Draft Treasury Management Strategy Statement (2019/20)

1. Background

1.1 The 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 commensurate with the Council's risk appetite, providing adequate liquidity initially before considering investment return.

1.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning, to ensure the 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 Council's risk or cost objectives.

1.3 In December 2017 CIPFA issued revised Prudential and Treasury Management Codes. As a consequence, from 2019/20 all local authorities are required to prepare a separate Capital Strategy report which will provide the following:

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

1.4 The aim of the Capital Strategy is to ensure that all elected members of the County Council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite. The Capital Strategy is reported alongside the budget report and the Treasury Management Strategy Statement for Council approval. Details of the Council's borrowing needs arising from the capital plans along with associated Prudential Indicators are also set out in the Capital Strategy.

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

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

1.6 Treasury management aims to manage risk; accordingly 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.

1.7 The contribution the treasury management function makes to the Council 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 external debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

1.8 Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury investments (arising usually from capital expenditure) and are separate from the day-to-day treasury management activities. Further details are set out in the Capital Strategy.

1.9 Brexit: Currently it is expected that the overall balance of risks to the UK economy is probably neutral, based on a reasonably orderly Brexit through to the end of the original two-year negotiation period (March 2019) and the following transitional period ending around December 2020. The risks of a no-deal Brexit, or conversely a compromise agreement that removes all threats of economic and political disruption, may materially change the forecasts (in either direction) for both UK gilt yields (and related borrowing costs) and the path of the UK Bank Rate (and corresponding short-term investment rates). For example, in the event of an orderly non-agreement exit it is likely the Bank of England would take action to cut the UK Bank Rate from 0.75% in order to help economic growth deal with the adverse effect of this situation.

1.10 The Council's 2019/20 Treasury Management Strategy is recommended on the assumption of an agreement being reached between the UK and the European Union (EU) in accordance with the original Brexit timetable. Both the borrowing and investment strategies contained within the attached report (including forecasts for investment income) may need to be revisited if the current Brexit assumptions do not materialise. Additionally, dependent on how the UK exits from the EU, the Council may lose access to specific counterparties named within the Treasury Management Strategy (for example the European Investment Bank).

2. Reporting Requirements

2.1 Treasury Management Reporting: In accordance with CIPFA's "Treasury Management Code of Practice" the Council is 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) detailing how the Council's investments and borrowings are to be organised; including the annual investment strategy which approves the parameters on how investments are to be managed. Details of the

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 Council’s Capital Strategy.

(b) A Mid-Year Treasury Management Report – Updating the 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; delegated to the Performance and Finance Select Committee in accordance with governance arrangements approved in February 2014. Additionally, the Regulation, Audit and Accounts Committee receive quarterly reports on compliance with the treasury management strategy.

(c) An Annual Treasury Management Report – Providing details of actual treasury operation as compared to the estimates within the strategy, together with a selection of actual prudential and treasury indicators; delegated to the Performance and Finance Select Committee as approved by County Council in July 2018.

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

2.3 Treasury management issues reported within the attached 2019/20 TMSS include the Council’s:

<u>Capital Issues</u>:
- Capital plans;
- Borrowing and repayment strategy forecast projections.

<u>Treasury Management Issues</u>:
- Current treasury position (**Appendix A**);
- Treasury indicators which limit the treasury risk and activities of the Council;
- Prospects for interest rates as provided by the Council’s treasury management advisor (**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.

2.4 These elements cover the requirements of the Local Government Act 2003; CIPFA’s Prudential and Treasury Management Codes; and the Ministry of Housing, Communities and Local Government’s (MHCLG) MRP and Investment Guidance.

3. Training

3.1 CIPFA's Code of Practice requires the Director of Finance, Performance and Procurement to ensure that members with responsibility for treasury management receive adequate training in treasury management. Future training for members responsible for the scrutiny of the Council's treasury management policies and activities, and members acting in an advisory role to the Director of Finance, Performance and Procurement, remain under constant review.

3.2 Additionally, the training needs of treasury management officers are periodically reviewed as part of staff appraisals and personal development plans. Ongoing training options for officers include professional qualifications from CIPFA and other appropriate organisations; attendance at workshops and seminars run by the 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).

4. Treasury Management Advisors

4.1 The Council uses Link Asset Services (Link Treasury Services Ltd) as its external treasury management advisor. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and therefore will ensure that undue reliance is not placed upon its external service providers. The Council recognises however that there is value in employing 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 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. The contract with Link Asset Services commenced on 1 November 2016 and is subject to triennial reviews, with the next review scheduled during 2019/20 *(to include an option to extend for an additional two years following a review of the service received across the period)*.

5. Capital Programme (2019/20 to 2023/24)

5.1 The Council's capital expenditure and financing plans as contained within the approved Capital Programme set out in the Capital Strategy are the key drivers of treasury management activity. The output of the Capital Programme is reflected in the Council's prudential indicators (which are included within the Capital Strategy), which are designed to provide members with an overview and confirm such expenditure and financing plans.

5.2 The table below is a summary of the 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 2019:

Capital Expenditure by Service	2018/19 Estimate £'m	2019/20 Estimate £'m	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Est. *(i)* £'m
Adults and Health	1.0	1.5	1.6	1.7	1.5	0.1
Children & Young People	0.0	0.0	1.0	1.0	1.0	0.0
Corporate Relations	1.2	1.3	16.0	2.1	0.0	0.0
Education & Skills	29.0	31.3	30.5	38.8	18.9	15.1
Environment	0.7	1.2	3.0	2.3	0.0	0.0
Finance and Resources	5.3	7.0	16.3	17.5	16.0	13.7
Highways and Infrastructure	38.7	33.8	45.0	57.9	35.7	37.5
Leader	5.8	7.7	8.2	4.0	12.0	2.0
Safer, Stronger Communities	4.9	9.0	16.7	7.7	8.0	9.1
Core Programme	**86.6**	**92.8**	**138.3**	**133.0**	**93.1**	**77.5**
Income Generating Initiatives *(ii)*	26.3	16.2	42.5	39.2	47.6	24.8
Total Capital Expenditure	**112.9**	**109.0**	**180.8**	**172.2**	**140.7**	**102.3**

(i) 2023/24 estimate includes subsequent years spend.
(ii) IGIs represent the Council's non-treasury (commercial) investment plans.

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. The table below summarises how the Council's capital expenditure plans will be financed across the period through to 2023/24, with any funding shortfall resulting in a borrowing requirement:

Financing the Capital Programme	2018/19 Estimate £'m	2019/20 Estimate £'m	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m
Capital Expenditure	**112.9**	**109.0**	**180.8**	**172.2**	**140.7**	**102.3**
Financed By:						
Government Grants	-79.3	-70.7	-37.8	-38.0	-28.9	-20.2
External	-5.0	-5.8	-9.7	-11.1	-11.8	-11.3

Contributions						
Capital Receipts	-1.0	-3.8	-3.8	-7.7	-22.3	-36.9
Revenue Funding	-1.1	-2.1	-19.4	-6.8	-2.3	-10.5
Capital Expenditure Reserve	-4.0	0.0	0.0	0.0	0.0	0.0
Financing (Excl. Borrowing)	**-90.4**	**-82.4**	**-70.7**	**-63.6**	**-65.3**	**-78.9**
Borrowing (Core)	-1.2	-13.5	-69.0	-76.2	-33.3	-7.4
Borrowing (IGIs and Bold Ideas)	-21.3	-13.1	-41.1	-32.4	-42.1	-16.0
Total Financing	**-112.9**	**-109.0**	**-180.8**	**-172.2**	**-140.7**	**-102.3**

5.5 The above financing table 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 so the Council is not required to separately borrow for them.

6. Borrowing and Repayment Strategy

6.1 The capital expenditure plans set out in Section 5 provide details of the service activity of the Council. The treasury management function ensures that the cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's capital strategy. This will involve both the organisation of the Council's cash flow and, where capital plans require, the organisation of appropriate borrowing facilities.

6.2 The borrowing strategy covers the relevant prudential and treasury indicators, and the current and projected debt positions. The key objectives of the Council's current borrowing strategy are:

(1) Ensure that future external debt is affordable within revenue budget constraints; with the timing of when to arrange new debt governed by the Council's long-term cash flow forecasts (as per the requirements of the capital plans through to 2023/24); and

(2) Potentially borrowing in advance of need so that external debt (fixed-rate funding) is arranged whilst interest rates are lower than they are projected to be over the next few years.

6.3 For all new external debt arrangements, the Council will first ensure that due diligence is given to both the affordability of such debt in the revenue budget and the future plans regarding the repayment of the debt; including the possible use of capital receipts or as per the agreed terms and conditions of any new debt arrangements (including 'annuity' and 'equal instalments of principal' loan structures).

6.4 Approved Funding Sources: The Council's primary objective when borrowing money is to strike an appropriately low risk balance 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 Council's long-term capital plans change is a secondary objective.

6.5 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 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 Council (including usable reserves and working capital) in lieu of external borrowing;
- Public Works Loan Board (PWLB) and any successor body;
- Borrowing from other UK local authorities (particularly with regard to borrowing for Income Generating Initiatives 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 (including the European Investment Bank); and
- Borrowing from the UK Municipal Bond Agency plc and/or other special purpose companies created to enable local authority bond issue.

6.6 The Council is in the process of arranging forward starting loans in line with the approved 2018/19 borrowing strategy, where the interest rate is agreed in advance (fixed in context with current rates) but the cash is received in later years. The arrangement of such debt will therefore enable certainty of cost to be achieved without suffering an investment "cost of carry" in the intervening period. The approval to arrange forward starting loans will continue into 2019/20.

6.7 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 <u>Current Portfolio Position</u>: 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. The Council's internal borrowing at the end of 2017/18 amounted to £69.8m, and is forecast to rise to £89.4m by the end of 2018/19.

6.9 Capital plans (paragraph 5.4) highlight that a borrowing requirement of £26.6m is required to finance the Council's capital expenditure plans in 2019/20 including:

- Borrowing of up to £13.5m relating to the core programme; and
- Additional borrowing of up to £13.1m relating to Income Generating Initiatives.

6.10 In accordance with CIPFA's Prudential Code, the Council's underlying borrowing need (the total historic outstanding capital expenditure which has not yet been financed) is represented by its Capital Financing Requirement (CFR). Capital expenditure financed through debt is subject to a minimum revenue provision charge as set out in the Minimum Revenue Policy which is set out in the Capital Strategy.

6.11 An analysis of the Council's levels of usable reserves, provisions and working balances show these are likely to be sufficient to maintain an internal borrowing strategy throughout 2019/20, with the need to externally borrow for the capital programme thereafter. The table below details the estimates of these year-end balances through to 2023/24, assuming no new external debt or optional refinancing of existing debt is arranged:

Balance Sheet Projections (at 31 March)	2018/19 Estimate £'m	2019/20 Estimate £'m	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m
Capital Financing Requirement	549.8	550.1	605.5	666.1	681.5	669.6
CFR – Commercial (IGIs)	36.6	52.0	92.1	122.8	163.3	195.5
Capital Financing Requirement	**586.4**	**602.1**	**697.6**	**788.9**	**844.8**	**865.1**
Less: PFI Schemes and Leases	-103.2	-100.2	-97.0	-93.4	-89.3	-84.8
Borrowing CFR *(i)*	**483.2**	**501.9**	**600.6**	**695.5**	**755.5**	**780.3**
Existing Borrowing Profile (PWLB)	-388.8	-381.8	-374.8	-371.3	-361.3	-361.3
Short-Term Borrowing *(ii)*	-5.0	-5.5	-5.5	-5.5	-5.5	-5.5
Over(-) / Under Borrowing	**89.4**	**114.6**	**220.3**	**318.7**	**388.7**	**413.5**
Usable Reserves	-175.6	-202.4	-143.4	-140.8	-138.0	-120.0
Provisions	-12.0	-11.0	-10.0	-10.0	-10.0	-10.0
Working Balances	-63.3	-64.9	-66.5	-68.2	-69.9	-70.0
Investment(-) / Borrowing	**-161.5**	**-163.7**	**0.4**	**99.7**	**170.8**	**213.5**

(i) The "Borrowing CFR" excludes other long-term liabilities (PFI schemes and finance leases) that form part of the Council's total borrowing requirement but include a borrowing facility so that the Council is not required to borrow separately for them.

(ii) Money held and invested on behalf of the Chichester Harbour Conservancy (CHC) and its associated charities; repayable to CHC on any given notice.

6.12 The Council has previously approved that a proportion of its usable reserves are held in long-term strategic investments (including PFI/MRMC reserve balances); as a result the Council's external debt and internal borrowing projections (including CFR forecasts; and internal borrowing as a percentage of the CFR) are summarised below:

Debt Projections	2018/19 Estimate £'m	2019/20 Estimate £'m	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m
Gross External Debt (1-Apr)	**506.2**	**497.0**	**487.5**	**517.9**	**610.1**	**667.1**

Repayment of Existing Debt	-6.7	-6.5	-7.0	-3.5	-10.0	0.0
External Debt (Core Borrowing)	0.0	0.0	0.0	17.1	30.6	10.3
External Debt (IGIs)	0.0	0.0	40.6	82.2	40.5	32.2
PFI/Finance Lease Movement	-2.5	-3.0	-3.2	-3.6	-4.1	-4.5
Gross External Debt (31- Mar)	**497.0**	**487.5**	**517.9**	**610.1**	**667.1**	**705.1**
Internal Borrowing (at 31 March)	89.4	114.6	179.7	178.8	177.7	160.0
Capital Financing Requirement	**586.4**	**602.1**	**697.6**	**788.9**	**844.8**	**865.1**
Internal Borrowing (%)	**15.2%**	**19.0%**	**25.8%**	**22.7%**	**21.0%**	**18.5%**

6.13 The benefits of internal borrowing will be regularly monitored against the potential for incurring additional costs through deferring external borrowing into future years when long-term borrowing rates are forecast to rise. Whilst this strategy has remained prudent against a continual backdrop of low investment returns and heightened counterparty risk, there will be a future point in time when internal borrowing will have to be externalised. As shown in the table above, under the Council's current capital plans, usable reserves and long-term strategic investment assumptions, it is forecast that the Council will be required to reintroduce external borrowing in 2020/21.

6.14 Revenue Impact: The revenue impact (capital financing cost as a percentage of net revenue streams) of the recommended borrowing strategy relating to the Council's 'core' capital programme (excluding IGIs, Bold Ideas, PFI and Finance Leases) is outlined below:

	2019/20 Estimate £'m	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m
Net Revenue Expenditure	574.9	580.9	593.3	607.3	620.0
Capital Financing Charges – ***Excluding*** *IGIs, PFI and Finance Leases*	27.3	27.8	29.9	32.6	33.8
% Ratio	**4.8%**	**4.8%**	**5.0%**	**5.4%**	**5.5%**

6.15 In accordance with this recommended borrowing strategy, the Council forecasts that the costs of external borrowing (interest charges) in 2019/20 will be:

- Core Programme: £17.5m (£17.8m in 2018/19)
- IGIs and Bold Ideas: Nil (unchanged from 2018/19)
- PFI schemes and finance leases: £9.7m (£9.9m in 2018/19)

6.16 Borrowing in Advance of Need: A decision to borrow in advance will be within forward approved CFR estimates and arranged to take advantage of favourable borrowing rates (given such rates are forecast to rise in the future) thereby ensuring that value for money can be demonstrated and that the Council can ensure the security of such funds. Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through quarterly compliance reports (and annual report to the Performance and Finance Select Committee).

6.17 The Authorised Borrowing Limit (paragraph 6.20) constraints 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.

6.18 Limits to Borrowing Activity: Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council ensures that its 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 2019/20 and the following two financial years. Based on the gross external debt projections (paragraph 6.12) the Director of Finance, Performance and Procurement reports that the Council complied with this prudential indicator in 2018/19 and does not envisage difficulties over the period of the capital programme.

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

Operational Boundary	Estimate 2018/19 £'m	Estimate 2019/20 £'m	Estimate 2020/21 £'m	Estimate 2021/22 £'m	Estimate 2022/23 £'m	Estimate 2023/24 £'m
External Debt (including CHC)	393.8	387.3	380.3	393.9	414.5	424.8
Income Generating Initiatives (IGIs)	0.0	0.0	40.6	122.8	163.3	195.5
PFI Schemes/ Finance Leases	103.2	100.2	97.0	93.4	89.3	84.8
Operational Boundary	**497.0**	**487.5**	**517.9**	**610.1**	**667.1**	**705.1**

6.20 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.

6.21 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.

Authorised Borrowing Limit	Estimate 2018/19 £'m	Estimate 2019/20 £'m	Estimate 2020/21 £'m	Estimate 2021/22 £'m	Estimate 2022/23 £'m	Estimate 2023/24 £'m
Gross Debt (inc. IGIs)	454.7	549.9	610.1	651.7	655.8	660.3
PFI Schemes/ Finance Leases	103.2	100.2	97.0	93.4	89.3	84.8
Authorised Borrowing Limit	**557.9**	**650.1**	**707.1**	**745.1**	**745.1**	**745.1**

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 2019/20 (£650.1m) equals the maximum external debt forecast in any one financial year over a three year period (i.e. the "Operational Boundary" over the period 2019/20 to 2021/22; therefore £610.1m for 2021/22) plus £40m.

6.22 In addition, the 'Maturity Structure of Fixed Rate Borrowing' Treasury Indicator are limits that highlight the existence of any large concentrations of fixed rate 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 fixed rate borrowing that is maturing in each period as a percentage of total projected fixed rate borrowing. The maturity period of borrowing is determined by reference to the earliest date on which the lender can require payment.

6.23 The upper and lower limits for the maturity structure of fixed rate borrowing in 2019/20 (with actual split as at 30 September 2018 included for comparison) are set out below:

Treasury Management	Actual 30/09/18	Lower Limit 2019/20	Upper Limit 2019/20
Debt Maturity:			
Over 30 Years	6%	0%	40%
Over 25 to 30 Years	0%	0%	25%
Over 20 to 25 Years	4%	0%	25%
Over 15 to 20 Years	8%	0%	25%
Over 10 to 15 Years	54%	0%	65%
Over 5 to 10 Years	19%	0%	45%
Over 1 to 5 Years	6%	0%	35%
Under 12 Months	3%	0%	25%

6.24 <u>Borrowing for Cash-flow Purposes</u>: The 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:

- Borrowing from other UK local authorities (excluding Police and Crime Commissioners, Fire Authorities and Local Authority Pension Funds);

- Borrowing from the money markets (financial institutions authorised by the Prudential Regulation Authority to operate in the UK).

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

6.26 Debt Rescheduling: As short-term borrowing rates will be considerably cheaper than long-term fixed interest rates there may be opportunities to generate savings by switching from long-term debt to short-term debt. Any savings generated will need to be considered in light of the Council's current treasury position (Balance Sheet projections; paragraph 6.11) and the actual cost of debt repayment (premiums incurred). The rationale for undertaking any debt repayment or rescheduling would be one or more of the following:

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

6.27 Reporting: All borrowing (and rescheduling) activity will be reported quarterly to the Regulation, Audit and Accounts Committee and Treasury Management Panel meetings within the prescribed compliance reports.

6.28 As at 31 March 2018 the Council had external loans with the PWLB totalling £395.9m, with a maturity profile which stretches out to 2059. As originally approved within the 2018/19 Treasury Management Strategy, the Council intends to repay any loan as it falls due; including the annual repayment of £7m in respect of the £70m PWLB loan taken out in April 2011. A projection of the Council's longer term borrowing requirement up to 2060 is set out in the Capital Strategy and this assumes an annual core programme borrowing requirement of £20m from 2024/25 and useable reserves, provisions and working capital of £130m form 2039/40 onwards.

7. Annual Investment Strategy (Treasury Investments)

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

7.2 The 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 Council by the Local Government Act 2003 (Section 12; "Power to Invest").

7.3 At 30 September 2018 the Council's investments amounted to £266.8m (**Appendix A**). In the past twelve months the Council's average investment balance was £293m (including Local Enterprise Partnership monies) but is forecast to average around £175m throughout 2019/20.

7.4 The Council's investment policy has regard to the CIPFA Treasury Management Code of Practice and MHCLG's Guidance on Local Government Investments. The Council's investment priorities will be the security first, liquidity second and then investment return ("SLY" investment principles). Accordingly the 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.

7.5 In accordance with the CIPFA and MHCLG guidance, and in order to minimise the risk to investments, the 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 Asset Services) the 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.

7.6 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 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.

7.7 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 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.

7.8 Accordingly, the Director of Finance, Performance and Procurement will comply with the following strategy 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 current list of approved brokers comprises:

- BGC Partners (including Martin Brokers)
- CBRE Limited
- Institutional Cash Distributors (ICD) Ltd
- King and Shaxson Limited
- Tradition (UK) Limited
- TP ICAP plc (including ICAP and Tullett Prebon Europe Ltd)

7.9 Creditworthiness Policy: The primary objective governing the Council's investment criteria is the security of its investments, although the yield or investment return is also a key consideration (paragraph 7.4). After this objective the 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 Council's prudential indicators covering the maximum principal sums invested.

7.10 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 Council (including bank secured, local authority and non-bank corporate deposits). In addition to the risks associated with bail-in, from January 2019 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". Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt-up. Several banks are very close to the threshold so may come into scope in the future regardless.

7.11 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.

7.12 While the structure of the banks included within this 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 Council will continue to assess the new-formed entities in the same way that it does others and those with sufficiently high ratings (and other credit metrics considered, paragraphs 7.6 and 7.7) will be considered for investment purposes.

7.13 At 30 September 2018, 57.1% of the Council's investment portfolio is invested in short-term unsecured bank deposits and short-term money market funds (excluding externally managed pooled funds) in accordance with the policies as contained within the 2018/19 TMSS. The Director of Finance, Performance and Procurement confirms that the Council will not be holding any investment at 31 March 2019 that will be in breach of the recommended 2019/20 strategy.

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

- Denominated in Sterling;
- With a maximum maturity of one year (365 days);
- Not defined as capital expenditure by legislation; and
- 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).

7.15 For investments to be regarded as specified, the 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 Banks: 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) Non-UK 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+**).

(d) Money Market Funds: Holding a **AAA** credit rating; rated by at least two of the three rating agencies and holding assets exceeding £1bn. New EU regulations implemented in 2018/19 changed fund valuation methodology from only Constant Net Asset Valuation (CNAV) to both Low Volatility Net Asset Valuation (LVNAV) and CNAV. As a consequence the Council approves the use of Money Market Funds that operate under a CNAV (funds that invest exclusively in government securities) or operate under a LVNAV (all other liquidity funds).

(e) UK Local Authorities: Assumed **AA-** rating (unless actual rating exists from any of the three rating agencies).

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

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

7.16 Any investment not meeting the 'Specified' investment criteria listed above will be treated as if it were unrated ('Non-Specified' investment; paragraph 7.45). 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.

7.17 Monitoring Credit Quality: Credit rating information is supplied by Link Asset Services (the Council's treasury advisor) on all active counterparties that comply with the criteria listed above. Any counterparty falling 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 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:

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

7.18 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 Council's minimum approved rating criteria) then decisions on new investments will be subject to approval by the Director of Finance, Performance and Procurement. This policy will not apply to negative 'outlooks', which indicate a longer term view rather than an imminent change to an institution's rating.

7.19 If an institution is placed on negative rating watch and is at (or likely to fall below) the Council's minimum rating criteria then no investments will be arranged until the outcome of the review is announced. Again, this policy will not apply to negative 'outlooks'.

7.20 Additional requirements under the CIPFA Treasury Management Code require the 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 7.6 and 7.7) 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 counterparties.

7.21 The Director of Finance, Performance and Procurement and the 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 7.15 and 7.25).

7.22 Liquidity Management: The Council uses purpose-built short-term cash flow forecasting software (SAP Treasury Management Module) to determine the maximum period for which funds may prudently be invested. The cash flow forecast is entered on a prudent basis with income under-estimated and expenditure over-estimated. Additionally, the Council seeks to maintain a smooth 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 Council's Medium Term Financial Strategy (MTFS) and long-term forecasts of usable reserve balances.

7.23 To assist liquidity management the Council operates a number of interest paying bank call (instant-access) accounts and money market funds where cash is deposited at competitive overnight interest rates and can be withdrawn without notice; these funds are therefore highly liquid.

7.24 Investment Policy: The Director of Finance, Performance and Procurement, in consultation with the Cabinet Member for Finance and Resources and the Treasury Management Panel, recommends a continuation of the existing investment strategy be approved in 2019/20.

7.25 The Director of Finance, Performance and Procurement will undertake the most appropriate form of investments in keeping with the approved strategy objectives, income and risk management requirements and the Council's Treasury Indicators. Accordingly the 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:

Institution/Issue Credit Rating	**Unsecured Bank Deposits**		**Secured Bank, Government Issues, UK Local Authorities and Non-Bank**	
	Cash Limit	**Time Limit**	**Cash Limit**	**Time Limit**
UK Government			Unlimited	50 Years
Local Authorities			£25m	20 Years
AAA	£15m	2 Years	£25m	10 Years
AA+	£15m	1 Year	£25m	5 Years
AA	£15m	1 Year	£25m	4 Years
AA-	£15m	1 Year	£25m	3 Years
A+	£15m	1 Year	£15m	2 Years
A	£15m	6 Months	£15m	1 Year
A-	£15m	100 Days	£15m	6 Months
BBB+	No Approval		£10m	100 Days
RBS Banking Group - Ring-Fenced Bank only *(Part Nationalised)*	£15m	1 Year	(as AAA rating above)	
Money Market Funds	£25m *(i)*	Overnight	£25m *(ii)*	Overnight
Housing Associations (rated A- or higher)			£15m	5 Years

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

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

(iii) *Maximum monetary limits for externally managed pooled funds (including ultra-short dated bond, equity, multi-asset 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 Banks 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.

7.27 Banks Secured: Includes covered bonds, reverse repurchase agreements (repos) and other collateralised arrangements with banks and building societies. These investment types are secured against the 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 remains responsible at all times 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.

7.28 The Council accepts repo/reverse repo as a form of collateralised lending and will be based on the GMRA 2000 ("Global Master Repo Agreement"). Should any investment counterparty not meet the Council's senior unsecured rating (as set out in paragraph 7.25) then a 102% collateralisation will be required. Acceptable collateral will include index linked gilts, conventional gilts, UK treasury bills, delivery by value (a basket of gilts covering differing maturity periods) and corporate bonds (subject to a minimum A- bond issue rating).

7.29 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 (as set out in paragraph 7.25). The combined secured and unsecured investments in any one bank will not exceed the monetary limit approved for secured investments.

7.30 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; 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). The Director of Finance, Performance and Procurement will approve a local authority as suitable for long-term investment (greater than one year) before the investment is placed.

7.31 In any future period of significant market stress the 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 Council's surplus cash will be deposited with the UK Government, via the Debt Management Office (DMO) and UK treasury bills, or other local authorities.

7.32 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 the Homes and Communities Agency and as providers of public services they retain a likelihood of receiving government support if needed.

7.33 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 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 7.15 and 7.25) up to a maximum of £15m per company (£10m for corporates rated BBB+).

7.34 Money Market Funds: Pooled investment vehicles consisting of unsecured money market deposits and similar instruments, unless the fund consists of government securities only (paragraph 7.36). 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 Council.

7.35 The Council continues to use short-term money market funds that offer same-day liquidity and aim for no (or very low) asset value volatility 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.

7.36 In times of significant market stress the 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 7.35). Such funds will be treated as a separate counterparty to a standard cash money market fund provided by the same sponsor.

7.37 Externally Managed Pooled Funds: Shares in diversified investment vehicles which may consist any of the investment types listed above (paragraphs 7.26 to 7.33) plus (but not limited to) equity shares, emerging market debt, and infrastructure/property. These funds allow the 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).

7.38 Ultra-short dated bond funds (enhanced cash funds) provide an alternative to short-term money market funds in the management of cash-flow liquidity (up to 12 months) with the potential of increasing investment returns; whilst introducing the potential for short-term capital volatility not evident in money market funds. Equity, multi-asset 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.

7.39 Selection of funds will be subject to credit risk appraisal undertaken by the Director of Finance, Performance and Procurement and will be reported to the Cabinet Member for Finance and Resources and the Treasury Management Panel. The Council's current investments in such funds are listed in **Appendix A**.

7.40 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 Council's investment objectives will be regularly monitored by the Director of Finance, Performance and Procurement. 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.

7.41 The Council's Main Provider of Banking Services: The Council currently banks with Lloyds Bank plc (Lloyds ring-fenced bank), the contract being effective up to 30 September 2022. Lloyds currently meets the Council's minimum credit criteria, however should its credit rating fall below the minimum rating criteria as prescribed in this strategy report (paragraph 7.15) the provider may continue to be used for short-term (overnight) liquidity requirements and business continuity arrangements.

7.42 Balances held within current accounts will be aggregated together with investments held with the Council's banker on a daily basis, and should remain within set counterparty monetary limits as prescribed within this strategy report (paragraphs 7.25 and 7.43). Occasionally however, the 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 Council approves that an operational breach of the Council's main banker's set 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.

7.43 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:

	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 amount per banking group	£25m
Maximum corporate exposure	£50m
Maximum RSL exposure (rated above A-)	£25m
Maximum money market fund exposure (excluding pooled funds)	£115m
Maximum externally managed pooled fund exposure	£100m
Maximum investment total for non-UK countries	£90m
Maximum investment per individual non-UK country	£30m
Maximum invested in negotiable instruments held in a broker's (including King & Shaxson) nominee account	£100m

7.44 Investments in multilateral development banks, short-term money market funds and externally managed pooled 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.

7.45 Non-Specified Investments: Any investment not meeting the MHCLG definition of a 'Specified' investment (or 'Loan') is classified as 'Non-Specified'. Having considered the rationale and risks associated with non-specified investments, the following have been determined appropriate for the Council's use:

- Long-term (greater than one year) investments
- Investments with credit ratings below A- (corporates)
- Investments in externally managed pooled funds (not rated AAA)
- Investments denominated in foreign currencies (Euros)
- Investments that are defined by legislation as capital expenditure

7.46 The following monetary limits will be applied to Non-Specified treasury investments in 2019/20; including a continuation of the £75m limit approved as being available for long-term investment (originally approved in 2018/19):

Investment Type	**Cash Limit £'m**
Total long-term investments (greater than one year)	75.0
Total investments with corporates rated below A-	30.0
Total investments within externally managed pooled funds, including ultra-short dated bond funds (not rated AAA);	60.0
Total investments denominated in foreign currencies	2.8

Total investments defined as capital expenditure	0.2

7.47 Long-Term Investments: Long-term investments including gilts, covered bonds, corporate bonds, supranational bank bonds, local authority loans, RSLs deposits/bonds, externally managed pooled funds and an equity investment with the UK Municipal Bond Agency are approved by the Council. The maximum monetary limit for long-term investments with any one organisation is set at £15m (£25m for individual UK local authorities). At 30 September 2018 the Council had £58.1m invested for greater than one year including:

- £26.0m invested with three UK local authorities;
- £24.0m invested in externally managed property funds;
- £7.9 invested in a Nationwide Building Society covered bond; and
- £0.2m equity held with the UK Municipal Bond Agency.

7.48 As required by the Prudential Code, the Council is required to set limits for total funds invested for greater than 365 days. These limits are set with regard to the 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 (as detailed in the Council's Balance Sheet Projections; paragraph 6.11). The resulting treasury indicator is shown below:

	Upper Limit 2018/19	**Upper Limit 2019/20**	**Upper Limit 2020/21**	**Upper Limit 2022/22**	**Upper Limit 2022/23**	**Upper Limit 2023/24**
Maximum Invested for a Year or longer (£)	£75m	£75m	£65m*(i)*	£55m	£45m	£45m

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

7.49 No long-term investment will be arranged with any bank or building society on an unsecured basis.

7.50 Non-Sterling Investments: Occasionally the Council may receive grant funding denominated in Euros and subsequently incurs expenditure in Euros. To remove the exchange rate risk associated with converting such funds into Sterling, these can be held in a Euro denominated bank account. The Director of Finance, Performance and Procurement may therefore make investments denominated in Euros up to a maximum limit of €3.2m (£2.8m equivalent based on a 1.1428 exchange rate).

7.51 Investments Defined as Capital Expenditure: Investments defined by legislation as capital expenditure, such as company shares, are covered by the Council's non-treasury (commercial) investment policy as set out in the Capital Strategy. The Council does however hold a £0.2m 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 in light of the Council's significant borrowing requirement in the period up to 2025, having the aim of providing the Council with a viable borrowing alternative to the Public Works Loan Board (PWLB).

7.52 Policy on Financial Derivatives: The 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 Council to clearly state their policy on the use of financial derivatives in the annual strategy.

7.53 The Council does not intend to use standalone financial derivatives unless they can be clearly demonstrated to reduce the overall level of financial risks the Council 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, Performance and Procurement, 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.

7.54 Loans: Loans to third parties (individuals and/or non-rated companies) will be approved based on the economic and social benefits to the Council and the residents of West Sussex; or following an external credit assessment of the company involved. At 31 March 2018 the Council had one outstanding loan with the Littlehampton Harbour Board, which commenced in March 2015 and is being repaid annually over a period of twenty years. Interest applicable to this loan is being received to fully recover costs incurred by the Council and not to generate additional income.

8. Investment Income (2019/20)

8.1 In accordance with interest forecasts provided by Link Asset Services (**Appendix B**) the Bank of England's Bank Rate is expected to average around 1.00% during 2019/20; a consequence of two 0.25% rate increase during the period (forecast in May 2019 and February 2020).

8.2 The Council is expected to have an average investment portfolio of £175m throughout 2019/20 (paragraph 7.3). Given the Bank Rate forecast and the continuation of the Council's 2018/19 investment strategy (approval to invest up to £75m in long-term local authority investments and externally managed pooled funds) it is forecast that the portfolio will attract an average interest rate of 1.69%. The Council therefore expects to receive investment income totalling £2.0m in 2019/20 (as shown in the table below):

	Average Portfolio £'m	Interest Rate (%)	Interest £'m
Liquidity Portfolio	35.0	0.97	0.3

Short-Term Investment Portfolio	90.0	1.16	1.1
Long-Term Investment Portfolio	50.0	3.10	1.6
Gross Interest Return	**175.0**	**1.69**	**3.0**
Less transfers to specific reserves			-1.0
Investment Income (2019/20)			**2.0**

8.3 If actual levels of investments and interest rates differ from the forecasts then performance against the budget will be correspondingly different. Given the constraints on the Council's 2019/20 revenue budget, the Director of Finance, Performance and Procurement will monitor the investment income budget throughout the period and report any changes to the above forecast within monthly Total Performance Monitors (TPMs).

9. Resource and Value for Money Implications

9.1 Covered in main body of report.

10. Risk Management Implications

10.1 Covered in main body of report.

11. Human Rights Act Implications

11.1 Not applicable.

12. Crime and Disorder Act Implications

12.1 Not applicable

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Appendices
A West Sussex County Council - Treasury Portfolio
B Economic and Interest Rate Forecast (Link Asset Services)

Background Papers
None