APPENDIX 4

Treasury Management Strategy Statement

1 Background

1.1 The council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the council's low risk appetite, providing adequate liquidity initially before considering investment return.

1.2 The second main function of the treasury management service is the funding of the council's capital plans. These capital plans provide a guide to the borrowing need of the council, essentially the longer-term cash flow planning to ensure that the council can meet its capital spending plans. This management of longer-term cash may involve arranging long or short-term loans or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet council risk or cost objectives.

1.3 The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund balance.

1.4 The Chartered Institute of Public Finance Accountants (CIPFA) defines treasury management as:

"The management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

1.5 Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities (arising usually from capital expenditure) and are separate from the day to day treasury management activities.

Reporting Requirements – Capital Strategy

1.6 The CIPFA revised 2021 Prudential and Treasury Management Codes require, for 2024-25, all local authorities to prepare an additional report, a capital strategy report, which will provide the following:

- a high-level, long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services.
- an overview of how the associated risk is managed.

- the implications for future financial sustainability.

The aim of this capital strategy is to ensure that all elected members of the Full Council understand the overall long term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite. Full Council approved the current Capital Strategy on 31st October 2023.

This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset.

Reporting Requirements – Treasury Management

1.7 The council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

I. **A Treasury Strategy including Prudential and Treasury indicators** (this report) - the first, and most important report covers:
   - the capital plans (including prudential indicators)
   - a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time)
   - the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
   - an investment strategy (the parameters on how investments are to be managed).

II. **A Mid-Year Treasury Management Report** – this will update the council with the progress of the capital position, amending prudential indicators as necessary, and whether the treasury activity is meeting the strategy or whether any policies require revision.

III. **An Annual Treasury Report** – this provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

1.8 The above reports are required to be adequately scrutinised before being recommended to the council. This role is undertaken by the Audit Committee and or Cabinet.

1.9 **Quarterly reports –** in addition to the three major reports detailed above, there is also provision for quarterly reporting (end of June/end of December) on Treasury/Prudential indicators, if required to do so. These additional reports do not have to be reported to Full Council but, there is an expectation that they will be appropriately scrutinised. This role is undertaken by the Audit Committee.

2 Treasury Management Strategy for 2024/25

2.1 The Treasury Management Strategy for 2024/25 covers two main areas:

Capital Issues

- The capital plans and the prudential indicators
- The minimum revenue provision (MRP) policy.

Treasury Management Issues

- current and projected treasury position
- treasury indicators which limit the treasury risk and activities of the council
- prospects for interest rates
- the borrowing strategy
- policy on borrowing in advance of need
- debt rescheduling
- the investment strategy
- creditworthiness policy; and
- policy on the use of external service providers.

These elements cover the requirements of the Local Government Act 2003, DLUHC Investment Guidance, DLUHC MRP Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code.

2.2 The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny with Treasury Management training planned in 2024.

2.3 The training needs of treasury management officers are periodically reviewed.

2.4 The council uses Link Group Treasury Services Limited as its external treasury management advisors. The council recognises that responsibility for treasury management decisions remains with the organisation at all times to avoid any undue reliance being placed upon our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

2.5 The council recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

2.6 The scope of investments within the council’s Treasury operations include the placing of residual cash from the council’s functions in various products such as fixed term deposits, call accounts and money markets with a variety of financial institutions.

3 The Capital Prudential Indicators 2024/25 – 2028/29

3.1 The council’s capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members’ overview and confirm capital expenditure plans.

Capital Expenditure

3.2 This prudential indicator is a summary of the council’s capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. The table also summarises how the capital expenditure plans are being financed. Any shortfall of resources results in a borrowing need. Members are asked to approve the capital expenditure forecasts.

Table 1: Capital expenditure plan and financing

Capital expenditure £m	2022/23 Actual £m	2023/24 Estimate (P8) £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
General Fund	133	165	219	111	59	28	17
HRA	62	109	358	313	233	249	253
Total	**195**	**274**	**577**	**424**	**292**	**277**	**270**
Financed by:							
Capital receipts	26	31	44	27	40	46	40
Capital grants	78	129	215	134	94	38	38
HRA (Self Financing)	33	32	32	32	33	33	34
Revenue	5	30	27	8	4	5	4
Net financing need for year	**53**	**52**	**259**	**223**	**121**	**155**	**154**
General Fund	**53**	**52**	**74**	**37**	**6**	**4**	**1**
HRA	**0**	**0**	**185**	**186**	**115**	**151**	**153**

Note - the table above exclude arrangements such as service-concession contracts including Private Finance initiative (PFI) and finance leases that have their own financing / borrowing facilities.

The council's borrowing need (the Capital Financing Requirement)

3.3 The Capital Financing Requirement (CFR) is the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the council's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR.

3.4 The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with each asset's life, and so charges the economic consumption of capital assets as they are used.

3.5 The CFR includes any long-term liabilities (eg PFI schemes, finance leases). Whilst these increase the CFR, and therefore the council's borrowing requirement, these types of schemes include a borrowing facility and so the council is not required to separately borrow for these schemes. The council currently has £118 million of such schemes within the CFR.

3.6 The council is asked to approve the CFR projections below:

Table 2: Capital Financing Requirement projections

	2022/23 Actual £m	2023/24 Estimate (P8) £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
CFR – non housing	577	615	676	699	690	679	665
CFR – PFI/Lease schemes	118	109	100	91	82	74	67
CFR – housing	245	245	430	615	727	874	1,021
Total CFR	**940**	**969**	**1,206**	**1,405**	**1,499**	**1,627**	**1,753**
Movement in CFR	**24**	**29**	**237**	**199**	**94**	**128**	**126**
Net financing need for year	53	52	259	223	121	155	154
Less MRP & other financing (GF)	(29)	(23)	(22)	(23)	(24)	(23)	(22)
Less MRP & other financing (HRA)				(1)	(3)	(4)	(6)
Movement in CFR	**24**	**29**	**237**	**199**	**94**	**128**	**126**

Liability Benchmark

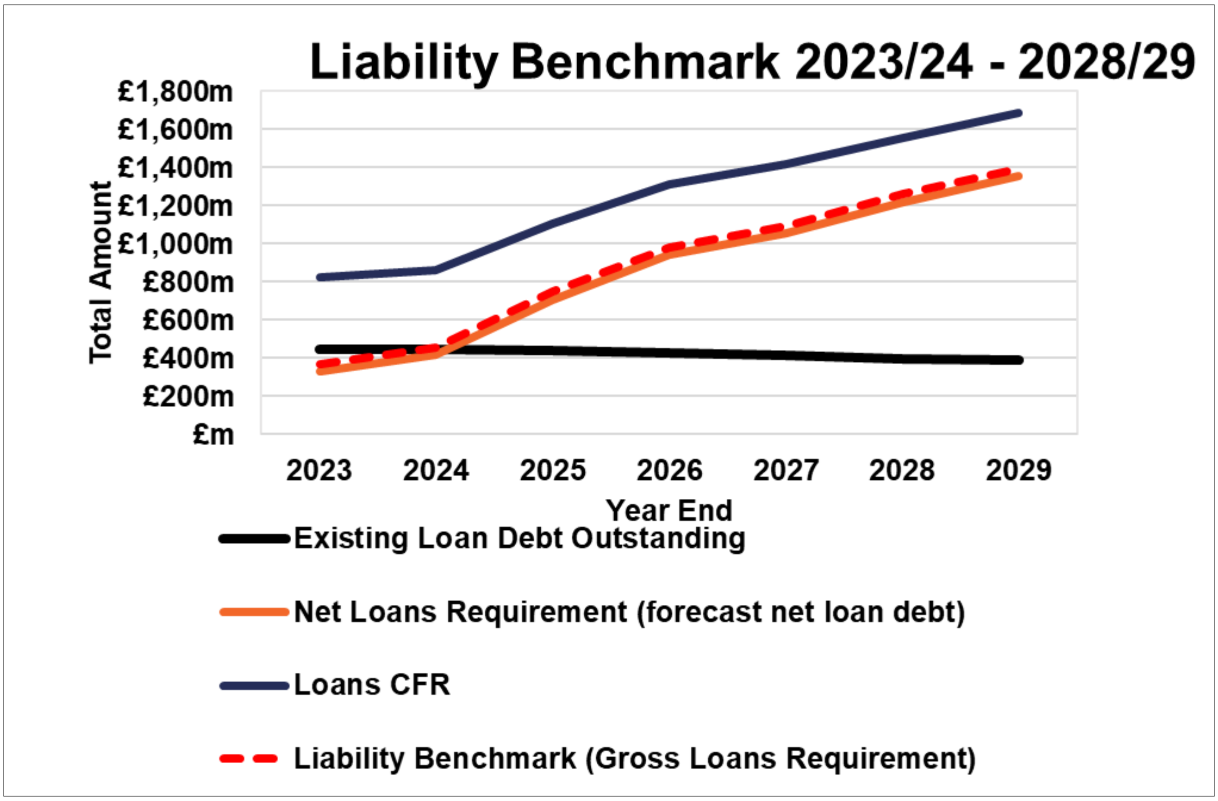
3.7 The Authority is required to estimate and measure the Liability Benchmark for the forthcoming financial year and the following two financial years, as a minimum.

There are four components to the Liability Benchmark: -

- **Existing loan debt outstanding**: the Authority's existing loans that are still outstanding in future years.
- **Loans Capital Financing Requirement (CFR)**: this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned Minimum Revenue Provision.
- **Net loans requirement**: this will show the Authority's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on its approved prudential borrowing, planned Minimum Revenue Provision and any other major cash flows forecast.
- **Liability benchmark** (or gross loans requirement): this equals net loans requirement plus short-term liquidity allowance.

The chart below sets out the four components of the Liability Benchmark.

Figure 1: Liability Benchmark



Minimum Revenue Provision (MRP) policy statement

3.8 The council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge, the minimum revenue provision (MRP), although it is also allowed to undertake additional voluntary provision (VRP).

3.9 The Department for Levelling Up, Housing and Communities (DLUHC) has issued regulations which require Full Council to approve an MRP Statement in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The council is recommended to approve the following MRP Statement:

For capital expenditure incurred before 1 April 2008 and capital expenditure incurred on or after that date which forms part of its Supported Capital Expenditure - The MRP policy will be based on the pre 2007/08 borrowing and post supported borrowing at 2% fixed so that the whole debt is repaid after 50 years.

Note a change in policy approved by Full Council on 13 December 2016 amended the rate that is used to calculate MRP from 4% reducing balance to 2% straight line as this is better aligned to the average lives of the authority's assets and results with the debt being fully repaid. This means that the authority has overprovided during the period 1 April 2008 through to 31 March 2016. The council has reduced its MRP provision in 2017/18 through to 2022/23 to recover this overprovision while also ensuring a prudent annual provision is maintained.

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be the asset life method – MRP will be based on the estimated life of the *assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction);*

Any loan or investment to an organisation defined as capital expenditure will not attract MRP. The original capital expenditure will be met from the capital receipt on the maturity of the loan/investment. However, where there is an expected credit loss or an impairment, the MRP policy will be to include a MRP charge of the same value.
Other methods to provide for debt repayment may occasionally be used in individual cases where this is consistent with the statutory duty to be prudent, as justified by the circumstances of the case, as determined by the Chief Finance Officer.

These options provide for a reduction in the borrowing need over approximately the asset's life.

3.10 There is no requirement on the HRA to make a minimum revenue provision but, there is a requirement for a charge for depreciation.

3.11 Repayments included in annual PFI or finance leases are applied as MRP.

MRP Consultation

3.12 DLUHC is also finalising a consultation on amending the MRP regulations and guidance that is planned to take effect from the 1st April 2024. The outcome of the proposed amendments is not expected to have an impact on the MRP policy proposed above or the estimated annual MRP charge as set out in the medium-term financial plan. Should there be any material change then this will be reported to Audit Committee and within the regular finance monitoring report.

Affordability prudential indicator

3.13 The previous sections cover the overall capital and control of borrowing prudential indicators but, within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the council's overall finances. Council is asked to approve the following indicator:

Ratio of financing costs to net revenue stream. This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

Table 3: Ratio of financing costs to net revenue stream

	2022/23 Actual %	2023/24 Estimate (P8) %	2024/25 Estimate %	2025/26 Estimate %	2026/27 Estimate %	2027/28 Estimate %	2028/29 Estimate %
General Fund	6.5	7.7	7.2	9.1	9.5	9.2	9.1
HRA	6.4	2.2	7.2	13.0	14.7	16.9	19.6

The estimates of financing costs include current commitments and the proposals in this budget report. The HRA is subject to an alternative affordability principle as set out in the Capital Strategy, The HRA thresholds are attributed to an Interest Cover Ratio (ICR) that cannot fall below 1.25 (currently at 1.27) supplemented by minimum reserves in relation to the major repairs reserve of at least £10m and a general HRA reserve of £21m.

4 Borrowing

4.1 The capital expenditure plans set out in Section 3 provide details of the service activity of the council. The treasury management function ensures that the council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the council's capital strategy. This will involve both the management of the daily cash flows and, where capital plans require, the arrangement of appropriate borrowing facilities. The strategy covers the relevant treasury/prudential indicators, the current and projected debt positions and the Annual Investment Strategy.

Current and projected portfolio position

4.2 The council's treasury portfolio position at 31 March 2023, with forward projections, is summarised below. The table shows the actual external debt against the underlying capital borrowing need (the Capital Financing Requirement), highlighting any over- or under-borrowing.

Table 4: Current and projected debt portfolio position

	2022/23 Actual £m	2023/24 Estimate (P8) £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
External Debt 1 April	**451**	**446**	**486**	**801**	**1,036**	**1,164**	**1,337**
Expected change in debt	(5)	40	315	235	128	173	145
Other long-term liabilities	125	118	109	100	90	82	74
Expected change in other long-term liabilities	(7)	(9)	(9)	(10)	(8)	(8)	(8)
Debt Administered on behalf of the Unitary authorities	(36)	(35)	(33)	(32)	(31)	(30)	(28)
Actual gross debt 31 March	**528**	**560**	**867**	**1,094**	**1,215**	**1,381**	**1,520**
Capital Financing Requirement	**940**	**969**	**1,206**	**1,405**	**1,499**	**1,627**	**1,753**
Under borrowing	**(412)**	**(409)**	**(339)**	**(311)**	**(284)**	**(246)**	**(233)**

Gross Debt and the Capital Financing Requirement

4.3 Within the prudential indicators there are a number of key indicators to ensure that the council operates its activities within defined limits. One of these is that the council needs to ensure that its gross debt does not, except in the short term, exceed the total of the

CFR in the preceding year plus the estimates of any additional CFR for 2024/25 and the following two financial years. This allows some flexibility for limited early borrowing for future years but ensures that borrowing is not undertaken for revenue or speculative purposes.

4.4 The Chief Finance Officer reports that the council complied with this prudential indicator in the current year and does not envisage any difficulties for future compliance. This view takes into account current commitments, existing plans, and the proposals in this budget report.

Treasury Indicators: limits to borrowing activity

4.5 **The operational boundary for external debt** - This 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 ability to fund under-borrowing by other cash resources.

4.6 Currently the operational boundary is planned to be lower than the CFR as the council is utilising other cash resources to support the financing of the capital programme, also commonly known as under-borrowing or internal borrowing, as shown in table 5.

Table 5: The Operational Boundary

	2023/24 Approved £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
Debt	546	801	1,036	1,164	1,337	1,482
Other long-term liabilities	116	109	100	90	82	74
Total	**662**	**910**	**1,136**	**1,254**	**1,419**	**1,556**

4.7 **The authorised limit for external debt.** A further key prudential indicator 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 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.

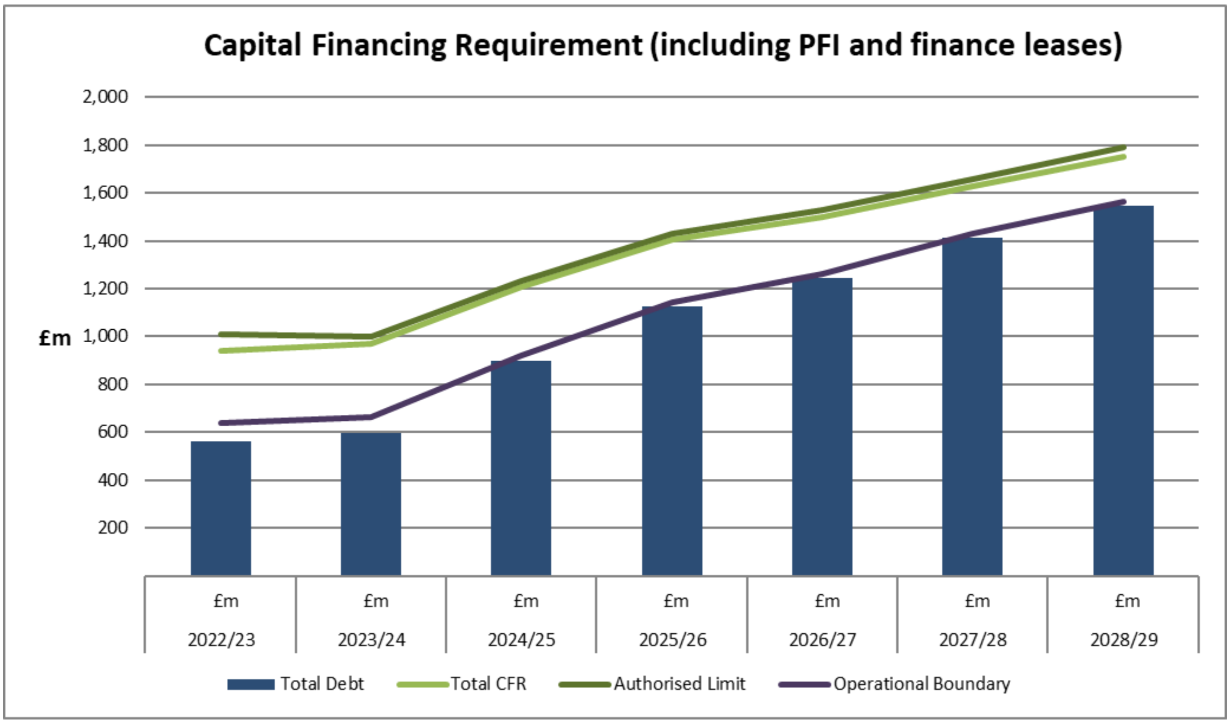
- This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.
- Council is asked to approve the following authorised limit:

Table 6: The Authorised limit for External Debt

	2023/24 Approved £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
Total	**1,000**	**1,230**	**1,430**	**1,530**	**1,660**	**1,790**

A graphical representation of these prudential indicators in relation to the council's projected external borrowing (Gross Debt) and its Capital Financing Requirement are presented below:

Figure 2: Capital Finance Requirement Chart



Prospects for interest rates

4.8 The council's treasury advisors routinely provide information on the prospects for interest rates to support the council in formulating its view on interest rates as set out in the following table.

Table 7: Prospects for Interest Rates

Period	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)			
		5 year	10 Year	25 year	50 year
Mar 2024	5.25	4.90	5.00	5.30	5.10
Mar 2025	4.00	4.20	4.20	4.50	4.30
Mar 2026	3.00	3.60	3.70	4.10	3.90
Mar 2027	3.00	3.50	3.50	4.00	3.80

4.9 The above forecast reflects the view that the Monetary Policy Committee are keen to demonstrate its anti-inflation credentials by keeping Bank Rate at 5.25% until at least September 2024. Rate cuts are expected to start when both the Core Price Inflation (CPI) and wage / employment data are supportive of such a move, and that there is a likelihood of the overall economy enduring at least a mild recession over the coming months,

although most recent Gross Domestic Product (GDP) releases have surprised markets with their on-going robustness.
The timing on this will remain one of fine judgment: cut too soon, and inflationary pressures may well build up further; cut too late, and any downturn or recession may be prolonged.

The above forecast expects the MPC to keep Bank Rate at 5.25% for the first half of 2024 to combat on-going inflationary and wage pressures. The council's treasury advisors do not think that the MPC will increase Bank Rate above 5.25%, but it is a possibility.

As there are so many variables at this time, caution must be exercised in respect of these interest rate forecasts.

Investment and borrowing rates

4.10 **Investment percentage returns** are expected to be similar in 2024/25 due to the expected fall in interest rates over the second half of the year, as inflationary pressures ease.

4.11 **Borrowing interest rates** - the forecast for PWLB borrowing rates show a general downward trend across all maturity bands over the next three years. There is likely to be exceptional volatility and unpredictability in respect of gilt yields and PWLB rates from numerous factors.
There are risks to these forecasts as set out in Annex 2: Economic Forecast and Interest Rate Forecast.

4.12 **Borrowing for capital expenditure**. The long-term (beyond 10 years), forecast for Bank Rate is 3.00%. As the PWLB certainty rates are significantly above 3.00%, there remains value in considering short term / temporary borrowing as these rates are likely to remain near Bank Rate, that is below forecasted PWLB rates over the medium to long term and may also prove attractive as part of having a balanced debt portfolio. It should be noted that HM Treasury have introduced a discounted HRA loan rate for one year from June 2023 with its continuation subject to review. The discount below the PWLB certainty rate that the Council's General Fund has access to is 20 basis points.

The policy of avoiding new borrowing by using spare cash balances has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in the future when authorities may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

There could be a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new long-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.

There are also alternative sources of long-term borrowing available, besides PWLB, if an authority is seeking to avoid a "cost of carry" but also wishes to mitigate future re-financing risk, and these sources will be considered.

Borrowing Strategy

4.13 Based on current cash flow forecasts, it is estimated that the council will have a net borrowing requirement of £996m over the MTFS period. The most significant consideration from a treasury management perspective is the timing and duration of that borrowing. Should the financial environment change and borrowing is deemed advantageous, the council will seek to borrow long-term loans near / below a “target rate” of 4.00% and short to medium term loans near / below the “target rate” of 5.50%.

4.14 The council is forecasting to reduce its under-borrowed position. The under-borrowed position means that the capital borrowing need (the Capital Financing Requirement) has not been fully funded with loan debt as cash supporting the council’s reserves, balances and cash flow has been used as a temporary measure (internal borrowing). This strategy is prudent as medium and longer dated borrowing rates are expected to fall from their current levels once inflation concerns are addressed by tighter near-term monetary policy. That is, the Bank Rate remains elevated through to the second half of 2024.

4.15 Against this background and the risks within the economic forecast, caution will be adopted with the 2024/25 treasury operations. The Chief Finance Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *If it was felt that there was a significant risk of a sharp FALL in borrowing rates,* then borrowing would be postponed.
- *if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast,* perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

4.16 Any decisions will be reported to the appropriate decision-making body at the next available opportunity.

- Long term and short-term fixed interest rates are expected to fall over the medium term. The Chief Finance Officer, under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time, taking into account the risks shown in the Economic Interest Rate Forecast (Annex 2).
- The strategy of postponing borrowing and running down investment balances has been applied in 2023/24. This approach will continue until balances are reduced to adequate liquidity requirements unless it is felt that there is a significant risk of a sharp rise in interest rates.
- The council’s borrowing strategy will consider new borrowing in the following ways:
    - The cheapest borrowing in recent years has been internal borrowing by running down cash balances and foregoing interest earned at historically low rates, however over the past 2 years, investment returns have increased significantly and the savings generated from internal borrowing over the coming year will be negligible.

      In view of the overall forecast for long-term borrowing rates to fall over the medium term, consideration will continue to be given to the short term advantage of internal borrowing while also considering taking short to medium term funding from the PWLB as long term borrowing rates are expected to fall during the medium term.

- Short to medium funding from local authorities and financial institutions at rates lower than the PWLB.
- Short to medium funding from Community Municipal Investments or Retail Bonds for Zero Carbon Initiatives as set out in paragraph 5.1 at rates lower than the PWLB
- PWLB loans for up to 10 years where rates are expected to be lower than rates for longer periods. This offers a range of options for new borrowing, which will spread debt maturities away from a concentration in the longer dated debt that the council holds.
- PWLB loans in excess of 10 years where rates are considered to be low and offer the council the opportunity to lock into low value long-term finance.
- Long term fixed rate market loans at rates significantly below PWLB rates for the equivalent maturity period (where available) and to maintain an appropriate balance between PWLB and market debt in the debt portfolio.
- Long-term borrowing from the Municipal Bond Agency and the UK Infrastructure bank if available and appropriate and the rates are lower than those offered by the Public Works Loan Board (PWLB).
- Financial institutions, primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a “cost of carry” or to achieve refinancing certainty over the next few years.

4.17 The authority is planning net borrowing of £996m over the period, to finance the expected Prudential Borrowing requirement of £912m as set out in in the Capital programme. The higher borrowing of £84m reflects the cash needed to reverse internal borrowing that was undertaken in previous years due to reserves and working capital that is now planned to be utilised during the MTFP period. This is increased further by the cash set aside for the repayment of debt, also known as Minimum Revenue Provision (MRP). The most efficient arrangement is for MRP to be used to reduce the new long-term debt expected to be required. This ensures that MRP is utilised and does not accumulate as cash on the balance sheet and reduces the expected level of debt. Alternatively, MRP could be used to repay existing debt, but this would be a cost to the council in the current interest rate environment.

The level of borrowing will ensure the authority will maintain adequate liquidity levels as set out in the strategy.

4.18 The council will seek to undertake temporary borrowing (less than one year) loans to cover day-to-day cashflow requirements as and when required. Such a decision will be based on the availability of and access to cash in deposit accounts and money market funds to cover the cashflow requirement, whilst also considering the most cost effective method for the authority.

4.19 Temporary borrowing will also be considered when the draw down deadline for a deposit account for same day transfer has passed, thus resulting in borrowing cash from the money markets.

4.20 The Chief Finance Officer will be kept informed of the temporary loans outstanding on a monthly basis and reviewed at the regular Treasury Management Group meeting.

Policy on borrowing in advance of need

4.21 The council will not borrow more than or in advance of its needs purely to invest to make an additional return. Any decision to borrow in advance will be within forward approved

Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that the council can ensure the security of such funds.

4.22 Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

Debt Rescheduling

4.23 As the yield curve is relatively flat there are limited opportunities to generate savings by switching from long term debt to short term debt. In addition, rescheduling of our PWLB loans is unlikely to be beneficial due to how the repayment penalties and discounts are calculated. Any savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

4.24 The reasons for any rescheduling to take place will include:

- the generation of cash savings and / or discounted cash flow savings.
- helping to fulfil the treasury management strategy.
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

4.25 All rescheduling will be reported to the council at the earliest meeting following its action.

4.26 As set out in the capital strategy, the council will seek to reduce its borrowing costs over the strategy's timeframe, by repaying and / or restructuring debt (CFR) to reduce annual debt financing costs to support delivery of services.

The Department for Levelling Up, Housing & Communities has recently published a document requesting a call for views on new local authority capital flexibilities. Included within these flexibilities are the use of disposal proceeds from Investment Estate assets to repay Public Works Loan Board Borrowing without a penalty (where one would otherwise be charged). This could be an opportunity for Council's to repay high coupon debt without penalty, though the loss of investment income will need to be considered. The outcome of any changes will be reported accordingly.

5 Zero Carbon initiatives

5.1 The capital strategy references the council being able to:
....explore zero carbon initiatives funded through Community Municipal Investments or Retail Bonds up to a maximum exposure in such investments of £2m. The exposure to such initiatives would be included within the General Fund capital financing costs exposure of a maximum 10% of the net revenue budget.

5.2 If such an opportunity arose, the council would explore the zero carbon initiative in accordance with this strategy.

6 Annual Investment Strategy

Investment policy

6.1 The Department of Levelling Up, Housing and Communities (DLUHC) and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with financial investments (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets and service investments, are covered in the capital strategy (a separate report approved by Council).

6.2 The council's investment policy has regard to the following:
- DLUHC's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2021 ("the Code")
- CIPFA Treasury Management Guidance Notes 2021.
- Ethical and Equitable Investment Policy (Annex 4)

6.3 The council's investment priorities will be security first, portfolio liquidity second and then yield, (return). The council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and within the council's risk appetite.

6.4 In the current economic climate, it is considered appropriate to maintain a degree of liquidity to cover cash flow needs but to also consider "laddering" investments for periods up to 12 months with high credit rated financial institutions, whilst investment rates remain elevated, as well as wider range fund options.

6.5 The above guidance from DLUHC and CIPFA places a high priority on the management of risk. This council has adopted a prudent approach to managing risk and defines its risk appetite by the following means:
- Minimum acceptable credit criteria are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term credit ratings.
- Credit ratings are collated by our advisors from the major credit rating agencies such as Moody's, S&P and Fitch.
- Other information: credit ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.
- Other information sources used will include the financial press, share price and other such information pertaining to the financial sector, in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.
- The council has defined the list of types of investment instruments that the treasury management team are authorised to use. There are two lists in Annex 3 under the categories of 'specified' and 'non-specified' investments. Counterparty limits are set through the council's treasury management practices – schedules using the parameters below:
    - **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year or those which could be for a longer period but where the council has the right to be repaid within 12 months if it wishes or have less than a year left to run to maturity if originally they were classified as being non-specified investments solely due to the maturity period exceeding one year.

- **Non-specified investments** are those with less high credit quality, maybe for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.
- Counterparty lending limits (amounts and maturity) will be set using the investment criteria below.

Creditworthiness policy

6.6 The primary principle governing the council's investment criteria is the security of its investments, whilst liquidity and the yield on the investment is also a key consideration. After this main principle, the council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the specified and non-specified investment sections below; and
- It has sufficient liquidity in its investments. For this purpose, it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the council's prudential indicators covering the maximum principal sums invested.

6.7 The Chief Finance Officer will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to council for approval as necessary. These criteria are separate to that which determines which types of investment instrument are either specified or non-specified as it provides an overall pool of counterparties considered high quality which the council may use, rather than defining what types of investment instruments are to be used.

6.8 The minimum rating criteria uses the lowest common denominator method of selecting counterparties and applying limits. This means that the application of the council's minimum criteria will apply to the lowest available rating for any institution. For instance, if an institution is rated by two agencies, one meets the council's criteria, the other does not, the institution will fall outside the lending criteria. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer-term change) are considered before making investment decisions.

6.9 The criteria for providing a pool of high-quality investment counterparties (both specified and non-specified investments) is:

- **Banks 1:** good credit quality **–** the council will only use banks which:
  - i. are UK banks; and/or
  - ii. are non-UK and domiciled in a country which has a minimum sovereign long-term rating of AA-

  and have, as a minimum, the following Fitch, Moody's and Standard and Poors credit ratings (where rated):
  - i. Short term – F1 (or equivalent)
  - ii. Long term – A- (or equivalent)
- **Banks 2:** part nationalised UK banks – Royal Bank of Scotland ring-fenced operations. This bank can be included if they continue to be part nationalised or they meet the ratings in Banks 1 above.
- **Banks 3:** the council's own banker for transactional purposes if the bank falls below the above criteria, although in this case balances will be minimised in both monetary size and time.

- **Bank subsidiary and treasury operation:** the council will use these where the parent bank has provided an appropriate guarantee or has the necessary ratings outlined above.
- **Building societies:** the council will use all societies which meet the ratings for banks outlined above.
- **Money market funds (CNAV Constant Net Asset Value):** AAA rated (sterling)
- **Money Market Funds (LVNAV Low Volatility Net Asset Value):** AAA rated (sterling)
- **Money Market Funds (VNAV Variable Net Asset Value):** AAA rated (sterling)
- **Ultra-Short dated Bond Funds with a volatility rating of S1+**
- **UK Government** (including gilts, Treasury Bills and the DMADF)
- **Local authorities, parish councils etc**
- **Supranational institutions**
- **Council owned subsidiaries:** the council invests in wholly owned council subsidiaries. Depending on the nature of the investment this will either be classified as a service investment or a treasury investment. Service investments fall outside the scope of the specified/ non-specified categories and currently investments of this type are classified as service investments.

A limit of £50 million will be applied to the use of non-specified investments.

Country and sector considerations

6.10 Due care will be taken to consider the country, group and sector exposure of the council's investments. The council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch (or equivalent). In addition:

- no more than 25% will be placed with any non-UK country at any time
- limits in place above will apply to a group of companies
- sector limits will be monitored regularly for appropriateness.

6.11 **Use of additional information other than credit ratings.** Additional requirements under the Treasury Management Code require the council to supplement credit rating information. Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making any specific investment decision. This additional market information (for example Credit Default Swaps (CDS), negative rating watches/outlooks) will be applied to compare the relative security of differing investment counterparties.

Time and monetary limits applying to investments

6.12 Time and monetary limits apply to investments. The time and monetary limits for institutions on the council's counterparty list are as follows (these will cover both specified and non-specified investments):

Table 8: Time & monetary limits applying to investments

	Fitch Long term Rating (or equivalent)	Money Limit	Time Limit
Banks 1 - higher quality	*AAA*	£50m	5 Years
Banks 1 - medium quality	*AA-*	£20m	3 Years
Banks 1 - lower quality	*A-*	£10m	1 Year
Banks 2 – part-nationalised	N/A	£10m	1 Year
Limit 3 category – council's banker (not meeting Banks 1/2)	-	£200k	Liquid
Other institutions limit*	-	£50m	5 Years
DMADF	UK Sovereign rating	unlimited	1 Year
Local authorities	-	£40m	5years
Money market funds (MMF) (Including CNAV, LVNAV & VNAV)	AAA	£40m	liquid
Ultra-Short Dated Bond Funds	S1+	£10m	liquid

**The Other Institution Limit will be for Gilt and Supranational investments*

The proposed criteria for specified and non-specified investments are shown in Annex 3 for approval.

6.13 Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (ie rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods.

6.14 The current shape of the yield curve suggests that this is the case at present, with the prospect of Bank Rate having peaked in the second half of 2023 and possibly reducing as early as the second half of 2024, so an agile investment strategy would be appropriate to optimise returns.

6.15 While most cash balances are required in order to manage the fluctuations of the cash flows, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed.

- If it is thought that Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments as being short term or variable.
- Conversely, if it is thought that Bank Rate is likely to fall within that time period, consideration will be given to locking in higher rates currently obtainable, for longer periods.

6.16 **Investment return expectations.**

The current forecast shown in Annex 2 includes a forecast for Bank Rate to have peaked in Q4 2023. The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows (the long term forecast is for periods over 10 years in the future):

- 2023/24 (remainder) 5.30%
- 2024/25 4.70%
- 2025/26 3.20%
- 2026/27 3.00%
- 2027/28 3.25%
- Long term later years 3.25%

As there are many variables at this time, caution must be exercised in respect of these interest rate forecasts.

Treasury management limits on activity

6.17 There are three debt-related treasury activity limits. The purpose of these is to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates
- Maturity structure of borrowing. These gross limits are set to reduce the council's exposure to large, fixed-rate sums falling due for refinancing, and are required for upper and lower limits
- The council is asked to approve the following treasury indicators and limits:

Table 9: Treasury management limits on activity

	2023/24 Upper	2024/25 Upper	2025/26 & Beyond Upper
Limits on fixed interest rates based on net debt	100%	100%	100%
Limits on variable interest rates based on net debt	40%	40%	40%
Maturity structure of fixed interest rate borrowing 2023/24			
		Lower	**Upper**
Under 12 months		0%	40%
12 months to 2 years		0%	40%
2 years to 5 years		0%	40%
5 years to 10 years		0%	50%
10 years and above		25%	100%

Investment treasury indicator and limit

6.18 **Total principal funds invested for greater than 364 days** - These limits are set with regard to the council's liquidity requirements and to reduce the need for early sale of an investment.

Table 10: Investment treasury indicators & limit

Maximum principal sums invested > 365 days (Treasury Investments)			
£m	2024/25	2025/26	2026/27 & Beyond
Principal sums invested > 364 days	£50m	£50m	£50m

6.19 For its cash flow generated balances, the council will seek to utilise its business reserve instant access and notice bank accounts, money market funds and short-dated deposits (overnight to 100 days) in order to benefit from the compounding of interest.

7 Ethical & Equitable Investment Policy

7.1 An updated Ethical and Equitable Investment Policy was approved by Cabinet and Full Council on the 18 January 2022 and 22 March 2022 respectively. The original policy stated the city council will not knowingly invest in organisations whose activities include practices which directly pose a risk of serious harm to individuals or groups, or whose activities are inconsistent with the mission and values of the city council. The updated policy builds on this by taking a more proactive approach to ethical investment and a widening of the policy to promote an equitable approach to investment across all communities in Bristol. It should be noted a core element of the new policy continues to be the application of statutory guidance relating to treasury management funds. A copy of this policy forms part of this report (annex 4).

During the financial year 2023/24, the Council deposited £5m of Treasury balances for 7 months of the year in a strongly rated UK bank at a comparable market interest rate for investment in sustainable development goals including climate change, health, financial inclusion and education.

Investment Risk Benchmarking

7.2 These benchmarks are simple guides to maximum risk, so they may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that officers will monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the mid-year or Annual Report.

7.3 **Security** - The council's maximum security risk benchmark for the current portfolio, when compared to these historic default tables, is:

- 0.04% (AAA rated) to 0.05% (A rated) historic risk of default when compared to the whole portfolio.

Liquidity – in respect of this area the council seeks to maintain:

- Bank overdraft – zero (available upon request).

- Liquid short-term deposits of at least £50m available within a rolling three-month period.
- Weighted average life benchmark is expected to be a minimum of a day with a maximum of 1 year.

Yield - local measures of yield benchmarks are:

- Investments – internal returns above the 7-day SONIA compounded rate (Sterling Overnight Interbank Average).

And in addition, that the security benchmark for each individual year is:

Table 11: Investment risk benchmarking

	1 year	2 years	3 years	4 years	5 years
Maximum	**0.05%**	**0.13%**	**0.24%**	**0.36%**	**0.50%**

This benchmark is an average risk of default measure and would not constitute an expectation of loss against a particular investment.

Annexes

Annex 1 - Treasury Management Policy Statement
Annex 2 – Economic Interest Rate Forecast
Annex 3 – TMP1 Credit and Counterparty Risk Management
Annex 4 – Ethical and Equitable Investment Policy

Annex 1

Treasury Management Policy Statement

1. The council defines its treasury management activities as follows:

   The management of the council's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.

2. The council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the council, and any financial instruments entered into to manage these risks.

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

4. The council's high-level policies for borrowing and investments are:

   - 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

   - 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.

Annex 2

Economic Interest Rate Forecast

Table 1 – Interest Rate Forecast

Link Group Interest Rate View	07.11.23												
	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
BANK RATE	5.25	5.25	5.25	5.00	4.50	4.00	3.50	3.25	3.00	3.00	3.00	3.00	3.00
3 month ave earnings	5.30	5.30	5.30	5.00	4.50	4.00	3.50	3.30	3.00	3.00	3.00	3.00	3.00
6 month ave earnings	5.60	5.50	5.40	5.10	4.60	4.10	3.60	3.40	3.10	3.10	3.10	3.10	3.10
12 month ave earnings	5.80	5.70	5.50	5.20	4.70	4.20	3.70	3.50	3.30	3.30	3.30	3.30	3.30
5 yr PWLB	5.00	4.90	4.80	4.70	4.40	4.20	4.00	3.80	3.70	3.60	3.50	3.50	3.50
10 yr PWLB	5.10	5.00	4.80	4.70	4.40	4.20	4.00	3.80	3.70	3.70	3.60	3.60	3.50
25 yr PWLB	5.50	5.30	5.10	4.90	4.70	4.50	4.30	4.20	4.10	4.10	4.00	4.00	4.00
50 yr PWLB	5.30	5.10	4.90	4.70	4.50	4.30	4.10	4.00	3.90	3.90	3.80	3.80	3.80

The forecasts for average earnings are averages ie rates offered by individual banks may differ significantly from these averages, reflecting their different needs for borrowing short term cash at any one point in time.

The central interest rate forecast reflects a view that the MPC are keen to further demonstrate its anti-inflation credentials by keeping Bank Rate at 5.25% until at least the middle of 2024. Rate cuts are expected to start when both the CPI inflation and wage/employment data are supportive of such a move, and that there is a likelihood of the overall economy enduring at least a mild recession over the coming months, although most recent GDP releases have surprised with their on-going robustness.

The timing on this will remain one of judgment: cut too soon, and inflationary pressures may well build up further; cut too late and any downturn or recession may be prolonged.

In the coming months, forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but also international factors such as policy development in the US and Europe, the provision of fresh support packages to support the faltering recovery in China as well as the on-going conflict between Russia and Ukraine, and Gaza and Israel.

On the positive side, consumers are still anticipated to be holding onto excess savings left over from the pandemic, which could cushion some of the impact of the above challenges and may be the reason why the economy is performing somewhat better at this stage of the economic cycle than may have been expected. However, most of those excess savings are held by more affluent households whereas lower income families already spend nearly all their income on essentials such as food, energy and rent/mortgage payments.

PWLB RATES

PWLB rates are expected to fall by circa 1.5% across all maturity periods during the next 3 years with 5 to 50 years PWLB rates operating within a narrow band of circa 0.50%.

The balance of risks to the UK economy: -

- The overall balance of risks to economic growth in the UK is to the downside.

Downside risks to current forecasts for UK gilt yields and PWLB rates include: -

- **Labour and supply shortages** prove more enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, could keep gilt yields high for longer).

- **The Bank of England** has increased Bank Rate too fast and too far over recent months, and subsequently brings about a deeper and longer UK recession than we currently anticipate.

- **UK / EU trade arrangements** – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.

- **Geopolitical risks,** for example in Ukraine/Russia, the Middle East, China/Taiwan/US, Iran and North Korea, which could lead to increasing safe-haven flows.

Upside risks to current forecasts for UK gilt yields and PWLB rates: -

- Despite the recent tightening to 5.25%, the **Bank of England proves too timid** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to remain elevated for a longer period within the UK economy, which then necessitates Bank Rate staying higher for longer than we currently project.

- **The pound weakens** because of a lack of confidence in the UK Government's pre-election fiscal policies, resulting in investors pricing in a risk premium for holding UK sovereign debt.

- Longer-term **US treasury yields** rise strongly if inflation remains more stubborn there than the market currently anticipates, consequently pulling gilt yields up higher. (We saw some movements of this type through October although generally reversed in the last week or so.)

- Projected **gilt issuance, inclusive of natural maturities and QT,** could be too much for the markets to comfortably digest without higher yields compensating.

Borrowing advice: Our long-term (beyond 10 years) forecast for Bank Rate has increased from 2.75% to 3% and reflects Capital Economics' research that suggests AI and general improvements in productivity will be supportive of a higher neutral interest rate. As all PWLB certainty rates are currently significantly above this level, borrowing strategies will need to be reviewed in that context. Overall, better value can generally be obtained at the shorter end of the curve and short-dated fixed LA to LA monies should be considered. Temporary borrowing rates will remain elevated for some time to come but may prove the best option whilst the market continues to wait for inflation, and therein gilt yields, to drop back later in 2024.

Annex 3

Treasury Management Practice (TMP1) – Credit and Counterparty Risk Management

The DLUHC issued Investment Guidance in 2018, and this forms the structure of the council's policy below. These guidelines do not apply to either trust funds or pension funds, which operate under a different regulatory regime.

The key intention of the Guidance is to maintain the current requirement for councils to invest prudently, and that priority is given to security and liquidity before yield. In order to facilitate this objective, the guidance requires this council to have regard to the CIPFA publication Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. The council has adopted the Code and will apply its principles to all investment activity. In accordance with the Code, the Chief Finance Officer has produced its treasury management practices (TMPs). This part, TMP 1(1), covering investment counterparty policy requires approval each year.

Annual investment strategy - the key requirements of both the Code and the investment guidance are to set an annual investment strategy, as part of its annual treasury strategy for the following year, covering the identification and approval of the following:

- The strategy guidelines for choosing and placing investments, particularly non-specified investments.
- The principles to be used to determine the maximum periods for which funds can be committed.
- Specified investments that the council will use. These are high security (i.e. high credit rating, although this is defined by the council, and no guidelines are given), and high liquidity investments in sterling and with a maturity of no more than a year.
- Non-specified investments, clarifying the greater risk implications, identifying the general types of investment that may be used and a limit to the overall number of various categories that can be held at any time.

The investment policy proposed for the council is:

Strategy guidelines – the main strategy guidelines are contained in the body of the treasury strategy statement.

Specified investments – these investments are sterling investments of not more than one-year maturity, or those which could be for a longer period but where the council has the right to be repaid within 12 months if it wishes. They also include investments which were originally classed as being non-specified investments, but which would have been classified as specified investments apart from originally being for a period longer than 12 months once the remaining period to maturity falls to under twelve months. These are considered low risk assets where the possibility of loss of principal or investment income is small. These would include sterling investments which would not be defined as capital expenditure with:

1. The UK Government (such as the Debt Management Account deposit facility, UK treasury bills or a gilt with less than one year to maturity).
2. Supranational bonds of less than one year's duration.
3. A local authority, housing association, parish council or community council.
4. Pooled investment vehicles (such as money market funds) that have been awarded a high credit rating by a credit rating agency. For category 4 this covers pooled investment vehicles, such as money market funds, rated AAA by Standard and Poor's, Moody's or Fitch rating agencies.

5. A body that is considered of a high credit quality (such as a bank or building society). For this category this covers bodies with a minimum short term rating of A- (or the equivalent) as rated by Standard and Poor's, Moody's or Fitch rating agencies.

Within these bodies, and in accordance with the Code, the council has set additional criteria to set the time and amount of monies which will be invested in these bodies. These criteria are set out below: -

Table 1 – Specified Investment Limits

	Fitch Long term Rating (or equivalent)	Money Limit	Time Limit
Banks 1 higher quality	*AAA*	£50m	5 Years
Banks 1 medium quality	*AA-*	£20m	3 Years
Banks 1 lower quality	*A-*	£10m	1 Year
Banks 2 – part nationalised	N/A	£10m	1 Year
Limit 3 category – council's banker (not meeting Banks 1/2)	-	£200k	Liquid
Other institutions limit*	-	£50m	5 Year
DMADF	AAA	unlimited	5 Years
Local authorities	-	£40m	5 Years
Money market funds (Including CNAV, LVNAV & VNAV)	AAA	£40m	Liquid
Ultra-Short Dated Bond Funds	S1+	£10m	liquid

**The Other Institution Limit will be for Gilt and Supranational investments*

Non-specified investments – are any other type of investment (ie not defined as specified above). The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out below. Non specified investments are limited to an overall exposure of £50m and would include any sterling investments with:

Table 2 – Non-Specified Investments Limits

	Non-Specified Investment Category	Limit (£ or %)
a.	**Supranational bonds greater than 1 year to maturity** **(a) Multilateral development bank bonds** - These are bonds defined as an international financial institution having as one of its objects economic development, either generally or in any region of the world (e.g. European Reconstruction and Development Bank etc.). **(b) A financial institution that is guaranteed by the United Kingdom Government** (e.g. National Rail) The security of interest and principal on maturity is on a par with the Government and so very secure. These bonds usually provide returns above equivalent gilt-edged securities. However, the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.	AAA long term ratings £50m
b.	**Gilt edged securities** with a maturity of greater than one year. These are Government bonds and so provide the highest security of interest and the repayment of principal on maturity. Similar to category (a) above, the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.	£50m
c.	**The council's own banker** if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as is possible.	Minimal
d.	Any **bank or building society** that has a minimum long-term credit rating of A-, for deposits with a maturity of greater than one year (including forward deals in excess of one year from inception to repayment).	£40m
e.	Any **non-rated subsidiary** of a credit rated institution included in the specified investment category. These institutions will be included as an investment category subject to: • Parent company guarantee • Parent company to be a UK institution.	£10m
f.	**Share capital** in a body corporate – The use of these instruments will be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. **Loan capital** in a body corporate. There is a higher risk of loss with these types of instruments.	£10m
g.	**Share capital to council owned companies** – The use of these instruments will be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. **Loan capital** to council owned companies	£50m
h.	**Bond funds** – There is a high risk of loss with this type of instrument.	£10m

i.	**Pooled property funds** – The use of these instruments will normally be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. The key exception to this is an investment in the CCLA Local Authorities Property Fund. This Authority will seek guidance on the status of any fund it may consider using.	£50m
j.	**Property funds managed by a wholly owned council subsidiary** – The use of these instruments will normally be deemed to be capital expenditure, and as such will be an application (spending) of capital resources.	£50m

In respect of categories f and h, these will only be considered after obtaining external advice and subsequent member approval.

Council owned companies - the council has purchased share capital / provided loans to wholly owned council subsidiaries. These are classified as service investments, rather than treasury management investments, and are therefore outside the specified / non specified categories.

The monitoring of investment counterparties - the credit rating of counterparties will be monitored regularly. The council receives credit rating information (changes, rating watches and rating outlooks) from Link Group as and when ratings change, and 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.

Annex 4

Bristol City Council Ethical and Equitable Investment Policy

Date published: Cabinet 18th January 2022

Contents

Purpose

The purpose of this policy statement is to provide guiding principles to ensure Bristol City Council ("the council") make investments which:

- are consistent with the council's values framework and ethical policies (ethical)
- are inclusive and equitable with regards to access to the council's investment funding, as well as helping to address economic inequalities (equitable)
- provide a positive social and/or environmental return, in other words have "impact", alongside financial return where possible

This policy should be regarded as a baseline when making decisions. It is in no way intended to limit projects that seek to tackle different council objectives in a joined up and innovative way.

Aim

The aim is to use the council's investments to support the council's vision in playing a leading role in driving an inclusive, sustainable and healthy city of hope and aspiration, one where everyone can share in its success, in line with the council's corporate strategy and the One City Plan.

To this end, the policy sets out investment principles which mainly based on three aspects:

- who the council will not invest in (ethical review 1)
- who the council want to invest in (ethical review 2)
- how the council will ensure investments are equitable (equitable principles)

These principles are outlined in more detail within the sections ethical review 1, ethical review 2 and equitable principles.

Legislative and Policy Context

Local authority investments are governed by the Statutory Guidance on Local Government Investments [1], and the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management Code [2]. This is set out in further detail in the council's annual Treasury Management Strategy.

This policy is also complemented by the council's Equality and Inclusion Policy and Strategy; its Social Value policy; and its commitments to payment of the Living Wage and eradicating modern slavery.

Strategic Alignment

This policy statement aligns to the One City Plan's 'Corporate Strategy and A One City: Economic Recovery and Renewal Strategy' which sets out the following priorities:

- Reduce poverty and inequality
- Increase the city's resilience and environmental sustainability
- Enhance community economic and social wellbeing

In addition, the positive environmental criteria's have been identified with reference to the One City Climate Strategy.

Investment Principles

The council's Ethical and Equitable Investment policy ensures that investments made will embed the following investment principles:

[1] Statutory Guidance on Local Government Investments, 3rd edition - https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/678866/Guidance_on_local_government_investments.pdf

[2] CIPFA: "Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes, 2017 Edition

Principle 1: We will be active owners and incorporate ethical and equitable issues into our investment policies and practices, making sure investments or loans support the council's policies and objectives on such matters

Principle 2: We will not knowingly undertake direct investments or loans to organisations whose core activities or behaviour include practices which directly pose a risk of serious harm to individuals, groups or the environment or are inconsistent with the mission and values of the council

Principle 3: We will aspire to make investments that achieve positive social and/or environmental benefit and impact within Bristol alongside financial return

Principle 4: We will seek investees who incorporate ethical and equitable practises into their business practises. Where appropriate, we will actively engage with investees and use our influence to encourage ethical standards, practices, and lines of business acceptable to the council

Principle 5: We will incorporate equitable principles into our investment policy, to ensure investments reach and benefit disadvantaged groups and communities experiencing greatest inequity and who are typically under-represented when receiving investment

Principle 6: When current service investments or loans mature and funds are returned to the council, where appropriate we will consider recycling those funds back into investments that deliver ethical and equitable impact

Principle 7: We will explore different ways of working to improve our systems and procedures and remove barriers. This includes collaborative working and partnerships with co-investors and intermediaries to help manage risk and enhance opportunities to deliver positive social and environmental impact, as well as support equitable access to investment

Principle 8: Where practical, we will seek disclosure on positive impact regarding ethical and equitable issues by the entities in which we invest

Principle 9: We will report on our activities and progress towards implementing these Principles

Scope

The council holds three types of investments:

- Treasury investments, which are short to medium-term investments to manage surplus cash
- Service investments, which are investments made primarily for service benefit or impact - for example investment in a subsidiary and
- Service loans, which are loans made primarily for service benefit or impact - this does not include loans to another local authority as these are categorised as treasury investments.

Whilst grant investments do not fall within the statutory definition of investments as these are not expected to generate profits, due regard to this policy statement should be made when making a decision on grant investments.

The council's pension fund is held with the Avon Pension Fund administered by Bath and North East Somerset Council. The scheme's funds are invested entirely separately from those of the council, has its own policy for Responsible Investment and are subject to separate regulatory regimes to local authority investments. They are therefore not directly governed by this policy. However, the policy can be used to inform the views of the council's pension representative who feeds into matters such as the pension funds' Responsible Investment policy.

Ethical Review 1

This first ethical review ensures that the council does not knowingly undertake direct investment or borrowing activities with organisations/Sovereigns whose behaviour or core activities are deemed unethical. This may be controversial business practices which directly pose a risk of serious harm to individuals, groups or the environment, corporate behaviour which is in serious violation of widely accepted international norms, or core activities and behaviour which are inconsistent with the mission and values of the council.

This review applies to direct investments only, except in the case where the council has invested in an intermediary specifically to deploy investments and deliver impact. The council cannot guarantee approved financial institutions will not have clients or branches/offices/subsidiaries in countries that may breach the exclusions list.

In some instances, the council may allow the counterparty time to achieve compliance over a reasonable timeframe, taking into consideration the risks and opportunities specific to that business and its size and resources. The council will only proceed with investment if we anticipate that the requirements of the policy will be met within the given timeframe. Any persistent delays in meeting the requirements would result in the council taking remedial action, which could be to cease funding or exit the investment.

Exclusion List

As part of this review, the council will exclude from consideration where there are consistent or significant transgressions of the appropriate regulatory framework or a failure to ignore directions of the regulatory body, investments in counterparties which have significant involvement with any of the activities or business practises on the following exclusions list:

Human Rights and Labour

- breaches of human rights principles
- breaches of international labour standards
- supports/are part of oppressive regimes
- modern slavery
- poor Health and Safety records

Environment

- toxic spills and releases
- negative impact on land use, habitats and biodiversity
- contributes to carbon intensive industries
- causes water resource scarcity
- poor supply chain management
- animal testing for cosmetic purposes / unnecessary exploitation of animals

Governance

- bribery/ fraud/ corruption
- violation of international intellectual property rights
- unethical market behaviour and business practise - for example, blocking competition

Controversial Business Activities

- alcohol – relating to manufacture, supply and distribution of alcoholic beverages
- gambling – relating to owning and/or operation of gambling establishments
- tobacco – relating to production, retail, distribution, or supply of tobacco products
- adult entertainment, such as pornography or violent material – relating to distribution and retail of adult entertainment products and/or services
- military or controversial weapons (Arms trade) – relating to manufacture or distribution of weapons
- fossil Fuel extraction
- nuclear industries
- exploitative credit providers – where credit has APR > 100% and provided in way that leads to significant harm to consumers
- third world debt exploitation

Other – for non-treasury investments only

- investments that don't generate any benefits within Bristol

Ethical Review 2

Where practical and applicable, we will prioritise investments that provide positive social or environmental impact by assessing whether they meet the positive criteria listed here. We will also prioritise those which will deliver the most impact (high impact return) and have greatest likelihood of delivering impact (low impact risk). The glossary provides more detailed definitions.

The positive criterions are not an exhaustive list as priorities and policies may change, but they provide a baseline for making investment decisions. Such investments are typically riskier and require longer term investment. Therefore, we will take a balanced portfolio approach, maximising the number of investments that provide positive social and/or environmental impact whilst balancing this with financial risk and return considerations.

Balanced Portfolio Approach

A balanced portfolio approach will enable the council to have a portfolio of investments that range from investments that deliver no impact but are less financially risky or more liquid (in other words accessible), to investments that deliver impact but are typically more financially risky or less liquid.

Impact is articulated through “Impact return”, the positive measurable impact generated and “Impact risk”, the likelihood that the investment does not achieve the desired impact. Whilst the aim is to transition our investments towards those that deliver impact, having a range of investments helps to diversify and thus reduce financial risk and liquidity issues.

In addition to managing risk, the balanced portfolio will also balance investments that address a range of challenges, from environmental issues to inequality. Appendix 1 sets out a table showing the spectrum of investments within the balanced portfolio, with investments providing greater impact to the right of the table.

This approach, which will be evaluated continuously, is preferable to setting percentage or monetary targets for investment, as this gives greater flexibility to respond to changes in priorities, economic outlook or the investment market as the responsible treasury investment market is still in the early stages of development.

Positive Criteria for Treasury Investments

The following positive criteria will be used to determine whether an investment is given greater priority when considering a range of investments to invest in. For treasury investments, whether priority is given based on positive criteria will need to be balanced against trade-off on yield since this could impact on the council’s ability to deliver services.

Where practical, ESG (Environmental, Social and Governance) investments that specifically fund ESG-related projects will be favoured over Responsible and Sustainable investments as the former provides direct impact whereas the latter is indirect. Greater priority will be given to investments with local impact and organisations that are living wage employers. Criterion outlined below carrying greater weighting is marked with an asterix*.

Responsible and Sustainable

- *counterparty pays Living Wage
- counterparty has ESG (environmental, social and governance) or Responsible Investment policy
- counterparty has Diversity and Inclusion policy
- counterparty is involved in projects addressing ethical or equitable issues - for example, runs free business support training for SMEs

*ESG Investments

- *investment specifically funds ethical and equitable projects locally within Bristol area
- investment specifically funds ethical and equitable projects - for example, funds renewable energy or SME businesses in deprived areas

Positive Criteria for Service Investments/Loans

The following positive criterion will be used to determine whether an investment is given greater priority when considering a range of investments to invest in. Some criteria carry greater weighting, indicated with an asterix*, for example, because they support the equitable investment principles. The criteria will be considered alongside the balance of portfolio, impact return, impact risk and alignment with current priorities as set out in the Corporate Strategy.

We will refer to the Social Value policy, National Social Value Measurement Framework, the TOMs, as a means for measuring and scoring impact return.

Reduce Poverty and Inequality

- *targets geographical areas with deprivation or other marker for inequality such as income disparity or ethnicity
- *targets population groups known to be economically disadvantaged or under-represented when receiving investments
  Both the above criteria will be linked to the Social Value policy
- *pays Living Wage
- supports tackling homelessness
- supports local employment

- supports the creation and retention of high-quality, sustainable jobs for local people

Increase the City's Resilience and Environmental Sustainability

- *the investment will lead to carbon emissions being reduced – supporting Bristol's Net Zero by 2030 target
- is a responsible buyer of goods and services
- provides jobs and skills related to the green economy
- improves ecology and biodiversity, within Bristol or elsewhere
- contributes to resilient food supply chain, with food and drink produced sustainably

Enhance Community Economic and Social Wellbeing

- *Bristol based investments - local investments focussed on creating impact in the city region, which in turn should create additional economic value in the area
- supports creation, sustainability and growth of micro, small and medium-sized enterprises
- supports local people with opportunities for life-long learning, skills development and experiences of work
- supports the creation, sustainability and growth of local community groups, voluntary groups and social enterprises
- promotes the involvement of local people and organisations in active citizenship such as volunteering and foster caring
- promotes the mental and physical health and well-being of local people
- supports the creation of high quality, affordable and sustainable homes and inclusive public spaces
- investment catalyses further investment into Bristol

Equitable Principles

The equitable investment principles enable investments to be used as a lever to help address equality issues affecting disadvantaged groups and communities in Bristol. The investments are intended to be inclusive and accessible to all.

Principles

We will ensure investments are equitable by applying the following principles:

Engaging with local groups

We will identify and engage with local disadvantaged and under-represented groups to make sure there is awareness of investment opportunities and to build confidence and ability for such groups to apply successfully for investment.

This could be through direct engagement with local communities or indirectly through intermediaries, linking with outreach programmes in order to maximise engagement reach with under-represented groups.

Targeting investment

Through our investment we will empower communities that experience the greatest inequity. We will place greater weighting on investments which invest in communities and enable greater self-determination. By investing in this way, we are building civic and social capital.

We will also favour investments that deliver positive impact around equality issues affecting Bristol, placing greater priority on those that deliver direct impact, but also recognising that some investments will have indirect impact. For instance, investment which reduces pollution could also address inequalities as less wealthier communities tend to live in areas of higher pollution [3].

Improving success

We will endeavour to identify and remove barriers that prevent local disadvantaged and under-represented groups from applying and being successful in securing investments. This may include providing support and training so those groups have equal opportunity of success when applying for investments or looking at alternative means of investments, such as asset transfers.

[3] Environmental inequality must not be ignored - GOV.UK (www.gov.uk)

Collecting and monitoring equalities data

We collect equalities data specifically around investments to improve our intelligence and ensure we monitor and track progress towards making investment more equitable. Data will also ensure that our targeted investment approach is focussed on the correct areas and groups.

Governance

In order to give effect to its commitment to this policy the council will:

- apply this policy at the point of investment
- monitor investments thereafter, to review the operation and effectiveness of the policy, including any setting of annual targets
- report progress annually, including any breaches, within the annual Treasury Management Outturn Report

Investment Breaches - Ethical Review 1

Where a counterparty is found in breach of the exclusions list under ethical review 1, the council will look to divest. Any outstanding investments will be reviewed in accordance with the terms and conditions of the contractual arrangement. A cost benefit appraisal will be undertaken to minimise the cost of prematurely redeeming the investment.

Depending on the nature of the breach and the investment, the council may enter into dialogue with the counterparty to allow the counterparty the opportunity and time to address the breach. If the breach is not addressed within a given timescale or the counterparty is not seen to be making any progress, then the council would look to divest.

The Chief Finance Officer, Cabinet Member for Finance and the council's Treasury Management Advisors will be consulted when a breach of the exclusions list has been identified and breaches will be reported through the Treasury Management Outturn Report.

Glossary

Impact return	The positive, measurable social and environmental impact generated by the investment alongside any financial return, such as those outlined in the list of positive criteria under ethical review 2 or in the council's corporate strategy.
Impact risk	The risk that the investment does not achieve the desired impact. The likelihood that impact will be different than expected, and that the difference will be material from the perspective of the people and the planet who experience such impact.
Service investments	These are investments made primarily for service benefit or impact. Like treasury investments, these are also subject to financial risk considerations around security, liquidity and yield, but these are secondary concerns to service benefit or impact. Service investments could be investments in impact funds, wholly owned subsidiaries or in non-financial assets such commercial property.
Service loans	These are loans repayable with interest made to a third party, joint venture, subsidiary or associates. Like service investments, these are made primarily for service benefit or impact, with financial risk considerations around security, liquidity and yield being secondary. This does not include loans to another local authority as these are categorised as treasury investments.
Treasury Investments	These are investments made using treasury powers under section 15(1)(a) of the Local Government Act 2003 to manage surplus cash. These are typically short-term investments (duration of less than one year), as cash must be accessible as and when

payments need to be made by the organisation. Hence security followed by liquidity are primary financial considerations for local authority treasury investments, as stipulated by the Treasury Management Code. Yield is also a consideration, after security and liquidity, as greater yield means more funding for the council's services. Due to the restrictions set out in the Treasury Management Code, treasury investments are typically with financial institutions such as banks, building societies and money market funds.

Appendix - Balanced Investment Portfolio

Greater positive social and/or environmental impact

Treasury Investments *Service investments/loans* *Grants*

	Classic Investment	**Responsible and Sustainable**	**ESG investment**	**Classic Investmen t**	**Service Investment**	**Grants**
Purpose	**Invest primarily for financial return**			**Invest primarily for Service impact/benefit**		
Description	Investment focuses on SLY only	Investment incorporates ESG into its investment approach	Investment has direct impact on environmental , social or governance (ESG) issues	Invest for indirect social benefit/ impact	Invest for direct social benefit/ impact	Invest for service/ social benefit only (no profit)
Financial risk (security)	Low	Low	Low	Medium	Medium - High	N/A
Liquidity risk (liquidity)	Low	Low	Low	High	Medium - High	N/A
Financial return (yield)	Medium - Low	Medium - Low	Low (often lower vs classic)	Medium - High	Low - High	N/A
Impact risk	High	High	Medium	Medium	Low	Low
Impact return	Low	Low	Medium	Medium	High	High
Examples	Standard treasury investments	For example, Investment counterparty has an ESG or Responsible investment policy	For example, ESG investment that specifically funds environmental projects	For example, Commerci al property	For example, Loan to Community bank	For example, Community Resilience Fund

Figure 3 - Table illustrating balanced portfolio of investments and associated financial and impact risks and returns