Item 5

Cabinet

7 March 2019

Treasury Management Strategy

Recommendations

That:

1) Cabinet recommends to the County Council that the Treasury Management Strategy and Investment Strategy for 2019/20 (Appendix A-I) be approved and their provisions have effect from 1st April 2019.

2) Cabinet recommends that the County Council requires the Strategic Director of Resources to ensure that gross borrowing does not exceed the prudential level as specified in Appendix B, taking into account current commitments, existing plans, and the proposals in the budget report.

3) Cabinet recommends that the County Council delegate authority to the Strategic Director of Resources to undertake all the activities listed in Appendix H of this report.

4) Cabinet recommends that the County Council requires the Strategic Director of Resources to implement the Minimum Revenue Provision Policy as specified in Appendix I.

1.0 Key Issues

1.1 The Council is required to set a Treasury Management Strategy each year and this report sets out the proposed strategy for 2019/20 at Appendix A-I.

1.2 The strategy is guided by the need to maintain security, liquidity, and yield, in that order of priority.

1.3 In response to updated government guidance the strategy has regard to the expectation that local authorities should not expose public funds to unnecessary or unquantified risk, and that local authorities must not borrow in advance of need or purely to profit from the investment of the extra sums borrowed. Council's may however make investments for commercial or service reasons and investments of this nature have been entitled "Non Treasury Management".

2.0 Strategy

2.1 The strategy is updated for current forecast conditions which include a slow increase in the bank rate and borrowing rates.

2.2 The strategy includes a £60m limit for investments over 365 days. This assists in facilitating options to consider longer dated investments.

2.3 The strategy also considers a new requirement to report on non-Treasury Management investments. This is driven by the Government observing an increasing number of local authorities taking on increasing levels of risk in search of financial returns to support the financial position of the authority or in search of new ways to meet the service objectives of the authority. The purpose of the new requirements is to ensure that local authorities do not take excessive risks and do manage and report risks appropriately. Section 3 sets out more details about this requirement.

3.0 Non Treasury Management Investments

3.1 Non treasury management investments may take a number of forms:

- Holding shares in companies, for example companies that promote organisational objectives such as protecting the environment.
- Issuing loans to companies, for example promoting economic development.
- Holding non-financial assets (e.g. property) for the sole or primary purpose of making a financial return.

3.2 The County Council does not at present rely on significant income streams from commercial or service investment activities, however this may change over time.

Companies – Service Investments

3.3 The Council holds shares and debt with some companies for the purposes of promoting the achievement of organisational objectives. These companies may provide a return on investment but that is not the primary reason for their existence. At the time of writing this report such investments included:

- University of Warwick Science Park Innovation Centre Ltd
- Warwick Technology Park Management Company Ltd
- Warwick Technology Park Management Company (No2) Ltd
- Eastern Shires Purchasing Organisation (ESPO)
- SCAPE Group Ltd
- Coventry and Warwickshire Local Enterprise Partnership
- Coventry and Warwickshire Waste Disposal Company
- UK Municipal Bond Agency PLC
- Border to Coast Pension Partnership Ltd

3.4 The share value relating to the above companies recorded in the 2017/18 accounts was £2m, with dividend income of £1m.

3.5 In addition to the above the Council currently operates two wholly owned Local Authority Trading Companies:

- Warwickshire Legal Services Trading Ltd
- Educaterers Ltd

3.6 The total shareholder value of these companies in their most recent accounts is £147k and there is a £1.5m loan facility in place with Educaterers until August 2020 to provide support to cash flow.

Loans to Local Businesses

3.7 The capital programme includes allocations available for the purposes of making grants or loans to local businesses who cannot raise funds through other means such as banks.

3.8 The maximum exposure to loans in 2019/20 of £892k, which makes up 0.4% of the 2019/20 capital budget which is £230.6m. Interest is charged at the Bank of England base rate (currently 0.75%) so the maximum interest income and therefore exposure to income loss is approximately £7k in 2019/20. Loans are made through the Coventry and Warwickshire Reinvestment Trust.

Property Investments

3.9 The Council does not currently invest in property for the purposes of generating commercial income, however the Council does currently hold some assets for the purpose of generating future capital receipts. The value of these assets can change and these assets generate a small amount of incidental income. The properties classified as investment property in 2017/18 had an asset value of £58.9m as at March 2018, out of a full asset value in the balance sheet of £1.192bn.

4.0 Measures

4.1 To support risk management in the development of future potential investments, measures will be developed to monitor the Council's position and some measures may be used to set controls and limits in alignment with the Council's risk appetite. Examples of key measures may include:

- Total Investment Related Commercial Income. This would provide an indication of the financial value of commercial income upon which the Council revenue budget is reliant.
- Ratio of Investment Related Commercial Income to Net Service Expenditure. This would provide an indication of the proportionality of reliance on commercial income.

- Total Assets At Risk – This would provide a measure of the total assets owned for commercial or service purposes which are at risk of loss in value.

5.0 Strategy Statement Requirements

5.1 Although the Council does not currently have a policy of investing in non-treasury management assets for the purpose of generating a financial return the Treasury Management Strategy is required to have regard to service and commercial investments and set out the Council's approach to managing them. The Strategy therefore includes new commentary in respect of non-Treasury Management activities (Appendix A, Section 8) and this will be reviewed over time.

Background papers

None

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The report was circulated to the following members prior to publication:

Local Member(s): N/A
Other members: O'Rourke, Butlin, Boad, Timms, Roodhouse, Chilvers, Chattaway and Singh Birdi

Appendix A

Warwickshire County Council
Treasury Management Strategy Statement
2019/20

1 Introduction

Background

1.1 Treasury management is defined as:

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

1.2 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 security of capital and sufficient 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 occasions, debt previously drawn may be restructured to meet Council risk or cost objectives.

Statutory Requirements

1.4 The Local Government Act 2003 (the Act) and supporting regulations require the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

1.5 The Act therefore requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance subsequent to the Act and included in section 7 of this report). This sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

CIPFA Requirements

1.6 The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
3. Receipt by the full Council of an annual Treasury Management Strategy Statement, to include the Annual Investment Strategy and Minimum Revenue Provision Policy for the year ahead, a Mid-year Review Report and an Annual (stewardship) Report covering activities during the previous year.
4. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
5. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is Resources and Fire & Rescue Overview and Scrutiny Committee.

Treasury Management Strategy for 2019/20

1.8 The proposed strategy for 2019/20 is based upon the treasury officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury adviser, Link Asset Services.

1.9 The strategy covers:

- Treasury limits for 2019/20 to 2021/22
- Prudential Indicators
- Prospects for Interest Rates
- Borrowing Strategy
- Debt Rescheduling
- Annual Investment Strategy
- Minimum Revenue Provision Strategy

Balanced Budget Requirement

1.10 Under Section 42B of the Local Government Finance Act 1992, it is a statutory requirement for the Council to produce a balanced budget. In particular, Section 42A states a local authority must include the revenue costs that flow from capital financing decisions in its budget requirement for each financial year. Therefore increases in capital expenditure must be limited to a level whereby charges to revenue derived 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.

MiFID II

1.11 The Markets in Financial Instruments Directive ('MiFID') was introduced due to increasing complexity of financial products and issues related to the 2008 financial crisis. Part two of the directive came into effect in January 2018 and re-classified investors into 'professional' or 'retail' clients. Officers have met the conditions to fulfil the role of professional client and this has enabled the treasury asset allocation to continue without disruption.

2 Treasury Limits for 2019/20 to 2021/22

2.1 It is a statutory duty under Section 3 of the Act and supporting regulations for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the "Affordable Borrowing Limit". In England and Wales, the Authorised Limit represents the legislative limit specified in the Act.

2.2 The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and the impact upon its future council tax is 'acceptable'.

2.3 Whilst termed an "Affordable Borrowing Limit", the capital to be considered for inclusion in corporate financing is both external borrowing and other forms of liability, such as credit arrangements. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years. Details of the Authorised Limit can be found in Appendix B of this report. Explanations of the terminology employed in the Appendix can be found in Appendix C.

3 Prudential Indicators for 2019/20 to 2021/22

3.1 The Prudential and Treasury Indicators relevant to the setting of an integrated Treasury Management Strategy are set out at Appendix B to this report.

3.2 Council will approve the Prudential Indicators as part of the budget resolution in February 2019. These indicators will be revised, if necessary, for the Council approved capital programme.

3.3 The Prudential Indicators are relevant for the purposes of setting an integrated Treasury Management Strategy. The indicators are provisional and based on the current agreed capital programme.

4 Prospects for Interest Rates

4.1 The Council has appointed Capita as treasury advisor to the Council and part of their service is to assist the Council to formulate a view on interest rates. The table below sets out Capita's view on the future Bank Rate.

Capita Bank Rate Forecast

	Bank Rate %
Jan 2018 to Aug 2019	0.75
Sep 2019 to May 2020	1.00
Jun 2020 to Feb 2021	1.25
Mar 2021 to Aug 2021	1.50
Sep 2021 to Feb 2022	1.75
Mar 2022 -	2.00

4.2 A detailed view of the current economic background is contained within Appendix D to this report.

5 Borrowing Strategy

5.1 The Council is currently maintaining an over borrowed position. This means there is no current need for further capital borrowing in order to meet the Capital Financing Requirement. Based on the estimates of medium term capital expenditure, the Council's gross borrowing covers the Capital Financing Requirement until 2021/22.

5.2 The Treasury Team will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances. Any borrowing decisions will be reported to the Resources and Fire & Rescue Overview and Scrutiny Committee at the next opportunity.

5.3 The Link forecasts for the Public Works Loan Board (PWLB) new borrowing rates are as follows:

Annual Average %	PWLB Borrowing Rates % (including *certainty rate adjustment)		
	5 year	**25 year**	**50 year**
Mar 2019	1.80	2.70	2.50
Jun 2019	1.90	2.80	2.60
Sep 2019	2.00	2.90	2.70
Dec 2019	2.10	3.00	2.80
Mar 2020	2.20	3.10	2.90
Jun 2020	2.30	3.20	3.00
Sep 2020	2.30	3.20	3.00
Dec 2020	2.40	3.30	3.10
Mar 2021	2.50	3.40	3.20
Jun 2021	2.50	3.40	3.20
Sep 2021	2.60	3.50	3.30
Dec 2021	2.60	3.50	3.30
Mar 2022	2.70	3.60	3.40

* The Government has reduced by 20 basis points (0.20%) the interest rates on loans to principal local authorities who provide information as required on their plans for long-term borrowing and associated capital spending (the Certainty Rate).

5.4 In view of the above forecast, the Council's borrowing strategy will be based upon the following:

- The cheapest borrowing will be internal borrowing by running down cash balances and foregoing interest earned at historically low rates.

- Internal borrowing will be weighed against potential long term costs that will be incurred if market loans at long term rates are higher in future years.

- Long term fixed rate market loans at rates significantly below PWLB rates for the equivalent maturity period will be considered where available, to ensure the best rates and to maintaining an appropriate balance between PWLB and market debt in the debt portfolio.

- PWLB borrowing for periods under ten years will be considered where rates are expected to be significantly lower than rates for longer periods. This offers a range of options for new borrowing which will spread debt maturities away from a current concentration in longer dated debt.

5.5 Against this background and the risks within the economic forecast, caution will be adopted with treasury operations. The Assistant Director of Finance and ICT Strategy will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances, for example:

- if it was felt that there was a significant risk of a sharp fall in long and short term rates then long term borrowings may be postponed, and potential rescheduling from fixed rate funding into short term borrowing 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, a likely action will be that fixed rate funding will be drawn whilst interest rates are still lower than they will be in the next few years

Policy on borrowing in advance of need

5.8 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 considered carefully to ensure value for money can be demonstrated and that the Council can ensure the security of such funds.

5.9 In determining whether borrowing will be undertaken in advance of need, the Council will:

- Ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to fund in advance of need;

- Ensure the ongoing revenue liabilities created, and the implications on future plans and budgets have been considered;

- Evaluate the economic and market factors that might influence the manner and timing of any decision;

- Consider the merits and demerits of alternative forms of funding;

- Consider the alternative interest rate bases available, the most appropriate time periods and repayment profiles;

- Consider the impact of temporarily increasing cash balances until cash is required to finance capital expenditure, and the consequent increase in exposure to counterparty and other risks.

Scheme of Delegation

5.10 The scheme of Delegation for Treasury Management Strategy decision making and overview/scrutiny are shown in Appendix E.

6 Debt Rescheduling

6.1 As short term borrowing rates are cheaper than longer term rates, there may be opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of their short term nature and the likely cost of debt repayments.

6.2 The reasons for any rescheduling to take place will include:

- The generation of cash savings and/or discounted cash flow savings;
- Helping to fulfil the strategy
- Enhancing the balance of the portfolio, for example reducing concentration of the debt maturity profile.

6.3 Consideration will also be given to identify if there is any potential for making savings by running down investment balances in order to repay debt prematurely as short term interest received on investments is likely to be lower than interest paid on current debt.

6.4 Consideration will be given to the option of making pension fund contributions earlier than is required.

6.5 The option to make repayment of some external debt to the PWLB in order to reduce the difference between its gross and net debt position will be kept under review. However, the penalty premiums that would be incurred by doing so means there currently is no net financial benefit from such early repayment. The Municipal Bonds Agency offers loans to local authorities and is on our list of options that we may consider.

7 Annual Investment Strategy

Investment Policy

7.1 The Council will have regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code").

7.2 The Council's investment priorities will be security first, liquidity second and then return.

7.3 In accordance with the above, and in order to minimise the risk to investments, the Council has stipulated in Appendix F, the minimum acceptable credit quality of counterparties for inclusion on the lending list.

7.4 It is recognised that ratings should not be the sole determinant of the quality of an institution and that 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 the institutions operate. The assessment will also take account of information that reflects the opinion of the markets. The Council will engage with its advisors to assist in this.

7.5 Other information sources used will be used including the financial press, share price and other such information pertaining to the banking sector in order to scrutinise the suitability of potential investment counterparties. The aim of the strategy is to generate a list of highly creditworthy counterparties which will enable diversification and therefore avoid concentration risk. The intention of the strategy is to provide security of investment and minimisation of risk.

7.6 Investment instruments identified for use in the financial year are listed in Appendix F under the 'Specified' and 'Non-Specified' Investments categories. Counterparty limits will be as set through the Council's Treasury Management Practices Schedules.

7.7 The Council on occasion will hold long term investments or provide loans for operational policy reasons, for example, to our local authority traded companies. Operational loans and investments will be assessed and approval sought from members on a case-by-case basis. This will include a full assessment of the risk, including credit risk and how this will be managed.

A new risk for 18/19 is the expected credit risk impairment resulting from changes to the code impacting financial instruments which fall under IFRS9. The Council currently invests in two pooled funds which are affected by this change, the Threadneedle Social Bond Fund and the CCLA Property Fund. These funds will be reviewed and accounted for as per the CIPFA code.

Creditworthiness Policy

7.8 The first principle governing the Council's investment criteria is the security of its investments. To mitigate security risk the Council will ensure that it:

- Maintains a policy covering both the categories and types of investment that can be invested in.
- Maintains criteria for choosing investment counterparties with adequate security.
- Maintains a process for the monitoring of their security.

7.9 The second principle is ensuring liquidity. The Council will ensure that 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 sum invested

7.10 The Assistant Director of Finance and ICT Strategy will maintain a counterparty list in compliance with the criteria and will revise and submit the criteria to Council for approval as necessary. These criteria are separate to that which determines which types of investment instrument are either specified or non-specified as it provides an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

7.11 Credit rating information is supplied by Link, our treasury consultants, on all counterparties that comply with the stated criteria. Any counterparty failing to meet the criteria will be deleted from the counterparty lending list. Any rating changes, watches (notification of a likely change), or outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing.

Country Limits

7.12 The Council has determined that it will only use approved counterparties from the UK and from countries with a minimum sovereign credit rating of AA from Fitch Ratings (or an equivalent rating from other agencies if Fitch does not provide). The list of countries that qualify using this credit criteria at the current time are shown in Appendix G. This list will be amended by officers as and when ratings change in accordance with this policy.

Investment Strategy

7.13 The Council has in-house managed funds that are mainly cash flow derived and a core balance available for investment mostly within periods of one year with some over one year period. Investments will be made with regard to the core balance, cash flow requirements and the outlook for short term interest rates.

7.14 For its cash flow generated balances, the Council will seek to utilise its balances in order to benefit from the compounding of interest.

End of Year Investment Report

7.15 At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Outturn Report.

External Fund Managers

7.16 The County Council uses a number of external managers to spread risk and obtain maximum market exposure. The fund managers will use both specified and non-specified investments and must comply with the terms set out in Appendix F. External fund managers actively used during the last year are listed below.

Fund Manager	Product/Fund Name
CCLA	Public Sector Deposit Fund Local Authority Property Fund
Standard Life	Short Duration Cash Fund
Aberdeen Asset Management	Ultra Short Duration fund
Federated Investors	Sterling Liquidity Fund
Columbia Threadneedle	UK Social Bond Fund
Aviva Investors	Sterling Core Liquidity Fund

Policy on the Use of External Service Providers

7.17 The Council uses Link as its external treasury management advisers. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed, documented and subject to regular review.

Role of the Section delegation
delegationcer

7.18 The detailed responsibilities of the Section 151 Officer in respect of Treasury Management are set out at Appendix H.

Pension Fund Cash

7.19 This Council will comply with the requirements of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009, implemented 1 January 2010. With effect 1 April 2010, the Council does not pool pension fund cash with its own cash balances for investment purposes. Any investments made by the pension fund directly with this local authority after 1 April 2010 must comply with the requirements of SI 2009 No 393.

8. Non Treasury Management Investments

8.1 This section covers investments made primarily made in order to earn income commercially or to deliver service objectives. Where the local authority holds investments in non-Treasury Management assets that are primarily for the purpose of achieving a financial return there is a new requirement under the revised code to report on these.

8.2 The Council does not have a policy of making investments primarily for the purpose of receiving a financial return.

8.3 The Council has no plans to borrow in 2019/20 purely to profit from the investment of the sums borrowed.

8.4 The Council does own shares and issue debt to some companies for service purposes, and holds some investment related property. Existing policies and controls will remain in place for the management of these.

8.4 New proposals for investment for non-Treasury Management purposes will be required to have direct Council approval or be approved through a delegated framework of controls that would be set out in an updated strategy statement.

8.5 The Section 151 Officer responsibilities (Appendix H) have been expanded to have regard to non-Treasury Management investments.

8.6 New investment proposals will be formally documented and assessed, including a financial appraisal, and an assessment of risk and risk management which must include consideration of credit risk. External expertise and advice will be sought where appropriate, and monitoring arrangements will include credit risk monitoring.

9 Minimum Revenue Provision

9.1 The Council’s policy on Minimum Revenue Provision (MRP) is shown in Appendix I.

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Appendices

A. Treasury Management Strategy Statement

B. Prudential and Treasury Indicators

C. Prudential Term Explanations

D. Capita Economic Commentary

E. Treasury Management Scheme of Delegation

F. Schedule of Specified and Non Specified Investments

G. Approved Countries for Investments

H. The Treasury Management Role of the S151 (Responsible) Officer

I. Minimum Revenue Provision

Appendix B

(1). AFFORDABILITY PRUDENTIAL INDICATORS	2017/18	2018/19	2019/20	2020/21	2021/22
	Actual	estimate	estimate	estimate	estimate
	£'000	£'000	£'000	£'000	£'000
Capital Expenditure	78,344	132,825	230,593	55,489	7,261
	%	%	%	%	%
Ratio of financing costs to net revenue stream	7.10	6.99	7.14	8.00	7.90
Gross borrowing requirement	£'000	£'000	£'000	£'000	£'000
Gross Debt	362,274	362,274	352,274	332,274	332,275
Capital Financing Requirement as at 31 March	313,947	336,652	441,402	424,933	408,127
Under/(Over) Borrowing	(48,327)	(25,622)	89,128	92,659	75,852
	£'000	£'000	£'000	£'000	£'000
In year Capital Financing Requirement	(2,746)	22,704	104,751	(16,470)	(16,806)
	£'000	£'000	£'000	£'000	£'000
Capital Financing Requirement as at 31 March	313,947	336,652	441,402	424,933	408,127

PRUDENTIAL INDICATOR (2). TREASURY MANAGEMENT PRUDENTIAL INDICATORS	2017/18	2018/19	2019/20	2020/21	2021/22
	Approved	estimate	estimate	estimate	estimate
Authorised limit for external debt -	£'000	£'000	£'000	£'000	£'000
Borrowing	549,049	516,818	587,675	579,911	535,744
other long term liabilities	12,000	12,000	12,000	12,000	12,000
TOTAL	**561,049**	**528,818**	**599,675**	**591,911**	**547,744**
Operational boundary for external debt -	£'000	£'000	£'000	£'000	£'000
Borrowing	457,540	430,681	489,729	483,259	446,453
other long term liabilities	10,000	10,000	10,000	10,000	10,000
TOTAL	**467,540**	**440,681**	**499,729**	**493,259**	**456,453**
Upper limit for fixed interest rate exposure					
Net principal re fixed rate borrowing / fixed term investments	100%	100%	100%	100%	100%
Upper limit for variable rate exposure					
Net principal re fixed rate borrowing / fixed term investments	25%	25%	25%	25%	25%
Upper limit for total principal sums invested for over 365 days	£	£	£	£	£
(per maturity date)	£0	£60,000	£60,000	£60,000	£60,000

Maturity structure of new fixed rate borrowing during year	upper limit	upper limit	lower limit
under 12 months	20%	20%	0%
12 months and within 24 months	20%	20%	0%
24 months and within 5 years	60%	60%	0%
5 years and within 10 years	100%	100%	0%
10 years and above	100%	100%	0%

Maturity structure of new variable rate borrowing during year	upper limit	upper limit	lower limit
under 12 months	20%	20%	0%
12 months and within 24 months	20%	20%	0%
24 months and within 5 years	60%	60%	0%
5 years and within 10 years	100%	100%	0%
10 years and above	100%	100%	0%

Appendix C

PRUDENTIAL INDICATORS

Ratio of financing costs to net revenue stream

The ratio of financing costs to net revenue stream shows the estimated annual revenue costs of borrowing, less net interest receivable on investments, plus repayments of capital, as a proportion of annual income from council taxpayers and central government. The estimates of financing costs include current and future commitments based on the capital programme.

Gross Borrowing

Gross borrowing refers to the Authority's total external borrowing and other long term liabilities versus the Capital Financing Requirement.

Actual and Estimated Capital Expenditure

Actual and estimates of capital expenditure for the current and future years.

Capital Financing Requirement

The Capital Financing Requirement (CFR) represents capital expenditure financed by external debt and not by capital receipts, revenue contributions, capital grants or third party contributions at the time of spending. The CFR measures the Authority's underlying need to borrow externally for a capital purpose. The Authority has a treasury management strategy which accords with the CIPFA Code of Practice for Treasury Management in the Public Services.

Authorised Limit

In respect of its external debt, the Authority approves authorised limits for its total external debt gross of investments. These limits separately identify borrowing from other long-term liabilities such as finance leases. Authorised Limits are consistent with the Authority's current commitments, service plans, proposals for capital expenditure and associated financing, cash flow and accord with the approved Treasury Management Policy statement and practices. The Authorised Limit is based on the estimate of most likely prudent, but not necessarily the worst case scenario and provides sufficient additional headroom over and above the Operational Boundary.

Operational Boundary

The Operational Boundary for external debt is based on the same estimates as the authorised limit but reflects the Head of Finance's estimate of the most likely, prudent but not worst case scenario, without the additional headroom included within the authorised limit to allow for unusual cash movements, and equates to the maximum of external debt projected by this estimate. The operational boundary represents a key management tool for in-year monitoring. Within the operational boundary, figures for borrowing and other long-term liabilities are separately identified.

Limits on Interest Rate Exposure

This means that the Authority will manage fixed and variable interest rate exposure within the ranges. This provides flexibility to take advantage of any favourable movements in interest rates.

Appendix D

Economic Commentary (LAS View)

Economic Background

GLOBAL OUTLOOK. World growth has been doing reasonably well, aided by strong growth in the US. However, US growth is likely to fall back in 2019 and, together with weakening economic activity in China, overall world growth is likely to weaken.

Inflation has been weak during 2018 but, at long last, unemployment falling to remarkably low levels in the US and UK has led to a marked acceleration of wage inflation. The US Fed has therefore increased rates nine times and the Bank of England twice. However, the ECB is now probably unlikely to make a start on raising rates in 2019.

KEY RISKS - central bank monetary policy measures

Looking back on nearly ten years since the financial crash of 2008 when liquidity suddenly dried up in financial markets, it can be assessed that central banks' monetary policy measures to counter the sharp world recession were successful. The key monetary policy measures they used were a combination of lowering central interest rates and flooding financial markets with liquidity, particularly through unconventional means such as quantitative easing (QE), where central banks bought large amounts of central government debt and smaller sums of other debt.

The key issue now is that that period of stimulating economic recovery and warding off the threat of deflation, is coming towards its close. A new period has already started in the US, and more recently in the UK, of reversing those measures i.e. by raising central rates and, (for the US), reducing central banks' holdings of government and other debt. These measures are now required in order to stop the trend of a reduction in spare capacity in the economy, and of unemployment falling to such low levels that the re-emergence of inflation is viewed as a major risk. It is, therefore, crucial that central banks get their timing right and do not cause shocks to market expectations that could destabilise financial markets. In particular, a key risk is that because QE-driven purchases of bonds drove up the price of government debt, and therefore caused a sharp drop in income yields, this also encouraged investors into a search for yield and into investing in riskier assets such as equities. Consequently, prices in both bond and equity markets rose to historically high valuation levels simultaneously. This now means that both asset categories are vulnerable to a sharp downward correction. It is important, therefore, that central banks only gradually unwind their holdings of bonds in order to prevent destabilising the financial markets. It is also likely that the timeframe for central banks unwinding their holdings of QE debt purchases will be over several years. They need to balance their timing to neither squash economic recovery, by taking too rapid and too strong action, or, conversely, let inflation run away by taking action that was too slow and/or too weak. **The potential for central banks to get this timing and strength of action wrong are now key risks.** It is particularly notable that, at its 30 January 2019 meeting, the Fed dropped its previous words around expecting further increases in interest rates; it merely said it would be "patient".

The world economy also needs to adjust to a sharp change in **liquidity creation** over the last five years where the US has moved from boosting liquidity by QE purchases, to reducing its holdings of debt. In addition, the European Central Bank has cut back its QE purchases substantially and is likely to end them completely by the end of 2018.

UK. 2018 was a year which started with weak growth of only 0.1% in quarter 1. However, quarter 2 rebounded to 0.4% in quarter 2 followed by quarter 3 being exceptionally strong at +0.6%. Quarter 4 though, was depressed by the cumulative weight of Brexit uncertainty and came in at only +0.2%. Growth is likely to continue being weak until the Brexit fog clears.

The MPC stated that future Bank Rate increases would be gradual and would rise to a much lower equilibrium rate, (where monetary policy is neither expansionary of contractionary), than before the crash; indeed they gave a figure for this of around 2.5% in ten years time but declined to give a medium term forecast. However, with so much uncertainty around Brexit, they warned that the next move could be up or down, even if there was a disorderly Brexit. While it would be expected that Bank Rate could be cut if there was a significant fall in GDP growth as a result of a disorderly Brexit, so as to provide a stimulus to growth, they warned they could also *raise* Bank Rate in the same scenario if there was a boost to inflation from a devaluation of sterling, increases in import prices and more expensive goods produced in the UK replacing cheaper goods previously imported, and so on. In addition, the Chancellor has held back some spare capacity to provide a further fiscal stimulus if needed.

Inflation. The Consumer Price Index (CPI) measure of inflation has been falling from a peak of 3.1% in November 2017 to 2.1% in December 2018. In the February Bank of England quarterly Inflation Report, inflation was forecast to still be marginally above its 2% inflation target two years ahead given a scenario of minimal increases in Bank Rate.
As for the **labour market** figures in November were particularly strong with an emphatic increase in total employment of 141,000 over the previous three months, unemployment at 4.0%, a 43 year low of 4% on the Independent Labour Organisation measure, and job vacancies hitting an all-time high, indicating that employers are having major difficulties filling job vacancies with suitable staff It was therefore unsurprising that wage inflation picked up to 3.3%, (3 month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates less CPI inflation), earnings are currently growing by about 128%, the highest level since 2009. This increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. This tends to confirm that the MPC was right to start on a cautious increase in Bank Rate in August as it views wage inflation in excess of 3% as increasing inflationary pressures within the UK economy.

In the **political arena**, the Brexit deal put forward by the Conservative minority government was defeated on 15 January. Prime Minister May is currently, (mid-February), seeking some form of modification or clarification from the EU of the Irish border backstop issue. However, our central position is that the Government will endure, despite various setbacks, along the route to reaching an orderly Brexit though the risks are increasing that it may not be possible to get full agreement by the UK and EU before 29 March 2019, in which case this withdrawal date is likely to be pushed back to a new date. If, however, the UK faces a general election in the next 12 months, this could result in a potential loosening of monetary and fiscal policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up.

USA. President Trump's massive easing of fiscal policy is fuelling a, (temporary), boost in consumption which has generated an upturn in the rate of strong growth which rose from 2.2%, (annualised rate), in quarter 1 to 4.2% in quarter 2 and 3.5%, (3.0% y/y), in quarter 3, but also an upturn in inflationary pressures. In particular, wage rates were increasing at 3.1% y/y in October and heading higher due to unemployment falling to a 49 year low of 3.7%. With CPI inflation over the target rate of 2% and on a rising trend towards 3%, the Fed increased rates another 0.25% in September to between 2.00% and 2.25%, this being the fourth increase in 2018. They also indicated that they expected to increase rates four more times by the end of 2019. The dilemma, however, is what to do when the temporary boost to consumption wanes, particularly as the recent imposition of tariffs on a number of countries' exports to the US, (China in particular), could see a switch to US production of some of those goods, but at higher prices. Such a scenario would invariably make any easing of monetary policy harder for the Fed in the second half of 2019. However, a combination of an expected four increases in rates of 0.25% by the end of 2019, together with a waning of the boost to economic growth from the fiscal stimulus in 2018, could combine to depress growth below its potential rate, i.e. monetary policy may prove to be too aggressive and lead to the Fed having to start on cutting rates. The Fed has also been unwinding its previous quantitative easing purchases of debt by gradually increasing the amount of monthly maturing debt that it has not been reinvesting.

The tariff war between the US and China has been generating a lot of heat during 2018, but it is not expected that the current level of actual action would have much in the way of a significant effect on US or world growth. However, there is a risk of escalation. The results of the mid-term elections are not expected to have a material effect on the economy.

Eurozone. Growth was 0.4% in quarters 1 and 2 but fell back to 0.2% in quarter 3, though this is probably just a temporary dip. In particular, data from Germany has been mixed and it could be negatively impacted by US tariffs on a significant part of manufacturing exports e.g. cars. For that reason, although growth is still expected to be in the region of nearly 2% for 2018, the horizon is less clear than it seemed just a short while ago. Having halved its quantitative easing purchases of debt in October 2018 to €15bn per month, the European Central Bank has indicated it is likely to end all further purchases in December 2018. Inflationary pressures are starting to build gently so it is expected that the ECB will start to increase rates towards the end of 2019.

China. Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems. Progress has been made in reducing the rate of credit creation, particularly from the shadow banking sector, which is feeding through into lower economic growth. There are concerns that official economic statistics are inflating the published rate of growth.

Japan - has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy. It is likely that loose monetary policy will endure for some years yet to try to stimulate growth and modest inflation.

Emerging countries. Argentina and Turkey are currently experiencing major headwinds and are facing challenges in external financing requirements well in excess of their reserves of foreign exchange. However, these countries are small in terms of the overall world economy, (around 1% each), so the fallout from the expected recessions in these countries will be minimal.

INTEREST RATE FORECASTS

The interest rate forecasts provided by our treasury management advisers, Link Asset Services are **predicated on an assumption of an agreement being reached on Brexit between the UK and the EU.** On this basis, while GDP growth is likely to be subdued in 2019 due to all the uncertainties around Brexit depressing consumer and business confidence, an agreement is likely to lead to a boost to the rate of growth in 2020 which could, in turn, increase inflationary pressures in the economy and so cause the Bank of England to resume a series of gentle increases in Bank Rate. Just how fast, and how far, those increases will occur and rise to, will be data dependent. The forecasts in this report assume a modest recovery in the rate and timing of stronger growth and in the corresponding response by the Bank in raising rates.

- In the event of an **orderly non-agreement exit**, it is likely that the Bank of England would take action to cut Bank Rate from 0.75% in order to help economic growth deal with the adverse effects of this situation. This is also likely to cause short to medium term gilt yields to fall.
- If there was a **disorderly Brexit**, then any cut in Bank Rate would be likely to last for a longer period and also depress short and medium gilt yields correspondingly. It is also possible that the government could act to protect economic growth by implementing fiscal stimulus.

However, there would appear to be a majority consensus in the Commons against any form of non-agreement exit so the chance of this occurring has now substantially diminished.

The balance of risks to the UK

- The overall balance of risks to economic growth in the UK is probably neutral.
- The balance of risks to increases in Bank Rate and shorter term PWLB rates, are probably also even and are broadly dependent on how strong GDP growth turns out, how slowly inflation pressures subside, and how quickly the Brexit negotiations move forward positively.

One risk that is both an upside and downside risk, is that all central banks are now working in very different economic conditions than before the 2008 financial crash as there has been a major increase in consumer and other debt due to the exceptionally low levels of borrowing rates that have prevailed for ten years since 2008. This means that the neutral rate of interest in an economy, (i.e. the rate that is neither expansionary nor deflationary), is difficult to determine definitively in this new environment, although central banks have made statements that they expect it to be much lower than before 2008. Central banks could therefore either over or under do increases in central interest rates.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- **Brexit** – if it were to cause significant economic disruption and a major downturn in the rate of growth.
- **Bank of England monetary policy** takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- A resurgence of the **eurozone sovereign debt crisis**, possibly in **Italy**, due to its high level of government debt, low rate of economic growth and vulnerable banking system, and due to the election in March of a government which has made a lot of anti-austerity noise. The EU rejected the initial proposed Italian budget and demanded cuts in government spending which the Italian government initially refused. However, a fudge was subsequently agreed, but only by *delaying* the planned increases in expenditure to a later year. This can has therefore only been kicked down the road to a later time. The rating agencies have started on downgrading Italian debt to one notch above junk level. If Italian debt were to fall below investment grade, many investors would be unable to hold it. Unsurprisingly, investors are becoming increasingly concerned by the words and actions of the Italian government and consequently, Italian bond yields have risen – at a time when the government faces having to refinance large amounts of debt maturing in 2019.
- Weak capitalisation of some **European banks**. Italian banks are particularly vulnerable; one factor is that they hold a high level of Italian government debt - debt which is falling in value. This is therefore undermining their capital ratios and raises the question of whether they will need to raise fresh capital to plug the gap.
- **German minority government.** In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. Then in October 2018, the results of the Bavarian and Hesse state elections radically undermined the SPD party and showed a sharp fall in support for the CDU. As a result, the SPD is reviewing whether it can continue to support a coalition that is so damaging to its electoral popularity. After the result of the Hesse state election, Angela Merkel announced that she would not stand for re-election as CDU party leader at her party's convention in December 2018, (a new party leader has now been elected). However, this makes little practical difference as she is still expected to aim to continue for now as the Chancellor. However, there are five more state elections coming up in 2019 and EU parliamentary elections in May/June; these could result in a further loss of electoral support for both the CDU and SPD which could also undermine her leadership.
- **Other minority eurozone governments.** Spain, Portugal, Ireland, the Netherlands and Belgium all have vulnerable minority governments dependent on coalitions which could prove fragile. Sweden is also struggling to form a government due to the anti-immigration party holding the balance of power, and which no other party is willing to form a coalition with. The Belgian coalition collapsed in December 2018 but a minority caretaker government has been appointed until the May EU wide general elections.
- **Austria, the Czech Republic and Hungary** now form a strongly anti-immigration bloc within the EU while **Italy,** in 2018, also elected a strongly anti-immigration government. Elections to the EU parliament are due in May/June 2019.
- Further increases in interest rates in the US could spark a **sudden flight of investment funds** from more risky assets e.g. shares, into bonds yielding a much improved yield. Throughout the last quarter of 2018, we saw sharp falls in equity markets interspersed with occasional partial rallies. Emerging countries which have borrowed heavily in dollar denominated debt, could be particularly exposed to this risk of an investor flight to safe havens e.g. UK gilts.

- There are concerns around the level of **US corporate debt** which has swollen massively during the period of low borrowing rates in order to finance mergers and acquisitions. This has resulted in the debt of many large corporations being downgraded to a BBB credit rating, close to junk status. Indeed, 48% of total investment grade corporate debt is now rated at BBB. If such corporations fail to generate profits and cash flow to reduce their debt levels as expected, this could tip their debt into junk ratings which will increase their cost of financing and further negatively impact profits and cash flow.
- **Geopolitical risks,** especially North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.

Upside risks to current forecasts for UK gilt yields and PWLB rates

- **Brexit –** if both sides were to agree by 29 March a compromise that quickly removed all threats of economic and political disruption and so led to an early boost to UK economic growth.
- **The Fed causing a sudden shock in financial markets** through misjudging the pace and strength of increases in its Fed Funds Rate and in the pace and strength of reversal of QE, which then leads to a fundamental reassessment by investors of the relative risks of holding bonds, as opposed to equities. This could lead to a major flight from bonds to equities and a sharp increase in bond yields in the US, which could then spill over into impacting bond yields around the world.
- The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflation pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.
- **UK inflation,** whether domestically generated or imported, returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

APPENDIX E

Treasury Management Scheme of Delegation

(i) County Council

- approval of annual strategy.
- budget consideration and approval.
- approval of the division of responsibilities.

(ii) Cabinet

- scrutinise the proposed annual strategy.
- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices.

(iii) Resources and Fire & Rescue Overview and Scrutiny Committee

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.
- receiving and reviewing regular monitoring reports and acting on recommendations.

Appendix F

Specified Investments

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

	Minimum ‘High’ Credit Criteria	**Use**
DMO Deposit Facility	--	In-house
Term deposits: Local Authorities	--	In-house
Nationalised Banks	Short-term F1, Support 1	In-house and External Manager
Term deposits: UK Banks	Short-term F1, Long-term A, Viability a, Support 3	In-house and External Manager
Term deposits: Bank Council uses for current account	--	In-house and External Manager
Term deposits: UK Building Societies	Top five largest societies as reported semi-annually. (To be continually monitored)	In-house and External Manager
Term deposits: Overseas Banks	Short-term F1+, Long-term AA, Viability aa, Support 1	In-house and External Manager
Certificates of deposits issued by UK banks and building societies	Short-term F1, Long-term A, Viability a, Support 3	External Manager
Money Market Funds	AA	In-house and External Manager
UK Government Gilts, Treasury Bills	--	External Manager
Gilt Funds and Bond Funds	Long-term A	External Manager

Non-Specified Investments

	Minimum Credit Criteria	**Use**
Term deposits: UK banks and building societies with maturities in excess of one year with a maximum of three years allowed for in-house deposits	Short-term F1, Long-term A, Viability a, Support 3	In-house and External Manager
Fixed Term Deposit with Variable Rates and Variable Maturities	Short-term F1, Long-term A, Viability a+, Support 3	In-house and External Manager
Certificates of Deposits issued by UK banks and building societies	Short-term F1, Long-term A, Viability a, Support 3	External Manager
UK Government Gilts with maturities in excess of 1 year	--	External Manager
Local Authority Mortgage Scheme	As per scheme conditions	In-house
Investment in the Local Government Association Mutual Bond Agency, the local Government Money Market and Property investment vehicles managed on behalf of the Local Government Association by CCLA.	--	--
Local Authority wholly owned trading company	--	In-house

* 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.

Appendix G

Approved Countries for Investments

AAA

- Australia
- Canada
- Denmark
- Germany
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)
- France
- Hong Kong
- U.K.

Appendix H

The Treasury Management Role of the S151 (Responsible) Officer: Strategic Director - Resources

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers
- entering into repurchase transactions where appropriate

Additional responsibilities in respect of non-financial investments:

- ensuring that due diligence is carried out on treasury and non-financial investments in accordance with the risk appetite of the authority.
- ensuring the proportionality of investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources.
- ensuring an adequate governance process is in place for the approval, monitoring, and ongoing risk management of non-financial investments and long term liabilities.
- Ensuring adequate treasury management practices are in place for non-financial investments

Appendix I

MINIMUM REVENUE PROVISION

1. What is a Minimum Revenue Provision?

Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, machinery etc. It would be impractical to charge the entirety of such expenditure to revenue in the year in which it was incurred and so such expenditure is spread over several years so as to try to match the years over which such assets benefit the local community through their useful life. The manner of spreading these costs is through an annual Minimum Revenue Provision (MRP).

2. Statutory Duty

Statutory Instrument 2008 no. 414 s4 lays down that:

"A local authority shall determine for the current financial year an amount of minimum revenue provision that it considers to be prudent."

There is no requirement to charge MRP where the Capital Financing Requirement is nil or negative at the end of the preceding financial year.

3. Government Guidance

Along with the above duty, the Government issued guidance in February 2008 which requires that a Statement on the Council's policy for its annual MRP should be submitted to the full Council for approval before the start of the financial year to which the provision will relate.

The Council is legally obliged to "have regard" to the guidance, which is intended to enable a more flexible approach to assessing the amount of annual provision than was required under the previous statutory requirements. The guidance offers four main options under which MRP could be made with an overriding recommendation that the Council should make prudent provision to redeem its debt liability over a period which is reasonably commensurate with that over which the capital expenditure is estimated to provide benefits. The requirement to "have regard" to the guidance therefore means that:

a. Although four main options are recommended in the guidance, there is no intention to be prescriptive by making these the only methods of charge under which a local authority may consider its MRP to be prudent.

b. It is the responsibility of each authority to decide upon the most appropriate method of making a prudent provision, after having had regard to the guidance.

4. Warwickshire County Council Policy

We have decided not to use any of the options outlined in the statutory guidance but to adopt an alternative approach, which we believe is prudent.

The MRP provision will be calculated on the average remaining useful life of the Council's asset portfolio. We will calculate and apply the remaining useful life over two categories of asset:

- Land, buildings and infrastructure;
- Vehicles, plant and equipment.

The proportion of debt outstanding in each category of asset will be determined by the value of assets included in the balance sheet at the end of each financial year.

The 2017 review shows that the remaining useful life of our assets is now 28 years. By using an average life of 28 years for our assets equates to an annual provision of 4% straight line MRP.

For vehicles, plant and equipment, the remaining useful life is assumed to be five years e.g. 5 years average remaining useful life will result in 20% straight line MRP.