UK Treasury bills
  - Corporate bonds

Non-Specified Investments (Maximum £20m)

104. Any core funds that are identified as being available longer term, e.g. reserves, could continue to be invested in suitable longer term assets, examples of which are: -

- fixed deposits with banks in excess of 12 months.
- High quality Certificates of Deposit with a maturity date in excess of 12 months.
- High quality bonds issued by banks, with a maturity date in excess of 12 months.

- Other Corporate Bonds that meet the Councils minimum investment criteria, with a maturity in excess of 12 months.

105. A full list of Specified and Non-Specified investments is shown in **Appendix E.**

106. Any new Non-Specified investment will require authorisation by the Chief Financial Officer. Details of minimum criteria and any additional due diligence required can also be seen in **Appendix E**.

107. 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.

	Maximum principal sums invested > 1 year			
£m	**2021/22**	**2022/23**	**2023/24**	**2024/25**
Principal sums invested > 1 year	£20m	£20m	£20m	£20m

End of year investment report

108. At the end of the financial year, the Council will report on its investment activity as part of the Quarter 4 Finance and Performance Improvement Report

Policy on the use of external service providers

109. 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.

110. 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.

OPTIONS CONSIDERED

111. Other options that have been considered and members need to be aware of, when compiling this report, that would affect the investments and borrowing decisions are as follows: -

Options	Likely impact on Income and Expenditure	Likely impact on risk management
1. Invest in a narrower range of institutions and shorter terms	Interest income will be lower	Reduced risk of losses from credit related defaults, but any single loss could be magnified.
2. Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income. Premium to be paid if debt paid down (avoided if the reduction is done, as planned, by not replacing maturing debt).	Reduced investment balance leading to a lower impact in the event of default, however long term interest costs become less certain.
3. Borrow additional sums at long term fixed interest rates	Debt interest costs will rise, this is unlikely to be offset by higher investment income	Reduced interest rate risk. But higher investment balance could lead to a higher impact in the event of a default.

Options	Likely impact on Income and Expenditure	Likely impact on risk management
4. Increase level of borrowing	Additional cost of debt interest is likely to exceed additional investment income received.	Under-borrowing uses a combination of reserves and working capital. Any adverse changes to either could lead to cash not being available to fund expenditure. Leading to increased levels of borrowing.
5. Borrow sufficient funds for under-borrowed position	Additional interest costs of up to £1.3m per annum. It should be noted that a proportion of the under-borrowed position has been used to prepay the pension contribution recently.	Reduced interest rate risk, but significantly higher costs. In addition the higher investment balance could lead to a higher impact in the event of a default.

REASONS FOR RECOMMENDED OPTION

112. Option 1 is the recommended option to maximize external interest savings without introducing unacceptable risk.

113. The strategy provides a good balance between our existing, predominantly long maturity profile, to produce additional savings to support front line budgets and service provision. Remaining under-borrowed also reduces the risk of losses from failed investments.

IMPACT ON THE COUNCIL'S KEY OUTCOMES

	Outcomes	Implications
	Doncaster Working: Our vision is for more people to be able to pursue their ambitions through work that gives them and Doncaster a brighter and prosperous future; • Better access to good fulfilling work • Doncaster businesses are supported to flourish • Inward Investment	Treasury Management impacts on all the outcomes; it makes sure that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet the Council's activities.
	Doncaster Living: Our vision is for Doncaster's people to live in a borough that is vibrant and full of opportunity, where people enjoy spending time; • The town centres are the beating heart of Doncaster • More people can live in a good quality, affordable home • Healthy and Vibrant Communities through Physical Activity and Sport • Everyone takes responsibility for keeping Doncaster Clean • Building on our cultural, artistic and sporting heritage	
	Doncaster Learning: Our vision is for learning that prepares all children, young people and adults for a life	

	Outcomes	Implications
	that is fulfilling; • Every child has life-changing learning experiences within and beyond school • Many more great teachers work in Doncaster Schools that are good or better • Learning in Doncaster prepares young people for the world of work	
	Doncaster Caring: Our vision is for a borough that cares together for its most vulnerable residents; • Children have the best start in life • Vulnerable families and individuals have support from someone they trust • Older people can live well and independently in their own homes	
	Connected Council: • A modern, efficient and flexible workforce • Modern, accessible customer interactions • Operating within our resources and delivering value for money • A co-ordinated, whole person, whole life focus on the needs and aspirations of residents • Building community resilience and self-reliance by connecting community assets and strengths • Working with our partners and residents to provide effective leadership and governance	

RISKS AND ASSUMPTIONS

114. This strategy report along with the Council's Treasury Management Practice Statements seeks to limit as far as possible the risks associated with the Council's Treasury function. However, the economic climate and financial markets are dynamic, and, can be prone to sharp unexpected movements. The Chief Financial Officer and the Council's advisors will continually monitor the environment and act as necessary to limit risk and achieve best value for the Council.

115. Key risks and the actions taken to mitigate those risks are: -

    a. The Council could be unable to borrow when funding is required due to adverse market conditions and/or budgetary restraints. This risk is mitigated by maintaining sufficient easily accessible funds. Further mitigating actions could be scaling back or re-profiling capital expenditure plans if necessary.

    b. There could be an increased use of reserves and working capital which is currently used to finance the under borrowed position. This risk is mitigated by regular monitoring of the use of reserves and having a robust cash flow forecast, which is monitored on a daily basis.

c. Interest rates for borrowing could be higher than forecast. This risk is mitigated by regular monitoring of economic forecasts, consulting with the Council's treasury advisers and reducing the borrowing term. Other sources of borrowing will also be identified if possible.

d. The Council could receive a lower than forecast return on its investments. This risk is mitigated by regular monitoring of economic forecasts, consulting with the Council's treasury advisers and regular benchmarking. Investment strategies would then be adjusted by the Chief Financial Officer, as appropriate.

e. An institute with whom the Council has investments could become insolvent. This risk is mitigated by only investing in financial institutions that meet the Council's minimum criteria. The Council will also continually monitor the credit ratings of approved institutions and spread investments across a number of financial institutions and assets.

f. A financial institution may not repay an investment at maturity date due to an administration error (not insolvency). This is mitigated by maintaining accurate records of all investments placed, including confirmation from the counterparty. Adequate borrowing sources are available to cover any temporary cashflow shortfalls. In addition a proportion of the investments placed will always be instantly accessible.

LEGAL IMPLICATIONS [Officer Initials SRF Date 27/01/21]

116. The Council's Treasury Management activities are regulated by a variety of professional codes, statutes and guidance: -

  a. Chapter 1 Part 1 of the Local Government Act 2003 (the Act) provides the powers to borrow as well as providing controls and limits on such capital finance and accounts;
  b. the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended, develops the controls and powers within the Act;
  c. the Regulations require local authorities to have regard to the code of practice entitled the Prudential Code for Capital Finance in Local Authorities published by CIPFA when determining their affordable borrowing limit;
  d. the Regulations also require local authorities to operate its overall treasury function having regard to the code of practice contained in the document entitled Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes published by CIPFA;
  e. the Regulations require local authorities, for each financial year, to make a minimum revenue provision, which they consider to be prudent, in respect of the financing of capital expenditure incurred in that and previous years.

117. The Treasury Management function is included in the Chief Financial Officer's duties under Section 151 of the Local Government Act 1972 to administer the Council's financial affairs.

FINANCIAL IMPLICATIONS [Officer Initials RI Date 05/02/21]

118. The treasury management budget required for 2021/22 has been reviewed and analysed over the following headings: -

	General Fund £'m
Costs	
Total Borrowing Costs	6.434
Other treasury management expenditure	0.089
Total Costs	**6.523**
Income	
Investment Interest	-0.615
Net Costs	**5.908**

119. The 2020/21 general fund budget was £6.148m for Treasury Management and after £0.240m of savings that have been included in the 2021/22 revenue budget proposals, the £5.908m referenced in the above table is available for these costs. The HRA interest costs are included in the separate HRA budget report that will be presented to Full Council in March 2021. Specific financial information is contained in the body of the report.

HUMAN RESOURCES IMPLICATIONS [Officer Initials KG Date 05/02/2021]

120. There are no specific Human Resources implications to this report

TECHNOLOGY IMPLICATIONS [Officer Initials…PW Date…27/01/21]

121. There are no technology implications in relation to this report.

HEALTH IMPLICATIONS [Officer Initials RS Date 27/01/2021]

122. Treasury management is unlikely to have direct health impacts. However both the borrowing and the investment strategies should take account of any indirect or unintended health impacts. These may arise from investing or borrowing in or from ventures that themselves have health impacts or are linked with other organisations that impact health. The most obvious case is that the council should protect its tobacco control work from the commercial and vested interests of the tobacco industry by not accepting any partnerships, payments, gifts and services, monetary or in kind or research funding offered by the tobacco industry.

EQUALITY IMPLICATIONS [Officer Initials: RS Date: [27/01/2021]

123. The Council must consider and have due regard to the three aims of the general equality duty, when developing and implementing the Treasury Management Strategy. By ensuring that the Treasury Management function is effective we can ensure that the right resources are available at the right time to enable the delivery of services. The equality implications for the revenue and capital budgets are detailed in the respective reports within the agenda papers.

CONSULTATION

124. The Council obtains advice from specialist organisations in respect of its treasury management activities. The impact of this is then assessed for its effect on the Council and appropriate action taken as necessary. Consultation has taken place with key financial managers and Executive Board.

125. This report has significant implications in terms of the following: -

Procurement		Crime & Disorder	
Human Resources		Human Rights & Equalities	
Buildings, Land and Occupiers		Environment & Sustainability	
ICT		Capital Programme	X

BACKGROUND PAPERS

C.I.P.F.A. Code of Practice on Treasury Management (Revised 2017).

C.I.P.F.A. Treasury Management in the Public Services Guidance Notes 2018.

C.I.P.F.A. Prudential Code for Capital Finance in Local Authorities (Revised 2017).

Localism Act 2011.

MHCLG Statutory Guidance Local Government Investments (3rd edition), April 2018.

The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2010 [SI 2010/454].

GLOSSARY OF ACRONYMS AND ABBREVIATIONS

Below is a list of all acronyms and abbreviations used throughout the report and their meaning in full.

MRP – Minimum Revenue Provision

CIPFA - Chartered Institute of Public Finance and Accountancy

CFR – Capital Financing Requirement

PFI – Private Finance Iniative

PPP – Purchasing Power Parity

PWLB – Public Works Loan Board

MHCLG - Ministry of Housing, Communities and Local Government

HRA – Housing Revenue Account

GF – General Fund

CDS – Credit Default Swaps

NRFB – Non Ring-Fenced Bank

LIBID – London Inter Bank Bid Rate

GMRA – Global Master Repurchase Agreement

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APPENDIX A

THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2020/21 – 2024/25

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.

Capital Expenditure	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
£m	**Actuals**	**Estimates**				
Adults, Health & Wellbeing	7,150	5,995	7,527	4,982	4,982	4,982
Finance & Corporate	10,386	7,614	21,127	13,792	12,850	12,500
Learning & Opportunity – Children	7,063	7,356	8,728	9,617	4,912	0
Economy & Environment	41,495	43,410	38,426	18,665	2,193	1,946
Non-HRA	**66,094**	**64,375**	**75,808**	**47,056**	**24,937**	**19,428**
HRA	**20,809**	**19,081**	**31,919**	**57,808**	**42,481**	**41,845**
TOTAL	**86,903**	**83,456**	**107,727**	**104,864**	**67,418**	**61,273**

Affordability prudential indicators

2) 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.

Ratio of financing costs to net revenue stream

3) 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	2024/25 Estimate
Non-HRA	4.60%	4.52%	3.60%	3.09%	2.81%	2.71%
HRA	16.92%	16.30%	16.10%	15.65%	14.99%	14.87%

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

HRA ratios

	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
HRA debt £k	266,063	266,422	279,410	295,410	311,410	327,410
HRA revenues £k	73,840	75,199	75,774	77,387	79,395	81,025
Ratio of debt to revenues %	27.75%	28.23%	27.12%	26.20%	25.50%	24.75%

	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
HRA debt £k	266,063	266,422	279,410	295,410	311,410	327,410
Number of HRA dwellings	20,108	20,043	19,980	19,860	19,740	19,620
Debt per dwelling £	13,232	13,293	13,984	14,875	15,776	16,688

Maturity Structure of Borrowing

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

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments;
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates;
- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing and are required for upper and lower limits.

£m	**2020/21**	**2021/22**	**2022/23**	**2023/24**	**2024/25**
Interest rate exposures					
	Upper	**Upper**	**Upper**	**Upper**	**Upper**
Limits on fixed interest rates based on net debt	100%	100%	100%	100%	100%
Limits on variable interest rates based on net debt	30%	30%	30%	30%	30%

Maturity structure of fixed interest rate borrowing 2021/22				
	Lower	**Upper**	**Actuals £k**	**Actuals %**
Under 12 months	0%	30%	108,690	20.65%
12 months to 2 years	0%	50%	55,101	10.47%
2 years to 5 years	0%	50%	27,000	5.13%
5 years to 10 years	0%	75%	16,621	3.16%
10 years and above	10%	95%	318,941	60.59%
Total			**526,353**	**100.00%**
Maturity structure of variable interest rate borrowing 2021/22				
	Lower	**Upper**	**Actuals £k**	**Actuals %**
Under 12 months	0%	30%	0	0
12 months to 2 years	0%	50%	0	0
2 years to 5 years	0%	50%	0	0
5 years to 10 years	0%	75%	0	0
10 years and above	10%	95%	0	0
Total			**0**	**0%**

APPENDIX B

Minimum Revenue Position (MRP) Policy Statement

1) The Council has an annual duty to charge an amount of MRP to the General Fund Revenue Account which it considers to be a prudent provision. The MRP charge is the means by which capital expenditure which has been funded by borrowing is paid for by council tax payers. The guidance on MRP allows different options for the calculation of MRP as below:

- Regulatory method
- CFR method
- Asset Life method, using either
    - Equal instalment method
    - Annuity method
- Depreciation method

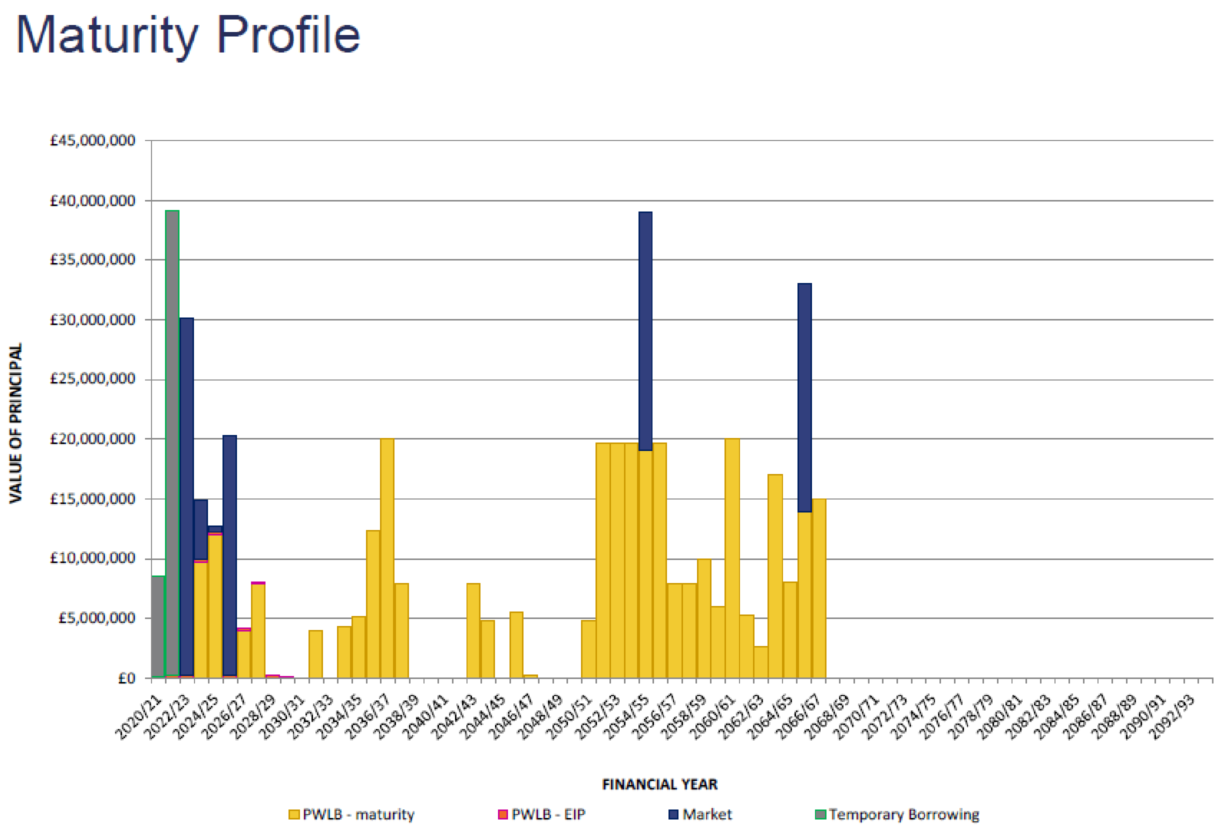
<u>Doncaster Council 2021/22 MRP Policy</u>

2) The Council adopts the most appropriate method of calculating and charging MRP for the specific asset. Methods used include either:
    - **Asset Life method – Equal instalment method** (option 3a); or
    - **Asset Life method - Annuity method** (option 3b); or
    - **Depreciation method** (option 4).

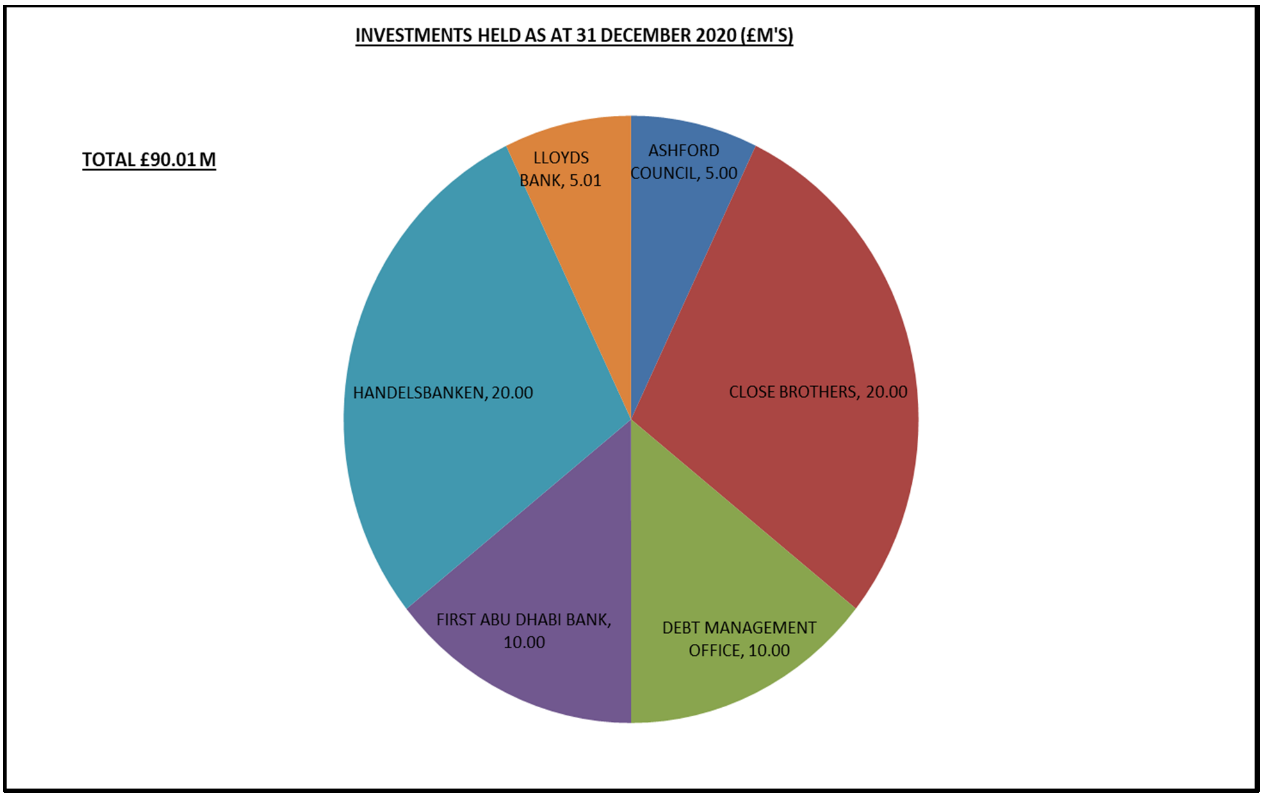
3) **MRP Overpayments** - A change introduced by the revised MHCLG MRP Guidance was the allowance that any charges made over the statutory minimum revenue provision (MRP), voluntary revenue provision or overpayments, can, if needed, be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. Up until the 31st March 2021, the total MRP overpayments are estimated to be £29.98m. It is proposed in the Revenue Budget 2020/21 – 2022/23 Report to utilise £8.2m over the next three years.

APPENDIX C

Analysis of Debt as at 31/12/20



Analysis of Investments as at 31/12/20



Interest Rate Forecasts

1) The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Link provided the following forecasts on 11.8.20. However, following the conclusion of the review of PWLB margins over gilt yields on 25.11.20, all forecasts below have been reduced by 1%. These are forecasts for certainty rates, gilt yields plus 80bps:

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

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. These forecasts were based on an assumption that a Brexit trade deal would be agreed by 31.12.20: as this has now occurred, these forecasts do not need to be revised.

Gilt yields / PWLB rates

3) There was much speculation during the second half of 2019 that bond markets were in a bubble which 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 thirty 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. The other side of this coin is that bond prices are elevated as investors would be expected to be moving out of riskier assets i.e. shares, in anticipation of a downturn in corporate earnings and so selling out of equities.

4) Gilt yields had therefore already been on a generally falling trend up until the coronavirus crisis hit western economies during March 2020. After gilt yields spiked up during the financial crisis in March, we have 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 i.e. 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: this also acted to put downward pressure on government bond yields at a time when there has been a huge and quick expansion of government expenditure financed by issuing 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.

5) 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. From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and 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 crisis and the quantitative easing operations of the Bank of England: indeed, gilt yields up to 6 years were negative during most of the first half of 20/21. 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. *(Please note that Link has concerns over this approach, as the fundamental principle of local authority borrowing is that borrowing is a treasury management activity and individual sums that are borrowed are not linked to specific capital projects.)* 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)

- As a consequence 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 25.11.20, 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)

- **Borrowing for capital expenditure.** As Link's long-term forecast for Bank Rate is 2.00%, and all PWLB rates are under 2.00%, there is now value in borrowing from the PWLB for all types of capital expenditure for all maturity periods, especially as current rates are at historic lows. However, greater value can be obtained in borrowing for shorter maturity periods so the Council will assess its risk appetite in conjunction with budgetary pressures to reduce total interest costs. Longer-term borrowing could also be undertaken for the purpose of certainty, where that is desirable, or for flattening the profile of a heavily unbalanced maturity profile.

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

APPENDIX E

TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT OPTION 1

SPECIFIED INVESTMENTS: All such investments will be sterling denominated, with maturities up to maximum of 1 year, meeting the minimum ‘high’ quality criteria where applicable.

NON-SPECIFIED INVESTMENTS: These are any investments which do not meet the specified investment criteria. A maximum of 30% of the investment pool 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:

SPECIFIED INVESTMENTS:

(All such investments will be sterling denominated, with maturities up to maximum of 1 year, meeting the minimum ‘high’ rating criteria where applicable)

	Minimum ‘High’ Credit Criteria	Maximum % of total investments or maximum Amount per institution	Max. maturity period
Term deposits and other instruments with local authorities	N/a	£30m (maximum of £5m per authority)	12 months
Term deposits with banks and building societies	Yellow Purple Orange Red Green No Colour	£50m £40m £30m £20m £10m nil	12 months 12 months 12 months 6 months 100 days Not for use
Term Deposits with UK part nationalised banks	Blue	£30m	12 months
Certificates of Deposit or corporate bonds with banks and building societies	Yellow Purple Orange Blue Red Green No Colour	£50m £40m £30m £30m £20m £10m nil	12 months 12 months 12 months 12 months 6 months 100 days Not for use
Bonds issued by multilateral development banks	UK sovereign rating	100%	12 months
UK Government Gilts	UK sovereign rating	100%	12 months
UK Government Treasury Bills	UK sovereign rating	100%	6 months
Debt Management Agency Deposit Facility	--	100%	6 months

	Minimum 'High' Credit Criteria	Maximum % of total investments or maximum Amount per institution	Max. maturity period
Collateralised deposit (Reverse Repurchase) (see note 2)	UK sovereign rating	100%	12 months
Bond issued by a financial institution which is explicitly guaranteed by the UK Government e.g. National Rail	UK sovereign rating	100%	12 months
Sovereign bond issues (other than the UK govt)	UK sovereign rating	100%	12 months
Collective Investment Schemes structured as Open Ended Investment Companies (OEICs): -			
Government Liquidity Funds	AAA MMF rating	100%	Liquid
Money market funds (CNAV/LVNAV or VNAV)	AAA MMF rating	100%	Liquid
Enhanced Cash Funds with a credit score of 1.25	Fitch rating Short term F1, long Term A- or equivalent	100%	Liquid
Enhanced Cash Funds with a credit score of 1.5	Fitch rating Short term F1, long Term A- or equivalent	100%	Liquid
Bond Funds	Fitch rating Short term F1, long Term A- or equivalent	100%	Liquid
Gilt Funds	Fitch rating Short term F1, long Term A- or equivalent	100%	Liquid

Note 1. If forward deposits are to be made, the forward period plus the deal period should not exceed one year in aggregate.

N.B. buy and hold may also include sale at a financial year end and repurchase the following day in order to accommodate the requirements of the Accounting Code of Practice.

Note 2. As collateralised deposits are backed by collateral such as UK Gilts, corporate bonds, etc. this investment instrument is regarded as being a AA rated investment as it is equivalent to lending to the UK Government.

Accounting treatment of investments. The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this 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 30% will be held in aggregate in non-specified investment

Maturities in excess of 1 year

	Minimum 'High' Credit Criteria	Maximum % of total investments or maximum Amount per institution	Max. maturity period
Term deposits and other instruments with local authorities	N/a	£20m (maximum of £5m per authority)	5 years
Term deposits with banks and building societies	Yellow Purple	£50m £40m	5 years 2 years
Term Deposits with UK part nationalised banks	Blue	£30m	5 years
Certificates of Deposit or corporate bonds with banks and building societies	Yellow Purple	£50m £40m	5 years 2 years
Bonds issued by multilateral development banks	UK sovereign rating	£5m	5 years
UK Government Gilts	UK sovereign rating	100%	50 years
Collateralised deposit (Reverse Repurchase)	UK sovereign rating	100%	5 years
Bond issuance issued by a financial institution which is explicitly guaranteed by the UK Government e.g. National Rail	UK sovereign rating	£20m	10 years
Commercial Paper Other	Fitch rating Short term F1, long Term A- or equivalent	£20m	10 years
Corporate Bonds	Fitch rating Short term F1, long Term A- or equivalent	£20m	10 years
Sovereign bond issues (other than the UK govt)	UK sovereign	£20m	5 years
Bond Funds	Fitch rating Short term F1, long Term A- or equivalent	£20m	10 years
Gilt Funds	Fitch rating Short term F1, long Term A- or equivalent	£20m	10 years
Municipal Bonds	UK sovereign rating	£5m	5 years
Floating Rate Notes	Fitch rating Short term F1, long Term A- or equivalent	£5m	5 years
Covered Bonds	Fitch rating Short term F1, long Term A- or equivalent	£5m per bond	10 years
Unrated Bonds	**Non-rated internal due diligence	£5m per bond	10 years

	Minimum 'High' Credit Criteria	Maximum % of total investments or maximum Amount per institution	Max. maturity period
Loans to Third Parties	**Non-rated internal due diligence	£5m	50 years
Churches, Charities and Local Authorities (CCLA) Property Fund	**Non-rated internal due diligence	£5m	10 years
Property Funds*	**Non-rated internal due diligence	£5m	10 years

*The use of these instruments can be deemed capital expenditure and as such will be an application (spending) of capital resources. This Authority will seek guidance on the status of any fund it may consider using. Appropriate due diligence will also be undertaken before investment of this type is undertaken.

**Due Diligence will include the following, if available, however the list isn't intended to be exhaustive: -

Capitalisation of the organisation,

Revenue profits and margin trends,

Competitors and industry,

Valuation multiples e.g. price/earnings ratio,

Management and share ownership and track records,

Balance sheet analysis,

Examination of future plans and expectations,

Stock options and dividend policy.

APPROVED COUNTRIES FOR INVESTMENTS

This list is based on those countries which have higher sovereign ratings than the UK (based on two out of three ratings from the agencies Fitch, Moody's and S&P) and have banks operating in sterling markets which have credit ratings of green or above in the Link Asset Services Treasury Solutions credit worthiness service. The UK is currently rated as AA- but is still an approved country for investments.

AAA	**AA+**	**AA**
Australia, Denmark, Germany	Finland	Abu Dhabi (UAE)
Luxembourg, Netherlands,	Canada	France
Norway, Singapore, Sweden		
Switzerland, USA		