SURREY
COUNTY COUNCIL

Audit & Governance Committee
26 November 2020

TREASURY MANAGEMENT MID YEAR REPORT 2020/21

Purpose of the report:

This report summarises the council's treasury management activity during the first half of 20202/21, as required to ensure compliance with CIPFA's Code of Practice for Treasury Management

Recommendations:

The Audit & Governance Committee is asked to note the content of the Treasury Management Mid Year Report for 2020/21

Introduction:

1. The Authority has adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in Public Services: Code of Practice (the CIPFA Code) which requires the authority to approve treasury management semi-annual and annual reports

2. The Authority's Treasury Management Strategy Statement for 2020/21 was approved at the County Council meeting on 4 February 2020. The investment and borrowing of cash exposes the Council to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's treasury management strategy.

External Context

3. Annex 1 contains commentary on the economic backdrop for 2020/21. The economic position is weakened by the impact of the CV-19 pandemic. The impact on Treasury Management activities is relatively limited as it has resulted in very low interest rates (forecast to continue over the medium-term) which support our strategy of minimising cash balances and meeting our borrowing requirement with short-term debt.

Overview

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4. Table 1 shows that the Authority held a net borrowing position of £643m on 31 March 2020 arising from its revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while useable reserves and working capital are the underlying resources available for investment.

5. The Treasury Management Strategy for 2020/21, Approved by Audit & Governance Committee in January 2020, continued the policy of internal borrowing. This maintains borrowing below its underlying level by utilising available cash balances on a temporary basis (i.e. working capital and useable reserves) which are not required in the short to medium term. This approach reduces market and credit risk for the investment portfolio and reduces borrowing costs. The Balance sheet position at 31 March 2020 is summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31/03/20 Actual £m
General fund CFR	1252
Less: Other long-term liabilities	(205)
Gross Borrowing Requirement	**1047**
Less: useable reserves and working capital	(404)
Net Borrowing Requirement	**643**

6. The Council also manages cash on behalf of Surrey Police and Crime Commissioner, the balance of which was £22.6m as at 30 September 2020. The Council accounts for this as short-term borrowing. The treasury management position as at 30 September 2020 and the change over the six months is summarised in Table 2.

Table 2: Treasury Management Summary

	31/03/20 Balance £m	**Movement £m**	**30/09/20 Balance £m**
Long-term borrowing	436	(1)	435
Short-term borrowing	222	21	243
Surrey Police	17	6	23
Total Borrowing	**675**	**26**	**701**
Money Market Funds	(32)	7	(25)
Net Borrowing	**643**	**33**	**676**

Borrowing Strategy

7. At 30 September 2020 the Authority held £701m of loans (an increase of £26m since 31 March 2020). Outstanding loans on 30 September 2020 are summarised in Table 3 below.

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Table 3: Borrowing position

	31/03/20 Balance £m	Net change £m	30/09/20 Balance £m	30/09/20 Weighted average rate %	30/09/20 Weighted average maturity (years)
Public Works Loan Board	426	(1)	425	3.84	29 years
Banks (fixed-term)	10	-	10	5.00	33 years
Local Authorities (short-term)	222	21	243	0.58	< 1 year
Surrey Police & Crime Commissioner	17	6	23	0.23	0 days
Total Borrowing	**675**	**26**	**701**		

8. The Authority's main objective when borrowing has been to strike a balance between securing low interest rates an achieving cost certainty over a period for which funds are required. This position provides short term savings with the flexibility to secure longer dated loans as and when the level of funds available for internal borrowing reduces, or financial forecasts indicate that external borrowing rates may increase.

9. In order to best meet these objectives, no new long-term borrowing was undertaken in the first half of 2020/21; internal borrowing was maximised and short-term borrowing was utilised to manage cash flow. This strategy enabled the authority to minimise net borrowing costs (despite foregone investment income) and reduce overall treasury risk.

10. The "cost of carry" analysis performed by the Authority's treasury management advisor, Arlingclose, did not indicate any value in borrowing in advance for future years' planned expenditure and therefore none was taken.

Investment Activity

11. The Authority holds invested funds, representing income received in advance for expenditure plus balances and reserves held. During the first half of 2020/21 the Authority's average daily level of investments was £67m compared to £42m for the first 6 months of 2019/20.

12. The Council can place cash on deposit on the money market through brokers, directly with counterparties, through the use of call accounts, money market funds or direct deal facilities, or with the Debt Management Office (DMO). No new fixed term deposits have been agreed during the first half of 2020/21. All investments have been made through overnight money market funds.

13. The weighted average return on all investments the council received in the quarter to 30 September 2020 is 0.23%. This compares to the average Bank of England (BoE) base rate of 0.10% for the same period.

Table 4: Investment Benchmarking

	BoE base rate	Weighted return on Investments
2020/21 Quarter 2	0.10%	0.14%
2020/21 Quarter 1	0.10%	0.32%
2019/20 Total	0.72%	0.69%
2018/19 Total	0.67%	0.51%

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14. Both the CIPFA Code and the government's Investment Guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike and appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. In furtherance of these objectives, the Council's strategy of maximising internal borrowing has reduced the cash available for investment and reduced the scope of creating longer-term investment deposits.

15. Continued downward pressure on short-dated cash rates brought net returns on sterling low volatility net asset value money market funds (LV NAV MMFs) close to zero even after some managers have temporarily reduced their fees. At this stage, negative returns are not the central case of most MMF managers over the short-term, and fee waivers should maintain positive net yields, but the possibility cannot be ruled out.

Other Investment Activity

16. The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Authority as well as other non-financial assets which the Authority holds primarily for financial return. the Authority holds £134m of investments in directly owned investment property (excluding assets under construction) and £327m in Loans to and shareholdings in its subsidiaries.

17. It is projected that these non-treasury investments will generate £11.6m net investment income for the Authority in 2020/21 after taking account of direct costs and Minimum Revenue Provision (MRP).

18. The impact of CV-19 and wider economic pressures provide a challenging economic backdrop for the investment property portfolio. Total reductions in the fair value of the assets across 2018/19 and 2019/20 amount to £63m. Whilst these represent temporary fluctuations in the value of the assets, the Council will review its policy for Minimum Revenue Provision against investment properties to ensure that it remains prudent. Work is ongoing to mitigate risks to rental income from the portfolio.

Treasury Performance

19. The authority measures the financial performance of its treasury management activities in terms of its impact on the revenue budget. Table 5 outlines the forecast for the interest payable and interest receivable budget for the full year of 2020/21. Currently both interest payable and interest receivable are forecast to budget as both depend on the level of capital expenditure for the remainder of the year and the extent to which this is funded through borrowing.

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Table 5: Revenue implications of treasury management activity

	Budget £m	**Full Year Forecast £m**	**Variance £m**
Interest Payable	18.9	18.9	0.0
Interest Receivable	(0.3)	(0.3)	0.0

Compliance Report

20. All treasury management activities undertaken during the first half of 2020/21 comply fully with the CIPFA Code of Practice and the Authority's approved Treasury Management Strategy. Compliance with specific investment limits, the authorised borrowing limit and operational boundary for external debt, is demonstrated in tables 6 and 7 below.

Table 6: Debt Limits

	01/04/20 to 30/09/20 Maximum £m	**30/09/20 Actual £m**	**2020/21 Operational Boundary £m**	**2020/21 Authorised Limit £m**	**Complied?**
Total			1,223	1,723	
Less: Other long-term liabilities			(136)	(136)	
Underlying Borrowing	**753**	**701**	**1,087**	**1,587**	✓

21. Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not considered a compliance failure. Total debt did not exceed the operational boundary in any period during the first half of 2020/21.

Table 7: Investment Limits

	01/04/20 – 30/09/20 Maximum £m	30/09/20 Actual £m	2020/21 Limit £m	Complied?
UK Central Government	0	0	Unlimited	✓
Money Market Funds	150	25	150	✓
Any group of pooled funds under the same management	0	0	25	✓
Any group of organisations under the same ownership	0	0	20	✓
Any single organisation, except the UK Central Government	0	0	20	✓
Unsecured Investments with Building Societies	0	0	10	✓

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Treasury management Indicators

22. The Authority measures and manages its exposures to treasury management risks using the following indicators

23. Maturity Structure of Borrowing: This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of all borrowing were:

Table 8: Maturity Structure of Borrowing

	30/09/20 Actual	Upper Limit	Lower Limit	Complied?
Under 12 months	36%	50%	0%	✓
12 months and within 24 months	1%	50%	0%	✓
24 months and within 5 years	0%	50%	0%	✓
5 years and within 10 years	0%	75%	0%	✓
10 years and above	63%	100%	25%	✓

24. Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

25. **Principal Sums Invested for Periods Longer than a year:** The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end were:

Table 9: Principal invested for more than one year

	30/09/20 Actual £m	2020/21 Limit £m	Complied?
Principal invested for more than one year	0	40	✓

Other Implications

Financial and value for money implications

26. The direct financial implications of this report are highlighted in table 5 and form part of the monthly budget monitoring report to Cabinet.

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Equalities and Diversity Implications

27. There are no direct implications of this report.

Risk Management Implications

28. The noteworthy risks posed by Treasury management are outlined in the body of the report and are monitored through the Authority's compliance with the approved Prudential and Treasury Management Indicators.

Next steps:

a. The Treasury Team will continue to monitor the UK and overseas banking sector and will continue to update this Committee as appropriate

b. In line with the requirements of CIPFA's Code of Practice for Treasury Management, a full-year report for 2020/21 will be bought to the Committee after financial year end.

c. The Treasury Team will prepare the annual Treasury Management Strategy, which will be presented to this committee in January 2020 for approval.

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Sources/background papers:

- Capital Budget, Prudential Indicators and Treasury Management Strategy 2020/21.
- CIPFA Code of Practice for Treasury Management
- CIPFA Prudential Code

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