Report to Council

Treasury Management Review 2019/20

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9 September 2020

Reason for Decision

The Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2019/20. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

During 2019/20 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (approved 27 February 2019)
- a mid-year (minimum) treasury update report (approved 8 January 2020)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

The regulatory environment places responsibility on Members for the review and scrutiny of treasury management policy and activities. This report is therefore important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

The Council confirms that it has complied with the requirements under the Code to give prior scrutiny to the treasury strategy and the mid-year update. The Audit Committee is charged with the scrutiny of treasury management activities in Oldham and reviewed the content of this annual report at its meeting of 21 July 2020 and commended the report to Cabinet. The report was considered by Cabinet at its meeting on 24 August

2020 and commended to Council. Approval of the report by Council will to ensure full compliance with the Code for 2019/20.

Executive Summary

During 2019/20, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

Actual prudential and treasury indicators	2018/19 Actual £'000	2019/20 Revised £'000	2019/20 Actual £'000
Actual capital expenditure	48,564	63,945	54,383
Total Capital Financing Requirement:	493,880	491,011	472,377
Gross borrowing	147,846	167,843	167,843
External debt	394,456	403,338	403,709
Investments			
· Longer than 1 year	15,000	15,000	15,000
· Under 1 year	69,900	52,000	103,120
· Total	**84,900**	**67,000**	**118,120**
Net Borrowing (Gross borrowing less investments)	**62,946**	**100,843**	**49,723**

As can be seen in the table above, actual capital expenditure was less than the revised budget estimate for 2019/20 presented within the 2020/21 Treasury Management Strategy report considered at the Council meeting of 26 February 2020. The outturn position was significantly less than the £84.332m original capital budget for 2019/20 as approved at Budget Council on 27 February 2019.

During the course of the year the Capital Programme saw substantial rephasing. A number of major schemes including a number of schools' schemes in the Children's Service Directorate were rephased. The Asset Management (Education) Essential Condition Works provision was realigned into future years to align with other works being undertaken at schools. Housing Revenue Account (HRA) schemes were re-phased into 2020/21 to align with the latest HRA Strategy. In addition, the 'Creating a Better Place' Strategy required a number of existing regeneration projects to be reviewed and rephased to align to the long-term vision of the strategy. Also, during the year, the Information Technology (IT) Capital Strategy, the Strategic Roadmap was reviewed. The outcome was a rephasing of resources to ensure that the Council's future IT offer takes account of new innovations in IT and creates efficiencies that will complement future ways of working.

Borrowing of £20m was undertaken during the year. Member training on treasury management issues was undertaken on 1 October 2019 in order to support Members and senior members of staff in their scrutiny role.

Other prudential and treasury indicators are to be found in the main body of this report.

The Director of Finance confirms that the statutory borrowing limit (the authorised limit) was not breached.

The financial year 2019/20 continued the challenging investment environment of previous years, namely low investment returns.

Recommendations

Council is recommended to:

1) Approve the actual 2019/20 prudential and treasury indicators presented in this report
2) Approve the annual treasury management report for 2019/20

Council **9 September 2020**

Treasury Management Review 2019/20

1 Background

1.1 The Council has adopted the Revised Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management 2017. The primary requirements of the code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's Treasury Management activities
- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives
- Receipt by the full Council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year
- Delegation by the Council of responsibilities for implementing and monitoring Treasury Management Policies and Practices and for the execution and administration of treasury management decisions. In Oldham, this responsibility is delegated to the Section 151 Officer (Director of Finance).
- Delegation by the Council of the role of scrutiny of the Treasury Management Strategy and policies to a specific named body. In Oldham, the delegated body is the Audit Committee.

Treasury management in this context is defined as:

"*The management of the local authority'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.* "

1.2 The report therefore summarises the following the:-

- Council's capital expenditure and financing during the year;
- Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
- Actual prudential and treasury indicators;
- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity; and
- Detailed investment activity

2 Current Position

2.1 The Council's Capital Expenditure and Financing during 2019/20

2.1.1 The Council incurs capital expenditure when it invests in or acquires long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- Financed by borrowing if insufficient immediate financing is available, or a decision is taken not to apply available resources, the capital expenditure gives rise to a borrowing need.

2.1.2 The actual capital expenditure forms one of the required prudential indicators (these indicators are all summarised in Appendix 1). The table below shows the actual level of capital expenditure and how this was financed. As can be seen in the table below, actual capital expenditure in 2019/20 was less than the revised budget estimate. The revised budget estimate is based on the month 8 2019/20 reported position to align with the Annual Treasury Management Strategy 2020/21 report, and not the latest reported position (March 2020). All prudential indicators in the 2019/20 strategy are based on this revised budget. Capital expenditure was less in year due to re-phasing of some IT projects, property related schemes, HRA schemes and education schemes that were expected to progress during the year. In addition, the 'Creating a Better Place' Strategy required a number of existing regeneration projects to be reviewed and rephased to align to the long-term vision of the strategy.

	2018/19 Actual £'000	2019/20 Revised £'000	2019/20 Actual £'000
Non-HRA capital expenditure	46,318	62,091	52,249
HRA capital expenditure	2,246	1,854	2,134
Total capital expenditure	**48,564**	**63,945**	**54,383**
Resourced by:			
• Capital receipts	14,919	13,143	9,914
• Capital grants	25,522	29,975	42,091
• HRA	851	6	2,134
• Revenue	7,272	1,854	244
Unfinanced capital expenditure	**0**	**18,967**	**0**

2.2 **The Council's Overall Borrowing Need**

2.2.1 The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2019/20 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

2.2.2 Part of the Council's treasury activity is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies (such as the Government, through the Public Works Loan Board [PWLB] or the money markets) or utilising temporary cash resources within the Council.

Reducing the CFR

2.2.3 The Council's (non-Housing Revenue Account [HRA]) underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision (MRP), to reduce the CFR. This is effectively a repayment of the non- HRA borrowing need (there is no statutory requirement to reduce the HRA CFR). This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

2.2.4 The total CFR can also be reduced by:

- The application of additional capital financing resources (such as unapplied capital receipts); or
- Charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

2.2.5 The Council's 2019/20 MRP Policy (as required by CLG Guidance) was approved as part of the Treasury Management Strategy report for 2019/20 on 27 February 2019.

2.2.6 The Council's CFR for the year is shown in the table below and represents a key prudential indicator. It includes PFI and leasing schemes on the balance sheet, which increase the Council's borrowing need. In 2019/20 the Council had seven PFI schemes in operation; however, no borrowing is actually required against these schemes as a borrowing facility is included within each contract.

Capital Financing Requirement	2018/19 Actual £'000	2019/20 Revised £'000	2019/20 Actual £'000
Opening balance	505,049	493,880	493,880
Add unfinanced capital expenditure	0	18,967	0
Add adjustment for the inclusion of on-balance sheet PFI and leasing schemes (if applicable)	450	0	525
Less MRP/VRP*	(2,944)	(2,742)	(2,742)
Less PFI & finance lease repayments	(8,675)	(19,094)	(19,286)
Closing balance	493,880	491,011	472,377

* Includes voluntary application of capital receipts and revenue resources

2.2.7 Borrowing activity is constrained by prudential indicators for net borrowing, the CFR and by the authorised limit.

Gross borrowing and the CFR

2.2.8 In order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2019/20) plus the estimates of any additional capital financing requirement for the current (2020/21) and next two financial years.

2.2.9 This essentially means that the Council is not borrowing to support revenue expenditure.

2.2.10 This indicator allowed the Council some flexibility to borrow in advance of its immediate capital needs in 2019/20 if so required. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	2018/19 Actual £'000	2019/20 Revised £'000	2019/20 Actual £'000
Gross borrowing position	394,456	403,338	403,709
CFR - including PFI / Finance Leases	493,880	491,011	472,377
Under / (Over) funding of the CFR	99,424	87,673	68,668

The table above shows the position as at 31 March 2020 for the Council's gross borrowing position and CFR. This shows, compared to the revised budget position:

- Movement in the gross borrowing position, reflecting the fact that additional borrowing of £20m of long term borrowing had been taken out during the year which has been offset by repayment of transferred debt, PFI and finance leases.

- A reduction in the CFR, predominantly due to the slippage in the capital programme and financing of capital through revenue resources.

The Authorised Limit

2.2.11 The authorised limit is the “affordable borrowing limit” required by Section 3 of the Local Government Act 2003 and was set at £512m. Once this has been set, the Council does not have the power to borrow above this level.

The Operational Boundary

2.2.12 The operational boundary is the expected borrowing position of the Council during the year and was set at £495m. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

	2019/20 Actual £'000
Authorised Limit	512,000
Operational Boundary	495,000

Actual financing costs as a proportion of net revenue stream

2.2.13 This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream and is within expected levels.

	2019/20 Actual £'000
External Debt	167,843
PFI / Finance leases	235,867
Actual External Debt (Gross Borrowing) (rounded)	**403,710**
Financing costs as a proportion of net revenue stream (General Fund)	13.41%

2.2.14 The table above splits the gross borrowing position of the Council between actual external debt (loans) and PFI / Finance lease debt. As can be seen above the gross borrowing position is well within the Authorised Limit and Operational Boundary. The difference between the two reflects the Council’s under borrowed position.

2.3 **The Council's Debt and Investment Position**

2.3.1 The Council's debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through Member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices.

2.3.2 At the end of 2019/20 the Council's treasury position was as follows:

	31 March 2019 Principal £'000	Average Rate/ Return	Average Life years	31 March 2020 Principal £'000	Average Rate/ Return	Average Life years
Fixed rate funding:						
-PWLB	15,482			35,482		
-Stock	6,600			6,600		
Market	125,764			125,761		
Total borrowings	**147,846**	4.50%	35.42	**167,843**	4.30%	37.08
PFI & Finance lease liabilities	**246,610**			**235,867**		
Total External debt	**394,456**			**403,710**		
CFR	**493,880**			**472,377**		
Over/ (under) borrowing	**(99,424)**			**(68,667)**		
Investments:						
Financial Institutions/LA's	69,900	0.76%		103,120	0.94%	
Property	15,000	4.36%		15,000	4.32%	
Total investments	**84,900**			**118,120**		
Net Debt	**62,946**			**49,723**		

2.3.3 The maturity structure of the debt portfolio was as follows:

	2018/19 Actual %	Upper Limit %	Lower Limit %	2019/20 Actual %
Under 12 months	30%	40%	0%	23%
12 months and within 24 months	0%	40%	0%	0%
24 months and within 5 years	33%	40%	0%	32%
5 years and within 10 years	5%	40%	0%	4%
10 years and above	32%	50%	40%	40%

2.3.4 The investment portfolio and maturity structure was as follows:

Investment Portfolio	Actual 31 March 2019 £'000	Actual 31 March 2019 %	Actual 31 March 2020 £'000	Actual 31 March 2020 %
Treasury Investments				
Banks	13,000	15.31%	37,500	31.75%
Local Authorities / Public Bodies	30,500	35.92%	28,500	24.13%
Money Market Funds (MMF's)	26,400	31.10%	37,120	31.43%
Total managed in house	**69,900**	**82.33%**	**103,120**	**87.30%**
Bond Funds				
Property Funds	15,000	17.67%	15,000	12.70%
Cash Fund Managers				
Total Managed Externally	**15,000**	**17.67%**	**15,000**	**12.70%**
TOTAL TREASURY INVESTMENTS	**84,900**	**100%**	**118,120**	**100%**
TOTAL NON TREASURY INVESTMENTS *	0	0%	2,181	110%

* Members should note that the Non-Treasury Investments during 2019/20 related to property purchase.

	2018/19 Actual £'000	2019/20 Actual £'000
Investments		
Longer than 1 year	0	0
Under 1 year	69,900	103,120
Property Fund	15,000	15,000
Total	**84,900**	**118,120**

2.3.5 Key features of the debt and investment position are:

a) Over the course of the year 2019/20, investments have increased by £33.220m. The large increase in investments related to borrowing completed during the year in line with the Council's Treasury Management Strategy, additional Government grants received in March 2020 to tackle the COVID-19 crisis together with the upfront payment for Grant in Lieu of Business Rates for 2020/21 that was also received in March 2020.

b) The average rate of return on investments with Financial Institutions increased from 0.76% in 2018/19 to 0.94% in 2019/20. This increase relates to the Bank of England base rate being at 0.75% for the majority of the year before it dropped to 0.10% in March 2020.

c) Investments were arranged throughout the year to ensure cash available to support the three-year up-front pension payment at the start of 2020/21.

2.4 Investment Strategy and control of interest rate risk

2.4.1 Investment returns remained low during 2019/20. The expectation for interest rates within the treasury management strategy for 2019/20 was that Bank Rate would stay at 0.75% during 2019/20 as it was not expected that the Monetary Policy Committee (MPC) would be able to deliver on an increase in Bank Rate until Brexit was finally settled. However, there was an expectation that Bank Rate would rise thereafter but would only rise to 1.0% during 2020.

2.4.2 Rising concerns over the possibility that the UK could leave the EU at the end of October 2019 caused longer term investment rates to be on a falling trend for most of April to September. They then rose after the end of October deadline was rejected by MPs but fell back again in early January 2020 before recovering again after the 31 January 2020 departure of the UK from the EU.

2.4.3 When the coronavirus outbreak hit the UK in February/March, rates initially plunged but then rose sharply back up again due to a shortage of liquidity in financial markets. As longer term rates were significantly higher than shorter term rates during the year, value was therefore sought by placing longer term investments where cash balances were sufficient to allow this.

2.4.4 While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the financial crisis. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

2.4.5 The table below shows the interest rate forecast as at mid-year of 2019-20:

Link Asset Services Interest Rate View 11.11.19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25	1.25	1.25	1.25
3 Month LIBID	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.30	1.30
6 Month LIBID	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40	1.50	1.50	1.50	1.50
12 Month LIBID	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60	1.70	1.70	1.70	1.70
5yr PWLB Rate	2.40	2.40	2.50	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.10	3.20	3.20
10yr PWLB Rate	2.70	2.70	2.70	2.80	2.90	3.00	3.10	3.20	3.20	3.30	3.30	3.40	3.50
25yr PWLB Rate	3.30	3.40	3.40	3.50	3.60	3.70	3.70	3.80	3.90	4.00	4.00	4.10	4.10
50yr PWLB Rate	3.20	3.30	3.30	3.40	3.50	3.60	3.60	3.70	3.80	3.90	3.90	4.00	4.00

2.5 Borrowing Strategy and control of interest rate risk

2.5.1 During 2019/20, the Council maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow was used as an interim measure. This strategy was prudent as investment returns were low and minimising counterparty risk on placing investments also needed to be considered.

2.5.2 The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years. However, this was kept under review to avoid incurring higher borrowing costs in the future when the Authority may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

2.5.3 Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. The Treasury Management Team and the Director of Finance therefore monitored interest rates in financial markets and adopted a pragmatic strategy based upon the following principles to manage interest rate risks

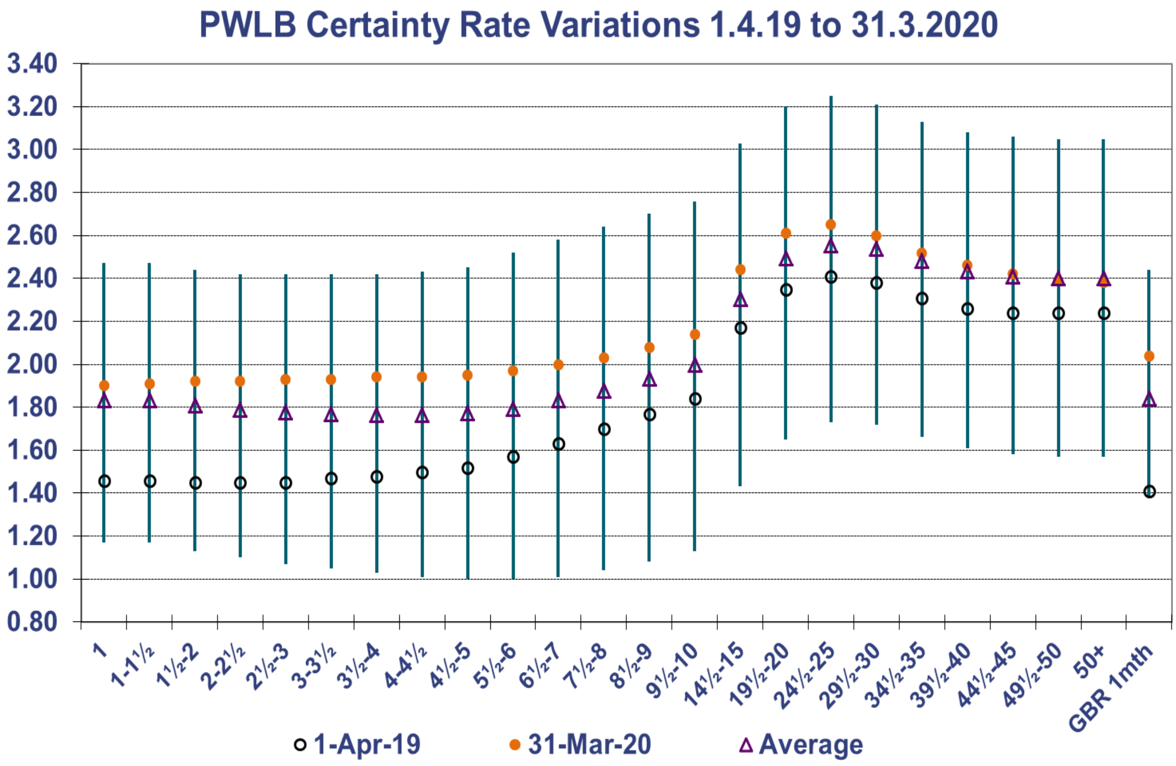
- if it had been felt that there was a significant risk of a sharp **fall** in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings would have been postponed, and potential rescheduling from fixed rate funding into short term borrowing would have been considered.
- if it had been felt that there was a significant risk of a much sharper **rise** in long and short term rates than initially expected, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would have been re-appraised. Most likely, fixed rate funding would have been drawn whilst interest rates were lower than they were projected to be in the next few years.

2.5.4 Interest rate forecasts expected only gradual rises in medium and longer term fixed borrowing rates during 2019/20 and the two subsequent financial years. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period.

2.5.5 The information below and in graphs and tables in Appendices 2 and 3 show PWLB rates for a selection of maturity periods, the average borrowing rates, the high and low points in rates, spreads and individual rates at the start and the end of the financial year:

- 5 year PWLB rate - started the year at 1.52%, falling to a low for the year at 1.00% in August 2019, peaking at 2.45% in March 2020 and finishing the year at 1.95%.

- 10 year PWLB rate - started the year at 1.84%, falling to a low for the year at 1.13% in September 2019, peaking at 2.76% in March 2020 and finishing the year at 2.14%.
- 25 year PWLB rate - started the year at 2.41%, falling to a low for the year at 1.73% in September 2019, peaking at 3.25% in March 2019 and finishing the year at 2.65%.
- 50 year PWLB rate. - started the year at 2.24%, falling to a low for the year at 1.57% in September 2019, peaking at 3.05% in December 2019 and finishing the year at 2.39%.



2.5.6 PWLB rates are based on, and are determined by, gilt (UK Government bonds) yields through H.M. Treasury determining a specified margin to add to gilt yields.

2.5.7 There was much speculation during the second half of 2019 that bond markets were in a bubble which was driving bond prices up and yields down to historically very low levels. The context for that was heightened expectations that the US could have been heading for a recession in 2020, and a general background of a downturn in world economic growth, especially due to fears around the impact of the trade war between the US and China, together with inflation generally at low levels in most countries and expected to remain subdued; these conditions were conducive to very low bond yields.

2.5.8 While inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation expectations, the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc.

2.5.9 This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years. We have therefore seen, over the last year, many bond yields up to 10 years in the Eurozone turn negative. In addition, there has, at times, been an inversion of bond yields in the US whereby 10 year yields have fallen below shorter term yields. In the past, this has been a precursor of a recession. The other side of this coin is that bond prices are elevated as investors would be expected to be moving out of riskier assets i.e. shares, in anticipation of a downturn in corporate earnings and so selling out of equities.

2.5.10 Gilt yields were on a generally falling trend during the last year up until the coronavirus crisis hit western economies. Since then, gilt yields have fallen sharply to unprecedented lows as investors have panicked in selling shares in anticipation of impending recessions in western economies and moved cash into safe haven assets i.e. government bonds.

2.5.11 Major western central banks also started quantitative easing purchases of government bonds which will act to maintain downward pressure on government bond yields at a time when there is going to be a huge and quick expansion of Government expenditure financed by issuing Government bonds; (this would normally cause bond yields to rise). At the close of the day on 31 March, all gilt yields from 1 to 5 years were between 0.12 – 0.20% while even 25-year yields were at only 0.83%.

2.5.12 However, HM Treasury has imposed two changes in the margins over gilt yields for PWLB rates in 2019/20 without any prior warning. The first on 9 October 2019, added an additional 1% margin over gilts to all PWLB rates. That increase was then partially reversed for some forms of borrowing on 11 March 2020, at the same time as the Government announced in the Budget a programme of increased spending on infrastructure expenditure. It also announced that there would be a consultation with Local Authorities on possibly further amending these margins. The consultation concluded at the end of July 2020 (the Council submitted a response). It is clear that the Treasury intends to put a stop to Local Authorities borrowing money from the PWLB for commercial activity if the aim is solely to generate an income stream.

2.5.13 Following the changes on 11 March 2020 in margins over gilt yields, the current situation is as follows: -

- **PWLB Standard Rate** is gilt plus 200 basis points (G+200bps)
- **PWLB Certainty Rate** is gilt plus 180 basis points (G+180bps)
- **PWLB HRA Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB HRA Certainty Rate** is gilt plus 80bps (G+80bps)
- **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)

There is likely to be little upward movement in PWLB rates over the next two years as it will take national economies a prolonged period to recover all the momentum that they will lose in the sharp recession that will be caused during the coronavirus shut down period. Inflation is also likely to be very low during this period and could even turn negative in some major western economies during 2020/21.

2.6 Borrowing Outturn for 2019/20

Treasury Borrowing

2.6.1 The Council borrowed £20m from the PWLB in August 2019. The borrowing was undertaken when market rates reached the Council's internal trigger points. This ensured borrowing was undertaken at the optimum point to minimise future costs, securing good value for money.

Date	Lender	Principal £'000	Type	Interest Rate	Maturity (Years)
20-Aug-19	PWLB	10,000	Maturity	1.720%	50
20-Aug-19	PWLB	5,000	Maturity	1.810%	30
20-Aug-19	PWLB	5,000	Maturity	1.740%	20
Total		**20,000**			

Debt Rescheduling

2.6.2 No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

Repayment of Debt

2.6.3 In March 2020 £3k was repaid in relation to Charitable Investments that the Council held.

2.7 Investment Outturn

Investment Policy

2.7.1 The Council's investment policy is governed by Ministry of Housing, Communities and Local Government (MHCLG) investment guidance, which has been implemented in the annual investment strategy which for 2019/20 was approved by Council on 27 February 2019. This policy sets out the approach for choosing investment counterparties and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

2.7.2 The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Resources

2.7.3 The Council's cash balances comprise revenue and capital resources and cash flow monies. The Council's core cash resources comprised as follows:

Balance Sheet Resources	31 March 2019 (£'000)	31 March 2020 (£'000)
Balances General Fund	14,840	15,110
Balances HRA	21,305	21,796
Earmarked Reserves	80,623	79,360
Provisions	29,251	28,367
Usable Capital Receipts	0	0
Total	**146,019**	**144,633**

Investments at 31 March 2020

2.7.4 The Council managed all of its investments in house with the institutions listed in the Council's approved lending list. At the end of the financial year the Council had £118.120m of investments as follows:

Institution	Type	Amount £'000	Term (days)	Rate %	Start date	End date
CCLA Property	Property	15,000		4.36%		
Total Property		**15,000**				
Goldman Sachs	Fixed	2,000	183	0.90%	03-Oct-19	03-Apr-20
Goldman Sachs	Fixed	3,000	179	0.90%	07-Oct-19	03-Apr-20
Thurrock Council	Fixed	2,500	193	0.76%	26-Sep-19	06-Apr-20
Thurrock Council	Fixed	2,500	87	0.80%	10-Jan-19	06-Apr-20
Ashford Borough Council	Fixed	5,000	54	0.82%	12-Feb-20	06-Apr-20
Eastleigh Borough Council	Fixed	5,000	49	0.73%	17-Feb-20	06-Apr-20
Slough Borough Council	Fixed	3,000	31	1.20%	06-Mar-20	06-Apr-20
Surrey County Council	Fixed	5,000	61	1.05%	27-Mar-20	27-May-20
Thurrock Council	Fixed	2,500	59	1.00%	31-Mar-20	29-May-20
North Lincolnshire Council	Fixed	3,000	184	1.15%	25-Mar-20	25-Sep-20
Total Fixed Deposits		**33,500**				
Standard Chartered	CD*	5,000	182	0.88%	04-Oct-19	03-Aor-20
Standard Chartered	CD	5,000	182	0.92%	05-Nov-19	05-May-20
Total Fixed Deposits		**10,000**				
Bank of Scotland	Notice	2,500	32	0.90%	21-Jun-19	
Bank of Scotland	Notice	12,500	95	1.10%	07-May-19	
Santander	Notice	7,500	95	1.00%	01-Mar-19	
Total Notice Accounts		**22,500**				
Federated MMF**	MMF	17,120	1	0.72%	31-Mar-20	01-Apr-20
Aberdeen MMF	MMF	20,000	5	0.78%	27-Mar-20	01-Apr-20
Total Money Market Funds		**37,120**				
Total Investments		**118,120**				

* Certificate of Deposit (CD)
** Money Market Funds (MMF)

2.7.5 The Council's investment strategy was to maintain sufficient cash reserves to give it necessary liquidity, whilst trying to attain a benchmark average rate of return of London Interbank Bid Rate (LIBID) on the relevant time deposit multiplied by 5%, whilst ensuring funds were invested in institutions which were the most secure. The table below shows the returns by the relevant time period

	LIBID + 5%	Actual Return %
7 Day	0.56%	0.73%
1 Month	0.59%	0.89%
3 Month	0.67%	1.01%
6 Month	0.74%	0.89%
12 Month	0.84%	0.97%
Average		0.90%
Target	0.68%	

2.7.6 The Council's overall average performance on its cash investments exceeded its LIBID benchmark in all periods.

2.7.7 The investments held with the CCLA property fund generated £632k of income with an average return in year of 4.32%. Furthermore, the Director of Finance confirms that the approved limits within the Annual Investment Strategy were not breached during 2019/20.

2.8 The Economy and Interest Rates

UK – Brexit

2.8.1 The main issue in 2019 was the repeated debates in the House of Commons to agree on one way forward for the UK over the issue of Brexit. This resulted in the resignation of Teresa May as the leader of the Conservative minority Government and the election of Boris Johnson as the new leader, on a platform of taking the UK out of the EU on 31 October 2019.

2.8.2 A general election was called and held in December 2019 and resulted in a decisive victory for the Conservative Party. The main election promise of leaving the EU was then enabled so that the UK could leave the EU on 31 January 2020.

2.8.3 However, this still leaves much uncertainty as to whether there will be a reasonable trade deal achieved by the target deadline of the end of 2020. It is also unclear as to whether the coronavirus outbreak may yet impact on this deadline. The second and third rounds of negotiations have already had to be cancelled due to the virus.

Economic Growth

2.8.4 The year 2019 was very volatile with economic growth for quarter 1 unexpectedly strong at 0.5%, quarter 2 was reduced by -0.7 to -0.2%, quarter 3 bouncing back up to +0.5% and quarter 4 was 0.0%, leaving a year on year percentage of +1.1%.

2.8.5 The year 2020 started with optimistic business surveys pointing to an upswing in growth after the ending of political uncertainty as a result of the decisive result of the general election in December which settled the Brexit issue. However, the three monthly GDP statistics in January were disappointing, being stuck at 0.0% growth. Since then, the whole world and the way in which we now live has changed as a result of the coronavirus outbreak.

2.8.6 It now looks likely that the closedown of whole sections of the economy will result in a fall in GDP of at least 15% in quarter two. What is uncertain, however, is the extent of the damage that will be done to businesses by the end of the lock down period, whether there could be a second wave of the outbreak, how soon a vaccine will be created and then how quickly it can be administered to the population. This leaves huge uncertainties as to how quickly the economy will recover.

2.8.7 After the Monetary Policy Committee raised the Bank Rate from 0.5% to 0.75% in August 2018, Brexit uncertainty caused the MPC to access and monitor the situation until March 2020. At this point it was clear that the coronavirus outbreak posed a huge threat to the economy of the UK. Two emergency cuts in the Bank Rate from 0.75% occurred in March 2020, first to 0.25% and then to 0.10%.

2.8.8 These cuts were accompanied by an increase in Quantitative Easing (QE), essentially the purchases of gilts (mainly) by the Bank of England of £200bn. The Government and the Bank were also very concerned and moved to stop people losing their jobs during this lock down period.

2.8.9 Accordingly, the Government introduced various schemes to subsidise both employed and self-employed jobs for an initial three months which has been extended, while the country was in full lock down and now enters the recovery stage. It also put in place a raft of other measures to help businesses access loans from their banks, (with the Government providing guarantees to the banks against losses), to tide them over during the lock down period when some firms may have little or no income.

2.8.10 However, it must be noted that at the time of writing, this leaves open a question as to whether some firms will be solvent, even if they take out such loans, and some may also choose to close as there is, and will be, insufficient demand for their services. This is a rapidly evolving situation so there may be further measures to come from the Bank and the Government in the next few months and beyond.

2.8.11 The measures to support jobs and businesses already taken by the Government will result in a huge increase in the annual budget deficit in 2020/21 from 2% to nearly 11%.

2.8.12 The ratio of debt to GDP is also likely to increase from 80% to around 105%. In the next Budget. The Government also announced a large increase in spending on infrastructure; this will also help the economy to recover and the Country moves forward in the recovery stage. Provided the coronavirus outbreak is brought under control relatively swiftly, and the lock down is fully eased, then it is hoped that there would be a sharp recovery, but one that would take a prolonged time to fully recover previous lost momentum.

Inflation

2.8.13 Inflation has posed little concern for the MPC during the last year, being mainly between 1.5 – 2.0%. It is also not going to be an issue for the near future as the world economy will be heading into a recession which is already causing an excess in the supply of oil which has fallen sharply in price.

2.8.14 Other prices will also be under downward pressure while wage inflation has also been on a downward path over the last half year and is likely to continue that trend in the current environment. While inflation could even turn negative in the Eurozone, this is currently not likely in the UK.

Employment

2.8.15 Employment had been growing healthily through the last year, but was obviously heading for a major reduction at the end of 2019/20 due to coronavirus. The good news over the last year is that wage inflation has been significantly higher than Consumer Price Index (CPI) inflation which means that consumer real spending power had been increasing and so will have provided support to GDP growth. However, as people have not been able to leave their homes to do non-food shopping, retail sales have also been significantly reduced.

USA

2.8.16 Growth in quarter 1 of 2019 was strong at 3.1% but growth fell back to 2.0% in quarter 2 and 2.1% in quarters 3 and 4. The slowdown in economic growth resulted in the Federal Reserve (Fed) cutting rates from 2.25-2.50% by 0.25% in each of July, September and October. Once coronavirus started to impact the US, the Fed took decisive action by cutting rates twice by 0.50%, and then 1.00%, in March, all the way down to 0.00 – 0.25%. At the end of March, Congress agreed a $2trn stimulus package (worth about 10% of GDP) and new lending facilities announced by the Fed which could channel up to $6trn in temporary financing to consumers and firms over the coming months. Nearly half of the first figure is made up of permanent fiscal transfers to households and firms, including cash payments of $1,200 to individuals.

2.8.17 The loans for small businesses, which convert into grants if firms use them to maintain their payroll, will cost $367bn and 100% of the cost of lost wages for four months will also be covered. In addition, there will be $500bn of funding from the Treasury's Exchange Stabilization Fund which will provide loans for hard-hit industries, including $50bn for airlines.

2.8.18 However, all this will not stop the US falling into a sharp recession in quarter 2 of 2020; some estimates are that growth could fall by as much as 40%. The first two weeks in March initial jobless claims reached total of 10 million and increased even further by the end of March.

Eurozone (EZ)

2.8.19 The annual rate of GDP growth has been steadily falling, from 1.8% in 2018 to only 0.9% year on year in quarter 4 in 2019. The European Central Bank (ECB) ended its programme of quantitative easing purchases of debt in December 2018, which meant that the central banks in the US, UK and EU had all ended the phase of post financial crisis expansion of liquidity supporting world financial markets by purchases of debt.

2.8.20 However, the downturn in EZ growth, together with inflation falling well under the upper limit of its target range of 0 to 2%, (but it aims to keep it near to 2%), prompted the ECB to take new measures to stimulate growth.

2.8.21 At its March 2019 meeting it announced a third round of Targeted longer-term refinancing operations (TLTROs), this provided banks with cheap two year maturity borrowing every three months from September 2019 until March 2021. However, since then, the downturn in EZ and world growth has gathered momentum so at its meeting in September 2019, it cut its deposit rate further into negative territory, from -0.4% to -0.5% and announced a resumption of quantitative easing purchases of debt to start in November at €20bn per month (a relatively small amount), plus more TLTRO measures.

2.8.22 Once coronavirus started having a major impact in Europe, the ECB took action in March 2020 to expand its QE operations and other measures to help promote expansion of credit and economic growth. What is currently missing is a coordinated EU response of fiscal action by all national Governments to protect jobs, support businesses directly and promote economic growth by expanding government expenditure on e.g. infrastructure; action is therefore likely to be patchy.

China

2.8.23 Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium-term risks have also been increasing.

2.8.24 The major feature of 2019 was the trade war with the US. However, this has been eclipsed by China being the first country to be hit by the coronavirus outbreak. This resulted in a lock down of the country and a major contraction of economic activity in February-March 2020.

2.8.25 While it appears that China had managed to contain the virus by the end of March, it is clear that the economy is going to take some time to recover its previous rate of growth. Ongoing economic issues remain, in needing to make major progress to eliminate excess industrial capacity and to switch investment from property construction and infrastructure to consumer goods production. It also needs to address the level of non-performing loans in the banking and credit systems.

Japan

2.8.26 Japan has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy. It appears to have missed much of the domestic impact from coronavirus in 2019/20 financial year, however, the virus is at an early stage.

World Growth

2.8.27 The trade war between the US and China on tariffs was a major concern to financial markets and was depressing worldwide growth during 2019, as any downturn in China would spill over into impacting countries supplying raw materials to China.

2.8.28 Concerns were particularly focused on the synchronised general weakening of growth in the major economies of the world. These concerns resulted in Government bond yields in the developed world falling significantly during 2019. In 2020, coronavirus is the big issue which is sweeping around the world and having a major impact in causing a world recession in growth in 2020.

2.9 Other Key Issues

International Financial Reporting Standards (IFRS) 9 – Financial Instruments

2.9.1 Following the introduction of IFRS 9 in 2018/19 and after the consultation undertaken by the Ministry of Housing, Communities and Local Government (MHCLG) on IFRS9, the Government has introduced a mandatory statutory override for Local Authorities to reverse out all unrealised fair value movements resulting from pooled investment funds. This was effective from 1 April 2018 and applies for five years from this date. The Council has elected to utilise the mandatory override. The Council is required to disclose the net impact of the unrealised fair value movements in a separate unusable reserve throughout the duration of the override in order for the Government to keep the override under review and to maintain a form of transparency.

International Financial Reporting Standards (IFRS) 16 - Leases

2.9.2 IFRS 16 should have been introduced for Local Authorities from 1 April 2020 which meant that the annual accounts for 2020/21 were to be the first set of accounts produced in accordance with this standard. The Code of Practice on Local Authority Accounting requires the Council to disclose information relating to the impact of an accounting change required by a new standard that has been issued but not yet adopted by the 2019/20 Code as a note in the 2019/20 accounts. Therefore, the Treasury team have been looking at the impact of the standard on the Council's treasury indicators that would be included in the Treasury Management strategy 2020/21.

2.9.3 However, due to the Coronavirus and the additional pressure faced by Local Authorities in these unprecedented times, on 20 March 2020, the Financial Reporting Advisory Board (FRAB), announced the deferral of International Financial Reporting Standard 16 (IFRS 16) implementation to 2021/22.

Other Treasury Management Issues

2.9.4 The Council is currently involved in legal action against Barclays Bank with regards to certain Lender Option Borrower Option (LOBO) transactions. This is based on the Bank's involvement in manipulation of the LIBOR benchmark rate and the subsequent impact on the Council's financial position. This matter is on-going.

3 Options/Alternatives

3.1 In order that the Council complies with the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management the Council has no option other than to consider and approve the contents of the report. Therefore, no options/alternatives have been presented.

4 Preferred Option

4.1 The preferred option is that the contents of the report are agreed.

5 **Consultation**

5.1 There has been consultation with Link Asset Services, Treasury Management Advisors.

5.2 The presentation of the Treasury Management Review 2019/20 to the Audit Committee for detailed scrutiny on 21 July 2020 was the first stage in compliance with the requirements of the CIPFA Code of Practice. The Audit Committee commended the report to Cabinet, where it was considered at the meeting of 24 August 2020. Cabinet was content to commend the report to Council for approval to ensure full compliance with the Code for 2019/20.

6 **Financial Implications**

6.1 All included in the report.

7 **Legal Services Comments**

7.1 None

8 **Cooperative Agenda**

8.1 The treasury management strategy embraces the Council's cooperative agenda. The Council will develop its investment framework to ensure it complements the cooperative ethos of the Council.

9 **Human Resources Comments**

9.1 None

10 **Risk Assessments**

10.1 There are considerable risks to the security of the Authority's resources if appropriate treasury management strategies and policies are not adopted and followed. The Council has established good practice in relation to treasury management which has previously been acknowledged in Internal Audit reports and in the External Auditors' reports presented to the Audit Committee.

11 **IT Implications**

11.1 None

12 **Property Implications**

12.1 None

13 **Procurement Implications**

13.1 None

14 **Environmental and Health & Safety Implications**

14.1 None

15 **Equality, community cohesion and crime implications**

15.1 None

16 **Equality Impact Assessment Completed**

16.1 No

17 **Key Decision**

17.1 Yes

18 **Key Decision Reference**

18.1 FG-07-20.

19 **Background Papers**

19.1 The following is a list of background papers on which this report is based in accordance with the requirements of Section 100(1) of the Local Government Act 1972. It does not include documents which would disclose exempt or confidential information as defined by the Act:

File Ref:	Background papers are provided in Appendices 1, 2 and 3
Officer Name:	Lee Walsh
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20 **Appendices**

Appendix 1 Prudential and Treasury Management Indicators
Appendix 2 Graphs
Appendix 3 Borrowing and Investment Rates

Appendix 1: Prudential and Treasury Indicators

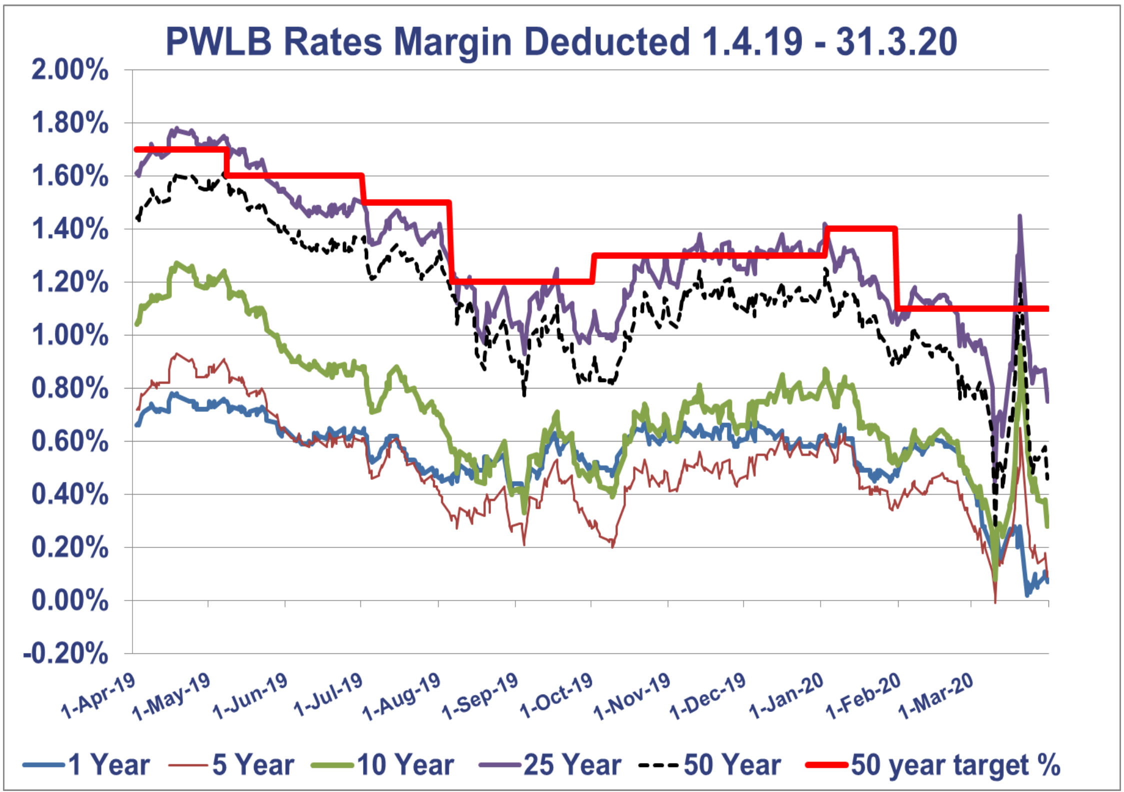
TABLE 1: Prudential indicators	2018/19	2019/20	2019/20	2019/20
	Outturn	Original	Revised	Outturn
	£'000	£'000	£'000	£'000
Capital Expenditure				
Non – HRA	46,318	80,097	62,091	52,249
HRA	2,246	4,235	1,854	2,134
TOTAL	48,564	84,352	63,945	54,383
Ratio of financing costs to net revenue stream				
Non – HRA	10.00%	%	%	13.41%
In year Capital Financing Requirement				
Non – HRA	(11,169)	31,125	(2,869)	(21,503)
TOTAL	(11,169)	31,125	(2,869)	(21,503)
Capital Financing Requirement as at 31 March	493,880	525,005	491,011	472,377

TABLE 2: Treasury management indicators	2018/19	2019/20	2019/20	2019/20
	Outturn	Original Budget	Revised	Outturn
	£'000	£'000	£'000	£'000
Authorised Limit for external debt				
Borrowing	305,000	305,000	272,000	272,000
Other long term liabilities	285,000	240,000	240,000	240,000
TOTAL	**590,000**	**545,000**	**512,000**	**512,000**
Operational Boundary for external debt -				
Borrowing	285,000	290,000	260,000	260,000
Other long term liabilities	275,000	235,000	235,000	235,000
TOTAL	**560,000**	**525,000**	**495,000**	**495,000**
Actual external debt	394,456			403,709
Upper limit for fixed interest rate exposure				
Net principal re fixed rate borrowing / investments	100%	100%	100%	100%
Actual	100%			100%
Upper limit for variable rate exposure				
Net principal re variable rate borrowing / investments	40%	40%	40%	40%
Actual	0%			0%
Upper limit for total principal sums invested for over 364 days	50,000	50,000	50,000	50,000

Maturity structure of fixed rate borrowing during 2019/20	Upper Limit	Lower Limit	Actual
Under 12 months	40%	0%	23%
12 months and within 24 months	40%	0%	0%
24 months and within 5 years	40%	0%	32%
5 years and within 10 years	40%	0%	4%
10 years and above	50%	40%	40%

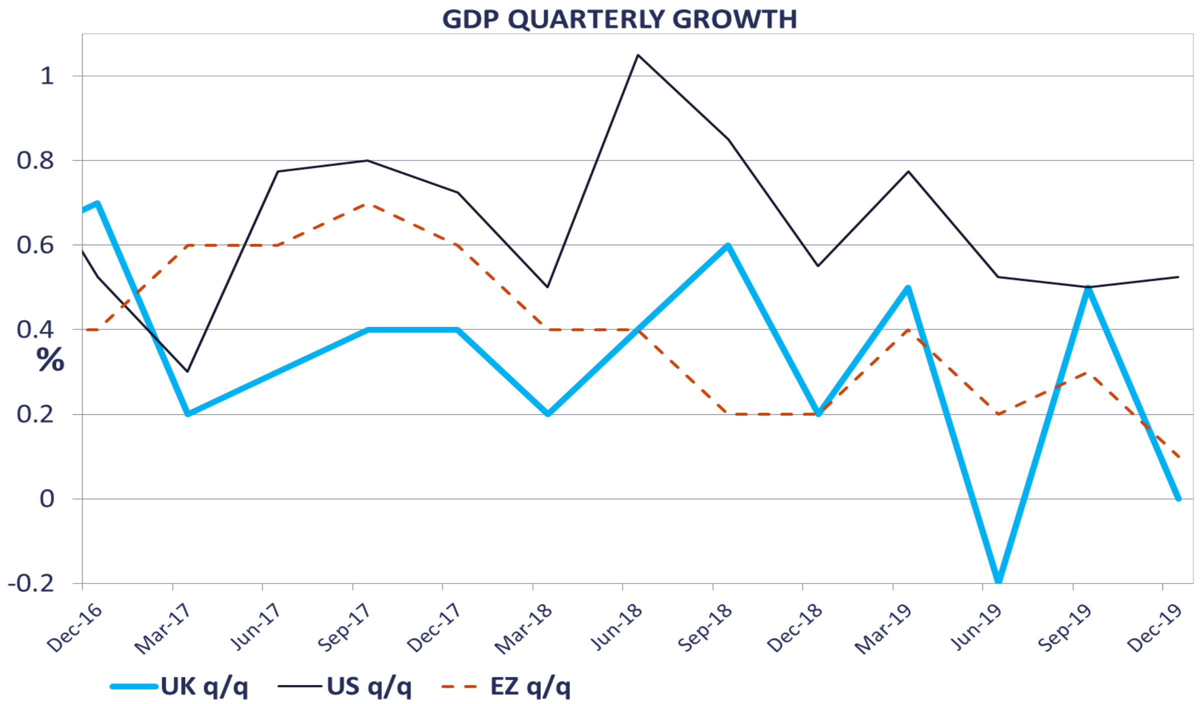
Appendix 2: Graphs

On 9.10.19, the margin over gilt yields for PWLB certainty rates was increased from 80 bps to 180 bps. The graph below shows PWLB rates less the margins added over gilt yields. This graph therefore shows more clearly the ***actual movements in gilt yields*** during the year on which PWLB rates are based.

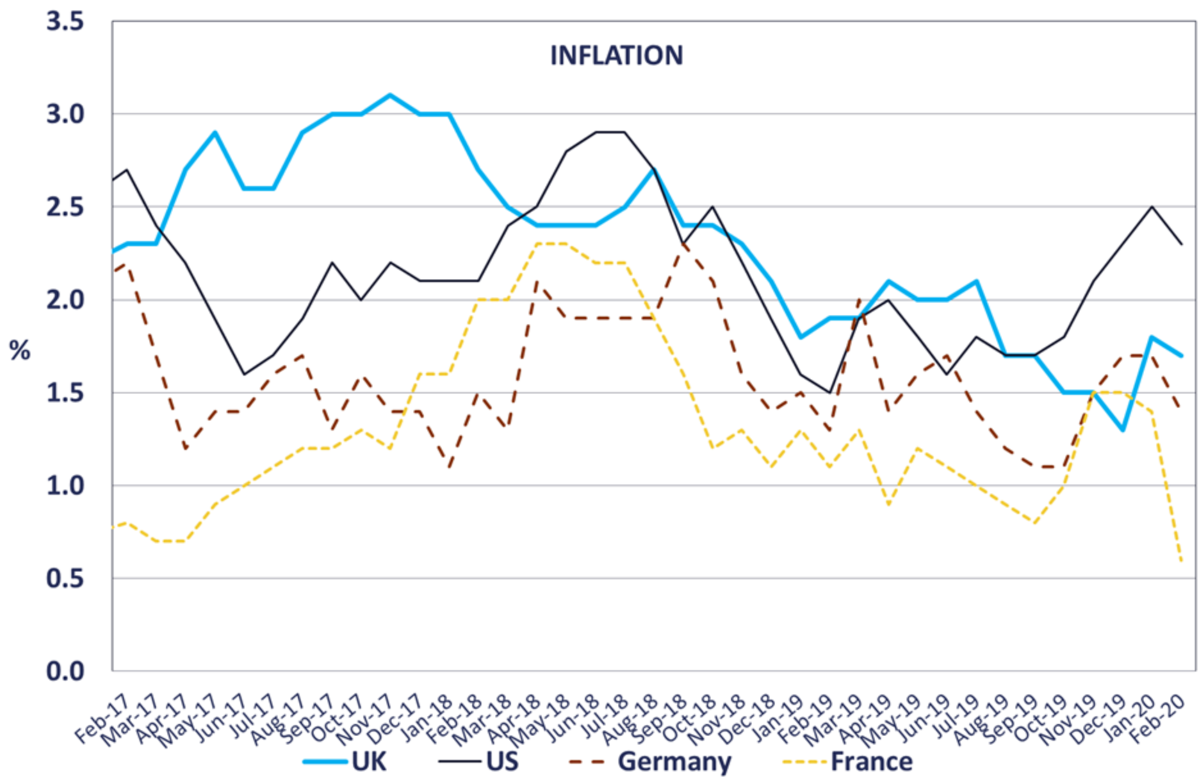


	1 Year	5 Year	10 Year	25 Year	50 Year
01/04/2019	0.66%	0.72%	1.04%	1.61%	1.44%
31/03/2020	0.10%	0.15%	0.34%	0.85%	0.59%
Low	0.02%	-0.01%	0.08%	0.45%	0.27%
Date	20/03/2020	09/03/2020	09/03/2020	09/03/2020	09/03/2020
High	0.78%	0.93%	1.27%	1.78%	1.61%
Date	15/04/2019	17/04/2019	17/04/2019	17/04/2019	17/04/2019
Average	0.55%	0.49%	0.72%	1.28%	1.12%

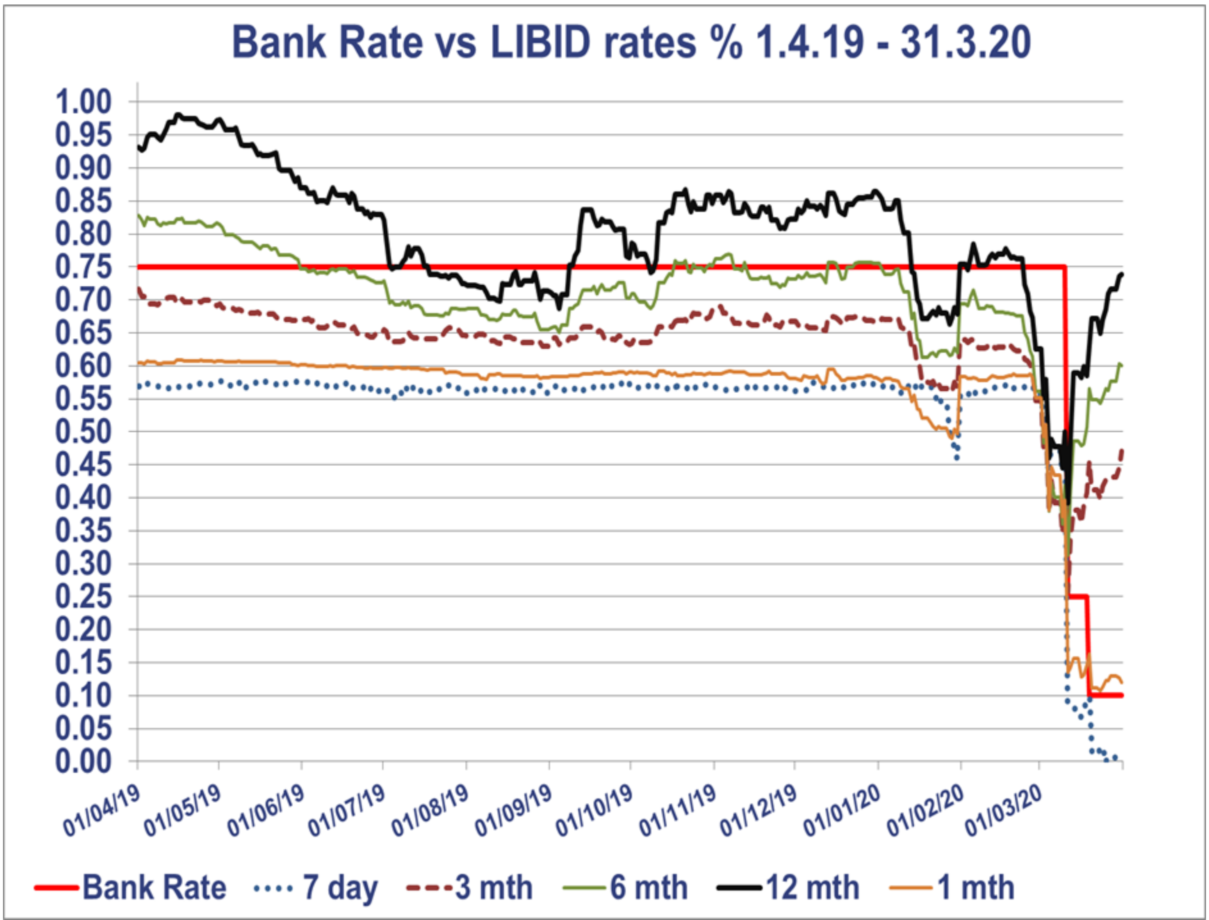
UK, US and EZ GDP growth



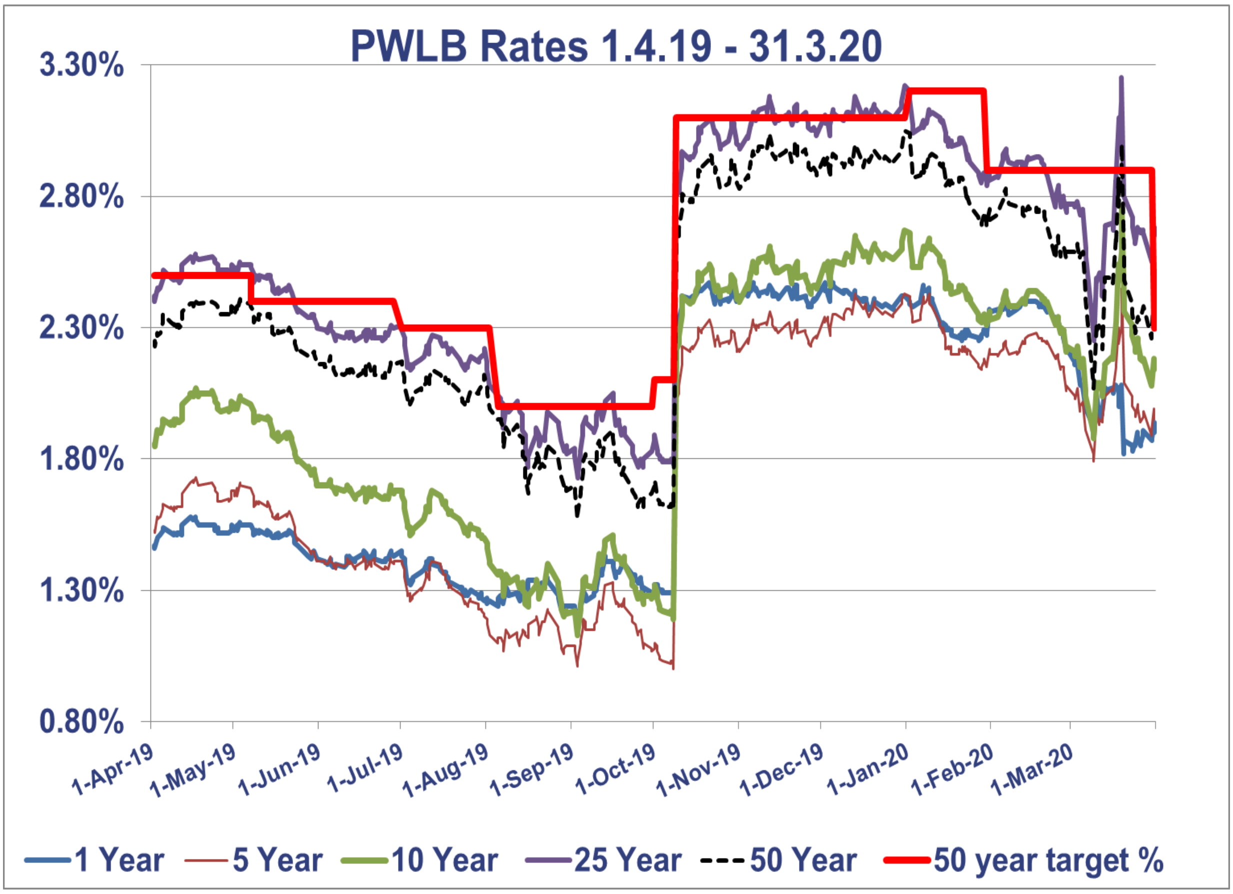
Inflation UK, US, Germany and France

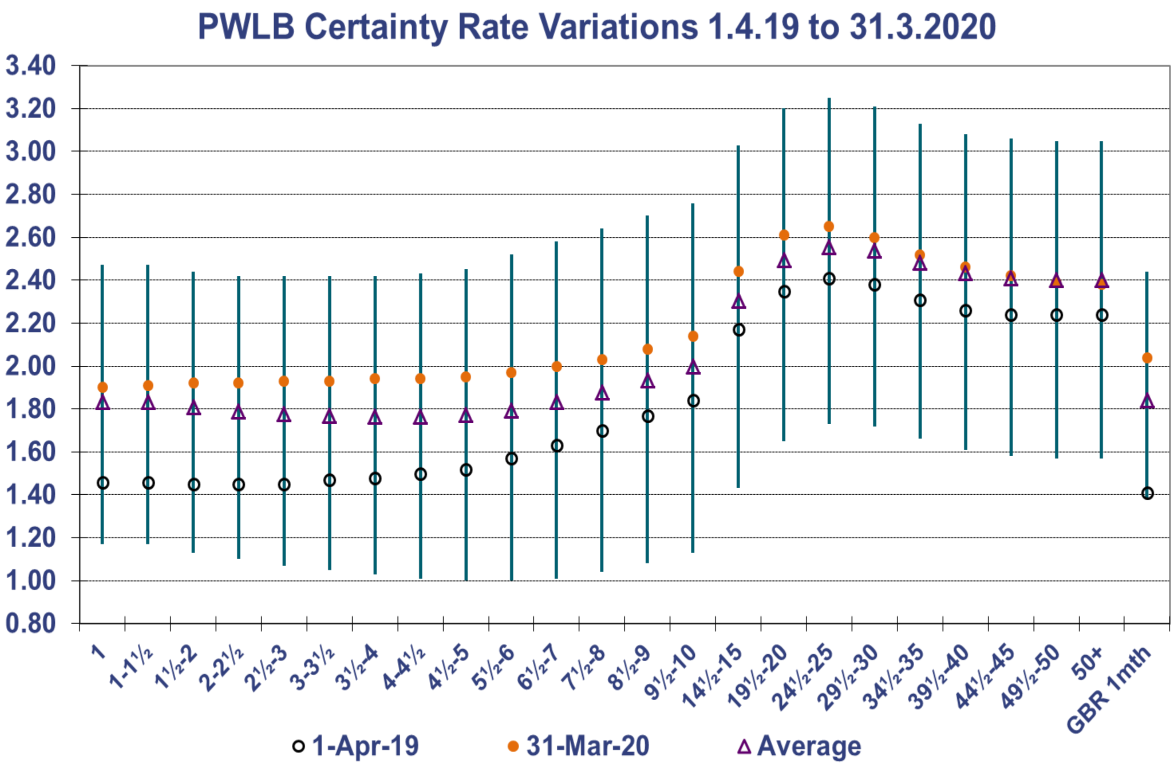


Appendix 3:Investment and Borrowing rates



	Bank Rate	7 day	1 mth	3 mth	6 mth	12 mth
High	0.75	0.58	0.61	0.72	0.83	0.98
High Date	01/04/2019	09/05/2019	15/04/2019	01/04/2019	01/04/2019	15/04/2019
Low	0.10	0.00	0.11	0.26	0.31	0.39
Low Date	19/03/2020	25/03/2020	23/03/2020	11/03/2020	11/03/2020	11/03/2020
Average	0.72	0.53	0.56	0.63	0.70	0.80
Spread	0.65	0.58	0.50	0.46	0.52	0.59


PWLB Rates 1.4.19 - 31.3.20
3.30%
2.80%
2.30%
1.80%
1.30%
0.80%
1-Apr-19
1-May-19
1-Jun-19
1-Jul-19
1-Aug-19
1-Sep-19
1-Oct-19
1-Nov-19
1-Dec-19
1-Jan-20
1-Feb-20
1-Mar-20
1 Year
5 Year
10 Year
25 Year
50 Year
50 year target %


PWLB Certainty Rate Variations 1.4.19 to 31.3.2020
3.40
3.20
3.00
2.80
2.60
2.40
2.20
2.00
1.80
1.60
1.40
1.20
1.00
0.80
1
1-1½
1½-2
2-2½
2½-3
3-3½
3½-4
4-4½
4½-5
5½-6
6½-7
7½-8
8½-9
9½-10
14½-15
19½-20
24½-25
29½-30
34½-35
39½-40
44½-45
49½-50
50+
GBR 1mth
1-Apr-19
31-Mar-20
Average

	1 Year	5 Year	10 Year	25 Year	50 Year
01/04/2019	1.46%	1.52%	1.84%	2.41%	2.24%
31/03/2020	1.90%	1.95%	2.14%	2.65%	2.39%
Low	1.17%	1.00%	1.13%	1.73%	1.57%
Date	03/09/2019	08/10/2019	03/09/2019	03/09/2019	03/09/2019
High	2.47%	2.45%	2.76%	3.25%	3.05%
Date	21/10/2019	19/03/2020	19/03/2020	19/03/2020	31/12/2019
Average	1.83%	1.77%	2.00%	2.56%	2.40%