



Herefordshire Council

Treasury Management Strategy
2022/23 – 2025/26

Treasury Management Strategy 2022-26

Herefordshire Council

Treasury Management Strategy 2022/23-2025/26

Contents

1. Introduction
2. Summary of Strategy for 2022/23
3. Economic Background and Interest Rate Forecast
4. Capital Financing Requirement
5. Borrowing Strategy
6. Annual Investment Strategy
7. Annual Minimum Revenue Provision Statement 2022/23

Annex

- a. Existing Borrowing and Investments
- b. Borrowing Maturity Profile
- c. Prudential and Treasury Indicators for the next four years
- d. Outlook for Interest Rates
- e. Treasury Management Policy Statement

Treasury Management Strategy 2022-26

1. Introduction

- 1.1 Treasury management is the management of the council'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. The council borrows and invests substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to an effective treasury management strategy.
- 1.2 This strategy has been prepared in accordance with the MHCLG Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code and should be considered alongside the council's capital strategy (reported separately). CIPFA published the updated Treasury Management and Prudential Codes on 20th December 2021. CIPFA has stated that there will be a soft introduction of the codes with full implementation required for 2023/24. The new CIPFA codes have adopted a set of restrictions to discourage capital expenditure on commercial investments for yield.
- 1.3 The purpose of this Treasury Management Strategy (TMS) is to approve:
- Treasury Management Strategy for 2022/23-2025/26
 - Borrowing Strategy – Section 5
 - Annual Investment Strategy – Section 6
 - Minimum Revenue Payment (MRP) Policy Statement – Section 7
 - Prudential Treasury Indicators – Annex C
- 1.4 In addition to the TMS, the council maintains treasury management practices that outline how the council's strategic policy objectives for treasury management will be achieved and are supported by schedules that describe the specific procedures to be used by staff involved in treasury management activities. The operational practices are maintained by the corporate finance team and approved by the chief finance officer.

2. Summary of Strategy for 2022/23

- 2.1 The financial market continues to offer low levels of interest rate cost of borrowing and even lower interest rate returns on investments therefore the council continues to aim to minimise the cash balances it maintains. Inflation rising to 4.2% (November 2021) is over twice the Government set target of 2%, however this is expected to be a temporary increase.

Borrowing

Treasury Management Strategy 2022-26

- 2.2 Borrowing is driven by the requirements of the approved capital investment budget. The forecast capital investment budget for 2022/23 indicates £51.3m of capital spend requiring financing from prudential borrowing. As long term borrowing rates are expected to be higher than investment rates, actual borrowings will be deferred by utilising cash balances and short term borrowing if required. Long term interest rate forecasts will be constantly monitored to ensure debt is secured at the best opportunity. If less capital spend is incurred than forecast then the need to borrow will be reduced.
- 2.3 PWLB is the usual route of obtaining loan finance for councils including Herefordshire Council. The forecast interest cost of new borrowing has been adjusted to reflect the new forecast interest rate cost on new borrowings required.
- 2.4 Using current forecasts during 2022/23 the councils underlying need to borrow is expected to increase by £16.6m, as shown in the table below.

| | £m excluding PFIs |
|---|----------------------------------|
| Estimated council borrowing as at 31st March 2022 | 122.6 |
| Capital spend financed by prudential borrowing | 51.3 |
| Net change in internal borrowing | (25.0) |
| Less minimum revenue provision | (9.7) |
| Estimated council borrowing as at 31st March 2023 | 139.2 |
| <i>Increase in estimated council borrowing</i> | 16.6 |

- 2.5 The borrowing budget for 2022/23 includes provision to pay short-term interest costs and the interest cost on existing fixed long term borrowing, a total budget of £5.2m.
- 2.6 The council's strategy is to cap the total short term loan stock holding at a threshold of a maximum of 50% of total loans. By restricting short term loans to a total of 50% of loans required the risk on interest rate exposure is minimised. Fixed rate loans can be secured quickly if this is decided the correct action to follow in consideration of all known factors at that time (including the councils cashflow and interest rate forecasts). Currently the council holds no short term loans, all loans are currently secured at a fixed interest rate and over a long term.
- 2.7 The council's exposure to variable rate debt has been discussed with the council's treasury adviser, Link Asset Services, who agree with the council's borrowing policy and the local consideration of interest rate forecasts.

Treasury Management Strategy 2022-26

Investments

2.8 When the council holds surplus funds (income received in advance of expenditure) the Code and Guidance requires councils to invest these funds prudently and to have regard to the security and liquidity of its investments before seeking the highest rate of return. The council tends to invest in banks, building societies, other local authorities and money market funds. The council continually assesses the various investment risks in conjunction with the support of its treasury advisors, Link Asset Services.

As a result of current banking regulations which, in the absence of government support, put the council's deposits at risk when banks get into difficulty, the council will:

- Maintain lower investment balances during the year;
- Keep low but liquid cash balances and invest these mainly in Money Market Funds (LVNAV (Low Volatility Net Asset Value));
- Maintain counterparty limits with the banks and building societies at prudent levels;
- Consider other creditworthy investments to increase diversification.

2.9 Where non treasury investments are considered, a separate report will be presented for approval with any changes that may be required to Prudential Indicators incorporated with an updated TMS if necessary.

2.10 There are a growing number of financial institutions promoting environmental, social and governance (ESG) issues. The council will take an active approach to target these entities, however these ESG issues must play a subordinate role to the priorities of security, liquidity and yield.

3. Economic Background and Interest Rate Forecast

Economic background

3.1 **UK** the Bank of England voted by a majority of 8-1 to increase Bank Rate by 0.15% to 0.25% during its December 2021 meeting, surprising markets who expected no changes due to the threat of the COVID-19 variant (Omicron).

3.2 The UK economy is continuing to recover from COVID-19 with a rise in spending by households and businesses and a reduction in unemployment. However the Omicron variant is starting to cause international concern due to it appearing more transmissible than the Delta version and having a higher reinfection rate than other variants.

3.3 Unlike 12 months ago, the possibility of negative interest rates are no longer a cause of concern and as inflation is expected to rise further to around 5% by spring next

Treasury Management Strategy 2022-26

year, modest interest rate increases will be required to bring inflation back to the 2% target.

- 3.4 The Office for Budget Responsibility's (the OBR) borrowing is £103.4bn less than on the same period last which reflects the economic recovery boosting receipts and the lower cost of pandemic-related support schemes.
- 3.5 **US** has recently announced decades' high inflation numbers where CPI has hit 6.2%. This was higher than forecast however the view is that this is transitory (albeit with a duration well into 2022). They have also seen a lasting reduction in the labour market participation, several million workers have retired or quit the labour market.
- 3.6 **EU** The slow roll out of vaccines initially delayed economic recovery in early 2021 but the vaccination rate then picked up sharply. After a contraction of -0.3% in Q1, Q2 came in with strong growth of 2%. With Q3 at 2.2%, the EU recovery is nearly complete although countries dependent on tourism are lagging. Recent sharp increases in gas and electricity prices have increased overall inflationary pressures but the European Central Bank is likely to see these as being only transitory after an initial burst through to around 4%, so is unlikely to be raising rates for a considerable time.

Interest rate forecast

- 3.7 Investment returns are likely to remain low for the foreseeable future; whilst there is some expectation that the bank rate may continue to increase, the uncertainty around the continuing effects of Covid remain.
- 3.8 There will remain a cost of carry to any new long-term borrowing that causes a temporary increase in cash balances as this position will incur a revenue cost of the difference between higher borrowing costs and lower investment returns. For example borrowing could be secured at a 1.5% interest cost and an investment could generate a 0.5% return, representing a cost of carry of 1.0%.
- 3.9 A more detailed interest rate forecast provided by the Link Asset Services is attached at Annex D.

4. Capital Financing Requirement

- 4.1 Capital expenditure can be financed in a number of ways including the application of usable capital receipts, a direct charge to revenue, capital grant or by securing an up-front contribution towards the cost of a project.
- 4.2 Capital expenditure not financed by one of the above methods will increase the capital financing requirement (CFR) of the council, representing the council's underlying borrowing requirement.

Treasury Management Strategy 2022-26

- 4.3 The CFR reflects the council's underlying need to finance capital expenditure by borrowing or by other long-term liability arrangements, for example public finance initiatives and finance leases.
- 4.4 The use of the term "borrowing" in this context does not necessarily imply external debt since, in accordance with best practice; the council has an integrated treasury management strategy. Borrowing is not associated with specific capital expenditure. The council, at any point in time, will have a number of cash flows both positive and negative and will be managing its position in terms of its borrowings and investments in accordance with its treasury management strategy.
- 4.5 The forecast movement in the CFR over future years is one of the Prudential Indicators which can be found in Annex C. The movement in actual external debt and usable reserve balances (which have a direct bearing on the requirement to borrow) combine to identify the council's borrowing requirement and potential investment strategy in the current and future years. The table below summarises the current forecast:-

| | 31.03.22 Estimate £000 | 31.03.23 Estimate £000 | 31.03.24 Estimate £000 | 31.03.25 Estimate £000 |
|---|---------------------------------------|---------------------------------------|---------------------------------------|---------------------------------------|
| Forecast Capital Finance Requirement (CFR) | 325,810 | 357,574 | 378,990 | 371,752 |
| Less: PFI and other long term commitments | (46,804) | (45,232) | (43,723) | (41,913) |
| CFR excluding other long-term liabilities (PFIs) | 279,006 | 312,342 | 335,267 | 329,839 |
| Less: Existing fixed long term borrowing (a) | (129,427) | (122,567) | (119,439) | (112,501) |
| Maximum new borrowing requirement | 149,579 | 189,775 | 215,828 | 217,338 |
| Less: Internal borrowing from reserves | (139,579) | (173,175) | (163,897) | (151,693) |
| Net new borrowing requirement (b) | 10,000 | 16,600 | 51,931 | 65,645 |
| Total Council Borrowing (a plus b) | 139,427 | 139,167 | 171,370 | 178,146 |

Treasury Management Strategy 2022-26

- 4.6 The above table shows the council's borrowing requirement due to capital expenditure and the refinancing of principal repaid on existing long-term debt. CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the council's total debt should be lower than its highest forecast CFR over the next three years. The council expects to comply with this recommendation.
- 4.7 From 1 April 2022 councils will be required to comply with IFRS16 that requires lease arrangements to be disclosed as finance leases, this will have the effect of increasing the capital financing requirement. The table above excludes this impact as work continues on establishing the effect of this accounting change. Indications are that the impact will be immaterial.

5. Borrowing Strategy

- 5.1 At 31 October 2021 the council held £125.7m of long-term fixed rate loans as shown in Annex A. A new £5m 15-year EIP loan was secured on 5/11/21 at an interest rate of 1.72% Current capital expenditure forecasts suggest that there will be further capital spend financed by borrowing before the end of the financial year, if spend slips and / or cash balances remain high then the need to borrow will be deferred.

Objective

- 5.2 The council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the council's long-term plans change is a secondary objective.

Strategy

- 5.3 Given the significant cuts to public expenditure and in particular to local government funding, the council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is more cost effective in the short-term to use internal resources and borrow using short-term loans.
- 5.4 This enables the council to reduce net borrowing costs and reduce its overall credit risk by tailoring the timing of borrowing to minimise cash balances held. The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecasted to rise. The council's treasury advisors will assist the council with 'cost of carry' and breakeven analysis. Its output will determine whether the council borrows additional sums at long-term fixed rates in 2022/23 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.
- 5.5 Short-term loans leave the council exposed to the risk of short-term interest rate rises; therefore the risk is mitigated by restricting the exposure to this risk at 50% of the debt total.

Treasury Management Strategy 2022-26

Sources

5.6 The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB)
- UK local authorities
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds
- capital market bond investors
- Local Capital Finance Company and other special purpose companies created to enable local authority bond issues.

5.7 In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- operating and finance leases
- hire purchase
- Private Finance Initiative
- sale and leaseback arrangements

LOBO loans

5.8 The council has two historic LOBO loans (Lender's Option, Borrower's Option) of £6m each on which the council pays interest at 4.5%. Every six months, when the interest charges become due, the lenders have the option to increase the interest rate being charged at which point the council can accept the revised terms or reject them and repay the loan. LOBO loans present a potential refinancing risk to the council since the decision to amend the terms is entirely at the lender's discretion.

Debt rescheduling

5.9 The PWLB allows the repayment of loans before maturity by either paying a premium or receiving a discount according to a set formula based on current interest rates. Due to the prevailing low interest rate regime, opportunities for debt rescheduling are likely to be very limited. However, this option will be kept under review and will be considered where this is expected to lead to an overall saving or reduction in risk.

6. Annual Investment Strategy

6.1 The council needs to hold adequate funds to meet day-to-day liquidity needs, for example salary and creditor payments. The council maintains a minimum cash flow balance of around £20m to cover all contingencies. A cash flow forecast is maintained that includes all known receipts and payments so that the council can take action to ensure that it can meet all its liabilities when they fall due.

Objective

Treasury Management Strategy 2022-26

- 6.2 Both the CIPFA Code and the MHCLG Guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and receiving unsuitably low investment income.

Strategy

- 6.3 Given the increasing risk and continued low returns from short-term unsecured bank deposits, the council will aim to keep its invested funds as low as possible and limit the amounts invested with banks and building societies. For 2022/23 the council will continue to rely on Money Market Funds which are highly diversified and carry reduced credit risk.

Risk Assessment and Credit Ratings

- 6.4 The council applies the credit worthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from three main credit rating agencies (Fitch, Moody's and Standard and Poor's). This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system to which Link Asset Services allocate a series of colour coded bands with suggested maximum durations for investments (as shown in table 2 below).
- 6.5 Typically the minimum credit ratings criteria the council use will be short-term rating (Fitch or equivalents) of F1 and a long term rating of A-. There may be occasions when the counterparty ratings from one agency are marginally lower than these ratings but still may 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.
- 6.6 The council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- (Fitch or equivalents). If investments are to be made overseas then approval ahead of the investment being made is required from the Chief Finance Officer. Santander UK plc (a subsidiary of Spain's Banco Santander) and Clydesdale Bank plc (a subsidiary of National Australia Bank) will be classed as UK banks due to their substantial franchises and the arms-length nature of the parent-subsidary relationship.

Approved Counterparties

- 6.7 The council will invest its surplus funds with any of the counterparty types in table 2 below, subject to the cash limits (per counterparty) and the time limits shown. A group of banks under the same ownership will be treated as a single organisation for investment limit purposes.

| |
|---|
| Table 2: Approved Investment Counterparties and Limits |
|---|

Treasury Management Strategy 2022-26

| | | Colour coding or long term rating | £ limit | Time limit |
|---|---------------------------------------|-----------------------------------|---|----------------|
| Banks and Building Societies | Term deposits, CDs or corporate bonds | Yellow | 5m | 5 years |
| | | Purple | 5m | 2 years |
| | | Orange | 5m | 1 year |
| | | Blue | 5m | 1 year |
| | | Red | 5m | 6 months |
| | | Green | 5m | 100 days |
| | | No colour | nil | Not to be used |
| Council's Banker (NatWest) | | | 5m | Liquid |
| DMADF | DMADF account | AAA | Unlimited | 6 months |
| UK Government | UK Gilts | UK sovereign rating | Unlimited | 1 year |
| UK Government | Treasury Bills | UK sovereign rating | Unlimited | 1 year |
| Multilateral development banks | Bonds | AAA | 5m | 6 months |
| Local Authorities | Term deposits | | 10m | 1 year |
| Money Market Funds | MMFs | AAA | 10m | Liquid |
| Other investments: | | | | |
| Top five UK Building Society | | | £5m per fund (up to six months' duration) | |
| Pooled funds | | | £5m per fund | |
| Mercia Waste Management (providing finance for Energy from Waste Plant) | | | £40m over the course of the contract | |

Specified Investments

6.8 The MHCLG Guidance defines specified investments as those:

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement,
- not defined as capital expenditure by legislation, and
- invested with one of:
 - the UK Government,
 - a UK local authority, parish council or community council, or
 - a body or investment scheme of "high credit quality".

6.9 The Authority defines "high credit quality" organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA- or higher.

Non-specified Investments

Treasury Management Strategy 2022-26

- 6.10 Any investment not meeting the definition of a specified investment is classed as non-specified. The Authority does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in table 3 below.

| Table 3: Non-Specified Investment Limits | Cash limit |
|--|-------------------|
| Total long-term investments | £5.0m |
| Total investments with unrecognised credit ratings | £5.0m |
| Total non-specified investments | £10.0m |

7. Annual Minimum Revenue Provision Statement 2022/23

- 7.1 Where the council finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the notional repayment of debt is known as Minimum Revenue Provision (MRP). The Local Government Act 2003 requires the council to have regard to the Ministry of Housing, Communities and Local Government's Guidance on Minimum Revenue Provision (the MHCLG Guidance) most recently issued in 2018. The broad aim of the Guidance is to ensure that debt is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits. In line with the Guidance, the policy for the 2022/23 calculation of MRP is as follows:

| | Indicative 2022/23 MRP charge £000 |
|--|---|
| Supported borrowing | 1,397 |
| Prudential borrowing | 8,275 |
| Sub Total | 9,672 |
| Finance leases and private finance initiatives | 2,058 |
| TOTAL | 11,730 |

MRP on supported borrowing is written down on an annuity basis with an annuity rate of 2%.

MRP on unsupported borrowing incurred before 1 April 2008 will be written down on a straight line basis over the asset life.

Treasury Management Strategy 2022-26

MRP on unsupported borrowing from 1 April 2008 onwards is written down on an annuity basis with an annuity rate of 3%.

MRP on assets acquired through finance leases and Private Finance Initiative (PFI) will be equal to the cash payments that reduce the outstanding liability each year.

Treasury Management Strategy 2022-26

Annex A

EXISTING BORROWING AND INVESTMENTS

The overall treasury management portfolio as at 31 March 2021 and for the position as at 31 October 2021 are shown below for both borrowing and investments.

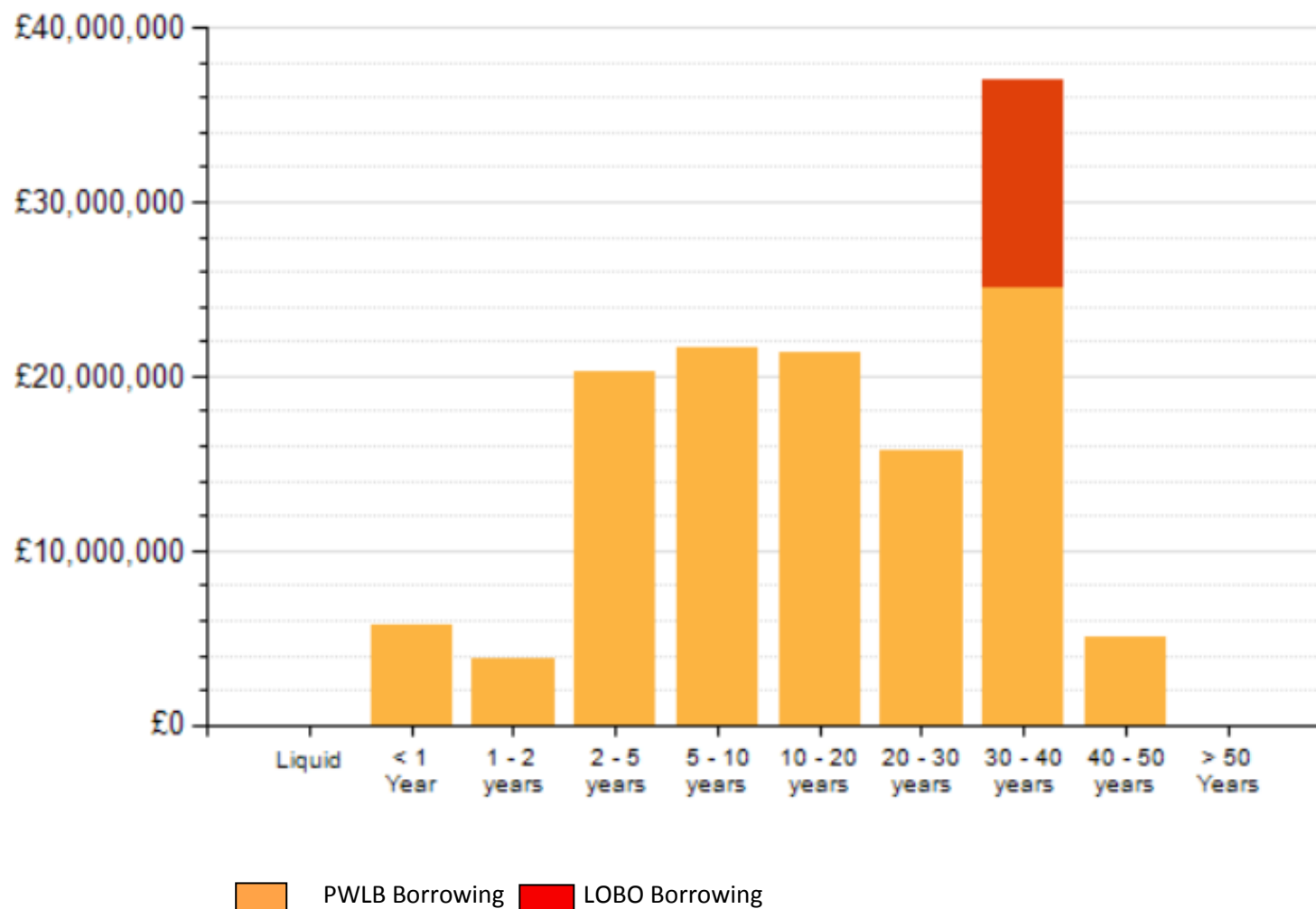
TREASURY PORTFOLIO

| | actual | actual | current | current |
|---|-----------------|-------------|-----------------|-------------|
| Treasury Investments | 31.03.21 | 31.03.21 | 31.10.21 | 31.10.21 |
| | £000 | % | £000 | % |
| banks | 19,030 | 31% | 19,200 | 21% |
| banks – ESG ‘green’ deposits | 0 | 0% | 10,000 | 11% |
| building societies - unrated | | 0% | 0 | 0% |
| building societies - rated | | 0% | 5,000 | 5% |
| local authorities | 25,000 | 41% | 10,000 | 11% |
| DMADF (H.M. Treasury) | | 0% | 0 | 0% |
| money market funds | 17,400 | 28% | 48,970 | 52% |
| certificates of deposit | 0 | 0% | 0 | 0% |
| Total managed in house | 61,430 | 100% | 93,170 | 100% |
| bond funds | 0 | 0% | 0 | 0% |
| property funds | 0 | 0% | 0 | 0% |
| Total managed externally | 0 | 0% | 0 | 0% |
| Total treasury investments | 61,430 | 100% | 93,170 | 100% |
| Treasury external borrowing | | | | |
| local authorities | 0 | 0% | 0 | 0% |
| PWLB | 114,798 | 91% | 113,658 | 90% |
| LOBOs | 12,000 | 9% | 12,000 | 10% |
| Total external borrowing | 126,798 | 100% | 125,658 | 100% |
| Net treasury investments / (borrowing) | (65,368) | 0 | (32,488) | 0 |

Treasury Management Strategy 2022-26

BORROWING MATURITY PROFILE AS AT 30.11.21

Loans Maturities by Type



Treasury Management Strategy 2022-26

Annex C

PRUDENTIAL AND TREASURY INDICATORS FOR THE NEXT FOUR YEARS

1. Background

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the council has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored.

2. Estimates of Capital Expenditure

- 2.1 This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax levels.

| Capital Programme | 2022/23 Forecast £000 | 2023/24 Estimate £000 | 2024/25 Estimate £000 | Total £000 |
|--|-----------------------------|-----------------------------|-----------------------------|----------------|
| Total expenditure | 99,094 | 90,546 | 44,901 | 234,541 |
| Funding | | | | |
| Grants, contributions and capital receipts | 47,745 | 52,504 | 35,933 | 136,182 |
| Prudential borrowing | 51,349 | 38,042 | 8,968 | 98,359 |
| Total | 99,094 | 90,546 | 44,901 | 234,541 |

The table above reflects both the approved and proposed capital investment budget. Should any further borrowing be required then Council approval will be required and additional revenue resources will need to be identified to fund the additional debt repayment costs. In addition the prudential indicators would need to be revisited in accordance with the requirements of the Prudential Code to provide the assurances of affordability of the additional debt.

Treasury Management Strategy 2022-26

3. Capital Financing Requirement

- 3.1 The Capital Financing Requirement (CFR) measures the council's underlying need to borrow for a capital purpose. The calculation of the CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and financing.

| Capital Financing Requirement (CFR) | 2021/22 Estimate £000 | 2022/23 Estimate £000 | 2023/24 Estimate £000 | 2024/25 Estimate £000 |
|-------------------------------------|--------------------------|--------------------------|--------------------------|--------------------------|
| CFR excluding PFI | 279,006 | 312,342 | 335,267 | 329,839 |
| PFI and finance leases* | 46,804 | 45,232 | 43,723 | 41,913 |
| Total forecast CFR | 325,810 | 357,574 | 378,990 | 371,752 |

* this value is expected to increase following the adoption of IFRS16 from 1 April 2022 when existing lease arrangements are expected to be required to be included as finance leases in the value above

4. Gross Debt and the Capital Financing Requirement

- 4.1 In order to ensure that over the medium term debt will only be for a capital purpose, the local authority should ensure that debt does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.
- 4.2 The Section 151 Officer reports that the council currently has no difficulty meeting this requirement nor are there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

5. Operational Boundary for External Debt

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

| Operational Boundary | 2021/22 Estimate £000 | 2022/23 Estimate £000 | 2023/24 Estimate £000 | 2024/25 Estimate £000 |
|--------------------------------------|--------------------------|--------------------------|--------------------------|--------------------------|
| Operational Boundary for Borrowing | 340,000 | 340,000 | 340,000 | 340,000 |
| Operational Boundary for other Long- | 60,000 | 60,000 | 60,000 | 60,000 |

Treasury Management Strategy 2022-26

| | | | | |
|---|----------------|----------------|----------------|----------------|
| Term Liabilities | | | | |
| Operational Boundary for External Debt | 400,000 | 400,000 | 400,000 | 400,000 |

6. Authorised Limit for External Debt

- 6.1 The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Authority can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

| Authorised Limit | 2021/22 Estimate £000 | 2022/23 Estimate £000 | 2023/24 Estimate £000 | 2024/25 Estimate £000 |
|--|--------------------------------------|--------------------------------------|--------------------------------------|--------------------------------------|
| Authorised Limit for Borrowing | 350,000 | 350,000 | 350,000 | 350,000 |
| Authorised Limit for other Long-Term Liabilities | 70,000 | 70,000 | 70,000 | 70,000 |
| Authorised Limit for External Debt | 420,000 | 420,000 | 420,000 | 420,000 |

7. Ratio of Financing Costs to Net Revenue Stream

- 7.1 This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs. The definition of financing costs is set out in the Prudential Code and includes both interest payable and provision for repayment of loan principal.
- 7.2 The ratio is based on costs net of investment income.

| Ratio of Financing Costs to Net Revenue Stream | 2022/23 Estimate £'000 | 2023/24 Estimate £'000 | 2024/25 Estimate £'000 |
|---|---------------------------------------|---------------------------------------|---------------------------------------|
| Net Revenue Stream | 175,112 | 177,745 | 181,715 |
| Financing Costs (excluding PFI) | 14,868 | 16,118 | 17,753 |
| Percentage | 8.5% | 9.1% | 9.8% |

- 7.3 The above table shows budgeted financing costs within the council's medium term financial strategy.

Treasury Management Strategy 2022-26

8 Maturity Structure of Borrowing (fixed and variable)

- 8.1 The council will also limit and monitor large concentrations of fixed rate debt needing to be replaced. Limits in the following table are intended to control excessive exposures to volatility in interest rates when refinancing maturing debt.
- 8.2 The maturity of borrowing (as shown in Annex B) is determined by reference to the date on which the loans could be repaid. The council's two LOBO loans could become repayable within 12 months although, if the lenders do not increase the interest rates being charged, which is the current assumption, then the loans could remain outstanding until 2054.

| Maturity structure of fixed rate borrowing | Estimated level at 31/03/22 | Lower Limit for 2022/23 | Upper Limit for 2022/23 |
|--|-----------------------------|-------------------------|-------------------------|
| Under 12 months | 6% | 0% | 10% |
| 12 months and within 24 months | 3% | 0% | 10% |
| 24 months and within 5 years | 16% | 0% | 25% |
| 5 years and within 10 years | 18% | 0% | 35% |
| 10 years and above | 57% | 0% | 80% |
| Total | 100% | | |

9. Upper Limit for total principal sums invested over 364 days:

- 9.1 The purpose of this limit is to contain exposure to the possibility of loss that may arise as a result of the council having to seek early repayment of the sums invested.

| Upper Limit for total principal sums invested over 364 days | 2022/23 Estimate £m | 2023/24 Estimate £m | 2024/25 Estimate £m | 2025/26 Estimate £m |
|---|------------------------|------------------------|------------------------|------------------------|
| Authorised counterparties | 5 | 5 | 5 | 5 |

Treasury Management Strategy 2022-26

Annex D

**OUTLOOK FOR INTEREST RATES
(FORECAST & ECONOMIC COMMENT PROVIDED BY TREASURY ADVISORS)**

| | Dec-21 | Mar-22 | Jun-22 | Sep-22 | Dec-22 | Mar-23 | Jun-23 | Sep-23 | Dec-23 | Mar-24 | Jun-24 | Sep-24 | Dec-24 |
|---|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Bank Base Rate (%) | 0.25 | 0.25 | 0.50 | 0.50 | 0.50 | 0.75 | 0.75 | 0.75 | 0.75 | 1.00 | 1.00 | 1.00 | 1.00 |
| PWLB Rates (%): | | | | | | | | | | | | | |
| 5 years | 1.40 | 1.50 | 1.50 | 1.60 | 1.60 | 1.70 | 1.80 | 1.80 | 1.80 | 1.90 | 1.90 | 1.90 | 2.00 |
| 10 years | 1.60 | 1.70 | 1.80 | 1.80 | 1.90 | 1.90 | 2.00 | 2.00 | 2.00 | 2.10 | 2.10 | 2.10 | 2.20 |
| 25 years | 1.80 | 1.90 | 2.00 | 2.10 | 2.10 | 2.20 | 2.20 | 2.20 | 2.30 | 2.30 | 2.40 | 2.40 | 2.50 |
| 50 years | 1.50 | 1.70 | 1.80 | 1.90 | 1.90 | 2.00 | 2.00 | 2.00 | 2.10 | 2.10 | 2.20 | 2.20 | 2.30 |
| The above PWLB rates are noted by Link Asset Services as being their “central” or most likely forecast, however, they also note that there are upside and downside risks to their forecast. | | | | | | | | | | | | | |

Forecast:

- The council’s treasury advisors forecast the bank base rate to increase to 1.00% by March 2024.

Council budget:

- The proposed treasury management budget is as follows:-

| | 2022/23 | 2023/24 | 2024/25 | 2025/26 |
|--|---------------|---------------|---------------|---------------|
| | £000 | £000 | £000 | £000 |
| Minimum revenue provision (excludes PFI) | 9,672 | 10,009 | 11,250 | 12,362 |
| Interest payable | 5,196 | 6,109 | 6,503 | 5,988 |
| Totals | 14,868 | 16,118 | 17,753 | 18,350 |

Treasury Management Strategy 2022-26

- As can be seen from the table above, the council's treasury advisors central forecast is for the Bank Base Rate to increase to 0.50% during 2022, with further increases expected in the following two years. The council's borrowing budget has been based on a rate of up to 2.5% which should incorporate sufficient headroom to accommodate any unexpected changes in the Base Rate.
- Should the Bank Base Rate increase sooner or more rapidly than forecast the increased yield on investments will partly offset any increase in short-term variable borrowing rates.
- Performance against budget will be reported to Cabinet in the financial performance reports.

Treasury Management Strategy 2022-26

Annex E

TREASURY MANAGEMENT POLICY STATEMENT

1. Statement of Purpose

- 1.1 Herefordshire Council adopts the recommendations made in CIPFA's *Treasury Management in the Public Services: Code of Practice*, which was revised in 2017. In particular, the council adopts the following key principles and clauses.

2. Key Principles

- 2.1 Herefordshire Council adopts the following three key principles (identified in Section 4 of the Code):
- The council will put in place formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of its treasury management activities.
 - The council will ensure that its policies and practices make clear that the effective management and control of risk are prime objectives of its treasury management activities and that responsibility for these lies clearly with the council. In addition, the council's appetite for risk will form part of its annual strategy and will ensure that priority is given to security and liquidity when investing funds.
 - The council acknowledges that the pursuit of best value in treasury management, and the use of suitable performance measures, are valid and important tools to employ in support of business and service objectives, whilst recognising that in balancing risk against return, the council is more concerned to avoid risks than to maximise returns.

3. Adopted Clauses

- 3.1 Herefordshire Council formally adopts the following clauses (identified in Section 5 of the code):
- The council will create and maintain, as the cornerstones for effective treasury management:
 - A treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities;
 - Suitable treasury management practices (TMPs), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

The content of the policy statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of the council. Such amendments will not result in the organisation materially deviating from the Code's key principles.

- Full council will receive reports on treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the

Treasury Management Strategy 2022-26

year, a mid-year review and an annual report after its close.

- The responsibility for the implementation and regular monitoring of treasury management policies and practices is delegated to Cabinet and for the execution and administration of treasury management decisions to the Chief Officer-Finance and Commercial, who will act in accordance with the organisation's policy statement and TMPs and, if he or she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.
- Overview and Scrutiny Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

4. Definition of Treasury Management

4.1 Herefordshire Council defines its treasury management activities 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.'

5. Policy Objectives

- 5.1 Herefordshire Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the council, and any financial instruments entered into to manage these risks.
- 5.2 Herefordshire Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

6. Non-treasury investments

- 6.1 Herefordshire Council recognises that investment in other financial assets and property primarily for financial return, taken for non-treasury management purposes, requires careful investment management. Such activity includes loans supporting service outcomes, investments in subsidiaries and investment property portfolios.
- 6.2 Herefordshire Council will ensure that all investments in the capital programme will set out, where relevant, the risk appetite and policy and arrangement for non-treasury investments. The risk appetite for these activities may differ from that of treasury management.
- 6.3 Herefordshire Council will maintain a schedule setting out a summary of existing material investments, subsidiaries, joint ventures and liabilities including financial guarantees and the organisations risk exposure within its annual statement of accounts.