## APPENDIX 1

## 2017-18 TREASURY MANAGEMENT STRATEGY

## INTRODUCTION

1. The Local Government Act 2003 (the Act) and supporting regulations requires the Authority to 'have regard to' the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code and the CIPFA Treasury Management Code of Practice to set prudential indicators for the next three years to ensure that capital investment plans remain affordable, prudent and sustainable.

2. The Act requires the Authority to prepare a Treasury Management Strategy (the Strategy) for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance issued subsequent to the Act). This sets out the Authority's policies for managing its investments and for giving priority to the security and liquidity of those investments.

3. The Authority's strategy is prepared having regard to the Department of Communities and Local Government (DCLG) Guidance on Local Government Investments ("the Guidance"), which came into effect from 1 April 2010.

4. The strategy also includes the Authority's 2017-18 Minimum Revenue Provision Strategy.

5. The CIPFA Code of Practice on Treasury Management (the Code) (revised November 2009) was adopted by this Authority on 14 April 2010. CIPFA issued revisions to the Prudential Code, Treasury Management Code and Treasury Guidance Notes in mid November 2011 (although there was little material change in the revisions, mainly in relation to Housing Revenue Account).

6. The primary requirements of the Code are as follows:

   (i) Creation and maintenance of a Treasury Management Policy Statement, which set out the policies and objectives of the Authority's treasury management activities.

   (ii) Creation and maintenance of Treasury Management Practices, which set out the manner in which the Authority will seek to achieve those policies and objectives:

   (iii) Reporting Requirements – the Authority is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of polices, estimates and actuals.

   - Prudential and treasury indicators and treasury strategy:

- An annual treasury report – this provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy

- A mid-year treasury management report – this will update members with the progress of the capital position, amending prudential indicators as necessary, and whether any policies require revision.

(iii) Delegation by the Authority of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

(iv) Where appropriate, delegation by the Authority of the role of scrutiny of the Treasury Management Strategy and policies to a specific named body. The Authority has previously delegated scrutiny to the Policy Committee. It will now retain this role for itself.

7. Warrington Borough Council act as the Authority's advisor on Treasury Management. The suggested Treasury Management Strategy for 2017-18 is informed by Warrington Borough Council treasury officers' views on interest rates and other financial matters, supplemented with leading market forecasts provided by Warrington Borough Council's treasury advisor (Capita). The strategy covers two main areas:

Capital Issues
- the capital programme and the capital prudential indicators 2017-18 to 2019-20; and
- the minimum revenue position (MRP) strategy.

Treasury management issues
- treasury prudential indicators;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling opportunities;
- the annual investment strategy;
- policy on use of external service providers; and
- treasury management scheme of delegation.

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

# Capital Issues

**The Capital Programme and Capital Prudential Indicators 2017-18 to 2019-20**

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

Capital Expenditure Plan

10. This prudential indicator is a summary of the Authority's capital expenditure plan, both those agreed previously, and those forming part of this budget cycle.

| 2015-16 Actual £000 | 2016-17 Estimate £000 | Capital Expenditure | 2017-18 Estimate £000 | 2018-19 Estimate £000 | 2019-20 Estimate £000 |
|---|---|---|---|---|---|
| 6,059 | 13,290 | | 3,605 | 6,556 | 4,065 |

11. The table below shows how the plan is being financed by capital or revenue resources. It is currently assumed that no capital grant will be available. Any shortfall of resources results in a funding borrowing need:

| 2015-16 Actual £000 | 2016-17 Estimate £000 | Capital Financing | 2017-18 Estimate £000 | 2018-19 Estimate £000 | 2019-20 Estimate £000 |
|---|---|---|---|---|---|
| 2,920 | 2,576 | Capital Grants | 0 | 0 | 0 |
| 61 | 51 | Capital Receipts | 55 | 55 | 55 |
| 3,078 | 10,664 | Reserves | 3,550 | 6,501 | 4,010 |
| **6,059** | **13,290** | **Total Capital Financing** | **3,605** | **6,556** | **4,065** |

Capital Financing Requirement

12. The Capital Financing Requirement (CFR) indicator is a notional figure which shows the Authority's theoretical need to borrow to fund capital expenditure. Any capital expenditure, which has not immediately been paid for, will increase the CFR.

13. The CFR does not increase indefinitely, as the Minimum Revenue Provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need.

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

| 2015-16 Actual £000 | 2016-17 Estimate £000 | Capital Financing Requirement (CFR) | 2017-18 Estimate £000 | 2018-19 Estimate £000 | 2019-20 Estimate £000 |
|---|---|---|---|---|---|
| **8,783** | **8,195** | CFR brought forward | **7,645** | **7,133** | **6,655** |
| | | **Movement in CFR represented by** | | | |
| 0 | 0 | Net financing need for the year | 0 | 0 | 0 |
| (588) | (550) | Less MRP | (512) | (478) | (446) |
| **8,195** | **7,645** | CFR carried forward | **7,133** | **6,655** | **6,209** |

Affordability prudential indicators

15. Prudential indicators are required to assess the affordability of the capital investment plan on the Authority's overall finances. The Authority is asked to approve the following indicators contained in this report.

Ratio of financing costs to net revenue stream

16. One of the indicators of affordability is the estimated ratio of the Authority's general fund capital financing costs to its net revenue stream in percentage terms. This indicator shows the proportion of the revenue budget spent on capital financing costs; if the ratio is increasing rapidly over time then a larger proportion of revenue resources is being taken up by capital financing costs, which could be used for other elements of the Authority's budget.

| 2015-16 Actual % | 2016-17 Estimate % | Ratio of financing costs to net revenue stream | 2017-18 Estimate % | 2018-19 Estimate % | 2019-20 Estimate % |
|---|---|---|---|---|---|
| 1.11 | 1.32 | | 1.22 | 1.12 | 1.03 |

Incremental impact of capital investment decisions on Council Tax

17. The other indicator of affordability is the estimate of the incremental impact on Council Tax, over and above capital investment decisions that have previously been taken by the Authority. This indicator identifies the revenue costs associated with proposed changes to the three year capital programme recommended in the budget report. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which are not published over a three year period. The indicator is intended to show the effect on Authority Tax of approving new capital expenditure in the capital programme.

18. The Authority has a strategy of funding capital from grant, revenue or reserves and the impact of this is included in the MTFP and the reserves strategy. The capital programme currently estimated does not therefore add any additional revenue cost to the budget, as can be seen by comparing the ratios in the table below.

| 2015-16 Actual £000 | 2016-17 Estimate £000 | Financing costs to Council Tax | 2017-18 Estimate £000 | 2018-19 Estimate £000 | 2019-20 Estimate £000 |
|---|---|---|---|---|---|
| 102 | 94 | Interest cost | 86 | 86 | 86 |
| 3 | 2 | Finance lease interest | 2 | 1 | 1 |
| 588 | 550 | MRP | 512 | 478 | 446 |
| **693** | **646** | **Total** | **600** | **565** | **533** |
| **24,513** | **25,541** | **Council tax** | **26,449** | **27,244** | **28,063** |
| **2.83** | **2.53** | **Ratio** | **2.27** | **2.07** | **1.90** |

**Minimum Revenue Provision (MRP) Strategy**

19. The Authority is required to make an annual provision from revenue to contribute towards the repayment of borrowing. This requirement arises under the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008, which simplifies earlier MRP requirements by placing a duty on the Authority to determine each year an amount of minimum revenue provision, which it considers to be prudent. In order to assist the Authority with this determination, guidance for assessing what would represent a prudent provision has been issued under Section 21 (1A) of the Local Government Act 2003 (The Guidance). The Authority is required to have regard to the Guidance when considering the amount of their annual "prudent" MRP.

20. It is proposed that the MRP for 2017-18 will continue to be charged at the rate of 6.7% of the opening Capital Financing Requirement. It is the Head of Finance's professional opinion that this approach continues to meet the statutory duty to make prudent revenue provision.

21. Based on the current projected capital outturn position for 2016-17, it is expected that this will equate to a charge of approximately £512k for 2017-18.

22. The policy will be reviewed on an annual basis. If it is proposed to vary the strategy during the year, a revised statement will be submitted to the Authority.

## Treasury Management Issues

23. The capital expenditure plan above shows the capital funds required by the Authority. The treasury management function ensures that the Authority's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this requirement. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant Treasury Prudential indicators, (including the current and projected debt positions) and the borrowing and annual investment strategy.

**Treasury Prudential Indicators: limits to borrowing activity**

Gross borrowing requirement

24. Within the code there is a key indicator of prudence that ensures that, over the medium term, gross borrowing is only for a capital purpose. This is shown below, and compares gross external borrowing to the total CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years. Gross external borrowing should not exceed this limit except in the short term.

| **2015-16 Actual £000** | **2016-17 Estimate £000** | **Gross Borrowing Requirement** | **2017-18 Estimate £000** | **2018-19 Estimate £000** | **2019-20 Estimate £000** |
|---|---|---|---|---|---|
| | | **External Debt** | | | |
| 2,258 | 2,247 | Debt at 1 April | 1,914 | 1,903 | 1,892 |
| (11) | (333) | Expected change in Debt | (11) | (11) | (880) |
| 2,247 | 1,914 | External Debt at 31 March | 1,903 | 1,892 | 1,012 |
| 59 | 48 | Finance Lease | 37 | 25 | 13 |
| (11) | (11) | Expected change in Finance Lease | (12) | (12) | (13) |
| 2,295 | 1,951 | Actual Gross Debt at 31 March | 1,928 | 1,905 | 1,012 |
| 8,195 | 7,645 | Capital Financing Requirement | 7,133 | 6,655 | 6,209 |
| **5,900** | **5,694** | **Under / (over) borrowing** | **5,205** | **4,750** | **5,197** |

25. The Head of Finance reports that he does not envisage the position indicated above leading to future difficulties for the Authority. This view takes into account current commitments, existing plans, and the proposals in the budget report.

The operational boundary

26. This is the limit which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

| 2015-16 Actual £000 | 2016-17 Estimate £000 | Operational Boundary | 2017-18 Estimate £000 | 2018-19 Estimate £000 | 2019-20 Estimate £000 |
|---|---|---|---|---|---|
| 2,396 | 2,053 | Debt | 2,032 | 2,011 | 1,121 |
| 60 | 60 | Other long term liabilities | 60 | 60 | 60 |
| **2,456** | **2,113** | **Total** | **2,092** | **2,071** | **1,181** |

Authorised Limit for external debt

27. This indicator demonstrates 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 Authority. 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.

| 2015-16 Actual £000 | 2016-17 Estimate £000 | Authorised limit for external debt | 2017-18 Estimate £000 | 2018-19 Estimate £000 | 2019-20 Estimate £000 |
|---|---|---|---|---|---|
| 4,296 | 3,953 | Borrowing | 4,032 | 4,011 | 3,121 |
| 100 | 100 | Other Long Term Liabilities | 100 | 100 | 100 |
| **4,396** | **4,053** | **Total Authorised Limit** | **4,132** | **4,111** | **3,221** |

28. In agreeing these limits, it should be noted that the Authorised Limit for 2017-18 will be 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 authorities' plans, or those of a specific authority, although this power has not yet been exercised.

Maturity structure of debt

29. It is recommended that the Authority sets upper and lower limits for the maturity structure of its debt for the forthcoming year as follows:

| Maturity Structure of Authority Borrowing | Lower Limit % | Upper Limit % |
|---|---|---|
| Under 12 months | 0% | 25% |
| 12 months to 2 years | 0% | 25% |
| 2 years to 5 years | 0% | 50% |
| 5 years to 10 years | 0% | 60% |
| 10 years and above | 5% | 100% |

30. The above percentages are the ranges for the projected borrowing maturing in each year out of the total projected borrowing. The indicator is designed to be a control over the Authority having large concentrations of fixed interest rate debt needing to be replaced at any one time and thus being at risk of having to borrow large amounts when interest rates may be unfavourable.

Fixed interest rate exposure

31. The table below shows the Authority's upper limit for fixed interest rate exposure for the next three years. This indicator shows the percentage of borrowing that can be undertaken at fixed interest rates. Up to 100% of borrowing can be at fixed interest rates. Again, this indicator is set at levels to reduce the risk from interest rate movements.

| **Upper Limit –<br>Fixed Interest Rate Exposure** | **2016-17<br>%** | **2017-18<br>%** | **2018-19<br>%** |
|---|---|---|---|
| Fixed Interest Rates | 100 | 100 | 100 |

Variable interest rate exposure

32. The following indicator shows the percentage of borrowing that can be undertaken at variable interest rates. The purpose of the indicator is to restrict variable rate borrowing in order to reduce the risk from sudden movements in interest rates. The Authority sets its upper limit for borrowing at variable rates at 40%.

| **Upper Limit –<br>Variable Interest Rate Exposure** | **2016-17<br>%** | **2017-18<br>%** | **2018-19<br>%** |
|---|---|---|---|
| Variable Interest Rates | 40 | 40 | 40 |

**Prospects for Interest Rates**

33. Warrington Borough Council, who advise the Authority on treasury management, has appointed Capita Asset Services to assist and advise the Council and the Authority to formulate a view on interest rates.

Capita Asset Services' interest rate forecast

34. The following table gives their central view:

| | **Bank Rate** | **PWLB Borrowing Rates** | | |
|---|---|---|---|---|
| | | **5 year** | **25 year** | **50 year** |
| Mar-17 | 0.25% | 1.60% | 2.90% | 2.70% |
| Jun-17 | 0.25% | 1.60% | 2.90% | 2.70% |
| Sep-17 | 0.25% | 1.60% | 2.90% | 2.70% |
| Dec-17 | 0.25% | 1.60% | 3.00% | 2.80% |
| Mar-18 | 0.25% | 1.70% | 3.00% | 2.80% |
| Jun-18 | 0.25% | 1.70% | 3.00% | 2.80% |
| Sep-18 | 0.25% | 1.70% | 3.10% | 2.90% |
| Dec-18 | 0.25% | 1.80% | 3.10% | 2.90% |
| Mar-19 | 0.25% | 1.80% | 3.20% | 3.00% |
| Jun -19 | 0.50% | 1.90% | 3.20% | 3.00% |
| Sep-19 | 0.50% | 1.90% | 3.30% | 3.10% |
| Dec-19 | 0.75% | 2.00% | 3.30% | 3.10% |
| Mar-20 | 0.75% | 2.00% | 3.40% | 3.20% |

35. The Monetary Policy Committee, (MPC), cut Bank Rate from 0.50% to 0.25% on 4th August in order to counteract what it forecast was going to be a sharp slowdown in growth in the second half of 2016. It also gave a strong steer that it was likely to cut Bank Rate again by the end of the year. However, economic data since August has indicated much stronger growth in the second half of 2016 than that forecast. Also, inflation forecasts have risen substantially as a result of a continuation of the sharp fall in the value of sterling since early August. Consequently, Bank Rate was not cut again in November and, on current trends, it now appears unlikely that there will be another cut, although that cannot be completely ruled out if there was a significant dip downwards in economic growth.

36. During the two-year period 2017 – 2019, when the UK is negotiating the terms for withdrawal from the EU, it is likely that the MPC will do nothing to dampen growth prospects, (i.e. by raising Bank Rate), which will already be adversely impacted by the uncertainties of what form Brexit will eventually take. Accordingly, a first increase to 0.50% is not tentatively pencilled in, as in the table above, until quarter 2 2019, after those negotiations have been concluded, (though the period for negotiations could be extended). However, if strong domestically generated inflation, (e.g. from wage increases within the UK), were to emerge, then the pace and timing of increases in Bank Rate could be brought forward.

37. Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The above forecasts, (and MPC decisions), will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

38. The overall longer run trend is for gilt yields and PWLB rates to rise, albeit gently. It has long been expected that at some point, there would be a start to a switch back from bonds to equities after a historic long term trend over about the last twenty five years of falling bond yields. The action of central banks since the financial crash of 2008, in implementing substantial quantitative easing purchases of bonds, added further impetus to this downward trend in bond yields and rising prices of bonds.

39. The opposite side of this coin has been a rise in equity values as investors searched for higher returns and took on riskier assets. The sharp rise in bond yields since the US Presidential election, has called into question whether, or when, this trend has, or may, reverse, especially when America is likely to lead the way in reversing monetary policy.

40. Until 2015, monetary policy was focused on providing stimulus to economic growth but has since started to refocus on countering the threat of rising inflationary pressures as strong economic growth becomes more firmly established. The expected substantial rise in the Fed. rate over the next few years may make holding US bonds much less attractive and cause their prices to fall, and therefore bond yields to rise.

41. Rising bond yields in the US would be likely to exert some upward pressure on bond yields in other developed countries but the degree of that upward pressure is likely to be dampened by how strong, or weak, the prospects for economic growth and

rising inflation are in each country, and on the degree of progress in the reversal of monetary policy away from quantitative easing and other credit stimulus measures.

42. PWLB rates and gilt yields have been experiencing exceptional levels of volatility that have been highly correlated to geo-political, sovereign debt crisis and emerging market developments. It is likely that these exceptional levels of volatility could continue to occur for the foreseeable future.

43. The overall balance of risks to economic recovery in the UK is negative, particularly in view of the current uncertainty over the final terms of Brexit and the timetable for its implementation.

44. Apart from the above uncertainties, negative risks to current forecasts for UK gilt yields and PWLB rates currently include:

- Monetary policy action by the central banks of major economies reaching its limit of effectiveness and failing to stimulate significant sustainable growth, combat the threat of deflation and reduce high levels of debt in some countries, combined with a lack of adequate action from national governments to promote growth through structural reforms, fiscal policy and investment expenditure.
- Major national polls:
  - Italian constitutional referendum 4.12.16;
  - Spain has a minority government with only 137 seats out of 350 after already having had two inconclusive general elections in 2015 and 2016. This is potentially highly unstable.
  - Dutch general election 15.3.17;
  - French presidential election April/May 2017;
  - French National Assembly election June 2017;
  - German Federal election August – October 2017.
- A resurgence of the Eurozone sovereign debt crisis, with Greece being a particular problem, and stress arising from disagreement between EU countries on free movement of people and how to handle a huge influx of immigrants and terrorist threats
- Weak capitalisation of some European banks, especially Italian.
- Geopolitical risks in Europe, the Middle East and Asia, causing a significant increase in safe haven flows.
- UK economic growth and increases in inflation are weaker than we currently anticipate.
- Weak growth or recession in the UK's main trading partners - the EU and US.

45. The potential for positive risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates, include: -

- UK inflation rising to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium in gilt yields.
- A rise in US Treasury yields as a result of Fed. funds rate increases and rising inflation expectations in the USA, dragging UK gilt yields upwards.

- The pace and timing of increases in the Fed. funds rate causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.
- A downward revision to the UK's sovereign credit rating undermining investor confidence in holding sovereign debt (gilts).

Investment and borrowing rates

46. Investment returns are likely to remain low during 2017-18 and beyond. Borrowing interest rates have been on a generally downward trend during most of 2016 up to mid-August; they fell sharply to historically phenomenally low levels after the referendum and then even further after the MPC meeting of 4th August when a new package of quantitative easing purchasing of gilts was announced. Gilt yields have since risen sharply due to a rise in concerns around a 'hard Brexit', the fall in the value of sterling, and an increase in inflation expectations.

47. The policy of avoiding new borrowing by running down spare cash balances, has served the Authority well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in later times when authorities will not be able to avoid new borrowing to finance capital expenditure and/or to refinance maturing debt.

48. There will be a potential cost attached to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost, being the difference between borrowing costs and investment returns.

49. Please see attached Appendix 2 for a more detailed economic background.

**Borrowing Strategy**

50. The capital expenditure plan provides details of the capital requirement of the Authority. The treasury management function ensures that the Authority's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet thisrequiremnet. This will involve both the organisation of the cash flow and, where the capital plan requires, the organisation of appropriate borrowing facilities.

51. In general, the Authority will borrow for one of two purposes – to finance cash flow in the short-term or to fund capital investment over the longer term. The Authority is currently maintaining an under-borrowed position. This means that the capital borrowing need (CFR), has not been fully funded with loan debt as cash supporting the Authority's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is high.

52. A key aim of the Treasury Management Strategy is to minimise the cost of the Authority's loan portfolio whilst ensuring that the obligation to repay the loan is spread over a period of time. This reduces the impact on the revenue budget of interest payments.

53. Currently the average rate of interest on the Authority's loan portfolio is 4.51%.

54. The Authority is not projecting a borrowing requirement during the life of its Medium Term Financial Plan to 2020-21. If it were to become necessary, the Authority will borrow from either the Public Works Loans Board (PWLB), the bond market or other Local Authorities during the strategy period.

55. The Head of Finance will monitor interest rates in financial markets in conjunction with Warrington Borough Council and adopt a pragmatic approach to changing circumstances, should any borrowing become required:

- If it was felt that there was a significant risk of a sharp fall in long and short term rates then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- 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 with the likely action that fixed rate funding will be drawn whilst interest rates are still lower than they will be in the next few years.

56. Any decisions will be reported to the Fire Authority at the next available opportunity.

57. The Authority's policy for 2017-18 will be to run down investments to maximise returns and minimise risks. However, an assessment of the opportunity for borrowing will be made on the cost of borrowing long-term dependent on the interest rate movements.

**Policy on Borrowing in Advance of Need**

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

59. In determining whether borrowing will be undertaken in advance of need the Authority will:

- 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;
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered;
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
- consider the merits and demerits of alternative forms of funding;
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use;

- consider the impact of borrowing in advance on temporarily increased investment cash balances, which would lead to an increase in exposure to counterparty risk.

**Debt Rescheduling**

60. As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

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

    (a) The generation of cash savings and / or discounted cash flow savings;

    (b) Fulfilment of the borrowing strategy outlined above;

    (c) Enhancement of the balance of the portfolio (amending the maturity profile and/or the balance of volatility).

62. 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.

63. All rescheduling will be reported to the Fire Authority at the earliest meeting following this action.

**Annual Investment Strategy**

64. The aim of our investment strategy is to:

    - Maintain capital security;
    - Maintain policy flexibility.

65. The Head of Finance, under delegated powers, will undertake the most appropriate form of investments depending on the prevailing interest rates at the time, taking into account the risks.

66. The Authority invests surplus cash balances only with certain approved organisations, as security of funds is of primary importance. All investments will be made in accordance with the Authority's investment policies and prevailing legislation and regulations.

<u>Investment Policy</u>

67. The Authority will have regard to the DCLG's Guidance on Local Government Investments ("the Guidance") issued in March 2004, any revisions to that guidance, the Audit Commission's report on Icelandic investments and the 2009 and revised 2011 CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code").

68. The Authority will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite of this Authority is low in order to give priority to security of its investments.

69. In accordance with guidance from DCLG and CIPFA, and in order to minimise the risk to investments, the Authority has stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list, which also enable diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

70. 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 this end the Authority will engage with Warrington Borough Council and its advisors to maintain and monitor on market pricing such as “credit default swaps” and overlay that information on top of the credit ratings. This is integrated into the credit methodology provided by the Warrington Borough Council’s advisors, Capita Asset Services in producing its colour coding which show the varying degrees of suggested creditworthiness.

71. 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.

72. The Authority maintains a list of highly creditworthy counterparties, which will also enables diversification and thus avoidance of concentration of risk. The strategy helps to provide security of investment and minimisation of risk.

73. Investment instruments identified for use in the financial year are listed below under the ‘Specified’ and ‘Non-Specified’ investments categories. Counterparty limits will be as set through the Authority’s Treasury Management Practices Statement.

Specified Investments (maturities up to one year)

- Bank and Building Society Term Deposits
- Other Local Authority Term Deposits
- Debt Management Agency Deposit Facility
- Money Market Fund
- Government Liquidity Fund

Non-specified Investments (maturities over one year)

- Bank and Building Society Term Deposits
- Other Local Authority Term Deposits
- Money Market Funds

Other Non-specified Investments

- Fixed term deposits with variable rate and variable maturities
- Local Authority Mortgage Schemes

Counterparty Limits

| | **Maximum Limit** |
|---|---|
| **1. Specified Investments (limit per counterparty)** | |
| UK Government | Unlimited |
| Local Authorities | £10.0m |
| Money Market Funds with a minimum rating AAA | £10.0m |
| Institutions with a minimum rating of AAA or A1 | £10.0m |
| Pooled Fund Institution with a minimum rating of AAA or A1 | £10.0m |
| Institutions with a minimum rating of AA- or A2 | £7.5m |
| Institutions with a minimum rating of A- or A2 | £5.0m |
| Building Societies – assets greater than £5,000 million | £2.5m |
| Building Societies – assets greater than £1,000 million | £1.75m |
| Building Societies – assets greater than £250 million | £1.0m |
| | |
| **2. Non-specified Investments (limit per counterparty)** | |
| Investments for more than 365 days | £5.0m |
| Other non specified investments | £5.0m |
| | |
| **3.Other limits (on day of investment)** | |
| Aggregate value of non specified investments | £10.0m |

Creditworthiness Policy

74. The Authority uses the creditworthiness service provided by Capita Asset Services on behalf of Warrington Borough Council. This service employs a sophisticated modelling approach utilising credit ratings from all three rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings of counterparties are supplemented with the following overlays:

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

75. The creditworthiness service uses a wider array of information than just primary ratings and by using a risk weighted scoring system, does not give undue weight to just one agency's ratings.

76. Typically the minimum credit ratings criteria the Authority use will be a short term rating (Fitch or equivalents) of short term rating F1, long term rating A-, viability

rating of a-, and a support rating of 1. 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.

77. All credit ratings will be monitored weekly by Warrington Borough Council, which is alerted to changes to ratings of all three agencies through its use of the Capita creditworthiness service:

    - If a downgrade results in the counterparty/investment scheme no longer meeting the Authority's minimum criteria, its further use as a new investment will be withdrawn immediately;
    - In addition to the use of Credit Ratings the Authority will be advised of information in movements in Credit Default Swap (CDS) against the iTraxx (CDS product brand name) benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Authority's lending list.

78. Sole reliance will not be placed on the use of this external service. In addition this Authority will also use market data and information, information on government support for banks and the credit ratings of that government support.

<u>Country Limits</u>

79. The Authority 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 them). The list will be added to, or deducted from by officers should ratings change in accordance with this policy.

<u>Liquidity of Investments</u>

80. The maximum period of investment of Authority money will be ten years. There will be no more than £10m committed for a period over 5 years.

**Policy on the use of External Service Providers**

81. The Authority uses Warrington Borough Council as its external treasury management advisers. They in turn use Capita Services to advise them.

82. The Authority 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.

83. 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 Authority 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.

**Treasury Management Scheme of Delegation**

84. The scheme of delegation is in the Authority's Treasury Management Practices statement which will be reported to the Fire Authority on an annual basis.