TORBAY COUNCIL

Meeting: Audit Committee **Date:** 26th May 2021

Wards affected: All Wards in Torbay

Report Title: Treasury Management Outturn 2020/21 Report

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1. Purpose of Report

1.1 This report is to provide members with an annual report on the treasury management activities undertaken during the year 2020/21, which is compared to the 2020/21 Treasury Management Strategy.

2. Reason for Proposal and its benefits

2.1 Treasury risk management at the Authority 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) which requires the Authority to approve a treasury management strategy before the start of each financial year and, as a minimum, a semi-annual and annual treasury outturn report. This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

3. Recommendation(s) / Proposed Decision

i) That the Treasury Management decisions made during 2020/21, as detailed in the submitted report be noted.

Appendices

Appendix 1: Economic Commentary

Appendix 2: Non-Treasury Investments (Exempt)

Background Documents

Treasury Management Strategy 2020/21

Supporting Information

1. Introduction

1.1 In February 2019 the Authority adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Authority to approve treasury management semi-annual and annual reports.

1.2 The Authority's treasury management strategy for 2020/21 was approved at a meeting on 6th February 2020. The Authority 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 Authority's treasury management strategy.

2. External Context

2.1 An economic commentary for the year provided by the Council's treasury management advisors, Arlingclose, is provided at Appendix 1 to this report. The Bank of England lowered its base rate to 0.1% as one of the economic responses to COVID.

2.2 The Council's cash flow was significantly impacted by Central Government's response to COVID. As examples: Central Government passed to the Council over £75m of funding for distribution to businesses as grants in their area and provided over £24m of additional grant as compensation for the COVID NNDR reliefs in 2021/22.

3. Local Context

3.1 On 31st March 2021, the Authority had net borrowing of £314.6m arising from its revenue and capital income and expenditure. 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. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.3.21 Actual £m
Total CFR (estimated)	**419.8**
Less: *Other debt liabilities	(16.8)
Borrowing CFR	**403.0**
External borrowing	391.5
Internal borrowing	11.5
Less: Usable reserves	(49.1)
Less: Working capital and other cash backed balance sheet items	(20.2)
Less: Timing of Covid grants to be applied or repayable to central government	(19.1)
Net treasury position	**314.6**

* PFI liabilities that form part of the Authority's total debt

3.2 Lower official interest rates have lowered the cost of short-term, temporary loans and investment returns from cash assets that can be used in lieu of borrowing. The Authority pursued its strategy of keeping borrowing and investments below their underlying levels, sometimes known as internal borrowing, to reduce risk and keep interest costs low.

3.3 The treasury management position on 31st March 2021 and the change during the year is shown in Table 2 below.

Table 2: Treasury Management Summary

	31.3.20 Balance £m	**Movement £m**	**31.3.21 Balance £m**	**31.3.21 Rate %**
Long-term borrowing*	395.2	(3.7)	391.5	2.99
Short-term borrowing	0.0	0.0	0.0	0.0
Total borrowing	**395.2**	**(3.7)**	**391.5**	**2.99**
Long-term investments*	(9.7)	5.0	(4.7)	2.97
Short-term investments	(48.5)	(22.6)	(71.4)	0.26
Cash and cash equivalents	(7.7)	6.6	(0.8)	0.13
Total investments	**(65.9)**	**(11.0)**	**(76.9)**	**0.36**
Net position	**329.3**	**(14.7)**	**314.6**	**2.56**

*Long term investments include the CCLA Property Fund at market valuation.

4. Borrowing Update

4.1 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 authority 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 for any borrowing 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.

4.2 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 Authority unwinds problematic transactions, suspending access to the PWLB and repayment of loans with penalties.

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

4.4 Borrowing strategy

At 31st March 2021 the Authority held £391.5m of loans, (a decrease of £3.7m 31st March 2020, as part of its strategy for funding previous [and current] years’ capital programmes. Outstanding loans on 31st March are summarised in Table 3 below.

Table 3: Borrowing Position

	31.3.20 Balance £m	Net Movement £m	31.3.21 Balance £m	31.3.21 Weighted Average Rate %	31.3.21 Weighted Average Maturity (years)
Public Works Loan Board	385.2	(3.7)	381.5	2.949	28.0
Banks (LOBO)	5.0	-	5.0	4.700	57.6
Banks (fixed-term)	5.0	-	5.0	4.395	53.5
Total borrowing	**395.2**	**(3.7)**	**391.5**	**2.989**	**28.7**

4.5 The Authority’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 Authority's long-term plans change being a secondary objective.

4.6 In keeping with these objectives, no new borrowing was undertaken, while £3.7m of existing loans could mature without replacement. This strategy enabled the Authority to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.

4.7 LOBO loans: The Authority continues to hold a £5m LOBO (Lender's Option Borrower's Option) loan where the lender has the option to propose an increase in the interest rate as set dates, following which the Authority has the option to either accept the new rate or to repay the loan at no additional cost. The lenders option does not become due until 2028.

5. Other Debt Activity

5.1 After £0.8m repayment of prior years' Private Finance Initiative liabilities, total debt other than borrowing stood at £16.8m on 31st March 2021, taking total debt to £408.3m

6. Treasury Investment Activity

6.1 During the year the Council received significant central government funding to support small and medium businesses during the coronavirus pandemic through grant schemes. Over £75m was received, temporarily invested in short-dated, liquid instruments such as call accounts and Money Market Funds. £56m was disbursed by the end of March with £8.7m of the balance being repaid to Central Government in May 2021.

6.2 The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year, the Authority's investment balances ranged between £77 million and £122 million due to timing differences between income and expenditure. The investment position is shown in table 4 below.

Table 4: Treasury Investment Position

	31.3.20 Balance £m	**Net Movement £m**	**31.3.21 Balance £m**	**2020/21 Income Return %**	**2020/21 Weighted Average Maturity days**
Banks & building societies (unsecured)	30.7	(7.9)	22.8	0.16	56
Government (incl. local authorities)	8.0	23.0	31.0	0.17	22
Money Market Funds	18.5	(4.1)	14.4	0.14	1

Other Pooled Funds:					
- *Cash plus fund*	4.0	-	4.0	1.13	
- *Property fund*	4.7	-	4.7	4.35	
Total investments	**65.9**	**11.0**	**76.9**	**0.50**	

6.3 Both the CIPFA Code and government guidance require the Authority 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 Authority'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.

6.4 Continued downward pressure on short-dated cash rate brought net returns on sterling low volatility net asset value money market funds (LVNAV MMFs) 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.

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

6.6 The net return on Money Market Funds net of fees, which had fallen after Bank Rate was cut to 0.1% in March, are now at or very close to zero; fund management companies have temporarily lowered or waived fees to avoid negative net returns.

6.7 The progression of risk and return metrics are shown in the extracts from Arlingclose's quarterly investment benchmarking in Table 5 below.

Table 5: Investment Benchmarking – Treasury investments managed in-house

	Credit Score	**Credit Rating**	**Bail-in Exposure**	**Weighted Average Maturity (days)**	**Rate of Return %**
31.09.2020	4.21	AA-	71%	41	0.15
31.03.2021	4.46	AA-	55%	32	0.11
Similar LAs	**4.66**	**A+**	**68%**	**32**	**0.12**
All LAs	**4.63**	**A+**	**63%**	**14**	**0.15**

6.8 The benchmarking results reflect the Council's risk averse attitude in both counterparties and the maximum sum invested in any one counterparty. Priority has been to keep funds as secure as possible during pandemic and while this is reflected in the relatively low return, the additional margins potentially available are insufficient reward for the increased risk.

6.9 Funds were substantially kept liquid to achieve the Council's policy of internal borrowing and to reflect the short-term holding of Central Government funding. At outturn the capital spend was £27m against the last revised plan of £43m resulting in a higher-than-expected cash balance at year end. No investment properties were purchased which resulted in the lowest level of capital expenditure for several years.

6.10 **Externally Managed Pooled Funds**: £5m of the Authority's investments are invested 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. These funds generated an income return of £0.23m (4.35%) and an unrealised capital loss of £-0.03m (-0.71%).

6.11 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 and lifted in September. There was also 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. The capital value of the property fund(s) is shown in Table 4, above.

7. Non-Treasury Investments

7.1 The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Authority as well as other non-financial assets which the Authority holds primarily for financial return. This is replicated in the Investment Guidance issued by Ministry of Housing, Communities and Local Government's (MHCLG) and Welsh Government, in which the definition of investments is further broadened to also include all such assets held partially for financial return.

7.2 A full list of the Authority's non-treasury investments is presented at Appendix 2 (exempt)

8. Treasury Performance

8.1 The Authority measures the financial performance of its treasury management activities both in terms of its impact on the revenue budget and its relationship to benchmark interest rates, as shown in table 6 below.

Table 6: Performance

As at 31st March 2021	**Revised Budget 2020/21**	**Projected Outturn 2020/21**	**Variation**
	£M	**£M**	**£M**
Investment Income	(0.4)	(0.5)	(0.1)
Interest Paid on Borrowing	12.5	11.8	(0.7)
Net Position (Interest)	**12.1**	**11.3**	**(0.8)**
Minimum Revenue Provision	6.4	6.4	0.0
Net Position (Other)	**6.4**	**6.4**	**0.0**
Net Position Overall	**18.5**	**17.7**	**(0.8)**

9. Compliance

9.1 The Chief Finance Officer reports that all treasury management activities undertaken during the year complied fully with the CIPFA Code of Practice and the Authority's approved Treasury Management. Compliance with specific limits is demonstrated in table 7 below.

Table 7: Debt Limits

	2020/21 Maximum	**31.3.21 Actual**	**2020/21 Operational Boundary**	**2020/21 Authorised Limit**	**Complied?** Yes/No
Borrowing	£395.2M	£391.5	£570m	£690m	Yes
PFI & Finance Leases	£17.8m	£16.8m	£20m	£20m	Yes
Total Debt	**£413.0m**	**£408.3**	**£590m**	**£710m**	Yes

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

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

	31.3.21 Actual	**Upper Limit**	**Lower Limit**	**Complied?**
Under 12 months	1%	40%	0%	Yes
12 months and within 24 months	1%	40%	0%	Yes
24 months and within 5 years	4%	30%	0%	Yes
5 years and within 10 years	9%	40%	0%	Yes
10 years and within 20 years	16%	50%	0%	Yes
20 years and within 30 years	8%	60%	0%	Yes
30years and within 40 years	33%	50%	0%	Yes
40 years and	27%	50%	0%	Yes

Principal Sums Invested for Periods Longer than a year: The purpose of this indicator is to control the Authority'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	£5m	£5m
Limit on principal invested beyond year end	£20m	£20m	£20m
Complied?	Yes	Yes	Yes

10. Other

10.1 **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.

10.2 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 an authority'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.

10.3 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.

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