Gateshead Council

AUDIT AND STANDARDS COMMITTEE
18 OCTOBER 2021

TITLE OF REPORT: **Treasury Management – Performance to 30 September 2021**

REPORT OF: **Darren Collins – Strategic Director, Resources & Digital**

Purpose of the Report

1. The purpose of this report is to review Treasury Management performance for the six months to 30 September 2021, covering investments and borrowing. This is consistent with approved performance management arrangements.

Background

2. The mid-year performance of the Treasury Management Service is reported in line with CIPFA's Code of Practice on Treasury Management and the Council's Treasury Policy Statement and Treasury Strategy which was approved by Council on 23 March 2021.

3. The Council operates a balanced approach, and this means broadly that cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensure this cash flow is adequately planned, with surplus monies being invested in low-risk counterparties, providing security and adequate liquidity initially before considering optimising investment return.

4. The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning to ensure the Council can meet its capital spending operations.

5. Accordingly, treasury management is defined as:

   "The management of the Council'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."

6. The primary objective of the investment strategy is to safeguard the Council's assets with a secondary objective of obtaining an optimum rate of return on investments and minimising the costs of borrowing.

Treasury Management Strategy Statement

7. The Treasury Management Strategy Statement (TMSS) for 2021/22 was approved by Council on 25 March 2021. There are no policy changes to the TMSS; the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

Investment Performance

8. The latest projection of gross investment income for 2021/22 based on interest earned to date and expected interest to March 2022 is £0.132m, compared to an original estimate of £0.076m.

9. This gross investment interest is adjusted to account for £0.041m interest payable to third parties and interest receivable of £1.401m from various third parties. This gives a projected net interest to the General Fund 2020/21 of £1.492m compared to the budget of £1.343m. The variance to budget is mainly as a result of higher levels of interest received on loans to third parties than was anticipated when the 2021/22 budget was set.

The Economy

10. The coronavirus outbreak has created huge economic damage to the UK and around the world. The Bank of England took emergency action in March 2020 to cut the Bank Rate to first 0.25% then to 0.10%. The 0.10% rate continues unchanged following the Bank of England Monetary Policy Committee meeting on 5 September 2021. The forecast now includes increases in Bank Rates in quarter 2 of 2022 of 0.25%, then quarter 2 of 2023 to 0.50% and a further increase in quarter 1 of 2024 to 0.75%.

Rate of Return

11. The average rate of return is monitored for each investment type the Council enters into and these are used to calculate an average rate of return for the year to date. The current rate of return is 0.17%, which is an improvement on the original estimate of 0.07%.

12. The quarterly LINK Asset Services Investment Benchmarking report assesses both the rate of return and the risk of the counterparty to calculate a weighted average rate of return, which is used for comparison across Local Authorities. In the most recent report received, June 2021, the Council achieved a weighted average rate of return of 0.18% on its investments for Quarter 1 2021/22 which is in line with the risk adjusted expectations (0.12% to 0.23%) defined in the Benchmarking Report for our Group.

13. The rate of return would be expected to decrease during the year as investment balances reduce and deposits are replaced for shorter terms with lower yielding returns.

14. It is currently a difficult investment market and the Council will be unable to match levels of interest rates achieved in previous financial years. The majority of available interest rates up to 12 months duration are at or below the bank rate of 0.10%. Given this risk environment and the fact that significant increases in Bank Rate are unlikely to occur until the end of the current financial year 31st March 2023, investment returns are expected to remain low.

Borrowing

14. The total borrowing for the Council and HRA as at 31 September 2021 was £649.151m, which was within the operational borrowing limit of £850m. This

borrowing is made up of £596.651m Public Works Loans Board (PWLB) loans and £52.5m market loans.

15. The Treasury Strategy estimates for the 2021/22 financial year were based on a borrowing requirement of £107.351m with £77.602m relating to the GF and £29.749m the HRA. However, due to the council holding high levels of cash reserves no borrowing has been taken in the year to date. The timing of further borrowing will depend on a combination of cash flow requirements to support the capital programme and achieving preferential borrowing rates.

16. The current forecast for interest payable on borrowing is allocated to the General Fund and the Housing Revenue Account (HRA) as shown in the following table:

	General Fund	**HRA**
Interest Payable	£11.572m	£12.022m
Average rate of interest	3.18%	3.89%

This represents a gross saving of £0.863m on the original estimate, of which £0.644m is a saving for the General Fund and £0.219m is for the HRA.

PWLB Government Intervention

17. The Government undertook a consultation exercise on the Prudential Code for PWLB borrowing during summer 2020. This resulted in the Treasury no longer allowing local authorities to borrow money from the PWLB primarily for commercial yield.

18. An additional consultation on the Prudential Code was announced on 24 September 2021 to further clarify and update the position on local authority commercial investment and introduce new affordability indicators.

Summary of Mid-Year Performance

19. The projected net impact of investment and borrowing activity on the revenue budget in 2021/22 is an underspend of £1.012m, comprising £0.793m General Fund and £0.219m HRA.

	General Fund			**HRA**		
	Estimate	Projected Outturn	Variance	Estimate	Projected Outturn	Variance
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Investments	(1.343)	(1.492)	(0.149)	(0.020)	(0.020)	0.000
Borrowing	12.216	11.572	(0.644)	12.241	12.022	(0.219)
Premia	0.046	0.046	0.000	0.000	0.000	0.000
Net Position	**11.335**	**10.542**	**(0.793)**	**12.221**	**12.033**	**(0.219)**

20. Investment returns are likely to remain relatively low during 2021/22 then beyond and interest rates are expected to be below long-term borrowing rates therefore value for money considerations indicate that best value can be obtained by delaying new external borrowing and by using internal cash balances to finance new capital expenditure in the short term (this is referred to as internal borrowing).

21. The current approach of borrowing internally provides benefits in terms of reduced credit risk, as the Council has less cash invested than if it had gone to the markets and borrowed externally. This means that cash balances and investment returns, remain historically low resulting in reduced levels of income, which at present is outweighed by the savings achieved from avoiding external borrowing. The additional element of interest rate risk will continue to be monitored.

Recommendation

The Committee is requested to note the Treasury Management Performance to 30 September 2021, prior to submission to Cabinet.