Annual Treasury Management Review
2020/21

North Hertfordshire District Council
April 2021

Annual Treasury Management Review 2020/21

1. Introduction

This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2020/21. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

During 2020/21 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 06/02/2020)
- a mid-year treasury update report (Council 21/01/2021)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

In addition, Cabinet and the Finance, Audit and Risk (FAR) Committee have received quarterly treasury management update reports.

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Finance, Audit and Risk Committee before they were reported to the full Council.

2. The Council's Capital Expenditure and Financing

The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

	19/20 Actual £'000	20/21 Original Budget £'000	20/21 Actual £'000
Capital expenditure	**1,473**	**9,357**	**1,883**
Financed in year	1,076	3,229	1,466
Unfinanced capital expenditure	**397**	**6,128**	**417**

The Unfinanced expenditure is the use of set aside receipts.

3. The Council's Overall Borrowing Need

The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2020/21 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies, (such as the Government, through the Public Works Loan Board [PWLB], or the money markets), or utilising temporary cash resources within the Council.

	31 March 2020 Actual £'000	2020/21 Original Budget £'000	31March 2021 Actual £'000
Opening Balance	-5,996	-2,411*	-5,599
Add unfinanced capital expenditure (as above)	397	6,128	417
Closing Balance	-5,599	3,717	-5,182

*The 20/21 Original Budget was prepared before the final outturn figures for 19/20 were complete. The figure is considerably less due to slippage on the Capital Programme in 19/20 resulting in less expenditure to finance.

The negative closing balances mean that the Council does not have a need to borrow.

Gross borrowing and the CFR - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2020/21) plus the estimates of any additional capital financing requirement for the current (2021/22) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allows the Council some flexibility to borrow to meet its planned capital needs. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator, as all borrowing is historic.

	31 March 2020 Actual £'000	31 March 2021 Original Budget £'000	31 March 2021 Actual £'000
Gross borrowing position	423	405	405
CFR	-5,599	3,717	-5,182

The authorised limit - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2020/21 the Council has maintained gross borrowing within its authorised limit.

The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limit not being breached.

Actual financing costs as a proportion of net revenue stream - this indicator identifies the trend in the cost of capital, (borrowing and other long term obligation costs net of investment income), against the net revenue stream.

	2020/21
Authorised limit	£10.0m
Maximum gross borrowing position during the year	£0.423m
Operational boundary	£4.0m
Average gross borrowing position	£0.416m
Financing costs as a proportion of net revenue stream	-0.74%

4. Treasury Position as at 31st March 2021

At the beginning and the end of 2020/21 the Council's treasury position was as follows:

DEBT PORTFOLIO	31.3.20 Principal £'000	Average Rate/ Return	Average Life yrs	31.3.21 Principal	Average Rate/ Return
Fixed rate funding:					
-PWLB	423	9.82%		405	9.96%
-Market	0			0	
Variable rate funding:					
-PWLB	0			0	
-Market	0			0	
Total debt	**423**	**9.82%**		**405**	**9.96%**
CFR	**-5,599**			**-5,182**	
Over / (under) borrowing	**6,022**			**5,587**	
Total investments	**29,500**	**1.18%**		**42,500**	**0.41%**

The change in average rate reflects the repayment of debt over the year and the balance of loans at different fixed interest rates. The Council does not have any variable rate borrowing.

The maturity structure of the debt portfolio was as follows

	31.3.20 Actual £'000	31.3.21 Actual £'000
Under 12 months	18	18
12 months and within 24 months	18	19
24 months and within 5 years	61	63
5 years and within 10 years	69	55
10 years and above	257	250

The table below summarises where investments were held at 31 March:

INVESTMENT PORTFOLIO	31.3.20 Actual £000	31.3.20 Actual %	31.3.21 Actual £000	31.3.21 Actual %
Treasury investments				
Banks	2,000	7	0	
Building Societies	9,500	32	10,500	25
Local authorities	16,000	54	20,000	47
Debt Management Account Deposit Facility (H M Treasury)	2,000	7	12,000	28
TOTAL TREASURY INVESTMENTS	29,500	100	42,500	100
Council's Current Account	8,072		4,056	

The maturity structure of the investment portfolio was as follows:

	31 March 2020 Actual £000	31 March 2021 Actual £000
Investments Longer than 1 Year	1,000	0
Investments Up to1 Year	28,500	42,500
Total	29,500	42,500

The increase in cash balances as at the end of 2020/21 (compared with 2019/20) is mainly due to the balances that the Council is holding in relation to Business Grants and s31 Business Rate relief funding.

5. The Strategy for 2020/21

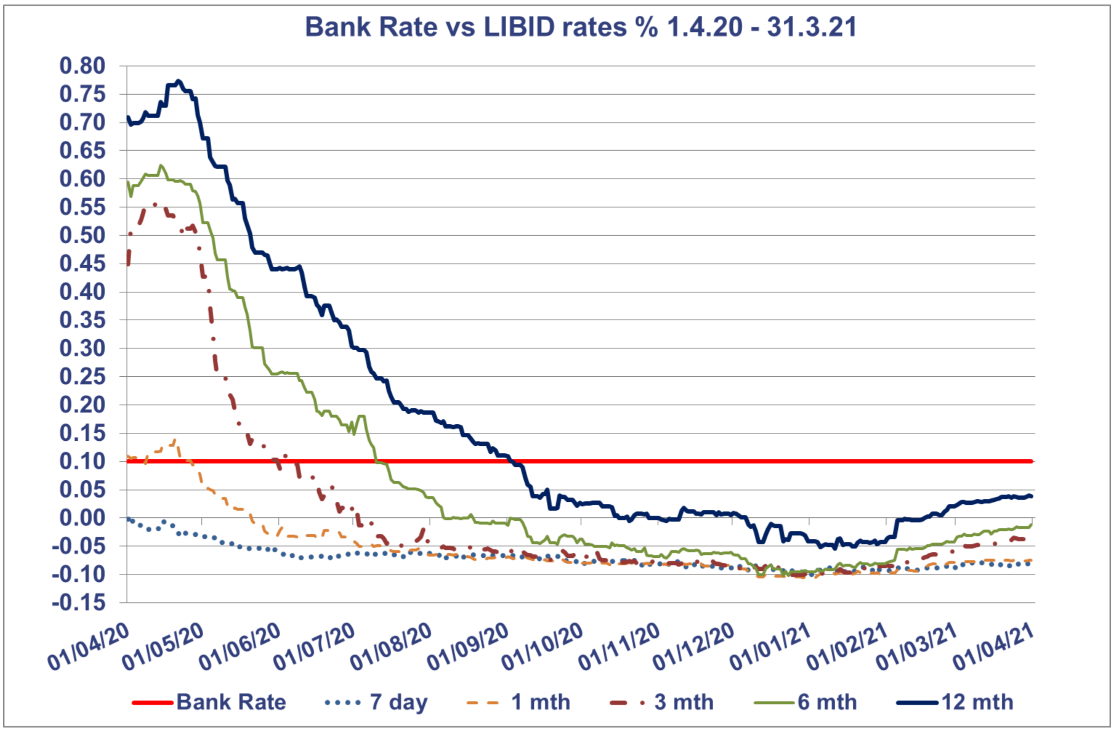
The strategy in 2020/21 was to continue lending to UK banks, building societies, money market funds, Local Authorities and property funds and allow investments with non-UK banks with a credit rating greater than AA- with a AAA Country rating. Only UK banks with a credit rating, for longer term deals, greater than "BBB" and F3 or above for short term credit ratings were on the Council's lending list. (These are Fitch definitions of ratings). Not all building societies are credit rated but this did not preclude them from the lending list as lending to a building society was dependant on their asset size. Where a society did have a rating, this was considered at the time of the deal taking into account the amount of investment and the length of the deal.

Change in strategy during the year – the strategy adopted in the original Treasury Management Strategy Report for 2020/21 was approved by the Council on 06/02/2020. The £5 million limit on the Council's current account was exceeded during the 1st quarter to ensure the Council had sufficient funds to pay Business Support Grants and to ensure that cash was available to respond more generally to the implications of Covid-19. The Chief Executive made an urgent decision on the 9th April to temporarily remove the limit on amounts held in the Council's current account to facilitate the grant payments. The current account limit of £5m has since been reinstated.

5.1 Investment strategy and control of interest rate risk

Investment returns which had been low during 2019/20, plunged during 2020/21 to near zero or even into negative territory. The expectation for interest rates within the treasury management strategy for 2020/21 was that Bank Rate would continue at the start of the year at 0.75 % before rising to end 2022/23 at 1.25%. This forecast was invalidated by the Covid-19 pandemic bursting onto the scene in March 2020 which caused the Monetary Policy Committee to cut Bank Rate in March, first to 0.25% and then to 0.10%, in order to counter the hugely negative impact of the national lockdown on large swathes of the economy. The Bank of England and the Government also introduced new programmes of supplying the banking system and the economy with massive amounts of cheap credit so that banks could help cash-starved businesses to survive the lockdown. The Government also supplied huge amounts of finance to local authorities to pass on to businesses. This meant that for most of the year there was much more liquidity in financial markets than there was demand to borrow, with the consequent effect that investment earnings rates plummeted.

While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the financial crisis. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.



6. Borrowing Outturn

Borrowing
No new borrowing was undertaken during the year.

Borrowing in advance of need

The Council has not borrowed more than, or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed.

Rescheduling
No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

Repayments
£18K of PWLB loans were repaid during the year, as they became due.

7. Investment Outturn

Investment Policy – the Council's investment policy is governed by MHCLG investment guidance, which has been implemented in the annual investment strategy approved by the Council on 06/02/20. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the Fitch credit rating agency for banks and asset size for building societies.

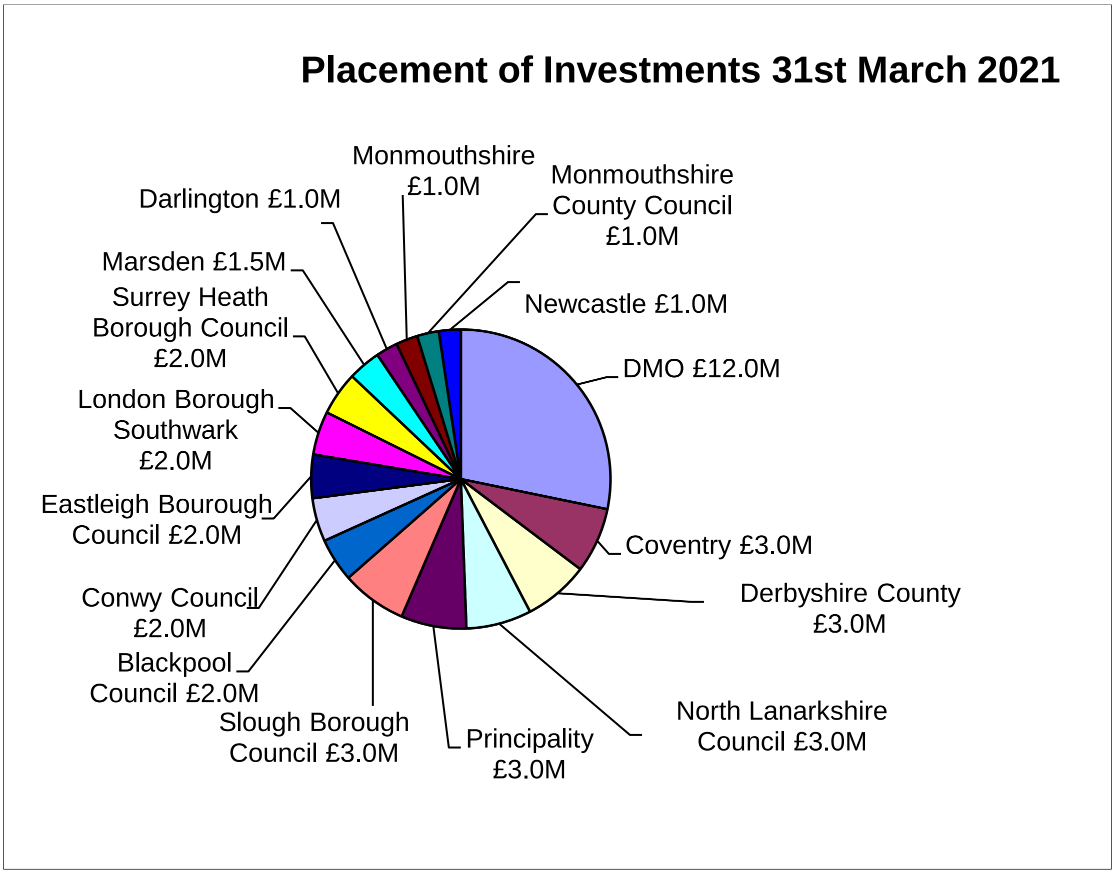
The investment activity during the year mostly conformed to the approved strategy although the limit on investments placed with Building Societies was exceeded by £2.0 million for 19 days in October and was reported to Members in the 3rd quarter monitoring report.

Investments placed by Cash Managers – the Council used an external cash manager to invest some of its longer term cash balances, where the rate achieved (after fees) was better than could be obtained by the Council directly. At the start of the year, Tradition had £8.5m of outstanding investments. This had reduced to £4.5m in June and then remained at that level throughout the rest of the year. The performance of the Tradition against the benchmark return was:

Cash Manager	Investments Placed	Interest	Return	Benchmark*
Tradition	£8.5M - £4.5M	£0.059M	1.20%	0.55%

* Ave 7 days notice Rate 0.55%
This compares with an original budget of £0.985M.

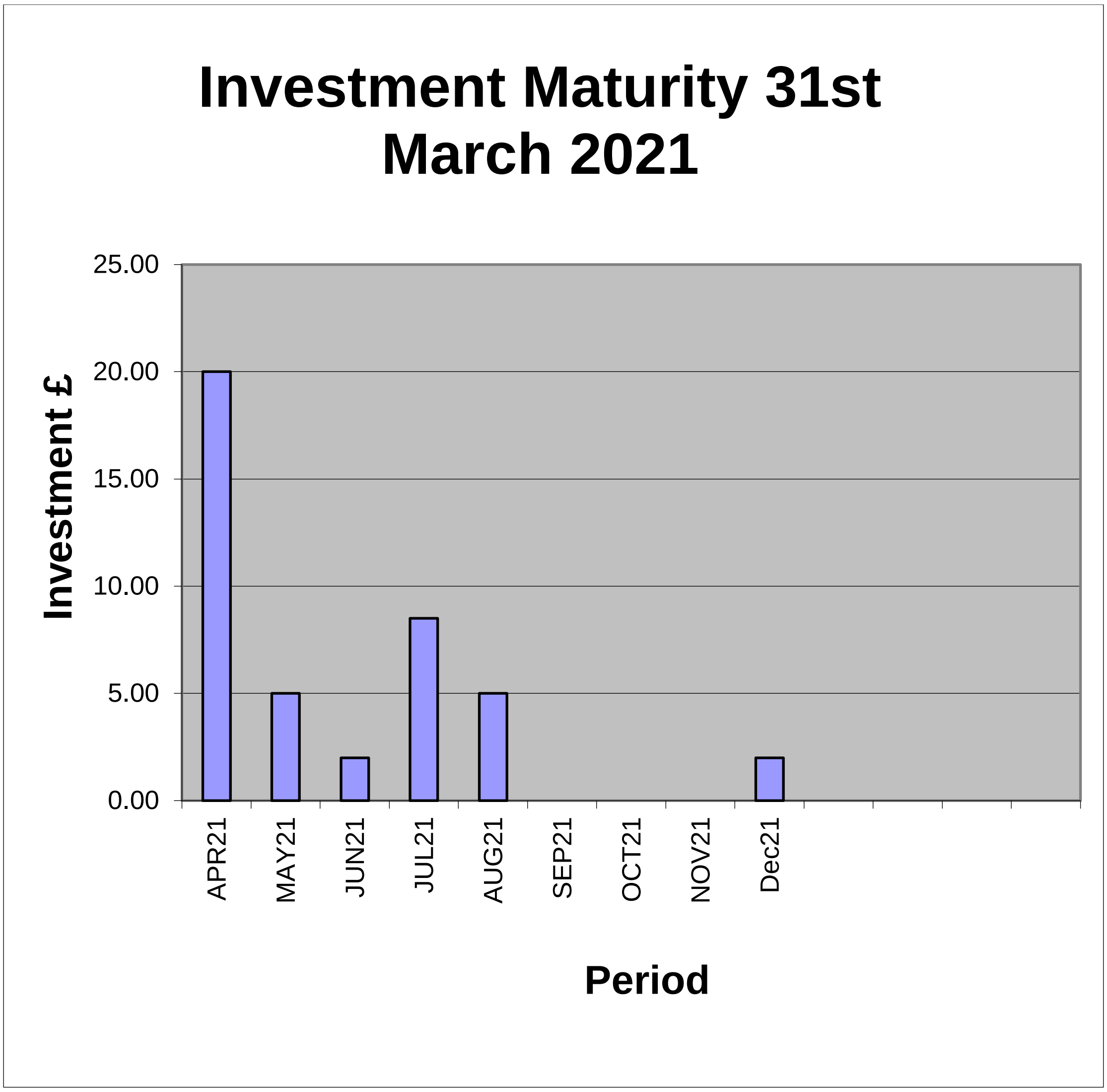
The pie chart below shows the spread of investment balances as at 31 March 2021 (excluding money held in our Current Account). This is a snapshot in time that demonstrates the diversification of investments.



The average daily balance of investments was £46.6m with balances varying between £34.5m and £69.0m.

£0.184m of interest was generated from investments during the year. This is slightly less than the estimated interest of £0.185m (as per Quarter 3 forecast). It is significantly below the Original Budget (£0.300m) that was set prior to Covid-19.

The graph below shows the maturity profile of investments at 31st March 2021 (excluding money held in our Current Account which is instant access).



The level of risk of any investment will be affected by the riskiness of the institution where it is invested and the period that it is invested for. Where an institution has a credit rating this can be used to measure its riskiness. This can be combined with the period remaining on the investment to give a historic risk of default percentage measure. The table below shows the Historic Risk of Default for outstanding investments at 31 March. The most risky investment still has a historic risk of default of below 1%. It should also be noted that in general the interest rate received is correlated to the risk, so the interest income received would be less if it took on less risk. All investments have been made in accordance with the Investment Strategy.

Borrower	Interest Rate %	Principal	Days to Maturity from 31/03/20	Historic Risk of Default %	Risk of Default %
DMO	-0.01	4,000,000	1	0.002	0.000
COVENTRY	0.02	3,000,000	6	0.050	0.001
CONWYN COUNTY BOROUGH COUNCIL	0.08	2,000,000	20	0.002	0.001
DMO	0.00	8,000,000	20	0.002	0.000
PRINCIPALITY BUILDING SOCIETY	0.06	2,000,000	20	0.140	0.008
PRINCIPLAITY BUILDING SOCIETY	0.06	1,000,000	30	0.140	0.012
EASTLEIGH BOROUGH COUNCIL	0.05	2,000,000	47	0.002	0.003
MOMMOUTHSHIRE BUILDING SOCIETY	1.50	1,000,000	58	0.140	0.022
SLOUGH BOROUGH COUNCIL	1.00	2,000,000	58	0.002	0.004
SLOUGH BOROUGH COUNCIL	0.10	1,000,000	62	0.002	0.004
MONMOUTHSHIRE COUNTY COUNCIIL	0.25	1,000,000	79	0.002	0.005
DERBYSHIRE COUNTY COUNCIL	0.10	3,000,000	96	0.002	0.006
DARLINGTON BUILDING SOCIETY	0.35	1,000,000	99	0.140	0.038
NORTH LANARKSHIRE COUNCIL	0.05	3,000,000	110	0.002	0.007
MARSDEN BUILDING SOCIETY	0.30	1,500,000	112	0.140	0.043
LONDON BOROUGH OF SOUTHWARK	0.20	2,000,000	127	0.002	0.008
NEWCASTLE BUILDING SOCIETY	0.20	1,000,000	149	0.140	0.057
SURREY HEATH BOROUGH COUNCIL	0.04	2,000,000	153	0.002	0.010
BLACKPOOL COUNCIL	0.32	2,000,000	257	0.002	0.016

Resources – the Council’s cash balances comprise revenue and capital resources and cash flow monies. The Council’s core cash resources comprised as follows:

Balance Sheet Resources (£m)	31 March 20 £’000	31 March 21 £’000
Balances	**9,332**	**8,895**
Earmarked reserves	**9,271**	**20,808**
Provisions	**2,446**	**2,783**
Usable capital receipts	**1,941**	**1,430**
Total	**22,990**	**33,916**