Treasury Management Strategy Statement (2023/24)

1 Background

1.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as:

> "The management of the County Council's borrowing, investments and cash flows, including its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

1.2 In accordance with the CIPFA definition, the County Council's treasury management function aims to manage risk. The successful identification, control and monitoring of risk are integral elements to treasury management activities and include credit and counterparty risk, liquidity risk, market and interest rate risk, refinancing risk, and legal and regulatory risk.

1.3 The County Council is required to operate a balanced budget which broadly means cash raised during the year will meet its 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, financial instruments, or externally managed pooled funds which align with the County Council's risk appetite and provide adequate liquidity initially before considering investment return.

1.4 The second main function of the treasury management service is to facilitate the funding of the County Council's capital plans. These capital plans provide a guide to the borrowing need of the authority, essentially the longer term cash flow planning, to ensure the County Council can meet its capital spending obligations. The management of longer term cash may involve the arrangement of long and/or short term loans (external borrowing) or may use longer term cash flow surpluses in lieu of external borrowing (internal borrowing). On occasion, when it is prudent and economic, any external debt previously drawn may be repaid and/or restructured to meet the County Council's risk or cost objectives.

1.5 The contribution the treasury management function makes to the County Council is critical because 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 resulting treasury operations generate interest costs in relation to external debt and income arising from investments, both of which affect the available revenue budget. Furthermore, since cash balances generally arise from the County Council's earmarked reserves and working balances, it remains paramount to ensure adequate security of the sums invested. Any loss of principal will in effect result in a loss to the General Fund Balance.

1.6 The County Council's economic development projects or loans to third parties will also impact on the treasury function. These activities are generally classed as non-treasury investments (usually arising from capital expenditure) and are separate from the day-to-day treasury management activities. Further details are set out in the annual Capital Strategy report (see Section 2).

1.7 During 2023/24, the County Council will need to consider the funding of its Climate Change Strategy and Action Plan to deliver on its commitment. This will be an integral part of part of the Medium Term Financial Strategy and Capital Strategy and will include incorporating Environmental, Social and Governance (ESG) considerations into the Council's treasury management procedures, including loans or investments that support environmentally-friendly activity (green finance options) where appropriate, albeit this is still a developing area of finance.

1.8 The County Council's ongoing commitment to achieving Carbon Net Zero and its Climate Change Strategy will be considered within the Council's Treasury Management Practices (TMPs) as required by the updated Treasury Management Code of Practice (2021 Edition). In accordance with the Code, the County Council plans to undertake a full review of its TMPs in 2023/24, including TMP1 ("Credit and Counterparty Risk Management") which will be updated to incorporate ESG considerations. This review will ensure that actions already taken by the County Council including the adoption of the UK Infrastructure Bank as an approved funding source (paragraph 6.6) and the requirement for approved external pooled fund managers to be signatories to the UN's Principles of Responsible Investment (paragraph 7.45) will be included in TMP1.

1.9 The Treasury Management Strategy complies with the principles and standards of the Financial Management Code, including:

- The County Council's approach towards engaging external professional advisors in delivering the Treasury Management Strategy (Section 4).
- The County Council's approach to debt and borrowing risk management, including projections of external debt and internal borrowing required to support capital expenditure, within its treasury management procedures (Section 6).
- Managing financial sustainability risks through the County Council's annual investment strategy, including its policies for approving counterparties for its investments and related management of cash flow liquidity (Section 7).

2 Reporting Requirements

2.1 CIPFA published the updated Treasury Management and Prudential Codes on 20 December 2021 and stated that revisions need to be included in the reporting framework from the 2023/24 financial year. Going forward therefore, the County Council must have regard to the updated Codes of Practice within both the Capital and Treasury Management Strategies that are reported annually alongside the Budget Report for County Council approval. Furthermore, the County Council must have regard to the Codes in all related treasury management reports during 2023/24.

2.2 The updated Treasury Management Code requires all investments and investment income (both treasury and non-treasury) to be attributed and reported by one of the following three purposes:

(1) **Treasury Management**: Investments arising from the County Council'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, including loans and deposits with the UK Government, local authorities and high credit quality institutions. 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.

(2) **Service Delivery**: Investments held primarily and directly for the delivery of public services including 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 or otherwise incidental to the primary purpose".

(3) **Commercial Return**: Investments held primarily for financial return with no treasury management or direct service provision purpose. Risks on such investments should be proportionate to the County Council's financial capacity. This means that "plausible losses" could be absorbed in budgets or earmarked reserves without unmanageable detriment to local services. Furthermore the updated Codes emphasis that a local authority must not borrow to invest primarily for financial return.

2.3 **Capital Strategy:** CIPFA's Prudential and Treasury Management Codes (2021 Editions) require all local authorities to prepare a separate Capital Strategy report which provides the following:

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

2.4 The purpose of the Capital Strategy is to set out a basis for addressing the competing demands for investment across the County Council, the approach for addressing the gap between aspirations and available resources and the options for identifying alternative sources of funding. The Capital Strategy therefore ensures that all elected members of the County Council fully understand the overall long-term policy objectives, governance procedures and associated risk appetite of all capital investment decisions. Details of the County Council's borrowing needs arising from the capital plans along with associated Prudential Indicators are also set out in the Capital Strategy.

2.5 Non-treasury investments will be reported through the Capital Strategy. This ensures the separation of the core treasury management function for investments made under statutory provisions granted to the County Council under the Local Government Act 2003 (governed by security, liquidity, and yield principles) from the County Council's commercialism policies where investments are usually driven by expenditure on an asset.

2.6 **Treasury Management Reporting:** In accordance with CIPFA's Treasury Management Code of Practice (2021 Edition), the County Council is currently required to receive and approve, as a minimum, three main reports each year, which incorporates a variety of policies, estimates and actuals, including:

(a) The Treasury Management Strategy Statement (TMSS). This sets out how the County Council's investments and borrowings are to be organised; including the annual investment strategy which approves the parameters on how treasury investments are to be managed. Details of the County Council's capital plans (including relevant prudential indicators) and the Minimum Revenue Provision (MRP) policy (how residual capital expenditure is charged to revenue over time) are set out in the County Council's Capital Strategy.

(b) A Mid-Year Treasury Management Report – Updating the County Council with the progress of the capital position, treasury management activity and performance, and whether any policies and/or prudential and treasury indicators require revision. This is delegated to the Performance and Finance Scrutiny Committee in accordance with governance arrangements approved in February 2014. The Regulation, Audit and Accounts Committee will receive quarterly reports on compliance with the treasury management strategy.

(c) An Annual Treasury Management Report – Providing the County Council with a backward-looking review document covering all treasury management activity and performance. This will include details on a basket of actual prudential and treasury indicators as compared against original estimates set out within the strategy agreed in the previous February. Scrutiny of the annual treasury management report is delegated to the Performance and Finance Scrutiny Committee as approved by County Council in July 2018.

2.7 Before recommendation to County Council, the TMSS report receives appropriate scrutiny from the Performance and Finance Scrutiny Committee. In addition, the County Council maintains a Treasury Management Panel comprising the Cabinet Member for Finance and Property and four other elected members. The Panel functions as an advisory body supporting the Director of Finance and Support Services in implementing the County Council's borrowing and investment strategies and reviewing all treasury management reports.

2.8 Treasury management issues reported within the attached 2023/24 TMSS include:

Capital Issues:

- A summary of capital expenditure plans up to 31 March 2028; and
- Associated capital financing plans, including forecasts of the County Council's future borrowing requirement.

Treasury Management Issues:

- Current treasury position (**attached at Appendix A**);
- Treasury indicators which limit the treasury risk and activities of the County Council;

- Prospects for interest rates as provided by the County Council’s treasury management advisor (**attached at Appendix B**);
- The borrowing and repayment strategy;
- Policy on borrowing in advance of need;
- Debt rescheduling;
- The investment strategy;
- Creditworthiness policy; and
- Policy on the use of external service providers.

2.9 These elements cover the requirements of the Local Government Act 2003; CIPFA’s Prudential and Treasury Management Codes; and the Department for Levelling Up, Housing and Communities (DLUHC) Investment Guidance.

3 Training

3.1 CIPFA’s Treasury Management Code requires the Director of Finance and Support Services to ensure that members involved with treasury management receive adequate training. Following County Council elections in May 2021, the training of members with responsibilities for the scrutiny of the County Council’s treasury management policies and activities (including Treasury Management Panel members) was provided by the County Council’s treasury management advisor in June 2021. Further training requirements remain under constant review.

3.2 The training needs of treasury management officers are periodically reviewed as part of staff appraisals and personal development plans and officers attended external training and received relevant internal on-the-job training during the year. Ongoing training options for officers include professional qualifications from CIPFA and other appropriate organisations; attendance at workshops and seminars run by the County Council’s appointed treasury management advisor; and on the job training in line with the approved Treasury Management Practices (TMPs) as provided by the Principal Finance Officer (Treasury Management & Insurance).

3.3 The updated Treasury Management Code requires the County Council to adopt a “formal and comprehensive training policy for the effective acquisition and retention of treasury management knowledge and skills for those responsible for management, delivery, governance and decision making”. A resulting knowledge and skills register will be developed during 2023/24 as part of the Council’s TMPs review (TMP10; “Training and Qualifications). As a minimum the review will cover the following to monitor and review knowledge and skills:

(1) Prepare tailored learning plans for County Council officers and members with treasury management responsibilities, and record attendance at training to ensure action is taken when poor attendance is identified;

(2) Require that County Council officers and members with treasury management responsibilities undertake self-assessment against required competencies (for example, CIPFA’s Better Governance Forum and Treasury Management Network have produced a ‘self-assessment by members responsible for the scrutiny of treasury management’); and

(3) Have regular communication between officers and members encouraging training needs to be highlighted on an ongoing basis (through regular TM Panel meetings).

4 Treasury Management Advisors

4.1 The County Council contracts external providers of treasury management services in order to acquire access to a wide range of specialist skills and resources including:

- Credit advice;
- Investment advice;
- Debt management advice;
- Capital and financial accounting advice; and
- Economic and interest rate forecasting.

4.2 The County Council recognises that the responsibility for all treasury management decisions always remains with the organisation and therefore will ensure that undue reliance is not placed upon its external service providers. Treasury management decisions will be undertaken with regards to all available information including, but not solely, that received from treasury advisors.

4.3 The County Council will ensure that the terms of the appointment of external treasury management advisors and the methods by which their value will be assessed are properly agreed and documented, and subject to regular review. Following a review of services provided, a three year contract with Link Group (Link Treasury Services Ltd) commenced on 1 November 2021; with the County Council having the option to extend for an additional two years following ongoing review of the services provided over the initial contractual period.

4.4 Details of arrangements with specialist advisors contracted by the County Council in relation to the Council’s non-treasury investments would be contained within the Capital Strategy report. To date, there are no specialist advisors in relation to the County Council’s non-treasury investments required.

5 Capital Programme (2023/24 to 2027/28)

5.1 The County Council’s capital expenditure and financing plans as contained within the approved Capital Programme in the Capital Strategy are key drivers of treasury management activity. The output of the Capital Programme is reflected in the County Council’s prudential indicators which are designed to provide an overview and confirm such expenditure and financing plans are both affordable and prudent (included as Annex 2(c)) to the 2023/24 Budget Report).

5.2 Table 1 provides a summary of the County Council’s capital expenditure plans, both those agreed previously and those forming part of the current budget cycle for approval by County Council in February 2023:

Table 1: Capital Expenditure by County Council Service

Capital Expenditure by Service	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m	2026/27 Estimate £'m	2027/28 Est. *(i)* £'m
Adults Services	0.1	0.0	0.9	1.0	0.3	0.0
Children and Young People	1.3	5.4	3.8	1.1	1.7	0.1
Community Support and Fire & Recue	10.3	9.1	7.3	10.2	5.6	3.9
Environment and Climate Change	5.5	12.2	23.9	27.5	25.4	7.6
Finance and Property	8.6	7.4	27.6	29.1	19.7	30.1
Highways and Transport	48.5	48.2	54.3	49.7	33.8	59.5
Leader	7.1	2.7	2.0	2.9	4.7	5.0
Learning and Skills	37.0	34.1	41.9	58.3	29.5	29.4
Support Services and Economic Development	12.1	5.8	12.8	8.1	2.2	1.4
Total Capital Expenditure	**130.5**	**124.9**	**174.5**	**187.9**	**122.9**	**137.0**

(i) 2027/28 estimate includes subsequent years spend.

5.3 Capital expenditure as reported above may be financed from a range of external and internal sources. External sources include private sector contributions (such as s106 developer contributions) as well as government grants. Internal sources include capital receipts, revenue contributions and reserves set aside for capital purposes.

5.4 Borrowing is required to meet the cost of any capital expenditure not financed by internal and/or external funding sources highlighted in paragraph 5.3. Table 2 summarises how the County Council's capital expenditure plans will be financed across the period through to 2027/28, with any funding shortfall resulting in a borrowing requirement:

Table 2: How the Capital Programme will be Financed

Financing the Capital Programme	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m	2026/27 Estimate £'m	2027/28 Estimate £'m
Capital Expenditure	**130.5**	**124.9**	**174.5**	**187.9**	**122.9**	**137.0**
Government Grants	-66.5	-68.7	-29.9	-32.8	-32.1	-28.5
External Contributions	-9.0	-6.5	-8.8	-23.6	-19.2	-37.3

Financing the Capital Programme	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m	2026/27 Estimate £'m	2027/28 Estimate £'m
Capital Receipts	-9.0	-8.0	-5.0	-1.0	-6.5	-1.0
Revenue Funding	-3.0	-1.1	-6.9	-7.1	-4.0	-0.9
Financing (Excl. Borrowing)	**-87.5**	**-84.3**	**-50.6**	**-64.5**	**-61.8**	**-67.7**
Borrowing (Core)	-34.5	-28.1	-101.2	-101.8	-50.4	-56.1
Borrowing (Economic Developments)	-8.5	-12.5	-22.7	-21.6	-10.7	-13.2
Total Financing	**-130.5**	**-124.9**	**-174.5**	**-187.9**	**-122.9**	**-137.0**

5.5 Table 2 excludes other long-term liabilities, such as existing PFI schemes (Crawley Schools; Street Lighting and Waste Management) and leasing arrangements which already include borrowing instruments within their contractual terms; and therefore means the County Council is not required to separately borrow for them.

6 Borrowing and Repayment Strategy

6.1 The capital expenditure plans set out in Table 1 (Section 5) provide details of the service activity of the County Council. The treasury management function ensures that cash is organised in accordance with the relevant professional codes and sufficient cash is available to meet service activity and the County 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.

6.2 The key objective of the County Council's current borrowing strategy is to ensure that all future external debt (including forward-starting borrowing and borrowing in advance of need when considered appropriate) is affordable within revenue budget constraints. The County Council will therefore ensure that due diligence is given to both the affordability of such debt and future plans regarding the repayment of debt. This will include consideration of the agreed terms and conditions of any new debt; including 'annuity' and 'equal instalments of principal' loan structures. The timing of when to arrange new debt is governed by the County Council's long-term cash flow forecasts as detailed in capital plans through to 2027/28 and as set out in the County Council's Liability Benchmark Prudential Indicator (Figure 1; paragraph 6.16).

6.3 In accordance with CIPFA's Codes of Practice, decisions on new debt arrangements and repayment of existing debt will include an appraisal of the possible use of capital receipts and/or proceeds from the sale of long-term commercial investments (including long-term externally managed pooled funds) should this be the most financially viable option as the approved funding source.

6.4 The borrowing and repayment strategy therefore set outs the County Council's current and projected debt positions, together with the following prudential and treasury indicators:

- Capital Financing Requirement;
- Liability Benchmark (new in 2023/24);
- The Operational Boundary and Authorised Borrowing Limit; and
- The maturity structure of existing debt.

6.5 **Approved Funding Sources:** The County Council's primary objective when borrowing money is to strike an appropriate level of risk between securing low interest borrowing costs whilst achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the County Council's long-term capital plans change is a secondary objective.

6.6 There is no counterparty risk associated with borrowing, except that associated with money laundering. In conjunction with advice received from its treasury management advisor the County Council will keep under review the following fixed or variable rate long-term and short-term (in lieu of long-term) borrowing options as sources of finance for the approved capital programme, including:

- Borrowing against internal resources held by the County Council (including usable reserves and working capital) in lieu of external borrowing;
- Public Works Loan Board (PWLB) and any successor body;
- Borrowing from the UK Infrastructure Bank;
- Borrowing from other UK local authorities (particularly regarding borrowing for Economic Developments on a short-term basis);
- Borrowing from the money markets (institutional lenders authorised by the Prudential Regulation Authority and/or the Financial Conduct Authority to operate in the UK);
- Borrowing from multilateral development banks; and
- Borrowing from the UK Municipal Bond Agency plc and/or other special purpose companies created to enable local authority bond issue.

6.7 The County Council has previously relied on the PWLB as its only source of funding, with approved alternative market borrowing options (including forward starting loans and bond issuance via the UK Municipal Bond Agency) being held under consideration. The Director of Finance and Support Services will continue to assess the benefits of approved market loan alternatives during 2023/24. Capital finance may additionally be raised by other methods that are not borrowing but may be classed as other debt liabilities (including leasing).

6.8 In accordance with the updated Prudential and Treasury Management Codes, together with the outcomes of HM Treasury's PWLB review during 2020/21 (aiming to ensure that local authorities invest public funds in infrastructure and front-line services only) all **new** PWLB borrowing will be conditional on the County Council demonstrating that over the period of the capital programme there will be no intention to buy investment assets primarily for yield (for example the purchase of investment property) irrespective of whether the transaction would be financed from a source other than the PWLB. Investment assets can, however, still be purchased without affecting the ability to borrow from the PWLB, if there is a demonstrable economic benefit to the County. The County Council confirms that capital plans have been reviewed and are compliant with these PWLB requirements.

6.9 **Current Portfolio Position:** On 31 December 2022 the County Council had external loans with the PWLB totalling £461.3m. In accordance with the approved 2022/23 Treasury Management Strategy no new external borrowing was arranged during the period April to December 2022; £10m (plus interest) was however repaid to the PWLB on maturity of a 20-year loan taken by the County Council in 2002. Cash supporting the County Council's usable reserves and working capital was therefore used as a temporary funding measure in lieu of external borrowing. Consequently, the County Council's internal borrowing at the end of 2022/23 is forecast to be £61.9m (£21.3m on 31 March 2022) as set out in Table 7 (paragraph 6.19).

6.10 Capital plans (Table 2; paragraph 5.4) highlight that a borrowing requirement of £40.6m is required to finance the County Council's capital expenditure in 2023/24; of which £12.5m relates to economic development projects.

6.11 **Capital Financing Requirement**: In accordance with CIPFA's Prudential Code, the County Council's underlying borrowing need (essentially a measure of the Council's indebtedness) is represented by its Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been financed from either revenue or capital resources, for example government grants, s106 developer contributions and capital receipts. Any capital expenditure (Table 1; paragraph 5.2) which is not immediately financed through a revenue and/or capital resource will increase the County Council's CFR. Additionally, the CFR includes any other long-term liabilities which include borrowing instruments within their contractual terms (including PFI schemes and finance leases).

6.12 The County Council's CFR does not increase indefinitely however; capital expenditure financed through debt is subject to a minimum revenue provision charge (the Minimum Revenue Policy) which is set out in the Capital Strategy. MRP is a statutory annual revenue charge which broadly reduces the Council's indebtedness in line with each asset life, and so charges the economic consumption of capital assets as they are used. The County Council's resulting CFR projections are set-out below:

Table 3: The Capital Financing Requirement (CFR) to 2027/28

Balance Sheet Projections (on 31 March)	**2022/23 Estimate £'m**	**2023/24 Estimate £'m**	**2024/25 Estimate £'m**	**2025/26 Estimate £'m**	**2026/27 Estimate £'m**	**2027/28 Estimate £'m**
CFR (Core Borrowing)	527.3	539.8	624.4	707.2	731.2	764.6
CFR (Economic Developments)	86.5	97.2	117.9	137.2	150.8	160.9
Capital Financing Requirement	**613.8**	**637.0**	**742.3**	**844.4**	**882.0**	**925.5**

6.13 **Liability Benchmark**: As per the requirements of the updated Prudential and Treasury Management Code of Practice, the Liability Benchmark is a new CIPFA Prudential Indicator for 2023/24. The Director of Finance and Support Services uses the Liability Benchmark to forecast the minimum amount of debt the County Council could hold if all available internal resources (excluding those set aside for long-term treasury management investment) are used in lieu of external borrowing. The resulting Liability Benchmark therefore assists the County Council's long-term borrowing strategy by forecasting the future timing of when external borrowing is required to fund approved capital plans.

6.14 The County Council has been making use of its Liability Benchmark for a number of years, but without formally reporting the benchmark within annually approved treasury management strategies. The three main components of the Liability benchmark include:

(1) **Existing loan debt outstanding** - The profile of the County Council's maturing PWLB and short-term borrowing, which is money held and invested on behalf of the Chichester Harbour Conservancy (CHC) and its associated charities and is repayable to CHC on any given notice, is set out in Table 4 below:

Table 4: Existing loan debt outstanding

Balance Sheet Projections (on 31 March)	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m	2026/27 Estimate £'m	2027/28 Estimate £'m
Existing Borrowing Profile (PWLB)	461.3	461.3	461.3	437.2	432.5	386.4
Short-Term Borrowing	5.5	5.5	5.5	5.5	5.5	5.5
External Borrowing	**466.8**	**466.8**	**466.8**	**442.7**	**438.0**	**391.9**

(2) **County Council's Loans CFR** - The County Council's projected Capital Financing Requirement (Table 3; paragraph 6.12); including future prudential borrowing and planned MRP but excluding the Council's long-term PFI/finance lease liabilities as set out in Table 5 below:

Table 5: County Council's Loans CFR

Balance Sheet Projections (on 31 March)	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m	2026/27 Estimate £'m	2027/28 Estimate £'m
Capital Financing Requirement	613.8	637.0	742.3	844.4	882.0	925.5
Less: PFI Schemes and Leases	-85.1	-81.5	-77.6	-73.1	-68.0	-62.2
Loans CFR	**528.7**	**555.5**	**664.7**	**771.3**	**814.0**	**863.3**

(3) **Liability Benchmark (Net Loans Requirement)** – The County Council's future projections of gross borrowing (Loans CFR) less cash balances available for treasury management investment (including usable reserves, capital contributions received in advance and working capital); excluding balances set aside for long-term treasury management investment, as set out in Table 6 below:

Table 6: Liability Benchmark (Net Loans Requirement)

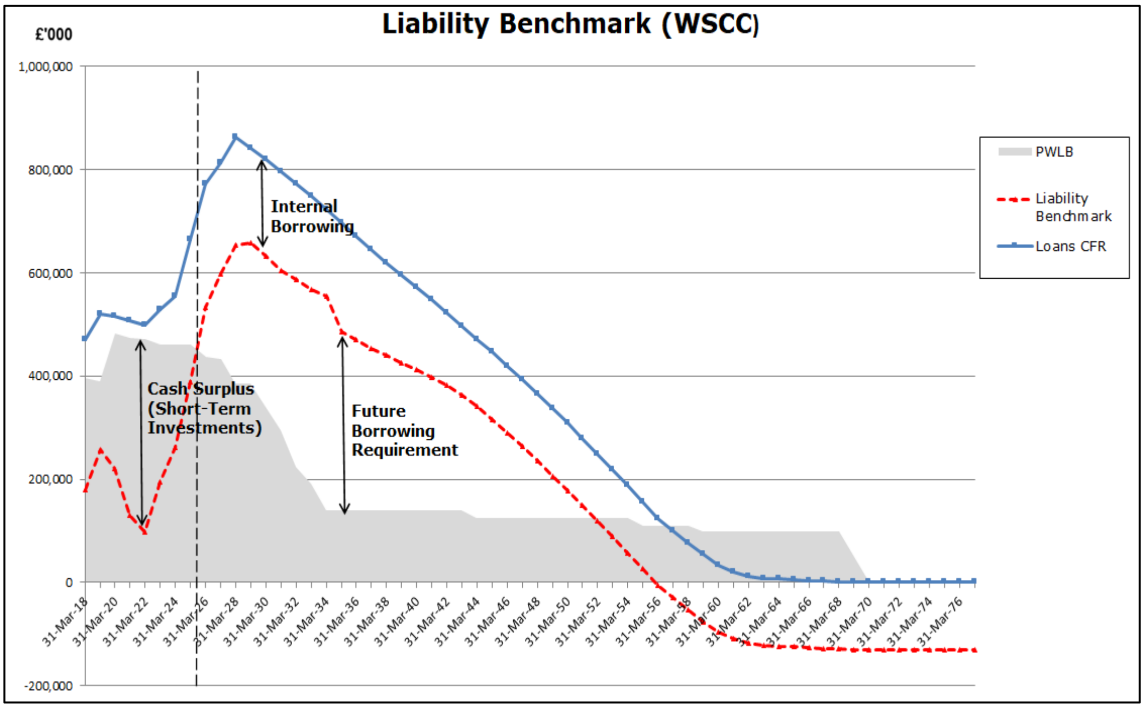
Balance Sheet Projections (on 31 March)	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m	2026/27 Estimate £'m	2027/28 Estimate £'m
Gross Borrowing (Loans CFR)	528.7	555.5	664.7	771.3	814.0	863.3
Usable Reserves	-239.7	-239.1	-198.7	-184.2	-181.3	-178.6
Capital Contributions (s106 Receipts)	-95.4	-89.0	-80.1	-56.5	-37.3	-33.2
Working Capital	-50.4	-18.4	-50.0	-50.0	-50.0	-50.0
Net Loans Requirement	**143.2**	**209.0**	**335.9**	**480.6**	**545.4**	**601.5**
Funding required for investments > one year *(i)*	52.0	52.0	52.0	52.0	52.0	52.0
Liability Benchmark	**195.2**	**261.0**	**387.9**	**532.6**	**597.4**	**653.5**

(i) Whilst the Annual Investment Strategy approves long-term treasury management investments up to a maximum of £100m (Table 17; paragraph 7.52), the Liability Benchmark is shown on the basis of no additional long-term investments over and above amounts originally invested in existing externally managed pooled funds.

6.15 Working capital balances are estimated and based on a series of assumptions and may therefore be higher during each financial year than shown above (Table 6). Following a review of these assumptions, working capital now include forecasts of the Dedicated Schools Grant (DSG) deficit reserve balance which is predicted to be £65m by the end of March 2024. The initial three year statutory override to March 2023 that allowed the County Council to hold the deficit balance as an unusable reserve has been extended to March 2026 which means that the DSG deficit can continue to be held as an unusable reserve and therefore does not impact on the balance sheet. However, any balance held in unusable reserves impacts the Council's cash flow and this deficit does equate to a potential loss of £54m in average cash balances in 2023/24 which is a loss of investment income of £2.2m. For 2024/25 onwards, no assumptions on the levels of the DSG deficit have been included in the working capital calculations given future funding arrangements remain unclear. Until funding arrangements are finalised there is a risk that the working capital estimates from 2024/25 are overstated which may have an impact of decreasing the County Council's future cash balances and bringing forward the timing of external borrowing.

6.16 The resulting Liability Benchmark is shown below with no assumptions of subsequent prudential borrowing required to fund ongoing capital plans after the approved 5-year capital programme (to 2027/28).

Figure 1: The Liability Benchmark



6.17 Under the County Council's updated Liability Benchmark projections, it is now forecast that the Council will be required to externally borrow in 2025/26 (previously 2023/24 as per the approved 2022/23 Treasury Management Strategy); that being the point at which the Liability Benchmark exceeds the level of maturing PWLB debt as shown above.

6.18 **Internal Borrowing**: In December 2010, County Council took a decision to introduce an internal borrowing strategy whereby the Council's capital borrowing need is not fully funded by external debt, but rather cash supporting the Council's usable reserves and working capital have been used as a temporary funding measure in lieu of external borrowing. As set-out in the County Council's Liability Benchmark the continuation of an internal borrowing strategy in 2023/24 remains prudent; however the continued benefits will be regularly monitored against future interest rate forecasts (**Appendix B**) and the resulting costs of deferring external borrowing into future years.

6.19 An analysis of the County Council's actual external debt projections (including PFI and Finance Lease liabilities), internal borrowing projections and internal borrowing as a percentage of the CFR, are summarised in Table 7 below.

Table 7: External Debt and Internal Borrowing Projections to 2027/28

Debt Projections	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m	2026/27 Estimate £'m	2027/28 Estimate £'m
Gross External Debt (1-April)	**565.6**	**551.9**	**548.3**	**544.4**	**605.7**	**665.4**
Repayment of Existing Debt	-10.0	0.0	0.0	-24.1	-4.7	-46.1
Chichester Harbour Conservancy Movement	-0.5	0.0	0.0	0.0	0.0	0.0
External Debt Core Borrowing	0.0	0.0	0.0	0.0	8.6	92.2
External Debt Economic Developments	0.0	0.0	0.0	89.9	60.9	10.1
PFI/Finance Lease Movement	-3.2	-3.6	-3.9	-4.5	-5.1	-5.8
Gross External Debt (31-Mar)	**551.9**	**548.3**	**544.4**	**605.7**	**665.4**	**715.8**
Cumulative Internal Borrowing (on 31 March)	61.9	88.7	197.9	238.7	216.6	209.7
Capital Financing Requirement	**613.8**	**637.0**	**742.3**	**844.4**	**882.0**	**925.5**
Internal Borrowing (%)	**10.1%**	**13.9%**	**26.7%**	**28.3%**	**24.6%**	**22.7%**

6.20 **Revenue Impact:** The revenue impact (capital financing cost as a percentage of net revenue streams) of the recommended borrowing strategy relating to the County Council's capital programme (excluding service funded Economic Developments, PFI schemes and Finance Leases) is outlined below:

Table 8: Revenue Impact of the Recommended Borrowing Strategy

	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m	2026/27 Estimate £'m	2027/28 Estimate £'m
Net Revenue Expenditure	648.3	708.8	728.2	732.0	739.0	754.0
Capital Financing Charges	29.7	30.4	30.5	34.4	36.6	39.5
% Ratio	**4.6%**	**4.3%**	**4.2%**	**4.7%**	**4.9%**	**5.2%**

6.21 In accordance with this recommended borrowing strategy, including the County Council's current approach to internal borrowing (paragraph 6.18), the County Council forecasts that the costs of long-term external borrowing (interest charges) in 2023/24 will be:

- PWLB Borrowing: £18.8m (£19.0m in 2022/23); of which £1.3m will be service funded from economic development schemes.
- PFI schemes and finance leases: £10.5m (£10.8m in 2022/23)

6.22 **Borrowing in Advance of Need:** Any decision to borrow in advance will be within forward approved CFR estimates and arranged at times that take advantage of favourable borrowing rates (as per forward-looking interest rate forecasts provided by Link Group) thereby ensuring that value for money can be demonstrated; and that the County 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 quarterly compliance reports (and annual report to the Performance and Finance Scrutiny Committee).

6.23 The Authorised Borrowing Limit (Table 10; paragraph 6.27) constrains borrowing in advance of future capital need by limiting such borrowing to within CFR estimates over a three-year planning period, therefore confirming that it is not being taken for revenue profit (investment of the extra sums borrowed) or speculative purposes.

6.24 **Limits to Borrowing Activity:** Within the prudential indicators there are several key indicators to ensure that the County Council operates its activities within well-defined limits. These indicators ensure that the County Council's gross external debt does not, except in the short-term, exceed the total of the CFR in the preceding year plus estimates for any additional CFR for 2023/24 and the following two financial years. Based on the gross external debt projections (Table 7; paragraph 6.19) the Director of Finance and Support Services reports that the County Council complied with these prudential indicators in 2022/23 and does not envisage any non-compliance over the period of the capital programme.

6.25 The 'Operational Boundary' is the limit (Prudential Indicator) beyond which external debt is not normally expected to exceed, as set out below:

Table 9: The Operational Boundary Limit (Prudential Indicator)

Operational Boundary	**2022/23 Estimate £'m**	**2023/24 Estimate £'m**	**2024/25 Estimate £'m**	**2025/26 Estimate £'m**	**2026/27 Estimate £'m**	**2027/28 Estimate £'m**
External Debt (including CHC)	466.8	466.8	466.8	442.7	446.6	492.7
Economic Developments	0.0	0.0	0.0	89.9	150.8	160.9
PFI Schemes/ Finance Leases	85.1	81.5	77.6	73.1	68.0	62.2
Operational Boundary	**551.9**	**548.3**	**544.4**	**605.7**	**665.4**	**715.8**

6.26 The 'Authorised Borrowing Limit' is a further key Prudential Indicator that reports the maximum level of borrowing. This represents the limit beyond which external debt (including overdrawn bank balances and short-term borrowing undertaken for unexpected cash flow movements) is prohibited, as approved by County Council. It reflects the level of external debt which, whilst not desired, could be afforded in the short-term (e.g. when borrowing in advance of capital need) but is not desirable in the long term.

6.27 This limit is a statutory limit determined under Section 3(1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans or those of a specific council; although to-date this power has not yet been exercised.

Table 10: The Authorised Borrowing Limit (Prudential Indicator)

Authorised Borrowing Limit	**2022/23 Estimate £'m**	**2023/24 Estimate £'m**	**2024/25 Estimate £'m**	**2025/26 Estimate £'m**	**2026/27 Estimate £'m**	**2027/28 Estimate £'m**
Gross Debt *(i)*	659.6	564.2	627.8	682.7	687.8	693.6
PFI Schemes/ Finance Leases	85.1	81.5	77.6	73.1	68.0	62.2
Authorised Borrowing Limit *(ii)*	**744.7**	**645.7**	**705.4**	**755.8**	**755.8**	**755.8**

(i) Gross debt estimates allow for external borrowing in advance of need for up to a maximum of two years; furthermore, gross debt includes additional headroom (£40m) for unexpected cash flow movements. For example, the 'Authorised Borrowing Limit' for 2023/24 (£645.7m) equals the maximum external debt forecast in any one financial year over a three year period (i.e. the 'Operational Boundary' over the period 2023/24 to 2025/26; therefore £605.7m for 2025/26) plus £40m.

(ii) The 2022/23 Authorised Borrowing Limit remains as approved by County Council in February 2022.

6.28 In addition, the 'Maturity Structure of External Borrowing' Treasury Indicator are limits that highlight the existence of any large concentrations of external debt needing to be replaced at times of uncertainty over interest rates, and is designed to protect against excessive exposures to interest rate changes in any one period, in particular over the course of the next ten years. It is calculated as the amount of projected debt that is maturing in each period as a percentage of total projected external debt. The maturity period of borrowing is determined by reference to the earliest date on which the lender can require payment.

6.29 The upper and lower limits for the maturity structure of external debt in 2023/24 (with actual split as of 31 December 2022 included for comparison) are set out below:

Table 11: Debt Maturity (Prudential Indicator)

Debt Maturity	Actual 31/12/22	Lower Limit 2023/24	Upper Limit 2023/24
Over 30 Years	27%	0%	50%
Over 25 to 30 Years	0%	0%	25%
Over 20 to 25 Years	3%	0%	25%
Over 15 to 20 Years	0%	0%	25%
Over 10 to 15 Years	14%	0%	50%
Over 5 to 10 Years	41%	0%	60%
Over 1 to 5 Years	14%	0%	35%
Under 12 Months	1%	0%	25%

6.30 **Borrowing for Cash-flow Purposes:** The County Council continues to approve the use of short-term loans (normally for up to one to three months) to cover unexpected cash-flow shortages. Short-term borrowing for cash-flow purposes, up to a maximum of £40m, will be limited to the following external funding sources:

(1) Borrowing from other UK local authorities (excluding Police and Crime Commissioners, Fire Authorities and Local Authority Pension Funds);
(2) Borrowing from the money markets (financial institutions authorised by the Prudential Regulation Authority to operate in the UK).

6.31 Additionally, the County Council holds and invests money on behalf of third parties including the Chichester Harbour Conservancy and its associated charities. The County Council reports any such money as short-term borrowing given the requirement that it is available for repayment at any future point in time.

6.32 **Debt Rescheduling:** Rescheduling of current borrowing in the County Council's debt portfolio is unlikely to occur as there remains a large difference between PWLB premature redemption rates and new borrowing rates. However, if any repayment or rescheduling of existing PWLB debt was approved the rationale would be one or more of the following:

(1) The generation of cash savings and/or discounted cash flow savings;
(2) Helping to fulfil the treasury management strategy;
(3) Enhancing the balance of the debt portfolio (amending the maturity profile and/or the balance of volatility).

6.33 **Reporting:** All borrowing and rescheduling activity will be reported to the Performance and Finance Scrutiny Committee (within the Mid-Year Review and/or Annual Treasury Management reports); and to the Regulation, Audit and Accounts Committee and Treasury Management Panel within the prescribed compliance reports.

7 Annual Investment Strategy (Treasury Investments)

7.1 CIPFA and the DLUHC have extended the meaning of 'investments' to include both financial and non-financial investments. This section deals solely with treasury (financial) investments, as managed by the County Council's Treasury Management Team. Non-treasury investments are dealt with in the separate Capital Strategy report.

7.2 The County Council's main treasury management activity continues to be the investment of its surplus funds, representing income received in advance of expenditure plus balances and reserves held. All treasury investments are made under statutory provisions granted to the County Council by the Local Government Act 2003 (Section 12; 'Power to Invest').

7.3 The Director of Finance and Support Services, in consultation with the Cabinet Member for Finance and Property and the Treasury Management Panel, recommends that a continuation of the existing investment strategy be approved in 2023/24; subject to the following changes.

(1) Revisions as required by the updated Treasury Management Code of Practice (2021 Edition); in particular the reporting of externally managed pooled funds and loans to third parties as commercial investments.

(2) The inclusion of Link Group's Agency Treasury Services in the list of approved money market brokers; potentially to be used for the arrangement of short-term deposits with approved financial institutions for the County Council's treasury management investment. Additionally, this would give the Council access to a UK bank offering a deposit that meet the ESG principles.

7.4 On 31 December 2022 the County Council's investments amounted to £402.6m (**Appendix A**). During the remainder of 2022/23 the County Council's average investment balance is forecast to average at around £435m, higher than the original £375m forecast due to capital and revenue funding received ahead of actual spend (including s106 developer contributions received in advance of capital spend) and is currently forecast to average at around £340m throughout 2023/24.

7.5 The County Council's investment policy has regard to the CIPFA Treasury Management Code of Practice and DLUHC's Guidance on Local Government Investments; as such the investment priorities will be the security first, portfolio liquidity second and then investment return ('SLY' investment principles). Accordingly, the County Council will look to strike an appropriate balance between risks and return; minimising the risk of incurring losses from defaults against the risk of receiving unsuitably low investment income.

7.6 In accordance with the CIPFA and DLUHC guidance, and in order to minimise the risk to investments, the County Council applies minimum acceptable credit criteria in order to generate a list of high creditworthy counterparties which also enables diversification and thus avoidance of concentration risks. In assessing credit ratings (as provided by Link Group) the County Council employs the 'Lowest Common Denominator (LCD)' approach, meaning that it uses the lowest rating of those published by Fitch Ratings Ltd, Moody's Investors Service Ltd or Standard & Poor's.

7.7 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 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 markets. To achieve this consideration the County Council will engage with its treasury management advisors to maintain a monitor on market pricing such as 'credit default swaps' and overlay that information on top of credit ratings.

7.8 Other information sources used will include the financial press, share price and other such information pertaining to institutions (banks, corporates etc.) in order to establish the most robust scrutiny process on the suitability of potential investment counterparties. The County Council continues to remain alert for any signs of credit or market distress that might adversely affect its treasury management activities and corrective action will be taken when deemed appropriate to ensure the security of the total investment portfolio.

7.9 Accordingly, the Director of Finance and Support Services will comply with the following policies when investing funds, whether directly or via the London money market. Investments arranged via the London money market will be made through approved brokers. The list of approved brokers in 2023/24 comprises:

(1) BGC Partners (including Martin Brokers)
(2) Imperial Treasury Services
(3) Institutional Cash Distributors (ICD) Ltd
(4) King and Shaxson Limited
(5) Link Group's Agency Treasury Services
(6) Tradition (UK) Limited
(7) TP ICAP Group (including ICAP and Tullett Prebon Europe Ltd)

7.10 **Creditworthiness Policy:** The primary objective governing the County Council's investment criteria is the security of its investments, although the yield or investment return is also a key consideration (paragraph 7.5). After this objective the County Council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in and the criteria for choosing investment counterparties with adequate security (including monitoring their security); and

- It has sufficient liquidity in its investments. For this purpose, it will set out procedures for determining maximum periods for which funds may prudently be committed. These procedures also apply to the County Council's prudential indicators covering the maximum principal sums invested.

7.11 The credit risks associated with making unsecured bank deposits remain evident (due to bail-in legislation) relative to the risks of other investment options available to the County Council (including bank secured, local authority and non-bank corporate deposits). In addition to the risks associated with bail-in, the largest UK banks (those with more than £25bn of retail/Small and Medium-sized Enterprise (SME) deposits) are required by UK law to separate core retail banking services from their investment and international banking activities; this being known as 'ring-fencing'.

7.12 Ring-fencing is a regulatory initiative created in response to the global financial crisis to improve the resilience and resolvability of banks by changing their structure. In general, simpler activities offered from within a ring-fenced bank will be focused on lower risk, day-to-day core transactions; whilst more complex and 'riskier' activities are required to be housed in a separate non-ring-fenced bank. This is intended to ensure that an entity's core activities are not adversely affected by the acts or omissions of other members of its group. Smaller banks with less than £25bn in deposits are exempt from ring-fencing, however they can choose to opt-up.

7.13 While the structure of the banks included within the ring-fencing process may have changed, the fundamentals of credit assessment have not. The probability of a bail-in of a ring-fenced bank is smaller than a non-ring-fenced entity from the same banking group; but the loss incurred as a result of a bail-in would likely be higher. This is because retail (ring-fenced) banks will typically have more capital to protect against losses, but fewer wholesale deposits and senior unsecured creditors to share losses with. The County Council will continue to assess ring-fenced and non-ring-fenced banks in the same way that it does for other financial institutions. Those with sufficiently high ratings (and other credit metrics considered, paragraphs 7.7 and 7.8) will be considered for investment purposes.

7.14 On 31 December 2022, 64.8% of the County Council's internally managed investment portfolio (excluding commercial investments) is invested in short-term unsecured bank deposits and short-term money market funds in accordance with the policies as contained within the 2022/23 TMSS. The Director of Finance and Support Services confirms that the County Council will not be holding any investment on 31 March 2023 that will be in breach of the recommended 2023/24 strategy.

7.15 Under DLUHC Investment Guidance investments are categorised as either '**Specified**', '**Non Specified**' (both categories being approved as suitable for Council's treasury investment) or '**Loans**'. Specified investments are designed to offer high security and high liquidity, with the minimum of formalities. The DLUHC Guidance defines specified investments as those:

(1) Denominated in Sterling;
(2) With a maximum maturity of one year (365 days);
(3) Not defined as capital expenditure by legislation; and
(4) Invested with one of:
- The UK Government (including Gilts, Treasury Bills and DMADF).
- A local authority in England, Wales, Scotland, or Northern Ireland.
- An institution or investment scheme of 'high credit quality'.
- Supranational Institutions (e.g. The European Investment Bank).

7.16 For investments to be regarded as specified, the County Council defines 'high credit quality' as institutions and securities meeting the following criteria:

(a) UK Institutions (Banks, Building Societies and Corporates): Minimum long-term credit rating of **A-**; rated by at least two of the three rating agencies; Fitch, Moody's and Standard & Poor's (S&P).

(b) Non-UK Institutions (Banks and Corporates): Minimum long-term credit rating of **A-**; rated by at least two of the three rating agencies (Country holding a sovereign rating of at least **AA+**).

(c) Money Market Funds: Assigned a **AAA** credit rating; rated by at least two of the three rating agencies and holding assets exceeding £1bn. The County Council approves the use of Money Market Funds that operate under a Constant Net Asset Valuation (funds that invest exclusively in government securities) or operate under a Low Volatility and/or Variable Net Asset Valuation (all other short-term liquidity funds).

(d) UK Local Authorities: Assumed rating aligned with the prevailing UK sovereign rating (**AA-** as of 31 December 2022) unless an actual credit rating exists from any of the three rating agencies.

(e) UK Registered Social Landlords (formerly Housing Associations): Minimum long-term credit rating of **A-**; rated by at least one of the three rating agencies.

(f) Externally Managed Pooled Funds: Assigned a **AAA** credit rating; rated by at least one of the three rating agencies.

7.17 Any investment not meeting the 'Specified' investment criteria listed above will be treated as if it were unrated (classified as 'Non-Specified' investment). For secured investments the credit rating relevant to the specific investment (covered bonds) or underlying collateral (reverse repurchase agreements) will be used as opposed to the individual rating of the bank/building society issuing the security.

7.18 **Monitoring Credit Quality:** Credit rating information is supplied by Link Group (the County Council's treasury advisor) on all active counterparties that comply with the criteria listed above. Any counterparty failing to meet the criteria will be omitted from the counterparty (dealing) list. Any rating changes, rating 'watches' (notification of a likely change) or rating 'outlooks' (notification of the longer term bias outside the central rating view) are provided to officers almost immediately after they occur and this information is considered before actual dealing arrangements. Where an institution has its credit rating downgraded so that it fails to meet any of the approved investment criteria then:

(1) No new investments will be made after the date of notification;
(2) Any existing investments that can be immediately recalled or sold at no cost (financial penalty) will be;
(3) Full consideration will be given to the recall or sale of all other existing investments with the affected counterparty; and
(4) Details will be reported to the Director of Finance and Support Services, the Cabinet Member for Finance and Property and Treasury Management Panel members.

7.19 Where an institution is placed on negative rating watch (notification of a possible rating downgrade) the reasons for the rating action will be evaluated. Unless there is sufficient cushion to absorb a two-notch downgrade to the long-term credit rating (to remain at or above the County Council's minimum approved rating criteria) then decisions on new investments will be subject to approval by the Director of Finance and Support Services. This policy will not apply to negative 'outlooks', which indicate a longer term view rather than an imminent change to an institution's rating.

7.20 If an institution is placed on negative rating watch and is at (or likely to fall below) the County Council's minimum rating criteria then no investments will be arranged until the outcome of the review is announced. The Council's policy for existing investments with such institutions is set out in paragraph 7.18(2). Again, this policy will not apply to negative 'outlooks'. The County Council will however regularly monitor the institutions' ratings reflecting advice received from the Council's treasury management advisor.

7.21 Additional requirements under the CIPFA Treasury Management Code require the County Council to supplement credit rating information. Whilst the above policies rely primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use; additional market information (see paragraphs 7.7 and 7.8) will be applied before making any specific investment decisions from the approved pool of counterparties. This additional market information will be applied to compare the relative security of differing investment opportunities.

7.22 The Director of Finance and Support Services and the County Council's treasury management advisor will continue to analyse and monitor market indicators and credit developments on a regular basis and respond as necessary to ensure the security of the capital sums invested. No investments will be made with an organisation if there are substantive concerns about its credit quality, even though it may meet the approved minimum credit rating criteria (as set out in paragraphs 7.16 and 7.25).

7.23 **Liquidity Management:** The County Council uses purpose-built short-term cash flow forecasting software (currently SAP Treasury Management Module) to determine the maximum period for which funds may prudently be invested. The County Council is however planning to undertake a procurement exercise to replace the existing treasury management system in 2023 as part of the SAP replacement project. It is therefore expected that new cash flow forecasting software will be operational by the end of 2023/24.

7.24 Cash flow forecasts are made on a prudent basis with income under-estimated and expenditure over-estimated. Additionally, the County Council seeks to maintain a rolling profile of maturing investments, allowing it to cover unexpected items of expenditure and to react to favourable market conditions as they arise. Monetary limits on long-term investments are set by reference to the County Council's Medium Term Financial Strategy (MTFS) and long-term forecasts of usable reserve balances. The County Council also has access to a number of money market funds where cash is deposited at prevailing overnight interest rates and can be withdrawn without notice; these funds are therefore highly liquid.

7.25 **Investment Policy:** The Director of Finance and Support Services will undertake the most appropriate form of investments in keeping with the approved strategy objectives, income and risk management requirements and the County Council's Treasury Indicators. Accordingly the County Council may invest its surplus funds over a range of maturity periods with any of the approved counterparty types listed below, subject to maximum monetary and duration limits (covering both 'Specified' and 'Non-Specified' investments) as shown, to ensure that prudent diversification of the investment portfolio is achieved:

Table 12: Unsecured Bank Deposit Limits

Credit Rating	**Cash Limit *(i)***	**Time Limit *(i)***
AAA	£15m	2 Years
AA+	£15m	1 Year
AA	£15m	1 Year
AA-	£15m	1 Year
A+	£15m	1 Year
A	£15m	6 Months
A-	£15m	100 Day
NatWest Banking Group: Ring Fenced Bank only	£15m	1 Year
Money Market Funds	£25m *(ii)*	Overnight
BBB+ (or below)	No Approval	No Approval

(i) *Maximum exposure limits (monetary and time) approved per individual financial institution holding an applicable credit rating.*

(ii) *Maximum monetary limits per fund approved as £25m or 0.5% of the fund's total assets under management (AUM), whichever is lower.*

Table 13: Other Internally Managed Investment Limits (including Bank Secured, Government Issues, UK Local Authorities and Non-Bank)

Institution/ Issue Credit Rating	**Cash Limit *(iii)***	**Time Limit *(iii)***
UK Government	Unlimited	50 Years
Local Authorities	£25m	20 Years
AAA	£25m	10 Years
AA+	£25m	5 Years
AA	£25m	4 Years
AA-	£25m	3 Years
A+	£15m	2 Years
A	£15m	1 Year
A-	£15m	6 Months
BBB+	£10m	100 Days
Money Market Funds	£25m *(iv)*	Overnight
Housing Associations (rated A- or higher)	£15m	5 Years
BBB (or below)	No Approval	No Approval

(iii) *Maximum exposure limits (monetary and time) approved per individual Local Authority, Housing Association, financial institution (secured bond) and applicably rated non-financial institution.*

(iv) *Maximum monetary limits per fund that invest in government securities only approved as £25m or 2% of the fund's total assets under management (AUM), whichever is lower.*

Table 14: Externally Managed Investment Limits

Externally Managed	Cash Limit	Time Limit
Pooled Funds	See Note *(v)*	No Defined Maturity. Withdrawals made on: - Liquidity requirements - Fund performance

(v) Maximum monetary limits for externally managed pooled funds (including ultra-short dated bond, multi-asset income and property funds) will be approved as £25m (AAA rated funds), £15m (all other funds) or 5% of the fund's total assets under management (AUM), whichever is lower.

7.26 **Investments categorised as "Treasury"**: In accordance with the CIPFA Treasury Management Code of Practice, treasury investments are short-term (up to a maximum duration of 365-days) and are invested under the DLUHC's 'SLY' principles (paragraph 7.5). Treasury investments generally represent the placement of the County Council's residual cash balances resulting from its day-to-day activities, but may also arise from other treasury risk management activity that seeks to prudently manage the risks, costs, or income relating to existing or forecast debt (including the investment of borrowing proceeds where it has been prudent for the Council to borrow in advance of capital need) or treasury investments. Details of investment types approved for the County Council's treasury use are shown below (paragraphs 7.27 to 7.38).

7.27 **Bank Unsecured:** Includes bank current accounts, call (instant-access) accounts, notice accounts, fixed-term deposits, certificate of deposits and senior unsecured bonds with banks and building societies, other than multilateral development banks (for example the European Investment Bank). These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail.

7.28 **Lloyds Bank Plc (Bank Unsecured):** The County Council currently banks with Lloyds Bank plc (Lloyds ring-fenced bank), the contract being renewed in 2022/23 by a direct award under a framework agreement for an initial 7-year term (up to 30 September 2029) with an option to then extend for an additional 3-year following an evaluation of the services provided. Lloyds Bank plc currently meets the County Council's minimum credit criteria, however, should its credit rating fall below the minimum rating criteria as prescribed in this strategy report (paragraph 7.16) the bank may continue to be used for short-term (overnight) liquidity requirements and business continuity arrangements.

7.29 Balances held within Lloyds current accounts will be aggregated together with other investments held with Lloyds Banking Group on a daily basis and should remain within set counterparty monetary limits as prescribed within this strategy report (paragraphs 7.25 and 7.39). Occasionally however, the County Council is in receipt of 'large' amounts of income which cannot be deposited into separate investment counterparties due to intra-day dealing deadlines. In such instances the Director of Finance and Support Services approves that an operational breach of Lloyds Banking Group's approved monetary limits may occur for a maximum period of one working day, with corrective action being taken on the next available working day as appropriate.

7.30 **Bank Secured:** Includes covered bonds and other collateralised arrangements with banks and building societies. These investment types are secured against a bank's assets, which consequently limits the potential losses in the unlikely event of insolvency and means that they are exempt from bail-in. Covered bonds will be considered when secured against a 'pool' of residential and/or low loan-to-value mortgages held by the issuing bank. Covered bonds differ from mortgage or asset-backed securities because the bank which issues the bond always remains responsible for paying dividends and repaying capital. The Council's investments are therefore protected firstly by having a direct call on the 'pool' and secondly by a call on the general assets of the issuer. The County Council also accepts reverse repurchase agreements (repos) as a form of collateralised lending and will be approved on entering into Repo Agreements with specific financial institutions as required.

7.31 For secured bank deposits, where there is no investment specific credit rating but the collateral upon which the investment is secured has a credit rating, then the higher of the collateral credit rating or the counterparty credit rating will be used in determining monetary and duration limits (set out in Table 13; paragraph 7.25). The combined secured and unsecured investments in any one bank will not exceed the monetary limit approved for secured investments.

7.32 **Government Backed:** Loans, deposits, bonds and/or bills issued or guaranteed by national governments, regional and local authorities, and multilateral development banks. These investments are not subject to bail-in and there is an insignificant risk of insolvency; for example, statutory provisions set out in the Local Government Act 2003 preventing a UK local authority default. Investments with UK local authorities can be made for up to twenty years (but may include early repayment conditions for both lender and borrower).

7.33 In any future period of significant market stress, the County Council will maintain required levels of security by restricting new investments to those organisations of high credit quality only and reducing maximum duration limits in accordance with the prevailing market conditions. If there are insufficient financial institutions of high credit quality then the County Council's surplus cash will be deposited with the UK Government, via the Debt Management Office (DMO) and UK gilts/treasury bills, or other local authorities.

7.34 **Registered Social Landlords (RSLs):** Loans, deposits and/or bonds either issued on an unsecured basis or guaranteed by or secured against the assets of the RSL (formerly known as Housing Associations). These bodies are tightly regulated by Homes England and the Regulator of Social Housing; and as providers of public services they retain a likelihood of receiving government support if needed.

7.35 **Corporates:** Loans, bonds and/or commercial paper issued by companies other than banks, building societies and RSLs. These investments are not subject to bail-in but are exposed to the risk of the company going insolvent. The County Council approves the use of investments issued by corporates that hold credit ratings in accordance with the approved investment policy as set out in paragraphs 7.16 and 7.25 (Table 13) up to a maximum of £15m per company (rated A- or above) or £10m for corporates rated BBB+ (investments with BBB+ rated companies being classified as "Non-Specified" in accordance with DLUHC's Investment Guidance). Additionally, the County Council will adhere to the UN's Principles of Responsible Investment (UNPRI) when approving investments with corporates.

7.36 **Money Market Funds:** Pooled investment vehicles consisting of unsecured money market deposits and similar instruments unless the fund consists of government securities only (paragraph 7.38). Such funds have the advantage of providing wide diversification of investment risks and high liquidity, coupled with the services of a professional fund manager. Fees of between 0.10% and 0.20% per annum are deducted from the interest paid to the County Council.

7.37 The County Council continues to use short-term money market funds that offer same-day liquidity as an alternative to instant access bank accounts, subject to approved monetary limits per fund set as £25m or 0.5% of the fund's total assets under management (calculated against the previous working day's closing assets total) whichever is lower.

7.38 In times of significant market stress the County Council may consider the use of money market funds that invest in government securities only as an alternative to Debt Management Office (DMO) deposits, up to a limit per fund of £25m or 2% of the fund's total assets under management, whichever lower (calculated as per paragraph 7.37). Such funds will be treated as a separate counterparty to a standard cash money market fund provided by the same sponsor.

7.39 **Country, Group and Sector Limits:** Due care will be taken to consider the county, group, and sector exposure (in addition to duration and monetary exposure). Specific limits for which investments may be placed are set out below:

Table 15: Country, Group and Sector Limits

Limit Type	**Cash Limit**
UK Central Government	Unlimited
Any single UK Local Authority (excluding individual Fire Authorities and Police and Crime Commissioners)	£25m
Any single financial institution, including UK building societies	£25m
Any single corporate or RSL: Rated A- or above	£15m
Any single corporate (including RSLs): Rated BBB+	£10m
Maximum % invested in UK domiciled institutions/organisations	100%
Maximum investment total for non-UK countries	£90m
Maximum investment per individual non-UK country	£30m
Maximum corporate exposure	£50m
Maximum investments with corporates rated below A-	£30m
Maximum RSL exposure (rated above A-)	£25m
Maximum money market fund exposure (excluding pooled funds)	£200m
Maximum invested in negotiable instruments held in a broker's (including King & Shaxson) nominee account	£100m

7.40 Investments in multilateral development banks and short-term money market funds do not count against the limit for any single non-UK country as shown above (£30m) since the risk is diversified across many countries.

7.41 **Investments categorised as “Commercial”:** In accordance with the CIPFA Treasury Management Code of Practice, all long-term investments (deposits and/or loans with durations greater than one year) and externally managed pooled funds are classed as commercial investments, unless justified by an approved cash flow business case. Long-term investments, where the County Council can demonstrate available cash flow liquidity, with bank secured deposits, local authorities and Registered Social Landlords will be treated as treasury investments; all other long-term investments (including loans to third parties) will be classified as commercial. All commercial investments (and long-term treasury investments) will be categorised as ‘Non-Specified’ in accordance with DLUHC’s Investment Guidance. No long-term investment will be arranged with any bank or building society on an unsecured basis.

7.42 Additionally, the following investment types have been determined appropriate for the County Council’s commercial use (paragraphs 7.43 to 7.49):

7.43 **Externally Managed Pooled Funds:** Shares in diversified investment vehicles which may consist any of the treasury investment types listed above (paragraphs 7.27 to 7.38) plus (but not limited to) equity shares, emerging market debt, and infrastructure/property. These funds allow the County Council to diversify its investment portfolio into asset classes other than cash without the need to own and manage the underlying investments (undertaken by a professional fund manager in return for a fee).

7.44 Ultra-short dated bond funds (enhanced cash funds) provide an alternative to short-term money market deposits (up to 12 months) with the potential of increasing investment returns; but introducing the potential for short-term capital volatility not evident in treasury investments. Multi-asset income and property funds provide the potential for enhanced returns over the longer-term but are significantly more volatile when viewed in the short-term. Consequently, all externally managed pooled funds may experience times of displaying capital losses when viewed over a short-term horizon, contravening ‘SLY’ investment principles.

7.45 The County Council will only approve external fund managers who are a confirmed signatory to the UN’s Principles of Responsible Investment (UNPRI). Selection of funds will then be subject to credit risk appraisal undertaken by the Director of Finance and Support Services and will be reported to the Cabinet Member for Finance and Property and the Treasury Management Panel. The County Council’s current investments in such funds are listed in **Appendix A**.

7.46 Because these funds have no defined maturity date and may be subject to experiencing periods of capital loss, their performance and continued suitability in meeting the County Council’s investment objectives will be regularly monitored by the Director of Finance and Support Services. Any compliance issues arising from pooled fund investments (for instance periods of capital loss) will be reported within quarterly compliance reports to the Regulation, Audit and Accounts Committee.

7.47 **Investments Defined as Capital Expenditure:** Investments defined by legislation as capital expenditure, such as investment property and company shares, are usually covered by the County Council’s non-treasury (commercial) policies as set out in the Capital Strategy; this included two investment properties held by the Council since 2018/19, both located within the boundaries of the 'Coast to Capital' Local Enterprise Partnership (LEP). Additionally, the County Council holds an equity investment in the UK Municipal Bond Agency plc; a capital finance company established in 2014 by the Local Government Association. This capital investment was originally approved in February 2015 having the aim of providing the County Council with a borrowing alternative to the PWLB.

7.48 **Loans:** Loans to third parties (individuals, non-rated companies and wholly owned companies of the County Council) will generally form part of the Council's Capital Strategy with approval based on the economic and social benefits to the County Council and the residents of West Sussex; or following an external credit assessment of the companies involved. Third party loans approved in support of a company's (or individual's) revenue cash flows may however be arranged through the prescribed Treasury Management Practices (TMPs) of the County Council. Ahead of the Director of Finance and Support Services approving a loan the Council will undertake appropriate due diligence of the third party including a financial analysis of an organisation's financial status which will involve analysis of recent accounts. The Council will also look to obtain appropriate levels of security or third party guarantees for any loan advanced. The Council would expect a return commensurate with the type, risk and duration of the loan and a maximum limit of £5m for all third party loans has been set. All loans should be in line with the Council's governance arrangements.

7.49 On 31 March 2022 the County Council had an outstanding loan with the Littlehampton Harbour Board, which commenced in March 2015 and is being repaid annually over a period of 20 years. Interest applicable to this loan is being received to fully recover costs incurred by the County Council and not to generate additional income. Additionally, during 2019/20 the Council introduced the "Financial Support for Recruitment and Retention Employee Loan" scheme, whereby eligible employees (in post designated by the Council as hard to fill) can apply for interest free loans up to £10,000 with repayment terms over a maximum five year period.

7.50 **Commercial Limits:** The following monetary limits will be applied to commercial investments approved though the County Council's prescribed Treasury Management Practices in 2023/24, including maintaining the £100m maximum amount approved as being available for long-term investment (see Table 17; paragraph 7.52):

Table 16: Commercial Investment Limits

Investment Type	**Cash Limit**
Total long-term investments (greater than one year)	£100m
Maximum long-term investment per individual counterparty (excluding local authorities)	£15m
Maximum externally managed pooled fund exposure	£100m
Total investments within externally managed pooled funds, including ultra-short dated bond funds (not rated AAA)	£60m
Total third party loans (in support of revenue cash flows)	£5m

7.51 As required by the Prudential Code, the County Council is required to set limits for total funds invested for greater than 365 days. These limits are set with regard to the County Council's liquidity requirements and to reduce the need for the early sale of an investment (potentially incurring additional costs) and are based on the availability of funds after each year-end.

7.52 The resulting treasury indicator for long-term investments is shown below:

Table 17: Long Term Investment Limits

Treasury Indicator *(i)*	**Upper Limit 2021/22**	**Upper Limit 2022/23**	**Upper Limit 2023/24**	**Upper Limit 2024/25**	**Upper Limit 2025/26**	**Upper Limit 2026/27**
Maximum Invested for a Year or longer	£100m	£100m	£100m	£100m	£100m	£100m

(i) Limits for future years to be reviewed on an annual basis.

7.53 **Policy on Financial Derivatives:** The County Council has previously made use of financial derivatives that are embedded into investments, to reduce interest rate risks through the use of forward dated deals and to increase income through the use of callable deposits. The 'General Power of Competence' in Section 1 of the Localism Act 2011 removed much of the uncertainty over local authorities' use of standalone financial derivatives (those not embedded into an investment), including swaps and options. The CIPFA Treasury Management Code of Practice requires the County Council to clearly state their policy on the use of financial derivatives in the annual strategy.

7.54 The County Council does not intend to use standalone financial derivatives unless they can be clearly demonstrated to reduce the overall level of financial risks the authority is exposed to. Embedded derivatives, including those present in externally managed pooled funds and forward starting investments, will not be subject to this policy; however, the risks they present will be managed in line with the overall treasury risk management strategy. Should this position change the Director of Finance and Support Services, after seeking a legal opinion on the use of standalone financial derivatives, will develop a detailed and robust risk management framework governing their use and will ensure that treasury management officers have the appropriate training.

8 Investment Income (2023/24)

8.1 Interest forecasts provided by Link Group (**Appendix B**) show the potential of further increases to the Bank of England's Bank Rate during the upcoming months (from its current 3.5% level) before peaking and averaging at around 4.5% throughout 2023/24. Forecasts beyond 2023/24 however show the Bank Rate gradually falling as inflationary concerns in the UK economy subside, before reaching a new baseline level of 2.5% by the end of 2025.

8.2 The Director of Finance and Support Services has approved a prudent £7m investment income revenue budget in 2023/24 (increased from £3m in 2022/23) based on the long-term forecasts for Bank Rate as provided by Link Group, mitigating the risks of a reducing income budget (thereby adding pressures to the Council’s Medium Term Financial Strategy) in future years. If the actual rate of return during 2023/24 is higher than the rate assumed in the budget, the Director of Finance and Support Services will consider the most appropriate use of any one-off surplus, with the first call being to mitigate the risk of additional revenue pressures that may arise during 2023/24. The Director of Finance and Support Services will monitor the investment income budget throughout the financial year and report any changes to the above forecast within quarterly Performance and Resources Reports (PRRs).

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Appendices

Appendix A – West Sussex County Council - Treasury Portfolio (31/12/2022)
Appendix B – Economic and Interest Rate Forecast (Link Group)

Background Papers: None