

**TITLE OF REPORT:** Treasury Management – Performance to 30 September 2020

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

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### **Purpose of the Report**

1. The purpose of this report is to review Treasury Management performance for the six months to 30 September 2020, covering investments and borrowing. This is consistent with approved performance management arrangements.

### **Background**

2. Cabinet will receive half yearly performance reports on the agreed Treasury Management budget identifying any variances. This report sets out the monitoring position at 30 September 2020.
3. Council agreed the Treasury Policy Statement and Treasury Strategy 2020/21 to 2024/25 which provided a framework for the Strategic Director, Resources and Digital to exercise his delegated powers on 16 July 2020.
4. Council also agreed the original General Fund budget for Treasury Management for 2020/21 on 27 February 2020. This was set at £11.586m.

### **Proposals**

5. The projected outturn for 2020/21 at 30 September 2020 is £11.259m compared to the estimate of £11.586m, an underspend on budget of £0.327m.
6. The Audit and Standards Committee reviewed the Treasury Management performance to 30 September 2020 on 19 October 2020 and raised no comments for submission to Council.
7. It is important that effective budget monitoring and action planning is in place to ensure that spending in 2020/21 is contained within approved budgets as this will contribute to a sustainable financial position for the Council.

### **Recommendation**

8. Cabinet is asked to recommend that Council note the Treasury Management Performance to 30 September 2020.

For the following reason:

To contribute to sound financial management and the long-term financial sustainability of the Council.

**Policy Context**

1. The proposals in this report are consistent with Council priorities and in particular they ensure that effective use is made of the Council's resources to ensure a sustainable financial position and support of the framework for achieving the Council's strategic approach 'Making Gateshead a Place Where Everyone Thrives'. The Council recognises there are huge financial pressures on not just Council resources, but those of partners, local businesses and residents. This requires the Council's decision-making to be policy and priority led and driven.

**Background**

2. The Prudential Code plays a key role in capital finance in local authorities. Local authorities determine their own programmes for capital investment that are central to the delivery of quality public services. The Prudential Code was developed by CIPFA, the Chartered Institute of Public Finance and Accountancy, as a professional code of practice to support local authorities in taking their decisions. Local authorities are required by regulation to have regard to the Prudential Code when carrying out their duties in England and Wales under Part 1 of the Local Government Act 2003.
3. In December 2017 CIPFA issued a revised Treasury Management Code of Practice and a revised Prudential Code (the Code) which represent best practice. The Council fully complies with the Code and this contributes towards achieving good practice.
4. Part 1 of the Local Government Act 2003 specifies the powers of a local authority to borrow for any purpose relevant to its functions under any enactment or for the purposes of the prudent management of its financial affairs. Borrowing is linked to the CIPFA Prudential Code for Capital which sets out a range of prudential and treasury indicators that must be calculated to ensure borrowing is affordable, prudent and sustainable. The Prudential Code refers to the need for a clear and integrated treasury strategy.
5. In addition, under Section 15 of the Local Government Act 2003, authorities are required to have regard to the MHCLG's guidance on Local Government Investments. This document stipulates the requirement for an annual investment strategy to be integrated into the Council's Treasury Strategy.
6. Under Part 4 of the Council's Constitution the Strategic Director, Resources and Digital will produce a Treasury Policy Statement annually, setting out the general policies and objectives of the Council's treasury management function.
7. The Council also provides a treasury management service to the Gateshead Housing Company through a Service Level Agreement.

## **Mid-Year Performance to 30 September 2020**

8. This report sets out the latest position on the 2020/21 Treasury Management budget as at 30 September 2020 and projects interest on borrowing and investment income to the end of the financial year.
9. The projected outturn for 2020/21 at 30 September 2020 is £11.259m compared to the estimate of £11.586m, a projected under spend of £0.327m. The underspend is made up of several elements:
  - a) Borrowing costs are lower than budget. Due to the uncertainty surrounding COVID-19 £30.000m of long term PWLB borrowing was taken in March 2020 which reduced the need for borrowing in the current financial year and subsequently no borrowing has been taken in the financial year to date.
  - b) Investment interest achieved in the year to date is lower than budgeted estimates. This is mainly as a result of interest on loan notes due from Newcastle International Airport which will not be received this year due to a curtailment in operations of the airport as a result of COVID-19 as well as reduced returns on investments as a direct result of a cut in the Bank of England base rate.
  - c) Investment interest received from loans to the Council trading companies is projected to be more than budgeted, offsetting some of the reduction in interest earned on investments and the Airport loan notes.
10. Appendix 2 details the budget for 2020/21 compared to an assessment of the projected outturn for the year.

## **Consultation**

11. The Leader of the Council has been consulted on this report.

## **Alternative Options**

12. There are no alternative options, as the Treasury Management mid-year performance report recommended for approval is required to comply with the policy on delegation, review requirements and reporting arrangements as outlined in the Treasury Policy Statement and Treasury Strategy.

## **Implications of Recommended Options**

13. **Resources:**
  - a) **Financial Implications** - The Strategic Director, Resources and Digital confirms that the financial implications are set out in this report. There are no additional financial implications associated with the report itself.
  - b) **Human Resources Implications** - There are no human resources implications arising from this report.
  - c) **Property Implications** – There are no property implications arising from this report.

**14. Risk Management Implications**

The Treasury Policy and Treasury Strategy which informs activity in this area were prepared with the primary aim of minimising risk to ensure that the Council's principal sums are safeguarded. Maximising income is considered secondary to this main aim.

**15. Equality and Diversity Implications**

There are no equality and diversity implications arising from this report.

**16. Crime and Disorder Implications**

There are no crime and disorder implications arising from this report.

**17. Health Implications**

There are no health implications arising from this report.

**18. Climate Emergency and Sustainability Implications**

There are no climate emergency or sustainability implications arising from this report.

**19. Human Rights Implications**

There are no human rights implications arising from this report.

**20. Ward Implications**

There are no direct area and ward implications arising from this report.

## Mid-Year Report - Performance to 30 September 2020

### 1. Investment Performance

- 1.1 The latest projection of gross investment income for 2020/21 based on interest earned to date and expected interest to March 2020 is £0.391m, compared to an original estimate of £0.663m.
- 1.2 This gross investment interest is adjusted to account for £0.326m interest payable to third parties and interest receivable of £1.053m from various third parties. This gives a projected net interest to the General Fund 2020/21 of £1.118m compared to the budget of £1.855m. The variance to budget is mainly as a result of interest on loan notes due from Newcastle International Airport which will not be received this year due to a curtailment in operations of the airport as a result of COVID-19 as well as reduced returns on investments as a direct result of a cut in the Bank of England base rate. This is partially offset by higher levels of interest received on loans to third parties than was anticipated when the 2020/21 budget was set.

### 2. The Economy

- 2.1 The coronavirus outbreak has created huge economic damage to the UK and around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its last meeting on 6th August, although some forecasters had suggested that a cut into negative territory could happen. No increase in Bank Rate is expected prior to 31st March 2023 as economic recovery is expected to be only gradual and, therefore, prolonged.

### 3. Rate of Return

- 3.1 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 0.42%, which is less than the original estimate of 0.91%.
- 3.2 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 2020, the Council achieved a weighted average rate of return of 0.35% on its investments for Quarter 1 2020/21 which is in line with the risk adjusted expectations (0.32% to 0.53%) defined in the Benchmarking Report for our Group.
- 3.3 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.
- 3.4 It is currently a difficult investment market; it is now not possible to earn the level of interest rates commonly seen in previously as all investment rates up to 12 months are either negative or just above zero now that Bank Rate is at 0.10%. Given this risk environment and the fact that increases in Bank Rate are unlikely to occur before the end of the current financial year 31st March 2023, investment returns are expected to remain low.

## 4 Borrowing

- 4.1 The total borrowing for the Council and HRA as at 30 September 2020 was £664.206m, which was within the operational borrowing limit of £865.000m. This borrowing is made up of £616.206m Public Works Loans Board (PWLB) loans and £48.000m market loans.
- 4.2 The Treasury Strategy estimates for the 2020/21 financial year were based on a borrowing requirement of £98.181m however, due to the uncertainty surrounding COVID-19 £30.000m of long term PWLB borrowing was taken in March 2020 which reduced the need for borrowing in the current financial year and subsequently no borrowing has been taken in the financial 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.
- 4.3 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:

	<b>General Fund</b>	<b>HRA</b>
Interest Payable	£11.915m	£13.047m
Average rate of interest	3.39%	3.83%

This represents a gross saving of £1.363m on the original estimate, of which £1.064m is a saving for the General Fund and £0.299m is for the HRA.

## 5 PWLB Government Intervention

- 5.1 PWLB lending is offered at a fixed margin above the Government's cost of borrowing, as measured by gilt yields. The Treasury raised the margin over gilts to 100bps (one percentage point) on 9th October 2019 and agreed to monitor the impact of the change and keep rates policy under review.
- 5.2 The Government undertook a consultation exercise on PWLB borrowing which closed on 31st July 2020.
- 5.3 The Treasury are proposing that they will no longer allow local authorities to borrow money from the PWLB to purchase commercial property if the aim is solely to generate an income stream. It is possible that the non-HRA Certainty Rate will be subject to revision downwards after the conclusion of the PWLB consultation; however, the timing of such a change is currently an unknown, although it would be likely to be within the current financial year.

## 6 Summary of Mid-Year Performance

- 6.1 The projected net impact of investment and borrowing activity on the revenue budget in 2020/21 is an underspend of £0.576m, comprising £0.327m General Fund and £0.249m HRA.

<b>General Fund</b>	<b>Estimate £m</b>	<b>Projected Outturn £m</b>	<b>Variance £m</b>
Investments	(1.855)	(1.118)	0.737
Borrowing	12.979	11.915	(1.064)
Premia	0.462	0.462	0.000
Net Position	11.586	11.259	(0.327)

- 6.2 Investment returns are likely to remain relatively low during 2020/21 and 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).
- 6.3 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, are 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.