

CABINET – 14TH JANUARY 2021

Report of the Head of Financial Services

Lead Member: Councillor Tom Barkley

Part A

ITEM 7 TREASURY MANAGEMENT UPDATE–MID-YEAR REVIEW FOR THE 6 MONTHS ENDED 22ND DECEMBER 2020

Purpose of Report

This report reviews the Treasury Management Strategy and the Annual Investment Strategy, plus the various Prudential Borrowing and Treasury Indicators for the first six months of 2020/21.

Recommendation

That it be recommended to Council to note this mid-year review of the Treasury Management Strategy Statement, Prudential Borrowing and Treasury Indicators plus the Annual Investment Strategy, as set out in Part B.

Reason

To ensure that the Council's governance and management procedures for Treasury Management reflect best practice and comply with the Revised CIPFA Treasury Management in the Public Services Code of Practice, Guidance Notes and Treasury Management Policy Statement, that funding of capital expenditure is taken within the totality of the Council's financial position, and that borrowing and Investment is only carried out with proper regard to the Prudential Code for Capital Finance in Local Authorities.

Policy Justification and Previous Decisions

The Capital Strategy including the Treasury Management Strategy, Annual Investment Strategy and Minimum Revenue Provision Policy, Prudential & Treasury Indicators must be approved by Council each year and reviewed half yearly. This review is set out in the attached report as Part B. The Strategy for the year was approved by Council on 9th November 2020.

Implementation Timetable including Future Decisions and Scrutiny

This report will be presented to Cabinet on 14th January 2021 for onward recommendation to the full Council meeting of 18th January 2021.

The report is available for scrutiny by the Scrutiny Commission at the regular meeting scheduled for 11th January 2021.

Report Implications

The following implications have been identified for this report.

Financial Implications

There are no direct financial implications arising from this report.

Risk Management

There are no direct risks arising from the recommendation in this report. Risks associated with the Treasury Policy, etc and in general are set out within Part B.

Key Decision: No

Background Papers: None

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1. Background

1.1 Capital Strategy

In December 2017, the Chartered Institute of Public Finance and Accountancy, (CIPFA), issued revised Prudential and Treasury Management Codes. As from 2019/20, all local authorities have been required to prepare a Capital Strategy which is to provide the following: -

a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services;

an overview of how the associated risk is managed;

the implications for future financial sustainability.

1.2 Treasury Management

The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering optimising investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer-term cash may involve arranging long or short-term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

Accordingly, treasury management is defined as:

“The management of the local authority's borrowing, 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

1.3 Regulatory framework

This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2017).

The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

3. Receipt by the full council of an annual Treasury Management Strategy Statement

- including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report, (stewardship report), covering activities during the previous year.

4. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

5. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is Audit Committee:

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

- An economic update for the first part of the 2020/21 financial year;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure, as set out in the Capital Strategy, and prudential indicators;
- A review of the Council's investment portfolio for 2020/21;
- A review of the Council's borrowing strategy for 2020/21;
- A review of any debt rescheduling undertaken during 2020/21;
- A review of compliance with Treasury and Prudential Limits for 2020/21.

2. Economics and Interest Rates

2.1 Economics update

As expected, the Bank of England's Monetary Policy Committee kept Bank Rate unchanged on 6th August. It also kept unchanged the level of quantitative easing at £745bn. Its forecasts were optimistic in terms of three areas:

- The fall in **GDP** in the first half of 2020 was revised from 28% to 23% (subsequently revised to -21.8%). This is still one of the largest falls in output of any developed nation. However, it is only to be expected as the UK economy is heavily skewed towards consumer-facing services – an area which was particularly vulnerable to being damaged by lockdown.
- The peak in the **unemployment rate** was revised down from 9% in Q2 to 7½% by Q4 2020.
- It forecast that there would be excess demand in the economy by Q3 2022 causing CPI **inflation** to rise above the 2% target in Q3 2022, (based on market interest rate expectations for a further loosening in policy). Nevertheless, even if the Bank were to leave policy unchanged, inflation was still projected to be above 2% in 2023.

It also squashed any idea of using **negative interest rates**, at least in the next six months or so. It suggested that while negative rates can work in some circumstances, it would be “less effective as a tool to stimulate the economy” at this time when banks are worried about future loan losses. It also has “other instruments available”, including QE and the use of forward guidance.

The MPC expected the £300bn of **quantitative easing** purchases announced between its March and June meetings to continue until the “turn of the year”. This implies that the pace of purchases will slow further to about £4bn a week, down from £14bn a week at the height of the crisis and £7bn more recently.

In conclusion, this would indicate that the Bank could now just sit on its hands as the economy was recovering better than expected. However, the MPC acknowledged that the “medium-term projections were a less informative guide than usual” and the minutes had multiple references to **downside risks**, which were judged to persist both in the short and medium term. One has only to look at the way in which second waves of the virus are now impacting many countries including Britain, to see the dangers. However, rather than a national lockdown, as in March, any spikes in virus infections are now likely to be dealt with by localised measures and this should limit the amount of economic damage caused. In addition, Brexit uncertainties ahead of the year-end deadline are likely to be a drag on recovery. The wind down of the initial generous furlough scheme through to the end of October is another development that could cause the Bank to review the need for more support for the economy later in the year. Admittedly, the Chancellor announced in late September a second six month package from 1st November of government support for jobs whereby it will pay up to 22% of the costs of retaining an employee working a minimum of one third of their normal hours. There was further help for the self-employed, freelancers and the hospitality industry. However, this is a much less generous scheme than the furlough package and will inevitably mean there will be further job losses from the 11% of the workforce still on furlough in mid September.

Overall, **the pace of recovery** is not expected to be in the form of a rapid V shape, but a more elongated and prolonged one after a sharp recovery in June through to August which left the economy 11.7% smaller than in February. The last three months of 2020 are now likely to show no growth as consumers will probably remain cautious in spending and uncertainty over the outcome of the UK/EU trade negotiations concluding at the end of the year will also be a headwind. If the Bank felt it did need to provide further support to recovery, then it is likely that the tool of choice would be more QE.

There will be some **painful longer term adjustments** as e.g. office space and travel by planes, trains and buses may not recover to their previous level of use for several years, or possibly ever. There is also likely to be a reversal of globalisation as this crisis has shown up how vulnerable long-distance supply chains are. On the other hand, digital services is one area that has already seen huge growth.

One key addition to **the Bank's forward guidance** was a new phrase in the policy statement, namely that "it does not intend to tighten monetary policy until there is clear evidence that significant progress is being made in eliminating spare capacity and achieving the 2% target sustainably". That seems designed to say, in effect, that even if inflation rises to 2% in a couple of years' time, do not expect any action from the MPC to raise Bank Rate – until they can clearly see that level of inflation is going to be persistently above target if it takes no action to raise Bank Rate

The **Financial Policy Committee** (FPC) report on 6th August revised down their expected credit losses for the banking sector to "somewhat less than £80bn". It stated that in its assessment "banks have buffers of capital more than sufficient to absorb the losses that are likely to arise under the MPC's central projection". The FPC stated that for real stress in the sector, the economic output would need to be twice as bad as the MPC's projection, with unemployment rising to above 15%.

US. The incoming sets of data during the first week of August were almost universally stronger than expected. With the number of new daily coronavirus infections beginning to abate, recovery from its contraction this year of 10.2% should continue over the coming months and employment growth should also pick up again. However, growth will be dampened by continuing outbreaks of the virus in some states leading to fresh localised restrictions. At its end of August meeting, the Fed tweaked **its inflation target** from 2% to maintaining an average of 2% over an unspecified time period i.e. following periods when inflation has been running persistently below 2%, appropriate monetary policy will likely aim to achieve inflation moderately above 2% for some time. This change is aimed to provide more stimulus for economic growth and higher levels of employment and to avoid the danger of getting caught in a deflationary "trap" like Japan. It is to be noted that inflation has actually been under-shooting the 2% target significantly for most of the last decade so financial markets took note that higher levels of inflation are likely to be in the pipeline; long term bond yields duly rose after the meeting. The Fed also called on Congress to end its political disagreement over providing more support for the unemployed as there is a limit to what monetary policy can do compared to more directed central government fiscal policy. The FOMC's updated economic and rate projections in mid-September showed that officials expect to leave the fed funds rate at near-zero until at least end-2023 and probably for another year or two beyond that. There is now some expectation that where the Fed has led in changing its inflation target, other major central banks will follow. The increase in

tension over the last year between the US and China is likely to lead to a lack of momentum in progressing the initial positive moves to agree a phase one trade deal.

EU. The economy was recovering well towards the end of Q2 after a sharp drop in GDP, (e.g. France 18.9%, Italy 17.6%). However, the second wave of the virus affecting some countries could cause a significant slowdown in the pace of recovery, especially in countries more dependent on tourism. The fiscal support package, eventually agreed by the EU after prolonged disagreement between various countries, is unlikely to provide significant support and quickly enough to make an appreciable difference in weaker countries. The ECB has been struggling to get inflation up to its 2% target and it is therefore expected that it will have to provide more monetary policy support through more quantitative easing purchases of bonds in the absence of sufficient fiscal support.

China. After a concerted effort to get on top of the virus outbreak in Q1, economic recovery was strong in Q2 and has enabled it to recover all of the contraction in Q1. However, this was achieved by major central government funding of yet more infrastructure spending. After years of growth having been focused on this same area, any further spending in this area is likely to lead to increasingly weaker economic returns. This could, therefore, lead to a further misallocation of resources which will weigh on growth in future years.

Japan. There are some concerns that a second wave of the virus is gaining momentum and could dampen economic recovery from its contraction of 8.5% in GDP. It has been struggling to get out of a deflation trap for many years and to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy. The resignation of Prime Minister Abe is not expected to result in any significant change in economic policy.

World growth. Latin America and India are currently hotspots for virus infections. World growth will be in recession this year. Inflation is unlikely to be a problem for some years due to the creation of excess production capacity and depressed demand caused by the coronavirus crisis.

2.2 Interest rate forecasts

The Council's treasury advisor, Link Group, provided the following forecasts on 11th August 2020 (PWLB rates are certainty rates, gilt yields plus 180bps):

Link Group Interest Rate View 11.8.20										
	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month average earnings	0.05	0.05	0.05	0.05	0.05	-	-	-	-	-
6 month average earnings	0.10	0.10	0.10	0.10	0.10	-	-	-	-	-
12 month average earnings	0.15	0.15	0.15	0.15	0.15	-	-	-	-	-
5yr PWLB Rate	1.90	2.00	2.00	2.00	2.00	2.00	2.10	2.10	2.10	2.10
10yr PWLB Rate	2.10	2.10	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.30
25yr PWLB Rate	2.50	2.50	2.50	2.60	2.60	2.60	2.70	2.70	2.70	2.70
50yr PWLB Rate	2.30	2.30	2.30	2.40	2.40	2.40	2.50	2.50	2.50	2.50

The coronavirus outbreak has done huge economic damage to the UK and economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its meeting on 6th August (and the subsequent September meeting), although some forecasters had suggested that a cut into negative territory could happen. However, the Governor of the Bank of England has made it clear that he currently thinks that such a move would do more damage than good and that more quantitative easing is the favoured tool if further action becomes necessary. As shown in the forecast table above, no increase in Bank Rate is expected within the forecast horizon ending on 31st March 2023 as economic recovery is expected to be only gradual and, therefore, prolonged.

GILT YIELDS / PWLB RATES. There was much speculation during the second half of 2019 that bond markets were in a bubble which was driving bond prices up and yields down to historically very low levels. The context for that was heightened expectations that the US could have been heading for a recession in 2020. In addition, there were growing expectations of a downturn in world economic growth, especially due to fears around the impact of the trade war between the US and China, together with inflation generally at low levels in most countries and expected to remain subdued. Combined, these conditions were conducive to very low bond yields. While inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation expectations, the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers. This means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. The consequence of this has been the gradual lowering of the overall level of interest rates and bond yields in financial markets over the last 30 years. Over the year prior to the coronavirus crisis, this has seen many bond yields up to 10 years turn negative in the Eurozone. In addition, there has, at times, been an inversion of bond yields in the US whereby 10 year yields have fallen below shorter term yields. In the past, this has been a precursor of a recession. The other side of this coin is that bond prices are elevated as investors would be expected to be moving out of riskier assets i.e. shares, in anticipation of a downturn in corporate earnings and so selling out of equities.

Gilt yields had therefore already been on a generally falling trend up until the coronavirus crisis hit western economies during March. After gilt yields spiked up during the initial phases of the health crisis in March, we have seen these yields fall sharply to

unprecedented lows as major western central banks took rapid action to deal with excessive stress in financial markets, and started massive quantitative easing purchases of government bonds: this also acted to put downward pressure on government bond yields at a time when there has been a huge and quick expansion of government expenditure financed by issuing government bonds. Such unprecedented levels of issuance in “normal” times would have caused bond yields to rise sharply. At the close of the day on 30th September, all gilt yields from 1 to 6 years were in negative territory, while even 25-year yields were at only 0.76% and 50 year at 0.60%.

From the local authority borrowing perspective, HM Treasury imposed **two changes of margins over gilt yields for PWLB rates** in 2019-20 without any prior warning. The first took place on 9th October 2019, adding an additional 1% margin over gilts to all PWLB period rates. That increase was then at least partially reversed for some forms of borrowing on 11th March 2020, but not for mainstream General Fund capital schemes, at the same time as the Government announced in the Budget a programme of increased infrastructure expenditure. It is now clear that HM Treasury will no longer allow local authorities to borrow money from the PWLB to purchase commercial property if the aim is solely to generate an income stream (assets for yield).

The balance of risks to the UK

- The overall balance of risks to economic growth in the UK is probably relatively even, but is subject to major uncertainty due to the virus.
- There is relatively little UK domestic risk of increases or decreases in Bank Rate and significant changes in shorter term PWLB rates. The Bank of England has effectively ruled out the use of negative interest rates in the near term and increases in Bank Rate are likely to be some years away given the underlying economic expectations. However, it is always possible that safe haven flows, due to unexpected domestic developments and those in other major economies, could impact gilt yields, (and so PWLB rates), in the UK.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- **UK** - second nationwide wave of virus infections requiring a national lockdown
- **UK / EU trade negotiations** – if it were to cause significant economic disruption and a fresh major downturn in the rate of growth.
- **UK - Bank of England** takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- A resurgence of the **Eurozone sovereign debt crisis**. The ECB has taken monetary policy action to support the bonds of EU states, with the positive impact most likely for “weaker” countries. In addition, the EU recently agreed a €750bn fiscal support package. These actions will help shield weaker economic regions for the next year or so. However, in the case of Italy, the cost of the virus crisis has added to its already huge debt mountain and its slow economic growth will leave it vulnerable to markets returning to taking the view that its level of debt is unsupportable. There remains a sharp divide between northern EU countries favouring low debt to GDP and annual balanced budgets and southern countries

who want to see jointly issued Eurobonds to finance economic recovery. This divide could undermine the unity of the EU in time to come.

- Weak capitalisation of some **European banks**, which could be undermined further depending on extent of credit losses resultant of the pandemic.
- **German minority government & general election in 2021.** In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. The CDU has done badly in subsequent state elections but the SPD has done particularly badly. Angela Merkel has stepped down from being the CDU party leader but she intends to remain as Chancellor until the general election in 2021. This then leaves a major question mark over who will be the major guiding hand and driver of EU unity when she steps down.
- **Other minority EU governments.** Austria, Sweden, Spain, Portugal, Netherlands, Ireland and Belgium also have vulnerable minority governments dependent on coalitions which could prove fragile.
- **Austria, the Czech Republic, Poland and Hungary** now form a strongly anti-immigration bloc within the EU. There has also been a rise in anti-immigration sentiment in Germany and France.
- **Geopolitical risks**, for example in China, Iran or North Korea, but also in Europe and other Middle Eastern countries, which could lead to increasing safe haven flows.
- **US – the Presidential election in 2020:** this could have repercussions for the US economy and SINO-US trade relations.

Upside risks to current forecasts for UK gilt yields and PWLB rates

- **UK** - stronger than currently expected recovery in UK economy.
- **Post-Brexit** – if an agreement was reached that removed the majority of threats of economic disruption between the EU and the UK.
- The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect

3. Treasury Management Strategy Statement and Annual Investment Strategy

Update

The Treasury Management Strategy Statement, (TMSS), for 2020/21 was approved by this Council on 9th November 2020. There are no changes in this report to the TMSS since 9th November Council in the light of economic and operational movements during the year.

To note the current Operational Boundary borrowing limits and the Authorised limits are part of the prudential guidelines and these remain as they were previously reported.

The Operational Boundary is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be similar to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under borrowing by other cash resources.

Operational Boundary Limits	2019/20 Actual £'000	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000
Debt	81,190	81,190	81,190	8,190
Commercial Activities	0	47,400	57,400	57,400
Total	81,190	128,590	138,590	138,590

A further prudential indicator controls the overall level of borrowing. This is **the Authorised Limit** which 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 Limits	2019/20 Actual £'000	2020/21 Estimate £'000	2021/22 Estimate £'000	2022/23 Estimate £'000
Debt	96,000	96,000	96,000	96,000
Commercial Activities	0	47,400	57,400	57,400
Total	96,000	143,400	153,400	153,400

4. 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.

4.1 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	2020/21 current Budget £m	Actual Spend 13/11/2020 £m	Variance underspend/ (overspend) £m
General Fund	12,395	4,668	7,727
Commercial Investments	25,000	10,673	14,327
Enterprise Zone	15,000	0	0
Regeneration	5,000	0	0
HRA	8,941	798	8,143
Total capital expenditure	66,336	16,139	50,197

1. The Actual Capital spend is slow for the first half of the year primarily due to Covid. The Capital Plan update report provides details of each scheme and was presented to Cabinet at the meeting of 10th December 2020.
2. Current year spend on Investment in Commercial Property is £10.7m. Three properties have been purchased to date:- 14/14A Market Street, Loughborough (previously Crawshaws Butchers), Belton Road, Loughborough (Car Showroom) and 1 Brookhill Way, Banbury. The purchase of these properties will generate revenue income, support the Medium Term Financial Strategy, thereby protecting the delivery of services to Charnwood's residents.

4.2 Financing of the Capital Programme

The table below draws together the main strategy elements of the capital expenditure plans (above), highlighting the original supported and unsupported elements of the capital programme, 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). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

<i>Financing of capital expenditure</i>	<i>2019/20 Actual £'000</i>	<i>2020/21 Revised Estimate £'000</i>
Total Capital Expenditure as per above table	10,444	66,336
<i>Financed by:</i>		
Capital receipts	1,120	5,942
Capital grants/S106	857	3,875
Capital reserves	4,595	662
Revenue Contributions	3,872	8,207
NHS Funding	0	250
Internal /External borrowing	0	47,400
Total Funding	10,444	66,336

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

The table below shows 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.

Prudential Indicator – Capital Financing Requirement

We are on target to achieve the original forecast Capital Financing Requirement.

Prudential Indicator – the Operational Boundary for external debt

<i>Capital Financing Requirement</i>	<i>2019/20 Actual £'000</i>	<i>2020/21 Revised Estimate £'000</i>
CFR - Fleet	0	2,400
CFR – Commercial Activities	0	25,000
CFR – Regeneration	0	5,000
CFR – Enterprise Zone	0	15,000
CFR – HRA	81,820	81,820
Total CFR	81,820	129,220
Movement in CFR represented by:		
Net financing need for the year	0	47,400
Less MRP/VRP and other financing movements	0	0
Movement in CFR	0	47,400

There is no MRP charged in 2020/21 as the current MRP policy is that a full years MRP will be made in the year after capital expenditure has incurred and when the assets are fully operational. MRP however will be charged from 2021/22 based on the assets purchased in 2020/21.

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 2020/21 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.

	<i>2019/20 Actual £'000</i>	<i>2020/21 Estimate £'000</i>	<i>2020/21 Actual £'000</i>
External Debt at 1 April	81,190	81,190	81,190
Expected change in Debt	0	47,400	0
Actual debt at 31 March	81,190	128,590	81,190
Capital Financing Requirement	81,820	129,220	81,820
Under/(over) borrowing	630	630	630

The Head of Finance & Property Services reports that no difficulties are envisaged for the current or future years in complying with this prudential indicator.

A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which 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	2020/21 Estimate £'000	2020/21 Actual £'000
External Debt Borrowing	96,000	81,190
Commercial Activities	47,400	0
Total	143,400	81,190

5. Investment Portfolio 2020/21

In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. As shown by forecasts in section 2.2, it is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low and in line with the current 0.10% Bank Rate. The continuing potential for a re-emergence of a Eurozone sovereign debt crisis, and its impact on banks, prompts a low risk and short-term strategy. Given this risk environment and the fact that increases in Bank Rate are likely to be gradual and unlikely to return to the levels seen in previous decades, investment returns are likely to remain low

The average level of funds available for investment purpose during the first half year was £50m. Internal investments as at 30th September 2020 and the investment portfolio yield for the first 6 months of the year is 0.53% against a benchmark of 3 months London interbank Bid Rate (LIBID) of 0.11 %. Although the rate of return is low, our performance can still to be reasonable as we have exceeded the target rate.

The interest & rental income earned by the Council's £5m External Property Funds' investments as at 30th September 2020 is £99k, net 1.61%. (£91k 2019/20) This is a good net rate of return in comparison to internal investments 0.53% and LIBID 0.11%.

The Head of Finance & Property Services confirms that the approved limits within the Annual Investment Strategy were not breached during the first 6 months of 2020/21.

The Council's revised budgeted annual investment return for 2020/21 is £300k, and performance for the year to date is £234k including Property Funds. The Council performed above target in both percentage and actual returns to date and should perform above the budget set 2020/21.

6. Borrowing

The Council's capital financing requirement (CFR) for 2020/21 is £129,220m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the 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; however, Table 4.4 shows the Council has actual borrowings of £81,190m, this is £2m of an external loan which matures in 2024 and £79,190 HRA Debt.

It is anticipated that further borrowing will not be undertaken during this financial year.

Due to the overall financial position and the underlying need to borrow for capital purposes (the CFR), no new external borrowing has been undertaken. However, due to the increase in PWLB margins over gilt yields in October 2019, and the subsequent consultation on these margins by HM Treasury - which ended on 31st July 2020 - the Authority has refrained from undertaking new long-term PWLB borrowing for the present and has met its requirements for additional borrowing by using short-term borrowing until such time as new PWLB margins are finally determined. In addition, the effect of coronavirus on the capital programme objectives are being assessed. Therefore, our borrowing strategy will be reviewed and then revised in order to achieve optimum value and risk exposure in the long-term.

7. Debt Rescheduling

Debt rescheduling opportunities have been very limited in the current economic climate given the consequent structure of interest rates and following the increase in the margin added to gilt yields which has impacted PWLB new borrowing rates since October 2010. No debt rescheduling has therefore been undertaken to date in the current financial year.

No new external borrowing was undertaken during the half year, the council however has plans to review its internal borrowing and external borrowing position in light of the updated Capital Strategy Report Strategy Cabinet Report of 15th October 2020 and the recent PWLB announcement to close PWLB borrowing for investments in Commercial Properties.

Appendices

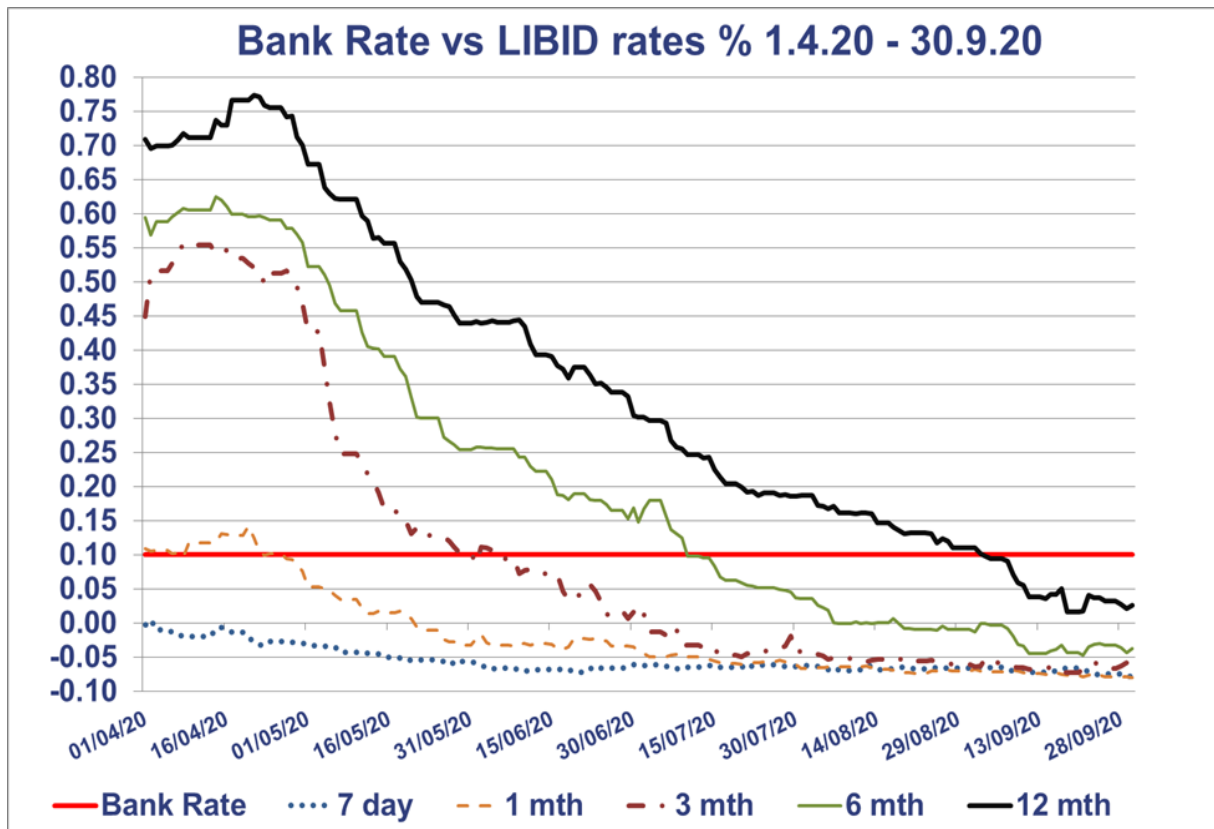
Appendix 1: Portfolio of investments as at 30th September 2020

Appendix 2: Approved countries for investments as at 30th September 2020

Appendix 3: Glossary of Terms

APPENDIX 1: Investment Portfolio
Investments held as at 30 September 2020

Institution	Maturity Date	Interest	
		Rate %	Principal £'000
Wyre Forest District Council	09/10/2020	1.40	2,000
Liverpool City Council	14/10/2020	1.00	2,000
Slough Borough Council	01/04/2021	0.96	2,000
HSBC - Evergreen	3 Month Notice	0.91	5,000
HSBC	31 Day Notice	0.25	7,000
Santander	180 Day Notice	1.00	8,000
Goldman Sachs International Bank	95 Day Notice	0.71	2,500
Goldman Sachs International Bank	35 Day Notice	0.17	2,500
Federated Money Market Fund	1 Day Notice	0.23	8,080
Standard Chartered Bank	91 Day Notice	0.11	5,000
Aberdeen Money Market Fund	1 Day Notice	0.19	10,000
Insight Money Market Fund	1 Day Notice	0.10	1,350
Lothbury Property Fund			2,500
Hermes Property Fund			2,500
Total			60,430



APPENDIX 2: Approved countries for investments as at 30th September 2020

AAA

- Australia
- Denmark
- Germany
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Canada
- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)
- France

AA-

- Belgium
- Hong Kong
- Qatar
- **U.K.**

APPENDIX 3: Glossary of Terms

Capital Financing Requirement

CFR 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.

The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of expenditure above, which has not immediately been paid for, will increase the CFR. The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each assets life, and so charges the economic consumption of capital assets as they are used.

Operational Boundary

The operational boundary is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

Authorised Limit for External Debt

A further key prudential indicator represents a control on the maximum level of borrowing. This is the Authorised Limit which 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.

Gross External Debt

This is the total amount borrowed by the Council at a point in time.

Investments

The budgeted figure is the estimated average funds available for investment during the year. The actual figure is the total amount invested as at 30th September for Internal and Property Funds .

Net Borrowing

Net borrowing is gross external debt less investments.

Loans

In this mid-year (and previously) interest receivable has exceeded interest payable for the General Fund producing a negative number for net interest payable and a somewhat odd-looking negative ratio; this can be construed as indicating that the Council has no issues servicing General Fund loans at this time.