APPENDIX A

OFFICE OF THE POLICE AND CRIME COMMISSIONER FOR GWENT

Treasury Management Strategy 2023/24 to 2025/26

1 INTRODUCTION

1.1 Treasury Management is the management of the organisation's borrowing, investments and cash flows, including its banking, money market and capital market transactions; the effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks. The treasury management service is an important part of the overall financial management of the Police and Crime Commissioner's (Commissioner) affairs. The Commissioner is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Commissioner's low risk appetite, providing adequate liquidity initially, before considering investment return. The second main function of the treasury management service is the funding of the Commissioner's capital plans. These capital plans provide a guide to the borrowing need of the Commissioner, essentially the longer term cash flow planning to ensure that the Commissioner can meet his capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion, any debt previously drawn may be restructured to meet the Commissioner's risk or cost objectives.

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

1.3 The Prudential Code 2017 introduced a new requirement for local authorities (including Commissioners) to produce a Capital Strategy. It is for local authorities to decide whether to include their treasury management strategy and annual investment strategy as part of a Capital Strategy or to complete separately. Since the first year of operation, the Commissioner has elected to complete a separate four-year Capital Strategy which was last completed at the conclusion of the budget setting process in February 2022 and approved before the commencement of the 2022/23 financial year. The Capital Strategy will next be updated for the commencement of the 2025/26 financial year.

1.4 The adoption of a Treasury Management Strategy for 2023/24, prior to the start of the financial year, is the first of the three reporting requirements in respect of that year. This will be followed in due course by a mid-year

Treasury Management report and an Annual Treasury Management Report before 30th September 2024, providing a selection of actual prudential and treasury indicators.

1.5 The Treasury Management Strategy for 2023/24 covers two main areas:

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

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

2. CAPITAL PRUDENTIAL INDICATORS 2023/24 to 2025/26

2.1 The Local Government Act 2003 requires the Commissioner to adopt the CIPFA Prudential Code, which was updated in 2021, and produce prudential indicators. Each indicator either summarises the expected capital activity or introduces limits upon that activity, and reflects the outcome of the underlying capital appraisal systems. This document updates currently approved indicators.

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

2.3 Capital Expenditure Plans

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

2.3.2 This unsupported capital expenditure needs to have regard to:

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

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

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

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

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

First Prudential Indicator - Estimates of Capital Expenditure					
	2022/23 Original £000's	**2022/23 Revised £000's**	**2023/24 Estimate £000's**	**2024/25 Estimate £000's**	**2025/26 Estimate £000's**
Capital Expenditure	**17,944**	**17,417**	**23,902**	**21,739**	**15,931**
Financed by:					
Capital Receipts	210	0	0	0	0
Capital Grants and PIF Grants	120	14	14	0	0
Reserves	6,580	9,336	6,662	140	852
Revenue	7,179	8,067	6,226	6,599	7,079
Net Financing Need for the Year	**3,855**	**0**	**11,000**	**15,000**	**8,000**

2.3.7 The above financing need excludes other long-term liabilities, such as Private Finance Initiative (PFI) and leasing arrangements which already include borrowing instruments. The table above identifies the financial requirements for the delivery of the Commissioner's draft Estate Strategy (which is still being finalised post review), which includes the investment in the transformation of operational policing presence into a 'Hub and Spoke' model, and a new Joint Firearms Range in collaboration with South Wales Police and Dyfed Powys Police, resulting in a borrowing need from 2023/24 onwards. During 2023/24, the Capital Programme will be funded from a combination of capital grant, revenue contributions to capital and committed funds in addition to borrowing.

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

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

2.4.2 The CFR includes any other long term liabilities (e.g. PFI schemes) brought onto the balance sheet. Whilst this increases the CFR, and therefore the Commissioner's borrowing requirement, these types of scheme include a borrowing facility and so the Commissioner is not required to borrow separately for these schemes.

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

Second Prudential Indicator - the Capital Financing Requirement (CFR)					
	2022/23 Original £000's	**2022/23 Revised £000's**	**2023/24 Estimate £000's**	**2024/25 Estimate £000's**	**2025/26 Estimate £000's**
Opening CFR	0	0	0	10,560	25,568
Capital Spend	17,944	17,417	23,902	21,739	15,931
Movement In finance lease liability	1,089	0	0	608	(107)
Resources Used	(14,089)	(17,417)	(12,902)	(6,739)	(7,931)
MRP		0	(440)	(600)	(320)
Closing CFR	**4,944**	**0**	**10,560**	**25,568**	**33,141**

2.4.4 The adoption of International Financial Reporting Standard (IFRS) 16 – 'Accounting for Leases' should have commenced at the 1st April 2021, which would have already impacted on the calculation of the Commissioner's CFR within this Strategy. However, in late November 2020 as a result of the Coronavirus pandemic, the adoption of this Standard has been delayed for a year and should have taken effect from 1st April 2022, but was then delayed a further two years and will now commence 1st April 2024. The table above shows the impact of the implementation of IFRS 16 with a net increase in the financial lease liability of £608,318. This represents the initial recognition of £713,150 as a finance lease liability under IFRS 16 plus a decrease due to the in-year lease payments. The above figures were estimates calculated with information available at the 31st October 2022 and will therefore be subject to change.

2.4.5 In line with the latest MRP guidance, the Commissioner will be required to make a MRP in 2023/24. The Commissioner's policy on this matter is therefore at section 3 below.

3. MINIMUM REVENUE PROVISION POLICY

3.1 The Commissioner is required to recognise an element of outstanding capital borrowing each year through a revenue charge known as the MRP. The MRP is calculated to match the repayment of borrowing over the life of the assets, for which debt has been raised and is charged in the following year after the asset becomes operational. It is also permissible to pay an additional amount known as a Voluntary Revenue Provision (VRP). Under Welsh Government (WG) Regulations the Commissioner has to approve an MRP Statement in advance of each year. The Commissioner is recommended to adopt the following MRP policy for 2023/24:

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

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

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

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

Investment Position - Year end Resources					
	2022/23 Original £000's	**2022/23 Revised £000's**	**2023/24 Estimate £000's**	**2024/25 Estimate £000's**	**2025/26 Estimate £000's**
Police Fund	5,000	5,000	5,000	5,000	5,000
Earmarked Reserves	17,232	19,565	6,878	6,238	5,586
Provisions	1,537	1,720	1,720	1,720	1,720
Total Core Funds	**23,769**	**26,285**	**13,598**	**12,958**	**12,306**
Working Capital	5,590	679	679	679	679
Expected Investments	**29,359**	**26,964**	**14,277**	**13,637**	**12,985**

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

5. AFFORDABILITY PRUDENTIAL INDICATORS

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

5.2 The third prudential indicator is the ratio of net financing costs (financing income less finance interest expense) to net revenue stream. This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream:

Third Prudential Indicator - Ratio of Financing Costs to Net Revenue Stream					
	2022/23 Original %	2022/23 Revised %	2023/24 Estimate %	2024/25 Estimate %	2025/26 Estimate %
Ratio	**0.06**	**0.00**	**0.43**	**1.27**	**1.65**

5.3 The estimates of financing costs include current commitments and the proposals in the budget report. The ratio turns positive in 2023/24 as interest expense will be payable on newly borrowed debt, at this point forecast interest expense will be greater than interest income.

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

Fourth Prudential Indicator - Incremental Increase in Council Tax Precept			
	2023/24 Estimate £	2024/25 Estimate £	2025/26 Estimate £
Increase	**5.87**	**6.26**	**3.24**

5.5 The 2021 CIPFA Prudential Code introduced a new Prudential Indicator to address the risks associated with investments for commercial purposes, to ensure they are proportionate to the local authority's financial capacity. As a minimum, the local authority will estimate for the forthcoming financial year and the following two financial years the proportion of net income from commercial and service investments compared to budgeted net revenue stream.

5.6 Net income from commercial and service investments comprises net income from financial investments (other than treasury management investments), together with net income from other assets held primarily for financial return, such as commercial property. Based on this definition, the Commissioner hold no commercial and service investments.

6. BORROWING

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

6.2 **Current borrowing portfolio position**

The current treasury borrowing position at 30th September 2022, with forward projections, are summarised below. The below table shows the actual and forecasted external debt (the treasury management operations), against the future underlying capital borrowing need (the CFR), highlighting any over or under borrowing:

Borrowing Position					
	2022/23 Original £000's	**2022/23 Revised £000's**	**2023/24 Estimate £000's**	**2024/25 Estimate £000's**	**2025/26 Estimate £000's**
External Debt					
Debt at 1st April	0	0	0	11,000	26,000
Expected Change in Debt	3,855	0	11,000	15,000	8,000
Other Long-Term Liabilities (Finance Lease Liability) at 1st April	1,352	0	0	713	608
Expected Change in OLTL	(262)	0	0	(105)	(107)
Gross Debt at 31st March	**4,944**	**0**	**11,000**	**26,608**	**34,501**
Capital Financing Requirement at 31st March	0	0	10,560	25,568	33,141
Under/(Over) Borrowing	**(4,944)**	**0**	**(440)**	**(1,040)**	**(1,360)**

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

Impact on Revenue Budgets					
	2022/23 Original £000's	**2022/23 Revised £000's**	**2023/24 Estimate £000's**	**2024/25 Estimate £000's**	**2025/26 Estimate £000's**
Revenue Budget Heading					
Interest on Borrowing	148	0	653	1,444	1,780
Investment Income	(50)	0	(400)	(286)	(205)
Net Police Fund Borrowing Cost	**98**	**0**	**253**	**1,158**	**1,576**

7. LIMITS ON BORROWING ACTIVITY

7.1 Within the prudential indicators there are a number of key indicators to ensure that the Commissioner operates activities within well-defined limits. For the first of these the Commissioner needs to ensure that gross debt does not, except in the short term, exceed the total of the CFR in the preceding year, plus the estimates of any additional CFR for 2023/24 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes. The following table is relevant for this indicator:

Limits on Borrowing Activity - Year End Position					
	2022/23 Original £000's	**2022/23 Revised £000's**	**2023/24 Estimate £000's**	**2024/25 Estimate £000's**	**2025/26 Estimate £000's**
Gross Debt	**4,944**	**0**	**11,000**	**26,608**	**34,501**
Investments	(29,359)	(26,964)	(14,277)	(13,637)	(12,985)
Net Borrowing	(24,415)	(26,964)	(3,277)	12,971	21,516
Capital Financing Requirement	**4,944**	**0**	**10,560**	**25,568**	**33,141**
Gross Debt <= CFR	**Yes**	**Yes**	**No**	**No**	**No**

Note: Gross Debt is greater than the CFR by the MRP amount and therefore does not raise a concern.

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

Operational Boundary for Debt at 1st April					
	2022/23 Original £000's	**2022/23 Revised £000's**	**2023/24 Estimate £000's**	**2024/25 Estimate £000's**	**2025/26 Estimate £000's**
Debt	3,855	0	11,000	26,000	34,000
Other Long-Term Liabilities	1,352	0	0	608	501
Net Borrowing	**5,207**	**0**	**11,000**	**26,608**	**34,501**

7.3 A further key prudential indicator representing a control on the overall level of borrowing is the Authorised Limit for External Debt. This is calculated on a 5% mark up on the operational boundary. This represents a limit beyond which external debt is prohibited and this limit needs to be set or revised by the Commissioner. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total plans of all Local Authorities and Commissioners, or those of a specific Authority or Commissioner, although no control has yet been exercised. The Commissioner is asked to approve the following Authorised Limit:

Authorised Limit for Debt at 1st April					
	2022/23 Original £000's	2022/23 Revised £000's	2023/24 Estimate £000's	2024/25 Estimate £000's	2025/26 Estimate £000's
Debt	4,047	0	11,550	27,300	35,700
Other Long Term Liabilities	1,352	0	0	608	501
Working Capital Requirement	5,590	679	679	679	679
Authorised Limit	10,989	679	12,229	28,587	36,880

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

8. PROSPECTS FOR INTEREST RATES

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

LINK Group

UK Interest Rate Forecast

	NOW	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
Bank Rate														
Link Group	3.00%	3.50%	4.25%	4.50%	4.50%	4.50%	4.00%	3.75%	3.50%	3.25%	3.00%	2.75%	2.50%	2.50%
Capital Economics	3.00%	3.75%	4.75%	5.00%	5.00%	5.00%	4.75%	4.25%	3.75%	3.25%	-	-	-	-
5yr PWLB Rate														
Link Group	4.09%	4.30%	4.30%	4.20%	4.10%	4.00%	3.90%	3.80%	3.60%	3.50%	3.40%	3.30%	3.20%	3.10%
Capital Economics	4.09%	4.50%	4.30%	4.10%	4.00%	3.80%	3.70%	3.60%	3.60%	3.50%	-	-	-	-
10yr PWLB Rate														
Link Group	4.21%	4.50%	4.50%	4.40%	4.30%	4.20%	4.00%	3.90%	3.70%	3.60%	3.50%	3.40%	3.30%	3.20%
Capital Economics	4.21%	4.30%	4.20%	4.10%	4.00%	3.80%	3.80%	3.70%	3.60%	3.60%	-	-	-	-
25yr PWLB Rate														
Link Group	4.36%	4.70%	4.70%	4.60%	4.50%	4.40%	4.30%	4.10%	4.00%	3.90%	3.70%	3.60%	3.50%	3.50%
Capital Economics	4.36%	4.30%	4.30%	4.20%	4.20%	4.10%	4.00%	4.00%	3.90%	3.90%	-	-	-	-
50yr PWLB Rate														
Link Group	3.82%	4.30%	4.40%	4.30%	4.20%	4.10%	4.00%	3.80%	3.70%	3.60%	3.40%	3.30%	3.20%	3.20%
Capital Economics	3.82%	4.20%	4.20%	4.10%	4.10%	4.10%	4.00%	3.90%	3.90%	3.80%	-	-	-	-

8.2 The Monetary Policy Committee (MPC) voted (7:2) to increase the Bank Rate by 0.75% to 3% during the November 2022 meeeting. In making this decision, the MPC assumed that some fiscal support will continue beyond the current six-month period of the Energy Price Guarantee (EPG), mechanically limiting CPI inflation and reducing its volatility. Against this backdrop, the MPC expect Gross Domestic Product (GDP) to decline by around 0.75% during the second half of 2022, in part reflecting the squeeze on real incomes from higher global energy and tradable goods prices. The MPC also projects that Consumer Price Index (CPI) inflation will increase to around 11% in the fourth quarter of 2022, lower than was expected in August, reflecting the impact of the EPG. The British economy expanded 2.4% year-on-year in the third quarter of 2022, the lowest reading since the contraction in quarter one of 2021, but slightly above market expectations of 2.1%, which preliminary estimates showed. On a quarterly basis in quaretr 3 of 2022 the economy shrank 0.2%, lower than market forecasts of a 0.5% drop, which preliminary estimates showed. The services sector stalled, while the production sector went down 1.5%, including a 2.3% fall in manufacturing and a 1% loss in mining and quarrying. On a monthly basis, the economy contracted by 0.6% in September, following a downwardly revised 0.1% decline in August, and worse than market forecasts of a 0.4% fall.

8.3 The S&P Global/CIPS UK Composite Purchasing Managers' Index (PMI) fell to 48.2 in October from 49.1 in September, but above the flash estimate of 47.2. The annual inflation rate in the UK rose to 10.1% year on year in September from 9.9% in August, above market expectations of 10%. The largest contribution to the increase was from food (which increased by 14.8% compared to 13.4% in August). On the other hand, price growth for motor fuels further slowed inflation for transportation (10.6% vs 12%). Compared to the previous month, core consumer prices went up by 0.6% in September, down from a 0.8% rise in August but slightly above market expectations of 0.5%.

8.4 The number of people in work in the UK fell by 109,000 in the three months to August, the biggest decline since January last year and compared to market expectations of a 155,000 fall. However, the unemployment rate fell to 3.5% in the three months to September, a new low since 1974 and below 3.6% in the previous period and market forecasts of 3.6%. The number of people claiming unemployment benefits increased by 25,500 in September, a second consecutive monthly rise.

8.5 Average weekly earnings including bonuses increased by 6.0% year on year in the three months to August, above a 5.5% gain in the three months to July and market forecasts of 5.9%. Regular pay (which excludes bonus payments) rose 5.4%, after a 5.2% rise in the previous period, exceeding expectations of 5.3%.

8.6 The US unemployment rate rose to 3.7% in August, the highest since February and above market expectations of 3.5%. The number of unemployed people increased by 344,000 to 6.01 million, while employment levels went up by 442,000 to 158.73 million. The US economy contracted by an annualised 0.6% in quarter two of 2022, confirming the economy technically entered a recession, following a 1.6% drop in quarter one. The Federal Reserve raised the Federal Funds Rate by 75 basis points to the

3%-3.25% range at its September meeting, the third straight three-quarter point increase and pushing borrowing costs to the highest since 2008. Policymakers also anticipate that ongoing increases in the target range will be appropriate, which was reinforced by Chair Powell at the post-meeting press conference. The Fed's "dot plot", which outlines individual member forecasts, showed interest rates will likely reach 4.4% by December, above 3.4% projected in June, and rise to 4.6% next year.

8.7 The Euro Area economy expanded 0.8% in quarter two of 2022, higher than a 0.6% rise indicated and the strongest growth rate in three quarters. Household spending was the main driver of the expansion, prompted by the easing of Coronavirus restrictions and the summer tourism season. The annual inflation rate in the Euro Area jumped to 10% in September of 2022 from 9.1% in August. It marks the fifth consecutive month of rising inflation, with prices showing no signs of peaking. In a similar vein, core inflation, which excludes prices of energy, food, alcohol and tobacco, increased to a record high of 4.8% in September from 4.3% in August.

9. BORROWING STRATEGY 2023/24 – 2025/26

9.1 The uncertainty over future interest rates increases the risks associated with treasury activity. Investment returns are likely to increase during 2023/24 with a small decrease during the latter half the financial year as interest rates are expected to reduce slightly. As a result, the Commissioner will continue a cautious approach to treasury strategy.

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

9.3 The Commissioner is currently maintaining a neutral-borrowing position. This means that the capital borrowing need (the CFR), has been fully matched with loan debt. During 2023/24 it is predicted there will be debt as the CFR exceeds the internal resources utilised to fund the Capital Programme.

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

10. INVESTMENT STRATEGY 2023/24 – 2025/26

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

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

10.3 These benchmarks are simple guides (not limits) and so may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that officers will monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the Mid-Year or Annual Report.

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

(i) 0.011% historic risk of default when compared to the whole portfolio**.**

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

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

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

(i) Investments – Internal returns compared to the average Sterling Overnight Index Average (SONIA) rate. The transition to SONIA is due to the phasing out of LIBOR, which took place on the 31st December 2021.

10.7 The security benchmark for each individual year is:

	1 year	**2 years**	**3 years**	**4 years**	**5 years**
Maximum	0.011%	0.011%	Not applicable	Not Applicable	Not Applicable

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

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

(i) A policy covering types of investment, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the Specified Investment (investments not exceeding 1 year 364 days) sections below; and

(ii) Sufficient liquidity in investments. For this purpose procedures will be set out for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the prudential indicators covering the maximum principal sums invested.

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

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

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

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

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

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

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

(iii) Building Societies which:
- Meet the ratings for banks outlined above; or
- Have assets in excess of £1bn;

(iv) Money Market Funds – AAA;

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

(vi) Local Authorities;

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

(viii) Supranational institutions.

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

(i) No more than £3m will be placed with any single non-UK country at any time;

(ii) Limits in place above will apply to Group companies; and

(iii) Sector limits will be monitored regularly for appropriateness.

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

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

	Fitch (or equivalent)	**Money Limit**	**Time Limit**
UK Banks (Groups)	*P1/F1/A1*	£10m	<365days
Non UK Banks (Groups)	*P1/F1/A1*	£5m	<365days
Building Societies	*P1/F1/A1*	£5m	<365days
Money Market Funds	AAA	£5m	<365days
Local Authorities	-	£15m	<2 years

UK DMO	-	None	<365days
Property Fund		£5m	<5 years
Guaranteed Organisations	-	£3m*	<365days

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

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

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

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

10.19 **Banking Arrangements**

The Commissioner's banker is Lloyds Bank, the contract is due to expire on 31st March 2023. The contract allows three extensions, the first one is due on the 1st April 2023 and is in the process of being formally extended for another year.

11. SENSITIVITY TO INTEREST RATE MOVEMENTS

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

Sensitivity to Interest Rate Movements		
	2023/24 Estimated +1% £000's	**2023/24 Estimated -1% £000's**
Interest on Borrowing	109	(109)
Investment Income	114	(114)

12. TREASURY MANAGEMENT - LIMITS ON ACTIVITY

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

	2023/24	**2024/25**	**2025/26**
Interest rate Exposures			
	Upper	**Upper**	**Upper**
Limits on fixed interest rates based on net debt	100%	100%	100%
Limits on variable interest rates based on net debt	35%	35%	35%
Maturity Structure of fixed interest rate borrowing 2023/24			
		Lower	**Upper**
Under 12 months		0%	20%
12 months to 2 years		0%	20%
2 years to 5 years		0%	20%
5 years to 10 years		0%	20%
10 years and above		20%	90%
Maximum principal sums invested > 364 days			
Principal sums invested > 364 days	£m 20	£m 20	£m 20

13. PERFORMANCE INDICATORS

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

(i) Debt – Borrowing - Average rate of borrowing for the year compared to PWLB rates; and
(ii) Investments – Internal returns compared with the average SONIA rate.

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

14. TREASURY MANAGEMENT ADVISERS

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

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

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

15. TREASURY MANAGEMENT TRAINING

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