Appendix G

East Hampshire District Council

Treasury Management Strategy, Minimum Revenue Provision Strategy and Annual Investment Strategy

1. The CIPFA Treasury Management Code of Practice

1.1 The Treasury Management and Investment Strategy has been set in accordance with the CIPFA Treasury Management Code of Practice 2011.

1.2 The Council is required to approve a Treasury Management Strategy which establishes the investment and borrowing activities for the Council. The Council's approach to Treasury Management is in accordance with the Cipfa Code of Practice, which requires a 3 year strategy to be agreed annually.

1.3 The Prudential Code for Capital requires the Council to set Prudential Indicators for Treasury Management and Capital Expenditure. These are linked to the Strategy and are set out at the end of this document.

1.4 The Council is also required to make an annual Policy statement on making Minimum Revenue Provision (MRP) for borrowing, together with the consideration of prudent provision in future financial years.

1.5 The Council delegates responsibility for the monitoring and scrutiny of treasury activity to the Governance, Audit & Scrutiny Committee, and delegates responsibility for implementing and administering the strategies, policy and procedures to the Chief Finance Officer. The Council also seeks external advice through Link Asset Services under the outsourced Finance function. A budget has been retained for strategic treasury advice for the retained client team.

2. Treasury Management Policy 2019/20

2.1 The Council's ambition to acquire property sites for strategic, operational and investment purposes will move the Authority into a net borrowing position. The proposed policy for managing borrowing to finance such expenditure is to borrow short term, or through the Public Works Loan Board, monitoring interest rates closely in order to switch to longer term fixed rate borrowing where analysis of market rates suggests this may be appropriate. The Council has utilised the Public Works Loan Board for strategic project investments since 2017/18 and for operational asset investments, including the Leisure Centre replacement programme, and will continue to do so.

2.3 Following the 0.25% increase in Base Rate in August 2018, market indications suggest that there could be further base rate increases in the short term as the Bank of England seek to mitigate increases in inflation that is currently being experienced.

Economic Factors

2.4 Factors that influence the Council's Treasury Management Strategy include the Council's overall level of resources, medium term spending plans and the need to finance the future cost of services. It is also influenced by the state of the economy in general, the outlook for interest rates and the credit risk environment.

2.5 The Treasury strategy is linked to the Council's medium term financial plans, and are reflected in a net interest cost or yield in the Council's budget. The net cost/yield estimates are updated regularly through the budget setting process and in year forecasting.

2.6 The Council's investment strategy gives scope to invest in approved instruments outlined in the approved lending/borrowing list (Schedule 3), but investments in banks and building societies are limited to high quality counterparties only.

Prudential Indicators

2.7 The Prudential Indicators were established as part of the Local Government Act 2003 through the Prudential Code. The Code requires the Council to produce indicators to demonstrate that capital financing is prudent, sustainable and affordable. The indicators are set out at the end of this document.

MRP Policy

2.8 The Council is required to calculate an amount in relation to its borrowing, and charge this amount as Minimum Revenue Provision to its Income & Expenditure Account in respect of borrowing repayment. The Policy is set out at Schedule 4 to the Treasury Management Strategy.

Officer Approval Limits

2.9 The power to approve the acquisition of properties meeting the Council's investment criteria be delegated to any Executive Director, in consultation with the Leader and the Section 151 Officer.

Risk Management

2.10 Minimising risk is a key aspect of treasury management activity. Risk is proactively managed with advice from Link Asset Services (formerly Capita Asset Services) and property investment decisions are subject to detailed business cases. As the Council moves towards a net borrowing position, interest rate exposure is an emerging risk and the timing of any move from short to long term borrowing is closely monitored.

2.11 The Finance Team carry out their duties in accordance with internal controls to ensure any day to day investment decisions are made in accordance with the Treasury Management Strategy.

2.12 The CFO reports on Treasury activity as part of the monthly financial monitoring.

2.13 The Governance, Audit & Scrutiny Committee will be responsible for the scrutiny of Treasury Management activity & practises.

SCHEDULE 1 – TREASURY MANAGEMENT STRATEGY

The Authority has adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code), which requires the Authority to approve a treasury management strategy before the start of each financial year. In addition, the Department for Communities and Local Government (CLG) issued revised Guidance on Local Authority Investments in February 2018 that requires the Authority to approve an investment strategy before the start of each financial year.

This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the CLG Guidance. The Authority is proposing to borrow substantial sums of money and, as a result, may be exposed to financial risks arising from changing interest rates.
The successful identification, monitoring and control of risk are therefore central to the Authority's treasury management strategy.

As part of the Provisional Settlement the Government launched a consultation into potential updates on Prudential Code and Treasury guidance, specifically to update it to reflect increasing use of borrowing to finance investment purchases. Updated guidance will not be released in time for the 2019/20 strategy, however once the revised guidance is available it will be reviewed and, if necessary, a revised Treasury Strategy will be produced during the financial year.

East Hampshire District Council's context

East Hampshire District Council has, as at 31st December 2018, £1.5M invested short-term (to mature within 12 months. There is external borrowing in place of £89M to fund capital expenditure on Leisure Centres and strategic property investment.

The underlying need to borrow is measured by the Council's Capital Financing Requirement (CFR). The CFR is anticipated to increase as a result of the Council's desire to build its investment property portfolio, and investment in Leisure facilities over the period of the Medium Term Financial Strategy (MTFS).

The current MTFS has modelled a further investment of £50M in the investment property portfolio in 2021/22 at the request of Cabinet. This is on the basis that funding would be through PWLB borrowing and therefore interest payments and MRP would be chargeable to the revenue budget. Before any decision is made to draw the monies down a full business case will be produced for Cabinet's approval.

In any event, once the current £200M has been borrowed, a full review of the investment property portfolio performance will be undertaken prior to any further increases. Therefore, no assumptions in relation to the £50M have been factored into the Prudential Indicators at this point in time.

Borrowing Strategy

The Council will adopt a flexible approach to borrowing in consultation with Treasury Management advisors, and will keep under review the following borrowing sources:

- Internal borrowing (borrowing against future revenue budgets)
- PWLB
- Other Local Authorities
- Finance Leasing
- Brokers for short term financing

Exposure to short dated/variable rate borrowing will be reviewed by reference to the difference between variable rate and longer term borrowing costs. A significant change in this difference will trigger a review of borrowing strategy to determine whether a switch to longer term rates is made or whether exposure to short term rates is maintained.

Capital Finance can also be raised through other debt liabilities, including Finance Leases, Private Finance Initiatives, Sale & Leaseback, or LGA Bonds. Any decision to raise finance through these methods will be subject to appraisal and a separate report to Cabinet.

The Council may take advantage of debt rescheduling (the repayment of loans before maturity to allow replacement with new loans) where it is expected to create a cost saving or significantly reduce interest rate risk to the Council.

Investment Strategy

The Council's overriding objective in relation to the investment of cash is the security of the capital invested, followed by the liquidity of investment. The Council aims to maximise yield given these parameters.

Investments are categorised as specified or non-specified investments. Specified investments are sterling denominated investments maturing under 1 year, and non-specified investments are effectively anything else.

The CFO has discretion to make investments outside of the Lending list on the advice of Link Asset Services. Institutions may be added or removed from the list if credit ratings improve or deteriorate below the thresholds outlined on the List.

Overnight funds are held in an overnight fund provided by the Council's bank. Consideration will be given to Money Market Funds in 2019/20 as an alternative to the overnight account, and may be utilised if the CFO is satisfied with the level of risk.

The Council will arrange short term investments through brokers, in order to ensure transactional security and to promote competition to enhance returns. The approved brokers are:

- ICAP Europe Ltd
- Prebon Marshall Yamane UK Ltd
- Tradition UK
- RP Martin

The Current Treasury Portfolio

The Council adopted a policy in previous strategies to transfer long term cash investments into property, building a balanced portfolio which balances returns with the Council's duty to maintain appropriate security and liquidity of public monies. Investment properties are revalued on an annual basis which may change the value reported. The expected value of these property investments at 31 March 2019 is:

Value as at 01/04/2017 £000's	Additions £000's	Revaluations £000's	**Value as at 31/03/2018 £000's**	**Additions £000's**	**Value as at 31/03/2019 £000's**
23,459	47,820	(957)	**70,322**	32,425	**102,747**

Interest Rate Forecasts

The Council formulates a view on interest rates as part of the budget setting process. This view is formulated on the basis of the Office for Budgetary Responsibility forecasts used for the Autumn Statement. The current view is that interest rates are likely to increase in 2019, and that increases beyond this would be incremental. Although there are inflationary pressures, and the weakening of Sterling since 2016, there is also uncertainty as to how Brexit negotiations will affect the wider economy. The annual FT survey on base rate expectations demonstrates a mixed view over when interest rates will change over the next 12 months. The table below details interest rate forecasts provided.

The table below details interest rate forecasts provided.

	2019/20				**2020/21**			
	Qtr 1	**Qtr 2**	**Qtr 3**	**Qtr 4**	**Qtr 1**	**Qtr 2**	**Qtr 3**	**Qtr 4**
OBR Forecast	1.0%	1.0%	1.0%	1.25%	1.25%	1.25%	1.5%	1.5%

It is important to note that although the base rate has changed, the rates that we can get on our investments are based on the London Interbank Offer rate, which fluctuates depending on other market factors. This explains the differing rates of return of our current investment portfolio.

Creditworthiness Policy

The Council monitors the creditworthiness of the counterparties used. The Council's lending list contains only counterparties of high credit quality. Credit quality is assessed through the size of the asset base of the counterparty, and the credit ratings awarded by independent credit rating agencies such as Fitch.

The asset base of counterparties is monitored on an annual basis when the Statement of Accounts for each counterparty is issued. Credit ratings are regularly monitored and are verified prior to investments being made.

Credit ratings of counterparties are available from credit agencies (Fitch, Standard & Poor, and Moody's). Advice on the credit worthiness of counterparties is also obtained from the Council's Treasury advisors.

If a counterparty on the current lending list is found to be of insufficient credit quality, the Council will not engage with that counterparty until it is satisfied that credit quality has improved. Treasury officers continue to monitor counterparties that are not currently on the lending list, and will add counterparties of high credit quality to the lending list in consultation with the Portfolio Holder for Finance.

The Council has not invested outside the United Kingdom since 2006, and currently no foreign counterparties are contained within the list (with the exception of Santander UK Plc, which is a UK bank under Spanish ownership). Foreign counterparties are monitored, and if sufficient credit quality is proved, may be added to the list in consultation with the Portfolio Holder for Finance.

Sole reliance will not be placed on credit ratings. The Council will continue to monitor reports in the press, market data and information on government support when reviewing credit worthiness. All counterparties on the long-term lending list are also covered by the government's Credit Guarantee Scheme.

All Long Term Investments will be carried out in consultation with the Finance Portfolio Holder and the S151 Officer.

Treasury Limits and Prudential Indicators 2017/18 to 2023/24

The revised CIPFA Code of Practice on Treasury Management and the Prudential Code for Capital Finance, in accordance with Section 3 of the Local Government Act 2003, require the Council to determine and review the level of borrowing that it can afford.

The Codes require a number of indicators to be formally set, on a rolling basis, for 2018/19 actuals and the following three years. The Council must have regard to the following when setting these indicators:

- Service Objectives
- Stewardship of Assets
- Value for Money
- Prudence and Sustainability
- Affordability and Practicality

The purpose of these indicators is to ensure that total capital investments and, in particular, the effect of these investments on the Council Tax level is 'acceptable'.

The Prudential Indicators set for 2019/20 are shown in Schedule 2 below. An explanation is provided for each indicator.

SCHEDULE 2 - PRUDENTIAL INDICATORS

1) Ratio of Financing Costs to Net Revenue Stream

The actual ratio for 2017/18, and estimated ratios for 2018/19 to 2022/23 are provided below.

2017/18 Actuals	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
4.8%	25.2%	44.8%	82.6%	85.5%	90.6%	99.7%

The ratio is calculated by comparing the financing cost of all borrowing with the revenue stream through Council Tax, general grants and Retained Business Rates. It increases as the level of borrowing increases year on year while government and tax revenues reduce. The cost of finance associated with this borrowing is more than covered by the revenues attached to investment income at an expected net yield of 5%.

2) Approved Capital Expenditure

The Capital Expenditure estimates are summarised below. The estimates come from approved schemes in the Capital Budget, which is to be agreed by Council in February 2019.

2017/18 Actual £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000
54,348	79,921	111,526	1,381	1,381	1,381	1,381

Note – the 2017/18 to 2019/20 figures above include property purchases

3) The Capital Financing Requirement

The Capital Financing Requirement (CFR) is used to assist in deciding whether capital expenditure is affordable, by measuring the underlying need to borrow. The indicator is calculated by matching fixed assets and projected capital expenditure to capital resources applied. The difference between the two, if positive, represents total capital expenditure financed by borrowing. The definition of unfinanced capital expenditure includes finance leases and PFI arrangements. Long Term borrowing should not, except in the short term, exceed the CFR. The indicator now also includes all borrowings associated with the purchase of investment property of £200M per annum by the end of 2019/20.

	2017/18 Actual £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Opening CFR	**1,475**	**50,213**	**121,357**	**226,238**	**217,172**
Unfinanced Capital Exp	48,981	73,623	110,000	0	0
MRP & Finance Leases	(243)	(2,479)	(5,119)	(9,066)	(9,066)
Closing CFR	**50,213**	**121,357**	**226,238**	**217,172**	**208,106**
Long Term Borrowing	70,000	90,000	200,000	200,000	200,000
Over/(Under) Borrowing	**19,787**	**(31,357)**	**(26,238)**	**(17,172)**	**(8,106)**

The Council has two leases that were reclassified as finance leases under International Financial Reporting Standards in 2010, where previously they had no impact on the CFR. The Finance Lease Liability is being reduced through budgeted lease repayments and as a result there is no requirement to borrow to meet this liability.

4) Authorised Limit for External Debt

To ensure good cashflow management, there is occasionally a need to borrow in the short term. Authority for any such borrowing is delegated to the S151 Officer. There are some circumstances where long term borrowing to support the Capital Programme is required to finance major capital projects or investment property purchases. The long-term limits set in this report are based on the projected Capital Financing requirement over the period of the Medium Term strategy, and will be the maximum permissible amount of total borrowing. Other Long-Term Liabilities are deposits held by the Council and relate to the Woolmer industrial estate.

	2017/18 £'000	2018/19 £'000	2019/20 £'000	2020/21 £'000	2021/22 £'000
Borrowing Authorised Limit	109,000	125,000	230,000	225,000	215,000
Other Long Term Liabilities	300	300	300	300	300

TREASURY MANAGEMENT INDICATORS

1) Operational Boundary for External Debt

The purpose of this indicator is to serve as a warning that the authorised limit for external debt is close. It has been set at £3M below the authorised limit.

	2017/18 Actual £'000	2018/19 Estimate £'000	2019/20 Estimate £'000	2020/21 Estimate £'000	2021/22 Estimate £'000
Borrowing Operational Limit (Up to 1 Yr)	106,000	122,000	27,000	£222,000	212,000
Other Long Term Liabilities	300	300	300	300	300

2) Interest Rate Exposures

Setting upper limits for variable and fixed interest rates provides a range in which the authority manages exposure to fixed and variable interest rates. Although fixed rates bring security to long term returns, variable rate investments can give the flexibility to maximise returns when interest rates are expected to increase. The indicators set will allow this flexibility.

Upper Limit for Fixed Rate Exposure

2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
100%	100%	100%	100%	100%

Upper Limit for Variable Rate Exposure

2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
100%	100%	100%	100%	100%

3) Total Principal Sums invested

The Prudential Code requires authorities to establish long term limits on principal sums invested in long term investments. The purpose of this indicator is to ensure that a good maturity profile of investments is maintained.

Term of Investment	Total Value £M
Within 1 Years	1,500
Between 1 and 2 Years	0
2+ Years	0

Schedule 3 - Borrowing and Lending List 2019/20

Fitch Ratings

Long Term: Investments will only be made in institutions which, if rated, are rated at BBB+ or above. Building Societies that are not rated are included on the basis of asset size, of a minimum of £1bn.

Short Term: Investments will only be made in institutions which, if rated, are rated F3 or above. Building Societies not rated are included on the basis of asset size, of a minimum of £500m.

Long Term Investments

Maximum Investment: Total investments not to exceed £5m; all investments to be carried out in consultation with the Portfolio Holder for Finance
Maximum Term: 5 years

Clearing Banks & Subsidiaries	Fitch Rating	
	Short Term	Long Term
Barclays Bank	F1	A+
HSBC	F1+	AA-
Lloyds Bank	F1	A+
Royal Bank of Scotland	F1	A+
Nat West Bank	F1	A+
Other UK Banks		
Santander UK plc	F1	A+
Close Brothers Ltd	F1	A
Abbey National Treasury Services Plc	F1	A
Goldman Sachs Group	F1	A
Local Authorities		
Central Government		

Building Societies (Assets over £1bn)	Rating by asset size	Fitch Rating	
		Short Term	Long Term
Nationwide	1	F1	A
Yorkshire	2	F1	A-
Coventry	3	F1	A
Skipton	4	F1	A-
Leeds	5	F1	A-
Principality	6	F2	BBB+
West Bromwich	7	-	-
Newcastle	8	B	BB+
Nottingham	9	-	-
Progressive	10	-	-
Cumberland	11	-	-
National Counties	12	-	-
Saffron	13	-	-
Cambridge	14	-	-

Short Term Lending List

For investments not exceeding 364 days.

Maximum Investment: £3,000,000
Maximum Duration: 364 Days

Clearing Banks & Subsidiaries	Fitch Rating	
	Short Term	Long Term
Barclays Bank	F1	A+
HSBC	F1+	AA-
HSBC Private Bank	-	-
Lloyds Bank	F1	A+
Royal Bank of Scotland	F1	A+
Nat West Bank	F1	A+
Other UK Banks		
Santander UK plc	F1	A+
Clydesdale Bank	F2	BBB+
Close Brothers Ltd	F1	A
Abbey National Treasury Services Plc	F1	A
Local Authorities		
Central Government		

Building Societies (Assets over £500m)	Rating by asset size	Fitch Rating	
		Short Term	Long Term
Nationwide	1	F1	A
Yorkshire	2	F1	A-
Coventry	3	F1	A
Skipton	4	F1	A-
Leeds	5	F1	A-
Principality	6	F2	BBB+
West Bromwich	7	-	-
Newcastle	8	B	BB+
Nottingham	9	-	-
Progressive	10	-	-
Cumberland	11	-	-
National Counties	12	-	-
Saffron	13	-	-
Cambridge	14	-	-
Monmouthshire	15	-	-
Leek United	16	-	-
Furness	17	-	-
Newbury	18	-	-
Hinckley and Rugby	19	-	-
Ipswich	20	-	-
Darlington	21	-	-

Long term Borrowing
Long term borrowing is for capital projects. Long term borrowing will be from PWLB, UK Sterling based institutions and to include Local Authorities.

Short Term Borrowing

Short term borrowing is for temporary cash shortfalls. Short term borrowing will be from UK Sterling based institutions, including Local Authorities. Short term borrowing will not exceed 364 days.

Schedule 4 – Minimum Revenue Provision Policy 2019/20

MRP on Finance Leased assets prior to 2017

The Council holds assets which are financed through a Finance Lease, as defined by International Financial Reporting standards. Where assets are financed in this way, MRP is charged over the life of the asset or, where this is not practical, over the life of the lease.

Prudential Code debt incurred in the year 2019/20 and onwards in relation to income generating property acquisitions

The Council will calculate the amounts for MRP for 2019/20 by applying a annuity formula incorporating a PWLB long-term borrowing rate, commensurate in duration to the estimated life of the item purchased/built to the apportionment of the value attributed to each financial year's opening CFR in relation to such income generating capital expenditure where the item purchased/built is expected to have a life of up to 50 years or more.

Prudential Code debt incurred in the year 2017 onwards in relation to Leisure Centres and other operational assets

The Council will apply the following methodology for MRP in relation to the Leisure Centre build:

- Annuity method (Asset life) - Annuity method, which works on the basis of a mortgage type repayment extended over the lifecycle of the asset. MRP Commencement on operational properties will be postponed until the financial year after asset becomes operational.

- Borrowing where timing differences arise between spend and future capital receipts; MRP will be charged in the year in which capital receipts are received

- Internal Borrowing; MRP repayment on internal borrowing will be offset against savings or income generated in the Income & Expenditure Account as a direct result of the investment. Repayment schedules will be confirmed prior to internal borrowing commencing.