PART 1 – OPEN TO THE PUBLIC	

REPORT OF THE LEAD MEMBER FOR FINANCE AND SUPPORT SERVICES

OVERVIEW AND SCRUTINY BOARD, 3 NOVEMBER 2021
COUNCIL, 17 NOVEMBER 2021

TITLE: TREASURY MANAGEMENT STRATEGY MID YEAR REVIEW 2021/22

RECOMMENDATIONS:
It is recommended that Members note the contents of the report and approve the update to the prudential indicators.

EXECUTIVE SUMMARY:
This report provides a progress report on the treasury management strategy for 2021/22 and updates the prudential indicators. Members are requested to approve the update to the prudential indicators

BACKGROUND DOCUMENTS:
Various working papers in the Finance division including:

- Treasury management strategy 2021/22 reported to council on 24 February 2021
- Treasury management practices TMPs 1 to 12 and supporting schedules
- Treasury management in the public services, code of practice and cross-sectoral guidance notes (CIPFA), “CIPFA Code”
- Treasury management in the public services, guidance notes for local authorities including police authorities and fire authorities (CIPFA), “CIPFA guidance”

KEY DECISION: ~~YES /~~ NO

DETAILS: overleaf

1. BACKGROUND

1.1 The Council operates a balanced budget which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operation ensures this cash flow is adequately planned with surplus monies being invested in low-risk counterparties, providing adequate liquidity initially before considering optimising investment return.

1.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially longer-term cash flow planning to ensure the Council can meet its capital spending schedule. This management of longer-term cash may involve arranging long or short-term loans or using longer term cash flow surpluses and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

1.3 Treasury management is defined as:

> "The management of the local authority's 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."

2. INTRODUCTION

2.1 This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2017).

The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

- Creation and maintenance of Treasury Management Practices which set out the way the Council will seek to achieve those policies and objectives.

- Receipt by the full council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report, (stewardship report), covering activities during the previous year.

- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to the Overview and scrutiny board.

2.2 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the first part of the 2021/22 financial year;

- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;

- The Council's capital expenditure, as set out in the budget report, and prudential indicators;

- A review of the Council's investment portfolio for 2021/22;

- A review of the Council's borrowing strategy for 2021/22;

- A review of compliance with Treasury and Prudential Limits for 2021/22.

3. ECONOMIC UPDATE

3.1 At its latest meeting, ending on 22 September 2021, the Bank of England Monetary Policy Committee voted to maintain the Bank Rate at 0.1%. There were no changes to the programme of quantitative easing, although there were concerns that this would add to inflationary pressures.

3.2 From the MPC September meeting, there were indications that interest rates could rise. Potential labour shortages could push up wage growth which, along with increased energy prices, would lead to increased levels of inflation with CPI rates peaking at 4% during 2021.

4. INTEREST RATE FORECAST

Table 1 Link Asset Services interest rate forecast:

Link Group Interest Rate View	29.9.21									
	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.75
3 month ave earnings	0.10	0.10	0.20	0.20	0.30	0.40	0.50	0.50	0.60	0.70
6 month ave earnings	0.20	0.20	0.30	0.30	0.40	0.50	0.60	0.60	0.70	0.80
12 month ave earnings	0.30	0.40	0.50	0.50	0.50	0.60	0.70	0.80	0.90	1.00
5 yr PWLB	1.40	1.40	1.50	1.50	1.60	1.60	1.60	1.70	1.70	1.70
10 yr PWLB	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10
25 yr PWLB	2.20	2.20	2.30	2.30	2.40	2.40	2.40	2.50	2.50	2.60
50 yr PWLB	2.00	2.00	2.10	2.20	2.20	2.20	2.20	2.30	2.30	2.40

4.1 Due to the coronavirus outbreak, the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, the level at which it remains and is expected to continue in the short term.

4.2 The forecast shows a small increase to 0.25% is expected in quarter 1 of 2022/23.

4.3 The latest forecast shows PWLB rates gradually rising.

5. TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY UPDATE

5.1 The Treasury Management Strategy Statement (TMSS) for 2021/22 was approved by the council on 24 February 2021. The council's Annual Investment Strategy, which is incorporated into the TMSS, outlines the council's investment priorities as *security of capital* and *liquidity*. The council also aims to achieve the optimum return (*yield*) in investments, commensurate with the proper levels of security and liquidity.

5.2 In the current economic climate, it is considered appropriate to keep a significant proportion of investments short term (less than 1 year) and only invest with high credit rated financial institutions or those guaranteed by the UK government, using Link Asset Services' suggested creditworthiness approach.

5.3 During the first half of 2021/22, investments with counterparties were within the £15m limit.

5.4 During the first half of 2021/22 the council had not taken out any long-term borrowing.

5.5 There are no policy changes to the TMSS; the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

6. THE COUNCIL'S CAPITAL POSITION (PRUDENTIAL INDICATORS)

Table 2 Prudential Indicator for Capital Expenditure £m for 2021/22

	Original estimate	Current position	Revised estimate
Capital expenditure	104.4	29.6	156.1

6.1 Table 2 shows the revised estimates for capital expenditure since the capital programme was agreed in February 2021. The main increase in forecast spend is due to schemes being reprofiled from the 2020/21 capital programme.

Table 3 Changes to the Financing of the Capital Programme 2021/22 £m

	Original estimate	Revised estimate
Grants	48.7	82.5
Borrowing requirement	55.8	73.6
Total	104.5	156.1

6.2 Table 3 shows the funding of the capital expenditure plans. The borrowing requirement increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision).

Table 4 Capital Financing Requirement (CFR) £m 2021/22

	Original estimate	Revised estimate
Capital financing requirement bfwd	703.8	673.0
Capital financing requirement	716.4	719.6
Annual change in CFR	12.6	46.6

6.3 The increase in the forecast annual change in the capital financing requirement is due to the revised estimate for capital expenditure that has consequently increased the borrowing requirement, as shown in tables 2 and 3.

Table 5 Debt forecast £m

	Original estimate	Current position	Revised estimate
Borrowing	440.6	332.8	369.0
Other long-term liabilities	165.8	168.1	165.5
Total debt (yearend position)	606.4	500.9	534.5

6.4 The reduction in the forecast debt position is due to a reduction in the level of temporary borrowing with the council not needing to renew temporary borrowing on its maturity.

6.5 Long term liabilities reduce as PFI schemes payments are made and as transferred debt (from the breakup of Greater Manchester Council) is repaid. By the end of the year a further 6 months of payments will have been made, this will reduce the balance nearer to the revised estimate.

6.6 A key control applied to treasury activity is a prudential indicator to ensure that, over the medium term, debt will only be for a capital purpose, so no borrowing to invest. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2021/22 and next two financial years. As the total debt at the end of the year is forecast to be £534.5m and the forecast CFR is £719.6m, this control has been complied with.

6.7 This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need if it is considered that this would be advantageous.

Table 6 Prudential Indicators Operational Boundary £m 2021/22

	Original estimate	Revised estimate
Borrowing	590.5	594.1
Other long-term liabilities	195.8	195.5
Total debt (yearend position)	786.3	789.6

6.8The Operational Boundary for External Debt is based on the probable external debt during the year. It is not a limit and actual borrowing could vary around this boundary for short times during the year. It acts as an early warning indicator to ensure the authorised limit is not breached. Similarly, to the authorised limit it also provides scope for the Council to borrow in advance of need. The prudential indicators have are similar to the original estimates.

6.9 The Chief Finance Officer reports that no difficulties are envisaged for the current or future years in complying with this prudential indicator.

6.10 A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which represents the limit beyond which borrowing is prohibited and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Authorised Limit is adjusted to reflect changes to the council's capital programme and the implementation of IFRS 16.

Table 7 Prudential indicator - authorised limit for external debt £m

	Original estimate	Current position	Revised estimate
Borrowing	610.5	332.8	614.1
Other long-term liabilities	225.8	195.5	225.5
Total debt (yearend position)	836.3	528.3	839.6

6.11 Appendix 2 details the prudential and treasury indicators for the next 4 years.

7. INVESTMENT PORTFOLIO 2021/22

7.1 In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. As shown by the forecasts in section 4, it is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low and in line with the current 0.10% Bank Rate.

7.2 The Council held £64.26m of investments as at 30 September 2021 (£36.25m at 31 March 2021) and the weighted average investment portfolio yield for the first 6 months of the year is 0.052% against current bank rate of 0.10%. The level of investments varies throughout the year

7.3 The Chief Finance Officer confirms that the approved limits within the Annual Investment Strategy were not exceeded during the first 6 months of 2021/22.

7.4 The Council's budgeted investment return for 2021/22 is £0.010m, and performance for the year to date is £0.007m. However, whilst reduced interest rates have affected the council's investment income, there has been a saving on the council's temporary borrowing budget with a budget for the year of £0.025m against costs of £0.015m for the year to date.

7.5 The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function. It provides sufficient creditworthy counterparties for the council's investments.

7.6 There has been no change in the council's risk appetite for investments.

8. BORROWING

8.1 The Council's capital financing requirement (CFR) for 2021/22 is forecast to be £719.6m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the PWLB or the market (external borrowing) or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. Table 5 shows the Council's current debt level of £332.8m and the yearend forecast of £369.0m.

8.2 The option to use long term borrowing to finance this expenditure to minimise the council's interest rate risk exposure will be kept under review. This will include an assessment of the different sources of funding available to the council.

Table 8 **Graph showing the movement in PWLB certainty rates since the start of the current financial year**

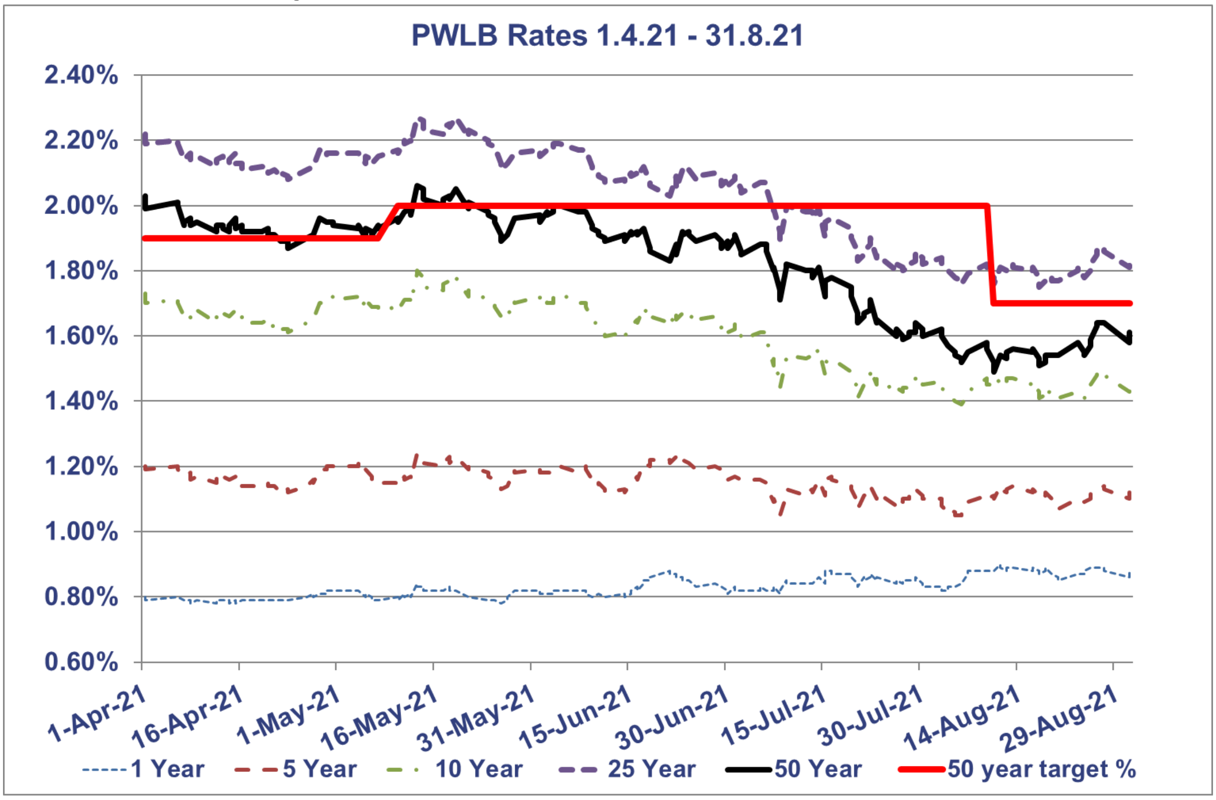

Table 9 **Table showing the movement in PWLB certainty rates since the start of the current financial year**

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	0.78%	1.05%	1.39%	1.75%	1.49%
Date	08/04/2021	08/07/2021	05/08/2021	17/08/2021	10/08/2021
High	0.90%	1.24%	1.80%	2.27%	2.06%
Date	11/08/2021	13/05/2021	13/05/2021	13/05/2021	13/05/2021
Average	0.83%	1.15%	1.59%	2.03%	1.82%

8.3 PWLB rates have mostly been on a falling trend since May apart from very short term rates which have been rising marginally.

8.4 No debt rescheduling has been undertaken to date in the current financial year.

9. OTHER

IFRS16 accounting standard

9.1 This accounting standard will come into effect from 1 April 2022 and be outlined in the 2021/22 financial accounts. It specifies the principles for recognition, measurement, presentation and disclosure of leases as a response to concerns about the lack of transparency in information. For any leases the council has entered or enters into as a lessee, the assets and liabilities arising with a term of more than 12 months are to be recognised in the financial statements unless they are of low value (less than £5k).

9.2 The impact on the council is likely to be the recognition of additional assets on the balance sheet leading to a significant increase in the CFR, due to the expected level of leases the council has entered into of this nature. The prudential indicators table in appendix 2 reflects an initial estimate based on information readily available. An exercise to review all the council's lease contracts is due to take place over the coming months.

Changes in risk appetite

9.3 The 2018 CIPFA Codes and guidance notes have placed enhanced importance on risk management. Where an authority changes its risk appetite e.g. for moving surplus cash into or out of certain types of investment funds or other types of investment instruments, this change in risk appetite and policy should be brought to members' attention in treasury management update reports. There has been no change in the council's risk appetite for investments.

10. CONCLUSION AND RECOMMENDATIONS

10.1 The council has not taken any new long term borrowing so far in this financial year. The option to use long term borrowing to finance capital expenditure to minimise the council's interest rate risk exposure will be kept under review. The council has also not taken any short-term borrowing so far in this financial year, although it will be considered when appropriate based upon a review of interest rates available in the market.

10.2 The council has remained within prudential limits in the review period.

10.3 Members are requested to approve the changes to the prudential indicators detailed in appendix 2.

KEY COUNCIL POLICIES: Treasury management strategy; budget strategy.

EQUALITY IMPACT ASSESSMENT AND IMPLICATIONS: Not applicable

ASSESSMENT OF RISK:

The monitoring and control of risk underpins all treasury management activities. The main risks are of adverse or unforeseen fluctuations in interest rates and security of capital sums.

LEGAL IMPLICATIONS Supplied by: Tony Hatton, Principal Solicitor

The Treasury Management Strategy sets out the Council's policies for managing its investments which includes giving priority to security and liquidity.

The Local Government Act 2003 (the Act) and supporting regulations requires the Council to 'have regard to' the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable. The Act therefore requires the Council to set out its Treasury Management Strategy at the start of each new financial year and to prepare an Annual Investment Strategy (as required by Investment Guidance subsequent to the Act); this sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

The Council is also required to "determine for the current financial year an amount of Minimum Revenue Provision (MRP) that it considers to be prudent." It is also required to submit a statement on the Council's policy for its annual MRP to the Council for approval before the start of the financial year to which the provision will relate.

The Treasury Management Strategy 2021/22 was set out in a report to Council and approved by them on the 24 February 2021. This complied with the relevant requirements of the Local Government Act 2003 and the CIPFA Treasury Management Code. This further report to Council provides a progress report on the Treasury Management Strategy for 2021/22.

FINANCIAL IMPLICATIONS Supplied by: May Sung, Finance Manager

This report has been prepared by the Finance division of the Service Reform service group. The costs of borrowing: minimum revenue provision, interest and debt management expenses, are borne by the corporate capital financing budget.

PROCUREMENT IMPLICATIONS provided by: Not applicable

HR IMPLICATIONS provided by: Not applicable

OTHER SERVICE GROUPS CONSULTED: Not applicable

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WARDS TO WHICH REPORT RELATES: None specifically.

APPENDIX 1
Glossary of Terms

Base rate – the rate at which the Bank of England offers loans to the wholesale banks, thereby controlling general interest rates in the economy.

Capital financing requirement – reflects the local authority underlying need to borrow for a capital purpose.

Consolidated rate of interest (CRI) – is the average rate of interest for external borrowing during the year.

Fixed rate funding - a fixed rate of interest throughout the time of the loan. The rate is fixed at the start of the loan and therefore does not affect the volatility of the portfolio, until the debt matures and requires replacing at the interest rates relevant at that time.

Gilts - The loan instruments by which the government borrows. Interest rates will reflect the level of interest shown by investors when the government auctions gilts.

LOBO – "Lender offer, borrower option", a financial instrument where the lender may choose to vary the interest rate at certain break points. Only if the lender chooses to vary the interest rate, the borrower has an option to terminate the arrangement at no penalty.

Market - The private sector financial institutions - banks, building societies etc.

Maturity profile - an illustration of when debts are due to mature, and either have to be renewed or money found to pay off the debt. A high concentration in one year will make the council vulnerable to current interest rates in that year.

Monetary Policy Committee (MPC) – the independent body which determines base rate.

PWLB - Public Works Loan Board. An institution managed by the government to provide loans to public bodies at rates which reflect the rates at which the government is able to sell gilts.

Variable rate funding - The rate of interest either continually moves reflecting interest rates of the day, or can be tied to specific dates during the loan period. Rates may change on a monthly, quarterly or annual basis.

Volatility - The degree to which the debt portfolio is affected by current interest rate movements. The more debt that matures in the year and needs replacing, and the more debt subject to variable interest rates, the greater the volatility.

Yield curve - A graph of the relationship of interest rates to the length of the loan. A normal yield curve will show interest rates relatively low for short term loans compared to long term loans. An inverted yield curve is the opposite of this.

APPENDIX 2

Table 10 Revised Prudential and Treasury Indicators £m

Prudential Indicators	2020/21 Actual	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Capital Expenditure	86.0	156.1	20.0	20.0	20.0
Capital financing requirement (CFR)	673.0	719.6	851.7	830.5	807.3
Total debt	518.6	534.5	681.4	668.9	643.9
Annual Change in CFR					
Capital expenditure financing	60.1	86.5	179.9	20.0	20.0
Debt repayment provision MRP	-50.6	-39.9	-47.9	-41.2	-43.2
Total	9.5	46.6	132.1	-21.2	-23.2

Table 11 Operational boundary for external debt £m

Treasury Indicators	2020/21	2021/22	2022/23	2023/24	2024/25
Borrowing	602.7	594.1	581.0	566.8	550.3
Other long-term liabilities	182.5	195.5	338.5	328.8	318.7
Total	785.2	789.6	919.5	895.6	869.0

Table 12 Authorised limit for external debt £m

Treasury Indicators	2020/21	2021/22	2022/23	2023/24	2024/25
Borrowing	622.7	614.1	601.0	586.8	560.3
Other long-term liabilities	192.5	225.5	368.5	358.8	348.7
Total	815.2	839.6	969.5	945.6	909.0

Table 13 Graph of CFR, total debt, operational boundary and authorised limit

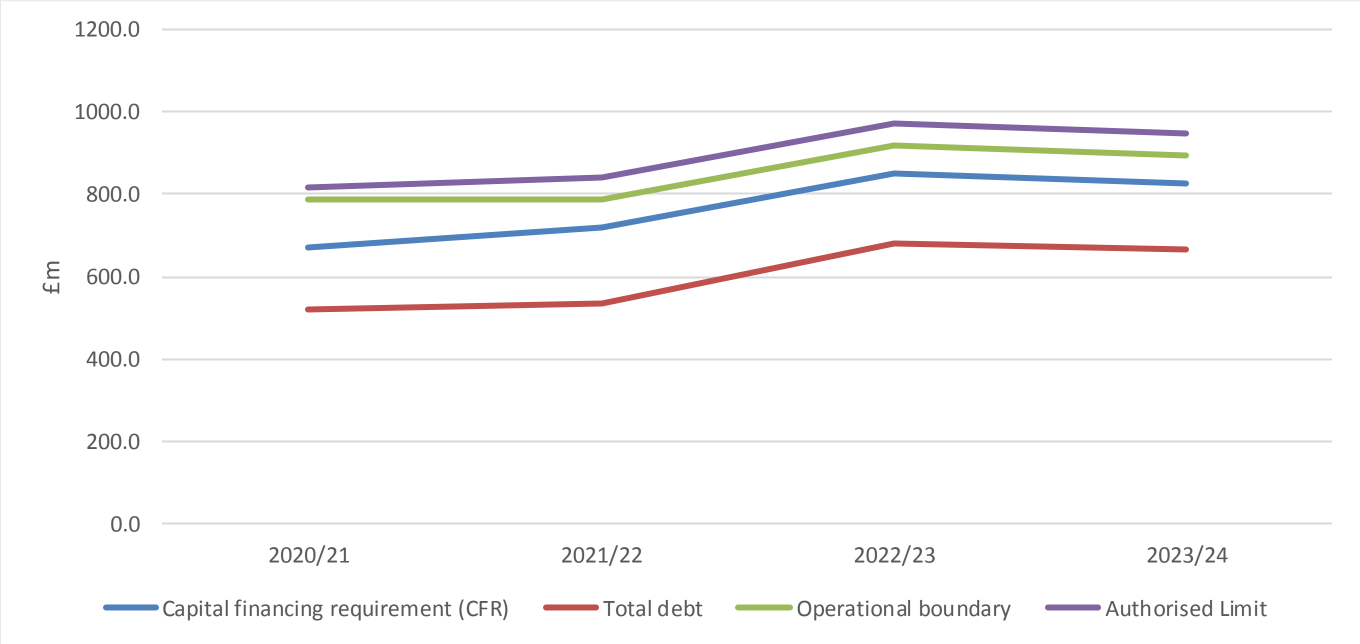

Table 14 Maturity structure for fixed rate borrowing estimated position at year end

	Upper Limit	Lower Limit	%	£M
Under 12 months	75%	0%	24%	125.7
12 and within 24 months	50%	0%	11%	61.2
24 months and within 5 years	50%	0%	19%	100.6
5 years and within 10 years	50%	0%	7%	39.2
10 years and above	100%	25%	39%	207.8

Table 15 Maturity structure for variable rate borrowing estimated position at year end

	Upper Limit	Lower Limit	%	£M
Under 12 months	10%	0%	0%	0.0
12 and within 24 months	0%	0%	0%	0.0
24 months and within 5 years	0%	0%	0%	0.0
5 years and within 10 years	0%	0%	0%	0.0
10 years and above	0%	0%	0%	0.0

Table 16 Upper Limit for Investments beyond 365 days estimated position at year end

	2021/22	2022/23	2023/24	2024/25	Estimated position at year end
Upper Limit for Investments beyond 365 days	£40m	£40m	£40m	£40m	£0

The operational boundary limits for external debt reflect the estimate of the most likely, prudent, but not worst case, scenario without the additional headroom included within the authorised limit.

These indicators should be considered together. Whilst all the council's borrowing is fixed, the amount due to mature in the next 12 months looks high at £125.7m, this is partly explained because the figure includes £83.0m of LOBO loans that are callable in 2021/22, it is unlikely that LOBO loans will be called over the next few years as the LOBO interest rates already exceed current market rates and the option to change lies with the banks. The forecast £36.2m of temporary borrowing due for renewal within 12 months; is in-line with the council's current strategy.

For exceptional reasons only, such as a large-scale voluntary transfer of assets, the indicators may be temporarily flexed to allow repayment and rescheduling of borrowing.