



DORSET

POLICE & CRIME
COMMISSIONER

TREASURY MANAGEMENT & INVESTMENT STRATEGY

2019/20



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1.0 Introduction

- 1.1 This Treasury Management Strategy Statement is for the Police and Crime Commissioner (PCC) for Dorset.
- 1.2 The Police and Crime Commissioner PCC has adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code) which requires the PCC to approve a Treasury Management Strategy before the start of each financial year.
- 1.3 In addition, this strategy also complies with elements of the Local Government Act 2003, the CIPFA Prudential Code, the Ministry of Housing, Communities and Local Government (MHCLG) MRP Guidance and MHCLG Investment Guidance.
- 1.4 This report fulfils the PCC's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the MHCLG Guidance.
- 1.5 Treasury Management is the management of the PCC's cash flows, borrowing and investments, and the associated risks. The PCC funds are exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates as well as ensuring that revenue cash flow is adequately planned and funding is available to meet capital expenditure plans. The successful identification, monitoring and control of financial risk are therefore central to the PCC's prudent financial management.
- 1.6 In accordance with the MHCLG Guidance, the PCC will be asked to approve a revised Treasury Management Strategy Statement should the assumptions on which this report is based change significantly. Such circumstances would include, for example, a large unexpected change; in interest rates; in the PCC's capital programme, or in the level of its investment balances.
- 1.7 The Treasury Management Strategy is integral to the Medium Term Financial Strategy (MTFS) and this document should be read in conjunction with the report on the MTFS for 2019/20 to 2022/23.
- 1.8 This Strategy includes the Borrowing Strategy, the Investment Strategy and Prudential Indicators.

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2.0 Treasury Management Strategy

- 2.1 On 31st March 2018 the PCC held £9.9m of investments and £31.1m of debt.
- 2.2 This is set out in further detail in Appendix 1 Table 1. Forecast changes in these sums are shown in the balance sheet analysis in Appendix 1 Table 2.
- 2.3 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The PCC's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.
- 2.4 Over the forecast period CFR will decrease by the amounts reflecting the reduction in the PFI liabilities, and other capital financing charges (e.g. minimum revenue provision), and will increase by any new unfinanced capital expenditure.
- 2.5 CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that total debt should be lower than the highest forecast CFR over the next three years. Appendix 1 Table 2 shows that the PCC expects to comply with this recommendation during 2019/20.
- 2.6 The current economic background, credit outlook and interest rate forecasts, provided by Arlingclose, is shown at Appendix 5.
- 2.7 For the purpose of setting the budget, it has been assumed that new investments will be made at an average rate of 0.75% and that forecast new borrowing will be undertaken at 2.85%.
- 2.8 **Liability benchmark:** To compare the PCC's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing at Appendix 1 Table 3. This assumes the same forecasts as Appendix 1 Table 2, but that cash and investment balances are kept to a minimum level at each year-end to maintain sufficient liquidity but minimise credit risk.
- 2.9 Following on from the medium-term forecasts in Appendix 1 Table 3, the long-term liability benchmark assumes capital expenditure funded by borrowing of £10.5m over 4 years, minimum revenue provision on new capital expenditure based on various years depending on the type of asset.

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3.0 Borrowing Strategy

3.1 The PCC held £29.9m of PFI loans and £1.2m of other long term loans at the 31 March 2018.

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

3.3 **Strategy:** Given the significant cuts in funding, the PCC borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

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

Alternatively, the PCC may arrange forward starting loans during 2019/20, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

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

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

- Public Works Loan Board (PWLB) and any successor body
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds (except the Police Pension Funds)
- capital market bond investors

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- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

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

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

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

3.6 Short-term and variable rate loans: These loans leave the PCC exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators (see para 7.iii below).

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

4.0 Investment Strategy

4.1 The PCC holds invested funds, representing income received in advance of expenditure plus balances and reserves held. In the first 6 months of the year, the PCC's investment balance has ranged between £0.8m and £26m. These levels are expected to reduce in the forthcoming year.

4.2 Objectives: The CIPFA Code and the MHCLG Guidance requires the PCC to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The PCC's

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objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the PCC will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

- 4.3 **Negative interest rates:** If the UK enters into a recession in 2019/20, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short term investments options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.
- 4.4 **Strategy:** Given the increasing risk and very low returns from short-term unsecured bank investments, the PCC aims to diversify into more secure and where possible higher yielding asset classes during 2019/20.
- 4.5 **Business Model:** Under the new IFRS 9 standard, the accounting for certain investments depends on the PCC's "business model" for managing them. The PCC aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.
- 4.6 **Approved counterparties:** The PCC may invest its surplus funds with any of the counterparty types shown in Appendix 2 Table 4, subject to the cash limits (per counterparty) and the time limits shown. Appendix 2 Table 5 and 6 contains more detailed information on specific counterparties and limits.
- 4.7 **Credit rating:** Investment limits are set by reference to the lowest published long-term credit rating from a selection of external rating agencies. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.
- 4.8 **Banks unsecured:** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail (see below for arrangements relating to operational bank accounts).

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- 4.9 **Banks secured:** Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.
- 4.10 **Government:** Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.
- 4.11 **Corporates:** 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 and only following an external credit assessment.
- 4.12 **Registered providers:** Loans and bonds issued by, guaranteed by or secured on the assets of registered providers of social housing and registered social landlords, formerly known as housing associations. These bodies are tightly regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department of Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.
- 4.13 **Pooled funds:** Shares or units in diversified investment vehicles consisting of any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity and very low or no volatility will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

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

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meeting the PCC's investment objectives will be monitored regularly. Any such investment would require the explicit approval of the Police and Crime Commissioner.

4.14 Operational bank accounts: The PCC's operational bank account is held with NatWest. The PCC may incur operational exposures, for example through current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but are still subject to the risk of a bank bail-in, and balances will therefore be kept below £1.25m per bank. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the PCC maintaining operational continuity.

4.15 Risk assessment and credit ratings: Credit ratings are obtained and monitored by the PCC'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.

4.16 Other information on the security of investments: The PCC understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press and analysis and advice from the PCC's treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the credit rating criteria.

When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in

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credit ratings, but can be seen in other market measures. In these circumstances, the PCC will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the PCC's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

4.16 Specified investments: The MHCLG Guidance defines specified investments as those:

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement,
- not defined as capital expenditure by legislation, and
- invested with one of:
 - the UK Government,
 - a UK local authority, parish council or community council, or
 - a body or investment scheme of “high credit quality”.

The PCC defines “high credit quality” organisations and securities as those having a credit rating of [A-] or higher that are domiciled in the UK or a foreign country with a sovereign rating of [AA+] or higher. For money market funds and other pooled funds “high credit quality” is defined as those having a credit rating of [A-] or higher.

4.17 Non-specified investments: Any investment not meeting the definition of a specified investment is classed as non-specified. The PCC does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in Appendix 2 Table 7.

4.18 Investment limits: The PCC's revenue reserves available to cover investment losses are forecast to be £6.5m on 31st March 2019. In order that no more than 8% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £0.5m for unsecured funds. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign

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countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries. Investment limits are shown in Appendix 2 Table 8.

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

5.0 2018 MHCLG Investment Guidance

5.1 The contribution that Treasury Management Investments make to the objectives of the PCC group is to support effective treasury management activities.

5.2 The statutory guidance issued by MHCLG in January 2018 requires authorities to report also on their investment strategy with regard to the following purposes:

- To support local public services by lending to or buying shares in other organisations (service investments), and
- To earn investment income (known as commercial investments where this is the main purpose)

5.3 The PCC does not have any current plans for such investments. Should these plans change in the future a full assessment will be made and an appropriate Investment Strategy Report will be prepared.

5.2 Financial guarantees are not strictly counted as investments, since no money has exchanged hands yet, but they do carry risks. The PCC is being asked, along with all other PCCs, to provide a financial guarantee for the Police ICT company amounting to c. £53,000 for Dorset. This would be covered within the General Fund Balance reserve.

6.0 Prudential Indicators

6.1 The Local Government Act 2003 requires the PCC to have regard to the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of the PCC are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the PCC has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year:

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i) Estimates of Capital Expenditure: The PCC's planned capital expenditure and financing is shown in Table 9 in Appendix 3 as well as the **estimates of Capital Financing Requirement:** The Capital Financing Requirement (CFR) (Table 10 in Appendix 3) measures the PCC's underlying need to borrow for a capital purpose.

ii) Gross Debt and the Capital Financing Requirement: In order to ensure that over the medium term debt will only be for a capital purpose, the PCC should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence which is shown in Appendix 3 Table 11.

Total debt for the PCC is expected to remain below the CFR during the forecast period.

iii) Operational Boundary for External Debt: The operational boundary shown in Appendix 3 Table 12 is based on the PCC's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the PCC's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring. Other long-term liabilities comprise finance lease, Private Finance Initiative and other liabilities.

iv) Authorised Limit for External Debt: The authorised limit shown in Appendix 3 Table 13 is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the PCC can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

v) Ratio of Financing Costs to Net Revenue Stream: This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income. This is shown in Appendix 3 Table 14.

7.0 Treasury Management Indicators

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

i) Security: The PCC has adopted a voluntary measure of its exposure to credit risk by monitoring the weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each

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investment. Unrated investments are assigned a score based on their perceived risk.

	Target
Portfolio average credit rating	A+

ii) Liquidity: Minimum limits are set for short term cash in order that sufficient liquidity is available to meet unexpected variation in the cash flow:

	Target
Minimum limit at less than 31 days duration	£9m
Minimum limit overnight	£3m

iii) Interest rate exposures: This indicator is set to control the PCC's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the amount of net interest payable will be:

	2019/20
	Limit
Upper limit on 1 year revenue impact of a 1% rise in interest rates	£1k
Upper limit on 1 year revenue impact of a 1% fall in interest rates	£1k

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

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

	Upper	Lower
Under 12 months	50%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	50%	0%
10 years and above	100%	0%

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

v) Principal sums invested for periods longer than a year: The purpose of this indicator is to control the PCC's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end will be:

PCC	2019/20	2020/21	2021/22	2022/23
Limit on principal invested beyond year end	£1m	£1m	£1m	£1m

8.0 Other Items

8.1 The CIPFA Code and MHCLG requires the PCC to also include the items below in its Treasury Management Strategy.

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

8.3 **Investment training:** The needs of the PCC's treasury management staff for training in investment management are assessed on an ongoing basis and as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change.

Staff attend internal training courses and/or training courses, seminars and conferences provided by Arlingclose and CIPFA.

8.4 **Investment advisers:** The PCC has appointed Arlingclose Limited as treasury management advisers and receives specific advice on investment, debt and capital finance issues.

8.5 **Investment of money borrowed in advance of need:** The PCC may, from time to time, borrow in advance of need, where this is expected to provide the best long-term value for money. Since amounts borrowed will be invested until spent, the PCC is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the PCC's overall management of its treasury risks.

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The total amount borrowed will not exceed the authorised borrowing limit of £42m. The maximum period between borrowing and expenditure is expected to be two years, although the PCC is not required to link particular loans with particular items of expenditure.

8.6 The Minimum Revenue Provision (MRP) Policy Statement is shown in Appendix 4. MRP is an amount charged to the revenue budget for the repayment of debt. The Local Government Act 2003 requires the PCC to have regard to the MHCLG Guidance on Minimum Revenue Provision, most recently issued in 2018.

9.0 Financial Implications

9.1 The budget for investment income in 2019/20 is £40k, based on an average investment portfolio of £5m at an interest rate of 0.75%. If actual levels of investments and borrowing, and actual interest rates differ from those forecast, performance against budget will be correspondingly different.

10.0 Other Options Considered

10.1 The MHCLG Guidance and the CIPFA Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Treasurer, having consulted the Police and Crime Commissioner believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are considered below.

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

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Alternative	Impact on income and expenditure	Impact on risk management
long-term fixed rates		broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

11.0 Governance Arrangements

11.1 The Treasury Management governance arrangements are set out in Appendix 6.

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INVESTMENTS

Appendix 1

Table 1

Existing Investment & Debt Portfolio Position

	31st March 2018 Actual Portfolio £'000
External Borrowing:	
Total External Borrowing	0
Other Long-Term Liabilities:	
Private Finance Initiative	(29,885)
Other long term liabilities	(1,205)
Total Other Long-Term Liabilities	(31,090)
Total Gross External Debt	(31,090)
Treasury Investments:	
Short-term investments	3,005
Cash and cash equivalents	6,928
Total Treasury Investments	9,933
Net Debt	(21,157)

Table 2

Balance Sheet Summary and Forecast

	31.3.18	31.3.19	31.3.20	31.3.21	31.3.22	31.3.23
	Actual	Estimate	Forecast	Forecast	Forecast	Forecast
	£'000	£'000	£'000	£'000	£'000	£'000
Total Capital Financing Requirement	32,781	30,375	31,575	33,344	33,205	29,961
Less: PFI Liabilities	(29,885)	(27,979)	(25,975)	(24,802)	(24,563)	(22,508)
Less: Other Long Term Liabilities	(1,205)	(1,086)	(966)	(846)	(727)	(607)
Internal Borrowing	1,691	1,311	4,634	7,696	7,915	6,846
Usable Reserves	9,993	6,482	6,188	7,238	7,238	7,238
Working Capital	1,631	1,600	1,600	1,600	1,600	1,600
Total Funds	11,624	8,082	7,788	8,838	8,838	8,838
Investments (Funds less internal borrowing)	9,933	6,771	3,154	1,142	923	1,992

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Appendix 1

Table 3

Liability Benchmark

	31.3.18	31.3.19	31.3.20	31.3.21	31.3.22	31.3.23
	Actual	Estimate	Forecast	Forecast	Forecast	Forecast
	£'000	£'000	£'000	£'000	£'000	£'000
Total Capital Financing Requirement	32,781	30,375	31,575	33,344	33,205	29,961
Less: Usable Reserves	(9,993)	(6,482)	(6,188)	(7,238)	(7,238)	(7,238)
Less: Working Capital	(1,631)	(1,600)	(1,600)	(1,600)	(1,600)	(1,600)
Plus: Minimum Investments	3,000	3,000	3,000	3,000	3,000	3,000
Liability Benchmark	24,157	25,293	26,787	27,506	27,367	24,123

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Appendix 2

**Table 4
Counterparty Types**

Credit Rating	Banks Unsecured	Banks Secured	Government	Corporates	Registered Providers
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£0.5m 5 years	£1m 20 years	£1m 50 years	£0.35m 20 years	£0.5m 20 years
AA+	£0.5m 5 years	£1m 10 years	£1m 25 years	£0.35m 10 years	£0.5m 10 years
AA	£0.5m 4 years	£1m 5 years	£1m 15 years	£1m 5 years	£0.5m 10 years
AA-	£0.5m 3 years	£1m 4 years	£1m 10 years	£1m 3 years	£0.5m 10 years
A+	£0.5m 2 years	£1m 3 years	£0.5m 5 years	£1m 3 years	£0.5m 5 years
A	£0.5m 13 months	£1m 2 years	£0.5m 5 years	£1m 2 years	£0.5m 5 years
A-	£0.5m 6 months	£1m 13 months	£0.5m 5 years	£1m 13 months	£0.5m 5 years
None	£0.15m 6 months	n/a	£0.5m 25 years	£1m 5 years	£0.5m 5 years
Pooled funds	£0.5m per fund				

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INVESTMENT STRATEGY

Appendix 2

**Table 5
Counterparties and Limits**

Approved List of Counterparties to Invest with:						
	UK	Unsecured £m	Secured £m	Group		Duration Unsecured
				Unsecured £m	Secured £m	
Lloyd Banking Group:				0.5	1	
Bank of Scotland	Yes	0.5	1			6 months
Lloyds Bank PLC	Yes	0.5	1			6 months
HSBC Bank	Yes	0.5	1			6 months
Bank of Montreal		0.5	1			6 months
Bank of Nova Scotia		0.5	1			6 months
Canadian Imperial Bank of Commerce		0.5	1			6 months
Royal Bank of Canada		0.5	1			6 months
Toronto Dominion Bank		0.5	1			6 months
Cooperatieve Rabobank		0.5	1			13 months
DBS Bank LTD		0.5	1			13 months
Oversea-Chinese Banking Corporation		0.5	1			13 months
United Oversea Bank		0.5	1			13 months
Nordea Bank AB Svenska Handlebanken		0.5	1			6 months
Close Brother Limited		0.5	1			6 months
Santander UK PLC	Yes	0.5	1			6 months
Australia and New Zealand Banking Group		0.5	1			6 months
Commonwealth Bank of Australia		0.5	1			6 months
National Australia Bank		0.5	1			6 months
Westpac Banking Group		0.5	1			6 months
Landesbank Hessen-Thuringen (Helaba)		0.5	1			6 months
Nationwide Building Society	Yes	0.5	1			6 months
Coventry Building Society	Yes	0.5	1			6 months
Standard Chartered Op Corporate	Yes	0.5	1			6 months
Bayerische Landesbank		0.5	1			6 months
DZ Bank		0.5	1			6 months

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Approved List of Counterparties to Invest with:						
	UK	Unsecured £m	Secured £m	Group		Duration Unsecured
				Unsecured £m	Secured £m	
Landesbank Baden Wuerttemberg		0.5	1			6 months
Danske Bank		0.5	1			100 days
ING Bank		0.5	1			100 days
Barclays Bank	Yes	0.5	1			100 days
Goldman Sachs International Bank	Yes	0.5	1			100 days
Leeds Building Society	Yes	0.5	1			100 days
Credit Suisse		0.5	1			100 days
Darlington BS	Yes	0.5	1			100 days
Furness BS	Yes	0.5	1			100 days
Harpenden BS	Yes	0.5	1			100 days
Hinckley & Rugby BS	Yes	0.5	1			100 days
Leek United BS	Yes	0.5	1			100 days
Mansfield BS	Yes	0.5	1			100 days
Marsden BS	Yes	0.5	1			100 days
Melton Mowbray BS	Yes	0.5	1			100 days
National Counties BS	Yes	0.5	1			100 days
Newbury BS	Yes	0.5	1			100 days
Scottish BS	Yes	0.5	1			100 days
Tipton & Coseley BS	Yes	0.5	1			100 days
RBS Banking Group				0.5	1	
National	Yes	0.5	1			100 days
Westminster Bank PLC	Yes	0.5	1			100 days
Royal Bank of Scotland	Yes	0.5	1			100 days

The table has been updated with additional counterparties recommended by Arlingclose.

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**Table 6
Counterparties and Limits**

High Quality Bond Issuers			
Country	Counterparty	Max Duration	Max Amount
Supra	Council of Europe Development Bank	15 years	£1m
Supra	European Bank for Reconstruction & Development	25 years	£1m
Supra	European Coal & Steel Community	25 years	£1m
Supra	European Investment Bank	25 years	£1m
Supra	Inter-American Development Bank	25 years	£1m
Supra	International Bank for Reconstruction & Development Bank	25 years	£1m
Supra	International Finance Corp	25 years	£1m
Supra	Nordic Investment Bank	25 years	£1m
Australia	New South Wales Treasury Corporation	25 years	£1m
Canada	Export Development Canada	25 years	£1m
Denmark	Kommunekredit	15 years	£1m
Finland	Finnish Government	15 years	£1m
Finland	Municipality Finance plc	15 years	£1m
Germany	FMS Wertmanagement	25 years	£1m
Germany	KfW	25 years	£1m
Germany	Landeskreditbank Baden-Württemberg - Förderbank	25 years	£1m
Germany	Landwirtschaftliche Rentenbank	25 years	£1m
Germany	State of Saxony-Anhalt	15 years	£1m
Netherlands	Bank Nederlandse Gemeenten	5 years	£1m
Netherlands	Nederlandse Waterschapsbank NV	5 years	£1m
Norway	Kommunalbanken AS	5 years	£1m
Singapore	Temasek Financial (I) Ltd	10 years	£1m
Sweden	Svensk Exportkredit AB	5 years	£1m
UK	LCR Finance plc	15 years	£1m
UK	Network Rail Infrastructure Finance plc	15 years	£1m
UK	Transport for London	10 years	£1m
UK	Wellcome Trust Finance plc	20 years	£1m

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**Table 7
Non-Specified Investment Limits**

	Cash limit
Total long-term investments	£1m
Total investments without credit ratings or rated below [A-] (except UK Government and local authorities)	£0.5m
Total investments (except pooled funds) with institutions domiciled in foreign countries rated below [AA+]	£0.5m
Total non-specified investments	£12m

**Table 8
Investment Limits**

	2019/20 Cash Limit
Any single organisation, except the UK Government	£1m each (£0.5m unsecured funds)
Any group of organisations under the same ownership	£1m per Group (£0.5m unsecured funds)
Any group of pooled funds under the same management	£1m per manager
Negotiable instruments held in a broker's nominee account	£12m per Broker
Limit per non-UK country	£1m per country
Registered providers	£3m in Total
Unsecured investments with building societies	£3m in Total
Money Market Funds	£12m in Total
Bank Account	£1.25m

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PRUDENTIAL INDICATORS

Appendix 3

**Table 9
Estimates of Capital Expenditure**

	2018/19	2019/20	2020/2021	2021/22	2022/23
	Forecast	Estimate	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000	£'000
Total Expenditure	6,213	10,845	6,180	3,735	4,728
Capital Receipts	5,062	5,250	580	200	2,200
Government Grants	412	412	412	412	412
Reserves	203	0	0	0	0
Revenue	386	1300	1300	1300	1216
Borrowing	150	3,883	3,888	1,823	900
Leasing and PFI	0	0	0	0	0
Total Financing	6,213	10,845	6,180	3,735	4,728

**Table 10
Capital Financing Requirement**

	2018/19	2019/20	2020/2021	2021/22	2022/23
	Forecast	Estimate	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000	£'000
Opening CFR	32,781	30,375	31,575	33,344	33,205
Capital expenditure to be funded by borrowing	150	3,883	3,888	1,823	900
Less: Repayment of PFI	(1,906)	(2,004)	(1,173)	(238)	(2,056)
Less: Repayment of Other Long Term Liabilities	(120)	(120)	(120)	(120)	(119)
Less: Minimum Revenue Provision	(530)	(560)	(826)	(1,604)	(1,969)
Closing CFR	30,375	31,575	33,344	33,205	29,961

**POLICE AND CRIME COMMISSIONER FOR DORSET
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PRUDENTIAL INDICATORS

Appendix 3

**Table 11
Total Debt**

Debt	2018/19	2019/20	2020/2021	2021/22	2022/23
	Forecast	Estimate	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000	£'000
PFI liabilities	27,979	25,975	24,802	24,563	22,508
Other Long Term Liabilities	1,086	966	846	727	607
Borrowing	1,311	4,634	7,696	7,915	6,846
Total Debt	30,375	31,575	33,344	33,205	29,961

**Table 12
Operational Boundary for External Debt**

Operational Boundary	2018/19	2019/20	2020/2021	2021/22	2022/23
	Forecast	Estimate	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000	£'000
PFI and Other long-term liabilities	29,064	26,941	25,648	25,290	23,115
Maximum forecast cashflow deficit arising from revenue budget operations	10,000	10,000	10,000	10,000	10,000
Total Operational Boundary	39,064	36,941	35,648	35,290	33,115

**Table 13
Authorised Limit for External Debt**

Authorised Limit	2018/19	2019/20	2020/2021	2021/22	2022/23
	Forecast	Estimate	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000	£'000
Total Operational Boundary Debt	39,064	36,941	35,648	35,290	33,115
Additional margin for unforeseen circumstances	5,000	5,000	5,000	5,000	5,000
Total Authorised Limit	44,064	41,941	40,648	40,290	38,115

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PRUDENTIAL INDICATORS

Appendix 3

Table 14
Ratio of Financing Costs to Net Revenue Stream

	2018/19 Revised %	2019/20 Estimate %	2020/21 Estimate %	2021/22 Estimate %	2022/23 Estimate %
Ratio of Financing Costs to Net Revenue Stream	0	0	0	0	0

This is based on an internal borrowing assumption.

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MINIMUM REVENUE PROVISION

Appendix 4

Annual Minimum Revenue Provision Statement 2019/20

Where the PCC finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the PCC to have regard to the Ministry of Housing, Communities and Local Government's (MHCLG) Guidance on Minimum Revenue Provision. The broad aim of the MHCLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits.

The MHCLG Guidance requires the PCC to approve an Annual MRP Statement each year, and provides four options for calculating an amount to put aside to revenue over time to cover the CFR i.e. the MRP. The PCC has opted for option 3; the Asset Life Method. The Asset Life Method determines that MRP is calculated on the basis of charging the unfinanced capital expenditure over the expected useful life of the relevant assets based on either an equal instalment method or an annuity method. The PCC has opted for the equal instalment method. This is applied from the year after the asset becomes operational. For assets acquired by finance leases, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.

The PCC can choose to make more MRP than considered the prudent minimum.

The maximum asset life used in MRP calculations is 50 years, unless a longer life is certified by an appropriately qualified professional adviser, or the asset has been acquired on a lease of longer than 50 years. For those assets purchased before 1st April 2018 that have an asset life of more than 50 years, the Code does not require a retrospective adjustment.

Based on the PCC's latest estimate of its Capital Financing Requirement on 31st March 2019, the budget for MRP has been set as follows:

	2019/20 Estimated CFR £'000	2019/20 Estimated MRP £'000
Unsupported capital expenditure after 31.03.2008	31,575	560

**POLICE AND CRIME COMMISSIONER FOR DORSET
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ECONOMIC CONTEXT

Appendix 5

Arlingclose Economic & Interest Rate Forecast October 2018

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

Following a weak reading in the first quarter of 2018 attributed to weather-related factors, UK GDP growth rebounded in the second quarter to 0.4%, but at an annual rate of only 1.2% this remains below trend. As economic growth had evolved broadly in line with its May Inflation Report forecast, the Bank of England's Monetary Policy Committee (MPC) voted unanimously for a rate rise of 0.25% in August, taking Bank Rate to 0.75%. In November 2018 the MPC maintained Bank Rate at 0.75% while the Inflation Report showed that compared to the August report further interest rate increases may be required to bring inflation down to the 2% target over the forecast horizon.

The headline rate of UK Consumer Price Inflation fell back to 2.4% year-on-year in September 2018 from 2.7% in August, as higher import and energy prices continued to hold inflation above the BoE target. Labour market data is positive. The ILO unemployment rate fell to 4%, its lowest level since 1975. The 3-month average annual growth rate for pay excluding bonuses rose to 3.1% in August providing some evidence that a shortage of labour is supporting wages. However, adjusting for inflation this means real wages were only up by 0.7% and only likely to have a moderate impact on household spending.

While external inflationary pressures from energy costs and import prices are expected to subside, domestic pressures are projected to build over the forecast horizon with the balance of these effects likely to keep inflation above the Bank of England's target throughout most of their forecast horizon, meaning that strong real income growth is unlikely to materialise any time soon.

As the US economy has continued to perform well, the Federal Reserve maintained its monetary tightening stance and pushed up its target range for the Fed Funds Rate in September 2018 by 0.25% to 2% - 2.25%. One further rise is expected in 2018 and two more in 2019. The fallout from the US-China trade war continues which, combined with tighter monetary policy, risks contributing to a slowdown in global economic activity in 2019. Despite slower growth in the region, the European Central Bank has started conditioning markets for the end of quantitative easing as well as the timing of the first interest rate hike, currently expected in 2019, and the timing and magnitude of increases thereafter.

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ECONOMIC CONTEXT

Appendix 5

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

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

Interest rate forecast: Following the increase in Bank Rate to 0.75% in August 2018, the Authority's treasury management adviser Arlingclose is forecasting two more 0.25% hikes during 2019 to take official UK interest rates to 1.25%. The Bank of England's MPC has maintained expectations for slow and steady rate rises over the forecast horizon. The MPC continues to have a bias towards tighter monetary policy but is reluctant to push interest rate expectations too strongly. Arlingclose believes that MPC members consider both that ultra-low interest rates result in other economic problems, and that higher Bank Rate will be a more effective policy weapon should downside Brexit risks crystallise when rate cuts will be required.

The UK economic environment remains relatively soft, despite seemingly strong labour market data. Arlingclose's view is that the economy still faces a challenging outlook as it exits the European Union and Eurozone growth softens. Whilst assumptions are that a Brexit deal is struck and some agreement reached on transition and future trading arrangements before the UK leaves the EU, the possibility of a "no deal" Brexit still hangs over economic activity. As such, the risks to the interest rate forecast are considered firmly to the downside.

Gilt yields and hence long-term borrowing rates have remained at low levels but some upward movement from current levels is expected based on Arlingclose's interest rate projections, due to the strength of the US economy and the ECB's forward guidance on higher rates. 10-year and 20-year gilt yields are forecast to remain around 1.5% and 2% respectively over the interest rate forecast horizon, however volatility arising from both economic and political events are likely to continue to offer borrowing opportunities.

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GOVERNANCE ARRANGEMENTS

Appendix 6

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 Independent 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.