Treasury Management Strategy Statement (2021/22)

1 Background

1.1 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".*

1.2 In accordance with the CIPFA definition, the 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 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.

1.4 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.

1.5 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 resulting treasury operations generate interest costs in relation to external debt and income arising from investments, both of which affecting the available revenue budget. Furthermore, since cash balances generally arise from the Council's earmarked reserves and working balances, it remains paramount to ensure adequate security of the sums invested, as any loss of principal will in effect result in a loss to the General Fund Balance.

1.6 Additionally, the Council's commercial activities (economic developments) or loans to third parties will 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).

2 Reporting Requirements

2.1 **Capital Strategy:** CIPFA's Prudential and Treasury Management Codes 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.

2.2 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.

2.3 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 Council under the Local Government Act 2003 (governed by security, liquidity and yield principles) from the Council's commercialism policies where investments are usually driven by expenditure on an asset. To demonstrate proportionality between the Council's treasury management operations and non-treasury (economic developments) high-level comparators are shown in Sections 5 and 6 of this report.

2.4 **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 treasury 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 Scrutiny 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 Scrutiny Committee as approved by County Council in July 2018.

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

2.6 Treasury management issues reported within the attached 2021/22 TMSS include the Council's:

Capital Issues:

- A summary of capital expenditure plans up to 31 March 2026; and
- Associated capital financing plans, including forecasts of the 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 Council;
- Prospects for interest rates as provided by the 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.

2.7 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) Investment Guidance.

3 Training

3.1 CIPFA's Code of Practice requires the Director of Finance and Support Services to ensure that members involved with 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 and Support Services 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 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 Council recognises that the responsibility for all treasury management decisions always remain 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 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. A three year contract with Link Group (Treasury Solutions) commenced on 1 November 2016 and was extended for an additional two years up to 31 October 2021 following a review undertaken in 2019 of the service received.

4.4 With the contractual period with Link Group ending in 2021/22, a treasury management advisor procurement exercise is scheduled to take place during 2021. Any resulting changes to the existing arrangements will be reported to the Performance and Finance Scrutiny Committee and the Treasury Management Panel.

5 Capital Programme (2021/22 to 2025/26)

5.1 The Council's capital expenditure and financing plans as contained within the approved Capital Programme set out in the Capital Strategy are 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 are both affordable and prudent.

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 2021:

Capital Expenditure by Service	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Est. *(i)* £'m
Adults and Health	3.6	2.1	4.3	4.3	4.0	1.0
Children & Young People	4.5	1.0	1.1	1.0	1.0	1.2
Economy and Corporate Resources	9.8	7.4	17.6	16.9	12.0	12.0
Education & Skills	23.6	19.5	34.8	25.6	21.6	38.9
Environment	1.4	4.5	11.3	16.0	16.3	22.5
Finance	6.5	8.8	13.9	22.3	20.2	24.3
Fire & Rescue and Communities	4.7	3.6	12.7	13.3	10.7	7.6
Highways and Infrastructure	41.4	54.8	65.7	29.7	19.8	61.2
Total Capital Expenditure	**95.5**	**101.7**	**161.4**	**129.1**	**105.6**	**168.7**

(i) 2025/26 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. The table below summarises how the Council's capital expenditure plans will be financed across the period through to 2025/26, with any funding shortfall resulting in a borrowing requirement:

Financing the Capital Programme	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m
Capital Expenditure	**95.5**	**101.7**	**161.4**	**129.1**	**105.6**	**168.7**
Government Grants	-78.0	-77.3	-36.3	-29.2	-21.4	-23.6
External Contributions	-7.0	-9.8	-12.5	-8.0	-5.1	-39.9
Capital Receipts	-3.7	-5.3	-1.0	-1.0	-1.0	-6.5
Revenue Funding	-2.1	-2.4	-7.6	-7.0	-4.5	-3.1
Financing (Excl. Borrowing)	**-90.8**	**-94.8**	**-57.4**	**-45.2**	**-32.0**	**-73.1**

Financing the Capital Programme	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m
Borrowing (Core)	0.0	0.0	-84.3	-55.1	-49.1	-58.3
Borrowing (Economic Developments)	-4.7	-6.9	-19.7	-28.8	-24.5	-37.3
Total Financing	**-95.5**	**-101.7**	**-161.4**	**-129.1**	**-105.6**	**-168.7**

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 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 2025/26); 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 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.

6.6 The 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 2021/22. Capital finance may additionally be raised by other methods that are not borrowing but may be classed as other debt liabilities (including leasing).

6.7 In November 2020 HM Treasury published the outcomes of the PWLB review that aims to ensure that local authorities invest public funds in infrastructure and front-line services only. As a result, from December 2020 local authorities (non-HRA) will be able to access funding at the PWLB Certainty Rate of UK Gilts plus 0.80%; representing a 1% reduction as compared with the cost of pre-December borrowing. From this date however all new PWLB borrowing will be conditional on the 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. The Council confirms that capital plans have been reviewed and are compliant with these PWLB requirements.

6.8 **Current Portfolio Position:** At 31 December 2020 the Council had external loans with the PWLB totalling £474.8m. In accordance with the approved 2020/21 Treasury Management Strategy no external borrowing was arranged during the period April to December 2020; cash supporting the Council's usable reserves and working capital was used as a temporary funding measure in lieu of external borrowing. Consequently, the Council's internal borrowing at the end of 2020/21 is forecast to be £27.9m (£28.7m at 31 March 2020) as set out in paragraphs 6.11 and 6.12.

6.9 Capital plans (paragraph 5.4) highlight that a borrowing requirement of £6.9m is required to finance the Council's capital expenditure plans in 2021/22; all relating to economic development projects.

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 (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 continue with an internal borrowing strategy throughout 2021/22 and 2022/23, with the need to externally borrow for the capital programme from 2023/24 onwards. The table below details the estimates of these year-end balances through to 2025/26, assuming no new additional external debt or optional refinancing of existing debt is arranged:

Balance Sheet Projections (at 31 March)	**2020/21 Estimate £'m**	**2021/22 Estimate £'m**	**2022/23 Estimate £'m**	**2023/24 Estimate £'m**	**2024/25 Estimate £'m**	**2025/26 Estimate £'m**
Capital Financing Requirement	518.5	505.2	577.8	615.4	644.9	682.2
CFR (Economic Developments)	81.4	86.2	103.6	129.6	150.5	183.5
Capital Financing Requirement	**599.9**	**591.4**	**681.4**	**745.0**	**795.4**	**865.7**
Less: PFI Schemes and Leases *(i)*	-91.7	-88.7	-87.6	-83.2	-78.5	-73.8
Borrowing CFR *(ii)*	**508.2**	**502.7**	**593.8**	**661.8**	**716.9**	**791.9**
Existing Borrowing Profile (PWLB)	-474.8	-471.3	-461.3	-461.3	-461.3	-437.2
Short-Term Borrowing *(iii)*	-5.5	-5.5	-5.5	-5.5	-5.5	-5.5
Under Borrowing	**27.9**	**25.9**	**127.0**	**195.0**	**250.1**	**349.2**

(i) International Financial Reporting Standards (IFRS)16 requires the Council to account for lessee operating leases (off Balance Sheet) as finance leases from 1 April 2022. The Council currently estimates that leases totalling £3.4m will be added to the Balance Sheet from 1 April 2022 as a result of IFRS16; and as such have been included in the above (and subsequent) tables in Section 6.

(ii) The 'Borrowing CFR' excludes other long-term liabilities (PFI schemes and finance leases) that form part of the Council's total borrowing requirement.

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

Balance Sheet Projections *(continued)*	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m
Under Borrowing	**27.9**	**25.9**	**127.0**	**195.0**	**250.1**	**349.2**
Usable Reserves	-206.2	-220.5	-148.3	-138.0	-134.5	-130.7
Provisions	-15.0	-15.0	-15.0	-15.0	-15.0	-15.0
Working Capital	-65.0	-65.0	-65.0	-65.0	-65.0	-65.0
Funding required for investments greater than one year	100.0	100.0	100.0	100.0	100.0	100.0
Short Term Investment(-) / External Borrowing (cumulative)	**-158.3**	**-174.6**	**-1.3**	**77.0**	**135.6**	**238.5**

6.12 The Council has previously approved that a proportion of its usable reserves (including PFI/MRMC reserve balances) are held in long-term strategic investments; 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	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m
Gross External Debt (1-Apr)	**581.2**	**572.0**	**565.5**	**554.4**	**627.0**	**680.9**
Repayment of Existing Debt	-7.0	-3.5	-10.0	0.0	0.0	-24.1
CHC 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	0.0	55.0
External Debt (Economic Developments)	0.0	0.0	0.0	77.0	58.6	47.9
PFI/Finance Lease Movement	-2.7	-3.0	-1.1	-4.4	-4.7	-4.7
Gross External Debt (31-Mar)	**572.0**	**565.5**	**554.4**	**627.0**	**680.9**	**755.0**

Debt Projections *(continued)*	2020/21 Estimate £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m
Cumulative Gross External Debt (at 31-March)	**572.0**	**565.5**	**554.4**	**627.0**	**680.9**	**755.0**
Cumulative Internal Borrowing (at 31 March)	27.9	25.9	127.0	118.0	114.5	110.7
Capital Financing Requirement	**599.9**	**591.4**	**681.4**	**745.0**	**795.4**	**865.7**
Internal Borrowing (%)	**4.6%**	**4.4%**	**18.6%**	**15.8%**	**14.4%**	**12.8%**

6.13 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 externally borrow in 2023/24 which reflects the need to ensure that cash (useable reserves and working capital) is available to maintain the £100m long-term investment limit up to 2025/26 (as set out in paragraph 7.49). Whilst the continuation of an internal borrowing strategy in 2021/22 remains prudent, the continued benefits 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 (**Appendix B**).

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 capital programme (excluding service funded Economic Developments, PFI schemes and Finance Leases) is outlined below:

	2020/21 Actual £'m	2021/22 Estimate £'m	2022/23 Estimate £'m	2023/24 Estimate £'m	2024/25 Estimate £'m	2025/26 Estimate £'m
Net Revenue Expenditure	593.9	624.8	633.9	656.9	687.2	700.0
Capital Financing Charges	28.5	28.7	28.7	32.2	35.2	38.8
% Ratio	**4.8%**	**4.6%**	**4.5%**	**4.9%**	**5.1%**	**5.5%**

6.15 In accordance with this recommended borrowing strategy, the Council forecasts that the costs of long-term external borrowing (interest charges) in 2021/22 will be:

- PWLB Borrowing: £19.3m (£19.5m in 2020/21); of which £1.4m will be service funded from economic development schemes.
- PFI schemes and finance leases: £11.0m (£11.2m in 2020/21)

6.16 **Borrowing in Advance of Need:** Any 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 Scrutiny Committee).

6.17 The Authorised Borrowing Limit (paragraph 6.21) 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.

6.18 **Limits to Borrowing Activity:** Within the prudential indicators there are several key indicators to ensure that the Council operates its activities within well-defined limits. These indicators ensure that the 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 2021/22 and the following two financial years. Based on the gross external debt projections (paragraph 6.12) the Director of Finance and Support Services reports that the Council complied with these prudential indicators in 2020/21 and does not envisage any non-compliance 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 below:

Operational Boundary	**Estimate 2020/21 £'m**	**Estimate 2021/22 £'m**	**Estimate 2022/23 £'m**	**Estimate 2023/24 £'m**	**Estimate 2024/25 £'m**	**Estimate 2025/26 £'m**
External Debt (including CHC)	480.3	476.8	466.8	466.8	466.8	497.7
Economic Developments	0.0	0.0	0.0	77.0	135.6	183.5
PFI Schemes/ Finance Leases	91.7	88.7	87.6	83.2	78.5	73.8
Operational Boundary	**572.0**	**565.5**	**554.4**	**627.0**	**680.9**	**755.0**

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 2020/21 £'m	Estimate 2021/22 £'m	Estimate 2022/23 £'m	Estimate 2023/24 £'m	Estimate 2024/25 £'m	Estimate 2025/26 £'m
Gross Debt *(i)*	600.5	578.3	633.3	711.8	716.5	721.2
PFI Schemes / Finance Leases	91.7	88.7	87.6	83.2	78.5	73.8
Authorised Borrowing Limit	**692.2**	**667.0**	**720.9**	**795.0**	**795.0**	**795.0**

(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 2021/22 (£667m) equals the maximum external debt forecast in any one financial year over a three year period (i.e. the 'Operational Boundary' over the period 2021/22 to 2023/24; therefore £627m for 2023/24) plus £40m.

(ii) The Authorised Borrowing Limit as reported above (£795m in 2025/26) is lower than the equivalent limit approved in the 2020/21 Treasury Management Strategy; reflecting a reduction to commercial property investment opportunity borrowing and the inclusion of the 2025/26 annual revenue charge (MRP) reducing the overall borrowing requirement.

6.22 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.

6.23 The upper and lower limits for the maturity structure of external debt in 2021/22 (with actual split as at 31 December 2020 included for comparison) are set out below:

Debt Maturity	Actual 31/12/20	Lower Limit 2021/22	Upper Limit 2021/22
Over 30 Years	26%	0%	40%
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	38%	0%	50%
Over 5 to 10 Years	28%	0%	60%
Over 1 to 5 Years	3%	0%	35%
Under 12 Months	2%	0%	25%

6.24 **Borrowing for Cash-flow Purposes:** 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:** Depending on the interest rates during 2021/22, there may be opportunities to reschedule some of the council's debt. However, if any repayment or rescheduling of existing PWLB debt was approved the rationale 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 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 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 (financial) investments are made under statutory provisions granted to the 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 the Treasury Management Panel, recommends that a continuation of the existing investment strategy be approved in 2021/22; subject to the following changes.

(1) To ensure that the Council achieves a more ethical investment policy (in line with Council's Climate Change Strategy):

(a) The inclusion of the requirement that in the future all external fund managers selected by the Council in relation to its pooled fund investments be signed up to the United Nations "Principles of Responsible Investment" (UNPRI).

(b) That internally managed investments made in the future with corporate (non-bank) organisations will adhere to the UNPRI principles.

(2) The Council approves the use of short-term Money Market Funds that operate under a Variable Net Asset Valuation, when a change from a Low Volatility Net Asset Valuation is adopted by the fund to allow continual and effective operation in a (or potential) negative interest rate environment.

(3) An increase to the maximum limit for the total invested in short-term Money Market Funds from £150m to £175m. To be utilised only in exceptional circumstances for the management of the Council's daily cash flows given the high level of investment balances currently held (see paragraph 7.4).

7.4 At 31 December 2020 the Council's investments amounted to £400.6m (**Appendix A**). In the past twelve months the Council's average investment balance was circa £375m (higher than original £280m forecast due to emergency Covid-19 funding received in 2020 ahead of actual spend) and is forecast to average around £320m throughout 2021/22.

7.5 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.

7.6 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 Group) 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.

7.7 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 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 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 2021/22 comprises:

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

7.10 **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 7.5). 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.

7.11 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 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'. 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.

7.12 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.

7.13 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 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 At 31 December 2020, 45% of the Council's internally managed investment portfolio (excluding externally managed pooled funds) is invested in short-term unsecured bank deposits and short-term money market funds in accordance with the policies as contained within the 2020/21 TMSS. The Director of Finance and Support Services confirms that the Council will not be holding any investment at 31 March 2021 that will be in breach of the recommended 2021/22 strategy.

7.15 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).

7.16 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: Assigned a **AAA** credit rating; rated by at least two of the three rating agencies and holding assets exceeding £1bn. The 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).

(e) UK Local Authorities: Assumed rating aligned with the prevailing UK sovereign rating (**AA-** as at 31 December 2020) unless an actual credit 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: 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 ('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.

7.18 **Monitoring Credit Quality:** Credit rating information is supplied by Link Group (the 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:

- 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 and Support Services, the Cabinet Member for Finance 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 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 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'.

7.21 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 7.7 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 counterparties.

7.22 The Director of Finance and Support Services 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 7.16 and 7.25).

7.23 **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 Council is however planning to undertake a procurement exercise to replace the existing treasury management system in 2021; as part of the Council's SAP replacement project. It is expected that new cash flow forecasting software will be operational from August 2021.

7.24 Cash flow forecasts are made 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. The Council also 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.

7.25 **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 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:

(a) Unsecured Bank Deposits

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
RBS 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.*

(b) Other Internally Managed Investments (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.*

(c) Externally Managed Investments

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 **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.

7.27 **Bank 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 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.

7.28 The Council accepts repo/reverse repo as a form of collateralised lending and will be approved on entering into a Global Master Repo Agreement (GMRA). 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; 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).

7.31 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 Homes England and the Regulator of Social Housing; and as providers of public services they retain a likelihood of receiving government support if needed.

7.33 **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 7.16 and 7.25) up to a maximum of £15m per company (£10m for corporates rated BBB+). Additionally, the Council will adhere to the UN's Principles of Responsible Investment (UNPRI) when approving investments with corporates.

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 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. 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.

7.39 The 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 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 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.

7.41 **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 7.16) 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:

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 amount per banking group	£25m
Maximum corporate exposure	£50m
Maximum RSL exposure (rated above A-)	£25m
Maximum money market fund exposure (excluding pooled funds)	£175m
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 2021/22; including maintaining the £100m maximum amount approved as being available for long-term investment (see paragraph 7.49):

Investment Type	**Cash Limit**
Total long-term investments (greater than one year)	£100m
Total investments with corporates rated below A-	£30m
Total investments within externally managed pooled funds, including ultra-short dated bond funds (not rated AAA);	£60m
Total investments denominated in foreign currencies	£2.8m
Total investments defined as capital expenditure	£0.2m

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. At 31 December 2020 the Council had £63.0m invested for greater than one year. The maximum monetary limit for long-term investments with any one organisation is set at £15m (£25m for individual UK local authorities).

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).

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

Treasury Indicator *(i)*	**Upper Limit 2020/21**	**Upper Limit 2021/22**	**Upper Limit 2022/23**	**Upper Limit 2023/24**	**Upper Limit 2024/25**	**Upper Limit 2025/26**
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.

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

7.51 **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 and Support Services may therefore make investments denominated in Euros up to a maximum limit of €3.1m (£2.8m equivalent based on a 1.1071 exchange rate).

7.52 **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 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 considering the Council's significant borrowing requirement in the period up to 2026, having the aim of providing the Council with a borrowing alternative to the PWLB.

7.53 **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.

7.54 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 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.

7.55 **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 companies involved. At 31 March 2020 the Council had an 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. 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.

7.56 **CIPFA Consultation on Treasury Management Code of Practice**: Statutory guidance currently issued by CIPFA and MHCLG makes clear that all treasury investments must adopt security, liquidity and yield (SLY) principles; ethical issues then play a subordinate role to those priorities. However, CIPFA plans to undertake a wider consultation in early 2021 which will include how ethical investment policies (including counterparty exposure and risk strategies) can be incorporated into the Treasury Management Code of Practice. It is anticipated that a new Code of Practice will be published in the second half of 2021/22 for adoption from April 2022. CIPFA's planned consultation in no way lessens the Council's commitment to ensure that any fund managers that we consider investing with are signed up to the UNPRI principles (see paragraph 7.3).

8 Investment Income (2021/22)

8.1 Interest forecasts provided by Link Group (**Appendix B**) show that the Bank of England's Bank Rate will remain at 0.10% throughout 2021/22 and the Director of Finance and Support Services has calculated expected investment income based on this assumption.

8.2 The Council is expected to have an average investment portfolio of £320m throughout 2021/22 (paragraph 7.4). Given the Bank Rate forecast and the continuation of the Council's 2020/21 investment strategy (including approved long-term strategic investments) it is forecast that the portfolio will attract an average interest rate of 0.66% in 2021/22. Consequently, the Council expects to receive investment income totalling £3.0m (including a £1.2m contribution from the interest smoothing reserve) as shown in the table below:

Investment	**Average Portfolio £'m**	**Interest Rate (%)**	**Interest £'m**
Liquidity Portfolio	75.0	0.01	-
Short-Term Investment Portfolio	170.0	0.19	0.3
Long-Term Investment Portfolio	75.0	2.39	1.8
Gross Interest Return	**320.0**	**0.66**	**2.1**
Less transfers to specific reserves	n/a	n/a	-0.3
Interest smoothing reserve transfer	n/a	n/a	1.2
Investment Income (2021/22)	n/a	n/a	**3.0**

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 2021/22 revenue budget, the Director of Finance and Support Services will monitor the investment income budget throughout the period and report any changes to the above forecast within Quarterly Performance Monitors (QPMs).

Katharine Eberhart
Director of Finance and Support Services

Contact Officers
Vicky Chuter, Financial Reporting Manager, 033 022 23414
Jon Clear, Treasury Management Officer, 033 022 23378

Appendices
Appendix A – West Sussex County Council - Treasury Portfolio (31/12/2020)
Appendix B – Economic and Interest Rate Forecast (Link Asset Services)

Background Papers

None