North Devon Council

Report Date: 1st November 2021

Topic: Mid-Year Treasury Management Report 2021/22

Report by: Director of Resources and Deputy Chief Executive

1. Introduction

1.1 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management (revised 2017), and covers the following:

- An economic update for the first part of the 2021/22 financial year (appendix A);
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure and prudential indicators;
- A review of the Council's investment portfolio for 2021/22;
- A review of the Council's borrowing strategy for 2021/22;
- A review of any debt rescheduling undertaken during 2021/22;
- A review of compliance with Treasury and Prudential Limits for 2021/22.

2. Recommendations

The Committee is asked to recommend to full Council that:

2.1 The changes to the prudential indicators be approved.

2.2 The report and the treasury activity be noted.

3. Reasons for Recommendations

3.1 This Council is required through regulations issued under the Local Government Act 2003 to produce a mid year treasury report reviewing treasury management activities and the prudential and treasury indicators for 2021/22. This report meets the requirements of the CIPFA Code of Practice on Treasury Management (revised 2017).

3.2 This Council is also required under the Code to give prior scrutiny to the treasury management reports by the Policy Development Committee before they are reported to the full Council.

4. Report

4.1 Treasury Management Strategy Statement and Annual Investment Strategy update

The Treasury Management Strategy Statement (TMSS) for 2021/22 was approved by this Council on 24th February 2021.

The underlying TMSS approved previously requires revision in the light of economic and operational movements during the year. The proposed changes are set out below:

Prudential Indicator 2021/22	Original Estimate £000	Revised Prudential Indicator £000
Capital Financing Requirement	17,410	23,644
Operational Boundary	14,500	17,500
Maturity Structure of borrowing over 10 years – Upper Limit	90%	95%

Section 4.3 of this report gives further information on the Capital Financial Requirement and the Operational Boundary. The change to the upper borrowing limit over 10 years will allow greater flexibility for long term borrowing.

4.2 The Council's Capital Position (Prudential Indicators)

This part of the report is structured to update:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

Prudential Indicator for Capital Expenditure

This table shows the revised estimates for capital expenditure and the changes since the capital programme was agreed at the budget.

Capital Expenditure by Service	2021/22 Original Estimate £000	Current Position 30/09/21 £000	2021/22 Revised Estimate £000
Chief Executive & Corporate	543	4	614
Corporate & Community	11,319	2,949	10,063
Environmental Health & Housing	2,293	535	2,999
Operational Services	2,588	10	1,052
Place	2,000	131	2,754
Resources	3,677	642	11,547
Total	**22,420**	**4,271**	**29,029**

Changes to the Financing of the Capital Programme

The table below draws together the capital expenditure plans (above), and the expected financing arrangements of this capital expenditure. The borrowing element of the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision).

Capital Expenditure	2021/22 Original Estimate £000	2021/22 Revised Estimate £000
Total capital spend	**22,420**	**29,029**
Financed by:		
Capital receipts	150	500
Capital grants	8,578	7,847
Capital reserves	1,502	1,115
Total financing	**10,230**	**9,462**
Borrowing requirement	**12,190**	**19,567**

4.3 Changes to the Prudential Indicators for the Capital Financing Requirement, External Debt and the Operational Boundary

The table below shows the borrowing requirement (above), the reduction for the Minimum Revenue Provision (MRP) and impact on the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period, which is termed the Operational Boundary.

	2021/22 Original Estimate £000	2021/22 Revised Estimate £000
Prudential Indicator – Capital Financing Requirement		
Borrowing requirement	12,190	19,567
Minimum Revenue Provision	(535)	(514)
Movement in CFR	11,655	19,053
Revised Total CFR	**17,410**	**23,644**
Prudential Indicator – the Operational Boundary for external debt		
Borrowing & Other long term liabilities	14,500	17,500
Total debt (year-end position)	**14,500**	**17,500**

Prudential Indicator – Capital Financing Requirement

The forecast Capital Financing Requirement has increased by circa £6.2m from the original budget. The main reason for this increase is the additional capital budget of £9m for the acquisition of a strategic asset, offset by £1.4m slippage on the new Leisure Centre budget and £1.2m slippage on the Watersports Centre budget. These two budgets have been re-profiled into the 2022/23 capital programme.

Prudential Indicator – the Operational Boundary for external debt

The forecast external borrowing has increased by £3m to support the additional capital spend above. It is projected that the remaining borrowing need can be funded from year end reserves and cash balances (internal borrowing). Section 4.5 looks at the borrowing strategy in more detail.

4.4 Limits to Borrowing Activity

The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. **Gross external borrowing** should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2021/22 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need, which will be adhered to if this proves prudent.

	2021/22 Original Estimate £000	Current Position 30/09/21 £000	2021/22 Revised Estimate £000
Gross borrowing & other long term liabilities	14,500	500	17,500
Total debt	**14,500**	**500**	**17,500**
CFR (year end position)	17,410		23,644

A further prudential indicator controls the overall level of borrowing. This is the **Authorised Limit** that represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Authorised limit for external debt	2021/22 Original Indicator £000	2021/22 Revised Indicator £000
Borrowing & Other long term liabilities	26,500	37,500
Total	26,500	37,500

The Extraordinary Council meeting held on 14th June 2021 approved the increase in the authorised borrowing limit to £37.5m as part of the report detailing the purchase of a strategic asset.

4.5 Borrowing

The Council's forecast capital financing requirement (CFR) for 2021/22 is £23.6m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the Public Works Loan Board (PWLB), or the market (external borrowing), or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions.

At present, the Council has projected total external borrowing of £17.5m and utilising £6.1m of cash flow funds in lieu of borrowing (internal borrowing). This is a prudent and cost effective approach in the current economic climate but will require ongoing monitoring of economic conditions.

At present we have been using internal borrowing from the Council's own cash flows, as this is a low cost financing option and reduces the net interest cost to the Council, but we will continue to monitor our cash position and amend the borrowing position as necessary.

The cash balances have allowed external borrowing to remain at £0.5m as at 30th September. However, with a further £24.7m budgeted capital spend in the second half of the financial year then additional external borrowing will be required. The current forecast is for a further £17m of external borrowing but the exact amount will depend on any capital spend slippages and our cash flow balances towards the financial year end.

The interest rates forecasts are showing that the Bank of England might increase the bank rate shortly and the Finance Team will continue to monitor the impact on the PWLB borrowing rates. The Link Group forecast as at 19th October is shown below:

Link Group Interest Rate View												
	Now	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24
Bank Rate	0.10%	0.10%	0.10%	0.25%	0.25%	0.25%	0.25%	0.50%	0.50%	0.50%	0.75%	-

PWLB Rates 1st April 2021 to 30th September 2021

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	0.78%	1.05%	1.39%	1.75%	1.49%
Date	08/04/2021	08/07/2021	05/08/2021	17/08/2021	10/08/2021
High	0.90%	1.24%	1.80%	2.27%	2.06%
Date	11/08/2021	13/05/2021	13/05/2021	13/05/2021	13/05/2021
Average	0.83%	1.15%	1.59%	2.03%	1.82%
Spread	0.12%	0.19%	0.41%	0.52%	0.57%

4.6 Debt Rescheduling

Debt rescheduling opportunities have been very limited in the current economic climate and following the various increases in the margins added to gilt yields which have impacted PWLB new borrowing rates since October 2010. No debt rescheduling has therefore been undertaken to date in the current financial year.

4.7 Compliance with Treasury and Prudential Limits

It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the half year ended 30th September 2021, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2021/22. The Chief Finance Officer reports that no difficulties are envisaged for the current or future years in complying with these indicators.

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

4.8 Annual Investment Strategy

The Treasury Management Strategy Statement (TMSS) for 2021/22, which includes the Annual Investment Strategy, was approved by the Council on 24th February 2021. In accordance with the CIPFA Treasury Management Code of Practice, it sets out the Council's investment priorities as being:

- Security of capital
- Liquidity
- Yield

The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months with high credit rated financial institutions, using the Link suggested creditworthiness approach.

As shown by the interest rate forecasts in Appendix A, it is now impossible to earn the level of interest rates commonly seen in previous decades as all short-term money market investment rates have only risen weakly since Bank Rate was cut to 0.10% in March 2020. Given this environment and the fact that Bank Rate may only rise marginally, or not at all, before the second half of 2023, investment returns are expected to remain low.

Creditworthiness.

Significant levels of downgrades to Short and Long Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. However, as economies are beginning to reopen, there have been some instances of previous lowering of Outlooks being reversed.

Investment Counterparty criteria

The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function

Investment balances

The Council held £40m of investments as at 30 September 2021 (£22.8m at 31 March 2021) and the investment portfolio yield for the first six months of the year was 0.05% against the benchmark 7 day LIBID of -0.08%.

The Council's budgeted investment return for 2021/22 was £35,000. As at 30th September 2021 £9,375 investment interest was earned in the half-year period. Although investment returns have been low; using the cash flow balances for internal borrowing has reduced the borrowing costs on the expenditure budget.

The cash position includes the residual balance of business support grants due to be repaid to central government shortly, this is currently estimated at circa £16m.

The Chief Financial Officer confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2021/22.

Non-Treasury Management Investments

The PWLB will no longer provide loans for 'debt for yield' projects where financial assets and property are purchased primarily for financial return. This would also mean no PWLB loans for the rest of the capital programme in that year.

The Chief Finance Officer confirms there have been no 'debt for yield' projects included in the current capital programme.

Bank Rate & LIBID rates 1st April 2021 to 30th September 2021

	Bank Rate	7 day	1 mth	3 mth	6 mth	12 mth
High	0.10	-0.08	-0.07	-0.04	-0.01	0.10
High Date	01/04/2021	09/04/2021	06/07/2021	01/04/2021	24/06/2021	27/08/2021
Low	0.10	-0.09	-0.08	-0.06	-0.04	0.03
Low Date	01/04/2021	27/08/2021	26/04/2021	23/08/2021	27/07/2021	16/04/2021
Average	0.10	-0.08	-0.07	-0.05	-0.02	0.05
Spread	0.00	0.01	0.01	0.02	0.03	0.07

5. Resource Implications

5.1 As detailed in the report.

6. Equalities Assessment

6.1 There are not any equalities implications anticipated as a result of this report, as the purpose of this report is to present the Council's financial position only.

7. Constitutional CONTEXT

7.1 Part 4 Financial Procedure Rules (Article 13.8) / Article 4.4

7.2 Delegated power

8. Statement Of Confidentiality

8.1 This report contains no confidential or exempt information under the provisions of Schedule 12A of 1972 Act.

9. Statement Of Internal Advice

9.1 The author (below) confirms that advice has been taken from all appropriate Councillors and Officers.

Jon Triggs, Director of Resources and Deputy Chief Executive