# Audit and Governance Committee

**Meeting: Monday, 7th March 2022 at 6.30 pm in Civic Suite, North Warehouse, The Docks, Gloucester, GL1 2EP**

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| **Membership:** | Cllrs. Wilson (Chair), Brooker (Vice-Chair), Bowkett, Patel, Durdey, Evans, Melvin and Pullen |
| **Contact:** | Democratic and Electoral Services<br>01452 396126<br>democratic.services@gloucester.gov.uk |

# AGENDA

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| **1.** | **APOLOGIES**<br><br>To receive any apologies for absence. |
| **2.** | **DECLARATIONS OF INTEREST**<br><br>To receive from Members, declarations of the existence of any disclosable pecuniary, or non-pecuniary, interests and the nature of those interests in relation to any agenda item. Please see Agenda Notes. |
| **3.** | **MINUTES** (Pages 7 - 12)<br><br>To approve as a correct record the minutes of the meeting held on 17 January 2022 |
| **4.** | **PUBLIC QUESTION TIME (15 MINUTES)**<br><br>The opportunity is given to members of the public to put questions to Cabinet Members or Committee Chairs provided that a question does not relate to:<br><br>• Matters which are the subject of current or pending legal proceedings or<br>• Matters relating to employees or former employees of the Council or comments in respect of individual Council Officers.<br><br>To ask a question at this meeting, please submit it to democratic.services@gloucester.gov.uk by 12pm on Wednesday 2 March 2022 or telephone 01452 396203 for support. |
| **5.** | **PETITIONS AND DEPUTATIONS (15 MINUTES)**<br><br>A period not exceeding three minutes is allowed for the presentation of a petition or deputation provided that no such petition or deputation is in relation to:<br><br>• Matters relating to individual Council Officers, or<br>• Matters relating to current or pending legal proceedings<br><br>To present a petition or deputation at this meeting, please submit it to democratic.services@gloucester.gov.uk by 12pm on Wednesday 2 March or telephone |

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| | 01452 396203 for support. |
| **6.** | **INTERNAL AUDIT ACTIVITY PROGRESS REPORT** (Pages 13 - 26)<br><br>To consider the report of the Head of Audit, Risk and Assurance in respect of progress made against the audit plan. |
| **7.** | **INTERNAL AUDIT PLAN 2022-23** (Pages 27 - 36)<br><br>To consider the proposed Internal Audit Plan for 2022-23. |
| **8.** | **TREASURY MANAGEMENT STRATEGY 2022/23** (Pages 37 - 76)<br><br>To consider the report of the Cabinet Member for Performance and Resources regarding the strategy for the next financial year. |
| **9.** | **CAPITAL STRATEGY 2022/23** (Pages 77 - 88)<br><br>To consider the report of the Cabinet Member for Performance and Resources regarding the capital strategy for the next financial year and to recommend its approval to Council. |
| **10.** | **EXCLUSION OF THE PRESS AND PUBLIC**<br><br>To **RESOLVE** that:<br><br>The press and public be excluded from the meeting during the following item of business on the grounds that it is likely, in view of the nature of business to be transacted or the nature of the proceedings, that if members of the press and public are present during consideration of this item there will be disclosure to them of exempt information as defined in Schedule 12A of the Local Government Act 1972 as amended.<br><br>Agenda Item No.<br><br>9 and 10<br><br>**Description of Exempt Information:**<br><br>Paragraph 3: Information relating to the financial or business affairs of any particular person (including the authority holding that information). |
| **11.** | **IT SYSTEMS UPDATE**<br><br>To receive an update from the Director of Policy and Resources. |
| **12.** | **EXEMPT MINUTES - 17 JANUARY 2022** (Pages 89 - 94)<br><br>To approve as a correct record the exempt minutes from the meeting held on 17 January 2022. |
| **13.** | **AUDIT AND GOVERNANCE COMMITTEE WORK PROGRAMME** (Pages 95 - 96)<br><br>To consider the work programme. |
| **14.** | **DATE OF NEXT MEETING**<br><br>18 July at 6.30pm, in the Civic Suite, North Warehouse |

**Jon McGinty**
**Managing Director**

**Date of Publication: Friday, 25 February 2022**

## NOTES

**Disclosable Pecuniary Interests**
The duties to register, disclose and not to participate in respect of any matter in which a member has a Disclosable Pecuniary Interest are set out in Chapter 7 of the Localism Act 2011.

Disclosable pecuniary interests are defined in the Relevant Authorities (Disclosable Pecuniary Interests) Regulations 2012 as follows –

| <u>Interest</u> | <u>Prescribed description</u> |
|---|---|
| Employment, office, trade, profession or vocation | Any employment, office, trade, profession or vocation carried on for profit or gain. |
| Sponsorship | Any payment or provision of any other financial benefit (other than from the Council) made or provided within the previous 12 months (up to and including the date of notification of the interest) in respect of any expenses incurred by you carrying out duties as a member, or towards your election expenses. This includes any payment or financial benefit from a trade union within the meaning of the Trade Union and Labour Relations (Consolidation) Act 1992. |
| Contracts | Any contract which is made between you, your spouse or civil partner or person with whom you are living as a spouse or civil partner (or a body in which you or they have a beneficial interest) and the Council<br>(a) under which goods or services are to be provided or works are to be executed; and<br>(b) which has not been fully discharged |
| Land | Any beneficial interest in land which is within the Council's area.<br><br>For this purpose "land" includes an easement, servitude, interest or right in or over land which does not carry with it a right for you, your spouse, civil partner or person with whom you are living as a spouse or civil partner (alone or jointly with another) to occupy the land or to receive income. |
| Licences | Any licence (alone or jointly with others) to occupy land in the Council's area for a month or longer. |
| Corporate tenancies | Any tenancy where (to your knowledge) –<br><br>(a) the landlord is the Council; and<br>(b) the tenant is a body in which you, your spouse or civil partner or a person you are living with as a spouse or civil partner has a beneficial interest |
| Securities | Any beneficial interest in securities of a body where –<br><br>(a) that body (to your knowledge) has a place of business or land in the Council's area and<br>(b) either –<br>i. The total nominal value of the securities exceeds £25,000 or one hundredth of the total issued share capital of that body; or<br>ii. If the share capital of that body is of more than one class, the total nominal value of the shares of any one class in which you, your spouse or civil partner or person with |

whom you are living as a spouse or civil partner has a beneficial interest exceeds one hundredth of the total issued share capital of that class.

For this purpose, "securities" means shares, debentures, debenture stock, loan stock, bonds, units of a collective investment scheme within the meaning of the Financial Services and Markets Act 2000 and other securities of any description, other than money deposited with a building society.

NOTE: the requirements in respect of the registration and disclosure of Disclosable Pecuniary Interests and withdrawing from participating in respect of any matter where you have a Disclosable Pecuniary Interest apply to your interests and those of your spouse or civil partner or person with whom you are living as a spouse or civil partner where you are aware of their interest.

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For enquiries about Gloucester City Council's meetings please contact Democratic Services, 01452 396126, democratic.services@gloucester.gov.uk.

If you, or someone you know cannot understand English and need help with this information, or if you would like a large print, Braille, or audio version of this information please call 01452 396396.

**Recording of meetings**

Please be aware that meetings may be recorded. There is no requirement for those wishing to record proceedings to notify the Council in advance; however, as a courtesy, anyone wishing to do so is advised to make the Chair aware before the meeting starts.

Any recording must take place in such a way as to ensure that the view of Councillors, Officers, the Public and Press is not obstructed. The use of flash photography and/or additional lighting will not be allowed unless this has been discussed and agreed in advance of the meeting.

**FIRE / EMERGENCY EVACUATION PROCEDURE**

If the fire alarm sounds continuously, or if you are instructed to do so, you must leave the building by the nearest available exit. You will be directed to the nearest exit by council staff. It is vital that you follow their instructions:

- You should proceed calmly; do not run and do not use the lifts;
- Do not stop to collect personal belongings;
- Once you are outside, please do not wait immediately next to the building; gather at the assembly point in the car park and await further instructions;
- Do not re-enter the building until told by a member of staff or the fire brigade that it is safe to do so.

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# AUDIT AND GOVERNANCE COMMITTEE

**MEETING** : Monday, 17th January 2022

**PRESENT** : Cllrs. Wilson (Chair), Brooker (Vice-Chair), Bowkett, Patel, Durdey, Evans, Melvin and Pullen

**Others in Attendance**

Director of Policy and Resources
Head of Audit, Risk and Assurance (ARA)
Financial Services Manager
ARA Principal Internal Auditor
Democratic and Electoral Services Officer

**Also in attendance**
Councillor Norman

**APOLOGIES** : Cllrs.

## 32. DECLARATIONS OF INTEREST

There were no declarations of interest.

## 33. MINUTES

In response to a query from the Chair regarding the new format for audit reports, the Head of Audit, Risk and Assurance (ARA) confirmed that new processes had commenced, that summaries will be provided as a matter of course unless requested otherwise and that there would be a period of transition while the new processes were implemented.

It was further confirmed, with reference to the possibility that a 'kickstarter' apprentice be employed to examine smaller VAT claims that this scheme would be looked into.

**RESOLVED** – That the minutes of the meeting held on Monday 15 November 2021 were approved and signed as a correct record by the Chair.

## 34. PUBLIC QUESTION TIME (15 MINUTES)

There were no public questions.

## 35. PETITIONS AND DEPUTATIONS (15 MINUTES)

There were no petitions nor deputations.

## 36. GRANTS AUDIT REPORT

The Director of Policy and Resources informed Members that a draft had been received that day and that the final report was pending. He confirmed that it to the form of a housing benefit audit and that, were there to be any adjustments, this could affect any subsidy received.

**RESOLVED** that: - The Audit and Governance Committee **NOTE** the update.

## 37. APPOINTMENT OF EXTERNAL AUDITOR

37.1 The Director of Policy and Resources outlined the report regarding procuring the external auditor to take effect as of 2023/24 and that the appointment was required by 31 December 2022. He stated that it needed to be made clear that the Council would opt into the public sector procurement process. The Director also advised that alternative courses were not likely to be as efficient.

37.2 The Chair agreed that opting into the procurement process was a sensible course of action and noted that the final decision would be taken at the next Council meeting.

**RESOLVED** that: - the **Audit and Governance Committee** endorse and **RECOMMEND** to Council the option to opt-in to the Public Sector Audit Appointments Ltd (PSAA) for the appointment of the Council’s External Auditors from 2023/24.

## 38. APPOINTMENT OF INDEPENDENT MEMBER

The Director of Policy and Resources informed Members that the recruitment of an independent Member would be progressed so they were in place for the next municipal year. In response to a question from Councillor Pullen as to why there would be an independent Member, the Head of ARA clarified that it had been recommended that all audit committees have an independent Member and that it was likely that this would become mandatory in the future.

**RESOLVED** that: - The Audit and Governance Committee **NOTE** the update.

## 39. INTERNAL AUDIT ACTIVITY PROGRESS REPORT

39.1 The Head of ARA provided an overview of internal audit activity and advised that ongoing work had been temporarily suspended due to IT issues. Of audits where assurance was sought, three had been completed – Accounts receivable, Disabled Facilities Grants (DFGs) and the certification of 2021 election accounts. The Principal Auditor also advised that anti-fraud work had been continuing. Eight cases had been identified and of these, four had been closed.

39.2 In response to a query from the Chair regarding accounts receivable, the Principal Auditor confirmed that this was in respect of goods and services and not the collection of council tax. With regard to DFGs, the Principal Auditor further confirmed that the audit was to ensure figures provided were accurate.

39.3 Councillor Pullen asked, in relation to the election accounts, whether the Returning Officer received three fees, there having been three elections. The Principal Auditor confirmed that there was one fee but made up of three distinct claims. In respect of a special fraud investigation, the Principal Auditor stated that full details would be provided to the Committee.

39.4 The Chair noted that there were five active audits which would need to be carried forward. The Principal Auditor advised that these would be examined on a case by case basis and that some were close to completion.

**RESOLVED** that: - The Audit and Governance Committee

(1) Accept the progress against the Internal Audit Plan 2021/22; and

(2) Accept the assurance opinions provided in relation to the effectiveness of the Council's control environment (comprising risk management, control and governance arrangements).

## 40. STRATEGIC RISK REGISTER UPDATE

40.1 The Head of ARA presented the report and outlined the purpose of the risk register. He advised that a review of risk management was being undertaken and, where appropriate, areas would be enhanced.

40.2 Councillor Pullen noted that the Council's target was to be carbon neutral by 2030 and that the City be carbon neutral by 2045. Whilst this was referred to in the report, he queried why it did not appear explicitly in the risk register. The Director of Policy and Resources explained that, as it was a key policy area the Council was working towards, it was not necessary to include as a risk on its own. The suggestion from Councillor Norman that it be included in the description of risk 1.13 (regarding the Council Plan) was agreed by the committee.

**RESOLVED that**: - The Audit and Governance Committee **NOTE** and **ENDORSE** the strategic risk register.

## 41. ANNUAL GOVERNANCE STATEMENT IMPROVEMENT PLAN 2021/22 UPDATE

The committee considered the update. The Chair noted that the Climate Change Strategy and Property investments were due to be reviewed and sought clarity on whether these could be completed within the timescale. The Principal Auditor advised that he would examine whether this was possible and that they may be carried forward. The Director of Policy and Resources stated the property investment had been considered by the Overview and Scrutiny Committee at a recent meeting.

**RESOLVED that**: - The Audit and Governance Committee **NOTE** the report.

## 42. EXCLUSION OF THE PRESS AND PUBLIC

**RESOLVED** that:

The press and public be excluded from the meeting during the following item of business on the grounds that it is likely, in view of the nature of business to be transacted or the nature of the proceedings, that if members of the press and public are present during consideration of this item there will be disclosure to them of exempt information as defined in Schedule 12A (para. 3) of the Local Government Act 1972 as amended.

## 43. IT SYSTEMS UPDATE

**RESOLVED**: - As per the exempt minutes.

## 44. AUDIT AND GOVERNANCE COMMITTEE WORK PROGRAMME

**RESOLVED that**: - The Audit and Governance Committee **NOTE** the work programme.

## 45. DATE OF NEXT MEETING

7 March 2022 at 6.30pm in the Civic Suite, North Warehouse

**Time of commencement: 6.30 pm hours**
**Time of conclusion: 7.20 pm hours**

**Chair**

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Gloucester City Council

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| **Meeting:** | **Audit and Governance Committee Date: 7th March 2022** |
| **Subject:** | **Internal Audit Activity Progress Report 2021/22** |
| **Report Of:** | **Head of Audit Risk Assurance (ARA)** |
| **Wards Affected:** | **Not applicable** |
| **Key Decision:** | **No Budget/Policy Framework: No** |
| **Contact Officer:** | **Piyush Fatania, Head of ARA** |
| | **Email: [piyush.fatania@gloucestershire.gov.uk](mailto:piyush.fatania@gloucestershire.gov.uk) Tel: 01452 328883** |
| **Appendices:** | **A: Internal Audit Activity Progress Report 2021/22** |

**FOR GENERAL RELEASE**

## 1.0 Purpose of Report

1.1 To inform Members of the Internal Audit activity progress in relation to the approved Internal Audit Plan 2021/22.

## 2.0 Recommendations

2.1 Audit and Governance Committee is asked to **RESOLVE** to:

(1) Accept the progress against the Internal Audit Plan 2021/22; and

(2) Accept the assurance opinions provided in relation to the effectiveness of the Council's control environment (comprising risk management, control and governance arrangements).

## 3.0 Background and Key Issues

3.1 Members approved the Internal Audit Plan 2021/22 at the 8th March 2021 Audit and Governance Committee meeting. In accordance with the Public Sector Internal Audit Standards 2017 (PSIAS), this report (through **Appendix A**) details the outcomes of Internal Audit work carried out in accordance with the approved Plan.

3.2 The Internal Audit Activity Progress Report 2021/22 at **Appendix A** summarises:

- The progress against the 2021/22 Internal Audit Plan, including the assurance opinions on the effectiveness of risk management and control processes;
- The continued ARA engagement with senior management regards the Council's ICT risk position and the impact on Audit Plan activities; and
- Special investigations/counter fraud activity.

3.3 The report is the fourth progress report in relation to the Internal Audit Plan 2021/22.

## 4.0 Social Value Considerations

4.1 There are no Social Value implications as a result of the recommendations made in this report.

## 5.0 Environmental Implications

5.1 There are no Environmental implications as a result of the recommendations made in this report.

## 6.0 Alternative Options Considered

6.1 No other options have been considered. The purpose of this report is to inform the Committee of the Internal Audit work undertaken to date and the assurance opinions provided. Non-completion of Internal Audit Activity Progress Reports would lead to non-compliance with the PSIAS and the Council Constitution (see report section 7.2 and 7.3).

## 7.0 Reasons for Recommendations

7.1 The role of the ARA Shared Service is to examine, evaluate and provide an independent, objective opinion on the adequacy and effectiveness of the Council's internal control environment, comprising risk management, control and governance. Where weaknesses have been identified, recommendations have been made to improve the control environment.

7.2 The PSIAS state the Head of ARA should report on the outcomes of Internal Audit work, in sufficient detail, to allow the Committee to understand what assurance it can take from that work and what unresolved risks or issues it needs to address.

7.3 Consideration of reports from the Head of ARA on Internal Audit's work and performance during the year is also a requirement of the Audit and Governance Committee's terms of reference (part of the Council Constitution).

## 8.0 Future Work and Conclusions

8.1 In accordance with the PSIAS and as reflected within the Audit and Governance Committee work programme, the Annual Report on Internal Audit Activity against the approved Internal Audit Plan 2021/22 is scheduled to be presented at the 18th July 2022 Audit and Governance Committee meeting.

## 9.0 Financial Implications

9.1 There are no Financial implications as a result of the recommendations made in this report.

Financial Services have been consulted in the preparation this report.

## 10.0 Legal Implications

10.1 Monitoring the implementation of Internal Audit recommendations assists the Council to minimise risk areas and thereby reduce the prospects of legal challenge.

One Legal have been consulted in the preparation this report.

## 11.0 Risk and Opportunity Management Implications

11.1 Failure to deliver an effective Internal Audit service will prevent an independent, objective assurance opinion from being provided to those charged with governance that the key risks associated with the achievement of the Council's objectives are being adequately controlled.

## 12.0 People Impact Assessment (PIA) and Safeguarding:

12.1 The Internal Audit service is delivered by ARA which is an Internal Audit and Risk Management Shared Service between Gloucester City Council, Stroud District Council and Gloucestershire County Council. Equality in service delivery is demonstrated by the team being subject to, and complying with, the Council's equality policies.

12.2 The PIA Screening Stage was completed and did not identify any potential or actual negative impact, therefore a full PIA was not required.

## 13.0 Community Safety Implications

13.1 There are no Community Safety implications as a result of the recommendations made in this report.

## 14.0 Staffing and Trade Union Implications

14.1 There are no Staffing and Trade Union implications as a result of the recommendations made in this report.

**Background Documents:** Internal Audit Plan 2021/22
PSIAS
CIPFA Local Government Application Note for the UK PSIAS

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# Internal Audit Activity Progress Report

2021-2022

ARA
AuditRiskAssurance

Gloucester City Council
Transforming Your City

## (1) Introduction

All Councils must make proper provision for Internal Audit in line with the 1972 Local Government Act (S151) and the Accounts and Audit Regulations 2015. The latter states that a relevant Council ‘must undertake an effective Internal Audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance’.

The Council’s Internal Audit service is provided by Audit Risk Assurance (ARA) under a Shared Service agreement between Gloucester City Council, Stroud District Council and Gloucestershire County Council. ARA carries out the work required to satisfy this legislative requirement and reports its findings and conclusions to management and to this Committee.

The guidance accompanying the Regulations recognises the Public Sector Internal Audit Standards 2017 (PSIAS) as representing ‘proper Internal Audit practices’. The standards define the way in which the Internal Audit service should be established and undertake its operations.

## (2) Responsibilities

Management are responsible for establishing and maintaining appropriate risk management processes, control systems (financial and non financial) and governance arrangements.

Internal Audit plays a key role in providing independent assurance and advising the Council that these arrangements are in place and operating effectively.

Internal Audit is not the only source of assurance for the Council. There are a range of external audit and inspection agencies as well as management processes which also provide assurance. These are set out in the Council’s Code of Corporate Governance and Annual Governance Statement.

## (3) Purpose of this Report

One of the key requirements of the PSIAS is that the Head of ARA should provide progress reports on Internal Audit activity to those charged with governance. This report summarises:

i. The progress against the 2021/22 Risk Based Internal Audit Plan, including the assurance opinions on the effectiveness of risk management and control processes;

ii. The continued ARA engagement with senior management regards the Council’s ICT risk position and the impact on Audit Plan activities; and

iii. Special investigations/counter fraud activity.

Due to the Council’s current ICT position and the impact on service delivery, there are no new Internal Audit assurance outcomes to report from 2021/22 Internal Audit activity delivered in January 2022.

### (4) Progress against the 2021/22 Internal Audit Plan, including the assurance opinions on risk and control

The schedule provided at **Attachment 1** provides the summary of 2021/22 activities which have not previously been reported to the Audit and Governance Committee.

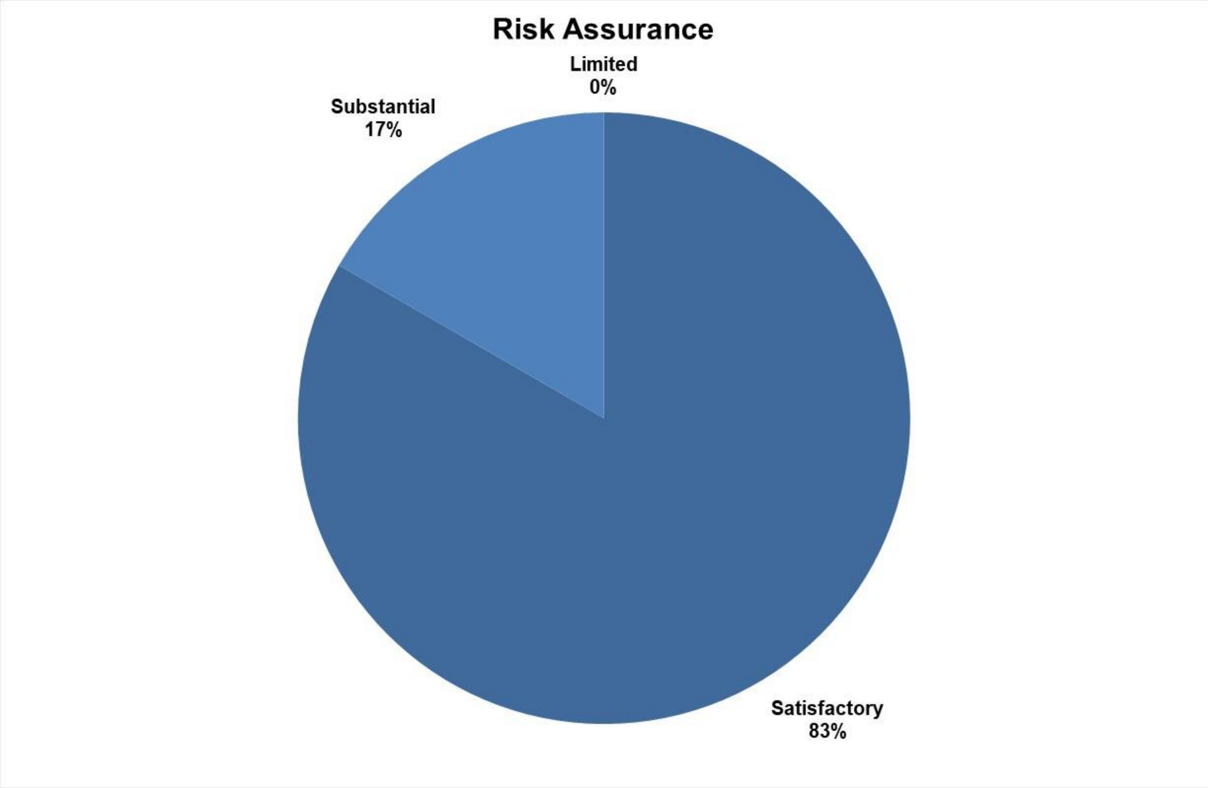
The schedule provided at **Attachment 2** contains a list of the 2021/22 Internal Audit Plan activity undertaken during the financial year to date. This includes, where relevant, the assurance opinions on the effectiveness of risk management arrangements and control processes in place to manage those risks and the dates where a summary of the activity outcomes have been presented to the Audit and Governance Committee.

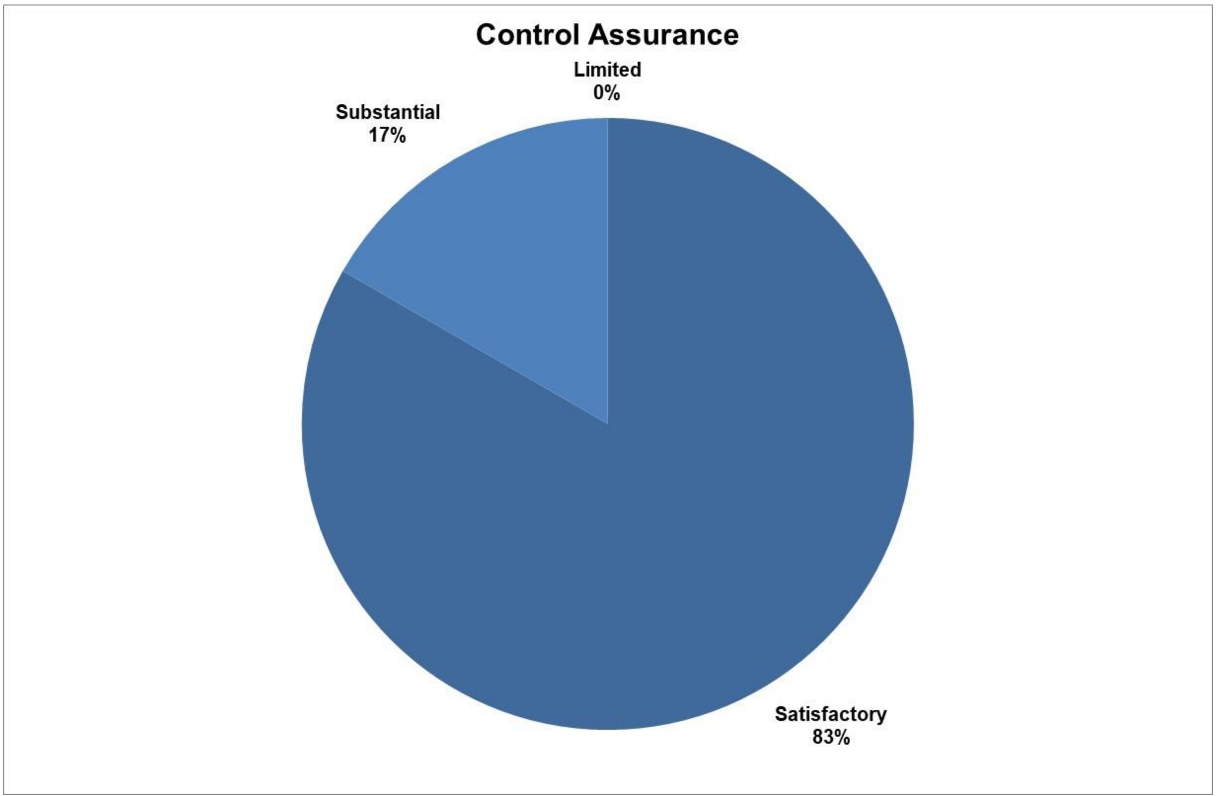
Explanations of the meaning of the assurance opinions are shown below.

| Assurance Levels | Risk Identification Maturity | Control Environment |
|---|---|---|
| **Substantial** | **Risk Managed**<br>Service area fully aware of the risks relating to the area under review and the impact that these may have on service delivery, other service areas, finance, reputation, legal, the environment, customers, partners, and staff. All key risks are accurately reported and monitored in line with the Council's Risk Management Strategy. | • System Adequacy – Robust framework of controls ensures that there is a high likelihood of objectives being achieved.<br>• Control Application – Controls are applied continuously or with minor lapses. |
| **Satisfactory** | **Risk Aware**<br>Service area has an awareness of the risks relating to the area under review and the impact that these may have on service delivery, other service areas, finance, reputation, legal, the environment, customers, partners, and staff. However, some key risks are not being accurately reported and monitored in line with the Council's Risk Management Strategy. | • System Adequacy – Sufficient framework of key controls for objectives to be achieved but, control framework could be stronger.<br>• Control Application – Controls are applied but with some lapses. |
| **Limited** | **Risk Naïve**<br>Due to an absence of accurate and regular reporting and monitoring of the key risks in line with the Council's Risk Management Strategy, the service area has not demonstrated a satisfactory awareness of the risks relating to the area under review and the impact that these may have on service delivery, other service areas, finance, reputation, legal, the environment, customers, partners, and staff. | • System Adequacy – Risk of objectives not being achieved due to the absence of key internal controls.<br>• Control Application – Significant breakdown in the application of control. |

## (4a) Summary of Internal Audit Assurance Opinions on Risk and Control

The below pie charts show the summary of the risk and control assurance opinions provided in relation to the 2021/22 audit activity undertaken up to January 2022. The pie chart content remains consistent with the 17th January 2022 Audit and Governance Committee report.



### (4b) Continued ARA engagement with senior management regards the Council's ICT risk position and the impact on Audit Plan activities

Following a cyber incident in December 2021, the Council have experienced some disruption to service delivery. Joint investigation of the situation (by the Council and independent parties) is underway.

Due to the above position and with agreement from Council senior management, Internal Audit activity delivery was temporarily suspended in January 2022.

During this time, ARA has continuously engaged with senior management regarding the ICT incident position and the impact on the Council services. This action has been taken by ARA to ensure that:

i. We maintain an up to date understanding of ICT and operational risks;

ii. Management of 2021/22 Internal Audit activity is progressed to enable delivery in appropriate areas only; and

iii. ARA are accessible to management and can support any required Council activities (from an assurance, Counter Fraud Team (CFT) or resource perspective) following the ICT incident. Examples of this type of activity include: CFT support on National Fraud Initiative (NFI) uploads; and ARA team member input into process and internal control discussions, to enable service provision continuity for an interim period where a base ICT system has not been accessible.

The ICT incident has caused a number of 2021/22 Internal Audit activities to be deferred. These activities will be considered for inclusion within the draft Risk Based Internal Audit Plan 2022/23. The draft Plan is due to be presented to the 7th March 2022 Audit and Governance Committee for consideration and approval.

**Attachment 1**

## Completed 2021/22 Internal Audit Activity during the period January 2022

### Summary of Internal Audit Opinions on Control

There are no new Internal Audit assurance outcomes to report from 2021/22 Internal Audit activity delivered in January 2022.

### Summary of Special Investigations/Counter Fraud Activities

**Current Status**

To date in 2021/22 there have been nine new potential irregularities referred to the ARA Counter Fraud Team (CFT). Five of the nine cases have been closed. Four of these have been reported the Audit and Governance Committee previously.

The latest referral related to concerns that an individual was undertaking a second paid job with the Council (whilst on sick leave) with a different employer. The CFT investigation found no evidence to support the allegation and the case has been closed.

The outcomes of the remaining four cases will be reported to the Audit and Governance Committee on their conclusion.

There is one non-grant related case that remains open from prior year and is still ongoing. The Council is currently liaising with One Legal to progress the case further and an independent Barrister has been appointed. The case has been provisionally listed at Cheltenham Magistrate Court.

In addition, the ARA CFT in conjunction with the Intelligent Client Officer (Revenues and Benefits) have continued to work on two cases carried forward from last year in respect of Covid-19 Government issued small business grant payments. One of these cases was previously closed, but then had to be reopened due to revised Government guidance. Advice has been sought from One Legal on this case due to potential complications. The subject of this case has now begun to repay the grant however, due to the Council's current ICT position a repayment schedule has not yet been agreed with the individual and therefore the case remains open.

It should be noted that the Council's current ICT position has impacted on the progression of the above cases.

Many potential attempted frauds are intercepted. This is due to a combination of local knowledge and the credible national communications including those from the National Anti-Fraud Network (NAFN) being swiftly cascaded to teams where more national targeted frauds are shared for the purpose of prevention.

**Covid-19 Omicron Business Grant Fraud update**

As reported by NAFN in January 2022, the updated value of Covid-19 Business Grant fraud prevented from a total of 206 Councils in England, Scotland and Wales is:


The CFT continues to provide support and guidance to Council staff in respect of Interviews Under Caution, court file preparation and taking witness statements where required.

**National Fraud Initiative (NFI)**

Internal Audit continues to support the NFI which is a biennial data matching exercise administered by the Cabinet Office. The data collections for the 2021/22 exercise have been uploaded to the Cabinet Office. The data matching reports were released at the end of January 2021.

The full NFI timetable can be found using the link available on GOV.UK – https://www.gov.uk/government/publications/national-fraud-initiative-timetables.

Examples of data sets include housing, insurance, payroll, creditors, council tax, electoral register and licences for market trader/operator, taxi drivers and personal licences to supply alcohol.

Not all matches are always investigated, but where possible all recommended matches are reviewed by either ARA or the appropriate service area within the Council.

To date and for this NFI cycle, the review of the matches has identified errors leading to the recovery of £39,904 together with the identification of further savings of £2,322 due to delays in updating notifications of Benefits changes in circumstances. This makes a total saving of £42,226 (of which £31,883 is Small Business Grant Fund related).

The Council's current ICT position has impeded the Council's ability to review the NFI matches. The NFI and Cabinet Office have been advised of the situation and have taken the interim action to suppress access to all Gloucester City Council matches by users with a Gloucester City email address.

As a result of the frauds associated with the various Covid-19 grants, a number of new matches have been released and new matching services introduced. These include identifying bank accounts that have been used for multiple claims and cross matching claimants with other Councils.

The CFT continues to work with the Council’s Intelligent Client Officer (Revenues and Benefits) where it is identified that further investigation is required.

In addition, the CFT has been working with the Revenues and Benefits team to upload the Covid-19 Business Grant applications. Applications are uploaded by the individual business and the bank details are then cross checked against the business name by NFI. This mitigates the risk of grants being issued to individuals not meeting the set criteria.

## Progress Report including Assurance Opinions

| Department | Activity Name | Priority | Activity Status | Risk Opinion | Control Opinion | Reported to Audit and Governance Committee | Comments |
|---|---|---|---|---|---|---|---|
| Exempt | Exempt | 1 | Final Report Issued | Satisfactory | Satisfactory | 15/11/2021 | Brought Forward from 20/21 plan. |
| Council Wide | Health and Safety Limited Assurance Second Follow Up | 1 | Planned | | | | Discussion ongoing with key contacts to confirm if a February 22 activity start remains viable. |
| Council Wide | Complaints Procedure | 2 | Review in Progress | | | | Consultancy review based on introduction of new system. |
| Council Wide | Agency Staff | 2 | Planned | | | | Terms of reference issued. |
| Council Wide | Employee Code of Conduct | 1 | Planned | | | | Deferral from 20/21 agreed through the Revised Internal Audit Plan 20/21. |
| Council Wide | Effective use of Probationary period | 2 | Planned | | | | Deferral from 20/21 agreed through the Revised Internal Audit Plan 20/21. |
| Council Wide | Patch Management | 1 | Final Report Issued | Substantial | Substantial | 13/09/2021 | Brought Forward from 20/21 plan. |
| Council Wide | Cyber Security | 1 | Audit in Progress | | | | Brought Forward from 20/21 plan. |
| Council Wide | Change Management | 1 | Deferred | | | | Deferred for consideration within the Internal Audit Plan 22/23. |
| Council Wide | PCI DSS | 2 | Deferred | | | | Deferred for consideration within the Internal Audit Plan 22/23. |
| Council Wide | Climate Change Strategy | 1 | Deferred | | | | Deferred for consideration within the Internal Audit Plan 22/23. |
| Council Wide | Covid Recovery Scheme - Plan and Financial Pressures | 1 | Planned | | | | |
| Council Wide | Data Breaches and Breach Reporting | 2 | Final Report Issued | Satisfactory | Satisfactory | 15/11/2021 | |
| Communities | Section 202 reviews | 2 | Planned | | | | Deferral from 20/21 agreed through the Revised Internal Audit Plan 20/21. Terms of reference issued. Audit due to start in quarter 4 22/23. |
| Communities | Tenancy Rescue | 2 | Planned | | | | Deferral from 20/21 agreed through the Revised Internal Audit Plan 20/21. |
| Communities | Social Values Policy | 1 | Final Report Issued | Not Applicable | Not Applicable | 15/11/2021 | |
| Communities | Disabled Facilities Grant | 2 | Final Report Issued | Satisfactory | Satisfactory | 17/01/2022 | |
| Communities | Homeless Outreach | 2 | Planned | | | | Terms of reference issued. |
| Communities | Compliance and Enforcement Grant | 1 | Final Report Issued | Not Applicable | Not Applicable | 13/09/2021 | **New Activity.** |
| Cultural Services | Cultural Strategy Review | 1 | Review in Progress | | | | Consultancy review across 21/22. Outcomes to be reported within the 21/22 Annual Report. |
| Cultural Services | Culture Recovery Fund - round 1 | 1 | Final Report Issued | Not Applicable | Not Applicable | 15/11/2021 | **New Activity.** |
| Cultural Services | Culture Recovery Fund - round 2 | 1 | Planned | | | | **New Activity.** For quarter 4 21/22 delivery. |
| Cultural Services | Culture Recovery Fund - round 3 | 1 | Planned | | | | **New Activity.** For quarter 4 22/22 delivery. |
| Place | Community Infrastructure Levy (CIL) and Section 106 | 1 | Audit in Progress | | | | Deferral from 20/21 agreed through the Revised Internal Audit Plan 20/21. Activity planning and risk discussions completed within the Audit and Governance Committee Chair and the Cabinet Member for Planning and Housing Strategy. |
| Place | High Street Heritage Action Zone | 2 | Deferred | | | | Deferred for consideration within the Internal Audit Plan 22/23. |
| Place | Recycling Commodities | 2 | Audit in Progress | | | | |
| Place | Recycling Credits | 2 | Audit in Progress | | | | |
| Place | Planning - Processing and Performance | 2 | Deferred | | | | Deferred for consideration within the Internal Audit Plan 22/23. |
| Policy and Resources | Bank Reconciliation | 1 | Audit in Progress | | | | Deferral from 20/21 agreed through the Revised Internal Audit Plan 20/21. |
| Policy and Resources | Cemeteries and Crematorium – compliance with GDPR | 2 | Deferred | | | | Deferred for consideration within the Internal Audit Plan 22/23. |
| Policy and Resources | Election Accounts | 1 | Final Report Issued | Not Applicable | Not Applicable | 17/01/2022 | |
| Policy and Resources | Blackfriars Priory Turnover Certificate | 1 | Final Report Issued | Not Applicable | Not Applicable | 13/09/2021 | |
| Policy and Resources | Investment Portfolio Risk | 1 | Planned | | | | |
| Policy and Resources | Technology Forge | 1 | Review in Progress | | | | Consultancy review across 21/22. Outcomes to be reported within the 21/22 Annual Report. |
| Policy and Resources | Procurement Cards | 2 | Final Report Issued | Satisfactory | Satisfactory | 15/11/2021 | |
| Policy and Resources | Disposals - HKP | 2 | Planned | | | | |
| Policy and Resources | Gloucestershire Airport | 1 | Planned | | | | |
| Policy and Resources | Lost Sales, Fees and Charges Claim Three | 1 | Final Report Issued | Not Applicable | Not Applicable | 13/09/2021 | |
| Policy and Resources | Accounts Receivable | 1 | Final Report Issued | Satisfactory | Satisfactory | 17/01/2022 | |

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Gloucester City Council

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|---|---|---|---|
| **Meeting:** | **Audit and Governance Committee** | **Date:** | **7th March 2022** |
| **Subject:** | **Draft Internal Audit Plan 2022/23** | | |
| **Report Of:** | **Head of Audit Risk Assurance (ARA)** | | |
| **Wards Affected:** | **Not applicable** | | |
| **Key Decision:** | **No** | **Budget/Policy Framework:** | **No** |
| **Contact Officer:** | **Piyush Fatania, Head of ARA** | | |
| | **Email:** **piyush.fatania@gloucestershire.gov.uk** | | **Tel:** **01452 328883** |
| **Appendices:** | **A: Draft Internal Audit Plan 2022/23** | | |

**FOR GENERAL RELEASE**

## 1.0 Purpose of Report

1.1 To provide the Committee with a summary of the draft Risk Based Internal Audit Plan 2022/23, as required by the Accounts and Audit Regulations 2015 and the Public Sector Internal Audit Standards (PSIAS) 2017.

## 2.0 Recommendations

2.1 Audit and Governance Committee is asked to **RESOLVE** to:

(1) Agree that the Internal Audit Plan for 2022/23 reflects the risk profile of the Council; and

(2) Approve the Internal Audit Plan 2022/23 as detailed in **Appendix A**.

## 3.0 Background and Key Issues

3.1 All Councils must make proper provision for Internal Audit in line with the Accounts and Audit Regulations 2015 (the Regulations). The Regulations provide that a relevant Council 'must undertake an effective Internal Audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance'. Completion of annual internal audits based on the risk profile of the Council also supports the Section 151 Officer's duty to ensure the proper administration of the Council's financial affairs.

3.2 The guidance accompanying the Regulations recognises the PSIAS 2017 (the Standards) as representing 'proper Internal Audit practices'. The Standards define the way in which the Internal Audit service should be established and undertake its operations. These Standards require the Head of ARA to produce an Annual Risk Based Internal Audit Plan to determine the priorities of Internal Audit activity.

The proposed activity should be consistent with the Council's priorities and objectives, taking into account the risk management framework, risk appetite levels set by management and Internal Audit's own judgement of risks.

3.3 To ensure Internal Audit resources continue to be focussed accordingly, particularly during periods of organisational change, it is essential that we understand the Council's needs. This requires building relationships with key stakeholders, including other assurance and challenge providers, to gain crucial insight and ongoing understanding of the strategic and operational change agendas within the Council.

3.4 This insight is not only identified at the initial development stages of the Risk Based Internal Audit Plan. Dialogue continues throughout the financial year(s) and increases the ability for the Internal Audit service to adapt more closely to meet the assurance needs of the Council, particularly during periods of significant change. Our Plan is therefore dynamic and flexible to meet these needs.

3.5 To ensure that an effective Plan is developed and alongside Internal Audit's own assessment of risk, a consultation process took place with Corporate Directors, Heads of Service and Service Managers to establish priorities and assurance requirements. Audit and Governance Committee and wider Member audit requests from 2021/22 were also considered as part of the consultation approach. The proposed activity from all sources was collated and matched against Internal Audit's resource availability and prioritised accordingly.

3.6 The Plan is stated in terms of estimated days input to the Council of 550 audit days, which is comparable to prior year.

3.7 By continuing to apply risk based Internal Audit planning principles, this level of input is considered acceptable to provide the Internal Audit assurance requirements of the Council. The Head of ARA will continue to reassess Internal Audit resource requirements against the Council's priorities and risks and will amend the Plan throughout the year as required. Any key changes to the Plan will be reported to the Audit and Governance Committee.

## 4.0 Social Value Considerations

4.1 There are no Social Value implications as a result of the recommendations made in this report.

## 5.0 Environmental Implications

5.1 There are no Environmental implications as a result of the recommendations made in this report.

## 6.0 Alternative Options Considered

6.1 No other options can be considered as a Risk Based Internal Audit Plan is required by the PSIAS.

## 7.0 Reasons for Recommendations

7.1 A requirement of the PSIAS is for the Head of ARA to produce an Annual Risk Based Internal Audit Plan and for this Plan to be approved by the appropriate body. In the case of Gloucester City Council, the appropriate body is the Audit and Governance Committee.

## 8.0 Future Work and Conclusions

8.1 Regular reports on progress against the Risk Based Internal Audit Plan and any significant control issues identified will be presented to the Audit and Governance Committee. These will be captured within the Audit and Governance Committee work programme for 2022/23.

## 9.0 Financial Implications

9.1 There are no Financial implications as a result of the recommendations made in this report.

Financial Services have been consulted in the preparation this report.

## 10.0 Legal Implications

10.1 As set out in the report, the Risk Based Internal Audit Plan assists the Council to discharge its statutory responsibilities under Regulation 5 of the Accounts and Audit Regulations 2015 and significant aspects of the Section 151 Officer’s duties.

One Legal have been consulted in the preparation this report.

## 11.0 Risk and Opportunity Management Implications

11.1 Failure to deliver an effective Risk Based Internal Audit Plan will impact on the statutory requirement to provide the Council with an annual independent Internal Audit opinion on the effectiveness of the Council’s control environment comprising risk management, control and governance.

## 12.0 People Impact Assessment (PIA) and Safeguarding:

12.1 The Internal Audit service is delivered by ARA which is an Internal Audit and Risk Management Shared Service between Gloucester City Council, Stroud District Council and Gloucestershire County Council. Equality in service delivery is demonstrated by the team being subject to, and complying with, the Council’s equality policies.

12.2 The PIA Screening Stage was completed and did not identify any potential or actual negative impact, therefore a full PIA was not required.

## 13.0 Community Safety Implications

13.1 There are no Community Safety implications as a result of the recommendations made in this report.

## 14.0 Staffing and Trade Union Implications

14.1 There are no Staffing and Trade Union implications as a result of the recommendations made in this report.

**Background Documents:** Accounts and Audit Regulations 2015
PSIAS 2017
CIPFA Local Government Application Note for the UK PSIAS

# AUDIT, RISK AND ASSURANCE – DRAFT INTERNAL AUDIT PLAN 2022/23

| Ref | Indicative Quarter | Entity | Audit | Risk Score | Proposed Scope | Risk Register Ref |
|---|---|---|---|---|---|---|
| **Quarter 1 2022/23** | | | | | | |
| 1 | 1 | Communities | Health and Safety Follow-up | High | To provide assurance on the effectiveness of the new framework for managing health and safety risks across the Council. | SRR 1.3 |
| 2 | 1 | Communities | High Street Heritage Action Zone | Medium | To review the systems in operation for processing applications and monitoring grant expenditure. This includes a review of the grant application process, to ensure compliance with guidance and to establish the level of monitoring undertaken once a grant award has been made. | SRR 1.5 |
| 3 | 1 | Communities | CIL and Section 106 Agreements | High | To review the risks, processes and controls regards CIL and Section 106 agreements. | SRR 1.4 and 1.8 |
| 4 | 1 | Culture | Blackfriars Turnover Certificate | Sign-off | To provide assurance that the turnover values stated to English Heritage are in accordance with, and supported by, documents and records held by the Council. | SRR 1.4 |
| 5 | 1 | Culture | Marketing Strategy | Consultancy | To assess the governance arrangements and the progress towards delivering the Council's commitment in this area. | SRR 1.2 and 1.5 |
| 6 | 1 | Culture | Statues and Monuments | Consultancy | This will provide consultancy input and support for the Council’s Statues and Monuments review, following on from the 2021/22 Internal Audit Plan Cultural Strategy activity. | SRR 1.2 |
| 7 | 1 | ICT | Cyber Incident Support | High | ARA support to the Council following the cyber incident. | SRR 1.9 and 1.10 |

# AUDIT, RISK AND ASSURANCE – DRAFT INTERNAL AUDIT PLAN 2022/23

| Ref | Indicative Quarter | Entity | Audit | Risk Score | Proposed Scope | Risk Register Ref |
|---|---|---|---|---|---|---|
| 8 | 1 | Policy and Resources | Agency Staff | Medium | To review the arrangements for the: Initial approval process to engage with an agency; Completion and authorisation of relevant timesheets; Scrutiny of invoices received from the agency; and Formalisation of contractual arrangement with the individual agency staff member (if required). | SRR 1.3 |
| 9 | 1 | Policy and Resources | Bank Reconciliation | High | To examine reconciliation processes to verify their regularity, accuracy, completeness, and timeliness. | SRR 1.1 |
| | | | **Quarter 2 2022/23** | | | |
| 10 | 2 | Communities | Housing Strategy | High | To assess the governance arrangements and the progress towards delivering the Council's commitment in this area. | SRR 1.1 |
| 11 | 2 | Culture | Cultural Recovery Fund | Medium | Required grant sign-off of the Cultural Recovery Fund. | SRR 1.5 |
| 12 | 2 | Culture | Culture Grants (Guildhall and Museum) | Medium | To assess the systems and processes in place to ensure effective use of grant allocations. | SRR 1.5 |
| 13 | 2 | ICT | ICT Internal Audits | High | Selection of ICT audits. Most likely carry forwards from 2021/22 - Change management and ICT benefits realisation. | SRR 1.9 and 1.10 |
| 14 | 2 | Place | Planning Performance and Income | Medium | To assess the arrangements for accepting, validating, publicising and determining planning applications. The Council's activities in monitoring and securing effective performance shall also be reviewed. | SRR 1.2 and 1.3 |
| 15 | 2 | Place | First Homes | Medium | To examine the processes and policies in line with the requirements of the first homes legislation. | SRR 1.5 |
| 16 | 2 | Policy and Resources | Key Financial Controls | High | To includes audits of Capital Accounting, Council Tax and NNDR. | SRR 1.1 and1.6 |

# AUDIT, RISK AND ASSURANCE – DRAFT INTERNAL AUDIT PLAN 2022/23

| Ref | Indicative Quarter | Entity | Audit | Risk Score | Proposed Scope | Risk Register Ref |
|---|---|---|---|---|---|---|
| | | | | | **Quarter 3 2022/23** | |
| 17 | 3 | Climate | Climate / Carbon Reduction | High | To assess the governance arrangements and the progress towards delivering the Council's commitment in this area. Areas for consideration include Service Planning, Climate Change Strategy and Canopy Cover Plan. | SRR 1.9 and 1.10 |
| 18 | 3 | Communities | Homeless Pathway | Medium | To review the effectiveness of the processing of homelessness applications. To include the monitoring of homelessness cases, the application process, compliance with the guidance, and the level of monitoring. | SRR 1.2 |
| 19 | 3 | Council Wide | Contract Management | High | To review the Council's contract management arrangements and assess the effectiveness of the governance of contractual arrangements with key partners and third parties. | SRR 1.4 |
| 20 | 3 | Council Wide | Procurement | High | To review a range of recent procurement activities to determine whether these have been made in compliance with the Council's Contract and Procurement Procedure Rules. | SRR 1.2 and 1.4 |
| 21 | 3 | Place | City Growth Strategies | Consultancy | To assess the governance arrangements and the progress towards delivering the Council's commitment in this area. | SRR 1.5 |
| 22 | 3 | Policy and Resources | IR35 | Medium | To review the systems, policies, and procedures in place to assess whether new and existing off-payroll workers are identified, assessed, and paid in accordance with IR35 requirements. | SRR 1.3 |
| | | | | | **Quarter 4 2022/23** | |
| 23 | 4 | Communities | Home Improvement Agency | Consultancy | Consultancy on the option of the Council to establish a Home Improvement Agency for the delivery of Disabled Facilities Grants. | SRR 1.1 and 1.11 |

# AUDIT, RISK AND ASSURANCE – DRAFT INTERNAL AUDIT PLAN 2022/23

| Ref | Indicative Quarter | Entity | Audit | Risk Score | Proposed Scope | Risk Register Ref |
|---|---|---|---|---|---|---|
| 24 | 4 | Council Wide | Leavers Processes (Off-Boarding) | Medium | This review will seek to determine the effectiveness of the Council's arrangements for managing the process for when employees leave the Council. | SRR 1.6 |
| 25 | 4 | Council Wide | Employee Wellbeing and Retention | Consultancy | Consultancy on employee wellbeing themes which could include: Employee training and retention schemes; A review of the Mental Health & Wellbeing Policy against best practice and industry leaders; and A review of the Agile Working Policy. | SRR 1.3 |
| 26 | 4 | Policy and Resources | Asset Management Strategy | High | To assess whether:<br>– The Strategy, policies and guidance, including roles and responsibilities, provide for the effective and sound management of assets;<br>– The processes, systems and tools to manage assets are effective including recording, capitalisation, depreciation and tagging of assets, effective tracking of asset movements and periodic verification and reconciliation of assets; and<br>– Assets adequately safeguarded and utilised as intended. | SRR 1.1 and 1.14 |
| 27 | 4 | Policy and Resources | Sickness and Absence | Medium | To review the content of, and compliance with, the Council's Sickness and Absence policy and procedures. | SRR 1.3 |
| **Throughout 2022/23** | | | | | | |
| 28 | Throughout | Contingency | Contingency | | An allowance of time to allow for flexibility regards emerging risks. Internal Audit to consider further work surrounding the cyber incident. | |
| 29 | Throughout | Council Wide | Assurance Mapping | | To complete and update assurance mapping, in line with the three lines of defence model to identify the key sources of assurance. | |

## AUDIT, RISK AND ASSURANCE – DRAFT INTERNAL AUDIT PLAN 2022/23

| Ref | Indicative Quarter | Entity | Audit | Risk Score | Proposed Scope | Risk Register Ref |
|---|---|---|---|---|---|---|
| 30 | Throughout | Counter Fraud | Counter Fraud | | This captures Counter Fraud support; Fraud Investigation and Detection; National Fraud Initiative (NFI) activity; and Fraud Risk Management. | SRR 1.6 |
| 31 | Throughout | Support | Management and Planning | | This captures a number of activity streams, including but not exclusive to: Audit Management and Planning; Committee reporting and attendance; Working Group and Board (such as Corporate Governance and Information Governance) attendance; Annual Governance Statement facilitation; Provision of Internal Control or General Advice; and Quality Assurance and Improvement Programme delivery. | |
| 32 | Throughout | Support | Recommendation Monitoring | | This allocation enables ARA to monitor management's progress with the implementation of Internal Audit recommendations. | |

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Gloucester City Council

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| **Meeting:** | **Audit & Governance Committee**<br>**Cabinet**<br>**Council** | **Date:** | **7 March 2022**<br>**9 March 2022**<br>**24 March 2022** |
| **Subject:** | **Treasury Management Strategy 2022/23** | | |
| **Report Of:** | **Cabinet Member for Performance and Resources** | | |
| **Wards Affected:** | **All** | | |
| **Key Decision:** | **No** | **Budget/Policy Framework:** | **Yes** |
| **Contact Officer:** | **Jon Topping, Director of Policy and Resources**<br>**Email: jon.topping@gloucester.gov.uk** | **Tel: 396242** | |
| **Appendices:** | **1. Treasury Management Strategy 2022/23** | | |

## 1.0 Purpose of Report

1.1 To formally recommend that Council approves the attached Treasury Management Strategy, the prudential indicators and note the Treasury activities.

## 2.0 Recommendations

2.1 Audit and Governance Committee is asked to **RECOMMEND** that the Treasury Management Strategy be approved.

2.2 Council is asked to **RESOLVE** that:

(1) The Treasury Management Strategy at Appendix 1 be approved;

(2) The authorised borrowing limit be approved at:-
a) 2022/23 £265m
b) 2023/24 £260m
c) 2024/25 £255m

(3) The prudential indicators set out in section two of the strategy be approved.

## 3.0 Background and Key Issues

3.1 Recent property acquisitions within Gloucester and continued regeneration of the City, the Councils borrowing requirements have increased. These long term investments and projects will significantly change the treasury position of the Council over the life of the investments, creating investable cashflow streams.

3.2 The Council has continued to support partners to further its strategic objectives. In 2021-22, the Council arranged additional funding to Ladybellgate Estates to facilitate the redevelopment of the Food Dock. The Council will continue to look at these social investments as a delivery mechanism to support its wider strategic objectives.

3.3 The 2022/23 treasury management strategy recommends to continue operating within an under-borrowing position. This position reflects that the Council uses internal resources, such as reserves, to fund the borrowing need rather than invest those funds for a return. This strategy is sensible, at this point in time, for two reasons. Firstly, the lost interest on those funds is significantly less than the costs of borrowing money for the capital programme. In addition, using the resources to reduce debt the Council will reduce exposure to investment counterparty risk.

3.4 There will be cash flow balances that will be invested for short periods within the year. Section 4 of the strategy outlines the Annual Investment Strategy; in particular it outlines the creditworthiness policy through the use of credit ratings.

3.5 The borrowing strategy is to utilise investments to reduce short term borrowing. Once investments have been applied it is anticipated that the majority of new debt will be short term as the current market rates are attractive. Where the capital programme, or investment strategy, requires the creation of long-term investment need then some long term borrowing is likely to be undertaken to take advantage of low rates and mitigate the risk presented by having all borrowing on short-term deals.

3.6 The strategy allows flexibility for either debt rescheduling or new long term fixed rate borrowing while allowing the Council to benefit from lower interest rates on temporary borrowing at the current time.

3.7 The strategy also includes the minimum revenue provision (MRP) policy statement. This policy continues with the practice approved last year. MRP is the revenue charge to reduce debt by placing a charge on the General Fund each year. The preferred option is to provide for the borrowing need created over the approximate life of the asset purchased. This is achieved with an annuity calculation which provides a consistent overall annual borrowing charge with the level of principal (MRP) increasing each year, much like a repayment mortgage.

## 4.0 Alternative Options Considered

4.1 The following option has been considered:

There remains the option to replace existing short term borrowing with longer term options, this is not as attractive due to the availability of short term funding which remains significantly below rates available for longer term funds.

**5.0 Reasons for Recommendations**

5.1 As outlined in the legal implications the recommendations require Council approval. The Treasury and Investment Strategies recommended provide the best platform for financing the long-term capital programme and managing daily cash flow whilst protecting Council funds.

**6.0 Future Work and Conclusions**

6.1 The Treasury Management Strategy provides a logical basis to fund the Council's capital financing requirement and long-term Capital Programme. The Council will continue to monitor the strategy and is prepared to adapt this strategy if there is changes within the markets.

**7.0 Financial Implications**

7.1 The expenditure and income arising from treasury management activities are included within the Council Money Plan.

**8.0 Social Value Considerations**

8.1 This report notes the Treasury Strategy of the Council. ESG requirements are covered within the Prudential Code.

**9.0 Legal Implications**

9.1 The Council is required to have a Treasury Management Strategy to meet the requirements of the Local Government Act 2003, the CIPFA Prudential Code, DLUHC Minimum Revenue Provision Guidance, the CIPFA Treasury Management Code and DLUHC Investment Guidance.

**10.0 Risk & Opportunity Management Implications**

10.1 There is a risk that short term and long term interest rates could increase and this will be monitored both in-house and by the Council Treasury Management Advisor, Link Asset Services. In this event the risk will be managed through the opportunities either to reschedule debt or new long term fixed rate borrowing in place of short term borrowing.

10.2 The risk of deposits not being returned by the counterparty is minimised by only investing short term cash flow monies with counterparties on the approved lending list. All counterparties on this list meet minimum credit rating criteria, ensuring the risk is kept extremely low although not eliminated.

## 11.0 People Impact Assessment (PIA):

11.1 A PIA screening assessment has been undertaken and the impact is neutral. A full PIA is not required.

## 12.0 Other Corporate Implications

Community Safety

12.1 None

Sustainability

12.2 None

Staffing & Trade Union

12.3 None

**Background Documents:**

Local Government Act 2003
CIPFA Treasury Management Code
CIPFA Prudential Code
DLUHC MRP Guidance

**Appendix 1**

# Treasury Management Strategy 2022/23

## 1. Introduction

**2021 revised CIPFA Treasury Management Code and Prudential Code – changes which will impact on future TMSS/AIS reports and the risk management framework**

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

The revised codes will have the following implications:

- a requirement for the Council to adopt a new debt liability benchmark treasury indicator to support the financing risk management of the capital financing requirement;

- clarify what CIPFA expects a local authority to borrow for and what they do not view as appropriate. This will include the requirement to set a proportionate approach to commercial and service capital investment;

- address ESG issues within the Capital Strategy;

- require implementation of a policy to review commercial property, with a view to divest where appropriate;

- create new Investment Practices to manage risks associated with non-treasury investment (similar to the current Treasury Management Practices);

- ensure that any long term treasury investment is supported by a business model;

- a requirement to effectively manage liquidity and longer term cash flow requirements;

- amendment to TMP1 to address ESG policy within the treasury management risk framework;

- amendment to the knowledge and skills register for individuals involved in the treasury management function - to be proportionate to the size and complexity of the treasury management conducted by each council;

- a new requirement to clarify reporting requirements for service and commercial investment, (especially where supported by borrowing/leverage).

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

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

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

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

As this Treasury Management Strategy Statement and Annual Investment Strategy deals soley with treasury management investments, the categories of service delivery and commercial investments will be dealt with as part of the Capital Strategy report.

### 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.

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."*

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.

## 1.2 Reporting requirements

### 1.2.1 Capital Strategy

The CIPFA 2017 Prudential and Treasury Management Codes require all local authorities to prepare 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 this 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.

### 1.2.2 Treasury Management reporting

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

**Prudential and treasury indicators and treasury strategy** (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).

**A mid-year treasury management report** – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

**An annual treasury report** – This is a backward-looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

**Scrutiny**
The above reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken at Gloucester by the Audit and Governance Committee.

## 1.3 Treasury Management Strategy for 2022/23

The strategy for 2022/23 covers two main areas:

**Capital issues**

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

**Treasury management issues**

- the current treasury position;
- 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, DLUHC Investment Guidance, DLUHC MRP Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management.

## 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. Finance training for members, including Treasury Management, featured in the member development programme during 2021/22

The training needs of treasury management officers are periodically reviewed and staff have attended training and seminars during 2021/22 and will continue to do so in the upcoming year.

## 1.5 Treasury management consultants

The Council uses Link Group, 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 will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

The scope of investments within the Council’s operations now includes both conventional treasury investments, (the placing of residual cash from the Council’s functions), and more commercial type investments, such as investment properties. The commercial type investments require specialist advisers, and the Council uses such advisors on a case by case basis in relation to this activity.

# 2 THE CAPITAL PRUDENTIAL INDICATORS 2022/23 – 2024/25

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.

## 2.1 Capital expenditure

This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts.

| Capital expenditure £m | 2020/21 Actual | 2021/22 Estimate | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|---|
| Policy & Resources | 2.715 | 3.707 | 3.395 | 0.150 | 0.195 |
| Place | 3.329 | 13.416 | 23.106 | 31.886 | 44.000 |
| Communities | 1.299 | 6.786 | 1.036 | 0.754 | 0.754 |
| Culture & Trading | 0.000 | 0.000 | 0.000 | 0.000 | 0.000 |
| **Total** | **7.343** | **23.909** | **27.537** | **32.790** | **44.949** |

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

| Financing of capital expenditure £m | 2020/21 Actual | 2021/22 Estimate | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|---|
| Capital receipts | 0.467 | 2.000 | 0.444 | 0.330 | 0.275 |
| Capital grants | 4.935 | 3.853 | 3.893 | 2.260 | 0.474 |
| Capital reserves | 0.000 | 0.000 | 0.000 | 0.000 | 0.000 |
| Revenue | 0.500 | 0.000 | 0.000 | 0.000 | 0.000 |
| **Net borrowing need for the year** | **1.441** | **18.056** | **23.200** | **30.200** | **44.200** |

## 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 its underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, 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 CFR includes any other long-term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility by the PFI, PPP lease provider and so the Council is not required to separately borrow for these schemes. The Council currently has £21.42m of such schemes within the CFR.

The Council is asked to approve the CFR projections below:

| £m | 2020/21 Actual | 2021/22 Estimate | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|---|
| | | | | | |
| **Capital Financing Requirement** | | | | | |
| **Total CFR** | **118.949** | **134.970** | **155.869** | **183.719** | **225.542** |
| **Movement in CFR** | **0.571** | **16.021** | **20.899** | **27.850** | **41.823** |

| | | | | | |
|---|---|---|---|---|---|
| **Movement in CFR represented by** | | | | | |
| Net financing need for the year (above) | 1.441 | 18.056 | 23.200 | 30.200 | 44.200 |
| Less MRP/VRP and other financing movements | (0.870) | (2.035) | (2.301) | (2.350) | (2.377) |
| **Movement in CFR** | **0.571** | **16.021** | **20.899** | **27.850)** | **41.823** |

## 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 £m | 2020/21 Actual | 2021/22 Estimate | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|---|
| Fund balances / reserves | 1.682 | 1.805 | 1.805 | 1.762 | 1.827 |
| Capital receipts | 0.236 | 0.990 | 4.500 | 1.000 | 0.500 |
| Provisions | 1.610 | 1.500 | 1.500 | 1.500 | 1.500 |
| Other (Grants) | 3.880 | 2.000 | 2.000 | 2.000 | 2.000 |
| **Total core funds** | **7.408** | **6.295** | **9.805** | **6.262** | **5.827** |
| Working capital* | (2.873) | (4.000) | (4.000) | (4.000) | (4.000) |
| Under/over borrowing** | 10.637 | 3.337 | (0.493) | (0.993) | (1.493) |
| **Expected investments** | **15.172** | **5.632** | **5.312** | **1.269** | **0.334** |

*Working capital balances shown are estimated year-end; these will vary in 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).

DLUHC 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*):*

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

- **Existing practice** - MRP will follow the existing practice outlined in former DLUHC regulations (option 1) This option provides for an approximate 4% reduction in the borrowing need (CFR) each year.

From 1 April 2008 for all unsupported borrowing (including finance leases) the MRP policy will be

- **Asset life method –** MRP will be based on the estimated life of the assets, in accordance with the regulations

These options provide for a reduction in the borrowing need over approximately the asset's life.

Repayments included in finance leases and loan principal are applied as MRP.

**MRP Overpayments** - A change introduced by the revised DLUHC 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. Up until the 31 March 2021 the total VRP overpayments were £1.359m.

## 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.

### 3.1 Current portfolio position

The Council's treasury portfolio position at 31 March 2021 with forward projections, is summarised below. The table shows the actual external debt (the treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

| £m | 2020/21 Actual | 2021/22 Estimate | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|---|
| **External Debt** | | | | | |
| Debt at 1 April | 101.229 | 108.150 | 112.738 | 132.847 | 159.918 |
| Expected change in Debt | 6.921 | 8.418 | 20.609 | 27.571 | 41.562 |
| *Other long-term liabilities (OLTL)* | *21.12* | *21.436* | *21.739* | *22.029* | *22.308* |
| *Expected change in OLTL* | *0.316* | *0.303* | *0.290* | *0.279* | *0.261* |
| Actual gross debt at 31 March | **129.586** | **138.004** | **155.376** | **182.726** | **224.049** |
| The Capital Financing Requirement | **118.949** | **134.970** | **155.869** | **183.719** | **225.542** |
| Under / (over) borrowing | **(10.637)** | **(3.337)** | **0.493** | **0.993** | **1.493** |

The Council was over borrowed at 31/3/21 as a result of securing long term borrowing while still holding temporary borrowing. Securing long term borrowing at preferential rates ensures long term stability to the Council's borrowing portfolio. The Council is forecast to be over borrowed at 31/1/22, which relates to the pension prepayment of secondary contributions. The prepayment was beneficial in reducing ongoing pension contributions, the Council is forecast to return to an under borrowed position in 22/23.

Within the 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 2022/23 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 Director of Policy and Resources 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 budget report.

### 3.2 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 £m | 2021/22 Estimate | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|
| Debt | 120 | 215 | 210 | 205 |
| Other long term liabilities | 30 | 30 | 30 | 30 |
| Total | 155 | 245 | 240 | 235 |

**The authorised limit for external debt.** A further key prudential indicator represents a control on the maximum level of borrowing. This represents a 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 £m | 2021/22 Estimate | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|
| Debt | 130 | 230 | 225 | 220 |
| Other long term liabilities | 35 | 35 | 35 | 35 |
| Total | 165 | 265 | 260 | 255 |

### 3.3 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 20th December 2021. These are forecasts for certainty rates, gilt yields plus 80 bps:

| Link Group Interest Rate View 20.12.21 | Dec-21 | Mar-22 | Jun-22 | Sep-22 | Dec-22 | Mar-23 | Jun-23 | Sep-23 | Dec-23 | Mar-24 | Jun-24 | Sep-24 | Dec-24 | Mar-25 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| BANK RATE | 0.25 | 0.25 | 0.50 | 0.50 | 0.50 | 0.75 | 0.75 | 0.75 | 0.75 | 1.00 | 1.00 | 1.00 | 1.00 | 1.25 |
| 3 month ave earnings | 0.20 | 0.30 | 0.50 | 0.50 | 0.60 | 0.70 | 0.80 | 0.90 | 0.90 | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 |
| 6 month ave earnings | 0.40 | 0.50 | 0.60 | 0.60 | 0.70 | 0.80 | 0.90 | 1.00 | 1.00 | 1.10 | 1.10 | 1.10 | 1.10 | 1.10 |
| 12 month ave earnings | 0.70 | 0.70 | 0.70 | 0.70 | 0.80 | 0.90 | 1.00 | 1.10 | 1.10 | 1.20 | 1.20 | 1.20 | 1.20 | 1.20 |
| 5 yr PWLB | 1.40 | 1.50 | 1.50 | 1.60 | 1.60 | 1.70 | 1.80 | 1.80 | 1.80 | 1.90 | 1.90 | 1.90 | 2.00 | 2.00 |
| 10 yr PWLB | 1.60 | 1.70 | 1.80 | 1.80 | 1.90 | 1.90 | 2.00 | 2.00 | 2.00 | 2.10 | 2.10 | 2.10 | 2.20 | 2.30 |
| 25 yr PWLB | 1.80 | 1.90 | 2.00 | 2.10 | 2.10 | 2.20 | 2.20 | 2.20 | 2.30 | 2.30 | 2.40 | 2.40 | 2.50 | 2.50 |
| 50 yr PWLB | 1.50 | 1.70 | 1.80 | 1.90 | 1.90 | 2.00 | 2.00 | 2.00 | 2.10 | 2.10 | 2.20 | 2.20 | 2.30 | 2.30 |

*Additional notes by Link on this forecast table: -*

- *LIBOR and LIBID rates will cease from the end of 2021. Work is currently progressing to replace LIBOR with a rate based on SONIA (Sterling Overnight Index Average). In* *the meantime, our forecasts are based on expected average earnings by local authorities for 3 to 12 months.*

- *Our forecasts for average earnings are averages i.e., rates offered by individual banks may differ significantly from these averages, reflecting their different needs for borrowing short term cash at any one point in time.*

Over the last two years, the coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16th December 2021.

As shown in the forecast table above, the forecast for Bank Rate now includes four increases, one in December 2021 to 0.25%, then quarter 2 of 2022 to 0.50%, quarter 1 of 2023 to 0.75%, quarter 1 of 2024 to 1.00% and, finally, one in quarter 1 of 2025 to 1.25%.

**Significant risks to the forecasts**

- **Mutations** of the virus render current vaccines ineffective, and tweaked vaccines to combat these mutations are delayed, or cannot be administered fast enough to prevent further lockdowns. 25% of the population not being vaccinated is also a significant risk to the NHS being overwhelmed and lockdowns being the only remaining option.

- **Labour and supply shortages** prove more enduring and disruptive and depress economic activity.

- **The Monetary Policy Committee** acts 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.

- **The Monetary Policy Committee** tightens monetary policy too late to ward off building inflationary pressures.

- **The Government** acts too quickly to cut expenditure to balance the national budget.

- **UK / EU trade arrangements** – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.

- **Longer term US treasury yields** rise strongly and pull gilt yields up higher than forecast.

- **Major stock markets** e.g., in the US, become increasingly judged as being over-valued and susceptible to major price corrections. Central banks become increasingly exposed to the "moral hazard" risks of having to buy shares and corporate bonds to reduce the impact of major financial market selloffs on the general economy.

- **Geopolitical risks,** for example in Ukraine, Iran, North Korea, but also in Europe and Middle Eastern countries; on-going global power influence struggles between Russia/China/US. These could lead to increasing safe-haven flows.

**The balance of risks to the UK economy: -**

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

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

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

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

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

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

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

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

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

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

In summary, with the high level of uncertainty prevailing on several different fronts, we expect to have to revise our forecasts again - in line with whatever the new news is.

It should also be borne in mind that Bank Rate being cut to 0.25% and then to 0.10%, were emergency measures to deal with the Covid crisis hitting the UK in March 2020. At any time, the MPC could decide to simply take away such emergency cuts on no other grounds than they are no longer warranted, and as a step forward in the return to normalisation. In addition, any Bank Rate under 1% is both highly unusual and highly supportive of economic growth.

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

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

**US treasury yields.** During the first part of 2021, US President Biden's, and the Democratic party's, determination to push through a $1.9trn (equivalent to 8.8% of GDP) fiscal boost for the US economy as a recovery package from the Covid pandemic was what unsettled financial markets. However, this was in addition to the $900bn support package already passed in December 2020. This was then followed by additional Democratic ambition to spend $1trn on infrastructure, (which was eventually passed by both houses later in 2021), and an even larger sum on an American families plan over the next decade; this is still caught up in Democrat / Republican haggling. Financial markets were alarmed that all this stimulus was happening at a time when: -

1. A fast vaccination programme had enabled a rapid opening up of the economy during 2021.
2. The economy was growing strongly during the first half of 2021 although it has weakened overall during the second half.
3. It started from a position of little spare capacity due to less severe lockdown measures than in many other countries.
4. And the Fed was still providing substantial stimulus through monthly QE purchases during 2021.

It was not much of a surprise that a combination of these factors would eventually cause an excess of demand in the economy which generated strong inflationary pressures. This has eventually been recognised by the Fed at its December meeting with an aggressive response to damp inflation down during 2022 and 2023.

**At its 3rd November Fed meeting**, the Fed decided to make a start on tapering its $120bn per month of QE purchases so that they ended next June. However, at its **15th December meeting** it doubled the pace of tapering so that they will end all purchases in February. These purchases are currently acting as downward pressure on treasury yields and so it would be expected that Treasury yields will rise over the taper period and after the taper ends, all other things being equal. The Fed also forecast that it expected there would be three rate rises in 2022 of 0.25% from near zero currently, followed by three in 2023 and two in 2024, taking rates back above 2% to a neutral level for monetary policy.

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

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

- How strongly will changes in gilt yields be correlated to changes in US treasury yields (see below). Over 10 years since 2011 there has been an average 75% correlation between movements in US treasury yields and gilt yields. However, from time to time these two yields can diverge. Lack of spare economic capacity and rising inflationary pressures are viewed as being much greater dangers in the US than in the UK. This could mean that central bank rates will end up rising earlier and higher in the US than in the UK if inflationary pressures were to escalate; the consequent increases in treasury yields could well spill over to cause (lesser) increases in gilt yields. There is, therefore, an upside risk to forecasts for gilt yields due to this correlation. The Link Group forecasts have included a risk of a 75% correlation between the two yields.
- Will the Fed take action to counter increasing treasury yields if they rise beyond a yet unspecified level?
- Would the MPC act to counter increasing gilt yields if they rise beyond a yet unspecified level?
- How strong will inflationary pressures actually turn out to be in both the US and the UK and so put upward pressure on treasury and gilt yields?
- How will central banks implement their new average or sustainable level inflation monetary policies?
- How well will central banks manage the withdrawal of QE purchases of their national bonds i.e., without causing a panic reaction in financial markets as happened in the "taper tantrums" in the US in 2013?
- Will exceptional volatility be focused on the short or long-end of the yield curve, or both?

As the US financial markets are, by far, the biggest financial markets in the world, any upward trend in treasury yields will invariably impact and influence financial markets in other countries. Inflationary pressures and erosion of surplus economic capacity look much stronger in the US compared to those in the UK, which would suggest that Fed rate increases eventually needed to suppress inflation, are likely to be faster and stronger than Bank Rate increases in the UK. This is likely to put upward pressure on treasury yields which could then spill over into putting upward pressure on UK gilt yields.

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

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

- There is a balance of upside risks to forecasts for medium to long term PWLB rates.

**A new era for local authority investing**
**– a fundamental shift in central bank monetary policy**

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

- The Fed in America has gone furthest in adopting a monetary policy based on a clear goal of allowing the inflation target to be symmetrical, (rather than a ceiling to keep under), so that inflation averages out the dips down and surges above the target rate, over an unspecified period of time.
- The Bank of England has also amended its target for monetary policy so that inflation should be ‘sustainably over 2%’ before starting on raising Bank Rate and the ECB now has a similar policy.
- ***For local authorities, this means that investment interest rates and very short term PWLB rates will not be rising as quickly or as high as in previous decades when the economy recovers from a downturn and the recovery eventually runs out of spare capacity to fuel continuing expansion.***
- Labour market liberalisation since the 1970s has helped to break the wage-price spirals that fuelled high levels of inflation and has now set inflation on a lower path which makes this shift in monetary policy practicable. In addition, recent changes in flexible employment practices, the rise of the gig economy and technological changes, will all help to lower inflationary pressures.
- Governments will also be concerned to see interest rates stay lower as every rise in central rates will add to the cost of vastly expanded levels of national debt; (in the UK this is £21bn for each 1% rise in rates). On the other hand, higher levels of inflation will help to erode the real value of total public debt.

**Investment and borrowing rates**

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

- **Borrowing interest rates** fell to historically very low rates as a result of the COVID crisis and the quantitative easing operations of the Bank of England and still remain at historically low levels. The policy of avoiding new borrowing by running down spare cash balances has served local authorities well over the last few years.

- On 25.11.20, the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates which had been increased by 100 bps in October 2019. The standard and certainty margins were reduced by 100 bps 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 current 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.** Our long-term (beyond 10 years), forecast for Bank Rate is 2.00%. As some PWLB certainty rates are currently below 2.00%, there remains value in considering long-term borrowing from the PWLB where appropriate. Temporary borrowing rates are likely, however, to remain near Bank Rate and may also prove attractive as part of a balanced debt portfolio.

- While this authority will not be able to avoid borrowing to finance new capital expenditure or to replace maturing debt, 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.

### 3.4 Borrowing strategy

The Council aims to maintain 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.

Against this background and the risks within the economic forecast, caution will be adopted with the 2022/23 treasury operations. The Director of Policy and Resources will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in long and short term rates* (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast,* perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

Any decisions will be reported to the appropriate decision making body at the next available opportunity.

### 3.5 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.

### 3.6 Debt rescheduling

Rescheduling of current borrowing in our debt portfolio is unlikely to occur as there is still a very large difference between premature redemption rates and new borrowing rates, even though the general margin of PWLB rates over gilt yields was reduced by 100 bps in November 2020.

All rescheduling will be reported to Cabinet at the earliest meeting following its action. The Council has recently taken long term loans and there is no current rescheduling planned.

### 3.7 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.

### 3.8 Approved Sources of Long and Short term Borrowing

| **On Balance Sheet** | **Fixed** | **Variable** |
|---|---|---|
| PWLB | ● | ● |
| Municipal bond agency | ● | ● |
| Local authorities | ● | ● |
| Banks | ● | ● |
| Pension funds | ● | ● |
| Insurance companies | ● | ● |
| UK Infrastructure Bank | ● | ● |
| | | |
| Market (long-term) | ● | ● |
| Market (temporary) | ● | ● |
| Market (LOBOs) | ● | ● |
| Stock issues | ● | ● |
| | | |
| Local temporary | ● | ● |
| Local Bonds | ● | |
| Local authority bills | ● | ● |
| Overdraft | | ● |
| Negotiable Bonds | ● | ● |
| Internal (capital receipts & revenue balances) | ● | ● |
| Commercial Paper | ● | |
| Medium Term Notes | ● | |
| Finance leases | ● | ● |

# 4 ANNUAL INVESTMENT STRATEGY

## 4.1 Investment policy

The Department of Levelling Up, Housing and Communities (DLUHC - this was formerly the Ministry of Housing, Communities and Local Government (MHCLG)) and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with treasury (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: -

- DLUHC'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 Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite.

The above guidance from the DLUHC 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. **Lending limits**, (amounts and maturity), for each counterparty will be set through applying the matrix table in paragraph 4.2.

6. **Transaction limits** are set for each type of investment in 4.2.

7. This authority will set a limit for the amount of its investments which are invested for **longer than 365 days**, (see paragraph 4.4).

8. Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating**, (see paragraph 4.3).

9. 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.

10. All investments will be denominated in **sterling**.

11. As a result of the change in accounting standards for 2022/23 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 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 the Link Group. 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:

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

This modelling approach combines credit ratings, and any assigned Watches and Outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads. The end product of this 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 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 daily. The Council is alerted to changes to ratings of all three agencies through its use of the Link 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 European Financials benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link. 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, as well as 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 |

| | **Colour (and long term rating where applicable)** | **Money and/or % Limit** | **Time Limit** |
|---|---|---|---|
| **Banks *** | **yellow** | **£10m** | **5yrs** |
| **Banks** | **purple** | **£10m** | **2 yrs** |
| **Banks** | **orange** | **£10m** | **1 yr** |

| | | | |
|---|---|---|---|
| **Banks – part nationalised** | **blue** | **£10m** | **1 yr** |
| **Banks** | **red** | **£10m** | **6 mths** |
| **Banks** | **green** | **£10m** | **100 days** |
| **Banks** | **No colour** | **Not to be used** | |
| **Limit 3 category – Council's banker (where "No Colour")** | **Barclays Bank** | **100 %** | **1 day** |
| **Other institutions limit** | **A-** | **£10m** | **6 months** |
| **DMADF** | **UK sovereign rating** | **unlimited** | **6 months** |
| **Local authorities** | **n/a** | **100%** | **1yrs** |
| | **Fund rating** | **Money and/or % Limit** | **Time Limit** |
| **Money Market Funds CNAV** | **AAA** | **£10m** | **liquid** |
| **Money Market Funds LVNAV** | **AAA** | **£10m** | **liquid** |
| **Money Market Funds VNAV** | **AAA** | **£10m** | **liquid** |
| **Ultra-Short Dated Bond Funds with a credit score of 1.25** | **Dark pink / AAA** | **£10m** | **liquid** |
| **Ultra-Short Dated Bond Funds with a credit score of 1.50** | **Light pink / AAA** | **£10m** | **liquid** |

### Creditworthiness.

Significant levels of downgrades to Short- and Long-Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. However, as economies are beginning to reopen, there have been some instances of previous lowering of Outlooks being reversed.

**CDS prices**

Although bank CDS prices, (these are market indicators of credit risk), spiked upwards at the end of March / early April 2020 due to the heightened market uncertainty and ensuing liquidity crisis that affected financial markets, they have returned to more average levels since then. However, sentiment can easily shift, so it will remain important to undertake continual monitoring of all aspects of risk and return in the current circumstances. Link monitor CDS prices as part of their creditworthiness service to local authorities and the Council has access to this information via its Link-provided Passport portal.

### 4.3 County limits

The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch or equivalent. The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 6.4. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

### 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.**
The current forecast shown in paragraph 3.3, includes a forecast for a first increase in Bank Rate in May 2022, though it could come in February..

The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year, (based on a first increase in Bank Rate in quarter 2 of 2022), are as follows.:

| Average earnings in each year | Now | Previously |
|---|---|---|
| 2022/23 | 0.50% | 0.50% |
| 2023/24 | 0.75% | 0.75% |
| 2024/25 | 1.00% | 1.00% |
| 2025/26 | 1.25% | 1.25% |
| Long term later years | 2.00% | 2.00% |

For its cash flow generated balances, the Council will seek to utilise its business reserve instant access and notice accounts, money market funds and short-dated deposits, in order to benefit from the compounding of interest.

**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 over 365 days | | | |
|---|---|---|---|
| **£m** | **2022/23** | **2023/24** | **2024/25** |
| Principal sums invested over 365 days | £30m | £30m | £30m |

### 4.5 Investment risk benchmarking

These benchmarks are simple guides to maximum risk, so they may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that officers will monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the mid-year or Annual Report.
Security - The Council's maximum security risk benchmark for the current portfolio, when compared to these historic default tables, is:

- **5% historic risk of default when compared to the whole portfolio.**

Liquidity – in respect of this area the Council seeks to maintain:

- Bank overdraft - £0m
- Liquid short term deposits of at least £5m available with a week's notice.
- Weighted average life benchmark is expected to be 25 years, with a maximum of 40 years.

Yield - local measures of yield benchmarks are:

- Investments – internal returns above the 7 day SONIA rate
- Investments – external fund managers - returns 110% above 7 day compounded SONIA.

And in addition that the security benchmark for each individual year is:

| | 1 year | 2 years | 3 years | 4 years | 5 years |
|---|---|---|---|---|---|
| **Maximum** | **5%** | **5%** | **5%** | **5%** | **5%** |

Note: This benchmark is an average risk of default measure, and would not constitute an expectation of loss against a particular investment.

### 4.6 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.

### 5.1 THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2022/23 – 2024/25

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

| Capital expenditure £m | 2020/21 Actual | 2021/22 Estimate | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|---|
| Policy & Resources | 2.715 | 3.707 | 3.395 | 0.150 | 0.195 |
| Place | 3.329 | 13.416 | 23.106 | 31.886 | 44.000 |
| Communities | 1.299 | 6.786 | 1.036 | 0.754 | 0.754 |
| Culture & Trading | 0.000 | 0.000 | 0.000 | 0.000 | 0.000 |
| **Total** | **7.343** | **23.909** | **27.537** | **32.790** | **44.949** |

### 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:

#### a. 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 Actual | 2021/22 Estimate | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate |
|---|---|---|---|---|---|
| | **14.64%** | **28.02%** | **28.76%** | **29.28%** | **29.34%** |

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

The current figures are largely the result of the Kings Walk investment, rental payments for the King's Walk lease are counted as financing expenditure as they pay off the lease liability included within the CFR. Rental payments received from retailers within Kings Walk will cover these financing costs.

The increases from 2021/22 are related to sums borrowed for the regeneration of the City including Kings Square and Kings Quarter – The Forum.

### 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:

| Maturity structure of fixed and variable interest rate borrowing 2022/23 | | |
|---|---|---|
| | **Lower** | **Upper** |
| Under 12 months | 0% | 100% |
| 12 months to 2 years | 0% | 100% |
| 2 years to 5 years | 0% | 100% |
| 5 years to 10 years | 0% | 100% |

| | | |
|---|---|---|
| 10 years and above | 0% | 100% |

#### 5.1.4. Control of interest rate exposure

Please see paragraphs 3.3, 3.4 and 4.4.

## 6 APPENDICES

1. Interest rate forecasts
2. Economic background
3. Treasury management practice 1 – credit and counterparty risk management (option 1)
4. Approved countries for investments
5. Treasury management scheme of delegation
6. The treasury management role of the section 151 officer

## 6.1 INTEREST RATE FORECASTS 2021 – 2025

**PWLB forecasts shown below have taken into account the 20 basis point certainty rate reduction effective as of the 1st November 2012.**

| Link Group Interest Ra 20.12.21 | Mar-22 | Jun-22 | Sep-22 | Dec-22 | Mar-23 | Jun-23 | Sep-23 | Dec-23 | Mar-24 | Jun-24 | Sep-24 | Dec-24 | Mar-25 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| BANK RATE | 0.25 | 0.50 | 0.50 | 0.50 | 0.75 | 0.75 | 0.75 | 0.75 | 1.00 | 1.00 | 1.00 | 1.00 | 1.25 |
| 3 month ave earnings | 0.30 | 0.50 | 0.50 | 0.60 | 0.70 | 0.80 | 0.90 | 0.90 | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 |
| 6 month ave earnings | 0.50 | 0.60 | 0.60 | 0.70 | 0.80 | 0.90 | 1.00 | 1.00 | 1.10 | 1.10 | 1.10 | 1.10 | 1.10 |
| 12 month ave earnings | 0.70 | 0.70 | 0.70 | 0.80 | 0.90 | 1.00 | 1.10 | 1.10 | 1.20 | 1.20 | 1.20 | 1.20 | 1.20 |
| 5 yr PWLB | 1.50 | 1.50 | 1.60 | 1.60 | 1.70 | 1.80 | 1.80 | 1.80 | 1.90 | 1.90 | 1.90 | 2.00 | 2.00 |
| 10 yr PWLB | 1.70 | 1.80 | 1.80 | 1.90 | 1.90 | 2.00 | 2.00 | 2.00 | 2.10 | 2.10 | 2.10 | 2.20 | 2.30 |
| 25 yr PWLB | 1.90 | 2.00 | 2.10 | 2.10 | 2.20 | 2.20 | 2.20 | 2.30 | 2.30 | 2.40 | 2.40 | 2.50 | 2.50 |
| 50 yr PWLB | 1.70 | 1.80 | 1.90 | 1.90 | 2.00 | 2.00 | 2.00 | 2.10 | 2.10 | 2.20 | 2.20 | 2.30 | 2.30 |
| Bank Rate | | | | | | | | | | | | | |
| Link | 0.25 | 0.50 | 0.50 | 0.50 | 0.75 | 0.75 | 0.75 | 0.75 | 1.00 | 1.00 | 1.00 | 1.00 | 1.25 |
| Capital Economics | 0.50 | 0.75 | 0.75 | 1.00 | 1.25 | 1.25 | 1.25 | 1.25 | - | - | - | - | - |
| 5yr PWLB Rate | | | | | | | | | | | | | |
| Link | 1.50 | 1.50 | 1.60 | 1.60 | 1.70 | 1.80 | 1.80 | 1.80 | 1.90 | 1.90 | 1.90 | 2.00 | 2.00 |
| Capital Economics | 1.80 | 1.90 | 2.10 | 2.20 | 2.20 | 2.30 | 2.40 | 2.40 | - | - | - | - | - |
| 10yr PWLB Rate | | | | | | | | | | | | | |
| Link | 1.70 | 1.80 | 1.80 | 1.90 | 1.90 | 2.00 | 2.00 | 2.00 | 2.10 | 2.10 | 2.10 | 2.20 | 2.30 |
| Capital Economics | 2.00 | 2.10 | 2.20 | 2.30 | 2.30 | 2.40 | 2.50 | 2.50 | - | - | - | - | - |
| 25yr PWLB Rate | | | | | | | | | | | | | |
| Link | 1.90 | 2.00 | 2.10 | 2.10 | 2.20 | 2.20 | 2.20 | 2.30 | 2.30 | 2.40 | 2.40 | 2.50 | 2.50 |
| Capital Economics | 2.20 | 2.30 | 2.50 | 2.70 | 2.70 | 2.70 | 2.80 | 2.90 | - | - | - | - | - |
| 50yr PWLB Rate | | | | | | | | | | | | | |
| Link | 1.70 | 1.80 | 1.90 | 1.90 | 2.00 | 2.00 | 2.00 | 2.10 | 2.10 | 2.20 | 2.20 | 2.30 | 2.30 |
| Capital Economics | 1.90 | 2.00 | 2.20 | 2.40 | 2.50 | 2.60 | 2.70 | 2.90 | - | - | - | - | - |

## 6.2 ECONOMIC BACKGROUND

### COVID-19 vaccines.

These were the game changer during 2021 which raised high hopes that life in the UK would be able to largely return to normal in the second half of the year. However, the bursting onto the scene of the Omicron mutation at the end of November, rendered the initial two doses of all vaccines largely ineffective in preventing infection. This has dashed such hopes and raises the spectre again that a fourth wave of the virus could overwhelm hospitals in early 2022. What we now know is that this mutation is very fast spreading with the potential for total case numbers to double every two to three days, although it possibly may not cause so much severe illness as previous mutations. Rather than go for full lockdowns which heavily damage the economy, the government strategy this time is focusing on getting as many people as possible to have a third (booster) vaccination after three months from the previous last injection, as a booster has been shown to restore a high percentage of immunity to Omicron to those who have had two vaccinations. There is now a race on between how quickly boosters can be given to limit the spread of Omicron, and how quickly will hospitals fill up and potentially be unable to cope. In the meantime, workers have been requested to work from home and restrictions have been placed on large indoor gatherings and hospitality venues. With the household saving rate having been exceptionally high since the first lockdown in March 2020, there is plenty of pent-up demand and purchasing power stored up for services in sectors like restaurants, travel, tourism and hotels which had been hit hard during 2021, but could now be hit hard again by either, or both, of government restrictions and/or consumer reluctance to leave home. Growth will also be lower due to people being ill and not working, similar to the pingdemic in July. The economy, therefore, faces significant headwinds although some sectors have learned how to cope well with Covid. However, the biggest impact on growth would come from another lockdown if that happened. The big question still remains as to whether any further mutations of this virus could develop which render all current vaccines ineffective, as opposed to how quickly vaccines can be modified to deal with them and enhanced testing programmes be implemented to contain their spread until tweaked vaccines become widely available.

**A SUMMARY OVERVIEW OF THE FUTURE PATH OF BANK RATE**

- In December, the Bank of England became the first major western central bank to put interest rates up in this upswing in the current business cycle in western economies as recovery progresses from the Covid recession of 2020.
- The next increase in Bank Rate could be in February or May, dependent on how severe an impact there is from Omicron.
- If there are lockdowns in January, this could pose a barrier for the MPC to putting Bank Rate up again as early as 3rd February.
- With inflation expected to peak at around 6% in April, the MPC may want to be seen to be active in taking action to counter inflation on 5th May, the release date for its Quarterly Monetary Policy Report.
- The December 2021 MPC meeting was more concerned with combating inflation over the medium term than supporting economic growth in the short term.
- Bank Rate increases beyond May are difficult to forecast as inflation is likely to drop sharply in the second half of 2022.
- However, the MPC will want to normalise Bank Rate over the next three years so that it has its main monetary policy tool ready to use in time for the next down-turn; all rates under 2% are providing stimulus to economic growth.
- We have put year end 0.25% increases into Q1 of each financial year from 2023 to recognise this upward bias in Bank Rate - but the actual timing in each year is difficult to predict.
- Covid remains a major potential downside threat in all three years as we ARE likely to get further mutations.
- How quickly can science come up with a mutation proof vaccine, or other treatment, – and for them to be widely administered around the world?
- Purchases of gilts under QE ended in December.  Note that when Bank Rate reaches 0.50%, the MPC has said it will start running down its stock of QE.

**MPC MEETING 16H DECEMBER 2021**

- The Monetary Policy Committee (MPC) voted 8-1 to raise Bank Rate by 0.15% from 0.10% to 0.25% and unanimously decided to make no changes to its programme of quantitative easing purchases due to finish in December 2021 at a total of £895bn.

- The MPC disappointed financial markets by not raising Bank Rate at its November meeting. Until Omicron burst on the scene, most forecasters, therefore, viewed a Bank Rate increase as being near certain at this December meeting due to the way that inflationary pressures have been comprehensively building in both producer and consumer prices, and in wage rates. However, at the November meeting, the MPC decided it wanted to have assurance that the labour market would get over the end of the furlough scheme on 30th September without unemployment increasing sharply; their decision was, therefore, to wait until statistics were available to show how the economy had fared at this time.

- **On 10th December we learnt of the disappointing 0.1% m/m rise in GDP** in October which suggested that economic growth had already slowed to a crawl even before the Omicron variant was discovered in late November. Early evidence suggests growth in November might have been marginally better. Nonetheless, at such low rates of growth, the government's "Plan B" COVID-19 restrictions could cause the economy to contract in December.

- **On 14th December, the labour market statistics** for the three months to October and the single month of October were released. The fallout after the furlough scheme was smaller and shorter than the Bank of England had feared. The single-month data were more informative and showed that LFS employment fell by 240,000, unemployment increased by 75,000 and the unemployment rate rose from 3.9% in September to 4.2%. However, the weekly data suggested this didn't last long as unemployment was falling again by the end of October. What's more, the 49,700 fall in the claimant count and the 257,000 rise in the PAYE measure of company payrolls suggests that the labour market strengthened again in November. The other side of the coin was a further rise in the number of vacancies from 1.182m to a record 1.219m in the three months to November which suggests that the supply of labour is struggling to keep up with demand, although the single-month figure for November fell for the first time since February, from 1.307m to 1.227m.

- These figures by themselves, would probably have been enough to give the MPC the assurance that it could press ahead to raise Bank Rate at this December meeting. However, the advent of Omicron potentially threw a spanner into the works as it poses a major headwind to the economy which, of itself, will help to cool the economy. The financial markets, therefore, swung round to expecting no change in Bank Rate.

- **On 15th December we had the CPI inflation** figure for November which spiked up further from 4.2% to 5.1%, confirming again how inflationary pressures have been building sharply. However, Omicron also caused a sharp fall in world oil and other commodity prices; (gas and electricity inflation has generally accounted on average for about 60% of the increase in inflation in advanced western economies).

- **Other elements of inflation are also transitory** e.g., prices of goods being forced up by supply shortages, and shortages of shipping containers due to ports being clogged have caused huge increases in shipping costs. But these issues are likely to clear during 2022, and then prices will subside back to more normal levels. Gas prices and electricity prices will also fall back once winter is passed and demand for these falls away.

- Although it is possible that the Government could step in with some **fiscal support for the economy**, the huge cost of such support to date is likely to pose a barrier to incurring further major economy wide expenditure unless it is very limited and targeted on narrow sectors like hospitality, (as announced just before Christmas). The Government may well, therefore, effectively leave it to the MPC, and to monetary policy, to support economic growth – but at a time when the threat posed by rising inflation is near to peaking!

- This is the adverse set of factors against which the MPC had to decide on Bank Rate. For the second month in a row, the MPC blind-sided financial markets, this time with a **surprise increase in Bank Rate from 0.10% to 0.25%.** What's more, the hawkish tone of comments indicated that the MPC is now concerned that inflationary pressures are indeed building and need concerted action by the MPC to counter. This indicates that there will be more increases to come with financial markets predicting 1% by the end of 2022. The 8-1 vote to raise the rate shows that there is firm agreement that inflation now poses a threat, especially after the CPI figure hit a 10-year high this week. The MPC commented that "there has been significant upside news" and that "there were some signs of greater persistence in domestic costs and price pressures".

- On the other hand, it did also comment that **"the Omicron variant is likely to weigh on near-term activity".** But it stressed that at the November meeting it had said it would raise rates if the economy evolved as it expected and that now "these conditions had been met". It also appeared more worried about the possible boost to inflation form Omicron itself. It said that "the current position of the global and UK economies was materially different compared with prior to the onset of the pandemic, including elevated levels of consumer price inflation". It also noted the possibility that renewed social distancing would boost demand for goods again, (as demand for services would fall), meaning "global price pressures might persist for longer". (Recent news is that the largest port in the world in China has come down with an Omicron outbreak which is not only affecting the port but also factories in the region.)

- On top of that, there were no references this month to inflation being expected to be below the **2% target in two years' time,** which at November's meeting the MPC referenced to suggest the markets had gone too far in expecting interest rates to rise to over 1.00% by the end of the year.

- These comments indicate that there has been a material reappraisal by the MPC of the inflationary pressures since their last meeting and the Bank also increased its forecast for inflation to peak at 6% next April, rather than at 5% as of a month ago. However, as the Bank retained its guidance that only **a "modest tightening"** in policy will be required, it cannot be thinking that it will need to increase interest rates that much more. A typical policy tightening cycle has usually involved rates rising by 0.25% four times in a year. "Modest" seems slower than that. As such, the Bank could be thinking about raising interest rates two or three times next year to 0.75% or 1.00%.

- In as much as a considerable part of the inflationary pressures at the current time are indeed **transitory,** and will naturally subside, and since economic growth is likely to be weak over the next few months, this would appear to indicate that this tightening cycle is likely to be comparatively short.

- As for the timing of the next increase in Bank Rate, the MPC dropped the comment from November's statement that Bank Rate would be raised "in the coming months". That may imply another rise is unlikely at the next meeting in February and that May is more likely. However, much could depend on how adversely, or not, the economy is affected by Omicron in the run up to the next meeting on 3rd February. Once 0.50% is reached, the Bank would act to start shrinking its stock of QE, (gilts purchased by the Bank would not be replaced when they mature).

- **The MPC's forward guidance on its intended monetary policy** on raising Bank Rate versus selling (quantitative easing) holdings of bonds is as follows: -

- Raising Bank Rate as "the active instrument in most circumstances".
- Raising Bank Rate to 0.50% before starting on reducing its holdings.
- Once Bank Rate is at 0.50% it would stop reinvesting maturing gilts.
- Once Bank Rate had risen to at least 1%, it would start selling its holdings.

- **US.** Shortages of goods and intermediate goods like semi-conductors, have been fuelling increases in prices and reducing economic growth potential. In November, **CPI inflation hit a near 40-year record level of 6.8%** but with energy prices then falling sharply, this is probably the peak. The biggest problem for the Fed is the mounting evidence of a strong pick-up in cyclical price pressures e.g., in rent which has hit a decades high.
- **Shortages of labour** have also been driving up wage rates sharply; this also poses a considerable threat to feeding back into producer prices and then into consumer prices inflation. It now also appears that there has been a sustained drop in the labour force which suggests the pandemic has had a longer-term scarring effect in reducing potential GDP. Economic growth may therefore be reduced to between 2 and 3% in 2022 and 2023 while core inflation is likely to remain elevated at around 3% in both years instead of declining back to the Fed's 2% central target.
- Inflation hitting 6.8% and the feed through into second round effects, meant that it was near certain that the **Fed's meeting of 15th December** would take aggressive action against inflation. Accordingly, the rate of tapering of monthly $120bn QE purchases announced at its November 3rd meeting. was doubled so that all purchases would now finish in February 2022. In addition, Fed officials had started discussions on running down the stock of QE held by the Fed. Fed officials also expected three rate rises in 2022 of 0.25% from near zero currently, followed by three in 2023 and two in 2024, taking rates back above 2% to a neutral level for monetary policy. The first increase could come as soon as March 2022 as the chairman of the Fed stated his view that the economy had made rapid progress to achieving the other goal of the Fed – "maximum employment". The Fed forecast that inflation would fall from an average of 5.3% in 2021 to 2.6% in 2023, still above its target of 2% and both figures significantly up from previous forecasts. What was also significant was that this month the Fed dropped its description of the current level of inflation as being "transitory" and instead referred to "elevated levels" of inflation: the statement also dropped most of the language around the flexible average inflation target, with inflation now described as having exceeded 2 percent "for some time". It did not see Omicron as being a major impediment to the need to take action now to curtail the level of inflationary pressures that have built up, although Fed officials did note that it has the potential to exacerbate supply chain problems and add to price pressures.
  *See also comments in paragraph 3.3 under PWLB rates and gilt yields.*

- **EU.** The slow role out of vaccines initially delayed **economic recovery** in early 2021 but the vaccination rate then picked up sharply. After a contraction of -0.3% in Q1, Q2 came in with strong growth of 2%. With Q3 at 2.2%, the EU recovery was then within 0.5% of its pre Covid size. However, the arrival of Omicron is now a major headwind to growth in quarter 4 and the expected downturn into weak growth could well turn negative, with the outlook for the first two months of 2022 expected to continue to be very weak.
- **November's inflation figures** breakdown shows that the increase in price pressures is not just due to high energy costs and global demand-supply imbalances for durable goods as services inflation also rose. Headline inflation reached 4.9% in November, with over half of that due to energy. However, oil and gas prices are expected to fall after the winter and so energy inflation is expected to plummet in 2022. Core goods inflation rose to 2.4% in November, its second highest ever level, and is likely to remain high for some time as it will take a long time for the inflationary impact of global imbalances in the demand and supply of durable goods to disappear. Price pressures also increased in the services sector, but wage growth remains subdued and there are no signs of a trend of faster wage growth which might lead to *persistently* higher services inflation - which would get the ECB

concerned. The upshot is that the euro-zone is set for a prolonged period of inflation being above the ECB's target of 2% and it is likely to average 3% in 2022, in line with the ECB's latest projection.

- **ECB tapering.** The ECB has joined with the Fed by also announcing at its meeting on 16th December that it will be reducing its QE purchases - by half from October 2022, i.e., it will still be providing significant stimulus via QE purchases for over half of next year. However, as inflation will fall back sharply during 2022, it is likely that it will leave its central rate below zero, (currently -0.50%), over the next two years. The main struggle that the ECB has had in recent years is that inflation has been doggedly anaemic in sticking below the ECB's target rate despite all its major programmes of monetary easing by cutting rates into negative territory and providing QE support.
- The ECB will now also need to consider the impact of **Omicron** on the economy, and it stated at its December meeting that it is prepared to provide further QE support if the pandemic causes bond yield spreads of peripheral countries, (compared to the yields of northern EU countries), to rise. However, that is the only reason it will support peripheral yields, so this support is limited in its scope.
- The EU has entered into a **period of political uncertainty** where a new German government formed of a coalition of three parties with Olaf Scholz replacing Angela Merkel as Chancellor in December 2021, will need to find its feet both within the EU and in the three parties successfully working together. In France there is a presidential election coming up in April 2022 followed by the legislative election in June. In addition, Italy needs to elect a new president in January with Prime Minister Draghi being a favourite due to having suitable gravitas for this post. However, if he switched office, there is a significant risk that the current government coalition could collapse. That could then cause differentials between Italian and German bonds to widen when 2022 will also see a gradual running down of ECB support for the bonds of weaker countries within the EU. These political uncertainties could have repercussions on economies and on Brexit issues.

- **CHINA.** After a concerted effort to get on top of the virus outbreak in Q1 2020, economic recovery was strong in the rest of **2020**; this enabled China to recover all the initial contraction. During 2020, policy makers both quashed the virus and implemented a programme of monetary and fiscal support that was particularly effective at stimulating short-term growth. At the same time, China's economy benefited from the shift towards online spending by consumers in developed markets. These factors helped to explain its comparative outperformance compared to western economies during 2020 and earlier in 2021.
- However, the pace of economic growth has now fallen back in **2021** after this initial surge of recovery from the pandemic and looks likely to be particularly weak in 2022. China has been struggling to contain the spread of the Delta variant through using sharp local lockdowns - which depress economic growth. Chinese consumers are also being very wary about leaving home and so spending money on services. However, with Omicron having now spread to China, and being much more easily transmissible, this strategy of sharp local lockdowns to stop the virus may not prove so successful in future. In addition, the current pace of providing boosters at 100 billion per month will leave much of the 1.4 billion population exposed to Omicron, and any further mutations, for a considerable time. The **People's Bank of China** made a start in December 2021 on cutting its key interest rate marginally so as to stimulate economic growth. However, after credit has already expanded by around 25% in just the last two years, it will probably leave the heavy lifting in supporting growth to fiscal stimulus by central and local government.
- Supply shortages, especially of coal for power generation, were causing widespread power cuts to industry during the second half of 2021 and so a sharp disruptive impact on some sectors of the economy. In addition, recent regulatory actions motivated by a political agenda to channel activities into officially approved directions, are also likely to reduce the dynamism and long-term growth of the Chinese economy.

- **JAPAN.** 2021 has been a patchy year in combating Covid. However, recent business surveys indicate that the economy has been rebounding rapidly in 2021 once the bulk of the population had been double vaccinated and new virus cases had plunged. However, Omicron could reverse this initial success in combating Covid.
- The Bank of Japan is continuing its **very loose monetary policy** but with little prospect of getting inflation back above 1% towards its target of 2%, any time soon: indeed, inflation was actually negative in July. New Prime Minister Kishida, having won the November general election, brought in a supplementary budget to boost growth, but it is unlikely to have a major effect.

- **WORLD GROWTH.** World growth was in recession in 2020 but recovered during 2021 until starting to lose momentum in the second half of the year, though overall growth for the year is expected to be about 6% and to be around 4-5% in 2022. Inflation has been rising due to increases in gas and electricity prices, shipping costs and supply shortages, although these should subside during 2022. While headline inflation will fall sharply, core inflation will probably not fall as quickly as central bankers would hope. It is 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, and vice versa. This is likely to reduce world growth rates from those in prior decades.

- **SUPPLY SHORTAGES**. The pandemic and extreme weather events, followed by a major surge in demand after lockdowns ended, have been highly disruptive of extended worldwide supply chains. Major queues of ships unable to unload their goods at ports in New York, California and China built up rapidly during quarters 2 and 3 of 2021 but then halved during quarter 4. Such issues have led to a misdistribution of shipping containers around the world and have contributed to a huge increase in the cost of shipping. Combined with a shortage of semi-conductors, these issues have had a disruptive impact on production in many countries. The latest additional disruption has been a shortage of coal in China leading to power cuts focused primarily on producers (rather than consumers), i.e., this will further aggravate shortages in meeting demand for goods. Many western countries are also hitting up against a difficulty in filling job vacancies. It is expected that these issues will be gradually sorted out, but they are currently contributing to a spike upwards in inflation and shortages of materials and goods available to purchase.

## 6.3 TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT OPTION 1

**SPECIFIED INVESTMENTS:** All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' quality criteria where applicable.

**NON-SPECIFIED INVESTMENTS**: These are any investments which do not meet the specified investment criteria. A maximum of 100% 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** | N/A | **100%** | **6 months** |
| UK Government gilts | UK sovereign rating | 50% | 12 months |
| UK Government Treasury bills | UK sovereign rating | 50% | 12 months |
| Bonds issued by multilateral development banks | AAA (or state your criteria if different) | 50% | 6 months |
| Money Market Funds (CNAV, LNAV and VNAV) | AAA | 100% | 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 | N/A | 100% | 12 months |
| Gloucestershire Airport | N/A | £7.25m | |
| Rokeby Merchant | N/A | £0.6m | |
| Ladybellegate Estates | N/A | £1.8m | |
| Gloucestershire Wildlife Trust | N/A | £0.55m | |

| | | | |
|---|---|---|---|
| Cheltenham YMCA | N/A | £1.5m | 31 years |
| Term deposits with banks and building societies | Blue<br>Orange<br>Red<br>Green<br>No Colour | £10m<br>£10m<br>£10m<br>£10m<br>£0 | 12 months<br>12 months<br>6 months<br>100 days<br>Not for use |
| CDs or corporate bonds with banks and building societies | Blue<br>Orange<br>Red<br>Green<br>No Colour | £1m<br>£1m<br>£1m<br>£1m<br>£0 | 12 months<br>12 months<br>6 months<br>100 days<br>Not for use |
| Gilt funds | UK sovereign rating | Nil | |
| CCLA Property/DIF Funds | | £15m | 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.

### 6.4 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.**

## 6.5 TREASURY MANAGEMENT SCHEME OF DELEGATION

**(i) Council**

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.

**(ii) Audit and Governance Committee**

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
- budget consideration and approval;
- approval of the division of responsibilities;
- receiving and reviewing regular monitoring reports and acting on recommendations;
- approving the selection of external service providers and agreeing terms of appointment.

**(iii) Body/person(s) with responsibility for scrutiny**

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

## 6.6 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 (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios;*
    - *Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments;*
    - *Decision making, governance and organisation (TMP5 and schedules), 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 (TMP6 and schedules), including where and how often monitoring reports are taken;*
    - Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.

Gloucester City Council

| | | | |
|---|---|---|---|
| **Meeting:** | **Audit & Governance Committee<br>Cabinet<br>Council** | **Date:** | **7 March 2022<br>9 March<br>24 March 2022** |
| **Subject:** | **Capital Strategy 2022/23** | | |
| **Report Of:** | **Cabinet Member for Performance and Resources** | | |
| **Wards Affected:** | **All** | | |
| **Key Decision:** | **No** | **Budget/Policy Framework:** | **Yes** |
| **Contact Officer:** | **Jon Topping, Director of Policy and Resources** | | |
| | **Email: jon.topping@gloucester.gov.uk** | **Tel: 396242** | |
| **Appendices:** | **1. Capital Strategy 2022/23** | | |

## 1.0 Purpose of Report

1.1 To formally recommend that Council approves the attached Capital Strategy.

## 2.0 Recommendations

2.1 Audit and Governance Committee is asked to **RECOMMEND** that the Capital Strategy be approved.

2.2 Council is asked to **RESOLVE** that:

(1) The Capital Strategy at Appendix 1 be approved;

## 3.0 Background and Key Issues

3.1 The Capital Strategy focuses on core principles that underpin the Council's five year capital programme, providing a position statement of progress (capital expenditure) and the resources available (funding). The Strategy projects the Capital programme while setting out how the programme will be achieved focusing on key issues and risks that will impact on the delivery of the Capital strategy and the governance framework required to ensure the Strategy is delivered.

3.2 The Strategy maintains a strong and current link to the Council's priorities and to its key strategy documents, notably the Treasury Management Strategy, Asset Management Strategy, Property Investment Strategy, Medium Term Financial Plan and the Corporate Plan.

**4.0 Alternative Options Considered**

4.1 The Capital Strategy is a requirement of the CIPFA Prudential Code, no alternatives considered as this is a code requirement.

**5.0 Reasons for Recommendations**

5.1 Capital Strategy is a requirement of the CIPFA Prudential Code.

**6.0 Future Work and Conclusions**

6.1 The Capital Strategy will be monitored and reviewed annually.

**7.0 Financial Implications**

7.1 There are no direct financial implications arising from this report. The Capital Strategy provides a position statement with regards to capital expenditure and the resources available in terms of funding.

**8.0 Social Value Considerations**

8.1 This report notes the Capital Strategy of the Council. This is a requirement of the CIPFA Prudential Code – ESG requirements are included within the Code.

**9.0 Legal Implications**

9.1 The Council is required to have a Capital Strategy to meet the requirements of the Local Government Act 2003, Localism Act 2011, Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2020, the CIPFA Prudential Code, DLUHC Minimum Revenue Provision Guidance, the CIPFA Treasury Management Code and DLUHC Investment Guidance.

**10.0 Risk & Opportunity Management Implications**

10.1 The Council must have reviewed its Capital Strategy by 31st March 2022.

**11.0 People Impact Assessment (PIA):**

11.1 A PIA screening assessment has been undertaken and the impact is neutral. A full PIA is not required.

**12.0 Other Corporate Implications**

Community Safety

12.1 None

Sustainability

12.2 None

Staffing & Trade Union

12.3 None

**Background Documents:** Local Government Act 2003
CIPFA Treasury Management Code
CIPFA Prudential Code
DLUHC MRP Guidance

## Introduction

This capital strategy sets out how Gloucester City Council intend to spend capital to provide services and meet the strategic aims in the Council plan. This strategy gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability. It has been written in an accessible style to enhance members', residents and other stakeholders understanding of these areas.

## Background

The Capital Strategy demonstrates that the authority takes capital investment decisions in line with service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability. The Capital Strategy also sets out the long-term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward and impact on the achievement of priority outcomes. Decisions around capital expenditure, investment and borrowing should align with the processes established for the setting and revising of the budget for the local authority.

The Capital Strategy should also be tailored to the authority's individual circumstances and should include capital expenditure, investments and liabilities and treasury management. For Gloucester, the Treasury Management Strategy drawn up in line with the Treasury Management Code will continue to be published as a separate document and this will remain separate to differentiate between the demand and assessment of capital expenditure and the management of the investment and borrowing portfolio.

CIPFA published the revised codes on Treasury Management and Prudential Code on 20th December 2021. Formal adoption is required from 2023/24 Financial Year. Both the Capital Strategy and Treasury Management Strategy are produced in accordance with the Prudential Code.

## Policy Context

The Council plan 22-24 defines the Council's vision:

**"Building a greener, fairer, better Gloucester"**

The priorities to support this vision are:

1. Building greener, healthier, and more inclusive communities
2. Building a sustainable city of diverse culture and opportunity
3. Building a socially responsible and empowering council

The vision and priorities are underpinned by our core values.

For full details of the Council Plan see: **Council Plan**

The Capital Strategy is an important policy document in delivering the Council's Vision in terms of maintaining and extending the Council's asset base but needs to take a longer-term view to reflect the life cycle of capital assets. The life cycle of capital assets, often known as non-current assets, will range between 5-60 years or even longer if land is acquired. Decisions made now will affect residents, business and other stakeholders for many years to come.

## Capital Expenditure and Financing

Capital expenditure is where the Council spends money on assets, such as property or vehicles, that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £6,000 are not capitalised and are charged to revenue in year.

- For details of the Council's policy on capitalisation, see: Statement of Accounts 2020/21 page 21, Accounting Policies point 19 - Statement of Accounts

In 2022/23, the Council is planning capital expenditure of £27.537 as summarised below:

*Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions*

| | 2020/21 actual | 2021/22 forecast | 2022/23 budget | 2023/24 budget | 2024/25 budget |
|---|---|---|---|---|---|
| General Fund services | 23.909 | 27.537 | 27.537 | 32.790 | 44.949 |
| **TOTAL** | 23.909 | 27.537 | 27.537 | 32.790 | 44.949 |

The capital programme includes a variety of projects from large regeneration to smaller individual projects, the main capital projects are detailed below:

Kings Quarter – The Forum is progressing; Council approved the project in January 2021. The project will see significant investment by the Council in both the physical, economic, and cultural redevelopment of this part of the city. The plans include retail, office, hotel and residential areas which will see this part of the City completely redeveloped. The required investment will be £107m and will be a long-term investment of up to 50 years. Significant due diligence has been undertaken with financial, property and legal advisors to confirm the projects long term viability. The development agreement was agreed late 2021 and the main contractor Keir were procured in January 2022 within the required funding envelope. Work has already commenced on phase 1, with an expected completion September 2022, to deliver residential units and relocation of the Tesco store in Grosvenor House.

In 2021 the Council was awarded £20m ‘levelling up’ funding from DLUHC which will support circa £200m of investment in the City. The overall purpose of package is to ‘rocket charge’ the regeneration of the City Centre, hugely increasing footfall, employment, tourists and overall economic growth by bringing back into creative use two empty buildings and a vacant site. The City Centre at present predominantly serves as a centre for local shopping and services. Its localised primary catchment area has high levels of deprivation. The three projects will combine to boost local pride, visibly demonstrate greater activity, and less empty buildings/sites, fill a major gap in tourist and visitor provision, bring Higher Education courses into the City Centre for the first time and provide new secure business facilities for start-ups in growth sectors. This will in turn create much greater footfall and consumer demand and stimulate further investment, as well as an audience for more cultural events planned for Kings Square.

The projects are:
The **Fleece Hotel** located in the heart of historic Gloucester, is a derelict Grade I and II Listed building. The funding will enable Phase 1 (2,170 sqm) of a high-quality mixed-use scheme to be developed.

The **UoG** has acquired the vacant iconic former Debenhams building, which is the first time a University has done this, to create a new City Campus for teaching, learning and community partnerships in the City Centre. The LUF bid will also enable an important public role in the UoG building by creating a drop in Well Being Centre, a new digitally enabled public library and information centre.

The **Forge Digital Innovation and Incubation Centre** will provide 2,430 sqm of accommodation and support for high value added SME businesses. It will form part of the wider mixed-use Forum development which will provide a vibrant and active destination in an important gateway adjacent to the City Centre bus station and rail interchange, in the Kings Quarter area.

The redevelopment of Kings Square is due for completion in March 2022. This significant project, part of the Councils regeneration plans will open up the square as a vibrant area for cultural and leisure within the City.

The Council continues to upgrade the Kings Walk site. Anchor tenant Primark has recently taken ownership of their store, this has redesigned the outside of the centre. Future work will see improvements to the Eastgate facias as well as improvements to the Mall. This will include work on the Clarence Street and Kings Square entrances. The Council anticipates initially borrowing to facilitate this project, with borrowing costs being met by the forecast income.

Work with partners is ongoing as part of the wider regeneration plans. Redevelopment of the Railway Station will ultimately see it link to the Transport Hub and City Centre supporting the Kings Quarter regeneration. The redevelop work is ongoing with the project funded via the LEP.

Food Dock is due for completion August 2022 bringing additional regeneration to the Docks within the City. The Council arranged additional funding to Ladybellgate Estates to facilitate the redevelopment of the Food Dock, this will bring economic benefits to the City Centre.

Housing Projects – The purchase of St Oswald's and approval of revised Housing Strategy will bring a number of housing projects forward.  As these projects are developed any required investment for delivery will be analysed to seek affordable solutions.

**Governance**: The Major Projects Steering group and/or the Property Investment Board review significant projects for inclusion within the Council's capital programme. Projects are collated by finance who calculate the financing cost (which can be nil if the project is fully externally financed). The groups appraise all bids based on a comparison of service priorities against financing costs and makes recommendations for the capital programme. The final capital programme is then presented to Cabinet and Council in February each year.

- For full details of the Council's capital programme see: Money Plan

All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council'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:

*Table 2: Capital financing in £ millions*

| | 2020/21 actual | 2021/22 forecast | 2022/23 budget | 2023/24 budget | 2024/25 budget |
|---|---|---|---|---|---|
| External sources | 4.935 | 3.853 | 3.893 | 2.260 | 0.275 |
| Own resources | 0.467 | 2.000 | 0.444 | 0.330 | 0.474 |
| Debt | 1.441 | 18.056 | 23.200 | 0.000 | 00.000 |
| **TOTAL** | **23.909** | **27.537** | **27.537** | **30.200** | **44.200** |

Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as minimum revenue provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP and use of capital receipts are as follows:

*Table 3: Replacement of debt finance in £ millions*

| | 2020/21 actual | 2021/22 forecast | 2022/23 budget | 2023/24 budget | 2024/25 budget |
|---|---|---|---|---|---|

| | | | | | |
|---|---|---|---|---|---|
| Own resources | 0.870 | 2.035 | 2.301 | 2.350 | 2.377 |

- The Council's full minimum revenue provision statement is available here: Treasury Management Strategy - MRP

The Council'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 CFR is expected to increase by £20.899m during 22/23. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

*Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions*

| | 31.3.2021 actual | 31.3.2022 forecast | 31.3.2023 budget | 31.3.2024 budget | 31.3.2025 budget |
|---|---|---|---|---|---|
| General Fund services | 118.949 | 134.970 | 155.869 | 183.719 | 225.542 |
| **TOTAL CFR** | **118.949** | **134.970** | **155.869** | **183.719** | **225.542** |

**Asset management:** To ensure that capital assets continue to be of long-term use, the Council has an asset management strategy in place. Gloucester City Council has a diverse estate from ancient monuments to commercial property. The asset management strategy details our approach to managing our diverse assets including our acquisitions and disposals, planned maintenance, governance and performance.

- The Council's asset management strategy can be read here: Asset Management Strategy

**Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Council is currently also permitted to spend capital receipts on service transformation projects until 2023/24. Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive £4.5m of capital receipts in the coming financial year as follows:

*Table 5: Capital receipts in £ millions*

| | 2020/21 actual | 2021/22 forecast | 2022/23 budget | 2023/24 budget | 2024/25 budget |
|---|---|---|---|---|---|
| Asset sales | 0.192 | 0.990 | 4.500 | 1.000 | 0.500 |
| Loans repaid | 0.000 | 0.000 | 0.000 | 0.000 | 0.000 |
| **TOTAL** | **0.192** | **0.990** | **4.500** | **1.000** | **0.500** |

- The Council's Flexible Use of Capital Receipts Policy is available here: Flexible Use of Capital Receipts Policy

## Treasury Management

Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

**Borrowing strategy:** The Council's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at around 0.10%) and long-term fixed rate loans where the future cost is known but higher (currently 1.25 to 1.68%).

Projected levels of the Council's total outstanding debt (which comprises borrowing, PFI liabilities, leases are shown below, compared with the capital financing requirement (see above).

*Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions*

| | 31.3.2021 actual | 31.3.2022 forecast | 31.3.2023 budget | 31.3.2024 budget | 31.3.2025 budget |
|---|---|---|---|---|---|
| Debt (incl. PFI & leases) | 129.586 | 138.004 | 155.376 | 182.726 | 224.049 |
| Capital Financing Requirement | 118.949 | 134.970 | 155.869 | 183.719 | 225.542 |

Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the Council expects to comply with this in the medium term.

**Affordable borrowing limit:** The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

*Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £m*

| | 2020/21 limit | 2021/22 limit | 2022/23 limit | 2023/24 limit |
|---|---|---|---|---|
| Authorised limit - borrowing | £130 | £230 | £225 | £220 |
| Authorised limit - PFI and leases | £35 | £35 | £35 | £35 |
| Authorised limit - total external debt | £165 | £265 | £260 | £255 |
| Operational boundary - borrowing | £120 | £215 | £210 | £205 |
| Operational boundary - PFI and leases | £30 | £30 | £30 | £30 |
| Operational boundary - total external debt | £150 | £245 | £240 | £235 |

- Further details on borrowing are in pages 11 to 15 of the treasury management strategy Treasury Management Strategy

**Investment strategy:** Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

The Council's policy on treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.

- Further details on treasury investments are in pages 16 to 21 of the treasury management strategy - Treasury Management Strategy

**Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Head of Policy and Resources and staff, who must act in line with the treasury management strategy approved by Council. Half yearly reports on treasury management activity are presented to Audit and Governance Committee which is responsible for scrutinising treasury management decisions.

## Investments for Service Purposes

The Council makes investments to assist local public services, including making loans to local service providers, businesses to promote economic growth, the Council's subsidiaries that provide services. In light of the public service objective, the Council is willing to take more risk than with treasury investments, however it still plans for such investments to generate a profit after all costs.

**Governance:** Decisions on service investments are made by the relevant service manager in consultation with the Head of policy and Resources and must meet the criteria and limits laid down in the investment strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme.

## Liabilities

In addition to debt of £129.586m detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £58.366m). It has also set aside £1.6m to cover risks of provisions, this mainly relates to NNDR appeals, where the

Council has estimated the costs arising from appeals by ratepayers. The Council did not have any contingent liabilities in 2020/21.

**Governance:** Decisions on incurring new discretional liabilities are taken by service managers in consultation with head of Policy and Resources. The risk of liabilities crystallising and requiring payment is monitored by finance.

- Further details on provisions (page 50), liabilities and guarantees are on page 65 of the 2020/21 statement of accounts - Statement of Accounts

## Revenue Budget Implications

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 Council Tax, business rates and general government grants.

*Table 9: Prudential Indicator: Proportion of financing costs to net revenue stream*

| | 2020/21 actual | 2021/22 forecast | 2022/23 budget | 2023/24 budget | 2024/25 budget |
|---|---|---|---|---|---|
| Financing costs (£m) | 0.870 | 2.035 | 2.301 | 2.350 | 2.377 |
| Proportion of net revenue stream | 14.64% | 28.02% | 28.76% | 29.28% | 29.34% |

- Further details on the revenue implications of capital expenditure are noted within the 2022/23 revenue budget - Money Plan

**Sustainability:** Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The Head of Policy and Resources is satisfied that the proposed capital programme is prudent, affordable and sustainable.

## Knowledge and Skills

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Director of Policy and Resources is a qualified accountant with 25 years' experience, the Financial Services and Accountancy Managers are both qualified accountants with 15 and 25 years' experience. The Council pays for junior staff to study towards relevant professional qualifications including CIPFA, ACT (treasury) and CIMA.

Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Link Group as treasury management advisers, the Council employs property consultants on a case by case basis. This approach is more cost effective than employing such staff directly and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

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# Gloucester City Council

## Audit and Governance Committee Work Programme 2021-22

## Updated 24 January 2022

| Item | Format | Committees | Lead Officer | Notes |
|---|---|---|---|---|
| **7th March 2022** | | | | |
| 1. Appointment of independent Member | Written Report | Audit and Gov | Head of Policy and Resources | Part of the Committee's annual programme of work |
| 2. Annual Risk Management Report 2021/22 and Strategic Risk Register | Written Report | Audit and Gov | Head of IA&RM Shared Service | Part of the Committee's annual programme of work<br><br>**JULY!!!** |
| 3. Internal Audit Activity 2021-22 Progress Report | Written Report | Audit and Gov | Head of IA&RM Shared Service | Part of the Committee's annual programme of work |
| 4. Internal Audit Plan 2022-23 | Written Report | Audit and Gov | Head of IA&RM Shared Service | Part of the Committee's annual programme of work |
| 5. Annual Report of the Audit and Governance Committee | Written Report | Audit and Gov<br><br>Council | Head of IA&RM Shared Service | Part of the Committee's annual programme of work |
| 6. Audit and Governance Committee Work Programme | Timetable | - | - | - |
| **18th July 2022** | | | | |

| | | | | |
|---|---|---|---|---|
| 1. Appointment of independent Member | Written Report | Audit and Gov | Director of Policy and Resources | Part of the Committee's annual programme of work |
| 2. Annual Risk Management Report 2021/22 and Strategic Risk Register | Written Report | Audit and Gov | Head of ARA Shared Service | Part of the Committee's annual programme of work |
| 3. Annual Report of the Audit and Governance Committee | Written Report | Audit and Gov<br><br>Council | Head of ARA Shared Service | Part of the Committee's annual programme of work |
| 4. Annual Report on Internal Audit Activity 2021/22 | Written Report | Audit and Gov | Head of ARA Shared Service | Part of the Committee's annual programme of work |
| 5. Treasury Management Annual Report 2021/22 | Written Report | Audit and Gov | Director of Policy and Resources | Part of the Committee's annual programme of work |
| 6. Audit and Governance Committee Work Programme | -- | -- | -- | Standing item |