Cambridgeshire County Council

Section 7

Treasury Management Strategy

2022-2023

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Contents

1: Introduction

Background

The Council is required to operate a balanced budget, which broadly means that the cash raised during the year will meet Council expenditure. The treasury management operation must ensure that this cash flow is adequately planned, as well as managed, with cash being available when it is needed. Surplus cash should be invested in low-risk counterparties or instruments in line with the Council's risk appetite, providing adequate liquidity initially, before considering investment return.

Another main function of the treasury management service is the funding of the Council's Capital Strategy. This Strategy provides a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans, or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

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

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

CIPFA Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes

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."

The Council has adopted CIPFA's Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes (the Treasury Code). The adoption is included in the Council's Constitution.

CIPFA Prudential Code for Capital Finance in Local Authorities

The CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code) is a professional code of practice. Local authorities have a statutory requirement to comply with the Prudential Code when making capital investment decisions and carrying out their duties under Part 1 of the Local Government Act 2003 (Capital Finance etc. and Accounts).

The CIPFA Prudential Code sets out the manner in which capital spending plans should be considered and approved, and in conjunction with this, the requirement for an integrated treasury management strategy.

Councils are required to set and monitor a range of prudential indicators for capital finance, covering affordability, prudence, and a range of treasury indicators.

Treasury Management Policy Statement

The Council's Treasury Management Policy Statement is included in Appendix 2 of the Treasury Management Strategy (TMS). The policy statement follows the wording recommended by the latest edition of the CIPFA Treasury Code.

Treasury Management Practices

The Council's Treasury Management Practices (TMPs) set out the manner in which the Council will seek to achieve its treasury management objectives, and how it will manage and control those activities through its policies.

The Council's TMPs Schedules cover the detail of how the Council will apply the TMP Main Principles in carrying out its operational treasury activities.

The Treasury Management Strategy

It is a requirement under the Treasury Code to produce an annual strategy report on proposed treasury management activities for the year. The Council's Treasury Management Strategy is drafted in the context of the key principles of the Treasury Code, as follows:

- Public service organisations should put in place formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of their treasury management activities.
- Their policies and practices should make clear that the effective management and control of risk are prime objectives of their treasury management activities and that responsibility for these lies clearly within their organisations. Their appetite for risk should form part of their annual strategy, including any use of financial instruments for the prudent management of those risks, and should ensure that priority is given to security and liquidity when investing funds.
- They should acknowledge that the pursuit of value for money in treasury management, and the use of suitable performance measures, are valid and important tools for responsible organisations to employ in support of their business and service objectives; and that within the context of effective risk management, their treasury management policies and practices should reflect this.

The purpose of the Treasury Management Strategy is to establish the framework for the effective and efficient management of the Council's treasury management activity, including the Council's investment portfolio, within legislative, regulatory, and best practice regimes. The Strategy needs to balance risk against reward in the best interests of stewardship of the public purse.

The Treasury Management Strategy incorporates:

- The Council's capital financing and borrowing strategy for the coming year
- The Council's policy on the making of the Minimum Revenue Provision (MRP) for the repayment of debt, as required by the Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008.
- The Affordable Borrowing Limit as required by the Local Government Act 2003.
- The Annual Investment Strategy for the coming year as required by the Department of Levelling Up, Housing and Communities (DLUHC) revised Guidance on Local Government Investments (updated 2018).

The Strategy takes into account the impact of the Council's Medium Term Financial Strategy (MTFS), its revenue budget and Capital Programme, the balance sheet position, and the outlook for interest rates.

The Treasury Management Strategy also includes the Council's:

- Policy on borrowing in advance of need
- Counterparty creditworthiness policies

The main changes from the Treasury Management Strategy adopted by Council in February 2021 are:

- Updates to interest rate forecasts
- Updates to debt financing budget forecasts
- Updates to the Council's Annual Investment Strategy in line with best practice guidance

The Council regards the successful identification, monitoring, and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. The Treasury Management Scheme of Delegation is shown in Appendix 1 of the TMS.

2: Current Treasury Management position

The Council's projected treasury portfolio position at 31 March 2022, with forward estimates, is summarised below. The table shows external borrowing (the treasury management operations), against the capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing. The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need.

Any capital expenditure which has not immediately been paid for, will increase the CFR. The CFR does not increase indefinitely, as the Minimum Revenue Provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with each asset's life. This is shown in graphical form in Appendix 1 of the TMS. The CFR and borrowing figures shown in Table 1 below include borrowing undertaken or planned for third party loans and Finance Lease liabilities, but excludes PFI schemes for which a separate borrowing facility forms part of the contracts and so the Council does not need to borrow itself for these.

The Council's projected borrowing need, alongside forecast external borrowing and investment balances, is shown in Tables 1 and 2 below:

Table 1: Forecast Borrowing and Investment Balances

	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m
External borrowing						
Borrowing at 1 April brought forward	811.3	820.0	910.0	990.0	990.0	1,000.0
Net Borrowing Requirement to fund capital programme (see Table 2 below)	30.7	59.8	60.3	10.8	15.4	-34.3
Internal borrowing (increase (-)/reduction)*	-21.9	30.2	19.7	-10.8	-5.4	-10.7
(1) Actual borrowing at 31 March carry forward	**820.0**	**910.0**	**990.0**	**990.0**	**1,000.0**	**955.0**
(2) CFR (ex. PFI) – the borrowing need	946.4	1,006.2	1,066.4	1,077.2	1,092.7	1,058.4
(3) *[2 – 1]* Internal borrowing*	126.4	96.2	76.4	87.2	92.7	103.4
Investments						

	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m
Investments at 1 April	98.1	85.0	85.0	85.0	85.0	85.0
In Year Movements	-13.1	0.0	0.0	0.0	0.0	0.0
(4) Investments at 31 March	**85.0**	**85.0**	**85.0**	**85.0**	**85.0**	**85.0**
(5) *[1 – 4]* Net borrowing	**735.0**	**825.0**	**905.0**	**905.0**	**915.0**	**870.0**

**Internal Borrowing, also referred to as under/over borrowing, is temporarily funding capital spending from cash-backed resources (reserves and cashflow timing surpluses) to hand. This avoids interest payments by deferring the need to borrow externally, reduces investment balances that would otherwise earn a rate of return lower than the cost of additional borrowing (therefore minimising net interest expenses), and consequently less investments reduces the Councils exposure to credit risk. Internal Borrowing is discussed further in Part 4 Borrowing Strategy.*

Table 2: Capital Borrowing Requirement

	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m
Unsupported Borrowing – General Fund	51.8	81.1	84.2	37.3	42.8	21.6
Unsupported Borrowing – Housing*	0.0	0.0	0.0	0.0	0.0	0.0
Less: MRP and other financing movements	-21.2	-21.3	-24.0	-26.5	-27.3	-55.8
Net Borrowing Requirement to fund Capital Programme	**30.7**	**59.8**	**60.3**	**10.8**	**15.4**	**-34.3**

** Loans raised by the Council for the purposes of on-lending to its wholly owned housing development company, This Land, will be classified as capital expenditure and therefore increase the Capital Financing Requirement. However, as these loans will be repaid in full in later years, no MRP will be charged on this borrowing.*

Within the set of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross borrowing does not, except in the short-term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for current and next two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes except to cover short-term cash flows.

The Chief Finance Officer (Section 151 Officer) reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties over the life of the current MTFS. This view takes into account current commitments, existing plans, and the proposals in this budget report.

3: Prospects for interest rates

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on short and longer-term interest rates as summarised in the following table:

LINK GROUP RATE VIEW											
	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24
Bank Rate View	0.25%	0.25%	0.50%	0.50%	0.50%	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%
5yr PWLB	1.40%	1.50%	1.50%	1.60%	1.60%	1.70%	1.80%	1.80%	1.80%	1.90%	1.90%
10yr PWLB	1.60%	1.70%	1.80%	1.90%	1.90%	1.90%	2.00%	2.00%	2.00%	2.10%	2.10%
25yr PWLB	1.80%	1.90%	2.00%	2.10%	2.10%	2.20%	2.20%	2.20%	2.30%	2.30%	2.40%
50yr PWLB	1.50%	1.70%	1.80%	1.90%	1.90%	2.00%	2.00%	2.00%	2.10%	2.10%	2.20%

These are forecasts for certainty rates; gilt yields plus 80 basis points.

The publication of official LIBOR (London Inter-Bank Offered Rate) figures (and related LIBID (London Inter-Bank Bid Rate) calculations) will cease at the close of 2021. As such, references within this document have been updated to SONIA (Sterling Overnight Index Average), which is the risk-free rate for sterling markets administered by the Bank of England and the preferred benchmark for the transition to sterling risk-free rates from LIBOR. SONIA is based on actual transactions and reflects the average of the interest rates that banks pay to borrow sterling overnight from other financial institutions and other institutional investors. To support the Risk-Free Rate transition in sterling markets, the Bank of England began publishing the SONIA Compounded Index from 3 August 2020. This simplifies the calculation of compounded interest rates and in doing so provides a standardised basis through its publication as an official source.

The coronavirus outbreak has resulted in significant economic damage to the UK and economies around the world. After the Bank of England took emergency action in March 2020 to cut the Bank Rate to 0.10%, it has then left the Bank Rate unchanged at its subsequent meetings until December 2021 when it increased the rate to 0.25%. However, as shown in the forecast table above, the forecast for the Bank Rate now includes a further three increases from 0.25% in December 2021 to 1.00% by June 2024.

Gilt yields / PWLB rates

As the interest forecast table for PWLB certainty rates above shows, the assumption is for a steady rise over the forecast period, with some degree of uplift due to rising treasury yields in the United States (US). However, there is likely to be exceptional volatility and unpredictability in respect of gilt yields and PWLB rates due to the following factors:

- The potential impact that rising treasury yields in the US could have. As an average since 2011, there has been a 75% correlation between movements in US 10-year treasury yields and UK 10-year gilt yields. This is a significant upward risk exposure to forecasts for longer-term PWLB rates. However, gilt yields and treasury yields do not always move in unison.
- Whether the Monetary Policy Committee (MPC) act to counter increasing gilt yields if they rise beyond a yet unspecified level.
- How strong inflationary pressures turn out to be in both the US and the UK, putting upward pressure on treasury and gilt yields.
- How central banks implement their new average or sustainable level inflation monetary policies.
- How well central banks manage the withdrawal of quantitative easing purchases of national bonds.

- Whether exceptional volatility will be focused on the short or long end of the yield curve, or both.

Investment and borrowing rates

Investment returns are forecast to improve in 2022/23 based on expected increases in the Bank Rate; but actual economic circumstances may result in less improvement than expected.

Borrowing interest rates fell to historically very low rates as a result of the Covid-19 pandemic and the quantitative easing operations of the Bank of England and remain at historically low levels. However, the policy of avoiding new borrowing by running down spare cash balances has continued to be beneficial for local authorities over the last few years. The current margins over gilt yields for different types of capital expenditure are as follows:

- PWLB Standard Rate is gilt plus 100 basis points (G+100bps)
- PWLB Certainty Rate is gilt plus 80 basis points (G+80bps)
- Local Infrastructure Rate is gilt plus 60bps (G+60bps)

The long-term forecast (beyond 10 years) for the Bank Rate is 2.00%. As some PWLB certainty rates are currently below 2.00%, there remains value in considering long-term borrowing from PWLB where appropriate, plus longer-term borrowing could also be undertaken for the purpose of certainty, or for flattening the profile of a heavily unbalanced maturity profile.

Temporary borrowing rates are likely, however, to remain near the current Bank Rate, which may also prove attractive as part of the Council's overall borrowing strategy. The Council will assess its risk appetite in conjunction with budgetary pressures to reduce total interest costs whilst also looking to balance out the debt portfolio. While this authority will not be able to avoid borrowing to finance new capital expenditure and to replace maturing debt, there will be a cost of carry (the difference between higher borrowing costs and lower investment returns) to any new borrowing that causes a temporary increase in cash balances.

4: Borrowing strategy

The overarching objectives for the borrowing strategy are as follows:

- To manage the Council's debt maturity profile.
- To maintain a view on current and possible future interest rate movements, and to plan borrowing accordingly.
- To monitor and review the balance between fixed and variable rate loans against the background of interest rates and the Prudential Indicators.
- Reduce reliance on one source of funding and review all alterative options available, including forward loan agreements.
- Continue to support UK Municipal Bonds Agency (MBA) bond issuance programme.
- Provide value for money and savings where possible to meet budgetary pressures.

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

Against this background and the risks within the economic forecast, caution will be adopted with the 2022/23 treasury operations. The Section 151 Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances. The decision to maintain internal borrowing will be evaluated against the potential for incurring additional long-term borrowing costs in later years, when long-term interest rates are forecast to be significantly higher.

If a significant risk of a sharp fall in long and short-term rates materialises (e.g., due to a marked increase of risks around relapse into recession or of risks of deflation), then long-term borrowings will be postponed, and potential rescheduling from fixed rate funding into short-term borrowing will be considered.

If a significant risk of a much sharper rise in long and short-term rates materialises than that currently forecast (e.g., perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the US and UK, an increase in world economic activity or a sudden increase in inflation risks), then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

In November 2019 the Council secured approval for £61m worth of discounted Local Infrastructure Rate funding via the PWLB to support clean energy work in Cambridgeshire in relation to the following projects:

- Five projects in our energy investment programme. These are primarily solar photovoltaic and battery storage projects across our assets. They are being developed to address major challenges our antiquated electricity grid is having which impact housing and business growth in the county, as well as limiting our ability to increase the amount of local, low carbon generation capacity.
- Three projects for community energy infrastructure. Swaffham Prior will be the first to retrofit an existing rural, off-gas community with a low carbon district heating scheme. Once built, the St Ives Smart Energy Grid would be the largest solar canopy project of its kind in the UK. One novel component is the Business Support Program offering which will pass along our lessons learned to the clean tech sector, assisting in wider uptake. And finally, ongoing energy efficiency and energy generation programme in schools. In this phase, we'll be exploring how to turn some schools into energy centres, supplying themselves and their communities with low carbon heat.

In March 2020, £8m of borrowing was drawn down at a rate of 1.45%, followed by a further £6m in August 2021 at a rate of 1.56%. The remainder of the borrowing is expected to be accessed during 2022/23.

Capital Prudential & Treasury Indicators

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their prudential indicators.

A full set of prudential indicators and borrowing limits are shown in Appendix 3 of the TMS.

Policy on borrowing in advance of need

The Council will not borrow more than, or in advance of, its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance of need will be within the forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds. Borrowing in advance will be considered within the following constraints:

Year	Max. Borrowing in advance	Notes
2022/23	100%	Borrowing in advance will be limited to no more than the expected increase in borrowing need (CFR) over the period of the approved Medium Term Capital Programme, a maximum of 3 years in advance.
2023/24	50%	
2024/25	25%	

The risks associated with any borrowing in advance activity will be subject to prior appraisal. Any advance borrowing undertaken will be reported in Treasury Management update reports.

Debt rescheduling

As short-term borrowing rates are often considerably cheaper than longer-term fixed interest rates, there may be potential opportunities to generate savings by switching from long-term borrowing to short-term borrowing. However, these savings will need to be considered in the light of the current treasury position and, in the current economic climate, the substantial exit costs of any debt repayment.

The reasons for any rescheduling to take place include:

- The generation of cash savings and/or discounted cash flow savings.
- Helping to fulfil the treasury strategy.
- Enhancing the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

Any rescheduling activity undertaken will be reported to Strategy and Resources (S&R) Committee, at the next quarterly report following its action.

New financial institutions as a source of borrowing

Currently the PWLB Certainty Rate is set at gilts + 80 basis points. However, consideration may still need to be given to obtaining funding from other sources:

- Local authorities provide primarily shorter-dated maturities of up to around 3 years at lower rates than the Certainty Rate.
- Financial institutions, primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a "cost of carry" or to achieve refinancing certainty over the next few years.
- UK MBA (see part 11).
- UK Infrastructure Bank, launched in June 2021 to support the Government's plan to deliver £600bn in gross public sector investment over the next 5 years. The bank will offer loans to local authorities at a rate of gilts plus 60 bps.

5: Minimum Revenue Provision

The Council is required to repay an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the Minimum Revenue Provision - MRP), although it is also allowed to undertake additional voluntary payments if desired (Voluntary Revenue Provision - VRP).

DLUHC Regulations have been issued which require Council to approve an MRP Statement in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The MRP Policy is in Appendix 4 of the TMS. The Council, in conjunction with its Treasury Management advisors, considers the MRP policy to be prudent.

6: Investment strategy

The Government's 'Guidance on Local Government Investments' requires that an Annual Investment Strategy (AIS) be set. The Guidance permits the Treasury Management Strategy and the Annual Investment Strategy to be combined into one document.

The Council's general policy objective is to invest its surplus funds prudently. As such the Council's investment priorities in priority order are:

- the security of the invested capital
- the liquidity of the invested capital
- the yield received from the investment

The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and within the Council's risk appetite. In the current economic climate, it is considered appropriate to keep investments short-term to cover cash flow needs. However, where appropriate (from an internal as well as external perspective), the Council will also consider the value available in periods up to 12 months with high credit rated financial institutions, as well as wider-ranging fund options.

The Council's Annual Investment Strategy (AIS) is shown in Appendix 5.

7: Risk Analysis and Forecast Sensitivity

Risk Management

The Council regards the successful identification, monitoring, and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Treasury management risks are identified in the Council's approved Treasury Management Practices. The main risks to the treasury activities are:

- Credit and counterparty risk (security of investments)
- Liquidity risk (adequacy of cash resources)
- Interest rate risk (fluctuations in interest rate levels)
- Exchange rate risk (fluctuations in exchange rates)
- Refinancing risks (impact of debt maturing in future years)

- Legal and regulatory risk (non-compliance with statutory and regulatory requirements)
- Fraud, error and corruption, and contingency management (in normal and business continuity situations)
- Market risk (fluctuations in the value of principal sums)

The TMP Schedules set out the ways in which the Council seeks to mitigate these risks. Examples are the segregation of duties (to counter fraud, error, and corruption), and the use of creditworthiness criteria and counterparty limits (to minimise credit and counterparty risk). Council officers, in conjunction with the treasury advisers, will monitor these risks closely.

Sensitivity of the Forecast

The sensitivity of the forecast is linked primarily to movements in interest rates and in cash balances, both of which can be volatile. Interest rates in particular are subject to global external influences over which the Council has no control.

Both interest rates and cash balances will be monitored closely throughout the year and potential impacts on the Council's debt financing budget will be assessed. Action will be taken as appropriate, within the limits of the TMP Schedules and the treasury strategy, and in line with the Council's risk appetite, to keep negative variations to a minimum. Any significant variations will be reported to S&R Committee as part of the Council's regular budget monitoring arrangements.

8: Reporting arrangements

Capital Strategy

The CIPFA revised 2017 Prudential and Treasury Management Codes requires local authorities to prepare a Capital Strategy report which provides the following:

- a high-level long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed

- the implications for future financial sustainability

The aim of the capital strategy is to ensure that all elected members fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

The Council's Capital Strategy is reported separately from the Treasury Management Strategy within the Business Plan and reports on non-treasury investments. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy on commercial investments usually driven by expenditure on an asset. The Capital Strategy demonstrates:

- The corporate governance arrangements for these types of activities
- Any service objectives relating to the investments
- The expected income, costs and resulting contribution
- The debt related to the activity and the associated interest costs
- For non-loan type investments, the cost against the current market value
- The risk associated with each activity

For non-treasury investment where a physical asset is being bought, details of market research, advisors used (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

Where the Council has borrowed to fund any non-treasury investment, there is also an explanation of why borrowing was required and why the DLUHC Investment Guidance and CIPFA Prudential Code have not been adhered to.

If any non-treasury investment sustains a loss during the final accounts and audit process, the strategy and revenue implications will be reported through the same procedure as the Capital Strategy.

The Capital Strategy will also consider the proportionality between the treasury investments shown throughout this report and non-treasury investments.

Treasury Management Reporting

The Council is currently required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals:

a) **Prudential and treasury indicators and treasury strategy (this report)** - The first, and most important report is forward looking and covers:

- capital plans (including prudential indicators)
- a Minimum Revenue Provision (MRP) policy (how residual capital expenditure is charged to revenue over time)
- the Treasury Management Strategy (how the investments and borrowings are to be organised), including treasury indicators
- an Investment Strategy (the parameters on how investments are to be managed)

b) **A mid-year treasury management report** – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision. In addition, S&R Committee will receive quarterly update reports.

c) **An annual treasury report** – This is a backward-looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

The above reports are required to be adequately scrutinised before being recommended to Council. This role is undertaken by the Section 151 Officer & S&R Committee.

9: Treasury Management Budget

The table below provides a breakdown of the treasury management budget at January 2022. Key assumptions behind the 2022/23 budget estimates are:

- Average rates achievable on short-term investments will be 0.1% (increasing to 0.6%), the average net return on the Council's long-term CCLA property fund treasury management investment will be 3.4%, the average return on multi-class asset will be 2.1% and the average return on the infrastructure income fund will be 3.8%.

- New and replacement borrowing to fund the capital programme will be financed by a mixture of short to medium-term borrowing, at rates equating to between 1.5% and 3.0% over the medium-term.
- The MRP charge is in line with the Council's MRP policy.

	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m
Interest payable	18.7	19.5	22.4	23.8	24.2	23.9
MRP	19.1	21.3	24.0	26.5	27.3	28.0
Interest receivable	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7
Interest on investment activity	0.7	0.7	0.7	0.7	0.7	0.7
Debt Management Expenses	0.6	0.4	0.4	0.4	0.4	0.4
Net Interest expenses recharged to Service	-6.2	-6.0	-7.4	-7.9	-9.1	-8.8
Technical adjustments	0.1	0.8	-0.7	-0.8	-0.9	0.1
Sub Total	**32.3**	**36.0**	**38.7**	**42.0**	**41.9**	**43.6**
Capitalised Interest	-2.1	-1.9	-2.0	-1.6	-0.8	-0.9
Grand Total	**30.3**	**34.0**	**36.8**	**40.5**	**41.1**	**42.6**

10: Policy on the use of external service providers/consultant

The Council's external treasury management advisors are Link Group, Treasury solutions. The two-year extension option within the contract with Link Asset Servicing has been activated, following the original formal procurement exercise in 2019/20.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, the Council's treasury advisers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

11: Future developments

Local Authorities are having to consider innovative strategies towards improving service provision to their communities. This approach to innovation also applies to councils' treasury management activities. The Government is introducing new statutory powers and policy change which will have an impact on treasury management approaches in the future. Examples of such changes are:

a) **Loans to Third Parties**
The Council may borrow to make grants or loans to third parties for the purpose of capital expenditure, as allowable under paragraph 25 (1) (b) of the Local Authorities (Capital Financing and Accounting) (England) Regulations 2003 (Statutory Instrument No. 3146). This will usually be to support local economic development, and may be funded by external borrowing.

A framework within which the Council may consider advancing loans to third party, not for profit, organisations is shown in Appendix 6 of the TMS.

In addition, the following material projects in this respect are under way:

- This Land – loans issued at commercial rates, to facilitate the construction of residential housing in Cambridgeshire and the vicinity

b) **UK Municipal Bonds Agency (MBA)**
The County Council remains committed to participating in a multi-authority pooled bond, facilitated by the MBA, as complementary to PWLB borrowing. The purpose of the MBA is to issue bonds in the capital markets at lower rates than the PWLB.

The November 2020 reduction in margin over gilts for PWLB rates by 100 basis points on local authorities' loans means that UK MBA is now a less favourable an option than it had been in comparison to higher PWLB rates but there should remain a narrow competitive margin relative to PWLB.

To date the MBA has issued a small number of single Council bonds and a pooled bond issue is awaited.

c) **Impact of IFRS 9**

An important consideration when assessing current and future investment policy is the implementation of accounting standard IFRS 9 in the Local Authority Code of Practice. A key element of this standard is the move away from assessing risk based on incurred losses on financial assets (i.e., an event that has happened) to expected loss (i.e., the likelihood of loss across the asset lifetime). Whilst this will not materially impact upon traditional treasury investments, the standard also encompasses other investment areas including loans to third parties, subsidiaries, or longer-dated service investments. The expected credit loss model requires local authorities to make provision for these potential losses having assessed the asset with regard to the due diligence undertaken prior to investment, the nature of any guarantees, and subsequent regular updates.

The Council has made the following material loan agreement with third parties:

- This Land – loans at commercial rates to facilitate the construction of residential housing in Cambridgeshire.

A revenue provision may be required to be set aside in future depending on the risk assessment of the investment.

In addition to the above, the new standard requires changes to the recognition and subsequent valuation treatment of certain investment products. These instruments include property and equity, but also service investments that give rise to cashflows that are not solely payments of principal and interest (SPPI) on the principal outstanding. DLUHC introduced a five-year statutory override allowing Councils to reverse any revenue impact of pooled fund valuation gains and losses. DLUHC were not minded to make this statutory override permanent, and will keep it under review.

12: Training

A key outcome of investigations into local authority investments following the credit crisis has been an emphasis on the need to ensure appropriate training and knowledge in relation to treasury management activities, for officers employed by the Council, in particular treasury management staff, and for members charged with governance of the treasury management function.

Link Group run training events regularly which are attended by the Treasury Team. In addition, members of the team attend national forums and practitioner user groups. Treasury Management training for committee members will be delivered as required to facilitate informed decision making and challenge processes. The last training to take place was a session as part of the Member induction plan for the 2021-25 Council in December 2021.

13: List of appendices

Appendix 1: Treasury Management Scheme of Delegation and Role of Section 151 Officer
Appendix 2: Treasury Management Policy Statement
Appendix 3: Prudential and Treasury Indicators
Appendix 4: Minimum Revenue Provision (MRP) Policy Statement
Appendix 5: Annual Investment Strategy
Appendix 6: Third Party Loans Policy

Appendix 1: Treasury Management Scheme of Delegation and role of the Section 151 Officer

The Scheme of Delegation

Council:

- Approval of annual Treasury Management Strategy and mid-year update to the strategy.
- Approval of the annual Treasury Management report.
- Approval of the Treasury Management budget.

Strategy & Resources Committee:

- Approval of the Treasury Management quarterly update reports.
- Approval of the Treasury Management outturn report
- Scrutiny of performance against the Strategy.
- Management of the Council's non-financial Investment Strategy

The Treasury Management role of the Section 151 Officer

The Council's Chief Finance Officer (CFO) is the officer designated for the purposes of Section 151 of the Local Government Act 1972 as the Responsible Officer for treasury management at the Council.

The Council's Financial Regulations delegates responsibility for the execution and administration of treasury management decisions to the CFO, who will act in accordance with the Council's policy statement and TMPs and CIPFA's Standard of Professional Practice on Treasury Management.

The CFO has delegated powers through this policy to take the most appropriate form of borrowing from the approved sources, and to make the most appropriate form of investments in approved instruments.

Prior to entering into any capital financing, lending, or investment transaction, it is the responsibility of the responsible officer to be satisfied, by reference to the Council's legal department and external advisors as appropriate, that the proposed transaction does not breach any statute, external regulation or the Council's Financial Regulations.

The CFO may delegate his power to borrow and invest to members of his staff.

The CFO is responsible for:

- Ensuring that the schedules to the Treasury Management Practices (TMPs) are fully reviewed and updated annually and monitoring compliance to the Treasury Management in the Public Services: Code of Practice and Guidance Notes
- Ensuring that the Council's Treasury Management Policy is adhered to, and if not, bringing the matter to the attention of elected members as soon as possible
- Submitting regular treasury management reports to S&R Committee and Council
- Submitting debt financing revenue budgets and budget variations in line with the Council's budgetary policies
- Receiving and reviewing treasury management information reports
- Reviewing the performance of the treasury management function and promoting value for money
- Ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- Ensuring the adequacy of internal audit, and liaising with external audit
- Recommending the appointment of external service providers (e.g., treasury management advisors) in line with the approval limits set out in the Council's procurement rules
- Preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments, and treasury management, with a long-term timeframe
- Ensuring that the capital strategy is prudent, sustainable, affordable, and prudent in the long-term and provides value for money
- Ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority
- Ensuring that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- Ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources

- Ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long-term liabilities
- Provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans, and financial guarantees
- Ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- Ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- Creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed

Appendix 2: Treasury Management Policy Statement

We define treasury management activities 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."

We regard the successful identification, monitoring, and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

We acknowledge that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management

Appendix 3: Prudential and Treasury Indicators

1: The Capital Prudential Indicators

The Council's capital expenditure plans are the key driver of Treasury Management activity. The output of the capital expenditure plans is reflected in prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

Capital expenditure. This prudential indicator shows the Council's capital expenditure plans; both those agreed previously, and those forming part of this budget cycle. Capital expenditure excludes spend on Private Finance Initiatives (PFI) and leasing arrangements, which are shown on the balance sheet.

The table below summarises the capital expenditure plans which give rise to a net financing need (borrowing). Detailed capital expenditure plans are set out in the Capital Strategy.

	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m
Net Borrowing Requirement to fund Capital Programme	30.7	59.8	60.3	10.8	15.4	-34.3

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

Following accounting changes, the CFR includes any other long-term liabilities (e.g., PFI schemes, finance leases) brought onto the balance sheet. Whilst this increases the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes.

	2021/22 Actual £m	2022/23 Estimate £m	2023/24 Estimate £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m
Capital Financing Requirement (CFR)						
Total CFR	**946.4**	**1,006.2**	**1,066.4**	**1,077.2**	**1,092.7**	**1,058.4**
Movement in CFR	**30.7**	**59.8**	**60.3**	**10.8**	**15.4**	**-34.3**
Movement in CFR represented by:						
Unsupported Capital Expenditure (Prudential Borrowing) in capital programme	51.8	81.1	84.2	37.3	42.8	21.6
Less: MRP and other financing movements	-21.2	-21.3	-24.0	-26.5	-27.3	-55.8
Movement in CFR	**30.7**	**59.8**	**60.3**	**10.8**	**15.4**	**-34.3**

The authorised limit for external borrowing. A key prudential indicator, this represents a control on the maximum level of borrowing and the legal limit beyond which external borrowing is prohibited. This limit is set by and can only be amended by Council. It reflects the level of external borrowing which, while not desired, could be afforded in the short-term, but is not sustainable in the longer-term. The limit represents the total CFR (assumed fully funded by borrowing) - including any other long-term liabilities (e.g., PFI schemes, finance leases) though these types of scheme including a borrowing facility and so the Council is not required to separately borrow for them - plus a margin to accommodate any unplanned adverse cashflow movements.

This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised. The Council is asked to approve the following Authorised Limit:

Authorised Limit	2022/23 £m	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m
Total Borrowing	1,090	1,140	1,190	1,200	1,220

The operational boundary. This is the operational limit, set deliberately lower than the authorised limit, beyond which external debt is not normally expected to exceed. The limit represents the total CFR (assumed fully funded by borrowing) - including any other long-term liabilities (e.g., PFI schemes, finance leases) though these types of scheme including a borrowing facility and so the Council is not required to separately borrow for them - plus a margin to accommodate any unplanned adverse cashflow movements. This limit acts as an early warning indicator should borrowing be approaching the Authorised Limit. This limit may be breached on occasion under normal circumstances, but sustained or regular breaches should trigger a review of borrowing levels.

Operational Boundary	2022/23 £m	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m
Total Borrowing	1,060	1,110	1,160	1,170	1,190

2: Treasury Management limits on activity

There are four debt and investment related treasury activity limits. The purpose of these are to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive, they will impair the opportunities to reduce costs or improve performance. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments.
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates.
- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large, fixed rate sums falling due for refinancing, and are required for upper and lower limits.

The interest rate exposure is calculated a percentage of net debt. Due to the mathematical calculation exposures could be greater than 100% of below zero (i.e., negative) depending on the component parts of the formula. The formulas are shown below.

Fixed rate calculation:

$$\frac{\text{Fixed rate borrowing – fixed rate investments}}{\text{Total borrowing – total investments}}$$

Variable rate calculation:

Variable rate borrowing** – fixed rate investments

Total borrowing – total investments

**defined as less than 1 year to remaining to maturity, or in the case of LOBO borrowing, the next call date falling within 12 months.

Limits on Interest Rate Exposure	2022/23	2023/24	2024/25	2025/26	2026/27
	Upper	Upper	Upper	Upper	Upper
Limits on fixed interest rates based on net debt	150%	150%	150%	150%	150%
Limits on variable interest rates based on net debt	65%	65%	65%	65%	65%

The maturity structure of borrowing indicator represents the borrowing falling due in each period expressed as a percentage of total borrowing. These gross limits are set to manage the Council's exposure to sums falling due for refinancing or repayment.

Maturity Structure of Borrowing			
	Lower	Upper	30/10/2021 Comparator
Under 12 months	0%	80%	27%
12 months to 2 years	0%	50%	6%
2 years to 5 years	0%	50%	10%
5 years to 10 years	0%	50%	12%
10 years and above	0%	100%	45%

The Treasury Management Code of Practice Guidance notes require that maturity is determined by the earliest date on which the lender can require repayment, which in the case of LOBO loans, is the next break point.

Total principal funds invested for periods longer than 365 days. The Council is asked to approve the following treasury indicator limits for total principal funds that may be invested for periods greater than 365 days. The limits are set with regard to the Council's liquidity requirements to reduce the risk of need for early liquidation of investment and are based on the medium/long-term availability of resources after each year end.

Maximum principal sums invested for periods longer than 365 days					
	2022/23	2023/24	2024/25	2025/26	2026/27
Limit (£m)	50	50	50	50	50

3: Affordability Prudential Indicators

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework is an indicator required to assess the affordability of the capital investment plans. This provides an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicator:

Actual and estimates of financing costs to net revenue stream. This indicator identifies the trend in the cost of capital (borrowing and other long-term obligation costs net of investment income) against the net revenue stream. The estimates of financing costs include current commitments and the proposals in this budget report.

This is calculated as the estimated net financing costs for the year divided by the amounts to be met from government grants and local taxpayers.

Actual and estimates of financing costs to net revenue stream					
	2022/23 Estimate %	2023/24 Estimate %	2024/25 Estimate %	2025/26 Estimate %	2026/27 Estimate %
Financing costs to net revenue stream	8.9	9.6	10.1	9.7	9.6

Appendix 4: Minimum Revenue Provision Policy Statement

Policy statement

The Council is required to repay an element of the accumulated General Fund capital spend each year (Capital Financing Requirement - CFR) through a revenue charge (Minimum Revenue Provision - MRP), although it is also allowed to undertake additional voluntary payments if required.

DLUHC have issued regulations that require Council to approve an MRP Statement in advance of each year. A variety of options are provided to Councils in the guidance with the underlying principle that a prudent provision is made. A formal review of this Policy is to be undertaken every five years with the next review due to take place in January 2021. Due to capacity issues, in part as a result of the additional work required by the ongoing pandemic, this review has been delayed by one year to March 2022. This has allowed a detailed review to be undertaken during 2021/22, in conjunction with the Council's treasury advisors.

Historic debt liability accumulated up to 31st March 2010

Up until 2014/15, the proportion of provision that related to historic debt liability accumulated up to 31st March 2010 was calculated using Option 1 of DLUHC Guidance (the 'Regulatory Method'). This method is based upon 4% of the CFR adjusted for 'Adjustment A' (the difference between the old credit ceiling system and the introduction of the Capital Financing Requirement). A reducing balance calculation means that debt liability is never entirely repaid, and the amount of debt equal to 'Adjustment A' (for this Council £2.133m) is not provided for at all. In January and February 2016, General Purposes Committee (GPC) considered a number of potential alternative methodologies. These covered both annuity and straight-line options, calculated over an average life of up to 50 years.

After considering the range of options available, a change in policy was introduced from 2015/16. The method chosen to replace the "Regulatory Method" for historic debt liability accumulated up to 31st March 2010 and that remained outstanding at 31st March 2015 was an annuity calculation, but one directly linked to the remaining life of the assets the debt liability had funded (held on the Council's balance sheet). This directly relates the cost of financing those assets with their expected useful life, thereby aligning costs with benefits and is allowable under the DLUHC Guidance. This approach will continue to be applied.

Debt liability accumulated from 1st April 2010

Prudent provision for any subsequent borrowing from 1st April 2010 onwards will be calculated using Option 3 of DLUHC Guidance (the 'Asset Life Method') on a straight line basis, in line with estimates for the expected useful life of the asset financed by debt. Estimated life periods will be determined under delegated powers. In view of the variety of types of capital expenditure incurred by the Council, which is not in all cases capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. MRP will be charged from the financial year after the asset becomes operational.

The determination as to which schemes shall be deemed to be financed from available capital resources and those which will remain as an outstanding debt liability to be financed by borrowing or other means will be assessed under delegated powers.

Third Party Loans

The only exception to these rules is loans classified as capital expenditure and raised by the Council for the purposes of funding third party loans. No MRP will be charged on this debt liability as the loans will be repaid in full in later years by way of capital receipt which will be used to repay that borrowing. Each item where there is no annual MRP charge will be reviewed on at least an annual basis and if there is a likelihood of capital loss, an expected loss would be charged in accordance with IFRS 9 requirements (see part 11).

Share/Equity Capital

The Council may invest in share and equity investments, either directly or through collective pooled funds. These investments will usually be treated as capital expenditure and in such cases, where these investments are funded by unsupported borrowing, MRP charges will be considered on a case-by-case prudent basis.

Private Finance Initiatives (PFI)

For assets acquired by leases, contracts or Private Finance Initiatives, the element of the annual charge that goes to write down the balance sheet liability will be applied as MRP.

Appendix 5: Annual Investment Strategy

1: Investment policy

DLUHC and CIPFA have extended the meaning of ‘investments’ to include both financial and non-financial investments. This report deals solely with financial investments managed by the treasury management team. Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy.

The Council’s appetite for risk must be clearly identified in its strategy report. The Council affirms that its investment policies are underpinned by a strategy of prudent investment of funds held on behalf of the local community. The objectives of the investment policy are firstly the security of funds (protecting the capital sum from loss) and then liquidity (keeping money readily available for expenditure when needed). Once approved levels of security and liquidity are met, the Council will seek to maximise yield from its investments, consistent with the applying of the agreed parameters. These principles are carried out by strict adherence to the risk management and control strategies set out in the TMP Schedules and the Treasury Management Strategy.

Responsibility for risk management and control lies within the Council and cannot be delegated to an outside organisation. Investment instruments identified for use in the financial year are listed in parts 6 and 7 of this appendix under the ‘Specified’ and ‘Non-Specified’ Investment categories.

Council’s in-house funds
Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e., rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. While most cash balances are required in order to manage the ups and downs of cash flow, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer-term investments will be carefully assessed.

- If it is thought that the Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments as short-term or variable.

- Conversely, if it is thought that the Bank Rate is likely to fall within that time period, consideration will be given to locking in higher rates for longer periods.

Investment returns expectations

The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows (the long-term forecast is for periods over 10 years in the future):

Average earnings in each year	
2022/23	0.50%
2023/24	0.75%
2024/25	1.00%
2025/26	1.25%
Long term later years	2.00%

2: Creditworthiness policy

The Council's counterparty and credit risk management policies and its approved instruments for investments are set out below. These, taken together, form the fundamental parameters of the Council's Investment Strategy.

The Council defines high credit quality in terms of investment counterparties as those organisations that:

- Meet the requirements of the creditworthiness service provided by the Council's external treasury advisors and;
- UK banking or other financial institutions, or are;
- UK national or local government bodies, or are;
- Countries with a sovereign ratings of -AA or above, or are;
- Triple-A rated Money Market funds.

The creditworthiness service provided by the Council's external treasury advisors applies a modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard & Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies

- Credit Default Swaps (CDS – a traded insurance policy market against default risk) spreads to give early warning of likely changes in credit ratings
- sovereign ratings to select counterparties from only the most creditworthy countries

This modelling approach combines credit ratings, credit Watches and credit Outlooks in a weighted calculation with an overlay of CDS spreads, to determine suggested duration for investment. The Council will apply these suggested duration limits to it investments at all times, unless otherwise approved by the CFO.

Investments held in a multi-class credit fund are diversified across investment grade and high-yielding credit in accordance with the Council's treasury management objectives and appetite for risk.

The Council makes arrangements for monitoring of the more 'liquid' non-specified investments through professional advice, including from an independent investment advisor, from time-to-time. These arrangements are overseen by the Strategy & Resources Committee.

All credit ratings will be monitored daily**.** The Council is alerted to changes in ratings of all three agencies through its use of the Link creditworthiness service:

- If a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- In addition to the use of credit ratings, the Council will be advised of information in movements in Credit Default Swap spreads against the iTraxx European Financials benchmark and other market data on a daily basis via its Passport website, provided exclusively by Link. Extreme market movements may result in a downgrade of an institution, or removal from the Council's lending list.

Sole reliance will not be placed on the use of the Council's external treasury advisor's creditworthiness service. In addition, the Council will also use market data, financial press, and information on any external support for banks to help support its decision-making process.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times, and as such the CFO shall have the discretion during the year to lift or increase the restrictions on the counterparty list and or to adjust the associated lending limits on values and durations should it become necessary, to enable the effective management of risk in relation to its investments.

3: Sovereign Limits

Expectation of implicit sovereign support for banks and financial institutions in extraordinary situations has lessened considerably in the last couple of years, and alongside that, changes to banking regulations have focussed on improving the banking sectors resilience to financial and economic stress.

The Council has determined that it will only use approved counterparties from overseas countries with a sovereign credit rating from the three main ratings agencies that is equal to or above AA-. Banks domiciled in the UK are exempt from this minimum sovereign credit rating, so may be used if the sovereign rating of the UK fall below AA-.

The list of countries that qualify using these credit criteria as at January 2022 is shown below. This list will be amended by officers should ratings change in accordance with this policy.

AAA	AA+	AA	AA-
Australia	Finland	Abu Dhabi (UAE)	Qatar
Canada	USA	Belgium	
Denmark		France	
Germany		UK	
Netherlands			
Singapore			
Sweden			
Switzerland			

4: Banking services

Following a competitive tender exercise and the completion of the contract standstill period in December 2019, the Council completed the switching of Banker on 5 October 2020 from Barclays Bank to NatWest Bank. The Council has remaining residual accounts at Barclays for treasury management purposes and deputyship clients.

The Council may continue to use its own bankers for transactional purposes if the credit rating of the institution falls below the above minimum criteria, however, balances will be minimised in both monetary size and time invested.

5: Investment position and use of Council's resources

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.).

Investments will be made with reference to core balances, cash flow requirements and the outlook for interest rates.

For its cash flow generated balances, the Council will seek to utilise its business banking reserve account and notice accounts, money market funds (CNAV, LVNAV and VNAV) and short-dated term deposits in order to benefit from the compounding of interest.

6: Specified investments

The Council assesses that an investment is a specified investment if all of the following criteria apply:

- The investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling.
- The investment is not a long-term investment (i.e., up to 1 year).
- The making of the investment is not defined as capital expenditure by virtue of regulation 25(1)(d) of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 [SI 3146 as amended].
- The investment is made with a body or in an investment scheme of high credit quality (see below) or with one of the following public-sector bodies:
    - The United Kingdom Government.
    - A local authority in England or Wales (as defined under section 23 of the 2003 Act) or a similar body in Scotland or Northern Ireland.
    - High credit quality is defined as a minimum credit rating as outlined in this strategy.

Specified investment instruments approved for use are:

Instrument	Minimum 'High' Credit Criteria	Maximum Amount
Debt Management Agency Deposit Facility (DMADF)	UK sovereign rating	No maximum
UK Government Gilts / Treasury Bills	UK sovereign rating	
Certificate of Deposits & Notice Accounts	Per Treasury Advisors creditworthiness service	£10m per individual/ group in total
Term Deposits - Banks and Building Societies	Per Treasury Advisors creditworthiness service	
Term Deposits - Local Authorities and Housing Associations	Considered on an individual basis	
Bank Call/Instant Access Accounts	Per Treasury Advisors creditworthiness service	£20m per individual/ group in total
Collateralised Deposit / Covered Bonds	AAA	
Bonds issued by multilateral development banks	AAA / UK sovereign rating	
Bond issuance issued by a financial institution which is explicitly guaranteed by UK Government (e.g., National Rail)	UK sovereign rating	
Sovereign bond issues (other than the UK Govt)	AAA / UK sovereign rating	
Collective Investment Schemes structured as Open-Ended Investment Companies (OEICs):		
Money Market Funds (CNAV, LVNAV or VNAV)	AAA MMF rating	£20m per individual/ group in total
CCLA (PSDF) Money Market Fund	Considered on an individual basis	
Bond Funds	Considered on an individual basis	
Gilt Funds	Considered on an individual basis	

The Council may enter into forward agreements up to 3 months in advance of the investment commencing. If forward agreements are made, the forward period plus the deal period should not exceed the 1 year to be classified as a specified investment.

Maximum counterparty limits may be temporarily exceeded by small amounts and for very short periods where interest is compounded by the counterparty to the principal investment amount. In such instances the interest amounts will be withdrawn as soon as reasonably practicable.

The counterparty limit with the Council's corporate bank may be utilised over and above the set counterparty limit on an overnight basis if cash surpluses are identified as a result of unexpected receipts of income after the day's dealing position is closed. This occurs when the timing for receipt of funds is uncertain, for example the sale of a property. In such instances, funds will be withdrawn to bring the Councils exposure back in line with the approved counterparty limit as soon as reasonably practicable and invested elsewhere in line with this strategy. If this happens, the CFO should be notified.

7: Non-specified investments

Non-specified investments are defined as those with less high credit quality, potentially for periods over one year, or for more complex instruments which require greater consideration and need to be passed by members and officers before authorisation.

Given the additional risk profile associated with non-specified investment, the Council may consult with its external treasury advisors before undertaking such investments where appropriate.

Non-specified investment instruments approved for use are:

Instrument	Minimum 'High' Credit Criteria	Maximum Amount
UK Government	Government backed	No maximum
Certificate of Deposits & Notice Accounts	Per Treasury Advisors creditworthiness service	£10m per individual/ group in total
Term Deposits - Banks and Building Societies	Per Treasury Advisors creditworthiness service	
Term Deposits - Local Authorities and Housing Associations	Considered on an individual basis	
Collateralised Deposit / Covered Bonds	AAA	£20m per individual/ group in total
Bonds issued by multilateral development banks	AAA / UK sovereign rating	
Bond issuance issued by a financial institution which is explicitly guaranteed by UK Government (e.g., National Rail)	UK sovereign rating	
Sovereign bond issues (other than the UK Govt)	AAA / UK sovereign rating	

Corporate Bond / Equity Holdings	Considered on an individual basis	£10m per individual/ group in total
Collective Investment Schemes structured as Open-Ended Investment Companies (OEICs):		
Property Funds	Considered on an individual basis	£20m per individual/ group in total
Infrastructure Funds	Considered on an individual basis	
Diversified Income / Multi Asset Funds	Considered on an individual basis	
Enhanced Money Market Funds	AAA VNAV MMF rating	
Corporate Bond / Equity Funds / Share Capital	Considered on an individual basis	
Asset Backed Securities / Green Energy Bonds	Considered on an individual basis	£5m per individual/ group in total
Ultra-short dated bond Funds	Considered on an individual basis	£5m per individual/ group in total

Maximum counterparty limits may be temporarily exceeded by small amounts and for very short periods where interest is compounded by the counterparty to the principal investment amount. In such instances the interest amounts will be withdrawn as soon as reasonably practicable.

8: Third Party Loans

The Council has the power to lend monies to third parties subject to a number of criteria:

- Any loans to or investments in third parties will be made under the Well Being powers of the Council conferred by section 2 of the Local Government Act 2000 or permitted under any other act.
- The Well Being power can be exercised for the benefit of some or all of the residents or visitors to a local authority's area. The power may also be used to benefit organisations and even an individual.

The primary aims of any investment - in order of priority - are the security of its capital, liquidity of its capital and to obtain a return on its capital commensurate with levels of security and liquidity. These aims are crucial in determining whether to proceed with a potential loan.

Appendix 6 of the TMS sets out the Council's framework within which it may consider advancing loans to third party, not for profit, organisations.

9: Investments defined as capital expenditure

The acquisition of share capital or loan capital in any corporate body is defined as capital expenditure under Regulation 25(1) (d) of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003. Such investments will have to be funded from capital or revenue resources and will be classified as 'non-specified investments'.

Investments in "money market funds" which are collective investment schemes and bonds issued by "multilateral development banks" – both defined in SI 2004 No 534 – will not be treated as capital expenditure.

A loan, grant or financial assistance provided by this Council to another body will be treated as capital expenditure if the Council would define the other body's use of those funds as capital had it undertaken the expenditure itself.

10: Provisions for credit related losses

If any of the Council's investments appear at risk of loss due to default (i.e., this is a credit related loss and not one resulting from a fall in price due to movements in interest rates) the Council will make revenue provision of an appropriate amount.

11: End of year investment report

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

12: External fund managers

Up to £60m of the Council's funds may be externally managed on a discretionary / pooled basis, currently by CCLA, Allianz Global Investors and VT Gravis. The Council's external fund managers comply with the Annual Investment Strategy. The agreements between the Council and the fund managers additionally stipulate guidelines on duration and other limits in order to contain and control risk.

The Council fully appreciates the importance of monitoring the activity and resultant performance of its appointed external fund manager. In order to aid this assessment, the Council has appointed Link Group & ArlingClose to monitor the performance of some of these funds and is provided with a suite of regular reporting. This includes:

- Measuring the external manager's performance on a periodic and ongoing basis.
- Monitoring and impact assessment (where appropriate) of investment decisions made by the manager, in light of portfolio positioning as well as general economic and specific market background.
- Comparing fund manager performance against fund guidelines, benchmark, and target return (where applicable).
- Comparing fund manager performance against the Council's threshold for market risk and the degree of volatility in returns it is willing to accept in its risk-reward relationship

In addition to formal reports, representatives of Link Group meet with representatives of the fund manager semi-annually to review performance, address any concerns, and gain a better understanding of the manager's future strategy and direction.

13: Investment performance / risk benchmarking

These benchmarks are simple guides to maximum risk, so they may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that officers will monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the mid-year or annual reports.

14: Pension fund cash

The Council will comply with the requirements of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009, which were implemented on 1 January 2010. The Council will not pool pension fund cash with its own cash balances for investment purposes. Any investments made by the pension fund directly with the Council will comply with the requirements of SI 2009 No 393.

Appendix 6: Third Party Loans Policy

Introduction

Whilst the Council should not wish to become a commercial lender in the marketplace it can use its ability to borrow, at relatively economic rates, to support the delivery of improved outcomes for the residents of Cambridgeshire. At the same time this will facilitate the creation of a relatively modest income stream to support the Council's overall financial resilience. All applications must demonstrate alignment to the Council's core objectives and priorities and should support those outcomes.

The intention of this policy is therefore to establish a framework within which the Council may consider advancing loans to third party, not for profit, organisations.

Nature of Organisations Considered

The Council will consider the provision of a loan facility to organisations that fulfil both of the following criteria:

- Not for Profit Organisations, where the loan required will be used to fund infrastructure to support the delivery of services to the residents of Cambridgeshire, and;
- Organisations that provide services that align to the Council's core objectives and priorities (including subsidiary companies and joint ventures)

Governance Arrangements

All proposals will be considered by the Capital Programme Board or equivalent forum. Loans of less than £250,000 that fulfil the policy framework are delegated to the Council's CFO in consultation with the Chair of S&R Committee. Should the Committee Chair declare a conflict of interest, consultation will take place with the Committee Vice-Chair.

Loans in excess of £250,000 or loans that are outside of the framework parameters require S&R Committee approval. The exception to this is loans associated with Council owned assets which remain within the remit of S&R Committee.

Limits

No specific limits are proposed but all loans in excess of £250,000 will require S&R Committee approval. Given the level of administration that will be required to manage the loan agreement over the life of the loan, no requests for loans of less than £10,000 will be considered.

Business Case Review

Any application for loan finance must be accompanied by a robust business case. Due-diligence checks will be undertaken to test the underlying assumptions applied. Specialist support may be required to carry out these assessments.

Subsidy control and Interest Rates

Under EU law, State Aid rules were to be taken into account whenever public money is given to an organisation that undertakes any commercial operation. State Aid is defined as an advantage in any form whatsoever conferred on a selective basis to undertakings by public authorities. Subsidies granted to individuals or general measures open to all enterprises are not covered by the State Aid prohibition. Although the UK has now left the EU, successor arrangements have been implemented to meet the UK's international obligations on subsidy control.

The general parameters of the scheme will not permit loans to be made where the funding could be used in the delivery of commercial activities. However, not for profit organisations often undertake commercial activities in order to support the delivery of non-commercial activities. State aid can be avoided by using the Market Economy Operator (MEO) principles. If the state is acting in a way that a rational private investor would, for example in providing loans or capital on terms that would be acceptable to a genuine private investor who is motivated by return and not policy objectives, then it is not providing State Aid. This is because the beneficiary is not considered to be obtaining an advantage from the State but on the same terms that it could have obtained on the open market.

The actual interest rate charged on loans of this nature will be set with reference to the minimum permitted within State Aid rules at the time of fund advance and the Council's cost of borrowing plus an appropriate credit risk margin, whichever is higher. If there is any doubt as to whether State Aid may be an issue, legal advice must be sought.

Loan Framework

- All loans must be secured against an asset or guaranteed by a public sector organisation with tax raising powers.
- The maximum loan to value will not exceed 80% unless fully guaranteed by a public sector body.
- The maximum duration of the loan will be 30 years, but the loan period must not exceed the useful life of the asset.
- An independent valuation of the asset upon which the loan is secured will be undertaken by the Council.
- A robust business case must be developed that demonstrates that the loan repayments are affordable.
- The on-going value of the asset(s) that the loan has been secured against will be valued on a 5-year basis. A charge to revenue may be required if the equity value falls below the debt outstanding or if it becomes clear that the borrowing organisation is unable to service the debt.
- Guarantees will be called upon if the lending organisation falls into arrears of more than 12 months.

Given the administrative costs incurred in both establishing and managing loans of this nature, an administration/arrangement fee will be applied to each loan made. The following arrangement fees will be applied:

Minimum Loan Value	Maximum Loan Value	Arrangement Fee
£10,000	£119,999	£1,200
£120,000	£289,999	1% of loan
£290,000	-	£2,950

Exemptions

Exemptions to this policy may be considered, but any exemption will need to be approved by S&R Committee.