

Report

Report to:	Finance and Corporate Resources Committee
Date of Meeting:	10 November 2021
Report by:	Executive Director (Finance and Corporate Resources)

Subject:	Treasury Management Activity – Second Quarter Review
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1. Purpose of Report

1.1. The purpose of the report is to:-

- ♦ provide a second quarter review of Treasury Management Activity for 2021/2022

2. Recommendation(s)

2.1. The Committee is asked to approve the following recommendation(s):-

- (1) that the contents of this report be noted.

3. Background

3.1 In order to provide members with information on the Council's Treasury Management activities, a quarterly report is presented to this Committee. This report covers the period 1 April 2021 to 30 September 2021.

4. Market Performance

- 4.1. After the Bank of England left the base rate unchanged at 0.75% in January 2020, the onset of the coronavirus epidemic in March of that year resulted in two emergency cuts, first to 0.25% and then to 0.10%.
- 4.2. As at 30 September 2021, the base rate remained at 0.10% and the Bank of England Asset Purchase Programme (commonly referred to as its policy of quantitative easing) was £895 billion.
- 4.2. At the time of writing this report, the Council's Treasury Management Advisers are predicting no further changes in the UK Base Rate during the remainder of 2021/2022 but are forecasting an increase to 0.25% in early 2022/2023.

5. Debt Management and Borrowing Strategy

- 5.1. The Council began the year with debt of £1,005.540 million with fixed rate loans from the Public Works Loans Board (PWLb) making up 99.15% of the debt.
- 5.2. Table 1 shows the movement in borrowing from 1 April 2021 to 30 September 2021. Short term borrowing reflects borrowing which will mature in the coming year, or where the debt can be recalled in the coming year.

Table 1 – Movement in Borrowing to 30 September 2021

	Balance as at 01/04/2021 £m	New Borrowing £m	Debt Maturing £m	Debt Repaid £m	Balance as at 30/09/2021 £m	Increase/ Decrease in Borrowing £m
Short Term Borrowing	40.954	0.000	(39.377)	0.00	1.577	(39.377)
Long Term Borrowing	964.586	0.000	0.00	0.00	964.586	0.000
TOTAL BORROWING	1,005.540	0.000	(39.377)	0.00	966.163	(39.377)

- 5.3. In 2012/2013, HM Treasury introduced a “certainty rate” to enable eligible local authorities to access cheaper PWLB funding, with a 20 basis point (0.20%) reduction on the standard rate. South Lanarkshire Council has access to this reduced rate.
- 5.4. The Council has an expected borrowing requirement of £193.938 million during 2021/2022.
- 5.5. The Executive Director (Finance and Corporate Resources), under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time, taking into consideration the differential between investment earnings and debt costs that remains high.
- 5.6. No borrowing has been taken so far in the current financial year. Instead, cash balances have been used to fund capital spend. Borrowing to replace these balances will be required going forward.
- 6. Investment Activity**
- 6.1. On a daily basis, the Treasury Management section within Finance and Corporate Resources manages the Council’s cash balances. These balances can result from day to day cash flow situations where income has been received before expenditure has taken place, and from the balances held in earmarked reserves for use at a later date. It is the responsibility of the section to manage these funds. The primary consideration when making deposits is the security of funds. Secondary to this, consideration is given to ensuring we have access to funds when necessary, and that these funds are working as well as they can for the Council.
- 6.2. The Prudential Indicators, Treasury Management Strategy and Annual Investment Strategy Report for 2021/2022 was approved by South Lanarkshire Council on 10 March 2021. This included details of permitted investments for the Council.
- 6.3. Prior to depositing funds with any bank or building society, checks are made with the Council’s treasury adviser, Link Asset Services, that the institution is considered safe and that any deposit conforms to their recommended time duration as determined by their Rating Methodology. This methodology uses credit ratings, rating watches and outlooks and credit default swap (CDS) prices to establish a suggested time duration for deposits.
- 6.4. Deposits made in the period 1 April 2021 to 30 September 2021 totalled £858.590 million. This is the cumulative deposits placed over this period. This is broken down per sector and institution in Table 2. 58.83% of these deposits were made in the UK Government through the Debt Management Office (DMO) deposit facility.

- 6.5. In order to manage their cash flow over the short term, local authorities, as part of normal treasury management activity, will place money on deposit with other local authorities. Deposits placed with other local authorities account for 16.65% of deposits with the remaining 24.52% placed in call accounts with Bank of Scotland and The Royal Bank of Scotland.
- 6.6. Deposits in the UK Government are considered to be the most secure and this is reflected in the low interest rate for deposits in the DMO.

Table 2 – Investment Activity 1 April 2021 to 30 September 2021

Counterparty	Deposit Totals (£m)	% of Total Deposits	Average Interest Rate
Deposits in UK Government			
Debt Management Account Deposit Facility	505.100	58.83%	0.01%
Total Deposits in UK Government	505.100	58.83%	0.01%
Deposits in UK Local Authorities	143.000	16.65%	0.04%
Deposits in UK Banks and Building Societies:			
Bank of Scotland	59.500	6.93%	0.01%
Royal Bank of Scotland	150.990	17.59%	0.01%
Total Deposits in UK Banks and Building Societies	210.490	24.52%	0.01%
Total Deposits 01/04/2021 to 30/09/2021	858.950	100.00%	0.02%

- 6.7. The average interest rates achieved from the deposits are also shown in Table 2. As the base interest rate has been at, or below, 0.75% since March 2009, interest rates achievable for deposits remain low.
- 6.8. Actual deposits as at 30 September 2021 totalled £226.930 million.

7. Management of Risk

- 7.1. It is recognised that no Treasury Management activity is without risk and practices are put in place in order to limit risk. As noted in section 6.2, the Treasury Management Strategy was approved in March 2021 and set a framework for Treasury Management activities in 2021/2022. It also set limits on debt and investments in order to mitigate risks.
- 7.2. The Annual Investment Strategy for 2021/2022, also approved in March 2021, included details on how risk would be managed for all permitted investments. This included criteria for placing deposits with the Debt Management Office (DMO), UK Local Authorities, Banks and Building Societies and Money Market Funds.

- 7.3. Part of the criteria for counterparties is meeting minimum credit ratings with the three main rating agencies. A credit rating evaluates the credit worthiness of an organisation. It is an evaluation made by a credit rating agency of the organisation's ability to pay back the debt and the likelihood of default.
- 7.4. Tables 3 to 5 show a breakdown of deposits with details of the credit ratings of banks and building societies used from 1 April 2021 to 30 September 2021. Deposits with the DMO are with the UK Government and so have a rating equivalent to the UK's sovereign rating. Deposits with local authorities are considered to be of very high credit quality.

Table 3 – Fitch Ratings

Long Term Rating	Short Term Rating	Deposits Totals	Percentage of Total Deposits
Deposits with DMO / UK Government (AA-)		505.100m	58.83%
Deposits with Local Authorities		143.000m	16.65%
A+	F1	210.490m	24.52%
Total		858.590m	100.00%

Table 4 – Moody's Ratings

Long Term Rating	Short Term Rating	Deposits Totals	Percentage of Total Deposits
Deposits with DMO / UK Government (Aa3)		505.100m	58.83%
Deposits with Local Authorities		143.000m	16.65%
A1	P-1	210.490m	24.52%
Total		858.590m	100.00%

Table 5 – Standard and Poor's Ratings

Long Term Rating	Short Term Rating	Deposits Totals	Percentage of Total Deposits
Deposits with DMO / UK Government (AA)		505.100m	58.83%
Deposits with Local Authorities		143.000m	16.65%
A+	A-1	59.500m	6.93%
A	A-1	150.990m	17.59%
Total		858.590m	100.00%

- 7.5. The tables above show that 75.48% of deposits were made with counterparties of very high credit quality (DMO/UK Government and other local authorities).
- 7.6. The remaining deposits were in instant access accounts with The Royal Bank of Scotland and Bank of Scotland.
- 7.7. The graph at Appendix 1 shows the duration of deposits made from 1 April 2021 to 30 September 2021. The graph shows that, since 1 April 2021, all deposits have been made for 1 year or less. The maximum maturity period of 326 days was for a deposit of £10.000 million.

8. Next Quarter Investment Plans

- 8.1. The current investment framework will be continued in the next quarter. Deposits will continue to be placed with the institutions where their ratings are consistent with the Council's approved criteria. Deposits will also continue to be placed with the DMO and UK local authorities.
- 8.2. Treasury Bills will be used when they return a higher yield than deposits in the DMO for the same, very low risk.
- 8.3. Deposits may also be placed with selected Money Market Funds that meet the Council's approved criteria.
- 8.4. We will continue to work with our Treasury Management Advisers, Link, to ensure we gain all information available on counterparties before any deposits are made.

9. Treasury Management Indicators

- 9.1. The purpose of these indicators is to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. However, if these are set to restrictive limits, they will impair the opportunities to reduce costs/improve performance. The indicators are detailed in sections 9.2 to 9.5.
- 9.2. **Limits for External Debt:** The operational and authorised limits for external debt for 2021/2022 were set in the Prudential Indicators, Treasury Management Strategy and Annual Investment Strategy 2021/2022 approved by South Lanarkshire Council on 10 March 2021. These are shown in Table 6, along with a column showing the difference between the actual debt level and the limits (headroom).

Table 6 – Limits for External Debt

	Estimate as per 2021/22 Strategy	Minimum Headroom to Limits in period	Headroom as at 30/09/2021
	£m	£m	£m
Operational Limit for external debt	1,340.000	334.460	373.837
Authorised Limit for external debt	1,360.000	354.460	393.837

- 9.3. The indicator shows that we have not breached the operational and authorised limits to 30 September 2021. There has been a minimum level of headroom of £393.837 million between actual and authorised level for external debt in the period to 30 September 2021.
- 9.4. **Limits on Maturity Structure:** By setting limits on the maturity structure of borrowing, the exposure to large concentrations of debt needing to be replaced at the same time in the future at currently unknown rates can be limited. This effectively places a limit on exposure to longer term interest rate movement. This is shown in Table 7.

Table 7 – Limits on Maturity Structure

Maturity Structure of Borrowing				
	Upper Limit	Lower Limit	Maximum for period to 30/09/21	Actuals as at 30/09/21
Under 12 months	30%	0%	4.07%	0.16%
12 months and 24 months	30%	0%	4.54%	4.54%
24 months and 5 years	50%	0%	12.20%	12.20%
5 years and 10 years	60%	0%	35.41%	35.41%
10 years and 20 years	60%	0%	12.42%	12.42%
20 years and 30 years	70%	0%	0.05%	0.05%
30 years and 40 years	80%	0%	35.22%	35.22%
40 years and 50 years	90%	0%	0.00%	0.00%
50 years and above	90%	0%	0.00%	0.00%

- 9.5. The indicator shows that the upper limits for all maturity profiles have not been breached to 30 September 2021.

10. Employee Implications

- 10.1. There are no employee implications.

11. Financial Implications

- 11.1. The current rate of interest receivable remains low.
- 11.2. Any deposit interest received offsets Loan Charges made to the Council's Revenue budget. The level of deposit interest factored into the Council's budget is minimal, therefore the low level of interest received will have no impact on existing budgets.
- 11.3. The costs of borrowing for capital expenditure have been built into the long term Revenue Budget Strategy.

12. Climate Change, Sustainability and Environmental Implications

- 12.1. There are no implications for climate change or sustainability in terms of the information contained in this report.
- 12.2. There is also no requirement to carry out an environmental impact assessment in terms of the information contained within this report.

13. Other Implications (Including Environmental and Risk Issues)

- 13.1. Section 7 of this report provides details of how investment risk is managed.

14. Equality Impact Assessment and Consultation Arrangements

- 14.1. This report does not introduce a new policy, function or strategy or recommend a change to an existing policy, function or strategy and, therefore, no impact assessment is required.
- 14.2. There is no requirement to carry out any consultation in terms of the information provided in this report.

Paul Manning

Executive Director (Finance and Corporate Resources)

1 October 2021

Link(s) to Council Values/Ambitions/Objectives

- ♦ Accountable, effective, efficient and transparent

Previous References

- ♦ Prudential Indicators, Treasury Management Strategy and Annual Investment Strategy 2021/2022, South Lanarkshire Council, 10 March 2021
- ♦ Treasury Management Activity – First Quarter Review, Finance and Corporate Resources Committee, 1 September 2021

List of Background Papers

- ♦ None

Contact for Further Information

If you would like to inspect the background papers or want further information, please contact:-

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Maturity of Deposits Placed 1 April 2021 - 30 September 2021

