North Wales Police and Crime Commissioner's Capital Strategy 2019/20

1. Introduction

1.1 This Capital Strategy is a new report for 2019/20, giving a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of police services along with an overview of how associated risk is managed and the implications for future financial sustainability. The new format stems from the Treasury Management in the Public Service: Code of Practice and Cross sectorial Guidance Note (TM Code) which was updated by CIPFA in 2017. There is a legal requirement to abide by the Code.

1.2 The new format includes this overriding Capital Strategy which can be thought of as an executive summary of the elements listed above. North Wales Police have historically included the elements listed within the previous Treasury Management Strategy and there is no fundamental change to the overall strategy from last years. A number of the elements are technical in nature; the intention is for this overriding Capital Strategy to be written in an accessible style to enhance understanding of these areas. Details of the Capital Programme, Revenue Provision for Borrowing and the Treasury Management and Investment Strategy 2019/20 to 2024/25 are attached in the appendices.

2. Capital Expenditure and Financing

2.1 Capital expenditure is where the Police and Crime Commissioner spends money on assets, such as property or vehicles, that will be used for more than one year.

2.2 The draft Capital Programme was presented to the Strategic Executive Board (SEB) on the 31 January 2019 and agreed subject to the final ratification of this Capital Strategy. The Police and Crime Commissioner is planning capital expenditure as summarised below, with the details as presented to SEB shown in Appendix A:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

	2017/18 actual	**2018/19 forecast**	**2019/20 budget**	**2020/21 budget**	**2021/22 budget**	**2022/23 budget**	**2023/24 budget**	**2024/25 budget**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Total Capital Expenditure	18.4	12.9	6.7	6.6	7.9	5.1	6.6	3.0

2.3 **Governance**: The Capital Programme has been fully revised as part of the 2019/20 planning cycle. The previous Capital Programme was coming to an end in 2018/19 with the completion of major schemes such as the new facilities in Wrexham and the upgrade and replacement of the Control Room IT system. Over the period 2011 to 2018 £70m will have been invested in new and replacement infrastructure as highlighted below:

- **Estates -** 4 Major new builds in Llangefni, Llandudno, Llay and Wrexham town centre plus 20+ other refurbs and relocations (£41m)
- **Fleet -** Vehicle Replacement Programme continued and reduced from £1.5m to £1.3m from 2019-20 from Fleet reductions (£15m)
- **IT -** Network upgraded, Servers Replaces, Control Room Technology Replacement, Desk top replacement and mobile units replacements (£14m)

2.4 The Capital Programme 2019-20 to 2024-25 is as a result of the new Estates Strategy, Digital Transformation Strategy, fleet replacement strategy and the conclusion of the planning cycle. A review was also conducted at the end of the cycle to ensure that end of life equipment were being replaced if required. As a number of the Estates and IT schemes are in their infancy detailed budget cases will need to be agreed for individual projects before they are commissioned. The Capital Programme is reported to the Strategic Planning Board (SPB) and the SEB as a whole. Specific areas of work are managed through the Digital Transformation Board and the Estates Board.

2.5 The main capital projects for 2019/20 include the refurbishment of Pwllheli Police Station £0.98m, Digital Transformation £3.5m and annual vehicle replacement £1.3m.

2.6 All capital expenditure must be financed, either from the Police and Crime Commissioner's own resources (revenue, reserves and capital receipts), from external sources (government grants and other contributions) or debt (borrowing, leasing and Private Finance Initiative). Government Capital Grants fund just over 1/3 of the Vehicle Replacement Programme (£0.462m), requiring the majority of the Programme to be funded from PCC's funds. The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ millions

	2017/18 actual	2018/19 forecast	2019/20 budget	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2024/25 budget
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
External sources	0.5	0.5	0.6	0.5	0.5	0.5	0.5	0.5
Own resources	15.2	6.6	4.9	2.2	1.5	0.9	2.3	1.3
Debt	2.7	5.8	1.1	3.9	5.9	3.7	3.9	1.3
TOTAL	**18.4**	**12.9**	**6.7**	**6.6**	**7.9**	**5.1**	**6.7**	**3.1**

2.7 Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as minimum revenue provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP is as follows:

Table 3: Replacement of debt finance in £ millions

	2017/18 actual	2018/19 forecast	2019/20 forecast	2020/21 forecast	2021/22 forecast	2022/23 budget	2023/24 budget	2024/25 budget
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Own resources	2.2	2.1	2.3	2.2	2.4	2.6	2.6	3.0

- The Police and Crime Commissioner’s full minimum revenue provision statement is shown in Appendix B to this report.

2.8 The Police and Crime Commissioner’s cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to decrease by £1.2m during 2019/20, and then increase £5.9m over the following 5 years. Based on the above figures for expenditure and financing, the Police and Crime Commissioner’s estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions

	31.3.18 actual	31.3.19 forecast	31.3.20 forecast	31.3.21 forecast	31.3.22 forecast	31.3.23 forecast	31.3.24 forecast	31.3.25 forecast
	£m	£m	£m	£m	£m	£m	£m	£m
Total CFR	**27.2**	**31.0**	**29.8**	**31.5**	**35.0**	**36.1**	**37.4**	**35.7**

2.9 **Asset management:** To ensure that capital assets continue to be of long-term use, the Police and Crime Commissioner has an asset management strategy in place. This is detailed in the Estates Strategy and the Digital Transformation Strategy.

2.10 **Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Police and Crime Commissioner is not anticipating to receive any significant capital receipts in the coming financial years.

Table 5: Capital receipts in £ millions

	17/18 actual	18/19 forecast	19/20 forecast	20/21 forecast	21/22 forecast	22/23 forecast	23/24 forecast	24/25 forecast
	£m	£m	£m	£m	£m	£m	£m	£m
Opening balance	**3.7**	**1.5**	**0.0**	**2.0**	**2.0**	**1.6**	**1.7**	**0.8**
Receipts	**0.8**	**0.5**	**2.7**	**0.2**	**0.0**	**0.2**	**0.5**	**0.4**
Budgeted use	**3.0**	**2.0**	**0.7**	**0.2**	**0.4**	**0.1**	**1.4**	**0.5**
Balance	**1.5**	**0.0**	**2.0**	**2.0**	**1.6**	**1.7**	**0.8**	**0.7**

3. Treasury Management

3.1 Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Police and Crime Commissioner's spending needs, while 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 Police and Crime Commissioner is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

3.2 The Treasury Management Strategy (Appendix C) and the set out the parameters under which the Treasury Management activities are governed and monitored. These are bases on prioritising security first, liquidity second and yield last. This does reduce potential investment income but minimises the risk of losing money though riskier investments. The below summarises the main points of the Treasury Management Strategy.

3.3 **Borrowing strategy:** The Police and Crime Commissioner's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Police and Crime Commissioner therefore seeks to strike a balance between cheap short-term loans (currently available at around 0.95%) and long-term fixed rate loans where the future cost is known but higher (currently 2.0 to 3.0%).

3.4 The Borrowing Strategy is also balanced by the use of revenue cash available (reducing investments) being used rather than borrowing, known as internal borrowing. Internal borrowing has been used extensively over recent years saving around £0.250m in interest charges per year and reducing risk by not investing cash. However, use of reserves to fund Capital has reduced the available amounts to internally borrow. Another factor to consider is that the Police and Crime Commissioner's income is not constant during the year; this is due to a Pension Grant of around £20m being paid in one lump sum each July. This has resulted in short term borrowing being required for 6 to 8 months of the year. At some point longer term borrowing will need to be secured, this is being monitored and discussed with our Treasury Management consultants on a regular basis.

3.5 Projected levels of the Police and Crime Commissioner's total outstanding debt (which comprises borrowing and PFI liabilities) are shown below, compared with the capital financing requirement (see above). These are based on the current position to inform future decisions, which is the timing of longer term borrowing.

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions

	31.3.18 actual	**31.3.19 forecast**	**31.3.20 forecast**	**31.3.21 forecast**	**31.3.22 forecast**	**31.3.23 forecast**	**31.3.24 forecast**	**31.3.25 forecast**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
PFI	**11.4**	**10.7**	**9.9**	**9.1**	**8.2**	**7.3**	**6.2**	**5.1**
Long Term Loans	**1.4**	**0.7**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Short Term loans	**10.0**	**16.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Debt (incl. PFI & leases)	**22.7**	**27.3**	**9.9**	**9.1**	**8.2**	**7.3**	**6.2**	**5.1**
Capital Financing Requirement	**27.2**	**31.0**	**29.8**	**31.5**	**35.0**	**36.1**	**37.4**	**35.7**

3.6 Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the Police and Crime Commissioner expects to comply with this in the medium term, but this will need to be part of the assessment when new borrowing is taken on.

3.7 **Affordable borrowing limit:** The Police and Crime Commissioner is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year and to keep it under review. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	2018/19 limit	***2019/20 limit***	***2020/21 limit***	***2021/22 limit***	***2022/23 limit***	***2023/24 limit***
	£m	***£m***	***£m***	***£m***	***£m***	***£m***
Authorised limit – borrowing	*19.8*	*22.4*	*26.8*	*28.8*	*31.2*	*30.6*
Authorised limit – PFI and leases	*10.7*	*9.9*	*9.1*	*8.2*	*7.3*	*6.2*
Authorised limit – total external debt	***30.5***	***32.3***	***35.9***	***37.1***	***38.4***	***36.8***
Operational boundary – borrowing	*19.8*	*20.4*	*24.8*	*26.8*	*29.2*	*28.6*
Operational boundary – PFI and leases	*10.7*	*9.9*	*9.1*	*8.2*	*7.3*	*6.2*
Operational boundary – total external debt	***30.5***	***30.3***	***33.9***	***35.1***	***36.4***	***34.8***

3.8 **Investment strategy:** Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

3.9 The Police and Crime Commissioner'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. Money that will be held for longer terms is 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 Police and Crime Commissioner may request its money back at short notice.

Table 8: Treasury management investments in £millions

	31.3.2018 actual	31.3.2019 forecast	31.3.2020 forecast	31.3.2021 forecast	31.3.2022 forecast
	£m	**£m**	**£m**	**£m**	**£m**
Near-term investments	21.1	15.0	15.0	15.0	15.0
Longer-term investments	0	0	0	0	0
TOTAL	**21.1**	**15.0**	**15.0**	**15.0**	**15.0**

3.10 **Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Head of Finance and staff, who must act in line with the treasury management strategy approved by the Police and Crime Commissioner and Joint Audit Committee. End of year and half year reports on treasury management activity are presented to SEB and the Joint Audit Committee. Any additional reporting required will be reported through the quarterly Finance reports to SEB and SPB, or directly between the Head of Finance and DFR and CFO as required. The Joint Audit Committee is responsible for scrutinising treasury management decisions.

3.11 **Liabilities:** In addition to debt detailed above, the Police and Crime Commissioner is committed to making future payments to cover its pension funds costs. Police Officers pension scheme is an unfunded scheme which is underwritten by the Government, liabilities stands at £1,645m as at 31.3.18. The cost to the Police and Crime Commissioner is the employer contribution rate, this has been increased from 24.2% to 31% from 1 April 2019 and has had to be funded from the revenue budget. The deficit on the Staff Pension fund stood at £60m as at 31.3.18, this is also managed through the contribution rate which is currently set at 16.3%. The Police and Crime Commissioner has also set aside £1.2m as a provision to cover risks of insurance claims and employment cases. The Police and Crime Commissioner is also at risk of having to pay for claims lodged with the Central London Employment Tribunal. These risks have been recognised as Contingent Liabilities in the Statement of Accounts, but The Police and Crime Commissioner has not put aside any money because the claims are subject to appeal, and there is uncertainty regarding remedy and quantum.

3.12 **Governance:** Decisions on incurring new discretional liabilities are taken by the Chief Officer Team in consultation with the Police and Crime Commissioner and his Chief Finance Officer. The risk of liabilities crystallising and requiring payment is monitored by Corporate Finance and reported to SPB and SEB as necessary. Details of contingent liabilities as at the 31 March will be included in the Statement of Accounts.

3.13 **Revenue Budget Implications -** Although capital expenditure is not charged directly to the revenue budget, interest payable on loans, Minimum Revenue Provision (MRP) for reducing the CFR and direct revenue contribution to capital are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Police and Crime Commissioners' Council Tax and general government grants.

Table 9: Prudential Indicator: Proportion of financing costs to net revenue stream

	2017/18 actual	**2018/19 forecast**	**2019/20 budget**	**2020/21 budget**	**2021/22 budget**	**2022/23 budget**	**2023/24 budget**
Financing costs (£m)	4.9	4.1	4.1	4.2	4.2	4.3	4.3
Proportion of net revenue stream	3.42%	2.90%	2.68%	2.65%	2.61%	2.58%	2.55%

3.14 **Sustainability:** Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 40 years into the future. The Police and Crime Commissioner's Chief Finance Officer and the Director of Finance and Resources are satisfied that the proposed capital programme is prudent, affordable and sustainable as there are revenue streams or reserves in place to fund the Programme as set out. It is likely that additional resources will need to be budgeted for future investments beyond the current Programme.

3.15 **Knowledge and Skills -** The Police and Crime Commissioner employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. Training is provided to all staff involved in making capital expenditure, borrowing and investment decisions.

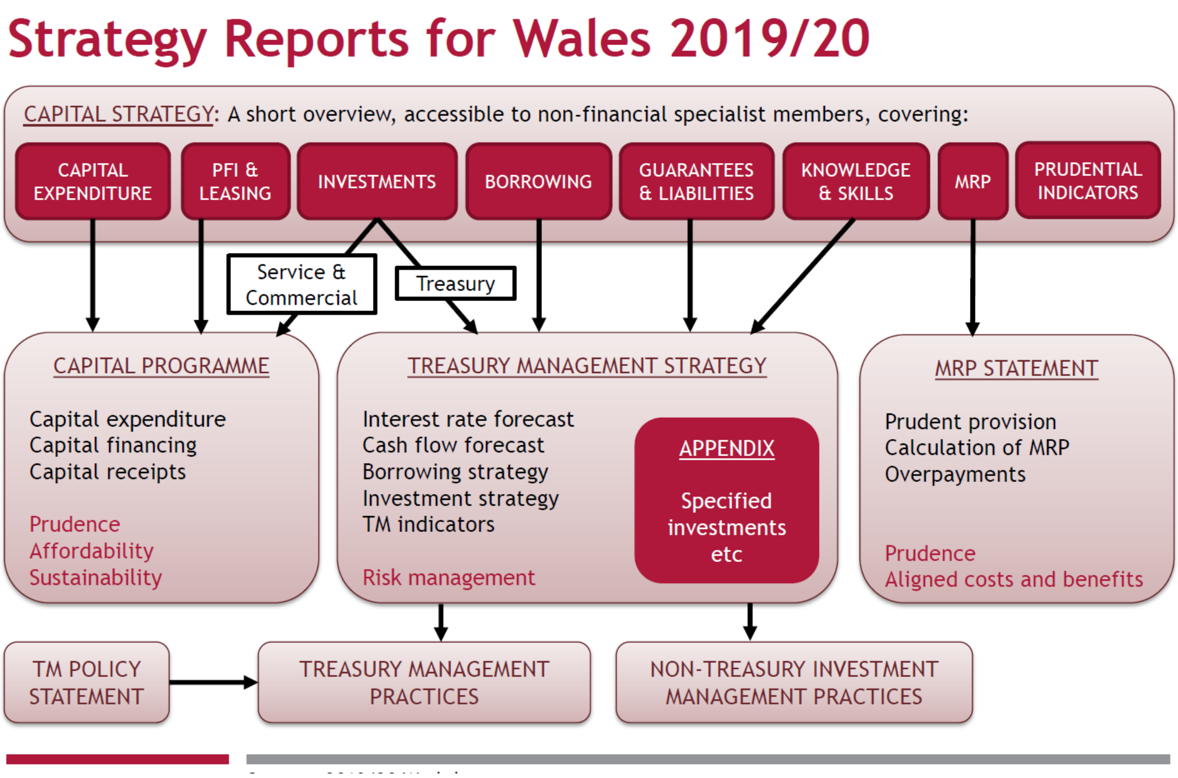
3.16 Where Police and Crime Commissioner staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Police and Crime Commissioner currently employs Arlingclose Limited as treasury management advisers, Wilks Head and Eve as property consultants and BDO as tax consultants. This approach is more cost effective than employing such staff directly, and ensures that the Police and Crime Commissioner has access to knowledge and skills commensurate with its risk appetite.

Appendix A

Extract from SEB report 31.1.2019

5. DRAFT CAPITAL BUDGET 2018-19 to 2024-25

5.1 The first draft of the Capital Programme 2018-19 to 2024-25 was discussed during the budgets meetings and included as a draft in the MTFP. However, further work was required to confirm funding available, confirm final additions to the programme (from the additionality), update phasing and check final requirements. This work has been done as far as possible now and the details are shown below. There is likely to be further re profiling of specific schemes. The individual projects are subject to business cases to be presented to the relevant Boards. It is recommended that the below be included in the 'Capital Strategy' which will formally ratify the Programme for 2018-19 and 2019-20 and the draft for future years (as well as the Treasury Management Strategy). The Capital Strategy is due be scrutinised by the Joint Audit Committee on 21 March 2019. Details of what's covered in the Capital Strategy are given in the first table, followed by the Capital Programme. Details of the projects are covered in the following sections.



Capital Programme 2018-19 to 2024-25

Ref	Description	Actual to to 31.3.18	Orig Est with c/f	2018-19 Revised Est Jan 19	Actual to Date Pd 9	2019-20 Est	2020-21 Est	2021-22 Est	2022-23 Est	2023-24 Est	2024-25 Est	Total Project Costs
		£000	£000	£000	*£000*	£000	£000	£000	£000	£000	£000	£000
	Estate Programme											
1	Retentions, Consultancy and QS	***7***	**25**	**25**	*0*	0						**32**
2	Sustainability Improvements	***573***	**155**	**155**	*0*	100	100	100	100	100	100	**1,328**
3	Wrexham new Custody and DHQ	***18,651***	**2,649**	**2,649**	*2,253*							**21,300**
4	Wrexham in town facility	***246***	**1,622**	**1,622**	*926*	170						**2,038**
5	Rhuddlan/Prestatyn works	***0***	**80**	**80**	*58*							**80**
6	Buckley Relocation	***41***	**0**	**0**	*0*							**41**
7	LlandudnoNew Build	***2,742***	**63**	**63**	*4*							**2,805**
8	Holyhead Port	***190***	**30**	**30**	*0*							**220**
9	OHU Relocation	***215***	**0**	**0**	*0*							**215**
10	**Estate Review 2**	***0***	**499**	**0**	*0*	0	0	0	0	0	0	**0**
11	*Pwllheli PS*	***0***	**0**	**0**		980						**980**
12	*Conwy PS **	***0***	**0**	**0**		0						**0**
13	*Holyhead PS*	***0***	**0**	**0**			772	2,570				**3,342**
14	*FHQ Complex + Canteen*	***0***	**0**	**0**			257					**257**
15	*Western Estate Area*	***0***	**0**	**0**			515					**515**
16	*VCC / Vehicle Workshop*	***0***	**0**	**0**			1,545	1,325				**2,870**
17	*Dolgellau PS*	***0***	**0**	**0**					545	2,391		**2,936**
18	*Abergele PS*	***0***	**0**	**0**							391	**391**
19	*Llanrwst PS*	***0***	**0**	**0**							178	**178**
20	*Deeside PS*	***0***	**0**	**0**						1,400	575	**1,975**
21	*Mold PS*	***0***	**0**	**0**					2,834			**2,834**
22	*Rhosllanerchrugog PS*	***0***	**0**	**0**							189	**189**
23	*Re locate/ co locate/ vacate*	***0***	**0**	**0**		185	127					**312**
24	Custody CCTV	***23***	**52**	**52**	*0*							**75**
25	Purchase of JCC	***0***	**2,739**	**2,739**	*2,806*							**2,739**
	Total Building Works	***22,688***	**7,914**	**7,415**	***6,047***	**1,435**	**3,316**	**3,995**	**3,479**	**3,891**	**1,433**	**47,652**
	Vehicles and Other Equipment											
26	Vehicle Purchase Replacement Programme	***7,481***	**2,233**	**2,233**	*971*	1,405	1,300	1,300	1,300	1,300	1,300	**17,619**
27	PSU Vehilces (Revenue Stream replacemnt programme)	***555***	**0**	**0**	*0*			555				**1,110**
28	Ports CCTV and ANPR and equipment (Check KN)	***125***	**104**	**150**	*0*							**275**
29	Dexun System (SCC)	*0*				78						78
30	Intoxilators x 3	*0*					30					30
31	ANPR replacement	*0*					470					470
32	Fingerprint Capture and Enhancement Equipment	*0*				62						62
33	Collision Surveying Equipment	*0*				131						131
	Total Vehicles and Other Equipment	***8,161***	**2,337**	**2,383**	***971***	**1,676**	**1,800**	**1,855**	**1,300**	**1,300**	**1,300**	**19,775**

Ref	Description	Actual to 31.3.18	2018-19 Orig Est with c/f	2018-19 Revised Est Jan 19	2018-19 Actual to Date Pd 9	2019-20 Est	2020-21 Est	2021-22 Est	2022-23 Est	2023-24 Est	2024-25 Est	Total Project Costs
		£000	£000	£000	*£000*	£000	£000	£000	£000	£000	£000	£000
	Information Technology and Communication Equipment											
34	Desk Top Replacement (Replacement Programme)	***963***	**588**	**588**	*528*	462	707	200	300	300	300	**3,820**
35	Control Room Technology Replacemnt	***1,650***	**1,281**	**1,281**	*871*							**2,931**
36	Server Replacement	***672***	**0**	**0**	*0*			700				**1,372**
37	Business Systems Servers (Replacement Programme)	***162***	**14**	**1**	*1*			145				**308**
38	Criminal Justice Digital Project	***613***	**227**	**0**	*0*							**613**
39	Mobile data devices	***825***	**231**	**231**	*70*	0	460		0	460		**1,976**
40a	Airwave (replacement units)	***62***	**96**	**596**	*0*							**658**
40b	Airwave replacement ESN		**0**	**0**	*0*	0		1,000				**1,000**
41	Wrexham Prison IT and Connection	***86***	**0**	**0**	*0*							**86**
42	DFU Server replacement	***149***	**119**	**119**	*109*		20			270		**558**
43	Intranet/Social Media	***0***	**55**	**55**	*2*							**55**
44	Cloud Storage	***0***	**79**	**79**	*0*							**79**
45	Mobile Responder App	***0***	**268**	**0**	*0*	268						**268**
46	EIS Replacement	***263***	**130**	**130**	*117*							**393**
47	CHORUS Upgrade	***0***	**30**	**30**	*30*							**30**
48	NEP Infrastructure/Sail Point/Internet Links	***0***	**0**	**0**	*0*	471						**471**
49	Connectivity Software	***0***	**0**	**0**	*0*	85						**85**
50	Wifi	***0***	**0**	**0**	*0*	250	250					**500**
51	Digital Workplace audio visiual	***0***	**0**	**0**	*0*	200						**200**
52	Single on line Home	***0***	**0**	**0**	*0*	40						**40**
53	**EOL (End of Life - various systems)**	***0***	**0**	**0**	*0*	0						**0**
54	*CISCO Telephony*	***0***	**0**	**0**	*0*	250						**250**
55	*Email (then re-used for NEP)*	***0***	**0**	**0**	*0*	220						**220**
56	*Nexus Memory Upgrade*	***0***	**0**	**0**	*0*	50						**50**
57	*Backup*	***0***	**0**	**0**	*0*	130						**130**
58	*LAN*	***0***	**0**	**0**	*0*	80						**80**
59	*Thin Clients*	***0***	**0**	**0**	*0*	50						**50**
60	*Risk Register*	***0***	**0**	**0**	*0*	100						**100**
61	*ICAD Upgrade*	***0***	**0**	**0**	*0*	500						**500**
62	Body Worn Video	*0*				400				400		800
	Total Information Technology and Communication	***5,445***	**3,118**	**3,110**	***1,728***	**3,556**	**1,437**	**2,045**	**300**	**1,430**	**300**	**17,623**
	Total Capital Expenditure	***36,294***	**13,369**	**12,908**	***8,746***	**6,667**	**6,553**	**7,895**	**5,079**	**6,621**	**3,033**	**85,050**

5.2 Estates

5.2.1 2018-19 – Draft revised budget £7.415, Expenditure to Pd 9 £6.047m.

- Sustainability budget, this budget will be used to fund sustainability elements of the Llay project.
- Wrexham DHQ is now operational. The project is on budget but there is no headroom for additional requirements within the Capital Budget. An additional amount of £0.096m for Airwave connectivity has been funded from the Airwave/ESN Capital Budget. Any additional furniture and equipment not covered by the project budget will need to be funded from other existing budgets where possible, with £0.2m being earmarked in contingency as stated in the revenue section.

- Wrexham Town Centre – delays due to finding asbestos on the site has put pressure on the budget. The costs are being reviewed and are currently projected to be £0.170m over the original budget, this amount has now been added to the current draft budget. There are likely to be further costs relating to the temporary Town Centre Station, these are being funded through revenue contingency.
- An additional £0.080m has been included for works at Rhuddlan and Prestatyn following the loss of the rented Prestatyn base. This has been funded from within the Capital Programme.
- The Joint Control Room in Prestatyn has been purchased. This will result in revenue savings of £0.1m per year compared to the current rental costs. The rules around Land Tax changed from the original business case with the Welsh Government setting these rates from 1.4.2018; this has resulted in £0.063m additional one off costs which will be funded from the 2018-19 rental saving.

5.2.2 **Estates 2019-20 to 2024-25** – The proposals shown are based on the conclusion of the Estates Review. The Schemes put forward have been prioritised using the matrix set out as part of the review. The individual schemes will need to be further developed and agreed scheme by scheme. The most mature scheme is the refurbishment of Pwllheli, this proposal has previously been discussed in detail and agreed at the Estates Board and a final updated version is being progressed to be formally agreed.

5.3 **Vehicles and Equipment**

5.3.1 **2018-19** - Draft revised budget £2.383m, expenditure to date £0.971m. The budget includes £0.660m carried forward from 2017-18. There may some slippage into 2019-20 depending on delivery dates which are currently being reviewed. Additional grant of £0.115m has been secured towards the upgrading of the Ports ANPR system.

5.3.2 **2019-20 to 2024-25** – This includes the replacement Programme for Vehicles at £1.3m per annum, the PSU replacement programme and an additional amount from the 2019-20 additionality. Once the Telematics system has been implemented the level of Fleet replacement can be reviewed. Amounts for the replacement of the Dexun system (SCC), Intoxilators in Custody, Fingerprint Equipment and Collision Investigation Equipment have been included as these have been identified as equipment reaching their end of life and critical for operational delivery. Replacement of all ANPR cameras has been included, although this needs to be detailed and scrutinised as the Welsh Government funded around half of the original instalment.

5.4 **IT and Communications Equipment**,

5.4.1 2018-19 - Draft revised budget £3.110m, Expenditure to date £1.728m.

- Desk Top replacement, budget includes £0.172m carry forward for planned upgrades as part of the moves in Wrexham.
- Payments for the Control Room upgrade are made on milestones being met, as these have not been satisfactorily met payments have been held back. Revised milestone payments have been made, with a 20% retention being held currently. There may be additional costs resulting from the issue following going live, discussions are on-going as to whether any of these are recoverable, or otherwise they will need to be funded.
- Airwave Units – Airwave Units need to be replaced due to the national delay in implementing ESN. A total of 1,056 units need replacing as their GPS chip will become defunct at the end of March 2019. It is intended to fund this from the revenue underspend. The cost of these replacements is £0.501m a further £0.096m was required to improve Airwave reception in Llay.

5.4.2 **2019-20 to 2024-25** – This section includes the replacement programme, the 'Desk Top' replacement includes desk tops, laptops and the 'two in ones' personal issue devices. Additional funding of £0.4m to pump prime the two in ones and £0.062m additional for the growth posts has been included. Lines 48 to 61 reflect the Digital investment and end of life equipment detailed during the budget cycle. This includes the capital element of the National Enablement Programme. These investments are managed through the Digital Transformation Programme Board. An amount of £0.4m is included in 2019-20 for the replacement of Body Worn Video equipment, for which a business case is currently being drafted.

5.5 **Funding** – based on the current revenue budget, estimated grants, and reserves available the Programme is affordable and funded as shown below.

Ref	Description	2018-19			2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	Total Fundinmg 18-19 to 24-25
		Orig Est with c/f	**Revised Est Jan 19**		**Est**	**Est**	**Est**	**Est**	**Est**	**Est**	
		£000	**£000**	***£000***	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**
	Funding										
	Home Office Grant	**462**	**462**		567	462	462	462	462	462	**3,339**
	Revenue Contribution	**1,432**	**2,047**		1,712	1,243	1,116	838	838	838	**8,632**
	Earmarked Reserves	**2,947**	**2,558**		2,549	770	0	0	0	0	**5,877**
	Capital Recipts	**2,851**	**2,008**		674	155	377	100	1,420	475	**5,209**
	Borrowing for Estates	**5,124**	**5,294**		1,165	3,216	3,895	3,379	3,141	958	**21,048**
	Borrowing for replacement programme	**553**	**539**		0	707	2,045	300	760	300	**4,651**
	Total Funding	**13,369**	**12,908**		6,667	6,553	7,895	5,079	6,621	3,033	48,756

5.6 The funding includes an additional £25.7m ‘borrowing’ (this may be ‘internal’ or external borrowing), the majority of this is to fund the Estates Programme. Over the same period the borrowing total (known as the Capital Financing Requirement (CFR)) is budgeted to be reduced by £12.3m through repayment of loans, a net increase of £13.4m over 7 years. (Updated: Reduction of £17.3m including PFI payments, net movement of £8.4m). The revenue contribution amount is reduced to the minimum required to fund the Vehicles replacement programme of £0.838m, this amount plus the Capital grant of £0.462m is required to fund vehicle replacements. Earmarked reserves are being used to fund £5.8m of the Programme, the vast majority of this is being used to fund digital investment. Capital receipts have been profiled towards the end of the programme to manage the risk of the receipts not materialising.

APPENDIX B

Minimum Revenue Provision (for debt re payment) Annual Statement

The Local Authorities (Capital Finance and Accounting)(Wales)(Amendment) Regulations 2008 (SI 2008/588 (W.59)) place a duty on local authorities to make a prudent provision for debt redemption. Guidance on Minimum Revenue Provision has been issued by the Secretary of State and local authorities are required to “have regard” to such Guidance under section 21(1B) of the Local Government Act 2003, the guidance were last updated by Ministers in 2018.

The four MRP options available are:

- Option 1: Regulatory Method
- Option 2: CFR Method
- Option 3: Asset Life Method
- Option 4: Depreciation Method

NB This does not preclude other prudent methods.

Capital expenditure incurred during 2018-19 will not be subject to a MRP charge until the year following the asset becoming operational.

MRP in 2019-20: Options 1 and 2 may be used only for capital expenditure incurred before 1 April 2008 and any supported (i.e. financing costs deemed to be supported through Revenue Support Grant from Central Government) capital expenditure funded from borrowing. Methods of making prudent provision for unsupported capital expenditure include Options 3 and 4 (which may also be used for supported capital expenditure if the Commissioner chooses).

The Police and Crime Commissioner will apply Option 2 in respect of historical supported capital expenditure, applying a 4% charge of the balance at the end of the proceeding year.

The Police and Crime Commissioner Option 3 in respect of unsupported capital expenditure which is calculated on a straight line basis resulting in annual equal instalments as set out below.

Equal instalment method

MRP is the amount given by the following formula:

$$\frac{A - B}{C}$$

Where-

A is the amount of the capital expenditure in respect of the asset financed by borrowing or credit arrangements
B is the total provision made before the current financial year in respect of that expenditure
C is the inclusive number of financial years from the current year to that in which the estimated life of the asset expires.

The life of the asset is provided by Wilks Head and Eve as property consultants in relation to estate assets and professional judgement in the case of shorter life assets.

If it is ever proposed to vary the terms of the original MRP Statement during the year, a revised statement will be brought to Joint Audit Committee and Strategic Executive Board.

MRP in respect of leases brought on to the Balance Sheet under the IFRS-based Code of Practice will match the annual principal repayment for the associated deferred liability.

The above complies with the guidance on Minimum Revenue Provision as set out by the Welsh Government.

Appendix C

Draft Treasury Management Strategy Statement and Investment Strategy 2018-19 to 2022-23

1. Introduction

1.1 Treasury management is the management of the organisation’s cash flows, borrowing and investments, and the associated risks. The Police and Crime Commissioner has invested substantial sums of money 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 organisation’s prudent financial management.

1.2 Treasury risk management at the organisation 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 Police and Crime Commissioner to approve a treasury management strategy before the start of each financial year. In addition, the Welsh Government (WG) issued revised Guidance on Local Authority Investments in March 2010 that requires the Police and Crime Commissioner to approve an investment strategy before the start of each financial year. This report fulfils the Police and Crime Commissioner’s legal obligation under the *Local Government Act 2003* to have regard to both the CIPFA Code and the WG Guidance.

1.3 **Revised strategy:** In accordance with the WG Guidance, the Police and Crime Commissioner will be asked to approve a revised Treasury Management Strategy Statement should the assumptions on which this report is based change significantly. Such circumstances would include, for example, a large unexpected change in interest rates, in the Police and Crime Commissioner’s capital programme or in the level of its investment balance.

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 Police and Crime Commissioner’s treasury management strategy for 2019/20.

2.2 UK Consumer Price Inflation (CPI) for October was up 2.4% year/year, slightly below the consensus forecast and broadly in line with the Bank of England’s November Inflation Report. The most recent labour market data for October 2018 showed the unemployment rate edged up slightly to 4.1% while the employment rate of 75.7% was the joint highest on record. The 3-month average annual growth rate for pay excluding bonuses was 3.3% as wages continue to rise steadily and provide some pull on general inflation. Adjusted for inflation, real wages grew by 1.0%, a level still likely to have little effect on consumer spending.

2.3 The rise in quarterly GDP growth to 0.6% in Q3 from 0.4% in the previous quarter was due to weather-related factors boosting overall household consumption and construction activity over the summer following the weather-related weakness in Q1. At 1.5%, annual GDP growth continues to remain below trend. Looking ahead, the BoE, in its November Inflation Report, expects GDP growth to average around 1.75% over the forecast horizon, providing the UK's exit from the EU is relatively smooth.

2.4 Following the Bank of England's decision to increase Bank Rate to 0.75% in August, no changes to monetary policy has been made since. However, the Bank expects that should the economy continue to evolve in line with its November forecast, further increases in Bank Rate will be required to return inflation to the 2% target. The Monetary Policy Committee continues to reiterate that any further increases will be at a gradual pace and limited in extent.

2.5 While US growth has slowed over 2018, the economy continues to perform robustly. The US Federal Reserve continued its tightening bias throughout 2018, pushing rates to the current 2%-2.25% in September. Markets continue to expect one more rate rise in December, but expectations are fading that the further hikes previously expected in 2019 will materialise as concerns over trade wars drag on economic activity.

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

2.7 The Bank of England released its latest report on bank stress testing, illustrating that all entities included in the analysis were deemed to have passed the test once the levels of capital and potential mitigating actions presumed to be taken by management were factored in. The BoE did not require any bank to raise additional capital.

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

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

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

2.11 Gilt yields and hence long-term borrowing rates have remained at low levels but some upward movement from current levels is expected based on Arlingclose's interest rate projections, due to the strength of the US economy and the ECB's forward guidance on higher rates. 10-year and 20-year gilt yields are forecast to remain around 1.7% and 2.2% respectively over the interest rate forecast horizon, however volatility arising from both economic and political events are likely to continue to offer borrowing opportunities.

2.12 A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix C.1.

3. Local Context

3.1 On 31 March 2019, the Police and Crime Commissioner is expected to hold £16.7m of borrowing and £15m of investments. This is set out in further detail at ***Appendix C.2***. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

Table 1: Balance sheet summary and forecast

	31.3.18 Actual £m	31.3.19 Estimate £m	31.3.20 Forecast £m	31.3.21 Forecast £m	31.3.22 Forecast £m	31.3.23 Forecast £m	31.3.24 Forecast £m	31.3.25 Forecast £m
General Fund CFR	27.2	31.1	29.8	31.5	35.0	36.1	37.4	35.7
Less: Other debt liabilities *	(11.3)	(10.6)	(9.9)	(9.1)	(8.2)	(7.3)	(6.2)	(5.1)
Loans CFR	**15.9**	**20.5**	**19.9**	**22.4**	**26.8**	**28.8**	**31.2**	**30.6**
Less: External borrowing (long term)**	(1.3)	(0.7)	0.0	0.0	0.0	0.0	0.0	0.0
Less: External borrowing (short term)**	(10.0)	(16.0)	0.0	0.0	0.0	0.0	0.0	0.0
Internal borrowing	**4.6**	**3.8**	**19.9**	**22.4**	**26.8**	**28.8**	**31.2**	**30.6**
Less: Usable reserves	(25.3)	(20.4)	(18.8)	(17.9)	(17.3)	(17.1)	(15.7)	(15.1)
Less: Working capital	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
New borrowing / (Investments)	**(20.5)**	**(16.4)**	**1.3**	**4.7**	**9.7**	**11.9**	**15.7**	**15.7**

* finance leases, PFI liabilities and transferred debt that form part of the Police and Crime Commissioner's total debt

** shows only loans to which the Police and Crime Commissioner is committed and excludes optional refinancing

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. The Police and Crime Commissioner's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

3.3 The Police and Crime Commissioner has an increasing CFR due to the capital programme, and to keep liquidity at the targeted £10m, borrowing of up to £25.7m will be required over the forecast period. This is currently achieved through short term borrowing. The decision to borrow on a longer term basis is being reviewed with the treasury management consultants.

3.4 CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Police and Crime Commissioner's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Police and Crime Commissioner expects to comply with this recommendation during 2019/20.

3.5 **Liability benchmark:** To compare the Police and Crime Commissioner's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table 1 above, but that cash and investment balances are kept to a minimum level of £10m at each year-end to maintain sufficient liquidity but minimise credit risk.

Table 2: Liability benchmark

	31.3.18 Actual £m	31.3.19 Estimate £m	31.3.20 Forecast £m	31.3.21 Forecast £m	31.3.22 Forecast £m	31.3.22 Forecast £m	31.3.22 Forecast £m	31.3.22 Forecast £m
Loans CFR	15.9	**20.5**	**19.9**	**22.4**	**26.8**	**28.8**	**31.2**	**30.6**
Less: Usable reserves	(25.3)	(20.4)	(18.8)	(17.9)	(17.3)	(17.1)	(15.7)	(15.1)
Plus: Working capital	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Plus: Minimum investments	0.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0
Liability Benchmark	**9.8**	**10.3**	**11.3**	**14.7**	**19.7**	**21.9**	**25.7**	**25.7**

3.6 Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the Police and Crime Commissioner expects to comply with this in the medium term, but this will need to be part of the assessment when new borrowing is taken on.

3.7 **Borrowing strategy:** The Police and Crime Commissioner's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Police and Crime Commissioner therefore seeks to strike a balance between cheap short-term loans (currently available at around 0.95%) and long-term fixed rate loans where the future cost is known but higher (currently 2.0 to 3.0%).

3.8 The Borrowing Strategy is also balanced by the use of revenue cash available (reducing investments) being used rather than borrowing, known as internal borrowing. Internal borrowing has been used extensively over recent years saving around £0.250m in interest charges per year and reducing risk by not investing cash. However, use of reserves to fund Capital has reduced the available amounts to internally borrow. A second issue is that the Police and Crime Commissioner's income is not constant during the year; this is due to a Pension Grant of around £20m being paid in one lump sum each July. This has resulted in short term borrowing being required for 6 to 8 months of the year and a no additional borrowing required for the remaining months. At some point longer term borrowing will need to be secured, this is being monitored and discussed with our Treasury Management consultants on a regular basis.

3.9 **Objectives:** The Police and Crime Commissioner'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 Police and Crime Commissioner's long-term plans change is a secondary objective.

3.10 **Strategy:** Given the significant cuts to public expenditure and in particular to local government funding, the Police and Crime Commissioner's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

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

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

3.13 In addition, the Police and Crime Commissioner may borrow further short-term loans to cover unplanned cash flow shortages.

3.14 Projected levels of the Police and Crime Commissioner's total outstanding debt (which comprises borrowing and PFI liabilities) are shown below, compared with the capital financing requirement (see above). These are based on the current position to inform future decisions, which is the timing of longer term borrowing.

Table 3: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions

	31.3.18 actual	**31.3.19 forecast**	**31.3.20 forecast**	**31.3.21 forecast**	**31.3.22 forecast**	**31.3.23 forecast**	**31.3.24 forecast**	**31.3.25 forecast**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
PFI	**11.4**	**10.7**	**9.9**	**9.1**	**8.2**	**7.3**	**6.2**	**5.1**
Long Term Loans	**1.4**	**0.7**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Short Term loans	**10.0**	**16.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Debt (incl. PFI & leases)	**22.7**	**27.3**	**9.9**	**9.1**	**8.2**	**7.3**	**6.2**	**5.1**
Capital Financing Requirement	**27.2**	**31.0**	**29.8**	**31.5**	**35.0**	**36.1**	**37.4**	**35.7**

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

- Internal
- UK Debt Management Office (previously PWLB) and any successor body
- UK Local authorities and bodies defined to be local authorities
- Social housing and registered social landlords, formerly known as housing associations as regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department for Communities (in Northern Ireland)
- Other UK Government Agencies
- Universities
- UK public and private sector pension funds (except Gwynedd Pension Fund)
- Commercial banks and building societies authorised to operate in the UK and included on the lending list
- European Investment Bank
- Capital markets (stock issues, commercial paper and bills)
- Structured finance

3.16 **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

3.17 The Police and Crime Commissioner has previously raised all of its long-term borrowing from the UK Debt Management Office but it continues to investigate other sources of finance, such as local Authority loans and bank loans, that may be available at more favourable rates.

3.18 **Short-term and variable rate loans**: These loans leave the Police and Crime Commissioner exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below.

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

4. Investment Strategy

4.1 The Police and Crime Commissioner holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Police and Crime Commissioner's investment balance has ranged between £28 and £10 million, and similar levels are expected to be maintained in the forthcoming year.

4.2 **Objectives:** Both the CIPFA Code and the WG Guidance require the Police and Crime Commissioner 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 Police and Crime Commissioner'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 Police and Crime Commissioner will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

4.3 **Negative interest rates:** If the UK enters into a recession in 2019/20, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term 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.

4.4 **Strategy:** Although there the increasing risk and very low returns from short-term unsecured bank investments, the Police and Crime Commissioner aims to continue to invest in short term bank investments during 2019/20. This in concurrence with the internal borrowing strategy, minimising the amounts invested (and associated risk) and maximising yield (by reducing interest payments).

4.5 **Business models:** Under the new IFRS 9 standard, the accounting for certain investments depends on the Police and Crime Commissioner's "business model" for managing them. The Police and Crime Commissioner aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

4.6 **Approved counterparties:** The Police and Crime Commissioner may invest its surplus funds with any of the counterparty types in table 3 below, subject to the cash limits (per counterparty) and the time limits shown. The minimum credit investment was been raised from BBB+ to A- in 2018/19.

Table 4: Approved investment counterparties and limits

Credit Rating	Banks Unsecured	Banks Secured	Government	Corporates
UK Govt	n/a	n/a	£ Unlimited	n/a
AAA	£4m	£7m	£7m	£7m
AA+	£4m	£7m	£7m	£7m
AA	£4m	£7m	£7m	£7m
AA-	£4m	£7m	£7m	£7m
A+	£4m	£7m	£7m	£7m
A	£4m	£7m	£7m	£7m
A-	£4m	£7m	£7m	£7m
HSBC[1]	£10m	£10m	n/a	n/a
Unrated Local Authorities	n/a	n/a	£7m	n/a
Pooled Funds	£4m per fund			

1 These are the Commissioner's bankers and are currently rated AA- by the credit rating agencies and are currently the highest rated UK banking institution.

This table must be read in conjunction with the notes below

4.7 **Credit rating:** Investment limits are set by reference to the lowest published long-term credit rating from a selection of external rating agencies. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

4.8 **Banks unsecured:** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

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

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

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

4.12 **Pooled funds:** Shares or units in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. 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.

4.13 Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Police and Crime Commissioner 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 Police and Crime Commissioner's investment objectives will be monitored regularly.

4.14 **Operational bank account:** The Police and Crime Commissioner uses the HSBC as his operational bank account. HSBC rating is within the minimum credit rating set, in the event that the rating falls below the minimum rating HSBC will still be used as the operational bank account until alternative arrangements are made.

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

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

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

4.17 **Other information on the security of investments**: The Police and Crime Commissioner 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 Police and Crime Commissioner'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.

4.18 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 Police and Crime Commissioner 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 Police and Crime Commissioner's cash balances, then the surplus will be deposited with the UK Government via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

4.19 **Investment limits**: The Police and Crime Commissioner's revenue reserves available to cover investment losses are forecast to be £20m million on 31 March 2019. In order to manage this risk limits have been set as per table 3. A group of banks under the same ownership will be treated as a single organisation for limit purposes.

4.20 **Liquidity management**: The Police and Crime Commissioner uses purpose-built cash flow forecasting model 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 Police and Crime Commissioner being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Police and Crime Commissioner's medium-term financial plan and cash flow forecast.

5 Treasury Management Indicators

5.1 The Police and Crime Commissioner measures and manages its exposures to treasury management risks using the following indicators.

5.2 **Security:** The Police and Crime Commissioner has set a minimum credit rating of A- for investments.

Credit risk indicator	Target
Minimum credit rating for investment	A-

5.3 **Liquidity:** The Police and Crime Commissioner has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling twelve month period, without additional borrowing.

Liquidity risk indicator	Target
Total cash available within 12 months	£10m

5.4 **Interest rate exposures**: This indicator is set to control the Police and Crime Commissioner's exposure to interest rate risk. The upper limit for variable rate exposure has been set to ensure that there is no exposure to interest rate rises which could adversely impact on the revenue budget. The limit allows for the use of variable rate debt to offset exposure to changes in short-term rates on investments

	2018-19 %	2019-20 %	2020-21 %	2021-22 %	2022-23 %	2023-24 %
Upper Limit for Fixed Interest Rate Exposure	100	100	100	100	100	100
Upper Limit for Variable Interest Rate Exposure	50	50	50	50	50	50

5.5 **Maturity structure of borrowing:** This indicator is set to control the Police and Crime Commissioner's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within 5 years	100%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

5.6 **Principal sums invested for periods longer than a year:** The purpose of this indicator is to control the Police and Crime Commissioner'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	2019/20	2020/21	2021/22
Limit on principal invested beyond year end	£5m	£5m	£5m

6 Related Matters

6.1 The CIPFA Code requires the Police and Crime Commissioner to include the following in its treasury management strategy.

6.2 **Financial Derivatives:** In the absence of any explicit legal power to do so, the Police and Crime Commissioner 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.

6.3 **Markets in Financial Instruments Directive**: The Police and Crime Commissioner 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.

6.4 **Government Guidance:** Further matters required by the WG Guidance are included in Appendix C.3

7 **Financial Implications**

7.1 The budget for investment income in 2019/20 is £0.1m million, based on an average investment portfolio of £10 million at an interest rate of 1%. The budget for debt interest paid in 2019/20 is £0.6 million, based on an average debt portfolio of approximately £17m million at an average interest rate of 3.8%. If actual levels of investments and borrowing, or actual interest rates, differ from those forecast, performance against budget will be correspondingly different. As a strategy of internal borrowing is being followed the actual interest payments are projected to be significantly lower than the budget, the balance available will be used to finance capital expenditure directly thus reducing future borrowing requirements.

8 **Other Options Considered**

8.1 The WG Guidance and the CIPFA Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. The strategy was discussed with the Joint Audit Committee on 21 March 2019. 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
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

Appendix C.1

Arlingclose Economic & Interest Rate Forecast December 2018

Underlying assumptions:

- Our central interest rate forecasts are predicated on there being a transitionary period following the UK's official exit from the EU.

- The MPC has a bias towards tighter monetary policy but is reluctant to push interest rate expectations too strongly. We believe that MPC members consider that: 1) tight labour markets will prompt inflationary pressure in the future, 2) ultra-low interest rates result in other economic problems, and 3) higher Bank Rate will be a more effective policy weapon if downside risks to growth crystallise.

- Both our projected outlook and the increase in the magnitude of political and economic risks facing the UK economy means we maintain the significant downside risks to our forecasts, despite the potential for slightly stronger growth next year as business investment rebounds should the EU Withdrawal Agreement be approved. The potential for severe economic outcomes has increased following the poor reception of the Withdrawal Agreement by MPs. We expect the Bank of England to hold at or reduce interest rates from current levels if Brexit risks materialise.

- The UK economic environment is relatively soft, despite seemingly strong labour market data. GDP growth recovered somewhat in the middle quarters of 2018, but more recent data suggests the economy slowed markedly in Q4. Our view is that the UK economy still faces a challenging outlook as the country exits the European Union and Eurozone economic growth softens.

- Cost pressures are easing but inflation is forecast to remain above the Bank's 2% target through most of the forecast period. Lower oil prices have reduced inflationary pressure, but the tight labour market and decline in the value of sterling means inflation may remain above target for longer than expected.

- Global economic growth is slowing. Despite slower growth, the European Central Bank is conditioning markets for the end of QE, the timing of the first rate hike (2019) and their path thereafter. More recent US data has placed pressure on the Federal Reserve to reduce the pace of monetary tightening – previous hikes and heightened expectations will, however, slow economic growth.

- Central bank actions and geopolitical risks have and will continue to produce significant volatility in financial markets, including bond markets.

Forecast:

- The MPC has maintained expectations of a slow rise in interest rates over the forecast horizon, but recent events around Brexit have dampened interest rate expectations. Our central case is for Bank Rate to rise twice in 2019, after the UK exits the EU. The risks are weighted to the downside.

- Gilt yields have remained at low levels. We expect some upward movement from current levels based on our central case that the UK will enter a transitionary period following its EU exit in March 2019. However, our projected weak economic outlook and volatility arising from both economic and political events will continue to offer borrowing opportunities.

	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Average
Official Bank Rate														
Upside risk	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.17**
Arlingclose Central Case	**0.75**	**0.75**	**1.00**	**1.00**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.25**	**1.13**
Downside risk	0.00	-0.50	-0.75	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	**-0.85**
3-mth money market rate														
Upside risk	0.10	0.10	0.10	0.10	0.15	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	**0.17**
Arlingclose Central Case	**0.90**	**0.95**	**1.10**	**1.30**	**1.40**	**1.40**	**1.40**	**1.35**	**1.35**	**1.35**	**1.35**	**1.35**	**1.35**	**1.27**
Downside risk	-0.20	-0.45	-0.60	-0.80	-0.90	-0.90	-0.90	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	**-0.76**
1-yr money market rate														
Upside risk	0.20	0.30	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	**0.33**
Arlingclose Central Case	**1.15**	**1.25**	**1.35**	**1.50**	**1.70**	**1.60**	**1.50**	**1.40**	**1.35**	**1.35**	**1.35**	**1.35**	**1.35**	**1.40**
Downside risk	-0.35	-0.50	-0.60	-0.80	-0.90	-0.90	-0.90	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	**-0.77**
5-yr gilt yield														
Upside risk	0.25	0.30	0.30	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.37**
Arlingclose Central Case	**1.15**	**1.25**	**1.35**	**1.50**	**1.50**	**1.40**	**1.35**	**1.35**	**1.30**	**1.30**	**1.30**	**1.30**	**1.30**	**1.33**
Downside risk	-0.50	-0.60	-0.65	-0.80	-0.80	-0.70	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	**-0.66**
10-yr gilt yield														
Upside risk	0.25	0.30	0.30	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.37**
Arlingclose Central Case	**1.50**	**1.65**	**1.70**	**1.80**	**1.80**	**1.75**	**1.75**	**1.70**	**1.70**	**1.70**	**1.70**	**1.70**	**1.70**	**1.70**
Downside risk	-0.55	-0.70	-0.70	-0.80	-0.80	-0.75	-0.75	-0.70	-0.70	-0.70	-0.70	-0.70	-0.70	**-0.71**
20-yr gilt yield														
Upside risk	0.25	0.30	0.30	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.37**
Arlingclose Central Case	**2.00**	**2.10**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.20**	**2.18**
Downside risk	-0.60	-0.70	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	**-0.73**
50-yr gilt yield														
Upside risk	0.25	0.30	0.30	0.35	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.37**
Arlingclose Central Case	**1.90**	**1.95**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**2.00**	**1.99**
Downside risk	-0.60	-0.70	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	**-0.73**

PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%
PWLB Infrastructure Rate (Maturity Loans) = Gilt yield + 0.60%

Appendix C.2

Existing Investment & Debt Portfolio Position

	31/03/19 **Actual Portfolio (with estimated movements up to the end of year and subject to end of year checks)** **£m**
External Borrowing:	
Fixed Rate – Debt Office	0.655
Fixed Rate – Local Government	16.000
Total External Borrowing	16.655
Other Long Term Liabilities:	
- PFI	10.660
- Finance Leases	0.00
Total Gross External Debt	27.315
Investments:	
Managed in-house	
- Short-term monies (Deposits/ monies on call /MMFs)	-15.040
- Long-term investments	0.00
Managed externally	
- By Fund Managers - Pooled Funds *(please list)*	0.00
Total Investments	-15.040
Net Debt	12.275

Appendix C.3

Additional requirements of Welsh Government Guidance

Specified investments: The WG Guidance defines specified investments as those:

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

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

Non-specified investments: Any investment not meeting the definition of a specified investment is classed as non-specified. The Police and Crime Commissioner does not intend to make any investments denominated in foreign currencies nor any defined as capital expenditure. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement and limited to no more than £5m.

Investment training: The needs of the Police and Crime Commissioner's treasury management staff for training in investment management are assessed on a regular basis and additionally when the responsibilities of individual members of staff change.

Staff regularly attend training courses, seminars and conferences provided by Arlingclose and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA, the Association of Corporate Treasurers and other appropriate organisations.

Investment advisers: The Police and Crime Commissioner has appointed Arlingclose Limited as treasury management advisers and receives specific advice on investment, debt and capital finance issues. The quality of this service is controlled by regular strategy meetings, review of data provided and professional judgement.

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

The total amount borrowed will not exceed the authorised borrowing limit of £35m million. The maximum period between borrowing and expenditure is expected to be two years, although the Police and Crime Commissioner is not required to link particular loans with particular items of expenditure.