Agenda Item	8.b
Report No	RES/06/21

THE HIGHLAND COUNCIL

Committee: **Corporate Resources Committee**

Date: 25 February 2021

Report Title: **Treasury Management Strategy Statement and Investment Statement – 2021/22**

Report By: Executive Chief Officer, Resources and Finance

1. Purpose/Executive Summary

1.1 The Council has adopted the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management in Local Authorities (the Code). A requirement of the Code is for an annual Treasury Management Strategy Statement and Investment Statement (TMSS & IS) to be approved by Council for the forthcoming financial year.

2. Recommendations

2.1 Members are asked to approve the TMSS & IS for 2021/22 and the Prudential Indicators as detailed in **Appendix 1** of the report

3. Implications

3.1 Resource – covered in the Appendices to this report.

3.2 Legal - none

3.3 Community (Equality, Poverty, Rural and Island) - none

3.4 Climate Change / Carbon Clever – none

3.5 Risk – A lack of available short-term borrowing, or increased interest rates for short term borrowing due to supply and demand issues would result in increased borrowing costs. In such circumstances the Council may have no option but to take long term PWLB borrowing at higher interest rates.

3.6 Gaelic – none

4. Introduction

4.1 Background

Treasury management is defined by the Code as:

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

4.2 Statutory Requirements

The Local Government in Scotland Act 2003 (the Act) and supporting regulations requires the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

The Act therefore requires the Council to set out its Treasury Strategy for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance subsequent to the Act and included in Section 13 of this report); this sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

4.3 CIPFA Requirements

The CIPFA Code of Practice on Treasury Management was updated in December 2017.

The primary requirements of the Code are as follows:

1. Creation and maintenance of a **Treasury Management Policy Statement** which sets out the policies and objectives of the Council's treasury management activities.
2. Receipt by the full council of an annual **Treasury Management Strategy Statement and Annual Investment Strategy** (this report) for the year ahead. Receipt by delegated Committee of a **Mid-year Review Report** and an **Annual Report** covering activities during the previous year.
3. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
4. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. This Council's delegated Committee is the Corporate Resources Committee.
5. Creation and maintenance of **Treasury Management Practices** which set out the manner, in which the Council will seek to achieve those policies and objectives.

4.4 Treasury Management Strategy for 2021/22

The proposed strategy for 2021/22 in respect of the following aspects of the treasury management function is based upon the Council officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury adviser, the Link Group (Link).

The strategy covers 2 main areas:

1. Capital issues - the capital plans and the prudential indicators.
2. Treasury management issues
    - the current treasury position
    - treasury limits and indicators for 2021/22 to 2023/24 (which will limit the treasury risk and activities of the Council)
    - prospects for interest rates
    - the borrowing requirement based upon the Council's current capital programmes
    - the borrowing strategy (including policy on borrowing in advance of need)
    - debt rescheduling
    - annual investment strategy
    - credit worthiness policy
    - policy on use of external service providers

4.5 Balanced Budget Requirement

It is a statutory requirement under Section 93 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, a local authority must calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions.

Therefore, increases in capital expenditure must be limited to a level whereby the corresponding increases in revenue charges are affordable and within the projected future income of the Council. Increases in revenue charges would include the following:

- increases in interest charges caused by increased borrowing to finance additional capital expenditure
- any increases in running costs from new capital projects
- Interest rates increasing for short term borrowing and a lack of availability of short term borrowing which requires the Council to take more expensive PWLB borrowing

4.6 Training

The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny (the Corporate Resources Committee).

The training needs of treasury management officers are periodically reviewed, with training provided throughout the year using a number of mediums; in-house training, meetings with and training provided by Treasury advisers, external training courses and attendance at treasury forum meetings with other Councils. Treasury training was provided to Members on 2 December 2020 by Link.

4.7 Treasury management advisors

The Council uses Link as its external treasury management advisors. Link were appointed to this role effective from 1 July 2018 for a three-year period with an option to extend for one year. The contract will expire on 30 June 2022.

5. Treasury Limits for 2021/22 to 2023/24

5.1 It is a statutory duty under part 7 of the Local Government in Scotland Act 2003 and supporting regulations, for the Council to determine and keep under review how much it can afford to allocate to capital expenditure.

5.2 The Council must have regard to the Prudential Code when setting the Affordable Capital Expenditure Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax and council house rent levels is 'acceptable'.

5.3 Whilst termed an "Affordable Capital Expenditure Limit", the capital plans to be considered for inclusion may incorporate financing by both external borrowing and other forms of liability, such as credit arrangements. The affordable capital expenditure limit is to be set, on a rolling basis, for the forthcoming and two successive financial years.

5.4 In March 2018, the Council agreed a capital programme which was reprofiled in a report to Council in January 2021. An initial impact assessment of the effect of the reprofiled capital plan on the annual general fund revenue budget for loan charges was as follows:

Year	£m
2020-21	57.832
2021-22	57.133
2022-23	59.007
2023-24	60.059
2024-25	59.334
2025-26	58.647
2026-27	56.686
2027-28	54.805
2028-29	52.901
2029-30	50.557

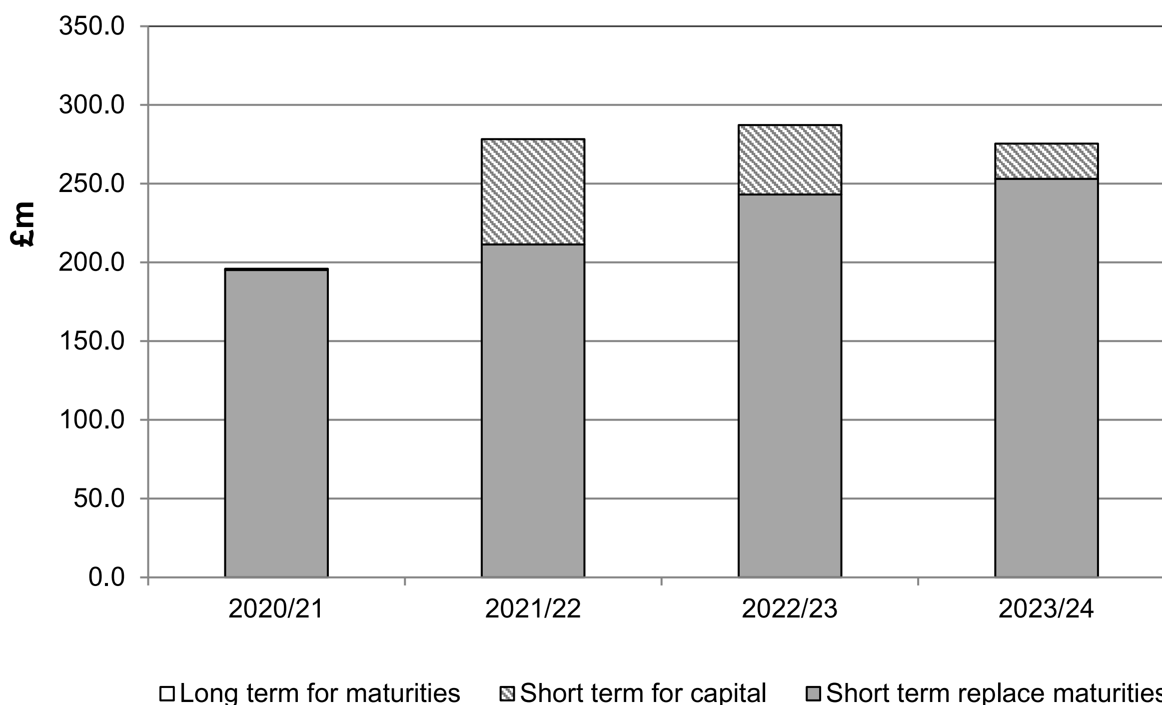
5.5 Whilst the anticipated loans charge exceeds the current revenue budget available the Council has flexibility to apply accumulated historic capital receipts to reduce loans charges from the levels above to bring them in line with the revenue budget provision. This approach was agreed by Members as part of the 2020/21 budget setting process. In addition, future years' loans charge budgets will increase to take account of decisions taken by Council to invest capital in roads infrastructure, savings generated by self-funding projects, and budget adjustments enabled by the funding model linked to capital investment in schools.

5.6 The Council's Housing Revenue account (HRA) capital programme was agreed in August 2015 and during 2021, an updated 5-year plan is to be developed. The implications on HRA rent levels of the agreed programme were considered as part of the programme setting process.

6. Borrowing Requirement

6.1 The following chart shows out the borrowing requirement, showing current year, as well as estimates for future years. The borrowing requirement takes account of borrowing to support the agreed capital programmes, less the projected instalments as capital repayments are charged to revenue accounts through loan charges. This figure is then adjusted to take account of any further borrowing required to go towards the capital financing requirement, or to replace existing loans maturing in these years.

Table 1 Estimates of borrowing (current year and next three years)



7. Statutory repayment of loans fund advances

7.1 The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 came into force on 1 April 2016. The main change introduced by the Regulations is to provide options for the prudent repayment of debt and requires the Council to set out its policy for the statutory repayment of loans fund advances prior to the start of the financial year. The repayment of loans fund advances ensures that the Council makes a prudent provision each year to pay off an element of the accumulated loans fund advances made in previous financial years.

7.2 A variety of options are provided to Councils so long as a prudent provision is made each year.

In February 2019 the Council adopted the following policy on the repayment of loans fund advances:

- For loans fund advances made before 1 April 2016, the policy will be to maintain the practice of previous years and apply the Statutory Method, using a fixed annuity rate.

- For loans fund advances made between 1 April 2016 and 31 March 2021, the policy for the repayment of loans advances will also be the Statutory method, with the majority of loans fund advances being repaid by the Annuity Method. The annuity rate applied to the loans fund repayments will continue to be based on the loans fund rate for the previous year which is calculated using interest paid as a proportion of the outstanding loans fund advances with the same rate applied for the full life of the asset.

- In certain circumstances the Council will consider using the Income Method, a new method available under the 2016 regulations. Under this method loans fund advances can be repaid linked to the phasing of income that is anticipated from a particular project. This method will be considered, where appropriate, for commercial, income generating projects.

7.3 For any loans fund advance made from 1 April 2021 onwards the Council will continue with its current approach as outlined in the two points immediately above- namely using the Annuity method with the Income method used as appropriate.

7.4 As required by the Local Government Finance Circular 7/2016, the commitment to repay loans fund advances for the General Fund and HRA are contained in **Appendices 11 and 12.**

7.5 The annuity rate applied to the loans fund repayments on capital expenditure incurred before March 2016 is 4.52% for the life of the asset. For financial year 2015/16 onwards, the annuity rate used is the loans fund rate for the year the capital expenditure is incurred which is applied for the full life of the asset.

7.6 Under regulation 14 (2) of SSI 2016 No 123, the Council has reviewed and re-assessed the historic annuity rate to ensure that it is a prudent application and provides more certainty over principal repayments. The result of this review suggests that this is a fair and prudent approach and provides certainty over historic principal repayments.

8. Prudential and Treasury Indicators

8.1 The prudential and treasury Indicators which are relevant for setting an integrated treasury management strategy are in **Appendix 1**. These Indicators are based on the approved capital programmes.

9. Economic Context and Prospects for Interest Rates

9.1 Link provide regular economic forecasts to inform the Council on interest rates and longer fixed interest rates projections. The following table is the current Link forecast for interest rates as at February 2021 which was updated when PWLB margins were reduced by 1.0% and includes the certainty rate reduction.

Link Group Interest Rate View	8.2.21												
	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
5 yr PWLB	0.90	0.90	0.90	0.90	1.00	1.00	1.10	1.10	1.10	1.20	1.20	1.20	1.20
10 yr PWLB	1.30	1.30	1.30	1.30	1.40	1.40	1.50	1.50	1.50	1.60	1.60	1.60	1.60
25 yr PWLB	1.90	1.90	1.90	1.90	2.00	2.00	2.10	2.10	2.10	2.20	2.20	2.20	2.20
50 yr PWLB	1.70	1.70	1.70	1.70	1.80	1.80	1.90	1.90	1.90	2.00	2.00	2.00	2.00

9.2 The current economic outlook and structure of market interest rates and government debt yields have several key treasury management implications:

- Investment returns are likely to remain low during 2021/22 and for future years.

- As the table above shows, there is expected to be little upward movement in PWLB rates over the next two years as it will take economies, including the UK, a prolonged period to recover following the sharp recession caused during the coronavirus lock down periods. From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and sharp changes in investor sentiment, (as shown on 9th November when the first results of a successful Covid-19 vaccine trial were announced). Such volatility could occur at any time during the forecast period.

- Short term borrowing and interest rates have been low so far in 2020/21 due to the impact of the Covid-19 on the economy. The policy of avoiding new borrowing by running down spare cash balances has worked well over the last few years. However, this needs to be carefully monitored to avoid incurring higher borrowing costs in the future when authorities may not be able to avoid new borrowing to finance capital expenditure and/or refinance of maturing debt.

- There will remain a cost of carry on any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost – the difference between borrowing costs and investment returns, particularly with low investment returns.

10. Context

10.1 There are some matters relating to the Council's budgets, strategies and external environment that are highlighted below for context to this report. Given the emergent nature of a number of these items a review of the Council's capital programme will be undertaken over the coming months. Any implications of that review on this TMSS & IS will be reported to the Corporate Resources committee or full Council as appropriate.

10.2 The emergence of Covid 19 has had a significant impact on the Council's capital programme. The pandemic has impacted on both the expected delivery timescales for projects, as well as anticipated projects costs. The anticipated impacts have been captured

in the reprofiled capital plan taken to Council in January 2021 (the deferred December 2020 meeting).

10.3 The Council is due to approve its revenue budget covering 2021/22 to 2023/24 on the 4 March 2021. Any decisions taken at that meeting on new capital commitments or the revenue budget more widely may influence the TMSS & IS. If Members do decide to invest in capital as part of the Recovery from Covid 19 they must do so being fully aware of any associated revenue impacts as a result of that investment.

10.4 The Council has received the draft revenue and capital budget settlement from the Scottish Government for financial year 2021/22. In addition, the Scottish Government has undertaken its capital spending review which provides an outline five-year indicative allocation for general capital grant and other specific funding streams provided through the local government finance settlement. Core capital grant allocations are expected to remain at their current levels over the five year period with some additional funds available for scheme in specific areas such as flood prevention and low-carbon schemes.

10.5 The Council intends to develop its Capital Strategy which is intended to provide the following: -

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

The Capital Strategy will include capital expenditure, investments and liabilities and treasury management in sufficient detail to allow all members to understand how stewardship, value for money, prudence, sustainability and affordability will be secured. The Capital Strategy is being developed as a precursor to a new capital programme to better inform and justify future investment decisions. These decisions are complex and inter-related and include:

- Links to the Council's broad programme of commitments
- The Council's investment philosophy such as place, low carbon, digital and partnerships
- Links to the Strategic Asset Management Strategy
- Capital governance by Members and those delegated to Officers
- Agreed approaches and decision-making relating to projects: prioritisation, scope and management
- The way in which affordability is determined and how that links to medium term financial planning.

10.6 As outlined in section 9 wider economic uncertainties at the time of writing this report have seen significant volatility in borrowing rates. Borrowing rates for both short and long term debt are close to historic lows and as always a balance will need to be struck between the security afforded by long term borrowing compared to the lower rates available on short term borrowing.

11. Borrowing Strategy

11.1 Over the past few years the Council has benefitted from lower borrowing costs due to low interest rates by using short term temporary borrowing and internal borrowing (use of existing cash). During financial year 2020/21, in order to achieve savings, the Council made the best use of the low rates available on temporary borrowing. There has been no PWLB borrowing undertaken since March 2020.

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and it helps mitigate counterparty risk.

11.2 During 2021/22 the Council plans to continue to use short term borrowing to fund the capital programme but will need to consider long term borrowing to replace maturities, in order to manage refinancing risk.

Considering the risks within the economic forecast, caution will be adopted with 2021/22 treasury operations. The Executive Chief Officer, Finance and Resources will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances. Any decisions will be reported to the appropriate committee at the next available opportunity.

The Council will ensure its strategy remains flexible, and will give consideration to new borrowing from the following sources based on prevailing market conditions:

1. Short dated borrowing from non PWLB sources through the Sterling Money Market.
2. Appropriately dated PWLB borrowing.
3. Long term fixed/variable rate market loans from the Sterling Money Market at rates significantly below PWLB rates for the equivalent maturity period (where available) and to maintaining an appropriate balance between PWLB and market debt in the debt portfolio.
4. Consideration of any government supported or promoted lending initiatives, which may offer attractive sources of finance e.g. low-cost borrowing for specific energy efficiency projects.

11.3 Sensitivity of the forecast – In normal circumstances the main sensitivities of the forecast are likely to be the two scenarios noted below. The Council officers, in conjunction with the treasury advisers, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- *if it were felt that there was a significant risk of a sharp FALL in long and short term rates,* e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then medium/ long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- *if it were felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast,* perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised.

Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

11.4 External v. Internal Borrowing

As reflected in the table below, the Council's objective is to maintain a level of temporary investments which will ensure a level of liquid cash available to the Council. The level shown takes account of the level of Council reserves and balances, and potential for these to be utilised through planned use or unforeseen events. Through this approach, the Council seeks to mitigate re-financing risk, particularly were the Council's reserves to be eroded due to unforeseen events.

Comparison of gross and net debt positions at year end

	2019/20 Actual	**2020/21 Estimate**	**2021/22 Estimate**	**2022/23 Estimate**	**2023/24 Estimate**
External Debt (gross)	£1,032.5m	£1,009.5m	£1,076.4m	£1,120.5m	£1,142.8m
Temporary Investments	£91.5m	£50.0m	£50.0m	£50.0m	£50.0m
External Debt (net)	**£941.0m**	**£959.5m**	**£1,026.4m**	**£1,070.5m**	**£1,092.9m**

The Table above excludes long-term liabilities e.g. PPP/NPD (Public Private Partnership/non Profit Distributing) schemes

- Another factor in considering the level of investments held is the difference between borrowing rates and investment rates to ensure the Council obtains value for money once an appropriate level of risk management has been attained to ensure the security of its investments and mitigating of re-financing risk.
- Following the PWLB Lending terms consultation by the Treasury on PWLB borrowing, on 25 November 2020, standard and certainty margins reduced by 1% and rates are not forecast to rise significantly over the next few years. However, short-term borrowing rates continue to be more favourable. In the long-term the Bank Rate is not expected to rise above 0.10%.
- The Treasury Team will monitor the interest rate market, take advice from our treasury advisor, and adopt a pragmatic approach to changing circumstances, reporting any decisions to the Corporate Resources Committee at the next available opportunity.

11.5 Policy on borrowing in advance of need

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

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

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need.

- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered.
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow.
- consider the merits and demerits of alternative forms of funding.
- consider the prevailing and projected interest rates based on best available information.
- Consider appropriate maturity profiles of new borrowing.
- consider the impact of borrowing in advance on temporarily (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk, and other risks, and the level of such risks given the controls in place to minimise them.

The maximum extent to which borrowing in advance would be undertaken will be based upon the existing and projected capital financial requirement, and existing level of debt.

12. Debt Rescheduling

12.1 At this time, and due to the early repayment penalties imposed by the PWLB, the opportunities for debt rescheduling are not cost effective. However, this position will be kept under regular review. All rescheduling will be reported to the Corporate Resources Committee, at the earliest meeting following its action.

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

- the generation of cash savings and/or discounted cash flow savings,
- helping to fulfil the strategy outlined in section 11 above, and
- to enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

13. Annual Investment Strategy

13.1 Investment Policy

The Council's investment policy has regard to the Scottish Government's Investments Investment (Scotland) Regulations, (and accompanying Finance Circular), and the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017, ("the CIPFA TM Code"). **The Council's investment priorities will be**

1. **Security**
2. **Liquidity**
3. **Yield**

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

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

The Council's policies in relation to Investment instruments and counter-parties identified for use are listed in **Appendices 4, 5, 6, 7 and 8** and explanatory notes on investment types and risks are detailed in **Appendix 9**.

13.2 Creditworthiness policy

The Council recognises the vital importance of credit-worthiness checks on the counterparties it uses for investments.

This Council uses the creditworthiness service provided by Link. This service employs a sophisticated modelling approach with credit ratings from all three rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings of counterparties are supplemented with further credit overlays to provide a colour coded system based on recommended durational band for use of the counter-party.

This Council does not use the approach suggested by CIPFA of using the lowest rating from all three rating agencies to determine creditworthy counterparties. The Link creditworthiness service uses a wider array of information than just primary ratings, from all three agencies and using a risk weighted scoring system, does not give undue consideration to just one agency's ratings.

The Link creditworthiness service is used on an advisory basis, with the decision on creditworthiness ultimately resting with the Treasury Team.

13.3 Foreign Exposures/Country limits

In relation to Money Market Funds, only AAA rated Sterling denominated funds will be used.

At present the Council uses mainly UK based institutions for investment (AA rating) and should the UK's credit rating be downgraded the Council will review its requirement and use AA- rated and above counterparties.

Examples of the institutions that the Council will invest in include UK banks and building societies, UK Local Authorities, non-UK banks and building societies of high credit worthiness, HM Treasury Debt Management Office.

The Council continues to use non-UK counterparties of high credit worthiness. The Link rating model is used in the same way as for UK institutions. In addition to UK counterparties, only institutions registered in countries with an AAA or AA+ credit rating will be considered. The list of countries where the Council will consider investing is at **Appendix 7**.

13.4 Investment Strategy

In-house funds are mainly cash-flow derived and investments will be made in accordance with cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments of up to 12 months).

13.5 Investment return expectations

As detailed in section 9, the Link group's view of interest rates, the Bank Rate is forecast to remain at its current rate, 0.10%, for the foreseeable future.

There are upside risks to these forecasts (i.e. increases in Bank Rate occurs sooner) if economic growth remains strong and unemployment falls faster than expected. However, should the pace of growth fall back, there could be downside risk.

The Council will avoid locking into longer term deals unless attractive rates are available with counterparties of particularly high creditworthiness which make longer term deals worthwhile and within the risk parameters set.

13.6 End of Year Investment Report

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report. Forecasts of investment balances for the next three years are provided in **Appendix 1**.

13.7 Policy on the Use of External Service Providers

The Council's tendered Treasury Management advisor contract is subject to regular review. The Council currently uses Link as its external treasury management advisers. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed, are properly agreed and documented, and subject to regular review.

The Council recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources.

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

13.8 Treasury Management Responsibilities

The Treasury Management Scheme of Delegation and Role of the Section 95 Officer are at **Appendix 10.**

Designation: Executive Chief Officer- Finance and Resources

Date: 15 February 2021

Author: Edward Foster

Background Papers: Treasury Live system reports, Link economic forecasts

https://www.highland.gov.uk/download/meetings/id/77562/item_17_highland_council_capital_plan_201819_to_202223_%E2%80%93_update_report

Received by Committee Services: 15 February 2021 at 13:53

Appendices

1. Prudential and Treasury Indicators
2. Economic Background
3. Treasury Management Policy
4. Permitted Investments – Common Good, Charitable, Educational and Other Trust Funds
5. Permitted Investments – Non-treasury Investments
6. Permitted Investments – Treasury Management
7. Approved countries for investment
8. Current counter party list as at 31/12/2020
9. Treasury Management Practice 1 (TMP1) Credit and Counterparty Risk Management
10. Treasury Management Scheme of Delegation and Role of the Section 95 Officer
11. Commitment to repay loan fund advances (General Fund)
12. Commitment to repay loan fund advances (HRA)

Appendix 1

Prudential and Treasury Indicators

The borrowing set out within the Prudential Indicators is based upon the General Fund capital programme agreed by the Council in March 2018 which was reprofiled and approved by Council in January 2021. The 5-year HRA capital plan is currently being developed and interim estimates of HRA new build borrowing have been provided for the purpose of this document. The Estimates of Capital Expenditure below in indicator 3 and 4 include expenditure in relation to the National Housing Trust which is self-financing.

A. Indicators for Affordability, Prudence and Capital Expenditure

Indicator 1 - Capital Expenditure

Gross Capital Expenditure

In absolute terms rather than as a ratio, these show the overall levels of estimated capital investment irrespective of how they are being funded.

	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
General Fund	£104.3m	£96.0m	£57.0m	£132.2m	£128.4m	£74.3m
HRA	£50.7m	£41.9m	£50.9m	£48.5m	£48.5m	£48.5m
Total	**£155.0m**	**£137.9m**	**£107.9m**	**£180.7m**	**£176.9m**	**£122.8m**
Income						
General Fund	(£48.0m)	(£64.9m)	(£41.6m)	(£51.2m)	(£69.9m)	(£36.7m)
HRA	(£17.7m)	(£15.0m)	(£24.2m)	(£19.5m)	(£19.5m)	(£19.5m)
Total	**(£65.7m)**	**(£79.9m)**	**(£65.8m)**	**(£70.7m)**	**(£89.4m)**	**(£56.2m)**

Net Capital Expenditure is the borrowing or funding requirement for new capital investment in each year.

General Fund	£56.3m	£31.1m	£15.4m	£81.0m	£58.5m	£37.6m
HRA	£33.0m	£26.9m	£26.7m	£29.0m	£29.0m	£29.0m
Total	**£89.3m**	**£58.0m**	**£42.1m**	**£110.0m**	**£87.5m**	**£66.6m**

Loan charge instalments (based on no change to asset lives)

General Fund	(£30.3m)	(£30.8m)	(£30.7m)	(£30.9m)	(£31.4m)	(£31.0m)
HRA	(£9.2m)	(£10.1m)	(£9.6m)	(£11.2m)	(£11.2m)	(£12.3m)
Total	**(£39.5m)**	**(£40.9m)**	**(£40.3m)**	**(£42.1m)**	**(£42.6m)**	**(£43.3m)**

Additional net borrowing in year

General Fund	£26.0m	£0.3m	(£15.3m)	£50.1m	£27.1m	£6.6m
HRA	£23.8m	£16.8m	£17.1m	£17.8m	£17.8m	£16.7m
Total	**£49.8m**	**£17.1m**	**£1.8m**	**£67.9m**	**£44.9m**	**£23.3m**

Indicator 2 – Capital Financing Requirement (CFR)

These indicators represent the level of the Council's underlying need to borrow or finance by other long-term liabilities for a capital purpose. This includes past and future borrowing or funding.

	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
General Fund excluding PPP/NPD	£738.9m	£716.1m	£723.5m	£773.6m	£800.7m	£807.3m
PPP/NPD	£148.8m	£142.1m	£142.1m	£135.7m	£129.3m	£122.3m
HRA	£287.8m	£301.7m	£304.9m	£322.7m	£340.5m	£357.1m
Total	**£1,175.5m**	**£1,159.9m**	**£1,170.5m**	**£1,232.0m**	**£1,270.5m**	**£1,286.7m**
Joint Boards	£18.0m	£17.1m	£17.1m	£16.1m	£15.3m	£14.4m
Total CFR (incl Police/Fire) (1)	**£1,193.5m**	**£1,177.0m**	**£1,187.6m**	**£1,248.1m**	**£1,285.8m**	**£1,301.1m**

Treasury Position This indicator shows the expected borrowing position, net of investments.

	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Gross Borrowing – long term	£859.0m	£799.3m	£821.5m	£806.2m	£774.4m	£763.6m
Gross Borrowing – short term	£173.5m	£209.6m	£188.0m	£270.2m	£346.1m	£379.2m
Total External Borrowing	**£1,032.5m**	**£1,008.9m**	**£1,009.5m**	**£1,076.4m**	**£1,120.5m**	**£1,142.8m**
Other Long-Term Liabilities	£148.8m	£142.1m	£142.1m	£135.7m	£129.3m	£122.3m
Total Gross Debt (2)	**£1,181.3m**	**£1,151.0m**	**£1,151.6m**	**£1,212.1m**	**£1,249.8m**	**£1,265.1m**
Investments	(£91.5m)	(£50.0m)	(£50.0m)	(£50.0m)	(£50.0m)	(£50.0m)
Net Borrowing	**£1,089.8m**	**£1,101.0m**	**£1,101.6m**	**£1,162.1m**	**£1,199.8m**	**£1,215.1m**

Difference between CFR (1) and Total Gross Debt (2)

This indicator shows the difference between the Capital Financing Requirement, and the Estimated Gross Debt. The difference represents an 'under-borrowed' position, with capital financed from internal cash flows.

	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2024/25 Estimate
Difference between CFR (1) and Total Gross Debt (2)	£12.2m	£26.0m	£36.0m	£36.0m	£36.0m	£36.0m

Indicator 3 – Authorised Limit for Borrowing

The Authorised Limit is the maximum level of external borrowing which should not be exceeded. The limit is linked to the estimated level of capital financing requirement, with some capacity for variations from that sum e.g. if capital expenditures are exceeded.

Authorised Limit	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Borrowing	£1,054.6m (indicator £1,049.7m)	£1,063.1m	£1,063.1m	£1,129.4m	£1,167.8m	£1,184.7m
Other Long-Term Liabilities	£148.8m	£142.1m	£142.1m	£135.7m	£129.3m	£122.3m

Indicator 4 - Operational Boundary for Borrowing

An Operational Boundary is also required which represents the Executive Chief Officer, Finance and Resources' estimate of the day to day limit for the Treasury Management activity based on the most likely i.e. prudent but not worse-case scenario.

Operational Boundary	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Borrowing	£1,054.6m (indicator £1,013.7m)	£1,037.0m	£1,037.0m	£1,093.4m	£1,131.8m	£1,148.7m
Other Long-Term Liabilities	£148.8m	£142.1m	£142.1m	£135.7m	£129.3m	£122.3m

Indicator 5 – Ratio of financing costs to net revenue stream

These indicators show the capital financing costs (interest charges, the provision for the repayment of debt and the financing of PPP/NPD outstanding capital investment liability) as a percentage of government grant (revenue), Council Tax, Rents and other income. This allows the authority to track how much of its annual income is needed to pay for its capital investment plans and outstanding funding liabilities compared to its day to day running costs.

	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
General Fund including PPP/NPD	13.0%	13.2%	13.2%	13.1%	13.4%	13.5%
Housing Revenue Account	36.4%	38.0%	37.8%	40.7%	40.5%	42.3%

Indicator 6- Interest rate exposures of debt net of investments

Interest rate exposures of debt net of investments are required to be set in compliance with the Code. This limits the Council's exposure to both fixed and variable interest rate movements as part of the overall risk management strategy for Treasury Management activities. It promotes a prudent strategy aimed to avoid the adverse effects of fluctuating interest rates. The limits are based on the Capital Financing Requirement (CFR) with variable exposures limited to 35% of the CFR.

Interest rate exposures of debt net of investments	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Upper Limit (Fixed)	£996.1m (indicator £1,034.9m)	£1,034.8m	£1,034.8m	£1,112.4m	£1,156.5m	£1,178.9m
Upper Limit (Variable)	£55.1m (indicator £361.8m)	£362.2m	£362.2m	£389.3m	£404.8m	£412.6m

Maturity structure of fixed rate borrowing during 2020/21

This indicator identifies the amount of debt maturing in specified periods. The overarching principle is that steps should be taken to limit exposure to significant refinancing risk in any short period of time. The Council currently applies the prudent practice of ensuring that no more than 30% of its total gross fixed rate debt matures in any one financial year unless triggered through specific debt restructuring exercises.

	upper limit	lower limit
under 12 months	30%	0%
12 months and within 24 months	30%	0%
24 months and within 5 years	40%	0%
5 years and within 10 years	50%	0%
10 years and above	100%	25%

Maximum principal invested for period longer than 365 days

The maximum total principal sum which may be invested with a maturity for a period longer than 365 (366 in a leap year) days and within the permitted investment limits is £20m.

Appendix 2

Economic Background Provided by Link (as at 10 February 2021)

UK

The Bank of England's Monetary Policy Committee (MPC) kept **Bank Rate** and quantitative easing (QE) unchanged on 4 February. However, it revised its economic forecasts to take account of a third national lockdown which started on 5 January, which is obviously going to delay economic recovery and do further damage to the economy. Moreover, it had already decided in November to undertake a further tranche of quantitative easing (QE) of £150bn, to start in January when the previous programme of £300bn of QE, announced in March to June 2020, finished. As only about £16bn of the latest £150bn tranche had been used towards the end of January, it felt that there was already sufficient provision for QE - which would be made to last to the end of 2021. This implied that the current rate of purchases of £4.4bn per week would be slowed during the year.

Although its short-term forecasts were cut for 2021, the medium-term forecasts were more optimistic than in November, based on an assumption that the current lockdown will be gradually eased after Q1 as vaccines are gradually rolled out and life can then start to go back to some sort of normality. The Bank's main assumptions were:

- The economy would start to **recover strongly** from Q3 2021.
- **£125bn of savings** made by consumers during the pandemic will give a significant boost to the pace of economic recovery once lockdown restrictions are eased and consumers can resume high street shopping, going to pubs and restaurants and taking holidays.
- The economy would still recover to reach its **pre-pandemic level** by Q1 2022 despite a long lockdown in Q1 2021.
- **Spare capacity** in the economy would be eliminated in Q1 2022.
- The Bank also expects there to be **excess demand** in the economy by Q4 2022.
- **Unemployment** will peak at around 7.5% during late 2021 and then fall to about 4.2% by the end of 2022. This forecast implies that 0.5m foreign workers will have been lost from the UK workforce by their returning home.
- **CPI inflation** was forecast to rise quite sharply towards the 2% target in Q1 2021 due to some temporary factors, (e.g. the reduction in VAT for certain services comes to an end) and given developments in energy prices. CPI inflation was projected to be close to 2% in 2022 and 2023.
- The Monetary Policy Report acknowledged that there were **downside risks** to their forecasts e.g. from virus mutations, will vaccines be fully effective, how soon can tweaked vaccines be devised and administered to deal with mutations? There are also issues around achieving herd immunity around the world from this virus so that a proliferation of mutations does not occur which prolong the time it takes for the global economy to fully recover.
- The Report also mentioned a potential **upside risk** as an assumption had been made that consumers would only spend £6bn of their savings of £125bn once restrictions were eased. However, the risk is that that consumers could spend a lot more and more quickly.
- The Bank of England also removed **negative interest rates** as a possibility for at least six months as financial institutions were not yet ready to implement them. As in six months' time the economy should be starting to grow strongly, this effectively means that negative rates occurring are only a slim possibility in the current downturn. However, financial institutions have been requested to prepare for them so that, at a future time, this could be used as a monetary policy tool if deemed appropriate. (**Gilt yields and PWLB rates** jumped upwards after the removal of negative rates as a key risk in the short-term.)
- Prior to 4 February, the **MPC's forward guidance** outlined that the sequencing of a withdrawal of monetary policy support would be that Bank Rate would be increased first,

and only once it had reached a certain level, 'around 1.5%', before a start would be made on winding down the stock of asset purchases made under QE. However, the MPC decided at the February meeting that this policy should be reviewed as to whether a start should be made first on **winding down QE** rather than raising Bank Rate.

- The MPC reiterated its previous guidance that Bank Rate would not rise until inflation was sustainably above 2%. This means that it will tolerate inflation running above 2% from time to time to balance out periods during which inflation was below 2%. This is termed **average inflation targeting.**

- **There are two views in respect of Bank Rate beyond our three-year time horizon:**
  1. The MPC will be keen to raise Bank Rate as soon as possible in order for it to be a usable tool when the next economic downturn comes along. This is in line with thinking on Bank Rate over the last 20 years.
  2. Conversely, that we need to adjust to the new post-pandemic era that we are now in. In this new era, the shift to average inflation targeting has set a high bar for raising Bank Rate i.e. only when inflation is demonstrably sustainably above 2%. In addition, many governments around the world have been saddled with high levels of debt. When central bank rates are low, and below the average GDP growth rate, the debt to GDP ratio will gradually fall each year without having to use fiscal tools such as raising taxes or austerity programmes, (which would depress economic growth and recovery). This could therefore result in governments revising the setting of mandates to their national central banks to allow a higher rate of inflation linked to other economic targets. This is the Capital Economics view – that Bank Rate will not rise for the next five years and will probably then struggle to get to 1% within 10 years.

- **Public borrowing** was forecast in November 2020 by the Office for Budget Responsibility (the OBR) to reach £394bn in the current financial year, the highest ever peace time deficit and equivalent to 19% of GDP. In normal times, such an increase in total gilt issuance would lead to a rise in gilt yields, and so PWLB rates. However, the QE done by the Bank of England has depressed gilt yields to historic low levels, (as has similarly occurred with QE and debt issued in the US, the EU and Japan). This means that new UK debt being issued, and this is being done across the whole yield curve in all maturities, is locking in those historic low levels through until maturity. In addition, the UK has one of the longest average maturities for its entire debt portfolio, of any country in the world. Overall, this means that the total interest bill paid by the Government is manageable despite the huge increase in the total amount of debt. The OBR was also forecasting that the government will still be running a budget deficit of £102bn (3.9% of GDP) by 2025/26. However, initial impressions are that they have taken a pessimistic view of the impact that vaccines could make in the speed of economic recovery. It is now likely that total borrowing will probably reach around £420bn due to further Government support measures introduced as a result of further restrictions and the third national lockdown.

- Overall, **the pace of recovery** was not expected to be in the form of a rapid V shape, but a more elongated and prolonged one. The initial recovery was sharp after quarter 1 saw growth at -3.0% followed by -18.8% in quarter 2 and then an upswing of +16.0% in quarter 3; this still left the economy 8.6% smaller than in Q4 2019. While the one month second national lockdown that started on 5th November caused a further contraction of 5.7% m/m in November, this was much better than had been feared and showed that the economy is adapting to new ways of working. This left the economy 'only' 8.6% below the pre-crisis level. However, a strong recovery from a further contraction during quarter 1 2021 is expected in the second half of 2021 and is likely to mean that the economy recovers to its pre-pandemic level during Q1 2022.

- **Vaccines** The Pfizer announcement on 9 November of a successful vaccine has been followed by approval of the Oxford University/AstraZeneca and Moderna vaccines. The Government has set a target to vaccinate 14 million people in the most at risk sectors of the population by 15 February; it has made good, and accelerating progress in hitting that target. The aim is also to vaccinate all over 50s by May and all adults by September. This means that the national lockdown starting in early January, could be replaced by regional tiers of lighter restrictions, beginning possibly in Q2. At that point, there would be less reason to fear that hospitals could become overwhelmed any more. Effective vaccines have radically improved the economic outlook so that it may now be possible for GDP to recover to its pre-virus level as early as Q1 2022. These vaccines have enormously boosted confidence that **life could largely return to normal during the second half of 2021**. With the household saving rate having been exceptionally high since the first lockdown in March, there is plenty of pent-up demand and purchasing power stored up for when life returns to normal.

- Provided that both monetary and fiscal policy are kept loose for a few years yet, then it is still possible that **in the second half of this decade**, the economy may be no smaller than it would have been if COVID-19 never happened. The major concern though, is that new mutations of the virus might defeat the current batch of vaccines. However, work is already advanced to produce what may well become annual revaccinations each autumn with updated vaccines. In addition, countries around the world have ramped up vaccine production facilities and vastly improved testing regimes; they are therefore now much better equipped to deal effectively with any new outbreaks of mutations of this virus.

It would be consistent with the government deficit falling to around 2.5% of GDP without any tax increases. This would be in line with the OBR's most optimistic forecast in the graph below, rather than their current central scenario which predicts a 4% deficit due to assuming much slower growth. However, Capital Economics forecasts in the graphs above and below, assumed that politicians do not raise taxes or embark on major austerity measures and so, (perversely!), depress economic growth and recovery.

- There will still be some **longer-term adjustments** as e.g. office space and travel by planes, trains and buses may not recover to their previous level of use for several years, or possibly ever, even if vaccines are fully successful in overcoming the current virus. There is also likely to be a **reversal of globalisation** as this crisis has exposed how vulnerable long-distance supply chains are. On the other hand, **digital services** are one area that has already seen huge growth.
- **Brexit.** The final agreement of a trade deal on 24.12.20 has eliminated a significant downside risk for the UK economy. The initial agreement only covers trade so there is further work to be done on the services sector where temporary equivalence has been granted in both directions between the UK and EU; that now needs to be formalised on a permanent basis. However, it is evident from problems with trade flows at ports in January and February, that work needs to be done to smooth out the issues and problems that have been created by complex customs paperwork, in order to deal with bottle necks currently being caused.
- **Fiscal policy.** In December, the Chancellor made a series of announcements to provide further support to the economy: -
  - An extension of the COVID-19 loan schemes from the end of January 2021 to the end of March.
  - The furlough scheme was lengthened from the end of March to the end of April.
  - The Budget on 3.3.21 will lay out the "next phase of the plan to tackle the virus and protect jobs". This does not sound like tax rises are imminent, (which could hold back the speed of economic recovery).

- The **Financial Policy Committee** (FPC) report on 6 August 2020 revised down the expected credit losses for the banking sector to "somewhat less than £80bn". It stated that in its assessment, "banks have buffers of capital more than sufficient to absorb the losses that are likely to arise under the MPC's central projection". The FPC stated that for real stress in the sector, the economic output would need to be twice as bad as the MPC's projection, with unemployment rising to above 15%.

USA

- Following elections for two senate seats in January, the Democrats now have a majority in the House of Representatives and a very slim majority in the Senate based on the vice president's casting vote. As the Democrats will be dependent on gaining the support of moderate Democrat senators, there will be a limit on just how radical they can be with their legislative and financial programmes. The $900bn fiscal stimulus passed in December will help the economy gain more traction in early 2021. There is a question mark, however, over whether they will be able to get a much bigger $1.9bn fiscal stimulus through both houses, though a smaller package would stand much more chance of being approved. The rapid roll out of vaccines is well on course to vaccinate nearly the entire population by the end of the summer; this will help to underpin a strong economic recovery in 2021 after the economy wilted during Q4 2020 as more restrictions were imposed to contain the pandemic.

- After Chair Jerome Powell unveiled the **Fed's adoption of a flexible average inflation target** in his Jackson Hole speech in late August 2020, the mid-September meeting of the Fed agreed by a majority to a toned down version of the new inflation target in his speech - that *"it would likely be appropriate to maintain the current target range until labour market conditions were judged to be consistent with the Committee's assessments of maximum employment and inflation had risen to 2% and was on track to moderately exceed 2% for some time."* This change was aimed to provide more stimulus for economic growth and higher levels of employment and to avoid the danger of getting caught in a deflationary "trap" like Japan. It is to be noted that inflation has actually been under-shooting the 2% target significantly for most of the last decade, (and in 2020), so financial markets took note that higher levels of inflation are likely to be in the pipeline; long-term bond yields duly rose after the meeting. The FOMC's updated economic and rate projections in mid-September showed that under this new regime of average inflation targeting, that officials expected to leave the fed funds rate at near-zero until at least end-2023 and probably for another year or two beyond that. Where the Fed has led in changing its monetary policy to one based on average inflation targeting in response to the damage that this pandemic has done to the economy, there was much expectation that other major central banks would also follow suit.

- Subsequent meetings of the Fed have projected that **inflation** will not get back sustainably to above 2% for some years and so the vast majority of Fed officials expect the Fed funds rate to still be at near-zero until 2024 or later. The key message is that policy will remain unusually accommodative – with near-zero rates and asset purchases continuing for several more years. This is likely to result in keeping Treasury yields lower than might otherwise be expected, although treasury yields have increased somewhat due to financial markets adjusting to expectations of higher rates of inflation.

EU

- The economy was recovering well from the first lockdowns towards the end of Q2 and during Q3 after a sharp drop in GDP. However, a second wave of the virus has caused a renewed fall back in growth during Q4. The slow role out of vaccines during Q1 2021 will delay economic recovery. In Q2 of 2020, GDP was 15% below its pre-pandemic level. But in Q3 the economy grew by 12.5% q/q leaving GDP down by "only" 4.4%. That was much

better than had been expected earlier in the year. However, growth contracted by another 0.7% in Q4 and is likely to at least stagnate during Q1 of 2021, as a second wave of the virus has seriously affected many countries. The €750bn fiscal support package eventually agreed by the EU after prolonged disagreement between various countries, is unlikely to provide significant support, and quickly enough, to make an appreciable difference in the countries most affected by the first wave.

- With inflation expected to be unlikely to get much above 1% over the next two years, the ECB has been struggling to get inflation up to its 2% target. It is currently unlikely that it will cut its central rate even further into negative territory from -0.5%, although the ECB has stated that it retains this as a possible tool to use. The ECB's December meeting added a further €500bn to the PEPP scheme, (purchase of government and other bonds), and extended the duration of the programme to March 2022 and re-investing maturities for an additional year until December 2023. Three additional tranches of TLTRO, (cheap loans to banks), were approved, indicating that support will last beyond the impact of the pandemic, implying indirect yield curve control for government bonds for some time ahead. The Bank's forecast for a return to pre-virus activity levels was pushed back to the end of 2021, but stronger growth is projected in 2022. The total PEPP scheme of €1,850bn of QE which started in March 2020 is providing protection to the sovereign bond yields of weaker countries like Italy. There is therefore unlikely to be a euro crisis while the ECB is able to maintain this level of support. However, as in the UK and the US, the advent of highly effective vaccines will be a game changer once the EU can get a comprehensive vaccination scheme up and running, although growth will struggle before later in quarter 2 of 2021.

CHINA

After a concerted effort to get on top of the virus outbreak in Q1, economic recovery was strong in the rest of 2020; this has enabled China to recover all of the contraction in Q1. Policy makers have both quashed the virus and implemented a programme of monetary and fiscal support that has been particularly effective at stimulating short-term growth. At the same time, China's economy has benefited from the shift towards online spending by consumers in developed markets. These factors help to explain its comparative outperformance compared to western economies. However, this was achieved by major central government funding of yet more infrastructure spending. After years of growth having been focused on this same area, any further spending in this area is likely to lead to increasingly weaker economic returns in the longer term. This could, therefore, lead to a further misallocation of resources which will weigh on growth in future years.

JAPAN

A third round of fiscal stimulus in early December took total fresh fiscal spending this year in response to the virus close to 12% of pre-virus GDP. That's huge by past standards, and one of the largest national fiscal responses. The budget deficit is now likely to reach 16% of GDP this year. Coupled with Japan's relative success in containing the virus without draconian measures so far, and the likelihood of effective vaccines being available in the coming months, the government's latest fiscal effort should help ensure a strong recovery and to get back to pre-virus levels by Q3 2021 – around the same time as the US and much sooner than the Eurozone. However, on the negative side, it has also been struggling - despite huge monetary and fiscal stimulus - to get out of a deflation trap for many years and to achieve consistent, significant GDP growth. Moreover, it has not consistently managed to raise inflation up to its target level of 2% and it is making little progress on fundamental reform of the economy.

WORLD GROWTH

- World growth has been in recession in 2020 and this is likely to continue into the first half of 2021 before recovery in the second half. Inflation is unlikely to be a problem for some

years due to the creation of excess production capacity and depressed demand caused by the coronavirus crisis.

- Until recent years, world growth has been boosted by increasing globalisation i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last thirty years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy. The Chinese government has targeted achieving major world positions in specific key sectors and products, especially high-tech areas and production of rare earth minerals used in high tech products. It is achieving this by massive financial support, (i.e. subsidies), to state owned firms, government directions to other firms, restrictions on market access by foreign firms and informal targets for the domestic market share of Chinese producers in the selected sectors. This is regarded as being unfair competition that is putting western firms at an unfair disadvantage or even putting some out of business. It is also regarded with suspicion on the political front as China is an authoritarian country that is not averse to using economic and military power for political advantage. The current trade war between the US and China therefore needs to be seen against that backdrop. It is, therefore, likely that we are heading into a period where there will be a reversal of world globalisation and a decoupling of western countries from dependence on China to supply products. This is likely to produce a backdrop in the coming years of weak global growth and so weak inflation.

Summary

Central banks are, therefore, likely to support growth by maintaining loose monetary policy through keeping rates very low for longer. Governments could also help a quicker recovery by providing more fiscal support for their economies at a time when total debt is affordable due to the very low rates of interest. They will also need to avoid significant increases in taxation or austerity measures that depress demand and the pace of recovery in their economies.

If there is a huge surge in investor confidence as a result of successful vaccines which leads to a major switch out of government bonds into equities, which, in turn, causes government debt yields to rise, then there will be pressure on central banks to actively manage debt yields by further QE purchases of government debt; this would help to suppress the rise in debt yields and so keep the total interest bill on greatly expanded government debt portfolios within manageable parameters. It is also the main alternative to a programme of austerity.

INTEREST RATE FORECASTS

The balance of risks to the UK

- The overall balance of risks to economic growth in the UK is now probably more to the upside but is subject to major uncertainty due to the virus - both domestically and its potential effects worldwide.
- There is relatively little domestic risk of increases or decreases in Bank Rate in the near-term, nor significant changes in shorter-term PWLB rates. The Bank of England has effectively ruled out the use of negative interest rates anytime soon but increases in Bank Rate are likely to be some years away given the underlying economic expectations. However, it is always possible that safe haven flows, due to unexpected domestic

developments and those in other major economies, could impact gilt yields, (and so PWLB rates).

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- **Mutations** of the virus render current vaccines ineffective, and tweaked vaccines to combat these mutations are delayed, resulting in further national lockdowns or severe regional restrictions.
- **UK government** takes too much action too quickly to raise taxation or introduce austerity measures that depress demand and the pace of recovery of the economy.
- **UK - Bank of England** takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- **UK / EU trade arrangements** – if there was a major impact on trade flows due to complications with customs paperwork or lack of co-operation in sorting out significant issues. A resurgence of the **Eurozone sovereign debt crisis.** The ECB has taken monetary policy action to support the bonds of EU states, with the positive impact most likely for "weaker" countries. In addition, the EU agreed a €750bn fiscal support package. These actions will help shield weaker economic regions for the next two or three years. However, in the case of Italy, the cost of the virus crisis has added to its already huge debt mountain and its slow economic growth will leave it vulnerable to markets returning to taking the view that its level of debt is unsupportable. There remains a sharp divide between northern EU countries favouring low debt to GDP and annual balanced budgets and southern countries who want to see jointly issued Eurobonds to finance economic recovery. This divide could undermine the unity of the EU in time to come.
- Weak capitalisation of some **European banks**, which could be undermined further depending on extent of credit losses resultant of the pandemic.
- **German minority government & general election in 2021.** In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. Angela Merkel has stepped down from being the CDU party leader but she will remain as Chancellor until the general election in 2021. This then leaves a major question mark over who will be the major guiding hand and driver of EU unity when she steps down.
- **Other minority EU governments.** Italy, Spain, Austria, Sweden, Portugal, Netherlands, Ireland and Belgium also have vulnerable minority governments dependent on coalitions which could prove fragile.
- **Austria, the Czech Republic, Poland and Hungary** now form a strongly anti-immigration bloc within the EU, and they had threatened to derail the 7 year EU budget until a compromise was thrashed out in late 2020. There has also been a rise in anti-immigration sentiment in Germany and France.
- **Geopolitical risks,** for example in China, Iran or North Korea, but also in Europe and other Middle Eastern countries, which could lead to increasing safe haven flows.

Upside risks to current forecasts for UK gilt yields and PWLB rates

- **UK -** a significant rise in inflationary pressures e.g. caused by a stronger than currently expected recovery in the UK economy after effective vaccines are administered quickly to the UK population, leading to a rapid resumption of normal life and return to full economic activity across all sectors of the economy.
- The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly within the UK economy, which then necessitates a rapid series of increases in Bank Rate to stifle inflation.

Treasury management policy **Appendix 3**

1.1 Treasury management is defined as:

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

1.2 The Council regards the successful identification, monitoring and control of risk to be key to the effectiveness of its treasury management activities. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council, and any financial instruments entered into to manage these risks.

1.3 The Council acknowledges that effective treasury management will support the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

Investment policy

2.1 The Council's investment policy has regard to the Local Government Investment (Scotland) Regulations (and accompanying finance circular) and the 2017 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). **The Council's investment priorities will be security first, liquidity second, and then yield.**

2.2 The Council will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite of this Council is low in order to give priority to security of its investments. The borrowing of monies purely to invest or on-lend and make a return is unlawful and this Council will not engage in such activity.

2.3 The Council's Treasury Management Consultants provide a creditworthiness matrix to aid the assessment of the risk involved in lending to individual counterparties.

2.4 The Council's detailed policies in relation to Investment instruments and counter-parties identified for use in the financial year are listed in **Appendices 5, 6, 7, 8 and 9** and explanatory notes on investment types and risks are detailed in **Appendix 10**.

Borrowing policy

3.1 The Council will ensure its strategy remains flexible, and will give consideration to new borrowing from the following sources based on prevailing market conditions:

- Short dated borrowing (for a period of 365 days or less, 366 in a Leap Year) from non PWLB sources through the Sterling Money Market.
- Appropriately dated PWLB borrowing.
- Long term fixed rate market loans (for a period greater than 365 days, or 366 in a leap year) from the Sterling Money Market at rates significantly below PWLB rates for the equivalent maturity period (where available) and to maintaining an appropriate balance between PWLB and market debt in the debt portfolio.
- Consideration of any government supported or promoted lending initiatives, which may offer attractive sources of finance e.g. low-cost borrowing for specific energy efficiency projects.

Appendix 4

Permitted Investments – Common Good, Charitable, Educational and Other Trust Funds

The Council approves the following forms of investment instruments for use as permitted investments for these Funds as set out in the Table below (these include internally and externally managed funds):

Investments

	Minimum Credit Criteria	Liquidity risk	Market risk	Max % of total investmt	Max. maturity period
Cash deposits – local authorities, banks, building societies and cash funds such as money market funds	Relevant parameters as per specific investment mandates and/or specific trust deeds	term	yes	Relevant parameters as per specific investment mandates and/or specific trust deeds	
Equities – UK and Overseas		term	yes		
Fixed Income, Index Linked Bonds, Unit Trusts		term	yes		
War Stock		term	no		
Alternative Investments - Property		term	yes		

Permitted Investments – Non-Treasury Investments **Appendix 5**

Definition of non-treasury investments

Regulation 9 of the Local Government Investment (Scotland) Regulations 2010 adds to the normal definition of investments the following categories: -

a) All shareholding, unit holding and bond holding, including those in a local authority owned company, is an investment;
b) Loans to a local authority company or other entity formed by a local authority to deliver services, is an investment;
c) Loans made to third parties are investments;
d) Investment property is an investment.

However, the following loans are excluded from the definition of investments: -

- Loans made by a local authority to another authority or harbour authority using powers contained in Schedule 3, paragraph 10 or 11 of the Local Government (Scotland) Act 1975.

Permitted Investments – Non-Treasury Investments

The Council approves the following forms of investment instruments for use as permitted investments for Non-Treasury Investments as set out in the Table below:

Investments

	Minimum Credit Criteria	**Liquidity risk**	**Market risk**	**Max % of total investments**	**Max. maturity period**
Loans to Companies, including Local Authority owned.	See Regulation Notes below	term	no	See Regulation requirements and current approvals below.	
Shares and Bonds in Companies, including Local Authority owned.		term	no		
Loans to Third Parties including investments in sub-ordinated debt (see note 1 and 2).		instant	no		
Local Authority Investment Properties.		term	no		
Other Investment Deposits (see note 3)		term	no		

Regulation 24. A local authority shall state the limits for the amounts which, at any time during the financial year, may be invested in each type of permitted investment, such limit being applied when the investment is made. The limits may be defined by reference to a sum of money or a percentage of the local authority's overall investments, or both. A local authority may state that a permitted investment is unlimited. Where a limit is not placed on any type of permitted investment the risk assessment must support that categorisation and an explanation provided as to why an unlimited categorisation is recommended.

Regulation 25. The local authority should identify for each type of permitted investment the objectives of that type of investment. Further, the local authority should identify the treasury risks associated with each type of investment, together with the controls put into place to limit

those risks. Treasury risks include credit or security risk of default, liquidity risk – the risks associated with committing funds to longer term investments and market risk – the effect of market prices on investment value.

Regulation 32. The Strategy shall include details of the maximum value and maximum periods for which funds may prudently be invested. The Strategy shall set out the local authority objectives for holding longer term investments. The Strategy shall also refer to the procedures for reviewing the holding of longer-term investments particularly those investments held in properties, shareholdings in companies or joint ventures.

The policy above, and requirements of regulations 24, 25 and 32, will be considered, and reported to members, as part of any report pertaining to new investment proposals.

In Part 1, section 12 of the Regulations, Consent includes as an investment any loan issued to a third party. Such loans are neither capital nor revenue transactions but are often made for Service reasons and for which specific statutory provision exists. For Service reasons these loans may be offered at an interest rate below the market rate. All loans to third parties are classified as investments for the purposes of the Consent. Where the loan is advanced at less than a market interest rate there is an associated loss of investment return which would otherwise have been earned on these monies. The Council's Annual Accounts will recognise and present all loans to third parties as investments.

This Council will refrain from issuing loans to third parties at less than market rate. If, in exceptional circumstances, the Council agrees to issue a loan/s to third parties at less than market rate the associated loss of investment return will be chargeable to the budget of the sponsoring Service. In circumstances where investment risk is a predominant factor the rate chargeable will reflect the equivalent market rate where this is greater than the Council's Loans Fund's most recent actual average interest rate. In all other cases the interest rate chargeable will be the Council's Loans Fund's most recent actual average interest rate.

Current Approvals

Note 1 – Subordinated Debt – the Highland Council, on 25 October 2012, agreed to permit an investment, at a maximum level of £1m for all current and future investments, for a maximum maturity period of 25 years, in 'Hub Co' projects.

Note 2 – Land banking Fund and Loan Advances to Registered Social Landlords (RSLs) – the Council has for many years operated a 'land bank fund'. The fund is used to provide loans and grants to partner organisations (including RSLs), enabling strategic sites to be secured or prepared for development of housing. The Land bank Fund is a revolving facility with loans repaid as land and property is resold or developed.

Note 3 – From May 2005 The Council has held £1.175m of unsecured loan stock in Inverness Airport Business Park Ltd (IABP). Under the Loan Stock Instrument IABP can exercise a right to defer the repayment due to be made to the Council in May 2010 and in May 2015. IABP have exercised this right on both repayment dates so the full amount of Loan Stock due to the council remains outstanding.

Permitted Investments – Treasury Investments **Appendix 6**

The Council's policy in relation to permitted investments is a three-stage process as summarised below.

1. Only use of permitted investments per the investment strategy is allowed. See Appendix 10 for definition of the different types of investment.
2. Credit-worthiness of counter-parties will be assessed having taken advice from the Council's treasury management advisers, Link. Maximum maturity periods for individual counter-parties will be based upon advice from the Adviser, with limits on treasury investments > 365 days as per the prudential indicators and shown below.
3. Counter-party limits, as set out within the investment strategy will be applied.

The following sections explain each aspect of the 3-stage process in further detail.

Stage 1 - Permitted Investments

The Council approves the following forms of investment instruments for use as permitted treasury management investments as set out in the Tables below. While there is a maximum permitted maturity period set out in the Tables, the actual maturity period will be based on an assessment of risk as part of the credit-worthiness assessment (see stage 2).

In relation to Money Market Funds, only AAA rated Sterling denominated funds will be used.

In relation to all other counter-parties, the Council will mainly use UK based institutions but where non-UK counterparties of high credit worthiness are available these may be used. In determining whether a counterparty is UK or non-UK, entities are classified under where their primary regulator is based. The list of countries where the Council can invest are at **Appendix 7**. For example, UK banks and building societies, UK Local Authorities, non-UK banks and building societies of high credit worthiness, HMT Treasury Debt Management Office.

a. Deposits (UK institutions only)

	Minimum Credit Criteria	**Liquidity risk**	**Market risk**	**Max % of total investments** (Stage 2 Below)	**Max. maturity period**
Debt Management Agency Deposit Facility	UK sovereign rating	term	no	**100**	**6 mths**
Term deposits – local authorities	N/A	term	no	**100**	**2 yrs**
Term deposits – banks and building societies	See Stage 2 below	term	yes	**100**	**2 yrs**
Call accounts – banks and building societies	See Stage 2 below	instant	yes	**100**	**1 yr**

b. **Deposits with counterparties currently in receipt of government support/ownership (UK institutions only)**

	Minimum Credit Criteria	Liquidity risk	Market risk	Max % of total investments (Stage 2 Below)	Max. maturity period
UK nationalised banks	See Stage 2 Below	term	limited	**100**	**2 yrs**
Term deposits – banks and building societies	See Stage 2 below	term	limited	**100**	**2 yrs**
UK Government support to the banking sector (implicit guarantee)	See Stage 2 below	term	limited	**100**	**2 yrs**

c. **Collective investment schemes structured as Open-Ended Investment Companies (OEICs) Sterling Deposits Only**

	Minimum Credit Criteria	Liquidity risk	Market risk	Max % of total investments	Max. maturity period
Government Liquidity Funds	AAA	Instant		**100**	**1 year**
Money Market Funds CNAV	AAA	Instant		**100**	**1 year**
Money Market Funds LVNAV	AAA	Instant		**100**	**1 year**
Money Market Funds VNAV	AAA	Instant		**100**	**1 year**

Note 1 – Money Market Funds: These funds invest across a wide spread of short-term instruments such as Government/Treasury issues, short-term corporate paper and Certificates of Deposits. By keeping a short timeframe, these funds attempt to reduce risk. The objective of these Funds is to maintain the net asset value, but they hold assets which can vary in value. Each Money Market Fund is treated as a single counterparty in relation to counter-party limits.

Note 2 - If forward deposits are to be made, the forward period plus the deal period will not exceed one year in aggregate.

Stage 2 – Credit worthiness policy and assessment

This Council uses the creditworthiness service provided by Link. This service employs a sophisticated modelling approach with credit ratings from all three rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings of counterparties are supplemented with the following overlays:

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

This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are also used by the Council to determine the duration for investments.

- All credit ratings are monitored from a weekly list which can be updated daily by Link. The Council is alerted to changes to ratings of all three agencies as these occur through its use of the Link creditworthiness service.
- if a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum criteria, immediate consideration will be given to whether funds should be withdrawn from this counterparty and the timescale for doing this.
- in addition to the use of Credit Ratings the Council will be advised of information in movements in Credit Default Swap against the iTraxx benchmark and other market data on a daily basis via its Passport website. Extreme market movements may result in downgrade of an institution or removal from the Councils lending list.

Based on the Link approach, the Council will therefore use counterparties within the following durational bands:

Yellow	5 years *
Dark pink	5 years for Enhanced cash funds (EMMFs) with a credit score of 1.25
Light pink	5 years for Enhanced cash funds (EMMFs) with a credit score of 1.5
Purple	2 years
Blue	1 year (only applies to nationalised or semi nationalised UK Banks)
Orange	1 year
Red	6 months
Green	100 days
No Colour	Not to be used

*Please note: the yellow colour category is for UK Government debt, or its equivalent, money market funds and collateralised deposits where the collateral is UK Government debt.

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

In relation to Money Market Funds, the Council will use Link's Weekly Investment report, and other regular updates, to ensure its MMF counterparties meet the minimum credit criteria described in the table above.

As set out within the Prudential Indicators, a limit is set on the value of Treasury Investments which can be invested for more than 365 days. The limit is £20m, which represents the maximum sum invested for longer than 365 days. Though the period of investment must be decided using Link credit ratings and maximum limits in permitted investments.

Stage 3 – Counter-party Limits

The limits described below apply to the Council's treasury management operations. Separate limits apply for the Highland Council Pension Fund, with Highland Council limits relating to all operations excluding the Pension Fund. If for unavoidable short-term operational reasons, limits are breached this will be communicated to management at the earliest opportunity.

Due to market volatility in treasury management investments and varying levels of investment it is possible that at any time in the year one category of investment could represent 100% of the portfolio although it is likely that investments will carry greater diversification than this.

No more than £20m can be invested with any single counterparty, with the exception of the nationalised or semi nationalised UK banks (see section B above) where no more than £25m can be invested in each bank.

The Council will place overnight and call deposits with the Council's bankers irrespective of credit rating. The limit on placing call deposits with the Council's bankers is currently £10m for the Highland Council bank accounts.

The Highland Council Pension Fund will place overnight and call deposits with the Council's bankers irrespective of credit rating. The limit on placing call deposits with the Council's bankers is currently £10m. The Pension Fund may also use other suitable counterparties, with a £10m limit applying to each.

Appendix 7

Approved countries for investment (as at 10/02/2021)

If a country rating is downgraded, this will be removed from our approved countries for investment.

This list is based on those countries which have sovereign ratings of AA- or higher, (we show the lowest rating from Fitch, Moody's and S&P) and also, (except - at the time of writing - for Hong Kong, Norway and Luxembourg), have banks operating in sterling markets which have credit ratings of green or above in the Link credit worthiness service.

Based on lowest available rating as at

- AAA
- Australia
- Denmark
- Germany
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland
-
- AA+
- Canada
- Finland
- U.S.A.
-
- AA
- Abu Dhabi (UAE)
- France
-
- AA-
- Belgium
- Hong Kong
- Qatar
- U.K.

Appendix 8

Current counter party list as at 31/12/2020

The following table is for use by the in-house treasury management team and is a list of current counterparties used. However, the use of counterparties depends on credit ratings and the Council may stop using certain counterparty's and/or decide to use alternative counterparties within its permitted investments. If for unavoidable short-term operational reasons, limits are breached this will be communicated to management immediately.

	At time of investment use Link rating Current rating 31/12/20	**Maximum Duration per TMSS**	**Investment limits**	
			Highland Council	**Highland Council Pension Fund (note 1)**
Government Backed Deposits				
Debt Management Agency Deposit Facility	Yellow (5 years)	6 months	Unlimited	Not used
Deposits with Counterparties currently in receipt of Government Support/Ownership				
RBS	Blue (12 mths)	2 years	£25m	£10m
Bank of Scotland	Red (6 mths)	2 years	£20m	Not used
Term deposits (*restricted to £20m invested >365 days*)				
Term deposits – local authorities	Purple (2 years)	2 years	£20m	Not used
Term deposits – banks and building societies (UK only)	Varies	2 years	£20m	Not used
Commonwealth Bank of Australia	Orange (12 mths)	2 years	£20m	Not used
Coventry Building Society	Red (6 mths)	2 years	£20m	Not used
DZ Bank	Orange (12 mths)	2 years	£20m	Not used
Goldman Sachs	Red (6 mths)	2 years	£20m	Not used
Nationwide	Red (6 mths)	2 years	£20m	Not used
Certificates of deposit				
Standard Chartered	Red (6 mths)	1 Year	£20m	Not used
Royal Bank of Scotland	Blue (12 mths)	2 years	£20m	Not used

	At time of investment use Link rating Current rating 31/12/20	Maximum Duration per TMSS	Investment limits	
			Highland Council	Highland Council Pension Fund (note 1)
Call accounts				
Clydesdale Bank (Council's Banker)	N/C – (0 mths)	1 year	£10m	£10m
Barclays	Red (6 mths)	1 year	£20m	Not used
Santander	Red (6 mths)	1 year	£20m	Not used
Svenska Handelsbanken	Orange (12 mths)	1 year	£20m	Not in use
Money Market Funds				
Aberdeen Standard Asset Management	AAA	1 Year	£20m	Not used
Insight Asset Management	AAA	1 Year	£20m	Not used
Blackrock Asset Management	AAA	1 Year	£20m	Not used
Northern Trust	AAA	1 Year	£20m	Not used

Note 1 – the Pension Fund currently uses a limited number of counterparties as shown above. In line with the limits detailed on **appendix 6**, additional counterparties could be considered up to the limits stipulated.

Appendix 9 Treasury Management Practice 1 (TMP1) Credit and Counterparty Risk Management

Type of Permitted Investment	Treasury Risks	Mitigating Controls
a. Deposits with the Debt Management Account Facility (UK Government) (**Very low risk)**	This is a deposit with the UK Government and as such counterparty and liquidity risk is very low, and there is no risk to value. Deposits can be between overnight and 6 months.	Little mitigating controls required. As this is a UK Government investment the monetary limit is unlimited to allow for a safe haven for investments.
b. Deposits with other local authorities or public bodies **(Very low risk)**	These are considered quasi UK Government debt and as such counterparty risk is very low, and there is no risk to value. Liquidity may present a problem as deposits can only be broken with the agreement of the counterparty, and penalties can apply. Deposits with other non-local authority bodies will be restricted to the overall credit rating criteria.	Little mitigating controls required for local authority deposits, as this is a quasi UK Government investment. Non-local authority deposits will follow the approved credit rating criteria.
c. Money Market Funds (MMFs) **(Very low risk)** CNAV, LVNAV, VNAV	Pooled cash investment vehicle which provides very low counterparty, liquidity and market risk. These will primarily be used as liquidity instruments.	Funds will only be used where the MMFs have a “AAA” rated status from either Fitch, Moody’s or Standard and Poor’s.
d. Ultra short dated bond funds **(low risk)**	Pooled cash investment vehicle which provides very low counterparty, liquidity and market risk. These will primarily be used as liquidity instruments.	Funds will only be used where the bonds have a “AAA” rated status from either Fitch, Moody’s or Standard and Poor’s.
e. Call account deposit accounts with financial institutions (banks and building societies) **(Low risk depending on credit rating)**	These tend to be low risk investments but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types of investments, liquidity is high and investments can be returned at short notice.	The counterparty selection criteria approved above restricts lending only to high quality counterparties.

Type of Permitted Investment	Treasury Risks	Mitigating Controls
f. Term deposits with financial institutions (banks and building societies) **(Low to medium risk depending on period & credit rating)**	These tend to be low risk investments but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types of investments, liquidity is low and term deposits can only be broken with the agreement of the counterparty, and penalties may apply.	The counterparty selection criteria approved above restricts lending only to high quality counterparties.
g. Government Gilts and Treasury Bills **(Very low risk)**	These are marketable securities issued by the UK Government and as such counterparty and liquidity risk is very low, although there is potential risk to value arising from an adverse movement in interest rates (no loss if these are held to maturity).	Little counterparty mitigating controls are required, as this is a UK Government investment. The potential for capital loss will be reduced by limiting the maximum monetary and time exposures.
h. Certificates of deposits with financial institutions **(Low risk)**	These are short dated marketable securities issued by financial institutions and as such counterparty risk is low but will exhibit higher risks than categories (a), (b) and (c) above. There is risk to value of capital loss arising from selling ahead of maturity if combined with an adverse movement in interest rates. Liquidity risk will normally be low.	The counterparty selection criteria approved above restricts lending only to high quality counterparties.
i. Structured deposit facilities with banks and building societies (escalating rates, de-escalating rates etc.) **(Low to medium risk depending on period & credit rating)**	These tend to be medium to low risk investments but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types of investments, liquidity is very low and investments can only be broken with the agreement of the counterparty (penalties may apply).	The counterparty selection criteria approved above restricts lending only to high quality counterparties.
j. Corporate bonds **(Medium to high risk depending on period & credit rating)**	These are marketable securities issued by financial and corporate institutions. Counterparty risk will vary and there is risk to value of capital loss arising from selling ahead of maturity if combined with an adverse movement in interest rates. Liquidity risk will be low.	The counterparty selection criteria approved above restricts lending only to high quality counterparties.

Type of Investment	Treasury Risks	Mitigating Controls
k. Investment properties	These are non-service properties which are being held pending disposal or for a longer-term rental income stream. These are highly illiquid assets with high risk to value (the potential for property prices to fall or for rental voids).	In larger investment portfolios some small allocation of property-based investment may counterbalance/compliment the wider cash portfolio. Property holding will be re-valued regularly and reported annually with gross and net rental streams.
l. Loans to third parties, including soft loans	These are service investments either at market rates of interest or below market rates (soft loans). These types of investments may exhibit credit risk and are likely to be highly illiquid.	Each third-party loan requires Member approval and each application is supported by the service rational behind the loan and the likelihood of partial or full default.
m. Loans to a local authority company	These are service investments either at market rates of interest or below market rates (soft loans). These types of investments may exhibit credit risk and are likely to be highly illiquid.	Each loan to a local authority company requires Member approval and each application is supported by the service rational behind the loan and the likelihood of partial or full default.
n. Shareholdings in a local authority company	These are service investments which may exhibit market risk and are likely to be highly illiquid.	Each equity investment in a local authority company requires Member approval and each application will be supported by the service rational behind the investment and the likelihood of loss.
o. Non-local authority shareholdings	These are non-service investments which may exhibit market risk, be only considered for longer term investments and will be likely to be liquid.	Any non-service equity investment will require separate Member approval and each application will be supported by the service rational behind the investment and the likelihood of loss.

The Monitoring of Investment Counterparties - The status of counterparties will be monitored regularly. The Council receives credit rating and market information from Link, including when ratings change, and counterparties are checked promptly. On occasion ratings may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria will be removed from the list immediately, and if required new counterparties which meet the criteria will be added to the list.

Use of External Fund Managers – It is the Council's policy to use an external fund manager for the investment portfolio relating to the Common Good Funds and Benevolent Funds. The fund managers are contractually committed to keep to the Council's investment strategy. The terms of the fund managers' investment policies are set out in the Investment Management Agreement. The performance of each manager is reviewed at least quarterly at the Investment Sub Committee by the Executive Chief Officer, Finance and Resources.

Appendix 10

Treasury Management Scheme of Delegation

(i) The Council

- receiving and reviewing reports on treasury management policies, practices and activities
- approval of annual strategy.

(ii) The Council's Corporate Resources Committee

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
- receiving and reviewing regular monitoring reports and acting on recommendations; including scrutiny/review of annual strategy, annual report and mid-year report;

(iii) Executive Chief Officer, Finance and Resources

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.
- approval of the division of responsibilities;
- approving the selection of external service providers and agreeing terms of appointment.

The Treasury Management Role of the Section 95 Officer

The S95 (responsible) Officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit recommending the appointment of external service providers.
- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long-term timeframe (to be determined in accordance with local priorities).
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money
- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority
- ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources

- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long-term liabilities
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- creation of Treasury Management Practices which specifically deal with how non-treasury investments will be carried out and managed.

Appendix 11 Commitment to pay to repay loans fund advances (General Fund)

Financial year	HISTORIC DEBT Opening Balance	Instalment	NEW DEBT Opening Balance	Instalment	Total Instalment	New Borrowing	Total GF LF debt
	£000	£000	£000	£000	£000	£000	£000
2020-21	722,022	30,756	0	0	30,756	15,409	706,675
2021-22	691,266	30,775	15,409	211	30,986	81,027	756,716
2022-23	660,491	30,376	96,225	1,012	31,388	58,523	783,851
2023-24	630,115	29,929	153,736	1,912	31,841	37,595	789,605
2024-25	600,186	29,122	189,419	2,181	31,303	32,384	790,686
2025-26	571,064	28,368	219,622	2,605	30,973	(1,114)	758,599
2026-27	542,696	27,715	215,903	2,799	30,514	(1,120)	726,965
2027-28	514,981	27,199	211,984	2,890	30,089	(1,124)	695,752
2028-29	487,782	26,609	207,970	2,984	29,593		666,159
2029-30	461,173	25,480	204,986	3,094	28,574		637,585
2030-31	435,693	25,055	201,892	3,208	28,263		609,322
2031-32	410,638	24,370	198,684	3,312	27,682		581,640
2032-33	386,268	23,272	195,372	3,433	26,705		554,935
2033-34	362,996	22,592	191,939	3,559	26,151		528,784
2034-35	340,404	21,156	188,380	3,690	24,846		503,938
2035-36	319,248	18,902	184,690	3,825	22,727		481,211
2036-37	300,346	15,947	180,865	3,965	19,912		461,299
2037-38	284,399	14,217	176,900	4,111	18,328		442,971
2038-39	270,182	13,179	172,789	4,262	17,441		425,530
2039-40	257,003	11,487	168,527	4,418	15,905		409,625
2040-41	245,516	10,879	164,109	4,474	15,353		394,272
2041-42	234,637	9,579	159,635	4,385	13,964		380,308
2042-43	225,058	9,419	155,250	4,307	13,726		366,582
2043-44	215,639	9,334	150,943	4,254	13,588		352,994
2044-45	206,305	9,049	146,689	4,330	13,379		339,615
2045-46	197,256	8,726	142,359	4,333	13,059		326,556
2046-47	188,530	8,261	138,026	4,498	12,759		313,797
2047-48	180,269	7,546	133,528	4,669	12,215		301,582
2048-49	172,723	6,859	128,859	4,840	11,699		289,883
2049-50	165,864	6,179	124,019	5,017	11,196		278,687
2050-51	159,685	6,102	119,002	4,775	10,877		267,810
2051-52	153,583	6,161	114,227	3,728	9,889		257,921
2052-53	147,422	6,291	110,499	2,802	9,093		248,828
2053-54	141,131	6,435	107,697	2,806	9,241		239,587
2054-55	134,696	6,158	104,891	2,895	9,053		230,534
2055-56	128,538	6,399	101,996	3,012	9,411		221,123
2056-57	122,139	6,276	98,984	3,133	9,409		211,714
2057-58	115,863	6,217	95,851	3,258	9,475		202,239
2058-59	109,646	6,493	92,593	3,377	9,870		192,369
2059-60	103,153	6,006	89,216	3,500	9,506		182,863
2060-61	97,147	6,031	85,716	3,628	9,659		173,204
2061-62	91,116	6,139	82,088	3,707	9,846		163,358
2062-63	84,977	6,185	78,381	3,780	9,965		153,393
2063-64	78,792	6,243	74,601	3,322	9,565		143,828
2064-65	72,549	6,402	71,279	2,922	9,324		134,504
2065-66	66,147	6,591	68,357	2,763	9,354		125,150
2066-67	59,556	6,533	65,594	2,864	9,397		115,753
2067-68	53,023	5,718	62,730	2,969	8,687		107,066
2068-69	47,305	5,755	59,761	3,077	8,832		98,234
2069-70	41,550	5,697	56,684	3,189	8,886		89,348

Appendix 11 Commitment to pay to repay loans fund advances (General Fund)

Financial year	HISTORIC DEBT Opening Balance	Instalment	NEW DEBT Opening Balance	Instalment	Total Instalment	New Borrowing	Total GF LF debt
	£000	£000	£000	£000	£000	£000	£000
2070-71	35,853	5,383	53,495	3,306	8,689		80,659
2071-72	30,470	4,959	50,189	3,426	8,385		72,274
2072-73	25,511	4,448	46,763	3,551	7,999		64,275
2073-74	21,063	4,190	43,212	3,681	7,871		56,404
2074-75	16,873	3,817	39,531	3,815	7,632		48,772
2075-76	13,056	3,712	35,716	3,954	7,666		41,106
2076-77	9,344	2,906	31,762	4,099	7,005		34,101
2077-78	6,438	2,374	27,663	4,248	6,622		27,479
2078-79	4,064	2,128	23,415	4,403	6,531		20,948
2079-80	1,936	1,115	19,012	4,563	5,678		15,270
2080-81	821	821	14,449	4,631	5,452		9,818
2081-82	0	0	9,818	3,175	3,175		6,643
2082-83	0	0	6,643	2,238	2,238		4,405
2083-84	0	0	4,405	1,834	1,834		2,571
2084-85	0	0	2,571	1,789	1,789		782
2085-86	0	0	782	814	814		(32)
2086-87	0	0	(32)	(32)	(32)		0
2087-88	0	0	0	0	0		0
		722,022		221,580	943,602		

Appendix 12 Commitment to pay to repay loans fund advances (HRA)

Financial year	HISTORIC DEBT Opening Balance	Instalment	NEW DEBT Opening Balance	Instalment	Total Instalment	New Borrowing	Total HRA LF debt
	£000	£000	£000	£000	£000	£000	£000
2020-21	287,808	9,610	0	0	9,610	26,710	278,198
2021-22	278,198	10,705	26,710	210	10,915	29,000*	293,993
2022-23	267,493	10,178	55,500	440	10,618	29,000*	312,375
2023-24	257,315	10,813	84,060	677	11,490	29,000*	329,885
2024-25	246,502	10,132	112,383	923	11,055		347,830
2025-26	236,370	10,402	111,460	955	11,357		336,473
2026-27	225,968	10,454	110,505	988	11,442		325,031
2027-28	215,514	10,573	109,517	1,023	11,596		313,435
2028-29	204,941	10,819	108,494	1,059	11,878		301,557
2029-30	194,122	11,219	107,435	1,096	12,315		289,242
2030-31	182,903	11,230	106,339	1,134	12,364		276,878
2031-32	171,673	11,498	105,205	1,174	12,672		264,206
2032-33	160,175	11,767	104,031	1,215	12,982		251,224
2033-34	148,408	11,563	102,816	1,257	12,820		238,404
2034-35	136,845	10,815	101,559	1,301	12,116		226,288
2035-36	126,030	9,815	100,258	1,347	11,162		215,126
2036-37	116,215	7,269	98,911	1,394	8,663		206,463
2037-38	108,946	6,507	97,517	1,443	7,950		198,513
2038-39	102,439	5,518	96,074	1,493	7,011		191,502
2039-40	96,921	4,567	94,581	1,546	6,113		185,389
2040-41	92,354	3,484	93,035	1,600	5,084		180,305
2041-42	88,870	3,473	91,435	1,656	5,129		175,176
2042-43	85,397	3,429	89,779	1,714	5,143		170,033
2043-44	81,968	3,437	88,065	1,774	5,211		164,822
2044-45	78,531	3,281	86,291	1,836	5,117		159,705
2045-46	75,250	3,243	84,455	1,900	5,143		154,562
2046-47	72,007	3,251	82,555	1,967	5,218		149,344
2047-48	68,756	3,117	80,588	2,035	5,152		144,192
2048-49	65,639	3,017	78,553	2,107	5,124		139,068
2049-50	62,622	2,572	76,446	2,180	4,752		134,316
2050-51	60,050	2,047	74,266	2,257	4,304		130,012
2051-52	58,003	1,907	72,009	2,091	3,998		126,014
2052-53	56,096	1,809	69,918	1,919	3,728		122,286
2053-54	54,287	1,736	67,999	1,742	3,478		118,808
2054-55	52,551	1,556	66,257	1,558	3,114		115,694
2055-56	50,995	1,540	64,699	1,613	3,153		112,541
2056-57	49,455	1,517	63,086	1,669	3,186		109,355
2057-58	47,938	1,467	61,417	1,728	3,195		106,160
2058-59	46,471	1,484	59,689	1,788	3,272		102,888
2059-60	44,987	1,430	57,901	1,851	3,281		99,607
2060-61	43,557	1,438	56,050	1,915	3,353		96,254
2061-62	42,119	1,493	54,135	1,912	3,405		92,849
2062-63	40,626	1,555	52,223	1,909	3,464		89,385
2063-64	39,071	1,619	50,314	1,906	3,525		85,860
2064-65	37,452	2,350	48,408	1,902	4,252		81,608
2065-66	35,102	2,450	46,506	1,969	4,419		77,189
2066-67	32,652	2,554	44,537	2,037	4,591		72,598
2067-68	30,098	3,182	42,500	2,109	5,291		67,307
2068-69	26,916	2,723	40,391	2,182	4,905		62,402
2069-70	24,193	2,837	38,209	2,259	5,096		57,306
2070-71	21,356	2,957	35,950	2,338	5,295		52,011

Financial year	HISTORIC DEBT Opening Balance	 Instalment	NEW DEBT Opening Balance	 Instalment	Total instalment	New Borrowing	Total HRA LF debt
	£000	£000	£000	£000	£000	£000	£000
2071-72	18,399	3,371	33,612	2,420	5,791		46,220
2072-73	15,028	2,930	31,192	2,505	5,435		40,785
2073-74	12,098	2,731	28,687	2,592	5,323		35,462
2074-75	9,367	2,294	26,095	2,683	4,977		30,485
2075-76	7,073	2,007	23,412	2,777	4,784		25,701
2076-77	5,066	1,823	20,635	2,874	4,697		21,004
2077-78	3,243	1,498	17,761	2,974	4,472		16,532
2078-79	1,745	1,122	14,787	3,079	4,201		12,331
2079-80	623	623	11,708	3,186	3,809		8,522
2080-81	0		8,522	3,298	3,298		5,224
2081-82	0		5,224	2,583	2,583		2,641
2082-83	0		2,641	1,751	1,751		890
2083-84	0		890	890	890		
2084-85	0						
2085-86	0						
2086-87	0						
2087-88	0						
		287,808		113,710	401,518	113,710	

*Assumed borrowing requirement pending development of new HRA capital investment plan