Agenda Item: 7

Meeting of:	**Cabinet**
Date of Meeting:	**Monday, 03 February 2020**
Relevant Scrutiny Committee:	Corporate Performance and Resources
Report Title:	Treasury Management and Investment Strategy 2020/21 and Update for 2019/20
Purpose of Report:	To provide an interim report on the Council's Treasury Management operations for the period 1st April to 31st December 2019 and to submit for consideration the proposed 2020/21 Treasury Management and Investment Strategy.
Report Owner:	Report of the Executive Leader and Cabinet Member for Performance and Resources
Responsible Officer:	Carys Lord, Section 151 Officer
Elected Member and Officer Consultation:	None
Policy Framework:	This report needs to be referred to Council for approval

Executive Summary:

- This interim report provides an update on the Council's Treasury Management operations for the period 1st April to 31st December 2019. All activities were in accordance with the Council's approved strategy on Treasury Management. Details of monies borrowed and repaid and those invested are outlined in the report.
- The report presents the proposed 2020/21 Treasury Management and Investment Strategy at Appendix 1.
- The Council must ensure that the Prudential Code is complied with, which has been developed by CIPFA as a professional code of practice. To demonstrate the Council has fulfilled these objectives, the Code sets out prudential indicators that should be used and the factors that must be taken into account. These are shown in Appendix 1 as part of the Strategy.
- The Council also has a legal requirement to comply with the Welsh Government Guidance on Investments and has taken this into consideration when developing the Strategy.
- Capital expenditure when financed by long term debt incurs two elements of cost, interest on and repayment of the principal sum borrowed. The resources the Council must put aside in each

year to repay the principal sum borrowed is known as Minimum Revenue Provision (MRP) and the Council's policy for calculation is detailed in the report.

- The Treasury Management Policy for 2020/21 is attached at Appendix 2.

Recommendations

1. That the Treasury Management interim report for the period 1st April to 31st December 2019 be endorsed.
2. That the policy for making Minimum Revenue Provision in 2020/21 be approved.
3. That Cabinet recommend to Council that the proposed 2020/21 Treasury Management and Investment Strategy be approved including the following specific resolutions (detailed in Appendix 1):

• The Authorised Limit for External Debt be set at £210.541m for 2019/20, £228.394m for 2020/21, £255.520m for 2021/22 and £271.600m for 2022/23.

• The Operational Boundary for External Debt be set at £203.608m for 2019/20, £221.461m for 2020/21, £246.087m for 2021/22 and £264.667m for 2022/23.

• The Section 151 Officer be given delegated authority within the total Authorised Limit and Operational Boundary as estimated for individual years to effect movement between the separately agreed limits for borrowing and other long-term liabilities.

• An upper limit is set on its fixed interest rate exposures of £147.810m for 2019/20, for 2020/21 of £168.021m, for 2021/22 of £204.111m and for 2022/23 of £221.408m of its net outstanding principal sum on its borrowings / investments.

• An upper limit is set on its variable interest rate exposures of £0 for 2019/20, 2020/21, 2021/22 and 2022/23 of its net outstanding principal sum on its investments.

• An upper limit of £0m for 2019/20, £10m for 2020/21, £10m in 2021/22 and £10m in 2022/23 is set for total principal sums invested for over 364 days.

• The amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate for 2020/21 be set as

	Upper Limit	**Lower Limit**
Under 12 months	20%	0%
12 months and within 24 months	20%	0%
24 months and within 5 years	30%	0%
5 years and within 10 years	40%	0%

10 years and above	100%	0%

- The Prudential Indicators set out in Appendix 1 be approved.
- The Treasury Management Policy set out in Appendix 2 be approved

Reasons for Recommendations

1. To present the Treasury Management Interim Report.
2. To agree the basis of the Minimum Revenue Provision calculation for 2020/21.
3. The Treasury Management and Annual Investment Strategy is prepared as required by the Local Government Act 2003.

1. Background

1.1 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.

1.2 The second main function of the Treasury Management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

1.3 The contribution the Treasury Management function makes to the Council is critical, as the balance of debt and investment operations ensure liquidity to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

1.4 Revised reporting is required for the 2019/20 reporting cycle due to revisions of the Welsh Government Investment Guidance, the Welsh Government Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a Capital Strategy, to provide a longer-term focus to the capital plans and greater reporting requirements surrounding any commercial activity which may be undertaken by the Council. This Council has not engaged in any commercial investments and the Councils only non-treasury investment is its investment in the big fresh catering company.

1.5 The Capital Strategy is being reported to members as a separate report on this agenda.

1.6 The Welsh Government (WG) provides the Council with a General Capital Funding grant and the Council is also advised of a level of borrowing that WG is prepared to fund via the Revenue Support Grant Settlement (supported borrowing). If the Council wishes to borrow in excess of this level to increase its capital expenditure, then it can. However, it will either have to find the additional costs of borrowing through revenue savings in other services or increases in Council Tax.

1.7 In order to manage this increased flexibility, Part 1 of the Local Government Act 2003 requires local authorities to have regard to the Prudential Code, which has been developed by the Chartered Institute of Public Finance and Accountancy (CIPFA) as a professional code of practice.

1.8 The key objectives of the fully revised Prudential Code are to ensure that the capital investment plans of local authorities:

- Are affordable;
- That all external borrowing and other long-term liabilities are within prudent and sustainable levels; and
- The treasury management decisions are taken in accordance with professional good practice.

2. Key Issues for Consideration

Treasury Management Reporting

2.1 In March 2018 the Council adopted the CIPFA Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code) which together with the WG revised guide on Local Government Investments (April 2010), requires the Council to receive and approve as a minimum three main treasury reports each year which incorporate a variety of policies, estimates and actuals. All reports will be reviewed at Cabinet and Scrutiny Committee before being reported to Council. These are as follows:

Treasury Management & Investment Strategy

2.2 A report presented and approved before the start of the financial year which is forward looking and covers the Authority's:

- Capital Plans (including prudential indicators);

- Minimum Revenue Provision (MRP);
- The Borrowing Strategy; and
- Investment Strategy

Mid-Year Treasury Management Report

2.3 A progress report which update members on Council's treasury activities to date and to provide an opportunity to revise policy or prudential indicators if required.

Annual Treasury Management Report

2.4 A backward-looking review report comparing actual outturn to estimates together with a selection of actual prudential and treasury indicators.

2.5 The proposed Treasury Management and Investment Strategy for 2020/21, is attached at Appendix 1. The Treasury Management Strategy itself covers a rolling period of three years and is intended to link into the Medium Term Financial Planning process. The Investment Strategy covers the next financial year. The document also includes a number of statutory Prudential Indicators that may be used to support and record local decision-making.

2.6 The Prudential Indicators that have been included in this Strategy will need to be revised during 2020/21 to reflect the changes to the treatment of lease liabilities and associated financing charges as required by IFRS 16.

Proposed Strategy 2020/21

Balance Sheet Projections

2.7 To assist the Treasury team in arriving at their Borrowing and Investment strategies for 2020/21 balance sheet projections have been prepared. These projections reflect the Final Capital Proposals 2020/21 to 2024/25. The projections also take into account the advice of our Treasury Management Advisers that interest rates are expected to remain low as are investment returns during the period and therefore seeks to maximise the use of reserves and spare cash balances to finance capital expenditure.

2.8 It is important that the level of Internal Borrowing as a percentage of the total borrowing requirement is kept under review by the Council to monitor the interest rate risk that the Council is exposed to.

2.9 As well as monitoring the use of internal borrowing these projections consider the levels of funds available for investment and the levels of external borrowing required in future years.

	2020/21	2021/22	2022/23	2023/24	2024/25
	£000	**£000**	**£000**	**£000**	**£000**
Capital Financing Requirement	216,739	238,743	253,030	263,248	270,792
Less External Borrowing	174,122	208,212	225,509	235,670	243,115
Internal Borrowing	**42,617**	**30,531**	**27,521**	**27,578**	**27,677**
Internal borrowing as a % of Capital Financing Requirement	**20%**	**13%**	**11%**	**10%**	**10%**
Reserve/Capital Grant Balances/Provisions	65,295	58,568	56,539	56,539	56,539
Capital Receipts	9,870	2,050	1,273	1,273	1,273
Total Cash Backed Reserves and Provisions	**75,165**	**60,618**	**57,812**	**57,812**	**57,812**
Less External Investments Target	30,000	30,000	30,000	30,000	30,000
Balance Available for Internal Borrowing	**45,165**	**30,618**	**27,812**	**27,812**	**27,812**

	2020/21	2021/22	2022/23	2023/24	2024/25
	£000	£000	£000	£000	£000
Working Capital Surplus	15,617	15,617	15,617	15,617	15,617
Projected External Investments	32,548	30,087	30,291	30,234	30,135
Total Projected Investments Balance	**48,165**	**45,704**	**45,908**	**45,851**	**45,752**

Borrowing Strategy

2.10 The Council's approach to the borrowing requirements in recent years on the advice of the Council's Treasury Management adviser has been to adopt a policy of avoiding new external borrowing by running down spare cash balances and reserves to finance capital expenditure. This policy has been based on the high levels of reserves held by the Council and because interest rates and investment returns have been forecast to remain low during this period.

2.11 The Council's Final Capital Proposals 2020/21 to 2024/25 forecast borrowing (supported and unsupported borrowing) in the period as set out in the table below. The Council is also projecting to use £12.314m of Capital receipts between 2020/21 and 2024/25.

Scheme	**2020/21**	**2021/22**	**2022/23**	**2023/24**	**2024/25**	**Total**
	£000	**£000**	**£000**	**£000**	**£000**	**£000**
General Fund						
General Capital Funding Supported Borrowing	3,393	3,422	3,422	3,422	3,422	17,081
Unsupported Borrowing						
21st Century Schools Band B	1,100	5,711	1,900	0	0	8,711
City Deal	1,313	675	675	972	972	4,607
Vehicles	305	1,102	1,372	264	0	3,043
Total General Fund	**6,111**	**10,910**	**7,369**	**4,658**	**4,394**	**33,442**
Housing Revenue Account						
Housing Revenue Account	17,359	16,807	13,334	12,552	10,514	70,566
Total New Borrowing	**23,470**	**27,717**	**20,703**	**17,210**	**14,908**	**104,008**

2.12 In addition, as part of the Initial Revenue Proposals 2020/21 the Council is projecting a reduction in its reserves, Capital grant balances and provisions of 13.4% or £8.756m.

2.13 Another factor influencing the Council's borrowing strategy is the high level of maturities on the Council's existing external debt over the coming years which have been calculated to be £33.795m between 2020/21 and 2024/25.

2.14 Taking these factors into account and the Council's requirement to hold approximately £30m in investment balances, the Council's additional external borrowing requirement will be £123m over the coming five years as set out in the table below. Balance Sheet projections for the period of the Strategy are set out in paragraphs 2.7 to 2.9 of this report.

Scheme	2020/21	2021/22	2022/23	2023/24	2024/25	Total
	£000	£000	£000	£000	£000	£000
New Borrowing	20,000	24,500	20,000	15,000	14,500	94,000
Replacement Borrowing	1,000	18,000	5,000	5,000	0	29,000
Total External Borrowing	21,000	42,500	25,000	20,000	14,500	123,000

2.15 The accuracy of these estimates will be impacted by the utilisation of reserves as planned and the delivery of the capital programme as profiled. There is a cost of carry associated with borrowing in advance of a borrowing requirement so the Treasury team will need to keep these factors under review as well as having regard to interest rate projections to minimise the financing costs of the proposed external borrowing. During 2019/20 the Public Works Loan Board (PWLB) increased its borrowing rates by 100bps which means that the Council will need to keep PWLB rates under review also. Whilst it is highly likely that any new borrowing will be carried out with the PWLB, shorter term financing and alternative providers will be considered.

Investment Strategy

2.16 As set out in the Council's Balance Sheet projections in paragraphs 2.7 to 2.9, the Council, following discussions with Link Asset Management Ltd. will seek to maintain a minimum £30m investment balance in addition to any working capital surplus during the period. The accuracy of these estimates will again be impacted by the use of reserves as planned and the delivery of the capital programme as profiled.

2.17 In 2020/21 the Council will place investments with the Debt Management Account Deposit Facility (DMADF) of the Bank of England or UK Treasury Bills which are guaranteed by the UK Government and with UK Local Authorities (including Police and Fire Authorities). The Council will continually review the financial stability of all local authorities with whom it places investments.

2.18 Although not guaranteed by the UK Government, if a Local Authority with whom the Council has placed an investment were to default on repayment, the Council would have recourse under the Local Government Act 2003 to collect any outstanding sums.

2.19 The Treasury Management section will in 2020/21 retain the maximum principal investment at £5m and normally will invest up to a period of 12 months with Local Authorities (including Fire and Police Authorities). Where appropriate the Council will consider opportunities to invest for a longer period not exceeding 3 years in consultation with our Treasury Management Advisers. Any change on this position will be brought to Cabinet as part of future Treasury Management monitoring reports.

2.20 The Council is in the process of engaging CCLA Investment Management Ltd and Federated UK to operate Money Market Funds on behalf of the Council. Both are domiciled in the UK. The contract documentation is in the process of being reviewed by the Council's Legal Department with the intention of being fully operational at the start of 2020/21.

2.21 The Council will continue to use credit ratings from the three main rating agencies Fitch Ratings Ltd, Moody's Investors Service and Standard & Poor's to assess the risk of loss of investments. The lowest available credit rating will be used to determine credit quality. In addition, regard will be given to other available information on the credit quality of banks and building societies.

Interim Report

2.22 In so far as the Council's Treasury Management operations entered into for the period 1st April to 31st December 2019 are concerned, all activities were in accordance with the Council's approved strategy on Treasury Management. The following table sets out the monies borrowed / repaid during the period.

Loan Type	**Opening Balance**	**Received**	**Repaid**	**Closing Balance**
	01/04/2019			**31/12/2019**
	£000	**£000**	**£000**	**£000**
PWLB	146,445	0	(239)	146,206
Other Long Term Loans	6,000	0	0	6,000
WG Concessionary Loans (2)	2,600	0	0	2,600
Temporary Loans	100	0	0	100
Total	**155,145**	**0**	**(239)**	**154,906**

2.23 Loans borrowed from the PWLB are intended to assist local authorities in meeting their longer-term borrowing requirements. The above loans are all at fixed rates of interest. The rate paid on each loan is largely dependent upon the original duration of the loan and date taken out. The average interest rate on all the Council's outstanding PWLB debt has moved over the period 1st April - 31st December 2019 from 4.7211% to 4.7210%.

2.24 Other long-term loans represent those non-PWLB loans that are repayable at least one year or more from the date they are advanced. The bulk of this debt is represented by two market loans of £2,000,000 and £4,000,000. The average interest rate on the Authority's outstanding market loans is 5.322%.

2.25 The Concessionary Loans were advanced to the Council by the Welsh Government. Loan 1 for £2m was advanced on the 1st April 2015 and will mature on the 31st March 2025 and Loan 2 for £0.5m was advanced on the 28th March 2019 and will mature on the 31st July 2020. Both are interest free.

2.26 Temporary loans represent loans that have no fixed maturity date. Current loans have been borrowed from The Vale of Glamorgan Welsh Church Act Fund. Interest is calculated on a monthly basis using the "Average 7 Day Rate".

2.27 The Council's investments for the period to 31st December 2019 are set out in the following table.

Investment Counterparty	**Opening Balance 01/04/2019 £000**	**Invested £000**	**Repaid £000**	**Closing Balance 31/12/2019 £000**
Local Authorities	81,000	251,650	(250,900)	81,750
Debt Management Account Deposit Facility	8,100	1,719,935	(1,721,535)	6,500
Treasury Bills	0	9,800	(9,800)	0
Total	**89,100**	**1,981,385**	**(1,982,235)**	**88,250**

2.28 Interest at an average rate of 0.74% and amounting to £525,987 has been received from maturing Local Authority and Debt Management Deposit Facility investments for the first 9 months of 2019/20. The average rate of return on Treasury Bills was 0.68% and amounted to £5,138 since the authority commenced utilising this investment tool in early November 2019.

Annual Minimum Revenue Provision Statement 2020/21

2.29 Capital expenditure when financed by long term debt incurs two elements of cost- interest on and repayment of the principal sum borrowed. The resource the Council must put aside in each year to repay the principal sum borrowed is known as the Minimum Revenue Provision (MRP). Pre 2008 there were detailed statutory rules for the calculation of MRP as laid down in the 2003 regulations but the introduction of the Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2008 which became effective from the 31st March 2008, replaced these statutory rules with: 'A local authority must calculate for the current financial year an amount of minimum revenue provision which it considers to be prudent'.

2.30 Welsh Government has issued guidance on what constitutes prudent provision, and this requires the Council to approve an annual statement of its policy on calculating MRP. The broad aim of the WG Guidance is to ensure that debt is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits.

2.31 The following statement incorporates options recommended in the Guidance.

2.32 For supported capital expenditure the Council will implement the "Asset Life Method". MRP will be determined by charging the expenditure over the expected useful life of the average asset lives (40 years) of the (Non HRA) Council Assets in equal instalments, starting in the year after the asset becomes operational.

2.33 For unsupported capital expenditure incurred after 31st March 2008, the Council will also implement the "Asset Life method". MRP will be determined by charging the expenditure over the expected useful life of the relevant asset in equal instalments, starting in the year after the asset becomes operational. Included in the 2020/21 revenue estimates are principal repayments totalling £390k in respect of prudential (unsupported) Borrowing (i.e. not supported for revenue purposes). Of this funding £64k is in respect of 21st Century Schools. The provision made in respect of these schemes is commensurate with asset life as estimated by the Council's external valuer. Provision of £171k has been made for the repayments against a loan of £1,200,000 for refuse vehicles over an expected life of 7 years and £155k in respect of loans raised for City Deal (20 years).

2.34 In addition, £417k has been included in respect of the Local Government Borrowing Initiative (LGBI) funding from WG for 21st Century Schools, the Local Road Network Improvement scheme and Affordable Housing. The provision in respect of LGBI schemes is commensurate with the applicable WG funding streams through the Revenue Support Grant. Loans have been raised on an annuity basis so MRP contributions vary annually.

2.35 MRP will be charged at 2% of the outstanding Housing Revenue Account (HRA) Capital Financing Requirement in respect of housing assets.

2.36 For debt incurred after 2021/22 the HRA is required to move to either an Asset Life method or depreciation method for calculating the Minimum Revenue Provision and the Treasury Management Strategy will be updated to reflect this requirement in future years.

2.37 Capital expenditure incurred during 2020/21 will not be subject to an MRP charge until 2021/22.

2.38 The estimates included in the MRP calculation will need to be revised during 2020/21 to include the estimates of MRP charged against the Council's lease liability as required by IFRS16.

2.39 Based on the Council's latest estimate of its Capital Financing Requirement on 31st March 2019, the budget for MRP has been set as follows:

	31.03.2020 Estimated CFR £000	2020/21 Estimated MRP £000
General Fund		
Supported capital expenditure	105,576	2,833
Unsupported capital expenditure	13,893	745
Total General Fund	**119,469**	**3,578**
Housing Revenue Account	78,970	1,591
Total Housing Revenue Account	**78,970**	**1,591**
Total	**198,439**	**5,169**

2.40 The Section 151 Officer considers that the estimated costs of unsupported borrowing are both prudent and sustainable.

Treasury Management Policy

2.41 Whilst considerations, such as interest rate forecasts, will inevitably inform the Treasury Management Strategy to be adopted over the coming years, account must also be taken of certain fundamental parameters that the Council must work within. These may include political, environmental, social, technical, economic and legislative factors and form the basis of the Treasury Management Policy that underpins the Strategy. Adherence to its requirements is mandatory for all matters relating to Treasury Management and investments and the Policy for 2020/21 is attached at Appendix 2.

3. How do proposals evidence the Five Ways of Working and contribute to our Well-being Objectives?

3.1 The Treasury Management and Investment Strategy ensures that the financial plans of the Council are sustainable into the future and do not adversely impact on future generations.

3.2 The Treasury Management and Investment Strategy underpins the financial management of the Council and its ability to achieve its Well Being objectives as set out in the Corporate Plan.

4. Resources and Legal Considerations

Financial

4.1 Money is borrowed for capital purposes and interest is charged to revenue accounts.

Employment

4.2 There are no direct employment issues relating to this report.

Legal (Including Equalities)

4.3 Compliance with the Local Government Act 2003 and CIPFA's "Code of Practice for Treasury Management in the Public Services" is mandatory.

5. Background Papers

CIPFA's "Code of Practice for Treasury Management in the Public Services" (2017 Edition), "The Prudential Code" (2017 Edition) and WG guidance on local authority investments
Committee papers for Audit Committee 31st January 2018 - Proposal to Amend the Minimum Revenue Proposals 2018-19 Policy.

Appendix 1

Treasury Management and Investment Strategy 2020/21

Introduction

The Treasury Management Strategy sets out the Council's plan for treasury management for the period 2020/21 to 2022/23. The plan forms an integral part of the Council's strategic planning process, linking in with the Medium Term Financial Plan, Capital Strategy and annual budget cycle.

This Treasury Management Strategy has been prepared taking into account the following:

- CIPFA Code of Practice on Treasury Management 2017
- CIPFA Prudential Code 2017
- CIPFA Treasury Management in the Public Services Guidance Notes 2018
- CIPFA Statement (17/10/18) on borrowing in advance of need and investment in commercial properties
- Local Government Act 2003
- Welsh Government Guidance on Investments
- Welsh Government Minimum Revenue Provision Guidance

Prudential Code

The key objectives of the Prudential Code are to ensure within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable and that treasury management decisions are taken in accordance with good professional practice and in full understanding of the risks involved and how the risks will be managed to levels that are acceptable to the organisation.

To demonstrate the Council has fulfilled these objectives, the Code sets out prudential indicators that should be used and the factors that must be taken into account.

The prudential indicators required by the Prudential Code are designed to support and record local decision making in a manner that is publicly accountable.

Welsh Government Investment Guidance

The Welsh Government Investment guidance notes lay down the requirements with regard to the need to set out the Council's policies for the prudential management of its investments giving regard to firstly security and secondly liquidity. It covers the definition of specified and non-specified investments and the approach to investment risk.

The Council has a legal obligation under the Local Government Act 2003 to have regard to the Prudential Code and the Welsh Government guidance.

In line with the Welsh Government Guidance this document has been prepared as a single strategy document covering both the requirements of the CIPFA Treasury Management Code and the Welsh Government's guidance.

The Strategy

The Strategy for 2020/21 covers two main areas:

Capital Issues

- Capital expenditure plans and the associated prudential indicators
- Minimum revenue provision (MRP) policy

Treasury Management Issues

* Economic background
* Prospects for interest rates
* Borrowing Strategy (including Current Treasury Position)
* Treasury indicators which limit the treasury risk and activities of the Council
* Policy on borrowing in advance of need
* Debt rescheduling
* Management of Housing Revenue Account (HRA) Debt
* Investment Strategy
* Creditworthiness policy
* Other investment tools
* External service providers

Capital Expenditure Plans and the Associated Prudential Indicators

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

Capital Expenditure – Prudential Indicator No. 1

The figures shown in the following table are a summary of the Council's capital expenditure plans, both those agreed previously and those forming part of this budget cycle.

Capital Expenditure	**2018/19**	**2019/20**	**2020/21**	**2021/22**	**2022/23**
	Actual £000	**Estimate £000**	**Estimate £000**	**Estimate £000**	**Estimate £000**
Learning & Skills	7,346	21,561	71,022	44,401	8,878
Social Services	662	1,421	100	1,439	100
City Deal	1,043	0	1,313	675	675
Environment & Transport	7,107	20,951	9,608	3,482	3,282
Resources & Managing Director	15,780	12,405	4,785	1,980	3,764
Non HRA total	**31,938**	**56,338**	**86,828**	**51,977**	**16,699**
HRA	11,444	19,219	27,047	24,780	21,756
Total	**43,382**	**75,557**	**113,875**	**76,757**	**38,455**

The estimates reflect the Draft Housing Business Plan Proposals and figures also reflect the Draft Final Capital Proposals.

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a need to increase borrowing.

	2018/2019	2019/2020	2020/2021	2021/2022	2022/23
	Actual	**Estimate**	**Estimate**	**Estimate**	**Estimate**
	£000	**£000**	**£000**	**£000**	**£000**
Capital Expenditure	43,382	75,557	113,875	76,757	38,455
Less Capital Grants and Contributions	24,196	45,967	68,309	29,807	9,727
Less Reserves & Revenue	10,429	15,732	18,380	11,413	7,509
Less Capital Receipts and Appropriation	3,355	8,674	3,717	7,820	516
Capital Expenditure Funded from Borrowing	**5,402**	**5,184**	**23,469**	**27,717**	**20,703**
Less MRP	4,992	5,116	5,169	5,713	6,416
Net Financing Need For Year CFR	**410**	**68**	**18,300**	**22,004**	**14,287**

The Council's Borrowing Need - Capital Financing Requirement (CFR) – Prudential Indicator No. 2

The Capital Finance Requirement (CFR) is the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so it's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each asset's life and so charges the economic consumption of capital assets as they are used.

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

The Council's CFR projections are listed below:

	2018/19	2019/20	2020/21	2021/22	2022/23
	Actual	**Estimate**	**Estimate**	**Estimate**	**Estimate**
	£000	**£000**	**£000**	**£000**	**£000**
Non HRA CFR	124,147	119,469	122,002	129,108	132,271
HRA CFR	74,224	78,970	94,737	109,635	120,759
Total CFR	**198,371**	**198,439**	**216,739**	**238,743**	**253,030**

In-Year Movement CFR	2018/19 Actual £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000	2022/23 Estimate £000
Non HRA	990	(4,678)	2,533	7,106	3,163
HRA	(580)	4,746	15,767	14,898	11,124
Total	**410**	**68**	**18,300**	**22,004**	**14,287**

Core Funds and Expected Investment Balances

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.).

Minimum Revenue Provision (MRP)

The Council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the Minimum Revenue Provision - MRP), although it is also allowed to undertake additional voluntary payments if required (Voluntary Revenue Provision - VRP).

Welsh Government regulations have been issued which require the full Council to approve a MRP Statement in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The Council's MRP Statement is set out below.

MRP Statement

For supported capital expenditure the Council will implement the "Asset Life Method". MRP will be determined by charging the expenditure over the expected useful life of the average asset lives (40 years) of the (Non HRA) Council Assets in equal instalments, starting in the year after the asset becomes operational.

For unsupported capital expenditure incurred after 31st March 2008, the Council will also implement the "Asset Life method". MRP will be determined by charging the expenditure over the expected useful life of the relevant asset in equal instalments, starting in the year after the asset becomes operational.

Included in the 2020/21 revenue estimates are principal repayments totalling £390k in respect of prudential (unsupported) Borrowing (i.e. not supported for revenue purposes). Of this funding £64k is in respect 21st Century Schools. The MRP provision made in respect of these schemes is commensurate with their asset life as estimated by the Authority's external valuer. Provision of £171k has been made for the repayments against a loan of £1.2m for refuse vehicles over an expected life of 7 years and £155k in respect of loans raised for City Deal over 20 years.

In addition £417k has been included in respect of the Local Government Borrowing Initiative (LGBI) funding from Welsh Government (WG) for 21st Century Schools, Local Road Network Improvement scheme and Affordable Housing. The provision in respect of LGBI schemes is commensurate with the applicable WG funding streams through the Revenue Support Grant (RSG). Loans have been raised on an annuity basis so MRP contributions vary annually.

MRP will be charged at 2% of the outstanding Housing Revenue Account Capital Financing Requirement in respect of housing assets with the exception of Affordable Housing, referred to above.

For debt incurred after 2021/22 the HRA is required to move to either an Asset Life method or depreciation method for calculating the Minimum Revenue Provision and the Treasury Management Strategy will be updated to reflect this requirement in future years.

Capital expenditure incurred during 2020/21 will not be subject to a MRP charge until 2021/22.

Based on the Authority's latest estimate of its Capital Financing Requirement on 31st March 2020, the budget for MRP has been set as follows:

	31.03.2020 Estimated CFR £000	2020/21 Estimated MRP £000	2021/22 Estimated MRP £000	2022/23 Estimated MRP £000
General Fund				
Supported Capital Expenditure	105,576	2,833	2,916	3,000
Unsupported Capital Expenditure	13,893	745	888	1,206
Total General Fund	**119,469**	**3,578**	**3,804**	**4,206**
Housing Revenue Account	78,970	1,591	1,909	2,210
Total Housing Revenue Account	**78,970**	**1,591**	**1,909**	**2,210**
Total	**198,439**	**5,169**	**5,713**	**6,416**

These projections will need to be revised during the 2020/21 financial year to include the principal element of leasing payments made as a requirement of IFRS 16. More detail is set out later in this strategy.

Economic Background

UK

- The General election on the 12th December 2019 returned a large Conservative majority on a platform of getting Brexit done and the UK is now set to leave the European Union (EU) by 31st January 2020. However there is still considerable uncertainty about whether the UK and EU will be able to agree the details of a trade deal by the deadline set by the Prime Minister of December 2020. This leaves open the potential risks of a no deal or a hard Brexit.

- Gross Domestic Product (GDP) growth has been weak in 2019 and is likely to be around only 1% in 2020.

- The November and December Monetary Policy Committee (MPC) meetings were concerned about weak UK growth caused by the dampening effect of Brexit uncertainties and by weak global economic growth, consequently there has been no change to the Bank Rate in 2019.

- Consumer Price Index (CPI) inflation has been hovering around the Bank of England’s target of 2% during 2019, but fell in both October and November to a three-year low of 1.5%. It is likely to remain close to, or under 2% over the next two years and so inflation does not pose any immediate concern to the MPC.

- Employment growth has been quite resilient through 2019 until the three months to September where it fell by 58,000. However, there was an encouraging pick up again in the three months to October to growth of 24,000, which showed that the labour market was not about to head into a major downturn. The unemployment rate held steady at a 44-year low of 3.8%.

- Wage inflation has been steadily falling from a high point of 3.9% in July to 3.5% in October (3-month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates higher than CPI inflation), earnings grew by about 2.0%. As the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months.

USA

- Economic growth in 2019 has been falling after a strong start in quarter 1 at 3.1%, (annualised rate), to 2.0% in quarter 2 and then 2.1% in quarter 3. Fears of a recession in 2020 have largely dissipated but growth is likely to remain relatively weak.

- Strong growth in employment numbers experienced during 2018 has weakened during 2019, indicating that the economy had been cooling, while inflationary pressures have also been weakening

- The Federal Bank (FED) finished its series of increases in rates to 2.25 – 2.50% in December 2018. Since then it has cut rates by 0.25% in July, September and October to end at 1.50 – 1.75%. In August it also ended its programme of quantitative tightening, (selling its holdings of treasuries etc. @ $50bn per month during 2019). At its September meeting it said it was going to start buying Treasuries again, although this was not to be seen as a resumption of quantitative easing but rather an exercise to relieve liquidity pressures in the repo market.

- The trade war with China is depressing US, Chinese and world growth. In the EU, it is also particularly impacting Germany as exports of goods and services are equivalent to 46% of total GDP. However, progress has been made in December on agreeing a phase one deal between the US and China to roll back some of the tariffs; this gives some hope of resolving this dispute.

Eurozone

- Economic growth has been slowing from +1.8 % in 2018 to around half of that at the end of 2019. There appears to be little upside potential in the near future.

- The European Central Bank (ECB) ended its programme of quantitative easing purchases of debt in December 2018, which then meant that the central banks in the US, UK and EU had all ended the phase of post financial crisis expansion of liquidity supporting world financial markets by quantitative easing purchases of debt.

- However, with the downturn in EZ and world growth gathering momentum the ECB at its meeting on 12 September cut its deposit rate further into negative territory, from -0.4% to -0.5%, and announced a resumption of quantitative easing purchases of debt for an unlimited period**.** These purchases would start in November at €20bn per month - a relatively small amount compared to the previous buying programme.

- It is doubtful whether the various monetary policy easing measures in 2019 will have much impact on growth and, unsurprisingly, the ECB has stated that governments would need to help stimulate growth by **‘**growth friendly’ fiscal policy.

World Growth – Reversal of Globalisation

- Until recent years, world growth has been boosted by increasing globalisation i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has depressed inflation. However, the rise of China as an economic superpower over the last thirty years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy. The Chinese government has targeted achieving major world positions in specific key sectors and products, especially high tech areas and production of rare earth minerals used in high tech products. It is achieving this by massive financial support, (i.e. subsidies), to state owned firms, government directions to other firms, restrictions on market access by foreign firms and informal targets for the domestic market share of Chinese producers in the selected sectors. This is regarded as being unfair competition that is putting western firms at an unfair disadvantage or even putting some out of business. It is also regarded with suspicion on the political front as China is an authoritarian country that is not averse to using economic and military power for political advantage. The current trade war between the US and China therefore needs to be seen against that backdrop. It is, therefore, likely that we are heading into a period where there will be a reversal of world globalisation and a decoupling of western countries from dependence on China to supply products. This is likely to produce a backdrop in the coming years of weak global growth and so weak inflation.

- This weak global growth outlook for 2020 and beyond therefore means that central banks are likely to come under more pressure to support growth by looser monetary policy measures. This will mitigate against central banks increasing interest rates and reversing the distortions in financial markets caused by a decade of ultra-low interest rates.

- The trade war between the US and China has been a major concern to financial markets due to the synchronised general weakening of growth in the major economies of the world, compounded by fears that there could even be a recession looming up in the US, though such fears have largely dissipated towards the end of 2019.

- These concerns resulted in government bond yields falling sharply in 2019 in the developed world. If there were a major worldwide downturn in growth, central banks in most of the major economies will have limited ammunition available, in terms of monetary policy measures, when rates are already very low in most countries, apart from the US. There are also concerns about how much distortion of financial markets has already occurred with the current levels of quantitative easing purchases of debt by central banks and the use of negative central bank rates in some countries. The latest PMI (Purchasing Managers Index) survey statistics of economic health for the US, UK, EU and China have all been predicting a downturn in growth, This confirms investor sentiment that the outlook for growth during the year ahead is weak.

Prospects for Interest Rates

The Council has appointed Link Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives their central view.

Link Asset Services Interest Rate View														
	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25	1.25	1.25	1.25
3 Month LIBID	0.70	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.30	1.30
6 Month LIBID	0.80	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40	1.50	1.50	1.50	1.50
12 Month LIBID	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60	1.70	1.70	1.70	1.70
5yr PWLB Rate	2.30	2.40	2.40	2.50	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.10	3.20	3.20
10yr PWLB Rate	2.60	2.70	2.70	2.70	2.80	2.90	3.00	3.10	3.20	3.20	3.30	3.30	3.40	3.50
25yr PWLB Rate	3.20	3.30	3.40	3.40	3.50	3.60	3.70	3.70	3.80	3.90	4.00	4.00	4.10	4.10
50yr PWLB Rate	3.10	3.20	3.30	3.30	3.40	3.50	3.60	3.60	3.70	3.80	3.90	3.90	4.00	4.00

These interest rate forecasts provided by Link Asset Services are predicated on an assumption of an agreement being reached on Brexit between the UK and the EU. On this basis, while GDP growth is likely to be subdued in 2019 and 2020 due to all the uncertainties around Brexit depressing consumer and business confidence, an agreement on the detailed terms of a trade deal is likely to lead to a boost to the rate of growth in subsequent years. This could, in turn, increase inflationary pressures in the economy and so cause the Bank of England to resume a series of gentle increases in Bank Rate. Just how fast, and how far, those increases will occur and rise to, will be data dependent. The forecasts in this report assume a modest recovery in the rate and timing of stronger growth and in the corresponding response by the Bank in raising rates.

- In the event of an orderly non-agreement exit in December 2020, it is likely that the Bank of England would take action to cut Bank Rate from 0.75% in order to help economic growth deal with the adverse effects of this situation. This is also likely to cause short to medium term gilt yields to fall.
- If there were a disorderly Brexit, then any cut in Bank Rate would be likely to last for a longer period and also depress short and medium gilt yields correspondingly. Quantitative easing could also be restarted by the Bank of England. It is also possible that the government could act to protect economic growth by implementing fiscal stimulus.

The balance of risks to the UK

- The overall balance of risks to economic growth in the UK is probably even, but dependent on a successful outcome of negotiations on a trade deal.
- The balance of risks to increases in Bank Rate and shorter term PWLB rates are broadly similarly to the downside.
- In the event that a Brexit deal was agreed with the EU and approved by Parliament, the balance of risks to economic growth and to increases in Bank Rate is likely to change to the upside.

Investment and Borrowing Rates

- Investment returns are likely to remain low during 2020/21 with little increase in the following two years. However, if major progress was made with an agreed withdrawal of the United Kingdom from the European Union, then there is upside potential for returns on investments.

- The Public Works Loan Board (PWLB) interest rates were on a major falling trend during the first half of 2019-20 but then jumped up by 100 bps on 9th October 2019. This increase has resulted in the return on investments and borrowing rates on debt materially widening. This coupled with the long term Bank Rate not expected to rise above 2.5**%** has endorsed the Authority's current policy of avoiding new borrowing by running down spare cash balances. However this approach will be carefully reviewed to avoid higher borrowing costs in future years when the Council may not be able to avoid external borrowing at higher interest rates. The Council will need to consider the effect on revenue and credit risk if it opts to borrow externally in 2020/21.

Borrowing

The capital expenditure plans previously detailed, highlight the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's Capital Strategy. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The Strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the Annual Investment Strategy.

Balance Sheet Projections

To assist the Treasury team in arriving at their Borrowing and Investment strategies for 2020/21 balance sheet projections have been prepared. These projections reflect the Final Capital Proposals 2020/21 to 2024/25. The projections also take into account the advice of our Treasury Management Advisers that interest rates are expected to remain low as are investment returns during the period and therefore seeks to maximise the use of reserves and spare cash balances to finance capital expenditure.

As well as monitoring the use of internal borrowing these projections consider the levels of funds available for investment and the levels of External Borrowing required in future years.

	2020/21	**2021/22**	**2022/23**	**2023/24**	**2024/25**
	£000	**£000**	**£000**	**£000**	**£000**
Capital Financing Requirement	216,739	238,743	253,030	263,248	270,792
Less External Borrowing	174,122	208,212	225,509	235,670	243,115
Internal Borrowing	**42,617**	**30,531**	**27,521**	**27,578**	**27,677**
Internal borrowing as a % of Capital Financing Requirement	**20%**	**13%**	**11%**	**10%**	**10%**
Reserve/Capital Grant Balances/Provisions	65,295	58,568	56,539	56,539	56,539
Capital Receipts	9,870	2,050	1,273	1,273	1,273
Total Cash Backed Reserves and Provisions	**75,165**	**60,618**	**57,812**	**57,812**	**57,812**
Less External Investments Target	30,000	30,000	30,000	30,000	30,000
Balance Available for Internal Borrowing	**45,165**	**30,618**	**27,812**	**27,812**	**27,812**
Working Capital Surplus	15,617	15,617	15,617	15,617	15,617
Projected External Investments	32,548	30,087	30,291	30,234	30,135
Total Projected Investments Balance	**48,165**	**45,704**	**45,908**	**45,851**	**45,752**

Borrowing Strategy

The Council’s borrowing strategy in recent years has been to maintain an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), 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 policy has been based on the high levels of reserves held by the Council. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

The Council's Final Capital Proposals 2020/21 to 2024/25 forecast borrowing (supported and unsupported borrowing) in the period as set out in the table below. The Council is also projecting to use £12.314m of Capital receipts between 2020/21 and 2024/25.

Scheme	2020/21	2021/22	2022/23	2023/24	2024/25	Total
	£000	**£000**	**£000**	**£000**	**£000**	**£000**
General Fund						
General Capital Funding Supported Borrowing	3,393	3,422	3,422	3,422	3,422	17,081
Unsupported Borrowing						
21st Century Schools Band B	1,100	5,711	1,900	0	0	8,711
City Deal	1,313	675	675	972	972	4,607
Vehicles	305	1,102	1,372	264	0	3,043
Total General Fund	**6,111**	**10,910**	**7,369**	**4,658**	**4,394**	**33,442**
Housing Revenue Account						
Housing Revenue Account	17,359	16,807	13,334	12,552	10,514	70,566
Total Capital Programme Borrowing	**23,470**	**27,717**	**20,703**	**17,210**	**14,908**	**104,008**

In addition, as part of the Initial Revenue Proposals 2020/21 the Council is projecting a reduction in its reserves, capital grant balances and provisions of 13.4% or £8.756m.

Another factor influencing the Council's borrowing strategy is the high level of maturities on the Council's existing external debt over the coming years which have been calculated to be £33.795m between 2020/21 and 2024/25.

Taking these factors into account and the Council's requirement to hold approximately £30m in investment balances the Council's additional external borrowing requirement £123m as set out in the borrowing requirement table below.

Borrowing Requirement

The Borrowing Requirement represents the estimated amount that the Council will borrow externally for this year and the next 3 years. The figures shown below exclude maturities which reduce the overall borrowing of the Council.

	2020/21	2021/22	2022/23	2023/24	2024/25	Total
	£000	**£000**	**£000**	**£000**	**£000**	**£000**
New Borrowing	20,000	24,500	20,000	15,000	14,500	94,000
Replacement Borrowing	1,000	18,000	5,000	5,000	0	29,000
Total External Borrowing	21,000	42,500	25,000	20,000	14,500	123,000

The accuracy of these estimates will be impacted by the utilisation of reserves as planned and the delivery of the capital programme as profiled. There is a cost of carry associated with borrowing in advance of a borrowing requirement so the Treasury team will need to keep these factors under review as well as having regard to interest rate projections to minimise the financing costs of the proposed external borrowing. As noted earlier in the Strategy, during 2019/20 the PWLB increased its borrowing rates by 100bps which means that the Council will also need to keep PWLB rates under review. Whilst it is highly likely that any new borrowing will be carried out with the PWLB, shorter term financing and alternative providers will be considered.

Against this background and the risks within the economic forecast, caution will be adopted with the 2020/21 treasury operations. The Head of Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- If it is felt that there is a significant risk of a sharp FALL in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- If it is felt that there is a significant risk of a much sharper RISE in long and short term rates than that currently forecast, perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

Any decisions in respect of new external borrowing will be reported to the Cabinet.

Investment Strategy

As set out in the Council's Balance Sheet projections, the Council, following discussions with Link Asset Management Ltd. will seek to maintain a minimum £30m investment balance in addition to any working capital surplus during the period. The accuracy of these estimates will again be impacted by the use of reserves as planned and the delivery of the capital programme as profiled.

In 2020/21 the Council will place investments with the Debt Management Account Deposit Facility (DMADF) of the Bank of England or UK Treasury Bills which are guaranteed by the UK Government and with UK Local Authorities (including Police and Fire Authorities). The Council will continually review the financial stability of all local authorities with whom it places investments.

Although not guaranteed by the UK Government if a Local Authority with whom the Council has placed an investment were to default on repayment, the Council would have recourse under the Local Government Act 2003 to collect any outstanding sums.

The Treasury Management section will in 2020/21 retain the maximum principal investment at £5m and the maximum period of investment to 12 months with Local Authorities. Any change on this position will be brought to Cabinet as part of future Treasury Management monitoring reports.

The Council is in the process of engaging CCLA Investment Management Ltd and Federated UK to operate Money Market Funds on behalf of the Council. Both are domiciled in the UK. The contract documentation is in the process of being reviewed by the Council's Legal Department with the intention of them being fully operational at the start of 2020/21.

The Council will continue to use credit ratings from the three main rating agencies Fitch Ratings Ltd, Moody's Investors Service and Standard & Poor's to assess the risk of loss of investments. The lowest available credit rating will be used to determine credit quality. In addition, regard will be given to other available information on the credit quality of banks and building societies.

Current Portfolio Position

The overall treasury management portfolios as at 31 March and 31st December 2019 are shown below for both borrowing and investments.

Treasury Portfolio	**31.03.19**	**31.03.19**	**31.12.19**	**31.12.19**
	£000	**% Return**	**£000**	**% Return**
Treasury Investments				
Local Authorities	81,000	0.67	81,750	0.78
Debt Management Account Deposit Facility	8,100	0.38	6,500	0.50
Total Investments	**89,100**		**88,250**	
Borrowing				
Public Works Loan Board	146,445	4.72	146,206	4.72
LOBOS	6,000	5.32	6,000	5.32
Concessionary Loans	2,600	0.00	2,600	0.00
Temporary Loans	100	0.51	100	0.65
Total External Borrowing	**155,145**		**154,906**	
Net Borrowing	**66,045**		**66,656**	

Gross Debt and the Capital Financing Requirement - Prudential Indicator No. 3

The Council's forward projections for borrowing are summarised below. The table shows the actual external debt, against the underlying capital borrowing need, (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

External Debt	**2018/19**	**2019/20**	**2020/21**	**2021/22**	**2022/23**
	Actual £000	**Estimate £000**	**Estimate £000**	**Estimate £000**	**Estimate £000**
External Debt as at 1st April	155,365	155,145	153,910	174,122	208,212
Expected Change In Debt (Net of maturities)	(220)	(1,235)	20,212	34,090	17,297
Other Long Term Liabilities	0	0	0	0	0
Expected Change In Other Long Term Liabilities	0	0	0	0	0
Gross Debt 31st March	**155,145**	**153,910**	**174,122**	**208,212**	**225,509**
The Capital Financing Requirement	198,371	198,439	216,739	238,743	253,030
Internal Borrowing	**43,226**	**44,529**	**42,617**	**30,531**	**27,521**

Other long term liabilities need to be updated during 2020/21 to reflect the Council's lease liabilities in accordance with IFRS 16.

Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2020/21 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue or speculative purposes.

The Head of Finance reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account the final proposals for capital and revenue.

Approved Methods of Raising Capital Finance

The Local Government Act 2003 provides that a local authority may borrow money for any purpose relevant to its functions under any enactment or for the purposes of the prudent management of its financial affairs. The Council will continue to borrow from the following sources: -

- by overdraft or short term from Financial Services Authority authorised banks;
- from the Public Works Loan Board (PWLB);
- by means of loan instruments;
- other local authorities;
- from the Municipal Bond Agency
- stock issues;
- short – term borrowing from any source;
- other credit arrangements; and
- Local Capital Finance Company and other special purpose companies created to enable local authority bond issues.

LOBO (Lender Option Borrower's Option)

The Council holds £6M of LOBO (Lender Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan. The Council will take the option to repay LOBO loans at no cost if it has the opportunity to do so. Total borrowing via LOBO loans will be limited to £6M and will reduce to £4m in 2021/22

Municipal Borrowing Agency

It is possible that the Municipal Bond Agency will be offering loans to local authorities in the future. The Agency hopes that the borrowing rates will be lower than those offered by the Public Works Loan Board (PWLB). This Council may make use of this new source of borrowing as and when appropriate. Any intention to borrow will be authorised by the Section 151 Officer and reported to Cabinet for approval prior to any action being taken.

Treasury Indicators: Limits to Borrowing Activity

The Operational Boundary – Prudential Indicator No. 4

This is the proposed limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources. The proposed Operational Boundary for external debt is based upon estimates of the most likely, prudent, but not worst case scenario. The Operational Boundary links to the Council's plans for capital expenditure, estimates of capital financing requirement and the estimate of cash flow requirements for the year. This is the expected maximum limit for external debt. It is lower than the Authorised Limit and cash flow variations may lead to the occasional breach of the Operational Boundary.

Operational Boundary	**2019/20**	**2020/21**	**2021/22**	**2022/23**
	Estimate	**Estimate**	**Estimate**	**Estimate**
	£000	**£000**	**£000**	**£000**
Debt	203,608	221,461	246,087	264,667
Other Long Term Liabilities	0	0	0	0
Total	**203,608**	**221,461**	**246,087**	**264,667**

The Authorised Limit for External Debt – Prudential Indicator No. 5

This is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited. 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. The Authorised Limit is the affordable borrowing limit determined in compliance with section 3 (1) of the Local Government Act 2003. It is not a limit that the Council will expect to borrow up to on a regular basis and provides headroom over and above the Operational Boundary.

These authorised limits set out below are considered to be consistent with the Council's current commitments and proposals for capital expenditure and financing and with its Treasury Management Policy. The estimates are based on most likely, (i.e. prudent but not worst case), scenario for external debt with sufficient headroom over and above this to allow for operational management (e.g. unusual cash movement).

Authorised Limit	**2019/20**	**2020/21**	**2021/22**	**2022/23**
	Estimate	**Estimate**	**Estimate**	**Estimate**
	£000	£000	£000	£000
Debt	210,541	228,394	255,520	271,600
Other Long Term Liabilities	0	0	0	0
Total	**210,541**	**228,394**	**255,520**	**271,600**

Affordability Prudential Indicators

The objective of the affordability indicator is to assess the affordability of the Council's investment plans by considering the impact on the council tax and for the HRA, the level of rent to be charged. To achieve this, the Council has to consider all of the resources available to it, together with the totality of its capital plans, revenue income and revenue expenditure forecast for the coming year and the following two years. These should be rolling scenarios and not fixed for three years.

The indicators in this category which are required to be approved by Council are set out below:

Ratio of Relevant Financing Costs to Net Revenue Stream – Prudential Indicator No. 6

This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of any investment income.

	2018/19	**2019/20**	**2020/21**	**2021/22**	**2022/23**
	Actual	**Estimate**	**Estimate**	**Estimate**	**Estimate**
	%	%	%	%	%
HRA (Rents)	22.91	22.68	24.81	28.54	31.10
Non HRA (Council tax)	3.45	3.42	3.28	3.41	3.74

The analysis above shows the Council Fund implications remain relatively stable throughout the period. The HRA cost is increasing over the period in line with the aspirations for maintenance and regeneration set out in the draft Housing Business Plan. The plan demonstrates that this level of investment is affordable over the 30 year period of the plan.

Upper Limits on Fixed Interest Rate and Variable Interest Rate Exposure – Prudential Indicator No. 7

Fixed Interest Rate Exposure	**2019/20 Probable Outturn £000**	**2020/21 Estimate £000**	**2021/22 Estimate £000**	**2022/23 Estimate £000**
Net Principal Fixed Rate Borrowing	147,810	168,021	204,111	221,408

This is a control over a Council having large concentrations of fixed rate debt needing to be replaced at the same time when interest rates may be relatively high. The upper limit for variable rate exposure measures the extent to which the Council is exposed to the effects of changes in interest rates.

In addition to the fixed rate borrowing shown above, the Council will have £6.1M variable rate borrowing which is projected to reduce to £4.1M from 2021/22.

Variable Interest Rate Exposure	**2019/20 Probable outturn £000**	**2020/21 Estimate £000**	**2021/22 Estimate £000**	**2022/23 Estimate £000**
Net Principal Upper Limit Variable Rate	0	0	0	0

Currently the Council's variable rate exposure is on net investments rather than as a result of borrowing at variable rates. By setting the upper limit as £0 this means the Council will not have more variable rate debt than variable rate investment.

Upper Limit for Principal Sums Invested for Longer Than 364 Days - Prudential Indicator No. 8

	2019/20 Probable Outturn £000	2020/21 Estimate £000	2021/22 Estimate £000	2022/23 Estimate £000
Upper limit principal sums invested for over 364 days (per maturity date)	0	10,000	10,000	10,000

Fixed Rate Borrowing Maturity Limit For External Debt - Prudential Indicator No. 9

Amount of Projected Borrowing that is Fixed Rate Maturing in Each Period as a Percentage of Total Projected Borrowing that is Fixed Rate for 2020/21	Upper Limit	Lower Limit
Under 12 months	20%	0%
12 months and within 24 months	20%	0%
24 months and within 5 years	30%	0%
5 years and within 10 years	40%	0%
10 years and above	100%	0%

The Authority's Maturity Profile of its Internal Borrowing

Set out below is a maturity profile of the Council's projected Internal Borrowing at the 31st March 2021, taking into account the balance sheet projections it is likely that a proportion of this internal borrowing will need to be refinanced by external borrowing during the period covered by this Strategy.

Amount of Internal Borrowing Maturing in Each Period as a Percentage of Total Projected Internal Borrowing for 2020/21	Amount	Percentage
	£000	
Under 12 months	1,115	2.53%
12 months and within 24 months	1,224	2.78%
24 months and within 5 years	3,500	7.94%
5 years and within 10 years	5,175	11.74%
10 years and above	31,603	75.01%
Total	42,617	

Policy on Borrowing in Advance of Need

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

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

Having considered the advice of the Council's treasury advisors, the Council will not be seeking to borrow sums in advance of need unless it is considered to be of significant economic benefit by the Section 151 Officer.

The maximum period between borrowing and expenditure is expected to be two years, although the Council does not link particular loans with particular items of expenditure.

Debt Rescheduling/Repayment

The Public Works Loan Board allows authorities to prematurely repay loans. As short-term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long-term debt to short-term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

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
- Enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as in the current climate short term rates on investments are likely to be lower than rates paid on current debt.

All rescheduling will be approved by the Section 151 Officer under delegated powers as set out in the Council's Constitution (Officer Delegations) and reported to Cabinet as part of the agreed monitoring procedure at the earliest meeting following its action.

Management of Housing Revenue Account Debt

On 2nd April 2015 as part of the agreed Housing Subsidy (HRAS) Buyout process a Public Works Loan Board loan of £63.186 million was drawn down and subsequently paid over to WG on behalf of HM Treasury.

Removal of HRA Borrowing Cap

On 29th October 2018 the Welsh Government confirmed that the Housing Revenue Account (HRA) was abolished with immediate effect therefore the “Final Limit of Indebtedness” cap of £103.723m reported in previous strategies has been removed.

As a result, Local Authorities with an HRA are no longer constrained by government controls over borrowing for house building and are able to borrow against their expected rental income, in line with the Prudential Code.

Policy on Apportioning Interest to the HRA

As part of the HRAS Buyout process the Council has reviewed its arrangements for dealing with the pooling of debt. The current approach is that the Council will continue to use a single pool for administering its debt. It is intended that interest will continue to be charged to the HRA using a consolidated rate.

Annual Investment Strategy

The strategy of the Council will have regard to the availability of capital receipts and financial reserves. The Investment Strategy is determined in parallel with Borrowing Strategy.

Management of Risk

The Council has borrowed and invested significant sums of money and is therefore exposed to financial risks such as the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council’s Treasury Management Strategy.

The Council’s investment priorities will be security first, portfolio liquidity second and then yield (return).

The Council’s Investment Policy has regard to the following: -

- The Welsh Government’s Guidance on Local Government Investments (“the Guidance”) issued in April 2010 (Revised from April 2020)

- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 (“the CIPFA Treasury Management Code”);

- The Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 Statutory Instrument 3239 (W 319) (as amended); and

- CIPFA Treasury Management Guidance Notes 2018.

- Welsh Government Minimum Revenue Provision (MRP) Guidance 2019

The Welsh Government Guidance and the CIPFA Code of Practice place a high priority on the management of risk. This Council has adopted a prudent approach to managing risk and defines its risk appetite by the following means:

Creditworthiness

Credit Rating Criteria

The Council uses credit ratings (long and short term) from the three main rating agencies Fitch Ratings Ltd, Moody's Investors Service and Standard & Poor's to assess the risk of default. This allows the Council to generate a list of highly creditworthy counterparties and enables diversification and thus avoidance of concentration risk. The lowest available credit rating will be used to determine credit quality. Credit ratings are obtained and monitored by the Council's Treasury Advisers, who will notify changes in ratings as they occur. Where an institution has its credit rating downgraded so that it fails to meet the minimum credit rating criteria then:

- No new investments will be made;
- Any existing investments that can be recalled at no cost will be recalled; and
- Full consideration will be given to the recall of any other existing investments.

The Section 151 Officer will be notified immediately to consider the appropriate action to be taken, if any, where a credit rating agency announces that it is actively reviewing an organisations credit rating with a view to downgrading it so that it is likely to fall below the Council's minimum criteria.

The categories and definitions are set out below:

Fitch's Credit Ratings and Definitions

Short Term Investments		
F1	Highest short-term credit quality	Indicates the strongest intrinsic capacity for timely payment of financial commitments; may have an added "+" to denote any exceptionally strong credit feature.
F2	Good short-term credit quality	Good intrinsic capacity for timely payment of financial commitments.
F3	Fair Credit Quality	Capacity for timely payment is adequate, however near term changes could result in a reduction to non-investment grade.
B	Speculative	Minimal Capacity for timely payment, vulnerability to near term adverse changes.
Long Term Investments		
AAA	Highest credit quality	Lowest expectation of default risk. Exceptionally strong capacity for payment of financial commitments which is highly unlikely to be adversely affected by foreseeable events.
AA:	Very high credit quality.	Very low default risk with very strong capacity for payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.

A:	High credit quality.	Expectations of low default risk. The capacity for payment of financial commitments is considered strong but may, nevertheless, be more vulnerable to adverse business or economic conditions than is the case for higher ratings.
BBB	Good credit quality	Expectations of default risk are currently low. The capacity for payment of financial commitments is considered adequate but adverse business or economic conditions are more likely to impair this capacity.
BB	Speculative	Elevated vulnerability to default risk, particularly in the event of adverse changes in business or economic conditions over time.
B	Highly speculative	material default risk is present, but a limited margin of safety remains. Financial commitments are currently being met; however, capacity for continued payment is vulnerable to deterioration in the business and economic environment.

Moody's Credit Rating and Definitions

Short Term Investments	
P1	Prime 1 - Issuers have a superior ability to repay short term debt obligations
P2	Prime 2 – Issuers have a strong ability to repay short term debt obligations
P3	Prime 3 – Issuers have an acceptable ability to repay short term debt obligations
NP	Not Prime – No prime rating
Long Term Investments	
Aaa	Judged to be highest quality and subject to the lowest level of risk
Aa	Judged to be high quality and subject to very low credit risk
A	Judged to be upper medium grade and subject to low credit risk
Baa	Judged to be medium, grade and subject to moderate credit risk
Ba	Judged to be speculative and subject to high credit risk
B	Considered speculative of poor standing and are subject to very high credit risk
Caa	Judged to be speculative of poor standing and are subject to very high credit risk
Ca	Highly speculative and are likely in, or very near, default, with some prospect of recovery of principal or interest.
C	Lowest rated and are typically in default

Standard and Poor's Credit Ratings and Definitions

AAA	Investment Grade – Extremely strong capacity to meet financial commitments
AA	Investment Grade – Very strong capacity to meet financial commitments
A	Investment Grade – Strong capacity to meet financial commitments but susceptible to adverse economic conditions and changes in circumstances
BBB	Investment Grade – Adequate capacity to meet financial commitments but susceptible to adverse economic conditions and changes in circumstances

BB	Speculative Grade – Less vulnerable in the near term but faces major ongoing uncertainties
B	Speculative Grade – Vulnerable to adverse conditions but still has capacity to meet financial commitments
CCC	Speculative Grade – Currently vulnerable and dependent on favourable conditions to meet financial commitments
CC	Speculative Grade – Highly vulnerable default has not yet occurred but is expected to as a virtual certainty
C	Speculative Grade –Currently highly vulnerable to non-payment
D	Payment breach of a financial commitment or in breach of an imputed promise

Other Information

Additional requirements under the Code require the Council to supplement credit rating information therefore credit ratings will not be the sole determinant of the quality of an institution. It is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration, the Council will engage with its treasury advisers to maintain a monitor on market pricing such as **"**credit default swaps**"** and overlay that information on top of the credit ratings.

Other Information Sources

Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

Categories of Investments

Investments fall into 1 of 2 categories, specified and non-specified investments.

Specified Investments

Specified investments are those expected to offer relatively high security and liquidity and can be entered into with the minimum of formalities. The WG Guidance defines an investment as a specified investment if all of the following apply:

- The investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling.
- The investment is not a long-term investment (i.e. due or available to be repaid within 12 months).
- The making of the investment is not defined as capital expenditure by virtue of regulation 20 (1)(d) of the Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 Statutory Instrument 3239 (W319) (as amended)
- The investment is made with a body or in an investment scheme of high credit quality or with one of the following public-sector bodies:
    - the United Kingdom Government

- a local authority in England or Wales (as defined in section 23 of the 2003 Act) or a similar body in Scotland or Northern Ireland
- a parish or community council.

The Council defines “high credit quality” organisations and securities as those having a long term credit rating of A- or higher that are domiciled in the UK or a Non UK country with a sovereign rating of AA- or higher. For money market funds and other pooled funds “high credit quality” is defined as those having a credit rating of A- or higher.

Brexit

The UK’s sovereign rating is AA long term. If there were to be a disorderly Brexit after December 2020, the Council will apply a sovereign rating at least equal to that of the United Kingdom for any UK based counterparty. This approach will not limit the number of UK counterparties available to the Council. To ensure the Council’s credit risk is not increased outside the UK, the sovereign rating requirement for investments to Non UK countries will be a minimum of AA-.

Non-Specified Investments

Any investment not meeting the definition of a specified investment is classed as Non-Specified. The Council does not intend to make any investments in foreign currencies, nor any with low credit quality bodies, nor any that are defined as capital expenditure by legislation.

Non-specified investments will therefore be limited to long-term investments. The Council does not currently hold any non-specified investments but will consider opportunities in this area subject to the advice of the Council’s treasury advisers and the views of the Section 151 Officer.

Investment Limits

	Short Term (under 12 months)	**Long Term (12 months+)**
UK Government incl. Treasury Bills, Gilts and DMADF	Unlimited	Unlimited
UK Local Authorities	£5M per organisation.	£5M per organisation
UK Fire & Police Authorities	£5M per organisation.	£5M per organisation
UK and Foreign Financial Institutions (A-)	£5M per organisation	£5M per organisation
UK Call Bank Accounts in UK Banks (F1/P-1/A-1)	£5M per organisation	Not required

The Council does not currently invest in any individual country outside the UK and it is intended that this approach will continue in 2020/21. The total investment in individual UK institutions that are part of the same UK owned group will not exceed the limit set out in the table above.

Investment Contingencies

Certain contingencies are required to be included in the Strategy for instances where sums of money cannot be invested on the money market either because it is received too late in the working day or for any other reason.
These monies will be deposited in the Council's current account. All deposits will be subject to the limit included in specified investments. Any such deposit must be withdrawn from the account and invested on the money market in the usual manner at the earliest opportunity.

Liquidity of Investments

The Council's expenditure programmes together with the maintenance of adequate reserves etc. will be used to determine the maximum period for which funds may prudently be committed. The maximum period for which funds may prudently be committed in any individual investment shall not exceed 10 years.

The Council's investments for the period to 31st December 2019 are set out below.

Investment Counterparty	**Opening Balance 01/04/2019**	**Invested**	**Repaid**	**Closing Balance 31/12/19**
	£000	**£000**	**£000**	**£000**
Local Authorities including Fire & Police	81,000	251,650	(250,900)	81,750
Debt Management Account Deposit Facility (DMADF)	8,100	1,719,935	(1,721,535)	6,500
Treasury Bills	0	9,800	9,800	0
Total	**89,100**	**1,981,385**	**(1,982,235)**	**88,250**

Interest, at an average rate of 0.74% and amounting to £525,987 has been received from maturing Local, Fire & Police Authorities and Debt Management Deposit Facility investments for the first 9 months of 2019/20. The average rate of return on Treasury Bills was 0.68% and interest amounted to £5,138.

The above analysis shows that 92.63% of the Council's investments were placed with local, fire & police authorities as at 31st December 2019. The Council has increased the average interest rate return from these investments 0.62% in 2018/19 to 0.78% in the first 9 months of 2019/20. Funds placed with the DMADF have yielded investment income at a rate of 0.50%.

Whilst the Council has no specific exposure, the Section 151 Officer has continued to follow closely the emerging picture in relation to a number of Council's financial positions and continues temporarily to suspend the placement of investments with certain councils. The Section 151 Officer considers that having taken the advice of Link Asset Management and with regard to the provisions in respect of any default set out in the Local Government Act 2003 that it is prudent for the Council to continue to invest with local authorities.

Treasury Bills

The Authority commenced the placement of funds with Treasury Bills in November 2019 after engaging the services of King & Shaxson Ltd.

King & Shaxson Ltd provide a tailor made service for local authorities together with the custodian account required to utilise this investment tool. They currently are the only provider of this service in the market at this time.

A Treasury Bill (T-Bill) is a short-term debt obligation backed by the Treasury Department of the U.K. Government with a maturity of less than one year, sold in denominations of a minimum of £500,000 with £50,000 increments thereafter. There is a weekly auction held on a Friday with settlement due the following Monday. T-bills have various maturities and are issued at a discount from par. Treasury Bills may also be purchased on the secondary market.

Contracts for financial services related to the issue or transfer of shares and other instruments are excluded contracts under the Public Contracts Regulations 2015 legislation. Services in relation to our investment in Treasury Bills fall into this exclusion.

Money Market Funds

The change in legislation in 2018/19 by the Welsh Government now permits the Council to consider the use of Money Market Funds when placing very short term investments as an alternative to the Debt Management Account Deposit Facility (DMADF).

Money Market Funds (MMFs) are pooled funds that invest in short- term debt instruments. They provide the benefits of pooled investment as investors can participate in a more diverse and high quality portfolio than they would otherwise individually. Each investor who invests in a money market fund is considered a shareholder of the investment pool, a part owner of the fund.

The principal objectives of MMF’s are preservation of capital, very high liquidity and competitive returns commensurate with security and liquidity. The most important characteristic of a MMF is the highly diversified, high credit quality investments in the fund.

Assets that a MMF may invest in are securities issued by sovereign governments, treasury bills, investments with the DMADF, certificates of deposits issued by financial institutions, floating rate and medium term notes, commercial paper and very short dated term deposits.

The Council has a comprehensive list of the best performing MMF’s commensurate with risk and is currently in the process of engaging the services of CCLA Investment Management Ltd and Federated UK as they are both domiciled in the United Kingdom. Contract documentation is in the process of being reviewed by the Council’s Legal Section. Any appointments will be reported to Cabinet as part of the Mid Year Report.

The maximum funds to be deposited in an individual MMF will be £5m.

Ethical Investing

Ethical investing is a topic of increasing interest to members, and one that is also being raised through officers. However, investment guidance, both statutory and from CIPFA, makes clear that all investment activities must adopt the principles of security, liquidity and yield and therefore ethical issues must play a subordinate role to those priorities. There is however some evidence already in place with local authority investing, including the incorporation of Environmental, Social and Governance (ESG) ESG metrics into credit rating agency assessments.

Climate Change

The Welsh Government (WG) investment guidance published on the 22nd November 2019 requires the following:-

"Local authorities should disclose to what extent investment decisions consider long-term climate risks to support a low carbon economy".

The Authority currently only invests funds with Local Authorities (including the Police & Fire Services) and the UK Government and borrows only from the PWLB therefore the above disclosure at present is not relevant from a treasury management point of view. Should the local authority expand the counterparties with whom it invests and borrows then the above will be taken account when making any strategic decisions and reported to Members.

External Service Providers

Treasury Management Advisors

The Council appointed Link Asset Management as their external treasury management advisors from September 2018. The services received include:

- Advice and guidance on relevant policies, strategies and reports;
- Advice on investment decisions;
- Notification of credit ratings and changes;
- Other information on credit quality;
- Advice on debt management decisions;
- Accounting advice;
- Reports on treasury performance;
- Forecasts of interest rates; and
- Training courses.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

The Section 151 Officer may appoint cash or fund managers to manage on its behalf all or part of the Council's investments. Any external manager so appointed will be expected to comply with the Annual Investment Strategy.

External Fund Managers

External cash or fund managers may be appointed by the Section 151 Officer to manage all or a proportion of its available cash balances. The external managers are also required to comply with Guidance on Local Government Investments issued by Welsh Government. The investment criteria imposed on the external managers will be included in the Investment Management Agreement**.** The Council at present do not engage external fund managers.

Investment Training

The CIPFA Code requires that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. Training provided by the Council's treasury advisor was undertaken by members in December 2017 and further training was provided in February 2019. The training needs of treasury management officers are periodically reviewed and are assessed as part of the staff appraisal process and from the frequent in-house meetings between the Treasury Management Team and the Section 151 Officer.

Use of Financial Derivatives

The Localism Act 2011 includes a general power of competence that removes the uncertain legal position over English local authorities' use of standalone financial derivatives (.i.e. those that are not embedded into a loan or investment). Although this change does not apply to Wales, the latest CIPFA Code requires authorities to clearly detail their policy on the use of derivatives in the annual strategy.

In the absence of any legislative power, the Council's policy is not to enter into standalone financial derivatives transactions such as swaps, forwards, futures and options. Embedded derivatives will not be subject to this policy, although the risks they present will be managed in line with the overall Treasury Risk Management Strategy.

Cardiff Capital Region City Deal

The Vale of Glamorgan Council is a participant in the Cardiff Capital Region City Deal which has been established between the UK Government, the Welsh Government and 10 local authorities in South East Wales. The agreement with the UK and Welsh Governments' provides £1.2 billion of which £734m is allocated to the Metro, with the balance of £495m being made available as the Wider Investment Fund.

The Vale of Glamorgan's share of the estimated total costs (8.5%) is projected to be in the order of £17.9m and will be funded by unsupported borrowing with a 20 year repayment period. The Vale of Glamorgan Council's contribution to expenditure was £1.043m in 2018/19 and this cost has been funded from borrowing which will be financed from the Council's own resources.

The Section 151 Officer considers that it is prudent to reflect the current funding proposals in the Treasury Management indicators and the Strategy, however, they will be updated as and when changes in expenditure plans are advised to the Council.

Project Bank Account

Welsh Government is committed to ensuring that sub-contractors involved in the delivery of public sector contracts in Wales are treated fairly. Previous experience suggests that payment practices have been historically poor throughout the supply chain and has led to cashflow pressures, which can have a greater effect on smaller companies further down the supply chain.

In order to improve this situation and to provide greater certainty of payment through the supply chain and to optimise payment periods to minimise financing charges, Welsh Government procurement policy requires Project Bank Account (PBA) arrangements to be used for publicly funded construction/infrastructure projects.

PBAs are ring fenced bank accounts with trust status which act solely as a receptacle for transferring funds from the client to the lead contractor and its sub-contractors. PBAs allow simultaneous payments to all levels of the supply chain.

As the PBA has trust status, monies can only be paid to the named beneficiaries of the PBA. These would be the lead contractor and other sub-contractors within the project's supply chain. The Vale of Glamorgan Council and the lead contractor would both be trustees of the bank account, however the account would be set up by the lead contractor The Council will only place its funds with institutions which have a credit rating of A- or higher. The PBA would therefore need to be opened with an institution which meets this minimum requirement.

The first Project Bank Account was set up during 2019/20 with Lloyds Bank PLC to be used as a vehicle to make payments under the design and build contracts for 21st Century Schools and additional accounts will be added as the various schemes progress.

MiFID II

Local authorities had been treated by regulated financial services firms as professional clients who can opt down to be treated as retail clients instead, however, from January 3rd 2018, as a result of the second Markets in Financial Instruments Directive (MiFID II), local authorities are treated as retail clients who can opt up to be professional clients, provided that they meet certain criteria.

Regulated financial services firms include banks, brokers, advisers, fund managers and custodians, but only where they are selling, arranging, advising or managing designated investments. In order to opt up to professional, the authority must have an investment balance of at least £10 million and the person authorised to make investment decisions on behalf of the authority must have at least one year's relevant professional experience. In addition the firm must assess that, that person has the expertise, experience and knowledge to make investment decisions and understand the risks involved.

The main additional protection for retail clients is a duty on the firm to ensure that the investment is suitable for the client. However, local authorities are not protected by the Financial Services Compensation Scheme nor are they eligible to complain to the Financial Ombudsman Service whether they are retail or professional clients. It is also likely that retail clients will face an increased cost and potentially restricted access to certain products including money market funds, pooled funds, treasury bills, bonds, shares and to financial advice. The Council has declined to opt down to retail client status in the past as the costs were thought to outweigh the benefits.

The Council meets the conditions to opt up to professional status and has opted to do so with the Council's treasury advisers Link Asset Management and the brokers that it transacts with in order to maintain their current MiFID status.

Management practices for non-treasury investments

This organisation recognises that investment in other financial assets and property primarily for financial return, taken for non-treasury management purposes, requires careful investment management. Such activity includes loans, supporting service outcomes, investments in subsidiaries and investment property portfolios.

The Council will ensure that all the organisation's investments of this nature are covered in the capital strategy, investment strategy or equivalent and will set out, where relevant, the organisation's risk appetite and specific policies and arrangements for non-treasury investments.

A schedule of the Council's existing non treasury investments (currently limited to the investment in the Big Fresh Catering Company) is set out below;

- **Investment in Subsidiary - Big Fresh Catering Company**

On 1st January 2020, the Council set up a Local Authority Trading Company to deliver Catering services called the Big Fresh Catering Company. The Council owns 100% of the company shares. In accordance with WG Investment Guidance this will be classified as a Non Treasury Investment.

IFRS9 – Local Authority Override

The Welsh Government issued draft regulations on 14.11.19 for consultation and feedback by 31.12.19, to introduce a statutory over-ride from 1 April 2020 for a four-year period until 31 March 2023 following the introduction of IFRS 9, over the requirement for any unrealised capital gains or losses arising from investment in marketable pooled funds to be chargeable in year. This has the effect of allowing any unrealised capital gains or losses arising from qualifying investments to be held on the balance sheet until 31 March 2023: this will enable councils to initiate an orderly withdrawal of funds if required.

IFRS 16 Leasing

From 1st April 2020 IFRS 16 which deals with the way the Council accounts for its lease arrangements will be introduced. The revised accounting code requires significant changes for how the Council accounts for contracts that convey the right of use of an asset for a period of time. Whereas the Council currently accounts for all its lessee lease arrangements through revenue income and expenditure, under the new arrangement the Council will be required to calculate a right of use asset and a corresponding liability which will be included on its balance sheet. The liability will increase the Council's CFR and the Council will need to charge MRP which will in practice be equivalent to the principal of the lease. Despite the extensive accounting requirements and disclosures this change of accounting policy will not impact the bottom line of the accounts. It will however have an impact on the Treasury Management indicators and MRP estimates included in this strategy. The accountancy section are currently undertaking an assessment of the likely right of use assets and liabilities associated with the Council's leases and embedded lease arrangements and it is intended that revised indicators that incorporate these estimates are reported as part of the Mid Year report.

Appendix 2

Treasury Management Policy

Whilst considerations, such as interest rate forecasts, will inevitably inform the Treasury Management Strategy to be adopted over the coming year(s), account must also be taken of certain fundamental parameters that the Council must work within. These may include political, environmental, social, technical, economic and legislative factors and form the basis of the Treasury Management Policy that underpins the Strategy.

The following statement therefore, constitutes the Treasury Management Policy of the Council. Adherence to its requirements is mandatory for all matters relating to Treasury management and Investment.

Definition

The Council defines Treasury Management as:

“The management of the Council’s borrowing, 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.”

Objectives and Purpose

The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its Treasury Management activities will be measured. Accordingly, the analysis and reporting of Treasury Management activities will focus on their risk implications for the Council and any financial instruments entered into to manage these risks.

The Council acknowledges that effective Treasury Management will provide support towards the achievement of its business and service objectives. It is, therefore, committed to the principles of achieving value for money in Treasury Management and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

The objectives of the policy are to: -

- Support the quality and status of Treasury Management; and
- Provide guidance on the proper practices to be employed for Treasury Management.

The purpose of this Policy is to give guidance and advice on such matters as: -

- The allocation of responsibility among the relevant staff;
- Reconciliation of the need for rapid decisions on dealing with the need to be accountable for use of delegated authority;
- Mechanisms to satisfy the statutory obligations placed upon the Monitoring Officer and the Section 151 Officer; and
- Good practice in reporting at various levels in the Council.

Procedure

All investments of money under the Council's control shall be made in the name of the Council or in the name of the nominees approved by the Council. Bearer securities shall be excluded from this regulation, but any purchase of such securities shall be reported to the Council.

All borrowings shall be effected in the name of the Council and must be authorised by the Section 151 Officer (subject to the Policy on Delegation set out below).

All money in the hands of the Council shall be under the control of the Section 151 Officer.

The Section 151 Officer shall be the Council's Registrar of Bonds and shall maintain records of all borrowings of money by the Council.

All officers acting as trustees by virtue of their official position shall deposit all securities, etc. relating to the trust with the Head of Legal Services unless the deed otherwise provides.

Formulation of Treasury Management/Investment

At or before the start of the financial year, the Section 151 Officer shall report to the Council on the Treasury Management Strategy it is proposed to adopt for the coming financial year (including Prudential Indicators for the coming three financial years). At the same time the Council will consider for adoption for the coming financial year an Annual Investment Strategy.

Borrowing Policy

Revenue budget stability is desirable and with this in mind the Council would usually borrow the majority of its long-term funding needs at long-term fixed rates of interest. Short-term and variable rate loans will only be borrowed to the extent that they either offset short-term and variable rate investments or can be shown to produce revenue savings.

The Council will set an affordable borrowing limit each year in compliance with the Local Government Act 2003 and will have regard to the CIPFA Prudential Code for Capital Finance in Local Authorities when setting that limit. It will also set limits on its exposure to changes in interest rates and limits on the maturity structure of its borrowing in the treasury management strategy report each year.

Investment Policy

The Council's primary objectives for the investment of its surplus funds are to protect the principal sums invested from loss and to ensure liquidity. Investment income is important but a secondary objective.

The Council will have regard to the Welsh Government Guidance on Local Government Investments and will approve an Investment Strategy each year as part of the Treasury Management strategy. The Strategy will set criteria to determine suitable organisations with which cash may be invested and limits on the amount of cash that may be invested with any one organisation.

Policy on Custodians

To facilitate the use of some approved investment instruments (eg Treasury Bills), the use of custodian facilities are required. The Section 151 Officer may appoint a custodian to administer and safeguard any investments on behalf of the Council providing that this custodian operates at all times within the Authority's Treasury Management Policy & Investment Strategy framework.

Policy on Delegation

All executive decisions on borrowing, investment or financing shall be delegated to the Section 151 and the Deputy Section 151 Officer (in his / her absence) or through the following posts, who shall all be required to act in accordance with CIPFA's "Code for Treasury Management in the Public Services".

- W-RM-AC003 Principal Accountant
- W-RM-AC015 Senior Accounting Technician
- W-RM-AC006 Capital Accountant
- W-RM-AC014 Corporate Accountant

Review Requirements and Reporting Arrangements

The Section 151 Officer shall report to the Council as follows: -

Before the 31st March each year

- The Treasury Management Prudential Indicators for the forthcoming three years; and
- The Treasury Management Strategy and Annual Investment Strategy for the following year (the Treasury Management Strategy also incorporates the indicators for the forthcoming three years).

A revised Investment Strategy may be prepared if at any time it is considered appropriate.)

A mid-year review during the current year.

As soon as possible after the end of the financial year - report on the out-turn for the previous year.

The Section 151 Officer shall also report to Cabinet and/or Scrutiny Committee other monitoring reports that are considered necessary to comply with CIPFA's "Code for Treasury Management in the Public Services".

Scheme of Delegation

(i) Full Council

- Receiving and reviewing reports on Treasury Management policies, practices and activities; and
- Approval of annual Treasury Management & Investment Strategy.

(ii) Cabinet

- Approval of/amendments to the organisation's adopted clauses, Treasury Management Policy Statement and Treasury Management practices;
- Budget consideration and approval;
- Receiving and reviewing regular monitoring reports and acting on recommendations; and

(iii) Scrutiny Committee

- Reviewing the Treasury Management policy and procedures and making recommendations to the responsible body.

The Role of the Section 151 Officer

The S151 Officer will be responsible for the following:

- Recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- Submitting regular Treasury Management policy reports;
- Submitting budgets and budget variations;
- Reviewing the performance of the Treasury Management function;
- Ensuring the adequacy of Treasury Management resources and skills, and the effective division of responsibilities within the Treasury Management function;
- Ensuring the adequacy of internal audit, and liaising with external audit;
- The appointment of external service providers;
- Preparation of a capital strategy to include capital expenditure, capital financing, and treasury management, with a long term timeframe;
- Ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money; and
- Ensuring that due diligence has been carried out on all investments and is in accordance with the risk appetite of the authority.