Cyngor Castell-nedd Port Talbot
Neath Port Talbot Council

NEATH PORT TALBOT COUNTY BOROUGH COUNCIL

CABINET

REPORT OF THE DIRECTOR OF FINANCE & CORPORATE SERVICES HYWEL JENKINS

11 NOVEMBER 2020

MATTERS FOR: MONITORING

WARDS AFFECTED - ALL

Treasury Management Mid Year Review Report 2020/21

Purpose of the Report

1. To review treasury management activities for the 6 month period to 30th September 2020.

Background

2. The Council operates a cash balanced treasury budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering maximising investment return.

3. The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt

previously drawn may be restructured to meet Council risk or cost objectives.

4. As a consequence treasury management 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. "

Introduction

5. The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2011) was adopted by this Council at the Council meeting in 28th February 2013.

The primary requirements of the Code are as follows:

(i) Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
(ii) Creation and maintenance of Treasury Management Practices set out in the manner in which the Council will seek to achieve those policies and objectives.
(iii) 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.
(iv) 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.
(v) Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated bodies are the Audit and Policy and Resources Committees.

Scheme of Delegation

Area of Responsibility	Council/ Committee	Frequency
Treasury Management Strategy / Annual Investment Strategy / MRP policy	Cabinet for approval by Full Council	Annually before the start of the year
Treasury Management Strategy / Annual Investment Strategy / MRP policy – mid year report	Cabinet	Mid year
Treasury Management Strategy / Annual Investment Strategy / MRP policy – updates or revisions at other times	Cabinet for approval by Full Council	Periodically
Annual Treasury Outturn Report	Cabinet	Annually by 30th September after the end of the year
Treasury Management Monitoring and Performance Reports	Cabinet and Audit Committee	Quarterly Quarterly
Treasury Management Practices	Cabinet for approval by Full Council	Annually
Scrutiny of Treasury Management Strategy	Cabinet (and Audit Committee	Annually

6. This mid-year report has been prepared in compliance with CIPFA's Code of Practice, and covers the following:

- An economic update for 2020/21;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure (prudential indicators);
- A review of the Council's investment portfolio for 2020/21;
- A review of the Council's borrowing strategy for 2020/21;
- A review of any debt rescheduling undertaken during 2020/21;

- A review of compliance with Treasury and Prudential Limits for 2020/21.
- Revised Treasury and Prudential Limits for 2020/21 to 2022/23.

7. There have been no changes to the approved Treasury Management and Investment Strategies for the 6 months up to 30th September 2020

Economic Update

8. The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it has left the Bank Rate unchanged to date, although some forecasters had suggested that a cut into negative territory could happen. However, the Governor of the Bank of England has made it clear that he currently thinks that such a move would do more damage than good and that more quantitative easing is the favoured tool if further action becomes necessary. As shown in the forecast table below, no increase in Bank Rate is expected within the forecast horizon ending on 31st March 2023 as economic recovery is expected to be only gradual and, therefore, prolonged.

Interest rate forecasts

9. The Council's treasury advisor, Link Group, provided the following forecasts on 11th August 2020 (PWLB rates are certainty rates, gilt yields plus 180bps)::

Link Group Interest Rate View 11.8.20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month average earnings	0.05	0.05	0.05	0.05	0.05	-	-	-	-	-
6 month average earnings	0.10	0.10	0.10	0.10	0.10	-	-	-	-	-
12 month average earnings	0.15	0.15	0.15	0.15	0.15	-	-	-	-	-
5yr PWLB Rate	1.90	2.00	2.00	2.00	2.00	2.00	2.10	2.10	2.10	2.10
10yr PWLB Rate	2.10	2.10	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.30
25yr PWLB Rate	2.50	2.50	2.50	2.60	2.60	2.60	2.70	2.70	2.70	2.70
50yr PWLB Rate	2.30	2.30	2.30	2.40	2.40	2.40	2.50	2.50	2.50	2.50

The Council's Capital Position (Prudential Indicators)

10. This part of the report updates:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

The Council's Capital Expenditure and Financing 2020/21

	2019/20 Actual £'000	**2020/21 Original Estimate £'000**	**2020/21 Current Estimate £'000**
Capital expenditure	39,131	84,518	77,684
Resourced by:			
• Capital receipts	0	4,725	925
• Capital grants & contributions	24,684	51,360	62,565
• Capital reserves + DRF	182	3,421	2,828
Capital Expenditure to be financed from borrowing	**14,265**	**25,012**	**11,366**

11. The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). The CFR results from the capital activity of the Council and what resources have been used to pay for the capital spend. It represents the unfinanced capital expenditure, and prior years' unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

12. Part of the Council's treasury activities 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 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.

13. Reducing the CFR – the Council's 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 borrowing need. 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.

14. 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).

15. The Council's 2020/21 MRP Policy (as required by CIPFA Code of Practice on Treasury Management) was approved by Council as part of the Treasury Management Strategy Report for 2020/21 on 6th March 2020.

16. The Council's CFR for the year is shown below, and represents a key prudential indicator.

CFR	**2019/20 Actual £'000**	**2020/21 Original Estimate £'000**	**2020/21 Current Estimate £'000**
Opening balance	338,618	343,818	342,874
Add unfinanced capital expenditure (point 10)	14,265	25,012	11,366
Less MRP/Set aside receipts	(10,009)	(10,410)	(10,147)
Closing balance	**342,874**	**358,420**	**344,093**

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

17. Net borrowing and the CFR – in order to ensure that borrowing levels are prudent over the medium term the Council's external borrowing, net of investments, must only be for a capital purpose. This essentially means that the Council is not borrowing to support revenue expenditure. Net borrowing should not therefore, except in the short term, have exceeded the CFR. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2020/21. The following table highlights the Council's net borrowing position against the CFR. This shows the Council is complying with this prudential indicator as projected net borrowing is less than the CFR.

	2019/20 Actual £'000	**2020/21 Original Estimate £'000**	**2020/21 Current Estimate £'000**
External Debt (Gross)	307,872	277,580	299,148
Less Investments	(56,500)	(61,000)	(61,000)
Net Borrowing Position	251,372	216,580	238,148
CFR	342,874	358,420	344,093

18. The authorised limit – the authorised limit is the "affordable borrowing limit" required by Section 3 of the Local Government Act 2003. The Council does not have the power to borrow above this level.

19. The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. 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	**2020/21 Original Estimate £'000**	**2020/21 Current Estimate £'000**
Authorised Limit	392,873	408,420	394,093
Operational Boundary	372,873	388,420	374,093
Gross Borrowing *	307,872	277,580	299,148

* Total maximum long term and short term

20. This report confirms that during the first 6 months of 2020/21 Council has maintained gross borrowing within the Authorised Limit.

Investment Portfolio 2020/21

21. In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. It is currently not possible to earn the level of interest rates commonly seen in previous decades as all investment rates are barely above zero now that Bank Rate is at 0.10%, while some entities, including more recently the Debt Management Account Deposit Facility (DMADF), are offering negative rates of return in some shorter time periods. Given this risk environment and the fact that increases in Bank Rate are unlikely to occur before the end of the current forecast horizon of 31st March 2023, investment returns are expected to remain low.

22. It is confirmed that the approved limits within the Annual Investment Strategy have not been breached during the first six months of 2020/21 other than with the Council's banker. Members should note that due to the COVID pandemic it was prudent for us to hold more cash in our Santander Deposit Account (the Authority's bankers) rather than the amount set out in the Specified Investment Criteria (appendix 3). Due to the front loading of RSG and receipt of other specific grant funding during the first quarter of 2020 the highest amount placed with Sandanter was £117m on 9 June. This reduced to £37.1m as at 30 September 2020. This is a temporary arrangement during the pandemic and all other criteria are being adhered to.

23. The Council's original budget for investment return for 2020/21 has been set at £400k. This needs to be revised down to £200k which is a reflection of the low level of returns anticipated on investments with the actual shortfall being funded from the Treasury Management Reserve.

24. The Treasury Management Strategy Statement (TMSS) for 2020/21, which includes the Annual Investment Strategy, sets out the Council's investment priorities as being:

- Security of Capital
- Liquidity

25. There has been no change in the Council's Investment Strategy aims from those approved on 6th March 2020. The aim continues to be to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity. In the current economic climate, it is considered appropriate to keep an adequate level of investments which can be instantly accessed to cover short term cash flow needs. The Council also seeks out value where available in significantly higher rates in periods up to 12 months with approved institutions that meet the Council's stringent credit rating assessment.

26. Investment rates available have continued at historically low levels. The average level of funds available for investment purposes during the period was affected by the timing of precept payments, receipt of grants and progress on the Capital Programme.

Investment performance to the 30th September 2020

27. The Council held £74.6m of investments as at 30th September 2020 and the investment portfolio yield for the first six months of the year is 0.15% against a benchmark 0.11%. The Council has outperformed the benchmark by 4 basis points. The benchmark for funds managed in-house is the 3 month LIBID uncompounded rate which is the most realistic comparison rate as advised by our treasury management consultants.

    A full list of investments held as at 30th September 2020 is provided in Appendix 1.

Investment counterparty criteria and proposed amendments

28. The current investment counterparty criteria approved by Members earlier this year are detailed in Appendix 3 of this report.

29. The Current Investment Policy to allow for a maximum investment of £20m with F1 rated institutions. Currently classified as F1 by the Fitch credit reference agency are banks such as Lloyds Bank, Barclays Bank and Santander UK plc.

Borrowing

30. The Council's agreed Strategy in relation to borrowing is set out in the Treasury Management Strategy Report as approved by Council. This strategy outlined that consideration would be given to entering into new external borrowing if PWLB (or money market) rates became more favourable.

31. During 2020/21 the Council has not entered into any new loan arrangements with the PWLB.

Borrowing in advance of need

32. The Council has not borrowed in advance of need during the six month period ended 30th September 2020. Members should note that the total external debt projection for 31st March 2021 is as follows:

	£'000
Public Works Loans Board (PWLB)	232,598
Market Loans	62,500
WG Town Centre Loan	1,500
Salix (Public Lighting) Loan	982
Temporary Borrowing	1,568
Total	**299,148**

Debt Rescheduling

33. Debt rescheduling opportunities have been non-existent during 2020/21 due to the penalties involved in entering into such arrangements.

Compliance with Treasury and Prudential Limits

34. It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's original approved Treasury and Prudential Indicators (affordability) limits were included in the approved Treasury Management Strategy Statement as reported to Council on 6th March 2020.

35. During the financial year to date, the Council has operated within the Treasury Limits and Prudential Indicators set out in the Treasury Management Strategy Statement and in compliance with

the Treasury Management Practices. The Prudential and Treasury Indicators for 2020/21 onwards have been revised and are presented in Appendix 2.

Financial Impact

36. All relevant financial information is provided in the body of the report.

Integrated Impact Assessment

37. There is no requirement to undertake an Integrated Impact Assessment as this report is for information purposes.

Valleys Communities Impacts

38. No implications

Workforce Impacts

39. There are no workforce impacts arising from this report.

Legal Impacts

40. There are no legal impacts arising from this report.

Risk Management

41. There are several risks associated with the treasury management activities. These include interest rate fluctuations, counter party investment, international economic and political etc. The treasury management strategy is included within the Council's Corporate Risk Register.

Consultation

42. There is no requirement under the Constitution for external consultation on this item.

Recommendation

43. It is recommended that Members:

Note the Treasury Management activities to date this financial year, and how they relate to the proposed activities within the original 2020/21 Treasury Management Strategy and Annual Investment Strategy Statements.

Reason for Proposed Decision

44. To comply with requirements of the Code of Practice on Treasury Management.

Implementation of Decision

45. The decision is proposed for implementation after the three day call in period.

Appendices

46. Appendix 1 – Investment Position as at 30th September 2020
Appendix 2 – Prudential Indicators
Appendix 3 – Specified Investments - Current Criteria

List of Background Papers

47. Link Asset Services Mid-year Reporting Template
Investment and Borrowing Records 2020/21

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Appendix 1

Investment Position as at 30th September 2020

Borrower	Maturity	Rate %	Total £'000
Banks and Building Societies			
Lloyds Banking Group	95 day notice	0.20	10,000
Other Local Authorities			
Birmingham City Council	30th Nov 2020	0.14	5,000
Birmingham City Council	11th Dec 2020	0.16	5,000
Glasgow City Council	24th Jun 2021	0.30	10,000
Call Deposit			
Santander	Instant Access	0.10	44,600
Total			**74,600**

Appendix 2

PRUDENTIAL INDICATORS

PRUDENTIAL INDICATORS	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate
	£'000	£'000	£'000	£'000	£'000
Capital Expenditure	39,131	84,518	77,684	38,820	12,814
Capital Financing Requirement	342,874	358,420	344,093	345,597	338,289
Ratio of financing costs to net revenue stream	7.04%	6.72%	6.81%	6.67%	6.72%

Appendix 2

PRUDENTIAL INDICATORS

TREASURY MANAGEMENT INDICATORS	2019/20 Actual	2020/21 Original Estimate	2020/21 Revised Estimate	2021/22 Estimate	2022/23 Estimate
	£'000	£'000	£'000	£'000	£'000
Authorised Limit for External Debt: Borrowing and other long term liabilities	392,873	408,420	394,093	395,597	388,289
Operational Boundary for External Debt: Borrowing and other long term liabilities	372,873	388,420	374,093	375,597	368,289
External Debt (Gross)	307,872	277,580	299,148	298,147	277,996
Less Investments	(56,500)	(61,000)	(61,000)	(61,000)	(61,000)
Net Borrowing Position	**251,372**	**216,580**	**238,148**	**237,147**	**216,996**

Appendix 2

PRUDENTIAL INDICATORS

	2020/21 limit
	£'000
Upper Limit on Fixed Interest Rate Exposure	408,420
Lower Limit on Fixed Interest Rate Exposure	
Upper Limit on Variable Rate Exposure	204,210
Lower Limit on Variable Rate Exposure	
Upper Limit for Total Principal Sums Invested for Over 364 Days (per maturity date)	£25m

Maturity Structure of Fixed Rate Borrowing During 2019/20	**2019/20 Actual**	**2020/21 Estimate**		
	%	**%**	**Upper Limit %**	**Lower Limit %**
Under 12 months	3	0	15	0
12 months to 2 years	0	10	15	0
2 to 5 years	12	2	40	0
5 to 10 years	0	0	60	0
10 years and above	85	88	100	15

Appendix 3

Specified Investments Criteria

	Minimum 'High' Credit Criteria	**Funds Managed**	**Max Amount**	**Max Duration**
Term deposits				
Term deposits - Debt Management Office	N/A	In-house	Unlimited	1 year
Term deposits – local, police and fire authorities	N/A	In-house	£10m	1 year
Term deposits – Nationalised & Part Nationalised UK banks/Building Societies	Fitch short-term rating F1+, F1	In-house	£20m	1 year
Term deposits – UK banks/Building Societies	Fitch short-term rating F1+	In-house	£20m	1 year
Term deposits – UK banks/Building Societies	Fitch short-term rating F1	In-house	£15m	6 months or 185 days
Callable deposits				
Callable deposits – Debt Management Agency deposit facility	N/A	In-house	Unlimited	
Callable deposits – Nationalised & Part Nationalised UK banks/Building Societies	Fitch short-term rating F1+, F1	In-house	£20m	
Callable deposits – Nationalised & Part Nationalised UK banks/Building Societies	Fitch short-term rating F2	In-house	£10m	
Callable deposits - UK banks/Building Societies	Fitch short-term rating F1+ or F1	In-house	£15m *	
Term deposits – non UK banks	Fitch short-term rating F1+	In-house	£5m	6 months or 185 days

* Where necessary this limit may be temporarily exceeded with the Authority's bankers only.