Public Document Pack

aditional papers 1

Audit, Governance & Standards
Committee

Thu 30 Jan
2020
7.00 pm

Committee Room Two
Town Hall
Redditch

REDDITCH BOROUGH COUNCIL

making a difference

www.redditchbc.gov.uk

If you have any queries on this Agenda please contact
Jess Bayley or Jo Gresham

Town Hall, Walter Stranz Square, Redditch, B98 8AH
Tel: 01527 (01527) 64252 Ext: 3268 / 3031
e.mail: jess.bayley@bromsgroveandredditch.gov.uk /
jo.gresham@bromsgroveandredditch.gov.uk

REDDITCH BOROUGH COUNCIL

making a difference

www.redditchbc.gov.uk

Audit, Governance & Standards

Committee

Thursday, 30th January, 2020

7.00 pm

Committee Room 2 - Town Hall Redditch

Agenda

Membership:

Cllrs:

John Fisher (Chair)
Mark Shurmer (Vice-Chair)
Salman Akbar
Tom Baker-Price
Michael Chalk
Ann Isherwood
Julian Grubb
Nyear Nazir
Yvonne Smith
David Thain

3. Minutes (Pages 1 - 14)

9. Treasury Management Strategy, Prudential Indicators and Minimum Revenue Policy Provision 2020/21 (Pages 15 - 48)

This page is intentionally left blank

REDDITCH BOROUGH COUNCIL

making a difference

www.redditchbc.gov.uk

Audit, Governance & Standards Committee

Thursday, 31 October 2019

MINUTES

Present:

Councillor John Fisher (Chair), Councillor Mark Shurmer (Vice-Chair) and Councillors Salman Akbar, Peter Fleming, Nyear Nazir, Yvonne Smith and David Thain

Also Present:

Mr R Percival (Grant Thornton)

Officers:

Andy Bromage, Jayne Pickering and David Riley

Senior Democratic Services Officer:

Jess Bayley

23. APOLOGIES AND NAMED SUBSTITUTES

Apologies for absence were received on behalf of Councillors Michael Chalk and Ann Isherwood and it was confirmed that Councillor Peter Fleming was attending as Councillor Chalk's substitute.

24. DECLARATIONS OF INTEREST

There were no declarations of interest.

25. MINUTES

RESOLVED that

the minutes of the meeting of the Audit, Governance and Standards Committee held on Thursday 26th September 2019 be approved as a true and correct record and signed by the Chair.

Audit, Governance & Standards Committee

Thursday, 31 October 2019

26. PUBLIC SPEAKING

The Chair confirmed that there were no registered public speakers on this occasion.

27. MONITORING OFFICER'S REPORT - STANDARDS REGIME

The Principle Solicitor presented the Monitoring Officer's report and in so doing highlighted that the investigation in respect of the complaint which had been reported at the previous meeting of the Committee had been resolved and no breaches had been identified.

The Member Support Steering Group had held a meeting since the previous meeting of the Committee. At this meeting Members had discussed and agreed a draft induction programme for Councillors due to be elected in May 2020. Members' ICT support had also been discussed and progress continued to be made in terms of enabling Councillors to access Committee papers electronically.

RESOLVED that

the report be noted.

28. LOCAL GOVERNMENT ETHICAL STANDARDS

The Principle Solicitor presented a report which outlined proposed changes to the Members' Code of Conduct. These changes had been proposed in response to findings in a review of standards in public life that had been conducted by a House of Commons Select Committee. As in previous years the Monitoring Officers for all of the Councils in Worcestershire had collectively reviewed the joint Code of Conduct for the county and the changes presented for Members' consideration had already been agreed by a number of other local authorities. Two changes had been proposed by other Councils to the draft joint code; the inclusion of trolling behaviour as an example of bullying and harassment and agreement that gifts and hospitality should be declared when valued at £15 or over.

Following the presentation of the report Members noted that reference had been made to Bromsgrove District Council in the document rather than to Redditch Borough Council. Officers explained that this was a typographical error and the code remained applicable in Redditch as it was a joint code for the whole of Worcestershire.

Audit, Governance & Standards Committee

Thursday, 31 October 2019

Members questioned the reasons for inclusion of a reference to trolling behaviour within the code of conduct and concerns were raised that the subject was subjective and open to interpretation. Officers explained however, that trolling behaviour was considered to be critical and personal comments about somebody else on social media. This type of behaviour had already been reported to the Monitoring Officer, particularly in relation to comments that had been posted on Facebook. In cases where the Monitoring Officer received reports of trolling behaviour this would be investigated like all other complaints and the context would be taken into account as part of this process.

The Committee also discussed arrangements for Members declaring gifts and hospitality. The £15 threshold for declaring gifts and hospitality had been requested by other local authorities in the county. All gifts and hospitality of this value or above would need to be declared and registered with the Monitoring Officer.

Members noted that the report made reference to the role of the Independent Person. This role had been introduced in the Localism Act 2011. The Independent Person was consulted in relation complaints and had a key investigative role in cases where a breach of the Council's Code of Conduct was found to have taken place.

RECOMMENDED that

the changes to the Code of conduct to reflect the CSPL Best Practice Recommendations be approved and that authority be delegated to the Head of Legal, Equalities and Democratic Services to update the constitution accordingly.

29. GRANT THORNTON SECTOR UPDATE

The Engagement Lead from Grant Thornton presented the external auditor's sector update. The update focused on the financial statement audit and the value for money audit. Members were asked to note that the external auditors were at an early planning stage for these processes, having produced the audit plan, and more detail would be available on the audit findings early in the New Year.

The value for money audit involved a risk based approach to auditing the Council. Following the issuing of the Section 24 Notice

Audit, Governance & Standards Committee

Thursday, 31 October 2019

earlier in the year a key focus of this audit would be on the Council's progress with the Medium Term Financial Plan (MTFP), in respect of achieving a balanced budget.

The external auditors were in the process of reviewing the Council's Housing Benefit subsidy claim for 2018/19. The deadline to complete this work was the end of November 2019 and Members were assured that Grant Thornton was on track to complete this work by the deadline.

Members were advised that an independent review was in the process of being undertaken in respect of the Local Government external audit function. This review had been launched in recognition that the scope of the Local Government external audit process had shrunk since the Audit Commission was disbanded. The Audit Commission had had a number of duties that had not been passed on to the external auditors, including best value audits and service inspections. There appeared to now be a gap between what auditors actually did and what people expected external auditors to do.

The House of Commons Public Accounts Committee had reviewed local government and how the governance role was discharged at local Councils. The Committee had made five recommendations on this subject which highlighted areas of concern. The external auditors were anticipating that as a result of this finding more local oversight would be expected than was currently happening moving forward.

RESOLVED that

the Grant Thornton progress report and updates be noted.

30. GRANT THORNTON AUDIT LETTER

The Engagement Lead for Grant Thornton presented a report in respect of the Grant Thornton Audit Letter and in so doing highlighted key issues identified in the 2018/19 audit. The external auditors had issued the Council with an unqualified audit opinion on the financial statements. However, the Council had been issued with an adverse value for money statement and subsequently the external auditors had published the Section 24 Notice for the Council.

Grant Thornton had had concerns about the Council's pension liabilities and the valuation of properties and buildings. The external audit work in 2018/19 had been particularly challenging and more input had been required than had been anticipated. The Value for Money audit had focused on the Council's financial sustainability and the external auditors had concluded that there was a need for action which was why the Section 24 Notice had been issued. Progress had been made by the Council in respect of Housing procurement and contract management. However, there was poor financial resilience in the Council's Housing Revenue Account (HRA) due to there being low levels of reserves.

The audit fee had been £13,000 higher than anticipated largely due to all of the additional work that had been required from the external auditors during the year. In particular, extra work had been required on the Council's property audit and in respect of the 2018/19 accounts.

During consideration of this matter Members noted that the value for money conclusion had highlighted concerns about short-term decision making at the Council and questions were raised about when this process was viewed to have started. The external auditors reported that they had anticipated that Members would make some challenging decisions in 2017/18 which had not materialised. This meant that in 2018/19 the Council's ability to balance the budget using balances became more difficult and some decisions had then been taken which had an impact on the Council's financial sustainability. In addition, at a national level there had been a judgement in respect of pension liabilities which had had significant financial implications for the Council.

RESOLVED that

the Audit Letter be noted.

31. COMPLIANCE TEAM UPDATE

The Financial Support Manager presented an update in respect of the work of the Council's Compliance Team. The role of the team was to monitor fraud and errors in the Council Tax base. The work of the team had helped to generate income for the Council which was reinvested in services.

Following the presentation of the report Members enquired about the impact that the introduction of Universal Credit had had on the work of the Compliance Team. Members were advised that the Council had not analysed the impact of Universal Credit so it was not possible to answer this question. The team was not just required to focus on Council Tax, but also considered areas such as undervalued rates and exemptions from Council Tax so the impact of Universal Credit would need to be assessed across a range of areas.

When the Compliance Team had initially launched there had been a number of examples of fraud and error which had been identified relatively quickly. By October 2019 the majority of mistakes had been identified. There was therefore the possibility that over time the role of the Compliance Team would change to focus on other areas, such as housing benefit fraud.

Members were asked to note that as with Council Tax the Council only retained a proportion of the funding recovered by the team in cases of fraud or where errors were identified. There was also approximately a 50:50 split between local government, including both the Borough and the County Council, and central Government in cases where income was returned where there had been fraud or errors in relation to non-domestic rates.

During consideration of this item Members briefly discussed the extent to which Worcestershire County Council, as the major beneficiary of Council Tax, could provide financial support to Redditch Borough Council in respect of collecting contributions from residents. Members were advised that Officers discussed this on a frequent basis with the County Council and some funding had been provided in previous years for this purpose.

The Committee also debated the reasons why non-banded properties might exist resulting in a failure to charge Council Tax or businesses might not pay non-domestic rates. Officers explained that there could be a variety of causal factors. For example there were building features that could increase the rental value of a retail unit, such as air conditioning, that the local authority might not be aware of and therefore the level of non-domestic rates might be lower than the Council was entitled to charge. Sometimes there were cases of misinformation or human error, such as Officers not identifying new developments that had received planning permission in a timely manner, which could lead to delays in obtaining Council Tax for a property.

RESOLVED that

the report be noted.

32. CORPORATE GOVERNANCE AND RISK UPDATE

The Executive Director of Finance and Corporate Resources presented an update in respect of the Council's approach to risk management. The Council had received a limited assurance assessment from Internal Audit about risk management arrangements. Whilst there were some strengths, such as health and safety arrangements for Rubicon Leisure and Environmental services respectively, there were also weak elements, particularly the authority's approach to managing corporate risks.

The Council had been working with Zurich Insurance to identify risks and to ensure that they were monitored effectively. Zurich Insurance had undertaken a review of the Council's risk management arrangements in June and July 2019 and this investigation had found that there were actions that could be taken to strengthen the Council's arrangements. This included the need for training to be provided to staff and Members in respect of managing risks. The Council had also been found not to have a consistent approach to managing risks.

The Audit, Governance and Standards Committee had an important role to play in managing the Council's risks. Zurich Insurance was aiming to attend a future development session with Members of the Committee to provide further information on risk management.

Departmental risk champions were in place and a corporate register was developed on an annual basis. However, there hadn't been a fundamental review of risks in recent years and there was a need for risk management to be considered more seriously as a corporate priority in future.

Members noted that the Audit, Governance and Standards Committee had received a number of reports over the preceding five to ten years in respect of the action that was being taken to improve risk management arrangements at the Council. Since then serious issues had been identified with the Council's approach first to gas maintenance and later in respect of the Housing Capital Service. Members raised concerns that in this context weaknesses had been found in the local authority's approach to risk management. Officers acknowledged that four years previously the

Audit, Governance & Standards Committee

Council had introduced a new Risk Management Strategy and there had been a clear focus on compliance in areas such as health and safety and Housing Services. However, there had been less focus on management of corporate risks. Progress was being made and Officers were aiming to provide an update in respect of the corporate risk register to Members together with training at the following meeting of the Committee.

RESOLVED that

the report be noted.

33. SECTION 24 ACTION PLAN UPDATE

The Executive Director of Finance and Corporate Resources explained that following the Audit, Governance and Standards Committee's agreement of the Section 24 Action Plan the external auditors had been notified of the Council's plans. Grant Thornton had included three recommendations in the Section 24 Notice and an update was provided in the report in respect of progress in relation to each of these recommendations.

The first recommendation focused on the need for the Council to achieve a balanced budget in 2019/20. Specifically the Council needed to be sure about the deliverability of savings proposed for the financial year. Officers were in the process of preparing the financial monitoring reports for the second quarter of the financial year, however, information gathered to date appeared to indicate that the Council was on track to deliver the forecast savings of £1.1 million in the MTFP for the year. In addition, it was anticipated that further savings would be made on top of this figure; any such savings would be returned to balances.

The second recommendation focused on the further savings that needed to be made to address the £1.4 million gap in the budget the following year as well as to balance the HRA. The Executive Committee had recently received an update on the Council's financial position as of October 2019. To date £1 million of savings had been secured for 2020/21. The Council had also secured £450,000 in New Homes Bonus (NHB) funding that year together with £400,000 in savings identified through a review of the Council's capital programme. Unfortunately, the Government had announced that the Council could only increase Council Tax by a maximum of 2 per cent before triggering a referendum, rather than the 2.99 per cent that Officers had budgeted for and this would have a negative impact on the Council's finances moving forward.

The Committee discussed the savings that had been secured to date by the Council and the review of the capital programme. Officers explained that the £400,000 savings in the capital programme related to borrowing costs. The Council had also reviewed the £20 million borrowing costs that had been incorporated into the Council's plans in relation to the Investment and Acquisition Strategy. As the Council had not agreed the number of investments that had originally been anticipated the borrowing costs for investments had been re-profiled to a more sensible level.

Members noted that there would be a need in seeking to balance the budget to take decisions that would ensure the Council's financial sustainability. The Section 151 Officer would be looking for a clear steer from Members in respect of balancing the Council's budget and approvals, at least in principle, on spending plans by December 2019.

Concerns were raised that some of the language included in the report was quite vague, such as the suggestion that the Council was anticipating that the unidentified savings included in the budget for 2019/20 would be met. Officers explained that certainty could not yet be provided as the figures from the monitoring report for the second quarter of the financial year had not yet been finalised. However, from the information that had been gathered to date Officers were anticipating that the Council was on track to achieve the savings required.

During consideration of this item Members asked about the inclusion of unidentified savings in the MTFP for 2019/20 and the value of including unidentified savings in a Council budget as these had tended to be delivered by Officers over a number of years. Officers acknowledged that unidentified savings had been delivered in the past. However, the amount of unidentified savings included in the budget in 2018/19, at £770,000 had been relatively high and Officers had not been able to deliver unidentified savings at this level. The Engagement Lead for Grant Thornton explained that whilst external auditors were sceptical about the inclusion of unidentified savings in a budget it was recognised that it was a judgement call and Councils could not always clarify every aspect of the budget in advance.

Audit, Governance & Standards Committee

Thursday, 31 October 2019

RESOLVED that

the report be noted.

34. FINANCIAL SAVINGS MONITORING REPORT

The Executive Director of Finance and Corporate Resources presented the Financial Savings Monitoring Report for Members' consideration. The report had been requested by Members and the content focused on progress with the delivery of savings in 2019/20. A number of savings were anticipated, including from Print Services, which were likely to be £14,000 higher than had been originally anticipated. Savings of £206,000 had also been achieved on vacancy management and it was likely that further savings would accrue from posts that were kept vacant. The Council was on track to deliver £1.1 million in savings as budgeted for 2019/20 together with a further £42,000 in savings that had not been anticipated, though Members were advised that this figure might change by the end of the financial year.

The Council's budgeted savings included plans for a decrease in the amount of fee that would need to be paid to the external auditors, despite the fact that an additional fee had been levied on the Council by the external auditors. This was due to the requirement nationally for external audit fees to be reduced for local government.

During consideration of this item concerns were raised that unexpected pressures or delays to progress might occur later in the financial year which would have a negative impact on the savings that the Council achieved. Officers explained that Heads of Service were consistently challenged to deliver savings and any issues would be identified at an early stage.

The reasons for the delay in reporting the figures for the second quarter of the financial year, from July to September, were briefly debated. Members were advised that whilst Heads of Service and managers had access to budget information on a monthly basis it would not be feasible to report to Members on the budget position every month. In the meantime, until the figures were reported to Members in December, any exceptions or areas of concern would be raised with the Section 151 Officer for consideration.

RESOLVED that

the report be noted.

35. INTERNAL AUDIT PROGRESS REPORT

The Head of Worcestershire Internal Audit Shared Service presented the Internal Audit Progress Report for Members' consideration. Several internal audits had identified limited assurance, which was quite unusual, and one for St David's House had found there to be no assurance. Due to the number of audits that had found low or no assurance, greater detail had been included in the report in respect of these audits for Members' consideration.

Action had already been taken to address many of the problems identified in internal audits where there had been limited or no assurance. The audit in respect of the Benefits Service had identified concerns which had resulted in direct intervention from the Department of Work and Pensions (DWP) but subsequently the service had improved. Risk management had been another area where limited assurance had been identified and the Council had since invited Zurich Insurance to undertake investigative work. The issues identified in the internal audit of health and safety had occurred during a transition period prior to the Council's Health and Safety Officer commencing employment with the authority and a lot of progress had been made since then to address those problems. At St David's House a substantial Action Plan had been developed and progress had been made.

In all cases where limited or no assurance had been identified the Internal Audit team would continue to monitor progress until all issues had been resolved. The Audit, Governance and Standards Committee would receive updates on any areas of concern. The Head of the Worcestershire Internal Audit Shared Service had also worked with the Executive Director of Finance and Corporate Resources to ensure that there was better escalation in terms of addressing issues that were not believed to be progressing as well as necessary. Members were also asked to note that all Internal Audit reviews that identified limited or no assurance were being reported to both the Corporate Management Team (CMT) and the Senior Management Team (SMT).

Members discussed the content of the report and concerns were raised that a number of Internal Audit reports had identified limited

Audit, Governance & Standards Committee

or no assurance. To assess the progress in respect of these areas Members agreed to invite representatives of St David's House, the Health and Safety Officer and representatives of the Benefits Service to attend future meetings of the Committee to provide an update on the action that had been taken to address the problems that had been identified by Internal Audit.

The Committee also discussed the intervention of the DWP in the Benefits Service and the reasons why this intervention had been required. Officers explained that the Benefits team had been restructured resulting in a number of experienced staff securing positions in the Financial Inclusion Team (FIT). The remaining staff in the Benefits team had not had the same level of experience but were still expected to handle complex cases. At this time there had been a number of officers on long term sick and resources in the team were stretched. In this context delays had occurred in the processing times. Since that time a number of changes had been made and the processing times had fallen to a comparable level to the national average. A further review of the service structure would be taking place towards the end of the year.

RESOLVED that

1) **Officers be invited to attend future meetings of the Committee to provide updates on the action being taken to address the problems identified in the Internal Audits of St David's House, the Benefits Service and Health and Safety; and**

2) **the report be noted.**

36. COMMITTEE WORK PROGRAMME

The Senior Democratic Services Officer (Redditch) advised that the items that had been requested for consideration at future meetings of the Committee earlier in the meeting would be added to the work programme.

RESOLVED that

the content of the Audit, Governance and Standards Committee's work programme be noted.

Audit, Governance & Standards
Committee

Thursday, 31 October 2019

The Meeting commenced at 7.00 pm
and closed at 8.40 pm

This page is intentionally left blank

REDDITCH BOROUGH COUNCIL

AUDIT, GOVERNANCE AND STANDARDS COMMITTEE 30th January 2020

Capital Strategy 2020/21 incorporating the Treasury Management Strategy

Relevant Portfolio Holder	Councillor David Thain, Portfolio Holder for Corporate Management
Portfolio Holder Consulted	No
Relevant Head of Service	Jayne Pickering – Exec Director Finance and Resources
Wards Affected	All Wards
Non-Key Decision	

1. **SUMMARY**

This report for 2020/21 presents the Capital strategy, Treasury Management Strategy, Minimum Revenue Provision Statement, a policy for use of flexible Capital receipts and the Investment Strategy for 2020/21 to be considered for recommendation to Council.

2. **RECOMMENDATIONS**

Audit, Governance and Standards Committee are asked to RECOMMEND TO COUNCIL that

i) the Capital Strategy (Appendix A) as an appropriate overarching strategy for the Council be approved

ii) the Treasury Management Strategy for 2020/21 (Appendix B) and the associated MRP policy (Appendix C) be approved

iii) the policy for Flexible use of Capital Receipts as per appendix D be approved

iv) the Investment Strategy (Appendix E) be approved

3. **KEY ISSUES**

Financial Implications

3.1 The report for 2020/21 is required following changes in the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Ministry of Housing, Communities and Local Government (MHCLG) guidance. It combines an overview of how capital expenditure, capital financing, treasury and other investment activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability. The strategies set limits and indicators that embody the risk management approach that the Council believes to be prudent. The strategies are set against the mid-term financial strategy, the context of the UK economy and projected interest rates.

The Council are required to set a balanced operating budget. The role of the treasury function is to manage cash flow within the authority so that the demands of expenditure can be met. The policies included in this report set out the criteria in which the Council can manage its Treasury management function.

The CIPFA Code of Practice for Treasury Management in Public services (the CIPFA TM Code) and the Prudential Code require local authorities to set the Treasury Management Strategy Statement (TMSS) and Prudential Indicators each financial year. The TMSS also incorporates the Investment Strategy as required under the CLG's Investment Guidance. In addition the Council has to receive a report on treasury management and this is reported on a quarterly basis which is included within the Quarterly Monitoring Report.

3.2 CIPFA has defined Treasury Management as:

"the management of the organisation's investments, 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."

3.3 The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Treasury management risks are identified in the Council's approved Treasury Management Practices and include:

- Liquidity Risk (Adequate cash resources)
- Market or Interest Rate Risk (Fluctuations in the value of investments)
- Inflation Risks (Exposure to inflation)
- Credit and Counterparty Risk (Security of Investments)
- Refinancing Risks (Impact of debt maturing in future years)
- Legal & Regulatory Risk (Compliance with statutory and regulatory requirements)

3.4 The guidance requires investment strategies to comment on the use of treasury management consultants and on the investment of money borrowed in advance of spending needs.

3.5 In formulating the Treasury Management Strategy and the setting of the Prudential Indicators, the Council adopts the Treasury Management Framework and Policy recommended by CIPFA.

Legal Implications

3.6 This is a statutory report under the Local Government Act 2003.

Service/Operational Implications

3.7 None as a direct result of this report.

Customer / Equalities and Diversity Implications

3.8 None as a direct result of this report.

4. RISK MANAGEMENT

Failure to manage the Treasury Management function effectively to ensure the delivery of maximum return within a secure environment.

Controls in place to mitigate these risks are as follows:

- Regular monitoring of the status of the organisations we invest with
- Daily monitoring by internal officers of banking arrangements and cash flow implications.

5. APPENDENCES

Appendix A – Capital Strategy 2020/21
Appendix B – Treasury Management Strategy 2020/21
Appendix C – Minimum Revenue Provision Statement 2020/21
Appendix D – Policy for the Flexible Use of Capital receipts
Appendix E – Investment Strategy 2020/21

AUTHOR OF REPORT

Name: Christopher Forrester – Financial Services Manager (Deputy S151)
E Mail: chris.forrester@bromsgroveandredditchbc.gov.uk
Tel: 01527 881673

Redditch Capital Strategy Report 2020/21

Introduction

This capital strategy report gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability. It has been written in an accessible style to enhance members' understanding of these sometimes technical areas.

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

Capital Expenditure and Financing

Capital expenditure is where the Authority spends money on assets, such as property or vehicles, that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. The Authority has some limited discretion on what counts as capital expenditure.

In 2020/21, the Authority is planning capital expenditure of £17.8m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
General Fund services	2.5	5.6	1.8	1.2	3.1
Council housing (HRA)	4.8	9.1	10.8	12.6	11.9
Capital investments	0	0.9	5.2	2	2
TOTAL	7.3	15.6	17.8	15.8	17

The main General Fund capital projects include the fleet replacement programme which totals £3.5m across the budget period, Locality improvements of £1.2m across the budget period and public building improvements/repairs of £874k. The Authority also plans to incur £10.1m of capital expenditure on investments, which are detailed later in this report.

The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately.

Governance: Service managers bid annually in November to include projects in the Authority's capital programme. Bids are collated by finance who calculate the financing cost (which can be nil if the project is fully externally financed). The final capital programme is then presented to Executive and Council in February each year.

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

Table 2: Capital financing in £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
External sources	0.6	3.3	0	0	0
Own resources	4.8	9.1	10.8	12.6	11.9
Debt	1.9	3.2	7	3.2	5.1
TOTAL	**7.3**	**15.6**	**17.8**	**15.8**	**17**

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

Table 3: Replacement of debt finance in £ millions

	2018/19 actual	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget
Own resources	0.8	0.9	0.9	1.0	1.0

The Authority's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase by £6m during 2020/21. Based on the above figures for expenditure and financing, the Authority's estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions

	31.3.2019 actual	31.3.2020 forecast	31.3.2021 budget	31.3.2022 budget	31.3.2023 budget
General Fund services/HRA	139.6	141.1	141.9	142.1	144.2
Capital investments	0	0.9	6.1	8.1	10.1
TOTAL CFR	**139.6**	**142**	**148**	**150.2**	**154.3**

Asset disposals: When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Authority is currently also permitted to spend capital receipts on service transformation projects until 2022/23. Repayments of capital grants, loans and investments also generate capital receipts.

Treasury Management

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

Due to decisions taken in the past, the Authority currently has £103.9m of long term external borrowing.

Borrowing strategy: The Authority's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Authority therefore seeks to strike a balance between cheap short-term loans (currently available at around 0.75%) and long-term fixed rate loans where the future cost is known but higher (currently 2.0 to 3.0%).

Liability benchmark: To compare the Authority's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes that cash and investment balances are kept to a minimum level of £0.2m at each year-end. This benchmark is currently £94.6m and is forecast to rise to £121.7m over the next three years.

Table 7: Borrowing and the Liability Benchmark in £ millions

	31.3.2019 actual	31.3.2020 forecast	31.3.2021 forecast	31.3.2022 forecast	31.3.2023 forecast
Outstanding borrowing	110	106.1	110.4	120.4	138
Liability benchmark	**94.6**	**100.2**	**108.4**	**114.1**	**121.7**

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

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

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

	2019/20 limit	2020/21 limit	2021/22 limit	2022/23 limit
Authorised limit – borrowing	147.3	160.0	170.0	180.0
Authorised limit – PFI and leases	0.5	1.5	1.5	1.5
Authorised limit – total external debt	147.8	161.5	171.5	181.5
Operational boundary – borrowing	135.0	155.0	165.0	175.0
Operational boundary – PFI and leases	0.5	1.5	1.5	1.5
Operational boundary – total external debt	135.5	156.5	166.5	176.5

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

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

Risk management: The effective management and control of risk are prime objectives of the Authority's treasury management activities. The treasury management strategy therefore sets out various indicators and limits to constrain the risk of unexpected losses and details the extent to which financial derivatives may be used to manage treasury risks.

Governance: Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Executive Director of Finance and staff, who must act in line with the treasury management strategy approved by council. Quarterly reports on treasury management activity are presented to council. The Audit Committee is responsible for scrutinising treasury management decisions.

Investments for Service Purposes

The Authority may make investments to assist local public services, including potentially making loans to the Authority's subsidiaries that provide services. In light of the public service objective, the Authority is willing to take more risk than with treasury investments, however it still plans for such investments to at least break even after all costs.

Governance: Decisions on service investments are made by the relevant service manager in consultation with the Executive Director of Finance and must meet the criteria and limits laid down in the investment strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme.

Commercial Activities

With central government financial support for local public services declining, the Authority is planning to invest in commercial property to encourage economic growth as well as to make a financial return and may lend to a future subsidiary should one be set up for the same reasons. Total commercial investments are currently valued at £0.9m.

With financial return being a primary objective, the Authority accepts higher risk on commercial investment than with treasury investments. The principal risk exposures are potential falls in property values, vacancies reducing rental income etc. These risks are managed by having a risk register in place, regularly reviewing purchased assets and the market place and talking to tenants. In order that commercial investments remain proportionate to the size of the authority, these are subject to an overall maximum investment limit of £20m.

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

Liabilities

In addition to the debt detailed above, the Authority is committed to making future payments to cover its pension fund deficit. It has also set aside £3.3m to cover risks of insurance £528k, NNDR appeals £2,630k and employee benefits £128k.

Governance: Decisions on incurring new discretional liabilities are taken by service managers in consultation with the Executive Director of Finance. The risk of liabilities crystallising and requiring payment is monitored by finance and reported as required.

Revenue Budget Implications

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

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

	2019/20 forecast	**2020/21 budget**	**2021/22 budget**	**2022/23 budget**
Financing costs (£m)	5.4	5.5	5.5	5.7
Proportion of net revenue stream	15.9%	16.2%	15.8%	16.4%

Sustainability: Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The Executive Director of Finance is satisfied that the proposed capital programme is prudent, affordable and sustainable because of the current MTFP forecasts which show that the council is financially sustainable and taking it into account.

Knowledge and Skills

The Authority employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Executive Director of Finance is a qualified accountant with more than 30 years' experience. The Authority pays for junior staff to study towards relevant professional qualifications including CIPFA and AAT.

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

This page is intentionally left blank

Redditch Treasury Management Strategy Statement 2020/21

Introduction

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

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

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

External Context

Economic background: The UK's progress negotiating its exit from the European Union, together with its future trading arrangements, will continue to be a major influence on the Authority's treasury management strategy for 2020/21.

UK Consumer Price Inflation (CPI) for September registered 1.7% year on year, unchanged from the previous month. Core inflation, which excludes the more volatile components, rose to 1.7% from 1.5% in August. The most recent labour market data for the three months to August 2019 showed the unemployment rate ticked back up to 3.9% while the employment rate was 75.9%, just below recent record-breaking highs. The headline 3-month average annual growth rate for pay was 3.8% in August as wages continue to rise steadily. In real terms, after adjusting for inflation, pay growth increased 1.9%.

GDP growth rose by 0.3% in the third quarter of 2019 from -0.2% in the previous three months with the annual rate falling further below its trend rate to 1.0% from 1.2%. Services and construction added positively to growth, by 0.6% and 0.4% respectively, while production was flat and agriculture recorded a fall of 0.2%. Looking ahead, the Bank of England's Monetary Policy Report (formerly the Quarterly Inflation Report) forecasts economic growth to pick up during 2020 as Brexit-related uncertainties dissipate and provide a boost to business investment helping GDP reach 1.6% in Q4 2020, 1.8% in Q4 2021 and 2.1% in Q4 2022.

The Bank of England maintained Bank Rate to 0.75% in November following a 7-2 vote by the Monetary Policy Committee. Despite keeping rates on hold, MPC members did confirm that if Brexit uncertainty drags on or global growth fails to recover, they are prepared to cut interest rates as required. Moreover, the downward revisions to some of the growth projections in the Monetary Policy Report suggest the Committee may now be less convinced of the need to increase rates even if there is a Brexit deal.

Growth in Europe remains soft, driven by a weakening German economy which saw GDP fall -0.1% in Q2 and is expected to slip into a technical recession in Q3. Euro zone inflation was 0.8% year on year in September, well below the European Central Bank's target of 'below, but close to 2%' and leading to the central bank holding its main interest rate at 0% while cutting the deposit facility rate to -0.5%. In addition to maintaining interest rates at ultra-low levels, the ECB announced it would recommence its quantitative easing programme from November.

In the US, the Federal Reserve began easing monetary policy again in 2019 as a pre-emptive strike against slowing global and US economic growth on the back on of the ongoing trade war with China. At its last meeting the Fed cut rates to the range of 1.50-1.75% and financial markets expect further loosening of monetary policy in 2020. US GDP growth slowed to 1.9% annualised in Q3 from 2.0% in Q2.

Credit outlook: Credit conditions for larger UK banks have remained relatively benign over the past year. The UK's departure from the European Union was delayed three times in 2019 and while there remains some concern over a global economic slowdown, this has yet to manifest in any credit issues for banks. Meanwhile, the post financial crisis banking reform is now largely complete, with the new ringfenced banks embedded in the market.

Challenger banks hit the news headlines in 2019 with Metro Bank and TSB Bank both suffering adverse publicity and falling customer numbers.

Looking forward, the potential for a "no-deal" Brexit and/or a global recession remain the major risks facing banks and building societies in 2020/21 and a cautious approach to bank deposits remains advisable.

Interest rate forecast: The Authority's treasury management adviser Arlingclose is forecasting that Bank Rate will remain at 0.75% until the end of 2022. The risks to this forecast are deemed to be significantly weighted to the downside, particularly given the upcoming general election, the need for greater clarity on Brexit and the continuing global economic slowdown. The Bank of England, having previously indicated interest rates may need to rise if a Brexit agreement was reached, stated in its November Monetary Policy Report and its Bank Rate decision (7-2 vote to hold rates) that the MPC now believe this is less likely even in the event of a deal.

Gilt yields have risen but remain at low levels and only some very modest upward movement from current levels are expected based on Arlingclose's interest rate projections. The central case is for 10-year and 20-year gilt yields to rise to around 1.00% and 1.40% respectively over the time horizon, with broadly balanced risks to both the upside and downside. However, short-term volatility arising from both economic and political events over the period is a near certainty.

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

For the purpose of setting the budget, it has been assumed that new treasury management investments will be made at an average rate of 0.5%, and that new long-term loans will be borrowed at an average rate of 1.5%.

Local Context

On 23 January 2020, the Authority held £103.9m of borrowing and £6m of treasury investments. This is set out in further detail at ***Appendix B***. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

Table 1: Balance sheet summary and forecast

	31.3.19 Actual £m	31.3.20 Estimate £m	31.3.21 Forecast £m	31.3.22 Forecast £m	31.3.23 Forecast £m
Total CFR	139.6	142.0	148.0	150.2	154.3
Less: External borrowing **	(111.1)	(103.9)	(103.9)	(103.9)	(103.9)
Internal (over) borrowing	**28.5**	**38.1**	**44.1**	**46.3**	**50.4**
Less: Usable reserves	(40.3)	**(37.1)**	**(34.9)**	**(31.4)**	**(27.9)**
Less: Working capital	**(4.9)**	**(4.9)**	**(4.9)**	**(4.9)**	**(4.9)**
Treasury investments (or New borrowing)	**16.7**	**3.9**	**(4.3)**	**(10)**	**(17.6)**

** shows only loans to which the Authority is committed and excludes optional refinancing

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Authority's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing. The underlying availability of internal borrowing will reduced over the period reflecting the use of the HRA capital reserve and capital receipts held on account and a reduction in HRA working balances to a minimum level of £0.6m in the medium term.

The Authority has an increasing CFR due to the capital programme, but minimal investments and will therefore be required to borrow up to £17.6m over the forecast period.

CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Authority expects to comply with this recommendation during 2019/20.

Liability benchmark: To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table 1 above, but that cash and investment balances are kept to a minimum level of £0.2m at each year-end to maintain sufficient liquidity but minimise credit risk.

Table 2: Liability benchmark

	31.3.19 Actual £m	31.3.20 Estimate £m	31.3.21 Forecast £m	31.3.22 Forecast £m	31.3.23 Forecast £m
CFR	139.6	142.0	148.0	150.2	154.3
Less: Usable reserves	(40.3)	(37.1)	(34.9)	(31.4)	(27.9)
Less: Working capital	(4.9)	(4.9)	(4.9)	(4.9)	(4.9)
Plus: Minimum investments	0.2	0.2	0.2	0.2	0.2
Liability Benchmark	**94.6**	**100.2**	**108.4**	**114.1**	**121.7**

Following on from the medium-term forecasts in table 2 above, the long-term liability benchmark assumes capital expenditure funded by borrowing each year, minimum revenue provision on new capital expenditure based on a 50 year asset life and income, expenditure and reserves all increasing/decreasing in line with the MTFP.

Borrowing Strategy

The Authority currently holds £103.9 million of loans, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that the Authority expects to borrow up to £4.3m in 2020/21. The Authority may however borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing.

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

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

By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal / short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2020/21 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

The Authority has previously raised the majority of its long-term borrowing from the PWLB but the government increased PWLB rates by 1% in October 2019 making it now a relatively expensive options. The Authority will now look to borrow any long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code.

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

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

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

- Public Works Loan Board (PWLB) and any successor body
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds (except Worcestershire Pension Fund)
- capital market bond investors

- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

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

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

Municipal Bonds Agency: UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to full Council.

Short-term and variable rate loans: These loans leave the Authority exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below.

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

Investment Strategy

The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held.

Objectives: The CIPFA Code requires the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Authority will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

Negative interest rates: If the UK enters into a recession in 2020/21, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

Strategy: Given the increasing risk and very low returns from short-term unsecured bank investments, the Authority aims to diversify into more secure and/or higher yielding asset classes during 2020/21. The majority of the Authority's surplus cash is currently invested in short-term unsecured bank deposits. This diversification will represent a continuation of the approved strategy.

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

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

Table 3: Approved investment counterparties and limits

Credit rating	Banks unsecured	Banks secured	Government	Corporates	Registered Providers
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£3 m 5 years	£3m 20 years	£3m 50 years	£3m 20 years	£1m 20 years
AA+	£3m 5 years	£3m 10 years	£3m 25 years	£3m 10 years	£1m 10 years
AA	£3m 4 years	£3m 5 years	£3m 15 years	£3m 5 years	£1m 10 years
AA-	£3m 3 years	£3m 4 years	£3m 10 years	£3m 4 years	£1m 10 years
A+	£3m 2 years	£3m 3 years	£3m 5 years	£3m 3 years	£1m 5 years
A	£3m 13 months	£3m 2 years	£3m 5 years	£3m 2 years	£1m 5 years
A-	£3m 6 months	£3m 13 months	£3m 5 years	£3m 13 months	£1m 5 years
None	£1.5m 6 months	n/a	£3m 25 years	£1m 5 years	£500k 5 years
Pooled funds and real estate investment trusts		£2.5m per fund or trust			

This table must be read in conjunction with the notes below

Credit rating: Investment limits are set by reference to the lowest published long-term credit rating from a selection of external rating agencies. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

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

Banks secured: Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

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

Corporates: Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made either following an external credit assessment or to a maximum as above per company as part of a diversified pool in order to spread the risk widely.

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

Pooled funds: Shares or units in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity and very low or no volatility will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

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

Real estate investment trusts: Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties. Investments in REIT shares cannot be withdrawn but can be sold on the stock market to another investor.

Operational bank accounts: The Authority may incur operational exposures, for example though current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but are still subject to the risk of a bank bail-in, and balances will therefore be kept below £500,000 per bank. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Authority maintaining operational continuity.

Risk assessment and credit ratings: Credit ratings are obtained and monitored by the Authority's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,

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

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

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

When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority’s cash balances, then the surplus will be deposited with the UK Government via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned but will protect the principal sum invested.

Investment limits: The Authority’s revenue reserves available to cover investment losses are forecast to be £37.1 million on 31st March 2020. The maximum that will be lent to any one organisation (other than the UK Government) will be as below. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers’ nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Table 4: Investment limits

	Cash limit
Any single organisation, except the UK Central Government	£4m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£4m per group
Any group of pooled funds under the same management	£5m per manager
Negotiable instruments held in a broker’s nominee account	£5m per broker
Foreign countries	£5m per country
Registered providers and registered social landlords	£2.5m in total
Unsecured investments with building societies	£2.5m in total

Loans to unrated corporates	£1m in total
Money market funds	£11m in total
Real estate investment trusts	£2.5m in total

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

Treasury Management Indicators

The Authority measures and manages its exposures to treasury management risks using the following indicators.

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

Credit risk indicator	**Target**
Portfolio average credit rating	*A*

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

Liquidity risk indicator	**Target**
Total cash available within 3 months	£2.5m

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

Interest rate risk indicator	**Limit**
Upper limit on one-year revenue impact of a 1% rise in interest rates	£500,000
Upper limit on one-year revenue impact of a 1% fall in interest rates	£500,000

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

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

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within 5 years	100%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

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

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

Price risk indicator	2020/21	2021/22	2022/23
Limit on principal invested beyond year end	£1.5m	£1.0m	£0.5m

Related Matters

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

Financial Derivatives: Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the *Localism Act 2011* removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

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

Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

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

Housing Revenue Account: On 1st April 2012, the Authority notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/ credited to the respective revenue account. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured at year end and interest transferred between the General Fund and HRA at the Authority's average interest rate on investments, adjusted for credit risk.

Markets in Financial Instruments Directive: The Authority has retained retail client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a smaller range of services but with the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the Executive Director of Finance believes this to be the most appropriate status.

Financial Implications

The budget for investment income in 2020/21 is £0.8 million. The budget for debt interest paid in 2020/21 is £0.3 million. If actual levels of investments and borrowing, or actual interest rates, differ from those forecast, performance against budget will be correspondingly different.

Other Options Considered

The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Executive Director of Finance, having consulted the Portfolio Holder for Finance, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

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

Appendix A – Arlingclose Economic & Interest Rate Forecast November 2019

Underlying assumptions:

- The global economy is entering a period of slower growth in response to political issues, primarily the trade policy stance of the US. The UK economy has displayed a marked slowdown in growth due to both Brexit uncertainty and the downturn in global activity. In response, global and UK interest rate expectations have eased.

- Some positivity on the trade negotiations between China and the US has prompted worst case economic scenarios to be pared back. However, information is limited, and upbeat expectations have been wrong before.

- Brexit has been delayed until 31 January 2020. While the General Election has maintained economic and political uncertainty, the opinion polls suggest the Conservative position in parliament may be strengthened, which reduces the chance of Brexit being further frustrated. A key concern is the limited transitionary period following a January 2020 exit date, which will maintain and create additional uncertainty over the next few years.

- UK economic growth has stalled despite Q3 2019 GDP of 0.3%. Monthly figures indicate growth waned as the quarter progressed and survey data suggest falling household and business confidence. Both main political parties have promised substantial fiscal easing, which should help support growth.

- While the potential for divergent paths for UK monetary policy remain in the event of the General Election result, the weaker external environment severely limits potential upside movement in Bank Rate, while the slowing UK economy will place pressure on the MPC to loosen monetary policy. Indeed, two MPC members voted for an immediate cut in November 2019.

- Inflation is running below target at 1.7%. While the tight labour market risks medium-term domestically-driven inflationary pressure, slower global growth should reduce the prospect of externally driven pressure, although political turmoil could push up oil prices.

- Central bank actions and geopolitical risks will continue to produce significant volatility in financial markets, including bond markets.

Forecast:

- Although we have maintained our Bank Rate forecast at 0.75% for the foreseeable future, there are substantial risks to this forecast, dependant on General Election outcomes and the evolution of the global economy.

- Arlingclose judges that the risks are weighted to the downside.

- Gilt yields have risen but remain low due to the soft UK and global economic outlooks. US monetary policy and UK government spending will be key influences alongside UK monetary policy.

- We expect gilt yields to remain at relatively low levels for the foreseeable future and judge the risks to be broadly balanced.

	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Average
Official Bank Rate														
Upside risk	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.21**
Arlingclose Central Case	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**
Downside risk	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	**-0.73**
3-month money market rate														
Upside risk	0.10	0.10	0.25	0.25	0.25	0.25	0.25	0.25	0.30	0.30	0.30	0.30	0.30	**0.25**
Arlingclose Central Case	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**
Downside risk	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	**-0.73**
1yr money market rate														
Upside risk	0.10	0.20	0.20	0.20	0.20	0.20	0.20	0.25	0.30	0.30	0.30	0.30	0.30	**0.23**
Arlingclose Central Case	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**	**0.85**
Downside risk	-0.30	-0.50	-0.55	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	**-0.60**
5yr gilt yield														
Upside risk	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.45	0.45	0.45	**0.37**
Arlingclose Central Case	**0.50**	**0.50**	**0.50**	**0.55**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.60**	**0.57**
Downside risk	-0.35	-0.50	-0.50	-0.55	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	**-0.56**
10yr gilt yield														
Upside risk	0.30	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.45	0.45	**0.37**
Arlingclose Central Case	**0.75**	**0.75**	**0.80**	**0.80**	**0.85**	**0.85**	**0.90**	**0.90**	**0.95**	**0.95**	**1.00**	**1.00**	**1.00**	**0.88**
Downside risk	-0.40	-0.40	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.45**
20yr gilt yield														
Upside risk	0.30	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.45	0.45	**0.37**
Arlingclose Central Case	**1.20**	**1.20**	**1.25**	**1.25**	**1.25**	**1.30**	**1.30**	**1.30**	**1.35**	**1.35**	**1.35**	**1.40**	**1.40**	**1.30**
Downside risk	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.50	-0.50	**-0.45**
50yr gilt yield														
Upside risk	0.30	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.40	0.40	0.45	0.45	**0.37**
Arlingclose Central Case	**1.20**	**1.20**	**1.25**	**1.25**	**1.25**	**1.30**	**1.30**	**1.30**	**1.35**	**1.35**	**1.35**	**1.40**	**1.40**	**1.30**
Downside risk	-0.40	-0.40	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.45	-0.50	-0.50	**-0.45**

PWLB Certainty Rate (Maturity Loans) = Gilt yield + 1.80%

PWLB Local Infrastructure Rate (Maturity Loans) = Gilt yield + 0.60%

Appendix B – Existing Investment & Debt Portfolio Position

	23/1/2020 **Actual Portfolio** **£m**	23/01/2020 **Average Rate** **%**
External borrowing: Public Works Loan Board Barclays	 **98.9** **5.0**	 **3.35** **4.71**
Total gross external debt	103.9	3.42
Total treasury investments	6.0	0.57
Net debt	97.9	

Redditch Borough Council

Minimum Revenue Provision Statement 2020/21

Annual Minimum Revenue Provision Statement 2020/21

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

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

The MHCLG Guidance requires the Authority to approve an Annual MRP Statement each year and recommends a number of options for calculating a prudent amount of MRP. The following statement incorporates options recommended in the Guidance and a locally determined approach to loans to third parties and asset backed capital expenditure where there are detailed plans in place to demonstrate that all expenditure will be recovered from income streams generated by the expenditure in an appropriate timeline.

- For capital expenditure incurred before 1st April 2008 MRP will be determined as 4% of the capital financing requirement in respect of that expenditure on an annuity basis.

- For unsupported capital expenditure incurred after 31st March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant asset as the principal repayment on an annuity with an annual interest rate of 4%, starting in the year after the asset becomes operational. MRP on purchases of freehold land will be charged over 50 years. MRP on expenditure not related to fixed assets but which has been capitalised by regulation or direction will be charged over 20 years.

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

- For capital expenditure loans to third parties that are repaid in annual or more frequent instalments of principal, the Council will make nil MRP, but will instead apply the capital receipts arising from principal repayments to reduce the capital financing requirement instead. In years where there is no principal repayment, MRP will be charged in accordance with the MRP policy for the assets funded by the loan, including where appropriate, delaying MRP until the year after the assets become operational.

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

- Where the council makes a capital contribution or loan to another entity or where responsibility for a council asset with borrowing attached is transferred to a third party, and

    - the payments are appropriately covered by assets

- there are detailed plans demonstrating that all the expenditure will be recovered in an appropriately short time frame

Then no MRP will be set aside. To ensure that this remains a prudent approach the Council will review the expenditure and income regularly to determine if the income or asset values have decreased to the point that MRP needs to be provided for. Should evidence emerge which suggests the expenditure will no longer be recovered MRP will be provided for.

- Where the council uses internal borrowing and receipts of rental income are greater than the MRP calculated then as there are sufficient revenues to repay the capital cost no MRP will be set aside.

Capital expenditure incurred during 2020/21 will not be subject to a MRP charge until 2021/22.

Based on the Authority's latest estimate of its capital financing requirement (CFR) on 31st March 2020, the budget for MRP has been set as follows:

	31.03.2020 Estimated CFR £m	**2020/21 Estimated MRP £**
Unsupported capital expenditure after 31.03.2008	19.8	910
Total General Fund		
Assets in the Housing Revenue Account	**23.3**	0
HRA subsidy reform payment	**98.9**	0
Total Housing Revenue Account	**122.2**	**0**
Total	**143.0**	**910**

Policy for Flexible use of Capital Receipts Purpose

1. This report reviews the statutory guidance on the flexible use of Capital Receipts and its application within this authority.

Background

2. Capital receipts can only be used for specific purposes and these are set out in Regulation 23 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 made under Section 11 of the Local Government Act 2003. The main permitted purpose is to fund capital expenditure and the use of capital receipts to support revenue expenditure is not permitted by the regulations.

3. The Secretary of State is empowered to issue Directions allowing expenditure incurred by local authorities to be treated as capital expenditure. Where such a direction is made, the specified expenditure can then be funded from capital receipts under the Regulations.

4. The Secretary of State for Communities and Local Government has issued guidance in March 2016, giving local authorities greater freedoms with how capital receipts can be used to finance expenditure. This Direction allows for the following expenditure to be treated as capital,

“expenditure on any project that is designed to generate ongoing revenue savings in the delivery of public services and/or transform service delivery to reduce costs and/or transform service delivery in a way that reduces costs or demand for services in future years for any of the public sector delivery partners.”

5. In order to comply with this Direction, the Council must consider the Statutory Guidance issued by the Secretary of State. This Guidance requires authorities to prepare, publish and maintain a Flexible Use of Capital Receipts Strategy with the initial strategy being effective from 1st April 2016 with future Strategies included within future Annual Budget documents.

6. There is no prescribed format for the strategy, the underlying principle is to support local authorities to deliver more efficient and sustainable services by extending the use of capital receipts to support the revenue costs of reform projects

7. The Statutory Guidance for the Flexible Use of Capital Receipts Strategy states that the Strategy should include a list of each project which plans to make use of the capital receipts flexibility, together with the expected savings that the project will realise. The Strategy should also include the impact of this flexibility on the affordability of borrowing by including updated Prudential Indicators.

Flexible Use of Capital Receipts Strategy

8. The Flexible Use of Capital Receipts Strategy is set out below

9. Government has provided a definition of expenditure which qualifies to be funded from capital receipts. This is: “Qualifying expenditure is expenditure on any project that is designed to generate ongoing revenue savings in the delivery of public services and/or transform service delivery to reduce costs and/or transform service delivery in a way that reduces costs or demand for services in

future years for any of the public sector delivery partners. Within this definition, it is for individual local authorities to decide whether or not a project qualifies for the flexibility.”

10. The Council's intends to use the following capital receipts to fund the following transformation projects:

Project description	2020/21
	£000
Restructure costs as part of ERP programme	150
Restructure of service delivery	300
Total General Fund	**450**
Housing system introduction and service redesign	300
Total HRA	**300**

11. The savings generated by these projects are set out in the table below.

Project description	2020/21
	£000
Restructure costs as part of ERP programme	15
Restructure of service	30
Total General Fund	**45**
Housing system introduction and service redesign	30
Total HRA	**30**

Impact on Prudential Indicators

12. The guidance requires that the impact on the Council’s Prudential Indicators should be considered when preparing a Flexible Use of Capital Receipts Strategy.

13. The indicators that will be impacted by this strategy are none. The scheme is currently funded from capital receipts and the new planned use of capital receipts will be funded from capital receipts which are currently unallocated.

14. The Prudential Indicators show that this Strategy is affordable and will not impact on the Council’s operational and authorised borrowing limits.

Investment Strategy Report 2020/21

Introduction

The Authority invests its money for three broad purposes:

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

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

Treasury Management Investments

The Authority typically receives its income in cash (e.g. from taxes and grants) before it pays for its expenditure in cash (e.g. through payroll and invoices). It also holds reserves for future expenditure and collects local taxes on behalf of other local authorities and central government. These activities, plus the timing of borrowing decisions, lead to a cash surplus which is invested in accordance with guidance from the Chartered Institute of Public Finance and Accountancy. The balance of treasury management investments is expected to fluctuate between £0m and £14m during the 2020/21 financial year.

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

Further details: Full details of the Authority's policies and its plan for 2020/21 for treasury management investments are covered in a separate document, the treasury management strategy.

Service Investments: Loans

Contribution: The Council may in future lend money to its subsidiaries and local businesses to support local public services and stimulate local economic growth.

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

Table 1: Loans for service purposes in £ millions

Category of borrower	31.3.2019 actual			2020/21
	Balance owing	Loss allowance	Net figure in accounts	Approved Limit
Subsidiaries	0	0	0	5
Local businesses	0	0	0	0.5
TOTAL	**0**	**0**	**0**	**0**

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

Risk assessment: The Authority assesses the risk of loss before entering into and whilst holding service loans by using specialist advice to understand the market and the potential future demands of the market and the customers in it. It will also use benchmarking data from the market to determine future potential risks which need to be planned for. External advice is only sought from credible sources eg acknowledged experts in their fields, and officers ensure that they fully understand any information given to them before decision or advice is taken.

Commercial Investments: Property

Contribution: The Council is currently and is planning to further invest in local (within the council's operating area boundary) commercial and residential property with the intention of regenerating the local area as well as making a surplus that will be spent on local public services, where a surplus will not be achieved a business case will explain the reasons as to why this is the case. To date the council has made one purchase, an office block. It is currently reviewing a number of potential investments in commercial property to ensure that the proposed investment is suitable for the authority and the risks of the investment are fully understood.

Table 3: Property held for regenerative and investment purposes in £ millions

Property	Actual	31.3.2019 actual		31.3.2020 expected	
	Purchase cost	Gains or (losses)	Value in accounts	Gains or (losses)	Value in accounts
Oak Tree Park	0.9	n/a	n/a	0	0.9
Property to be purchased during 2020	5.2 (planned)	n/a	n/a	n/a	n/a
TOTAL	**6.1**	**-**	**-**	**0**	**0.9**

Security: In accordance with government guidance, the Authority considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs.

A fair value assessment of the Authority's investment property portfolio will be undertaken every year. Should the 2019/20 year end accounts preparation and audit process value these properties below their purchase cost, then an updated investment strategy will be presented to full council detailing the impact of the loss on the security of investments and any revenue consequences arising therefrom.

Risk assessment: The Authority assesses the risk of loss before entering into and whilst holding property investments by involving specialist advisors with expertise in the type of property being purchased, looking at historic data and speaking to other councils undertaking similar activities.

Liquidity: Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice, and can take a considerable period to sell in certain market conditions. To ensure that the invested funds can be accessed when they are needed, for example to repay capital borrowed, the Authority ensures that properties purchased are in an active market where there is demonstrable demand to ensure that the authority does not purchase assets which it will not be able to sell on at a later date.

Proportionality

The Authority does not plan to become dependent on profit generating investment activity to achieve a balanced revenue budget.

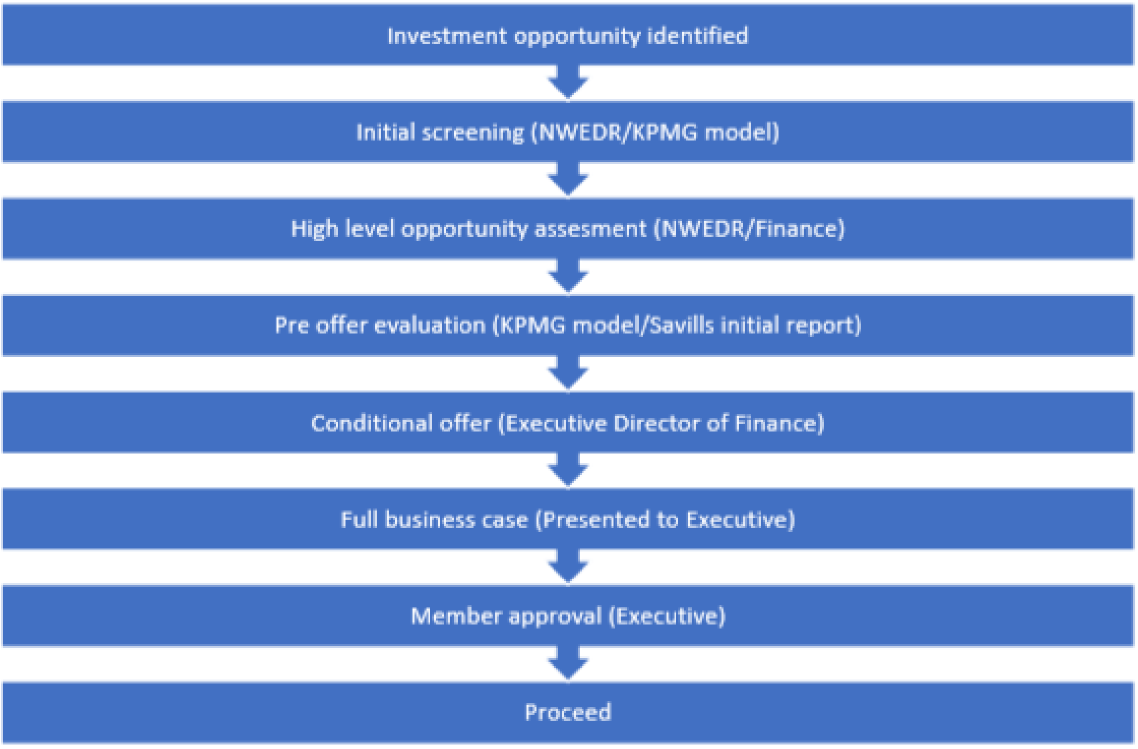
Capacity, Skills and Culture

Elected members and statutory officers: Member training will take place annually as part of the induction process. External advisors will provide reports to support investment decisions with officers ensuring that they fully understand them and can relate them to the strategic objectives and risk profile of the authority.

Commercial deals: Significant work has been undertaken using external advisors and relevant training courses have been attended to ensure that officers are fully aware of the code and statutory requirements of a local authority which is investing.

KPMG have developed a modelling tool for the authority to use when assessing potential purchases as a precursor to engaging with external consultants to ensure that potential purchases are likely to make sense from the perspective of the authority before incurring advisor costs. The minimum net yield for an investment return is largely to be set at 0.75%. However, following an internal review of policy, it has been decided that the council may wish to make purchases which do not make a financial return or may indeed make a loss in the short term. On these occasions a business case will be developed which specifies the non-financial benefits of the investment. These are likely to be regenerative schemes for the greater good of the area with an intended long term impact. The regenerative and redevelopment benefits which will flow from the investment will be taken into account in the development of the business case, so if the net investment yield falls below 0.75% it can still proceed if these benefits are deemed to outweigh the lower than target yield.

Corporate governance: when investment decisions are to be made, they are to be led by the Council’s Executive Director of Finance in consultation with the Corporate Management Team. They will assess the potential investment opportunity, consulting North Worcestershire Economic Development and Regeneration (NWEDR) and using the KPMG finance appraisal model, and should they decide it presents a strong opportunity for the authority and complies with the relevant criteria a conditional offer can be made. A business case will then be developed and presented ensuring that once greater detail is included, it makes a satisfactory income yield and/or economic redevelopment and regeneration impact. When the business case is completed, if it is still compliant with the council criteria, it will be presented to Executive for approval before purchase is completed.



Once a purchase has been made the Executive Director of Finance will provide quarterly updates, in line with budget monitoring reports on the status of the investment.

__Investment Indicators__

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

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

Table 5: Total investment exposure in £millions

Total investment exposure	**31.03.2019 Actual**	**31.03.2020 Forecast**	**31.03.2021 Forecast**
Treasury management investments	0	0	0
Service investments: Loans	0	0	0
Commercial investments: Property	0	0.9	6.1
TOTAL INVESTMENTS	0	0.9	6.1
TOTAL EXPOSURE	0	0.9	6.1

How investments are funded: Government guidance is that these indicators should include how investments are funded. Since the Authority does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. However, the following investments could be described as being funded by borrowing. The remainder of the Authority's investments are funded by usable reserves and income received in advance of expenditure.

Table 6: Investments funded by borrowing in £millions

Investments funded by borrowing	**31.03.2019 Actual**	**31.03.2020 Forecast**	**31.03.2021 Forecast**
Treasury management investments	0	0	0
Service investments: Loans	0	0	0
Commercial investments: Property	0	0.9	6.1
TOTAL FUNDED BY BORROWING	0	0.9	6.1

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

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

Investments net rate of return	**2018/19 Actual**	**2019/20 Forecast**	**Minimum Return**
Treasury management investments	0	0	0.4
Service investments: Loans	0	0	0.75
Commercial investments: Property	0	1.2	0.75
ALL INVESTMENTS	0	0	0.62

Table 8: Other investment indicators

Indicator	**2018/19 Actual**	**2019/20 Forecast**	**Limit**
Debt to net service expenditure ratio	0	9%	200%
Commercial income to net service expenditure ratio	0	0.8%	5%

This page is intentionally left blank