Appendix A

TREASURY MANAGEMENT INTERIM REPORT 2020/21

INTRODUCTION

1. The CIPFA Code of Practice for Treasury Management in Local Authorities has been adopted by the Authority. The Code requires that Treasury Management activities are subject to reports to Members. This report represents the interim report for 2020/21.

2. For each financial year the Authority sets a balanced budget so that cash income raised during the year is sufficient to meet all of its cash expenditure commitments. One of the key functions of the Authority's treasury management activity is to ensure that these cash flows are effectively managed, so that cash is available when it is needed. Surplus cash is invested having regard to risk, liquidity and yield.

3. A further key function of the treasury management activity is to ensure that the Authority has sufficient funds to pay for its capital and other investment plans. These capital plans, which are set out in the Capital Programme, identify the borrowing needs of the Authority over a longer time horizon than the current year. In managing its longer term cash flow requirements for capital expenditure the Authority will take out loans or alternatively use its cash flow surpluses in lieu of external borrowing. This latter practice is referred to as "internal borrowing". In managing its loans, it may at times be advantageous for the Authority to repay or restructure its borrowings to optimise interest payments or achieve a balanced debt portfolio.

4. Having regard to these activities, the Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as:

   "The management of the Council's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

5. As treasury management decisions involve borrowing and investing substantial sums of money, the Authority is exposed to potentially large financial risks, including the loss of invested funds and the revenue effect of changing interest rates. The identification, control and monitoring of risk are therefore integral elements of treasury management activity.

6. The strategy for the year was identified in the Treasury Management Strategy Statement 2020/21 and was contained within the Budget and Financial Plan report CFO/008/20 approved by the Authority at its meeting on 27th February, 2020. The strategy covered the following areas:

   (a) prospects for interest rates;
   (b) capital borrowing and debt rescheduling;
   (c) annual investment strategy;
   (d) external debt prudential indicators;
   (e) treasury management prudential indicators.
   (f) performance indicators;
   (g) treasury management advisers

7. The Treasury Management Interim Report considers actual treasury management performance up to September 2020.

3. **Executive Summary** of the key points on performance so far include:

- No new borrowing has been arranged in the year or is expected to be arranged.
- Borrowing of £0.45m is due to be repaid in the second half of 2020/21.
- Financial Investments at 30 September 2020 stood at £48.2m, with associated income of £0.104m compared to an annual budget target of £0.172m for the year.
- The Bank of England (BOE) base rate has remained at 0.10% throughout the period.
- Longer term Public Works Loan Board (PWLB) rates have risen slightly during the first half of the year by 0.06% from 2.54% at the start of the year to 2.60 % at 30 September 2020.
- Treasury Management activity for 2020/21 has been carried out in compliance with the relevant codes and statutes and within the borrowing and treasury management limits approved by the Authority as part of the budget setting process.

PROSPECTS FOR INTEREST RATES

3. The medium-term global economic outlook remains weak. The second waves of Covid cases have prompted more restrictive measures on a regional and national basis. This ebb and flow of restrictions on normal activity will continue for the foreseeable future, at least until an effective vaccine is produced and distributed.

The global central bank and government responses have been significant and are in many cases on-going, maintaining more stable financial, economic and social conditions than otherwise might be the case.

The scale of the economic shock to demand, on-going social distancing measures, regional lock downs and reduced fiscal support will mean that the subsequent pace of recovery is limited. Early signs of this are already evident in the UK monthly GDP and PMI data, even before the latest restrictions.

This situation will result in central banks maintaining low interest rates for the medium term. In the UK, Brexit is a further complication. Bank Base Rate is therefore likely to remain at low levels for a very long time, with a distinct possibility of being cut to zero. Money markets have already priced in a chance of a negative Bank Rate.

Longer-term yields will also remain depressed, anchored by low central bank policy rates, expectations of potentially even lower rates and insipid inflation expectations. There is a chance yields may follow a slightly different path in the medium-term, depending on investor perceptions of growth and inflation, or if the UK leaves the EU without a deal.

The Bank of England Base Rate is expected to remain at the current level of 0.10%.
We can expect additional monetary loosening in the future, most likely through further financial asset purchases. Whilst the central case for Bank Rate is no change, further cuts to zero, or perhaps even into negative territory, cannot be completely ruled out.

4. The PWLB certainty rate for borrowing is linked to Gilt yield plus a margin of 1.80%. Gilt yields will remain very low in the medium-term. Shorter term gilt yields are currently negative and will remain around zero or below until either the Bank expressly rules out a negative Bank Rate or growth/inflation prospects improve. PWLB rates for longer term loans have risen slightly by 0.06% during the first half of the financial year. The table below shows the spread of interest rates during the first six months of the year.

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.90%	1.87%	2.11%	2.60%	2.33%
Date	21/09/20	31/7/20	31/7/20	18/6/20	24/4/20
High	2.14%	2.19%	2.39%	3.00%	2.85%
Date	08/4/20	08/4/20	08/4/20	28/8/20	28/8/20
30/9/20	1.96%	1.94%	2.22%	2.76%	2.60%
Average	2.00%	2.00%	2.24%	2.74%	2.53%

(*figures do not include 20bps certainty rate discount)*

CAPITAL BORROWINGS AND DEBT RESCHEDULING

5. The borrowing requirement comprises the expected movements in the Capital Financing Requirement and reserves plus any maturing debt which will need to be re-financed. The Authority does not envisage that any new long term borrowing will be required in 2020/21.

6. Current PWLB lending terms have severely constrained the option to generate savings via debt rescheduling. A significant rise in long term interest rates is required before rescheduling of debt is viable. However, interest rate structures are continually monitored for opportunities to generate savings from debt rescheduling. Any rescheduling that takes place will be reported to Members in monitoring reports.

ANNUAL INVESTMENT STRATEGY

7. The investment strategy for 2020/21 set out the priorities as the security of capital and liquidity of investments. Investments are made in accordance with DCLG Guidance and CIPFA Code of Practice. Investments are made in sterling with an institution on the counterparty list and for a maximum of one-year duration.

8. Investments have been made with various counterparties including UK and foreign banks with higher credit ratings, the larger Building Societies, “nationalised” banks and AAA rated money market funds. This diversity has enabled reasonable returns in a low interest rate environment. In the period 1st April to 30 September 2020 the average rate of return achieved on average principal available was 0.50 %. This compares with an average seven day deposit (7 day libor) rate of 0.08 %.

9. The credit ratings and individual limits for each institution within the categories of investments to be used by the Authority in 2020/21 are as follows:

UK Government (including gilts and the DMADF)	Unlimited
UK Local Authorities (each)	Unlimited
Part Nationalised UK banks	£4m
Money Market Funds (AAA rated)	£3m
Enhanced Money Market (Cash) Funds (AAA rated)	£3m
UK Banks and Building Societies (A- or higher rated)	£2m
Foreign banks registered in the UK (A or higher rated)	£2m

10. The Authority had investments of £48.2m as at 30th September 2020 (this included a £30.1m firefighters' pension grant received in July that will be utilised in the year):

ANALYSIS OF INVESTMENTS END OF QUARTER 2 2020/21

Institution	Credit Rating	MM Fund*	Bank / Other	Building Society	Local Authority	Average Interest
		£	£	£	£	%
Aberdeen Global	AAA	3,000,000				0.70
Federated Investors	AAA	3,000,000				0.69
Fidelity	AAA	3,000,000				0.70
JP Morgan	AAA	3,000,000				0.54
LGIM (Legal & General)	AAA	3,000,000				0.69
Morgan Stanley	AAA	700,000				0.63
Close Brothers	A		2,000,000			0.76
HSBC (MFRS Deposit Account)	A		500,000			0.00
Santander	A		2,000,000			0.58
Coventry BS				1,000,000		0.80
Leeds BS				2,000,000		0.75
Newcastle B Soc				1,000,000		0.75
Nottingham B Soc				2,000,000		0.68
Aberdeen Council					2,000,000	0.58
Blackburn Council					2,000,000	0.63
Blackpool Council					2,000,000	0.61
Broxbourne DC					2,000,000	0.53
Broxtowe BC					2,000,000	0.86
Guildford BC					2,000,000	0.55
Lancashire CC					2,000,000	0.63
PCC Lancashire					2,000,000	0.80
Slough BC					2,000,000	0.79
Tameside MBC					2,000,000	0.71
Thurrock Council					2,000,000	0.86
Totals		**15,700,000**	**4,500,000**	**6,000,000**	**22,000,000**	**0.66**
Total Current Investments					**48,200,000**	

**MM Fund - Money Market Funds -these are funds that spread the risk associated with investments over a wide range of credit worthy institutions.*

EXTERNAL DEBT PRUDENTIAL INDICATORS

10. The external debt indicators of prudence for 2020/21 required by the Prudential Code were set in the strategy as follows:

Authorised limit for external debt: £64 million
Operational boundary for external debt: £58 million

Against these limits, the maximum amount of debt that was reached in the period April to September 2020 was £37.3 million.

TREASURY MANAGEMENT PRUDENTIAL INDICATORS

11. The treasury management indicators of prudence for 2020/21 required by the Prudential Code were set in the strategy as follows:

a) Interest Rate Exposures
Upper limit on fixed interest rate exposures: 100%
Upper limit on variable interest rate exposures: 50%

The maximum that was reached in the period April to September 2020 was as follows:

Upper limit on fixed interest rate exposures: 100%
Upper limit on variable interest rate exposures: 0%

b) Maturity Structure of Borrowing
Upper and lower limits for the maturity structure of borrowing were set and the maximum and minimum that was reached for each limit in the period April to September 2020 was as follows: -

Maturity Period	Upper Limit	Lower Limit	Maximum Actual	Minimum Actual
Under 12 months	50%	0%	1%	0%
12 months and within 24 months	50%	0%	1%	1%
24 months and within 5 years	50%	0%	9%	8%
5 years and within 10 years	50%	0%	0%	0%
10 years and above	95%	0%	90%	90%

c) Total principal sums invested for periods longer than 364 days
The limit for investments of longer than 364 days was set at £2 million for 2020/21. One investment of £2m for 365 days was placed in the first half of 2020/21.

11. PERFORMANCE INDICATORS

The Code of Practice on Treasury Management requires the Authority to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking.

13. The indicators for the treasury function are:

Borrowing – the indicator is the average rate of actual borrowing compared to the average available for the period of borrowing. However, there has been no borrowing in the period April to September 2020.

Investments – Internal returns compared to the 7 day LIBOR rate. The return in the period April to September 2020 was 0.42% above the benchmark.

TREASURY MANAGEMENT ADVISORS

14. The treasury management service is provided to the Authority by Liverpool City Council. The terms of the service are set out in an agreed Service Level Agreement. The Council employs treasury management advisors appointed under a competitive procurement exercise who provide a range of services which include: -

- Technical support on treasury matters, capital finance issues.
- Economic and interest rate analysis.
- Debt services which includes advice on the timing of borrowing.
- Debt rescheduling advice surrounding the existing portfolio.
- Generic investment advice on interest rates, timing and investment instruments.
- Credit ratings/market information service comprising the three main credit rating agencies.

15. Whilst Liverpool City Council and its advisors provide the treasury function, ultimate responsibility for any decision on treasury matters remains with the Authority.

CONCLUSION

16. Treasury Management activity in 2020/21 has been carried out in compliance with the relevant Codes and Statutes and within the borrowing and treasury management limits set by the Authority under the prudential code.