Agenda Item 7

Treasury Management Strategy

FALKIRK COUNCIL

Subject: **Treasury Management Strategy**

Meeting: **Executive**

Date: **13 April 2021**

Author: **Director of Corporate & Housing Services**

1. Purpose of Report

1.1 The Code of Practice for Treasury Management sets out a framework for Treasury Management reporting for a financial year. This framework requires a Treasury Management Strategy Report, an Interim Review Report and an Annual Review Report. This report presents the Treasury Management Strategy Report for 2021/22.

1.2 The Treasury Management Strategy Report is a forward looking report which includes:

- Economic Outlook
- Capital plans
- The Loans Fund
- A borrowing strategy for 2021/22
- An investment strategy for 2021/22

1.3 The Code of Practice requires that, following consideration by the Executive, the report is referred to Council for approval.

2. Recommendations

2.1 **Executive agrees that the report is referred to Council for consideration, and that Council:**

1) adopts the Borrowing Strategy for 2021/22 as set out in section 7 of this report;
2) approves the Treasury Indicators as set out in sections 7 and 8 of this report and;
3) adopts the Investment Strategy for 2021/22 and approves the list of "Permitted Investments" as set out in section 8 of this report.

3. Background

3.1 Treasury Management within the Council involves two main functions:

- The Council must operate a balanced revenue budget. Treasury Management ensures that the cashflow of the Council is adequately planned and cash is available when needed. Cash is borrowed or invested as required, and the security of the Council's cash is the main consideration.

- Treasury Management funds the Council's Capital Programme, essentially requiring longer term cashflow planning to ensure that capital spend can be funded.

3.2 This report presents the Treasury Management Strategy Report for 2021/22 and is the first of three Treasury Management reports that Members will receive covering 2021/22.

3.3 Revisions to the CIPFA Prudential Code and the CIPFA Treasury Management Code introduced the requirement for a Capital Strategy to be developed. The aim of the Capital Strategy is to provide a high level overview of how capital expenditure, capital financing and treasury management activity contributes to the provision of services. The Council's Capital Strategy for 2021 - 2026 was approved by Members at Council on 11 March 2021.

4. Economic Outlook

4.1 The spread of Covid-19 and the efforts taken globally have led to more economic uncertainty than experienced before. The third national lockdown at the start of 2021, pushed economic recovery further back.

4.2 Whilst short term forecasts have been cut for 2021, the medium term forecasts are more optimistic based on the assumption that the current lockdown will be gradually eased as vaccines are rolled out. Key assumptions from the Bank of England Monetary Policy Committee (MPC) are:

- The economy will start to recover strongly from quarter 3 of 2021.

- Those who have saved during the pandemic will spend once lockdown restrictions are eased, providing a boost to the economy.

- The economy will return to pre-pandemic levels by quarter 1 of 2022.

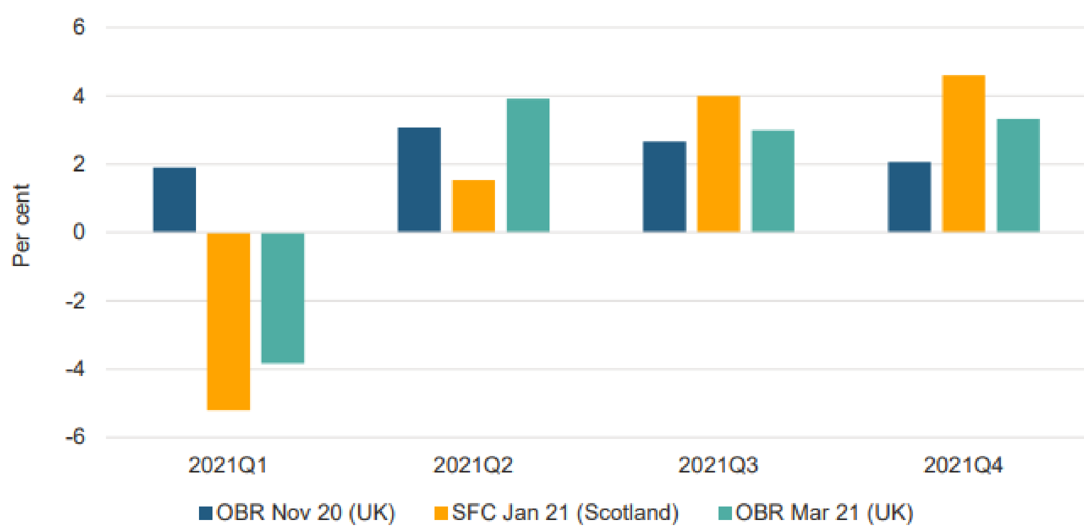
- Unemployment will peak at around 7.5% during late 2021 and then fall to about 4.2% by the end of 2022. Around 0.5m foreign workers will have returned home and no longer be part of the UK workforce.

- CPI inflation is forecast to rise sharply towards the 2% target in quarter 1 of 2021 and remain close to 2% in 2022 and 2023.

4.3 The MPC acknowledged the risks in their assumptions, mainly focused on virus mutations and vaccine efficiency. The MPC also removed negative interest rates as a possibility for at least six months. Given that the economy is expected to start growing strongly around this time, this suggests that negative interest rates are only a very slight possibility.

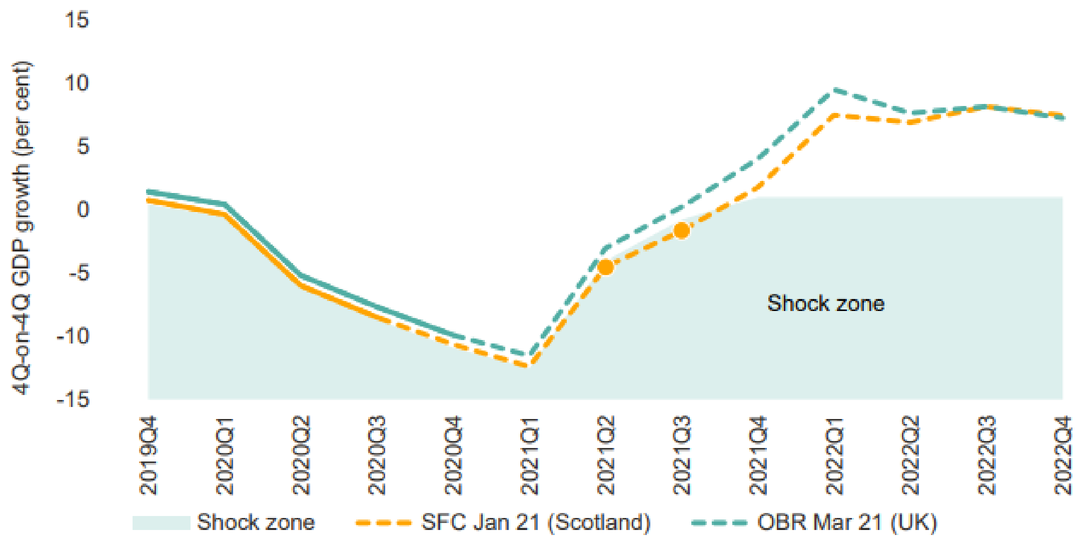
4.4 The Chancellors budget, presented in March 2021, set out the start of rebalancing public finances mainly through increased taxation. Spend forecasts omit any extra Covid relating spending post 2021/22. Whilst the fiscal balance has deteriorated in the short term, it is projected to recover more quickly than before so that by 2025/26 the current budget deficit is eliminated. However, debt is projected to remain at more than 100% of GDP for the foreseeable future.

4.5 In January 2021, the Scottish Fiscal Commission (SFC) set out various forecasts for the Scottish economy. This work was updated in March 2021. The chart below is extracted from that March update and shows the Office of Budget Responsibility (OBR) forecasts for UK growth in November 2020 and March 2021, compared to the SFC January forecasts.



Source: Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – January 2021 , OBR (2021) Economic and Fiscal Outlook – March 2021 OBR (2020) Economic and Fiscal Outlook – November 2020

4.6 The OBR forecasts in November were obviously before the third lockdown announcements. The OBR are forecasting a smaller fall in GDP for the UK than the SFC forecast for Scotland in the quarters one and two. However, the SFC forecast a stronger growth for Scotland in quarters three and four. The SFC believes that the outlook for Scottish GDP and UK GDP are broadly similar but a Scotland specific economic shock has already been triggered and the conditions leading to that are still present, partly due to differences in the timing of the forecasts. A comparison of the positions is shown in the chart below:



Source: Scottish Fiscal Commission (2021) Scotland's Economic and Fiscal Forecasts – January 2021 OBR (2021) Economic and Fiscal Outlook – March 2021

4.7 From a longer term perspective the SFC expect that in 2025 the Scottish GDP will be around 4% smaller than in pre Covid forecasts. This compares to the OBR's forecast of 3% in the UK as a whole.

4.8 Ultimately, uncertainty remains with the outlook largely dependent on the success of the vaccine rollout and the lifting of restrictions.

5. Capital Plans

Capital Expenditure

5.1 The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators. Capital Expenditure is the first Prudential Indicator.

5.2 The General Fund Capital Programme for 2021/22 – 2025/26 was approved by Members on 11 March 2021. The Housing Investment Programme was approved on 20 January 2021. A summary of the proposed total investment is shown below:

Capital expenditure	2021/22 £m	2022/23 £m	2023/24 £m	2024/25 £m	2025/26 £m
Non-HRA	86.8	68.4	82.8	59.4	61.6
HRA	54.8	83.1	86.6	55.9	52.8
Total	**141.6**	**151.5**	**169.4**	**115.3**	**114.4**

5.3 The approved Programme sets out a total of £692m of expenditure over the next five years. These figures include the impact of the projected year end position for 31 March 2021 but this will be updated fully to reflect the final position following the financial year end. The carry forward of any projects will be reported separately to Executive.

5.4 The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in the need to borrow.

Capital financing	**2021/22 £m**	**2022/23 £m**	**2023/24 £m**	**2024/25 £m**	**2025/26 £m**
Capital receipts	1.4	-	-	-	-
Capital grants	30.9	36.1	42.5	47.3	49.8
Capital reserves	0.8	-	0.2	-	-
Revenue	2.2	1.6	1.4	-	-
Borrowing Requirement	**106.3**	**113.8**	**125.3**	**68.0**	**64.6**
Total Financing	141.6	151.5	169.4	115.3	114.4

The Council's Need to Borrow (the Capital Financing Requirement or CFR)

5.5 The second Prudential Indicator that the Council has to calculate is the Capital Financing Requirement or CFR. CFR is the total historic outstanding capital expenditure which has not yet been paid for. Any capital expenditure which requires borrowing will increase the CFR.

5.6 The CFR is reduced by annual repayments of debt from revenue. The CFR also includes any other long term liabilities, for example PFI schemes. Whilst these schemes increase the CFR, and therefore the Council's borrowing requirement, they have their own financing arrangement and so the Council does not have to separately borrow for these schemes. CFR projections for the Council are shown in the table below:

	2021/22 £m	**2022/23 £m**	**2023/24 £m**	**2024/25 £m**	**2025/26 £m**
CFR – Non HRA	272.4	309.1	333.0	331.5	331.4
CFR – HRA	237.8	289.5	361.7	402.1	438.3
Total CFR	**510.2**	**598.6**	**694.7**	**733.6**	**769.7**
Movement in CFR (from prior year)	**+85.1**	**+88.4**	**+96.1**	**+38.9**	**+36.1**

Movement in CFR represented by:					
Net financing need for the year (above)	106.3	113.8	125.3	68.0	64.6
Less loan fund repayments and other financing movements	(21.2)	(25.4)	(29.2)	(29.1)	(28.5)
Movement in CFR	**85.1**	**88.4**	**96.1**	**38.9**	**36.1**

6. Loans Fund

6.1 The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 require disclosures within the Annual Strategy, in relation to Loans Fund Accounting. Details of the disclosures required are as follows:

- Explanation of the Loans Fund
- The policy for determining the repayment for Loans Fund Advances
- An analysis of the movement in Loans Fund Advances
- A profile of future Loans Fund Repayments
- Separate disclosure for Housing Revenue Account (HRA)
- An explanation for any changes to Loans Fund Repayment profile

6.2 Every local authority in Scotland as required by The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016, must operate a loans fund. This is unique to Scotland. The loans fund acts as an internal bank for the Council. The loans fund also provides the long term financing that the Council needs in respect of capital expenditure.

6.3 As required by the 2016 regulations, an analysis of the current loans fund advances together with a profile of future loans fund repayments is detailed in Appendix 4. This information has been separately shown for General Fund, HRA and TIF. Specific details have been provided for 2020/21 and thereafter shown in bands of years. Note that the advances for years 1 – 5 includes 2020/21 slippage/rescheduled projects as well as those included in the approved 2021/22 – 2025/26 capital programmes.

6.4 The 2016 Regulations allow Councils to revise the repayment period and/or the repayment amount of historic debt for debt prior to 1 April 2016. Officers will explore the opportunities that this may provide and report back to Members.

6.5 The 2016 Regulations also allow Councils to review the interest rate used to calculate the loans fund repayment. The rate currently used is a consolidated loans fund interest rate that is applied consistently to the General Fund debt and Housing Revenue Account (HRA) debt. It does not reflect that in recent years and indeed over the next five years, the level of borrowing has been/will be heavily skewed towards the HRA because of the significant investment programmes that have been approved. It is therefore the intention to review the interest rate applied and consider whether different interest rates should be applied to the General Fund and HRA, to more accurately reflect the actual cost of borrowing undertaken.

Statutory Repayment of Debt

6.6 Under the 2016 regulations, the Council is required to set out its policy for the statutory repayment of loans fund advances prior to the start of the financial year. The repayment of loans fund advances ensures that the Council makes a prudent provision each year to pay off an element of the accumulated loans fund advances made in previous financial years. The Council’s method is as follows:

- All historic loans fund advances made up to 31 March 2021, will continue to be repaid on the existing repayment basis i.e. annuity method. The repayment term is commensurate with the benefit of the asset to which the advance relates. All loans fund advances made during 2021/22 will also be repaid using the annuity method with a repayment term which is commensurate with the benefits of asset to which the advance relates.

6.7 The annuity rate applied to loans fund repayments is consolidated based on the historic interest rates of loans taken out previously and projections of interest payable during the year. The current projected rate for 2021/22 is approximately 3.5%. That rate will change on an annual basis, consolidating all the interest paid and received.

7. Borrowing Strategy 2021/22

7.1 The capital expenditure plans set out in section 5 detail the planned activities of the services. The treasury management function ensures that the Council's cash is organised so that sufficient cash is available to meet this service activity and the Council's capital strategy. This requires the organisation of cashflow and appropriate borrowing facilities. This section on borrowing includes:

- An estimate of the external borrowing as at 31 March 2021
- An estimate of the borrowing requirement for 2021/22
- Prospects for interest rates
- Treasury Indicators: limits to borrowing activity

External Borrowing

7.2 The year end position for 2020/21 is currently being finalised. The external borrowing position at the time of writing this report is:

External Borrowing	£'m	% of Total Debt
Local Authorities	36.0	13.3%
PWLB	208.2	77.1%
Market Loans	26.0	9.6%
Total Estimated Debt	**270.2**	**100.0%**

Borrowing Requirement for 2021/22

7.3 The Council's capital programmes were approved in January 2021 (HRA) and March 2021 (General Fund). The total borrowing requirement for the capital programmes 2021/22 is £106.3m. Consideration is also given to any borrowing which will mature and be replaced in year. The budgeted borrowing requirement for 2021/22 is shown in the table below:

Borrowing Requirement for 2021/22	£'m
Capital Programmes (net of capital receipts)	106.3
Service Payments	(21.2)
Replacement of Long Term Borrowing	2.0
Replacement of Short Term Borrowing	41.0
Total Budgeted Borrowing Requirement	**128.1**

7.4 The £106.3m borrowing requirement for capital programmes is made up of £12.3m borrowing for TIF projects, £48.6m for the Housing capital programme and £45.4m for the General Fund capital programme. As the year progresses, these figures will change and the borrowing requirement will be updated. This will be reported to Members as part of the capital programme monitoring reports.

7.5 The replacement of short term borrowing shown in the table above refers to £41m of short term debt that matures throughout 2021/22. These loans may be replaced on a short term or long term basis depending on cash flow requirements and relative prevailing interest rates.

Prospects for Interest Rates

7.6 Previous reports to Members have noted that at each borrowing point, consideration is given to all the options available and the complete range of borrowing periods is reviewed. The table below sets out indicative interest rates for both the bank base rate, short term borrowing and PWLB long term borrowing.

		MONEY RATES		PWLB RATES			
	Bank Rate	3 Mths	1Yr	5Yr	10Yr	25Yr	50Yr
2021/22	0.1	0.1	0.2	1.2	1.6	2.2	2.0
2022/23	0.1	0.1	0.2	1.2	1.7	2.3	2.1
2023/24	0.1	0.1	0.2	1.4	1.9	2.5	2.3

7.7 As shown in the forecast table above, no increase in Bank Rate is expected in the near-term as it is unlikely that inflation will rise sustainably above 2% during this period.

7.8 There is expected to be little upward movement in PWLB rates over the next two years as government gilt yields of major countries around the world are expected to rise little during this time (PWLB rates are linked to gilt yields). There can be volatility in gilt yields and this would impact on PWLB rates.

7.9 In November 2020, the Chancellor announced the outcome from a review of margins over gilt yields for PWLB rates which had been increased in October 2019 and had resulted in a significant reduction in PWLB borrowing across the UK. The margins were reduced by 1%. The Council will harness these improved rates at the appropriate time. The Council can borrow from PWLB using three available rates:

- PWLB certainty rate (gilt plus 0.8%)
- PWLB HRA certainty rate (gilt plus 0.8%)
- Local Infrastructure rate (gilt plus 0.6%; up to a value of £2.678m)

7.10 There remains uncertainty over the timing of future interest rate increases. The rates available at a given time will impact on cost to the General Fund and HRA. The indications are that there will continue to be a significant interest rate differential in favour of short term borrowing. However, it is important that a balanced approach is taken to short and longer term borrowing to ensure risk is appropriately managed.

7.11 The total value of Market Loans is £26m. It should be noted that there is potential for £13m of these Market Loans to be repaid during the year should any of the lenders invoke a rate change clause as per their individual contracts. These Market Loans are held with Dexia Credit (£8m) and Just Retirement Ltd (£5m). The remaining two Market Loans (£13m) are held with Barclays Bank and as previously advised they have waived their right to change the applicable interest rate of these loans. Given the current level of interest rates, the risk of early repayment of any of the remaining loans is assessed as extremely low.

7.12 Rescheduling of current borrowing in the debt portfolio is unlikely to occur as there is still a very large difference between PWLB premature redemption rates and new borrowing rates. In short, debt rescheduling would be expensive and cost more than simply continuing to repay the original loan.

Treasury Indicators: Limits to Borrowing Activity

7.13 There are two main treasury indicators which set out limits in respect to borrowing. These are the Operational Boundary and the Authorised Limit for External Debt.

7.14 The operational boundary is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

Operational Boundary	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m	2024/25 Estimate £m	2025/26 Estimate £m
Debt	433.6	527.0	631.2	671.3	714.2
Other long term liabilities	76.4	68.0	58.8	53.7	50.8
Total	**510.0**	**595.0**	**690.0**	**725.0**	**765.0**

7.15 The authorised limit for external debt is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

Authorised Limit	2021/22 Estimate £m	2022/23 Estimate £m	2023/24 Estimate £m	2024/25 Estimate £m	2025/26 Estimate £m
Debt	438.6	532.0	636.2	676.3	719.2
Other long term liabilities	76.4	68.0	58.8	53.7	50.8
Total	**515.0**	**600.0**	**695.0**	**730.0**	**770.0**

7.16 The table below shows the upper and lower limits on the maturity structure of any borrowing as well as the interest rate spread.

1) MATURITY STRUCTURE	2021/22 LOWER	2021/22 (2020/21) UPPER
Fixed Interest Rate Borrowing:	%	%
Under 12 months	0	35 (35)
12 months – 2 years	0	20 (20)
2 years – 5 years	0	20 (20)
5 years – 10 years	0	30 (30)
10 years – 20 years	0	30 (30)
20 years – 30 years	0	30 (30)
30 years – 40 years	0	30 (30)
40 years – 50 years	0	40 (40)
Variable Interest Rate Borrowing:		
Under 12 months	0	5 (5)
12 months – 2 years	0	5 (5)
2 years – 5 years	0	5 (5)
5 years – 10 years	0	5 (5)
10 years – 20 years	0	5 (5)
20 years – 30 years	0	5 (5)
30 years – 40 years	0	5 (5)
40 years – 50 years	0	5 (5)

8. Investment Strategy 2021/22

8.1 The Council will invest any surplus funds it has for a short term, to help effectively manage the Council's cashflow. This will take account of the outlook for short term interest rates. The regulatory framework provides greater autonomy for local authorities but makes clear that the onus is on local authorities to act prudently with regard to their investment and treasury management activities. The investment priorities are listed in order below:

1. Security
2. Liquidity
3. Yield

8.2 This section on investments covers:

- Permitted investments
- Counterparties
- Investment returns
- Treasury Indicators: limits to investment activity

Permitted Investments

8.3 The Local Government Investments (Scotland) Regulations 2010 requires Council approval of all the types of investments, known as “Permitted Investments”, to be used and set limits, where appropriate, for the amount and period that can be held in each type of investment.

8.4 The Permitted Investments which may be used in the forthcoming year are:

- CASH TYPE INSTRUMENTS
  - Deposits with other local authorities
  - Deposits with UK Government including Deposits with the Debt Management Account Facility (DMADF), treasury bills and gilts
  - Instant Access or On-Notice deposit accounts with financial institutions (banks and building societies).
  - Term deposits with financial institutions (banks and building societies)
  - Money Market Funds

- OTHER INVESTMENTS
  - Investment Properties (none currently held by the Council)
  - Shareholdings in a local authority company (refer Appendix 1)
  - Loans to a local authority company (none currently held by the Council)
  - Non-Local authority shareholdings (refer to Appendix 1)
  - Loans to third parties, including soft loans (refer to Appendix 3)

8.5 The Investment Regulations also require the investment position of the Common Good fund(s) to be made explicit. Surplus funds are invested in the Council’s loans fund on which interest is earned. There are also a number of property assets, such as Kilns House, the Steeple and Arnotdale which attract a rental yield.

8.6 Details, as appropriate, of the risks, mitigating controls and limits associated with each of the Permitted Investments are attached at Appendix 1.

Counterparties

8.7 The Report provides details of the counterparties that the Council engages with in terms of its investments (see Appendix 1). To assess counterparty risk, prior to investing the Council makes use of credit ratings information. Credit rating information is supplied by the Link Group, our treasury advisors, on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating Watches (notification of a likely change), rating Outlooks (notification of the longer-term bias outside the central rating view) are provided to officers almost immediately after they occur and this information is considered before dealing. The lending criterion for 2021/22 has been reviewed to ensure it is robust enough to enable the Council to manage its investments effectively.

8.8 Previous reports to Members have highlighted risks arising from high cash balances and a limited pool of counterparties. Officers have therefore been working to open accounts with counterparties which fit with the criteria previously approved by Members. This has been done in conjunction with our Treasury Management advisors. A deposit account with Handelsbanken has been set up. Handelsbanken is a UK entity which offers call account facilities and is used by a number of Scottish local authorities. Handlesbanken has a good rating and comfortably meets the F1 short term and A- long term rating criteria.

8.9 For permitted cash type investments, the Council maintains a counterparty list in compliance with the relevant counterparty selection criteria. Appropriate extracts from the Council's Treasury Management Practices (TMPs) are attached for Members' information at Appendix 2.

8.10 The Regulations make clear that the Council must not borrow more, or in advance of its capital financing requirement as determined under the Prudential Code purely to profit from the investment of the extra sums borrowed. It is confirmed that the Council has no plans to borrow in advance of need in the forthcoming financial year.

Investment Returns

8.11 As noted earlier in this report, the bank rate is unlikely to rise from 0.10% for a considerable period. As a result, it may be safe to assume that investment earnings will be low for the foreseeable future.

8.12 Money market fund yields have fallen near to zero. Inter-local authority lending and borrowing rates have also declined due to the surge in the levels of cash seeking a short-term home at a time when many local authorities are probably having difficulties over accurately forecasting when disbursements of funds received will occur or when further large receipts will be received from the Government.

Treasury Indicators: Limits to Investment Activity

8.13 Local authorities are asked to set limits for principal funds invested for greater than 365 days. These limits are set with regard to the Council's liquidity requirements, to ensure the Council has adequate cashflow and doesn't incur financial penalties through the early sale of investments. However, Falkirk Council does not currently invest sums for longer than 365 days.

1)	**MAXIMUM PRINCIPAL SUMS INVESTED > 365 DAYS** The Council does not envisage having sums available for investment for periods longer than 365 days.

9. Other Areas to Consider

Prudential Code & Treasury Management Code

9.1 On 1 February 2021 the Chartered Institute of Public Finance and Accountancy (CIPFA) issued consultations on two Codes of Practice – Treasury Management Code and the Prudential Code.

9.2 The main amendments proposed to the Treasury Management Code are:

- Augmenting the training and qualifications requirements to ensure that an organisation recognises the importance of all staff and council Members having the required skills and knowledge to undertake their duties and responsibilities

- The introduction of a new treasury management practice to establish, implement and monitor the arrangements for the identification, management, and control of Environmental, Social and Governance risks.

- The introduction of a dedicated treasury management board or committee, because of more complex treasury management functions being undertaken by Local Authorities.

9.3 The main amendments proposed to the Prudential Code are focussed on commercial activity which is not relevant at this point for Falkirk Council. There are, however, some relevant changes including:

- Increased emphasis on sustainability and ensuring that capital expenditure is consistent with a local authority's corporate objectives.
- The introduction of new prudential indicators on affordability.

9.4 It is anticipated that the revised Codes will be published towards the end of 2021/22 for implementation. Members will be updated on the impact of the revised Codes.

Treasury Management Advisers

9.5 The Council has appointed Link Asset Services as its treasury management advisers. The contract is subject to regular review and comprises:

- Technical support on treasury and capital finance issues
- Economic and interest rate analysis
- Advice on debt rescheduling
- Borrowing and investment advice on interest rates, timing and financial instruments
- Credit ratings/market information service accessing the three main credit rating agencies

9.6 The Council currently has a two year contract with Link Asset Services effective from 1 April 2021 to 31 March 2023.

9.7 It is important to recognise under the terms of the revised Code, that regardless of the input from Link, the final decision on treasury matters always rests with the Council.

Member/Officer Training

9.8 The Investment Regulations provide for increased scrutiny by Members of treasury management issues. It was expected that training sessions for Members would be scheduled during 2020. However, the Covid-19 pandemic has impacted on this. Training sessions will be scheduled as and when required, to ensure that Members are fully aware of their scrutiny role. It is intended that a training session will be set up late Spring/early Summer 2021.

9.9 There is a requirement under the Treasury Management Practices (TMPs), that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. This is achieved by in-house training supplemented by staff attending training courses/seminars organised by the Council's Treasury Advisers or other institutions in the field of Treasury Management or CIPFA (Scotland) Treasury Management Forum.

9.10 There will be an enhanced focus on training for Members and officers as part of the response to the Treasury Management Code (see paragraph 9.2).

10. Consultation

10.1 There is no requirement to carry out a consultation on this report.

11. Implications

Financial

11.1 Assumptions made on both borrowing and investment is an integral part of the Revenue Budget setting process. The Revenue Budget and Capital Programmes for both General Fund and Housing reflect the financial consequences of the proposed Borrowing and Investment Strategies within this report.

Resources

11.2 There are no resource implications arising from the report recommendations.

Legal

11.3 There are no legal implications arising from the report recommendations.

Risk

11.4 Although interest rate assumptions are considered after discussion with Link, the Council's treasury advisers, there is always the risk that they could change, which could impact on the level of interest payable by the Council. The Council's prudent approach to lending attempts to mitigate the Council's risk.

11.5 In terms of investments, the Council engages with a number of counterparties who meet the minimum rating criteria with at least one of the three credit rating agencies. There is a risk that some counterparties will fall below this minimum criteria which would limit the number of available counterparties to the Council.

11.6 The level of cash balances that the Council holds has been very volatile over the past year, mainly as a result of the Covid-19 pandemic. Work is ongoing to ensure there are sufficient counterparties to place money with, ensuring that any risk, no matter how small, is adequately spread. However, there is a risk that if this volatility continues, it will lead to a breach of counterparty limits.

Equalities

11.7 An equality and poverty impact assessment is not required.

Sustainability/Environmental Impact

11.8 A sustainable assessment is not required.

12. Conclusion

12.1 The key messages from this report are that whilst there is optimism in improvements to the economy, that is predicated on the rapid rollout of the vaccination programme and the effectiveness of the vaccine to manage the Covid-19 pandemic. At this time, it is considered likely that interest rates will remain low for the next 2 to 3 years. However, there is the potential for volatility in rates, not least due to the pandemic.

12.2 The approved Capital Strategy and capital programmes set out an ambitious level of investment by Falkirk Council over the next five years - £692m in total. It will be important to ensure that Treasury Management arrangements are robust in helping to support this level of investment through good management of cashflows and effective decision making on borrowing. The Council's Treasury Management Advisors, Link Asset Services, will be a key part of this work.

12.3 Consultation exercises on CIPFA's Treasury Management Code and the Prudential Code are underway. The implications of any changes as a result of these reviews will be reported back to Members.

Director of Corporate & Housing Services

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Appendices
Appendix 1 – Falkirk Council Permitted Investments, Associated Controls and Limits
Appendix 2 - Credit & Counterparty Policies
Appendix 3 – Third Party Loans
Appendix 4 – Loans Fund Advances & Repayments

List of Background Papers
Link Asset Services Interest Rate Forecast

APPENDIX 1

FALKIRK COUNCIL PERMITTED INVESTMENTS, ASSOCIATED CONTROLS AND LIMITS

Type of Investment	Treasury Risks	Mitigating Controls	Council Limits
(a) Deposits with other local authorities or public bodies **(very low risk)**	These are considered quasi UK Government debt and as such there is no risk to value. Deposits will be for a fixed term and liquidity may therefore present a problem as deposits can only be broken with the agreement of the counterparty and penalties can apply. Non local authority deposits will follow the approved credit rating criteria.	Little mitigating controls required for local authority deposits, as this is a quasi UK Government investment. .	£10m per LA and maximum 1 year
(b) Deposits with the Debt Management Account Facility (UK Government) **(very low risk)**	This is a deposit with the UK Government and as such there is no risk to value. Deposits can be between overnight and 6 months and liquidity may therefore present a problem as deposits can only be broken with the agreement of the counterparty and penalties can apply.	Little mitigating controls required. As this is a UK Government investment, the monetary limit is unlimited to allow for a safe haven for investments.	£unlimited, maximum 6 months
(c) Money Market Funds (MMFs) - LVNAV **(very low risk)**	Pooled cash investment vehicle which provides very low counterparty, liquidity and market risk. These will primarily be used as liquidity instruments.	Funds will only be used where the MMFs have a “AAA” rated status from all of Fitch, Moody’s or Standard & Poors.	£10m per fund and on Call

Type of Investment	Treasury Risks	Mitigating Controls	Council Limits
(d) Instant Access or On-Notice deposit accounts with financial institutions (banks and building societies) **(low risk depending on credit rating)**	These tend to be low risk investments, but will exhibit higher risks than categories (a), (b) and (c) above. There is little risk to value with these types of investments, liquidity is high and investments can be returned at short notice.	The counterparty selection criteria restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard & Poors. On day to day investment dealing, use of the selection criteria will be further strengthened by additional market intelligence.	£10m max and on Call subject to individual institution criteria
(e) Term deposits with financial institutions (banks and building societies) **(low to medium risk depending on period and credit rating)**	This tends to be low risk investments, but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is little risk to value with these types of investments, liquidity is low and term deposits can only be broken with the agreement of the counterparty and penalties may apply.	The counterparty selection criteria restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard & Poors. On day to day investment dealing, use of the selection criteria will be further strengthened by additional market intelligence.	Banks - £10m and maximum 1 year subject to individual institution criteria for banks. Building Societies - £7m and maximum 1 year subject to individual institution criteria for building societies
(f) Investment Properties - The Council does not currently hold any investment properties, but this may change with the progression of the Falkirk Gateway Development	These are non-service properties which are being held pending disposal or for a longer term rental income stream. These are highly illiquid assets with high risk to value (the potential for property prices to fall or for rental voids).	In larger investment portfolios, some small allocation of property based investment may counterbalance/compliment the wider cash portfolio. Property holding will be re-valued regularly and reported annually with gross and net rental streams.	N/A at the moment, but may be revised in the future

Type of Investment	Treasury Risks	Mitigating Controls	Council Limits
(g) Loans to third parties, including soft loans and loans to Registered Social Landlords	These are service transactions either at market rates of interest or below market rates (soft loans). These types of transactions may exhibit credit risk and are likely to be highly illiquid.	Each third party loan and each application is supported by the service rationale behind the loan and the likelihood of partial or full default.	Consistent with the particular scheme
(h) Loans to a local authority company (the Council currently has no such loans)	These are service investments either at market rates of interest or below market rates (soft loans). These types of investments may exhibit credit risk and are likely to be highly illiquid.	Each loan to a local authority company and each application is supported by the service rationale behind the loan and the likelihood of partial or full default.	N/A
(i) Shareholdings in a local authority Company. The Council has an investment of £3.597m as at 31/03/20 in Falkirk Community Stadium Ltd (represented by a range of assets at Westfield, Falkirk)	These are service investments which may exhibit market risk and are likely to be highly illiquid.	Each equity investment in a local authority company requires Member approval and each application will be supported by the service rationale behind the investment and the likelihood of loss.	£5m
(j) Non-local authority shareholdings: The Council has an investment of £0.5m in thinkWhere, an independent company in Geographical Information Systems. The Council relies on their systems, software and data management capacity to analyse, interrogate and utilise information that underpins some of the Council's Core Services	These are non-service investments which may exhibit market risk; be only considered for longer term investments and will likely be liquid.	Any non-service equity investment will require separate Member approval and each application will be supported by the service rationale behind the investment and the likelihood of loss.	£0.5m

The Monitoring of Investment Counterparties – The status of counterparties will be monitored regularly. The Council receives credit rating and market information from Link Asset Services, from which counterparties are checked promptly. On occasion, ratings may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria will be removed from the list immediately by the Chief Finance Officer and, if required, new counterparties which meet the criteria will be added to the list.

APPENDIX 2

CREDIT AND COUNTERPARTY POLICIES

Criteria to be used for creating/managing approved counterparty lists/limits.

- Chief Finance Officer in conjunction with the treasury management advisers, will formulate suitable criteria for assessing and monitoring the credit risk of investment counterparties and shall construct a lending list comprising period, type, sector and specific counterparty limits.

- To qualify for use, a counterparty must meet the minimum rating criteria with at least one of the three credit rating agencies.

- The Council will also have regard to additional operational market information such as negative rating watches/outflows before selecting the relevant counterparties.

- The Council's approved counterparty list will extend to selected counterparties from the following sectors:

  UK Banks
  Overseas Banks (but with UK authorisation) Minimum Sovereign rating of AA
  Building Societies
  UK Local Authorities
  UK Government

- The minimum level of credit rating for an approved counterparty per Fitch or equivalent ratings will be as undernoted, with particular reference to the short term rating but having regard to the long term rating.

SHORT TERM	F1	Indicates the strongest capacity for timely payment of financial commitments within a 12 month timeframe
LONG TERM	A-	High Credit Quality. A low expectation of credit risk with a strong capacity for timely payment of financial commitments

- The Council's own banker (Royal Bank of Scotland) will continue to be used for investment purposes even if the bank falls below the above criteria, because it is part nationalised. Balances will also be held on a Call basis too. Investments will be restricted to the ring fenced bank – Royal Bank of Scotland Plc.

- Investments in Nat West, which is also part nationalised with the Royal Bank of Scotland, can be included if they continue to be part nationalised or if they meet the ratings above. Investments will be restricted to the ring fenced bank – National Westminster Bank Plc.

- The maximum period for investments will be 1 year unless an alternative period is recorded against a specific counterparty.

- The maximum value for any one investment transaction will be £10 million unless a lesser amount is recorded against a specific counterparty.

Full individual listings of counterparties and their limits are shown below.

APPROVED COUNTERPARTIES AND COUNTERPARTY LIMITS

Investments in the form of Temporary Deposits may be placed with the institutions noted below subject to the limit per institution indicated.

INSTITUTIONS UK BANKS	**LIMIT**	**MAX PERIOD**
Royal Bank of Scotland or Nat West *	£10m	1 year
Santander UK	£10m	1 year
Barclays Bank	£10m	1 year
HSBC	£10m	1 year
Standard Chartered	£10m	1 year
Sumitomo Mitsui Banking Corporation Europe	£10m	1 year
Lloyds Bank or Bank of Scotland *	£10m	1 year
Goldman Sachs International Bank	£10m	1 year
Handelsbanken	£10m	1 year

A maximum combined monetary limit of £10m in Royal Bank of Scotland/Nat West and £10m in Lloyds Bank/ Bank of Scotland

BUILDING SOCIETIES		
Nationwide	£7m	1 year
Coventry	£7m	1 year
Leeds	£7m	6 months
Yorkshire	£7m	6 months
Skipton	£7m	6 months
UK LOCAL AUTHORITIES	£10m per LA	1 year
UK GOVERNMENT	Unlimited	6 months
MONEY MARKET FUNDS	£10m per fund	Call

APPENDIX 3

THIRD PARTY LOANS

The Investment Regulations require all loans to third parties to be classified as investments.

The (questionable) rationale behind this is to identify monies utilised in this way, which would otherwise be available for general investment and give rise to investment income.

To comply with the Regulations, the following is presented:-

Category and Context	Outstanding	
	No of loans	**Value £**
(a) Care Home Deferred/Front Funding Payments When a person enters a care home, legislation requires the Council to offer the facility to pay care home fees to avoid a forced house sale. In the case of Deferred Payments, a standard security allows the monies to be recovered in due course. The Council is not allowed to charge interest.	39	854,606
(b) Bike to Work Scheme During the course of 2010/11, the Council launched a "Bike to Work" Scheme to encourage employees to become greener. The scheme provides tax and national insurance savings to employees who obtain bicycles and safety equipment used mainly for cycling to and from work. The scheme provides a loan which is paid over a one year period.	11	765
(c) Owner/Occupiers – High Rise Flats Communal repairs for High Rise blocks of flats e.g. lift refurbishment. Owner/occupiers have deferred their share of costs until such time as flat is sold and thereafter Council will be reimbursed. An Admin Fee for the service is also recharged to owner/occupiers.	15	116,590

APPENDIX 4

LOANS FUND ADVANCES & REPAYMENTS

TOTAL		Years	Years	Years	Years	Years	Years	Years	Years	Years
	2020/21	1-5	6-10	11-15	16-20	21-30	31-40	41-50	51-60	61-65
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Opening Balance	**307.5**	**325.1**	**693.7**	**548.5**	**404.3**	**293.7**	**128.5**	**60.4**	**30.5**	**7.0**
Advances	39.5	483.2	-	-	-	-	-	-	-	-
Repayments	(21.9)	(114.6)	(145.2)	(144.2)	(110.6)	(165.5)	(68.1)	(29.9)	(23.5)	(7.0)
Closing Balance	**325.1**	**693.7**	**548.5**	**404.3**	**293.7**	**128.5**	**60.4**	**30.5**	**7.0**	**-**

GENERAL FUND		Years	Years	Years	Years	Years	Years	Years	Years	Years
	2020/21	1-5	6-10	11-15	16-20	21-30	31-40	41-50	51-60	61-65
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Opening Balance	**135.8**	**141.9**	**240.9**	**184.6**	**132.4**	**90.7**	**24.9**	**3.5**	**-**	**-**
Advances	12.4	142.2	-	-	-	-	-	-	-	-
Repayments	(6.3)	(43.2)	(56.3)	(52.2)	(41.7)	(65.8)	(21.4)	(3.5)	-	-
Closing Balance	**141.9**	**240.9**	**184.6**	**132.4**	**90.7**	**24.9**	**3.5**	**-**	**-**	**-**

HRA		Years	Years	Years	Years	Years	Years	Years	Years	Years
	2020/21	1-5	6-10	11-15	16-20	21-30	31-40	41-50	51-60	61-65
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Opening Balance	**171.2**	**182.7**	**409.4**	**337.2**	**263.8**	**203.0**	**103.6**	**56.9**	**30.5**	**7.0**
Advances	27.1	289.6	-	-	-	-	-	-	-	-
Repayments	(15.6)	(62.9)	(72.2)	(73.4)	(60.8)	(99.4)	(46.7)	(26.4)	(23.5)	(7.0)
Closing Balance	**182.7**	**409.4**	**337.2**	**263.8**	**203.0**	**103.6**	**56.9**	**30.5**	**7.0**	**-**

TIF		Years	Years	Years	Years	Years	Years	Years	Years	Years
	2020/21	1-5	6-10	11-15	16-20	21-30	31-40	41-50	51-60	61-65
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Opening Balance	**0.5**	**0.5**	**43.4**	**26.7**	**8.1**	**-**	**-**	**-**	**-**	**-**
Advances	-	51.4	-	-	-	-	-	-	-	-
Repayments	(0.0)	(8.5)	(16.7)	(18.6)	(8.1)	-	-	-	-	-
Closing Balance	**0.5**	**43.4**	**26.7**	**8.1**	**-**	**-**	**-**	**-**	**-**	**-**