# The Treasury Management Strategy Statement (TMSS) 2020/21

Report of the Cabinet Member for Finance and Procurement

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| Date: | 5 February 2020 |
| Agenda Item: | |
| Contact Officers: | Anthony Thomas |
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| **Key Decision?** | **YES** |
| **Local Ward Members** | Full Council |

Lichfield district council
www.lichfielddc.gov.uk

**AUDIT AND MEMBER STANDARDS COMMITTEE**

## 1. Executive Summary

**Introduction**

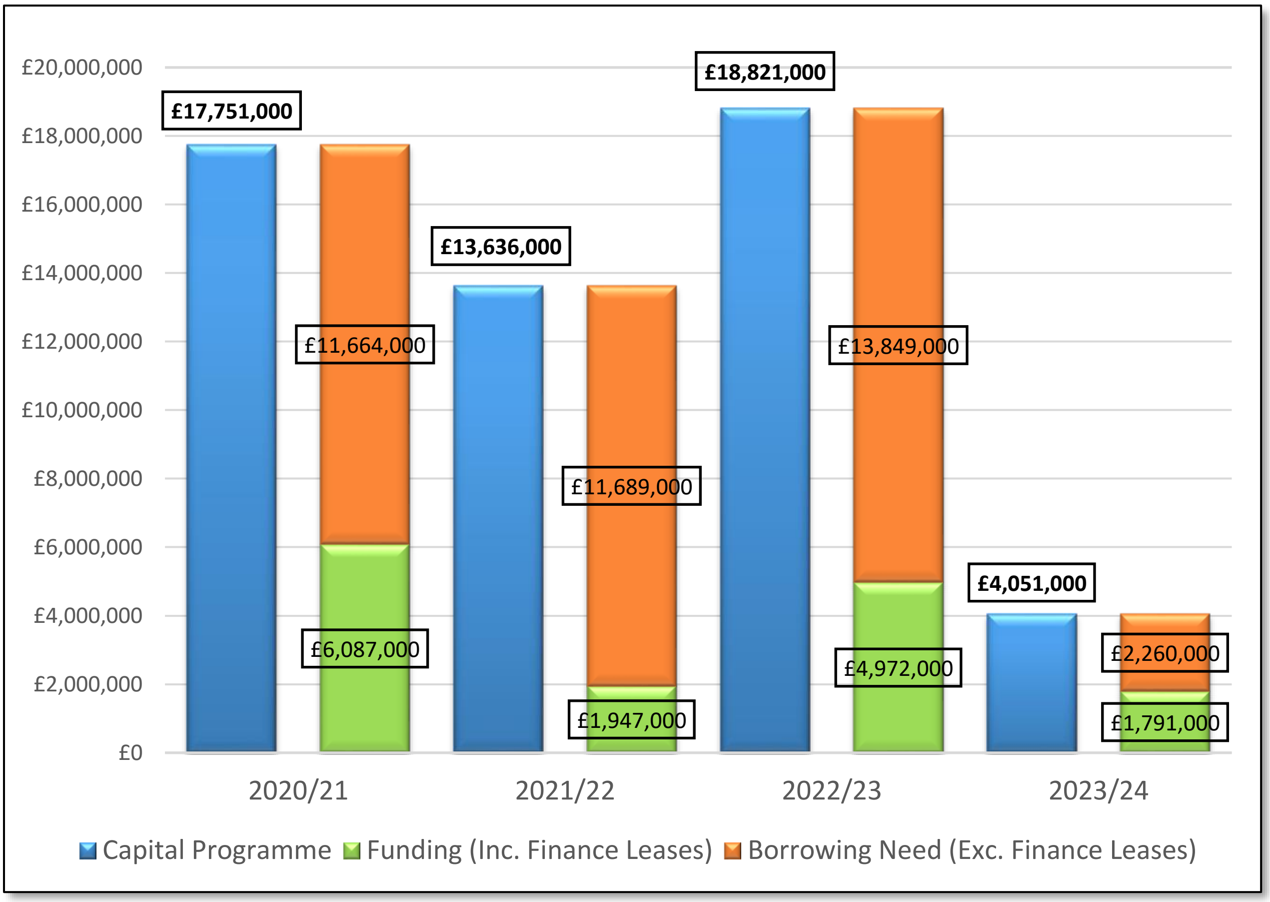
1.1 The Council has adopted the Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management in the Public Services: Code of Practice 2018 Edition (the CIPFA) Code which requires the Authority to approve a treasury management strategy before the start of each financial year.

1.2 This report fulfils the Authority's legal obligation, under the Local Government Act 2003, to have regard to both the CIPFA Code and the Ministry of Housing, Communities and Local Government MHCLG Guidance.

**The Capital Strategy and Capital Programme**

1.3 The Capital Programme shows longer term investment for our **Strategic Plan**.

1.4 The Capital Strategy required by the Prudential Code is outlined at **APPENDIX A** and the Capital Programme is outlined in **APPENDIX B** and below:



**Treasury Management**

1.5 The Treasury Management Strategy Statement incorporates the Annual Investment Strategy and it covers the financing and investment strategy for the forthcoming financial year.

1.6 The purpose of this paper is, therefore, to review:

- The Capital Strategy and Capital Programme, outlined in **APPENDICES A** & **B.**
- Minimum Revenue Provision Statement for 2020/21 **(APPENDIX C).**
- Treasury Management Strategy Statement for 2020/21 **(APPENDIX D).**
- Treasury Investments and their Limits **(APPENDIX D)**.
- The Investment Strategy Report for 2020/21 **(APPENDIX E)** as required under Statutory Guidance in January 2018.
- The Capital and Treasury Prudential Indicators 2019-24 in the financial implications section.

1.7 All treasury activity will comply with relevant statute, guidance and accounting standards.

# 2. Recommendations

That Members consider the Treasury Management Strategy Statement and highlight any changes or recommendations to Cabinet in relation to:

2.1 The Capital Strategy and Capital Programme, outlined in **APPENDICES A** & **B**.

2.2 The Minimum Revenue Provision Statement for 2020/21, at **APPENDIX C**, which sets out the Council's policy of using the asset life method for making prudent provision for debt redemption.

2.3 Treasury Management Strategy Statement for 2020/21 including proposed limits **(APPENDIX D)**.

2.4 The Investment Strategy Report **(APPENDIX E)** including the proposed limits for 2020/21.

2.5 The Capital and Treasury Prudential Indicators for 2019-24 in the financial implications section.

2.6 The Authorised Limit Prudential Indicator shown within the financial implications section.

2.7 The plan to undertake further Strategic Fund investments up to **£4m** although this will be subject approval by Council of recommendations 2.3 to 2.5.

# 3. Background

## The Capital Strategy

3.1 The Capital Strategy at **APPENDIX A** sets out the Council's framework for managing the Capital Programme including:

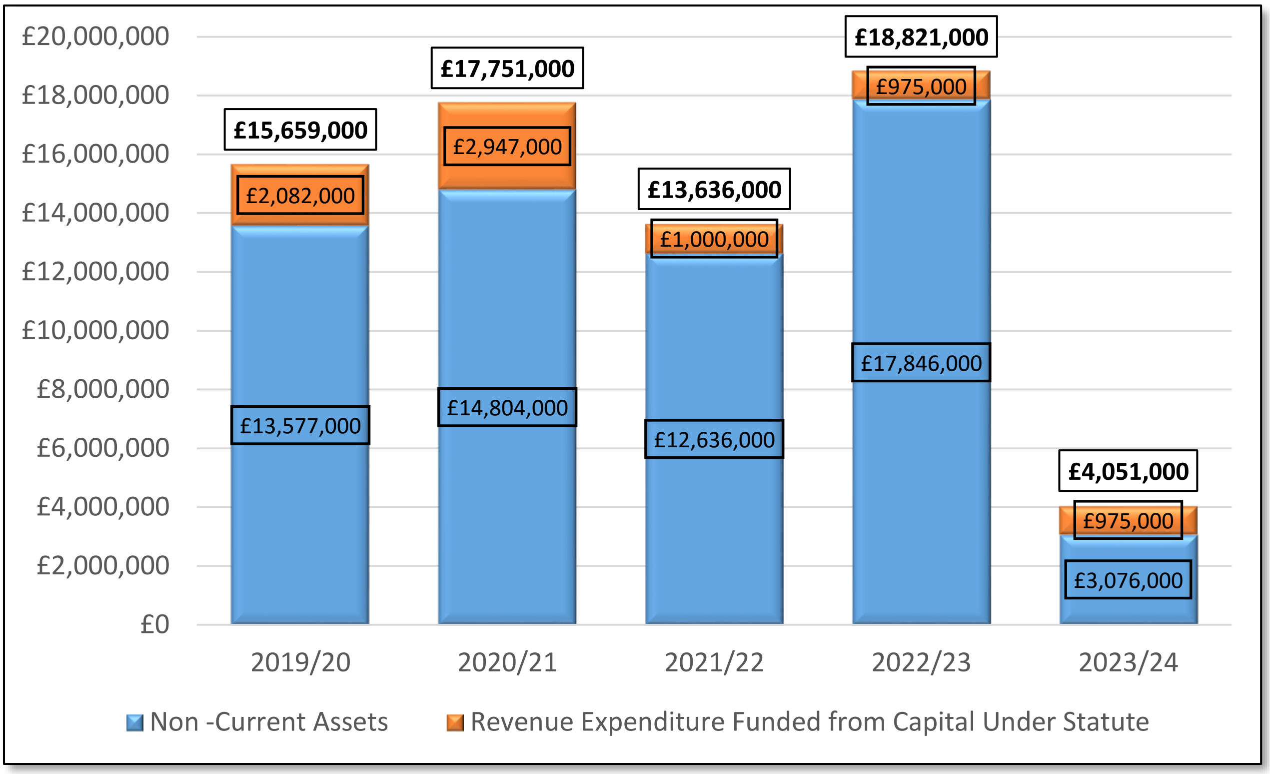
- **Capital expenditure**, including the approval process, long-term financing strategy, asset management, maintenance requirements, planned disposals and funding restrictions.
- **Debt and borrowing and treasury management**, including projections for the level of borrowing, capital financing requirement (Borrowing Need) and liability benchmark, provision for the repayment of debt, the authorised limit and operational boundary for the coming year and the authority's approach to treasury management.
- **Commercial activities**, including due diligence processes, the authority's risk appetite, proportionality in respect of overall resources, requirements for independent and expert advice and scrutiny arrangements.
- **Other long-term liabilities**, such as financial guarantees.
- **Knowledge and skills**, including a summary of that available to the authority and its link to the authority's risk appetite.

3.2 The key risks associated with the Capital Strategy are principally related to the investment in Property and its funding given this is planned to be funded through borrowing.

3.3 The Council's Chief Financial Officer has assessed the current risk as **material (yellow)**.

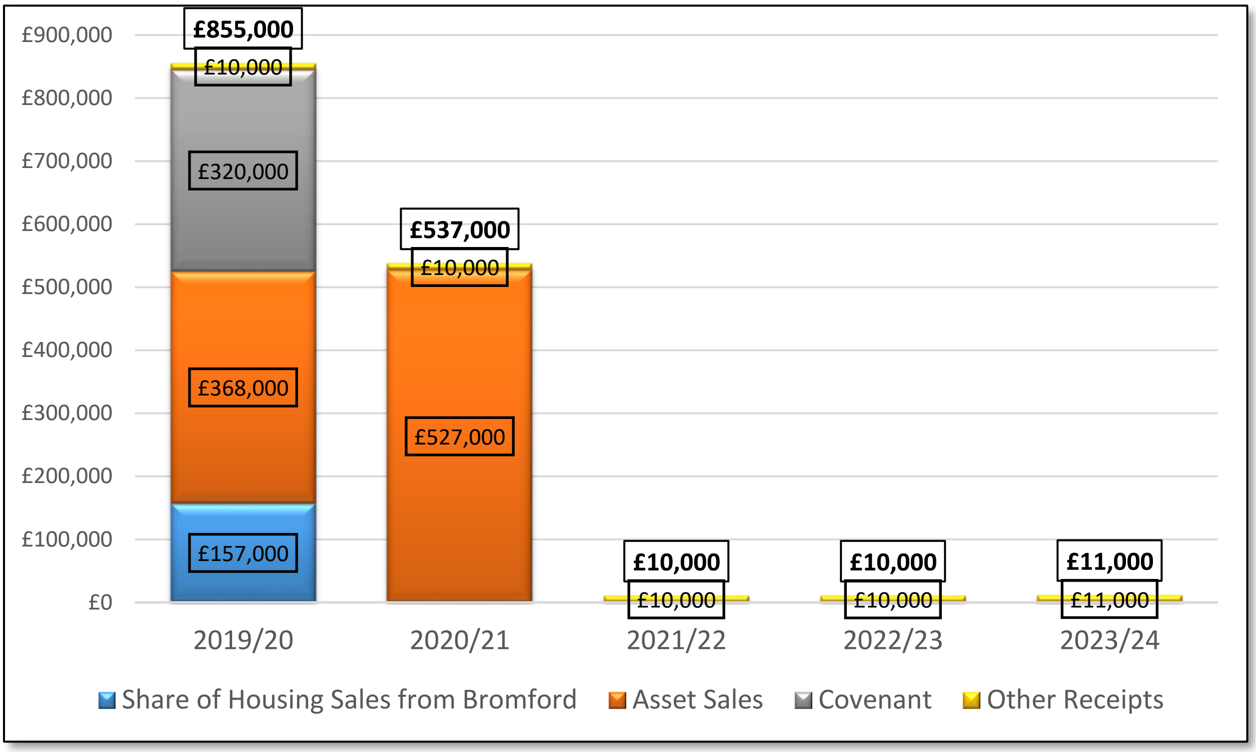
## The Capital Programme

3.4 The Capital Programme (Revenue Expenditure Funded from Capital Under Statute relates to projects such as Disabled Facilities Grants) is shown in detail at **APPENDIX B** and below:



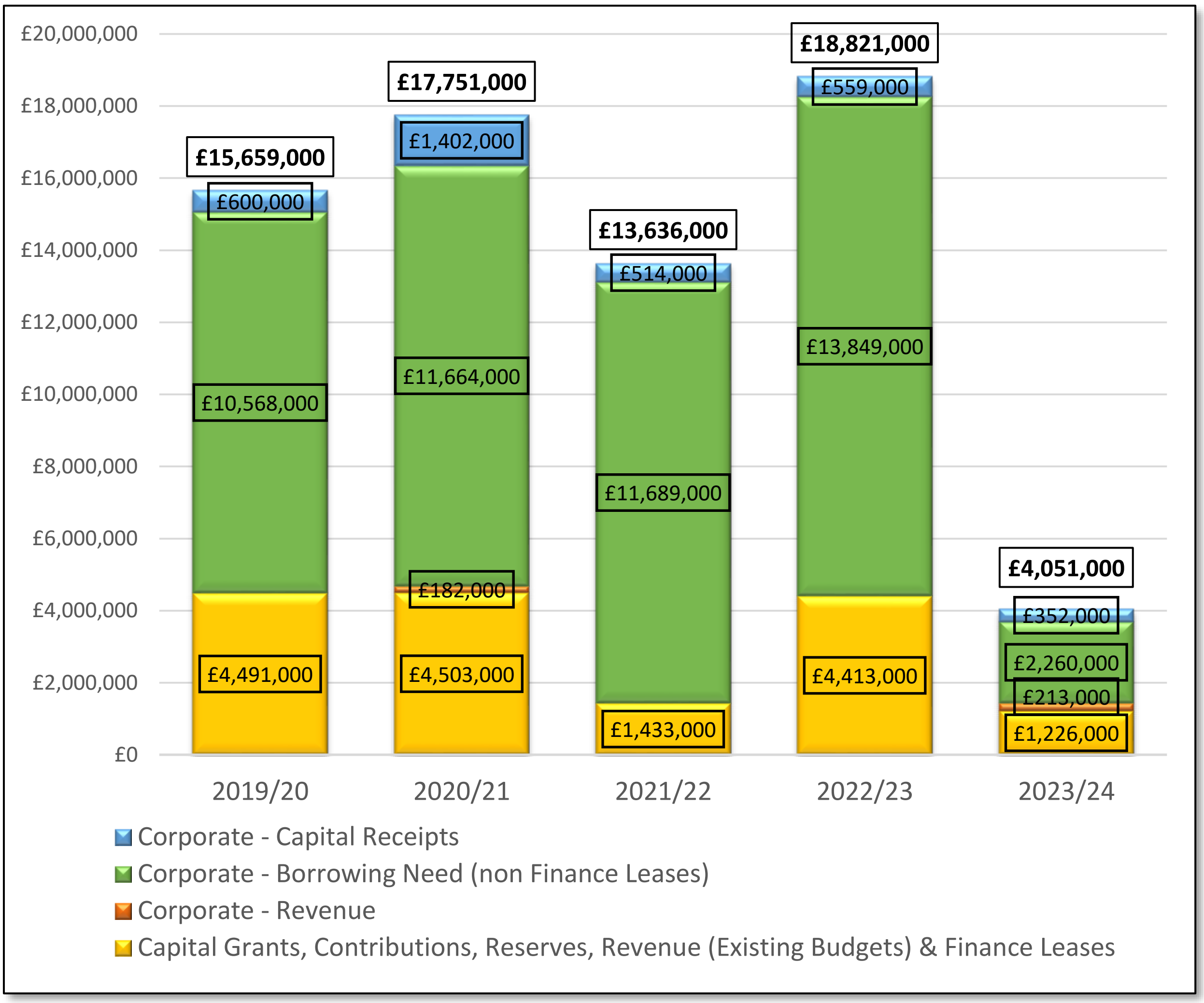

Capital Receipts

3.5 The projected Capital Receipts included in the Medium Term Financial Strategy are shown below:



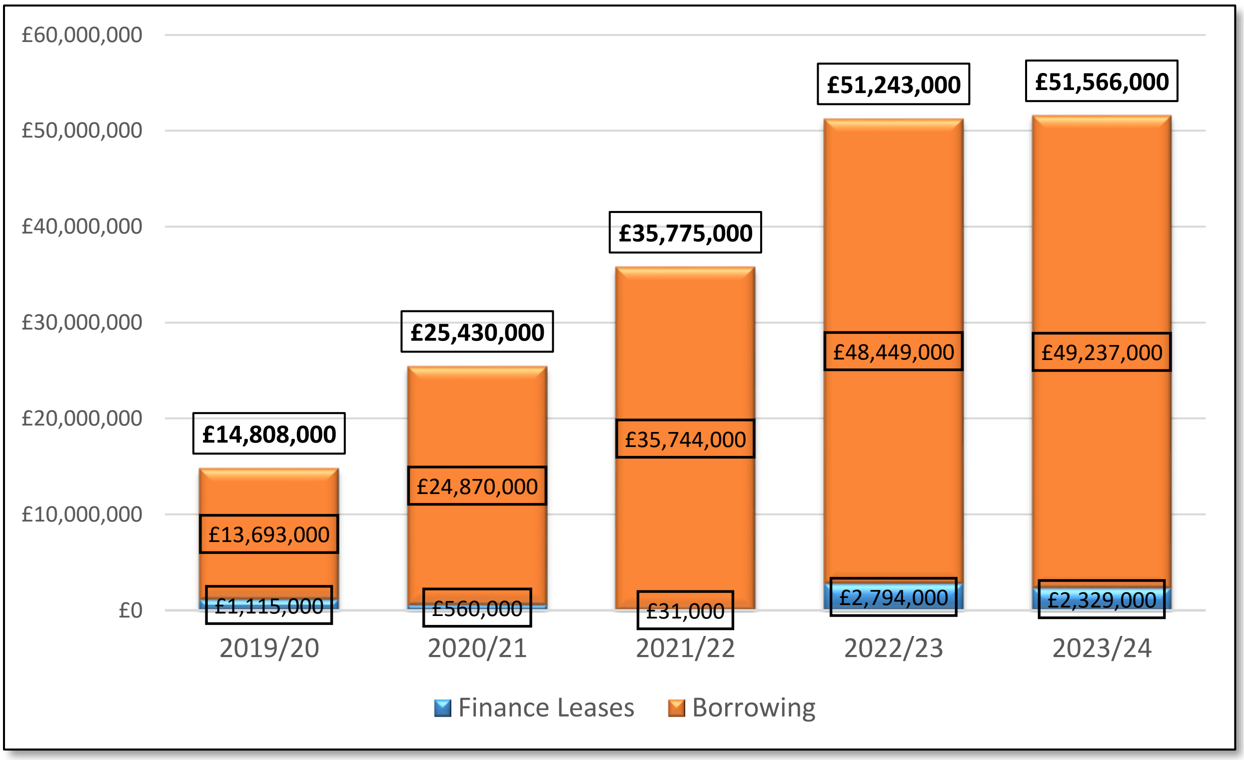
The Funding of the Capital Programme

3.6 The funding of the Capital Programme including the element funded by the corporate sources of capital receipts, borrowing and revenue is shown at **APPENDIX B** and below:

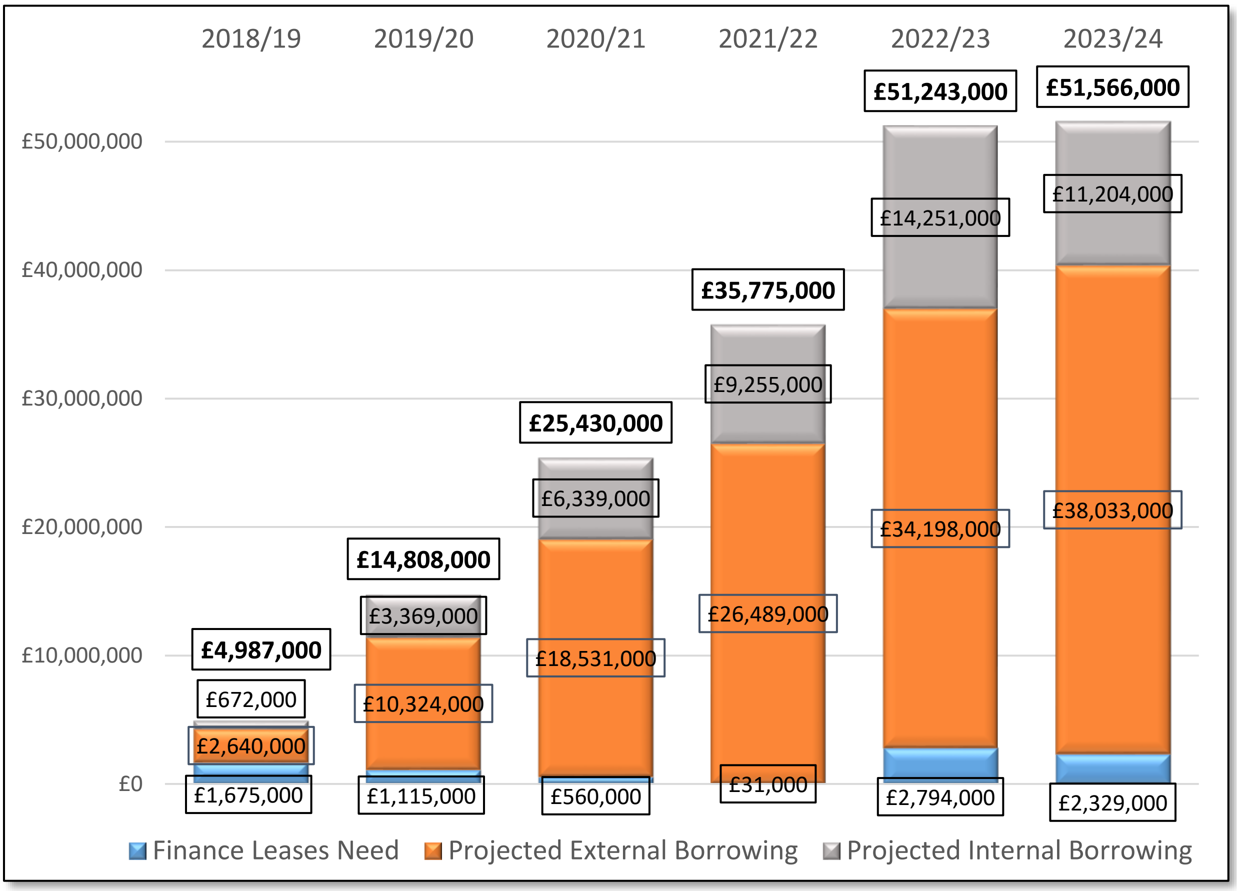



The Capital Financing Requirement (Borrowing Need) and its Financing

3.7 The projected Cumulative Borrowing Need related to the Capital Programme is shown below:

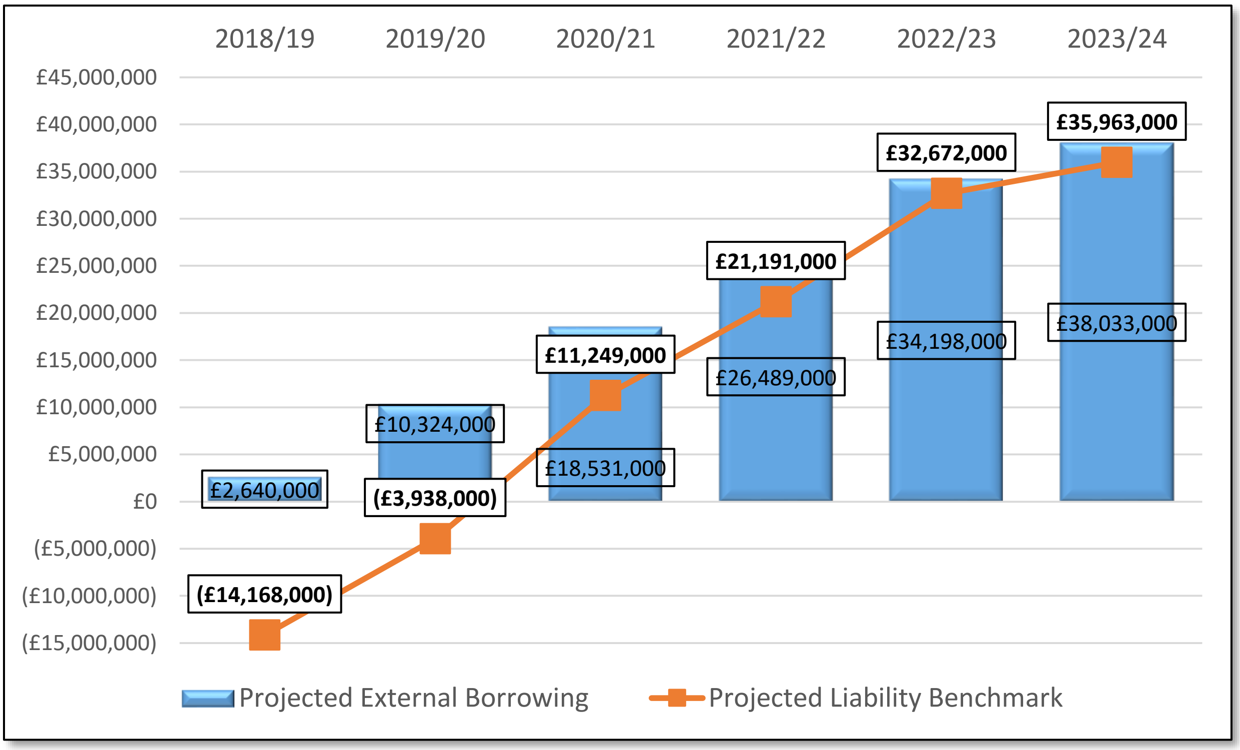


3.8 The projected financing of this Cumulative Borrowing Need is shown at **APPENDIX A** and below:




3.9 The **liability benchmark** is the lowest risk level of <u>external borrowing</u> by keeping cash and investment balances to a minimum level of **£10m,** at each year end, to maintain liquidity but minimise credit risk.

3.10 The projected level of external borrowing together with the projected liability benchmark in the Medium Term Financial Strategy is shown at **APPENDIX A** and below:




3.11 The chart above indicates that, based on current Balance Sheet projections and funding **£11m** of Investment in Property though Internal Borrowing, the Council's projected External Borrowing from 2022/23 will be closer to the liability benchmark.

Current Revenue Implications of the Capital Programme

3.12 The Revenue Implications compared to the Approved Budget are shown at **APPENDIX A** and below:


**Treasury Management**

3.13 CIPFA has defined Treasury Management as :

*"the management of the organisation's 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."*

3.14 The Council is responsible for its treasury decisions and activity. No treasury management activity is without risk. The successful identification, monitoring and control of risk are an important and integral element of its treasury management activities. The main risks to the Council's treasury activities are:

- Liquidity Risk (Inadequate cash resources)
- Market or Interest Rate Risk (Fluctuations in interest rate levels)
- Inflation Risk (Exposure to inflation)
- Credit and Counterparty Risk (Security of Investments)
- Refinancing Risk (Impact of debt maturing in future years)
- Legal and Regulatory Risk

3.15 The Strategy also takes into account the impact of the Council's Revenue Budget and Capital Programme on the Balance Sheet position, the current and projected Treasury position, the Prudential Indicators and the outlook for interest rates.

3.16 **International Financial Reporting Standard 16 (Leases)**

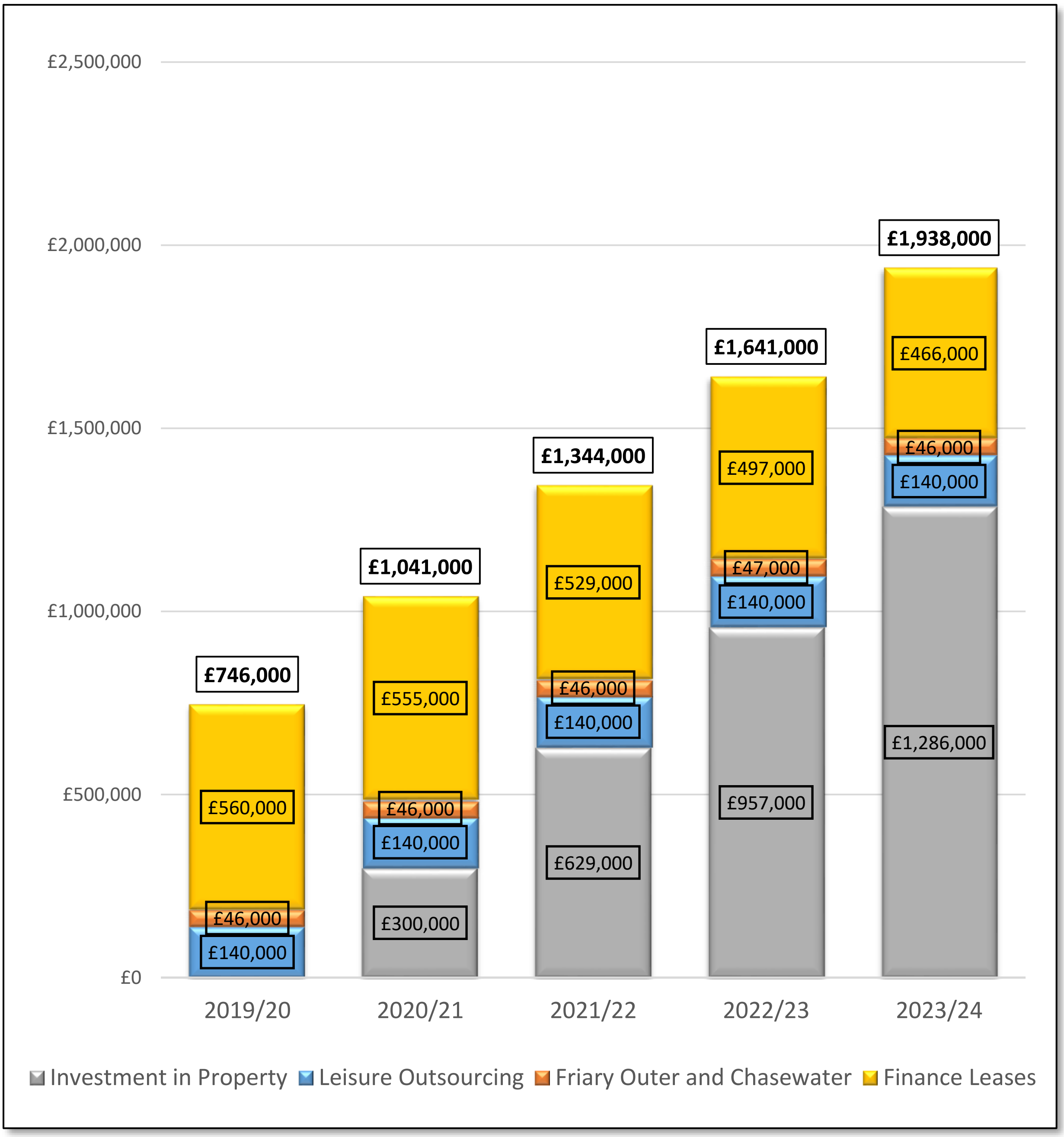
- The new Standard is applicable from 1 April 2020 and will require more arrangements, where there is a right to use an asset, to be included on the Council's Balance Sheet. The level of non-current assets is likely to increase and these will be matched by a liability to reflect the lease payments to be made.
- The identification and inclusion of these assets on the Council's Balance Sheet will also mean there will be an increase in the Capital Financing Requirement (Borrowing Need), financing and a number of Prudential Indicators related to debt.
- It is important to note that CIPFA/LASAAC published its proved text for the leases section of the 2020/21 Code in July 2019, in order to give local authorities time to prepare for the successful implementation of IFRS 16. However, it is understood that the final version of the 2020/21 Code will have some significant differences to the July text. However the only area potentially impacting on this Council is lessor leases for nil consideration, which are still under discussion.
- These changes have arisen due to late decisions made by HM Treasury for central government's adoption of IFRS 16, which CIPFA/LASAAC is keen to align with. The decision to exempt PFI schemes apparently relates to a politically unacceptable increase in liabilities under the new accounting standard.
- Review of the finance system and the list of leases used to compile the Statement of Accounts has identified a small number of assets where the arrangements are currently classified as operating leases that are therefore potentially in scope.
- However a number of these arrangements are for periods of less than 12 months or the asset value is likely to be less than £10,000 and therefore these can be excluded.
- In addition, there is also the arrangement being negotiated with Staffordshire County Council for Friary Grange leisure Centre for the 5 year extended opening that could be in scope depending on the Head of Terms.
- These arrangements are shown in more detail below:

| Asset / Service Description | Start | End | Finance System | Lease List Annual | Estimated Value | In Scope? |
|---|---|---|---|---|---|---|
| Land Burntwood LC | 25/03/1997 | 24/03/2122 | £3,854 | £5,139 | £254,000 | Yes |
| Land Burntwood LC - Clinic | In Negotiation | | £1,875 | £2,500 | | Possibly |
| Spot Hire | | | £3,175 | | | No < 12 months |
| Spot Hire | | | £2,234 | | | No < 12 months |
| Sweeper | 01/04/2019 | 31/03/2020 | £18,857 | | | No < 12 months |
| Chauffer's Car | 01/10/2016 | 28/09/2020 | £2,535 | £2,942 | | No < 12 months |
| Vending Machine Rental | 13/03/2018 | 12/03/2021 | £1,610 | £1,560 | | No < 12 months |
| Spot Hire | | | £2,425 | | | No < 12 months |
| Tourist Information Centre | In Negotiation | | | £12,000 | | Possibly |
| Friary Grange Leisure Centre | In Negotiation | | | TBD | | Possibly |
| | | **Total** | **£36,565** | **£24,140** | **£254,000** | |

- The arrangements in scope of the new Standard, plus any other new ones identified, will be assessed in more detail.
- However it is likely the value (excluding Friary Grange Leisure Centre) of the assets and matching liabilities will not be significant. At this stage the **£4,448,000** of finance lease 'head room' identified in both the Operational Boundary and Authorised Limit Prudential Indicators is likely to be sufficient to accommodate the new arrangements.
- However the Capital Programme will still need to be updated at a later date to add the assets and matching liabilities to the Council's Balance Sheet.

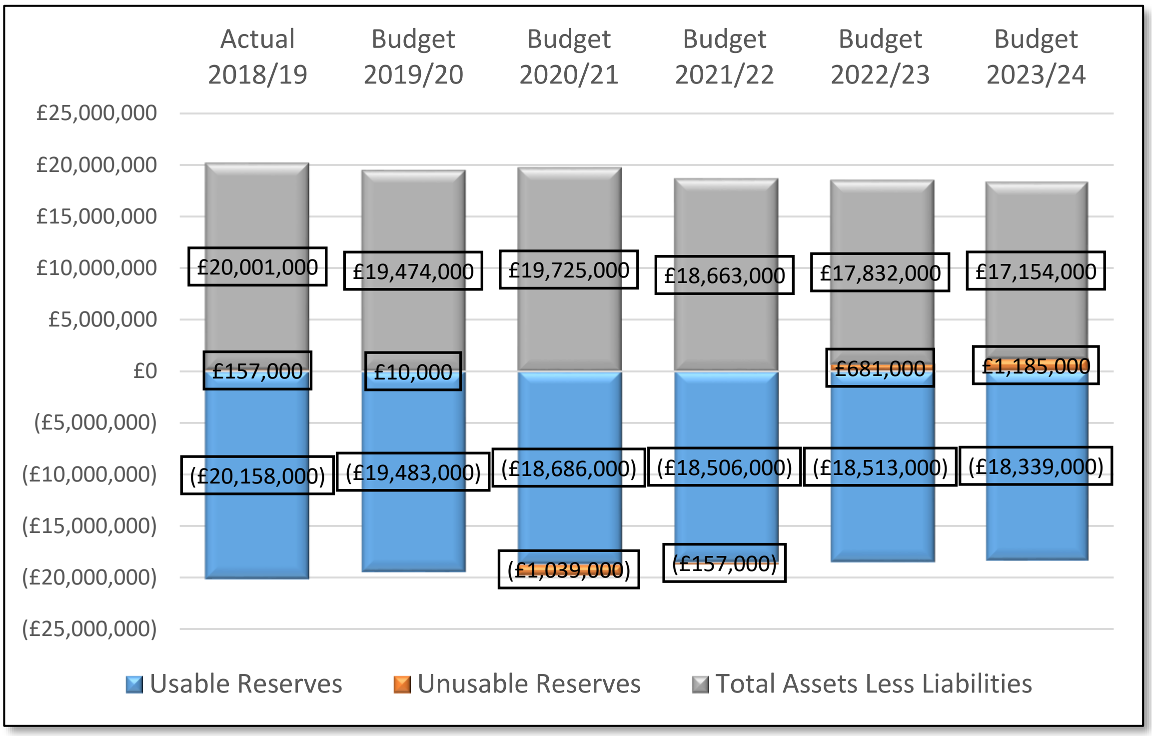
3.17 **Minimum Revenue Provision Statement 2020/21**

- The Council is required to make prudent provision for debt redemption (known as Minimum Revenue Provision (MRP)) and each year the Council must approve its MRP statement and this will include an allowance for finance leases that appear on the Council's Balance Sheet.
- As in previous years, the Council proposes to base its MRP on the estimated life of the asset **(APPENDIX C)**. The estimated MRP chargeable during the Medium Term Financial Strategy is shown below:



3.18 **Balance Sheet Projections**

- Integrated Revenue Budgets and a Capital Programme budgets are prepared. These budgets together with the actual Balance Sheet from the previous financial year are used to prepare Balance Sheet projections.
- These Balance Sheet projections (**APPENDIX D**) are significant in assessing the Council's Treasury Management Position in terms of borrowing requirement, investment levels and the Investment Strategy.
- The projected changes in the Balance Sheet over the Strategy period 2019/20 to 2023/24 are summarised below:




<u>Total Assets less Liabilities (a reduction of £2,847,000):</u>

1. **Non-Current Assets** – Non Current Assets will significantly increase with Investment in Property and the capital provision for a replacement Leisure Centre
2. **Borrowing and Leasing** – the capital investment in Non-Current Assets will partly be financed through an increase in external debt (borrowing and leases).
3. **Investments** – the levels are projected to reduce due to the financing of the Capital Programme from earmarked reserves, grants and contributions plus an increase in Internal Borrowing.
4. **Long term liability for pensions** – this value is projected to increase.

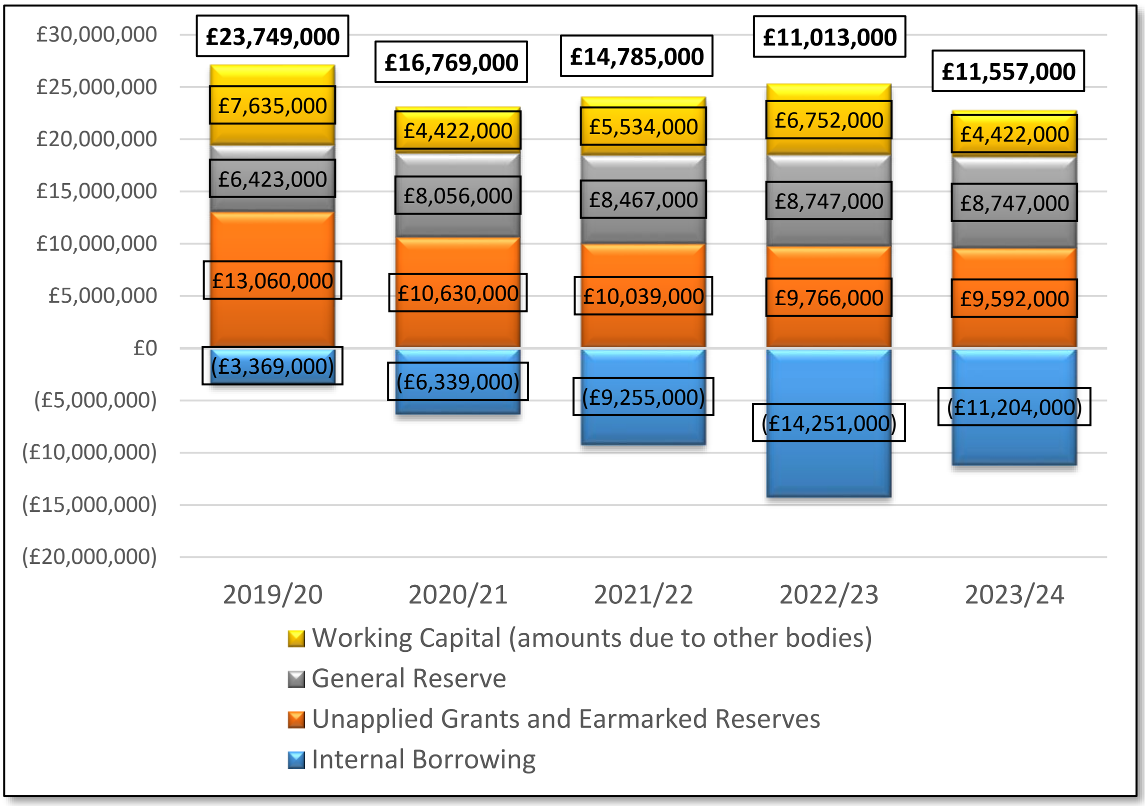
<u>Unusable Reserves (a reduction of £1,028,000):</u>

5. **Capital Funding** – this will increase as a result of the use of grants, contributions and capital receipts to fund capital investment.
6. **Pensions Reserve** – the negative value will increase to offset projected increases in the long term liability for pensions.

<u>Usable Reserves (a reduction of £1,819,000):</u>

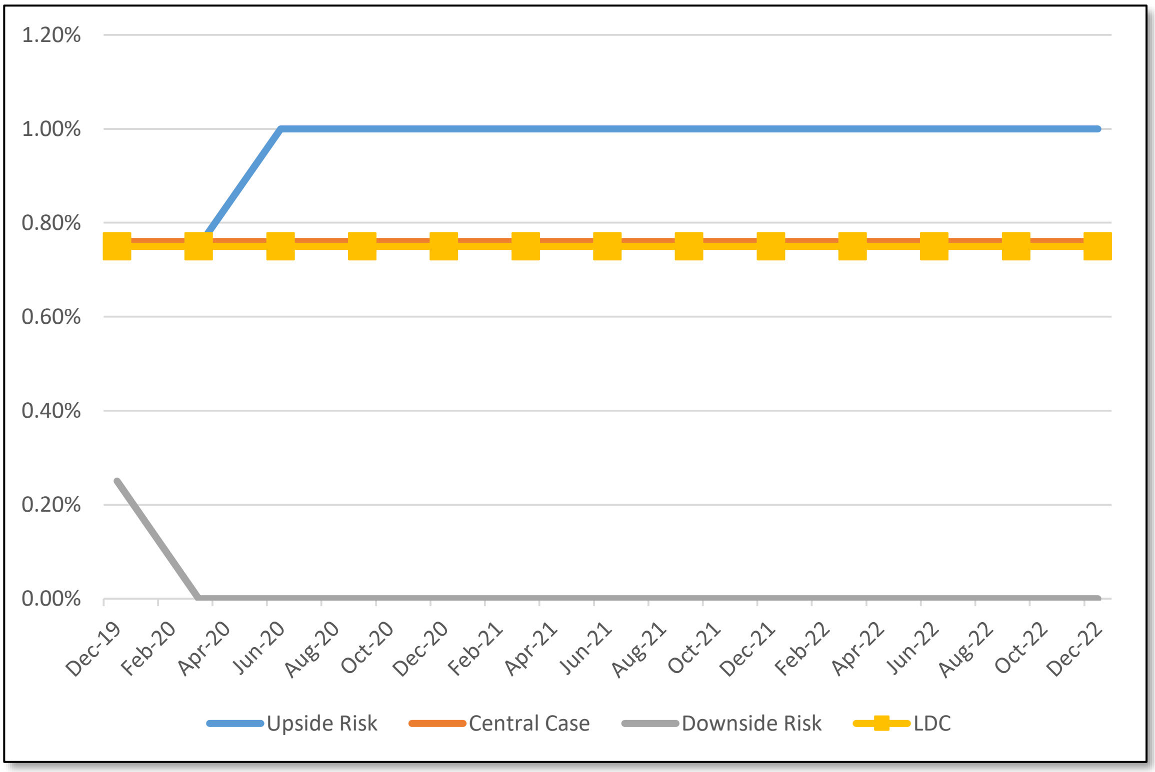
7. **Earmarked Reserves** – these will reduce as they are used to fund both revenue expenditure and the Capital Programme.
8. **General Reserve** – there will be an increase as a result of the contributions from 2019/20 and 2020/21 together with the transfer of projected New Homes Bonus in excess of the 'cap' up to 2022/23.

- The Balance Sheet Projections **(APPENDIX D)** also show the projected year end investment levels and the sources of cash:




3.19 **Treasury Management Advice and the Expected Movement in Interest Rates**

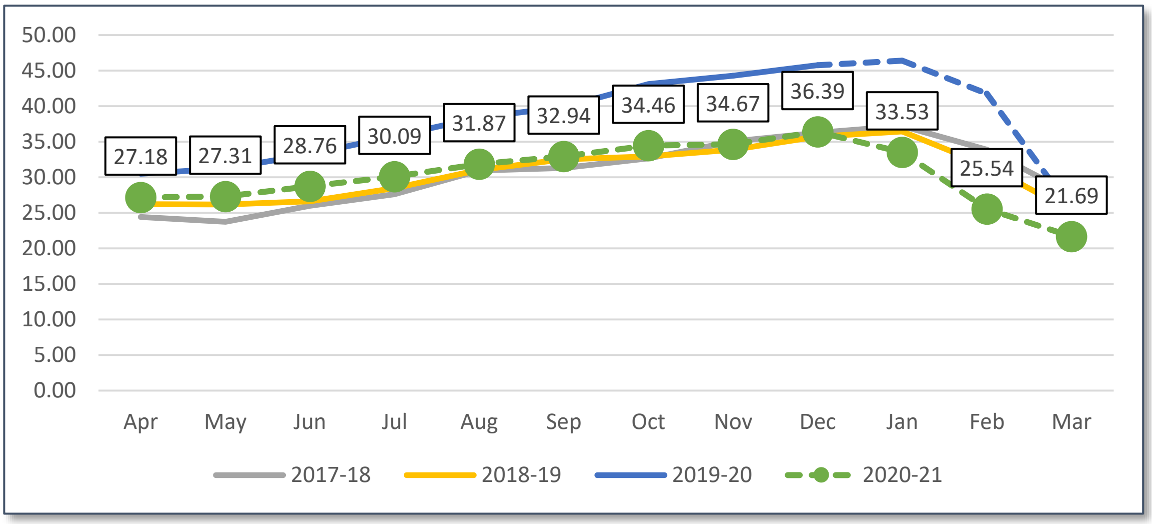
- The Official Bank Rate outlook provided by the Council's Treasury Advisor, together with the Council's assumption where interest rates remain at the current level of **0.75%**, is shown below:




- The Council assumptions have been used as the basis for preparation of the investment income and borrowing budgets for 2020/21 and future years.

3.20 **Cash Flow Forecast**

- Treasury Management includes the management of the Council's cash flows as a key responsibility. The cash flow forecast takes account of the income the Council receives including Housing Benefits Grant, Council Tax and Business Rate income and expenditure such as payments to precepting bodies, employee costs and Housing Benefit Payments.
- The graph below shows average investment levels throughout the financial year with a significant reduction in February and March due to minimal Council Tax income being received.




- The planned monthly cash flow forecast for the 2020/21 financial year has been used to calculate the investment income budget. The key components of this calculation are the average level of investment balances and the rate or yield achieved.
- The Treasury Management estimates for 2020/21 for both investment income and borrowing are shown in the table below:

| Treasury Management | 2020/21 Approved Budget | |
|---|---|---|
| | **Investment Income** | **Borrowing** |
| Average Balance | £31.27m | £10.10m |
| Average Rate | 1.27% | 2.68% |

| | | |
|---|---|---|
| Gross Investment Income | (£397,000) | |
| Property Fund Transfer to Reserves | £45,000 | |
| DIF Transfer to Reserves | £15,000 | |
| External Interest | | £273,000 |
| Internal Interest | | £4,000 |
| Minimum Revenue Provision (less Finance Leases) | | £486,000 |
| **Net Treasury Position** | **(£337,000)** | **£763,000** |
| | **£426,000** | |

- The gross interest receipts have been estimated as **(£397,000)** (this equates to 13% of The Council's income from Retained Business Rates of **£3,020,000** in **2020/21**), transfers to the Property and Diversified Income Reserves of **£60,000** and therefore Net Investment income is **(£337,000).**

3.21 **Treasury Management Strategy Statement and the Annual Investment Strategy**

- The Treasury Investments and their limits are shown in detail at **APPENDIX D** with proposed changes shown in red. The proposed changes for 2020/21 compared to those approved for 2019/20, principally to accommodate higher investment balances, are:

    1. **Approved Investment Counterparties and Limits** – Pooled Funds and Real Estate Investment Trusts. Recommended increase from **£2m per fund** to **£4m per fund** (based on Arlingclose advice of 10% of £42.3m[1]).
    2. **Investment Limits** – Any Group of Funds under the same Management. Recommended increase from **£9m per manager** to **£11m per manager** (based on Arlingclose advice of 25% of £42.3m).
    3. **Investment Limits** – Money Market Funds. Recommended increase from **£12m in total** to **£21m in total** (based on Arlingclose advice of 50% of £42.3m).
    4. **Strategic Fund Investments** – the Council diversified its investment portfolio to include two Strategic Fund investments with CCLA totalling **£4m**. To further diversify the investment portfolio and achieve higher returns, further potential investment of up to **£4m** is planned.

3.22 **Investment Strategy Report for 2020/21**

- This investment strategy that is shown at **APPENDIX E** meets the requirements of statutory guidance issued by the government in January 2018, and focuses on how the Authority invests its money to support local public services and earns investment income from commercial investments.

| Alternative Options | There are no alternative options. |
|---|---|

| Consultation | This Committee and the Strategic (Overview and Scrutiny) Committee. |
|---|---|

Financial Implications

**Prudential and Local Indicators (PIs)**

The Prudential and Local Indicators are shown below:

**Capital Strategy Indicators**

**Prudential Indicators**

| Indicators | 2018/19 Actual | 2019/20 Original | 2019/20 Revised | 2020/21 Original | 2021/22 Original | 2022/23 Original | 2023/24 Original |
|---|---|---|---|---|---|---|---|
| **Capital Investment** | | | | | | | |
| Capital Expenditure (£m) | £4.910 | £11.618 | £15.659 | £17.751 | £13.636 | £18.821 | £4.051 |
| Capital Financing Requirement (£m) | £4.987 | £10.301 | £14.809 | £25.432 | £35.777 | £51.245 | £51.567 |
| **Gross Debt and the Capital Financing Requirement** | | | | | | | |
| Gross Debt | (£4.315) | (£9.598) | (£11.439) | (£19.091) | (£26.520) | (£36.993) | (£40.362) |
| Borrowing in Advance - Gross Debt in excess of the Capital Financing Requirement | No | No | No | No | No | No | No |
| **Total Debt** | | | | | | | |
| Authorised Limit (£m) | £3.991 | £21.598 | £23.473 | £31.906 | £40.515 | £48.379 | £51.933 |
| Operational Boundary (£m) | £3.991 | £13.006 | £14.881 | £23.088 | £31.046 | £38.755 | £42.590 |
| Proportion of Financing Costs to Net Revenue Stream (%) | 5% | 6% | 4% | 10% | 17% | 22% | 27% |

**Local Indicators**

| Indicators | 2018/19 Actual | 2019/20 Original | 2019/20 Revised | 2020/21 Original | 2021/22 Original | 2022/23 Original | 2023/24 Original |
|---|---|---|---|---|---|---|---|
| Replacement of Debt Finance or MRP (£m) | (£0.709) | (£0.720) | (£0.746) | (£1.041) | (£1.344) | (£1.641) | (£1.938) |
| Capital Receipts (£m) | (£0.760) | (£1.056) | (£0.855) | (£0.537) | (£0.010) | (£0.010) | (£0.011) |
| Liability Benchmark (£m) | £14.168 | £5.017 | £3.938 | (£11.249) | (£21.191) | (£32.672) | (£35.963) |
| Treasury Management Investments (£m) | £26.876 | £23.689 | £23.749 | £16.769 | £14.785 | £11.013 | £11.557 |

[1] Highest projected balance in 2020/21 of £36m plus Internal Borrowing of £6.3m.

## Treasury Management Indicators

### Prudential Indicators

| | Lower Limit | Upper Limit | As at 31/03/19 | As at 31/12/19 |
|---|---|---|---|---|
| **Refinancing Rate Risk Indicator** | 0% | 100% | | |
| Under 12 months | 0% | 100% | 7.24% | 7.89% |
| 12 months and within 24 months | 0% | 100% | 7.32% | 7.99% |
| 24 months and within 5 years | 0% | 100% | 22.49% | 24.53% |
| 5 years and within 10 years | 0% | 100% | 36.43% | 33.48% |
| 10 years and within 20 years | 0% | 100% | 23.06% | 24.86% |
| 20 years and within 30 years | 0% | 100% | 3.46% | 1.24% |
| 30 years and within 40 years | 0% | 100% | | |
| 40 years and within 50 years | 0% | 100% | | |
| 50 years and above | 0% | 100% | | |

| Indicators | 2018/19 Actual | 2019/20 Original | 2019/20 Revised | 2020/21 Original | 2021/22 Original | 2022/23 Original | 2023/24 Original |
|---|---|---|---|---|---|---|---|
| Principal Sums invested for periods longer than a year (£m) | £2.000 | £6.000 | £6.000 | £10.000 | £10.000 | £10.000 | £10.000 |

### Local Indicators

| Indicators | 2018/19 Actual | 2019/20 Original | 2019/20 Revised | 2020/21 Original | 2021/22 Original | 2022/23 Original | 2023/24 Original |
|---|---|---|---|---|---|---|---|
| | £m | £m | £m | £m | £m | £m | £m |
| **Balance Sheet Summary and Forecast** | | | | | | | |
| Borrowing Capital Financing Requirement | £3.312 | £9.152 | £13.694 | £24.871 | £35.745 | £48.450 | £49.238 |
| Internal (over) Borrowing | £0.672 | £0.703 | £3.370 | £6.340 | £9.256 | £14.252 | £11.205 |
| Investments (or New Borrowing) | (£26.519) | (£23.689) | (£23.748) | (£16.093) | (£14.109) | (£10.337) | (£10.881) |
| Liability Benchmark | (£14.168) | (£5.017) | (£3.938) | £11.249 | £21.191 | £32.672 | £35.963 |

| | Target |
|---|---|
| **Security** | |
| Portfolio average credit rating | A- |
| **Liquidity** | |
| Temporary Borrowing undertaken | £0.000 |
| Total Cash Available within 100 days (maximum) | 90% |

| | |
|---|---|
| Contribution to the Delivery of Lichfield District Council's Strategic Plan | The report directly links to overall performance and especially the delivery of Lichfield District Council's Strategic Plan. |
| Equality, Diversity and Human Rights Implications | These areas are addressed as part of the specific areas of activity prior to being included in Lichfield District Council's Strategic Plan. |
| Crime & Safety Issues | These areas are addressed as part of the specific areas of activity prior to being included in Lichfield District Council's Strategic Plan. |
| GDPR/Privacy Impact Assessment | None identified in this report. |

| | Risk Description | How We Manage It | Severity of Risk (RYG) |
|---|---|---|---|
| A | Planned Capital Receipts are not received. | The budget for capital receipts will be monitored as part of The Council's normal budget monitoring procedures. | Green - Tolerable |
| B | Non achievement of The Council's key Council priorities. | Close monitoring of performance and expenditure; maximising the potential of efficiency gains; early identification of any unexpected impact on costs including Central Government Policy changes, movement in the markets and changes in the economic climate. | Green - Tolerable |
| C | The affordability and risk associated with the Capital Strategy (see specific risk assessment in the Capital Strategy). | An estates management team has been recruited to provide professional expertise and advice in relation to investment in property and to continue to take a prudent approach to budgeting. | Yellow - Material |

## Background documents:

- CIPFA Code of Practice for Treasury Management in the Public Services
- The Prudential Code for Capital Finance in Local Authorities
- Money Matters: Medium Term Financial Strategy (Revenue and Capital) 2018-23 – Cabinet 12 February 2019
- Allocation of Strategic Community Infrastructure Levy (CIL) Funding – Cabinet 12 March 2019
- Multi Storey Car Park – Cabinet 12 March 2019
- Money Matters: 2018/19 Review of Financial Performance against the Financial Strategy – Cabinet 13 June 2019
- Jigsaw Funding Agreement – Cabinet 9 July 2019
- Money Matters: 2019/20 Review of Financial Performance against the Financial Strategy – Cabinet 10 September 2019
- Birmingham Road Site Enabling Works – Cabinet 10 September 2019
- Friary Grange Leisure Centre – Cabinet 7 October 2019
- Medium Term Financial Strategy 2019-24 – Cabinet 8 October 2019
- St Stephen's School allocation of Section 106 – Cabinet Member Decision 24 October 2019
- Community Lottery – Cabinet 12 November 2019
- Money Matters: 2019/20 Review of Financial Performance against the Financial Strategy – Cabinet 3 December 2019
- Money Matters: Calculation of Business Rates 2020/21, Council Tax Base for 2020/21 and the projected Collection Fund Surplus / Deficit for 2019/20 – Cabinet 3 December 2019
- Money Matters: 2019/20 Review of Financial Performance against the Financial Strategy – Cabinet 11 February 2020
- Capital Bids

## Relevant web link:

# Capital Strategy

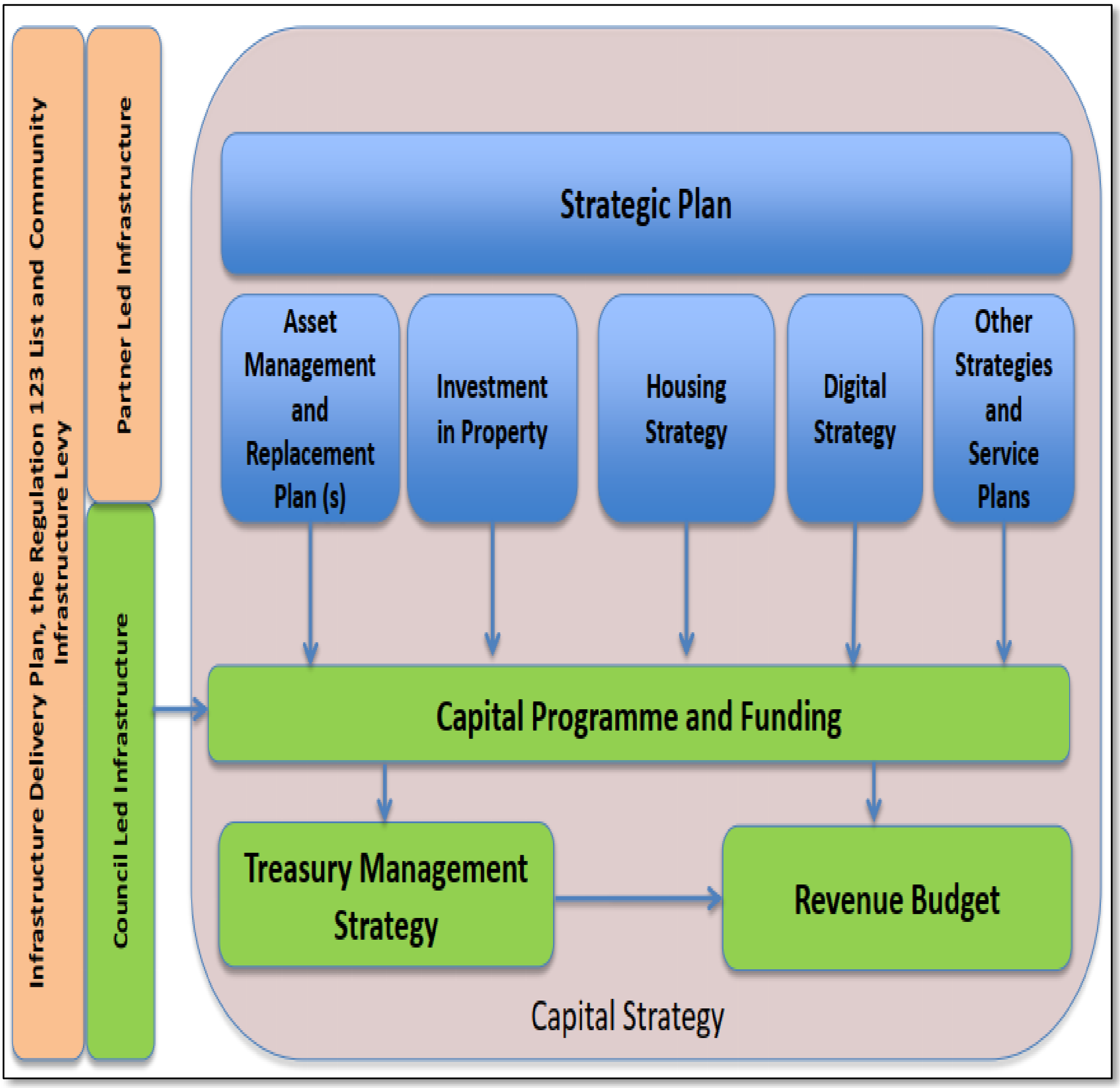
## 1. Introduction

1.1. The Prudential Code requires the completion of a Capital Strategy that is approved by Full Council.

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

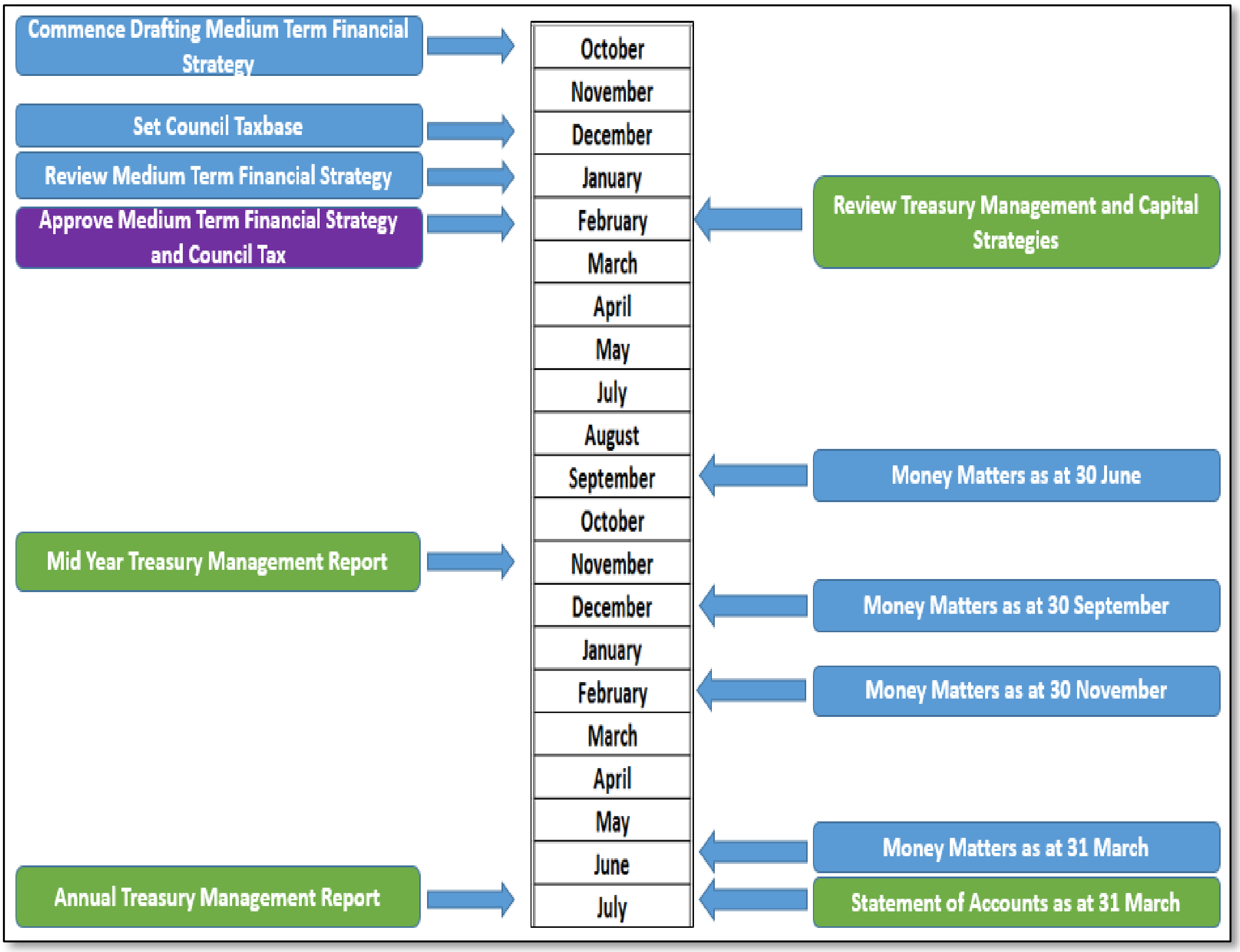
1.3. It forms part of the Councils integrated revenue, capital and balance sheet planning. The Council already undertakes elements of the new requirements although some areas such as Asset Management Planning need further development.

1.4. The Prudential Code now requires all of this information to be brought together in a single place as shown below:



## 2. The Capital Programme

2.1. The financial planning process and its Governance (Blue is Cabinet and Strategic (Overview and Scrutiny) Committee, Green is Audit and Member Standards and Purple is Council) is shown below:




**The Capital Programme Process**

2.2. As the Council becomes more commercial and Asset Management Plans are developed, it is probable that capital needs will be identified that exceed resources available thus necessitating a more transparent and robust process to inform Members during the development of the MTFS.

2.3. This process has been designed to ensure consistency, objectivity, equity and transparency to the prioritisation and allocation of capital funding, while ensuring we get maximum value for money.

2.4. A summary of the new process is identified below:

- Service identifies a budget requirement and consults with the Finance and Procurement Team.
- Service requests funding by completing and submitting a funding bid form.
- Service completes a funding bid financial profile form and submits this with their bid.
- Service completes a funding bid assessment form and submits this with their bid.
- The Finance and Procurement Team reviews all bids and assessments and requests clarification where required.
- The Finance and Procurement Team reviews bids using the assessment criteria and submits a report to Leadership Team.

- Leadership Team review all bids and recommend changes before recommending the allocation of funding either through a Cabinet Report or through the MTFS.
- Finance and Procurement monitor funding allocations and spend, reporting to Leadership Team as part of Money Matters Reports.
- Service completes work / project outlined within the bid and undertakes a review (i.e. post-project review) within 6 months of work being completed, providing this to Finance and Procurement to include in a report to Leadership Team.

**Planning Obligations - Section 106 and Community Infrastructure Levy (CIL)**

2.5. As part of the planning process planning obligations, including the Community Infrastructure Levy, are received from new developments. The vast majority is spent directly on infrastructure works or will be spent in line with the Infrastructure Delivery Plan (IDP).

2.6. There is however an element of contributions, which afford an element of discretion on how they are allocated. These contributions towards social and community facilities are linked to the development proposed.

2.7. Whilst some of these financial contributions are very specific in terms of the projects on which they must be spent, a proportion is to be allocated towards appropriate social and community schemes that result in time from the proposed development.

2.8. The Council's Capital Programme includes a number of projects that are to be funded by Section 106 and will begin to include projects funded by CIL; this is a significant source of funding and there is a significant level of interest from the community in relation to the allocation of sums to projects.

2.9. The **Capital Programme** and its **funding** by Strategic Priority is summarised below:

| Strategic Priority | 2019/20 £000 | 2020/21 £000 | 2021/22 £000 | 2022/23 £000 | 2023/24 £000 | Total £000 | Corporate £000 |
|---|---|---|---|---|---|---|---|
| Enabling People | 2,324 | 3,424 | 1,164 | 3,324 | 3,235 | 13,471 | 396 |
| Shaping Place | 809 | 1,045 | 502 | 3,482 | 427 | 6,265 | 273 |
| Developing Prosperity | 1,732 | 625 | 0 | 0 | 0 | 2,357 | 471 |
| A Good Council | 10,794 | 12,657 | 11,970 | 12,015 | 389 | 47,825 | 2,682 |
| **Grand Total** | **15,659** | **17,751** | **13,636** | **18,821** | **4,051** | **69,918** | **3,822** |

| Funding Source | 2019/20 £000 | 2020/21 £000 | 2021/22 £000 | 2022/23 £000 | 2023/24 £000 | Total £000 |
|---|---|---|---|---|---|---|
| Capital Receipts | 547 | 1,402 | 514 | 559 | 352 | 3,374 |
| Capital Receipts - Statue | 53 | 0 | 0 | 0 | 0 | 53 |
| Revenue - Corporate | 0 | 182 | 0 | 0 | 213 | 395 |
| **Corporate Council Funding** | **600** | **1,584** | **514** | **559** | **565** | **3,822** |
| Grant | 1,266 | 2,343 | 931 | 931 | 931 | 6,402 |
| Section 106 | 673 | 865 | 25 | 0 | 0 | 1,563 |
| CIL | 221 | 79 | 0 | 0 | 0 | 300 |
| Reserves | 1,946 | 1,066 | 327 | 72 | 145 | 3,556 |
| Revenue (Joint Waste Service) | 150 | 150 | 150 | 150 | 150 | 750 |
| Sinking Fund | 235 | 0 | 0 | 0 | 0 | 235 |
| Leases | 0 | 0 | 0 | 3,260 | 0 | 3,260 |
| **Total** | **5,091** | **6,087** | **1,947** | **4,972** | **1,791** | **19,888** |
| **Borrowing Need** | **10,568** | **11,664** | **11,689** | **13,849** | **2,260** | **50,030** |
| **Funding Total** | **15,659** | **17,751** | **13,636** | **18,821** | **4,051** | **69,918** |

**APPENDIX A**

2.10. The Revenue implications are shown below:

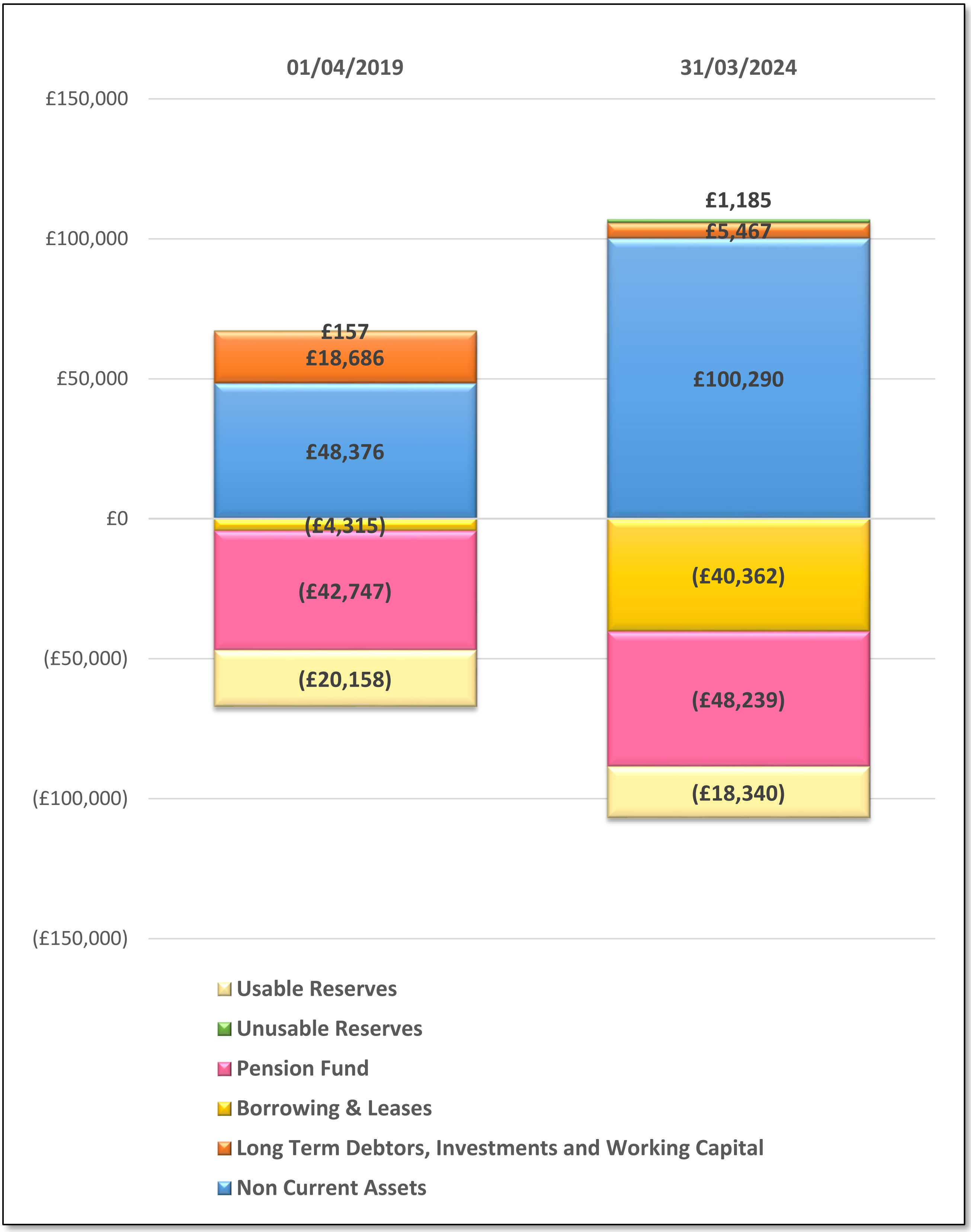
| Revenue Implications | 2019/20 £000 | 2020/21 £000 | 2021/22 £000 | 2022/23 £000 | 2023/24 £000 | Total £000 |
|---|---|---|---|---|---|---|
| <u>Approved Budgets</u> | | | | | | |
| Investment in Property | 0 | (56) | (180) | (303) | (427) | (966) |
| Interest on Loan to the LA Company | 0 | (4) | (18) | (22) | (22) | (66) |
| Leisure Outsourcing | (57) | (58) | (61) | (63) | (63) | (302) |
| Friary Grange - Refurbishment | 33 | 135 | 135 | 135 | 135 | 573 |
| Digital Strategy | 50 | (30) | (100) | (150) | (150) | (380) |
| **Approved Budget** | **26** | **(13)** | **(224)** | **(403)** | **(527)** | **(1,141)** |
| <u>Capital Programme</u> | | | | | | |
| Revenue Implications of Bids | 0 | 78 | 68 | 79 | 37 | 262 |
| Property - Internal Borrowing | 0 | (31) | (98) | (164) | (231) | (524) |
| Revenue Budget | 0 | 182 | 0 | 0 | 213 | 395 |
| **Changes to Approved Budget** | **0** | **229** | **(30)** | **(85)** | **19** | **133** |
| **Capital Programme** | **26** | **216** | **(254)** | **(488)** | **(508)** | **(1,008)** |

2.11. Planned disposals (and grant repayments) resulting in capital receipts and their use in funding the Capital Programme are shown in the table below:

| Capital Receipts | 2019/20 £000 | 2020/21 £000 | 2021/22 £000 | 2022/23 £000 | 2023/24 £000 | Total £000 |
|---|---|---|---|---|---|---|
| **Opening Balance** | **(2,004)** | **(2,259)** | **(1,394)** | **(890)** | **(341)** | **(2,004)** |
| Guardian House Covenant | (320) | | | | | (320) |
| Sale of Beacon Cottage | (368) | | | | | (368) |
| Sale of land at Netherstowe and Leyfields | | (527) | | | | (527) |
| Right to Buy Receipts | (157) | | | | | (157) |
| Other Receipts | (10) | (10) | (10) | (10) | (11) | (51) |
| Utilised in Year | 600 | 1,402 | 514 | 559 | 352 | 3,427 |
| **Closing Balance** | **(2,259)** | **(1,394)** | **(890)** | **(341)** | **0** | **0** |

## 3. The Balance Sheet (in £000s)

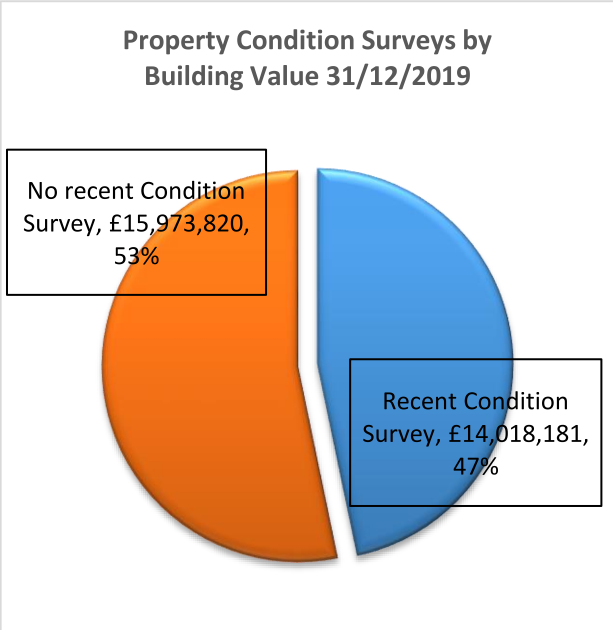
3.1. The Capital Programme and its funding will significantly impact on the Council's Balance Sheet through investment in property funded by borrowing:

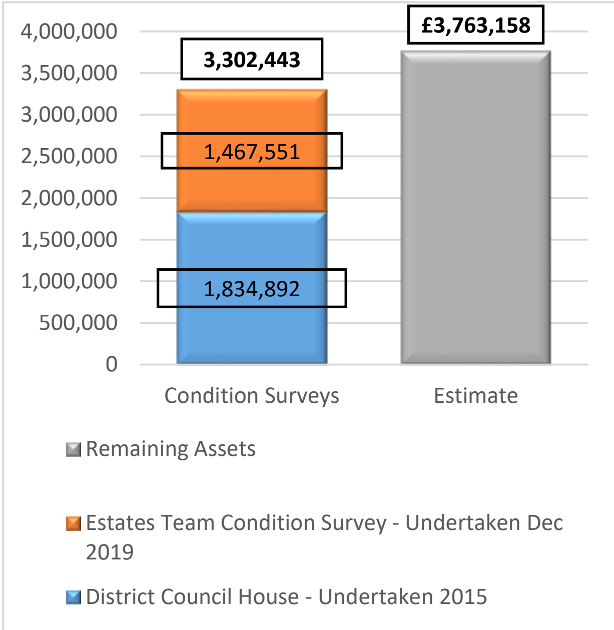


## 4. Asset Management Planning

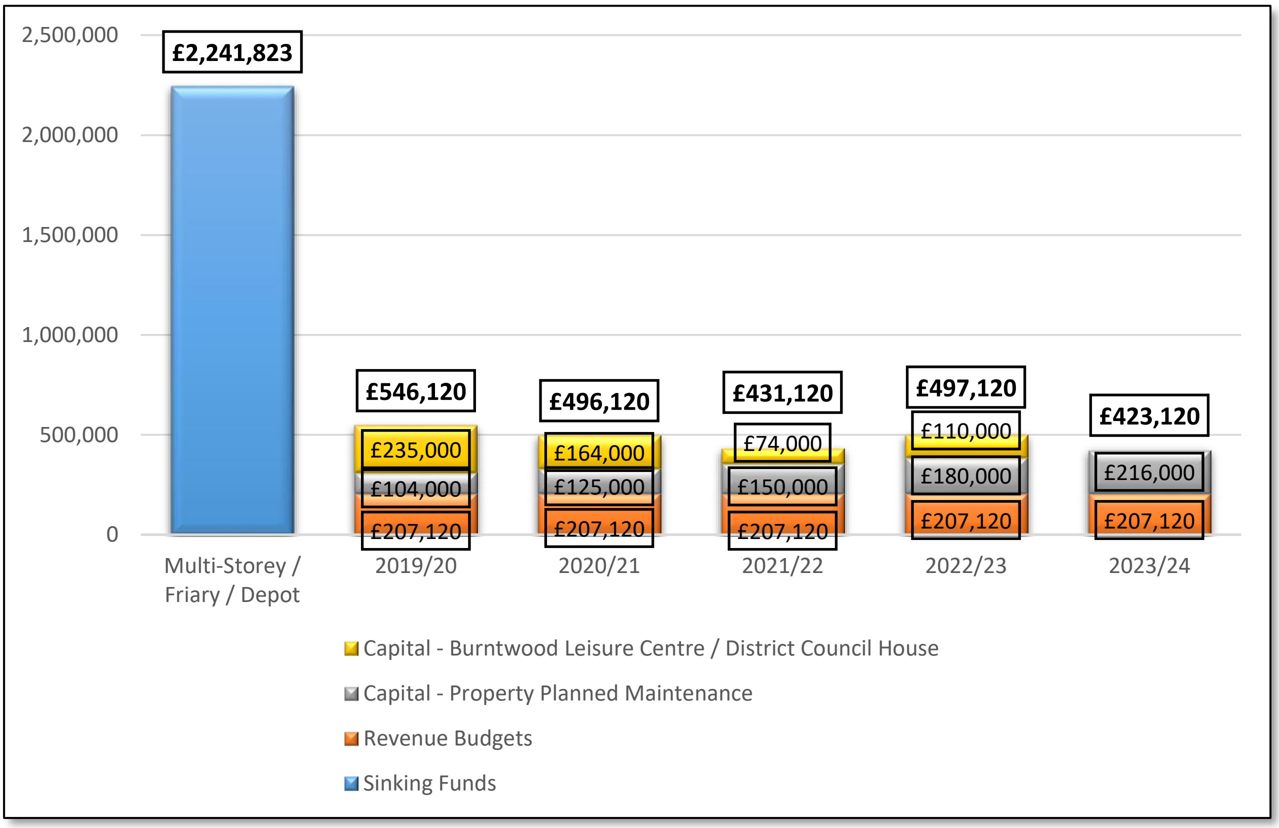
4.1. The Estates Team is currently in the process of undertaking Property Condition Surveys for Property Assets owned by the Council.

4.2. Property assets with recent Property Condition Surveys and the backlog maintenance identified plus a projection for all property assets is shown below:

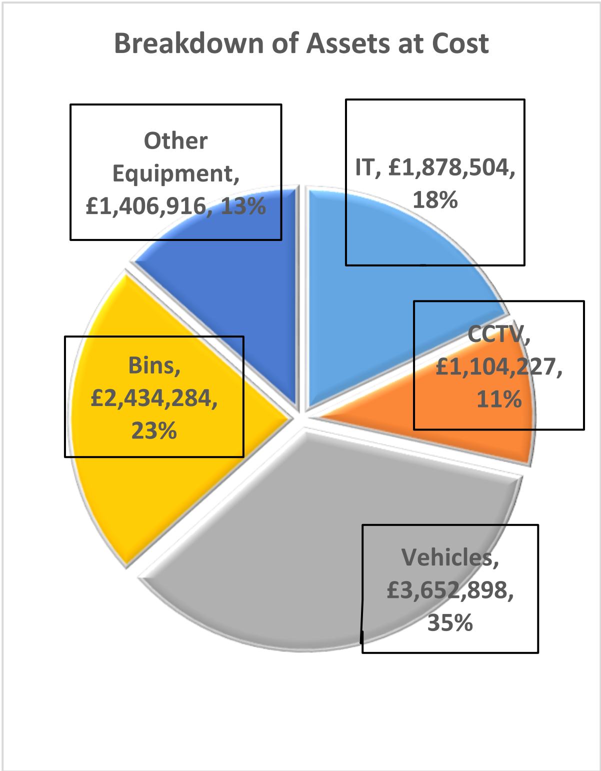


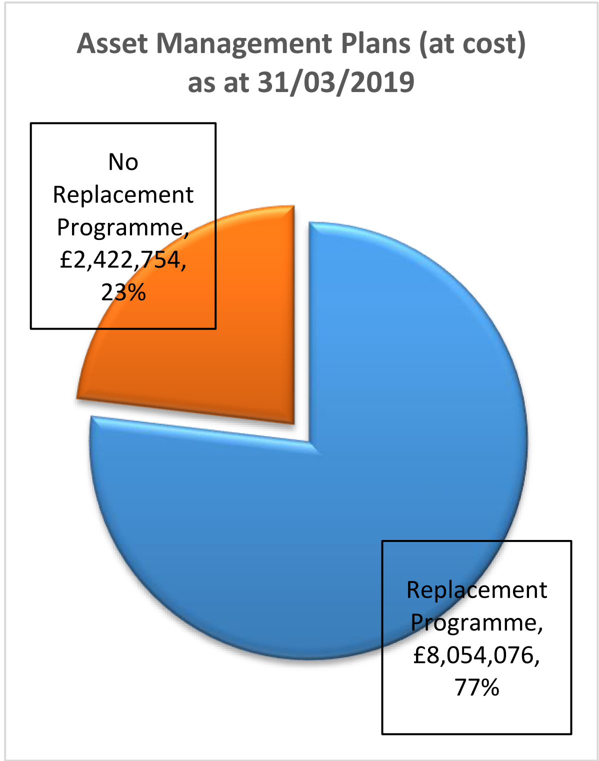




4.3. The resources identified for enhancement and maintenance of property assets are:

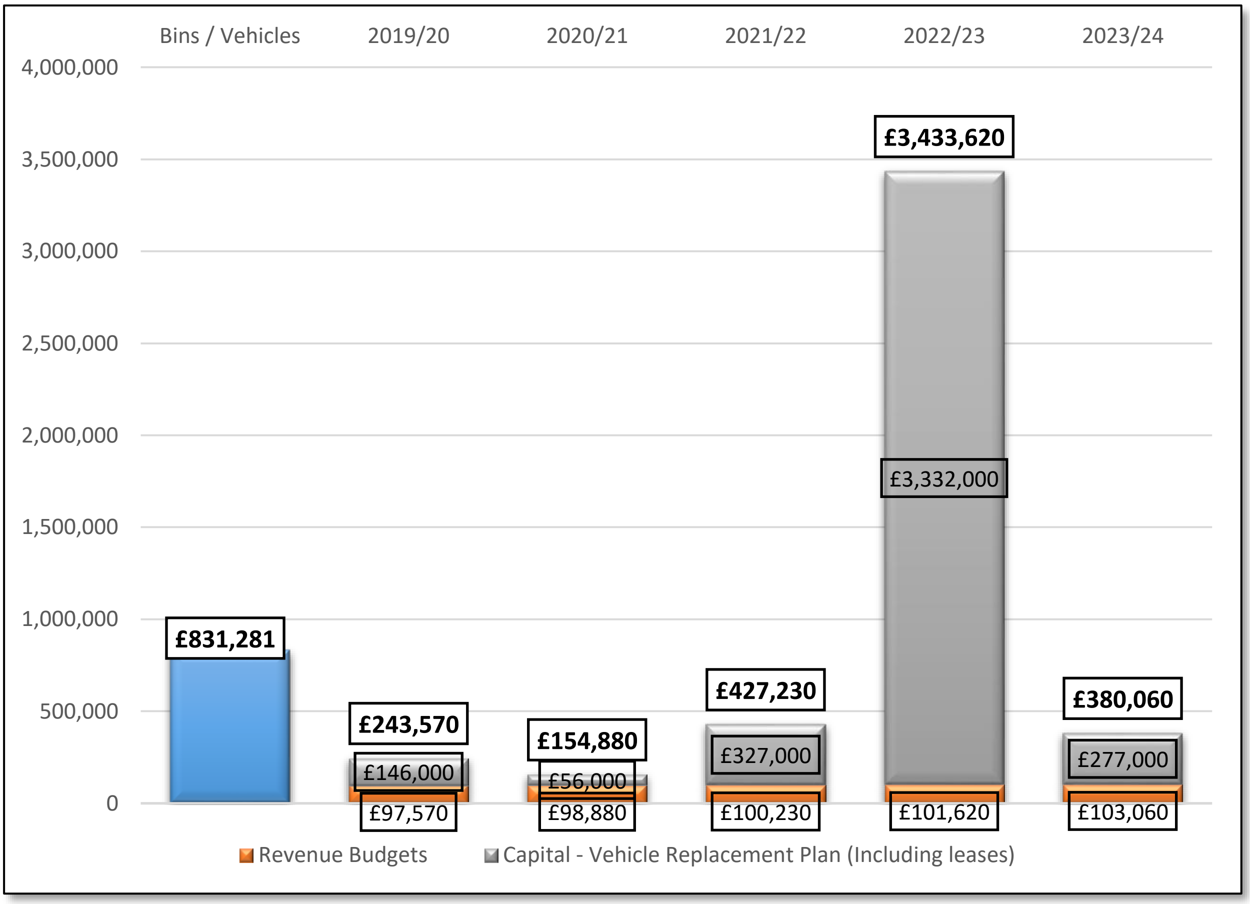


4.4. The Asset Management Plans in place for vehicles, plant and equipment assets are:




4.5. The resources identified for replacement and maintenance of vehicles, plant and equipment are:



## 5. Investment in Property

5.1. The Council is committed to investing in land and property to shape places, enable regeneration, enhance communities, grow the economy, meet local housing needs and thereby deliver its strategic objectives whilst also providing opportunities to realise an ongoing source of income. For this reason, the council approved an investment fund of £45m to invest in land and property assets across the district.

5.2. The Council must give due consideration to the drivers for investment (below), along with the guidance from CIPFA and the Ministry of Housing, Communities and Local Government. The latter is a clear steer to look at investments as listed below, where yield is the last consideration after security and liquidity, so that a focus on the potential return on investment does not hamper the need for appropriate due diligence and assessment of risk.

1. **Security** – ensure capital sums are largely protected from loss.
2. **Liquidity** – ensure money is available when required to meet ongoing needs.
3. **Yield** – ensure there is a viable and sustainable return on investment.

5.3. To ensure the maximum number of benefits are achieved, that public perception is considered and that management cost are optimised, the following principles have been selected by the Council to govern any decisions made on property investment;

- **Diversified** – property investment will be diversified to broaden the portfolio and so reduce the risk, with a focus given to particular groups, such as housing and offices, when justification is clear and evidenced
- **Local** – property will be within the District of Lichfield, or within the functional economic geography. It should be close enough to allow it to be effectively managed and maintained, as well as being appealing to tenants or purchasers now and in the future.
- **Profitable** – property investment will provide a return on investment, either through lettings or sales. The yield on the property should exceed the ongoing costs for management, maintenance and borrowing, while considering the full costs of acquisition or development (e.g. Stamp Duty, legal fees, external valuations and structural surveys). To ensure these principles are considered in each case any decision to invest will be supported by the introduction of an assessment methodology, considering the key aspects of the property, such as; location, tenancy strength, tenure, lease length, repairing terms and size. This could be done through an assessment matrix, which would provide a level of assurance and objectivity to decision making.
- **Prudent** – property investment will be appropriately risk assessed. Where acquisition is being considered, the current tenancy should offer some security in relation to the length of tenure, strength of the covenant and ongoing viability of the tenant. Where development is being considered, likely tenancies and pre-lets would need to be leveraged to support any financial assessment.
- **Sustainable** – property investment decisions will support the council to reduce the impact it has on the environment. Property acquisitions will consider the environmental impact of either the property or the nature of the businesses who will utilise it. In addition, when undertaking development the council will seek to adopt sustainable forms of construction wherever feasible and practicable.

- **Strategic** – property investment should be for the long-term and be regularly rebalanced to support our strategic priorities as well as being acceptable to our community.

5.4. Investment, including property acquisitions and development, always attracts a level of risk and higher returns are often associated with higher risks. This is one of the reasons for every decision to be appropriately risk assessed, while the overall portfolio should be adequately managed to reduce the risk attached to it.

5.5. Risk will come from a number of factors, including;

- **Customer** – reputational damage from resident perception of investment
- **Economic** – periods of rental decline or lack of income, the costs of maintaining the property and falls in property values in a recessionary environment, certain property market segments or certain geographical areas becoming less attractive than others
- **Legislative** – changes to ownership, investment or borrowing legislation
- **Political** – changes to national government or local priorities,
- **Tenant** - in the form of default/insolvency, resulting in loss of rental income and voids

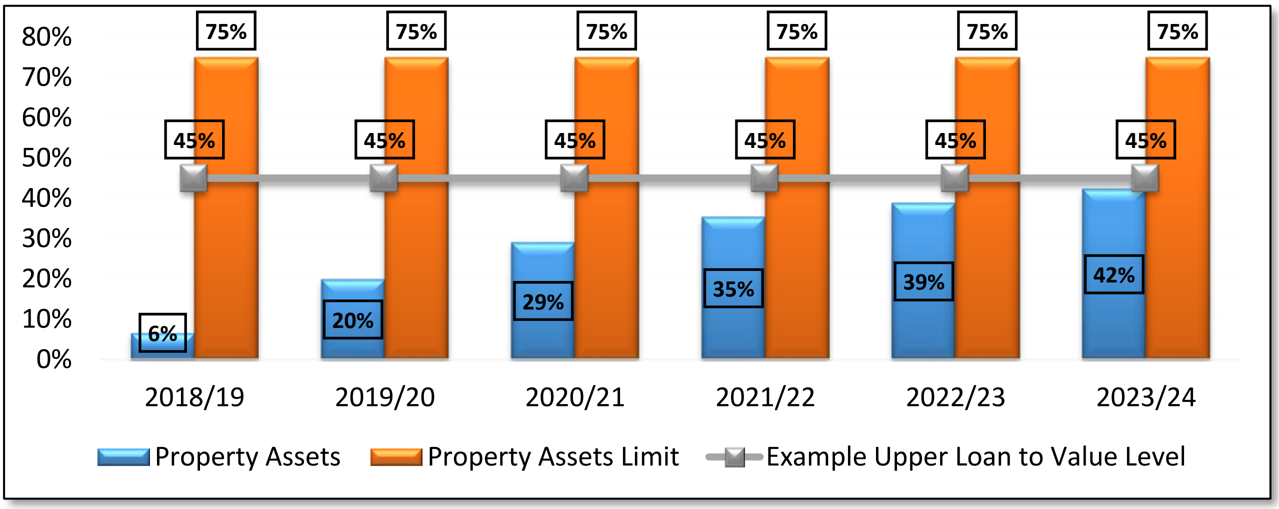
5.6. Ongoing risk, will be managed through standard risk management policies and procedures, ensuring appropriate transparency and challenge.

5.7. Investment in property will predominantly be funded through borrowing, however other funding routes will be considered where it would support the affordability of the investment being proposed and the non-financial benefits it would offer.

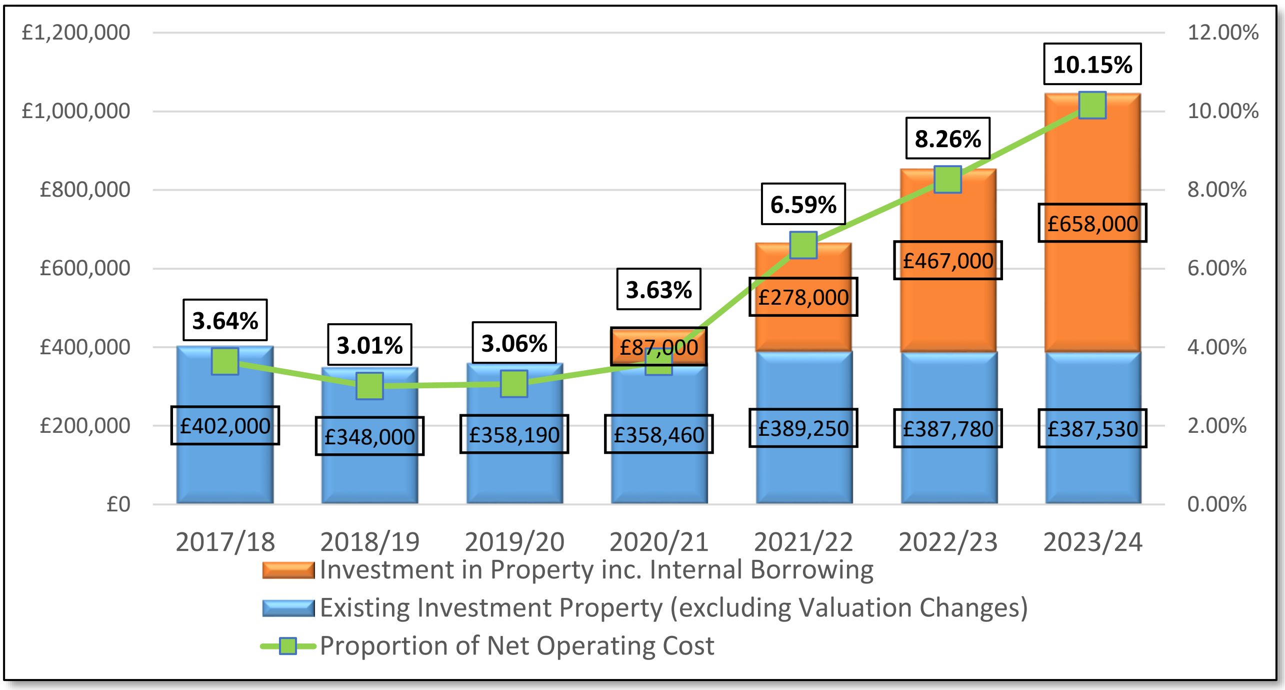
5.8. The level of property value funded by borrowing is known as gearing and in the private sector is measured as the loan to value (LTV) ratio. The private sector will set a maximum loan to value range for property typically **35%** to **45%** to manage the risk that the loans outstanding are unable to adapt to changing asset strategy or property value. This will be evident in a recession where typically property values reduce and loans therefore can exceed property value (known as negative equity).

5.9. A negative equity scenario can make it difficult to rebalance the portfolio through disposals due to the existing loan repayments that will still need to be paid whilst income is no longer received.

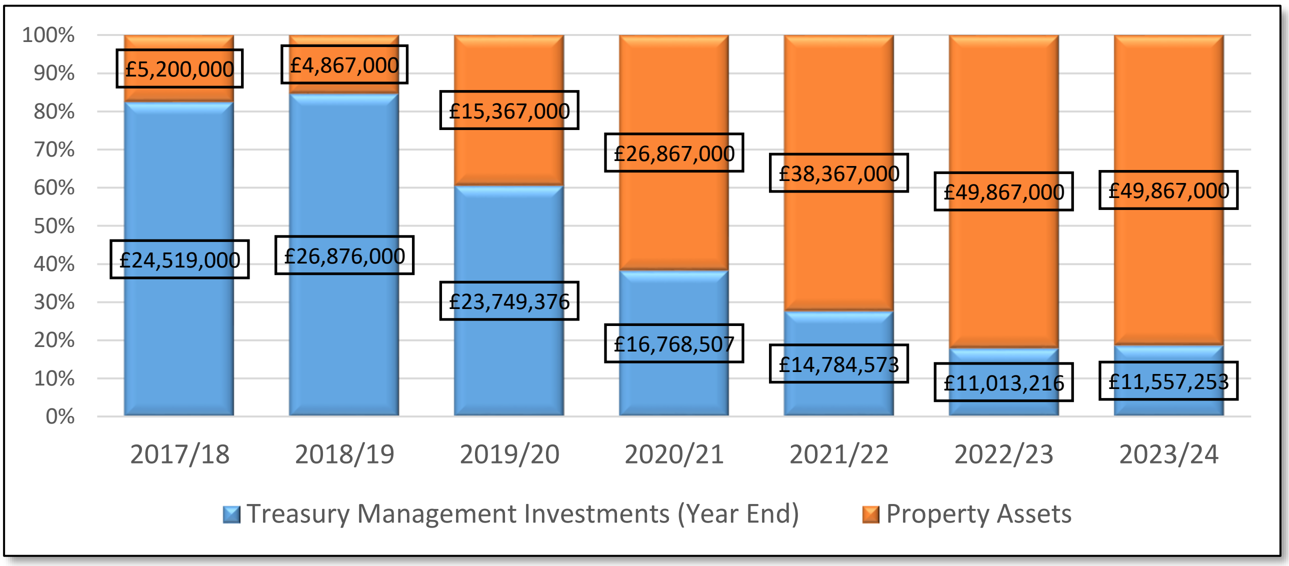
5.10. The projected gearing ratio and an example upper loan to value limit from a property investment company is shown below:



5.11. The Revenue Budget supported by income (including the savings from Internal Borrowing) is:




5.12. The ratio of Treasury Management Investments to relevant Property Investments is shown below:




5.13. The Council has a joint venture partnership with PSP for property established in 2016/17 and Lichfield Housing Limited (a Local Authority Trading Company) was incorporated in September 2019 with an aim to deliver development and housing ambitions.

5.14. The Capital Programme includes an equity investment of **£225,000** in 2019/20 and a loan of up to **£675,000** in 2020/21 for a period of **5 years** to facilitate housing development.

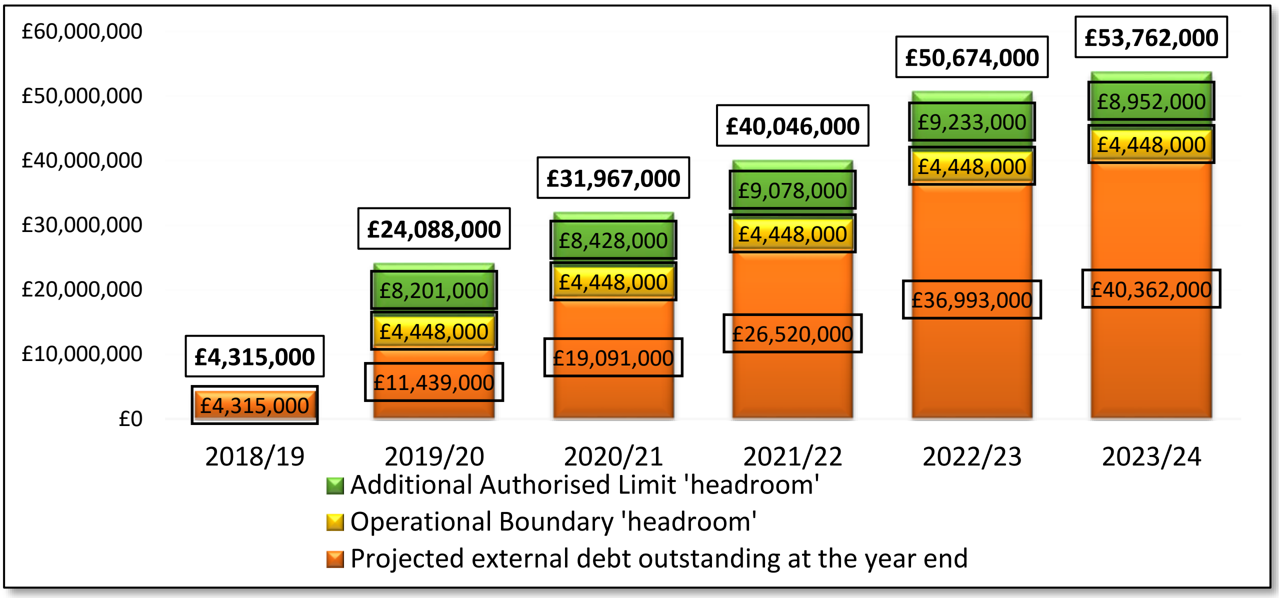
5.15. The loan to the Company will produce an income stream at **4%** from the company and the loan repayment will be treated as a capital receipt in 2024/25 in the Medium Term Financial Strategy. At present, no dividend income is assumed to be received from the Company.

5.16. The investment rate of return (net of all costs) is forecast to be **9.38%** for 2020/21.

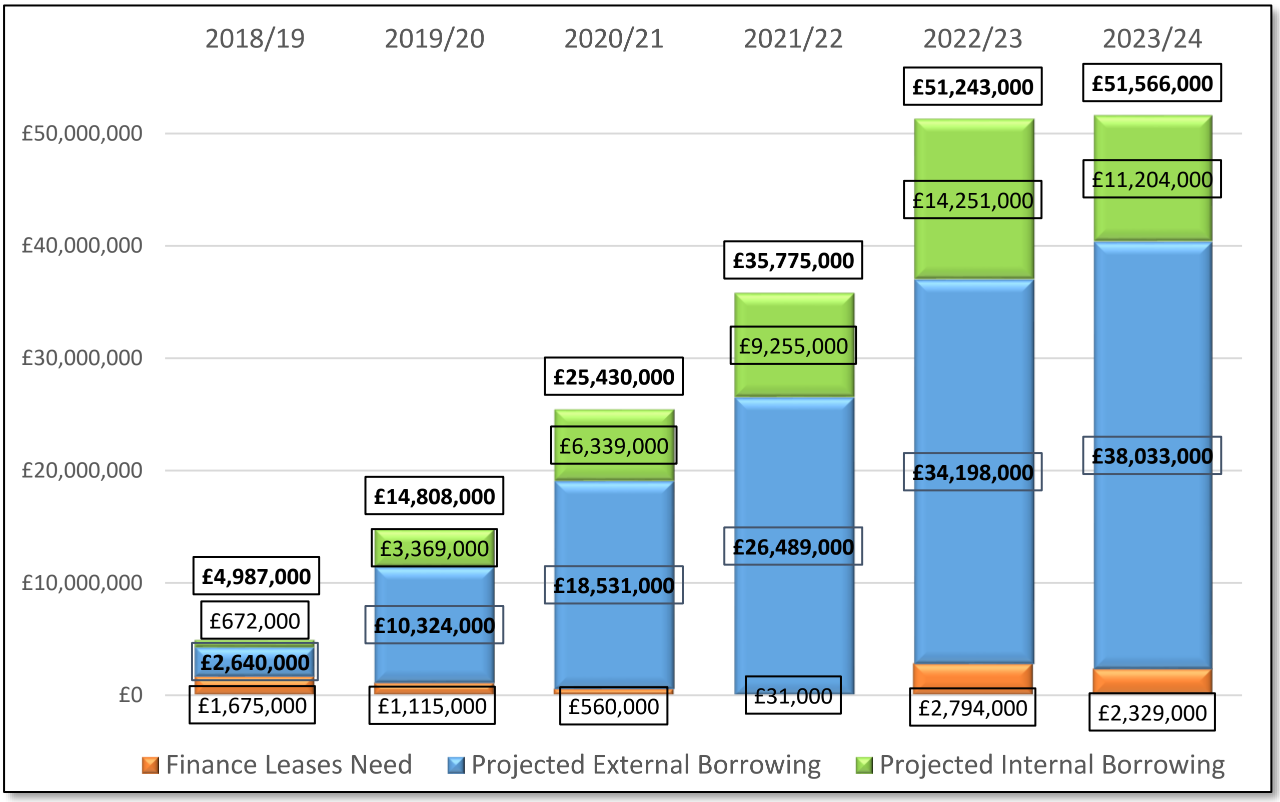
## 6. Debt Management

6.1. At the 31 March 2019 the Council had a relatively low level of debt outstanding of **£4.315m**. The Investment in Property and the renewal of the waste fleet will mean external debt is projected to increase to **£40.362m** by 31 March 2024.

6.2. The Council is managing its debt through setting Prudential Indicators related to the statutory maximum known as the **Authorised Limit** and an **Operational Boundary** as shown below:

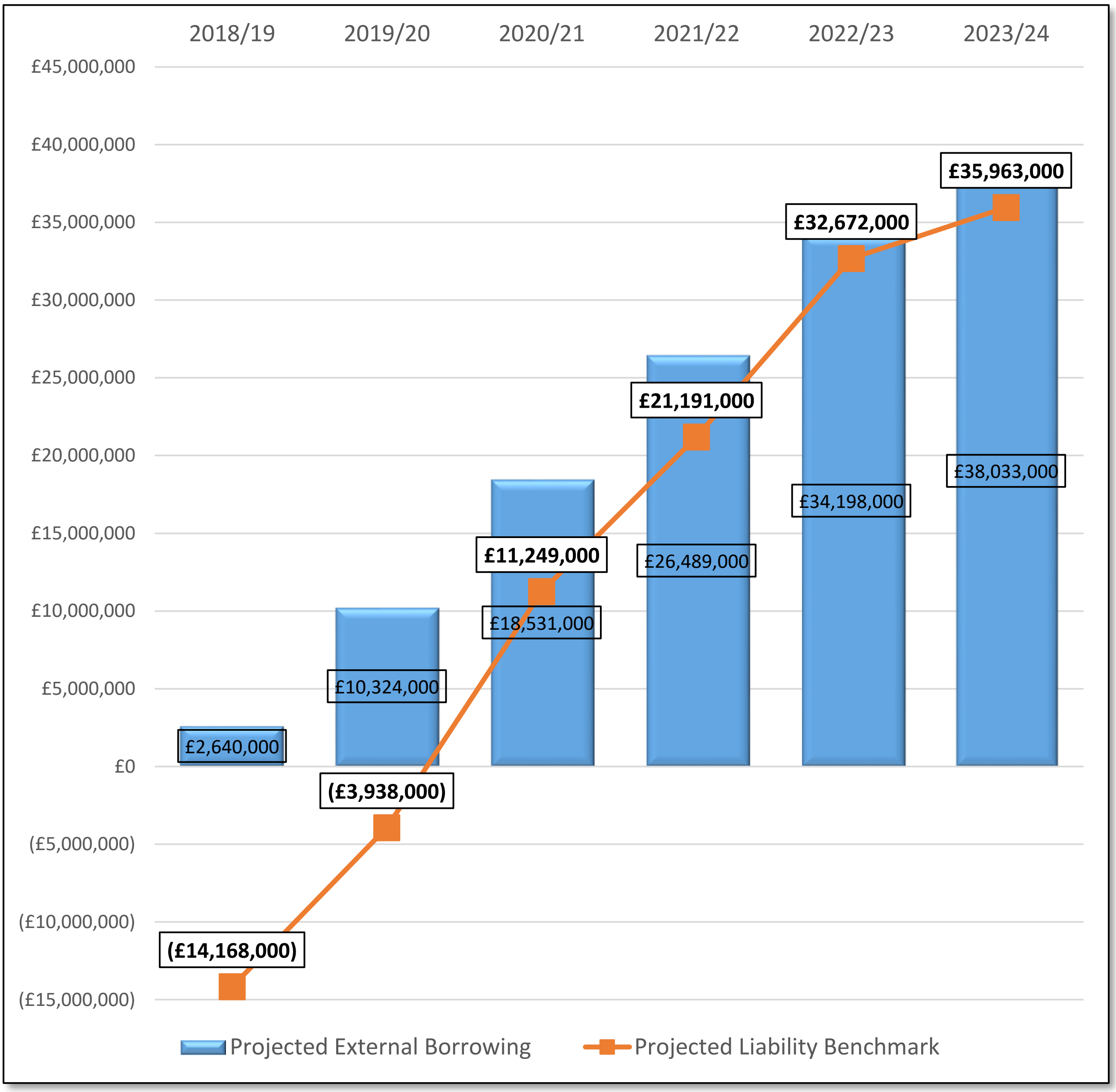



6.3. The projected **Capital Financing Requirement** or borrowing need (the total for each column), **external debt** (finance leases and external borrowing) and **internal borrowing** is shown below:



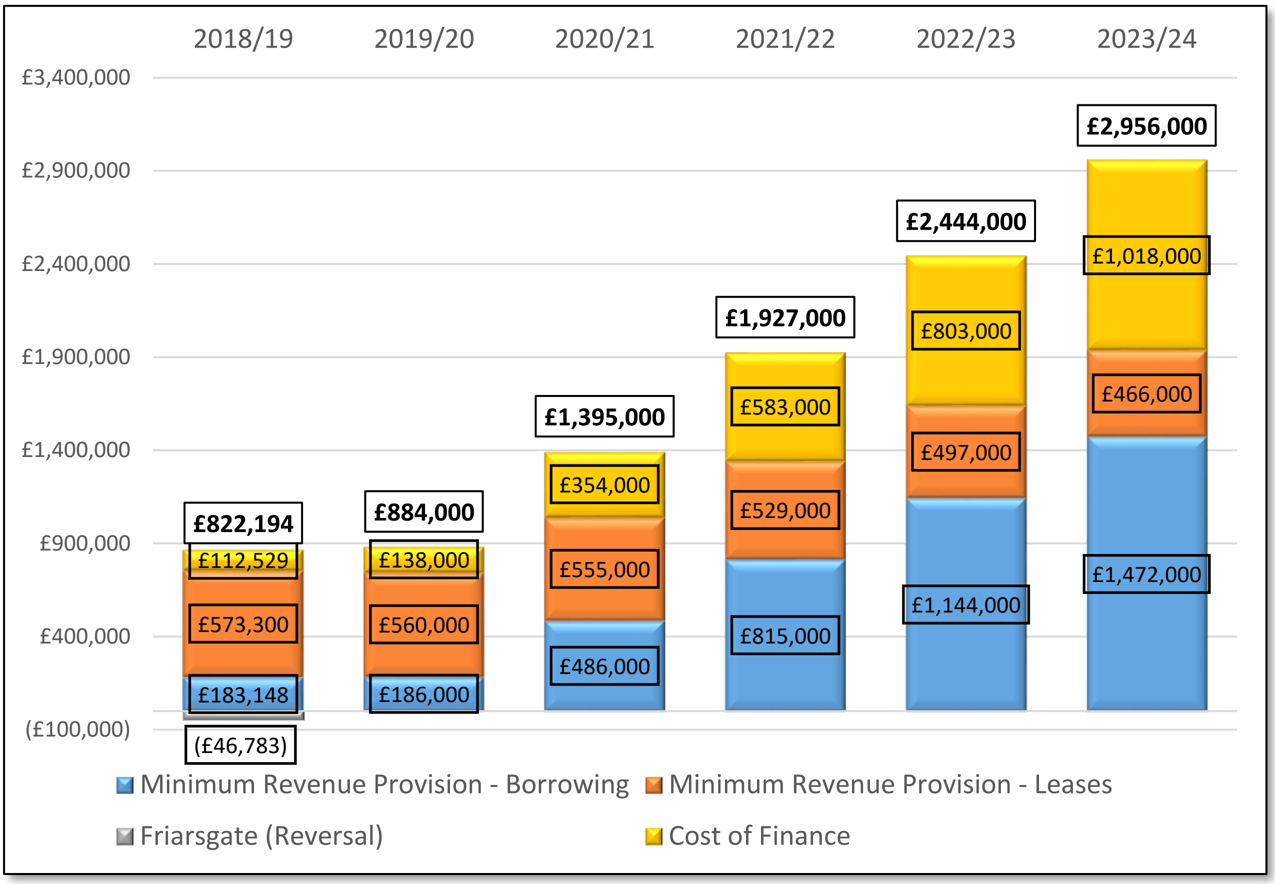
6.4. The **liability benchmark** is the lowest risk level of external borrowing by keeping cash and investment balances to a minimum level of **£10m** at each year end to maintain liquidity but minimise credit risk.

6.5. The projected level of external borrowing, together with the projected liability benchmark in the Medium Term Financial Strategy, is shown in the chart below:

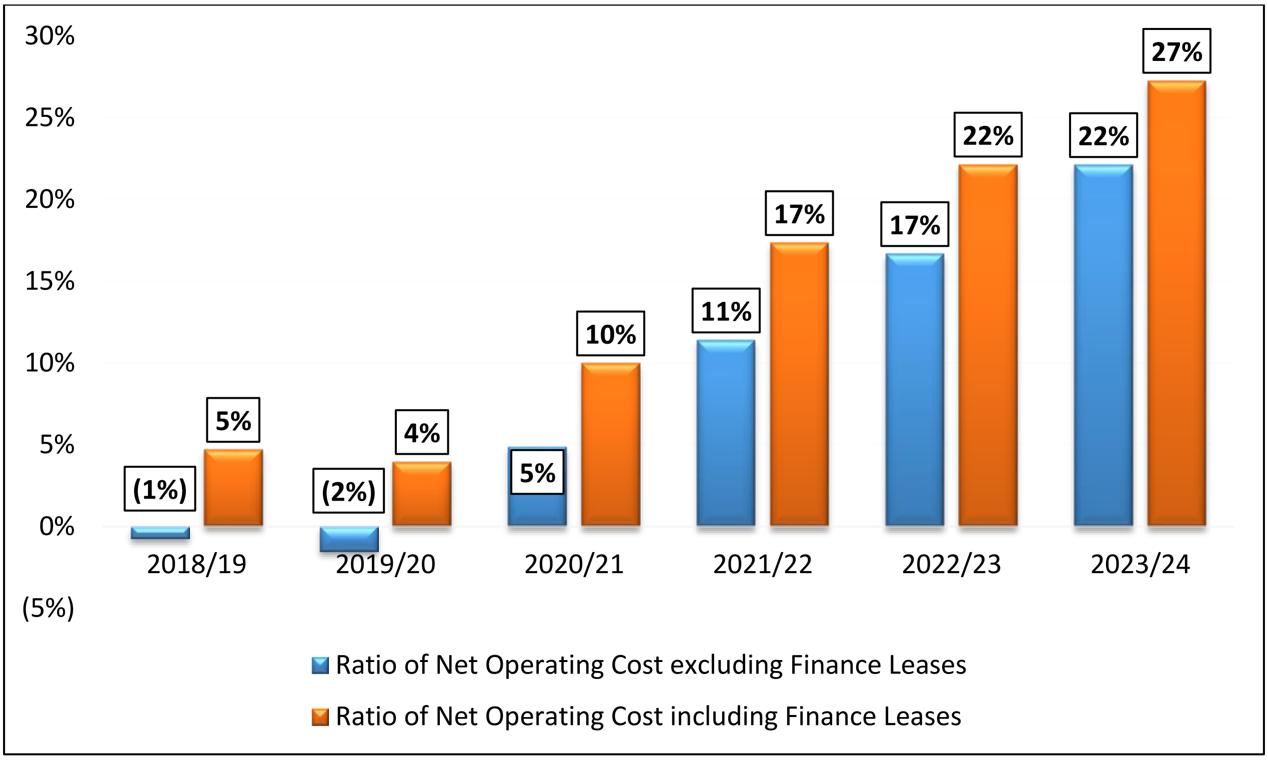



6.6. The chart above indicates that based on current Balance Sheet projections and funding **£11m** of Investment in Property though Internal Borrowing, the Council's projected External Borrowing from 2022/23 will be closer to the liability benchmark.

6.7. The level of debt determines the cost of debt servicing (Minimum Revenue Provision which is similar to depreciation with asset cost divided by assessed asset life plus the cost of finance):




6.8. The proportion of the net budget allocated to financing costs (net of investment income) is below:



## 7. Financial Guarantees

7.1. In addition, to the debt projections shown above in relation to external borrowing and finance leases, the Council also acts as a guarantor for an admitted body that delivers services on behalf of the Council.

7.2. In the event that it is probable that these guarantees will be required a financial provision would be created to mitigate the risk. The guarantees identified in the Statement of Accounts under the Contingent Liabilities note are:

- **The Lichfield Garrick** – the guarantee relates to the pensions of transferred employees and at 31 March 2019 the risk of default was assessed as less than **1%** and therefore the financial risk to the Council is **£4,250.**
- **Freedom Leisure -** the guarantee relates to the pensions of transferred employees and at 31 March 2019 the risk of default was assessed as less than **1%** and therefore the financial risk to the Council is **£85,750.** Freedom Leisure have been admitted to the Pension Fund using a 'pass through' agreement where the Council bears all market related risks such as investment returns. The Pension Fund actuary assessed a market related bond to manage these risks to be **£677,000**. The Council agreed to the creation of an earmarked reserve, projected to total **£267,080** (£33,390 at 31 March 2019) at the end of the ten year contract period, from the leisure outsourcing savings with any additional sum to be provided by General Reserves.

7.3. These guarantees are assessed throughout the year, in terms of the financial viability of the organisations for which the guarantee is provided, to determine whether a financial provision will need to be created.

## 8. The Authority's Risk Appetite, Knowledge and Skills

8.1. The Council's risk appetite along with the majority of Local Government is increasing due to the need to offset funding reductions from Central Government with income from alternative and commercial sources.

8.2. The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Head of Finance and Procurement is a qualified accountant with 30 years' experience, the Council has recruited a new Estates Team to optimise the management of existing property and support the future investment in land and property. The Council pays for junior staff to study towards relevant professional qualifications including CIPFA and the Association of Accounting Technicians.

8.3. 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 and has access to property professionals through the PSP joint venture. 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.

8.4. The Council does not plan to utilise the flexible use of capital receipts for transformation projects.

## 9. Prudential and Local Indicators

9.1. The Prudential and Local Indicators in relation to the Capital Strategy are shown below:

| Prudential Indicators | | | | | | | |
|---|---|---|---|---|---|---|---|
| Indicators | 2018/19 Actual | 2019/20 Original | 2019/20 Revised | 2020/21 Original | 2021/22 Original | 2022/23 Original | 2023/24 Original |
| **Capital Investment** | | | | | | | |
| Capital Expenditure (£m) | £4.910 | £11.618 | £15.659 | £17.751 | £13.636 | £18.821 | £4.051 |
| Capital Financing Requirement (£m) | £4.987 | £10.301 | £14.809 | £25.432 | £35.777 | £51.245 | £51.567 |
| **Gross Debt and the Capital Financing Requirement** | | | | | | | |
| Gross Debt | (£4.315) | (£9.598) | (£11.439) | (£19.091) | (£26.520) | (£36.993) | (£40.362) |
| Borrowing in Advance - Gross Debt in excess of the Capital Financing Requirement | No | No | No | No | No | No | No |
| **Total Debt** | | | | | | | |
| Authorised Limit (£m) | £3.991 | £21.598 | £23.473 | £31.906 | £40.515 | £48.379 | £51.933 |
| Operational Boundary (£m) | £3.991 | £13.006 | £14.881 | £23.088 | £31.046 | £38.755 | £42.590 |
| Proportion of Financing Costs to Net Revenue Stream (%) | 5% | 6% | 4% | 10% | 17% | 22% | 27% |

| Local Indicators | | | | | | | |
|---|---|---|---|---|---|---|---|
| Indicators | 2018/19 Actual | 2019/20 Original | 2019/20 Revised | 2020/21 Original | 2021/22 Original | 2022/23 Original | 2023/24 Original |
| Replacement of Debt Finance or MRP (£m) | (£0.709) | (£0.720) | (£0.746) | (£1.041) | (£1.344) | (£1.641) | (£1.938) |
| Capital Receipts (£m) | (£0.760) | (£1.056) | (£0.855) | (£0.537) | (£0.010) | (£0.010) | (£0.011) |
| Liability Benchmark (£m) | £14.168 | £5.017 | £3.938 | (£11.249) | (£21.191) | (£32.672) | (£35.963) |
| Treasury Management Investments (£m) | £26.876 | £23.689 | £23.749 | £16.769 | £14.785 | £11.013 | £11.557 |

## 10. Chief Finance Officer Assessment of the Capital Strategy

10.1. The key risks associated with the Capital Strategy are principally related to the Investment in Property and its funding given this is planned to be funded through borrowing. I have assessed the current overall risk as **81** out of **144** based on the following factors:

| | Likelihood | Impact | 2020/21 | 2019/20 |
|---|---|---|---|---|
| **Minimum** | | | 0 | 0 |
| **Capital Strategy** | | | | |
| Slippage Occurs in the Capital Spend | 4 | 2 | 8 | 8 |
| Planned Capital Receipts are not received | 3 | 4 | 12 | 12 |
| Actual Cash flows differ from planned Cash flows | 2 | 2 | 4 | 4 |
| **Investment in Property** | | | | |
| Slippage Occurs in the Capital Spend | 4 | 2 | 8 | 8 |
| Change of Government policy including regulatory change | 3 | 4 | 12 | 8 |
| The form of exit from the EU adversely impacts on the UK economy including the Property Market and Borrowing Costs | 3 | 4 | 12 | 12 |
| There is a cyclical 'downturn' in the wider markets | 3 | 3 | 9 | 9 |
| Insufficient expertise to Invest in Property | 1 | 4 | 4 | 12 |
| Inability to acquire or dispose of assets due to good opportunities not being identified | 3 | 4 | 12 | 12 |
| **Assessed Level of Risk** | | | 81 | 85 |
| **Maximum** | | | 144 | 144 |

**APPENDIX B**

## Capital Programme

| Project | Capital Programme (R=>500k, A=250k to 500k and G=<250k) | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | 2019/20 £000 | 2020/21 £000 | 2021/22 £000 | 2022/23 £000 | 2023/24 £000 | TOTAL £000 | Corporate |
| Leisure Review: Capital Investment | A | 30 | 0 | 0 | 0 | 0 | 30 | 0 |
| Play Equipment at Hill Ridware Village Hall | R | 30 | 0 | 0 | 0 | 0 | 30 | 0 |
| New Build Parish Office/Community Hub | R | 0 | 92 | 0 | 0 | 0 | 92 | 0 |
| Fradley Village Heating & CCTV | R | 5 | 0 | 0 | 0 | 0 | 5 | 0 |
| Fradley Youth & Community Centre Cladding | R | 15 | 0 | 0 | 0 | 0 | 15 | 0 |
| Armitage with Handsacre Village Hall heating | R | 5 | 0 | 0 | 0 | 0 | 5 | 0 |
| Armitage with Handsacre Village Hall storage | R | 0 | 6 | 0 | 0 | 0 | 6 | 0 |
| Improvement of Armitage War Memorial | R | 0 | 120 | 0 | 0 | 0 | 120 | 0 |
| Replacement of canopy and artificial grass | R | 13 | 0 | 0 | 0 | 0 | 13 | 0 |
| Burntwood LC CHP Unit | A | 235 | 0 | 0 | 0 | 0 | 235 | 0 |
| Westgate Practice Refurbishment | R | 120 | 0 | 0 | 0 | 0 | 120 | 0 |
| King Edwards VI School | R | 101 | 0 | 0 | 0 | 0 | 101 | 0 |
| Friary Grange - Short Term Refurbishment | R | 174 | 521 | 0 | 0 | 0 | 695 | 0 |
| Replacement Leisure Centre | A | 38 | 164 | 189 | 2,349 | 2,260 | 5,000 | 0 |
| St. Stephen's School, Fradley | R | 22 | 0 | 0 | 0 | 0 | 22 | 0 |
| Accessible Homes (Disabled Facilities Grants) | R | 1,200 | 1,698 | 950 | 950 | 950 | 5,748 | 396 |
| Home Repair Assistance Grants | R | 28 | 15 | 15 | 15 | 15 | 88 | 0 |
| Decent Homes Standard | R | 0 | 172 | 0 | 0 | 0 | 172 | 0 |
| Energy Insulation Programme | R | 38 | 10 | 10 | 10 | 10 | 78 | 0 |
| DCLG Monies | R | 0 | 212 | 0 | 0 | 0 | 212 | 0 |
| Unallocated S106 Affordable Housing Monies | A | 270 | 414 | 0 | 0 | 0 | 684 | 0 |
| **Enabling People Total** | | **2,324** | **3,424** | **1,164** | **3,324** | **3,235** | **13,471** | **396** |
| Darnford Park (S106) | A | 0 | 13 | 0 | 0 | 0 | 13 | 0 |
| Canal Towpath (Brereton & Ravenhill) | R | 211 | 0 | 0 | 0 | 0 | 211 | 0 |
| Loan to Council Dev Co. | A | 0 | 675 | 0 | 0 | 0 | 675 | 116 |
| Lichfield St Johns Community Link (CIL) | R | 0 | 35 | 0 | 0 | 0 | 35 | 0 |
| Staffordshire Countryside Explorer (CIL) | R | 0 | 44 | 0 | 0 | 0 | 44 | 0 |
| Equity in Council Dev Co. | A | 225 | 0 | 0 | 0 | 0 | 225 | 0 |
| Vehicle Replacement Programme (Waste) | A | 0 | 0 | 0 | 3,190 | 75 | 3,265 | 75 |
| Vehicle Replacement Programme (Other) | A | 146 | 56 | 327 | 142 | 202 | 873 | 57 |
| Bin Purchase | A | 150 | 150 | 150 | 150 | 150 | 750 | 0 |
| Shortbutts Park, Lichfield | A | 23 | 0 | 0 | 0 | 0 | 23 | 20 |
| Env. Improvements - Upper St John St | R | 7 | 0 | 0 | 0 | 0 | 7 | 0 |
| Stowe Pool Improvements | A | 0 | 50 | 0 | 0 | 0 | 50 | 5 |
| The Leomansley Area Improvement Project | R | 3 | 0 | 0 | 0 | 0 | 3 | 0 |
| Cannock Chase SAC | R | 44 | 22 | 25 | 0 | 0 | 91 | 0 |
| **Shaping Place Total** | | **809** | **1,045** | **502** | **3,482** | **427** | **6,265** | **273** |
| Multi Storey Car Park Refurbishment Project | A | 300 | 0 | 0 | 0 | 0 | 300 | 0 |
| Birmingham Road Site - Coach Park | A | 861 | 625 | 0 | 0 | 0 | 1,486 | 418 |
| Birmingham Road Site - Short Term Use | A | 473 | 0 | 0 | 0 | 0 | 473 | 0 |
| Car Parks Variable Message Signing | A | 32 | 0 | 0 | 0 | 0 | 32 | 0 |
| Old Mining College - Refurbish access | R | 13 | 0 | 0 | 0 | 0 | 13 | 0 |
| Erasmus Darwin Lunar Legacy (Lichfield Art) | R | 3 | 0 | 0 | 0 | 0 | 3 | 3 |
| St. Chads Sculpture (Lichfield City Art Fund) | R | 50 | 0 | 0 | 0 | 0 | 50 | 50 |
| **Developing Prosperity Total** | | **1,732** | **625** | **0** | **0** | **0** | **2,357** | **471** |
| Investment in Property | A | 10,500 | 11,500 | 11,500 | 11,500 | 0 | 45,000 | 0 |
| Property Planned Maintenance | A | 104 | 125 | 150 | 180 | 215 | 774 | 774 |
| Depot Sinking Fund | A | 0 | 11 | 0 | 0 | 0 | 11 | 11 |

## APPENDIX B

| Project | | 2019/20 £000 | 2020/21 £000 | 2021/22 £000 | 2022/23 £000 | 2023/24 £000 | TOTAL £000 | Corporate |
|---|---|---|---|---|---|---|---|---|
| | | Capital Programme (R=>500k, A=250k to 500k and G=<250k) | | | | | | |
| New Financial Information System | A | 0 | 250 | 0 | 0 | 0 | 250 | 250 |
| IT Infrastructure | A | 105 | 55 | 35 | 15 | 0 | 210 | 210 |
| IT Cloud | A | 25 | 100 | 0 | 0 | 0 | 125 | 125 |
| IT Innovation | A | 60 | 250 | 50 | 50 | 0 | 410 | 305 |
| IT Hardware | A | 0 | 202 | 161 | 160 | 174 | 697 | 697 |
| District Council House Repair Programme | A | 0 | 164 | 74 | 110 | 0 | 348 | 310 |
| **A Good Council Total** | | **10,794** | **12,657** | **11,970** | **12,015** | **389** | **47,825** | **2,682** |
| **Capital Programme** | | **15,659** | **17,751** | **13,636** | **18,821** | **4,051** | **69,918** | **3,822** |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Non-Current Assets** | **A** | **13,577** | **14,804** | **12,636** | **17,846** | **3,076** | **61,939** | **3,373** |
| **Revenue Expenditure Funded by Capital Under Statute** | **R** | **2,082** | **2,947** | **1,000** | **975** | **975** | **7,979** | **449** |

| Funding Source | 2019/20 £000 | 2020/21 £000 | 2021/22 £000 | 2022/23 £000 | 2023/24 £000 | Total £000 |
|---|---|---|---|---|---|---|
| | Capital Programme | | | | | |
| Capital Receipts | 547 | 1,402 | 514 | 559 | 352 | 3,374 |
| Capital Receipts - Statue | 53 | 0 | 0 | 0 | 0 | 53 |
| Revenue - Corporate | 0 | 182 | 0 | 0 | 213 | 395 |
| **Corporate Council Funding** | **600** | **1,584** | **514** | **559** | **565** | **3,822** |
| Grant | 1,266 | 2,343 | 931 | 931 | 931 | 6,402 |
| Section 106 | 673 | 865 | 25 | 0 | 0 | 1,563 |
| CIL | 221 | 79 | 0 | 0 | 0 | 300 |
| Reserves | 1,946 | 1,066 | 327 | 72 | 145 | 3,556 |
| Revenue (Joint Waste Service) | 150 | 150 | 150 | 150 | 150 | 750 |
| Sinking Fund | 235 | 0 | 0 | 0 | 0 | 235 |
| Leases | 0 | 0 | 0 | 3,260 | 0 | 3,260 |
| **Total** | **5,091** | **6,087** | **1,947** | **4,972** | **1,791** | **19,888** |
| **Borrowing Need** | **10,568** | **11,664** | **11,689** | **13,849** | **2,260** | **50,030** |
| **Funding Total** | **15,659** | **17,751** | **13,636** | **18,821** | **4,051** | **69,918** |

## APPENDIX B

### Reconciliation of Original Capital Programme to this Capital Programme

| | Cabinet or Decision Date | 2019/20 £000 | 2020/21 £000 | 2021/22 £000 | 2022/23 £000 | 2023/24 £000 | Total £000 |
|---|---|---|---|---|---|---|---|
| **Original Budget Council 19/02/2019** | | **11,618** | **14,909** | **14,466** | **17,250** | **0** | **58,243** |
| **Approved Changes** | | | | | | | |
| Allocation of Community Infrastructure Levy | 12/03/2019 | 255 | 45 | | | | 300 |
| Multi Storey Car Park Refurbishment | 12/03/2019 | 300 | | | | | 300 |
| Slippage from 2018/19 | 13/06/2019 | 819 | | | | | 819 |
| Quarter 1 Money Matters | 10/09/2019 | (805) | 333 | | | | (472) |
| Birmingham Road Enabling Works | 10/09/2019 | 120 | | | | | 120 |
| St. Stephen's School (S106) | 24/10/2019 | 22 | | | | | 22 |
| Quarter 2 Money Matters | 03/12/2019 | (1,664) | 1,664 | | | | 0 |
| 8 Months Money Matters | 11/02/2020 | 4,183 | (1,109) | (1,500) | (1,500) | | 74 |
| **Friary Grange Leisure Centre** | | | | | | | |
| Replacement Facility | 07/10/2019 | 38 | 164 | 189 | 2,349 | 2,260 | 5,000 |
| Short Term Refurbishment | 07/10/2019 | 174 | 521 | | | | 695 |
| **Capital Bids Received - 21/11/2019** | | | | | | | |
| Vehicle Replacement Programme (score 80) | Medium Term Financial Strategy | (280) | (103) | 20 | 232 | 277 | 146 |
| Property Planned Maintenance (score 72) | | 104 | 125 | 150 | 180 | 215 | 774 |
| Disabled Facilities Grants (score 68) | | | | | | 950 | 950 |
| New Financial Information System (score 65) | | | 250 | | | | 250 |
| ICT Hardware (score 59) | | | 202 | 161 | 160 | 174 | 697 |
| Coach Park - Acquisition (score 55) | | 50 | | | | | 50 |
| Coach Park - Works (score 55) | | 575 | 625 | | | | 1,200 |
| **Capital Bids fully funded by Revenue or External** | | | | | | | |
| Joint Waste Service Bin Purchase (score 84) | | 150 | 150 | 150 | 150 | 150 | 750 |
| Energy Insulation Programme (score 68) | | | (10) | | | 10 | 0 |
| Home Repair Assistance Grants (score 60) | | | (15) | | | 15 | 0 |
| **Capital Programme** | | **15,659** | **17,751** | **13,636** | **18,821** | **4,051** | **69,918** |

# Minimum Revenue Provision Statement 2020/21

Where the Authority 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 this Authority to have regard to the Ministry of Housing, Communities and Local Government's (MGCLG) guidance on MRP most recently issued in 2018.

The broad aim of the MHCLG Guidance is to ensure that debt is repaid over the period that is reasonably commensurate with that over which the capital expenditure provides benefits.

The MHCLG Guidance requires the Authority to approve an annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP.

- For capital expenditure incurred after 1 April 2008 where no financial support is provided by the Government through the Finance Settlement, MRP will be determined by charging the expenditure over the expected useful life of the relevant asset in equal instalments. MRP on purchases of **freehold land** will be charged over a maximum of **50 years**. MRP on expenditure not related to assets but that has been **capitalised by regulation or direction** (Revenue Expenditure Funded by Capital under Statute or REFCUS) will be charged over a maximum of **20 years**.
- For assets acquired by **finance leases**, MRP will be determined as being equal to the **element of the charge that is used to reduce the Balance Sheet liability**.
- For **capital expenditure loans to third parties that are repaid** in annual or more frequent instalments of principal, the Council will make **nil MRP**, but instead apply the capital receipts arising to reduce the Capital Financing Requirement or Borrowing Need. In years where there is no principal repayment, MRP will be charged in accordance with the MRP policy for the assets funded by the loan, including where appropriate delaying the MRP until the year after the assets become operational.

# Treasury Management

## Introduction

Treasury management is the management of the Authority's cash flows, borrowing and investments, and the associated risks. The Authority has invested and is planning to borrow 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 risks are therefore central to the Authority's prudent financial management.

Treasury risk management at the Authority 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 Authority to approve a treasury management strategy before the start of each financial year. This report fulfils the Authority's legal obligation under the *Local Government Act 2003* to have regard to the CIPFA Code.

Investments held for service purposes or for commercial profit are considered in a different report, the Investment Strategy.

As part of the MTFS, we prepare integrated Revenue Budgets and a Capital Programme. These budgets, together with the actual Balance Sheet from the previous financial year, are used to also prepare Balance Sheet projections. These Balance Sheet Projections are shown on the next page.

These Balance Sheet projections are significant in assessing the Council's Treasury Management Position in terms of borrowing requirement (including comparison to a **Liability Benchmark** explained below), investment levels and our Investment Policy and Strategy.

**A Liability benchmark** compares 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 used in the Balance Sheet projections, but that cash and investment balances are kept to a minimum level (**£10m**) to maintain sufficient liquidity but minimise credit risk through the use of Internal Borrowing.

CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Authority's total debt should be lower than its highest forecast Capital Financing Requirement (CFR) or Borrowing Need over the next three years. The table shows that the Authority expects to comply with this recommendation.

| | **2018/19 £000** | **2019/20 £000** | **2020/21 £000** | **2021/22 £000** | **2022/23 £000** | **2023/24 £000** |
|---|---|---|---|---|---|---|
| Capital Financing Requirement (Borrowing) | £3,312 | £13,694 | £24,872 | £35,746 | £48,451 | £49,238 |
| Capital Financing Requirement (Finance Leases) | £1,675 | £1,115 | £560 | £31 | £2,794 | £2,329 |
| **Total** | **£4,987** | **£14,809** | **£25,432** | **£35,777** | **£51,245** | **£51,567** |

| | | | | | | |
|---|---|---|---|---|---|---|
| External Borrowing | (£2,640) | (£10,324) | (£18,531) | (£26,489) | (£34,198) | (£38,033) |
| Finance Leases | (£1,675) | (£1,115) | (£560) | (£31) | (£2,794) | (£2,329) |
| **Total** | **(£4,315)** | **(£11,439)** | **(£19,091)** | **(£26,520)** | **(£36,993)** | **(£40,362)** |

| | | | | | | |
|---|---|---|---|---|---|---|
| Liability Benchmark | £14,168 | £3,938 | (£11,249) | (£21,191) | (£32,672) | (£35,963) |

# Balance Sheet Projections 2019-24

| | Type | 2018/19 Actual £000s | 2019/20 Budget £000s | 2020/21 Budget £000s | 2021/22 Budget £000s | 2022/23 Budget £000s | 2023/24 Budget £000s | 2019/24 Change £000s |
|---|---|---|---|---|---|---|---|---|
| Non-Current Assets | ASSET | 48,376 | 59,743 | 72,087 | 82,938 | 98,999 | 100,290 | 40,547 |
| Equity Investment in Local Authority Company | ASSET | 0 | 225 | 225 | 225 | 225 | 225 | 0 |
| Long Term Debtors | CRED | 288 | 288 | 288 | 288 | 288 | 288 | 0 |
| Long Term Investment (Company Loan) | LOAN | 0 | 0 | 675 | 675 | 675 | 675 | 675 |
| Investments | INV | 26,808 | 23,681 | 16,701 | 14,717 | 10,945 | 11,489 | (12,192) |
| Borrowing | BOLE | (2,640) | (10,324) | (18,531) | (26,489) | (34,198) | (38,033) | (27,710) |
| Finance Leases | BOLE | (1,675) | (1,115) | (561) | (32) | (2,795) | (2,329) | (1,213) |
| Working Capital | CRED | (8,409) | (8,095) | (7,212) | (7,212) | (7,212) | (7,212) | 883 |
| Pensions | CRED | (42,747) | (44,930) | (43,948) | (46,448) | (49,096) | (48,239) | (3,309) |
| **TOTAL ASSETS LESS LIABILITIES** | | **20,001[2]** | **19,474** | **19,725** | **18,663** | **17,832** | **17,154** | **(2,319)** |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Unusable Reserves | | | | | | | | |
| Revaluation Reserve | REV | (9,419) | (9,419) | (9,419) | (9,419) | (9,419) | (9,419) | 0 |
| Capital Adjustment Account | CAP | (33,970) | (35,741) | (38,137) | (38,643) | (39,236) | (40,205) | (4,464) |
| Deferred Credits | CRED | (47) | (47) | (47) | (47) | (47) | (47) | 0 |
| Pension Scheme | CRED | 43,621 | 44,930 | 46,278 | 47,666 | 49,096 | 50,569 | 5,639 |
| Benefits Payable During Employment Adjustment Account | CRED | 219 | 219 | 219 | 219 | 219 | 219 | 0 |
| Collection Fund | CRED | (315) | 0 | 0 | 0 | 0 | 0 | 0 |
| Available for Sale Financial Instruments Reserve | CRED | 68 | 68 | 68 | 68 | 68 | 68 | 0 |
| Usable Reserves | | | | | | | | |
| Unapplied Grants and Contributions | UGER | (2,220) | (1,817) | (994) | (969) | (944) | (919) | 898 |
| Usable Capital Receipts | UGER | (2,004) | (2,259) | (1,394) | (890) | (341) | 0 | 2,259 |
| Burntwood Leisure Centre Sinking Fund | UGER | (236) | 0 | 0 | 0 | 0 | 0 | 0 |
| Earmarked Reserves - Unrestricted | UGER | (6,591) | (5,321) | (4,352) | (4,082) | (4,175) | (4,191) | 1,130 |
| Earmarked Reserves - Restricted | UGER | (3,798) | (3,663) | (3,891) | (4,099) | (4,306) | (4,483) | (819) |
| General Fund Balance | GEN | (5,310) | (6,423) | (8,056) | (8,467) | (8,747) | (8,747) | (2,324) |
| **TOTAL EQUITY** | | **(20,001)** | **(19,474)** | **(19,725)** | **(18,663)** | **(17,832)** | **(17,154)** | **2,319** |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| **Reserves Available to cover Investment Losses** | **(11,901)** | **(11,744)** | **(12,408)** | **(12,549)** | **(12,922)** | **(12,938)** | **(1,194)** |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Summary** | | | | | | | | |
| Capital Funding | CAP | (33,970) | (35,741) | (38,137) | (38,643) | (39,236) | (40,205) | (4,464) |
| Revaluation Reserve | REV | (9,419) | (9,419) | (9,419) | (9,419) | (9,419) | (9,419) | 0 |
| Borrowing and Leasing | BOLE | (4,315) | (11,439) | (19,091) | (26,520) | (36,993) | (40,362) | (28,923) |
| Non-Current Assets | ASSET | 48,376 | 59,968 | 72,312 | 83,163 | 99,224 | 100,515 | 40,547 |
| Investments | INV | 26,876 | 23,749 | 16,769 | 14,785 | 11,013 | 11,557 | (12,192) |
| Unapplied Grants & Earmarked Reserves | UGER | (14,848) | (13,060) | (10,630) | (10,039) | (9,766) | (9,592) | 3,468 |
| General Reserve | GEN | (5,310) | (6,423) | (8,056) | (8,467) | (8,747) | (8,747) | (2,324) |
| Long Term Debtors | DEBT | 288 | 288 | 288 | 288 | 288 | 288 | 0 |
| Long Term Investment (Company Loan) | LOAN | 0 | 0 | 675 | 675 | 675 | 675 | 675 |
| Working Capital & Pensions | CRED | (7,678) | (7,923) | (4,710) | (5,822) | (7,040) | (4,710) | 3,213 |
| **Total** | | **0** | **0** | **0** | **0** | **0** | **0** | **0** |
| **Internal Borrowing** | | **672** | **3,369** | **6,339** | **9,255** | **14,251** | **11,204** | **7,835** |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| **Liability Benchmark** | | | | | | | |
| Capital Financing Requirement (Borrowing) | 3,312 | 13,468 | 24,645 | 35,519 | 48,224 | 49,012 | 35,545 |
| Working Capital | (7,322) | (7,923) | (4,710) | (5,822) | (7,040) | (4,710) | 3,213 |
| Usable Reserves | (20,158) | (19,483) | (18,686) | (18,506) | (18,513) | (18,339) | 1,144 |
| Minimum Level of Investments | 10,000 | 10,000 | 10,000 | 10,000 | 10,000 | 10,000 | 0 |
| **Total** | **(14,168)** | **(3,938)** | **11,249** | **21,191** | **32,672** | **35,963** | **39,902** |

[2] The Mid Year Treasury Management Report to Committee on 14 November 2019 showed Total Assets less Liabilities and Total Equity of £21.350m which was the figure prior to Statement of Accounts External Audit adjustments related to Pension valuations of £1.349m

**Borrowing Strategy**

The Authority currently projects **£10.324 million** of loans at 31 March 2020, an increase of **£7.684 million** on the previous year, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast above and the Capital Programme shows that the Authority expects to borrow up to **£11.664 million** in 2020/21.

**Objectives:** The Authority'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 Authority's long-term plans change, is a secondary objective.

**Strategy:** Given the significant cuts to public expenditure and in particular to local government funding, the Authority'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 is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal 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 Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority 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.

The Authority 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 Authority will now look to borrow any long-term loans from other sources including banks, pensions and local authorities, and will 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.

Alternatively, the Authority may arrange forward starting loans during 2019/20, 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.

In addition, the Authority may borrow short-term loans to cover unplanned cash flow shortages.

**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 bank or building society authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds (except Staffordshire 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

**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 other debt liabilities:

- leasing
- hire purchase
- sale and leaseback

The Authority has previously raised all of its long-term borrowing from the Public Works Loans Board (PWLB) but it continues to investigate other sources of finance, such as local authority loans and bank loans that may be available at more favourable rates.

**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 full Council.

**Short-term and variable rate loans**: These loans leave the Authority 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.

**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 Authority 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**

The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In 2020/21, the Authority's investment balance is projected to range between **£21.69 million** and **£36.39 million**.

**Objectives:** The CIPFA Code requires the Authority 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 Authority'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 Authority 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.

**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 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.

**Strategy:** Given the increasing risk and very low returns from short-term unsecured bank investments, the Authority aims to further diversify into more secure and/or higher yielding asset classes during 2020/21. This is especially the case for the estimated **£12 million** that is available for longer-term investment. The majority of the Authority's surplus cash is currently invested in short-term unsecured bank deposits, certificates of deposit and money market funds. This diversification will represent a continuation of the new strategy adopted in the last few years.

**Business models:** Under the new IFRS 9 standard, the accounting for certain investments depends on the Authority's "business model" for managing them. The Authority aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

**APPENDIX D**

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

Approved investment counterparties and limits

| Credit rating | Banks unsecured | Banks secured | Government | Corporates | Registered Providers |
|---|---|---|---|---|---|
| UK Govt | n/a | n/a | £ Unlimited<br>50 years | n/a | n/a |
| AAA | £1m<br>5 years | £1m<br>20 years | £2m<br>50 years | £1m<br>20 years | £1m<br>20 years |
| AA+ | £1m<br>5 years | £1m<br>10 years | £2m<br>25 years | £1m<br>10 years | £1m<br>10 years |
| AA | £1m<br>4 years | £1m<br>5 years | £2m<br>15 years | £1m<br>5 years | £1m<br>10 years |
| AA- | £1m<br>3 years | £1m<br>4 years | £2m<br>10 years | £1m<br>4 years | £1m<br>10 years |
| A+ | £1m<br>2 years | £1m<br>3 years | £2m<br>5 years | £1m<br>3 years | £1m<br>5 years |
| A | £1m<br>13 months | £1m<br>2 years | £2m<br>5 years | £1m<br>2 years | £1m<br>5 years |
| A- | £1m<br>6 months | £1m<br>13 months | £2m<br>5 years | £1m<br>13 months | £1m<br>5 years |
| None | £0.5m<br>6 months | n/a | £2m<br>25 years | £50,000<br>5 years | £0.5m<br>5 years |
| **Pooled funds and real estate investment trusts** | £4m per fund (previously £2m)<br>Arlingclose recommendation is 10% of maximum investments for the year projected to be £36m plus internal borrowing of £6.3m = £42.3m. | | | | |
| **UK Domiciled Pooled Funds** | £5m per fund | | | | |

This table must be read in conjunction with the notes below

**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.

**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.

**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.

**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 be made in unlimited amounts for up to 50 years.

**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 **£250,000** per company as part of a diversified pool in order to spread the risk widely.

**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.

**Pooled funds:** Shares or units in diversified investment vehicles consisting of 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.

Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Authority 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 Authority's investment objectives will be monitored regularly.

**Real estate investment trusts (REIT):** Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties. Investments in REIT shares cannot be withdrawn but can be sold on the stock market to another investor.

**Operational bank accounts:** The Authority 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 **£500,000** per bank. 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 Authority maintaining operational continuity.

**Risk assessment and credit ratings**: Credit ratings are obtained and monitored by the Authority'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 existing investments with the counterparty.

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 on the next working day 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.

**Other information on the security of investments**: The Authority 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 Authority'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.

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 Authority 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 Authority'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.

**Investment limits**: The Authority's revenue reserves available to cover investment losses are forecast to be **£11.218 million** on 31st March 2020. In order that no more than **10%** of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government, other Local Authorities and Pooled Funds) will be **£1 million**. 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.

Investment limits

| | Approved Cash limit | Recommended Cash Limit | Rationale for the Recommended Change |
|---|---|---|---|
| Any single organisation, except Pooled Funds, UK Central Government and UK Local Authorities | £1m each | £1m each | To reflect recommended increases in pooled fund limits. |
| UK Domiciled Pooled Funds | £5m each | £5m each | |
| UK Central Government | unlimited | unlimited | |
| UK Local Authorities | £2m each | £2m each | |
| Any group of organisations under the same ownership | £1m per group | £1m per group | |
| Any group of pooled funds under the same management | £9m per manager | £11m per manager | This needs to reflect the potential total investments with CCLA, Arlingclose recommendation is 25% of maximum investments for the year projected to be £36m plus internal borrowing of £6.3m = £42.3m. |
| Negotiable instruments held in a broker's nominee account | £12m per broker | £12m per broker | |
| Foreign countries | £2m per country | £2m per country | |
| Registered providers and registered social landlords | £5m in total | £5m in total | |
| Unsecured investments with building societies | £2m in total | £2m in total | |
| Loans to unrated corporates (excluding the Council's Company) | £2m in total | £2m in total | |
| Money market funds | £12m in total | £21m in total | Arlingclose recommendation is 50% of maximum investments for the year projected to be £36m plus internal borrowing of £6.3m = £42.3m. |
| Real estate investment trusts | £5m in total | £5m in total | |

**Liquidity management**: The Authority uses cash flow forecasting via excel 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 Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the medium-term financial strategy and cash flow forecast.

## Related Matters

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

**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).

The Authority 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 Authority 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.

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.

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

**Markets in Financial Instruments Directive**: The Authority has opted up to **professional client status** with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the Head of Finance and Procurement believes this to be the most appropriate status.

**Other Options Considered**

The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Head of Finance and Procurement, having consulted the Cabinet Member for Finance and Democratic Services, 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) |

# Investment Strategy Report 2020/21

## Introduction

The Authority 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 or buying shares in other organisations (**service investments**), and
- to earn investment income (known as **commercial investments** where this is the main purpose).

This investment strategy is a new report, meeting 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

The Authority 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 **£21.69 million** and **£36.39 million** during the 2020/21 financial year.

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

**Further details:** Full details of the Authority's policies and its plan for 2020/21 for treasury management investments are covered in a separate document in this report, the treasury management strategy.

## Service Investments: Loans

**Contribution:** The Council lends money to its employees for car loans, inherited housing loans from Birmingham City Council, makes loans to individuals to reduce the risk of homelessness and will lend to its subsidiary to support the development of local housing.

**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 Authority, upper limits on the outstanding loans to each category of borrower have been set as follows:

| Category of borrower | 31.3.2019 actual | | | 2019/20 | 2020/21 |
|---|---|---|---|---|---|
| | Balance owing | Loss allowance | Net figure in accounts | Projection | Proposed Limit |
| Subsidiaries | £0 | £0 | £0 | £0 | £675,000 |
| Employees – car loans | £3,927 | £0 | £3,927 | £3,927 | £100,000 |
| Housing Loans - secured | £44,320 | £0 | £44,320 | £44,320 | £45,000 |
| Housing Loans - unsecured | £2,771 | £0 | £2,771 | £2,771 | £3,000 |
| Homelessness Loans | £21,848 | (£18,006) | £3,842 | £3,842 | £50,000 |
| **TOTAL** | **£72,866** | **(£18,006)** | **£54,860** | **£54,860** | **£873,000** |

Accounting standards require the Authority to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Authority's statement of accounts from 2019/20 onwards will be shown net of this loss allowance. However, the Authority makes every reasonable effort to collect the full sum lent including placing charges on properties for housing loans (secured) and has appropriate credit control arrangements in place to recover overdue repayments.

**Risk assessment:** The most significant loan for a service purpose is the **£675,000** loan for **5 years** to the Council Development Company for the provision of housing. The Board of Directors of the Company will initially consist of Council employees and therefore the Council will be able to manage the repayment risk through project due diligence and the monitoring of selected projects.

## Commercial Investments: Property

See the Capital Strategy at **APPENDIX A**.

## Loan Commitments and Financial Guarantees

See the Capital Strategy at **APPENDIX A**.

## Proportionality

See the Capital Strategy at **APPENDIX A**.

## Borrowing in Advance of Need

Government guidance is that local authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed. The Authority has chosen not to follow this guidance and plans to borrow for this purpose to fund the approved Property Investment Strategy. The Authority's policies in investing the money borrowed, including management of the risks, for example, of not achieving the desired profit or borrowing costs will be managed as part of the Authority's overall management of its treasury risks.

## Capacity, Skills and Culture

See the Capital Strategy at **APPENDIX A**.

## Investment Indicators

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

**Total risk exposure:** The first indicator shows the Authority's total exposure to potential investment losses. This includes amounts the Authority is contractually committed to lend but have yet to be drawn down and guarantees the Authority has issued over third party loans.

| Total Investment Exposure | 31/03/2019 Actual £000 | 31/03/2020 Forecast £000 | 31/03/2021 Forecast £000 | 31/03/2022 Forecast £000 | 31/03/2023 Forecast £000 | 31/03/2024 Forecast £000 |
|---|---|---|---|---|---|---|
| Treasury Management Investments | £26,876 | £23,749 | £16,769 | £14,785 | £11,013 | £11,557 |
| Commercial Investments: Property | £4,867 | £15,367 | £26,867 | £38,367 | £49,867 | £49,867 |
| **TOTAL INVESTMENTS** | **£31,743** | **£39,116** | **£43,636** | **£53,152** | **£60,880** | **£61,424** |
| Commitments to Lend | £0 | £0 | £675 | £675 | £675 | £675 |
| **TOTAL EXPOSURE** | **£31,743** | **£39,116** | **£44,311** | **£53,827** | **£61,555** | **£62,099** |

**How investments are funded:** Government guidance is that these indicators should include how investments are funded. Since the Authority 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 Authority's investments are funded by usable reserves and income received in advance of expenditure.

Investments funded by borrowing

| Investments Funded by Borrowing (cumulative at year-end) | 31/03/2019 Actual £000 | 31/03/2020 Forecast £000 | 31/03/2021 Forecast £000 | 31/03/2022 Forecast £000 | 31/03/2023 Forecast £000 | 31/03/2024 Forecast £000 |
|---|---|---|---|---|---|---|
| Commercial Investments: Property | £0 | £10,500 | £22,000 | £33,500 | £45,000 | £45,000 |
| **TOTAL FUNDED BY BORROWING** | **£0** | **£10,500** | **£22,000** | **£33,500** | **£45,000** | **£45,000** |

**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.

Investment rate of return (net of all costs)

| Investments Net Rate of Return | 31/03/2019 Actual % | 31/03/2020 Forecast % | 31/03/2021 Forecast % | 31/03/2022 Forecast % | 31/03/2023 Forecast % | 31/03/2024 Forecast % |
|---|---|---|---|---|---|---|
| Treasury Management Investments | 0.90% | 1.08% | 1.27% | 1.43% | 1.64% | 1.97% |
| Commercial Investments | | | | | | |
| Property (excluding valuation changes) | 8.30% | 8.30% | 8.30% | 8.30% | 8.30% | 8.30% |
| Investment in Property | 0.00% | 0.00% | 1.00% | 1.00% | 1.00% | 1.00% |
| **ALL INVESTMENTS** | **9.20%** | **9.38%** | **10.57%** | **10.73%** | **10.95%** | **11.27%** |

See the Capital Strategy at **APPENDIX A**.