SURREY
COUNTY COUNCIL

Audit & Governance Committee
18 June 2021

2020/21 Treasury Management Outturn Report

Purpose of the report:

This report summarises the Council's treasury management activities during 2020/21, as required, to ensure compliance with the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Authority to approve a treasury management annual report after the end of each financial year.

Recommendations:

It is recommended that the committee:

- Note the content of the Treasury Management Outturn Report for 2020/21 and compliance with all Prudential Indicators.

Background:

1. The Authority has adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code) which requires the Authority to approve Treasury Management half-year and annual outturn reports. This is the annual outturn report for 2020/21.

2. The Authority's Treasury Management Strategy Statement and Prudential Indicators for 2020/21 were approved at Audit & Governance Committee on 29 January 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 Authority's Treasury management Strategy.

3. An economic commentary provided by our expert Treasury Management Advisors, Arlingclose is included in Annex 1

Treasury Management Annual Report 2020/21

Overview

4. On 31 March 2021, the Authority had net borrowing of £660m arising from its revenue and capital income and expenditure, an increase of £17m since 31 March 2020. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), which represents the amount of capital expenditure that is not funded from capital receipts, government grants, third party contributions or revenue.

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5. Net borrowing has increased due to a rise in the CFR as new capital expenditure was higher than the financing applied, including minimum revenue provision. This is set out in table 1, below:

Table 1: Balance Sheet Summary

	31/03/20 Balance £m	2020/21 Movement £m	31/03/21 Balance £m
General Fund CFR	1,252	92	1,344
Less PFI Liabilities	(205)	19	(186)
Gross Borrowing Requirement	**1,047**	**111**	**1,158**
Less usable reserves and working capital	(404)	(94)	(498)
Net Borrowing Requirement	**643**	**17**	**660**

Note: Columns do not sum due to rounding

6. The Treasury Management Strategy for 2020/21, approved by Audit & Governance Committee in January 2020, continued the policy of internal borrowing wherever possible. This maintains borrowing below its underlying level by using available reserves and working capital to reduce the need for external borrowing. This minimises interest rate risks and keeps interest costs low.

7. The Council also manages cash on behalf of Surrey Police and Crime Commissioner, the balance of which was £11.6m as at 31 March 2021. The Council accounts for this as short-term borrowing. The treasury management position as at 31 March 2021 and the year-on-year change is shown in table 2 below.

Table 2: Treasury Management Summary

	31/03/20 Balance £m	2020/21 Movement £m	31/03/21 Balance £m
Long-term borrowing	436	(2)	434*
Short-term borrowing	222	51	273
Surrey Police	17	(5)	12
Total borrowing	**675**	**44**	**719**
Money Market Funds	(32)	(27)	(59)
Net borrowing	**643**	**17**	**660**

*Total long term borrowing is £444m. This includes £2.6m of Local Enterprise Partnership (LEP) loans and £6.1m of Salix which are managed outside of the Treasury Management Strategy.

Borrowing Activity

8. At 31 March 2021, the Authority held £719m of borrowing, an increase of £44m on the previous year. The sources of borrowing, interest rates and the year-on-year change is shown in table 3 below.

Table 3: Borrowing Position

	31/03/20 Balance £m	2020/21 Net Movement £m	31/03/21 Balance £m	31/03/21 Rate %
Public Works Loan Board (PWLB)	426	(2)	424	3.85
Banks (fixed-term)	10	0	10	5.00
Local authorities (short-term)	222	51	273	0.09
Surrey Police & Crime Commissioner	17	(5)	12	0.10
Total borrowing	**675**	**44**	**719**	

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9. The Authority's primary consideration when borrowing money is to balance low interest charges and cost certainty over the period, while allowing enough flexibility to renegotiate a portion of the debt portfolio based upon changing strategic needs. The Authority has explored the potential for early repayment of the £10m bank loan at 5% but the penalties of early repayment are prohibitively high.

10. In keeping with these objectives, no new long-term borrowing was undertaken in 2020/21. The local authority inter-lending market was extremely liquid during 2020/21, due to uncertainty over cashflow during the first half of the year, and compounded by significant government support which benefitted local authorities' cash flow positions. This resulted in the over-supply of Local Authority cash and therefore the Council being able to borrow from other Local Authorities at very low interest rates (below the Bank of England Base Rate). Additionally, the Council's advisors, Arlingclose, forecasts that long-term borrowing rates will remain low over the next 3 years, therefore the strategy for the year was to continue to finance the Council's cash flow and borrowing requirements by using short term borrowing.

Investment Activity

11. The Authority holds invested funds, representing income received in advance of expenditure, plus reserves and balances held which have not been utilised for internal borrowing.

12. Both the CIPFA Code and government 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 an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

13. In furtherance of these objectives and given the continuing risk and low returns from short-term unsecured bank investments, the Authority has kept its cash balances and investments low throughout 2020/21 and invested funds principally in Money Market Funds to ensure liquidity. During the year, the Authority's investment balance ranged between £0.5m and £150m. The Council's average daily level of cash investments was £57.1m during 2020/21, compared to an average of £41.5m during 2019/20. The Council invests temporary cash surplus exclusively through the use of money market funds (MMF).

14. The year-end investment position and the year-on-year change is shown in table 4 below:

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Table 4: Investment Position (Treasury Investments)

	31/03/20 Balance £m	2020/21 Net Movement £m	31/03/21 Balance £m	31/03/21 Rate* %
Money Market Funds	32	27	59	0.14
Total Investments	**32**	**27**	**59**	**0.14**

*weighted average rate earned in the year

15. The weighted average return on all investments the Council received in the year to 31 March 2021 was 0.14%. This compares favourably against a -0.07% average 7-day London Interbank Bid Rate (LIBID) for the same period.

Financial Implications

16. The outturn for interest paid, interest received and the minimum revenue provision are outlined in table 5 below.

Table 5: Revenue Implications of Treasury Management Activity

	Budget £m	Outturn £m	Variance £m
Interest Paid	18.9	17.7	(1.2)
Interest Received	(0.3)	(0.3)	(0.0)
MRP	16.1	16.0	(0.1)

17. The amount of the Authority's revenue budget required to be set aside for the future repayment of external borrowing is known as the Minimum Revenue Provision (MRP). This amount is calculated by reference to the Council's balance sheet as at the end of the previous financial year. The amount required for 2020/21 was £0.1m less than expected when the budget was set due to marginally lower capital expenditure in 2019/20.

18. The variance of £1.2m on interest payable relates primarily to the Council's continued short-term borrowing strategy. This resulted in rates payable lower than those assumed when setting the 2020/21 budget.

Compliance Report

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

Table 6: Debt Limits

	2020/21 Max £m	31/03/21 Actual £m	2020/21 Operational Boundary £m	2020/21 Authorised Limit £m	Complied
Total			1,223	1,723	
Less: Other long term liabilities (PFI)			(136)	(136)	
Underlying Borrowing	765	718	1,087	1,587	✓

20. 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 at any point in 2020/21.

Table 7: Investment Limits

	2020/21 Maximum £m	31/03/21 Actual £m	2020/21 Limit £m	Complied
UK Central Government	0	0	Unlimited	✓
Money Market Funds	150	59	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

21. The Authority measures and manages its exposure to treasury management risks using the following indicators.

Security: The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard is therefore given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis. No investments will be made with an organisation if there are substantive doubts about its credit quality. In addition, if insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government via the Debt Management Office or invested in government treasury bills or with other Local Authorities.

Liquidity: The Council manages its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments. The Council maintains a bank overdraft of £100,000, utilises overnight access Money Market Funds and accesses short term borrowing to meet cash flow requirements. The Local Authority market provides readily available funds.

Interest Rate Exposures:

The Council currently has £273m of short-term borrowing with an additional £63m expected to finance the 2021-22 capital programme, which would result in a total of £336m by March 2022. Short term borrowing is subject to variable interest rates linked to the Bank of England (BoE) base rate, meaning it is subject to interest rate risk if the base rate increases. The Council's Treasury Management advisor Arlingclose has not forecast an increase in interest rates in the short term so this scenario is unlikely, however if there was an increase in rates a 0.25% increase would result in a potential increase of £0.5m in interest costs by March 2022, assuming an even profile of borrowing to fund capital expenditure in 2021-22 and factoring in the Q1 BoE rate decision has already passed with no increase in rates. The Council has set aside £2.1m in reserves to mitigate variable interest rate exposure which more than covers this interest exposure scenario.

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 fixed rate borrowing were:

Table 8: Maturity Structure of Borrowing

	31/03/21 Actual	Upper Limit	Lower Limit	Complied
Under 12 months	40%	60%	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	59%	100%	25%	✓

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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 interest rate changes.

Table 9: Sums invested for more than one year

	2020/21 Maximum £m	31/03/21 Actual £m	2020/21 Limit £m	Complied
Sums invested for longer than one year	0	0	40	✓

Other Non-Treasury Holdings and Activity

22. Although not classed as treasury management activities, the CIPFA Code requires the Authority to report on investments for policy reasons outside of normal treasury management. This includes service investments for operational and/or regeneration as well as commercial investments which are made mainly for financial reasons.

23. The Authority holds the following non-treasury investments:
    - £122m of directly owned investment property
    - £240m of loans to Halsey Garton Ltd
    - £96m of equity investments in Halsey Garton Ltd
    - £2m of loans to other subsidiaries

24. Such loans and investments have been approved in accordance with the Council's agreed processes. A register of such investments is maintained and performance information is reported to the Strategic Investment Board or the Shareholder and Investment Panel, in accordance with their Terms of Reference.

25. These non-treasury investments generated £6.6m of investment income for the Authority after taking account of direct costs and interest payable.

Implications:

Financial

26. The financial implications of this report are discussed in paragraph 16-17 and were included in the outturn report to Cabinet on 1st June 2021.

Equalities and Diversity Implications

27. There are no direct equities implications of this report

Risk Management Implications

28. The risk management arrangements in relation to treasury management are discussed in paragraph 20.

Next steps:

i. The treasury team will continue to monitor the UK and overseas banking sector and will continue to update this Committee as appropriate

ii. In line with the requirements the CIPFA Code, this Committee will receive a half yearly report on the Council's treasury management activities in December 2022 and a full year report for 2021/22 in July 2022.

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Sources/background papers:
Capital Budget, Prudential Indicators & Treasury Management Strategy 2020/21
CIPFA Code of Practice for Treasury Management
CIPFA Prudential Code

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