Treasury Management Mid Term Report Financial Year 2020/21

Committee considering report:	Executive
Date of Committee:	17 December 2020
Portfolio Member:	Councillor Ross Mackinnon
Date Portfolio Member agreed report:	26 November 2020
Report Author:	Shannon Coleman-Slaughter
Forward Plan Ref:	EX3989

1 Purpose of the Report

The Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) requires the Council to approve treasury management semi-annual and annual reports. This report provides an overview of the treasury management activity for financial year 2020/21 as at 30th September 2020.

2 Recommendation

There are no recommendations made within this report. This report is to note only.

3 Implications and Impact Assessment

Implication	**Commentary**
Financial:	The Treasury function is responsible for the daily cash flow management of the Council. Income from investments contributes to the Council's annual budget. The first two quarters of financial year 20/21 have been economically turbulent, the long term economic outlook is uncertain. The Council has seen a reduction on returns on investments but this has been offset from reduced borrowing costs, resulting in no negative impact on the revenue budget as at the end of September 2020.
Human Resource:	Not applicable

Legal:	Not applicable			
Risk Management:	All investments are undertaken with a view to minimising the risk of financial loss. The Investment and Borrowing Strategy approved by the Council sets parameters to ensure this.			
Property:	Not applicable			
Policy:	Not applicable			
	Positive	**Neutral**	**Negative**	**Commentary**
Equalities Impact:				
A Are there any aspects of the proposed decision, including how it is delivered or accessed, that could impact on inequality?		X		
B Will the proposed decision have an impact upon the lives of people with protected characteristics, including employees and service users?		X		
Environmental Impact:		X		
Health Impact:		X		
ICT Impact:		X		
Digital Services Impact:		X		

Council Strategy Priorities:	X			The treasury function supports the delivery of the Council Strategy through the financing of the Council's approved Capital Programme and monitoring of Council cash flows in support of core activities.
Core Business:		X		
Data Impact:		X		
Consultation and Engagement:	Joseph Holmes – Director of Resources Cllr Ross Mackinnon – Portfolio Holder for Finance Treasury Management Group			

4 Executive Summary

4.1 The Council's Investment and Borrowing Strategy for 2020/21 was approved at a meeting 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.

4.2 On 31st March 2020, the Council had a Capital Financing Requirement (CFR) of £239 million (i.e. the underlying need to borrow for capital purposes is measured by the CFR, while usable reserves and working capital are the underlying resources available for investment). On 9th October 2019 the PWLB raised the cost of certainty rate borrowing to 1.8%. A wide ranging consultation on the Public Works and Loan Board (PWLB) closed on 31st July 2020 with the announcement and implementation of the revised lending terms expected in the latter part of this calendar year or early next year. The Council's chief 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 flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective. In keeping with this objective, with short-term interest rates remaining much lower than long-term rates and temporary investments earning Bank Rate or lower, it has been considered to be more cost effective in the near term to use borrowed rolling temporary / short-term loans. At 30th September 2020 the Council held £221.8 million of loans, (an increase of £2.4 million compared to 31st March 2020, as part of its strategy for funding previous and current years' capital programmes. The Council's borrowing position is summarised in the table below.

Borrowing Position	31.3.20 Balance £000	Net Movement £000	30.9.20 Balance £000	30.9.20 Weighted Average Rate %	30.9.20 Weighted Average Maturity (years)
Public Works Loan Board	202,362	-2,925	199,436	3.34%	31.5
PFI Debt	12,971	-361	12,610	6.10%	11.0
Community Bond	0	785	785	1.20%	5.0
Local authorities (short-term)	4,000	5,000	9,000	0.03%	0.1
Total borrowing	**219,333**	**2,499**	**221,832**		

4.3 As PWLB funding margins have lurched quite substantially and there remains a strong argument for diversifying funding sources. During the first two quarters of the financial year West Berkshire became the first Council to successfully launch a community bond designed to fund green initiates in support of the Council Strategy. As at the end of September £785k had been raised against the target £1million. Moving forward the Council will evaluate and pursue these lower cost solutions and opportunities with its external treasury advisor Arlingclose.

4.4 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year, the Council's investment balances ranged between £32 million as at 31st March 2020 to £40 million as at the end of September due to timing differences between income and expenditure. The investment position is shown in the table below.

Treasury Investment Position	31.3.20 Balance £m	Net Movement £m	30.9.20 Balance £m	30.9.20 Income Return %	30.9.20 Weighted Average Maturity days
Banks & building societies (unsecured)	26.3	-13.6	12.6	0.81	55
Government (incl. local authorities)	1.0	26.0	27.0	0.62	147
Money Market Funds	5.0	-4.9	0.1	0.01	1
Total investments	**32**	**7**	**40**	**0.68**	**117**

4.5 In respect of the economic outlook moving forward the corporate world is still adjusting to the economic shock of the coronavirus pandemic, as a result investment income is set against a very different economic backdrop. Bank Rate, which was 0.75% in January/February 2020, now stands at 0.1%. Interest earned from short-dated money market investments is expected to be significantly lower by the end of March 2021. Anticipated shortfalls in investment income are currently being offset through cheaper than budgeted borrowing costs, through the strategy of undertaking short-term borrowing.

5 Supporting Information

Introduction

5.1 The Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Council to approve treasury management semi-annual and annual reports. This report provides an overview of the treasury management activity for financial year 2020/21 as at 30th September 2020.

5.2 The Council's treasury management strategy for 2020/21 was approved at a meeting 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 remains central to the Council's Investment and Borrowing Strategy.

Background

5.3 Economic Conditions: The spread of the coronavirus pandemic dominated during the period as countries around the world tried to manage the delicate balancing act of containing transmission of the virus while minimising negative impacts on national economies. Over the past six months:

(a) The Bank of England (BoE) maintained Bank Rate at 0.1% and its Quantitative Easing programme at £745 billion. The potential use of negative interest rates was not ruled in or out by BoE policymakers.

(b) Government initiatives continued to support the economy, with the furlough (Coronavirus Job Retention) scheme keeping almost 10 million workers in jobs, grants and loans to businesses and 100 million discounted meals being claimed during the 'Eat Out to Help Out' (EOHO) offer.

(c) GDP growth contracted by a massive 19.8% (revised from first estimate -20.4%) between April and June (Office for National Statistics), pushing the annual growth rate down to -21.5% (first estimate -21.7%). Construction output fell by 35% over the quarter, services output by almost 20% and production by 16%. Recent monthly estimates of GDP have shown growth recovering, with the latest rise of almost 7% in July.

(d) The headline rate of UK Consumer Price Inflation (CPI) fell to 0.2% year/year in August, further below the Bank of England's 2% target, with the largest downward contribution coming from restaurants and hotels influenced by the EOHO scheme. The Office for National Statistics' preferred measure of CPIH which includes owner-occupied housing was 0.5% y/y.

(e) Financial markets: Equity markets continued their recovery, with the Dow Jones climbing to not far off its pre-crisis peak, albeit that performance being driven by a handful of technology stocks including Apple and Microsoft, with the former up 75% in 2020. The FTSE 100 and 250 have made up around half of their losses at the height of the pandemic in March. Central bank and government stimulus packages continue to support asset prices, but volatility remains.

(f) Ultra-low interest rates continued, keeping gilts yields low but volatile over the period with the yield on some short-dated UK government bonds remaining negative. The 5-year UK benchmark gilt yield started and ended the June–September period at -0.06% (with much volatility in between). The 10-year gilt yield also bounced around, starting at 0.21% and ending at 0.23% over the same period, while the 20-year rose from 0.56% to 0.74%. 1-month, 3-month and 12-month bid rates averaged 0.02%, 0.06% and 0.23% respectively over the period.

(g) There continues to remain much uncertainty around the extent the losses banks and building societies will suffer due to the impact from the coronavirus pandemic. For UK institutions there is also the further added complication of the end of the Brexit transition period on 31st December and any potential trade deal with the European Union.

5.4 Local Context: Borrowing Strategy over the period 1.4.2020 – 30.9.2020

(a) On 31st March 2020, the Council had a Capital Financing Requirement (CFR) of £239 million (i.e. the underlying need to borrow for capital purposes is measured by the CFR, while usable reserves and working capital are the underlying resources available for investment).

(b) On 9th October 2019 the PWLB raised the cost of certainty rate borrowing to 1.8%. A wide ranging consultation on the Public Works and Loan Board (PWLB) closed on 31st July 2020 with the announcement and implementation of the revised lending terms expected in the latter part of this calendar year or early next year. The consultation titled "Future Lending Terms" allows stakeholders to contribute to developing a system whereby PWLB loans can be made available at improved margins to support qualifying projects. It contains proposals to allow Councils that are not involved in "debt for yield" activity to borrow at lower rates as well as stopping local authorities using PWLB loans to buy commercial assets primarily for yield. The consultation also broaches the possibility of slowing, or stopping, individual authorities from borrowing large sums in specific circumstances.

(c) At 30th September 2020 the Council held £221.8 million of loans, (an increase of £2.4 million compared to 31st March 2020, as part of its strategy for funding previous and current years' capital programmes. The Council's borrowing position is summarised in the table below.

Borrowing Position	31.3.20 Balance £000	Net Movement £000	30.9.20 Balance £000	30.9.20 Weighted Average Rate %	30.9.20 Weighted Average Maturity (years)
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(d) The Council's chief 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 flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective. In keeping with this objective, with short-term interest rates remaining much lower than long-term rates and temporary investments earning Bank Rate or lower, it has been considered to be more cost effective in the near term to use borrowed rolling temporary / short-term loans.

(e) As PWLB funding margins have lurched quite substantially and there remains a strong argument for diversifying funding sources. During the first two quarters of the financial year West Berkshire became the first Council to successfully launch a community bond designed to fund green initiates in support of the Council Strategy. As at the end of September £785k had been raised against the target £1million. Moving forward the Council will evaluate and pursue these lower cost solutions and opportunities with its external treasury advisor Arlingclose.

5.5 Other Debt Activity

(a) Although not classified as borrowing, the Council also has a Private Finance Initiative (PFI) in respect of the Padworth Waste Recycling Facility. This debt, which is included in the total borrowing shown on the Council's balance sheet, stood at £12.8 million at end of September 2020. (Repayments of this debt are included in the monthly waste contract charges, which are paid from the revenue budget for waste management).

5.6 Treasury Management Strategy over the period 1.4.2020 – 30.9.2020

(a) On 1st April 2020 the Council received central government funding to support small and medium businesses during the coronavirus pandemic through grant schemes. £29.3m was received, temporarily invested in short-dated, liquid instruments such as call accounts and Money Market Funds. £28.8m was disbursed by the end of September 2020.

(b) The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year, the Council's investment balances ranged between £32 million as at 31st March 2020 to £40 million as at the end of September due to timing differences between income and expenditure. The investment position is shown in the table below.

Treasury Investment Position	31.3.20	Net	30.9.20	30.9.20	30.9.20
	Balance	Movement	Balance	Income Return	Weighted Average Maturity
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(c) Both the CIPFA Code and government guidance requires the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum 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.

5.7 Non-Treasury Investments

(a) The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. For Councils this is replicated in the Investment Guidance issued by the Ministry of Housing, Communities and Local Government (MHCLG), in which the definition of investments is further broadened to also include all such assets held partially for financial return. The Council also holds £61 million of such investments in respect of directly owned commercial and investment property. These investments at the end of September generated £590k of investment income for the Council after taking account of direct costs, representing a rate of return of 0.96%.

Proposals

There are no proposals included within this report. Report is to note only.

6 Other options considered

No other options have been considered.

7 Conclusion

7.1 In respect of the economic outlook moving forward the corporate world is still adjusting to the economic shock of the coronavirus pandemic, as a result investment income is set against a very different economic backdrop. Bank Rate, which was 0.75% in January/February 2020, now stands at 0.1%. Interest earned from short-dated money market investments is expected to be significantly lower by the end of March 2021. Anticipated shortfalls in investment income are currently being offset through cheaper than budgeted borrowing costs, through the strategy of undertaking short-term borrowing.

8 Appendices

None

Subject to Call-In:

Yes: ☐ No: X

Report is to note only X

Officer details:

Name: Shannon Coleman-Slaughter
Job Title: Chief Financial Accountant
Tel No: 01635 519225
E-mail: shannon.colemanslaughter@westberks.gov.uk

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