Report to Audit and Governance Committee

Date: 30th November 2021

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

Cabinet Member(s): Cllr John Chilver, Cabinet Member for Finance, Resources, Property and Assets and Cllr Tim Butcher Deputy Cabinet Member for Finance, Resources, Property and Assets

Contact officer: Julie Edwards

Ward(s) affected: None specific

Recommendations: **The Committee is asked to note the Treasury Management Mid-Year Update Report for 2021/22.**

1. 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 the Audit and Governance Committee.

1.2 The table below is a summary of the Council's borrowing.

Principal 31 March 2021		Principal 30 September 2021	Average Interest Rate
286.459	PWLB	**283.059**	2.77%
30.000	LOBO	30.000	4.04%
316.459	**Total**	**313.059**	**2.89%**

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

31 March 2021 £m	%	Treasury Investments	30 September 2021 £m	%
68.85	48%	Local Authorities (invested less than 364 days)	93.50	44%
29.17	20%	Money Market Funds	71.24	33%
15.35	11%	UK Government	20.00	9%
10.00	7%	Local Authorities (invested longer than 364 days)	10.00	5%
20.00	14%	Property Fund	20.00	9%
143.37	**100%**	**Total Treasury Investments**	**214.74**	**100%**

1.4 In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs. Liquid cash was diversified over several counterparties and Money Market Funds to manage both credit and liquidity risks. It is now impossible to earn the level of interest rates commonly seen in previous decades as all short term money market investment rates have only risen weakly since the Bank Rate was cut to 0.10% in March 2020. Given this environment and the fact that Bank Rate may only rise marginally by mid-2022, investment returns are expected to remain low. The Council continues to pursue a strategy of keeping borrowing and investments below their underlying levels, sometimes known as internal borrowing, in order to reduce risk. The Council will continue the strategy of internal borrowing while it makes sense to continue with the strategy. There continues to be a shortage of counterparties available in the inter-local authority market, although the Council has been able to place several deals of six months duration earning a marginal premium for locking out the maturity date. Over the next few months the Council will continue to seek these opportunities achieving a marginal premium as the market prices in the anticipated interest rate increase.

1.5 In overall budget terms, the Council is forecast to be £1.000m net better off during the year, despite an underachievement of £0.426m on treasury investment returns due in part to low rates of interest available and a need to invest surplus cash short term to help manage cashflow risk during the pandemic. Another factor, however, was the continuation of the Council's strategy to use surplus cash instead of borrowing, keeping external financing costs low.

1.6 Following a competitive tendering process, Link Treasury Services Limited (Link) were appointed as the Council's treasury advisor with effect from 1 August 2021. Link provided a training session for members of the Audit & Governance Committee in September and they are currently reviewing the Council's treasury management strategy, including investment counterparties and borrowing requirements.

2. Content of report

2.1 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.

2.2 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.

2.3 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). CIPFA is currently consulting on changes to the Treasury Management in the Public Services: Code of Practice and if there are any key changes proposed we will report back to the Committee.

2.4 The Council's Treasury Management Strategy Statement (TMSS) was approved by Council on 24th February 2021, there are no policy changes to the TMSS. 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.

Borrowing

2.5 The Council has a combination of Public Works Loan Board (PWLB[1]) loans and loans from financial institutions to meet its current borrowing requirements. Loans outstanding totalled £313m at 30 September 2021; £283m was from the PWLB, £30m Lenders Option Borrowers Option (LOBOs[2]) 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 £9.041m on interest for external borrowing activity in the financial year. The table below is a summary of the Council's borrowing on 30 September 2021.

Principal 31 March 2021		Principal 30 September 2021	Average Interest Rate
286.459 30.000	PWLB LOBO	**283.059** 30.000	2.77% 4.04%
316.459	**Total**	**313.059**	**2.89%**

[1] 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.

[2] 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.

2.6 Debt rescheduling opportunities have been very limited in the current economic climate and therefore no debt rescheduling has been undertaken to date in the current financial year.

Annual Investment Strategy

2.7 The TMSS for 2021/22, which includes the Council's Treasury Investment Strategy requires the Council to invest its treasury 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. 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. Following a competitive tendering process, Link Treasury Services Limited (Link) were appointed as the Council's treasury advisor with effect from 1 August 2021. Link provided a training session for members of the Audit & Governance Committee in September and they are currently reviewing the Council's treasury management strategy, including investment counterparties and borrowing requirements.

2.8 The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year to date, the Council's investment balances ranged between £155m and £235m, including the CCLA property fund investment, due to timing differences between income and expenditure.

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

31 March 2021 £m	%	Treasury Investments	30 September 2021 £m	%

68.85	48%	Local Authorities (invested less than 364 days)	93.50	44%
29.17	20%	Money Market Funds	71.24	33%
15.35	11%	UK Government	20.00	9%
10.00	7%	Local Authorities (invested longer than 364 days)	10.00	5%
20.00	14%	Property Fund	20.00	9%
143.37	**100%**	**Total Treasury Investments**	**214.74**	**100%**

2.10 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 £1.008m interest on its investments. There continues to be a shortage of counterparties available in the inter-local authority market, although the Council has been able to place several deals of six months duration earning a marginal premium for locking out the maturity date. Over the next few months the Council will continue to seek these opportunities achieving a marginal premium as the market prices in the anticipated interest rate increase.

2.11 In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs. Liquid cash was diversified over several counterparties and Money Market Funds to manage both credit and liquidity risks. It is now impossible to earn the level of interest rates commonly seen in previous decades as all short term money market investment rates have only risen weakly since the Bank Rate was cut to 0.10% in March 2020. Given this environment and the fact that Bank Rate may only rise marginally by mid-2022, investment returns are expected to remain low.

2.12 Treasury management's role is to ensure that the Council has cash available to meet its day to day requirements. Environmental, Social and Governance (ESG) treasury investments are being developed but do not represent a significant proportion. Treasury investments are generally short term, some overnight, secure, providing access to cash when the Council needs it. They don't include fossil fuels or companies with a large carbon footprint. Treasury investments place cash somewhere safe that generates a return to the benefit of the residents of Buckinghamshire.

2.13 **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.

Prudential Indicators

2.14 Each year, the Council agrees Prudential Indicators under the Local Government Act 2003 which are affordable, prudent and sustainable. The indicators were agreed by full Council at its meeting on 24th February 2021. During the half year ended 30th September, the Council has operated within the treasury and prudential indicators set out in the Council's TMSS for 2021/22. The Service Director – Corporate Finance and Section 151 Officer reports that no difficulties are envisaged for the current or future years in complying with these indicators. CIPFA is currently consulting on changes to the Prudential Code for Capital Finance in Local Authorities and if there are any key changes proposed we will report back to the Committee.

Borrowing Indicators

2.15 The Capital Financing Requirement (CFR) measures the Council's underlying external need to borrow for capital purposes. This is essentially the Council's outstanding debt, necessary to finance the Council's capital expenditure. Each year the CFR is increased by the amount of debt required to support the capital programme and reduced by revenue charges for the repayment of debt. The actual debt is dependent on the type and maturity of the borrowing undertaken as well as seeking the optimal cashflow situation.

2.16 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. Gross external borrowing should not, except in the short term, exceed the total of the CFR. The values are measured at the end of the financial year. The table below shows that the Council is projected to have borrowings of £309.64m by 31 March 2022 which means that it has utilised £173.94m of cash flow funds in lieu of borrowing (internal borrowing). The Council's estimated annual saving by not paying interest on external debt and foregoing investment interest, which is low in the current economic circumstances, is £3.1m.

Indicator	**Unit**	**Year End Forecast 2021/22**	**Approved 2021/22**	**Approved 2022/23**
Gross Debt	£m	309.64	394.56	439.86
Capital Financing Requirement	£m	483.58	483.58	482.54
Internal Borrowing	**£m**	**173.94**	**89.02**	**42.68**

2.17 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.

2.18 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	2021/22	2022/23
Authorised limit (for borrowing) *	£m	670.00	710.00
Authorised limit (for other long term liabilities) *	£m	10.00	10.00
Authorised Limit (for total external debt) *	**£m**	**680.00**	**720.00**

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

Indicator	Unit	2021/22	2022/23
Operational boundary (for borrowing)	£m	570.00	610.00
Operational boundary (for other long term liabilities)	£m	7.50	7.50
Operational Boundary	**£m**	**577.50**	**617.50**

2.19 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.

Treasury Management Indicators

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

2.21 **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 2021	Target
Portfolio average credit rating	AA-	A

2.22 **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	£86.2m	£10m

Maturity structure of borrowing: This indicator is set to control the Council's exposure to refinancing risk. The 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. The upper and lower limits on the maturity structure of borrowing will be:

Refinancing rate risk indicator	**2021/22**	**Upper Limit**	**Lower Limit**
Under 12 months	1%	30%	0%
12 months and within 24 months	5%	25%	0%
24 months and within 5 years	7%	30%	0%
5 years and within 10 years	25%	40%	0%
10 years and above	62%	80%	20%

2.23 **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:

Price risk indicator	**2021/22**	**2022/23**	**2023/24**
Actual principal invested beyond year end	£10m	£0m	£0m
Limit on principal invested beyond year end	£50m	£25m	£25m

3. Legal and financial implications

1.1 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.

4. Corporate implications

4.1 There are none.

5. Background papers

5.1 **None.**