



Cabinet

Decision Maker	Cabinet
Date	17 February 2022
Status	General Release
Title	Treasury Management Strategy Statement for 2022/23 to 2026/27
Wards Affected	All
Policy Context	To manage the Council's finances prudently and efficiently.
Cabinet Member	Cabinet Member for Finance and Smart City
Financial Summary	<p>The Annual Treasury Management Strategy Statement sets out the Council's strategy for ensuring that:</p> <ul style="list-style-type: none">a. its capital investment plans are prudent, affordable and sustainable;b. the financing of the Council's capital programme and ensuring that cash flow is properly planned;c. cash balances are appropriately invested to generate optimum returns having regard to security and liquidity of capital.
Report of:	<p>Gerald Almeroth Executive Director of Finance and Resources galmeroth@westminster.gov.uk 020 7641 2904</p>

1. EXECUTIVE SUMMARY

- 1.1 The Local Government Act 2003 (“the Act”) and the Regulations made under the Act require the Council to have regard to the Prudential Code for Capital Finance in Local Authorities and to set Prudential Indicators for the next three years to ensure that the Council’s capital investment plans are affordable, prudent and sustainable. These are contained within this report.
- 1.2 The Act also requires the Council to set out a statement of its treasury management strategy for borrowing and to prepare an Annual Investment Strategy (as shown in Appendix 1). This sets out the Council’s policies for managing its investments and for giving priority to the security and liquidity of those investments. The Treasury Management Strategy Statement and Annual Investment Strategy must both have regard to guidance issued by the Department for Levelling Up, Housing and Communities (DLUHC) and must be agreed by the Full Council.
- 1.3 This report sets out the Council’s proposed Treasury Management Strategy Statement (TMSS) for the period 2022/23 to 2026/27, and Annual Investment Strategy (AIS) for the year ended 31 March 2023, together with supporting information.
- 1.4 The TMSS and AIS form part of the Council’s overall budget setting and financial framework.
- 1.5 There are no material changes from the 2021/22 TMSS.

2. RECOMMENDATIONS

- 2.1 The Cabinet is asked to recommend to Full Council the approval of:
 - the Treasury Management Strategy Statement;
 - the borrowing strategy and borrowing limits for 2022/23 to 2026/27 set out in section 6;
 - the Prudential Indicators set out in section 8;
 - the Annual Investment Strategy and approved investments set out in Appendix 1;
 - the Minimum Revenue Provision Policy set out in Appendix 2.

3. REASONS FOR DECISIONS

- 3.1 To comply with the Local Government Act 2003, other regulations and guidance and to ensure that the Council’s borrowing and investment plans are prudent, affordable and sustainable and comply with statutory requirements.

4. BACKGROUND INFORMATION

- 4.1 The Council is required to operate a balanced budget, which broadly means that monies received during the year will meet payments expenditure. The function of treasury management is to ensure that the Council’s capital programme and corporate investment plans are adequately funded, and the cashflow is adequately planned, with cash being available when it is needed to discharge the Council’s legal obligations and deliver Council services. Surplus monies are invested to obtain an optimal return, while ensuring security of capital and liquidity.

- 4.2 The Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as “the management of the local authority’s borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.”
- 4.3 The Council has formally adopted CIPFA’s Code of Practice on Treasury Management and follows the key requirements of the Code as set out in Appendix 3.
- 4.4 The TMSS covers three main areas summarised below:

Capital spending

- Capital spending plans
- Other investment opportunities
- Capital Finance Requirement (CFR)
- Affordability

Borrowing

- Borrowing strategy
- New Loans
- Limits on external borrowing
- Maturity structure of borrowing
- Policy on borrowing in advance of need
- Forward borrowing
- Debt rescheduling
- Investing primarily for yield

Managing cash balances

- The current cash position and cash flow forecast
- Prospects for investment returns
- Council policy on investing and managing risk
- Balancing short and long term investments
- Improving investment returns

- 4.5 The Annual Investment Strategy (AIS) at Appendix 1 provides more detail on how the Council’s surplus cash investments are to be managed in 2022/23. Approved schedules of specified and non-specified investments will be updated following consideration by Members and finalisation of 2022/23 budget plans.
- 4.6 CIPFA published revised Treasury Management and Prudential codes on 20 December 2021 and has stated that formal adoption is not required until the 2023/24 financial year. The Council must regard to these codes when it prepares the Treasury Management Strategy Statement and Annual Investment Strategy, and also related reports (monitoring and outturn) during the financial year, submitted to the Audit and Transparency Committee.
- 4.7 The revised codes will have the following implications for 2023/24:
- adoption of a new debt liability benchmark treasury indicator to support the financing risk management of the capital financing requirement;

- clarification of what CIPFA expects a local authority to borrow externally and what is regarded as inappropriate: requirement to adopt a proportionate approach to commercial and service capital investment;
- addressing of environmental, social and governance (ESG) issues within the capital strategy;
- review of the commercial property portfolio, with a view to divest where appropriate;
- documentation of investment practices to manage risks associated with non-treasury investment;
- business model to support long term treasury investment;
- effective management of liquidity and longer term cash flow requirements;
- amendment to TMP1 (Treasury Management Practice) to address ESG policy within the treasury management risk framework;
- knowledge and skills register for individuals involved in the treasury management function (proportionate to the size and complexity of the treasury management operation);
- requirement to clarify reporting requirements for service and commercial investments (particularly where supported by borrowing/leverage).

TREASURY MANAGEMENT STRATEGY STATEMENT

5. SECTION 1 - CAPITAL SPENDING

Capital spending plans

- 5.1 The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.
- 5.2 Table 1 summarises the Council's capital expenditure plans, both in terms of those projects agreed previously, and those forming part of the current budget cycle. The table sets out the Council's current expectations reference the revenue or capital financing.
- 5.3 Compared with the forecast in the original 2021/22 TMSS, General Fund capital spend has slipped back by around £168m in the 2022/23 revised budget and there remains an element of further slippage in future years.

The risks are that:

- continued slippage in new starts will push borrowing requirements to later years when interest rates are forecast to be higher than currently;
- slippage in the programme of capital receipts may increase the need to borrow in the short to medium term.

Table 1 Capital spending and funding plans

2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	Total
Actual	Forecast	Estimate	Estimate	Estimate	Estimate	Estimate	
£m	£m	£m	£m	£m	£m	£m	£m
Expenditure							
135 General Fund	271	302	307	431	333	185	1,829
140 HRA	165	198	229	214	131	86	1,023
275	436	500	536	645	464	271	2,852
Funding							
General Fund							
45 Grants & Contributions	84	47	39	22	10	11	213
9 Capital Receipts Applied	7	84	47	9	80	122	349
1 Revenue Financing	0	0	0	0	0	0	0
HRA							
88 Grants & Contributions	96	105	117	100	68	58	544
52 Capital Receipts Applied	30	42	81	89	23	23	288
195	217	278	284	220	181	214	1,394
80 Net financing need for the year	219	222	252	425	283	57	1,458

Other investment opportunities

- 5.4 As well as investing in assets owned by the Council and used in the delivery of services, the Council can also invest, where appropriate, in:
- infrastructure projects, such as green energy;
 - loans to third parties;
 - shareholdings, and loans to limited companies and joint ventures.
- 5.5 Such investments are treated as expenditure for treasury management and prudential borrowing purposes even though they do not create physical assets in the Council's accounts. Appropriate budgets in respect of these activities are agreed as part of the Council's budget setting and ongoing monitoring processes and considered as part of the Annual Investment Strategy.
- 5.6 In addition, the Council has a substantial commercial investment property portfolio which forms part of the investment strategy. The Council has allocated funds of £120m. The aim is to diversify the property portfolio into sectors that have historically been considered alternatives but are increasingly being viewed as mainstream. The strategy focuses on increasing the income generated by the Council from its property holdings, while also meeting its strategic aims. Future Public Work Loans Board (PWLB) borrowing will not form part of the investment portfolio's source of external funding.
- 5.7 The Council has also invested £30m within the overall context of the Council's annual investment strategy in a residential housing partnership. This partnership was developed in response to the lack of private rented accommodation accessible to rising numbers of people living in temporary accommodation or otherwise at risk of homelessness in London.

Capital Financing Requirement (CFR)

- 5.8 The CFR measures the extent to which capital expenditure has not yet been financed from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so its underlying borrowing need. Any capital expenditure which has not immediately been paid for through a revenue or capital resource, will increase the CFR.
- 5.9 The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each asset's life, and so charges the economic consumption of capital assets as they are used.
- 5.10 Table 2 shows that the CFR will increase over the medium term. Consequently, the capital financing charge to revenue will increase, reflecting the capital spending plans.

Table 2 Capital Financing Requirement forecast

2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
Actual	Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
£m	£m	£m	£m	£m	£m	£m
CFR as at 31 March						
598 General Fund	778	949	1,170	1,570	1,813	1,865
294 HRA	333	384	415	440	480	485
892	1,111	1,333	1,585	2,010	2,293	2,350
Annual Charge						
81 General Fund	180	171	221	400	243	52
0 HRA	39	51	31	25	40	5
81	219	222	252	425	283	57
Reason for Change						
100 Net financing	238	242	276	454	325	106
(19) Less MRP	(19)	(20)	(24)	(29)	(42)	(49)
81	219	222	252	425	283	57

- 5.11 Table 3 below confirms that the Council's gross debt does not exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for current year and the following financial years. This allows some flexibility for limited early borrowing for future years and ensures that borrowing is not undertaken for revenue purposes.

Table 3 Borrowing compared to the Capital Financing Requirement

2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
Actual	Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
£m	£m	£m	£m	£m	£m	£m
206 Gross Projected Debt	238	400	587	571	558	549
892 Capital Financing Requirement	1,111	1,333	1,585	2,010	2,293	2,350
686 Under / (over) borrowing	873	933	998	1,439	1,735	1,801

- 5.12 The Council’s MRP policy is shown at Appendix 2. The Department for Levelling Up, Housing and Communities (DLUHC) has issued a Consultation on changes to Minimum Revenue Provision (MRP), for which the deadline for response is 8 February 2022. Government’s intention is not to change policy, but to clearly set out in legislation the practices that authorities should already be following. Authorities that are already fully compliant with MRP requirements (including Westminster) will be unaffected.
- 5.13 There are two changes proposed to the 2003 MRP Regulations, which already reflect general local authority accounting practice:
1. Capital receipts may not be used in place of the revenue charge.
 2. Prudent MRP must be determined with respect to the authority’s total capital financing requirement, with the intention of stopping the intentional exclusion of debt from the MRP determination because it relates to an investment asset or capital loan.
- 5.14 Members will be updated on how the new Regulations will impact the Council’s current approach (minimal) and any changes required will be formally adopted within MRP appendix within the 2023/24 TMSS Strategy report.

Affordability

- 5.15 The objective of the affordability indicator is to ensure that the level of investment in capital assets proposed remains within sustainable limits and, in particular, the impact on the Council’s “bottom line”. The estimates of financing costs include current commitments and the proposals in the Council’s budget report. Table 4 below sets out the expected ratio of capital financing costs to income for both General Fund and HRA activities:

Table 4 Ratio of capital financing costs to income

2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
Actual	Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
%	%	%	%	%	%	%
(3.60) General Fund	(10.33)	(11.67)	(13.60)	(14.15)	(13.98)	(13.79)
46.91 HRA	45.15	44.98	44.94	43.67	43.40	43.07

- 5.16 For the next five years, gross capital financing charges for the General Fund capital programme are largely outweighed or balanced by income from investments and the commercial property portfolio. The capital financing charges arising from the HRA capital programme remain in line with the forecast increase income, hence, capital charges as a proportion of the HRA net revenue stream remain relatively steady.

6. SECTION 2 - BORROWING

Borrowing strategy

- 6.1 One of the main functions of the treasury management service is the funding of the Council’s capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the 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, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

- 6.2 The Council's main objective when borrowing money is to strike an appropriate balance between securing low interest costs and achieving cost certainty over the period for which funds are required. Given the significant cuts to public expenditure and, in particular, to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the long-term stability of the debt portfolio.

The key factors influencing the 2022/23 strategy are:

- forecast borrowing requirements,
- the current economic and market environment, and
- interest rate forecasts.

- 6.3 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement) was not fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow was used as an interim funding measure. This strategy was prudent as investment returns have remained low and counterparty risk has been minimised. It has also saved a considerable amount of interest payable, known as the 'cost of carry'.

- 6.4 The borrowing position needs to be kept under review to avoid incurring higher borrowing costs in future years when the Council may not be able to avoid new borrowing to finance capital expenditure and/or to refinance maturing debt. The monitoring process includes the setting of various trigger points, the breaking of which will require officer consideration of borrowing requirements and market conditions.

New Loans

- 6.5 All new loans are subject to the relevant gilt yields +0.8% (known as the PWLB certainty rate). A prohibition has been recently introduced to deny access to borrowing from the PWLB for any local authority which has purchase of assets for yield in its three-year capital programme.

- 6.6 The Council's treasury management strategy permits borrowing from various sources, but it has not been previously anticipated that any alternatives to PWLB would need to be utilised, given the current low cost of PWLB funding.

- 6.7 The key advantage of PWLB is the speed and ease of transaction processing and the low fee and administration cost associated with the loans. Alternative types of funding could result in lengthy due diligence, consultancy costs, legal advice and fees and will be far more costly administratively.

- 6.8 In addition, there are also some alternative sources of long-term borrowing. These alternative options for funding to PWLB include:

- **Banks**

Discussions with the Council's treasury consultant suggest that the Council could access borrowing from banks. However the decision by the PWLB to

reverse the 1% additional cost of general fund borrowing has resulted in banks now being placed in an overly competitive environment.

➤ **Pension Fund institutional investors**

Initial indications have suggested that the Council may be able to borrow from institutional investors at rates of around gilt yield plus 1.2% to 1.8% for periods of over 20 years, via a private placement agreement (PPA). Such an arrangement will be subject to extensive negotiations with the lenders, who will need to carry out due diligence on a Council's finances, budgets and balance sheet.

➤ **Bond issuance**

A bond issue would first require the Council to become credit rated by one (or more) of the major ratings agencies: Fitch, S&P or Moody's. This is a complex, lengthy, repetitive and costly process.

The precise rate offered will be market led and dependent on the financial resilience of the authority and the market's perception of creditworthiness.

Councils with significant reserves and a record of not overspending on budget will be able to secure the most advantageous rates. Bond releases typically require a minimum size of at least £200m.

➤ **The Municipal Bonds Agency**

This has been in existence since 2013 but has only recently transacted its first bond issuance and local authority borrower and is not regarded as a major provider.

- 6.9 Alternative opportunities for the Council may well present themselves, and the borrowing strategy will be designed to allow for this. The 'benchmark' for a borrowing opportunity is regarded at around gilts +0.8%. It is unclear at this stage whether feasible PWLB competition will materialise, and it is likely to take some time to do so. Officers will continue to explore alternatives to the PWLB, working with the Council's treasury advisor, Link. PWLB rates will also be kept under regular and active review.
- 6.10 Immediate liquidity needs can be satisfied by borrowing from other local authorities in the short term, consistent with the Council's current approved treasury management strategy. Temporary borrowing rates are likely, however, to remain near Bank Rate and may also prove attractive as part of a balanced debt portfolio.
- 6.11 While the Council will not be able to avoid borrowing to finance new capital expenditure, to replace maturing debt and the rundown of reserves, there will be a "cost of carry", to any new borrowing that will cause a temporary increase in cash balances. Indicative work recently undertaken indicates there may be need to take new long term financing in the financial year 2024/25.

Table 5 The Council's balance sheet position at 31 March 2022

	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
	Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
	£m	£m	£m	£m	£m	£m
Capital Financing Requirement	1,111	1,333	1,585	2,010	2,293	2,350
Other Long Term Liabilities						
PFI	(7)	(6)	(6)	(6)	(6)	(6)
Leases	(44)	(43)	(42)	(42)	(41)	(40)
Under / (over) borrowing	1,060	1,284	1,537	1,962	2,246	2,304
External Borrowing	238	400	587	571	558	549
Under borrowing/ Internal borrowing	822	884	950	1,391	1,688	1,755

Limits on external borrowing

6.12 The Prudential Code requires the Council to set two limits on its total external debt, as set out in Table 6 below. The Authorised Limit has been increased in line with the CFR.

The limits are:

- **Authorised Limit for External Debt (Prudential Indicator 5a)** – This is the limit prescribed by section 3(1) of the Local Government Act 2003 representing the maximum level of borrowing which the Council may incur. It reflects the level of external debt which, while not desired, could be afforded in the short term, but may not be sustainable in the longer term.
- **Operational Boundary (Prudential Indicator 5b)** – This is the limit which external debt is not normally expected to exceed. The boundary is based on current debt plus anticipated net financing need for future years.

Table 6 Overall borrowing limits

2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
Actual	Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
£m	£m	£m	£m	£m	£m	£m
Authorised Limit:						
944 Borrowing and other long term liabilities	1,162	1,382	1,633	2,058	2,340	2,396
Operational Boundary:						
206 Borrowing	238	400	587	571	558	549
17 Other long term liabilities	51	49	48	48	47	46
223 Operational Boundary	289	449	635	619	605	595

6.13 The Executive Director of Finance and Resources reports that the Council complied with these prudential indicators in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans and the proposals in this report.

Maturity structure of borrowing (Prudential Indicator 8)

- 6.14 Managing the maturity profile of debt is essential for reducing the Council's exposure to large fixed rate sums falling due for refinancing within a short period, and thus potentially exposing the Council to additional cost. Table 7 below sets out current upper and lower limits for debt maturity which are unchanged from 2021/22. The principal repayment profile for current council borrowing remains within these limits.

Table 7 Debt maturity profile limits

Actual Maturity at 31 Dec 2021	Duration	Upper Limit	Lower Limit
0	Under 12 Months	40	0
0	12 Months and within 24 Months	35	0
13	24 Months and within 5 Years	35	0
23	5 Years and within 10 Years	50	0
64	10 Years and Above	100	35

Table 8 Maturity profile of long-term borrowing

Borrowing as at 31 December 2021		
Period	General Fund	HRA
	£m	£m
0 - 5 years	0	27
5 - 10 years	0	46
10 - 15 years	0	48
15 - 20 years	0	0
20 - 25 years	15	0
25 - 30 years	0	20
30 - 35 years	0	20
35 - 40 years	0	0
40 - 45 years	10	15
Total	25	176

- 6.15 The Council has £70 million of LOBOs (Lender Option Borrower Option) debt, none of which matures in the near future. Were the lender to exercise their option, the Executive Director of Finance and Resources will consider accepting the new rate of interest or repaying (with no penalty) if it is in the Council's interest. Repayment of the LOBO may result in a need for refinancing.
- 6.16 In the event that there is a much sharper rise in long and short term rates than currently forecast, then the balance of the loan portfolio will be revisited with a view to taking on further longer term fixed rate borrowing in anticipation of future rate rises.

Policy on Borrowing in Advance of Need

- 6.17 The Council has the power to borrow in advance of need in line with its future borrowing requirements under the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended.

- 6.18 Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.
- 6.19 Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

Forward Borrowing

- 6.20 As anticipated in the 2021/22 TMSS, the Council took no additional borrowing for the financial year due to the high level of cash holdings. Officers are monitoring market conditions and reviewing the need to borrow at current low rates if a requirement is identified for either the General Fund or Housing Revenue Account (HRA). The monitoring process includes the setting of various trigger points, the breaking of which will require officer consideration of borrowing requirements and market conditions.
- 6.21 Due to the overall financial position and the underlying need to borrow for capital purposes, it is prudent for the Council to lock in affordability by placing some forward borrowing for the amounts it can be relatively certain it will need, while maintaining some forward flexibility as projects may or may not proceed within the expected timeframes.
- 6.22 During the financial year 2019/20, the Council arranged forward borrowing loans totalling £400m. These loans have enabled the Council to agree competitive rates in advance of need which eliminates the “cost of carry”, i.e., the difference between loan interest cost and the rate of return on cash investments. This also gives some stability and certainty to the financing of the Councils housing development schemes in particular.
- 6.23 An analysis of these loans can be found in the table below.

Counterparty	Amount (£m)	Start Date	Maturity Date	Rate (%)	Profile
Phoenix Group	37.5	15 March 2022	15 March 2062	2.706	Annuity
Barings LLC	150.0	15 August 2022	15 August 2052	1.970	Maturity
Phoenix Group	12.5	15 March 2023	15 March 2063	2.751	Annuity
Rothsay Life Plc	200.0	08 May 2023	08 May 2063	2.887	Equal Instalment of Principal
Weighted average interest rate	400.0			2.579	

Debt Rescheduling

- 6.24 As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the cost of debt repayment (premiums incurred).
- 6.25 The reasons for any rescheduling to take place will include:
- generating cash savings and/or discounted cash flow savings;
 - helping to fulfil the treasury strategy; and
 - enhancing the balance of the portfolio by amending the maturity profile and/or the balance of volatility.

6.26 Consideration will also be given to identifying the potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

Investing Primarily For Yield

6.27 Under the new Public Work Loans Board (PWLB) framework, the Council will need to submit its three-year capital plan to the PWLB and classify under different areas of spend, listed below, with classification the responsibly of the S151 officer. Any monies lent by the PWLB would also need to be classified under the following areas of spend:

- Service spending
- Housing
- Regeneration
- Preventative action
- Treasury Management: refinancing and externalisation of internal borrowing

6.28 Under the PWLB criteria, it is stipulated: “Local authorities must not pursue a deliberate strategy of using private borrowing or internal borrowing to support investment in an asset that the PWLB would not support and then refinancing or externalising this with a PWLB loan.”

6.29 On transacting a PWLB loan, the S151 officer is required to confirm that the local authority is not borrowing in advance of need and does not intend to buy investment assets primarily for yield. When applying for a new PWLB loan, the Council will be asked to confirm that the latest plans submitted remain current and the assurance that they do not intend to buy investment assets primarily for yield remains valid.

6.30 The PWLB guidance defines investment assets bought primarily for yield as:

- buying land or existing buildings to let out at market rate;
- buying land or buildings which were previously operated on a commercial basis which is then continued by the local authority without any additional investment or modification;
- buying land or existing buildings, other than housing, which generate income and are intended to be held indefinitely, rather than until the achievement of some meaningful trigger, such as the completion of land assembly.

7. SECTION 3 – MANAGING CASH BALANCES

The current cash position and cash flow forecast

7.1 Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

7.2 Table 9 below shows that cash balances have increased by £353m since 31 March 2021 to 31 December 2021 which is mainly due to the forecast pattern of the Council's cashflows and is mainly dependant on the timing of precept payments, receipt of grants, council tax and business rates, and progress on the capital expenditure programme. The cash balance would be expected to be closer to £600m by 31 March 2022, but a one-off payment of approximately £292m from the GLA will result in a higher than usual year end balance.

Table 9 Cash position at 31 December 2021

As at 31 March 2021		As at 31 December 2021	
Principal	Average Rate	Principal	Average Rate
£m	%	£m	%
Investments			
315	0.19	668	0.17
	Specified		
18	1.74	18	1.74
	Non-Specified		
333	0.35	686	0.23
	Total		
Borrowing			
136	3.77	131	3.74
	Public Works Loan Board		
70	5.08	70	5.08
	Market Loans		
206	4.22	201	4.21
	Total		

7.3 The medium-term cash flow forecast below demonstrates that the Council currently has a substantial positive cash flow position with the average cash position expected to decrease each subsequent year with a projected requirement to take further financing in 2024/25. Treasury officers will work closely with the capital finance team to monitor slippage within the capital program. Information relating to future business rates and the amounts held pending rating appeals will also be monitored as these are uncertain and will have an impact on the figures detailed below.

Table 10 Medium-term cashflow forecast

	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
	Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
	£m	£m	£m	£m	£m	£m
Balance at 1 April	350	116	61	6	(427)	(719)
Movement in Cash						
Capital Receipt	37	126	128	98	103	145
Grants & Contributions	180	152	156	122	78	69
Cash In	217	278	284	220	181	214
Other Cash movements	(58)	4	4	4	4	4
HRA Cash movements	10	2	6	4	0	0
Capital Programme	(436)	(500)	(536)	(645)	(464)	(271)
Cash Out	(484)	(494)	(526)	(637)	(460)	(267)
Forward Borrowing	38	162	200	0	0	0
Repayment of debt	(5)	(1)	(13)	(16)	(13)	(10)
Balance 31 March	116	61	6	(427)	(719)	(782)
Average Balance	233	89	34	(211)	(573)	(751)

7.4 The Council aims to manage daily cash flow peaks and troughs to achieve a nil current account balance throughout the year. As such the average yearly surplus cash balances should be fully invested throughout. Although the opening balance of £350m on 1 April 2021 is used in table 10, this does not represent the average balance for the month of April 2021 and results in lower balances being reflected in the cashflow forecast. The average investment balance was £497m in April 2021 and £615m for the year to 31st December 2021.

Prospects for investment returns

7.5 Investment returns are expected to increase in 2022/23. However, while markets are pricing in a series of Bank Rate increases, actual economic circumstances may see the MPC fall short of these elevated expectations. As part of the response to the pandemic and lockdown, the Bank of England and the Government have provided financial markets and businesses with plentiful access to credit, either directly or through commercial banks. In addition, the Government has provided large sums of grants to local authorities to help deal with the COVID-19 crisis. This has caused some local authorities to have sudden large increases in cash balances searching for an investment home, some of which was only very short term until those sums were able to be passed on.

7.6 As for Money Market Funds (MMFs), yields have remained low. Some managers resorted to trimming fee levels to ensure that net yields for investors remain in positive territory where possible and practical. Investor cash flow uncertainty, and the need to maintain liquidity in these unprecedented times, has meant there is a surfeit of money available at the very short end of the market.

- 7.7 Inter-local authority lending and borrowing rates have also declined due to the surge in the levels of cash seeking a short-term home at a time when many local authorities are probably having difficulties producing accurate forecasts of when the overpayment of disbursements of funds received will require repayment, or when further large receipts will be received from the Government.

Council policy on investing and managing risk

- 7.8 The aim is to manage risk and reduce the impact of any adverse movement in interest rates on the one hand but, at the same time, not setting the limits to be so restrictive that they impair opportunities to reduce costs or improve performance.

Balancing short and long term investments

- 7.9 Greater returns are usually obtainable by investing for longer periods. While most cash balances are required in order to manage the ups and downs of cash flow where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed. During 2021/22, investments of £18m exceeded 364 days. This means the Council remains well within the upper limit for such investments of £450m.

Table 11 Investment limits

2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
Actual	Forecast	Estimate	Estimate	Estimate	Estimate	Estimate
£m	£m	£m	£m	£m	£m	£m
18 Upper Limit for principal sums invested for more than 364 days	18	450	450	450	450	450

Improving investment returns

- 7.10 An Investment Executive was set up to ensure that the Council made best use of its resources and ensure value for money was being achieved in its overall investment strategy. The task force contains both Council Members and Officers and meets on a half yearly basis. This is the subject of a concurrent report on this agenda.

8. SUMMARY OF PRUDENTIAL INDICATORS (PIs)

- 8.1 The purpose of prudential indicators (PIs) is to provide a reference point or “dashboard” so that senior officers and Members can:
- easily identify whether approved treasury management policies are being applied correctly in practice and,
 - take corrective action as required.
- 8.2 As the Council’s S151 officer, the Executive Director of Finance and Resources has a responsibility to ensure that appropriate PIs are set and monitored and that any breaches are reported to Members.
- 8.3 The Executive Director of Finance and Resources has confirmed that the PIs set out below are all expected to be complied with in 2021/22 and does not envisage at this stage that there will be any difficulty in achieving compliance with the suggested indicators for 2022/23.

PI Ref	Paragraph Reference		2020/21 Actual	2021/22 Forecast	2022/23 Proposed
1	5.1	Capital expenditure	£275m	£436m	£500m
2	5.8	Capital Financing Requirement (CFR)	£892m	£1,111m	£1,333m
3	5.12	Net debt vs CFR	£686m underborrowing	£873m underborrowing	£933m underborrowing
4	5.13	Ratio of financing costs to revenue stream	GF (3.60)% HRA 46.91%	GF (10.33)% HRA 45.15%	GF (11.67)% HRA 44.98%
5a	6.12	Authorised limit for external debt	£944m	£1,162m	£1,382m
5b	6.12	Operational debt boundary	£223m	£289m	£449m
6	7.3	Working Capital Balance	£0m	£0m	£0m
7	7.90	Limit on surplus funds invested for more than 364 days (i.e. non specified investments)	£18m	£18m	£450m
8	6.14	Maturity structure of borrowing	Upper limit under 12 months: 40% Actual: 3% Lower limit 10 years and above: 35% Actual: 67%	Upper limit under 12 months: 40% Forecast: 0% Lower limit 10 years and above: 35% Forecast: 64%	Upper limit under 12 months: 40% Lower limit 10 years and above: 35%

9. LEGAL IMPLICATIONS

- 9.1 The Local Government Act 2003 provides that a local authority has the power both to borrow and invest money for any purpose relevant to its functions and for the prudent management of its financial affairs. The Act requires the Council to determine and to keep under review how much money it can afford to borrow. The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, provide that, in complying with this duty, the Council must have regard to the Prudential Code for Capital Finance in Local Authorities published by CIPFA. The Council is also required to have regard to the CIPFA Treasury Management Code of Practice.
- 9.2 The current CIPFA Treasury Management Code of Practice 2017 and the Secretary of State's Investment Code both require the Section 151 officer (Executive Director) to present an Annual Treasury Management Strategy Statement, which includes an Annual Investment Strategy, for the forthcoming year for approval by the Full Council before the beginning of each financial year.
- 9.3 The revised CIPFA Prudential Code for Capital Finance in Local Authorities sets out various indicators that are to be used to support capital expenditure plans and treasury management decisions. The prudential and treasury indicators have to be set by the Full Council when the budget is set and are monitored during the year. The prudential indicators are included in section 8 of this report.
- 9.4 The Council is also required to approve a Treasury Management Strategy Statement setting out the overarching framework for treasury management services within the Council. This statement is set out in sections 5-7 of this report.

10. APPENDICES

- 1 Annual Investment Strategy
- 2 Minimum Revenue Provision (MRP) Policy
- 3 CIPFA Requirements
- 4 Prospects for Interest Rates and Economic Update

BACKGROUND PAPERS

Treasury Management Strategy Statement 2021/22 (Approved by Council March 2021)

1. Section 3 Local Government Act 2003
2. Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended
3. DLUHC Guidance on Minimum Revenue Provision (fourth edition) February 2018
4. DLUHC Capital Finance Guidance on Local Government Investments February 2018
5. CIPFA Prudential Code for Capital Finance in Local Authorities, 2017
6. CIPFA Treasury Management Code of Practice, 2017
7. CIPFA Treasury Management Guidance Notes, 2018

If you have any queries about this Report or wish to inspect any of the Background Papers, please contact:

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ANNUAL INVESTMENT STRATEGY

1. The Council holds significant invested funds, representing income received in advance of expenditure, balances and reserves. During the first half of the current year, the Council's average investment balance has been around £580m and the cash flow projections show this pattern is expected to increase in the forthcoming year. Investments are made with reference to the core balance, future cash flow requirements and the outlook for interest rates.
2. The Council's investment policy has regard to the DLUHC's Guidance on Local Government Investments ("the Investment Guidance") and the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second, then followed by yield.
3. In accordance with the above guidance and to minimise the risk to investments, the Council applies minimum acceptable credit criteria to generate a list of highly creditworthy counterparties which will provide security of investments, enable diversification and minimise risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

Investment returns expectations

4. It is not expected that Bank Rate will go up fast after the initial rate rise in December 2021 as the supply potential of the economy is not likely to have taken a major hit during the pandemic: it should, therefore, be able to cope well with meeting demand after supply shortages subside over the next year, without causing inflation to remain elevated in the medium term, or to inhibit inflation from falling back towards the MPC's 2% target after the spike up to around 5%. The forecast includes four increases in Bank Rate over the three-year forecast period to March 2025, ending at 1.25%.
5. It should also be borne in mind that Bank Rate being cut to 0.25% and then to 0.10% in early 2020 were emergency measures to deal with the Covid crisis hitting the UK. At any time, the MPC could decide to simply take away such emergency cuts on no other grounds that they are no longer warranted, and as a step forward in the return to normalisation. In addition, any Bank Rate under 1.00% is both highly unusual and highly supportive of economic growth.
6. The suggested budgeted investment earnings rates for returns on investments placed for periods up to approximately three months during each financial year, (based on a first increase in Bank Rate in quarter 2 of 2022) are as follows:

Average earnings in each year	
2022/23	0.50%
2023/24	0.75%
2024/25	1.00%
2025/26	1.25%
Long term later years	2.00%

Investment time limits

7. This limit is set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment. For the year 2022/23, the proposed limit of investments for over 364 days is £450m as set out in table 11 of the TMSS.

Investment policy

8. The Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to assess continually and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.
9. Other information sources used will include the financial press, share prices and other such information pertaining to the banking sector to establish the most robust scrutiny process on the suitability of potential investment counterparties.

Creditworthiness policy

10. The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration.

After this main principle, the Council will ensure that:

- it maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security and monitoring their security. This is set out in the specified and non-specified investment sections below; and
 - it has sufficient liquidity in its investments. For this purpose, it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.
11. The Executive Director of Finance and Resources will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to those which determine which types of investment instrument are either specified or non-specified as they provide an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.
 12. Credit rating information is supplied by Link Asset Services, the Council's treasury advisors. Any counterparty failing to meet the criteria would be omitted from the counterparty list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of the longer-term bias outside the central rating view) are provided to officers almost immediately after they occur and this information is considered before dealing.
 13. The Council takes into account the following relevant matters when proposing counterparties:
 - the financial position and jurisdiction of the institution;
 - the market pricing of credit default swaps for the institution;
 - any implicit or explicit Government support for the institution;
 - Standard & Poor's, Moody's and Fitch's short and long term credit ratings;

- sovereign ratings to select counterparties from only the most creditworthy countries; and
 - core Tier 1 capital ratios.
14. Changes to the credit rating will be monitored and, in the event, that a counterparty is downgraded and does not meet the minimum criteria specified in Appendix 1, the following action will be taken immediately:
- no new investments will be made;
 - existing investments will be recalled if there are no penalties; and
 - full consideration will be given to recall or sale of existing investments which would be liable to penalty clause.
15. Significant levels of downgrades to Short and Long-Term credit ratings have not materialised since the start of the pandemic crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. However, as economies are beginning to reopen, there have been some instances of previous lowering of Outlooks being reversed.

Specified and non-specified investments

16. The DLUHC Guidance on Local Government Investments made under section 15(1) of the Local Government Act 2003, places restrictions on local authorities around the use of specified and non-specified investments.

A specified investment is defined as an investment which satisfies all of the conditions below:

- the investment and any associated cash flows are denominated in sterling;
 - the investment has a maximum maturity of one year;
 - the investment is not defined as capital expenditure; and
 - the investment is made with a body or in an investment scheme of high credit quality; or with the UK Government, a UK Local Authority or parish/community council.
17. **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use. In addition to the long-term investments listed in the table at the end of Appendix 1, the following non-specified investments that the Council may make include:
- **Green Energy Bonds:** investments in solar farms are a form of Green Energy Bonds that provide a secure enhanced yield. The investments are structured as unrated bonds and secured on the assets and contracts of solar and wind farms. Before proceeding with any such investment, internal and external due diligence will be undertaken in advance of investments covering the financial, planning and legal aspects.

- **Social Housing Bonds:** various fund managers facilitate the raising of financing housing associations via bond issues. The investment is therefore asset backed and provides enhanced returns. Officers will need to undertake due diligence on each potential investment in order to understand the risks and likelihood of default.
- **Asset Backed Securities (ABS) / Residential Mortgage backed securities (RMBS)** – as these securities by their nature are asset backed they are regarded as low risk should a default take place, but have a higher return. These are available for direct investment, or as pooled / segregated assets managed by a third party fund manager. In the event of a fund manager option being selected, this would need to be procured through a proper procurement process.
- **Loans:** the Council will allow loans (as a form of investment) to be made to organisations delivering services for the Council where this will lead to the enhancement of services to Westminster Stakeholders. The Council will undertake due diligence checks to confirm the borrower’s creditworthiness before any sums are advanced and will obtain appropriate levels of security or third party guarantees for loans advanced. The Council would expect a return commensurate with the type, risk and duration of the loan. A limit of £50 million for this type of investment is proposed with a duration commensurate with the life of the asset and Council’s cash flow requirements. All loans will need to be in line with the Council’s Scheme of Delegation and Key Decision thresholds levels.
- **Shareholdings in limited companies and joint ventures:** the Council invests in three forms of company:
 - Small scale businesses funded through the Civic Enterprise Fund aimed at promoting economic growth in the area. Individual investments are no more than £0.5m and the aim is for the Fund to be self-financing over the medium-term.
 - Trading vehicles which the Council has set up to undertake particular functions. These are not held primarily as investments but to fulfil Council service objectives. Any new proposals will be subject to due diligence as part of the initial business case. As these are not to be held primarily as investment vehicles, then there is an expectation that they will break even.
 - Trading vehicles held for a commercial purpose where the Council is obliged to undertake transactions via a company vehicle. These will be wholly owned subsidiaries of the Council with the aim of diversifying the investment portfolio risk.
 - Westminster Housing Investment Ltd

18. For any such investments, specific proposals will be considered by the Tri-Borough Director of Treasury and Pensions, and approved by the S151 Officer after taking into account:

- cash flow requirements
- investment period
- expected return

- the general outlook for short to medium term interest rates
- creditworthiness of the proposed investment counterparty
- other investment risks.

19. The value of non-specified investments will not exceed their investment allocation. The Council must now formulate a strategy that allocates its cash in the most effective manner to short, medium and long term non-specified investments.

Country of domicile

20. The current TMSS allows deposits/ investments with financial entities domiciled in the following countries: Australia, Canada, Denmark, Finland, France, Germany, Luxembourg, Netherlands, Norway, Singapore, Sweden, Switzerland, UK and USA. This list will be kept under review and any proposed changes to the policy reported to the next meeting.

Schedule of investments

21. The criteria for providing a pool of high quality short, medium and long-term, cash-based investment counterparties along with the time and monetary limits for institutions on the Council's counterparty list are in the table below:
22. Officers will monitor the impact of the UK's exit from the European Union on the names within the Council's counterparty list.

All investments listed below must be sterling denominated

Investments	Minimum Credit Rating Required (S&P/Moody's/Fitch)	Maximum Individual Counterparty Investment Limit (£m)	Maximum tenor
DMO Deposits	Government Backed	Unlimited	6 months
UK Government (Gilts/T-Bills/Repos)	Government Backed	Unlimited	Unlimited
Supra-national Banks, European Agencies	LT: AA/Aa/AA	£200m	5 years
Covered Bonds	LT: AA/Aa/AA	£300m	10 years
Network Rail	Government guarantee	Unlimited	Oct 2052
TFL	LT: AA/Aa/AA	£100m	5 years
Greater London Authority (GLA)	N/A	GLA: £100m	5 years
UK Local Authorities (LA)		LA: £100m per LA, per criteria £500m in aggregate	3 years
Local Government Association (LGA)		LGA: £20m	15 years
Commercial Paper issued by UK and European Corporates	ST: A-1/P-1/F-1	£40m per name, £200m in aggregate	6 months
Money Market Funds (MMF)	LT: AAA/Aaa/AAA By at least two of the main credit agencies	£70m per Fund Manager, £300m in aggregate	3 day notice
Ultra Short Dated Bond Funds (USDBFs)	Due Diligence	£25m per fund manager £75m in aggregate	Up to 7 day notice
Collateralised Deposits	Collateralised against loan	£100m	50 years
Social Housing Bonds	Due Diligence	£200m	10 years
Pooled Property Funds	Due Diligence	£200m	10 years
Asset backed securities (ABS) and Residential mortgage backed securities (RMBS)	Asset Backed / Due Diligence	£200m	10 years
UK Bank (Deposit or Certificates of Deposit)	LT: AA-/Aa3/AA- ST: F1+	£75m	5 years
	LT: A-/A3/A ST: F1	£50m	3 years
Non-UK Bank (Deposit or Certificates of Deposit)	LT: AA-/Aa2/AA- ST: F1+	£50m	5 years
	LT: A/A2/A ST: F1	£35m	3 years
Green Energy Bonds	Internal and External due diligence	Less than 25% of the total project investment or maximum £20m per bond. £50m in aggregate	10 years
Rated UK Building Societies	LT: A-/A3/A ST: F1	£10m per Building Society, £50m in aggregate	1 year
Loans to organisations delivering services for the Council	Due diligence	£50m in aggregate	Over the life of the asset
Government Bonds - regulated investment vehicle	AAA/AA only	£50m	Daily pricing
Sovereign approved list (AA- rated and above): Australia, Canada, Denmark, Finland, France, Germany, Luxembourg, Netherlands, Norway, Singapore, Sweden, Switzerland, UK and USA			

Rationale for investment limits

Debt Management Office (DMO): Unlimited. The DMO is an executive agency of Her Majesty's Treasury. Being fully UK government backed, the DMO is the ultimate low risk depositary. Being ultra-low risk, the investment return is very low.

UK Government Gilts/T-Bills/Repos: Unlimited. UK Government gilts are regarded by the market as high quality and ultra-low risk. Being ultra-low risk, the investment return is low.

Supranational Banks, European Agencies: £200m limit. A supra-national bank is a financial institution, such as the European Investment Bank or the World Bank, whose equity is owned by sovereign states. Being owned by overseas states, they are regarded as being low risk, but not in the same safe risk category as UK. The investment return is low.

Covered Bonds: £300m limit. Covered bonds are debt securities issued by a bank or mortgage institution and collateralised against a pool of assets that, in case of failure of the issuer, can cover claims at any point of time. They are subject to specific legislation to protect bond holders. With slightly more risk, the investment return is higher than UK Gilts.

Network Rail: Unlimited. Network Rail is the owner and infrastructure manager of most of the rail network in England, Scotland and Wales. Having a UK government guarantee, they are regarded as being reasonably low risk with a lower investment return.

Transport for London (TfL): £100m limit. Transport for London is a local government body responsible for the transport system in Greater London. Its parent organisation is the Greater London Authority (GLA). Being a GLA owned entity, the investment is regarded as safe and the return is low.

Greater London Authority (GLA): £100m limit. The Greater London Authority is the top-tier administrative body for Greater London, consisting of a directly elected executive Mayor of London and an elected 25-member London Assembly. Being categorised alongside UK local authorities, the investment is regarded as safe and the return is low.

UK Local Authorities: £100 limit per authority, £500m in total. Local authorities have always been regarded as safe counterparties. As an additional safeguard, each new local authority counterparty will be subject to due diligence checks regarding latest accounts, external audit opinion, financial budget projections and financial reputation. There are 326 billing authorities with tax-raising powers in England, consisting of 201 non-metropolitan district councils, 55 unitary authority councils, 36 metropolitan borough councils, 32 London borough councils, the City of London Corporation and the Council of the Isles of Scilly. Additionally, there are levying authorities, consisting of 45 police authorities, 52 fire authorities and six waste disposal authorities. UK local authorities and levying authorities are regarded as safe and the return is relatively low.

Local Government Association: £20m limit. The Local Government Association (LGA) is a charitable organisation, funded largely from subscriptions, which comprises local authorities in England and Wales, representing the interests of local government to national government. Its core membership comprises 335 councils. Despite being an entity which represents local authorities, this entity is not regarded as risk free as local authorities and therefore the limit is lower at £20m.

Commercial Paper issued by the UK and European Corporates: £40m per name, £200m in total. Commercial paper is an unsecured, short-term debt instrument issued by a corporation, typically for the financing of accounts receivable, inventories and meeting short-term liabilities. Investment is confined to high quality investment grade corporates. The risk and investment return are higher than the sovereign categories.

Money Market Funds (MMF): £70m per manager, £300m in total. Money market funds are open-ended funds that invests in short-term high quality debt securities such as Treasury bills and commercial paper.

Ultra short dated bond funds (USDBFs): £25m per manager, £75m in total. Enhanced money market funds increase returns via increasing interest rate, credit and liquidity risk in order to enhance the return. Being well diversified reduces the impact of a single default within the portfolio.

Collateralised Deposits: £100m limit. In lending agreements, collateral is a borrower's pledge of specific property to a lender to secure repayment of a loan, serving as a lender's protection against a borrower's default. Being asset backed, they are regarded as being reasonably low risk should a default take place, but with a higher return.

Social Housing Bonds: £200m limit. Housing associations are increasingly issuing public bonds, secured against social housing assets, to meet financing requirements. This category is greater risk and will provide an enhanced return.

Pooled Property Funds: £200m limit. These are investment vehicles such as mutual funds, commingled funds, group trusts, real estate funds, limited partnership funds, and alternative investments. The distinguishing feature of a pooled fund is that a number of investors contribute money to the fund.

Residential Mortgage Backed Securities (RMBS): £200m limit. A residential mortgage backed security is a pool of mortgage loans created by banks and other financial institutions. The cash flows from each of the pooled mortgages is packaged by a special-purpose entity into classes and tranches, which then issues securities and can be purchased by investors. Being asset backed, they are regarded as being reasonably low risk should a default take place, but with a higher return.

UK Bank Deposits: £75m or £50m per bank. Banks have become a riskier counterparty since the bail outs of Lloyds and RBS. The Financial Services (Banking Reform) Act 2013 confers on the Bank of England a bail-in stabilisation option for the resolution for banks and building societies, ensuring that shareholders and creditors/depositors of the failed institution, rather than the taxpayer, meet the costs of the failure. Despite the bail-in risk, the return on UK bank deposits is relatively low.

Non-UK Bank Deposits: £50m or £35m (Sterling deposits only) per bank. Overseas banks incorporated in the UK provide a number of options for high quality institutions with returns largely similar to UK banks.

Green Energy Bonds: £20m per bond, £50m limit (subject to due diligence). This comprises of finance for the supply of electricity from renewable energy sources, particularly in areas such as energy storage and electric vehicle networks. This category is greater risk and will provide an enhanced return. Use should be made of regulated markets where available in order to provide additional investment security and risk reduction.

Rated Building Societies: £10m per building society, £50m limit. Same rationale as UK banks, see above.

Loans to organisations delivering services to the Council: £50m limit. Assessed individually and subject to due diligence. At markets rates of interest and reflecting the risk of the borrower, this will offer an enhanced rate of return.

UK Government Bonds (Regulated Investment Vehicle): £50m limit. The Fund takes a specialised investment approach to fixed income investments, seeking to generate returns from high quality government bonds and related derivatives that are largely independent of the level of bond yields, changes in interest rates and wider market fluctuations. The strategy aims to generate returns by exploiting mispricing occurring when very closely related securities are priced inconsistently with each other.

Minimum Revenue Provision (MRP) Policy

- Capital expenditure is generally defined as expenditure on assets that have a life expectancy of more than one year. The accounting approach is to spread the cost over the estimated useful life of the asset. The mechanism for spreading these costs is through an annual MRP. The MRP is the means by which capital expenditure, which is financed by borrowing or credit arrangements, is funded by Council Tax.
- Regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended (Statutory Instrument (SI) 3146/2003) requires full Council to approve a Minimum Revenue Provision (MRP) Statement setting out the policy for making MRP and the amount of MRP to be calculated which the Council considers to be prudent. In setting a level which the Council considers to be prudent, the Guidance states that the broad aim is to ensure that debt is repaid over a period reasonably commensurate with that over which the capital expenditure provides benefits to the Council.
- The Council is recommended to approve the following MRP Statement:
 - For capital expenditure incurred before 1 April 2007, MRP will be calculated using Option 1 (the 'Regulatory Method') of the CLG Guidance on MRP. Under this option MRP will be 4% of the closing non-HRA CFR for the preceding financial year.
 - For all capital expenditure incurred after 1 April 2007 financed from unsupported (prudential) borrowing (including PFI and finance leases), MRP will be based upon the asset life method under Option 3 of the DCLG Guidance.
 - In some cases, where a scheme is financed by prudential borrowing it may be appropriate to vary the profile of the MRP charge to reflect the future income streams associated with the asset, whilst retaining the principle that the full amount of borrowing will be charged as MRP over the asset's estimated useful life.
 - The Council reserves the right to adopt an annuity MRP structure where appropriate to match an assets cash flows.
 - A voluntary MRP may be made from either revenue or voluntarily set aside capital receipts.
 - Estimated life periods and amortisation methodologies will be determined under delegated powers. To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the guidance, these periods will generally be adopted by the Council. However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate.
 - As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

- Charges included in annual PFI or finance leases to write down the balance sheet liability shall be applied as MRP.
- Where borrowing is undertaken for the construction of new assets, MRP will only become chargeable once such assets are completed and operational.
- If property investments are short-term (i.e. no more than 4 years) and for capital appreciation, the Council will not charge MRP as these will be funded by the capital receipt on disposal
- There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made. For the Council this is componentised based on the life of component and the gross replacement cost within the overall existing use value – social housing of the HRA stock.
- For commercial properties, MRP is charged on a hurdle rate basis to ensure that the Council's investment return is sufficient to meet MRP and associated borrowing costs.

CIPFA Requirements

The Council has formally adopted CIPFA's Code of Practice on Treasury Management (updated 2017) and complies with the requirements of the Code as detailed in this appendix. There are no changes to the requirements formally adopted in the 2017 update with regard to reporting, these are listed below:

- Maintaining a Treasury Management Policy Statement setting out the policies and objectives of the Council's treasury management activities.
- Maintaining a statement of Treasury Management Practices that sets out the manner in which the Council will seek to achieve these policies and objectives.
- Presenting the Full Council with an annual TMSS statement, including an annual investment strategy and Minimum Revenue Provision policy for the year ahead (this report), a half year review report and an annual report (stewardship report) covering compliance during the previous year.
- A statement of delegation for treasury management functions and for the execution and administration of statement treasury management decisions. (see below)
- Delegation of the role of scrutiny of treasury management activities and reports to a specific named body. At Westminster City Council this role is undertaken by the Audit and Performance Committee

Treasury Management Delegations and Responsibilities

The respective roles of the Council, Cabinet, Audit and Performance Committee and Section 151 officer are summarised below. Further details are set out in the Treasury Management Practices.

Council

Council will approve the annual treasury strategy, including borrowing and investment strategies. In doing so Council will establish and communicate their appetite for risk within treasury management having regard to the Prudential Code.

Cabinet

Cabinet will recommend to Council the annual treasury strategy, including borrowing and investment strategies and receive a half-year report and annual out-turn report on treasury activities.

Cabinet also approves revenue budgets, including those for treasury activities.

Audit and Performance Committee

This committee is responsible for ensuring effective scrutiny of the Treasury strategy and policies.

Section 151 Officer

Council has delegated responsibility for the implementation and monitoring of treasury management decisions to the Section 151 Officer to act in accordance with approved policy and practices. The s151 Officer has full delegated powers from the Council and is responsible for the following activities:

- investment management arrangements and strategy;
- borrowing and debt strategy;
- monitoring investment activity and performance;
- overseeing administrative activities;
- ensuring compliance with relevant laws and regulations;
- provision of guidance to officers and members in exercising delegated powers.

Tri-Borough Director of Treasury and Pensions

Has responsibility for the execution and administration of treasury management decisions, acting in accordance with the Council's Treasury Policy Statement and CIPFA's 'Standard of Professional Practice on Treasury Management'.

Treasury Team

Undertakes day to day treasury investment and borrowing activity in accordance with strategy, policy, practices and procedures.

Training

The CIPFA code requires the s151 officer to ensure that Members with responsibility for making treasury management decisions and for scrutinising treasury functions receive adequate training. The training needs of all officers are reviewed periodically as part of the Learning and Development programme. Officers attend various seminars, training sessions and conferences during the year and appropriate Member training is offered as and when is needed, and suitable opportunities, are identified.

Prospects for Interest Rates

- The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Link provided the following forecasts on 20 December 2021. These are forecasts for certainty rates, gilt yields plus 80 bps.

Link Group Interest Rate View 20.12.21														
	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
BANK RATE	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25
3 month ave earnings	0.20	0.30	0.50	0.50	0.60	0.70	0.80	0.90	0.90	1.00	1.00	1.00	1.00	1.00
6 month ave earnings	0.40	0.50	0.60	0.60	0.70	0.80	0.90	1.00	1.00	1.10	1.10	1.10	1.10	1.10
12 month ave earnings	0.70	0.70	0.70	0.70	0.80	0.90	1.00	1.10	1.10	1.20	1.20	1.20	1.20	1.20
5 yr PWLB	1.40	1.50	1.50	1.60	1.60	1.70	1.80	1.80	1.80	1.90	1.90	1.90	2.00	2.00
10 yr PWLB	1.60	1.70	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10	2.20	2.30
25 yr PWLB	1.80	1.90	2.00	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.40	2.40	2.50	2.50
50 yr PWLB	1.50	1.70	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.20	2.20	2.30	2.30

- Over the last two years, the coronavirus outbreak has caused significant economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left the Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16 December 2021.
- As shown in the forecast table above, the forecast for Bank Rate now includes four increases, an actual increase December 2021 to 0.25%, then Q2 2022 to 0.50%, Q1 2023 to 0.75%, Q1 2024 to 1.00% and, finally, in Q1 2025 to 1.25%.
- Gilt yields / PWLB rates.** Since the start of 2021, there has been much volatility in gilt yields, and hence PWLB rates. As the interest forecast table for PWLB Certainty Rates above shows, there is forecast to be a steady, but slow, rise in both the Bank Rate and gilt yields during the forecast period to March 2025, though there will doubtless be a lot of unpredictable volatility during this forecast period.
- While monetary policy in the UK will have a major impact on gilt yields, there is also a need to consider the potential impact that rising treasury yields in America could have on UK gilt yields. As an average since 2011, there has been a 75% correlation between movements in US ten-year treasury yields and UK ten-year gilt yields. This is a significant upward risk exposure to the forecasts for longer term PWLB rates. However, gilt yields and treasury yields do not always move in unison.

Economic Update

- Covid 19 Vaccines.** These are regarded as the game changer during 2021 which raised high hopes that life in the UK would be able to largely return to normal in the second half of the year. However, the arrival of the Omicron mutation at the end of November 2021 rendered the initial two doses of all vaccines largely ineffective in preventing reinfection. This has dashed such hopes and raises the spectre again that a fourth wave of the virus could overwhelm hospitals in early 2022. Rather than go for full lockdowns which heavily damage the economy, the government strategy this time is focusing on getting as many people as possible to have a third (booster) vaccination after three months from the previous last injection.

7. With the household saving rate having been exceptionally high since the first lockdown in March 2020, there is considerable pent-up demand and purchasing power for services in sectors like restaurants, travel, tourism and hotels which had been hit hard during 2021, but could now be hit hard again by either, or both, of government restrictions and/or consumer reluctance to leave home. The economy, therefore, faces significant headwinds although some sectors have learned how to cope well with Covid.
8. **A summary overview of the future path of bank rate.**
- In December 2021, the Bank of England became the first major western central bank to put interest rates up in this upswing in the current business cycle in western economies as recovery progresses from the Covid recession of 2020.
 - The next increase in Bank Rate could be in February 2022 to May 2022, dependent on how severe an impact there is from Omicron.
 - With inflation expected to peak at around 6% in April 2022, the MPC may want to be seen to be active in taking action to counter inflation on 5 May 2022, the release date for its Quarterly Monetary Policy Report.
 - The December 2021 MPC meeting was more concerned with combating inflation over the medium term than supporting economic growth in the short term.
 - The Bank Rate increases beyond May 2022 are difficult to forecast as inflation could drop in the second half of 2022.
 - However, the MPC will want to normalise the Bank Rate over the next three years so that it has its main monetary policy tool ready to use in time for the next downturn: all rates under 2% are providing stimulus to economic growth.
 - Year end 0.25% increases into Q1 of each financial year from 2023 have been assumed to recognise this upward bias in the Bank Rate, but the actual timing in each year is difficult to predict.
 - Covid remains a major potential downside threat in all three years as there could be further mutations.
 - Purchases of gilts under QE ended in December 2021. Note that when the Bank Rate reaches 0.50%, the MPC has said it will start running down its stock of QE.
9. **MPC Meeting 16 December 2021.** The Monetary Policy Committee (MPC) voted 8-1 to raise the Bank Rate from 0.10% to 0.25% and unanimously decided to make no changes to its programme of quantitative easing purchases due to finish in December 2021 at a total of £895bn.
10. The MPC disappointed financial markets by not raising the Bank Rate at its November 2021 meeting. Most forecasters had viewed a Bank Rate increase as being near certain at this December meeting due to the way that inflationary pressures have been comprehensively building in both producer and consumer prices, and in wage rates. The decision taken was to wait until statistics were available to show how the economy had fared at this time.

11. On 15 December 2021, the CPI inflation figure for November 2021 spiked up further from 4.2% to 5.1%, confirming again how inflationary pressures have been building sharply. However, Omicron also caused a sharp fall in world oil and other commodity prices (gas and electricity inflation has generally accounted on average for about 60% of the increase in inflation in advanced western economies).
12. Other elements of inflation are also transitory, e.g., prices of goods being forced up by supply shortages, and shortages of shipping containers due to ports being clogged have caused huge increases in shipping costs. But these issues are likely to clear during 2022, and then prices will subside back to more normal levels. Gas prices and electricity prices should also fall back once winter is passed and demand for energy reduces.
13. Although it is possible that the Government could step in with some fiscal support for the economy, the huge cost of such support to date is likely to pose a barrier to incurring further major economy wide expenditure, unless it is very limited and targeted on narrow sectors like hospitality (as announced just before Christmas). The Government may well, therefore, effectively leave it to the MPC, and to monetary policy, to support economic growth, but at a time when the threat posed by rising inflation is near to peaking.
14. This is an adverse set of factors against which the MPC had to decide on Bank Rate. The MPC is now concerned that inflationary pressures are building and need concerted action by the MPC to counter. The 8-1 vote to raise the rate shows that there is firm agreement that inflation now poses a threat, especially after the CPI figure announced for November 2021. The MPC commented that there were some signs of greater persistence in domestic costs and price pressures.
15. These comments indicate that there has been a material reappraisal by the MPC of the inflationary pressures since their last meeting and the Bank also increased its forecast for inflation to peak at 6% in April 2022, rather than at 5%. However, as the Bank retained its guidance that only a “modest tightening” in policy will be required, the increases are not likely to be much more.
16. The MPC’s forward guidance on its intended monetary policy on raising Bank Rate versus selling (quantitative easing) holdings of bonds is as follows:
 - Raising Bank Rate as “the active instrument in most circumstances”.
 - Raising Bank Rate to 0.50% before starting on reducing its holdings.
 - Once Bank Rate is at 0.50% it would stop reinvesting maturing gilts.
 - Once Bank Rate had risen to at least 1%, it would start selling its holdings.
17. United States of America: inflation hitting 6.8% and the feed through into second round effects, meant that it was near certain that the Federal Reserve’s meeting of 15 December 2021 would take aggressive action against inflation. Federal reserve officials also expected three rate rises in 2022 of 0.25% from near zero currently, followed by three in 2023 and two in 2024, taking rates back above 2% to a neutral level for monetary policy. The first increase could come as soon as March 2022 as the Federal Reserve chairman stated his view that the economy had made rapid progress to achieving the other goal: maximum employment.

18. European Union: the slow roll out of Covid vaccines initially delayed economic recovery in early 2021 but the vaccination rate then picked up sharply. After a contraction of -0.3% in Q1, Q2 showed strong growth of 2.0%. With Q3 at 2.2%, the EU recovery was then within 0.5% of its pre Covid size. The arrival of Omicron is now a major headwind to growth in Q4 and the expected downturn into weak growth could well turn negative, with the outlook for the first two months of 2022 expected to continue to be very weak.
19. Headline inflation reached 4.9% in November 2021, with over half of that due to energy. However, oil and gas prices are expected to fall after the winter and so energy inflation is expected to fall in 2022. The Eurozone is set for a prolonged period of inflation being above the ECB's target of 2% and it is likely to average 3% in 2022, in line with the ECB's latest projection.
20. The EU has entered into a period of political uncertainty where a new German government formed of a coalition of three parties with Olaf Scholz replacing Angela Merkel as Chancellor in December 2021, will need to find its feet both within the EU and in the three parties successfully working together. In France there is a presidential election coming up in April 2022 followed by the legislative election in June 2022. Political uncertainties could have repercussions on economies and on Brexit issues.
21. **World Growth.** World growth was in recession in 2020 but recovered during 2021 until starting to lose momentum in the second half of the year, though overall growth for the year is expected to be about 6% and to be around 4 to 5% in 2022. Inflation has been rising due to increases in gas and electricity prices, shipping costs and supply shortages, although these should subside during 2022. While headline inflation will fall sharply, core inflation will probably not fall as quickly as central bankers would hope.