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### TREASURY MANAGEMENT ANNUAL REVIEW REPORT 2020/21

#### 1. INTRODUCTION AND BACKGROUND

The Chartered Institute of Public Finance and Accountancy's Code of Practice on Treasury Management 2009 was adopted by this Council in February 2010 and this Council fully complies with its requirements. The Code was revised in 2011 and further revised in 2017.

The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
3. Receipt by the Council of an annual treasury management strategy report (including the annual investment strategy report) for the year ahead, a mid year review and an annual review report of the previous year.
4. 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, which in this Council is the Chief Officer Resources.
5. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specified named body which in this Council is the Corporate Overview Scrutiny Committee.

Treasury management in this context is defined as:

*"The management of the local authority's 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."*

The purpose of this report is to meet one of the above requirements of the CIPFA Code, namely the annual review report of treasury management activities, for the financial year 2020/21.

#### 2. THIS TREASURY MANAGEMENT ANNUAL REVIEW REPORT COVERS

- ❖ economic Background during the period
- ❖ the Council's treasury position as at 31st March 2021;
- ❖ borrowing and investment rates for 2020/21;
- ❖ annual review of the borrowing strategy 2020/21;
- ❖ borrowing outturn for 2020/21;
- ❖ debt rescheduling for 2020/21;
- ❖ compliance with treasury limits and Prudential Indicators for 2020/21;
- ❖ annual review of the investment strategy for 2020/21;
- ❖ investment outturn for 2020/21;

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#### 3. ECONOMIC BACKGROUND DURING PERIOD

PWLB rates are based on, and are determined by, gilt (UK Government bonds) yields through H.M.Treasury determining a specified margin to add to gilt yields. The main influences on gilt yields are Bank Rate, inflation expectations and movements in US treasury yields. Inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation and the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years. Gilt yields fell sharply from the start of 2020 and then spiked up during a financial markets melt down in March 2020 caused by the pandemic hitting western countries; this was rapidly countered by central banks flooding the markets with liquidity. Once the UK vaccination programme started making rapid progress in the new year of 2021, gilt yields and PWLB rates started rising sharply as confidence in economic recovery rebounded. Financial markets also expected Bank Rate to rise.

At the close of the day on 31 March 2021, all gilt yields from 1 to 5 years were between 0.19 – 0.58% while the 10-year and 25-year yields were at 1.11% and 1.59%.

HM Treasury imposed two changes of margins over gilt yields for PWLB rates in 2019/20 without any prior warning. The first took place on 9<sup>th</sup> October 2019, adding an additional 1% margin over gilts to all PWLB period rates. That increase was then, at least partially, reversed for some forms of borrowing on 11<sup>th</sup> March 2020. A consultation was then held with local authorities and on 25<sup>th</sup> November 2020, the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates; the standard and certainty margins were reduced by 1% but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three-year capital programme. The new margins over gilt yields are as follows: -.

- **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB Certainty Rate** is gilt plus 80 basis points (G+80bps)
- **PWLB HRA Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB HRA Certainty Rate** is gilt plus 80bps (G+80bps)
- **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)

There is likely to be only a gentle rise in gilt yields and PWLB rates over the next three years as the Bank Rate is not forecast to rise from 0.10% until March 2024 as the Bank of England has clearly stated that it will not raise rates until inflation is sustainably above its target of 2%; this sets a high bar for Bank Rate to start rising.

**Change in strategy during the year** – the strategy adopted in the original Treasury Management Strategy Report for 2020/21 approved by the Council in March 2020 was subject to revision during the year, due to the agreement by Welsh Government to issue the Authority with a specific loan in relation to the Rail Track project, this resulted in the Operational Boundary and the Authorised limits being amended accordingly.

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#### 4. TREASURY POSITION AS AT 31st MARCH 2021

The Council's debt and investment position at the beginning and the end of the year was as follows:

This illustrates that the total debt outstanding as at 31st March 2021 was £235.649 million, comprising of long term debt of £170.334 million and short term debt of £65.315 million.

	31 March 2020 Principal	Average Rate/ Return	31 March 2021 Principal	Average Rate/ Return	Increase/ (Decrease ) in Borrowing
	<u>£000</u>		<u>£000</u>		<u>£000</u>
Fixed Rate Funding:					
- PWLB	79,430	4.71%	76,764	4.05%	(2,666)
- Market Loans	14,000	1.67%	17,000	1.38 %	3,000
Variable Rate Funding:					
- Market (LOBO *)	4,000	4.5%	4,000	4.5%	0
<i>Rail &amp; Town Centre Loan</i>	<b>0</b>	<b>0</b>	<b>72,570</b>	<b>0.00%</b>	<b>72,570</b>
<b>Total Long Term Debt</b>	<b>97,430</b>	<b>4.10%</b>	<b>170,334</b>	<b>2.08%</b>	<b>72,904</b>
Short Term Loans(<365 days)	60,699	0.86%	65,315	0.52%	4,616
<b>Total Debt</b>	<b>158,129</b>	<b>2.86%</b>	<b>235,649</b>	<b>1.72%</b>	<b>77,520</b>
Investments:					
- Short Term	0		84,870		84,870
<b>Total Investments</b>	<b>0</b>		<b>84,870</b>		<b>84,870</b>

\* LOBO – Lenders Option Borrowers Option. This loan has a fixed rate for the first two years of 3.85%. The remaining period of the loan (which we are now in) has a rate of 4.5%, but the lender can increase this rate at six month intervals.

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#### 5. BORROWING AND INVESTMENT RATES IN 2020/21

The following table displays a selection of interest rates prevailing as at 1<sup>st</sup> April 2020 and 31<sup>st</sup> March 2021.

	01/04/2020	31/3/2021
Bank Base Rate	0.10%	0.10%
7 day LIBID	0.01%	0.08%
PWLB 10 year Maturity	2.34%	1.91%
PWLB 15 year maturity	2.64%	2.20%
PWLB 25 year maturity	2.85%	2.39%

#### 6. ANNUAL REVIEW OF THE BORROWING STRATEGY FOR 2020/21

The Treasury Management Strategy Statement for 2020/21 was approved by Council in July 2020. The Borrowing Strategy adopted as part of this was as follows:

*To utilise the Authority's overdraft facility:*

to fund unexpected daily cash deficits;  
to fund temporary cash shortfalls where there are no other sources of funding available within the marketplace.

*To borrow over the short term:*

to fund temporary cash shortfalls;  
to maintain a suitably balanced maturity profile;  
to make short term savings required in order to meet budgetary constraints;  
in anticipation of securing longer term loans at more attractive rates.

*To borrow over the long term:*

to reduce the Authority's average cost of borrowing;  
to maintain a stable, longer term portfolio;  
to maximise the potential for future debt rescheduling.

*If appropriate to avoid all new external borrowing:*

to maximise savings in the short term;  
to run down temporary investment levels;  
to minimise exposure to interest rate and credit risk.

Borrowings undertaken during the period (see section 7 below) have been done so in accordance with this strategy and has focused on short term borrowings in order to minimise borrowing costs. Current short term borrowing rates continue to be very low (despite the change to PWLB rates) and are forecast to stay at these levels for the foreseeable future. The Authority is therefore taking advantage of such rates and is predominantly borrowing short term to fund the remainder of its capital expenditure and maturing debt until such time the market indicates that long term rates are more advantageous. Throughout the 2020/21 financial year long term rates started to fall,

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Welsh Government awarded the Authority a specific interest-free loan in relation to the Rail Track project, this resulted in longer term borrowing increasing by £70million.

In the current economic climate, it is considered that the approved strategy is still fit for purpose and therefore no revisions are proposed.

### 7. BORROWING OUTTURN FOR 2020/21

#### Long Term Borrowing

##### *Definition*

Long term borrowing relates to debt taken out for a period of greater than one year. It is taken out for periods of 1 year up to 50 years. This borrowing is required to finance capital expenditure undertaken in the year that is funded through:

- Borrowing approvals from Welsh Government, known as un-hypothecated supported borrowing (USB), for which revenue support for the borrowing costs is provided through the revenue support grant;
- Prudential borrowing, for which borrowing costs are funded through revenue savings.

##### ***Total outstanding as at 31<sup>st</sup> March 2021***

The total long term debt outstanding as at 31st March 2021 was £170.334 million. This is made up of debt taken from the Public Works Loan Board (PWLB), from other local authorities (through the market place), and from the market (LOBO). This debt is due to be repaid within the following years:

<b>Maturing Within</b>	<b>£000s</b>
1YR	5,698
1-2YRS	10,920
2-3YRS	10165
3-4YRS	15,451
4-5YRS	3276
5-6YRS	12,610
6-10YRS	16,429
10-15YRS	12,961
15+ YRS	82,824
<b>Total</b>	<b>170,334</b>

##### ***New borrowings for 2020/21***

During 2020/21, the Authority did take £73m long term debt, predominantly from Welsh Government, this related to a specific loan in relation to the Rail Track project..

#### Short Term Borrowing

##### *Definition*

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Short term borrowing relates to debt taken out for a period of less than one year i.e. it will all be fully repaid within a year. These short term loans are taken out to manage the Authority's short term cash flow i.e. to fund deficits in cash flow on a daily basis pending receipt of income from grants or other sources, or pending the taking out of longer term debt to fund capital expenditure whilst we wait for advantageous longer term borrowing opportunities. Current short term borrowing rates are very low and are forecast to stay at these levels for the foreseeable future. The Authority is therefore taking advantage of such rates and is borrowing short term to fund the remainder of its capital expenditure and maturing debt until such time the market indicates that long term rates are more advantageous.

#### **Total outstanding as at 31st March 2021**

The total short term debt outstanding as at 31st March 2021 was £65.3 million. This is made up of debt taken from other local authorities through the market place.

#### **New borrowings for 2020/21**

Appendix A lists the short term loan activity during the year and shows that over the period a total of £60.8 million loans were brought forward from the previous year and £105 million of new short term loans were raised. A total of £100.5 million of these new loans were repaid during the year (including the brought forward loans) leaving a balance outstanding as at 31st March 2021 of £65.3 million.

The following table gives a summary which shows that the average rate of interest paid was well within the benchmark.

	Total Value of Loans during the period	Average Loan	Interest paid during the period	Average Interest Rate	Benchmark Interest Rate *
<b>Short Term borrowing</b>	£165.815M	£2.81M	£265k	0.83%	1.00%

\* Benchmark = budgeted interest rate for new borrowings 1.00%

### 7. DEBT RESCHEDULING

No debt rescheduling was undertaken during the period.

### 8. COMPLIANCE WITH TREASURY LIMITS

During the financial year the Council operated within the treasury limits and Prudential Indicators set out in the Treasury Strategy Statement 2020/21, approved by Council in March 2012.

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#### Operational Boundary for external debt

The Council resolved that this limit be set at £237 million for 2020/21 (£167 million prior to receipt of rail loan). The level of borrowings on the 31st March was £236 million this is within the required limit.

The operational boundary can be exceeded on an occasional basis, this is likely to be due to the volume of payments being made in relation to capital spend at the year end and the delay in receiving grant funding this is therefore to be expected due to cash flow fluctuations. Sustained breaches however, would indicate that either the limit has been set too low, or that the Authority is breaching its prudential boundaries and that corrective action needs to be taken.

Monitoring of the operational boundary is undertaken on a daily basis and any such continual breaches would be investigated and a recommended course of action reported to Council.

#### Authorised Limit for external Debt

The Council resolved that this limit be set at £258 million for 2020/21 (£183 million prior to receipt of rail loan). The Authorised Limit is set having regard to the operational boundary above.

The average level of borrowings for the year to the 31st March was £149 million, so well within the limit set.

The Authorised Limit must not be breached.

#### Maturity Structure of Fixed Rate Borrowing

The Council resolved the following limits for the maturity structure of fixed rate borrowings for 2020/21:

	Upper Limit	Lower Limit	Actual as at 31/3/2021
under 12 months	20%	0%	3.34%
12 months and within 24 months	20%	0%	6.41%
24 months and within 5 years	50%	0%	16.96%
5 years and within 10 years	75%	0%	17.05%
10 years and above	95%	25%	56.23%

The actual debt maturity profile at 31st March 2021 is well within the limits set.

#### Upper Limit on Variable Interest Exposure

Council resolved the upper limit on variable rate exposures for 2020/21 should be set at 30% of outstanding long term debt. This strategy limits the proportion of interest which is subject to variable rate terms and hence protects the Council against increased costs in times of rising interest rates.

The actual level of variable borrowings is £4 million (LOBO) which equates to 2.35% of the outstanding long term debt as at 31st March 2021, so is well within the limit set.

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#### 9. ANNUAL REVIEW OF INVESTMENT STRATEGY FOR 2020/21

The Annual Investment Strategy for 2020/21 adopted by Council in March 2021, was to maintain only temporary, short term investments and to make those investments in accordance with anticipated cash flow requirements (including the investing of sums borrowed at prevailing low interest rates in anticipation of capital spending). The Council's investment priorities are:

- a. the security of capital;
- b. the liquidity of its investments.

The Council also aims to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite of this Council is low in order to give priority to the security of its investments.

In order to ensure that the Authority's investments are secure and that risk is minimised an investment matrix is used to determine investment counterparties, which factors in Fitch and Moody's credit ratings, credit default swap (CDS) spread data, and credit rating agency comments.

This strategy has been adhered to in determining the investments for 2020/21 outlined in section 10 below.

#### 10. INVESTMENT OUTTURN FOR 2020/21

Appendix B gives details of the investments made during the year, and the following table gives a summary, which shows the Authority's average rate of return was below the benchmark.. This is in line with the Authority's risk averse policy whereby the security of the capital sum is the number one priority at the expense of competitive investment returns.

	Total Value of Investments	Average Investment	Investment Returns	Average Rate of Return	Benchmark Return *
<b>Internally Managed</b>	£400M	£3.0	£7.8k	0.04%	0.08%

\* Benchmark = 7 day LIBID

0.08%

No institutions in which investments were made had any difficulty in repaying investments and interest in full during the year.