Item No. 9.	Classification: Open	Date: 18 November 2020	Meeting Name: Audit, governance and standards committee
Report title:		Capital and treasury management strategy 2021-22	
Ward(s) or groups affected:		All	
From:		Strategic Director of Finance and Governance	

RECOMMENDATIONS

1. That the audit governance and standards committee note the draft Capital Strategy and Treasury Management Strategy 2021-22.

BACKGROUND INFORMATION

2. Each year council assembly agrees an annual strategy covering the management of council debt, capital and treasury investments. The strategy is to be agreed following consultation with the audit, governance and standards committee.

3. Treasury management is the management of the authority's cash flows, borrowing and investments. The council is exposed to financial risks from treasury management activity including possible losses associated with council investment and potential for increased borrowing costs arising from market movements. The identification, monitoring and control of financial risks are therefore a crucial part the financial management and governance arrangements of the council.

4. Since 2019-20 the council is required to produce a capital strategy report (Appendix A) providing a high level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how any associated risks are managed and the implications for future financial sustainability.

5. The impact on the UK from coronavirus, together with its exit from the European Union and future trading arrangements, will remain a major influence on the Authority's treasury management strategy for 2021-22.

6. Under financial delegation, the strategic director of finance and governance is responsible for all executive and operational decisions on treasury management. This treasury management strategy, together with supporting prudential indicators and policies will ensure that these responsibilities can be carried out effectively.

KEY ISSUES FOR CONSIDERATION

Borrowing strategy and debt management activity and position

7. The council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required.

8. The council's debt management strategy is to pursue a policy of internal borrowing, which is the use of existing reserves and balances to temporarily fund capital expenditure, where possible, rather than the use of external borrowing.

9. The use of internal borrowing allows the council to minimise unnecessary external borrowing costs by only borrowing when needed for liquidity, or to benefit from advantageous borrowing rates. Efficient use of existing council resources to fund capital expenditure through internal borrowing also reduces the council's counterparty risk inherent in the investment of cash balances.

10. To finance capital expenditure and to maintain minimum cash balances, the council has also needed to borrow externally. During the financial year to 31 March 2020 the council borrowed £81m from the Public Works Loans Board (PWLB), as part of HM Treasury. The loans were taken with fixed rates with maturities between 8 and 49 years at an average interest rate of 1.58%.

11. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans. By doing so, the Authority is able to reduce net borrowing costs and reduce overall treasury risk.

12. Drawing of long term borrowing has therefore been supplemented by short term borrowing from other local authorities to reduce the overall debt interest expense for the council. The level of short term borrowing from other local authorities as at 31 March 2020 was £177m. This policy has continued during 2020-21.

13. The benefits of internal/short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. This will help inform decisions on whether the council borrows additional sums at long-term fixed rates in 2021-22 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

14. During the first half of 2020-21 the council borrowed £7m from the Mayor of London's Energy Efficiency Fund (MEEF). The MEEF gets funding from the European Regional Development Fund and other partner banks to fund developments within London councils and other

public sector bodies that will result in reduction in carbon emissions. The rates are therefore more favourable than comparable PWLB rates.

15. The council has an ambitious capital programme for both General Fund and Housing Revenue Account capital expenditure, as set out in the approved Capital Programme Refresh 2020-2030. Projects for capital expenditure and financing, as well as long term cashflow forecasts, indicate that the council may require additional borrowing of £1bn by the end of 2025.

Public Works Loan Board

16. All historical long term debt for the council has been drawn from the PWLB. However the government increased PWLB rates by 1% in October 2019 making it now a relatively expensive option. A HM Treasury consultation on lowering PWLB rates concluded in July 2020 but the government has yet to publish its response. In the meantime, the Authority will consider long-term loans from other sources. Any borrowing decision will be made in consideration of capital and cashflow forecasts, market conditions, interest rate expectations and with respect to associated risks. The council will also utilise the advice of external treasury advisor Arlingclose.

Proposed Investment Strategy

17. The council's investment objectives are to preserve principal, provide liquidity and secure a return on investments consistent with the prior objectives of security and liquidity. This is in line with investment guidance produced by the Ministry of Housing, Communities and Local Government (MHCLG).

18. The annual investment management strategy 2021-22 is attached at Appendix C. The strategy will allow investment access to highly rated sovereigns, banks and other corporates, quasi-sovereigns, covered bonds whilst limiting excessive exposure to market volatility and maintaining the overarching objective of ensuring appropriate security and liquidity. External fund managers will be utilised to implement the strategy when appropriate.

19. In considering the investment strategy for 2021-22 the council has taken advice from the external treasury advisor Arlingclose, in addition to ongoing engagement with the council's external fund managers, to ensure that any investment limits and restrictions remain appropriate to meet the investment objectives.

20. The investment strategy for the council for 2021-22 is proposed to remain unchanged as it is considered overall to be well structured to limit any undue risks to the security of assets and preservation of liquidity whilst also allowing the council and delegated managers to access suitable investment opportunities.

21. The COVID-19 pandemic has increased the risk that the Bank of

England will set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options.

Minimum Revenue Provision

22. Each year, the General Fund sets aside sums known as the minimum revenue provision to reduce its borrowing liabilities. The HRA may also set aside sums to reduce its own borrowing liabilities. The policy for MRP is set out in Appendix D and complies with the latest guidance issued by the MHCLG.

23. Government guidance on the MRP requires that the general fund set aside prudent sums to reduce debt and long term liabilities (such as PFI schemes) arising from capital spend and that the council produces a statement on its MRP policy. MRP costs fall on revenue budgets and runs on for many years into the future, usually over the period to which the capital item provides an economic benefit or the duration of the revenue grant supporting the expenditure.

24. Under the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, a local authority is required to charge a minimum revenue provision annually to its revenue account in respect of capital financing obligations that arise in that year or arose in any prior year. Capital financing obligations represent debt or long term liabilities taken to fund capital expenditure.

25. A council may not change the total MRP it is liable for but may prudently modify the timing of payments to improve affordability and take account of individual spend and financing characteristics.

Prudential Indicators

26. Local authority borrowing, investment and capital finance activity is supported by the Prudential Code for Capital Finance and the Treasury Management in the Public Services Code of Practice and Guidance published by the Chartered institute of Public Finance and Accountancy, backed by the Local Government Act 2003. The codes introduced a series of indicators and limits, which the council assembly should agree annually.

27. The indicators needing approval relate to 2021-22 to 2023-24 and are set out at Appendix E. The indicators are of a technical nature and include a self imposed authorised limit on debt which the council assembly must determine each year. Approval will ensure that the council meets its obligations under the 2003 Act and that the strategic director of finance and governance can carry out their financial responsibilities in this area.

Community Impact Statement

28. This report and the accompanying annual governance statement are not

considered to have a direct impact on local people and communities. However, good governance arrangements are important to the delivery of local services and to the achievement of outcomes.

Resource implications

29. There are no direct resource implications in this report.

Consultation

30. There has been no consultation on this report.

SUPPLEMENTARY ADVICE FROM OTHER OFFICERS

31. None required.

BACKGROUND DOCUMENTS

Background Papers	Held at	Contact
None		

APPENDICES

No.	Title
Appendix A	Capital Strategy 2021-22 to 2030-31
Appendix B	Treasury Management Strategy 2021-22
Appendix C	Annual Investment Management Strategy 2021-22
Appendix D	Annual Minimum Revenue Provision Statement
Appendix E	Prudential Indicators

AUDIT TRAIL

Lead Officer	Duncan Whitfield, Strategic Director of Finance and Governance	
Report Author	Rob Woollatt, Interim Departmental Finance Manager	
Version	Final	
Dated	10 November 2020	
Key Decision?	No	
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / CABINET MEMBER		
Officer Title	**Comments Sought**	**Comment included**
Director of Law and Democracy	No	N/A
Strategic Director of Finance and Governance	No	N/A
Cabinet Member	**No**	**N/A**
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