WIRRAL

POLICY AND RESOURCES COMMITTEE

Wednesday, 17 February 2021

REPORT TITLE:	TREASURY MANAGEMENT STRATEGY 2021/22
REPORT OF:	DIRECTOR OF RESOURCES

REPORT SUMMARY

The Authority's treasury management activity is underpinned by CIPFA's 2017 Code of Practice on Treasury Management ("the Code"), which requires the production of annual Treasury Management Indicators and a Treasury Management Strategy Statement on likely financing and investment activity. The Code also recommends that Members are informed of treasury management activities at least twice a year.

This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code. It does not cover the requirements of the 2018 Ministry for Housing, Communities and Local Government (MHCLG) Investment Guidance, which mostly refers to non-treasury investments and is the subject of a separate report.

This matter affects all Wards within the Borough.

The decisions in this report are key decisions.

RECOMMENDATIONS

The Policy & Resources Committee are requested to: -

1. Recommend to the Council the approval of the Treasury Management and Investment Strategy for 2021/2022.

2. Recommend to the Council the approval of the Treasury Management Indicators.

SUPPORTING INFORMATION

1.0 REASON/S FOR RECOMMENDATION/S

1.1 The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") requires local authorities to determine the Treasury Management Strategy Statement (TMSS) on an annual basis. The TMSS no longer incorporates the Investment Strategy as required under the MHCLG's Investment Guidance, which mostly refers to non-treasury investments.

2.0 OTHER OPTIONS CONSIDERED

2.1 CIPFA's 2017 Code of Practice on Treasury Management requires the production of annual Treasury Management Indicators and a Treasury Management Strategy Statement on likely financing and investment activity. The accompanying 2021/26 Capital Programme impacts on the levels of borrowing being forecast within this report. An annual strategy is standard practice, but should it become appropriate to amend any key elements of this strategy during the period covered, a revised report will be produced.

3.0 BACKGROUND INFORMATION

3.1 Treasury risk management at the Authority is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code) which requires the Authority to approve a treasury management strategy before the start of each financial year.

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

3.3 This report fulfils the Authority's legal obligation under the Local government Act 2003 to have regard to the CIPFA Code.

3.4 Wirral Council defines its treasury management activities as:

"the management of the organisation'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."

3.5 The Council will create and maintain, as the cornerstones for effective treasury management:

- A Treasury Management Policy Statement (see Appendix 1, stating the policies, objectives and approach to risk management of its treasury management activities.
- Suitable Treasury Management Practices (TMPs), setting out the manner in which the organisation will seek to achieve those policies

and objectives, and prescribing how it will manage and control those activities.

3.6 Treasury Management is about the management of risk. The Council is responsible for its treasury decisions and activity. No treasury management activity is without risk.

3.7 As per the requirements of the Prudential Code, the Authority has adopted the CIPFA Treasury Management Code of Practice. All treasury activity will comply with relevant statute, guidance and accounting standards.

3.8 Adoption of this Treasury Management Strategy Statement approves the following:

- Treasury Management Strategy for 2021/22.
- Treasury Management Policy Statement
- Treasury Management Indicators for 2021/22.

3.9 The Authority will be asked to approve a revised Treasury Management Strategy Statement should the assumptions on which this report is based change significantly. Such circumstances would include, for example, a large, unexpected change in interest rates, or in the level of its investment balance.

ECONOMIC BACKGROUND

3.10 **The Economy:** The impact on the UK from coronavirus, lockdown measures, the rollout of vaccines, as well as the new trading arrangements with the European Union (EU), will remain major influences on the Authority's treasury management strategy for 2021/22.

3.11 The Bank of England (BoE) maintained Bank Rate at 0.10% in December 2020 and Quantitative Easing programme at £895 billion having extended it by £150 billion in the previous month. Within the latest forecasts, the Bank expects the UK economy to shrink -2% in Q4 2020 before growing by 7.25% in 2021, lower than the previous forecast of 9%. The BoE also forecasts the economy will now take until Q1 2022 to reach its pre-pandemic level rather than the end of 2021 as previously forecast.

3.12 UK Consumer Price Inflation (CPI) for November 2020 registered 0.3% year on year, down from 0.7% in the previous month. Core inflation, which excludes the more volatile components, fell to 1.1% from 1.5%. The most recent labour market data for the three months to October 2020 showed the unemployment rate rose to 4.9% while the employment rate fell to 75.2%. Both measures are expected to deteriorate further due to the ongoing impact of coronavirus on the jobs market, particularly when the various government job retention schemes start to be unwound in 2021, with the BoE forecasting unemployment will peak at 7.75% in Q2 2021.

3.13 GDP growth rebounded by 16.0% in Q3 2020 having fallen by -18.8% in the second quarter, with the annual rate rising to -8.6% from -20.8%. Monthly

GDP estimates have shown the economic recovery slowing and remains well below its pre-pandemic peak. Looking ahead, the BoE's November MPR forecasts economic growth will rise in 2021 with GDP reaching 11% in Q4 2021, 3.1% in Q4 2022 and 1.6% in Q4 2023.

3.14 **Credit outlook:** Credit Default Swaps (CDS) are instruments that can be used to gage market perception of a bank's financial condition. They are financial derivatives that guarantee against risk, similar to an insurance policy. The greater the perceived risk, the higher the price of insurance. After spiking in late March as coronavirus became a global pandemic and then rising again in October/November, Credit Default Swap (CDS) prices for the larger UK banks have steadily fallen back to almost pre-pandemic levels. However, general bank profitability in 2020 is likely to be significantly lower than in previous years. The credit ratings for many UK institutions were downgraded on the back of downgrades to the sovereign rating. Credit conditions more generally though in banks and building societies have tended to be relatively benign, despite the impact of the pandemic.

3.15 Looking forward, the potential for bank losses to be greater than expected when government and central bank support starts to be removed remains a risk, suggesting a cautious approach to bank deposits in 2021/22 remains advisable.

3.16 **Interest rate forecast:** The Authority's treasury management adviser Arlingclose is forecasting that Bank of England (BoE) Bank Rate will remain at 0.1% until at least the first quarter of 2024. The risks to this forecast are judged to be to the downside as the BoE and UK government continue to react to the coronavirus pandemic and the new EU trading arrangements. The BoE extended its asset purchase programme to £895 billion in November while keeping Bank Rate on hold. However, further interest rate cuts to zero, or possibly negative, cannot yet be ruled out but this is not part of the Arlingclose central forecast.

3.17 Gilt yields are expected to remain very low in the medium-term while short-term yields are likely to remain below or at zero until such time as the BoE expressly rules out the chance of negative interest rates or growth/inflation prospects improve. The central case is for 10-year and 20-year gilts to rise to around 0.5% and 0.75% respectively over the time horizon. The risks around the gilt yield forecasts are judged to be broadly balanced between upside and downside risks, but there will almost certainly be short-term volatility due to economic and political uncertainty and events.

3.18 A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix 5.

CAPITAL FINANCING REQUIREMENT

3.19 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Authority's strategy will be to minimise and delay external borrowing where possible, through the utilisation of investment balances, sometime known as internal borrowing.

3.20 The Authority's current level of debt and investments are set out in Appendix 2.

3.21 CIPFA's Prudential Code of Practice recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years.

3.22 The forecast movement in the CFR in coming years is one of the Prudential Indicators (PIs). The movement in actual external debt and usable reserves combine to identify the Authority's borrowing requirement and potential investment strategy in the current and future years.

Table 1: Balance Sheet Summary Analysis

	31-Mar-21 Estimate £m	31-Mar-22 Estimate £m	31-Mar-23 Estimate £m	31-Mar-24 Estimate £m
Capital Financing Requirement (CFR)	390	432	441	428
Less: Existing Profile of Long Term Borrowing and Other Long Term Liabilities	203	199	190	186
Cumulative Maximum External Borrowing Requirement	**187**	**233**	**251**	**242**
Usable Reserves	54	49	52	54
Cumulative Net Borrowing Requirement	**133**	**184**	**199**	**188**

3.23 Table 1 shows that the capital expenditure plans of the Authority over the next three years cannot be funded entirely from other sources and external borrowing will be required. Useable reserves are subject to review as part of the Medium-Term Financial Strategy.

BORROWING STRATEGY

3.24 The Authority as at 31st December 2020 held £170 million of longer-term loans, a decrease of £3 million from March 2020, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that in theory the Authority could need to borrow up to £184 million in 2021/22. The Authority may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing as per the Capital Strategy.

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

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

3.27 By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal and/or short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. The Authority's Treasury Management advisors will assist the Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2021/22 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

3.28 The Authority has previously raised a proportion of its long-term borrowing from the Public Works Loan Board (PWLB). The Authority will consider long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield.

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

3.30 In addition, the Authority may borrow short-term to cover unexpected cash flow shortages.

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

- HM Treasury's PWLB lending facility (formerly the Public Works Loan Board)
- Any other UK public sector body
- Any institution approved for investments
- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (with the exception of Merseyside Pension Fund)
- Capital market bond investors

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

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

- Leasing
- Hire purchase
- Private Finance Initiative
- Sale and leaseback

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

Type of borrowing

3.34 As the cost of carry remains high there is a greater reliance upon shorter dated and variable rate borrowing. This type of borrowing injects volatility into the debt portfolio in terms of interest rate risk but is counterbalanced by its affordability and alignment of borrowing costs with investment returns. Financial derivatives may also be used to manage this interest rate risk. The Authority's exposure to shorter dated and variable rate borrowing is kept under regular review.

LOBOs

3.35 The Authority has £108m of exposure to LOBO loans (Lender's Option Borrower's Option) of which £93m of these can be called within 2021/22. A LOBO is called when the lender exercises its rights to amend the interest rate on the loan at which point the borrower can accept the revised terms or reject them and repay the loan at no additional cost. LOBO loans present a potential refinancing risk to the Authority since the decision to call a LOBO is entirely at the lender's discretion. This refinancing risk is mitigated by the low interest rate climate, which has now been in existence for a number of years.

3.36 Any LOBOs called will be discussed with our Treasury Management advisors prior to acceptance of any revised terms. If a lender proposes to exercise their right to amend the interest rate of the loan, the default position will be the repayment of the LOBO without penalty i.e., the revised terms will not be accepted. Should the possibility arise of a LOBO being refinanced, for example by replacing the loan with a new loan arrangement, then the approach detailed below will be adopted.

Debt Rescheduling

3.37 The Authority's debt portfolio can be restructured by prematurely repaying loans and refinancing them on similar or different terms to achieve a reduction in risk and/or savings in interest costs.

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

- Savings in risk adjusted interest costs
- Rebalancing the interest rate structure of the debt portfolio
- Changing the maturity profile of the debt portfolio

3.39 Borrowing and rescheduling activity will be reported to the Policy & Resources Committee in the Annual Treasury Management Report and the regular treasury management reports.

TREASURY INVESTMENT STRATEGY

3.40 The Authority holds invested funds, representing income received in advance of expenditure plus balances and reserves held. As at 31st December 2020, the Authority held £19 million of treasury investments. In the past 12 months, the Authority's treasury investment balance has ranged between £19 and £140 million. Investment balances were higher than usual during March 2020 to June 2020 due to cash received from central government in response to the COVID-19 pandemic. As this cash was utilised investment levels reduced to an average £40 million between July 2020 and December 2020. A similar range in investment level is expected in the forthcoming year, varying between £40 million and £20 million, depending on the levels of grant received and the payment profiles.

3.41 **Objectives:** The CIPFA Code requires the Authority to invest its treasury funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. The Authority is facing severe funding pressures over future years and therefore any potential opportunities to increase income generation via investments, whilst adhering to CIPFA guidance, will be assessed for viability.

3.42 The Authority and its advisors continually assess economic and market conditions for signs of credit or market distress that might adversely affect the Authority.

3.43 **Negative Interest Rates**: The COVID-19 pandemic has increased the risk that the Bank of England will set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. Since investments cannot pay negative income, negative rates will be applied by reducing the value of investments. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

3.44 **Strategy:** Given the increasing risk and very low returns from short-term unsecured bank investments, the Authority aims to further diversify into more secure and/or higher yielding asset classes during 2021/22. This is especially the case for funds that are available for longer-term investment. The majority of the Authority's surplus cash is currently invested in short-term unsecured bank deposits and money market funds.

3.45 The Authority may invest its surplus funds with any of the counterparties shown in Appendix 3, subject to the cash and time limits shown.

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

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

3.48 **Secured Investments:** Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds and reverse repurchase agreements with banks and building societies are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used. The combined secured and unsecured investments with any one counterparty will not exceed the cash limit for secured investments.

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

3.50 Inter-authority investment and borrowing is a major source of local government financing with £115 billion of transactions reported nationally in 2018/19. The Council has not invested any funds with other local authorities since 2017 and no amounts remain outstanding. The treasury management team have utilised other options such as money market funds to place short term funds which have paid slightly higher rates. The inter-authority interest rate is not set by the individual local authority but by the market on the day and therefore no local authority has any influence over what rate it can charge. As with all lending, this purpose is for cash flow purposes and the funds cannot be used for day to day expenditure. The benefit of investing cashflows is that any interest the authority does make goes into the general budget that does support day to day expenditure.

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

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

3.53 **Money Market Funds:** Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. Although no sector limit applies to money market funds, the Authority will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.

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

3.55 **Real estate investment trusts (REITs)**: Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.

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

3.57 **Other investments:** The Authority may also invest cash with other organisations, for example by making loans to small businesses. Because of the higher perceived risk of unrated businesses, such investments may provide considerably higher rates of return. They will however only be made following a favourable external credit assessment.

3.58 **Risk Assessment and Credit Ratings:** Credit ratings are obtained and monitored by the Authority's treasury advisers, who will notify changes in ratings as they occur. The credit rating agencies in current use are listed in the Treasury Management Practices document. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

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

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

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

3.61 When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2020, this is not generally reflected immediately in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause investment returns to fall but will protect the principal sum invested.

3.62 **Investment Limits:** In order that the risk to the Authority's finances is further minimised in the case of a single default, a group of entities under the same ownership or a group of funds under the same management will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts and foreign countries as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country since the risk is diversified over many countries. Group Investment can be found in Appendix 3.

3.63 When calculating counterparty limits, the investment portfolio may be grossed up to include amounts that are being utilised by the Authority in lieu of borrowing (internally borrowed), as per the Authority's external advisor.

3.64 **Liquidity management:** The Authority uses cash flow forecasting to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium-term financial plan and cash flow forecast. The Authority will spread its liquid cash over providers (e.g., bank accounts and money market funds) to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

3.65 The Section 151 Officer, under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements. Decisions taken on the core investment portfolio will be reported to Committee meetings.

3.66 **Environmental, Social and Governance (ESG**): The Council's approach towards responsible investment, sustainability, its impact on society and the environment, as well as other ethical and good governance considerations. These factors can collectively be termed 'ESG'. Integrating ESG will allow the Council to deliver on key goals and also improve the long-term resilience of the balance sheet, particularly as it is now increasingly clear that there are financial benefits to be gained in the long-term from recognising the impact of climate change, efficient energy consumption, sustainable resources, inclusion, diversity, equality and strong corporate governance. A summary of the key ESG consideration is included in Appendix 6 to this report.

OTHER ITEMS REQUIRED BY CIPFA TO BE INCLUDED IN THE TREASURY MANAGEMENT STRATEGY

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

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

3.69 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for derivative exposures. An allowance for credit risk calculated using the methodology in the Treasury Management Practices document will count against the counterparty credit limit and the relevant foreign country limit.

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

3.71 **Markets in Financial Instruments Directive:** The Authority has opted up to professional client with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

3.72 **Investment Advisors**: The Authority continues to utilise an independent treasury advisor to provide the following services:

- Credit advice
- Investment advice

- Technical advice
- Economic & interest rate forecasts
- Workshops and training events

During 2020/21 these services were provided by Arlingclose. A competitive tendering exercise will be completed to appoint an advisor for 2021/22.

The Treasury Management Team within the Accountancy Services monitor the quality of the service provided.

INTEREST RATE FORECAST

3.73 The economic interest rate forecast provided by the Authority's treasury management advisor is attached at Appendix 5 The Authority will reappraise its strategies from time to time in response to evolving economic, political and financial events.

POLICY ON DELEGATION

3.74 The Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to the Policy and Resources Committee, and for the execution and administration of treasury management decisions to the Director of Resources who will act in accordance with the Council's Strategy Statement, Treasury Management Practices (TMPs) and CIPFA's Standard of Professional Practice on Treasury Management.

3.75 On a day-to-day basis the Treasury Management Team within Finance undertake the treasury management activities.

3.76 Decisions on short term investments and short-term borrowings may be made on behalf of the Section 151 Officer by the Senior Finance Business Partner with the responsibility for investments or any other members of that team who are empowered to agree deals subject to their conforming to the Authority's Treasury Management Strategy and policies outlined in this report.

3.77 A list of the current Authorised Signatories for Treasury Management activity, as designated by the Director of Finance & Investment, is included in Appendix 7.

3.78 Decisions on long term investments or long-term borrowings (i.e., for periods greater than one year) may be made on behalf of the Section 151 Officer by the Senior Finance Business Partner (or equivalent) or the Finance Business Partner (or equivalent) on the Treasury Management function and will be reported to Committee.

3.79 All officers will act in accordance with the policies contained within this document.

PERFORMANCE MONITORING AND REPORTING

3.80 The Council will receive reports on its treasury management policies, practices and activities, 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 in the form prescribed in its TMPs.

3.81 The Council will produce an Outturn Report on its treasury activity no later than 30 September after the financial year end.

4.0 FINANCIAL IMPLICATIONS

4.1 Approval and implementation of this strategy will limit financial risks while helping to minimise financing costs and maximise investment returns.

4.2 If the Council fails to set a balanced budget as a result of the significant financial pressures attributable to COVID-19, a Section 114 notice may be issued by the Section 151 Officer. Should this action be required, this would impede upon the Authority's ability to borrow funds.

5.0 LEGAL IMPLICATIONS

5.1 The MHCLG Guidance is issued by the Secretary of State under section 15(1)(a) of the Local Government Act 2003. Under that section local authorities are required to "have regard" to "such guidance as the Secretary of State may issue". The Council has adopted the requirement of the MHCLG to produce a Treasury Management Strategy**.** The Council would be putting its financial standing at risk, as well as failing to meet the requirements of the Local Government Act 2003, if it failed to follow the revised Treasury Management Code and the associated guidance. The Council has adopted the CIPFA Code of Practice on Treasury Management. This requires the annual production of a Treasury Management Strategy Statement, which this report fulfils and the reporting of treasury management activities at least twice a year.

6.0 RESOURCE IMPLICATIONS: STAFFING, ICT AND ASSETS

6.1 There are none arising out of this report.

7.0 RELEVANT RISKS

7.1 The Council is responsible for treasury decisions and activity and none of these decisions are without risk. The successful identification, monitoring and control of risk are important and the main risks and mitigations are:

Risk	**Mitigation**
Fluctuations in interest rate levels	That the borrowing and investment profiles are balanced both in terms of maturity (utilising short- and long-term instruments) and also in terms

	of the nature of the interest rate of the portfolio (fixed rate and variable interest rate products)
Exposure to inflation	That wherever possible investments are into at inflation equalling levels of interest. This depends entirely on the nature and purpose of the proposed investment.
Legal and Regulatory Risk	That appropriate legal advice is sought on new opportunities to ensure adherence to relevant legislation and regulation.
Credit and Counterparty Risk (Security of investments).	That any potential counterparty is subjected to suitable due diligence to ascertain appropriateness for investment and investment criteria
Council issues S114 notice	Should the Council encounter difficulties in obtaining borrowing following a S114 notice, the Authority has access to borrow from the PWLB as a lender of last resort. Any such borrowing would be subject to higher rates of interest.

8.0 ENGAGEMENT/CONSULTATION

8.1 This strategy report has been written in consultation with the Council's external treasury management advisors, Arlingclose Ltd, in accordance with best practice. There has also been consultation with Camdor Global Advisors in respect to the 'ESG' considerations outlined in Appendix 6 to this report. undertaken or proposed for this strategy report. There are no implications for partner organisations arising out of this report.

9.0 EQUALITY IMPLICATIONS

9.1 There are none arising directly from this report.

10.0 ENVIRONMENT AND CLIMATE IMPLICATIONS

10.1 As part of future investment strategy, consideration will be given to potential opportunities to invest in environmentally focussed instruments or organisations. 'Ethical, Social and Governance' (ESG) investment criteria will be considered and, where viable in adherence to the policies laid out in this strategy, will only be entered into following satisfactory assessment of the instrument and/or organisation. An example of such investment is the holding in the Public Sector Social Impact Fund.

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APPENDICES

1. Treasury Management Policy Statement
2. Existing Investment and Debt Portfolio Position
3. Approved Investment Counterparties
4. Treasury Management Indicators 2021/22 – 2023/24
5. Interest Rate Outlook
6. Environmental, Social and Governance Considerations
7. Authorised Signatories

BACKGROUND PAPERS

CIPFA Code of Practice on Treasury Management

SUBJECT HISTORY

Council Meeting	**Date**
Treasury Management Strategy Statement 2020-21	**17th February 2020**
Treasury Management Mid-Year Report 2020-21	**3rd November 2020**

APPENDIX 1

TREASURY MANAGEMENT POLICY STATEMENT

1. Introduction and background

1.1 The Council adopts the key recommendations of CIPFA's Treasury Management in the Public Services: Code of Practice (the Code), as described in Section 5 of the Code.

1.2 Accordingly, the Council will create and maintain, as the cornerstones for effective treasury management: -

- A treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities.

- Suitable treasury management practices (TMPs), setting out the manner in which the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

1.3 The Council (i.e., full Council) will receive reports on its treasury management policies, practices and activities 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, in the form prescribed in its TMPs.

1.4 The Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Committee, and for the execution and administration of treasury management decisions to the Section 151 Officer who will act in accordance with the Council's Strategy Statement, Treasury Management Practices (TMPs) and CIPFA's Standard of Professional Practice on Treasury Management.

2. Policies and objectives of treasury management activities

2.1 The Council defines its treasury management activities as:

"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."

2.2 This 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 organisation, and any financial instruments entered into to manage these risks.

2.3 This 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.

2.4 The Council's borrowing will be affordable, sustainable and prudent and consideration will be given to the management of interest rate risk and refinancing risk. The source from which the borrowing is taken and the type of borrowing should allow the Council transparency and control over its debt.

2.5 The Council's primary objective in relation to investments remains the security of capital. The liquidity or accessibility of the Authority's investments followed by the yield earned on investments remain important but are secondary considerations.

APPENDIX 2

EXISTING INVESTMENT & DEBT PORTFOLIO POSITION

	Current Portfolio as at 31 Dec 20 £m
External Borrowing (Long & Short Term)	
Public Works Loan Board	18
Local Authorities Temporary Loans	40
LOBO Loans	108
Other Loans	44
Total External Borrowing	210
Other Liabilities	
PFI	39
Total Other Long-Term Liabilities	39
Total External Debt	**249**
Treasury Investments:	
Managed in-house	
Deposits with Banks & Building Societies	1
Deposits with Community Interest Companies	1
Managed Externally:	
Royal London	1
Public Sector Social Investment Fund	10
Payden Sterling Reserve	4
Columbia Threadneedle	1
CCLA Property Fund	1
Total Investments	19
Net Borrowing Position	230

APPENDIX 3

APPROVED INVESTMENT COUNTERPARTIES

Investment Limits

Sector	**Time limit**	**Counterparty limit**	**Sector limit**
The UK Government	**50 years**	**Unlimited**	**n/a**
Local authorities & other government entities	**25 years**	**£10m**	**Unlimited**
Secured investments *	**25 years**	**£10m**	**Unlimited**
Banks (unsecured) *	**13 months**	**£5m**	**Unlimited**
Building societies (unsecured) *	**13 months**	**£5m**	**£10m**
Registered providers (unsecured) *	**5 years**	**£5m**	**£25m**
Money market funds *	**n/a**	**£10m**	**Unlimited**
Strategic pooled funds	**n/a**	**£10m**	**£50m**
Real estate investment trusts	**n/a**	**£10m**	**£25m**
Other investments *	**5 years**	**£5m**	**£10m**

* Minimum credit rating: Treasury investments in the sectors marked with an asterisk will only be made with entities whose lowest published long-term credit rating is no lower than A-. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be considered.

For entities without published credit ratings, investments may be made where external advice indicates the entity to be of sound credit quality.

Additional investment limits

Any group of pooled funds under the same management	£25m per manager
Negotiable instruments held in a broker's nominee account	£25m per broker
Foreign countries	£10m per country

APPENDIX 4

TREASURY MANAGEMENT INDICATORS 2021/2022

1. Background

Treasury management indicators are not in the 2017 edition of the CIPFA Treasury Management Code itself but in the separate Treasury Management Code guidance notes for local authorities, which was last published in 2011. The Authority measures and manages its exposures to treasury management risks using the following indicators.

<u>Treasury Management Indicators</u>

1. Security

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

Credit risk indicator	Target
Portfolio average credit rating	A-

2. Liquidity

The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount it can borrow each quarter without giving prior notice.

Liquidity risk indicator	Target
Total sum borrowed in past 3 months without prior notice	**£15m**

3. Maturity Structure of Borrowing

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

Maturity Structure of Borrowing	Lower Limit 2021/22 %	Upper Limit 2021/22 %
Under 12 Months	0	90
12 Months and within 24 months	0	75
24 Months and within 5 years	0	75
5 years and within 10 years	0	75
10 years and over	0	100

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment, including LOBO loans, many of which have repayment options every six months.

4. Principal Sums Invested for Periods Longer Than a Year

The Council has placed an upper limit for principal sums invested for periods longer than a year. This limit is to contain exposure to the possibility of loss that may arise as a result of the Council having to seek early repayment of the sums invested.

Price risk indicator	2021/22	2022/23	2023/24
Limit on principal invested beyond year end	£50m	£30m	£30m

APPENDIX 5

The Arlingclose Economic and Interest Rate Outlook

Underlying assumptions:

- The medium-term global economic outlook has improved with the distribution of vaccines, but the recent upsurge in coronavirus cases has worsened economic prospects over the short term.

- Restrictive measures and further lockdowns are likely to continue in the UK and Europe until the majority of the population is vaccinated by the second half of 2021. The recovery period will be strong thereafter, but potentially longer than previously envisaged.

- Signs of a slowing UK economic recovery were already evident in UK monthly GDP and PMI data, even before the second lockdown and Tier 4 restrictions. Employment is falling despite an extension to support packages.

- The need to support economic recoveries and use up spare capacity will result in central banks maintaining low interest rates for the medium term.

- Brexit will weigh on UK activity. The combined effect of Brexit and the after-effects of the pandemic will dampen growth relative to peers, maintain spare capacity and limit domestically generated inflation. The Bank of England will therefore maintain loose monetary conditions for the foreseeable future.

- Longer-term yields will also remain depressed, anchored by low central bank policy rates, expectations for potentially even lower rates and insipid longer-term inflation expectations. There is a chance yields may follow a slightly different path in the medium term, depending on investor perceptions of growth and inflation, or the deployment of vaccines.

Forecast:

- Arlingclose expects Bank Rate to remain at the current 0.10% level.

- Our central case for Bank Rate is no change, but further cuts to zero, or perhaps even into negative territory, cannot be completely ruled out, especially with likely emergency action in response to a no-deal Brexit.

- Gilt yields will remain low in the medium term. Shorter term gilt yields are currently negative and will remain around zero or below until either the Bank expressly rules out negative Bank Rate or growth/inflation prospects improve.

	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
	%	%	%	%	%	%	%	%	%	%	%	%	%
Official Bank Rate													
Upside Risk	0.00	0.00	0.15	0.15	0.15	0.15	0.30	0.30	0.30	0.30	0.30	0.30	0.30
Arlingclose Central Case	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Downside Risk	0.30	0.40	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
3 Month Money Market Rate													
Upside Risk	0.05	0.05	0.10	0.10	0.15	0.20	0.30	0.30	0.30	0.30	0.30	0.30	0.30
Arlingclose Central Case	0.10	0.10	0.15	0.15	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
Downside Risk	0.30	0.40	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
5 Year Gilt Rate													
Upside Risk	0.40	0.40	0.45	0.45	0.50	0.50	0.55	0.60	0.60	0.65	0.65	0.70	0.70
Arlingclose Central Case	0.00	0.00	0.05	0.10	0.15	0.20	0.20	0.20	0.25	0.25	0.25	0.25	0.25
Downside Risk	0.40	0.45	0.50	0.55	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60
10 Year Gilt Rate													
Upside Risk	0.30	0.35	0.40	0.45	0.50	0.50	0.55	0.60	0.60	0.65	0.65	0.70	0.70
Arlingclose Central Case	0.25	0.30	0.35	0.35	0.40	0.40	0.45	0.45	0.50	0.55	0.55	0.55	0.60
Downside Risk	0.50	0.50	0.55	0.55	0.55	0.55	0.55	0.55	0.55	0.55	0.55	0.55	0.55
20 Year Gilt Rate													
Upside Risk	0.40	0.40	0.45	0.45	0.50	0.50	0.55	0.60	0.60	0.65	0.65	0.70	0.70
Arlingclose Central Case	0.70	0.70	0.75	0.75	0.75	0.80	0.80	0.85	0.85	0.85	0.85	0.90	0.90
Downside Risk	0.30	0.30	0.35	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40
50 Year Gilt Rate													
Upside Risk	0.40	0.40	0.45	0.45	0.50	0.50	0.55	0.60	0.60	0.65	0.65	0.70	0.70
Arlingclose Central Case	0.60	0.60	0.65	0.65	0.65	0.80	0.70	0.70	0.75	0.75	0.75	0.80	0.80
Downside Risk	0.30	0.30	0.35	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40

APPENDIX 6

Environmental, Social and Governance (ESG) Considerations

Outside of financial risks, it is increasingly evident that there are also key non-financial risks with financial consequences over the longer-term for the Council. In particular

- **Environmental risks**: Climate change has continued to become an increasingly evident problem, with extreme weather events rising and temperatures increasingly on a global basis. Coupled with the depletion of natural resources and the negative feedback loop created by hydrocarbon pollution, there are growing concerns about the environment and the potential financial impact on societies, economies and businesses.

- **Social risks**: Inequality, diversity and inclusion are becoming more important considerations. The unequal recovery since the last financial crisis coupled with financial pressures on public sector balance sheets have led to a growing divergence of outcomes and concerns about parts of society being systematically left behind. There is also increased scrutiny from a range of stakeholders. For the Council, there is also a vested interest in protecting and minimising the most vulnerable in society.

- **Governance risks**: Governance covers the rights and responsibilities of the senior management of companies, institutions and counterparties, in particular its structures, corporate values and accountability processes. The proper treatment of employees, ensuring an ethical approach to supply chains, paying living wages, how counterparties ensure that management is acting in the best interests of all stakeholders – these are all clear areas of focus that if poorly managed, can lead to reputational and financial consequences for the Council's portfolio in the long-term.

The Council's objective is to recognise all these risks, to mitigate them where possible and thereby improve the security of its portfolios and balance sheet in the long-term.

Within these risks, the Council has identified climate change as a long-term, material and systemic financial risk with the potential to significantly impact the treasury portfolio, the capital strategy and the Council's financial resilience over time. The Council has declared a Climate Emergency already in response to this, and further, in respect of its investments, will seek to:

- Minimise exposure to counterparties and investments heavily impacted by climate change risk.
- Increase exposure to sectors, counterparties and investments, such as renewables, whose activities aid the transition to a lower carbon world and economy.
- Contribute meaningfully to an improved economically sustainable future locally and nationally, without sacrificing security

The Council will incorporate ESG issues into its analysis and decision-making processes when considering the treasury portfolio and capital investments. The Council will seek to use data and analysis where available to determine the type and materiality of relevant issues for counterparties.

ESG Risk Appetite

It is important to note that risk will always exist in some measure and cannot be removed in its entirety. Additionally, in order to realise investment and commercial gains, it is unavoidable for some measure of risk to exist.

Therefore, risks need to be considered both in terms of potential threats to the Council and positive opportunities.

The risk appetite will be considered annually and monitored on an ongoing basis by senior management and external advisors.

In general, the Council seeks to minimise its exposure to risks that are unwanted and unrewarded. Of relevance to ESG, the Council is exposed to a range of risks across its balance sheet and portfolios:

Environmental risks related to the environmental impact of the Council's strategy and investments.
• Social risks related to the social impact of the Council's strategy and investments.
• Governance risks related to ensuring that prudence and careful consideration sit at the heart of the Council's decision-making, augmented by quality independent advice and appropriate checks and balances.

Within these, the Council's appetite is as follows:

Risk	Appetite
Environmental	No appetite for environmentally negative risks. Moderate to high appetite for projects and investments that reduce environmental risks and promote sustainability. Always subject to full due diligence and subsequent monitoring of risks and key appropriate metrics.
Social	Low appetite for social risks, especially in the local region. Moderate appetite for projects and investments that reduce social risk. Always subject to full due diligence and subsequent monitoring of risks and key appropriate metrics.
Governance	No appetite for investments and initiatives that are not accompanied by careful due diligence and an assessment of the transaction versus the Council's resources, funding needs, cashflow requirements, ESG risk preferences and broader goals. All subject to ongoing monitoring of risks and key relevant metrics to manage the Council's

	exposure and respond to any emerging issues. Depth and frequency of monitoring should be proportional to the complexity and capital at risk for the Council.

APPENDIX 7

AUTHORISED SIGNATORIES

The following officers are authorised to make payments, either via the Council's online banking system or by signing cheques, and issue other instructions relating to Treasury Management transactions on behalf of Wirral Borough Council:

Director of Resources – Shaer Halewood

Assistant Director of Finance & Investment – Daniel Kirwan

Senior Finance Manager – Peter J. Molyneux

Senior Finance Manager – Peter McCann

Senior Finance Manager – Vikki Gregorich

Senior Finance Manager – Diane Grisdale

This list can be amended at the discretion of the Director of Resources, should the need arise due to operational requirements.