



# Report to Audit and Governance Committee

**Date:** 27<sup>th</sup> January 2021

**Reference number:** for cabinet member decisions only

**Title:** Treasury Management Mid-Year Update Report

**Relevant councillor(s):** Katrina Wood, Deputy Leader and Cabinet Member for Resources

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**Recommendations:** The Committee is asked to note the Treasury Management Mid-Year Update Report for 2020/21.

## Executive summary

1.1 The Council is required to report to members on the current year's treasury management activity. It has been agreed that a mid-year report on the treasury management activity for the first six months of the financial year would be reported to CMT and the Audit and Governance Committee.

1.2 The table below is a summary of the Council's borrowing on 30 September 2020.

Principal 1 April 2020		Principal 30 September 2020	Average Interest Rate	Years to Final Maturity (average)
335.448	PWLB	329.975	2.65%	21.8
30.000	LOBO	30.000	4.04%	57.9
365.448	<b>Total</b>	359.975	<b>2.77%</b>	<b>24.8</b>

1.3 The treasury cash (investments) position is summarised below.

As at April 2020		Treasury Investments	As at Sept 2020	
£m	%		£m	%
42.17	31%	Banks	9.00	5%
35.51	26%	Local Authorities (invested less than 364 days)	10.50	6%
37.61	28%	Money Market Funds (MMFs)	137.12	73%
0.000	0%	UK Government	10.000	5%
20.00	15%	Property Fund	20.00	11%
<b>135.29</b>	<b>100%</b>	<b>Total Investments</b>	<b>186.62</b>	<b>100%</b>

1.4 The Council pursues a strategy of keeping borrowing and investments below their underlying levels, sometimes known as internal borrowing, in order to reduce risk and keep external financing costs low. The Council's main 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. In the light of the pandemic crisis and the likelihood of unexpected calls on cash flow, the Council kept more cash available at very short notice than is normal. Liquid cash was diversified over several counterparties and Money Market Funds to manage both credit and liquidity risks. The Council has a £20m investment in the CCLA (Churches, Charities and Local Authorities) Local Authorities Property Fund; trading was suspended by the fund in March 2020. The relative infrequency of property transactions in March as the pandemic intensified meant that it was not possible for valuers to be confident that their valuations correctly reflected prevailing conditions. To avoid material risk of disadvantage to buyers, sellers and holders of units in the property fund, the management company was obliged to suspend transactions until the required level of certainty is re-established. The dealing suspension was lifted in September 2020.

## Content of report

1.5 In line with the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice for Treasury Management and the Council's Financial Regulations, this Council is required to provide the Audit and Governance Committee with a mid-year report on the treasury management activity for the first six months of the financial year.

1.6 The Code of Practice defines Treasury Management as: The management of the organisation'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.

1.7 Treasury management 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).

1.8 The Council’s treasury management strategy was approved by the Shadow Authority on 27<sup>th</sup> February 2020. The general policy is the prudent investment of its treasury balances and cost-effective borrowing to finance long term investment in the Council’s assets.

1.9 **Borrowing**

The Council has arranged a combination of Public Works Loan Board (PWL<sup>1</sup>) loans and loans from financial institutions to meet its borrowing requirements in 2020/21. Loans outstanding totalled £360m at 30 September 2020; £330m was from the PWLB, £30m Lenders Option Borrowers Option (LOBOs<sup>2</sup>) from the money markets. The Council pursues a strategy of keeping borrowing and investments below their underlying levels, sometimes known as internal borrowing, in order to reduce risk and keep external financing costs low. The Council is actively reviewing opportunities for borrowing at low rates if borrowing is required to finance items within the capital programme. The Council is forecast to spend £10.228m on interest for external borrowing activity in the financial year. The table below is a summary of the Council’s borrowing on 30 September 2020.

<b>Principal 1 April 2020</b>		<b>Principal 30 September 2020</b>	<b>Average Interest Rate</b>	<b>Years to Final Maturity (average)</b>
<b>335.448</b>	PWLB <sup>1</sup>	<b>329.975</b>	2.65%	21.8
30.000	LOBO <sup>2</sup>	30.000	4.04%	57.9
<b>365.448</b>	<b>Total</b>	<b>359.975</b>	<b>2.77%</b>	<b>24.8</b>

<sup>1</sup> PWLB Public Works Loans Board. The PWLB is a statutory body, part of HM Treasury; its purpose is to lend money to local authorities. The Council’s main 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.

<sup>2</sup>LOBOs Lender Option Borrower Option. LOBOs are long term borrowing instruments which include an option for the lender to periodically revise the interest rate. If the lender decides to revise the interest rate, the borrower then has the option to pay the revised interest rate or repay the loan.

1.10 On 9<sup>th</sup> October 2019 the PWLB raised the cost of certainty rate borrowing to 1.8%, an increase of 1% above UK gilt yields making it relatively expensive. A reduction of 1% in PWLB loans took effect on 26<sup>th</sup> November 2020 which presents the Council with the opportunity for borrowing for regeneration schemes at low cost. As a

condition of accessing the PWLB, the Council will be asked to confirm there is no intention to buy commercial properties in the current or next two financial years.

1.11 **Treasury Position:** The Council’s investment strategy sets out the approach for choosing investment counterparties. They are based on a system of credit ratings provided by the three main credit rating agencies and supplemented by additional market data (such as rating outlooks, credit default swaps and bank share prices) provided by our treasury advisors.

1.12 The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year, the Council’s investment balances ranged between £185m and £295m, including the CCLA property fund investment, due to timing differences between income and expenditure.

1.13 The treasury cash (investments) position is summarised below.

As at April 2020		Treasury Investments	As at Sept 2020	
£m	%		£m	%
42.17	31%	Banks	9.00	5%
35.51	26%	Local Authorities (invested less than 364 days)	10.50	6%
37.61	28%	Money Market Funds (MMFs)	137.12	73%
0.00	0%	UK Government	10.00	5%
20.00	15%	Property Fund	20.00	11%
<b>135.29</b>	<b>100%</b>	<b>Total Investments</b>	<b>186.62</b>	<b>100%</b>

1.14 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 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. The Council is forecast to achieve £1.205m interest on its investments.

1.15 On 25th September the overnight, 1- and 2-week deposit rates on Debt Management Account Deposit Facility (DMADF) deposits dropped below zero percent to -0.03%, the rate was 0% for 3-week deposits and 0.01% for longer maturities.

1.16 The return on Money Market Funds net of fees also fell over the six months and for many funds net returns range between 0% and 0.1%. In many instances, the fund management companies have temporarily lowered or waived fees to maintain a positive net return.

- 1.17 In the light of the pandemic crisis and the likelihood of unexpected calls on cash flow, the Council kept more cash available at very short notice than is normal. Liquid cash was diversified over several counterparties and Money Market Funds to manage both credit and liquidity risks.
- 1.18 **Externally Managed Pooled Funds** £20m of the Council's investments are held in an externally managed strategic pooled property fund where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and long-term price stability.
- 1.19 Similar to many other property funds, dealing (i.e. buying or selling units) in the CCLA Local Authorities Property Fund was suspended by the fund in March 2020. The relative infrequency of property transactions in March as the pandemic intensified meant that it was not possible for valuers to be confident that their valuations correctly reflected prevailing conditions. To avoid material risk of disadvantage to buyers, sellers and holders of units in the property fund, the management company was obliged to suspend transactions until the required level of certainty is re-established. The dealing suspension was lifted in September 2020. There has also been a change to redemption terms for the CCLA Local Authorities Property Fund; from September 2020 investors are required to give at least 90 calendar days' notice for redemptions.
- 1.20 In 2020/21 Buckinghamshire Council expects to receive significantly lower income from its cash and short-dated money market investments and from its externally managed funds than the legacy Councils did in 2019/20 and earlier years. Income paid will ultimately depend on many factors including but not limited to the duration of COVID-19 and the extent of its economic impact.
- 1.21 In the exceptional circumstances due to the covid pandemic, the Council has invested more in Money Market Funds than the approved Strategy due to the need to keep funds liquid, the near zero rates obtainable with the DMADF and the shortage of counterparties available in the inter-local authority market.
- 1.22 **Prudential Indicators:** Each year, the Council agrees Prudential Indicators under the Local Government Act 2003 which are affordable, prudent and sustainable. The indicators were agreed by the Shadow Authority at its meeting on 27 February 2020.
- 1.23 **Borrowing Indicators:** The Capital Financing Requirement measures the Council's underlying need to borrow for capital purposes. This is essentially the Council's outstanding debt, necessary to finance the Council's capital expenditure. The actual debt is dependent on the type and maturity of the borrowing undertaken as well as seeking the optimal cashflow situation.
- 1.24 Comparing gross debt with the capital financing requirement is an indicator of the Council's prudence in managing its capital expenditure and is designed to ensure that, over the medium term, external borrowing is only for capital purposes. The

Council should ensure that gross debt does not exceed the total of the ‘capital financing requirement’. The values are measured at the end of the financial year.

The authorised limit for external debt is required to separately identify external borrowing (gross of investments) and other long-term liabilities such as covenant repayments and finance lease obligations. The limit provides a maximum figure that the Council could borrow at any given point during each financial year.

- 1.25 The Operational Boundary for External Debt is a key management tool for in-year monitoring and is lower than the Authorised Limit as it is based on an estimate of the most likely level of external borrowing at any point in the year. In comparison, the authorised limit is the maximum allowable level of borrowing.

Indicator			Unit	2020/21	2021/22	2022/23
Gross Debt	Estimate	Years 1, 2 and 3	£m	323.96	394.56	439.86
Capital Financing Requirement			£m	467.53	483.58	482.54

Indicator			Unit	2020/21	2021/22	2022/23
Authorised limit (for borrowing) *	Estimate	Years 1, 2 and 3	£m	630	670	710
Authorised limit (for other long-term liabilities) *	Estimate	Years 1, 2 and 3	£m	10	10	10
<b>Authorised Limit (for total external debt) *</b>			<b>£m</b>	<b>640</b>	<b>680</b>	<b>720</b>

\* These limits can only be breached with the approval of the full Council to raise them

Indicator			Unit	2020/21	2021/22	2022/23
Operational boundary (for borrowing)	Estimate	Years 1, 2 and 3	£m	530.00	570.00	610.00
Operational boundary (for other long-term liabilities)	Estimate	Years 1, 2 and 3	£m	7.50	7.50	7.50
<b>Operational Boundary</b>			<b>£m</b>	<b>537.50</b>	<b>577.50</b>	<b>617.50</b>

- 1.26 The operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

- 1.27 **Treasury Management Indicators:** The Council measures and manages its exposures to treasury management risks using the following indicators.

- 1.28 **Security:** The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Credit Risk Indicator	Indicator as at 30 September 2020	Target
Portfolio average credit rating	AA-	A

- 1.29 **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 one-month period, without additional borrowing.

Liquidity Risk Indicator	Actual	Target
Total cash available within one month	£152.1m	£10m

- 1.30 **Interest rate exposures:** This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

Interest Rate Risk Indicator	Indicator at 30 September 2020	Target
Upper limit on one-year revenue impact of a 1% rise in interest rates	£220,000	£250,000
Upper limit on one-year revenue impact of a 1% fall in interest rates	-£220,000	-£250,000

- 1.31 The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates.

- 1.32 **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 borrowing will be:

Refinancing rate risk indicator	2020/21	Upper Limit	Lower Limit
Under 12 months	17%	25%	0%
12 months and within 24 months	2%	20%	0%
24 months and within 5 years	12%	20%	0%
5 years and within 10 years	18%	25%	0%
10 years and above	51%	70%	25%

1.33 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.

1.34 **Principal sums invested for periods longer than a year:** 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 will be:

<b>Price risk indicator</b>	<b>2020/21</b>	<b>2021/22</b>	<b>2022/23</b>
Actual principal invested beyond year end	£0m	£0m	£0m
Limit on principal invested beyond year end	£25m	£25m	£25m

### Legal and financial implications

1.35 The publication of an annual strategy, a mid-year treasury report and an annual treasury management report conforms to best practice as required by the Code of Practice CIPFA Treasury Management in the Public Services.

### Corporate implications

1.36 There are none.

