Report Title:	**Mid Year Treasury Management Update 2020/21**
Contains Confidential or Exempt Information?	No - Part I
Lead Member:	Councillor Hilton, Lead Member for Finance and Ascot
Meeting and Date:	Audit and Governance Committee – 9 November 2020
Responsible Officer(s):	Adele Taylor, Director of Resources (S151151 Officer)
Wards affected:	All

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Royal Borough of Windsor & Maidenhead

REPORT SUMMARY

1. The purpose of this report is to:

   a) Update Members on the delivery of the Treasury Management Strategy approved by Council on 25th February 2020 and allows for any changes to be made depending on market conditions;

   b) This report forms part of the monitoring of the treasury management function as recommended in the Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management Code of Practice which requires that the Council receives a report on its treasury management activity at least twice a year;

   Specifically this report includes:

   a) a review of the Council's financial investment portfolio for 2020/21 as at 30th September 2020;

   b) a review of the Council's borrowing strategy in 2020/21;

   c) a review of compliance with the Council's Treasury and Prudential limits for the first 6 months of 2020/21; and

   d) an economic update for the first half of the financial year. (Appendix C)

2. The Council has complied with all elements of its Treasury Management Strategy Statement (TMSS) as agreed by Council in February 2020.

1. DETAILS OF RECOMMENDATION(S)

RECOMMENDATION: That the Audit and Governance Committee notes and approves the mid-year Treasury Management Update Report 2020/21.

2. REASON(S) FOR RECOMMENDATION(S) AND OPTIONS CONSIDERED

2.1 The Council has adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Authority to approve treasury management mid-year and annual reports.

2.2 The Council's treasury management strategy for 2020/21 was approved at the Council meeting on 25th February 2020. When borrowing and investing money the Authority is exposed to financial risks including the loss of invested funds and the revenue impact of changing interest rates. The successful identification, monitoring and control of risk remains central to the Council's treasury management strategy.

3. KEY IMPLICATIONS

3.1 A successful treasury management approach will ensure the security of the Council's assets whilst meeting the liquidity requirements of the Council and ensuring an investment return that meets the target set in the table below.

Table 1: Investment return target

Outcome	Unmet	Met	Exceeded	Significantly Exceeded	Date of delivery
A return that exceeds benchmark (Bank of England base rate plus 0.25%)	<0%	>0%	>0.1%	>0.2%	31 March 2021

4. FINANCIAL DETAILS / VALUE FOR MONEY

Half-yearly Review of Treasury Management Activity

4.1.1 This report reviews the period from 1st April 2020 to 30th September 2020.

4.1.2 An economic update for the period provided by the Council's treasury management advisors Arlingclose is attached as Appendix C.

4.2 **Investments**

4.2.1 The Council receives payments from a variety of external sources, including government grants, council tax and business rates. These funds are invested in either fixed rate loans, cash deposits or money market funds within Council approved counterparties. The list of approved counterparties is known as the "Lending List". A copy of the current approved Lending List is attached to this report as Appendix A.

4.2.2 Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return. The Council's objective when investing money is to strike an appropriate balance between risk and return,

minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

4.2.3 Whilst total funds under management varied throughout the period, total funds under management at the 30th September 2020 were £22,382,000. (£51,726,000 at 31st March 2020).

4.2.4 It should be noted that during the period central government provided government grant funding in advance to assist with potential cashflow issues arising from Covid-19 . There was a likelihood of unexpected calls on cash flow to deal with the impacts of the crisis so the Council has kept more cash available at very short notice than is normal. Liquid cash was diversified between multiple counterparties to minimise counterparty risk.

4.2.5 The returns available for liquid cash held in Money Market Funds or call accounts have moved towards zero over the period which has lowered the overall return on the Council's investments.

4.2.6 The allocation of funds under management by counterparty type at 30th September 2020 is as follows:

Lloyds Current Account	£3,140,000
Money Market Funds	£13,000,000
Loans to partner organisation	£6,242,000
Total	£22,382,000

4.2.7 The investment return benchmark is 0.25% above Bank of England base rate. The Bank of England base rate is currently 0.10%.

4.2.8 The investment return for the 6 months to 30th September 2020 was 0.36% compared to the benchmark of 0.35%.

4.2.9 In 2020/21 we have made an upfront prepayment of Pension Fund contributions for 2020/21 that has reduced the overall costs by £108,000. This amount is not included in the investment return reported above but it contributes towards budget targets.

4.3 Borrowing Requirement & Borrowing Strategy

4.3.1 The table below shows how the level of long and short term borrowing is projected to change during 2020/21.

Borrowing Type	Actual 31/03/2020	Actual 30/09/2020	Projected 31/03/2021
	£000	£000	£000
Long Term	57,049	57,049	57,049
Short Term – Local Authority	134,000	82,000	161,000
Short Term – LEP	33,521	68,584	0
Investments	(51,726)	(22,382)	(20,000)
Net Borrowing	**172,844**	**185,251**	**198,049**

4.3.2 The above table projects that the Council will need to borrow an additional £79,000,000 from Local Authorities by 31st March 2021 to finance its capital investment and to replace internally borrowed funds held on behalf of the LEP (Local Enterprise Partnership).

4.3.3 This projection is based on the following assumptions:

(i) The capital programme will be implemented in line with current assumptions – if there is any further slippage within the programme then the short-term borrowing requirement will be lower.

(ii) The LEP will utilise all of their funding in year which the Council will need to borrow to replace. If there are any unspent funds retained by the LEP at the end of March this would reduce the amount of replacement borrowing required to be taken out with other local authorities.

4.3.4 The Council's borrowing requirement has revenue implications for the Council. Accordingly, the Council has engaged Treasury Management Advisors, Arlingclose to advise on its Borrowing and Treasury Management Strategy.

4.3.5 Current market conditions are as follows:-

(a) In response to the economic effect of the Covid-19 crisis interest rates have been reduced to the historic low level of 0.1%.

(b) Pending the outcome of the PWLB consultation the PWLB certainty borrowing rate remains at its increased rate of 1.8% above gilts making it a relatively expensive option.

(c) Short term loans remain at a significantly lower rate than long term loans.

4.3.6 On the basis of the above, the Council has continued to take up short term borrowing when required and continues to review the option to increase the proportion of long term borrowing with its treasury management advisors.

4.3.7 No new long term borrowing has been taken on since the 1st of April 2020 as the current PWLB and other market alternative rates are unfavourable compared to those offered for the short term. This is kept under regular review.

4.3.8 As at 30th September 2020 the Authority's total long term external borrowing was £57,049,400, with an average interest rate of 4.97% for the Public Works Loan Board (PWLB) loans and 4.19% for the Lender Option Borrower Option (LOBO) loans borrowed from Barclays and Dexia. Appendix B shows the breakdown of this long term borrowing figure. During the course of 2020/21 a total of £2,733,000 will be paid on existing long term loans in the form of interest payments.

4.3.9 The Chancellor's March 2020 Budget statement included changes to Public Works Loan Board (PWLB) policy and launched a wide-ranging consultation on the PWLB's future direction. It contained proposals to allow authorities that are not

involved in “debt for yield” activity to borrow at lower rates as well as stopping local authorities using PWLB loans to buy commercial assets primarily for yield.

4.3.10 In response to these proposed changes the Council has reviewed its current capital programme and is satisfied that it is not engaged in any projects that would lead it to be classified by the PWLB as engaging in debt for yield activity. Therefore based on the information provided as part of the consultation if lower rates are introduced the Council would expect to be able to access these. While this would be expected to give the Council access to long term borrowing at lower rates than are currently available it likely these will still be significantly higher than the current short term rates that are available.

4.3.11 The strategy to increase short-term borrowing has exposed the council to the risk that rates could rise. A 1% increase in interest rates for the current level of short-term loans could be in the region of £1m.

4.3.12 Officers will therefore keep under review options to increase the proportion of its borrowing that is fixed long-term during 2020/21 including reviewing options within the market.

4.4 Treasury Management Strategy

4.4.1 The Treasury Management Strategy approved on 25th February 2020 sets out parameters that are designed to govern the level of council borrowing.

(i) **The operational boundary** – sets the maximum level of borrowing that the Council will incur based on its estimated need to finance its capital investment. It is recognised that the Council may borrow in excess of this amount for cash flow purposes i.e. while it waits to receive government grants or other significant income. The limit for 2020/21 is £252,000,000.

(ii) **The authorised limit** – is an absolute limit and sets the absolute maximum level of borrowing that the council can undertake and cannot be exceeded in the short term. The limit for 2020/21 is £275,000,000.

4.4.2 The Council has remained within these approved borrowing limits during 2020/21.

4.4.3 The Council’s upper limit for the proportion of its borrowing that is exposed to variable interest rates is 80%. The Council has remained within this limit during 2020/21 with the actual proportion forecast to be 74% at 31st March 2021.

LEGAL IMPLICATIONS

4.5 In producing and reviewing this report the Council is meeting legal obligations to properly manage its funds.

5. RISK MANAGEMENT

Risks	Uncontrolled Risk	Controls	Controlled Risk
That a counterparty defaults on repayment of a loan resulting in a loss of capital for the Council	MEDIUM	Loans are only made to counterparties on the approved lending list. The credit ratings of counterparties on the lending list are monitored regularly.	LOW
That funds are invested in fixed term deposits and are not available to meet the Council's commitment to pay suppliers and payroll.	MEDIUM	A cash flow forecast is maintained and referred to when investment decisions are made to ensure that funds are available to meet the Council's commitment to pay suppliers and payroll.	LOW

6. POTENTIAL IMPACTS

6.1 Equalities. None identified.

6.2 Climate change/sustainability. None identified.

6.3 Data Protection/GDPR. None identified.,

7. CONSULTATION

7.1 Not applicable

8. TIMETABLE FOR IMPLEMENTATION

8.1 This section is not applicable.

9. APPENDICES

This report is supported by three appendices:

- Appendix A – Approved Lending List
- Appendix B – Long Term Borrowing at 30th September 2020
- Appendix C – Economic Update

10. BACKGROUND DOCUMENTS

- Not applicable

11. CONSULTATION (MANDATORY)

Name of consultee	Post held	Date sent	Date returned
Cllr Hilton	Lead Member for Finance and Ascot	23/10/20	
Duncan Sharkey	Managing Director	23/10/20	
Russell O'Keefe	Director of Place	23/10/20	
Adele Taylor	Director of Resources and S151 Officer	23/10/20	27/10/20
Elaine Browne	Head of Law	23/10/20	28/10/20
Nikki Craig	Head of HR, Corporate Projects & ICT	23/10/20	27/10/20
Louisa Dean	Communications	23/10/20	
Kevin McDaniel	Director of Children's Services	23/10/20	27/10/20
Hilary Hall	Director of Adults, Commissioning & Health	23/10/20	26/10/20
Karen Shepherd	Head of Governance	23/10/20	26/10/20
Andrew Vallance	Head of Finance	23/10/20	23/10/20
Mary Severin	Monitoring Officer	23/10/20	28/10/20

REPORT HISTORY

Decision type: No	**Urgency item?** No	**To Follow item?** No
Report Author: Ryan Stone, Accountant		

APPENDIX A

Royal Borough of Windsor & Maidenhead Approved Counterparty Lending List

Fitch Ratings	FITCH ShortTerm Rating	FITCH Long Term Rating	FITCH Outlook	Max. Sum To Be Lent £m
UK Government				
Debt Management Office	F1+	AA-	Negative	**no limit**
Banks				
Australia and New Zealand Bank	F1	A+	Negative	**5**
Barclays Bank	F1	A	Negative	**5**
Clydesdale Bank	F2	A-	Negative	**5**
HSBC	F1+	AA-	Negative	**5**
Lloyds Banking Group	F1	A+	Negative	**7.5**
National Australia Bank Ltd	F1	A+	Negative	**5**
Royal Bank of Canada	F1+	AA	Negative	**5**
Royal Bank of Scotland	F1	A	Negative	**5**
Santander UK	F2	A-	Negative	**5**
Standard Chartered	F1	A	Negative	**5**
Ulster Bank	F1	A+	Negative	**5**
Local Authorities				
All UK Local Authorities, with the exception of those with reported financial irregularities.				**5**
Money Market Funds				
All money market funds with a Fitch AAA long term credit rating, including:				
Federated Short Term Sterling Prime Fund		AAA		**5**
Invesco Sterling Liquidity Fund		AAA		**5**
Aberdeen Sterling Liquidity Fund		AAA		**5**
Insight GBP Liquidity Fund		AAA		**5**
LGIM Sterling Liquidity Fund		AAA		**5**
Revolving Credit Facility				
AFC				**11.7**
Financial Services Companies				
Kames Capital				**1**
Legal & General				**1.5**
RBWM associated companies				
Flexible Home Improvement Loans Ltd				**0.5**
RBWM Property Company Ltd				**1.5**
Charitable Trusts				
Leisure Focus Trust				**0.35**

SHORT TERM RATING
Expectation of timely repayment of financial commitments.
F1+ is most likely to repay on time, **F1** Highest Credit, **F2** Good, **F3** Fair, **B** Speculative, **C** High Default Risk

LONG TERM RATING
Expectation of credit risk. **AAA** is the least risky, ie little credit risk. **AA** Very High Credit, **A** High, **BBB** Good.
Below BBB indicates non-investment grade

Long Term Borrowing at 30th September 2020

PWLB Borrowing

Duration/ Type	Repayment Date	Loan Value £000s
25yrs/Maturity	25/09/21	785
25yrs/Maturity	08/06/29	7,500
26yrs/Maturity	25/09/29	2,500
26yrs/Maturity	23/09/30	10,000
25yrs/Maturity	08/12/30	5,000
30yrs/Maturity	25/09/33	5,000
45yrs/Maturity	08/12/50	5,000
45yrs/Maturity	08/12/50	5,000
60yrs/Maturity	25/03/55	1,600
60yrs/Maturity	25/09/55	1,000
60yrs/Maturity	25/03/56	400
60yrs/Maturity	25/09/56	265
Total Fixed Term Borowing		**44,049**

ANALYSIS OF PWLB RESIDUAL MATURITY at 30.9.20

Maturing Within	Amount £000s	Average Rate
1 Year	785	8.000%
1 to 2 Years	0	0.000%
2 to 5 Years	0	0.000%
5 to 10 Years	20,000	4.950%
10 to 15 Years	10,000	4.475%
15 to 20 Years	0	0.000%
20 to 25 Years	0	0.000%
25 to 30 Years	0	0.000%
30 to 35 Years	11,600	4.741%
35 to 40 Years	1,665	8.240%
40 to 45 Years	0	0.000%
TOTAL	**44,049**	**4.966%**

LOBO Borrowing

	Duration/ Type	Repayment Date	Loan Value £000s
Barclays	60yrs/15yrs fixed, 6mth LOBO	19-Jul-66	5,000
Dexia	35yrs/5yrs fixed, 5yr LOBO	26-Jan-43	8,000
Total Fixed Term Borowing			**13,000**

ANALYSIS OF LOBO RESIDUAL MATURITY at 30.9.20

Maturing Within	Amount £000s	Average Rate
5 to 30 Years	8,000	4.190%
30 to 55 Years	5,000	4.190%
TOTAL	**13,000**	**4.190%**

Mid-year Economic Update from the Authority's Treasury Management Advisors Arlingclose

External Context

Economic background: The spread of the coronavirus pandemic dominated during the period as countries around the world tried to manage the delicate balancing act of containing transmission of the virus while easing lockdown measures and getting their populations and economies working again. After a relatively quiet few months of Brexit news it was back in the headlines towards the end of the period as agreement between the UK and EU on a trade deal was looking difficult and the government came under fire, both at home and abroad, as it tried to pass the Internal Market Bill which could override the agreed Brexit deal, potentially breaking international law.

The Bank of England (BoE) maintained Bank Rate at 0.1% and its Quantitative Easing programme at £745 billion. The potential use of negative interest rates was not ruled in or out by BoE policymakers, but then a comment in the September Monetary Policy Committee meeting minutes that the central bank was having a harder look at its potential impact than was previously suggested took financial markets by surprise.

Government initiatives continued to support the economy, with the furlough (Coronavirus Job Retention) scheme keeping almost 10 million workers in jobs, grants and loans to businesses and 100 million discounted meals being claimed during the 'Eat Out to Help Out' (EOHO) offer.

GDP growth contracted by a massive 19.8% (revised from first estimate -20.4%) in Q2 2020 (Apr-Jun) according to the Office for National Statistics, pushing the annual growth rate down to -21.5% (first estimate -21.7%). Construction output fell by 35% over the quarter, services output by almost 20% and production by 16%. Recent monthly estimates of GDP have shown growth recovering, with the latest rise of almost 7% in July, but even with the two previous monthly gains this still only makes up half of the lost output.

The headline rate of UK Consumer Price Inflation (CPI) fell to 0.2% year/year in August, further below the Bank of England's 2% target, with the largest downward contribution coming from restaurants and hotels influenced by the EOHO scheme. The Office for National Statistics' preferred measure of CPIH which includes owner-occupied housing was 0.5% y/y.

In the three months to July, labour market data showed the unemployment rate increased from 3.9% to 4.1% while wages fell 1% for total pay in nominal terms (0.2% regular pay) and was down 1.8% in real terms (-0.7% regular pay). Despite only a modest rise in unemployment over the period, the rate is expected to pick up sharply in the coming months as the furlough scheme ends in October. On the back of this, the BoE has forecast unemployment could hit a peak of between 8% and 9%.

The US economy contracted at an annualised rate of 31.7% in Q2 2020 (Apr-Jun). The Federal Reserve maintained the Fed Funds rate at between 0% and 0.25% but announced a change to its inflation targeting regime. The move is to a more flexible form of average targeting which will allow the central bank to maintain interest rates at low levels for an extended period to support the economy even when inflation is 'moderately' above the 2% average target, particularly given it has been below target for most of the last decade.

The European Central Bank maintained its base rate at 0% and deposit rate at -0.5%.

Financial markets: Equity markets continued their recovery, with the Dow Jones climbing to not far off its pre-crisis peak, albeit that performance being driven by a handful of technology stocks

including Apple and Microsoft, with the former up 75% in 2020. The FTSE 100 and 250 have made up around half of their losses at the height of the pandemic in March. Central bank and government stimulus packages continue to support asset prices, but volatility remains.

Ultra-low interest rates and the flight to quality continued, keeping gilts yields low but volatile over the period with the yield on some short-dated UK government bonds remaining negative. The 5-year UK benchmark gilt yield started and ended the June–September period at -0.06% (with much volatility in between). The 10-year gilt yield also bounced around, starting at 0.21% and ending at 0.23% over the same period, while the 20-year rose from 0.56% to 0.74%. 1-month, 3-month and 12-month bid rates averaged 0.02%, 0.06% and 0.23% respectively over the period.

At the end of September, the yield on 2-year US treasuries was around 0.13% while that on 10-year treasuries was 0.69%. German bund yields remain negative across most maturities.

Credit review: Credit default swap spreads eased over most of the period but then started to tick up again through September. In the UK, the spreads between ringfenced and non-ringfenced entities remains, except for retail bank Santander UK whose CDS spread remained elevated and the highest of those we monitor at 85bps while Standard Chartered was the lowest at 41bps. The ringfenced banks are currently trading between 45 and 50bps.

After a busy second quarter of the calendar year, the subsequent period has been relatively quiet for credit changes for the names on our counterparty list. Fitch assigned a AA- deposit rating to Netherlands lender Rabobank with a negative outlook and prior to that, while not related to our counterparty list but quite significant, revised the outlook on the US economy to Negative from Stable while also affirming its AAA rating.

There continues to remain much uncertainty around the extent of the losses banks and building societies will suffer due to the impact from the coronavirus pandemic and for the UK institutions on our list there is the added complication of the end of the Brexit transition period on 31st December and what a trade deal may or may not look like. The institutions on Arlingclose's counterparty list and recommended duration remain under constant review, but at the end of the period no changes had been made to the names on the list or the recommended maximum duration of 35 days.