

TREASURY MANAGEMENT ACTIVITY DURING 2020/21

BORROWING REQUIREMENT AND DEBT MANAGEMENT

1. On the 31st March 2021, the Authority had a reduction in its net borrowing need of £67M arising from its revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR) while useable reserves and working capital the underlying resources available for investments. These are the core drivers of TM Activity and the year-on-year change is summarised in table 1 below.
2. The Authority's current strategy, as we have an increasing borrowing requirement, is to minimise both external borrowing and investments and to only borrow to the level of the net borrowing requirement. The reasons for this are to reduce credit risk, take pressure off the Council's lending list and also to avoid the cost of carry existing in the current interest rate environment. This has resulted in an increase of our internal borrowing of £36.3M for 20/21 from £163.65M to £199.92M.

Table 1 – Balance Sheet Summary

	31-Mar-20 Actual	31-Mar-21 Strategy	31-Mar-21 Actual	31-Mar-21 Movement in year
	£M	£M	£M	£M
General Fund CFR	339.58	349.95	337.18	(12.77)
Housing CFR	169.13	177.48	169.13	(8.35)
Total CFR	508.71	527.43	506.31	(21.12)
Less Other Debt Liabilities*	(67.83)	(64.44)	(64.44)	0.00
Loans CFR	440.88	462.99	441.87	(21.12)
Less External Borrowing**	(277.23)	(231.59)	(241.95)	(10.36)
Internal (over) Borrowing	163.65	231.40	199.92	(31.48)
Less Usable Reserves	(174.55)	(178.40)	(208.52)	(30.12)
Less Working Capital Surplus	(58.01)	(58.01)	(58.29)	(0.28)
New Borrowing or (Investments)	(68.91)	(5.01)	(66.89)	(61.88)

* finance leases, PFI liabilities and Transferred debt that form part of the authority's total debt

3. The forecast movement in coming years is one of the Prudential Indicators (PIs). When the strategy was updated in February 2021, the CFR for 31 March 2021 was estimated at £527.43M, the Council's actual CFR at the end of the year was £506.31M. This decrease (£20.12M) was due to slippage in borrowing on the capital programme, £12.77M on the General Fund and £8.35M on HRA. In addition, external borrowing was £10.36M less and usable reserves and working balances were £30.14M higher than expected (but are expected to be utilised during 21/22) resulting in our need to borrow being reduced by £61.89M in year.

Actual Movement in year is shown in the following table.

Table 2 – Capital Financing Requirement Movement in year

Capital Financing Requirement	31/03/2020	31/03/2021	31/03/2021	31-Mar-21
	Actual	Forecast Revised Strategy	Actual	Movement since last reported position
	£M	£M	£M	£M
Balance Brought forward	334.02	339.58	339.58	0.00
New Borrowing	17.26	20.28	7.51	(12.77)
MRP	(6.06)	(6.50)	(6.50)	0.00
Appropriations (to) from HRA	(2.40)	0.00	0.00	0.00
Movement in Other Liabilities	(3.24)	(3.41)	(3.41)	0.00
Total General Fund Debt	339.58	349.95	337.18	(12.77)
HRA	169.13	177.48	169.13	(8.35)
Total CFR	508.71	527.43	506.31	(21.12)
Estimated Debt (<i>see below for breakdown</i>)	345.07	359.90	306.39	(53.51)
Under / (Over) Borrowed	163.64	167.53	199.92	32.39

NB "MRP" in the table = Minimum Revenue Provision – a provision for repayment of loans

4. The movement in actual external debt and usable reserves combine to identify the Authority's borrowing requirement and potential investment strategy in the current and future years.
Replacement of maturing debt was deferred due to the increase in reserves and a corresponding reduction in our net borrowing need. This is shown in the tables below together with activity in the year.

5. **Table 3: Borrowing and Investment Position**

	31-Mar-20 Actual £M	31-Mar-20 Average Yield / Rate %	31-Mar-21 Actual £M	31-Mar-21 Average Yield / Rate %	31-Mar-22 Estimated Balance £M
Long Term Borrowing					
Public Works Loan	257.87	3.30	222.59	2.72	388.85
LOBO Loans from Banks	9.00	4.86	9.00	4.86	9.00
	266.87	3.36	231.59	2.75	397.85
Short Term Borrowing					
Other Local Authorities	10.00	0.75	10.00	0.28	10.00
Other	0.36		0.36	0.28	
Total External Borrowing	277.23	3.03	241.95	2.75	407.85
Other Long Term Liabilities					
PFI Schemes	54.00	8.82	50.97	9.16	47.52
Deferred Debt Charges (HCC)	13.83	2.61	13.47	2.13	13.10
Total Gross External Debt	345.06	4.08	306.39	3.78	468.46
Investments:					
Managed In-House					
Cash (Instant access)	(31.22)	0.77	(30.13)	0.01	(10.00)
Long Term Bonds	(3.17)	5.30	(3.17)	5.30	(3.00)
Managed Externally					
Pooled Funds (CCLA)	(26.76)	4.40	(26.57)	4.16	(27.02)
Total Investments	(61.15)	4.03	(59.87)	4.26	(40.02)
Net Debt	283.91		246.52		428.44

6. **Table 4: Movement in Borrowing during the year**

Movement during the year	2019/20	31-Mar-21	2020/21	Average Life
	Actual £M	Movement £M	Actual £M	
Long-term borrowing Carried Forward	206.34		266.87	
Maturities in year	(39.47)		(35.29)	
New borrowing taken in year	100.00		0.00	
Net Long Term Borrowing	266.87	(35.29)	231.59	21 Years
Short-term borrowing Carried Forward	40.36		10.36	
Maturities in year	(54.00)		40.00	
New borrowing taken in year	24.00		(40.00)	
Net Short Term Borrowing	10.36	0.00	10.36	2 Months
Total Borrowing at 31st March	277.23	(35.29)	241.95	

Please note that these figures do not reflect the accounting convention of moving loans maturing in the year from long term to short term so will differ from the maturity analysis.

7. The maturity analysis of the Council's debt at 31 March 2021 is further analysed below. Debt due in one year includes both short term and long term loans due in year, LOBO loans are shown as uncertain as although they are within the call option they are unlikely to be called in the current interest environment.

8. **Table 5: Maturity Structure of Borrowing**

Total Financial Liabilities	Outstanding 31 March 2021	% of Total Portfolio
	£M	%
Source of Loan		
Public Works Loan Board	222.59	92
Other Financial Institutions (borrowing)	19.36	8
	241.95	100
Analysis of Loans by Maturity		
Less than 1 Year	19.10	8
Between 1 and 2 years	6.00	2
Between 2 and 5 years	18.00	7
Between 5 and 10 years	30.00	12
Between 10 and 20 years	31.00	13
Between 20 and 40 years	124.60	51
Over 40	4.25	2
Uncertain Date**	9.00	4
	241.95	100

Borrowing Update

9. In November 2020 the PWLB published its response to the consultation on 'Future Lending Terms'. From 26th November the margin on PWLB loans above gilt yields was reduced from 1.8% to 0.8% providing that the borrowing authority can confirm that it is not planning to purchase 'investment assets primarily for yield' in the current or next two financial years. Authorities that are purchasing or intending to purchase

	<p>investment assets primarily for yield will not be able to access the PWLB except to refinance existing loans or externalise internal borrowing. As part of the borrowing process authorities will now be required to submit more detailed capital expenditure plans with confirmation of the purpose of capital expenditure from the Section 151 / Section 95 Officer. The PWLB can now also restrict local authorities from borrowing in unusual or large amounts.</p> <p>Acceptable use of PWLB borrowing includes service delivery, housing, regeneration, preventative action, refinancing and treasury management. Misuse of PWLB borrowing could result in the PWLB requesting that Authority unwinds problematic transactions, suspending access to the PWLB and repayment of loans with penalties.</p> <p>Competitive market alternatives may be available for authorities with or without access to the PWLB. However, the financial strength of the individual authority and borrowing purpose will be scrutinised by commercial lenders.</p> <p>Following a review of the capital programme the Authority is not planning to purchase any investment assets primarily for yield within the next three years and so is able to take advantage of the reduction in the PWLB borrowing rate.</p>
10.	<p>Municipal Bonds Agency (MBA): The MBA revised its standard loan terms and framework agreement. Guarantees for the debt of other borrowers are now proportional and limited and a requirement to make contribution loans in the event of a default by a borrower has been introduced. The agency has issued 5-year floating rate and 40-year fixed rate bonds in 2020, in both instances Lancashire County Council is the sole borrower and guarantor. A planned third bond issuance by Warrington Borough Council was withdrawn in early December after the reduction in PWLB borrowing rates.</p> <p>If the Authority intends future borrowing through the MBA, it will first ensure that it has thoroughly scrutinised the legal terms and conditions of the arrangement and is satisfied with them.</p>
11.	<p>UK Infrastructure Bank: In his March 2021 budget the Chancellor confirmed that a UK Infrastructure Bank will be set up with £4bn in lending earmarked for local authorities from the summer of 2021. Loans will be available at gilt yield plus 0.60%, 0.20% lower than the PWLB certainty rate. A bidding process to access these loans is likely with a preference to projects likely to help the government meet its Net Zero emissions target. However other “high value and complex economic infrastructure projects” may also be considered.</p>
<u>Borrowing Strategy</u>	
12.	<p>At 31st March 2021 the Authority held £241.95M of loans, (a decrease of £35.28M since 31st March 2020), as part of its strategy for funding previous and current years’ capital programmes. Outstanding loans are summarised in Table 4 and 5 above.</p>
13.	<p>The Authority’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 Authority’s long-term plans change being a secondary objective.</p>
14.	<p>In keeping with these objectives short term borrowing was kept to a minimum, while existing loans were allowed to mature without replacement. We have remained under our CFR limit and had internal borrowing of £199.92M at the end of the year.</p> <p>This strategy enabled the Authority to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.</p>

15.	The PWLB remained the Council's preferred source of long term borrowing given the transparency and control that its facilities continue to provide, however PWLB funding margins have lurched quite substantially and there remains a strong argument for diversifying funding sources, particularly if rates can be achieved on alternatives which are below gilt yields + 0.80%.
16.	Due to the continued depressed markets and the 'cost of carry' associated with long term debt, the Council deferred long term borrowing and continued to use internal resources to finance the capital programme to minimise the cost of TM by keeping debt interest payments as low as possible without compromising the longer-term stability of the portfolio.
17.	This will be kept under review during 2021/22 with the need to resource an increasing capital programme, which will be reported to Council in September and February as part of the capital review, and projected rising interest rates (although at historically low rates). The Authority with its advisor Arlingclose will evaluate and pursue options for lower cost solutions and opportunities, together with the 'cost of carry' and breakeven analysis.
18.	The Authority'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.

Lender's Option Borrower's Option Loans (LOBOs)

19.	The council continues to hold £9M of LOBO loans where the lender has the option to propose an increase in the interest rate at set dates, following which the council has the option to either accept the new rate or to repay the loan at no additional cost. All of these LOBOS had options during the year, none of which were exercised by the lender, but if they were it is likely that they would be replaced.
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Other Debt Activity

20.	Although not classed as borrowing the Council has previously raised capital finance via Private Finance Initiative (PFI). The balance at the end of the year, after allowing for repayment in year of £3.04M is £50.97M.
21.	In addition, the Authority holds debt in relation to debt transferred from Hampshire County Council on the 1 April 1997 when we became a unitary authority, of £13.46M. This is being repaid over 50 years at £0.37M per annum.

INVESTMENT ACTIVITY

22.	Both the CIPFA and DCLG's Investment Guidance requires the council to invest prudently and have regard to the security and liquidity of investments before seeking the optimum yield. The Authority'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 income returns. Hence the activity cannot be simply measured against returns made over the year.
23.	The Authority received central government funding to support small and medium businesses during the coronavirus pandemic through grant schemes. This was invested in short-dated, liquid instruments such as call accounts and Money Market Funds until dispersed which led to higher investment balances throughout the year, although interest rates were at all-time lows averaging 0.01% for short term

	investments. The Council maintained its strategy of offsetting investment and borrowing to reduce treasury costs.																																										
24.	The council has held significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During 2020/21 the council's investment balances have ranged between £53.38M and £114.07M. Movement in year is summarised in the table below:																																										
25.	<p>Table 6: Investment activity during the year</p> <table border="1"> <thead> <tr> <th></th> <th>Balance on 01/04/2020</th> <th>Investments Repaid</th> <th>New Investments</th> <th>Balance on 31/03/2021</th> <th>(Increase)/ Decrease in Investment for Year</th> <th>Average Life of Investments</th> </tr> <tr> <th></th> <th>£M</th> <th>£M</th> <th>£M</th> <th>£M</th> <th>£M</th> <th>Life</th> </tr> </thead> <tbody> <tr> <td>Multi- National Bonds (not subject to bail in)</td> <td>(3.17)</td> <td>0.01</td> <td>(0.01)</td> <td>(3.17)</td> <td>(0.00)</td> <td>1.47 years</td> </tr> <tr> <td>Money Market Funds and Call Account</td> <td>(31.22)</td> <td>431.68</td> <td>(430.59)</td> <td>(30.13)</td> <td>1.09</td> <td>1 day</td> </tr> <tr> <td>Government & Local Authority Managed Externally (CCLA Pooled funds)</td> <td>0.00 (26.76)</td> <td>208.02 0.30</td> <td>(208.02) (0.11)</td> <td>0.00 (26.57)</td> <td>0.00 0.19</td> <td>Unspecified</td> </tr> <tr> <td>Total Investments</td> <td>(61.15)</td> <td>640.01</td> <td>(638.73)</td> <td>(59.87)</td> <td>1.28</td> <td></td> </tr> </tbody> </table>		Balance on 01/04/2020	Investments Repaid	New Investments	Balance on 31/03/2021	(Increase)/ Decrease in Investment for Year	Average Life of Investments		£M	£M	£M	£M	£M	Life	Multi- National Bonds (not subject to bail in)	(3.17)	0.01	(0.01)	(3.17)	(0.00)	1.47 years	Money Market Funds and Call Account	(31.22)	431.68	(430.59)	(30.13)	1.09	1 day	Government & Local Authority Managed Externally (CCLA Pooled funds)	0.00 (26.76)	208.02 0.30	(208.02) (0.11)	0.00 (26.57)	0.00 0.19	Unspecified	Total Investments	(61.15)	640.01	(638.73)	(59.87)	1.28	
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26.	Security of capital has remained the council's main investment objective. This has been maintained by following the Authority's counterparty policy as set out in its TM Strategy Statement for 2020/21. 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, which is supplied by our advisors. 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.																																										
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27.	Counterparty credit quality was assessed and monitored with reference to credit ratings (the Authority's minimum long-term counterparty rating is A-) across rating agencies Fitch, S&P and Moody's); for financial institutions analysis of funding structure and susceptibility to bail-in, credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. The authority also used secured investments products that provide collateral in the event that the counterparty cannot meet its obligations for repayment.																																										
28.	The table below summarises the Council's investment portfolio at 31 March 2021 by credit rating and confirms that all investments were made in line with the Council's approved credit rating criteria:																																										

Table 7: Credit ratings of Investments held at 31st March 2021

Credit Rating	Long Term		Short Term	
	2020	2021	2020	2021
	£000	£000	£000	£000
AAA	3,013	1,009	295	2,142
AA+			0	0
AA			10	0
AA-			16,839	12,000
A+			12,000	18,028
A			2,368	102
A-				
Unrated local authorities	0	0		
Shares in unlisted companies	20	20		
Unrated pooled funds	26,469	26,281	141	292
Total Investments	29,502	27,310	31,653	32,564

29. **Benchmarking:** Our advisors produce quarterly benchmarking which shows the breakdown of our investments and how we compare to their other clients and other English Unitary. Details can be seen in Appendix 3. It shows that on average the return on our internal investments at 0.49% is higher than the average of 0.15% and our overall return including the Local Authority Property Fund (income only) is 4.42% as opposed to the average of 3.85%. This has been achieved without impacting on our average credit rating which at AA- which is higher than the average for both other Local Authorities and Unitary Authorities at A+.

Liquidity Management

30. In keeping with the DCLG's Guidance on Investments, the Council maintained a sufficient level of liquidity through the use of Money Market Funds and call accounts. There is no perceived risk that the Council will be unable to raise finance to meet its commitments. The Council also has to manage the risk that it will be exposed to replenishing a significant proportion of its borrowing at a time of unfavourable interest rates. The Council would only borrow in advance of need where there is a clear business case for doing so and will only do so for the current capital programme or to finance future debt maturities.

Externally Managed Funds

31. The Council has invested £27M in property funds which offer the potential for enhanced returns over the longer term but will be more volatile in the shorter term. These funds are managed by professional fund managers which allows the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments.
32. During the initial phase of the pandemic, similar to many other property funds, dealing (i.e. buying or selling units) in the CCLA Local Authorities' Property Fund was suspended by the fund in March 2020 and lifted in September. There was also a change to redemption terms for the CCLA Local Authorities Property Fund; from September 2020 investors are required to give at least 90 calendar days' notice for redemptions.
33. During 2020/21 this investment returned an average yield of 4.25% against the initial investment. Due to market conditions the value of the fund fell from £26.47M at 31 March 2020 to £26.28M a movement of £0.19M in the year, a reduction of £0.72M

against the original investment. This notional “loss” at year end would only be a cost to the Authority at the point the investment is sold as the Authority is using the alternative fair value through profit and loss (FVPL) accounting and must defer the funds’ fair value losses to the Pooled Investment Fund Adjustment Account until 2023/24.

The market value of the investment has continued to improve against its lowest point in August 2020 (£25.29M) and at June 2021 was £27.18M, an increase of £0.90M since March.

34. 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 Authority’s investment objectives is 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 long-term and the Authority’s latest cash flow forecasts, investment in these funds has been maintained.

Non – Treasury Investments

35. 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.

36. Between 2016 and 2017, SCC implemented a strategy to invest in commercial properties with the expected return on investment being used to fund council services, known as the Property investment fund (PIF). To date the authority has purchased 3 properties. Details of the properties purchased are shown in the table below. The rate of return on these investment in 2020/21 was 6.07% gross and 2.17% net (after borrowing costs of £1.16M were incurred), which therefore represents a contribution to the revenue account of around £0.64M.

37. All of the properties remain fully let and the tenants are meeting their financial obligations under the leases and there are currently no concerns regarding the property that has currently fallen in value below the debt outstanding on it due to the current financial environment.

38. **Table 8: Property Investment Fund**

Property	Actual	31.03.2020 Actual		31.03.2021 Actual		Outstanding Debt 31.03.2021
	Purchase Cost £M	Value in Accounts	Gain or (Loss) in Year	Value in Accounts	Gain or (Loss) in Year	£M
Property 1	6.47	6.30	0.03	5.21	(1.09)	5.92
Property 2	14.69	10.80	(3.07)	10.32	(0.48)	13.44
Property 3	8.53	8.39	0.22	8.73	0.34	7.81
	29.69	25.49	(2.82)	24.26	(1.23)	27.17