# Cabinet

# 17 June 2021

# Treasury Management Strategy and Investment Strategy

## Recommendations

That Cabinet recommends to Council that:

1. The Treasury Management Strategy for 2021/22 (Appendix 1) be approved with immediate effect.

2. The Investment Strategy for 2021/22 (Appendix 2) be approved with immediate effect.

3. That the County Council requires the Strategic Director for Resources to ensure that gross borrowing does not exceed the prudential level specified (Appendix 1,Section 3.2, Table 10 “Authorised Borrowing Limit”).

4. That the County Council requires the Strategic Director for Resources to ensure that gross investment in non-Treasury investments does not exceed the prudential levels specified (Appendix 2, Annex 7).

5. That the County Council delegate authority to the Strategic Director for Resources to undertake delegated responsibilities in respect of both strategies (Appendix 1, Annex 7, and Appendix 2, Section 2.5).

6. That the County Council requires the Strategic Director for Resources to implement the Minimum Revenue Provision (MRP) Policy (Appendix 1, Section 2.4).

## 1 Executive Summary

1.1 The Council operates firm controls around making and financing investments due to the risks involved. The Council operates a Treasury Management Strategy to govern treasury investments and an Investment Strategy to cover Non-Treasury investments, and both of these policies must be approved by Council.

1.2 The Council has developed a proposal to implement a Warwickshire Recovery Investment Fund (WRIF), which is designed to provide finance to support business start-ups and business growth within Warwickshire and to support the Council's strategic goals and priorities as set out in the Warwickshire Council Plan 2025, Covid 19 Recovery Plan, Economic Strategy, Commercial Strategy, and Play Shaping Programme.

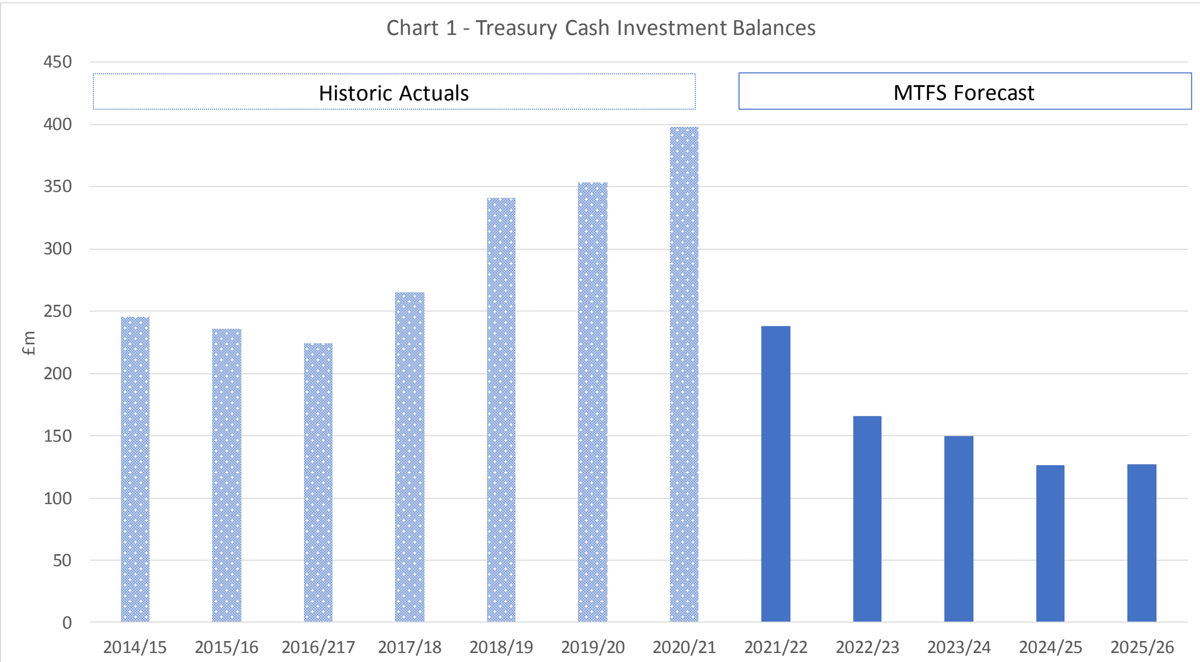
1.3 The details of the WRIF are set out within a report elsewhere on the agenda.

1.4 This report presents an updated Treasury Management Strategy and Investment Strategy with the primary purpose of enabling the creation of the WRIF and ensuring appropriate overarching controls are in place to manage risk.

1.5 In addition, the opportunity is being taken to make some other minor updates to these policies. The policy documents are presented at Appendix 1 and Appendix 2 and each policy covers holistically all investment activity, including and incorporating the proposals for the WRIF. This covering report however focuses on explaining the changes to the policies.

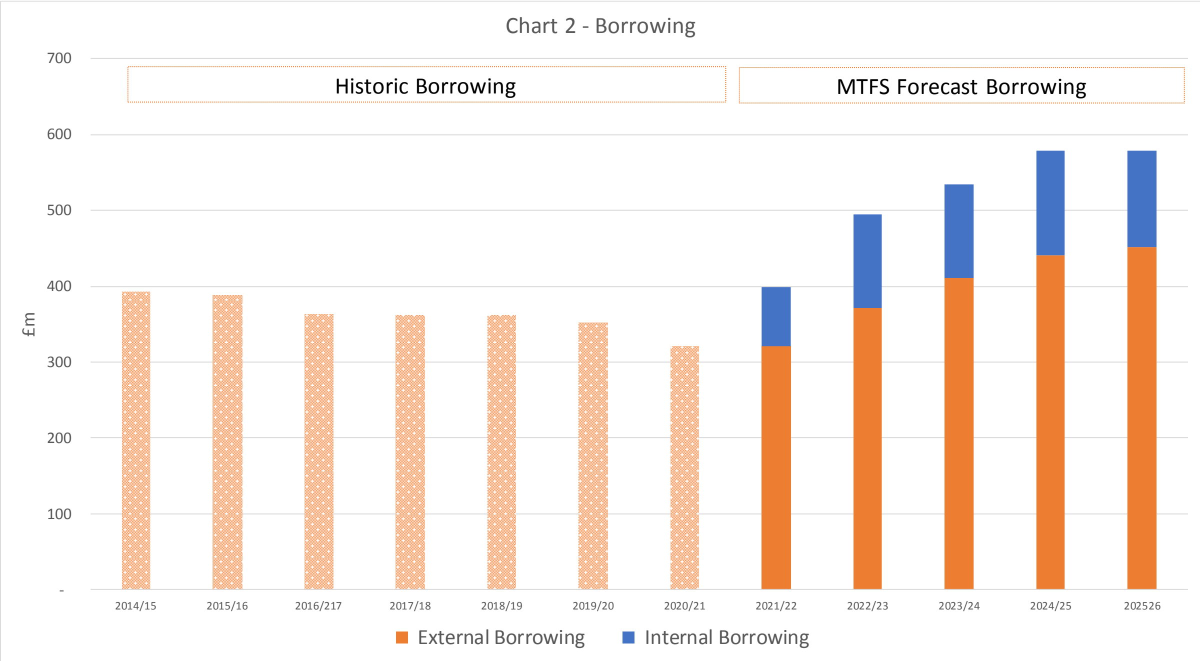
**Cash Balances**

1.6 This update to the strategy introduces a formal minimum cash balance of £125m. Previously there was no formal minimum but for comparison the low point of previous forecast cash balances was £150m. £125m would be a more efficient floor and would still facilitate adequate cash balances to manage operations and manage risk:



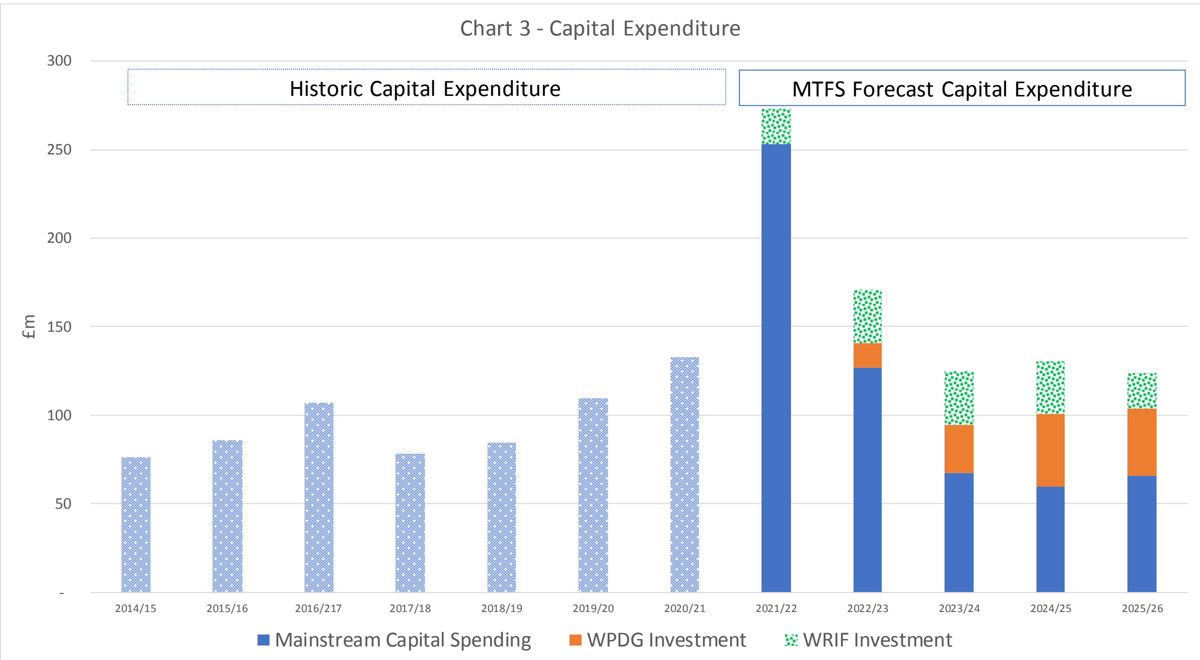

**Internal Borrowing**

2.1 "Internal borrowing" (also called "under borrowing") whereby the Council makes use of cash balances where they are available in order to reduce the amount of external borrowing required to support new investment because internal borrowing is cheaper (Appendix 1, Table 7) will increase due to the WRIF, as will overall borrowing. Chart 2 summarises the borrowing forecast and shows how a part of that increase will be through internal borrowing.




### Total Borrowing

2.2 Total borrowing, also referred to as the Capital Financing Requirement or CFR (Appendix 1 Table 4) is forecast to increase as a result of the addition of the WRIF, as illustrated below.



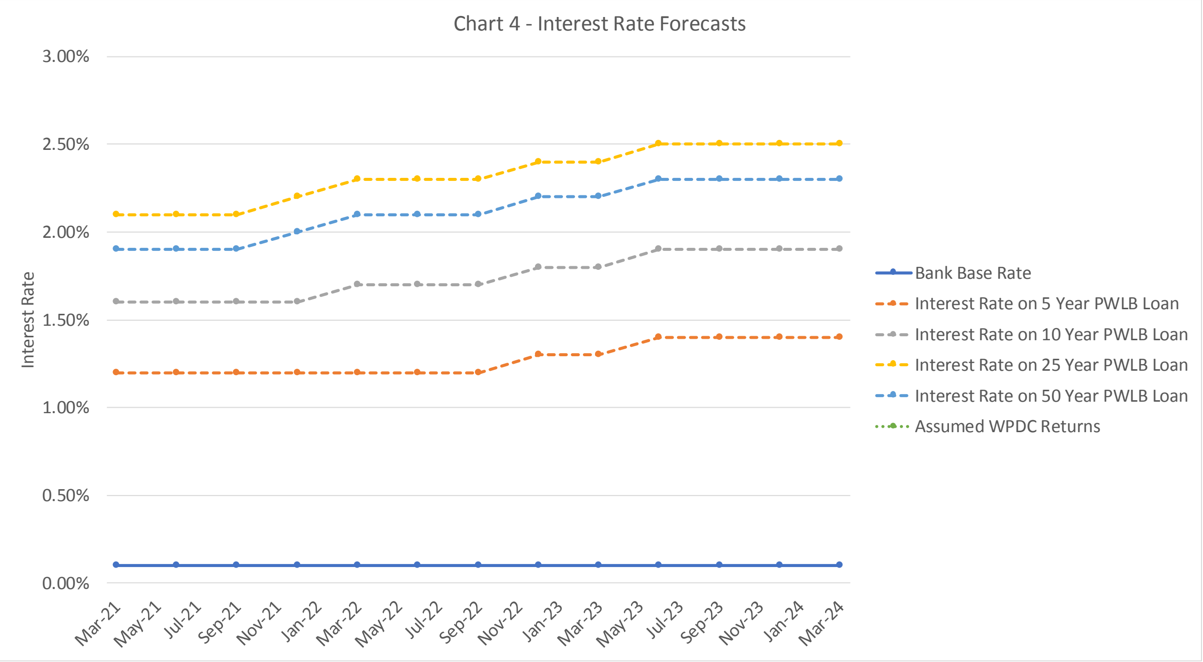
Note: WPDG – Warwickshire Property Development Group

**Minimum Revenue Provision**

2.3 The Council sets aside a minimum amount of revenue resources each year in order to be able to repay debt, called the Minimum Revenue Provision or MRP. The MRP policy will continue to reflect assumed underlying asset life, equating overall to 25 years , which equates to setting aside 4% per year. The MRP policy is set out at Appendix 1 Section 2.4.

**Interest Rates**

2.4 Interest rates have risen slightly but continue to be low and the outlook remains low with the bank rate forecast to stay at 0.1% for the next few years. The rates at which local authorities can borrow from the Public Works Loan Board (PWLB) are also low, in the range 0.2% to 2.5% for durations from 5 years to 50 years and are only expected to rise slowly over the medium term (Appendix 1, Section 3.3). The latest forecasts are set out in the chart below.




2.5 WRIF investments will provide returns in the range 5% to 15% commensurate with risk, therefore the Council will earn a net positive return on WRIF investments because it is possible to finance the investments at a lower cost than the financial return, However higher returns are associated with higher risk.

**Borrowing**

2.6 A key issue will be to ensure that the Council maintains access to PWLB rates (although alternatives will also be considered when borrowing is required to ensure best value is achieved). The WRIF Investment Strategy sets out the objectives of the Fund and these align with PWLB criteria. This means PWLB financing will be an option for WRIF investment.

2.7 Limits for borrowing have been updated based upon expected levels of WRIF investment, including an “Authorised Borrowing Limit” which cannot be exceeded (Appendix 1 Table 10).

**Treasury Investments**

2.8 The facility to make loans to other local authorities has been updated to enable loans of up to 18 months rather than 12 months (Appendix 1 Section 4.3). This will enable a higher volume of opportunities and therefore improve the opportunities to secure better deals and get the best value for money when lending.

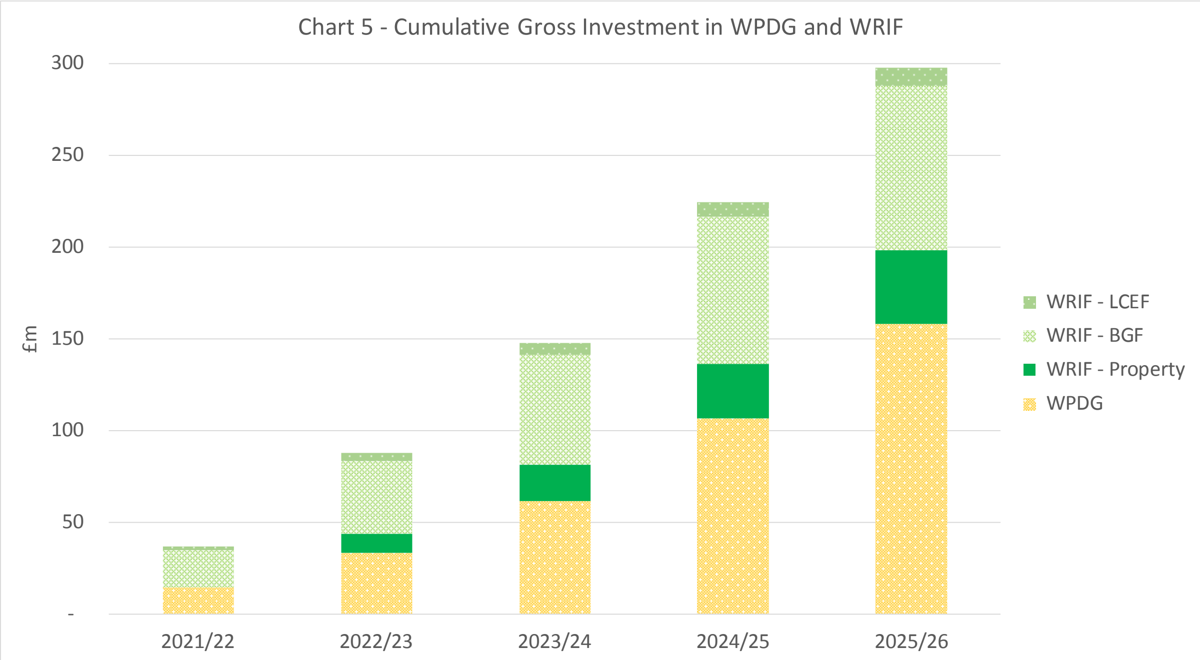
2.9 The limits for loans to local authority controlled companies have been increased to provide some headroom and avoid the need for Council approval should there be small changes in the need to lend (Appendix 1 Annex C4.2).

2.10 The limits on the maturity structure of any debt taken out have been updated to provide more flexibility (Appendix 1, Annex 1). This change allows the flexibility for a greater proportion of debt to be taken out over shorter timescales if this is appropriate.

## 3 Investment Strategy (Non-Treasury Investments - Appendix 2) – Headlines

**New Investments**

3.1 The Warwickshire Property Development Group (WPDG) business plan commits to £160m of investment and the WRIF adds a further £140m of non-treasury investment by 2025/26.




Note BGF – Business Growth Fund, LCEF – Local Communities Enterprise Fund

**Risk**

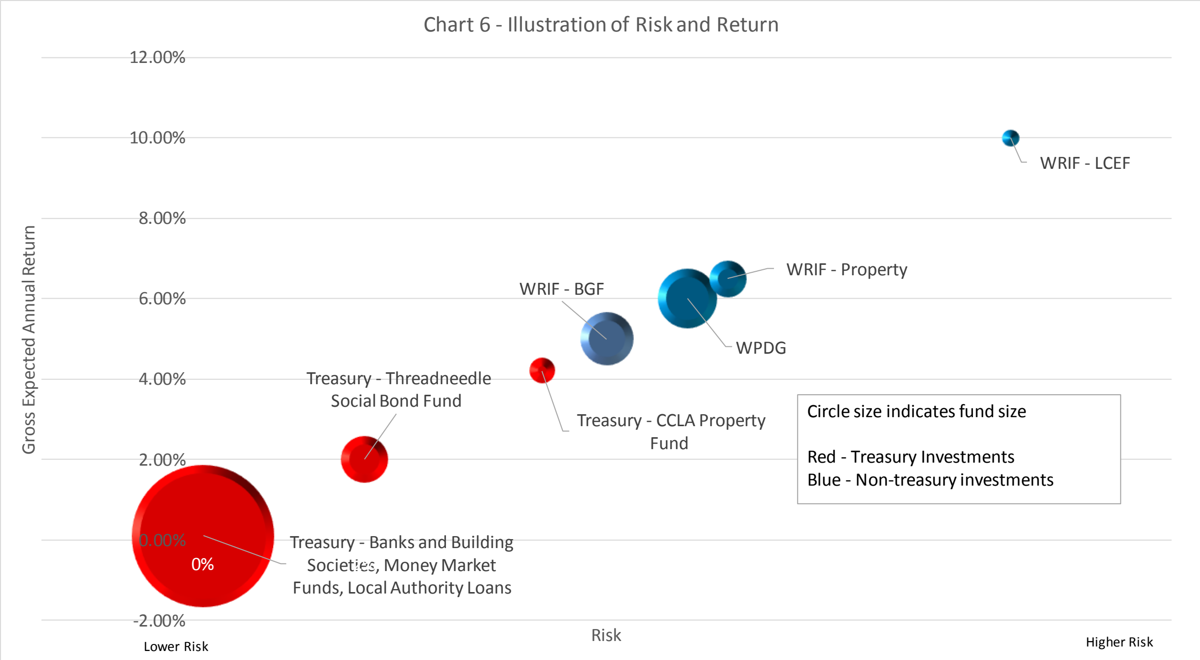
3.2 Any investment involves risk, with the risks depending upon the nature of the investment. A range of strategic governance and risk management standards are set out throughout the Investment Strategy which all non-treasury investments must adhere to (but refer to Appendix 2 Annex 2 – Annex 4 in particular). In addition, more detailed requirements may be determined for specific funds and incorporated into the approval of those funds.

3.3 Investment risk and return are directly linked, with higher risks typically being rewarded by higher returns. How financial risk actually manifests itself varies with the type of investment, for example equity risk manifests in the form of share price volatility, and lending risk manifests in the form of loan repayment default.

3.4 The WRIF is being set up with 3 sub-funds that have different risk profiles and the expected returns vary in accordance with risk (higher risks equating to higher returns). The WRIF as a whole is higher risk than traditional treasury management investments and some aspects of the WRIF are higher risk than others. The sub funds are:

- Property Fund –lower risk due to the likelihood of relating to larger and more established businesses and investment in an asset (property) that can provide some collateral.
- Business Growth Fund –lower risk as this will be larger loans to larger more established businesses.
- Local Communities Enterprise Fund – higher risk as this will relate to smaller organisations and start-ups with less likelihood of security.

3.5 The chart below illustrates schematically the spectrum of risk (by simply showing risk as being in direct proportion to return) and this shows how non-treasury investments are higher risk.

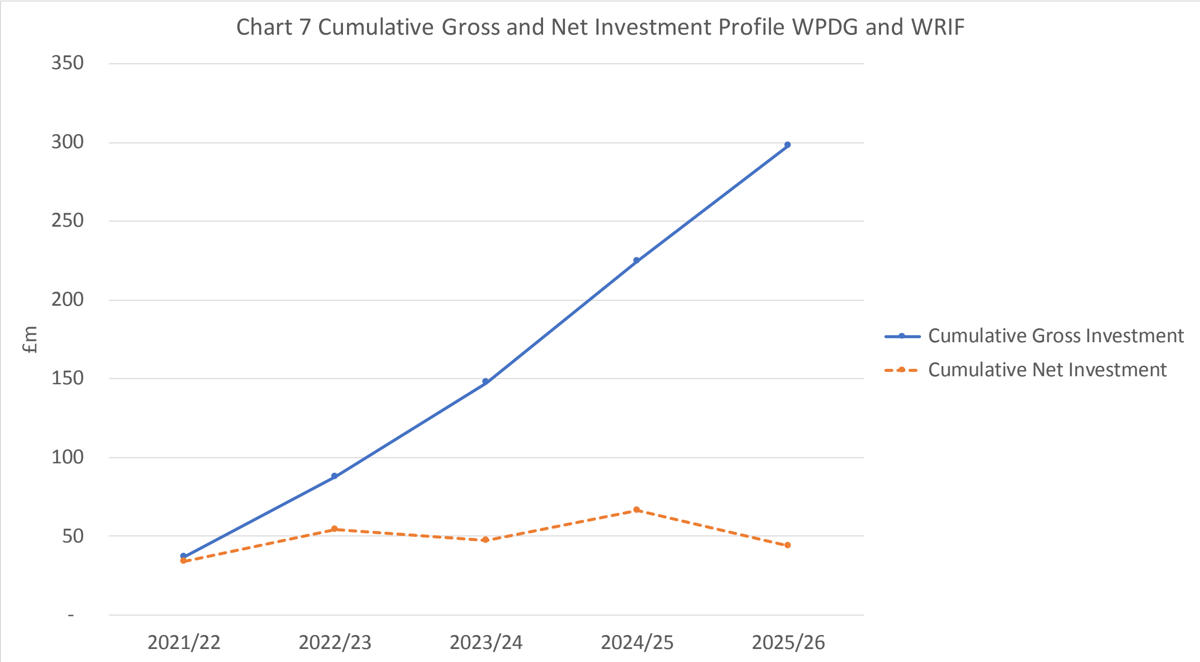



3.6 A key feature of managing risk will include having arrangements to manage the risk of losses (where investments are not repaid). The WRIF business plan and investment strategy have regard to risk management and this includes minimising losses but also expecting a certain degree of losses (no investment is 100% guaranteed to pay back).

3.7 Aside from the risks associated with any particular individual investments, another type of risk is addressed by the Investment Strategy called "proportionality" (Appendix 2 Section 9). This is to do with the overall aggregate level of investment and exposure to loss, in particular in comparison to the size and financial capacity of a local authority to bear the losses that it is exposed to. The issue of proportionality will be monitored and proportionality measures may be used in the future to put limits on investment activity. The introduction of the WRIF increases the exposure to proportionality risk but in return it provides the opportunity to meet certain service objectives.

**Prudential Indicators**

3.8 The Investment Strategy has been updated to have regard to the proposed WRIF investments, including the introduction of Prudential Indicators (Appendix 2 Annex 7) that place limits on gross and net investment:




3.9 This shows how anticipated repayment of investments over time means the net exposure to risk is kept lower than the gross investment figures. The gross amount that may be invested in each fund annually is a hard ceiling as set out in Appendix 2 Annex 7. The net level of investment will be monitored (i.e. after accounting for repayment of previous investments). If the annual net position is breached due to repayment defaults, this would trigger a review of future gross investment limits.

3.10 In addition, the following more detailed limits will be applied to manage WRIF investment risk (Appendix 2 Annex 7).

- The amount that can be invested in each sub-fund.
- The length of time that investments may be made for.
- The amount of a fund that may be equity in nature.
- The maximum investment that may be made in a single counter party.

3.11 The “Authorised Borrowing Limit” set within the Treasury Management Strategy (Appendix 1, Table 10) includes borrowing required to service WRIF investments.

**Governance**

3.12 The WRIF Business Plan and Investment Strategy set out detailed governance arrangements, and these arrangements are designed to meet the requirements of the overarching Council Investment Strategy.

## 4 Financial Implications

4.1 The financial implications are detailed within the report and appendices.

## 5 Environmental Implications

5.1 Both strategies include an "Environmental Social and Governance" (ESG) policy. The primary objectives of treasury management will however remain security, liquidity, and yield, with non-treasury investments also including the delivery of organisational service objectives.

## 6 Supporting Information

6.1 None.

## 7 Timescales Associated with Next Steps

7.1 The Treasury Management Strategy and Investment Strategy will be reported to Council in July for approval.

## Appendices

- Appendix 1 - Treasury Management Strategy
- Appendix 2 - Investment Strategy (for Non Treasury Investments)

## Background Papers

None

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The report was not circulated to members prior to publication