CITY OF YORK COUNCIL

Executive **18 November 2021**

Report of the Chief Finance Officer

Portfolio of the Executive Member for Finance and Performance

Treasury Management Mid-Year Review and Prudential Indicators 2021/22

Summary

1. The Council is required through legislation to provide members with a mid-year update on treasury management activities. This report provides an update on activity for the period 1 April 2021 to 30 September 2021.

Recommendations

2. Members are required, in accordance with the Local Government Act 2003 (revised), to:
    - Note the Treasury Management activities to date in 2021/22
    - Note the Prudential Indicators set out at Annex A and note the compliance with all indicators.

Reason: to ensure the continued performance of the Council's Treasury Management function.

Background

3. The Treasury Management function is responsible for the effective management of the Council's investments, cash flows, banking, and money market transactions. It also considers the effective control of the risks associated with those activities and ensures optimum performance within those risk parameters.

4. This mid-year report has been prepared in compliance with the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management, and covers the following:
    - An economic update for the first part of the 2020/21 financial year;
    - A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
    - The prudential indicators;
    - A review of the Council's investment portfolio;

- A review of the Council's borrowing strategy;
- A review of compliance with the Treasury and Prudential Limits.

Interest Rate Forecast

5. Table 1 is Link Asset Services Interest Rate forecast for both the bank rate and long term Public Works Loans Board borrowing rates (note all figures are percentages):

	Dec 21	Mar 22	Jun 22	Sep 22	Dec 22	Mar 23	Jun 23	Sep 23	Dec 23	Mar 24
Bank Rate	0.10	0.10	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.75
5 Yr PWLB rate	1.40	1.40	1.50	1.50	1.60	1.60	1.60	1.70	1.70	1.70
10 Yr PWLB rate	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10
25 Yr PWLB rate	2.20	2.20	2.30	2.30	2.40	2.40	2.40	2.50	2.50	2.50
50 Yr PWLB rate	2.00	2.00	2.10	2.20	2.20	2.20	2.20	2.30	2.30	2.40

Table 1: Link Asset Services Interest Rate Forecast (%)

6. 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 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings.

7. As shown in the forecast table above, one increase in Bank Rate from 0.10% to 0.25% has now been included in quarter 2 of 2022/23, a second increase to 0.50% in quarter 2 of 23/24 and a third one to 0.75% in quarter 4 of 23/24

8. The Monetary Policy Committee has acknowledged that the "challenge of avoiding a steep rise in unemployment has been replaced by that of ensuring a flow of labour into jobs". They will be closely monitoring any evidence regarding developments in the labour market and particularly unemployment and underlying wage pressures given the potential danger that labour shortages could push up wage growth by more than expected and that, as a result, CPI inflation would stay above the 2% target for longer.

9. There continues to be concern that more recent increases in prices, particularly the increases in gas and electricity prices in October and due again next April, are likely to lead to faster and higher inflation expectations and underlying wage growth, which would in turn increase the risk that price pressures would prove more persistent next year than previously expected.

10. COVID-19 vaccines have boosted confidence in the market. With the household saving rate having been exceptionally high since the first lockdown in March 2020, there is plenty of pent up demand and purchasing power stored up for services in hard hit sectors like restaurants, travel and hotels. The big question is whether mutations of the virus could develop which render current vaccines ineffective, as opposed to how quickly vaccines can be modified to deal with them and enhanced testing programmes be implemented to contain their spread.

Annual Investment Strategy Update

11. Council approved the Treasury Management Strategy Statement for 2021/22 on 25 February 2021. There are no policy changes and the details in this report do not amend the Statement.

12. The Council's Annual Investment Strategy, which is incorporated in the Strategy, outlines the Council's investment priorities as follows:
    - security of capital
    - liquidity
    - yield
    - FTSE4Good index

13. The Council continues to aim to achieve the optimum return (yield) on investments commensurate with the proper levels of security and liquidity and the Councils risk appetite.

Investment Portfolio

14. The average level of cash balances available for investment purposes in the first 6 months of 2021/22 was £40.376m (£20.272m for the same 6-month period in 20/21). The level of cash balances available is largely dependent on the timing of the Council's cash flow as a result of precept payments, receipt of grants, receipt of developers contributions, borrowing for capital purposes, payments to its suppliers of goods and services and spend progress on the Capital Programme. These funds are therefore only available on a temporary basis depending on cash flow movement.

    The average level of cash balances has increased compared to a year ago due to a number of factors. These include the 2021/22 cash transactions between the Council and MHCLG in relation to business rates being significantly different in 2021/22 compared to previous years with repayments to MHCLG over the full financial year reducing by approximately £35m. Government continues to provide Covid related support to businesses through business rate relief. This is paid directly to local authorities and improves the Council's cash flow position because the cash receipt from MHCLG is received before the business would have paid the Council. Significant payments were received of approximately £22m during the first 6 months of the year.

15. With the increase in cash balances over 2021/21 so far the Council has been able to delay taking on long term debt to finance the Councils capital programme, compared to the second half of 2020/21 where new debt had been taken to cover the Councils under borrowed position.

16. Investment return (calculated as the amount of interest earned against the average cash balance for the period) during the first six months of 2021/22 is shown in table 2:

	2020/21 (full year)	**2021/22 (part year to date)**
Average CYC Rate of Return	0.17	0.04
Benchmarks		
Average 7 Day LIBID	-0.07	-0.08
Average 1 Month LIBID	-0.05	-0.07

Table 2: CYCs investment rate of return performance vs. benchmarks

17. The average rate of return achieved to date in 2021/22 has continued to decrease compared to the average seen in 2020/21, due to keeping cash in highly liquid Money Market Funds. Opportunities for longer term investments at higher yields have generally not been available due to the continued low interest rate environment. Any opportunities that have arisen are considered in terms of the Councils short to medium term cash flow requirement and under borrowed position.

18. It remains a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates continue to be very low and in line with the current 0.1% Bank Rate. Financial markets are now pricing in a first increase in Bank Rate from 0.10% to 0.25% earlier than anticipated with some forecasts for this before the end of 2021/22. Reasons for this shift include inflationary pressures in the economy being less transitory and possible wage growth in some sectors of the economy. This has led to an upward shift in longer term investment rates in the last couple of

weeks of September as shown in the graph below for LIBID rates. Any impact of improved longer term investment rates is unlikely to have an effect on Council investments which are being kept liquid in the short to medium term as the Council continues to use its cash balances to delay long term borrowing.

19. Figure 1 shows the interest rates available on the market based on LIBID rates between 7 days and 1 year and also the rate of return that the Council has achieved for the first six months of 2021/22. It shows that the Council has maintained an average rate of return above zero for the first six months of the year for investments whilst ensuring the required liquidity and security of funds for the Council.

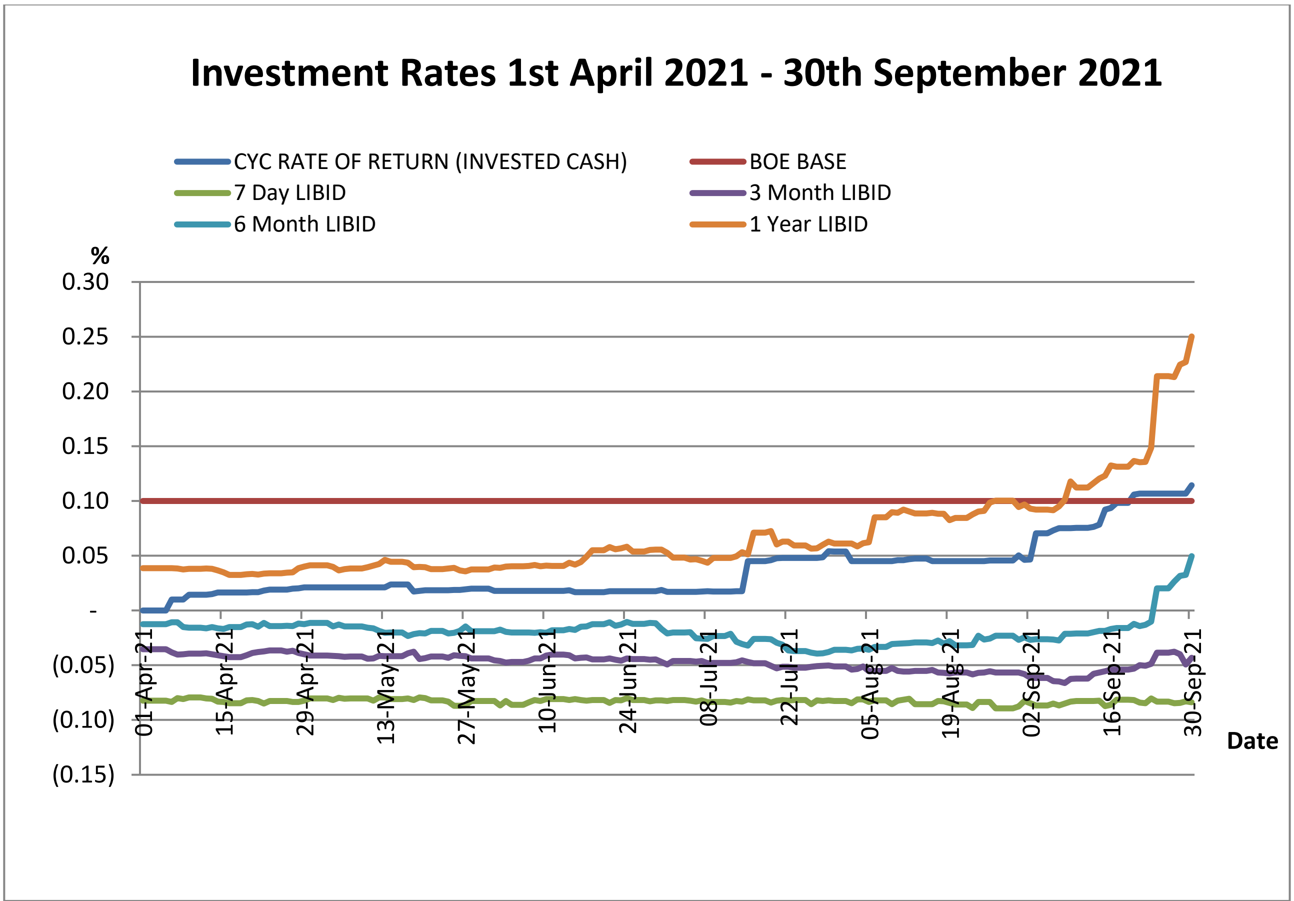

Figure 1 CYC Investments vs Money Market Rates up to 30th September 2021

20. Figure 2 shows the investments portfolio split by cash in bank, deposits in short term call accounts, fixed term investments and money market funds (MMFs).

21. All of the money market funds have an AAAm credit rating, the call notice account has an A credit rating and the cash in the bank account is A+.

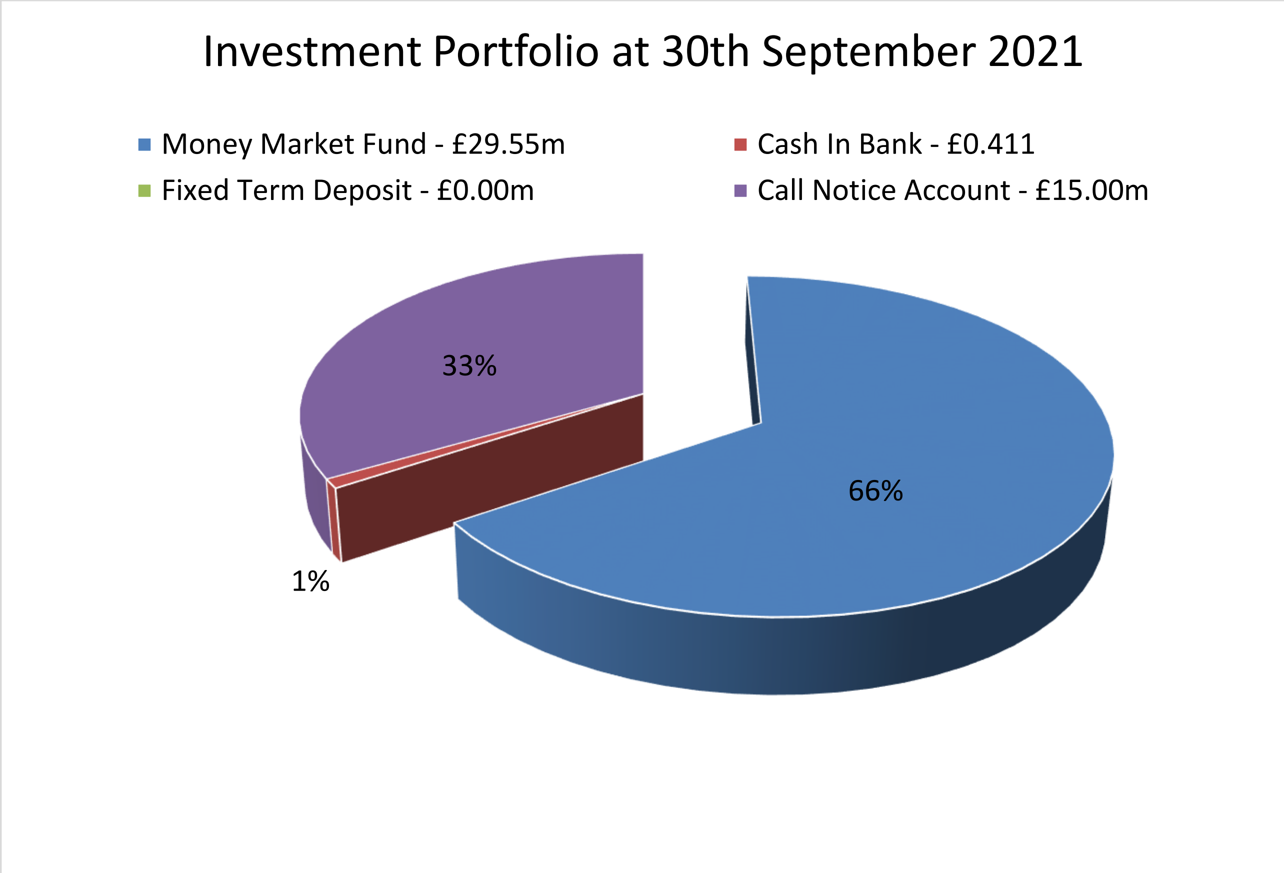

Figure 2 Investment Portfolio by type at 30th September 2021

Borrowing Portfolio

22. The Council undertakes long term borrowing in accordance with the investment requirements of the capital programme and all borrowing is therefore secured for the purpose of its asset base.

23. The level of borrowing taken by the Council is determined by the Capital Financing Requirement (the Councils underlying need to borrow for capital expenditure purposes). Borrowing needs to be affordable, sustainable and prudent.

24. Under regulation, the Council can borrow in advance of need and Markets are therefore constantly monitored and analysed to ensure that advantage is taken of favourable rates and the increased borrowing requirement is not as dependant on interest rates in any one year.

25. On the reverse side, the Council's level of borrowing can also be below the Capital Financing Requirement. This would mean that instead of increasing the Council's level of borrowing, surplus funds held for investment purposes would be utilised. In the current interest rate environment, where investment rates on holding investments are significantly below borrowing rates, consideration is given to the value of taking borrowing or whether it is better for the council to keep investment balances lower.

26. The finance team continues to closely monitor the opportunities that arise and receive daily updates from Link Asset Services in respect of borrowing timings and amounts. No new loans have been taken during the first six months of the year.

27. The Councils long-term borrowing started the year at a level of £297.465m. On 10th August 2021 a £2m PWLB loan was repaid taking the Councils long-term borrowing figure to £295.465m. A further £5m of PWLB loan repayments will be made this financial year, two £1m loans on 5th November 2021 and one £3m loan on 28th February 2022.

28. The Housing Revenue Account debt amount is 49% of the borrowing portfolio at £146.359m (of which £121.550 is self-financing debt) and the General Fund debt is 51% at £149.606m.

29. Figure 3 illustrates the 2021/22 maturity profile of the Council's debt portfolio at 30th September 2021. The maturity profile shows that there is no large concentration of loan maturity in any one year, thereby spreading the interest rate risk dependency.

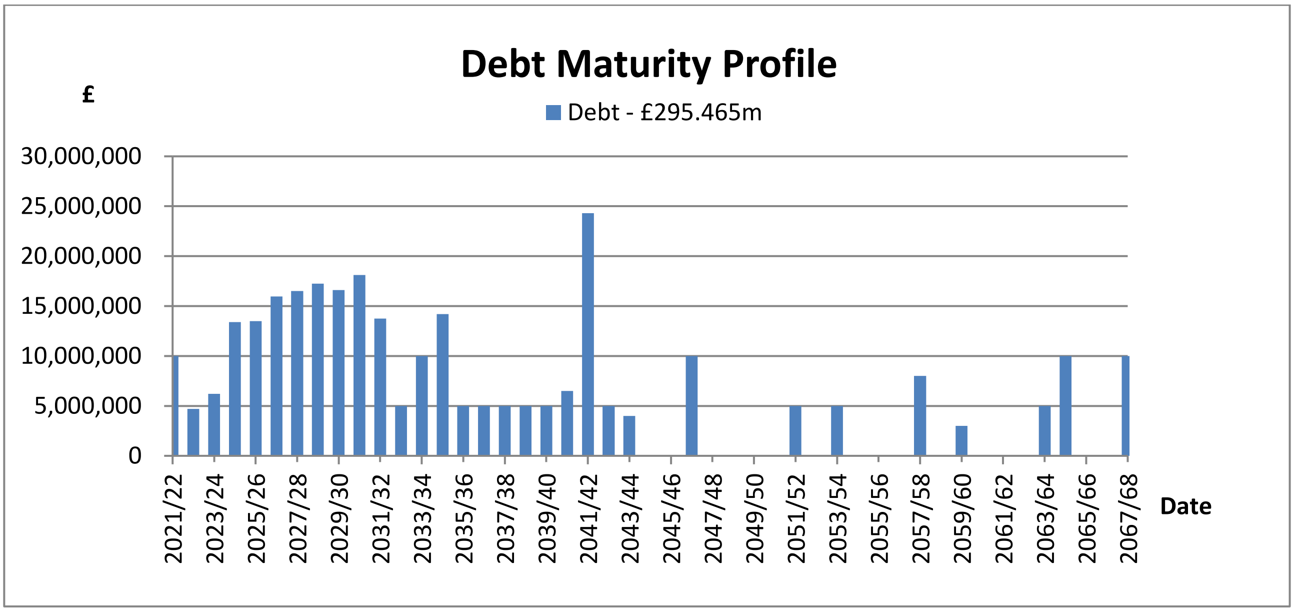

Figure 3 – Debt Maturity Profile at 30th September 2021

30. Table 3 shows PWLB Certainty borrowing rates available for selected loan durations.

	PWLB Certainty borrowing rates by duration of loan

	1 Year	5 Year	10 Year	25 Year	50 Year
Yr High	1.05	1.46	1.84	2.27	2.05
Yr Low	0.81	1.08	1.42	1.75	1.49
Yr Avg	0.88	1.21	1.63	2.02	1.80

Table 3 – PWLB Borrowing Rates (%) – to 30th September 2021

Compliance with Prudential Indicators

31. The Prudential Indicators for 2021/22 included in the Treasury Management Strategy Statement are based on the requirements of the Council's capital programme and approved at Budget Council on 25 February 2021.

32. It is a statutory duty for the Council to determine and keep under review the "Affordable Borrowing Limits" included in the Prudential Indicators. The monitoring of the Prudential Indicators is attached at Annex A. During the financial year 2020/21 to date the Council has operated within the treasury limits and Prudential Indicators set out.

Consultation and Options

33. The report shows the six month position of the treasury management portfolio in 2021/22. The treasury management budget was set in light of the council's expenditure plans and the wider economic market conditions, based on advice from Link Asset Services. It is a statutory requirement to provide the information detailed in the report.

Council Plan

34. The treasury management function aims to achieve the optimum return on investments commensurate with the proper levels of security, and to minimise the interest payable by the Council on its debt structure. It thereby contributes to all Council Plan priorities.

Financial implications

35. The financial implications are in the body of the report.

Legal Implications

36. Treasury Management activities have to conform to the Local Government Act 2003, the Local Authorities (Capital; Finance and Accounting) (England) Regulations 2003 (SI 2003/3146), which specifies that the Council is required to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice and also the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (SI 2008/414), which clarifies the requirements of the Minimum Revenue Provision guidance.

Other Implications

37. There are no crime and disorder, information technology, property, equalities, human resources or other implications because of this report.

Risk Management

38. The Treasury Management function is a high-risk area because of the level of large money transactions that take place. As a result, there are procedures set out for day to day treasury management operations that aim to reduce the risk associated with high volume high value transactions. These are detailed in the Treasury Management Strategy Statement at the start of each financial year.

Contact Details

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<tr><td colspan="4">Wards Affected: All</td><td></td></tr>
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For further information please contact the author of the report

Specialist Implications:
Legal – Not Applicable
Property – Not Applicable
Information Technology – Not Applicable

Annexes
Annex A – Prudential Indicators 2021/22

Glossary of Abbreviations used in the report:

LIBID	London Interbank Bid Rate
PWLB	Public Works Loans Board
MHCLG	Ministry of Housing, Communities & Local Government