

<b>SUBJECT:</b>	<b>PRUDENTIAL INDICATORS 2021-2022 – 2024/25 AND TREASURY MANAGEMENT STRATEGY 2022/23</b>
<b>DIRECTORATE:</b>	<b>CHIEF EXECUTIVE AND TOWN CLERK</b>
<b>REPORT AUTHOR:</b>	<b>COLLEEN WARREN, FINANCIAL SERVICES MANAGER</b>

## 1. Purpose of Report

- 1.1 The purpose of the report is for Executive to review and recommend to Council for approval the adoption of the 15 statutory prudential indicators and 8 local indicators for the period 2021/22 to 2024/25 together with the 2022/23 Treasury Management Strategy.

## 2. Executive Summary

- 2.1 The table below summarises the key prudential indicators that have been incorporated into the 2022/23 strategy. The projected capital expenditure will determine the capital financing or borrowing requirement, which will in turn determine the actual level of external borrowing taken and hence, cash balances available for investment.

<b>Key Prudential Indicators</b>	<b>2021/22 Revised £'000</b>	<b>2022/23 Estimated £'000</b>	<b>2023/24 Estimated £'000</b>	<b>2024/25 Estimated £'000</b>
<b>Capital Expenditure</b>				
General Fund	11,328	19,407	1,864	683
HRA	19,668	21,721	12,918	12,673
<b>Total</b>	<b>30,996</b>	<b>41,128</b>	<b>14,782</b>	<b>13,356</b>
<b>Capital Financing Requirement</b>				
Non HRA	69,242	69,398	68,840	67,432
HRA	73,889	78,189	78,846	79,861
<b>Total</b>	<b>143,131</b>	<b>147,587</b>	<b>147,686</b>	<b>147,293</b>
<b>Net Borrowing</b>	<b>94,000</b>	<b>109,000</b>	<b>113,000</b>	<b>109,000</b>
<b>External debt (borrowing only)</b>	<b>126,000</b>	<b>139,000</b>	<b>140,000</b>	<b>136,000</b>
<b>Investments</b>				
Under one year	<b>32,000</b>	<b>30,000</b>	<b>27,000</b>	<b>27,000</b>

- 2.2 The methodology employed for selecting investment counterparties is a multi-stage formula based creditworthiness methodology provided by the Council's treasury management advisors, Link Group. The aim of the investment strategy is to generate a list of highly creditworthy counterparties, allowing the Council to maintain a diversified portfolio of investments that safeguards the cash balances whilst generating a reasonable rate of return. The Link methodology, which incorporates credit ratings, credit outlooks and watches and overlays credit default swaps as a measure of market risk, fully meets the aim of the strategy.
- 2.3 The Council is required to by statutory provision and regulation to 'have regard to' the Prudential Code when carrying out their duties in England and Wales under Part 1 of the Local Government Act 2003. An updated Prudential Code has been published in December 2021 and applies with immediate effect, except that authorities may defer introducing the revised reporting requirements until the 2023/24 financial year if they wish. The revised reporting requirements include changes to the capital strategy, prudential indicators and investment reporting. The Council has opted to defer full implementation of the revised reporting requirements until the 2023/24 financial year.

The general ongoing principles of the revised Prudential Code, including the requirement in paragraph 51 that an authority must not borrow to invest primarily for financial return, apply with immediate effect. The Council's Treasury Management Strategy has been prepared in accordance with this.

### 3. Background

- 3.1 This report covers the operation of the Council's prudential indicators, its treasury function and its likely activities for the forthcoming year. It incorporates four key Council reporting requirements:
- **Prudential and Treasury Indicators** – the reporting of the statutory prudential indicators together with local indicators, in accordance with the requirements of the CIPFA Prudential Code for Capital Finance in Local Authorities and the CIPFA Treasury Management Code of Practice.
  - **Minimum Revenue Provision (MRP) Statement** – the reporting of the MRP policy which sets out how the Council will pay for capital assets through revenue each year (as required by regulation under the Local Government Act 2003)
  - **Treasury Management Strategy** – which sets out how the Council's treasury activity will support capital decisions, the day-to-day treasury management and the limitations on activity through treasury prudential indicators. The key indicator is the **Authorised Limit**, the maximum amount of debt the Council could afford in the short term, but which would not be sustainable in the longer term. This is the Authorised Borrowing Limit required by s3 of the Local Government Act 2003 and is in accordance with the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code.
  - **Investment Strategy** – this is included within the Treasury Management Strategy and sets out the criteria for choosing investment counterparties

and limiting exposure to the risk of loss. It is reported annually (in accordance with Department for Levelling Up, Housing and Communities (DLUHC) Investment Guidance).

#### 4. Treasury Management Requirements 2022/23

##### 4.1 The Capital Prudential Indicators 2021/22 – 2024/25

4.1.1 The Council's capital expenditure plans are one of the key drivers of treasury management activity. The outputs of the capital expenditure plans are reflected in prudential indicators, which are designed to assist members to overview and confirm capital expenditure plans. The Local Government Act 2003 requires the Council to adopt the CIPFA Prudential Code and to produce prudential indicators. The Prudential Code requires the Council to approve as a minimum the statutory indicators and limits. This report revises the indicators for 2021/22 and details them for 2022/23 to 2024/25. An explanation and calculation of each Prudential Indicator is provided in **Appendix 1** and the key messages summarised in section 4.1.3.

##### 4.1.2 Capital Expenditure and Financing

The Council's capital expenditure plans (as detailed in the Draft MTFS 2022-27) are summarised below. Capital expenditure can be paid for immediately (by resources such as capital receipts, capital grants or revenue resources) but if these resources are insufficient, any residual capital expenditure will form a borrowing need. This can be supported by government grant for the repayment of debt (very limited support available) or can be unsupported (prudential borrowing) where the Council needs to identify the resources to finance and repay debt through its own budget.

<b>Indicators 1&amp;2</b>	<b>2021/22 Revised £'000</b>	<b>2022/23 Estimated £'000</b>	<b>2023/24 Estimated £'000</b>	<b>2024/25 Estimated £'000</b>
<b>Capital Expenditure</b>				
General Fund	11,328	19,407	1,864	683
HRA (including New Build)	19,668	21,721	12,918	12,673
<b>Total Expenditure</b>	<b>30,996</b>	<b>41,128</b>	<b>14,782</b>	<b>13,356</b>
<b>Financed by:</b>				
Borrowing	6,950	11,359	1,843	1,398
Capital Receipts	1,778	4,325	438	677
Capital Grants and Contributions	13,832	10,106	678	300
Major Repairs Reserve	5,494	8,941	8,657	8,815
Revenue Contributions	2,942	6,397	3,166	2,166
<b>Total Financing</b>	<b>30,996</b>	<b>41,128</b>	<b>14,782</b>	<b>13,356</b>

##### 4.1.3 The Council's Borrowing Need - the Capital Financing Requirement (CFR)

The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either capital or revenue resources. It is essentially a measure of the Council's underlying borrowing need. Based on the capital expenditure plans in

paragraph 4.1.2 the CFR for 2021/22 to 2024/25 is projected to be:

<b>Indicators 3&amp;4</b>	<b>2021/22 Revised £'000</b>	<b>2022/23 Estimated £'000</b>	<b>2023/24 Estimated £'000</b>	<b>2024/25 Estimated £'000</b>
<b>Capital Financing Requirement</b>				
General Fund	69,242	69,398	68,840	67,432
HRA	73,889	78,189	78,846	79,861
<b>Total CFR @ 31 March</b>	<b>143,131</b>	<b>147,587</b>	<b>147,686</b>	<b>147,293</b>
<b>Net movement in CFR</b>	<b>5,356</b>	<b>4,456</b>	<b>99</b>	<b>(393)</b>
Actual debt (borrowing & other liabilities)	126,000	139,000	140,000	136,000
Net borrowing need for the year	7,100	6,170	1,843	1,399
Minimum Revenue Provision (MRP)	(1,594)	(1,714)	(1,744)	(1,792)
Application of Capital Receipts	(150)	0	0	0
<b>Movement in CFR</b>	<b>5,356</b>	<b>4,456</b>	<b>99</b>	<b>(393)</b>

The CFR also includes any other long term liabilities (e.g. finance and embedded leases) brought onto the balance sheet. Whilst this increases the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility, so the Council is not required to separately borrow for them. The Council has no such leases within the CFR in 2021/22. The CFR does not yet include any allowance for the planned replacement of the majority of the vehicle fleet under leasing. Once the final cost of the replacement fleet is established the CFR will be increased to reflect a borrowing requirement for the replacement fleet. This will also increase the MRP charge annually during the lifetime of the lease arrangements.

In future years all lease liabilities, including some of those currently treated as operating leases and expensed through revenue, will be 'on balance sheet' which will increase the CFR. With the exception of the new leased fleet it is not considered that any of the council's existing arrangements will be on balance sheet at the point of transition.

**4.1.4 Limits on Borrowing** – In order to ensure that borrowing decisions are based on consideration of affordability, prudence and sustainability and that treasury management decisions are taken in accordance with good professional practice, in full understanding of the risks involved and how these risks will be managed to levels that are acceptable to City of Lincoln Council, the Prudential Code requires that Council's set limits on borrowing activity.

**Limiting Borrowing for Capital Purposes** - the Council needs to ensure that its total borrowing net of any investments, does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years. The Chief Finance Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future.

**Operational Boundary for External Debt** – boundary based on the expected maximum external debt during the course of the year.

**Authorised Limit for External Debt** - represents the limit beyond which external debt is prohibited. It represents the level of debt, which while not desired, could be afforded in the short term, but is unsustainable in the long term. This limit needs to be set or revised by full Council.

The level of the proposed operational and authorised limits is based on an assessment of the level of borrowing required to meet the Capital Financing Requirement (CFR) and also an allowance for temporary borrowing for working capital and also in lieu of other capital financing sources (e.g. capital receipts). Financial modelling has been carried out for both and the affordability and sustainability of the potential borrowing requirement has been assessed and can be contained within the Draft MTF5 2022-27. This is reflected in the table below and in the Prudential Indicators 7 and 8 tables in Appendix 1.

<b>Indicator 7</b>	<b>2021/22 Revised £'000</b>	<b>2022/23 Estimated £'000</b>	<b>2023/24 Estimated £'000</b>	<b>2024/25 Estimated £'000</b>
<b>Authorised limit</b>				
Borrowing	138,428	156,991	153,511	148,051
Other long term liabilities	1,380	1,380	1,380	1,380
<b>Total Authorised limit</b>	<b>139,808</b>	<b>158,371</b>	<b>154,891</b>	<b>149,431</b>

## 4.2 Minimum Revenue Provision (MRP) Policy

- 4.2.1 The Council is required to pay off an element of the accumulated General Fund borrowing each year (the CFR) through a revenue charge - the Minimum Revenue Provision (MRP), and is also allowed to undertake additional voluntary payments (VRP). No revenue charge is currently required for the HRA. However, under self-financing, the HRA is now required to charge depreciation on its assets, which has been built into the revenue charges in the HRA 30 year Business Plan.

The Department for Levelling Up, Homes and Communities have issued statutory guidance on the options available for making prudent provision for the repayment of debt. The Council must have regard to this guidance. The guidance is not prescriptive and makes it clear that councils can follow an alternative approach, provided they still make a prudent provision. The broad aim of a 'prudent provision' is to ensure that debt is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits to service delivery.

Guidance issued by the Secretary of State requires that before the start of each financial year the Council prepares a statement of its policy on making MRP in respect of the forthcoming financial year and submits it to Full Council for approval. There has been no amendment to the proposed MRP policy for 2022/23.

The MRP policy statement is set out in **Appendix 2**.

### 4.3 The Treasury Management Strategy 2022/23

4.3.1 Treasury Management is an important part of the overall financial management of the Council's affairs. The treasury management service performs the borrowing and investment activities of the Council and effectively manages the associated risks. Its activities are strictly regulated by statutory requirements and a professional code of practice (the CIPFA Code of Practice on Treasury Management). The Treasury Management Policy and Practices and the annual Treasury Management Strategy provides the operational rules and limits by which day to day treasury management decisions are made.

4.3.2 The Treasury Management Strategy for 2022/23 is attached at **Appendix 3**. The strategy outlines expected treasury activity for the coming year and expected prudential indicators relating the treasury management for the next three years. The key principals in the strategy are summarised below.

- **Debt and Investment Projections (Treasury Management Strategy section 2)** – based on the budgeted borrowing requirements, estimated balances and cash flow, year-end debt and investment projections are:

	2021/22 Revised £'000	2022/23 Estimated £'000	2023/24 Estimated £'000	2024/25 Estimated £'000
<b>External Debt</b>				
Debt at 31 March (including other long term liabilities)	126,000	139,000	140,000	136,000
<b>Investments</b>				
Total Investments at 31 March	32,000	30,000	27,000	27,000

- **Expected Movement in Interest Rates (Treasury Management Strategy section 3)** - the forecast for Bank Rate is that this will be at or above 1% by the end of 2022.
- **Borrowing & Debt Strategy (Treasury Management Strategy section 4)** - The main aims are:
  - To reduce the revenue costs of debt
  - To manage the Council's debt maturity profile
  - To effect funding at the cheapest cost commensurate with future risk
  - To forecast average future interest rates and borrow accordingly
  - To proactively reschedule debt in order to take advantage of potential savings as interest rates change.
  - To manage the day-to-day cash flow of the Authority in order to, where possible, negate the need for short-term borrowing.
- **Investment Strategy (Treasury Management Strategy section 5)** - The Council's investment strategy primary objectives are safeguarding the repayment of the principal and interest of its investments on time, then ensuring adequate liquidity, with investment return being the final objective.

The current investment climate continues to present one over-riding risk consideration, that of counterparty security risk. In order to fully consider counterparty risk factors when selecting investment counterparties, the Council employs the multi-stage formula based creditworthiness methodology provided by the Council's treasury management advisors, Link Group. This methodology, developed by Link, uses credit ratings as the core criteria but also incorporates other market information on a mathematical basis. The methodology is continuously reviewed and changes are made in response to changes made by the credit rating agencies. There haven't been any major changes made to the credit rating methodology since last year's change when any reference to the implied levels of sovereign support (which were phased out last year) were taken out. The current methodology is explained in detail in the Council's Investment Strategy 2022/23 in **Section 5 of Appendix 3**.

The aim of the investment strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoidance of concentration risk (i.e. placing a large proportion of investments with a small number of counterparties). The intention of the strategy is to provide security of investment and minimisation of risk.

Investment instruments identified for use are listed in **Appendix 3** under the specified and non-specified investments categories. Counterparty limits will be as shown in **Appendix 3**. Examples of institutions which currently fall under the various colour coded categories are as follows:

- Blue (part-government owned - 1 year)
- Orange (1 year)
- Green (100 days)
- Yellow (5 years) – Local Authorities.

Sole reliance will not be placed on the use of this external service. In addition, officers will also use market data and market information, information on government support for banks and the credit ratings of that supporting government.

The criteria to be used to select investment counterparties are set out in Appendix 3. These include:-

- Maintenance of a counterparty list with approved credit ratings and time and principal limits
  - Regular monitoring of counterparties with the help of the Council's treasury management advisors
  - Limits on the amounts on non-specified investments (e.g. over 1 year investments)
  - Limits on non-UK counterparties
- **Risk Benchmarking** – The revised CIPFA Code and the CLG Investment Guidance adopted 2<sup>nd</sup> March 2010 introduced the consideration and approval of security and liquidity benchmarks. The Investment Strategy for 2022/23 includes the following benchmarks for liquidity and security:-

*Liquidity* – The Council’s bank overdraft limit is nil. The Council will seek to maintain liquid short-term deposits of at least £5,000,000 available with a week’s notice. The weighted average life (WAL) of investments is expected to be 0.08 years as investments are kept in accounts of less than 365 days maturity.

*Security* – the Council’s expected security risk benchmark from its budgeted investment strategy is 0.012% historic risk of default when compared to the whole portfolio. This means that the risk amounts to approximately £0.002m on the expected investment portfolio of £18 million. Money Market Funds are not subject to historic risk of default.

- **Treasury Limits on Activity (Treasury Management Strategy section 6)** – This section includes statutory and local indicators covering treasury management activity. These include limits on fixed and variable interest rate exposure, maturity structure of debt and performance targets for interest rates on new investments and loans.
- **Breakdown of Investment Categories (Treasury Management Strategy section 7)** – covers authorised posts for treasury management activities.

The need to limit the risk to the Council of loss from counterparty failure results in a restricted range of counterparties available for investment.

#### **4.4 Treasury Management Practices**

The Council adopted the CIPFA Code of Practice on Treasury Management (revised December 2017) on 2<sup>nd</sup> March 2010. The Treasury Management Policy Statement was also adopted at this time. The Treasury Management Policy and Practices (TMP’s) are updated annually to reflect the Treasury Management Strategy approved by Council and to reflect any changes in staffing structures or working practices of the treasury function and are attached as Appendix 4.

### **5. Strategic Priorities**

- 5.1 The budget process sets the resources in support of the Council’s Strategic Priorities and determines the Service Plans for the year ahead. Effective scrutiny of the budget process should support the Executive in reaching the right decisions with regard to finances.

### **6. Organisational Impacts**

#### **6.1 Finance**

Financial implications are contained in the main body of the report.

#### **6.2 Legal Implications including Procurement Rules**

The powers for a local authority to borrow and invest are governed by the Local Government Act 2003 (LGA 2003) and associated Regulations. A local authority may borrow or invest for any purpose relevant to its functions, under any enactment,



or for the purpose of the prudent management of its financial affairs. The Regulations also specify that authorities should have regard to the CIPFA Treasury Management Code and the MHCLG Investment Guidance when carrying out their treasury management functions.

### 6.3 Equality, Diversity and Human Rights

The Public Sector Equality Duty means that the Council must consider all individuals when carrying out their day-to-day work, in shaping policy, delivering services and in relation to their own employees.

It requires that public bodies have due regard to the need to:

- Eliminate discrimination
- Advance equality of opportunity
- Foster good relations between different people when carrying out their activities.

Due to the nature of the report, no specific Equality Impact Analysis is required.

## 7. Risk Implications

The Local Government Act 2003, the Prudential Code and the Treasury Management Code of Practice include a key principal that an organisations appetite for risk is included in their annual Treasury Management Strategy and this should include any use of financial instruments for the prudent management of those risks, and should ensure that priority is given to security and liquidity when investing.

## 8. Recommendations

8.1 The Executive are recommended to:

8.2 Review and recommend to full Council the prudential indicators detailed in section 4.1 and appendix 1 of the report.

8.3 Review and recommend to full Council the Treasury Management Strategy (including the treasury management prudential indicators and the Investment Strategy) set out section 4 and appendix 3 of the report.

8.4 Review and recommend to full Council the MRP policy in appendix 2 of the report.

8.5 Review and recommend to full Council the Treasury Management Practices in Appendix 4.

8.6 To note the minutes from Audit Committee at Appendix 5.

**Is this a key decision?** No

**Do the exempt information categories apply?** No

**Does Rule 15 of the Scrutiny Procedure Rules (call-in and urgency) apply?** No

**How many appendices does the report contain?** 5

**List of Background Papers:** Medium Term Financial Strategy 2022-27  
CIPFA Code of Practice  
CIPFA Prudential Code  
Treasury Management Practices

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## **Prudential Indicators 2021/22 – 2024/25**

### **1.0 Introduction**

1.1 The Local Government Act 2003 requires the Council to adopt the CIPFA Prudential Code and to produce prudential indicators. The Code sets out a framework for self-regulation of capital spending, in effect allowing councils to invest in capital projects without any limit as long as they are affordable, prudent and sustainable. The Prudential Code operates by the provision of prudential indicators, which highlight particular aspects of the capital expenditure planning. This report revises the indicators for 2021/22 and details them for 2022/23-2024/25. Each indicator either summarises the expected capital activity or introduces limits upon the activity, and reflects the outcomes of the Council's underlying capital appraisal systems.

1.2 The Prudential Code requires the Executive and full Council to approve as a minimum the 15 statutory indicators. The Chief Finance Officer has added 8 local indicators that are believed to add value and assist understanding of the main indicators.

1.3 The purpose of the indicators is to provide a framework for capital expenditure decision-making. It highlights, through the prudential indicators, the level of capital expenditure, the impact on borrowing and investment levels and the overall controls in place to ensure the activity remains affordable, prudent and sustainable.

1.4 Within this overall capital expenditure framework there is a clear impact on the Council's treasury management activity, either through increased borrowing levels or the investment of surplus balances. As a consequence the treasury management strategy for 2022/23 (see Appendix 3) includes the expected treasury management activity, together with the 5 specific Prudential indicators and 8 local indicators, which relate to treasury management.

1.5 The 15 statutory prudential indicators can be categorised under the following four headings:

- Capital Expenditure and External Debt (numbers 1, 2, 3, 4, 5, 7, 8)
- Prudence (number 6)
- Affordability (numbers 9,10)
- Treasury Management limits (numbers 11, 12, 13, 14, 15)

(The numbers above relate to the reference given to each indicator).

1.6 The paragraphs 2 to 4 below detail the 10 statutory indicators under the headings of Capital Expenditure/External Debt, Prudence and Affordability. The remaining 5 statutory and 8 local indicators relating to the treasury management strategy are set out in appendix 3.

### **2.0 Capital Expenditure Prudential Indicators**

2.1 The Council's capital expenditure plans are summarised below and this forms the

first of the prudential indicators. This expenditure can be paid for immediately (by resources such as capital receipts, capital grants etc.), but if resources are insufficient any residual expenditure will form a borrowing need.

2.2 A certain level of capital expenditure may be supported by government grant; any decisions by Council to spend above this level will be unsupported and will need to be paid for from the Council's own resources. This unsupported capital expenditure needs to have regard to:

- Service objectives e.g. strategic planning
- Stewardship of assets e.g. asset management planning
- Value for money
- Prudence and sustainability e.g. implications for external borrowing and whole life costing
- Affordability
- Practicality e.g. achievability of plan

The revenue consequences of capital expenditure, particularly the unsupported expenditure, will need to be paid for from the Council's own resources.

The Government retains an option to control either the total of all councils' plans, or those of a specific council, although no control has yet been required.

2.3 The key risks to the plans are that some estimates for sources of funding, such as capital receipts, may be subject to change over this timescale. For instance, anticipated asset sales may be postponed due to the impact of the recession on the property market.

2.4 The summary capital expenditure and financing projections are shown in the table below.

<b>Indicators 1&amp;2</b>	<b>2021/22 Revised £'000</b>	<b>2022/23 Estimated £'000</b>	<b>2023/24 Estimated £'000</b>	<b>2024/25 Estimated £'000</b>
<b>Capital Expenditure</b>				
General Fund	11,328	19,407	1,864	683
HRA (including New Build)	19,668	21,721	12,918	12,673
<b>Total Expenditure</b>	<b>30,996</b>	<b>41,128</b>	<b>14,782</b>	<b>13,356</b>
<b>Financed by:</b>				
Capital receipts	1,778	4,325	438	677
Capital grants & contributions	13,832	10,106	678	300
Depreciation (HRA only)	5,494	8,941	8,657	8,815
Revenue/Reserve				
Contributions	2,942	6,397	3,166	2,166
Borrowing need	6,950	11,359	1,843	1,398

### 3.0 External Debt and Prudence Prudential Indicators

3.1 **Borrowing Need** - The Council's Capital Financing Requirement (CFR) represents the Council's borrowing need. The CFR is simply the total outstanding capital expenditure, which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. The capital expenditure above which has not immediately been paid for will increase the CFR.

3.2 The CFR also includes any other long term liabilities (e.g. finance and embedded leases) brought on to the balance sheet. Whilst this increases the CFR, and therefore the Council's borrowing requirement, they are purely accounting adjustments and include a borrowing facility, so the Council is not required to separately borrow for them. The Council has no such leases within the CFR in 2021/22. The CFR does not yet include any allowance for the planned replacement of the majority of the vehicle fleet under leasing arrangements.

3.3 Capital Financing Requirement projections are detailed below:

Indicators 3&4	2021/22 Revised £'000	2022/23 Estimated £'000	2023/24 Estimated £'000	2024/25 Estimated £'000
<b>Capital Financing Requirement</b>				
General Fund	69,242	69,398	68,840	67,432
HRA	73,889	78,189	78,846	79,861
<b>Total CFR @ 31 March</b>	<b>143,131</b>	<b>147,587</b>	<b>147,686</b>	<b>147,293</b>
<b>Net movement in CFR</b>	<b>5,356</b>	<b>4,456</b>	<b>99</b>	<b>(393)</b>
Actual debt (borrowing & other liabilities)	126,000	139,000	140,000	136,000
Net borrowing need for the year	7,100	6,170	1,843	1,399
Minimum Revenue Provision (MRP)	(1,594)	(1,714)	(1,744)	(1,792)
Application of Capital Receipts	(150)	0	0	0
<b>Movement in CFR</b>	<b>5,356</b>	<b>4,456</b>	<b>99</b>	<b>(393)</b>

\* MRP = Minimum Revenue Provision – Statutory requirement to annually fund the repayment of General Fund borrowing.

3.4 **Estimates of External Debt** - The expected impact of the capital expenditure decisions on the Council's net debt position is shown below:

<b>Indicator 5</b>	<b>2021/22 Revised £'000</b>	<b>2022/23 Estimated £'000</b>	<b>2023/24 Estimated £'000</b>	<b>2024/25 Estimated £'000</b>
<b>External Debt</b>				
Gross Borrowing	126,000	139,000	140,000	136,000
Other Long Term Liabilities*	0	0	0	0
<b>Total Debt at 31 March</b>	<b>126,000</b>	<b>139,000</b>	<b>140,000</b>	<b>136,000</b>

\*Other Long Term liabilities include finance leases

3.5 The expected movement in the CFR over the next three years is dependent on the level of capital borrowing taken during the budget cycle. Such borrowing is the capital expenditure freedom allowed under the Prudential Code i.e. prudential borrowing which allows the freedom to enter into projects such as spend to save schemes, or decisions to allocate additional resources from revenue to capital to enable service enhancements (subject to affordability).

3.6 There are two limiting factors on the Council's ability to undertake prudential borrowing:

1. Whether the revenue resource is available to support in full the implications of capital expenditure, both borrowing costs and running costs. Can the Council afford the implications of the capital expenditure?
2. The Government may use a long stop control to ensure that either the total of all the Councils' plans do not jeopardise national economic policies, or in the event of an assessment by Central Government that local plans are unaffordable at a council, it may implement a specific control to limit its capital expenditure plans. No such control has been implemented during 2021/22.

3.7 **Limits to Borrowing Activity** - Within the prudential indicators there are a number of key indicators to ensure the Council operates its activities within well-defined limits.

3.8 For the first of these the Council needs to ensure that its total borrowing net of any investments, does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2022/23 and next two financial years. This allows some flexibility for limited early borrowing for future years but ensures that borrowing is not undertaken for revenue purposes.

<b>Indicator 6</b>	<b>2021/22 Revised £'000</b>	<b>2022/23 Estimated £'000</b>	<b>2023/24 Estimated £'000</b>	<b>2024/25 Estimated £'000</b>
Gross Borrowing	126,000	139,000	140,000	136,000
Investments	32,000	30,000	27,000	27,000
Net Borrowing	94,000	109,000	113,000	109,000
CFR	143,131	147,587	147,685	147,292
Net Borrowing is below CFR	<b>49,131</b>	<b>38,587</b>	<b>34,685</b>	<b>38,292</b>

The Chief Finance Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

3.9 A further two key prudential indicators control or anticipate the overall level of borrowing, these are:

- **The Authorised Limit for External Debt** – This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by full Council. It reflects the level of external debt, which while not desired, could be afforded in the short term, but is not sustainable in the longer term. This is the 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 no control has yet been exercised.
- **The Operational Boundary for External Debt** – This indicator is based on the expected maximum external debt during the course of one year; it is not a limit and actual borrowing could vary around the boundary for short times during the year.

The level of the proposed operational and authorised limits is based on an assessment of the level of borrowing required to meet the Capital Financing Requirement (CFR) and also an allowance for temporary borrowing for working capital and also in lieu of other capital financing sources (e.g. capital receipts). The affordability and sustainability of the borrowing requirement for both have been assessed and can be contained within the Draft MTFS 2022-27. The operational and authorised limits for 2021/22 have been set to allow these.

<b>Indicator 7</b>	<b>2021/22 Revised £'000</b>	<b>2022/23 Estimated £'000</b>	<b>2023/24 Estimated £'000</b>	<b>2024/25 Estimated £'000</b>
<b>Authorised Limit</b>				
Borrowing	138,428	156,991	153,511	148,051
Other long term liabilities*	1,380	1,380	1,380	1,380
<b>Total Authorised Limit</b>	<b>139,808</b>	<b>158,371</b>	<b>154,891</b>	<b>149,431</b>

<b>Indicator 8</b>	<b>2021/22 Revised £'000</b>	<b>2022/23 Estimated £'000</b>	<b>2023/24 Estimated £'000</b>	<b>2024/25 Estimated £'000</b>
<b>Operational Boundary</b>				
Borrowing	135,738	148,523	149,453	145,228
Other long term liabilities*	1,200	1,200	1,200	1,200
<b>Total Operational Boundary</b>	<b>136,938</b>	<b>149,723</b>	<b>150,653</b>	<b>146,428</b>

\*Other Long Term liabilities include finance leases

- 3.10 **Borrowing in advance of need** – The Council has some flexibility to borrow funds this year for use in future years. The Chief Finance Officer may do this under delegated power where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or meet budgetary constraints. Whilst the Chief Finance Officer will adopt a cautious approach to any such borrowing, where there is a clear business case for doing so borrowing may be undertaken to fund the approved capital programme or to fund future debt maturities. Borrowing in advance will be made within the constraints that:
- It will be limited to no more than 75% of the expected increase in borrowing need (CFR) over the three year planning period; and
  - Would not look to borrow more than 36 months in advance of need
- 3.11 Risks associated with any advance borrowing activity will be subject to appraisal in advance and subsequent reporting through the mid-year or annual reporting mechanism.

#### **4.0 Affordability Prudential Indicators**

- 4.1 The 8 statutory indicators above cover the overall capital and control of borrowing, but in addition, within this framework, there are further indicators that assess the affordability of the capital investment plans. These indicators provide an indication of the impact of the capital investment plans on the Council's overall finances. For 21/22 and 22/23 the figures used to calculate these indicators have been adjusted to reflect one-off adjustments in respect of business rates as a result of the Covid 19 pandemic. The adjusted calculations are shown below:

<b>Indicators 9 &amp; 10</b>	<b>2021/22 Revised</b>	<b>2022/23 Estimated</b>	<b>2023/24 Estimated</b>	<b>2024/25 Estimated</b>
General Fund	26.8%	23.8%	23.9%	25.1%
HRA	31%	30.1%	29.5%	28.9%



### **Minimum Revenue Provision (MRP) Policy**

1.0 The Council is required to pay off an element of the accumulated General Fund borrowing each year through a revenue charge (the Minimum Revenue Provision), and is also allowed to undertake additional voluntary payments (VRP).

1.1 DLUHC Regulations have been issued which require full Council to approve an MRP Statement in advance of each year. A variety of options are provided so long as there is a prudent provision. The MRP policy takes into account recent changes to guidance issued by DHLUC.

1.2 Members are recommended to approve the following MRP Statement:

For capital expenditure incurred:

(A) Before 1<sup>st</sup> April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will be:

**Existing practice** - MRP will follow the existing practice outline in former CLG Regulations, but on a 2% straight-line basis, i.e. provision for the full repayment of debt over 50 years;

(B) From 1<sup>st</sup> April 2008 for all unsupported borrowing (including finance leases) the MRP policy will be:

**Asset Life Method** – MRP will be based on the estimated life of the assets on either a straight line or annuity basis (as deemed most appropriate for capital expenditure being financed through borrowing). Asset life is deemed to begin once the asset becomes operational. MRP will commence from the financial year following the one in which the asset becomes operational.

MRP in respect of unsupported borrowing taken to meet expenditure, which is treated as capital expenditure by virtue of either a capitalisation direction or regulations, will be determined in accordance with the asset life method as recommended by the statutory guidance.

(C) The Council has set aside £750k of capital receipts to the Capital Adjustment Account instead of applying these receipts to new expenditure in order to reduce the total debt liability (£150k per annum over the period 2017/18 to 2021/22). The Council will reduce the MRP provision for the year by the same amount. The application of these capital receipts to the Capital Adjustment Account will be complete in 2021/22 and will not apply to 2022/23 and future years.

## **Treasury Management Strategy 2022/23**

### **1.0 Introduction**

- 1.1 Treasury Management is an important part of the overall financial management of the Council's affairs. Its importance has increased as a result of the freedoms provided by the Prudential Code. The prudential indicators in Appendix 1 cover the affordability and impact of capital expenditure decisions and set out the Council's overall capital framework. The treasury service considers the effective funding of these decisions. Together they form part of the process which ensures the Council meets its balanced budget requirement under the Local Government Finance Act 1992. There are 5 specific statutory treasury management prudential indicators and 8 local indicators.
- 1.2 The treasury management service performs the borrowing and investment activities of the Council and effectively manages the associated risks. Its activities are strictly regulated by statutory requirements and a professional code of practice (the CIPFA Code of Practice on Treasury Management - Revised December 2017). The adoption of the Code is one of the 12 statutory Prudential Indicators. This Council adopted the Code of Practice on Treasury Management on 2<sup>nd</sup> March 2010. As a result of adopting the Code, the Council also adopted a Treasury Management Policy Statement on 2<sup>nd</sup> March 2010.
- 1.3 The policy requires an annual strategy to be reported to Council outlining the expected treasury activity for the forthcoming year and includes prudential indicators relating specifically to Treasury Management for the next three years. Further reports are produced; a mid-year monitoring report and a year-end report on actual activity for the year (Annual Treasury Management Stewardship Report). In addition, Treasury Management Practice (TMPs) documents are also maintained by the Chief Finance Officer. The TMPs have been reviewed and updated to reflect any changes in the Treasury Management Strategy and are attached as appendix 4.
- 1.4 A key requirement of this report is to explain both the risks, and the management of the risks, associated with the treasury service. This strategy covers:
- The Council's debt and investment projections;
  - The expected movement in interest rates;
  - The Council's borrowing strategy;
  - The Council's investment strategy;
  - Treasury Management prudential indicators and limits on activity;
  - Local Treasury issues

### **2.0 Debt and Investment Projections 2021/22 – 2024/25**

- 2.1 The borrowing requirement comprises the expected movement in the Capital Financing Requirement (CFR) and any maturing debt that will need to be re-financed. The table below shows the anticipated effect on the treasury position over the current and next three years based on the current capital programme.

The expected maximum debt position during each year represents the Operational Boundary prudential indicator (for borrowing only) and so may be different from the year-end position. It also highlights the expected change in investment balances.

	2021/22 Revised £'000	2022/23 Estimated £'000	2023/24 Estimated £'000	2024/25 Estimated £'000
<b>External Debt</b>				
Debt at 1 April	123,448	125,738	138,523	139,453
Expected change in debt	2,290	12,785	930	(4,225)
Debt at 31 March	<b>125,738</b>	<b>138,523</b>	<b>139,453</b>	<b>135,228</b>
Operational Boundary (debt only)	135,738	148,523	149,453	145,228
<b>Investments</b>				
Total Investments at 31 March	32,000	30,000	27,000	27,000
Investment change	(3,000)	(2,000)	(3,000)	0

Expected borrowing has been profiled to take out loans before current low borrowing interest rates are forecast to rise significantly.

2.2 The related impact of the above movements on the revenue budgets are:

	2021/22 Revised £'000	2022/23 Estimated £'000	2023/24 Estimated £'000	2024/25 Estimated £'000
<b>Revenue Budgets</b>				
Total interest payable on borrowing	3,975	4,040	4,200	4,215
Related HRA charge	2,500	2,580	2,650	2,665
Net General Fund interest payable	1,475	1,460	1,550	1,550
Total investment income	27,247	123,710	129,820	146,640
Related HRA income share	9,290	66,220	65,610	72,150
Net General Fund income	17,957	57,490	64,210	74,490

### 3.0 Prospects for Interest Rates

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives the Link central view and paragraph 3.1 gives Link's view on economic prospects.

Annual Average %	Bank Rate	PWLB Rates*		
		5 year	25 year	50 year
March 2021	0.25	1.50	1.90	1.70
March 2022	0.75	2.20	2.40	2.20
March 2023	1.25	2.30	2.60	2.40
March 2024	1.25	2.30	2.60	2.40

\* Borrowing Rates

Over the last two years, the coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16<sup>th</sup> December and then to 0.50% at its meeting of 4<sup>th</sup> February 2022..

As shown in the forecast table above, the forecast for Bank Rate now includes a further three increases of 0.25%, in March, May and November 2022 to end at 1.25%

#### **4.0 The Council's Borrowing and Debt Strategy 2022/23**

- 4.1 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the CFR), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is high and will be maintained for the borrowing.
- 4.2 Against this background and the risks within the economic forecast, caution will be adopted with the 2022/23 treasury operations. The Chief Finance Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances as follows.
- 4.3 If it was felt that there was a significant risk of a sharp fall in long term rates e.g. due to a marked increase of risks around a relapse into recession or of risks of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- 4.4 If it was felt that there was a significant risk of a much sharper rise in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates remain low.
- 4.5 The Council's overall core borrowing objectives will remain uniform and follow a similar pattern to previous years as follows:
- To reduce the revenue costs of debt in line with the targets set for the Chief Finance officer (see local indicators).
  - To manage the Council's debt maturity profile, leaving no one future year with a high level of repayments that might cause problems in re-borrowing.
  - To effect funding at the cheapest cost commensurate with future risk.
  - To forecast average future interest rates and borrow accordingly i.e. short term/variable when rates are 'high', long term/fixed when rates are 'low'.
  - To monitor and review the level of variable rate loans in order to take greater advantage of interest rate movements.
  - To proactively reschedule debt in order to take advantage of potential savings as interest rates change. Each rescheduling exercise will be considered in terms of the effect of premiums and discounts on the

General Fund and the Housing Revenue Account.

- To manage the day-to-day cash flow of the Council in order to, where possible, negate the need for short-term borrowing. However, short-term borrowing will be incurred, if it is deemed prudent to take advantage of good investment rates.

4.7 There is unsupported borrowing in the General Fund Investment Programme (GIP) as detailed in the Capital Strategy – the requirement to produce a Capital Strategy was introduced in 2018. The Council expects to take out loans for the General Fund however, will continue to use internal balances whilst interest rates on investments remain low. Officers are continually evaluating the cost effectiveness of borrowing as opposed to selling capital assets. Proposals are presented to Members when borrowing becomes more cost effective.

4.8 During the next MTFS period borrowing is planned for the HRA investment programme.

4.9 The strategy allows for additional borrowing in line with the expected movement in the Capital Financing Requirement (CFR), should it become necessary for cash flow requirements. The Council will consider PWLB loans, Market loans, the Municipal Bond Agency and other financial institutions, if attractive rates are offered. In addition, should schemes be identified that benefit the Council's strategic aims and be deemed cost effective, i.e. Invest to Save schemes where the income streams more than pay for the borrowing costs, unsupported borrowing will be considered.

## **5.0 The Council's Investment Strategy 2022/23**

5.1 The Council's investment strategy's primary objectives are safeguarding the repayment of the principal and interest of its investments on time, ensuring adequate liquidity, with the investment return being the final objective.

The intention of the strategy is to provide security of investment and minimisation of risk.

The aim of the strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoidance of concentration risk.

In line with this aim, the Council will ensure:

- It maintains a policy covering the types of specified and unspecified investments it will invest in, criteria for choosing investment counterparties with adequate security and monitoring their security. This is set out in the paragraphs below.
  - Specified Investments – these are high security investments (i.e. high credit quality) and high liquidity investments in sterling with a maturity of no more than one year.
  - Non-specified Investments – investments that do not fall into the category of Specified Investments, representing a potential greater risk (e.g. over one year).

- It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the 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.

## 5.2 Risk benchmarking

Yield benchmarks are widely used to assess investment performance. Discrete security and liquidity benchmarks are also requirements to Treasury Management reporting, although the application of these is more subjective in nature. Additional background in the approach taken is shown at the end of this appendix.

- 5.3 These benchmarks are simple guides to maximum risk and so may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that officers will monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the Mid-Year or Annual Report.

## 5.4 Security

The Council's expected security risk benchmark for the current portfolio, when compared to these historic default tables, is:

- 0.012% historic risk of default when compared to the whole portfolio.

## 5.5 Liquidity

In respect of this area the Council seeks to maintain:

- Bank overdraft - £nil.
- Liquid short term deposits of at least £5 million available with a week's notice.
- Weighted Average Life benchmark is expected to be 0.08 years.

## 5.6 Yield

Local measure of yield benchmark employed is:

- Investments – return above the appropriate SONIA rate – This measure has been revised following the cessation of the use of LIBOR and associated LIBID rates at the end of 2021.

## 5.7 Investment Counterparty Selection Criteria

The primary principle governing the Council's investment criteria is the security of its investments although the yield or return on the investment is also a key consideration. After this main principle the Council will ensure:

- It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the

## Specified and Non-Specified investment sections below.

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

- 5.8 The Chief Finance Officer will maintain a counterparty list in compliance with the criteria set out in the table contained within this appendix and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to that which chooses Specified and Non-Specified investments as they provide an overall pool of counterparties considered high-quality which the Council may use rather than defining what its investments are.
- 5.9 Following the reductions to the Council's grant funding settlement and ongoing financial pressures, the identification of savings and income generation are critical to the delivery of the Medium Term Financial Strategy. Treasury Management is an important area for further income generation and therefore, the main theme of the Council's investment strategy must continue to be to maximise interest from investments, after ensuring adequate security and liquidity. The Investment Strategy 2022/23 seeks to achieve this objective by establishing a pool of counterparties available for investment whilst still containing overall risk within acceptable levels.
- 5.10 The Council uses Link Group' creditworthiness service. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies – Fitch, Moody's and Standard and Poor's.

In accordance with the guidance from the DLUHC and CIPFA, and in order to minimise the risk to investments, the Council applies minimum acceptable credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

As with previous practice, ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets, engaging with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings. This is fully integrated into the creditworthiness methodology provided by Link Group . The result is a colour coding system, which shows the varying degrees of suggested creditworthiness.

Alongside the credit ratings other information sources are used and include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process with regard to the suitability of potential investment counterparties.

The credit ratings of counterparties are supplemented with the following overlays:

- Credit watches and credit outlooks from credit rating agencies;

- Credit Default Swaps (CDS) spreads to give early warning of likely changes in credit ratings;
- Sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads resulting in a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands:

Yellow	5 years
Purple	2 years
Blue	1 year (only applies to part-government owned UK banks)
Orange	1 year
Red	6 months
Green	100 days
No colour	Not to be used

The Link Group creditworthiness service uses a wider array of information than primary ratings alone and by using a risk weighted scoring system, does not give undue preponderance to just one agency's ratings.

- 5.11 Typically, the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances, consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

The credit ratings specified above are defined as follows:-

F1 (short term rating) – Highest credit quality

A- (long term rating) – High credit quality, denoting a very strong bank

- 5.12 All credit ratings will be monitored regularly. The Council is alerted to changes to ratings of all three agencies through its use of Link's creditworthiness service.

- If a downgrade results in the counterparty no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- In addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's counterparty list.

Sole reliance will not be placed on the use of this external service. In addition the Council will also use market data and market information, information on sovereign support for banks and the credit ratings of that supporting government.



### 5.13 Country and sector considerations

Due care will be taken to consider the country, group and sector exposure of the Council's investments. In part the country selection will be chosen by the credit rating of the Sovereign state. In addition:

- No more than 50% will be placed with any non-UK country at any time (see below).
- Group limits have been set to ensure that the Council is not exposed to excessive risk due to concentration of investments within any one institution or group. These are detailed in the Investment Counterparty Limits table contained within this appendix.

Although the strategy sets a limit for investment in non-UK countries at no more than 50%, the Council has been operating a tighter operational strategy in the light of the Eurozone difficulties and has not been investing outside the UK. This operational restriction will continue until the problems in the Eurozone economy have been sufficiently resolved.

- 5.14 In the normal course of the Council's cash flow operations it is expected that both Specified and Non-specified investments will be used for the control of liquidity as both categories allow for short-term investments. The Chief Finance Officer will strive to keep investments within the Non-specified category to a prudent level (having regard to security and liquidity before yield). To these ends the Council will maintain a maximum of 75% of investments in Non-specified investments.
- 5.15 The use of longer-term instruments (greater than one year from inception to repayment) will fall in the Non-specified investment category. These instruments will only be used where the Council's liquidity requirements are safeguarded. The investment in longer-term instruments is also limited by the prudential indicator 14 shown in paragraph 6.3, which gives the maximum amount to be invested over 1 year, as well as the limits on the amounts that can be placed with the categories within the non-specified range of investments (see above paragraph 5.14).
- 5.16 Expectations on shorter-term interest rates, on which investment decisions are based, reflect the fact that an increase in the current 0.50% Bank Rate is likely during 2022. The Council's investment decisions are based on comparisons between the rises priced into market rates against the Council's and advisers own forecasts.
- 5.17 There are operational challenges arising from the ongoing economic conditions. Ideally investments would be invested longer to secure better returns, however shorter dated investments provide better security.
- 5.18 The criteria for choosing counterparties set out above provide a sound approach to investment in difficult market circumstances.

## 5.19 Sensitivity to Interest Rate Movements

The Council's Statement of Accounts is required to disclose the impact of risks on the Council's treasury management activity. Whilst most of the risks facing the treasury management service are addressed elsewhere in this report (credit risk, liquidity risk, market risk, maturity profile risk), the impact of interest rate risk is discussed but not quantified. The table below highlights the estimated impact of a 0.5% increase/decrease in the average interest rates for investments for next year. That element of the debt and investment portfolios, which are of a longer term, fixed interest rate nature, will not be affected by interest rate changes. There will be no effect on borrowing costs as all the Council's existing debt is fixed rate and the additional borrowing planned will also be fixed rate and has been included within the budget figures in this report at the forecast rate for 2021/22.

£000	2022/23 Estimated + 0.5%*	2022/23 Estimated - 0.5%
<b>Revenue Budgets</b>		
Investment income	121	0
Related HRA Income	75	0
Net General Fund/Other Income	46	0

\*This assumes that the rise of 0.50% would be reflected in the rates available to invest– in practice a rate rise of 0.50% would not equal an increase in the rates available. As the rates of interest on investments assumed in the MTFs are lower than 0.50% a reduction of 0.50% would result in Nil income.

## 6.0 Treasury Management Limits on Activity

6.1 There are four further treasury activity limits, which were previously prudential indicators. The purpose of these is to contain the activity of the treasury function within certain limits, thereby managing the risk and reducing the impact of an adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunity to reduce costs. The indicators are:

- **Upper limit on variable rate exposure** – this identifies a maximum limit for variable interest rates based upon the debt position net of investments.
- **Upper limit on fixed rate exposure** – Similar to the previous indicator this covers a maximum limit on fixed interest rates.
- **Maturity structures of borrowing** – These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing at the same time and are required for upper and lower limits.
- **Total principal sums invested for periods longer than 1 year** – These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

6.2 In addition, the Chief Finance Officer has set eight additional local indicators. The aim of these indicators is to increase the understanding of the treasury management indicators.

6.3 The 4 treasury limits above together with the adoption of the Code of Practice indicators are shown below:

<b>Indicator 11</b>	<b>2022/23 Target £m</b>	<b>2023/24 Target £m</b>	<b>2024/25 Target £m</b>
<b>Upper Limit on variable interest rate exposure</b>	55.4	55.8	54.1

<b>Indicator 12</b>	<b>2022/23 Target £m</b>	<b>2023/24 Target £m</b>	<b>2024/25 Target £m</b>
<b>Upper Limit on fixed interest rate exposure</b>	134.0	135.4	131.2

<b>Indicator 13</b>	<b>2022/23</b>		<b>2023/24</b>		<b>2024/25</b>	
<b>Maturity Structure of fixed borrowing</b>	<b>Lower</b>	<b>Upper</b>	<b>Lower</b>	<b>Upper</b>	<b>Lower</b>	<b>Upper</b>
Under 12 months	0%	40%	0%	40%	0%	40%
12 months to 2 years	0%	40%	0%	40%	0%	40%
2 years to 5 years	0%	60%	0%	60%	0%	60%
5 years to 10 years	0%	80%	0%	80%	0%	80%
10 years and above	10%	100%	10%	100%	10%	100%

<b>Indicator 14</b>	<b>2022/23 £m</b>	<b>2023/24 £m</b>	<b>2024/25 £m</b>
<b>Maximum principal sums invested for longer than 1 year</b>	7	7	7

<b>Indicator 15</b>
<b>CIPFA Code of Practice for Treasury Management in the Public Services (Revised December 2017) adopted by Council on 2<sup>nd</sup> March 2010.</b>

6.4 The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury management function over the year. The Chief Finance Officer has therefore set 8 local indicators, which are believed to add value and assist the understanding of the main prudential indicators. These indicators are:

- Debt – Borrowing rate achieved against the average appropriate SONIA rate.\*
- Investments – Investment rate achieved against the average appropriate SONIA rate.\*
- Average rate of interest paid on the Councils Debt – this will evaluate performance in managing the debt portfolio to release revenue

savings.

- Amount of interest on debt as a percentage of gross revenue expenditure.
- Limit on fixed interest rate investments
- Limit on fixed interest rate debt
- Limit on variable rate investments
- Limit on variable rate debt

\*See paragraph 5.6 above

6.5 The 8 indicators are shown below:

	<b>2022/23 Target</b>	<b>2023/24 Target</b>	<b>2024/25 Target</b>
<b>Debt - Borrowing rate achieved i.e. temporary borrowing (loans of less than 1 year) *</b>	less than SONIA rate	less than SONIA rate	less than SONIA rate

\*See paragraph 5.6 above

	<b>2022/23 Target</b>	<b>2023/24 Target</b>	<b>2024/25 Target</b>
<b>Investment rate achieved*</b>	Greater than SONIA rate	Greater than SONIA rate	Greater than SONIA rate

\*See paragraph 5.6 above

	<b>2022/23 Target</b>	<b>2023/24 Target</b>	<b>2024/25 Target</b>
<b>Average rate of Interest Paid on Council Debt (%)</b>	4.25%	4.25%	4.25%

	<b>2022/23 Target</b>	<b>2023/24 Target</b>	<b>2024/25 Target</b>
<b>Interest on Debt as a % of Gross Revenue Expenditure</b>	5%	5%	5%

	<b>2022/23 Target</b>	<b>2023/24 Target</b>	<b>2024/25 Target</b>
<b>Upper Limit on fixed interest rate Investments</b>	100%	100%	100%

	<b>2022/23 Target</b>	<b>2023/24 Target</b>	<b>2024/25 Target</b>
<b>Upper Limit on fixed interest rate debt</b>	100%	100%	100%

	<b>2022/23 Target</b>	<b>2023/24 Target</b>	<b>2024/25 Target</b>
<b>Upper Limit on variable interest rate investments</b>	75%	75%	75%

	2022/23 Target	2023/24 Target	2024/25 Target
<b>Upper Limit on variable interest rate debt</b>	40%	40%	40%

## 6.6 Treasury Management Advisers

The Council has engaged the services of Link Group as its treasury management consultants. The company provides a range of services which include:

- Technical support on treasury matters, capital finance issues and the drafting of Member reports;
- Economic and interest rate analysis;
- Debt rescheduling advice surrounding the existing portfolio;
- Credit ratings/market information service comprising the three main credit rating agencies.

Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the final decision on treasury matters remains with the Council. This service is subject to regular review.

## 6.7 Member and Officer Training

The increased Member consideration of treasury management matters and the need to ensure officers dealing with treasury management are trained and kept up to date requires a suitable training process for Members and officers.

This Council has addressed this important issue by:

- Member Training – Our treasury management advisers provided training to the Audit Committee prior to the consideration of this year’s strategy. They also provided training to the Performance Scrutiny Committee to support their consideration of the mid-year report. The training needs will be regularly reviewed and updated as necessary in 2022/23.
- Staff Training – training needs for staff engaged in treasury management are addressed through the appraisal process. Training is provided both by the Council’s treasury management advisers, other external providers and internally. In addition, the Council encourages staff engaged in treasury to undertake a professional accountancy qualification and ensures that the day-to-day trading is overseen by a professionally qualified accountant following the CIPFA Code of Practice.

## 7.0 Breakdown of Investment Categories with Maximum Amounts and Periods

The Chief Finance Officer, in accordance with TMP 1 (1) within the Council’s Code of Practice, is authorised to invest funds surplus to immediate requirements with the following types of institutions subject to the minimum ratings produced by the three credit rating agencies Fitch, Moody’s and Standard & Poor’s. The Link Group creditworthiness service is applied to determine a list of suitable counterparties available for investment. The minimum ratings applied by Link Group in compiling their recommended counterparty list are set out in section 5.11 of the investment strategy.

All counterparty ratings are updated on a regular basis on the advice of the Council's Treasury Consultants. Notifications of rating changes are received as they happen.

### Investment Counterparty Limits

Institution	Minimum credit criteria/colour band	Maximum limit per group or institution £ million	Maximum maturity period
<b>SPECIFIED INVESTMENTS</b>			
UK Bank <sup>*1</sup>	Orange/Blue Red Green	£7 million	1 year 6 months 100 days
Non-UK Banks <sup>*1</sup> Sovereign rating AA	Orange Red Green	£7 million	1 year 6 months 100 days
Building Society <sup>*2</sup>	Orange Red Green	£5 million	1 year 6 months 100 days
Money Market Fund <sup>*3</sup>	Yellow	£7 million	Liquid
UK Government <sup>*4</sup>	Yellow	unlimited	6 months
UK Local Authority <sup>*4</sup>	Yellow	£3 million	1 year
<b>NON-SPECIFIED INVESTMENTS</b>			
UK Bank <sup>*1</sup>	Purple	£7 million	2 years
Non-UK Banks <sup>*1</sup> Sovereign rating AA	Purple	£7 million	2 years
Building Society <sup>*2</sup>	Purple Yellow	£2 million	2 years 5 years
UK Local Authority <sup>*4</sup>	Yellow	£3 million	5 years
Lincoln Credit Union	N/A	£10K	N/A
Council's own bank <sup>*5</sup> (operational cash limit in addition to investment group limit)	N/A	£500K	Overnight

<sup>\*1</sup>Where the term 'Bank' is used, this denotes a UK or European Bank authorised to accept deposits through a bank account incorporated within the UK banking sector. The maximum amount indicated is the 'Group total' and covers the total amount that can be invested when spread over any number of subsidiaries within that group.

<sup>\*2</sup> Where the term Building Society is used, this denotes a UK Building Society.

<sup>\*3</sup> Money market funds (MMF) are mutual funds that invest in short-term high quality debt instruments. The assets are actively managed within very specific guidelines to offer liquidity and competitive returns. Recently MMFs have changed from a constant net asset value basis to a low volatility net asset value. Although money funds are regarded as short-term investments the rating agencies use a classification system based on long-term debt ratings.

<sup>\*4</sup> The UK Government (i.e. HM Treasury and its Executive Agency, the Debt Management Office) and Local Authorities, although not rated as such, are classified as having the equivalent of the highest possible credit rating.

<sup>\*5</sup>This limit covers normal treasury management activities but excludes any deposits received after money market trading has closed.

It allows up to £500K of operational cash to be held in the Council's main bank account in addition to the group investment limit for the bank, if the bank is included on the Council's counterparty list.

## **Approved Investment Instruments**

In addition to determining the rating and limits of authorised counterparties TMP 4 “Approved instruments, methods and techniques” within the Council’s Code of Practice requires the Council to define the instruments that the Authority will use in undertaking its Treasury Management activities. In accordance with this, and the investment regime issued as part of the prudential capital finance system, the Instruments that the Chief Finance Officer will consider investing surplus funds in are shown below:

### **Instruments of Specified Investments \*1**

1. Gilt-edged securities issued by the United Kingdom Debt Management Office (UK DMO), an Executive Agency of HM Treasury.
2. Treasury Bills issued by the UK DMO.
3. Deposits with the Debt Management Office Debt Management Account Deposit Facility (DMADF).
4. Deposits with a Local Authority, Parish Council or Community Council.
5. Deposits with Banks and Building Societies (Including opening Business Accounts).
6. Certificates of deposit issued by Banks and Building societies.
7. Pooled investment vehicles (e.g. money market funds)

**\*1** To be defined as a Specified Investment the above instruments will have these features common to all:

- Be denominated in Sterling,
- Of not more than 1 year maturity,
- Of longer than 1 year maturity but the Council has the right to be repaid within 12 months,
- For instruments numbered 5 to 7 these must be with institutions of high credit quality.

### **Instruments of Non-Specified Investments \*2**

1. Deposits with Banks, Building Societies and their subsidiaries.
2. The Council’s own banker if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as is possible.
3. Certificates of deposit issued by Banks and Building Societies.

**\*2** To be defined as a Non-Specified Investment the above instruments will have these features common to all:

- Denominated in Sterling,
- Of more than 1 year maturity,
- Of less than 1 year maturity with an institution that does not meet the basic security requirements under Specified Investments e.g. a deposit with a non-credit rated Bank or Building Society



## Security, Liquidity and Yield benchmarking

### **Benchmarking and Monitoring Security, Liquidity and Yield in the Investment Service**

A requirement for Treasury Management reporting is the consideration and approval of security and liquidity benchmarks.

These benchmarks are targets and so may be breached from time to time. Any breach will be reported, with supporting reasons in the Annual Treasury Report.

Yield – These benchmarks are widely used to assess investment performance. Local measures of yield benchmarks are:

- Investments – Internal returns above the appropriate SONIA rate- see paragraph 5.6 above.

Security and liquidity benchmarks are already intrinsic to the approved treasury strategy through the counterparty selection criteria and some of the prudential indicators. Benchmarks for the cash type investments are set out below and these will form the basis of reporting in this area. In other investment categories appropriate benchmarks will be used where available.

Liquidity – This is defined as “having adequate, though not excessive cash resources, borrowing arrangements, overdrafts or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives” (CIPFA Treasury Management Code of Practice). In respect of this area the Council seeks to maintain:

- Bank overdraft - nil
- Liquid short term deposits of at least £5m available with a week’s notice.

The availability of liquidity and the term risk in the portfolio can be benchmarked by the monitoring of the Weighted Average Life (WAL) of the portfolio – a shorter WAL would generally embody less risk. In this respect the proposed benchmark to be used is:

- WAL benchmark is expected to be 0.08 years.
- Security of the investments – In context of benchmarking, assessing security is a much more subjective area to assess. Security is currently evidenced by the application of minimum credit quality criteria to investment counterparties, primarily through the use of credit ratings supplied by the three main credit rating agencies (Fitch, Moody’s and Standard and Poor’s). Whilst this approach embodies security considerations, benchmarking levels of risk is more problematic. One method to benchmark security risk is to assess the historic level of default against the minimum criteria used in the Council’s investment strategy.

The Council’s expected security risk benchmark from its budgeted investment strategy is:

- 0.012% historic risk of default when compared to the whole portfolio which equates to a potential loss of £2,160 on an investment portfolio of £18m. In addition that the security benchmark for each individual year is:

	1 year	2 year	3 year	4 year	5 year
Maximum	0.30%	0.30%	0.30%	0.30%	0.30%

These benchmarks are embodied in the criteria for selecting cash investment counterparties and these will be monitored and reported to Members in the Investment Annual Report. As this data is collated, trends and analysis will be collected and reported