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### TREASURY MANAGEMENT ANNUAL REVIEW REPORT 2019/2020

#### 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 2019/20.

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

- ❖ Economic Background during the period
- ❖ the Council's treasury position as at 31st March 2020;
- ❖ borrowing and investment rates for 2019/20;
- ❖ annual review of the borrowing strategy 2019/20;
- ❖ borrowing outturn for 2019/20;
- ❖ debt rescheduling for 2019/20;
- ❖ compliance with treasury limits and Prudential Indicators for 2019/20;
- ❖ annual review of the investment strategy for 2019/20;
- ❖ investment outturn for 2019/20;

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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. There was much speculation during the second half of 2019 that bond markets were in a bubble which was driving bond prices up and yields down to historically very low levels. Gilt yields were on a generally falling trend during the last year up until the coronavirus crisis hit western economies. Since then, gilt yields have fallen sharply to unprecedented lows as investors have panicked, selling shares in anticipation of impending recessions in western economies, and moving cash into safe haven assets i.e. government bonds. Major western central banks also started quantitative easing purchases of government bonds which will act to maintain downward pressure on government bond yields at a time when there is going to be a huge and quick expansion of government expenditure financed by issuing government bonds; (this would normally cause bond yields to rise). At the close of the day on 31 March, all gilt yields from 1 to 5 years were between 0.12% – 0.20% while even 25-year yields were at only 0.83%.

HM Treasury also imposed **two changes in the margins over gilt yields for PWLB rates** during 2019-20 without any prior warning; the first on 9 October 2019, added an additional 1% margin over gilts to all PWLB rates. That increase was then partially reversed for some forms of borrowing on 11 March 2020, at the same time as the Government announced in the Budget a programme of increased spending on infrastructure. It also announced that there would be a consultation with local authorities on possibly further amending these margins. It is clear that the Treasury intends to put a stop to local authorities borrowing money (at preferential rates) from the PWLB to purchase commercial property if the aim is solely to generate an income stream.

Following the changes on 11 March 2020 in margins over gilt yields, the current situation is as follows: -

- **PWLB Standard Rate** is gilt plus 200 basis points (G+200bps)
- **PWLB Certainty Rate** is gilt plus 180 basis points (G+180bps)
- **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 little upward movement in PWLB rates over the next two years as it will take national economies a prolonged period to recover all the momentum they will lose in the sharp recession caused during the coronavirus shut down period. Inflation is also likely to be very low during this period and could even turn negative in some major western economies during 2020-21.

#### 4. TREASURY POSITION AS AT 31st MARCH 2020

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

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This illustrates that the total debt outstanding as at 31st March 2020 was £158.129 million, comprising of long term debt of £97.430 million and short term debt of £60.699 million.

	31 March 2019 Principal	Average Rate/ Return	31 March 2020 Principal	Average Rate/ Return	Increase/ (Decrease) in Borrowing
	<u>£000</u>		<u>£000</u>		<u>£000</u>
Fixed Rate Funding:					
- PWLB	72,700	4.64%	79,430	4.71%	6,730
- Market Loans	19,000	2.05%	14,000	1.67%	(5,000)
Variable Rate Funding:					
- Market (LOBO *)	4,000	4.5%	4,000	4.5%	0
<b>Total Long Term Debt</b>	<b>95,700</b>	<b>4.19%</b>	<b>97,430</b>	<b>4.10%</b>	<b>1,730</b>
Short Term Loans(<365 days)	61,649	0.90%	60,699	0.86%	(950)
<b>Total Debt</b>	<b>157,349</b>	<b>2.85%</b>	<b>158,129</b>	<b>2.86%</b>	<b>780</b>
Investments:					
- Short Term	6,000		0		(6,000)
<b>Total Investments</b>	<b>6,000</b>		<b>0</b>		<b>(6,000)</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.

## 5. BORROWING AND INVESTMENT RATES IN 2019/20

The following table displays a selection of interest rates prevailing as at 1<sup>st</sup> April 2019 and 31st March 2020.

	01/04/2019	31/3/2020
Bank Base Rate	0.75%	0.10%
7 day LIBID	0.57%	0.01%
PWLB 10 year Maturity	2.05%	2.34%
PWLB 15 year maturity	2.37%	2.64%
PWLB 25 year maturity	2.60%	2.85%

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#### 6. ANNUAL REVIEW OF THE BORROWING STRATEGY FOR 2019/20

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 19/20 financial year long term rates started to fall and the Council converted £10m of short term debt into long term debt, with a view to making further conversions in 2020/2021.

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 2019/20

##### 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;

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- Prudential borrowing, for which borrowing costs are funded through revenue savings.

#### **Total outstanding as at 31<sup>st</sup> March 2020**

The total long term debt outstanding as at 31st March 2020 was £97.430 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:

Maturing Within	£000s
1YR	8,666
1-2YRS	5,697
2-3YRS	7,920
3-4YRS	2,764
4-5YRS	14,051
5-6YRS	1,877
6-10YRS	23,439
10-15YRS	5,962
15+ YRS	27,054
<b>Total</b>	<b>97,430</b>

#### **New borrowings for 2019/20**

During 2019/20, the Authority did take £10m long term debt from the PWLB towards the end of the financial year to replace maturing loans and finance capital expenditure.

#### **Short Term Borrowing**

##### **Definition**

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 31<sup>st</sup> March 2020**

The total short term debt outstanding as at 31st March 2020 was £60,699 million. This is made up of debt taken from other local authorities through the market place.

#### **New borrowings for 2019/20**

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Appendix A lists the short term loan activity during the year and shows that over the period a total of £61.699 million loans were brought forward from the previous year and £131.500 million of new short term loans were raised. A total of £132.500 million of these new loans were repaid during the year (including the brought forward loans) leaving a balance outstanding as at 31st March 2020 of £60.699 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 *
Short Term borrowing	£193,199M	£2.45M	£488k	1.09%	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 2019/20, approved by Council in March 2019.

#### Operational Boundary for external debt

The Council resolved that this limit be set at £155 million for 2019/20. The level of borrowings on the 31st March was £158 million this exceeds the limit slightly.

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.

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#### Authorised Limit for external Debt

The Council resolved that this limit be set at £171 million for 2019/20. 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 £158 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 2019/20:

	Upper Limit	Lower Limit	Actual as at 31/3/2020
under 12 months	20%	0%	8.89%
12 months and within 24 months	20%	0%	5.85%
24 months and within 5 years	50%	0%	25.39%
5 years and within 10 years	75%	0%	25.98%
10 years and above	95%	25%	33.89%

The actual debt maturity profile at 31st March 2020 is well within the limits set.

#### Upper Limit on Variable Interest Exposure

Council resolved the upper limit on variable rate exposures for 2019/20 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 4.1% of the outstanding long term debt as at 31st March 2020, so is well within the limit set.

### 9. ANNUAL REVIEW OF INVESTMENT STRATEGY FOR 2019/20

The Annual Investment Strategy for 2019/20 adopted by Council in March 2018, 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.

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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 2019/20 outlined in section 10 below.

#### 10. INVESTMENT OUTTURN FOR 2019/20

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>	£321M	£2.5	£61k	0.46%	0.54%

\* Benchmark = 7 day LIBID

0.54%

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