

Open	Would any decisions proposed :			
Any especially affected Wards	(a) Be entirely within Audit Committee's powers to decide NO			
None	(b) Need to be recommendations to Council/Cabinet			Yes
	(c) Be partly for recommendations to Council and partly within Cabinets powers –			NO
Lead Member: Brian Long E-mail:		Other Cabinet Members consulted:		None
		Other Members consulted:		None
Lead Officer: Ruth Wilson E-mail: ruth.wilson@west-norfolk.gov.uk Direct Dial: 01553 616450		Other Officers consulted:		None
Financial Implications Yes	Policy/Personnel Implications NO	Statutory Implications (incl S.17) YES	Equal Opportunities Implications NO	Risk Management Implications NO

Date of meeting: 2 February 2021

TREASURY MANAGEMENT STRATEGY STATEMENT, MINIMUM REVENUE PROVISION POLICY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2021/2022

Summary

The Council is required to receive and approve a Treasury Management Strategy Statement; Annual Investment Strategy; and Minimum Revenue Provision Policy Statement which covers:

- The Treasury Management Strategy
- Capital plans, including prudential indicators
- A Minimum Revenue Provision (MRP) Policy
- An Investment Strategy

This report covers the requirements of the Local Government Act 2003, the Chartered Institute of Public Finance Accountants (CIPFA) Prudential Code, the Ministry of Housing, Communities and Local Government (MHCLG) MRP Guidance, the CIPFA Treasury Management Code and the MHCLG Investment Guidance.

The Council's Treasury Advisor, Link Asset Services, provide a template document for the Treasury Management Strategy Statement, which is fully compliant with CIPFA's code and MHCLG's guidance. The Council has used this template in preparing this report.

This report looks at the period 2020-2025, which fits with the Council's Financial Plan and Capital Programme. Officers of the council have prepared the report based on their views of forecasts for interest rates, and have used information provided by the council's Treasury Management Advisor, Link Asset Services.

Recommendations

Cabinet is asked to recommend that Council approve:

- 1. The Treasury Management Strategy Statement 2021/2022, including treasury indicators for 2021-2025.**
- 2. The Minimum Revenue Provision Policy 2021/2022**
- 3. The Investment Strategy 2021/2022**

Reason for the Decision

The Council must have approved a Treasury Management Strategy Statement, Minimum Revenue Provision Policy Statement and Annual Investment Strategy 2021/2022 by 31 March 2021.

Treasury Management Strategy Statement

Minimum Revenue Provision Policy Statement
and Annual Investment Strategy

2021/2022

Including commercial activities / non treasury investments

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1 INTRODUCTION

1.1 Background

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

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

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

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

CIPFA defines treasury management as:

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

1.2 Reporting requirements

1.2.1 Capital Strategy

The CIPFA revised 2017 Prudential and Treasury Management Codes require all local authorities to prepare an additional report, a capital strategy report, which will provide the following:

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

The aim of the capital strategy is to ensure that all elected members on the full council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

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

- The corporate governance arrangements for these types of activities;
- Any service objectives relating to the investments;
- The expected income, costs and resulting contribution;
- The debt related to the activity and the associated interest costs;
- The payback period (MRP policy);
- For non-loan type investments, the cost against the current market value;
- The risks associated with each activity.

Where a physical asset is being bought, details of market research, advisers used, (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

If any non-treasury investment sustains a loss during the final accounts and audit process, the strategy and revenue implications will be reported through the same procedure as the capital strategy.

To demonstrate the proportionality between the treasury operations and the non-treasury operations, high-level comparators are shown throughout this report.

1.2.2 Treasury Management reporting

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

- a. Treasury Management Strategy and Prudential Indicators** (this report) - The first, and most important report is forward looking and covers:
 - the capital plans, (including prudential indicators);
 - a minimum revenue provision (MRP) policy, (how residual capital expenditure is charged to revenue over time);
 - the treasury management strategy, (how the investments and borrowings are to be organised), including treasury indicators; and
 - an investment strategy, (the parameters on how investments are to be managed).
- b. Mid-Year Treasury Management Report** – To update members on the capital position, amending prudential indicators as necessary, and revising policies if necessary.
- c. Annual Treasury Report** – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

1.3 TREASURY MANAGEMENT STRATEGY 2021/22

The strategy for 2021/22 covers two main areas:

Capital

- the capital expenditure plans and the associated prudential indicators;
- the minimum revenue provision (MRP) policy.

Treasury management

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

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

1.4 Training

The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. Treasury Awareness training was provided for members by Link Asset Services on the 9 January 2020.

The training needs of the Council's treasury management officers are periodically reviewed and with full support being given for officers to attend workshops, courses and conferences that will keep their knowledge up to date.

1.5 Treasury management consultants

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

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and ensures that undue reliance is not placed upon the services of our external Treasury Management Advisors. All decisions are undertaken with regard to all available information, including, but not solely, our treasury advisors.

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.

2 THE CAPITAL PRUDENTIAL INDICATORS 2021/22 – 2024/25

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

2.1 Capital expenditure

This prudential indicator is a summary of the Council's capital expenditure plans. (Capital Programme 2020-2025 to be agreed by Council 25 February 2021, which is the same meeting that this report will be approved at.)

	2020/2021	2021/2022	2022/2023	2023/2024	2024/2025
	£	£	£	£	£
Major Projects	11,590,610	29,711,470	44,307,400	26,289,520	18,045,180
Operational:					
Community and Partnerships	2,343,120	2,316,850	2,260,000	2,260,000	2,260,000
Resources	465,680	150,000	150,000	150,000	150,000
Regeneration	21,350	-	-	-	-
Property and Projects	42,000	28,000	-	-	-
Operational and Commercial Services	987,990	2,204,150	170,500	507,770	100,000
Alive West Norfolk	68,860	1,261,490	25,000	-	-
Total	15,519,610	35,671,960	46,912,900	29,207,290	20,555,180
Exempt Schemes (Major Projects)	5,122,840	19,230,000	18,848,270	3,461,660	-
Total Capital Programme	20,642,450	54,901,960	65,761,170	32,668,950	20,555,180

The table below summarises how the capital expenditure in the table above is being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Financing Capital Expenditure					
	£'000	£'000	£'000	£'000	£'000
Capital Receipts	(19,234)	(1,709)	(42,361)	(51,915)	(35,990)
Capital Grants	(1,775)	(1,775)	(1,775)	(1,775)	(1,775)
Capital Reserves	(889)	(2,187)	(1,591)	(20)	0
Revenue	(5,757)	(2,803)	(654)	(993)	(608)
Total	(27,655)	(8,474)	(46,380)	(54,703)	(38,373)
CFR Reduced / (Increased) By	7,013	(46,428)	(19,381)	22,034	17,818
Net financing need for the year	0	(46,428)	(19,381)	-	-

The net financing need for commercial activities included in the above table against expenditure is shown below:

Commercial activities	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
Net financing need for the year for Exempt Schemes - Commercial	-	4,788	4,538	1,942	-
Percentage of total net financing need (Closing CFR Requirement for the year as detailed in 2.2)	-	6%	5%	3%	-

2.2 The Council's borrowing need (the Capital Financing Requirement)

The second prudential indicator is the Council'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 Council's indebtedness and so it's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

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

The Council is asked to approve the CFR projections below:

Capital Financing Requirement (CFR)	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
Opening CFR	38,885	31,338	77,218	95,868	73,121
CFR – Services	(7,013)	41,640	14,843	(23,976)	(17,818)
CFR – Commercial Activities	0	4,788	4,538	1,942	0
Net Financing Need Total	31,872	77,766	96,599	73,834	55,303
Less MRP and other financing movements*	(522)	(580)	(650)	(577)	(575)
Closing CFR	31,350	77,198	95,929	73,318	54,926

Movement in CFR	(7,535)	45,848	18,730	(22,611)	(18,392)
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*Includes finance lease annual principal payments and the repayment of borrowing.

A key aspect of the regulatory and professional guidance is that elected members are aware of the size and scope of any commercial activity in relation to the authority's overall financial position. The capital expenditure figures shown in 2.1 and the details above demonstrate the scope of this activity and, by approving these figures, consider the scale proportionate to the Authority's remaining activity.

2.3 Core funds and expected investment balances

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 ongoing impact on investments unless resources are supplemented each

year from new sources (asset sales etc.). Detailed below are estimates of the year-end balances for each resource and anticipated day-to-day cash flow balances.

Year End Resources	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
General fund balances / ear marked reserves	(35,421)	(33,165)	(35,572)	(38,984)	(39,085)
Capital receipts	(5,264)	(3,992)	(5,641)	(8,231)	(10,431)
Provisions (Collection Fund)	(3,000)	(3,000)	(3,000)	(3,000)	(3,000)
Other	(1,000)	(1,000)	(1,000)	(1,000)	(1,000)
Total core funds	(44,685)	(41,158)	(45,213)	(51,215)	(53,516)
Working capital	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)
Internal Borrowing*	21,568	26,204	26,882	24,555	22,602
Expected investments	(28,117)	(19,954)	(23,331)	(31,660)	(35,914)

*Use of internal and/or temporary borrowing will reflect actual capital expenditure during the year.

2.4 MINIMUM REVENUE PROVISION (MRP) POLICY STATEMENT

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

MHCLG regulations have been issued which require the full Council to approve **an MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement:

- **Asset life method** – MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) which provides for a reduction in the borrowing need over approximately the asset's life.

MRP Overpayments - A change introduced by the revised MHCLG MRP Guidance was the allowance that any charges made over the statutory minimum revenue provision (MRP), voluntary revenue provision or overpayments, can, if needed, be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year.

3 BORROWING

The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's capital strategy. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

The Council's forward projections for borrowing are summarised below. The table shows the actual external debt, against the underlying capital borrowing need, (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

Year End Resources	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
External Debt					
Debt at 1 April	10,000	9,783	50,994	69,047	48,763
Expected change in Debt	0	41,411	18,234	(20,120)	(16,294)
Other long-term liabilities	(236)	(217)	(199)	(181)	(163)
Expected change in Other long-term liabilities	18	18	18	18	18
Actual gross debt at 31 March	9,783	50,994	69,047	48,763	32,324
The Capital Financing Requirement	31,350	77,198	95,929	73,318	54,926
BORROWING	21,568	26,204	26,882	24,555	22,602

Within the above figures the level of debt relating to commercial activities is:

External Debt for commercial activities	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
Actual debt at 31 March £m	-	4,788	4,538	1,942	-
Percentage of total external debt %	0%	9%	7%	4%	0%

External borrowing requirements will be reviewed at the time that the funding is required.

Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2021/22 and the following two financial years. This allows some flexibility for limited early borrowing for future years but ensures that borrowing is not undertaken for revenue or speculative purposes.

The S151 Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this report.

3.1 Treasury Indicators: limits to borrowing activity

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

Operational boundary	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
Debt	31,000	77,000	96,000	73,000	55,000
Other long term liabilities	1,000	1,000	1,000	1,000	1,000
Commercial activities	10,000	10,000	10,000	10,000	10,000
Total	42,000	88,000	107,000	84,000	66,000

The authorised limit for external debt. This is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

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

Authorised Limit	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
Debt	36,000	82,000	101,000	78,000	60,000
Other long term liabilities	1,000	1,000	1,000	1,000	1,000
Commercial activities	10,000	10,000	10,000	10,000	10,000
Total	47,000	93,000	112,000	89,000	71,000

3.2 Prospects for interest rates

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Link provided the following forecasts on 11.8.20. However, following the conclusion of the review of PWLB margins over gilt yields on 25.11.20, all forecasts below have been reduced by 1%. These are forecasts for certainty rates, gilt yields plus 80bps:

Link Group Interest Rate View		9.11.20											
These Link forecasts have been amended for the reduction in PWLB margins by 1.0% from 26.11.20													
	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
5 yr PWLB	0.80	0.80	0.80	0.80	0.90	0.90	0.90	0.90	0.90	1.00	1.00	1.00	1.00
10 yr PWLB	1.10	1.10	1.10	1.10	1.20	1.20	1.20	1.20	1.20	1.30	1.30	1.30	1.30
25 yr PWLB	1.50	1.60	1.60	1.60	1.60	1.70	1.70	1.70	1.70	1.80	1.80	1.80	1.80
50 yr PWLB	1.30	1.40	1.40	1.40	1.40	1.50	1.50	1.50	1.50	1.60	1.60	1.60	1.60

The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its subsequent meetings to 16th December, although some forecasters had suggested that a cut into negative territory could happen. However, the Governor of the Bank of England has made it clear that he currently thinks that such a move would do more damage than good and that more quantitative easing is the favoured tool if further action becomes necessary. As shown in the forecast table above, no increase in Bank Rate is expected in the near-term as economic recovery is expected to be only gradual and, therefore, prolonged. These forecasts were based on an assumption that a Brexit trade deal would be agreed by 31.12.20: as this has now occurred, these forecasts do not need to be revised.

As the interest forecast table for PWLB certainty rates above shows, there is expected to be little upward movement in PWLB rates over the next two years as it will take economies, including the UK, a prolonged period to recover all the momentum they have lost in the sharp recession caused during the coronavirus shut down period. From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and sharp changes in investor sentiment, (as shown on 9th November when the first results of a successful COVID-19 vaccine trial were announced). Such volatility could occur at any time during the forecast period.

Investment and borrowing rates

- **Investment returns** are likely to remain exceptionally low during 2021/22 with little increase in the following two years.
- **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: indeed, gilt yields up to 6 years were negative during most of the first half of 20/21. The policy of avoiding new borrowing by running down spare cash balances has served local authorities well over the last few years. The unexpected increase of 100 bps in PWLB rates on top of the then current margin over gilt yields of 80 bps in October 2019, required an initial major rethink of local authority treasury management strategy and risk management. However, in March 2020, the Government started a consultation process for reviewing the margins over gilt rates for PWLB borrowing for different types of local authority capital expenditure. *(Please note that Link has concerns over this approach, as the fundamental principle of local authority borrowing is that borrowing is a treasury management activity and individual sums that are borrowed are not linked to specific capital projects.)* It also introduced the following rates for borrowing for different types of capital expenditure: -
 - **PWLB Standard Rate** is gilt plus 200 basis points (G+200bps)
 - **PWLB Certainty Rate** is gilt plus 180 basis points (G+180bps)

- **PWLB HRA Standard Rate** is gilt plus 100 basis points (G+100bps)
 - **PWLB HRA Certainty Rate** is gilt plus 80bps (G+80bps)
 - **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)
- As a consequence of these increases in margins, many local authorities decided to refrain from PWLB borrowing unless it was for HRA or local infrastructure financing, until such time as the review of margins was concluded.
 - On 25.11.20, the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates; the standard and certainty margins were reduced by 1% but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three year capital programme. The new margins over gilt yields are as follows: -
 - **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)
 - **PWLB Certainty Rate** is gilt plus 80 basis points (G+80bps)
 - **PWLB HRA Standard Rate** is gilt plus 100 basis points (G+100bps)
 - **PWLB HRA Certainty Rate** is gilt plus 80bps (G+80bps)
 - **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)
 - **Borrowing for capital expenditure.** As Link's long-term forecast for Bank Rate is 2.00%, and all PWLB rates are under 2.00%, there is now value in borrowing from the PWLB for all types of capital expenditure for all maturity periods, especially as current rates are at historic lows. However, greater value can be obtained in borrowing for shorter maturity periods so the Council will assess its risk appetite in conjunction with budgetary pressures to reduce total interest costs. Longer-term borrowing could also be undertaken for the purpose of certainty, where that is desirable.
 - While this authority will not be able to avoid borrowing to finance new capital expenditure, there will be a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.

3.3 BORROWING STRATEGY

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

It is anticipated that the Council will need to take external borrowing from 2021/22 to meet the funding requirements of its Capital Programme 2020-2025. Against this background and the risks within the economic forecast, caution will be adopted with the 2021/22 treasury operations. The Assistant Director of Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances. Monitoring arrangements are detailed at Appendix 5.

3.4 Policy on borrowing in advance of need

The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

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

3.5 Debt rescheduling

Rescheduling of current borrowing in our debt portfolio is unlikely to occur as the 100 bps increase in PWLB rates only applied to new borrowing rates and not to premature debt repayment rates.

If rescheduling was done, it will be reported to the Audit Committee, at the earliest meeting following its action.

3.6 New Financial Institutions as a source of borrowing and / or types of borrowing

Currently the PWLB Certainty Rate is set at gilts + 80 basis points for both HRA and non-HRA borrowing. However, consideration may still need to be given to sourcing funding from the following sources for the following reasons:

- Local authorities (primarily shorter dated maturities out to 3 years or so – still cheaper than the Certainty Rate).
- Financial institutions (primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a “cost of carry” or to achieve refinancing certainty over the next few years).
- Municipal Bonds Agency (possibly still a viable alternative depending on market circumstances prevailing at the time).

Our advisors will keep us informed as to the relative merits of each of these alternative funding sources.

4 ANNUAL INVESTMENT STRATEGY

4.1 Investment policy – management of risk

The MHCLG and CIPFA have extended the meaning of ‘investments’ to include both financial and non-financial investments. This report deals solely with financial investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy, (a separate report).

The Council’s investment policy has regard to the following: -

- MHCLG’s Guidance on Local Government Investments (“the Guidance”)
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 (“the Code”)
- CIPFA Treasury Management Guidance Notes 2018

The Council’s investment priorities will be security first, portfolio liquidity second and then yield, (return).

The above guidance from the MHCLG and CIPFA place a high priority on the management of risk. This authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

1. Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.
2. **Other information:** ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as “**credit default swaps**” and overlay that information on top of the credit ratings.
3. **Other information sources** used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.
4. This authority has defined the list of **types of investment instruments** that the treasury management team are authorised to use. There are two lists in appendix 5.4 under the categories of ‘specified’ and ‘non-specified’ investments.
 - **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.
 - **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.

5. **Non-specified investments limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being £4m of the total investment portfolio, (see paragraph 4.3).
6. **Lending limits**, (amounts and maturity), for each counterparty will be set through applying the matrix table in paragraph 4.2.
7. **Transaction limits** are set for each type of investment in 4.2.
8. This authority will set a limit for the amount of its investments which are invested for **longer than 365 days**, (see paragraph 4.4).
9. Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating**, (see paragraph 4.3).
10. This authority has engaged **external consultants**, (see paragraph 1.5), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.
11. All investments will be denominated in **sterling**.
12. As a result of the change in accounting standards for 2020/21 under IFRS 9, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the Ministry of Housing, Communities and Local Government, [MHCLG], concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years ending 31.3.23.

However, this authority will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance, (see paragraph 4.5). Regular monitoring of investment performance will be carried out during the year.

Changes in risk management policy from last year.

The above criteria are unchanged from last year.

4.2 Creditworthiness policy

This Council applies 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, Moody's and Standard & Poor's. The credit ratings of counterparties are supplemented with the following overlays:

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

This 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 creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands:

Yellow	5 years
Dark pink	5 years for Ultra-Short Dated Bond Funds with a credit score of 1.25
Light pink	5 years for Ultra-Short Dated Bond Funds with a credit score of 1.5
Purple	2 years
Blue	1 year (only applies to nationalised or semi nationalised UK Banks)
Orange	1 year
Red	6 months
Green	100 days
No colour	not to be used

The Link Asset Services' creditworthiness service uses a wider array of information other than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

Typically the minimum credit ratings criteria the Council use will be a 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 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.

All credit ratings will be monitored regularly. The Council is alerted to changes to ratings of all three agencies through its use of the Link Asset Services' creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information, information on any external support for banks to help support its decision making process.

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour

Counterparties	Colour (and long term rating where applicable)	Money per institution Limit	Time Limit
Banks *	yellow	£2m	5yrs
Banks	purple	£4m	2 yrs
Banks	orange	£4m	1 yr
Banks – part nationalised	blue	£4m	1yr
Banks	red	£4m	6 mths
Banks	green	£4m	100 days
Banks	No colour	Not to be used	
DMADF (Debt Management Account Deposit Facility)	UK sovereign rating	Unlimited	6 months
Local authorities	yellow	£10m	Unlimited
Local Authorities Companies which are 100% owned by the Borough Council King's Lynn and West Norfolk	N/A	£12m	Unlimited
	Fund rating	Money and/or % Limit	Time Limit
Money Market Funds CNAV	AAA	£4m	liquid
Money Market Funds LVNAV	AAA	£4m	liquid
Money Market Funds VNAV	AAA	£4m	liquid
Ultra-Short Dated Bond Funds with a credit score of 1.25	Dark pink / AAA	£3m	liquid
Ultra-Short Dated Bond Funds with a credit score of 1.50	Light pink / AAA	£3m	liquid

*Please note: the yellow colour category is for UK Government debt, or its equivalent, money market funds and collateralised deposits where the collateral is UK Government debt – see appendix 5.4.

4.3 Other limits

Due care will be taken to consider the exposure of the Council's total investment portfolio to non-specified investments, countries, groups and sectors.

- a) **Non-specified investment limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being £4m of the total investment portfolio.
- b) **Country limit.** The Council has determined that it will only use approved counterparties from the UK and from countries with a **minimum sovereign credit rating of AA-** from Fitch. The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 5.4. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.
- c) **Other limits.** In addition:
 - no more than £4m will be placed with any non-UK country at any time;
 - limits in place above will apply to a group of companies;
 - sector limits will be monitored regularly for appropriateness.

4.4 Investment strategy

In-house funds. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. While most cash balances are required in order to manage the ups and downs of cash flow, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed.

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

Investment returns expectations.

Bank Rate is unlikely to rise from 0.10% for a considerable period. It is very difficult to say when it may start rising so it may be best to assume that investment earnings from money market-related instruments will be sub 0.50% for the foreseeable future.

The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows (the long term forecast is for periods over 10 years in the future):

Average earnings in each year	
2020/21	0.10%
2021/22	0.10%
2022/23	0.10%
2023/24	0.10%
2024/25	0.25%
Long term later years	2.00%

- The overall balance of risks to economic growth in the UK is probably now skewed to the upside but is subject to major uncertainty due to the virus and how quickly successful vaccines may become available and widely administered to the population.

- There is relatively little UK domestic risk of increases or decreases in Bank Rate and significant changes in shorter term PWLB rates. The Bank of England has effectively ruled out the use of negative interest rates in the near term and increases in Bank Rate are likely to be some years away given the underlying economic expectations. However, it is always possible that safe haven flows, due to unexpected domestic developments and those in other major economies, or a return of investor confidence in equities, could impact gilt yields, (and so PWLB rates), in the UK.

Negative investment rates

While the Bank of England said in August / September 2020 that it is unlikely to introduce a negative Bank Rate, at least in the next 6 -12 months, and in November omitted any mention of negative rates in the minutes of the meeting of the Monetary Policy Committee, some deposit accounts are already offering negative rates for shorter periods. As part of the response to the pandemic and lockdown, the Bank and the Government have provided financial markets and businesses with plentiful access to credit, either directly or through commercial banks. In addition, the Government has provided large sums of grants to local authorities to help deal with the COVID crisis; this has caused some local authorities to have sudden large increases in cash balances searching for an investment home, some of which was only very short term until those sums were able to be passed on.

As for money market funds (MMFs), yields have continued to drift lower. Some managers have already resorted to trimming fee levels to ensure that net yields for investors remain in positive territory where possible and practical. Investor cash flow uncertainty, and the need to maintain liquidity in these unprecedented times, has meant there is a surfeit of money swilling around at the very short end of the market. This has seen a number of market operators, now including the DMADF, offer nil or negative rates for very short-term maturities. This is not universal, and MMFs are still offering a marginally positive return, as are a number of financial institutions for investments at the very short end of the yield curve.

Inter-local authority lending and borrowing rates have also declined due to the surge in the levels of cash seeking a short-term home at a time when many local authorities are probably having difficulties over accurately forecasting when disbursements of funds received will occur or when further large receipts will be received from the Government.

Investment treasury indicator and limit - total principal funds invested for greater than 365 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment and are based on the availability of funds after each year-end.

The Council is asked to approve the following treasury indicator and limit:

Maximum principal sums invested > 365 days			
	2021/2022	2022/2023	2023/2024
Principal sums invested > 365 days	£4m	£4m	£4m
With Local Authorities	£10m	£10m	£10m
With Local Authorities Companies which are 100% owned by BCKLWN	£12m	£12m	£12m
Current investments as at 31.01.20 in excess of 1 year maturing in each year	£8m	-	-

4.5 End of year investment report

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

4.6 Financial Implications

The financial implications of the borrowing and investment strategy and MRP are reflected in the financing adjustment figure included in the Financial Plan 2020-2025 to be approved at Council on 25 February 2021.

The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this council. To ensure that the council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

4.7 Risk Management Implications

There are elements of risk in dealing with the treasury management function although the production and monitoring of such controls as Prudential Indicators and Treasury Management Strategies help to reduce the exposure of the council to the market. The costs and returns on borrowing and investment are in themselves a reflection of risk that is seen by the market forces. The action and controls outlined in the report will provide for sound financial and performance management procedures.

4.8 Policy Implications

There are no other changes in the Treasury Management policy at present, other than those outlined in this report. Appendices 5.5 and 5.6 detail the treasury management scheme of delegation and the role of the Section 151 Officer.

4.9 Statutory Considerations

The council must set Prudential Indicators and adopt a Treasury Management Strategy and Annual investment Strategy before 31 March 2021.

4.10 Access to Information

Monthly Monitoring reports 2020/2021 and 2021/2022
The Financial Plan 2020-2025
Capital Programme 2020-2025
Council Website – Treasury Management Practices
Capital and Local Property Investment Fund Strategy 2017/2021
Capital Strategy 2020/2021 and 2021/2022

5 APPENDICES

1. Prudential and treasury indicators and MRP statement
2. Economic background
3. Treasury management practice 1 – credit and counterparty risk management
4. Approved countries for investments
5. Treasury management scheme of delegation
6. The treasury management role of the section 151 officer

5.1 THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2021/22 – 2024/25 AND MRP STATEMENT

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

5.1.1 Capital expenditure

	2020/2021	2021/2022	2022/2023	2023/2024	2024/2025
	£	£	£	£	£
Major Projects	11,590,610	29,711,470	44,307,400	26,289,520	18,045,180
Operational:					
Community and Partnerships	2,343,120	2,316,850	2,260,000	2,260,000	2,260,000
Resources	465,680	150,000	150,000	150,000	150,000
Regeneration	21,350	-	-	-	-
Property and Projects	42,000	28,000	-	-	-
Operational and Commercial Services	987,990	2,204,150	170,500	507,770	100,000
Alive West Norfolk	68,860	1,261,490	25,000	-	-
Total	15,519,610	35,671,960	46,912,900	29,207,290	20,555,180
Exempt Schemes (Major Projects)	5,122,840	19,230,000	18,848,270	3,461,660	-
Total Capital Programme	20,642,450	54,901,960	65,761,170	32,668,950	20,555,180

5.1.2 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 Council's overall finances. The Council is asked to approve the following indicators:

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.

%	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000	2023/24 Estimate £'000	2024/25 Estimate £'000
Services	3.13	2.01	2.29	2.22	2.04
Commercial activities	0.06	0.72	0.62	1.16	1.79

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

5.1.3 Maturity structure of borrowing

Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

The Council is asked to approve the following treasury indicators and limits:

£m	2020/21	2021/22	2022/23
Interest rate exposures			
	Upper	Upper	Upper
Limits on fixed interest rates based on net debt	100%	100%	100%
Limits on variable interest rates based on net debt	40%	40%	40%
Maturity structure of fixed interest rate borrowing 2021/22			
	Lower	Upper	£m
Under 12 months	0%	100%	-
12 months to 2 years	0%	100%	-
2 years to 50 years	0%	100%	-
50 years +	0%	100%	10

5.1.5. Control of interest rate exposure

Please see paragraphs 3.3, 3.4 and 4.4.

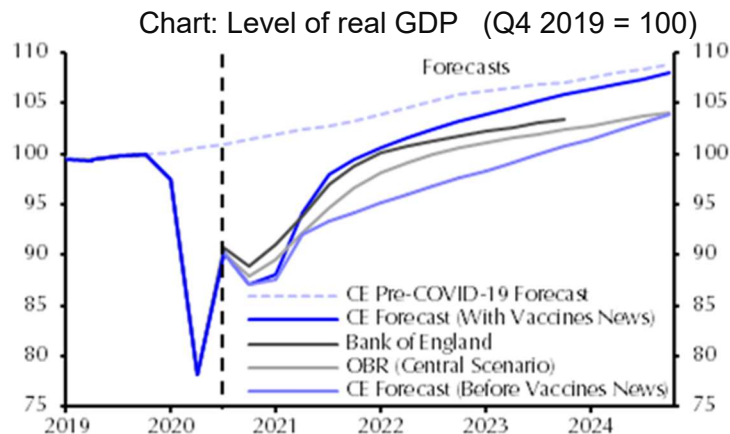
5.2 ECONOMIC BACKGROUND

- **UK.** The key quarterly meeting of the Bank of England Monetary Policy Committee kept **Bank Rate** unchanged on 5.11.20. However, it revised its economic forecasts to take account of a second national lockdown from 5.11.20 to 2.12.20 which is obviously going to put back economic recovery and do further damage to the economy. It therefore decided to do a further tranche of **quantitative easing (QE) of £150bn**, to start in January when the current programme of £300bn of QE, announced in March to June, runs out. It did this so that “announcing further asset purchases now should support the economy and help to ensure the unavoidable near-term slowdown in activity was not amplified by a tightening in monetary conditions that could slow the return of inflation to the target”.
- Its forecasts appeared, at that time, to be rather optimistic in terms of three areas:
 - The economy would recover to reach its pre-pandemic level in Q1 2022
 - The Bank also expected there to be excess demand in the economy by Q4 2022.
 - CPI inflation was therefore projected to be a bit above its 2% target by the start of 2023 and the “inflation risks were judged to be balanced”.
- Significantly, there was no mention of **negative interest rates** in the minutes or Monetary Policy Report, suggesting that the MPC remains some way from being persuaded of the case for such a policy, at least for the next 6 -12 months. However, rather than saying that it “stands ready to adjust monetary policy”, the MPC this time said that it will take “whatever additional action was necessary to achieve its remit”. The latter seems stronger and wider and may indicate the Bank’s willingness to embrace new tools.
- One key addition to **the Bank’s forward guidance in August** was a new phrase in the policy statement, namely that “it does not intend to tighten monetary policy until there is clear evidence that significant progress is being made in eliminating spare capacity and achieving the 2% target sustainably”. That seems designed to say, in effect, that even if inflation rises to 2% in a couple of years’ time, do not expect any action from the MPC to raise Bank Rate – until they can clearly see that level of inflation is going to be persistently above target if it takes no action to raise Bank Rate. Our Bank Rate forecast currently shows no increase, (or decrease), through to quarter 1 2024 but there could well be no increase during the next five years as it will take some years to eliminate spare capacity in the economy, and therefore for inflationary pressures to rise to cause the MPC concern. **Inflation** is expected to briefly peak at just over 2% towards the end of 2021, but this is a temporary short-lived factor and so not a concern.
- However, the minutes did contain several references to **downside risks**. The MPC reiterated that the “recovery would take time, and the risks around the GDP projection were judged to be skewed to the downside”. It also said, “the risk of a more persistent period of elevated unemployment remained material”. Downside risks could well include severe restrictions remaining in place in some form during the rest of December and most of January too. **Upside risks** included the early roll out of effective vaccines.
- **COVID-19 vaccines.** We had been waiting expectantly for news that various COVID-19 vaccines would be cleared as being safe and effective for administering to the general public. The Pfizer announcement on 9th November was very encouraging as its 90% effectiveness was much higher than the 50-60% rate of effectiveness of flu vaccines which might otherwise have been expected. However, this vaccine has demanding cold storage requirements of minus 70c that impairs

the speed of application to the general population. It has therefore been particularly welcome that the Oxford University/AstraZeneca vaccine has now also been approved which is much cheaper and only requires fridge temperatures for storage. The Government has 60m doses on order and is aiming to vaccinate at a rate of 2m people per week starting in January, though this rate is currently restricted by a bottleneck on vaccine production; (a new UK production facility is due to be completed in June).

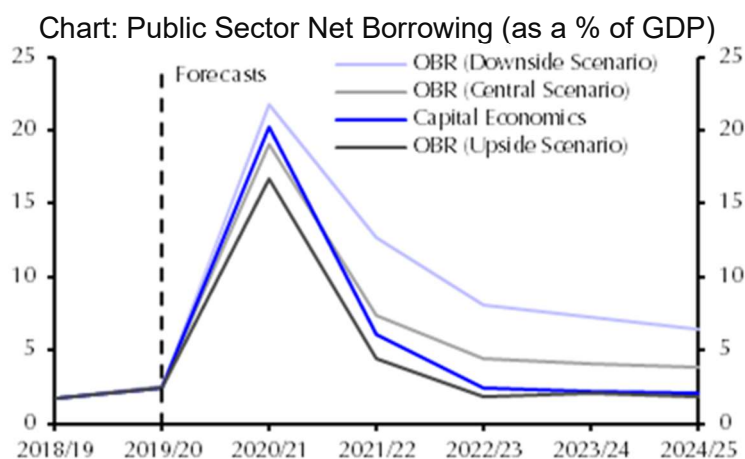
- These announcements, plus expected further announcements that other vaccines could be approved soon, have enormously boosted confidence that **life could largely return to normal during the second half of 2021**, with activity in the still-depressed sectors like restaurants, travel and hotels returning to their pre-pandemic levels; this would help to bring the unemployment rate down. With the household saving rate having been exceptionally high since the first lockdown in March, there is plenty of pent-up demand and purchasing power stored up for these services. A comprehensive roll-out of vaccines might take into late 2021 to fully complete; but if these vaccines prove to be highly effective, then there is a possibility that restrictions could start to be eased, beginning possibly in Q2 2021 once vulnerable people and front-line workers have been vaccinated. At that point, there would be less reason to fear that hospitals could become overwhelmed any more. Effective vaccines would radically improve the economic outlook once they have been widely administered; it may allow GDP to rise to its pre-virus level a year earlier than otherwise and mean that the unemployment rate peaks at 7% in 2021 instead of 9%.
- **Public borrowing** was forecast in November by the Office for Budget Responsibility (the OBR) to reach £394bn in the current financial year, the highest ever peace time deficit and equivalent to 19% of GDP. In normal times, such an increase in total gilt issuance would lead to a rise in gilt yields, and so PWLB rates. However, the QE done by the Bank of England has depressed gilt yields to historic low levels, (as has similarly occurred with QE and debt issued in the US, the EU and Japan). This means that new UK debt being issued, and this is being done across the whole yield curve in all maturities, is locking in those historic low levels through until maturity. In addition, the UK has one of the longest average maturities for its entire debt portfolio, of any country in the world. Overall, this means that the total interest bill paid by the Government is manageable despite the huge increase in the total amount of debt. The OBR was also forecasting that the government will still be running a budget deficit of £102bn (3.9% of GDP) by 2025/26. However, initial impressions are that they have taken a pessimistic view of the impact that vaccines could make in the speed of economic recovery.
- Overall, **the pace of recovery** was not expected to be in the form of a rapid V shape, but a more elongated and prolonged one. The initial recovery was sharp after quarter 1 saw growth at -3.0% followed by -18.8% in quarter 2 and then an upswing of +16.0% in quarter 3; this still left the economy 8.6% smaller than in Q4 2019. It is likely that the one-month national lockdown that started on 5th November, will have caused a further contraction of 8% m/m in November so the economy may have then been 14% below its pre-crisis level.
- **December 2020 / January 2021**. Since then, there has been rapid backtracking on easing restrictions due to the spread of a new mutation of the virus, and severe restrictions were imposed across all four nations. These restrictions were changed on 5.1.21 to national lockdowns of various initial lengths in each of the four nations as the NHS was under extreme pressure. It is now likely that wide swathes of the UK will remain under these new restrictions for some months; this means that the near-term outlook for the economy is grim. However, the distribution of vaccines and the expected consequent removal of COVID-19 restrictions, should allow GDP

to rebound rapidly in the second half of 2021 so that the economy could climb back to its pre-pandemic peak as soon as late in 2022. Provided that both monetary and fiscal policy are kept loose for a few years yet, then it is still possible that in the second half of this decade, the economy may be no smaller than it would have been if COVID-19 never happened. The significant caveat is if another mutation of COVID-19 appears that defeats the current batch of vaccines. However, now that science and technology have caught up with understanding this virus, new vaccines ought to be able to be developed more quickly to counter such a development and vaccine production facilities are being ramped up around the world.



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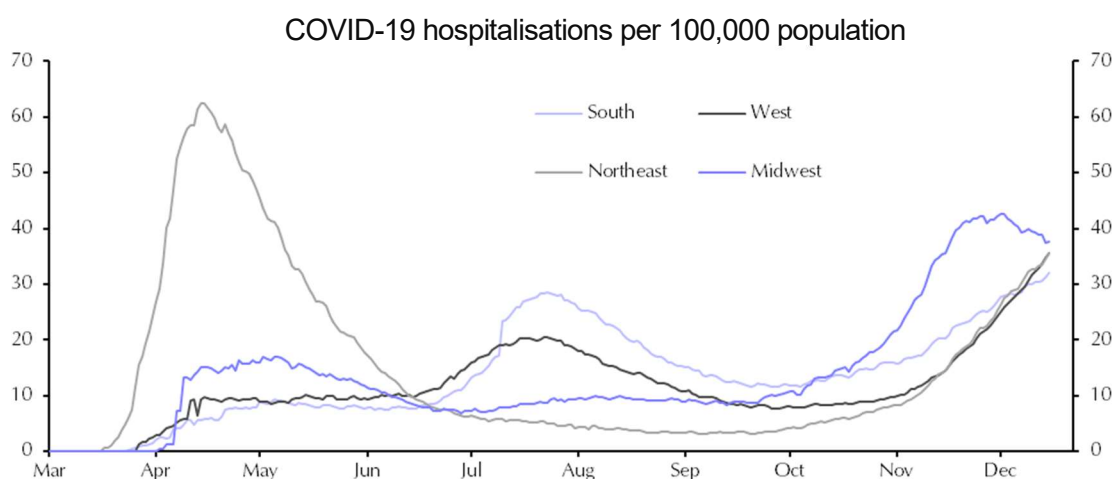
This recovery of growth which eliminates the effects of the pandemic by about the middle of the decade would have major repercussions for public finances as it would be consistent with the government deficit falling to around 2.5% of GDP without any tax increases. This would be in line with the OBR's most optimistic forecast in the graph below, rather than their current central scenario which predicts a 4% deficit due to assuming much slower growth. However, Capital Economics forecasts assumed that there is a reasonable Brexit deal and also that politicians do not raise taxes or embark on major austerity measures and so, (perversely!), depress economic growth and recovery.



(if unable to print in colour..... the key describing each line in the above graph is in sequential order from top to bottom in parallel with the lines in the graph.)

- There will still be some **painful longer-term adjustments** as e.g. office space and travel by planes, trains and buses may not recover to their previous level of use for several years, or possibly ever, even if vaccines are fully successful in overcoming the current virus. There is also likely to be a reversal of globalisation as this crisis has exposed how vulnerable long-distance supply chains are. On the other hand, digital services are one area that has already seen huge growth.
- **Brexit.** While the UK has been gripped by the long running saga of whether or not a deal would be made by 31.12.20, the final agreement on 24.12.20, followed by ratification by Parliament and all 27 EU countries in the following week, has eliminated a significant downside risk for the UK economy. The initial agreement only covers trade so there is further work to be done on the services sector where temporary equivalence has been granted in both directions between the UK and EU; that now needs to be formalised on a permanent basis. As the forecasts in this report were based on an assumption of a Brexit agreement being reached, there is no need to amend these forecasts.
- **Monetary Policy Committee meeting of 17 December.** All nine Committee members voted to keep interest rates on hold at +0.10% and the Quantitative Easing (QE) target at £895bn. The MPC commented that the successful rollout of vaccines had reduced the downsides risks to the economy that it had highlighted in November. But this was caveated by it saying, “Although all members agreed that this would reduce downside risks, they placed different weights on the degree to which this was also expected to lead to stronger GDP growth in the central case.” So, while the vaccine is a positive development, in the eyes of the MPC at least, the economy is far from out of the woods. As a result of these continued concerns, the MPC voted to extend the availability of the Term Funding Scheme, (cheap borrowing), with additional incentives for small and medium size enterprises for six months from 30.4.21 until 31.10.21. (The MPC had assumed that a Brexit deal would be agreed.)
- **Fiscal policy.** In the same week as the MPC meeting, the Chancellor made a series of announcements to provide further support to the economy: -
 - An extension of the COVID-19 loan schemes from the end of January 2021 to the end of March.
 - The furlough scheme was lengthened from the end of March to the end of April.
 - The Budget on 3.3.21 will lay out the “next phase of the plan to tackle the virus and protect jobs”. This does not sound like tax rises are imminent, (which could hold back the speed of economic recovery).
- The **Financial Policy Committee** (FPC) report on 6.8.20 revised down their expected credit losses for the banking sector to “somewhat less than £80bn”. It stated that in its assessment, “banks have buffers of capital more than sufficient to absorb the losses that are likely to arise under the MPC’s central projection”. The FPC stated that for real stress in the sector, the economic output would need to be twice as bad as the MPC’s projection, with unemployment rising to above 15%.
- **US.** The result of **the November elections** meant that while the Democrats gained the presidency and a majority in the House of Representatives, it looks as if the Republicans could retain their slim majority in the Senate provided they keep hold of two key seats in Georgia in elections in early January. If those two seats do swing to the Democrats, they will then control both Houses and President Biden will consequently have a free hand to determine policy and to implement his election manifesto.

- **The economy** had been recovering quite strongly from its contraction in 2020 of 10.2% due to the pandemic with GDP only 3.5% below its pre-pandemic level and the unemployment rate dropping below 7%. However, the rise in new cases during quarter 4, to the highest level since mid-August, suggests that the US could be in the early stages of a fourth wave. While the first wave in March and April was concentrated in the Northeast, and the second wave in the South and West, the third wave in the Midwest looks as if it now abating. However, it also looks as if the virus is rising again in the rest of the country. The latest upturn poses a threat that the recovery in the economy could stall. This is **the single biggest downside risk** to the shorter term outlook – a more widespread and severe wave of infections over the winter months, which is compounded by the impact of the regular flu season and, as a consequence, threatens to overwhelm health care facilities. Under those circumstances, states might feel it necessary to return to more draconian lockdowns.



- The restrictions imposed to control the spread of the virus are once again weighing on the economy with employment growth slowing sharply in November and retail sales dropping back. The economy is set for further weakness in December and into the spring. However, a \$900bn fiscal stimulus deal passed by Congress in late December will limit the downside through measures which included a second round of direct payments to households worth \$600 per person and a three-month extension of enhanced unemployment insurance (including a \$300 weekly top-up payment for all claimants). GDP growth is expected to rebound markedly from the second quarter of 2021 onwards as vaccines are rolled out on a widespread basis and restrictions are loosened.
- After Chair Jerome Powell unveiled the **Fed's adoption of a flexible average inflation target** in his Jackson Hole speech in late August 2020, the mid-September meeting of the Fed agreed by a majority to a toned down version of the new inflation target in his speech - that *"it would likely be appropriate to maintain the current target range until labour market conditions were judged to be consistent with the Committee's assessments of maximum employment and inflation had risen to 2% and was on track to moderately exceed 2% for some time."* This change was aimed to provide more stimulus for economic growth and higher levels of employment and to avoid the danger of getting caught in a deflationary "trap" like Japan. It is to be noted that inflation has actually been under-shooting the 2% target significantly for most of the last decade, (and this year), so financial markets took note that higher levels of inflation are likely to be in the pipeline; long-term bond yields duly rose after the meeting. The FOMC's updated economic and rate projections in mid-September showed that

officials expect to leave the fed funds rate at near-zero until at least end-2023 and probably for another year or two beyond that. There is now some expectation that where the Fed has led in changing its inflation target, other major central banks will follow. The increase in tension over the last year between the US and China is likely to lead to a lack of momentum in progressing the initial positive moves to agree a phase one trade deal.

- The Fed's meeting on **5 November** was unremarkable - but at a politically sensitive time around the elections. At its **16 December** meeting the Fed tweaked the guidance for its monthly asset quantitative easing purchases with the new language implying those purchases could continue for longer than previously believed. Nevertheless, with officials still projecting that inflation will only get back to 2.0% in 2023, the vast majority expect the fed funds rate to be still at near-zero until 2024 or later. Furthermore, officials think the balance of risks surrounding that median inflation forecast are firmly skewed to the downside. The key message is still that policy will remain unusually accommodative – with near-zero rates and asset purchases – continuing for several more years. This is likely to result in keeping Treasury yields low – which will also have an influence on gilt yields in this country.
- **EU.** In early December, the figures for Q3 GDP confirmed that the economy staged a rapid rebound from the first lockdowns. This provides grounds for optimism about growth prospects for next year. In Q2, GDP was 15% below its pre-pandemic level. But in Q3 the economy grew by 12.5% q/q leaving GDP down by “only” 4.4%. That was much better than had been expected earlier in the year. However, growth is likely to stagnate during Q4 and in Q1 of 2021, as a second wave of the virus has affected many countries: it is likely to hit hardest those countries more dependent on tourism. The €750bn fiscal support package eventually agreed by the EU after prolonged disagreement between various countries, is unlikely to provide significant support, and quickly enough, to make an appreciable difference in the countries most affected by the first wave.
- With inflation expected to be unlikely to get much above 1% over the next two years, **the ECB** has been struggling to get inflation up to its 2% target. It is currently unlikely that it will cut its central rate even further into negative territory from -0.5%, although the ECB has stated that it retains this as a possible tool to use. The ECB's December meeting added a further €500bn to the PEPP scheme, (purchase of government and other bonds), and extended the duration of the programme to March 2022 and re-investing maturities for an additional year until December 2023. Three additional tranches of TLTRO, (cheap loans to banks), were approved, indicating that support will last beyond the impact of the pandemic, implying indirect yield curve control for government bonds for some time ahead. The Bank's forecast for a return to pre-virus activity levels was pushed back to the end of 2021, but stronger growth is projected in 2022. The total PEPP scheme of €1,850bn of QE which started in March 2020 is providing protection to the sovereign bond yields of weaker countries like Italy. There is therefore unlikely to be a euro crisis while the ECB is able to maintain this level of support. However, as in the UK and the US, the advent of highly effective vaccines will be a game changer, although growth will struggle before later in quarter 2 of 2021.
- **China.** After a concerted effort to get on top of the virus outbreak in Q1, economic recovery was strong in Q2 and then into Q3 and Q4; this has enabled China to recover all of the contraction in Q1. Policy makers have both quashed the virus and implemented a programme of monetary and fiscal support that

has been particularly effective at stimulating short-term growth. At the same time, China's economy has benefited from the shift towards online spending by consumers in developed markets. These factors help to explain its comparative outperformance compared to western economies. However, this was achieved by major central government funding of yet more infrastructure spending. After years of growth having been focused on this same area, any further spending in this area is likely to lead to increasingly weaker economic returns in the longer term. This could, therefore, lead to a further misallocation of resources which will weigh on growth in future years.

- **Japan.** A third round of fiscal stimulus in early December took total fresh fiscal spending this year in response to the virus close to 12% of pre-virus GDP. That's huge by past standards, and one of the largest national fiscal responses. The budget deficit is now likely to reach 16% of GDP this year. Coupled with Japan's relative success in containing the virus without draconian measures so far, and the likelihood of effective vaccines being available in the coming months, the government's latest fiscal effort should help ensure a strong recovery and to get back to pre-virus levels by Q3 2021 – around the same time as the US and much sooner than the Eurozone.
- **World growth.** World growth will have been in recession in 2020. Inflation is unlikely to be a problem for some years due to the creation of excess production capacity and depressed demand caused by the coronavirus crisis.
- Until recent years, world growth has been boosted by increasing **globalisation** i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last thirty years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy. The Chinese government has targeted achieving major world positions in specific key sectors and products, especially high tech areas and production of rare earth minerals used in high tech products. It is achieving this by massive financial support, (i.e. subsidies), to state owned firms, government directions to other firms, technology theft, restrictions on market access by foreign firms and informal targets for the domestic market share of Chinese producers in the selected sectors. This is regarded as being unfair competition that is putting western firms at an unfair disadvantage or even putting some out of business. It is also regarded with suspicion on the political front as China is an authoritarian country that is not averse to using economic and military power for political advantage. The current trade war between the US and China therefore needs to be seen against that backdrop. It is, therefore, likely that we are heading into a period where there will be a **reversal of world globalisation and a decoupling of western countries** from dependence on China to supply products. This is likely to produce a backdrop in the coming years of weak global growth and so weak inflation.

Summary

Central banks are, therefore, likely to support growth by maintaining loose monetary policy through keeping rates very low for longer. Governments could also help a quicker recovery by providing more fiscal support for their economies at a time when total debt is affordable due to the very low rates of interest. They will also need to avoid significant increases in taxation or austerity measures that depress demand in their economies.

If there is a huge surge in investor confidence as a result of successful vaccines which leads to a major switch out of government bonds into equities, which, in turn, causes government debt yields to rise, then there will be pressure on central banks to actively manage debt yields by further QE purchases of government debt; this would help to suppress the rise in debt yields and so keep the total interest bill on greatly expanded government debt portfolios within manageable parameters. It is also the main alternative to a programme of austerity.

INTEREST RATE FORECASTS

Brexit. The interest rate forecasts provided by Link in paragraph 3.3 were predicated on an assumption of a reasonable agreement being reached on trade negotiations between the UK and the EU by 31.12.20. There is therefore no need to revise these forecasts now that a trade deal has been agreed. Brexit may reduce the economy's potential growth rate in the long run. However, much of that drag is now likely to be offset by an acceleration of productivity growth triggered by the digital revolution brought about by the COVID crisis.

The balance of risks to the UK

- The overall balance of risks to economic growth in the UK is probably now skewed to the upside but is still subject to some uncertainty due to the virus and the effect of any mutations, and how quick vaccines are in enabling a relaxation of restrictions.
- There is relatively little UK domestic risk of increases or decreases in Bank Rate and significant changes in shorter term PWLB rates. The Bank of England has effectively ruled out the use of negative interest rates in the near term and increases in Bank Rate are likely to be some years away given the underlying economic expectations. However, it is always possible that safe haven flows, due to unexpected domestic developments and those in other major economies, could impact gilt yields, (and so PWLB rates), in the UK.

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

- **UK government** takes too much action too quickly to raise taxation or introduce austerity measures that depress demand in the economy.
- **UK - Bank of England** takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- A resurgence of the **Eurozone sovereign debt crisis**. The ECB has taken monetary policy action to support the bonds of EU states, with the positive impact most likely for "weaker" countries. In addition, the EU agreed a €750bn fiscal support package. These actions will help shield weaker economic regions for the next two or three years. However, in the case of Italy, the cost of the virus crisis has added to its already huge debt mountain and its slow economic growth will leave it vulnerable to markets returning to taking the view that its level of debt is unsupportable. There remains a sharp divide between northern EU countries favouring low debt to GDP and annual balanced budgets and southern countries who want to see jointly issued Eurobonds to finance economic recovery. This divide could undermine the unity of the EU in time to come.
- Weak capitalisation of some **European banks**, which could be undermined further depending on extent of credit losses resultant of the pandemic.
- **German minority government & general election in 2021**. In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. The CDU has

done badly in subsequent state elections but the SPD has done particularly badly. Angela Merkel has stepped down from being the CDU party leader but she will remain as Chancellor until the general election in 2021. This then leaves a major question mark over who will be the major guiding hand and driver of EU unity when she steps down.

- **Other minority EU governments.** Austria, Sweden, Spain, Portugal, Netherlands, Ireland and Belgium also have vulnerable minority governments dependent on coalitions which could prove fragile.
- **Austria, the Czech Republic, Poland and Hungary** now form a strongly anti-immigration bloc within the EU, and they had threatened to derail the 7 year EU budget until a compromise was thrashed out in late 2020. There has also been a rise in anti-immigration sentiment in Germany and France.
- **Geopolitical risks**, for example in China, Iran or North Korea, but also in Europe and other Middle Eastern countries, which could lead to increasing safe haven flows.

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

- **UK** - a significant rise in inflationary pressures e.g. caused by a stronger than currently expected recovery in the UK economy after effective vaccines are administered quickly to the UK population, leading to a rapid resumption of normal life and return to full economic activity across all sectors of the economy.
- The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly within the UK economy, which then necessitates a rapid series of increases in Bank Rate to stifle inflation.

5.3 TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT

SPECIFIED INVESTMENTS: All such investments will be sterling denominated, with **maturities up to a maximum of 1 year**, meeting the minimum 'high' quality criteria where applicable. (Non-specified investments which would be specified investments apart from originally being for a period longer than 12 months, will be classified as being specified once the remaining period to maturity falls to under twelve months.)

NON-SPECIFIED INVESTMENTS: These are any investments which do not meet the specified investment criteria. A maximum of £4m ** will be held in aggregate in non-specified investment.

A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made, it will fall into one of the above categories.

The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

	Minimum credit criteria / colour band	** Max % of total investments / £ limit per institution	Max. maturity period
DMADF – UK Government	yellow	100%	6 months (max. is set by the DMO*)
UK Government gilts	yellow		5 years
UK Government Treasury bills	yellow		364 days (max. is set by the DMO*)
Bonds issued by multilateral development banks	yellow		5 years
Money Market Funds CNAV	AAA	100%	Liquid
Money Market Funds LNAV	AAA		Liquid
Money Market Funds VNAV	AAA		Liquid
Ultra-Short Dated Bond Funds with a credit score of 1.25	AAA	100%	Liquid
Ultra-Short Dated Bond Funds with a credit score of 1.5	AAA	100%	Liquid
Local authorities	yellow	100%	5 years

Term deposits with housing associations	Blue Orange Red Green No Colour		12 months 12 months 6 months 100 days Not for use
Term deposits with banks and building societies	Blue Orange Red Green No Colour		12 months 12 months 6 months 100 days Not for use
CDs or corporate bonds with banks and building societies	Blue Orange Red Green No Colour		12 months 12 months 6 months 100 days Not for use
Gilt funds	UK sovereign rating		
Local Authority Mortgage Scheme. Under LAMS the council is required to place funds with the lender for a period of 5 years. This is classified as being a service investment, rather than a treasury management investment, and is therefore outside of the Specified / Non specified categories.			

* DMO – is the Debt Management Office of H.M.Treasury

Non Specified Investments (can be longer than 1 year)	Minimum Credit Criteria	Use	Max % of total investments	Max. maturity period
With Local Authorities Companies which are 100% owned by the Borough Council King's Lynn and West Norfolk	N/A	In-house	100%	Unlimited
Term deposits – UK government (with maturities in excess of 1 year)	Credit rating in TMP's	In-house	100%	5 years
Term deposits – other LA's (with maturities in excess of 1 year)	Credit rating in TMP's	In-house	100%	5 years
Term deposits – banks and building societies (with maturities in excess of 1 year)	Credit rating in TMP's	In-house	As set out in TMP 1	5 years
Term deposits with unrated counterparties : any maturity	Credit rating in TMP's	In-house	As set out in TMP 1	5 years
Certificates of deposits issued by banks and building societies with maturities in excess of 1 year	Credit rating in TMP's	In house on a 'buy and hold basis' and Fund managers	As set out in TMP 1	2 years
UK Government Gilts with maturities in excess of 1 year	AAA	In house on a 'buy and hold basis' and Fund Managers	As set out in TMP 1	Overall duration of 3 years

Bonds issued by multilateral development banks with maturities in excess of 1 year	AAA	In-house on a 'buy-and-hold' basis. Also for use by fund managers	50% of the total fund	Overall duration of 3 years
Bonds issued by a financial institution which is guaranteed by the UK government with maturities in excess of 1 year	AAA	In-house on a 'buy-and-hold' basis. Also for use by fund managers	50% of the total fund	Overall duration of 3 years
Sovereign bond issues (i.e. other than the UK govt) with maturities in excess of 1 year	AAA	In house on a 'buy and hold basis' and Fund Managers	50% of the total fund	Overall duration of 3 years
Corporate Bonds : <i>the use of these investments would constitute capital expenditure</i>		In house on a 'buy and hold basis' and Fund Managers	50% of the total fund	Overall duration of 3 years
Floating Rate Notes : <i>the use of these investments would constitute capital expenditure unless they are issued by a multi lateral development bank</i>		Fund managers	50% of the total fund	Overall duration of 3 years
Property Fund: the use of these investments would constitute capital expenditure		In house and Fund Managers	50% of the total fund	Overall duration of 10 years

Accounting treatment of investments. The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

5.4 APPROVED COUNTRIES FOR INVESTMENTS

This list is based on those countries which have sovereign ratings of AA- or higher, (we show the lowest rating from Fitch, Moody's and S&P) and also, (except - at the time of writing - for Hong Kong, Norway and Luxembourg), have banks operating in sterling markets which have credit ratings of green or above in the Link credit worthiness service.

Based on lowest available rating

AAA

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

AA+

- Canada
- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)
- France

AA-

- Belgium
- Hong Kong
- Qatar
- U.K.

THIS LIST IS AS AT 5.1.21

5.5 TREASURY MANAGEMENT SCHEME OF DELEGATION

(i) Full Council

- Approval of annual strategy;
- Budget consideration and approval.

(ii) Cabinet

- Amendments to the organisation's adopted clauses, treasury management policy statement;

(iii) Audit Committee

- Receiving and reviewing regular monitoring reports and acting on recommendations;
- Mid-Year Treasury Management Report
- Annual Treasury Report (Actuals)

5.6 THE TREASURY MANAGEMENT ROLE OF THE SECTION 151 OFFICER

The S151 (responsible) officer

- 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;
- recommending the appointment of external service providers.
- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long term timeframe
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money
- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority
- ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following:
 - *Risk management, including investment and risk management criteria for any material non-treasury investment portfolios;*
 - *Performance measurement and management, including methodology and criteria for assessing the performance and success of non-treasury investments;*
 - *Decision making, governance and organisation, including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making;*
 - *Reporting and management information, including where and how often monitoring reports are taken;*

- *Training and qualifications, including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.*