Police and Crime Commissioner for Devon and Cornwall
Open for the purposes of FOI
Report of the Treasurer

Treasury Management Strategy for 2015-16

RECOMMENDATIONS:

That the Treasury Management / Investment Strategy be approved and specifically:

(i) the Annual Investment Strategy be approved;
(ii) the Borrowing Strategy be approved;
(iii) that the Treasurer should retain the flexibility to invest funds directly in the PCC's Investment Fund within the limits set out in the strategy;
(iv) that the counterparty list attached at Appendix 7 be approved for all new lending;
(v) that the capital expenditure prudential indicators (paragraph 3.1), the external debt indicators (paragraphs 5.2 & 5.6), the Treasury Management Limits on Activity (paragraph 5.15 and 5.16) and the Investment Treasury Indicator (paragraph 6.25) be approved;
(vi) that the Minimum Revenue Provision Statement attached at Appendix 1 be approved;
(vii) the use of Barclays as the Police and Crime Commissioner's bankers be noted.

1.0 Purpose of the Treasury Management Strategy

1.1 The purpose of the Treasury Management Strategy is to ensure that:

(i) Revenue Cash Flow is Adequately Planned

The Police and Crime Commissioner (PCC) is required to operate a balanced budget, which in broad terms means that cash raised during the year will meet cash expenditure. The treasury management operation is designed to:

- ensure that cash flow is adequately planned during the year, with cash being available when it is needed;
- Surplus monies are invested in counterparties or instruments commensurate with the Police and Crime Commissioner's (PCC's) risk appetite, providing adequate liquidity before considering the investment return.

(ii) Funding is Available to meet Capital Expenditure Plans

The second main objective of the treasury management function is the funding of the PCC's capital plans. Capital expenditure does not have to be charged against the income for the year and for this reason longer term cash flow planning is required to ensure that the PCC 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 PCC's risk or cost objectives.

1.2 The Treasury Management Strategy is integrated with the Medium Term Financial Strategy and this document should be read in conjunction with the report on the Medium Term Financial Strategy 2015-16 to 2018-19.

2.0 Treasury Management Strategy 2015-16

2.1 The strategy for 2015-16 covers two main areas:

2.2 Capital issues:

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

2.3 Treasury management issues:

- the current treasury position;
- treasury indicators which limit the treasury risk and related activities of the PCC;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- policy on use of external service providers.

2.4 These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the Department for Communities and Local Government's (DCLG) MRP Guidance, the CIPFA Treasury Management Code and DCLG Investment Guidance.

2.5 The PCC's objectives for treasury management both investing and borrowing are as follows:

- effective management and control of risk is the prime objective;
- the PCC attaches a high priority to revenue cost stability. This aids stable financial planning and avoids a stop-start approach to service delivery. This means a relatively low-risk attitude to treasury management is adopted, and it is accepted that this may come at a cost;
- the main risks with regard to treasury management activities are security, liquidity and yield risk. The PCC's treasury management policies will prioritise the risks in that order of importance, that is highest priority will be given to security, followed by liquidity and then yield;
- the PCC will pursue best value in treasury management within the context of effective risk management.

3.0 The Capital Prudential Indicators 2015-16 to 2018-19

3.1 The PCC's capital expenditure plans are set out in detail in the Medium Term Financial Strategy and are summarised in table 1.

Table 1
The Capital Programme

	2014-15 £000	2015-16 £000	2016-17 £000	2017-18 £000	2018-19 £000
Capital Expenditure	**10,875**	**12,994**	**27,171**	**13,477**	**7,594**
Funded By					
Gross Borrowing	1,130	1,396	2,336	4,530	1,215
Other capital resources	9,745	11,598	24,835	8,947	6,379

3.2 The capital financing requirement is a measure of the Commissioner's underlying need to borrow.

Table 2
Capital Financing Requirement

	2014-15 £000	2015-16 £000	2016-17 £000	2017-18 £000	2018-19 £000
Opening Capital Financing Requirement	**42,059**	**41,593**	**41,314**	**42,054**	**45,011**
Capital expenditure to be funded by borrowing	1,130	1,396	2,336	4,530	1,215
Less application of capital receipts to reduce borrowing*	0	0	0	0	0
Less minimum revenue provision	(1,421)	(1,489)	(1,533)	(1,573)	(1,627)
Less finance lease minimum revenue provision	(175)	(186)	(63)	0	0
Closing Capital Financing Requirement	**41,593**	**41,314**	**42,054**	**45,011**	**44,599**

Capitalisation of Equal Pay

3.3 Following recent changes to legislation the PCC may use capital receipts to fund one off costs in relation to equal pay claims. The proposed capital programme as set out in the MTFS assumes that there will be no need to apply capital receipts to cover the one off costs of equal pay claims. This Treasury Management Strategy and in particular the calculation of the Capital Financing Requirement as set out in table 2 above and the borrowing strategy as set out in paragraph 5.9 below are based on this assumption.

Minimum Revenue Provision (MRP) Policy Statement

3.4 The PCC is required to pay off an element of the Capital Financing Requirement each year through a charge to revenue. DCLG regulations have been issued which require the PCC to approve an MRP Statement in advance of each year. The proposed statement is attached at Appendix 1.

Core Funds and Expected Investment Balances

3.5 Budget decisions with regard to contributions to and from revenue reserves and the application of resources (capital receipts, reserves etc.) to finance capital expenditure have an ongoing impact on investments. The 2015-16 Medium Term Financial Strategy includes a temporary increase to revenue reserves in the period 2015-16 to 2016-17. Detailed below are estimates of the year end balances for each resource and anticipated day to day cash flow balances.

Table 3
Core Funds and Expected Investment Balances

	31/3/15 £000	31/3/16 £000	31/3/17 £000	31/3/18 £000	31/3/19 £000
Fund balances / reserves	61,457	54,356	40,670	22,785	18,092
Unapplied capital grant/ receipts	4,220	16,553	3,874	3,074	570
Provisions	654	654	654	654	654
Total core funds	**66,331**	**71,563**	**45,198**	**26,513**	**19,316**
Working capital*	3,700	3,700	3,700	3,700	3,700
(Under)/over borrowing	(2,600)	(1,500)	(3,800)	(3,200)	(1,800)
Actual/Expected investments	**67,431**	**73,763**	**45,098**	**27,013**	**21,126**

*Working capital balances shown are estimated year end; these may be higher or lower mid year

Internal Borrowing

3.6 For a number of years the Police and Crime Commissioner has had a policy of internal borrowing. This approach uses revenue cash balances to fund capital expenditure. In recent months long term borrowing rates have declined considerably and for this reason it is proposed that the level of internal borrowing is reduced as compared with previous forecasts.

4.0 Affordability Indicators 2015-16 to 2018-19

4.1 The affordability indicators demonstrate the impact of the capital investment plans on the PCC's overall finances.

Estimate of the ratio of net capital financing costs to revenue budget

4.2 Capital financing costs comprise minimum repayment of "loan principal" and interest paid on loans, offset by interest received.

Table 4

Ratio of Net Capital Financing Costs to Revenue Budget

	2014-15 £000	2015-16 £000	2016-17 £000	2017-18 £000	2018-19 £000
Minimum Revenue Provision	1,421	1,489	1,533	1,573	1,627
Finance Lease Minimum Revenue Provision	175	186	63	0	0
Interest payable on Long Term Borrowing	1,365	1,588	1,646	1,730	1,836
Interest Received (net)	(325)	(494)	(470)	(373)	(305)
Capital Financing Costs	**2,636**	**2,769**	**2,772**	**2,930**	**3,158**
Net Budget Requirement	284,491	279,724	274,257	270,916	270,897
Ratio of financing costs to net revenue stream	0.93%	0.99%	1.01%	1.08%	1.17%

Incremental Impact on Council Tax

4.3 This indicator shows the incremental impact on the Band D council tax payer of the additional capital expenditure funded from borrowing included in the 2015-16 capital programme.

Table 5

Incremental Impact on Council Tax

	2015-16	2016-17	2017-18	2018-19
Incremental increase in Council Tax arising from Capital Expenditure Plans	£0.04p	£0.18p	£0.28p	£0.37p

5 Borrowing

5.1 The capital expenditure plans set out in Section 3 above provide detail of the service activity of the PCC. This section shows how those plans impact on the need to borrow and the forecast level of external borrowing.

5.2 **Current Position**

The PCC's borrowing position at 31 March 2015, with forward projections are 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. It is based on certain assumptions with regard to new borrowing which are set out in paragraphs 5.9 to 5.12 below.

Table 6

External Debt

		2014-15 Est £000	2015-16 Est £000	2016-17 Est £000	2017-18 Est £000	2018-19 Est £000
1	Debt at 1 April	33,203	39,028	39,841	38,278	41,778
2	Finance Lease Liabilities	(175)	(187)	(63)	0	0
3	Debt maturing	(2,000)	0	(4,500)	0	0
4	New Debt arranged to Dec 2014	4,000				
5	Debt as at 12/2/2015	35,028				
6	Additional Debt	4,000	1,000	3,000	3,500	1,000
7	Total Forecast Debt	39,028	39,841	38,278	41,778	42,778
8	Capital Financing Requirement	41,593	41,314	42,053	45,010	44,598
8	Internal Borrowing (CFR-Debt)	2,565	1,473	3,775	3,232	1,820

5.3 Within the prudential indicators there are a number of key indicators to ensure that the PCC operates its activities within well defined limits. One of these is that the PCC 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 2015-16 and the following two financial years.

5.4 The Treasurer reports that the PCC complied with this prudential indicator in the current year and does not envisage difficulties for the future (row 5 of table 6 is always lower than row 6). This view takes into account current commitments, existing plans, and the proposals in the Medium Term Financial Strategy.

Prudential Indicators for External Debt

5.5 **The operational boundary** is the limit which external debt is not normally expected to exceed.

5.6 **The Authorised Limit** represents the maximum level at which the Commissioner is able to borrow and enter into other long term liabilities. Additional borrowing beyond this level is prohibited unless the limit is revised by the Commissioner.

Table 7

Prudential Indicators for External Debt

	2015-16	2016-17	2017-18	2018-19
	£000	£000	£000	£000
Long term borrowing for capital purposes	41,314	42,053	45,010	44,598
Lease Finance	250	63	0	0
Maximum cash-flow deficit arising from revenue budget operations	10,000	10,000	10,000	10,000
Operational Boundary	**51,564**	**52,116**	**55,010**	**54,598**
Additional margin for unforeseen circumstances	3,000	3,000	3,000	3,000
Authorised Limit	**54,564**	**55,116**	**58,010**	**57,598**

Prospects for Long Term Interest Rates

5.7 The PCC has appointed Capita Asset Services as its treasury advisor and part of their service is to assist the Commissioner to formulate a view on interest rates. The Appendix 4 gives the Capita central view with regards to long term interest rates (published 5 January 2015). It should be noted that:

- The Capita forecast shows long term interest rates rising steadily over the next three years, with 25 yr PWLB debt rising from 3.3% to 4.8%
- Actual experience in January has been that rates have declined further to aaproximately 3.0%

. **Borrowing Strategy 2015-16 to 2018-19**

5.8 The overall aims of the borrowing strategy are:

- borrowing at the lowest possible rates in the most appropriate periods
- minimising borrowing costs and expenses
- the management of debt maturities to avoid large levels of maturities in any one year.

5.9 For a number of years market conditions have been such that internal borrowing (use of the PCC's own cash resources to fund capital expenditure) was in the short term, the most cost effective method of borrowing. This is because the opportunity cost of not lending working balances and reserves (i.e. the interest returns on short term loans) is significantly below the cost of borrowing to finance the capital programme. Internal borrowing also has the advantage of reducing credit and counter party risk as external lending by the PCC is reduced.

5.10 Three factors mean that this approach needed to be re-evaluated:

- A reduction in long term interest rates (25 year rates are currently 3.0% as compared to 4.7% as forecast in last year's Treasury Management Strategy). In addition Capita's forecast indicates that this reduction in rates is relatively temporary.
- A forecast reduction in reserves from 2017-18 onwards

- An increase in capital expenditure to be funded from borrowing.

Based on current forecasts of reserves and capital expenditure it is clear that the capital financing requirement and hence the need to borrow will increase over the next few years. If the reduction in interest rate is temporary as the advisers forecast indicate this suggests that borrowing should be undertaken sooner rather than later.

5.11 In December 2014 the PCC approved new borrowing of £4.0m on the basis of a report setting out the factors outlined above. This new loan is contained within the total borrowing set out at Appendix 10.

5.12 The borrowing strategy for 2015-16 is set out in table 8 below, which shows the planned increase in external debt and whether this arises from a reduction in internal borrowing or changes in the Capital Financing Requirement.

Table 8

Borrowing Strategy 2015-16

Change in External Debt

	2014-15 £000	2015-16 £000	2016-17 £000	2017-18 £000	2018-19 £000
New debt taken December 2014	4,000				
Further external debt	4,000	1,000	3,000	3,500	1,000
Debt maturities and reductions in lease finance	(2,200)	(200)	(4,600)		
Net increase/(decrease) in external debt	**5,800**	**800**	**(1,600)**	**3,500**	**1,000**
(Reduction)/increase in internal borrowing	(6,300)	(1,100)	2,300	(500)	(1,400)
Reduction/(increase) in Capital Financing Requirement	500	300	700	3000	(400)

Forecast Level of Internal Borrowing

	2014-15 £000	2015-16 £000	2016-17 £000	2017-18 £000	2018-19 £000
Total Internal Borrowing	2,600	1,500	3,800	3,200	1, 800

Debt Rescheduling

5.13 Opportunities to restructure the existing debt have been reviewed. This has shown that the cost of debt repayment in terms of premiums incurred exceeds the savings in interest. Restructuring would not therefore generate any savings at the present time.

Policy on Borrowing in Advance of Need

5.14 For the purposes of clarity this strategy makes clear that the PCC will not borrow more than or in advance of needs, purely in order to profit from the investment of the extra sums borrowed. Any proposal to borrow in advance of need to minimise the costs of future borrowing requirements will be on the basis of a detailed business case and will require specific approval.

Treasury Management Limits on Activity

5.15 **Interest Rate Exposures**

Upper limit on fixed and variable interest rate exposures for 2015-16 to 2018-19 are:-

This indicator sets a limit for the exposure to change in interest rates.

	Upper Limit
Upper limit on fixed rate exposures - debt	100%
Upper limit on variable rate exposures - debt	30%

This means 70% - 100% of borrowing will be at rates fixed until the loan is repayable, while no more than 30% will be at variable rates and so liable to change at short notice. All of the variable rate borrowing will be internal borrowing.

5.16 **Maturity Structure of Borrowing**

Maturity Structure of Fixed Interest Rate Borrowing

	Lower Limit %	Upper Limit %
Under 12 Months	0	10
12 Months to 2 Years	0	15
2 years to 5 Years	0	25
5 Years to 10 Years	0	40
10 Years and Above	60	100

This indicator shows a maximum of 40% of the Commissioner's borrowing may be for periods of less than 10 years. The remaining debt will be for periods of 10 years or more.

5.17 The actual maturity profile of the PCC debt is provided in Appendix 10.

6 Annual Investment Strategy

6.1 The PCCs investment policy has regard to the DCLG's Guidance on Local Government Investments ("the Guidance") and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA Treasury Management Code").

6.2 The overall aims of the PCC's investment strategy are:

- to limit the risk of the loss of capital
- ensure funds are always available to meet cash-flow requirements
- to maximise investment returns consistent with the first two aims.

The overriding objective will be to invest prudently, with priority being given to security and liquidity before yield.

6.3 The PCC's risk appetite can be characterised as follows:

- the PCC looks to invest in banks and building societies of a high credit quality and sets lending limits against each one;
- lending to other Local Authorities and Public Bodies can be undertaken;
- the PCC may lend to the Debt Management Office (central government), this lending is seen as having the highest level of security;
- the PCC may use Treasury Bills and Certificates of Deposit;
- the PCC may invest in money market funds and enhanced money market fund with a AAA/AAA(f) credit rating;

6.4 The PCC has two different mechanisms for investing surplus funds:

- The PCC's Investment Fund managed by the Treasurer - this fund is invested in fixed interest deposits and money market funds. The remit of the fund is contained at Appendix 2
- Very short term deposits varying from overnight to 3 months which are used to facilitate short term cash management.

6.5 There is one exception to the above which is a holding of £0.5m UK gilts which were transferred to the PCC investment fund when the PCC ceased investing with an external fund manager.

6.6 The low level of return currently available for fixed term deposits has led to the consideration of a number of alternative investment approaches. The only options that meets all of the PCC's objectives is the use of "cash plus" funds and this type of investment will be an approved instrument within the 2015-16 Treasury Management Strategy.

6.7 The options of using either a property fund or a corporate bond fund require more detailed investigation and whilst they have not been rejected they are not included in the strategy at present.

Investment Strategy Principles

6.8 It should be borne in mind that it would be impossible for the PCC to mitigate all of the possible risks inherent in investing cash balances. Further economic or banking problems could impact on the security or returns achieved from the investment strategy.

6.9 In exceptional circumstances, the Treasurer will be empowered to invest in foreign currencies but only with the explicit approval of the PCC.

6.10 The investment strategy for the PCC Investment Fund is set out in Appendix 2. The investment fund will hold all internally managed cash investments with durations of more than 100 days. Short term deposits of less than 100 days will be managed separately. Specifically the performance benchmark of 3 month LIBID will not apply to short term deposits. Also short term deposits do not require approval from the Treasurer as set out in Treasury Management Practices.

Changes to the Regulation of the Banking Sector and the Removal of Implied Sovereign Support

6.11 A number of changes to the regulations of the banking sector within the EU will be fully implemented in the 2015-16 financial year. As a result of these changes rating agencies have started a process to remove implied sovereign support from their ratings. As a number of institutions on the PCC's current lending list are benefiting from sovereign support the changes in approach may reduce the number of counter parties available to the PCC. To mitigate the impact of this change whilst at the same time maintaining a high quality counter party list the following changes have been made to the Treasury management Strategy for 2015-16.

- Counter parties were previously included on the counter party list on the basis of lowest common denominator (that is counter parties must be rated A or above with all of the agencies if a counter party fell below A with any of the three agencies it would be removed from the list). For 2015-16 counter parties will be included on the list on the basis that at least one agency rates the counter party A or above. In addition the counter party must be allocated a colour band by Capita.
- The counter party limit for AAA rated money market funds has been raised from £10m to £20m for each fund. As money market funds provide a significant level of diversification among well rated counter parties, increasing the threshold with these fund will provide helpful capacity should some institution be removed from the lending list.

Creditworthiness Policy

6.12 The PCC will utilise a creditworthiness policy that:

i. fully accounts for the ratings and outlook watches published by all three ratings agencies with a full understanding of what they reflect in the eyes of each agency
ii. recognises that ratings should not be the sole determinant of the quality of an institution and that 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
iii. takes account of information that reflects the opinion of the market, such as "Credit Default Swaps"
iv. Uses other information sources, for example, 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

6.13 To comply with the above the PCC will utilise the creditworthiness service supplied by Capita Assets Services which meets all of the requirements set out above. When using this service the PCC will be aware that the ultimate responsibility for ensuring the creditworthiness of counterparties will lie with the PCC.

6.14 For ease of reference the Capita Assets Services approach uses colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the PCC to determine the duration for investments. The PCC will therefore use counterparties within the durational bands set out in table 9.

Table 9

Yellow	5 years *
Dark Pink	5 Years **
Light Pink	5 Years ***
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

* This category is for AAA rated Government debt or its equivalent
** This category is for enhanced money market funds with a credit score of 1.25
*** This category is for enhanced money market funds with a credit score of 1.5

6.15 The PCC has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch. The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 6. This list will be added to, or deducted from by officers should ratings change in accordance with this policy.

6.16 If Barclays, the PCC's bankers, fall below the rating criteria set out below or they are removed from the Capita Asset Services list the threshold for new deposits will be reduced to £250,000 to allow the current account to operate in the short term. When using durational bands set out above the PCC will also apply credit limits as set out in table 10 below. The proposed counter party list is set out in Appendix 7.

Table 10

Counterparty Limits Investment Fund and Short Term cash Deposits

Counterparty type	**Minimum Credit Criteria/ Colour Band**			**Credit Limit**
Banks				
Term Deposits with UK and Foreign Banks		Green		
Overnight deposits UK and Foreign Banks	Fitch	Moodys	Standard and Poors	£12m
	A	A2	A	
Building Societies				
UK Building Societies		Green		£6m
Public Bodies				
Central Government				
Debt Management Office (credit criteria relates to UK sovereign rating)		AA+		No limit
Local Government				
All Local Authorities, Fire Authorities and Police and Crime Commissioners		N/A		£12m
Money Market Funds including enhanced money market funds		AAA		£20m

6.17 The approved list of counterparties is formally reviewed at least weekly. Notification of credit rating downgrades (or other market intelligence) is acted upon immediately, resulting in any further lending being suspended.

6.18 All additions, to the approved counterparty list will be approved by the Treasurer.

6.19 The DCLG classifies investments as either specified or non-specified. Specified investments are lower risk whereas non-specified investments are higher risk. To be a specified investment an investment must be:

- Sterling denominated
- For less than 365 days
- Be of high credit quality
- not deemed to be capital expenditure

6.20 Appendix 3 sets out the PCC’s investments and classifies them according to whether they are specified or non-specified investments. No more £20m or 50% of the overall portfolio whichever is the lower will be invested in non-specified investments.

Investment Return Expectations

6.21 Capita Asset Services have provided a detailed forecast for Bank of England (BoE) bank rate and market rates which is provided in Appendix 4. The BoE bank rate is forecast to remain unchanged at 0.5% before starting to rise from quarter 4 of 2015. BoE bank rate forecasts for financial year ends (March) are:

- 2015-16 0.75%
- 2016-17 1.75%
- 2017-18 2.0%

6.22 The rates used to calculate the interest receipts budget are as contained in table 11 below.

Table 11

Forecast Rates for Budget Purposes (Interest receipts)	**Average %**			
	15-16	**16-17**	**17-18**	**18-19**
Short Term Cash	0.6	1.0	1.7	1.7
Devon and Cornwall Police Investment Fund	0.9	1.7	2.1	2.1

6.23 The economic data and commentary that underpins these forecasts is provided in Appendix 8. If the economy were to recover more quickly than Capita Asset Services' forecast then the investment returns would be higher than included in the Medium Term Financial Strategy. Conversely if the pace of economic recovery is slower than forecast then returns, particularly in the later years of the Medium Term Financial Strategy, will be lower than forecast.

Performance

6.24 The benchmark for performance on the Investment fund will be the 3 month LIBID (London Interbank Bid Rate); this is a more challenging target than that used in previous year (7 day LIBID).

Investment Treasury Indicator

6.25 **Upper limit for principal sums invested for period of over 364 days.**

This indicator sets a limit on the level of investments that are held for more than 364 days.

The Treasury Management Strategy imposes the following controls on sums invested for more than 364 days:

> Police and Crime Commissioner's Investment Fund - no more than the lesser of £20m or 50% of the Investment Fund may be invested for more than 364 days

The total for forecast investments as at 31 March 2015 is £38m

Limits on investments to mature beyond:

31 March 2016 £19.0m
31 March 2017 £0.5m
31 March 2018 £0

7.0 Monitoring & Benchmarking

7.1 Income and expenditure will be monitored monthly to ascertain performance against the budget. Performance and changes in borrowing and lending will be reported regularly to the PCC through the Treasurer.

7.2 During 2015-16 the PCC will participate in the Capita Asset Services benchmarking club. The aim of this benchmarking will be to determine, whether, given the risk appetite of the PCC the rate of return on internally managed funds has been maximised.

8 Governance Structure

8.1 The governance arrangements for the Treasury Management Strategy are set out in Appendix 8. This strategy will be considered by the Joint Audit Committee before it is presented to the PCC.

9 Banking Arrangements

9.1 The PCC's bankers are Barclays PLC. In November 2014 an extension of the current contract for one year until 31 March 2016 was approved in November 2014.

10 Treasury Management Consultants

10.1 The PCC uses Capita Asset Services as its external treasury management advisors.

10.2 The PCC recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon external service providers. The PCC 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 PCC 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.

11.0 Conclusion

11.1 The continuation of the low bank rate of 0.5% and changes to the regulation of the banking sector mean that 2015-16 will be another challenging year in terms of investment returns.

11.2 The nature of the PCC's debt means that no rescheduling or repayment is possible. However a "window" of particularly low long term interest rates in early 2015 means that it is advantageous to reduce the level of internal borrowing and increase the level of external debt on the basis that internal borrowing will need to be reduced from 2017-18 onwards as revenue balances decline.

11.2 The Treasury Management Strategy has been reviewed by the treasury management advisers, Capita Asset Services, and their view is; that it complies with all the legislative requirements and is sound in terms of the current and forecast interest rates.

11.3 This Strategy is compliant with all the relevant statutory and regulatory requirements including; the CIPFA Code of Practice on Treasury Management, the CIPFA Prudential Code, the Local Government Act 2003 and the Department for Communities and Local Government investment guidance.

Duncan Walton
Treasurer

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Appendices

1 MRP Policy
2 Objectives of the PCC's Investment Fund
3 Interest Rate Forecasts
4 Alternative Investment Strategies
5 Countries Approved for Investment
6 Police and Crime Commsiioner for Devon and Cornwall - Approved List of Borrowers
7 Economic Background
8 Treasury Management Governance Arrangements
- Role of the PCC Senior Management Team
- Role of the Joint Audit Committee
- The treasury management role of Treasurer (the section 151 officer)

9 External Borrowing

Minimum Revenue Provision Policy Statement 2015-16

DCLG Regulations have been issued which require The Police and Crime Commissioner to approve an MRP Statement in advance of each year.. The Commissioner 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 CLG Regulations (Option 1);

This option provides for an approximate 4% reduction in the borrowing need (CFR) each year.

For expenditure incurred after 1 April 2008 the MRP policy will be:

- Asset Life Method – MRP will be based on the estimated life of the assets, in accordance with the regulations (Option 3);

This option provides for a reduction in the borrowing need over approximately the asset’s life.

Devon and Cornwall PCC's Investment Fund

Purpose

To invest cash balances to achieve best value in terms of return whilst giving primacy to the effective management and control of risk. This means that the security of the principal sums invested and the liquidity of funds will be given priority over yield.

Investment Strategy

1. Funds may be invested in:
    - fixed interest deposits with UK and Overseas banks and UK building societies;
    - the Debt Management Account Deposit Facility provided by central government;
    - pooled money market funds with either a constant net asset value or a variable net asset value;
    - certificates of deposit

    A more detailed definition of approved investment is provided in Annex 3.

2. All investments to be with countries with a sovereign rating of AA- or above. Banks with a UK banking licence will be deemed to be rated according to the UK sovereign rating.

3. Funds to be invested only with counterparties on the approved list.

4. The fund will not invest directly in government bonds, foreign currency or international bonds. The exception to this being the investment in UK government gilts transferred to the Devon and Cornwall Investment Fund following the winding up of segregated fund managed by the external investment manager.

6. Investments for more than one year are classified as non-specified investments. A limit of £20m or 50% of the overall portfolio will be placed on the amount of the fund that can be invested for a period of more than 1 year.

7. The benchmark for performance will be the 3 months LIBID (London Inter Bank Bid Rate).

8. Investment decisions within the policy will be taken by the Treasurer.

Appendix 3

Specified and Non Specfied Investments

Specified Investments	Non Specified Investments
Term deposits with banks and building socities for 365 days or less duration – minimum credit criteria green	Term deposits with banks and building socities for more than 365 days duration – minimum credit criteria green
Certficates of deposit for 365 days or less duration – minimum credit criteria green	
Term deposits with other local authorities for 365 days or less duration	Term deposits with other local authorities for 365 days or more duration
Money Market Funds – with a credit rating of AAA	
Enhanced money market funds – with a credit rating of AAAf	
UK government gilts	

Appendix 4

Capita Asset Services Interest Rate Forecasts

	NOW	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18
BANK RATE	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.75	1.75	2.00
3 month LIBID	0.50	0.50	0.50	0.60	0.80	0.90	1.10	1.10	1.30	1.40	1.50	1.80	1.90	2.10
6 month LIBID	0.65	0.70	0.70	0.80	1.00	1.10	1.20	1.30	1.50	1.60	1.70	2.00	2.10	2.30
12 month LIBID	0.93	0.90	1.00	1.10	1.30	1.40	1.50	1.60	1.80	1.90	2.00	2.30	2.40	2.60
5 yr PWLB	2.00	2.20	2.20	2.30	2.50	2.60	2.80	2.90	3.00	3.20	3.30	3.40	3.50	3.60
10 yr PWLB	2.60	2.80	2.80	3.00	3.20	3.30	3.50	3.60	3.70	3.80	3.90	4.00	4.10	4.20
25 yr PWLB	3.30	3.40	3.50	3.70	3.80	4.00	4.20	4.30	4.40	4.50	4.60	4.70	4.70	4.80
50 yr PWLB	3.30	3.40	3.50	3.70	3.80	4.00	4.20	4.30	4.40	4.50	4.60	4.70	4.70	4.80

Alternative Investments

Type of Investment	Comments
Cash Fund Managers (i.e investment managers who manage an institutions cash by investing according to an agreed manadate across a range of instruments – these are different from Money Market Funds).	Managers with cash/gilt mandates similar to the previous external fund manager find it difficult to provide good returns in the current market environment and for this reason it is not appropriate to seek an alternative cash fund manager.
Enhanced Cash Funds – these are similar to money market fund but the underlying deposits have a longer duration. As a result the value of the investment is more likely to vary as compared to money market funds but under certain conditions the returns can be higher than money market funds	These fund will be approved instruments within the 2015-16 Strategy
Exchange Traded Funds – are investment funds traded on stock exchanges, much like equities.	The value of these investments can go up or down dependent on market conditions. For this reason they are not appropriate for short term investments due to the level of risk. As the PCC's cash position cannot be forecast with certainty over the medium to long term and therefore these are not appropriate investments.
Equities	As exchange traded funds above.
Property funds	The value of property fund investments can can go up or down dependent on market conditions. In addition there can be high entrance and exit costs. For this reason thay must be seen as a medium to long term investment.
Corporate Bonds – longer dated instruments issued by financials and non-financial corporate bodies	These instruments can have higher returns than other investments, however the value of bonds can go up and down. The level of risk inherent in investing in individual corporate bonds does not match the PCC's investment strategy of putting security and liquidity before yield.
Corporate Bond Funds – invest in corporate bonds but diversify the risk by investing in a wide range of corporate bonds.	Corporate bond funds may be an appropriate investment for the PCC however more investigation is required particularly in terms of whether the funds meet legislative requirements in terms of use of derivatives.

Appendix 6

Countries Approved for Investment

AAA

- Australia
- Canada
- Denmark
- Germany
- Luxembourg
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Finland
- Hong Kong
- Netherlands
- U.S.A.
- UK

AA

- Abu Dhabi (UAE)
- France
- Qatar

AA-

- Belgium
- Saudi Arabia

Appendix 7

DEVON AND CORNWALL POLICE
APPROVED LIST OF BORROWERS

	DCPA Lending Limits Counterparty £ millions	Group Limit	Capita Asset Services Classification
1 CLEARING BANKS & SUBSIDIARIES (GROUP Limit £) (term deposits and certificate of deposits)			
BARCLAYS BANK-			
FIBCA Account	12 *	12.25	Red
Current Account	0.25	12.25	N/A
HSBC BANK	12	12	Orange
LLOYDS BANKING GROUP	12	12	Blue
ROYAL BANK OF SCOTLAND	12	12	Blue
SANTANDER	12	12	Red
STANDARD CHARTERED	12	12	Red
NORDEA FINLAND	12	12	Orange
SVENSKA HANDELSBANKEN	12	12	Orange
TORONTO DOMINION BANK	12	12	Orange
DEUTSCHE BANK	12	12	Red
RABOBANK	12	12	Orange
NATIONAL AUSTRALIA BANK	12	12	Orange
GOLDMAN SACHS INTERNATIONAL BANK	12	12	Green
* See Voluntary operational limits below			
2. BUILDING SOCIETIES			
NATIONWIDE	4	4	Red
3. LOCAL AUTHORITIES	5	5	Yellow *
4. DEBT MANAGEMENT ACCOUNT (CENTRAL GOVERNMENT)			
DMA Deposit Facility (DMADF)	Unlimited		Yellow
Treasury Bills	Unlimited		Yellow
5. MONEY MARKET FUNDS			N/A
IGNIS – Sterling Liquidity 2		20	N/A
IGNIS – Short Duration Fund			Pink
Prime Rate – Sterling Liquidity Share Class 4		20	N/A
Prime Rate – Cash Plus Fund			Pink

Key to Sector Classification

Colour	Maximum Length of Deposit
Yellow	Up to 5 years
Purple	Up to 2 years
Blue (applies to nationalised or semi nationalised banks only	Up to 1 year
Orange	Up to 1 year
Red	Up to 6 months
Green	Up to 3 months
Pink	To be used after agreement from a TM meeting
* - Not classified by Capita Asset Services	Up to 1 year

Economic Background

Economic forecasting remains difficult with so many external influences weighing on the UK. Our Bank Rate forecasts, (and also MPC decisions), will be liable to further amendment depending on how economic data transpires over 2015. Forecasts for average earnings beyond the three year time horizon will be heavily dependent on economic and political developments. Major volatility in bond yields is likely to endure as investor fears and confidence ebb and flow between favouring more risky assets i.e. equities, or the safe haven of bonds.

The overall longer run trend is for gilt yields and PWLB rates to rise, due to the high volume of gilt issuance in the UK, and of bond issuance in other major western countries. Increasing investor confidence in eventual world economic recovery is also likely to compound this effect as recovery will encourage investors to switch from bonds to equities.

The overall balance of risks to economic recovery in the UK is currently evenly balanced. Only time will tell just how long this current period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.

The interest rate forecasts in this report are based on an initial assumption that there will not be a major resurgence of the EZ debt crisis. There is an increased risk that Greece could end up leaving the Euro but if this happens, the EZ now has sufficient fire walls in place that a Greek exit would have little immediate direct impact on the rest of the EZ and the Euro. It is therefore expected that there will be an overall managed, albeit painful and tortuous, resolution of any EZ debt crisis that may occur where EZ institutions and governments eventually do what is necessary - but only when all else has been tried and failed. Under this assumed scenario, growth within the EZ will be weak at best for the next couple of years with some EZ countries experiencing low or negative growth, which will, over that time period, see an increase in total government debt to GDP ratios. There is a significant danger that these ratios could rise to the point where markets lose confidence in the financial viability of one, or more, countries, especially if growth disappoints and / or efforts to reduce government deficits fail to deliver the necessary reductions. However, it is impossible to forecast whether any individual country will lose such confidence, or when, and so precipitate a sharp resurgence of the EZ debt crisis. While the ECB has adequate resources to manage a debt crisis in a small EZ country, if one, or more, of the larger countries were to experience a major crisis of market confidence, this would present a serious challenge to the ECB and to EZ politicians.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.

- UK strong economic growth is weaker than we currently anticipate.
- Weak growth or recession in the UK's main trading partners - the EU, US and China.
- A resurgence of the Eurozone sovereign debt crisis.
- Recapitalisation of European banks requiring more government financial support.
- Monetary policy action failing to stimulate sustainable growth and to combat the threat of deflation in western economies, especially the Eurozone and Japan.

The potential for upside risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -

- An adverse reaction by financial markets to the result of the UK general election in May 2015 and the economic and debt management policies adopted by the new government
- ECB either failing to carry through on recent statements that it will soon start quantitative easing (purchase of government debt) or severely disappointing financial markets with embarking on only a token programme of minimal purchases which are unlikely to have much impact, if any, on stimulating growth in the EZ.
- The commencement by the US Federal Reserve of increases in the central rate in 2015 causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities, leading to a sudden flight from bonds to equities.
- A surge in investor confidence that a return to robust world economic growth is imminent, causing a flow of funds out of bonds into equities.
- UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

Treasury Management Governance Arrangements

The PCC is responsible for:

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

The Joint Audit Committee is responsible for:

- scrutinising the treasury management policy and procedures and making recommendations to the PCC.

The Treasurer is responsible for:

- 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.

Police and Crime Commisioner for Devon and Cornwall - External Borrowing

Lender	Term	Maturity Date	Amount Borrowed	Period Outstanding as at 31/3/2015
	Years		£	Years
PWLB	8	02/11/2016	4,500,000	2.59
PWLB	15	01/10/2025	2,000,000	10.51
PWLB	26	03/05/2029	1,697,070	14.10
PWLB	26	03/05/2029	168,930	14.10
PWLB	26	03/05/2029	461,600	14.10
PWLB	26	03/11/2029	2,000,000	14.61
PWLB	20	01/10/2030	2,000,000	15.52
PWLB	26	23/11/2030	2,500,000	15.66
PWLB	25	16/12/2034	2,500,000	19.73
PWLB	31	03/05/2036	6,200,000	21.11
PWLB	31	23/11/2036	2,000,000	21.67
PWLB	30	03/05/2037	4,750,000	22.11
PWLB	25	16/12/2036	4,000,000	24.73
			34,777,600	
Lease Finance			250,000	
Total Debt Finance			35,027,600	