

# **Treasury Management Strategy Statement**

Annual Investment Strategy

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2023/24

## **1. INTRODUCTION**

### **1.1 Background**

Transport for the North is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low-risk counterparties or instruments commensurate with Transport for the North's low risk appetite, providing adequate liquidity initially before considering investment return.

The contribution the treasury management function makes to Transport for the North is critical to ensure liquidity and the ability to meet spending commitments as they fall due. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to Transport for the North.

CIPFA defines treasury management as:

*"The management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."*

Transport for the North does not engage in any commercial investments and has no non-treasury investments.

### **1.2 Reporting Requirements**

#### **1.2.1 Capital Strategy**

A capital strategy report is designed to show how local authorities will finance and fund long-term investment plans. They are designed to evidence that investment plans are both affordable in the short-term and sustainable in the long-term.

Transport for the North has no powers to enter into credit liabilities, so cannot borrow to finance investment. Transport for the North also owns no assets which could be disposed of to generate capital receipts. Finally, Transport for the North has no revenue raising powers, which could be used to raise cash for capital investment.

Instead, Transport for the North is an entirely grant funded organisation. All capital investments are grant funded, with no additional financing or funding issues.

Transport for the North's capital expenditure profiles are outlined later in this appendix.

#### **1.2.2 Treasury Management Reporting**

Transport for the North Board is currently required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals.

- a. **Prudential and treasury indicators and treasury strategy** (this report) - The first, and most important report is forward looking and

covers the aspects relevant to Transport for the North – notably management of cash and investments:

- any capital plans, (including prudential indicators)
  - the treasury management strategy, (how the investments are to be organised), including treasury indicators
  - an investment strategy, (the parameters on how investments are to be managed)
- b. **A mid-year treasury management report** – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision
- c. **An annual treasury report** – This is a backward-looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

### 1.2.3 Scrutiny

The following bodies within TfN’s governance receive Treasury Management Reporting:

- The Audit & Governance Committee
- The TfN Board

## 1.3 Treasury Management Strategy for 2023/24

The strategy for 2023/24 covers two main areas:

### Capital issues

- any capital expenditure plans and the associated prudential indicators.

### Treasury management issues

- the current treasury position
- treasury indicators which limit the treasury risk and activities of Transport for the North
- prospects for interest rates
- the investment strategy
- creditworthiness policy
- the policy on use of external service providers

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the CIPFA Treasury Management Code and MHCLG Investment Guidance.

## 1.4 Training

The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. Transport for the North will review training requirements for members in the new financial year.

The training needs of finance officers involved in treasury management are periodically reviewed.

### **1.5 Treasury management consultants**

Transport for the North uses Link Treasury Services, Treasury solutions as its external treasury management advisors, as required.

Transport for the North recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. Transport for the North will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

## **2 THE CAPITAL PRUDENTIAL INDICATORS 2023/24 – 2025/26**

Regulation requires Transport for the North to present its capital prudential indicators. This reflects that, for most authorities, capital expenditure plans are a key driver of treasury management activity. This is principally because those plans will be underpinned by financing strategies that use debt or cash balances to finance activity.

Transport for the North's statutory position means that it is not able to raise credit, and its funding environment means that it is unlikely to generate significant long-term cash surpluses. Instead, Transport for the North's capital investment plans will be funded from grant awards.

These factors mean the capital prudential indicators are largely insignificant, though they do reflect the parameters in which Transport for the North operates.

### **2.1 Capital expenditure**

There are currently no plans to incur any capital expenditure in 2023/24 or following years. This could change should Transport for the North receive grant funding to invest in capital assets. Any such change would be reported in accordance with the arrangements detailed above.

### **2.2 Core funds and expected investment balances**

Transport for the North's cash balances are largely determined by its reserve strategy and working capital fluctuations. Transport for the North is funded on a needs basis, so only draws upon grant it requires to meet its expenditure plans. It does, however, hold cash in reserve to guard against financial shock. TfN will invest its cash balances in accordance with its investment policy.

### **2.3 Prospects for interest rates**

Although there is available a great deal of commentary about and forecasting of future interest rates, the market remains essentially uncertain. In general, it does appear likely that rates will continue to rise at least in the first half of 2023, but the size, timing and duration of such increases cannot be known.

### **Investment and borrowing rates**

- **Investment returns** are expected to improve in 2023/24. Generally, we can expect longer deposits to generate higher returns, but in a rising market it is appropriate to limit the length of the deposit as higher rates of return may have emerged by the maturity date.

### 3 ANNUAL INVESTMENT STRATEGY

#### 3.1 Investment policy – management of risk

Transport for the North's investment policy has regard to the following: -

- DLUHC's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the Code")
- CIPFA Treasury Management Guidance Notes 2018

Transport for the North's investment priorities will be security first, portfolio liquidity second and then yield, (return).

The above guidance from the MHCLG and CIPFA place a high priority on the management of risk. Transport for the North has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

1. Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.
2. **Other information:** ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration Transport for the North will engage with its advisors to maintain a monitor on market pricing such as "**credit default swaps**" and overlay that information on top of the credit ratings.
3. **Other information sources** used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.
4. Transport for the North has defined the list of **types of investment instruments** that the treasury management team are authorised to use.
  - a. **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year.
  - b. **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use. Transport for the North will not use these investment categories.
5. **Non-specified investments limit.** Transport for the North has determined that it will not invest in any non-specified investment categories.
6. **Lending limits**, (amounts and maturity), for each counterparty will be set through applying the matrix table in paragraph 3.3.

7. **Transaction limits** are set for each type of investment in paragraph 3.3.
8. Transport for the North will set a limit for the amount of its investments which are invested for **longer than 365 days**, (see paragraph 3.5).
9. Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating**, (see paragraph 3.4).
10. Transport for the North has engaged **external consultants**, (see paragraph 1.5), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of Transport for the North in the context of the expected level of cash balances and need for liquidity throughout the year.
11. All investments will be denominated in **sterling**.
12. As a result of the change in accounting standards for 2022/23 under **IFRS 9**, Transport for the North will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the Ministry of Housing, Communities and Local Government, [MHCLG], concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years commencing from 1.4.18.)

However, Transport for the North will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance, (see paragraph 3.5). Regular monitoring of investment performance will be carried out during the year.

### **3.2 Changes in risk management policy from last year.**

The above criteria are unchanged from last year

Transport for the North continues to engage treasury management advisors to shape its investment strategy. It currently uses Link Treasury Services creditworthiness service to choose investment counterparties.

### **3.3 Creditworthiness policy**

Transport for the North applies the creditworthiness service provided by Link Treasury Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard & Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies
- CDS spreads to give early warning of likely changes in credit ratings

- sovereign ratings to select counterparties from only the most creditworthy countries

This modelling approach combines credit ratings, credit Watches and credit Outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by Transport for the North to determine the suggested duration for investments.

This approach is then tempered by Transport for the North's funding environment, and in particular its funding relationship with the Department for Transport. This environment sees Transport for the North directly funded every quarter for activity, and thus negates the need for, and the possibility of, running up significant cash balances over a long duration.

Transport for the North will therefore use counterparties within the following durational bands:

- Yellow 3 months
- Dark pink 3 months
- Light pink 3 months
- Purple 3 months
- Blue 3 months
- Orange 3 months
- Red 3 months
- Green 1 month
- No colour not to be used

The Link Treasury Services creditworthiness service uses a wider array of information other than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

Before consideration of underlying sovereign rating, typically the minimum credit ratings criteria Transport for the North use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances, consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored weekly. Transport for the North is alerted to changes to ratings of all three agencies through its use of the Link Treasury Services' creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting Transport for the North's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings Transport for the North will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Treasury Services. Extreme

market movements may result in downgrade of an institution or removal from Transport for the North's lending list.

Sole reliance will not be placed on the use of this external service. In addition Transport for the North will also use market data and market information, information on any external support for banks to help support its decision making process.

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour

<i>See Appendix 4.7 for an indicative counterparty list</i>	Colour (and long term rating where applicable)	Money and/or % Limit	Transaction limit	Time Limit
<b>Banks *</b>	<b>yellow</b>	<b>100%</b>	<b>£5m</b>	<b>3 months</b>
<b>Banks</b>	<b>purple</b>	<b>100%</b>	<b>£5m</b>	<b>3 months</b>
<b>Banks</b>	<b>orange</b>	<b>100%</b>	<b>£5m</b>	<b>3 months</b>
<b>Banks – part nationalised</b>	<b>blue</b>	<b>100%</b>	<b>£5m</b>	<b>3 months</b>
<b>Banks</b>	<b>red</b>	<b>100%</b>	<b>£5m</b>	<b>3 months</b>
<b>Banks</b>	<b>green</b>	<b>100%</b>	<b>£5m</b>	<b>1 month</b>
<b>Banks</b>	<b>No colour</b>	<b>Not to be used</b>	<b>£0m</b>	<b>-</b>
<b>Limit 3 category – TfN's banker^</b>	<b>n/a</b>	<b>100%</b>	<b>n/a</b>	<b>3 days</b>
<b>DMADF</b>	<b>UK sovereign rating</b>	<b>unlimited</b>	<b>n/a</b>	<b>3 months</b>
<b>Local authorities</b>	<b>n/a</b>	<b>100%</b>	<b>£5m</b>	<b>3 months</b>
	<b>Fund rating</b>	<b>Money and/or % Limit</b>		<b>Time Limit</b>
<b>Money Market Funds CNAV</b>	<b>AAA</b>	<b>100%</b>	<b>£5m</b>	<b>liquid</b>
<b>Money Market Funds LVNAV</b>	<b>AAA</b>	<b>100%</b>	<b>£5bm</b>	<b>liquid</b>

\* Please note: the yellow colour category is for UK Government debt, or its equivalent, money market funds and collateralised deposits where the collateral is UK Government debt

*^ Transport for the North retains the ability to directly invest its cash surpluses with its own bank above the defined transaction limit where necessary. This includes managing unexpected cash flows, dealing with urgent matters, or where other options are not available to.*

### **3.4 Country limits**

Due care will be taken to consider the exposure of Transport for the North's total investment portfolio to non-specified investments, countries, groups and sectors.

- a. **Non-specified investment limit.** Transport for the North has determined that it will not use non-specified investment products.
- b. **Country limit.** Transport for the North has determined that it will only use approved counterparties from the UK and from countries with a **minimum sovereign credit rating of AA-** from Fitch, at the time that the investment decision is made.

### **3.5 Investment strategy**

#### **Investment Durations**

Transport for the North's approach to investments is influenced by its funding environment. Transport for the North has no revenue raising powers, nor ability to raise credit. This limits its ability to raise surplus cash unilaterally, and also obviates the need for retaining significant amounts of cash to pay down debt obligations.

Transport for the North is funded on a needs basis from the Department for Transport, receiving periodical grants to meet its cash requirements. This funding arrangement is supplemented by a reserve strategy that enables Transport for the North to retain cash balances from its flexible Core Grant to mitigate against financial shock.

These arrangements mean that it is unlikely Transport for the North will have significant amounts of surplus cash that does not have a short-term call upon it. This in turn engenders a short-term view on investments, with the primacy of consideration being on security and liquidity.

Transport for the North considers that it will not invest for time-periods beyond 3 months.

#### **Investment treasury indicator and limit**

There is a regulatory requirement to set and publish a limit upon total principal funds invested for greater than 365 days. These limits are set with regard to Transport for the North's liquidity requirements and to reduce the need for early sale of an investment and are based on the availability of funds after each year-end. Transport for the North's funding environment is such that it will limit itself to investments of periods not greater than 3 months.

Therefore, the limit is set to ZERO for 2023/24, 2024/25 and 2025/26.

### **3.6 Investment risk benchmarking**

These benchmarks are simple guides to maximum risk, so they may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that officers will monitor the current and trend position and amend the operational strategy to manage

risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the mid-year or Annual Report.

Security – Transport for the North has opted for a particularly prudent approach to security

Liquidity – in respect of this area Transport for the North seeks to maintain:

- Liquid short-term deposits of at least £1m available with a day's notice in its own bank.
- Weighted average life benchmark is expected to be no greater than 3 months.

Yield - local measures of yield benchmarks are:

- Investments – internal returns above the 7-day LIBID rate

### **3.7 End of year investment report**

At the end of the financial year, Transport for the North will report on its investment activity as part of its Annual Treasury Report.

#### **4 APPENDICES**

1. Prudential and treasury indicators and MRP statement
2. Treasury management practice 1 – credit and counterparty risk management (option 1)
3. Treasury management scheme of delegation
4. The treasury management role of the section 151 officer
5. Indicative counterparty list

## **4.1 THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2023/24 – 2025/26**

Transport for the North's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

### **4.1.1 Capital expenditure**

ZERO for all three years.

### **4.1.2 Affordability prudential indicators**

#### **Ratio of financing costs to net revenue stream**

ZERO for all three years.

## 4.2 TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT OPTION 1

**SPECIFIED INVESTMENTS:** All such investments will be sterling denominated, with **maturities up to maximum of 3 months**, meeting the minimum 'high' quality criteria where applicable.

**NON-SPECIFIED INVESTMENTS:** These are any investments which do not meet the specified investment criteria. Transport for the North will not use investment classes that fall under this category.

	<b>Minimum credit criteria / colour band</b>	<b>Max % of total investments/</b>	<b>Max. maturity period</b>
<b>DMADF – UK Government</b>	UK sovereign rating	<b>100%</b>	<b>3 months</b>
UK Government gilts	UK sovereign rating	100%	3 months
UK Government Treasury bills	UK sovereign rating	100%	3 months
Bonds issued by multilateral development banks	AAA (or state your criteria if different)	100%	3 months
Money Market Funds CNAV	AAA	100%	Liquid
Money Market Funds LNAV	AAA	100%	Liquid
Local authorities	N/A	100%	3 months
Term deposits with banks and building societies	Blue Orange Red Green No Colour		3 months 3 months 3 months 1 month Not for use

**Accounting treatment of investments.** The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by Transport for the North. To ensure that Transport for the North is protected from any adverse revenue impact, which may arise from these

differences, we will review the accounting implications of new transactions before they are undertaken.

### **4.3 TREASURY MANAGEMENT SCHEME OF DELEGATION**

#### **(i) Transport for the North Board**

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.
- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
- budget consideration and approval;
- approval of the division of responsibilities;
- receiving and reviewing regular monitoring reports and acting on recommendations;

#### **(ii) Scrutiny Committee**

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

#### **(iii) Audit and Governance Committee**

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

#### **4.4 THE TREASURY MANAGEMENT ROLE OF THE SECTION 151 OFFICER**

##### **The S151 (responsible) officer (Transport for the North Finance Director)**

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers.

