Treasury Management Outturn 2020/21

Report of the Finance Portfolio Holder

Recommended:

That the Annual Treasury Management Report for 2020/21 and the Prudential Indicators for the year as shown in the Annex to the report be noted.

SUMMARY:

- This report reviews the performance of the Treasury Management function in 2020/21 compared with the forecasts and policies set out for the year.
- Investment income for the year was around £1,000 higher than the level of income included in the forecast in February 2021.

1 Introduction

1.1 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 each financial year. 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).

1.2 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.

2 The Council's Capital Expenditure and Financing

2.1 The Council undertakes capital expenditure on 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
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

2.2 The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

£M	2019/20 Actual	2020/21 Forecast	2020/21 Actual
Capital expenditure	7.8	14.5	7.8
Financed in year	6.2	14.5	7.8
Unfinanced capital expenditure	**1.6**	**0**	**0**

3 The Council's Overall Borrowing Need

3.1 The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR).

3.2 **Gross borrowing and the CFR** - 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 (2020/21) plus the estimates of any additional capital financing requirement for the current (2021/22) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. The table in Annex 1 highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

3.3 The funding of the CFR in 2020/21 was originally expected to be left in an over borrowed position (gross borrowing exceeding the financing requirement). The borrowing position has now been amended to an under borrowed position for 2020/21 and 2021/22. This is because an additional £14.8M of capital expenditure is expected to be incurred in 2021/22, which will be fully funded by internal borrowing.

4 Treasury Performance in 2020/21

4.1 The Council managed all the investments in-house in 2020/21.

4.2 Most investments during the year were placed in call-accounts or fixed-term deposits for durations of up to one year, with the exception of investments to a Local Authority totalling £5M for five years.

4.3 The average return on investments for the year was 0.52% compared to the average 7 day Libid benchmark of -0.07%, an out-performance of 0.59%. The Libid rate is the standard benchmark rate used by Councils when analysing their investment performance. The Libid rate is derived from Libor, London Interbank Offer rate, which is set by a panel of banks each day. In order to get the Libid rate, which is the benchmark rate for deposits, it is calculated as Libor – 0.125%. Essentially, it is a measure of the rate that banks are willing to borrow from other banks and is therefore used as a benchmark rate for deposits. An outperformance against this rate confirms that the Council has performed well on its lending activities in the year.

4.4 The Council's investment position at the end of the year is detailed below.

	Principal at 31/03/21 £M	Principal at 31/03/20 £M	Rate of Return 2020/21 %	Benchmark Return %	Variance %
Internally Managed Investments	66.5	71.5	0.52	-0.07	0.59

4.5 Of the principal invested at 31 March 2021, £25M was invested in fixed rate, fixed term deposits. The remainder was invested in call and notice accounts with access ranging from immediate to 95 days' notice.

4.6 A comparison of the investment interest earned with the original budget and forecast is shown in the table below.

	Original Budget 2020/21 £000	Forecast 2020/21 £000	Actual 2020/21 £000	Variance to Original £000
Interest on Investments	629.5	399.1	400.1	229.4

4.7 Income received on the Council's cash balances exceeded the income expected within the budget forecast, which was prepared in February 2021, by £1,000. There was however an adverse variance of £229,400 when measured against the original budget. This is because investment returns have been far lower than originally expected. Original budgets were set assuming a 0.75% rate of return, which did not materialise (see section 5 below).

5 The strategy for 2020/21

5.1 Investment returns, which had been low during 2019/20, reduced during 2020/21 to near zero. Most local authority lending managed to avoid negative rates and one feature of the year was the growth of inter local authority lending.

5.2 The expectation for interest rates within the treasury management strategy for 2020/21 was that Bank Rate would continue at the start of the year at 0.75% before rising to end 2022/23 at 1.25%. This forecast was invalidated by the Covid-19 pandemic in March 2020 which caused the Monetary Policy Committee to cut Bank Rate in March, first to 0.25% and then to 0.10%, in order to counter the hugely negative impact of the national lockdown on the economy.

5.3 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.

5.4 Investment balances in 2020/21 have been kept to a minimum through the agreed strategy of using reserves and balances to support internal borrowing, rather than borrowing externally from the financial markets. External borrowing would have incurred an additional cost, due to the differential between borrowing and investment rates. Such an approach has also provided benefits in terms of reducing the counterparty risk exposure, by having fewer investments placed in the financial markets.

6 Prudential Indicators and Treasury Limits

Prudential Indicators

6.1 The prudential indicators and borrowing limits are shown in Annex 1 and are relevant for setting an integrated treasury management statement.

6.2 The first indicator is the ratio of financing costs to net revenue stream. This compares the Council's net investment income and borrowing expenditure as a ratio of the budget requirement. A negative figure shows that investment income is greater than borrowing costs.

6.3 The second indicator is the Capital Financing Requirement (CFR). This is the total amount by which the funding of capital expenditure is reliant on external borrowing.

7 Consultations/ Communications

7.1 The Council's treasury advisors, Link Asset Services, have been consulted in the preparation of this report.

8 Equality Issues

8.1 An EQIA screening has been completed in accordance with the Council's EQIA methodology and no potential for unlawful discrimination or low level negative impact have been identified, therefore a full EQIA has not been carried out.

9 Conclusion and reasons for recommendation

9.1 The Council achieved an average investment income rate of 0.52% in the year compared with an average benchmark figure of -0.07.

9.2 Actual income for the year was below the original estimate. £229,400 but was £1,000 above the forecast set in February 2021.

9.3 The report summarises performance during 2020/21. It does not propose any changes in respect of Treasury Management in the future and therefore the recommendation is that the report be noted.

Background Papers (Local Government Act 1972 Section 100D) None			
Confidentiality It is considered that this report does not contain exempt information within the meaning of Schedule 12A of the Local Government Act 1972, as amended, and can be made public.			
No of Annexes:	1	File Ref:	N/A
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