Rother District Council

Report to:	Audit and Standards
Date:	7 December 2020
Title:	Treasury Management Update
Report of:	Antony Baden – Finance Manager
Purpose of Report:	To note the Council's treasury activities for the second financial quarter ending the 30 September 2020.
Officer Recommendation(s):	It be **RESOLVED**: That the report be noted.

Introduction

1. Cabinet approved the Council's Investment Strategy for 2020/21 on 10 February 2020 (Minute CB19/93 refers). The strategy requires regular reports to be presented to the Audit and Standards Committee on the Council's treasury management activities. In managing these activities, the Council follows the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management. This report implements best practice in accordance with the Code. Members are also reminded that investment activity is reported through the Members' Bulletin.

2. This report focuses on the financial period ending on 30 September 2020.

Financial Investments Review

3. The Council continues to hold investments in call accounts with the major financial UK institutions. It also holds investments totalling £8m in Property Funds.

4. The Council's investment policy is governed by the Ministry of Housing, Communities and Local Governments' investment guidance, which has been implemented in the approved Annual Investment Strategy. The investment activity to date conforms to the approved strategy and the Council had no liquidity difficulties.

5. As at 30 September 2020, the Council's total investments are £32.430m. There is £11,927m of borrowing and the Capital Financing requirement is forecast to be £40.287m by the 31 March 2021.

6. The total income from investments is currently forecast at £302,000, which is £50,000 higher than the previous forecast. The largest returns are from the Council's property funds, which are currently delivering an average rate of return of between 3.47% and 3.86% on investments.

7. As at 30 September 2020, the Council held £24.4m in its General Account (GA). This included £7.6m, which is the balance of Government funding for the

payment of business and discretionary grants during lockdown. It is expected that this will have to be returned at some point soon, so it has not been invested.

8. The GA funds also need to be kept available for other large payments such as Council Tax and Business Rates payments to preceptors and capital project expenditure as referred to in paragraph 13.

9. The table below shows that interest rates for call deposit accounts from main banks are zero or near zero so it is sensible to have the GA funds readily available for the reasons explained in paragraphs 7 and 8. The investment portfolio as at 30 September 2020 is shown in the table below:

Deposit	Type of account	Maturity Date	Amount £	Interest Rate	Share %
Lloyds - General (RFB)	Call	N/A	24,427,456	0.00%	75.32%
Bank of Scotland (RFB)	Call	N/A	11	0.00%	0.00%
Barclays - Call Account (NRFB)	Call	N/A	1,066	0.05%	0.00%
Santander - 31 Day Notice Account	31 Days Notice	N/A	1,658	0.27%	0.01%
CCLA Local Authority Property Fund	Long Term	N/A	5,000,000	3.86%	15.42%
HERMES Property Fund	Long Term	N/A	2,999,998	3.47%	9.25%
Total			**32,430,190**		**100.00%**
Total managed in-house			24,430,192		
Total managed externally			7,999,998		
Total Treasury Investments			**32,430,190**		

10. The Council's property funds continue to provide a sustainable return on investment as mentioned in paragraph 6 but as previously reported to Members, their market values have been adversely impacted by the Coronavirus pandemic. The current values are shown in the table below:

Name of Property Fund	Original Investment Value	Value at 30th June 2020	Value at 30th September 2020	Change
	£	£	£	£
CCLA Local Authority Property Fund	5,000,000	4,568,164	4,581,628	13,464
Hermes Property Fund	2,999,998	2,750,923	2,730,939	-19,984
Total	**7,999,998**	**7,319,087**	**7,312,567**	**-6,520**

11. Although the overall values have reduced by a further £6,520 the rate of decline is significantly lower than the previous quarter when the pandemic first started. However, the future is still very uncertain despite the recent announcement that a potential vaccine may be available by Christmas and further fluctuations should be expected before the overall economic situation improves.

Borrowing

12. The Council's underlying need to borrow is termed the Capital Financing Requirement (CFR). The Council manages this by organising its cash position

to ensure that enough cash is available to meet its capital plans and day-to-day cash flow requirements, in the cheapest and most efficient way.

13. The total expenditure and funding of the revised Capital Programme (CP) for 2020/21 is summarised in the following table:

	2020/21 Original Budget £ (000)	**2020/21 Revised Budget £ (000)**	**2020/21 Estimated Outturn £ (000)**
Capital Expenditure	**19,510**	**41,436**	**41,436**
Financing:			
Capital Receipts	1,240	1,085	1,085
Grants and Contributions	4,262	15,100	15,100
Borrowing	13,287	23,412	23,412
Capital Expenditure Charged to Revenue	721	1,839	1,839
Total Funding	**19,510**	**41,436**	**41,436**

14. The Council's CFR is not allowed to rise indefinitely so it is reduced by a statutory annual revenue charge, called the Minimum Revenue Provision (MRP), which is effectively a repayment of borrowing. The CP includes new borrowing in 2020/21 of £23.412m but even though it is expected to increase, the MRP charge will remain as originally budgeted because it is not charged in the first year of borrowing. The change in the CFR is shown in the following table:

Capital Financing Requirement	**2020/21 Original Budget £ (000)**	**2020/21 Revised Budget £ (000)**	**2020/21 Estimated Outturn £ (000)**
Opening Balance	17,117	17,117	17,117
Add unfinanced capital expenditure	13,287	23,412	23,412
Less Minimum Revenue Provision (MRP)	(242)	(242)	(242)
Closing Balance	**30,162**	**40,287**	**40,287**

15. The Council's borrowing position as at 30 September 2020 remains unchanged from the previous quarter and is shown in the table overleaf:

Borrowing position as at the 30th September 2020					
PWLB Ref:	**Amount o/s**	**Interest Rate**	**Term**	**Type**	**Full Year Repayments**
507499	£440,931	2.59%	50	Annuity	£16,102
507503	£440,905	2.58%	50	Annuity	£16,070
509130	£1,632,498	2.39%	50	Annuity	£56,729
509131	£1,000,000	2.24%	50	Maturity	£22,400
509165	£8,412,690	2.48%	50	Annuity	£297,572
Total Borrowing	**£11,927,025**				**£408,873**

16. The Council's borrowing activity is controlled by prudential indicators that form part of the approved Treasury Management Strategy (TMS). The Operational boundary is the maximum expected borrowing position whilst the Authorised limit allows for some headroom in case of unusual/unexpected cash outflows. The table below shows the borrowing limits and gross external debt level as at 30 September 2020.

Treasury Indicators	**30th Sept 2020 £ (000)**
Authorised Limit for External Debt	57,400
Operational boundary for External Debt	52,000
Gross External Debt (actual)	11,927
Remaining Authorised Limit for External Debt	**45,473**

17. Members may recall from the previous update that the Council had committed to a significant increase in the CP from 2020/21 and this would necessitate an increase in the borrowing limits mentioned in paragraph 16. At the Cabinet meeting on 2 November 2020, Members considered the Council's Medium-Term Financial Plan for 2021/22 to 2025/26 and approved a recommendation to update the borrowing limits in the TMS. The table below shows the newly approved borrowing limits.

Revised Treasury Indicators	**2020/21 £ (000)**	**2021/22 £ (000)**	**2022/23 £ (000)**	**2023/24 £ (000)**	**2024/25 £ (000)**	**2025/26 £ (000)**
Authorised Limit for External Debt	66,370	94,960	118,980	122,480	122,330	122,070
Operational boundary for External Debt	61,370	89,960	113,980	117,480	117,330	117,070

18. Net Financing Costs as a proportion of the Net Revenue Stream has reduced from 3.89% to 3.57% due to the increase in forecast interest income outlined in paragraph 6. The table overleaf compares the current forecast prudential indicators against the original budget.

Prudential Indicators	2020/21 Original Budget £ (000)	2020/21 Estimate Outturn £ (000)
Capital Expenditure Charged to Revenue	1,359	1,839
Capital Financing Requirement (CFR)	30,162	40,287
Annual Change in CFR	13,045	23,170
In-Year Borrowing Requirements	11,927	11,927
Ratio of Financing costs to Net Revenue Stream %	3.39%	3.57%

19. The Council continues to maintain an under-borrowed position, which means the CFR is not fully funded by loan debt but also managed by using reserves and balances. Returns remain low so this is a prudent strategy that also minimises the counterparty risk associated with placing investments.

Non-Treasury Investments

20. The pandemic has temporarily slowed activity in the Council's Property Investment Strategy (PIS) although expected income from the existing portfolio remains unchanged. This is shown below:

2020/21 Estimated Property Investment Income			
Property	**Rental Income £**	**MRP & Interest £**	**Net Income £**
14 Terminus Road	106,000	(31,793)	74,207
18-40 Beeching Road	88,080	(28,504)	59,576
16 Beeching Road	97,000	(31,391)	65,609
Glovers House	425,000	(275,458)	149,542
Market Square, Battle	195,000	(110,263)	84,737
Total	**911,080**	**(477,410)**	**433,670**

21. Although the Council has not made any further property purchases, negotiations are continuing with several parties and further acquisitions are expected over the next few months.

22. The budget for rental income from all investment properties is £1,919,840, made up of £1,008,760 for the existing assets and £911,080 for properties purchased through the PIS. Tenants are being pursued for rent arrears but because economic conditions are still difficult the forecast outturn for 2020/21 prudently includes a shortfall of £200,000, which would reduce overall income to £1,719,840 and equates to a gross return of 6.27%. After allowing for borrowing costs the expected return on PIS properties is 2.71%.

Economic Update and Outlook

23. There have been several developments since the previous update to Members. Having seen the number of Coronavirus infections brought under some sort of control during the summer months, the number of cases have since escalated significantly, leading to another national lockdown with the duration not yet known. The Government has again responded by announcing various support packages including further cash injections for local authorities, grants to local

businesses, ‘test and trace’ payments for lower paid people forced to self-isolate and the extension of the furlough scheme until March 2021.

24. Other developments include a possible change of political power in the United States where Joe Biden appears to have won the election. The protracted nature of the outcome had an initial impact on global stock markets, which have now settled. Closer to home the inconclusive nature of the BREXIT negotiations continues to cause economic uncertainty. Any trade deal needs to be ready for 1 January 2021 but there is no indication as to what? this may look like, assuming one can be agreed.

25. The Bank of England (BoE) base rate remains unchanged at 0.10% although PWLB rates have increased marginally. For example, the 50 year rate has recently hovered between 2.5% and 2.6% however, the Link Asset Services (the Council’s Treasury Management advisors) expect rates soon to stabilise to their previously predicted level (2.3%), thus ensuring that borrowing remains attractive both in the short and medium term, which is good news for the Council as it embarks upon its ambitious CP. The BoE has also announced further quantitative easing of £150 billion with effect from January in order to stimulate spending and investment.

26. The economic future remains difficult to predict but although the recovery is likely to be prolonged the announcement at the beginning of November of a vaccine breakthrough has provided some optimism.

27. House prices, boosted by the stamp duty holiday announced by the Chancellor in July of this year, have risen to a 21-year high and the surge is expected to continue. However, the stamp duty holiday finishes on 31 March 2021 and together with predicted rising unemployment, this presents a more pessimistic outlook.

28. The UK economy grew significantly in Quarter 3, recording Gross Domestic Product growth of 15.5% on Quarter 2, as lockdown restrictions were eased but it is still 9.7% lower than at the beginning of the year. Also, Quarter 3 growth started to tail off at the end and with another national lockdown in place, the outlook for Quarter 4 is much less positive. Link Asset Services have indicated it could be anywhere between a fall of 3.5% and growth of just 1.1%. They have also forecast unemployment peaking at 9% next year (currently 4.5%).

Conclusion

29. The investment activity conforms to the approved strategy and the Council has no liquidity difficulties.

30. The investment environment for treasury activities remains difficult and is likely to remain so for the foreseeable future. Absolute returns are expected to remain low. The diversification into Property Funds increases the overall return but is less liquid and carries greater capital risk than other investments.

31. The Council’s PIS is still expected to generate net returns of 2.7% but the risks associated with the long-term commitment to repay borrowing and the operational management of properties will remain.

Other Implications	Applies?	Other Implications	Applies?
Human Rights	No	Equalities and Diversity	No
Crime and Disorder	No	Consultation	No
Environmental	No	Access to Information	No
Sustainability	No	Exempt from publication	No
Risk Management	No		

Chief Executive:	Malcolm Johnston
Report Contact Officer:	Antony Baden
e-mail address:	antony.baden@rother.gov.uk
Appendices:	None
Relevant Previous Minutes:	None
Background Papers:	None
Reference Documents:	None