**EAST SUSSEX FIRE AUTHORITY**

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| **Meeting** | Fire Authority |
| **Date** | 10 February 2022 |
| **Title of Report** | Treasury Management Strategy for 2022/23 |
| **By** | Duncan Savage, Assistant Director Resources/Treasurer |
| **Lead Officer** | Richard Carcas, Principal Finance Officer (Treasury Management) ESCC |

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| **Background Papers** | Fire Authority:<br>11 February 2021 Treasury Management Strategy for 2021/22<br>2 September 2021 Treasury Management Stewardship Report 2021/22<br><br>Policy & Resources Panel:<br>11 November 2021 Half year review for 2021/22<br><br>CIPFA Prudential Code<br><br>CIPFA Treasury Management in the Public Services - Code of practice<br><br>Local Government Act 2003 Local Government Investments - Guidance from the The Department for Levelling Up, Housing and Communities (DLUHC). |

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| **Appendices** | 1 Treasury Management Scheme of Delegation<br>2 The Prudential & Treasury Indicators<br>3 Minimum Revenue Provision (MRP) Policy Statement<br>4 Approved countries for investment<br>5 Comment from Link Asset Services on the outlook for 2022/23<br>6 Counterparty list<br>7 Investment Benchmarking<br>8 Glossary |

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**Implications (please tick ✓ and attach to report)**

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|---|---|---|---|
| **CORPORATE RISK** | | **LEGAL** | |
| **ENVIRONMENTAL** | | **POLICY** | |

| | | | |
|---|---|---|---|
| **FINANCIAL** | ✓ | **POLITICAL** | |
| **HEALTH & SAFETY** | | **OTHER (please specify)** | |
| **HUMAN RESOURCES** | | **CORE BRIEF** | |
| **EQUALITY IMPACT ASSESSMENT** | | | |

**PURPOSE OF REPORT**

To approve the treasury management strategy, policy statement and the Minimum Revenue Provision (MRP) Statement 2022/23

**EXECUTIVE SUMMARY**

This report contains recommendations about the borrowing limits, the prudential indicators and limits, the investment strategy and policy as required by Section 3 (1) of the Local Government Act 2003 and the Prudential Code for Capital Finance 2017.

The emphasis continues to be on security (protection of the capital sum invested) and liquidity (keeping money readily available for expenditure when needed). The strategy and limits are consistent with the proposed capital programme and revenue budget dealt with elsewhere on the agenda. As will be clear from the global events, it is impossible in practical terms to eliminate all credit risk. The Fire Authority seeks to be prudent.

The Authority is recommended to approve borrowing limits to give flexibility for any future consideration in undertaking new external long-term / replacement borrowing should the need arise or market conditions prove favourable.

The Fire Authority has always adopted a prudent approach on its investment strategy and, in the last few years, there have been regular changes to the list of the approved organisations used for investment of short term surpluses. No further changes to the Investment Strategy are proposed for 2022/23.

Since March 2020 global economic events triggered by the COVID 19 pandemic have caused the Authority to pause consideration of entering into longer duration funds.

The 2022/23 Strategy counterparty list for specified and non-specified investment is set out in the Appendices 4 and 6 with an updated recommendation to note.

The Fire Authority will explore Investment options that meet Environment, Social and Governance (ESG) aims. The parameter will act as an added 4th consideration to investment decisions behind Security, Liquidity and Yield. The preservation of capital is the Authority’s principal and overriding priority.

The Fire Authority is recommended to approve the 2022/23 investment strategy. The Fire Authority should note that any introduction of longer term instruments will result in an increased (but appropriate) level of risk to the investment portfolio.

The Fire Authority to the 31st December 2021 earned £41k in investment interest at an average rate of 0.23%. This level of return is broadly consistent with recent available Investment benchmarking (Appendix 7).

The background information and the calculation of the Authorised Limit for borrowing for 2022/23 of £12.767m are set out in the attached Appendix 2 (Table 8).

Self-imposed Prudential and Treasury Management indicators that are set on an annual basis are shown in Appendix 2.

CIPFA published the revised Treasury and Prudential codes on 20 December 2021. To ensure Local Authorities can implement the code changes in a smooth and orderly fashion, formal adoption is not required until 2023/24. CIPFA is proposing a soft implementation, with full implementation expected by the required date. The Fire Authority will have regard to these codes of practice when it prepares the Treasury Management Strategy Statement and Annual Investment Strategy, and also related reports during the financial year.

The Department for Levelling Up, Housing and Communities (DLUHC) is proposing to make changes to the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (the 2003 Regulations). There is a consultation open which closes on 8 February 2022. The Authority will feed into this consultation and report on the results in due course.

The Government has identified that some Local Authorities are not sufficiently complying with their statutory MRP (Minimum Revenue Provision) duty and is proposing changes to regulations to make sure that practices are prudent and consistent across the sector. The Authority is compliant with the proposed changes. It is therefore considered that the proposed changes will not have any significant impact.

The Capital Financing Requirement (CFR) and MRP statement is set out in Appendix 2 and 3 to comply with best practice.

The Treasury Management policy statement for 2022/23 is set out in Section 5.

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**RECOMMENDATION** The Fire Authority is recommended to:

(i) approve the treasury management strategy and policy statement for 2022/23 (and adopt for the remainder of 2021/22);

(ii) determine that for 2022/23 the Authorised Limit for borrowing shall be £12.767m;

(iii) adopt the prudential indicators as set out in the attached Appendix 2;

(iv) approve the Minimum Revenue Provision (MRP) Statement for 2022/23 as set out in the attached Appendix 3; and

(v) approve the Annual Investment strategy for 2022/23 as set out in Section 5 including the additional consideration of Environmental, Social and Governance (ESG) factors.

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## 1. INTRODUCTION

1.1 The CIPFA Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") requires authorities to set the Treasury Management Strategy Statement (TMSS) for borrowing and to prepare an Investment Strategy each financial year. CIPFA has defined Treasury Management as:

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

1.2 This strategy takes into account the impact of the Authority's Revenue Budget, Medium Term Capital Programme and the Balance Sheet position. The Prudential Indicators and the outlook for interest rates are also considered within the strategy.

1.3 The Treasury Management Strategy for 2022-23 covers the following areas:

- economic overview (section 2);
- the treasury position (section 3);

- the borrowing strategy to finance the capital plans (section 4);
- the investment strategy (section 5);
- MRP strategy (section 6); and
- policy on use of external service provider (section 7).

1.4 The Authority 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. The Treasury Management Scheme of Delegation is shown in Appendix 1.

## 2. ECONOMIC OVERVIEW

2.1 The Authority uses Link Asset Services as its treasury advisor and part of their service is to assist the Authority to formulate a view on interest rates. Table 1 below gives the Link Asset Services central view for short term (Bank Rate) and fixed term borrowing rates.

**Table 1**

| Annual Average % | Bank Rate % | PWLB Borrowing Rates % (including certainty rate adjustment) | | |
|---|---|---|---|---|
| | | 5 year | 25 year | 50 year |
| Mar 2022 | 0.25 | 1.50 | 1.90 | 1.70 |
| Jun 2022 | 0.50 | 1.50 | 2.00 | 1.90 |
| Sep 2022 | 0.50 | 1.60 | 2.10 | 1.90 |
| Dec 2022 | 0.50 | 1.60 | 2.10 | 1.90 |
| Mar 2023 | 0.75 | 1.70 | 2.20 | 2.00 |
| Jun 2023 | 0.75 | 1.80 | 2.20 | 2.00 |
| Sep 2023 | 0.75 | 1.80 | 2.20 | 2.00 |
| Dec 2023 | 0.75 | 1.80 | 2.30 | 2.10 |
| Mar 2024 | 1.00 | 1.90 | 2.30 | 2.10 |
| Jun 2024 | 1.00 | 1.90 | 2.40 | 2.20 |

2.2 Over the last two years, the coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16 December 2021. As shown in Table 1 above, the forecast for Bank Rate now includes four increases, one in December 2021 to 0.25%, then quarter 2 of 2022 to 0.50%, quarter 1 of 2023 to 0.75%, quarter 1 of 2024 to 1.00% and, finally, one in quarter 1 of 2025 to 1.25%.

2.3 The current economic outlook and structure of market interest rates and government debt yields have several key treasury management implications:

- Investment returns are expected to improve in 2022/23. However, while markets are pricing in a series of Bank Rate hikes, actual economic circumstances may see the Monetary Policy Committee (MPC) fall short of these elevated expectations.

- Borrowing interest rates fell to historically very low rates as a result of the COVID crisis and the quantitative easing operations of the Bank of England and still remain at historically low levels.

- While the Fire Authority will not be able to avoid borrowing to finance new capital expenditure, to replace maturing debt and the rundown of reserves, 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.

## 3. TREASURY MANAGEMENT POSITION

3.1 The Authority's projected debt portfolio position at 31 March 2022, with forward estimates is summarised in Table 2 below. The table shows the actual external borrowing (the treasury management operations), against the capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

**Table 2**

| | **2021/22** | **2022/23** | **2023/24** | **2024/25** |
|---|---|---|---|---|
| | **Projected** | **Estimate** | **Estimate** | **Estimate** |
| | **£000** | **£000** | **£000** | **£000** |
| **External Debt** | | | | |
| Debt at 1 April | 10,698 | 10,298 | 9,910 | 14,386 |
| New Debt | - | 93 | 4,876 | 3,516 |
| Maturing Debt | (400) | (481) | (400) | (402) |
| **Actual external debt at 31 March** | **10,298** | **9,910** | **14,386** | **17,500** |
| ***CFR – the borrowing need** | **10,298** | **9,910** | **14,386** | **17,500** |
| **Under/(over) borrowing** | **-** | **-** | **-** | **-** |

**The Authority's Capital Financing Requirement (CFR) is the total historical outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is a measure of the Authority's underlying borrowing need. Any capital expenditure, which has not immediately been paid for, will increase the CFR. CFR in Table 2 is the underlying need to borrow and excludes PFI and lease arrangements, which are included in the CFR figure in the Prudential Indicators in Appendix 2*

3.2 Within the set of prudential indicators there are a number of key tests to ensure that the Authority operates its activities within well-defined limits. One of these is that the Authority needs to ensure that its total borrowing, 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 current and next two financial years.

3.3 The CFR forecast at the end of 2022/23 is £9.910m. The Authority is required to repay an element of the CFR each year through a revenue charge called the minimum revenue provision (MRP).

3.4 The Authority has a number of long-term loans and could aim to reschedule these loans if interest rates increase and the premature repayment rates become favourable.

3.5 Any future loans will be arranged giving consideration to the various debt repayment options, including an Equal Instalments of Principal (EIP) arrangement, where each payment includes an equal amount in respect of loan principal. Therefore the interest due with each payment reduces as the principal is eroded, and the total amount reduces with each instalment.

## 4. BORROWING STRATEGY

4.1 The net borrowing requirement within Table 2 above shows that, based on current estimates, the Authority will need to consider recommencing borrowing in the short to medium term in order to fund its Capital Strategy. However any future new borrowing taken out will be completed with regard to the limits, indicators, the economic environment, the cost of carrying this debt ahead of need, and interest rate forecasts set out above. The Assistant Director Resources/Treasurer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances.

### Policy on Borrowing in Advance of Need

4.2 The Authority will not borrow 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 Authority can ensure the security of such funds.

4.3 Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the reporting mechanism.

### Revised Prudential & Treasury Codes

4.4 CIPFA published revised prudential and treasury codes on 20th December 2021 and has stated that formal adoption is not required until the 2023/24 financial year. The Fire Authority has to have regard to these codes of practice when it prepares the Treasury Management Strategy Statement and Annual Investment Strategy, and also related reports during the financial year, which are taken to the Fire Authority for approval.

4.5 The revised codes will have the following implications:

- a requirement for the Authority to adopt a new debt liability benchmark treasury indicator to support the financing risk management of the capital financing requirement;
- clarify what CIPFA expects a local authority to borrow for and what they do not view as appropriate. This will include the requirement to set a proportionate approach to commercial and service capital investment;
- address ESG issues within the Capital Strategy;
- require implementation of a policy to review commercial property on an annual basis, with a view to divest where appropriate;

- create new Investment Practices to manage risks associated with non-treasury investment (similar to the current Treasury Management Practices);
- ensure that any long term treasury investment is supported by a business model;
- a requirement to effectively manage liquidity and longer term cash flow requirements;
- amendment to Treasury Management Practice 1 (TMP1) to address ESG policy within the treasury management risk framework;
- amendment to the knowledge and skills register for individuals involved in the treasury management function - to be proportionate to the size and complexity of the treasury management conducted by each authority;
- a new requirement to clarify reporting requirements for service and commercial investment, (especially where supported by borrowing/leverage).

4.6 In addition, all investments and investment income must be attributed to one of the following three purposes:

**Treasury management -** Arising from the organisation's cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.

**Service delivery -** Investments held primarily and directly for the delivery of public services including housing, regeneration and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in cases where the income is "either related to the financial viability of the project in question or otherwise incidental to the primary purpose".

**Commercial return -** Investments held primarily for financial return with no treasury management or direct service provision purpose. Risks on such investments should be proportionate to a authority's financial capacity – i.e., that 'plausible losses' could be absorbed in budgets or reserves without unmanageable detriment to local services. An authority must not borrow to invest primarily for financial return.

4.7 Members will be updated on how all these changes will impact our current approach and any changes required will be formally adopted within the 2023/24 TMSS report.

4.8 A full set of Prudential Indicators and borrowing limits is shown in Appendix 2.

**Debt Rescheduling**

4.9 Rescheduling of current borrowing in the current debt portfolio is unlikely to be an option during 2022/23. This is due to a difference between the rate used to calculate the premature redemption, and the rates used to take on new borrowing. This difference would create a premium that the authority would have to pay that would make it more expensive to repay or restructure than retain the debt

4.10 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;
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

4.11 Consideration will also be given to identifying 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.

4.12 All debt rescheduling will be agreed by the Assistant Director Resources / Treasurer.

**Sensitivity of the Forecast and Risk Analysis**

4.13 Treasury management risks are identified in the Authority's approved Treasury Management Practices, the main risks to the Authority's treasury activities are:

- liquidity risk (inadequate cash resources);
- market or interest rate risk (fluctuations in interest rate levels and thereby in the value of investments);
- inflation risks (exposure to inflation);
- credit and counterparty risk (security of investments);
- refinancing risks (impact of debt maturing in future years); and
- legal and regulatory risk (non-compliance with statutory and regulatory requirements, risk of fraud).

4.14 Officers, in conjunction with the treasury advisers, will monitor these risks closely. Particular focus will be applied to:

the global economy – indicators and their impact on interest rates will be monitored closely. Investment and borrowing portfolios will be positioned according to changes in the global economic climate; counterparty risk – the Authority follows a robust credit worthiness methodology and continues to monitor counterparties and sovereign ratings closely particularly within the Eurozone.

## 5. Investment Strategy

5.1 The Authority's investment policy has regard to the DLUHC's Guidance on Local Government Investments (the Guidance), the 2017 revised CIPFA Treasury Management in Public Services Code of Practice and Link Asset Services Guidance Notes (including CIPFA TM Code). The Authority's investment priorities will be security first, liquidity second, and then return.

### Changes to Investment Strategy

5.2 It is recommended where possible, to actively seek to support Environmental, Social and Governance (ESG) investment products and institutions that satisfy all the underlying key principals of Security, Liquidity and Yield in that order.

5.3 The market for green and broader ESG investments is still relatively immature. However, research and the consideration of the suitability of ESG investment products will continue into 2022/23. An investment of £1m in a Standard Chartered ESG product has been made in 2021/22.

5.4 No further changes are proposed to the Investment Strategy for 2022/23.

### Sovereign Credit Ratings

5.5 The Authority has determined that it will only use approved counterparties based in the UK. The UK currently holds an AA sovereign rating. However the credit rating agencies will be carefully monitoring the rate of growth in the economy as a disappointing performance in that area could lead to a major derailment of the plans to contain the growth in the total amount of Government debt over the next few years.

### Credit Worthiness Policy

5.6 Officers regularly review the investment portfolio, counterparty risk and construction, market data, information on government support for banks and the credit ratings of that government support. Latest market information is arrived at by reading the financial press and through city contacts as well as access to the key brokers involved in the London money markets.

5.7 Additionally, the Authority will make use of the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- credit default swap (CDS) spreads to give early warning of likely changes in credit ratings; and
- sovereign ratings to select counterparties from only the most creditworthy countries.

5.8 The modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative credit worthiness of counterparties. These colour codes are used by the Authority to determine the duration for investments. The strategy provides scope to invest in AAA rated foreign banks. However the Authority proposes to only use counterparties (Appendix 6) within the following durational bands that are domiciled in the UK.

- Yellow 5 years
- Purple 2 years
- Blue 1 year (semi nationalised UK Bank – NatWest/RBS)
- Orange 1 year
- Red 6 months
- Green 3 months
- No Colour Not to be used

| **Y** | **P** | **B** | **O** | **R** | **G** | **N/C** |
|---|---|---|---|---|---|---|
| Up to 5yrs | Up to 2yrs | Up to 1yr | Up to 1yrs | Up to 6 months | Up to 100 days | Not to be used |

5.9 The Link Asset Services credit worthiness service uses a wider array of information than just primary ratings and by using a risk weighted scoring system, does not give undue influence to just one agency's ratings.

5.10 Typically the minimum credit ratings criteria the Authority use, will be a short term rating (Fitch or equivalents) of short term rating F1, long term rating A-, viability rating of A-, and a support rating of 1. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

5.11 All credit ratings will be monitored daily. The Authority is alerted to changes to ratings of all three agencies through its use of the Link Asset Services credit worthiness service.

- if a downgrade results in the counterparty or investment scheme no longer meeting the Authority's minimum criteria, its further use as a new investment will be withdrawn immediately.

- in addition to the use of credit ratings the Authority will be advised of information in movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Authority's lending list.

5.12 The primary principle governing the Authority's investment criteria is the security of its investments, although the return on the investment is also a key consideration. After this main principle, the Authority will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in and the criteria for choosing investment counterparties with adequate security, and monitoring their security;

- It has sufficient liquidity in its investments.
- It receives a yield that is aligned with the level of security and liquidity of its investments
- Where possible, support ESG investment products and institutions that meet all of the above requirements.

The preservation of capital is the Authority's principal and overriding priority.

5.13 The Link Asset Services methodology was revised in October 2014 and determines the maximum investment duration under the credit rating criteria. Key features of Link Asset Services credit rating policy are:

- a mathematical based scoring system is used taking ratings from all three credit rating agencies;
- negative and positive watches and outlooks used by the credit rating agencies form part of the input to determine a counterparty's time band (i.e. 3, 6, 9, 12 months etc.);
- CDS spreads are used in Link Asset Services creditworthiness service as it is accepted that credit rating agencies lag market events and thus do not provide investors with the most instantaneous and "up to date" picture of the credit quality of a particular institution. CDS spreads provide perceived market sentiment regarding the credit quality of an institution;
- After a score is generated from the inputs a maximum time limit (duration) is assigned and this is known as the Link Asset Services colour which is associated with a maximum suggested time boundary.

5.14 The Link Asset Services colours and the maximum time periods are shown para 5.9 above. In the Link Asset Services methodology if counterparty has no colour then they are not recommended for investment and this would remove these counterparties from the Authority's counterparty list.

5.15 Whilst the Link Asset Services methodology categorises counterparty time limits up to two years, the Authority's policy remains only to make investments up to a maximum of one year.

**Specified Investments**

5.16 An investment is a specified investment if all of the following apply:

- the investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling;
- the investment is not a long term investment (i.e. up to 1 year);
- the making of the investment is not defined as capital expenditure by virtue of regulation 25(1)(d) of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 [SI 3146 as amended];

- the investment is made with a body or in an investment scheme of high credit quality (see below) or with one of the following public-sector bodies:
    - The United Kingdom Government;
    - A local authority in England or Wales (as defined under section 23 of the 2003 Act) or a similar body in Scotland or Northern Ireland; and
    - High credit quality is defined as a minimum credit rating as outlined in section 5.11 of this strategy.

5.17 **The use of Specified Investments -** Investment instruments identified for use in the financial year are as follows:

Table 3 below sets out the types of investments that fall into each category, counterparties available to the Authority, and the limits placed on each of these. A detailed list of each investment type is available in the Treasury Management Practices guidance notes;

5.18 Criteria for Specified Investments:

**Table 3**

| Counterparty | Country/ Domicile | Instrument | Min. Credit Criteria LAS/Colour band | Max. Amount* | Max. maturity period |
|---|---|---|---|---|---|
| Debt Management and Depost Facilities (DMADF) | UK | Term Deposits | UK Sovereign Rating | unlimited | 12 months |
| Government Treasury bills | UK | Term Deposits | UK Sovereign Rating | unlimited | 12 months |
| UK Local Authorities | UK | Term Deposits | UK Sovereign Rating | unlimited | 12 months |
| Banks – part nationalised | UK | • TDs<br>• Deposits on Notice<br>• Certificates of Deposit (CDs) | Blue | £6m | 12 Months |
| | | | Orange | £6m | 12 Months |
| | | | Red | £6m | 6 Months |
| | | | Green | £6m | 100 Days |
| Banks | UK | • TDs<br>• Deposits on Notice<br>• CDs | Blue | £6m | 12 Months |
| | | | Orange | £6m | 12 Months |
| | | | Red | £6m | 6 Months |
| | | | Green | £6m | 100 Days |
| Individual Money Market Funds (MMF) CNAV and LVNAV | UK/Ireland/ EU domiciled | AAA Rated Money Market Fund Rating | N/A | £6m | Liquidity/ instant access |
| VNAV MMF's and Ultra Short Dated Bond Funds | UK/Ireland/ EU domiciled | AAA Rated Bond Fund Fund Rating | N/A | £6m | Liquidity |

**No more than 25% of the investment portfolio held with one single counterparty where practically possible.*

### Non Specified Investments

5.19 Non Specified Investments are any other types of investment that are not defined as specified. The identification and rationale supporting the selection of these other investments are set out in Table 4 below:

| Table 4 | Minimum credit criteria | Period |
| --- | --- | --- |
| Local Authorities | Government Backed | 2 years |
| Mixed Asset Fund(s) | N/A | 2 - 5 years |
| Short Dated Bond Fund(s) | N/A | 2 - 5 years |
| Pooled Property Fund(s) | N/A | 5+ years |

The maximum amount that can be invested will be monitored in relation to the Authority's surplus monies and the level of reserves, the limit will be £2.5m across all non specified investments for 2022/23. The approved counterparty list will be maintained by referring to an up-to-date credit rating agency reports, and the Authority will liaise regularly with brokers for updates. Counterparties may be added to or removed from the list only with the approval of the Assistant Director Resources / Treasurer. A detailed list of specified and non-specified investments that form the counterparty list is shown in section 10.

### Investment Position and Use of Authority's Resources

5.20 Investment returns are expected to improve in 2022/23. However, while markets are pricing in a series of Bank Rate hikes, actual economic circumstances may see the MPC fall short of these elevated expectations. Bank rate rises at March in the next 3 years are forecast to be.

- March 2023 0.50%
- March 2024 0.75%
- March 2025 1.25%

5.21 The overall balance of risks to economic growth in the UK is now to the downside, including risks from Covid and its variants - both domestically and their potential effects worldwide.

5.22 The Link Asset Services suggested budgeted investment earnings rates for returns on investments placed for each financial year for the next four years are as follows:

- 2022/23 0.50%
- 2023/24 0.75%
- 2024/25 1.00%
- 2025/26 1.25%

5.23 The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an on-going impact on investments unless resources are supplemented each year from new sources (asset sales etc.).

5.24 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).

## 6. Minimum Revenue Provision

6.1 The Authority is required to repay an element of the CFR through a revenue charge (MRP), although it is also allowed to undertake additional voluntary payments if required.

6.2 DLUHC Regulations have been issued which require the Authority to approve an MRP Statement in advance of each year. A variety of options is provided to authorities, so long as there is a prudent provision. The Authority is recommended to approve the MRP Policy in Appendix 3.

6.3 The Authority, in conjunction with its Treasury Management advisors, has considered the MRP policy to be prudent.

## 7. Policy on the use of External Service Providers

7.1 The Authority uses Link Asset Services as its external treasury management advisors.

7.2 The Authority recognises that responsibility for treasury management decisions remains with the Authority at all times and will ensure that undue reliance is not placed upon our external service providers.

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

## 8. Update to Accounting Requirements

### 8.1 IFRS 9 – Financial Instruments

- **IFRS9 – local authority override – English local authorities**

The DLUHC enacted a statutory over-ride from 1 April 2018 for a five year period until 31 March 2023 following the introduction of IFRS 9 and the requirement for any capital gains or losses on marketable funds to be chargeable in year. This has the effect of allowing any capital losses on funds to be held on the balance sheet until 31 March 2023, allowing councils to initiate an orderly withdrawal of funds if required.

The Authority does not hold any investments that are catergorisrd as in-scope of the statutory over-ride and therefore there is no impact on the Authority of these changes.

- **IFRS 16 – Leasing**

The CIPFA Code of Practice will incorporate the requirement to account for all leases onto the council's balance sheet from 2022/23 onwards.

Once implemented, this has the following impact to the Treasury Management Strategy:

- The MRP Policy sets out how MRP will be applied for leases bought onto the balance sheet;
- The Authority's Capital Financing Requirement authorised limit and operational boundary for 2022/23 onwards has been increased to reflect the estimated effect of this change. These limits can be amended during 2022/23 if required.

**APPENDIX 1**

**Treasury Management Scheme of Delegation**

**1. Fire Authority**

1.1 In line with best practice, the Fire Authority is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of polices, estimates and actuals. These reports are:

**a) Prudential and Treasury Indicators and Treasury Strategy (This report)**
The first and most important report covers:
- the capital plans (including prudential indicators);
- the Capital Strategy
- a Minimum Revenue Provision 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).

**b) A Mid-Year Treasury Management Report** – This will update members with the progress of the capital position, amending prudential indicators as necessary, and indicating whether the treasury strategy is meeting the strategy or whether any policies require revision.

**c) An Annual Treasury Management Stewardship Report** – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

**2. The Treasury Management Role of the Section 112 Officer**

2.1 The Section 112 (responsible) Officer (the fire service equivalent to the S151 Officer in local government):
- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit; and
- recommending the appointment of external service providers.

3. Training **-** Treasury Management training for Authority members will be delivered as required to facilitate more informed decision making and challenge processes.

**APPENDIX 2**

## 1. The Prudential and Treasury Indicators

1.1 The Fire Authority's capital expenditure plans are the key driver of treasury management activity. The outputs of the capital expenditure plans are reflected in prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

1.2 **Capital Expenditure**. This prudential Indicator shows the Authority's capital expenditure plans; both those agreed previously, and those forming part of this budget cycle. Capital expenditure excludes spend on PFI and leasing arrangements, which are now shown on the balance sheet.

1.3 The table below summarises the capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding need (borrowing).

**Table 5**

| **Description** | **2021/22 Projected** | **2022/23 Estimate** | **2023/24 Estimate** | **2024/25 Estimate** |
|---|---|---|---|---|
| | **£m** | **£m** | **£m** | **£m** |
| **Capital Expenditure** | 2.682 | 7.250 | 5.824 | 4.641 |
| Capital receipts | (2.483) | (4.017) | - | - |
| Capital grants & Contributions | - | - | - | - |
| Revenue Financing | (0.085) | - | - | - |
| Capital Reserves | - | (3.209) | (0.952) | (0.952) |
| Other Reserves | (0.086) | - | - | - |
| **Borrowing Need*** | **0.028** | **0.024** | **4.872** | **3.689** |

*prior to MRP deducted

1.4 The Authority's borrowing need (the Capital Financing Requirement) - The second prudential indicator is the Authority's Capital Financing Requirement (CFR). The CFR is simply 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 Authority's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR.

1.5 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.

1.6 Following accounting changes for 2022/23, the CFR will include any other long term liabilities (e.g. PFI schemes, finance leases) brought on the balance sheet. Whilst these increase the CFR, and therefore the Authority's borrowing requirement, these types of scheme include a borrowing facility and so the Authority is not required to separately borrow for these schemes. The Authority has no PFI Schemes, and work is being undertaken during 2022/23 to identify where the Authority holds finance leases. Tables 6, 7 and 8 include an estimate for finance leases that will be bought onto the balance sheet during the year.

**Table 6**

| | 2021/22 Projected | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|
| **Capital Financing Requirement** | | | | |
| | **£m** | **£m** | **£m** | **£m** |
| Opening CFR | 10.698 | 10.298 | 11.910 | 15.386 |
| Borrowing Need (table 5 as above) | 0.028 | 0.024 | 4.872 | 3.689 |
| MRP | (0.428) | (0.412) | (0.396) | (0.575) |
| Lease Liabilities | | 2.000 | | |
| **Closing CFR** | **10.298** | **11.910** | **15.386** | **19.500** |

1.7 **The Operational Boundary.** This is the limit beyond which external borrowing 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 borrowing.

**Table 7**

| Description | 2021/22 Projected | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|
| | **£m** | **£m** | **£m** | **£m** |
| Borrowing | 11.766 | 10.378 | 14.854 | 17.968 |
| PFI/Leases | - | 2.000 | 2.000 | 2.000 |
| **Total** | **11.766** | **12.378** | **16.854** | **19.968** |

1.8 **The Authorised Limit for external borrowing**. A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external borrowing is prohibited, and this limit needs to be set or revised by the full Authority. It reflects the level of external borrowing 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 authority's plans, or those of a specific authority, although this power has not yet been exercised; and
- The Authority is asked to approve the following Authorised Limit:

**Table 8**

| Description | 2021/22 Projected | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|
| | **£m** | **£m** | **£m** | **£m** |
| Borrowing | 14.155 | 12.767 | 17.243 | 19.968 |
| PFI/Leases | - | 2.000 | 2.000 | 2.000 |
| **Total** | **14.155** | **14.767** | **19.243** | **21.968** |

## 2. Treasury Management Limits on Activity

2.1 There are three debt related treasury activity limits. The purpose of these are 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. However, if these are set to be too restrictive they will impair the opportunities to reduce costs or improve performance. 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 Authority's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

**Table 9**

| **Maturity structure of fixed interest rate borrowing 2022/23**<br><br>All Fire Authority borrowing is at a Fixed Rate | | | |
|---|---|---|---|
| | **Lower** | **Upper** | **Actual** |
| Under 12 months | 0% | 25% | 0% |
| 12 months to 2 years | 0% | 40% | 7% |
| 2 years to 5 years | 0% | 60% | 11% |
| 5 years to 10 years | 0% | 80% | 26% |
| 10 years to 20 years | 0% | 80% | 19% |
| 20 years to 30 years | 0% | 80% | 3% |
| 30 years to 40 years | 0% | 80% | 34% |
| 40 years to 50 years | 0% | 80% | 0% |

**Table 10**

| **Principle sums invested for periods longer than 365 days** | | | |
|---|---|---|---|
| | **2022/23 £m** | **2023/24 £m** | **2024/25 £m** |
| Limit | 2.50 | 1.00 | 0.50 |

The above limits are deemed prudent and will be reviewed in future years.

2.2 **Affordability Prudential Indicators -** 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 Authority's overall finances. The Authority is asked to approve the following indicators:

2.3 **Actual and estimates of the 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. The estimates of financing costs include current commitments and the proposals in this budget report.

**Table 11**

| **Description** | **2021/22 Projected** | **2022/23 Estimate** | **2023/24 Estimate** | **2024/25 Estimate** |
|---|---|---|---|---|
| | **%** | **%** | **%** | **%** |

| | | | | |
|---|---|---|---|---|
| **Ratio** | 2.14 | 2.08 | 2.05 | 2.58 |

## 3. Treasury Management Budget

**Table 12**

| **Description** | **2021/22** | **2022/23** | **2023/24** | **2024/25** |
|---|---|---|---|---|
| | **£m** | **£m** | **£m** | **£m** |
| Interest Payable | 0.483 | 0.474 | 0.499 | 0.586 |
| Interest Receipts | (0.040) | (0.020) | (0.010) | (0.010) |
| Minimum Revenue Provision | 0.428 | 0.412 | 0.396 | 0.575 |
| **TOTAL** | **0.871** | **0.866** | **0.885** | **1.151** |

**APPENDIX 3**

**Minimum Revenue Provision Policy Statement**

## 1. Policy Statement

1.1 The statutory requirement for local authorities to charge the Revenue Account each year with a specific sum for debt repayment has been replaced with a more flexible statutory guidance. A variety of options is provided to authorities to replace the existing Regulations, so long as there is a prudent provision.

1.2 The statutory duty is that a local authority shall determine for the financial year an amount of minimum revenue provision (MRP) that it considers to be prudent. This replaces the previous prescriptive requirement that the minimum sum should be 4% of the Authority's Capital Financing Requirement (CFR).

1.3 To support the statutory duty the Government also issued a guidance, which requires that a Statement on the Authority's policy for its annual MRP should be submitted to The Fire Authority for approval before the start the financial year to which the provision will relate. The Authority is therefore legally obliged to have regard to this MRP guidance in the same way as applies to other statutory guidance such as the CIPFA Prudential Code, the CIPFA Treasury Management Code and the DLUHC guidance on Investments.

1.4 The MRP guidance offers four options under which MRP might be made, with an overriding recommendation that The Fire Authority should make 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).

1.5 The guidance also requires an annual review of MRP policy being undertaken and it is appropriate that this is done as part of this Annual Treasury Management Strategy.

1.6 The move to International Financial Reporting Standards (IFRS) involves Private Finance Initiative (PFI) contracts and potentially some leases (being reclassified as finance leases instead of operating leases) coming onto the Balance Sheet as long term liabilities. The accounting treatment would impact on the Capital Financing Requirement with the result that an annual MRP provision would be required.

1.7 To ensure that this change has no overall financial impact on Local Authorities, the Government has updated their "Statutory MRP Guidance" which allows MRP to be equivalent to the existing lease rental payments and "capital repayment element" of annual payments to PFI Operators. There are no implications for the Authority's MRP policy.

The policy for 2022/23 is therefore as follows:-

1.8 For capital expenditure incurred before 1 April 2008 or which in the future will be Government Supported Capital Expenditure, the MRP policy will be:

- Based on based on the non-housing CFR, i.e., The Authority currently set aside a Minimum Repayment Provision based on basic MRP of 4% each year to pay for past capital expenditure and to reduce its CFR.

1.9 From 1 April 2008 for all unsupported borrowing the MRP policy will be:

- Asset Life Method – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations (this option will be applied for any expenditure capitalised under a Capitalisation Direction).

- For all leases coming onto the balance sheet, Asset Life Method (annuity method) – will be used. The MRP will be calculated according to the flow of benefits from the asset, and where the principal repayments increase over the life of the asset. Any related MRP will be equivalent to the "capital repayment element" of the annual charge payable.

Under both methods, the Authority has the option to charge more than the statutory MRP each year through a Voluntary Revenue Provision (VRP).

1.10 This approach also allows the Authority to defer the introduction of an MRP charge for new capital projects/land purchases until the year after the new asset becomes operational rather than in the year borrowing is required to finance the capital spending. This approach is beneficial for projects that take more than one year to complete and is therefore included as part of the MRP policy. Half-yearly review of the Authority's MRP Policy will be undertaken and reported to Members as part of the Half-yearly Treasury Management Strategy review.

1.11 The government are currently consulting Local Authorities on proposed changes to the MRP guidance. Whilst the changes are not expected to impact on the Fire Authority, officers will be reviewing the Authority's MRP policy during 2022/23 in light of these changes and the increase in the Authority's borrowing need to ensure the MRP policy remains appropriate.

**APPENDIX 4**

The list below shows the countries that would currently meet these criteria:

AAA

- Australia
- Denmark
- Germany
- Netherlands
- Singapore
- Sweden
- Switzerland

AA+

- Canada

AA

- U.K.

*Note: There are three other countries with AA, but the Authority will only be using UK because of the best understanding of the UK market.*

**APPENDIX 5**

## Economic Overview

**Provided Link Assets Services (our Treasury advisors) January 2022**

### 1. The UK

1.1 The Bank of England MPC confounded market expectations for a second consecutive meeting in December, raising Bank Rate by 0.15% to 0.25%. In doing so, it became the first major central bank to raise official policy rates since the onset of the pandemic.

1.2 The Committee voted 8-1 for the change in the policy rate with only well-established "dove", Silvana Tenreyro, dissenting. Meanwhile, the Committee voted unanimously to keep the current QE programme unchanged. The minutes showed that the Bank now expects inflation to peak at 6% in April, and while Omicron was already having an impact on some sectors, the Committee felt it had to act now because it saw "some signs of greater persistence in domestic costs and price pressures". It also stressed how it had stated at its November meeting that it would raise rates if the economy evolved as expected and that "these conditions had been met".

1.3 Looking ahead, unlike in November, there was no references to inflation being expected to be below the 2% target over its forecast period, which may suggest that the Committee is contemplating raising rates further than it had been at its previous meeting.

1.4 While this may underpin market expectations that Bank Rate will rise to 1% in the second half of 2022, the minutes also retained the comment that a "modest tightening" in policy will be required over its 3yr forecast period. Further, it did caveat that inflation could yet prove weaker or stronger than expected. Market expectations for future hikes have increased in the aftermath of the result, with the potential for the next hike in Q1 2022, with a move to 0.75% by May and the 1% level being hit in August / September, compared to November ahead of the meeting. By the close of 2022, markets are now edging nearer to a 1.25% level, with this expectation having picked up since the start of trading this year.

1.5 Link has formally reviewed its own forecast in light of the December meeting but has made no change to its Bank Rate forecast, with just modest changes to expectations for longer term yields which are reflected in the table below. Typically, a rate hike would fully flow through market pricing, especially at the short end of the curve.

### 2. Link Asset Services forward view January 2022

2.1 It is not expected that Bank Rate will go up fast after the initial rate rise as the supply potential of the economy is not likely to have taken a major hit during the pandemic: it should, therefore, be able to cope well with meeting demand after supply shortages subside over the next year, without causing inflation to remain elevated in the medium-term, or to inhibit inflation from falling back towards the MPC's 2% target after the spike up to around 5%. The forecast includes four increases in Bank Rate over the three-year forecast period to March 2025, ending at 1.25%. However, it is likely that these forecasts will need changing within a relatively short timeframe for the following reasons: -

- We do not know how severe an impact Omicron could have on the economy and whether there will be another lockdown or similar and, if there is, whether there would be significant fiscal support from the Government for businesses and jobs.

- There were already increasing grounds for viewing the economic recovery as running out of steam during the autumn and now into the winter. And then along came Omicron to pose a significant downside threat to economic activity. This could lead into stagflation, or even into recession, which would then pose a dilemma for the MPC as to whether to focus on combating inflation or supporting economic growth through keeping interest rates low.

- Will some current key supply shortages spill over into causing economic activity in some sectors to take a significant hit.

- Rising gas and electricity prices in October and next April and increases in other prices caused by supply shortages and increases in taxation next April, are already going to deflate consumer spending power without the MPC having to take any action on Bank Rate to cool inflation.

- On the other hand, consumers are sitting on over £160bn of excess savings left over from the pandemic so when will they spend this sum, in part or in total.

- It looks as if the economy coped well with the end of furlough on 30th September. It is estimated that there were around 1 million people who came off furlough then and there was not a huge spike up in unemployment. The other side of the coin is that vacancies have been hitting record levels so there is a continuing acute shortage of workers. This is a potential danger area if this shortage drives up wages which then feed through into producer prices and the prices of services i.e., a second-round effect that the MPC would have to act against if it looked like gaining significant momentum.

- We also recognise there could be further nasty surprises on the Covid front beyond the Omicron mutation.

- If the UK invokes article 16 of the Brexit deal over the dislocation in trading arrangements with Northern Ireland, this has the potential to end up in a no-deal Brexit.

2.2 In summary, with the high level of uncertainty prevailing on several different fronts, we expect to have to revise our forecasts again - in line with whatever the new news is.It should also be borne in mind that Bank Rate being cut to 0.25% and then to 0.10%, were emergency measures to deal with the Covid crisis hitting the UK in March 2020. At any time, the MPC could decide to simply take away such emergency cuts on no other grounds than they are no longer warranted, and as a step forward in the return to normalisation. In addition, any Bank Rate under 1% is both highly unusual and highly supportive of economic growth.

2.3 **Forecasts for PWLB rates and gilt and treasury yields**

Since the start of 2021, we have seen a lot of volatility in gilt yields, and hence PWLB rates. As the interest forecast table for PWLB certainty rates above shows, there is forecast to be a steady, but slow, rise in both Bank Rate and gilt yields during the forecast period to March 2025, though there will doubtless be a lot of unpredictable volatility during this forecast period.

2.4 While monetary policy in the UK will have a major impact on gilt yields, there is also a need to consider the potential impact that rising treasury yields in America could have on our gilt yields. As an average since 2011, there has been a 75% correlation between movements in US 10-year treasury yields and UK 10-year gilt yields. This is a significant upward RISK exposure to our forecasts for longer term PWLB rates. However, gilt yields and treasury yields do not always move in unison.

2.5 There are also possible downside risks from the huge sums of cash that the UK populace have saved during the pandemic; when savings accounts earn little interest, it is likely that some of this cash mountain could end up being invested in bonds and so push up demand for bonds and support their prices i.e., this would help to keep their yields down. How this will interplay with the Bank of England eventually getting round to not reinvesting maturing gilts and then later selling gilts, will be interesting to monitor.

2.6 There is likely to be exceptional volatility and unpredictability in respect of gilt yields and PWLB rates due to the following factors: -

- How strongly will changes in gilt yields be correlated to changes in US treasury yields (see below). Over 10 years since 2011 there has been an average 75% correlation between movements in US treasury yields and gilt yields. However, from time to time these two yields can diverge. Lack of spare economic capacity and rising inflationary pressures are viewed as being much greater dangers in the US than in the UK. This could mean that central bank rates will end up rising earlier and higher in the US than in the UK if inflationary pressures were to escalate; the consequent increases in treasury yields could well spill over to cause (lesser) increases in gilt yields. There is, therefore, an upside risk to forecasts for gilt yields due to this correlation. The Link Group forecasts have included a risk of a 75% correlation between the two yields.

- Will the Fed take action to counter increasing treasury yields if they rise beyond a yet unspecified level.

- Would the MPC act to counter increasing gilt yields if they rise beyond a yet unspecified level.

- How strong will inflationary pressures actually turn out to be in both the US and the UK and so put upward pressure on treasury and gilt yields.

- How will central banks implement their new average or sustainable level inflation monetary policies.

- How well will central banks manage the withdrawal of QE purchases of their national bonds i.e., without causing a panic reaction in financial markets as happened in the “taper tantrums” in the US in 2013

- Will exceptional volatility be focused on the short or long-end of the yield curve, or both.

2.7 The forecasts are also predicated on an assumption that there is no break-up of the Eurozone or EU within the forecasting period, despite the major challenges that are looming up, and that there are no major ructions in international relations, especially between the US and China / North Korea and Iran, which have a major impact on international trade and world GDP growth.

2.8 **The balance of risks to medium to long term PWLB rates: -**

There is a balance of upside risks to forecasts for medium to long term PWLB rates.
A new era – a fundamental shift in central bank monetary policy

- One of the key results of the pandemic has been a fundamental rethinking and shift in monetary policy by major central banks like the Fed, the Bank of England and the ECB, to tolerate a higher level of inflation than in the previous two decades when inflation was the prime target to bear down on so as to stop it going above a target rate. There is now also a greater emphasis on other targets for monetary policy than just inflation, especially on 'achieving broad and inclusive "maximum" employment in its entirety' in the US, before consideration would be given to increasing rates.

- The Fed in America has gone furthest in adopting a monetary policy based on a clear goal of allowing the inflation target to be symmetrical, (rather than a ceiling to keep under), so that inflation averages out the dips down and surges above the target rate, over an unspecified period.

- The Bank of England has also amended its target for monetary policy so that inflation should be 'sustainably over 2%' before starting on raising Bank Rate and the ECB now has a similar policy.

- For local authorities, this means that investment interest rates and very short term PWLB rates will not be rising as quickly or as high as in previous decades when the economy recovers from a downturn and the recovery eventually runs out of spare capacity to fuel continuing expansion.

- Labour market liberalisation since the 1970s has helped to break the wage-price spirals that fuelled high levels of inflation and has now set inflation on a lower path which makes this shift in monetary policy practicable. In addition, recent changes in flexible employment practices, the rise of the gig economy and technological changes, will all help to lower inflationary pressures.

- Governments will also be concerned to see interest rates stay lower as every rise in central rates will add to the cost of vastly expanded levels of national debt; (in the UK this is £21bn for each 1% rise in rates

# APPENDIX 6

| Bank with duration colour | Country | Fitch Ratings | | | | Moody's Ratings | | S & P Ratings | | CDS Price | ESFA Duration | Link Duration Limit | Money Limit |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Specified Investments:** | | L Term | S Term | Viab. | Supp. | L Term | S Term | L Term | S Term | | (Months) | (Months) | (£m) |
| **Lloyds Banking Group:** | | | | | | | | | | | | | |
| Lloyds Bank | UK | A+ | F1 | a | 5 | A1 | P-1 | A+ | A-1 | 35.56 | 6 | 6 | 6 |
| Bank of Scotland | UK | A+ | F1 | a | 5 | A1 | P-1 | A+ | A-1 | 42.64 | 6 | 6 | |
| **RBS/NatWest Group:** | | | | | | | | | | | | | |
| NatWest Bank | UK | A+ | F1 | a | 5 | A1 | P-1 | A | A-1 | - | 12 | 12 | 6 |
| Royal Bank of Scotland | UK | A+ | F1 | a | 5 | A1 | P-1 | A | A-1 | - | 12 | 12 | |
| HSBC Bank | UK | AA- | F1+ | a | 1 | A1 | P-1 | A+ | A-1 | 39.03 | 12 | 12 | 6 |
| Barclays Bank | UK | A+ | F1 | a | 5 | A1 | P-1 | A | A-1 | 53.97 | 6 | 6 | 6 |
| Santander (UK) | UK | A+ | F1 | a | 2 | A1 | P-1 | A | A-1 | - | 6 | 6 | 6 |
| Goldman Sachs IB | UK | A+ | F1 | - | 1 | A1 | P-1 | A+ | A-1 | 38.03 | 6 | 6 | 6 |
| Standard Chartered Bank | UK | A+ | F1 | a | 5 | A1 | P-1 | A | A-1 | 32.32 | 6 | 6 | 6 |
| Handelsbanken (UK) PLC | UK | AA | F1+ | - | 1 | - | - | A+ | A-1+ | - | 12 | 12 | 6 |

| *Yellow* | *Purple* | *Blue* | *Orange* | *Red* | *Green* | *No Colour* |
|---|---|---|---|---|---|---|
| | | | | | | |
| *Up to 5yrs* | *Up to 2yrs* | *Up to 1yr (semi nationalised UK banks)* | *Up to 1yr* | *Up to 6 months* | *Up to 100 days* | *Not to be used* |

| Non Specified Investments: | Minimum credit criteria | Period |
|---|---|---|
| Local Authorities | Government Backed | 2 years |
| Mixed Asset Fund(s) | N/A | 2 - 5 years |
| Short Dated Bond Fund(s) | N/A | 2 - 5 years |
| Pooled Property Fund(s) | N/A | 5+ years |

**APPENDIX 7**

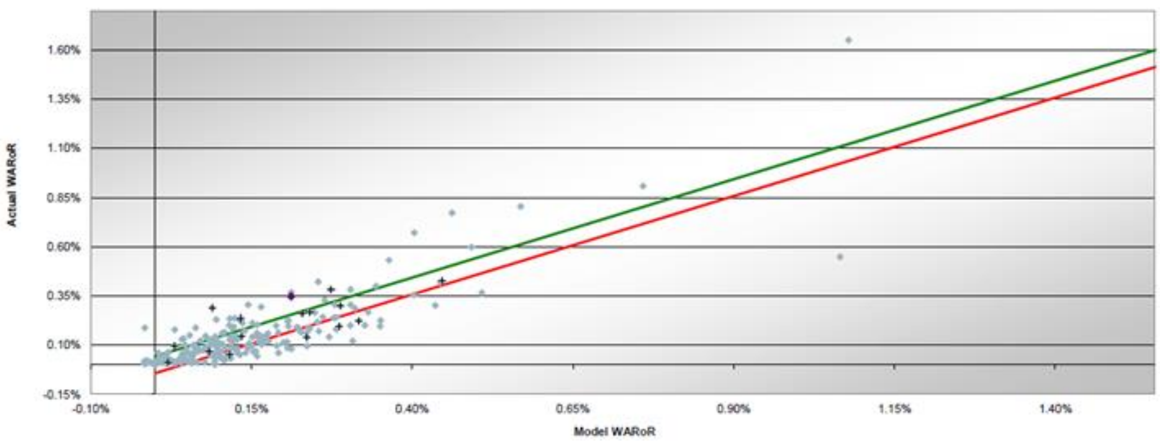
## Investment Benchmarking

### 1 Investment Benchmarking

1.1 The Authority has access to Investment benchmarking results from its Treasury Advisors Link Asset Services (LAS). Officers attend two annual meetings to review performance and compare to peers within the South East Region (group 8).

1.2 Local Authority Investment benchmarking returns to September 2021.

Population Returns against Model Returns




1.3 The cluster graph above shows that the rate of return grouping for Local Authorities is within a range of 0.05 - 0.40% which is broadly consistent with returns achieved by this Authority. As at December 2020 £41k was earned in investment interest at an average rate of 0.23%.

1.4 Fire Authority Investment returns 2021/22 to date:

| 2020/21 | Return (%) | Base Rate (%) | +/- (%) |
|---|---|---|---|
| April | 0.26 | 0.10 | +0.16 |
| May | 0.27 | 0.10 | +0.17 |
| June | 0.28 | 0.10 | +0.18 |
| July | 0.27 | 0.10 | +0.17 |
| August | 0.23 | 0.10 | +0.13 |
| September | 0.23 | 0.10 | +0.13 |
| October | 0.22 | 0.10 | +0.12 |
| November | 0.15 | 0.10 | +0.05 |
| December | 0.19 | 0.18* | +0.01 |

*Average Base Rate in Month

**APPENDIX 8**

**Investment Product Glossary**

**Bank / Building Society**: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail.

**Bank / Building Society Secured (Covered Bonds):** These investments are secured on the bank's assets, which limit the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in.

**Corporate Bonds:** Bonds issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent.

**Enhanced Cash / Ultra Short Dated Bond Funds:** Funds designed to produce an enhanced return over and above a Money Market Fund. The manager may use a wider range of alternative options to try and generate excess performance. These could include different counterparties, instruments as well as longer dated investments.

**Equity Fund:** Equity funds are pooled investment vehicles that will focus investments primarily in UK equities.

**Government:** Loans, bonds and bills issued or guaranteed by UK government, local authorities and supranational banks. These investments are not subject to bail-in, and there is a minimal risk of insolvency.

**Money Market Funds:** An open ended fund that invests in short term debt securities, offers same-day liquidity and very low volatility.

**Mixed Asset Funds:** Rather than focus on a particular asset class, these funds will look to invest across a broader range of classes in an effort to provide investors with a smoother performance on a year-to-year basis. Primarily, the asset classes will be equities and fixed income, but the latter will include both corporate and government-level investments.

**Pooled Property Funds:** Shares in diversified property investment vehicles. Property funds offer enhanced returns over the longer term, but are more volatile in the short term. The funds have no defined maturity date, but are available for withdrawal after a notice period

**Short Dated Bond Funds:** Funds designed to produce an enhanced return over and above an Ultra Short Dated Fund. The manager may use a wider range of alternative options to try and generate excess performance. These could include different counterparties, instruments as well as longer dated and a proportion of lower rated investments. The return on the funds are typically much higher, but can be more volatile than Ultra-Short Dated bond funds, so a longer investment time horizon is recommended.