



AGENDA ITEM 07

**JOINT AUDIT COMMITTEE
25 MARCH 2021**

**TREASURY MANAGEMENT STRATEGY
2021/22 REPORT**

1. PURPOSE OF REPORT

- 1.1 This report sets out the Police and Crime Commissioner's Treasury Strategy Statement for 2021/22 and updates on debt management activity and investment activity during the financial year 2020/21.
- 1.2 This report also updates on recent Treasury Management activity, in line with recommended best practice and the revised CIPFA Code of Practice for Treasury Management.
- 1.3 It is important to note that financial information contained within this report should not be used by any individual or organisation as a basis for making investment or borrowing decisions. The Commissioner and his treasury advisers will not accept any liability on behalf of any individual or organisation who seeks to act on the financial information contained within this report.

2. INTRODUCTION AND BACKGROUND

- 2.1 The Commissioner is legally required to produce an Annual Investment Strategy. Therefore, included is an Investment Strategy as part of the Treasury Strategy Statement shown in **Appendix B**.
- 2.2 In order to protect the Commissioner's position if an individual or organisation were to act upon this advice, it is deemed necessary to produce a disclaimer, which is shown as a note at the head of **Appendix B**.

2.3 The Commissioner is responsible for administering a Capital Programme of £150.2m between 2021-22 and 2024-25. As far as possible all surplus revenue money and other reserves are invested on a daily basis until they are required.

2.4 The Commissioner follows the Code of Practice for Treasury Management produced by the Chartered Institute of Public Finance and Accountancy (CIPFA). The Code emphasises the following key points:

- The Commissioner must formally adopt the Code.
- The strategy report will affirm that the effective management and control of risk are prime objectives.
- The Commissioner's appetite for risk must be clearly identified within the strategy report and the priority given to security of capital and liquidity when investing funds and an explanation as to how that will be carried out.
- Responsibility for risk management and control lies within the organisation.
- Credit ratings should be used as a starting point when considering risk but use should also be made of market data and information, the financial media, information on government support for banks and the credit ratings of that government support.
- The Commissioner needs a sound diversification policy with high credit quality counterparties and should consider setting country, sector and group limits.
- Borrowing in advance of need is only allowed when there is a clear business case for doing so and only for the current capital programme or to finance future debt maturities.
- There needs to be, at a minimum, a mid-year review of treasury management strategy and performance to highlight any areas of concern that have arisen since the original strategy was approved.
- The Commissioner must delegate the role of scrutiny of treasury management strategy and policies to a specific named body.
- Treasury management performance and policy setting should be subjected to prior scrutiny.
- The Commissioner, and his staff, should be provided with access to relevant training as those charged with governance are also personally responsible for ensuring they have the necessary skills and training.
- Officers involved in treasury management must be explicitly required to follow treasury management policies and procedures when making investment and borrowing decisions on behalf of the Commissioner.

2.5 The Commissioner's Treasury Management activity is governed by the following documents:

- 1 **Treasury Policy Statement.** This is a statement, defining treasury management and the general approach to it. It emphasises firstly the control of risk and secondly the pursuit of best value as the main factors defining the approach. A copy is attached at **Appendix A.**
- 2 **Treasury Management Practices (TMPs) and Schedules to TMPs.** TMPs define the overall approach to various aspects of treasury management, including such things as risk management, performance monitoring and management, segregation of duties and dealing arrangements, cash flow management, money laundering and staff training. The Schedules to TMPs deal with the criteria for selecting third parties (banks and building societies) with whom the Commissioner is prepared to deposit funds. The TMPs and Schedules are reviewed regularly by the Commissioner's CFO and electronic copies are available on request.

3 Annual Treasury Strategy Statement details the expected activities of the treasury function in the financial year 2021-22. A copy is attached at **Appendix B**.

3. DEBT MANAGEMENT ACTIVITY 2020/21

- 3.1 Since April 1986, the Police Authority had been incurring long term debt from the Public Works Loans Board to finance major capital expenditure. All the borrowing was transferred to the Commissioner in November 2012.
- 3.2 Borrowing at the 31 March 2021 is expected to total £94.5m, all at fixed rates and repayable over various periods up to 2069.
- 3.3 The Commissioner has the capacity to undertake variable rate borrowing (up to 20% of the total debt portfolio) should the need arise or to take advantage of favourable rates to fund identified need.
- 3.4 One loan for £2.8m matured during 2020/21 and no new borrowing was taken out. PWLB rates dropped 100 basis points (1%) in November 2020 in response to a consultation. The current borrowing rate represents the lowest that has been available for some time.
- 3.5 As a result of the loan maturing there was a change to the average rate of interest payable on debt from 3.32% to 3.29%. Link Asset Services, the Commissioner's treasury advisors, continue to advise on debt restructuring to enable the Commissioner to take advantage of opportunities to reduce the overall cost of debt, set in the context of the financial constraints and markets. There were no opportunities for this during 2020/21. This is likely to be the case for the foreseeable future with low interest rates forecast in the context of the national economy.
- 3.6 The table below shows the level of borrowing during 2019/20 and the average interest rate and the change since 2019/20.

PWLB Borrowing

Loan Type	Borrowing £'m		Average Interest Rates %	
	2019/20	2020/21	2019/20	2020/21
Fixed	97.3	94.5	3.32	3.29
Variable	0.0	0.0	0.0	0.0
Total	97.3	94.5	3.32	3.29

4. INVESTMENT ACTIVITY 2020/21

- 4.1 Any surplus funds have been invested on a daily basis. The target was to achieve an average return on investments as close as possible to the 3 month London Inter Bank Offer Rate (LIBOR).
- 4.2 Interest earned on investments up to the end of March 2021 is predicted to average 0.25%, approximately 21 basis points above the average return on 3 month LIBOR (0.04%) as at 01/02/20. This represents good performance amid concerns about Coronavirus, Brexit uncertainty, and expectations of a further Base Rate cut.

- 4.3 From 2021/22 the benchmark to measure return on investments will be the Sterling Overnight Index Average (SONIA). LIBOR will no longer continue to be offered beyond the end of 2021 and the Bank of England recommends SONIA as its preferred replacement. The main differences in these two rates are as follows:
- SONIA, unlike LIBOR, is purely an overnight rate
 - LIBOR contains bank risk, but SONIA is near risk-free (and therefore the return will be lower)
 - LIBOR is forward-looking, but SONIA is based on past transactions
- 4.4 The Commissioner approved a list of counter parties with whom investments could be placed for 2020/21. At 8 February 2021, the Commissioner had £76m invested with a range of maturity dates between fourteen days and three years, and a further £5m with CCLA with no maturity date.
- 4.5 All of the Commissioner's investments are with UK based entities: 69% Local Authorities, 25% British Banks/Building Societies, 6% CCLA as at 24/02/21 (see **Appendix D**). Since the final recovery, in January 2014, of investments frozen in the Icelandic bank Landsbanki, the Commissioner has held no investments with foreign banks.
- 4.6 Based on market information provided by Link Asset Services, the counter party list has been fully reviewed to reflect: current market conditions, credit ratings of sovereign nations, and the impact of Government support for the banking sector. As a consequence, the limits, both financial and duration, have been adjusted for some institutions. Specifically the group and individual limits (£65m) for the part government owned institutions (National Westminster Bank, Royal Bank of Scotland) have been increased by £5m as it is considered that they are less risky than other UK institutions that are not directly supported by the government. (The NatWest group are the bankers for the PCC)
- 4.7 Similarly all Local Authorities are eligible for inclusion on the counter party list because ultimately they have the support of the national government. However, during 2020 it became known that some Local Authorities issued Section 114 notices, effectively stating they cannot balance the budget for the year and placing a freeze on any non-essential spending. (It should be noted that the repayment of investments fall outside the scope of this as it is a legal obligation). As a result of this, additional due diligence is now carried out on any Local Authority investments to ensure that investments are secure and to avoid any adverse publicity.
- 4.8 If institutions now fall below the set criteria they have been removed from the list and added if they become eligible. A copy of the latest list, which will be kept under review by the Commissioner's CFO, in accordance with the TMP Statements, is attached at **Appendix C**. Details of the criteria are contained within the annual investment strategy in **Appendix B**.
- 4.9 The day to day work of Treasury Management is carried out in the Finance Department with oversight from the Director of Commercial Services. The Treasury Management Strategy is therefore managed using appropriate delegations and periodic management reporting to the Director of Commercial Services and the Commissioner's CFO. This will continue for the next financial year.

5 TREASURY STRATEGY STATEMENT 2021/22

- 5.1 The Treasury Strategy Statement covers the Commissioner's latest capital funding requirements, view of interest rate movements, and strategy for borrowing and

investment in the light of that view. As such, it needs to be reviewed annually. The Treasury Strategy Statement for 2021/22 is attached at **Appendix B**.

5.2 Following the UK's exit from the EU on 31 December 2020 the expectations for interest rates over the next twelve months, which will be subject to continuous review with the Commissioner's treasury advisors and are caveated by recent market volatility following market responses to the Coronavirus outbreak, are as follows:

Short-term rates.

- The Bank of England Base Rate was lowered to 0.1% on 19 March 2020 in response to Government policy regarding the Coronavirus outbreak. The forecast is that rates are unlikely to rise above 0.1% for a considerable period of time.
- As the Base Rate underpins investment returns it is unlikely that this forecast is an under estimate especially if the economic growth is weaker than currently anticipated or there is negative fallout from the UK's exit from European Union. The low interest rates will continue to depress future interest receivable estimates and an average investment return of sub 0.20% on new investments made in 2021/22 can be expected. Further detail can be found in **Appendix B**.

Long-term rates.

- Very long term rates (50 year PWLB rate) are 2.15%. This follows a 100bps (basis points-1%) drop in late 2020 following a consultation.
- Long term rates (25 year PWLB rate) are 2.32% (rates correct as at 23/02/2021)
- The view of long term rates will affect the borrowing strategy in 2021/22. The Estates Strategy has highlighted the need to borrow and borrowing rates are currently very attractive and should remain low for some time.

5.3 The Local Government Act 2003 introduced a new system of "prudential borrowing" which allows the Commissioner to set borrowing limits subject to criteria of prudence and affordability. These criteria are set out in more detail in the CIPFA Prudential Code that specifically requires a number of prudential indicators are set. The full range of prudential indicators was considered when the 2021/22 Budget and Precept were agreed in February 2021. This is particularly relevant when set in the context of the overall limitation of planned capital resources and therefore a potential increase in prudential borrowing across the medium term plan. The proposed indicators that relate to treasury management, including the Estates Strategy, are set out in the Treasury Strategy Statement.

5.4 The Local Government Act 2003 also requires the Commissioner to set out a treasury strategy for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance issued subsequent to the Act); this sets out the Commissioner's policies for managing investments and for giving priority to the security and liquidity of those investments.

6. FINANCIAL IMPLICATIONS

6.1 The financial implications of the Treasury Management function are included in the Commissioner's annual budget. The estimated total net cost of capital financing in 2021/22 (including direct charges to revenue) is £7.0m.

7. LEGAL IMPLICATIONS

- 7.1 These matters are governed by Part IV of the Local Government and Housing Act 1989 and Section 111 of the Local Government Act 1972, which empowers the Commissioner to do anything which is calculated to facilitate or is conducive or incidental to the discharge of their various statutory functions.
- 7.2 Adoption of the CIPFA Code of Practice on Treasury Management in the Public Services as part of the Commissioner's Standing Orders and Financial Regulations gives it the status of "a code of practice made or approved by or under any enactment" and hence proper practice under the provisions of the Local Government and Housing Act 1989.
- 7.3 The Commissioner's CFO continues to delegate the responsibility for the discharge of Treasury Management on a daily basis to the Director of Commercial Services through the appropriate Finance Department staff.

8. EQUALITY IMPLICATIONS

- 8.1 Any issues of Equality and Diversity that may arise during the undertaking of Treasury Management activities will be noted, considered and reported upon.

9. RECOMMENDATIONS

- 9.1 It is recommended that the Joint Audit Committee:
- a. note the treasury management activity in 2020-21 set out in paragraphs 3 and 4, and the interest rate observations in paragraph 5.
 - b. Approve the Treasury Strategy Statement for 2021/22 set out in **Appendix B**.
 - c. Approve the criteria for selecting counter parties in **Appendix B** and the current eligible counter parties and their limits as set out in **Appendix C**.
 - d. Continue to include a mid-year review of Treasury Management activity in the Joint Audit Committee's work plan in accordance with the CIPFA Code of Practice for Treasury Management.

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TREASURY POLICY STATEMENT AND TREASURY MANAGEMENT PRACTICES

TREASURY POLICY STATEMENT

1. The Commissioner defines treasury management activities as:
 - the management of cash flows;
 - banking, money market and capital market transactions;
 - the effective control of the risks associated with those activities;
 - the pursuit of optimum performance consistent with those risks.
2. The Commissioner regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Commissioner.
3. The Commissioner acknowledges that effective treasury management will provide support towards the achievement of business and service objectives. It is therefore a commitment to the principles of achieving best value in treasury management, and to employing suitable performance measurement techniques within the context of effective risk management.
4. Treasury operations are managed within the overall strategy approved by the Commissioner at the following levels:
 - Formal reviews of strategy and performance by the Commissioner's CFO, Director of Commercial Services, and Assistant Director Finance in conjunction with representatives from the external advisors (Linked Asset Services).
 - Monthly monitoring is conducted by the Commissioner's CFO, Director of Commercial Services and Assistant Director Finance.
 - On a daily basis by trained staff under the direction of the Assistant Director Finance.
 - Reports to the Joint Audit Committee and treasury activity.
 - The annual review of the strategy for the Commissioner.

APPENDIX B

Note:

It is important to note that the Treasury Strategy Statement is adopted by the Commissioner based upon advice from external treasury advisors, and accordingly the Strategy is tailored to meet the specific and unique needs of the Commissioner. All financial information contained within this Report and Statement should not be used by any individual or organisation as a basis for making investment or borrowing decisions. The Commissioner and the treasury advisors will not accept any liability on behalf of any individual or organisation who seeks to act on the financial information contained within this Report and Statement.

TREASURY STRATEGY STATEMENT 2021/22

1.0 INTRODUCTION

1.1 This Treasury Strategy Statement details the expected activities of the treasury function in the financial year 2021/22. The suggested strategy is based upon views of interest rates as advised by external advisors, supplemented with leading market forecasts. The strategy covers:

- the current portfolio position;
- prudential indicators;
- prospects for interest rates;
- the borrowing requirement & strategy;
- the investment strategy;
- debt rescheduling opportunities; and
- MRP strategy.

2.0 CURRENT PORTFOLIO POSITION

2.1 The Commissioner's estimated portfolio position as at 1st April 2021 will be as follows:

<u>Treasury Investments</u>	
	£m
Maturity less than 1 year	46.8
Maturity between 1 and 5 years	10.0
CCLA	5.0
	61.8
<u>Treasury external borrowing</u>	
-PWLB fixed rate	93.8
- PWLB variable rate	0.0
	93.8
Net Treasury Borrowing	-32.0

2.2 The average rate of interest on the above debt is expected to be 3.29%.

The treasury investments less than 5 years relates to Bank, Building society and Local Authority Investments. The £5.0m investment placed with CCLA is for at least five years.

3.0 PRUDENTIAL INDICATORS for 2021/22 to 2024/25

- 3.1 The Prudential Code for Capital Finance in Local Authorities (Prudential Code) is applicable to the Police and Crime Commissioner and has been developed by the Chartered Institute of Public Finance and Accountancy (CIPFA) to provide a code of practice to underpin the system of capital finance embodied in Part 1 of the Local Government Act 2003. PCCs, like Local Authorities, are free to determine their own level of capital investment controlled by self-regulation.
- 3.2 The key objectives of the Prudential Code are to ensure that capital investment plans are affordable, prudent and sustainable.
- 3.3 The Prudential Code supports a system of self-regulation that is achieved by the setting and monitoring of a suite of Prudential Indicators that directly relate to each other. The indicators establish parameters within which the PCC should operate to ensure the objectives of the Prudential Code are met.
- 3.4 The Prudential Code introduced requirements for the manner in which capital spending plans are to be considered and approved. It requires the Commissioner to set a number of prudential indicators over a period of three years. The following prudential indicators are relevant for the purposes of setting an integrated treasury management strategy:

External debt

These indicators are intended to ensure that levels of external borrowing are affordable, prudent and sustainable. The authorised limit for external debt is a statutory limit (section 3 of the Local Government Act 2003) that should not be breached under any circumstances. The proposed limits set out below have been calculated to take account of the current Commissioner's capital expenditure and financing plans and allowing for the possibility of unusual cash movements. If this limit is likely to be breached, it would be necessary for the Commissioner to determine if it is prudent to raise the limit or to instigate procedures to ensure that such a breach does not occur.

The operational boundary for external debt is a management tool for day to day monitoring and has been calculated with regard to the Commissioner's capital expenditure and financing plans allowing for the most likely, prudent, but not worst case scenario for cash flow. Temporary breaches of the operational boundary, due to variations in cash flow, will not be regarded as significant.

	2021/22	2022/23	2023/24
	£m	£m	£m
Authorised limit for external debt - Borrowing	125.0	130.0	130.0
Operational boundary - Borrowing	120.0	125.0	125.0

The Commissioner's actual external debt as at 31/03/21 is currently expected to be £94.5m, excluding transferred debt managed by Dudley M.B.C.

CIPFA Code of Practice for Treasury Management in the Public Services

The Commissioner continues to adopt the CIPFA Code of Practice for Treasury Management in the Public Services first adopted by the Police Authority in March 2002.

Interest rate exposures

These indicators allow the Commissioner to manage the extent to which he is exposed to changes in interest rates. The upper limit for fixed interest reflects the fact that it is possible to construct a prudent treasury strategy on the basis of using only fixed rate debt and investments, so long as the maturity dates of these debts and investments are reasonably spread. The same does not apply to variable rates where a 100% exposure could lead to significant year on year fluctuations in the cost of debt. The upper limit for variable rate exposure allows for the use of variable rate debt to offset the exposure to changes in short-term rates on the portfolio of investments. This limit reduces over time as the strategy is to gradually reduce the level of investments.

	2020/21 %	2021/22 %	2022/23 %
Upper limit for fixed interest rate exposure			
Net principal fixed rate borrowing / investments	100	100	100
Upper limit for variable rate exposure			
Net principal variable rate borrowing / investments	20	20	20

Maturity structure of borrowing and Investments longer than 364 days

The purpose of the prudential limits for principal sums invested for periods longer than 364 days is for the Commissioner to contain his exposure to the possibility of loss that might arise as a result of having to seek early repayment of principal sums invested. The maturity structure of fixed rate borrowing is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

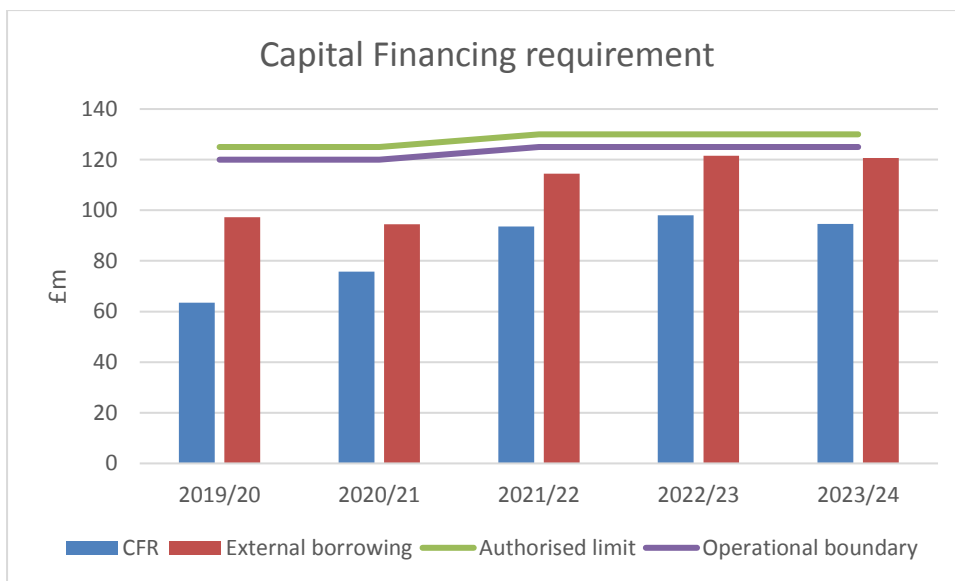
Upper limit of principal invested for periods over 364 days	£40m
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Maturity structure of fixed rate borrowing	Upper limit %	Lower limit %
Under 12 months	25	0
12 months and within 24 months	25	0
24 months and within 5 years	50	0
5 years and within 10 years	75	0
10 years and above	100	25

- 3.5 In considering the capital programme for 2021/22, the anticipated future borrowing requirements were considered in the context of overall capital resources and the impact on the revenue budget.

	31 March 2020 £'m	31 March 2021 £'m	31 March 2022 £'m	31 March 2023 £'m	31 March 2024 £'m
Capital financing requirement (CFR)	63.5	75.8	93.6	98.0	94.6
External borrowing	-97.3	-94.5	-114.5	-121.5	-120.7
Variance	-33.8	-18.7	-20.9	-23.5	-26.1

The CFR is the historic underlying need to borrow for capital expenditure net of all capital receipts, grant, revenue contributions etc. The CFR increases when unfinanced expenditure is incurred and reduces when provision is made to repay that debt.



3.6 External Borrowing is used to finance capital expenditure in land and buildings. Therefore although there is an increased liability on the balance sheet this is offset by increase in the value of assets to be utilised by the commissioner.

4.0 PROSPECTS FOR INTEREST RATES

4.1 The Commissioner continues to use Link Asset Services (LAS) as a treasury advisor and has made use of their services in formulating a view on interest rates. LAS has in turn drawn upon the work of a number of City economic forecasters. Having discussed these, the following view of the prospects for interest rates over the next twelve months and beyond has been derived:

- **Short-term rates.**

The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to first 0.25%, and then to 0.10%, it subsequently left Bank Rate unchanged at its subsequent meetings, including its last meeting on 4th February 2021, although some forecasters had suggested that a cut into negative territory could happen. However, at that last meeting, the BoE were informed that financial institutions were not prepared for implementing negative rates. The Monetary Policy Committee (MPC), therefore, requested that the Prudential Regulation Authority require financial institutions to prepare for such implementation if, at any time in the

future, the MPC may wish to use that as a new monetary policy tool. The MPC made it clear that this did not in any way imply that it was about to use this tool.

- **Long-term rates.**

LINK group have provided the following interest rate forecasts:

Link Group Interest Rate View		8.2.21											
	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
5 yr PWLB	0.90	0.90	0.90	0.90	1.00	1.00	1.10	1.10	1.10	1.20	1.20	1.20	1.20
10 yr PWLB	1.30	1.30	1.30	1.30	1.40	1.40	1.50	1.50	1.50	1.60	1.60	1.60	1.60
25 yr PWLB	1.90	1.90	1.90	1.90	2.00	2.00	2.10	2.10	2.10	2.20	2.20	2.20	2.20
50 yr PWLB	1.70	1.70	1.70	1.70	1.80	1.80	1.90	1.90	1.90	2.00	2.00	2.00	2.00

PWLB rates dropped 100 basis points (1%) in November 2020 in response to a consultation. The current borrowing rate represents the lowest that has been available for some time. As the interest forecasts above shows, there is expected to be little upward movement in PWLB rates over the next two years as government bond yields of major countries around the world are expected to rise little during this time in an environment where central bank rates are also expected to remain low for some years. This is the result of a change of inflation targeting policy of central banks to one based on average inflation over a number of years. From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and sharp changes in investor sentiment (as shown on 9th November 2020 when the first results of a successful COVID-19 vaccine trial were announced). Such volatility could occur at any time during the forecast period.

4.2 While this Commissioner will not be able to avoid borrowing to finance new capital expenditure, to replace maturing debt and the rundown of reserves, there will be a *cost of carry*, (the difference between higher borrowing costs and lower investment returns), to any new borrowing that causes a temporary increase in cash balances.

4.3 The overall strategy will be based on the projections above. However, the Commissioner will maintain flexibility to take account of unexpected variations from the forecast.

5.0 ANNUAL INVESTMENT STRATEGY

5.1 The Commissioner's investment activities have regard to guidance issued by the Government and CIPFA.

5.2 In making investment decisions, the Commissioner's investment priorities will be security first (capital preservation), liquidity second and then yield (return). Pursuit of the best possible return on investments will only be allowed to the extent that this is consistent with very low levels of risk in terms of security and liquidity.

5.3 In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs. However, where appropriate (from an internal as well as external perspective), the Commissioner will also consider the value available in periods up to 12 months with high credit rated financial institutions, as well as a wider range of options.

- 5.4 The borrowing of monies purely to invest or on-lend and make a return is unlawful and the Commissioner will not engage in such activity.
- 5.5 The Commissioner will make use of both specified investments and non-specified investments. Specified investments are those that satisfy the following conditions:
- a) The investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling.
 - b) The Commissioner requires that the investment be repaid or redeemed within 12 months of the date on which the investment was made.
 - c) The investment does not involve the acquisition of share capital or loan capital in any corporate body.
 - d) The investment satisfies any of the following conditions:

The investment is made with the UK government (Debt Management Agency Deposit Facility), a local authority, a parish council or a community council.

The investment is made with a body which has been awarded a “high credit rating” by a credit rating agency.

- If the body is not a UK bank, the sovereign country must be awarded a “high credit rating” by a credit rating agency.

For the purposes of this strategy, use is made of the creditworthiness service provided by Link Asset Services to define a “high credit rating”

- UK banks and building societies – short-term rating F1 or higher and viability rating of “a-” or higher.
- Foreign banks – short-term rating F1+, and a viability rating of a minimum of “a” with a sovereign rating of AAA.
- Money market Funds (MMF’s) – Any AAA rated fund

These will be supported by other accredited rating systems (Standard & Poor’s and Moody’s), credit watches and outlooks, Credit Default Swap data, and information from the financial press. A full list of the credit ratings to be used can be found in **Appendix C**.

- 5.6 Since the credit crisis, there are several semi-nationalised banks in the UK with credit ratings which do not conform to the credit criteria usually used to identify banks which are of high credit worthiness. In particular, as they no longer are separate institutions in their own right, it is impossible for the rating agencies to assign them an individual rating for their standalone financial strength. However, these institutions are now recipients of at least an F2 short term rating (effectively taking on the creditworthiness of the Government). That is deposits made with them are effectively being made to the Government. This relates to National Westminster Bank and Royal Bank of Scotland.
- 5.7 Money market funds (MMFs) are to be used for the first time as a treasury management tool by the Commissioner. They are a type of fixed income fund that invests in debt securities which are characterised by their enhanced diversification, short maturities and minimal credit risk. Money market funds are among the lowest-volatility types of investments. One of the key objectives of MMFs is to provide investors with security of capital and daily liquidity together with an investment return which is comparable to

normal sterling denominated money market interest rates. Broadly, MMFs may invest in certificates of deposit (CD), commercial paper, medium-term notes (MTNs), variable rate notes (VRNs), floating rate notes (FRNs), bankers acceptances, government bonds, treasury bills, Eurobonds, asset-backed securities and corporate bonds. Funds can be deposited and accessed on a daily basis.

- 5.8 The Commissioner’s CFO will monitor credit ratings through the receipt of credit rating bulletins from the treasury management consultants at Link Asset Services. Institutions that cease to meet the criteria above will immediately cease to be treated as specified investments.
- 5.9 Non-specified investments are those that do not meet the criteria in 5.4 to 5.6 above. In determining which categories of non-specified investments may prudently be used, account will be taken of advice from the advisors, Link Asset Services, and, if investments are for 12 months or more, long-term credit ratings will be utilised as determined by Fitch IBCA.
- 5.10 So far, the following categories of investment have been identified as prudent for use for non-specified investments. The table also shows the maximum value of investments that may be held:

Category of investment	Maximum value for this category of investments
Sterling deposits in excess of 364 days with Local Authorities and UK banks (where these are not “specified investments” as defined above).	£40m
Property Funds based in the UK	£5m

- 5.11 Property funds provide investors with long term income and potential long-term capital appreciation. These type of funds are actively managed in a diversified portfolio of commercial property
- 5.12 In determining the maximum period for which investments may be held, regard to the most recent cash flow forecast will be taken. No investment will be entered into where the cash-flow forecast indicates that, as a result of that investment, the Commissioner would be forced to borrow money in a future year that would not otherwise have had to be borrowed.
- 5.13 Also at the time of making a new investment, long-term investments (investments of one year’s duration or more) should not constitute more than 30% of the total pool of investments.
- 5.14 Investments with a single institution should not exceed 25% (15% for Building Societies) of the total pool of investments at month end. Investments with a group of banks should not exceed 30% of the total pool of investments at month end.
- 5.15 There is currently no impact expected on investment or borrowing strategies as a result of United Kingdom leaving the European Union

Future Investment returns & Negative Interest rates

- 5.16 While the Bank of England said in August / September 2020 that it is unlikely to introduce a negative Bank Rate, at least in the next 6 -12 months, and in February 2021 stated that financial institutions would not be ready to implement negative rates for six months, some deposit accounts were offering negative rates for shorter periods prior to this latest announcement. As part of the response to the coronavirus pandemic and lockdown, the Bank and the Government have provided financial markets and businesses with plentiful access to credit, either directly or through commercial banks. In addition, the Government has provided large sums of grants to local authorities to help deal with the COVID crisis; this has caused some local authorities to have sudden large increases in cash balances searching for an investment home, some of which was only very short term until those sums were able to be passed on. Investment return expectations for the next 12 months are likely to be sub 0.2% due to the unlikely event of bank rate increasing from 0.10% for a considerable period. (Bank of England base rate is the primary driver for investment returns from other institutions such as banks and Local Authorities)

As for money market funds (MMFs), yields have fallen near to zero. Some managers have resorted to trimming fee levels to ensure that net yields for investors remain in positive territory where possible and practical. Investor cash flow uncertainty, and the need to maintain liquidity in these unprecedented times, has meant there is a surfeit of money swilling around at the very short end of the market.

Inter-local authority lending and borrowing rates have also declined due to the surge in the levels of cash seeking a short-term home at a time when many local authorities are probably having difficulties over accurately forecasting when disbursements of funds received will occur or when further large receipts will be received from the Government.

6.0 CAPITAL BORROWING REQUIREMENT & STRATEGY

- 6.1 The Commissioner's CFO has undertaken a review of capital investment requirements and likely resource levels. Although there is some uncertainty around specific requirements and future funding levels, it is likely that there will be a need to borrow further to fund the Estates Strategy over the life of the Capital Programme.
- 6.2 Forecasts suggest that there are potential borrowing options available. Short Term borrowing may be attractive throughout 2021/22 as it is expected to be cheaper than long term fixed borrowing. Under 10 year PWLB rates are forecast to be lower than longer term borrowing which could enable the spread of debt maturities as the focus in recent years has been to concentrate on long dated debt.
- 6.3 As mentioned previously PWLB rates dropped to their lowest point in November 2020. Alternative sources of borrowing are available and the Municipal Bonds Agency have issued a bond on behalf of a Local Authority.
- 6.4 The next financial year is expected to see a continuation of the relatively low bank rate which may present an opportunity to review the Commissioner's external borrowing strategy. If investments exceed the borrowing requirement over the next year, and cash can be accessed from maturing investments, consideration needs to be given to the potential of internal borrowing.
- 6.5 As long term borrowing rates are expected to be higher than rates on the loss of investment income, and look likely to be so going forward, it may be preferable to avoid some new external borrowing to maximise savings in the short term. A reduction of investments also has the benefit of reducing exposure to interest rate and credit risk.

- 6.6 The Commissioner's CFO will continue to cautiously monitor the interest rate market and adopt a pragmatic approach to any changing circumstances such as the evolving Estates Strategy or deployment of new technology.

7.0 DEBT RESCHEDULING AND PREMATURE REPAYMENT OPPORTUNITIES

- 7.1 The introduction of different PWLB rates on 1 November 2007 for new borrowing as opposed to early repayment of debt, and the setting of a spread between the two rates (of about 40 – 50 basis points for the longest period loans narrowing down to 25 – 30 basis points for the shortest loans), has meant that PWLB to PWLB debt restructuring is now much less attractive.
- 7.2 Due to short term borrowing rates expected to be considerably cheaper than longer term rates, there may be 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 their short term nature and the cost of refinancing short term loans as they mature. Any rescheduling and repayment of debt is likely to cause a rebalancing of the Commissioner's debt maturities towards a flatter maturity profile because in the past there has been a concentration on longer dated PWLB loans.
- 7.3 The potential for making savings by reducing investment balances by repaying debt prematurely will be considered as short term rates on investments will be lower than rates paid on currently held debt. However, this will need careful consideration in the light of premiums that may be due on early debt repayment. It is therefore unlikely that this will be economically attractive.

8.0 MINIMUM REVENUE PROVISION STRATEGY

- 8.1 Capital expenditure is expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, and equipment. Occasionally the Commissioner has to borrow to fund this expenditure. The loans taken out for this purpose are fully repayable at a future point in time (they are paid off at maturity and not in instalments). The concept of Minimum Revenue Provision was introduced to prescribe a minimum amount which must be charged to the revenue account each year in order to make provision to meet the cost of that borrowing.
- 8.2 The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 which came into force on 31 March 2008 states that an annual MRP statement needs to be produced which details the methodology for the charge to revenue for debt redemption. The Regulations require that the Commissioner "shall determine for the current financial year an amount of minimum revenue provision which it considers to be prudent".
- 8.3 Methods of making prudent provision for MRP include four options. Options 1 and 2 should only be used in relation to Capital expenditure incurred before 1 April 2008 and Capital expenditure incurred on or after that date which the Commissioner is satisfied forms part of Supported Capital Expenditure. For all unsupported borrowing covered by the Prudential Code on or after 1 April 2008, Options 3 or 4 must be used.
- 8.4 The MRP options are:

- **Option 1 – Regulatory Method.** MRP is equal to the amount determined in accordance with the former sections 28 and 29 of the 2003 Regulations as if they had not been revoked.
- **Option 2 – Capital Financing Requirement Method.** MRP is equal to 4% of the Capital Financing Requirement at the end of the previous year.
- **Option 3 – Asset Life Method.** Revenue provision is spread over the determined useful life of the Asset either in equal instalments or using an annuity method. The first charge can be delayed until the asset is operational.
- **Option 4 – Depreciation Method.** MRP is equal to the provision required in accordance with depreciation accounting in respect of the asset.

8.5 It is recommended that for 2021/22, Option 2 will continue to be used for Capital expenditure incurred before 1 April 2008. For all subsequent Capital expenditure financed by Borrowing, the equal instalment method of Option 3 will be used. In the future it will be necessary to choose which assets are financed by borrowing carefully since the useful lives of the assets could increase or decrease MRP charges.

APPENDIX C

EXTERNAL INVESTMENTS - APPROVED COUNTERPARTY LIST 2021/22

BRITISH BANKS & SUBSIDIARIES	FITCH RATING				LIMIT £m	GROUP LIMIT	PERIOD
	L/T	S/T	Viab	Sup			
Lloyds Banking Group						30	6mth
Lloyds Bank	A+	F1	a	5	30		6mth
Bank of Scotland	A+	F1	a	5	30		6mth
RBS Group						65	1 year
National Westminster	A+	F1	a	5	65		1 year
Royal Bank of Scotland	A+	F1	a	5	65		1 year
HSBC	A+	F1+	a	1	30		1 year
Santander UK plc	A+	F1	a	2	30		6mth
Standard Chartered Bank	A+	F1	a	5	30		6mth
Barclays	A+	F1	a	1	30		6mth
Bank of England (DMADF)					100		1 year +

BUILDING SOCIETIES	FITCH RATING				LIMIT £m	PERIOD
	L/T	S/T	Viab	Sup		
Nationwide	A	F1	a	5	30	6mth
Leeds	A-	F1	a-	5	30	100 days
Skipton	A-	F1	a-	5	30	100 days
Yorkshire	A-	F1	a-	5	30	100 days
Coventry	A-	F1	a-	5	30	3mth

FOREIGN COUNTRIES	NATIONAL RATING	LIMIT £m	PERIOD
Canada	AAA	20	3mth
Denmark	AAA	20	3mth
Germany	AAA	20	3mth
Netherlands	AAA	20	3mth
Singapore	AAA	20	3mth
Sweden	AAA	20	3mth
Switzerland	AAA	20	3mth
USA	AAA	20	3mth

Investments with foreign banks will only be made if they are in Sterling and it is with a British subsidiary. The minimal national credit rating for the bank must then be AAA.

LOCAL AUTHORITIES	LIMIT for each LA £000	PERIOD
All Local Authorities**	30	1 year+

** Local authorities may be subject to lower limits throughout the year if they are deemed to be under severe financial stress.

Money Market funds		LIMIT £000	PERIOD
All	AAA	30	<1 year

Long Term Ratings AAA to DDD the best quality to junk bonds

Short Term Ratings F1+ to F3 the safest to the riskier

Viability Rating aaa to bbb as its title suggests

Support Rating 1 to 5 how well backed by sovereign nation

Local Authorities are assumed to have the same ratings as UK Government.

APPENDIX D

INVESTMENTS AS AT 24/02/21

Maturity	Borrower	Principal £	Rate %	Rating
05-Mar-21	Coventry Building Society	10,000,000	0.02	F1
25-Mar-21	Isle of Wight County Council	5,000,000	0.85	Local Authority
31-Mar-21	Oxford City Council	5,000,000	0.05	Local Authority
08-Apr-21	Leeds Building Society	10,000,000	0.02	F1
19-Apr-21	Slough BC	5,000,000	0.25	Local Authority
23-Apr-21	Surrey County Council	5,000,000	0.02	Local Authority
28-May-21	Fife Council	5,000,000	0.85	Local Authority
01-Jul-21	Corby Borough Council	5,000,000	0.06	Local Authority
05-Jul-21	London Borough of Croydon	10,000,000	0.90	Local Authority
13-Aug-21	Staffordshire Moorlands DC	1,000,000	0.40	Local Authority
25-Mar-22	Wokingham BC	5,000,000	1.45	Local Authority
07-Jul-23	Dudley MBC	10,000,000	1.70	Local Authority
	Total	76,000,000		
5 to 10 years	CCLA	5,000,000		Property Fund