ESSEX POLICE, FIRE AND CRIME COMMISSIONER
FIRE & RESCUE AUTHORITY
Essex County Fire & Rescue Service

Meeting	**Service Leadership Team**	Agenda Item	
Meeting Date	2019	Report Number	
Report Author:	Glenn McGuinness, Acting Chief Finance Officer		
Presented By	Glenn McGuinness, Acting Chief Finance Officer		
Subject	**Treasury Management Strategy Statement 2019/20**		
Type of Report:	Information and Decision		

Recommendations

1. Members of the Team are asked to:
   a) Note the external context of economic background, credit outlook and interest rate outlook.
   b) The local context regarding Capital Financing requirement, need to borrow and investments is noted.
   c) The borrowing and investment strategy is recommended for approval by the Commissioner.
   d) The proposed investment and counterparty limits set out in table 3 are recommended for approval by the Commissioner.
   e) The Treasury Management indicators are approved.
   f) Under Related Matters, approve the strategies for financial derivatives and financial instruments.
   g) Note appendices A, B and C.

Introduction

Treasury management is the management of the Authority's cash flows, borrowing and investments, and the associated risks. The Authority has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Authority's prudent financial management.

Treasury risk management at the Authority is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2017 Edition* (the CIPFA Code) which requires the Authority to approve a treasury management strategy before the start of each financial year. A draft Treasury Management Strategy was submitted to the Performance and

Resources Board on 25th March 2019, a decision was then taken to carry out a review of our current treasury management strategy by Alingclose, an independent treasury advisory company. This report reflects that independent advice.

External Context

Economic background: The UK's progress negotiating its exit from the European Union, together with its future trading arrangements, will continue to be a major influence on the Authority's treasury management strategy for 2019/20.

UK Consumer Price Inflation (CPI) for April was up 2.0% year/year, in line with both the consensus forecast and the Bank of England's November Inflation Report. The most recent labour market data for June 2019 showed the unemployment rate was 3.8%, the lowest since October to December 1974, while the employment rate of 76.1% was the joint highest on record. The 3-month average annual growth rate for pay excluding bonuses was 3.1% as wages continue to rise steadily and provide some pull on general inflation. Adjusted for inflation, real wages grew by 1.5%, a level still likely to have little effect on consumer spending.

The rise in quarterly Gross Domestic Product (GDP) growth to 0.5% in Q1 from 0.2% in the previous quarter was due to growth in the services sector, which picked up as a result of the output of the wholesale, retail and motor trades industries. However, UK economic growth has slowed since and Q2 growth is likely to be sluggish, with the Office of National Statistics already reporting a monthly contraction in GDP for April and Purchasing Managers Index (PMI) data signalling broadly stagnant business conditions. Retail sales in Q1 2019 increased by 1.6% in the three months to March 2019 and this drove the overall growth of services. At 1.8%, annual GDP growth continues to remain below trend. Brexit-related uncertainty has led to a reduction in business investment and a rise in stock building, which is expected to be reflected in growth going forward.

Following the Bank of England's decision to increase Bank Rate to 0.75% in August, no changes to monetary policy has been made since. Global growth slowed over 2018, impacting export-growth for the UK, but is beginning to stabilise. In the UK forecast market-implied interest rates are lower than in many other advanced economies.

While US growth has slowed over 2018, the economy continues to perform robustly. The US Federal Reserve continued its tightening bias throughout 2018, pushing rates to the current 2.25%-2.50% in December. However, a recent softening in US data caused the Fed to signal a pause in hiking interest rates at the last Federal Open Market Committee (FOMC) meeting in March.

Credit outlook: The big four UK banking groups have now divided their retail and investment banking divisions into separate legal entities under ring-fencing legislation. Bank of Scotland, Barclays Bank UK, HSBC UK Bank, Lloyds Bank, National Westminster Bank, Royal Bank of Scotland and Ulster Bank are the ring-fenced banks that now only conduct lower risk retail banking activities. Barclays Bank, HSBC Bank, Lloyds Bank Corporate Markets and NatWest Markets are the investment banks. Credit rating agencies have adjusted the ratings of some of these banks with the ring-fenced banks generally being better rated than their non-ring-fenced counterparts.

The Bank of England (BOE) released its latest report on bank stress testing, illustrating that all entities included in the analysis were deemed to have passed the test once the

levels of capital and potential mitigating actions presumed to be taken by management were factored in. The BoE did not require any bank to raise additional capital.

European banks are considering their approach to Brexit, with some looking to create new UK subsidiaries to ensure they can continue trading here. The credit strength of these new banks remains unknown, although the chance of parental support is assumed very high if ever needed. The uncertainty caused by protracted negotiations between the UK and EU is weighing on the creditworthiness of both UK and European banks with substantial operations in both jurisdictions.

Interest rate forecast: Following the increase in Bank Rate to 0.75% in August 2018, the Monetary Policy Committee's (MPC) bias towards higher interest rates has changed as a result of recent events regarding the resignation of the Prime Minister and the Conservative party leadership contest having increased the uncertainty surrounding Brexit. It is unlikely policymakers will raise Bank Rate unless there is some certainty to the withdrawal agreement; therefore rate rises are unlikely in the short- to medium-term.

Essex County Fire & Rescue appointed Arlingclose, a local authority treasury advisor, to review its treasury strategy. Arlingclose's central case incorporates the MPC keeping Bank Rate at 0.75% for the foreseeable future. The forecast recognises risks to both sides, which is dependent on Brexit outcomes and the evolution of the global economy.

The UK economic environment remains relatively soft, after strong labour market data in the first quarter. Arlingclose's view is that the economy still faces a challenging outlook as it exits the European Union and Eurozone growth softens. While assumptions are that, a Brexit deal is struck and some agreement reached on transition and future trading arrangements before the UK leaves the EU, the possibility of a "no deal" Brexit still hangs over economic activity.

Gilt yields and hence long-term borrowing rates have remained at low levels but some upward movement from current levels is expected based on Arlingclose's interest rate projections, due to the strength of the US economy and the European Central Bank's (ECB) forward guidance on higher rates. 10-year and 20-year gilt yields are forecast to remain around 1.2% and 1.5% respectively over the interest rate forecast horizon, however volatility arising from both economic and political events are likely to continue to offer borrowing opportunities.

A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix A.

For setting the budget, it has been assumed that new investments will be made at an average rate of 0.8%, and that new long-term loans will be borrowed at an average rate of 2.2%.

Local Context

On 31st March 2019, the Authority held £27m of borrowing and £8.5m of investments. This is set out in further detail at ***Appendix B***. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

[Note - 31.3.18 figures are taken from the 2018 audited accounts and 31.3.19 figures are taken from the 2019 unaudited accounts]

Table 1: Balance sheet summary and forecast (further detail 31.3.19 at appendix C)

	31.3.18 Actual £m	**31.3.19 Estimate £m**	**31.3.20 Forecast £m**	**31.3.21 Forecast £m**	**31.3.22 Forecast £m**
General Fund CFR	37.9	36.5	37.0	36.8	36.6
Less: External borrowing *	-28.3	-27.0	-24.5	-24.5	-24.5
Internal borrowing	**9.7**	**9.5**	**12.5**	**12.3**	**12.1**
Less: Usable reserves	-20.4	-21.9	-21.9	-21.9	-21.9
Plus: Working capital	3.1	3.9	3.9	3.9	3.9
Investments	**7.6**	**8.6**	**5.5**	**5.8**	**5.9**

* shows only loans to which the Authority is committed and excludes optional refinancing

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Authority's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

The Authority's capital expenditure plans do not currently imply any need to borrow over the forecast period. Investments are forecast to fall to below £6m as a result of maturing loans.

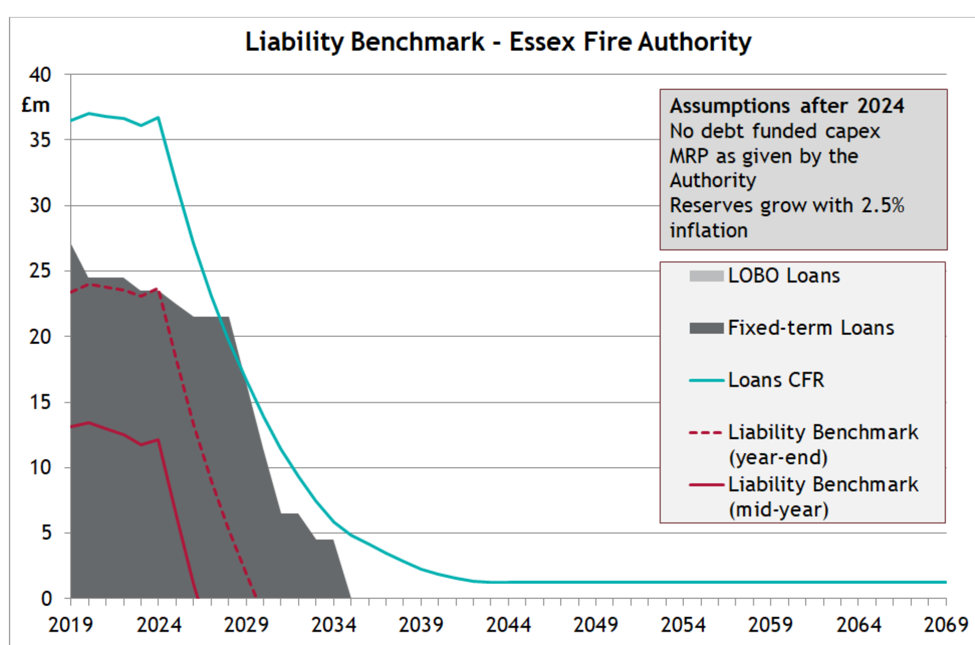
CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Authority expects to comply with this recommendation during 2019/20.

Liability benchmark: To compare the Authority's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table 1 above, but that cash and investment balances are kept to a minimum level of £5m at each year-end to maintain sufficient liquidity but minimise credit risk.

Table 2: Liability benchmark

	31.3.18 Actual £m	31.3.19 Estimate £m	31.3.20 Forecast £m	31.3.21 Forecast £m	31.3.22 Forecast £m
Loans CFR	37.9	36.5	37.0	36.8	36.6
Less: Usable reserves	-20.4	-21.9	-21.9	-21.9	-21.9
Plus: Working capital	3.1	3.9	3.9	3.9	3.9
Plus: Minimum investments	5.0	5.0	5.0	5.0	5.0
Liability Benchmark	**25.7**	**24.0**	**23.7**	**23.6**	**23.1**

Following on from the medium-term forecasts in table 2 above, the long-term liability benchmark assumes no capital expenditure funded by borrowing, minimum revenue provision on new capital expenditure spread over the asset life and income, expenditure and reserves all increasing by inflation of 2.5% a year. This is shown in the chart below:



Borrowing Strategy

The Authority currently holds £27 million of loans as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that the Authority does not expect to need to borrow in 2019/20 or the subsequent two years. The Authority may however borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £40 million.

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

Strategy: Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key

issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal/short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2019/20 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

In addition, the Authority may borrow short-term loans to cover unplanned cash flow shortages.

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

- Public Works Loan Board (PWLB) and any successor body
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds
- capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

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

- leasing
- hire purchase
- Private Finance Initiative
- sale and leaseback

The Authority has previously raised all of its long-term borrowing from the PWLB but it continues to investigate other sources of finance, such as local authority loans and bank loans that may be available at more favourable rates.

Municipal Bonds Agency: UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a joint and several guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to the Commissioner.

Short-term and variable rate loans: These loans leave the Authority exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below.

Debt rescheduling: The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Authority may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

Investment Strategy

The Authority holds modest levels of invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Authority's investment balance has ranged between £8 and £18 million; however, levels are expected to be fall in the forthcoming year and going forward.

Objectives: The CIPFA Code requires the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Authority will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

Negative interest rates: If the UK enters into a recession in 2019/20, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

Strategy: Given that investment balances are projected to fall and then remain low, the Authority aims to maintain an investment portfolio of high creditworthiness with a liquid maturity profile. All of the Authority's surplus cash is currently invested in money market funds.

Business models: Under the new IFRS 9 standard, the accounting for certain investments depends on the Authority's "business model" for managing them. The Authority aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

Approved counterparties: The Authority may invest its surplus funds with any of the counterparty types in table 3 below, subject to the cash limits (per counterparty) and the time limits shown.

Table 3: Approved investment counterparties and limits

Credit rating	Banks unsecured	Banks secured	Government	Corporates	Registered Providers
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£1m 5 years	£2m 20 years	£1m 50 years	£1m 20 years	£1m 20 years
AA+	£1m 5 years	£2m 10 years	£1m 25 years	£1m 10 years	£1m 10 years
AA	£1m 4 years	£2m 5 years	£1m 15 years	£1m 5 years	£1m 10 years
AA-	£1m 3 years	£2m 4 years	£1m 10 years	£1m 4 years	£1m 10 years
A+	£1m 2 years	£2m 3 years	£1m 5 years	£1m 3 years	£1m 5 years
A	£1m 13 months	£2m 2 years	£1m 5 years	£1m 2 years	£1m 5 years
A-	£1m 6 months	£2m 13 months	£1m 5 years	£1m 13 months	£1m 5 years
None	£1m 6 months	n/a	£1m 25 years	£1m 5 years	£1m 5 years
Pooled funds and real estate investment trusts		£2m per fund or trust			

This table must be read in conjunction with the notes below

Credit rating: Investment limits are set by reference to the lowest published long-term credit rating from a selection of external rating agencies. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

Banks unsecured Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

Banks secured: Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

Government: Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are

not zero risk. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.

Registered providers: Loans and bonds issued by, guaranteed by or secured on the assets of registered providers of social housing and registered social landlords, formerly known as housing associations. These bodies are tightly regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.

Pooled funds: Shares or units in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity and very low or no volatility will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.
Bond, equity and property funds offer enhanced returns over the longer term but are more volatile in the short term. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.

Real estate investment trusts: Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.

Operational bank accounts: The Authority may incur operational exposures, for example, though current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments but are still subject to the risk of a bank bail-in, and balances will therefore be kept below £1 million per bank. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Authority maintaining operational continuity.

Risk assessment and credit ratings: Credit ratings are obtained and monitored by the Authority's treasury staff, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be recalled or sold at no cost will be, and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review

is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Other information on the security of investments: The Authority understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis and advice from the Authority's treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.
When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority's cash balances, then the surplus will be deposited with the UK Government via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned but will protect the principal sum invested.

Investment limits: The Authority's revenue reserves available to cover investment losses are forecast to be £13.6 million on 31st March 2019. In order that no more than 15% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £2 million. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Table 4: Investment limits

	Cash limit
Any single organisation, except the UK Central Government	£2m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£2m per group
Any group of pooled funds under the same management	£2m per manager
Negotiable instruments held in a broker's nominee account	£4m per broker
Foreign countries	£2m per country
Registered providers and registered social landlords	£2m in total
Unsecured investments with building societies	£2m in total
Loans to unrated corporates	£2m in total
Money market funds of which 50% in UK domiciled MMFs	£10m in total
Real estate investment trusts	£2m in total

Liquidity management: The Authority uses Microsoft Excel spreadsheets for cash flow forecasting to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium-term financial plan and cash flow forecast.

Treasury Management Indicators

The Authority measures and manages its exposures to treasury management risks using the following indicators.

Security: The Authority has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating 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.

Credit risk indicator	Target
Portfolio average credit rating	A

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

Liquidity risk indicator	Target
Total cash available within 3 months	£8.5m

Interest rate exposures: This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

Interest rate risk indicator	Limit
Upper limit on one-year revenue impact of a 1% rise in interest rates	- £55,000
Upper limit on one-year revenue impact of a 1% fall in interest rates	£55,000

The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates.

Maturity structure of borrowing: This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	25%	0%
12 months and within 24 months	10%	0%
24 months and within 5 years	10%	0%
5 years and within 10 years	40%	0%
10 years and within 15 years	80%	0%
15 years and above	100%	0%

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

Principal sums invested for periods longer than a year: 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 on the long-term principal sum invested to final maturities beyond the period end will be:

Price risk indicator	2019/20	2020/21	2021/22
Limit on principal invested beyond year end	£5m	£3m	£2m

Related Matters

The CIPFA Code requires the Authority to include the following in its treasury management strategy.

Financial Derivatives: In the absence of any explicit legal power to do so, the Authority will not use standalone financial derivatives (such as swaps, forwards, futures and options). Derivatives embedded into loans and investments, including pooled funds and forward starting transactions, may be used, and the risks that they present will be managed in line with the overall treasury risk management strategy.

Markets in Financial Instruments Directive: The Authority has retained retail client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a smaller range of services but with the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

Financial Implications

The forecast for investment income in 2019/20 is £68k, based on an average investment portfolio of £8.5 million at an interest rate of 0.8%. The forecast for debt interest paid in 2019/20 is £1.3 million, based on an average debt portfolio of £27 million at an average interest rate of 4.7%. If actual levels of investments and borrowing, or actual interest rates, differ from those forecasts, performance against budget will be correspondingly different.

Other Options Considered

The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer, having consulted the Commissioner, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

Appendix A – Arlingclose Economic & Interest Rate Forecast May 2019
Underlying assumptions:

- The global economy is entering a period of slower growth in response to political issues, primarily the trade policy stance of the US.

- There appears no near-term resolution to the trade dispute between China and the US. The US has also targeted other countries. With the 2020 presidential election a year away, Donald Trump is unlikely to want to display perceived weakness in trade negotiations to his supporters.

- The resignation of Theresa May has created greater uncertainty with regard to Brexit. Boris Johnson is the new Prime Minister and favours exiting the EU on 31st October. It is unlikely the UK will be able to negotiate a different withdrawal deal before the deadline. We remain of the belief that policymakers are unlikely to raise Bank Rate unless there is some certainty to the withdrawal arrangement.

- While the potential for divergent paths for UK monetary policy remain in the event of a withdrawal agreement, the weakening external environment severely limits the potential upside for movement in Bank Rate.

- UK economic growth is slowing after a relatively strong Q1 2019. Q2 growth is likely to be sluggish, with the ONS already reporting a monthly contraction in GDP for April and PMI data signalling broadly stagnant business conditions. The MPC has downgraded its growth forecast for 2019.

- Inflation remains around target. The tight labour market risks medium-term domestically driven inflationary pressure. Slower global growth should reduce the prospect of externally driven inflationary pressure, although political turmoil could push up oil prices.

- Central bank actions and geopolitical risks will continue to produce significant volatility in financial markets, including bond markets.

Forecast:

- We have altered our central forecasts in response to the external and political risks facing the UK economy.

- Bank Rate is expected to remain at 0.75% for the foreseeable future. There are substantial risks to both sides of this forecast, dependant on Brexit outcomes and the evolution of the global economy.

- Gilt yields have fallen to recent lows. Resolution of global political uncertainty would see yields rise but volatility arising from both economic and political events will continue to offer longer-term borrowing opportunities.

	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Average
Official Bank Rate														
Upside risk	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	**0.27**
Arlingclose Central Case	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**
Downside risk	0.00	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.46**
3-month money market ra														
Upside risk	0.10	0.10	0.25	0.25	0.25	0.25	0.25	0.25	0.30	0.35	0.50	0.55	0.55	**0.30**
Arlingclose Central Case	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**	**0.80**
Downside risk	-0.10	-0.50	-0.55	-0.55	-0.55	-0.55	-0.55	-0.55	-0.55	-0.55	-0.55	-0.55	-0.55	**-0.51**
1yr money market rate														
Upside risk	0.10	0.20	0.20	0.20	0.20	0.20	0.20	0.25	0.30	0.35	0.40	0.50	0.50	**0.28**
Arlingclose Central Case	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**	**0.95**
Downside risk	-0.30	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.48**
5yr gilt yield														
Upside risk	0.20	0.20	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.45	0.50	0.50	0.50	**0.37**
Arlingclose Central Case	**0.60**	**0.60**	**0.65**	**0.70**	**0.70**	**0.70**	**0.70**	**0.75**	**0.75**	**0.80**	**0.80**	**0.80**	**0.80**	**0.72**
Downside risk	-0.30	-0.30	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	**-0.34**
10yr gilt yield														
Upside risk	0.20	0.20	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.45	0.50	0.50	0.50	**0.37**
Arlingclose Central Case	**0.85**	**0.90**	**0.95**	**1.00**	**1.00**	**1.00**	**1.00**	**1.05**	**1.10**	**1.15**	**1.20**	**1.20**	**1.20**	**1.05**
Downside risk	-0.30	-0.30	-0.35	-0.35	-0.35	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	**-0.37**
20yr gilt yield														
Upside risk	0.20	0.20	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.45	0.50	0.50	0.50	**0.37**
Arlingclose Central Case	**1.40**	**1.40**	**1.40**	**1.45**	**1.45**	**1.50**	**1.50**	**1.50**	**1.50**	**1.50**	**1.50**	**1.50**	**1.50**	**1.47**
Downside risk	-0.30	-0.30	-0.35	-0.35	-0.35	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	**-0.37**
50yr gilt yield														
Upside risk	0.20	0.20	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.45	0.50	0.50	0.50	**0.37**
Arlingclose Central Case	**1.35**	**1.35**	**1.35**	**1.35**	**1.35**	**1.40**	**1.40**	**1.45**	**1.45**	**1.45**	**1.45**	**1.45**	**1.45**	**1.40**
Downside risk	-0.30	-0.30	-0.35	-0.35	-0.35	-0.35	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	**-0.37**

PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%

PWLB Infrastructure Rate (Maturity Loans) = Gilt yield + 0.60%

Appendix B – Existing Investment & Debt Portfolio Position

	31/03/2019 **Actual Portfolio £m**	31/03/2019 **Average Rate %**
External borrowing:		
Public Works Loan Board	27.0	4.7
Total external borrowing	**27.0**	**4.7**
Total other long-term liabilities	**0.0**	**0.0**
Total gross external debt	**27.0**	**4.7**
Treasury investments:		
Money Market Funds	8.5	0.8
Total treasury investments	**8.5**	**0.8**
Net debt	**18.5**	**3.9**

Appendix C – Balance sheet analysis at 31st March 2019 per unaudited Accounts 31st July 2019

Balance Sheet Analysis 31st March 2019	Balance 31/03/2019	Capital Financing Requirement (CFR)	Useable Reserves	Working Capital	Investments	External Borrowing	Balance 31/03/2019
	£000	£000	£000	£000	£000	£000	£000
Property, Plant & Equipment							
Land and Buildings	105,425	105,425					105,425
Vehicles, plant and equipment	12,872	12,872					12,872
Fixed assets under construction	711	711					711
Surplus Assets	-	-					0
Long Term Investments	94				94		94
Long Term Assets	**119,102**	**119,008**	**0**	**0**	**94**	**0**	**119,102**
Inventories	432			432			432
Short Term Debtors	9,672			9,672			9,672
Cash and Cash Equivalents	11,682			3,182	8,500		11,682
Current Assets	**21,786**	**0**	**0**	**13,286**	**8,500**	**0**	**21,786**
Short Term Borrowing	(2,499)			0		(2,499)	(2,499)
Short Term Creditors	(6,194)			(6,194)			(6,194)
Grants Receipts in advance	(2,029)			(2,029)			(2,029)
Current Liabilities	**(10,722)**	**0**	**0**	**(8,223)**	**0**	**(2,499)**	**(10,722)**
Long Term Borrowing	(24,500)			0		(24,500)	(24,500)
Provisions	(850)			(850)			(850)
Other Long Term Liabilities	(799,437)			(799,437)			(799,437)
Long Term Liabilities	**(824,787)**	**0**	**0**	**(800,287)**	**0**	**(24,500)**	**(824,787)**
Net Liabilities	**(694,621)**	**119,008**	**0**	**(795,224)**	**8,594**	**(26,999)**	**(694,621)**
Usable Reserves							
General Fund	7,935		7,935				7,935
Earmarked General Fund Reserves	5,653		5,653				5,653
Useable Capital Receipts Reserve	8,335		8,335				8,335
Usable reserves	**21,923**	**0**	**21,923**	**0**	**0**	**0**	**21,923**
Revaluation Reserve	21,726	21,726					21,726
Capital Adjustment Account	60,807	60,807					60,807
Holiday Pay Account	(838)			(838)			(838)
Collection Fund Adjustment Account	1,198			1,198			1,198
Pension Reserve	(799,437)			(799,437)			(799,437)
Unusable Reserves	**(716,544)**	**82,533**	**0**	**(799,077)**	**0**	**0**	**(716,544)**
Total Reserves	**(694,621)**	**82,533**	**21,923**	**(799,077)**	**0**	**0**	**(694,621)**
Analysis Totals	**0**	**36,475**	**(21,923)**	**3,853**	**8,594**	**(26,999)**	**0**