APPENDIX B

TREASURY MANAGEMENT STRATEGY STATEMENT 2021-22

Introduction

1. 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 a crucial part of the financial management and governance arrangements of the council.

2. Treasury risk management is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code) which requires the council to approve a treasury management strategy before the start of each financial year. This report fulfils the council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

3. Investments held for service purposes or for commercial profit are considered in the Capital Strategy.

4. 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.

5. The impact on the UK from coronavirus, lockdown measures, the rollout of vaccines, as well as the new trading arrangements with the European Union (EU) will remain major influences on the council's treasury management strategy for 2021-22.

6. Monthly GDP estimates have shown that the economic recovery in the summer has slowed and remains well below its pre-pandemic peak. Looking ahead, the BoE's November MPR forecasts economic growth will rise in 2021 with GDP reaching 11% in Q4 2021.

Net Borrowing Position

7. As at 31 December 2020 the council held £788m of borrowing and £147m of investments.

8. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, known as internal borrowing.

9. The Council has an increasing CFR due to its ambitious capital programme. Based on current forecasts there is an estimated need to borrow up to £1bn by 31 March 2025.

Borrowing strategy and debt management activity and position

10. The council's debt management strategy since 2011-12 has been to pursue a policy of internal borrowing, which is the use of existing reserves and balances to temporarily fund capital expenditure rather than the use of external borrowing.

11. 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. Borrowing in advance of need from a cashflow perspective creates a 'cost of carry' which is the difference between the short term investment income earned through holding cash balances compared against longer term external debt financing costs

12. During the period from 2011-12 to 2017-18 the rate of return on short term investments was consistently much lower compared to longer term borrowing. The savings for the council from deferring external borrowing in this way equate to circa £20m

13. 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.

14. During the financial year to 31 March 2020, the extent of internal borrowing and the need to refinance scheduled debt repayments, together with potential for interest rate rises, indicated the need for long-term borrowing. The council borrowed £50m from the Public Works Loans Board (PWLB), as part of HM Treasury, with maturity terms of 49 years at an interest rate of 1.5%.

15. In the current financial year the council has borrowed a further £7m of long term debt from the Mayor of London's Energy Efficiency Fund (MEEF).

16. Drawing of long term borrowing has been supplemented by a continuation of 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.

17. This approach to short term borrowing has continued during 2020-21 with the balance of short term borrowing from local authorities at £154m as at 31 December 2020. The weighted average rate of interest on existing short term borrowing is 0.6%, significantly less than long term rates of borrowing.

18. Officers regularly monitor current and forecast interest rates to determine the appropriateness of the internal and short term borrowing approach, so that the reduction in current borrowing costs from use of internal balances is not offset by higher borrowing costs in the future.

19. The Covid-19 pandemic has had a significant impact on capital programme delivery in 2020-21, deferring spend to future periods. The re-profiling of capital expenditure into future years has allowed the council to defer external borrowing, reducing the interest cost associated with debt financing.

20. With the exception £7m of long term debt from the Mayor of London's Energy Efficiency Fund (MEEF), all historical long term debt for the council has been drawn from the PWLB. The PWLB remains the council preferred lender. However future borrowing could come from a variety of different sources. The council could borrow through other financial institutions and banks, or directly from other local authorities.

21. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield. The council intends to avoid this activity in order to retain its access to PWLB loans.

22. All 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 its external treasury advisor Arlingclose.

23. The council's outstanding debt portfolio, used to fund historical capital expenditure, stood at £632m as at 31 March 2020 with £435m attributable to the HRA and £198m to the general fund.

24. Long term outstanding debt was borrowed from the PWLB, part of HM Treasury, at fixed rates of interest. At the end of 2019-20, £50m was borrowed from the PWLB and during 2020-21 a further £7m of long term debt was drawn from the Mayor of London's Energy Efficiency Fund (MEEF). £5m of long term debt principal will mature in 2020-21 and be repaid to PWLB.

25. The weighted average rate of interest for the council's debt portfolio is 4.3% as at 31 December 2020 a reduction from 4.4% as at 31 March 2020.

Investment Position and Activity

26. The council holds sizable investment balances, representing income received in advance of expenditure plus balances and reserves held. Investments as at 31 December 2020 were £151m (£148m at 31 December 2019).

27. Council resources that are not immediately required for current expenditure are invested in money market instruments in accordance with the MHCLG Guidance on Local Authority Investments and the approved

investment strategy. The MHCLG guidance gives priority to security and liquidity and the council's aim is to achieve a yield commensurate with these principles.

28. Council investments are managed both in-house and delegated to two fund managers: Alliance Bernstein and Aberdeen Standard (formerly Aberdeen Asset Management). The focus for in-house investment is to meet variable near term cash liquidity requirements, principally using money market funds and other highly secure, liquid financial instruments

29. Any surplus cash resources not required in the short term to fund council activities is placed with the council's two external fund managers. The fund managers invest for a longer term in UK government gilts, supranational bank bonds, certificates of deposits issued by major banks/ building societies and other financial instruments.

30. The use of fund managers has the advantage of diversification of investment risk, coupled with the services of professional fund managers, which over the longer-term, provides enhanced returns within the council's risk appetite. Although investments can be redeemed from the fund managers at short notice, the intention is to hold them for the medium term. Their performance and suitability in meeting the council's investment objectives are regularly monitored.

31. The distribution of council investments across counterparties by rating and maturity as at 31 December 2020 is set out in the table below:

	A		**AA**		**AAA**		**Total**
Investment Maturity	**£m**	**%**	**£m**	**%**	**£m**	**%**	**£m**
Up to 1 Year	44.3	40%	21.3	20%	12.1	11%	77.7
1 - 2 Years	3.4	3%	2.7	3%	10.4	10%	16.5
2 - 5 Years	0.6	1%	0.6	1%	11.6	11%	12.8
Total	**48.3**	**44%**	**24.6**	**24%**	**34.1**	**32%**	**107**

32. The annualised rate of return for council treasury management assets for the first nine months of the financial year was 0.69%. To analyse the treasury management portfolio, the council measures the return against a composite investment benchmark of three month LIBID and one to three year gilt index. For the equivalent period the benchmark index annualised return was 0.57% indicating an outperformance of 0.12%.

33. The rate of investment return generated by the treasury management portfolio is a consequence of the council's prudent, low risk approach to treasury management investing. This is in line with the requirements of the statutory guidance for local government treasury investment issued by MHCLG.

34. The priorities for treasury management investment are, in order of priority, security, liquidity and yield. The objective therefore is to ensure that funds are available to meet council liabilities as they fall due.

35. The COVID-19 pandemic has increased the risk that the Bank of England will set its Bank Rate at or below zero, which would likely feed through to negative interest rates on all low risk, short-term investment options. Since investments cannot pay negative income, negative rates will be applied by reducing the value of investments. The Authority's treasury management adviser Arlingclose is forecasting that Bank of England Bank Rate will however remain at 0.1% until at least the end of 2023. The risks to this forecast are judged to be to the downside as the BoE and UK government continue to react to the coronavirus pandemic and the Brexit transition period ends.

36. It is important that the treasury management strategy is suitably flexible such that the council can take advantage of market opportunities and maintain appropriate asset diversification within the portfolio to best support the council's revenue budget, whilst retaining the overriding objectives of security and liquidity.

37. The 2020-21 investment strategy, agreed by Council Assembly in February 2020 allowed for enhanced flexibility in the implementation of the investment strategy for the council such that there is no requirement to change it further at this time.