

WEST OF ENGLAND COMBINED AUTHORITY COMMITTEE

31 January 2020

REPORT SUMMARY SHEET

CAPITAL STRATEGY INCLUDING TREASURY MANAGEMENT & INVESTMENT STRATEGIES

Purpose

This report presents the Capital Strategy for the West of England Combined Authority including;

- The detailed capital budget for 2020/21, and indicative budget up to 2022/23
- The Treasury Management Strategy for 2020/21
- WECA Investment Strategy 2019 to 2023

Summary

This report includes the following key information:

- The areas covered by the capital strategy are as follows;
 - Medium term capital expenditure and financing;
 - Investment strategy for non-treasury investments
 - Treasury management including prudential indicators
 - Liabilities, revenue implications of the capital programme, and knowledge and skills employed in delivering the strategy.
- The funding for the WECA Capital Programme comes from 2 main sources:
 - Investment funding provided by Government as part of the Devolution Deal (£15m revenue and £15m capital funding pa for 30 years, totalling £900m);
 - The Transforming Cities Fund (£103m over 5 years)
- The proposed WECA capital programme, assumes the approval at today's Committee of proposed spend as detailed in the Investment Fund report. In 2020/21, the WECA is planning capital expenditure of £38.439m
- The Mayor is responsible for the payment of £17.572m annual transport related capital grant funding that was previously distributed by the Department for Transport incorporating Highways maintenance grants, highways incentive grants and integrated transport grants. This funding will continue to be allocated to the three West of England councils as per the previous three financial years.
- The Highways and Transport grants are currently funded through Business Rate Retention within the current WECA 100% pilot scheme. With the new national business rate retention system due for implementation in 2021/22, it is assumed that the £17.572m will revert back to capital grant funding.

- WECA has developed an Investment Strategy which deals with the prioritisation, and allocation, of capital projects up to March 2023. The Strategy primarily covers the WECA Investment Fund and Transforming Cities Funding amounting to £350m over the period.
- The Authority's Treasury Management Strategy, sets out the proposals and guidance that the Authority will use to manage its daily cash-flow activities during the 2020/21 financial year.

Recommendations

Members of the Combined Authority Committee are asked to:

1. Approve the Capital Budget;
2. Approve the Treasury Management Strategy for 2020/21
3. Note the WECA Investment Strategy

Contact officer: Malcolm Coe

Position: Director of Investment and Corporate Services

Email: Malcolm.Coe@westofengland-ca.gov.uk

REPORT TO: WECA COMMITTEE

DATE: 31 JANUARY 2020

**REPORT TITLE: CAPITAL STRATEGY INCLUDING TREASURY
MANAGEMENT & INVESTMENT STRATEGIES**

**DIRECTOR: MALCOLM COE, DIRECTOR OF INVESTMENT AND
CORPORATE SERVICES**

AUTHOR: MALCOLM COE

Purpose of Report

1. This report presents the Capital Strategy for the West of England Combined Authority including;
 - The detailed capital budget for 2020/21, and indicative budget up to 2022/23
 - The Treasury Management Strategy for 2020/21
 - WECA Investment Strategy 2019 to 2023

Recommendation:

The WECA Committee is requested to approve:

- a) the Capital Budget as shown in Appendix 1;
- b) the Treasury Management Strategy for 2020/21 detailed in Appendix 3

and Committee is to note:

- c) the WECA Investment Strategy as shown in Appendix 2

Background / Issues for Consideration

2.1.1 The capital strategy is a report which is instigated through the 2017 edition of the Prudential Code. As explained in paragraph 21 of the code, “the capital strategy is intended to give a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services along with an overview of how associated risk is managed and the implications for future financial sustainability.”

2.1.2 The areas covered by the capital strategy are as follows;

- Medium term capital expenditure and financing (Appendix 1);
- Investment strategy for non-treasury investments (Appendix 2);
- Treasury management including prudential indicators (Appendix 3);
- Liabilities, revenue implications of the capital programme, and knowledge and skills employed in delivering the strategy.

2.1.3 There is a clear link between this strategy and the financial impact upon various elements of the Authority's revenue budget, for example, the investment and treasury strategies are key components upon how much interest the Authority could achieve on its investments compared to budgeted levels.

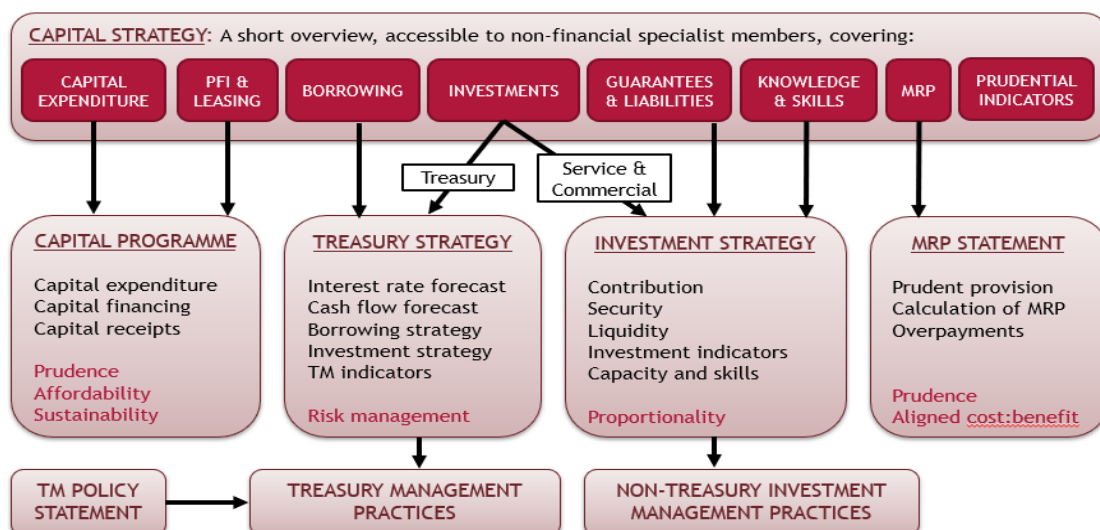
2.1.4 MHCLG published updated *Guidance on Local Government Investments* in February 2018. The previous edition covered treasury investments only, but the current edition focuses on non-treasury investments including:

- loans made for service purposes
- shares in companies bought for service purposes
- loans to and shares in subsidiaries, irrespective of the purpose of the company
- non-financial assets, (e.g. property), held primarily or partially to generate a profit

2.1.5 It is recommended that these components are included under an overarching capital strategy covering all interlinked capital programme, financing, treasury and investment policies and decisions, both in the short and medium term;

Figure 1: Prudential Code (2017) recommended reporting structure

Strategy Reports: England



2.2 Capital Expenditure and Financing

- 2.2.1 Capital expenditure is where the Combined Authority spends money on assets, such as property or vehicles, that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. WECA has some limited discretion on what counts as capital expenditure, for example assets costing below £5,000 are not capitalised and are charged to revenue in year.
- 2.2.2 Costs incurred on developing outline business cases and feasibility work, as a rule, are not able to be capitalised. However, costs incurred on generating full business cases can be capitalised including specific staff costs, such as project managers or engineers, who are engaged in the development. Support service costs incurred on business case development are required to be treated as revenue.
- 2.2.3 The funding for the WECA Capital Programme comes from 2 main sources:
- Investment funding provided by Government as part of the Devolution Deal (£15m revenue and £15m capital funding pa for 30 years, totalling £900m);
 - The Transforming Cities Fund (£103m over 5 years)

2.3 WECA Capital Investment Programme 2019/20 to 2022/23

- 2.3.1 The proposed WECA Capital programme as set out at **Appendix 1** shows both approved and indicative schemes:
- **Approved** – these schemes are fully agreed to be progressed and will be taken forwards in line with financial regulation, standing orders and the relevant assurance framework.
 - **Indicative** (shown in italics in Appendix 1) – contribution to the MetroWest Phase 1 project subject to future approval of the full business case. This scheme will need to be brought back to the WECA Committee for further approval.
 - **Proposed** – Two additional capital schemes are considered within the Investment Fund report elsewhere on this agenda. The schemes are the Whitfield Tabernacle Stabilisation project at £682,000 and the Lockleaze Sustainable Transport Improvements at £3.346m. These are not currently included in the capital budget but will be added when all the relevant conditions have been complied with.
- 2.3.2 The proposed WECA capital programme, as detailed in *Figure 2*, assumes the approval at today's Committee of proposed spend as detailed in the Investment Fund report elsewhere on the agenda. In 2020/21, the WECA is planning capital expenditure of **£38.439m** as summarised below:

Figure 2: Prudential Indicator: Estimates of Capital Expenditure in £000s

	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget
WECA Capital	31,377	20,867	1,360	1,000
Mayoral Capital *	18,234	17,572	17,572	17,572
TOTAL	49,611	38,439	18,932	18,572

** Assuming transport capital grants are maintained by government beyond the current West of England Business Rates Retention pilot.*

- 2.3.3 Several WECA capital projects are at an early stage of feasibility and design. Various assumptions have therefore been made which will materially change as further development is undertaken. Upon completion of full business cases there will be significant further capital approvals which can be expected throughout the 2020/21 financial year.
- 2.3.4 Priority Infrastructure Schemes – schemes such as MetroWest, (current approval of £5.86m), and Bristol Temple Meads Eastern Entrance, (£2.5m), are examples where a much larger capital draw-down is expected over the coming months as the schemes progress towards delivery.
- 2.3.5 The Mayor is responsible for the payment of £17.572m annual transport related capital grant funding that was previously distributed by the Department for Transport incorporating highways maintenance grants, highways incentive grants and integrated transport grants. This funding will continue to be allocated to the three West of England councils as per the previous three financial years.
- 2.3.6 The Highways and Transport grants are currently funded through Business Rate Retention within the current WECA 100% pilot scheme. With the new national business rate retention system due for implementation in 2021/22, it is assumed that the £17.572m will revert back to capital grant funding.
- 2.3.7 All new projects requiring approval, (whether delivered externally via grant or delivered internally by WECA), will go through an integrated 'One Front Door' approach as per the approved Assurance Framework.
- 2.3.8 **Capital Funding** – All capital costs will be met from Government grants, devolution investment funding or revenue contributions to capital outlay (RCCO). The capital funding period to 2022/23 includes the Government's first 5-year gateway review and further investment funding beyond 2020/21 will be subject to meeting the requirements of the gateway review.
- 2.3.9 **Investment Fund Revenue** – This report includes capital projects only. Revenue running costs and one-off projects which are revenue in nature, will be funded from the revenue element of the Investment Fund, which are detailed in the WECA Revenue Budget report on this agenda.
- 2.3.10 There is no intention at this stage for WECA to finance any of its capital spend from long term borrowing. The only borrowing currently being considered is short term borrowing to cover cash flow issues, as detailed within the Treasury Management Strategy (Appendix 3 of this report).

2.4 Accountable Body Functions

2.4.1 WECA act as Accountable Body for the Local Enterprise Partnership, (LEP), activities, which includes significant capital investment in the region. This capital investment is the responsibility of the Joint Committee but is being presented within this report to provide context and magnitude for the regional capital investment programme, being delivered or influenced by WECA.

2.4.2 The capital funding streams administered by the Accountable Body include:

- Local Growth Funding (LGF) provided by the Government as West of England Growth Deal capital funding (£202m funding to be spent by March 2021);
- The Revolving Infrastructure Fund (£57m);
- The Economic Development Fund (£500m)

2.4.3 The LGF and RIF Capital Programme is detailed in *Figure 3*:

Figure 3: LGF and RIF Medium Term Capital Programme

Forecast Spend	2019/20 £000	2020/21 £000	2021/22 £000	2022/23 £000
LGF				
Transport	20,222	15,726	0	0
FE Skills	7,355	8,601	0	0
Infrastructure	9,960	11,954	0	0
Innovation	17,998	7,544	0	0
RIF				
GP & RGF2	4,800	1,000	1,000	1,000
Total	60,335	44,825	1,000	1,000

2.4.4 All of the projects within the LGF and RIF programmes are delivered by the constituent authorities or other bodies – but not directly delivered by WECA. WECA acts as agent in administering the grants.

2.4.5 WECA is the Accountable Body for the £500m Economic Development Fund, although the associated finances are administered by South Gloucestershire Council. The four constituent authorities will deliver approved projects and can claim the costs of borrowing from the fund once practical completion of the project is achieved. Similar to LGF, the WECA does not include the capital spend within its capital programme.

The table below shows the estimated practical EDF completions within the time frame of this report:

Figure 4: EDF estimated spend within MTFP period

Forecast Completions	2019/20 £000	2020/21 £000	2021/22 £000	2022/23 £000
EDF	12,311	46,072	117,739	33,701

2.5 WECA Investment Strategy

2.5.1 WECA has developed an Investment Strategy which details the prioritisation, and allocation, of capital projects up to March 2023. The Strategy primarily covers the WECA Investment Fund and Transforming Cities Funding amounting to £350m over the period. The Strategy is shown as **Appendix 2** to this report.

2.6 Treasury Management

- 2.6.1 Treasury management is concerned with keeping sufficient, but not excessive, cash available to meet the Authority's spending needs, whilst managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Authority is typically cash rich in the short-term as grant income is often received before it is spent, but these cash surpluses reduce as capital expenditure is incurred.
- 2.6.2 The Authority's Treasury Management Strategy, as detailed in **Appendix 3**, sets out the proposals and guidance that the Authority will use to manage its daily cash-flow activities during the 2020/21 financial year. The Authority must give due regard to the management of these sums, to ensure that it is sufficiently able to balance the daily cash requirements for all operational services whilst still achieving the strategic outcomes required within the medium-term financial plan.
- 2.6.3 The Council's policy on treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss.
- 2.6.4 Money that will be held for longer terms can be invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.
- 2.6.5 In the early years of the Combined Authority's operations, holding high cash balances are common practice as early spend on feasibility studies and development work is relatively low compared to the annual allocation of Investment Funding. However, balances will diminish over time as significant construction costs are incurred.
- 2.6.6 Decisions on treasury management investment and borrowing are made daily and are delegated to the Director of Investment and Corporate Services and designated staff, who must act in line with the Treasury Management Strategy. Reports on treasury management activity are presented to the WECA committee on a regular basis with the Audit Committee being responsible for scrutinising treasury management decisions.

2.7 Knowledge and skills employed in delivering the strategy

- 2.7.1 The Authority employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. Throughout 2019/20 WECA has sought to reduce reliance on external contractor finance support, building up capacity and expertise within the in-house finance team.
- 2.7.2 Use is made of external advisers and consultants that are specialists in their field only to plug the identified gaps that can't be covered through in-house capacity. The main examples are the engagement of Arlingclose Limited as Treasury Management advisers and PSTax as VAT advisors. This approach is more cost effective than employing such staff directly, and also ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

Consultation

- 3 Consultation has been carried out with Chief Executives, Section 151 Officers and WECA's Monitoring Officer. Consultation has taken place throughout the 2019/20 financial year in determining the WECA £350m prioritised Investment Programme that was approved by the WECA Committee in July 2019.

Other Options Considered

- 4 None.

Risk Management/Assessment

- 5 This report forms a core part of the WECA's governance and risk management process. Members will be aware that there is a direct link between the levels of risk and the levels of return achieved on investment, although there are many other factors which also affect the capital financing budgets. The priority of the Treasury Management Strategy will be the minimisation of risk to safeguard public resources.

Public Sector Equality Duties

- 6 The public sector equality duty created under the Equality Act 2010 means that public authorities must have due regard to the need to:

- Eliminate unlawful discrimination, harassment and victimization and other conduct prohibited by the Act.
- Advance equality of opportunity between people who share a protected characteristic and those who do not.
- Foster good relations between people who share a protected characteristic and those who do not.

- 6.1 The Act explains that having due regard for advancing equality involves:

- Removing or minimising disadvantages suffered by people due to their protected characteristics.
- Taking steps to meet the needs of people from protected groups where these are different from the needs of other people.
- Encouraging people from protected groups to participate in public life or in other activities where their participation is disproportionately low.

- 6.2 The general equality duty therefore requires organisations to consider how they could positively contribute to the advancement of equality and good relations. It requires equality considerations to be reflected in the design of policies and the delivery of services, including policies, and for these issues to be kept under review.

Finance Implications, including economic impact assessment where appropriate:

- 7 Financial implications are contained throughout the report and impact on both the capital programme, annual revenue budget, as well as the balance sheet.

Advice given by: Malcolm Coe, Director of Investment & Corporate Services

Legal Implications:

- 8 The Budget proposals have been developed in accordance with appropriate Local Government Regulations, including the specific funding and related governance requirements set out in the The West of England Combined Authority Order 2017 and The Combined Authorities (Finance) Order 2017.

Climate Change Implications

- 9 On 19 July 2019, the West of England Combined Authority declared a climate emergency, recognising the huge significance of climate change and its impact on the health, safety and wellbeing of the region's residents. The Combined Authority is committed to taking climate change considerations fully into account as an integral part of its governance and decision-making process.

Each report/proposal submitted for Combined Authority / Joint Committee approval is assessed in terms of the following:

Will the proposal impact positively or negatively on:

- * The emission of climate changing gases?
- * The region's resilience to the effects of climate change?
- * Consumption of non-renewable resources?
- * Pollution to land, water or air?

Particular projects will also be subject to more detailed environmental assessment/consideration as necessary as part of their detailed project-specific management arrangements

- 9.1 Much of the WECA approved investment on building the infrastructure within the region will have a positive impact on climate change. Specifically, stepped change and improvements to rail and bus services along with an investment in cycling and walking facilities will help to reduce our carbon footprint.
- 9.2 Consideration of climate issues are incorporated within the assessed criteria that is used by WECA to determine priority financial allocations from investment funding and Transforming Cities funding.

Land/property Implications

- 10 Where WECA investment allocations concern any acquisition or disposal of land and/or property, full consideration is given to relevant state issues, market valuation and the requirement to deliver best value.

Advice given by: Malcolm Coe, Director of Investment & Corporate Services

Human Resources Implications:

- 11 The funding for the staff establishment for WECA functions is provided for within the proposed Budget in line with the resourcing requirements. There are no direct human resource implications arising from the report itself.

Advice given by: Alex Holly, Head of Human Resources

Appendices:

Appendix 1: Capital Budget 2020/21

Appendix 2: Investment Strategy 2019 to 2023

Appendix 3: Treasury Management Strategy 2020/21

Background papers:

WECA Committees 14 June 2019, 19 July 2019 and 4 October 2019 – Investment Fund Update Reports

WECA Committee 1 February 2019 - Capital Strategy including Treasury Management and Investment Strategies

West of England Combined Authority Contact:

Any person seeking background information relating to this item should seek the assistance of the contact officer for the meeting who is Ian Hird / Tim Milgate on 0117 332 1486; or by writing to West of England Combined Authority, 3 Rivergate, Temple Way, Bristol BS1 6EW; email:

democratic.services@westofengland-ca.gov.uk

WECA & Mayoral Capital Budget					
	2019/20 Revised Budget £000	2020/21 Original Budget £000	2021/22 Phased Budget £000	2022/23 Phased Budget £000	Total (incl 19/20) Budget £000
WECA Capital					
Infrastructure					
Business Case Development (see breakdown below)	5,183	2,704	0	0	7,887
Real Time Information	94				94
Metrowest		5,860			5,860
Cribbs Patchway Metrobus Extension	14,147	8,053			22,200
CPPN Cycle Links	125	3,000			3,125
Bristol Temple Meads Station Eastern Entrance	1,250	1,250			2,500
On Bus Contactless Payment	418				418
Housing Land Acquisition Fund	9,000				9,000
Great Stoke Roundabout Improvements			1,360	1,000	2,360
	30,217	20,867	1,360	1,000	53,444
Business & Skills					
5G Smart Tourism	875				875
	875	0	0	0	875
Corporate Services					
Scheme Prioritisation/Monitoring & Evaluation	285				285
	285	0	0	0	285
Mayoral Capital					
Highways & Transport Grants	17,572	17,572	17,572	17,572	70,288
Pothole Action Grant	662				662
	18,234	17,572	17,572	17,572	70,950
Grand Total	49,611	38,439	18,932	18,572	125,554
Business Case Development					
A37 to A362 Improvements – Somer Valley Enterprise Zone	176				176
Cribbs Patchway Cycle Links	40				40
Unlocking Lockleaze Development	68				68
Great Stoke Roundabout Capacity Improvements	298				298
Hicks Gate Roundabout	402				402
Wraxall Roundabout Signal Scheme FBC	1,488				1,488
Somer Valley Enterprise Zone	326	420			746
Bath River Line	75	75			150
Metro West Phase 2	1,760	1,759			3,519
Charfield Station	450	450			900
Local Cycling & Walking	100				100
	5,183	2,704	0	0	7,887

West of England Combined Authority Investment Strategy



APPENDIX 2

2019 - 2023

November 2019



Investment Strategy (four year)

2019 to 2023

1. Organisational Context

This is the first published Investment Strategy for the West of England Combined Authority (WECA).

Since its inception in 2017, WECA has evolved and grown rapidly in response to delivering its statutory responsibilities as part of the approved devolution deal with government. This includes prioritisation, programming and governance of additional government funding into the region, in excess of £1bn.

The strength of the region has previously been recognised by government as being the biggest net contributor to the national purse outside of London. £500m of Economic Development Funding and £200m of Local Growth Funding has been successfully programmed out across the partnership of Bristol City, South Gloucestershire, Bath and North East Somerset and North Somerset Councils.

“The West of England is one of the UK’s most prosperous regions with an economy worth over £33.2 billion a year. A net contributor to the national purse, with a population of over 1 million and over 43,000 businesses”

WECA, through an established formal committee, is now responsible for delivering clean and sustainable growth through £900m of Investment Funding, (£30m per annum for 30 years), and £103m of Transforming Cities Funding.

This Investment Strategy covers the parameters, priorities, uses and constraints of this, £1bn, of WECA funding for the initial period up to March 2023.

2. Strategic Context

The WECA Committee has adopted a framework which details the outcomes that we are aiming to deliver in the region through a structured, prioritised, medium to long term investment programme.

Figure 1: West of England Combined Authority Operating Framework:



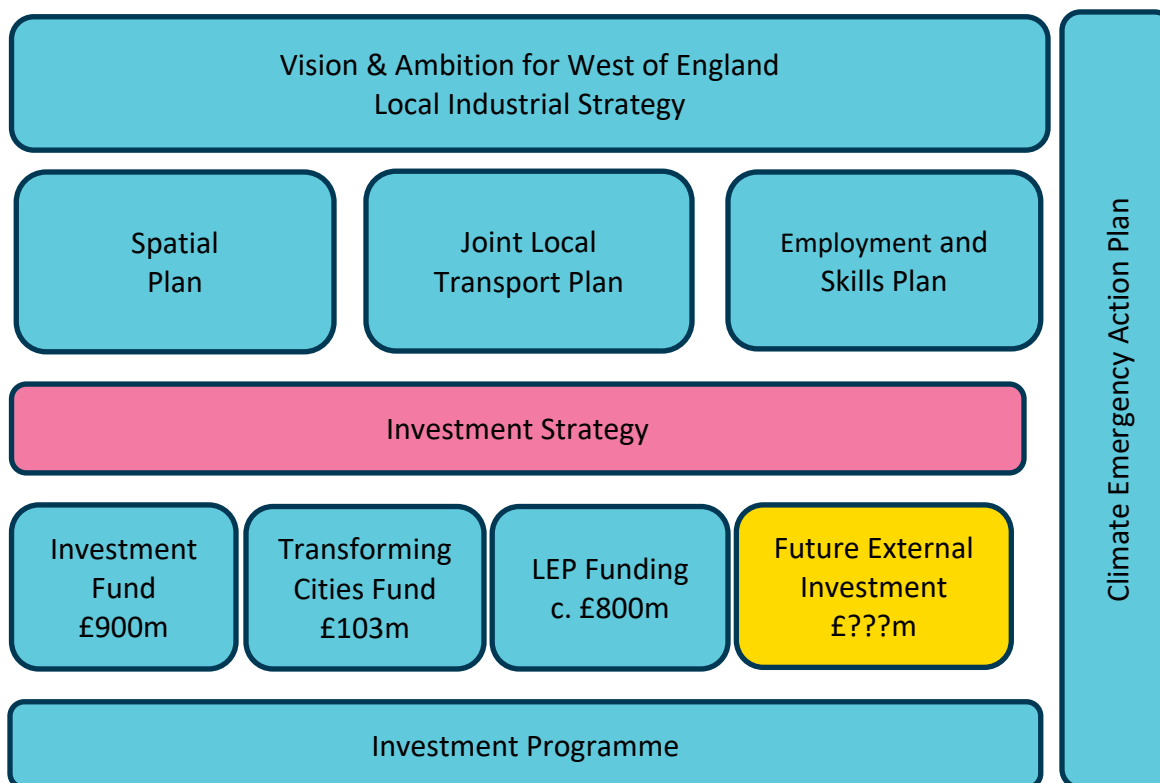
Source: Operating Framework (May 2018) – Revised WECA Business Plan 2020/21

This framework overarches and sets out the long-term direction and aspiration for the region which is well articulated in the core strategic documents including:

- Joint Local Transport Plan, (JLTP);
- Local Industrial Strategy, (LIS);
- Employment and Skills Plan;
- Energy Strategy and Climate Change Action Plan

With strategic direction and Operating Model established and medium to long term resources identified, the next stage for WECA development is to articulate a longer-term Investment Strategy as demonstrated in *Figure 2*.

Figure 2: Linkage Between WECA Strategic Direction and Funding Decisions



The West of England Local Industrial Strategy sets out our vision and ambition for the future of our region. We have a suite of plans setting out the actions we will take to deliver this vision across infrastructure, skills provision and business support. These plans also set out our approach to addressing a number of wider priorities and will drive our investment decisions. All of these strategies and plans should be seen in the context of the climate change emergency action plan which will touch on all the actions the Combined Authority takes.

3. WECA Funding Context and Allocations

Investment Fund - £900m

The WECA Order has determined this fund as being 50% Revenue and 50% capital at £30m per year over 30 years (£900M). This allows the Combined Authority to have a reasonable amount of flexibility in using revenue to develop relevant feasibility studies required to effectively prioritise capital investment.

Government will allocate investment funding based on WECA successfully completing 5 yearly 'Gateway' Reviews which requires tangible evidence of progress against the strategic direction set and delivery and outcomes achieved on the ground. The first of these Gateways will be undertaken during 2019/2020 with the Government forming a final view and subsequently reporting back in late 2020.

The ability to set long term strategic direction compared with delivering short to medium term capital projects is a tension faced by all Combined Authorities. The £30m per annum Investment Fund is year on year cash limited and not uplifted in any way to reflect increases in costs / prices through the Retail Price Index, Construction Inflation or any other pertinent index. The net present value of the £30m fund, in ten year blocks, is demonstrated in *Figure 3*

Figure 3: Net Present Value of the Investment Fund over 30-year period:

Year	Grant	Equivalent Purchasing Power
0	£30m	£30m
10	£30m	£22.3m
20	£30m	£16.6m
30	£30m	£12.7m

Transforming Cities Fund - £103m

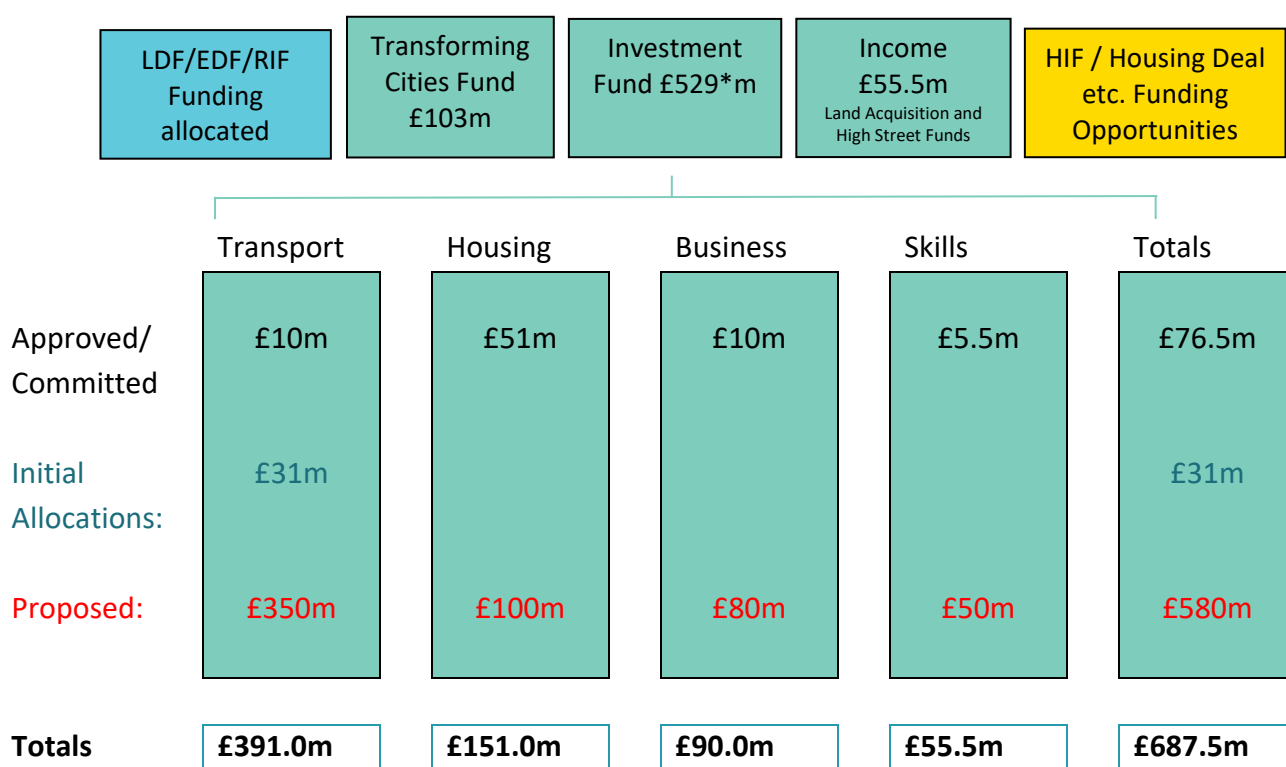
In terms of the Transforming Cities Fund, the allocation is time limited, having to be fully spent by March 2023, on major projects that will improve productivity and spread prosperity in public and sustainable transport in English city regions.

Investment Programme

To balance strategic direction with tangible delivery, WECA has gone through a series of stages to 'chunk' up the overall funding available into manageable blocks and time periods.

In February 2019, the WECA Committee approved a notional 20-year financial allocation, (Investment Fund and Transforming Cities Fund), to ensure that adequate resources are deployed to each strategic priority area of the approved Operating Model. This 20-year allocation, as detailed in *Figure 4*, is coterminous with the time period covered through emerging spatial planning and the Joint Local Transport Plan for the region.

Figure 4: Indicative 20 Year Funding allocation (February 2019 WECA Committee)



*Net of running costs

Alongside the constituent Unitary Councils, WECA has been prioritising a short to medium term capital investment programme of £350m for the period up to March 2023, as approved by the WECA Committee on 19 July 2019. This programme demonstrates a reasonable geographical and functional split across priority areas and will be a vital 'building block' in support of the first government gateway review of investment progress.

A summary of the approved awards and feasibility funding as at October 2019 is detailed in Figure 5

Figure 5: £350m approved WECA Investment Programme (up to March 2023)

	Funding Awards and Allocations £000s
Transport Infrastructure	
Approved Awards and Allocations	57,221
Associated 'tail' required to deliver all projects up to March 2023	87,623
Total Investment in Transport Infrastructure	144,844
Housing Infrastructure	
Approved Awards and Allocations	56,720
Associated 'tail' required to deliver all projects up to March 2023	28,100
Total Investment in Housing Infrastructure	84,820
Business and Skills	
Approved Awards and Allocations	74,078
Associated 'tail' required to deliver all projects up to March 2023	18,440
Total Investment in Business and Skills Infrastructure	92,518
Opportunities and Challenges / Other	
Funding put aside to respond to opportunities and challenges	20,000
Approved WECA set up, operating costs and elections up to 2023	7,818
Total Investment Programme up to March 2023	350,000

The Investment Programme will deliver significant regional outcomes including improving local rail availability, enhancing bus services, reducing congestion pressure points, developing viable walking and cycling options, unlocking and accelerating housing delivery and supporting and developing businesses in compliance with the, recently published, West of England Local Industrial Strategy.

However, the vast majority of this initial Investment Programme is in the form of grant related spend with very little requirement for repayment to the fund over time. Moving forward beyond 2023, it will be essential to further develop our investment criteria – which will include incorporating the need for a balanced share of the investment portfolio being repayable into a sustainable, long term investment resource programme.

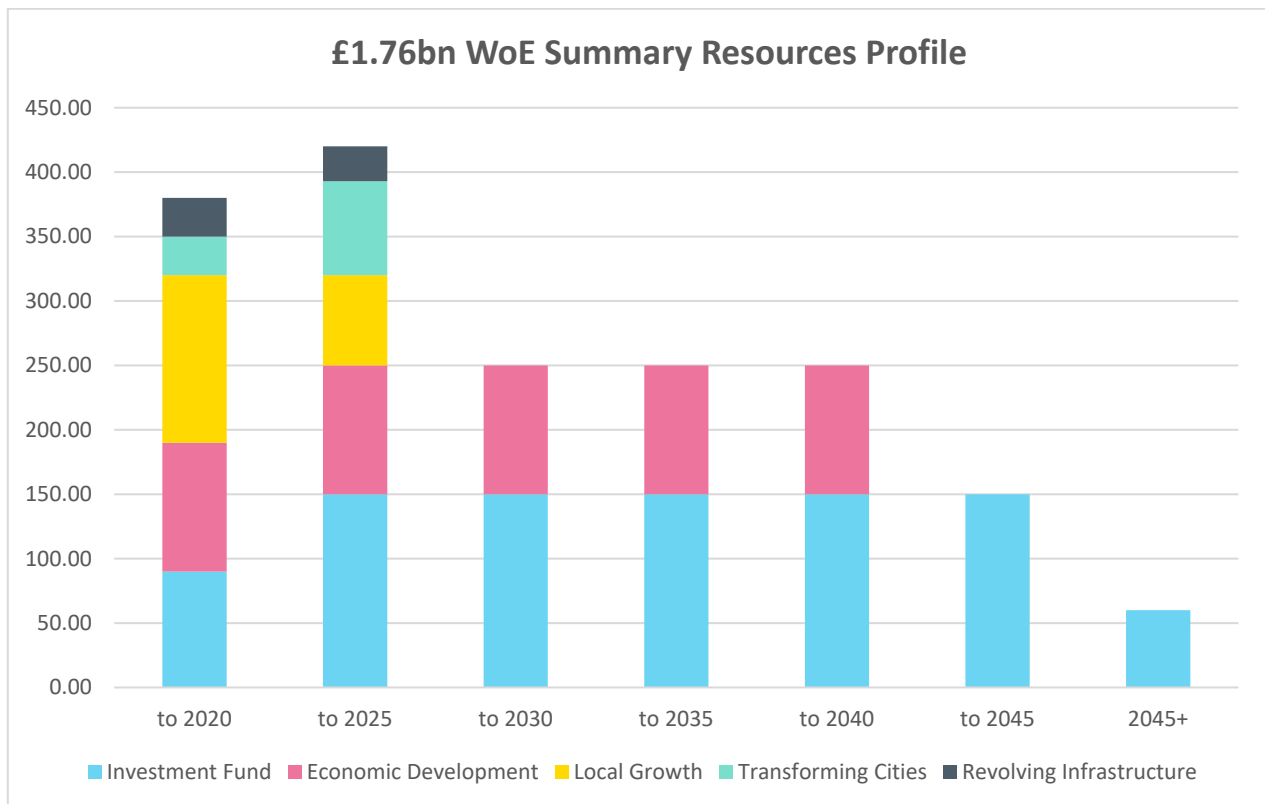
4. WECA Investment Strategy – Core Principles and Constraints

There are a number of capital investment funding streams available to the region. Where feasible and relevant we ‘mix and match’ spend from individual projects across different funds in order to maximise and retain maximum investment into the area. However, each element of funding does carry certain constraints and reporting requirements alongside specific time periods for spend to incur.

A headline summary of the core capital investment funding streams and their intended purpose and constraints are detailed in *Figure 6*

Figure 6: Capital Investment Funding Sources

Fund	Amount	Time Period	Narrative overview
Economic Development Fund	£500m	25 years 2015 to 2040	LEP funding reliant on delivering and retaining business rates growth within defined Enterprise Zones/Areas
Local Growth Fund	£200m	Up to March 2021	LEP time limited Grant Funding with set criteria to deliver local growth.
Revolving Infrastructure Fund	£57m	Revolving	Growth Deal LEP funding targeted at schemes that will repay into the fund
Shared Prosperity Fund	tbc	Post March 2021	LEP Funding successor to the Local Growth Fund (yet to be determined)
Housing Infrastructure Fund	Bid	various	Grant Funding to enable significant housing growth. Competitive bidding into a national funding pot.
Department for Transport Grants	Bid	various	Bid into Government for areas such as exceptional structural maintenance / delivery of local major capital schemes
Various Business and Skills Funding	Bid	various	Various funding pots open to competitive bidding to support local business and skills development
WECA Investment Fund	£900m	30 years to 2047	£30m p.a. to deliver sustainable long term growth. Must demonstrate ‘additionality’ and outcomes. Drawdown subject to passing 5-year gateway reviews.
WECA Transforming Cities Fund	£103m	Up to March 2023	Major public and sustainable transport projects. Schemes need to be fully delivered by March 2023.



** WECA funding incorporates Bristol, Bath and North East Somerset and South Glos Councils*

** LEP Funding sources cover the three WECA Councils and, in addition, North Somerset Council*

It is important to understand how these different funding streams inter-relate with a sustained focus on utilising the funding at our disposal to lever in additional public or private sector investment into the region. There are various examples of where we have utilised West of England funding as 'match' to attract inward investment such as:

- £50m of Investment Funding in support of a £258m bid for Housing Infrastructure funding (covering Bristol and Bath);
- £10m High Streets fund, created from the Investment Fund, to support Unitary Authorities to bid for government match funding;
- £6m from the Investment Fund, alongside EDF and LGF contributions, attracting £32m of Department of Transport Funding for MetroWest Rail;
- £4m from the Investment Fund for 'Workforce for the Future' attracting £4m of European match funding;
- £400k from the Investment Fund to support Unitary Authorities in developing bids for local majors and structural maintenance funding from government.

Investment Fund Criteria – Project inception and management

To warrant consideration for programme entry, all proposals **must** :

- Deliver ‘additionality’/outcomes over and above current service and/or infrastructure levels;
- Demonstrate how it contributes to the strategic direction for the region and how it fits within a programme of like projects delivering wider benefit; and
- Demonstrate delivery of the required Value for Money level in compliance with the approved criteria relevant to the project in question

In addition, to ensure that the Investment Fund continues to deliver against its required purpose of sustainable long term growth, whilst maintaining future value and flexibility in the fund, the core criteria as detailed in *Figure 7* will be applied to all emerging projects / investments moving forward.

Figure 7: Investment Fund Core Criteria for any proposed drawdown

	Required Criteria for Accessing the Investment Fund	Yes/No
1	Each proposal must demonstrate how the requested funding could lever in further public or private sector contributions / match funding in it’s implementation or operation	✓
2	Each capital investment must demonstrate how it could repay, (either part or full), into the Investment Fund at a future point in time	✓
3	Investments involving land transactions must consider, within the business case, associated income from either capital receipt, uplift in value and/or developer contributions on the site and the surrounding area	✓
4	Proposals must be fully compliant with the approved WECA Assurance Framework in order to drawdown funding for feasibility / outline business case / full business / construction	✓
5	Up to 10% of the total estimated capital scheme cost will be allocated for feasibility / development with the option to extend to 20% by exception upon providing relevant evidence of estimated costs and outcomes.	✓
6	The Investment Fund can’t be used to solely address viability issues on specific development sites	✗
7	Investment Fund can’t be used to solely deliver repair or maintenance to existing assets (but modest revenue can be deployed to develop funding bids)	✗
8	Investment Fund can’t be used to fund on-going revenue costs (the future source of such costs must be detailed within business case development)	✗
9	The Investment Fund can be used to ‘pump prime’ revenue costs for a defined period of time until a scheme becomes operationally viable. This is limited to no more than 3 years and must be supported by a robust business case	✓
10	Any proposed investment must consider how it contributes towards the region’s vision for becoming carbon neutral / addressing climate change	✓

All proposed projects need to evidence a detailed build-up of costs, (internal and external), to trigger initial draw down against development funding. Capital Cost estimates should be evidenced by an appropriate submission which provides estimates using industry accepted methodology.

WECA, as overall accountable body for the fund, will require formal sign-off of the strategic fit, estimated outcomes, costs and draw down of funding in compliance with the respective stages of the approved Assurance Framework. Development Funding, Outline Business Case, (OBC), and Final Business Case, (FBC) will need approval of the WECA Statutory (Section 73) Finance Officer in conjunction with the Director of Infrastructure, Head of Business and Skills and Head of Capital Projects Delivery as relevant.

For more straightforward and lower value schemes formal committee approval may not be required at OBC stage providing the costs and scope have not changed significantly since the Development Funding Application stage.

To ensure value for money, and pace in scheme progression, any new commissions for professional services required for development work must be procured through the West of England Professional Services Framework. Any exception to using this Framework needs to be agreed with the WECA Head of Capital Delivery. This will allow WECA and UA lead officers to set appropriate and consistent scopes and briefs for development work, and get best value from public sector investment through maximising the benefits of the framework.

Investment Fund Criteria – Programme-wide management






In addition to criteria that must be applied for every proposed scheme, there are a few criteria that must be applied to the WECA Investment Fund programme as a whole in order to:

- maintain a balanced portfolio of projects;
- ensure sustainability of future resource levels of the fund;
- promote consistency in the allocation and drawdown of funding;

These are detailed in *Figure 8*.

Figure 8: Investment Fund Overall Programme Criteria / Principles

	Required Criteria / Principles for Delivering the Investment Fund	Yes/No
1	Funding allocations across the strategic themes of Transport Infrastructure, Housing, Business and Skills need to be within the overall 20-year control totals as approved by WECA Committee in February 2019	✓
2	The programme must be regional in nature and supported by evidence in compliance with Government Gateway review criteria	✓
3	The overall Investment Programme, and projects within it, should give due consideration as to how climate issues are being addressed in compliance with the regional commitment to be carbon neutral by 2030	✓

4	There should not be a defined financial allocation to each individual Authority However, consideration must be given to a reasonable geographical spread.	
5	WECA will retain management and reporting responsibility across the whole Investment Programme. Projects managed by individual authorities will need to report on progress and outcomes using approved processes and templates	
6	Where approval has been given for feasibility funding /outline business case, an appropriate capital delivery 'tail' may be accounted for in the Investment Programme, but not disclosed in the public domain until costs have been verified.	
7	If any project / scheme should not progress for any reason, or actual costs be significantly less than programmed – funding must be returned to the overall regional investment programme. Individual authorities are not able to substitute in an alternative project of their choice.	
8	The aspiration is to maximise the number of approved schemes that provide some form of repayment back in to the Investment Programme in order for the fund to become more sustainable in the long term.	

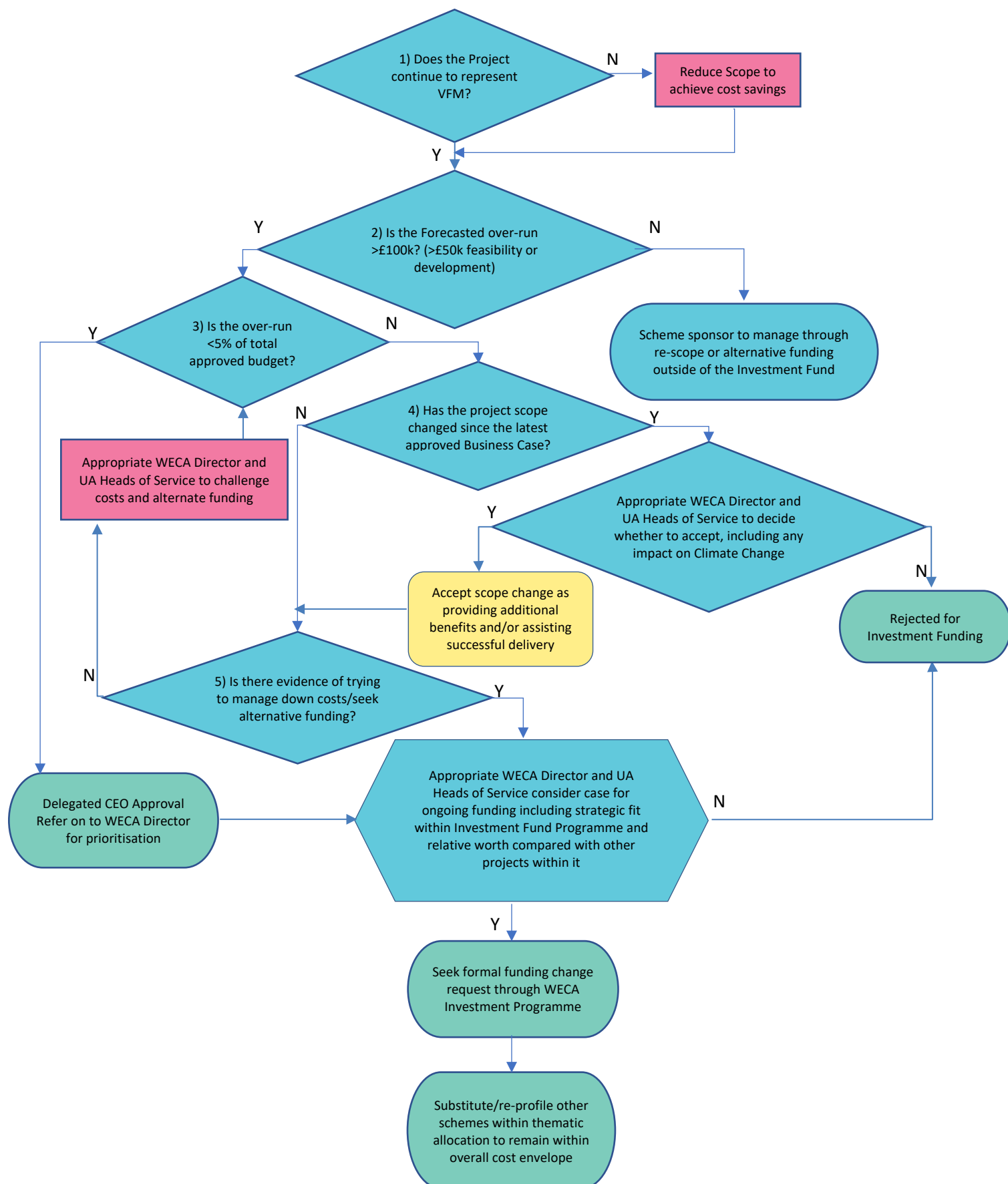
Funding allocations to projects will be subject to successful compliance with the approved assurance stage gate process. All costs must be clearly evidenced, and verified by the WECA Section 73, (Statutory Finance Officer), prior to receiving formal allocation.

On occasions, costs will fluctuate on major projects as schemes are developed and move through in to delivery. The formal Boards within the established WECA governance structure will monitor progress on scheme delivery in terms of timescale and cost variations. In the event of estimated cost over-run, the process as detailed in *Figure 9*, must be applied.

Figure 9: Process for responding to forecasted cost over-runs

This process applies to both development and implementation costs.

For changes to implementation costs, schemes must have at least reached Outline Business Case



Guidance on the Application of the Cost Change Process

1	<p>Does the Project continue to represent VFM?</p> <p>The change request should include a description of the impact on the value for money having regard to both the costs and benefits arising from the change. The VFM statement should be revised and represented. Where a cost increase results in the VFM score dropping below the required threshold, for example a BCR of 2 for a transport scheme, the project will need to be rescoped to reduce costs. Where the VFM metric shows a reduction of over 10% then this should be considered by the WECA Director and relevant UA Heads of Service.</p> <p>For Feasibility and Development applications VFM will be more qualitative.</p> <p>The confirmation of the change request should be signed off by the s151/CFO</p>
2	<p>Is the Forecasted over-run >£100k (>£50k for feasibility and development)?</p> <p>This should be the increase in funding sought net of any additional match funding identified. Amounts under £100k (or £50k) should be managed within the overall project budget by the sponsoring authority.</p>
3	<p>Is the over-run <5% of total approved budget?</p> <p>To calculate the cost change this should be compared to the current approved funding award from WECA.</p>
4	<p>Has the project scope changed since the latest approved Business Case?</p> <p>The business case or Change Request should clearly set out, in detail, the reason(s) for and impact of the change. A revised cost plan or breakdown must be provided. Any changes in scope must be described, or confirmation provided that the scope is unchanged.</p> <p>Consideration should be given as to whether the scope change has modified the project's impact on addressing climate change.</p> <p>The information will be considered by the appropriate Review Panel which, depending on the circumstances, may include independent local authority officers. A report will then be provided to the appropriate WECA Director and UA Heads of Service.</p>
5	<p>Is there evidence of trying to manage down costs/seek alternative funding?</p> <p>The business case or Change Request should set out the overall funding make-up of the scheme, other potential funding sources and why these have been discounted.</p> <p>The information will be considered by the Review Panel and this will form part of the report to the appropriate WECA Director and UA Heads of Service.</p>

Where schemes progress to a position where a formal change request/new business case is to be submitted, including the cost increase, this must be agreed by the appropriate WECA Director and UA Heads of Service having regard to the strategic fit with the Investment Fund programme and the relative worth compared with other projects contained within it.

The need for any necessary substitution/reprofiling should be from within the relevant investment programme thematic allocation. This to be proposed by the relevant WECA Director and UA Heads of Service and to be approved by the CEOs/WECA Committee as appropriate. Where schemes are joint funded through either Economic Development Fund or Local Growth Fund, it is envisaged that these funds should be revised and reprofiled as a first point of call for any cost over-run.

Commercial Investments

In compliance with approved evaluation criteria, the Investment Fund can be used for commercial investment as long as there is a clear strategic fit with the organisation's Operating Model and priorities.

An example of this is the 'Land Acquisition Fund' which enables the commercial acquiring of land and property where there is an identified need for public sector intervention for accelerating housing delivery (or implementing planning policy objectives).

Similarly, the Investment Fund could be used for acquiring business premises and other assets of value as long as there is a clear purpose for the use of such assets in delivering regional outcomes that are congruent with the WECA Order.

The Investment Fund should not be used for:

- speculative purchases for pure uplift in value;
- land-banking without clear purpose for development;
- acquiring assets purely for revenue return on investment.

5. Review arrangements

This Capital Investment Strategy runs over a period from October 2019 to March 2023. It is a fundamental strategy within the overall suite of WECA governance, assurance and budget setting documents.

Annual reviews of the strategy will be incorporated within the usual budget setting process with any required amendments or modifications presented to WECA committee for approval each February.

Any exemptions required from the Investment Fund Criteria, as detailed in Figure 7, needs to be formally approved by the WECA Committee.

November 2019

West of England Combined Authority
Treasury Management Strategy Statement 2020/21

1. Introduction

- 1.1 Treasury management is the management of the Authority's cash flows, borrowing and investments, and the associated risks. The Authority has substantial sums of money invested and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Authority's prudent financial management.
- 1.2 Treasury risk management at the Authority is conducted within the framework of 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 Authority to approve a treasury management strategy before the start of each financial year. This report fulfils the Authority's legal obligation under the *Local Government Act 2003* to have regard to the CIPFA Code.

2. External Context

- 2.1 **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 Authority's treasury management strategy for 2020/21.
- 2.2 UK Consumer Price Inflation (CPI) for September registered 1.7% year on year, unchanged from the previous month and below target. The most recent labour market data, for the three months to August 2019, showed the unemployment rate as 3.9% while the employment rate was 75.9%, just below recent record-breaking highs. The headline 3-month average annual growth rate for pay was 3.8% as wages continue to rise steadily. In real terms, after adjusting for inflation, pay growth increased 1.9%.

- 2.3 GDP growth rose by 0.3% in the third quarter of 2019 from -0.2% in the previous three months with the annual rate falling further below its trend rate to 1.0% from 1.2%. Services and construction added positively to growth, by 0.6% and 0.4% respectively, while production was flat and agriculture recorded a fall of 0.2%. Looking ahead, the Bank of England's Monetary Policy Report forecasts economic growth to pick up during 2020 as Brexit-related uncertainties dissipate and provide a boost to business investment helping GDP reach 1.6% in Q4 2020, 1.8% in Q4 2021 and 2.1% in Q4 2022.
- 2.4 The Bank of England maintained Bank Rate as 0.75% in November 2019 following a 7-2 vote by the Monetary Policy Committee (MPC). Despite keeping rates on hold, MPC members did confirm that if global growth fails to recover, they are prepared to cut interest rates as required.
- 2.5 **Credit outlook:** Credit conditions for larger UK banks have remained relatively benign over the past year. The UK's departure from the European Union was delayed three times in 2019 and while there remains some concern over a global economic slowdown, this has yet to manifest in any credit issues for banks. Meanwhile, the post financial crisis banking reform is now largely complete, with the new ringfenced banks embedded in the market.
- 2.6 Challenger banks hit the news headlines in 2019 with Metro Bank and TSB Bank both suffering adverse publicity and falling customer numbers. Looking forward, the detail of Brexit and/or a global recession remain the major risks facing banks and building societies in 2020/21 and a cautious approach to bank deposits remains advisable.
- 2.7 **Interest rate forecast:** The Authority's treasury management adviser Arlingclose is forecasting that the Bank Rate will remain at 0.75% until the end of 2022. The risks to this forecast are deemed to be significantly weighted to the downside given the need for greater clarity on Brexit and the continuing global economic slowdown.
- 2.8 Gilt yields have risen but remain at low levels and only some modest upward movement from current levels are expected based on Arlingclose's interest rate projections. The central case is for 10-year and 20-year gilt yields to rise to around 1.00% and 1.40% respectively over the time horizon, with broadly balanced risks to both the upside and downside.
- 2.9 For the purpose of setting the budget, it has been assumed that new investments will be made at an average rate of 1.0% for WECA balances, and 0.9% for LGF and RIF balances.

3. Local Context

- 3.1 On 30th November 2019, the Authority held £205m of investments and no borrowing. This is set out in further detail at **Appendix A**.
- 3.2 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.
- 3.3 The Authority is currently debt free and its capital expenditure plans do not currently imply any need to borrow over the forecast period. Investments are forecast to fall to £150m by the end of 2020/21 as capital grants are used to finance capital expenditure and earmarked reserves are spent on their intended purpose.

4. Investment Strategy

- 4.1 The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. Since 1 April 2019, the Authority's investment balance has ranged between £165m and £235m, and similarly for 2020/21 the balances are expected to range between £100m and £210m (slightly lower due to capital grants and reserves being used to finance spend).
- 4.2 As well as holding investments in its own right, the Authority also acts as Accountable Body for the West of England Revolving Investment Fund (RIF) and Local Growth Fund (LGF), holding Government Grants until they are ready to be distributed to Local Authorities and other organisations for approved project spend over the coming years.
- 4.3 The funds are invested primarily to protect the capital and, to achieve a high level of capital security, investments are made predominantly with Central Government, Local Authorities and Banks with high credit ratings. See **Appendix B** for Treasury Monitoring.
- 4.4 Interest earned on RIF investments is re-invested into the Fund. LGF investment returns are earmarked to fund the corporate support and governance costs that come with performing the Accountable Body function for the Local Enterprise Partnership (LEP).
- 4.5 **Objectives:** The CIPFA Code requires the Authority 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 Authority's 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 Authority 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. Given the current level of CPI at 1.7% this will be difficult to achieve with fixed term deposits alone. However, we will continue to consider further longer-term investments within our overall investment portfolio, such as pooled funds, which will achieve a higher rate of return. Any temporary liquidity issues that may arise throughout the year will be dealt with by short term borrowing.

- 4.6 **Negative interest rates:** If the UK enters into a recession in 2020/21, 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 investment 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.
- 4.7 **Strategy:** Given the increasing risk and very low returns from short-term unsecured bank investments, the Authority aims to further diversify into more secure and/or higher yielding asset classes during 2020/21. A reduced proportion of the Authority's surplus cash remains invested in short-term unsecured bank deposits and money market funds. This diversification will represent a continuation of the strategy adopted in 2019/20 with outer limits set for treasury management operations.
- 4.8 **Business models:** Under the IFRS 9 standard, the accounting for certain investments depends on the Authority's "business model" for managing them. The Authority 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.
- 4.9 **Approved counterparties:** The Authority may invest its surplus funds with any of the counterparty types as detailed in *Figure 1*, subject to the cash limits (per counterparty), and the time limits shown.

Figure 1: Approved investment counterparties and limits

Credit rating	Banks unsecured	Banks secured	Government	Corporates	Registered Providers
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£10m 5 years	£15m 20 years	£10m 50 years	£10m 20 years	£5m 20 years
AA+	£10m 5 years	£15m 10 years	£15m 25 years	£5m 10 years	£5m 10 years
AA	£10m 4 years	£15m 5 years	£15m 15 years	£5m 5 years	£5m 10 years
AA-	£10m 3 years	£15m 4 years	£10m 10 years	£5m 4 years	£5m 10 years
A+	£10m 2 years	£15m 3 years	£10m 5 years	£5m 3 years	£5m 5 years
A	£10m 13 months	£10m 2 years	£10m 5 years	£5m 2 years	£5m 5 years
A-	£10m 6 months	£10m 13 months	£10m 5 years	£5m 13 months	£5m 5 years
None	£1m 6 months	n/a	£10m 5 years	£50,000 5 years	£3m 5 years
Pooled funds and real estate investment trusts		£10m per fund or trust			

This table must be read in conjunction with the following notes

- a) **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 considered.
- b) **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.

- c) **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.
- d) **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.
- e) **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 either following an external credit assessment or to a maximum of £50,000 per company as part of a diversified pool in order to spread the risk widely.
- f) **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 for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.
- g) **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.

The Authority may consider further investment in Pooled Funds during 2020/21 with a view to providing further diversification and the potential for earning a higher investment yield on long-term investment balances. Cash that is not required to meet any short or medium-term liquidity can be invested for the

longer term with a greater emphasis on achieving returns that will support spending on local WECA services.

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

- h) **Real estate investment trusts:** Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.
- i) **Operational bank accounts:** The Authority 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 £250,000 per bank. This is a relatively low risk as deposits tend to be only held overnight and can be moved without notice. 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 Authority maintaining operational continuity.
- j) **Risk assessment and credit ratings:** Credit ratings are obtained and monitored by the Authority's treasury advisers, ArlingClose, 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.

- k) **Other information on the security of investments:** The Authority 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, reports in the quality financial press and analysis and advice from the Authority'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 above criteria.

When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority 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 Authority's cash balances, then the surplus will either be deposited with the UK Government, (via the Debt Management Office), invested in government treasury bills or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

- l) **Investment limits:** The maximum that will be lent to any one organisation, (other than the UK Government), will be £10 million. 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 countries and industry sectors. 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. The Authority's revenue reserves, which could be made available to cover any investment losses, are forecast to be £1.3 million on 31st March 2020.

Figure 2: Investment Limits

	Cash limit
Any single organisation, except the UK Central Government	£10m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£10m per group
Any group of pooled funds under the same management	£10m per manager
Negotiable instruments held in a broker's nominee account	£10m per broker
Foreign countries	£15m per country (AAA sovereign rating)
	£10m per country (AA+ sovereign rating)
Registered providers and registered social landlords	£50m in total
Unsecured investments with building societies	£20m in total
Loans to unrated corporates	£20m in total
Money market funds	£100m in total
Real estate investment trusts	£50m in total

m) **Liquidity management:** The Authority uses cash flow forecasting 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 Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium-term financial plan and cash flow forecast.

5. Borrowing Strategy

- 5.1 The Authority currently holds no borrowing. The balance sheet forecast shows that the Authority does not expect to need to borrow in 2020/21.
- 5.2 **Objectives:** The Authority's 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 Authority's long-term plans change is a secondary objective.
- 5.3 **Strategy:** The Authority does not currently have any underlying need to borrow long-term to fund capital expenditure. WECA holds no long-term loans and no long-term borrowing is anticipated during 2020/21. Therefore, a debt-free strategy will be maintained until such time as the Authority determines that its capital strategy and prioritised programme of investment requires consideration of any borrowing decision.
- 5.4 As part of its approach to liquidity management, the Authority may borrow short-term loans to cover any unplanned cash flow shortages as they arise. Rather than always keeping cash on instant access for unplanned cash flows, (where security and liquidity will mean yields will be low), the Authority will retain the option of short-term borrowing at current low rates to enable it to explore increasing investments in longer-term and more diversified assets. The Authority will test access to borrowing occasionally even where this is not required to ensure liquidity is available.
- 5.5 **Sources of borrowing:** The approved sources of 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 Avon Pension Fund)
 - capital market bond investors
 - UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues
- 5.6 **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:
- leasing
 - hire purchase
 - Private Finance Initiative
 - sale and leaseback

- 5.7 **Short-term and variable rate loans:** These loans leave the Authority exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits as detailed in the treasury management indicators.

6. Treasury Management Indicators

- 6.1 The Authority measures and manages its exposures to treasury management risks using the following indicators.

- 6.2 **Security:** The Authority has adopted a voluntary measure of its exposure to credit risk by monitoring the value-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 investment.

Credit risk indicator	Target
Minimum portfolio average credit rating	A-

- 6.3 **Liquidity:** The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount it can borrow each quarter without giving prior notice.

Liquidity risk indicator	Target
Total sum borrowed in past 3 months without prior notice	£30m

- 6.4 **Interest rate exposures:** This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

Interest rate risk indicator	Limit
Upper limit on one-year revenue impact of a 1% <u>fall</u> in interest rates	£900k

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

- 6.5 **Principal sums invested for periods longer than a year:** The purpose of this indicator is to control the Authority'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:

Price risk indicator	2020/21	2021/22	2022/23
Limit on principal invested beyond year end	£100m	£75m	£50m

7. Related Matters

The CIPFA Code requires the Authority to include the following in its treasury management strategy.

- 7.1 **Financial Derivatives:** In the absence of any explicit legal power to do so, the Authority 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.
- 7.2 **Markets in Financial Instruments Directive (MiFID II):** As a result of the directive, Local Authorities will be treated as retail clients, but can opt up to professional client status, providing that they meet certain criteria which includes having an investment balance of at least £10m and the persons authorised to make investment decisions on behalf of WECA having at least a year's relevant professional experience. In addition, the regulated financial services firms to whom this directive applies must assess that these persons have the expertise, experience and knowledge to make investment decisions and understand the risks involved.

The Authority has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

8. Financial Implications

- 8.1 The budget for WECA investment income in 2020/21 is £1.02 million, based on an average investment portfolio of **£110 million** at an interest rate of **1.00%** and making an allowance for impairment as required. In addition, the budget for the LEP investment income in 2020/21 is £0.2 million, based on an average investment of £21 million at an interest rate of 0.9%. The differing levels of interest expected to be achieved reflect the ability to invest WECA funds for longer terms and hence achieve a higher return. Longer term investment of LEP funds is limited as LGF grant will be fully spent by March 2021. Actual levels of investments, and interest rates attained, will updated in budget monitoring reports to committee throughout the financial year.

9. Other Options Considered

- 9.1 The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer, having consulted the West of England Mayor and Chief Executive, 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 listed 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

Appendix A – Existing Investment & Debt Portfolio Position

	30-Nov-19 Actual Portfolio £m	30-Nov-19 Average Rate %
External borrowing:	0	0
Other long-term liabilities:	0	0
Total gross external debt	0	0
Treasury investments:		
Banks & building societies (unsecured)	20	0.89
Covered bonds & repo (secured)	0	0
Government (incl. local authorities)	135	0.97
Corporate bonds and loans	0	0
Money Market Funds	30	0.73
Other pooled funds		
CCLA Property Fund	10	4.11
Investec	7	3.00
Kames	3	3.00
Real estate investment trusts	0	0
Total treasury investments	205	1.19
Net debt	0	0

Appendix B – Treasury Management Monitoring

The Authority's investment position as at 30th November 2019 is detailed below. This shows a balance held of £205m which is an increase from £170m at 31st March 2019.

As shown in the charts, the investment portfolio has been diversified across UK banks, Building Societies and Local Authorities. The Authority also uses AAA rated Money Market Funds to maintain short term liquidity with £30.3m invested as at 30th November 2019. The Authority also retains units in pooled funds with £10m invested with the CCLA Property Fund, £7m with Investec and £3m with Kames.

The forecast investment income to 31st March 2020 is £1.4m with an average rate of interest earned of circa 1.2%.

Investments are forecast to fall to £150m by the end of the 2019/20 financial year as capital grants are used to finance capital expenditure and project spend. Investments have been staggered, in terms of maturity dates, to ensure that there is a reasonable balance of available liquidity to finance required spend.

The Authority's term of investments are as follows:	Balance as at 30th Nov 2019 £000s
Instant Access Funds	30,300
Pooled	19,957
Up to 1 month	19,800
1 month to 3 months	40,000
4 month to 6 months	40,000
6 month to 12 months	35,000
More than 12 months	20,000
	205,057

Type / Lendee	Credit Rating	Amount	Average Rate	Start	End
Notice					
Goldman Sachs - 95 Days	A	10,000,000			
Lloyds - 95 Day	A	10,000,000			
		20,000,000	0.89%		
Money Market Funds					
Aberdeen Liquidity	AAA	600,000			
Federated	AAA	10,000,000			
Blackrock	AAA	9,850,000			
Insight	AAA	9,850,000			
		30,300,000	0.73%		
Pooled Funds					
CCLA		9,956,738			
Investec		7,000,000			
Kames		3,000,000			
		19,956,738	3.37%		
Local Authorities & Banks					
DMO (Debt Management Workshop)	LA	1,800,000		19/11/2019	02/12/2019
Thurrock Council	LA	8,000,000		19/06/2019	19/12/2019
Slough Borough Council	LA	5,000,000		25/02/2019	02/01/2020
Highland Council	LA	5,000,000		20/02/2019	27/01/2020
West Dumbartonshire Council	LA	10,000,000		26/04/2019	27/01/2020
Dundee City Council	LA	5,000,000		29/01/2019	28/01/2020
Birmingham City Council	LA	5,000,000		31/07/2019	31/01/2020
Warrington BC	LA	5,000,000		19/06/2019	19/02/2020
Yarmouth Borough Council	LA	10,000,000		16/05/2018	15/05/2020
Salford City Council	LA	5,000,000		01/08/2019	01/06/2020
Rotherham MBC	LA	10,000,000		26/04/2019	01/06/2020
Suffolk County Council	LA	5,000,000		09/08/2019	09/06/2020
Liverpool City Council	LA	5,000,000		04/10/2019	06/07/2020
Mid Suffolk District Council	LA	5,000,000		06/07/2018	06/07/2020
South Ayrshire Council	LA	5,000,000		19/08/2019	20/07/2020
London Borough of Croydon	LA	5,000,000		30/07/2019	28/07/2020
London Borough of Brent	LA	5,000,000		28/11/2019	28/08/2020
Liverpool City Council	LA	5,000,000		29/11/2019	28/08/2020
Aberdeenshire Council	LA	10,000,000		29/10/2019	02/09/2020
Lancashire Council	LA	10,000,000		31/10/2019	29/10/2020
North Lanarkshire Council	LA	5,000,000		29/01/2019	29/01/2021
Cambridgeshire County Council	LA	5,000,000		01/02/2019	01/02/2021
		134,800,000	0.97%		
		205,056,738	1.19%		

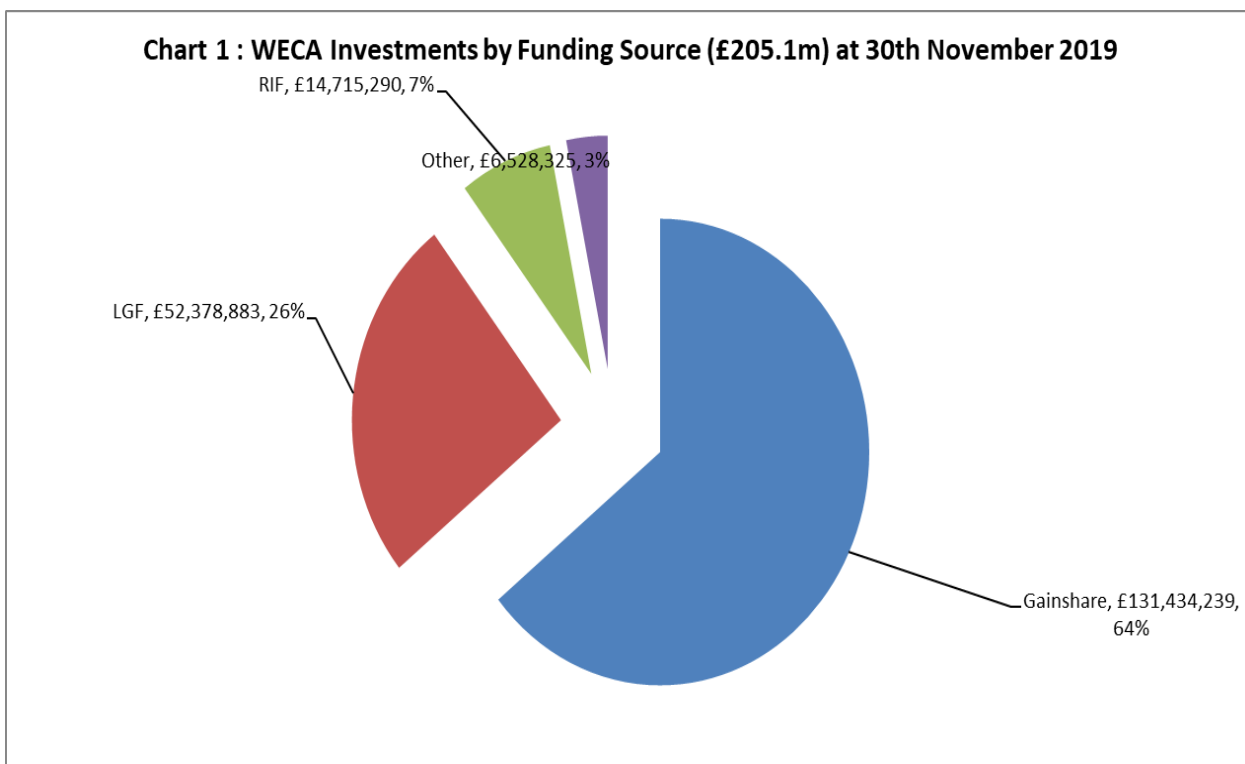


Chart 2: WECA Investments per lowest equivalent Long Term credit rating (£205.1m) at 30th November 2019

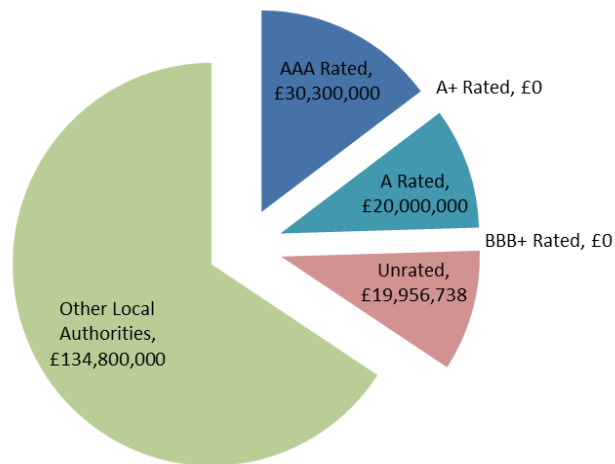


Chart 3: WECA Investments by Type (205.1m) as at 30th November 2019

