TREASURY MANAGEMENT POLICY STATEMENT 2020/21

1 Introduction

1.1 The Council has adopted the key recommendations from the CIPFA Treasury Management Code of Practice. Accordingly the Council will create and maintain, as the cornerstone for effective treasury management, a Treasury Management Policy Statement, stating the policies, objectives and approach to risk management of its treasury management activities.

1.2 The Council will receive reports on its treasury management practices and activity including as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close.

1.3 The Council delegates responsibility for the monitoring and scrutiny of treasury management practices and activity to the Audit and Accounts Committee.

1.4 The Council has delegated responsibility for the execution and administration of the treasury management policy, strategy, practices and activity to the Council's Section 151 Officer. This officer should act in accordance with the Council's treasury management policy statement, strategy and Treasury Management Practices (TMP's) and as a member of CIPFA with standards of professional practice on treasury management.

2 Treasury Management Policy Objectives

2.1 The Council defines its treasury management activities as:

2.2 "The management of the Council'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."

2.3 The Council acknowledges that it is responsible for its treasury management decisions and activities.

2.4 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. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council.

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

2.6 The primary policy objective of the Treasury Management Strategy is:

i) To invest prudently having regard to the security of investments.

2.7 The supplementary policy objectives of the Treasury Management Strategy (in order of importance) are:

i) To maintain liquidity (accessibility) in the investment portfolio to meet the Council's spending plans;

ii) To aim to achieve the optimum return on investments commensurate with the proper levels of security and liquidity and predictability of returns; and

iii) To minimise the cost of any temporary borrowing (which may be required for day to day cash flow reasons).

3 The Council's Approach to Ethical Investments

3.1 As an organisation the Council does not have an overall ethical policy and has not defined what is, or what is not, ethical. The Council does not invest in equities and therefore does not have influence over the activities of companies that part-ownership might provide. However as an investor the Council is able to take the following approach:

i) For direct investments the Council will seek to ensure that counterparties (excluding the UK Government and other UK Local Authorities) have 'Responsible Investment Policies or Environmental, Social and Governance (ESG) policies' in place prior to investing;

ii) For indirect investments the Council will seek to ensure that any fund managers used have their own responsible investment policies or have signed up to widely recognised policies such as the United Nations Principles for Responsible Investment; and

iii) The Council recognises that it has no control or influence over where its counterparties themselves lend money or invest once an investment has been made by the Council.

Basingstoke and Deane Borough Council

TREASURY MANAGEMENT STRATEGY FOR 2020/21

Contents:

1 Background Information

1.1 This strategy statement has been produced in accordance with:

i) The Council's Treasury Management Policy Statement;

ii) The latest Code of Practice on Treasury Management published by the Chartered Institute of Public Finance and Accountancy (CIPFA);

iii) The Council's constitution which requires the annual production of a Treasury Management Strategy for the forthcoming year; and

iv) The Government Department guidance on local government investments which requires treasury management investments to consider security, liquidity and yield (in that order).

1.2 The Council's Treasury Management Strategy is undertaken within the following context:

i) The level of the Council's investment balances is one of the highest of all district authorities and has been for some time. The Council has therefore been able to take a longer term view on investment decisions; and

ii) The income generated from investments is significant to the Council and supports the cost of revenue services.

2 Interest Rate Forecast

2.1 In order to put a treasury management strategy into context it is necessary to appreciate the current forecasts for interest rates.

2.2 The UK Central Bank Official Rate (base rate) is currently at 0.75%. The average of forecasts from independent city forecasters is that the official rate will average 0.78% in 2020, 0.95% in 2021 and 1.24% in 2022.

2.3 The Council's treasury advisors (Arlingclose Ltd) are forecasting that the Bank of England will hold rates at 0.75% for the foreseeable future but with risks significantly weighted to the downside.

2.4 The Council's advisors' forecasts for interest rates for future years are shown in Table 1:

Table 1 – Arlingclose's Forecast for Interest Rates (Jan 2020)

	Official Bank Rate			Longer Term Rates (5yr Gilts)		
	Upside Risk	Central Case	Downside Risk	Upside Risk	Central Case	Downside Risk
	%	%	%	%	%	%
Mar-20	0.00	**0.75**	-0.50	+0.30	**0.50**	-0.35
Jun-20	0.00	**0.75**	-0.75	+0.35	**0.50**	-0.50
Sep-20	0.00	**0.75**	-0.75	+0.35	**0.55**	-0.55
Dec-20	+0.25	**0.75**	-0.75	+0.35	**0.55**	-0.55
Mar-21	+0.25	**0.75**	-0.75	+0.35	**0.55**	-0.55
Jun-21	+0.25	**0.75**	-0.75	+0.35	**0.60**	-0.60
Sep-21	+0.25	**0.75**	-0.75	+0.35	**0.60**	-0.60
Dec-21	+0.25	**0.75**	-0.75	+0.35	**0.65**	-0.65
Mar-22	+0.25	**0.75**	-0.75	+0.35	**0.65**	-0.65
Jun-22	+0.25	**0.75**	-0.75	+0.40	**0.70**	-0.70
Sep-22	+0.25	**0.75**	-0.75	+0.45	**0.75**	-0.75
Dec-22	+0.25	**0.75**	-0.75	+0.45	**0.75**	-0.75

2.5 Arlingclose's commentary on their forecasts is as follows:

i) "We have maintained our Bank Rate forecast at 0.75% for the foreseeable future. Substantial risks to this forecast remain, arising primarily from the government's policy around Brexit and the transitionary period."

ii) "Gilt yields 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."

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

3 Overall Resources and the Treasury Management Portfolio

3.1 The Council's Balance Sheet as at 31 March 2019 shows that it had overall net assets of approximately £419.00M. This included £285.70M of investment property and £138.70M of cash resources in the form of long and short term treasury investments.

3.2 The Council's Medium Term Financial Forecast estimates that the Council will have cash resources of £117.00M at the beginning of 2020/21. The latest forecast is for this to increase by £15.00M in the early part of the year before reducing to £111.00M at the end of the year. This results in an average balance for the year of £129.00M and this is expected to generate £2.56M of interest income in 2020/21.

3.3 The Council's existing investment portfolio reflects the effect of previous treasury management strategies. Investments have been made for a combination of short and long term periods using different investment instruments.

3.4 A breakdown of the forecast investment portfolio position as at 31 March 2020 shows total investments of £117.00M (at cost) as shown in Table 2.

Table 2 – Expected Treasury Investment Portfolio 31 March 2020

Instruments	£'M	%	Maximum Limit
Government Gilts	12.30	11%	91%
Local Authority Deposits/Bonds	14.00	12%	£50.00M
Money Market Funds	10.70	9%	£25.00M
Collective Investment Funds	80.00	68%	£120.00M
Total Investments	**117.00**	**100%**	

4 Risk Management Assessment

4.1 Treasury management involves the management of risk as no treasury management activity is without some risk.

4.2 Due to the size, complexity and importance of the income generated from treasury management activities it is important that all associated risks are assessed and managed.

4.3 The main risks associated with treasury management are as follows:

i) **Credit and counterparty risk** (risk to capital) – the risk that a third party will fail to meet its contractual investment obligation resulting in a loss of the Council's capital investment or the risk that there will be a permanent reduction in the capital value of the investment.

ii) **Liquidity risk** – the risk that the Council will commit too much of its investments in fixed term investments and might have to recall investments prematurely resulting in possible additional costs or losses upon disposal of tradable securities.

iii) **Market or interest rate risk** – the risk that fluctuating interest rates will have an adverse impact on the Council's investment income or the value of its investments.

iv) **Other risks** – this includes inflation risks and risks associated with cash management, legal requirements and fraud.

4.4 These risks are managed as follows:

i) Credit and Counterparty Risk (risk to capital)

Wherever possible the Council will attempt to externalise the management of credit risk through the use of pooled funds and fund managers who have the required knowledge, experience and resources needed to assess and monitor credit risk effectively.

For any remaining internally managed credit risk the Council's exposure to this risk is controlled by limiting the maximum sum invested with any single counterparty and by restricting investments to only those counterparties considered to be of high credit quality, as agreed in the Council's Treasury Management Practices.

The Council's treasury advisors (Arlingclose Ltd) provide advice on the security of the Council's investments which includes credit ratings and other factors such as sovereign guarantees, country of origin, credit default swaps, share prices and market sentiment.

The assessment of security also includes credit ratings produced by the international credit rating agencies which are used throughout the banking and investment industry. Credit ratings are continuously monitored.

The market prices of the Council's tradable investments are also monitored as these give an indication of market sentiment which can include credit concerns.

If the credit rating of a counterparty or a security held by the Council is downgraded with the result that it no longer meets the Council's minimum acceptable credit quality or other factors give cause for serious concern then potential opportunities to dispose of the security will be investigated.

The Council requires the necessary flexibility in its treasury management investment strategy to enable it to move a proportion of the portfolio into safer investment instruments during times of general concern about credit risk.

ii) Liquidity Risk

This risk is managed by maintaining a minimum proportion of investments in the short term for cash flow purposes and by setting a maximum amount that can be invested long term (more than 364 days).

When investing in external funds the Council will have regard to each fund's access requirements (daily, monthly, quarterly etc.) and will ensure that a suitable mix of fund liquidity is available to meet planned expenditure.

When the Council is using fixed long term investments it sets limits on the maximum amount that can be invested in each future year to ensure that the maturity structure for its investments results in a significant amount of investments maturing each year. The maturities can be used (rather than being re-invested) if required for short term cash requirements.

The Council also has the option to borrow short term funds in order to meet its commitments if necessary.

iii) Market or Interest Rate Risk

The Treasury Management Strategy attempts to control interest rate risk by spreading investments across different financial instruments and for different time periods.

When using external funds consideration is given to the interest rate risk characteristics of each fund as part of the selection process.

The fund manager's ongoing effectiveness in managing the risk is monitored on a regular basis with the assistance of the Council's treasury advisors.

The Council uses a mix of instruments in order to spread the risk and reduce the overall volatility. Limits are set on the maximum amount in each type of investment.

A proportion of investments in long term fixed rate instruments would provide the Council with stable and known amounts of income for a sustained period of time.

A proportion of investments at variable interest rates would enable the Council to benefit from future increases in interest rates.

Internally managed investments that have a fluctuating market price are purchased with the intention that they will be held to maturity ('buy to hold'), thereby reducing the impact of market risk.

In addition, the Council currently has an interest rate risk reserve (estimated to be £2.63M as at 31 March 2020).

iv) Other Risks

These risks are managed through the Council's adoption of standard Treasury Management Practices (TMPs) which are reviewed annually. These cover all aspects of treasury management procedures including cash flow forecasting, documentation, monitoring, reporting and division of duties.

All treasury management procedures and transactions are subject to annual inspections by both internal and external auditors.

The Council also employs external financial advisors to provide information on market trends, credit rating alerts, lending criteria advice and investment opportunities.

The Council will ensure that all staff and elected members tasked with treasury management responsibilities will receive appropriate training relevant to their needs and understand fully their roles and responsibilities.

5 Treasury Management Risks Indicators

5.1 The Council measures and manages its exposure to treasury management risk using the indicators set out in Table 3.

Table 3 – Treasury Management Risk Indicators

	2020/21	
Credit Risk Indicator Portfolio average credit rating	A-	
Liquidity Risk Indicator Total cash available within 3 months	£100.00M	
Interest Rate Risk Indicator Revenue impact of a 1% change in rates	£0.50M	pa
Price/Market Risk Indicator Revenue impact of a 1% change in value of investments	£1.00M	pa

5.2 The Council will measure its exposure to credit risk by monitoring the overall credit rating/score of its treasury portfolio. This is calculated by applying a score to each investment (AAA = 1, AA+ = 2, etc.) and taking the average, weighted by the size of the investment. Unrated investments are assigned a score based on their perceived risk.

5.3 The Council will measure its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three month period, without borrowing.

5.4 The interest rate risk indicator is set to measure the Council's exposure to interest rate risk by monitoring the impact that a 1% rise or fall in interest rates would have on the Council's income.

5.5 The price/market risk indicator is set to measure the Council's exposure to price/market risk by monitoring the revenue impact that a 1% rise or fall in the capital value of the Council's investments would have on the Council's income (before the effect of the Government's temporary statutory override).

5.6 These indicators will be monitored throughout the year and will be reported quarterly to the Audit and Accounts Committee and half-yearly to Council.

6 The Treasury Investment Strategy for 2020/21

Background

6.1 The Treasury Management Strategy is drawn up in order to comply with central government guidance on Local Government Investments and CIPFA's Treasury Management Code of Practice.

6.2 The Treasury Management Strategy sets out the ranges and limits within which the treasury management function can operate. It states which investment instruments the Council may use for the prudent management of its treasury balances during the financial year and sets limits on the different types of investment instrument.

Investment Objectives

6.3 The treasury management policy objectives for this Council are to invest prudently having regard to all of the associated risks including the security of investments and to maintain liquidity in the investment portfolio to meet the Council's spending plans.

Fund Selection

6.4 The selection of collective investment schemes or pooled funds will be determined following a selection process that will include evaluation of certain criteria including the size, duration, credit-worthiness of the underlying investments, income distribution levels, past performance, management fees and risk and reward profiles.

6.5 The Council will seek to ensure that any fund managers used have their own responsible investment policies or have signed up to widely recognised policies such as the United Nations Principles for Responsible Investment.

6.6 Any selection of funds or fund managers by the Council would be made with the assistance of its treasury management advisors Arlingclose Ltd or KPMG Investment Advisory.

Counterparty Selection

6.7 For in-house specified investments the Council has determined that the minimum allowable credit rating for investments that are not with the UK Government or a UK local authority will be a long term rating of : A- (Fitch); A3 (Moody's); A- (Standard & Poor's).

6.8 The Council will seek to ensure that counterparties (excluding the UK Government and other UK Local Authorities) have 'Responsible Investment Policies or Environmental, Social and Governance (ESG) policies' in place prior to investing.

6.9 The lowest available counterparty credit rating will be used to determine credit quality.

6.10 In the event that the credit rating of the Council's contracted provider of banking services falls below the Council's minimum credit rating criteria the bank will continue to be used for business continuity and short term liquidity requirements (overnight and weekend) and the Council will ensure that balances are kept at the minimum amount practicable.

6.11 Currently, the Council's banking services are provided by HSBC Bank Plc.

6.12 For long term investments with other UK local authorities the Council will consider their financial strength by assessment of their financial statements and other external indicators where available.

6.13 For externally managed investments minimum credit ratings shall be determined by the fund managers as part of their own investment policy and this policy will be considered fully by the Council as part of the fund selection process prior to investment in any fund.

6.14 The Council understands that credit ratings are not perfect predictors of investment default. Full regard will therefore be given to other available information on credit quality including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

6.15 All credit ratings and other factors detailed above are by Arlingclose Ltd (the Council's treasury advisors) and the Council is alerted to any changes.

6.16 The Council will consider the use of counterparties outside of the United Kingdom where the country of origin has a sovereign rating of not lower than AA+ or equivalent. The Council may also have exposure to non-UK investments indirectly through the use of money market funds and collective investment funds.

Investment Balances / Liquidity of Investments

6.17 Based on cash flow forecasts, the Council anticipates its fund balance at the end of 2020/21 will be £111.00M. Of this, approximately £10.00M is required for cash flow requirements.

6.18 Giving due consideration to the Council's level of balances over the next three years, the need for liquidity and its spending commitments, the Council has determined that £100M of its overall fund balances could be prudently committed to investments beyond 364 days.

6.19 Where investments are made in longer term instruments, the Council will have regard to liquidity by using funds with appropriate withdrawal policies or by spreading fixed term investments over future years ensuring that significant amounts mature each year.

Allowable Investment Types for 2020/21

6.20 In deciding which types of investment to use the Council has regard to its treasury management advisors. This year's strategy has been produced following consultation with the Council's advisors and with assessment of the risks and returns of the different instruments used.

6.21 The investment types that this Council will allow to be used for new investment in 2020/21 are as follows

Bank overnight call account deposits
Debt Management Agency Deposit Facility
Treasury Bills
Money Market Funds
Collective investment schemes (unitised pooled funds)*
Covered bonds with a AAA rating issued by banks and building societies up to 5 years**
Reverse repurchase agreements with banks and building societies up to 3 years (subject to minimum quality of collateral)
Loans to UK local authorities up to 5 years
Loans to UK registered providers of social housing and registered social landlords (formerly known as housing associations) up to 5 years**
Bonds issued by UK local authorities up to 10 years
UK treasury stock (Gilts) up to 10 years
Supranational bonds up to 10 years

*Includes: Diversified Credit Funds; Absolute Return Bond Funds; Property Funds; Multi-Asset Funds; and Short Term Cash Funds.
**Newly added for 2020/21 onwards.

6.22 All investments will be denominated in pounds sterling.

6.23 The Authority defines “high credit quality” organisations and securities as:

- UK Government
- UK Local Authorities
- UK registered providers of social housing
- AAA rated Supranational bonds
- AAA rated covered bonds
- Low Volatility Net Asset Value (LVNAV) Money Market Funds
- Banks and building societies with a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher.

6.24 The code requires the Council to state its position regarding the use of derivative investments. The Council does not intend to use standalone financial derivatives directly. However, the use of derivatives by fund managers or collective investment schemes (pooled funds) is permitted.

6.25 The Council will allow all previously purchased investments which are held as a result of investment decisions made under an earlier year’s approved strategy to be held during 2020/21.

6.26 For each type of investment that might be used during 2020/21 the maximum amounts allowed (actual amount or percentage of the overall portfolio) are shown in Table 4.

Table 4 - Limits for Types of Investment

Type of Investment	**Counter-party Limit 2020/21**	**Maximum Limit £'s/ % age of Portfolio**
Government Gilts	None	91%
Treasury Bills	None	91%
H M Treasury (DMADF)	None	100%
Supranational Bonds	£20.00M	£50.00M
Local Authority Loans	£5.00M	£50.00M
Loans to Registered Providers	£5.00M	£10.00M
Money Market Funds	£5.00M	£25.00M
Short Term Cash Funds	£5.00M	£15.00M
Collective Investment Funds [1]	£25.00M	£120.00M
Bank and Building Society Repurchase Agreements[2]	£10.00M	£25.00M
Bank and Building Society Covered Bonds[2]	£5.00M	£20.00M
Bank Overnight Call Accounts[2]	£5.00M	£10.00M

[1]Counterparty limit is per fund. Collective Investment Funds include Diversified Credit Funds, Absolute Return Funds and Property Funds and Multi-Asset Funds.
[2]Includes a £20.00M limit on each allowable foreign country.

6.27 For bank and building society investments counterparties will be chosen in conjunction with the Council's treasury advisors and will be approved by the Chief Finance Officer. A group of banks under the same ownership will be treated as a single organisation for counterparty limit purposes.

6.28 Under the new IFRS 9 accounting standard the Council is required to state its business model for accounting for certain investments. The Council aims to achieve value from its internally managed investments by a business model of collecting the income under a buy to hold strategy and does not aim to make short term gains from selling investments when the valuation of those investments change.

7 Borrowing Requirement and Strategy for 2020/21

7.1 Any borrowing (long term or short term) will be within the Council's Authorised Borrowing Limit of £50.00M as set out in the Council's Capital Investment Strategy.

7.2 The Council is expecting to have external borrowing of £2.20M in 2020/21.

7.3 The Council has no other plans or intentions to carry out any further long term external borrowing during 2020/21 however it has taken steps to secure preferential borrowing rates (called the Certainty Rate) from the PWLB in case the borrowing position changes.

7.4 The Council might occasionally borrow on a short term basis for cash flow reasons.

8 Cash-flow Management

8.1 The Council actively manages its cash flows and looks for opportunities to make savings as well as investments.

8.2 The Council will be taking advantage of an offer from its pension fund administrators relating to the advance payment of employer pension contributions in return for a discount on the amounts payable resulting in an overall saving of approx. £0.26M over the next 3 years.

9 Treasury Management Performance Monitoring and Reporting

9.1 Performance of the Council's treasury function will continue to be monitored monthly and will be reported quarterly to the Audit and Accounts Committee. Half year and outturn reports on treasury management activities and performance will also be prepared for Full Council.

9.2 The Council participates in quarterly portfolio benchmarking provided by its treasury advisors Arlingclose. This benchmarking includes measures of the level of risk taken and the corresponding returns. Results of the benchmarking exercise are included in all of the monitoring reports detailed above.

10 Training

10.1 The Treasury Management Code of Practice requires the Chief Financial Officer to ensure that all members tasked with treasury management responsibilities, including scrutiny of the function, have access to appropriate training relevant to their needs and understand fully their roles and responsibilities.

10.2 Treasury workshops are provided for members of the Audit and Accounts Committee and are open to all members of the Council. The workshops are delivered by a combination of external training providers, Council officers and the Council's treasury advisors.

10.3 Officers responsible for treasury management attend external workshops and seminars as part of their continued professional development.

11 Use of Investment Consultants/Treasury Advisors

11.1 The Council has contracted Arlingclose Ltd. as treasury advisors. Under the contract Arlingclose provide the following services:

- Advice on counterparty selection and creditworthiness;
- Assistance in compliance with codes of practice;
- Economic and interest rate forecasts;
- Strategy and review meetings;
- An annual report on the Council's investment strategy and portfolio;
- Advice and guidance on treasury management issues;
- Benchmarking and performance monitoring; and
- Seminars and training events.

11.2 The Council has also contracted KPMG Investment Advisory to provide asset allocation advice and monitoring services for the externally managed collective investment schemes (pooled funds) that are used by the Council.