TREASURY MANAGEMENT STRATEGY STATEMENT, ANNUAL INVESTMENT STRATEGY AND MINIMUM REVENUE PROVISION POLICY STATEMENT 2016/17

1 POLICY STATEMENT

1.1 This report sets out the Council's Treasury Management Strategy for borrowing and investment for 2016/17 and seeks the views of the Review Committee on the approach proposed in this Strategy, before it is presented for approval by Full Council on 23 February 2016.

1.2 The investment policy objective for this Council is the prudent investment of its treasury balances. The Council's investment priorities are security of capital and liquidity of its investments so that funds are available for expenditure when needed.

1.3 Both the Chartered Institute of Public Finance and Accountancy (CIPFA) Code and the Department of Communities and Local Government (DCLG) guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The generation of investment income to support the Council's spending plans is an important, but secondary objective.

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

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

2 REPORTING

2.1 The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of polices, estimates and actuals. These reports are:-

- The Prudential and Treasury Indicators and Treasury Strategy (this report), which 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).

- The Mid Year Treasury Management Report, which will update members with the progress of the capital position, amending prudential indicators as necessary, and whether the Treasury Strategy is delivering its objectives or whether any policies require revision. In addition, the Executive will receive quarterly updates of the capital programme position.

- Annual Strategy report (reported to Council in June). This provides details of actual performance compared to the estimates.

- The above reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken by the Review Committee.

2.2 The Strategy covers:-

Capital Issues

- The capital plans and the prudential indicators;
- The Minimum Revenue Provision (MRP) Strategy;

Treasury Management Issues

- Treasury indicators which will limit the treasury risk and activities of the Council;
- The current treasury position;
- The borrowing strategy;
- Prospects for interest rates;
- Policy on borrowing in advance of need;
- The investment strategy;
- Creditworthiness policy; and
- Policy on use of external service providers.

2.3 These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the Communities and Local Government (CLG) MRP Guidance, the CIPFA Treasury Management Code and the CLG Investment Guidance.

2.4 The CIPFA Code requires the responsible financial officer to ensure that members with responsibility for treasury management receive adequate training in treasury management.

2.5 The Council uses Capita Asset Services "Capita" (formerly Sector Treasury Services) as its external treasury management advisors.

3 CAPITAL PRUDENTIAL INDICATORS FOR 2016/17 TO 2018/19

3.1 The Council's capital expenditure plans are one of the key drivers of treasury management activity. The capital expenditure plans are reflected in prudential indicators, which are designed to assist Members' overview and confirm capital expenditure plans.

3.2 **Capital Expenditure and the Capital Financing Requirement (CFR)** 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. The table below also shows how these plans are being financed and any shortfall that will require borrowing.

£000s	2014/15 Actual	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Opening CFR	**1,061**	**687**	**687**	**687**	**687**
Capital Expenditure	911	3,363	509	446	503
Financed by:					
Capital receipts	688	1,613	71	-	-
Capital grants	223	519	250	250	250
General Fund	374	-	-	-	-
Capital Financing Reserve	-	1,231	188	196	253
Closing CFR	**687**	**687**	**687**	**687**	**687**

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 essentially a measure of the Council's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR. The CFR is reduced by the application of resources such as capital receipts, grants or charges to revenue.

4 MINIMUM REVENUE PROVISION (MRP) POLICY STATEMENT

4.1 The Council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the minimum revenue provision - MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

4.2 CLG Regulations have been issued which require Full Council to approve an MRP Statement in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision.

4.3 There is an historic adjustment arising from the former Housing Revenue Account which results in a negative CFR for the purposes of the MRP calculation. No MRP provision is envisaged in the current capital programme.

5 OTHER INDICATORS

The Use of the Council's Resources and the Investment Position

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 on-going 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.

Year End Resources £000s	2014/15 Actual	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Fund balances / reserves	2,605	2,525	2,500	2,500	2,500
Capital receipts	1,613	-	71	-	-
Total core funds	**4,218**	**2,525**	**2,571**	**2,500**	**2,500**
Expected investments	**1,508**	**-**	**1,000**	**2,000**	**2,500**

Affordability Prudential Indicators

5.1 The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans.

5.2 The indicators are designed to support and record local decision making in a manner that is publicly accountable and are not designed to be comparative performance indicators to other organisations. There are no recommended limits or values for the indicators.

5.3 These provide an indication of the impact of the capital investment plans on the Council's overall finances. Members are asked to approve the following indicators.

5.4 **Ratio of financing costs to net revenue stream.** This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

%	2014/15 Actual	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Ratio of Financing Costs to Net Revenue Stream	(0.25%)	(0.37%)	(0.96%)	(1.26%)	(1.51%)

5.5 **Incremental impact of capital investment decisions on the Band D Council Tax.** If the capital programme is to be funded through revenue

(Council Tax) this indicator identifies the revenue costs associated with proposed changes to the three year capital programme. The assumptions are based on the budget.

£000's	2014/15 Actual	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Capital Expenditure	1,262	3,958	509	446	503
Incremental impact of capital investment	(1,316)	2,696	(3,449)	(63)	57
Council Tax Income	6,216	6,317	6,511	6,637	6,765
Council Tax – band D	(0.21)	0.43	(0.53)	(0.01)	0.01

6 BORROWING

6.1 At present, there are no plans to borrow to finance new capital expenditure in the current medium term resource strategy.

6.2 Borrowing could be used for "invest to save" projects providing the cost of servicing the debt is contained within the revenue savings/income the project generates, the project generates a positive net present value and the payback period for invest to save projects should be shorter than the life of the asset.

6.3 Borrowing would add pressure on the revenue budget as MRP and interest would become payable. The capacity to make these payments would need to be identified in advance, namely the further efficiency savings generated by the investment in the assets.

6.4 The following issues will be considered prior to undertaking any external borrowing:

– Affordability

– Maturity profile of existing debt

– Interest rate and refinancing risk

– Borrowing source including Internal

6.5 Sources of Borrowing. In conjunction with advice from its treasury advisor, the Council will keep under review the following external borrowing sources:-

– Public Works Loan Board (PWLB) (or its replacement)

– any institution approved for investments

– any other bank or building society authorised to operate in the UK

– UK public and private sector pension funds (except for Essex Pension Fund)

– Capital market bond investors

– Local Capital Finance Company and other special purpose companies created to enable local authority bond issues

– Capital markets (stock issues, commercial paper and bills)

Treasury Indicators: Limits to Borrowing Activity

6.6 **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, limited to 85% of the closing CFR.

6.7 The Operational Boundary reflects the most likely (not worst case scenario), and should be a prudent view of the level of gross external indebtedness (borrowing + long term liabilities). It is regularly monitored and any breaches would be investigated promptly.

6.8 **The Authorised Limit for external debt**. A further key prudential indicator represents a control on the maximum level of borrowing. This represents the upper limit beyond which external debt is prohibited, and this limit can only be revised by Full Council. It reflects the level of external debt which could be afforded in the short term, but is not sustainable in the longer term and provides headroom over and above the operational boundary which should be sufficient for unusual cash limits.

6.9 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.

6.10 The Authorised and Operational limits are based on the assumption that there will be long term borrowing to fund capital expenditure and that borrowing will be to fund long and short term cash flow requirements. The limits include balance sheet liabilities such as finance leases and creditors.

Authorised limit £000s	2015/16 Estimate	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
Debt	700	700	700	700

Treasury Management Limits on Activity

6.11 There are debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs / improve performance.

6.12 The limit indicators are shown separately for borrowing and investments. Fixed rates for investments or borrowing for a period of less than one year are treated as variable by the Prudential Code.

Interest rate Exposures %	2016/17	2017/18	2018/19
	Upper	**Upper**	**Upper**
Limits on fixed interest rates:			
Borrowing	75	75	75
Investments	25	25	25
Limits on variable interest rates:			
Borrowing	25	25	25
Investment	75	75	75

7 BORROWING IN ADVANCE OF NEED

7.1 The Council has some flexibility to borrow funds for use in future years where a future need for borrowing has been identified. Any decision to borrow in advance will be considered carefully to ensure value for money can be demonstrated and that the Council can ensure the security of such funds.

7.2 The Section 151 Officer may do this under delegated power where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or meet budgetary constraints. Whilst the Section 151 Officer will adopt a cautious approach to any such borrowing, where there is a clear business case for doing so borrowing may be undertaken to fund the approved capital programme or to fund future debt maturities.

7.3 In determining whether borrowing will be undertaken in advance of need the Council will:-

- Ensure revenue liabilities created and the implications for the future plans and budgets have been considered;

- Consider economic and market factors that might influence the manner and timing of any decision to borrow;

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

- Consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use

7.4 Borrowing in advance will be made within the constraints that: -

- It will be limited to no more than 50% of any expected increase in borrowing need (CFR) over the three year planning period; and

- It would not look to borrow more than 2 years in advance of need.

7.5 Risks associated with any advance borrowing activity will be subject to appraisal in advance and subsequent reporting through the mid-year or annual reporting mechanism. It is unlikely that the Council will require any borrowing in advance of need.

8 ANNUAL INVESTMENT STRATEGY

8.1 Following consultation with the Council’s Treasury Management advisers, the Council would like to consider a more diversified investment portfolio to the traditional cash deposits, as these generally as a rule of thumb provide increased returns and minimise risk by diversifying the Council’s investment.

8.2 In order to diversify an investment portfolio largely invested in cash, investments will be placed with a range of approved investment counterparties in order to achieve a diversified portfolio of prudent counterparties, investment periods and rates of return. Maximum investment levels with each counterparty will be set; this is to ensure prudent diversification is achieved and the Council can remain confident that any cash invested will not be required at short notice, or within a short time-span.

- Term and call deposits with banks and building societies

- Term deposits, call deposits and bonds with other UK local authorities

- Investments with Registered Providers (former Registered Social Landlords)

- Investments in property based funds (indirect property investment).

- Certificates of deposit with banks and building societies

- UK Government Gilts

- UK Government Treasury Bills (T-Bills)

- UK Government Debt Management Account

- Deposit Facility (DMADF)

– Bonds issued by Multilateral Development

– Banks/Supranational banks

– Commercial Paper

– Corporate Bonds

– Standard Money Market Funds and Collective Investment

8.3 Standard Money Market Funds (MMF) – these offer safety, security, liquidity and yield. Whilst not a replacement for all other kinds of investments; money market funds are suitable for managing short term funds. The Council is permitted to use these funds and only deals with Counterparties on the approved list and must limit the total investment to the amount on the approved counterparty list.

8.4 Money market funds (MMFs) will be used as they provide good diversification. The Council will also seek to manage operational risk by using at least two MMFs. The Authority will also restrict its exposure to MMFs with lower levels of funds under management and will not exceed 0.5% of the net asset value of the MMF.

9 CREDIT RATINGS

9.1 The Council uses long-term credit ratings from the three main rating agencies: Fitch Ratings, Moody's Investors Service and Standard & Poor's Financial Services to assess the risk of investment default. The lowest available counterparty credit rating will be used to determine credit quality, unless an investment-specific rating is available. Credit ratings are obtained and monitored by the Council's treasury advisor, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:-

– no new investments will be made,

– any existing investments that can be recalled or sold at no cost will be, and

– full consideration will be given to the recall or sale of all other existing investments with the affected counterparty

9.2 In order to minimise risk and maintain diversity, the Council will have a limit on the amount which can be placed in institution. This limit will also apply to groups. Because the value of investments held at any time can vary by up to £6m, depending on cash flow requirements, it is not considered practical to have a percentage limit. The limits will be linked to duration and be as follows:-

Capita Colour Coding	Maximum Duration	Maximum Investment
No colour	Not to be used	0
Green	100 days	£6m
Red	6 months 100 days	£3m £6m
Orange	1 year 6 months 100 days	£1m £3m £6m
Blue	1 year	£4m
Purple	2 years 100 days	£3m £6m

Organisation	Maximum Duration	Maximum Investment
Debt Management Office (Government Body)	3 months	£14m
Lloyds Bank current account The Council's main banker	On call (can be withdrawn immediately)	£3m
Money Market Funds – AAA long-term credit rating	On call (can be withdrawn immediately)	£3m per fund
Certificates of Deposit and Treasury Bills.	Will follow the Capita Colour Coding limits as per the above table.	Will follow the Capita Colour Coding limits as per the above table.
Local Authorities	1 year	£3m
Local Capital Finance Company Limited	10 years	£10,000 & 0.6% of borrowing

9.3 If in the case of a decision to recall or sell an investment at a cost which is over the approved virement limits, the Council's urgent action procedure in its Constitution would be invoked by officers.

9.4 Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "negative rating watch" or "negative credit watch") so that it may fall below the approved rating criteria, then only investments that can be withdrawn in a timely manner will be made with that organisation until the outcome of the review is announced, any further investment with the counterparty would be suspended until its credit rating came back in line with Capita's suggested colour coding. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating. Any counterparty downgrades must be included in the monitoring reports sent to the Members of the Treasury Management Task & Finish Group.

10 INVESTMENT STRATEGY

Country Limits

10.1 The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA+ from Fitch Ratings (or equivalent from other agencies if Fitch does not provide).

10.2 Countries other than the UK will be subject to a £3m investment limit for duration of up to one year, subject to Section 151Officer authorisation.

Investment Management

10.3 The Council does not use a fund manager and funds are managed in-house. Investments will accordingly be made with reference to the core balances and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

10.4 **Investment returns expectations.** Bank Rate is forecast to remain unchanged at 0.5% before starting to rise from quarter 2 of 2016/17. Bank Rate forecasts for financial year ends (March) are:-

- 2016/ 2017 1.00%
- 2017/ 2018 1.50%
- 2018/ 2019 2.00%

10.5 There are upside risks to these forecasts (i.e. start of increases in Bank Rate occur sooner) if economic growth strengthens. However, should the pace of growth fall back there could be downside risk, particularly if Bank of England forecasts for unemployment prove too optimistic.

10.6 The Council will avoid locking into longer term deals while investment rates are down at historically low levels unless attractive rates are available with counterparties of particularly high creditworthiness which make longer term deals worthwhile and within the risk parameters set by this Council.

10.7 It is expected that this authority will have sufficient funds to invest that will realise a return on investments c£80,000 - £100,000 for financial year 2016/17.

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

11 LIQUIDITY RISK MANAGEMENT

11.1 This Council will ensure it has adequate though not excessive cash resources, borrowing arrangements, overdraft or standby facilities to enable it at all times to have sufficient liquidity in its investments, taking into account known and potential cash-flow requirements and the level of funds available to it which are necessary for the achievement of its business/service objectives.

11.2 Giving due consideration to the Council's level of balances over the next year, the need for liquidity, its spending commitments and provisioning for contingencies, it is considered very unlikely that the Council will have cash balances to invest other than on a temporary basis. For this reason, no cash will be held on term deposit maturities in excess of one year.

12 CASH AND CASH FLOW MANAGEMENT

12.1 The optimum amount of cash held by the council will depend on working capital needs. The overall amount of working capital needed can be estimated from forecast activity and the cash conversion cycle. Based on 2015/16 activity and 2016/17 budgets average working capital requirements are estimated to be £3.8m for the Council (including 10% variation contingency).

12.2 The objective should be to keep low interest cash balances at an optimum and maximise temporary investments. There is likely to be a difference between forecast activity and actual activity and therefore working capital will need to be subject to regular review and report to Treasury Committee/Full Council in the light of changing levels of activity.

12.3 The Council will prepare reports which include cash flow forecasts and actuals on a 12 month rolling basis so as to be able to determine:

- whether minimum acceptable levels of cash balances plus short-term investments might be (or have been) breached
- the adequacy (or otherwise) of standby/overdraft facilities or contingency arrangements
- the optimum arrangements to be made for investing and managing surplus cash.

13 POLICY ON THE USE OF EXTERNAL SERVICE PROVIDERS

13.1 The Council uses Capita Asset Services as its external treasury management advisers.

13.2 The Council recognises that responsibility for treasury management decisions remains with the Council at all times and will ensure that undue reliance is not placed upon our external service providers.

13.3 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. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

14 SCHEME OF DELEGATION

14.1 Under the Code, the Council is required to specify its Scheme of Delegation for Treasury Management and the responsibilities of the Section 151 Officer, and this is shown below:-

(i) Council

- Receiving and reviewing reports on treasury management policies, practices and activities.
- Approval of annual strategy (including the limits and parameters for investment and borrowing activity).
- Budget consideration and approval.
- Receiving the end of year report on treasury management.

(ii) Review Committee Treasury Management Task & Finish Group

- Scrutiny of the three main treasury reports, before recommendation to Council or Executive.

(iii) Executive

- Approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices.
- Approval of the division of responsibilities.
- Receiving and reviewing regular monitoring reports and acting on recommendations.

(iv) Audit Committee

- Reviewing the treasury management policy and procedures and making recommendations to the responsible body.

(v) Section 151 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.
- Ensuring the adequacy of internal audit, and liaising with external audit.

- Approving the selection of external service providers and agreeing terms of appointment.

15 RISK IMPLICATIONS

15.1 As a debt free authority with a medium term resource strategy identifying the potential for investment income the Council's highest priority in its treasury management function is the security of those investments in accordance with the priorities set out in the CIPFA Code. Where investment returns are short term in nature they should be used to fund one-off expenditure or capital investment and not to balance the base revenue budget.

15.2 Sums are invested with a diversified range of counter parties using a wide range of instruments consistent with avoiding the risk of the capital sum being diminished through movements in prices.

15.3 This means that the Council whilst fundamentally risk adverse, will accept some modest degree of risk. It will consider first the range of risks and secondly how prudently to manage those different risks. It will ensure that priority is given to security and liquidity when investing funds before seeking to optimise yield. The use of different investment instruments and diversification of high credit quality counter parties along with country, sector and group limits, as set out in the Strategy, enables the Council to minimise the nature and extent of the different risks.

16 RESOURCE IMPLICATIONS

16.1 All interest paid and received is accounted for within the General Fund. The amount of income generated is dependent upon interest rates and level of balances.

17 LEGAL IMPLICATIONS

17.1 This strategy complies with the statutory requirements set out in the Local Government Act 2003 and associated guidance and regulations.

18 RECOMMENDATION

18.1 It is proposed that the Committee **RESOLVES**

(1) To note the Treasury Management Strategy Statement and Annual Investment Strategy including the investments instruments, indicators, limits and delegations contained within the report.

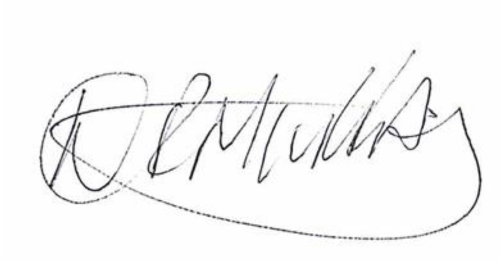
(2) To note the Capital Expenditure Forecasts.

(3) To note the Minimum Revenue Provision (MRP) policy for 2016/17.

(4) To note the Authorised Limit and Operational Boundary for external debt as laid down in the report.

(5) To identify any issues on this topic for further consideration and discussion by the Committee.

(6) Recommend the contents of this report to Full Council.



Denise Murray

Section 151 Officer

Background Papers:-

None

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