Executive Committee

12 February 2019

Treasury Management & Investment Strategy

Relevant Wards: - All

Portfolio Holder: - Cllr Paul Cumming

Head of Service: - Deputy Chief Executive – Andy Baldwin

Contact Officer - As Above

(If you have any queries or questions about the content of this report, please speak to the portfolio holder or contact officer in advance of the meeting.)

1. Purpose and Summary

To approve a Treasury Management and Investment Strategy as required by the Prudential Code for Capital Finance.

2. Recommendations

i) **Council are recommended to approve the Treasury Management and Investment Strategy for 2019/20**.

3. Background

3.1 The Council invests for three broad purposes:

- because it has surplus cash as a result of its day to day activities, for example when income is received in advance of expenditure (known as **treasury management investments**),
- to support local public services by lending to or buying shares in other organisations (**service investments**), and
- to earn investment income to support council services (known as **commercial investments**).

3.2 MHCLG maintains that the borrowing of monies purely to invest and make a return is unlawful and this Council will not engage in such activity.

3.3 The Prudential Code for Capital Finance requires authorities to self regulate the affordability, prudence and sustainability of their capital expenditure and the need for any potential borrowing.

3.4 To comply with the Code the Council needs to consider its Treasury Management Strategy at the beginning of each year that links with and supports the Medium Term Financial Plan (MTFP). The projected earnings from our expected cash and property investment portfolio have been updated in the budget report for 2019/20.

3.5 The Prudential Code also requires the Council to set a number of prudential indicators for the next three years that underpin the proposed spending plans, these are set out in the report.

3.6 The Treasury Management Strategy is based upon market forecasts, together with the planned level of Council balances (both capital and revenue) detailed in the MTFP.

3.7 If any of the Council's investments appeared at risk of loss due to default (e.g. credit-related loss) the Council will make revenue provision of an appropriate amount.

4. Treasury Management Investments

4.1 The Council typically receives its income (e.g. from taxes and grants) before it pays for its expenditure (e.g. through payroll and invoices). It also holds reserves for future expenditure and collects local taxes on behalf of other local authorities and central government. These activities, lead to cash surpluses which are invested in accordance with this strategy. The balance of treasury management investments is expected to fluctuate between £13m and £25m during the 2019/20 financial year.

4.2 Over the coming financial year the Council will continue to maintain its revenue and capital reserves as stated in the MTFP.

4.3 Detailed daily cash projections are calculated by the Accountancy team to ensure that the Council keeps minimal overnight cash balances, while maximising the amounts invested in accordance with the Treasury Management Practices.

4.4 The investment target budget for 2019/20 is set at £310,000. This budget will be achievable if yields average 1.6%, hence a yield of only 1.2% will result in a £75,000 shortfall.

4.5 The strategy is underpinned by a Treasury Management Policy which remains unchanged and can be found at Appendix A.

Current investments

4.6 The Council's cash portfolio is managed in-house. The Council is expected to receive some £338,255 from its cash investments net of short term borrowing costs in 2018/19. This will be some £68,255 more than the budgeted figure.

4.7 Interest rates have remained at historically low levels, with base rates at 0.5%. The current low levels of interest rates are forecast to remain at similarly low levels throughout the next financial year

4.8 The levels of interest earned have stayed stable from last year, however the Council has earned better rates of interest investing with the CCLA property fund and CCLA diversified Income fund. The average rate of return for our cash investments in 2018/19 is currently standing at 1.83%.

4.9 The range of interest rates vary from a low of 0.75% for overnight monies to 1.05% for longer term deposits to around 3% in the CCLA diversified income fund and 5% in the CCLA property fund.

4.10 The majority of money market investments this financial year have been for relatively short periods with HSBC and CCLA.

Investment strategy

4.11 Investments which the Council may use for the prudent management of its treasury balances are called Specified Investments and can be made with those organisations detailed in the practice statements.

4.12 Given the volatility of the money markets rather than rely on out of date counterparty lists. Up to date credit ratings have been sought from one of the rating companies such as Moody's, S&P or Fitch when placing monies in any financial institution.

4.13 All investments will be in sterling. The general policy objective for this Council is the prudent investment of its treasury balances. The Council's investment priorities are the security of capital and liquidity of its investments.

4.14 The Council will aim to achieve the optimum return on its investments commensurate with the proper levels of security and liquidity.

4.15 Having given due consideration to the Council's level of balances over the next three years, the need for liquidity and current money market instability, It is felt prudent that the majority of funds continue to be invested in short term investments (i.e. those with a maturity less than a year), however where the risk is deemed manageable that longer term investments are investigated where appropriate.

Treasury Performance

4.16 At the end of the financial year, the Deputy Chief Executive will prepare a report on investment activity and performance as part of the Final Accounts Report.

4.17 The Council relies on the credit ratings for investing monies as listed in the Practice Statements. The Aaa/AAA through to the C/D (long term) and the A1+/F1+(short term) ratings express these organisation's opinions on an institution's ability to service and repay punctually its debt obligations. A short-term rating will cover obligations that have a maturity date of less than one year. Long term ratings cover maturities beyond one year.

4.18 Counterparties will only be used for investments if they meet the criteria set out in the practice statements. Any variations to this will be agreed by the Deputy Chief Executive in consultation with the portfolio holder for Finance & Resources.

4.19 The careful monitoring and management of cash flows is necessary to forecast how much surplus cash there may be available each day and how long that surplus is likely to be available. This helps to form a view on which of the investment options available are likely to be the most advantageous.

Borrowing strategy

4.20 The Council held £3.16M of capital reserves as at 31 March 2018. If the capital programme is approved then the level of capital reserves is expected to reduce to around £2.2M over the life of the MTFP.

4.21 Given these levels of reserves, there is currently no need to enter into external borrowing to fund the capital programme over the next three financial years. However given that the programme is funded by receipts which can always be at risk due to economic downturns then it is prudent for the Council to consider its approach to external borrowing should this become a necessity.

4.22 Local Authorities have the power to borrow funds directly from both the Public Works Loan Board (PWLB), which is directly managed by the Bank of England, as well as the commercial money market.

4.23 The Prudential Code allows the Council to borrow funds to finance its capital programme providing the borrowing can be shown to be affordable in revenue terms and prudent in terms of the Council's overall financial strategy.

4.24 If prudential borrowing were deemed to be necessary then the Deputy Chief Executive would need to submit a report to Council for formal borrowing approval and delegated authority regarding the timing and the mechanics of any borrowing decisions.

5 Service Investments (Shares)

5.1 The acquisition of share capital or loan capital in any body corporate is defined as capital expenditure under Section 16(2) of the Local Government Act 2003. Such investments will have to be funded out of capital or revenue resources and will be classified as Non Specified Investments. Shares are the only investment type that the Authority has identified that meets the definition of a non-specified investment.

5.2 The Council has invested in Malvern Hills Science Park (MHSP) a joint venture company in partnership with Worcestershire County Council, and Worcester Chamber of Commerce. The purpose of the venture is the promotion of job creation and economic development in the Malvern area.

5.3 The Council has 1,044,900 1p non-voting cumulative preference shares (P1), 654 £1 non-voting cumulative preference shares (P2) and 9 of the 100 1p voting shares in the company. The Council is entitled to a 3% dividend on the P1 preference shares and 6.37% dividend on the P2 dividends. The levels of investment and rates of return are set out in the table below.

Share Investment	**Original Investment £**	**Fair Value in accounts £**	**Rate of Return %**
Ordinary Shares	9	601,256	0
Preference Shares (P1)	1,044,909	1,295,687	3.0
Preference Shares (P2)	369,810	427,661	6.37

5.4 The investment in MHSP is not readily liquid but there are no plans to dispose of the investment because of its wider economic aims.

5.5 The Councils Chief Executive is on the board of MHSP. The company has limited liability and as such the Council's liability is restricted to the value of its shareholding in the event of losses or deficits.

6 Commercial Investments (Property)

6.1 The Council has invested in local industrial and commercial property with the intention of making a return that will be spent on services. The following table lists the main investment assets currently held.

Property	**Value in accounts £**	**Net Income 2019/20 £**	**Rate of Return %**
Tenbury Business Park	509,150	51,780	10.2
Spring Court	375,000	45,110	12.0
Spring Lane	892,500	52,780	5.9
4 High Street Upton	97,170	1,230	1.3
TOTAL	**1,873,820**	**150,900**	**8.0**

6.2 In accordance with government guidance, the Council considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs. The properties listed above have been in Council ownership for many years making this calculation both difficult but also academic

6.3 A fair value assessment of the Authority's investment property portfolio has been made recently, and the underlying assets provide security for capital investment.

6.4 Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice and can take a considerable period to sell in certain market conditions. Should the rate of return be deemed to be insufficient then proposals will be brought forward for the Council to consider disposing of that particular property.

7. Prudential Code Limits

7.1 The Council is required by the CIPFA Prudential Code for Capital Finance to consider Prudential Indicators in conjunction with its Treasury Management Strategy and budget for the following year.

7.2 The proposed indicators and limits detailed in this report tie in with the Council's MTFP, and are designed to ensure that the Council's investment plans are affordable, prudent and sustainable

7.3 The key indicators and limits which have to be set are as follows:

i) Authorised and Operational limits for external debt

7.4 The Council is required to approve authorised limits for external debt, together with a lower operational limit. The limits are in accordance with those shown in the proposed Treasury Management Strategy and are set to allow for unexpected borrowing if required in exceptional circumstances.

Borrowing	**2019/20 £000**	**2020/21 £000**	**2021/22 £000**
Authorised Limit	5,000	5,000	5,000
Operational Limit	2,500	2,500	2,500

ii) Actual Level of External Debt

7.5 The Council's external debt at 31 March 2018 was nil. The proposed capital programme expects the Council to remain debt free over the next five financial years.

iii) Treasury Management Indicators

7.6 Whilst it is anticipated that the Council will remain debt free the prudential code requires the setting of upper and lower limits for the maturity structure of any borrowings in the unlikely event that circumstances require the Council to take out borrowing.

7.7 It is recommended that the upper and lower limits for the maturity structure of any projected fixed rate borrowing in each period, as a percentage of total fixed rate borrowing are:

	Upper limit	Lower limit
Under 12 Months	50%	0%
12 months and within 5 years	75%	0%
5 years and above	100%	0%

7.8 The Council currently has no cash invested in long term investments (over 364 days). The Prudential Code requires that authorities set out the total principal of sums invested for periods longer than 364 days and set an upper limit for each forward financial year for the maturity of these investments.

7.9 The level of cash invested in long term deals for the next three financial years will be limited by the cashflow position of the Council over that period and an upper limit of £5m per year is currently most appropriate.

8. Implications and Impact:

How does it meet Council priorities?
The contribution that these investments make to the priorities of the Council is to support effective treasury management activities.

What are the financial / resource implications?
Contained within Budget proposals for 2019/20

What are the Risks?
The strategic risks addressed in the implementation of the recommendations made are as follows:

Failure to keep an updated Treasury Management strategy, could lead to inappropriate investment decisions and non-compliance with the Accounting code of Practice on Treasury Management.

Is a Diversity Impact Assessment Required?
No

Appendices
Appendix A Treasury Management Policy

Background Papers
None