

**The Office of the Police and Crime Commissioner for Norfolk
Annual Investment and Treasury Management Strategy Statement 2019/20**

1. Background

- 1.1 The PCC 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 PCC'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 PCC's capital plans. These capital plans provide a guide to the borrowing need of the PCC, essentially the longer-term cash flow planning, to ensure that the PCC can meet his 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 PCC risk or cost objectives.
- 1.3 The contribution the treasury management function makes to the PCC 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 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 Revised reporting is required for the 2019/20 reporting cycle due to revisions of the Ministry of Housing, Communities and Local Government (MHCLG) Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a capital strategy, to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011. The capital strategy is being reported separately.
- 1.6 This PCC has not engaged in any commercial investments and has no non-treasury investments.

2. Reporting requirements

Capital Strategy

- 2.1 The CIPFA revised 2017 Prudential and Treasury Management Codes require, for 2019/20, 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
- 2.2 The aim of this capital strategy is to ensure that the PCC fully understands the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.
- 2.3 The Capital Strategy will be published separately but is included within the PCC's Budget and MTFP report.

Treasury Management reporting

- 2.4 The PCC is currently required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals.
- a. Prudential and treasury indicators and treasury strategy** (this report)
- The first, and most important report is forward looking and covers:
- the capital plans, (including prudential indicators); (Appendix 1)
 - a minimum revenue provision (MRP) policy, (how unfunded capital expenditure is charged to revenue over time); (Appendix 2)
 - 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).
- b. A mid-year treasury management report** – This is primarily a progress report and will update the PCC on the capital position, amending prudential indicators as necessary, and whether any policies require revision.
- c. An annual treasury report** – This is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

3. Treasury Management Strategy for 2019/20

3.1 The strategy for 2019/20 covers two main areas:

Capital issues

- the capital expenditure plans and the associated prudential indicators; see Annex 1.
- the minimum revenue provision (MRP) policy. See Annex 2.

Treasury management issues

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

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

Training

3.2 The CIPFA Code requires the responsible officer to ensure that officers with responsibility for treasury management receive adequate training in treasury management. This also applies to Audit Committee members responsible for scrutiny. Training on the Prudential Code and the Capital Strategy was provided to Audit Committee members in October 2018.

Treasury management consultants

3.3 The PCC uses Link Asset Services, Treasury solutions as its external treasury management advisors.

3.4 The PCC recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regard to all available information, including, but not solely, our treasury advisers.

3.5 It is also recognised that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The PCC 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.

The Treasury Management Function

- 3.6 The CIPFA Code defines treasury management activities as “the management of the PCC’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.”
- 3.7 The PCC 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 PCC, and any financial instruments entered into to manage these risks.
- 3.8 The PCC 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.
- 3.9 The PCC is required to operate a balanced budget, which broadly means that cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensures this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties, providing adequate liquidity before considering investment return.
- 3.10 A further function of the treasury management service is to provide for the borrowing requirement of the PCC, essentially the longer term cash flow planning, typically 30 years plus, to ensure the PCC can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using internal cash balances on a temporary basis. Debt previously borrowed may be restructured to meet PCC risk or cost objectives.
- 3.11 The PCC has delegated responsibility for treasury management decisions taken within the approved strategy to the PCC CFO. Day to day execution and administration of investment and borrowing decisions is undertaken by Specialist Accountants based in the Joint Finance Department for Suffolk and Norfolk Constabularies.
- 3.12 External treasury management services continue to be provided by Link Asset Services in a joint contract with the PCC for Suffolk. Link Asset Services provides a range of services which include:
- Technical support on treasury matters and capital finance issues.

- Economic and interest rate analysis.
- Debt services which includes advice on the timing of long term borrowing.
- Debt rescheduling advice surrounding the existing portfolio.
- Generic investment advice on interest rates, timing and investment instruments.
- Credit ratings/market information service for the three main credit rating agencies (Fitch, Moody's and Standard & Poors).

3.13 Whilst Link Asset Services provide support to the treasury function, under market rules and in accordance with the CIPFA Code of Practice, the final decision on treasury matters remains with the PCC.

3.14 Performance will continue to be monitored and reported to the PCC as part of the budget monitoring report.

3.15 Link Asset Service's Economic Forecast is set out in Annex 3.

4. Investment Strategy 2019/20

4.1 The Bank Rate is forecast to stay flat at 0.75% until quarter 2 2019 and not to rise above 1.25% until quarter 4 2020. Bank Rate forecasts for financial year ends (March) are:

- 2018/19 0.75%
- 2019/20 1.25%
- 2020/21 1.50%
- 2021/22 2.00%

4.2 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:

Financial Year	Budgeted Interest Earnings
2018/19	0.75%
2019/20	1.00%
2020/21	1.50%
2021/22	1.75%
2022/23	1.75%

2023/24	2.00%
Later Years	2.50%

4.3 There are 3 key considerations to the treasury management investment process. MHCLG's Investment Guidance ranks these in the following order of importance:

- security of principal invested,
- liquidity for cash flow, and
- investment return (yield).

Each deposit is considered in the context of these 3 factors, in that order.

4.4 MHCLG's Investment Guidance requires local authorities and PCCs to invest prudently and give priority to security and liquidity before yield, as described above. In order to facilitate this objective, the Guidance requires the PCC to have regard to CIPFA's Code of Practice for Treasury Management in the Public Sector.

4.5 The key requirements of both the Code and the Investment Guidance are to produce an Annual Investment and Treasury Strategy covering the following:

- Guidelines for choosing and placing investments – Counterparty Criteria and identification of the maximum period for which funds can be committed – Counterparty Monetary and Time Limits (Section 5).
- Details of Specified and Non-Specified investment types (Section 10).

5. Investment Strategy 2019/20 - Counterparty Criteria

5.1 The PCC works closely with its external treasury advisors to determine the criteria for high quality institutions.

5.2 The criteria for providing a pool of high quality investment counterparties for inclusion on the PCC's 'Approved Authorised Counterparty List' is provided below

- **UK Banks** which have the following minimum ratings from at least one of the three credit rating agencies:

UK Banks	Fitch	Standard & Poors	Moody's
Short Term Ratings	F1	A-1	P-1

Long Term Ratings	A-	A-	A3
-------------------	----	----	----

- **Non-UK Banks** domiciled in a country which has a minimum sovereign rating of AA+ and have the following minimum ratings from at least one of the credit rating agencies:

Non-UK Banks	Fitch	Standard & Poors	Moody's
Short Term Ratings	F1+	A-1+	P-1
Long Term Ratings	AA-	AA-	Aa3

- **Part Nationalised UK Banks** – Royal Bank of Scotland Group (including Nat West). These banks are included while they continue to be part nationalised or they meet the minimum rating criteria for UK Banks above.
- **The PCC's Corporate Banker** – If the credit ratings of the PCC's corporate banker (currently Barclays Bank plc) fall below the minimum criteria for UK Banks above, then cash balances held with that bank will be for account operation purposes only and balances will be minimised in terms of monetary size and time.
- **Building Societies** – The PCC will use Building Societies which meet the ratings for UK Banks outlined above.
- **Money Market Funds (MMFs)** – which are rated AAA by at least one of the three major rating agencies. MMF's are 'pooled funds' investing in high-quality, high-liquidity, short-term securities such as treasury bills, repurchase agreements and certificate of deposit. Funds offer a high degree of counterparty diversification that include both UK and Overseas Banks.
- **UK Government** – including the Debt Management Account Deposit Facility & Sterling Treasury Bills. Sterling Treasury Bills are short-term (up to six months) 'paper' issued by the UK Government. In the same way that the Government issues Gilts to meet long term funding requirements, Treasury Bills are used by Government to meet short term revenue obligations. They have the security of being issued by the UK Government.
- **Local Authorities, Parish PCCs etc.** – Includes those in England and Wales (as defined in Section 23 of the Local Government Act 2003) or a similar body in Scotland or Northern Ireland.

5.3 All cash invested by the PCC in 2019/20 will be either Sterling deposits (including certificates of deposit) or Sterling Treasury Bills invested with banks and other institutions in accordance with the Approved Authorised Counterparty List.

- 5.4 The Code of Practice requires local authorities and PCCs 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 use, additional market information will be used to inform investment decisions. This additional market information includes, for example, Credit Default Swap rates and equity prices in order to compare the relative security of counterparties.
- 5.5 The current maximum lending limit of £10m for any counterparty will be maintained in 2019/20 to reflect the level of cash balances and to avoid large deposits with the DMO.
- 5.6 In addition to individual institutional lending limits, “Group Limits” will be used whereby the collective investment exposure of individual banks within the same banking group is restricted to a group lending limit of £10m.
- 5.7 The Strategy permits deposits beyond 365 days (up to a maximum of 2 years) but only with UK banks which meet the credit ratings at paragraph 5.2. Deposits may also be placed with UK Part Nationalised Banks and Local Authorities for periods of up to 2 years.
- 5.8 A reasonable amount will be held on an instant access basis in order for the PCC to meet any unexpected needs. Instant access accounts are also preferable during periods of credit risk uncertainty in the markets, allowing the PCC to immediately withdraw funds should any concern arise over a particular institution.

6. Investment Strategy 2019/20 – Specified and Non-Specified Investments

6.1 As determined by CLG's Investment Guidance, Specified Investments offer "high security and high liquidity". They are Sterling denominated and have a maturity of less than one year. Institutions of "high" credit quality are deemed to be Specified Investments. From the pool of high quality investment counterparties identified in Section 5, the following are deemed to be Specified Investments where the period of deposit is 365 days or less:

- Banks: UK and Non-UK;
- Part Nationalised UK Banks;
- The PCC's Corporate Banker (Barclays Bank plc)
- Building Societies (which meet the minimum ratings criteria for Banks);
- Money Market Funds;
- UK Government;
- Local Authorities, Parish PCCs etc.

6.2 Non-Specified Investments are those investments that do not meet the criteria of Specified Investments. From the pool of counterparties identified in Section 5, they include:

- Any investment greater than 365 days.

6.3 The categorisation of 'Non-Specified' does not in any way detract from the credit quality of these institutions, but is merely a requirement of the Government's guidance.

6.4 The PCC's proposed Strategy for 2019/20 therefore includes both Specified and Non-Specified Investment institutions.

7. Borrowing Strategy 2019/20

7.1 Capital expenditure can be funded immediately by applying capital receipts, capital grants or revenue contributions. Capital expenditure in excess of available capital resources or revenue contributions will add to the PCC's borrowing requirement. The PCC's need to borrow is measured by the Capital Financial Requirement, which simply represents the total outstanding capital expenditure, which has not yet been funded from either capital or revenue resources.

7.2 For the PCC, borrowing principally relates to long term loans (i.e. loans in excess of 365 days). The borrowing strategy includes decisions on the timing of when further monies should be borrowed.

- 7.3 The main source of long term loans is the Public Works Loan Board (PWLB), which is part of the UK Debt Management Office (DMO). The maximum period for which loans can be advanced by the PWLB is 50 years.
- 7.4 External borrowing currently stands at £16.11m (excluding PFI). At 31 March 2018 there was a £29.1m Capital Financing Requirement (CFR) relating to unfunded capital expenditure which had been financed from internal resources. The CFR is estimated to be £31.2m at 31 March 2019, £40.3m at 31 March 2020 and £45.8 at 31 March 2021. Additional long term borrowing is estimated at £4.0m for 2018/19, £11.7m for 2019/20 and £6.95m for 2020/21. The borrowing requirement does not include the funding requirement in respect of assets financed through PFI.
- 7.5 The challenging and uncertain economic outlook outlined by Link Asset Services in Section 3, together with managing the cost of “carrying debt” requires a flexible approach to borrowing. The PCC, 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 identified in Link Asset Services economic overview (Section 3).
- 7.6 The level of outstanding debt and composition of debt, in terms of individual loans, is kept under review. The PWLB provides a facility to allow the restructure of debt, including premature repayment of loans, and encourages local authorities and PCCs to do so when circumstances permit. This can result in net savings in overall interest charges. The PCC CFO and Link Asset Services will monitor prevailing rates for any opportunities during the year. As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these 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). Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt
- 7.7 The PCC has flexibility to borrow funds in the current year for use in future years, but will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. 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 PCC can ensure the security of such funds
- 7.8 The PCC will continue to use the most appropriate source of borrowing at the time of making application, including; the PWLB, commercial market loans, Local Authorities and the Municipal Bond Agency.

8. Treasury Management Prudential Indicators

8.1 In addition to the key Treasury Indicators included in the Prudential Code and reported separately, there are two treasury management indicators. The purpose of the indicators is to restrict the activity of the treasury function to within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. However, if these indicators are too restrictive, they will impair the opportunities to reduce costs/improve performance. The Indicators are:

- **Maturity Structures of Borrowing** – These gross limits are set to reduce the PCC’s exposure to large fixed rate sums falling due for refinancing and require upper and lower limits. It is recommended that the PCC sets the following limits for the maturity structures of its borrowing at 31.3.19:

	Actual*	Lower Limit	Upper Limit
Under 12 months	0.3%	0%	15%
12 months and within 24 months	0.3%	0%	15%
24 months and within 5 years	11.2%	0%	45%
5 years and within 10 years	33.7%	0%	75%
10 years and above	54.5%	0%	100%

* Actual is based on existing balances at 31.12.18

- **Upper Limits to the Total of Principal Funds Invested for Greater than 365 Days** – This limit is set with regard to the PCC’s liquidity requirements. It is estimated that in 2019/20, the maximum level of PCC funds invested for periods greater than 365 days will be no more than £4.475m.