Prudential Indicators and Treasury Management and Investment Strategy 2021/22 – 2023/24

1. Purpose of the Report

To seek approval of the Treasury Management Strategy and the Investment Strategy.

2. Background

2.1 The Local Government Act 2003 and supporting regulations require the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice and prepare, set and publish prudential indicators and treasury indicators that ensure the Council's capital expenditure plans are affordable, prudent and sustainable in the long-term.

The prudential indicators consider the affordability and impact of capital expenditure plans, and set out the Council's overall capital framework. Each prudential indicator either summarises the expected activity or introduces limits upon the activity, and reflects the underlying capital programme.

Within the overall prudential framework there is a clear impact on the Council's treasury management activity, either through borrowing or investment activity. As a consequence a Treasury Management Strategy is prepared which considers the effective funding of the capital expenditure decisions and complements the prudential indicators.

2.2 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 in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return. The Council is required to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions.

This, therefore, means that increases in capital expenditure must be limited to a level whereby charges to revenue remain affordable within the projected income of the Council for the foreseeable future. These increased charges may arise from:

- increases in interest charges and debt repayment caused by increased borrowing to finance additional capital expenditure; and
- any increases in operational running costs from new capital projects.

2.3 Treasury management is, therefore, an important part of the overall financial management of the Council's affairs and is defined 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."

Specific treasury indicators are prepared and included in the Treasury Management Strategy which requires Member approval.

The Council's treasury activities are strictly regulated by statutory requirements and guidance, including;

- CIPFA Treasury Management Code
- CIPFA Prudential Code
- MHCLG Investment Guidance
- MHCLG Minimum Revenue Provision (MRP) Guidance

2.4 The Council's Constitution (via Financial and Procurement Procedure Rules) requires the annual Treasury Management Strategy to be reported to Council outlining the expected treasury activity for the forthcoming 3 years. A key requirement of this report is to explain both the risks, and the management of the risks, associated with the treasury service. As a minimum a mid-year monitoring report is produced with a further report produced after the year-end to report on actual activity for the year.

Reports on Treasury matters are also required to be adequately scrutinised before being recommended to the Council and this role is undertaken by Audit Committee.

3. Key Issues

3.1 Overview

The Council's 2020/21 Prudential Indicators and Treasury Management Strategy was approved by Council on 26th February 2020, whilst a Mid-Year report which updated the 2020/21 approved indicators was considered by Audit Committee on the 19th January 2021. This report provides an update for the period 2021/22 to 2023/24.

Section 3.2 of the report details the key elements of the Council's Capital Expenditure Plans and associated Prudential Indicators. The Treasury Management Strategy (including the Investment Strategy) is detailed in Sections 3.3. Supporting detail is provided in the Appendices.

The Treasury Management Strategy has been drawn up taking account of advice from the Council's treasury management advisors, Link Treasury Services Ltd.

This is a technical and complex report however the key messages are:

- Investments – the primary governing principle will remain security over return and the criteria for selecting counterparties reflect this. Cash available for

investment will remain low and investment yields are presently at historic lows, resulting in low returns.

- Borrowing – overall, this is estimated to increase year on year over the period covered by this report as the Council plans to incrementally reduce its under-borrowing position as part of managing its daily and long term liquidity position. New borrowing will only be taken up as current portfolio debt matures and where approved capital investment is to be financed by borrowing. For the financial year 2021/22 the Council will continue to utilise short term borrowing only, to enable significant revenue savings on interest to support the revenue budget position. This strategy has continued to be successful during 2020/21.

- Governance – strategies and risk are reviewed by the Audit Committee with continuous monitoring which includes the Mid-Year and Year End reporting.

- The underlying economic and financial environment remains difficult for the Council, foremost being the improving, but still challenging, concerns over investment counterparty risk. This background encourages the Council to continue maintaining investments short term and with low risk counterparties. The downside of such a policy is that investment returns remain low. This situation has been further exacerbated by the economic impact of the Covid-19 pandemic, that has seen the Bank of England base rate fall to 0.1%.

  As the Council continues to utilise the short term borrowing market to generate interest rate savings as part of approved budget plans, the level of short term borrowing will continue to rise. As a result of this the Council increased its prudential indicator for borrowing volumes with a maturity date less than 12 months, to 50% of total borrowing as part of the 2020/21 Treasury Management Strategy. Whilst the Covid-19 pandemic has seen severe impacts to the global economy, its reduction in the base rate has also lead to a significantly reduced cost of short-term borrowing, enabling the Council to generate greater savings from its strategy.

- On 26th November PWLB made a significant change to their long-term borrowing rates decreasing them all by 1%. The key features of this change were to allow local authorities to access cheaper long term borrowing but under a more restrictive borrowing arrangement that would allow the PWLB to prevent borrowing for commercial investments. The PWLB will no longer lend to any local authority that has any plans to buy investment assets primarily for yield anywhere in their capital programme. The immediate impact of this decision has seen PWLB 50 year borrowing levels fall to 1.5% and below but with that short-term borrow falling, to as little as 0.3% for 3 months, for example. The Council keeps interest rates under constant review within its borrowing strategies and decisions on the mix of long-term and short-term borrowing.

- The Chartered Institute of Public Finance and Accountancy has recommended to the Government that implementation of IFRS 16 – Leases, should be further delayed in the public sector and it will now be introduced in 2022/23. This will ensure that public sector accounts will be aligned to the Whole of Government Accounts.

- The CIPFA revised 2017 Prudential and Treasury Management Codes require, for 2021-22, all local authorities to prepare an additional report, a capital strategy report, which will provide the following:

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

The aim of the capital strategy is to ensure that all elected members fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite. The Council is currently working towards the implementation of a revised capital governance structure that will in turn enable the production of the required Capital Strategy.

3.2 CAPITAL EXPENDITURE PLANS & PRUDENTIAL INDICATORS 2021/22 TO 2023/24

3.2.1 The Capital Expenditure Plans

The Council's capital expenditure plans are summarised below and form the first of the prudential indicators. A certain level of capital expenditure is grant supported by the Government; any decisions by the Council to spend above this level will be considered unsupported capital expenditure. This unsupported capital expenditure needs to have regard to:

- Service objectives (e.g. strategic planning);
- Stewardship of assets (e.g. asset management planning);
- Value for money (e.g. option appraisal)
- Prudence and sustainability (e.g. implications for external borrowing and whole life costing);
- Affordability (e.g. implications for the council tax and rents)
- Practicality (e.g. the achievability of the Capital Programme).

The revenue consequences of capital expenditure, particularly the unsupported expenditure, will need to be paid for from the Council's own revenue resources.

This capital expenditure can be paid for immediately (by applying capital resources such as capital receipts, capital grants etc., or revenue resources), but if these resources are insufficient any residual expenditure will add to the Council's borrowing need.

3.2.2 The key risks to the plans are that the level of Government support has been estimated and is therefore subject to change. Similarly some of the estimates for other sources of funding, such as capital receipts, may also be subject to change over this timescale. For example, anticipated asset sales resulting from the Council's on-going asset rationalisation programme may be deferred due to the on-going impact of the current economic & financial conditions on the property market.

3.2.3 The revised capital expenditure plans in the updated Capital Strategy and Capital Programme being presented within this report, are summarised in the table below.

It should be noted, that these represent the capital investment forecasts under traditional forms of financing and exclude assets acquired under PFI and finance lease arrangements which are a type of borrowing but which are budgeted for separately outside of the capital financing budget.

	2020/21 Estimated £m	**2021/22 Estimated £m**	**2022/23 Estimated £m**	**2023/24 Estimated £m**
Children and Young People's Services	12.415	13.842	4.508	6.573
Assistant Chief Executive	0.424	0.210	0.210	0.210
Adult Care & Housing	4.824	6.611	12.653	6.130
Finance and Customer Services	6.876	5.648	3.204	10.523
Regeneration and Environment	46.998	72.070	52.553	24.646
Capitalisation Direction	2.000	2.000	0.000	0.000
Total Non HRA	**73.537**	**100.381**	**73.128**	**48.082**
HRA	51.749	62.324	44.811	42.964
Total HRA	**51.749**	**62.324**	**44.811**	**42.964**
Total expenditure	**125.286**	**162.705**	**117.939**	**91.046**
Capital receipts	12.177	16.253	5.901	1.378
Capital grants, capital contributions & sources other capital funding	75.246	95.174	57.075	43.303
Total financing	**87.423**	**111.427**	**62.976**	**44.682**
Unsupported borrowing requirement for the year	**37.863**	**51.279**	**54.963**	**46.365**

3.2.4 **<u>The Capital Financing Requirement (the Council's Borrowing Need)</u>**

The Council's Capital Financing Requirement (CFR) is the total outstanding capital expenditure which has not yet been financed from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need.

As can be seen in the table in 3.2.3 above, the latest revised estimated unsupported borrowing requirement over the period 2020/21 to 2022/23 based on the updated Capital Strategy and Capital Programme is £190.470m. This will be reflected in the year on year change to the CFR.

The CFR is then reduced by the amount the Council sets aside from revenue for the repayment of debt and other financing movements.

As explained in 3.2.3, in addition to the underlying borrowing need arising from the Council's capital investment programme, the overall CFR also includes other long term liabilities (OLTL) brought onto the Balance Sheet as a result of the recognition of Private Finance Initiative (PFI) and finance lease assets. This is a technical adjustment to recognise the underlying borrowing facility taken out by the PFI or finance lease provider and does not require the Council to take out any additional borrow in its own right.

The CFR projections for which approval is being sought are set out in the table below:

	2020/21 Estimated £m	**2021/22 Estimated £m**	**2022/23 Estimated £m**	**2023/24 Estimated £m**
CFR – General Fund	565.510	603.206	629.636	649.284
CFR – HRA	305.871	310.604	326.951	339.701
Total CFR	**871.381**	**913.810**	**956.587**	**988.985**
Movement in CFR	**29.178**	**42.429**	**42.777**	**32.398**
Of which:				
CFR – capital investment	747.891	793.307	839.704	876.181
OLTL	123.490	120.503	116.883	112.804
Movement in CFR represented by:				
Unsupported borrowing requirement for the year (table at 3.2.3 above)	37.863	51.279	54.963	46.365
Net financing need for the year for OLTL	-3.028	-2.987	-3.620	-4.079
Less Minimum Revenue Provision and other financing movements	-5.657	-5.863	-8.566	-9.888
Movement in CFR	**29.178**	**42.429**	**42.777**	**32.398**

3.2.5 **Minimum Revenue Provision Policy Statement**

3.2.5.1 The Council is required to pay off an element of the accumulated General Fund CFR each year through a revenue charge (the Minimum Revenue Provision - MRP). In addition, it is also allowed to make additional voluntary payments (VRP) where it is prudent to do so. Repayments included in annual PFI charges or finance lease payments are also applied as MRP. No MRP charge is currently

required for the HRA. The HRA charges depreciation on its assets, which is a revenue charge.

3.2.5.2 MHCLG Regulations require Council to approve an MRP Policy Statement in advance of each financial year setting out how it will discharge its duty to charge an amount of MRP which the Council considers 'prudent'.

The Strategic Director of Finance & Customer Services will, where it is prudent to do so, use discretion to review the overall financing of the capital programme and the opportunities afforded by the regulations to maximise the benefit to the Council whilst ensuring it meets its duty to charge a 'prudent' provision. To provide maximum flexibility the recommended MRP policy includes the use of the annuity method and the equal instalments method.

The wording of the proposed MRP Policy Statement for which Council approval is being sought is shown at Appendix A.

3.2.6 **Affordability Prudential Indicators**

Affordability prudential indicators are used to assess the affordability of the capital expenditure plans by reference to their impact on the Council's finances overall. The following indicators are proposed.

3.2.6.1 **Actual and Estimates of the 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 of the Council.

The estimates of financing costs include all current commitments, the proposals contained in the proposed 2021/22 Revenue Budget and updated future years' capital expenditure plans.

Ratio of financing costs to Net Revenue Stream				
	2020/21 Estimated %	**2021/22 Estimated %**	**2022/23 Estimated %**	**2023/24 Estimated %**
Non-HRA	5.81	5.31	5.47	5.31
HRA	15.90	16.80	17.13	17.33

3.2.6.2 **Estimates of the incremental impact of capital expenditure plans on Council Tax**

This indicator identifies the revenue costs associated with proposed changes to the capital programme compared to the Council's existing commitments and current plans.

Only schemes in the Council's approved capital programme are included in the indicators and there may be further schemes pending approval. Any additional approvals will normally have to be funded from unsupported borrowing as all identified available resources have been allocated. This would impact on the prudential indicators above.

The impact on Band D Council Tax, as shown in the table below, indicates the impact of the Council's capital expenditure plans as already budgeted for within the proposed Revenue Budget for 2021/22 and the Council's Medium Term Financial Strategy, and does not indicate additional requirements for Rotherham council tax payers.

Incremental impact of capital expenditure plans on the Band D Council Tax				
	Estimated 2020/21 £	**Estimated 2021/22 £**	**Estimated 2022/23 £**	**Estimated 2023/24 £**
Council Tax – Band D	11.31	41.68	90.76	119.68

3.2.6.3 **Estimates of the incremental impact of capital expenditure plans on Housing Rent levels**

Similar to the Council tax calculation, this indicator identifies the revenue cost of proposed changes in the housing capital programme compared to the Council's existing approved commitments and current plans expressed in terms of the impact on weekly rent levels. Given the latest HRA 30 Year Business Plan does forecast the use of new borrowing over the period due, there is an estimated impact on housing rent levels, as indicated in the table below.

Incremental impact of capital expenditure plans on Housing Rent levels				
	Estimated 2020/21 £	**Estimated 2021/22 £**	**Estimated 2022/23 £**	**Estimated 2023/24 £**
Weekly Housing Rent Levels	0.00	8.51	34.91	29.00

3.3 TREASURY MANAGEMENT STRATEGY 2021/22 – 2023/24

The Treasury Management Strategy covers:

a) The Council's borrowing and investment projections (para. 3.3.1);
b) The Council's estimates and limits to borrowing activity (para. 3.3.2 to 3.3.5);
c) The expected movement in interest rates (para. 3.3.6);
d) The Council's borrowing and debt strategy (para. 3.3.7);
e) The Council's investment strategy (para. 3.3.8);
f) Treasury Management prudential indicators and limits on activity (para. 3.3.9);
g) Treasury performance indicators (para. 3.3.10); and
h) Policy on the use of external service advisers (para. 3.3.12).

3.3.1 **Borrowing and Investment Projections 2021/22 – 2023/24**

The borrowing requirement comprises the expected movement in the CFR and any maturing debt which will need to be re-financed.

The effect on the treasury position over the next three years for the Council is shown in the table attached at Appendix B. The table also highlights the expected level of investment balances.

The ex-SYCC debt that the Council was administering on behalf of the other South Yorkshire authorities has been fully repaid in 2020/21 and therefore will no longer be included as part of the strategy.

3.3.2 **Limits to Borrowing Activity**

There are a number of key indicators to ensure the Council operates its activities within well-defined limits.

For the first of these, the Council needs to ensure that its total borrowing, does not, except in the short term, exceed the total of the CFR at the end of the previous year plus the estimated additional CFR for the current year (2020/21) and the following three financial years. This is designed to ensure that in the medium term, debt is only for a capital purpose. The purpose of including the estimated additional CFR for the following two financial years, is that it allows some flexibility for limited early borrowing for future years (para. 3.3.4).

The Strategic Director - Finance & Customer Services reports that the Council has complied with this indicator in the current year and does not envisage difficulties for the future (the table below refers). This view takes into account approved commitments and existing plans.

Whilst the forecast changes in the CFR assume significant reductions in the amount of under-borrowing by the Council, the actual change in the year-on- year level of under-borrowing will be determined by the Strategic Director – Finance and Customers Services, after consideration of all relevant factors in determining the appropriate strategy for borrowing levels within the Council's overall financial strategy.

	2020/21 Estimated £m	2021/22 Estimated £m	2022/23 Estimated £m	2023/24 Estimated £m
CFR – excl. OLTL	747.891	793.307	839.704	876.181
CFR – OLTL	123.490	120.503	116.883	112.804
Total CFR	**871.381**	**913.810**	**956.587**	**988.985**
Borrowing (loans outstanding)	714.930	765.881	820.779	867.144
Borrowing - OLTL	123.490	120.503	116.883	112.804
Total Borrowing	**838.420**	**886.384**	**937.662**	**979.948**
CFR less Borrowing (underborrowed)	**32.961**	**27.426**	**18.925**	**9.037**

3.3.3 **The Overall Level of Borrowing**

A further two prudential indicators control or anticipate the overall level of borrowing. These are:

- The Authorised Limit for External Debt
- The Operational Boundary for External Debt

3.3.3.1 **The Authorised Limit for External Debt**

The Authorised Limit represents the maximum amount an authority can borrow for capital and cash flow purposes. 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 Authorised Limit is set by the Council and any breach must be reported. The Government retains an option to control either the total of all councils plans, or those of a specific council, although no such Government control has yet been exercised.

The following Authorised Limit for RMBC is proposed, set at £20m above the Council's CFR:

Authorised Limit for External Debt	2020/21 Estimated £m	2021/22 Estimated £m	2022/23 Estimated £m	2023/24 Estimated £m
Borrowing	767.891	813.307	859.704	896.181
OLTL	125.960	122.913	119.221	115.060
Total	**893.851**	**936.220**	**978.925**	**1,011.241**

3.3.3.2 Separately, the Council was limited to a maximum HRA CFR through the HRA self-financing regime debt cap. This cap was removed in the Government's Autumn Budget 2018. The latest iteration of the HRA Business Plan requires additional borrowing to support the Growth Programme, and therefore there has been an increase in the HRA CFR. Therefore a prudent debt limit has been applied to the Council's HRA borrowing, allowing for their current need, plus £20m to enable a reaction to any significant development opportunity that arises.

HRA Debt Limit	**2020/21 Estimated £m**	**2021/22 Estimated £m**	**2022/23 Estimated £m**	**2023/24 Estimated £m**
HRA Debt Limit	335.871	340.604	356.951	369.701
HRA CFR	305.871	310.604	326.951	339.701
HRA Headroom (+)	**30.000**	**30.000**	**30.000**	**30.000**

3.3.3.3 **The Operational Boundary for External Debt**

This is the amount beyond which external borrowing (for capital and cash flow purposes) is not normally expected to exceed. Its purpose is to act as a tool for monitoring day to day treasury activity. Occasionally, for operational reasons it may be necessary to breach the limit. Temporary breaches are not a cause for concern but sustained breaches may be an indication that the Council is acting imprudently or experiencing major financial difficulty.

The Operational Boundary for which Council approval is being sought is set out in the table below.

Operational Boundary for External Debt	**2020/21 Estimated £m**	**2021/22 Estimated £m**	**2022/23 Estimated £m**	**2023/24 Estimated £m**
Borrowing	744.930	795.881	850.779	887.144
Other long term liabilities	123.490	120.503	116.883	112.804
Total	**868.420**	**916.384**	**967.662**	**1,009.948**

3.3.4 **Policy on Borrowing in Advance of Need**

The Council has some flexibility to borrow funds in advance for use in future years. The Strategic Director of Finance & Customer Services may do this under delegated powers where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or help meet budgetary constraints.

Whilst the Strategic Director of Finance & Customer Services will adopt a prudent approach to any such borrowing, where there is a clear business case for doing so, borrowing may be undertaken to fund the approved capital programme or to fund debt maturities.

Risks associated with any advance borrowing activity will be subject to appraisal in advance and subsequent reporting through the mid-year and annual reporting mechanism.

3.3.5 **Debt Rescheduling**

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. These savings will need to be considered in the light of the current treasury position and the value of the cost of debt repayment (premiums incurred).

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

3.3.6 **Expected Movement in Interest Rates**

The Base Rate, currently 0.1%, underpins investment returns and is currently the lowest level on record. There remains a great deal of economic uncertainty affecting growth forecasts for the UK economy and the rate of inflation both of which are key factors influencing the Base Rate.

The uncertainty began initially due to the UK leaving the EU and the on-going issues in areas of the world economy which could result in weak growth or recession in the UK's main trading partners.

However, these events have been taken over by the Covid 19 pandemic and the economic consequences this has brought. The bank rate was lowered to 0.1% in March with the onset of the pandemic.

On 26th November 2020 the Public Works Loan Board (PWLB) made a significant change to their long-term borrowing rates decreasing them all by 1%. The key features of this changes were to allow local authorities to access cheaper long term borrowing but under a more restrictive borrowing arrangement that would allow the PWLB to prevent borrowing for commercial investments. The PWLB will no longer lend to any local authority that has any plans to buy investment assets primarily for yield anywhere in their capital programme. The immediate impact of this decision has seen PWLB 50 year borrowing levels fall to 1.5% and below but with that short-term borrow falling, to as little as 0.3% for 6 months, for example

The Council is currently under-borrowed as shown in 3.3.2. The delay in borrowing long-term reduces the cost of carrying borrowed monies when yields on investments are low relative to the borrowing rates. The highest return from the Money Market Funds currently is 0.023% and the Debt Management Office is

0.01% (which is further reduced as there is a cost of transfer). This clearly results in little to nothing in return for any surplus cash invested throughout the year.

The Council is currently utilising a strategy of borrowing only in the short term at very low cost and as a result are generating savings against the anticipated cost of borrowing. The Council is however, remaining vigilant and prepared to act on any increases in the base rate where we may need to begin to enter into long-term borrowing.

3.3.7 **Borrowing and Debt Strategy 2020/21 – 2022/23**

As shown in the table in 3.3.2, the Council is currently maintaining an under-borrowed position. This means that the CFR 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 strategy is prudent as investment returns are low and counterparty risk remains relatively high as outlined above.

The uncertainty over future interest rates increases the inherent risks associated with treasury activity. As a result the Council will continue to take a prudent approach to its treasury strategy.

The Strategic Director of Finance & Customer Services, under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time, taking into account the risks shown in the forecast above. It is likely shorter term fixed rates may provide lower cost opportunities in the short to medium term.

3.3.8 **Investment Strategy 2020/21 – 2022/23**

The primary objectives of the Council's investment strategy are:

- Firstly to safeguard the timely repayment of principal and interest (security);
- Secondly to ensure adequate liquidity; and
- Thirdly to produce an investment return (yield).

3.3.8.1 As part of this Strategy, Members need to consider and approve security and liquidity benchmarks in addition to yield benchmarks which are currently widely used to assess investment performance and have previously been reported to Members. The proposed benchmarks are set down in Appendix D.

3.3.8.2 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:

- It maintains a policy covering both 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 of Appendix C.

- 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 as set out in Appendix D.

3.3.8.3 The Strategic Director of Finance & Customer Services will maintain a counterparty list in compliance with the criteria set out in 3.3.8.5 and will revise the criteria and submit them to Council for approval as necessary. These criteria are different to those which are used to select Specified and Non-Specified investments.

The rating criteria use the lowest common denominator method of selecting counterparties and applying limits. This means that the application of the Council's minimum criteria will apply to the lowest available rating for any institution. For instance, if an institution is rated by two agencies, one meets the Council's criteria, the other does not, the institution will fall outside the lending criteria. This is in compliance with the CIPFA Treasury Management Code of Practice.

3.3.8.4 Credit rating information is supplied by our treasury advisors on all active counterparties that comply with the criteria in section 3.3.8.5. Any counterparty failing to meet the criteria would be omitted from the counterparty list. Any rating changes, rating watches (notification of a likely change) and rating outlooks (notification of a possible long term change) are provided to officers almost immediately after they occur and this information is considered before any investment decision is taken.

3.3.8.5 The criteria for providing a portfolio of high quality investment counterparties (both Specified and Non-Specified investments) are:

- **Banks** – The Council will use banks which are rated by at least two rating agencies and have at least the following Fitch, Moody's and Standard and Poors' ratings (where rated):

	Fitch	Moody's	Standards & Poor's
Short-term	F1	P-1	A-1
Long-term	A-	A3	A-

To allow for the day to day management of the Council's cash flow the Council's bankers will also be retained on the list of counterparties if ratings fall below the above minimum criteria.

- **Building Societies** – the Council will use the top 20 Building Societies ranked by asset size but restricted to a maximum of 20% of the investment portfolio

- **Money Market Funds** – AAA (CNAV or LVNAV) – restricted to a maximum investment of £20m per fund. This has been increased from previous years in recognition that the Council is carrying greater levels of cash at any given period due to the extended short term borrowing strategy. The Council works

with its specialist Treasury Advisors to review and select appropriate MMF's to ensure that those selected are AAA rated and therefore highly secure, with cash available for withdrawal each day, therefore these are very low risk accounts.

- **UK Government** – Debt Management Office

- **UK Single Tier & County Councils** – (i.e. Metropolitan Districts, London Boroughs, County Councils, Unitary Authorities)

A limit of 35% will be applied to the use of Non-Specified investments within the investment portfolio, excluding day to day cash management through the Council's own bank.

Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market and sovereign information will continue to be applied before making any specific investment decision from the agreed portfolio of counterparties.

3.3.8.6 The time and monetary limits for institutions on the Council's Counterparty List are as follows and they include a proposed increase in the level of investments possible with any single Money Market Fund to £20m (these will cover both Specified and Non-Specified Investments):

	Fitch	Moody's	Standard & Poor's	Money Limit	Time Limit
Upper Limit Category	F1+/AA-	P-1/Aa3	A-1+/AA-	£20m	5 years
Middle Limit Category	F1/A-	P-1/A3	A-1/A-	£10m	364 days
Lower Limit Category *	All Building Soc's ranked 1 to 10 All Building Soc's ranked 11 to 20			£5m £1m	6 mths 3 mths
Debt Management Office	-	-	-	Unlimited **	6 months
Money Market Funds	-	-	-	£20m	n/a
UK Single Tier & County Councils	-	-	-	£20m	5 years
Council's Bankers	-	-	-	£10m*	364 days
The above money limits are exclusive of bank balances held by schools * Based on maximum of 20% of the investment portfolio ** Provides maximum flexibility *** There may be occasions where the Council has to exceed this limit, where government issues out significant grant funding, such as Covid Business Grants and the Council is unable to invest those resources within the options available on the day. This risk is mitigated by daily review of the cashflow forecast,					

however, the volume of government funding issued during the pandemic has been significant.

3.3.8.7 The proposed criteria for Specified and Non-Specified investments and monitoring of counterparties are shown in Appendix C for Member approval.

In the normal course of the Council's cash flow operations it is expected that both Specified and Non-specified investments will be utilised for the control of liquidity as both categories allow for short term investments.

The use of longer-term instruments (greater than one year from inception to repayment) will fall in the non-specified investment category. These instruments will only be used where the Council's liquidity requirements are safeguarded. This will also be limited by the long-term investment limits.

3.3.9 **Treasury Management Prudential Indicators and Limits on Activity**

3.3.9.1 There are four further treasury activity limits the purpose of which are to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. However if these are set to be too restrictive they will impair the opportunities to reduce costs. The limits are:

- Upper limits on fixed interest rate exposure – This identifies a maximum limit for fixed interest rates based upon the fixed debt position net of fixed interest rate investments.

- Upper limits on variable interest rate exposure – as above this limit covers a maximum limit on variable interest rates based upon the variable debt position net of variable interest rate investments.

- Maturity structures of borrowing – These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

- Total funds invested for greater than 364 days – These limits are set to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

For the purposes of these indicators the Council's market debt with Financial Institutions is treated as variable where debt may be subject to variation on specific call dates each year. However, over the period covered by this Strategy it is considered very unlikely that any market debt will be called due to the prevailing historically low interest rates.

3.3.9.2 The activity limits (prudential indicators) for Member approval are as follows:

RMBC	2020/21	2021/22	2022/23	2023/24
Interest rate Exposures				
	Upper	**Upper**	**Upper**	**Upper**
Limits on fixed interest rate debt based on fixed net debt	100%	100%	100%	100%
Limits on variable interest rate debt based on variable net debt	50%	50%	50%	50%

RMBC Maturity Structure of fixed interest rate borrowing 2021/22		
	Lower	**Upper**
Under 12 months	0%	60%
12 months to 2 years	0%	35%
2 years to 5 years	0%	45%
5 years to 10 years	0%	45%
10 years to 20 years	0%	45%
20 years to 30 years	0%	50%
30 years to 40 years	0%	50%
40 years to 50 years	0%	55%
50 years and above	0%	60%

RMBC Maximum Funds invested > 364 days			
	1 to 2 years	2 to 3 years	3 to 5 years
Funds invested > 364 days	£m 10	£m 8	£m 6

3.3.10 **Treasury Performance Indicators**

The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking. The results of the following two indicators will be reported in the Treasury Annual Report for 2020/21:

- Debt – Borrowing - Average rate of borrowing for the year compared to average available
- Investments – Internal returns above the 7 day London Interbank Bid rate (LIBID) which is the rate at which a bank is willing to borrow from other banks

3.3.11 **Training**

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. Training has recently been undertaken by Members of the Audit Committee and

further training will be arranged as required. The training needs of treasury management officers are periodically reviewed.

3.3.12 **Policy on the use of external service advisors**

The Council uses Link Asset Services as its treasury management advisors.

The company provides a range of services which include:

- Technical support on treasury matters, capital finance issues and the drafting of Member reports;
- Economic and interest rate analysis;
- Debt services which includes advice on the timing of borrowing;
- Debt rescheduling advice surrounding the existing portfolio;
- Generic investment advice on interest rates, timing and investment instruments; and,
- Credit rating/market information service comprising the three main credit rating agencies.

Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the Council recognises that responsibility for treasury management decisions remains with the Council at all times. The service is provided to the Council under a contractual agreement which is subject to regular review.

Appendix A

Proposed Wording of Minimum Revenue Provision Policy Statement

It is being recommended that Council approve the following MRP policy in relation to the charge for the 2021/22 financial year:

(a) The MRP charge in relation to capital expenditure incurred prior to 2007/08 where the expenditure was funded by either supported or unsupported borrowing will be calculated using the expected useful life of the asset and the calculation of the provision will be by the annuity method;

(b) The MRP charge in relation to capital expenditure incurred since 2007/08 where the expenditure is funded by either supported or unsupported borrowing will be calculated using the expected useful life of the asset at the point the asset is brought into use. The calculation of the provision will be either the annuity method or the equal instalments method depending on which is most appropriate; and

(c) The MRP charge in relation to capital expenditure incurred since 2007/08 where the expenditure is funded by a 'capitalisation directive' (e.g. equal pay) will be calculated on the basis of the specified period(s) set down within the regulations. The calculation of the provision will be either the annuity method or the equal instalments method depending on which is most appropriate.

(d) For the sake of clarity, where MRP has been overcharged in previous years, the recovery of the overcharge will be effected by taking an MRP holiday in full or in part against future years charges that would otherwise have been made. The MRP holiday adjustment to the future years charge will be done in such a way as to ensure that:

- the total MRP after applying the adjustment will not be less than zero in any financial year
- the cumulative amount adjusted for will never exceed the amount over-charged;
- the extent of the adjustment will be reviewed on an annual basis

In order to meet the requirement to make an annual, prudent repayment of debt, the Council may use prior year capital receipts to pay down debt, reducing the level of MRP charged to revenue. This policy has been factored into the planned capital programme and management of capital programme resources.

Appendix B

Borrowing and Investment Projections 2020/21 to 2022/23

RMBC	2020/21 Estimated £m	2021/22 Estimated £m	2022/23 Estimated £m	2023/24 Estimated £m
External Debt				
Borrowing at 1 April - Short Term	262.309	329.861	406.140	474.109
Borrowing at 1 April - Long Term	397.389	385.069	359.741	346.670
Total Borrowing at 1 April	**659.698**	**714.930**	**765.881**	**820.779**
Expected change in debt	55.232	50.951	54.898	46.365
Borrowing at 31 March	**714.930**	**765.881**	**820.779**	**867.144**
Other long-term liabilities (OLTL) at 1 April	126.518	123.490	120.503	116.883
Expected change in OLTL	-3.028	-2.987	-3.620	-4.079
Other long-term liabilities (OLTL) at 31 March	123.490	120.503	116.883	112.804
Total Borrowing & OLTL at 31 March	**838.420**	**886.384**	**937.662**	**979.948**
Investments				
Total Investments at 1 April	27.530	53.825	50.000	50.000
Investment change	26.295	-3.825	0.000	0.000
Total Investments at 31 March	53.825	50.000	50.000	50.000
Net borrowing at 31 March	**784.595**	**836.384**	**887.662**	**929.948**

Appendix C

Treasury Management Practice (TMP) 1 (5) – Credit and Counterparty Risk Management

1. Overview

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

- MHCLG'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 key intention of the Guidance is to maintain the current requirement for councils to invest prudently, and that priority is given to security and liquidity before yield.

The Prudential Code has also expressed concern that local authorities should ensure that an authority's approach to commercial activities should be proportional to its overall resources. Any such commercial investments should be appropriately disclosed throughout the Treasury Management Strategy, clearly identifying the related debt, capital financing requirement and terms. However this Council does not plan on entering into any significant commercial investments.

1.2 In order to facilitate this objective the guidance requires this Council to have regard to the CIPFA publication Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. This Council has adopted the Code and will apply its principles to all investment activity.

In accordance with the Code, the Strategic Director of Finance & Customer Services has reviewed and prepared its treasury management practices. This part, TMP 1(5), covering investment counterparty policy requires approval each year.

2. Annual Investment Strategy

2.1 The key requirements of both the Code and the investment guidance are to set an annual investment strategy, as part of its annual treasury strategy for the following year, covering the identification and approval of the following:

- The guidelines for investment decision making, particularly non-specified investments.
- The principles to be used to determine the maximum periods for which investments can be made.
- The specified investments the Council may use.
- The non-specified investments the Council may use.

This strategy is to be approved by Council.

The investment policy proposed for the Council is detailed in the paragraphs below (sections 2.3 and 2.4).

2.2 Strategy Guidelines

The main strategy guidelines are contained in the body of the treasury strategy statement.

2.3 Specified Investments

2.3.1 These investments are sterling investments of not more than one-year maturity. If they are for a longer period then the Council must have the right to be repaid within 12 months if it wishes.

These are low risk assets where the possibility of loss of principal or investment income is small.

2.3.2 These would include the following investment categories:

1. The UK Government Debt Management Office.

2. UK Single Tier & County Councils – (i.e. Metropolitans District, London Boroughs, County Councils, Unitary Authorities)

3. Money Market Funds that have been awarded AAA credit ratings by Standard and Poor's, Moody's or Fitch rating agencies and restricted to £20m per fund.

4. A bank or a building society that has been awarded a minimum short-term rating of F1 by Fitch, P-1 by Moody's and A-1 by Standard and Poor's rating agencies. For Building Societies investments will be restricted to 20% of the overall investment portfolio and:

   - a maximum of £5m for a period not exceeding 6 months if the society is ranked in the top 10 by asset size; or
   - a maximum of £1m and a period not exceeding 3 months if the society is ranked 11 to 20 by asset size.

2.4 Non-Specified Investments

2.4.1 Non-specified investments are any other type of investment not defined as specified above.

The criteria supporting the selection of these investments and the maximum limits to be applied are set out below.

2.4.2 Non specified investments would include any sterling investments with:

1. A bank that has been awarded a minimum long term credit rating of AA- by Fitch, Aa3 by Moody's and AA- by Standard & Poor's for deposits with a maturity of greater than 1 year.

2. The Council's own bank if ratings fall below the above minimum criteria.

3. A Building Society which is ranked in the top 20 by asset size. Investments will be restricted to 20% of the overall investment portfolio and:

   - a maximum of £5m for a period not exceeding 6 months if the Society is ranked in the top 10 by asset size; or
   - a maximum of £1m and a period not exceeding 3 months if the Society is ranked 11 to 20 by asset size.

3 The Monitoring of Investment Counterparties

3.1 The credit rating of counterparties will be monitored regularly. The Council receives credit rating information from the Council's Treasury Management advisors on a daily basis, as and when ratings change, and counterparties are checked promptly.

On occasions ratings may be downgraded after the date on which an investment has been made. It would be expected that a minor downgrading would not affect the full receipt of the principal and interest.

3.2 Any counterparty failing to meet the minimum criteria will be removed from the list immediately by the Strategic Director of Finance & Customer Services, and new counterparties will be added to the list if and when they meet the minimum criteria.

Appendix D

Security, Liquidity and Yield Benchmarking

These benchmarks are targets and so may be exceeded from time to time with any variation reported, with supporting reasons in Mid-Year & Annual Treasury Reports.

1. Security and liquidity

These benchmarks are already intrinsic to the approved treasury strategy through the counterparty selection criteria and some of the prudential indicators, e.g. the maximum funds which may be invested for more than 364 days, the limit on the use of non-specified investments, etc.

1.1 Security

1.1.1 Security is currently evidenced by the application of minimum criteria to investment counterparties, primarily through the use of credit ratings supplied by the three main credit rating agencies. Whilst this approach embodies security considerations, benchmarking the levels of risk is more subjective and therefore problematic.

1.1.2 One method to benchmark security risk is to assess the historic level of default against the minimum criteria used in the Council's investment strategy. The default rates are little changed from last year.

Credit Rating	1 year	2 years	3 years	4 years	5 years
AAA	0.04%	0.10%	0.19%	0.26%	0.36%
AA	0.02%	0.04%	0.09%	0.17%	0.24%
A	0.05%	0.14%	0.26%	0.40%	0.56%
BBB	0.17%	0.42%	0.73%	1.10%	1.47%

1.1.3 The Council's minimum long term rating criteria (over one year) is "AAA" meaning the average expectation of default for a three year investment in a counterparty with a "AAA" long term rating would be 0.19% of the total investment (e.g. for a £1m investment the average potential loss would be £1,900).

The Council's minimum long term rating criteria (up to one year) is "BBB" and the average expectation of default for such an investment would be 0.17% (e.g. for a £1m investment the average loss would be £1,700).

These are only averages but do act as a benchmark for risk across the investment portfolio.

The Council's maximum security risk benchmark for the estimated maximum portfolio during 2020/21 is 0.070% which means that for every £1m invested the

average potential loss would be £700. This position remains largely unchanged from 2019/20 (benchmark was 0.073% or £730).

1.1.4 The Council's Treasury advisers maintain a continuous review of the risk position by the inclusion of the Council's daily investment position within their online model.

1.2 **Liquidity**

1.2.1 This is defined as "having adequate, though not excessive cash resources, borrowing arrangements, overdrafts or standby facilities to enable the Council at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives" (CIPFA Treasury Management Code of Practice). The Council seeks to maintain:

- Bank overdraft – on a day-to-day basis the Council works to an agreed overdraft limit of £100,000 with the Council's bankers. Whilst a short-term increase could be negotiated less expensive short-term borrowing is accessed through the financial markets to remain within the agreed overdraft.
- Liquid, short term deposits of at least £6m available with a week's notice.

1.2.2 The availability of liquidity and the inherent risks arising from the investment periods within the portfolio is monitored using the Weighted Average Life (WAL) of the portfolio. This measures the time period over which half the investment portfolio would have matured and become liquid

A shorter WAL generally represents less risk and in this respect the benchmark to be used for 2020/21 is:

- 0.08 years which means that at any point in time half the investment portfolio would be available within 28 days.

2. <u>Yield</u>

These benchmarks are currently widely used to assess investment performance and the Council's local measure of yield is:

- Internal returns above the 7 day London Interbank Bid rate (LIBID) which is the rate at which a bank is willing to borrow from other banks