APPENDIX 1

TREASURY MANAGEMENT STRATEGY 2021-22

INTRODUCTION

1.1 Cheshire Fire Authority ("the Authority") is required to operate a balanced budget meaning that cash raised during the year from grants, council tax and other income sources will match the cash expenditure for the year. The first requirement of treasury management is to ensure that this cashflow is adequately planned with cash being available when it is needed. Surplus funds are invested in low risk counterparties or financial instruments commensurate with a low risk appetite, that offer adequate liquidity (i.e. ease of access) before considering any return on the investment. The investment strategy objectives are, in order of priority, security, liquidity and then yield.

1.2 The second main function of treasury management is the funding of the capital programme. The capital programme and plans provide a guide to the Authority's borrowing requirement which is essentially the longer-term cashflow planning to ensure that the capital programme commitments can be met. The management of longer-term cashflow may involve arranging long or short-term loans or by using cashflow surpluses. Any debt currently held may also be re-structured when favourable conditions arise and in line with risk and/or cost objectives.

1.3 The contribution the treasury management function makes to the organisation 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 balance on the General Reserve.

1.4 The Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as:

'*The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.'*

1.5 The CIPFA 2017 Prudential and Treasury Management Codes require the preparation of a Capital Strategy providing a longer-term focus to capital plans including:

- a high-level long term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed

- the implications for future financial sustainability

The Capital Strategy is being reported separately as part of the annual budget report pack.

1.6 This Authority has not engaged in any commercial investments and has no non-treasury investments.

2. TREASURY MANAGEMENT REPORTING REQUIREMENTS

2.1 The Authority is required to receive and approve, as a minimum, three main reports each year which incorporate policies, estimates and actual income and expenditure.

Prudential and Treasury Indicators and Treasury Strategy (this report) – the first and most important report covering:

- the capital plans (including prudential indicators);
- a minimum revenue provision (MRP) policy statement (how residual capital expenditure is charged to revenue over time);
- the Treasury Management Strategy (how the investments and borrowings are to be organised and includes the treasury indicators); and
- an Investment Strategy (the parameters on how investments are to be managed).

A Mid-Year Treasury Management Report – this updates the Authority on the progress of the capital position, updates prudential indicators as necessary, and whether the actual execution of treasury management is in line with the Strategy or whether any policies need revision. Should there be a particularly volatile period affecting treasury management then more frequent reports will be submitted.

An Annual Treasury Management 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.

3. TREASURY MANAGEMENT STRATEGY 2021-22

3.1 The Treasury Management Strategy covers two main areas:-

Capital:

- The capital plans and associated prudential indicators; and
- The minimum revenue provision (MRP) statement.

Treasury Management:

- The current position;
- Prudential indicators which limit the treasury risks and activities of the Authority;
- Prospects for interest rates;
- The borrowing strategy;
- The policy on borrowing in advance of need;
- Debt rescheduling;

- The investment strategy;
- The policy on creditworthiness; and
- The policy on using external service providers in relation to Treasury Management.

3.2 The above cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, Communities and Local Government's Minimum Revenue Provision (MRP) Guidance; the CIPFA Treasury Management Code and the Communities and Local Government's Investment Guidance.

3.3 The CIPFA Treasury Management Code requires the responsible officer (the Fire Authority Treasurer) to ensure that anyone with responsibility for treasury management receives adequate training. The external treasury management supplier will provide suitable training during the year as appropriate.

3.4 The joint Police and Fire Finance team will manage all day to day Treasury management services on behalf of the Authority, supported directly by Link Asset Services, Treasury Solutions as its external treasury management advisors. However, it is recognised that responsibility for treasury management decisions remains with the Authority at all times and overdue reliance will not be placed upon one source of advice alone. Nevertheless, it is also recognised that there is value in employing external advisors in order to gain access to specialist skills and resources.

4. CAPITAL EXPENDITURE PRUDENTIAL INDICATORS 2021-24

4.1 Capital expenditure

4.1.1 Capital expenditure plans are a key driver of treasury management activity. The funding of such plans impact on cash balances and borrowing requirements in the short and longer terms. The on-going consequences of these decisions have a direct impact on the annual revenue budget. As such, the following prudential indicators show the proposed capital expenditure plans, how they are to be funded, the impact on the organisation's finances and their affordability in terms of the impact on revenue budgets.

4.1.2 This prudential indicator is a summary of the Authority's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. These are based on actual and current forecast cash spend along with the planned future capital programme.

Table 1: Capital Expenditure

2020-21 Estimate £000	2021-22 Estimate £000	2022-23 Estimate £000	2023-24 Estimate £000
14,797	8,228	13,354	4,378

4.1.3 The next table shows how the above capital expenditure is to be financed. Where there is a shortfall in available funds, the shortfall is covered by an additional borrowing requirement. It is anticipated that c£21m of additional borrowing will be required over the period to finance the new operational training centre and other planned major build projects.

Table 2: Capital Financing

2020-21 Estimate £000		2021-22 Estimate £000	2022-23 Estimate £000	2023-24 Estimate £000
14,797	Forecast Spend	8,228	13,354	4,378
	Financed by:			
0	General capital grants	0	0	0
0	Specific capital grants	0	0	0
430	Capital Receipts	450	0	0
7,964	Capital Reserves & Revenue Contributions	3,778	5,354	2,378
6,403	Borrowing requirement	4,000	8,000	2,000

4.2 Capital Financing Requirement (or borrowing needs)

4.2.1 The second prudential indicator is the Authority's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been financed either from revenue or capital funds. It is essentially a measure of borrowing need and any capital expenditure not financed in the above table will increase the CFR.

4.2.2 It should be noted that the CFR increases during the period of the current MTFP, reflecting the new borrowing requirement due to planned capital expenditure, and a reduction in alternative capital funding sources.

Table 3: Capital Financing Requirement (CFR)

2020-21 Estimate £000	Capital Financing Requirement (CFR)	2021-22 Estimate £000	2022-23 Estimate £000	2023-24 Estimate £000
6,807	CFR brought forward	**12,794**	**16,126**	**23,324**
6,403	Net financing need for the year	4,000	8,000	2,000
(416)	Less MRP	(668)	(802)	(1,098)
12,794	**CFR carried forward**	**16,126**	**23,324**	**24,226**
5,987	**Movement in CFR**	**3,332**	**7,198**	**902**

4.2.3 The CFR is reduced every year by the minimum revenue provision (MRP). The Authority is required by statute to set aside MRP each year for the repayment of external debt. Under amendment regulation 4(1) of the 2008 Regulations, the Authority is charged with a simple duty to set aside MRP which it considers to be prudent. Guidance has been issued which sets out recommendations on the interpretation of 'prudent' and the Authority is required to prepare an annual statement on how it proposes to calculate MRP. The 2021-22 annual statement is set out in the Annex.

4.3 Core Funds and Expected Investment Balances

4.3.1 The application of funds (capital receipts, reserves etc.) to finance capital expenditure or other budget decisions to support the revenue budget will have an on-going impact on the cash available for investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are the estimated year-end balances for reserves. The Capital Receipts and Unapplied Capital Grants reserves are restricted in their usage to funding capital expenditure or repaying debt and cannot be used for revenue purposes.

Table 4: Reserves

Reserves	**31 March 2020 Actual £000**	**31 March 2021 Estimate £000**	**31 March 2022 Estimate £000**	**31 March 2023 Estimate £000**	**31 March 2024 Estimate £000**
Earmarked Revenue Reserves					
IRMP Reserve	8,296	6,169	4,039	535	7
Resource Centre Managers Reserves	6,227	4,761	5,035	4,971	4,314
Community Risk Reduction Reserve	344	344	344	344	344
Unitary Performance Group Reserve	120	120	120	120	120
	14,987	11,394	9,538	5,970	4,785
Capital Reserves					
Usable Capital Receipts	0	100	0	0	0
Revenue Reserve for Capital Expenditure	4,266	52	0	0	0
Unapplied Capital Grants	0	0	0	0	0
	4,266	152	0	0	0
General Reserve					
General Fund	2,210	2,210	2,210	2,210	2,210
Total Reserves	**21,463**	**13,756**	**11,748**	**8,180**	**6,995**

Affordability Prudential Indicators

4.3.2 So far the Strategy has covered the control of overall capital expenditure plans and borrowing prudential indicators. The following indicator provides an indication of the impact of the above capital expenditure plans and their financing proposals on the overall finances and precept (council tax).

Table 5: Ratio of financing costs to net revenue funding

2019-20 Actual	2020-21 Estimate	2021-22 Estimate	2022-23 Estimate	2023-24 Estimate
0.66%	0.91%	1.97%	2.79%	3.45%

4.3.3 This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream. The estimates of financing costs include current commitments and the proposals included in the budget/medium-term financial plan. The ratios are increasing due to the requirement to increase borrowing in order to finance the capital programme from 2018-19 onwards, most notably new debt repayment provision (MRP) in respect of the new Operational Training Centre and planned replacement fire station at Crewe and emergency services facility on the Wilmslow Fire Station site.

5. BORROWING

5.1 The capital expenditure plans set out in Section 4 provide details of the capital plans of the Authority. A key function of treasury management is to ensure that the cash resources are organised in accordance with the relevant regulations and professional codes so that sufficient cash is available to meet service activity and the capital strategy. This will involve both cashflow management and where capital expenditure plans require it, the arrangement of appropriate borrowing facilities. This Strategy covers the relevant treasury and prudential indicators, the current and projected debt positions and the Annual Investment Strategy.

Current Debt Position

5.1.1 The current debt position, as at 31 March 2020, with forward projections is summarised below. The table shows actual external debt against the underlying capital borrowing need highlighting any internal borrowing or over borrowing.

Table 6: Debt Position

2019-20 Actual £000	2020-21 Estimate £000	Gross Borrowing Requirement	2021-22 Estimate £000	2022-23 Estimate £000	2023-24 Estimate £000
		External Debt			
1,892	1,012	Debt at 1 April	1,012	12,012	20,012
(880)	0	Expected change in Debt	11,000	8,000	1,574
1,012	1,012	External Debt at 31 March	12,012	20,012	21,586
13	0	Finance Lease	0	0	0
(13)	0	Expected change in Finance Lease	0	0	0
1,012	1,012	Actual Gross Debt at 31 March	12,012	20,012	21,586
6,807	12,794	Capital Financing Requirement	16,126	23,324	24,226
5,795	**11,782**	**Internal / (over) borrowing**	**4,114**	**3,312**	**2,640**

5.1.2 Within the prudential indicators there are a number of key indicators to ensure that the Authority operates its activities within well-defined limits. One of these is that the Authority ensures that its gross debt does not, except in the short-term, exceed the total Capital Financing Requirement in the preceding year plus the estimates for any additional Capital Financing Requirement for 2021-22 and the following two financial years. This allows some flexibility for limited early borrowing for future plans but ensures that borrowing is not undertaken for revenue or speculative purposes.

5.1.3 The Treasurer confirms that the Authority complied with this prudential indicator in the current year and does not envisage any issues for the immediate future. This view takes into account current commitments, existing plans and the proposals included in the budget report and Medium Term Financial Plan for 2021-26 to be considered by the Fire Authority on 10th February 2021.

5.2 Treasury Indicators – limits to borrowing activities

5.2.1 There are two limits to borrowing, the operational boundary and the authorised limit for external debt. These are the current debt position as shown in 5.1.1 above plus the forecast requirement for external financing over the next three years.

5.2.2 **The operational boundary** is the limit which external debt and long-term liabilities is not normally expected to exceed. In most cases this would be a similar figure to the Capital Financing Requirement but may be higher or lower depending on the level of actual debt and repayment schedules. Temporary breach of the operational boundary is not in itself cause for concern but an indicator that such liabilities should be reviewed. If there was a sustained breach, (such as an increase in long-term borrowing), then this would need to be investigated and action taken.

5.2.3 The operational boundaries below are based on estimating the Authority's most likely level of borrowing and leasing each year. It includes long-term borrowing to fund capital expenditure plans, short-term temporary borrowing for cashflow purposes and the impact of any finance leases.

Table 7: Operational Boundary

Operational Boundary	**2021-22 Estimate £000**	**2022-23 Estimate £000**	**2023-24 Estimate £000**
Debt	12,112	20,112	21,686
Other long term liabilities	100	100	100
Total	**12,212**	**20,212**	**21,786**

5.2.4 As Table 7 shows, the Operational Boundary over the period 2021-24 is increasing because of the planned borrowing to support the capital programme.

5.2.5 The **authorised limit for external debt** is a further key prudential indicator representing a control on the maximum level of borrowing. This represents a limit beyond which external debt and finance leases are prohibited and is set or revised by the Authority. It reflects the level of such debt which, while not desired, could be afforded in the short term but is not sustainable in the longer-term.

5.2.6 This is a 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 local authorities' plans or those of any specific public body; although this power has yet to be exercised.

5.2.7 There is a statutory requirement for the Authority to confirm the authorised limit. This is set out in the table below:

Table 8: Authorised Limit

Authorised limit for external debt	**2021-22 Estimate £000**	**2022-23 Estimate £000**	**2023-24 Estimate £000**
Borrowing	14,112	22,112	23,686
Other Long Term Liabilities	100	100	100
Total Authorised Limit	**14,212**	**22,212**	**23,786**

5.3 Prospects for Interest Rates

5.3.1 Link Asset Services have been appointed as external treasury advisor and part of their service is to assist the Authority to formulate a view on interest rates. The following table gives our central view.

Link Group Interest Rate View 9.11.20

These Link forecasts have been amended for the reduction in PWLB margins by 1.0% from 26.11.20

	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
5 yr PWLB	0.80	0.80	0.80	0.80	0.80	0.90	0.90	0.90	0.90	0.90	1.00	1.00	1.00	1.00
10 yr PWLB	1.10	1.10	1.10	1.10	1.10	1.20	1.20	1.20	1.20	1.20	1.30	1.30	1.30	1.30
25 yr PWLB	1.50	1.50	1.60	1.60	1.60	1.60	1.70	1.70	1.70	1.70	1.80	1.80	1.80	1.80
50 yr PWLB	1.30	1.30	1.40	1.40	1.40	1.40	1.50	1.50	1.50	1.50	1.60	1.60	1.60	1.60

Source: Link Asset Services

5.3.2 The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its subsequent meetings to date, although some forecasters had suggested that a cut into negative territory could happen. However, the Governor of the Bank of England has made it clear that he currently thinks that such a move would do more damage than good and that more quantitative easing is the favoured tool if further action becomes necessary.

5.3.3 As shown in the forecast table above, no increase in Bank Rate is expected in the forecast table above as economic recovery is expected to be only gradual and, therefore, prolonged.

5.3.4 There was much speculation during the second half of 2019 that bond markets were in a bubble which was driving bond prices up and yields down to historically very low levels. The context for that was a heightened expectation that the US could have been heading for a recession in 2020. In addition, there were growing expectations of a downturn in world economic growth, especially due to fears around the impact of the trade war between the US and China, together with inflation generally at low levels in most countries and expected to remain subdued. Combined, these conditions were conducive to very low bond yields. While inflation targeting by the major central banks has been successful over the last thirty years in lowering inflation expectations, the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers. This means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. The consequence of this has been the gradual lowering of the overall level of interest rates and bond yields in financial markets over the last 30 years.

5.3.5 Over the year prior to coronavirus, this has seen many bond yields up to 10 years turn negative in the Eurozone. In addition, there has, at times, been an inversion of bond yields in the US whereby 10 year yields have fallen below shorter term yields. In the past, this has been a precursor of a recession. The other side of this is that bond prices are elevated as investors would be expected to be moving out of riskier assets i.e. shares, in anticipation of a downturn in corporate earnings and so selling out of equities.

5.3.6 Gilt yields had therefore already been on a generally falling trend up until the coronavirus crisis hit western economies during March 2020. After gilt yields spiked up during the financial crisis in March, we have seen these yields fall sharply to unprecedented lows as investors panicked during March in selling shares in anticipation of impending recessions in western economies, and moved cash into safe haven assets i.e. government bonds.

5.3.7 However, major western central banks took rapid action to deal with excessive stress in financial markets during March, and started massive quantitative easing purchases of government bonds: this also acted to put downward pressure on government bond yields at a time when there has been a huge and quick expansion of government expenditure financed by issuing government bonds. Such unprecedented levels of issuance in “normal” times would have caused bond yields to rise sharply. Gilt yields and PWLB rates have been at remarkably low rates so far during 2020-21.

5.3.8 As the interest forecast table for PWLB certainty rates above shows, there is expected to be little upward movement in PWLB rates over the next two years as it will take economies, including the UK, a prolonged period to recover all the momentum they have lost in the sharp recession caused during the coronavirus shut down period. From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and sharp changes in investor sentiment, (as shown on 9th November when the first results of a successful COVID-19 vaccine trial were announced). Such volatility could occur at any time during the forecast period.

Investment and borrowing rates

5.3.9 Investment returns are likely to remain exceptionally low during 2021-22 with little increase in the following two years.

5.3.10 Borrowing interest rates fell to historically very low rates as a result of the coronavirus crisis and the quantitative easing operations of the Bank of England: indeed, gilt yields up to 6 years were negative during most of the first half of 2020-21. The policy of avoiding new borrowing by running down spare cash balances has served local authorities well over the last few years. The unexpected increase of 1% in PWLB rates on top of the then current margin over gilt yields in October 2019 required an initial major rethink of local authority treasury management strategy. As a consequence of these increases in margins, the Authority decided to refrain from new PWLB borrowing, if possible, until such time as the additional 1% margin was removed.

5.3.11 On 25 November 2020, the Chancellor announced the conclusion to a review of margins over gilt yields for PWLB rates; the standard and certainty margins were reduced by 1% but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which intends to purchase assets in order to simply generate a return as part of its three year capital programme.

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

5.3.13 As Link's long-term forecast for Bank Rate is 2.00%, and all PWLB rates are under 2.00%, there is now value in borrowing from the PWLB for all types of capital expenditure for all maturity periods, especially as current rates remain at historic lows. The Authority will assess its borrowing requirement in conjunction with budgetary pressures to reduce total interest costs and long term borrowing will be undertaken for the purpose of certainty, and to secure long term favourable interest rates at the appropriate time.

5.4 Borrowing Strategy

5.4.1 As shown in Table 6, the Authority is currently utilising internal borrowing and forecast to remain so for the period covered by this Strategy. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting reserves, balances and cash flow has been used as a temporary measure. This Strategy is appropriate for the current economic scenario and prudent given that limited investment return on surplus cash flow and counter-party risk are still issues that need to be considered.

5.4.2 As capital reserves and therefore cash resources available are being used to fund the ongoing capital programme, historic internal borrowing levels are no longer sustainable. At this point, and in line with the current Treasury Management Strategy, temporarily increasing under-borrowing to c£12m by the end of 2020-21 is considered to be manageable and a sensible position in view of available cash reserves and almost non-existent returns that can be achieved on cash balances invested. However, as cash reserves are utilised to finance planned capital expenditure this will no longer be sustainable and a level of c£3m is currently considered more appropriate going forward.

5.4.3 Against this background and the risks within the economic forecast, caution will be adopted with the 2021-22 treasury operations. The Treasurer will keep interest rates and the cashflow under continual review in order to adopt a pragmatic approach to changing circumstances, supported by advice from the external Treasury Management advisers. It may at some point be necessary to reduce internal borrowing further if cash reserves continue to reduce due to ongoing budget pressures by securing additional new external borrowing above that forecast to fund the ongoing capital programme in Table 2 although this is not anticipated in the short or medium term.

5.4.4 A key aim of the borrowing strategy is to minimise the cost of the loan portfolio whilst ensuring that the obligation to repay the loans is spread out over a period of time. This reduces the impact of such loans on the revenue budget. The profile of the repayment of the debt portfolio is shown below at 5.6.3.

5.4.5 New long term borrowing is currently planned during the life of this strategy. Where short term borrowing arrangements are required to support a temporary low general fund bank balance, the Authority will engage with Treasury Advisors to understand if there are any Local Authority counterparties available to lend from. The offer will then be considered and terms of loans agreed between the Principal Accountant and nominated officer from the lending organisation.

5.5 Policy on borrowing in advance of need

5.5.1 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 that value for money can be demonstrated and that the Authority can ensure the security of such funds.

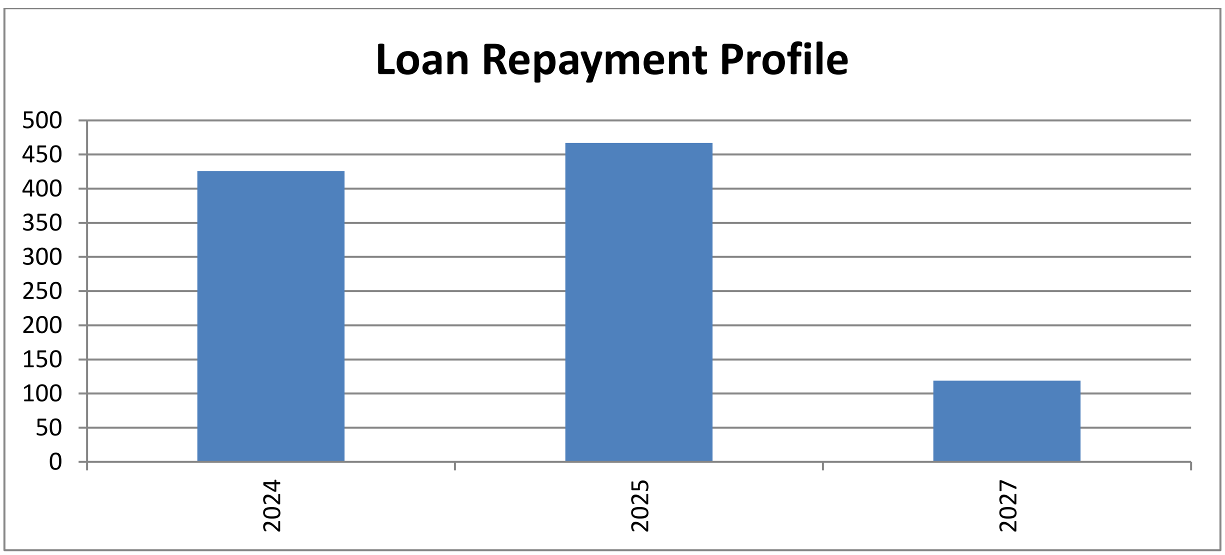
5.6 Debt Rescheduling

5.6.1 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 size of the cost of debt repayments (premiums incurred).

5.6.2 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
- Enhancing the balance of the portfolio (amending the maturity profile and/or the balance of volatility).

5.6.3 Any potential rescheduling will be very carefully considered. A table showing the current profile of the debt portfolio, highlighting years in which debt matures, is shown below:



5.6.4 All current borrowing is on a fixed rate basis with a current overall weighted average 4.65%. Any new loans taken out for future capital expenditure plans or the repayment of maturing debt will be subject to the rates applicable at that time. Any early repayment of debt would also be subject to the expense of early pay-back premiums.

5.6.5 Key sensitivities of the interest rate forecast are likely to be:

- 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 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 reviewed with the potential action of increasing borrowing to cover the under borrowed position or future known commitments or repayments while rates were still relatively low; and

- If it were felt that there was a significant risk of a sharp fall in short and long-term interest rates due to a weakening of economic factors; then longer-term borrowing will be postponed until rates were deemed at their lowest and a review of current debt would be undertaken to ascertain the benefit of rescheduling to more competitive short term loans.

5.7 Treasury Management limits on activity

5.7.1 There are three debt-related treasury activity limits. Their purpose is to restrain borrowing activity within certain limits to manage risk and reduce the impact of adverse movement in interest rates. However, if these are set too restrictively they will impair the opportunity to reduce costs or maximise value for money.

Table 9: Interest Rate Limits

	2020-21 Upper	2021-22 Upper	2022-23 Upper
Limits on fixed interest rates based on net debt	100%	100%	100%
Limits on variable interest rates based on net debt	25%	25%	25%

Table 10: Maturity structure of fixed interest rate borrowing 2021-22

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%	75%
10 years and above	0%	100%

6. ANNUAL INVESTMENT STRATEGY

6.1 Investment Policy

6.1.1 The Authority’s investment policy has regard to the Communities and Local Government’s Guidance on Local Government Investments and the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectorial Guidance Notes (the CIPFA TM Code). The Authority’s principal objectives for investments are security first, liquidity next and finally yield.

6.1.2 The above guidance from the MHCLG 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:

a) 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.

b) 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 Authority will engage with its advisors to monitor market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.

c) 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.

d) The Authority has defined the list of types of investment instruments that the treasury management team are authorised to use. There are two lists in table 11 below 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.

Table 11: Approved Investment Instruments

Specified Investments (maturities up to one year)
▫ Bank & Building Societies Term Deposits
▫ Other Local Authority Term Deposits
▫ Debt Management Agency Deposit Facility
▫ AAA Money Market Funds (CNAV/LVNAV/VNAV)
Non-Specified Investments (maturities over one year)
▫ Bank & Building Societies Term Deposits
▫ Other Local Authority Term Deposits
Other Non-Specified Investments
▫ Fixed term deposits with variable rates & maturities

e) Non-specified investments limit. The Authority has determined that it will limit the maximum total exposure to non-specified investments as being 20% of the total investment portfolio.

f) Lending limits, the maximum amount for each counterparty will be set at £10m per organisation/group. The maximum investment duration for each counterparty will be set in line with the creditworthiness service provided by Link Asset Services as set out in paragraph 6.2.

g) The Authority will set a limit for the amount of its investments which are invested for longer than 365 days, (see paragraph 6.4.5).

h) Investments will only be placed with counterparties from countries with a specified minimum sovereign rating, (see paragraph 6.3).

i) The Authority has engaged external consultants, (see paragraph 3.4), 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.

j) All investments will be denominated in sterling.

k) As a result of the change in accounting standards for 2020-21 under IFRS 9, the 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. (In November 2018, the Ministry of Housing, Communities and Local Government, [MHCLG], concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years ending 31 March 2023).

6.2 Creditworthiness Policy and Exposure to Risk

6.2.1 The Authority utilises the creditworthiness service provided by Link Asset Services as its Treasury Management advisers. This service employs a sophisticated modelling approach incorporating credit ratings from the three main credit rating agencies – Fitch, Moody’s and Standard & 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 to give early warning of likely changes in credit ratings; and
- Sovereign ratings to select counterparties from only the most creditworthy countries.

6.2.2 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 for 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 Authority to determine the suggested duration of investments. The Authority will use counterparties within the following durational bands:

- Yellow 5 years
- 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

6.2.3 As this methodology uses a wide range of information beyond basic credit ratings, it ensures that no one source of information is given undue credence. All ratings and colour codes are monitored weekly via Link's credit listings and in-between via business press. The Authority is alerted to changes to any ratings via email from Link. 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 and any current investments reviewed for potential movement.

6.2.4 Sole reliance will not be placed on the use of this external service. In addition to Link, the Joint Finance Team officers will also use market data and information on any external support for banks to help support its decision making process.

6.3 Country Limits

6.3.1 The Authority has determined that it will only use approved counterparties from the UK and from countries outside of the UK with a minimum sovereign credit rating of AAA from Fitch (or equivalent). The list will be added to, or deducted from, should ratings change.

6.4 Investment Strategy

6.4.1 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).

6.4.2 The Authority would seek to maintain at all times a core liquid balance of £4m, and maintain a liquid balances vs longer term balances ratio of 50:50.

6.4.3 For its cash flow generated balances, the Authority will seek to utilise its business reserve instant access and notice accounts, money market funds and short-dated deposits, (overnight to 100 days), in order to benefit from the compounding of interest.

6.4.4 Bank Rate is unlikely to rise from 0.10% for a considerable period. It is very difficult to say when it may start rising so it may be best to assume that investment earnings from money market-related instruments will be sub 0.50% for the foreseeable future. Bank Rate forecasts for financial year ends (March) are:

2020-21 – 0.10%	2021-22 – 0.10%	2022-23 – 0.10%	2023-24 – 0.10%

6.4.5 The overall balance of risks to economic growth in the UK is probably now skewed to the upside, but is subject to major uncertainty due to the virus and how quickly successful vaccines can be widely administered to the population. It may also be affected by the implications of the agreed UK Brexit deal.

6.4.6 There is relatively little UK domestic risk of increases or decreases in Bank Rate and significant changes in shorter term PWLB rates. The Bank of England has effectively ruled out the use of negative interest rates in the near term and increases in Bank Rate are likely to be some years away given the underlying economic expectations. However, it is always possible that safe haven flows, due to unexpected domestic developments and those in other major economies, or a return of investor confidence in equities, could impact gilt yields, (and so PWLB rates), in the UK.

Negative Interest Rates

6.4.7 While the Bank of England said in August/September 2020 that it is unlikely to introduce a negative Bank Rate, at least in the next 6 - 12 months, and in November omitted any mention of negative rates in the minutes of the meeting of the Monetary Policy Committee, some deposit accounts are already offering negative rates for shorter periods. As part of the response to the pandemic and lockdown, the Bank and the Government have provided financial markets and businesses with plentiful access to credit, either directly or through commercial banks. In addition, the Government has provided large sums of grants to local authorities to help deal with the Covid crisis; this has caused some local authorities to have sudden large increases in cash balances searching for an investment home, some of which was only very short term until those sums were able to be passed on.

6.4.8 As for money market funds (MMFs), yields have continued to drift lower. Some managers have already resorted to trimming fee levels to ensure that net yields for investors remain in positive territory where possible and practical. Investor cash flow uncertainty, and the need to maintain liquidity in these unprecedented times, has meant there is a surfeit of money swilling around at the very short end of the market. This has seen a number of market operators, now including the Debt Management Office, offer nil or negative rates for very short term maturities. This is not universal, and MMFs are still offering a marginally positive return, as are a number of financial institutions for investments at the very short end of the yield curve.

6.4.9 Investment treasury indicator and limit - total principal funds invested for greater than 365 days. This limit is set with regard to the Authority’s liquidity requirements and to reduce the need for early sale of an investment. It is based on the forecast availability of funds after each year-end.

Table 12: Investment Treasury Limit:

	2020-21	**2021-22**	**2022-23**
	Upper	**Upper**	**Upper**
Principal sums invested for longer than 365 days	£5m	£5m	£5m

6.5 End of Year Investment Report

6.5.1 At the end of the financial year, the Treasurer will report on the Authority's investment activity as part of the Annual Treasury Report.

ANNEX 1

Minimum Revenue Provision (MRP) Statement

1. 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.

2. It is proposed that the Authority continues to set the MRP at 6.7% of the opening Capital Financing Requirement (CFR) relating to the balance of historic debt liability. This is considered to be a prudent and sustainable approach, however the 6.7% level remains subject to review.

3. Any post 2017-18 new borrowing will, under delegated powers (known as prudential borrowing), be subject to MRP under option 3 of the Government Guidance. It will be charged over a period which is reasonably commensurate with the estimated useful life applicable to the nature of expenditure, using the equal annual instalment method. For example, borrowing in respect of capital expenditure on the new Training Centre Project will be related to the estimated life of that asset.

4. The use of this option for certain schemes will also result in a nil MRP charge until the year after that in which all expenditure on the scheme, project or other item of capital expenditure has been fully accrued under proper accounting practices, regardless of the extent of such expenditure that has not been accrued at the end of the previous financial year. Estimated life periods will be determined using appropriately qualified Officers professional judgement.

5. Based on the current projected capital outturn position for 2020-21, it is expected that this will equate to a charge of approximately £668k for 2021-22.

6. 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.