Agenda Item 5

Referral from the Executive – Treasury Management Annual Review 2020/21

Agenda Item 5

Falkirk Council

Title:	**Referral from the Executive – Treasury Management Annual Review 2020/21**
Meeting:	**Falkirk Council**
Date:	**29 September 2021**
Submitted by:	**Director of Corporate and Housing Services**

1. Purpose of Report

1.1 This report presents, as an appendix, the Treasury Management Annual Review 2021/21 for consideration. The Executive agreed to refer the report to Council at its meeting on 24 August 2021.

2. Recommendation

2.1 It is recommended that Council notes the Treasury Management Annual Review 2021/21.

3. Consultation

3.1 No consultation was carried out on this report.

4. Implications

Financial

4.1 Any financial implications are set out in the referred report, provided as an appendix.

Resources

4.2 Any resource implications are set out in the referred report, provided as an appendix.

Legal

4.3 Any legal implications are set out in the referred report, provided as an appendix.

Risk

4.4 Any risk implications are set out in the referred report, provided as an appendix.

Equalities

4.5 Any equalities implications are set out in the referred report, provided as an appendix.

Sustainability/Environmental Impact

4.6 No sustainability assessment has been completed as part of compiling the report.

5. Conclusions

5.1 Council is asked to note the Treasury Management Annual Review 2020/21.

Director of Corporate & Housing Services

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Date: 31 August 2021

Appendix 1 - Report to the Executive 'Treasury Management Annual Review 2020/21' – 24 August 2021

List of Background Papers:

No papers were relied on in the preparation of this report in terms of the Local Government (Scotland) Act 1973.

Falkirk Council

Title:	**Treasury Management Annual Review 2020/21**
Meeting:	**Executive**
Date:	**24 August 2021**
Submitted By:	**Director of Corporate & Housing Services**

1. Purpose of Report

1.1. As part of the Treasury Management Code of Practice, reporting requirements include an annual review of the Treasury Management Strategy. This review should be considered by the appropriate Committee and full Council. The purpose of this report is to comply with these requirements.

2. Recommendations

2.1. **The Executive is asked to:**

(1) Note the contents of the Treasury Management Annual Review 2020/21.
(2) Refer the report to Council for consideration.

3. Background

3.1. This report is the final of three Treasury Management reports to Members related to the 2020/21 financial year. The Treasury Management Strategy report for 2020/21 was considered by the Emergency Executive in September 2020 and thereafter approved by Council in September 2020. This was considerably later than usual as a result of the Covid-19 pandemic. An interim Treasury Management report was considered by the Executive and Council in November 2020 and December 2020, respectively. This report to Members provides an annual review of the Treasury Management function for 2020/21.

4. Considerations

4.1 Economic Review

4.1.1 The approved Treasury Management Strategy (TMS) for 2020/21 highlighted the impact of Covid-19 and global efforts to contain the virus. At the time of writing the TMS, the UK was in a recession and the economy had shrunk by 20.4% compared to the first three months of the year. However, by August 2020 the Bank of England Monetary Policy Committee (MPC) had highlighted some positive signs in the economy, with a prolonged, but faster than originally anticipated, recovery expected. The roll out of the vaccination programme has been instrumental in speeding economic recovery. Nonetheless, by the end of March 2021, the UK gross domestic product was 8.7% below pre-pandemic levels.

4.1.2 Bank rates were reduced to 0.10% on 19 March 2020 and have remained at that level since. In June 2021, the MPC left monetary policy unchanged.

4.1.3 Inflation is one of the key factors that the MPC consider when setting the base rate. For example, if inflation is likely to be below the target of 2%, the bank may cut interest rates to lower the cost of borrowing and encourage spending. The 2020/21 TMS stated that inflation was likely to continue to be very low for the year ahead and could turn negative. However, inflation has been increasing significantly. Consumer Price Inflation (CPI) increased by 2.5% year on year in June 2021, the highest level since 2018.

4.1.4 In June 2021 the MPC expected inflation to breach its target level of 2% and potentially push through 3% before reducing back. They reiterate that they view these increases as transitory, linked to activity surges as restrictions relating to Covid are pared back. It is unlikely that action will be taken to raise the bank rate unless it can be clearly seen that inflation is going to be persistently above target. Link Asset Services have therefore advised that the projections previously provided to Members for the bank rate remain valid and that rates are likely to stay at 0.10% for some time yet.

4.1.5 The TMS noted that PWLB rates were expected to stay relatively stable over the next two years to support recovery following the shutdowns arising from the Covid-19 pandemic. This remains the case.

Borrowing Strategy 2020/21 – Outcome

4.1.6 The Council's borrowing requirement for 2020/21 was estimated as part of the three year capital programmes for both General Fund & HRA. Assumptions on 2020/21 borrowing were made in January 2020, taking into account the anticipated approved capital programmes (approved in February 2020), the estimated slippage for 2019/20 and any projects which may be rescheduled to 2020/21. Given that the capital projects are part of a three year plan, there will be movement in spend across the years. Consequently because of the timing of spend, borrowing will also move across the years to match the spend.

4.1.7 The 2020/21 Interim Strategy report to the November 2020 Executive advised Members that the revised borrowing requirement was c£77.6. This figure was revised further to £75.5m in the Capital Programmes Update 2020/21 reported to the Executive on 12 January 2021. The actual borrowing requirement against this revised forecast is as detailed below:

	2020/21 Estimate £'m	**2020/21 Actual £'m**	**2020/21 Variance £'m**
Capital Programme (net of receipts and including TIF)	51.7	37.7	(14.0)
Service Payments	(20.2)	(21.9)	(1.7)
Replacement of Long Term Loans Maturing	4.0	-	(4.0)
Replacement of Short Term Loans Maturing	40.0	41.0	1.0
Total Borrowing Requirement	**75.5**	**56.8**	**18.7**

4.1.8 The borrowing requirement for capital programme purposes, was £14m less than reported to the January Executive. This reduction is analysed below:

		2020/21 Actual £'m
January Executive - Forecast borrowing required for Capital Programme (net of receipts & including TIF)		51.7
Adjustments:		
Slippage General Fund Capital Programme	(15.7)	
Miscellaneous Additional General Fund	2.1	
Slippage Housing Revenue Contribution	(0.2)	
Miscellaneous Additional Housing	(0.4)	
Borrowing for TIF Capital Programme	0.2	
		(14.0)
Actual Borrowing Requirement for Capital Programme (net of receipts & including TIF)		**37.7**

4.1.9 The reduction in borrowing for the capital programme is primarily due to the increase in slippage in the general fund. The requirement to borrow to finance the capital programmes reduced by £14m. In addition, the increase in funding to the Council for Covid-19 etc., improved the cashflow position and as a result, £4m of replacement long term borrowing was not required.

4.1.10 Borrowing of £0.4m was required for the TIF project, meaning that the total TIF debt outstanding at 31 March 2021 was £0.9m. The level of spend and therefore borrowing for TIF is expected to rise significantly over the next three years with spend of £12.4m provisionally expected in 2021/22.

4.1.11 The slippage in the capital programmes is rolled forward to the next year along with the associated borrowing. However, as a result of the Covid-19 pandemic and Brexit, and the associated pressures on prices as well as supply shortages, it is likely that a significant proportion of the planned capital investment will be rescheduled into future years and that borrowing will continue to be lower than anticipated. The anticipated borrowing requirement for 2021/22 was reported to Members in April 2021 as part of the 2021/22 Treasury Management Strategy. The long term borrowing requirement at that time was set at £128.1m. It is anticipated that the actual outturn will be significantly lower than this.

4.1.12 Borrowing undertaken during 2020/21 is as detailed below:

	Short Term £'m	**Long Term £'m**	**Total £'m**
Borrowing at 01/04/20	**40.0**	**238.2**	**278.2**
Maturing in Year	(40.0)	(4.0)	(44.0)
Borrowing in Year	41.0	-	41.0
Borrowing at 31/03/21	**41.0**	**234.2**	**275.2**

4.1.13 As detailed in the table at paragraph 4.1.7, the actual borrowing requirement for 2020/21 was £56.8m, however £41m of borrowing was undertaken as shown in the table above. Previous Strategy reports have noted the Council's under-borrowed position. The level of borrowing undertaken is within the limits approved in the Strategy and remains within the prudential indicator limits approved by Members.

4.1.14 The TMS set out expectations on interest rate changes both for long term and short term debt. When the TMS was approved, the PWLB consultation exercise on future lending terms had completed but the outcome wasn't known. The 2021/22 TMS noted that PWLB rates had reduced by 1% following the review. Before any borrowing is undertaken, the complete range of borrowing period options is considered, and interest rates closely monitored. However, short term loans remained more favourable during 2020/21 and no long term borrowing was undertaken.

4.1.15 The Strategy noted that the Council has £13m of Market Loans which could be repaid during the year should any of the lenders invoke a rate change, albeit the risk of this was assessed as low. As anticipated these rate changes were not made and the Market Loans remain on existing terms. The Market Loans are held with Dexia Credit (£8m) and Just Retirement Ltd; (£5m).

4.1.16 There was no debt rescheduling activity carried out during the year. Due to prevailing premature redemption rates for PWLB, it would cost more to pay off debt earlier than simply continuing to repay the original loan.

4.2 Investment Strategy

4.2.1 Members are reminded that the primary objectives of the Council's investment strategy remain first and foremost to ensure timeous and full repayment of principal and interest, then securing adequate liquidity of funds invested and finally optimising investment returns consistent with those counterparty risks.

4.2.2 Consistent with the requirement of the investment regulations and as part of the Strategy Report, Council approved a list of "Permitted Investments" setting out the types of investments to be used and monetary/time limits applied to each type of investment. There was no change to the counterparty selection criteria nor to the list of eligible counterparties as advised in the annual Strategy Report to Members. However, the TMS for 2021/22 noted that work was underway to open a new deposit account with Handelsbanken, which sits well within our counterparty criteria. This account is now operational.

4.2.3 The Council held £56.6m of investments as at 31 March 2021 of which, £36m was available on instant access from money market funds, £18.1m was available on instance access from two UK Banks and £2.5m was placed with another Local Authority. Previous reports to Members have noted that Local Authorities across Scotland are carrying high levels of cash balances, in part due to additional funding for Covid-19 and in part due to lower than expected expenditure (for example in the capital programme). The Council's cashflow position is forecast regularly during the course of the year and at this stage, it is likely that the Council will draw down deposits over the coming months to meet future Council commitments such as maturing short term debt, salary costs, supplier invoices etc. The Council will potentially move to a borrowing position at the end of the calendar year.

4.3 Treasury Management Prudential Indicators

4.3.1 Financing of the Capital Programme is a key driver of Treasury Management activities. A series of treasury management prudential indicators are included within the TMS. The purpose of the indicators is to contain the activity of the treasury function within specified limits, thereby managing risk and reducing the impact of an adverse movement in interest rates.

4.3.2 The treasury indicators are set out at Appendix 1 and show comparison with the Council's actual exposure as at 31 March 2021. This confirms that the Council's treasury operations were operating well within the set parameters during financial year 2020/21.

4.4 Benchmarking

4.4.1 Whilst Members have recognised that benchmarking information varies across Councils because of the size of capital programmes, grant levels, capital receipts etc. and that as a result there are some limitations to the comparisons that can be made, it was agreed that future Treasury Strategy reports would include some benchmarking information. Appendix 2 therefore provides details of investment balances held by Scottish Local Authorities as at 31 March 2021. The data includes information for 31 out of 32 Scottish Authorities and Falkirk is positioned 17 out of 31, so sitting at the mid/lower end of the table. This is consistent with previous years.

4.5 Banking Contract

4.5.1 The Council's banking contract with the Royal Bank of Scotland started on 1 April 2018. The bank contract is currently working well. During the course of 2020/21, there were one or two occasions where a local branch of the Royal Bank of Scotland had to be closed as a result of Covid. As was common during 2020, there were a number of teething problems with establishing appropriate processes and communications but these largely seem to have been resolved.

4.5.2 There are regular meetings between the Treasury team and the Bank to discuss changes, issues or future developments and the contract will continue to be monitored in this way.

4.6 Treasury Management Advisers

4.6.1 Throughout 2020/21, Link Asset Services provided the Council's treasury management advice. The contract expired on 31 March 2021 and was replaced with a new two year contract, expiring on 31 March 2023.

4.7 Member Training

4.7.1 The Investment Regulations provide for increased scrutiny by Members of treasury management issues. It was expected that training sessions for Members would be scheduled during 2020 but the Covid-19 pandemic impacted on this. A training session has now been scheduled for 17 August 2021 (in advance of this report being considered by Members).

5. Consultation

5.1 There is no requirement to carry out a consultation on this report.

6. Implications

Financial

6.1 The slippage in both the General Fund and Housing Capital Programmes in 2020/21 directly impacted on the Council's need to borrow during the year. As a result, borrowing was £18.7m less than previously forecast and this borrowing requirement will be carried forward.

6.2 The borrowing requirement for 2021/22 will be updated as part of the Capital Programme Projection Report also on this agenda.

Resources

6.3 There are no resources implications arising from the recommendations in this report.

Legal

6.4 There are no legal implications arising from the recommendations in this report.

Risk

6.5 The financial implications section of this report notes the relationship between the capital programmes, slippage and borrowing requirements. The reasons for slippage are, in the main, well understood. However, such large movements do carry risk for the Council's borrowing position. Should slippage continue, resulting in a very large amount of investment happening all in one year, the prevailing interest rates at that time become critical. As projects slip there is more risk that borrowing is undertaken at a higher rate than originally anticipated. Fortunately, at this stage, it is anticipated that interest rates will continue to be low for some time. Nevertheless, Members should be aware of the risk in this area.

6.6 There is a risk that the cost of those projects which have slipped or been rescheduled may increase in future years because of construction inflation and associated Covid-19 costs. This would also have the potential to impact on the amount of borrowing required.

6.7 Across Scotland Local Authorities are holding large cash balances. This can make it difficult to find appropriate counterparties and remain within deposit limits. The Treasury section have increased the number of counterparties in place to try and mitigate this risk. In addition, increases to deposit limits were also approved by Council.

Equalities

6.8 An equality and poverty impact assessment is not required.

Sustainability/Environmental Impact

1.9 A sustainability/environmental assessment is not required.

7. Conclusions

7.1 Treasury objectives consistent with the 2020/21 Treasury Management Strategy and Interim Strategy Review report, have been met for both borrowing and investment.

7.2 The uncertainties in the economy remain, and whilst expectations remain of low interest rates, inflation is increasing rapidly. It is expected that this increase will be temporary and therefore that interest rates will not be revised as a result.

7.3 The continuing slippage in the Capital Programmes impacts on the Council's need to borrow, with the Council borrowing significantly less in 2020/21 than forecast.

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Director of Corporate & Housing Services

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Appendices
Appendix 1 – Treasury Management Prudential Indicators
Appendix 2 – Investment Levels at 31 March 2021

List of Background Papers:
None

APPENDIX 1

TREASURY MANAGEMENT PRUDENTIAL INDICATORS

1. INTEREST RATE EXPOSURE

Changes in the Prudential Code no longer require Local Authorities to set indicators for interest rate exposure. A commentary on interest rates is included in section 4 of this report.

2. MATURITY STRUCTURE ON FIXED INTEREST RATE BORROWING 2020/21

These gross limits are set to control the Council's level of exposure to loans expiring in any one period.

	Lower %	Upper %	Position (31/03/21) %
Under 12 months	0	35	13.8
12 months – 2 years	0	20	5.8
2 years – 5 years	0	20	7.9
5 years – 10 years	0	30	22.5
10 years – 20 years	0	30	8.5
20 years – 30 years	0	30	10.9
30 years – 40 years	0	30	20.1
40 years – 50 years	0	40	10.5
			100.0%

3. PRINCIPAL SUM INVESTED > 364 DAYS

The Council does not place investments for periods longer than 364 days.

Summary of Scottish Local Authoristy Total Investments Outstanding as at 31 March 2021

APPENDIX 2

By Council	Total Sum Investment
Misc 1	£530,917,235.60
Misc 4	£274,362,700.00
Misc 9	£236,666,511.11
Misc 3	£187,720,000.00
Misc 2	£171,099,989.15
Misc 7	£140,020,000.00
Misc 28	£131,272,342.75
Misc 27	£127,220,310.35
Misc 16	£118,351,444.95
Misc 8	£112,200,000.00
Misc 11	£105,308,000.00
Misc 5	£85,110,000.00
Misc 14	£81,367,342.10
Misc 10	£73,947,319.00
Misc 12	£71,680,000.00
Misc 17	£63,607,155.00
Misc 18	£56,575,454.63
Misc 29	£48,572,957.83
Misc 21	£42,392,341.15
Misc 20	£42,250,000.00
Misc 22	£39,950,000.00
Misc 13	£39,905,731.60
Misc 6	£35,447,525.26
Misc 15	£34,981,578.25
Misc 25	£32,120,000.00
Misc 30	£30,630,782.85
Misc 23	£29,874,080.60
Misc 31	£27,000,000.00
Misc 32	£22,700,000.00
Misc 19	£17,475,046.00
Misc 24	£9,100,000.00
Misc 26	£0.00
	£3,019,825,848.18