AGENDA ITEM NO 7

REPORT NO 326/20

ANGUS COUNCIL

17 DECEMBER 2020

TREASURY MANAGEMENT 2020/21 MID-YEAR REVIEW

REPORT BY DIRECTOR OF FINANCE

ABSTRACT
This report reviews Angus Council's treasury management arrangements, activity and performance for the period 1 April 2020 to 30 September 2020.

1. RECOMMENDATION

1.1 It is recommended that the council review and scrutinise the treasury management activities for the period 1 April 2020 to 30 September 2020, as attached at **Appendix 1**.

2. ALIGNMENT TO THE COUNCIL PLAN / COMMUNITY PLAN

2.1 Treasury management is the management of borrowing, investments and cash flows; banking, money market and capital market transactions; the effective control of risks associated with those activities; and the pursuit of optimum performance consistent with those risks. Effective treasury management therefore maximises the resources available to the council to provide services.

2.2 The activities undertaken through the council's treasury management processes, as reflected in **Appendix 1** to this report, therefore contribute as a whole to the outcomes contained within the Council Plan and the Community Plan.

3. BACKGROUND

3.1 The annual minimum reporting requirements with regard to treasury management (per the Treasury Management in the Public Services Code of Practice (2017 edition) and the Prudential Code for Capital Finance in Local Authorities (2017 edition), both published by the Chartered Institute of Public Finance and Accountancy (CIPFA)) are that full council should receive the following reports:

- an annual treasury strategy in advance of the year (for 2020/21, report 72/20 refers)
- a mid-year treasury management review (this report)
- an annual report following the year end describing the activity compared to the strategy (this will be produced after the 2020/21 year end).

3.2 This treasury management mid-year review details Angus Council's treasury management arrangements, activities and performance for the period 1 April 2020 to 30 September 2020 (as attached at **Appendix 1**), thereby ensuring compliance with the aforementioned CIPFA Codes of Practice.

4. TREASURY MANAGEMENT MID-YEAR REPORT

<u>COVID-19 Pandemic</u>

4.1 The first 6 months of 2020/21 has been dominated by the COVID-19 pandemic, the impact of which has filtered into every aspect of economic and commercial life at both a national and local level. Angus Council has experienced unprecedented levels of cash balances during this time - partly due to the timing and phasing of grant income coming into the Council, but also resulting from the cessation of all capital works due to lockdown. Continued economic uncertainty has seen the Bank Rate remain at a historically low 0.10 per cent throughout this time and investment rates hovering just above zero in many cases, and it is within this context that the mid-year review must be viewed.

4.2 Other events with the potential to impact on treasury operations going forward include:

- PWLB Consultation on Future Lending Terms
  An unexpected increase in Public Works Loan Board (PWLB) interest rates took place on 9 October 2019 which was subsequently partially reversed on 11 March 2020 in terms of HRA borrowing with the creation of a specific HRA rate to support lending for social housing. Subsequent to this the Government announced a consultation with local authorities on possibly further amending the margins over gilt yields for PWLB rates. The consultation closed on 31 July 2020 and the outcome is awaited. One aspect that is clear from this review, is that the Treasury will no longer allow local authorities to borrow money from the PWLB to purchase commercial property if the aim is solely to generate an income stream (assets for yield). This is predominantly an issue concerning a small number of English local authorities.

- Review of Angus Council's Loans Fund
  Angus Council's treasury advisors, Link Asset Services, have undertaken a review of the loans fund as a result of revised flexibility that has been granted to local authorities (through the Local Authority (Capital Financing and Accounting) (Scotland) Regulations 2016) on how they account for loans fund advances. The report on the loans fund review was originally intended to be presented to council at this same meeting. It has however been deferred to allow officers to assess how the review will work alongside the fiscal flexibilities that have been provided to support COVID costs, specifically the flexibility relating to the loan repayment holiday. A further update on the outcome of this assessment will be provided in due course.

  Link Asset Services carried out an online training session for members on 2 November which, as well as covering the loans fund review and a council-specific treasury management overview, provided an update on the current and forecast economic climate.

5. FINANCIAL IMPLICATIONS

5.1 There are no direct financial implications arising from the recommendations in this report. An effective treasury management service does however form a significant part of the council's financial arrangements and its financial wellbeing.

6. RISK IMPLICATIONS

6.1 This report does not require any specific risk issues to be addressed, however members will be aware that the management of risk is an integral part of the council's treasury management activities.

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NOTE

No background papers as defined by Section 50D of the Local Government (Scotland) Act 1973 (other than any containing confidential or exempt information) were relied on to any material extent in preparing this Report.

List of Appendices

Appendix 1: Treasury Management Mid-Year Review for the Period 1 April 2020 to 30 September 2020

Appendix 1

Treasury Management Mid-Year Review for the Period 1 April 2020 to 30 September 2020

1. Introduction

1.1 This mid-year review report has been prepared in compliance with the Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management Code of Practice and covers the following:

- borrowing position at 30 September 2020 (section 2)
- capital financing requirement (section 3)
- long term borrowing undertaken (section 4)
- long term borrowing repaid (section 5)
- PWLB interest rates (section 6)
- investment position at 30 September 2020 (section 7)
- debt rescheduling (section 8)
- variations from agreed policies and practices (section 9)
- compliance with treasury and prudential limits (section 10).

1.2 The 2020/21 Treasury Management Strategy Statement (TMSS) was approved by this council on 19 March 2020 (report 72/20 refers). There are no policy amendments required to the TMSS based on the latest economic position or budgetary changes already approved.

2. Borrowing Position at 30 September 2020

2.1 The council's gross and net external debt positions as at 30 September 2020 are shown in Table 1 below. The gross and net external debt positions as at 1 April 2020 are also shown for comparative purposes.

Table 1

External Debt	Position as at 30 September 2020 £m	Position as at 1 April 2020 £m
Fixed Rate Borrowing – PWLB *	114.274	114.570
Fixed Rate Borrowing – LOBO **	16.000	16.000
Fixed Rate Borrowing – Market ***	14.000	14.000
Total External Debt	**144.274**	**144.570**
Investments	(109.394)	(68.442)
Total Net External Debt	34.880	76.128

Notes

* PWLB = Public Works Loans Board
** LOBO borrowing is from banks and similar financial institutions – these loans allow the lender to vary the rate of interest at specific points in time (referred to as call dates) but the council is not legally obliged to accept such changes hence both the lender and borrower have options on whether to continue the loan or not.
*** Market borrowing is from banks and similar institutions in traditional fixed rate and fixed term form.

3. Capital Financing Requirement

3.1 The council calculates a rolling 12 month forecast of its Capital Financing Requirement (CFR). The CFR represents the level of borrowing for capital purposes which it is projected that the council requires to have in place, including the gross external debt already in place, at the end of the rolling 12 month period. The forecast CFR at any point in time therefore essentially takes the existing gross external debt and adjusts for projected net capital expenditure over the forthcoming 12 month period. The CFR therefore denotes a snapshot of the underlying need to borrow for capital purposes and this makes it a crucial part of our borrowing arrangements in compliance with relevant Codes of Practice. At 30 September 2020 the CFR was projected to be £169.518m (that is to say the projected value of our external debt requirements at 30 September 2020).

3.2 Where there is headroom between existing gross external debt levels and the CFR, the council may, at any time over the 12 month period, borrow from the Public Works Loan Board (PWLB) or the money market (external borrowing). Alternatively, the council may on a temporary basis borrow from internal balances (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. When the gross external debt and CFR information shown above is taken into account, it can be seen that there is borrowing headroom at 30 September 2020 of £25.244m (CFR of £169.518m less gross debt of £144.274m). This is however a snapshot position, with the headroom projected to rise over the remainder of the financial year.

4. Long Term Borrowing Undertaken

4.1 No new borrowing has been undertaken during the period 1 April 2020 to 30 September 2020. Whilst under normal circumstances there would be an underlying need to borrow for capital purposes, as the council currently holds significant levels of temporary cash in balances new long term borrowing has been deferred over the first half of the year, with the intention of reducing underlying cash balances. This deferment strategy benefits the council by reducing the total interest payable on debt providing interest rates do not rise significantly in the interim.

4.2 The latest interest rate forecast provided by the council's treasury management advisers (detailed in Table 4 below) indicates that there is likely to be little upward movement in PWLB interest rates for new borrowing over the next two years. It will take economies, including the UK, a prolonged period to recover all of the momentum lost in the sharp recession caused during the COVID-19 pandemic shut down period.

4.3 In respect of potential borrowing from the PWLB, the council has access to a 20 basis point (0.20 per cent) discount (otherwise known as the Certainty Rate) on all borrowing undertaken from PWLB in return for providing information on potential long term borrowing and associated capital spending plans. Angus Council will continue to annually submit the information necessary to ensure ongoing access to the reduced borrowing rates.

4.4 It is the view of the Director of Finance that new borrowing is unlikely to be undertaken over the remainder of the financial year, having taken account of:

- the interest rate forecast (Table 4 below);
- the Certainty Rate discount on new borrowing detailed above;
- external advice from the council's treasury advisers;
- the current and projected headroom between the council's current external debt and the CFR;
- the slow-down in capital expenditure as a result of the COVID-19 pandemic; and
- the current and projected levels of cash balances.

4.5 Although the council has a significant capital programme it is currently more appropriate to use surplus cash balances held to finance that capital expenditure before considering taking out new loans. This approach makes sense both in terms of managing counterparty risk and also allows the council to postpone the cost of new borrowing.

4.6 Further borrowing could still however be undertaken should prevailing economic and market conditions over the remainder of the financial year move to the advantage of the council. It is also possible that non-PWLB borrowing may become more competitive compared with PWLB rates and the Director of Finance will closely monitor the situation to ensure that any appropriate borrowing opportunities are fully considered and actioned where this is of benefit to the council.

4.7 As previously, it would be intended that any such borrowing will be taken at a number of points during the year to mitigate the risk of interest rate movements and taking cognisance of the subsequent lending opportunities that are available in respect of the net cost of incurring additional borrowing.

4.8 In accordance with the 2020/21 Treasury Management Strategy Statement, the council has not borrowed in advance of need during the first half of the 2020/21 financial year and has no intention to borrow in advance for the remainder of the 2020/21 financial year.

5. Long Term Borrowing Repaid

5.1 The council has repaid £0.296m of PWLB loans that naturally matured in the period 1 April 2020 to 30 September 2020, the details of which are shown in Table 2 below:

Table 2

Date Repaid	Amount £m	Rate %
30/09/20	0.296	10.875
Totals	**0.296**	

5.2 A further £3.180m of PWLB loans (at interest rates between 8.250 per cent and 14.000 per cent) mature during the second half of the financial year.

6. PWLB Interest Rates

6.1 The lowest, highest and average PWLB interest rates available during the period 1 April 2020 to 30 September 2020 for 5, 10, 25 and 50 year terms are detailed in Table 3 below. For clarity the rates shown within Table 3 have been reduced to reflect the 20 basis point PWLB Certainty Rate discount. It will be noted that even in a short period of only six months there has been sizeable movements in the rates available.

Table 3

Period	Interest Rate Low Point %	Interest Rate High Point %	Average Interest Rate %
5 years	1.67	1.99	1.81
10 years	1.91	2.19	2.04
25 years	2.40	2.80	2.52
50 years	2.13	2.65	2.30

6.2 The council's treasury advisor, Link Asset Services, has provided the following forecast for UK Bank Rates (also known as the Base Rate) and new PWLB borrowing interest rates (again reflecting the Certainty Rate discount), as detailed in Table 4 below.

Table 4

Rate	Dec 20 %	Mar 21 %	Jun 21 %	Sep 21 %	Dec 21 %	Mar 22 %	Jun 22 %	Sep 22 %
Bank Rate	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
5 Year	1.90	2.00	2.00	2.00	2.00	2.00	2.10	2.10
10 Year	2.10	2.10	2.10	2.10	2.20	2.20	2.20	2.30
25 Year	2.50	2.50	2.50	2.60	2.60	2.60	2.70	2.70
50 Year	2.30	2.30	2.30	2.40	2.40	2.40	2.50	2.50

7. Investment Position at 30 September 2020

7.1 In accordance with CIPFA's Treasury Management Code of Practice, it is the council's investment priority to:

- ensure the **security** of capital (i.e. the safety of the investment);

- ensure the availability of **liquidity** (i.e. the accessibility of the cash); and
- thereafter to obtain an appropriate level of **return** (i.e. the income received) which is consistent with the council's risk appetite.

7.2 The average daily level of funds available for investment purposes in the first six months of 2020/21 was £89.789m. These funds were available on a temporary basis, and the level of funds that were available was mainly dependent on the timing of payments, receipt of grants and other income and progress on the capital programme.

7.3 Angus Council has experienced unprecedented levels of cash balances during the COVID-19 pandemic, in part due to the timing and phasing of grant income coming into the council. In many cases, this additional grant income was expended relatively soon after it was received, e.g. the business grants. General revenue grant, which would normally be received in equal instalments from the Scottish Government throughout the financial year, was "front loaded" over April, May and June to allow councils to cover additional COVID-related costs coming through at this time. The cessation of all capital works due to the lockdown, as well limited spending on other areas such as maintenance works, drastically reduced payments to suppliers however, hence the build up of cash balances over this time.

7.4 During the six month period to 30 September 2020 there were two breaches of counterparty limits approved within the Annual Investment Strategy:

- In accordance with our treasury management strategy any excess funds, up to a maximum of £20m, can be invested overnight with the Clydesdale Bank to earn interest and allow readily available funds to meet daily cash flow requirements. On 27 May 2020 due to an unexpected higher amount of income being received, funds available for overnight investment exceeded the maximum which can be placed with Clydesdale Bank. Readily available cash was required at this time as cash flows were unpredictable, therefore a decision had to be made at short notice to place £1m overnight on a money market fund. This was an expedient and low risk solution to unexpected circumstances. Although this resulted in the maximum balance on the fund being exceeded by £1m for 1 day there was no risk to the cash placed and no interest was lost on the overnight investment.

- On 9 April 2020 an investment of £5m was made with an A rated counterparty. The investment was due to mature on 10 August 2020, however the option to rollover the investment for a further six months was exercised. It only came to light that the rating of the counterparty had changed from A to A- after the decision to rollover the investment was taken, and it could not be revoked. In accordance with the council's treasury management strategy for 2020/21 the maximum value of investments which can be held with an A rated counterparty is £12.5m and an A- counterparty is £2.5m. The investment limit for this counterparty has thus been exceeded by £2.5m for a six month period, albeit the risk associated with this is considered to be very low. The internal checklist that is used by Finance officers when assessing potential investments has since been expanded and improved in order to avoid any repeat of this issue arising in the future.

7.4 Notwithstanding the historically low Bank of England base rate and the council's cautious and controlled approach to lending, a rate of return for the period 1 April 2020 to 30 September 2020 was achieved, as follows:

Table 5

Average Daily Investment Exposure £m	Angus Council Rate of Return %	6 Month Benchmark Return %	Internally Set Investment Rate Target %
89.789	0.62	0.21	0.95

7.5 The benchmark included above represents the six month London Interbank Bid (LIBID) rate as at 30 September 2020. It can be seen from the above table that the Angus Council rate of return is 0.41 per cent higher than the LIBID benchmark and 0.33 per cent lower than the internally set local investment rate target of 0.95 per cent as set out in the annual strategy (which was set prior to the onset of COVID-19 and the related impact ono investment rates.

7.6 Given the current risk environment and the fact that increases in bank rate are unlikely to occur before the end of the current forecast horizon of 31 March 2023, investment returns are expected to remain low.

8. Debt Rescheduling

8.1 No debt rescheduling was undertaken during the first six months of 2020/21 as the opportunity to reschedule debt has been limited in the current economic climate. This situation is expected to continue for the foreseeable future.

9. Variations from Agreed Policies and Practices

9.1 The Treasury Management Strategy Statement for 2020/21 was approved by Angus Council on 19 March 2020 (report 72/20 refers). No adjustments to the strategy were made when the Treasury Management Annual Report for 2019/20 was presented to Angus Council on 5 November 2020 (report 231/20 refers) and the Director of Finance is not recommending any changes at this time.

9.2 There were also no variations from agreed policies or practices to report during the period 1 April 2020 to 30 September 2020.

10. Compliance with Treasury and Prudential Limits

10.1 It is a statutory duty for the council to determine and keep under review affordable borrowing limits. The council's approved Prudential Indicators are outlined in the 2020/21 Treasury Management Strategy Statement and detailed in the Setting of Prudential Indicators for 2020/21 Budget Process committee report (report number 90/20 to the Special Budget Meeting of Angus Council on 27 February 2020).

10.2 During the first six months of the 2020/21 financial year the council has operated within the treasury limits and Prudential Indicators set out in the council's 2020/21 Treasury Management Strategy Statement and in compliance with the council's Treasury Management Practices.