Report To:	**Audit Committee**
Date of Meeting:	**22 January 2020**
Report Title:	**Treasury Management, Annual Investment Strategy and Capital Strategy 2020/21**
Report By:	**Peter Grace** **Assistant Director – Financial Services and Revenues (Chief Finance Officer)**
Key Decision:	**Yes**
Classification:	**Open**

Purpose of Report

To consider the draft Treasury Management Strategy, Annual Investment Strategy, Minimum Revenue Provision (MRP) Policy and Capital Strategy and make recommendations to Cabinet and full Council as appropriate. This is to ensure that there is an effective framework for the management of the Council's investments, cash flows and borrowing activities prior to the start of the new financial year. This report also provides an update on performance to 31 December 2019.

The Council has some £64.55 million of debt (as at 1 January 2020), and investments which can fluctuate between £15m and £30m in the year. The level of debt is set to increase to some £104m by 2021/22 with a consequently increase in risks.

Recommendation(s)

The Audit Committee recommend to Cabinet and full Council that:

1. **The Council approve the Treasury Management Strategy, Minimum Revenue Provision (MRP) Policy, Annual Investment Strategy, and the Capital Strategy.**

2. **The strategies listed be updated as necessary during 2020/21 in the light changing and emerging risks and the Council's evolving future expenditure plans.**

3. **The Financial rules and the Financial Operating Procedures of the Council are reviewed and revised as necessary to meet the requirements of the Code of Practice.**

4. **The Cabinet and full Council note that there is likely to be the use of Money Market Funds in 2020/21 – as already allowed for in the investment strategy.**

Reasons for Recommendations

1. The Council seeks to minimise the costs of borrowing and maximise investment income whilst ensuring the security of its investments. The Council continues to make substantial investments in commercial property, housing and energy generation initiatives, and this will continue to involve the Council in taking on additional borrowing.

2. The sums involved are significant and the assumptions made play an important part in determining the annual budget. The CIPFA Treasury Management Code of Practice (2017 Edition), adopted by the Council last year, was released to take account of the more commercialised approach being adopted by councils and the enhanced levels of transparency required. The Code represents best practice and helps ensure compliance with statutory requirements.

3. The Council has the ability to diversify its investments and must consider carefully the level of risk against reward against a background of historically relatively low interest rates. Investments can help to close the gap in the budget in the years ahead and thus help to preserve services, assist in the regeneration of the town, provide additional housing and enhance the long term sustainability of the town. However over reliance on such income streams would involve taking unnecessary risks with the future of the Council and its ability to deliver statutory services.

4. The Council has the option of using Money Market funds within its Investment Policy already. These are on occasion providing higher rates of return than some straight deposit accounts and as such the use of these funds is likely to occur in the near future.

Introduction

1. The Council is required to operate a balanced budget, which broadly means that cash raised will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

2. The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing needs of the Council, essentially the longer term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

3. Treasury management in this context is defined by CIPFA as:

   "The management of the organisation'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"

4. The Chief Finance Officer responsibilities were extended last year to include a series of new roles in respect of the capital strategy and also a specific role in respect of investment in non-financial assets. These are included within the Appendices.

5. The Audit Committee considered the same report and strategies at its meeting on the 22 January 2020 and resolved to recommend the policies and strategies to Cabinet and full Council.

Borrowing / Borrowing Levels

Investment guidance

6. In early 2018 the Ministry of Housing, Communities and Local Government (MHCLG) issued new statutory guidance on local government investments). This provided for added focus on non-financial asset investments and includes for example loans made to wholly-owned companies, third parties, joint ventures.

7. Investments made by a local authority can be classified into one of two main categories:

   (i) **Investments held for treasury management purposes**

   Where treasury management investments are held the Council discloses the contribution these investments make to the local authority

   (ii) Other investments

   Councils are required to disclose the contribution that all other investments make towards the service delivery objectives and /or place making role of the authority. Each authority is able to define the types of contribution that investments can make and a single investment can, make more than one type of contribution. These include:

- Yield/profit
- Regeneration
- Economic benefit/business rates growth
- Responding to market failure
- Treasury management

The Primary Requirements of the Code

8. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

9. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

10. Receipt by the full council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a capital Strategy, a Mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.

11. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

12. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is the Audit Committee.

13. Publication of the Strategies on the Council's website.

Reporting Arrangements

14. The reporting arrangements proposed, in accordance with the requirements of the 2017 Code, are summarised below:-

Area of Responsibility	Council/ Committee/ Officer	Frequency
Treasury Management Strategy / Annual Investment Strategy / MRP policy/ Capital Strategy (in future years)	Cabinet and Council	Annually before the start of the year
Treasury Management Strategy / Annual Investment Strategy / Capital Strategy/MRP policy – Mid	Cabinet and Council	Mid-year

Year report		
Treasury Management Strategy/Capital Strategy / Annual Investment Strategy / MRP policy – updates or revisions at other times	Cabinet and Council	As required
Annual Treasury Outturn Report	Cabinet and Council	Annually by 30 September after the end of the year
Treasury Management Practices	S151 Officer	Reviewed as required (minimum - annually)
Scrutiny of Treasury Management Strategy	Audit Committee	Annually before the start of the year
Scrutiny of treasury management performance and strategy	Audit Committee	Quarterly Monitoring reports, Mid-Year report,

15. The latest CIPFA Code of Practice on Treasury Management (2017) was adopted by this Council in February 2018. The main clauses adopted are included in Appendix 8.

16. The Audit Committee is required to consider the Prudential Indicators as part of the Treasury Management Strategy and make recommendations to Cabinet and full Council; these are identified in the report and Appendix 4 of the Treasury Management Strategy.

Investment Performance 2019-20

17. The performance for the first 9 months of 2019/20 provided an average return of 0.90%.This compares to 0.65% for the same period last year. The total interest receivable for the first 9 months is £182,603 (2018/19 £117,000). These figures exclude the interest receivable in respect of loans to other organisations, the Property Fund, Diversified Investment Fund (DIF) – See below.

Property Fund

18. It was agreed in February 2017 that the option for diversification of some of the investments into a property fund be undertaken with CCLA in the sum of £2m. The investment being in respect of the Council's reserves that are not required for a period of at least 5 years in order that any fall in values and entry costs into such funds can be covered. The £2m was invested in April 2017 and the performance is detailed below:

CCLA – LA's Property Prices and Dividend yields

End of	Dec-19	Sep-19	Jun-19	Mar-19	Dec-18	Dec-17	Apr-17
Offer Price p	322.7	324.35	327.66	327.4	329.35	319.44	307.19
Net Asset Value p	302.3	303.84	306.94	306.7	308.53	299.24	287.77
Bid Price p	297.61	299.13	302.19	301.95	303.75	294.60	283.31
Dividend* on XD Date p	3.19	3.45	3.15	3.31	3.32	3.38	
Dividend* - Last 12 Months p	13.1	13.22	12.94	13.08	12.98	13.71	13.19
Dividend Yield on NAV %	4.33	4.35	4.22	4.26	4.21	4.58	4.58
Fund Size £m	1200.1	1173.1	1178.2	1127.1	1,099.0	930.8	710.2

19. The dividend yield is around 4.3% on the net asset value. Dividends for the first 3 quarters of 2019/20 amount to some £63,650. Full year dividends are estimated at around £85,000 (December figures are provisional).

Property Fund Capital Value

Units (651,063)	Dec-19	Sep-19	Jun-19	Mar-19	Dec-18	Dec-17	Apr-17
Mid Market Price(£)	1,968,163	1,978,189.82	1,998,372.77	1,996,810.22	2,008,724.67	1,948,240.92	1,873,564.00
Bid Price (£)	1,937,629	1,947,524.75	1,967,447.28	1,965,884.73	1,977,603.86	1,918,031.60	1,844,526.59

20. The Capital value has increased by some 5.05% between April 2017 and December 2019 but continues to fluctuate as can be seen from the above table. It is important that this is continued to be viewed as a longer term investment (5 years plus) if the original Capital value is to be recovered.

Diversified Income Fund

21. It was agreed in February 2019 that a sum of £3m would be made available for further diversification of the Council's investments. £1m was invested on 26 July 2019 and a further £2m investment was made on 24 September 2019 into the CCLA Diversified Income Fund. Anticipated returns were around 3% with the added advantage of much higher liquidity than the property fund.

22. The capital value has already recovered from the initial investment where charges are effectively deducted, and was valued at £3,012,479 at the end of December 2019. Dividend yield (annual) on price is 3.15% for December (3.17% November). It should be remembered that this is a long term investment and prices can go up and down.

23. The Cabinet on 6 January 2020 considered a Mid-Year report on Treasury Management based on the performance and activities arising since setting the strategies before the start of the financial year. The current strategy and policies were considered to be appropriate and no recommendations for change were made.

Money Market Funds

24. The Council has the option of using Money Market funds within its Investment Policy already. These are on occasion providing higher rates of return than some straight deposit accounts currently being used on a daily basis. As such the use of these funds is likely to occur, once arrangements are in place. These funds remain highly rated and must meet the Council's existing creditworthiness criteria.

Capital Strategy

25. In the light of the increasing commercialisation within local government in particular, in December 2017, CIPFA issued revised Prudential and Treasury Management Codes.

26. The codes require all local authorities to produce detailed Capital Strategies.

27. The Capital Strategy is intended to give a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services along with an overview of how associated risk is managed and the implications for future financial sustainability.

28. The development of such a Strategy allows flexibility to engage with full council to ensure that the overall strategy, governance procedures and risk appetite are fully understood by all elected members.

29. The Capital Strategy should be tailored to the authority's individual circumstances but should include capital expenditure, investments and liabilities and treasury management. The Capital Strategy should include sufficient detail to allow all members to understand how stewardship, value for money, prudence, sustainability and affordability will be secured and to meet legislative requirements on reporting.

30. The Capital strategy being a high level document that summarises in appropriate detail the requirements for specific investment appraisals. As a minimum such requirements being:

    - The capital schemes that are proposed and their objectives
    - The legal power to undertake a particular scheme
    - The key aspects of the financial appraisal, including any significant risks that have been identified
    - Qualitative criteria that have underpinned the recommendation for a scheme to proceed e.g. links to Corporate plan, economic growth, job retention, etc.
    - Likely source of funding
    - Long term implications
    - Risks and affordability
    - In assessing new income generating proposals the Council does already consider the above list of issues as part of the due diligence checklist and decisions are fully documented.

31. This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset.

32. The Capital Strategy looks to cover a much longer planning period than the existing capital programme. The future expenditure plans continue to evolve. The capital strategy and all the prudential indicators and controls are attached for the known schemes. Borrowing limits will need to be determined by full Council based on affordability and risk in due course.

Risk Management

33. The Investment strategy prioritises security of investments over return. Where investments are made they are limited in size and duration. External treasury advisers are used to advise the Council and have been used to train members. The Council has introduced further checks on credit worthiness of counterparties over the last seven years as and when these have been further developed by its advisers.

34. Whilst there is no absolute security for investments made, the Council has limited its investments to the higher rated institutions, in order to mitigate the risk as far as practical and looks to reduce the risk by spreading its investment portfolio. The Council has adopted the CIPFA Code of Practice.

35. 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. Further training sessions for all members will be arranged prior to the consideration of the future Mid-year review by the Audit Committee and Cabinet in the autumn of 2020.

36. The training needs of treasury management officers will also be reviewed in the light of the Code's requirements and experience of new staff.

37. The additional risks that the Council is taking on with commercial property, housing and energy investments needs to be considered in the context of the totality of risk that the Council faces e.g. NHS, rates claim, robustness of income streams, loans and guarantees to other parties, economic downturns, etc. Where there is more risk and volatility in income streams the Council will need to ensure that it maintains sufficient reserves to ensure the Council's ability to deliver key services is not jeopardised.

38. The Council spreads its risk on investments by limiting the amount of monies with any one institution or group and limiting the timeframe of the exposure. In determining the level of the investment and period the Council considers formal credit ratings (Fitch) along with its own advisers (Link Asset Services) ratings advice.

39. The security of the principal sum remains of paramount importance to the Council.

Economic/Financial Implications

40. The Council generally has investments in the year of between £15 million and £27 million at any one time, and is estimated to have longer term borrowings approaching £65m by the end of March 2020 (if no further external borrowing is undertaken). Management of its investments, borrowing and cash flow remains crucial to the proper and effective management of the Council. The Strategies and Policies detailed in the report directly influence the Council's Medium Term Financial Strategy and the annual budget.

Organisational Consequences

41. The Cabinet is responsible for the development and review of the Treasury Management Strategy, Minimum Revenue Provision (MRP) Policy, Investment Strategy and the future Capital Strategy. The Audit Committee is responsible for scrutinising these strategies, policies and performance throughout the year. Full Council, as the budget setting body, remains responsible for the approval of the Treasury Management Strategy, MRP Policy, and Investment Strategy and for the new Capital Strategy.

42. Monitoring reports will be produced and will be presented to Cabinet and the Audit Committee. A mid-year report is presented to full Council on any concerns arising since approving the initial strategies and policies. Only full Council will be able to amend the Treasury Management Strategy, MRP Policy, Investment Strategy or Capital Strategy. The Chief Finance Officer will determine the Treasury Management Practices and associated schedules.

43. There are new responsibilities placed on the Council and the Chief Finance officer from the new Codes of Practice which relate to governance arrangements, ensuring robustness of business cases, and risk management. The risk management requirements relate to asset related properties which the Council has borrowed to finance, and assessments of overall risk.

44. There are specific requirements to maintain schedules of counterparties and of any guarantees that the Council may give or have given in the past in order to fully assess the potential risks that the Council may be exposed to when making investment decisions.

Timetable of Next Steps

Please include a list of key actions and the scheduled dates for these:

Action	Key milestone	Due date (provisional)	Responsible
Update Treasury Management Practices, produce necessary schedules for full compliance with Codes of Practice	1 April 2020	Full implementation by 2020/21	Chief Finance Officer
Arrange Training for members/ officers	Year End & Mid-Year Review Report	July 2020	Chief Finance Officer

Wards Affected

None

Policy Implications

Reading Ease Score: 24.9
Reading Grade Level: 15.3%

Equalities and Community Cohesiveness	**No**
Crime and Fear of Crime (Section 17)	No
Risk Management	Yes
Environmental Issues & Climate Change	No
Economic/Financial Implications	Yes
Human Rights Act	No
Organisational Consequences	Yes
Local People's Views	No
Anti-Poverty	No
Legal	No

Additional Information

Documents Attached:

(i)Treasury Management Strategy (including Investment Policy)

Includes the following Appendices:-

1. MRP Introduction and Policy Statement
2. Interest Rate Forecasts
3. Economic Review
4. Prudential and Treasury Indicators
5. Specified and non-Specified Investments
6. Approved Countries for Investments
7. Treasury Management Policy Statement
8. Purpose and Requirements of the Code
9. Treasury Management Scheme of Delegation
10. The Treasury Management Role of the Section 151 Officer

(ii) Capital Strategy

Other Supporting Documents:-

CIPFA - Treasury Management Code of Practice (2017)
CIPFA - The Prudential Code (2017)
Budget Report - Cabinet 10 February 2020

Officer to Contact

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