# Treasury Management Sub-Committee Agenda

## 16 December 2019 at 7pm

**Crompton Room, Civic Centre,
Duke Street, Chelmsford**

## Membership

Councillor C.K. Davidson (Chair)

## and Councillors

M.W. Bracken, D.J.R. Clark, P.H. Clark and J.M.C Raven

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## TREASURY MANAGEMENT SUB-COMMITTEE

## 16 December 2019

## AGENDA

## PART I

1. **APOLOGIES FOR ABSENCE AND SUBSTITUTIONS**

2. **MINUTES**

   To consider the minutes of the meeting held on 21 October 2019.

3. **DECLARATION OF INTERESTS**

   All Members are reminded that they must disclose any interests they know they have in items of business on the meeting's agenda and that they must do so at this point on the agenda or as soon as they become aware of the interest. If the interest is a Disclosable Pecuniary Interest they are also obliged to notify the Monitoring Officer within 28 days of the meeting.

4. **PUBLIC QUESTION TIME**

5. **TREASURY MANAGEMENT STRATEGY 2020/21**

6. **URGENT BUSINESS**

   To consider any other matter which, in the opinion of the Chair, should be considered by reason of special circumstances (to be specified) as a matter of urgency.

## PART II (EXEMPT ITEMS)

To consider whether the public (including the press) should be excluded from the meeting during consideration of the following agenda items on the grounds that it involves the likely disclosure of exempt information specified in the appropriate paragraph or paragraphs of Part 1 of Schedule 12A of the Local Government Act 1972 indicated in the Agenda item.

# MINUTES

of the

## TREASURY MANAGEMENT SUB-COMMITTEE

held on 21 October 2019 at 7pm

Present:

Councillor C.K. Davidson (Chair), Councillors M.W. Bracken, D.J.R. Clark, P.H. Clark and J.M.C. Raven

1. **Apologies for Absence and Substitutions**

No apologies for absence were received.

2. **Minutes**

The minutes of the meeting held on 20 June 2019 were confirmed as a correct record and signed by the Chair after a clarification was made on the closing time of the last meeting. This was amended to read 8.43pm.

3. **Public Question Time**

There were no questions from members of the public.

4. **Declaration of Interests**

All Members were reminded to declare any Disclosable Pecuniary interests or other registerable interests where appropriate in any items of business on the meeting's agenda. None were made.

5. **Treasury Management Mid-Year Review 2019/20**

In accordance with the CIPFA Code of Practice the mid-year review of the Council's treasury management function and activities in 2019/20 was presented to the Sub-Committee. The review examined the position with the Council's investments at 31 August 2019 and compared treasury activity to the approved Treasury Management Strategy. The Sub-Committee was asked to consider whether any amendments to the Strategy were necessary and, if so, to recommend them to the Cabinet on 19 November and then Full Council on 11 December 2019.

The Sub-Committee was informed that the review detailed the activity since 1st April 2019 and any challenges since then. Members were informed that there was a breach of the Counter Party limits on 27th June 2019. It was noted that this was due to human error and guidance had since been expanded to stress the importance of following the standard process. It was also noted that this breach had no impact on the council's financial position.

Members were also informed that the review recommended an increase in the external debt limit. It was noted that this would provide greater flexibility for officers when considering the funding requirements of any new capital schemes. In response to questions from members, it was confirmed that officers wanted to maximise options and any decision to borrow would be taken after advice from Arlingclose. The Sub-Committee agreed that raising the limit would allow greater flexibility. It was also agreed that officers look into the possibility of Arlingclose running a session on the topic for members.

It was noted by a member of the Committee that the CCLA property fund had not performed as well recently as in previous years and should therefore be closely monitored going forward. Officers agreed to continue to monitor the fund closely and confirmed that with Arlingclose they regularly monitor and review all investments. It was noted that the capital value had slightly decreased but the fund did still reflect half of the interest made by the council on investments. The Committee agreed that the fund should be monitored but did not agree with the suggestion made, to set a level at which the Council should liquidate the fund. The Committee stated it should be an operational decision by officers as to when to consider liquidating any fund. The other members of the Committee agreed that the concerns raised by one member were legitimate, but were happy with the current monitoring arrangements in place.

The Committee agreed that they were happy with the review and current position and to recommend the report to Cabinet. The Committee were also in agreement with the suggestion to raise the external debt limit, to provide greater flexibility

**RESOLVED** that;

1. the investment strategy is an appropriate balance of risk and return for the Council and;
2. that the report be recommended to the Cabinet.

*(7pm to 7.52pm)*

6. **Urgent Business**

There were no matters of urgent business brought before the Sub-Committee.

The meeting closed at 7.52pm.

Chair

| TREASURY MANAGEMENT SUB-COMMITTEE |
|---|
| **16th December 2019** <br><br> AGENDA ITEM 5 |

| | |
|---|---|
| **Subject** | TREASURY MANAGEMENT STRATEGY 2020/21 |
| **Report by** | DIRECTOR OF FINANCIAL SERVICES |

**Enquiries contact:** Phil Reeves, Chief Accountant (phil.reeves@chelmsford.gov.uk 01245 606562)

**Purpose**

To update the Sub-Committee on Treasury Management activities and recommend a Treasury Management Strategy for 2020/21 to Cabinet and then Full Council

**Recommendation(s)**

That the sub-committee:

Recommend the Treasury Management Strategy 2020/21 to Cabinet or amend as appropriate

| Corporate Implications | | |
|---|---|---|
| **Legal:** | | If no proposal is made to Council the authority will be in breach of its statutory duties |
| **Financial:** | | As detailed in the report |
| **Potential impact on climate change and the environment** | | Any fund managers will be required to consider ESG (Environmental, Social and Governance) factors in their investment process. All the fund managers would be expected to have signed up to the UN Principles for Responsible Investment (PRI). PRI argues that active participation in ESG and exercising shareholder rights on this basis can help to improve the performance of companies which may otherwise not address such concerns and so being an engaged corporate stakeholder is a more effective way to bring about change in corporate behaviour on ethical issues.<br>Further requirements from those identified above are not practical given the limited ability to directly influence any immediate change in the financial markets. |

| | | |
|---|---|---|
| **Contribution toward achieving a net zero carbon position by 2030** | | None |
| **Personnel:** | | None |
| **Risk Management:** | | The report identifies how risk to sums invested and interest rate risk will be managed. |
| **Equalities and Diversity:** **(For new or revised policies or procedures has an equalities impact assessment been carried out? Y/N)** | | N |
| **Health and Safety:** | | None |
| **IT:** | | None |
| **Other:** | | None |

| | |
|---|---|
| **Consultees** | None. |

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| **Policies and Strategies**<br>The report takes into account the following policies and strategies of the Council:<br>Treasury Management Strategy<br>Capital and Investment Strategy |

1. Background

1.1 Cabinet and Council are legally responsible for treasury management. The attached draft report enables Cabinet and Council to review the Treasury Management Strategy for 2020/21. The Council is legally required to approve a strategy for the coming year.

1.2 The report in **Appendix A** complies with the CIPFA Code of Practice and covers the following:

- Identification of a draft Treasury Management Strategy
- Identification of any proposed changes

1.3 Members of the sub-committee are able to amend the contents of the attached report and thereby recommend changes to how the Council invests its money.

1.4 The borrowing limits in the report will be reviewed, and if necessary amended, in light of the Capital expenditure plans set out in the Budget report and Capital and Investment Strategy (to be considered by Cabinet in January) whilst also retaining some headroom to allow for flexibility within the Capital Programme.

List of Appendices
**Appendix A** – Treasury Management Strategy 2020/21

Background Papers
Nil

Chelmsford City Council

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| **CABINET** |
| **28TH January 2020** |
| AGENDA ITEM X |

| | |
|---|---|
| **Subject:** | **TREASURY MANAGEMENT STRATEGY 2020/21** |
| **Report by:** | Cabinet Member for Fairer Chelmsford |

**Enquiries contact:**
Phil Reeves Tel: 01245 606562
e-mail: phil.reeves@chelmsford.gov.uk

**Purpose**
This report sets out the recommended approach together with the associated risks in managing the Council's cash investments in 2020/21.

**Options**
To agree or vary the proposals in the report.

**Recommendation**
That the Cabinet accepts the report as endorsed by the Audit Committee and recommends to Council that:

i. the Treasury Strategy for 2020/21 is approved (**Appendix 1**)
ii. the Treasury Management indicators for 2020/21 are approved (**Appendix 2**)

**Corporate Implications**

| | |
|---|---|
| Legal: | If no proposal is made to Council the authority will be in breach of its statutory duties |
| Financial: | As detailed in the report |
| Potential impact on climate change and the environment | Any fund managers will be required to consider ESG (Environmental, Social and Governance) factors in their investment process. All the fund managers would be expected to have signed up to the UN Principles for Responsible Investment (PRI). PRI argues that active participation in ESG and exercising shareholder rights on this basis can help to improve the performance of companies which may otherwise not address such concerns and so being an engaged corporate stakeholder is a more effective |

| | |
|---|---|
| | way to bring about change in corporate behaviour on ethical issues.<br>Further requirements from those identified above are not practical given the limited ability to directly influence any immediate change in the financial markets. |
| Contribution toward achieving a net zero carbon position by 2030 | None |
| Personnel: | None |
| Risk Management: | The report identifies how risk to sums invested and interest rate risk will be managed. |
| Equalities and Diversity:<br>(For new or revised policies or procedures has an equalities impact assessment been carried out? Y/N) | None |
| Health and Safety: | None |
| IT: | None |
| Other: | None |

**Consultees:**
Treasury Management Sub Committee

**Policies and Strategies:**
Capital and Investment Strategies

1.0 Background

1.1 The Council can expect to have cash to invest arising from its revenue and capital balances, and collection of Council Tax. This cash can be usefully invested to produce a return to help support services and Council Tax. The activities around the management of this cash are known as 'Treasury Management'.

1.2 The amount of cash the Council has to invest will decline as the Council funds its capital programme.

1.3 Treasury Management is defined by the Chartered Institute of Public Finance and Accountancy (CIPFA) 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"

1.4 CIPFA produce a framework for managing treasury activities, called a 'Code'. Councils are legally required to have regard to this Code and members of CIPFA are expected to comply with its requirements. This report fulfils the Authority's legal obligation under the *Local Government Act 2003* to have regard to both the CIPFA Code and the MHCLG Guidance.

1.5 The Council's investment priorities as required by Government regulations are in order of priority:
(a) the security of capital
(b) the liquidity of its investments; and
when these are satisfied
(c) Yield.

1.6 Treasury Management is also the monitoring, planning and undertaking of borrowing. The Council may use borrowing to fund capital expenditure. There are effectively two types of borrowing;

- External, where the Council borrows from a bank, local authority or the Government with agreed repayment and interest terms. The Council's revenue budget is annually charged with interest for the loan and a charge is also made for principal debt repayment (**M**inimum **R**evenue **P**rovision). It is important to note that MRP may assume capital expenditure is repaid over say 50 years but in cash terms for example a 5-year loan may have been agreed so new financing would need to be arranged at the end of this loan.
- Internal, where cash say from Community Infrastructure Levy (CIL) has been received by the Council but is not yet spent so it is 'borrowed' to fund the cash payments on capital expenditure. The Council still must charge its revenue budget MRP arising from the use of internally borrowed funds and will forgo the income it would have earned had the internally borrowed money been invested.

All borrowing and investment is undertaken by the Director of Finance and the role of members is to provide appropriate limits and scrutiny of the borrowing and investment.

1.7 Treasury Management regulations for local authorities require the Council to produce the following documentation:

i) An overarching **Treasury Management Policy Statement.** This sets out the objectives of the Council's treasury management activities and was approved at February 2019 Council.

ii) **Treasury Strategy (Appendix 1)**. This sets out the Council's approach to managing its investments for the year ahead.

iii) **Treasury Management Practice Statements (TMPS).** These are procedure notes, detailing how the Council will manage its treasury management risks. The Director of Finance is delegated to produce the TMPS; they do not require member approval and are therefore not reported formally. TMPs are reviewed regularly and updated as required.

iv) **Yearly and Half Yearly Activity Reports.**

1.8 In 2018 changes were made to both the Prudential Code and the MHCLG investment guidance for local authorities. As such the Council is now required to prepare a Capital and Investment Strategies as overarching documents to support the prudent management of its capital expenditure, borrowing and investment activity. The Treasury Management Strategy now serves as a detailed supporting document to the Capital & Investment strategy and focuses on the management of investments and borrowing arising from the organisation's cashflows.

1.9 It has been previously reported (Capital & Investment Strategy 2019/20) that the Council was projecting a need to borrow to fund the capital programme in 2019/20. The capital programme is being partially funded by internal borrowing and this is forecast to continue into future years.

## 2. <u>Audit and Risk Committee Review of Treasury Management Strategy</u>

2.1 The Treasury Management Sub-committee of the Audit and Risk Committee has reviewed the contents of this report and any comments or changes recommended have been incorporated.

## 3. <u>Executive summary of Proposed Investment Strategy</u>

3.1 The key requirements operationally for the Council are summarised in paragraph 3.2, with a more detailed version in **Appendix 1.**

3.2 **Summary of Treasury Strategy for 2020/21 (full details Appendix 1)**

1) All Council investments will be made in UK sterling.

2) The Council expects to earn around 0.75-0.9% on its cash investments in 2020/21 and 4.1% from the CCLA property fund. Should Pooled funds be used they can be expected to achieve yields of around 3%.

3) The Council's cash flow and investment balances will be lower in 2020/21. The largest element of Council cash holdings will come from unspent CIL funds and Revenue Reserves.

4) There are no changes proposed to the investment criteria compared to the 2019/20 strategy. The Council investments will be managed by the Director of Finance in line with the Counter party criteria set out in **Appendix 1** (paragraph 4.15). The criteria set out in the report allow investment in:

- Enhanced Money Market Funds
- Money Market Funds (MMF)
- UK Public bodies
- Unsecured Bank investments
- Unsecured Building Society Investments
- Unsecured Non-UK Banks investments
- Unsecured Registered Social Landlord Loans
- Covered Bonds, Reverse Repurchase Agreements and Supranational Bonds
- Potential to undertake unsecured Challenger bank investments
- Multi asset funds Bond and property funds

Each investment has a maximum monetary investment limit in place, identified in **Appendix 1** Paragraph 4.15. The Council has appointed Arlingclose to advise on Treasury matters including providing advice on the investment criteria used.

5) The Council as part of the 2019/20 budget undertook funding of its capital programme from internal borrowing and this is forecast to continue. The use of internal borrowing reduces the sums available to invest. The Council does within the strategy provide enough flexibility to enable internal borrowing to be switched to external loans if the financial case arises, so external borrowing limits will be set to that end.

4. Conclusion

4.1 The Council's investment strategy prioritises the security and liquidity of the Council's financial assets over yield.

4.2 The Council's methods for investment and selecting counter party do not remove all risk of losses but balance the need to make an appropriate return within reasonable risk parameters.

4.3 The Council's borrowing to fund its capital programme is planned to be internalised, but the strategy permits the switching to external loans should the financial case arise.

Background Papers
None

Appendices

1) Treasury Management Strategy

2) Treasury Management Indicators

**Appendix 1 - Treasury Management Strategy 2020/21**

1. Introduction

1.1 Chelmsford City Council has adopted and complies with both the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes and the Ministry of Housing, Communities and Local Government's Guidance on Local Government Investments.

1.2 Both the Code and MHCLG regulations require the Authority to prepare and authorise a Treasury Management Strategy prior to the start of each financial year. This report fulfils the Council's legal requirement under the Local Government Act 2003.

1.3 Chelmsford City Council has invested substantial sums of money and is therefore exposed to a series of financial risks including the loss of invested funds. Risk also comes from possible changes in interest rates affecting investment income or the cost of any external borrowings.

1.4 This strategy will set out how the Council monitors and manages the financial risks arising from its treasury management operations. It should be noted that the Council prioritises the security of its capital first and foremost, its liquidity needs secondly and finally the maximisation of yield on investments only once security and liquidity have been addressed.

1.5 It is important to note that the borrowing of monies purely to invest or lend on to make a return is unlawful and this Council will not engage in such activity.

1.6 In the event of major changes to the external or internal context in which this strategy has been set, it may be necessary for the Council to revise its strategy during the year.

1.7 The CIPFA Prudential code requires authorities to publish an overarching Capital Strategy which considers capital expenditure, treasury management, investment strategy and various other factors.

1.8 In addition, the MHCLG guidance on borrowing and investments requires authorities to consider both financial and non-financial assets held for the generation of profit in a new Investment Strategy.

1.9 This Treasury Management Strategy will focus solely on investments arising from the organisation's cashflows and debt management activity and matters of borrowing. Non-treasury investments will be covered separately under the Capital Strategy. Prudential indicators will now be presented within the capital strategy and this report will instead put forward separate treasury management indicators.

2. External Context

2.1 The Council's treasury management strategy operates in a macroeconomic environment which can have a significant impact on the Council's treasury operations in terms of inflation, interest rate and counterparty risks.

### The economic environment and interest rate forecast

2.2 Arlingclose, the Council's treasury advisors, forecast that interest rates are likely to remain at current levels until at least 2022. The risks to this forecast are deemed to be significantly weighted to the downside.

2.3 The key assumptions behind the forecast are:

- The global economy is entering a period of slower growth in response to political issues, primarily the trade policy stance of the US. The UK economy has displayed a marked slowdown in growth due to both Brexit uncertainty and the downturn in global activity. In response, global and UK interest rate expectations have eased.
- Some positivity on the trade negotiations between China and the US has prompted worst case economic scenarios to be pared back. However, information is limited, and upbeat expectations have been wrong before.
- UK economic growth has stalled despite Q3 2019 GDP of 0.3%. Monthly figures indicate growth waned as the quarter progressed and survey data suggests falling household and business confidence. Both main political party have promised substantial fiscal easing, which should help support growth.
- The weaker external environment severely limits potential upside movement in Bank Rate, while the slowing UK economy will place pressure on the MPC to loosen monetary policy. Indeed, two MPC members voted for an immediate cut in November 2019.
- Inflation is running below target at 1.7%. While the tight labour market risks medium-term domestically-driven inflationary pressure, slower global growth should reduce the prospect of externally driven pressure, although political turmoil could push up oil prices.

### Credit Outlook and counterparty risk

2.4 Over recent years the Council has reduced the amount of unsecured bank deposits it holds in reaction to the "bail in" risk arising from reform to the banking sector. Under "bail in" provisions, investors would face losses to their deposits and share-holdings in order to recapitalise a bank before any Government bailout would occur.

2.5 Public Bodies provide much less risk as investment counterparty but a balance between risk and return does allow the use of other types of investment counter party. The Council should where possible continue to spread investments over different organisations and different investment categories (property, pooled funds, public bodies, etc) to provide a satisfactory balance of security of capital and return.

2.6 An economic slowdown will impact on the capital value of pooled funds and property investments. However, a balanced portfolio and ability to look beyond temporary price fluctuations could enable the effective use of these types of investment to generate a level of income/yield which protects against sub-inflation levels of return.

2.7 Banks and building societies may be financially weakened by an economic slowdown. Council credit criteria should therefore be set at a sufficient level to identify the counter party who are less at risk of suffering materially during such a slowdown; additionally the criteria must allow identification of  enough active counter party to enable spread of investment and risk.

3. Local Context

3.1 At the end of November 2019, the Council held £60m of investments. These investments arise from balances (including unspent CIL) and reserves, as well as income received in advance of expenditure. The investments provide the Council with an income stream to support revenue expenditure.

3.2 A factor in setting the current individual limit of £3m per financial institution was it represented some 5% of total funds, clearly as investment balances fall the £3m represents a greater percentage of total funds, so investments become less spread proportionally if the £3m limit is kept. However, reducing the £3m limit would reduce the number of institutions willing to take Council deposits as the investment is judged too small to be economic for large institutions. The strategy must therefore balance these factors and for 2020/21 has retained the £3m limit.

3.3 The duration that an investment is made for impacts on the level of risk to capital invested. The longer the investment the more risk of some unexpected change occurring to the financial strength of the deposit taker. Perhaps, more importantly the Council can only invest for durations that enables Council liquidity to be managed effectively. To reduce these risks limits can be placed on the length of investments.

3.4 The Council's current and projected year end levels of investments are shown in the table below. It should be noted that year end tends to be the lowest point in the year for the Council's cash balances. This is because most residents pay their Council Tax over 10 instalments, but the Council pays these out to central government and other precepting authorities on a monthly basis; therefore, significant net cash outflows occur in February and March each year. The table below can be considered worse case scenarios given cashflow balances have historically turned out to be higher than projected (reflecting the difficulty of making such projections). The forecast reflects draft budget information.

| | November 2019 £m | 31 March 2020 £m | 31 March 2021 £m | 31 March 2022 £m |
|---|---|---|---|---|
| Investments | 60 | 42 | 29 | 34 |

3.5 Community Infrastructure Levy contributions (CIL) and Revenue Reserves will continue to support the Council's average cash balance in 2020/21 but the forecast decline in cash balance reflects the use of internal borrowing. Should the Council identify an immediate need to use the unspent CIL balance (currently some £20m) then the cash balance will decline further, or external borrowing may be required.

4 Investment Strategy 2020/21

4.1 The Council's investment strategy will prioritise its investment objectives in the following order:

- Security of assets – investing in counterparty only where the risks of incurring a capital loss through default and the risks of late payment of principal and interest are low
- Liquidity – Ensuring that the authority can access enough cash to meet its obligations with appropriate notice
- Yield – subject to the management of risks associated with security and liquidity of assets, the Council will seek to maximise the yield from its investment portfolio

This is a prudent approach in line with CIPFA and MHCLG guidance.

4.2 The Council use Credit Rating and Arlingclose's recommendations to determine suitable Counter party. Arlingclose's approach is not based on a rigid model but on an assessment of a range of measures that require a final human judgement of the overall risk. The assessments include the following; credit ratings, the likelihood of UK or another Government support, market information (e.g. share price or Credit Default Swap), collateral offered by the Counter Party, types of activity undertaken by the institution and other external advice. The Counter Party recommended in this report reflect discussions by officers with Arlingclose, the Cabinet Member for Fairer Chelmsford and the Treasury Management Sub-committee.
No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

4.3 Given the advice received by the Council regarding credit risks, sub inflation returns and potential economic slowdown the Council will retain within the strategy the following investments types:

- Enhanced Money Market Funds & Money Market Funds (MMF)
- UK Public bodies
- Unsecured Bank Investments
- Unsecured Building Society Investments
- Unsecured Non-UK Banks Investments
- Unsecured Registered Social Landlord Loans
- Covered Bonds, Reverse Repurchase Agreements and Supranational Bonds
- Potential to undertake unsecured Challenger bank investments
- Multi asset funds Bond and property funds

4.4 **Enhanced Money Market and Money Market Funds.** The Council has access to enhanced money market funds (AAA rated) which offer a rate of return (0.8-0.95%) but require 2 – 5 day notice to withdraw funds.
The Council invests short term cash in several AAA rated money market funds. These funds provide a modest rate of interest around 0.75% at November 2019 and most importantly allow same day access to funds. These funds spread the Council's investment over many financial institutions, so reducing risk. Historically the funds have proved very safe.

4.5 **UK Public Bodies.** Debt Management Agency Deposit Facility, Government Treasury Bills or Gilts as these are all investments with the UK Central Government. These are the safest possible form of UK investment, so the Council will place no limit on the amount that can be invested.
Local Authorities / Bank Deposits Collateralised (guaranteed against local authority loans). These are theoretically as safe as lending to Government, but what would happen should a Local Authority go bankrupt has never been tested in law. It is therefore prudent to place some limit on investments with each local authority but recognising this type of investment is much safer than most alternatives. Arlingclose offer some guidance on risks of each local authority but the data is based on snap shot year end accounts as only a few authorities can afford the cost of ratings by credit agencies.

4.6 **Unsecured UK bank investments.** The changes to UK Bank regulation from the adoption of a "bail-in" approach to recapitalising banks and the move to ringfencing of UK bank retail operations has increased the amount that could be lost in the event of a bank failure. With the completion of ringfencing activities by major banks to protect retail investors from investment banking losses, different banks have placed local authority depositors in either the retail or investment banking divisions. It should be noted that the credit scores for the banks with which the Council operates have either remained the same or improved as a result of ringfencing. The Council feels that it is still prudent to invest with banks subject first to credit rating criteria but considering the advice supplied by Arlingclose.

4.7 **Unsecured building society investments.** The Council's treasury strategy takes a different, more cautious approach to building societies than that recommended by Arlingclose, who undertake their own analysis to identify building societies that they believe have good financial characteristics. The Council instead requires that building societies have a long-term credit rating of at least A-.

4.8 **Unsecured Non-UK bank investments.** Arlingclose review the approach to investment with non-UK banks separately to UK banks. This reflects the different risks and ownership structures that affect the security of the investment. The Council first uses credit rating information to select appropriate non-UK banks and then uses Arlingclose advice to make investment decisions. The Council uses credit rating of AA- for selecting investments with non-UK banks of up to 364 days but over 100 days and A- for investments of up to 100 days.

4.9 **Registered Social Landlord (RSL) Loans.** The Council can lend to RSLs in the pursuit of treasury management objectives but must treat loans made for policy reasons as capital expenditure. The option to lend for Treasury purposes has been on the Council's counter party list for several years but there has not been a suitable opportunity.

4.10 **Covered Bonds, Reverse Repurchase Agreements and Supranational Bonds**. These are all different investment products but have the highest levels of credit rating. They are either backed by a pool of guaranteed bank assets or UK and/or foreign Governments. The Council takes advice from Arlingclose before undertaking any of these investments, so an investigation of the individual strength of each investment has been determined. They are rarely used by the Council.

4.11 **Multi-Asset, Bond and Property Funds**. These potentially offer the Council income and capital growth of the sum invested. There are several types of fund including property funds, bond funds, equity funds and mixed asset funds. Funds seek to reduce risk by building a pool of investments and as such are considerably safer than an investment of comparable size in a specific single asset. However, any fund exposes the Council to market price volatility. Officers will carefully consider any investment opportunities and always keep any ownership under review. A review of the risks and benefits of using Funds was made in the summer of 2019 and which concluded that Multi-asset, Bond and Property funds provide a suitable method to invest Council funds.
At the time of drafting this report the Council has an investment of over £6.5m in the CCLA property fund and the Director of Finance is considering making investments in Multi-Asset and Bond funds, this decision is pending determination of the funding needs of the Council for its future capital programme.

4.12 **Challenger Banks.** As part of the Government's policy to reduce the size of banks and to encourage competition, new 'challenger banks' are appearing in the UK banking market. Many of these challenger banks are unrated but do have high levels of capital buffers. There has been insufficient evidence to demonstrate during 2019/20 that investments would be appropriately secure. However, it is recommended that the Treasury Management Sub-committee reviews any new evidence on these challenger banks and if satisfied that they provide sufficient Security, Liquidity and Return, that up to £3m could be invested by the Council.

4.13 Durations allowed for each investment type are set out below in paragraph 4.15 and reflect a judgement on the level of risk and the need to keep investment size large enough to make it attractive to a counterparty.

4.14 **Appendix 2** contains the Treasury indicators which set key measures to limit and report exposure on security, liquidity and yield.

4.15 **Counterparty – Duration and Monetary Limits**
The Council is required by law to identify the proposed investment criteria under the categories Specified and Non-Specified, as shown below:

| **Specified Investments**<br>-investments of duration less than 365 days and denominated in sterling.<br>-investments made to UK Government, UK local authorities or institutions of high credit quality.<br>- high credit quality defined as a minimum A- by Fitch or the equivalent score of the other main rating bodies. | | | | |
|---|---|---|---|---|
| **Specified Counterparty** | **Minimum Credit Criteria** | **Max. Limit £m** | **Max. maturity period** | **Change from Prev. approach** |
| Enhanced Money Market Funds (Variable Unit Price) Up to 5 funds | AAA | £6m each fund | 2-5-day notice | None |
| Money Market Funds (per fund) | AAA | £6m each fund | Instant Access | None |
| Debt Management Agency Deposit Facility, Government Treasury Bills or Gilts | UK Government | No Limit | 364 days | None |
| Local Authorities / Bank Deposits Collateralised (guaranteed against local authority loans) | UK Government | £10m each authority | 364 days | Limit reduced to £10m each |
| UK Banks | A- | £3m for each group | 364 days | None |
| Building Societies | A- | £3m for each group | 364 days | None |
| Non-UK Banks | AA- | £3m each group | 364 days | None |
| Non-UK Banks | A- | £3m each group | 100 days | None |
| Registered Social Landlord Loans | A- | £3m each group | 364 days | None |
| Covered Bonds | AA- | £6m | 364 days | None |
| Reverse Repurchase Agreements (each agreement) | AA- | £6m | 364 days | None |
| Supranational Bonds (per institution) | AAA | £6m | 364 days | None |

| **Non-specified Investments**<br>These do not meet the criteria of specified investments. They are identified separately to ensure the Council understands that these are higher risk, either due to counter party risk, liquidity risk, market risk or interest rate risk | | | | |
|---|---|---|---|---|
| **Counterparty** | **Min. Credit Criteria** | **Max. Limit £m** | **Max. maturity period** | **Change from existing approach** |
| | | | | |
| CCLA Local Authority Property Fund | Unrated | £8m | n/a | None |
| Multi-Asset or Bond funds | Unrated | £5m per fund | n/a | None |
| Covered Bonds<br>(per bond) | AA- | £6m | 3 years | None |
| Supranational Bonds<br>(per each institution) | AAA | £6m | 3 years | None |
| Debt Management Agency Deposit Facility, Government Bills or Gilts | UK Government | No Limit | 5 years | None |
| Local Authorities / Bank Deposits Collateralised (guaranteed against local authority loans) | UK Government | £10m each authority | 5 years | Reduced limit to £10m |
| Challenger Banks e.g. Aldermore, Metro etc | Unrated | Delegate to Treasury Mgt committee authority to determine criteria to invest up to £3m | | |

5. Borrowing Strategy

5.1 The Council has a need to fund its capital plans from borrowing. This section of the report sets out the Council's approach to borrowing externally should it become necessary for reasons such as additions to the authorised capital programme, for short term liquidity purposes or it simply becomes the most effective method of funding.

5.2 The Council has enough cash to fund its expenditure needs. This cash is not capital resource so though expenditure can be met from it, the Council in its accounts needs to reflect capital expenditure is being financed from internal borrowing of non-capital cash. The cash internally borrowed would have been invested at around 1% (best case in funds is 3%), given that rate of interest on external borrowing would be above 1% and long-term interest rates are not expected to rise for a number of years, it is more cost effective to run down investments. This achieves benefit for the taxpayer by investing low yielding cash into capital expenditure. However, the Director of Finance will monitor external rates of borrowing and the sustainability of using internal borrowing to determine if it becomes more beneficial to externalise the debt.
The authorised and operational borrowing limits for external debt determine the amount the Director of Finance can externally borrow, they are contained in **Appendix 2**. The

Authorised (maximum borrowing limit) will bet set to reflect the maximum overall need to fund capital expenditure set out in the Capital Strategy but in practice the plan is to use internal borrowing.

5.3 When the Authority needs to borrow it will seek to strike a balance between minimising interest costs and securing certainty of borrowing costs. Examples of where the Council can seek to borrow funds from are:

- Public Works Loan Board (PWLB)
- Other UK Local Authorities
- Any institution which meets the Council's investment criteria
- UK public or private sector pension funds (Excluding the Essex Local Authority Pension Fund)

5.4 Officers may decide to undertake very short term borrowing for liquidity purposes.

5.5 In addition to borrowing via loans, other debt financing models may be used to finance the capital programme where this represents best value for the authority. These forms of debt are included in the overall borrowing limits. Such debt finance models include:

- Sale and leaseback arrangements
- Hire purchase arrangements

6. <u>Role of the Treasury management sub-committee</u>

6.1 The Sub-committee will be informed of investment activity and of significant changes in conditions that lessen or increase the risks of the Council's Treasury Management activity. The Sub-committee will recommend changes to officers and where necessary report back to Council.

## Treasury Management Performance Indicators

**At 30/11/2019**

## Security

| | Month ending | Projection year ending | Target for year | Target for year | Target for year | Target for year |
|---|---|---|---|---|---|---|
| | *30/11/2019* | *31/03/2020* | *2019/20* | *2020/21* | *2021/22* | *2022/23* |
| Require -Only to invest with approved counterparties | No breach | No breach | No breach | No breach | No breach | No breach |
| Require- Only to invest up to approved limits | One breach | One breach | No breach | No breach | No breach | No breach |
| Target Bail in exposure to not exceed portfolio* | 43.50% | 50.00% | 50.00% | 50.00% | 50.00% | 50.00% |

* The method for this calculation was changed in the Mid Year Treasury report to Council

## Liquidity

| | Month ending | Projection year ending | Target for year | Target for year | Target for year | Target for year |
|---|---|---|---|---|---|---|
| | *30/11/2019* | *31/03/2019* | *2019/20* | *2020/21* | *2021/22* | *2022/23* |
| Target - To have minimum amount maturing in 100 days or less | £ 40,180,000 | £ 30,000,000 | £ 10,000,000 | £ 10,000,000 | £ 10,000,000 | £ 10,000,000 |
| Require - Investments maturing in more than 365 days not to exceed target | £ - | £ - | £ 18,000,000 | £ 20,000,000 | £ 20,000,000 | £ 20,000,000 |

| | Actual Borrowing Month ending | Borrowing projection year ending | Target for year | Target for year | Target for year | Target for year |
|---|---|---|---|---|---|---|
| | *30/11/2019* | *31/03/2019* | *2019/20* | *2020/21* | *2021/22* | *2022/23* |
| Requirement -Authorised Limit of Borrowing not to exceed | £ Nil | £ Nil | £ 45,000,000 | £ 45,000,000 | £ 45,000,000 | £ 45,000,000 |
| Target - Operational Boundary of Borrowing (excluding finance leases) | £ Nil | £ Nil | £ 25,000,000 | £ 25,000,000 | £ 25,000,000 | £ 25,000,000 |

## Yield

| | Month ending | Projection year ending | Projected benchmarks | Projected benchmarks | Projected benchmarks |
|---|---|---|---|---|---|
| | *30/11/2019* | *31/03/2019* | *2020/21* | *2021/22* | *2022/23* |
| Average yield on liquid portfolio | 0.72% | 0.72% | | | |
| 3 month Libid benchmark | 0.63% | 0.63% | 0.75% | 0.75% | 0.75% |
| Average yield on strategic portfolio | 4.14% | 4.14% | | | |
| Average yield on total portfolio | 1.20% | 1.20% | | | |
| 1 year Libid benchmark | 0.85% | 0.85% | 0.85% | 0.85% | 0.85% |

APPENDIX 2