Agenda Item No

North East Derbyshire District Council

Council

31 January 2022

Treasury Strategy Reports 2022/23 - 2025/26

Report of the Portfolio Holder with Responsibility for Finance

Classification: This report is public

Report By: Jayne Dethick, Assistant Director - Finance and Resources (S151 Officer)

Contact Officer: as above

PURPOSE/SUMMARY

The purpose of this report is to provide Council with the necessary information to approve the Council's suite of Treasury Strategies for 2022/23 to 2025/26.

RECOMMENDATIONS

1. That Council approve the Treasury Management Strategy at **Appendix 1** and in particular:

   a) Approve the Borrowing Strategy

   b) Approve the Investment Strategy

   c) Approve the use of the external treasury management advisors Counterparty Weekly List (or similar) to determine the latest assessment of the counterparties that meet the Council's Criteria before any investment is undertaken.

   d) Approve the Prudential Indicators

2. That Council approve the Capital Strategy as set out in **Appendix 2** and in particular:

   a) Approve the Capital Financing Requirement

   b) Approve the Minimum Revenue Provision Statement for 2022/23

   c) Approve the Prudential Indicators for 2022/23, in particular:

Authorised Borrowing Limit	£203,786,000
Operational Boundary	£198,786,000

Capital Financing Requirement £193,786,000

3. That Council approve the Investment Strategy as set out in **Appendix 3.**

Approved by the Portfolio Holder – Yes

IMPLICATIONS

Finance and Risk **Yes ✓** **No**

These are considered throughout the report.

On Behalf of the Section 151 Officer

Legal including Data Protection **Yes ✓** **No**

As part of the requirements of the CIPFA Treasury Management Code of Practice the Council is required to produce every year a Treasury Management Strategy and Capital Strategy which requires approval by full Council prior to the commencement of each financial year. This report is prepared in order to comply with these obligations.

There are no Data Protection issues arising directly from this report.

On Behalf of the Solicitor to the Council

Staffing **Yes** **No ✓**

There are no staffing issues arising directly from this report.

On Behalf of the Head of Paid Service

DECISION INFORMATION

Is the decision a Key Decision? A Key Decision is an executive decision which has a significant impact on two or more District wards or which results in income or expenditure to the Council above the following thresholds: *BDC: Revenue - £75,000* ☐ *Capital - £150,000* ☐ *NEDDC: Revenue - £100,000* ☐ *Capital - £250,000* ☐	No

☑ *Please indicate which threshold applies*	
Is the decision subject to Call-In?(Only Key Decisions are subject to Call-In)	No
Has the relevant Portfolio Holder been informed	Yes
District Wards Affected	All
Links to Corporate Plan priorities or Policy Framework	All

REPORT DETAILS

1.1 Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2017 Edition* (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year. This report fulfils the Council's legal obligation under the *Local Government Act 2003* to have regard to the CIPFA Code.

1.2 The CIPFA Code requires that a Capital Strategy be produced alongside the Treasury Management Strategy. In addition, the 2018 Investment Guidance issued by the Department for Levelling Up, Housing and Communities requires local authorities to produce an investment Strategy. So there is now a requirement to produce three separate treasury strategies.

1.3 The Council's Treasury Management Strategy provides the framework for managing the Council's cash flows, borrowing and investments, and the associated risks for the years 2022/23 to 2025/26. The Strategy also sets out the parameters for all borrowing and lending as well as listing all approved borrowing and investment sources. Prudential indicators aimed at monitoring risk are also included. (**Appendix 1**).

1.4 The Capital Strategy is intended to provide a high level, concise overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of the Council's services. The report provides an overview of the associated risk, its management and the implications for future financial sustainability. The Capital Strategy also sets out the capital expenditure plans for the period and how they will be financed. It includes information of the minimum revenue provision, capital financing requirement and prudential indicators aimed at monitoring risk (**Appendix 2).**

1.5 The Investment Strategy focuses on investments made for service purposes and commercial reasons, rather than those made for treasury management. Investments covered by this strategy include earning income through commercial investments or by supporting local services by lending to or buying shares in other organisations **(Appendix 3).**

2 Reasons for Recommendation

2.1 This report outlines the Council's proposed suite of Treasury Strategies for the period 2022/23 to 2025/26 for consideration and approval by Council. It contains:

- The Treasury Management Strategy which provides the framework for managing the Council's cash flows, borrowing and investments for the period.

- The Capital Strategy which is intended to provide a high level, concise overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of the Council's services.

- The Investment Strategy which focuses on investments made for service purposes and commercial reasons, rather than those made for treasury management.

The above strategies provide an approved framework within which the officers undertake the day to day capital and treasury activities.

3 Alternative Options and Reasons for Rejection

3.1 Alternative options are considered throughout the report.

DOCUMENT INFORMATION

Appendix No	Title
1 2 3	Treasury Management Strategy Capital Strategy Investment Strategy
Background Papers	

Report Author	Contact Number
Jayne Dethick – Assistant Director - Finance and Resources (S151 Officer)	(01246) 217078

APPENDIX 1

North East Derbyshire District Council

Treasury Management Strategy 2022/23 – 2025/26

Introduction

1.1 Treasury Management is the management of the Council's cash flows, borrowing and investments, and the associated risks. The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Council's prudent financial management.

1.2 Treasury risk management at the Council is conducted within the framework of the *Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition* (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year. This report fulfils the Council's legal obligation under the *Local Government Act 2003* to have regard to the CIPFA code.

1.3 Investments held for service purposes or for commercial profit are considered in a different report, the Investment Strategy.

External Context

1.4 **Economic background:** The ongoing impact on the UK from coronavirus, together with higher inflation, higher interest rates, and the country's trade position post-Brexit, will be major influences on the Council's treasury management strategy for 2022/23.

1.5 The Bank of England (BoE) increased Bank Rate at 0.25% in December 2021 while maintaining its Quantitative Easing programme at £895 billion. The Monetary Policy Committee (MPC) voted 8-1 in favour of raising rates, and unanimously to maintain the asset purchase programme. Within the announcement the MPC noted that the pace of the global recovery was broadly in line with its November Monetary Policy Report. Prior to the emergence of the Omicron coronavirus variant, the Bank also considered the UK economy to be evolving in line with expectations, however the increased uncertainty and risk to activity the new variant presents, the Bank revised down its estimates for Q4 GDP growth to 0.6% from 1.0%. Inflation was projected to

be higher than previously forecast, with CPI likely to remain above 5% throughout the winter and peak at 6% in April 2022. The labour market was generally performing better than previously forecast and the BoE now expects the unemployment rate to fall to 4% compared to 4.5% forecast previously, but notes that Omicron could weaken the demand for labour.

1.6 UK CPI for November 2021 registered 5.1% year on year, up from 4.2% in the previous month. Core inflation, which excludes the more volatile components, rose to 4.0% year on year from 3.4%. The most recent labour market data for the three months to October 2021 showed the unemployment rate fell to 4.2% while the employment rate rose to 75.5%.

1.7 In October 2021, the headline 3-month average annual growth rate for wages were 4.9% for total pay and 4.3% for regular pay. In real terms, after adjusting for inflation, total pay growth was up 1.7% while regular pay was up 1.0%. The change in pay growth has been affected by a change in composition of employee jobs, where there has been a fall in the number and proportion of lower paid jobs.

1.8 Gross Domestic Product (GDP) grew by 1.3% in the third calendar quarter of 2021 according to the initial, compared to a gain of 5.5% quarter on quarter in the previous quarter, with the annual rate slowing to 6.6% from 23.6%. The Q3 gain was modestly below the consensus forecast of a 1.5% quarter on quarter rise. During the quarter activity measures were boosted by sectors that reopened following pandemic restrictions, suggesting that wider spending was flat. Looking ahead, while monthly GDP reading suggest there had been some increase in momentum in the latter art of Q3, Q4 growth is expected to be soft.

1.9 GDP Growth in the euro zone increased by 2.2% in calendar Q3 2021 following a gain of 2.1% in the second quarter and a decline of -0.3% in the first. Headline inflation has been strong, with CPI registering 4.9% year-on-year in November, the fifth successive month of inflation. Core CPI inflation was 2.6% year on year in November, the fourth month of successive increases from July's 0.7% year on year. At these levels, inflation is above the European Central Bank's target of 'below, but close to 2%', putting some pressure on its long-term stance of holding its main interest rate of 0%.

1.10 The US economy expanded at an annualised rate of 2.1% in Q3 2021, slowing sharply from gains of 6.7% and 6.3% in the previous two quarters. In its December 2021 interest rate announcement, the Federal Reserve continue to maintain the Fed Funds rate at between 0% and 0.25% but outlined its plan to reduce its asset purchase programme earlier than previously stated and signalled they are in favour of tightening interest rates at a faster pace in 2022, with three 0.25% movements now expected.

1.11 **Credit outlook:** Since the start of 2021, relatively benign credit conditions have led to credit default swap (CDS) prices for the larger UK banks to remain low and had steadily edged down throughout the year up until mid-November when the

emergence of Omicron has caused them to rise modestly. However, the generally improved economic outlook during 2021 helped bank profitability and reduced the level of impairments many had made as provisions for bad loans. However, the relatively recent removal of coronavirus-related business support measures by the government means the full impact on bank balance sheets may not be known for some time.

1.12 The improved economic picture during 2021 led the credit rating agencies to reflect this in their assessment of the outlook for the UK sovereign as well as several financial institutions, revising them from negative to stable and even making a handful of rating upgrades.

1.13 Looking ahead, while there is still the chance of bank losses from bad loans as government and central bank support is removed, the institutions on the Council's counterparty list are well-capitalised and general credit conditions across the sector are expected to remain benign. Duration limits for counterparties on the Council's lending list are under regular review and will continue to reflect economic conditions and the credit outlook.

1.14 **Interest rate forecast:** The Council's treasury management adviser Arlingclose is forecasting that Bank Rate will continue to rise in calendar Q1 2022 to subdue inflationary pressures and the perceived desire by the BoE to move away from emergency levels of interest rates.

1.15 Investors continue to price in multiple rises in Bank Rate over the next forecast horizon, and Arlingclose believes that although interest rates will rise, the increases will not be to the extent predicted by financial markets. In the near-term, the risks around Arlingclose's central case are to the upside while over the medium-term the risks become more balanced.

1.16 Yields are expected to remain broadly at current levels over the medium-term, with the 5, 10 and 20 year gilt yields expected to average around 0.65%, 0.90%, and 1.15% respectively. The risks around for short and medium-term yields are initially to the upside but shifts lower later, while for long-term yields the risk is to the upside. However, as ever there will almost certainly be short-term volatility due to economic and political uncertainty and events.

1.17 A more detailed economic and interest rate forecast provided by Arlingclose is attached at **Appendix A.**

1.18 For the purpose of setting the budget, it has been assumed that new treasury management investments will be made at an average rate of 0.01%, and that new long-term loans will be borrowed at an average rate of 2%.

Local Context

1.19 On 30th November 2021, the Council held £147.1m of borrowing and £34.0m of investments. This is set out in further detail at **Appendix B**. Forecast changes in these sums are shown in the balance sheet analysis in **Table 1** below.

Table 1: Balance sheet summary and forecast

	31/3/21 Actual £m	31/3/22 Estimate £m	31/3/23 Forecast £m	31/3/24 Forecast £m	31/3/25 Forecast £m	31/3/26 Forecast £m
General Fund CFR	13.4	17.0	18.3	16.8	13.7	10.6
HRA CFR	169.8	173.4	175.2	177.0	178.8	180.6
Total CFR	**183.2**	**190.4**	**193.5**	**193.8**	**192.5**	**191.2**
Less: Other debt liabilities *	0	0	0.3	0.2	0.1	0.1
Loans CFR	183.2	190.4	193.8	194.0	192.6	191.3
Less: External borrowing **	(149.2)	(147.0)	(147.2)	(145.0)	(140.8)	(139.8)
Internal borrowing	34.0	43.4	46.6	49.0	51.8	51.5
Less: Balance sheet reserves	(70.0)	(67.4)	(58.3)	(59.0)	(61.8)	(61.5)
Investments	**36.0**	**24.0**	**11.7**	**10.0**	**10.0**	**10.0**

* leases that form part of the Council's total debt.
** shows only loans to which the Council is committed and excludes optional refinancing

1.20 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

1.21 The Council has an increasing CFR due to commitments within the capital programme and also loans for Northwood Group Ltd and Rykneld Homes Ltd. The forecast level of reserves means that the majority of borrowing throughout this period is likely to be from internal resources.

1.22 CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Council's total debt should be lower than its highest forecast CFR over the next

three years. Table 1 shows that the Council expects to comply with this recommendation during 2022/23.

1.23 **Liability benchmark:** To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as **Table 1** above, but that cash and investment balances are kept to a minimum level of £10m at each year-end to maintain sufficient liquidity but minimise credit risk.

Table 2: Liability benchmark

	31/3/20 Actual £m	31/3/21 Estimate £m	31/3/22 Forecast £m	31/3/23 Forecast £m	31/3/24 Forecast £m	31/3/25 Forecast £m
CFR	**183.2**	**190.4**	**193.8**	**194.0**	**192.6**	**191.2**
Less: Balance sheet reserves	(70.0)	(67.4)	(58.3)	(59.0)	(61.8)	(61.5)
Net loans requirement	113.2	123.0	135.5	135.0	130.8	129.7
Plus: Liquidity allowance	10.0	10.0	10.0	10.0	10.0	10.0
Liability Benchmark	**123.2**	**133.0**	**145.5**	**145.0**	**140.8**	**139.7**

Borrowing Strategy

1.24 The Council currently holds £149.2m of loans, a decrease of £0.3m on the previous year, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in **Table 1** shows that the Council does not expect to need to borrow in 2022/23. The Council may however, borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £203.8m.

1.25 **Objectives:** The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

1.26 **Strategy:** Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

1.27 By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal

borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Council with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2022/23 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

1.28 The Council has previously raised all of its long-term borrowing from the PWLB but will consider long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield; the Council intends to avoid this activity in order to retain its access to PWLB loans.

1.29 Alternatively, the Council may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

1.30 In addition, the Council may borrow short-term loans to cover unplanned cash flow shortages.

1.31 **Sources of borrowing:** The approved sources of long-term and short-term borrowing are:

- HM Treasury's PWLB lending facility (formerly the Public Works Loan Board)
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds (except Derbyshire County Council Pension Fund)
- capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

1.32 **Other sources of debt finance:** In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- leasing
- hire purchase
- Private Finance Initiative
- sale and leaseback

1.33 **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds

on the capital markets and lends the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to Council.

1.34 **LOBOs:** The Council doesn't hold or intend to hold any LOBO (Lender's Option Borrower's Option) loans.

1.35 **Short-term and variable rate loans**: These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below. Financial derivatives may be used to manage this interest rate risk (see section below).

1.36 **Debt rescheduling:** The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

Treasury Investment Strategy

1.37 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's treasury investment balance has ranged between £33.0m and £48.0m, and similar levels are expected to be maintained in the forthcoming year.

1.38 **Objectives:** The CIPFA Code requires the Council to invest its treasury funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

1.39 Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

1.40 **Negative interest rates:** The COVID-19 pandemic has increased the risk that the Bank of England will set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. Since investments cannot pay negative income, negative rates will be applied by reducing

the value of investments. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

1.41 **Strategy:** Given the increasing risk and very low returns from short-term unsecured bank investments, the Council aims to further diversify into more secure and/or higher yielding asset classes during 2022/23. The majority of the Council's surplus cash is currently invested in short-term unsecured bank deposits, local authorities, registered providers and money market funds. This diversification will represent a continuation of the strategy currently adopted.

1.42 **Business models:** Under the new IFRS 9 standard, the accounting for certain investments depends on the Council's "business model" for managing them. The Council aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

1.43 **Approved counterparties:** The Council may invest its surplus funds with any of the counterparty types in **Table 3** below, subject to the cash limits (per counterparty) and the time limits shown.

Table 3: Approved investment counterparties and limits

Sector	Time limit	Counterparty limit	Sector limit
The UK Government	50 years	Unlimited	n/a
Local authorities & other government entities	25 years	£5m	Unlimited
Secured investments *	25 years	£5m	Unlimited
Banks (unsecured) *	13 months	£5m	Unlimited
Building societies (unsecured) *	13 months	£5m	£20m
Registered providers (unsecured) *	5 years	£5m	£20m
Money market funds *	n/a	£5m	Unlimited
Strategic pooled funds	n/a	£5m	£20m
Real estate investment trusts	n/a	£5m	£20m
Other investments *	5 years	£5m	£20m

1.44 * **Minimum credit rating:** Treasury investments in the sectors marked with an asterisk will only be made with entities whose lowest published long-term credit rating is no lower than A-. Where available, the credit rating relevant to the specific

investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

1.45 For entities without published credit ratings, investments may be made either (a) where external advice indicates the entity to be of similar credit quality; or (b) to a maximum of £5m per counterparty as part of a diversified pool e.g. via a peer-to-peer platform.

1.46 **Government:** Loans to, and bonds and bills issued or guaranteed by, national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Government are deemed to be zero credit risk due to its ability to create additional currency and therefore may be made in unlimited amounts for up to 50 years.

1.47 **Secured Investments:** Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds and reverse repurchase agreements with banks and building societies are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used. The combined secured and unsecured investments with any one counterparty will not exceed the cash limit for secured investments.

1.48 **Banks and building societies (unsecured):** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

1.49 **Registered providers (unsecured):** Loans to, and bonds issued or guaranteed by, registered providers of social housing or registered social landlords, formerly known as housing associations. These bodies are regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.

1.50 **Money market funds:** Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. Although no sector limit applies to money market funds, the Council will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.

1.51 **Strategic pooled funds:** Bond, equity and property funds that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

1.52 **Real estate investment trusts:** Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.

1.53 **Other investments:** This category covers treasury investments not listed above, for example unsecured corporate bonds and company loans. Non-bank companies cannot be bailed-in but can become insolvent placing the Council's investment at risk.

1.54 **Operational bank accounts:** The Council may incur operational exposures, for example though current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but are still subject to the risk of a bank bail-in, and balances will therefore be kept at £5m per bank. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

1.55 **Risk assessment and credit ratings**: Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. The credit rating agencies in current use are listed in the Treasury Management Practices document. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be recalled or sold at no cost will be, and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

1.56 Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "negative watch") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

1.57 **Other information on the security of investments**: The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis and advice from the Council's treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.

1.58 When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2020, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This may cause investment returns to fall, but will protect the principal sum invested.

1.59 **Investment limits**: The Council's revenue reserves available to cover investment losses are forecast to be £23.3 million on 31st March 2022. In order that no more than 21.5% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £5 million. A group of entities under the same ownership will be treated as a single organisation for limit purposes.

1.60 Credit risk exposures arising from non-treasury investments, financial derivatives and balances greater than £5 million in operational bank accounts count against the relevant investment limits.

1.61 Limits are also placed on fund managers, investments in brokers' nominee accounts and foreign countries as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Table 4: Additional Investment limits

	Cash limit
Any group of pooled funds under the same management	£5m per manager
Negotiable instruments held in a broker's nominee account	£5m per broker
Foreign countries	£5m per country

1.62 **Liquidity management**: The Council uses its own cash flow forecasting techniques to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium-term financial plan and cash flow forecast.

1.63 The Council will spread its liquid cash over a number of providers (e.g. bank accounts and money market funds) to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

Treasury Management Indicators

1.64 The Council measures and manages its exposures to treasury management risks using the following indicators:

1.65 **Security**: The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Credit risk indicator	
Portfolio average credit rating	**Target** <3.0
Current portfolio average credit rating on investments	**Actual** 1.45

1.66 **Liquidity:** The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three month period, without additional borrowing.

Liquidity risk indicator	**Amount available**
Total cash available within 3 months	£32m

1.67 **Interest rate exposures**: This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

Interest rate risk indicator	Limit each year
Upper limit on one-year revenue impact of a 1% rise in interest rates	£1.5m
Upper limit on one-year revenue impact of a 1% fall in interest rates	(£1.5m)

1.68 The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at new market rates.

1.69 **Maturity structure of borrowing:** This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	20%	0%
12 months and within 24 months	20%	0%
24 months and within 5 years	40%	0%
5 years and within 10 years	40%	0%
10 years and above	90%	0%

1.70 Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

1.71 **Principal sums invested for periods longer than a year:** The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end will be:

Price risk indicator	2022/23	2023/24	2024/25
Limit on principal invested beyond year end	£20m	£20m	£20m

Related Matters

1.72 The CIPFA Code requires the Council to include the following in its treasury management strategy.

1.73 **Financial Derivatives:** Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income

at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the *Localism Act 2011* removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

1.74 The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

1.75 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for derivative exposures. An allowance for credit risk calculated using the methodology in the Treasury Management Practices document will count against the counterparty credit limit and the relevant foreign country limit.

1.76 In line with the CIPFA code, the Council will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.

1.77 **Markets in Financial Instruments Directive**: The Council has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

1.78 **Financial Implications**: The General Fund budget for investment income in 2022/23 is £0.003m with the HRA budget for investment income in 2022/23 being £0.007m, based on an average investment portfolio of £22.0m at an average interest rate of 0.04%. The General Fund budget for debt interest paid in 2022/23 is £0.459m with the HRA budget for debt interest paid in 2022/23 being £4.729m, based on an average debt portfolio of £147.0m at an average interest rate of 3.53%. If actual levels of investments and borrowing, or actual interest rates, differ from those forecast, performance against budget will be correspondingly different.

Other Options Considered

1.79 The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer, having consulted the Cabinet Member for Finance, believes that the above strategy represents an

appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

Appendix A

Economic & Interest Rate Forecast (Arlingclose October 2021)

Underlying assumptions:

- The global recovery from the pandemic has entered a more challenging phase. The resurgence in demand has led to the expected rise in inflationary pressure, but disrupted factors of supply are amplifying the effects, increasing the likelihood of lower growth rates ahead. The advent of the Omicron variant of coronavirus is affecting activity and is also a reminder of the potential downside risks.

- Despite relatively buoyant activity survey data, official GDP data indicates that growth was weakening into Q4 2021. Other data, however, suggested continued momentum, particularly for November. Retail sales volumes rose 1.4%, PMIs increased, and the labour market continued to strengthen. The end of furlough did not appear to have had a significant impact on unemployment. Wage growth is elevated.

- The CPI inflation rate rose to 5.1% for November and will rise higher in the near term. While the transitory factors affecting inflation are expected to unwind over time, policymakers' concern is persistent medium term price pressure.

- These factors prompted the MPC to raise Bank Rate to 0.25% at the December meeting. Short term interest rate expectations remain elevated.

- The outlook, however, appears weaker. Household spending faces pressures from a combination of higher prices and tax rises. In the immediate term, the Omicron variant has already affected growth – Q4 and Q1 activity could be weak at best.

- Longer-term government bond yields remain relatively low despite the more hawkish signals from the BoE and the Federal Reserve. Investors are concerned that significant policy tightening in the near term will slow growth and prompt the need for looser policy later. Geo-political and coronavirus risks are also driving safe haven buying. The result is a much flatter yield curve, as short-term yields rise even as long-term yields fall.

- The rise in Bank Rate despite the Omicron variant signals that the MPC will act to bring inflation down whatever the environment. It has also made clear its intentions to tighten policy further. While the economic outlook will be challenging, the signals from policymakers suggest their preference is to tighten policy unless data indicates a more severe slowdown.

- While Q2 UK GDP expanded more quickly than initially thought, the 'pingdemic' and more latterly supply disruption will leave Q3 GDP broadly stagnant. The outlook also appears weaker. Household spending, the driver of the recovery to date, is under pressure from a combination of retail energy price rises, the end of government support programmes and soon, tax rises. Government spending, the other driver of recovery, will slow considerably as the economy is taken off life support

- Inflation rose to 3.2% in August. A combination of factors will drive this to over 4% in the near term. While the transitory factors affecting inflation, including the low base effect of 2020, are expected to unwind over time, the MPC has recently communicated fears that these transitory factors will feed longer-term inflation expectations that require tighter monetary policy to control. This has driven interest rate expectations substantially higher

- The supply imbalances are apparent in the labour market. While wage growth is currently elevated due to compositional and base factors, stories abound of higher wages for certain sectors, driving inflation expectations. It is uncertain whether a broad-based increased in wages is possible given the pressures on businesses.

- Government bond yields increased sharply following the September FOMC and MPC minutes, in which both central banks communicated a lower tolerance for higher inflation than previously thought. The MPC in particular has doubled-down on these signals in spite of softer economic data. Bond investors expect higher near-term interest rates but are also clearly uncertain about central bank policy.

- The MPC appears to be playing both sides, but has made clear its intentions to tighten policy, possibly driven by a desire to move away from emergency levels. While the economic outlook will be challenging, the signals from policymakers suggest Bank Rate will rise unless data indicates a more severe slowdown.

Forecast:

- The MPC will want to build on the strong message it delivered this month by tightening policy despite Omicron uncertainty.

- Arlingclose therefore expects Bank Rate to rise to 0.50% in Q1 2022, but then remain there. Risks to the forecast are initially weighted to the upside, but becoming more balanced over time. The Arlingclose central forecast remains below the market forward curve.

- Gilt yields will remain broadly flat from current levels. Yields have fallen sharply at the longer end of the yield curve, but expectations of a rise in Bank Rate have maintained short term gilt yields at higher levels.

- Easing expectations for Bank Rate over time could prompt the yield curve to steepen, as investors build in higher inflation expectations.

- The risks around the gilt yield forecasts vary. The risk for short and medium term yields is initially on the upside but shifts lower later. The risk for long-term yields is weighted to the upside.

	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24
Official Bank Rate													
Upside risk	0.00	0.00	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downside risk	0.00	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
3-month money market ra													
Upside risk	0.05	0.05	0.25	0.35	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.25	0.55	0.55	0.60	0.60	0.60	0.60	0.65	0.65	0.65	0.65	0.65	0.65
Downside risk	0.00	-0.25	-0.25	-0.30	-0.30	-0.30	-0.30	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35
5yr gilt yield													
Upside risk	0.00	0.35	0.45	0.55	0.55	0.55	0.55	0.55	0.55	0.50	0.50	0.45	0.45
Arlingclose Central Case	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.65	0.70	0.75	0.75
Downside risk	-0.10	-0.20	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.30	-0.35	-0.40	-0.40
10yr gilt yield													
Upside risk	0.10	0.25	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55
Arlingclose Central Case	0.80	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.90	0.90	0.95	0.95
Downside risk	-0.10	-0.25	-0.30	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.40	-0.40	-0.40	-0.40
20yr gilt yield													
Upside risk	0.30	0.40	0.45	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	1.00	1.05	1.10	1.10	1.10	1.10	1.15	1.15	1.15	1.20	1.20	1.20	1.20
Downside risk	-0.15	-0.30	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45
50yr gilt yield													
Upside risk	0.25	0.30	0.40	0.45	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.70	0.75	0.80	0.85	0.90	0.95	1.00	1.05	1.05	1.10	1.10	1.15	1.15
Downside risk	-0.15	-0.30	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45

PWLB Standard Rate (Maturity Loans) = Gilt yield + 1.00%
PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%
PWLB Infrastructure Rate (Maturity Loans) = Gilt yield + 0.60%

Appendix B

Existing Investment & Debt Portfolio Position

	30/11/21 Actual Portfolio £m	30/11/21 Average Rate %
External borrowing:		
Public Works Loan Board	147	3.53
Total external borrowing	**147**	**3.53**
Total other long-term liabilities:	**0**	**0**
Total gross external debt	**147**	**3.53**
Treasury investments:		
The UK Government	0	0.00
Local authorities	5	0.15
Banks (unsecured)	0	0.00
Money Market Funds	29	0.01
Total treasury investments	**34**	**0.03**
Net debt	**113**	

APPENDIX 2

North East Derbyshire District Council

North East Derbyshire District Council

Capital Strategy 2022/23 – 2025/26

Introduction

1.1 This capital strategy report, gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability.

1.2 Decisions made this year on capital and treasury management will have financial consequences for the Council for many years into the future. They are therefore subject to both a national regulatory framework and to a local policy framework, summarised in this report.

Capital Expenditure and Financing

1.3 Capital expenditure is where the Council spends money on assets, such as property or vehicles that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £10,000 are not capitalised and are charged to revenue in year.

In 2022/23, the Council is planning capital expenditure of £24.7m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure

	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
General Fund Services	1.5	7.7	5.9	2.9	3.1	1.9
Council Housing (HRA)	11.2	27.8	18.8	18.1	18.1	18.1
TOTAL	12.7	35.5	24.7	21.0	21.2	20.0

1.4 The main General Fund capital projects include replacement vehicles, asset refurbishment, ICT replacement and disabled facilities grants.

1.5 The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately. The main HRA capital projects involve refurbishment and ECO works to the Council's non-traditional housing stock.

1.6 The Council has no capital investments but this would include loans and shares made for service purposes and property to be held primarily for financial return in line with the definition in the CIPFA Treasury Management Code.

1.7 **Governance**: Projects are included in the capital programme as part of the annual budget review or through ad hoc approval during the year. The capital programme is refreshed each year and the new requirements are presented to Cabinet and Council each February. Full details of the Council's Capital Programme can be seen at **Appendix A** to this report.

1.8 All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing and leasing). The planned financing of the above expenditure is as follows:

Table 2: Financing of Capital Programme

	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
External Sources	1.0	4.1	2.2	0.8	0.8	0.8
Own Resources	11.1	24.4	19.3	18.4	18.6	17.4
Debt	0.6	7.0	3.2	1.8	1.8	1.8
TOTAL	**12.7**	**35.5**	**24.7**	**21.0**	**21.2**	**20.0**

1.9 Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as minimum revenue provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to repay and/or replace debt finance. Planned MRP and use of capital receipts are as follows:

Table 3: Replacement of debt finance

	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
Capital Resources	1.6	0	0	0	0	0
Revenue Resources	0.7	0.6	0.2	0.3	0.2	0.2
Total	2.3	0.6	0.2	0.3	0.2	0.2

The Council's full minimum revenue provision statement is **Appendix B** to this report.

1.10 The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase by £3.4m during 2022/23. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement

	31/3/2021 Actual £m	31/3/2022 Forecast £m	31/3/2023 Budget* £m	31/3/2024 Budget £m	31/3/2025 Budget £m	31/3/2026 Budget £m
General Fund Services	13.4	17.0	18.6	17.0	13.8	10.7
Council Housing (HRA)	169.8	173.4	175.2	177.0	178.8	180.6
TOTAL CFR	**183.2**	**190.4**	**193.8**	**194.0**	**192.6**	**191.3**

*£0.3m of the CFR increase in 2022/23 arises from a change in the accounting for leases.

1.11 **Asset management:** The Council's assets require regular maintenance to ensure they remain safe and fit for purpose. It is also important for income generation that assets remain in a good condition and so remain lettable. A planned approach yields savings in running costs and energy efficiency benefits over time as works are completed and asset conditions improve.

1.12 **Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive £4.2m of capital receipts in the coming financial year as follows:

Table 5: Capital receipts receivable

	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
Asset Sales	4.03	3.79	4.20	4.20	4.80	4.80
Loans Repaid	0	0	0	0	0	0
TOTAL	**4.03**	**3.79**	**4.20**	**4.20**	**4.80**	**4.80**

Treasury Management

1.13 Treasury Management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

1.14 Due to decisions taken in the past, the Council currently has £147.1m borrowing at an average interest rate of 3.53% and £35.0m treasury investments at an average rate of 0.03%.

1.15 **Borrowing strategy:** The Council's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at around 0.10%) and long-term fixed rate loans where the future cost is known but higher (currently 1.50%-2.50%).

1.16 Projected levels of the Council's total outstanding debt (which comprises borrowing and leases) are shown below, compared with the capital financing requirement (see above):

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement

	31/3/2021 Actual £m	31/3/2022 Forecast £m	31/3/2023 Budget £m	31/3/2024 Budget £m	31/3/2025 Budget £m	31/3/2026 Budget £m
Debt (incl. leases)	149.2	147.0	147.2	145.0	140.8	139.8
Capital Financing Requirement	183.2	190.4	193.8	194.0	192.6	191.3

1.17 Statutory guidance states that debt should remain below the capital financing requirement, except in the short-term. As can be seen from **Table 6**, the Council expects to comply with this in the medium term.

1.18 **Liability benchmark:** To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing:

Table 7: Borrowing and the Liability Benchmark

	31/3/2021 Actual £m	31/3/2022 Forecast £m	31/3/2023 Budget £m	31/3/2024 Budget £m	31/3/2025 Budget £m	31/3/2026 Budget £m
Outstanding Borrowing	149.2	147.0	147.2	145.0	140.8	139.8
Liability Benchmark	123.2	133.0	145.5	145.0	140.8	139.7

1.19 The table above shows that the Council expects to remain borrowed above its liability benchmark. This is because cash outflows to date have been below the assumptions made when the loans were borrowed.

1.20 **Affordable borrowing limit:** The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year and to keep it under review. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

Table 8: Prudential Indicators: Authorised limit and operational boundary for external debt

	2021/22 limit £m	2022/23 limit £m	2023/24 limit £m	2024/25 limit £m	2025/26 limit £m
Authorised Limit – Borrowing	200.4	203.5	203.8	202.5	201.2
Authorised Limit – Leases	0	0.3	0.2	0.1	0.1
Authorised Limit – Total External Debt	**200.4**	**203.8**	**204.0**	**202.6**	**201.3**
Operational Boundary – Borrowing	195.4	198.5	198.8	197.5	196.2
Operational Boundary – Leases	0	0.3	0.2	0.1	0.1
Operational Boundary – Total External Debt	**195.4**	**198.8**	**199.0**	**197.6**	**196.3**

1.21 **Treasury Investment strategy:** Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

1.22 The Council's policy on treasury investments is to prioritise security and liquidity over yield, which is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.

Table 9: Treasury Management investments

	31/3/2021 Actual £m	31/3/2022 Forecast £m	31/3/2023 Budget £m	31/3/2024 Budget £m	31/3/2025 Budget £m	31/3/2026 Budget £m
Near-Term Investments	36.0	24.0	11.7	10.0	10.0	10.0
Longer-Term Investments	0	0	0	0	0	0
TOTAL	**36.0**	**24.0**	**11.7**	**10.0**	**10.0**	**10.0**

1.23 **Risk management:** The effective management and control of risk are prime objectives of the Council's treasury management activities. The treasury management strategy therefore sets out various indicators and limits to constrain the

risk of unexpected losses and details the extent to which financial derivatives may be used to manage treasury risks.

1.24 **Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Chief Finance Officer and staff, who must act in line with the treasury management strategy approved by Council. Quarterly reports on treasury management activity are presented to Cabinet and the Audit Committee. The Audit and Corporate Governance Scrutiny Committee is responsible for scrutinising treasury management decisions.

Investments for Service Purposes

1.25 The Council can make investments to assist local public services, including making loans to local service providers and businesses to promote economic growth. In light of the public service objective, the Council is willing to take more risk than with treasury investments, however it still plans for such investments to at least break even after all costs. This includes loans to the Rykneld Homes Ltd to allow development of social housing. Rykneld Homes Ltd is a wholly owned subsidiary of the Council, limited by guarantee.

1.26 With central government financial support for local public services declining, the Council has invested in developing residential property through Northwood Group Ltd. Currently (at 30/11/21), an investment of £1.510m has been made into Northwood Group Ltd and further future investment of £7.153m is approved to provide a total investment of £8.663m.

1.27 **Governance:** Decisions on service investments are made by the relevant service manager and submitted to Cabinet then Council in consultation with the Chief Finance Officer and must meet the criteria and limits laid down in the Investment Strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme.

Commercial Activities

1.28 The Council has investment properties generating between £0.410m and £0.527m in net income a year after all costs, before exposing it to normal commercial risks. These risks are managed by maintaining the properties in good order and advertising vacant properties as soon as possible over a wide area to generate interest in letting the vacant properties.

1.29 With financial return being the main objective, the Council accepts higher risk on commercial investment than with treasury investments. The principal risk exposures include build cost estimates, sales values estimates and demand. These risks are

mitigated by working with experienced builders and professionals who have knowledge of the local market. In order that commercial investments remain proportionate to the size of the Council contingency plans are in place should expected yields not materialise.

1.30 **Governance:** Decisions on commercial investments are made by Council in line with the criteria and limits approved in the Investment Strategy. Property and most other commercial investments are also capital expenditure and purchases will therefore also be approved as part of the capital programme.

	2020/21 Actual £m	**2021/22 Forecast £m**	**2022/23 Budget £m**	**2023/24 Budget £m**	**2024/25 Budget £m**	**2025/26 Budget £m**
Net income from commercial investments	0.527	0.459	0.412	0.411	0.410	0.410
Net income from service investments	0.317	0.432	0.468	0.443	0.373	0.264
Total net income from service and commercial investments	0.844	0.891	0.880	0.854	0.783	0.674
Proportion of net revenue stream	6.65%	5.68%	6.33%	6.47%	5.94%	5.14%
Proportion of usable revenue reserves	**3.23%**	**3.82%**	**3.82%**	**3.80%**	**3.56%**	**3.09%**

Liabilities

1.31 In addition to debt of £149.2m detailed above, the Council is committed to making future payments to cover its net pension fund deficit (valued at £58.2m). It has also set aside £1.5m to cover risks of business rates appeals and £1.1m to cover risks of water claims.

1.32 **Governance:** Decisions on incurring new discretional liabilities are taken to Council for approval. The risk of liabilities occurring and requiring payment are monitored as part of the year-end process.

Revenue Budget Implications

1.33 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, Business Rates and general government grants.

Table 10: Prudential Indicator: Proportion of financing costs to net revenue stream

	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Budget £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m
Financing Costs	0.7	0.6	0.1	0.1	0.1	0.1
Proportion of Net Revenue Stream	5.49%	3.82%	1.13%	1.31%	1.02%	1.13%

1.34 **Sustainability:** Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The Chief Finance Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable.

Knowledge and Skills

1.35 The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. Suitably qualified and experienced officers are employed throughout the Council to perform such functions.

1.36 Where Council officers do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers. This approach is more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

1.37 Members receive individual training and development through the Member Development Programme and are periodically required to attend seminars held by the external treasury management advisors.

Treasury Management Operations

1.38 As mentioned above the Council uses external treasury management advisors. The company provides a range of services which include:

- Technical support on treasury matters, capital finance issues and the drafting of Member reports;
- Economic and interest rate analysis;
- Debt services which includes advice on the timing of borrowing;
- Debt rescheduling advice surrounding the existing portfolio;
- Generic investment advice on interest rates, timing and investment instruments;
- A number of places at training events offered on a regular basis.
- Credit ratings/market information service comprising the three main credit rating agencies;
-

1.39 Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the final decision on treasury matters remains with the Council. This service is subject to regular review. It should be noted that the Council has Arlingclose Ltd as external treasury management advisors, for a period of up to 3 years commencing October 2019.

Banking Contract

1.40 The contract with the Councils banking provider Lloyds Bank was extended on the 10th February 2022 for a period of up to 7 years.

Business Continuity Arrangements

1.41 As part of the Councils business continuity arrangements officers have sought to set up and provide alternative banking arrangements for the Council should they be required at short notice. These arrangements effectively mean a separate bank account is in place with the required security controls and appropriate officer access to undertake transactions. This account is with Barclays Bank and will only be utilised should a business continuity need or similar issue arise. Officers will continue to review this arrangement.

Appendix A

Capital Programme 2021-2026

Capital Expenditure	Revised Budget 2021/22 £	Original Budget 2022/23 £	Original Budget 2023/24 £	Original Budget 2024/25 £	Original Budget 2025/26 £
Housing Revenue Account					
HRA Capital Works	12,211,000	10,823,500	10,441,000	10,441,000	10,441,000
HRA Capital Works - Non Traditional Properties	7,152,000	4,600,000	4,370,000	4,370,000	4,370,000
Green Homes EWI - Mickley	1,110,000	0	0	0	0
Pine View, Danesmoor	1,007,000	70,000	0	0	0
Stock Purchase Programme (1-4-1)	3,000,000	2,500,000	2,500,000	2,500,000	2,500,000
Acquisitions and Disposals (RHL)	500,000	500,000	500,000	500,000	500,000
North Wingfield New Build Project	2,081,000	0	0	0	0
Garage Demolitions	37,000	23,000	23,000	23,000	23,000
Concrete Balconies	111,000	0	0	0	0
Parking Solutions	576,000	288,000	288,000	288,000	288,000
HRA - Capital Expenditure	**27,785,000**	**18,804,500**	**18,122,000**	**18,122,000**	**18,122,000**
General Fund					
Private Sector Housing Grants (DFG's)	820,000	820,000	820,000	820,000	820,000
ICT Schemes	204,500	248,500	87,000	119,000	119,000
Clay Cross Football Pitch	9,000	0	0	0	0
Asset Refurbishment - General	386,000	500,000	500,000	500,000	500,000
Asset Refurbishment - Eckington Depot	525,000	0	0	0	0
Roller Shutter Doors	42,000	0	0	0	0
Eckington Pool Carbon Efficiencies Programme	1,565,000	0	0	0	0
Dronfield Sports Centre Carbon Efficiencies Programme	0	1,380,000	0	0	0
Replacement of Vehicles	920,000	2,976,000	1,518,500	1,677,000	449,000
Contaminated Land	42,000	0	0	0	0
Killamarsh Leisure Centre	1,991,000	0	0	0	0
Clay Cross Towns Fund Project	1,205,000	0	0	0	0
General Fund Capital Expenditure	**7,709,500**	**5,924,500**	**2,925,500**	**3,116,000**	**1,888,000**
Total Capital Expenditure	**35,494,500**	**24,729,000**	**21,047,500**	**21,238,000**	**20,010,000**

Capital Financing	2020/21	2021/22	2022/23	2023/24	2025/26
Housing Revenue Account					
Major Repairs Reserve	(19,348,000)	(15,423,500)	(14,811,000)	(14,811,000)	(14,811,000)
Prudential Borrowing - HRA	(3,576,000)	(1,800,000)	(1,800,000)	(1,800,000)	(1,800,000)
Development Reserve	(1,751,000)	(381,000)	(311,000)	(311,000)	(311,000)
Grants	(1,045,000)	0	0	0	0
1-4-1 Receipts	(2,065,000)	(1,200,000)	(1,200,000)	(1,200,000)	(1,200,000)
HRA Capital Financing	**(27,785,000)**	**(18,804,500)**	**(18,122,000)**	**(18,122,000)**	**(18,122,000)**
General Fund					
Disabled Facilities Grant	(820,000)	(820,000)	(820,000)	(820,000)	(820,000)
External Grant - Lottery Funded Schemes	(9,000)	0	0	0	0
External Grant - Contaminated Land	(42,000)	0	0	0	0
External Grant - Eckington Pool Carbon Efficiencies	(1,015,000)	0	0	0	0
External Grant - Clay Cross Towns Fund	(1,205,000)	0	0	0	0
External Grant - Dronfield Sports Centre Carbon Efficiencies	0	(1,347,000)	0	0	0
Prudential Borrowing - Vehicles	(920,000)	(1,417,000)	0	0	0
Prudential Borrowing - Eckington Depot	(525,000)	0	0	0	0
Prudential Borrowing - Killamarsh Leisure Centre	(1,991,000)	0	0	0	0
RCCO - Roller Shutter Doors	(42,000)	0	0	0	0
Useable Capital Receipts	(1,140,500)	(2,340,500)	(2,105,500)	(2,296,000)	(1,068,000)
General Fund Capital Financing	**(7,709,500)**	**(5,924,500)**	**(2,925,500)**	**(3,116,000)**	**(1,888,000)**
HRA Development Reserve					
Opening Balance	(2,382,074)	(240,074)	0	(241,830)	(382,666)
Amount due in year	391,000	(140,926)	(552,830)	(451,836)	(441,780)
Amount used in year	1,751,000	381,000	311,000	311,000	311,000
Closing Balance	**(240,074)**	**0**	**(241,830)**	**(382,666)**	**(513,446)**
Major Repairs Reserve					
Opening Balance	(2,173,612)	0	0	0	0
Amount due in year	(17,174,388)	(15,423,500)	(14,811,000)	(14,811,000)	(14,811,000)
Amount used in year	19,348,000	15,423,500	14,811,000	14,811,000	14,811,000
Closing Balance	**0**	**0**	**0**	**0**	**0**
Capital Receipts Reserve					
Opening Balance	(1,406,741)	(566,241)	(225,741)	(120,241)	(424,241)
Income expected in year	(3,000,000)	(3,000,000)	(3,000,000)	(3,600,000)	(3,600,000)
Allowable Debt/Pooling Expenses	2,700,000	1,000,000	1,000,000	1,000,000	1,000,000
Amount used in year	1,140,500	2,340,500	2,105,500	2,296,000	1,068,000
Closing Balance	**(566,241)**	**(225,741)**	**(120,241)**	**(424,241)**	**(1,956,241)**
Capital Receipts Reserve 1-4-1 receipts					
Opening Balance	(1,275,114)	0	0	0	0
Income expected in year	(789,886)	(1,200,000)	(1,200,000)	(1,200,000)	(1,200,000)
Amount used in year	2,065,000	1,200,000	1,200,000	1,200,000	1,200,000
Closing Balance	**0**	**0**	**0**	**0**	**0**
Total Capital Financing	**(35,494,500)**	**(24,729,000)**	**(21,047,500)**	**(21,238,000)**	**(20,010,000)**

Appendix B

Annual Minimum Revenue Provision Statement 2021/22

Where the Council finances General Fund capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Authority to have regard to the former Ministry of Housing, Communities and Local Government's *Guidance on Minimum Revenue Provision* (the MHCLG Guidance) most recently issued in 2018.

The broad aim of the MHCLG Guidance is to ensure that capital expenditure is financed over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government, Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

The MHCLG Guidance requires the Council, to approve an Annual MRP Statement each year, and includes recommendations for calculating a prudent amount of MRP. In line with this guidance the Council has adopted the following approach:

- For capital expenditure incurred after 31st March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant asset in equal instalments, starting in the year after the asset becomes operational. MRP on purchases of freehold land will be charged over 50 years. MRP on expenditure not related to fixed assets but which has been capitalised by regulation or direction will be charged over 20 years.

- For assets acquired by leases, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.

- Where former operating leases have been brought onto the balance sheet on 1st April 2022 due to the adoption of the *IFRS 16 Leases* accounting standard, and the asset values have been adjusted for accruals, prepayments, premiums and/or discounts, then the annual MRP charges will be adjusted so that the total charge to revenue remains unaffected by the new standard.

- For capital expenditure loans to third parties that are repaid in annual or more frequent instalments of principal, the Council will make nil MRP, but will instead apply the capital receipts arising from principal repayments to reduce the capital financing requirement instead. In years where there is no principal repayment, MRP will be charged in accordance with the MRP policy for the assets funded by the loan, including where appropriate, delaying MRP until the year after the assets become operational. While this is not one of the options in the MHCLG Guidance, it is thought

to be a prudent approach since it ensures that the capital expenditure incurred in the loan is fully funded over the life of the assets.

- No MRP will be charged in respect of assets held within the Housing Revenue Account.

Capital expenditure incurred during 2022/23 will not be subject to a MRP charge until 2023/24 and so on.

Based on the Council's latest estimate of its Capital Financing Requirement on 31st March 2022, the budget for MRP has been set as follows:

	31/03/22 Estimated CFR £m	**2022/23 Estimated MRP £m**
Supported Capital Expenditure after 31.03.2008	0	0
Unsupported Capital Expenditure after 31.03.2008	17.0	0.2
Leases	0	0
Total General Fund	**17.0**	**0.2**
Assets in the Housing Revenue Account	46.3	0
HRA Subsidy Reform Payment	127.1	0
Total Housing Revenue Account	**173.4**	**0**
Total	**190.4**	**0.2**

Revenue Account (HRA)

Following the budget on 30 October 2018, the legislation that capped the amount of HRA debt a local housing authority could hold was revoked with immediate effect. The capital financing requirements relating to the HRA will remain the same so there will still be no requirement for an MRP and levels of debt will be managed through prudential borrowing limits controlled by the Treasury Management Strategy.

Removing the debt cap and not having a statutory requirement to make a provision to repay debt presents a significant risk to the HRA. Very careful treasury management is needed to ensure that the Council's HRA borrowing remains affordable, prudent and reasonable and that the HRA remains sustainable over the long term.

North East Derbyshire District Council

North East Derbyshire District Council

Investment Strategy 2022/23 – 2025/26

Introduction

1.1 The Council invests its money 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 (known as **commercial investments** where this is the main purpose).

1.2 This investment strategy meets the requirements of the statutory guidance issued by the Government in January 2018, and focuses on the second and third of these categories.

Treasury Management Investments

1.3 The Council typically receives its income in cash (e.g. from taxes and grants) before it pays for its expenditure in cash (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, plus the timing of borrowing decisions, lead to a cash surplus which is invested in accordance with guidance from the Chartered Institute of Public Finance and Accountancy. The balance of treasury management investments is expected to fluctuate between £11.7m and £30.0m during the 2022/23 financial year.

1.4 **Contribution:** The contribution that these investments make to the objectives of the Council is to support effective treasury management activities.

1.5 **Further details:** Full details of the Council's policies and its plan for 2022/23 for treasury management investments are covered in the Treasury Management Strategy.

Service Investments: Loans

1.6 **Contribution:** The Council lends money to assist local public services, including making loans to local service providers and businesses to stimulate local economic growth. This includes loans to Rykneld Homes Ltd to allow development of social housing. Rykneld Homes Ltd is a wholly owned subsidiary of the Council, limited by guarantee. It also includes a loan to Northwood Group Ltd for a mixed tenure housing development scheme in the district.

1.7 **Security:** The main risk when making service loans is that the borrower will be unable to repay the principal lent and/or the interest due. In order to limit this risk, and ensure that total exposure to service loans remains proportionate to the size of the Council, upper limits on the outstanding loans to each category of borrower have been set as follows:

Table 1: Loans for service purposes

Category of borrower	31/3/2021 actual			2022/23
	Balance owing £m	Loss allowance £m	Net figure in accounts £m	Approved limit £m
Rykneld Homes Ltd	7.104	0	7.104	13.500
Northwood Group Ltd	1.510	0	1.510	8.663
Total	**8.614**	**0**	**8.614**	**22.163**

1.8 Accounting standards require the Council to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Council's statement of accounts are shown net of this loss allowance. However, the Council makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments.

1.9 **Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding service loans by requiring a fully costed business case in all instances that includes any investment/loan requirements and financial/risk implications. A significant amount of due diligence work is undertaken in each case to ensure the business case is robust. The strength of the partnership between Rykneld Homes company and the Council and Northwood group Ltd and the Council helps to mitigate any risk associated with non-payment.

Service Investments: Shares

1.10 **Contribution:** The Council has invested £0.150m to date (up to 31st December 2021) in the shares of Northwood Group Ltd to support local public services and stimulate local economic growth by delivering housing developments whilst generating income for the Council.

1.11 **Security:** One of the risks of investing in shares is that they fall in value meaning that the initial outlay may not be recovered. In order to limit this risk, upper limits on the sum invested in each category of shares have been set as follows:

Table 2: Shares held for service purposes

Category of company	31/3/2021 actual			2022/23
	Amounts invested £m	Gains or (losses) £m	Value in accounts £m	Approved Limit £m
Northwood Group Ltd	0.150	(0.006)	0.144	0.150
TOTAL	**0.150**	**(0.006)**	**0.144**	**0.150**

1.12 **Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding shares by working with experienced professionals who have extensive knowledge of the projects and the local markets. In order that commercial investments remain proportionate to the size of the Council, these are subject to overall maximum investment limits and contingency plans are in place should expected yields not materialise.

1.13 **Liquidity:** the viability models for each project the Council considers take account of the maximum periods for which funds may prudently be committed and states what those maximum periods are within approved contracts. This will assist the Council to stay within its stated investment limits.

1.14 **Non-specified Investments:** Shares are the only investment type that the Council has identified that meets the definition of a non-specified investment in the government guidance. The Council has not adopted any procedures for determining further categories of non-specified investment since none are likely to meet the definition.

Commercial Investments: Property

1.15 MHCLG defines property to be an investment if it is held primarily or partially to generate a profit.

1.16 **Contribution:** The Council invests in local, commercial and residential property with the intention of making a profit that will be spent on local public services. These are mainly industrial units owned across the district.

Table 3: Property held for investment purposes

Property	Actual	31/3/2021 actual		31/3/2022 expected	
	Purchase cost £m	Gains or (losses) £m	Value in accounts £m	Gains or (losses) £m	Value in accounts £m
Industrial Units	4.4	3.3	7.7	0	7.7
Land	1.7	2.0	3.7	0	3.7
Commercial Properties	1.1	0.3	1.4	0	1.4
Shared Ownership Properties	1.1	0.3	1.4	0	1.4
TOTAL	**8.3**	**5.9**	**14.2**	**0**	**14.2**

1.17 **Security:** 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.

1.18 A fair value assessment of the Council's investment property portfolio has been made within the past twelve months, and the underlying assets provide security for capital investment. Should the 2021/22 year end accounts preparation and audit process value these properties below their purchase cost, then an updated investment strategy will be presented to full council detailing the impact of the loss on the security of investments and any revenue consequences arising therefrom.

1.19 Where value in the accounts is below purchase cost, the fair value of the Council's investment property portfolio would no longer be sufficient to provide security against loss, and the Council would therefore need to take mitigating actions to protect the capital invested. These actions could include maintaining the investment properties to a required standard and once vacant, advertising any empty investment properties quickly and with professional advertising agencies.

1.20 **Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding property investments by working with experienced professionals who have extensive knowledge of the projects, properties and local markets. In order that commercial investments remain proportionate to the size of the Council, these are subject to overall maximum investment limits and contingency plans are in place should expected yields not materialise.

1.21 **Liquidity:** 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. The Council's Treasury Management Strategy provides assurances through limits on long-term investments to ensure that the invested funds or suitable alternatives can be accessed when they are needed, for example to repay capital borrowed.

Loan Commitments and Financial Guarantees

1.22 Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees carry similar risks to the Council and are included here for completeness.

1.23 The Council has contractually committed to make up to £8.663m of loans to Northwood Group Ltd should it request it. The Council has also guaranteed loans of £7.288m to Rykneld Homes Ltd.

Proportionality

1.24 The Council is to some extent dependent on income generating investment activity to achieve a balanced revenue budget. Table 4 below shows the extent to which the expenditure planned to meet the service delivery objectives is dependent on achieving the expected net profit from investments over the lifecycle of the Medium Term Financial Plan. Should it fail to achieve the expected net profit, the Council's contingency plans for continuing to provide these services are to meet the shortfalls from other efficiencies generated within the general fund revenue budget or utilise reserves set aside for this purpose.

Table 4: Proportionality of investments

	2020/21 Actual £m	**2021/22 Forecast £m**	**2022/23 Budget £m**	**2023/24 Budget £m**	**2024/25 Budget £m**	**2025/26 Budget £m**
Net Service Expenditure	8.000	12.821	11.017	10.292	10.258	10.182
Net Investment Income	0.527	0.459	0.424	0.422	0.421	0.420
Proportion	**6.6%**	**3.6%**	**3.8%**	**4.1%**	**4.1%**	**4.1%**

Borrowing in Advance of Need

1.25 Government guidance is that local authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed.

Capacity, Skills and Culture

1.26 **Elected members and statutory officers:** The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. Suitably qualified and experienced officers are employed throughout the Council to perform such functions.

1.27 Where Council officers do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers. This approach is more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

1.28 Members receive individual training and development through the Member Development Programme and are periodically required to attend seminars held by the external treasury management advisors.

1.29 **Commercial deals:** All Officers involved in negotiating such arrangements are aware of the core principles of the prudential framework and of the regulatory regime within which local authorities operate and considerable due diligence is undertaken in all instances.

1.30 **Corporate governance:** All decisions regards new loans or investments of this nature are considered by the Council's Cabinet before being recommended for approval at Council. Any presentation to members will have been through a fully costed business case that includes any investment/loan requirements and financial/risk implications. A significant amount of due diligence work is undertaken in each case to ensure the business case is robust before reporting to Cabinet.

Investment Indicators

1.31 The Council has set the following quantitative indicators to allow elected members and the public to assess the Council's total risk exposure as a result of its investment decisions.

1.32 **Total risk exposure:** The first indicator shows the Council's total exposure to potential investment losses. This includes amounts the Council is contractually committed to lend but have yet to be drawn down and guarantees the Council has issued over third party loans.

Table 5: Total investment exposure

Total investment exposure	31/03/2021 Actual £m	31/03/2022 Forecast £m	31/03/2023 Forecast £m
Treasury management investments	38.00	20.00	11.70
Service investments: Loans – Rykneld Homes Ltd	7.10	7.03	6.77
Service investments: Loans – Northwood Group Ltd	1.51	4.62	6.26
Service investments: Shares – Northwood Group Ltd	0.15	0.15	0.15
Commercial investments: Property	14.20	14.20	14.20
TOTAL INVESTMENTS	**60.96**	**46.00**	**39.08**
Commitments to lend	13.55	10.51	9.13
TOTAL EXPOSURE	**74.51**	**56.51**	**48.21**

1.33 **How investments are funded:** Government guidance is that these indicators should include how investments are funded. Since the Council does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. To date these investments have been funded by usable reserves and income received in advance of expenditure.

Table 6: Investments funded by borrowing

Investments funded by borrowing	31/03/2021 Actual £m	31/03/2022 Forecast £m	31/03/2023 Forecast £m
Treasury management investments	0	0	0
Service investments: Loans – Rykneld Homes Ltd	7.10	7.03	6.77
Service investments: Loans – Northwood Group Ltd	1.51	4.62	6.26
Service investments: Shares – Northwood Group Ltd	0	0	0
Commercial investments: Property	0	0	0
TOTAL FUNDED BY BORROWING	**8.61**	**11.65**	**13.03**

1.34 **Rate of return received:** This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested. Note that due to the complex local government accounting framework, not all recorded gains and losses affect the revenue account in the year they are incurred.

Table 7: Investment rate of return (net of all costs)

Investments net rate of return	2020/21 Actual £m	2021/22 Forecast £m	2022/23 Forecast £m
Treasury management investments	0.11%	0.03%	0.04%
Service investments: Loans – Rykneld Homes Ltd	3.55%	3.50%	3.53%
Service investments: Loans – Northwood Group Ltd	5.09%	5.09%	5.09%
Service investments: Shares – Northwood Group Ltd	0.00%	0.00%	0.00%
Commercial investments: Property	3.71%	3.23%	2.90%

1.35 The indicators used to report on the risks and opportunities associated with investment decisions will be kept under review as the Council's Investment Strategy and activities evolve over time.