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| **Report To:** | **AUDIT PANEL** |
| **Date:** | 9 November 2021 |
| **Executive Member /Reporting Officer:** | Councillor Ryan – Executive Member – Finance and Economic Growth<br><br>Caroline Barlow – Assistant Director of Finance |
| **Subject:** | **TREASURY MANAGEMENT ACTIVITIES** |
| **Report Summary:** | This report provides a mid-year review of the Council's Treasury Management activities for 2021/22, including the borrowing strategy and the investment strategy. |
| **Recommendations:** | That the reported treasury activity and performance be noted. |
| **Links to Community Strategy:** | The Treasury Management function of the Council underpins the ability to deliver the Council's priorities. |
| **Policy Implications:** | In line with Council Policies. |
| **Financial Implications:**<br><br>**(Authorised by the Section 151 Officer)** | The achievement of savings on the cost of financing the Council's debt through repayment, conversion and rescheduling, together with interest earned by investing short term cash surpluses, is a crucial part of the Council's medium term financial strategy. This has to be carefully balanced against the level of risk incurred.<br><br>The Council held £127.205m of investments as at 30 September 2021 and the investment portfolio yield to date is 0.30% against the London Interbank Bid Rate (LIBID) benchmark of -0.08%. This represents an actual cash return of £0.195m, being £0.250m in excess of the benchmark. |
| **Legal Implications:**<br><br>**(Authorised by the Borough Solicitor)** | As there is a statutory duty for the Council to set, monitor and comply with its requirements to ensure a balanced budget, sound treasury management is a key tool in managing this process.<br><br>Demonstration of sound treasury management will in turn provide confidence to the Council that it is complying with its fiduciary duty to the public purse, and in turn allows the Council to better plan and fulfil its key priorities for the coming year.<br><br>Members should ensure they understand the meaning of **Appendix 1** and the outturn of prudential indicators they are being asked to approve, and the reasons for the same, before making their decision. |
| **Risk Management:** | Failure to properly manage and monitor the Council's loans and investments could lead to service failure and loss of public confidence. |

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| **Access to Information:** | The background papers relating to this report can be inspected by contacting Heather Green, Finance Business Partner by: |

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## 1. BACKGROUND

1.1 Cash-flow management is a core element of the Council's financial management activities. The Council operates a balanced budget, which broadly means cash raised during the year will meet cash expenditure. Treasury Management operations firstly ensure that cash flow is adequately planned, with short term surplus funds being invested. The investment strategy priorities are security (i.e. there is a low risk that the counterparty will default on the Council's investment), then liquidity (cash flow needs), and lastly, yield – providing adequate liquidity initially before considering maximising investment return.

1.2 The second main function of the treasury management service is the funding of the Council's capital investment plans, agreed as part of the annual budget setting process and updated throughout the financial year. These capital plans provide a guide to the borrowing need of the Council, essentially this is the long term cash flow planning to ensure the Council can meet its capital spending requirements. 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 management or cost reduction objectives.

1.3 Accordingly, 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. "*

## 2. INTRODUCTION

2.1 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2017) was adopted by this Council on 8 February 2012. 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 which set out 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) to Executive Cabinet 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 body is the Audit Panel.

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

- An economic update for the first six months of 2021/22;
- 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 2021/22;
- A review of the Council's borrowing strategy for 2021/22;
- A review of any debt rescheduling undertaken during 2021/22;
- A review of compliance with Treasury and Prudential Limits for 2021/22;

## 3. ECONOMIC UPDATE

3.1 The following economic update is provided by the Council's treasury management advisors, Link Group:

***UK.*** *The Monetary Policy Committee (MPC) voted unanimously to leave Bank Rate unchanged at 0.10% and made no changes to its programme of quantitative easing purchases due to finish by the end of this year at a total of £895bn; two MPC members voted to stop the last £35bn of purchases as they were concerned that this would add to inflationary pressures.*

*There was a major shift in the tone of the MPC's minutes at this meeting from the previous meeting in August which had majored on indicating that some tightening in monetary policy was now on the horizon, but also not wanting to stifle economic recovery by too early an increase in Bank Rate. In his press conference after the August MPC meeting, Governor Andrew Bailey said, "the challenge of avoiding a steep rise in unemployment has been replaced by that of ensuring a flow of labour into jobs" and that "the Committee will be monitoring closely the incoming evidence regarding developments in the labour market, and particularly unemployment, wider measures of slack, and underlying wage pressures." In other words, it was flagging up a potential danger that labour shortages could push up wage growth by more than it expects and that, as a result, CPI inflation would stay above the 2% target for longer. It also discounted sharp increases in monthly inflation figures in the pipeline in late 2021 which were largely propelled by events a year ago e.g., the cut in VAT in August 2020 for the hospitality industry, and by temporary shortages which would eventually work their way out of the system: in other words, the MPC had been prepared to look through a temporary spike in inflation.*

*So, in August the country was just put on alert. However, this time the MPC's words indicated there had been a marked increase in concern that more recent increases in prices, particularly the increases in gas and electricity prices in October and due again next April, are, indeed, likely to lead to faster and higher inflation expectations and underlying wage growth, which would in turn increase the risk that price pressures would prove more persistent next year than previously expected. Indeed, to emphasise its concern about inflationary pressures, the MPC pointedly chose to reaffirm its commitment to the 2% inflation target in its statement; this suggested that it was now willing to look through the flagging economic recovery during the summer to prioritise bringing inflation down next year. This is a reversal of its priorities in August and a long way from words at earlier MPC meetings which indicated a willingness to look through inflation overshooting the target for limited periods to ensure that inflation was 'sustainably over 2%'. Indeed, whereas in August the MPC's focus was on getting through a winter of temporarily high energy prices and supply shortages, believing that inflation would return to just under the 2% target after reaching a high around 4% in late 2021, now its primary concern is that underlying price pressures in the economy are likely to get embedded over the next year and elevate future inflation to stay significantly above its 2% target and for longer.*

*Financial markets are now pricing in a first increase in Bank Rate from 0.10% to 0.25% in February 2022, but this looks ambitious as the MPC has stated that it wants to see what happens to the economy, and particularly to employment once furlough ends at the end of September. At the MPC's meeting in February it will only have available the employment figures for November: to get a clearer picture of employment trends, it would need to wait until the May meeting when it would have data up until February. At its May meeting, it will also have a clearer understanding of the likely peak of inflation.*

*The MPC's forward guidance on its intended monetary policy on raising Bank Rate versus selling (quantitative easing) holdings of bonds is as follows: -*

1. *Placing the focus on raising Bank Rate as "the active instrument in most circumstances".*
2. *Raising Bank Rate to 0.50% before starting on reducing its holdings.*
3. *Once Bank Rate is at 0.50% it would stop reinvesting maturing gilts.*
4. *Once Bank Rate had risen to at least 1%, it would start selling its holdings.*

***COVID-19 vaccines.*** *These have been the game changer which have enormously boosted confidence that life in the UK could largely return to normal during the summer after a third wave of the virus threatened to overwhelm hospitals in the spring. With the household saving rate having been exceptionally high since the first lockdown in March 2020, there is plenty of pent-up demand and purchasing power stored up for services in hard hit sectors like restaurants, travel and hotels. The big question is whether mutations of the virus could develop which render current vaccines ineffective, as opposed to how quickly vaccines can be modified to deal with them and enhanced testing programmes be implemented to contain their spread.*

***US.*** *See comments below on US treasury yields.*

***EU.*** *The slow role out of vaccines initially delayed economic recovery in early 2021 but the vaccination rate has picked up sharply since then. After a contraction in GDP of -0.3% in Q1, Q2 came in with strong growth of 2%, which is likely to continue into Q3, though some countries more dependent on tourism may struggle. Recent sharp increases in gas and electricity prices have increased overall inflationary pressures but the ECB is likely to see these as being only transitory after an initial burst through to around 4%, so is unlikely to be raising rates for a considerable time.*

*German general election. With the CDU/CSU and SDP both having won around 24-26% of the vote in the September general election, the composition of Germany's next coalition government may not be agreed by the end of 2021. An SDP-led coalition would probably pursue a slightly less restrictive fiscal policy, but any change of direction from a CDU/CSU led coalition government is likely to be small. However, with Angela Merkel standing down as Chancellor as soon as a coalition is formed, there will be a hole in overall EU leadership which will be difficult to fill.*

***China.*** *After a concerted effort to get on top of the virus outbreak in Q1 2020, economic recovery was strong in the rest of the year; this enabled China to recover all the initial contraction. During 2020, policy makers both quashed the virus and implemented a programme of monetary and fiscal support that was particularly effective at stimulating short-term growth. At the same time, China's economy benefited from the shift towards online spending by consumers in developed markets. These factors helped to explain its comparative outperformance compared to western economies during 2020 and earlier in 2021. However, the pace of economic growth has now fallen back after this initial surge of recovery from the pandemic and China is now struggling to contain the spread of the Delta variant through sharp local lockdowns - which will also depress economic growth. There are also questions as to how effective Chinese vaccines are proving. In addition, recent regulatory actions motivated by a political agenda to channel activities into officially approved directions, are also likely to reduce the dynamism and long-term growth of the Chinese economy.*

***Japan.*** *2021 has been a patchy year in combating Covid. However, after a slow start, nearly 50% of the population are now vaccinated and Covid case numbers are falling. After a weak Q3 there is likely to be a strong recovery in Q4. The Bank of Japan is continuing its very loose monetary policy but with little prospect of getting* *inflation back above 1% towards its target of 2%, any time soon: indeed, inflation was negative in July. New Prime Minister Kishida has promised a large fiscal stimulus package after the November general election – which his party is likely to win.*

***World growth.*** *World growth was in recession in 2020 but recovered during 2021 until starting to lose momentum more recently. Inflation has been rising due to increases in gas and electricity prices, shipping costs and supply shortages, although these should subside during 2022. It is likely that we are heading into a period where there will be a reversal of world globalisation and a decoupling of western countries from dependence on China to supply products, and vice versa. This is likely to reduce world growth rates from those in prior decades.*

***Supply shortages.*** *The pandemic and extreme weather events have been highly disruptive of extended worldwide supply chains. At the current time there are major queues of ships unable to unload their goods at ports in New York, California and China. Such issues have led to mis-distribution of shipping containers around the world and have contributed to a huge increase in the cost of shipping. Combined with a shortage of semi-conductors, these issues have had a disruptive impact on production in many countries. Many western countries are also hitting up against a difficulty in filling job vacancies. It is expected that these issues will be gradually sorted out, but they are currently contributing to a spike upwards in inflation and shortages of materials and goods on shelves.*

3.2 Link Group's view on the outlook for the remainder of 2021/22 is as follows:-

*The coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings.*

*As shown in the forecast table below, one increase in Bank Rate from 0.10% to 0.25% has now been included in quarter 2 of 2022/23, a second increase to 0.50% in quarter 2 of 23/24 and a third one to 0.75% in quarter 4 of 23/24.*

***Significant risks to the forecasts***

- *COVID vaccines do not work to combat new mutations and/or new vaccines take longer than anticipated to be developed for successful implementation.*
- *The pandemic causes major long-term scarring of the economy.*
- *The Government implements an austerity programme that supresses GDP growth.*
- *The MPC tightens monetary policy too early – by raising Bank Rate or unwinding QE.*
- *The MPC tightens monetary policy too late to ward off building inflationary pressures.*
- *Major stock markets e.g. in the US, become increasingly judged as being over-valued and susceptible to major price corrections. Central banks become increasingly exposed to the "moral hazard" risks of having to buy shares and corporate bonds to reduce the impact of major financial market sell-offs on the general economy.*
- *Geo-political risks are widespread e.g. German general election in September 2021 produces an unstable coalition or minority government and a void in high-profile leadership in the EU when Angela Merkel steps down as Chancellor of Germany; on-going global power influence struggles between Russia/China/US.*

***The balance of risks to the UK economy: -***

*The overall balance of risks to economic growth in the UK is now to the downside,* *including residual risks from Covid and its variants - both domestically and their potential effects worldwide.*

***Forecasts for Bank Rate***

*Bank Rate is not expected to go up fast after the initial rate rise as the supply potential of the economy has not generally taken a major hit during the pandemic, so should be able to cope well with meeting demand without causing inflation to remain elevated in the medium-term, or to inhibit inflation from falling back towards the MPC's 2% target after the surge to around 4% towards the end of 2021. Three increases in Bank rate are forecast in the period to March 2024, ending at 0.75%. However, these forecasts may well need changing within a relatively short time frame for the following reasons: -*

- *There are increasing grounds for viewing the economic recovery as running out of steam during the summer and now into the autumn. This could lead into stagflation which would create a dilemma for the MPC as to which way to face.*
- *Will some current key supply shortages e.g., petrol and diesel, spill over into causing economic activity in some sectors to take a significant hit?*
- *Rising gas and electricity prices in October and next April and increases in other prices caused by supply shortages and increases in taxation next April, are already going to deflate consumer spending power without the MPC having to take any action on Bank Rate to cool inflation. Then we have the Government's upcoming budget in October, which could also end up in reducing consumer spending power.*
- *On the other hand, consumers are sitting on around £200bn of excess savings left over from the pandemic so when will they spend this sum, in part or in total?*
- *There are 1.6 million people coming off furlough at the end of September; how many of those will not have jobs on 1st October and will, therefore, be available to fill labour shortages in many sectors of the economy? So, supply shortages which have been driving up both wages and costs, could reduce significantly within the next six months or so and alleviate the MPC's current concerns.*
- *There is a risk that there could be further nasty surprises on the Covid front, on top of the flu season this winter, which could depress economic activity.*

*In summary, with the high level of uncertainty prevailing on several different fronts, it is likely that these forecasts will need to be revised again soon - in line with what the new news is.*

*It also needs to be borne in mind that Bank Rate being cut to 0.10% was an emergency measure to deal with the Covid crisis hitting the UK in March 2020. At any time, the MPC could decide to simply take away that final emergency cut from 0.25% to 0.10% on the grounds of it no longer being warranted and as a step forward in the return to normalisation. In addition, any Bank Rate under 1% is both highly unusual and highly supportive of economic growth.*

***Forecasts for PWLB rates and gilt and treasury yields***

*As the interest forecast table for PWLB certainty rates above shows, there is likely to be a steady rise over the forecast period, with some degree of uplift due to rising treasury yields in the US.*

*There is likely to be exceptional volatility and unpredictability in respect of gilt yields and PWLB rates due to the following factors: -*

- *How strongly will changes in gilt yields be correlated to changes in US treasury yields?*

- *Will the Fed take action to counter increasing treasury yields if they rise beyond a yet unspecified level?*
- *Would the MPC act to counter increasing gilt yields if they rise beyond a yet unspecified level?*
- *How strong will inflationary pressures turn out to be in both the US and the UK and so impact treasury and gilt yields?*
- *How will central banks implement their new average or sustainable level inflation monetary policies?*
- *How well will central banks manage the withdrawal of QE purchases of their national bonds i.e., without causing a panic reaction in financial markets as happened in the "taper tantrums" in the US in 2013?*
- *Will exceptional volatility be focused on the short or long-end of the yield curve, or both?*

*The forecasts are also predicated on an assumption that there is no break-up of the Eurozone or EU within our forecasting period, despite the major challenges that are looming up, and that there are no major ructions in international relations, especially between the US and China / North Korea and Iran, which have a major impact on international trade and world GDP growth.*

***Gilt and treasury yields***

*Since the start of 2021, there has been a lot of volatility in gilt yields, and hence PWLB rates. During the first part of the year, US President Biden's, and the Democratic party's determination to push through a $1.9trn (equivalent to 8.8% of GDP) fiscal boost for the US economy as a recovery package from the Covid pandemic was what unsettled financial markets. However, this was in addition to the $900bn support package already passed in December 2020 under President Trump. This was then followed by additional Democratic ambition to spend further huge sums on infrastructure and an American families plan over the next decade which are caught up in Democrat / Republican haggling. Financial markets were alarmed that all this stimulus, which is much bigger than in other western economies, was happening at a time in the US when: -*

- *A fast vaccination programme has enabled a rapid opening up of the economy.*
- *The economy had already been growing strongly during 2021.*
- *It started from a position of little spare capacity due to less severe lockdown measures than in many other countries. A combination of shortage of labour and supply bottle necks is likely to stoke inflationary pressures more in the US than in other countries.*
- *And the Fed was still providing monetary stimulus through monthly QE purchases.*

*These factors could cause an excess of demand in the economy which could then unleash stronger and more sustained inflationary pressures in the US than in other western countries. This could then force the Fed to take much earlier action to start tapering monthly QE purchases and/or increasing the Fed rate from near zero, despite their stated policy being to target average inflation. It is notable that some Fed members have moved forward their expectation of when the first increases in the Fed rate will occur in recent Fed meetings. In addition, more recently, shortages of workers appear to be stoking underlying wage inflationary pressures which are likely to feed through into CPI inflation. A run of strong monthly jobs growth figures could be enough to meet the threshold set by the Fed of "substantial further progress towards the goal of reaching full employment". However, the weak growth in August, (announced 3.9.21), has spiked anticipation that tapering of monthly QE purchases could start by the end of 2021. These purchases are currently acting as downward pressure on treasury yields. As the US financial markets are, by far, the* *biggest financial markets in the world, any trend upwards in the US will invariably impact and influence financial markets in other countries. However, during June and July, longer term yields fell sharply; even the large non-farm payroll increase in the first week of August seemed to cause the markets little concern, which is somewhat puzzling, particularly in the context of the concerns of many commentators that inflation may not be as transitory as the Fed is expecting it to be. Indeed, inflation pressures and erosion of surplus economic capacity look much stronger in the US than in the UK. As an average since 2011, there has been a 75% correlation between movements in 10 year treasury yields and 10 year gilt yields. This is a significant UPWARD RISK exposure to our forecasts for longer term PWLB rates. However, gilt yields and treasury yields do not always move in unison.*

*There are also possible DOWNSIDE RISKS from the huge sums of cash that the UK populace have saved during the pandemic; when savings accounts earn little interest, it is likely that some of this cash mountain could end up being invested in bonds and so push up demand for bonds and support their prices i.e., this would help to keep their yields down. How this will interplay with the Bank of England eventually getting round to not reinvesting maturing gilts and then later selling gilts, will be interesting to keep an eye on.*

***The balance of risks to medium to long term PWLB rates:** -*
*There is a balance of upside risks to forecasts for medium to long term PWLB rates.*

***A new era – a fundamental shift in central bank monetary policy***
*One of the key results of the pandemic has been a fundamental rethinking and shift in monetary policy by major central banks like the Fed, the Bank of England and the ECB, to tolerate a higher level of inflation than in the previous two decades when inflation was the prime target to bear down on so as to stop it going above a target rate. There is now also a greater emphasis on other targets for monetary policy than just inflation, especially on 'achieving broad and inclusive "maximum" employment in its entirety' in the US before consideration would be given to increasing rates.*

- *The Fed in America has gone furthest in adopting a monetary policy based on a clear goal of allowing the inflation target to be symmetrical, (rather than a ceiling to keep under), so that inflation averages out the dips down and surges above the target rate, over an unspecified period of time.*
- *The Bank of England has also amended its target for monetary policy so that inflation should be 'sustainably over 2%' and the ECB now has a similar policy.*
- *For local authorities, this means that investment interest rates and very short term PWLB rates will not be rising as quickly or as high as in previous decades when the economy recovers from a downturn and the recovery eventually runs out of spare capacity to fuel continuing expansion.*
- *Labour market liberalisation since the 1970s has helped to break the wage-price spirals that fuelled high levels of inflation and has now set inflation on a lower path which makes this shift in monetary policy practicable. In addition, recent changes in flexible employment practices, the rise of the gig economy and technological changes, will all help to lower inflationary pressures.*
- *Governments will also be concerned to see interest rates stay lower as every rise in central rates will add to the cost of vastly expanded levels of national debt; (in the UK this is £21bn for each 1% rise in rates). On the other hand, higher levels of inflation will help to erode the real value of total public debt.*

3.3 Link Group's view on the anticipated future movement in interest rates is shown below.

| Link Group Interest Rate View | 29.9.21 | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Dec-21 | Mar-22 | Jun-22 | Sep-22 | Dec-22 | Mar-23 | Jun-23 | Sep-23 | Dec-23 | Mar-24 |
| BANK RATE | 0.10 | 0.10 | 0.25 | 0.25 | 0.25 | 0.25 | 0.50 | 0.50 | 0.50 | 0.75 |
| 3 month ave earnings | 0.10 | 0.10 | 0.20 | 0.20 | 0.30 | 0.40 | 0.50 | 0.50 | 0.60 | 0.70 |
| 6 month ave earnings | 0.20 | 0.20 | 0.30 | 0.30 | 0.40 | 0.50 | 0.60 | 0.60 | 0.70 | 0.80 |
| 12 month ave earnings | 0.30 | 0.40 | 0.50 | 0.50 | 0.50 | 0.60 | 0.70 | 0.80 | 0.90 | 1.00 |
| 5 yr PWLB | 1.40 | 1.40 | 1.50 | 1.50 | 1.60 | 1.60 | 1.60 | 1.70 | 1.70 | 1.70 |
| 10 yr PWLB | 1.80 | 1.80 | 1.90 | 1.90 | 2.00 | 2.00 | 2.00 | 2.10 | 2.10 | 2.10 |
| 25 yr PWLB | 2.20 | 2.20 | 2.30 | 2.30 | 2.40 | 2.40 | 2.40 | 2.50 | 2.50 | 2.60 |
| 50 yr PWLB | 2.00 | 2.00 | 2.10 | 2.20 | 2.20 | 2.20 | 2.20 | 2.30 | 2.30 | 2.40 |

## 4. TREASURY MANAGEMENT STRATEGY AND ANNUAL INVESTMENT STRATEGY UPDATE

4.1 The Treasury Management Strategy Statement (TMSS) for 2021/22 was approved by the Council on 23 February 2021 as part of the Budget Report.

4.2 There are no required policy changes to the TMSS; the details in this report update the position in the light of the current economic position and budgetary changes already approved.

4.3 In recent years the Council has moved to a more diverse portfolio involving more foreign banks and more longer-duration investments in order to achieve an enhanced return in the current low interest rate environment; however, more liquid investments have been sought during the current pandemic in order to maintain the Council's cash position. All counterparties used have been selected on the basis that they are highly rated and meet the criteria set out in the Council's Treasury Management Strategy.

## 5. THE COUNCIL'S CAPITAL POSITION (PRUDENTIAL INDICATORS)

5.1 The Prudential Indicators are reported on a quarterly basis as part of the Capital Monitoring process. The Prudential Indicators show the current position against the Prudential Indicator limits initially set as part of the 2021/22 Budget Report.

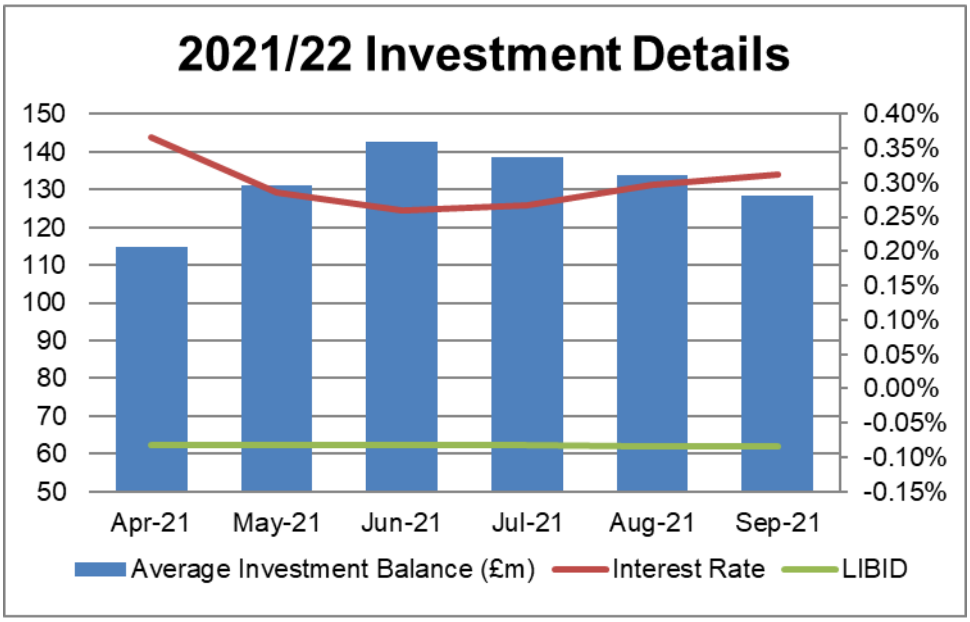
5.2 The indicators are updated from the Capital Programme as at 30 September 2021, showing the Council's capital expenditure plans and how these plans are being financed. Any changes in the capital expenditure plans will impact of the on the prudential indicators and the underlying need to borrow.

5.3 The current prudential indicator position is shown as **Appendix 1** of this report. All the indicators are within the set limits showing that the Council's borrowing strategy remains a prudent one.

## 6. INVESTMENT PORTFOLIO 2021/22

6.1 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. As set out in Section 3, it was a difficult interest environment even before the Covid-19 crisis, and this along with the added uncertainty in the pandemic prompts a low risk strategy. Given this risk environment, investment returns are likely to remain low.

6.2 The Council held £127.205m of investments as at 30 September 2021, with an investment portfolio yield to date of 0.30% against LIBID of -0.08%. At 31 March 2021 the portfolio consisted of £94.260m of investments. The movement is largely in relation to grants received early in the year. The below graph illustrates the change in investment balances over time along with the change in interest earned and the LIBID benchmark:




6.3 The portfolio as at 30 September 2021 was as follows:

| Investment Type | Total Invested | Weighted Average Duration | Average Interest Rate |
|---|---|---|---|
| | **(£m)** | **(days)** | **(%)** |
| Money Market Funds | 20.505 | n/a (overnight) | 0.03 |
| Banks (fixed term) | 30.000 | 160 | 0.21 |
| Banks (notice) | Nil | n/a | n/a |
| Local Authorities | 76.700 | 426 | 0.46 |
| **Total** | **127.205** | | |

6.4 As outlined in paragraph 4.3, above, this return has largely been earned due to an increased number of longer-duration investments, including a number of investments placed with other Local Authorities in previous years which are paying what are now very favourable rates. However, these investments are gradually maturing and inevitably being replaced with investments earning lower returns.

6.5 The Assistant Director of Finance confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2021/22.

6.6 The Council's projections as at September 2021 show that external loans will incur interest charges of £5.838m. Investment income to be earned during the year is estimated to be £3.583m, which will reduce these costs to give an estimated net interest charge of £2.255m.

6.7 As outlined in the Treasury Management Strategy, the Council uses the Link Group creditworthiness service to inform counterparty selection.

6.8 The Link Group creditworthiness service uses a wider array of information than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

6.9 Typically the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

6.10 All credit ratings will be monitored regularly. The Council is alerted to changes to ratings of all three agencies through its use of the Link Group creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Group. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

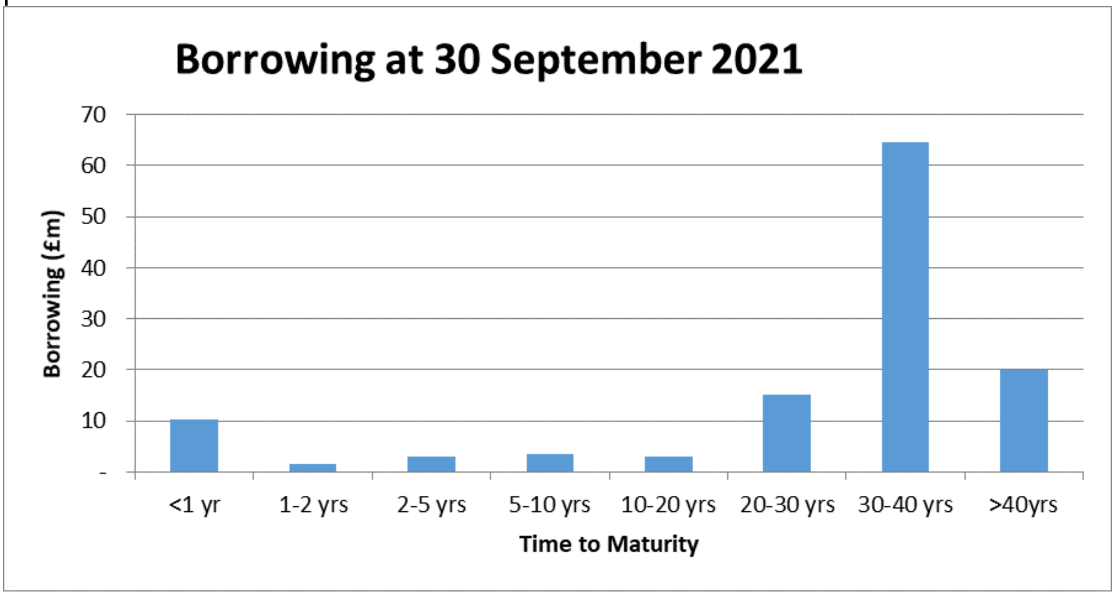
6.11 Sole reliance will not be placed on the use of this external service. In addition the Council will also use market data and market information, and information on any external support for banks to help support its decision making process.

## 7. BORROWING

7.1 The Council has not taken up any new borrowing in the first half of 2021/22.

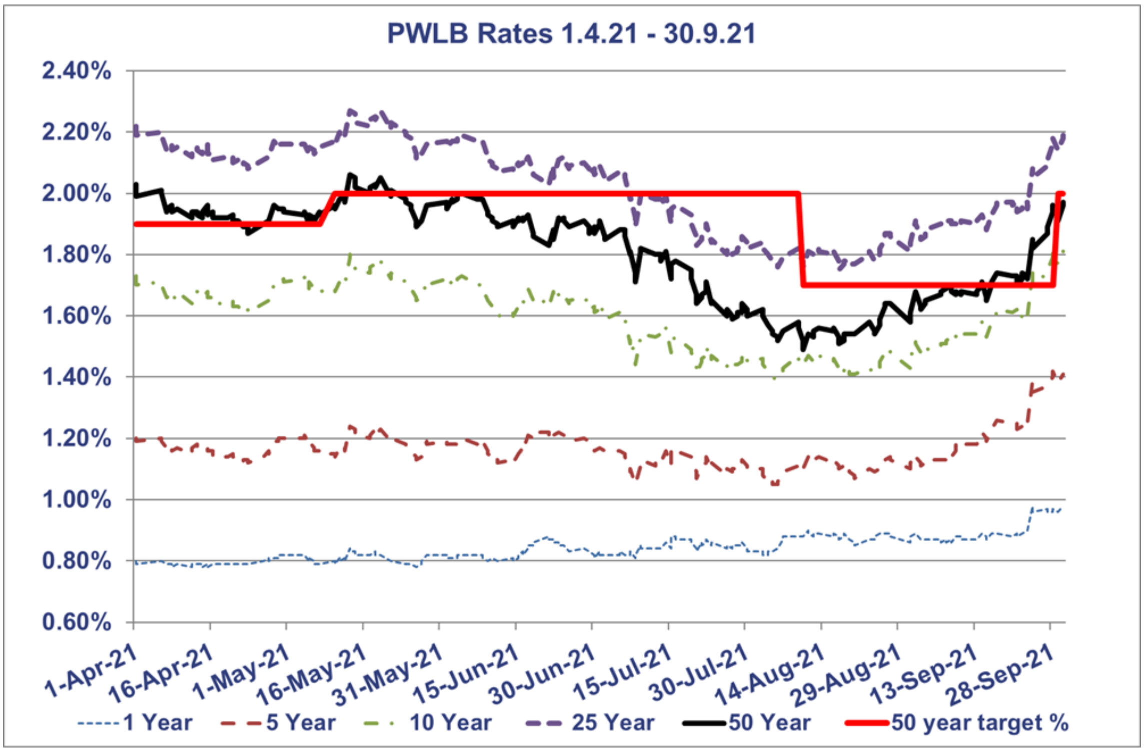
7.2 The Council has previously relied on the PWLB as a major source of funding, but will consider potential alternative sources of borrowing when the need arises.

7.3 As at 30 September 2021 the Council's total borrowing was £150.978m. The maturity profile is as follows:




7.4 The Council's capital financing requirement (CFR) at 31 March 2021 was £191.128m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the Public Works Loan Board or the market (external borrowing) or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions.

7.5 The Council had an outstanding borrowing requirement of £53.866m at 31 March 2021. This is forecast to increase to £62.154m by the end of 2021/22 due to planned capital investment. The remaining outstanding borrowing requirement is currently funded from internal balances on a temporary basis and has the impact of reducing the level of the Council's investment balances. This continues to be a prudent and cost effective approach in the current economic climate but is kept under regular review.




7.6 The table above shows the movement in Public Works Loan Board borrowing rates in 2021/22.

## 8. MINIMUM REVENUE PROVISION

8.1 The amount of long-term debt that the Council may have is governed by the Prudential Limits set by the Council at the start of the financial year. This is based on the amount of borrowing which the Council has deemed to be prudent. It also allows for advance borrowing for future years' capital expenditure.

8.2 The Council must also allow for repayment of the debt, by way of the Minimum Revenue Provision (MRP). This is the minimum amount that the Council must set aside annually. The Local Authority (Capital Finance and Accounting) Regulations 2008 revised the previous detailed regulations and introduced a duty that an authority calculates an amount of MRP which it considered prudent, although the 2008 Regulations do not define "prudent provision", they provide guidance to authorities on how they should interpret this.

8.3 In 2015/16 the Council's MRP policy was revised from the previous practice (4% of the capital finance requirement on a reducing balance basis) to a straight line method of 2% of the 2015/16 capital financing requirement over a period of 50 years.

8.4 Any new prudential borrowing taken up will be provided for within the MRP calculation based upon the expected useful life of the asset or by an alternative approach deemed appropriate to the expenditure in question. This will continue to be reviewed on an ongoing basis.

8.5 For any finance leases and any on-balance sheet public finance initiative (PFI) schemes, the MRP charge will be equal to the principal repayment during the year, calculated in accordance with proper practices.

8.6 There will be no MRP charge for any cash backed Local Authority Mortgage Scheme (LAMS) that the Council operates. As for this type of scheme, any future debt liability would be met from the capital receipt arising from the deposit maturing after a 5 year period. Any repossession losses for this type of scheme would be charged to a LAMS reserve.

8.7 The MRP policy was updated as part of the 2018/19 Treasury Management Strategy to clarify the Council's position on loans to third parties. The Council considers an MRP charge is not necessary in respect of any loans made to third parties as the debt liability is covered by the existence of a debtor; typically long term depending on the life of the loan. The only expenditure consequence of a loan for an authority is the interest on its cash shortfall whilst the loan is outstanding, so provision for the principal amount would be over-prudent until such time as the assumption has to be made that the loan will not be repaid.

## 9. DEBT RESCHEDULING

9.1 Debt rescheduling opportunities have been limited in the current economic climate and consequent structure of interest rates. No debt rescheduling was undertaken during the first six months of 2021/22.

## 10. GREATER MANCHESTER METROPOLITAN DEBT ADMINISTRATION FUND (GMMDAF)

10.1 Tameside Council is the lead council responsible for the administration of the debt of the former Greater Manchester County Council, on behalf of all ten Greater Manchester Metropolitan Authorities. All expenditure of the fund is shared by the authorities on a population basis.

10.2 Unlike Tameside the GMMDAF incurs no capital expenditure, and therefore the total debt outstanding reduces annually by the amount of debt repaid by the constituent authorities. However, loans are raised to replace those maturing during the year, and for cashflow purposes.

10.3 At 31 March 2021 the fund had the following outstanding balances:

| | **£m** |
|---|---|
| Public Works Loan Board | 25.863 |
| Pre 1974 Transferred Debt | 0.065 |
| Temporary Loans / (Investments) | 6.406 |
| Other Balances | 0.897 |
| Total Debt | 20.780 |

10.4 The fund's borrowing requirement for 2021/22 is estimated to be:-

| | **£m** |
|---|---|
| **Long term debt maturing** | |
| Public Works loan Board | 18.754 |
| Other | 0.037 |
| | 18.791 |
| Less principal repayments | (20.780) |
| Deficit/ (Surplus) in year | (1.989) |

10.5 As GMMDAF winds down in this year the surplus, along with that brought forward from 2020/21, will be used towards the repayment of loans with a maturity date beyond that of the Fund.

10.6 During 2021/22 it is estimated that the total interest payments will be £1.391m at an average interest rate of 6.69%. This compares with 6.47% in 2020/21.

## 11. RECOMMENDATIONS

11.1 As set out on the front of the report.

## Appendix 1 – Prudential Indicators

**Actuals v limits as at 30 September 2021**

| | Limit | Actual | Amount within limit |
|---|---|---|---|
| | **£000s** | **£000s** | **£000s** |
| Operational Boundary for External Debt | 220,710 | 150,978 | (69,732) |
| Authorised Limit for External Debt | 240,710 | 150,978 | (89,732) |

These limits include provision for borrowing in advance of the Council's requirement for future capital expenditure. This may be carried out if it is thought to be financially advantageous to the Council.

| | Limit | Actual | Amount within limit |
|---|---|---|---|
| | **£000s** | **£000s** | **£000s** |
| Upper Limit for fixed | 199,373 | 13,961 | (185,412) |
| Upper Limit for variable | 66,458 | 9,648 | (56,810) |

These limits are in respect of the Council's exposure to the effects of changes in interest rates.

The limits reflect the net amounts of fixed/variable rate debt (i.e. fixed/variable loans less fixed/variable investments).

| | Limit | Actual | Amount within limit |
|---|---|---|---|
| | **£000s** | **£000s** | **£000s** |
| Capital Financing Requirement | 199,373 | 199,373 | - |

The Capital Financing Requirement (CFR) is aimed to represent the underlying need to borrow for a capital purpose and is calculated from the aggregate of specified items on the balance sheet. The CFR increases by the value of capital expenditure not immediately financed (i.e. borrowing) and is reduced by the annual MRP repayment.

| | Limit | Actual | Amount within limit |
|---|---|---|---|
| | **£000s** | **£000s** | **£000s** |
| Capital expenditure | 88,117 | 10,145 | (77,972) |

This is the estimate of the total capital expenditure to be incurred.

| Gross borrowing and the capital financing requirement | CFR @ 31/03/21 + increase years 1,2,3 | Gross borrowing | Amount within limit |
|---|---|---|---|
| | **£000s** | **£000s** | **£000s** |
| | 199,373 | 150,978 | (48,395) |

To ensure that medium term debt will only be for capital purposes, the Council will ensure that the gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement (CFR).

| Maturity structure for borrowing 2021/22<br>Fixed rate | | |
|---|---|---|
| **Duration** | **Limit** | **Actual** |
| Under 12 months | 0% to 15% | 6.75% |
| 12 months and within 24 months | 0% to 15% | 1.07% |
| 24 months and within 5 years | 0% to 30% | 1.99% |
| 5 years and within 10 years | 0% to 40% | 2.35% |
| 10 years and above | 50% to 100% | 87.83% |

These limits set out the amount of fixed rate borrowing maturing in each period expressed as a percentage of total fixed rate borrowing. Future borrowing will normally be for periods in excess of 10 years, although if longer term interest rates become excessive, shorter term borrowing may be used. Given the low current long term interest rates, it's felt it is acceptable to have a long maturity debt profile.