Carlisle City Council
Report to Audit Committee

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Report details

Meeting Date:	10 December 2021
Portfolio:	Finance, Governance and Resources
Key Decision:	Yes: Recorded in the Notice Ref: KD.10/21
Policy and Budget Framework	Yes
Public / Private	Public
Title:	DRAFT TREASURY MANAGEMENT STRATEGY STATEMENT, INVESTMENT STRATEGY AND MINIMUM REVENUE PROVISION STRATEGY 2022/23
Report of:	CORPORATE DIRECTOR OF FINANCE & RESOURCES
Report Number:	RD 53/21

Purpose / Summary:

This report sets out the Council's draft Treasury Management Strategy Statement for 2022/23, in accordance with the CIPFA Code of Practice on Treasury Management. The Investment Strategy and the Minimum Revenue Provision (MRP) Strategy for 2022/23 are also incorporated as part of the Statement. So too are the Prudential Indicators as required within the Prudential Code for Capital Finance in Local Authorities.

Recommendations:

Members of the Audit Committee are asked to note and make comments on the proposed Treasury Management Strategy for 2022/23.

Tracking

Executive:	20 December 2021, 19 January 2022
Scrutiny:	BTSP 6 January 2022
Audit Committee:	10 December 2021
Council:	1 February 2022

Carlisle City Council
Report to Executive

Report details

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Recommendations:

The Executive is asked to note the draft Treasury Management Strategy Statement for 2022/23, which incorporates the Investment Strategy and the MRP Strategy, together with the Prudential Indicators for 2022/23 as set out in Appendix A and the Treasury Management Policy Statement as set out at Appendix D, and to seek comments from the Business and Transformation Scrutiny Panel in January 2022.

Tracking

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1. BACKGROUND

1.1 The CIPFA Code of Practice on Treasury Management in Local Authorities was first issued in 1992 and updated in 1996, 2001, 2011 and 2017. The City Council formally adopted this Code in March 2002 and adopted the 2017 revision in February 2018.

1.2 CIPFA has consulted on revisions to the Treasury Management Code, and the Prudential Code, throughout 2021 and the new Codes are intended to be implemented by authorities for 2023/24 Treasury Management Strategies.

1.3 Under the requirements of the revised Code, the Council will receive each year the following reports:

- Annual strategy and plan in advance of the year
- A mid-year review
- Annual report after its close.

2. TREASURY MANAGEMENT STRATEGY STATEMENT

2.1 As required under the Code, the Treasury Management Strategy Statement (TMSS) for 2022/23, which also incorporates both the Investment Strategy for that year and the Minimum Revenue Strategy, is set out in **Appendix A**. The schedule of approved investment vehicles is contained in **Appendix B** and **Appendix C** includes a summary of current economic forecasts on interest rates that have been utilised in preparing the Strategy.

2.2 Also included within Appendix A are the **Prudential Indicators** that must be determined under the requirements of the CIPFA Prudential Code for Capital Finance in Local Authorities. These requirements came into operation on 1 April 2004 under the provisions of the Local Government Act 2003. Part 1 of the Act allows a local authority to borrow money for any purpose that is within its control or for the purposes of the prudent management of its financial affairs. The main purpose for borrowing money is to fund capital expenditure although some short-term borrowing is permitted to cover temporary cash flow needs.

2.3 Since 1 April 2004 there has been no statutory limit to the amount that can be borrowed. There is, however, a requirement for full compliance with CIPFA's Prudential Code; the key objectives of which are to demonstrate that the proposed capital investment plans have been assessed by the Council as affordable, prudent and sustainable. Section 3(1) of the Act puts a duty on the Council to determine before the start of the financial year and keep under review the maximum amount that it can afford to borrow. This amount is called the **Authorised Limit** and is discussed in **Appendix A**.

2.4 The Prudential Indicators are monitored via the quarterly Treasury Management monitoring reports.

2.5 The council recognises its responsibilities in terms of climate change and environmental sustainability and that consideration of these responsibilities may form part of its Investment Portfolio; however, consideration must also be given to ensure the security of principal, portfolio liquidity and return on investment when making investment decisions. Work continues to review the Investment Strategy in line with these recognised responsibilities and this will involve ensuring that counterparties have a relevant environmental strategy that sets out their position on climate responsibilities.

3. RISKS

3.1 The Treasury Management function must ensure the security of Council funds at all times over the yield that is gained. It must also ensure it follows the key principles as outlined in the Treasury Management Code of Practice and the Prudential Code.

3.2 There is a risk that interest rates could change over the period of the Treasury Management Strategy Statement, particularly in respect of volatile economic situations, but close monitoring of the situation will be maintained, particularly if there are forecast changes to interest rates that could have an impact on borrowing decisions or reduce the availability of counterparties with which the Council can invest its funds.

4. CONSULTATION

4.1 The Council has appointed Link Asset Services Treasury Services as its Treasury Advisers and they have been involved in the Strategy and proposals contained within this report.

5. CONCLUSION AND REASONS FOR RECOMMENDATIONS

5.1 The Executive is asked to note the Treasury Management Strategy Statement for 2022/23, which incorporates the Investment Strategy and the MRP Strategy, together with the Prudential Indicators for 2022/23 as set out **in Appendix A**. and the Treasury Management Policy Statement as set out at **Appendix D.**

6. CONTRIBUTION TO THE CARLISLE PLAN PRIORITIES

6.1 To ensure the Council's investments are in line with the appropriate policies including the Treasury Management Strategy Statement.

Contact details:

Contact Officer: Steven Tickner Ext: 7280

Appendices attached to report:

Appendix A – Treasury Management Strategy Statement

Appendix B – Approved Investment Instruments

Appendix C – Interest Rate Forecasts

Appendix D – Treasury Management Policy Statement

Note: in compliance with section 100d of the Local Government Act 1972 the report has been prepared in part from the following papers:

- None

Corporate Implications:

Legal - The Council has a fiduciary duty to manage its resources effectively for the benefit of its area and the delivery of its services. Treasury Management is an important part of this function and it is appropriate that the Council has a strategy and takes account of the available specialist internal and external advice. The Treasury Management Strategy forms part of the Budget and Policy framework and, therefore, ultimately requires approval by Council.

Property Services -

Finance - contained within the report.

Equality - not applicable

Information Governance - There are no information governance issues in this report

APPENDIX A

Draft Treasury Management Strategy Statement

Draft Minimum Revenue Provision Policy Statement and Annual Investment Statement

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Carlisle City Council

2022/23

1. INTRODUCTION

1.1 It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This, therefore, means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from: -

- increases in interest charges caused by increased borrowing to finance additional capital expenditure, and
- any increases in running costs from new capital projects are limited to a level which is affordable within the projected income of the Council for the foreseeable future

1.2 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

1.3 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

1.4 The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

1.5 Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day-to-day treasury management activities.

1.6 CIPFA defines treasury management as:
"The management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

1.7 Revised reporting has been required from 2019/20 due to revisions of the DLUHC Investment Guidance, the DLUHC Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes included the introduction of a capital investment strategy, to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011. The capital investment strategy has been reported separately.

1.8 CIPFA have consulted on proposed changes to the Prudential Code and Treasury Management Codes throughout 2021 and intends to publish the final versions of the revisions by the end of 2021. Implementation of the revised Codes will be for the 2023/24 Treasury Management Strategy Statements.

1.9 The suggested strategy for 2022/23 in respect of the following aspects of the treasury management function is based upon officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury consultants. The strategy covers the following issues:

- Treasury limits in force that will limit the treasury risk and activities of the Council;
- Prudential and Treasury Indicators;
- Current treasury position;
- Borrowing requirement;
- Prospects for interest rates;
- Borrowing strategy considerations;
- Debt rescheduling opportunities.
- Investment Strategy
- Minimum Revenue Provision Strategy
- Capital Investment Strategy

2. CAPITAL INVESTMENT STRATEGY

2.1 The CIPFA revised 2017 Prudential and Treasury Management Codes requires all local authorities to prepare a Capital Investment Strategy report, which will provide the following:

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

2.2 The aim of the Capital Investment Strategy is to ensure that all elected members fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

2.3 The Capital Investment Strategy is reported separately from the Treasury Management Strategy Statement alongside the Medium-Term Financial Plan with non-treasury investments being reported through this document. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset. The Capital Investment Strategy will show:

- The corporate governance arrangements for these types of activities;
- Any service objectives relating to the investments;
- The expected income, costs and resulting contribution;
- The debt related to the activity and the associated interest costs;
- The payback period (MRP policy);
- For non-loan type investments, the cost against the current market value;
- The risks associated with each activity.

2.4 Where a physical asset is being bought, details of market research, advisers used, (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

2.5 Where the Council has borrowed to fund any non-treasury investment, there should also be an explanation of why borrowing was required and why the DLUHC Investment Guidance and CIPFA Prudential Code have not been adhered to.

2.6 If any non-treasury investment sustains a loss during the final accounts and audit process, the strategy and revenue implications will be reported through the same procedure as the Capital Investment Strategy.

3. TREASURY LIMITS 2022/23 TO 2024/25

3.1 It is a statutory duty, under S.3 of the Local Government Act 2003 and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount determined is termed the 'Affordable Borrowing Limit'.

3.2 The Council must have regard to the Prudential Code when setting its Affordable Borrowing Limit. This essentially requires it to ensure that total capital investment remains within sustainable limits and in particular, that the impact upon its future council tax levels is 'acceptable'. It is important to understand, however, that the Indicators themselves, which are set out in paragraph 6, do not have an inherently right or wrong answer. They are not intended as comparator information between different authorities but are designed to support and record local decision making.

4. USE OF TREASURY CONSULTANTS

4.1 The authority has, like most other authorities, employed treasury advisers for specialist advice and assistance for many years. In the case of this authority, this role has long been fulfilled by Link Asset Services.

4.2 Link Asset Services provide specialist advice on both borrowing and investment matters. They also supply other relevant information and hold regular client seminars which help provide up to date training in what is an important and continually changing field. That said, it is important to recognise that responsibility for all treasury matters lies solely with the City Council and this responsibility is not delegated to Link Asset Services or any other third party. The Council has regard to the advice and information supplied by Link Asset Services along with advice and information from a variety of other sources. Such advice is valued and the authority is in frequent contact with Link Asset Services but this does not lessen the ultimate responsibility of the City Council in dealing with treasury matters and taking relevant decisions.

5. CURRENT PORTFOLIO POSITION

The Council's treasury portfolio position at 26 November 2021 comprised:

Table 1		Principal £m	£m	Ave Rate %
Fixed Rate Funding	PWLB	13.0		
	Market	0.0	13.0	1.63
Variable Rate Funding	PWLB	0		
	Market	0	0	0.00
Other Long Term Liabilities			0	0.00
Gross Debt			**13.0**	**1.63**
Total Investments			**26.5**	**0.75**

6. PRUDENTIAL AND TREASURY INDICATORS 2022/23 – 2024/25

6.1 The Prudential and Treasury Indicators have been based on current projections for capital spending and resources in 2022/23 to 2024/25 (which may be subject to change during the budget process). The Council has ensured that future years' capital programmes have been set in accordance with the principles contained within the City Council's Capital Strategy and Asset Management Plan.

PRUDENTIAL INDICATOR AFFORDABILITY INDICATORS	2020/21 actual £000	2021/22 revised estimate £000	2022/23 estimate £000	2023/24 estimate £000	2024/25 estimate £000
Capital Expenditure	14,172	30,378	18,079	9,527	3,409
Ratio of financing costs to net revenue stream	1.19%	4.35%	7.04%	13.43%	12.51%
Net borrowing requirement in year (Internal & External)	3,408	21,023	10,334	974	(5,400)
Capital Financing Requirement as at 31 March	19,521	40,544	50,878	51,853	46,453
Annual change in Cap. Financing Requirement	(1,026)	21,023	10,334	974	(5,400)
Incremental impact of capital investment decisions					
Increase in council tax (band D) per annum (£)	2.97	18.19	8.85	0.83	(4.54)

6.2 The estimates of financing costs include both current capital commitments and the capital programme. In the case of this authority, it is assumed that any support from central government towards the costs of capital expenditure programmes in the next three years will be by means of a capital grant e.g. Disabled Facilities Grant.

6.3 <u>The Council's Borrowing Need (Capital Financing Requirement)</u>

6.3.1 The Capital Financing Requirement (CFR) is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is a measure of the Council's indebtedness and so its underlying borrowing need. Any capital expenditure above, which has not immediately been paid for from capital grants, capital receipts or revenue contributions, will increase the CFR as it will be funded from borrowing.

6.3.2 The CFR does not increase indefinitely. The Minimum Revenue Provision (MRP) is a statutory annual charge to the revenue budget which reduces the CFR in line with each asset's life, and so charges the economic consumption of capital assets as they are used.

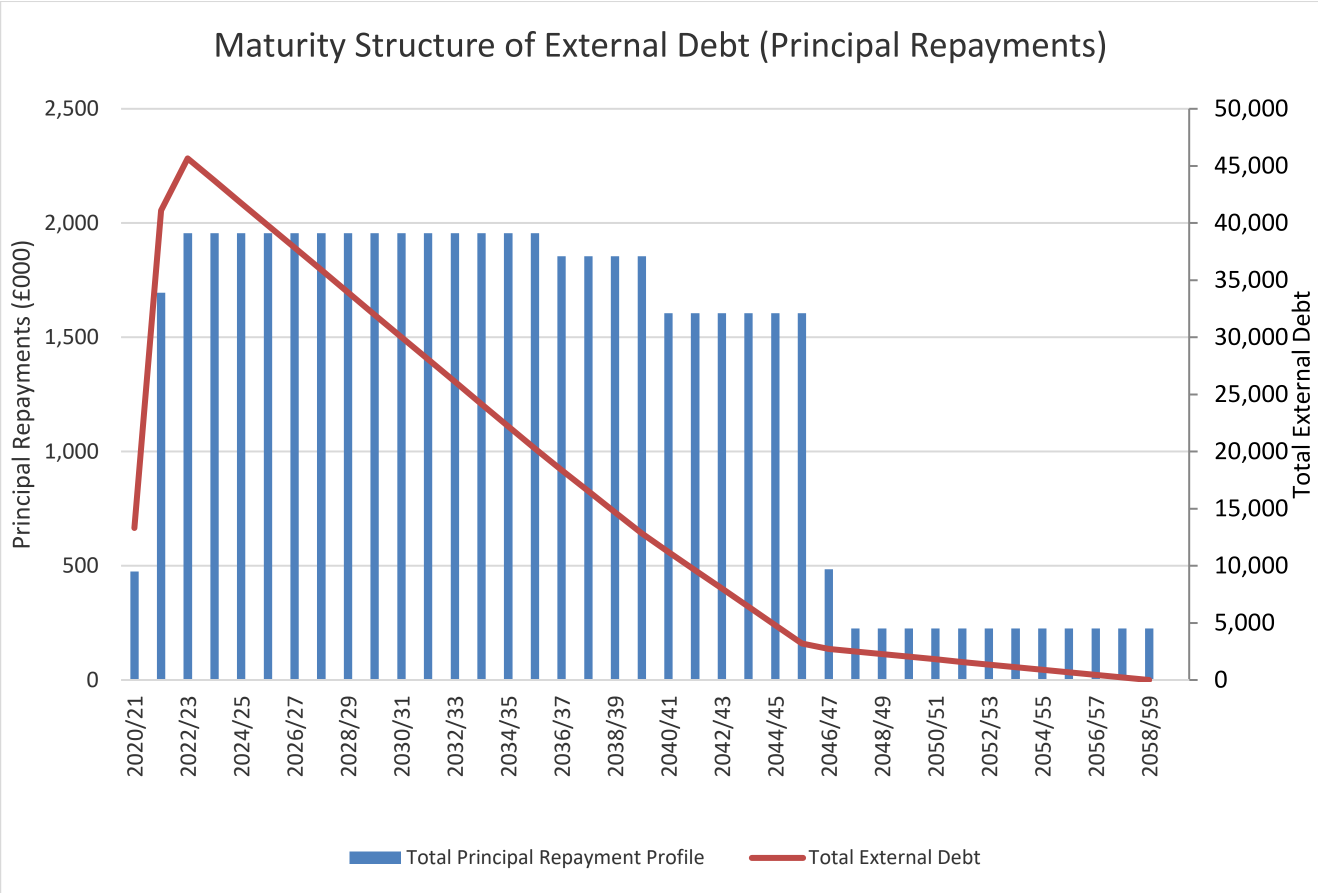
PRUDENTIAL INDICATOR TREASURY MANAGEMENT INDICATORS	2020/21 actual £000	2021/22 revised estimate £000	2022/23 estimate £000	2023/24 estimate £000	2024/25 estimate £000
Authorised Limit for External Debt:					
- Borrowing	44,000	48,000	52,000	52,000	50,000
- Other Long Term Liabilities	100	100	100	100	100
TOTAL	**44,100**	**48,100**	**52,100**	**52,100**	**50,100**
Operational Boundary for external debt:					
- Borrowing*	32,500	43,000	47,000	47,000	45,000
- Other Long Term Liabilities	100	100	100	100	100
TOTAL	**32,600**	**43,100**	**47,100**	**47,100**	**45,100**
Upper Limit for fixed interest rate exposure:					
- Net principal re. Fixed rate borrowing/investments	**100%**	**100%**	**100%**	**100%**	**100%**
Upper Limit for variable rate exposure					
- Net principal re. Variable rate borrowing/investments	**100%**	**100%**	**100%**	**100%**	**100%**
Upper Limit for total principal sums invested for over 1 year	**50%**	**50%**	**50%**	**50%**	**50%**

Notes:

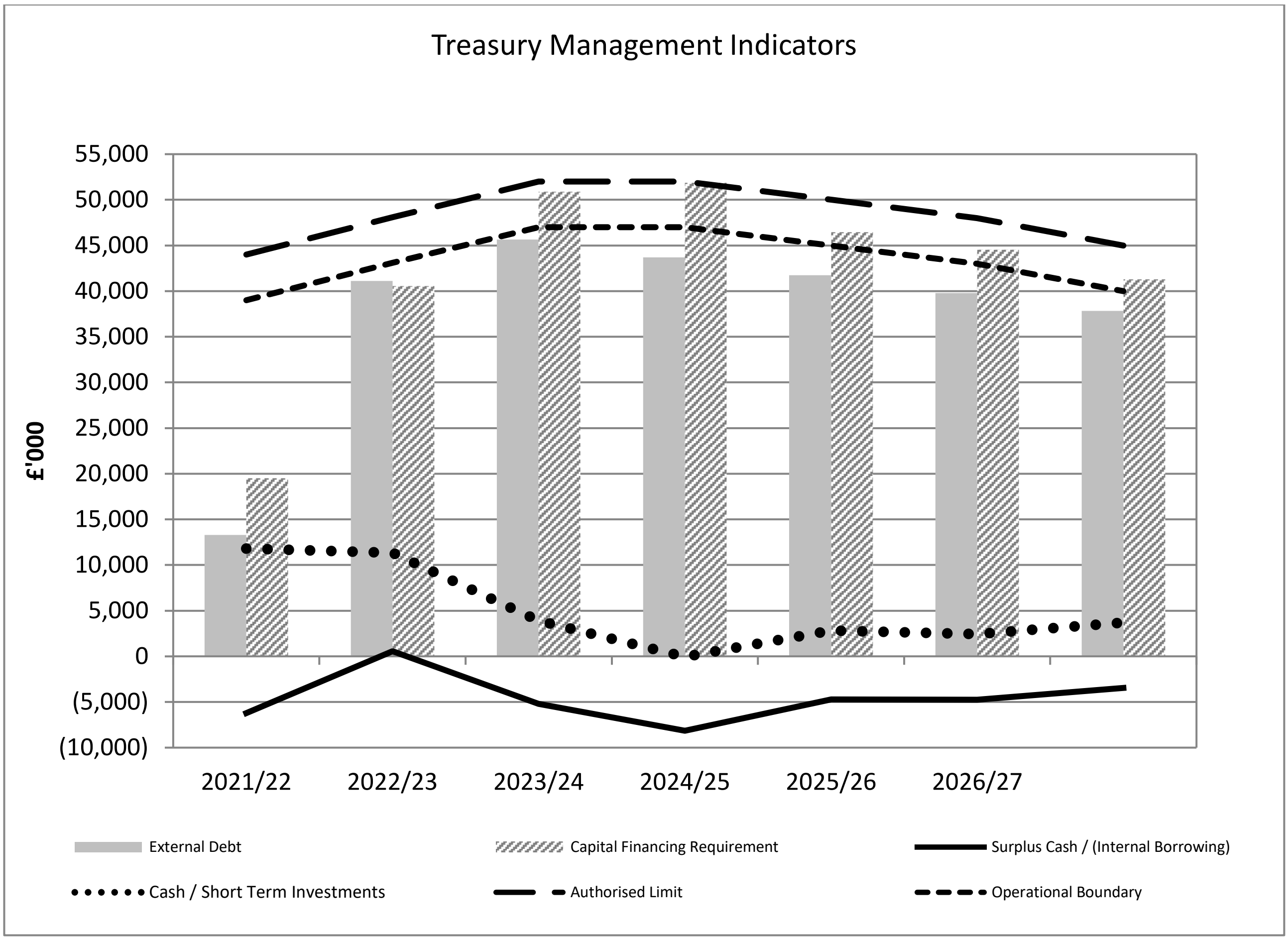
The authorised limit for external debt. This is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

The operational boundary. This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

PRUDENTIAL INDICATOR TREASURY MANAGEMENT INDICATORS	2020/21 actual £000	2021/22 revised estimate £000	2022/23 estimate £000	2023/24 estimate £000	2024/25 estimate £000
External Debt B/Fwd	**13,763**	**13,288**	**41,093**	**45,645**	**43,690**
New External Debt (Actual & Planned)	0	29,500	6,507	0	0
External Debt Repaid	(475)	(1,695)	(1,955)	(1,955)	(1,955)
External Debt C/fwd	**13,288**	**41,093**	**45,645**	**43,690**	**41,735**



6.3.3 The graph below shows the level of external debt currently forecast against the Capital Financing Requirement. This chart makes assumptions included in the Executive's budget regarding the use of external borrowing. However, funding of capital expenditure could change, for example, if additional assets are sold generating capital receipts or expenditure requirements change. Therefore, this chart could be subject to change in the future. This shows that external debt is not forecast to rise above the authorised limit over the next five years. However, this is predicated on the assumption that capital receipts can be generated that will be used to fund some of the capital expenditure requirements identified. Should these receipts not be achieved, then then the use of borrowing will need to be re-examined. The Medium-Term Financial Plan assumes that external borrowing will be undertaken to support expenditure on major capital schemes. These areas will be closely monitored prior to any further external borrowing being undertaken.

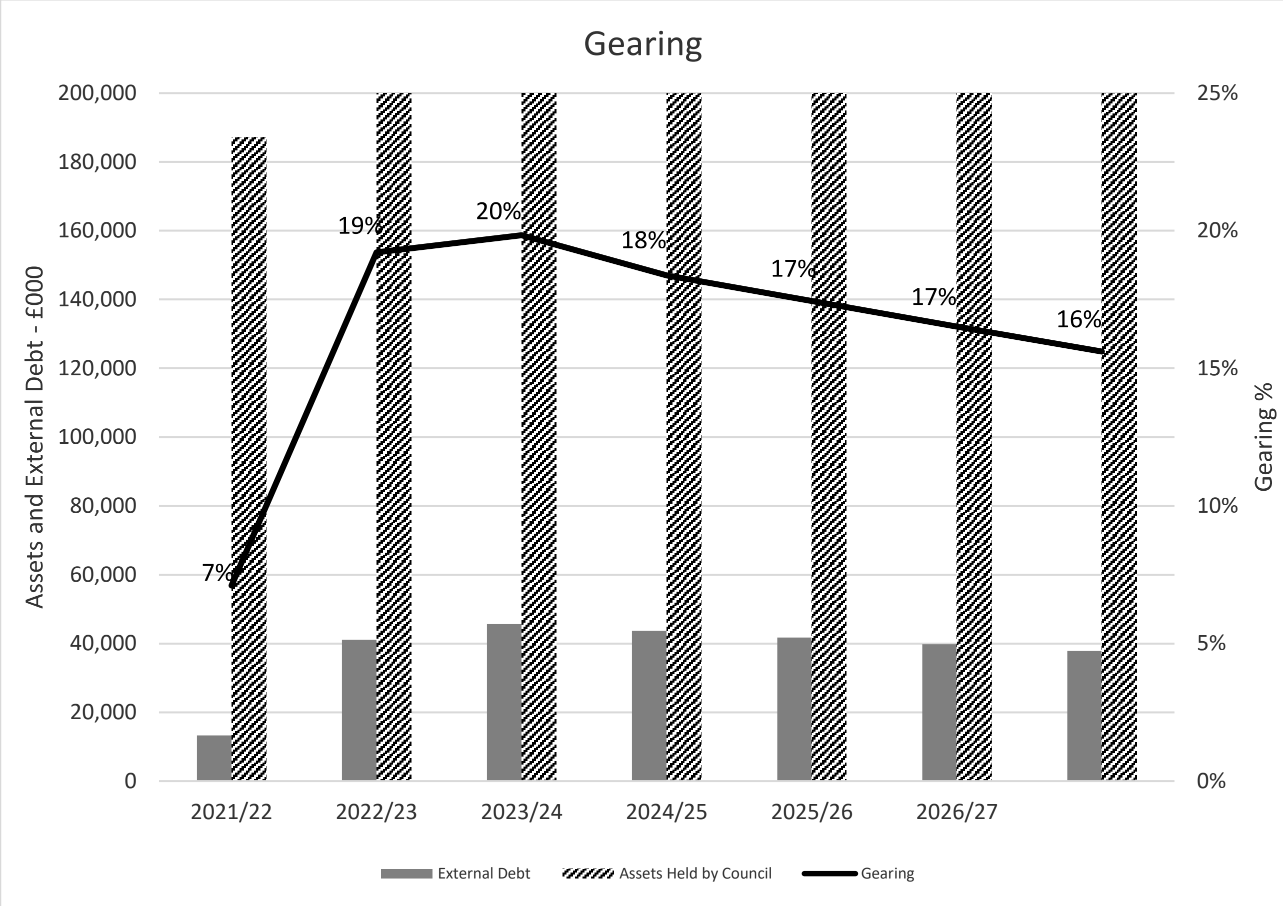


Maturity structure of any fixed rate borrowing during 2022/23	Upper limit	Lower limit
Under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within 5 years	100%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

6.3.4 In respect of its external debt, it is recommended that the Council approves the authorised limits as outlined above for its total external debt, gross of investments, for the next three financial years. The limit separately identifies borrowing from other long-term liabilities such as finance leases. The Council will be asked to approve these limits and to delegate authority to the Corporate Director of Finance and Resources, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities in accordance with option appraisal and best value for money. Any such change would be reported to the next available Council meeting.

6.3.5 The authorised limit is consistent with the authority's current commitments, plans and proposals for capital expenditure and it's financing. **However, the overall authorised limit is not to be exceeded without prior Council approval.**

6.3.6 In setting the Authorised Limit consideration should be made to the chart below which demonstrates the level of indebtedness against the Council's overall asset base (i.e. its gearing).



6.3.7 The operational boundary is based upon the same estimates as the authorised limit but without the headroom included within the authorised limit to allow for unusual cash movements. As with the authorised limit, the Council is asked to delegate authority to the Corporate Director of Finance and Resources to effect movement between the separately agreed limits for borrowing and other long-term liabilities. The operational boundary can be exceeded in exceptional circumstances without prior Council approval providing that it remains within the authorised limit.

6.3.8 The City Council's current limits for maximum levels of fixed and variable rate funding are both 100% and this is as recommended by the treasury advisers.

7 PROSPECTS FOR INTEREST RATES

7.2.1 The Council has appointed Link Asset Services as its treasury adviser and part of their service is to assist the Council to formulate a view on interest rates. The following table gives the Link Asset Services view although it should be noted that there are some differing views among the various economic forecasters regarding the future pattern of these rates:

	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Bank Rate	0.25%	0.25%	0.50%	0.50%	0.50%	0.75%	0.75%	0.75%	0.75%	1.00%

7.2.2 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. As shown in the forecast table above, one increase in Bank Rate from 0.10% to 0.25% has now been included in December 2021, a second increase to 0.50% in quarter 2 of 2022/23 and a third one to 0.75% in quarter 4 of 2022/23.

7.2.3 **Significant risks to the forecasts**

- COVID vaccines do not work to combat new mutations and/or new vaccines take longer than anticipated to be developed for successful implementation.
- The pandemic causes major long-term scarring of the economy.
- The Government implements an austerity programme that supresses GDP growth.
- The MPC tightens monetary policy too early – by raising Bank Rate or unwinding QE.
- The MPC tightens monetary policy too late to ward off building inflationary pressures.
- Major stock markets e.g., in the US, become increasingly judged as being over-valued and susceptible to major price corrections. Central banks become increasingly exposed to the “moral hazard” risks of having to buy shares and corporate bonds to reduce the impact of major financial market selloffs on the general economy.
- Geo-political risks are widespread e.g., German general election in September 2021 produces an unstable coalition or minority government and a void in high-profile leadership in the EU when Angela Merkel steps down as Chancellor of Germany; on-going global power influence struggles between Russia/China/US.

7.3 Forecasts for Bank Rate

7.3.1 Link are not expecting Bank Rate to go up fast after the initial rate rise; their view is that the supply potential of the economy has not taken a major hit during the pandemic: it should, therefore, be able to cope well with meeting demand after supply shortages subside over the next year, without causing inflation to remain elevated in the medium-term, or to inhibit inflation from falling back towards the MPC’s 2% target after the spike up to 5%. Link are therefore forecasting five increases in Bank Rate over the forecast period to March 2025, ending at 1.25%.

However, we are far from confident that these forecasts will not need changing within a relatively short timeframe for the following reasons:-

- There are increasing grounds for viewing the economic recovery as running out of steam during the summer and now into the autumn. This could lead into stagflation which would create a major dilemma for the MPC in how to strike a balance between combating inflation and supporting economic growth.
- Will some current key supply shortages spill over into causing economic activity in some sectors to take a significant hit over the next year?
- Rising gas and electricity prices could also pose a potential threat to the supply chain through some energy intensive sections of industry having to close that are no longer economic to run while prices remain so high.
- Rising gas and electricity prices in October and next April and increases in other prices caused by supply shortages, plus increases in taxation next April, are already going to deflate consumer spending power without the MPC having to take any action on Bank Rate to cool inflation and excess demand in the economy compared to supply. Then we have the Government's upcoming budget in October, which could also end up in reducing consumer spending power.
- On the other hand, consumers are sitting on around £200bn of excess savings left over from the pandemic so when will they spend this sum, in part or in total?
- It is estimated that there were around 1 million people who came off furlough on 30th September; how many of those would not have had jobs on 1st October and would, therefore, have been available for filling labour shortages in many sectors of the economy? So, supply shortages which have been driving up both wages and costs, could reduce significantly within the next six months or so and alleviate the MPC's current concerns. However, some key labour shortages will be more difficult to fill due to the need for time to train and qualify.
- There is a risk that there could be further nasty surprises on the Covid front, on top of the flu season this winter, which could depress economic activity.

7.3.2 In summary, with the high level of uncertainty prevailing on several different fronts, it is likely that these forecasts will need to be revised again soon - in line with what the new news is.

7.3.3 It also needs to be borne in mind that Bank Rate being cut to 0.10% was an emergency measure to deal with the Covid crisis hitting the UK in March 2020. At any time, the MPC could simply decide to take away that final emergency cut from 0.25% to 0.10% on the grounds of it no longer being warranted and as a step forward in the return to normalisation. The MPC may also be concerned to protect its inflation fighting credentials and may view that such a small increase would do little to damage growth. There is therefore a significant risk that the first increase could be as early as December 2021. In addition, any Bank Rate under 1% is both highly unusual and highly supportive of economic growth.

7.4 Forecasts for PWLB rates and gilt and treasury yields

7.4.1 As the interest forecast table for PWLB certainty rates above shows, there is likely to be a steady rise over the forecast period, with some degree of uplift due to rising treasury yields in the US.

7.4.2 There is likely to be **exceptional volatility and unpredictability in respect of gilt yields and PWLB rates** due to the following factors: -

- How strongly will changes in gilt yields be correlated to changes in US treasury yields (see explanation on the next page)? Over 10 years since 2011 there has been an average 75% correlation between movements in US treasury yields and gilt yields. However, from time to time these two yields can diverge. Lack of spare economic capacity and rising inflationary pressures are viewed as being much greater dangers in the US than in the UK. This could mean that central bank rates will end up rising earlier and higher in the US than in the UK if inflationary pressures were to escalate; the consequent increases in treasury yields could well spill over to cause (lesser) increases in gilt yields. There is, therefore, an upside risk to forecasts for gilt yields due to this correlation. The Link Group forecasts have included a risk of a 75% correlation between the two yields.
- Will the Fed take action to counter increasing treasury yields if they rise beyond a yet unspecified level?
- Would the MPC act to counter increasing gilt yields if they rise beyond a yet unspecified level?
- How strong will inflationary pressures actually turn out to be in both the US and the UK and so put upward pressure on treasury and gilt yields?
- How will central banks implement their new average or sustainable level inflation monetary policies?
- How well will central banks manage the withdrawal of QE purchases of their national bonds i.e., without causing a panic reaction in financial markets as happened in the "taper tantrums" in the US in 2013?
- Will exceptional volatility be focused on the short or long-end of the yield curve, or both?

7.4.3 The forecasts are also predicated on an assumption that there is no break-up of the Eurozone or EU within our forecasting period, despite the major challenges that are looming up, and that there are no major ructions in international relations, especially between the US and China / North Korea and Iran, which have a major impact on international trade and world GDP growth.

7.5 **Gilt and treasury yields**

7.5.1 Since the start of 2021, there has been a lot of volatility in gilt yields, and hence PWLB rates. During the first part of the year, US President Biden's, and the Democratic party's determination to push through a $1.9trn (equivalent to 8.8% of GDP) fiscal boost for the US economy as a recovery package from the Covid pandemic was what unsettled financial markets. However, this was in addition to the $900bn support package already passed in December 2020 under President Trump. This was then followed by additional Democratic ambition to spend up to $3.5trn on infrastructure and an 'American families' plan over the next decade. Financial markets were alarmed that all this stimulus, which is much bigger than in other western economies, was happening at a time in the US when: -

1. A fast vaccination programme has enabled a rapid opening up of the economy.
2. The economy had already been growing strongly during 2021.
3. It started from a position of little spare capacity due to less severe lockdown measures than in many other countries. A combination of shortage of labour caused largely by an enduring fall in the labour participation rate, and supply bottle necks, is likely to stoke inflationary pressures more in the US than in other major western countries.
4. And the Fed was still providing monetary stimulus through monthly QE purchases.

7.5.2 These factors could cause an excess of demand in the economy which could then unleash stronger and more sustained inflationary pressures in the US than in other western countries: this would imply that interest rates will eventually need to go up higher in the US than elsewhere. The September Federal Reserve (Fed) minutes revealed that the Fed is likely to decide at its next meeting to start tapering monthly QE purchases by the end of 2021, reducing the level of purchases each month until they cease around the middle of 2022. These purchases are currently acting as downward pressure on treasury yields and so that pressure will reduce as tapering progresses. As an average since 2011, there has been a 75% correlation between movements in 10-year treasury yields and 10-year gilt yields. This is a significant upward exposure to the forecasts for longer term PWLB rates. However, gilt yields and treasury yields do not always move in unison.

7.5.3 The balance of risks to medium to long term PWLB rates: -

- There is a balance of upside risks to forecasts for medium to long term PWLB rates.

7.6.1 **Investment and borrowing rates**

7.6.1 Investment returns are expected to improve in 2022/23. However, while markets are pricing in a series of Bank Rate hikes, actual economic circumstances may see the MPC fall short of these elevated expectations. Borrowing interest rates fell to historically very low rates as a result of the COVID crisis and the quantitative easing operations of the Bank of England and still remain at historically low levels. The policy of avoiding new borrowing by running down spare cash balances has served local authorities well over the last few years.

7.6.2 On 25 November 2020, the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates which had been increased by 100 bps in October 2019. The standard and certainty margins were reduced by 100 bps but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three-year capital programme. The current margins over gilt yields are as follows: -.

- **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB Certainty Rate** is gilt plus 80 basis points (G+80bps)
- **PWLB HRA Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB HRA Certainty Rate** is gilt plus 80bps (G+80bps)
- **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)

7.6.3 Link's long-term (beyond 10 years), forecast for Bank Rate is 2.00%. As some PWLB certainty rates are currently below 2.00%, there remains value in considering long-term borrowing from the PWLB where appropriate. Temporary borrowing rates are likely, however, to remain near Bank Rate and may also prove attractive as part of a balanced debt portfolio.

7.6.4 While this authority will not be able to avoid borrowing to finance new capital expenditure, there will be a *cost of carry*, (the difference between higher borrowing costs and lower investment returns), to any new borrowing that causes a temporary increase in cash balances.

8 BORROWING STRATEGY

8.1 The Link Asset Services forecast for the PWLB new borrowing rate (repayment at Maturity) is as follows:

	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24
5 Yr PWLB	1.50%	1.50%	1.60%	1.60%	1.70%	1.70%	1.70%	1.80%	1.80%	1.80%	1.90%
10Yr PWLB	1.80%	1.90%	1.90%	2.00%	2.00%	2.10%	2.10%	2.20%	2.20%	2.20%	2.30%
25Yr PWLB	2.10%	2.20%	2.30%	2.40%	2.40%	2.40%	2.50%	2.50%	2.60%	2.60%	2.60%
50Yr PWLB	1.90%	2.00%	2.10%	2.20%	2.20%	2.20%	2.30%	2.30%	2.40%	2.40%	2.40%

8.2 The Council is, as stated above, expecting to have to borrow externally between 2021 and 2023 to finance capital expenditure on assets. Approval was given as part of the Capital Investment Strategy approved in September 2016, for the Section 151 Officer to undertake external borrowing at a time it was felt to be most appropriate to be used for the repayment or refinancing of the £15million stock issue and/or to fund the capital programme where a borrowing requirement has been identified, taking into account forecasts for potential rises in interest rates and utilising any favourable borrowing rates. It is anticipated that although a combination of capital grants and internal resources will be used to meet most capital commitments in the new financial year there will be a requirement to borrow externally. Nevertheless, the use of external borrowing is planned for in future years. The Corporate Director of Finance and Resources will therefore continue to monitor the interest rate market as regards borrowing opportunities as well as in respect of investment policy.

8.3 Against this background and the risks with the economic forecast, caution will be adopted with the 2022/23 treasury operations. The Corporate Director of Finance and Resources will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- If it was felt that there was a significant risk of a sharp FALL in long term and short-term borrowing rates (e.g. due to a marked increase in the risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into shorter term borrowings will be considered.
- 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 an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

8.4 **<u>Policy on borrowing in advance of need</u>**

8.4.1 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds. As part of the Capital Investment Strategy approved by Council in September 2016, approval in principle was given to the Council's S.151 Officer to borrowing in advance of need for the re-financing of the stock issue loan and/or to fund the capital programme where a borrowing requirement has been identified, if interest rates were favourable and would be cost effective over the term of any new loan.

8.5 **<u>External v. Internal Borrowing</u>**

8.5.1 This Council currently has differences between gross debt and net debt (after deducting cash balances). This is shown in the graphs at 6.2.2.

8.5.2 The general aim of this Treasury Management Strategy is to reduce the difference between the two debt levels over the next three years in order to reduce the credit risk incurred by holding investments. However, measures taken in the last year have already reduced substantially the level of credit risk (see paragraph 10.2) so another factor which will be carefully considered is the difference between borrowing rates and investment rates to ensure the Council obtains value for money once an appropriate level of risk management has been attained to ensure the security of its investments.

8.5.3 The next financial year will likely be one of continued low Bank Rates even though there may well be incremental increases from the current levels. This provides a continuation of the current window of opportunity for local authorities to fundamentally review their strategy of undertaking new external borrowing.

8.5.4 Over the next three years, investment rates are expected to continue to be below long-term borrowing rates and so value for money considerations would indicate that value could best be obtained by avoiding new external borrowing by using internal cash balances to finance new capital expenditure or to replace maturing external debt (this is referred to as internal borrowing). This would maximise short term savings.

8.5.5 However, short term savings by avoiding new long-term external borrowing in 2022/23 will also be weighed against the potential for incurring additional long-term extra costs by delaying unavoidable new external borrowing until later years when PWLB long term rates are forecast to be significantly higher. By utilising internal cash balances consideration will also need to be given to the availability of cash to service the day-today cash flow of the Council. This could require the Council to undertake short-term borrowing to cover cash-flows.

8.5.6 Against this background caution will be adopted with the 2022/23 treasury operations. The Corporate Director of Finance and Resources will monitor the interest rate market and adopt a pragmatic approach to changing circumstances, reporting any decisions to the appropriate decision-making body at the next available opportunity.

9. DEBT RESCHEDULING

9.1 There is unlikely to be much scope for debt rescheduling in either the current financial year or in 2022/23.

10. INVESTMENT STRATEGY

10.1 <u>Principles</u>

10.1.1 The DLUHC and CIPFA have extended the meaning of ‘investments’ to include both financial and non-financial investments. This report deals solely with financial investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets (e.g. property), are covered in the Capital Investment Strategy.

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

- DLUHC's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the Code")
- CIPFA Treasury Management Guidance Notes 2018

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

10.1.4 The Council will also endeavour to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. Security of principal will always be the primary consideration. The risk appetite of this Council is low in order to give priority to security of its investments.

10.1.5 The above guidance from the DLUHC and CIPFA place a high priority on the management of risk. This authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means (Further details of limits and timescales for all approved investments are shown at **Appendix B**): -

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

- Credit ratings will be used as one means of assessing the credit quality of rated counterparties although it is recognised that reliance should not be placed on credit rating alone. The minimum short-term rating for a bank will be either F1 (Fitch) or P1 (Moody's). For a rated UK building society, a similar rating would be anticipated although the proposed criteria do give authority to the Corporate Director of Finance and Resources to approve, if considered appropriate, the addition of other building societies with both a F2 (Fitch) and a P2 rating (Moody's). This is still a high-quality credit rating but recognises the very strong record of the UK building society movement over many years in protecting the capital of all depositors. The Strategy already allows discretion to the Corporate Director of Finance and Resources to include as counterparties non-credit rated building societies whose assets total at least £1bn. Any such investment would be subject to an assessment of such a society as a suitable counterparty. There are, for example, good reasons why many building societies do not have a credit rating but there are other means of making an appropriate financial judgment.

- **Other information:** ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as **"credit default swaps"** and overlay that information on top of the credit ratings.

- **Other information sources** used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

- This authority has defined the list of **types of investment instruments** that the treasury management team are authorised to use. There are two lists in Appendix B under the categories of 'specified' and 'non-specified' investments.
    - **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.
    - **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.

- **Non-specified investments limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being 50% of the total investment portfolio.

- **Lending limits**, (amounts and maturity), for each counterparty are set. Total investments with any one counterparty or group currently will not exceed £10m to ensure a reasonable spread of investments in terms of counterparties. Investments with Money Market Funds and investments in overseas banks with a sovereign rating of not less than the UK sovereign rating will not exceed £4m.

- **Transaction limits** are set for each type of investment are set.

- This authority will set a limit for the amount of its investments which are invested for **longer than 365 days**.

- Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating**.

- This authority has engaged **external consultants**, (see paragraph 4), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.

- All investments will be denominated in **sterling**.

- As a result of the change in accounting standards for 2019/20 under **IFRS 9,** this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (The Ministry of Housing, Communities and Local Government [DLUHC], have recently issued a statutory override for Local Authorities so that the impact of IFRS9 does not affect a Council's General Fund. This override is currently in place for 5-years from 1st April 2018.)

- Due care will be taken to consider the country, group and sector exposure of the Council's investments. In addition:
  <u>Country limits</u>:
  - where the country of registration of an institution has an average credit rating (i.e. an average sovereign credit rating) equal to, or better than that of the UK; it will enable the Council to consider the placement of investments on the same basis applied for UK-registered institutions (i.e. subject to the overarching counterparty criteria as set out at **Appendix B**; and
  - where an institution meets the approved counterparty status* but the country of registration has an average credit rating below that of the UK; limit such investments in total to such rated non-UK countries to be no more than £2m of the portfolio.
    i.e. it meets the overarching counterparty criteria as set out at **Appendix B**.
  - sector limits will be monitored regularly for appropriateness.

10.1.6 Following approval in 2014/15, the Council now makes use of the CCLA Property Fund for longer term investments, and at present has invested £3m into this fund. The anticipated yield from this investment is assumed to be 4.00% in the MTFP.

10.1.7 Any investments with institutions that do not have a credit rating e.g. many smaller building societies or investments for periods over one year would be classed as non-specified investments**. However, it is important to stress that both the specified and non-specified investments in Appendix B are perfectly legal instruments in which the City Council may invest.** This includes for example many building societies as only the larger societies have an individual credit rating although there are other criteria by which a judgement can be made as to their credit quality.

10.2 Creditworthiness Policy

10.2.1 This Council applies the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard & Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- CDS spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

10.2.2 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 for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore have consideration to using counterparties within the following durational bands:

Yellow	5 Years *
Dark Pink	5 years for Ultra-Short Dated Bond Funds with a credit score of 1.25
Light pink	5 years for Ultra-Short Dated Bond Funds with a credit score of 1.5
Purple	2 years
Blue	1 year (only applies to nationalised or semi nationalised UK Banks)
Orange	1 year
Red	6 months
Green	100 Days
No Colour	Not to be used

**The Council does not usually invest for longer periods than 2-years, however if it were to it would follow the same creditworthiness policy provided by Link Asset Services*

10.2.3 The Link Asset Services' creditworthiness service uses a wider array of information other than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

10.2.4 All credit ratings will be monitored weekly. The Council is alerted to changes to ratings of all three agencies through its use of the Link Asset Services' creditworthiness service.

- if a downgrade results in the counterparty / investment scheme 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 daily basis via its Passport website, provided exclusively to it by Link Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

10.2.5 Sole reliance will not be placed on the use of this external service. In addition, this Council will also use market data and market information, information on any external support for banks to help support its decision-making process.

10.3 **Investment Strategy**

10.3.1 With bank base rate forecast for a first increase in Bank Rate in late 2021. However, the September 2021 Monetary Policy Committee (MPC) meeting minutes indicated that their concerns over the sudden recent rise in multiple inflationary pressures could well mean that an earlier increase in Bank Rate is now possible ahead of the start of the financial year covered by this Strategy. The view of Link Asset Services is that bank rate will be at the following levels:

	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Bank Rate	0.25%	0.25%	0.50%	0.50%	0.50%	0.75%	0.75%	0.75%	0.75%	1.00%

10.3.2 The Council has historically outperformed bank rates in its investment returns. Therefore, the suggested budgeted average investment earnings currently included in the MTFP projections are as follows:

	Investment Balances	CCLA Property Fund
2022/23	0.83%	4.00%
2023/24	1.08%	4.00%
2024/25	1.33%	4.00%

10.3.3 Clearly, these projections can only be best estimates at this stage and the risk is to the downside i.e. if the economic recovery is slower than expected, then interest rates are likely to rise more slowly. At this stage, the budget for 2022/23 has assumed an average yield of 0.83% on its investments (excluding CCLA Property Fund) in the next financial year. This allows for the fact that there are some higher value, longer term investments placed and there will be some shorter dated instant access investments placed. This forecast will, however, be reviewed further during the budget cycle. The anticipation of interest yielded from investing in the Property Fund is estimated at 4.00% in the MTFP.

10.3.4 In this situation, the authority will continue to try and seek value in its investments by placing them out for longer periods where possible e.g. six months to one year, to meet future cash flow needs, subject to retaining some sums for shorter periods to meet liquidity requirements and also to take advantage of any particular investment opportunities. Much of the basic framework of the authority's cash flows is already known for the next financial year and use will be made of this information in determining investment periods. The money market is monitored daily and use will be made of a plurality of sources of financial information in determining investment opportunities. All investments will be placed only with institutions that conform to the criteria set out in the Investment Strategy. However, should the council use internal cash balances to support the capital programme rather than undertaking external borrowings this will have a significant impact on the investment returns achieved, but will be offset by reduced costs of borrowing.

10.3.5 The investment income budget will, as ever, be carefully monitored in the coming financial year and reported to members via the regular Treasury Transactions reports.

10.4 **<u>End of Year Investment Report</u>**

In line with current practice, the Council will receive a report on its investment activity as part of the Annual Treasury Report at the end of the financial year. It should also be noted that best practice now requires a mid-year report on the treasury function. This has long been the practice within the City Council where quarterly reports are presented to the Executive. In addition, the Audit Committee has taken on the role of the 'strategic committee' that oversees treasury matters.

11. THE MINIMUM REVENUE PROVISION STRATEGY

11.1 The Council implemented the new Minimum Revenue Provision (MRP) guidance in 2008/09 and will assess their MRP for 2022/23 in accordance with the main recommendations contained within the guidance issued by the Secretary of State under section 21(1A) of the Local Government Act 2003. Furthermore, the Council revised its MRP Policy in 2017/18 to provide for MRP on a 3% straight Line basis going forward.

11.2 The Council is currently forecasting to undertake additional external borrowing in 2022/23 to facilitate the delivery of its capital programme. Current estimates include this borrowing on a principal and interest repayment basis. Any principal repaid would be a cash outflow for the Council and cash would be replenished through the charging of MRP from the General Fund to reduce the underlying borrowing requirement.

11.3 The Council is obliged to make proper provision for the repayment of its outstanding debt liabilities. Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. land, buildings, vehicles etc. It would usually be impractical to charge the entirety of such expenditure, which is often funded by borrowing, to the revenue account in the year it was incurred. Instead, this is spread over a longer period to try and match the years over which these assets will benefit the community. The manner of spreading these costs is through the Minimum Revenue Provision (MRP). Until recently, the MRP was calculated according to detailed and complex regulations. It is now determined under Guidance.

11.4 The only statutory duty that a local authority has under the new MRP regime is *'to determine for the current financial year an amount of minimum revenue provision that it considers to be prudent'*. The Guidance, which authorities must 'have regard to' provides four options for calculating the MRP. It is important to realise, however, that there is no obligation to follow any of these options and that it is up to each authority to decide upon the most appropriate method of making a prudent provision, having had regard to the Guidance.

11.5 Using the 3% Straight Line method for calculating the MRP charge more reflects an average life of Council assets of 33 years and since it has a mix of short life assets such as vehicles (typical life 5-10 years) and long-life assets such as land and buildings (typical life 40-50+ years) this is still deemed to be a prudent approach to take.

11.6 In 2021/22, the opening CFR was £19.521million.

11.7 In 2018/19 the Council implemented a recommendation from Link Asset Services to review its CFR for MRP purposes in relation to what is known as 'Adjustment A'. The purpose of Adjustment A was to ensure that the starting point for calculating MRP under the new system in 2004 did not significantly vary the level of liability that would have arisen had the previous system of capital controls remained unchanged.

11.8 The MRP review undertaken by (then) Capita Asset Services identified a misstatement in the basis of calculation of Adjustment A which indicated that the value originally assessed in 2004/05 to be understated. The Council's reassessed Adjustment A figure is £4.426 million. This misstatement related to the inclusion of revenue expenditure (premiums on the early repayment of debt) being included in the original Adjustment A calculation which the Code states should be excluded from the calculation.

11.9 Therefore when calculating MRP for future years, the actual Capital Financing requirement should be reduced by this Adjustment A figure and then MRP charged at 3% of the reduced figure.

11.10 The CFR and MRP charges currently included in the MTFP and budget projections are as follows (The MRP charge calculated for 2022/23 is chargeable in 2023/24 and so on):

	2022/23 £000	2023/24 £000	2024/25 £000
Opening CFR	19,521	40,544	50,878
Closing CFR	**40,544**	**50,878**	**52,192**
Adjustment A	4,426	4,426	4,426
Adjustment Assets Under Construction	19,165	0	0
CFR for MRP Purposes	**16,953**	**46,452**	**47,766**
MRP Charge @ 3%	**509**	**1,394**	**1,433**
Adjustments to MRP for historical Overpayments	(241)	(241)	(241)
Actual MRP charge	**268**	**1,153**	**1,192**
Voluntary MRP	0	0	0
Actual MRP charge	**268**	**1,153**	**1,192**

11.11 MRP is a statutory requirement for local authorities to charge to their revenue account for each financial year a prudent amount for the principal cost of their debt in that financial year. It impacts upon the CFR, one of the Council's prudential indicators.

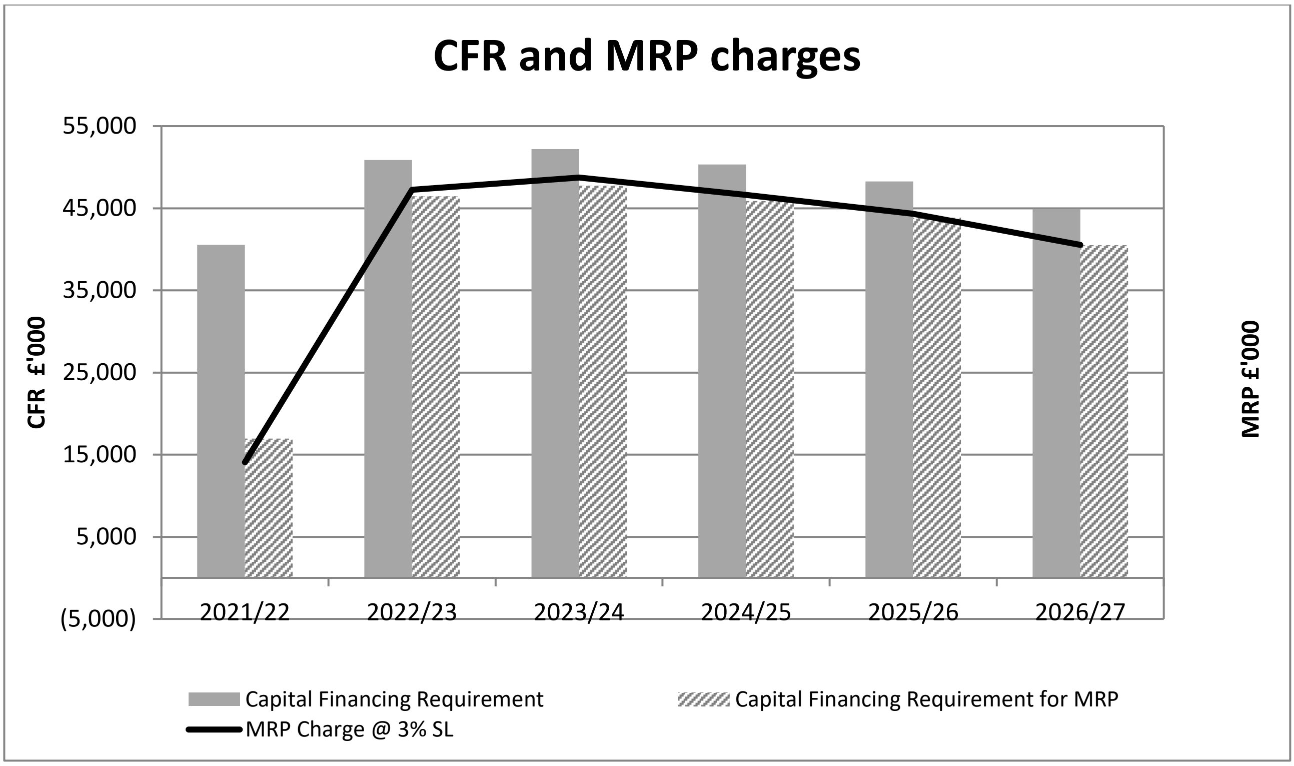
11.12 The CFR is a measure of the Council's underlying debt liability, resulting from historic capital expenditure which has been financed from borrowing. Amending the MRP as proposed will lead to an increase in the short to medium term CFR compared to current projections. This is because the MRP reduces the CFR each year, so a decrease in the amount of reduction causes an increase in the current projected CFR.

11.13 When an amount previously set aside for debt liability in the budget is released and then used for another revenue purpose the Authority will have less cash. This is likely to lead to a reduction in external investments and with thus lead to a reduction in interest income.

11.14 The regulations allow the Authority to review its policy every year and set a policy that it considers prudent at that time. The impact of a revised MRP policy will be kept under regular review in order to ensure that the annual provision is prudent.

11.15 As the MRP policy has to be considered by the Executive and approved by Council each year there will be an opportunity to revisit any decision at least annually or make additional voluntary payments.

11.16 The chart below shows the anticipated CFR in future years as well as the CFR for MRP Calculation purposes.



CFR and MRP charges
55,000
45,000
35,000
25,000
15,000
5,000
(5,000)
CFR £'000
MRP £'000
2021/22
2022/23
2023/24
2024/25
2025/26
2026/27
Capital Financing Requirement
Capital Financing Requirement for MRP
MRP Charge @ 3% SL

APPENDIX B

APPROVED INVESTMENT INSTRUMENTS

Specified Investments

All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' rating criteria where applicable.

- All UK banks and building societies with a minimum specified 'high' credit rating shall have a **maximum of £6m** as the counterparty limit **(individual Transaction Limit for fixed term investments £2m, for instant access and call accounts £6m)**.
- Investments with Lloyds Group banks, HSBC, Santander and Goldman Sachs shall have a maximum of **£10m** as the counterparty limit.
- All overseas banks with a sovereign rating of not less than the UK sovereign rating and a minimum individual credit rating, shall have a **maximum of £4m** as the counterparty limit **(individual Transaction Limit for fixed term investments £2m, for instant access and call accounts £4m)**.
- Where an institution meets the approved counterparty status but the country of registration has an average credit rating below that of the UK; limit such investments in total to such rated non-UK countries to be no more than **£2m** as the counterparty limit. **(individual Transaction Limit for fixed term investments £2m, for instant access and call accounts £2m)**.
- UK building societies that are not credit rated shall have a maximum of **£2m** as the counterparty limit. **(individual Transaction Limit for fixed term investments £2m, for instant access and call accounts £2m)**.
- MMFs shall have a maximum counterparty limit of **£4m (Individual Transaction limit of £4m).**

Fixed Term Deposits with fixed rates and maturities:-	Minimum 'High' Credit Criteria	Use
Debt Management Agency Deposit Facility	Government backed	In-house
Term deposits – local authorities	--High level of security	In-house
Term deposits – U K banks**	Short-term F1 (Fitch) or P1(Moodys)	In-house
Term Deposits – UK building societies**	Short Term F1 (Fitch) or P1 (Moodys) or as determined by the Chief Finance Officer	In-house
Term Deposits – Non UK Banks	Sovereign Rating (not less than UK) Short Term F1 (Fitch) or P1 (Moodys) or as determined by the Chief Finance Officer	In-house
Fixed term deposits with variable rate and variable maturities: -	**Minimum 'High' Credit Criteria**	**Use**
Callable deposits	Short-term F1 (Fitch) or P1 (Moodys)	In-house
Certificates of deposits issued by UK banks and building societies	Short-term F1 (Fitch) or PI (Moodys)	In-house buy and hold
UK Government Gilts	Government backed	In-house buy and hold

Bonds issued by multilateral development banks	AAA	In-house on a ‘buy-and-hold’ basis.
Bonds issued by a financial institution which is guaranteed by the UK government	AAA	In-house on a ‘buy-and-hold’ basis.
Collective Investment Schemes structured as Open Ended Investment Companies (OEICs): -	**Minimum ‘High’ Credit Criteria**	**Use**
1. Money Market Funds	Short-term AAA	In-house
2. Enhanced Cash Funds	Short-term AAA	In-house
3. Government Liquidity Funds	Short-term AAA	In-house

** If forward deposits are to be made, the forward period plus the deal period should not exceed one year in aggregate.

<u>Non-Specified Investments</u>:

A maximum of 50% will be held in aggregate in non-specified investments

1. Maturities of ANY period.

	Minimum Credit Criteria	Use	Max % of total investments	Max. maturity period
Term deposits with non credit rated UK Building Societies	As approved by the S151 Officer. Minimum asset base of £1bn	In-house	50	364 days
Ultra-Short Dated Bond Funds with a credit score of 1.25	AAA	In-house	50	Liquid
Ultra-Short Dated Bond Funds with a credit score of 1.5	AAA	In-house	50	Liquid

2. Maturities in excess of 1 year

	Minimum Credit Criteria	Use	Max % of total investments	Max. maturity period
Term deposits – local authorities	Any authority	In-house	50	3 Years
Term deposits – UK banks and building societies	Long-term A (Fitch) or A2 (Moodys)	In-house	50	3 Years
Fixed term deposits with variable rate and variable maturities	**Minimum Credit Criteria**	**Use**	**Max % of total investments**	**Max. maturity period**
Certificates of deposits issued by UK banks and building societies	Long-term A (Fitch) or A2 (Moodys)	In house on a 'buy and hold basis'	50	3 Years
UK Government Gilts	Government backed	In house on a 'buy and hold basis'	50	3 Years
Bonds issued by multilateral development banks	AAA	In-house on a 'buy-and-hold' basis.	50	3 Years
Bonds issued by a financial institution which is guaranteed by the UK government	AAA	In-house on a 'buy-and-hold' basis.	50	3 Years
Collective Investment Schemes structured as Open Ended Investment Companies (OEICs)	**Minimum Credit Criteria**	**Use**	**Max % of total investments**	**Max. maturity period**
1. Bond Funds	Long-term AAA	In-house	50	3 Years
2. Gilt Funds	Long-term AAA	In-house	50	3 Years

3. Approved Property Funds

	Use	Max % of total investments	Max. maturity period
CCLA Property Fund	In-house as determined by the S151 Officer	50	No maximum

The Council uses Fitch (primarily) or Moody's ratings to derive its counterparty criteria. All credit ratings will be monitored monthly. The Council is alerted to changes in credit ratings through its use of the Link Asset Services creditworthiness service. If a downgrade results in the counterparty/investment scheme no longer meeting the Council’s minimum criteria, its further use as a new investment will be withdrawn immediately.

APPENDIX C

INTEREST RATE FORECASTS

The data below shows a variety of forecasts published by Link Asset Services and Capital Economics. The forecast within this strategy statement has been drawn from these diverse sources and officers' own views. Revised forecasts will be provided when they become available. The rates shown below for PWLB borrowing include the 20bps reduction for the Certainty Rate.

1. INDIVIDUAL FORECASTS

Link Group Interest Rate View	8.11.21													
	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
BANK RATE	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25
3 month ave earnings	0.30	0.40	0.50	0.50	0.50	0.60	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00
6 month ave earnings	0.40	0.50	0.60	0.60	0.70	0.80	0.90	1.00	1.10	1.10	1.10	1.10	1.10	1.10
12 month ave earnings	0.50	0.60	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20	1.20
5 yr PWLB	1.50	1.50	1.60	1.60	1.70	1.70	1.70	1.80	1.80	1.80	1.90	1.90	2.00	2.00
10 yr PWLB	1.80	1.90	1.90	2.00	2.00	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.30	2.40
25 yr PWLB	2.10	2.20	2.30	2.40	2.40	2.40	2.50	2.50	2.60	2.60	2.60	2.60	2.70	2.70
50 yr PWLB	1.90	2.00	2.10	2.20	2.20	2.20	2.30	2.30	2.40	2.40	2.40	2.40	2.50	2.50
Bank Rate														
Link	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25
Capital Economics	0.25	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	-	-	-	-	-
5yr PWLB Rate														
Link	1.50	1.50	1.60	1.60	1.70	1.70	1.70	1.80	1.80	1.80	1.90	1.90	2.00	2.00
Capital Economics	1.60	1.70	1.70	1.80	2.10	2.10	2.10	2.10	2.10	-	-	-	-	-
10yr PWLB Rate														
Link	1.80	1.90	1.90	2.00	2.00	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.30	2.40
Capital Economics	1.80	1.90	2.00	2.20	2.30	2.30	2.30	2.30	2.30	-	-	-	-	-
25yr PWLB Rate														
Link	2.10	2.20	2.30	2.40	2.40	2.40	2.50	2.50	2.60	2.60	2.60	2.60	2.70	2.70
Capital Economics	2.10	2.20	2.40	2.60	2.70	2.80	2.80	2.80	2.90	-	-	-	-	-
50yr PWLB Rate														
Link	1.90	2.00	2.10	2.20	2.20	2.20	2.30	2.30	2.40	2.40	2.40	2.40	2.50	2.50
Capital Economics	1.90	2.00	2.20	2.40	2.50	2.60	2.60	2.60	2.70	-	-	-	-	-

APPENDIX D

TREASURY MANAGEMENT POLICY STATEMENT

Carlisle City Council defines treasury management as:

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

Carlisle City Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the authority, and any financial instruments entered into to manage these risks.

Carlisle City Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

Investment Policy

The Council will manage its investments in line with the criteria set out in section 9 of the TMSS with the security of investment being paramount. The Council's investments will be placed in line with those outlined in Appendix B of the TMSS.

Borrowing Strategy

The Council will manage its borrowings in line with the criteria set out in section 8 of the TMSS with the emphasis being on external borrowing only being taken when absolutely necessary and ensuring it offers the best value for money.