CAMBRIDGESHIRE & PETERBOROUGH COMBINED AUTHORITY | JAMES PALMER CAMBRIDGESHIRE & PETERBOROUGH MAYOR

Agenda Item No: 9

Treasury Management Strategy

To:	Audit and Governance Committee
Meeting Date:	29 January 2021
From:	Robert Emery Deputy Chief Finance Officer
Recommendations:	The Audit and Governance Committee is recommended to: a) Review the Treasury Management and Capital Strategies for 2021-22 b) Note the in-year performance against the adopted 2020-21 prudential and treasury indicators

1. Purpose

1.1 The purpose of the report is for the Audit and Governance Committee to review the proposed Treasury Management and Capital Strategies for 2021/22 and in year performance against the prudential indicators included within the 2020/21 Treasury Management and Capital Strategies.

2. Background

2.1 According to its Terms of Reference, the Audit and Governance Committee shall "ensure there is effective scrutiny of the treasury management strategy and policies in accordance with CIPFA's Code of Practice".

2.2. The Treasury Management in the Public Services: Code of Practice 2017 recommends that Members receive regular reports on the authority's treasury management policies, practices, and activities, including a mid-year review progress report.

3. 2020-21 Treasury Management Strategy Update

3.1. The Combined Authority Board on the 27 January 2021 has been asked to approve an amendment to the 2020/21 Treasury Management Strategy revising the investment limit for a particular class of investment, Money Market Funds (MMFs).

3.2. The Combined Authority's treasury advisors, Arlingclose have revised their investment advice for Money Markets Funds (MMFs), removing the upper limit on sums invested in MMFs in total.

The previously advised limit was in place because individual funds make similar underlying investments which limits the diversification achievable across the ultimate entities invested in, even when money is invested with different funds.

3.3. Unlike fixed term deposits, MMFs allow for near immediate investment and withdrawal of funds and are therefore a key tool to manage credit and liquidity risks. Given the increased risk in other sectors, due to the current economic climate, the relative risk of MMFs is decreased and so the advice has changed to remove the upper limit on investments.

3.4. In line with previous Arlingclose advice, the 2020/21 Treasury Management Strategy limits total investments in MMFs to £100m, with a £25m limit per individual fund. The Board is asked to approve that the £100m total investment limit be removed, whilst retaining the £25m limit per individual fund in line with the advice from our advisors. Holding increased balances with MMFs will allow the CPCA to maximise the security and liquidity of investments whilst protecting yield by reducing the exposure risk of the Combined Authority's investments to negative rates that may be offered by similarly liquid investments such as bank accounts and balances held with the UK Government.

3.5. This change is also reflected in the proposed 2021/22 Treasury Management Strategy

4. 2021-22 Strategies

4.1. The following strategies have been updated for 2021/22 and are attached as Appendix 2.

(a) Capital Strategy: To provide a high-level overview for elected members to understand how stewardship, value for money, prudence, sustainability and affordability will be secured.
(b) Treasury Management Strategy: Being the management of the Authority's cash flows, borrowing and investments and the associated risks.
(c) Investment Strategy: To meet the requirements of statutory guidance in which the Authority would support local public services by lending to or buying shares in other organisations, or to earn investment income.
(d) Minimum Revenue Provision Statement: An MHCLG requirement to approve an MRP Statement each year to ensure that capital expenditure is financed over a reasonable period

4.2. The Committee is asked to review the suite of strategies ahead of being taken to the Board for approval.

5. Treasury Management Strategy Prudential Indicators

5.1. The Prudential Code underpins the system of capital finance. Prudential indicators are developed to ensure that:

a) Capital investment plans are affordable;
b) All external borrowing and other long-term liabilities are within prudent and sustainable levels; and
c) Treasury management decisions are taken in accordance with professional good advice.

5.2. The current performance against the adopted Prudential Indicators is shown at appendix 1.

5.3. The figure for Indicator 9 - Liquidity risk as at 31.8.20 is different to the figure previously reported as it now includes DMO investments. The figures for Indicator 10 – Interest Rate Risk have changed due to the calculation now including the impact of investments maturing within the next 12 months. Actual performance is outside the limit due to higher levels of liquid funds being held to meet operational needs. The limit is increased to £1.5m in the proposed 21/22 Treasury Management Strategy. It should be noted that the calculation of the indicator doesn't take account of forecast spend – the full impact would only materialise if no further spend was undertaken in the next 12 months.

6. Investment Activity

6.1. Surplus cash balances are held in accordance with the principles set out in the Treasury Management Strategy in order to support strategic investment decisions, the Capital Programme, and the Medium-Term Financial Plan (MTFP).

6.2. The table below shows the investments held with Approved Investments in accordance with the Treasury Management Strategy as at 31 March 2020, 31 August 2020 and 31 December 2020.

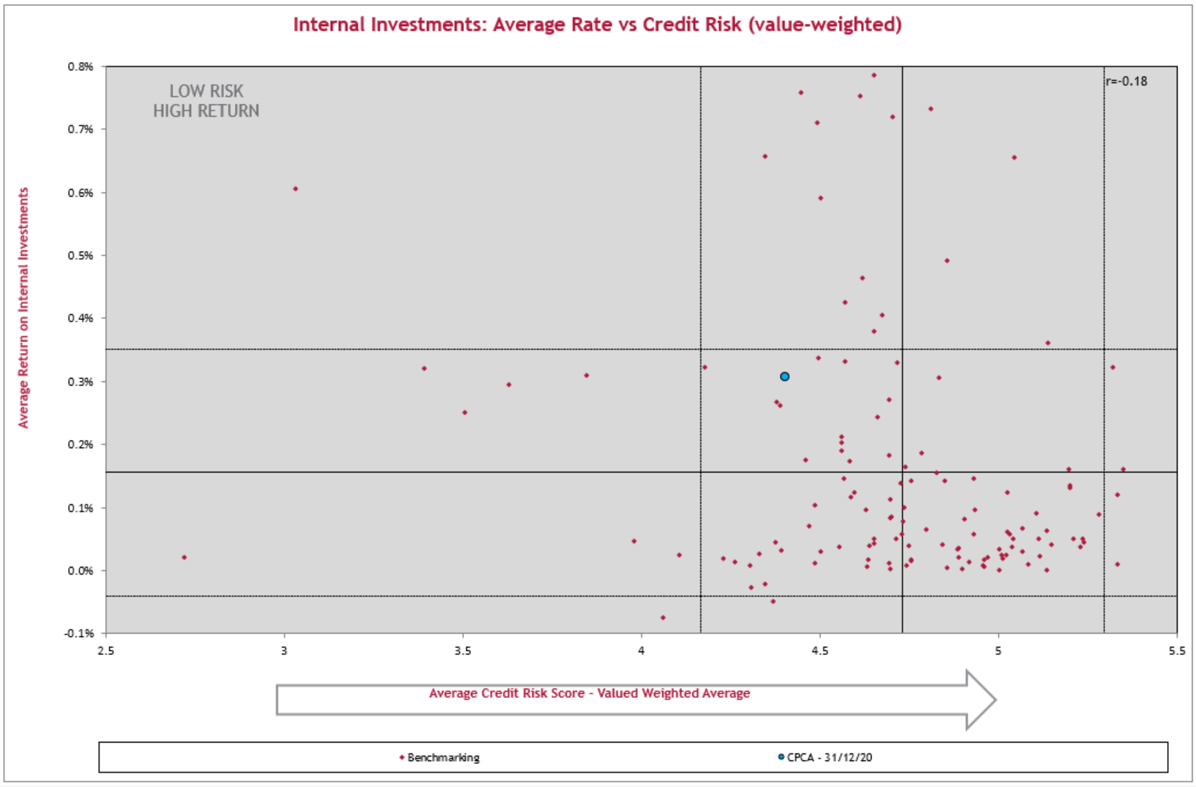
Principal outstanding		As at 31.03.2020		As at 31.08.2020		As at 31.12.2020	
Fixed Term Deposits: Local Authority:		£k	Av. Rate	£k	Av. Rate	£k	Av. Rate
	less than 3 months	69,000	0.88%	40,000	0.85%	50,000	0.50%
	4-6 months	40,000	0.84%	50,000	0.50%	18,000	1.05%
	7-9 months	25,000	0.84%	15,000	0.78%	30,000	0.44%
	10-12 months	15,000	0.97%	20,000	0.44%	23,000	0.33%
	Total Local Authority	**149,000**	**0.87%**	**125,000**	**0.64%**	**121,000**	**0.47%**
DMO	less than 3 months	0	0	46,720	0.01%	26,400	0.01%
Access:							
Call Account		921	0.00%	14,888	0.00%	100	0.01%
Money Market Funds		10,000	0.47%	30,000	0.13%	40,000	0.02%
Total Investments		**159,921**	**0.84%**	**216,608**	**0.39%**	**187,500**	**0.31%**

DMO (formally the Debt Management Account Deposit Facility) is a government department which offers risk-free deposits for Local Authorities.

6.3. In response to the global economic recession due to COVID, the Bank of England, in line with many national and international institutions, has reduced the cost of borrowing (the base rate) to historically low levels. The cost of debt from the Bank has a knock-on effect on lending rates across the country.

6.4. As we predominantly lend to other Local Authorities this reduction in the cost of debt is further exacerbated as Government has made substantial cash injections into the sector and projects have been put on hold, reducing the demand for borrowing and thus the rates achievable. As deals mature they are likely to be replaced at lower rates so even if the rates stabilise, the average rate of the portfolio will continue to fall.

6.5. The investment portfolio compares favourably against benchmarking data provided by our treasury management advisors, Arlingclose. The graph below shows value weighted average credit risk of the portfolio against the average return. The expectation would be that as credit risk increases, returns increase. The Authority’s portfolio has a below average credit risk, whilst enjoying returns close to one standard deviation above the average. The maturity of a portfolio will impact on this metric as more established portfolios with investments taken out longer ago will benefit from the higher rates on offer at the time.



Significant Implications

7. Financial Implications

7.1. None other than those highlighted in the main body of the report.

8. Legal Implications

8.1. Treasury Management activities have to conform to the Local Government Act 2003, the Local Authorities (Capital; Finance and Accounting) (England) Regulations 2003 (SI 2003/3146), which specifies that the Council is required to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice and also the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (SI 2008/414), which clarifies the requirements of the Minimum Revenue Provision guidance.

9. Other Significant Implications

9.1. None

10. Appendices

10.1. Appendix 1 – Prudential Indicators update December 2020

10.2. Appendix 2 – Cambridgeshire and Peterborough Combined Authority Draft Strategies 2021-22

11. Background Papers

11.1. Cambridgeshire and Peterborough Combined Authority Treasury Management Strategy 2020-21

11.2. Cambridgeshire and Peterborough Combined Authority Capital Strategy 2020-21

Appendix 1 – Prudential indicators update December 2020

Prudential Indicators

The Code requires the Combined Authority to set a range of Prudential Indicators. The information provided below sets out the current performance as at 31 December 2020 against the Indicators adopted by the Combined Authority as set out in the Treasury Management Strategy and Capital Strategy.

Indicator 1 - Capital Expenditure in £ millions.
The table shows the Combined Authority's capital expenditure for current and following years. Estimates for future years are taken from the 21/22 Medium Term Financial Plan, the 20/21 forecast is taken from the November Budgetary Control Report.

	2020/21 budget	2020/21 Forecast	2021/22 budget
Capital investments	208.06	182.31	132.37
TOTAL	208.06	182.31	132.37

Indicator 2 – Capital Financing in £ millions.
All capital expenditure must be financed, either from external sources (government grants and other contributions), the Authority's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing and Private Finance Initiative). The planned financing of the above expenditure is as follows:

	2020/21 budget	2020/21 Forecast	2021/22 budget
Grant Funding	201.32	175.57	104.86
Usable Capital Receipts	6.74	6.74	27.51
Debt	0	0	0
TOTAL	**208.06**	**182.31**	**132.37**

Indicator 3 – Gross Debt and the Capital Financing Requirement in £ millions.
The Authority's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The Authority currently has no debt and therefore no CFR. Projected levels of the Authority's total outstanding debt (which comprises borrowing, PFI liabilities, leases) are shown below, compared with the capital financing requirement.

	31.3.2021 budget	31.3.2021 forecast	31.3.2022 budget
Debt (incl. PFI & leases)	0	0	0
Capital Financing Requirement	0	0	0

Indicator 4 – Borrowing and the Liability Benchmark in £ millions.
To compare the Authority’s actual borrowing against an alternative strategy, a liability benchmark is calculated showing the lowest risk level of borrowing. Given that there are no current plans to borrow, this benchmark is currently set at the existing debt cap, but will be kept under review.

	31.3.2021 budget	31.3.2021 forecast	31.3.2022 budget
Outstanding borrowing	0	0	0
Liability benchmark	84.81	84.81	84.61

Indicators 5 and 6 - Authorised limit and operational boundary for external debt in £ millions.
The Authority is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year and to keep it under review. In line with statutory guidance, a lower “operational boundary” is also set as a warning level should debt approach the limit.

	2020/21 limit	2020/21 forecast	2021/22 limit
Authorised limit - total external debt	84.61	0	84.61
Operational boundary - total external debt	74.61	0	74.61

Indicator 7 - Proportion of financing costs to net revenue stream
Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from general government grants.

	2020/21 budget	2020/21 Forecast	2021/22 budget
Financing costs (£m)	£2.56m	0	0
Proportion of net revenue stream	15.1%	0%	0%

Indicator 8 – Credit Risk Indicator.
The Authority has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit score of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk. (low is good)

Credit risk indicator	Target	As at 31.3.2020	As at 30.6.2020	As at 31.12.2020
Portfolio average credit rating	6 (A)	3.96 (AA-)	3.77 (AA-)	4.40 (AA-)

This indicator is provided as at 30.6.20 as it is calculated by our Treasury Management advisors as part of our quarterly benchmarking. The credit rating of investments as at 31.08.2020 is not materially different from the position as at 30.06.2020.

Indicator 9 – Liquidity Risk Indicator.
The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet payments within a rolling three-month period, without additional borrowing.

Liquidity risk indicator	Target	As at 31.3.2020	As at 31.8.2020	As at 31.12.2020
Total cash available within 3 months	£50m	£182.7m	£133.5m	£101.5m

Indicator 10 – Interest Rate Risk Indicator.
This indicator is set to control the Authority’s exposure to interest rate risk.

Interest rate risk indicator	Limit	As at 31.3.2020	As at 31.8.2020	As at 31.12.2020
Upper limit on one-year revenue impact of a 1% rise in interest rates	£1m	£1.1m	£1.6m	£1.3m
Upper limit on one-year revenue impact of a 1% fall in interest rates	£1m	(£1.1m)	(£1.6m)	(£1.3m)

The figure for 1% fall assumes negative rates.

Indicator 11 - Principal sums invested for periods longer than a year (excluding loans).
The purpose of this indicator is to control the Authority’s exposure to the risk of incurring losses by seeking early repayment of its investments. The limits set and performance against them are as follows:

Price risk indicator	2020/21 limit	2021/22 limit	2022/23 limit
Limit on principal invested beyond year end	£160m	£50m	£50m
As at 31.3.2020	£0m	£0m	£0m
As at 31.8.2020	£40m*	£0m	£0m
As at 31.12.2020	£86m*	£10m*	£0m

**The table above includes both deals outstanding as at the relevant dates, plus forward investments which had been agreed at those dates.*