APPENDIX A

Capital Strategy Report 2020/21

Introduction

1. The capital strategy report gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability. It has been written in an accessible style to enhance Members' understanding of these, sometimes, technical areas.

2. Decisions made this year on capital and treasury management will have financial consequences for the Council for many years into the future. They are therefore subject to both a national regulatory framework and to local policy framework, summarised in this report.

Capital Expenditure and Financing

3. Capital expenditure is where the Council spends money on assets, such as property or vehicles, that will be used for more than one year. In local government this includes, in addition, spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £5,000 are not capitalised and are charged to revenue in year.

4. For details of the Council's policy on capitalisation, see Note x (page 32) of the Council's Accounting Policies contained within the 'Statement of Accounts 2018/19'.

5. In 2020/21, the Council is planning capital expenditure of £38.8m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

	2018/19 actual (£m)	2019/20 forecast (£m)	2020/21 budget (£m)	2021/22 budget (£m)	2022/23 budget (£m)	*2023/24 budget (£m)*	*2024/25 budget (£m)*
General Fund services							
Core Programme	3.701	3.111	4.500	4.082	3.745	*2.818*	*3.335*
Building Council Homes (GF)	-	0.355	1.185	2.765	-	-	-
Enterprise Zone (GF)	5.530	8.114	5.363	-	-	-	-
Prentice Place (GF)	1.191	2.158	-	-	-	-	-
Sub-Total	10,422	13.738	11.048	6.847	3.745	*2.818*	*3.335*
Council housing (HRA)							
Core Programme	16.873	20.547	15.908	14.535	12.937	*15.123*	*13.236*
Building Council Homes (HRA)	0.332	2.458	11.831	11.179	1.202	-	
Sub-Total	17.205	28.765	27.739	25.714	14.139	*15.123*	*13.236*
TOTAL	**27.627**	**42.503**	**38.787**	**32.561**	**17.884**	***17.941***	***16.571***

The Prudential Code requires disclosure through until 2022/23 only. .

6. A significant element of the General Fund Capital Programme relates to the ongoing development of Harlow's Enterprise Zone and Science Park. It is a major development which the Council is supporting by creation of a campus environment for leveraging in dynamic businesses creating new technologies and new products, thereby stimulating innovation and generating economic growth in the town.

7. The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. Housing capital expenditure is therefore recorded separately, and includes the anticipated building of 130 new homes over the forecast period at a cost of £26.7 million.

8. There is a further house building scheme totalling £4.3 million planned to be funded through the Non Housing Capital Programme.

9. Further details of projected capital expenditure are contained in the ‘Capital Programme Strategy Statement’ (see Appendix B to this Report).

10. **Governance**: Service Managers commence a process annually in September to bid for projects in the Council’s Non Housing Capital Programme. Bids are collated by the Finance Department who calculate the financing costs (which can be nil if the project is fully externally financed) and formulate capital project appraisals. The Deputy to the Chief Executive and Head of Finance & Property presents capital proposals to the Senior Management Board (SMB) for review. The review is based on a comparison of corporate priorities and service priorities and considers projected capital costs, financing costs and any resulting ongoing service costs. Recommendations from SMB formalise the Capital Programme for approval by Cabinet and to Full Council in January / February each year.

11. For full details of the Council’s latest Capital Programme, see the report entitled ‘Capital Programmes 2020/21’, which is presented separately in the agenda to Cabinet (23 January 2020 then to Full Council on 6 February 2020) and, upon publication, is available on the Council’s website pages for Committees.

12. Capital expenditure may only be financed either from external sources (government grants and other contributions), the Council’s own resources (revenue, reserves and capital receipts) or debt (borrowing, and leasing).

13. The planned financing of the above expenditure (Table 1) is as follows:

Table 2: Capital financing in £ millions

	2018/19 actual (£m)	2019/20 forecast (£m)	2020/21 budget (£m)	2021/22 budget (£m)	2022/23 budget (£m)	*2023/24 budget (£m)*	*2024/25 budget (£m)*
General Fund services							
Capital Receipts: RTB	0.205	0.209	0.209	0.212	0.214	*0.216*	*0.218*
Capital Receipts: Other	1.276	0.609	-	-	-	-	-
Grants	1.351	0.525	0.525	0.525	0.525	*0.525*	*0.505*
Direct Revenue Financing	0.268	0.893	0.427	0.156	0.156	*0.156*	*0.150*
Internal borrowing	7.322	11.502	-	-	-	-	-
External borrowing	-	-	9.887	5.954	2.851	*1.921*	*2.462*
Sub-Total	10.422	**13.738**	**11.048**	**6.847**	**3.745**	***2.818***	***3.335***
Council housing (HRA)							
Capital Receipts	2.013	1.590	1.563	1.444	1.321	*1.192*	*1.057*
Grants	0.131	-	-	-	-	-	-
Major Repairs Reserve	10.362	10.092	10.229	10.383	10.560	*10.767*	*10.968*
Direct Revenue Financing	3.950	10.586	2.198	2.633	1.097	*3.165*	*1.211*
Pooling Receipts	0.749	0.737	3.549	3.354	0.361	-	-
External borrowing for building council homes	-	-	10.200	7.900	0.800	-	-
Sub-Total	17.205	**23.005**	**27.739**	**25.714**	**14.139**	***15.123***	***13.236***
TOTAL	**27.627**	**42.503**	**38.787**	**32.561**	**17.884**	***17.941***	***16.571***

14. Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as minimum revenue provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP and use of capital receipts are as follows:

Table 3: Replacement of debt finance in £ millions

	2018/19 actual (£m)	2019/20 forecast (£m)	2020/21 budget (£m)	2021/22 budget (£m)	2022/23 budget (£m)	*2023/24 budget (£m)*	*2024/25 budget (£m)*
General Fund	0.250	0.265	0.305	0.411	0.560	*0.630*	*0.678*
HRA	-	-	-	-	-	-	-

15. The Council's full 'Minimum Revenue Provision Statement' forms part of this Capital Report (Appendix E).

16. The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase by £20.412m during 2020/21. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions

	31.3.2019 actual	31.3.2020 forecast	31.3.2021 budget	31.3.2022 budget	31.3.2023 budget
General Fund services	53.358	63.254	73.466	80.003	83.905
Council housing (HRA)	187.370	187.370	197.570	205.470	206.270
Capital investments	-	-	-	-	-
TOTAL CFR	**240.728**	**250.624**	**271.036**	**285.473**	**290.175**

17. **Asset management:** To ensure that capital assets continue to be of long-term use, the Council has recently reviewed its Asset Management Strategy and has undertaken a detailed stock condition survey of all of its non housing property assets. The strategy and associated action plan combined with the outputs of the stock condition survey have been applied to develop a future non housing capital investment programme. The strategy also sets out the desire to dispose of or transfer those assets which no longer fulfil an operational, community or commercial objective especially where there is a clear investment requirement which would outweigh the long term benefits of undertaking that investment. The objective of the strategy is to recognise the Council's asset portfolio as a resource which whilst providing operational and community benefits naturally consumes resources if it is to be maintained in a fit for purpose state. The Strategy sets out a framework for governance of the portfolio which

seeks to achieve greater engagement with users and elected councillors in order to ensure that capital investment decisions are aligned with the agreed corporate priorities as set out in the Council's Corporate Plan.

18. **Asset disposals:** When a capital asset is no longer required it may be sold so that the proceeds, known as capital receipts, can be spent on existing or new assets or to repay debt. Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive £1.772m of capital receipts in the coming financial year, 2020/21, as follows:

Table 5: Capital receipts in £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
Asset sales	1.663	2.441	1.772	1.656	1.535
Loans repaid	-	-	-	-	-
TOTAL	**1.663**	**2.441**	**1.772**	**1.656**	**1.535**

19. Further details of projected asset disposals are included in the 'Capital Programme Statement' (Appendix B).

Treasury Management

20. Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by temporary borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

21. Due to decisions taken in the past, the Council currently (as at 31 December 2019) has £211.837m borrowing at an average interest rate of 3.31% and £33.730m treasury investments at an average rate of 0.968%. This is detailed in Annex B of the 'Treasury Management Statement' (Appendix C).

22. **Borrowing strategy:** The Council's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between low cost

short-term loans (currently available at around 0.75%) and long-term fixed rate loans where the future cost is known but higher (currently around to 3.0%). The Council also utilises its ability to “internally borrow” which is very attractive when it has surplus funds available and it is unable to achieve any significant return through its Treasury Management activities with external interest rates for investments being at historic lows.

23. Projected levels of the Council’s total outstanding borrowing are shown below, compared with the capital financing requirement (see above).

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions

	31.3.2019 actual	**31.3.2020 forecast**	**31.3.2021 budget**	**31.3.2022 budget**	**31.3.2023 budget**
Borrowing	211.837	211.837	235.837	252.437	254.737
Capital Financing Requirement	240.728	250.624	271.036	285.473	290.175

24. Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the Council expects to comply with this in the medium term.

25. **Liability benchmark:** To compare the Council’s actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes that cash and investment balances are kept to a minimum level of £10m at each year-end. This benchmark is currently £196.751m and is forecast to rise to £244.338m over the next three years.

Table 7: Borrowing and the Liability Benchmark in £ millions

	31.3.2019 actual	**31.3.2020 forecast**	**31.3.2021 budget**	**31.3.2022 budget**	**31.3.2023 budget**
Outstanding borrowing	211.837	211.837	235.837	252.437	254.737
Liability benchmark	180.185	196.751	225.644	242.265	244.338

26. The table shows that the Council expects to remain borrowed above its liability benchmark. This is because cash outflows to date have been below the assumptions made when the loans taken on.

27. **Affordable borrowing limit:** The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year and to keep it under review. In line with statutory

guidance, a lower “operational boundary” is also set as a warning level should debt approach the limit.

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	2019/20 limit	2020/21 limit	2021/22 limit	2022/23 limit
Authorised limit – borrowing	280.700	301.000	315.500	320.200
Operational boundary – borrowing	270.700	291.000	305.500	310.200

28. Further details on borrowing are given in paragraphs 31 to 42 of the ‘Treasury Management Strategy’ (Appendix C).

29. **Investment strategy:** Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

30. The Council’s policy on treasury investments is to prioritise security and liquidity over yield; that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, which might include bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.

Table 8: Treasury management investments in £millions

	31.3.2019 actual	31.3.2020 forecast	31.3.2021 budget	31.3.2022 budget	31.3.2023 budget
Near-term investments	29.752	13.036	8.193	8.172	8.399
Longer-term investments: Property Fund	2.000	2.000	2.000	2.000	2.000
TOTAL	**31.752**	**15.036**	**10.193**	**10.172**	**10.399**

31. Further details on treasury investments are in paragraphs 43 to 66 of the ‘Treasury Management Strategy’ (Appendix C).

32. **Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Deputy to

the Chief Executive and Head of Finance & Property and staff, who must act in line with the treasury management strategy approved by Full Council. Half-yearly reports on treasury management activity are presented to Cabinet. The Cabinet Overview Working Group is responsible for scrutinising treasury management decisions.

Investments for Service Purposes

33. The Council makes investments to assist local public services, including making loans to promote economic growth and lending to its subsidiary company, HTS (Property and Environment) Ltd, which provides extensive building maintenance, grounds and environmental maintenance services to the Council. In light of the public service objective, the Council is willing to take more risk than with treasury investments, however it still plans for such investments to, at least, break even after all costs.

34. **Governance:** All decisions to date have been made subject to formal reporting and approval by Cabinet.

35. Further details on service investments are in paragraphs 6 to 10 of the 'Investment Strategy' (Appendix D).

Commercial Activities

36. With central government financial support for local public services declining, some Councils are investing in commercial property purely or mainly for financial gain. Harlow Council has not followed this course of action to date.

37. New Guidance requires Councils to disclose any property that it holds primarily or partially to generate a profit.

38. Harlow Council has only four such assets, namely, the golf course, two cottages and a former farmhouse. These generate an income of just over £82,000 a year (see Appendix D, 'Investment Strategy').

39. Construction commenced in 2018 on the new Nexus building at the Harlow Enterprise Zone with practical completion and handover of the building expected in early 2020. This will be a wholly owned asset which will be let to commercial tenants and whilst it will deliver an income stream to the Council a key determinant in the decision to proceed with the building was the regeneration and economic benefits it would bring to Harlow.

Liabilities

40. In addition to debt of £211.837m detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £90.200m as at 31 March 2019). It has also set aside £2.533m to cover risks of Business Rates appeals and £5.900m for other minor provisions. The Council is also covers the risk of having to pay for small-value insurance claims for which self-insurance is in place and managed through earmarked reserves.

41. **Governance:** Decisions on incurring new discretional liabilities are taken by Senior Management Board in consultation with the Deputy to the Chief Executive and Head of Finance & Property. It is the responsibility of Senior Managers to consult the Deputy to the Chief Executive and Head of Finance & Property on any matter liable to affect the Council's finances materially (for values above £50,000). In the event of any substantial liabilities arising during the course of the financial year, these are highlighted in the financial and performance monitoring reports, presented quarterly to Cabinet and onwards to Full Council.

42. Further details guarantees are set out in the Investment Strategy 2019/20 (Appendix D, paragraph 14), whilst further details of contingent liabilities are contained in Note 32 of the 'Statement of Accounts 2018/19'.

Revenue Budget Implications

43. Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. for the General Fund, the amount funded from Council Tax, business rates and general government grants; and for the Housing Revenue Account, predominantly housing rent income.

Table 9: Prudential Indicator: Proportion of financing costs to net revenue stream

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
General Fund					
Financing costs (£m)	0.067	0.347	0.482	0.624	0.800
Proportion of net revenue stream	0.61%	3.21%	4.46%	5.68%	7.27%
HRA					
Financing costs (£m)	6.528	6.554	6.863	7.095	7.101
Proportion of net revenue stream	12.04%	15.28%	14.29%	13.70%	12.91%

44. Further details on the revenue implications of capital expenditure are on pages 28 to 29 of the General Fund 2020/21 report.

45. **Sustainability**: Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. Capital investment decision making is not only about ensuring the initial allocation of capital funds meets the corporate and service priorities but ensuring the asset is fully utilised, sustainable and affordable throughout its whole life, which also includes the affordability of its debt financing costs. In approving the inclusion of schemes and projects within the Capital Programme the Deputy to the Chief Executive and Head of Finance & Property will need to have been satisfied that the proposed capital programme is prudent, affordable and sustainable.

Knowledge and Skills

46. The Council employs professionally qualified and experienced staff across a range of disciplines including finance, legal and property that follow Continuous Professional Development (CPD). The Council encourages apprenticeships and study programmes for staff with the ambition to achieve a professional qualification.

47. Recognising the scale of the Council’s staffing, where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers, Wilks Head and Eve LLP as property valuation advisers, as well as other reputable firms of property consultants to support it in assessing the condition of its asset, advising on property transactions and any new developments. This approach is more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

48. Internal and external training is offered to elected Members to ensure they have up to date knowledge and expertise to understand and challenge capital and treasury decisions taken by the administration, the Strategic Management Board and the Deputy to the Chief Executive and Head of Finance & Property.

APPENDIX B

Capital Programme Strategy Statement 2020/21

Introduction

1. This document sets out the Council's Capital Programme Medium Term Financial Strategy, providing more information to that given in the 'Capital Strategy Report' (Appendix A).

Capital Expenditure: Medium Term Financial Strategy

2. Estimates for Capital Expenditure through to 2024/25 are summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

	2018/19 actual (£m)	2019/20 forecast (£m)	2020/21 budget (£m)	2021/22 budget (£m)	2022/23 budget (£m)	*2023/24 budget (£m)*	*2024/25 budget (£m)*
General Fund services							
Core Programme	3.701	3.111	4.500	4.082	3.745	*2.818*	*3.335*
Building Council Homes (GF)	-	0.355	1.185	2.765	-	-	-
Enterprise Zone (GF)	5.530	8.114	5.363	-	-	-	-
Prentice Place (GF)	1.191	2.158	-	-	-	-	-
Sub-Total	10.422	13.738	11.048	6.847	3.745	*2.818*	*3.335*
Council housing (HRA)							
Core Programme	16.873	20.547	15.908	14.535	12.937	*15.123*	*13.236*
Building Council Homes (HRA)	0.332	2.458	11.831	11.179	1.202	-	
Sub-Total	17.205	28.765	27.739	25.714	14.139	*15.123*	*13.236*
TOTAL	**27.627**	**42.503**	**38.787**	**32.561**	**17.884**	***17.941***	***16.571***

3. The above table repeats that given in the 'Capital Strategy Report' (Appendix A) with the forecast 2019/20 and estimates for 2020/21 requiring Council approval given in more detail in a separate report 'Capital Programmes 2019/20 & 2020/21' to this meeting.

4. The Capital Programme is divided, for convenience, between a Housing Capital Programme (HCP) and Non Housing Capital Programme (NHCP). Both are then sub-divided between their Core Programmes and specific projects: in the NHCP this is the Enterprise Zone and regeneration of Prentice Place; in the HCP this covers the first major programme to build Council homes. The financing of the Capital Programme (see Table 3 below) is likewise treated separately, the Housing Capital Programme being funded exclusively through the Housing Revenue Account.

Building Council Homes

5. The Council's Corporate Plan places emphasis on 'More and Better Housing', tackling the housing need of Harlow residents, both in quantity, affordability, range and quality.

6. In addition to projects included in the 'HRA Business Plan 2019-2049', a cross-departmental Officer Task Group has updated and extended the programme of house building. This includes a number of projects: The Readings, Bushey Croft and Lister House / Perry Road where planning permission has already been granted.

7. Projects will be held in both the Non Housing Capital Programme and Housing Capital Programme. Some costs will be met from revenue.

8. The programme will be financed from retained pooling receipts and external borrowing, both within the Council's Housing Revenue Account. The Government allows Councils to keep receipts from a proportion of 'Right To Buy' sales on condition that these are spent within three years on building replacement council homes. Failure to deliver would result in retained receipts being repaid to Government at a penalty of base rate plus 4%. It is therefore essential that the programme is delivered in a timely manner, and that further retained receipts are drawn down prior to need. As a result of the need to borrow to finance these schemes they are being evaluated on the basis of viability utilising varying rental / tenure models.

9. A programme for house building is set out below.

Table 2A: House Building Programme met by the Housing Capital Programme

	Number of Units	2019/20 forecast (£m)	2020/21 budget (£m)	2021/22 budget (£m)	2022/23 budget (£m)	*2023/24 budget (£m)*	*2024/25 budget (£m)*
Programme							
Temporary Accom-modation	6	0.072	-	-	-	-	-
Sumners Farm Close	4	0.459	-	-	-	-	-
The Readings	3	0.382	0.996	-	-	-	-
Bushey Croft	16	0.101	-	2.808	1.202	-	-
Perry Road	46	1.444	5.267	7.289	-	-	-
The Yorkes	13	-	2.513	0.502	-	-	-
Land at Brenthall Towers	8	-	2.155	0.430	-	-	-
Stackfield	2	-	0.400	0.150	-	-	-
The Hill	2	-	0.500	-	-	-	-
TOTAL (see Table 1)	**115**	**2.458**	**11.831**	**11.179**	**1.202**	**-**	**-**
Financed by							
Pooling Receipts (see Table 3)		0.737	3.549	3.354	0.361	-	-
HRA balances, including External Borrowing		1.721	8.282	7.825	0.841	-	-
TOTAL		**2.458**	**11.831**	**11.179**	**1.202**	**-**	**-**

Table 2B: House Building Programme met by the Non Housing Capital Programme

	Number of Units	2019/20 forecast (£m)	2020/21 budget (£m)	2021/22 budget (£m)	2022/23 budget (£m)	*2023/24 budget (£m)*	*2024/25 budget (£m)*
Programme							
Elm Hatch	12	0.355	1.185	2.765	-	-	-
TOTAL (see Table 1)	**12**	**0.355**	**1.185**	**2.765**	**-**	**-**	**-**
Financed by							
GF Internal Borrowing		0.355	-	-	-	-	-
GF External Borrowing		-	1.185	2.765	-	-	-
TOTAL		**0.355**	**1.185**	**2.765**	**-**	**-**	-

10. This programme has been included in the ‘HRA Business Plan 2019-2049’, included for approval at this same meeting.

11. It is the intention that external borrowing will finance the balance of the house building programme. The HRA Business Plan has set out an indicative draw down of finance to support this goal: £10.2m in 2020/21, £7.9m in 2021/22 and a further £0.8m in 2021/22 with repayment after 25 years. Borrowing will be utilised as the need arises, as indicated in Table 3 below.

Capital Financing: Medium Term Financial Strategy

12. The planned financing of the above expenditure (Table 1) is as follows:

Table 3: Capital financing in £ millions

	2018/19 actual (£m)	2019/20 forecast (£m)	2020/21 budget (£m)	2021/22 budget (£m)	2022/23 budget (£m)	*2023/24 budget (£m)*	*2024/25 budget (£m)*
General Fund services							
Capital Receipts: RTB	0.205	0.209	0.209	0.212	0.214	*0.216*	*0.218*
Capital Receipts: Other	1.276	0.609	-	-	-	-	-
Grants	1.351	0.525	0.525	0.525	0.525	*0.525*	*0.505*
Direct Revenue Financing	0.268	0.893	0.427	0.156	0.156	*0.156*	*0.150*
Internal borrowing	7.322	11.502	-	-	-	-	-
External borrowing	-	-	9.887	5.954	2.851	*1.921*	*2.462*
Sub-Total	10.422	**13.738**	**11.048**	**6.847**	**3.745**	***2.818***	***3.335***
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Capital Receipts	2.013	1.590	1.563	1.444	1.321	*1.192*	*1.057*
Grants	0.131	-	-	-	-	-	-
Major Repairs Reserve	10.362	10.092	10.229	10.383	10.560	*10.767*	*10.968*
Direct Revenue Financing	3.950	10.586	2.198	2.633	1.097	*3.165*	*1.211*
Pooling Receipts	0.749	0.737	3.549	3.354	0.361	-	-
External borrowing	-	-	10.200	7.900	0.800	-	-
Sub-Total	17.205	**23.005**	**27.739**	**25.714**	**14.139**	***15.123***	***13.236***
TOTAL	**27.627**	**42.503**	**38.787**	**32.561**	**17.884**	***17.941***	***16.571***

APPENDIX C

Treasury Management Strategy Statement 2020/21

Summary of the Report

1. This Treasury Management Strategy Statement (TMSS) is now nestled within an overarching sequence of capital related reports but is of no less importance than before. It sets out the treasury management issues in accordance with proper practice.

2. It provides an update of external economic conditions impacting on the Council. The major issues of borrowing and non treasury investments are now covered in the new 'Investment Strategy' (Appendix D).

3. The Council uses treasury management advisors to help its decision making, keeping officers up to date with economic developments and providing training and support. Arlingclose Limited has been the Council's appointed advisor since December 2012.

4. Economic background and commentary has been provided by Arlingclose and included throughout the Statement. Treasury management continues to operate in a challenging environment with low interest rates and inflation above the Bank of England's target of 2%.

5. The UK economy is in an uncertain state as the government continues to navigate its exit from the European Union.

6. As a steward of public finance, the Council will continue to take all practical steps to protect its investment portfolio. In this respect emphasis remains in this order of priority:

   - **Security:** which includes the following, some of which might appear contradictory:
     - Reducing risk in order to protect the return of capital sums, particularly in relation to the Council's investments;
     - The repayment of the sums invested ; and / or
     - Attempting as far as possible, within the parameters of this document, a total return equal to or higher than the prevailing rate of inflation.

   - **Liquidity:** availability of cash when needed (adequate but not excessive liquidity).

   - **Yield:** a return commensurate with the level of risk.

7. Harlow Council has embarked on a number of major projects which will deplete surplus cash held. It is anticipated that, during 2019/20, the Council will need to undertake external borrowing.

Introduction

8. Treasury management is the management of the Council's cash flows, borrowing and investments, and the associated risks. The Council has invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Council's prudent financial management.

9. Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's 'Treasury Management in the Public Services: Code of Practice 2017 Edition' (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year. This report fulfils the Council's legal obligation under the 'Local Government Act 2003' to have regard to the CIPFA Code.

10. Investments held for service purposes or for commercial profit are considered in a different report, the 'Investment Strategy' (Appendix D).

External Context. (Commentary provided by Arlingclose Ltd.)

11. **Economic background:** The UK's progress negotiating its exit from the European Union, together with its future trading arrangements, will continue to be a major influence on the Council's treasury management strategy for 2020/21. The General election has removed some uncertainty within the market, however following the expected Withdrawal Bill, uncertainties around the future trading relationship with the EU remain.

12. GDP growth rose by 0.4% in the third quarter (Jul – Sep) of 2019 from (-)0.2% in the previous three months with the annual rate falling further below its trend rate to 1.1% from 1.2%. Services, construction and production added positively to growth, by 0.5%, 1.2% and 0.1% respectively, while agriculture recorded a fall of 0.1%. Looking ahead, the Bank of England's Monetary Policy Report (formerly the Quarterly Inflation Report) forecasts economic growth to pick up during 2020 as Brexit-related uncertainties dissipate and provide a boost to business investment helping GDP reach 1.6% in Q4 (Oct-Dec) 2020, 1.8% in Q4 2021 and 2.1% in Q4 2022.

13. The headline rate of UK Consumer Price Inflation remained the same in November 2019 at 1.5% year-on-year, the same as October 2019, however continuing to fall from highs of 2.1% in July and April 2019 as accommodation services and transport continued to contribute to a level of inflation below the Bank of England target of 2%. Labour market data continues to be positive. The International Labour Organisation unemployment rate continues to hold at historic lows at 3.8%, its lowest level since 1975. The 3-month average annual growth rate for pay excluding bonuses rose to 3.5% in November 2019 providing some evidence that a shortage of labour is supporting wages. However, adjusting for inflation this means real wages were only up by 0.9% in October 2019 and only likely to have a moderate impact on household spending.

14. Domestic inflationary pressures have abated, as domestic gas and electricity price freezes have taken effect until 2020. The price of oil has fallen through the year, despite a rise in prices in December 2019. The limited inflationary pressure from real wages will likely keep inflation below the Bank of England target of 2%. The Bank of England maintained Bank Rate to 0.75% in November following a 7-2 vote by the Monetary Policy Committee (MPC). Despite keeping rates on hold, MPC members did confirm that if Brexit uncertainty drags on or global growth fails to recover, they are prepared to cut interest rates as required. Moreover, the downward revisions to some of the growth projections in the Monetary Policy Report suggest the Committee may now be less convinced of the need to increase rates even if there is a Brexit deal.

15. The US economy has continued to perform relatively well compared to other developed nations; however, the Federal Reserve has started to unwind its monetary tightening through 2019. The Federal Reserve has cut rates three times to 1.5% - 1.75%, to stimulate growth as GDP growth has started to fall (to 2.1%).

16. The fallout from the US-China trade war continues which, risks contributing to a slowdown in global economic activity in 2019. Recent suggestions have been an initial compromise and potential unwinding of tariffs; however, this can change quickly. Slow growth in Europe, combined with changes in leadership at the European Central Bank and International Monetary Fund has led to a change of stance in 2019. Quantitative easing has continued and been extended.

17. **Credit outlook:** The recent Bank of England stress tests assessed all seven UK banking groups. The tests scenarios include deep simultaneous recessions in the UK and global economies that are more severe overall than the global financial crisis, combined with large falls in asset prices and a separate stress of misconduct costs. All seven banks passed the test on both a CET1 (Common Equity Tier) ratio and

a leverage ratio basis. Major banks have steadily increased their capital for many years now. However, there are a number of shortcomings in the Bank's approach; timeliness as the results are over 11 months of out date when they are published, being based on end-2018 balance sheets; ringfencing, as the tests ignore the restrictions on transferring capital between ringfenced "retail" banks and non-ringfenced "investment" banks within the larger groups and; coverage – the tests should be expanded to cover a wider range of UK banks and building societies.

18. The Bank of England will seek to address some of these issues in 2020, when Virgin Money / Clydesdale will be added to the testing group and separate tests will be included with ringfenced banks.

19. Challenger banks hit the news headlines in 2019 with Metro Bank and TSB Bank both suffering adverse publicity and falling customer numbers.

20. Looking forward, the potential for a "no-deal" Brexit and/or a global recession remain the major risks facing banks and building societies in 2020/21 and a cautious approach to bank deposits remains advisable.

21. **Interest rate forecast:** The Council's treasury management adviser Arlingclose is forecasting that the Bank Rate will remain at 0.75% until the end of 2022. The risks to this forecast are deemed to be significantly weighted to the downside, particularly given the upcoming general election, the need for greater clarity on Brexit and the continuing global economic slowdown. The Bank of England, having previously indicated interest rates may need to rise if a Brexit agreement was reached, stated in its November Monetary Policy Report and its Bank Rate decision (7-2 vote to hold rates) that the MPC now believe this is less likely even in the event of a deal.

22. Gilt yields have risen but remain at low levels and only some very modest upward movement from current levels are expected based on Arlingclose's interest rate projections. The central case is for 10-year and 20-year gilt yields to rise to around 1.00% and 1.40% respectively over the time horizon, with broadly balanced risks to both the upside and downside. However, short-term volatility arising from both economic and political events over the period is a near certainty.

23. A more detailed economic and interest rate forecast provided by Arlingclose is attached at Annex A.

24. For the purpose of setting the budget, it has been assumed that new investments will be made at an average rate of 1.18%, and that new long-term loans will be borrowed at an average rate of 3%.

Local Context

25. On 31 December 2019, the Council held £211.837m of borrowing and £33.340m of investments. This is set out in further detail at ***Annex B***. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

Table 1: Balance sheet summary and forecast

	31.3.19 Actual £m	31.3.20 Estimate £m	31.3.21 Forecast £m	31.3.22 Forecast £m	31.3.23 Forecast £m
General Fund CFR	53.358	63.254	73.466	80.003	83.905
HRA CFR	187.370	187.370	197.570	205.470	206.270
Total CFR	**240.728**	**250.624**	**271.036**	**285.473**	**290.175**
Less: Other debt liabilities	-	-	-	-	-
Borrowing CFR	**240.728**	**250.624**	**271.036**	**285.473**	**290.175**
Less: External borrowing	(-)211.837	(-)211.837	(-)235.837	(-)252.437	(-)254.737
Internal borrowing	**28.891**	**38.787**	**35.199**	**33.036**	**35.438**
Less: Usable reserves	(-)54.175	(-)47.523	(-)39.042	(-)36.858	(-)39.487
Less: Working capital	(-)6.468	(-)6.350	(-)6.350	(-)6.350	(-)6.350
Investments	**(-)31.752**	**(-)15.086**	**(-)10.193**	**(-)10.172**	**(-)10.399**

26. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

27. The Council has an increasing CFR due to the capital programme, but minimal investments and will therefore be required to borrow up to £46.1m over the forecast period (to March 2024).

28. CIPFA's 'Prudential Code for Capital Finance in Local Authorities' recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Council expects to comply with this recommendation during 2020/21.

29. **Liability benchmark:** To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table 1 above, but that cash and investment balances are kept to a minimum level of £10m at each year-end to maintain sufficient liquidity but minimise credit risk.

Table 2: Liability benchmark

	31.3.19 Actual £m	31.3.20 Estimate £m	31.3.21 Forecast £m	31.3.22 Forecast £m	31.3.23 Forecast £m
Borrowing CFR	240.728	250.624	271.036	285.473	290.175
Less: Usable reserves	(-)54.175	(-)47.523	(-)39.042	(-)36.858	(-)39.487
Less: Working capital	(-)6.368	(-)6.350	(-)6.350	(-)6.350	(-)6.350
Plus: Minimum investments	10.000	10.000	10.000	10.000	10.000
Liability Benchmark	**180.185**	**196.751**	**225.644**	**242.265**	**244.338**

30. Following on from the medium-term forecasts in table 2 above, the long-term liability benchmark assumes capital expenditure funded by borrowing of £46.1m, minimum revenue provision on new capital expenditure based on a 40 year asset life and income, expenditure and reserves all increasing by inflation of 0% a year.

Borrowing Strategy

31. The Council currently holds £211.837m of loans, being the same as the previous year, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that the Council expects to borrow up to £24m in 2020/21. The Council may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £301 million.

32. **Objectives:** The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

33. **Strategy:** Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it remains likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead. Where longer-term loans are utilized, they will be considered in the context of ensuring interest rates will be adequately balanced by income streams associated with the capital investment being financed.

34. By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal/ short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring

borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Council with this ‘cost of carry’ and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2020/21 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

35. The Council has previously raised all of its long-term borrowing from the PWLB but the government increased PWLB rates by 1% in October 2019 making it now a relatively expensive option. The Council will now look to borrow any long-term loans from other sources including banks, pensions and local authorities, and will, subject to advice, investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code.

36. Alternatively, the Council may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

37. In addition, the Council may borrow short-term loans to cover unplanned cash flow shortages, although this eventuality is highly unlikely to occur because the spread of investments provides for sufficient cash liquidity to meet forecast cash flows.

38. **Sources of borrowing:** The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB) and any successor body
- any institution approved for investments (see below)
- any other UK public sector body
- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except Essex County Council Pension Fund)
- capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues.

39. **Other sources of debt finance:** In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as debt liabilities:

- Leasing

- Hire purchase
- Private Finance Initiative
- Sale and leaseback

40. **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to Cabinet and Full Council.

41. **Short-term and variable rate loans**: These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below. Financial derivatives may be used to manage this interest rate risk (see section below).

42. **Debt rescheduling:** The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

Investment Strategy

43. The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's investment balance has ranged between £15.086m and £42.070m. The expenditure profile of the Council is changing dramatically which will mean surpluses available for investment will reduce to about £10m.

44. **Objectives:** The CIPFA Code requires the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than

one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

45. **Negative interest rates:** If the UK enters into a recession in 2020/21, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation has already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

46. **Strategy:** Given the increasing risk and very low returns from short-term unsecured bank investments, the Council will retain diversification into more secure and/or higher yielding asset classes during 2019/20 where cash is identified as available for longer-term investment. This diversification will represent a continuation of the current strategy.

47. **Approved counterparties:** The Council may invest its surplus funds with any of the counterparty types in table 3 below, subject to the cash limits (per counterparty) and the time limits shown.

48. With reduce cash surpluses anticipated to be available, the cash limits assume an investment portfolio between £10m and £20m.

49. Harlow Council's typical day-to-day investments are with local authorities for up to one year. The maximum investment of £4m per local authority in 2019/20 will reduce to £2m from 2020/21 (see below).

Table 3: Approved investment counterparties and limits

Credit rating	**Banks unsecured**	**Banks secured**	**Government**	**Corporates**	**Registered Providers**
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£1m 5 years	£2m 20 years	£2m 50 years	£1m 20 years	£1m 20 years
AA+	£1m 5 years	£2m 10 years	£2m 25 years	£1m 10 years	£1m 10 years
AA	£1m 4 years	£2m 5 years	£2m 15 years	£1m 5 years	£1m 10 years
AA-	£1m 3 years	£2m 4 years	£2m 10 years	£1m 4 years	£1m 10 years
A+	£1m 2 years	£2m 3 years	£1m 5 years	£1m 3 years	£1m 5 years
A	£1m 13 months	£2m 2 years	£1m 5 years	£1m 2 years	£1m 5 years
A-	£1m 6 months	£2m 13 months	£1m 5 years	£1m 13 months	£1m 5 years
None	£0.5m 6 months	n/a	**£2m 25 years**	£50,000 5 years	£1m 5 years
Pooled funds and real estate investment trusts	£4m per fund or trust				

This table must be read in conjunction with the notes below

50. **Credit rating:** Investment limits are set by reference to the lowest published long-term credit rating from a selection of external rating agencies. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

51. **Banks unsecured:** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

52. **Banks secured:** Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

53. **Government:** Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Central Government may, in principle, be made in unlimited amounts for up to 50 years, although tying up the Council's cashflow for such an extensive period is particularly unlikely and an unforeseen occurrence.

54. **Local Authorities:** The Council's day-to-day investment transactions have moved more towards investments with other local authorities rather than banks. Councils have a legal duty to pass a balanced budget, have revenue raising powers, and a lender of last resort in the form of the Public Works Loan Board. In unusual circumstances, the lender is able to recoup the principal sum lent under the Local Government Act 2003, sections 6 and 13. In spite of continued reductions in central government funding, making the setting of budgets and budget monitoring even more challenging, the risk of default remains very low. Where a Council issues a notice under Section 114(3) of the Local Government Finance Act 1988 – as is currently the case with Northamptonshire County Council – then section 115(6) of the Act prevents local authority lending. The local government community is becoming more concerned about some entering into a new field of excessive commercial activity. This Council will exercise a degree of caution and will not lend where it feels the risk is too great. The Council may consider using an investment platform (iDealTrade) which contains qualitative information about borrowers.

55. **Corporates:** Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made either following an external credit assessment or to a maximum of £50,000 per company as part of a diversified pool in order to spread the risk widely.

56. **Registered providers:** Loans and bonds issued by, guaranteed by or secured on the assets of registered providers of social housing and registered social landlords, formerly known as housing associations. These bodies are tightly regulated by the Regulator of Social Housing (in England). As providers of public services, they retain the likelihood of receiving government support if needed.

57. **Pooled funds:** Shares or units in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a

professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity and very low or no volatility will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

58. Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

59. **Operational bank accounts:** The Council may incur operational exposures, for example though current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but are still subject to the risk of a bank bail-in, and balances will therefore be kept below £4m (except over the Christmas period, defined as 20 December to 4 January inclusive when the limit will be £6m). The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

60. **Risk assessment and credit ratings**: Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be recalled or sold at no cost will be, and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

61. Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then only investments that can be withdrawn will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

62. **Other information on the security of investments**: The Council understands that credit ratings are good, but not perfect, predictors of

investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis and advice from the Council's treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.

63. When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

64. **Investment limits**: The Council's revenue reserves available to cover investment losses are forecast to be £47.5m on 31 March 2020. The maximum that will be lent to any one organisation (other than the UK Government) will be £4m. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

65. The cash limits assume an investment portfolio between £10m and £20m. If, as anticipated, the cash holding falls to £12.2m then the approved investment limits will be reduced accordingly on instruction to officers by the Deputy to the Chief Executive and Head of Finance & Property.

Table 4: Investment limits

	Cash limit
Any single organisation, except the UK Central Government	£2m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£2m per group
Any group of pooled funds under the same management	£5m per manager
Negotiable instruments held in a broker's nominee account	£5m per broker
Foreign countries	£2m per country
Registered providers and registered social landlords	£5m in total
Unsecured investments with building societies	£2m in total
Loans to unrated corporates	£2m in total
Money market funds	£20m in total
Real estate investment trusts	£5m in total

66. **Liquidity management:** The Council uses a purpose-built cash flow forecasting spreadsheet to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium-term financial plan and cash flow forecast.

Treasury Management Indicators

67. The Council measures and manages its exposures to treasury management risks using the following indicators.

68. **Interest rate exposures**: This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

Interest rate risk indicator	**Limit**
Upper limit on one-year revenue impact of a 1% rise in interest rates	£113,641
Upper limit on one-year revenue impact of a 1% fall in interest rates	£113,641

69. The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates.

70. **Maturity structure of borrowing:** This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	25%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	100%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

71. Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

72. **Principal sums invested for periods longer than a year:** The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end will be:

Price risk indicator	2020/21	2021/22	2022/23
Limit on principal invested beyond year end	£5m	£5m	£5m

Related Matters

73. The CIPFA Code requires the Council to include the following in its treasury management strategy.

74. **Policy on apportioning interest to the Housing Revenue Account:** On 1 April 2012, the Council notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/ credited to the respective revenue account. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured each month and interest transferred between the General Fund and HRA at the Council's average interest rate on investments, adjusted for credit risk.

75. **Policy on the use of Financial Derivatives:** Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the 'Localism Act 2011'

removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

76. The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

77. Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

78. In line with the CIPFA Code, the Council will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.

79. **Markets in Financial Instruments Directive**: The Council has opted up to professional client status with its providers of financial services, including advisers, brokers and fund managers, allowing it access to a smaller range of services but with the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Deputy to the Chief Executive and Head of Finance & Property believes this to be the most appropriate status.

Financial Implications

80. The budget for investment income in 2020/21 is £149,000, based on an average investment portfolio of £12.6 million at an interest rate of 1.179%. The budget for debt interest paid in 2020/21 is £7.729 million, based on an average debt portfolio of £235.837 million at an average interest rate of 3.31%. If actual levels of investments and borrowing, or actual interest rates, differ from those forecast, performance against budget will be correspondingly different.

Other Options Considered

81. The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Deputy to the

Chief Executive and Head of Finance & Property, having consulted the Portfolio Holder (Resources), believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	**Impact on income and expenditure**	**Impact on risk management**
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

Annex A – Arlingclose Economic & Interest Rate Forecast November 2019.

Underlying assumptions:

1. The global economy is entering a period of slower growth in response to political issues, primarily the trade policy stance of the US. The UK economy has displayed a marked slowdown in growth due to both Brexit uncertainty and the downturn in global activity. In response, global and UK interest rate expectations have eased.

2. Some positivity on the trade negotiations between China and the US has prompted worst case economic scenarios to be pared back. However, information is limited, and upbeat expectations have been wrong before.

3. Brexit has been delayed until 31 January 2020. While the General Election has maintained economic and political uncertainty, the opinion polls suggest the Conservative position in parliament may be strengthened, which reduces the chance of Brexit being further frustrated. A key concern is the limited transitionary period following a January 2020 exit date, which will maintain and create additional uncertainty over the next few years.

4. UK economic growth has stalled despite Q3 (Jul-Sep) 2019 GDP of 0.3%. Monthly figures indicate growth waned as the quarter progressed and survey data suggest falling household and business confidence. Both main political parties have promised substantial fiscal easing, which should help support growth.

5. While the potential for divergent paths for UK monetary policy remain in the event of the General Election result, the weaker external environment severely limits potential upside movement in Bank Rate, while the slowing UK economy will place pressure on the MPC to loosen monetary policy. Indeed, two MPC members voted for an immediate cut in November 2019.

6. Inflation is running below target at 1.7%. While the tight labour market risks medium-term domestically-driven inflationary pressure, slower global growth should reduce the prospect of externally driven pressure, although political turmoil could push up oil prices.

7. Central bank actions and geopolitical risks will continue to produce significant volatility in financial markets, including bond markets.

Forecast:

8. Although we have maintained our Bank Rate forecast at 0.75% for the foreseeable future, there are substantial risks to this forecast, dependant on General Election outcomes and the evolution of the global economy.

9. Arlingclose judges that the risks are weighted to the downside.

10. Gilt yields have risen but remain low due to the soft UK and global economic outlooks. US monetary policy and UK government spending will be key influences alongside UK monetary policy.

11. We expect gilt yields to remain at relatively low levels for the foreseeable future and judge the risks to be broadly balanced.

	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Average
Official Bank Rate														
Upside risk	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.21**
Arlingclose Central Case	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**
Downside risk	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	**-0.73**
3-month money market rate														
Upside risk	0.10	0.10	0.25	0.25	0.25	0.25	0.25	0.25	0.30	0.30	0.30	0.30	0.30	**0.25**
Arlingclose Central Case	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**
Downside risk	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	**-0.73**
1yr money market rate														
Upside risk	0.10	0.20	0.20	0.20	0.20	0.20	0.20	0.25	0.30	0.30	0.30	0.30	0.30	**0.23**
Arlingclose Central Case	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**
Downside risk	-0.30	-0.50	-0.55	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	**-0.60**
5yr gilt yield														
Upside risk	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.45	0.45	0.45	**0.37**
Arlingclose Central Case	**0.50**	**0.50**	**0.50**	**0.55**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.57**
Downside risk	-0.35	-0.50	-0.50	-0.55	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	**-0.56**
10yr gilt yield														
Upside risk	0.30	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.45	0.45	**0.37**
Arlingclose Central Case	**0.75**	**0.75**	**0.80**	**0.80**	**0.85**	**0.85**	**0.90**	**0.90**	**0.95**	**0.95**	**1.00**	**1.00**	**1.00**	**0.88**
Downside risk	-0.40	-0.40	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.45**
20yr gilt yield														
Upside risk	0.30	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.45	0.45	**0.37**
Arlingclose Central Case	**1.20**	**1.20**	**1.25**	**1.25**	**1.25**	**1.30**	**1.30**	**1.30**	**1.35**	**1.35**	**1.35**	**1.40**	**1.40**	**1.30**
Downside risk	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.50	-0.50	**-0.45**
50yr gilt yield														
Upside risk	0.30	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.45	0.45	**0.37**
Arlingclose Central Case	**1.20**	**1.20**	**1.25**	**1.25**	**1.25**	**1.30**	**1.30**	**1.30**	**1.35**	**1.35**	**1.35**	**1.40**	**1.40**	**1.30**
Downside risk	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.50	-0.50	**-0.45**

PWLB Certainty Rate (Maturity Loans) = Gilt yield + 1.80%
PWLB Local Infrastructure Rate (Maturity Loans) = Gilt yield + 0.60%

Annex B – Existing Investment & Debt Portfolio Position

	31.12.19 Actual Portfolio £m	31.12.19 Average Rate %
External borrowing:		
Public Works Loan Board	**211.837**	**3.31%**
Total external borrowing	**211.837**	**3.31%**
Other long-term liabilities:	-	-
Total gross external debt	211.837	3.31%
Treasury investments:		
Banks & building societies (unsecured)	(-)2.360	0.50%
Government (incl. local authorities)	(-)14.500	0.83%
Money Market Funds	(-)12.870	0.69%
Other pooled funds:		
Property Fund	(-)2.000	4.50%
Cash Plus Fund	(-)2.000	0.75%
Total treasury investments	(-)33.730	0.97%
Net debt	178.107	

<u>Mortgage and other loans rate</u>

Schedule 16 of the Housing Act 1985 specifies that Councils must set the interest rate on mortgages arranged since October 1985 on an annual basis. Councils are required to charge the higher of:

i. The Standard National Rate, which is set by the Secretary of State (currently 3.13%), or,
ii. The applicable local average rate, based on the Council's own borrowing costs and a small percentage (0.25%) for administration.

The interest rate chargeable is therefore 3.56%.

Annex C
Treasury Management Scheme of Delegation

(i) Full Council

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.

(ii) Cabinet

- review of/ amendments to the Council's adopted clauses and Treasury Management Strategy Statement and making associated recommendations to Full Council;
- budget consideration and recommendation to Full Council;
- approval of the division of responsibilities;
- receiving ad hoc treasury management monitoring reports and acting on recommendations.

(iii) Portfolio Holder for Resources

- receiving and reviewing regular monitoring reports and making recommendations to Cabinet;
- reviewing the treasury management policy and procedures and making recommendations to the Cabinet;
- reviewing the treasury management practices;
- approving the selection of external service providers and agreeing terms of appointment in conjunction with normal contract approval procedures.

(iv) Section 151 Officer

- recommending clauses, treasury management policy for approval, reviewing the same regularly, and monitoring compliance;
- setting treasury management practices;
- 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, skills and training, 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.

Annex D
Credit Ratings Table

The Credit Ratings Table has been included as an annex in order to assist with understanding of the ratings referred to within the TMSS. Generally the Council will invest in 'High Grade' or 'Upper Medium Grade' investments.

	Moody's	S&P	Fitch	Meaning
Investment Grade	Aaa	AAA	AAA	Prime
	Aa1	AA+	AA+	High Grade
	Aa2	AA	AA	
	Aa3	AA-	AA-	
	A1	A+	A+	Upper Medium Grade
	A2	A	A	
	A3	A-	A-	
	Baa1	BBB+	BBB+	Lower Medium Grade
	Baa2	BBB	BBB	
	Baa3	BBB-	BBB-	
Junk	Ba1	BB+	BB+	Non Investment Grade Speculative
	Ba2	BB	BB	
	Ba3	BB-	BB-	
	B1	B+	B+	Highly Speculative
	B2	B	B	
	B3	B-	B-	
	Caa1	CCC+	CCC+	Substantial Risks
	Caa2	CCC	CCC	Extremely Speculative
	Caa3	CCC-	CCC-	In Default w/ Little Prospect for Recovery
	Ca	CC	CC+	
		C	CC	In Default
			CC-	
	D	D	DDD	

Annex E
Glossary of Terms and Definitions

Bank Rate:
The term 'Bank Rate' is 'the official Bank Rate paid on commercial bank reserves', i.e. reserves placed by commercial banks with the Bank of England as part of the Bank's operations to reduce volatility in short term interest rates in the money markets. Previously referred to as "repo rate" this term has been replaced as a result of the change in terminology used by the Bank of England as from May 2006

Base Rate:
The term Base Rate refers to the rate which is set by each high street bank; it is the key foundational rate on which they each base all their various lending rates to customers. It is normally set at the same rate as the Bank Rate (q.v.) and changes in line with, and very soon after changes in Bank Rate.

BRRD: 'Bank Recovery and Resolution Directive'

CD: see 'Certificate of deposit'.

CDS: see 'Credit Default Swaps'

CFR: see 'Capital Financing Requirement'

CP: see 'Commercial paper'.

CRA: see 'Credit Rating Agency'.

Call Account: 'Call account' is a bank deposit where funds can be withdrawn at any time.

Callable Deposit
Placing a deposit with a bank or building society at a set rate for a set amount of time. However, the borrower has the right to repay the funds on pre agreed dates before maturity. This decision is based upon how market rates have moved since the deal was agreed. If rates have fallen, the likelihood of the deposit being repaid rises, as cheaper money can be found by the borrower.

Capital Financing Requirement
The Capital Financing Requirement reflects the Council's underlying need to borrow for capital purposes. Thus, if new capital expenditure is incurred and not financed from sources other than by borrowing, the CFR will increase by the amount of that expenditure. Borrowing, up to the value of the CFR, may be either from internal cash balances or externally, such as from the Public Works Loan Board (q.v.).

Certificate of Deposit
A certificate of deposit is an unsecured investment issued by a bank or building society which is a fixed deposit, giving a guaranteed interest return. These differ from term deposits in that the lender is not obliged to hold the investment through to maturity and may realise the cash by selling the CD into an active secondary market. This may be useful in instances where the counterparty receives a downgraded credit rating, or the investor encounters an unexpected cashflow issue. CDs are obtained through specialist brokers who deal through the primary and secondary market. CDs offer liquidity and greater access to counterparties who do not trade in term deposits.

CIPFA: Chartered Institute of Public Finance and Accountancy.

CIPFA Treasury Management Code of Practice
This represents official practitioners' guidance, which is produced by CIPFA. The government expects Councils and other public service authorities to adopt and comply with the code. The recommendations made in the Code provide a basis for all these public service organisations to create clear treasury management objectives and to structure and maintain sound treasury management policies and practices.

CLG: Department of Communities and Local Government.

Commercial Paper
Short-term obligations with maturities ranging from 2 to 270 days issued by banks, corporations and other borrowers. Such instruments are unsecured and usually discounted, although some may be interest bearing.

Corporate Bond
Strictly speaking, corporate bonds are those issued by companies. However, the term is used to cover all bonds other than those issued by governments in their own currencies and includes issues by companies, supranational organisations and government agencies

Counterparty
A counterparty is a party with which a transaction is done.

CPI: Consumer Prices Index

Credit Default Swaps
A CDS is a contract between two counterparties in which the buyer of the contract makes quarterly payments to the seller of the contract in exchange for a payoff if there is a credit event (e.g. default) of the reference entity (i.e. the third party on whom the contract is based). The contract essentially provides a means of insurance to the buyer of the CDS against default by a borrower. The "spread" (effectively the premium paid by the CDS buyer) provides an indication of the perceived risk of a default occurring.

Credit Rating
A credit rating is an estimate of the quality of a debt from the lender viewpoint in terms of the likelihood of interest and capital not being paid and of the extent to which the lender is protected in the event of default.

An individual, a firm or a government with a good credit rating can borrow money from financial institutions more easily and cheaply than those who have a bad credit rating.

Credit Ratings are evaluated by Credit Rating agencies (q.v.).

Credit rating agency
'Credit rating agency', or 'rating agency', or CRA, is a firm that issues opinions on companies' ability to pay back their bonds. These opinions are often abbreviated on an alphanumeric scale ranging from AAA to C (or equivalent). The three CRAs used by the Council are Fitch, Moody's and Standard and Poor's.

DMADF: see 'Debt Management Agency Deposit Facility'

DMO: see 'Debt Management Office'

Dealing
Is the process of carrying out transactions with a counterparty (q.v.), including agreeing the terms of an investment. This is usually conducted through a broker.

Debt Management Agency Deposit Facility
Deposit Account offered by the Debt Management Office (q.v.), guaranteed by the UK government.

Debt Management Office
The Debt Management Office (DMO) is an executive agency of HM Treasury responsible for carrying out the government's debt management policy and managing the aggregate cash needs of the Exchequer. It is also responsible for lending to local authorities and managing certain public sector funds.

Derivative
A contract whose value is based on the performance of an underlying financial asset, index or other investment. e.g. an option is a derivative because its value changes in relation to the performance of an underlying stock.

ECB: European Central Bank

Equity
A share in a company with limited liability. It generally enables the holder to share in the profitability of the company through dividend payments and capital gain.

EU: European Union

Fed: The Federal Reserve (US)

FLS: Funding for Lending Scheme

Floating Rate Notes
Bonds on which the rate of interest is established periodically with reference to short-term interest rates

Forward Deal
The act of agreeing today to deposit funds with an institution for an agreed time limit, on an agreed future date, at an agreed rate.

Forward Deposits: see ‘forward deal’

Fund Manager
The individual responsible for making decisions related to any portfolio of investments in accordance with the stated goals of the fund.

GDP: Gross Domestic Product

Gilt
Registered British government securities giving the investor an absolute commitment from the government to honour the debt that those securities represent.

Gilt Funds
Pooled fund investing in bonds guaranteed by the UK government.

HRA: Housing Revenue Account

HRACFR: Housing Revenue Account Capital Financing Requirement

iTraxx benchmark
A group of international credit derivative indexes that are monitored by the International Index Company (IIC). The credit derivatives market that iTraxx provides allows parties to transfer the risk and return of underlying assets from one party to another without actually transferring the assets. iTraxx indexes cover credit derivatives markets in Europe, Asia and Australia.

Lender Option Borrower Option
'Lender Option Borrower Option' (LOBO) is a floating rate instrument which allows the lender to designate an adjustment rate at periodic reset dates and lets the borrower decide whether to pay the rate or redeem the bond.

Liquidity
Liquidity refers to an asset that can be turned into cash or the ability to quickly sell or buy an asset

LIBID: see 'London Interbank Bid Rate'

LIBOR: see 'London Interbank Offer Rate'

LOBO: see 'Lender Option Borrower Option'

London Interbank Bid Rate
The 'London Interbank Bid Rate' (LIBID) is the rate of interest at which first-class banks in London will bid for deposit funds. Often used as a benchmark for deposit rates. LIBID is not fixed in the same way as LIBOR (q.v.), but is typically one-sixteenth to one-eighth of a per cent below LIBOR.

London Interbank Offer Rate
'London Interbank Offer Rate' (LIBOR) is the interest rate which banks pay when lending to each other. It is calculated at a specified time each day and based on what it would cost a panel of banks to borrow funds for various periods of time and in various currencies. It then creates an average of the individual banks' figures.

Markets in Financial Instruments Directive II
New client classification rules were introduced from 3 January 2018 as a result of the UK's implementation of the second Markets in Financial Instruments Directive (MiFID II). Local authorities were transferred to 'client status' unless it requested to institutions to continue to be treated as a professional client in respect of all the regulated financial services that are provided.

MHCLG: Ministry of Housing, Communities and Local Government

MiFID II: see Markets in Financial Instruments Directive II

MMF: see 'Money Market Fund'

Money Market Fund
Money Market Funds are mutual funds that invest in short-term debt instruments. They provide the benefits of pooled investment, as investors can participate in a more diverse and high-quality portfolio than they otherwise could individually. Like other mutual funds, each

investor who invests in a money market fund is considered a shareholder of the investment pool, a part owner of the fund. Money market funds are actively managed within rigid and transparent guidelines to offer safety of principal, liquidity and competitive sector-related returns. It is very similar to a unit trust, however, in a MMF equities are replaced by cash instruments. Returns are typically around 1 month LIBID (q.v.), and the average maturity is generally below 60 days.

MPC: Monetary Policy Committee

MRP: Minimum Revenue Provision, for the repayment of debt.

Open Ended Investment Companies (OEIC)
Investment funds that partly resemble an investment trust and partly a unit trust. Like investment trusts, they issue shares on the London Stock Exchange and invest money raised from shareholders in other companies. The term open-ended means that when demand for the shares rises the fund manager just issues more shares, instead of there being a rise in the share price. The price of OEIC shares is determined by the value of the underlying assets of the fund.

Other Bond Funds
Pooled funds investing in a wide range of bonds.

PWLB: see 'Public Works Loan Board'

Programme of Development
The balance of Programme of Development funding (POD) represents monies received from Central Government for regeneration in the east of England, and is held by the Council on behalf of a Partnership comprising local councils and partners from the third and private sectors. The funding was received after a series of successful bids by the Partnership.

Public Works Loan Board
The Public Works Loan Board (PWLB) is a UK Government statutory body whose function is to lend money from the National Loans Fund to Councils and other public bodies and to collect the repayments.

Rating Agency: see 'Credit Rating Agency'

Repo: see 'Repurchase Agreement'

Repurchase Agreement
'Repurchase agreement', or repo, is a contract where the seller of certain securities agrees to buy them back from the purchaser at a specified time for an agreed price.

Reverse Gilt Repo
This is a transaction as seen from the point of view of the party which is buying the gilts. In this case, one party buys gilts from the other and, at the same time and as part of the same transaction, commits to resell equivalent gilts on a specified future date, or at call, at a specified price.

Sovereign Issues (Ex UK Gilts)
Bonds issued or guaranteed by nation states, but excluding UK government bonds.

Supranational Bonds
Bonds issued by supranational bodies, e.g. European Investment Bank. These bonds – now known as Multilateral Development Bank bonds – are generally AAA rated and behave similarly to gilts, but pay a higher yield ("spread") given their relative illiquidity when compared with gilts.

T-bills: see 'Treasury Bills'.

Term Deposit
(or 'Time deposit') is a generic term for a bank deposit where funds cannot be withdrawn for a fixed period of time. The lender receives a fixed rate of interest. These are unsecured investments and place the lender at risk of bail-in should this occur during the term of the investment.

Time Deposit: see 'Term Deposit'

Treasury Bills
Treasury bills are a AAA/AA+ rated, short-dated form of Government debt, issued by the Debt Management Office (q.v.), via a weekly tender, on a Friday. Lenders would use the services of a specialist broker to access the market. These usually have a maturity of one, three or six months and provide a return to the investor by virtue of being issued at a discount to their final redemption value. There is also an active secondary market for T-bills which means that lending may be available for a range of dates. Interest rates tend to be higher than the DMADF (q.v.).

Treasury Management Strategy
This is the Council's overall policy and framework by which it will carry out that policy in relation to its borrowing and investment needs in the coming financial year.

Treasury Management Policy Statement
This is the Council's statement of intention in respect of its treasury management. It is prescribed by the CIPFA Treasury Management Code of Practice (q.v.).

Variable Rate Asset Value
'Variable Rate Asset Value' (VNAV) occurs where the net asset value, or principal sum, invested may change depending on trading conditions. The value is calculated at the end of the business day based on the value of investments less any liabilities divided by the number of shares outstanding. With investments carrying this attribute, the capital sum invested may not be equal to the capital sum repaid.

VNAV: see 'Variable Net Asset Value'.

Weighted Average Maturity
'Weighted average maturity', or WAM, is used to measure interest rate risk. WAM is calculated by taking the maturity of the underlying money market instruments held by the fund, weighted according to the relative holdings per instrument.

APPENDIX D

Investment Strategy Report 2020/21

Introduction

1. The Council invests its money for three broad purposes:
   - because it has surplus cash as a result of its day-to-day activities, for example when income is received in advance of expenditure (known as **treasury management investments**),
   - to support local public services by lending to other organisations (**service investments**), and
   - to earn investment income (known as **commercial investments** where this is the main purpose).

2. This investment strategy meets the requirements of statutory guidance issued by the government in January 2018, and focuses on the second and third of these categories.

Treasury Management Investments

3. The Council typically receives its income in cash (e.g. from taxes and grants) before it pays for its expenditure in cash (e.g. through payroll and invoices). It also holds reserves for future expenditure and collects local taxes on behalf of other local authorities and central government. These activities, plus the timing of borrowing decisions, lead to a cash surplus which is invested in accordance with guidance from the Chartered Institute of Public Finance and Accountancy. The balance of treasury management investments is expected to fluctuate between £10m and £20m during the 2020/21 financial year.

4. **Contribution:** The contribution that these investments make to the objectives of the Council is to support effective treasury management activities.

5. **Further details:** Full details of the Council's policies and its plan for 2020/21 for treasury management investments are covered in a separate document, the 'Treasury Management Strategy' (Appendix C).

Service Investments: Loans

6. **Contribution:** The Council lends money to its subsidiary and a local business, to support local public services and stimulate local economic growth.

7. HTS (Property and Environment) Ltd is a wholly owned subsidiary of Harlow Council which began trading on 1 February 2017. The Council provided a start-up loan to the business of £1.209m repayable over five years, two months, approved on 21 July 2016. The balance outstanding as at 31 March 2019 was £0.702m. The company is also in the process of replacing plant and equipment for which the Cabinet has agreed a further loan of £670,000 likely to be drawn down in early 2020.

8. Harlow Property Limited was provided with two loans to support the development of a part of the Harlow Enterprise Zone, approved on 23 January 2014. The amounts loaned were £1m on 15 March 2016 and a further £1.5m on 3 March 2017. Interest accrues on these loans. The total outstanding as at 31 March 2019 was £2.800m.

9. **Security:** The main risk when making service loans is that the borrower will be unable to repay the principal lent and/or the interest due. In order to limit this risk, and ensure that total exposure to service loans remains proportionate to the size of the Council, upper limits on the outstanding loans to each category of borrower have been set as follows:

Table 1: Loans for service purposes in £ millions

Category of borrower	**31.3.2019 Actual**			**2020/21**
	Balance owing	**Loss allowance**	**Net figure in accounts**	**Approved Limit**
Subsidiaries	0.702	-	0.702	1.500
Local businesses	2.800	-	2.800	3.100
Local residents	0.021	-	0.021	0.100
TOTAL	**3.523**	**-**	**3.523**	**4.700**

10. Accounting standards require the Council to set aside loss allowance for loans, reflecting the likelihood of non-payment. The Council considers that this loss should be zero because, (1) HTS is the sole shareholder of the Council; (2) HPL loans are a charge secured against property which considerably exceeds the value of the loan.

Commercial Investments: Property

11. The Ministry of Housing, Communities and Local Government (MHCLG) defines property to be an investment if it is held primarily or partially to generate a profit.

12. **Contribution:** The Council has historically held nine commercial and residential properties with the intention of making a profit that will be spent on

local public services. These include a Golf Club, and three other properties. Annual income from all these assets is about £82,000.

Table 2: Property held for investment purposes in £ millions

Property	Actual	31.3.2019 Actual		31.3.2020 expected	
	Value	Gains or (losses)	Value in accounts	Gains or (losses)	Value in accounts
Golf Club	0.782	-	0.782	-	0.782
Stewards Farm	0.329	-	0.329	-	0.329
Barrow Farm Cottage	0.143	-	0.143	-	0.143
Canons Cottage	0.086	-	0.086	-	0.086
TOTAL	**1.340**	**-**	**1.340**	**-**	**1.340**

Loan Commitments and Financial Guarantees

13. Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees carry similar risks to the Council and are included here for completeness.

14. In 1987 and 1992 the Council agreed to undertake joint liability with a number of other local authorities to guarantee loans of £66.3 million and £17.3 million to Home Housing Association (previously called North Housing Association) in support of their private initiative for the provision of housing in Harlow and surrounding authorities. The guarantee is for a 50-year period ending 2037. The Council's proportion of the total liability is £4.5 million. The Council considers that the probability of the guarantee being called upon is low.

Capacity, Skills and Culture

15. **Elected members and statutory officers**: Strategic investment decisions are subject to the advice from officers or treasury management advisors. Elected members are also invited to formal or informal training. The process is subject to scrutiny through the Overview Working Group, Cabinet and Full Council.

Investment Indicators

16. The Council has set the following quantitative indicators to allow elected members and the public to assess the Council's total risk exposure as a result of its investment decisions.

17. **Total risk exposure:** The first indicator shows the Council's total exposure to potential investment losses. This includes amounts the Council is

contractually committed to lend but have yet to be drawn down and guarantees the Council has issued over third party loans.

Table 3: Total investment exposure in £millions

Total investment exposure	31.03.2019 Actual	31.03.2020 Forecast	31.03.2021 Forecast
Treasury management investments	31.752	15.086	10.193
Service investments: Loans	3.523	4.700	4.500
Service investments: Shares	-	-	-
Commercial investments: Property	1.340	1.340	1.340
TOTAL INVESTMENTS	**36.615**	**21.126**	**16.033**

18. **How investments are funded:** Government guidance is that these indicators should include how investments are funded. Since the Council does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. However, the following investments could be described as being funded by borrowing. The remainder of the Council's investments are funded by usable reserves and income received in advance of expenditure.

Table 4: Investments funded by borrowing in £millions

Investments funded by borrowing	31.03.2019 Actual	31.03.2020 Forecast	31.03.2021 Forecast
Treasury management investments	Nil	Nil	Nil
TOTAL FUNDED BY BORROWING	**Nil**	**Nil**	**Nil**

19. **Rate of return received:** This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested. Note that due to the complex local government accounting framework, not all recorded gains and losses affect the revenue account in the year they are incurred.

Table 5: Investment rate of return (net of all costs)

Investments net rate of return	2018/19 Actual	2019/20 Forecast	2020/21 Forecast
Treasury management investments	0.83%	1.01%	1.18%
Service investments: Loans	4.53%	4.53%	4.53%
Commercial investments: Property	6.12%	6.12%	6.12%

APPENDIX E

Minimum Revenue Provision Statement 2020/21

1. Where the Council finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The 'Local Government Act 2003' requires the Council to have regard to the Ministry of Housing, Communities and Local Government's 'Guidance on Minimum Revenue Provision' (the MHCLG Guidance), with revisions relating to MRP most recently issued in 2018.

2. The broad aim of the MHCLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

3. The MHCLG Guidance requires the Council to approve an Annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP. The following statement incorporates options recommended in the Guidance.

4. For capital expenditure incurred before 1 April 2008, and for supported capital expenditure incurred on or after that date, MRP will be determined in accordance with the former regulations that applied on 31 March 2008. For Harlow Council, the adjusted Capital Financing Requirement upon which the MRP is calculated is negative in each year prior to April 2008. The MRP on this portion of CFR is therefore zero. *(Option 1 in England & Wales)*

5. For unsupported capital expenditure incurred after 31 March 2008, with the exception of pump-priming economic development (defined below), MRP will be determined by charging the expenditure over the expected useful life of the relevant asset in equal instalments, starting in the year after the asset becomes operational. *(Option 3, the "Asset Life method", in England and Wales)*

6. Economic development is defined as the following capital expenditure projects: Prentice Place and the Enterprise Zone.

7. For assets acquired by finance leases, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.

8. Minimum Revenue Provision will not be made in relation to the following specific circumstances:

- Capitalised loan advances to other organisations or individuals. Instead of MRP, the capital receipts arising from the capitalised loan repayments will be used as provision to repay debt. However, revenue MRP contributions would still be required equal to the amount of any impairment of the loan advanced.
- Any capital investment made in projects aligned with Harlow's Enterprise Zone where third party funding is guaranteed to meet the costs of that investment (repayment of debt principal and interest) and borrowing has been aligned with the life of the designated enterprise zone.
- The Housing Revenue Account (HRA) is not subject to a statutory requirement to make a minimum revenue provision payment, and is not currently doing so.

9. Capital expenditure incurred during 2020/21 will not be subject to a MRP charge until 2021/22.

10. Based on the Council's latest estimate of its Capital Financing Requirement (CFR) on 31 March 2020, the budget for MRP has been set as follows:

	31.03.2020 Estimated CFR £m	**2020/21 Estimated MRP £**
Capital expenditure before 01.04.2008	**5.455**	0
Capital expenditure after 31.03.2008	**57.799**	305,000
Total General Fund	**63.254**	**305,000**
Assets in the Housing Revenue Account	**187.370**	0
Total Housing Revenue Account	**187.370**	**0**
Total	**250.624**	**305,000**