NORTH WEST LEICESTERSHIRE DISTRICT COUNCIL

CABINET – TUESDAY, 8 JUNE 2021

Title of Report	**TREASURY MANAGEMENT STEWARDSHIP REPORT 2020/21**	
Presented by	Councillor Nick Rushton Corporate Portfolio Holder	
Background Papers	Capital Strategy 2020/21 – Council 25 February 2020 Treasury Management Strategy Statement 2020/21 and Prudential Indicators 2020/21 to 2022/23 – Council 25 February 2020 Investment Strategy – Service and Commercial 2020/21 – Council 25 February 2020 Budget and Council Tax 2019/20 – Council 25 February 2020 Treasury Management Activity Report April 2020 to December 2020 – Audit and Governance 17 March 2020	**Public Report:** Yes **Key Decision:** No
Financial Implications	A total of £204k in investment interest was earned on balances. This is mainly split between the General Fund £116k, Housing Revenue Account £67k and S106 Fund 22k. Annual principal repayment of £1.1m was paid on two PWLB loans for the Housing Revenue Account. In addition, interest on loans of £2.7m was paid on external debt, of which £2.2m was for the Housing Revenue Account and £400k for the General Fund. Over £35m in various COVID grants were received by the Council which provided additional cashflow from the time of grant receipt to the point of disbursement. The above has an impact on the financial resources available to the Council. **Signed off by the Section 151 Officer**: Yes	

Legal Implications	Bringing this report to cabinet complies with the councils legal obligation under the Local Government Act 2003
	Signed off by the Monitoring Officer: Yes
Staffing and Corporate Implications	None
	Signed off by the Head of Paid Service: Yes
Purpose of Report	To inform Cabinet of the Council's Treasury Management activity undertaken for the financial year 2020/21.
Reason for Decision	Informing Cabinet of the Council's Treasury Management activity is a statutory requirement.
Recommendations	**THAT CABINET APPROVE THIS REPORT.**

1.0 BACKGROUND

1.1 Treasury Management activity is underpinned by CIPFA's Code of Practice on Treasury Management ("the code"), which requires local authorities to produce Prudential Indicators and a Treasury Management Strategy Statement annually on the likely financing and Investment activity.

1.2 This report fulfils the council's legal obligation under the Local Government Act 2003, to have regard to both the CIPFA Code and the Ministry of Housing, Communities and Local Government (MHCLG) Investment Guidance.

1.3 In 2020/21, council approved its Capital Strategy (included in the Budget and Council Tax report) and Treasury Management Strategy Statement, including the Borrowing Strategy, Debt Rescheduling Strategy, Annual Investment Policy and Strategy, Interest Apportionment Policy, Prudential Indicators and Annual Minimum Revenue Position Statement in its meeting on 25 February 2020.

1.4 Investing or borrowing activities expose the council to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risks are therefore central to the council's treasury management strategy.

2.0 THE U.K. ECONOMY AND OTHER FACTORS.

2.1 An economic update and Interest rate forecast has been provided by our Treasury Advisers (Arlingclose Ltd) and summarised below. A full update can be found at Appendix A.

- The medium-term global economic outlook has improved with the rollout of vaccination programmes, of which the UK remains at the forefront. The Roadmap out of Lockdown has bolstered expectations through March.
- The ONS Q4 2020 growth was higher than expected at 1%, leaving the UK economy 8% smaller than Q4 2019. January GDP fell by 2.9%, but less than Bank of England expectations. Unemployment had risen to 5.1% in the three months to December.
- Support packages such as the Coronavirus Job Retention Scheme were extended in the Government's Budget, reducing the downside risks facing the UK economy. However, the extension of furlough will not totally mitigate an inevitable rise in unemployment when costs start to be shared with employers.
- While restrictive measures are likely to continue in the UK until most of the population is vaccinated by the second half of 2021, the end of the strict lockdowns in Q2 will prompt a sharp increase in GDP. Meanwhile, inflation is set to rise quickly back to

target due to weaker base effects as the pandemic hit in 2020. This will be partly offset by the extensions to VAT reductions and the freezing of various duties.

- There remain risks to the more positive narrative that has developed since the turn of the year. This is especially apparent in the Eurozone, where virus cases are once again on the rise due to the slow vaccine rollout, and recent issues in both the UK and Eurozone with vaccine supply.
- The uncertain outlook will maintain pressure on central banks to maintain loose monetary conditions for the foreseeable future. Bank Rate is unlikely to change despite developing market expectations.
- Longer term yields have risen sharply, albeit remaining at low levels. US stimulus and the relaxation of restrictions has boosted global growth and inflation expectations, raising expectations of monetary tightening.
- Upward movement in gilt yields could continue in the short term due to market momentum and rising CPI rates, but this is likely to taper once inflation fears recede as the effect of weak base effects subsides.

3.0 THE COUNCIL'S TREASURY POSITION.

3.1 The council's current strategy is to use internal borrowing to reduce risk and keep interest costs low. The treasury management change over the financial year is shown below.

	Balance at 01/04/2020 £m	**Net Movement £m**	**Balance at 31/03/2021 £m**
Long term borrowing - HRA	£71.70	-£1.20	£70.50
Long term borrowing – General Fund	£8.40	£0.00	£8.40
Other long-term liabilities - HBBC	£0.10	£0.00	£0.10
Total Borrowing	**£80.20**	**-£1.20**	**£79.00**
Long term investments – greater than 1 year	£3.00	-£3.00	£0.00
Short term investments – less than 1 year	£39.70	-£0.90	£38.80
Pooled funds and externally managed investments*	£8.00	£3.50	£11.50
Total Investments	**£50.70**	**-£0.40**	**£50.30**
Net debt	**£29.50**	**-£0.80**	**£28.70**

*Represents investments held in Money Market Funds

3.2 The annual repayments on two PWLB annuity loans taken out as part of the self-financing system of Council Housing in 2011/2012, are shown in the Net Movement column.

3.3 In 2020/21, the capacity for investment has decreased by £0.4m. This can be affected by various factors including: reduced income, contributions to/from reserves, setting aside expenditure to repay borrowing (MRP), fortuitous expenditure, Section106 disbursements.

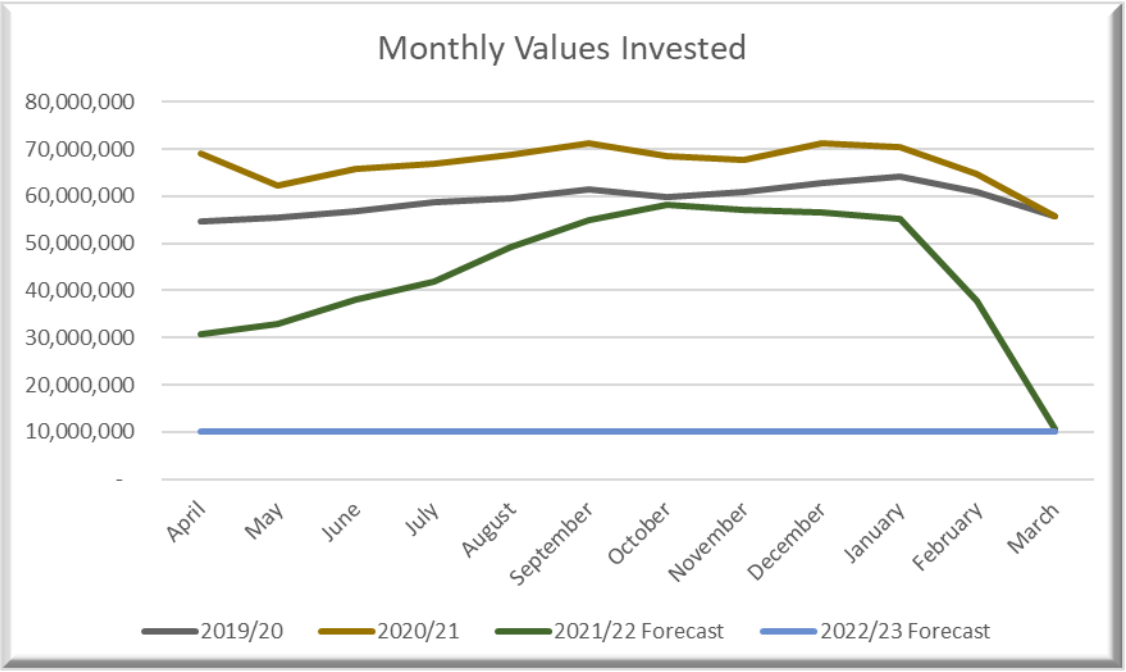
3.4 In 2020/21, some of the highlights that have impacted on the capacity are:

- HRA
  - Council House RTB sales +£2.4m
  - Council Houses Non RTB sales +£166k
  - Purchase of new Council Houses +£2.7m
  - Expenditure on New Builds -£435k (8 units completed)
  - Property purchased for demolition as part of new build development -£139k
  - RTB discount previously given returned to the Council +£19.6k
- General Fund
  - Sale of Vehicles +£21k
  - Purchase of new vehicles -£173k

- MRP £715k
- Capital Programmes slippages: General Fund +£13.1m (largely attributable from the New Leisure Centre Project +£8.7m) and Housing Revenue Account for +£2.36m
- Prepayment into the Pension Fund -£3.1m
- COVID-19 financial impact
    - Income & expenditure variances due to COVID-19 General Fund -£940k
    - Timing difference between receipt and disbursement of COVID-19 grants +£35m

3.5 The pattern of cash held and subsequently invested per month is shown in the chart below, illustrating the cash flow trends throughout the year. The delay in implementation of Capital programmes will provide additional scope for short term investments in 2021/22.

3.6 The chart below also shows the forecast position for 2021/22 and 2022/23. This reflects lower levels of cash available in the next two years since it is planned that internal borrowing will be used to fund Capital programmes along with the effect of the expected maturity of Housing Revenue Account's £13m PWLB loans in 2021/22. The repayment of £1m Cornwall Bond147 is also due in 2022/23.



4.0 BORROWING ACTIVITY.

4.1 The council's Borrowing Strategy 2020/21 incorporates a prudent and pragmatic approach to borrowing to minimise borrowing costs without compromising the longer-term stability of the portfolio, consistent with the council's Prudential Indicators.

4.2 No loans matured in 2020/21 that required replacement.

4.3 The Borrowing Strategy identified that borrowing would not be required until 2021/22 and the council has not undertaken any new long-term borrowing during the year. Annual principal repayment of £1.1m and interest payments totalling £2.68m were made in respect of existing debt. Members should note that a significant proportion of the HRA self-financing debt was taken out on a maturity basis and therefore whilst interest is paid, the principal repayment of the loan is not made. The Council has the funds set aside within HRA reserves for the first two maturity loan redemptions in 2021/22 of £3m and £10m, should it decide to repay the loans rather than refinance.

4.4 The council's cash flow remained positive and did not require and temporary loans during the year.

4.5 The council had approximately £9m of internal debt at 31 March 2021. This is the cumulative value of internal cash balances used to finance new capital expenditure instead of financing through unsupported borrowing. This is currently judged to be the most cost-effective means of funding the capital programme.

4.6 The estimated Minimum Revenue Provision (MRP) is intended to ensure that the capital financing debt is paid off over the longer term. The MRP charge made to General Fund revenue account for 2020/21 is £715k.

4.7 The Housing Revenue Account is not required to make MRP charges. However, the council classes the principal repayments made in respect of the two PWLB annuity loans taken out as part of the housing self-financing in 2011/12, as MRP. In 2020/21, this repayment was £1.1m (as per 4.3 above).

5.0 DEBT RESCHEDULING ACTIVITY.

5.1 The council's Debt Rescheduling Strategy 2020/21, established a flexible approach where the rationale for rescheduling could be one or more of the following:

- Savings in interest costs with minimal risk.
- Balancing the volatility profile (i.e. the ratio of fixed to variable rate debt) of the debt portfolio.
- Amending the profile of maturing debt to reduce any inherent refinancing risks.

5.2 No opportunities for debt rescheduling were identified which conformed to the above rationale. Accordingly, the council has undertaken no debt rescheduling activity during the year.

5.3 The council's portfolio of thirteen loans - ten PWLB loans and three market loans continue to be monitored for debt rescheduling opportunities.

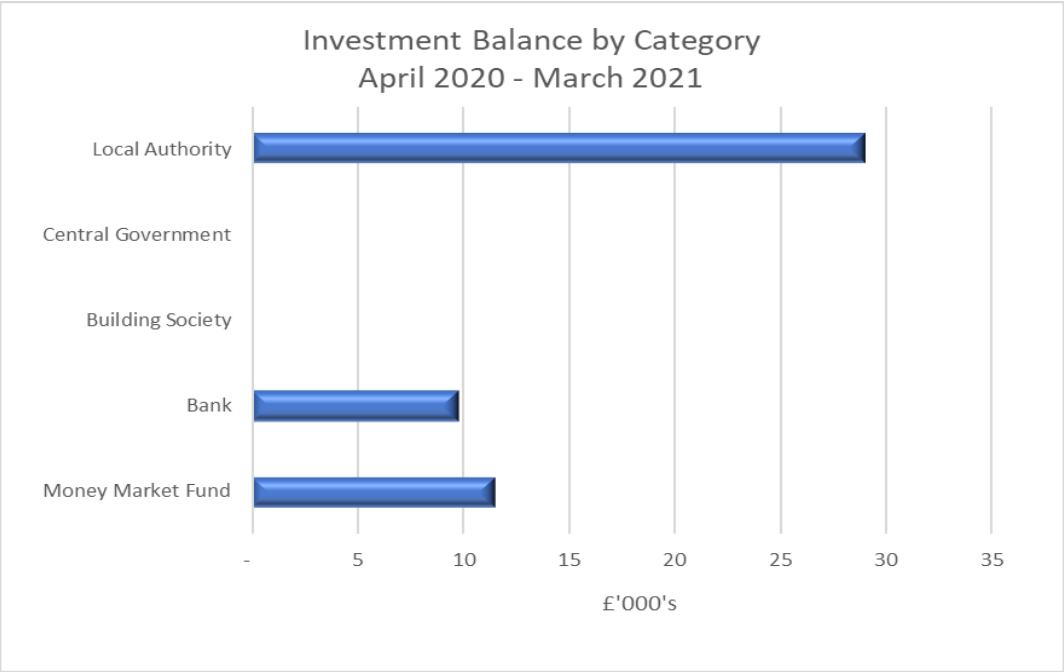
6.0 TREASURY MANAGEMENT INVESTMENT ACTIVITY.

6.1 The main objective of the council's Investment Policy and Strategy 2020/21 is to invest its surplus funds prudently.

6.2 The council's investment priorities (S.L.Y.) are:

- **S**ecurity of the invested capital;
- sufficient **L**iquidity to permit investments; and,
- Optimum **Y**ield which is commensurate with security and liquidity.

6.3 To lower the inherent investment risk, the council has minimised the use of banks and increased the use of other Local Authorities as investment counterparties. A range of lengths of investment, from overnight investments to short and long fixed term, from 32 days to 1 year, are currently utilised to ensure that the principles of security, liquidity and yield are followed. The table below shows the range of counterparties used by the council and the values invested at 31 March 2021.



6.4 The counterparties that the council currently use all meet the criteria set out in the Treasury Management Strategy Statement 2020/21 and are monitored by the Treasury Management Advisors. A detailed list of the counterparties used and amounts currently invested can be seen in Appendix B.

6.5 Inter-Local Authority lending accounted for 58% of investments placed during the year. The Council's investments are made with reference to the Council's cash flow forecast, the outlook for the UK Bank Rate, money market rates, the economic outlook and advice from the Council's treasury adviser.

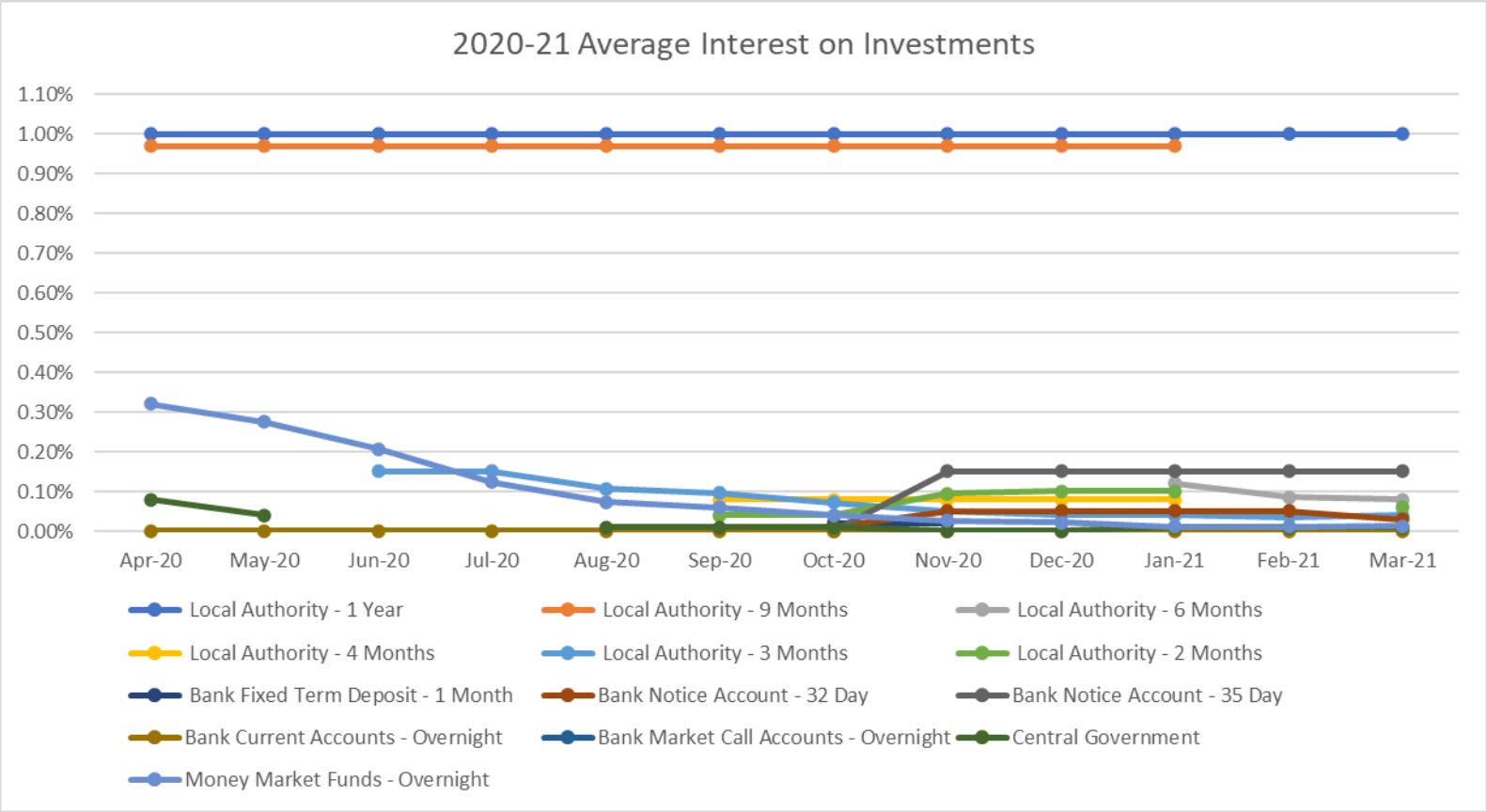
6.6 The Council exercises due diligence by assessing the organisation's financial stability. This is achieved by reviewing their credit status, most recent audited financial statements, auditor's report, budget report and current news which is financial in nature. All decisions are signed off the by the Section 151 Officer or the Deputy Section 151 Officer.

6.7 The average rate of return on the council's investment balances for the year was 0.30%. For comparison purposes, the benchmark return (average 7-day London Interbank Bid Rate or LIBID rate) on 31 March 2020 was 0.06% and the average 7-day London Interbank Offered Rate (LIBOR) rate was 0.06%. This shows that we are achieving a good rate of return against benchmark.

6.8 Paragraph 6.6 above explains that the current average rate of return of 0.30% has been achieved. This was an under performance from the budgeted interest of 0.83%, which was mainly due to the COVID-19 impact on the financial market. It resulted to the interest income of £181k for the year - £119k below the budget of £300k.

6.9 The COVID-19 pandemic hugely impacted the financial market and investment opportunities during the year. With the exception of two forward deals made prior to the national lockdown in March 2020, interest rates on in-year investments ranged between 0% and 0.40%. This is reflected of the decision made by the Bank of England to cut the interest rate to as low as 0.10% and has remained at this level for the whole financial year.

Graph 1 - Average interest rate on in year investments and the movement of interest rates over the year.

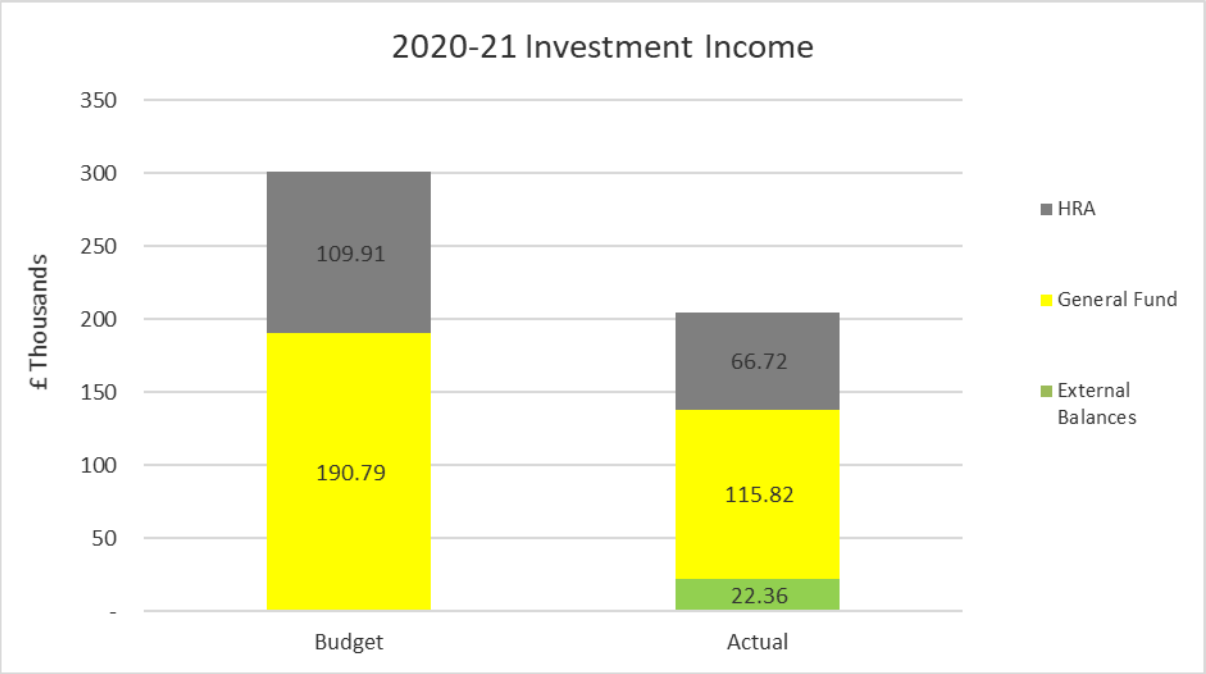


6.10 The council budgeted to achieve £300,700 of income from its investment activity in 2020/21 of which £190,800 is applied to General Fund and £109,900 to Housing Revenue Account. Investment activity for the year achieved £204,892 in interest.

6.11 Of the income achieved, an element is applied to balances held on external income. This external income largely represents balances from S106 contributions that have not yet been spent. The amount to be applied is £21,825. This is not budgeted for as S106 contributions are only achieved when specific conditions are met and are anticipated to be spent.

6.12 The remaining balance of £182,537 is apportioned between the General Fund which will receive £115,817; and Housing Revenue Account which will receive £66,720.

6.13 The budgeted and projected levels of investment income is represented in the table below.



6.13 There were two breaches of investment limits in the year reported to Audit and Governance committee in October 2020.

1. The COVID-19 support grants received from the central government were deposited in short term call accounts and money market funds as the council was required to disburse this to local businesses as soon as possible. Individual account limits on money market funds were maintained, but the aggregate money market limit of £20m as per TMSS was breached by an amount of £2m. This occurred on April 1 when the grants were received and was resolved on April 9 when grants were paid out to businesses. The Head of Finance and S151 officer was made aware of this in advance prior to the initial receipt of the grants. This was closely monitored through a weekly update on the council's Cashflow and investments.
2. The £5m limit on the Lloyds day-to-day banking account was breached by £1.2m on 1 July 2020. This occurred as a result of £5.7m in Council Tax, Business Rates and Rent being received on this date. As the funds were required the next day to make payments to preceptors (Fire, Police and Leicestershire County Council) and the money market funds were already at their approved limits. The Finance Team Manager and Deputy S151 Officer in the absence of the Head of Finance, approved the breach of the TMSS and to leave the funds in the Lloyds account overnight.

7.0 NON-TREASURY INVESTMENT ACTIVITY

7.1 The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Authority 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.

7.2 The following list represents the council's current investments in this area.

Property or Type	Value at 31 Mar 2021	Reason held
Industrial Units	£6.5m	To support the local economy and to generate profits to supplement council expenditure
Markets	£1.5m	Any profit supplements council expenditure
Land	£4.8m	Future economic benefit

7.3 More detailed information can be found in the "Investment Strategy – Service and Commercial" which was presented to Council on 25 February 2020.

7.4 In November 2019, Cabinet approved a new Corporate Asset Management Strategy, which set out a framework from which to manage our corporate property assets for the next five years. This strategy commits to reviewing the financial performance of our commercial assets as a priority, and an external review identified an average yield of 7.88% across our portfolio. Lower yielding assets are planned to be reviewed as part of the Council's Journey to Self Sufficiency (J2SS) programme to assess whether they can managed in a different way to increase overall portfolio yield. The work on the J2SS programme was halted in 2020/21 in reaction to the demands of the COVID-19 pandemic.

8.0 SUMMARY

8.1 For the financial year 2020/21, the council can confirm that it has complied with its Prudential Indicators, which were approved as part of the council's Treasury Management Strategy Statement.

8.2 The council can confirm that during the financial year, other than the breach of prescribed limit detailed in paragraph 6.13, it has complied with its Treasury Management Practices.

Policies and other considerations, as appropriate	
Council Priorities:	Value for Money
Policy Considerations:	Treasury Management Strategy Statement
Safeguarding:	Not Applicable
Equalities/Diversity:	Not Applicable
Customer Impact:	Not Applicable
Economic and Social Impact:	Not Applicable

Environment and Climate Change:	Not Applicable
Consultation/Community Engagement:	Not Applicable
Risks:	Borrowing and investment both carry an element of risk. This risk is mitigated through the adoption of the Treasury and Investment Strategies, compliance with the CIPFA code of Treasury Management and the retention of Treasury Management Advisors (Arlingclose) to proffer expert advice.
Officer Contact	Dan Bates Head of Finance and Section 151 Officer dan.bates@nwleicestershire.gov.uk

APPENDIX A

Economic information provided by Treasury Management Advisors

External Context *(based on data as at 24/03/21)*

Economic commentary

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 earliest with the focus on getting those most at risk from the virus vaccinated first and to date some 28 million people have had their first dose.

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 (EU) on Christmas Eve.

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.

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.

After contracting sharply in Q2 (Apr-Jun) 2020 by 19.8%, growth in Q3 and Q4 bounced back by 15.5% and 1.0% respectively. The main sectors of production, construction, and services all increased in output in Q4, rising by 1.8%, 4.6% and 0.6% 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.

Inflation has remained low all year and the 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). The weaker-than-expected readings were exacerbated by downward price pressures from the latest lockdown with the main upward impact coming from car fuel prices.

Despite the furlough scheme supporting many jobs throughout the year, unemployment still rose. Labour market data showed that in the three months to January 2021 the unemployment rate was 5.0%, down slightly from the previous month but higher than the 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). The employment rate fell to 75.0% from 75.2% in the previous quarter. Unemployment is still expected to increase once the various government job support schemes come to an end, but with the extensions announced in the Budget likely to help with longer-term employment, the BoE is now predicting unemployment to peak at around 6-6.5%, rather than the 7.5% it had forecast previously.

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.

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.

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 gave 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, pushing yields higher more quickly than had been anticipated.

The 5-year UK benchmark gilt yield began the financial year at 0.184% before declining to -0.033% at the end of 2020 and then rising strongly to the current level of 0.33%. Over the same period the 10-year gilt yield fell from 0.314% to 0.192% before rising to 0.764% currently. The 20-year declined slightly from 0.696% to 0.681% before increasing to the current level of 1.265%.

1-month, 3-month and 12-month SONIA bid rates averaged 0.01%, 0.11% and 0.24% respectively over the financial year.

The yield on 2-year US treasuries is currently 0.1452%, up from 0.121% at the beginning of January but down from 0.206% at the start of the financial year. For 10-year treasuries the current yield is 1.647%, up from both the beginning of 2021 (0.913%) and the start of the financial year (0.583%).

German bund yields remain negative across most maturities.

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 59bps and Standard Chartered the lowest at 29bps. The other ringfenced banks were trading between 30 and 32bps while Nationwide Building Society was 40bps.

Credit rating actions to the period ending December 2020 have been covered in previous outturn reports, however 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.

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 on Arlingclose's counterparty list and recommended duration 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

APPENDIX B

Counterparties and Investment Summary as at 31/03/2021

Counterparty	Length	From	To	Amount	Rate
Blackrock MMF	Overnight	31/03/2021	01/04/2021	2,000,000.00	0.0001%
Aberdeen Asset Management MMF	Overnight	31/03/2021	01/04/2021	2,500,000.00	0.0100%
Federated Investors MMF	Overnight	31/03/2021	01/04/2021	3,000,000.00	0.0100%
CCLA MMF	Overnight	31/03/2021	01/04/2021	4,000,000.00	0.0459%
Lloyds Main	Overnight	31/03/2021	01/04/2021	2,778,414.98	0.0000%
Bank of Scotland	Overnight	31/03/2021	01/04/2021	1,000,000.00	0.0000%
Lloyds Market Call Account	Overnight	31/03/2021	01/04/2021	2,000,000.00	0.0100%
Lloyds Notice Account	32	31/03/2021	02/05/2021	2,000,000.00	0.0300%
Santander Notice Account	35	31/03/2021	05/05/2021	2,000,000.00	0.0150%
Walsall Metropolitan Borough Council	364	09/04/2020	08/04/2021	5,000,000.00	1.0000%
Watford Borough Council	184	29/03/2021	29/09/2021	5,000,000.00	0.0700%
Surrey Heath Borough Council	181	17/02/2021	17/08/2021	4,000,000.00	0.0500%
Epping Forest District Council	176	25/01/2021	20/07/2021	5,000,000.00	0.1200%
Monmouthshire County Council	91	05/01/2021	06/04/2021	5,000,000.00	0.0500%
Sedgemoor District Council	60	08/03/2021	07/05/2021	5,000,000.00	0.0600%
Total				**50,278,414.98**	