Agenda Item No:10

Treasury Management Report – Quarter One Update 2021-22

To:	Strategy & Resources Committee
Meeting Date:	21st September 2021
From:	Chief Finance Officer
Electoral division(s):	All
Key decision:	No
Forward Plan ref:	Not applicable
Outcome:	Through this report the Committee supervises the Council's treasury management, and ensures that public money across the Council's cashflows, borrowing and investments is utilised and deployed effectively and in compliance with the Treasury Management Strategy.
Recommendation:	The Strategy & Resources Committee is recommended to note the Treasury Management Quarter One Report for 2021/22.

Officer contact:
Name: Tom Kelly
Post: Director of Resources and Chief Finance Officer
Email: treasury@cambridgeshire.gov.uk
Tel: 01223 715568

Member contacts:
Names: Cllr L Nethsingha & Cllr E Meschini
Post: Chair/Vice-Chair
Email: lucy.nethsingha@cambridgeshire.gov,uk & elisa.meschini@cambridgeshire.gov.uk
Tel: 01223 706398

1. Background

1.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice for Treasury Management recommends that Members be updated on treasury management activities regularly (annual, mid-year or quarterly reports). This report, therefore, ensures this Council is implementing best practice in accordance with the Code.

2. Economic Climate

2.1 A current economic commentary is in Appendix 1, provided by Link Asset Services, the Council's treasury management advisers. Some of the key points to note are set out below.

2.2 Since May, developments in global GDP growth have been somewhat more substantial than anticipated, particularly in advanced economies. International price pressures have picked up further, reflecting strong demand for goods, rising commodity prices, supply-side constraints and transportation bottlenecks. These have started to become apparent in consumer price inflation in some advanced economies. Financial market measures of inflation expectations suggest that the near-term strength in inflation is expected to be transitory. Vaccine rollout has been a key factor boosting economic confidence.

2.3 **GDP:** The Bank of England revised its expectations for the level of UK GDP in 2021 quarter 2 by around 1.5% since the May Report due to the easing of restrictions on economic activity; this now leaves total GDP in June around only 2.5% below its pre-Covid 2019 quarter 4 level.

2.4 **CPI:** The annual inflation rate in the United Kingdom rose to 2.1% year on year in May from 1.5% year on year in April; this is the first time that the measure has been above the Bank of England's 2% target since July 2019.

3. Interest Rate Forecast

3.1 The latest forecast for UK Bank Rate along with Public Works Loan Board (PWLB) borrowing rates (certainty rate) from the Council's treasury advisors is set out in Table 1.

3.2 This suggests that PWLB rates have increased marginally and there is also now a first increase in Bank Rate from 0.10% to 0.25% forecast for quarter 2 of 2023/24.

Table 1: Interest Rate Forecast (%) May 10, 2021

Link Group Interest Rate View	Sep-21	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	0.10	0.10	0.10	0.10	0.10	0.10	0.25	0.25	0.25
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.30	0.30	0.30
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.20	0.30	0.40	0.40	0.40
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.30	0.30	0.40	0.50	0.50	0.50
5 yr PWLB	1.20	1.30	1.30	1.30	1.40	1.40	1.40	1.40	1.50	1.50	1.50
10 yr PWLB	1.70	1.70	1.80	1.80	1.90	1.90	1.90	2.00	2.00	2.00	2.00
25 yr PWLB	2.20	2.30	2.40	2.40	2.40	2.50	2.50	2.50	2.50	2.50	2.60
50 yr PWLB	2.00	2.10	2.20	2.20	2.20	2.30	2.30	2.30	2.30	2.30	2.40

Gilt yields / PWLB rates

3.3 At the start of 2021, all gilt yields from 1 to 8 years were negative: however, since then all gilt yields have become positive and have risen sharply, especially in medium and longer-term periods. The main driver of these increases has been investors becoming progressively more concerned at the way that inflation has risen sharply in major western economies during 2021, and further increases in inflation are expected.

3.4 Following the sudden increase in margins on PWLB loans in October 2019, a consultation was held with local authorities in July 2020 as part of a review of margins over gilt yields for PWLB rates. This led in November 2020 to the margins over gilt yields being reduced by 1% back to their original level (80 basis points above gilts). However, at the same time a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three-year capital programme. Additionally, the Council also has access to over £50m of borrowing from PWLB at the local infrastructure rate (60 basis points above gilts) as expenditure on energy schemes, approved in a bid to HM Treasury, comes forward.

3.5 The Council has renewed its interest in borrowing from the UK Municipal Bonds Agency, as an alternative to the PWLB, and is advised by the agency that a pooled local government bond is in prospect for later in 2021.

4. Summary Portfolio Position

4.1. The level of net borrowing set in the Treasury Management Strategy Statement (TMSS) for 31st March 2022 was £805.0m. On 1st April 2021, the net debt was £714.1m, and the actual at 30th June 2021 was £623.0m (excluding all Third-party loans and Equity). This is a decrease in borrowing over the period, due to some loans maturing and not yet being refinanced. Cash flows at the beginning of the year are typically stronger than at the end of the year, as many grant receipts are received in advance of spend (and due to the current Covid-19 pandemic the Council is in receipt of further grants compared to before the pandemic). The 2021/22 net borrowing position is expected rise more substantially towards the end of the financial year as capital projects are progressed to completion and financed.

4.2 Further analysis on borrowing and investment is set out in the next two sections. A snapshot of the Council's debt and investment position is shown in Table 2 below.

Table 2: Net Borrowing quarter 1 2021/22

Borrowings	Actual as at 1 April 2021 £m	Actual as at 30 June 2021 £m	In- months change £m
Long term Borrowing (>12mth)	685.7	704.6	-18.9
Short term Borrowing (<12mth)	127.0	92.0	35.0
Total Borrowings	812.7	796.6	-16.1
Treasury Investment	-98.1	-173.6	-75.5
Total Net Debt/Borrowings	714.6	623.0	91.6

5. Investments

5.1 The Treasury Management Strategy Statement (TMSS) for 2021/22, including the Annual Investment Strategy for financial assets, was approved by Council in February 2021. It sets out the Council's investment priorities as being:

1. Security of Capital;
2. Liquidity; and then
3. Yield

5.2 The Council will aim to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity. As shown by the interest rate forecasts in section 3, it is now impossible to earn the level of interest rates commonly seen in previous decades as all short-term money market investment rates are barely above zero now that Bank Rate is at 0.10%. Some entities are offering negative rates of return in some shorter time periods. Given this environment and the fact that increases in Bank Rate are unlikely to occur before the end of the current forecast horizon of quarter 2 2023/24, investment returns are expected to remain low.

5.3 At 30th June 2021 the Council's investment balances totalled £173.6m; the balance is split between Money Market Funds, Call/Notice accounts and CCLA and Allianz collective investment funds (see Table 3 below). The balance excludes Third Party Loans and Share Capital.

5.4 **Property Fund:** During quarter 1, the key focus for CCLA was to protect income. The revenue return on investment for quarter 1 was 2.86%. The capital value of the investment at 30th June 2021 was £11.1m (£10.4m at 30th June 2020) compared to an original investment value of £12m. Income held up better than expected during the pandemic, reflecting the fund's active asset management strategy and tenant engagement.

5.5 **Multi-Class Credit Fund:** At the end of quarter 1, the valuation of the CCC share of the fund stood at £14.9m. The Council originally invested £14.5m in September 2020, an increase in valuation of £400,000. The fund distributes income annually in December; however, over quarter 1 to 30th June 2021 the fund produced a net return of 1.19%, a significant improvement on the 0.04% net return from quarter 4 2020/21.

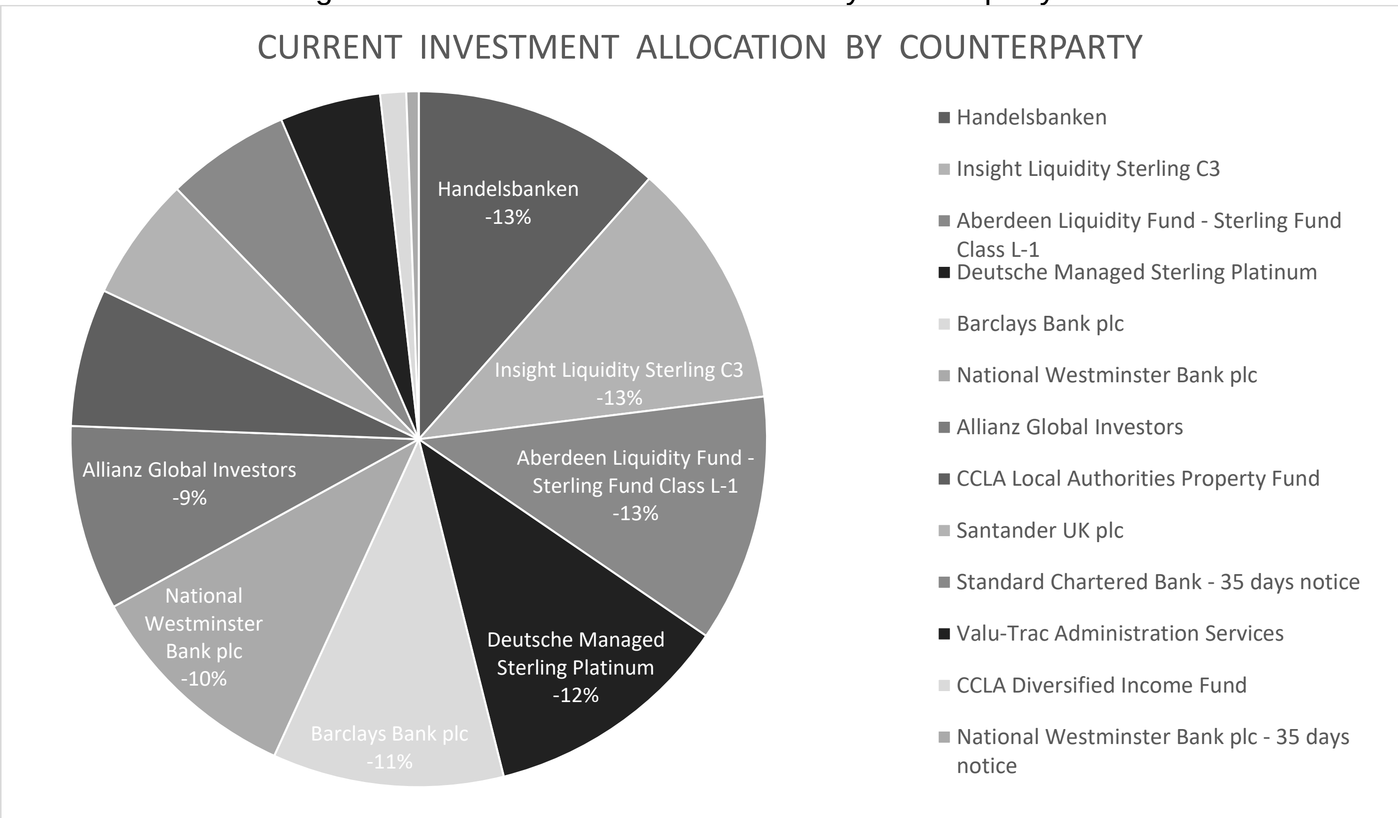
5.6 The Council invested £8.0m in the Gravis Clean Energy fund in May 2021. The fund was first launched in December 2017, and the current fund size is £330.2m. The fund:

- Aims to deliver a regular income expected to be 4.5% per annum.
- Aims to preserve investors' capital throughout market cycles, with the potential for capital growth.
- Invests in a diversified portfolio of global listed securities, including Investment Companies and Equities.
- Offers exposure to companies engaged in the provision, storage, supply and consumption of clean energy.

The current valuation at the end of quarter 1 is £8.13m, an increase in valuation of £130k. The Council received the first dividend of £76k in July 2021.

5.7. The average level investment in quarter 1 (excluding 3rd party loans and equity) was £124.6m, which carried a weighted average rate of 3.02%. The level of investment funds varies dependent on the timing of precept receipts, grants, and the progress of the capital programme; at the end of quarter 1 investments (excluding 3rd party loans and equity) totalled £173.6m. Figure 1 below shows the investment by counterparty as at 30th June 2021.

Figure 1: CCC Investments allocation by Counterparty



5.8 Table 3 below summarises the maturity profile of the Council's investment portfolio at the end of quarter 1 2021/22 (excluding Third Party Loans):

Table 3: Investment maturity profile at end of quarter 1 2021/22

		Maturity Period					
		0d	0-3m	3-6m	~5yrs	Total	
Product	Access Type	£m	£m	£m	£m	£m	%
Money Market Funds	Same-Day	60.0				60.0	34.6
Bank Call Account	Instant Access	66.3				66.3	38.2
Notice Account	35 Day Notice			11.0		11.0	6.3
Pooled Property Fund	Redemption Period Applies				11.1	11.1	6.4
Pooled Diversified Income Fund	Redemption – two days				2.1	**2.1**	1.2
Pooled Multi-class credit Fund	Redemption Period Applies				14.9	**14.9**	*8.6*
Income Fund (Energy)	Redemption Period Applies				8.1	**8.1**	*4.7*
	Total	126.3	0.00	11.0	36.2	173.6	*100.0*
	%	*72.8*	*0.00*	*6.3*	*20.9*	*100.0*	

5.9 Set out below are details of the amounts outstanding on loans and share capital investments classed as capital expenditure advanced to third party organisations at the end of quarter 4:

Table 4: Loans/Equity holdings in This Land companies end of quarter 1 2021/22

Loan Summary	Amount Outstanding (£m)	Repayment Year
Loans for land acquired from third parties	2.040	2021/22
Land, Construction & Development loans	113.851	2026/27, 2027/28 and 2028/29
Equity holding	5.851	N/A
Total Loans/Equity in This Land Ltd	121.742	

Table 5: Loans/Equity holdings in LGSS Law end of quarter 1 2021/22

Loan Summary	Original Amount (£m)	Amount Outstanding (£m)	Repayment Year
Cashflow loan	0.325	0.325	2029/30
Equity holding	0.475	0.475	-
Total Loans/Equity in LGSS Law Ltd	0.800	0.800	

Table 6: Third Party Loans Principal Outstanding end of quarter 1 2021/22

Loan Counterparty	Original Amount (£m)	Amount Outstanding (£m)	Repayment Year
Arthur Rank Hospice Charity	4.000	3.340	2042/43
Estover Playing Field 2015 CIC (Guaranteed by March Town Council)	0.350	0.221	2024/25
Wisbech Town Council	0.150	0.150	2043/44
VIVA Arts & Community Group	0.300	0.287	2043/44
Total Third Party Loans	4.800	3.998	

5.10 Investment returns compared to benchmark are shown in Table 7 below.

Table 7: Average Benchmark Performance – quarter 1 2021/22

	Benchmark	Benchmark Return	Council Performance
Quarter 1	3m LIBID	-0.04%	0.08%
Year To Date	3m LIBID	-0.04%	0.08%

5.11 Leaving market conditions aside, the Council's return on investments is influenced by a number of factors, the largest contributors being the duration of investments and the credit quality of the institution or instrument:

- Credit risk is the consideration of the likelihood of default and is controlled through the creditworthiness policy approved by Council.
- The duration of an investment introduces liquidity risk; the risk that funds cannot be accessed when required.
- Interest rate risk; the risk that arises from fluctuating market interest rates.

These factors and associated risks are actively managed by the Council's Finance team.

6. Borrowing

6.1 The Council can raise cash through borrowing in order to fund expenditure on its capital programme for the benefit of Cambridgeshire. The amount of new borrowing needed each year is determined by capital expenditure plans and projections of the Capital Financing Requirement, underlying borrowing requirement, forecast cash-backed reserves and both current and forecast economic conditions.

6.2 The Council will continue to utilise short to medium-term borrowing from other local authorities and authorised brokers, as well as PWLB following the recent rate reduction. The Council intends to keep a proportion of the borrowing portfolio short-dated; but is also focused on extending the average duration of loans in the portfolio, whilst there are opportunities to fix loans for extended maturities at historically low levels.

6.3 In quarter 1, the Council repaid on maturity a total of £80.0m, of which £60m was short-term loans from other local authorities and £20.1m was longer-term loans from other authorities and PWLB. Loans raised during quarter 1 amounted to £59.0m. Of which short-term borrowing maturing within 1 year was £20.0m, £5.0m was fixed-term loans maturing within 2-3 years, and £34.0m was PWLB loans.

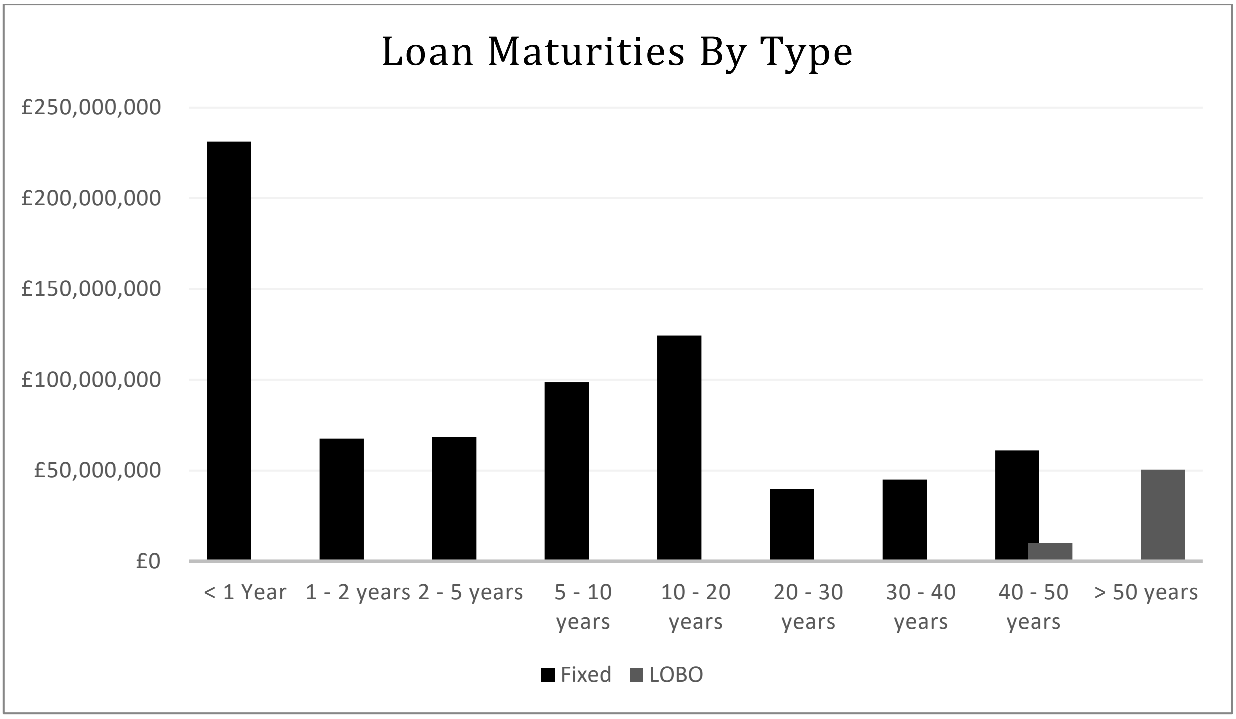
6.4 At the end of quarter 1, the Council held £796.6m of borrowing, of which £92m was short-term borrowing that matures in less than 1 year from date of issue. The Council continues to be able to re-finance loans as required, generally at this time at a lower interest rate than the maturity loan. As opportunities arise, we are seeking longer loan terms, rather than less than 1 year, in view of the current conditions.

6.5 Table 8 below sets out the maturity profile of the Council's borrowing portfolio at the end of quarter 1; £454.1m.1m is held with the PWLB, £282.0m from other local authorities, £45.0m in market loans and £15.5m is a single market Lender Option Borrower Option (LOBO) loan. Of the £796.6m of borrowing, £231.4m (including both short-term and longer-term loans) will mature in less than 1 year, therefore potentially requiring refinancing.

Table 8: Loan Maturity Profile – quarter 1 2021/22

Term remaining	Borrowing	
	£m	%
< 1 Year	£231,365,333	29.04%
1 - 2 years	£67,493,333	8.47%
2 - 5 years	£68,419,000	8.59%
5 - 10 years	£98,683,667	12.39%
10 - 20 years	£124,323,333	15.61%
20 - 30 years	£39,833,333	5.00%
30 - 40 years	£45,000,000	5.65%
40 - 50 years	£71,000,000	8.91%
> 50 years	£50,500,000	6.34%
Total	£796,618,000	100.0

Figure 3 Loan Maturities by Type – quarter 1 2021/22



6.6 The market LOBO loan is included in Table 8 at final maturity rather than next potential call date. In the current low interest rate environment, the likelihood of the lender exercising their option to increase the interest rate on this loan - and so triggering the Council's option to repayment at par - is considered to be low.

6.7 The Council is in an internally borrowed cash position and balances will need to be replenished at some point in the future (subject to expenditure demands). This strategy is prudent while investment returns are lower than the cost of servicing debt and also serves to mitigate counterparty risk. The Council therefore plans to maintain this internal borrowing position but will closely monitor those reserves, balances and cashflows supporting this approach.

6.8 No borrowing rescheduling was undertaken during quarter 1. Rescheduling opportunities are limited in the current economic climate. For PWLB loans, due to the spread between the carrying rate of existing borrowing and early redemption rates, substantial exit (premium) costs would be incurred. For market borrowing, the lender uses the certainty of the loans cashflow profile to hedge against forecast interest rate movements and so would pass the cost of unwinding these instruments onto the Council as an exit (premium) cost. Officers continue to monitor the position regularly.

7. Compliance with Treasury and Prudential Limits

7.1 The Council's treasury and prudential indicators are shown in Appendix 2.

7.2 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the quarter ended 31st March 2021, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2021/22.

7.3 All treasury management operations have also been conducted in full compliance with the Council's Treasury Management Practices.

8. Alignment with Corporate Priorities

8.1 Communities at the heart of everything we do

There are no significant implications for this priority.

8.2 A good quality of life for everyone

There are no significant implications for this priority.

8.3 Helping our children learn, develop and live life to the full

There are no significant implications for this priority.

8.4 Cambridgeshire: a well-connected, safe, clean, green environment

There are no significant implications for this priority.

8.5 Protecting and caring for those who need us

There are no significant implications for this priority.

9. Significant Implications

9.1 Resource Implications

This report provides information on performance against the Treasury Management Strategy. Decisions on treasury management, which are driven by the capital programme and the Council’s overall financial position, will impact the Debt Charges Budget and are reported through the Budget Monitoring process.

9.2 Procurement/Contractual/Council Contract Procedure Rules Implications

There are no significant implications for this category.

9.3 Statutory, Legal and Risk Implications

The Council continues to operate within the statutory requirements for borrowing and investments. Further details can be found within Appendix 2.

9.4 Equality and Diversity Implications

There are no significant implications for this category.

9.5 Engagement and Communications Implications

There are no significant implications for this category.

9.6 Localism and Local Member Involvement

There are no significant implications for this category.

9.7 Public Health Implications

There are no significant implications for this category.

9.8 Environment and Climate Change Implications on Priority Areas:

While this paper proposes no significant implications for this category, it should be noted that the Council’s investments in Multi-Class Credit have been placed in a Sustainable and Responsible Investment (SRI) Fund and a Clean Energy Fund.

9.8.1 Implication 1: Energy efficient, low carbon buildings.

Status: Neutral
Explanation: There are no significant implications within this category

9.8.2 Implication 2: Low carbon transport.

Status: Neutral
Explanation: There are no significant implications within this category.

9.8.3 Implication 3: Green spaces, peatland, afforestation, habitats and land management.

Status: Neutral
Explanation: There are no significant implications within this category.

9.8.4 Implication 4: Waste Management and Tackling Plastic Pollution.

Status: Neutral
Explanation: There are no significant implications within this category.

9.8.5 Implication 5: Water use, availability and management:

Status: Neutral
Explanation: There are no significant implications within this category.

9.8.6 Implication 6: Air Pollution.

Status: Neutral
Explanation: There are no significant implications within this category.

9.8.7 Implication 7: Resilience of our services and infrastructure and supporting vulnerable people to cope with climate change.

Status: Neutral
Explanation: There are no significant implications within this category.

10. Source documents

10.1 None

Appendix 1: Extracted economic commentary from the Council's external Treasury Management Advisor (prepared in June 2021)

During the quarter ended 30th June 2021 (quarter 1 of financial year 2021/22):
GDP rose by 2.3% m/m in April as restrictions were lifted on non-essential retailers.

- There were signs that activity was given another boost in May as indoor hospitality resumed.
- Sharply increasing virus cases in June delayed the final easing of lockdown restrictions by four weeks.
- Inflation accelerated to 2.1% in May due to energy effects and a surge in reopening inflation.
- Gilt yields and sterling made little headway, while the FTSE 100 failed to catch up on the S&P 500.

The economic recovery stepped up a gear as non-essential retailers and outdoor hospitality reopened on 12th April. The 2.3% m/m gain in GDP in April was the fastest pace of growth since July 2020 and left the economy just 3.8% below its February 2020 level. It was the accommodation and food sector and the retail sector that led the charge with monthly gains of 44.1% and 8.9% respectively.

Some sectors will take longer to recover than consumer spending. Trade flows are still well below pre-crisis levels and trade with the EU remains especially depressed after Brexit. Exports values to the EU, excluding erratic's, were 5.7% below their December level in April, while imports were a whopping 19.1% below. The slower recovery in the euro-zone and lingering Brexit effects are still hampering the recovery in trade with the EU, which will probably continue to lag behind the broader recovery.

After being subdued over much of the pandemic, inflation picked up sharply in this quarter. A large portion of the rise in CPI inflation from 0.7% in March to 1.5% in April was due to temporary energy price effects. Fuel price inflation added 0.3 percentage points (ppts). And the 9.2% increase in Ofgem's gas and electricity price cap from 1st April added 0.3ppts too. Inflation climbed further in May to 2.1% and core CPI inflation rose from 1.3% to 2.0%. Some of this was driven by reopening inflation, with clothing inflation, restaurants/hotels inflation and package holidays inflation all rising and likely rise further.

A strong recovery is underway in the labour market. The 113,000 rise in LFS employment in the three months to April was the largest rise since February 2020 and the ILO unemployment rate edged down to 4.7% from 4.8%. The strong set of labour market figures for April fed concerns over the anecdotal reports of labour shortages and its possible impact on inflation from higher wage growth. Vacancies rose to just 3.4% below their pre-virus level in May.

The myriad of factors boosting inflation (energy price effects, utility price effects, supply/shipping constraints, commodity prices and reopening), are likely to prove temporary. As such, the Bank of England will probably look through increases in inflation above the 2.0% target due to these factors. The minutes of the June meeting emphasised “the medium-term prospects for inflation” and left intact the forward guidance designed to stress the MPC’s patience.

Appendix 2: Treasury and Prudential Indicators Quarter 1

Treasury / Prudential Indicator	2021/22 Indicator	2021/22 Quarter 1
Authorised limit for external debt (Inc' loans raised to on-lend to Housing & Investment Company)	-----£1,074.0m-----	
Operational boundary for external debt (Inc' loans raised to on-lend to Housing & Investment Company)	----- £1,044.0m-----	
Total Net Borrowing – Quarter 1	--------£623.0m------	
Capital Financing Requirement (CFR) *[Including PFI and Finance Lease Liabilities]*	£984.4m	£984.4m
Ratio of financing costs to net revenue streams	8.8%	5.53%
Upper limit of fixed interest rates based on net debt*	150%	120%
Upper limit of variable interest rates based on net debt*	65%	-20%
Principal sums invested over 365 days (exc' third party loans)	£50.0m	£36.3m
Maturity structure of borrowing limits**:		
Under 12 months	Max. 80% Min. 0%	29.04%
12 months to 2 years	Max. 50% Min. 0%	8.47%
2 years to 5 years	Max. 50% Min. 0%	8.59%
5 years to 10 years	Max. 50% Min. 0%	12.39%
10 years and above	Max. 100% Min. 0%	41.51%

*The interest rate exposure is calculated a percentage of net debt. Due to the mathematical calculation exposures could be greater than 100% or below zero (i.e. negative) depending on the component parts of the formula.

**The Treasury Management Code of Practice guidance notes requires that maturity is determined by the earliest date on which the lender can trigger repayment, which in the case of LOBO loans is the next break/call point. This approach differs to Table 6 at paragraph 6.5 above, which instead shows the Council’s LOBO loan at maturity date as the likelihood of the option being exercised is low.