East Northamptonshire Council

Finance and Performance Sub-Committee – 6 May 2020

Treasury Management Strategy Statement 2020/21 Update

Purpose of report

This report proposes a recommendation to (full) Council to the Council's Treasury Management Investment Strategy to enable it to manage its cash resources effectively during the unprecedented situation arising from the Covid-19 coronavirus emergency.

Attachment(s)

Annex A – Proposed Changes to the Treasury Management Strategy Statement

1.0 Background

1.1 The Council approves its Treasury Management Strategy Statement on an annual basis as part of the budget and council tax setting process. The Strategy for 2020/21 was approved at the council meeting on 2nd March 2020.

1.2 A core element of the Treasury Management Strategy Statement is the Investment Strategy, which sets out how the council's surplus cash resources are managed.

1.3 The Investment Strategy general policy objective is to invest the council's surplus funds prudently, with a focus on the safe return of the sum invested. As such the Council's investment criteria in priority order are:

- Security of capital invested
- Liquidity of capital invested
- Return on investment

1.4 The Council primarily invests its surplus monies with a range of financial institutions, other local authorities, money market funds and government. These organisations are referred to as counterparties.

1.5 The Council maintains a counterparty list based on its criteria and monitors/updates the credit standing of the institutions on a regular basis, liaising with its Treasury Advisers as appropriate. The counterparty list includes limits on the amount of cash that can be invested with any given organisation. The limit is based on the creditworthiness of that organisation. For example our limit for a "high" credit rated financial institution or fund is £3m and for government is £10m.

2.0 Impact of Covid-19 Emergency Response on the Investment Strategy

2.1 The Council has typically had cash investments averaging around £25m over the past few years. In response to the Covid-19 situation the government has announced unprecedented levels of support for businesses and individuals.

2.2 Councils have been the conduit through which the government has allocated this support to businesses and individuals. Examples include extending the Business Rates Relief Scheme and the Business Grants Scheme to support business and a Hardship Grant to support individuals. The government is paying these monies to local councils to distribute.

2.3 The impact of the payment of these monies is a step change in the level of cash balances being held by the council on a temporary basis before they are paid out to businesses and individuals. For example, the level of cash investments in late

March and early April has been up to £50m.

2.4 The current counterparty limits set out in the Investment Strategy cannot support these elevated cash balances.

2.5 As such the council has breached its counterparty limits from 27th March. To mitigate this breach and ensure the council upheld its priorities as set out in the Investment Strategy, excess monies were placed with the highest credit rated counterparty the council is able to invest with, namely the Debt Management Office, which is part of HM Treasury/UK Government. This decision was taken to ensure the security of council funds. This breach in strategy was reported to the Chairs of Finance & Performance Sub Committee and the Governance & Audit Committee and was then reported to all councillors via a report to Annual Council to be held on 15 April. However this meeting was cancelled and so is now being reported in the first instance to the Sub-Committee.

2.6 The current elevated levels of cash balances are anticipated to continue until the council has paid out the grants to businesses and individuals. This is expected to happen as soon as practically possible. However, there is the potential that further government support in response to the Covid-19 emergency response may be needed for businesses and individuals. To manage such situations the council needs to ensure its Investment Strategy is flexible enough to cope.

3.0 Options

3.1 The primary options open to the council in these exceptional circumstances are:

Options	Pros	Cons
Do nothing (leave surplus monies in the councils bank account - Barclays)	- Simplest option operationally	- Requires a change to approved TM Investment Strategy - Significant exposure with one counterparty
Increase the counterparty limit for Debt Management Office (DMO) (current limit £10m, increase to unlimited)	- DMO is the HM Treasury and is UK government backed - Higher credit quality than Barclays - Reasonably simple to implement operationally	- Requires a change to approved TM Investment Strategy
Increase the counterparty limits for banks/financial institutions/money market funds (From current £3m to £5m per counterparty)	- Increases flexibility of counterparties - Ensures credit quality of counterparties is not reduced	- Requires a change to approved TM Investment Strategy - More exposure to financial institutions when there is stress on the financial markets - No guarantee monies will be placed due to money market saturation
Reduce the credit worthiness rating from “high” to a lower level (from current A- to BBB)	- Increases number of counterparties ENC is able to place monies with	- Requires a change to approved TM Investment Strategy - Exposes council to lower credit quality

		- No guarantee monies will be placed due to money market saturation

4.0 Proposed Change to Investment Strategy

4.1 The proposed solution is to provide a delegation to the Chief Finance Officer (or their nominee), following consultation with the Chairmen of the Finance & Performance Sub Committee and the Governance & Audit Committee, to temporarily increase the Debt Management Office counterparty limit from £10m to unlimited if required due to exceptional circumstances.

4.2 The rationale for this proposed solution is that it:

- Provides the ability for the council to keep its cash secure in the highest level of creditworthiness available in the UK;
- Follows the principle that security of monies is the highest priority in the Investment Strategy;
- Provides a pragmatic operational solution.

4.3 It should be noted that the council will do everything possible to operate within its existing Investment Strategy and this delegation will only be used in exceptional circumstances. If the delegation is instigated at any point a specified period of time will need to be clearly set out for how long it is to be in operation for.

4.4 To facilitate this change, Appendix E of the council's Treasury Management Strategy Statement will require amendment. A copy of this along with the proposed amendments to the wording (which have been highlighted) is included at Annex A.

4.5 The Finance & Performance Sub Committee receives regular reports on the Treasury Management Strategy at its meetings. An update will be provided as part of the reporting process if this delegation has been required to be utilised.

5.0 Privacy Implications

5.1 There are no privacy implications as a result of this report.

6.0 Equality and Diversity Implications

6.1 There are no equality or diversity implications arising from this report.

7.0 Legal Implications

7.1 There are no known legal implications arising from the changes proposed in this report.

8.0 Risk Management

8.1 This report seeks to minimise the risks of legal non-compliance by updating the TM Investment Strategy in line with the latest environment facing the council.

9.0 Constitutional Implications

9.1 The proposed changes to the TM Investment Strategy enable the council to operate within its constitution and will take effect immediately after the Council approves the amendments.

10.0 Resource and Financial Implications

10.1 The report sets out the financial implications in sections 1 to 4.

11.0 Customer Services Implications

11.1 There are no direct customer services implications arising from this report.

12.0 Corporate Outcomes

12.1 The proposed amendments to the Investment Strategy will contribute to the corporate outcome of Effective Management by ensuring transparency in decision making.

13.0 Recommendations

13.1 That Finance and Performance Sub-Committee recommend to (full) Council that it:

a) Delegates to the Chief Finance Officer (or their nominee), following consultation with the Chairmen of Finance & Performance Sub Committee and the Governance & Audit Committee, to temporarily increase the Debt Management Office counterparty limit from £10m to unlimited for a specified period of time due to exceptional circumstances.

b) Approves the amended wording to Appendix E of the Treasury Strategy Statement 2020/21 as set out in Annex A.

[Reason: To ensure that the council is able to operate within its Investment Strategy at a time of extraordinary circumstances in response to the coronavirus (Covid-19) emergency.]

<table>
<tr><td rowspan="2">Legal</td><td colspan="5">Power: Local Government Act 2003</td></tr>
<tr><td colspan="5">Other considerations: Coronavirus Act 2020
Various - published Guidance on Treasury Management</td></tr>
<tr><td colspan="6">Background Papers: Treasury Management Strategy Statement of East Northamptonshire Council.</td></tr>
<tr><td colspan="6">Person Originating Report: Glenn Hammons, Executive Director (Resources & Commercial)
Chief Finance Officer
⌧ghammons@east-northamptonshire.gov.uk ☎ 01832 742120</td></tr>
<tr><td colspan="6">Date: 27 April 2020</td></tr>
<tr><td>CFO
08/04/20</td><td></td><td>MO</td><td></td><td>CX
08/04/20</td><td>D. Oliver</td></tr>
</table>

ANNEX A

Extract from Treasury Management Strategy Statement 2020/21

[Proposed new wording is highlighted]

Appendix E

CRITERIA TO BE USED FOR CREATING/ MANAGING APPROVED COUNTERPARTY LISTS/LIMITS

1. The Chief Financial Officer will formulate suitable criteria for assessing and monitoring the credit risk of investment counterparties and shall construct a lending list comprising time, type, sector and specific counterparty limits.
2. Treasury Management staff will add or delete counterparties to/from the approved counterparty list in line with the policy on criteria for selection of counterparties.
3. The Council will use credit criteria in order to select creditworthy counterparties for placing investments with and will take advice as appropriate from the Council's external Treasury Advisors.
4. Credit ratings will be used as supplied from one or more of the following credit rating agencies: -
    - Fitch
    - Standard & Poor's
    - Moody's Investors Services

5. Selection criteria for approved investment counterparties.
    - Published credit ratings for financial institutions (minimum long term rating of A- or equivalent for counterparties; A+ or equivalent for non-UK sovereigns).
    - Credit Default Swaps
    - Economic fundamentals (Net Debt as a percentage of GDP)
    - Share Prices
    - Corporate Developments, news, market sentiment and momentum
    - Subjective overlay

The Councils Bank

The Council banks with Barclays Bank. If their credit rating does not meet the minimum credit criteria specified in this Investment Strategy, Barclays Bank will continue to be used for the short term liquidity requirements (overnight and weekend investments) only to ensure business continuity arrangements are maintained.

6. Investment limits for each counterparty:

Credit Rating	Banks Unsecured	Bank Secured	Government	Corporate	Registered Providers
UK Govt	n/a	n/a	£10m [unlimited in exceptional circumstances] 50 years	n/a	n/a
AAA	£3m 5 years	£3.5m 20 years	n/a	£2m 20 years	£2m 20 years
AA+	£3m 5 years	£3.5m 10 years	n/a	£2m 10 years	£2m 10 years
AA	£3m 4 years	£3.5m 5 years	n/a	£2m 5 years	£2m 10 years
AA-	£3m 3 years	£3.5m 4 years	n/a	£2m 4 years	£2m 10 Years
A+	£3m 2 years	£3.5m 3 years	n/a	£2m 3 years	£2m 5 years
A	£3m 13 months	£3.5m 2 years	n/a	£2m 2 Years	£2m 5 years
A-	£3m 6 months	£3.5m 13 months	n/a	£2m 13 months	£2m 5 years
BBB+	£1m 100 days	£1.5m 6 months	n/a	£1m 6 months	£2m 2 years
B or BBB-	Next day only	Next day only	n/a	n/a	n/a
None	£1m 6 months	n/a	n/a	£50,000 5 years	£1m 5 years
Pool funds	£3m per fund				

7. The maximum value for any one investment transaction will be as shown in the table above.
8. Sterling denominated only.
9. Sovereign rating of any non-UK counterparty will not be less than the current UK Sovereign rate.
10. When exceptional circumstances (e.g. Covid-19 emergency response) lead to elevated cash balances there is a delegation in place for the Chief Finance Officer, in consultation with the Chairs of Finance & Performance Sub Committee and Governance & Audit Committee, to temporarily increase the Debt Management Office counterparty limit from £10m to unlimited for a specified period of time.

Below is an explanation of the headings used:

Credit Ratings and Risk Assessment: Investment decisions are made by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used.

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

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

Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as “rating watch negative” or “credit watch negative”) so that it may fall below the approved rating criteria, then only investments that can be withdrawn (on the next working day) will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Banks Unsecured: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. Unsecured investment with banks rated BBB or BBB- are restricted to overnight deposits at the Authority’s current account bank.

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

Government: Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.

Corporate: Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made as part of a diversified pool in order to spread the risk widely.

Registered Providers: Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services; they retain a high likelihood of receiving government support if needed.

Pooled Funds: Shares in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Money Market Funds that offer same-day liquidity and aim for a constant net asset value will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority’s investment objectives will be monitored regularly.