



ADUR & WORTHING  
COUNCILS

Joint Governance Committee  
25 January 2022  
Agenda Item 9

Joint Strategic Committee  
8 February 2022  
Agenda Item 6

Key Decision : No  
Ward(s) Affected: All

## **JOINT TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2022/23 to 2024/25, ADUR DISTRICT COUNCIL AND WORTHING BOROUGH COUNCIL**

### **REPORT BY THE DIRECTOR FOR DIGITAL, SUSTAINABILITY AND RESOURCES**

#### **EXECUTIVE SUMMARY**

##### **1. PURPOSE**

- 1.1 This report asks Members to approve and adopt the contents of the Treasury Management Strategy Statement and Annual Investment Strategy for 2022/23 to 2024/25 for Adur and Worthing Councils, as required by regulations issued under the Local Government Act 2003.

##### **2. RECOMMENDATIONS**

- 2.1 The Joint Governance Committee is recommended to:

- i) Note the report (including the Prudential Indicators and Limits, and MRP Statements) for 2022/23 to 2024/25
- ii) Refer any comments or suggestions to the next meeting of the Joint Strategic Committee on 8 February 2022.

- 2.2 The Joint Strategic Committee is recommended to:

- i) Approve and adopt the TMSS and AIS for 2022/23 to 2024/25, incorporating the Prudential Indicators and Limits, and MRP Statements
- ii) Forward the Prudential Indicators and Limits, and MRP Statements of the report for approval by Worthing Council at its meeting on 22 February 2022, and by Adur Council at its meeting on 24 February 2022.

### **3. INTRODUCTION**

#### **3.1 Background**

The Councils are required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in high quality counterparties or instruments commensurate with the Councils' low risk appetite, providing adequate liquidity initially, before considering investment return. This is consistent with national guidance which promotes security and liquidity above yield.

The second main function of the treasury management service is the funding of the Councils' capital plans. These capital plans provide a guide to the borrowing needs of the Councils, essentially the longer term cash flow planning, to ensure that the Councils can meet their 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 the Councils' risk or cost objectives.

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

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.”*

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

#### **3.2 Reporting requirements**

##### **3.2.1 Capital Strategy**

The CIPFA 2017 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 this capital strategy is to ensure that all elected members on the full Councils fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

### 3.2.2 Treasury Management Reporting

The Councils are required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

**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).

**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 noting whether any policies require revision.

**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.

**Scrutiny** - The above reports are required to be scrutinised by the Joint Governance Committee (JGC) which may make recommendations to the Joint Strategic Committee (JSC) regarding any aspects of Treasury Management policy and practices it considers appropriate in fulfilment of its scrutiny role. Such recommendations as may be made shall be incorporated within the above named reports and submitted to meetings of the JSC for consideration as soon after the meetings of the JGC as practically possible. The reports are approved by the JSC and recommended to the Councils for approval.

### 3.3 Treasury Management Strategy for 2022/23

The strategy for 2022/23 covers two main areas:

#### **Capital issues**

- the capital expenditure plans and the associated prudential indicators;
- the minimum revenue provision (MRP) policy.

### **Treasury management**

- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Councils;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- the policy on use of external service providers

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

### **3.4 Training**

The CIPFA 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. Following the Covid-19 pandemic, member training will be provided as soon as possible.

The training needs of treasury management officers are periodically reviewed and officers attend courses provided by appropriate trainers such as Link and CIPFA.

### **3.5 Treasury management consultants**

The Councils use Link Group, Treasury Solutions as the external treasury management advisors.

The Councils recognise that responsibility for treasury management decisions remains with the organisations at all times and will ensure that undue reliance is not placed upon our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

They also recognise that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Councils 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.

## **4. THE CAPITAL PRUDENTIAL INDICATORS 2022/23 – 2024/25**

The Councils' 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.

#### 4.1 Capital expenditure and financing

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

The tables below summarise the capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a financing or borrowing need.

##### ADUR DISTRICT COUNCIL

Capital expenditure	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
	£m	£m	£m	£m	£m
Non-HRA	12.512	10.270	52.997	2.473	1.862
HRA	5.186	25.666	19.513	5.600	5.600
<b>TOTAL</b>	<b>17.698</b>	<b>35.936</b>	<b>72.510</b>	<b>8.073</b>	<b>7.462</b>
<b>Financed by:</b>					
Capital receipts	1.282	1.519	0.200	0.100	0.121
Capital grants and contributions	10.722	4.363	1.546	0.471	0.462
Revenue Reserves & contributions	4.216	6.474	5.976	6.709	6.739
<b>Net financing need for the year</b>	<b>1.478</b>	<b>23.580</b>	<b>64.788</b>	<b>0.793</b>	<b>0.140</b>

##### WORTHING BOROUGH COUNCIL

Capital expenditure	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
	£m	£m	£m	£m	£m
Non-HRA	17.744	52.068	74.896	3.811	3.332
<b>TOTAL</b>	<b>17.744</b>	<b>52.068</b>	<b>74.896</b>	<b>3.811</b>	<b>3.332</b>
<b>Financed by:</b>					
Capital receipts	1.211	0.184	0.918	0.000	0.089
Capital grants and contributions	7.328	6.541	6.385	0.888	0.856
Revenue Reserves & contributions	2.361	1.979	2.398	3.761	3.997
<b>Net financing need for the year</b>	<b>6.844</b>	<b>43.364</b>	<b>65.195</b>	<b>(0.837)</b>	<b>(1.611)</b>

## 4.2 The Councils' borrowing need (the Capital Financing Requirement)

The second prudential indicator is the Councils' Capital Financing Requirement (CFR). The CFR is simply the total historical outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Councils' indebtedness and so their underlying borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

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.

The CFR includes any other long term liabilities (e.g. finance leases). Whilst these increase the CFR, and therefore the Councils' borrowing requirement, these types of schemes include a borrowing facility and so the Councils are not required to separately borrow for these schemes. The Councils currently do not have any such schemes within the CFR. The Councils are asked to approve the CFR projections below:

### ADUR DISTRICT COUNCIL

Capital Financing Requirement (£m)	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
CFR – non-HRA	27.278	33.958	84.082	84.146	83.581
CFR - HRA	61.591	79.713	95.226	96.826	98.426
CFR – strategic	79.627	78.405	77.556	76.685	75.790
<b>Total CFR</b>	<b>168.496</b>	<b>192.076</b>	<b>256.864</b>	<b>257.657</b>	<b>257.797</b>
<b>Movement in CFR</b>	1.478	23.580	64.788	0.793	0.140
<b>Movement in CFR represented by</b>					
Financing need for the year	3.700	25.894	66.785	3.532	2.930
<b>Less: MRP/VRP and other financing movements</b>	(2.222)	(2.314)	(1.997)	(2.739)	(2.790)
<b>Movement in CFR</b>	<b>1.478</b>	<b>23.580</b>	<b>64.788</b>	<b>0.793</b>	<b>0.140</b>

## WORTHING BOROUGH COUNCIL

Capital Financing Requirement (£m)	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
CFR – non-HRA	65.338	109.444	175.400	175.344	174.534
CFR - strategic	70.294	69.552	68.791	68.010	67.209
<b>Total CFR</b>	<b>135.632</b>	<b>178.996</b>	<b>244.191</b>	<b>243.354</b>	<b>241.743</b>
<b>Movement in CFR</b>	<b>6.844</b>	<b>43.364</b>	<b>65.195</b>	<b>(0.837)</b>	<b>(1.611)</b>
<b>Movement in CFR represented by</b>					
Net financing need for the year (above)	9.054	44.900	67.364	2.757	2.220
<b>Less: MRP/VRP and other financing movements</b>	<b>(2.210)</b>	<b>(1.536)</b>	<b>(2.169)</b>	<b>(3.594)</b>	<b>(3.831)</b>
<b>Movement in CFR</b>	<b>6.844</b>	<b>43.364</b>	<b>65.195</b>	<b>(0.837)</b>	<b>(1.611)</b>

### 4.3 Minimum revenue provision (MRP) policy statement

The Councils are 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 they are also allowed to undertake additional voluntary payments (voluntary revenue provision - VRP).

DLUHC regulations have been issued which require the full Councils 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.

For both Councils, the MRP relating to built assets under construction will be set aside once the asset is completed. If any finance leases are entered into, the repayments are applied as MRP.

The Councils are recommended to approve the following MRP Statements:

#### ADUR DISTRICT COUNCIL

For Adur District Council it was approved by the Joint Strategic Committee on 2nd June 2016 that for borrowing incurred before 1st April 2008, the MRP will be set aside in equal instalments over the life of the associated debt.

#### 4.3.1 General Fund

For non-HRA capital expenditure after 1st April 2008 the MRP will be calculated as the annual amount required to repay borrowing based on the annuity method: equal annual payments of principal and interest are calculated, with the interest element reducing and the principal element

increasing over the life of the asset as the principal is repaid. The interest is based on the rate available to the Council at the beginning of the year in which payments start and the MRP is calculated as the amount of principal, so that by the end of the asset's estimated life the principal is fully repaid (the Asset Life Method). The option remains to use additional revenue contributions or capital receipts to repay debt earlier.

An exception was agreed in the 2015/16 Treasury Management Strategy Statement: the Chief Financial Officer has discretion to defer MRP relating to debt arising from loans to Registered Social Landlords (RSLs) to match the profile of debt repayments from the RSL and other public bodies. RSLs normally prefer a maturity type loan as it matches the onset of income streams emanating from capital investment with the timing of the principal debt repayment. The deferral of MRP to the maturity date would therefore mean that MRP is matched at the same point as the debt is repaid, and is therefore cash (and revenue cost) neutral to the Council.

If concerns arise about the ability of the borrower to repay the loan, the Chief Financial Officer will use the approved discretion to make MRP as a "prudent provision" from the earliest point to ensure that sufficient funds are set aside from revenue to repay the debt at maturity if the RSL defaults.

It is proposed to use the same policy for 2022/23.

#### 4.3.2 **Housing Revenue Account**

Unlike the General Fund, the HRA is not required to set aside funds to repay debt. There is a requirement for a charge for depreciation to be made but there are transitional arrangements in place. The Council's MRP policy previously applied the financially prudent option of voluntary MRP for the repayment of HRA debt, to facilitate new borrowing in future for capital investment. However in order to provide additional capital funding to address the maintenance backlog identified by the condition survey, the payment of voluntary MRP was suspended for a period of 9 years from 2017/18 whilst the Council invests in its current housing stock and manages the impact of rent limitation.

### **WORTHING BOROUGH COUNCIL**

4.3.3 Worthing had no debt prior to 1 April 2008. Worthing applies the same MRP policy as Adur for capital expenditure funded from borrowing from 1 April 2008. Worthing also has discretion in the application of MRP in respect of capital loans to approved Counterparties (currently Worthing Homes and GB Met College).

4.3.4 In addition to the above policy, it is also recommended that where the Council purchases a property to facilitate a development whether via a Compulsory Purchase Order or via a negotiated arrangement with the intention of disposing of the property to a development partner, no MRP shall be provided for the first three years. Any capital receipt received for the land shall be used to repay the associated debt. This change to the policy was initially approved

by Council in July 2021.

4.3.5 It is proposed to retain this policy for 2022/23.

#### **ADUR and WORTHING COUNCILS - VOLUNTARY REVENUE PROVISION**

4.3.4 **MRP Overpayments** – A change introduced by the revised DLUHC MRP Guidance was the allowance that any charges made over the statutory MRP, which are designated as voluntary revenue provision or overpayments, can, if needed, be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayments made each year. Up until the 31<sup>st</sup> March 2022 Adur has a net VRP overpayment of £30k and Worthing has a cumulative net £470k VRP overpayment which will be reclaimed over the five years following each voluntary overpayment.

### **5. BORROWING**

The capital expenditure plans set out above provide details of the service activity of the Councils. The treasury management function ensures that the Councils' cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Councils' capital strategy. This will involve 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.

#### **5.1 Current portfolio position**

The Councils' treasury portfolio positions at 31st March 2021 and at 31st December 2021 are shown below.

## Adur District Council

	Principal at 31.03.21 £m	Actual 31.03.2021 %	Principal at 31.12.21 £m	Actual 31.12.2021 %
<b>External Borrowing</b>				
PWLB	(136.052)	86%	(135.018)	85%
Other Borrowing	(22.884)	14%	(23.066)	15%
Finance lease	(0.000)		(0.000)	
<b>TOTAL BORROWING</b>	<b>(158.936)</b>	100%	<b>(158.084)</b>	100%
<b>Treasury Investments:</b>				
Local Authority Property Fund	2.708	23%	3.043	13%
<b>In-house:</b>				
Banks	6.000	51%	15.810	66%
Building societies	0.000	0%	2.000	8%
Bonds	0.030	1%	0.025	0%
Local authorities	0.000	0%	0.000	0%
Money market funds	3.000	25%	3.010	13%
<b>TOTAL INVESTMENTS</b>	<b>11.738</b>	100%	<b>23.888</b>	100%
<b>NET DEBT</b>	<b>(147.198)</b>		<b>(134.196)</b>	

## Worthing Borough Council

	Principal at 31.03.21 £m	Actual 31.03.2021 %	Principal at 31.12.21 £m	Actual 31.12.2021 %
<b>External Borrowing</b>				
PWLB	(108.725)	79%	(111.439)	85%
Other Borrowing	(29.000)	21%	(37.000)	15%
Finance lease	(0.000)		(0.000)	
<b>TOTAL BORROWING</b>	<b>(137.725)</b>	100%	<b>(148.439)</b>	100%
<b>Treasury Investments:</b>				
Local Authority Property Fund	1.354	14%	1.522	4%
<b>In-house:</b>				
Banks	3.010	30%	17.160	44%
Government DMO	0.000	0%	4.000	10%
Building societies	0.000	0%	2.000	5%
Bonds	0.050	1%	0.050	0%
Local authorities	2.500	25%	2.500	6%
Money market funds	3.000	30%	12.000	31%
<b>TOTAL INVESTMENTS</b>	<b>9.914</b>	100%	<b>39.232</b>	100%
<b>NET DEBT</b>	<b>(127.811)</b>		<b>(109.207)</b>	

Worthing Borough Council has also made two loans which are categorised as

capital rather than treasury investments:

- a £10m loan to Worthing Homes
- a £5m repayment loan to GBMet College, with £4.737m remaining

The Councils' forward projections for borrowing are summarised below. The tables show the actual external debt against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

### ADUR DISTRICT COUNCIL

Adur District Council External Debt £m	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Debt at 1 April	(161.802)	(158.936)	(182.516)	(247.304)	(248.097)
Expected change in Debt	2.866	(23.580)	(64.788)	(0.793)	( 0.140)
Other long-term liabilities (OLTL)	0.000	0.000	0.000	0.000	0.000
Actual gross debt at 31 March	(158.936)	(182.516)	(247.304)	(248.097)	(248.237)
The Capital Financing Requirement	168.496	192.076	256.864	257.657	257.797
Under/(over) borrowing	9.560	9.560	9.560	9.560	9.560

Within the above figures the level of debt relating to commercial property is:

Adur District Council	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
<b>External Debt for commercial activities / non-financial investments</b>					
Actual debt at 31 March £m	(79.627)	(78.405)	(77.556)	(76.685)	(75.790)
Percentage of total external debt %	50%	43%	31%	31%	31%

### Worthing Borough Council

Worthing BC External Debt £m	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Debt at 1 April	(128.071)	(137.725)	(177.077)	(242.272)	(241.435)
Expected change in Debt	(9.654)	(39.352)	(65.195)	0.837	1.611
Other long-term liabilities (OLTL)	0.000	0.000	0.000	0.000	0.000
Actual gross debt at 31 March	(137.725)	(177.077)	(242.272)	(241.435)	(239.824)
The Capital Financing Requirement	135.632	178.996	244.191	243.354	241.743
Under/(over) borrowing	(2.093)	1.919	1.919	1.919	1.919

Within the above figures the level of debt relating to commercial property is:

Worthing B C	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
<b>External Debt for commercial activities / non-financial investments</b>					
Actual debt at 31 March £m	(70.294)	(69.552)	(68.791)	(68.010)	(67.209)
Percentage of total external debt %	51%	39%	28%	28%	28%

Within the range of prudential indicators there are a number of key indicators to ensure that the Councils operate their activities within well-defined limits. One of these is that the Councils need to ensure that their 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 2022/23 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.

The Chief Financial Officer reports that the Councils 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.

## 5.2 Treasury Indicators: limits to borrowing activity

**The operational boundary** - This is the limit 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.

### ADUR DISTRICT COUNCIL

Operational boundary £m	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Debt	185.0	248.0	249.0	249.0
Other long term liabilities	1.0	1.0	1.0	1.0
<b>Total</b>	<b>186.0</b>	<b>249.0</b>	<b>250.0</b>	<b>250.0</b>

### WORTHING BOROUGH COUNCIL

Operational boundary £m	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Debt re Worthing Homes	10.0	10.0	10.0	10.0
Debt re GB Met	5.0	4.5	4.3	4.0
Other Debt	167.0	229.5	229.5	227.0
Other long term liabilities	1.0	1.0	1.0	1.0
<b>Total</b>	<b>183.0</b>	<b>245.0</b>	<b>244.8</b>	<b>242.0</b>

**The authorised limit for external debt** - This is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Councils. 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.

1. 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.
2. The Councils are asked to approve the following authorised limits:

#### ADUR DISTRICT COUNCIL

Authorised limit £m	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Debt	190.0	252.0	253.0	253.0
Other long term liabilities	1.0	1.0	1.0	1.0
<b>Total</b>	<b>191.0</b>	<b>253.0</b>	<b>254.0</b>	<b>254.0</b>

#### WORTHING BOROUGH COUNCIL

Authorised limit £m	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Debt re Worthing Homes	10.0	10.0	10.0	10.0
Debt re GB Met	5.0	4.5	4.3	4.0
Other Debt	172.0	233.0	233.0	230.0
Other long term liabilities	1.0	1.0	1.0	1.0
<b>Total</b>	<b>188.0</b>	<b>248.5</b>	<b>248.3</b>	<b>245.0</b>

### 5.3 Prospects for interest rates

The Councils have appointed Link Group as their treasury advisor and part of their service is to assist the Councils to formulate a view on interest rates. Link provided the following forecasts on 20th December 2021. These are forecasts for certainty rates, gilt yields plus 80bps:

Link Group Interest Rate View 20.12.21														
	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
BANK RATE	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25
3 month ave earnings	0.20	0.30	0.50	0.50	0.60	0.70	0.80	0.90	0.90	1.00	1.00	1.00	1.00	1.00
6 month ave earnings	0.40	0.50	0.60	0.60	0.70	0.80	0.90	1.00	1.00	1.10	1.10	1.10	1.10	1.10
12 month ave earnings	0.70	0.70	0.70	0.70	0.80	0.90	1.00	1.10	1.10	1.20	1.20	1.20	1.20	1.20
5 yr PWLB	1.40	1.50	1.50	1.60	1.60	1.70	1.80	1.80	1.80	1.90	1.90	1.90	2.00	2.00
10 yr PWLB	1.60	1.70	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10	2.20	2.30
25 yr PWLB	1.80	1.90	2.00	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.40	2.40	2.50	2.50
50 yr PWLB	1.50	1.70	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.20	2.20	2.30	2.30

Over the last two years, the coronavirus outbreak has done huge economic damage to the UK and to other economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16<sup>th</sup> December 2021.

As shown in the forecast table above, the forecast for Bank Rate now includes four increases, one in December 2021 to 0.25%, then quarter 2 of 2022 to 0.50%, quarter 1 of 2023 to 0.75%, quarter 1 of 2024 to 1.00% and, finally, one in quarter 1 of 2025 to 1.25%.

Additional information about interest rates and the risks to the forecasts are contained in Appendix E.

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

While the Councils will not be able to avoid borrowing to finance new capital expenditure and to replace maturing debt, there will be a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.

#### 5.4 **Borrowing Strategy**

The Councils are both currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt, as cash supporting the Councils' reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are currently low and counterparty risk is still an issue that needs to be considered.

Against this background and the risks within the economic forecast, caution will be adopted with the 2022/23 treasury operations. The Chief Financial Officer 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 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.*

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

- 5.5 Both Councils will refer in the first instance to the Public Works Loan Board (PWLB) for sourcing their borrowing needs, given that they are eligible to access the PWLB “Certainty” rate of interest, being 20 basis points below the normal prevailing PWLB rates. However, borrowing from other sources, including other Local Authorities and the Local Government Association Municipal Bonds Agency, may from time to time offer options to borrow more cheaply than from the PWLB, and therefore will be considered.

Where appropriate, the Councils will investigate the possibility of using “ethical” or “green” borrowing options eg “green bonds.” Such borrowing is usually only available for significant amounts e.g. over £20m and takes time to arrange because the lender and the Council needs to undertake due diligence. PWLB rates have now been reduced meaning that other options are less likely to be economically viable. Local Climate Bonds may offer another alternative for funding carbon reduction projects.

Given the expected under borrowing position of the Councils, the borrowing strategy will give consideration to the most appropriate sources of funding from the following list:

- i) Internal borrowing, by running down cash balances and foregoing interest earned at historically low rates, as this is the cheapest form of borrowing;
  - ii) Weighing the short term advantage of internal borrowing against potential long term borrowing costs, in view of the overall forecast for long term borrowing rates to increase over the next few years;
  - iii) PWLB fixed rate loans for up to 50 years;
  - iv) Long term fixed rate market loans at rates significantly below PWLB rates for the equivalent maturity period (where available) and to maintaining an appropriate balance between PWLB, market debt and loans from other councils in the debt portfolio;
  - v) PWLB borrowing for periods under 5 years 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 concentration in longer dated debt.
  - vi) Short term loans from other Councils where appropriate;
  - vii) Other forms of borrowing where appropriate eg green bonds or the Municipal Bonds Agency where these offer better value than the PWLB
- 5.6 Preference may be given to PWLB borrowing by annuity and EIP loans instead of maturity loans, as this may result in lower interest payments over the life of the loans. However debt maturity must be spread appropriately in order to reduce refinancing risk.

## **5.7 Policy on borrowing in advance of need**

The Councils will not borrow more than or in advance of their 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 Councils can ensure the security of such funds.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

## **5.8 Debt rescheduling**

Rescheduling of current borrowing in our debt portfolio is unlikely to occur as there is still a very large difference between premature redemption rates and new borrowing rates, even though the general margin of PWLB rates over gilt yields was reduced by 100 bps in November 2020.

If rescheduling is done, it will be reported to the Councils at the earliest meeting following its action.

## **5.9 New financial institutions as a source of borrowing**

Currently the PWLB Certainty Rate is set at gilts + 80 basis points for both HRA and non-HRA borrowing. However, consideration will also need to be given to sourcing funding at cheaper rates from the following:

- 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)
- “Green Bonds” or “Local Climate Bonds”

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

## **6. ANNUAL INVESTMENT STRATEGY**

### **6.1 Investment Policy – Management of risk**

6.1.1 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 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.

6.1.2 The Councils' investment policy has regard to the following:

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

The Councils' investment priorities will be security first, portfolio liquidity second and then yield, (return). The Councils will aim to achieve the maximum yield on investments commensurate with proper levels of security and liquidity and with the Councils' risk appetite. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs. However, where appropriate (from an internal as well as external perspective), the Councils will also consider the value available in periods up to 12 months with high credit rated financial institutions, as well as wider range fund options.

6.1.3 The Chief Financial Officer, under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements, and Prudential Indicators. As conditions in the financial markets remain uncertain, the proposed maximum limits for specified and unspecified investments for 2022/23 are the same as for 2021/22, as amended by the Mid Year Review. The Mid Year Review added the UK bank Standard Chartered (currently A+ rated) to the specified investments and increased the limit for investment with the Local Authorities' Property Fund from £3m to £5m per Council for the purpose of setting aside long term funds for the repayment of debt. Counterparties' "sustainability", "ethical" or "climate change" policies will be reviewed to ensure that the Council invests funds appropriately.

6.1.4 Investment instruments identified for use in the financial year are listed in Appendix B under the 'specified' and 'non-specified' investments categories. Counterparty limits will be as set through the Councils' treasury management practices.

6.1.5 The guidance from the DLUHC and CIPFA places a high priority on the management of risk. The Councils have adopted a prudent approach to managing risk and define 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 Councils will engage with the advisors to maintain a monitor on market pricing such as "credit default swaps" (a financial derivative or contract that allows an investor to "swap" or offset his or her credit risk with that of another investor) 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) The Councils have defined the list of **types of investment instruments** that the treasury management team is authorised to use. There are two lists in Appendix B under the categories of 'specified' and 'non-specified' investments.
  - **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year 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) **Lending limits**, (amounts and maturity), for each counterparty will be set through applying the matrix table in Appendix B.
- f) The Councils will set a limit for the amount of its investments which are invested for **longer than 365 days**, (see paragraph 6.8).
- g) Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating** (see paragraph 6.4). The UK is excluded from this limit because it will be necessary to invest in UK banks and other institutions even if the sovereign rating is cut.
- h) The Councils have engaged **external consultants**, (see paragraph 3.5), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of the Councils in the context of the expected level of cash balances and need for liquidity throughout the year.
- i) All investments will be denominated in **sterling**.
- j) As a result of the change in accounting standards for 2022/23 under IFRS 9, the Councils 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 Ministry of Housing, Communities and Local Government, [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 March 2023. Consequently any fluctuations in the value of the Councils' investments in the Local Authorities' Property Fund will not be taken through the General Fund for the period of the override).

6.1.6 However, the Councils will also pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance, (see paragraph 6.15). Regular monitoring of investment performance will be carried out during the year.

## 6.2 Creditworthiness Policy

6.2.1 The primary principle governing the Councils' joint treasury management service investment criteria is the security of investments, although the yield or return on the investment is also a key consideration. After this main principle, the service will ensure that:

- It maintains a policy covering 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
- It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Councils' prudential indicators covering the maximum principal sums invested.

6.2.2 The Chief Financial Officer will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to the Councils 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 service may use, rather than defining what types of investment instruments are to be used.

6.2.3 Credit rating information is supplied by Link Group, our treasury advisors, on all active counterparties that comply with our criteria. 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 a counterparty at the minimum Council criteria will be suspended from use, with all others being reviewed in light of market conditions.

6.2.4 In accordance with the Code, Link Group's creditworthiness service uses a wider array of information other than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to

just one agency's ratings.

6.2.5 The result is a series of colour coded bands for counterparties indicating the relative creditworthiness of each as they are categorised by durational bands. These bands are used by the Councils to form a view of the duration for investments by each counterparty. The Councils are satisfied that this service gives a robust level of analysis for determining the security of its investments. It is also a service which the Councils would not be able to replicate using its own in-house resources.

6.2.6 Using Link's ratings service, potential counterparty ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications. The effect of a change in ratings may prompt the following responses:

- If a downgrade results in the counterparty/investment scheme no longer meeting the Councils' minimum criteria, its further use as a new investment will be withdrawn immediately.
- In addition to the use of Credit Ratings the Councils will be advised by Link of movements in Credit Default Swaps and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Councils' lending lists.

6.2.7 The Councils' officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets, the government support for banks, and the credit ratings of that government support.

6.2.8 Accordingly, the Councils may exercise discretion to deviate from Link's suggested durational bands for counterparties where circumstances warrant a more flexible approach being taken.

### **The Councils' Minimum Investment Creditworthiness Criteria**

6.3 The minimum credit ratings criteria used by the Councils generally will be a short term rating (Fitch or equivalent) of F1, and long term rating A-. There may be occasions when the counterparty ratings from one or more of the three Ratings Agencies are marginally lower than the minimum requirements of F1 Short term, A- Long term (or equivalent). Where this arises, the counterparties to which the ratings apply may still be used with discretion, but in these instances consideration will be given to the whole range of topical market information available, not just ratings.

The Councils include the top five **building society** names in the specified investments. It is recognised that they may carry a lower credit rating than the Councils' other counterparties, therefore the lending limits for the building

societies shall be £2m each, excepting that for Nationwide (the top building society) the lending limit shall be £4m.

#### **6.4 Country Limits and Proposed Monitoring Arrangements**

Due care will be taken to consider the country, group and sector exposure of the Councils' investments.

The Councils have determined that they will only use approved counterparties from countries (other than the UK) with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide one). The list of countries that qualify using these credit criteria as at the date of this report is reflected in the counterparty approved lending list shown at Appendix B. This list will be added to, or deducted from, by officers should ratings change, in accordance with this policy. No more than 25% of investments shall be placed in non-UK financial institutions for more than 7 days.

#### **6.5 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, as economies are beginning to reopen, there have been some instances of previous lowering of Outlooks being reversed.

##### **CDS prices - Credit Default Swaps**

Although bank CDS prices (these are credit derivative contracts that enable investors to swap credit risk and are therefore indicators of market 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 Councils have access to this information via the Link-provided Passport portal.

##### **Investment Strategy**

#### **6.6 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. For cash flow balances, the Councils will seek to use notice accounts, money market funds, call accounts

and short-dated deposits to benefit from the compounding of interest.

- 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.

The Chief Financial Officer, under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators. Decisions taken on the core investment portfolio will be reported to the meetings of the JGC and JSC in accordance with the reporting arrangements contained in the Treasury Management Practices Statement.

### 6.7 Investment returns expectations

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:

2022/23	0.50%
2023/24	0.75%
2024/25	1.00%
2025/26	1.25%
Later years	2.00%

- 6.8 **Investment treasury indicator and limit** - total principal funds invested for greater than 365 days. These limits are set with regard to the Councils' liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

The Councils are asked to approve the following treasury indicators and limits:

#### ADUR DISTRICT COUNCIL

MAXIMUM PROPORTION OF PRINCIPAL SUMS INVESTED > 365 DAYS			
	2022/23	2023/24	2024/25
Principal sums invested > 365 days	50%	50%	50%

#### WORTHING BOROUGH COUNCIL

MAXIMUM PROPORTION OF PRINCIPAL SUMS INVESTED > 365 DAYS			
	2022/23	2023/24	2024/25
Principal sums invested > 365 days	50%	50%	50%

Both Councils are currently holding investments in the Local Authorities' Property Fund (£3m for Adur and £1.5m for Worthing) and other small bonds in the local credit union (£50k for Worthing and £25k for Adur) which are expected to be invested for more than 365 days. Worthing holds long term investments with Worthing Homes and GB Met College.

6.9 In any sustained period of significant stress in the financial markets, the default position is for investments to be placed with the Debt Management Account Deposit Facility of the UK central government. The rates of interest may be below equivalent money market rates, however, if necessary, the returns are an acceptable trade-off for the guarantee that the Councils' capital is secure.

6.10 The Councils' proposed investment activity for placing cash deposits in 2022/23 will be to use:

- AAA rated Money Market Funds with a Constant Net Asset Value (CNAV) or a Low Volatility Net Asset Value (LVNAV) under the new money market fund regulations
- other local authorities, parish councils etc.
- business reserve accounts and term deposits, primarily restricted to UK institutions that are rated at least A- long term.
- the top five building societies by asset size

#### **Other Options for Longer Term Investments**

6.12 To provide the Councils with options to enhance returns above those available for short term durations, it is proposed to retain the option to use the following for longer term investments, as an alternative to cash deposits:

- a) **Supranational bonds greater than 1 year to maturity**
- b) **Gilt edged securities** with a maturity of greater than one year. These are Government bonds and so provide the highest security of interest and the repayment of principal on maturity. Similar to category (a) above, the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.
- c) **The Councils' own banker** (currently Lloyds) if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as is possible.
- d) **Building societies not meeting the basic security requirements under the specified investments.** The operation of some building societies does not require a credit rating, although in every other respect the security of the society would match similarly sized societies with ratings. The Council may use the top five building societies by asset size up to £2m, (£4m Nationwide).
- e) Any **bank or building society** that has a minimum long term credit rating of A- for deposits with a maturity of greater than one year

(including forward deals in excess of one year from inception to repayment).

- f) Any **non-rated subsidiary** of a credit rated institution included in the specified investment category. These institutions will be included as an investment category subject to a guarantee from the parent company, and total exposure up to the limit applicable to the parent.
- g) **Registered Social Landlords** (Housing Associations) **and other public sector bodies** - subject to confirming that the Councils have appropriate powers, consideration will be given to lending to Registered Social Landlords and other public sector bodies. Such lending may either be as an investment for treasury management purposes, or for the provision of “social policy or service investment”, that would not normally feature within the Treasury Management Strategy.
- h) **Property Investment Funds** for example the Local Authorities’ Property Fund. The Councils will consult the Treasury Management Advisors and undertake appropriate due diligence before investment of this type is undertaken. Some of these funds are deemed capital expenditure – the Councils will seek guidance on the status of any fund considered for investment. The Councils may invest up to £5m in Property Investment Funds - this reflects the request from Adur members to invest more in the CCLA Local Authorities’ Property Fund.
- i) **Other local authorities**, parish councils etc.
- j) **Loan capital** in a body corporate.
- k) **Share capital in a body corporate** – *The use of these instruments will be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. Revenue resources will not be invested in corporate bodies.*

**(Note:** For (j) and (k) above the Councils will seek further advice on the appropriateness and associated risks with investments in these categories as and when an opportunity presents itself).

6.13 **The accounting treatment** may differ from the underlying cash transactions arising from investment decisions made by the Councils. To ensure that the Councils are protected from any adverse revenue impact, which may arise from these differences, the accounting implications of new transactions will be reviewed before they are undertaken.

6.14 The Councils will not transact in any investment that may be deemed to constitute **capital expenditure** (e.g. Share Capital, or pooled investment funds other than Money Market Funds), without the resource implications being approved as part of the consideration of the Capital Programme or other appropriate Committee report.

6.15 **Investment risk benchmarking** – the Councils will subscribe to Link’s Investment Benchmarking Club to review the investment performance and risk

of the portfolios.

6.16 **End of year investment report** – at the end of the financial year the Councils will report on investment activity as part of the Annual Treasury Report.

6.17 **Local Authorities' Property Fund** – both Councils hold investments in the Fund (Adur DC - £3m and Worthing BC £1.5m). The treasury service receives regular reports and quarterly dividends. Representatives of the Fund gave a presentation on current and forecast performance to the Councils in October 2021.

## 7. OTHER MATTERS

7.1 **2021 revised CIPFA Treasury Management Code and Prudential Code – changes which will impact on future TMSS/AIS reports and the risk management framework**

CIPFA published the revised codes on 20th December 2021 and has stated that formal adoption is not required until the 2023/24 financial year. The Councils have to have regard to these codes of practice when they prepare the Treasury Management Strategy Statement and Annual Investment Strategy, and also related reports during the financial year, which are taken to the Full Councils for approval.

The revised codes will have the following implications:

- a requirement for the Councils to adopt a new debt liability benchmark treasury indicator to support the financing risk management of the capital financing requirement;
- clarify what CIPFA expects a local authority to borrow for and what they do not view as appropriate. This will include the requirement to set a proportionate approach to commercial and service capital investment;
- address Environmental Social and Governance issues within the Capital Strategy;
- require implementation of a policy to review commercial property, with a view to divest where appropriate;
- create new Investment Practices to manage risks associated with non-treasury investment (similar to the current Treasury Management Practices);
- ensure that any long term treasury investment is supported by a business model;
- a requirement to effectively manage liquidity and longer term cash flow requirements;
- amendment to the Treasury Management Practices to address Environmental, Social and Governance policy within the treasury management

risk framework;

- amendment to the knowledge and skills register for individuals involved in the treasury management function - to be proportionate to the size and complexity of the treasury management conducted by each council;

- a new requirement to clarify reporting requirements for service and commercial investment, (especially where supported by borrowing/leverage).

In addition, all investments and investment income must be attributed to one of the following three purposes: -

### **Treasury management**

Arising from the organisation's cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.

### **Service delivery**

Investments held primarily and directly for the delivery of public services including housing, regeneration and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in cases where the income is "either related to the financial viability of the project in question or otherwise incidental to the primary purpose".

### **Commercial return**

Investments held primarily for financial return with no treasury management or direct service provision purpose. Risks on such investments should be proportionate to a council's financial capacity – i.e., that 'plausible losses' could be absorbed in budgets or reserves without unmanageable detriment to local services. An authority must not borrow to invest primarily for financial return.

Members will be updated on how all these changes will impact our current approach and any changes required will be formally adopted within the 2023/24 TMSS report.

7.2 **Balanced budget requirement** - the Councils comply with the provisions of S32 of the Local Government Finance Act 1992 to set a balanced budget.

7.3 For social policy purposes, the Councils both hold deferred shares in the local Credit Union, Boom. Boom approached the Councils with a request to hold and invest some of Boom's funds in order to mitigate their treasury management investment risk. The Councils approved this through the Mid Year Review of Treasury Management. Boom's management has indicated that there is likely to be a request to lend around £2m to Worthing Borough Council, on mutually beneficial terms.

## **8. ENGAGEMENT AND COMMUNICATION**

- 8.1 The Adur and Worthing Councils' treasury management team provides treasury services to Mid Sussex District Council through a shared services arrangement (SSA). The SSA is provided under a Service Level Agreement that was renewed from 18th October 2019, and which defines the respective roles of the client and provider authorities for a period of three years.
- 8.2 The treasury management team also entered into a Service Level Agreement with Arun District Council to provide treasury services for three years from 1st March 2021
- 8.3 Information and advice is supplied throughout the year by Link Group, the professional consultants for the Councils' shared treasury management service.

## **9. FINANCIAL IMPLICATIONS**

- 9.1 This report has no quantifiable additional financial implications to those outlined above. Interest payable and interest receivable arising from treasury management operations, and annual revenue provisions for repayment of debt, form part of the revenue budget.

## **10. LEGAL IMPLICATIONS**

- 10.1 The approval and adoption of the Treasury Management Strategy Statement, Annual Investment Strategy, Minimum Revenue Provision Policy and Prudential Indicators is required by regulations issued under the Local Government Act 2003.

### **Background Papers**

Joint Treasury Management Strategy Statement and Annual Investment Strategy Report 2021/22 to 23/24 – Adur Council 18 February 2021 and Worthing Council 23 February 2021

Annual Joint In-House Treasury Management Operations Report 1 April 2020 – 31 March 2021 for Adur District Council and Worthing Borough Council – Joint Governance Committee, 29 July 2021 and Joint Strategic Committee, 7 September 2021

Overall Budget Estimates 2022/23 and Setting of 2022/23 Council Tax Report

Link Asset Services Ltd TMSS Template 2022/23

Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes (CIPFA, December 2017) and CIPFA Treasury Management Guidance Notes 2018

The Prudential Code for Capital Finance in Local Authorities (CIPFA, December 2017)

MHCLG Investment Guidance

**Officer Contact Details:-**

Pamela Coppelman

Group Accountant (Strategic Finance)

Telephone: 01903 221236

Email: [pamela.coppelman@adur-worthing.gov.uk](mailto:pamela.coppelman@adur-worthing.gov.uk)

## **SUSTAINABILITY & RISK ASSESSMENT**

### **1. ECONOMIC**

The treasury management function ensures that the Councils have sufficient liquidity to finance their day to day operations. Borrowing is arranged as required to fund the capital programmes. Available funds are invested according to the specified criteria to ensure security of the funds, liquidity and, after these considerations, to maximise the rate of return.

### **2. SOCIAL**

#### **2.1 Social Value**

Matter considered and no issues identified.

#### **2.2 Equality Issues**

Matter considered and no issues identified.

#### **2.3 Community Safety Issues (Section 17)**

Matter considered and no issues identified.

#### **2.4 Human Rights Issues**

Matter considered and no issues identified.

### **3. ENVIRONMENTAL**

Matter considered and no issues identified.

### **4. GOVERNANCE**

4.1 The Councils' Treasury Management Strategy and Annual Investment Strategy place the security of investments as foremost in considering all treasury management dealing. By so doing it contributes towards the Council priorities contained in Platforms for our Places.

4.2 The operation of the treasury management function is as approved by the Councils' Treasury Management Strategy and Annual Investment Strategy 2022/23 - 2024/25, submitted and approved before the commencement of the 2022/23 financial year.

4.3 In the current economic climate the security of investments is paramount, the management of which includes regular monitoring of the credit ratings and other incidental information relating to credit worthiness of the Councils' investment counterparties.

## Appendix A

### THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2022/23 – 2024/25

- 1.1 The Councils' 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.

#### Adur District Council

Adur Capital expenditure	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
	£m	£m	£m	£m	£m
Non-HRA	12.512	10.270	52.997	2.473	1.862
HRA	5.186	25.666	19.513	5.600	5.600
Commercial property	0.000	0.000	0.000	0.000	0.000
<b>TOTAL</b>	<b>17.698</b>	<b>35.936</b>	<b>72.510</b>	<b>8.073</b>	<b>7.462</b>

#### Worthing Borough Council

Worthing Capital expenditure	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
	£m	£m	£m	£m	£m
Non-HRA	17.744	52.068	74.896	3.811	3.332
Strategic property	0.000	0.000	0.000	0.000	0.000
<b>TOTAL</b>	<b>17.744</b>	<b>52.068</b>	<b>74.896</b>	<b>3.811</b>	<b>3.332</b>

#### 1.2 Affordability prudential indicators

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. These provide an indication of the impact of the capital investment plans on the Councils' overall finances. The Councils are asked to approve the following indicators:

##### **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.

## Adur District Council

Adur	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
	%	%	%	%	%
Non-HRA	10.03	14.43	15.83	24.14	22.51
HRA	16.03	23.51	24.89	26.36	26.03
Strategic purchases	(9.93)	(19.10)	(21.91)	(24.07)	(23.56)
<b>TOTAL</b>	<b>16.13</b>	<b>18.84</b>	<b>18.81</b>	<b>26.43</b>	<b>24.98</b>

## WORTHING BOROUGH COUNCIL

Worthing	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
	%	%	%	%	%
Non-HRA	4.95	5.50	8.40	8.33	8.36
Commercial activities	(7.82)	(11.87)	(15.39)	(15.78)	(15.09)
<b>TOTAL</b>	<b>(2.87)</b>	<b>(6.37)</b>	<b>(6.99)</b>	<b>(7.45)</b>	<b>(6.73)</b>

The estimates of financing costs include current commitments and the proposals in this budget report.

### HRA Ratio

Adur	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
HRA debt £m	(60.476)	(78.598)	(94.111)	(95.711)	(97.311)
Number of HRA dwellings	2537	2537	2583	2630	2622
Debt per dwelling	£23.8k	£31.0k	£36.4k	£36.4k	£37.1k

### 1.3 Maturity structure of borrowing

These gross limits are set to reduce the Councils' exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits. Neither Council has any variable rate borrowing.

The Councils are asked to approve the following treasury indicators and limits:

**Adur District Council**

<b>Limits to maturity structure of fixed interest rate borrowing 2022/23</b>		
	<b>Lower Limit</b>	<b>Upper Limit</b>
<b>Under 12 months</b>	0%	25%
<b>12 months to 2 years</b>	0%	30%
<b>2 years to 5 years</b>	0%	50%
<b>5 years to 10 years</b>	0%	70%
<b>10 years to 20 years</b>	0%	80%
<b>20 years to 30 years</b>	0%	60%
<b>30 years to 40 years</b>	0%	60%
<b>40 years to 50 years</b>	0%	45%

**WORTHING BOROUGH COUNCIL**

<b>Limits to maturity structure of fixed interest rate borrowing 2022/23</b>		
	<b>Lower Limit</b>	<b>Upper Limit</b>
<b>Under 12 months</b>	0%	35%
<b>12 months to 2 years</b>	0%	40%
<b>2 years to 5 years</b>	0%	75%
<b>5 years to 10 years</b>	0%	75%
<b>10 years to 20 years</b>	0%	75%
<b>20 years to 30 years</b>	0%	75%
<b>30 years to 40 years</b>	0%	75%
<b>40 years to 50 years</b>	0%	75%

### **TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT**

The MHCLG (now DLUHC) issued Investment Guidance in 2018, and this forms the structure of the Councils' policy below. These guidelines do not apply to either trust funds or pension funds which operate under a different regulatory regime.

The key intention of the Guidance is to maintain the current requirement for councils to invest prudently, and that priority is given to security and liquidity before yield. In order to facilitate this objective the guidance requires the Councils to have regard to the CIPFA publication Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes, which will apply to all investment activity. In accordance with the Code, the Chief Financial Officer has produced its treasury management practices (TMPs). This part, TMP 1(1), covering investment counterparty policy requires approval each year.

**Annual investment strategy** - The key requirements of both the Code and the investment guidance are to set an annual investment strategy, as part of the annual treasury strategy for the following year, covering the identification and approval of following:

- The strategy guidelines for choosing and placing investments, particularly non-specified investments;
- The principles to be used to determine the maximum periods for which funds can be committed;
- Specified investments that the Councils will use. These are high security (i.e. high credit rating, although this is defined by the Councils, and no guidelines are given), and high liquidity investments in sterling and with a maturity of no more than a year;
- Non-specified investments, clarifying the greater risk implications, identifying the general types of investment that may be used and a limit to the overall amount of various categories that can be held at any time.

The investment policy proposed for the Councils is:

**Strategy guidelines** – The main strategy guidelines are contained in the body of the treasury strategy statement.

### **SPECIFIED AND NON SPECIFIED INVESTMENTS**

#### **Specified Investments identified for use by the Councils**

These investments are sterling investments of not more than one-year maturity, or those which could be for a longer period but where the Councils have the right to be repaid within 12 months if they wish. They also include investments which were originally classed as being non-specified investments, but which would have been classified as specified investments apart from originally being for a period longer than 12 months once the remaining period to maturity falls to under twelve months. These are considered low risk assets where the possibility of loss of principal or investment

income is small. These would include sterling investments which would not be defined as capital expenditure with:

- The UK Government (such as the Debt Management Account deposit facility, UK treasury bills or a gilt\* with less than one year to maturity)
- Supranational bonds of less than one year's duration\*
- A local authority, housing association, parish council or community council
- Pooled investment vehicles (such as money market funds) that have been awarded a AAA rating by Standard and Poor's, Moody's and/or Fitch rating agencies
- A body that is considered of a high credit quality (such as a bank or building society). This covers bodies with a minimum Short Term rating of F1 (or the equivalent) as rated by Standard and Poor's, Moody's and/or Fitch rating agencies.

Within these bodies, and in accordance with the Code, the Councils have set additional criteria to set the time and amount of monies which will be invested in these bodies - see Annexes 1 and 2.

### **Non-Specified Investments identified for use by the Councils**

These are any other type of investment (ie not defined as specified above). The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out in Annexes 1 and 2.

Where appropriate, the Councils will seek further advice on the associated risks with non-specified investments.

For credit rated counterparties, the minimum criteria, excepting for the Councils' own banker and the specified building societies, (see below) will be the short-term / long-term ratings assigned by various agencies which may include Moody's Investors Services, Standard and Poor's, Fitch Ratings, being:

**Long-term investments (over 365 days): minimum: A- (Fitch) or equivalent**

**Or**

**Short-term investments (365 days or less): minimum: F1 (Fitch) or equivalent**

For all investments the Councils will also take into account information on corporate developments of, and market sentiment towards, investment counterparties.

Where appropriate the Ring Fenced entities of banks will be used.

**ADUR DISTRICT COUNCIL - SPECIFIED AND NON SPECIFIED INVESTMENTS****Specified Investments identified for use by the Council**

New specified investments will be made within the following limits:

<b>Instrument</b>	<b>Country and sovereign rating</b>	<b>Counterparty and current rating</b>	<b>Max'm exposure limit £m and/or %</b>
Term Deposits	UK	DMADF, DMO	No limit
Term Deposits/ Call Accounts	UK	Other UK Local Authorities	£5m
Term Deposits/ Call Accounts	UK	Santander UK A+	£4m
Term Deposits/ Call Accounts	UK	Bank of Scotland/ Lloyds (RFB) A+	£4m
Term Deposits/ Call Accounts	UK	Barclays (RFB) A+	£4m
Term Deposits/ Call Accounts	UK	Clydesdale A-	£4m
Term Deposits/ Call Accounts	UK	HSBC (RFB) AA-	£4m
Term Deposits/ Call Accounts	UK	Close Brothers Ltd A-	£4m
Term Deposits/ Call Accounts	UK	Royal Bank of Scotland/Nat West Group (RFB) A+	£4m
Term Deposits/ Call Accounts	UK	Standard Chartered Bank A+	£3m
Term Deposits/ Call Accounts	Australia - AAA	National Australia Bank Ltd A+	£3m
Term Deposits/ Call Accounts	US - AAA	JP Morgan Chase Bank NA AA	£3m
Term Deposits/ Call Accounts	UK	Handelsbanken plc AA	£4m
Term Deposits/ Call Accounts	UK	Goldman Sachs Int Bank A+	£3m
Gilts	UK	Debt Management Office (DMO)	£3m or 25% of funds

<b>Instrument</b>	<b>Country and sovereign rating</b>	<b>Counterparty and current rating</b>	<b>Max'm exposure limit £m and/or %</b>
Bonds	EU	European Investment Bank/ Council of Europe	£3m or 25% of funds
AAA rated Money Market Funds		Constant Net Asset Value or LVNAV MMFs	to manage liquidity, maximum £3m per fund
Other MMFs and CIS	UK	Collective Investment Schemes	25%
Term Deposits	UK	Nationwide BS A	£4m
Term Deposits	UK	Yorkshire BS A-	£2m
Term Deposits	UK	Coventry BS A-	£2m
Term Deposits	UK	Skipton BS A-	£2m
Term Deposits	UK	Leeds BS A-	£2m
Share Capital	n/a	West Sussex Credit Union	£0.025m deferred shares
Share Capital	n/a	Local Capital Finance Co (Municipal Bonds Agency)	£0.05m

*NB Any existing deposits outside of the current criteria will be reinvested with the above criteria on maturity.*

*NB No more than 25% of funds shall be invested in Non-UK financial institutions whether by term deposits, call accounts or Money Market Funds, or any combination thereof, except that this limit may be breached for liquidity purposes for up to 1 week at any time.*

*NB Investments in AAA rated Money Market Funds are to be used for liquidity purposes - funds should be invested to achieve higher returns wherever possible.*

*Institution ratings shown are as at 20 December 2021 and are subject to change.*

## APPENDIX B - ANNEX 1

### ADUR DISTRICT COUNCIL NON-SPECIFIED INVESTMENTS DETERMINED FOR USE BY THE COUNCIL:

Having considered the rationale and risk associated with Non-Specified Investments, the following have been determined for the Council's use:

	In-house use	Use by Fund Managers	Maximum Maturity	Maximum % of portfolio or £m	Capital Expenditure ?
<ul style="list-style-type: none"> <li>☒ Deposits with banks and building societies</li> <li>☒ Certificates of deposit with banks and building societies</li> <li>☒ Deposits with Local Authorities</li> <li>☒ The UK Government</li> </ul>	<ul style="list-style-type: none"> <li>√</li> <li>√</li> <li>√</li> <li>√</li> </ul>	<ul style="list-style-type: none"> <li>√</li> <li>√</li> <li>√</li> <li>√</li> </ul>	5 years	The higher of £8m or 50% of funds, maximum of £2m per institution  £5m No limit	No
<b>Gilts and Bonds:</b> <ul style="list-style-type: none"> <li>☒ Gilts</li> <li>☒ Bonds issued by multilateral development banks</li> <li>☒ Bonds issued by financial institutions guaranteed by the UK government</li> <li>☒ Sterling denominated bonds by non-UK sovereign governments</li> </ul>	<ul style="list-style-type: none"> <li>√</li> <li>√</li> <li>√</li> <li>√ on advice from treasury advisors</li> </ul>	<ul style="list-style-type: none"> <li>√</li> <li>√</li> <li>√</li> <li>√</li> </ul>	5 years	The higher of £3m or 25% of funds	No
Money Market Funds and Collective Investment Schemes (pooled funds which meet the definition of a collective investment scheme as defined in SI 2004 No. 534 and SI 2007, No. 573), but which are not credit rated.	<ul style="list-style-type: none"> <li>√ (on advice from treasury advisor)</li> </ul>	<ul style="list-style-type: none"> <li>√</li> </ul>	These funds do not have a defined maturity date.	The higher of £5m or 30% of funds, maximum of £3m per fund	No
Government guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies	<ul style="list-style-type: none"> <li>√ (on advice from treasury advisor)</li> </ul>	<ul style="list-style-type: none"> <li>√</li> </ul>	5 years	The higher of £2m or 10% of funds	Yes

## APPENDIX B - ANNEX 1

### ADUR DISTRICT COUNCIL NON-SPECIFIED INVESTMENTS DETERMINED FOR USE BY THE COUNCIL:

	In-house use	Use by Fund Managers	Maximum Maturity	Maximum % of portfolio or £m	Capital Expenditure?
Non-guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies	√ (on advice from treasury advisor)	√	5 years	The higher of £2m or 10% of funds	Yes
Property Funds approved by HM Treasury and operated by managers regulated by the Financial Conduct Authority, such as the Local Authorities' Property Fund	√ (on advice from treasury advisor)	√	These funds do not have a defined maturity date	£5m	To be confirmed
Collective Investment Schemes (pooled funds) which do not meet the definition of collective investment schemes in SI 2004 No. 534 or SI 2007, No. 573.	√ (on advice from treasury advisor)	√	These funds do not have a defined maturity date	The higher of £2m or 20% of funds	Yes

1. In determining the period to maturity of an investment, the investment should be regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty.
2. The use of the above instruments by the Council's fund manager(s) will be by reference to the fund guidelines contained in the agreement between the Council and the individual manager.
3. The Council's own banker may also be used if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as possible.

## APPENDIX B - ANNEX 2

### WORTHING BOROUGH COUNCIL SPECIFIED AND NON SPECIFIED INVESTMENTS

#### Specified Investments identified for use by the Council

New specified investments will be made within the following limits:

<b>Instrument</b>	<b>Country and sovereign rating</b>	<b>Counterparty</b>	<b>Max'm exposure limit £m and/or %</b>
Term Deposits	UK	DMADF, DMO	No limit
Term Deposits/ Call Accounts	UK	Other UK Local Authorities	£5m
Term Deposits/ Call Accounts	UK	Santander UK A+	£4m
Term Deposits/ Call Accounts	UK	Bank of Scotland/ Lloyds (RFB) A+	£4m
Term Deposits/ Call Accounts	UK	Barclays (RFB) A+	£4m
Term Deposits/ Call Accounts	UK	Clydesdale A-	£4m
Term Deposits/ Call Accounts	UK	HSBC (RFB) AA-	£4m
Term Deposits/ Call Accounts	UK	Standard Chartered Bank A+	£3m
Term Deposits/ Call Accounts	UK	Close Brothers Ltd A-	£4m
Term Deposits/ Call Accounts	UK	Royal Bank of Scotland/Nat West Group (RFB) A+	£4m
Term Deposits/ Call Accounts	Australia - AAA	National Australia Bank Ltd A+	£3m
Term Deposits/ Call Accounts	US - AAA	JP Morgan Chase Bank NA AA	£3m
Term Deposits/ Call Accounts	UK	Handelsbanken plc AA	£4m
Term Deposits/ Call Accounts	UK	Goldman Sachs Int Bank A+	£3m
Gilts	UK	Debt Management Office (DMO)	£3m or 25% of funds

<b>Instrument</b>	<b>Country and sovereign rating</b>	<b>Counterparty</b>	<b>Max'm exposure limit £m and/or %</b>
Bonds	EU	European Investment Bank/ Council of Europe	£3m or 25% of funds
AAA rated Money Market Funds		Constant Net Asset Value or LVNAV MMFs	£9m or 25% of funds (the limit may be exceeded for up to 7 days), max £3m per fund
Other MMFs and CIS	UK	Collective Investment Schemes	25%
Term Deposits	UK	Nationwide BS A	£4m
Term Deposits	UK	Yorkshire BS A-	£2m
Term Deposits	UK	Coventry BS A-	£2m
Term Deposits	UK	Skipton BS A-	£2m
Term Deposits	UK	Leeds BS A-	£2m
*Term Deposits	UK	Worthing Homes (10 year loan)	£10m
*Term Deposits	UK	GB Met (20 year loan)	£5m
Share Capital	n/a	West Sussex Credit Union	£0.05m deferred shares
Share Capital	n/a	Local Capital Finance Co (Municipal Bonds Agency)	£0.05m
Temporary Loans	n/a	Worthing Leisure Trust	£0.5m

*NB Any existing deposits outside of the current criteria will be reinvested with the above criteria on maturity.*

*NB No more than 25% of funds shall be invested in Non-UK financial institutions whether by term deposits, call accounts or Money Market Funds, or any combination thereof, except that this limit may be breached for liquidity purposes for up to 1 week at any time.*

\* These loans are for more than 1 year, therefore are “unspecified”, but are included here as they have been approved by Council.

*Institution ratings shown are as at 20 December 2021 and are subject to change.*

## APPENDIX B - ANNEX 2

### WORTHING BOROUGH COUNCIL NON-SPECIFIED INVESTMENTS DETERMINED FOR USE BY THE COUNCIL:

Having considered the rationale and risk associated with Non-Specified Investments, the following have been determined for the Council's use:

	In-house use	Use by Fund Managers	Maximum Maturity	Maximum % of portfolio or £m	Capital Expenditure ?
<ul style="list-style-type: none"> <li>☒ Deposits with banks and building societies</li> <li>☒ Certificates of deposit with banks and building societies</li> <li>☒ Deposits with Local Authorities</li> <li>☒ The UK Government</li> </ul>	√	√	5 years	The higher of £8m or 50% of funds, maximum of £2m per institution	No
<p><b>Gilts and Bonds:</b></p> <ul style="list-style-type: none"> <li>☒ Gilts</li> <li>☒ Bonds issued by multilateral development banks</li> <li>☒ Bonds issued by financial institutions guaranteed by the UK government</li> <li>☒ Sterling denominated bonds by non-UK sovereign governments</li> </ul>	√	√	5 years	The higher of £3m or 25% of funds	No
<p>Money Market Funds and Collective Investment Schemes (pooled funds which meet the definition of a collective investment scheme as defined in SI 2004 No. 534 and SI 2007, No. 573), but which are not credit rated.</p>	√ (on advice from treasury advisor)	√	These funds do not have a defined maturity date.	The higher of £5m or 30% of funds, maximum of £3m per fund	No
<p>Government guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies</p>	√ (on advice from treasury advisor)	√	5 years	The higher of £2m or 10% of funds	Yes

**APPENDIX B- ANNEX 2**

**WORTHING BOROUGH COUNCIL  
NON-SPECIFIED INVESTMENTS DETERMINED FOR USE BY THE COUNCIL:**

	In-house use	Use by Fund Managers	Maximum Maturity	Maximum % of portfolio or £m	Capital Expenditure?
Non-guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies	√ (on advice from treasury advisor)	√	5 years	The higher of £2m or 10% of funds	Yes
Property Funds approved by HM Treasury and operated by managers regulated by the Financial Conduct Authority, such as the Local Authorities' Property Fund	√ (on advice from treasury advisor)	√	These funds do not have a defined maturity date	£5m	To be confirmed
Collective Investment Schemes (pooled funds) which do not meet the definition of collective investment schemes in SI 2004 No. 534 or SI 2007, No. 573.	√ (on advice from treasury advisor)	√	These funds do not have a defined maturity date	The higher of £2m or 20% of funds	Yes

1. In determining the period to maturity of an investment, the investment should be regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty.
2. The use of the above instruments by the Council's fund manager(s) will be by reference to the fund guidelines contained in the agreement between the Council and the individual manager.
3. The Council's own banker may also be used if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as possible.

**COUNTERPARTIES WHERE THE COUNCILS HAVE OPTED UP TO  
PROFESSIONAL INVESTOR STATUS**

**(i) Money Market Funds**

Invesco  
Federated Investors  
CCLA  
Black Rock  
HSBC ESG Fund

**(ii) Building Societies**

Skipton Building Society  
Coventry Building Society  
Leeds Building Society  
Nationwide Building Society  
Yorkshire Building Society

**(iii) Brokers**

BGC (Sterling)  
Tradition  
ICAP  
Imperial

**(iv) Other**

ICD (Portal used for money market fund investments)  
Link Group

These arrangements will be regularly reviewed as appropriate.

**TREASURY MANAGEMENT SCHEME OF DELEGATION**

**(i) Full Council**

- receiving and reviewing reports on treasury management policies, practices and activities
- approval of annual Treasury Management Strategy Statement and Annual Investment Strategy
- approval of MRP Statement

**(ii) Joint Strategic Committee**

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices
- budget consideration and approval
- approval of the division of responsibilities
- receiving and reviewing regular monitoring reports and acting on recommendations
- approving the selection of external service providers and agreeing terms of appointment.

**(iii) Joint Governance Committee**

Receiving and reviewing the following, and making recommendations to the Joint Strategic Committee

- the Treasury Management Strategy Statement and regular monitoring reports on compliance with the Treasury Management Strategy, practices and procedures.

**(iv) 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
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers.

### TREASURY MANAGEMENT SCHEME OF DELEGATION

The revised CIPFA Treasury Management and Prudential Codes have extended the functions of the S151 role in respect of non-financial investments

- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management
- ensuring that the capital strategy is prudent, sustainable and affordable in the long term and provides value for money
- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authorities
- ensuring that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed

## APPENDIX E

### Prospects for interest rates

The Councils have appointed Link Group as their treasury advisor and part of their service is to assist the Councils to formulate a view on interest rates.

Link provided the following forecasts on 20<sup>th</sup> December 2021. These are forecasts for certainty rates, gilt yields plus 80 bps.

Link Group Interest Rate View 20.12.21														
	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
BANK RATE	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25
3 month ave earnings	0.20	0.30	0.50	0.50	0.60	0.70	0.80	0.90	0.90	1.00	1.00	1.00	1.00	1.00
6 month ave earnings	0.40	0.50	0.60	0.60	0.70	0.80	0.90	1.00	1.00	1.10	1.10	1.10	1.10	1.10
12 month ave earnings	0.70	0.70	0.70	0.70	0.80	0.90	1.00	1.10	1.10	1.20	1.20	1.20	1.20	1.20
5 yr PWLB	1.40	1.50	1.50	1.60	1.60	1.70	1.80	1.80	1.80	1.90	1.90	1.90	2.00	2.00
10 yr PWLB	1.60	1.70	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10	2.20	2.30
25 yr PWLB	1.80	1.90	2.00	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.40	2.40	2.50	2.50
50 yr PWLB	1.50	1.70	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.20	2.20	2.30	2.30

Over the last two years, the coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16<sup>th</sup> December 2021.

As shown in the forecast table above, the forecast for Bank Rate now includes four increases, one in December 2021 to 0.25%, then quarter 2 of 2022 to 0.50%, quarter 1 of 2023 to 0.75%, quarter 1 of 2024 to 1.00% and, finally, one in quarter 1 of 2025 to 1.25%.

### Significant risks to the forecasts

- **Mutations** of the virus render current vaccines ineffective, and tweaked vaccines to combat these mutations are delayed, or cannot be administered fast enough to prevent further lockdowns. 25% of the population not being vaccinated is also a significant risk to the NHS being overwhelmed and lockdowns being the only remaining option.
- **Labour and supply shortages** prove more enduring and disruptive and depress economic activity.
- **The Monetary Policy Committee** acts too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- **The Monetary Policy Committee** tightens monetary policy too late to ward off building inflationary pressures.
- **The Government** acts too quickly to cut expenditure to balance the national budget.

- **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.
- **Longer term US treasury yields** rise strongly and pull gilt yields up higher than forecast.
- **Major stock markets** e.g., in the US, become increasingly judged as being over-valued and susceptible to major price corrections. Central banks become increasingly exposed to the “moral hazard” risks of having to buy shares and corporate bonds to reduce the impact of major financial market selloffs on the general economy.
- **Geopolitical risks**, for example in Ukraine, Iran, North Korea, but also in Europe and Middle Eastern countries; on-going global power influence struggles between Russia/China/US. These could lead to increasing safe-haven flows.

#### **The balance of risks to the UK economy: -**

- The overall balance of risks to economic growth in the UK is now to the downside, including risks from Covid and its variants - both domestically and their potential effects worldwide.

#### **Forecasts for Bank Rate**

It is not expected that Bank Rate will go up fast after the initial rate rise as the supply potential of the economy is not likely to have taken a major hit during the pandemic: it should, therefore, be able to cope well with meeting demand after supply shortages subside over the next year, without causing inflation to remain elevated in the medium-term, or to inhibit inflation from falling back towards the MPC's 2% target after the spike up to around 5%. The forecast includes four increases in Bank Rate over the three-year forecast period to March 2025, ending at 1.25%. However, it is likely that these forecasts will need changing within a relatively short timeframe for the following reasons: -

- We do not know how severe an impact Omicron could have on the economy and whether there will be another lockdown or similar and, if there is, whether there would be significant fiscal support from the Government for businesses and jobs.
- There were already increasing grounds for viewing the economic recovery as running out of steam during the autumn and now into the winter. And then along came Omicron to pose a significant downside threat to economic activity. This could lead into stagflation, or even into recession, which would then pose a dilemma for the MPC as to whether to focus on combating inflation or supporting economic growth through keeping interest rates low.
- Will some current key supply shortages spill over into causing economic activity in some sectors to take a significant hit?
- Rising gas and electricity prices in October and next April and increases in other prices caused by supply shortages and increases in taxation next April, are already going to deflate consumer spending power without the MPC having to take any action on Bank Rate to cool inflation.
- On the other hand, consumers are sitting on over £160bn of excess savings left over from the pandemic so when will they spend this sum, in part or in total?

- It looks as if the economy coped well with the end of furlough on 30<sup>th</sup> September. It is estimated that there were around 1 million people who came off furlough then and there was not a huge spike up in unemployment. The other side of the coin is that vacancies have been hitting record levels so there is a continuing acute shortage of workers. This is a potential danger area if this shortage drives up wages which then feed through into producer prices and the prices of services i.e., a second-round effect that the MPC would have to act against if it looked like gaining significant momentum.
- We also recognise there could be further nasty surprises on the Covid front beyond the Omicron mutation.
- If the UK invokes article 16 of the Brexit deal over the dislocation in trading arrangements with Northern Ireland, this has the potential to end up in a no-deal Brexit.

In summary, with the high level of uncertainty prevailing on several different fronts, we expect to have to revise our forecasts again - in line with whatever the new news is.

It should also be borne in mind that Bank Rate being cut to 0.25% and then to 0.10%, were emergency measures to deal with the Covid crisis hitting the UK in March 2020. At any time, the MPC could decide to simply take away such emergency cuts on no other grounds than they are no longer warranted, and as a step forward in the return to normalisation. In addition, any Bank Rate under 1% is both highly unusual and highly supportive of economic growth.

### **Forecasts for PWLB rates and gilt and treasury yields**

Since the start of 2021, we have seen a lot of volatility in gilt yields, and hence PWLB rates. As the interest forecast table for PWLB certainty rates above shows, there is forecast to be a steady, but slow, rise in both Bank Rate and gilt yields during the forecast period to March 2025, though there will doubtless be a lot of unpredictable volatility during this forecast period.

While monetary policy in the UK will have a major impact on gilt yields, there is also a need to consider the potential impact that rising treasury yields in America could have on our gilt yields. **As an average since 2011, there has been a 75% correlation between movements in US 10-year treasury yields and UK 10-year gilt yields. This is a significant UPWARD RISK exposure to our forecasts for longer term PWLB rates. However, gilt yields and treasury yields do not always move in unison.**

**US treasury yields.** During the first part of 2021, US President Biden's, and the Democratic party's, determination to push through a \$1.9trn (equivalent to 8.8% of GDP) fiscal boost for the US economy as a recovery package from the Covid pandemic was what unsettled financial markets. However, this was in addition to the \$900bn support package already passed in December 2020. This was then followed by additional Democratic ambition to spend \$1trn on infrastructure, (which was eventually passed by both houses later in 2021), and an even larger sum on an American families plan over the next decade; this is still caught up in Democrat / Republican haggling. Financial markets were alarmed that all this stimulus was happening at a time when: -

1. A fast vaccination programme had enabled a rapid opening up of the economy during 2021.
2. The economy was growing strongly during the first half of 2021 although it has weakened overall during the second half.

3. It started from a position of little spare capacity due to less severe lockdown measures than in many other countries.
4. And the Fed was still providing substantial stimulus through monthly QE purchases during 2021.

It was not much of a surprise that a combination of these factors would eventually cause an excess of demand in the economy which generated strong inflationary pressures. This has eventually been recognised by the Fed at its December meeting with an aggressive response to damp inflation down during 2022 and 2023.

**At its 3<sup>rd</sup> November Fed meeting**, the Fed decided to make a start on tapering its \$120bn per month of QE purchases so that they ended next June. However, at its **15<sup>th</sup> December meeting** it doubled the pace of tapering so that they will end all purchases in February. These purchases are currently acting as downward pressure on treasury yields and so it would be expected that Treasury yields will rise over the taper period and after the taper ends, all other things being equal. The Fed also forecast that it expected there would be three rate rises in 2022 of 0.25% from near zero currently, followed by three in 2023 and two in 2024, taking rates back above 2% to a neutral level for monetary policy.

There are also possible **DOWNSIDE RISKS** from the huge sums of cash that the UK populace have saved during the pandemic; when savings accounts earn little interest, it is likely that some of this cash mountain could end up being invested in bonds and so push up demand for bonds and support their prices i.e., this would help to keep their yields down. How this will interplay with the Bank of England eventually getting round to not reinvesting maturing gilts and then later selling gilts, will be interesting to monitor.

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

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

As the US financial markets are, by far, the biggest financial markets in the world, any upward trend in treasury yields will invariably impact and influence financial markets in other countries. Inflationary pressures and erosion of surplus economic capacity look much stronger in the US compared to those in the UK, which would suggest that Fed rate increases eventually needed to suppress inflation, are likely to be faster and stronger than Bank Rate increases in the UK. This is likely to put upward pressure on treasury yields which could then spill over into putting upward pressure on UK gilt yields.

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

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

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

#### **A new era – a fundamental shift in central bank monetary policy**

One of the key results of the pandemic has been a fundamental rethinking and shift in monetary policy by major central banks like the Fed, the Bank of England and the ECB, to tolerate a higher level of inflation than in the previous two decades when inflation was the prime target to bear down on so as to stop it going above a target rate. There is now also a greater emphasis on other targets for monetary policy than just inflation, especially on ‘achieving broad and inclusive “maximum” employment in its entirety’ in the US, before consideration would be given to increasing rates.

- The Fed in America has gone furthest in adopting a monetary policy based on a clear goal of allowing the inflation target to be symmetrical, (rather than a ceiling to keep under), so that inflation averages out the dips down and surges above the target rate, over an unspecified period of time.
- The Bank of England has also amended its target for monetary policy so that inflation should be ‘sustainably over 2%’ before starting on raising Bank Rate and the ECB now has a similar policy.
- **For local authorities, this means that investment interest rates and very short term PWLB rates will not be rising as quickly or as high as in previous decades when the economy recovers from a downturn and the recovery eventually runs out of spare capacity to fuel continuing expansion.**
- Labour market liberalisation since the 1970s has helped to break the wage-price spirals that fuelled high levels of inflation and has now set inflation on a lower path which makes this shift in monetary policy practicable. In addition, recent changes in flexible employment practices, the rise of the gig economy and technological changes, will all help to lower inflationary pressures.
- Governments will also be concerned to see interest rates stay lower as every rise in central rates will add to the cost of vastly expanded levels of national debt; (in the UK this is £21bn for each 1% rise in rates). On the other hand, higher levels of inflation will help to erode the real value of total public debt.

## Investment and borrowing rates

- **Investment returns** are expected to improve in 2022/23. However, while markets are pricing in a series of Bank Rate hikes, actual economic circumstances may see the MPC fall short of these elevated expectations.
- **Borrowing interest rates** fell to historically very low rates as a result of the COVID crisis and the quantitative easing operations of the Bank of England and still remain at historically low levels. The policy of avoiding new borrowing by running down spare cash balances has served local authorities well over the last few years.
- On 25.11.20, the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates which had been increased by 100 bps in October 2019. The standard and certainty margins were reduced by 100 bps but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three-year capital programme. The current margins over gilt yields are as follows: -.

§ **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)

§ **PWLB Certainty Rate** is gilt plus 80 basis points (G+80bps)

§ **PWLB HRA Standard Rate** is gilt plus 100 basis points (G+100bps)

§ **PWLB HRA Certainty Rate** is gilt plus 80bps (G+80bps)

§ **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)