WIRRAL

# POLICY AND RESOURCES COMMITTEE

## Wednesday, 15 February 2023

| REPORT TITLE: | TREASURY MANAGEMENT STRATEGY 2023/24 |
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| REPORT OF: | DIRECTOR OF FINANCE (S151 OFFICER) |

**REPORT SUMMARY**

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

Key points that the report covers include;

- The Council complies with the requirement to produce an annual Treasury Management Strategy

- This strategy includes the capabilities to reschedule debt, should a prudent opportunity arise to either minimise interest costs, reprofile the debt maturity profile or reduce the level of refinancing risk.

- The Council policy of internal borrowing, which delays entering into new long term loan arrangements by using cashflows available to temporarily fund capital expenditure.

- The level of interest charges made to the Treasury budget in 2023/24 will be determined by the delivery rate of the capital programme coupled with the interest rate environment. The level of investment income received will also be affected by the interest rate market.

- Included with this report are the investment parameters within which Treasury activity will be carried out during 2023/24.

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

The report supports the delivery of the Wirral Plan 2021 - 26 as the Capital Programme contributes towards projects that support all five Wirral Plan priorities.

This matter affects all Wards within the Borough.

The decisions in this report are key decisions.

## RECOMMENDATIONS

The Policy & Resources Committee is requested to recommend to Council the approval of:

(1) the Treasury Management and Investment Strategy for 2023/2024.

(2) the Treasury Management Prudential 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. This report no longer incorporates the Investment Strategy as required under the Department of Levelling Up, Housing and Communities' Investment Guidance, which mostly refers to non-treasury investments. Investments held for service purposes or for commercial profit are considered in a different report, the Investment Strategy.

## 2.0 OTHER OPTIONS CONSIDERED

2.1 CIPFA's 2021 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 2023/28 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 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."*

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

- A Treasury Management Policy Statement (see Appendix A), stating the policies, objectives and approach to risk management of its treasury management activities.

- Suitable Treasury Management Practices, 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.

3.3 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. Generally, higher financial returns reflect higher levels of risk.

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

3.5 Adoption of this Treasury Management Strategy Statement includes approval for the following:

- Treasury Management Strategy for 2023/24.
- Treasury Management Policy Statement
- Treasury Management Prudential Indicators for 2023/24.

**ECONOMIC BACKGROUND**

3.6 The Economy: The ongoing impact on the UK from the war in Ukraine, together with higher inflation, higher interest rates, uncertain government policy, and a deteriorating economic outlook, will be major influences on the Council's treasury management strategy for 2023/24.

3.7 The Bank of England increased Bank Rate by 0.5% to 4.0% in February 2023, the tenth successive rise since December 2021. The decision was voted for by a 7-2 majority of the Monetary Policy Committee, with two members preferring to maintain Bank Rate at 3.50%. The November quarterly Monetary Policy Report forecast a prolonged but shallow recession in the UK with CPI inflation remaining elevated at over 10% in the near-term. While the projected peak of inflation is lower than in the August report, due in part to the government's support package for household energy costs, inflation is expected remain higher for longer over the forecast horizon and the economic outlook remains weak, with unemployment projected to start rising.

3.8 Credit outlook: Credit Default Swaps are instruments that can be used to gauge 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. Credit default swap prices have followed an upward trend throughout 2022, indicating higher credit risk. They have been boosted by the war in Ukraine, increasing economic and political uncertainty and a weaker global and UK outlook, but remain well below the levels seen at the beginning of the Covid-19 pandemic. The prices in this market serve as an indicator of the financial direction of a bank, which may impact upon the counterpart limit imposed upon any bank on the investment counterpart list.

3.9 There are competing tensions in the banking sector which could impact bank balance sheet strength going forward. The weakening economic outlook and likely recessions in many regions increase the possibility of a deterioration in the quality of banks' assets, while higher interest rates provide a boost to net income and profitability. However, the institutions on the Council's adviser Arlingclose's counterparty list remain well-capitalised and their counterparty advice on both recommended institutions and maximum duration remain under constant review and will continue to reflect economic conditions and the credit outlook.

3.10 Interest rate forecast: The Council's treasury management adviser Arlingclose forecasts that bank rate will continue to rise in 2023 as the Bank of England attempts to subdue inflation which is significantly above its 2% target. Arlingclose expects bank rates to rise to 4.25% by June 2023 under its central case, with the risks in the near- and medium-term to the upside should inflation not evolve as the bank forecasts and remains persistently higher.

3.11 PWLB loans base their interest rates on Gilts. It is anticipated that current Gilt prices have potential future interest rate increases factored in and consequently PWLB loan rates available to the Council are to remain largely at current levels. As ever, there will undoubtedly be short-term volatility due to economic and political uncertainty and events.

**CAPITAL FINANCING REQUIREMENT**

3.12 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying sums available for investment. The Council's strategy will be to minimise and delay external borrowing where possible, through the utilisation of investment balances, sometimes known as internal borrowing.

3.13 The Council's current level of debt and investments are set out in Appendix B.

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

3.15 The forecast movement in the CFR in coming years is one of the Prudential Indicators. The movement in actual external debt and usable reserves combine to identify the Council's borrowing requirement and potential investment strategy in the current and future years. As determined by the 'Liability Benchmark' described below.

3.16 Table 1 shows that, because of the capital expenditure plans of the Council over the next three years, there is a net borrowing requirement each year. Useable reserves are subject to review as part of the Medium-Term Financial Strategy.

**Table 1: Balance Sheet Summary Analysis**

| | **31-Mar-23 Estimate £m** | **31-Mar-24 Estimate £m** | **31-Mar-25 Estimate £m** | **31-Mar-26 Estimate £m** |
|---|---|---|---|---|
| Total Capital Financing Requirement (CFR) | 390 | 421 | 420 | 402 |
| Less: Other Long Term Liabilities | -31 | -28 | -25 | -21 |
| **Loans CFR** | **359** | **393** | **395** | **381** |
| Less: Existing Profile of Long Term Borrowing | -164 | -163 | -156 | -142 |
| **Internal Borrowing** | **195** | **230** | **239** | **239** |
| Less Usable Reserves | -53 | -33 | -33 | -33 |
| **New Borrowing Requirement** | **142** | **197** | **206** | **206** |

3.17 The Council as at 31st December 2022 held £160 million of longer-term loans, a decrease of £4 million from March 2022, as part of its strategy for funding previous years' capital programmes. As evidenced by table 1 there is a difference between the CFR and the level of actual longer term borrowing. This is due to the Council's approach over recent years of using readily available cash resources rather than entering into costly borrowing to fund the capital programme This is not a permanent measure as cash balances need to be appropriate to allow reserves to be used as required. The balance sheet forecast in table 1 shows that in theory the Council could need to borrow up to an additional £142 million in 2023/24. The Council 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.

3.18 Liability benchmark: To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table 1 above, but that cash and investment balances are kept to a minimum level of £10m at each year-end to maintain sufficient liquidity but minimise credit risk.

3.19 The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level required to manage day-to-day cash flow, as shown below. The 'Loans CFR' is derived by subtracting any other long-term liabilities (e.g., PFI liabilities) from the total CFR.

**Table 2: Prudential Indicator: Liability benchmark**

| | 31.3.23 Estimate £m | 31.3.24 Forecast £m | 31.3.25 Forecast £m | 31.3.26 Forecast £m |
|---|---|---|---|---|
| Loans CFR | 359 | 393 | 395 | 381 |
| Less: Balance sheet resources | -176 | -176 | -176 | -176 |
| **Net loans requirement** | **183** | **217** | **219** | **205** |
| Plus: Liquidity allowance | 10 | 10 | 10 | 10 |
| **Liability benchmark** | **193** | **227** | **229** | **215** |

3.20 Table 2 reiterates that over the coming years there will be a requirement to borrow additional funds to deliver the existing capital plans and maintain a minimum level of investments. There is a requirement to show the information in Table 2 in a graphical format, this is included in Appendix C to this report.

**BORROWING STRATEGY**

3.21 Objectives: The Council'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 Council's long-term plans change is a secondary objective.

3.22 Strategy**:** Given the significant pressures on local government funding, the Council'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 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.

3.23 By doing so, the Council 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 Council's Treasury Management advisors will assist the Council with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2023/24 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

3.24 The Council has previously raised a proportion of its long-term borrowing from the Public Works Loan Board (PWLB). The Council will consider long-term loans from other sources including banks, pensions and local authorities 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.

3.25 Alternatively, the Council 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.

3.26 In addition, the Council will need from time to time to borrow short-term to cover unexpected cash flow shortages.

3.27 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

3.28 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

**Short-term and variable rate loans**

3.29 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 Council's exposure to shorter dated and variable rate borrowing is kept under regular review.

**'Lender's Option Borrower's Option' (LOBO) Loans**

3.30 At 31 December 2022 the Council has £94.5m of exposure to LOBO loans of which £84.5m of these can be called within 2023/24. 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 Council since the decision to call a LOBO is entirely at the lender's discretion. With interest rates having risen recently, there is now a reasonable chance that lenders will exercise their options.

3.31 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, to reduce refinancing risk in later years. 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**

3.32 The Council'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.

3.33 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 Council 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

3.34 As mentioned in 3.18 to 3.20 the 'liability benchmark' illustrates the current level of Council borrowing. Any potential refinancing of existing loans will be scheduled with the consideration of the existing maturity profile of Council debt, along with the duration of required debt, as per the liability benchmark.

3.35 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**

3.36 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. As at 31st December 2022, the Council held £37 million of treasury investments. In the past 12 months, the Council's treasury investment balance has ranged between £23 and £84 million. Investment balances were higher than usual during March 2022 and May 2022 due to cash received from central government in late March 2022 relating to the Council Tax Rebate grant. As this cash was utilised investment levels reduced to an average £40 million between June 2022 and December 2022. A similar range in investment level is expected in the forthcoming year, depending on the levels of grant received and the payment profiles.

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

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

3.39 Strategy: As demonstrated by the liability benchmark above, the Council expects to be a long-term borrower and new treasury investments will therefore be made primarily to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different sectors and boost investment income.

3.40 The CIPFA Code does not permit local authorities to both borrow and invest long-term for cash flow management. But the Council may make long-term investments for treasury risk management purposes, including to manage interest rate risk by investing sums borrowed in advance for the capital programme for up to three years; to manage inflation risk by investing usable reserves in instruments whose value rises with inflation; and to manage price risk by adding diversification to the strategic pooled fund portfolio.

3.41 The Council may invest its surplus funds with any of the counterparties shown in Appendix D, subject to the cash and time limits shown.

3.42 Business models: Under the International Financial Reporting Standard 9 accounting standard, the accounting for certain investments depends on the Council's "business model" for managing them. The Council 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.

3.43 Operational bank accounts: The Council 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 Council maintaining operational continuity.

3.44 Risk Assessment and Credit Ratings: Credit ratings are obtained and monitored by the Council'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.

3.45 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.

3.46 Other Information on the Security of Investments: The Council 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 Council'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.

3.47 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 Council 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 Council'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.

3.48 Investment Limits: In order that the risk to the Council'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 D.

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

3.50 Liquidity management: The Council 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 Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium-term financial plan and cash flow forecast. The Council 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.

3.51 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.

3.52 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 F to this report.

3.53 Related Matters: Appendix G to this report includes detail on related matters that the CIPFA code requires the Council to include within its Treasury Management Strategy.

3.54 Investment Advisors: The Council 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

A competitive tendering exercise was completed to appoint an advisor for an initial period spanning April 2021 to March 2024, with the option to extend for a further two years. The successful bid came from Arlingclose Ltd.
The Treasury Management Team within the Accountancy Services monitor the quality of the service provided.

**INTEREST RATE FORECAST**

3.55 Economic and interest rate forecasts are provided by the Council's treasury management advisor. The Council will reappraise its strategies from time to time in response to evolving economic, political, and financial events.

**POLICY ON DELEGATION**

3.56 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 Finance who will act in accordance with the Council's Strategy Statement, Treasury Management Practices and CIPFA's Standard of Professional Practice on Treasury Management.

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

3.58 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 Council's Treasury Management Strategy and policies outlined in this report.

3.59 A list of the current Authorised Signatories for Treasury Management activity, as designated by the Director of Finance, is included in Appendix H.

3.60 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.

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

**PERFORMANCE MONITORING AND REPORTING**

3.62 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.

3.63 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, a Section 114 notice may be issued by the Section 151 Officer. Should this action be required, this would impede upon the Council's ability to borrow funds.

## 5.0 LEGAL IMPLICATIONS

5.1 The DLUHC 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 DLUHC 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 entered 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 Council has access to borrow from the PWLB as a lender of last resort. Any such borrowing would be subject to higher rates of interest. |

7.2 The risks mentioned above are inherent in Treasury activity, therefore they are persistent, continuous risks. Appendix A of this report states that "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, setting out the way the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities."

## 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 F to this 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 are the holdings in the Altana Social Impact Partnership and the Green Energy Bond.

## 11.0 COMMUNITY WEALTH IMPLICATIONS

11.1 The Community Wealth Building Strategy is a key part of how the Council will tackle economic, social and health inequalities across the borough and make a major contribution to improving the economic, social and health outcomes on the Wirral. As mentioned within 10.1 of this report, 'ESG' criteria will be considered in investment decision. The Altana Social Impact Partnership "offers local authorities an opportunity to improve Public Sector cash flows and quality of life for their constituents. Cash flow is improved by pooling capital and knowledge while creating and investing in long lasting social impact UK projects."

11.2 Also contained within this strategy are the Council considerations in respect to borrowing. This borrowing requirement would occur as a result of financing the ongoing capital programme. Schemes contained within the Capital programme include several regeneration projects that look to improve the economic outlook for the borough, including job creation, training facilities and enhanced transport links. The Community Wealth Building implications are reported for each scheme separately to the relevant policy and service committee.

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**APPENDICES**

A. Treasury Management Policy Statement
B. Existing Investment and Debt Portfolio Position
C. Liability Benchmark – Graphical Format
D. Approved Investment Counterparties
E. Treasury Management Indicators 2023/24 – 2025/28
F. Environmental, Social and Governance Considerations
G. CIPFA Code – Related Matters
H. Authorised Signatories

**BACKGROUND PAPERS**

CIPFA Code of Practice on Treasury Management

**TERMS OF REFERENCE**

This report is being considered by the Policy and Resources Committee in accordance with 1.2(a)(i) of the Policy and Resources Committee Terms of Reference:

formulate, co-ordinate and implement corporate policies and strategies and the medium term financial plan (budget), which includes responsibility for any decision:
(i) that relates to such matters to the extent that they are not reserved to full Council.

**SUBJECT HISTORY (last 3 years)**

| Council Meeting | Date |
|---|---|
| **Treasury Management Strategy Statement 2020-21** | **Cabinet – 17 Feb 2020** |
| **Treasury Management Annual Report 2019-20** | **Cabinet – 27 July 2020** |
| **Treasury Management Mid-Year Report 2020-21** | **P&R – 3 Nov 2020** |
| **Treasury Management Strategy Statement 2021-22** | **P&R - 17 Feb 2021** |
| **Treasury Management Annual Report 2020-21** | **P&R - 28 July 2021** |
| **Treasury Management Mid-Year Report 2021-22** | **P&R - 10 Nov 2021** |

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|---|---|
| **Treasury Management Strategy Statement 2022-23**<br>**Treasury Management Annual Report 2021-22**<br>**Treasury Management Mid-Year Report 2022-23** | **P&R - 15 Feb 2022**<br>**P&R - 13 Jul 2022**<br>**P&R - 9 Nov 2022** |

**APPENDIX A**

**TREASURY MANAGEMENT POLICY STATEMENT**

**Introduction and background**

A1 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.

A2 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, setting out the way the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

A3 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.

A4 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 and CIPFA's Standard of Professional Practice on Treasury Management.

**Policies and objectives of treasury management activities**

A5 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."

A6 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.

A7 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.

A8 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.

A9 The Council's primary objective in relation to investments remains the security of capital. The liquidity or accessibility of the Council's investments followed by the yield earned on investments remain important but are secondary considerations.

**APPENDIX B**

**EXISTING INVESTMENT & DEBT PORTFOLIO POSITION**

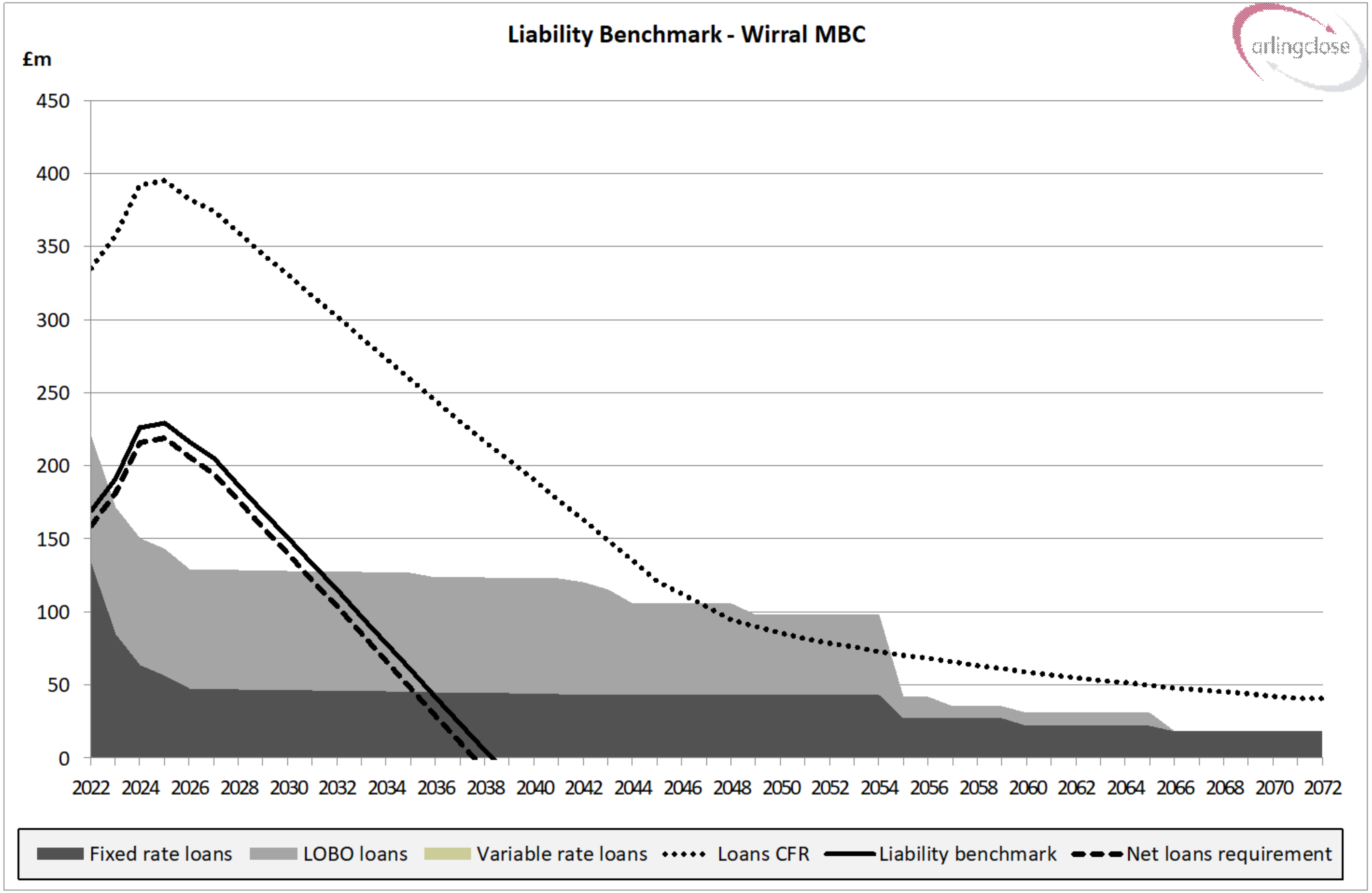
| | **Current Portfolio as at 31 Dec 22 £m** |
|---|---|
| **External Borrowing (Long & Short Term)** | |
| Public Works Loan Board | 24.1 |
| Local Authorities Temporary Loans | 77.0 |
| LOBO Loans | 94.5 |
| Other Loans | 41.6 |
| Total External Borrowing * | 237.2 |
| **Other Liabilities** | |
| Private Finance Initiative | 33.1 |
| Total Other Long-Term Liabilities | 33.1 |
| **Total External Debt** | **270.2** |
| **Treasury Investments:** | |
| Community Interest Companies | 1.1 |
| Money Market Funds | 16.9 |
| Green Energy Bond | 1.5 |
| *Strategic Pooled Funds:* | |
| Royal London | 1.0 |
| Altana Social Investment Partnership | 10.0 |
| Payden Sterling Reserve | 4.0 |
| Columbia Threadneedle | 1.0 |
| CCLA Property Fund | 1.0 |
| **Total Investments** | 36.5 |

B1 *£14.8 million of the £237.2 million of external borrowing relates to transferred debt from the former Merseyside County Council. Wirral administers this debt on behalf of the following other Authorities who make annual repayments towards this liability:

- Knowsley Council
- Liverpool City Council
- Sefton Council
- St Helens Council
- Merseyside Fire and Rescue Service
- Merseyside Police
- Merseyside Recycling & Waste Authority
- Merseytravel

APPENDIX C

LIABILITY BENCHMARK – GRAPHICAL FORMAT



Supporting Notes:

- The concept is that the chart allows a comparison of the current level of borrowing against the need to borrow, looking at both the amount (on the y axis) and the term (on the x axis).

- Where level of actual loans (the grey shaded areas on the chart) exceed the Liability Benchmark (the solid middle line of the three lines), the Council can make long-term investments for cash flow management or repay loans early; where the Liability Benchmark exceeds loans, the authority can take long-term borrowing or sell investments.

- The 'Loans CFR' (the top, dotted line of the three lines on the chart) can be described as the maximum permitted level of borrowing. Borrowing up to the 'Loans CFR' will usually mean high levels of investments, exposing the authority to credit, price and interest rate risks.

- The 'Net Loans Requirement' (the bottom, dashed line of the three lines on the chart) is the minimum possible level of borrowing, at which investments would be zero. This would expose the authority to the liquidity risk of being unable to make payments when due.

- The Liability Benchmark is then the level between the two, where an appropriate balance of risks can be struck between these two extremes.

- There is no requirement to borrow exactly to the Liability Benchmark, but a decision to borrow more or less, or longer or shorter, than the Liability Benchmark implies a deliberate decision to accept additional risk. This may be entirely appropriate if it is accompanied by a reduction in cost, for example through short-term borrowing at lower margins.

- For the Council what this chart estimates is that, if capital plans proceed as forecast and following which there in no new capital borrowing added to the programme, then there will be a need for additional borrowing for a period of about ten years of up to a peak of approximately £100 million. This requirement can be seen on the chart as the white segment that is above the current level of shaded debt and the below the solid middle line of the Liability Benchmark.

- The profile of this chart will change over time if additional capital borrowing is added to the existing programme, or new external debt is entered into.

**APPENDIX D**

**APPROVED INVESTMENT COUNTERPARTIES**

**Table 1: Limits for New Investment**

| Sector | Time limit | Counterparty limit | Sector limit for total investments |
|---|---|---|---|
| The UK Government | 3 years | Unlimited | n/a |
| Local authorities & other government entities | 3 years | £10m | Unlimited |
| Secured investments * | 3 years | £10m | £30m |
| Banks (unsecured) * | 13 months | £5m | £15m |
| Building societies (unsecured) * | 13 months | £5m | £10m |
| Registered providers (unsecured) * | 3 years | £5m | £10m |
| Money market funds * | n/a | £10m | £100m |
| Strategic pooled funds | n/a | £10m | £20m |
| Real estate investment trusts | n/a | £5m | £10m |
| Other investments * | 3 years | £5m | £15m |

*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.

**Table 2: 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 |
| Financial Institutions not domiciled in the UK | £10m per country |

D1 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.

D2 Local Authority: Inter-authority investment and borrowing is a major source of local government financing with over £8 billion of active short term inter-authority loans reported nationally at 30th September 2022. 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.

D3 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.

D4 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.

D5 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.

D6 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 Council will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.

D7 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 Council 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 Council's investment objectives will be monitored regularly.

D8 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.

D9 Other investments: The Council may also invest cash with other organisations, for example by making loans to small businesses. These investments are not subject to bail-in but are exposed to the risk of the company going insolvent. 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.

**APPENDIX E**

**TREASURY MANAGEMENT PRUDENTIAL INDICATORS 2023/2024**

## E1 Background

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

**Treasury Management Indicators**

## E2 Security

The Council 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 |

## E3 Liquidity

The Council 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** | **£10m** |

## E4 Maturity Structure of Borrowing

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

| Maturity Structure of Borrowing | Lower Limit 2023/24 % | Upper Limit 2023/24 % |
|---|---|---|
| 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.

## E5 Long-term treasury management investments

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. The prudential limits on the long-term treasury management investments will be:

| **Price risk indicator** | **2022/23** | **2023/24** | **2024/25** |
|---|---|---|---|
| **Limit on principal invested beyond year end** | £40m | £30m | £30m |

Long-term investments with no fixed maturity date include strategic pooled funds and real estate investment trusts but exclude money market funds and bank accounts with no fixed maturity date as these are considered short-term.

## APPENDIX F

### Environmental, Social and Governance (ESG) Considerations

F1 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:

F2 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.

F3 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.

F4 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.

F5 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.

F6 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.

F7 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**

F8 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.

F9 Therefore, risks need to be considered both in terms of potential threats to the Council and positive opportunities.

F10 The risk appetite will be considered annually and monitored on an ongoing basis by senior management and external advisors.

F11 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.

F12 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 G

## CIPFA CODE – RELATED MATTERS

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

### Financial Derivatives

G1 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.

G2 The Council 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 Council 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.

G3 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.

G4 In line with the CIPFA Code, the Council will seek external advice and will where necessary consider that advice before entering into financial derivatives to ensure that it fully understands the implications.

### Markets in Financial Instruments Directive

G5 The Council has chosen to be assigned the 'professional client' status 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 Council's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status to not limit the range of products available to the Council.

**APPENDIX H**

**AUTHORISED SIGNATORIES**

H1 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 Finance – Matthew Bennett

Assistant Director of Finance & Investment – Daniel Kirwan

Senior Finance Manager – Peter Molyneux

Senior Finance Manager – Diane Grisdale

Senior Finance Manager – Mark Goulding

Senior Finance Manager – Christopher Kelly

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