

Treasury Management

Borrowing and Investments

1. The table below shows the year's opening balance of borrowing and investments, current levels and those predicted for year-end. Forecast borrowing is currently based on month 3 capital monitoring and will be subject to review during the year.

Lower official interest rates have continued to lower the cost of short-term, temporary loans and investment returns from cash assets that can be used in lieu of borrowing. The Authority maintained its strategy of keeping borrowing and investments below their underlying levels in order to reduce risk and make a net saving.

2.

	31-Mar-21 Actual £M	31-Mar-21 Average %	30-Jun-21 Actual £M	30-Jun-21 Average %	31-Mar-22 Forecast £M	31-Mar-21 Forecast %
Long Term Borrowing						
Public Works Loan	222.59	2.72	219.84	2.77	388.85	2.74
LOBO Loans from Banks	9.00	4.86	9.00	4.86	9.00	4.86
	231.59	2.75	228.84	2.80	397.85	2.82
Short Term Borrowing						
Other Local Authorities	10.00	0.28	0.00	0.28	10.00	0.06
Other	0.36	0.28	0.36	0.28	0.36	0.06
Total External Borrowing	241.95	2.75	229.20	2.80	408.21	2.78
Other Long Term Liabilities						
PFI Schemes	50.97	9.16	49.24	8.82	47.52	9.16
Deferred Debt Charges (HCC)	13.47	2.13	13.28	2.61	13.10	2.13
Total Gross External Debt	306.39	3.78	291.73	4.08	468.82	3.78
Investments:						
Managed In-House						
Government & Local Authority	0.00	0.00	0.00	0.00		
Cash (Instant access)	(30.13)	0.01	(27.74)	0.01	(10.00)	0.03
Cash (Notice Account)	0.00	0.00	0.00	0.00	0.00	0.00
Long Term Bonds	(3.17)	5.30	(1.06)	5.27	(1.10)	5.27
Managed Externally						
Pooled Funds (CCLA) & Shares	(26.57)	4.16	(27.02)	3.81	(27.02)	3.00
Total Investments	(59.87)	4.26	(55.83)	3.85	(38.12)	2.29
Net Debt	246.52		235.90		430.70	

3. After taking into account maturing and new debt requirements in year and a forecast reduction in investment balances, net borrowing is expected to increase by £184.18M for the year.

This will change throughout the year as capital plans firm up and actual cash flow are known and will be reported at the next quarter.

4. The interest cost of financing the council's long term and short term loan debt is charged to the general fund revenue account and is detailed below together with a summary of performance to date.

	<u>Borrowing</u>
5.	The forecast cost of financing the council's loan debt is £16.65M of which £5.19M relates to the HRA, however this will be subject to movement as the need for further borrowing for the remainder of the year becomes more certain.
6.	<p>Short term interest rates have remained low and are likely to do so for the remainder of the year and offer good value, which we will utilise to fund any further borrowing needs in the year, unless an opportunity arises to secure a long term loan at advantageous rates or to provide certainty for the portfolio.</p> <p>Although we currently do not have any short term debt, we anticipate borrowing from September onwards to replace maturing long term debt, expected reduction in reserves and to fund the forecast capital programme for the year, until a decision is taken with regards to long term borrowing. Any increase in short term borrowing costs will be offset by a reduction in long term costs. This is later than previously reported as cash flows have remained higher than expected.</p>
7.	<p>PWLB: Local authorities can borrow from the PWLB provided they can confirm they are not planning to purchase 'investment assets primarily for yield' in the current or next two financial years, with confirmation of the purpose of capital expenditure from the Section 151 Officer. Acceptable use of PWLB borrowing includes service delivery, housing, regeneration, preventative action, refinancing and treasury management.</p> <p>Competitive market alternatives may be available however, the financial strength of the individual authority and borrowing purpose will be scrutinised by commercial lenders.</p>
8.	<p>Municipal Bonds Agency (MBA): The MBA is working to deliver a new short-term loan solution, available in the first instance to principal local authorities in England, allowing them access to short-dated, low rate, flexible debt. The minimum loan size is expected to be £25 million. Importantly, local authorities will borrow in their own name and will not cross guarantee any other authorities.</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>
9.	UK Infrastructure Bank: £4bn has been earmarked for lending to local authorities by the UK Infrastructure Bank. The availability of this lending to local authorities is due to commence in summer 2021 for which there is expected to be a bidding process. Loans will be available for qualifying projects at gilt yields plus 0.6%, which is 0.2% lower than the PWLB certainty rate.
	<u>Investment</u>
10.	<p>The Authority received central government funding to support small and medium businesses during the coronavirus pandemic through grant schemes which was temporarily invested in short-dated, liquid instruments such as call accounts and Money Market Funds and led to higher than expected cash flow whilst the cash was being disbursed. Investment balances have ranged between £86.05M and £43.02M during the year and are currently £55.83M.</p> <p>Continued downward pressure on short-dated cash means net returns on money market funds are low between 0.02% and zero even after some managers have temporarily lowered their fees. This supports our decision to only borrow for cash flow purposes at this stage as savings on borrowing costs more than offset the loss on short term investments.</p>

	The impact of COVID-19 will continue during the year and will be reported at each quarter and as part of Treasury Reports to Governance Committee.																																																																						
	<u>External Managed investments</u>																																																																						
11.	<p>The council has invested £27M in property funds as an alternative to buying property directly. As previously reported these funds offer the potential for enhanced returns over the longer term but may be more volatile in the shorter term and 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.</p> <p>Because these funds have no defined maturity date but are usually available for withdrawal after a notice period (90 days), their performance and continued suitability in meeting the Authority's investment objectives is regularly reviewed.</p>																																																																						
12.	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.																																																																						
13.	<p>Since the onset of the COVID-19 pandemic and the current global economic environment, the value of the fund fell below the original investment and was reported at £26.28M in the accounts at 31 March 2021, a reduction of £0.72M against the original investment but was an increase of £0.99M from its lowest point in August 2020.</p> <p>The market has continued to improve and at June 2021 the value was £27.18M, an increase of £0.90M since March and is now above the initial investment.</p> <p>The dividend for April to June has been estimated at £0.26M, 3.86% against original investment. This is lower than 2020/21 which was boosted by a significant level of one-off receipts. If rates remain at this level the total forecast dividend for the year is £1.02M.</p>																																																																						
	<u>Financial Review and Outlook</u>																																																																						
14.	<p>A summary of the external factors, which sets the background for Treasury, as provided by the council's treasury advisors, Arlingclose Ltd, is summarised below. The low for longer interest rate outlook theme that has been at the core of the recommended strategic advice for over a decade remains.</p> <table border="1"> <thead> <tr> <th></th> <th>Sep-21</th> <th>Dec-21</th> <th>Mar-22</th> <th>Jun-22</th> <th>Sep-22</th> <th>Dec-22</th> <th>Mar-23</th> <th>Jun-23</th> <th>Sep-23</th> <th>Dec-23</th> <th>Mar-24</th> <th>Jun-24</th> <th>Sep-24</th> </tr> </thead> <tbody> <tr> <td>Official Bank Rate</td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td> <td></td> </tr> <tr> <td>Upside risk</td> <td>0.15</td> <td>0.15</td> <td>0.15</td> <td>0.15</td> <td>0.30</td> <td>0.30</td> <td>0.30</td> <td>0.30</td> <td>0.30</td> <td>0.30</td> <td>0.30</td> <td>0.30</td> <td>0.30</td> </tr> <tr> <td>Arlingclose Central Case</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> <td>0.10</td> </tr> <tr> <td>Downside risk</td> <td>0.10</td> <td>0.15</td> <td>0.20</td> <td>0.20</td> <td>0.20</td> <td>0.20</td> <td>0.20</td> <td>0.20</td> <td>0.20</td> <td>0.20</td> <td>0.20</td> <td>0.20</td> <td>0.20</td> </tr> </tbody> </table>		Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Official Bank Rate														Upside risk	0.15	0.15	0.15	0.15	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	Arlingclose Central Case	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	Downside risk	0.10	0.15	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
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15.	Arlingclose expects Bank Rate to remain at the current 0.10% level. The risk of movement in Bank Rate in the short term is low.																																																																						
16.	The medium-term global economic outlook has continued to improve with the rollout of vaccination programmes. The UK has continued to benefit from its initial rapid vaccine rollout and has shifted focus onto second vaccinations to increase protection to counter a third wave of Covid variant.																																																																						

	<p>The opening up of the UK economy in Q2/Q3 will continue to prompt a sharp increase in GDP. While downside risks seem to have fallen somewhat after recent trends in GDP and labour, the upside risks remain relatively balanced with the MPC reiterating its commitment not to tighten policy until there is clear evidence that the recovery is eliminating spare capacity in the economy.</p>
17.	<p>Inflation has moved above the Bank of England's 2% target. Alongside the increase in commodity prices, the MPC has acknowledged the prospect of a sharper upturn in inflation, with the potential CPI could rise above 3% in the coming months. However, the nature of the commodity price rise and the base effect easing, this is likely a more transitory effect.</p>
18.	<p>Gilt yields could continue to increase in the short term but will begin to plateau and reduce once the market's expectation of rises in Bank Rate and inflation fears subside. Longer term yields may face upward pressure towards the end of Arlingclose's forecast period as the economy moves back to a sustained footing and policy expectations start to strengthen.</p>
19.	<p>Downside risks remain – the damage from the pandemic will have lasting effects and there is the risk of further virus mutations due to the uneven global rollout of vaccines. Downside risks also arise from potential future vaccine shortages as the global demand for vaccines increases.</p>
	<p><u>Credit background</u></p>
20.	<p>Economic resurgence from coronavirus pandemic continued to dominate the first quarter of the financial year. In the biggest inoculation programme the country has ever undertaken, over 44 million people in the UK had received their first dose of a COVID-19 vaccine with 32 million also having a second dose.</p> <p>The Bank of England (BoE) held Bank Rate at 0.1% throughout the period and maintained its Quantitative Easing programme at £895 billion, unchanged since the November 2020 meeting. In its June 2021 policy announcement, the BoE expected the economy to experience a temporary period of strong GDP growth and above-target CPI inflation, after which growth and inflation is expected to fall back.</p> <p>There were, however, two-sided risks around this central path, and it is possible that near-term upward pressure on prices could prove somewhat larger than expected. The Bank's Monetary Policy Committee does not intend to tighten monetary policy at least until there is clear evidence that significant progress is being made in eliminating spare capacity and achieving the 2% inflation target sustainably. Government initiatives continued to support the economy over the quarter, following the range of measures announced by the Chancellor in the 2021 Budget, which included extending the furlough (Coronavirus Job Retention) scheme until September 2021.</p>
21.	<p>Ongoing monetary and fiscal stimulus together with improving economic growth prospects and successful vaccine rollout programmes continued to boost equity markets over the period. The Dow Jones reached a record high during the period while the UK-focused FTSE 250 index was back above pre-pandemic levels and the more internationally focused FTSE 100 had recouped around three-quarters of 2020 losses.</p> <p>Inflation worries continued during the period but declines in bond yields between April and June suggest bond markets may be expecting any general price increases to be less severe, or more transitory, that was previously thought.</p>

	<p>The 5-year UK benchmark gilt yield began the financial year at 0.36% before declining to 0.32% by the end of June 2021. Over the same period the 10-year gilt yield fell from 0.80% to 0.71%, despite jumping to 0.90% in May. The 20-year yield declined from 1.31% to 1.21%. 1-month, 3-month and 12-month SONIA bid rates averaged 0.03%, 0.02% and 0.15% respectively over the period.</p>
22.	<p>The successful vaccine rollout programme is 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</p>
23.	<p>There were only a small number of credit rating actions over the period, none of which impacted on our investment decisions.</p>
24.	<p><u>Investment Performance</u></p>
25.	<p>The council's advisors undertake quarterly investment benchmarking across its client base. As reported previously our portfolio was more diversified and at higher interest rates than the average as a result of moving into the bond programme earlier than most clients, but there is now more competition for bonds from both government bodies and other local authorities, so opportunities to replace maturing bonds are limited and we will see a fall in suitable instruments. With this in mind, and following discussions with our advisors, it was decided to move more into property funds, which are a longer term investment, and to short term investments for cash flow purposes.</p>
26.	<p>Our current investments in bonds has reduced from £3M to £1M following maturities in 2021/22 and we maintained the property funds at £27M, with all other cash being placed in short term deposits as shown in paragraph 2.</p>
27.	<p>As detailed in paragraph 11 our cash balances have continued to be higher than forecast. As a result, we had £27.74M in short term investment which is above our normal working balances. Our target is to reduce this to a £10M working balance to reduce borrowing and therefore net interest costs but this will be dependent on actual capital spend and movement in balances.</p>
28.	<p>Investments managed internally are currently averaging a return of 0.19% which is higher than the average unitary authority at 0.09% whilst still maintaining the same average credit rating of A+. Total income return at 2.31% is also higher than the average for both unitary (0.98%) and LA's (0.82%), this is primarily due to historic investment in EIB bonds which return 5.27%, although on a small balance of £1M, since maturities cannot be replaced at the same level. It should also be noted that in line with our strategy to hold minimum investments to reduce borrowing costs that our investment is below the average at £55.9M compared to £83.8M for other unitaries, 49% of which is held in strategic funds which offer higher return over the long term as detailed in paragraphs 11 to 14 above.</p> <p>In addition due to the increase in the capital value of our external funds of +6.94% our total investment return at 5.68% is significantly higher than the average LA's at 2.13% and the average unitary at 2.52% across Arlingclose's client base, but as previously reported it is the income return that is the driver to invest plus they are deemed less risky than buying individual properties and do not constitute capital spend.</p>

