South Northamptonshire Council

Audit Committee

30 July 2020

Treasury Management Report – Q1 – June 2020

Report of the Executive Director – Finance

This report is public

Appendix 1 to this report is exempt from publication by virtue of paragraph 3, Part 1 of Schedule 12A of the Local Government Act 1972

Purpose of report

To receive information on treasury management performance and compliance with treasury management policy for 2020/21 as required by the Treasury Management Code of Practice.

1.0 Recommendations

The meeting is recommended:

1.1 To note the contents of the Q1 June 2020 Treasury Management Report.

2.0 Introduction

2.1 In 2012 the Council 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 Council to approve treasury management semi-annual and annual reports.

2.2 The Council's treasury management strategy for 2020/21 was approved at a meeting on 26 February 2020. The Council has invested substantial sums of money and is therefore exposed 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 is therefore central to the Council's treasury management strategy.

2.3 Following consultation in 2017, CIPFA published new versions of the Prudential Code for Capital Finance in Local Authorities (Prudential Code) and the Treasury Management Code of Practice; the local authority specific Guidance Notes for the Codes were published in July 2018. In England MHCLG published its revised Investment Guidance which came into effect from April 2018.

2.4 The updated Prudential Code includes a requirement for local authorities to provide a Capital Strategy, which is to be a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy for 2020/21, complying with CIPFA's requirement, was approved by full Council on 26 February 2020.

3.0 Report Details

2020/21 Performance

3.1 As at the end of June 2020 the Council had £31.6m of funds invested.

Appendix 1 details the schedule of investments as at 30 June 2020.

Strategy

3.3 The Treasury Management Strategy for 2020/21 includes the Annual Investment Strategy which sets out the Council's investment priorities.

Security of capital has remained the Council's main investment objective, followed by liquidity of capital, and then by yield. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2020/21.

3.4 Counterparty credit quality is assessed and monitored with reference to:

- Credit Ratings - the Council's minimum long-term counterparty rating of A- (or equivalent) across rating agencies Fitch, S&P and Moody's
- Credit default swaps – a type of insurance to protect against default risk
- GDP of the country in which the institution operates
- The country's net debt as a percentage of GDP
- Sovereign support mechanisms or potential support from a well-resourced parent institution
- Share price

3.5 The Arlingclose ratings and advice encompass all of these and other factors and is our primary source of guidance in selecting investments. In addition to Arlingclose ratings and advice, the council keeps an internal counterparty 'Watch List' based on intelligence from a variety of other sources available to officers.

3.6 All treasury management activities undertaken during the first 3 months of 2020/21 complied with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy, and all indicators were met during, and at the end of, the reporting period.

Investment performance for 3 months ended 30 June 2020:

3.7 Investment rates available in the market have reduced to very low levels as a result of the Bank of England base rate reducing to 0.1% in March 2020.

Funds available for investment purposes are available on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme.

3.8 Table 1 shows the investment summary to 30 June 2020:

Year to Date:

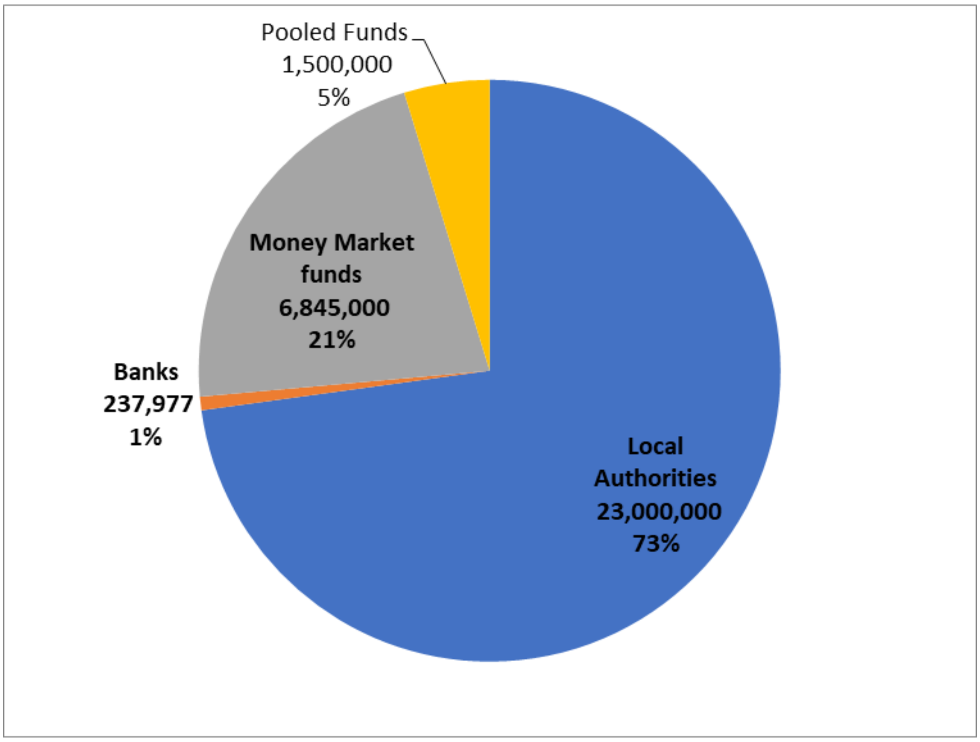
Average Investment balance	**Interest Budget £**	**Interest Actual £**	**Variance £**	**Annualised rate of return**
£38.6m	62,500	62,919	419	0.65%
Rate Benchmarking	**1-month**	**3-month**	**6-month**	**12-month**
Average LIBOR rate	0.17%	0.41%	0.54%	0.70%

The Council is currently slightly above target in terms of interest earned at 30 June, but is forecast to be approximately £60k below budget at the end of the financial year. Although cash balances are higher than forecast as a result of receiving significant Government funding in relation to business grants, rates look set to remain very low for the foreseeable future. There is, of course, still a high degree of uncertainty around this – see Arlingclose comments in 3.10 below.

The average duration of investments held at 30/06/2020 is 13 months and the average interest rate is 0.78%. Our rates are slightly below LIBOR rates as our investment counterparty criteria (ratings, etc.) are more stringent than the market average, in order to maintain the security of our capital.

A full list of current investments is shown at Appendix 1 and summarised by type below:

Table 2 - Types of Investment as at 30/06/2020:



3.9 **Non-treasury investment activity.**

The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council. This is replicated in MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially to generate a profit.

As at the report date, the Council holds £3m of investments in the form of a loan to Silverstone Heritage Ltd, at a rate of 5%.

This non-treasury investment generates a higher rate of return than earned on treasury investments, but this reflects the additional risks to the Council of holding such investments.

3.10 Arlingclose have provided the following economic commentary and interest rate forecast (comments are as at 30 June 2020):

- The UK's exit from the European Union took a back seat during the first quarter of 2020/21 as the global economic impact from coronavirus took centre stage. Part of the measures taken to stop the spread of the pandemic included the government implementing a nationwide lockdown in late March which effectively shut down almost the entire UK economy. These measures continued throughout most of the quarter with only some easing of restrictions at the end of May and into June.
- Bank Rate was maintained at 0.1% despite some speculation that the Bank of England's Monetary Policy Committee (MPC) might cut further and some MPC members also suggesting that negative rates are part of the Bank's policy tools. In June the Bank increased the asset purchase scheme by £100 billion, taking the recent round of QE to £300bn and total QE to £745 billion
- At the same time, the government also implemented a range of fiscal stimulus measures totalling over £300 billion which had been announced in March and designed to dampen the effect of the pandemic on the labour market.
- GDP growth contracted by 2.2% in Q1 (Jan-Mar) 2020 pushing the annual growth rate down to -1.6%. The lockdown only came into force on 23rd March, and the markets are braced for a dire set of growth data for Q2. In April UK GDP fell 20.4% month-on-month. On the back of the 5.8% month-on-month fall in March, this means economic output fell by 25% compared to its pre-coronavirus peak in February 2020.
- The first few months of 2020 will indicate whether the economy benefits from restored confidence. The government will undertake substantial fiscal easing in 2020/21, which should help support growth in the event of a downturn in private sector activity

- The headline rate of UK Consumer Price Inflation UK Consumer Price Inflation fell to 1.2% y/y in May, further below the Bank of England's 2% target.

- In the three months to June, labour market data remained largely unchanged on the previous quarter. This is likely due to the government's furlough scheme as more than a quarter of the UK workforce was estimated to be supported by it. The ILO unemployment rate remained unchanged at 3.9% while the employment rate fell to 76.4%. However, employers will have to contribute towards furlough payments from August and the scheme is due to stop at the end of October; unemployment is expected to rise as a result.

- The US economy contracted at an annualised rate of 5.0% in Q1 2020. The Federal Reserve maintained the Fed Funds rate at between 0% and 0.25% while the US government announced a $2 trillion fiscal stimulus package. Relations between the US and China, which had briefly improved when Phase 1 of the trade agreement was signed in January, deteriorated over the quarter.

- With little room to move on interest rates, the European Central Bank maintained interest rates at 0% and the rate on the deposit facility (which banks may use to make overnight deposits with the Eurosystem) at -0.5% and announced a further huge, open-ended commitment to buy €600bn of bonds under its Pandemic Emergency Purchase Programme (PEPP) which can be reinvested out to 2022. This lifted the ECB's total bond buying support package to €1.35trillion

- <u>Outlook for the remainder of 2020/21</u>

- The medium-term global economic outlook is very weak. While containment measures taken by national governments in response to coronavirus are being eased, it is likely to be some time before demand recovers to pre-crisis levels due to rises in unemployment, the on-going need for virus control measures and the impact on consumer/business confidence.

- The responses from the Bank of England, HM Treasury as well as other central banks and governments have been significant and will act to support the recovery when it occurs, by keeping financial conditions stable and many businesses solvent/employees employed than would otherwise have been the case. There will be an economic bounce in the second half of the year, as businesses currently dormant begin production/supply services once more.

- However, the scale of the economic shock to demand and the probable on-going social distancing measures necessary before a vaccine is produced will mean that the subsequent pace of recovery is limited.

- Arlingclose expects Bank Rate to remain at the current 0.10% level and additional monetary loosening in the near future through further financial asset purchases (QE). While the Arlingclose central case for Bank Rate is no change, further cuts to Bank Rate to zero or even into negative territory cannot be ruled out.

- Downside risks remain in the near term, as households and businesses react to an unprecedented set of economic circumstances**.**

	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23
Official Bank Rate												
Upside risk	0.00	0.00	0.00	0.00	0.00	0.15	0.15	0.15	0.15	0.30	0.30	0.30
Arlingclose Central Case	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Downside risk	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35	-0.35

4.0 Conclusion and Reasons for Recommendations

This report details the Treasury Performance for the Council for the period ending 30 June 2020.

5.0 Consultation

None

6.0 Alternative Options and Reasons for Rejection

6.1 The following alternative options have been identified and rejected for the reasons as set out below.

Option 1: To request further information on the performance reported.

7.0 Implications

Financial and Resource Implications

7.1 There are no financial implications arising directly from any outcome of this report.

Comments checked by:
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Legal Implications

7.2 There are no legal implications arising directly from any outcome of this report.

Comments checked by:
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Risk Management Implications

7.3 It is essential that this report is considered by the Audit Committee as it demonstrates that the risk of not complying with the Council's Treasury Management Policy has been avoided.

Comments checked by:
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8.0 Decision Information

Wards Affected
All wards are affected

Links to Corporate Plan and Policy Framework
Links to all areas of Corporate Plan

Lead Councillor
Councillor Peter Rawlinson – Portfolio Holder for Finance, Performance and Governance

Document Information

Appendix No	Title
Appendix 1	Schedule of Investments – EXEMPT
Background Papers	
None	
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