South Downs National Park Authority

Agenda Item 10
Report PR19/20-32

Report to	**Policy & Resources Committee**
Date	**27 February 2020**
By	**Chief Finance Officer / Head of Business Services**
Title of Report **(Decision)**	**Treasury Management Strategy 2020/21**

Recommendation: The Committee is recommended to :

1) **Recommend that the National Park Authority ("NPA") approves the Treasury Management Strategy 2020/21 document as set out in Appendix 1 comprising of:**
   - **Treasury Management Policy Statement 2020/21;**
   - **Treasury Management Practices 2020/21;**
   - **Borrowing Strategy 2020/21;**
   - **Prudential and Treasury Indicators 2020/21 to 2024/25;**
   - **Minimum Revenue Provision Policy Statement; and**
   - **Annual Investment Strategy 2020/21, including the benchmark risk factor of 0.05%.**

1. Introduction

1.1 Part 1 of the Local Government Act 2003 requires the Authority to adopt and comply with requirements issued by the Chartered Institute of Public Finance & Accountancy (CIPFA) and investment guidance issued by the Secretary of State. This report is presented in order to comply with the requirements of:

- CIPFA Code of Practice on Treasury Management in the Public Services;
- The CIPFA Prudential Code for Capital Finance in Local Authorities; and
- The Ministry of Housing, Communities and Local Government (MHCLG) Guidance on Local Government Investments and Minimum Revenue Provision.

1.2 In accordance with Financial Procedures, Policy and Resources Committee will receive an annual strategy on treasury management policies, practices and activities in advance of the financial year for recommendation to the Authority.

1.3 This report proposes the Treasury Management Strategy 2020/21 document as set out in **Appendix 1** comprising of:

- Treasury Management Policy Statement 2020/21;
- Treasury Management Practices 2020/21;
- Borrowing Strategy for 2020/21;
- Prudential and Treasury Indicators 2020/21 to 2024/25;

- Minimum Revenue Provision Policy Statement; and
- Annual Investment Strategy 2020/21, including the benchmark risk factor of 0.05%.

1.4 Some of the above policies and statements were previously presented as separate documents; however, with the inclusion of new statements, they have all been incorporated into one treasury management strategy document to ensure that interrelated financial decisions and strategies can be considered together.

2. Policy Context.

2.1 There are no direct policy implications within this report.

3. Issues for consideration

Treasury Management Policy Statement and Practices 2020/21

3.1 The Code of Practice on Treasury Management published by CIPFA ("the Code") has been produced to satisfy a number of key purposes for treasury management including:

- to assist in the development and maintenance of firm foundations and clear objectives;
- to emphasise the overriding importance of effective risk management as the foundation;
- to encourage the pursuit of value for money;
- to help facilitate the standardisation and codification of policies and practices.

3.2 The Treasury Management Policy Statement and Practices set out in sections 2 and 3 of Appendix 1 comply with the requirements of the Code. All monies will be invested by the Authority's treasury team and investment income will be reported as part of quarterly monitoring.

Borrowing Strategy

3.3 The Treasury Management Strategy incorporates a Borrowing Strategy, Prudential and Treasury Indicators and a Minimum Revenue Provision Policy Statement as set out in sections 4, 5 and 6 of Appendix 1. The inclusion of these documents reflects the anticipated requirement of the Authority to undertake borrowing to meet its capital funding requirement.

3.4 A key function of treasury management is to ensure that the Authority's capital plans are appropriately funded by managing the longer-term cash flow requirements. The borrowing strategy identifies the anticipated borrowing need to meet capital plans, whilst focusing on meeting this borrowing need from internal borrowing where possible i.e. avoiding external borrowing by utilising the Authority's own surplus cash flow. This will reduce the net revenue cost of borrowing and reduce counterparty risk within the Authority's investment portfolio by reducing the portfolio size. The balance between internal and external borrowing will be continuously reviewed giving consideration to long term interest rate forecasts and the cost of carry (the difference between borrowing costs and investment rates) to reduce the risk of revenue loss between borrowing costs and investment returns.

3.5 The Authority is required to 'have regard to' the Prudential Code and to set up Prudential Indicators to ensure that the Authority's capital investment plans are affordable, prudent and sustainable. The Code sets out the indicators that must be used. Alongside additional indicators set to measure treasury performance. The Treasury Indicators have been calculated and determined by officers in compliance with the Treasury Management Code of Practice.

3.6 Where borrowing is undertaken, the Authority is required to pay off an element of its accumulated capital spend each year through a revenue charge (the minimum revenue provision - MRP). MHCLG regulations require the Authority to approve an MRP Statement in advance of each year.

Annual Investment Strategy 2020/21

3.7 The annual investment strategy as set out in section 7 of **Appendix 1** sets out the parameters within which the Authority's cash balances and reserves will be invested. The strategy concentrates on two key areas:

a) capital security through investment in institutions with the highest credit ratings, and;
b) liquidity by limiting the maximum period of investment.

3.8 The Annual Investment Strategy provides compliance with the investment guide issued by the Secretary of State. An assessment has been undertaken of the expected level of the Authority's reserves and anticipated capital programme over the Medium Term Financial Strategy period. This review has identified a proportion of the authority's reserves are expected to be maintained for this period, and can therefore potentially support the following:

- Allowing the authority to internally borrow for a proportion of its capital programme, avoiding financing costs of external debt.
- A proportion of the Authority's reserves to be invested for a longer period.

3.9 The Investment Strategy has therefore been updated to include short dated bond funds as permitted instruments. Short dated bond funds are a pooled investment vehicle which invests in a wide range of fixed income instruments, including corporate and government bonds. Suggested minimum investment durations range typically from 12-18 months to 2-3 years, depending on the strategy of each fund. Short dated bond funds have been selected as an appropriate instrument for the authority as the suggested time horizon of up to 3 years will help provide increased investment returns without exposing the authority to the volatility of much longer dated instruments. Any decision to use these funds will include an in depth review of the appropriate level of investment (including the potential impact of losses on reserves), and a selection process of funds which will include a due diligence process.

3.10 The investment strategy details the criteria used for selecting suitable counterparties for investing funds. The strategy recommends a maximum risk indicator of 0.05% that reflects the emphasis placed on the security of the Authority's investments. This risk indicator represents the probability, of capital loss within the authority's investment portfolio. A risk factor of 0.00% cannot be achieved and the benchmark is a simple target that measures the risk based on the financial standing of counterparties and the length of each investment based on historic default rates. The risk factor is a way of setting a parameter and monitoring the ongoing security of the authority's portfolio but does not equate to an expected loss in the portfolio.

3.11 The Authority's bank balance continues to be maintained at a maximum limit of £50,000. This process simply limits the risk of exposure to the Authority's operational bank, but does not reflect an expectation of loss.

3.12 The Prudential Code states that decisions around capital expenditure, investment and borrowing should align with the processes established for the setting of an authority's budget, and prescribes that ultimate responsibility for implementation lies with the Authority. As a result, officers will present a Capital Strategy alongside the 2020/21 Budget Report.

<u>Economic Background</u>

3.13 **Appendix 2** to this report provided an economic overview provided by Brighton & Hove City Council's Treasury advices, Link Asset Services, as at 4 February 2020.

<u>Treasury Management Function</u>

3.14 The Authority's treasury management and Section 151 function is provided through a service contract with Brighton & Hove City Council. The treasury function complies with all statutory powers and regulatory requirements and is carried out by staff with relevant training and qualifications to undertake the duties and responsibilities allocated to them.

3.15 The authority's day to day cash requirements are currently invested in Brighton & Hove City Council. This is considered the most cost effective way to run the service for the Authority, and has the added following benefits:

a) The Authority is able to have access to daily liquidity to manage day-to-day cash flow requirements;

b) By investing in Brighton & Hove City Council, the Authority benefits from enhanced rates as the average rate earned on the whole of the Brighton & Hove City Council's investment portfolio is payable to the Authority on its balances, including investments held on a longer term basis. The Authority, investing alone, would have barriers in investing in instruments open to Brighton & Hove City Council.

3.16 This report is presented by both the Section 151 Chief Finance Officer and the Head of Business Services. The Head of Business Services is required to be a qualified accountant and is able, if necessary, to seek advice from other treasury specialists other than from Brighton & Hove City Council.

4. Options & cost implications

4.1 The Treasury Management Strategy document recommended in this report seeks to minimise the cost of external borrowing and optimise return on the Authority's investments, subject to ensuring the security of the Authority's resources.

5. Next steps

5.1 This report makes recommendations for Authority approval of the Treasury Management Strategy 2020/21. The Authority will be asked to approve these documents at the March 2020 Authority meeting.

5.2 Quarterly update reports and an annual report after the close of the financial year, in the form prescribed in the TMPs will be submitted to the Policy & Resources Committee

6. Other Implications

Implication	**Yes*/No**
Will further decisions be required by another committee/full authority?	Yes - This report makes recommendations for full Authority approval.
Does the proposal raise any Resource implications?	Yes – Policy & Resources Committee will be advised at least four time a year on the financial implications arising from the Treasury Management activity
How does the proposal represent Value for Money?	The Treasury Management Strategy recommended in this report seeks to minimise the cost of external borrowing and optimise return on the Authority's investments, subject to ensuring the security of the Authority's resources.
Are there any Social Value implications arising from the proposal?	No
Have you taken regard of the South Downs National Park Authority's equality duty as contained within the Equality Act 2010?	Yes – there are no implications arising directly from the report.
Are there any Human Rights implications arising from the proposal?	No
Are there any Crime & Disorder implications arising from the proposal?	No
Are there any Health & Safety implications arising	No

from the proposal?	
Are there any Data Protection implications?	No
Are there any Sustainability implications based on the 5 principles set out in the SDNPA Sustainability Strategy: 1.	The Authority's investments are undertaken in accordance with its ethical investment policy, which is unchanged from last year, as set out in Appendix 1. There are no other sustainability implications arising from this report.

7. Risks Associated with the Proposed Decision

7.1 A risk assessment is contained within the treasury management practices set out in **Appendix 1** to this report.

NIGEL MANVELL
Chief Finance Officer
South Downs National Park Authority

ALAN BROUGH
Head of Business Services
South Downs National Park Authority

Contact Officer:	Steven Bedford, Principal Accountant
Tel:	01273 293047
email:	steven.bedford@brighton-hove.gov.uk
Appendices	1. Treasury Management Strategy 2020/21 2. Economic Overview
SDNPA Consultees	Chief Executive; Director of Countryside Policy and Management; Director of Planning; Chief Finance Officer; Monitoring Officer; Legal Services, Business Service Manager
External Consultees	None
Background Documents	This report is presented in accordance with the Authority's Financial Regulations and Financial Procedures

South Downs National Park Authority
Treasury Management Strategy 2020/21

Contents

1. Introduction

The Authority 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 counterparties or instruments commensurate with the Authority's risk appetite, providing adequate liquidity initially before considering investment return.

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

The Authority is required to receive and approve its prudential and treasury indicators, and treasury strategy which covers the following:

- Treasury Management Policy Statement and Practices (how the investments and borrowings are to be organised);
- a borrowing strategy (including prudential indicators) to ensure that sufficient cash is available to meet the capital investment plans the capital investment plans; and
- a Minimum Revenue Provision (MRP) policy, (how residual capital expenditure is charged to revenue over time); and
- an Annual Investment Strategy, (the parameters on how investments are to be managed).

2. Treasury Management Policy Statement 2020/21

The following paragraphs set out the Authority's Treasury Management Policy Statement for the year commencing 1 April 2020:

1 The Authority defines its treasury management activities as:

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

2 The Authority regards the successful identification, monitoring and management 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 Authority.

3 The Authority 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 best value in treasury management and to employing suitable

performance measurement techniques within the context of effective risk management.

3. Treasury Management Practices 2020/21

TMP1: Risk management

The Authority's Section 151 Officer will secure all arrangements for the identification and management of treasury management risk. The Section 151 Officer will report at least annually on the adequacy and suitability thereon and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the Authority's objectives in this respect.

The arrangements secured by the Section 151 Officer will ensure:

- the Authority has adequate (though not excessive) cash resources, borrowing arrangements, overdraft and standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business / service objectives;
- the prudent use of approved financing and investment instruments, methods and techniques;
- a prudent attitude towards the organisations with which the Authority's funds may be deposited, including the limiting of investment activity to instruments, methods and techniques referred to in 'TMP4 Approved instruments, methods and techniques';
- all of the Authority's treasury management activity complies with its statutory powers and regulatory requirements;
- the use of systems and procedures that minimise the exposure to risk of loss through fraud, error, corruption or other eventualities in its treasury management dealings.

TMP2: Best value and performance measurement

The Section 151 Officer will ensure the Authority is committed to the pursuit of best value in its treasury management activities.

TMP3: Decision-making and analysis

The Section 151 Officer will maintain full records of the Authority's treasury management decisions and of the processes and practices applied in reaching those decisions, both for the purposes of learning from the past, and for demonstrating that reasonable steps were taken to ensure that all issues relevant to those decisions were taken into account at the time.

TMP4: Approved instruments, methods and techniques

The Section 151 Officer will undertake the Authority's treasury management activity by employing only those instruments, methods and techniques suitable to meet the organisation's short to medium term needs.

TMP5: Organisation, clarity and segregation of responsibilities / dealing arrangements

The Section 151 Officer will ensure:

- there are clear written statements of the responsibilities for each post engaged in treasury management and arrangements for absence cover and business continuity;
- there is proper documentation for all deals and transactions, and;
- procedures exist for the effective transmission of funds.

TMP6: Reporting / management information arrangements

The Section 151 officer will prepare and present to the Authority:

- an annual report on the strategy and plan to be pursued in the coming year;
- quarterly reports on transactions undertaken, and;
- an annual report on the performance of the treasury management service.

TMP7: Budgeting, accounting and audit arrangements

The Section 151 Officer will account for the Authority's treasury management activity, for decisions made and transactions executed, in accordance with appropriate accounting practices and standards, and with statutory and regulatory requirements in force for the time being.

TMP8: Cash / cash flow management

Unless statutory or regulatory requirements demand otherwise, all funds of the Authority will be under the control of the Section 151 Officer and will be aggregated for cash flow and investment management purposes. Cash flow projections will be prepared on a regular and timely basis and the Section 151 Officer will monitor that these are adequate for compliance with TMP1 (Liquidity risk management).

TMP9: Money laundering

The Section 151 Officer will ensure the Authority introduces and maintains procedures for verifying and recording the identity of counterparties and reporting suspicions and will ensure that staff involved are properly trained.

TMP10: Staff training / qualifications

The Section 151 Officer will ensure that all staff involved in the treasury management service shall be fully equipped to undertake the duties and responsibilities allocated to them.

The Section 151 Officer will ensure Authority members tasked with treasury management responsibility have access to training relevant to their needs and responsibilities.

TMP11: Use of external service providers

The Authority recognises that the responsibility for treasury management decisions remain with the Authority at all times. It recognises that there may be potential value in employing external providers in order to acquire access to specialist skills and resources. Where it employs such services, it will ensure that the terms of such an appointment and the methods by which their value will be assessed are properly agreed and documented and subject to regular review.

TMP12: Corporate governance

The Authority is committed to the pursuit of proper corporate governance throughout its business and services, and to establishing the principles and practices by which this can be achieved. Accordingly, the Section 151 Officer will ensure that the treasury management service and its activities will be undertaken with openness and transparency, honesty, integrity and accountability.

The Authority will adopt the key recommendations of the Code of Practice in Treasury Management.

4. **Borrowing Strategy**

The capital expenditure plans of the Authority are set out in the approved Capital Strategy. The treasury management of the Authority function ensures that the Authority's cash is organised in accordance with the relevant professional codes so that sufficient cash is available to meet the capital expenditure plans.

Any capital investment that is not funded from new and/or existing resources (e.g. capital grants, receipts from asset sales, revenue contributions or earmarked reserves) increases the Authority's need to borrow, represented by the Authority's Capital Financing Requirement (CFR). However, external borrowing does not have to take place immediately to finance related capital expenditure:

the Authority can utilise cash being held for other purposes (such as earmarked reserves and working capital balances) to temporarily defer the need for external borrowing. This is known as 'internal borrowing' or 'under-borrowing'.

The Authority's primary objective is to strike an appropriate balance between securing cost certainty and securing low interest rates.

Borrowing Strategy for 2020/21

The Authority's capital programme 2020/21 to 2024/25 forecasts a total of £2.377m capital investment, £0.977m of which will be met from existing or new resources. The increase in the borrowing need over this period is therefore £1.400m (difference of the above figures) as shown in Table 1 below.

Table 1: Borrowing Need	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
Capital Expenditure	1,877	440	20	20	20
Financed by New / Existing Resources	(897)	(20)	(20)	(20)	(20)
Borrowing Need	980	420	0	0	0

Of the £1.400m borrowing need shown, all is from projects that are awaiting approval or detailed analysis. Therefore, the timing of borrowing is uncertain, and borrowing decisions for these projects will form part of the viability and due diligence process.

For the remaining borrowing need, the strategy will initially focus on meeting this borrowing need from internal borrowing i.e. avoiding external borrowing by utilising the Authority's own surplus cash flow. This will reduce the net revenue cost of borrowing and reduce counterparty risk within the Authority's investment portfolio by reducing the portfolio size. The internal borrowing position needs to be carefully and continually reviewed to avoid incurring higher borrowing costs in the future at a time when the authority may not be able to avoid new borrowing to finance capital expenditure or refinance maturing debt.

There will remain a cost of carry (the difference between borrowing costs and investment rates) to any new long term borrowing that causes a temporary increase in cash balances which will, most likely, lead to a cost to revenue.

Policy on Borrowing in Advance of Need

The Authority will not borrow purely in order to profit from investment of extra sums borrowed. Any decision to borrow in advance will be within approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that the Authority can ensure the security of such funds. Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting.

Debt Rescheduling

Officers will regularly review opportunities for debt rescheduling where there is a clear difference between new borrowing and repayment rates which would result in savings.

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 strategy;
- enhancing the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

<u>Interest Rate Risk & Continual Review</u>

The Authority's total borrowing need of £1.400m as identified in Table 1 is the extent to which the Authority is subject to interest rate risk over the next five years. Officers will review the need to borrow taking into consideration the potential increases in borrowing costs, the need to finance new capital expenditure, the need to refinance maturing debt, availability of internal borrowing, and the cost of carry that might incur a revenue loss between borrowing costs and investment returns. The Chief Finance Officer will therefore continue to monitor interest rates in financial markets and adopt a proactive approach to changing circumstances.

5. Prudential and Treasury Indicators 2020/21 to 2024/25

The Authority's capital expenditure plans are a key driver to treasury management activities. The output of the capital expenditure plans are reflected in prudential indicators. The Authority is required to 'have regard to' the Prudential Code and to set up Prudential Indicators to ensure that the Authority's capital investment plans are affordable, prudent and sustainable. The Code sets out the indicators that must be used but does not suggest limits, as these are for the authority to set itself.

The Prudential Indicators to 2020/21 to 2024/25 are set out in Table 2 below:

Table 2: Prudential Indicators	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
Capital Expenditure Capital expenditure plans	1,877	440	20	20	20
Capital Financing Requirement Measures to underlying need to borrow for capital purposes	1,130	1,526	1,491	1,455	1,419
Ratio of financing costs to new revenue stream* Identifies the trend in the cost of capital (borrowing and other long term obligation costs new of investment income) against revenue stream	(0.75%)	(0.25%)	(0.10%)	(0.08%)	(0.15%)

* The ratio of financing costs to net revenue stream illustrates the percentage of the net revenue budget being used to finance the authority's borrowing. This includes interest costs relating to the authority's borrowing portfolio and MRP, net of the investment income from the Authority's investment portfolio. A negative ratio illustrates a net contribution to the Authority, as anticipated investment income is greater than the anticipated cost of borrowing.

The Treasury Management Code requires that a number of indicators are set for treasury performance in addition to the Prudential Indicators which fall under the Prudential Code. The Treasury Indicators for 2020/21 to 2024/25 are set out in Tables 3 & 4 below. The Treasury Indicators have been calculated and determined by officers in compliance with the Treasury Management Code of Practice.

Table 3: Treasury Performance Indicators	**2020/21 Estimate £'000**	**2021/22 Estimate £'000**	**2022/23 Estimate £'000**	**2023/24 Estimate £'000**	**2024/25 Estimate £'000**
Authorised Limit for External Debt* The Authority is expected to set a maximum authorised limit for external debt. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Authority.	1,500	2,000	2,000	2,000	2,000
Operational boundary for external debt* The Authority is required to set an operational boundary for external debt. This is the limit which external debt is not normally expected to exceed. This indicator can be breached temporality for operational reasons.	1,300	1,800	1,800	1,800	1,800
Principal Sums invested for longer than 365 days	0	0	0	0	0

*From 2020/21 The Authorised Limit and Operational Boundary includes an estimate for leases that will be bought onto the balance sheet under a change in leasing accounting regulations.

Table 4: Maturity Structure of fixed interest rate borrowing The Authority needs to set upper and lower limits with respect of the maturity structure of its borrowing.		
	Lower Limit	**Upper Limit**
Under 12 months	0%	40%
12 months to 2 years	0%	40%
2 years to 5 years	0%	50%
5 years to 10 years	0%	75%
Over 10 years	40%	100%

6. <u>Minimum Revenue Provision Policy Statement</u>

The authority is required to pay off an element of the accumulated capital spend each year (the Capital Financing Requirement - CFR) through a revenue charge (the minimum revenue provision - MRP). Ministry of Housing, Communities and Local Government (MHCLG) regulations require the Authority to approve an MRP Statement in advance of each year if borrowing has been undertaken. A variety of options are available, so long as the principle of any option selected ensures a prudent provision to redeem its debt liability over a period which is commensurate with that over which the capital expenditure is estimated to provide benefits (i.e. estimated useful life of the asset being financed).

The Authority is recommended to approve the following MRP Statement for 2020/21:

For all debt where the government has provided revenue support (supported capital expenditure), the MRP policy will be:

- Provision on a straight line basis over 50 years.

For all debt where the government does not provide revenue support:

- Where the debt relates to an asset, the Authority will set aside a sum equivalent to repaying the debt over the life of the asset either in equal instalments or on an annuity basis over a maximum life of 50 years. The method to be adopted will be determined according to which is the most financially beneficial to the Authority over the life of the asset. Asset Life Method (annuity method);

- Where the debt relates to expenditure which is subject to a capitalisation direction issued by the government, the Authority will set aside a sum equivalent to repaying the debt over a period consistent with the nature of the expenditure on an annuity basis.

- In the case of assets under construction, MRP will be delayed until the relevant asset becomes operational.

Where the debt relates to capital loans to a third party:

- The repayments of principal will be set aside as capital receipts to finance the initial capital advance in lieu of making a MRP;

There is the option to charge more than the prudent provision of MRP each year through a Voluntary Revenue Provision (VRP).

7. Annual Investment Strategy 2020/21

This Strategy complies with guidance to be issued by the Secretary of State on investments.

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

Greater returns are usually obtainable by investing for longer periods. While most cash balances are required in order to manage the ups and downs of cash flow, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed.

The annual investment strategy sets out the parameters within which the Authority's cash balances and reserves will be invested. The strategy concentrates on two key areas:

a) capital security through investment in institutions with the highest credit ratings, and;
b) liquidity by limiting the maximum period of investment.

Investment classification (regulatory)

The investment guidance issued by the Secretary of State requires the Authority to identify investments as either 'specified' or 'non-specified'.

This authority has defined the list of types of investment instruments that the treasury management team are authorised to use.

- **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year. The limits and permitted instruments for specified investments are listed within Table 5.
- **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use. The limits and

permitted instruments for non-specified investments are listed within Table 6.

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

Each counterparty included on the Authority's approved lending list must meet the criteria set out below. Without the prior approval of the NPA, no investment will be made in an instrument that falls outside the list below.

Credit ratings will be based on those issued periodically by the Fitch Ratings Group, Moody's and Standard & Poors.

Table 5 below summarises the types of specified investment counterparties available to the Authority, and the maximum amount and maturity periods placed on each of these. A full list of the Authority's counterparties and the current limits for 2020/21 are provided at Table 7.

When assessing credit ratings to ascertain limits for each counterparty, the lowest short and long term ratings from each of the three ratings agencies is applied. For simplicity, the ratings for Standard & Poor's are used in the tables below.

Table 5: Criteria for Specified Investments	Country/ Domicile	Minimum Capital Requirements	Min. Credit Criteria (L/term / S/term)	Max. Amount	Max. maturity period
UK Banks & Building Societies	UK	Must meet minimum credit criteria	AA- / A-1+	£10m	12 months
			A / A-1	£5m	12 months
			BBB / A-2	£5m	6 months
Debt Management and Deposit Facilities (DMADF)	UK	N/A	N/A	£5m	12 months
UK Local Authorities (excluding Brighton & Hove City Council)	UK	N/A	UK Sovereign Rating	£5m	12 months
Brighton & Hove City Council*	UK	N/A	N/A	N/A	Liquid
Non-rated Building Societies	UK	Must have an asset base of at least £5bn at the time of investment	N/A	£5m	6 months
Money Market Funds (CNAV and LVNAV)	UK/Ireland/ EU domiciled	Must meet minimum credit criteria	AAA	£5m	Liquid

* The amount invested in Brighton & Hove City Council will be the amount available for investment less investment made in any other approved counterparty.

Table 6: Criteria for Non-Specified Investments	Country/ Domicile	Min. Credit Criteria	Max. Amount	Max. maturity period
Short Date Bond Funds	UK/Ireland/ EU domiciled	Short Dated bond funds are not rated. A selection process will evaluate relative risks & returns. Security of the Authority's money and fund volatility will be key measures of suitability.	£2m	Liquid

<u>Maximum permitted investment by counterparty / sector</u>

The maximum amount invested in any one counterparty will be established in accordance with the criteria set out Tables 5 and 6 above, based on each counterparty's credit rating.

The maximum amount invested in any one sector will be 100%, with the exception of the building society sector where the maximum limit will be 75%.

Where practicable no one counterparty may have more than 75% of the relevant sector total at the time the investment is made.

<u>Approved methodology for changing limits and adding / removing counterparties</u>

A counterparty shall be removed from the Authority's list where a change in their credit rating results in a failure to meet the minimum credit rating set out in "Criteria to be used for creating / managing approved counterparty lists / limits" above.

A counterparty's exposure limit and investment period will be reviewed and (changed where necessary) in accordance with the criteria set out in Tables 7 following notification of a change in that counterparty's credit rating or a view expressed by the credit rating agency warrants a change.

A counterparty's exposure limit will also be reviewed where information contained in the financial press or other similar publications indicates a possible worsening in credit worth of a counterparty. The review may lead to the suspension of a counterparty where it is considered appropriate to do so by the Section 151 Officer.

<u>Full individual listings of UK Bank and Building Society counterparties and counterparty limits</u>

A full list of <u>UK Bank and Building Society</u> counterparties, together with counterparty limits, is set out in Table 7.

Table 7 – Schedule of Counterparties and counterparty limits		
Institution	**Lending Limit**	**Duration limit (months)**
UK Banks		
Lloyds Banking Group:		
Bank of Scotland PLC (RFB)	£5m	12
Lloyds Bank PLC (RFB)	£5m	12
Lloyds Bank Corporate Markets PLC (NRFB)	£5m	12
**Total max. exposure to Lloyds Banking Group	£5m	12
Barclays Banking Group:		
Barclays Bank PLC (NRFB)	£5m	12
Barclays Bank UK PLC (RFB)	£5m	12
**Total max. exposure to Barclays Banking Group:	£5m	12
RBS/Natwest Group:		
Natwest Markets PLC (NRFB)	£5m	6
National Westminster Bank PLC (RFB)	£5m	6
The Royal Bank of Scotland PLC	£5m	6
**Total max. exposure to RBS/Natwest Group:	£5m	6
HSBC Group:		
HSBC Bank PLC (NRFB)	£10m	12
HSBC UK Bank PLC (RFB)	£10m	12
**Total max. exposure to HSBC Group:	£10m	12
Santander UK PLC	£5m	12
UK Building Societies		
Nationwide	£5m	12

**Where there are multiple counterparties within a banking group, exposure to the overall group will be the largest limit, but exposure to individual counterparties within the group will be based on the individual counterparty limit.

Permitted types of investment instrument

All investments will be denominated in Sterling and in fixed term and/or variable term cash deposits, money market funds, short dated bond funds and open ended investment companies.

Investment risk

In addition to credit ratings, the Authority will apply additional operational market information before making any specific investment decision. This additional market information will be applied to compare the relative security of different investment counterparties.

The Authority is recommended to agree a benchmark risk factor for 2020/21 of 0.05%. The purpose of the benchmark is to monitor current and trend positions and amend the operational strategy depending on any changes.

Liquidity is achieved by limiting the maximum period for investment and by investing to dates where cash flow demands are known or forecast.

Ethical investment statement

South Downs National Park Authority, in making investments through its treasury management function, fully supports the ethos of socially responsible investments. The Authority will actively seek to communicate this support to those institutions invested in as well as those it is considering investing in by:

- encouraging those institutions to adopt and publicise policies on socially responsible investments;
- requesting those institutions to apply the Authority's deposits in a socially responsible manner.

Counterparties shall be advised of the above statement each and every time a deposit is placed with them.

ANNEX B - ECONOMIC OVERVIEW

Provided by Link Asset Services on 4 February 2020

UK. Brexit. 2019 was a year of upheaval on the political front culminating in a new Conservative Government gaining a large overall majority in the **general election** on 12 December on a mandate of leaving the EU on 31 January. However, there will still be much market uncertainty as the detail of a comprehensive trade deal will need to be negotiated by the current end of the transition period in December 2020, which the Prime Minister has pledged he will not extend. Should this prove to be an unrealistically short timetable for such major negotiations that leaves open three possibilities; a partial agreement on many areas of agreement and then continuing negotiations to deal with the residual areas, the need for the target date to be put back, probably two years, or, a no deal Brexit in December 2020.

GDP growth took a big hit from both the political and Brexit uncertainty during 2019; quarter three 2019 surprised on the upside by coming in at +0.4% (+1.1% year-on-year). However, the peak of Brexit uncertainty during the final quarter appears to have suppressed quarterly growth to probably around zero. The forward-looking surveys in January have indicated that there could be a significant recovery of growth now that much uncertainty has gone. Nevertheless, economic growth may only come in at about 1% in 2020, pending the final outcome of negotiations on a trade deal. Provided there is a satisfactory resolution of those negotiations, which are in both the EU's and UK's interest, then growth should strengthen further in 2021.

At its 30 January meeting, the Monetary Policy Committee held Bank Rate unchanged at 0.75%. The vote continued to be split 7-2, with two votes for a cut to 0.50%. The financial markets had been predicting a 50:50 chance of a rate cut at the time of the meeting. Admittedly, there had been plenty of downbeat UK economic news in December and January which showed that all the political uncertainty leading up to the general election, together with uncertainty over where Brexit would be going after the election, had depressed economic growth in quarter 4. In addition, three members of the MPC had made speeches in January which were distinctly on the dovish side, flagging up their concerns over weak growth and low inflation; as there were two other members of the MPC who voted for a rate cut in November, five would be a majority at the January MPC meeting if those three followed through on their concerns.

However, that downbeat news was backward looking; more recent economic statistics and forward-looking business surveys, have all pointed in the direction of a robust bounce in economic activity and a recovery of confidence after the decisive result of the general election removed political and immediate Brexit uncertainty. In addition, the September spending round increases in expenditure will be kicking in in April 2020 while the Budget in March is widely expected to include a substantial fiscal boost by further increases in expenditure, especially on infrastructure. However, the MPC's forecasts for growth that were cut from 1.2% to 0.8% for 2020, and from 1.8% to 1.4% for 2021, could not include any allowance for the March Budget. Overall, the MPC clearly decided to focus on the more recent forward-looking news than the earlier downbeat news.

The quarterly Monetary Policy Report did, though, flag up that there was still a risk of a Bank Rate cut; "Policy may need to reinforce the expected recovery in UK GDP growth should the more positive signals from recent indicators of global and domestic activity not be sustained or should indicators of domestic prices remain relatively weak." Obviously, if trade negotiations with the EU failed to make satisfactory progress, this could dampen confidence and growth. On the other hand, there was also a warning in the other direction, that if growth were to pick up strongly, as suggested by recent business surveys, then "some modest tightening" of policy might be needed further ahead. It was therefore notable that the Bank had dropped its phrase that tightening would be "limited and gradual", a long-standing piece of forward guidance; this gives the MPC more room to raise Bank Rate more quickly if growth was to surge and, in turn, lead to a surge in inflation above the 2% target rate.

As for **inflation** itself, CPI has been hovering around the Bank of England's target of 2% during 2019, but fell again in both October and November to a three-year low of 1.5% and then even further to

1.3% in December. It is likely to remain close to or under 2% over the next two years and so, it does not pose any immediate concern to the MPC at the current time. However, if there was a hard or no deal Brexit, inflation could rise towards 4%, primarily because of imported inflation on the back of a weakening pound.

With regard to the **labour market,** growth in numbers employed has been quite resilient through 2019 until the three months to September, where it fell by 58,000. However, there was an encouraging pick up again in the three months to October to growth of 24,000 and then a marked increase of 208,000 in the three months to November. The unemployment rate held steady at a 44-year low of 3.8% on the Independent Labour Organisation measure. Wage inflation has been steadily falling from a high point of 3.9% in July to 3.4% in November (3-month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates higher than CPI inflation), earnings grew by about 2.1%. As the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. The other message from the fall in wage growth is that employers are beginning to find it easier to hire suitable staff, indicating that supply pressure in the labour market is easing.

Coronavirus. The recent Coronavirus outbreak could cause disruption to the economies of affected nations. The Chinese economy is now very much bigger than it was at the time of the SARS outbreak in 2003 and far more integrated into world supply chains. However, a temporary dip in Chinese growth could lead to a catch up of lost production in following quarters with minimal net overall effect over a period of a year. However, it's unknown quite how big an impact the virus may have around the world; if the efforts of the WHO and the Chinese authorities to contain the virus are successful this is likely to minimise economic impact.

WORLD GROWTH. Until recent years, world growth has been boosted by increasing **globalisation** i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last thirty years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy.

The trade war between the US and China is a major concern to financial markets due to the synchronised general weakening of growth in the major economies of the world, compounded by fears that there could even be a recession looming up in the US, though this is probably overblown. These concerns resulted in government bond yields in the developed world falling significantly during 2019. If there were a major worldwide downturn in growth, central banks in most of the major economies will have limited ammunition available, in terms of monetary policy measures, when rates are already very low in most countries (apart from the US). There are also concerns about how much distortion of financial markets has already occurred with the current levels of quantitative easing purchases of debt by central banks and the use of negative central bank rates in some countries.

Prospects for interest rates

The following table gives LAS's central view

Link Asset Services Interest Rate View													
	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25	1.25	1.25	1.25
3 Month LIBID	0.70	0.70	0.80	0.80	0.90	1.00	1.00	1.10	1.20	1.30	1.30	1.30	1.30
6 Month LIBID	0.80	0.80	0.90	1.00	1.00	1.10	1.20	1.30	1.40	1.50	1.50	1.50	1.50
12 Month LIBID	0.90	0.90	1.00	1.10	1.20	1.30	1.40	1.50	1.60	1.70	1.70	1.70	1.70
5yr PWLB Rate	2.30	2.30	2.40	2.40	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.00	3.10
10yr PWLB Rate	2.50	2.50	2.60	2.60	2.70	2.80	2.90	3.00	3.10	3.10	3.20	3.20	3.30
25yr PWLB Rate	3.00	3.00	3.10	3.20	3.30	3.40	3.50	3.60	3.70	3.80	3.80	3.90	3.90
50yr PWLB Rate	2.90	2.90	3.00	3.10	3.20	3.30	3.40	3.50	3.60	3.70	3.70	3.80	3.80

The above forecasts have been based on an assumption that there is an agreed deal on Brexit, including agreement on the terms of trade between the UK and EU, at some point in time. The result of the general election has removed much uncertainty around this major assumption. However, it does not remove uncertainty around whether agreement can be reached with the EU on a comprehensive trade deal within the short time to December 2020, as the prime minister has pledged.

2019 was a weak year for UK economic growth as political and Brexit uncertainty depressed confidence. It was therefore of little surprise that the Monetary Policy Committee (MPC) left Bank Rate unchanged at 0.75% during the year. However, during January 2020, financial markets were predicting a 50:50 chance of a cut in Bank Rate at the time of the 30 January MPC meeting.

Admittedly, there had been plenty of downbeat UK economic news in December and January which showed that all the political uncertainty leading up to the general election, together with uncertainty over where Brexit would be going after that election, had depressed economic growth in quarter 4 of 2019. However, that downbeat news was backward looking; more recent economic statistics and forward looking business surveys, all pointed in the direction of a robust bounce in economic activity and a recovery of confidence after the decisive result of the general election removed political and Brexit uncertainty. The MPC clearly decided to focus on the more recent forward-looking news, rather than the earlier downbeat news, and so left Bank Rate unchanged.

Provided that the forward-looking surveys are borne out in practice in the coming months, and the March Budget delivers with a fiscal boost, then it is expected that Bank Rate will be left unchanged until after the December trade deal deadline. However, the MPC is on alert that if the surveys prove optimistic and/or the Budget disappoints, then they may still take action and cut Bank Rate in order to stimulate growth.

Investment and borrowing rates

- Investment returns are likely to remain low during 2020/21 with little increase in the following two years. However, if major progress were made with an agreed Brexit, then there is upside potential for earnings.

- Borrowing interest rates were on a major falling trend during the first half of 2019/20 but then jumped up by 100 bps on 9/10/2019. The policy of avoiding new borrowing by running down spare cash balances has served local authorities well over the last few years. However, the unexpected increase of 100 bps in PWLB rates requires a re-think of local authority treasury management strategy and risk management. As Link Asset Services' long-term forecast for Bank Rate is 2.25%, and all PWLB certainty rates are close to or above 2.25%, there is little value in borrowing from the PWLB at present. Accordingly, the Authority will reassess its risk appetite in terms of either seeking cheaper alternative sources of borrowing or switching to short term borrowing in the money markets until such time as the Government might possibly reconsider the margins charged over gilt yields. Longer term borrowing could also be undertaken for the purpose of certainty, where that is desirable, or for flattening the profile of a heavily unbalanced maturity profile.

- While this authority may not be able to avoid borrowing to finance new capital expenditure, there will be a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new short or medium-term borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.