Report of the
Director Governance and Partnerships

Agenda Item 4
Meeting: 11 October 2021

NORTH LINCOLNSHIRE COUNCIL

COUNCIL

TREASURY MANAGEMENT MID YEAR AND ANNUAL REPORT 2020/21

1. OBJECT AND KEY POINTS IN THIS REPORT

1.1. To inform Council of the Treasury arrangements, activity and performance during 2020-21. The key points being:-

1.1.1. The level of borrowing was within Prudential Indicator Limits and the Council was able to maintain its policy of avoiding new borrowing.

1.1.2. Investment returns dropped to near zero due to the impact of the Covid 19 pandemic. The Council has taken a cautious approach to investing.

2. BACKGROUND INFORMATION

2.1 CIPFA has defined treasury management as:

"The management of the organisation's borrowing, 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"

2.2 The Treasury Management Strategy Statement (TMSS) for 2020/21 was approved by Council in February 2020. This statement also incorporates the Investment Strategy.

2.3 Whilst the Council has advisors to support effective treasury management arrangements, the Council is ultimately responsible for its treasury decisions and activity. No treasury activity is without risk. The successful identification, monitoring and control of risk is therefore an important and integral element of treasury management arrangements.

2.4 The Council has nominated the Audit Committee to be responsible for ensuring effective scrutiny of treasury management arrangements.

3. OPTIONS FOR CONSIDERATION

3.1 The Mid-Year and Annual Treasury Management Review is at Appendix 1. The key issues include: -

3.2 Investments – The Treasury Management Strategy (TMS) for 2020/21 assumed that interest rates would continue at the start of the year at 0.75% rising to 1.25% by 2022/23. As a result of the Covid 19 pandemic, bank rates were cut back to 0.25% and then 0.10% to counteract the impact of the national lockdown on the economy.

3.3 Borrowing Requirement – The TMS expected that new borrowing would be required to finance new capital expenditure, replace maturing debt and the rundown of reserves. However, the Council has continued to maintain a position where its need to borrow to finance its capital programme (Capital Financing Requirement (CFR)) was not fully funded by loan debt; cash supporting the Councils reserves, balances and cash flow was used as an interim measure.

3.4 Repayment of Debt – During 2020/21 the Council repaid £51.6m at scheduled payment dates.

3.5 The cost of servicing the council's debt was £10.9m or 9.39% of the council's net revenue stream. This remained below the 10%-12% range which is seen as the maximum affordable level.

3.6 Investment Outturn – The Council maintained an average balance of £49.9m of internally managed funds with an average rate of return of 0.03%.

3.7 Borrowing Outturn – A loan of £9m was drawn for cash flow purposes to fund advanced pension contributions resulting in a net saving of £0.283m

3.8 No loans were drawn in advance of need and no debt rescheduling was carried out.

3.9 Investment income was £13k compared to a budget of £75k.

4. ANALYSIS OF OPTIONS

4.1 The investment activity during the year conformed to the approved strategy and the Council had no liquidity issues.

4.2 The borrowing requirement strategy was prudent as investment returns were very low and this minimised counterparty risk on placing investments.

4.3 The level of debt was within the operational boundary and authorised limits set in the Treasury Management Strategy.

4.4 This report is a requirement of the Prudential Code and provides the Council with assurance on the Treasury Management operation in 2020/21.

5. FINANCIAL AND OTHER RESOURCE IMPLICATIONS (e.g. LEGAL, HR, PROPERTY, IT, COMMUNICATIONS etc.)

5.1 The financial implications to this report are covered in section 3.

6. OTHER RELEVANT IMPLICATIONS (e.g. CRIME AND DISORDER, EQUALITIES, COUNCIL PLAN, ENVIRONMENTAL, RISK etc.)

6.1 Not applicable.

7. OUTCOMES OF INTEGRATED IMPACT ASSESSMENT (IF APPLICABLE)

7.1 No impact assessment is required for the purpose of this report.

8. OUTCOMES OF CONSULTATION AND CONFLICTS OF INTERESTS DECLARED

8.1 The mid-year and annual report Treasury Report was considered by the Audit Committee on 21st July 2021. There are no reported conflicts in respect of Treasury activity.

9. RECOMMENDATIONS

9.1 That Council notes the Treasury Management performance for the 2020/21 financial year.

DIRECTOR: GOVERNANCE AND PARTNERSHIPS

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Background Papers used in the preparation of this report
CIPFA Treasury Management Code and Guidance Notes
Treasury Management Strategy 2020-21

Appendix 1

SAFE WELL PROSPEROUS CONNECTED

Mid-Year & Annual Treasury Management Review 2020/21

North Lincolnshire Council

www.northlincs.gov.uk

1. Introduction

The Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2020/21. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

During 2020/21 the minimum reporting requirements were as follows.

- an annual treasury strategy in advance of the year (Council)
- a mid-year (minimum) treasury update report (Audit Committee)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

2. The Council's Capital Expenditure and Financing

The Council undertakes capital expenditure on long-term assets. These activities are financed by a combination of :

- capital resources being capital receipts, capital grants and revenue contributions,
- cash resources (internal borrowing)
- borrowing (external borrowing)

The actual capital expenditure is one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

£m	31.3.20 Actual	30.9.20 Actual	31.3.21 Actual
Capital expenditure	**32.15**	**9.97**	**28.14**
Financed from Capital Resources	17.55	N/A	19.19
Financed from Cash Resources	14.60	N/A	8.95

3. The Council's Overall Borrowing Need

Gross borrowing and the Capital Financing Requirement (CFR) - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2020/21) plus the estimates of any additional capital financing requirement for the current (2021/22) and next two financial years. This essentially means that the Council is not borrowing to support revenue

expenditure. This indicator allowed the Council some flexibility to borrow in advance of its immediate capital needs in 2020/21. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

£m	31.3.20 Actual	30.09.20 Actual	31.3.21 Actual
Capital Financing Requirement (CFR)	244.33	242.39	248.27
Gross borrowing position	203.84	172.52	161.25
Under / over funding of CFR	(40.49)	(69.87)	(87.02)

The authorised limit - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2020/21 the Council has maintained gross borrowing within its authorised limit.

The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limit not being breached.

Actual financing costs as a proportion of net revenue stream - this indicator identifies the trend in the cost of capital, (borrowing and other long term obligation costs net of investment income), against the net revenue stream.

	2020/21
Authorised limit	£309.55m
Maximum gross borrowing position during the year	£203.91m
Operational boundary	£271.55m
Average gross borrowing position	£178.625m
Financing costs as a proportion of net revenue stream	6.65%

4. Treasury Position & Prudential Indicators as of 30th September 2020 and 31st March 2021

4.1 Treasury Position

At the beginning, mid and at the end of 2020/21, the Council's treasury position was as follows:

Mid-Year

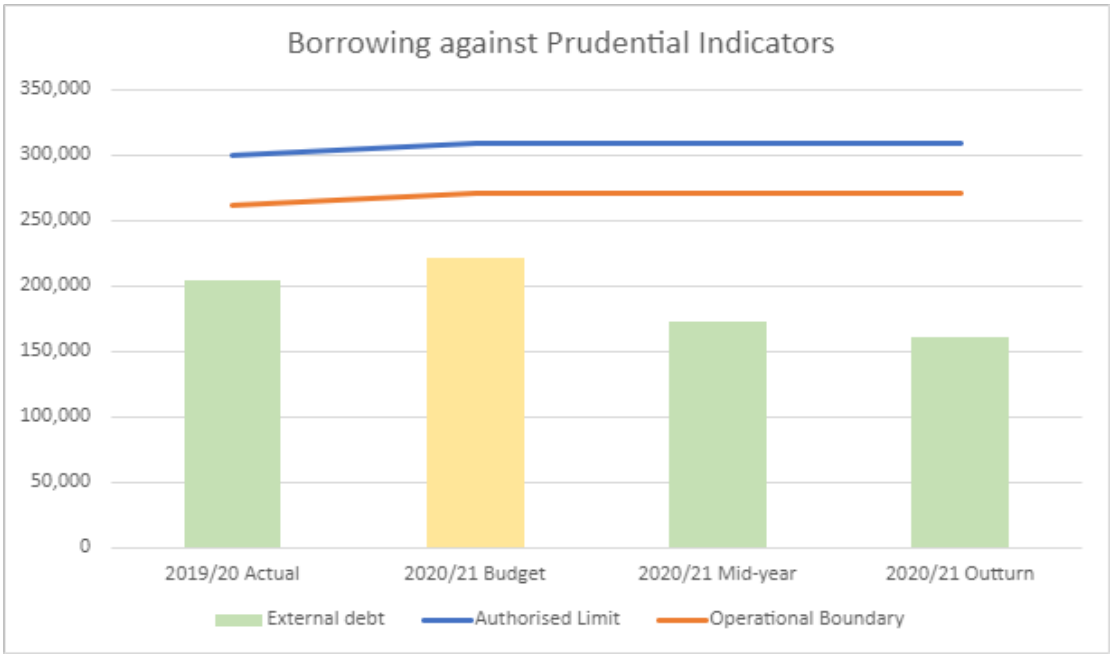
DEBT PORTFOLIO	31.3.20 Principal	Rate/ Return	Average Life yrs	30.9.20 Principal	Rate/ Return	Average Life yrs
Fixed rate funding:	£m			£m		
PWLB	156.84	3.79%	10.85	154.52	3.81%	11.00
Market	47.00	1.14%	0.32	18.00	1.43%	0.70
Total debt	203.84	3.18%	9.05	172.52	3.54%	10.12
CFR	244.33			242.39		
Over / (under) borrowing	-40.49			-69.87		
Total investments	35.27	0.13%	0.01	35.87	0.010%	0.05
Net debt	168.57			136.65		

Year End

DEBT PORTFOLIO	31.3.20 Principal	Rate/ Return	Average Life yrs	31.3.21 Principal	Rate/ Return	Average Life yrs
Fixed rate funding:	£m			£m		
PWLB	156.84	3.79%	10.85	152.25	3.84%	10.67
Market	47.00	1.14%	0.32	9.00	1.32%	0.05
Total debt	203.84	3.18%	9.05	161.25	3.70%	10.06
CFR	244.33			234.15		
Over / (under) borrowing	-40.49			-72.91		
Total investments	35.27	0.13%	0.01	24.00	0.002%	0.05
Net debt	168.57			137.25		

The maturity structure of the debt portfolio was as follows:

	31.3.20 Actual £m	31.3.20 Actual %	31.3.21 Actual £m	31.3.21 Actual %
Less than 1 year	51.60	25.31%	10.56	6.55%
1-2 years	5.63	2.76%	6.11	3.79%
2-5 years	17.34	8.51%	31.85	19.75%
5-10 years	50.24	24.65%	43.77	27.14%
10-20 years	52.08	25.55%	43.73	27.12%
20-30 years	15.27	7.49%	14.25	8.84%
30-40 years	11.68	5.73%	10.97	6.81%
40-50 years	0.00	0.00%	0.00	0.00%



4.2 Prudential Indicators

Year End

PRUDENTIAL INDICATORS	2019/20	2020/21
	Actual £m	Actual £m
Capital Expenditure	**32.15**	**28.14**
Ratio of financing costs to net revenue stream	**8.06%**	**9.39%**
Gross borrowing requirement General Fund		
brought forward 1 April	193.59	203.84
carried forward 31 March/ 30 September	203.84	161.25
in year borrowing requirement	10.25	-42.59
Gross debt	203.84	161.25
CFR	244.33	248.27
Annual change in Cap. Financing Requirement	-40.49	-87.02

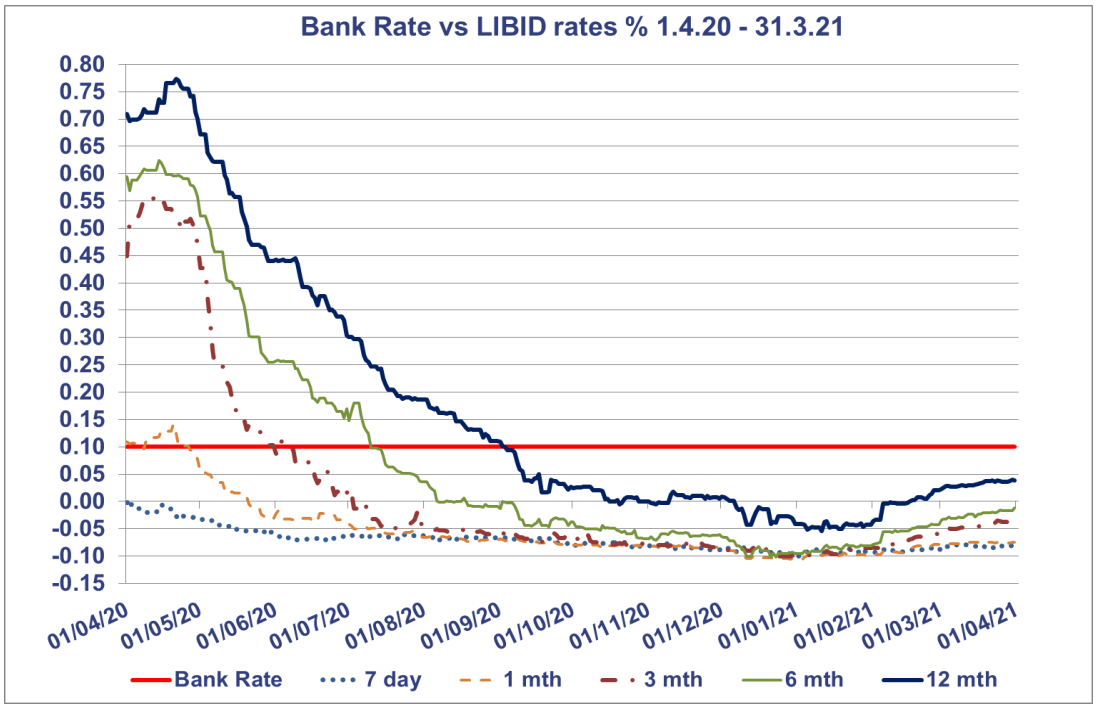
5. The Strategy for 2020/21

5.1 Investment strategy and control of interest rate risk

Investment returns which had been low during 2019/20, dropped during 2020/21 to near zero or even into negative territory. The expectation for interest rates within the treasury management strategy for 2020/21 was that Bank Rate would continue at the start of the year at 0.75 % before rising to end 2022/23 at 1.25%. This forecast was invalidated by the Covid-19 pandemic in March 2020 which caused the Monetary Policy Committee to cut Bank Rate in March, first to 0.25% and then to 0.10%, and introduce schemes and incentives to guard against an unwarranted tightening in financial conditions and support the economy. The Government also supplied Covid-19 grant support funding to local authorities to pass on to businesses. This meant that for most of the year there was much more liquidity in financial markets than there was demand to borrow, with the consequent effect that investment earnings rates dropped.

The table and graph below show interest rate movement during 2020-21 financial year.

	Bank Rate	7 day	1 mth	3 mth	6 mth	12 mth
High	0.10	0.00	0.14	0.56	0.62	0.77
High Date	01/04/2020	02/04/2020	20/04/2020	08/04/2020	14/04/2020	21/04/2020
Low	0.10	-0.10	-0.11	-0.10	-0.10	-0.05
Low Date	01/04/2020	31/12/2020	29/12/2020	23/12/2020	21/12/2020	11/01/2021
Average	0.10	-0.07	-0.05	0.01	0.07	0.17
Spread	0.00	0.10	0.25	0.66	0.73	0.83



While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the financial crisis. These requirements have provided a far stronger

basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

Investment balances have been kept to a minimum through the agreed strategy of using reserves and balances to support internal borrowing, rather than borrowing externally from the financial markets. External borrowing would have incurred an additional cost, due to the differential between borrowing and investment rates as illustrated in the charts shown above. Such an approach has also provided benefits in terms of reducing the counterparty risk exposure, by having fewer investments placed in the financial markets.

Council uses 7 days average LIBID rate as benchmark for yield on its investments. For the year 2020-21 LIBID 7 days average was -0.07%. In the environment of extreme low and negative returns on investments, council managed to earn £12,987 at the rate of 0.03% on its overall investments during the year.

5.2 Borrowing strategy and control of interest rate risk

During 2020-21, the Council maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow was used as an interim measure. This strategy was prudent as investment returns were very low and minimising counterparty risk on placing investments also needed to be considered.

A cost of carry remained during the year on any new long-term borrowing that was not immediately used to finance capital expenditure, as it would have caused a temporary increase in cash balances; this would have incurred a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns.

The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years. However, this is being kept under review to avoid incurring higher borrowing costs in the future when this authority may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

In 2020-21, council's primary policy was to avoid borrowing. However, following business case evaluation, the council borrowed £9.00 million for cash flow purposes to fund pension contributions for the next 3 years. At the time of borrowing, net savings from prepayment of these pension contributions were £ 283,000:

Total savings from 3 years prepayment:	£ 559,000
Interest costs for 3 years borrowing:	£ 276,000
Net savings:	£ 283,000

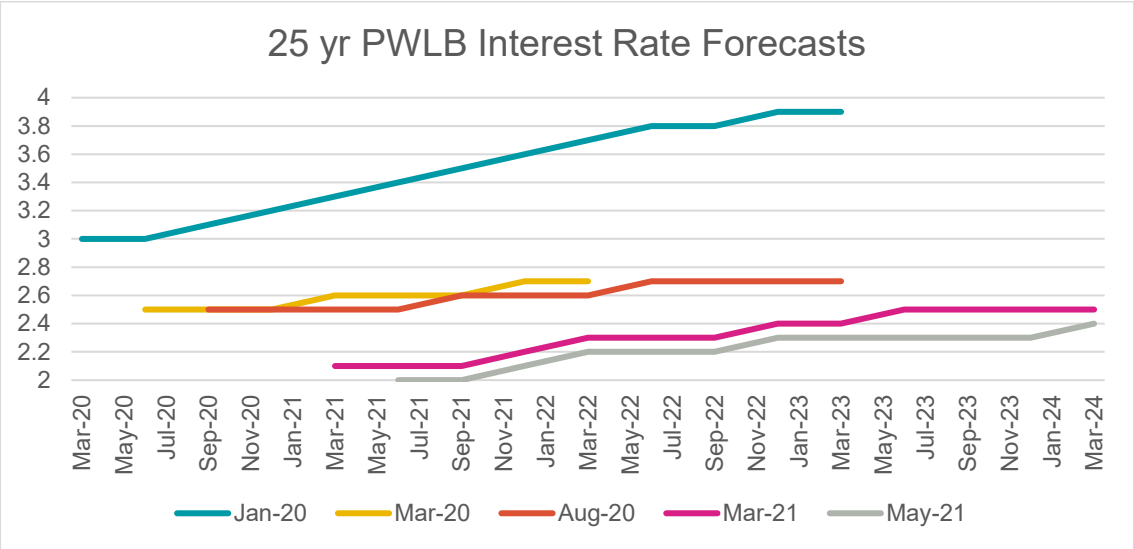
Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. Treasury team therefore monitored interest rates in financial markets and adopted a pragmatic strategy based upon the following principles to manage interest rate risks

- if it had been felt that there was a significant risk of a much sharper RISE in long and short term rates than initially expected, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would have been re-appraised. Most likely, fixed rate funding would have been drawn whilst interest rates were lower than they were projected to be in the next few years.

- If, it had been felt that there was a significant risk of a sharp FALL in long- and short-term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation),

then long term borrowings would have been postponed, and potential rescheduling from fixed rate funding into short term borrowing would have been considered.

Interest rate forecasts expected only gradual rises in medium- and longer-term fixed borrowing rates during 2020/21 and the two subsequent financial years. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period.



6. Borrowing Outturn

6.1 Borrowing

Loans were drawn for cash flow purposes to fund pension fund contributions.

The loans drawn were:

Lender	Principal	Type	Interest Rate	Maturity	Average for 2020/21
PWLB	£0.00m	Fixed interest rate	0.00%	-	£0.00m
Market	£9.00m	Fixed interest rate	1.317%	1.67 years	£9.00m

6.2 Borrowing in advance of need

No loans were drawn in advance of need.

6.3 Rescheduling

No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

6.4 Repayments

During 2020-21 Council repaid £51.595m at scheduled repayment dates.

7. Investment Outturn

7.1 Investment Policy

The Council's investment policy is governed by MHCLG investment guidance, which has been implemented in the annual investment strategy approved by the Council on 26.02.2020. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data, (such as rating outlooks, credit default swaps, bank share prices etc.).

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

7.2 Investments held by the Council

- The Council maintained an average balance of £49.948m of internally managed funds.
- The internally managed funds earned an average rate of return of 0.03%.
- The comparable performance indicator is the average 7day LIBID rate, which was -0.07%.
- Total investment income was £12,987 compared to a budget of £75,000.

INVESTMENT PORTFOLIO	31.3.20 Actual		30.09.20 Actual		31.3.21 Actual	
	£m	%	£m	%	£m	%
Treasury investments						
Banks	1.37	3.88	3.31	9.23%	5.83	24.30
MMF*	6.00	17.01	8.46	23.59%	7.67	31.95
DMADF (H M Treasury)**	27.90	79.11	24.10	67.18%	10.50	43.75
Total managed in house	35.27	100.00	35.87	100.00%	24.00	100.00
Total managed externally	0.00	0.00	0.00	0.00%	0.00	0.00
Treasury investments - Total	**35.27**	**100.00**	**35.87**	**100.00%**	**24.00**	**100.00**
Treasury investments	35.27	91.46	35.87	94.10%	24.00	91.43
Non-Treasury investments	3.29	8.54	2.25	5.90%	2.25	8.57
Total Investments	**38.56**	**100.00**	**38.12**	**100%**	**26.25**	**100.00**

*Money Market Fund
**Debt Management Account Deposit Facility

All treasury investments were up to one year.

8. Other Issues

8.1. Non-treasury management investments.

Council holds non treasury investment of £2.25 million as of 31.3.2021.

8.2. Sources of borrowing

Council has borrowed money from other local authorities mostly up to one year except one loan of £3.00 million with maturity of 3 years.

8.3. Changes in risk appetite

No fundamental change in risk appetite.

8.4. Counterparty limits

Council changed limits of two counterparties during the year. Barclays bank overnight limit was increased from £3.00 million to £5.00 million to meet operational requirements.

Limit of BlackRock MMF was increased from £3.00 million to £10.00 million temporarily until June 2021 to house a large COVID grant received from central government.

8.5. Sovereign limits

There was no change in policy on minimum sovereign ratings during the financial year.