SELBY DISTRICT COUNCIL

TO ACT FOR OTHERS

Report Reference Number: E/21/43

To:	Executive
Date:	3 February 2022
Status:	Non-Key Decision
Ward(s) Affected:	All
Author:	Christopher Chapman, Accountant
Lead Executive Member:	Councillor Cliff Lunn, Lead Member for Finance & Resources
Lead Officer:	Karen Iveson, Chief Finance Officer, S151

Title: **Treasury Management –Quarterly Update Q3 2021/22**

Summary:

This report reviews the Council's borrowing and investment activity (Treasury Management) for the period 1st April to 31st December 2021 (Q3) and presents performance against the Prudential Indicators. As a result of the timing of the report, the figures presented in the current version of the report reflect the expected position as at 31st December based on current quarterly trends, and the document should be read on this basis.

Investments – On average the Council's investments held in the NYCC Investment pool totalled an estimated £79.6m up to the end of the third quarter, at an average rate of 0.20% and earned interest of £114.5k (£77.2k allocated to the General Fund; £37.3k allocated to the HRA) which is £26.4k above the year to date budget. Interest rates on council investments have now stabilised following the initial drop in Bank of England base rate as a result of the Covid-19 pandemic, and for the remainder of the 21/22 financial year the rate of return on investment is currently expected to slowly increase from current levels. In this regard forecast returns could be in the region of £159k, a budget surplus of £41k. The Bank of England voted by a majority of 8-1 to increase the Bank Rate by 0.15 Percentage points, to 0.25% during its December Meeting. The increased rate will take time to filter though to council investments, as existing investments mature and are replaced by those at higher rates.

Cash balances invested over the course of the year have remained higher than was forecast in earlier reports, due to the timing of expenditure on the Capital Programme. The increased balances invested is the main driving factor behind the currently forecast budget surplus.

In addition to investments held in the pool, the Council has £5.06m invested in property funds as at 31st December 2021. The funds have achieved a 3.41% revenue return and 8.06% capital gain over the course of the year. This resulted in revenue income of £124.3k to the end of Q3 and an 'unrealised' capital gain of £374.8k. These funds are long term investments and changes in capital values are realised when the units in the funds are sold.

Borrowing – Long-term borrowing totalled £52.833m at 31st December 2021, (£1.6m relating to the General Fund; £51.233m relating to the HRA). Interest payments of £1.912m are forecast for 2021/22, a saving of £0.015m against budget. The Council had no short-term borrowing in place as at 31st December 2021.

Prudential Indicators – the Council's affordable limits for borrowing were not breached during this period.

Recommendation:

i. That Executive note the actions of officers on the Council's treasury activities for Q3 2021/22 and approve the revised Prudential Indicators set out at Appendix A to the report.

Reasons for recommendation

To comply with the Treasury Management Code of Practice, the Executive is required to receive and review regular treasury management monitoring reports.

1. Introduction and background

1.1 This is the third monitoring report for treasury management in 2021/22 and covers the period 1 April to 31 December 2021. During this period the Council complied with its legislative and regulatory requirements.

1.2 Treasury management in Local Government is governed by the CIPFA "Code of Practice on Treasury Management in the Public Services" and in this context is the management of the Council's cash flows, its banking and its capital market transactions, the effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks. This Council has adopted the Code and complies with its requirements. The Council's Treasury Strategy, including the Annual Investment Strategy and Prudential Indicators was approved by Council on 18 February 2021.

1.3 The two key budgets related to the Council's treasury management activities are the amount of interest earned on investments £118k (£80k General Fund, £38k HRA) and the amount of interest paid on borrowing £1.927m (£75.2k General Fund, £1.852m HRA).

2. The Report

Market Conditions and Interest Rates

2.1 A summary of the key updates provided by the Council's treasury advisors Link Asset Services – Treasury Solutions associated with economic activity in Q3 2021/22 up to 31 December 2021 are provided below**:**

- The emergence of the Omicron Covid variant has formed a key focus, which had caused expectations for a Bank of England Base Rate rise in December's Monetary Policy Committee (MPC) to be cut back accordingly by some observers.
- Despite this however, the MPC voted by an 8-1 majority to increase the Base rate to 0.25% in its 16th December meeting.
- A further rise in Base rate to 0.50% in June 2022 and 0.75% in March 2023 remains forecast, though this remains under review as the impact of the emergence of the Omicron Variant, and the efficacy of existing vaccines, becomes further understood.
- Decembers MPC saw a vote to leave the current Quantitative Easing Programme unchanged
- Bank of England Staff have revised growth estimates for the UK economy for 2022 down from 6% to 5%. It is also forecast that growth is expected to slow sharply to 1.5% in 2023 and 1% in 2024.
- CPI inflation is expected to remain at current levels over the course of the Winter months, peaking at around 5% in April 2022, before falling back materially from the second half of next year. Current forecasts project CPI inflation to be marginally above the 2% target in two years' time, subsequent to possible tightening of monetary policy by the MPC.

Interest Rate Forecasts

2.2 The current interest rate forecasts of Link Asset Services – Treasury Solutions are as follows:

Link Group Interest Rate View 20.12.21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
BANK RATE	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25
3 month ave earnings	0.20	0.30	0.50	0.50	0.60	0.70	0.80	0.90	0.90	1.00	1.00	1.00	1.00	1.00
6 month ave earnings	0.40	0.50	0.60	0.60	0.70	0.80	0.90	1.00	1.00	1.10	1.10	1.10	1.10	1.10
12 month ave earnings	0.70	0.70	0.70	0.70	0.80	0.90	1.00	1.10	1.10	1.20	1.20	1.20	1.20	1.20
5 yr PWLB	1.40	1.50	1.50	1.60	1.60	1.70	1.80	1.80	1.80	1.90	1.90	1.90	2.00	2.00
10 yr PWLB	1.60	1.70	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10	2.20	2.30
25 yr PWLB	1.80	1.90	2.00	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.40	2.40	2.50	2.50
50 yr PWLB	1.50	1.70	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.20	2.20	2.30	2.30

Figures are Net of certainty rate 0.2% discount

2.3 After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, the Monetary Policy Committee had left the rate unchanged at its subsequent meetings, before voting by a majority of 8-1 to increase the rate to 0.25% in its December 2021 meeting. As shown in the forecast table above, a second increase to 0.50% is forecast in June 2022, a third to 0.75% in March 2023, and a fourth to 1.00% in March 2024, and a final rise to 1.25% in March 2025.

<u>Annual Investment Strategy</u>

2.4 The Annual Investment Strategy outlines the Council's investment priorities which are consistent with those recommended by DCLG and CIPFA:

- Security of Capital and
- Liquidity of its investments

2.5 The Investment of cash balances of the Council are managed as part of the investment pool operated by North Yorkshire County Council (NYCC). In order to facilitate this pooling, the Council's Annual Investment strategy and Lending List has been aligned to that of NYCC.

2.6 NYCC continues to invest in only highly credit rated institutions using the Link suggested creditworthiness matrices which take information from all the credit ratings agencies. Officers can confirm that the Council has not breached its approved investment limits during the year.

2.7 The Council's investment activity in the NYCC investment pool up to Q3 2021/22 was as follows:-

- <u>Forecast</u> Balance invested at 30 December 2021 £79.6m
- Average Daily Balance Q3 21/22 £79.6m
- Average Interest Rate Achieved Q3 21/22 0.20%
- Total Interest Budgeted for 2021/22 £118k
- Total Forecast income for 2021/22 £159k

2.8 The average return to Q3 2021/22 of 0.20% compares with the average benchmark returns as follows:

- 7 day -0.08%
- 1 month -0.07%
- 3 months -0.05%
- 6 months -0.02%
- 12 months 0.07%

Borrowing

2.9 It is a statutory duty for the Council to determine and keep under review its “Affordable Borrowing Limits”. The Council’s approved Prudential Indicators (affordable limits) were outlined in the Treasury Management Strategy Statement (TMSS). A list of the limits is shown at Appendix A. Officers can confirm that the Prudential Indicators were not breached during the year.

2.10 The TMSS indicated that there was no requirement to take external borrowing during 2021/22 to support the budgeted capital programme. However, the borrowing requirement is largely dependent on the Housing Development Programme and whilst it is expected that this will be funded by internal borrowing, this will continue to be reviewed to optimise the timing of external debt.

2.11 The Council approved an Authorised Borrowing Limit of £78m (£77m debt and £1m Leases) and an Operational Borrowing Limit of £73m (£72m debt and £1m Leases) for 2021/22.

2.12 The current strategy in relation to capital financing, is to continue the voluntary set aside of Minimum Revenue Provision (MRP) payments from the HRA in relation to self-financing debt, to enable the Council to be in a position to repay the outstanding debt. Following an updating of the HRA business plan, the voluntary set aside of HRA MRP payments has been reprofiled over the life of the existing debt, a change from the original 30 year profiling period. As a result of this update, £1.33m is budgeted for HRA Voluntary MRP for 2021/22.

2.13 The combination of the long-term loan repayment in 2020/21, and the Council’s voluntary MRP strategy, has meant the Council was in an under-borrowed position of £3.6m as at 31 December 2021. This means that capital borrowing (external debt) is currently lower than Council’s underlying need to borrow. Based on current forecasts, and the timing on current year capital spend and adjustments, the council will be in an under borrowed position of £1.1m at year end, which is in line with MTFS indicators.

2.14 The Council’s external borrowing requirements continue to be reviewed on an on-going basis to ensure the borrowing strategy reflects the latest capital programme needs and forecast borrowing rates.

2.15 Plans to undertake any additional long term borrowing in the short/medium term will be kept under review while borrowing rates remain low, as the HRA Extended Housing Delivery Programme will continue to progress.

Capital Strategy

2.16 The Capital Strategy was included as part of the Council’s Annual Treasury Management and Investment Strategy 2021/22, approved in February 2021 and updated in July 2021 as part of a refreshed Medium-Term Financial Strategy. The Capital Strategy sets out how capital expenditure, capital financing and treasury management contribute to the provision of corporate and service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability. It sets out the long-term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward and impact on the achievement of priority outcomes.

2.17 Alternative non-treasury investments are considered as part of the Capital Strategy. Given the technical nature of potential alternative investments and strong linkages to the Council’s Treasury Management function, appropriate governance and decision-making arrangements are needed to ensure robust due diligence in order to make recommendations for implementation. As a result, all investments are subject to consideration and where necessary recommendations of the Executive.

Housing Delivery Programme Loans

2.18 The Housing Delivery Programme has delivered a number of successful schemes so far, in partnership with Selby & District Housing Trust. Whilst no further schemes are planned, existing loans to fund provision of affordable homes in the District continue. The forecast income for the year in addition to standard treasury returns is £118k, which is approximately £112k over the forecasted standard interest that is currently achieved on cash investments.

2.19

Scheme	Loan Rate %	Principal Outstanding 30 December 2021 £	Interest Q3 21/22 £	Interest Full Year £
Kirgate, Tadcaster	4.56%	182,373	6,531	8,708
St Joseph's St	4.20%	198,103	6,390	8,520
Jubliee Close, Ricall	3.55%	536,299	14,120	18,826
Ulleskelf	4.87%	1,049,193	37,921	50,562
Ousegate	3.65%	849,425	23,359	31,146
Average Rate / Total Principal and Interest	**4.19%**	**2,815,394**	**88,321**	**117,762**

Commercial Property Investments

2.20 To date there have been two Commercial Property acquisitions, one in Selby town and one in Tadcaster, both buildings are ex-Natwest Bank Properties. The first acquisition was a Tadcaster property, which completed during Q2 18/19. The second in Selby, which completed towards the end of Q3 18/19 and was subsequently sold in July 2020 generating small surplus of around £10k. Plans for the future of the Tadcaster property are currently being considered.

2.21 **Property Funds**

The position on Property Funds at 31 December 2021 is as follows:

<u>In Year Performance</u>

			In Year Performance Q3 21/22			
Fund	**Bfwd Investment £k**	**Valuation as at 31-Dec-21 £k**	**Capital Gain / (Loss)**		**Revenue Return**	
			£k	**%**	£k	%
Blackrock	2,394.96	2,587.88	192.9	8.05	52.1	2.78
Threadneedle	2,225.82	2,474.28	218.5	9.68	72.1	4.06
Total	**4,650.78**	**5,062.16**	**411.4**	**8.85**	**124.3**	**3.41**

Total Fund Performance

2.22

Fund	Original Investment £k	Valuation as at 31-Dec-21 £k	Total Performance: Capital Gain / (Loss) £k	Total Performance: Capital Gain / (Loss) %	Total Performance: Revenue Return £k	Total Performance: Revenue Return %
Blackrock	2,502.50	2,587.88	85.4	3.41	247.3	3.46
Threadneedle	2,439.24	2,474.28	35.0	1.44	328.2	4.08
Total	**4,941.73**	**5,062.16**	**120.4**	**2.44**	**575.5**	**3.76**

2.23 Investments held in Property Funds are classified as Non-Specified Investments and are, consequently, long term in nature. Valuations can, therefore, fall and rise over the period they are held. Any gains or losses in the capital value of investments are held in an unusable reserve on the balance sheet and do not impact on the General Fund until units in the funds are sold.

The strong performance of the Capital Values of both funds has continued into Q3, with both funds now showing a combined capital gain on their initial purchase price. At the end of Q3 2021/22 the funds have demonstrated a combined capital gain of £411.4k in the year. Both funds have also continued to generate a positive revenue return, amounting to £124.3k for 2021/22 by the end of Q3.

3.0 Alternative Options Considered

3.1 The Council has access to a range of investments through the pooled arrangements in place through North Yorkshire County Council.

4.0 Implications

4.1 Legal Implications

4.1.1 There are no legal implications as a direct result of this report.

4.2 Financial Implications

4.2.1 The financial implications are set out in the report.

5. Conclusion

5.1 The ongoing impact of the pandemic, and the speed and nature of the economic recovery seen, continue to have an impact on the Council's investment returns. An increase in Bank of England base rate in December 2021 has now been announced, though this will take time to filter through to Council investments as existing investments mature and are replaced.

Further rate increases are forecast for 2022, however this position will be kept under review as the impacts of the emergence of the new Omicron Covid variant become better understood.

5.2 The Council's debt position is in line with expectations with no further in year loans to the Selby District Housing Trust, and no expenditure funded by borrowing as part of the capital programme anticipated, as approved under the latest Medium Term Financial Strategy. Opportunities to optimise the Council's debt portfolio will continue to remain under review. As part of this, a reprofiling of the HRA Voluntary MRP provision has taken place as part of the revision of the HRA business plan, with MRP provision now linked to the life of existing debt, as set out in paragraph 2.12.

5.3 The Prudential Indicators are reviewed annually as part of the Treasury Strategy to ensure approved boundaries remain appropriate. The indicators in the Appendix reflect the updated position approved as part of the refreshed MTFS approved in July 2021, as referenced in the Q1 report. The Council operated within approved Strategy Indicators for the quarter, with no breaches on authorised limits

6. Background Documents

None

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Appendices:
Appendix A – Prudential Indicators as at 31 December 2021