Rother District Council

Report to:	Audit and Standards Committee
Date:	21 June 2021
Title:	Treasury Management Update report
Report of:	Antony Baden – Finance Manager
Purpose of Report:	To note the Council's treasury activities for the fourth financial quarter ending 31 March 2021
Officer Recommendation(s):	It be **RESOLVED**: That the report be noted

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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 this 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 31 March 2021.

Financial Investments review

3. 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 has had no liquidity difficulties.

4. As at 31 March 2021, the Council's total investments were £32.047m. It has £11.869m of borrowing and the Capital Financing requirement was £18.168m as at 31 March 2021.

5. Since the Quarter 3 report to Members, the Council has slightly diversified its investment portfolio in order to spread risk and earn a small amount interest income. It continues to hold investments of £14.054m in Call accounts and now also holds £5.0m in an interest earning call account and £3.0m in a 31-day Notice account. All these investments are with the major financial UK institutions. The Council continues to hold £8.0m in Property Funds.

6. The total income from investments was £324,000, which is £16,000 lower than the previous forecast. The largest returns are from the Council's property funds, which delivered an average rate of return of between 3.64% and 4.14% on investments.

7. As at 31 March 2021, the Council held £14.1m in its General account, including Government funding for individuals and businesses in response to the pandemic. The unspent balance is £7.465m and will be returned to the MHCLG in June so it cannot be invested externally.

8. The General Account 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.

9. The table below shows that interest rates for call deposit accounts from main banks remain at or near to zero, so it is sensible to have the General Account funds readily available for the reasons explained in paragraphs 7 and 8. The investment portfolio as at 31 March 2021 is shown in the table below: -

Deposit	**Type of account**	**Maturity Date**	**Amount £**	**Interest Rate**	**Share %**
Lloyds - General (RFB)	Call	N/A	14,054,021	0.00%	43.85%
Bank of Scotland (RFB)	Call	N/A	11	0.00%	0.00%
Barclays - Call Account (NRFB)	Call	N/A	4,996,066	0.05%	15.59%
Santander - Call Account	Call	N/A	2,995,000	0.12%	9.35%
Santander - 31 Day Notice Account	31 Days Notice	N/A	2,001,660	0.27%	6.25%
CCLA Local Authority Property Fund	Long Term	N/A	5,000,000	4.14%	15.60%
HERMES Property Fund	Long Term	N/A	2,999,998	3.64%	9.36%
Total			**32,046,757**		**100.00%**
Total managed in-house			24,046,759		
Total managed externally			7,999,998		
Total Treasury Investments			**32,046,757**		

10. The Council's property funds continued to provide a good return on investment as mentioned in paragraph 6, but their market values fluctuated considerably during the pandemic. The table below shows how the values changed from the start of the pandemic in March 2020 during the financial year up until 31 March 2021:

Name of Property Fund	Original Investment Value	Value as at 31st Mar 2020	Value as at 30th Jun 2020	Value as at 31st Dec 2020	Value as at 31st Mar 2021	Change in Value	Year on Year Change
	£	£	£	£	£	£	£
CCLA Local Authority Property Fund	5,000,000	4,780,465	4,568,164	4,647,469	4,746,477	-253,523	-33,988
HERMES Property Fund	2,999,998	2,857,751	2,750,923	2,740,334	2,779,774	-220,224	-77,977
Total	**7,999,998**	**7,638,216**	**7,319,087**	**7,387,803**	**7,526,251**	**-473,747**	**-111,965**

11. The above table shows that the total value fell by £319,000 during the first quarter of 2020/21 due to the pandemic however, it can also be seen that it recovered during the remainder of the year and is now only £112,000 lower than at the same time last year. This includes a recovery of £139,000 since the last report to Committee.

12. Members will note that their current values are still £474,000 lower than their original values, although it is expected that they will continue to recover over time. However, although the market has reacted positively to the success of the vaccine rollout, the future remains uncertain and future adverse changes cannot be ruled out. It is not expected that the Council will need to call on this money in the short term.

Borrowing

13. The 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.

14. The Council had planned to significantly increase its capital investment programme in 2020/21, but the pandemic had a major impact on the pace of planned spend. This is reflected in the revised Capital Programme for 2020/21 and is summarised in the following table:

	2020/21 Original Budget £ (000)	**2020/21 Draft Outturn £ (000)**
Capital Expenditure	**19,510**	**5,477**
Financing:		
Capital Receipts	1,240	0
Grants and Contributions	4,262	2,470
Borrowing	12,649	2,530
Capital Expenditure Charged to Revenue	1,359	477
Total Funding	**19,510**	**5,477**

15. 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 change in the CFR is shown in the following table:

Capital Financing Requirement	**2020/21 Original Budget £ (000)**	**2020/21 Draft Outturn £ (000)**
Opening Balance	15,788	15,788
Add unfinanced capital expenditure	12,649	2,530
Less Minimum Revenue Provision (MRP)	(242)	(150)
Closing Balance	**28,833**	**18,168**

16. The Council's borrowing position as at 31 March 2021 has not changed from the previous quarter, because loan principal repayments are made at six monthly intervals. The following table reminds Members of the current position:

Borrowing position as at the 31st March 2021					
PWLB Ref:	**Amount o/s**	**Interest Rate**	**Term**	**Type**	**Full Year Repayments**
507499	£438,590	2.59%	50	Annuity	£16,102
507503	£438,558	2.58%	50	Annuity	£16,070
509130	£1,623,747	2.39%	50	Annuity	£56,729
509131	£1,000,000	2.24%	50	Maturity	£22,400
509165	£8,368,222	2.48%	50	Annuity	£297,572
Total Borrowing	**£11,869,117**				**£408,873**

17. The Council's borrowing activity is controlled by prudential indicators that form part of the approved Treasury Management Strategy. The Operational boundary is the maximum expected borrowing position, whilst the Authorised limit allows for some headroom in case of unusual/unexpected cash outflows. Members will recall that Council approved an increase to both limits on 21 December 2020 (Minute C20/51 refers) in response to an anticipated increase in capital project expenditure. The table below shows the new borrowing limits and gross external debt level as at 31 March 2021.

Treasury Indicators	**30th Mar 2021 £ (000)**
Authorised Limit for External Debt	66,370
Operational boundary for External Debt	61,370
Gross External Debt (actual)	11,869
Remaining Authorised Limit for External Debt	**54,501**

18. Since the Quarter 3 report, Net Financing Costs as a proportion of the Net Revenue Stream reduced slightly from 0.84% to 0.82%. The table below compares the current draft prudential indicators against the original budget.

Prudential Indicators	**2020/21 Original Budget £ (000)**	**2020/21 Draft Outturn £ (000)**
Capital Expenditure Charged to Revenue	1,359	477
Capital Financing Requirement (CFR)	28,833	18,168
Annual Change in CFR	12,407	2,380
In-Year Borrowing Requirements	11,927	11,869
Ratio of Financing costs to Net Revenue Stream %	3.62%	0.82%

19. The Council continues to maintain an under-borrowed position, which means the CFR is not fully funded by loan debt but is 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 in line with expectations. This is shown below:

2020/21 Draft Actual Property Investment Income			
Property	**Rental Income £**	**MRP & Interest £**	**Net Income £**
14 Terminus Road	106,000	(31,793)	74,207
18-40 Beeching Road	92,809	(29,287)	63,523
16 Beeching Road	97,000	(30,609)	66,391
Glovers House	437,244	(275,458)	161,785
Market Square, Battle	195,000	(65,124)	129,876
Total	**928,053**	**(432,271)**	**495,782**

21. The Council did not make any further property purchases in 2020/21, although negotiations are continuing with several parties and further acquisitions are expected in 2021/22.

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. The draft actual for 2020/21 is £1,860,620, which is £59,220 below budget due to factors such as void periods.

23. Tenants are being pursued for rent arrears and it is expected that there will be minimal write offs in 2020/21 as a result of the pandemic. However, economic conditions are still difficult and further rent write-offs cannot be ruled out. After allowing for borrowing costs the expected return on PIS properties is 2.82%.

Economic Update and Outlook

24. The Government recently outlined a timeline to lift restrictions and consequently the country is beginning to come out of its third national lockdown. It has set a deadline of 21 June 2021 for all restrictions to be lifted, but a high level of uncertainty remains especially with regards to the new Indian variant. At the time of writing, the uncertainty has not had an adverse impact on the speed of the economic recovery.

25. The continued success of the vaccination rollout programme continues to have a positive bearing on the markets and economic forecasts have been revised accordingly. The latest Office for Budget Responsibility have forecasted Gross Domestic Product (GDP) to increase by 7.5% in 2021 (previously 7.3% by mid-2022), although continued growth is expected to flatten out by the first quarter of 2022. These predictions are also borne out by an increase in the Purchasing Managers Index (PMI), which recently rose from 60.7 to a record high of 62.0 in April, (the PMI is regarded by economists as a strong barometer of future GDP growth).

26. It is a similar story for the European Union where the euro-zone composite PMI rose from 53.8 to 56.9, which was 1.8 higher than expected.

27. CPI inflation increased from 0.7% in March to 1.5% in April, mainly as a result of an increase in energy prices (partly driven by Ofgem increasing the energy price cap).

28. The Bank of England (BoE) base rate remains unchanged at 0.10% and is likely to remain at a similar level at least over the next 12 months. However, PWLB rates have increased slightly again in recent weeks, fluctuating between 1.90% and 2.01%. This has been driven by some market volatility in the Investments markets. The current 50-year PWLB rate is around 1.97%. Despite the small increase, borrowing remains an attractive option in both the short and medium term.

29. Global markets continue to settle down following various other events over the last six or so months, but Members should note that the future remains difficult to predict and future economic trends remain volatile.

Conclusion

30. The Council's investment activity conformed to the approved strategy in 2020/21 and had no liquidity difficulties.

31. The investment environment for treasury activities was difficult throughout the year 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.

32. The Council's PIS generated net returns of 2.82%, 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		

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Appendices:	None
Relevant Previous Minutes:	CB19/93 C20/51
Background Papers:	None
Reference Documents:	None