POLICY & RESOURCES COMMITTEE	Agenda Item 65 Brighton & Hove City Council

Subject:		**Treasury Management Strategy Statement 2021/22 - Mid Year Review**		
Date of Meeting:		**2 December 2021**		
Report of:		**Acting Chief Finance Officer**		
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Ward(s) affected:		**All**		

FOR GENERAL RELEASE

1. PURPOSE OF REPORT AND POLICY CONTEXT

1.1 The 2021/22 Treasury Management Strategy Statement (TMSS) was approved by Policy & Resources Committee on 11 February 2021 and full Council on 25 February 2021.

1.2 The TMSS sets out the role of Treasury Management and includes the Annual Investment Strategy (AIS) which sets out the key parameters for investing council cash funds.

1.3 It is recommended good and proper practice that Members receive half yearly reports and review and endorse treasury management actions during the year. The purpose of this report is to advise of the action taken in the first half of 2021/22.

2. RECOMMENDATIONS:

That the Policy & Resources Committee:

2.1 Notes the key actions taken during the first half of 2021/22 to meet the TMSS and the investment strategy as set out in this report.

2.2 Notes the reported compliance with the AIS for the period under review.

2.3 Notes that the approved maximum indicator for investment risk of 0.05% has been adhered to and the authorised borrowing limit and operational boundary have not been exceeded.

3. CONTEXT/ BACKGROUND INFORMATION

Economic Background

3.1. The council's treasury advisors, Link Asset Services (LAS) provide their assessment of the UK and global economic landscapes, and their interest rate forecast. This is included at Appendix 2.

Treasury Management Strategy

3.2. A summary of the action taken in the 6 months to September 2021 is provided in Appendix 3 to this report. The main points are:

- The council has entered into £25.0m of new borrowing during the period to support the HRA capital programme;
- The highest risk indicator during the period was 0.015% which is well below the maximum benchmark of 0.050%;
- The return on investments has exceeded the target benchmark rate;
- The two borrowing limits approved by full Council have not been exceeded.

3.5 Treasury management activity for the half-year has focused on a short-term horizon as summarised in the table below:

	Amount invested 1 Apr 2021 to 30 Sep 2021			
	Fixed deposits	Money market funds & Notice Accounts	Total	
Up to 1 week	-	£382.5m	£382.5m	77.5%
Between 1 week & 1 month	-	-	-	0%
Between 1 month & 3 months	£5.0m	£10.0m	£15.0m	3.0%
Over 3 months	£96.0m	-	£96.0m	19.5%
	£101.0m	**£392.5m**	**£493.5m**	**100.0%**

Summary of Treasury Activity April 2021 to September 2021

3.6 The following table summarises the treasury activity in the half year to September 2020 compared to the corresponding period in the previous year:

April to September	2020/21	2021/22
Long-term borrowing raised (General Fund)	(£0.0m)	(£0.0m)
Long-term borrowing raised (HRA)	(£0.0m)	(£25.0m)
Long-term borrowing repaid (i360)	£0.5m	£0.5m
Long-term borrowing repaid (General Fund)	£0.3m	£0.0m
Long-term borrowing repaid (HRA)	£0.4m	£0.0m
Short-term borrowing (raised)/repaid	(£1.5m)	£2.0m
Investments made	£375.7m	£493.5m
Investments maturing	(£382.7m)	(£396.4m)

3.7 As at TBM month 5 (August), an underspend of £1.866m had been reported within the Financing Costs Budget for the year. This underspend is largely as a result of a reduced minimum revenue provision due to a reduced need to borrow within the 2019/20 and 2020/21 capital programmes caused by the delay to capital projects.

3.8 The following table summarises how the day-to-day cash flows in the half-year have been funded compared to the same period in the previous year:

April to September	2020/21	2021/22

Net cash flow (shortage)/surplus	(£7.3m)	(£70.4m)
Represented by:		
Increase/(reduction) in long-term borrowing	(£1.2m)	£24.5m
Increase/(reduction) in short-term borrowing*	£1.5m	£2.0m
Reduction/(increase) in investments	£7.0m	(£97.1m)
Reduction/(increase) in bank balance	(£0.0m)	£0.2m

*including South Downs National Park external investments

Investment Strategy

3.9 A summary of investments made by the in-house team and outstanding as at 30 September 2021 in the table below shows that investments continue to be held in highly rated, short term instruments.

'AAA' rated money market funds	£59.11m	24.4%
'AA' rated institutions	£103.00m	42.6%
'A' rated institutions	£80.00m	33.0%
Total	**£242.11m**	**100.0%**
Period – less than one week	£69.11m	28.5%
Period – between one week and one month	£10.00m	4.1%
Period – between one month and three months	£20.00m	8.3%
Period – between three months and 1 year	£118.00m	48.8%
Period – 1 year +	£25.00m	10.3%
Total	**£242.11m**	**100.0%**

Risk

3.10 As part of the investment strategy for 2021/22 the Council agreed a maximum risk benchmark of 0.050% i.e. there is a 99.95% probability that the council will receive its investments back. The benchmark is a simple target that measures the risk based on the financial standing of counterparties and length of each investment based on historic default rates. The actual risk indicator has varied between 0.015% and 0.006% between April 2021 and September 2021. It should be remembered however that the benchmark is an 'average risk of default' measure and does not constitute an expectation of loss against a particular investment.

3.11 In July 2019, Internal Audit undertook an audit of the treasury management function. The audit concluded that "reasonable assurance" is provided on the effectiveness of the control framework operating and mitigating risks for treasury management. One medium and two low priority recommendations were provided; all recommendations have been actioned.

Compliance with the Annual Investment Strategy

3.12 For the reporting period, the information in this report provides assurance that the Annual Investment Strategy has been complied with in full.

3.13 The council is committed to its ethical investment policy and encourages counterparties to invest the council's funds ethically.

3.14 Within the last year, the council has been able to undertake investments in opportunities as follows:

- The Council invested £7.5m in Royal London's Investment Grade Short Dated Bond Fund in February 2021. This fund has exclusions for all companies that generate profits from income relating to armaments and tobacco;
- The council has undertaken £10m in fixed term Green deposits with Standard Chartered which support's Standard Chartered's investments in green technology.

3.15 These investments meet the council's requirements for security, liquidity and yield whilst enabling the furthering of Environmental, Social and Governance (ESG) criteria within the investment portfolio. Officers continue to look for opportunities in this area, but the market is relatively immature and there is some "catching up" in terms of the market being able to meet local authorities' aspirations in this area whilst delivering our core requirement of maintaining a high level of security of our investment portfolio.

Investment Performance

3.16 The council's investment portfolio achieved an average rate of 0.30% over the first six months of the year. This is against a benchmark rate of -0.08% for the same period. The industry standard benchmark rate is the 7 Day LIBID; the rate at which UK banks are willing to pay for borrowing for a 7-day period. This rate was negative in the six months to September 2021 due to very low short term interest rates in the market and a high supply of short-term cash. The Investment portfolio has therefore outperformed the benchmark by 0.38%. The average rate has reduced compared to 2020/21 (full year 0.62%) as expected.

3.17 The current forecast estimates that the average investment rate earned over the full year will remain at 0.30%. The market is forecasting that the official bank rate will increase sooner than originally expected, so new investments are able to be undertaken at higher interest rates than the current levels. However, cash balances are expected to reduce in the last 6 months of the year as a result of planned capital programme spend and government clawback of excess Covid Business Grants, and therefore few fixed term deposits will be undertaken in the second half of the year.

Borrowing Strategy

3.18 The council operates separate debt portfolios for the General Fund and the HRA following the introduction of the HRA Self-Financing regime in 2012.

3.19 The General Fund has been carrying an internal borrowing position (i.e. where the General Fund borrows cash from its own reserves) since 2008 as a response to the financial crisis. The reserves and balances are reviewed regularly to ensure that the cash will remain available to continue to support the internal borrowing.

3.20 The general fund internal borrowing position has reached £72.0m at the end of 2021/22, which is just below the level assessed as the maximum that that the reserves and balances are able to support. Additionally, market expectation of the timing of interest rates rises have changed following the MPC meeting in September 2021, with the council's treasury advisors (Link Asset Services - LAS) bringing forward their forecast of the first increase in the official bank Rate from

June 2023 to June 2022. Officers have therefore been reviewing borrowing options in consultation with LAS in order to ascertain whether new borrowing should be entered into to ensure sufficient cash is available to support current and future capital plans.

3.21 No new general fund borrowing was undertaken in the first six months of 2021/22. However, in November 2021 (and therefore in the second half of the year and outside of the period under review here), officers took advantage of a large temporary change in PWLB rates which was caused by investor reaction to central government's spending review. New long-term borrowing of £25.0m was undertaken at an average interest rate of 1.62%. This borrowing will be allocated between the General Fund and the HRA on assessment of the Capital Programme forecast at TBM7.

3.22 There is still a cost of carry of any new long-term debt that is undertaken: if borrowing is entered into and not applied to expenditure directly, it increases the level of cash balances requiring investment until it is spent. The cost of carry is the difference between the interest rate paid on borrowing compared with the interest that can be earned on investing the cash until it is spent. Consequently, officers are continually reviewing the levels of under-borrowing that the council's reserves can support to ensure an appropriate balance is struck between a number of risks including interest rate risk, holding sufficient cash when it's required (liquidity) and the cost of holding that cash.

3.23 The Housing Revenue Account (HRA) adopts a fully funded borrowing position (i.e. the HRA does not borrow from its own reserves, but instead undertakes borrowing for its entire borrowing requirement). The HRA has undertaken a number of new loans over the last 5 years to support its capital programme, including borrowing a total of £7m from the general fund on a short-term basis.

3.24 Most recently, £25.0m of PWLB borrowing was undertaken in July & August 2021 to support the 2021/22 capital programme. This borrowing was undertaken at a time when PWLB temporarily dropped, so officers took advantage of attractive interest rates compared to the prevailing rates and interest rate forecast. The £25.0m was undertaken as a series of long-term loans at an average rate of 1.61%.

3.25 The treasury team, along with the council's treasury advisors, monitor interest rates and will seek to externalise the remainder of the HRA's borrowing from the General Fund at a time which would be optimal for both the HRA and the General Fund. The treasury team are exploring alternative borrowing sources such as forward market borrowing for future capital investment plans.

3.26 A summary of the council's debt portfolio is summarised in Appendix 1.

Treasury Advisors

3.27 The council has a 4-year contract for treasury advisory services with Link Asset Services (LAS) which started 1 April 2020.

3.28 The council recognises that responsibility for decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers. It also recognises that there is value in employing external providers of treasury management services in order to access specialist skills and resources.

4. ANALYSIS & CONSIDERATION OF ANY ALTERNATIVE OPTIONS

4.1 This report sets out action taken in the 6 months to September 2021. Treasury management actions have been carried out within the parameters of the AIS, TMSS and Prudential Indicators. Therefore, no alternative options have been considered.

5. COMMUNITY ENGAGEMENT & CONSULTATION

5.1 The council's external treasury advisors have been consulted over the content of this report. No other consultation was undertaken.

6. CONCLUSION

6.1 Treasury management is governed by a code that is recognised as "best and proper practice" under the Local Government Act 2003. The Code requires a minimum of two reports per year, one of which is required to review the previous year's performance. This report fulfils that requirement.

7. FINANCIAL & OTHER IMPLICATIONS:

Financial Implications:

7.1 The financial implications of treasury management activity are reflected in the financing costs budget set out in paragraph 3.7

Finance Officer Consulted: James Hengeveld Date: 15/11/2021

Legal Implications:

7.2 The TMSS is approved and associated actions carried out under the powers given to the Council by Part 1 of the Local Government Act 2003 to invest for the purposes of the prudent management of its financial affairs (section 12).

7.3 Local authorities are required to have regard to statutory guidance in the form of the Prudential Code for Capital Finance in Local Authorities (2017 ed), issued by the Chartered Institute of Public Finance and Accountancy (CIPFA) when carrying out functions under Part 1 of the Act.

7.4 The Council's approach is consistent with the requirements of the Act and the Prudential Code.

Lawyer Consulted: Victoria Simpson Date:11/11/21

Equalities, Sustainability and other significant implications:

7.5 There are no direct implications arising from this report.

SUPPORTING DOCUMENTATION

Appendices:

1. Glossary of terms
2. The Economy & Interest Rates – Link Asset Services
3. A summary of the action taken in the period April 2021 to September 2021

Background Documents

1. Part I of the Local Government Act 2003 and associated regulations.
2. The Treasury Management Policy Statement 2021/22 (including the Annual Investment Strategy) approved by Policy & Resources Committee on 11 February 2021 and by full Council on 25 February 2021.
3. The Prudential Code for Capital Finance in Local Authorities 2017 published by CIPFA.
4. The Code for Treasury Management in Local Authorities 2017 published by CIPFA