AGENDA ITEM NO 9

REPORT NO 391/21

ANGUS COUNCIL

ANGUS COUNCIL - 16 DECEMBER 2021

TREASURY MANAGEMENT 2021/22 MID-YEAR REVIEW

REPORT BY THE DIRECTOR OF FINANCE

ABSTRACT
This report reviews Angus Council's treasury management arrangements, activity and performance for the period 1 April 2021 to 30 September 2021.

1. RECOMMENDATION

1.1 It is recommended that the council:

(i) review and scrutinise the treasury management activities for the period 1 April 2021 to 30 September 2021, as attached at **Appendix 1**; and
(ii) approve the proposed revisions to the counterparty limits detailed in section 5.2 of this report.

2. ALIGNMENT TO THE COUNCIL 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 2021/22, report 101/21 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 2021/22 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 2021 to 30 September 2021 (as attached at **Appendix 1**), thereby ensuring compliance with the aforementioned CIPFA Codes of Practice.

4. TREASURY MANAGEMENT MID-YEAR REPORT

Economic Climate

4.1 The first 6 months of 2021/22 saw businesses and economies begin the long recovery from the COVID-19 pandemic. This recovery is being adversely affected by the disruption within worldwide supply chains, labour shortages and increased prices of shipping, materials and energy. It is expected that these issues will eventually ease, but they are currently contributing to an upwards spike in inflation.

4.2 Interest rates have remained low during this time which, from a treasury viewpoint, is both good and bad. Good in so far as the cost of borrowing is low but, more noteworthy for the Council, bad in terms of the return available on the investment of temporary cash balances. Angus Council has experienced high levels of temporary cash balances over recent years, latterly due to the slowdown of the capital programme during the pandemic coupled with high levels of COVID-related grant provided by the Scottish Government which will be spent over the short and medium term. This has made it difficult to justify incurring any borrowing over the first 6 months of 2021/22 even with borrowing rates at low levels. This is however being kept under close review given the Council's underlying need to borrow to finance its capital expenditure plans.

Loans Fund Review

4.3 Whilst the Council's treasury advisors (Link Asset Services) have concluded their review of the council's Loans Fund and provided a draft report, the application of the review findings (in particular the phasing of the savings) was deferred, as agreed through the 2021/22 budget setting on 4 March 2021 (report 76/21 refers). Link Asset Services are currently updating their report findings to reflect the loans fund activitiy in 2020/21. The outcome of this review is to be the subject of a separate report intended to be brought to Council early in 2022.

5 PROPOSED AMENDMENTS TO COUNTERPARTY LIMITS

5.1 The ongoing unprecedented level of temporary cash balances the Council is holding has necessitated a review of counterparty investment limits to ensure there is sufficient flexibility to place funds with a diverse range of institutions. There are also opportunities being missed because the current counterparty lending limits were originally set some years ago when the levels of temporary cash balances held were significantly lower. In short the investment limits agreed by Council in the 2021/22 Treasury Management Strategy in March 2021 are proving too restrictive in practice during a period when the Council's temporary cash balances are unusually high due to the effects of the pandemic.

5.2 A small number of adjustments to existing limits are therefore proposed to ensure the Council can meet its treasury management objectives. The following table details the revised limits compared with those currently in place which were approved through the 2021/22 Treasury Management Strategy Statement (report 101/21). Only those elements where a change is proposed are shown.

Long Term Fitch Rating / Institution type	**Proposed New Maximum Value of Investment per Institution £ million**	**Current Maximum Value of Investment per Institution (per report 101/21) £ million**
A minus (UK Domiciled)	£5.0	£2.5
A / A plus (UK Domiciled)	£15.0	£12.5
A / A plus (Non-UK Domiciled)#	£5.0	n/a
AA minus or greater (UK Domiciled)	£20.0	£15.0
AA minus or greater (Non-UK Domiciled)	£15.0 (£30.0 in total)	£10.0 (£20.0 in total)
UK Nationalised Banks	£20.0	£15.0
Clydesdale Bank *	£25.0	£20.0
Money Market Funds	£15.0 (£30.0 in total)	£10.0 (£20.0 in total)

- this is a new category being proposed in this report to provide additional flexibility
*The Clydesdale Bank is the council's own bank and the limit is maintained at such a level for operational reasons.

5.3 The council's investment priorities will continue to be security, liquidity and return in that order and the proposed new limits will be applied in accordance with Link Asset Services counterparty credit ratings which are provided on a weekly basis. It is not considered that the changes outlined above increase the Council's risk exposure but rather provide greater flexibility for officers in placing investments in a diversified manner. The above changes aren't considered to be permanent and will be re-assessed as part of preparing the 2022/23 Treasury Management Strategy.

6. FINANCIAL IMPLICATIONS

6.1 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.

7. RISK IMPLICATIONS

7.1 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.

8. EQUALITY IMPACT ASSESSMENT

8.1 An Equality Impact Assessment is not required.

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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 2021 to 30 September 2021

Appendix 1

Treasury Management Mid-Year Review for the Period 1 April 2021 to 30 September 2021

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 2021 (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 2021 (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 2021/22 Treasury Management Strategy Statement (TMSS) was approved by this council on 18 March 2021 (report 101/21 refers). There are no policy amendments required to the TMSS based on the latest economic position or budgetary changes already approved but some revisions to investment limits are proposed (see Section 5 of covering report).

2. Borrowing Position as at 30 September 2021

2.1 The council's gross and net external debt positions as at 30 September 2021 are shown in Table 1 below. The gross and net external debt positions as at 1 April 2021 are also shown for comparative purposes.

Table 1

External Debt	Position as at 30 September 2021 £m	Position as at 1 April 2021 £m
Fixed Rate Borrowing – PWLB *	109.173	111.094
Fixed Rate Borrowing – LOBO **	16.000	16.000
Fixed Rate Borrowing – Market ***	14.000	14.000
Total External Debt	**139.173**	141.094
Investments	(89.565)	(87.471)
Total Net External Debt	49.608	53.623

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 2021 the CFR was projected to be £164.474m (that is to say the projected value of our external debt requirements at 30 September 2021).

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 2021 of £25.301m (CFR of £164.474m less gross debt of £139.173m per Table 1). 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 2021 to 30 September 2021. 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 a steady rise 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 The Director of Finance will closely monitor borrowing opportunities over the remainder of the financial year. Further borrowing may be undertaken should prevailing economic and market conditions move to the advantage of the council or should the current approach of deferring borrowing in the short term be put under threat by rising interest rates. 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.

4.5 As has happened 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.

4.6 In accordance with the 2021/22 Treasury Management Strategy Statement, the council has not borrowed in advance of need during the first half of the 2021/22 financial year and has no intention to borrow in advance for the remainder of the 2021/22 financial year.

5. Long Term Borrowing Repaid

5.1 The council has repaid £1.921m of PWLB loans that naturally matured in the period 1 April 2021 to 30 September 2021, the details of which are shown in Table 2 below:

Table 2

Date Advanced	Date Repaid	Amount £m	Rate %
14/04/89	15/05/21	0.296	9.375
07/06/12	07/06/21	1.000	2.410
22/02/82	30/09/21	0.625	15.000
Totals		1.921	

5.2 A further £0.526m of PWLB loans (at interest rates of 11.750 per cent and 13.625 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 2021 to 30 September 2021 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	1.05	1.42	1.16
10 years	1.39	1.81	1.60
25 years	1.75	2.27	2.02
50 years	1.49	2.06	1.81

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 21 %	Mar 22 %	Jun 22 %	Sep 22 %	Dec 22 %	Mar 23 %	Jun 23 %	Sep 23 %
Bank Rate	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75
5 Year	1.50	1.50	1.60	1.60	1.70	1.70	1.70	1.80
10 Year	1.80	1.90	1.90	2.00	2.00	2.10	2.10	2.20
25 Year	2.10	2.20	2.30	2.40	2.40	2.40	2.50	2.50
50 Year	1.90	2.00	2.10	2.20	2.20	2.20	2.30	2.30

7. Investment Position at 30 September 2021

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 2021/22 was £90.125m. 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 continued to experience unprecedented levels of cash balances during the six months to 30 September 2021, in part due to the timing and phasing of grant income to deal with the pandemic, received towards the very end of 2020/21 and carried forward to be utilised in the current financial year. The capital programme is still subject to a degree of constriction due to shortages of labour and materials and although much improved on 2020/21 levels payments to suppliers have yet to fully recover to pre-pandemic levels.

7.4 Notwithstanding the historically low Bank of England base rate (which remained at 0.10% throughout) and the council's cautious and controlled approach to lending, a rate of return for the period 1 April 2021 to 30 September 2021 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 %
90.125	0.22	-0.02	0.20

7.5 The benchmark included above represents the six month London Interbank Bid (LIBID) rate as at 30 September 2021. It can be seen from the above table that the Angus Council rate of return is 0.22 per cent higher than the LIBID benchmark and 0.02 per cent higher than the internally set local investment rate target of 0.20 per cent as set out in the annual strategy.

8. Debt Rescheduling

8.1 No debt rescheduling was undertaken during the first six months of 2021/22 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 2021/22 was approved by Angus Council on 18 March 2021 (report 101/21 refers). No adjustments to the strategy were made when the Treasury Management Annual Report for 2020/21 was presented to the Scrutiny & Audit Committee on 30 November 2021 (report 373/21 refers).

Australia & New Zealand Banking Group

9.2 During the 6 months to 30 September 2021 a total of £12.5m was placed on deposit with the Australia and New Zealand Banking Group Limited (ANZ). The banking group is domiciled in Australia and has a current credit rating of A plus. The council's Treasury Management Strategy Statement (report 101/21) only permits investments with A plus counterparties (up to a maximum of £12.5m) if they are domiciled in the UK. Non-UK domiciled counterparties are permitted if they have a credit rating of AA minus or above, with a maximum investment level of £10.0m per institution.

9.3 The following table is an extract from report 101/21 for information, showing the credit rating and associated investment limit.

Long Term Fitch Rating / Institution type	Maximum Value of Investment per Institution £ million
A minus	£2.5
A / A plus	£12.5
AA minus or greater (UK Domiciled)	£15.0
AA minus or greater (Non-UK Domiciled)	£10.0 (£20.0 in total)

9.4 Based on the above credit ratings and associated limits, no funds should have been placed with ANZ. A review of procedures to establish how the error arose has determined:

- The credit rating for ANZ changed from AA minus to A plus in April 2020 and this was updated in Treasury Live, the council's treasury management system. However, the permitted investment limit was amended on the system from £10.0m to £12.5m instead of £nil. The data contained in Treasury Live was thereafter used as the basis for investment decisions concerning ANZ.
- The presentation of the counterparty credit ratings and investment limits in the Treasury Management Strategy Statement was open to misinterpretation as it does not clearly distinguish between UK domiciled and non-UK domiciled institutions for A minus, A and A plus rated counterparties.

9.5 To prevent such a breach occurring in the future, it is intended that the A minus, A and A plus counterparty investment limits in the 2022/23 Treasury Management Strategy Statement will be amended to make clearer that these may be used for UK domiciled banks only. The following process for updating Treasury Live has also been adopted with immediate effect:

- A log has been created to record any amendments to counterparty ratings / limits which are notified by email from our treasury management advisors, Link Asset Services.
- Once Treasury Live has been updated this will be reflected in the log and verified by another member of the treasury team, who will check the information has been properly interpreted and recorded.
- The log will be signed and dated by both the amender and verifier.

9.6 The first tranche of the ANZ deposit (£5m) was returned on 18 November 2021 with the final tranche due back on 10 August 2022. It should be noted that the investments with ANZ have always remained within the maximum length of term recommended by Link and at no time have the council's funds been at risk of loss.

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 2021/22 Treasury Management Strategy Statement and detailed in the Setting of Prudential Indicators for 2021/22 Budget Process committee report (report number 77/21 to the Special Budget Meeting of Angus Council on 4 March 2021).

10.2 During the first six months of the 2021/22 financial year the council has operated within the treasury limits and Prudential Indicators set out in the council's 2021/22 Treasury Management Strategy Statement and in compliance with the council's Treasury Management Practices.