APPENDIX A

OFFICE OF THE POLICE AND CRIME COMMISSIONER FOR GWENT

Treasury Management Strategy 2021/22 to 2023/24

1 INTRODUCTION

1.1 Treasury Management is the management of cash flows, banking, money market and capital market transactions; the management of the associated risks, and the pursuit of the optimum performance or return consistent with those risks. The treasury management service is an important part of the overall financial management of the Police and Crime Commissioner's (Commissioner) affairs. The Commissioner 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 Commissioner'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 Commissioner's capital plans. These capital plans provide a guide to the borrowing need of the Commissioner, essentially the longer term cash flow planning to ensure that the Commissioner can meet his 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, any debt previously drawn may be restructured to meet the Commissioner's risk or cost objectives.

1.2 The Commissioner's treasury activities are strictly regulated by statutory requirements and a professional code of practice, the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management. Under the Code, the Commissioner is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

1.3 The Prudential Code 2017 introduced a new requirement for local authorities (including Commissioners) to produce an annual capital strategy. It is for local authorities to decide whether to include their treasury management strategy and annual investment strategy as part of a capital strategy or to complete separately. In the first year of operation, the Commissioner has elected to complete a separate capital strategy which was completed at the conclusion of the budget setting process in February 2020 and approved before the commencement of the 2020/21 financial year.

1.4 The adoption of a Treasury Management Strategy for 2021/22, prior to the start of the financial year, is the first of the three reporting requirements in respect of that year. This will be followed in due course by a mid-year Treasury Management report and an Annual Treasury Report before 30th September 2022, providing a selection of actual prudential and treasury indicators.

1.5 The Treasury Management Strategy for 2021/22 covers two main areas:

Capital Issues

(i) The capital plans and the prudential indicators; and
(ii) The Minimum Revenue Provision (MRP) strategy.

Treasury Management Issues

(i) Debt and investment projections;
(ii) Limits on borrowing activity;
(iii) The expected movement in interest rates;
(iv) Borrowing and investment strategies;
(v) Treasury performance indicators; and
(vi) Specific limits on treasury activities.

2. CAPITAL PRUDENTIAL INDICATORS 2021/22 to 2023/24

2.1 The Local Government Act 2003 requires the Commissioner to adopt the CIPFA Prudential Code, which was updated in 2017, and produce prudential indicators. Each indicator either summarises the expected capital activity or introduces limits upon that activity, and reflects the outcome of the underlying capital appraisal systems. This document updates currently approved indicators.

2.2 Within this overall prudential framework there is an impact on the Commissioner’s treasury management activity, as it will directly impact on borrowing or investment activity.

2.3 Capital Expenditure Plans

2.3.1 The capital expenditure plans are summarised below and this forms the first of the prudential indicators. A certain level of capital expenditure is grant supported by the Government; any decisions by the Commissioner to spend above this level will be considered unsupported capital expenditure.

2.3.2 This unsupported capital expenditure needs to have regard to:

(i) Service objectives (e.g. strategic planning);
(ii) Stewardship of assets (e.g. asset management planning);
(iii) Value for money (e.g. option appraisal);
(iv) Prudence and sustainability (e.g. implications for external borrowing and whole life costing);
(v) Affordability (e.g. implications for the council tax); and
(vi) Practicality (e.g. the achievability of longer term plans).

2.3.3 The revenue consequences of capital expenditure, particularly the supported capital expenditure, will need to be paid for from the Commissioner's own resources.

2.3.4 This capital expenditure can be paid for immediately (by applying capital resources such as capital receipts, capital grants, earmarked reserves (known as committed funds) or revenue resources), but if these resources are insufficient any residual capital expenditure will add to the Commissioner's borrowing need.

2.3.5 A key risk to the plans, are that the level of Government support has been estimated and could therefore be subject to change.

2.3.6 The Commissioner is asked to approve the following summary capital expenditure projections which is the first prudential indicator:

First Prudential Indicator - Estimates of Capital Expenditure					
	2020/21 Original £000's	2020/21 Revised £000's	2021/22 Estimate £000's	2022/23 Estimate £000's	2023/24 Estimate £000's
Capital Expenditure	**28,063**	**22,507**	**18,655**	**16,608**	**26,055**
Financed by:					
Capital Receipts	0	201	500	0	0
Capital Grants and PIF Grants	539	120	120	120	120
Reserves	24,879	12,173	13,399	2,227	0
Revenue	2,645	10,013	4,636	3,641	3,641
Net Financing Need for the Year	**0**	**0**	**0**	**10,620**	**22,294**

2.3.7 The above financing need excludes other long term liabilities, such as Private Finance Initiative (PFI) and leasing arrangements which already include borrowing instruments. The table above identifies the financial requirements for the delivery of the Commissioner's Estate Strategy, which includes the investment in a new Headquarters and the transformation of operational policing presence into a 'Hub and Spoke' model, resulting in a borrowing need from 2022/23 onwards. During 2021/22, the Capital Programme will continue to be funded from a combination of capital grant, revenue contributions to capital, capital receipts and committed funds.

2.4 The Commissioner's Borrowing Need (the Capital Financing Requirement)

2.4.1 The second prudential indicator is the Commissioner's Capital Financing Requirement (CFR) which is simply the total outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is a measure of the Commissioner's underlying borrowing need. Any capital expenditure in the table in paragraph 2.3.6 above which has not immediately been paid for will increase the CFR.

2.4.2 The CFR includes any other long term liabilities (e.g. PFI schemes) brought onto the balance sheet. Whilst this increases the CFR, and therefore the Commissioner's borrowing requirement, these types of scheme include a borrowing facility and so the Commissioner is not required to borrow separately for these schemes. As at 31st March 2020, the Commissioner had no schemes of this type within the CFR.

2.4.3 The Commissioner is asked to approve the CFR projections below:

Second Prudential Indicator - the Capital Financing Requirement (CFR)					
	2020/21 Original £000's	2020/21 Revised £000's	2021/22 Estimate £000's	2022/23 Estimate £000's	2023/24 Estimate £000's
Opening CFR	0	0	0	0	10,619
Capital Spend	28,063	22,507	18,655	16,608	26,055
Movement In finance lease liability	0	0	0	0	0
Resources Used	(28,063)	(22,507)	(18,655)	(5,988)	(3,761)
MRP		0	0	0	(425)
Closing CFR	**0**	**0**	**0**	**10,619**	**32,489**

2.4.4 The table above confirms that the Commissioner will be reliant upon external borrowing during 2022/23, as the combination of capital grant, revenue contributions to capital, capital receipts and committed funds become insufficient to fund the Capital Programme.

2.4.5 The adoption of International Financial Reporting Standard (IFRS) 16 – 'Accounting for Leases' should have commenced at the 1st April 2021, which would have impacted on the calculation of the Commissioner's CFR within this Strategy. However, in late November 2020 as a result of the Coronavirus pandemic, the adoption of this Standard has been delayed for a year and will now take effect from 1st April 2022.

2.4.6 In line with the latest MRP guidance, although the Commissioner will not be required to make a MRP until 2022/23, he will still require a policy on this matter as per section 3 below.

3. MINIMUM REVENUE PROVISION POLICY

3.1 The Commissioner is required to recognise an element of outstanding capital borrowing each year through a revenue charge known as the MRP. The MRP is calculated to match the repayment of borrowing over the life of the assets, for which debt has been raised and is charged the following year after the asset becomes operational. It is also permissible to pay an additional amount known as a Voluntary Revenue Provision (VRP). Under Welsh Government (WG) Regulations the Commissioner has to approve an MRP Statement in advance of each year. The Commissioner is recommended to adopt the following MRP policy for 2021/22:

(i) For all capital expenditure incurred before 1st April 2008 and all supported capital expenditure incurred since that date or in the future, the MRP policy will be 4% of the CFR. This is consistent with the practice in place prior to the current regulations; and

(ii) For all unsupported borrowing since 1st April 2008 and in the future, the asset life method will be used, i.e., the amount borrowed will be divided by the life of the asset.

4. THE USE OF THE COMMISSIONER'S RESOURCES AND INVESTMENT POSITION

4.1 The application of resources (capital receipts, committed funds, etc.) will have an on-going impact on investments. Detailed below are estimates of the year-end balances for each resource and anticipated day to day cash flow balances:

Investment Position - Year end Resources					
	2020/21 Original £000's	2020/21 Revised £000's	2021/22 Estimate £000's	2022/23 Estimate £000's	2023/24 Estimate £000's
Police Fund	4,000	4,750	4,750	4,750	4,750
Earmarked Reserves	14,255	27,982	10,625	7,211	6,624
Provisions	1,497	1,417	1,417	1,417	1,417
Total Core Funds	19,752	34,149	16,792	13,378	12,791
Working Capital	6,220	4,101	4,101	4,101	4,101
Expected Investments	25,972	38,250	20,893	17,479	16,892

*Working capital balances shown are estimated year end; these may be higher mid-year.

5. AFFORDABILITY PRUDENTIAL INDICATORS

5.1 The previous sections cover the overall capital and control of borrowing prudential indicators. Prudential indicators are also required to assess the affordability of the capital investment plans. The Commissioner is asked to approve the third and fourth prudential indicators, which assess affordability in terms of the impact of the capital investment plans on the Commissioner's overall finances.

5.2 The third prudential indicator is the ratio of net financing costs (financing income less finance interest expense) 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:

Third Prudential Indicator - Ratio of Financing Costs to Net Revenue Stream					
	2020/21 Original %	2020/21 Revised %	2021/22 Estimate %	2022/23 Estimate %	2023/24 Estimate %
Ratio	**-0.18%**	**-0.18%**	**-0.15%**	**0.21%**	**1.05%**

5.3 The estimates of financing costs include current commitments and the proposals in the budget report. The ratio turns positive in 2022/23 as interest expense will be payable on newly borrowed debt, at this point forecast interest expense will be greater than interest income.

5.4 The fourth prudential indicator identifies the increased revenue costs associated with the approved three year Capital Programme and expresses these in terms of the increase in Band D Council Tax Precept. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which is not published over a three year period:

Fourth Prudential Indicator - Incremental Increase in Council Tax Precept			
	2021/22 Estimate £	2022/23 Estimate £	2023/24 Estimate £
Ratio	**0.28**	**1.89**	**5.77**

6. BORROWING

6.1 The capital expenditure plans are set out in Section 2.3.6. The treasury management function ensures that the cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet the capital expenditure requirements. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of approporiate borrowing facilities. The strategy covers the relevant treasury prudential indicators, the current and projected debt positions and the annual investment strategy.

6.2 Current borrowing portfolio position

The current treasury borrowing position at 30th September 2020, with forward projections, are summarised below. The below table shows the actual and forecasted external debt (the treasury management operations), against the future underlying capital borrowing need (the CFR), highlighting any over or under borrowing:

Borrowing Position					
	2020/21 Original £000's	2020/21 Revised £000's	2021/22 Estimate £000's	2022/23 Estimate £000's	2023/24 Estimate £000's
External Debt					
Debt at 1st April	0	0	0	(0)	10,619
Expected Change in Debt	0	0	(0)	10,620	22,294
Other Long Term Liabilities at 1st April	0	0	0	0	0
Expected Change in OLTL	0	0	0	0	0
Gross Debt at 31st March	**0**	**0**	**(0)**	**10,619**	**32,913**
Capital Financing Requirement at 31st March	0	0	(0)	10,619	32,489
Under/(Over) Borrowing	**0**	**0**	**0**	**0**	**(425)**

6.3 The related impact of the above movements on the revenue budget is shown below:

Impact on Revenue Budgets					
	2020/21 Original £000's	2020/21 Revised £000's	2021/22 Estimate £000's	2022/23 Estimate £000's	2023/24 Estimate £000's
Revenue Budget Heading					
Interest on Borrowing	0	0	0	585	1,267
Investment Income	(246)	(260)	(221)	(88)	(79)
Net Police Fund Borrowing Cost	**(246)**	**(260)**	**(221)**	**496**	**1,188**

7. LIMITS ON BORROWING ACTIVITY

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

Limits on Borrowing Activity - Year End Position					
	2020/21 Original £000's	2020/21 Revised £000's	2021/22 Estimate £000's	2022/23 Estimate £000's	2023/24 Estimate £000's
Gross Debt	0	0	(0)	10,619	32,913
Investments	(30,672)	(38,250)	(20,893)	(17,479)	(16,892)
Net Borrowing	(30,672)	(38,250)	(20,893)	(6,860)	16,021
Capital Financing Requirement	0	0	(0)	10,619	32,489
Gross Debt <= CFR	Yes	Yes	Yes	Yes	No

7.2 The next key indicator is the operational boundary. This is the limit beyond which external debt is not normally expected to exceed:

Operational Boundary for Debt at 1st April					
	2020/21 Original £000's	2020/21 Revised £000's	2021/22 Estimate £000's	2022/23 Estimate £000's	2023/24 Estimate £000's
Debt	0	0	(0)	10,619	32,913
Other Long Term Liabilities	0	0	0	0	0
Net Borrowing	0	0	(0)	10,619	32,913

7.3 A further key prudential indicator representing a control on the overall level of borrowing is the Authorised Limit for External Debt. This is calculated on a 5% mark up on the operational boundary. This represents a limit beyond which external debt is prohibited and this limit needs to be set or revised by the Commissioner. 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. 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 plans of all Local Authorities and Commissioners, or those of a specific Authority or Commissioner, although no control has yet been exercised. The Commissioner is asked to approve the following Authorised Limit:

Authorised Limit for Debt at 1st April					
	2020/21 Original £000's	2020/21 Revised £000's	2021/22 Estimate £000's	2022/23 Estimate £000's	2023/24 Estimate £000's
Debt	0	0	(0)	11,150	34,559
Other Long Term Liabilities	0	0	0	0	0
Working Capital Requirement	6,220	4,101	4,101	4,101	4,101
Authorised Limit	6,220	4,101	4,101	15,251	38,660

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

8. PROSPECTS FOR INTEREST RATES

8.1 The Commissioner uses Link Asset Services (previously known as Capita Asset Services) as treasury management advisors and part of their service is to provide a view on the prospects for interest rates and economic growth. The following table gives the Link Asset Services central view on the prospects for interest rates:

UK Interest Rate Forecast

Bank Rate	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%
Capital Economics	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	-	-	-	-	-
5yr PWLB Rate	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	1.83%	1.80%	1.80%	1.80%	1.80%	1.80%	1.90%	1.90%	1.90%	1.90%	1.90%	2.00%	2.00%	2.00%	2.00%
Capital Economics	1.83%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	-	-	-	-	-
10yr PWLB Rate	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	2.17%	2.10%	2.10%	2.10%	2.10%	2.20%	2.20%	2.20%	2.30%	2.30%	2.30%	2.20%	2.30%	2.30%	2.30%
Capital Economics	2.17%	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	-	-	-	-	-
25yr PWLB Rate	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	2.75%	2.50%	2.50%	2.60%	2.60%	2.60%	2.60%	2.70%	2.70%	2.70%	2.70%	2.80%	2.80%	2.80%	2.80%
Capital Economics	2.75%	2.80%	2.80%	2.80%	2.80%	2.80%	2.80%	2.80%	2.80%	2.80%	-	-	-	-	-
50yr PWLB Rate	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	2.58%	2.30%	2.30%	2.40%	2.40%	2.40%	2.40%	2.50%	2.50%	2.50%	2.50%	2.60%	2.60%	2.60%	2.60%
Capital Economics	2.58%	2.70%	2.70%	2.70%	2.70%	2.70%	2.70%	2.70%	2.70%	2.70%	-	-	-	-	-

8.2 The Monetary Policy Committee (MPC) reduced the Bank Rate to 0.10% in 2020, due to the economic challenges experienced related to the Coronavirus pandemic. This was one of the measures to help UK businesses and households ease the temporary disruption cause by the pandemic. The MPC reported that any future Bank Rate changes would depend on the growth in the global economy and in turn, the UK economy. This rate cutting action has been mirrored around the world by other major central banks. There has been some market 'chatter' about a move to negative interest rates by the MPC, but with the recent announcement of the potential rollout of a vaccine, combined with the Bank of England favouring additional Quantative Easing of £150bn at their November policy meeting, these have placed that idea on the backburner for now.

8.3 At the November 2020 meeting, the Bank of England voted unanimously to keep interest rates on hold at 0.10% and expected GDP to not fully recover until after Quarter 3 in 2022 (which was their initial forecast). The inflation rate is forecast to end at 0.6% this year, with unemployment expected to end at 6.3%. The UK economy grew by 15.5% in the three months to September 2020, the most on record and compared with market consensus of 15.8%, as restrictions on movement eased across June, July, August and September. The final Chartered Institure of Procurememt and Supply (CIPS) UK Composite Purchasing Manager's Index (PMI) dropped to 52.1 in October 2020 from 56.5 in September, further than preliminary estimates of 52.9. This reflects the weakest period of growth in the manufacturing and services sectors in four months, suggesting that the economic recovery is slowing in the face of the reimposition of lockdown restrictions around the country.

8.4 Having left the EU on the 31st January 2020 and entered the transition period, attention will now focus on the success of the UK's attempt to negotiate a free trade treaty with the EU.

8.5 The US economy expanded by an annualised 33.1% in Quarter 3 of 2020, beating forecasts of a 31% surge. It is the biggest expansion ever, following a record 31.4% plunge in Quarter 2, as the economy rebounds from the Coronavirus pandemic. Meanwhile, the Federal Reserve voted to leave the federal funds rate unchanged once again in their November meeting. However, the Federal Open Market Committee stated that they would increase their holdings of treasury and asset backed securities over the coming months. They also confirmed that rates will remain low until the labour market is sufficiently consistent with maximum employment. The US Composite PMI stood at 56.3 in October 2020 up from the previous month's 54.3 and signalling a further solid rise in business activity.

8.6 According to the final reading, the Eurozone Composite PMI decreased to 50 in October 2020 from 50.4 in September, slightly higher than preliminary estimates of 49.4. This latest reading pointed to neither growth nor contraction in manufacturing and services activity. The Eurozone economy shrank by 4.4% year on year in Quarter 3 of 2020, easing from a record slump of 14.8% seen during Quarter 2 and very close to market expectations of a 4.3% contraction. At its October meeting, the European Central Bank left its key interest rates and Coronavirus stimulus package unchanged, as they took a 'wait and see' approach until more insightful projections are released in December, allowing for a more thorough assessment of the economic outlook. This means that they will continue with their pledge to buy up to 1.35 trillion Euros worth of debt through to June 2021, under their Pandemic Emergency Purchase Programme and maintain interest rates until inflation is sufficiently close to, but below, 2%.

8.6 The Chinese economy grew by 4.9% year on year in Quarter 3 of 2020, faster than the 3.2% year on year rate recorded in Quarter 2, but less than market forecasts of a 5.2% expansion. These two consecutive periods of expansion have proved enough to more than compensate for the contraction earlier in the year, with the Chinese economy expanding 0.7% through the first three quarters of this year. The 'official' Chinese manufacturing PMI fell slightly to 51.4 in October 2020 from 51.5 in the previous month and above market expectations of 51.3. This was the eighth straight month of growth in factory activity and the second strongest since March 2020, as the economy recovered further from the Coronavirus shock. However, the 'offical' non manufacturing PMI index increased to 56.2 in October 2020 from 55.9 a month earlier. This marked the fastest growth in the service sector since October 2013, as the economy recovers further from the Coronavirus crisis.

9. BORROWING STRATEGY 2021/22 – 2023/24

9.1 The uncertainty over future interest rates increases the risks associated with treasury activity. Investment returns are likely to remain low during 2021/22 and will continue to remain low for the foreseeable future. As a result, the Commissioner will continue a cautious approach to treasury strategy.

9.2 The Chief Finance Officer (CFO) (Section 151 Officer), under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time, taking into account the risks shown in the forecast above. It is likely that shorter term fixed rates may provide lower cost opportunities in the short/medium term.

9.3 The Commissioner is currently maintaining a neutral-borrowing position. This means that the capital borrowing need (the CFR), has been fully matched with loan debt. For 2022/23 it is predicted there will be debt as the CFR exceeds the internal resources utilised funding the Capital Programme.

9.4 External debt will only be sought once the committed funds earmarked for capital expenditure have been utilised. In future years, the over-borrowing position is a direct impact of the MRP charge reducing the CFR.

10. INVESTMENT STRATEGY 2021/22 – 2023/24

10.1 **Key Objectives -** The Commissioner's primary investment strategy objectives are, firstly, safeguarding the re-payment of the principal and interest of his investments on time; and secondly, ensuring adequate liquidity. The investment return is an important third objective, but not as important as the first two objectives. Following the economic background outlined above, the current investment climate has one over-riding risk consideration; that of counterparty security risk.

10.2 **Risk Benchmarking** – A development in the revised 2011 Codes and the Welsh Government Investment Guidance is the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance. Discrete security and liquidity benchmarks are new requirements in the revised Code, although the application of these is more subjective in nature.

10.3 These benchmarks are simple guides (not limits) and so 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.

10.4 **Security** - The Commissioner's maximum security risk benchmark for the current portfolio, when compared to these historic default tables, is:

(i) 0.010% historic risk of default when compared to the whole portfolio**.**

10.5 **Liquidity** – In respect of this area the Commissioner seeks to maintain:

(i) Liquid short term deposits of at least £2m available with a week's notice;
(ii) Weighted Average Life of investments with banks between 3 and 12 months; and
(iii) Note that no overdraft facility is held at Lloyds bank.

10.6 **Yield** - Local measures of yield benchmarks are:

(i) Investments – Internal returns compared to the 7 day London Interbank Bid Rate (LIBID).

10.7 The security benchmark for each individual year is:

	1 year	**2 years**	**3 years**	**4 years**	**5 years**
Maximum	0.010%	0.010%	Not applicable	Not Applicable	Not Applicable

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

10.8 **Investment Counterparty Selection Criteria -** The primary principle governing the Commissioner's investment criteria is the security of his investments, although the yield or return on the investment is also a key consideration. The Commissioner will not use non-specified investments, i.e. investments exceeding 1 year 364 days. The Commissioner will ensure:

(i) A policy covering types of investment, criteria for choosing investment counterparties with adequate security and monitoring their security. This is set out in the Specified Investment (investments not exceeding 1 year 364 days) sections below; and
(ii) Sufficient liquidity in investments. For this purpose procedures will be set out for determining the maximum periods for which funds

may prudently be committed. These procedures also apply to the prudential indicators covering the maximum principal sums invested.

10.9 The Assistant Chief Officer - Resources will maintain a counterparty list in compliance with the following criteria. This criteria is separate from that which chooses Specified and Non-Specified Investments, as it provides an overall pool of counterparties considered high quality, that the Commissioner may use rather than defining what his investments are.

10.10 The rating criteria uses the lowest common denominator method of selecting counterparties and applying limits. This means that the application of the Commissioner's minimum criteria will apply to the lowest available rating for any institution. For instance, if an institution is rated by two agencies, one meets the Commissioner's criteria, the other does not, the institution will fall outside the lending criteria. This is in compliance with a CIPFA Treasury Management Panel recommendation in March 2009 and the CIPFA Treasury Management Code of Practice.

10.11 Credit rating information is supplied by the Commissioner's treasury consultants on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing. For instance a negative rating watch applying to a counterparty at the minimum of the Commissioner's criteria will be suspended from use, with all others being reviewed in light of market conditions.

10.12 The Commissioner only uses the following high credit quality counterparties:

(i) UK banks and banks domiciled in a country other than the UK which has a minimum Sovereign long term rating of AAA, which have at least the following Fitch, Moody's and Standard and Poor's ratings (where rated):

- Short Term – F1/A1/P1;
- Long Term – A;

(ii) Part nationalised UK banks – Lloyds Banking Group and Royal Bank of Scotland. These banks can be included if they continue to be part nationalised or they meet the ratings in Banks above;

(iii) Building Societies which:

- Meet the ratings for banks outlined above; or
- Have assets in excess of £1bn;

(iv) Money Market Funds – AAA;

(v) UK Government (including gilts and the DMADF (see below));

(vi) Local Authorities;
(vii) Property Funds – These funds allow the Commissioner to diversify into asset classes other than cash, without the need to own and manage the underlying investments; Property Funds offer enhanced returns over the longer term, but are more volatile in the short term. Their value changes with market prices, so will be considered for longer investment periods; and
(viii) Supranational institutions.

10.13 Due care will be taken to consider the country, group and sector exposure of the Commissioner's investments. In part, the country selection will be chosen by the credit rating of the Sovereign state. In addition:

(i) No more than £3m will be placed with any single non-UK country at any time;
(ii) Limits in place above will apply to Group companies; and
(iii) Sector limits will be monitored regularly for appropriateness.

10.14 Additional requirements under the Code of Practice now require the Commissioner to supplement credit rating information. Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information (for example Credit Default Swaps, negative rating watches/ outlooks) will be applied to compare the relative security of differing investment counterparties.

10.15 The time and monetary limits for institutions on the Commissioner's Counterparty List are as follows:

	Fitch (or equivalent)	**Money Limit**	**Time Limit**
UK Banks (Groups)	*P1/F1/A1*	£10m	<365days
Non UK Banks (Groups)	*P1/F1/A1*	£5m	<365days
Building Societies	*P1/F1/A1*	£5m	<365days
Money Market Funds	AAA	£5m	<365days
Local Authorities	-	£15m	<2 years
UK DMO	-	None	<365days
Property Fund		£5m	<5 years
Guaranteed Organisations	-	£3m*	<365days

**Guaranteed institutions will need to be restricted to the terms of the guarantee.*

10.16 In the normal course of the Commissioner's cash flow operations it is expected that only Specified Investments will be utilised.

10.17 **The criteria for choosing counterparties set out above provide a sound approach to investment in 'normal' market circumstances. However, under exceptional market conditions the CFO may, after consulting the Commissioner, temporarily restrict further investment activity to those counterparties considered of higher credit quality, than the minimum criteria set out for approval. These restrictions will remain in place until the banking system returns to 'normal' conditions. Similarly the time periods for investments may be restricted.** Examples of these restrictions would be the greater use of the Debt Management Account Deposit Facility (DMADF – a Government body which accepts local authority deposits), Money Market Funds, guaranteed deposit facilities and strongly rated institutions offered support by the UK Government. The credit criteria has been amended to reflect these facilities.

10.18 Additionally, the Commissioner reserves the right to continue to hold an investment if the institutions credit rating is down-graded during the investment period, if he is satisfied that the risks associated with the institution and investment are able to be managed and/or mitigated appropriately.

10.19 **Banking Arrangements**

The Commissioner's banker is Lloyds Bank, having switched from the Co-operative Bank during 2014/15. Lloyds Bank was successful in the tendering process and the contract will now expire on 31st March 2023.

11. SENSITIVITY TO INTEREST RATE MOVEMENTS

11.1 The Commissioner is required to disclose in the accounts the impact of risks on treasury management activity. Whilst most of the risks facing the treasury management service are addressed elsewhere in this report (credit risk, liquidity risk, market risk, maturity profile risk), the impact of interest rate risk is discussed but not quantified. The table below highlights the estimated impact of a 1% increase/decrease in all interest rates to the estimated treasury management costs/income for next year. That element of the debt and investment portfolios which are of a longer term, fixed interest rate nature will not be affected by interest rate changes:

12. TREASURY MANAGEMENT - LIMITS ON ACTIVITY

Sensitivity to Interest Rate Movements		
	2021/22 Estimated +1% £000's	2021/22 Estimated -1% £000's
Interest on Borrowing	0	0
Investment Income	480	(221)

12.1 There are four further treasury activity limits, which were previously prudential indicators. The purpose of these is to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. The Commissioner approves these limits:

	2021/22	2022/23	2023/24
Interest rate Exposures			
	Upper	**Upper**	**Upper**
Limits on fixed interest rates based on net debt	100%	100%	100%
Limits on variable interest rates based on net debt	35%	35%	35%
Maturity Structure of fixed interest rate borrowing 2021/22			
		Lower	**Upper**
Under 12 months		0%	20%
12 months to 2 years		0%	20%
2 years to 5 years		0%	20%
5 years to 10 years		0%	20%
10 years and above		20%	90%
Maximum principal sums invested > 364 days			
Principal sums invested > 364 days	£m 20	£m 20	£m 20

13. PERFORMANCE INDICATORS

13.1 The Code of Practice on Treasury Management requires the Commissioner to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking. Performance indicators to be used for the treasury function are:

(i) Debt – Borrowing - Average rate of borrowing for the year compared to Public Works Loan Board (PWLB) rates; and
(ii) Investments – Internal returns compared with the 7 day LIBID rate.

The results of these indicators will be reported in the Treasury Annual Report.

14. TREASURY MANAGEMENT ADVISERS

14.1 The Commissioner uses Link Asset Services as treasury management advisors. The company provides a range of services which include:

(i) Technical support on treasury matters, capital finance issues and code compliance;
(ii) Economic and interest rate analysis;
(iii) Debt services, which includes advice on the timing of borrowing;
(iv) Debt rescheduling advice surrounding the existing portfolio;
(v) Generic investment advice on interest rates, timing and investment instruments; and
(vi) Credit ratings/market information service, comprising the three main credit rating agencies.

14.2 Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the final decision on treasury matters remains with the Commissioner.

15. TREASURY MANAGEMENT TRAINING

15.1 Officer training needs are assessed on appointment, as part of the Personal Development Review (PDR) process and when legislation changes are announced. Officers attend seminars arranged by Link Asset Services and other organisations. Staff within the Office of the Police and Crime Commissioner and Joint Audit Committee members also receive periodic Treasury Management training.