APPENDIX 1

CYNGOR
Sir y Fflint
Flintshire
COUNTY COUNCIL

FLINTSHIRE COUNTY COUNCIL

TREASURY MANAGEMENT

DRAFT ANNUAL REPORT 2020/21

1.00 INTRODUCTION

The Council approved the Treasury Management Strategy 2020/21 (the Strategy) including key indicators, limits and an annual investment strategy on 18th February 2020.

The Strategy was produced based on the 2017 edition of the *CIPFA Treasury Management in the Public Services: Code of Practice*.

The purpose of this report is to review the outcomes from 2020/21 treasury management operations and compare these with the Strategy.

Treasury management comprises the management of the local authority's 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.

2.00 ECONOMIC & INTEREST RATE REVIEW 2020/21

This is provided by Arlingclose Ltd, the Council's treasury management advisors.

2.01 Economic background

The coronavirus pandemic dominated 2020/21, leading to almost the entire planet being in some form of lockdown during the year. The start of the financial year saw many central banks cutting interest rates as lockdowns caused economic activity to grind to a halt. The Bank of England cut the Bank Rate to 0.1% and the UK government provided a range of fiscal stimulus measures, the size of which has not been seen in peacetime.

Some good news came in December 2020 as two COVID-19 vaccines were given approval by the UK Medicines and Healthcare products Regulatory Agency (MHRA). The UK vaccine rollout started in earnest; over 31 million people had received their first dose by 31st March.

A Brexit trade deal was agreed with only days to spare before the 11pm 31st December 2020 deadline, having been agreed with the European Union on Christmas Eve.

The Bank of England (BoE) held Bank Rate at 0.1% throughout the year but extended its Quantitative Easing programme by £150 billion to £895 billion at its November 2020 meeting. In its March 2021 interest rate announcement, the BoE noted that while GDP would remain low in the near-term due to COVID-19 lockdown restrictions, the easing of these measures means growth is expected to recover strongly later in the year. Inflation is forecast to increase in the near-term and while the economic outlook has improved there are downside risks to the forecast, including from unemployment which is still predicted to rise when the furlough scheme is eventually withdrawn.

Government initiatives supported the economy and the Chancellor announced in the 2021 Budget a further extension to the furlough (Coronavirus Job Retention) scheme until September 2021. Access to support grants was also widened, enabling more self-employed people to be eligible for government help. Since March 2020, the government schemes have helped protect more than 11 million jobs.

Despite the furlough scheme, unemployment still rose. Labour market data showed that in the three months to January 2021 the unemployment rate was 5.0%, in contrast to 3.9% recorded for the same period 12 months ago. Wages rose 4.8% for total pay in nominal terms (4.2% for regular pay) and was up 3.9% in real terms (3.4% for regular pay). Unemployment is still expected to increase once the various government job support schemes come to an end.

Inflation has remained low over the 12 month period. Latest figures show the annual headline rate of UK Consumer Price Inflation (CPI) fell to 0.4% year/year in February, below expectations (0.8%) and still well below the Bank of England's 2% target. The Office for National Statistics' preferred measure of CPIH, which includes owner-occupied housing, was 0.7% year/year (1.0% expected).

After contracting sharply in Q2 (Apr-Jun) 2020 by 19.8% q/q, growth in Q3 and Q4 bounced back by 15.5% and 1.3% respectively. The easing of some lockdown measures in the last quarter of the calendar year enabled construction output to continue, albeit at a much slower pace than the 41.7% rise in the prior quarter. When released, figures for Q1 (Jan-Mar) 2021 are expected to show a decline given the national lockdown.

After collapsing at an annualised rate of 31.4% in Q2, the US economy rebounded by 33.4% in Q3 and then a further 4.1% in Q4. The US recovery has been fuelled by three major pandemic relief stimulus packages totalling over $5 trillion. The Federal Reserve cut its main interest rate to between 0% and 0.25% in March 2020 in response to the pandemic and it has remained at the same level since. Joe Biden became the 46th US president after defeating Donald Trump.

The European Central Bank maintained its base rate at 0% and deposit rate at -0.5% but in December 2020 increased the size of its asset purchase scheme to €1.85 trillion and extended it until March 2022.

2.02 Financial markets

Monetary and fiscal stimulus helped provide support for equity markets which rose over the period, with the Dow Jones beating its pre-crisis peak on the back of outperformance by a small number of technology stocks. The FTSE indices performed reasonably well during the period April to November, before being buoyed in December by both the vaccine approval and Brexit deal, which helped give a boost to both the more internationally focused FTSE 100 and the more UK-focused FTSE 250, however they remain lower than their pre-pandemic levels.

Ultra-low interest rates prevailed throughout most of the period, with yields generally falling between April and December 2020. From early in 2021 the improved economic outlook due to the new various stimulus packages (particularly in the US), together with the approval and successful rollout of vaccines, caused government bonds to sell off sharply on the back of expected higher inflation and increased uncertainty, pushing yields higher more quickly than had been anticipated.

The 5-year UK benchmark gilt yield began the financial year at 0.18% before declining to -0.03% at the end of 2020 and then rising strongly to 0.39% by the end of the financial year. Over the same period the 10-year gilt yield fell from 0.31% to 0.19% before rising to 0.84%. The 20-year declined slightly from 0.70% to 0.68% before increasing to 1.36%.

1-month, 3-month and 12-month SONIA bid rates averaged 0.01%, 0.10% and 0.23% respectively over the financial year.

The yield on 2-year US treasuries was 0.16% at the end of the period, up from 0.12% at the beginning of January but down from 0.21% at the start of the financial year. For 10-year treasuries the end of period yield was 1.75%, up from both the beginning of 2021 (0.91%) and the start of the financial year (0.58%).

German bund yields continue to remain negative across most maturities.

3.00 BORROWING REQUIREMENTS AND DEBT MANAGEMENT

3.01 PWLB (Public Works Loans Board) Certainty Rate

The Council qualified for the PWLB Certainty Rate, allowing the authority to borrow at a reduction of 20 basis points on the Standard Rate for a further 12 months from 1st November 2020.

3.02 Borrowing Activity in 2020/21.

The total long term borrowing outstanding, brought forward into 2020/21 was £291.3 million.

	Balance 01/04/2020 £m	Debt Maturing £m	New Debt £m	Balance 31/03/2021 £m
Capital Financing Requirement	**350.3**	(7.1)	8.5	**351.7**
Short Term Borrowing	53.0	(53.0)	58.0	58.0
Long Term Borrowing	291.3	(11.7)	9.4	289.0
TOTAL BORROWING	**344.3**	**(64.7)**	**67.4**	**347.0**
Other Long Term Liabilities	4.5	(0.6)	0.0	3.9
TOTAL EXTERNAL DEBT	**348.8**	**(65.3)**	**67.4**	**350.9**
Increase/(Decrease in Borrowing (£m)	-	-	2.1	

The Council's Capital Programme is financed by a combination of capital receipts and grants, capital expenditure charged to the revenue account (CERA) and borrowing. The borrowing strategy in recent years, in accordance with advice received from the Council's treasury management advisors, Arlingclose, has been to use existing cash balances and short term borrowing to confirm the long term borrowing requirement. This is to ensure that the Council does not commit to long term borrowing too early and borrow unnecessarily which will be costly. This is balanced against securing low interest costs and achieving cost certainty over the period for which the funds are required so as not to compromise the long term stability of the portfolio.

Short term borrowing continued to be available throughout the year at much lower rates than long term borrowing and was utilised as far as possible without exposing the Council to excessive refinancing risk. The total short term (temporary) borrowing as at 31st March 2021 was £58m with an average rate of 0.10%.

The relative costs and benefits of internal / short term borrowing and long term borrowing were monitored closely, in conjunction with Arlingclose, throughout the year. The Council continues to have a long term borrowing requirement and as PWLB long term rates remained low during the year the following loans were taken out:

Start Date	Maturity Date	Amount	Rate	Loan Type
02 Nov 2020	02 Nov 2057	£1.406m	2.53%	Annuity
16 Dec 2020	16 Dec 2042	£5.0m	1.16%	EIP
9 Feb 2021	9 Feb 2058	£2.553m	1.79%	Annuity

£3.96m of these loans have been on-lent to NEW Homes, the Council's wholly owned subsidiary, to fund the building of affordable homes in Flintshire.

At 31st March 2021, £264.9m of the Council's loans were in the form of fixed rate with the PWLB, £18.95m were variable rate in the form of LOBO's (Lender Option Borrower Option) and £5.15m were interest free loans from the Government, available for specific schemes. The Council's average rate for long term borrowing was 4.61%.

The Council's underlying need to borrow as measured by the Capital Financing Requirement (CFR) as at 31st March 2021 was £351.7m. The Council's total external debt was £350.9m.

3.03 Loans at Variable Rates

The Council repaid its £10m PWLB variable rate loan in May 2020.

3.04 Lender Option Borrower Option loans (LOBOs)

The Council holds £18.95m of LOBOs, loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. All of these LOBOs had options during the year, none of which were exercised by the lender.

3.05 Debt Rescheduling

Options for debt rescheduling were explored in conjunction with our treasury management advisors. The premium charged for early repayment of PWLB debt remained relatively expensive for the loans in the Council's portfolio and therefore unattractive for debt rescheduling activity. As a consequence no rescheduling activity was undertaken.

The Corporate Finance Manager, in conjunction with the Council's treasury management advisors, will continue to review any potential opportunities for restructuring the Council's debt in order to take advantage of potential savings as interest rates change and to enhance the balance of the long term portfolio (amend the maturity profile and/or the balance of volatility).

4.00 INVESTMENT ACTIVITY

4.01 Guidance

The Welsh Government's Investment Guidance gives priority to security and liquidity and the Council's aim is to achieve a yield commensurate with these principles.

4.02 Investment Activity in 2020/21

Summary of investments as at 31st March 2021.

Country	Total	<1 month	1 –12 months	>12 months
	£m	%	£m	£m
UK BANKS	4.0	4.0		
UK BUILDING SOCIETIES				
OVERSEAS				
MMF's	22.3	22.3		
LOCAL AUTHORITIES	5.0	5.0		
DMO	20.0	10.00	10.00	
TOTAL	**51.3**	**41.3**	**10.00**	**0.0**

As none of these investments were greater than three months they are classified as cash in the Council's Balance Sheet.

Security of capital remained the Council's main investment objective. This was maintained by following the Council's counterparty policy as set out in its Strategy for 2020/21. Investments during the year included:

- Deposits with the Debt Management Office
- Deposits with other local authorities
- Investments in AAA-rated Low Volatility Net Asset Value (LVNAV) money market funds
- Call accounts and deposits with banks and building societies

4.03 Credit Risk

The Council assessed and monitored counterparty credit quality with reference to credit ratings; credit default swaps; GDP of the country in which the institution operates; the country's net debt as a percentage of GDP, and share price. The minimum long-term counterparty credit rating determined by the Council for the 2020/21 treasury strategy was A-/A-/A3 across rating agencies Fitch, S&P and Moody's.

4.04 Counterparty Update

After spiking in March 2020, credit default swap spreads declined over the remaining period of the year to broadly pre-pandemic levels, suggesting financial markets consider credit risk in the banking sector to have reduced. The gap in spreads between UK ring fenced and non-ring fenced entities remains with the ring-fenced entities typically benefiting from their lower risk business models and balance sheets.

Credit rating actions to the period ending September 2020 have been covered in previous outturn reports. Subsequent credit developments include Moody's downgrading the UK sovereign rating which then impacted a number of other UK institutions, banks and local government. In the last quarter of the financial year S&P upgraded Clydesdale Bank's rating and revised Barclays outlook to stable (from negative) while Moody's affirmed HSBC's long-term rating.

The vaccine approval and subsequent rollout programme are positive for the financial services sector in general, but there remains much uncertainty around the extent of the losses banks and building societies will suffer due to the economic slowdown from the pandemic. The Council's counterparty list recommended by treasury management advisors Arlingclose remains under constant review, but at the end of the period no changes had been made to the names on the list or the recommended maximum duration of 35 days.

4.05 Liquidity

In keeping with the WG's Guidance on Investments, the Council maintained a sufficient level of liquidity through the use of money market funds and call accounts.

4.06 Yield

The UK Bank Rate remained at 0.10% throughout the year. Short term money market rates also remained at very low levels which continued to have a significant impact on investment income. The low rates of return on the Council's short-dated money market investments reflect prevailing market conditions and the Council's objective of optimising returns commensurate with the principles of security and liquidity.

The Council's budgeted investment income for the year had been prudently estimated at £75k. The average cash balance was £41.1m during the period and interest earned was £12.3k, at an average interest rate of 0.03%. This was offset by reductions in corresponding borrowing costs during the year.

4.07 Loans to NEW Homes

The loans to NEW Homes do not meet the definition of an investment and are not therefore included in the Council's investment figures below. They are classed as capital expenditure.

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5.00 COMPLIANCE

The Council can confirm that it has complied with its Prudential Indicators for 2020/21. These were approved by Council as part of the Treasury Management Strategy on 18th February 2020.

In compliance with the requirements of the CIPFA Code of Practice this report provides members with a summary report of the treasury management activity during 2020/21. None of the Prudential Indicators have been breached and a prudent approach has been taking in relation to investment activity with priority being given to security and liquidity over yield.

The treasury function operated within the limits detailed in the Treasury Management Policy and Strategy Statement 2020/21.

6.00 OTHER ITEMS

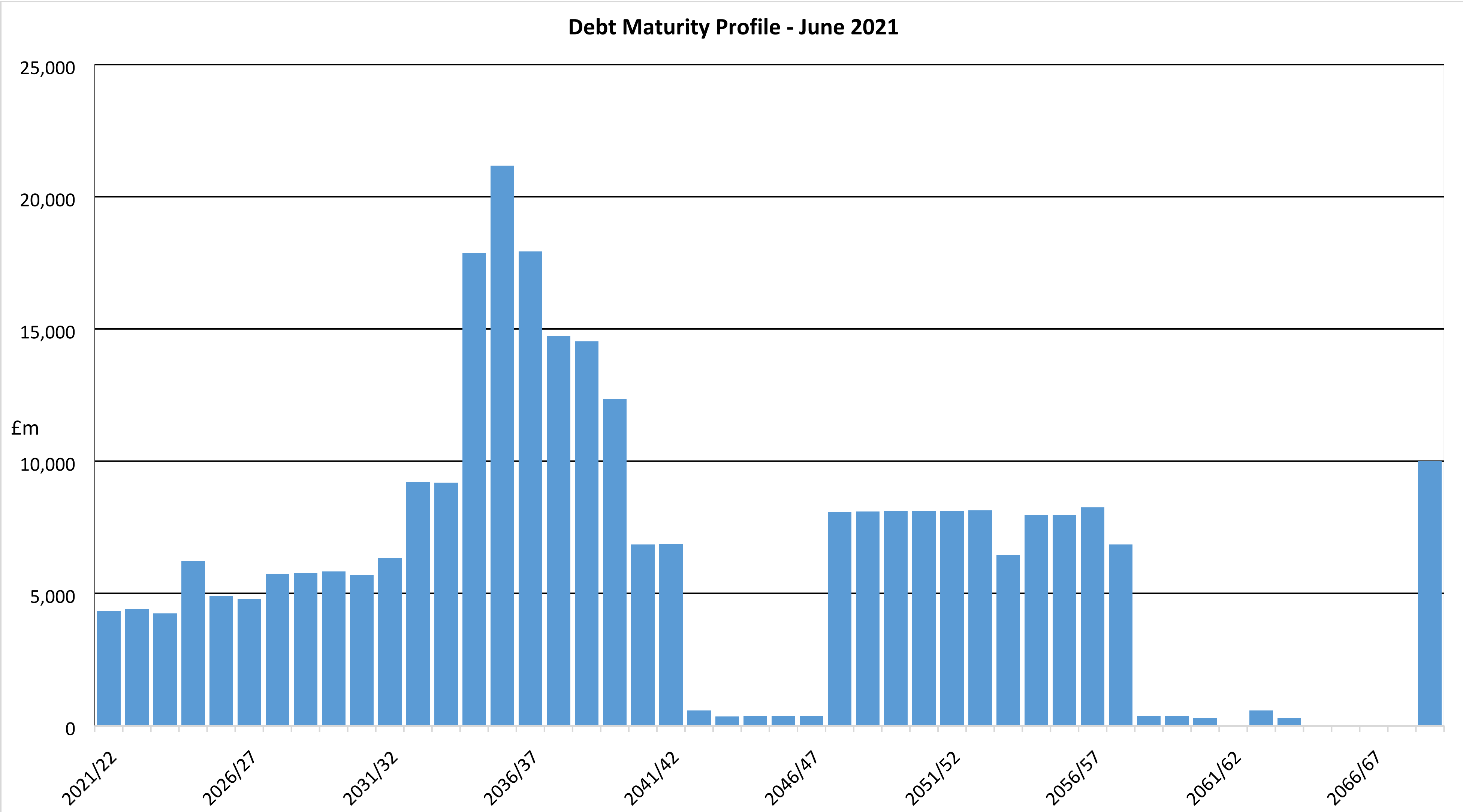
The following were the main treasury activities during 2020/21

- The Council's Audit Committee received a Mid-Year Report on 18th November 2020.
- Quarterly update reports were presented to the Audit Committee.
- The 2021/22 Investment Strategy Statement was approved by Council on 16th February 2021.
- The Council's cash flow was managed on a daily basis. During the year the Council acted both as a borrower and as a lender and was a net borrower over the year in question. The maximum investments the Authority had on deposit at any one time were £80.5m and the maximum long-term borrowing at any one time was £290.7m.

7.00 CONCLUSION

The treasury management function has operated within the statutory and local limits detailed in the 2020/21 Treasury Management Strategy.

The Policy was implemented in a pro-active manner with security and liquidity as the focus.


Debt Maturity Profile - June 2021
£m
25,000
20,000
15,000
10,000
5,000
0
2021/22
2026/27
2031/32
2036/37
2041/42
2046/47
2051/52
2056/57
2061/62
2066/67