AUDIT, GOVERNANCE & STANDARDS COMMITTEE	14 January 2019

Treasury Management, Investment and Capital Strategies 2019/20

Final Decision-Maker	Council
Lead Head of Service/Lead Director	Mark Green, Director of Finance & Business Improvement
Lead Officer and Report Author	John Owen – Finance Manager
Classification	Public
Wards affected	None

Executive Summary

This report sets out the draft Treasury Management Strategy, Investment Strategy and Capital Strategy for 2019/20 for consideration by the Audit, Governance & Standards Committee and recommendation to Council for adoption. The strategies are attached as Appendices A-C to this report.

This report makes the following recommendations to this Committee:

1. That the Treasury Management Strategy for 2019/20 attached as Appendix A to this report is agreed and recommended to Council for adoption, subject to any amendments arising from consideration of the Capital Programme by Policy and Resources Committee at its meeting on 23rd January 2019.
2. That the Investment Strategy for 2019/20 attached as Appendix B to this report is agreed and recommended to Council for adoption.
3. That the Capital Strategy for 2019/20 attached as Appendix C to this report is agreed and recommended to Council for adoption.

Timetable	
Meeting	***Date***
Audit, Governance & Standards Committee	14th January 2019
Council	27th February 2019

Treasury Management, Investment and Capital Strategies 2019/20

1. **INTRODUCTION AND BACKGROUND**

1.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year must meet cash expenditure. The Treasury Management Strategy assists the Council in achieving this objective while maintaining value for money.

1.2 The first function of the Council's treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

1.3 The second main function of the treasury management operation is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, so this means longer term cash flow planning to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

1.4 The council has adopted the Treasury Management in Public Services: Code of Practice 2011 Edition ('the Code') issued by the Chartered Institute of Public Finance and Accountancy (CIPFA)

1.5 CIPFA defines treasury management as:

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

1.6 The current 2018/19 Strategy was reviewed by this Committee and agreed by Council in February 2018. A mid-year monitoring report was considered by this Committee at its November meeting. Essentially the Council are taking a similar stance with its Strategy for 2019/20, which is:

- to utilise cash balances rather than loan debt to finance the capital programme in the short term, due to low investment returns and high counterparty risk in the current economic climate;

- to further diversify its portfolio, as far as is operationally feasible, ensuring that a combination of secured and unsecured investments are considered. Greater use of Local Authority investments will be investigated where the borrowers offer high security and enable investment over a longer period where funds are not required immediately.

Changes to the Code

1.7 CIPFA revised the 2011 edition of the Code in 2017, which ensures that local authorities also take into account the risks involved with non-treasury investments. CIPFA have therefore recommended that authorities development an Investment Strategy – **Appendix B** and a Capital Strategy - **Appendix C** which set out the Council's risk appetite and specific policies and arrangements for non-treasury investments.

1.8 The three strategy documents are linked and support the overall Medium Term Financial Strategy (MTFS), alluding to the risk appetites around capital investment priorities and funding decisions including borrowing. Below is an illustration of how these documents are linked:

Table A.

MTFS – covers governance, long term plans and financial resourcing

TM Strategy	Investment Strategy	Capital Strategy
- Governance - Long term Planning incl. MRP - Risk appetite, key risks and sensitivities	- Approach, due diligence, risk appetite - Governance process for approval and monitoring] - Summary of material investments, guarantees and liabilities	

1.9 The Treasury Management Strategy (TMS) is set out at **Appendix A** to this report. It is consistent with the requirements of the CIPFA and MHCLG and has been developed in line with currently approved spending and financing proposals.

1.10 The Policy & Resources Committee will consider a capital programme for the period 2019/20 to 2023/24 at its meeting on 23th January 2019. The attached Strategy includes assumptions about the Capital Programme and it is not anticipated that the Capital Programme as finally agreed will differ significantly from these.

1.11 The following table shows the maximum prudential borrowing required to fund the draft capital programme. It is assumed that internal borrowing will be used to fund the 2019/20 programme and the Council will have to borrow externally from then on:

	2019/20 £	2020/21 £	2021/22 £
Capital Programme	21,887,430	9,894,220	8,449,400
Other Funding Streams (incl. New Homes Bonus)	(6,131,000)	(1,080,000)	(863,000)
Maximum Prudential Borrowing	15,756,430	8,814,220	7,586,400
Estimated Internal Borrowing	(9,650,000)	0	0
Expected Borrowing	6,106,430	8,814,220	7,586,400

Investment Strategy

1.12 The Investment Strategy focuses on service investments (supporting local services by lending or buying shares) and commercial investments (property investment to generate a profit).

1.13 The Council has made one loan to Kent Savers for £25,000 in 2017/18 which is repayable in 2022/23 at an interest rate of 1%. However, loans to Maidstone Property Holdings Limited and Cobtree Manor Estates Trust may also be made in the near future for which the interest rate applicable would be at commercial rates. There is a provision for these service loans of £1 million and £310,000 respectively.

1.14 The Council does not currently have any investments in property that are considered to be purely commercial in nature. Acquisitions are limited to properties situated within the borough, with the intention of supporting the local community, housing and regeneration objectives rather than for the exclusive purpose of generating profits. All property investments are therefore classified as general fund capital projects.

Capital Strategy

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

1.16 The strategy forms part of the Council's integrated revenue, capital and balance sheet planning and requires annual approval by full Council. It sets out the long term context in which capital expenditure and investment decisions are made, and considers risk, reward and impact on the achievement of the Council's priority outcomes identified within the strategic plan.

1.17 Clearly the Capital Strategy has close links with the Treasury Management Strategy, and it is therefore considered appropriate for the committee to review both documents at the same time.

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2. AVAILABLE OPTIONS

2.1 **Option 1:** The Committee could decide not to recommend the strategies to Council. The Council must adopt these strategies for 2019/20 and should the Committee decide not to recommend it would need to recommend an alternative to Council. The strategies are in line with the necessary codes and practice guides and take a low risk approach favouring liquidity and security over return. As such the approach set out within the strategies is considered suitable for this Council.

2.2 **Option 2:** Subject to any legal obligations placed upon the Council, the Committee could amend the strategies prior to recommendation to Council. The Committee would need to provide Council with detailed reasons for the amendments and the risks and benefits that the proposed amendments provide in order for the Council to make a fully informed decision on the recommendation.

2.3 **Option 3:** The Committee could agree the attached strategies and recommend them to Council. The attached strategies have been produced in line with current guidance from CIPFA and the Ministry of Housing for Communities and Local Government (MHCLG). They have also been developed in line with advice and guidance from the Council's Treasury Management Advisors.

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3. PREFERRED OPTION AND REASONS FOR RECOMMENDATIONS

3.1 The recommended option is Option 3, to recommend to Council the TMS, the investment strategy and the capital strategy as set out in Appendices A-C.

3.2 As stated above, the proposed strategies have been produced in line with current guidance from CIPFA and the Ministry of Housing for Communities and Local Government (MHCLG).

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4. RISKS

4.1 Detailed risk management policies are included within the Treasury Management Practices and have been included in both investment strategies and capital strategies to which the Council adheres to. A brief description of these risks along with the Council's actions to mitigate these risks are as follows:

Liquidity Risk - Liquidity risk is the risk that cash not be available when it is required. The Council has sufficient standby facilities to ensure that there is always sufficient liquidity to deal with unexpected occurrences. The Council also has an overdraft facility with Lloyds Bank of £500,000 plus the option of short term borrowing.

Interest Rate Risk - Interest rate risk is the risk that unexpected changes in interest rates expose the Council to greater costs or a shortfall in income than have been budgeted for. The Council will seek to minimise this risk by seeking expert advice on forecasts of interest rates from treasury management consultants and agreeing with them its strategy for the coming year for the investment and debt portfolios. It will also determine appropriate limits and trigger points which are set out in the annual Treasury Management Strategy .

Exchange Rate Risk - Exchange rate risk is the risk that unexpected changes in exchange rates expose the Council to greater costs or a shortfall in income than have been budgeted for. The Council has a minimal exposure to exchange rate risk as it has no powers to enter into loans or investments in foreign currency for treasury management purposes.

Inflation Risk - Inflation risk is the risk that unexpected changes in inflation expose the Council to greater costs or a shortfall in income than have been budgeted for. Inflation both current and projected will form part of the debt and investment decision-making criteria both within the strategy and operational considerations.

Credit and Counterparty Risk - Credit and counter-party risk is the risk of failure by a third party to meet its contractual obligations under an investment, loan or other commitment, especially one due to deterioration in its creditworthiness, which causes the Council an unexpected burden on its capital or revenue resources. Treasury management staff will add or delete counterparties to/from the approved counterparty list in line with the policy on criteria for selection of counterparties. Due to volatility of the financial market, Treasury Management staff will use information from various sources, eg brokers, Treasury Management Consultants and other local Authority experience to determine the credit worthiness of an institution and to decide if funds are at risk and agree best course of action with Director of Finance & Business Improvement.

Refinancing Risk - Refinancing risk is the risk that when loans or other forms of capital financing mature, that they cannot be refinanced where necessary on terms that reflect the assumptions made in formulating revenue and capital budgets. The Council is currently debt-free, however it will soon be looking to borrow to fund its capital programme in the coming years. In considering the affordability of its capital plans, the Council will consider all the resources currently available/estimated for the future together with the totality of its capital plans, revenue income and revenue expenditure forecasts for the forthcoming year and the two following years and the impact these will have on council tax. It will also take into account affordability in the longer term beyond this three year period.

Legal and Regulatory Risk - Legal and regulatory risk is the risk that either the Council, or a third party which it is dealing with in its treasury management activities, acts outside of its legal powers or regulatory requirements and as a result the Council incurs loss. The treasury management activities of the Council shall comply fully with legal statute, guidance, Codes of Practice and the regulations of the Council. The Authority will provide written evidence of its powers and authorities to any counterparty that requests us to do so. Counterparties will also provide their details to the Authority as a matter of course.

Fraud, Error and Corruption Risk - Fraud, error and corruption risk is the risk that the Council may fail to employ adequate systems, procedures and other arrangements which identify and prevent losses through such occurrences. The Council will seek to ensure an adequate division of responsibilities and maintenance at all times of an adequate level of internal checks which minimises such risks along with maintaining records of all treasury management transactions so that there is a full audit trail and evidence of the appropriate checks being carried out. Delegated members of staff have the responsibility for the treasury management function for the Council and the Director of Finance & Business Improvement authorises who these are. The Council also has a Fidelity Guarantee insurance policy with Zurich Insurance which covers against loss of cash through fraud or dishonesty of employees.

Risk Appetite – The Council takes a slightly higher risk with its non-treasury investments compared to its treasury management investments due to the fact treasury investments are mainly maintaining funds in high security instruments for when they are required and non-treasury decisions are for service delivery which may have to be riskier.

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5. CONSULTATION RESULTS AND PREVIOUS COMMITTEE FEEDBACK

5.1 None.

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6. NEXT STEPS: COMMUNICATION AND IMPLEMENTATION OF THE DECISION

6.1 This report will be considered by Council at its meeting on 27th February 2019.

7. CROSS-CUTTING ISSUES AND IMPLICATIONS

Issue	Implications	Sign-off
Impact on Corporate Priorities	We do not expect the recommendations will by themselves materially affect achievement of corporate priorities. However, they will support the Council's overall achievement of its aims as set out in section 3.	Head of Finance
Risk Management	Already covered in the risk section of the report.	Head of Finance
Financial	This report relates to the financial activities of the Council in respect of treasury management and specific	Director of Finance & Business Improvement

	financial implications are therefore detailed within the body of the report.	
Staffing	None	
Legal	The report is in compliance with statutory and legal regulations, e.g. CIPFA Code of Practice on Treasury management in local authorities.	Legal Team
Privacy and Data Protection	None	
Equalities	None	
Crime and Disorder	None	
Procurement	None	

8. REPORT APPENDICES

The following documents are to be published with this report and form part of the report:

- Appendix A: Treasury Management Strategy
- Appendix B: Investment Strategy
- Appendix C: Capital Strategy

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9. BACKGROUND PAPERS

9.1 None