Renfrewshire Council

To: Finance Resources and Customer Services Policy Board

On: 11 November 2020

Report by: Director of Finance and Resources

Heading: Treasury Management Mid-Year Review 2020-2021

1. Summary

1.1 This mid-year report has been prepared in compliance with the Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management in the Public Services Code of Practice.The report covers the following:

- an economic update for the first half of the 2020-2021 financial year;
- a review of the Treasury Management Strategy Statement 2020-2021, incorporating the annual investment strategy;
- a review of the Council's investment portfolio for 2020-2021;
- a review of the Council's borrowing strategy for 2020-2021; and
- a review of compliance with treasury management indicators for 2020-2021.

2. Recommendations

2.1 It is recommended that Members note the treasury management activity for the period 1 April 2020 to 9 October 2020.

3. Economic update

3.1 The following paragraphs outline a review of the economy over the first half of 2020-2021. Over this period the UK economy suffered a significant downturn related to the Coronavirus pandemic, with a 23% fall in GDP. The Bank of England forecast that recovery is unlikely to be "V" shaped, with significant downside risks to the pace of recovery linked to the potential of a second wave of the pandemic; and also ongoing risks around Brexit.

3.2 The wind down of the initial furlough scheme through to the end of October is another development that could cause the Bank to review the need for more support for the economy later in the year. The Chancellor has announced a second six-month package from 1st November of government support for jobs whereby it will pay up to 22% of the costs of retaining an employee working a minimum of one third of their normal hours. There was further help for the self-employed, freelancers and the hospitality industry. However, this is a much less generous scheme than the furlough package and will inevitably mean there will be further job losses from the 11% of the workforce still on furlough in mid-September. The last three months of 2020 are now likely to show no growth as consumers will probably remain cautious in spending and uncertainty over the outcome of the UK/EU trade negotiations concluding at the end of the year will also be a headwind. There will be some painful longer-term adjustments as e.g. office space and travel by planes, trains and buses may not recover to their previous level of use for several years, or possibly ever. There is also likely to be a reversal of globalisation as this crisis has shown up how vulnerable long-distance supply chains are. On the other hand, digital services is one area that has already seen huge growth.

3.3 The Bank of England's Monetary Policy Committee (MPC) kept the Bank Rate unchanged on 6th August. It also kept the level of quantitative easing at £745bn.

3.4 The Bank also downplayed any idea of using negative interest rates, at least in the next six months or so. It suggested that while negative rates can work in some circumstances, it would be "less effective as a tool to stimulate the economy" at this time when banks are worried about future loan losses. It also has "other instruments available", including QE and the use of forward guidance.

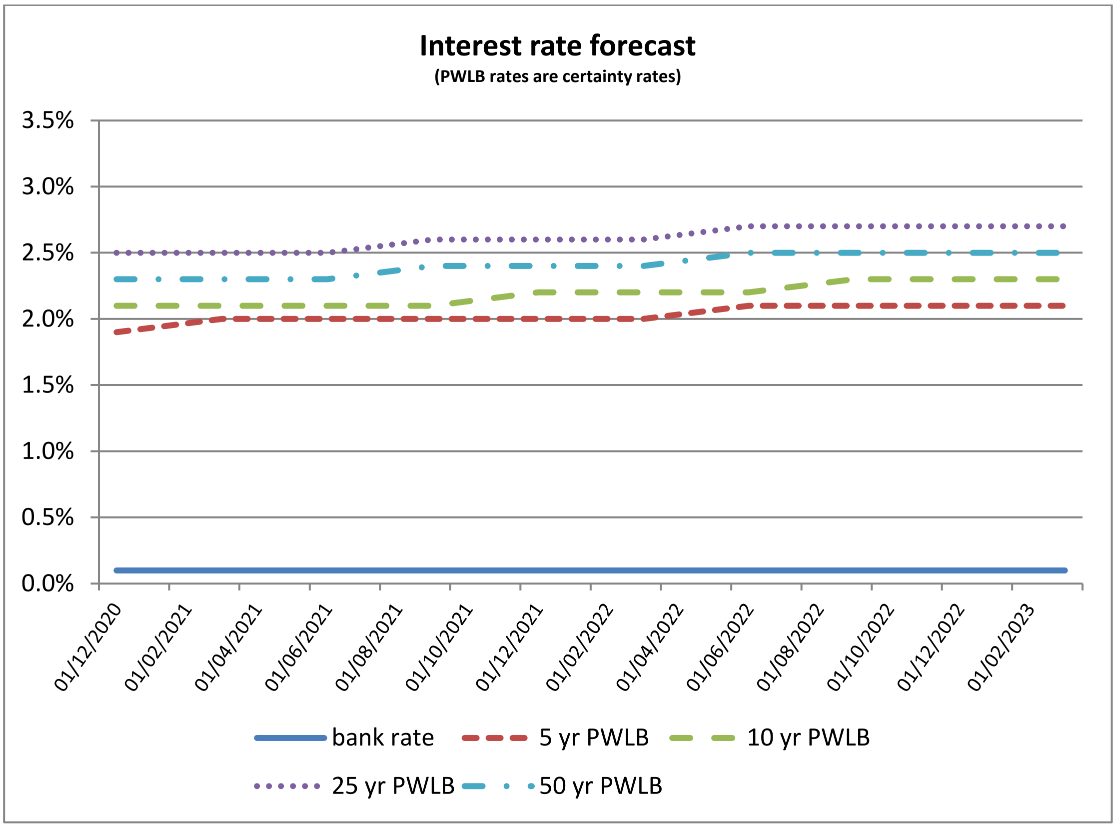
3.5 **Credit background:** Although the credit rating agencies changed their outlook on many UK banks from stable to negative outlook during the quarter ended 30th June 2020 due to upcoming risks to banks' earnings and asset quality during the economic downturn caused by the pandemic, the majority of ratings were affirmed due to the continuing strong credit profiles of UK banks. However, during Q1 and Q2 2020, banks made provisions for *expected* credit losses and the rating changes reflected these provisions. As we move into the next quarters, more information will emerge on *actual* levels of credit losses. This has the potential to cause rating agencies to revisit their initial rating adjustments earlier in the current year.

These adjustments could be negative or positive, although it should also be borne in mind that UK banks went into this pandemic with strong balance sheets.

4 Interest rate forecasts

4.1 The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to 0.25%, and then to 0.10%, it left Bank Rate unchanged at its meeting on 6th August (and the subsequent September meeting). As shown in the forecast graph below, no increase in Bank Rate is expected within the forecast horizon ending on 31st March 2023 as economic recovery is expected to be only gradual and, therefore, prolonged.

4.2 The Council's Treasury Advisers are Link Treasury Services Ltd and their central case is for Bank Rate to remain unchanged for the rest of this year and for all of 2021. The overall balance of risks to economic growth in the UK is probably relatively even but is subject to major uncertainty due to the virus.



4.3 There is relatively little UK domestic risk of increases or decreases in Bank Rate and significant changes in shorter term PWLB rates. The Bank of England has effectively ruled out the use of negative interest rates in the near term and increases in Bank Rate are likely to be some years away given the underlying economic expectations.

However, it is always possible that safe haven flows, due to unexpected domestic developments and those in other major economies, could impact gilt yields, (and so PWLB rates), in the UK.

4.4 From the Council's borrowing perspective, 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 9th October 2019, adding an additional 1% margin over gilts to all PWLB period rates. That increase was then partially reversed for some forms of borrowing on 11th March 2020, but not for mainstream General Fund capital schemes. It also announced that there would be a consultation with local authorities on possibly further amending these margins; this was to end on 4th June, but that date was subsequently put back to 31st July.

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

- **PWLB Standard Rate** is gilt plus 200 basis points
- **PWLB Certainty Rate** is gilt plus 180 basis points
- **PWLB HRA Standard Rate** is gilt plus 100 basis points
- **PWLB HRA Certainty Rate** is gilt plus 80bps
- **Local Infrastructure Rate** is gilt plus 60bps

4.6 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.

4.7 As the interest forecast graph for PWLB above shows, there is likely to be little upward movement in PWLB rates over the next two years as it will take economies, including the UK, a prolonged period to recover all the momentum they have lost 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

5 Review of the Treasury Management Strategy Statement 2020-2021 (incorporating annual investment strategy) as at 9 October 2020

5.1 The Treasury Management Strategy Statement for 2020-2021 was approved by Council on 9 March 2020. The Council's annual investment strategy, which is incorporated in the Treasury Management Strategy Statement, sets out the Council's investment priorities as follows:

- the security of capital and
- the liquidity of its investments.

5.2 The Council also aims to achieve the optimum returns on its investments commensurate with the proper levels of security and liquidity. Investments and borrowing during the first six months of the year have been in line with the strategy and there have been no changes to the policies set out in the Treasury Management Strategy Statement 2020-2021. The details in this report update the position in light of the updated economic position and budgetary changes already approved.

6 Review of borrowing and investments over the period 1 April 2020 to 9 October 2020

6.1 The Council's net borrowing position as at 9 October 2020 is shown in Appendix 1.

6.2 During the period 1 April 2020 to 9 October 2020 the Council's total external borrowings have decreased by £1.22 million to £220.05 million, due to the scheduled repayments of PWLB debt.

6.3 During this period, temporary investments have increased from £115.80 million to £183.18 million. The increase in investments is after financing the £1.22 million of debt repayment and reflects:

- the re-profiling of elements of the current capital programme due to the pause in construction activity during and following the coronavirus lockdown period;
- the "front-loading" (that is, more income being received in the early part of the year) of revenue support grant income.

6.4 The Director of Finance and Resources confirms that, during the period 1 April 2020 to 9 October 2020, the approved limits set out within the annual investment strategy sections of the Treasury Management Strategy Statement 2020-2021 were complied with. The Council only invested with institutions listed in the Council's approved lending list. Similarly, only permitted investment vehicles were used, mainly call accounts, fixed term deposits and money market funds.

6.5 In accordance with CIPFA's Treasury Management in the Public Services Code of Practice, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite.

6.6 The table below shows the average interest rate achieved by the Council on its temporary investments during the period 1 April 2020 to 9 October 2020. The table also shows for comparison the benchmark comparator, which is the average 7-day LIBID rate (uncompounded). (The 7-day LIBID rate is the London Interbank Bid Rate, being the rate at which a bank is willing to borrow from other banks, for borrowings of a maturity of seven days.)

The LIBID benchmark is closely related to the LIBOR benchmark; both of which are being phased out from 2021 following evidence in recent years of manipulation of these rates. A comparable benchmark in terms of evaluating short term investment returns is SONIA – the Sterling Overnight Index Average – which is reflects bank and building societies actual overnight funding rates in Sterling and is administered by the Bank of England. In future reports the SONIA benchmark will be used; however both benchmarks are detailed in the table below.

Interest rates achieved on investments	Average value of investments	Actual rate of return	Benchmark return
Internally managed investments	£140.29m	0.567%	-0.057% (LIBID) 0.061% (SONIA)

6.7 **Debt rescheduling**

Debt rescheduling opportunities have been limited in the current economic climate and it is not anticipated that this is likely to change over the short to medium term. However, in conjunction with the Council's treasury advisors, the service will remain alert to any opportunities which may arise.

7 Review of compliance with treasury management indicators for 2020-2021

7.1 During the period 1 April 2020 to 9 October 2021 the Council complied with the approved treasury management indicators as set out in the Treasury Management Strategy Statement 2020-2021. These indicators relate to:

- interest rate exposures: the upper limit on the proportion of investments which are exposed to fixed interest rates and the upper limit on the proportion of investments which are exposed to variable interest rates;
- the maturity structure of borrowing: the lower and upper limits on the proportion of investments which fall into each maturity band.

7.2 In addition to the treasury management indicators referred to at 7.1, there are two *prudential* indicators (as set out in the Prudential Framework for Capital Finance and Treasury Management Strategy Statement 2020-2021, approved by Council on 9 March 2020) which are of particular relevance to the Council's treasury management strategy:

- operational boundary for external debt;
- authorised limit for external debt.

7.3 During the period 1 April 2020 to 9 October 2020 the Council operated within the operational boundary for external debt, and within the authorised limit for external debt. These indicators, along with the Council's actual external debt, are shown in Appendix 2.

Implications of the Report

1. **Financial** – As described in the report. The Treasury Management Strategy Statement and treasury management indicators assist in providing assurance that the Council's treasury management activities and longer term plans are affordable, prudent and sustainable.

2. **HR & Organisational Development** – none

3. **Community Planning** – none

4. **Legal** – none

5. **Property/Assets** – none

6. **Information Technology** – none

7. **Equality & Human Rights** – Recommendations contained within this report have been assessed in relation to their impact on equalities and human rights. No negative impacts on equality groups or potential for infringement of individuals' human rights have been identified arising from the recommendations contained in the report because it is for noting only. If required following implementation, the actual impact of the recommendations and the mitigating actions will be reviewed and monitored, and the results of the assessment will be published on the Council's website.

8. **Health & Safety** – none

9. **Procurement** – none

10. **Risk** – The Treasury Management Strategy Statement and treasury management indicators provide a framework to take forward the Council's treasury activities in the context of the effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks. This mid-year review report demonstrates that the treasury management activities carried out during the period 1 April 2020 to 9 October 2020 have been consistent with the Treasury Management Strategy Statement 2020-2021 and have complied with the treasury management indicators set out in the Strategy Statement

11. **Privacy Impact** – none

12. **COSLA Policy position** – none

13. **Climate risk** - none

List of Background Papers
None

Author: Alastair MacArthur – 0141 618 7363

Appendix 1

Borrowing and investment position as at 9 October 2020

	balance at 01-Apr-20	new borrowing in 2020-2021	principal repayments	debt restructuring	net cash movements	balance at 09-Oct-20
Long term borrowings						
PWLB - fixed	168,357,429.17	-	(1,223,838.63)	-	-	167,133,590.54
PWLB - variable	-	-	-	-	-	-
Market loans	52,916,000.00	-	-	-	-	52,916,000.00
	221,273,429.17	-	(1,223,838.63)	-	-	220,049,590.54
Short term borrowings						
Temporary loans	-	-	-	-	-	-
	-	-	-	-	-	-
Total external borrowings	221,273,429.17	-	(1,223,838.63)	-	-	220,049,590.54
Investments						
Fixed term deposits	93,000,000.00	-	-	-	57,830,000.00	150,830,000.00
Notice accounts	-	-	-	-	-	-
Call accounts	600,000.00	-	-	-	-	600,000.00
Money market funds	22,200,000.00	-	-	-	9,550,000.00	31,750,000.00
Total investments	115,800,000.00	-	-	-	67,380,000.00	183,180,000.00
Net borrowing	105,473,429.17	-	(1,223,838.63)	-	67,380,000.00	36,869,590.54

Appendix 2

Treasury Management Indicators as at 9 October 2020

	2020-2021 estimate	2020-2021 probable	2021-2022 estimate	2022-2023 estimate
Authorised limit for external debt	£449m	£409m	£561m	£601m
Operational boundary for external debt	£431m	£393m	£537m	£575m
Actual external debt at 9 October 2020	n/a	£291.49m	n/a	n/a
Upper limit for fixed interest rate exposure (borrowing) expressed as percentage of total net outstanding principal	100%	n/a	100%	100%
Upper limit for variable interest rate exposure (borrowing) expressed as percentage of total net outstanding principal	25%	n/a	25%	25%

	new borrowing in 2020-2021		total of all borrowing	
	value	maturity structure	upper limit	actual at 9 Oct 2020
Maturity structure of fixed rate borrowing				
under 12 months	0	0%	15%	0.01%
12 months and within 24 months	0	0%	15%	0.38%
24 months and within 5 years	0	0%	45%	3.50%
5 years and within 10 years	0	0%	50%	2.28%
10 years and above	0	0%	100%	93.83%