Appendix A

Treasury Management 6 Month Performance Review

1.0 Introduction

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

The Council's treasury management strategy for 2020/21 was approved at a meeting on 26th February 2020. The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remain central to the Council's treasury management strategy.

The 2017 Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy, complying with CIPFA's requirement, was approved by full Council on 26th February 2020.

2.0 External Context

2.1 Economic background

The coronavirus pandemic dominated 2020/21, leading to almost the entire planet being in some form of lockdown during the year. The start of the financial year saw many central banks cutting interest rates as lockdowns caused economic activity to grind to a halt. The Bank of England cut Bank Rate to 0.1% and the UK government provided a range of fiscal stimulus measures, the size of which has not been seen in peacetime.

Some good news came in December 2020 as two COVID-19 vaccines were given approval by the UK Medicines and Healthcare products Regulatory Agency (MHRA). The UK vaccine rollout started in earnest; over 31 million people had received their first dose by 31st March.

A Brexit trade deal was agreed with only days to spare before the 11pm 31st December 2020 deadline having been agreed with the European Union on Christmas Eve.

Government initiatives supported the economy and the Chancellor announced in the 2021 Budget a further extension to the furlough (Coronavirus Job Retention) scheme until September 2021. Access to support grants was also widened, enabling more self-employed people to be eligible for government help. Since March 2020, the government schemes have help protect more than 11 million jobs.

Despite the furlough scheme, unemployment still rose. Labour market data showed that in the three months to January 2021 the unemployment rate was 5.0%, in contrast to 3.9% recorded for the same period 12 months ago. Wages rose 4.8% for total pay in nominal terms (4.2% for regular pay) and was up 3.9% in real terms (3.4% for regular pay). Unemployment is still expected to increase once the various government job support schemes come to an end.

Inflation has remained low over the 12 month period. Latest figures showed the annual headline rate of UK Consumer Price Inflation (CPI) fell to 0.4% year/year in February, below expectations (0.8%) and still well below the Bank of England's 2% target. The ONS' preferred measure of CPIH which includes owner-occupied housing was 0.7% year/year (1.0% expected).

After contracting sharply in Q2 (Apr-Jun) 2020 by 19.8% q/q, growth in Q3 and Q4 bounced back by 15.5% and 1.3% respectively. The easing of some lockdown measures in the last quarter of the calendar year enabled construction output to continue, albeit at a much slower pace than the 41.7% rise in the prior quarter. When released, figures for Q1 (Jan-Mar) 2021 are expected to show a decline given the national lockdown.

After collapsing at an annualised rate of 31.4% in Q2, the US economy rebounded by 33.4% in Q3 and then a further 4.1% in Q4. The US recovery has been fuelled by three major pandemic relief stimulus packages totalling over $5 trillion. The Federal Reserve cut its main interest rate to between 0% and 0.25% in March 2020 in response to the pandemic and it has remained at the same level since. Joe Biden became the 46th US president after defeating Donald Trump.

The European Central Bank maintained its base rate at 0% and deposit rate at -0.5% but in December 2020 increased the size of its asset purchase scheme to €1.85 trillion and extended it until March 2022.

Government initiatives continued to support the economy, with the furlough (Coronavirus Job Retention) scheme keeping almost 10 million workers in jobs, grants and loans to businesses and 100 million discounted meals being claimed during the 'Eat Out to Help Out' (EOHO) offer.

Credit review: After spiking in March 2020, credit default swap spreads declined over the remaining period of the year to broadly pre-pandemic levels. The gap in spreads between UK ringfenced and non-ringfenced entities remained, albeit Santander UK is still an outlier compared to the other ringfenced/retail banks. At the end of the period Santander UK was trading the highest at 57bps and Standard

Chartered the lowest at 32bps. The other ringfenced banks were trading around 33 and 34bps while Nationwide Building Society was 43bps.

Credit rating actions to the period ending September 2020 have been covered in previous outturn reports. Subsequent credit developments include Moody's downgrading the UK sovereign rating to Aa3 with a stable outlook which then impacted a number of other UK institutions, banks and local government. In the last quarter of the financial year S&P upgraded Clydesdale Bank to A- and revised Barclay's outlook to stable (from negative) while Moody's downgraded HSBC's Baseline Credit Assessment to baa3 whilst affirming the long-term rating at A1.

The vaccine approval and subsequent rollout programme are both credit positive for the financial services sector in general, but there remains much uncertainty around the extent of the losses banks and building societies will suffer due to the economic slowdown which has resulted due to pandemic-related lockdowns and restrictions. The institutions and durations on the Authority's counterparty list recommended by treasury management advisors Arlingclose remain under constant review, but at the end of the period no changes had been made to the names on the list or the recommended maximum duration of 35 days.

Interest Rates Forecast

The Bank of England (BoE) held Bank Rate at 0.1% throughout the year but extended its Quantitative Easing programme by £150 billion to £895 billion at its November 2020 meeting. In its March 2021 interest rate announcement, the BoE noted that while GDP would remain low in the near-term due to COVID-19 lockdown restrictions, the easing of these measures means growth is expected to recover strongly later in the year. Inflation is forecast to increase in the near-term and while the economic outlook has improved there are downside risks to the forecast, including from unemployment which is still predicted to rise when the furlough scheme is eventually withdrawn.

The historical low level of interest rates has made it difficult to achieve a higher rates returns on investment.

2.2 Financial markets

Monetary and fiscal stimulus helped provide support for equity markets which rose over the period, with the Dow Jones beating its pre-crisis peak on the back of outperformance by a small number of technology stocks. The FTSE indices performed reasonably well during the period April to November, before being buoyed in December by both the vaccine approval and Brexit deal, which helped give a boost to both the more internationally focused FTSE 100 and the more UK-focused FTSE 250, however they remain lower than their pre-pandemic levels.

Ultra-low interest rates prevailed throughout most of the period, with yields generally falling between April and December 2020. From early in 2021 the improved economic outlook due to the new various stimulus packages (particularly in the US), together with the approval and successful rollout of vaccines, caused government bonds to sell off sharply on the back of expected higher inflation and increased uncertainty, pushing yields higher more quickly than had been anticipated.

The 5-year UK benchmark gilt yield began the financial year at 0.18% before declining to -0.03% at the end of 2020 and then rising strongly to 0.39% by the end of the financial year. Over the same period the 10-year gilt yield fell from 0.31% to 0.19% before rising to 0.84%. The 20-year declined slightly from 0.70% to 0.68% before increasing to 1.36%.

1-month, 3-month and 12-month SONIA bid rates averaged 0.01%, 0.10% and 0.23% respectively over the financial year.

The yield on 2-year US treasuries was 0.16% at the end of the period, up from 0.12% at the beginning of January but down from 0.21% at the start of the financial year. For 10-year treasuries the end of period yield was 1.75%, up from both the beginning of 2021 (0.91%) and the start of the financial year (0.58%).

German bund yields continue to remain negative across most maturities.

3.0 Local Context

On 31st March 2021, the Council had net borrowing of £21.37m arising from its revenue income and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.3.21 Actual £m
General Fund CFR	74.8
Less: *Other debt liabilities	0.5
Total CFR	**75.3**
External borrowing	39.4

Internal borrowing	**35.9**
Less: Usable reserves	66.3
Less: Working capital	22.8
Net (Investing) or New Borrowing	**(53.2)**

The Council pursued its strategy of keeping borrowing and investments below their underlying levels, sometimes known as internal borrowing, to reduce risk and keep interest costs low.

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

Table 2: Treasury Management Summary

	30.9.20 Balance £m	**Movement £m**	**31.3.21 Balance £m**	**31.3.21 Rate %**
Long-term borrowing	39.69	-0.26	39.43	0.65
Short-term borrowing	0.00	0	0.00	0.00
Total borrowing	**39.69**	**-0.26**	**39.43**	
Long-term investments	9.63	0.33	9.96	3,43
Short-term investments	4.00	-4.00	0.00	
Cash and cash equivalents	18.56	9.78	28.34	53.0
Total investments	**32.18**		**38.30**	
Net borrowing	**7.51**		**1.13**	

The movement in the cash and cash equivalent has been as result of council tax and NNDR receipts and Government cash funding for Covid 19 (temporary holding of business grants from Central Government and increased S31 Grant income); these funds were invested in bank deposits and Money Market Funds for easy access and liquidity reasons.

3.1 Borrowing Strategy during the period

At 31st March 2021, the Council held £39.43m of loans, a decrease of £0.26m from 30 September 2020. Outstanding loans on 31st March are summarised in Table 3 below.

Table 3: Borrowing Position

	30.9.20 Balance £m	**Net Movement £m**	**31.3.21 Balance £m**	**31.3.21 Weighted Average Rate %**	**31.3.21 Weighted Average Maturity (years)**
Public Works Loan Board	39.69	-0.26	39.43	2.76%	22.6
Local authorities (short-term)	0.00	0.00	0.00	0.00%	0.0
Total borrowing	**39.69**	**-0.26**	**39.69**		**22.6**

The Council's chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective.

With short-term interest rates remaining much lower than long-term rates, the Council considered it to be more cost effective in the near term to use internal resources or short-term loans instead. The Council had not used short-term loans facility so far in this financial year.

Although it was anticipated that the Council's CFR would increase due to the capital programme, delays in the capital programme due to the pandemic no new loans have been taken out.

Long-dated Loans borrowed	PWLB Reference	Amount £	Rate %	Period (Years)
PWLB 1	495152	5,000,000	3.91	37.7
PWLB 2	495153	5,000,000	3.90	36.7
PWLB 3	502463	406,883	2.24	2.4
PWLB 4	504487	673,930	3.28	25.7
PWLB 5	504598	895,763	3.10	25.8
PWLB 6	504810	458,870	2.91	26.0
PWLB 7	504922	362,768	3.10	26.1
PWLB 8	504993	294,007	2.92	26.2
PWLB 9	505255	581,820	2.31	26.3
PWLB 10	505372	446,305	2.18	26.5
PWLB 11	505649	798,522	2.67	26.8
PWLB 12	506436	5,000,000	2.78	16.5
PWLB 13	508696	7,280,439	2.49	18.0
PWLB 14	508931	266,666	1.48	1.0
PWLB 15	509389	11,963,000	2.18	18.2
Total borrowing		**39,428,973**	**2.76**	**22.6**

The Council's borrowing decisions are not predicated on any one outcome for interest rates and a balanced portfolio of short- and long-term borrowing was maintained.

3.2 Treasury Investment Activity

The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. The investment position is shown in table 4 below.

Table 4: Treasury Investment Position

The weighted average rate for the investment portfolio up to 31.03.2021 was 0.9%.

	30.9.20 Balance £	Net Movement £m	31.3.21 Balance £m	31.3.21 Income Return %	31.3.21 Weighted Average Maturity days
Banks & building societies (unsecured)	7,355,000	7,338,000	14,693,000	0.01%	1
Government (incl. local authorities)	4,000,000	-4,000,000	0	0.00%	-
Money Market Funds	11,200,000	2,450,000	13,650,000	0.01%	1
Loans to other organisation	5,805,996	156,769	5,962,765	3.21%	>365
Other Pooled Funds.					
- *Property funds*	3,823,829	-27,282	3,796,547	4.25%	>365
Total investments	**32,184,825**	**5,917,487**	**38,102,312**		

3.3 Risk Management

Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

Given the increasing risk and low returns from short-term unsecured bank investments, the Council has maintained a diversified portfolio of asset classes as shown in table 4 above.

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

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

	Credit Score	Credit Rating	Bail-in Exposure %	Weighted Average Maturity (days)	Rate of Return %
30.09.2020	4.49	AA-	100	1	1.35
31.03.2021	4.54	A+	82	3	0.63
Similar LAs	4.15	AA-	65	51	1.83
All LAs	4.16	AA-	64	18	0.9

*Weighted average maturity

£3.79m of the Council's investments are held in externally managed strategic pooled property funds – CCLA Property Fund where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and long-term price stability. This fund generated an average total return of £76,422 (4.25%), for period of 1st April to 31st March which is used to support services in year.

Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives are regularly reviewed. Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years; but with the confidence that over a three- to five-year period total returns will exceed cash interest rates. In light of their performance over the medium-term and the Council's latest cash flow forecasts, investment in these funds has been maintained.

3.4 Non-Treasury Investments

The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Authority holds primarily for financial return. This is replicated in MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return.

The Authority also held £55.04m of such investments in:

- directly owned property £54.9m
- shareholding in subsidiaries £0.1m

Table 6: Property held for investment purposes in £'000

Property	Actual	31.3.2021 actual	
	Purchase cost	Gains or (losses)	Value in accounts
Existing Portfolio	19,644	1,581	21,225
2 Stonehill	1,400	400	1,800
80 Wilbury Way	2,200	(330)	1,870
Shawlands Retail Park	6,500	(2,000)	4,500
1400 & 1500 Parkway	5,425	(1,025)	4,400
Units 21a, 21b,23a,b,c Little End Road, St Neots	3,200	(300)	2,900
Rowley Centre, St Neots	7,600	(1,850)	5,750
Tri-link, Wakefield	13,750	(1,250)	12,500
TOTAL	**59,719**	**(4,774)**	**54,945**

These investments generated £4.1m of investment income for the Authority for 20/21, generating a yield of 7.46%.

The Authority is dependent on profit generating investment activity to achieve a balanced revenue budget. The table below shows the extent to which the expenditure planned to meet the service delivery objectives and/or place making role of the Authority is dependent on achieving the expected net profit from investments over the lifecycle of the Medium Term Financial Plan. Current outturn is showing a shortfall of expected net investment income of 732k due to the impact of the Covid 19 pandemic. Therefore, the Authority's contingency plans for continuing to provide these services, are to use reserves where necessary to offset any negative variances in the final outturn. Unallocated general fund balances and budget surplus reserve can be used in case of a downturn in investment income to meet any detrimental effect.

Table 7: Proportionality of Investments in £'000

	2018/19 Actual	**2019/20 Actual**	**2020/21 Actual**	**2021/22 Budget**	**2022/23 Budget**
Gross service expenditure	75,729	77,760	76,143	69,710	58,836
Investment income	2,753	3,283	4,125	5,290	5,345
Proportion	3.6%	4.22%	5.42%	7.59%	9.1%

4.0 Compliance

The Chief Finance Officer (s151 officer) reports that all treasury management activities undertaken during the first half year complied fully with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in table 9 below.

Compliance with the authorised limit and operational boundary for external debt is demonstrated in table 8 below.

Table 8: Debt Limits

	31.3.21 Actual £m	**2020/21 Operational Boundary £m**	**2020/21 Authorised Limit £m**	**Complied?**
General	10.00	70.00	80.00	Yes
Loans	5.18	15.00	20.00	Yes
CIS	24.25	30.00	30.00	Yes
Total debt	**43**	**115.00**	**130.00**	

Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure. Total debt was below the operational boundary all through the quarter.

Table 9: Investment Limits

	31.3.21 Actual £m	2020/21 Limit £m	Complied?
Deposit Accounts			
NatWest	10.7	unlimited	Yes
Debt Management Office (DMO)	-	unlimited	Yes
Barclays	4.00	4.00	Yes
Money Market Funds			
Aberdeen Liquidity Fund	3.00	5.00	Yes
BlackRock Institutional sterling liquidity Fund	1.10	5.00	Yes
CCLA Public Sector Deposit Fund	3.20	5.00	Yes
Federated Short Term Prime Fund	3.00	5.00	Yes
Insight Liquidity Funds	0.65	5.00	Yes
Invesco	2.00	5.00	Yes
Legal & General Sterling Liquidity Fund	0.70	5.00	Yes

5.0 Treasury Management Indicators

The Council measures and manages its exposures to treasury management risks using the following indicators.

Security

The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

	31.3.21 Actual	2020/21 Target	Complied?
Portfolio average credit rating	A+	A-	Yes

Liquidity

The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period, without additional borrowing.

	30.9.20 Actual £m	2020/21 Target £m	Complied?
Total cash available within 3 months	28.34	2	Yes

Interest Rate Exposures

This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interests was:

Interest rate risk indicator	31.3.21 Actual	2020/21 Limit	Complied?
Upper limit on one-year revenue impact of a 1% rise in interest rates	0*	£128,000	Yes
Upper limit on one-year revenue impact of a 1% fall in interest rates	0*	£128,000	Yes

*no impact as borrowing is fixed rate

The impact of a change in interest rates is calculated on the assumption that maturing loans and investment will be replaced at current rates.

Maturity Structure of Borrowing

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

	31.3.21 Actual	Upper Limit	Lower Limit	Complied?
Under 12 months	0%	80%	0%	Yes
12 months and within 24 months	0.67%	80%	0%	Yes
24 months and within 5 years	1.03%	80%	0%	Yes
5 years and within 10 years	0%	100%	0%	Yes
10 years and above	98.3%	100%	0%	Yes