

Title of report: Treasury Policy Statement and Treasury Strategy 2021/22 to 2025/26

Report of: Darren Collins – Strategic Director, Resources and Digital

Purpose of the Report

1. This report asks the Audit and Standards Committee to review the proposed Treasury Policy Statement and Treasury Strategy for 2021/22 to 2025/26 prior to consideration by Cabinet.

Background

2. To provide a framework for the Strategic Director, Resources and Digital to exercise his delegated powers, the Council agrees a five-year Treasury Management Policy and Treasury Strategy which is reviewed at the start of each financial year.
3. The attached Treasury Policy and Treasury Strategy have been prepared considering the Local Government Act 2003, Ministry of Housing, Communities and Local Government 's (MHCLG) Guidance on Local Government Investments, CIPFA's Prudential Code for Capital and CIPFA's Code of Practice on Treasury Management (2017).

Proposals

4. The Committee is asked to review the Treasury Policy and Treasury Strategy attached at Appendix 1 and Appendix 2, to ensure that the Council fully complies with the requirements of good financial practice in Treasury Management.

Recommendation

5. The Committee is asked to review the recommendations on the Treasury Policy and the Treasury Strategy and submit any comments to Cabinet.

For the following reason:

- To ensure that the Council fully complies with the requirements of good practice as recommended by the Local Government Act 2003, the Chartered Institute of Public Finance and Accountancy (CIPFA) in its Code of Practice on Treasury Management and Prudential Code for Capital (2017) and the Ministry of Housing, Communities and Local Government (MHCLG), Guidance on Local Government Investments.

Treasury Policy 2021/22 to 2025/26

1. Approved Activities of the Treasury Management Operation

- 1.1 In December 2017 CIPFA published a revised Code of Practice on Treasury Management in the Public Services (the Code), which represents best practice. Treasury management activities are defined by CIPFA as:

“The management of the organisation’s borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.”

- 1.2 The term “investments” used in the definition of treasury management activities includes all financial assets of the organisation, as well as other non-financial assets which the Council may hold primarily for financial returns. The control of risk and optimising returns on these more commercial investments is also consistent with the Council’s risk appetite.
- 1.3 The Council currently provides a treasury management service to the Gateshead Housing Company through a Service Level Agreement. This service will cease on 31st March 2021 when the Gateshead Housing Company is integrated back into the council.

2. Formulation of the Treasury Strategy

- 2.1 The formulation of a Treasury Strategy involves determining the appropriate borrowing and investment decisions with the prime objective of safeguarding the Council’s assets and secondary objectives of obtaining a reasonable rate of return on investments and minimising the costs of borrowing. Accordingly, the analysis and reporting of treasury management activities will focus on the risk implications for the Council and ensure robust due diligence procedures cover all treasury and non-treasury investments.
- 2.2 The Treasury Strategy encompasses the requirements of CIPFA’s Treasury Management Code of Practice, Prudential Code for Capital and the MHCLG Guidance on Local Government Investments.
- 2.3 The Strategy for 2021/22 to 2025/26 is attached at Appendix 2.

3. Prudential and Treasury Indicators

- 3.1 Under Part 1 of the Local Government Act 2003 the Council may borrow money (a) for any purpose relevant to its functions under any enactment, or (b) for the purposes of the prudent management of its financial affairs.
- 3.2 Under the requirements of the Prudential Code and Treasury Management Code of Practice the Council have adopted prudential indicators (detailed in Appendix 2, section 1.4).

4. Annual Investment Strategy

- 4.1 The MHCLG has issued guidance to supplement the investment regulations contained within the Local Government Act 2003. It is also referred to under Section 15 (1) of the 2003 Local Government Act which requires authorities to “have regard (a) to such guidance as the Secretary of State may issue and (b) to such other guidance as the Secretary of State may by regulations specify”. The guidance encourages authorities to invest prudently but without burdening them with the detailed prescriptive regulation of the previous regime.
- 4.2 Central to the guidance and the Code is the need to produce an Annual Investment Strategy. This is included as Section 6 of the Treasury Strategy in Appendix 2.
- 4.3 The Annual Investment Strategy document will include:
- The Council’s risk appetite in respect of security, portfolio liquidity and return;
 - The definition of ‘high’ and ‘non-high’ credit quality to determine what are specified investments and non-specified investments;
 - Which specified and non-specified instruments the Council will use, dealing in more detail with non-specified investments given the greater potential risk;
 - The categories of counterparties that may be used during the course of the year e.g. foreign banks, nationalised/part nationalised banks, building societies;
 - The types of investments that may be used during the course of the year;
 - The limit to the total amount that may be held in each investment type;
 - The Council’s policy on the use of credit ratings, credit rating agencies and other credit risk analysis techniques to determine creditworthy counterparties for its approved lending list and how the Council will deal with changes in ratings, rating watches and rating outlooks;
 - Limits for individual counterparties, groups and countries;
 - Guidelines for making decisions on investments and borrowing; and
 - The Council’s policy on commercial investments held for return.

5. Policy on Interest Rates Exposure

- 5.1 The use of any financial instruments, such as derivatives, to mitigate interest rate risks will be considered on an individual basis and the Strategic Director, Resources and Digital, will obtain approval from the Council prior to entering into any arrangement of this nature.

6. Policy on Delegation, Review Requirements and Reporting Arrangements

- 6.1 It is the Council’s responsibility under the Code to approve a Treasury Policy statement.
- 6.2 The Council delegates the review of the policy and monitoring of the performance of the treasury management function to Cabinet, the scrutiny of treasury management strategy and policies to the Audit and Standards Committee, and the execution and administration of treasury management decisions to the Strategic Director, Resources and Digital, who will act in accordance with the organisations policy statement and TMPs and CIPFA’s Standard of Professional Practice on Treasury Management. Any proposals to approve, adopt or amend policy require the consent of the Council and are matters for the Council to determine.
- 6.3 Treasury Strategy (Appendix 2, Section 1.3) outlines the Council’s arrangements for reporting on Treasury Management.

- 6.4 As from 1st April 2019, CIPFA required all local authorities to prepare an additional report, a Capital Strategy report, which is intended to provide the following: -
- a) a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services;
 - b) an overview of how the associated risk is managed; and
 - c) the implications for future financial sustainability.
- 6.5 The aim of this report is to ensure that all elected members of the Council fully understand the overall strategy, governance procedures and risk appetite entailed by this Strategy.
- 6.6 The Capital Strategy 2021/22 to 2025/26 was approved by Cabinet on 17th November 2020.

Treasury Strategy 2021/22 to 2025/26

1. Introduction

1.1 The CIPFA Code of Practice on Treasury Management 2017 (the Code) emphasises a number of key areas including the following:

- a) All authorities must formally adopt the Code.
- b) The strategy report will affirm that the effective management and control of risk are prime objectives of the Council's treasury management activities.
- c) The Council's appetite for risk, including the appetite for any use of financial instruments in the prudent management of those risks, must be clearly identified within the strategy report and will affirm that priority is given to security and portfolio liquidity when investing treasury management funds and explain how that will be carried out.
- d) Responsibility for risk management and control lies within the organisation and cannot be delegated to any outside organisation.
- e) Credit ratings should only be used as a starting point when considering risk. Use should also be made of market data and information, the quality financial press, information on government support for banks and the credit ratings of that government support.
- f) Councils need a sound diversification policy with high credit quality counterparties and should consider setting country, sector and group limits.
- g) Borrowing in advance of need is only to be permissible when there is a clear business case for doing so and only for the current capital programme or to finance future debt maturities.
- h) The main annual treasury management reports must be approved by full Council.
- i) There needs to be a mid-year review of Treasury Management Strategy and performance. This is intended to highlight any areas of concern that have arisen since the original strategy was approved.
- j) Each council must delegate the role of scrutiny of Treasury Management Strategy and policies to a specific named body.
- k) Treasury Management performance and policy setting should be subjected to prior scrutiny.
- l) Councillors should be provided with access to relevant training as those charged with governance are also personally responsible for ensuring they have the necessary skills and training.
- m) Responsibility for these activities must be clearly defined within the organisation.
- n) Officers involved in treasury management must be explicitly required to follow treasury management policies and procedures when making investment and borrowing decisions on behalf of the Council (this will form part of the Treasury Management Practices).
- o) "Investments" covers the financial and non-financial assets which the organisation holds primarily for financial returns. This will include investments which are not managed as part of the normal treasury management delegations.

1.2 This Strategy has been prepared in accordance with the Code.

1.3 The Council will adopt the following reporting arrangements in accordance with the requirements of the revised Code:

Area of Responsibility	Council/ Committee/ Officer	Frequency
Treasury Management Policy & Strategy / Annual Investment Strategy	Council approval with review delegated to Cabinet/ Audit and Standards Committee	Annually before the start of the year or where a material change is proposed
Annual Report on borrowing and investment activity	Council with review delegated to Cabinet/ Audit and Standards Committee	Annually by 30 September after the end of the year
Scrutiny of treasury management performance via mid-year report	Council approval with review delegated to Cabinet / Audit and Standards Committee	Mid-Year
In year changes to agreed Treasury Management Policy & Strategy / Annual Investment Strategy / Prudential and Treasury Indicators	Cabinet	By exception
Scrutiny of treasury management Policy, Strategy and procedures	Audit and Standards Committee	Annually before the start of the year
Treasury Management Monitoring Reports	Strategic Director, Resources and Digital	Bi-Monthly/Weekly
Treasury Management Practices	Strategic Director, Resources and Digital	Monthly

1.4 Given the link to the revenue budget and capital programme, the following indicators were approved by the Council on 25 February 2021 as part of the Budget and Council Tax Level 2021/22 report. For completeness, the approved indicators are attached at Appendix 3:

- Actual and estimates of financing costs to net revenue stream;
- Estimates of capital expenditure;
- Actual capital expenditure;
- Estimate of Capital Financing Requirement;
- Actual Capital Financing Requirement;
- Authorised limit;
- Operational boundary;
- Actual external debt;
- Gross debt and Capital Financing Requirement;
- Upper and lower limit of maturity structure of borrowing fixed and variable; and
- Upper limit on principal sums invested for periods of over 365 days.

- 1.5 In addition to the above indicators, local indicators showing the level of reserves which are backed by cash in the bank and internal borrowing as a percentage of the capital financing requirement are included in this report. Also, where there is a significant difference between the net and the gross borrowing position the risk and benefits associated with this strategy will be clearly stated in the annual strategy. This is highlighted within the main borrowing strategy outlined in Section 4.6 below.
- 1.6 The Strategy covers:
- Prospects for interest rates;
 - Treasury limits in force which will limit the treasury risk and activities of the Council, including prudential and treasury indicators;
 - The borrowing strategy;
 - Sensitivity forecast;
 - External and internal borrowing;
 - Debt rescheduling;
 - Policy on borrowing in advance of need;
 - The investment strategy; and
 - The policy on the use of external service providers.

2. Prospects for Interest Rates

- 2.1 The table shown below outlines the Council's view of anticipated movements in interest rates, based on guidance received from the Council's treasury management advisers Link Asset Services as at 8th February 2021.

	March 2021	June 2021	Sept 2021	Dec 2021	March 2022	March 2023	March 2024
Bank Rate	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%
5 yr PWLB	0.90%	0.90%	0.90%	0.90%	1.00%	1.10%	1.20%
10 yr PWLB	1.30%	1.30%	1.30%	1.30%	1.40%	1.50%	1.60%
25 yr PWLB	1.90%	1.90%	1.90%	1.90%	2.00%	2.10%	2.20%
50 yr PWLB	1.70%	1.70%	1.70%	1.70%	1.80%	1.90%	2.00%

Interest Rates

- 2.2 The coronavirus outbreak has caused huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its subsequent meetings to 4th February 2021. The Governor of the Bank of England has made it clear that more quantitative easing is favoured if further action becomes necessary. As shown in the forecast table above, no increase in Bank Rate is expected as economic recovery is expected to be only gradual and, therefore, prolonged.

Long Term Interest Rates

- 2.3 Investment returns are likely to remain exceptionally low during 2021/22 with little increase in the following two years.

3 Treasury Limits for 2021/22 to 2025/26 including Prudential Indicators

- 3.1 It is a statutory requirement of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 31(a), as amended by the Localism Act 2011, requires a local authority to calculate its budget requirement

for each financial year to include the revenue costs that flow from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from increases in interest charges and increases in running costs from new capital projects are limited to a level, which is affordable within the projected income of the Council for the foreseeable future. This is reported within the Council's Medium-Term Financial Strategy.

- 3.2 It is a statutory duty under Section 3 of Part 1 of the Local Government Act 2003, and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the Affordable Borrowing Limit. The Authorised Limit represents the legislative limit specified in the Act.
- 3.3 The Prudential Code for Capital Finance in Local Authorities is a professional code that sets out a framework for self-regulation of capital spending, in effect allowing councils to invest in capital projects without any limit as long as they are affordable, prudent and sustainable. The Code requires that treasury management decisions be taken in accordance with good professional practice and in full understanding of the risks involved and how these risks will be managed to levels that are acceptable to the Council. The Council will take into account its arrangements for the repayment of debt and consideration of any impact, on the authority's overall fiscal sustainability.
- 3.4 The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires the Council to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax and housing rent levels is affordable.
- 3.5 To facilitate the decision-making process and support capital investment decisions the Prudential Code and the Treasury Management Code require the Council to agree and monitor a minimum number of prudential indicators which were approved by Council on 25 February 2021 as attached at Appendix 4.
- 3.6 The Strategic Director, Resources and Digital, will ensure systems are in place to monitor the treasury limits and will report to Council instances where limits are breached, with the exception of short-term breaches of the Operational Boundary. The Operational Boundary is set so that if breached it acts as an early warning of the potential to exceed the higher Authorised Limit and as such temporary breaches due to debt restructuring and temporary borrowing are acceptable, providing they are not sustained.

4 Borrowing Strategy

- 4.1 The Local Government Act 2003 does not prescribe approved sources of finance, only that borrowing may not, without the consent of HM Treasury, be in other than Sterling.
- 4.2 The main options available for the borrowing strategy for 2020/21 are PWLB loans, market loans, capital market loans and the Municipal Bond Agency. The interest rate applicable to either PWLB or markets loans can be fixed or variable.
- 4.3 Variable rate short term borrowing is expected to be cheaper than long term fixed borrowing and therefore may be considered throughout the financial year. Due to the expectation that interest rates will rise, the risk of the potential increase in interest rates will be balanced against any potential short-term savings.

- 4.4 There are different types of market loans available, including forward starting, at variable and fixed interest rates. It is not usual practice to agree forward starting loans, but their use may be considered to avoid the 'cost of carry' – the difference between borrowing costs and investment returns. These loans generally would have to be offered at rates below the current or future PWLB forecast rates to make them an attractive option and considered as a means of mitigating future interest rate movements if the opportunity arose, i.e. where the Council can agree an interest rate ahead of when it would actually be required to draw down the funds.
- 4.5 To mitigate this interest rate risk a limit is placed on the total level of borrowing that can be taken as variable interest rate loans. To provide scope to utilise new market products should they become available as well as minimise the cost of borrowing and increase the diversification of the debt portfolio it is proposed that the limit on variable rate loans should be 40% of total borrowing in 2021/22.
- 4.6 The main strategy is therefore:
- Current (February 2021) long term PWLB rates (50 years) are around 2.00%. It is forecast that there will be little upward movement in PWLB rates over the next two financial years, being 1.70% Q1, 1.70% Q2, 1.70% Q3 and 1.80% Q4. Should interest rates fall below these targets borrowing should be considered, with preference given to terms which ensure a balanced profile of debt maturity, this may include Local Infrastructure Rate borrowing. The average interest rates forecast across this financial year for various borrowing periods are as follows: -
 - 10 years – 1.32%
 - 25 years – 1.92%
 - 50 years – 1.72%
 - Whilst monitoring borrowing interest rates if there appears to be an upward trend then it may be considered prudent to lock into rates which exceed those outlined in paragraph 4.6 above, to minimise interest rate risk.
 - The use of short-term borrowing (6 months to 18 months) will also be considered with the aim of minimising borrowing costs. This short-term borrowing will be replaced with longer term loans when rates are preferable.
 - External borrowing rates currently far exceed the return that is available for investments, meaning savings can be achieved by borrowing internally from reserves in the short term. The current policy of internal borrowing will continue to be followed as a short-term funding option serving to minimise overall cost.
 - Consideration will be given to borrowing market loans which are at least 20 basis points below the PWLB target rate.

Sensitivity of the forecast

- 4.7 The Council, in conjunction with Link Asset Services, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to any changes. The main sensitivities of the forecast are likely to be the two scenarios below:
- *if it was felt that there was a significant risk of a sharp FALL in borrowing rates, then borrowing will be postponed.*

- *if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast, perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.*

4.8 Against this background, caution will be adopted in the management of the 2021/22 treasury operations. The Strategic Director, Resources and Digital, will monitor the interest rate market and adopt a pragmatic approach to any changing circumstances having delegated powers to invest and manage the funds and monies of the Council.

External and Internal Borrowing

4.9 As at 30 November 2020 the Council had net debt of £595.921m; this includes total borrowing of £665.224m and investments of £69.303m.

4.10 Investment returns are likely to remain exceptionally low during 2021/22 with little change in the following two years but on a rising trend over the next few years.

4.11 Borrowing interest rates fell to historically very low levels as a result of the covid pandemic and the quantitative easing operations of the Bank of England. The policy of avoiding new borrowing by running down spare cash balances has served the Council well over recent years. The Council will assess its risk appetite in conjunction with budgetary pressures to reduce total interest costs. Although short-term interest rates are cheapest, longer-term borrowing could also be undertaken for the purpose of certainty.

4.12 There remains a cost of carry, (the difference between higher borrowing costs and lower investment returns) to any new long-term borrowing that causes a temporary increase in cash balances as this position will most likely incur a revenue cost.

Borrowing in advance of need

4.13 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be considered carefully to ensure that it is in line with the projected capital financing requirement and prudential indicators and that the Council can demonstrate value for money and ensure the security of the funds.

4.14 In determining whether borrowing will be undertaken in advance of need the Council will;

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need;
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered;
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow; and
- consider the alternative forms of funding.

Municipal Bond Agency

4.15 The Municipal Bond Agency UK are now established and began offering bonds to local authorities from March 2020. The initial bond issue offered a competitive rate compared to borrowing rates offered by the Public Works Loan Board (PWLB). The Council may consider this as an additional source of borrowing as and when appropriate.

5. Debt Rescheduling

5.1 Any rescheduling opportunities will be considered in line with procedures approved under the Council's Treasury Management Practice Statements and will include a full cost/benefit analysis of any proposed variations. Any positions taken via rescheduling will be in accordance with the strategy position outlined in Section 4 above and will also take into account the prudential and treasury limits.

5.2 The reasons for any proposed rescheduling will include:

- the generation of cash savings at minimum risk;
- help to fulfil the treasury strategy; and
- in order to amend the maturity profile and/or the balance of volatility in the Council's borrowing portfolio.

5.3 The Strategic Director, Resources and Digital, in line with delegated powers outlined in the approved Treasury Management Practice Statement, will approve all rescheduling.

5.4 The Council has examined the potential for undertaking early repayment of external PWLB or LOBO debt in order to reduce the difference between its gross and net debt positions. The significant difference between early redemption rates and interest rates payable on new debt means that large premiums are likely to be incurred by such action. This situation will be monitored in case the differential is narrowed by changes in current borrowing rates.

5.5 Consideration will also be given to the potential for making savings by running down investment balances by repaying debt prematurely as short-term rates on investments are likely to be lower than rates paid on currently held debt. However, this will need careful consideration in the light of premiums that may be incurred by such a course of action and other financial considerations.

5.6 All rescheduling will be reported to Council in the mid-year and annual reports.

6. Investment Strategy 2021/22 to 2025/26

Introduction

6.1 The Council has regard to the MHCLG's Guidance on Local Government Investments and CIPFA's Code of Practice. The Council must produce a strategy on an annual basis which covers the subsequent five years.

6.2 The CIPFA definition of "investments" covers all the financial assets of the organisation, as well as other non-financial assets which the organisation holds primarily for financial returns, such as investment property portfolios. This may therefore include investments which are not managed as part of normal treasury management or under treasury management delegations.

- 6.3 This annual strategy states which investments the Council may use for the prudent management of its treasury balances during the financial year under the categories of **specified investments** and **non-specified investments**.
- Specified investments are those with a high-level credit quality and subject to a maturity limit of one year.
 - Non-specified investments are those with less high credit quality, may be for periods in excess of one year and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.
- 6.4 Both specified and non-specified investment types currently utilised by the Council are detailed in Appendix 5, along with approved limits. These limits reflect the Council's investment requirements whilst assessing risk and obtaining advice from Link Asset Services.
- 6.5 In addition to these, numerous other investment options are available for use and these may be considered suitable for use in the future. Should this be the case then the option will be evaluated in line with the procedures contained within the approved Treasury Management Practice Statement.

Investment Objectives

- 6.6 All investments will be in Sterling.
- 6.7 The Council's primary investment objective is the security of the capital investment. The Council will also manage the investments to meet cash flow demands and to achieve a reasonable return commensurate with the proper levels of security and liquidity. The risk appetite of the Council is low in order to give priority to security of its investments.
- 6.8 The borrowing of monies purely to invest is unlawful and the Council will not engage in such activity.

Creditworthiness Policy

- 6.9 The Council applies the creditworthiness service provided by Link Asset Services. The service uses a sophisticated modelling approach with credit ratings from the three main rating agencies - Fitch, Moody's and Standard and Poor's. This service uses a scoring system to ensure that it does not give undue consideration to just one agency's ratings. It does not rely solely on the current credit ratings of counterparties but also uses the following information as overlays which are combined in a weighted scoring system:
- Credit watches and credit outlooks from credit rating agencies;
 - Credit Default Swap spreads, financial agreements that compensate the buyer in the event of a default, which give an early warning of likely changes in credit ratings; and
 - Sovereign ratings to select counterparties from only the most creditworthy countries.
- 6.10 The end product of this modelling system which indicate the relative creditworthiness of counterparties. The Council is satisfied that this service gives the required level of

security for its investments. It is also a service which the Council would not be able to replicate using in-house resources.

The minimum credit rating criteria the Council use will be a Short-Term rating (Fitch or equivalents) of F1 and a long-term rating of A. In circumstances where ratings from all three agencies are not available, two acceptable ratings will be deemed as sufficient.

Where three ratings are published and all three do not meet our minimum criteria the counterparty will not be used until such a time as all three ratings meet the minimum criteria or the lowest rating is withdrawn.

6.11 The credit ratings will be monitored as follows:

- All credit ratings are reviewed weekly. The Council has access to Fitch, Moody's and Standard and Poor's credit ratings and is alerted to changes through its use of the Link Asset Services creditworthiness service. Ongoing monitoring of ratings also takes place in response to ad-hoc e-mail alerts from Link Asset Services.
- If a counterparty's or deposit scheme's rating is downgraded with the result that it no longer meets the Council's minimum criteria, the further use of that counterparty/deposit scheme as a new deposit will be withdrawn immediately.
- If a counterparty is upgraded so that it fulfils the Council's criteria, its inclusion will be considered for approval by the Strategic Director, Resources and Digital.

6.12 Sole reliance will not be placed on the use of this external service. In addition, the Council will also use market data and information on government support for banks and the credit ratings of government support.

6.13 The Council has determined the minimum long term and short-term ratings it deems to be "high" for each category of investment. These "high" ratings allow investments of 365 days or less to be classified as **specified investments**. The Council's approved limits for this "high" credit rating for deposit takers is as follows:

High Rated	Fitch	Moody's	Standard & Poor's
Short Term (ability to repay short term debt)	F1	P1	A1
Long Term (ability to repay long term debt)	A	A2	A

6.14 In addition to the above specified investments, the Council has also fully considered the increased risk of **non-specified investments** and has set appropriate limits for non-high rated deposit takers. These are as follows:

Non- High Rated	Fitch	Moody's	Standard & Poor's
Short term	F1	P1	A1
Long term	A-	A3	A-

The selection of counterparties with an acceptable level of creditworthiness will be achieved by selecting institutions down to a minimum durational band within Link Asset Services weekly credit list of worldwide potential counterparties. The maximum maturity periods and amounts to be placed in different types of investment instruments are detailed in Appendix 5.

- 6.15 UK Government nationalised/part nationalised banks will have a maximum limit of 40% or £20m of total investment, all other counterparties will not exceed a maximum limit equal to 20% of total investments or £15m. Unless there are major changes in the level of investment balances throughout the year this limit will be reviewed prior to the commencement of each financial year.
- 6.16 Where more than one counterparty from a group is included on the counterparty list the group in total will be controlled by the above limits with the maximum limit being that of the parent company. Within the group each counterparty/subsidiary will have individual limits based on their creditworthiness although the total placed with the subsidiaries will not exceed the limit of the parent company. Subsidiaries that do not satisfy the minimum credit criteria will not be included.
- 6.17 A number of counterparties are also approved by the Strategic Director, Resources and Digital for direct dealing. These counterparties are included on the approved list and dealing will be within agreed limits. Direct dealing with individual counterparties must be approved by the Strategic Director, Resources and Digital prior to investments being placed.

UK Banks - Ring Fencing

- 6.18 The largest UK banks were required by UK law to separate core retail banking services from their investment and international banking activities by 1 January 2019. This is known as “ring-fencing”.
- 6.19 Ring-fencing is a regulatory initiative created in response to the global financial crisis which improves the resilience of banks by changing their structure. In general, simpler, lower risk activities will be offered by a ring-fenced Bank (RFB), whilst more complex and riskier activities will sit within a non-ring-fenced bank (NRFB).

Foreign Banks

- 6.20 The Council will continue to use UK banks irrespective of the UK sovereign rating, however non-UK banks domiciled in countries with a minimum sovereign rating of AA+ will be considered for inclusion on the approved list, they must also meet the high rated lending criteria and have operations based in the UK. Limits will be prescribed by the Link Asset Services creditworthiness list and limited to 365 days or less. Each country will be limited to the maximum investment limit of £15m or 20% of the Council’s total investments. A list of those countries with a minimum sovereign rating of AA+ is shown in Appendix 6.

Local Authorities

- 6.21 The Council invests with other Local Authorities on an ad hoc basis; each investment is considered on an individual basis and agreed by the Strategic Director, Resources and Digital, prior to funds being placed. Limits are detailed at Appendix 6.

Investment balances / Liquidity of investments

- 6.22 Creditworthiness of counterparties is considered prior to depositing funds. The maximum term for investments is 3 years. Longer term deposits will continue where the counterparty is deemed to be a low credit risk to ensure a good rate of return is maintained in the current market conditions. Deposits beyond 365 days will only be considered when there is minimal risk involved. With deposits of this nature there is an increased risk in terms of liquidity and interest rate fluctuations. To mitigate these risks a limit of £15m (20% of total investments whichever is the higher) has been set and a prudential indicator has been calculated (See Appendix 3). Such sums will only be placed with counterparties who have the highest available credit rating or other local authorities.
- 6.23 Deposits for periods longer than 365 days are classed as **non-specified investments** and this will increase the total limit of overall deposits in this classification to 25%.

Non-Treasury Investments

- 6.24 The acquisition of share capital or loan capital in any body corporate is defined as capital expenditure under the Local Government Act 2003. Such investments will have to be funded out of capital or revenue resources and will be classified as '**non-specified investments**'.
- 6.25 A loan or grant by the Council to another body for capital expenditure by that body is also deemed by regulation to be capital expenditure by the Council. It is therefore important for the Council to clearly identify if the loan was capital expenditure or if it is an investment made primarily to generate a financial yield. The latter will be assessed using the Council's Investment Framework.
- 6.26 The Council will ensure that all the organisation's investments are covered in either the Capital Strategy or Investment Strategy, and will set out, where relevant, the organisation's risk appetite and specific policies and arrangements for non-treasury investments. It will be recognised that the risk appetite for these activities may differ from that for treasury management.
- 6.27 To date the Council have not entered into any non-treasury investments which are purely to generate a commercial return, neither are there any plans to consider entering into non-treasury investments solely or primarily to obtain a revenue return. However, if an opportunity to do so arose the long-term financial impact and the risks inherent to the scheme would be assessed as part of the due diligence process. Where the size of the investment or the risk of the investment required external advice, this will be obtained. Any potential investment entered for a commercial return will require prior Cabinet approval.
- 6.28 The Council does not invest for solely commercial reasons or to generate income to support the revenue budget. Any capital investment entered into to deliver service

objectives and/or the placemaking role of the local authority is monitored and reported in line with the Capital Strategy. Capital investments are assessed in terms of their contribution to deliver the following objectives:

- Health and Housing
- Economy
- Poverty and Equality
- Climate Change
- Transport

Further information can be obtained from the Council's Capital Strategy at the following link: [Capital Strategy 2021/22 to 2025/26](#)

- 6.29 The Council maintains a schedule setting out a summary of existing material investments, subsidiaries, joint ventures and liabilities including financial guarantees and the organisation's risk exposure, which is attached at Appendix 7.

Internal Investment Strategy

- 6.30 The Strategic Director, Resources and Digital will monitor the interest rate market and react appropriately to any changing circumstances.
- 6.31 The Council takes the view that bank rate is forecast to remain the same over the next few years. Bank rate forecasts for financial year ends are 2020/21 0.10%, 2021/22 0.10% and 2022/23 0.10%.
- 6.32 The overall balance of risks to economic growth in the UK are probably weighted to the upside. This will be from stronger than currently expected economic recoveries in UK and/or other major developed economies and if The Bank of England is too slow in its pace and strength of increases in Bank Rate, therefore allowing inflationary pressures to build up too strongly within the UK economy, necessitating a later rapid series of increases in Bank Rate faster than we currently expect.
- 6.33 The balance of risks to increases or decreases in Bank Rate and shorter term PWLB rates are also weighted to the upside.

Investment Risk Benchmark

- 6.34 The Council will use an investment benchmark to assess the investment performance of its investment portfolio against the 3-month London Interbank Bid Rate (LIBID) annualised. The Council is also a member of the Link Asset Services investment benchmarking Group who meet semi-annually. As a member, quarterly reports on comparative performance with other members of the group and the wider Link Asset Services client base are received. The benchmarking return for the group is a reasonable target for the Council, which allows the relative risk appetite to be considered as part of the benchmark.

End of year investment report

- 6.35 By the end of September each year Council will receive a report from Cabinet on its investment activity as part of its annual treasury report.

Policy on use of external service providers

- 6.36 The Council currently uses Link Asset Services as its external treasury management advisers.
- 6.37 It is recognised that responsibility for treasury management decisions remains with the Council at all times and will ensure that undue reliance is not placed upon our external service providers.
- 6.38 It is also recognised that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

Scheme of Delegation

- 6.39 As required by the Guidance Notes for Local Authorities the Treasury Management Scheme of Delegation is detailed in Appendix 2, paragraph 1.3.

Role of the Section 151 Officer

- 6.40 As required by the Guidance Notes for Local Authorities the role of the Section 151 Officer in relation to treasury management is detailed below:
- Recommending the Code of Practice to be applied, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
 - Submitting regular treasury management policy reports;
 - Submitting budgets and budget variations;
 - Receiving and reviewing management information reports;
 - Reviewing the performance of the treasury management function;
 - Ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
 - Ensuring the adequacy of internal audit, and liaising with external audit; and
 - Arranging for the appointment of external service providers;
 - Preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management;
 - Ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority;
 - Ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing;
 - Ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources;
 - Ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long-term liabilities;
 - Provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees;

- Ensuring that members are adequately informed and understand the risk exposures taken on by an authority; and
- Ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above.

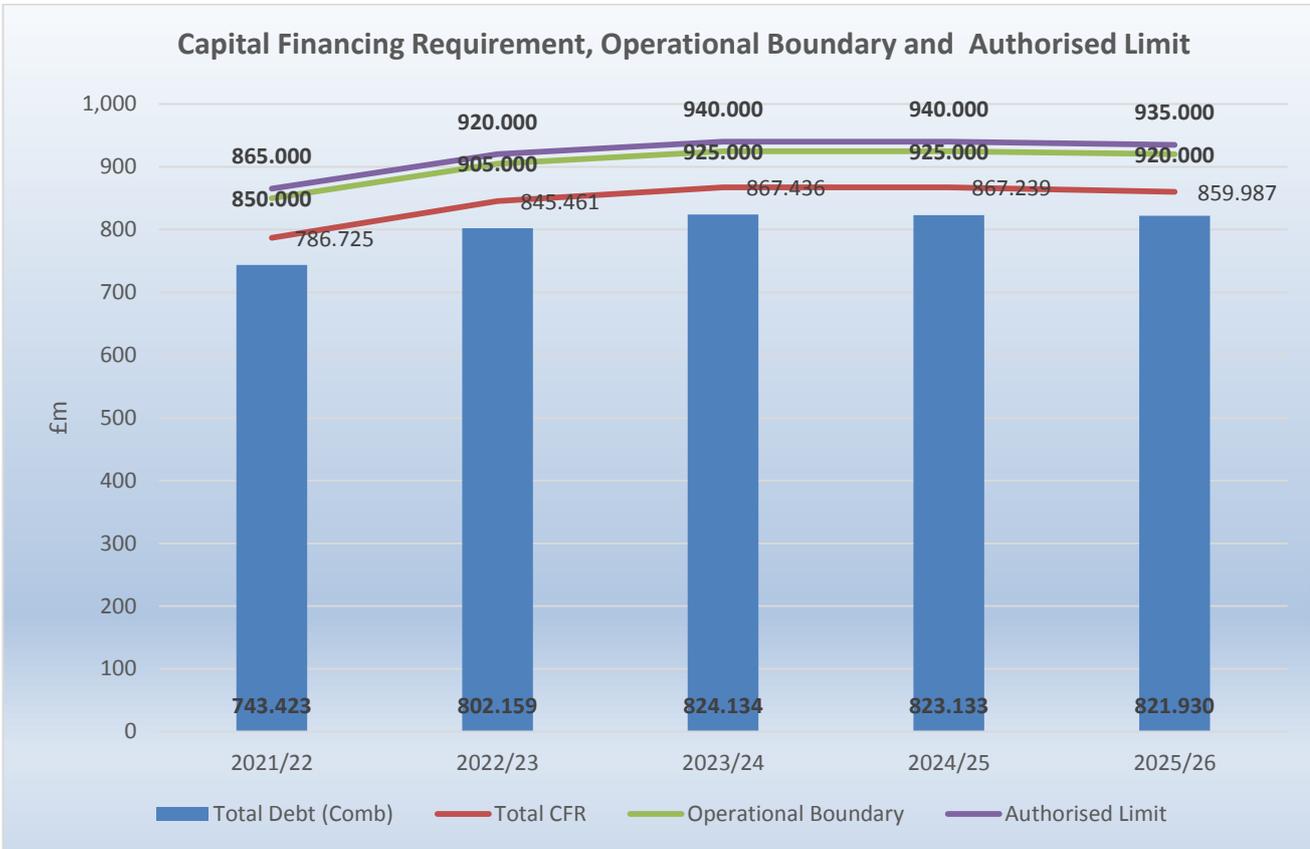
Prudential Indicators – Treasury Management

Authorised Limit for External Debt					
	2021/22 £000	2022/23 £000	2023/24 £000	2024/25 £000	2025/26 £000
Borrowing	865,000	920,000	940,000	940,000	935,000

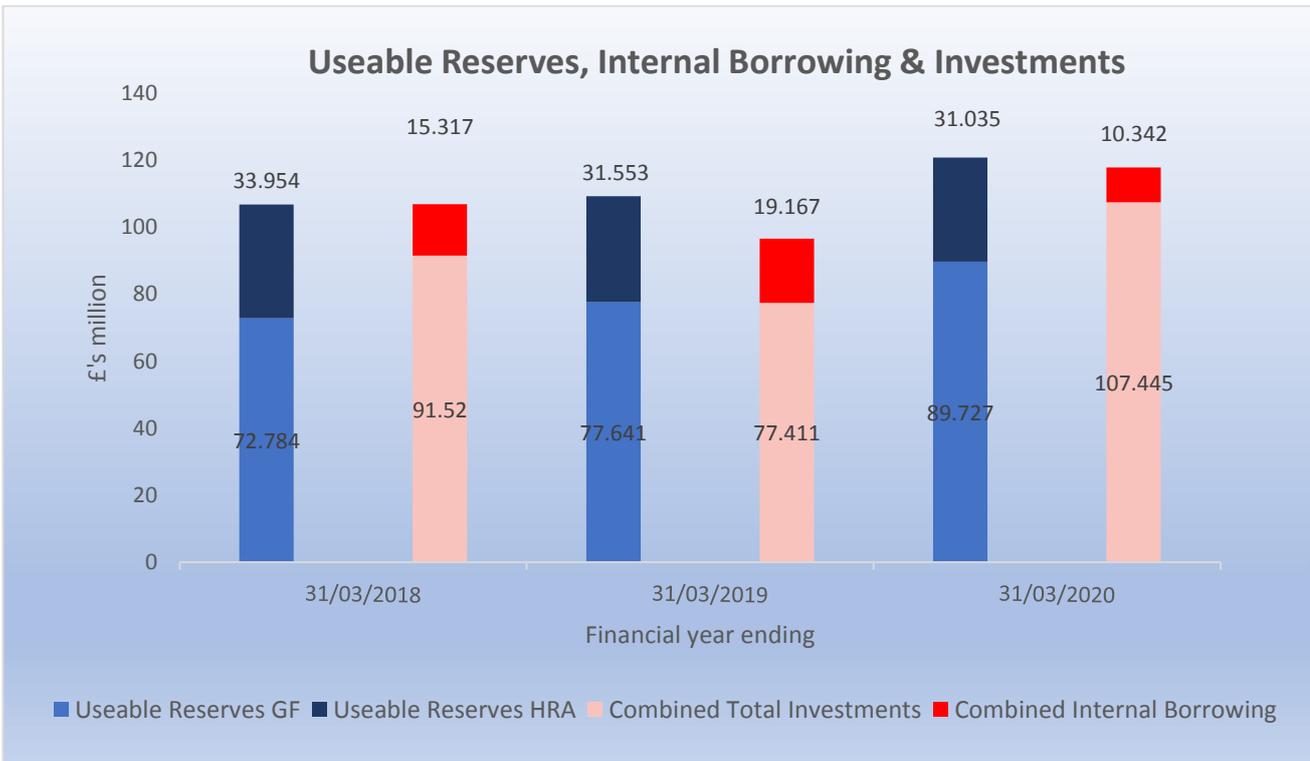
The Authorised Limit for External Debt sets the maximum level of external borrowing that the Council can incur. It reflects the level of borrowing which, while not desired, could be afforded in the short-term, but is not sustainable. It is the Council's expected maximum borrowing need with headroom for unexpected cashflow. The limit also provides scope for the Council to borrow in advance of need.

Operational Boundary for External Debt					
	2021/22 £000	2022/23 £000	2023/24 £000	2024/25 £000	2025/26 £000
Borrowing	850,000	905,000	925,000	925,000	920,000

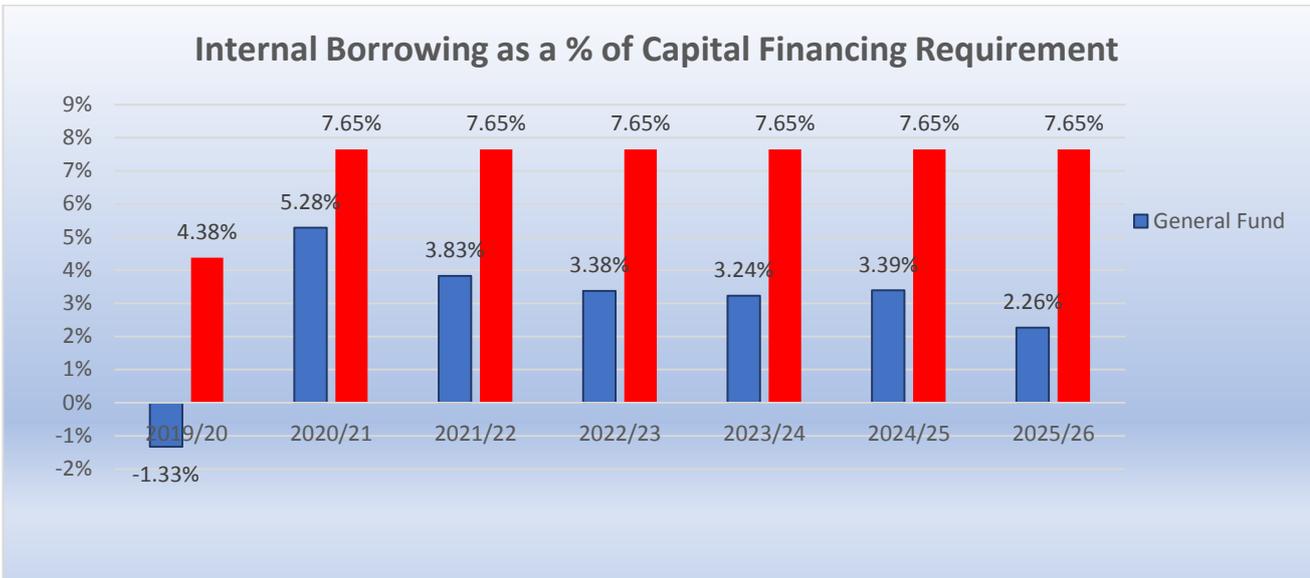
The Operational Boundary for External Debt is based on the probable external debt during the course of the year. It is not a limit and actual borrowing could vary around this boundary for short times during the year. It acts as an early warning indicator to ensure the authorised limit is not breached. Similar, to the authorised limit it also provides scope for the Council to borrow in advance of need.



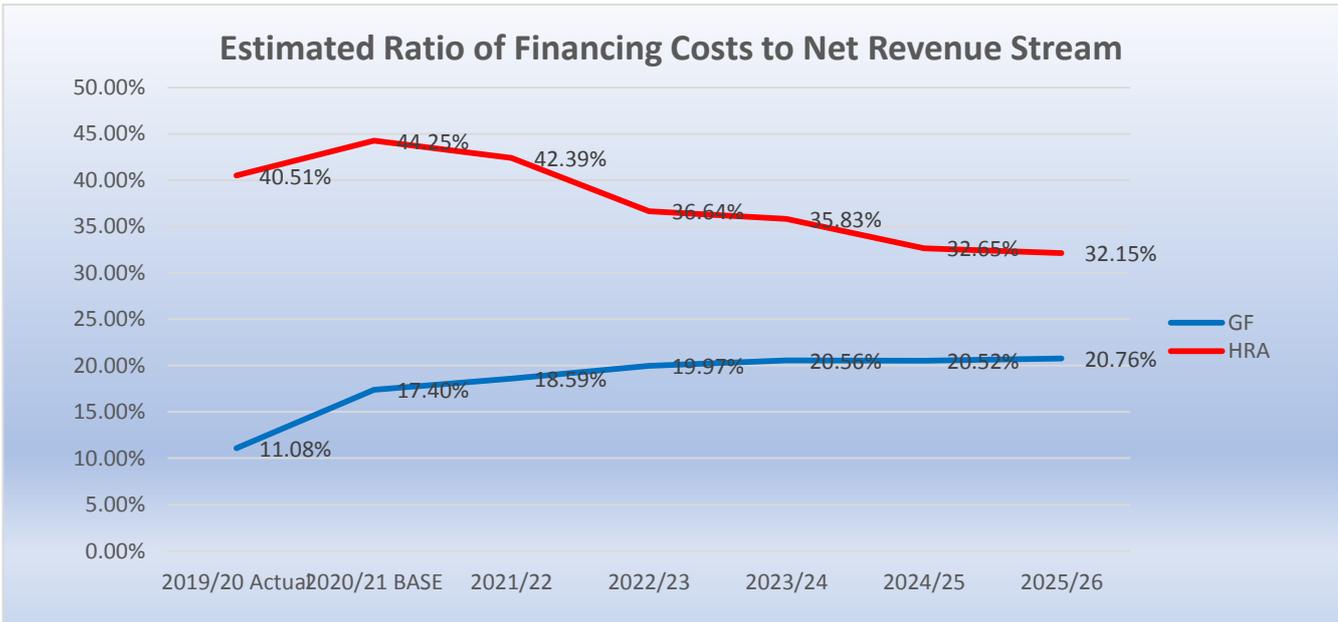
Capital Financing Requirement (CFR) shows the Council’s capital borrowing requirement. Any gap between the CFR and the total debt highlights the potential to borrow further if the cashflow and treasury management position dictate.



The internal borrowing position represents the level to which reserves, and balances have temporarily been used to support borrowing positions and therefore the reserves will not be backed by cash in the bank.



Internal borrowing as a percentage of the Council’s underlying borrowing requirement reflects the Council’s exposure to interest rate movements and the element of borrowing that is being undertaken at variable rates (i.e. rates equivalent to the lost interest on investment income).



Ratio of financing costs to net revenue stream – financing costs must be met before any services have been delivered. Higher financing costs leaves less available to provide services.

Treasury Indicators

Upper and Lower Limits for the Maturity Structure of Fixed Rate Borrowings		
	Upper Limit	Lower Limit
Under 12 months	20%	0%
12 months and within 24 months	19%	0%
24 months and within 5 years	21%	0%
5 years and within 10 years	27%	0%
10 years and within 20 years	22%	0%
20 years and within 30 years	18%	0%
30 years and within 40 years	44%	0%
40 years and within 50 years	46%	0%
50 years and above	16%	0%

Upper and Lower Limits for the Maturity Structure of Variable Rate Borrowings		
	Upper Limit	Lower Limit
Under 12 months	20%	0%
12 months and within 24 months	20%	0%
24 months and within 5 years	20%	0%
5 years and within 10 years	20%	0%
10 years and within 20 years	20%	0%
20 years and within 30 years	20%	0%
30 years and within 40 years	20%	0%
40 years and within 50 years	20%	0%
50 years and above	20%	0%

Upper Limit on Amounts Invested Beyond 365 Days					
	2021/22 £000	2022/23 £000	2023/24 £000	2024/25 £000	2025/26 £000
Investments	15,000	15,000	15,000	15,000	15,000

Specified Investments (All Sterling Denominated)

Investment type	Share/ Loan Capital	Repayable/ Redeemable within 12 months	Security / Minimum Credit Rating	Capital Expenditure	Circumstance of use	Maximum period
Term deposits with the UK Government or with UK local authorities (i.e. local authorities as defined under Section 23 of the 2003 Act) with maturities up to 365 days.	No	Yes	High security although LA's not credit rated. <i>See appendix 2 Creditworthiness Policy</i>	No	In-house	365 days
Term deposits with credit-rated deposit takers (banks and building societies), including callable deposits with maturities up to 365 days.	No	Yes	Secure Varied minimum credit rating <i>See appendix 2 Creditworthiness Policy</i>	No	In-house	365 days

<p>Short Term Money Market Funds The majority of these funds are instant access and therefore do not have a maturity date.</p>	No	Yes	Secure Varied minimum credit rating <i>See appendix 2 Creditworthiness Policy</i>	No	In-house	The investment period is subject to liquidity and cash flow requirements. It is assumed that funds are placed overnight and will be returned and reinvested the next working day (although no actual movement of cash may take place).
<p>Standard Money Market Funds and Ultra Short Duration Funds 3-day notice cash plus fund These funds require three-day notice for withdrawals and therefore do not have a maturity date.</p>	No	Yes	Secure Varied minimum credit rating <i>See appendix 2 Creditworthiness Policy</i>	No	In-house	The investment period is subject to liquidity and cash flow requirements. Notice required is three days, however it is the intention to leave these funds for terms longer than other money market funds to achieve greater returns.

Non-Specified Investments (All Sterling Denominated)

Investment type	(A) Why use it (B) Associated risks	Share/ Loan Capital	Repayable/ Redeemable within 12 months	Security / Minimum credit rating	Capital Expenditure	Circumstance of use	Max % of overall investments	Maximum maturity of investment
Rated deposit takers (banks and building societies) which do not meet the Council's "high" credit rating	(A) To improve ability to place smaller amounts (B) Greater risk than "high" credit rating counterparties but advance warning by rating agency of potential problems. The Council has fully considered this investment category and set appropriate investment and maturity limits in order to minimise risk.	No	Yes	Secure Varied minimum Credit rating <i>Minimum: Long term A- Short term F1</i>	No	In-house	Total not high rated deposits as a proportion of total investments 25%	6 months (but set on an individual counterparty basis)
Term deposits with UK Government, UK Local Authorities or credit rated banks and building societies, with maturities over 1 year	A) To improve the ability to "lock in" at times of high interest rates to secure a higher return over a longer period should rates be forecast to fall. B) Lower liquidity and greater risk of adverse interest rate fluctuations. The Council has fully considered this investment category and set appropriate investment and maturity limits in order to minimise risk.	No	No	Secure Varied minimum credit rating	No	In-house	Total investment per Counterparty 20%	3 years

<p>Certificate of Deposits issued by banks and building Societies</p>	<p>A) Provides additional counterparties, as many banks do not want to take fixed term cash deposits. B) Credit risk could change but if adverse there is an option to sell onto a secondary market. The Council has fully considered this investment category and set appropriate investment and maturity limits in order to minimise risk.</p>	<p>No</p>	<p>Yes</p>	<p>Secure Varied minimum Credit rating <i>Minimum:</i> <i>Fitch</i> <i>Long term</i> A- <i>Short term</i> F1</p>	<p>No</p>	<p>In-House</p>	<p>20%</p>	<p>12 months (but set on an individual counterparty basis)</p>
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Appendix 5

Maximum Maturity Periods and Amounts

Organisation	Criteria	Max Amount*	Max Period
High Rated (Specified Investments – High rated and up to 365 days see Appendix 4)	Minimum Fitch rating of F1 short term and A long term. Moody's minimum rating of P1 short term backed by A2 long term and S&P minimum rating of A1 short term and A long term.	£20m (Gov't Backed, otherwise £15m)	3 years
Foreign Banks	Must meet the minimum high rated criteria above and have a minimum sovereign rating of AA+	£15m country limit	365 Days
Non-High Rated	Minimum Fitch rating of F1 short term and A- long term. Moody's minimum rating of P1 short term backed by A3 long term and S&P minimum rating of A1 short term and A- long term.	£10m	6 months
UK Local Authorities	(i.e. local authorities as defined under Section 23 of the 2003 Act) Each investment is considered on an individual basis	£10m	3 years
Short-Term Money Market Funds (Same day settlement)	AAA mmf fund rating or equivalent with assets >£1bn	£10m	Overnight
Standard Money Market Funds and Ultra-Short Duration Funds (Trade plus 3-day settlement)	AAAf fund rating or equivalent, backed up with lowest volatility rating (S1) or equivalent with assets > £0.75bn	£10m (excludes any compound interest)	3 days

* Restricted to a maximum of either 40% if government backed or 20% of total investments if non-government backed counterparty.

Foreign Banks

This list is based on those countries which have non-UK sovereign ratings of AA+ or higher at 20/01/2021.

AAA

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

AA+

- Canada
- Finland
- U.S.A.

Non-Treasury Management Investments

Investment	Latest Balance	Notes
Long term loans to Keelman Homes	£ 14,527,453.07	Loan Balance at 16/02/2021
SCAPE System Build Ltd	£ 784,000.00	17% Shareholding in SCAPE
Newcastle International Airport	£ 7,811,428.00	13.33% shareholding in Newcastle Airport
Hospital of King James	£ 65,929.18	Loan Balance at 16/02/2021
Loan to Citizens Advice Bureau	£ 512,141.70	Loan Balance at 16/02/2021
Loans to Trading Company	£ 2,637,863.04	Loan Balance at 16/02/2021
Newcastle International Airport Long Term credit notes	£ 9,424,660.89	Loan notes - interest paid bi annuall - principal repayment due 2032
Soft Loans	£ 286,614.08	North Misic Trust - Soft Loan
Loan to NE Credit Union	£ 100,993.22	Loan Balance at 16/02/2021
Loan to NGI	£ 230,355.11	Loan Balance at 16/02/2021