MEETING:	**AUDIT AND GOVERNANCE COMMITTEE**
DATE:	**17 JUNE 2021**
TITLE:	**TREASURY MANAGEMENT 2020/21**
PURPOSE:	**CIPFA's Code of Practice requires that a report on the results of the Council's actual treasury management is produced.**
RECOMMENDATION:	**RECEIVE THE REPORT FOR INFORMATION**
AUTHOR:	**DELYTH JONES-THOMAS, INVESTMENT MANAGER**

Executive Summary

During the 2020/21 financial year the Council's borrowing remained within the limits originally set and total interest received on deposits was £422,000 which was above the budgeted level of £400,000. There were no defaults by institutions in which the Council had deposited money with.

1. Introduction

The Council's Treasury Management Strategy for 2020/21 was approved at Full Council on 5th March 2020.

The Council has borrowed and 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 risk are therefore central to the Council's Treasury Management Strategy.

This report compares the actual performance against the strategy for the financial year 2020/21 and fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the Welsh Government's Investment Guidance.

2. Year End Position

Balance Sheet Summary

At 31 March 2021 the Council had net borrowing of £48m arising from its revenue and capital activities. 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 movements are summarised in the following table:

	31.3.20 Actual £m	**2020/21 Movement £m**	**31.3.21 Actual £m**
CFR	177	(3)	174
Less: Other debt liabilities	(2)	0	(2)
Borrowing CFR	**175**	**(3)**	**172**
Less: Usable reserves	(78)	(30)	(108)
Less: Working capital	3	(19)	(16)
Net borrowing	**100**	**(52)**	**48**

The Council pursued its strategy of keeping borrowing and investments below their underlying levels, sometimes known as internal borrowing, in order to reduce risk and keep interest costs low.

Treasury Management Summary

	31.3.20 Balance £m	**Movement £m**	**31.3.21 Balance £m**	**31.3.21 Rate %**
Long- term borrowing	(104,346)	1,236	(103,110)	5.5
Short-term borrowing	(20,578)	13,999	(6,579)	1.2
PFI	(1,700)	160	(1,540)	n/a
Total borrowing	**(126,624)**	**15,395**	**(111,229)**	
Long-term investments	17	0	17	4.0
Short-term investments	11,259	23,659	34,918	1.5
Cash and cash equivalents	14,900	13,718	28,618	0.02
Total investments	**26,176**	**37,377**	**63,553**	
Net borrowing	**100,448**	**(52,772)**	**47,676**	

3. Borrowing Activity

At 31st March 2021, the Council held £109.7m of loans, a decrease of £15.2m on the previous year.

The debt interest paid in 2020/21 was £5.9 million on an average debt portfolio of £110.7 million at an average interest rate of 5.3%.

The year-end borrowing position and the year-on-year change is summarised in the following table:

	31.3.20 Balance £m	2020/21 Movement £m	31.3.21 Balance £m	31.3.21 Rate %	31.3.21 WAM* years
PWLB	88.2	(1.3)	86.9	5.79	18.9
Bank (Fixed term)	16.2	0.0	16.2	4.22	57.4
Local Authorities (Short term)	19.0	(14.0)	5.0	1.20	0.1
Other	1.5	0.1	1.6	0.00	3.5
Total borrowing	**124.9**	**(15.2)**	**109.7**		

*Weighted average maturity

The Council's main objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with a secondary objective of flexibility to renegotiate loans should the Council's long-term plans change.

Further to these objectives, no new long-term borrowing was undertaken in 2020/21, with existing loans maturing without replacement. This strategy enabled the Council to reduce net borrowing costs (despite foregoing investment income) and reduce overall treasury risk.

The short-term loans taken this year was to ensure sufficient cash was available during the period from January to April 2021 rather than taking on long-term borrowing.

Borrowing Update

In November 2020 the PWLB published its response to the consultation on 'Future Lending Terms'. From 26th November the margin on PWLB loans above gilt yields was reduced from 1.8% to 0.8% providing that the borrowing council can confirm that it is not planning to purchase 'investment assets primarily for yield' in the current or next two financial years. Authorities that are purchasing or intending to purchase investment assets primarily for yield will not be able to access the PWLB except to refinance existing loans or externalise internal borrowing. As part of the borrowing process authorities will now be required to submit more detailed capital expenditure plans with confirmation of the purpose of capital expenditure from the Section 151 Officer. The PWLB can now also restrict local authorities from borrowing in unusual or large amounts.

Acceptable use of PWLB borrowing includes service delivery, housing, regeneration, preventative action, refinancing and treasury management. Misuse of PWLB borrowing could result in the PWLB requesting that the Council unwinds problematic transactions, suspending access to the PWLB and repayment of loans with penalties.

The Council is not planning to purchase any investment assets primarily for yield within the next three years and so is able to take advantage of the reduction in the PWLB borrowing rate.

4. Treasury Investment Activity

During the year, the Council received funding to support small and medium businesses during the coronavirus pandemic through grant schemes. £107,259,960 was received, temporarily invested in short- dated, liquid instruments such as call accounts and Money Market Funds. £106,732,000 was disbursed by the end of March.

The Council has held significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During 2020/21 the Council's investment balances have ranged between £57.0 million and £110.4 million.

Treasury Investment Position

	31.3.20 Balance £m	**2020/21 Movement £m**	**31.3.21 Balance £m**	**31.3.21 Rate %**	**31.3.21 WAM* days**
Banks & building societies (unsecured)	8.7	(0.1)	8.6	0.12	22.4
Local Authorities	0.0	20.0	20.0	0.10	56.0
Money Market Funds	9.1	16.9	26.0	0.02	1.0
Pooled Funds	8.3	0.6	8.9	5.13	365+
Total investments	**26.1**	**37.4**	**63.5**		

*Weighted average maturity

Both the CIPFA Code and government guidance require the Council 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 Council'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. Consequently, the duration of investments and number of institutions available to deposit money with has been reduced based on the advice received from Arlingclose following the impact of the pandemic.

Continued downward pressure on short- dated cash rate brought net returns on sterling low volatility Money Market Funds close to zero even after some managers have temporarily lowered their fees. At this stage net negative returns are not the central case of most MMF managers over the short- term, and fee waivers should maintain positive net yields, but the possibility cannot be ruled out.

Deposit rates with the Debt Management Account Deposit Facility (DMADF) have continued to fall and are now largely around zero.

£8.9m of the Council's investments are held in externally managed strategic pooled equity and property funds where short term liquidity are lesser considerations, and the objectives instead are regular revenue income and long- term price stability. These funds generated an income return of 5.1% and an unrealised capital gain of £0.66m in this financial year.

The Council is invested in equity and property funds. During the initial phase of the pandemic in March 2020, the sharp falls in corporate bond and equity markets had a negative impact on the value of the Council's pooled fund holdings and was reflected in the 31st March 2020 fund valuations with every fund registering negative capital returns over a 12 month period. Since March 2020 there has been improvement in market sentiment which is reflected in an increase in capital values of these funds in the Council's portfolio. The recovery in UK equities has lagged those of US and European markets.

Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued stability in meeting the Council's medium to long term investment objectives are regularly reviewed. Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years but with the confidence that over a three-to five year period total returns with exceed cash interest.

Investment Benchmarking

	Credit Score	**Credit Rating**	**Bail-in Exposure**	**WAM* (days)**	**Income Rate of Return**
31.03.2020	4.99	A+	100%	31	1.97%
31.03.2021	**4.73**	**A+**	**63%**	**25**	**0.77%**
Similar LAs	**4.42**	**AA-**	**34%**	**70**	**0.22%**
All LAs	**4.63**	**A+**	**63%**	**14**	**0.90%**

*Weighted average maturity

5. Compliance Report

Compliance with specific investment limits is demonstrated in the following tables:

Debt Limits

	2020/21 Maximum	31.3.21 Actual	2020/21 Operational Boundary	2020/21 Authorised Limit	Complied
Borrowing	£123.4m	£108m	£190m	£200m	✓

Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure.

Investment Limits

	2020/21 Maximum	31.3.21 Actual	2020/21 Limit	Complied
Any single organisation, except the UK Government	£7m	£7m	£8m each	✓
Any group of organisations under the same ownership	£0m	£0m	£8m per group	✓
Any group of pooled funds under the same management	£5m	£5m	£20m per group	✓
Negotiable instruments held in a broker's nominee account	£0m	£0m	£40m per broker	✓
Foreign countries	£5m	£0m	£8m per country	✓
Registered providers and registered social landlords	£0m	£0m	£20m in total	✓
Unsecured investments with Building Societies	£0m	£0m	£8m in total	✓
Loans to unrated companies	£0m	£0m	£8m in total	✓
Money Market Funds	£40m	£26m	£40m in total	✓
Real Estate Investment Trusts	£0m	£0m	£20m in total	✓

6. Treasury Management Indicators

The Council measures and manages its exposures to treasury management risks using the following indicators:

Security: The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the time-weighted average credit score of its investment portfolio. This is calculated by applying a score to each investment and taking the arithmetic average, weighted by the length of each investment. Unrated investments are assigned a score based on their perceived risk.

	31.3.21 Actual	2020/21 Target	Complied
Portfolio average credit score	4.73	a score of 6 or lower	✓

Liquidity: The Council 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 three month period, without additional borrowing.

	31.3.21 Actual	2020/21 Target	Complied
Total cash available within 3 months	£54.6m	£10m	✓

Interest Rate Exposures: This indicator is set to control the Council's exposure to interest rate risk. The upper limits on interest rate exposures expressed as the proportion of net principal borrowed was:

	31.3.21 Actual	2020/21 Limit	Complied
Upper limit on one year revenue impact of a 1% rise in interest rates	£460,757	£324,000	✗
Upper limit on one year revenue impact of a 1% fall in interest rates	£5,096	£23,000	✓

As was reported to the Audit Committee in the Mid Year Review on 30th November 2020, since setting this indicator the economic outlook for interest rates has changed completely with the onset of the global pandemic. The average interest rate received on short term balances was 0.07% during the six month period to 30th September 2020, with more recent investment being made as low as 0.01%. This indication was set when the base rate was 0.75% and therefore it is reasonable that there is such an impact of a 1% rise, and demonstrates the severe impact that the pandemic has had on investment returns.

Maturity Structure of Borrowing: This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing were:

	31.3.21 Actual	**Upper Limit**	**Lower Limit**	**Complied**
Under 12 months	6.00%	25%	0%	✓
12 months and within 24 months	1.43%	25%	0%	✓
24 months and within 5 years	10.85%	50%	0%	✓
5 years and within 10 years	6.43%	75%	0%	✓
10 years and above	75.29%	100%	0%	✓

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

Principal Sums Invested for Periods Longer than 364 days: The purpose of this indicator is to control the Council'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 were:

	2020/21	**2021/22**	**2022/23**
Actual principal invested beyond year end	£10m	£0	£0
Limit on principal invested beyond year end	£20m	£20m	£20m
Complied	✓	✓	✓

Other

CIPFA consultations: In February 2021 CIPFA launched two consultations on changes to its Prudential Code and Treasury Management Code of Practice. These follow the Public Accounts Committee's recommendation that the prudential framework should be further tightened following continued borrowing by some authorities for investment purposes. These are principles-based consultations and will be followed by more specific proposals later in the year.

In the Prudential Code the key area being addressed is the statement that "local authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed". Other proposed changes include the sustainability of capital expenditure in accordance with a council's corporate objectives, i.e. recognising climate, diversity and innovation, commercial investment being proportionate to budgets, expanding the capital strategy section on commercial activities, replacing the "gross debt and the CFR" with the liability benchmark as a graphical prudential indicator.

Proposed changes to the Treasury Management Code include requiring job specifications and "knowledge and skills" schedules for treasury management roles to be included in the Treasury Management Practices (TMP) document and formally reviewed, a specific treasury management committee for MiFID II professional clients and a new TMP 13 on Environmental, Social and Governance Risk Management.

IFRS 16: The implementation of the new IFRS 16 Leases accounting standard has been delayed for a further year until 2022/23.