CYNGOR SIR *POWYS* COUNTY COUNCIL.

FULL COUNCIL

7th March 2019

REPORT AUTHOR: **County Councillor Aled Davies**
Portfolio Holder for Finance

SUBJECT: **TREASURY MANAGEMENT STRATEGY STATEMENT & ANNUAL INVESTMENT STRATEGY**

REPORT FOR: **Decision**

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1. Introduction

1.1 This Treasury Management Strategy Statement and Annual Investment Strategy report is a requirement of the CIPFA Code of Practice on Treasury Management and a requirement under the Local Government Act 2003. It has regard to the Guidance on Local Government Investments issued by the Welsh Government which requires the Treasury Management Strategy Statement and Annual Investment Strategy to be approved by Full Council.

1.2 The report requires an appropriate strategy for borrowing and investing for the financial year 2019/20 and details the expected activities of the Treasury function.

1.3 The Strategy will be monitored throughout the year and will be revised for approval by Full Council if there are any significant changes necessary due to such things as the following:-

- updates in legislation/guidance
- changes in the economy/financial outlook which may affect the Authority's Strategy
- changes in the financial position of the Authority.

2. Background

2.1 The Council is required to operate a balanced budget which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned with cash being available when it is needed. Surplus cash is invested.
The second main function of the treasury management service is the funding of the Council's capital plans. These plans provide 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 involves arranging short or long-term loans or using longer-term cash flow surpluses.

The contribution the treasury management function makes to the authority is critical as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects.

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

Revised reporting is required for 2019/20 due to the revisions of the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a capital strategy to provide a longer-term focus on the capital plans and greater reporting requirements surrounding any commercial activity undertaken. The capital strategy is being reported separately.

3. <u>CIPFA Code of Practice on Treasury Management and Prudential Code</u>

3.1 In December 2017 CIPFA issued a revised TM Code of Practice and a revised Prudential Code. CIPFA issued a statement that accepted that the issue of revised codes at a late stage of the 2018-19 budget cycle made it very difficult for most authorities to fully implement both codes. Accordingly, full implementation was not expected until 2019-20.
It is a requirement of the Code that this Authority formally adopts the key principles of the Code. This was done by Cabinet on 14^{th} February 2012 (see Appendix B). The 2017 revised Code made no changes to these key principles.

3.2 The Code emphasises a number of key areas including the following:-

i. All authorities must formally adopt the revised Code
ii. The strategy report will affirm that the effective management and control of risk are prime objectives of the Authority's treasury management activities
iii. The Authority's appetite for risk must be clearly identified within the strategy report and will affirm that priority is given to security of capital and liquidity when investing funds and explain how that will be carried out
iv. Responsibility for risk management and control lies within the organisation and cannot be delegated to any outside organisation
v. Credit ratings should only be used as a starting point when considering risk. Use should also be made of market data and information, the quality financial press, information on government support for banks and the credit ratings of that government support
vi. Authorities need a sound diversification policy with high credit quality counterparties and should consider setting country, sector and group limits
vii. Borrowing in advance of need is only to be permissible when there is a clear business case for doing so and only for the current capital programme or to finance future debt maturities
viii. The main annual treasury management reports must be approved by Cabinet/Full Council
ix. There needs to be, at a minimum, a mid-year review of treasury management strategy and performance. This is intended to highlight any areas of concern that have arisen since the original strategy was approved

x. Each Authority must delegate the role of scrutiny of treasury management strategy and policies to a specific named body
xi. Treasury management performance and policy setting should be subject to scrutiny prior to implementation
xii. Members should be provided with access to relevant training
xiii. Those charged with governance are also personally responsible for ensuring they have the necessary skills and training
xiv. Responsibility for treasury management activities must be clearly defined within the organisation
xv. Officers involved in treasury management must be explicitly required to follow treasury management policies and procedures when making investment and borrowing decisions on behalf of the Authority.

3.3 The Authority will adopt the following reporting arrangements in accordance with the Code of Practice:-

Report/Document	Committee	Frequency
Treasury Management Policy Statement and Practices	Audit Committee followed by Cabinet	When changes require
Treasury Management Strategy and Annual Investment Strategy	Full Council	Annually before the start of financial year
Treasury Management Quarterly Reports	Audit Committee followed by Cabinet	Quarterly
Treasury Management Annual Review	Audit Committee followed by Cabinet	Annually by 30th Sept after the end of financial year

4. Economic Background and Forecasts

4.1 The economic background is attached at Appendix C. The information contained therein is considered in the formulation of this Treasury Management Strategy Statement and Investment Strategy.

4.2 The most recent forecast of interest rates for 2019/20 by the Authority's advisor is:

	Jun19	Sep19	Dec19	Mar20	Jun20	Sep20	Dec20
Bank rate	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%
5yr PWLB	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%
10yr PWLB	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%
25yr PWLB	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%
50yr PWLB	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%

At its February 2019 meeting the Bank of England Monetary Policy Committee held bank rate at 0.75%. On the assumption that Parliament and the EU agree a Brexit deal, the next increase is forecast for May 2019 followed by increases in February and November 2020.

Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK and the question of a deal or no deal Brexit. As such, the above forecasts (and MPC decisions) will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year.

5. Borrowing Strategy

5.1 The Authority's Capital Financing Requirement (CFR) is the amount of capital expenditure that is not financed from revenue resources, capital grants and other contributions and capital receipts. Any expenditure that is not financed from these resources increases the authority's underlying need to borrow. Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through external borrowing or utilising temporary cash resources within the Council.

The Authority is currently maintaining an under borrowed position. This means that the capital borrowing need (the Capital Financing Requirement) has not been fully funded with loan debt as cash supporting the Authority's reserves, balances and cashflow has been used as a temporary measure. This is a prudent and cost effective approach in the current economic climate of low interest rates and is a good use of the Council's cash. However, members will be aware that internal borrowing is only a temporary situation and officers have advised that, based on capital estimates, it would be necessary for the Authority to borrow at some stage. £37.9m of longer term borrowing has taken place in 2018/19 year to date. Further long-term borrowing of circa £30m is expected to take place before the end of the 2018/19 financial year.

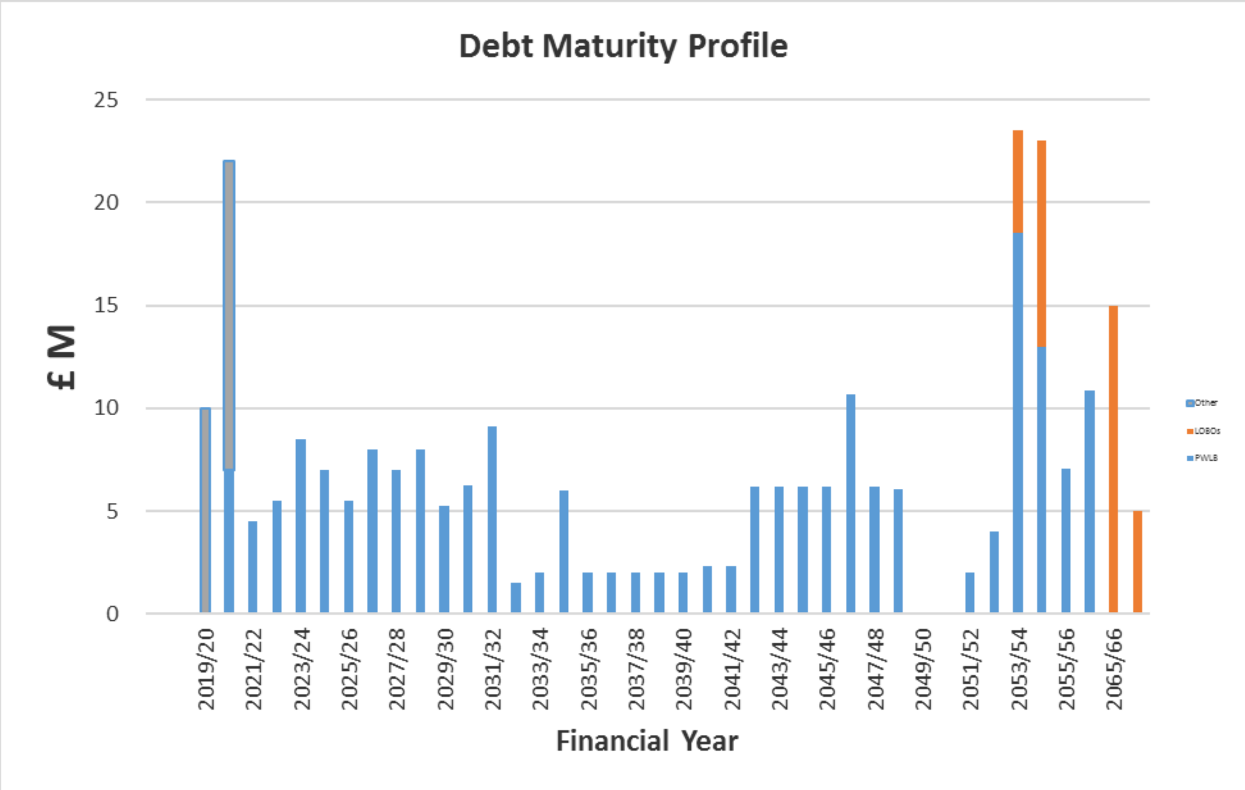
The Authority's estimated closing Capital Financing Requirement (CFR) for 2018/19 is £401.5m. If no further borrowing takes place within the remainder of the current financial year, the outstanding debt at 31st March 2019 will be £279.2m showing that the Authority is still under borrowed well below its CFR. The approved Capital budget for 2019/20 is £92.3m. £42.2m of this is financed by Prudential Borrowing.

5.2 PWLB Certainty Rate:

In 2012-13, the Government introduced a 20 basis points (bps) discount on loans from the Public Works Loan Board (PWLB) under the prudential borrowing regime for those principal local authorities providing improved information and transparency on their locally-determined long-term borrowing and associated capital spending plans. The Government said it would also work with the local authority sector to consider the potential for an independent body to facilitate the provision of PWLB lending at a reduced rate to authorities demonstrating best quality and value for money. This certainty rate continues to be available and this Authority has registered its interest in this preferred rate option.

5.3 Estimated Debt Maturity Profile as at 01.04.19:

(please click on the graph below and increase the percentage in the View option of the toolbar above for an enhanced view)



Members will see that the debt maturity profile is fairly even across the years. This maturity profile has been managed as such, so as to ensure that there is no undue preponderance in any particular year which may put the Authority's financing and cashflow position at risk.

6. <u>Debt Rescheduling</u>

6.1 The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt, which was compounded on 20th October 2010 by a considerable further widening of the difference between new borrowing and repayment rates, has meant that PWLB to PWLB debt restructuring is now much less attractive than before both of these events.

6.2 However, as short term borrowing rates will be considerably cheaper than longer term rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of any debt repayment i.e. premiums incurred.

The reasons for any rescheduling to take place will include:

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

6.3 All rescheduling will be reported to Cabinet as soon as is practicable.

7. Policy on borrowing in advance of need

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

8. Investments

8.1 *Investment Policy:*

8.1.1 The Authority's investment policy has regard to the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code") and the Welsh Government Guidance on Local Government Investments. This guidance places a high priority on the management of risk.

8.1.2 The Authority's investment priorities are: -

(a) the security of capital
(b) the liquidity of its investments
(c) yield

8.1.3 The Authority will aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite of this Authority has been low in order to give priority to security of its investments.

8.1.4 The borrowing of monies purely to invest or on-lend and make a return is unlawful and this Authority will not engage in such activity.

8.1.5 The minimum amount that is to be held during the financial year in investments other than long-term is Nil.

8.2 Definition of Investments – Specified and Non-Specified:

8.2.1 The Local Government Act 2003 refers to specified and non-specified investments. The Welsh Government's Guidance on Local Government Investments defines specified and non-specified investments.

Specified Investments are those with a high level of credit quality and subject to a maturity limit of one year.
Non-specified investments are those for periods in excess of one year; those with less high credit quality; and/or are more complex instruments which require greater consideration before being authorised for use.

8.3 Creditworthiness policy:

8.3.1 This Authority uses the creditworthiness service provided by Link Asset Services although the Authority has adopted a position that is slightly more risk averse than Link's suggested list in respect of counterparties and durations.

8.3.2 Link uses a sophisticated modelling approach with credit ratings from all three main rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays: -

- credit watches and credit outlooks from credit rating agencies
- CDS (credit default swap) spreads to give early warning of likely changes in credit ratings
- sovereign ratings to select counterparties from only the most creditworthy countries.

This approach is in line with the CIPFA Code of Practice which states that "credit ratings should only be used as a starting point when considering credit risk". Authorities should also use financial press, market data, information on government support for banks and the credit ratings of that government support.

8.3.3 Link's modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes can be used by the Authority to determine the suggested duration for investments and are therefore referred to as durational bands:-

- Yellow - 5 years
  for UK Government debt or its equivalent, Money Market Funds and collateralised deposits where the collateral is UK Government debt
- Dark pink - 5 years
  for Ultra-Short Dated Bond Funds with a credit score of 1.25
- Light pink - 5 years
  for Ultra-Short Dated Bond Funds with a credit score of 1.5
- Purple - 2 years
- Blue - 1 year
  only applies to nationalised or semi nationalised UK Banks
- Orange - 1 year
- Red - 6 months
- Green - 100 days
- No Colour - not to be used

8.3.4 The TM Code of Practice advises that authorities have regard for all the ratings issued by all three main agencies and to make their decisions based on all ratings. The advisors' creditworthiness service corresponds with this as it uses the ratings from all three agencies but, by using a scoring system, does not give undue preponderance to just one agency's ratings.

8.4 "High" credit quality:

8.4.1 It is proposed that the Authority continue with the following in respect of defining a "high" credit quality. If a rating is not available from any of the rating agencies then the available ratings will be used.

Long Term Ratings (in respect of long-term investments):

Permitted Fitch Ratings	Permitted Moody's Ratings	Permitted S&P Ratings
AAA	Aaa	AAA
AA+	Aa1	AA+
AA	Aa2	AA
AA-	Aa3	AA-

Short Term Ratings (in respect of short-term investments):

Permitted Fitch Ratings	Permitted Moody's Ratings	Permitted S&P Ratings
F1+	N/A	A-1+
F1	P-1	A-1

8.4.2 All credit ratings will be monitored daily. The Authority is alerted to changes to ratings of all three agencies through its use of the advisors' creditworthiness service.

8.4.3 Any institution which drops below any of the above ratings will be removed from the Authority's counterparty list for investments. Any investments held with the counterparty will also be reviewed in order to establish whether the premature maturity of the investment should be sought.

8.4.4 In addition to the use of Credit Ratings the Authority will also be advised of information in movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Authority's investment list. Any investments held with the counterparty will also be reviewed in order to establish whether the premature maturity of the investment should be sought.

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

8.5 Country limits:

8.5.1 It is proposed that the Authority will use approved counterparties from the UK and approved counterparties from other countries with the following sovereign credit ratings:-

Permitted Fitch Ratings	Permitted Moodys Ratings	Permitted S&P Ratings
AAA	Aaa	AAA

The list of countries (excluding the UK) that qualify using this credit criteria, as at the date of this report, are shown in Appendix D. This list will be added to or deducted from by officers should ratings change.

8.5.2 Our advisor's view is that all Authorities should avoid a concentration of investments in too few counterparties or countries but that a suitable spreading approach in itself is likely to be sufficient given the safeguards already built into its creditworthiness service.

As such the following limits are proposed:-

Country	**Maximum Investment per Country**	**Credit Rating/Other Assessment of Risk**
AAA countries (listed at Appendix C)	£20M (held in call accounts)	As per rating list
UK	No Maximum Investment	As per rating list

8.6 Group/Institutions - Counterparty Criteria/Limits:

<u>Specified Investments:</u>

The current limits per the 2018/19 Strategy are as follows:-

Institution	**Maximum Investment per Group/Institution £M**	**Maximum Length**	**Credit Rating/Other Assessment of Risk**
UK Banks	20 (a maximum £10M to be held in fixed term investments)	Up to 364 days	As per Link's matrices and the Authority's definition of a high credit rating
Foreign Banks	5	Up to 364 days	As per Link's matrices and the Authority's definition of a high credit rating
Other Local Authorities	25	Up to 364 days	N/A

As the Authority may be holding higher levels of cash for short-term periods, it is proposed that the following limits are in place for 2019/20:-

Institution	Maximum Investment per Group/Institution £M	Maximum Length	Credit Rating/Other Assessment of Risk
UK Banks	30	Up to 364 days	As per Link's matrices and the Authority's definition of a high credit rating
Foreign Banks	5	Up to 364 days	As per Link's matrices and the Authority's definition of a high credit rating
Other Local Authorities	25	Up to 364 days	N/A

Non-Specified Investments:

The current limits per the 2018/19 Strategy are as follows:-

Institution	Maximum Investment per Group/Institution £M	Maximum Length	Credit Rating/Other Assessment of Risk
UK Banks	10 (£5M limit with any one institution)	Up to 2 years	As per Link's matrices and the Authority's definition of a high credit rating
Foreign Banks	2	Up to 2 years	As per Link's matrices and the Authority's definition of a high credit rating
Money Market Funds (max. of 5)	10	N/A	All are AAA rated
Other Local Authorities	10	Up to 5 years	N/A
Note: Limits for Specified and Non-Specified are combined limits. The maximum limit will also apply to a banking group as a whole.			

It is proposed that these limits remain the same for 2019/20.

9. Investment Strategy

9.1 In-house funds*:*
The majority of the Authority's in-house managed funds are cash flow derived.

9.2 Investment returns area likely to remain relatively low during 2019/20. Bank rate is forecast to increase steadily over the next few years to reach 2.00% by Qtr 1 2022.
The suggested budgeted investment returns from the Authority's advisors for investments up to 3 months are:

2019/20	1.00%
2020/21	1.50%

Members should be aware that these returns may not be achieved when cash levels are low and hence being kept in liquid accounts.

9.3 The Authority currently has no investments that are longer-term.

10. Policy on the use of external service providers

10.1 The Authority currently uses Link Asset Services as its external treasury management advisors. This contract was awarded following a competitive process and runs to 31st August 2021.

10.2 The Authority recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed on external service providers.

10.3 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 Authority 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. This review will incorporate assessing the following:-

- level of technical expertise/advice
- appropriateness of advice given
- value of information provided i.e. market commentaries, forecasts, etc.
- value of training given
- attendance at meetings

11. Scheme of delegation

11.1 (i) Full Council

- approval of annual strategy

(ii) Audit Committee

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

(iii) Cabinet

- receiving and reviewing reports on treasury management policies, practices and activities
- approval of amendments to the Authority's adopted clauses, treasury management policy statement and treasury management practices
- budget consideration and approval
- approval of the division of responsibilities

- receiving and reviewing regular monitoring reports and acting on recommendations
- approving the selection of external service providers.

12. Role of the section 151 officer (Chief Financial Officer)

12.1 The S151 officer will have responsibility for:

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers

The 2017 Code introduced a major extension of the functions of this role, especially in respect of non-financial investments (which CIPFA has defined as being part of treasury management).

These functions are:-

- 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 the 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, to include the following:-

  - risk management including investment and risk management criteria for any material non-treasury investment portfolios

  - performance measurement and management including methodology and criteria for assessing the performance and success of non-treasury investments

  - decision making, governance and organisation, including a statement of the governance requirements for decision making in relation to non-treasury investments and arrangements to ensure that appropriate professional due diligence is carried out to support decision making

  - reporting and management information, including where and how often monitoring reports are taken

  - training and qualifications, including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.

13. Treasury Management Training

13.1 The Authority recognises that relevant individuals will need appropriate levels of training in treasury management due to its increasing complexity. There are two categories of relevant individuals: -

- treasury management staff employed by the Authority
- members charged with governance of the treasury management function.

13.2 All treasury management staff should receive appropriate training relevant to the requirements of their duties at the appropriate time. All treasury management staff are required to be members of an appropriate professional body and, in line with the continuing professional development requirements of these professional bodies, the Authority operates a Professional Development Review system which identifies the training requirements of individual members of staff engaged on treasury related activities. Additionally, training is also provided in the job and it is the responsibility of the s151 officer to ensure that all staff under his/her authority receive the level of training appropriate to their duties.

13.3 Details of Approved Training Courses

Treasury management staff and members will go on courses provided by our treasury management advisors, CIPFA, etc.

13.4 Records of Training received by Treasury Staff

As required by their relevant professional bodies, treasury management staff will maintain records of training they receive.

13.5 Approved Qualifications for Treasury Staff

It is the Authority's policy that the Treasury Manager and the Technical Accountancy Assistants are qualified to at least AAT level.

13.6 Members

The CIPFA Code of Practice states that members charged with governance (all members as the annual strategy requires approval by Full Council) have a personal responsibility to ensure that they have the appropriate skills and training for their role. To aid this, the Authority normally holds two briefing sessions per year for members and members should ensure that they attend at least one of these each year.

14. Pension Fund Cash

The Authority will comply with the requirements of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009, which were implemented on 1st Jan 2010. The Pension Fund has its own bank accounts although, due to use of the Authority's financial systems, a small amount of pension fund cash remains pooled with the Authority's cash balances for investment purposes. Any investments made by the pension fund directly with this local authority will comply with the requirements of SI 2009 No 393.

15. Treasury Management Budget

A requirement of the Authority's Treasury Management Policy Statement is that a summary treasury management budget is included in the Strategy report. This is attached at Appendix E.

16. CIPFA Prudential Code - Prudential and Treasury Indicators

16.1 The following indicators, required by the CIPFA Prudential Code, are included as part of the annual budget report :-

- authorised limit for external debt
- operational boundary for external debt

- actual external debt

16.2 Prudential and Treasury Indicators are relevant for the purposes of setting an integrated treasury management strategy and, as such, the indicators required to be included as part of this strategy are as follows:-

16.3.1 *Interest Rate Exposure:*

The setting of upper and lower limits for interest rate exposures has the effect of creating ranges within which the Authority will limit its exposure to both fixed and variable interest rate movements.

The current limits are as follows:-

Fixed rates	140%
Variable rates	60%

As dictated by the Code of Practice, this indicator for fixed and variable limits is calculated by looking at the net position between debt and investments.

It is proposed that the limits above remain the same for 2019/20.

16.3.2 Maturity Structure of Borrowing:

Local authorities are exposed to the risk of having to refinance debt at a time in the future when interest rates may be volatile or uncertain. This indicator is designed to assist authorities in avoiding large concentrations of fixed rate debt that has the same maturity structure and would therefore need to be replaced at the same time. It is recommended that the Authority sets upper and lower limits in each period as a percentage of its total borrowings.

The current limits are as follows:-

	Upper Limit	Lower Limit
Under 12 months	40%	0%
12 months to 2 years	40%	0%
2 years to 5 years	40%	0%
5 years to 10 years	40%	0%
10 years to 20 years	40%	0%
20 years to 30 years	40%	0%
30 years to 40 years	40%	0%
40 years to 50 years	40%	0%

It is proposed that the limits above remain the same for 2019/20.

16.3.3 Principal sums invested for periods longer than 364 days:

This indicator is used to demonstrate that the Authority has taken into account all the resources available for investment. This is to minimise the possibility that longer-term investments will need to be realised early which might have disadvantageous results. This indicator is also used to demonstrate that the

Authority is not borrowing more than it needs to, or in advance of its needs, purely to profit through investment from the extra borrowing.

The current limit is set at £10M.

It is proposed that this limit remains at £10M for 2019/20.

Proposal

It is proposed that Council approves the Treasury Management Strategy Statement and Annual Investment Strategy.

Statutory Officers

The s151 officer has made the following comment:

"The Treasury Management Strategy Statement and Annual Investment Strategy forms a key part of the Council`s overall approach to borrowing and investments. The report ensures the authority complies with relevant legislation and the Code of Practice on Treasury Management."

The Solicitor to the Council (Monitoring Officer) has made the following comment:

"I have nothing to add to the report."

Future Status of the Report

Not applicable

Recommendation:		**Reason for Recommendation:**	
That Council approves the Treasury Management Strategy Statement and Annual Investment Strategy		**Statutory Requirement**	
Relevant Policy:		Treasury Management Policy	
Within Policy:	**Y**	**Within Budget:**	**Y**
Person(s) To Implement Decision:		**Ann Owen – Treasury Manager**	
Date By When Decision To Be Implemented:			**1st April 2018**

Contact Officer Name:	Tel:	Fax:	Email:
Ann Owen	01597 826327	01597 826290	ann.owen@powys.gov.uk

Background Papers used to prepare Report:

CIPFA Code of Practice on Treasury Management and Cross Sectoral Guidance Notes
Treasury Management Policy Statement
Advisors' Information
WAG Guidance on Local Government Investments 2010

Appendix A:

Treasury Management Policy Statement

1. This organisation defines its treasury management activities as: “The management of the authority’s borrowings, 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”.

2. This organisation 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. 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.

3. This organisation acknowledges 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 B:

1. This Authority adopts the key principles of CIPFA's *Treasury Management in the Public Services : Code of Practice (2011 Edition),* as described in Section 4 of that Code as follows:-

   Key Principle 1:
   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.

   Key Principle 2:
   Their policies and practices should make clear that the effective management and control of risks 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.

   Key Principle 3:
   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.

   In framing these recommendations, CIPFA acknowledges the difficulties of striving for effective risk management and control, whilst at the same time pursuing value for money. This code does not seek to be prescriptive about how this issue should be handled, particularly since it covers such a wide variety of organisations. However, where appropriate, the sector specific guidance notes give suitable advice. CIPFA recognises that no two organisations in the public services are likely to tackle this issue in precisely the same manner but success in this area of treasury management is likely to be viewed, especially in value for money terms, as an indicator of a strongly performing treasury management function.

   Even though it dates back to 1991, CIPFA considers that the report by the Treasury and Civil Service Committee of the House of Commons on the BCCI closure is still pertinent, wherein it was stated that:

   In balancing risk against return, local authorities should be more concerned to avoid risks than to maximise returns.

   Indeed this view was supported by the Communities and Local Government Select Committee report into local authority investments in 2009.
   It is CIPFA's view that throughout the public services the priority is to protect capital rather than to maximise return. The avoidance of all risk is neither appropriate nor possible. However, a balance must be struck with a keen responsibility for public money.

2. Accordingly, the Authority will create and maintain, as the cornerstones for effective treasury management:

   - a treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities

   - suitable treasury management practices (TMPs) setting out the manner in which the Authority will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

   The content of the policy statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of the Authority. Such amendments will not result in the Authority materially deviating from the Code's key principles.

3. The Authority will also have regard for the Guidance on Local Government Investments issued by the Welsh Assembly Government and effective from 1st April 2010.

4. Full Council will receive the annual strategy report as recommended in the Welsh Assembly Guidance on Local Government Investments and the Authority's Cabinet will receive reports on its treasury management policies, practices and activities, including, as a minimum, a mid-year review and an annual report after its close, in the form prescribed in its TMPs.

5. The Authority delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to the Cabinet, and for the execution and administration of treasury management decisions to the Chief Financial Officer, who will act in accordance with the Authority's policy statement and TMPs and, if he/she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

6. The Authority nominates Audit Committee to be responsible for ensuring effective scrutiny of treasury management policies, practices and performance.

Appendix C:

ECONOMIC BACKGROUND

GLOBAL OUTLOOK:

World growth has been doing reasonably well, aided by strong growth in the US. However, US growth is likely to fall back in 2019 and, together with weakening economic activity in China and the Eurozone, overall world growth is likely to weaken. Inflation has been weak during 2018 but, at long last, unemployment falling to remarkably low levels in the US and UK has led to an acceleration of wage inflation. The US Fed has therefore increased rates nine times and the Bank of England twice. However, the ECB is now probably unlikely to make a start on raising rates in 2019.

KEY RISKS:

Central bank monetary policy measures:

Looking back on more than ten years since the financial crash of 2008 when liquidity suddenly dried up in financial markets, it can be assessed that central banks' monetary policy measures to counter the sharp world recession were successful. The key monetary policy measures they used were a combination of lowering central interest rates and flooding financial markets with liquidity, particularly through unconventional means such as quantitative easing (QE), where central banks bought large amounts of central government debt and smaller sums of other debt.

The key issue now is that the period of stimulating economic recovery and warding off the threat of deflation is coming towards its close. A new period is well advanced in the US, and started more recently in the UK, of reversing those measures i.e. by raising central rates and, (for the US), also reducing central banks' holdings of government and other debt. These measures are now required in order to stop the trend of a reduction in spare capacity in the economy and of unemployment falling to such low levels, that the re-emergence of inflation is viewed as a significant risk. It is, therefore, crucial that central banks get their timing right and do not cause shocks to market expectations that could destabilise financial markets. In particular, a key risk is that, because QE-driven purchases of bonds drove up the price of government debt and therefore caused a sharp drop in income yields, this also encouraged investors into a search for yield and into investing in riskier assets such as equities. Consequently, prices in both bond and equity markets rose to historically high valuation levels simultaneously. This meant that both asset categories were exposed to the risk of a sharp downward correction and we did, indeed, see a sharp fall in equity values in the last quarter of 2018 and into early 2019. It is important, therefore, that central banks only gradually unwind their holdings of bonds in order to prevent destabilising the financial markets. It is also likely that the timeframe for central banks unwinding their holdings of QE debt purchases will be over several years.

UK: 2018 was a year which started with weak growth of only 0.1% in quarter 1. However, quarter 2 rebounded to 0.4% followed by quarter 3 being exceptionally strong at +0.6%. Quarter 4, however, was depressed by the Brexit uncertainty and came in at only +0.2%, (1.3% y/y). Growth is likely to continue being weak until the Brexit situation clears.

The MPC has stated that future Bank Rate increases would be gradual and they have given a figure for this of around 2.5% in ten years' time but have declined to give a medium term forecast. However, with so much uncertainty around Brexit, the next move could be up or down, even if there was a disorderly Brexit.

Inflation - the Consumer Price Index (CPI) measure of inflation has been falling from a peak of 3.1% in November 2017 to 1.8% in January 2019. In the February Bank of

England quarterly Inflation Report, inflation was forecast to still be marginally above its 2% inflation target two years ahead given a scenario of minimal increases in Bank Rate.

The **labour market** figures in November were particularly strong with an emphatic increase in total employment of 141,000 over the previous three months, unemployment at 4.0%, a 43 year low on the Independent Labour Organisation measure, and job vacancies hitting an all-time high, indicating that employers are having major difficulties filling job vacancies with suitable staff. It was therefore unsurprising that wage inflation continued at its high point of 3.3%, (3 month average regular pay, excluding bonuses). This means that in real terms, (i.e. wage rates less CPI inflation), earnings are currently growing by about 1.2%, the highest level since 2009. This increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. This tends to confirm that the MPC was right to start on a cautious increase in Bank Rate in August as it views wage inflation in excess of 3% as increasing inflationary pressures within the UK economy.

In the **political arena**, the Brexit deal put forward by the Conservative minority government was defeated in a vote in the House of Commons on 15 January and its motions were again defeated on 14 February. Prime Minister May is currently seeking some form of modification or clarification from the EU of the Irish border backstop issue. Our advisors' central position is that the Government will endure, despite various setbacks along the route to reaching an orderly Brexit, although the risks are increasing that it may not be possible to get full agreement by the UK and EU before 29 March 2019, in which case this withdrawal date is likely to be pushed back to a new date. If, however, the UK faces a general election in the next 12 months, this could result in a potential loosening of monetary and fiscal policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up.

USA: President Trump's massive easing of fiscal policy is fuelling a (temporary) boost in consumption which has generated an upturn in the rate of strong growth which rose from 2.2% (annualised rate) in quarter 1 to 4.2% in quarter 2 and 3.5%, (3.0% y/y), in quarter 3, but also an upturn in inflationary pressures. The strong growth in employment numbers and an unemployment rate of 4.0%, near to a recent 49 year low, has fed through to an upturn in wage inflation which hit 3.2% in December. However, CPI inflation overall fell to 1.9% in December and looks to be on a falling trend to continue below the Fed's target of 2% during 2019. The Fed has continued on its series of increases in interest rates with another 0.25% increase in December to between 2.25% and 2.50%, which was the fifth increase in 2018 and the ninth in this cycle. However, they dropped any specific reference to expecting further increases at their January 30 meeting. The last increase in December compounded investor fears that the Fed could overdo the speed and level of increases in rates in 2019 and so cause a US recession as a result. There is also much evidence in previous monetary policy cycles of the Fed's series of increases doing exactly that. Consequently, we have seen stock markets around the world falling under the weight of fears around the Fed's actions, the trade war between the US and China and an expectation that world growth will slow. Since the more reassuring words of the Fed in January, equity values have recovered somewhat. The tariff war between the US and China generated a lot of heat during 2018; it could significantly damage world growth if an agreement is not reached during the current three month truce declared by President Trump to hold off from further tariff increases.

Eurozone: Growth was 0.4% in quarters 1 and 2 but fell back to 0.2% in quarters 3 and 4 (1.2% y/y). Germany only narrowly avoided slipping into recession in quarter 4 whereas

Italy did slip into recession. The trend of economic statistics is now indicating that growth is likely to weaken further in 2019. This will make it difficult for the ECB to make any start on increasing rates until 2020 at the earliest. Indeed, the issue now is rather whether the ECB will have to resort to new measures to boost liquidity in the economy in order to support growth. Having halved its quantitative easing purchases of debt in October 2018 to €15bn per month, the European Central Bank ended all further purchases in December 2018. In its January meeting, it made a point of underlining that it will be fully reinvesting all maturing debt for an extended period of time past the date at which it starts raising the key ECB interest rates.

China: Economic growth has been weakening over successive years despite repeated rounds of central bank stimulus and medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity, the stock of unsold property and to address the level of non-performing loans in the banking and credit systems. Progress has been made in reducing the rate of credit creation which is feeding through into lower economic growth but there are concerns that official economic statistics are inflating the published rate of growth.

Japan has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy. It is likely that loose monetary policy will endure for some years yet to try to stimulate growth and modest inflation.

Emerging countries: Argentina and Turkey are currently experiencing major problems and are facing challenges in external financing requirements well in excess of their reserves of foreign exchange. However, these countries are small in terms of the overall world economy, (around 1% each), so the fallout from the expected recessions in these countries will be minimal.

Appendix D:

Approved Countries for Investment

AAA

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

Appendix E:

Summary Treasury Management Budget

	2019/20 £	2018/19 £
Employees	165,000	165,000
Transport	1,250,450	1,266,450
Supplies and Services	200,000	200,000
Interest Paid	14,845,370	12,699,120
Debt Management Expenses	6,000	6,000
Gross Expenditure	**16,466,820**	**14,336,570**
Interest Received	0	0
Gross Income	**0**	**0**
Net Expenditure	**16,466,820**	**14,336,570**

Notes:

- Transport is the Authority's leasing costs – leasing is classified as a Treasury Management activity.

- Supplies and Services includes the following main items:-

  Dr/Cr card and bank charges 175k
  Treasury /Leasing Advice 17k

- Interest Received has no budget as cash balances have significantly reduced. Any interest received in respect of cash surpluses may need to be used to offset borrowing costs for negative cash balances.