Appendix 2

Treasury Management Strategy Statement

Warwickshire County Council
2023/24

1.0 Introduction

Background

1.1 The Chartered Institute of Public Finance and Accountancy (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."

1.2 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 and managed 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 cash liquidity and 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.

Treasury Management reporting

1.5 The Council is currently required to receive and approve, as a minimum, three main Treasury reports each year, which incorporate a variety of policies, estimates and actuals:

a.) **Prudential and Treasury indicators and Treasury strategy** (this report) - The first, and most important report is forward looking and covers:
- the capital plans, (including prudential indicators);
- a minimum revenue provision (MRP) policy, (how residual capital expenditure is charged to revenue over time);
- the Treasury Management strategy, (how the investments and borrowings are to be organised), including Treasury indicators; and
- an investment strategy, (the parameters on how investments are to be managed).

b.) **A mid-year Treasury Management report** – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

c.) **An annual Treasury report** – This is a backward-looking review document and provides details of a selection of actual prudential and Treasury indicators and actual Treasury operations compared to the estimates within the strategy.

d.) **Scrutiny -** The above reports are scrutinised by the Resources and Fire and Rescue Overview and Scrutiny Committee.

e.) **Quarterly reports** – In addition to the three major reports detailed above, from 2023/24 quarterly reporting is also required. However, these additional reports do not have to be reported to full Council/Cabinet but do need to be adequately scrutinised. This role is undertaken by the Resources and Fire and Rescue Overview and Scrutiny Committee.

Capital Strategy and Investment Strategy

1.6 The Treasury Management Strategy Statement (TMSS) interacts with both the Capital Strategy and the Investment Strategy.

1.6.1 **Capital Strategy -** The CIPFA 2021 Prudential and Treasury Management Codes require all local authorities to prepare a Capital 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

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

1.6.2 **Investment Strategy -** The Council is required to set out separately an Investment Strategy (IS) in relation to non-Treasury investments. Non-Treasury investments must consider security, liquidity, and yield, however the relative priority of these three factors does not have to follow Treasury Management principles as non-Treasury investments are, by their nature, not intended to deliver Treasury Management objectives. The Council's Investment Strategy is a separate document; however, it does interrelate with the Treasury Management Strategy and Capital Strategy.

1.7 The table below summarises these different strategies.

Capital Strategy	Treasury Management Strategy – including Treasury Investment Strategy	Investment Strategy
Traditional capital expenditure to directly meet service objectives.	Management of cash and debt to service the delivery of day-to-day operations and the long-term financing of investments.	Non-Treasury investments with the primary objective of meeting service objectives.

Treasury Management Strategy for 2023/24

1.8 The strategy for 2023/24 covers two main areas:

a.) Capital considerations -
- Capital expenditure plans and the associated prudential indicators; and
- Minimum revenue provision (MRP) policy.

b.) Treasury Management considerations -
- The current Treasury position;
- Treasury indicators which limit the Treasury risk and activities of the Council;
- Prospects for interest rates;
- Borrowing Strategy;
- Policy on borrowing in advance of need;
- Debt rescheduling;
- Investment Strategy;
- Creditworthiness policy;
- The policy on use of external service providers; and
- The Councils Income Management Policy.

1.9 These elements cover the requirements of the Local Government Act 2003, DLUHC Investment Guidance, DLUHC MRP Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code.

1.10 The Treasury Management scheme of delegation, and responsibilities of the Section 151 officer are set out in Annex 6 and 7 respectively.

Training

1.11 The CIPFA Treasury Management Code requires the responsible officer to ensure that members with responsibility for Treasury Management receive adequate training in Treasury Management. This especially applies to members responsible for scrutiny.

The following is carried out to monitor and review knowledge and skills:

- Planned and recorded attendance at training and events.
- Tailored learning plans for Treasury Management officers and board/Council members.
- Treasury Management officers and board/Council members undertake a self-assessment against the required competencies.
- Regular communication with officers and board/Council members to highlight training needs on an ongoing basis.

A formal record of the training received by officers central to the treasury function will be maintained by the treasury team. Similarly, a formal record of the Treasury Management/capital finance training received by members will also be maintained by the Treasury Manager. Both records will be included in Treasury Management Outturn reports at the end of the financial year

Treasury Management Consultants

1.11 The Council currently contracts Link Group, Treasury Solutions as its external Treasury Management advisers.

1.12 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 the services of our external service providers. All decisions will be undertaken with regard to all available information, including, but not solely, our Treasury advisers.

1.13 It also recognises that there is value in employing external providers of Treasury Management services in order to acquire access to specialist skills and resources as and when required. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly contracted, agreed and documented and subjected to regular review.

1.14 In respect of non-Treasury investments, two advisers are used for access to specialist skills and resources. These are detailed in the Investment Strategy and the contracts remain separate to the above treasury adviser contract at all times.

2.0 The Capital Prudential Indicators 2023/24 – 2025/26

2.1 The Council's capital expenditure plans are the key driver of Treasury Management activity. The outputs of the capital expenditure plans are reflected in the prudential indicators (Annex 1), which are designed to assist members to review and confirm capital expenditure plans.

Prudential Indicator - ***Capital Expenditure and Financing***

2.2 This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts:

Table 1 – Total Capital Programme

£000's	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
Capital Expenditure	115,343.67	277,242.12	181,276.51	82,427.25	63,135.61	57,329.40
Non-Treasury Investment WPDG*	-	19,101.40	21,762.84	7,610.72	242.41	16,334.00
Non-Treasury Investment WRIF*	2,500.00	20,600.00	20,000.00	20,000.00	26,500.00	-
Total	**117,843.67**	**316,943.52**	**223,039.36**	**110,037.96**	**89,878.02**	**73,663.40**

***WPDG Warwickshire Property and Development Group**

***WRIF Warwickshire Recovery and Investment Fund BIG and PIF Pillars**

2.3 The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a need to borrow to fund the shortfall.

Table 2 – Financing of Capital Expenditure

£000's	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
Capital receipts	8,779.80	3,984.00	4,128.00	-	-	-
Capital grants	78,162.09	150,183.25	66,522.20	30,526.78	21,928.00	21,828.00
Self Financed Borrowing	-	-	-	-	-	-
Revenue	462.70	319.99	-	-	-	-
Capital Programme Funding/Income	87,404.59	154,487.25	70,650.20	30,526.78	21,928.00	21,828.00
WPDG Receipts	-	12,596.42	15,547.63	26,506.92	7,778.87	6,449.49
WRIF Receipts	1.67	532.08	2,470.42	6,416.25	10,857.08	13,756.67
Non Treasury Investment Funding/Income	1.67	13,128.50	18,018.04	32,923.17	18,635.96	20,206.15
Total Funding/Income	**87,406.25**	**167,615.75**	**88,668.24**	**63,449.95**	**40,563.96**	**42,034.15**
Total Capital Expenditure	117,843.67	316,943.52	223,039.36	110,037.96	89,878.02	73,663.40
Net financing need for the year	**30,437.41**	**149,327.77**	**134,371.12**	**46,588.01**	**49,314.06**	**31,629.25**
Minimum Revenue Provision (MRP)	- 10,502.91	- 11,300.29	- 16,821.39	- 21,523.38	- 22,525.97	- 23,597.49
Borrowing Requirement	**19,934.50**	**138,027.48**	**117,549.73**	**25,064.63**	**26,788.10**	**8,031.76**

2.4 The net financing need split between capital expenditure and non-Treasury investments is shown below, to help show the relative scale of non-Treasury investments.

Table 3 – Financing of Non-Treasury Investments

£000's	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
WPDG Capital Investment	-	19,101.40	21,762.84	7,610.72	242.41	16,334.00
Less: WDPG Related Receipts and Repayments	-	12,596.42	15,547.63	26,506.92	7,778.87	6,449.49
WRIF Capital Investment	2,500.00	20,600.00	20,000.00	20,000.00	26,500.00	-
Less: WRIF Related Receipts and Repayments	1.67	532.08	2,470.42	6,416.25	10,857.08	13,756.67
Net financing need for the year	**2,501.67**	**52,829.91**	**59,780.88**	**60,533.89**	**45,378.37**	**36,540.15**
Percentage of total net financing need %	8.2%	35.4%	44.5%	129.9%	92.0%	115.5%

2.5 Further details in respect of non-Treasury investments are set out in the separate Investment Strategy document.

*Prudential Indicator - **The Council's Borrowing Need (Capital Financing Requirement)***

2.6 The second prudential indicator is the Council's Capital Financing Requirement (CFR). The 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 indebtedness and underlying borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

2.7 The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each asset's life, and so charges the economic consumption of capital assets as they are used.

Table 4 – Capital Financing Requirement

£000's	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
CFR – Capital Programme	284,792.96	396,247.54	490,052.47	520,429.55	539,111.20	551,015.11
CFR - WPDG	0.00	6,504.98	12,720.20	(6,176.01)	(13,712.47)	(3,827.96)
CFR - WRIF	2,498.33	22,566.25	40,095.83	53,679.58	69,322.50	55,565.83
Total CFR	**287,291.30**	**425,318.77**	**542,868.50**	**567,933.13**	**594,721.23**	**602,752.98**
Movement in CFR - Capital Prog		122,754.87	110,626.32	51,900.46	41,207.61	35,501.40
Movement in CFR - WPDG		6,504.98	6,215.21	(18,896.20)	(7,536.47)	9,884.51
Movement in CFR - WRIF		20,067.92	17,529.58	13,583.75	15,642.92	(13,756.67)
Movement in CFR - Total		**149,327.77**	**134,371.12**	**46,588.01**	**49,314.06**	**31,629.25**
Movement in CFR represented by						
Net financing need for the year	30,437.41	149,327.77	134,371.12	46,588.01	49,314.06	31,629.25
Less MRP and other financing	(10,502.91)	(11,300.29)	(16,821.39)	(21,523.38)	(22,525.97)	(23,597.49)
Movement in CFR net of MRP	**19,934.50**	**138,027.48**	**117,549.73**	**25,064.63**	**26,788.10**	**8,031.76**

*Prudential Indicator – **Liability Benchmark***

1.1 A third and new prudential indicator for 2023/24 is the Liability Benchmark (LB). The Council is required to estimate and measure the LB for the forthcoming financial year and the following two financial years, as a minimum**.**

1.2 There are four components to the LB: -

- Existing loan debt outstanding: the Authority's existing loans that are still outstanding in future years.

- CFR: this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned MRP.

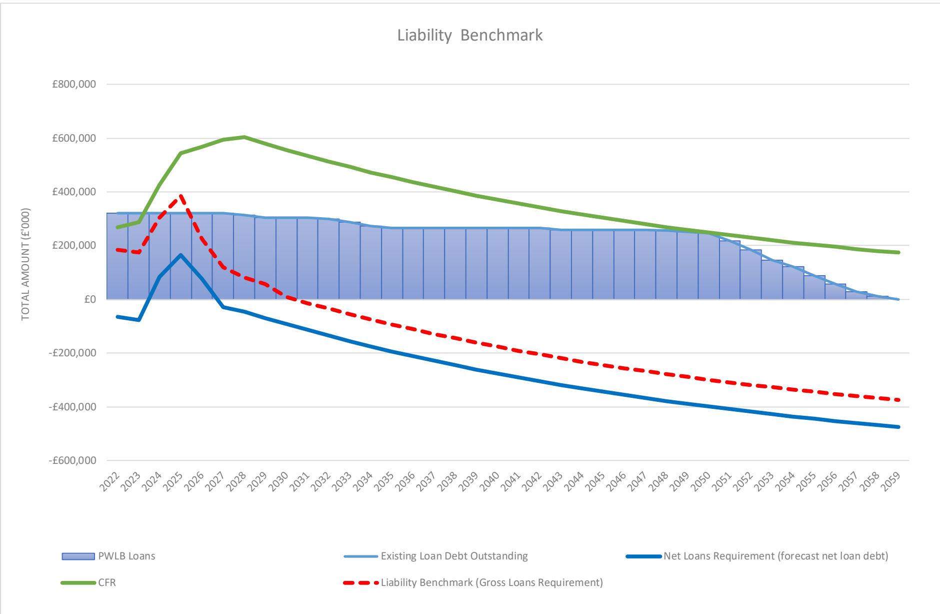
- Net loans requirement: this will show the Authority's gross loan debt less Treasury Management investments at the last financial year-end, projected into the future and based on its approved prudential borrowing, planned MRP and any other major cash flows forecast.

- Liability benchmark (or gross loans requirement): this equals net loans requirement plus short-term liquidity allowance.

Table 6 Liability Benchmark

In £000's	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31	2031/32
Existing Loan Debt	£321,413	£321,413	£321,413	£321,413	£321,413	£313,413	£303,413	£303,413	£303,413	£299,413
Net Loans Requirement	-£76,154	£83,949	£164,895	£75,508	-£29,307	-£44,873	-£68,792	-£91,754	-£113,798	-£134,959
CFR	£287,291	£425,319	£542,869	£567,933	£594,721	£602,753	£578,834	£555,872	£533,829	£512,667
Liability Benchmark	**£184,348**	**£173,846**	**£303,949**	**£384,895**	**£225,508**	**£120,693**	**£80,127**	**£56,208**	**£8,246**	**-£13,798**
Forecast Investments	£387,064	£210,000	£200,000	£200,000	£150,000	£150,000	£125,000	£125,000	£100,000	£100,000
(Over)/Under LB	-£137,064	-£147,567	-£17,464	£63,482	-£95,905	-£200,720	-£233,286	-£247,205	-£295,167	-£317,210

Chart 1 Liability Benchmark



Core Funds and Expected Investment Balances

2.10 The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year-end balances for each resource and anticipated day-to-day cash flow balances.

Table 7 – Expected Investments

£000's	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
Fund balances / reserves	223,244.36	188,595.40	178,378.17	176,305.94	170,383.71	170,383.71
Capital receipts	-	-	-	-	-	-
Other	3,305.42	4,577.99	4,577.99	4,577.99	4,577.99	4,577.99
Total core funds	**226,549.78**	**193,173.39**	**182,956.16**	**180,883.93**	**174,961.70**	**174,961.70**
Working capital	127,000.00	127,000.00	127,000.00	127,000.00	127,000.00	127,000.00
(Under)/over borrowing	34,114.70	- 103,912.77	- 206,462.50	- 191,527.13	- 188,315.23	- 196,346.98
Expected treasury investments	**387,664.48**	**216,260.62**	**103,493.66**	**116,356.80**	**113,646.47**	**105,614.71**

* Working capital balances shown are estimated year-end; these may be higher mid-year

Minimum Revenue Provision (MRP) Policy Statement

2.11 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).

2.12 The MRP should be designed to make prudent provision to redeem debt liabilities over a period which is reasonably commensurate with the associated capital expenditure benefits.

2.13 Having regard to these requirements, the MRP provision will be calculated as set out below.

MRP for Capital Programme Expenditure.

2.14 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; and
- Vehicles, plant and equipment and intangible assets.

2.15 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.

2.16 The 2020 review shows that the remaining useful life of our assets is now 22 years. By using an average life of 25 years for our assets equates to an annual provision of 4% straight line MRP.

2.17 For vehicles, plant and equipment, the remaining useful life is assumed to be 6 years e.g. 5 years average remaining useful life will result in 20% straight line MRP.

MRP for the Warwickshire Property Development Group (WPDG)

2.18 Unlike mainstream capital spending where provision for purchase of replacement assets has to be made in order to have funding available for replacement assets, expenditure (investment) in the WPDG will at a later date be repaid in full.

2.19 It is possible to assume that these repayments of principal amount to the necessary revenue provision. However, there is a risk that repayment of principal is not made, or not made in full. In order to mitigate this risk, the MRP policy for the WPDG will be to make a provision as follows:

- No MRP will be charged to the revenue account on any equity land or asset transfers into Wholly Owned subsidiaries.
- No MRP will be charged on working capital loans. Any anticipated impairments will be treated following the relevant accounting standards (namely IFRS9 - Financial Instruments), and not charged through the capital financing regime.
- MRP on development loans made to DevCo (a subsidiary of WPDG) will be charged over 25 years of equivalent to 4% per year, in line with the existing MRP policy for the capital programme.
- MRP on loans to ManCo (a subsidiary of WPDG for purchase of assets from DevCo) will be charged to the revenue account over 25 years (4% per year) in order to match the repayment profile of senior lending and operating life of those assets.
- Any capital receipts then received as repayment of the loan principal from ManCo and Dev Co will be used to offset "traditional" borrowing requirements for financing the wider capital programme.

MRP for the Warwickshire Recovery Investment Fund (WRIF)

2.20 Unlike mainstream capital spending where provision for purchase of replacement assets has to be made in order to have funding available for replacement assets, expenditure (investment) in the WRIF will at a later date be repaid in full.

2.21 It is possible to assume that these repayments of principal amount to the necessary revenue provision. However, there is a risk that repayment of principal is not made, or not made in full. In order to mitigate this risk, the MRP policy for the WRIF will be to make a provision as follows:

- MRP on WRIF loans that are capital in nature will be 4% per year. This aligns with the intention for MRP to be associated with the underlying asset life rather than the duration of the loan.
- Any capital receipts then received as repayment of the loan principal from WRIF will be used to offset "traditional" borrowing requirements for financing the wider capital programme.

MRP Calculation

2.22 The actual calculation of MRP will be based on the [Total Capital Financing Requirement x 4%]. This is deemed to be a prudent overall level of provision based upon the requirements set out above.

2.23 The Council has the option to directly and specifically link internal borrowing to specific investments and where this is the case a MRP would not be made. This would mean that repayments associated with the loan would not be capital and would therefore not be ringfenced to financing capital spending. Any anticipated impairments will be treated following the relevant accounting standards (namely IFRS9 - Financial Instruments), and not charged through the capital financing regime. However, the default position is that specific funding sources are not directly linked to specific investments therefore an express decision to link specific funding to a specific investment would need to be made for this to happen.

3.0 BORROWING

3.10 The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The Treasury Management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Capital Strategy. This involves both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant Treasury / prudential indicators, the current and projected debt positions, and the Annual Investment Strategy

3.11 The Council currently holds an over borrowed position (meaning external borrowing is greater than the total capital financing requirement), however this is forecast to change based on capital expenditure plans in the coming years. The need for further borrowing will be kept under review.

Current Portfolio Position

3.12 The overall Treasury Management portfolio as at 31st March 2022, 30th September 2022 and 31st December 2022 are shown below for both borrowing and investments.

Table 8 – Current Portfolio Position

Treasury Portfolio						
	Actual 31.03.2022 £m	Actual 31.03.2022 %	Actual 30.09.2022 £m	Actual 30.09.2022 %	**Actual 31.12.2022 £m**	**Actual 31.12.2022 %**
Treasury investments						
Banks	28.60	6.24%	25.49	5.61%	37.57	8.64%
Building Societies	80.10	17.47%	80.00	17.60%	80.00	18.39%
Local authorities	180.09	39.27%	176.00	38.72%	176.00	40.45%
Total managed in house	**288.79**	**62.97%**	**281.49**	**61.93%**	**293.57**	**67.48%**
Bond funds	31.87	6.95%	27.89	6.13%	29.05	6.68%
Property funds	12.00	2.62%	12.09	2.66%	10.22	2.35%
Cash fund managers	125.95	27.46%	133.07	29.27%	102.22	23.50%
Total managed externally	**169.83**	**37.03%**	**173.05**	**38.07%**	**141.49**	**32.52%**
TOTAL TREASURY INVESTMENTS	**458.62**	**100%**	**454.54**	**100%**	**435.07**	**100%**

3.13 Annex 2 sets out the current maturity profile of investments held, and the borrowing portfolio. Currently there is a significant concentration of debt maturities across the period 2050-2060.

3.14 The Council's forward projections for borrowing are summarised below. The table shows the actual external debt, against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

Table 9 – External Debt Forecast

£m	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
External Debt						
Debt at 1 April	321.406	321.406	321.406	336.406	376.406	406.406
New Debt	-	-	15.000	40.000	30.000	-
Actual gross debt at 31 March	**321.406**	**321.406**	**336.406**	**376.406**	**406.406**	**406.406**
The Capital Financing Requirement	287.291	425.319	542.869	567.933	594.721	602.753
Under / (over) borrowing	**- 34.115**	**103.913**	**206.463**	**191.527**	**188.315**	**196.347**

Internal Debt

3.15 The Council will seek to hold efficient levels of cash and will therefore run down external investment balances and use cash to finance a share of the Capital Financing Requirement. This is referred to as internal borrowing and when implemented it will improve our annual net interest costs, as the loss of interest on investment is currently lower than the cost of interest on external loans. The level of internal borrowing will be kept under review to ensure that the level of total Treasury investments (a liquidity buffer) does not fall below £100m.

Table 10 – Internal Debt Forecast

£m	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
External Debt	321.406	321.406	336.406	376.406	406.406	406.406
Internal Debt (internal borrowing)	-	103.913	206.463	191.527	188.315	196.347
Internal borrowing as % of CFR	**0.0%**	**24.4%**	**38.0%**	**33.7%**	**31.7%**	**32.6%**

3.16 Where it is deemed appropriate to add to the level of current external loan finance, any risks associated with such borrowing will be subject to prior appraisal (including borrow now or borrow later analysis) and subsequent reporting through the mid-year or annual reporting mechanism.

3.17 Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2023/24 and the following two financial years. This allows some flexibility for limited early borrowing for future years but ensures that borrowing is not undertaken for revenue or speculative purposes.

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

Treasury Indicators: Limits to Borrowing Activity

3.19 **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.

Table 11 – Operational Boundary

£m	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
External Debt	321.406	467.851	597.155	624.726	654.193	663.028
Total	**321.406**	**467.851**	**597.155**	**624.726**	**654.193**	**663.028**

The Authorised Limit for External Debt

3.20 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.

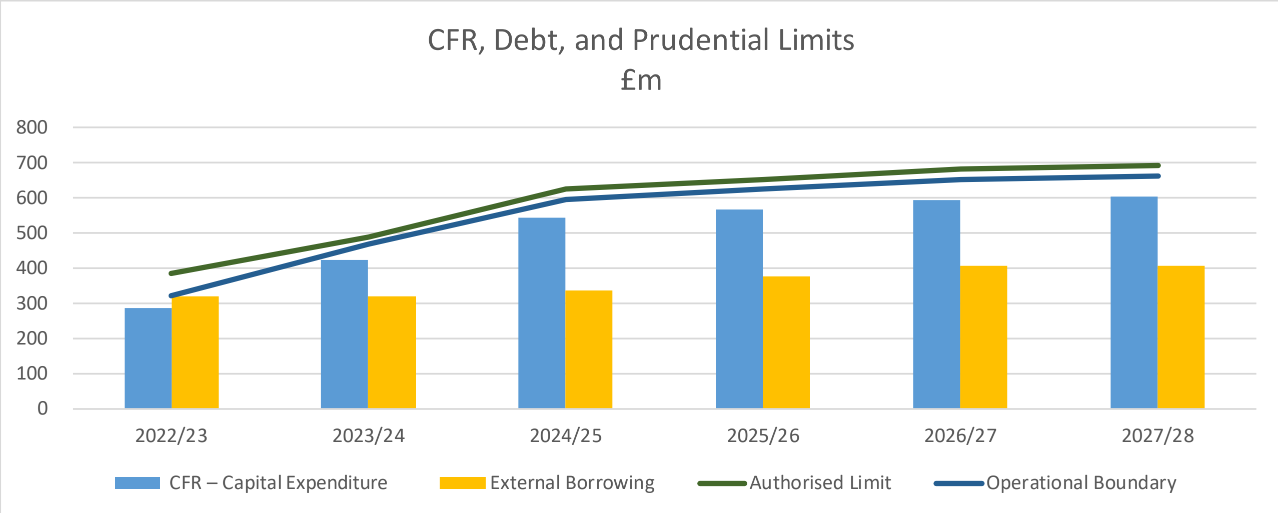
3.21 This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all Councils' plans, or those of a specific Council, although this power has not yet been exercised.

3.22 The Council is asked to approve the following authorised limit.

Table 12 – Authorised Limit

£m	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate
External Debt	386.00	490.00	625.00	654.00	684.00	694.00
Total	**386.000**	**490.000**	**625.000**	**654.000**	**684.000**	**694.000**

Chart 2 - Capital Financing Requirement, Debt and Prudential Limits



Prospects for Interest Rates

3.23 The Council has appointed Link Group as its Treasury adviser and part of their service is to assist the Council to formulate a view on interest rates. Link provided the following forecasts on 19th November 2022. These are forecasts for certainty rates, gilt yields plus 80 bps.

Table 12 – Interest Rate Forecasts

Link Group Interest Rate View	19.12.22												
	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
BANK RATE	3.50	4.25	4.50	4.50	4.50	4.00	3.75	3.50	3.25	3.00	2.75	2.50	2.50
3 month ave earnings	3.60	4.30	4.50	4.50	4.50	4.00	3.80	3.30	3.00	3.00	2.80	2.50	2.50
6 month ave earnings	4.20	4.50	4.60	4.50	4.20	4.10	3.90	3.40	3.10	3.00	2.90	2.60	2.60
12 month ave earnings	4.70	4.70	4.70	4.50	4.30	4.20	4.00	3.50	3.20	3.10	3.00	2.70	2.70
5 yr PWLB	4.20	4.20	4.20	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.20	3.10
10 yr PWLB	4.30	4.40	4.40	4.30	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.30
25 yr PWLB	4.60	4.60	4.60	4.50	4.40	4.20	4.10	4.00	3.90	3.70	3.60	3.50	3.50
50 yr PWLB	4.30	4.30	4.30	4.20	4.10	3.90	3.80	3.70	3.60	3.50	3.30	3.20	3.20

3.24 This forecast from Link Group reflects a view that the Monetary Policy Committee (MPC) will be keen to demonstrate its anti-inflation credentials by delivering a succession of rate increases. Bank Rate stands at 3.5% currently but is expected to reach a peak of 4.5% in H1 2023.

3.25 Link anticipate the Bank of England will be keen to loosen monetary policy when the worst of the inflationary pressures have lessened however the timing of this is uncertain.

3.26 The CPI measure of inflation will peak at close to 11% in Q4 2022. Despite the cost-of-living crisis that is still taking shape, the Bank will want to see evidence that wages are not spiralling upwards in what is evidently a very tight labour market. Wage increases, excluding bonuses, are currently running at 5.7%.

3.27 Regarding the plan to sell £10bn of gilts back into the market each quarter (Quantitative Tightening), this has started but will focus on the short to medium end of the curve for the present. This approach will prevent any further disruption to the longer end of the curve following on from the short-lived effects of the Truss/Kwarteng unfunded dash for growth policy.

3.28 In the upcoming months, Link forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but the on-going conflict between Russia and Ukraine. (More recently, the heightened tensions between China/Taiwan/US also have the potential to have a wider and negative economic impact.)

3.29 On the positive side, consumers are still estimated to be sitting on over £160bn of excess savings left over from the pandemic so that will cushion some of the impact of the above challenges. However, most of those are held by more affluent people whereas lower income families already spend nearly all their income on essentials such as food, energy and rent/mortgage payments.

3.30 PWLB RATES

- Yield curve movements have become less volatile under the Sunak/Hunt government. PWLB 5 to 50 years Certainty Rates are, generally, in the range of 3.75% to 4.50%. The medium to longer part of the yield curve is currently inverted (yields are lower at the longer end of the yield curve compared to the short to medium end).
- Link view the markets as having built in, already, nearly all the effects on gilt yields of the likely increases in Bank Rate and the poor inflation outlook but markets are volatile and further whipsawing of gilt yields across the whole spectrum of the curve is possible.

3.31 The balance of risks to the UK economy: -

The overall balance of risks to economic growth in the UK is to the downside. Indeed, the Bank of England projected two years of negative growth in their November Quarterly Monetary Policy Report.

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

- Labour and supply shortages prove more enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, rising gilt yields).

- The Bank of England acts too quickly, or too far, over the next two years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.

- UK / EU trade arrangements – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.

- Geopolitical risks, for example in Ukraine/Russia, China/Taiwan/US, Iran, North Korea and Middle Eastern countries, which could lead to increasing safe-haven flows.

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

- The Bank of England is too slow in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly and for a longer period within the UK economy, which then necessitates an even more rapid series of increases in Bank Rate faster than we currently expect.

- The Government acts too slowly to increase taxes and/or cut expenditure to balance the public finances, in the light of the cost-of-living squeeze.

- The pound weakens because of a lack of confidence in the UK Government's fiscal policies, resulting in investors pricing in a risk premium for holding UK sovereign debt.

- Longer term US Treasury yields rise strongly, if inflation numbers disappoint on the upside, and pull gilt yields up higher than currently forecast.

Borrowing advice:

- Link's long-term (beyond 10 years) forecast for Bank Rate stands at 2.5%. As all PWLB certainty rates are now above this level, borrowing strategies will need to be reviewed in that context. Better value can generally be obtained at the shorter end of the curve and short-dated fixed LA to LA monies should be considered. Temporary borrowing rates are likely, however, to remain near Bank Rate and may also prove attractive whilst the market waits for inflation, and therein gilt yields, to drop back later in 2023.

- Link suggested budgeted earnings rates for investments up to about three months' duration in each financial year are as follows: -

Average earnings in each year	
2022/23 (remainder)	4.00%
2023/24	4.40%
2024/25	3.30%
2025/26	2.60%
2026/27	2.50%
Years 6 to 10	2.80%
Years 10+	2.80%

- As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts.

- Our interest rate forecast for Bank Rate is in steps of 25 bps, whereas PWLB forecasts have been rounded to the nearest 10 bps and are central forecasts within bands of + / - 25 bps. Naturally, we continue to monitor events and will update our forecasts as and when appropriate.

Borrowing Strategy

3.32 The Council is currently maintaining an over-borrowed position. This means that more external borrowing exists than is necessary which results in higher cash balances being held by the Council. However, the borrowing position is forecast to change based on the capital expenditure planned over the next 5 years and beyond, switching to an "under-borrowed" position. This is planned in order to make efficient use of cash balances. By, in effect, borrowing from internal balances the cost of borrowing is lower than borrowing from an external lender.

3.33 Against this background and the risks within the economic forecast, caution will be adopted with the 2023/24 Treasury operations. The Assistant Director - Finance 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 borrowing rates, then borrowing will be postponed.
- if it was felt that there was a significant risk of a much sharper RISE in borrowing 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.

3.34 Any decisions will be reported to the appropriate decision-making body at the next available opportunity.

3.35 With the current over-borrowed position, but also being mindful of the economic outlook for 2023/24 (annex 8) the following assumptions will be adopted in the borrowing strategy:

- 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 will be considered where available, to ensure the best rates and to maintain 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.
- To ensure that the Council considers all options to secure long-term certainty, the Council may also look to make use of forward starting loans as this will allow us to lock into a known financing rate out of a future date. These loans tend to be offered by Financial institutions (primarily insurance companies and pension funds but also some banks, where the objective is to use the forward loan with a

mix of internal loans/temporary borrowing to avoid a “cost of carry” or to achieve refinancing certainty over the next few years).

Policy on Borrowing in Advance of Need

3.36 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.

3.37 However, the Council may borrow in advance of need for risk management or borrowing efficiency purposes. 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; and
- 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.

Debt Rescheduling

3.38 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 cost of debt repayments. Reasons for debt rescheduling would include:

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

3.39 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, currently the penalty premiums that would be incurred by doing so means there currently is no net financial benefit from such early repayment.

New Financial Institutions as a Source of Borrowing and / or Types of Borrowing

3.40 Currently the PWLB Certainty Rate is set at gilts + 80 basis points for both Housing Revenue Account and non-Housing Revenue Account borrowing. However, consideration may still need to be given to sourcing funding from the following sources for the following reasons (for full list see annex 3):

- Local authorities (primarily shorter dated maturities out to 3 years or so – still cheaper than the Certainty Rate).
- Financial institutions (primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a "cost of carry" or to achieve refinancing certainty over the next few years).
- Municipal Bonds Agency (possibly still a viable alternative depending on market circumstances prevailing at the time).

3.41 Our advisors will keep us informed as to the relative merits of each of these alternative funding sources.

4.0 ANNUAL INVESTMENT STRATEGY

Investment Policy – Management of Risk

4.10 The Department of Levelling Up, Housing and Communities (DLUHC - this was formerly the Ministry of Housing, Communities and Local Government (MHCLG)) and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with Treasury (financial) investments, (as managed by the Treasury Management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy, (a separate report).

4.11 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 2021 ("the Code")
- CIPFA Treasury Management Guidance Notes 2018

4.12 The Council's investment priorities will be security first, portfolio liquidity second and then yield (return). The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and within the Council's risk appetite. In the current economic climate, it is considered appropriate to maintain a degree of liquidity to cover cash flow needs but to also consider spreading investments for periods up to 12 months with high credit rated financial institutions, whilst investment rates remain elevated, as well as wider range fund options

4.13 The above guidance from the DLUHC and CIPFA places 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:

a.) 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.

b.) **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 advisers to maintain a monitor on market pricing such as **"credit default swaps"** and overlay that information on top of the credit ratings.

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

d.) 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 annex 4 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 or have less than a year left to run to maturity if originally, they were classified as being non-specified investments solely due to the maturity period exceeding 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.

e.) **Non-specified and loan investment limits.** The Council has determined that it will set a limit to the maximum exposure of the total Treasury Management investment portfolio to non-specified Treasury Management investments of £80m.

f.) **Lending limits**, (amounts and maturity), for each counterparty will be set through applying the matrix table in Annex 4.

g.) **Sector Limits.** The Council has determined that it will limit the maximum exposure within different sectors of investments. These are set out in Annex 4

h.) **Transaction limits** are set for each type of investment in Annex 4.

i.) Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating**, (see paragraph 4.10).

j.) This authority has engaged **external consultants**, (see paragraph 1.11), 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.

k.) As a result of the change in accounting standards for 2022/23 under IFRS 9, the Council 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. (In November 2018, the MHCLG, concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years ending 31.3.23. At the current juncture it has not been determined whether a further extension to the over-ride will be agreed by Government.)

4.14 However, this authority will also pursue **value for money** in Treasury Management and will monitor the yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year.

4.15 The above risk management policy criteria are **unchanged** from last year.

Creditworthiness Policy

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

- Maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the specified and non-specified investment sections below; and
- Has sufficient liquidity in its investments. For this purpose, it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

4.17 The Assistant Director – Finance will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them 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.

4.18 Credit rating information is supplied by the Link Group, our Treasury advisers, on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating Watches (notification of a likely change), rating Outlooks (notification of the longer-term bias outside the central rating view) are provided to officers almost immediately after they occur, and this information is considered before dealing. For instance, a negative rating Watch applying to counterparty at the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions.

4.19 The criteria for providing a pool of high-quality investment counterparties, (both specified and non-specified investments) is:

a.) **Banks of good credit quality –** the Council will only use banks which are:
- UK banks; or
- non-UK and domiciled in a country which has a minimum sovereign Long-Term rating of A-

and have, as a minimum, the following Fitch Ratings:
- Short Term – F1
- Long Term – A-

b.) **Council's own Bank** – The Council's own banker for transactional purposes if the bank falls below the above criteria, although in this case balances will be minimised in both monetary size and time invested.

c.) **Building Societies** - The Council will use all societies which meet the ratings for banks outlined above;

d.) **Money Market Funds (MMFs)**:
- CNAV (constant net asset value) – AAA rated
- LVNAV (low volatility net asset value)– AAA rated
- VNAV (variable net asset value) – AAA rated

e.) **Property Funds** - CCLA (refer to table D and E in annexes)

f.) **Social Bond Funds** - Threadneedle (refer to table D and E in annexes)

g.) **Ultra-Short Dated Bond Funds** – at least AA rated

h.) **Local Authorities and Parish Council Loans** - both spot and forward dates

i.) **Housing Association Loans** - both spot and forward dates

4.20 **Use of additional information other than credit ratings** – Additional requirements under the Code require the Council to supplement credit rating information. Whilst the above criteria rely primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information (for example Credit Default Swaps, rating Watches/Outlooks) will be applied to compare the relative security of differing investment opportunities.

4.21 **Time and monetary limits applying to investments** – The time and monetary limits for institutions on the Council's counterparty list are detailed in Annex 4.

4.22 **Creditworthiness** – Significant levels of downgrades to Short and Long-Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. However, more recently the UK sovereign debt rating has been placed on Negative Outlook by the three major rating agencies in the wake of the Truss/Kwarteng unfunded tax-cuts policy. Although the Sunak/Hunt government has calmed markets, the outcome of the rating agency reviews is unknown at present, but it is possible the UK sovereign debt rating will be downgraded. Accordingly, when setting minimum sovereign debt ratings, the Council will not set a minimum rating for the UK.

4.23 **Credit Default Swaps (CDS) prices** – Although bank CDS prices (these are market indicators of credit risk) spiked upwards at the end of March / early April 2020 due to the heightened market uncertainty and ensuing liquidity crisis that affected financial markets, they have returned to more average levels since then. However, sentiment can easily shift, so it will remain important to undertake continual monitoring of all aspects of risk and return in the current circumstances. Link monitor CDS prices as part of their creditworthiness service to local authorities and the Council has access to this information via its Link-provided Passport portal.

Other Limits

4.24 Due care will be taken to consider the exposure of the Council's total investment portfolio to non-specified investments, countries, groups and sectors:

a.) **Country limit** – The Council has determined that it will only use approved counterparties from the UK and from countries with a **minimum sovereign credit rating of *A-*** from Fitch Ratings. The list of countries that qualify using this credit criteria as at the date of this report are shown in Annex 5. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

b.) **In-house funds** – Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e., rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. While most cash balances are required in order to manage the ups and downs of cash flow where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed:

- If it is thought that Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments as being short term or variable.
- Conversely, if it is thought that Bank Rate is likely to fall within that time period, consideration will be given to locking in higher rates currently obtainable, for longer periods.

Investment Returns Expectations

4.25 The current forecast shown in paragraph 3.3, includes a forecast for Bank Rate to reach 4.5% in Q2 2023.

4.26 The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows:

Table 13 – Estimated Investment Returns

Average earnings in each year	
2022/23 (remainder)	3.95%
2023/24	4.40%
2024/25	3.30%
2025/26	2.60%
2026/27	2.50%
Years 6 to 10	2.80%
Years 10+	2.80%

As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts.

Investment Performance / Risk Benchmarking

4.27 **Benchmarks** are guides to risk, they may be breached depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is so that officers can monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Current advice suggests using the investment benchmark – ‘returns above the 7-day SONIA compounded rate’.

Non-Treasury Investment Strategy

4.28 A separate document entitled “Investment Strategy” covers the Council’s position in **respect of non-Treasury Management investments held for service reasons or commercial reasons.**

End of Year Investment Report

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

External Fund Managers

4.30 The County Council uses a number of external managers to spread risk and obtain maximum market exposure. Current external fund managers actively used during the last year are listed below. This list is not exhaustive and new fund managers may be engaged if necessary. Officers will periodically review the position, performance, and costs of external fund managers, and may meet with client relationship managers or fund managers as appropriate.

- Blackrock
- Deutsche Bank
- Goldman Sachs
- Insight
- Aberdeen
- Federated Hermes
- CCLA
- Threadneedle

Environmental, Social, and Governance Policy

4.31 As a responsible investor, the Council is committed to considering environmental, social, and governance (ESG) issues, and has a particular interest in taking action against climate change and pursuing activities that have a positive social impact.

4.32 However, the Treasury Management function is controlled by statute and by professional guidelines and the first priorities of Treasury must remain security, liquidity, and yield. With those priorities kept in place, the following activity will be undertaken in respect of climate change and responsible investing. Steps will be taken to:

- Ensure an understanding of the degree to which investments may contribute towards climate change. This may take the form of measuring the carbon footprint or some similar measure.

- Where appropriate, move cash balances to funds that have are ESG driven targets, or “green funds”, to ensure our investment is contributing towards tackling ESG issues.
- Identify and understand the extent to which investments which are exposed to risks driven by climate change, for example investments in assets at risk of weather change (e.g. property or infrastructure at risk of flooding), assets at risk of becoming stranded (e.g. fossil fuel investments), or assets at risk from geopolitical risks driven by climate change (e.g. water access, the capacity for food production, or economic conflict).
- Keep abreast of new investment opportunities that have regard to ethical investing and climate change as this is a quickly developing arena.
- Understand the ESG policies of funds, other local authorities, when considering new investment opportunities.

Pension Fund Cash

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. The council has a separate statement for Pension Fund investment purposes.

5.0 Early Payment of Pension Fund Contributions

5.10 The Council intends to pay its 3-year pension fund contributions for the valuation period 2023/24-2025/26 in one lump sum at the start of the valuation period, with the preference being to do this in April 2023. An early payment in April 2023 will be given a discount rate compared to cash payments made at normal monthly intervals. The benefits, costs, and risks this are set out below:

5.11 Benefits

a.) A gross saving of £6.205m in the total cash contributions required over the valuation period.

Total Payments in Normal Monthly Contributions	Total Payment Single Lump Sum Contribution	Gross Difference
£107.879m	£101.674m	£6.205m

b.) A net one-off saving would be made after having regard to the loss of assumed returns that would otherwise have been made on the cash before it was paid out in pension contributions (refer to Section 5.12 below for alternative returns).

5.12 Early payment entails the following costs and risks:

- Timing / volatility risk – Pension fund investments provide a higher rate of return but at a higher level of volatility. Therefore although over time the returns are likely to be better, at any one moment in time the value of the fund could be unusually high or low and across shorter period of time the return could be more distant above or below the expected average. By placing all the cash into the fund at one moment in time the exposure to volatility and therefore to losses is higher. However making the payments more spread out to reduce this risk would also reduce the opportunity to benefit.

- The pension fund contributions to cover future service costs normally vary with the payroll bill by being calculated as a % of payroll but with an up-front payment this cannot happen naturally. Therefore the pension fund will reserve the right to ask for top up payments if the total payroll costs increase significantly enough. This needs to be planned for but this would amount to a correction for costs that would have to be paid anyway – it would not mean a loss. The Council will undertake to pay any such adjustments and holds a Pension Deficit Reserve to assist in providing cover for future pension fund deficits.

- The County Council will run lower cash balances, however the Council will have the facilities to maintain enough cash to manage its operations. The cash position will also gradually over the 3-year period move back to what it would have been if monthly payments had been made, but adjusted to reflect the lower total amount required to be paid.

- The County Council will earn less interest on cash balances which will offset the benefits. For example, if returns of 1.5% were earned on cash balances then the interest foregone would amount to £5m and this would offset the reduction in pension fund contribution payments above.

- The Council could not invest this cash in other new investment opportunities. For example, if the funds were to be invested in high return stocks or property funds. However other opportunities entail different risks, for example with property funds entailing liquidity risks and stocks entailing higher volatility risks. As early payment action has an effect over a period of a few years with most of the impact being in the early part of that time frame it does not preclude the Council from considering wider opportunities in the longer term.

- Scenarios in which the Council would suffer reductions in benefits or incur losses are:

    - If there is volatility in the pension fund investment valuation – in particular an if there are significant falls in volatile assets after the point of payment.

    - If new Treasury investment opportunities with a better risk/return profile become available elsewhere then the cash to pursue those opportunities would be less or would be delayed.

- If lump sum payment is made later than April 2023 then the expected financial benefit would be less as the duration of the benefit would be less, the amounts would be less, and the discount rate may be less. However exposure to timing and volatility risk would also be less.

- If a loss were experienced this would manifest in the next pension fund valuation and would be recovered through future contributions to the pension fund as determined by the next valuation.

5.13 The early payment is a cash flow measure, it does not mean the Council is paying more than it should into the pension fund. From the period April 2023 to March 2026 the Council's cash position will gradually move back to the same position that it would have been in March 2026, except for the net benefit or loss arising from the early payment.

5.14 The potential to benefit is greatest in April 2023, however the strategy provides the flexibility to make an early payment later or not at all if the right conditions are not met. A payment will only be made and the timing of any payment decided on subject to the following conditions being met.

a.) Obtaining legal confirmation that the payment is lawful.
b.) That external auditors are content with the payment and its accounting treatment.
c.) Having the approval of the Section 151 officer and Monitoring Officer.
d.) Having the agreement of the Pension Fund Actuaries.
e.) Having a Rates and Adjustment Certificate from the Pension Fund actuaries setting out the amount payable, which may be varied from the above quoted figure to reflect the final Warwickshire County Council related payment.
f.) That the payment can be accommodated within the overall Treasury position, having regard to wider investment and borrowing commitments.
g.) That the Section 151 Officer is satisfied that the market position at the time of making the early payment still supports the early payment being made, compared to the option of investing Treasury balances with normal Treasury counterparties and taking into account the relative uncertainty of returns from normal Treasury activity.

ANNEXES

1. Prudential and Treasury Indicators
2. Treasury Management - Portfolio
3. Approved Sources of Long and Short Term borrowing
4. Treasury Management - Practice
5. Approved Countries for Investments
6. Treasury Management - Scheme of Delegation
7. Treasury Management - Role of the Section 151 Officer
8. Economic background

Annex 1

Prudential and Treasury Indicators

The Council's capital expenditure plans are the key driver of Treasury Management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

The following indicators are set out in the main body of the report:

Prudential Indicator	Reference
Capital Expenditure	Table 1
Gross Debt	Table 2
Capital Financing Requirement	Table 4
Liability Benchmark	Table 6
Over/Under Borrowing	Table 7
Borrowing - Operational Boundary	Table 11
Borrowing - Authorised Borrowing Limit	Table 12

In addition, the prudential indicators below will be applied.

TREASURY MANAGEMENT PRUDENTIAL INDICATORS	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28
Upper limit for fixed interest rate exposure						
Net principal re fixed rate borrowing / fixed term investments	100%	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%	25%
Upper limit for total principal sums invested for over 365 days	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
(per maturity date)	150,000	150,000	150,000	150,000	150,000	150,000

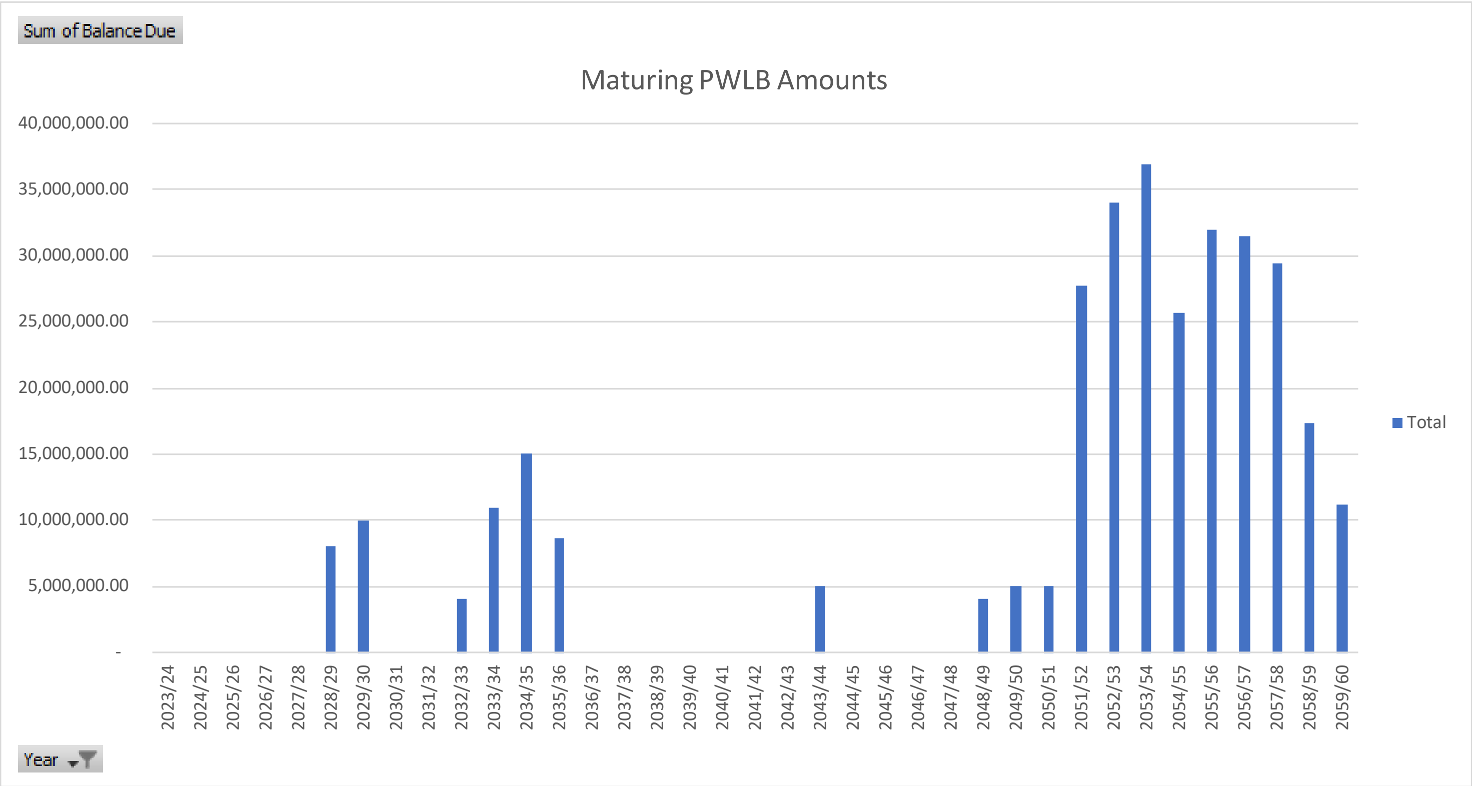
Maturity structure of new fixed rate borrowing during year	upper limit	lower limit
under 12 months	20%	0%
12 months and within 24 months	40%	0%
24 months and within 5 years	60%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

Maturity structure of new external borrowing during year	upper limit	lower limit
under 12 months	35%	0%
12 months and within 24 months	45%	0%
24 months and within 5 years	65%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

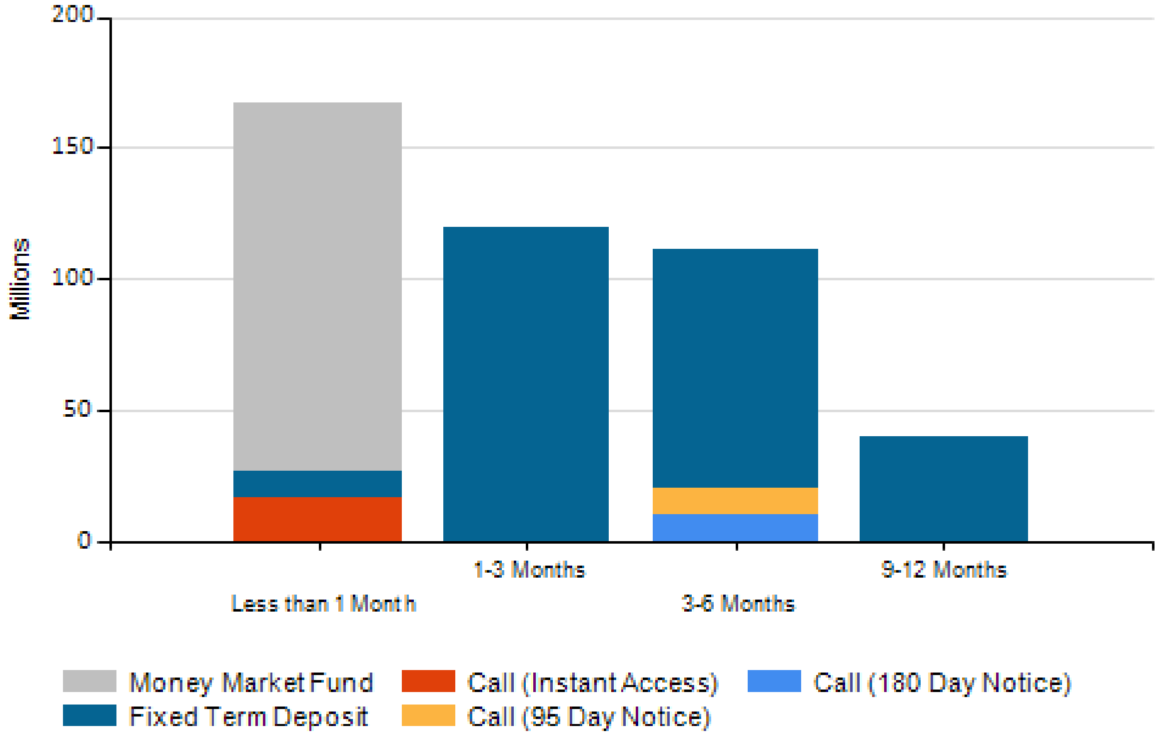
Annex 2

Treasury Management Portfolio

1. Debt Schedule



2. Investment Portfolio as at 31st December 2022



3. Balance Sheet Forecast

Warwickshire County Council
Balance Sheet Projections

2022/23* (£'000)		2023/24 (£'000)	2024/25 (£'000)	2025/26 (£'000)	2026/27 (£'000)	2027/28 (£'000)
CAPITAL FINANCING REQUIREMENT						
287,291	CFR Relating to General Fund	425,319	542,869	567,933	594,721	602,753
287,291	Total CFR	425,319	542,869	567,933	594,721	602,753
-	Finance Lease Liabilities		-	-	-	-
287,291	Underlying Borrowing Requirement	425,319	542,869	567,933	594,721	602,753
321,406	External Borrowing c/fwd	321,406	321,406	336,406	376,406	406,406
	Loan Maturities					
-	New Loans	-	15,000	40,000	30,000	-
321,406	External Borrowing	321,406	336,406	376,406	406,406	406,406
(34,115)	Under / (Over) Borrowing	103,913	206,463	191,527	188,315	196,347
-12%	*Borrowing as a % of Requirement*	*24%*	*38%*	*34%*	*32%*	*33%*
RESERVES / BALANCES, INVESTMENTS & WORKING CAPITAL (£'000)						
4,573	General Fund Balance	4,573	4,573	4,573	4,573	4,573
224	Collection Fund Adjustment Account	224	224	224	224	224
218,447	Earmarked reserves	183,798	173,581	171,509	165,586	165,586
-	Capital Receipts Reserve	-	-	-	-	-
949	Provisions	2,221	2,221	2,221	2,221	2,221
2,357	Capital Grants Unapplied	2,357	2,357	2,357	2,357	2,357
34,115	Over / (Under) Borrowing	(103,913)	(206,463)	(191,527)	(188,315)	(196,347)
127,000	Working Capital	127,000	127,000	127,000	127,000	127,000
387,664	Expected Treasury Investments	216,261	103,494	116,357	113,646	105,615

*Year end balances currently estimated for 2022/23

Annex 3

Approved Sources of Long and Short-Term Borrowing

On Balance Sheet	Fixed	Variable
PWLB	●	●
UK Municipal Bond Agency	●	●
Local Authorities	●	●
Banks	●	●
Pension Funds	●	●
Insurance Companies	●	●
UK Infrastructure Bank	●	●
Market (long-term)	●	●
Market (temporary)	●	●
Market (LOBOs)	●	●
Stock Issues	●	●
Local Temporary	●	●
Local Bonds	●	
Local Authority Bills	●	●
Overdraft		●
Negotiable Bonds	●	●
Internal (capital receipts & revenue balances)	●	●
Commercial Paper	●	
Medium Term Notes	●	
Finance Leases	●	●

Annex 4

Treasury Management – Practice

4.1 Counterparty Limits

	Fitch Long term Rating	Money Limit	Transaction limit	Time Limit
Banks	*A-*	£20m	£20m	1yr
Building Societies	*A-*	£20m	£20m	18 months
Local authorities	N/A	£10m	£10m	2yr
Housing Associations	N/A	£10m	£10m	3yr
DMADF	UK sovereign	unlimited	unlimited	6 months
Other Institutions limit	N/A	£10m	£10m	1yr
	Fund rating**	Money Limit	Transaction Limit	Time Limit
Money Market Funds CNAV	AAA	£60m	£60m	liquid
Money Market Funds LVNAV	AAA	£60m	£60m	liquid
Money Market Funds VNAV	AAA	£60m	£60m	liquid
Ultra-Short Dated Bond Funds	AA	£60m	£60m	liquid
Property Fund	N/A	£15m	£15m	90 day
Social Bond Funds	N/A	£40m	£40m	90 day

4.2 Sector Limits

Sector Type	Limit Applied
Money Market Funds (overnight funds) and Instant Access funds	£300m aggregate
Money Market Funds (overnight funds) and Instant Access funds	Maximum holding in any one fund should not represent more than 5% of that funds total asset value
Short Term Investments 7-95 day (deposits, call and notice accounts, property and social bond funds)	£200m aggregate
Medium Term Investments 95-365 day (lending, deposit, call and notice accounts)	£100m aggregate
Lending to Local Authorities	Maximum £250m total (increased from £200m last year)
Lending to Local Authorities	Forward deals (deals agreed in advance of the loan issue date) allowed up to a total of 2 years to include both notice and loan term
Deposits with Housing Associations	Maximum £100m total (this is a new limit)
Deposits with Housing Associations	Forward deals (deals agreed in advance of the loan issue date) allowed up to a total of 3 years to include both notice and loan term (this is a new limit).
Deposits with Building Societies	Maximum £100m total
Deposits with Building Societies	Forward deals (deals agreed in advance of the loan issue date) allowed up to a total of 18 months to include both notice and loan term (this is a new limit).

4.3 Specified Investments

Investment Type	Credit Criteria (Fitch Ratings)	Limits (per institution)	Use
DMO Deposit Facility	--	No Limit	In-house
Term deposits: Local Authorities	--	£10m	In-house
Term deposits: Housing Associations	--	£10m	In-house
Nationalised Banks	Short-term F1, Support 1	£20m	In-house and External Manager
Term deposits: UK Banks	Short-term F1, Long-term A, Viability a, Support 3	£20m	In-house and External Manager
Term deposits: Bank Council uses for current account	--	£25m	In-house and External Manager
Term deposits: UK Building Societies	Top five largest societies as reported annually. (To be continually monitored)	£20m	In-house and External Manager
Term deposits: Overseas Banks	Short-term F1+, Long-term AA- Viability aa, Support 1	£20m	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	£20m	External Manager
Money Market Funds	AAA	£60m	In-house and External Manager
Ultra Short Dated Bond Funds	AA	£40m	In-house and External Manager
UK Government Gilts, Treasury Bills	--	No Limit	External Manager
Gilt Funds and Bond Funds	Long-term A	No Limit	External Manager

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

4.4 Non-Specified Investments

Investment Type	Credit Criteria (Fitch Ratings)	Limits (per institution)	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	£20m	In-house and External Manager
Fixed Term Deposit with Variable Rates and Variable Maturities	Short-term F1, Long-term A, Viability a+, Support 3	£20m	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	£20m	External Manager
UK Government Gilts with maturities in excess of 1 year	--	£20m	External Manager
Local Government Association Municipal Bond Agency	--	£20m	--
CCLA Property Fund	--	£20m	--
Threadneedle Social Bond Fund	--	£40m	--
Local Authority wholly owned trading company	--	£5m	In-house

Annex 5

APPROVED COUNTRIES FOR INVESTMENTS

This list is based on those countries which have sovereign ratings of AA- or higher, (we show the lowest rating from Fitch, Moody's and S&P) and also, (except - at the time of writing - for Hong Kong, Norway and Luxembourg), have banks operating in sterling markets which have credit ratings of green or above in the Link credit worthiness service.

Based on lowest available rating

AAA

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

AA+

- Canada
- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)
- France

AA-

- Belgium
- Hong Kong
- Qatar
- **U.K.**

Annex 6

Treasury Management - Scheme of Delegation

(i) 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.
- Receiving and reviewing half year and annual monitoring reports and acting on recommendations.

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

- Overview and scrutiny of Treasury Management policy, practice, and activity as required.
- Receiving quarterly monitoring reports for overview and scrutiny.

Annex 7

Treasury Management – Role of the Section 151 Officer

The S151 (responsible) officer

- 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;
- approve the early payment of pension fund contributions
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers.
- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and Treasury Management, with a long term timeframe.
- Recommending the MRP policy.

Annex 8

ECONOMIC BACKGROUND-

Provided by Link Treasury Advisors

Against a backdrop of stubborn inflationary pressures, the easing of Covid restrictions in most developed economies, the Russian invasion of Ukraine, and a range of different UK Government policies, UK interest rates have been volatile right across the curve, from Bank Rate through to 50-year gilt yields, for all of 2022.

Market commentators' misplaced optimism around inflation has been the root cause of the rout in the bond markets with, for example, UK, EZ and US 10-year yields all rising by over 200bps since the turn of the year. The table below provides a snapshot of the conundrum facing central banks: inflation is elevated but labour markets are extra-ordinarily tight, making it an issue of fine judgment as to how far monetary policy needs to tighten.

	UK	Eurozone	US
Bank Rate	3.5%	2.0%	4.25%-4.50%
GDP	-0.2%q/q Q3 (2.4%y/y)	+0.2%q/q Q3 (2.1%y/y)	2.6% Q3 Annualised
Inflation	10.7%y/y (Nov)	10.1%y/y (Nov)	7.1%y/y (Nov)
Unemployment Rate	3.7% (Oct)	6.5% (Oct)	3.7% (Nov)

Q2 of 2022 saw UK GDP revised upwards to +0.2% q/q, but this was quickly reversed in the third quarter, albeit some of the fall in GDP can be placed at the foot of the extra Bank Holiday in the wake of the Queen's passing. Nevertheless, CPI inflation has picked up to what should be a peak reading of 11.1% in October, although with further increases in the gas and electricity price caps pencilled in for April 2023, and the cap potentially rising from an average of £2,500 to £3,000 per household, there is still a possibility that inflation will spike higher again before dropping back slowly through 2023.

The UK unemployment rate fell to a 48-year low of 3.6%, and this despite a net migration increase of c500k. The fact is that with many economic participants registered as long-term sick, the UK labour force actually shrunk by c500k in the year to June. Without an increase in the labour force participation rate, it is hard to see how the UK economy will be able to grow its way to prosperity, and with average wage increases running at over 6% the MPC will be concerned that wage inflation will prove just as sticky as major supply-side shocks to food and energy that have endured since Russia's invasion of Ukraine on 22nd February 2022.

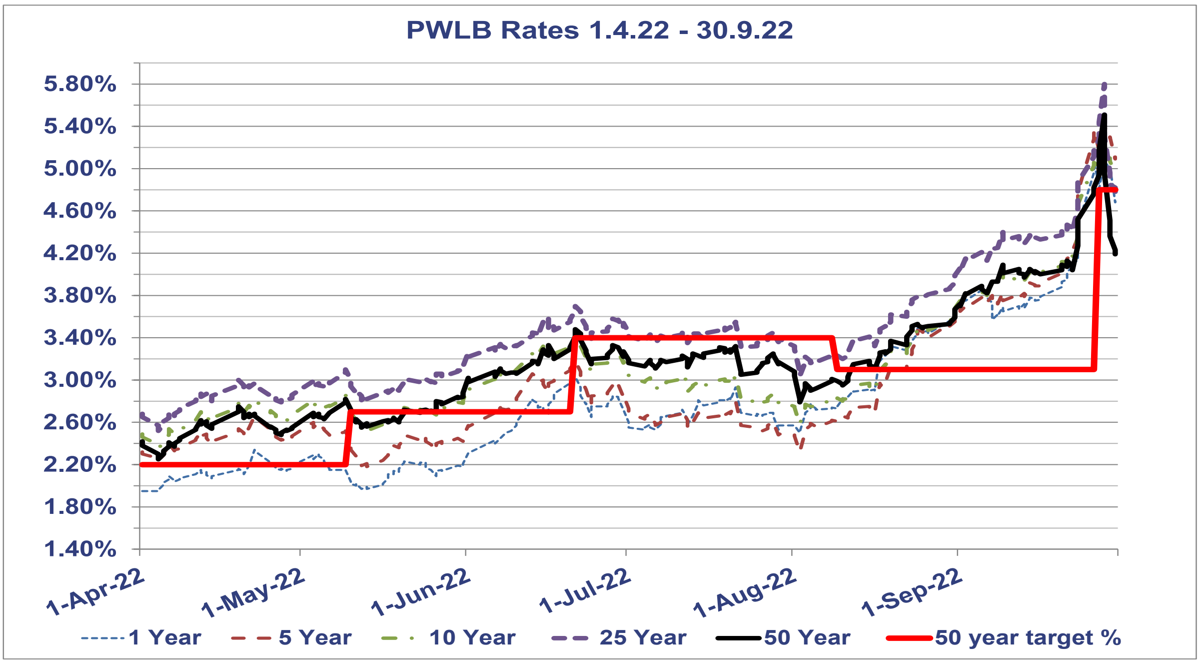
Throughout Q3 Bank Rate increased, finishing the quarter at 2.25% (an increase of 1%). Q4 has seen rates rise to 3.5% in December and the market expects Bank Rate to hit 4.5% by May 2023.

Following a Conservative Party leadership contest, Liz Truss became Prime Minister for a tumultuous seven weeks that ran through September and October. Put simply, the markets did not like the unfunded tax-cutting and heavy spending policies put forward by her Chancellor, Kwasi Kwarteng, and their reign lasted barely seven weeks before being replaced by Prime Minister Rishi Sunak and Chancellor Jeremy Hunt. Their Autumn Statement of 17th November gave rise to a net £55bn fiscal tightening, although much of the "heavy lifting" has been left for the next Parliament to deliver. However, the markets liked what they heard, and UK gilt yields have almost completely reversed the increases seen under the previous tenants of No10/11 Downing Street.

Globally, though, all the major economies are expected to struggle in the near term. The fall below 50 in the composite Purchasing Manager Indices for the UK, US, EZ and China all point to at least one, if not more, quarters of GDP contraction. In November, the MPC projected eight quarters of negative growth for the UK lasting throughout 2023 and 2024, but with Bank Rate set to peak at lower levels than previously priced in by the markets and the fiscal tightening deferred to some extent, it is not clear that things will be as bad as first anticipated by the Bank.

The £ has strengthened of late, recovering from a record low of $1.035, on the Monday following the Truss government's "fiscal event", to $1.22. Notwithstanding the £'s better run of late, 2023 is likely to see a housing correction of some magnitude as fixed-rate mortgages have moved above 5% and affordability has been squeezed despite proposed Stamp Duty cuts remaining in place.

In the table below, the rise in gilt yields, and therein PWLB rates, through the first half of 2022/23 is clear to see.



However, the peak in rates on 28th September as illustrated in the table covering April to September 2022 below, has been followed by the whole curve shifting lower. PWLB rates at the front end of the curve are generally over 1% lower now whilst the 50 years is over 1.75% lower.

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.95%	2.18%	2.36%	2.52%	2.25%
Date	01/04/2022	13/05/2022	04/04/2022	04/04/2022	04/04/2022
High	5.11%	5.44%	5.35%	5.80%	5.51%
Date	28/09/2022	28/09/2022	28/09/2022	28/09/2022	28/09/2022
Average	2.81%	2.92%	3.13%	3.44%	3.17%
Spread	3.16%	3.26%	2.99%	3.28%	3.26%

After a shaky start to the year, the S&P 500 and FTSE 100 have climbed in recent weeks, albeit the former is still 17% down and the FTSE 2% up. The German DAX is 9% down for the year.

CENTRAL BANK CONCERNS – DECEMBER 2022

In December, the Federal Reserve System (FED) decided to push up US rates by 0.5% to a range of 4.25% to 4.5%, whilst the MPC followed by raising Bank Rate from 3% to 3.5%, in line with market expectations. EZ rates have also increased to 2% with further tightening in the pipeline.

Having said that, the sentiment expressed in the press conferences in the US and the UK were very different. In the US, FED Chair, Jerome Powell, stated that rates will be elevated and stay higher for longer than markets had expected. Governor Bailey, here in the UK, said the opposite and explained that the two economies are positioned very differently so you should not, therefore, expect the same policy or messaging.

Regarding UK market expectations, although they now expect Bank Rate to peak within a lower range of 4.5% - 4.75%, caution is advised as the Bank of England Quarterly Monetary Policy Reports have carried a dovish message over the course of the last year, only for the Bank to have to play catch-up as the inflationary data has proven stronger than expected.

In addition, the Bank's central message that GDP will fall for eight quarters starting with Q3 2022 may prove to be a little pessimistic. Ultimately it will not only be inflation data but also employment data that will mostly impact the decision-making process, although any softening in the interest rate outlook in the US may also have an effect.