**Manchester City Council**
**Report for Information**

**Report to:** Audit Committee – 26 July 2022

**Subject:** Treasury Management Outturn Report 2021-22

**Report of:** Deputy Chief Executive and City Treasurer

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## Summary

To report the Treasury Management activities of the Council during the financial year 2021-22.


## Recommendation

The Audit Committee is asked to note the contents of the report.

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## Wards Affected:

Not Applicable

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**Background documents (available for public inspection):**

The following documents disclose important facts on which the report is based and have been relied upon in preparing the report. Copies of the background documents are available up to 4 years after the date of the meeting. If you would like a copy please contact one of the contact officers above.

Treasury Management Strategy Statement 2021/22, including Borrowing Limits and Annual Investment Strategy (Executive – 16th February 2022, Resource and Governance Scrutiny Committee – 28th February 2022, Council – 4th March 2022)

## 1 Introduction and Background

1.1 Treasury Management in Local Government is regulated by the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management in Local Authorities (the Code). The City Council has adopted the Code and complies with its requirements. A primary requirement of the Code is the formulation and agreement by full Council of a Treasury Policy Statement which sets out Council, Committee and Chief Financial Officer Responsibilities, and delegation and reporting arrangements.

1.2 CIPFA amended the CIPFA Treasury Management in the Public Services Code of Practice in late 2011. The revised Code recommended local authorities include, as part of their Treasury Management Strategy Statement, the requirement to report to members at least twice a year on the activities of the Treasury Management function. This report, along with the Interim Treasury Management report received by the Audit Committee on the 23rd November 2021 therefore ensures that the Council meets the requirements of the Strategy, and therefore the Code.

1.3 Treasury Management in this context is defined as:
'*The management of the organisation's 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*'.

1.4 This outturn report covers:

Section 1: Introduction and Background
Section 2: Portfolio Position as at 31st March 2022
Section 3: Review of Economic Conditions 2021-22
Section 4: Treasury Borrowing in 2021-22
Section 5: Compliance with Prudential Indicators and Treasury Limits
Section 6: Investment Strategy for 2021-22
Section 7: Temporary Borrowing and Investment for 2021-22
Section 8: Current Market Conditions and Forward Fixing
Section 9: Conclusion

Appendix 1: Public Works Loans Board (PWLB) Interest Rates
Appendix 2: Treasury Management Prudential Indicators
Appendix 3: Review of Economic Conditions, provided by advisors
Appendix 4: Glossary of Terms

## 2 Portfolio Position as at 31st March 2022

2.1 As outlined in the approved Treasury Management Strategy Statement (TMSS) for 2021/22 it was anticipated that there would be a need to undertake some permanent borrowing in 2021/22 to fund the capital programme and to replace some of the internally borrowed funds.

2.2 The Council has faced a challenging market environment, with volatile interest rates amid global inflation concerns and the enduring fiscal impact of the pandemic.

2.3 During the year, the temporary borrowing taken last year matured and has been refinanced with long term debt from the Public Works Loan Board (PWLB). The Council's debt position at the beginning and the end of the financial year shown in the table below. The gross debt is significantly below both the Council's capital financing requirement, which is its underlying need to borrow, and the authorised limit (the maximum amount it is allowed to borrow) shown in appendix 2.

| Loan Type | 31 March 2021 | | | | 31 March 2022 | | | |
|---|---|---|---|---|---|---|---|---|
| | GF | HRA | Principal | Avg. Rate | GF | HRA | Principal | Avg. Rate |
| | £m | £m | £m | % | £m | £m | £m | % |
| | | | | | | | | |
| PWLB | 150.0 | 0.0 | 150.0 | 2.45 | 400.0 | 0.0 | 400.0 | 2.00 |
| Temporary Borrowing | 177.2 | 0.0 | 177.2 | 0.67 | 10.7 | 0.0 | 10.7 | 0.34 |
| Market Loans | 336.8 | 61.9 | 398.7 | 4.48 | 334.2 | 61.4 | 395.7 | 4.47 |
| Stock | 0.9 | 0.0 | 0.9 | 4.00 | 0.9 | 0.0 | 0.9 | 4.00 |
| Government Lending | 23.5 | 0.0 | 23.5 | 0.00 | 19.4 | 0.0 | 19.4 | 0.00 |
| **Gross Total** | **688.4** | **61.9** | **750.3** | **3.03** | **765.2** | **61.4** | **826.7** | **3.11** |
| | | | | | | | | |
| Temporary Deposits | (27.4) | 0.0 | (27.4) | 0.03 | (122.7) | 0.0 | (122.7) | 0.47 |
| Internal Balances (GF/HRA) | 58.4 | (58.4) | 0.00 | 0.00 | 49.5 | (49.5) | 0.0 | 0.00 |
| | | | | | | | | |
| **Net Total** | **719.4** | **3.5** | **722.9** | **-** | **692.0** | **11.9** | **703.9** | **-** |

2.4 The temporary borrowing and deposit figures fluctuate daily to meet the ongoing cash flow requirements of the Council. The figures for these categories in the table above are therefore only a snapshot at a particular point in time.

2.5 Throughout the financial year 2021/22 a total of £319.4m of new borrowing was taken and a total of £243.0m matured. The net movement in temporary loans was a repayment of £166.5m, with long term PWLB borrowing of £250.0m taken. Market debt of £3.0m matured during the year and was repaid. Total Government borrowing dropped from £23.5m to £19.4m due to the planned repayment of £4.1m SALIX loans.

2.6 Total Gross Debt has therefore increased by £76.4m throughout the financial year 2021/22.

## 3 Review of Economic Conditions 2021-22

3.1 The financial year provided challenging market conditions, as the economy transitioned away from one of historic low interest rates towards a more active monetary policy to tackle inflation pressures. The Bank of England raised the base rate from 0.1% to 0.25% in December, before increasing by 25 basis points again in both February and March to reach 0.75% by the end of the financial year. Subsequently the bank has raised the rate twice more, with base rate at 1.25% by June 2022, a level not seen since early February 2009 at the start of the global financial crisis.

3.2 Appendix 3 provides a more detailed review of the economic situation.

## 4 Treasury Borrowing in 2021-22

### PWLB

4.1 PWLB interest rates during the year are illustrated in the table below, which sets out the low points and high points during the year for key maturity periods. This is also illustrated in the graph at Appendix 1. All maturity periods saw an increase in rates towards the end of the financial year.

| **PWLB Standard Borrowing Rates 2021-22 for 1 to 50 years** | | | | | |
|---|---|---|---|---|---|
| | **1 Year** | **5 Year** | **10 Year** | **25 Year** | **50 Year** |
| **Low** | 0.78% | 1.05% | 1.39% | 1.67% | 1.25% |
| **Date** | 08/04/2021 | 08/07/2021 | 05/08/2021 | 08/12/2021 | 09/12/2021 |
| **High** | 2.03% | 2.37% | 2.52% | 2.75% | 2.49% |
| **Date** | 15/02/2022 | 28/03/2022 | 28/03/2022 | 23/03/2022 | 28/03/2022 |
| **Average** | 1.13% | 1.45% | 1.78% | 2.10% | 1.85% |

4.2 During the year the Council borrowed £250m from the PWLB, as detailed in the table below, at an average rate of c. 1.73%. This was to refinance the temporary borrowing taken last year, and ultimately is to fund the Council's capital programme.

| Maturity Date | Value (£m) | Interest Rate (%) |
|---|---|---|
| 17/06/2055 | 15 | 2.05 |
| 17/06/2062 | 25 | 1.99 |
| 17/06/2063 | 25 | 1.99 |
| 17/06/2064 | 20 | 1.98 |

| | | |
|---|---|---|
| 17/06/2068 | 20 | 1.94 |
| 08/12/2068 | 25 | 1.38 |
| 17/06/2069 | 15 | 1.93 |
| 08/12/2069 | 25 | 1.37 |
| 17/06/2070 | 15 | 1.92 |
| 08/12/2070 | 25 | 1.36 |
| 17/06/2071 | 15 | 1.91 |
| 08/12/2071 | 25 | 1.34 |
| Total | 250 | 1.73 |

4.3 A number of loans were taken out, with maturities spread over a number of years to allow the repayments to be manageable, and closer aligned to the likely MRP charges that the Council is expected to make in the years that the loans are due to mature.

4.4 For any additional borrowing required further market assessments will be undertaken and the risks and benefits of any approach will be reviewed before any decision is made.

**Temporary Borrowing**

4.5 As noted above, the temporary borrowing previously agreed became due for repayment during the financial year, with a c. £166.5m net repayment. This was predominantly refinanced through the PWLB debt taken during the year.

**Salix Borrowing**

4.6 Salix Finance Ltd provides interest-free Government funding to the public sector to improve their energy efficiency, reduce carbon emissions and lower energy bills. The supported scheme in relation to LED lighting Council projects will be repaid by 1st April 2023.

4.7 During the year, the Council made scheduled repayments of £4.1m, bringing the total value of Salix debt to £10.9m on 31st March 2022.

4.8 The borrowing strategy will remain under constant review to support achieving value for money for the Council whilst balancing the treasury risks that any approach will create.

## 5 Compliance with Prudential Indicators and Treasury Limits

5.1 The Council operated within the updated prudential indicators, and performance against these is shown in Appendix 2.

5.2 The Council also sets an operational limit on the cleared balance that is left within the Council's current accounts. The limit is aimed at minimising the cash held in these accounts which attracts no interest and thereby maximises the investment return for the authority. The limit is set at £400k and this was met during the financial year with the exception of the breaches described below.

5.3 Where the limit is breached it means that the Council either incurred interest costs due to being in an overdraft position or lost potential investment income due to excess cash not being invested. It is important to note that any such breach will be rectified the following working day, and therefore the financial impact is minimised.

5.4 During the period 1st April to 31th March 2022 there were fifteen breaches of the daily £0-400k limit on the Barclays current account.

i. On eight occasions, Treasury Management purposely kept the current account in surplus following a payment made in error by the bank for the amount of £3.3m, the limit was breached for 8 days while the bank investigated.

ii. On the seven occasions, the limit was breached due to various late afternoon receipts which the Treasury Management team had not been made aware of. Where possible, officers are asked to inform the team of any expected receipts or payments over £50k in order to efficiently manage cash.

5.5 Each breach was notified to the Deputy Chief Executive and City Treasurer and action taken on the following working day to bring balances back within approved limits. No additional costs arose as a result, other than the opportunity cost incurred of not investing the surplus cash, which in the current interest market is minimal.

## 6 Investment Strategy for 2021-22

6.1 The Treasury Management Strategy Statement (TMSS) for 2021-22 was approved by Executive on 16th February 2022. The Council's Annual Investment Strategy, which is incorporated in the TMSS, outlines the Council's investment priorities as:

(a) the security of capital; and
(b) the liquidity of investments.

6.2 The Strategy details the investment limits the Council has for counterparties, based on an assessment of their creditworthiness, to a maximum of £20m for any single organisation other than the UK Government or the Greater

Manchester Combined Authority. It also provides information on the types of investment instruments that the Council will use, including bank deposits, deposits with other local authorities and the UK Government, and money market funds (MMFs).

6.3 The Council continues to operate a total of five MMFs with an upper limit of £15.0m per fund. The Council also holds ongoing contingency call accounts with two major banks to help maintain liquidity.

6.4 The current strategy means that a significant proportion of the Council's investments are with the chosen five MMFs, the Debt Management Office (DMO), and other Local Authorities. This highlights the relatively low rate of credit risk that the Council takes when investing.

6.5 It should be noted that, whilst seeking to broaden the investment base, officers will continue to seek high quality investments to limit the level of risk taken by the Council. It is not expected that the measures considered above will have a significant impact on the rates of return the Council currently achieves.

6.6 During the financial year the Council's temporary cash balances have been managed by the Deputy Chief Executive and City Treasurer in-house and invested with those institutions listed in the Council's Approved Lending List. Officers can confirm these institutions meet the security criteria set out in the Annual Investment Strategy agreed at Executive in February and Council in March.

## 7 Temporary Borrowing and Investment for 2021-22

7.1 Compared to the previous twelve months, the Council's cash flows have been far more predictable compared to the early periods of the pandemic. Liquidity has remained a key focus for the treasury management function, alongside the refinancing of the temporary borrowing.

7.2 During the first half of the financial year investment rates remained at near their historic lows. However, since December inflation concerns have seen the Bank of England raise the bank rate from 0.1% to 0.75% by year end, and now 1.25%, which has seen investment returns rise. For the Council, the average level of funds available for investment purposes in 2021/22 was £64.9m. These funds were available on a temporary basis and the level of funds available was mainly dependent on the timing of precept payments, the receipt of grants, payments of COVID-19 related grants, progress on the capital programme, and working capital.

7.3 As noted, a significant amount of short term borrowing was repaid during the year and refinanced with long term debt. The average level of temporary borrowing in this period was £40.1m, but was £10.7m by year end.

7.4 Detailed in the table below is the temporary investment and borrowing undertaken by the Council. Historically this has been compared to the average equivalent London Inter-Bank investment or borrowing rate (LIBOR/LIBID), but following changes implemented to the UK financial markets these rates are no longer calculated. The benchmark rate is now the Sterling Overnight Index Average (SONIA), being the overnight rate of interest banks pay to borrow sterling overnight, unsecured, from other financial institutions.

7.5 This change means that the benchmark rate is now based on observable data, whereas LIBOR/ID was based on information provided by major banks. The impact on SONIA of changes in the Bank of England bank rate is far more immediate, particularly when compared to the investment instruments that the Council uses where there is a time lag between bank rate changing and the rate offered for the instrument reflecting that change. As interest rates have risen during the final part of the 21/22 financial year it has therefore taken some time for the Council's investments to rise to similar levels.

7.6 As illustrated, the Council under performed the benchmark by 4 basis points on investments. The treasury team will continue to search for stronger inter-Local Authority market rates and Money Market Funds which could improve return without compromising security of the funds.

7.7 The temporary borrowing portfolio consisted of loans with various investment tenors ranging from 14 day notice terms to fixed two-year maturities. The average cost was therefore higher by 41 basis points when compared to the overnight benchmark.

| | Average temporary investment /borrowing | Net Return/Cost | Benchmark Return / Cost * |
|---|---|---|---|
| Temporary Investments | £65.0m | 0.10% | 0.14% |
| Temporary Borrowing | £40.2m | 0.55% | |

* *Average SONIA 1st April 21 to 31st March 22*

7.8 None of the institutions in which investments were made, such as banks, local authorities and MMFs, showed any difficulty in repaying investments and interest during the year. The list of institutions in which the Council invests is kept under continuous review.

**8 Current Market Conditions and Forward Fixing**

8.1 As noted above, the Bank of England base rate has continued to rise in the early part of the 2022/23 financial year which, along with inflation concerns across the globe, has caused interest rates to rise.

8.2 This means that any debt taken by the Council in this market environment is likely to be at rates significantly higher than those shown above for the debt taken in 2021/22.

8.3 There is significant volatility in interest rates, and the timing of further borrowing will be important to seek to minimise interest costs for the duration of those loans. Officers keep debt markets under constant review, working with the Council's treasury advisors and financial market brokers to examine potential debt options. One of the options currently being offered by major financial institutions is the opportunity to "forward fix" debt, by agreeing to take debt at a point in the future at an interest rate fixed now. This approach gives interest rate certainty, but avoids the cost of carry associated with taking debt before it is needed.

8.4 In the Treasury Management Strategy for 2022/23 the potential for forward fixing was noted, but as rate forecasts at the time of writing were relatively benign it was not expected that forward fixing would provide value for money.

8.5 The changes in rates noted above, and the ongoing uncertainty across global financial markets, means that this view has changed, and forward fixing may now provide an opportunity to reduce future interest rate risk and give cost certainty.

8.6 Officers will continue to review debt market options, with a specific focus on forward fixing opportunities, and will report to members through the interim and outturn treasury management reports on any further borrowing taken.

## 9 Conclusion

9.1 Financial markets during the 2021/22 financial year saw significant changes, as inflationary pressures across the globe saw central banks raise rates for the first-time post-pandemic. The Council was able to take advantage of the low interest rates available on debt during the year to secure long term financing and has continued to ensure security and liquidity in its investments.

9.2 The current borrowing position reflects the strong balance sheet of the Council. It enables net interest costs to be minimised and reduces credit risk by making temporary use of internal borrowing (reserves, provisions, positive cash flows, etc). The Council's policy remains to keep cash as low as possible and not to borrow in advance of need for capital purposes.

9.3 It is important to note that this strong balance sheet position is not without risk, and with interest rates rising the timing and structure of future debt financing will be important in sustaining this position.

9.4 Proactive treasury management during the year has enabled the Council to achieve an average net return on investments of 0.10%, which although below the average SONIA rate for the year is higher than the rate offered by the DMO, which is the default option if there are no other investment opportunities based on the credit criteria set.