Dear Councillor

EXECUTIVE - MONDAY, 4 FEBRUARY, 2019

Please find attached updated the appendices related to the Treasury Management Strategy Item Monday 4 February, 2019 meeting of the Executive, forwarded to Members under separate cover.

This document will also be considered at the Council meeting to be held on the 27 February 2019, please bring this document to either meeting if you are attending.

Agenda No	Item
6	**TREASURY MANAGEMENT STRATEGY 2019/20** **(Pages 1 - 30)**

Yours sincerely

This page is intentionally left blank

BLACKPOOL COUNCIL

REPORT

of the

DIRECTOR OF RESOURCES

to the

EXECUTIVE

on

4 FEBRUARY 2019

TREASURY MANAGEMENT STRATEGY 2019/20

---

1. Purpose

1.1 The Council is required by statute to publish an annual Treasury Management Strategy incorporating its Borrowing and Investment Strategies. It is also required to prepare a Capital Strategy incorporating both strategic investments for economic regeneration as well as more detailed capital plans for effective service delivery. The Council's Capital Strategy is the subject of a separate report and will be presented to the Executive and then to Full Council with the Treasury Management Strategy.

1.2 In essence the Treasury Management Strategy is an annual plan of how Blackpool Council will manage its investments and cashflows. It identifies the Council's borrowing needs and shows how it will invest temporary surplus cash balances, and how it will control its banking, money market and capital market transactions.

1.3 The Scale of Operations at Annex A shows the levels of capital expenditure, borrowing and temporary investments and also the impact that spending on new capital schemes, strategic investments and economic regeneration activities have on affordability levels.

2. Definition

2.1 CIPFA defines Treasury Management as *"The management of the organisation's borrowing, investments and cashflows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".*

3. Background

3.1 Blackpool's Capital Programme for 2019/20–2021/22 continues to focus to schemes which will help to improve the economic wellbeing and prosperity of Blackpool and the surrounding area. Capital grants received from central government remain at a low level but the Council is using low cost borrowing to invest in regeneration. Total cash moving annually through the Council's bank account including the re-investment of temporary cash surpluses and re-borrowing of temporary cash shortfalls is expected to be over £900m in the current year.

3.2 Large capital regeneration schemes such as the continuing rollout of the Central Business District, the extension of the Tramway to Blackpool North Station and the new Conference Centre are in a mature stage of development. Other large schemes are also expected to progress with the Council focusing on those projects which will help grow the economy and prosperity within the town.

3.3 The Treasury Management Panel, which comprises the Director of Resources, Chief Accountant and representatives from Corporate Finance and Blackpool Coastal Housing, has the responsibility for managing the risks associated with treasury management activities on an operational basis. The Panel recognises the need to balance investment risk against achieving an acceptable return on temporary surplus cash balances. The balance sought is to maximise the security and liquidity of the Council's investments, with higher yields being obtained only where they are consistent with those desired levels of security and liquidity.

4. Objectives

4.1 The objectives of the Treasury Management Strategy are as follows:

- To set the framework for the Council's treasury management operations
- To manage the Council's investments and cashflows
- To control banking, money market and capital market transactions
- To plan and secure appropriate borrowing in order to finance the requirements of the Capital Strategy at the lowest overall cost to the Council
- To achieve the best rates of return from the investment of temporary surplus cash balances commensurate with risk, subject to the overriding principle of maintaining an acceptable level of security
- To monitor and control effectively the risks associated with these transactions
- To comply with appropriate codes and regulations including the International Financial Reporting Standards as they apply to Treasury Management.

4.2 In delivering the above objectives the Council is required to:

- Determine its own borrowing limits taking into account its financial situation, long-term plans and in particular what it thinks is affordable now and sustainable in the future

- Monitor its borrowing limits using performance measures called Prudential indicators, these are set out in detail in Annex E to this report

- Consider annual and six-monthly reports on Treasury Management which contain Prudential indicators.

5. Economic Outlook

5.1 The outlook for the UK economy continues to be uncertain as the UK Government continues negotiations with the European Union on the terms of its future trade relationship with other EU countries. The resulting uncertainty means continuing risk and so it is important that the Council's treasury and investment affairs continue to be managed in a cautious and prudent manner.

5.2 The interest rate environment continues to be difficult but the Bank of England expects that interest rates will continue to remain low in the foreseeable future. In an effort to control the threat of inflation to the UK economy the Bank of England increased the base rate on the 3rd August 2018 from 0.50% to 0.75%. The rate had been at this level since November 2017 and it was only the second increase in the last 10 years. The Bank of England anticipates that there may be further gradual increases by the end of 2019. Money market investment rates for temporary surplus cash balances increased following the base rate rise and are expected to remain at present levels. The current rate for a three-month fixed-term deposit with a high street bank is typically 0.65% and analysts anticipate that this may increase in line with further base rate increases during the period covered by this report.

5.3 Long-term borrowing rates, influenced by gilt yields, are generally stable but they have risen gradually during the last 12 months. Rates which are typically priced at UK gilt yield plus 80 basis points have increased by 0.1% to just over 2.6%. Market expectations are that the increase in rates will continue during the next 12 months.

6. Treasury Management Strategy - Key Principles

6.1 A summary of the key principles upon which the strategy is based is set out below and is expanded in more detail in Annex B:

- Temporary investments will be restricted to UK Banks and Building Societies unless non-UK institutions satisfy the stringent requirements set out in the Investment Counterparty and Liquidity Framework (Annex D, paragraph 2.4).

- Short-dated Gilts (UK government securities with a life of less than one year) will continue to form part of our approved list of investments.

- Fixed-term cash deposits are currently restricted to terms of not more than three months (subject to review by the Treasury Management Panel).

- Temporary cash surpluses will continue to be applied to reduce the Council's need to borrow.

- New long term borrowing to support capital expenditure will only be taken in favourable conditions. We are a registered shareholder in the Municipal Bond Agency, which entitles us to borrow from them if the Treasury Management Panel considers them to be competitive.

- The Treasury Management Panel will remain alert to market intelligence through the financial press, contacts in the financial markets and our contacts in other local authorities.

- Treasury management advisers will only be engaged on an ad-hoc basis, retaining responsibility in-house for all treasury management activities.

- Long-term debt will be repaid in advance of redemption date where there is demonstrable financial advantage to the Council.

- The Policy for allocating borrowing costs to the HRA for 2019/20 and future years will be the same as in previous years and will be based on the HRA share of the Capital Financing Requirement (HRACFR). The charge will be made up of the interest payable on long-term loans in the HRA pool and an additional charge or credit where the HRA pool of loans is either below or above the HRACFR.

- Prudentially funded capital schemes will be charged a Minimum Revenue Provision (MRP) and interest at the pooled borrowing rate for the General Fund except in exceptional circumstances when the Director of Resources deems it appropriate to use an alternative rate. In cases where the interest rate is lower than the pooled rate there must be clear evidence that the use of the lower rate is affordable. The policy on charging Minimum Revenue Provision is set out in Annex F. This policy is reviewed annually.

6.2 During the last 12 months the Council borrowed £8m in long-term loans. Whilst temporary borrowing rates are low the Treasury Management Panel will continue to use temporary loans as its preferred source of finance. A switch to long-term borrowing is made in order to protect the margin and when the interest rate environment is favourable.

6.3 When the Council makes business loans, it takes into account its own cost of borrowing, the likelihood of future interest rate movements, the risks of the venture and any state aid implications in ensuring that it at least covers its own costs.

6.4 Capital spending has been financed by using internal balances and by using short-term loans which continue to be available at very low interest rates

6.5 A revised Treasury Management Code (the Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes) was issued in December 2017. This report follows its requirements and full details are set out in the Annex B.

6.6 The Council's approach to the implementation of the revised Prudential and Treasury Management Codes is in line with the statement issued by CIPFA's Treasury and Capital Management Panel on the 21 December 2017.

7. Recommendations

The Executive is asked to recommend to Council that it:

i) Approves the Treasury Management Strategy 2019/20 including both the Borrowing and Investment Strategies which are set out in Annex C and Annex D to this report;

ii) Adopts the Treasury Management Policy Statement, three key principles and four clauses taken from the Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes (2017 Edition) and set out in Annex B to this report,

iii) Approves the revised Prudential Indicators and Limits for 2018/19 and the new Prudential Indicators and Limits for 2019/20 - 2021/22 which are set out in Annex E to this report; and

iv) Approves the Minimum Revenue Provision Policy Statement for 2019/20, which will ensure a prudent Minimum Revenue Provision charge in the annual statement of accounts. The policy is set out within Annex F to this report.

S THOMPSON

DIRECTOR OF RESOURCES

This page is intentionally left blank

TREASURY MANAGEMENT STRATEGY 2019/20

ANNEX A – Scale of Operations

==

Capital Expenditure - The projected capital expenditure - presented here in order to show the complete treasury position - and for which approval is separately requested in the Capital Programme 19/20 – 21/22 Report is expected to be:

Capital expenditure £M	2018/19 Revised	2019/20 Programme	2021/21 Programme	2021/22 Programme
Non-HRA programme	43	37	38	6
HRA programme	8	9	9	3
Sub total	51	46	47	9
Business Loans Fund	20	50	50	0
Total	71	96	97	9

Debt Requirement - Part of the capital expenditure programme will be financed directly through government grants, capital receipts etc. This leaves a residue which will increase the Council's external borrowing requirement (its Capital Financing Requirement [CFR]). The General Fund CFR is reduced each year by a statutory revenue charge for the repayment of debt. The HRA is under no requirement to make such a charge.

Capital Financing Requirement £M	2018/19 Revised	2019/20 Programme	2020/21 Programme	2021/22 Programme
Non-HRA	392	500	568	556
HRA	11	11	11	11
Total	403	511	579	567

Against this borrowing need (the CFR), the Council's expected external debt position for each year (the **Operational Boundary**) and the maximum amount it can borrow (the **Authorised Limit**) are:

£M	2018/19 Revised	2019/20 Projection	2020/21 Projection	2021/22 Projection
Authorised Limit	403	511	579	567
Operational Boundary	369	488	552	538

Affordability Prudential Indicators – Actual and estimates of the ratio of financing costs to net revenue stream. This indicator identifies the trend in the cost of capital (borrowing costs net of investment income) against the net revenue stream:

%	2018/19 Revised	2019/20 Programme	2020/21 Programme	2021/22 Programme
Non-HRA	12.0%	15.1%	15.6%	15.9%
HRA	4.0%	4.0%	4.0%	4.0%

Investments - The value of resources applied to finance the capital spend above is one of the elements which influence the Council's overall resources. The expected position of the Council's year-end resources (capital reserves, capital receipts, etc.), is shown below. This is supplemented with the expected cashflow position to provide an overall estimate of the year-end investment position. The Prudential Indicator identifying the ability to invest longer term is also shown.

£M	2018/19 Revised	2019/20 Projection	2020/21 Projection	2021/22 Projection
Total resources	-	-	-	-
Working capital	-	-	-	-
Temporary borrowing	(148)	(264)	(324)	(300)
Sums invested > 364 days	-	-	-	-

This page is intentionally left blank

TREASURY MANAGEMENT STRATEGY 2019/20

ANNEX B – Treasury Management Policy Statement 2019/20 - 2021/22

1. Introduction

1.1 Treasury management is undertaken in accordance with the CIPFA Code of Practice for Treasury Management in the Public Services ("the TM Code"). This Code has been reviewed and updated following recent developments in the marketplace and the introduction of the Localism Act 2011 for English local authorities. The updated code was issued in December 2017 with a requirement that it should be fully implemented by the 1st April 2019.

2. Key Principles – the Code identifies three key principles:

2.1 The Council 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.

2.2 The Council's policies and practices should make clear that the effective management and control of risk are prime objectives of its treasury management activities and that responsibility for these lies clearly within it. The Council's appetite for risk should form part of its 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 portfolio liquidity when investing treasury management funds.

2.3 The Council acknowledges that the pursuit of value for money in treasury management, and the use of suitable performance measures, are valid and important tools to employ in support of business and service objectives; and that within the context of effective risk management, treasury management policies and practices should reflect this.

3. Clauses Formally Adopted

3.1 The Council adopts the following four clauses recommended by CIPFA:

1. This Council will create and maintain, as cornerstones of its 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 Council 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 TM Code, subject only to amendment where necessary to reflect the particular circumstances of this Council. Such amendments will not result in the Council materially deviating from the TM Code's key principles.

2. The Council's Executive will receive reports on its treasury management policies, practices and activities, including as a minimum, an annual

strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMPs. The annual strategy is reported to Full Council.

3. The Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to the Treasury Management Panel, and for the execution and administration of treasury management decisions to the Director of Resources (Section 151 Officer), who will act in accordance with the Council's policy statement and TMPs, and as a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

4. The Council nominates the Tourism, Economy and Resources Scrutiny Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

4. Treasury Management Policy Statement

4.1 In accordance with the TM Code, the Council defines treasury management activities as:

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

4.2 'Investments' in the definition above covers all the financial assets of the Council, as well as other non-financial assets which the Council holds primarily for financial returns, such as investment property portfolios. This may therefore include investments which are not managed as part of normal treasury management or under treasury management delegations. All investments require an appropriate investment management and risk management framework under the Treasury Management Code.

4.2 The Council 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.

4.3 Further details about the Council's approach to borrowing are included in Annex C, and in respect of its approach to investments are included in Annex D and the separate Capital Strategy Report for 2019/20.

TREASURY MANAGEMENT STRATEGY 2019/20

ANNEX C – Borrowing Strategy

1. Introduction

1.1 The Borrowing Strategy is prepared in accordance with a professional code of practice (the CIPFA Code of Practice and Cross-Sectoral Guidance Notes on Treasury Management – 2017 Edition).

1.2 It includes the following:

- The Council's debt and investment projections (section 2).
- The expected movement in interest rates (section 3).
- The Council's borrowing strategy (section 4).
- The Council's policy on borrowing in advance of need (section 5).
- The Council's approach to debt rescheduling (section 6).
- The Council's Lender Option Buyer Option (LOBO) strategy (section 7).

2. Debt and Investment Projections 2019/20 – 2021/22

2.1 The borrowing requirement comprises the expected movement in the Capital Financing Requirement (CFR in the table below) and any maturing debt which will need to be re-financed. The table below shows this effect on the treasury position over the next three years. It also highlights the expected change in investment balances:

£'000s	**2018/19 Revised**	**2019/20 Projection**	**2020/21 Projection**	**2021/22 Projection**
External Debt				
Long-term debt at 1 April	92,225	94,526	98,909	106,802
Repaid debt	(5,699)	(5,617)	(2,107)	(7,107)
Replacement of maturing debt	-	-	-	-
Additional long-term debt	8,000	10,000	10,000	20,000
Long-term debt at 31 March	**94,526**	**98,909**	**106,802**	**119,695**
Short-term debt at 31 March	149,000	264,314	323,759	299,567
PFI and Other Liabilities	90,305	87,559	84,775	81,954
Total external debt at 31 March	**333,831**	**450,782**	**515,336**	**501,216**
Annual change in debt	**3,117**	**116,951**	**64,554**	**(14,120)**
Investments				
Total investments at 31 March	(1,000)	-	-	-
Investment change	**8,050**	**1,000**	**-**	**-**
Change in debt less investment	11,167	117,951	64,554	(14,120)
Annual change in CFR (annex E 3.3)	**13,769**	**108,305**	**67,338**	**(11,299)**

2.2 The additional long-term debt includes any borrowing in advance and catch-up borrowing. The related impact of the above movements on the revenue budget are:

£'000s	2018/19 Revised	2019/20 Projection	2020/21 Projection	2021/22 Projection
Revenue Budget				
Interest on long-term loans	4,497	7,941	8,291	8,991
Interest on short- term loans	1,050	1,485	3,238	2,996
Total Interest Cost	**5,547**	**9,426**	**11,529**	**11,987**
General Fund long-term borrowing cost	5,164	9,028	11,131	11,589
HRA long-term borrowing cost	383	398	398	398
Investment income/Internal Financing	(3)	(444)	(444)	(444)

3. Expected Movements in Interest Rates

3.1 The Bank Base Rate is forecast to remain at 0.75% until the 4th quarter of 2019 when it may increase slowly to 1.40% by the 4th quarter of 2021. Bank Rate forecasts made by the Office of Budget Responsibility in November 2018 are as follows:

- 2018/19 0.75%
- 2019/20 1.10%
- 2020/21 1.30%
- 2021/22 1.40%

3.2 Market expectations of Long Term Interest Rates are estimated to be:

PWLB Certainty Borrowing Rates				
Indicative %	**5 Year**	**10 Year**	**25 Year**	**50 Year**
2018/19 (actual January 2019)	1.70	2.05	2.61	2.48
2019/20	1.90	2.35	2.91	2.78
2020/21	2.10	2.65	3.10	2.98
2021/22	2.30	2.80	3.30	3.10

3.3 These assumptions have been used to determine the treasury management budget projections, included as part of the 2019/20 revenue budget and future year projections.

3.4 The interest rate environment continues to be uncertain but the Bank of England expects that interest rates will continue to remain at low levels throughout the period covered by this report. In an effort to control the threat of inflation on the UK economy the Bank of England increased the base rate on the 3rd August 2018 from 0.50% to 0.75%. The rate had been at this level since November 2017 and it was only the second increase in the previous 10 years. Money market investment rates for temporary surplus cash balances increased following the base rate rise and are expected to remain at present levels. The current rate for a three-month fixed-term deposit with a high street bank is typically 0.65% and analysts anticipate that this may increase marginally during the next 12 months.

3.5 Long-term borrowing rates, influenced by gilt yields, are generally stable but they have increased gradually during the last 12 months. Rates which are typically priced at UK Gilt plus 80 basis points have increased by 0.1% to just over 2.6%. Market expectations are that the increase in rates will continue during the next 12 months.

4. Borrowing Strategy

4.1 The Council borrows for one of two purposes – to finance cash flow in the short-term or to fund capital investment over the longer term. The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully financed with either long term loans or with temporary borrowing. Instead part of the Capital Financing Requirement has been financed using the Council's reserves and cash balances. This strategy is prudent as investment returns are low and there is a plentiful supply of inexpensive short term finance currently available in the market.

4.2 A key aim of the Borrowing Strategy is to minimize the cost of the Council's loan portfolio whilst ensuring that the obligation to repay loans is matched with the benefit received from expenditure incurred on the capital programme.

4.3 The average rate of interest on the Council's loan portfolio is currently 2.15%, which is one of the lowest rates of the CIPFA group of authorities that we compare ourselves to. The achievement of such low rates ensures the Council benefits from the best value for money in terms of its borrowing. This is the result of a number of years proactively managing the portfolio on loans through restructuring and taking advantage of inexpensive short term borrowing. The borrowing strategy will continue with this successful approach.

4.4 The approved sources of long-term and short-term borrowing will be:

- Public Works Loan Board
- UK Local Authorities
- Municipal Bond Agency (see paragraph 4.7 below for further details)
- Any institution approved for investments

4.5 As stated above in paragraph 3.4, the interest rate environment continues to be uncertain and the Bank of England expects that interest rates will continue to remain at low levels throughout the period covered by this report. The Treasury Management Panel, under delegated powers, will take the most appropriate form of borrowing in this uncertain economic environment depending on the prevailing interest rates at the time.

4.6 In order to secure the lowest cost of borrowing Blackpool Council has agreed to disclose estimates of its capital transactions including new borrowing and planned capital expenditure for the next three years to Her Majesty's Treasury. The disclosure of this information in summary format entitles the Council to receive a 20 basis point discount on all new loans borrowed from the Public Works Loan Board during the next 12 months. The information provided to Her Majesty's Treasury is updated annually.

4.7 Along with other local authorities the Council became a shareholder in the Municipal Bond Agency (MBA). The council saw this as a viable alternative to borrowing from the PWLB. However, the failure of the MBA to issue its first bond in the market means that it is currently unable to provide any form of finance to local authorities.

5. Policy On Borrowing In Advance Of Need

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

5.2 In determining whether borrowing will be undertaken in advance of need the Council will:

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio, which supports the need to take funding in advance of need;
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered;
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
- consider the merits and demerits of alternative forms of funding;
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use;
- consider the impact of borrowing in advance (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk and the level of such risks given the controls in place to minimise them. Any risks arising will be reported via the mid-year or annual reporting mechanism.

6. Debt Rescheduling

6.1 The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt (which has now been compounded since 20 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 these events. In particular, consideration would have to be given to the large premiums, which would be incurred by prematurely repaying existing PWLB loans and it is very unlikely that these could be justified on value for money grounds if using replacement PWLB refinancing. However, some interest savings may still be achievable through using other local authority loans and market loans in rescheduling exercises rather than using PWLB borrowing as the source of replacement financing.

6.2 As short term borrowing rates are currently considerably cheaper than longer term fixed interest 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 debt repayment (premiums incurred).

6.3 The reasons for any rescheduling to take place will include:

(a) The generation of cash savings and / or discounted cash flow savings;
(b) Help fulfil the borrowing strategy outlined above;
(c) Enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

6.4 Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

6.5 Any decision taken on rescheduling existing long term debt will be made by the Treasury Management Panel.

7. Lender Option Borrower Option debt (LOBOs)

7.1 LOBOs typically carry a cheaper initial rate of interest than new debt available from other sources. They are structured with an initial period in which a fixed rate of interest is paid, followed by a much longer 'variable' period. During this period at the agreed 'call' dates (typically between every six months to every five years) the Lender has the option to increase the interest rate. If the Lender exercises their Option to increase the rate, the Borrower has the Option to repay the debt.

7.2 When general interest rates are rising, the interest the Council pays on its LOBOs will tend to ratchet up at call dates, lagging just below other available market rates. The higher rate chosen by the lender is always likely to be enticingly below other immediately available market rates so that at the decision points when the borrower has the option to repay, it will be seduced into a longer relationship with the LOBO at higher rates. However, when general interest rates are falling, the interest the borrower pays on its LOBOs will remain fixed at the higher rates.

7.3 The Treasury Management Panel notes that whenever a lender calls an increase in the rate of a LOBO there will be a great temptation to accept the higher rate and remain tied into the LOBO (as the alternative borrowing is likely to be slightly more expensive in the short term). The Council will continue to take advantage of the beneficial rates available through LOBOs as part of a balanced portfolio of fixed and variable debt, especially through the early fixed period of the instrument.

7.4 The Council's policy is that on every occasion when a lender opts to increase the interest rate on one of its LOBOs there is a presumption that the Council will repay the LOBO.

7.5 In view of the recent bad press on LOBO's the Treasury Management Panel is looking for ways to redeem them whenever favourable opportunities arise.

This page is intentionally left blank

1. Introduction

1.1 This Investment Strategy covers the following:

- Treasury Management Investments and the Council's investment and counterparty liquidity framework (section 2)
- The Treasury Investment Strategy for 2019/20 – 2021/22 (section 3)
- The Council's power to invest for Treasury Management purposes (section 4)

2. Treasury Management Investments

2.1 The primary principles of security and liquidity, governing the Council's day to day treasury management activity are set out in the Statutory Guidance on Local Government Investments (3rd Edition) issued on the 2nd February 2018. The yield or return on investments is of secondary importance.

2.2 To achieve sufficient liquidity in its investments, guidelines will be used to determine the maximum periods for which funds may prudently be committed. These also apply to the Council's Prudential Indicators covering the maximum principal sums invested.

2.3 In relation to security, a policy will be applied to the categories of investment, the choice of investment counterparties with adequate security, and the monitoring of their security. This is set out in the Specified and Non-Specified investment sections below.

2.4 The Treasury Management Panel will maintain a counterparty list in accordance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to those which determine Specified and Non-Specified investments, as it selects which counterparties the Council will choose rather than defining what its investments are. The criteria are based on information from Fitch, Moody's and Standard & Poors, the three principal credit ratings agencies.

(i) **Banks** - the Council will use banks which have at least the following Fitch or equivalent ratings from Moody's and Standard & Poors:
- Short Term - F1 from Fitch or equivalent from Moody's or Standard & Poors.
- Long Term - Single A from Fitch or equivalent from Moody's or Standard & Poors.
- Individual / Financial Strength – C from Fitch or Moody's or the equivalent from Standard & Poors
- Support - 3 from Fitch or the equivalent from Moody's or Standard and Poors

(ii) **Bank Subsidiary and Treasury Operations** - the Council will use these where the parent bank has the necessary ratings outlined above. The investment limit to be applied will be calculated across the whole group.

(iii) **Building Societies** - the Council will use any United Kingdom Society with assets in excess of £1.5 billion.

(iv) **Local Authorities** - The Council will use upper-tier authorities only.

(v) **Investment in the UK Government** (including short-term gilts and sterling treasury bills) are permitted because of their overall security.

(vi) **Investment in Money Market Funds** are not permitted.

(vii) **Non-UK Exposure Limits** - The Treasury Management Panel may impose overall sector or country limits to restrict the level of exposure within non-UK financial institutions. The Panel has no short-term plans to start investing in non-UK financial institutions, but it can foresee the possibility in future years covered by the Strategy when it may invest up to 25% of temporary cash investments in non-UK financial institutions which satisfy the criteria in (i) above and whose sovereign government rating is triple A according to Fitch or the equivalent from Moody's or Standard & Poors.

2.5 It is not considered necessary to apply different maximum time limits for investing with different counterparties according to their precise credit rating. Institutions are either on the list of potential counterparties for any timescale (subject to the overriding restriction of 364 days or less) or they are not on the list at all. The Treasury Management Panel has placed a temporary 3-month time limit on deposits placed with all Banks and Building Societies on its counterparty list.

2.6 The proposed criteria for Specified and Non-Specified investments are shown in section 4 for approval.

2.7 In the normal course of the Council's cash flow operations it is expected that only Specified Investments will be utilised for the control of liquidity.

2.8 The use of longer-term instruments (greater than one year from inception to repayment) would fall in the Non-Specified Investment category. These instruments will not be used for the control of liquidity. This will also be limited by the investment Prudential Indicator below.

3. Investment Strategy 2019/20 – 2021/22

3.1 In Managing the Council's treasury operations on a day-to-day basis, the Treasury Management Panel is more concerned to avoid risks than to maximise returns.

3.2 The Treasury Management Panel currently operates a restriction of 3 months or less on all fixed term deposits placed with those counterparties included in paragraph 2.4 (i), (ii), (iii), (iv) and (v). It also considered it necessary to restrict temporary fixed-term investments to UK Banks and Building Societies and those subsidiaries of non-UK financial institutions which are incorporated in the UK. However, as market conditions improve the Panel is likely to lift these restrictions and extend the term of temporary investment back to a maximum of 364 days. Moreover, the Treasury Management Panel may invest up to 25% of temporary cash investments in non-UK financial institutions which satisfy the requirements set out in paragraph 2.4 (vii).

3.3 The Bank of England base rate determines the level of interest which can be earned on short term cash surpluses arising in normal day to day treasury activities. Following the base rate increase on the 3rd August 2018 from 0.50% to 0.75%, a typical three month deposit rate increased to 0.65%. Deposit rates are expected to remain at present levels throughout 2019 and then increase in tandem with future base rate increases in 2020. The Council's investment decisions are based on comparisons between the current low level of interest rates and the market's expectation of gradual increases during the period covered by this report. As a result it is likely that investment decisions will continue to be made for shorter periods until investment rates start to rise after 2020. However, the overriding principle is to maintain sufficient security and liquidity within the cash balances and a shorter profile of temporary investments will help achieve this. The Treasury Management Panel, under delegated powers, will undertake the most appropriate form of investments based on current market conditions as surplus funds become available. The three-month time limit for temporary investments will continue during 2019 but may be relaxed in future years covered by this Strategy. The current restrictions are explained in more detail in paragraph 3.2 above.

4. Power To Invest

4.1 Blackpool Council has the power to invest:

(i) for any purpose relevant to its functions under any enactment, and
(ii) for the purposes of the prudent management of its financial affairs.

This includes investments which are not directly linked to statutory functions but are simply made in the course of treasury management. This allows for the temporary investment of funds borrowed for the purpose of expenditure in the reasonably near future.

4.2 Speculative borrowing in order to invest in the course of day to day treasury management activities is unlawful.

4.3 The speculative purchase and subsequent disposal of property is generally also unlawful. However, there may be occasions when such purchase and resale are necessary as part of a strategic development. This is permitted only where this is part of an approved project plan which is covered by proper statutory powers in pursuance of the Council's approved objectives. Examples of this are in the pursuit of delivery of projects related to Blackpool's regeneration strategy - such as the planned phases of the Central Business District and the development of land near the Airport.

4.4 Priority is to be given to the security of investments and then to liquidity. The highest rate of return (yield) can only be sought once officers are satisfied that the principal sums invested are secure.

4.5 The Council is planning to expand its Business Loans Fund further with the aim to promote, develop and support local businesses and public sector partners within the Blackpool area. Before any lending is authorised the Loans Panel (which includes the Chief Executive, Director of Communications and Regeneration and Director of Resources) supported by both Accountancy and Legal, will analyse and validate the business case for each loan.

4.6 No other types of (Non-Specified) investments are identified as being permissible, other than those explicitly allowed as share or loan capital under paragraph 4.7.

4.7 Investments in share or loan capital are restricted to shareholdings in Blackpool Transport Services Ltd., Blackpool Operating Company Ltd., Blackpool Entertainments Company Ltd, Blackpool Housing Company Ltd, Regional and City Airports (Blackpool) Holdings Ltd and Blackpool Waste Services Ltd. The guidance defines acquisition of share or loan capital in a corporate body as capital or revenue expenditure (rather than as an investment).

4.8 Further details about how the Council manages the risks and rewards coming from its Business Loans Fund and from its investments in subsidiary companies, referred to above in paragraphs 4.5 and 4.7 above, are explained in more detail in its Capital Strategy.

This page is intentionally left blank

PRUDENTIAL INDICATORS

1. Background and Summary

1.1 The Local Government Act 2003 requires the Council to adopt the CIPFA Prudential Code for Capital Finance in Local Authorities (2017 Edition) and agree Prudential Indicators. This report revises the Indicators for 2018/19, 2019/20, 2020/21 and introduces new Indicators for 2021/22. Each indicator either summarises the expected activity or introduces limits upon the activity and reflects the outcome of the Council's underlying capital appraisal systems.

2. Capital expenditure plans

2.1 The Council's capital expenditure plans are reported and recommended for approval in the Capital Programme 2019/20 and are summarised below. This forms the first of the Prudential Indicators. This expenditure can be paid for immediately (by resources such as capital receipts, capital grants, etc.), but if resources are insufficient any residual expenditure will need to be borrowed.

2.2 A certain level of capital expenditure will be grant supported by the Government; anything above this level will be unsupported and will need to be paid for from the Council's own resources.

2.3 The key risks to the plans are that the level of Government support has been estimated and is therefore subject to change. Similarly some estimates for other sources of funding, such as capital receipts, may also be subject to change over this timescale.

2.4 The Council is referred to the summary capital expenditure projections below, as reported in the Capital Programme 2019/20. This forms the first Prudential Indicator:

£'000s	2018/19 Revised	2019/20 Programme	2020/21 Programme	2021/22 Programme
Capital Expenditure:				
Non-HRA	42,781	36,689	37,760	5,583
HRA	7,589	9,086	8,535	2,669
Financed by:				
Capital receipts	(410)	(236)	(236)	(236)
Capital grants	(28,519)	(18,034)	(14,471)	(7,255)
Capital reserves	-	-	-	-
Revenue Contributions	(6,841)	(500)	-	-
Net financing need for the year: *(para 3.3)*	**14,600**	**27,005**	**31,558**	**761**

3. The Council's borrowing need (the Capital Financing Requirement)

3.1 The second Prudential Indicator is the Council's Capital Financing Requirement (CFR). The CFR is made up of the total outstanding capital expenditure which has not yet been paid for from either revenue or capital resources along with any business loans issued from the expanded Business loans Fund including loans made to Blackpool Housing Company. The expansion of the Business Loans Fund is explained in more detail in the Capital Strategy Report. The CFR is essentially a measure of the Council's underlying need to borrow.

3.2 The Council is required to pay off an element of the accumulated General Fund capital spend each year through a revenue charge known as the Minimum Revenue Provision (MRP). The overriding principle in calculating the MRP is that it must be prudent and this is covered in more detail in Annex F of this report.

3.3 The Council is asked to approve the CFR projections below:

£'000s	2018/19 Revised	2019/20 Programme	2020/21 Programme	2021/22 Programme
Capital Financing Requirement:				
CFR – Non Housing	383,955	410,160	522,948	559,359
CFR - Housing	11,363	11,363	11,363	11,363
Business Loans Fund	7,600	89,700	44,250	(3,460)
Total CFR	402,918	511,223	578,561	567,262
Movement in CFR	**13,769**	**108,305**	**67,338**	**(11,299)**

Movement in CFR represented by:				
Net financing need for the year: *(para 2.4)*	14,600	27,005	31,588	761
MRP/Voluntary Revenue Provision and other financing movements:	(8,431)	(8,400)	(8,500)	(8,600)
Business Loans Fund advances	10,000	94,400	50,000	0
Business Loans Fund repayments	(2,400)	(4,700)	(5,750)	(3,460)
Movement in CFR	**13,769**	**108,305**	**67,338**	**(11,299)**

3.4 In order to ensure that over the medium-term borrowing will only be taken for a capital purpose, the local authority should ensure that gross external borrowing does not, except in the short term, exceed the total of Capital Financing Requirement in the preceding year plus the estimates of any additional Capital Financing Requirement for the current and next two financial years. If in any of these years there is a reduction in the CFR, this reduction is ignored in estimating the cumulative increase in the CFR which is used for comparison with gross external borrowing. This is a key indicator of prudence.

4. The use of the Council's resources and the investment position

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

4.2 Any capital receipts and capital reserves available to finance capital expenditure during the period covered by the Treasury Management Strategy are shown in the table under paragraph 2.4 above.

5. Limits to borrowing activity

5.1 Within the Prudential Indicators there are a number of key indicators to ensure the Council operates its activities within well-defined limits.

5.2 For the first of these the Council needs to ensure that its total 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 2019/20 and the next two financial years.

Y/end positions £'000s	2018/19 Revised	2019/20 Projection	2020/21 Projection	2021/22 Projection
L/T borrowing	94,526	98,909	106,802	119,695
Short-term debt	149,000	264,314	323,759	299,567
PFI & Other Liabilities	90,305	87,559	84,775	81,954
Gross borrowing	333,831	450,782	515,336	501,216
CFR	402,918	511,223	578,561	567,262

5.3 The Director of Resources reports that the Council has complied with this Prudential Indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans and the proposals in next year's budget report.

5.4 A further two Prudential Indicators control or anticipate the overall level of borrowing:

5.5 **The Authorised Limit for external debt** - This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by Full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

5.6 **The Operational Boundary for external debt** - This indicator is based on the expected maximum external debt during the course of the year; it is not a limit. The Operational Boundary differs from the Authorised Limit in that it is based on expectations of the maximum external debt according to probable - not simply possible - events and is consistent with the maximum level of external debt projected by the estimates. The setting of this Operational Boundary is a matter of careful judgement. If it is set too high then it may be too near the Authorised Limit for there to be a margin sufficient to allow time to take corrective action before the Authorised Limit is breached. Alternatively, if it is set too low it will be breached so frequently that it will cease to act as a credible warning indicator. The intention therefore is that this operates as a form of early warning about certain cash-flow problems.

5.7 The Council is asked to approve the following Authorised Limit and Operational Boundaries, two indicators which are based on debt (including short-term) and are gross of investments.

Authorised Limit £'000s	2018/19 Revised	2019/20 Projection	2020/21 Projection	2021/22 Projection
Borrowing limit	310,000	420,000	491,000	482,000
Other long term liabilities limit	93,000	91,000	88,000	85,000
Total limit	403,000	511,000	579,000	567,000
Operational Boundary £'000s	**2018/19 Revised**	**2019/20 Projection**	**2020/21 Projection**	**2021/22 Projection**
Borrowing limit	278,000	399,000	466,000	455,000
Other long term liabilities limit	91,000	89,000	86,000	83,000
Total limit	369,000	488,000	552,000	538,000

5.8 The Authorised Limit is set by reference to the CFR and to allow for any potential peaks in temporary borrowing, since this will be counted against the overall borrowing. The Operational Boundary is set to equate to expected debt levels including normal day to day cash requirements.

6. Affordability Prudential Indicators

6.1 The previous sections cover the overall capital and control of borrowing Prudential Indicators, but within this framework Prudential Indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the overall Council's finances. The Council is asked to approve the following indicators:

6.2 Actual and estimates of the ratio 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.

%	2018/19 Revised	2019/20 Programme	2020/21 Programme	2021/22 Programme
Non-HRA	12.0%	15.1%	15.6%	15.9%
HRA	4.0%	4.0%	4.0%	4.0%

The estimates of financing costs include current commitments and the proposals in the Budget Report presented concurrently for approval.

7. Treasury Management Prudential Indicators, Limits on Activity and Attitude to Risk

7.1 Blackpool Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities is measured. It uses the Treasury Management Prudential Indicators as part of the risk control process to limit activity and monitor performance.

7.2 There are five treasury Prudential Indicators. The purpose of these Prudential Indicators is to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs. The indicators are:

7.3 **Gross debt and the Capital Financing Requirement (CFR)** - In order that over the medium-term, debt will only be taken for a capital purpose, the Council should ensure that external debt 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 the current and next two financial years. If in any of these years there is a reduction in the CFR, this reduction is ignored in estimating the cumulative increase in the CFR which is used for comparison with gross external debt. This is a key indicator of prudence.

7.4 **Upper limits on variable interest rate exposure** - This indicator identifies a maximum limit for variable interest rates based upon the debt position net of investments. In cases where the terms of the borrowing or investment raise questions as to whether it should be treated as fixed or variable, it is to be treated as variable for the purposes of these Prudential Indicators. We consider that this indicator is best calculated using the principal capital value rather than percentages.

7.5 **Upper limits on fixed interest rate exposure** - This indicator is similar to the previous indicator but covers a maximum limit on fixed interest rates.

7.6 **Maturity structures 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. They show the amount of projected borrowing that is fixed rate maturing in each period as a percentage of the total projected borrowing that is fixed rate.

7.7 **Total principal funds invested for over 365 days** - These limits are set to reduce the need for early sale of an investment and are based on the availability of funds after each year-end.

7.8 The Council is asked to approve the following Prudential Indicators (in the table below). Note that for each year, the upper limits on fixed interest rates equate to the expected Capital Financing Requirement for that year:

	2019/20	2020/21	2021/22
Gross debt (£M)			
	Upper	**Upper**	**Upper**
Gross Debt	451	515	501
Capital Financing Requirement	511	579	567
Interest rate exposures (£M)			
	Upper	**Upper**	**Upper**
Limits on fixed interest rates based on net debt	511	579	567
Limits on variable interest rates based on net debt	307	347	340
Maturity structure of fixed interest rate borrowing 2019/20 (%)			
		Lower	**Upper**
Under 12 months		-	18%
12 months and within 2 years		-	18%
2 years and within 5 years		-	30%
5 years and within 10 years		2%	60%
10 years and within 30 years		2%	70%
30 years and above		15%	90%
Total principal sums invested for over 364 days			
Principal sums invested for over 365 days	£ nil	£ nil	£ nil

This page is intentionally left blank

1. Minimum Revenue Provision (MRP) Strategy

1.1 Local authorities are required to set aside 'prudent' revenue provision for debt repayment (MRP) where they have used borrowing or credit arrangements to finance capital expenditure. Statutory Guidance covering Minimum Revenue Provision (MRP) was revised and updated in February 2018 by the Ministry of Housing Communities and Local Government (MHCLG) and applies to accounting periods on or after 1st April 2019. The guidance sets out various options and boundaries for calculating prudent provision which are set out in paragraph 1.5 below.

1.2 Local authorities can vary the MRP methodologies they use during the year and if they do so must present a revised MRP statement to the next full Council. Where a change would impact on the value of money assessment of non-financial investments the updated statement should summarise this impact.

1.3 Under the new guidance, where a change takes place the calculation of MRP under the new method should be based on the residual Capital Financing Requirement (CFR) at the point the change in method is made (i.e. it should not be applied retrospectively). Changing the method used to calculate MRP can never give rise to an overpayment in respect of previous years, and should not result in a local authority making a reduced charge or charge of £nil for the accounting period in which the charge is made, or in a subsequent period, on the grounds that it needs to recover overpayments of MRP relating to previous years.

1.4 Whilst 'prudent provision' is not specifically defined, the guidance suggests that debt ought to be repaid over a period that is either commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Revenue Support Grant, it is reasonably commensurate with the period implicit in the determination of the grant.

1.5 There are four options set out in the statutory guidance for determining the MRP:

Option 1 - Regulatory Method
Option 2 - The Capital Financing Requirement (CFR) Method
Option 3 - Asset Life Method (the MRP is determined by reference to the life of the asset either by equal instalments of principal or the annuity method)
Option 4 - Depreciation Method (MRP is equal to the provision required under depreciation accounting).

1.6 Options 1 and 2 may only be used in relation to capital expenditure incurred before 1st April 2008, which form part of its supported capital expenditure. For expenditure incurred on or after 1st April 2008, which does not form part of the authority's supported capital expenditure, prudent approaches include options 3 and 4.

1.7 Minimum Revenue Provision (MRP) Policy Statement for 2019/20 is as follows:

(i) In 2016/17 under the previous Statutory Guidance on MRP the Council changed its policy on all supported capital expenditure incurred prior to 1st April 2008 and for future supported capital expenditure, the MRP is based on the 2% straight line method, before making an adjustment for £24.1m, which is the difference between debt calculated under the prudential code (as at 1st April 2004) and debt calculated under the previous 'statutory' capital controls regime which commenced on 1st April 1990. This method is considered to be better than the previous method because it ensures that all the debt incurred prior to 1st April 2008 is repaid over a finite number of years. The method will continue to be used for 2019/20 and for future years.

(ii) For capital expenditure incurred after 1st April 2008 and financed by unsupported borrowing, the MRP will be based on option 3, the Asset Life Method. This method is considered both appropriate and prudent and will continue to be used in 2019/20.

(iii) In exceptional circumstances MRP for capital expenditure incurred after 1st April 2008 and which is funded by unsupported borrowing can be calculated using the Annuity Method (a variation allowed under option 3 of the 2018 Regulations). However, this method is only suitable for particular types of capital expenditure projects where the benefits are expected to increase in later years or where the income stream generated by the new project mirrors the Annuity profile. It may be particularly attractive in connection with projects promoting regeneration or administrative efficiencies where revenues will increase over time. This method may only be used if it receives approval by the Treasury Management Panel.

(iv) In the case of finance leases, where a right-of-use asset is on the balance sheet, and on balance sheet PFI contracts, the MRP requirement is by a charge equal the element of the rent/charge that goes to write down the balance sheet liability.

(v) Where on or after 1st April 2008 expenditure is incurred which is:

- Financed by borrowing or credit arrangements; and
- Treated as capital expenditure by virtue of either a direction under section 16(2)(b) of the 2003 Act or Regulation 25(1) of the 2003 Regulations,

MRP will be calculated in accordance with Option 3, the asset life method. The asset life used is set out in the table for the relevant expenditure type which is included in the Statutory Guidance on MRP (4th Edition) issued on 2nd February 2018.

(vi) In the case of investment properties where their acquisition has been partially or fully funded by an increase in borrowing or credit arrangements. MRP will be charged in accordance with option 3, the Asset Life Method.

(vii) In accordance with the Statutory Guidance no MRP will be charged on borrowing or credit arrangements used to finance capital expenditure on housing assets, to which Section 74(1) of the Local Government Housing Act 1989 applies.

(viii) The Council provides loans to wholly owned subsidiaries on a commercial basis. Under these arrangements, the cash advances are used by the companies to fund capital expenditure which in turn improves the standard of rented housing available in the local area and also improves the standard of local transport. These loans are funded by borrowing which in turn increases the Capital Financing Requirement (CFR). Loan repayments of principle are treated as a capital receipt and are available to be offset against the CFR. As a result there is no need to set aside MRP to repay the increased borrowing. The outstanding loans are reviewed on an annual basis and if necessary a provision for MRP will be made.

(ix) Including the business loans made to wholly owned subsidiaries above the Council's Business Loans Fund provides loan finance to businesses to help regenerate the local economy. The loans are made by the Council on a commercial basis and follow a comprehensive due diligence process, ensuring that recipients of the loans provide security against non-repayment and also have in place a valid and robust business plan. As with the loans to subsidiary companies, these third party loans are funded by borrowing which also increases the CFR. Loan repayments of principle are treated as a capital receipt and are available to be offset against the CFR. As a result there is no need to set aside MRP to repay the increased borrowing. The outstanding loans are reviewed on an annual basis and if necessary a provision for MRP will be made.

(x) The above policy will ensure that the Council satisfies the requirement to set aside a prudent level of MRP.

This page is intentionally left blank