

To: Cabinet
Date: 8 February 2023
Report of: Head of Financial Services
Title of Report: Treasury Management Strategy 2023/24

Summary and recommendations	
Purpose of report:	To present the Council's Treasury Management Strategy for 2023/24 together with the Prudential Indicators for 2023/24 to 2026/27
Key decision:	Yes
Cabinet Member:	Councillor Ed Turner, Deputy Leader (Statutory) and Cabinet Member for Finance and Asset Management
Corporate Priority:	All
Policy Framework:	Council Strategy 2020 - 24
Recommendations: That Cabinet resolves to:	
Recommend that Council approves:	
<ol style="list-style-type: none"> 1. The Treasury Management Strategy 2023/24 as set out in paragraphs 29 to 78 of this report and the Prudential Indicators for 2023/24 – 2026/27 as set out in Appendix 2; 2. The Borrowing Strategy 2023/23 at paragraphs 52 to 54 of this report; 3. The Minimum Revenue Provision (MRP) Statement at paragraphs 55 to 57 which sets out the Council's policy on charging borrowing to the revenue account; 4. The Investment Strategy for 2023/24 and the investment criteria as set out in paragraphs 58 to 77 of this report and in Appendix 1; and 5. The Treasury Management Scheme of Delegation at Appendix 4 	

Appendices	
Appendix 1	Credit and Counterparty Risk Management
Appendix 2	Prudential Indicators 2023/24 – 2026/27
Appendix 3	Environmental, Social and Governance (ESG) Policy
Appendix 4	Scheme of Delegation
Appendix 5	Risk Register

Summary

1. The Council's Treasury Management Strategy has been written in accordance with the CIPFA Prudential Code, the CIPFA Treasury Management Code of Practice (the Codes) and the Department of Levelling Up, Housing and Communities' (DLUHC) Guidance on Local Government Investments.
2. The report presents the Council's prudential indicators for 2023/24 – 2026/2027. Notable indicators include capital expenditure and borrowing limits as these are areas of significant activity.
3. The average value of investments during the calendar year to 31st December 2022 was £107.7 million. The actual daily value fluctuated between £79.5 million and £135.0 million. For the previous calendar year, average balances were £101.2 million and daily values ranged from £77.6 million to £128.8 million.
4. All external debt as at 31 March 2022 (£198.5m) relates to the Housing Revenue Account (HRA) self-financing debt originally taken out in 2012 which is held at fixed rates with varying fixed periods to maturity.
5. The Council's General Fund Capital Programme over the next four years is funded from a combination of government grants, capital receipts, revenue, Community Infrastructure Levy and prudential borrowing. However, due to the scale of investment over the period to 2023/24 to 2026/27, including the loans to the Council's Housing Company (£89.0 million), the level of prudential borrowing will increase to over £813.3 million in 2026/27 from the projected £374.8 million at the end of 2022/23. Borrowing from internal resources will be maximised on the General Fund, however much of the borrowing will need to be from external resources with anticipated external borrowing increasing from £198.5 million to £698.5 million in 2026/27. The Housing Revenue Account Capital Programme is largely funded from council house rents over time but includes £376.4 million borrowing from 2022/23 to 2025/26. Since the Council operates a two pool system for borrowing, any prudential borrowing on the HRA will be funded by external borrowing to the same value.
6. The CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice were revised in late 2021 and these versions have been fully adopted from 2023/24 onwards in line with the required adoption timescale. The key changes are outlined in the section below.
7. All Prudential Indicators continue to be covered together in the Treasury Strategy. This will allow the indicators to be seen as a whole and in the context of Treasury Management activity to which they are closely related. There are, however, some cross-overs to areas covered in more detail by the Capital Strategy. There have been changes to the indicators in line with the requirements of the codes.
8. The Department for Levelling Up, Housing and Communities (DLUHC) is due to undertake an additional consultation on the detail of proposed changes to regulations around Minimum Revenue Provision. Although the outcome of this is

not yet known, the treasury budgets and, consequently, the prudential indicators include the latest assessment of potential financial impacts which, following discussions with DLUHC are expected to have limited impact on the Council. The driver for this change was to restrict local authorities financing capital expenditure on investments in commercial projects made primarily for yield, although it has wider implications. The Government has already closed access to all Public Works Loans Board (PWLB) borrowing if such schemes are included in an authority's capital programme. The new CIPFA codes have also adopted a similar set of restrictions to discourage further capital expenditure on commercial investments for yield.

9. The limit for non-specified investments is proposed to remain at 30% of the previous year's total investment portfolio or £30 million, whichever is the greater, which allows capacity for occasional non-specified investments other than pooled investment funds such as investments with local authorities for longer than 364 days.

Key Changes from Previous Years

10. CIPFA published the revised Codes on 20th December 2021 and has stated that revisions need to be included in the reporting framework from the 2023/24 financial year. The Council, therefore, has to have regard to these Codes of Practice when it prepares the Treasury Management Strategy Statement and Annual Investment Strategy, and also related reports during the financial year, which are taken to Full Council for approval.
11. The revised Treasury Management Code has widened the definition of investments and requires all investments and investment income to be attributed to one of the following three purposes: -

Treasury management – Arising from the organisation's cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.

Service delivery – Investments held primarily and directly for the delivery of public services including housing, regeneration and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in cases where the income is "either related to the financial viability of the project in question or otherwise incidental to the primary purpose". These are covered by considerations in the Capital Strategy but are also included in the prudential indicators in this report.

Commercial return – Investments held primarily for financial return (which is measured as 50% or more) with limited treasury management or direct service provision purpose. Risks on such investments should be proportionate to an authority's financial capacity – i.e., that 'plausible losses' could be absorbed in budgets or reserves without unmanageable detriment to local services. An authority must not borrow to invest primarily for financial return. The Council is not planning to undertake this type of activity.

12. The Prudential Indicators have been revised in line with the Codes of Practice. This includes separate indicators relating to “commercial investment” and “service investment”. This change has occurred due to some Councils (which have been featured in the press) incurring substantial expenditure buying investment properties to support their revenue budgets. Changes include: -
 - Adopting a new liability benchmark treasury indicator to support the financing risk management of the capital financing requirement; this is to be shown in chart form for a minimum of ten years, with material differences between the liability benchmark and actual loans to be explained;
 - A prudential indicator for the net income from commercial and service investments as a proportion of the net revenue stream;
 - Long-term treasury investments, (including pooled funds), are to be classed as commercial investments unless justified by a cash flow business case;
 - Pooled funds are to be included in the indicator for principal sums maturing in years beyond the initial budget year;
13. Inclusion of Management Practices around managing risks and other governance arrangements associated with non-treasury investments, (similar to the current Treasury Management Practices) – this is included within the Capital Strategy.
14. Production of a knowledge and skills register for officers and members involved in the treasury management function to be proportionate to the size and complexity of the treasury management conducted by each authority. This will be considered over the 2023/24 financial year and any training needed will be identified.
15. Environmental, social and governance (ESG) issues to be considered within an authority’s treasury management policies and practices (TMP1) where applicable.
16. A scheme of delegation which formally defines where various reports and information are considered and / or approved (this is shown at Appendix 4).

Interest and Economic Outlook

17. The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Link provided the following forecasts on 19th December 2022. This includes forecasts for Public Works Loans Board (PWLB) interest rates which represent gilt yields plus 80 bps (0.8%).

Link Group Interest Rate View		19.12.22											
	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
BANK RATE	3.50	4.25	4.50	4.50	4.50	4.00	3.75	3.50	3.25	3.00	2.75	2.50	2.50
3 month ave earnings	3.60	4.30	4.50	4.50	4.50	4.00	3.80	3.30	3.00	3.00	2.80	2.50	2.50
6 month ave earnings	4.20	4.50	4.60	4.50	4.20	4.10	3.90	3.40	3.10	3.00	2.90	2.60	2.60
12 month ave earnings	4.70	4.70	4.70	4.50	4.30	4.20	4.00	3.50	3.20	3.10	3.00	2.70	2.70
5 yr PWLB	4.20	4.20	4.20	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.20	3.10
10 yr PWLB	4.30	4.40	4.40	4.30	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.30
25 yr PWLB	4.60	4.60	4.60	4.50	4.40	4.20	4.10	4.00	3.90	3.70	3.60	3.50	3.50
50 yr PWLB	4.30	4.30	4.30	4.20	4.10	3.90	3.80	3.70	3.60	3.50	3.30	3.20	3.20

Link Group Interest Rate View		08.11.22											
	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
BANK RATE	3.50	4.25	4.50	4.50	4.50	4.00	3.75	3.50	3.25	3.00	2.75	2.50	2.50
3 month ave earnings	3.60	4.30	4.50	4.50	4.50	4.00	3.80	3.30	3.00	3.00	2.80	2.50	2.50
6 month ave earnings	4.20	4.50	4.60	4.50	4.20	4.10	3.90	3.40	3.10	3.00	2.90	2.60	2.60
12 month ave earnings	4.70	4.70	4.70	4.50	4.30	4.20	4.00	3.50	3.20	3.10	3.00	2.70	2.70
5 yr PWLB	4.30	4.30	4.20	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.20	3.10
10 yr PWLB	4.50	4.50	4.40	4.30	4.20	4.00	3.90	3.70	3.60	3.50	3.40	3.30	3.20
25 yr PWLB	4.70	4.70	4.60	4.50	4.40	4.30	4.10	4.00	3.90	3.70	3.60	3.50	3.50
50 yr PWLB	4.30	4.40	4.30	4.20	4.10	4.00	3.80	3.70	3.60	3.40	3.30	3.20	3.20

Bank Rate

18. The interest rate forecast reflects a view that the Monetary Policy Committee (MPC) of the Bank of England will wish to put in what measures that it can to demonstrate it's trying to control inflation by delivering a succession of rate increases. This has happened but the Government's policy of emphasising fiscal control will probably mean Bank Rate will not need to increase to further than 4.5%. It is anticipated that the Bank of England will loosen monetary policy when inflationary pressures reduce, However if they cut too soon, inflationary pressures may well build up further; but if they cut too late then any downturn or recession may be prolonged.
19. The Consumer Prices Index (CPI) measure of inflation looks to have peaked at 11.1% in Q4 2022 (currently 10.7%). Despite the cost-of-living pressures, the Bank will want to see evidence that wages are not spiralling upwards in what is evidently a very tight labour market. However increased interest rates will tend to put additional pressure on costs.
20. The plan to sell £10bn of gilts back into the market each quarter (Quantitative Tightening) has started and will focus on the short, medium and longer period.
21. In the future, interest rate forecasts will be influenced by economic data releases, clarifications from the MPC over its monetary policies, clarifications from the Government over its fiscal policies, and macro-economic factors including the on-going conflict between Russia and Ukraine and the heightened tensions between China, Taiwan and the United States.
22. Consumers are still estimated to be sitting on over £160bn of excess savings left over from the pandemic however, most of those are held by more affluent people whereas lower income families already spend nearly all their income on essentials such as food, energy and rent / mortgage payments.

Gilt Yields/PWLB rates

23. The yield curve movements have become less volatile and the Public Works Loans Board (PWLB) Certainty Rates from 5 to 50 years are, generally, in the range of 4.10% to 4.80%. The forecasts assume that the markets have already built in nearly all the effects on gilt yields of the likely increases in Bank Rate and the elevated inflation outlook.
24. The overall balance of risks to economic growth in the UK is to the downside. Indeed, the Bank of England projected two years of negative growth in their November Quarterly Monetary Policy Report.
25. Downside Risks to current forecasts are:
- Labour and supply shortages prove more enduring and disruptive and depress economic activity.
 - The Bank of England acts too quickly, or too far, over the next year to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than anticipated.
 - UK / EU trade arrangements – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.
 - Geopolitical risks, for example in Ukraine/Russia, China/Taiwan/US, Iran, North Korea and Middle Eastern countries, which could lead to increasing safe-haven flows.
26. Upside risks to current forecasts are:
- The Bank of England is too slow in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly and for a longer period within the UK economy, which then necessitates the Bank Rate staying higher for longer than currently projected or even necessitates a further series of increases in Bank Rate.
 - The Government acts too quickly to cut taxes and/or increases expenditure in light of the cost-of-living pressures.
 - The pound weakens because of a lack of confidence in the UK Government's fiscal policies, resulting in investors pricing in a risk premium for holding UK sovereign debt.
 - Longer term US treasury yields rise strongly and pull gilt yields up higher than currently forecast.
 - Projected gilt issues are too much for the markets to accommodate leading to higher yields.

Investment and borrowing Rates

27. The Link long-term (beyond 10 years) forecast for Bank Rate is 2.5%. As all PWLB certainty rates are now above this level, borrowing strategies will need to be reviewed in that context. Better value can generally be obtained at the shorter end of the curve and short-dated fixed Local authority to Local Authority money should also be considered. Temporary borrowing rates are likely to remain near Bank Rate and may also prove attractive whilst the market waits for inflation, and therefore gilt yields, to drop back later in 2023.

28. Link's suggested budgeted earnings rates for investments up to about three months' duration in each financial year are as follows: -

Average earnings in each year	
2022/23 (remainder)	4.00%
2023/24	4.40%
2024/25	3.30%
2025/26	2.50%
2026/27	2.50%
Years 6 to 10	2.80%
Years 10+	2.80%

This shows the expected trajectory in interest rates. This profile has been built in to the Council's medium term financial plan.

Treasury Management Strategy Statement

Background

29. 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 counterparties or instruments commensurate with the Council's risk appetite, providing adequate liquidity initially before considering investment return.
30. 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.
31. The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance. Additionally reserves and balances are forecast to reduce over the short to medium term which will lead to reduced balances available for investment or to use for internal borrowing.

32. Whilst any loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, arising usually from capital expenditure, and are separate from the day to day treasury management activities and need different consideration and due diligence.
33. CIPFA defines treasury management as:
“The management of the local authority’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.”
34. Revised reporting has been required for the 2019/20 reporting cycle onwards due to revisions of the then Ministry for Housing, Communities and Local Government (MHCLG) Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The reporting changes included the introduction of the requirement to approve a capital strategy (which the Council produced in a slightly different form previously), to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011. The capital strategy is being reported separately and includes the additional requirements introduced with these changes.

Treasury Management Advisors

35. Treasury advice and market information is provided by Link Group. A procurement exercise was undertaken during 2018 and the contract was awarded to Link Group in September 2018 for 3 years and an option to extend for a further 2 years has been taken up with the contract now expiring in 2023. This service will be put out to tender over the coming months. The information provided by Link Group that is used for making investment decisions has been considered in the writing of this report and its associated appendices.
36. 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.

Training

37. The CIPFA Treasury Management Code requires the responsible officer to ensure that officers and members with responsibility for treasury management receive adequate training in treasury management. This focus of this is on members responsible for scrutiny.
38. The code also says that authorities should carry out the following to monitor and review knowledge and skills:

- Record attendance at training and ensure action is taken where poor attendance is identified.
 - Prepare tailored learning plans for treasury management officers and board/council members.
 - Require treasury management officers and board/council members to undertake self-assessment against the required competencies.
 - Have regular communication with officers and board/council members, encouraging them to highlight training needs on an ongoing basis.”
39. The training needs of treasury management officers are periodically reviewed. A formal record of the training received by officers central to the Treasury function will be maintained by the Treasury Manager. Similarly, a formal record of the treasury management / capital finance training received by members will also be maintained.
40. Officers will identify a training plan to be delivered over 2023/24, probably using the independent expertise of the Council’s Treasury Advisors, Link.

Bank Account Management

41. Bank accounts for the Council and wholly owned companies are with the same banker. Accounts have a grouping arrangement in place which means that overall there are limits of a net overdraft of £100k and aggregate overdraft balances cannot exceed £5 million.
42. The daily treasury function aims to keep net overnight balances as close to zero as possible to maximise the level of funds invested and balances between accounts are managed by making temporary cash transfers between the entities.
43. Interest is paid / charged based on the true balance (i.e. excluding any temporary cash transfers). Overdrawn balances are charged at a rate based on PWLB 1 year borrowing rates plus a supplement to account for arms-length transfer pricing; interest is paid at the average interest earned on investments (excluding the pooled funds).

Borrowing and Debt

44. Under the Prudential Code, individual authorities are responsible for deciding their level of borrowing. The system is designed to allow authorities with an affordable borrowing requirement, to borrow in order to pay for capital investment. The arrangements also facilitate ‘invest to save’ schemes where they are affordable, prudent and sustainable.
45. In the Prudential Code guidance, CIPFA has defined the Council’s investments in Property Funds and Multi Asset Funds as “Commercial Investments”. It then goes on to say “Authorities with existing commercial investments (including property) are not required by this Code to sell these investments. Such authorities may carry out prudent active management and rebalancing of their portfolios. However, authorities that have an expected need to borrow should

review options for exiting their financial investments for commercial purposes and summarise the review in their annual treasury management or investment strategies.” Accordingly the Council’s Chief Financial Officer has considered these investments and does not believe that divesting from them is prudent or appropriate given the current economic climate and also does not consider that divestment is in the best interest of the Council or its Medium Term Financial Plan at this time.

46. The parameters for determining the level of prudential borrowing are:
- A balanced revenue budget that includes the revenue consequences of any capital financing i.e. interest, debt repayment and running costs of any new project; and
 - That the impact of the Authorised Borrowing Limit on Council Tax or council rents is reasonable.
47. The Council’s draft Capital Programme for 2023/24 to 2026/27, which appears elsewhere on the Agenda; includes the £481.6 million expenditure which is currently planned to be financed by borrowing of which £317.2 million relates to the Housing Revenue Account.
48. The Council Chief Financial Officer (the Section 151 officer) has delegated authority to determine the need for external borrowing taking into account prevailing interest rates and associated risks. Borrowing may be undertaken to fund the approved Capital Programme or to fund future debt maturities and a combination of long-term and short-term fixed and variable rate borrowing may be considered which may include borrowing in advance of future years’ requirements. In using the delegated authority, the S151 Officer will take into account the following factors:
- The on-going revenue liabilities created, and the implications for the future plans and budgets;
 - The economic and market factors that might influence the manner and timing of any decision to borrow;
 - The pros and cons of alternative forms of funding including internal borrowing; and
 - The impact of borrowing in advance on cash balances and the consequent increase in counterparty risk.
49. Council officers, in conjunction with the Council’s treasury advisors, Link Group, monitor prevailing interest rates and market forecasts, thereby allowing the Council to respond to any changes that may impact on the timing and manner of borrowing decisions, to ensure these are optimised.
50. The Council currently has £198.5m of external debt held at fixed rates with varying maturity terms up to 2057. This debt relates to the Council’s housing stock within its HRA. The first repayment, of £20 million, was made at the end of 2020/21. Debt to the same value was taken out in order to replace the debt repaid. The first repayment of the remaining existing debt, in the sum of £20 million, will now take place in 2025-26 and it is currently expected that this will be refinanced.

51. The Council's Capital Financing Requirement (CFR) is an indication of the Council's underlying need to borrow to fund its capital investments; this borrowing can be undertaken internally using available resources or externally by borrowing from a reputable institution or the Public Works Loans Board (PWLB). The estimated level of CFR for each year can be found in the Prudential Indicators in Appendix 2.

Borrowing Strategy 2023/24

52. The Council had £60.4 million internal borrowing as at 1st April 2022. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt since cash supporting the Council's reserves, balances and cash flow has been used as a temporary funding source. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

53. The Head of Financial Services will continue to monitor interest rates and take a pragmatic approach to changing circumstances. Due to the risks within the economic forecast, and the increased fluctuations in cashflow being experienced, caution will be adopted with the 2022/23 treasury operations, although the decrease in PWLB rates has made the PWLB more competitive than other sources of borrowing again. Additionally the Council will consider carefully when to take out borrowing, balancing the need for cash to fund capital expenditure and the cost of borrowing.:

- If it is considered that there is a likelihood of a significant fall in long and short term rates (e.g. due to a marked increase of risks in respect of recession or deflation), then long term borrowing will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- Alternatively, if it is felt that there is a significant risk of a sharp increase in long and short term rates than currently forecast, then external borrowing is likely to be taken earlier.

Borrowing in Advance of Need

54. 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. Prior to borrowing in advance the risks and benefits of undertaking the borrowing will be considered. Actual borrowing will be subsequently reported through either the mid-year performance report or annual report as appropriate. Due to the amount of prudential borrowing in the Capital Programme, the potential benefits of earlier borrowing will be closely monitored.

Minimum Revenue Provision (MRP) Statement 2023/24

55. Prudential borrowing increases the Council's Capital Financing Requirement (CFR) or underlying need to borrow. Whether the Council actually borrows externally to finance capital expenditure is a treasury management decision which is not directly linked to the capital financing decision. In practice, the

Council is likely to use a combination of internal and external borrowing in the medium term to fund the Capital Programme. The amount of external borrowing undertaken will depend on the borrowing requirement compared to the projected level of cash balances. The Council is required to make a prudent charge to its revenue account for borrowing, whether that borrowing is financed internally or externally. This charge is known as the Minimum Revenue Provision (MRP) and reflects the repayment cost of principal borrowed.

56. Regulations require the Council to approve an MRP policy on an annual basis and to calculate in each financial year an amount of MRP that it considers to be prudent. In doing this, the Council has to pay regard to governmental statutory guidance on MRP. MRP is not charged until the financial year after the expenditure has been incurred and the asset being financed has become operational.
57. It is recommended that these MRP methodologies continue to be adopted for 2023/24, noting that these are likely to change for 2024/25 when there will be a change in regulations:
- a) For borrowing incurred before 1 April 2008 the practice of making a 4% annual charge on the reducing balance, outlined in the former Department for Communities and Local Government (DCLG) regulations, will apply.
 - b) For borrowing that relates to the assets transferred from the Housing Revenue Account (HRA) to the General Fund (GF), MRP will be based on the estimated useful life of the assets, taking into account the number of years the assets have been in existence, and previous funding allocated to them.
 - c) There will be no annual MRP charge made for the following items where they are deemed to be capital under s25(b) / s25(d) of The Local Authorities Capital Finance and Accounting (England) Regulations 2003 and where it is anticipated the investment will be repaid in full:
 - i. The Council's investments in a Directly Managed Property Fund;
 - ii. Loans to other organisations, such as a company in which the Council has an interest;
 - iii. Treasury management investments undertaken in accordance with section 12 of the Local Government Act 2003;
 - iv. Borrowing related to capital expenditure incurred on assets which are to be leased to one of the Council's companies; and
 - v. Other borrowing related to expenditure where it is anticipated the investment will be repaid in full.

The repayment to the Council for these will be a capital receipt of which the Council will set aside the amount for which borrowing was used in order to repay that borrowing. Each item where there is no annual MRP charge will be reviewed on at least an annual basis and if there is a likelihood of capital loss, a prudent MRP provision will then be made. Although this aspect of the policy is still considered to be prudent it is this element that the Government is looking to make changes to which could require an annual MRP charge regardless of whether loan agreements are in place to repay the loans.

- d) For all borrowing incurred after 1 April 2008 relating to expenditure other than that which is covered in c) above, the MRP will be charged using the Asset Life Method. The default methodology under this option is that MRP will be based on the estimated life of the asset and will be charged to the revenue account in equal instalments over the life of the asset. Where the Head of Financial Services, in their capacity of section 151 officer, is comfortable that the asset or the income arising from that asset is appreciating over time, MRP will be based on an annuity charge over the estimated life of the asset. Applying the annuity method results in an annual charge to revenue which takes account of the time value of money. The charges made through the annuity method thus results in a consistent charge over an asset's life, taking into account the real value of the annual charges when they fall due.
- e) For finance leases the council will charge MRP to its General Fund each year dependant on the life of the underlying asset.

Annual Investment Strategy 2023/24

58. This Treasury Management Strategy and the Annual Investment Strategy deals solely with treasury management investments; the categories of service delivery and commercial investments are addressed as part of the Capital Strategy report and appendix and also appear within the prudential indicators set out in appendix 2 to this report.

Management of Risk

59. The Department for Levelling Up, Housing and Communities (DLUHC) and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with financial investments, (as managed by the Council's treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy which is presented in a separate report.

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

- DLUHC's (then MHCLG) Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2021 ("the Code")
- CIPFA Prudential Code for Capital Finance 2021
- Prudential Code for Capital Finance Guidance Notes 2021

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

61. The guidance from DLUHC and CIPFA place a high priority on the management of risk. This authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

- a) Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.

- b) **Other information:** 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 advisors to maintain a monitor on market pricing such as “**credit default swaps**” and overlay that information on top of the credit ratings.
- c) **Other information sources** used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.
- d) This authority has defined the list of **types of investment instruments** that the treasury management team are authorised to use. There are two lists in Appendix 1 under the categories of ‘specified’ and ‘non-specified’ investments.
- **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.
 - **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.

62. As a result of the change in accounting standards for 2018/19 under IFRS 9, the Council will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. In November 2018, MHCLG concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years commencing from 1st April 2018. Even were this over-ride removed now, this would not give cause for concern since the value of investments is higher than the original balance sheet value, although it is worth noting this may not always be the case.

Investment Levels and Interest Rates

63. The average value of the Council’s investments during the calendar year to 31st December 2022 was £107.7 million. The actual daily value fluctuated between £79.5 million and £135.0 million. For the previous calendar year, average balances were £101.2 million and daily values ranged from £77.6 million to £128.8 million.
64. At 31st March 2022 the Bank of England (BOE) base rate was 0.75% and there have been steady increases throughout 2022 leaving the current base rate at 3.5%. The base rate is forecast to peak at 4.5% in mid 2023. The Council aims to achieve 0.2% above base rate on its investments over the course of a year.

Investment Durations

65. Most existing investment deal terms are for 6 months or 364 days. Investments are made in accordance with the Council's Treasury Management Strategy such that returns are balanced against security of investment and liquidity of cash to ensure funding of day to day cash flows and yield. Consequently, procedures are in place to determine the maximum periods that funds may be invested for, as well as the nature of those investments. The Council works to achieve the optimum rate of return on its investments commensurate with proper levels of security and liquidity.

Creditworthiness

66. Investment instruments identified for use are listed in Appendix 1 under the Specified and Non-specified investment categories. Counterparty limits are set in accordance with the Council's Treasury Management Practices (TMPs).

67. The Council utilises the creditworthiness services provided by Link Group. The model combines the credit ratings, credit watches and credit outlooks provided by the credit rating agencies - Fitch, Moody's and Standard and Poor's in a weighted scoring system which is then combined with an overlay of Credit Default Swap (CDS) spreads and sovereign ratings. The end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the duration of investments.

68. The Council is alerted to changes to ratings by Link Group's creditworthiness service and takes the following action in respect of updates:

- If a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum criteria, it is withdrawn immediately from further use.
- If a counterparty's credit rating is placed on negative watch or negative outlook, officers carry out a review to determine whether the institution is still worthy of inclusion on the counterparty list. If there is any doubt, the counterparty is temporarily suspended pending the credit rating agency's full review.

69. As part of the creditworthiness methodology a minimum sovereign rating equal to the UK sovereign rating from Fitch (or equivalent from other agencies if Fitch does not provide one) has been determined.

70. In addition to the recommendations from Link Group, the S151 Officer and the Council's Treasury Management Team have agreed to limit the amounts invested with any one country (excluding the UK) or sector as follows:

- No more than 20% of the previous year's average investment balance (to 31st December) with any one counterparty or group or £15 million, whichever is the greater
- Maximum of 10% of total investments to be with institutions in other countries that meet the required criteria.

71. To ensure that the Investment Strategy is not breached and to also be aware of any new opportunities, the Council's counterparty list is reviewed on a daily basis

taking into account market information and changes to the methodology used. The list is maintained by the Treasury Management Team, and reported to the S151 Officer on a regular basis.

72. The Investment Strategy provides delegated authority for the S151 Officer to determine the most appropriate form of investment dependant on prevailing interest rates and counterparty risk at the time.

Specified and Non-Specified investments

73. In approving the Investment Strategy, Members are approving the types of investments the Council can undertake. Investments are classified as either Specified or Non-specified and are shown in more detail in Appendix 1.
74. The Investment Strategy defines a Specified Investment as one that is in sterling, no more than one year in duration or, if in excess of one year can be repaid earlier on request and with counterparties that meet the Council's credit rating criteria. Additionally, once the duration of a Non-specified Investment falls below 365 days, it also falls into the Specified Investment category.
75. Non-specified investments are any other type of investment including pooled investment funds. Whilst generally these investments will earn a higher rate of return they are inherently more risky in nature and therefore limited to either a maximum of 30% (currently £35.9 million) of the previous full year's average monthly investment balance to 31st December, or £30 million, whichever is the greater. The Council currently has £10 million of property investments; £7 million with Lothbury property fund and £3 million with CCLA Investment Management Ltd property fund. A further investment of £10 million has been placed split equally between Fidelity and Artemis multi asset funds.
76. Investments may be arranged in advance and there has been a significant rise in "forward deals" in recent times. Trades arranged up to four weeks in advance of the start date are still classified as Specified Investments provided the duration of the investment from the start date to the maturity is no longer than 364 days. Trade dates are factored into the duration of the investment if arranged more than four weeks in advance because there is an increased risk due to funds being contractually committed.

Ethical Investment Policy

77. The Council adopted an Ethical Investment Policy in 2015/16. No changes are proposed to the policy which is set out below:

The Council will not knowingly invest directly in businesses whose activities and practices pose a risk of serious harm to individuals or groups, or whose activities are inconsistent with the Council's mission and values. This would include, inter alia, avoiding direct investment in institutions with material links to:

- a. Human rights abuse (e.g. child labour, political oppression)
- b. Environmentally harmful activities (e.g. pollutants, destruction of habitat, fossil fuels)
- c. Socially harmful activities (e.g. tobacco, gambling)

There is an Environmental, Social and Governance (ESG) Policy attached at Appendix 3. This will be refined over time as more consistent metrics are developed but it is an important step in raising the consideration of ESG matters, informing investment decisions and offering appropriate challenge where there is room for improvement.

Prudential Indicators

78. The Council is required to set out a number of indicators, relating to the affordability and prudence of its Treasury Strategy. These indicators are detailed in Appendix 2 for the period 2022/23 – 2026/27, and will be monitored and reported on an annual basis.

Other implications

79. Environmental Impact –the inclusion of the Ethical Investment Policy, ensures that, through the Council’s treasury management investments, the Council will not knowingly, directly invest in businesses that undertake harmful environmental activities. In addition, environmental measures are covered in our Environmental, Social and Governance policy in Appendix 3.

Financial implications

80. All financial issues are addressed in the body and appendices of the report. The Council’s assumptions for net investment interest for the General Fund for 2023/24 to 2026/27 are as follows:

	2023/24	2024/25	2025/26	2026/27
	£000's	£000's	£000's	£000's
Interest Payable	11,148	15,949	18,445	21,731
Interest from companies on borrowing	-4,002	-5,325	-6,545	-8,058
Transfer from HRA	-10,745	-14,142	-15,814	-18,501
Treasury management investment interest	-1,793	-1,674	-1,622	-1,611
Net investment interest	-5,392	-5,192	-5,536	-6,439

81. This includes the cost of borrowing, interest from companies and interest from external investments.

Legal issues

82. This report fulfils four key requirements:

- The reporting of the Prudential Indicators setting out the Council’s expected capital activities (as required by the CIPFA Prudential Code for Capital Finance in Local Authorities).
- Agreeing the Council’s Minimum Revenue Provision (MRP) Policy, which sets out how the Council will pay for capital assets through revenue each year.
- Agreeing the Treasury Management Strategy, which links day to day Treasury Management to the Capital Programme and the Treasury Management Prudential Indicators. The key indicator is the Authorised Limit, the maximum amount of debt the Council could afford in the short term, but which would not be sustainable in the longer term. This is the

Affordable Borrowing limit required by Section 3 of the Local Government Act 2003.

- Agreeing the Annual Investment Strategy, this sets out the Council's criteria for choosing investment counterparties and limiting exposure to the risk of loss.

83. The Local Government Act 2003 and supporting regulations require the Council to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set prudential and treasury indicators to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

84. The Council's Constitution requires the Treasury Management Strategy to be reported to the Cabinet on an annual basis outlining the expected treasury activity for the forthcoming four years and for it to be approved by a Council meeting.

Level of risk

85. Risks are managed as set out in this report and appendices.

86. The value of property funds is reliant on the value of the property held by the funds and of multi-asset funds on the value of the assets held by those funds. Property and investment asset values can go down as well as up. The Funds that the Council uses are monitored to ensure that they hold an asset portfolio which will mitigate the risk of specific sectors suffering a loss. The regular returns from property funds are from property rentals so as long as the properties remain tenanted there will be a return. The risk of holding property is also affected by the uncertainty over the UK's exit from the EU and changes in markets, especially retail. The regular returns from multi-asset funds are from income returns which are reliant on the earnings of the underlying assets. Increases and decreases in the value of funds now have to be charged to the revenue account, although there is a statutory mitigation from Government that allows these impacts to be reversed out for the next few years. Returns from the funds are around 4% of the original investment value.

Equalities impact

87. The Council has adopted an ethical investment policy to help reduce the environmental, health and wellbeing impacts that could potentially arise from investments. There are no other equalities impacts relating to this report.

Report author	Bill Lewis
Job title	Financial Accounting Manager
Service area or department	Financial Services
Telephone	01865 252607
e-mail	blewis@oxford.gov.uk

Background Papers: None