

ISLE OF ANGLESEY COUNTY COUNCIL	
REPORT TO:	AUDIT COMMITTEE
DATE:	11 FEBRUARY 2020
SUBJECT:	TREASURY MANAGEMENT STRATEGY STATEMENT 2020/21
LEAD OFFICER:	MARC JONES, DIRECTOR OF FUNCTION (RESOURCES AND SECTION 151 OFFICER
CONTACT OFFICER:	JEMMA ROBINSON, SENIOR ACCOUNTANT (TEL: EXT 2675)
Nature and reason for reporting For scrutiny - consistent with professional guidance.	

1. This report is presented to ensure that the Council is implementing best practice in accordance with the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice for Treasury Management. The code recommends that prior to being presented for adoption, members should scrutinise the Treasury Management Strategy Statement (which includes the Annual Investment Strategy, the annual MRP Policy Statement, the annual Treasury Management Policy Statement and the Treasury Management Scheme of Delegation). This Authority's scheme of delegation charges the Audit & Governance Committee with this function.
2. The CIPFA Code of Practice on Treasury Management (Section 7) recommends that the Authority's Treasury Management Practices (TMPs) should be approved, documented and monitored. It goes on to state that the nature and extent of the involvement of an organisation's responsible body in approving and monitoring its TMPs and accompanying schedules is a matter for local decision and recognises that in some organisations this may be delegated to the responsible officer. In all cases, it should be subjected to scrutiny by the responsible body following recommendations by the responsible officer. This Authority has produced documented TMPs, and were approved by the Audit Committee on 6 December 2016.
3. In terms of updates to the Treasury Management Strategy Statement, there are no proposed amendment to the core principals and policies of the 2019/20 Statement.
4. Under the revised Code of Practice, it is a requirement that the Council prepares a Capital Strategy, which takes a longer-term view as to the capital investment that is required and how that investment will be funded. The Executive will approve this Strategy, along with other budget resolutions. This Treasury Management Strategy sits below the Capital Strategy, and considers the impact of that strategy on the Council's borrowing and investments. It sets out how both strategies will be undertaken in a controlled way, which is in line with a suitable level of risk that the Council wishes to take, bearing in mind the guidance set out in the CIPFA Code of Practice on Treasury Management.
5. **Recommendations**
 - To consider the Treasury Management Strategy for 2020/21 and to make recommendations or note comments for consideration by the Executive Committee.

TREASURY MANAGEMENT STRATEGY STATEMENT

ANNUAL INVESTMENT STRATEGY, MINIMUM REVENUE PROVISION POLICY STATEMENT AND TREASURY MANAGEMENT POLICY STATEMENT 2020/21

1. BACKGROUND

1.1. 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.”

The Treasury Management Policy Statement defines the policies and objectives of the treasury management activities (see **Appendix 1**).

1.2. 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 with counterparties which meet the criteria in terms of security, liquidity and investment return as set out in this strategy.

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

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

2. CIPFA CODE OF PRACTICE ON TREASURY MANAGEMENT

2.1. The CIPFA Code of Practice on Treasury Management requires the Council to prepare and approve the following documents:-

- A Capital Strategy Statement which sets out a high level, long term overview of capital expenditure and financing, along with details on any associated risks and how they will be managed.
- A Treasury Management Strategy which sets out the Council’s strategy in terms of borrowing and investment which follows on from the Capital Strategy, sets out the constraints on borrowing, determines a set of prudential indicators and determines the Council’s risk appetite and strategy in respect of investments.

- 2.2. The key principles of the CIPFA Treasury Management Code of Practice are set out in Appendix 2.

3. EXTERNAL CONTEXT

- 3.1. Setting the Treasury Management Strategy cannot be undertaken in isolation, and consideration must be given to the economic situation as this has an impact on investment interest rates, the cost of borrowing and the financial strength of counterparties. A full summary of the economic outlook is set out in **Appendix 3**, but the main points to consider are as follows:-
- Weakening economic growth in the US, China and the Eurozone.
 - Inflation in the UK is likely to remain close to or under 2% over the next two years.
 - A potential for interest rates rises from March 2021 onwards.
 - Continuing uncertainty surrounding Brexit and its impact on the UK and Eurozone economy.
 - Investment returns are likely to remain low during 2020/21 with little increase in the following two years.
- 3.2. Having considered the available information and having considered the advice from the Council's Treasury Management Advisors, the following table sets out the Council's view on interest rate levels for the following 3 years:-

Table 1
Prospects for Interest Rates to March 2023

Annual Average	Bank Rate (%)	PWL B Borrowing Rates (including certainty rate adjustment)		
		5 year	25 year	50 year
December 2019	0.75	2.30	3.20	3.10
March 2020	0.75	2.40	3.30	3.20
June 2020	0.75	2.40	3.40	3.30
September 2020	0.75	2.50	3.40	3.30
December 2020	0.75	2.50	3.50	3.40
March 2021	1.00	2.60	3.60	3.50
June 2021	1.00	2.70	3.70	3.60
September 2021	1.00	2.80	3.70	3.60
December 2021	1.00	2.90	3.80	3.70
March 2022	1.00	2.90	3.90	3.80
June 2022	1.25	3.00	4.00	3.90
September 2022	1.25	3.10	4.00	3.90
December 2022	1.25	3.20	4.10	4.00
March 2023	1.25	3.20	4.10	4.00

Information provided by Link Asset Services is attached as **Appendix 4**.

- 3.3. Given the forecast for bank base rates, the following rates of return on investments are expected during the financial years:-

2019/20: 0.75%;
 2020/21: 0.75%;
 2021/22: 1.00%;
 2022/23: 1.25%;
 2023/24: 1.50%;
 2024/25: 1.75%;
 2025/26 Onwards: 2.25%.

4. THE COUNCIL'S CURRENT POSITION

4.1. Borrowing

4.1.1. The Council's current external borrowing is set out in Table 2 below. A full analysis is attached as **Appendix 5**.

Table 2
Summary of the Council's Current Outstanding Loans

PWLB LOANS							
	PWLB / PWLB Maturity	PWLB EIP/ Annuity	Market Loans	PWLB Variable	Total Maturing		
Loan Outstanding	£126,184k	£220k	£0k	£0k	£126,404k		
Average life (years)	25.48	6.94	0.00	0.00	25.44		
Average rate (%)	5.15	9.44	0.00	0.00	4.73		
OTHER LOANS							
	Welsh Government	Salix Loan 1	Salix Loan 2	Salix Loan 3	Salix Loan 4	Salix Loan 5	Total
Outstanding Balance	£44k	£74k	£274k	£572k	£251k	£1,178k	£2,393k
Repayment Date	2020/21	2024/25	2025/26	2028/29	2029/30	2030/31	
Interest Rate (%)	0.00	0.00	0.00	0.00	0.00	0.00	

4.2. Investments

4.2.1. Any surplus cash is currently invested in short term deposit accounts, call accounts and with other UK local authorities. The balance invested in these accounts changes daily (balance as at 31 December 2019 was £23.2m).

4.2.2. Under the current treasury management strategy, the Council invests surplus cash ensuring first of all the security of the deposit, secondly the liquidity of the deposit and, finally, the return on the investment. In practice, in order to ensure the first and second principles, the rate of return on investments is sacrificed and the current average return on investments is 0.55% (as at 31 December 2019).

5. IMPACT OF FUTURE PLANS ON BORROWING

5.1. Capital expenditure is partly funded from borrowing and the capital programme, as set out in the Capital Strategy, is set out in Table 3 below:-

Table 3
Proposed Capital Expenditure Programme 2020/21 – 2022/23

	2020/21 £'000	2021/22 £'000	2022/23 £'000
Non - HRA	19,765	21,662	14,675
HRA	17,138	17,704	14,402
Commercial Activities / Non Financial Investment	0	0	0
TOTAL EXPENDITURE	36,903	39,366	29,077
Financed By			
Capital Grants	12,286	9,856	8,090
Capital Receipts	245	250	250
Reserves	0	750	0
Revenue	14,728	9,294	10,642
Balance Funded from Borrowing	9,644	19,216	10,095

- 5.2.** An important factor to consider is the impact of borrowing on the Council's Capital Financing Requirement (CFR). The CFR is the measure of the Council's underlying borrowing need. Borrowing is not limited to external borrowing from PWLB but also the use of the Council's own cash balances (internal borrowing) which have been used to fund capital expenditure.
- 5.3.** Capital expenditure will increase the CFR but only by the sum that is not funded from grants, capital receipts, reserves or revenue. The CFR will also reduce annually by the sum of the Minimum Revenue Provision (MRP) which is charged to revenue. The level of the CFR is an important measure to ensure that the Council does not commit itself to unaffordable levels of borrowing.
- 5.4.** In order to ensure that the Council has sufficient funds available to repay debt as it falls due, the Council is required to make a charge to the revenue account each year and this charge is known as the Minimum Revenue Provision. Regulations require that the Council approves a MRP statement in advance of each financial year. The policy for 2020/21 is set out in **Appendix 6**. The Council's MRP was substantially revised in 2018 but there are no changes from that revised policy for 2020/21. By making the MRP charge each year, the Council's cash balances are replenished and that, in turn, reduces the level of internal borrowing.
- 5.5.** The policy will provide an equal charge on borrowing up to 31 March 2018 and, for all borrowing after that date, the MRP charge will be based on the useful life of the asset which has been funded from borrowing, e.g. if £1m is borrowed to fund the capital expenditure on an asset that has an asset life of 20 years, the annual MRP in respect of that loan would be £50k per annum. As new borrowing is undertaken, it will increase the MRP charge over time and this increase in costs is allowed for in the Council's budgets.
- 5.6.** The impact of the Council's capital expenditure plans and the MRP charge on the CFR and level of external and internal borrowing is shown in Table 4 below:-

Table 4
Capital Financing Requirement and Borrowing 2019/20 to 2022/23

	2019/20 £'000	2020/21 £'000	2021/22 £'000	2022/23 £'000
Capital Financing Requirement				
Opening Balance of CFR	138,662	142,034	147,985	163,265
Capital Expenditure	33,126	36,903	39,366	29,077
External Capital Grants	(14,380)	(12,286)	(9,856)	(8,090)
Capital Receipts	(1,612)	(245)	(250)	(250)
Revenue Contribution & Reserves	(10,331)	(14,728)	(10,044)	(10,642)
Minimum Revenue Provision	(3,431)	(3,693)	(3,936)	(4,391)
CLOSING BALANCE OF CFR	142,034	147,985	163,265	168,969
External Borrowing				
Opening Balance of External Borrowing	132,549	129,257	134,093	152,944
Borrowing to Fund Capital Expenditure	2,001	9,644	19,216	10,095
Borrowing to Fund Loan Repayments	0	0	0	0
Borrowing to Replace Internal Borrowing	0	0	0	0
Loan Repayments	(5,293)	(4,808)	(365)	(2,651)
Closing Balance of External Borrowing	129,257	134,093	152,944	160,388
Internal Borrowing				
Opening Balance of Internal Borrowing	6,113	12,777	13,892	10,321
Replacement of Internal Borrowing	0	0	0	0
Funding Loan Repayments from External Borrowing	0	0	0	0
External Loan Repayments	5,293	4,808	365	2,651
Borrowing to Fund Capital Expenditure	4,802	0	0	0
Minimum Revenue Provision	(3,431)	(3,693)	(3,936)	(4,391)
Closing Balance of Internal Borrowing	12,777	13,892	10,321	8,581
TOTAL BORROWING	142,034	147,985	163,265	168,969

6. BORROWING STRATEGY

6.1. The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement) has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This approach is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered. As part of this strategy, the ability to externally borrow to repay the reserves and balances, if needed, is important. Table 4 indicates that £12.777m may need to be externally borrowed if urgently required. This is the amount of Council reserves and balances used in the past to fund the capital programme instead of taking out borrowing.

6.2. Against this background and the risks within the economic forecast, caution will be adopted with the 2020/21 treasury operations. The Section 151 Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:-

- if it was felt that there was a significant risk of a sharp FALL in long and short term rates (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered if it is cost effective to do so.
- If it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.
- Any decisions will be reported to this Committee at the next available opportunity.

6.3. External v Internal Borrowing

6.3.1. Current conditions indicate a need for a flexible approach to the choice between internal and external borrowing. Many of the factors which lay behind previous policies to externalise all borrowing remain valid, e.g.:-

- With a continuing historically abnormally low Bank Rate and PWLB rates, there remains a unique opportunity for local authorities to actively manage their strategy of undertaking new external borrowing.

6.3.2. However, it remains the case that there are certain limitations to this approach, as previously noted, e.g.:-

- The policy can cause exposure to credit risk (e.g. risk of the bank defaulting on the debt), so this aspect must be very carefully managed;
- Careful on-going consideration needs to be given to the difference between borrowing rates and investment rates to ensure the Council obtains value for money once an appropriate level of risk management has been attained to ensure the security of its investments.

6.3.3. In favour of internalisation, over the medium term, investment rates are expected to continue to be below long term borrowing rates. This means that value for money considerations would indicate that value could best be obtained by avoiding new external borrowing and by using internal cash balances to finance new capital expenditure, or to replace maturing external debt (this is referred to as internal borrowing). This would maximise short term savings.

6.3.4. However, short term savings by avoiding new long term external borrowing in 2020/21 must also be weighed against the potential for incurring additional long term extra costs, by delaying unavoidable new external borrowing until later years when PWLB long term rates are forecast to be higher. Additionally, the cash flow implications of internalising borrowing require regular review and will limit the potential extent of internalising borrowing.

6.4. Borrowing in Advance of Need

6.4.1. The Council will not borrow more than, or in advance of, its needs, solely 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.

6.4.2. In determining whether borrowing will be undertaken in advance of need, the Council will:-

1. ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need;
2. ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets, have been considered;
3. evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
4. consider the advantages and disadvantages of alternative forms of funding;
5. consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use; and
6. consider the impact of borrowing in advance on temporarily (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk, and other risks, and the level of such risks given the controls in place to minimise them.

6.4.3. 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.

6.5. Debt Rescheduling

6.5.1. Rescheduling of current borrowing in our debt portfolio is unlikely to occur as the 100 bps increase in PWLB rates in November 2019 only applied to new borrowing and not to premature debt repayment .

6.5.2. The reasons for any rescheduling to take place will include:-

- the generation of cash savings and/or discounted cash flow savings;
- helping to fulfil the treasury strategy; and
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

6.5.3. Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

6.5.4. All rescheduling will be reported to the Audit Committee at the earliest practicable meeting following its action.

6.6. Debt Profile

6.6.1. As can be seen from **Appendix 5**, the existing borrowing is due to be repaid in various years up to 2068/69. As part of any decision on future borrowing, the Council will aim to ensure that the repayment date is arranged so as to smooth out repayments as far as possible, but priority will be given to the interest rate payable when determining the type of loan (maturity or annuity) and the length of the loan.

7. INVESTMENT STRATEGY

7.1. In-house funds: 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). Greater returns are usually obtainable by investing for longer periods. While most cash balances are required in order to manage the ups and downs of cash flow where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed.

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

7.2. Management of Risk

7.2.1. CIPFA has extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with financial investments (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy (a separate report).

7.2.2. The Council's investment policy has regard to the following:-

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

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

1. Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.
2. **Other information:** ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration, the Council will engage with its advisors to maintain a monitor on market pricing such as "**credit default swaps**" and overlay that information on top of the credit ratings.

3. **Other information** sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.
4. This Authority has defined the list of **types of investment instruments** that the treasury management team are authorised to use. There are two lists in **Appendix 7** under the categories of 'specified' and 'non-specified' investments.
 - **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.
 - **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year and/or are more complex instruments which require greater consideration by Members and officers before being authorised for use.
5. **Non-specified investments limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments by ensuring that no non-specific investment is undertaken without the prior consent of the Council. The Council does not hold any non-specified investments, nor does it intend to during 2020/21 (see **Appendix 7**).
6. **Lending limits** (amounts and maturity) for each counterparty will be set through applying the matrix table as set out in the Creditworthiness section of this strategy.
7. **Transaction limits** are set for each type of investment in **Appendix 8**.
8. This Authority will set a limit for the amount of its investments which are invested for **longer than 365 days** (see **Appendix 11**).
9. Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating** (see **Appendix 9**).
10. This Authority has engaged **external consultants** to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this Authority in the context of the expected level of cash balances and need for liquidity throughout the year.
11. All investments will be denominated in **sterling**.
12. As a result of the change in accounting standards for 2019/20 under **IFRS 9**, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund.

7.3. Creditworthiness Policy

- 7.3.1. The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle, the Council will ensure that:-
 - It maintains a policy covering the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the specified and non-specified investment sections below; and
 - It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

- 7.3.2.** The Section 151 Officer will maintain a counterparty list in compliance with the criteria set out in **Appendix 8** and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to that which determines which types of investment instrument are either specified or non-specified as it provides an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.
- 7.3.3.** Credit rating information is supplied by Link Asset Services, our treasury consultants, on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating Watches (notification of a likely change), rating Outlooks (notification of the longer term bias outside the central rating view) are provided to officers almost immediately after they occur and this information is considered before dealing. For instance, a negative rating Watch applying to a counterparty at the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions.
- 7.3.4.** As an additional layer to the minimum credit rating criteria described above, this Council also employs the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:-
- Credit watches and credit outlooks from credit rating agencies;
 - Credit Default Swaps (CDS) spreads to give early warning of likely changes in credit ratings;
 - Sovereign ratings to select counterparties from only the most creditworthy countries.
- 7.3.5.** This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads from which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council, at the discretion of the Section 151 Officer, to assist in determining the duration for investments. The Council will, therefore, normally use counterparties within the following durational bands:-
- | | |
|--------------|----------------------------------------------------------------------|
| Yellow: | 5 years * |
| Dark pink : | 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.25 |
| Light pink : | 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.5 |
| Purple: | 2 years |
| Blue: | 1 year (only applies to nationalised or semi nationalised UK Banks) |
| Orange: | 1 year |
| Red: | 6 months |
| Green: | 100 days |
| No colour: | not to be used |
- 7.3.6.** The Link Asset Services creditworthiness service uses a wider array of information than just primary ratings and, by using a risk weighted scoring system, does not give undue preponderance to just one agency's ratings.
- 7.3.7.** Typically, the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances, consideration will be given to the whole range of ratings available, or other topical market information, to support their use.
- 7.3.8.** All credit ratings will be monitored daily. The Council is alerted to changes to ratings of all three agencies through its use of the Link Asset Services' creditworthiness service.

- If a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- In addition to the use of credit ratings, the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

7.3.9. Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information and information on any external support for banks to help support its decision making process.

7.3.10. 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". 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.

7.3.11. 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.

7.3.12. 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.

7.4. Country Limits

7.4.1. The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide). The list of countries that qualify using this credit criteria as at the date of this report are shown in **Appendix 9**. This list will be added to or deducted from by officers should ratings change in accordance with this policy.

8. GOVERNANCE AND CONTROL

8.1. The Prudential Code reflects a move towards self regulation for local authorities and effective corporate governance is one of the key elements to the successful implementation of the Code.

8.2. Corporate Governance includes the following elements:-

- A formal role for the Section 151 Officer;
- Setting and monitoring of Prudential and Treasury Indicators;
- A scheme of delegation and a process of formal approval;
- Reporting on Treasury Management matters to Members.

8.3. Role of the Section 151 Officer and Members

- 8.3.1.** The Section 151 Officer is responsible for ensuring that matters relating to Treasury Management and Capital Financing are taken into account and reported to the Executive / full Council for consideration and that procedures are established to monitor performance.
- 8.3.2.** The Section 151 Officer must ensure that prudential indicators are set and monitored in order to demonstrate the legislative requirement that the Council's financial plans are affordable.
- 8.3.3.** Members also play an important role in not just authorising the relevant decisions but also in scrutinising treasury management processes, decisions and performance. In order to undertake this role, 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. In order to support the scrutiny role of the members of the Audit and Governance Committee, the Committee's members received training in treasury management, delivered by the appointed treasury management consultants on 7 November 2019. Further training will be arranged when required. The training needs of treasury management officers are regularly reviewed and addressed.
- 8.3.4.** The Treasury Management Scheme of Delegation and a fuller explanation of the role of the Section 151 Officer is set out in **Appendix 10**.

8.4. Treasury Management Advice

- 8.4.1.** The Council uses Link Asset Services as its external treasury management advisors. In accordance with procurement regulations, the Treasury Management advisory service was advertised for tender for the period 1 April 2016 to 31 March 2019 with an option to extend for two years, with Link Asset Services (previously Capita Asset Services) being the successful tenders. The Council has exercised the option to extend for two years.
- 8.4.2.** The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers. Final responsibility for treasury management decisions remains with the Council.
- 8.4.3.** It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

8.5. Prudential and Treasury Indicators

- 8.5.1.** The Prudential and Treasury Indicators set out in **Appendix 11** cover affordability, prudence and sets out limits for capital expenditure, external debt and the structure of the debt. It is for the Council to set the Prudential Indicators and it is important to not just consider the indicators for each individual year in isolation but also to consider the past performance and the future forecasts. A fuller explanation of the purpose of each indicator is set out in **Appendix 12**.

8.6. Reporting

8.6.1. The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals. These reports are required to be adequately scrutinised by Committee before being recommended to the Council. This role is undertaken by the Audit and Governance Committee.

8.6.2. Prudential and Treasury Management Indicators and Treasury Strategy - the first and most important report (this report) covers:-

- the Treasury Management Strategy (how the investments and borrowings are to be organised) including treasury management indicators;
- an Investment Strategy (the parameters on how investments are to be managed);
- a Minimum Revenue Provision (MRP) Policy (how residual capital expenditure is charged to revenue over time);
- a Treasury Management Policy Statement (definition of the policies and objectives of the treasury management function); and
- the capital plans (including the associated prudential indicators).

8.6.3. A Mid-Year Treasury Management Report - this will update members with the progress of the capital position, amending prudential indicators as necessary and whether the treasury strategy is meeting its objectives or whether any policies require revision.

8.6.4. An Annual Treasury Report - this is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

APPENDICES

1. Treasury Management Policy Statement
2. Treasury Management Key Principles
3. Economic background
4. Interest rate forecasts
5. Loan maturity profile
6. MRP Policy Statement
7. Specified and non-specified investments
8. Counterparty criteria
9. Approved countries for investments
10. Treasury management scheme of delegation and the role of the Section 151 Officer
11. Prudential and Treasury Indicators
12. Explanation of Prudential Indicators
13. Glossary of, and information on, Prudential & Treasury Management indicators

Treasury Management Policy Statement

1. CIPFA defines its treasury management activities as: “The management of the authority’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks”.
2. This organisation 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.
3. This organisation 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.

The CIPFA Treasury Management in the Public Services: Code of Practice

The key principles of CIPFA's *Treasury Management in the Public Services: Code of Practice (2011 Edition)*, as described in Section 4 of that Code are as follows:-

Key Principle 1:

Public service organisations should put in place formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of their treasury management activities.

Key Principle 2:

Their policies and practices should make clear that the effective management and control of risks are prime objectives of their treasury management activities and that responsibility for these lies clearly within their organisations. Their appetite for risk should form part of their annual strategy, including any use of financial instruments for the prudent management of those risks, and should ensure that priority is given to security and liquidity when investing funds.

Key Principle 3:

They should acknowledge that the pursuit of value for money in treasury management and the use of suitable performance measures are valid and important tools for responsible organisations to employ in support of their business and service objectives; and that, within the context of effective risk management, their treasury management policies and practices should reflect this.

The Code then goes on to say that:

“In framing these recommendations, CIPFA acknowledges the difficulties of striving for effective risk management and control, whilst at the same time pursuing value for money. This code does not seek to be prescriptive about how this issue should be handled, particularly since it covers such a wide variety of organisations. However, where appropriate, the sector specific guidance notes give suitable advice. CIPFA recognises that no two organisations in the public services are likely to tackle this issue in precisely the same manner but success in this area of treasury management is likely to be viewed, especially in value for money terms, as an indicator of a strongly performing treasury management function.”

“Even though it dates back to 1991, CIPFA considers that the report by the Treasury and Civil Service Committee of the House of Commons on the BCCI closure is still pertinent, wherein it was stated that:”

“In balancing risk against return, local authorities should be more concerned to avoid risks than to maximise returns.”

“Indeed this view was supported by the Communities and Local Government Select Committee report into local authority investments in 2009.”

“It is CIPFA’s view that throughout the public services the priority is to protect capital rather than to maximise return. The avoidance of all risk is neither appropriate nor possible. However, a balance must be struck with a keen responsibility for public money.”

Accordingly the Authority will adopt, as part of the standing orders, the following four clauses;

1. The Authority will create and maintain, as the cornerstones for effective treasury management:
 - a treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities; and
 - suitable treasury management practices (TMPs) setting out the manner in which the Authority will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

The content of the Policy Statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of the Authority. Such amendments will not result in the Authority materially deviating from the Code's key principles.

2. The County Council, Executive Committee and the Audit Committee will receive reports on the Authority's treasury management policies, practices and activities, including; an annual strategy and plan in advance of the year, a mid-year review report and an annual report after its close, in the form prescribed in the TMPs.
3. The County Council/Executive Committee are responsible for the implementation of the Authority's treasury management policies and practices in accordance with the Treasury Management Scheme of Delegation. The S151 Officer is responsible for the execution and administration of treasury management decisions, who will act in accordance with the Authority's policy statement and TMPs and, if he/she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.
4. The Authority nominates Audit Committee to be responsible for ensuring effective scrutiny of treasury management strategy and policies.

ECONOMIC BACKGROUND

UK. Brexit. 2019 has been a year of upheaval on the political front as Theresa May resigned as Prime Minister to be replaced by Boris Johnson on a platform of the UK leaving the EU on 31 October 2019, with or without a deal. However, MPs blocked leaving on that date and the EU agreed an extension to 31 January 2020. In late October, MPs approved an outline of a Brexit deal to enable the UK to leave the EU on 31 January. Now that the Conservative Government has gained a large overall majority in the **general election** on 12 December, this outline deal will be passed by Parliament by that date. However, there will still be much uncertainty as the detail of a trade deal will need to be negotiated by the current end of the transition period in December 2020, which the Prime Minister has pledged he will not extend. This could prove to be an unrealistically short timetable for such major negotiations that leaves open two possibilities; one, the need for an extension of negotiations, probably two years, or, a no deal Brexit in December 2020.

GDP growth has taken a hit from Brexit uncertainty during 2019; quarter three 2019 surprised on the upside by coming in at +0.4% q/q, +1.1% y/y. However, the peak of Brexit uncertainty during the final quarter appears to have suppressed quarterly growth to probably around zero. The economy is likely to tread water in 2020, with tepid growth around about 1% until there is more certainty after the trade deal deadline is passed.

While the Bank of England went through the routine of producing another **quarterly Inflation Report**, (now renamed the Monetary Policy Report), on 7 November, it is very questionable how much all the writing and numbers were worth when faced with the uncertainties of where the UK will be after the general election. The Bank made a change in their Brexit assumptions to now include a deal being eventually passed. Possibly the biggest message that was worth taking note of from the Monetary Policy Report, was an increase in concerns among MPC members around weak global economic growth and the potential for Brexit uncertainties to become entrenched and so delay UK economic recovery. Consequently, the MPC voted 7-2 to maintain Bank Rate at 0.75% but two members were sufficiently concerned to vote for an immediate Bank Rate cut to 0.5%. The MPC warned that if global growth does not pick up or Brexit uncertainties intensify, then a rate cut was now more likely. Conversely, if risks do recede, then a more rapid recovery of growth will require gradual and limited rate rises. The speed of recovery will depend on the extent to which uncertainty dissipates over the final terms for trade between the UK and EU and by how much global growth rates pick up. The Bank revised its inflation forecasts down – to 1.25% in 2019, 1.5% in 2020, and 2.0% in 2021; hence, the MPC views inflation as causing little concern in the near future.

The **MPC meeting of 19 December** repeated the previous month's vote of 7-2 to keep Bank Rate on hold. Their key view was that there was currently 'no evidence about the extent to which policy uncertainties among companies and households had declined' i.e. they were going to sit on their hands and see how the economy goes in the next few months. The two members who voted for a cut were concerned that the labour market was faltering. On the other hand, there was a clear warning in the minutes that the MPC were concerned that "domestic unit labour costs have continued to grow at rates above those consistent with meeting the inflation target in the medium term".

If economic growth were to weaken considerably, the MPC has relatively little room to make a big impact with Bank Rate still only at 0.75%. It would therefore, probably suggest that it would be up to the Chancellor to provide help to support growth by way of a **fiscal boost** by e.g. tax cuts, increases in the annual expenditure budgets of government departments and services and expenditure on infrastructure projects, to boost the economy. The Government has already made moves in this direction and it made significant promises in its election manifesto to increase government spending by up to £20bn p.a., (this would add about 1% to GDP growth rates), by investing primarily in infrastructure. This is likely to be announced in the next Budget, probably in February 2020. The Chancellor has also amended the fiscal rules in November to allow for an increase in government expenditure.

As for **inflation** itself, CPI has been hovering around the Bank of England's target of 2% during 2019, but fell again in both October and November to a three-year low of 1.5%. It is likely to remain close to or under 2% over the next two years and so, it does not pose any immediate concern to the

MPC at the current time. However, if there was a hard or no deal Brexit, inflation could rise towards 4%, primarily because of imported inflation on the back of a weakening pound.

With regard to the **labour market**, growth in numbers employed has been quite resilient through 2019 until the three months to September where it fell by 58,000. However, there was an encouraging pick up again in the three months to October to growth of 24,000, which showed that the labour market was not about to head into a major downturn. The unemployment rate held steady at a 44-year low of 3.8% on the Independent Labour Organisation measure in October. Wage inflation has been steadily falling from a high point of 3.9% in July to 3.5% in October (3-month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates higher than CPI inflation), earnings grew by about 2.0%. As the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. The other message from the fall in wage growth is that employers are beginning to find it easier to hire suitable staff, indicating that supply pressure in the labour market is easing.

USA. President Trump's massive easing of fiscal policy in 2018 fuelled a temporary boost in consumption in that year which generated an upturn in the rate of growth to a robust 2.9% y/y. **Growth** in 2019 has been falling after a strong start in quarter 1 at 3.1%, (annualised rate), to 2.0% in quarter 2 and then 2.1% in quarter 3. The economy looks likely to have maintained a growth rate similar to quarter 3 into quarter 4; fears of a recession have largely dissipated. The strong growth in employment numbers during 2018 has weakened during 2019, indicating that the economy had been cooling, while inflationary pressures were also weakening. However, CPI inflation rose from 1.8% to 2.1% in November, a one year high, but this was singularly caused by a rise in gasoline prices.

The Fed finished its series of increases in rates to 2.25 – 2.50% in December 2018. In July 2019, it cut rates by 0.25% as a 'midterm adjustment' but flagged up that this was not intended to be seen as the start of a series of cuts to ward off a downturn in growth. It also ended its programme of quantitative tightening in August, (reducing its holdings of treasuries etc.). It then cut rates by 0.25% again in September and by another 0.25% in its October meeting to 1.50 – 1.75%.. At its September meeting it also said it was going to **start buying Treasuries again**, although this was not to be seen as a resumption of quantitative easing but rather an exercise to relieve liquidity pressures in the repo market. Despite those protestations, this still means that the Fed is again expanding its balance sheet holdings of government debt. In the first month, it will buy \$60bn, whereas it had been reducing its balance sheet by \$50bn per month during 2019. As it will be buying only short-term (under 12 months) Treasury bills, it is technically correct that this is not quantitative easing (which is purchase of long term debt). The Fed left rates unchanged in December. However, the accompanying statement was more optimistic about the future course of the economy so this would indicate that further cuts are unlikely.

Investor confidence has been badly rattled by the progressive ramping up of increases in tariffs President Trump has made on Chinese imports and China has responded with increases in tariffs on American imports. This **trade war** is seen as depressing US, Chinese and world growth. In the EU, it is also particularly impacting Germany as exports of goods and services are equivalent to 46% of total GDP. It will also impact developing countries dependent on exporting commodities to China. However, in November / December, progress has been made on agreeing a phase one deal between the US and China to roll back some of the tariffs; this gives some hope of resolving this dispute.

EUROZONE. **Growth** has been slowing from +1.8 % during 2018 to around half of that in 2019. Growth was +0.4% q/q (+1.2% y/y) in quarter 1, +0.2% q/q (+1.2% y/y) in quarter 2 and then +0.2% q/q, +1.1% in quarter 3; there appears to be little upside potential in the near future. German GDP growth has been struggling to stay in positive territory in 2019 and fell by -0.1% in quarter 2; industrial production was down 4% y/y in June with car production down 10% y/y. Germany would be particularly vulnerable to a no deal Brexit depressing exports further and if President Trump imposes tariffs on EU produced cars.

The European Central Bank (ECB) ended its programme of quantitative easing purchases of debt in December 2018, which then meant that the central banks in the US, UK and EU had all ended the

phase of post financial crisis expansion of liquidity supporting world financial markets by quantitative easing purchases of debt. However, the downturn in EZ growth in the second half of 2018 and into 2019, together with inflation falling well under the upper limit of its target range of 0 to 2%, (but it aims to keep it near to 2%), has prompted the ECB to take new measures to stimulate growth. At its March meeting it said that it expected to leave interest rates at their present levels “at least through the end of 2019”, but that was of little help to boosting growth in the near term. Consequently, it announced a **third round of TLTROs**; this provides banks with cheap borrowing every three months from September 2019 until March 2021 that means that, although they will have only a two-year maturity, the Bank was making funds available until 2023, two years later than under its previous policy. As with the last round, the new TLTROs will include an incentive to encourage bank lending, and they will be capped at 30% of a bank’s eligible loans. However, since then, the downturn in EZ and world growth has gathered momentum; at its meeting on 12 September it cut its deposit rate further into negative territory, from -0.4% to -0.5%, and announced a **resumption of quantitative easing purchases of debt for an unlimited period**. At its October meeting it said these purchases would start in November at €20bn per month - a relatively small amount compared to the previous buying programme. It also increased the maturity of the third round of TLTROs from two to three years. However, it is doubtful whether this loosening of monetary policy will have much impact on growth and, unsurprisingly, the ECB stated that governments would need to help stimulate growth by ‘growth friendly’ fiscal policy.

There were no policy changes in the December meeting, which was chaired for the first time by the new President of the ECB, Christine Lagarde. However, the outlook continued to be down beat about the economy; this makes it likely there will be further monetary policy stimulus to come in 2020. She did also announce a thorough review of how the ECB conducts monetary policy, including the price stability target. This review is likely to take all of 2020.

On the political front, Austria, Spain and Italy have been in the throes of **forming coalition governments** with some unlikely combinations of parties i.e. this raises questions around their likely endurance. The latest results of German state elections has put further pressure on the frail German CDU/SDP coalition government and on the current leadership of the CDU. The results of the Spanish general election in November have not helped the prospects of forming a stable coalition.

CHINA. Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and shadow banking systems. In addition, there still needs to be a greater switch from investment in industrial capacity, property construction and infrastructure to consumer goods production.

JAPAN - has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.

WORLD GROWTH. Until recent years, world growth has been boosted by increasing **globalisation** i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last thirty years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy. The Chinese government has targeted achieving major world positions in specific key sectors and products, especially high tech areas and production of rare earth minerals used in high tech products. It is achieving this by massive financial support, (i.e. subsidies), to state owned firms, government directions to other firms, technology theft, restrictions on market access by foreign firms and informal targets for the domestic market share of Chinese producers in the selected sectors. This is regarded as being unfair competition that is putting western firms at an unfair disadvantage or even putting some out of business. It is also regarded with suspicion on the political front as China is an authoritarian country that is not averse to using economic and military power for political advantage. The current trade war between the US and China therefore needs to be seen against that backdrop. It is, therefore, likely that we are heading into a period where there will be a **reversal of world globalisation and a decoupling of western countries** from dependence on China to supply products. This is likely to produce a

backdrop in the coming years of weak global growth and so weak inflation. **Central banks are, therefore, likely to come under more pressure to support growth by looser monetary policy measures and this will militate against central banks increasing interest rates.**

The trade war between the US and China is a major concern to **financial markets** due to the synchronised general weakening of growth in the major economies of the world, compounded by fears that there could even be a recession looming up in the US, though this is probably overblown. These concerns resulted in **government bond yields** in the developed world falling significantly during 2019. If there were a major worldwide downturn in growth, central banks in most of the major economies will have limited ammunition available, in terms of monetary policy measures, when rates are already very low in most countries, (apart from the US). There are also concerns about how much distortion of financial markets has already occurred with the current levels of quantitative easing purchases of debt by central banks and the use of negative central bank rates in some countries. The latest PMI survey statistics of economic health for the US, UK, EU and China have all been predicting a downturn in growth; this confirms investor sentiment that the outlook for growth during the year ahead is weak.

INTEREST RATE FORECASTS

The interest rate forecasts provided by Link Asset Services in paragraph 3.3 are **predicated on an assumption of an agreement being reached on Brexit between the UK and the EU**. On this basis, while GDP growth is likely to be subdued in 2019 and 2020 due to all the uncertainties around Brexit depressing consumer and business confidence, an agreement on the detailed terms of a trade deal is likely to lead to a boost to the rate of growth in subsequent years. This could, in turn, increase inflationary pressures in the economy and so cause the Bank of England to resume a series of gentle increases in Bank Rate. Just how fast, and how far, those increases will occur and rise to, will be data dependent. The forecasts in this report assume a modest recovery in the rate and timing of stronger growth and in the corresponding response by the Bank in raising rates.

- In the event of an **orderly non-agreement exit in December 2020**, it is likely that the Bank of England would take action to cut Bank Rate from 0.75% in order to help economic growth deal with the adverse effects of this situation. This is also likely to cause short to medium term gilt yields to fall.
- If there were a **disorderly Brexit**, then any cut in Bank Rate would be likely to last for a longer period and also depress short and medium gilt yields correspondingly. Quantitative easing could also be restarted by the Bank of England. It is also possible that the government could act to protect economic growth by implementing fiscal stimulus.

The balance of risks to the UK

- The overall balance of risks to economic growth in the UK is probably even, but dependent on a successful outcome of negotiations on a trade deal.
- The balance of risks to increases in Bank Rate and shorter term PWLB rates are broadly similarly to the downside.
- In the event that a Brexit deal was agreed with the EU and approved by Parliament, the balance of risks to economic growth and to increases in Bank Rate is likely to change to the upside.

One risk that is both an upside and downside risk, is that all central banks are now working in very different economic conditions than before the 2008 financial crash as there has been a major increase in consumer and other debt due to the exceptionally low levels of borrowing rates that have prevailed since 2008. This means that the neutral rate of interest in an economy, (i.e. the rate that is neither expansionary nor deflationary), is difficult to determine definitively in this new environment, although central banks have made statements that they expect it to be much lower than before 2008. Central banks could therefore either over or under do increases in central interest rates.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- **Brexit** – if it were to cause significant economic disruption and a major downturn in the rate of growth.
- **Bank of England** takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- A resurgence of the **Eurozone sovereign debt crisis**. In 2018, Italy was a major concern due to having a populist coalition government which made a lot of anti-austerity and anti-EU noise. However, in September 2019 there was a major change in the coalition governing Italy which has brought to power a much more EU friendly government; this has eased the pressure on Italian bonds. Only time will tell whether this new coalition based on an unlikely alliance of two very different parties will endure.
- Weak capitalisation of some **European banks**, particularly Italian banks.
- **German minority government**. In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. The CDU has done badly in recent state elections but the SPD has done particularly badly and this has raised a major question mark over continuing to support the CDU. Angela Merkel has stepped down from being the CDU party leader but she intends to remain as Chancellor until 2021.
- **Other minority EU governments**. Austria, Finland, Sweden, Spain, Portugal, Netherlands and Belgium also have vulnerable minority governments dependent on coalitions which could prove fragile.
- **Austria, the Czech Republic, Poland and Hungary** now form a strongly anti-immigration bloc within the EU. There has also been rising anti-immigration sentiment in Germany and France.
- In October 2019, the IMF issued a report on the World Economic Outlook which flagged up a synchronised slowdown in world growth. However, it also flagged up that there was **potential for a rerun of the 2008 financial crisis**, but this time centred on the huge debt binge accumulated by corporations during the decade of low interest rates. This now means that there are corporates who would be unable to cover basic interest costs on **some \$19trn of corporate debt in major western economies**, if world growth was to dip further than just a minor cooling. This debt is mainly held by the shadow banking sector i.e. pension funds, insurers, hedge funds, asset managers etc., who, when there is \$15trn of corporate and government debt now yielding negative interest rates, have been searching for higher returns in riskier assets. Much of this debt is only marginally above investment grade so any rating downgrade could force some holders into a fire sale, which would then depress prices further and so set off a spiral down. The IMF's answer is to suggest imposing higher capital charges on lending to corporates and for central banks to regulate the investment operations of the shadow banking sector. In October 2019, the deputy Governor of the Bank of England also flagged up the dangers of banks and the shadow banking sector lending to corporates, especially highly leveraged corporates, which had risen back up to near pre-2008 levels.
- **Geopolitical risks**, for example in North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.

Upside risks to current forecasts for UK gilt yields and PWLB rates

- **Brexit** – if agreement was reached all round that removed all threats of economic and political disruption between the EU and the UK.
- The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.
- **UK inflation**, whether domestically generated or imported, returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

Rhagolygon Graddfeydd Llog 2020/2023

Interest Rate Forecasts 2020/2023

PWLB rates and forecast shown below have taken into account the 20 basis point certainty rate reduction effective as of the 1st November 2012.

Link Asset Services Interest Rate View													
	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25	1.25	1.25	1.25
3 Month LIBID	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.30	1.30
6 Month LIBID	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40	1.50	1.50	1.50	1.50
12 Month LIBID	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60	1.70	1.70	1.70	1.70
5yr PWLB Rate	2.40	2.40	2.50	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.10	3.20	3.20
10yr PWLB Rate	2.70	2.70	2.70	2.80	2.90	3.00	3.10	3.20	3.20	3.30	3.30	3.40	3.50
25yr PWLB Rate	3.30	3.40	3.40	3.50	3.60	3.70	3.70	3.80	3.90	4.00	4.00	4.10	4.10
50yr PWLB Rate	3.20	3.30	3.30	3.40	3.50	3.60	3.60	3.70	3.80	3.90	3.90	4.00	4.00
Bank Rate													
Link Asset Services	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.25%
Capital Economics	0.75%	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	-	-	-	-	-
5yr PWLB Rate													
Link Asset Services	2.40%	2.40%	2.50%	2.50%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.20%	3.20%
Capital Economics	2.40%	2.50%	2.50%	2.60%	2.60%	2.80%	2.80%	2.90%	-	-	-	-	-
10yr PWLB Rate													
Link Asset Services	2.70%	2.70%	2.70%	2.80%	2.90%	3.00%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.50%
Capital Economics	2.70%	2.70%	2.80%	2.80%	2.90%	3.00%	3.00%	3.10%	-	-	-	-	-
25yr PWLB Rate													
Link Asset Services	3.30%	3.40%	3.40%	3.50%	3.60%	3.70%	3.70%	3.80%	3.90%	4.00%	4.00%	4.10%	4.10%
Capital Economics	3.10%	3.10%	3.20%	3.20%	3.20%	3.30%	3.30%	3.40%	-	-	-	-	-
50yr PWLB Rate													
Link Asset Services	3.20%	3.30%	3.30%	3.40%	3.50%	3.60%	3.60%	3.70%	3.80%	3.90%	3.90%	4.00%	4.00%
Capital Economics	3.10%	3.10%	3.20%	3.20%	3.30%	3.40%	3.40%	3.50%	-	-	-	-	-

Rhan o gyngor dderbyniwyd gan / An extract from advice received from: Link Asset Services

DADANSODDIAD BENTHYCIADAU PWLB YN AEDDFEDU 2020/21 YMLAEN / PWLB LOANS MATURITY ANALYSIS 2020/21 ONWARDS						
	Aeddfedu PWLB Maturity £'000	Blwydd-dal PWLB EIP/ Annuity £'000	Benthyciadau Marchnad/ Market Loans £'000	Amrywiol/ PWLB Variable £'000	Cyfanswm yn Aeddfedu/ Total Maturing £'000	%Yn Aeddfedu o'r Cyfran yn sefyll/ Maturing of Total Outstanding %
2020/21	4,500	12	0	0	4,512	3.6
2021/22	0	14	0	0	14	0.0
2022/23	2,285	15	0	0	2,300	1.8
2023/24	1,854	16	0	0	1,870	1.5
2024/25	0	18	0	0	18	0.0
2025/26	0	20	0	0	20	0.0
2026/27	1,381	22	0	0	1,403	1.1
2027/28	2,165	24	0	0	2,189	1.7
2028/29	263	26	0	0	289	0.2
2029/30	1,538	21	0	0	1,559	1.2
2030/31	451	15	0	0	466	0.4
2031/32	1,941	9	0	0	1,950	1.5
2032/33	315	8	0	0	323	0.3
2033/34	637	0	0	0	637	0.5
2034/35	624	0	0	0	624	0.5
2035/36	611	0	0	0	611	0.5
2036/37	599	0	0	0	599	0.5
2037/38	587	0	0	0	587	0.5
2038/39	225	0	0	0	225	0.2
2039/40	5,000	0	0	0	5,000	4.0
2040/41	3,500	0	0	0	3,500	2.8
2042/43	1,000	0	0	0	1,000	0.8
2043/44	1,020	0	0	0	1,020	0.8
2044/45	1,010	0	0	0	1,010	0.8
2045/46	11,464	0	0	0	11,464	9.1
2050/51	2,000	0	0	0	2,000	1.6
2052/53	28,238	0	0	0	28,238	22.3
2054/55	3,000	0	0	0	3,000	2.4
2055/56	3,500	0	0	0	3,500	2.8
2056/57	5,000	0	0	0	5,000	4.0
2057/58	8,513	0	0	0	8,513	6.7
2059/60	1,763	0	0	0	1,763	1.4
2064/65	10,000	0	0	0	10,000	7.9
2066/67	6,200	0	0	0	6,200	4.9
2068/69	15,000	0	0	0	15,000	11.9
	126,184	220	0	0	126,404	100.0
Cyfartaledd bywyd (blynyddoedd)/ Average life (years)	25.48	6.94	0.00	0.00	25.44	
Cyfartaledd graddfa (%)/ Average rate (%)	5.15	9.44	0.00	0.00	4.73	

PROFFIL AD-DALU BENTHYCIADAU ERAILL 2020/21 YMLAEN / OTHER LOANS REPAYMENT PROFILE 2020/21 ONWARDS							
	Llywodraeth Cymru / Welsh Government	Benthyciad Salix Loan 1	Benthyciad Salix Loan 2	Benthyciad Salix Loan 3	Benthyciad Salix Loan 4	Benthyciad Salix Loan 5	Cyfanswm / Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
2020/21	44	16	46	64	26	100	296
2021/22	0	16	46	64	26	199	351
2022/23	0	17	46	63	26	199	351
2023/24	0	17	46	64	26	200	353
2024/25	0	8	45	64	26	200	343
2025/26	0	0	45	64	27	200	336
2026/27	0	0	0	63	27	200	290
2027/28	0	0	0	63	27	200	290
2028/29	0	0	0	63	27	200	290
2029/30	0	0	0	0	13	200	213
2030/31	0	0	0	0	0	99	99
Cyfanswm / Total	44	74	274	572	251	1,997¹	3,212

¹ Total amount to be repaid differs from the total amount outstanding in Table 4.1.1 due to only having received £1,178k to date, however £1,997k will be received.

Minimum Revenue Provision Policy Statement 2020/21

The Council is required to pay off an element of the accumulated Council Fund capital spend each year (the CFR) through a revenue charge (the minimum revenue provision, MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision, VRP).

The Welsh Government regulations require the full Council to approve an MRP Statement in advance of each year. A variety of options is provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement:-

For capital expenditure incurred between 1 April 2008 and 31 March 2018, financed by supported borrowing, the MRP policy will be to charge MRP on the Equal Instalment method, Asset Life basis over 50 years. The MRP on capital expenditure funded by unsupported borrowing during this period has already been charged using the Equal Instalment method, Asset Life basis using the estimated lives of the assets, based on information available at that time. This change in policy realigns the MRP policies for assets funded by supported borrowing and assets funded by unsupported borrowing.

From 1st April 2018 for all supported and unsupported borrowing (including PFI and finance leases), the MRP policy will also be the Equal Instalment Annuity Method, the Asset Life basis. However, the estimated life periods, will be set by the S151 Officer based upon advice received from the relevant officers and will have regard to Welsh Government guidance in relation to MRP and asset lives. Where land is purchased, the asset life will be based on the asset life of the asset placed on the land, which in the majority of cases will be 50 years in line with the asset life for buildings.

MRP charges based on asset life would not be charged until the year the asset becomes operational. The S151 Officer may postpone the MRP charge until the financial year following the one in which the asset becomes operational. The estimated asset life of the asset would be determined in the year the MRP commences and would not change over the life of the asset. The estimated life periods, will be set by the S151 Officer based upon advice received from the relevant officers and will have regard to Statutory requirements and Welsh Government guidance in relation to MRP and asset life. Where land is purchased, the asset life will be based on the asset life of the asset placed on the land, which in the majority of cases will be 50 years in line with the asset life for buildings.

As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis, which most reasonably reflects the anticipated period of benefit that arises from the expenditure. In addition, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

The Council retains the right to make additional voluntary payments to reduce debt if deemed prudent.

The Housing Revenue Account share of the CFR is subject to a 2% MRP charge, based upon the closing CFR for the previous year, in line with the approved 30-year business plan.

Any repayments included in annual PFI or finance leases are applied as MRP and will be consistent with the asset life basis over the life of the lease or PFI scheme.

Specified and Non-Specified Investments

The Welsh Government 'Guidance on Local Government Investments' (Effective from 1 April 2010) provides the definition of specified and non-specified investments.

Paragraph 5.1 of the 'Guidance' states that an investment is specified if all of the following apply:-

- (a) the investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling; and
- (b) the investment is not a long-term investment (*); and
- (c) the making of the investment is not defined as capital expenditure by virtue of regulation 20(1)(d) of the Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 [SI 3239 as amended]; and
- (ch) the investment is made with a body or in an investment scheme of high credit quality (**); or with one of the following public-sector bodies:
 - (i) the United Kingdom Government
 - (ii) a local authority in England or Wales (as defined in section 23 of the 2003 Act) or a similar body in Scotland or Northern Ireland
 - (iii) a parish or community council.

The 'Guidance' also states that any investment not meeting the definition of paragraph 5.1 is classified as a non-specified investment.

During 2020/21 the Council does not intend to make any investments in foreign currencies, nor any with low credit quality bodies, nor any that are defined as capital expenditure by legislation (such as company shares). Non-specified investments will therefore be limited to (i) long-term investments; and (ii) deposits with the Council's own banker for transactional purposes if it fails to meet the basic credit criteria; in this instance balances will be minimised as far as is possible

The table in Appendix 8 set out the investment criteria and limits for the categories of investments intended for use during 2020/21 and therefore form the basis for the approved lending list.

Any proposed revisions or amendments during the year to the categories of specified and non-specified investments to be used and / or to the associated credit rating criteria / investment limits will be subject to prior approval by the County Council.

* Section 2.4 of the 'Guidance' defines a long term investment as "any investment other than (a) one which is due to be repaid within 12 months of the date on which the investment was made or (b) one which the local authority may require to be repaid within that period."

** For the purposes of high credit quality the 'Guidance' states that "for the purposes of paragraph 5.1(d), Welsh ministers recommend that the Strategy should define high credit quality (and where this definition refers to credit ratings, paragraph 6.1 (***) is relevant)."

*** Paragraph 6.1 of the 'Guidance' recommends that "the Strategy should set out the authority's approach to assessing the risk of loss of investments, making clear in particular:

- (a) to what extent, if any, risk assessment is based upon credit ratings issued by one or more credit rating agencies;
- (b) where credit ratings are used, how frequently credit ratings are monitored and what action is to be taken when ratings change; and
- (c) what other sources of information on credit risk are used, additional to or instead of credit ratings."

The table in Appendix 6 of this strategy sets out what this Council defines as high credit quality and the associated investment criteria and limits and section 4.2 of this strategy sets out the Council's creditworthiness approach.

Counterparty Criteria

Category	Short Term Credit Rating (Fitch)	Short Term Credit Rating (Moody's)	Short Term Credit Rating (Standard & Poor's)	Long Term Credit Rating (Fitch)	Long Term Credit Rating (Moody's)	Long Term Credit Rating (Standard & Poor's)	Cash Limit	Time Limit
Bank and Building Societies (not nationalised or part nationalised)	F1+	P-1	A-1+	AAA	Aaa	AAA	£10m	5 years
	F1+	P-1	A-1+	AA	Aa2	AA	£10m	3 years
	F1+	P-1	A-1+	AA-	Aa3	AA-	£10m	364 days
	F1	P-1	A-1	A	A2	A	£7.5m	6 months
Nationalised / Part Nationalised UK Banks	n/a	n/a	n/a	n/a	n/a	n/a	£10m	364 days
UK Central Government (irrespective of credit rating)	n/a	n/a	n/a	n/a	n/a	n/a	No maximum	No maximum
UK Local Authorities**	n/a	n/a	n/a	n/a	n/a	n/a	£5m	364 days
Money Market Funds	n/a	n/a	n/a	AAA	AAA	AAA	£5m	6 months

* as defined in the Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003

** as defined in the Local Government Act 2003

Notes and Clarifications**(1) Cash Limit**

- (i) The cash limits apply both to the individual counterparty and to the overall group to which it belongs (e.g. for the banks within the Lloyds Banking Group plc (being Bank of Scotland plc and Lloyds Bank plc), the investment limit applies to those banks individually and the banking group as a whole);
- (ii) The overall cash limit for deposits over 364 days is £15m.

(2) Time Limit

- (i) This up to and including the period indicated.

(3) Foreign Countries

- (i) Investments in foreign countries will be limited to those that hold a sovereign credit rating of (Fitch) AA- or equivalent (from the agencies referred to in section 4.3 of this strategy) sovereign credit rating (based upon the lowest common denominator), and to a maximum of £10 million per foreign country.
- (ii) Investments in countries whose lowest sovereign rating is not AA- or above will not be permitted. No country limit will apply to investments in the UK, irrespective of the sovereign credit rating.
- (iii) Subsidiaries of foreign banking groups will normally be assessed according to the country of domicile of the parent organisation. However, Santander UK plc (a subsidiary of Spain's Banco Santander) will be classed as a UK bank due to its substantial UK franchises and the arms-length nature of the parent-subsidary relationships.
- (iv) Sovereign credit rating criteria and foreign country limits will not apply to investments in multilateral development banks (e.g. the European Investment Bank and the World Bank) or other supranational organisations (e.g. the European Union).

4. Credit Rating Downgrade

Should a credit rating downgrade place a counterparty below the minimum credit rating criteria for investment, the counterparty will cease to be used as soon as practicable.

If the S151 Officer wishes to continue investing with that counterparty approval will be sought from the Chair of the Audit Committee plus one other member of the Chair's choosing, who both must approve the action. This will then be reported as appropriate at the next available opportunity.

Approved countries for investments [correct as at 3 January 2020]

This list is based on those countries which have sovereign ratings of AA- or higher (we show the lowest rating from Fitch, Moody's and S&P) and also, (except - at the time of writing - for Hong Kong, Norway and Luxembourg), have banks operating in sterling markets which have credit ratings of green or above in the Link Asset Services credit worthiness service.

Based on lowest available rating

AAA

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

AA+

- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)
- France
- Hong Kong
- U.K.

AA-

- Belgium
- Qatar

Treasury management scheme of delegation

(i) County Council

- budget approval;
- approval of the annual Treasury Management Strategy Statement, Annual Investment Strategy and MRP Policy, annual Treasury Management Policy Statement and amendments thereto;
- approval of amendments to the Council's adopted clauses;
- receiving and reviewing monitoring reports on treasury management policies, practices and activities; and
- acting on recommendations received from the Audit Committee and/or Executive Committee.

(ii) Executive Committee

- budget consideration;
- approval of the division of responsibilities;
- approval of the selection of external service providers and agreeing terms of appointment;
- receiving and reviewing monitoring reports on treasury management policies, practices and activities and making recommendations to the County Council as appropriate; and
- acting on recommendations received from the Audit Committee.

(iii) Audit Committee

- Scrutiny of Treasury Management matters as required by CIPFA's Code of Practice on Treasury Management and the Council's Treasury Management Policy. This includes:-
 - scrutinising the annual Treasury Management Strategy Statement, Annual Investment Strategy, Annual MRP Policy, Annual Treasury Management Policy and Treasury Management Practices and making recommendations to the Executive Committee and County Council as appropriate;
 - scrutinising proposals for amendments to the annual Treasury Management Strategy Statement, Annual Investment Strategy, Annual MRP Policy, Annual Treasury Management Policy and Treasury Management Practices and to the adopted clauses and making recommendations to the Executive and County Council as appropriate;
 - receiving and scrutinising any other proposals relating to the treasury management which require a decision by the Executive or County Council; and
 - receiving and scrutinising monitoring reports on treasury management policies, practices and activities and make recommendations to the Executive and County Council as appropriate.

The Treasury Management role of the Section 151 Officer

The Section 151 (responsible) Officer's role includes:-

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers; and
- Responsibility for the execution and administration of its Treasury decisions, including decision on borrowing, investment and financing, have been delegated to the Section 151 Officer, who will act in accordance with the Council's policy statements and TMP's.

- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long term timeframe
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money
- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority
- ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following: -
 - Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios;
 - Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments;
 - Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making;
 - Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken;
 - Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.

**PRUDENTIAL & TREASURY INDICATORS
BUDGET SETTING 2020/21**

APPENDIX 11

No. Indicator		2018/19 out-turn	2019/20 estimate	2020/21 proposal	2021/22 proposal	2022/23 proposal
Affordability						
1,2	Estimates of [or actual] ratio of financing costs to net revenue stream:					
	Council Fund	4.92%	5.03%	5.15%	5.40%	5.91%
	Housing Revenue Account (inclusive of settlement)	16.88%	18.78%	17.16%	14.57%	14.18%
	Total	6.34%	6.68%	6.62%	6.57%	7.01%
Prudence						
3	Gross debt and the Capital Financing Requirement (CFR)	✓	✓	✓	✓	✓
	<i>Is the gross external debt < the CFR for the preceding year plus the estimates of any additional CFR for the current and the next two financial years?</i>			✓	✓	✓
Capital Expenditure		£000	£000	£000	£000	£000
4,5	Estimates of [or actual] capital expenditure					
	Council Fund	21,650	18,820	19,765	21,662	14,675
	Housing Revenue Account	9,028	14,307	17,138	17,704	14,402
	Total	30,678	33,127	36,903	39,366	29,077
6,7	Estimates of [or actual] Capital Financing Requirement					
	Council Fund	97,847	102,036	108,536	118,856	124,349
	Housing Revenue Account	40,815	39,998	39,449	44,410	44,621
	Total	138,662	142,034	147,985	163,266	168,970
External Debt		£000	£000	£000	£000	£000
8	Authorised Limit					
	: General Borrowing	174,000	175,000	178,000	193,000	199,000
	: Other long term liabilities	3,000	3,000	5,000	5,000	5,000
	: Total	177,000	178,000	183,000	198,000	204,000

9	Operational Boundary					
	: General Borrowing	161,000	170,000	173,000	188,000	194,000
	: Other long term liabilities	3,000	3,000	5,000	5,000	5,000
	: Total	164,000	173,000	178,000	193,000	199,000
10	Actual External Debt	132,549				
Treasury Management		2018/19 out-turn	2019/20 estimate	2020/21 proposal	2021/22 proposal	2022/23 proposal
11	The Local Authority has adopted the CIPFA Code of Practice for Treasury Management in the Public Services	✓	✓	✓	✓	✓
		£000	£000	£000	£000	£000
12	Gross and net debt	100%	100%	100%	100%	100%
	<i>The upper limit on the net debt as a proportion of gross debt</i>					
13	The upper limit on fixed rate exposures:	157,000	155,000	158,000	173,000	179,000
	(net principal outstanding)					
14	The upper limit on variable rate exposures:	20,000	20,000	20,000	20,000	20,000
	(net principal outstanding)					
15	The limit for total principal sums invested for periods longer than 364 days	15,000	15,000	15,000	15,000	15,000
	(any long term investments carried forward from previous years will be included in each year's limit)					
			2020/21 upper limit		2020/21 lower limit	
16	The upper and lower limits for the maturity structure of fixed rate borrowing					
	• under 12 months		20%		0%	
	• 12 months and within 24 months		20%		0%	
	• 24 months and within 5 years		50%		0%	
	• 5 years and within 10 years		75%		0%	
	• 10 years and above		100%		0%	
			no change		no change	

Information on Prudential & Treasury Management indicators

A) Affordability

1 & 2 Ratio of financing costs to net revenue stream

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

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

B) Prudence

3 Gross Debt and the CFR

The Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2020/21 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

C) Capital expenditure

4 & 5 Estimates of Capital Expenditure

This is the forecast Capital Expenditure from 2019/20 to 2022/23, and is based on the Capital Programme for 2019/20 and the Capital Strategy for 2020/21.

6 & 7 The Council's borrowing need (the Capital Financing Requirement)

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

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

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

CH) External Debt

8. **The authorised limit for external debt.** A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

The S151 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 the budget report.

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

Glossary

CAPITAL EXPENDITURE

Capital expenditure is expenditure on the purchase of a non-current asset, which will be used in providing services beyond the current financial year, or expenditure which adds to, and not merely maintains, the value of an existing non-current asset. Examples include: the building of a new school, the purchase of IT equipment, a major refurbishment of a care home.

CAPITAL FINANCING

Funds that are available to pay for capital expenditure. There are various methods of financing capital expenditure including borrowing, leasing, direct revenue financing, usable capital receipts, capital grants, capital contributions, revenue reserves and earmarked reserves.

CAPITAL FINANCING REQUIREMENT

The total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need.

CAPITAL PROGRAMME

The capital schemes the Council intends to carry out over a specific period of time.

CAPITAL RECEIPTS

Capital receipts represent the proceeds from the disposal of land or other non-current assets. Proportions of capital receipts can be used to finance new capital expenditure, within rules set down by the government, but they cannot be used to finance revenue expenditure.

CIPFA

This is The Chartered Institute of Public Finance and Accountancy, the lead professional and regulatory body for local Authority accounting.

HOUSING REVENUE ACCOUNT (HRA)

The HRA is a separate account to the Council Fund, and includes the income and expenditure arising from the provision of housing accommodation by the Council.

INTEREST RECEIVABLE OR PAYABLE

The effective interest rate method is used to measure the carrying value of a financial asset or liability measured at cost less accumulated amortisation, and to allocate associated interest income or expense to the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to equal the amount at initial recognition. The effective interest is adjusted to the actual interest payment or receipt through the Movement in Reserves Statement to ensure only actual interest is charged to Council Tax. For financial assets and liabilities carried at cost because the effective rate of interest is the same as the carrying rate of interest, the carrying value is adjusted for accrued interest.

MINIMUM REVENUE PROVISION (MRP)

The minimum amount which must be charged to the revenue account each year in order to provide for the repayment of loans and other amounts borrowed by the Council.

NET DEBT

The Net Debt is the Council's borrowings less cash and liquid resources.

PUBLIC WORKS LOANS BOARD (PWLB)

A Central Government Agency which provides loans for one year and/or more to authorities at interest rates only slightly higher than those at which the government can borrow itself.

REVENUE EXPENDITURE FUNDED BY CAPITAL UNDER STATUTE (REFCUS)

Expenditure which can be properly deferred (i.e. treated as capital in nature), but which does not result in, or remain matched with, a tangible asset. Examples of deferred charges are grants of a capital nature to voluntary organisations.

REVENUE SUPPORT GRANT

A grant paid by Central Government to authorities, contributing towards the general cost of their services.

SUPPORTED BORROWING

The Council borrows money to fund part of its capital programme. This borrowing is recognised by Central Government in its calculation of formula funding for the Council.

TEMPORARY BORROWING

Money borrowed for a period of less than one year.

UNSUPPORTED BORROWING

The Council can borrow additional money to the borrowing supported by Government to finance its capital expenditure as long as it is affordable and sustainable. This power is governed by the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code, with which the Council fully complies.