ADUR & WORTHING COUNCILS

Joint Governance Committee
29 July 2021
Agenda Item 6

Joint Strategic Committee
7 September 2021

Key Decision : No
Ward(s) Affected: All

ANNUAL TREASURY MANAGEMENT REPORT 2020-21 FOR ADUR DISTRICT COUNCIL AND WORTHING BOROUGH COUNCIL

REPORT BY THE DIRECTOR FOR DIGITAL AND RESOURCES

EXECUTIVE SUMMARY

1. PURPOSE

1.1 This report asks Members to note the Treasury Management performance for Adur and Worthing Councils for 2020/21 as required by regulations issued under the Local Government Act 2003.

2. RECOMMENDATIONS

2.1 **Recommendation One**
The Joint Governance Committee is recommended to note the annual report and to refer any comments or suggestions to the next meeting of the Joint Strategic Committee on 7th September 2021.

2.2 **Recommendation Two**
The Joint Strategic Committee is recommended to note the annual report.

3. CONTEXT

3.1 Treasury Management is:

"The management of the local authority'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".

3.2 This report details the treasury management activities and portfolio positions for the 2020/21 financial year for Adur District Council and Worthing Borough Council. The

Councils are required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2020/21. This report meets the requirements of both the CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

3.3 This is the last of three treasury management reports that the Councils are required to consider during the financial year:

- Before the beginning of the financial year, the first report, the Treasury Management Strategy and Annual Investment Strategy, seeks approval for the Councils' approach to the management of investments and the borrowing of funds for the forthcoming year. This report details how the Councils will manage risk in their treasury activities and was approved by Worthing Council on the 18th February 2020 and by Adur Council on the 20th February 2020 .
- This is followed by a mid year review of performance against the approved strategies (JGC 24th November 2020, JSC 1 December 2020).
- At the year end, there is an annual report which confirms actual performance for the year (this report) to be submitted by the 30th September.

3.4 There is a clear regulatory environment governing the Council's investment and treasury activities. The Local Government Act 2003 requires that the Council complies with the Prudential Code for Capital Finance. This is a framework established to support local strategic planning, local asset management planning and proper option appraisal. The objectives of the Prudential Code are to ensure, within this clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable. As part of the Prudential Code, indicators are established to ensure that the Council has approved limits on both capital expenditure plans and associated borrowing activity.

3.5 The Councils' Treasury Management Strategy and Annual Investment Strategy place the security of investments as foremost in considering all treasury management dealing. By so doing it contributes towards the Councils' priorities set out in Platforms for our Places.

4. ISSUES FOR CONSIDERATION

4.1 The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury management activities and highlights compliance with the Councils' policies previously approved by members.

4.2 The Annual Report also confirms that the Councils have complied with the requirement under the Code to give scrutiny to all of the above treasury management reports by the Joint Governance Committee and the Joint Strategic Committee before they were reported to the full Councils.

4.3 Member training on treasury management issues was not possible during the year due to the Covid pandemic, but will be arranged during 2021/22 in order to support members' scrutiny role.

5. The Councils' Capital Expenditure and Financing

5.1 The Councils undertake capital expenditure on long-term assets (land, buildings, vehicles, software and equipment). These activities may either be:

- financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Councils' borrowing need; or
- if insufficient financing is available, or a decision is taken not to apply these resources, then capital expenditure will give rise to a borrowing need.

5.2 The actual capital expenditure forms one of the required prudential indicators, because the Councils must ensure that capital expenditure is affordable, approved and monitored. The tables below show the actual capital expenditure and how this was financed. The full explanation of the expenditure and the variances between the budgets and actual expenditure can be found in the Capital Monitoring Reports, but the most significant items are detailed below. There have been some delays in delivery of the capital programme due to the Covid 19 virus. The "current budget" includes subsequent approvals and reprofiled budgets approved during the year.

Adur District Council Total	2019/20 Actual	2020/21 Original Budget	2020/21 Current Budget	2020/21 Actual
Capital expenditure £m	**60.270**	**63.988**	**23.422**	**17.698**
Financed in year £m	**16.502**	**9.785**	**19.464**	**16.220**
Borrowing for capital expenditure £m	**43.768**	**54.203**	**3.958**	**1.478**

The following table shows the General Fund share of the figures in the table above

Adur District Council General Fund	2019/20 Actual	2020/21 Original Budget	2020/21 Current Budget	2020/21 Actual
Capital expenditure £m	**56.411**	**47.220**	**13.946**	**12.512**
Financed in year £m	**12.834**	**4.436**	**12.682**	**12.331**
Borrowing for capital expenditure £m	**43.577**	**42.784**	**1.264**	**0.181**

The following table shows the HRA share of the figures in the table above

Adur District Council HRA	2019/20 Actual	2020/21 Original Budget	2020/21 Current Budget	2020/21 Actual
Capital expenditure £m	**3.859**	**16.768**	**9.476**	**5.186**
Financed in year £m	**3.668**	**5.349**	**6.782**	**3.889**
Borrowing for capital expenditure £m	**0.191**	**11.419**	**2.694**	**1.297**

For Adur, the original budget was revised due to subsequent approvals and re-profiling of budgets, most significantly the reprofiling of the Strategic Property Investment Fund and the impact of Covid 19 on the ability to deliver some projects.

The difference between the current budget and the actual spend is due to:

- re-profiling of £3.543m of the 2020/21 budget into 2021/22
- a net underspend of £2.181m

Worthing Borough Council	2019/20 Actual	2020/21 Original Budget	2020/21 Current Budget	2020/21 Actual
Capital expenditure £m	**64.486**	**69.469**	**16.471**	**17.744**
Financed in year £m	**6.372**	**14.110**	**12.291**	**10.900**
Borrowing for capital expenditure £m	**58.114**	**55.359**	**4.180**	**6.844**

For Worthing, the original budget was revised due to subsequent approvals and re-profiling of budgets, most significantly the reprofiling of the Strategic Property Investment Fund and the impact of Covid 19 on the ability to deliver some projects.

The difference between the current budget and the actual spend is due to:

- net budget brought forward from future years of £1.729m
- an underspend of £0.456m

6. THE COUNCILS' OVERALL BORROWING NEED

6.1 Some of the Councils' capital expenditure is funded immediately by, for example, capital grants, capital receipts from the sale of assets, or from contributions from the revenue budget (capital funded by revenue as approved by statute). Capital expenditure that is not funded by any of these means is described as "the underlying need to borrow" and is known as the Capital Financing Requirement (CFR). The

Councils decide whether or not to borrow these amounts externally, or alternatively to use cash that would otherwise be invested (internal borrowing). The Councils make these decisions based on a number of factors, including the prevailing interest rates for borrowing compared to those for investing, the likelihood of a capital receipt in the near future or a forecast of additional capital grants.

Gross borrowing and the CFR - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Councils should ensure that their gross external borrowing does not, except in the short term, exceed the total of the Capital Financing Requirement in the preceding year (2020/21), plus the estimates of any additional capital financing requirement for the current (2021/22) and next two financial years. This essentially means that the Councils are not borrowing to support revenue expenditure. This indicator allows the Councils some flexibility to borrow in advance of immediate capital needs to take advantage of, say, low interest rates.

The difference between the CFR and the gross borrowing position is termed under or over borrowing. If a Council is under borrowed, it is using some of its internal cash that could otherwise be invested. It can therefore choose to borrow externally up to the CFR so as to take advantage of favourable interest rates. If a Council is over borrowed, it needs to ensure that this position is remedied over a two year period. The Councils have complied with this prudential indicator over a two year period.

This table shows the total CFR and gross borrowing for Adur District Council and the two following tables show the separate figures for the General Fund and the HRA.

Adur District Council Total	31 March 2020 Actual	31 March 2021 Strategy	31 March 2021 Actual
CFR £m	**167.018**	**230.292**	**168.496**
Gross borrowing position £m	**161.802**	**221.709**	**158.936**
Under/(over)funding of CFR £m	**5.216**	**8.583**	**9.560**

Adur District Council General Fund	31 March 2020 Actual	31 March 2021 Strategy	31 March 2021 Actual
CFR General Fund £m	**106.724**	**158.443**	**106.905**
Gross borrowing position £m	**103.350**	**151.702**	**98.460**
Under/(over)funding of CFR £m	**3.374**	**6.741**	**8.445**

Adur District Council HRA	31 March 2020 Actual	31 March 2021 Strategy	31 March 2021 Actual
CFR HRA £m	**60.294**	**71.849**	**61.591**
Gross borrowing position £m	**58.452**	**70.007**	**60.476**
Under/(over)funding of CFR £m	**1.842**	**1.842**	**1.115**

As at 31 March 2021, for Adur District Council, the HRA was under borrowed by £1.115m. The General Fund was under borrowed by £8.445m. Under borrowing results from the use of internal resources to fund capital expenditure, which reduces the amount of interest payable on external borrowing. Interest rates on investments are currently very low in comparison to the rates charged on borrowed sums, so this is a cost-effective strategy reducing the overall net cost of borrowing. The difference between the budgets and the actual CFR figures is due to re-profiling of the Capital budgets as detailed in section 5.2 above.

Worthing Borough Council	31 March 2020 Actual	31 March 2021 Strategy	31 March 2021 Actual
CFR General Fund £m	**129.140**	**188.892**	**135.632**
Gross borrowing position £m	**128.071**	**184.868**	**137.725**
Under/(over)funding of CFR £m	**1.069**	**4.024**	**(2.093)**

Worthing Borough Council was over borrowed by £2.093m at 31 March 2021, mainly due to grants relating to economic regeneration projects which were due to reimburse the Council, but were received after the year end.

6.2 The **authorised limit** is the “affordable borrowing limit” required by s3 of the Local Government Act 2003. Once this has been set, the Councils do not have the power to borrow above this level. The Councils did not breach the authorised limits during the year.

The **operational boundary** is the expected borrowing position of the Councils during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limits not being breached.

Actual financing costs as a proportion of net revenue stream - this indicator identifies the trend in the cost of capital, (borrowing and other long term obligation costs, net of investment income), against the net revenue stream. The costs incurred through capital expenditure are the interest payable on money borrowed and the Minimum Revenue Provision (see section 12), which is a statutory annual revenue charge to reduce the indebtedness of a Council, based on the amount of capital expenditure which has not been funded by capital receipts, grants etc.

Investment income and other income generated from the capital assets purchased or created through the capital programme are deducted from these costs. The net figure is then compared to the Councils' net revenue streams - the income received from grants and taxation as shown in the Statement of Accounts. Consequently if only the costs of the capital programme increase, so will the proportion of financing cost to net revenue stream. If only the net revenue stream increases, then the proportion will reduce. Usually there will be a combination of both factors.

Adur District Council	2020/21
Authorised limit	**£245.000m**
Maximum gross borrowing position during the year	**£165.980m**
Operational boundary	**£230.000m**
Average gross borrowing position	**£160.840m**
Commercial properties financing as a proportion of net revenue stream	**(9.93)%**
Other GF financing costs as a proportion of net revenue stream	**10.03%**
HRA Financing costs as a proportion of net revenue stream	**16.13%**

The figures for the financing as a proportion of net revenue stream differ from the original forecasts, partly due to the high level of grants received to support the Council through the pandemic, which increased the value of the net revenue stream. In addition:

- the forecast for Adur's commercial property financing costs as a proportion of net revenue stream was -19.43%, the negative figure meaning that the income would exceed the financing costs. However the planned additional commercial property purchases did not proceed, resulting in lower net income

- the Other General Fund financing cost proportion is lower than the forecast of 14.82%, due to re-profiling of the capital programme

- the HRA figure is lower than the forecast of 27.24%, due to the re-profiling of the capital programme.

Worthing Borough Council	2020/21
Authorised limit	**£200.000m**
Maximum gross borrowing position during the year	**£137.725m**
Operational boundary	**£195.000m**
Average gross borrowing position	**£131.016m**
Commercial properties financing as a proportion of net revenue stream	**(7.82)%**
Other GF financing costs as a proportion of net revenue stream	**4.95%**

As with Adur, the figures for the financing as a proportion of net revenue stream differ from the original forecasts, partly due to the high level of grants received to support the Council through the pandemic, which increased the value of the net revenue stream. In addition:

- the forecast for Worthing's commercial property financing costs as a proportion of net revenue stream was -19.09%, the negative figure meaning that the income would exceed the financing costs. However the planned additional commercial property purchases did not proceed, resulting in lower net income

- the Other General Fund financing cost proportion is higher than the forecast of 2.53% due to the reduction in returns on investments and the lower than forecast income from General Fund properties

7. TREASURY POSITION AS AT 31 MARCH 2021

7.1 Adur District Council's position at the beginning and end of the year is shown below (nb PWLB refers to the Public Works Loan Board - an arm of the government).

	Principal at 31.03.21 £m	Average Rate of Return	Average Life in Years	Principal at 31.03.20 £m	Average Rate of Return	Average Life in Years
Debt Portfolio						
PWLB (Public Works Loan Board)	(136.052)	2.67%	17.56	(141.540)	2.65%	17.86
Other Borrowing	(22.884)	4.40%	36.23	(20.262)	4.62%	41.45
Total Debt	**(158.936)**			**(161.802)**		
CFR	**168.496**			**167.018**		
(Over)/under borrowing	**9.560**			**5.216**		
Investments						
Bonds	0.030	n/a	n/a	0.029	n/a	n/a
Property Fund	2.708	3.90%	n/a	2.728	4.05%	n/a
Long Term	0.000	n/a	n/a	0.000	n/a	n/a
Short Term	9.000	0.20%	< 1 year	10.665	0.85%	< 1 year
TOTAL INVESTMENTS	**11.738**			**13.422**		
NET DEBT	**(147.198)**			**(148.380)**		

The maturity structure of debt table that follows demonstrates that procedures are in place to prevent the maturity of too much debt in a single period, when only high interest rates may be available for refinancing the debt, if required.

Adur District Council Maturity Structure of Debt	31 March 2021 actual	2020/21 original limits	31 March 2020 actual
under 12 months	6%	20%	7%
12 months and within 24 months	7%	25%	5%
24 months and within 5 years	13%	40%	13%
5 years and within 10 years	24%	70%	24%
10 years and within 20 years	29%	80%	31%
20 years and within 30 years	1%	60%	2%
30 years and within 40 years	7%	60%	7%
Over 40 years	13%	45%	11%

7.2 Worthing Borough Council's position at the beginning and end of the year was as follows:-

	Principal at 31.03.21 £m	Average Rate of Return	Average Life in Years	Principal at 31.03.20 £m	Average Rate of Return	Average Life in Years
Debt Portfolio						
PWLB	(108.725)	1.96%	15.39	(111.071)	1.94%	14.68
Other Borrowing	(29.000)	1.13%	1.12	(17.000)	1.41%	1.34
TOTAL BORROWING	**(137.725)**			**(128.071)**		
CFR	**135.632**			**129.140**		
(Over)/under borrowing	**(2.093)**			**1.069**		
Investments						
Bonds	0.050	n/a	n/a	0.050	n/a	n/a
Property Fund	1.354	3.90%	n/a	1.364	4.05%	n/a
Long Term	2.500	1.00%	1.25	-	-	-
Short Term	6.010	0.03%	< 1 year	8.900	0.66%	< 1 year
TOTAL INVESTMENTS	**9.914**			**10.314**		
NET DEBT	**(127.811)**			**(117.757)**		

The maturity structure of debt table that follows demonstrates that procedures are in place to prevent the maturity of too much debt in a single period, when only high interest rates may be available for refinancing the debt, if required.

Worthing Borough Council Maturity Structure of Debt	31 March 2021 actual	2020/21 original limits	31 March 2020 actual
under 12 months	14%	35%	9%
12 months and within 24 months	16%	35%	15%
24 months and within 5 years	9%	75%	11%
5 years and within 10 years	33%	75%	33%
10 years and within 20 years	15%	75%	21%
20 years and within 30 years	0%	75%	0%
30 years and within 40 years	10%	75%	11%
Over 40 years	3%	75%	0%

7.3 **Investments held by Adur District Council at 31 March 2021:**

Counterparty	Issue Date	Maturity Date	Principal	Current Interest Rate	Long Term Rating
Lloyds Bank 95 day notice	22/07/2020	n/a	£1,000,000	0.05%	A+
Close Bros	10/08/2020	10/08/2021	£1,000,000	0.80%	A-
Close Bros	20/08/2020	06/09/2021	£1,000,000	0.80%	A-
Handelsbanken	16/07/2018	n/a	£3,000,000	0.02%	AA-
CCLA MMF	01/04/2020	n/a	£3,000,000	variable	AAA
CCLA Local Auth Property Fund	25/04/2017	n/a	£2,708,093	variable	n/a
Boom Credit Union & War Bond	06/03/2015	n/a	£29,630	n/a	n/a
TOTAL			**£11,737,723**		

Non-treasury investments

Adur District Council has approved a strategy to invest in properties and developments for economic regeneration purposes. Full details can be found in the Capital Strategy and Commercial Property Investment Strategy. It also holds shares in Boom Credit Union for policy purposes.

7.4 **Investments held by Worthing Borough Council at 31 March 2021:**

Counterparty	Issue Date	Maturity Date	Principal	Current Interest Rate	Long Term Rating
Lloyds Bank 95 day notice	01/03/2021	n/a	£10,000	0.05%	A+
Handelsbanken	01/04/2020	n/a	£3,000,000	0.02%	AA-
Adur District Council	30/06/2020	30/06/2022	£2,500,000	1.00%	n/a
CCLA MMF	01/04/2020	n/a	£3,000,000	variable	AAA
CCLA Local Auth Property Fund	25/04/2017	n/a	£1,354,048	variable	n/a
Boom Credit Union	06/03/2015	n/a	£50,000	n/a	n/a
TOTAL			**£9,914,048**		

Non-treasury investments

Worthing Borough Council has made two loans of £5m each for 10 years to Worthing Homes to support the building of homes. The Council receives £70k per annum net in interest over and above the cost to the Council of borrowing the £10m from the Public Works Loan Board. The loans are fully secured on property.

A loan of £5m was made to GB Met College in January 2020 for 20 years to support local education. The Council received £103k in 2020/21 net in interest over and above the cost to the Council of borrowing the £5m from the Public Works Loan Board. This amount will reduce in future years because the loan is repayable by equal instalments of principal. The loan is fully secured on property.

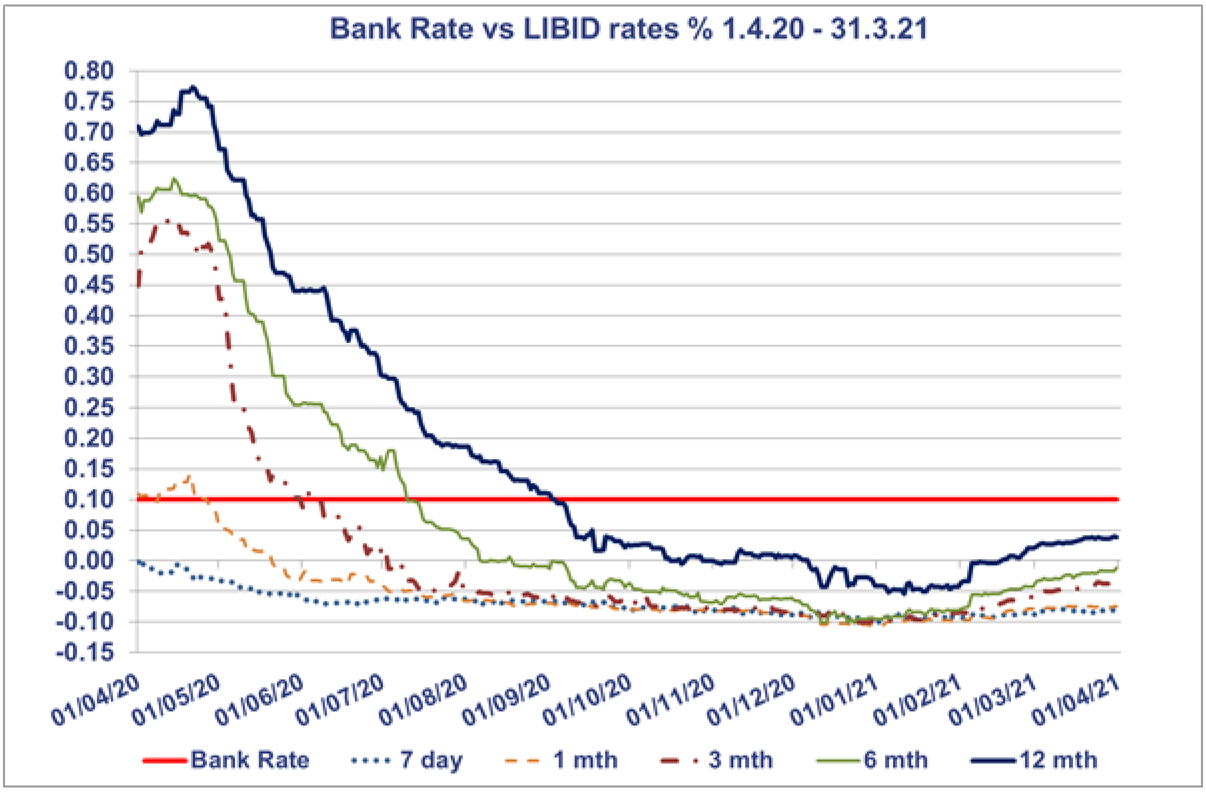
Worthing BC has approved a strategy to invest in properties and developments for economic regeneration purposes. Details can be found in the Capital Strategy and Commercial Property Investment Strategy. Worthing also holds shares in Boom Credit Union for policy purposes.

8. THE STRATEGY FOR 2020/21

Some of the information and tables in the following paragraphs are supplied by the Councils' treasury advisors, Link Asset Services and consists of detailed economic and market information which informed the Councils' treasury management decisions throughout the year.

Investment strategy and control of interest rate risk

(LIBID - London Interbank Bid Rate - the rate bid by banks on deposits)



Investment returns which had been low during 2019/20, plunged during 2020/21 to near zero or even into negative territory. Most local authority lending managed to avoid negative rates and one feature of the year was the growth of inter local authority lending. The expectation for interest rates within the treasury management strategy for 2020/21 was that Bank Rate would continue at the start of the year at 0.75 % before rising to end 2022/23 at 1.25%. This forecast was invalidated by the Covid-19 pandemic bursting onto the scene in March 2020 which caused the

Monetary Policy Committee to cut Bank Rate in March, first to 0.25% and then to 0.10%, in order to counter the hugely negative impact of the national lockdown on large swathes of the economy. The Bank of England and the Government also introduced new programmes of supplying the banking system and the economy with massive amounts of cheap credit so that banks could help cash-starved businesses to survive the lockdown. The Government also supplied huge amounts of finance to local authorities to pass on to businesses. This meant that for most of the year there was much more liquidity in financial markets than there was demand to borrow, with the consequent effect that investment earnings rates plummeted.

While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the financial crisis. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

Investment balances have been kept to a minimum through the agreed strategy of using reserves and balances to support internal borrowing, rather than borrowing externally from the financial markets. External borrowing would have incurred an additional cost, due to the differential between borrowing and investment rates as illustrated in the charts shown above and below. Such an approach has also provided benefits in terms of reducing the counterparty risk exposure, by having fewer investments placed in the financial markets.

9. BORROWING STRATEGY AND CONTROL OF INTEREST RATE RISK

9.1 During most of 2020/21, the Councils maintained an under-borrowed position. This meant that the capital borrowing requirements (the Capital Financing Requirement), was not fully funded with loan debt, as cash supporting the Councils' reserves, balances and cash flow was used as an interim measure. This strategy was prudent as investment returns were very low in relation to the cost of borrowing and minimising counterparty risk on placing investments also needed to be considered.

A cost of carry remained during the year on any new long-term borrowing that was not immediately used to finance capital expenditure, as it would have caused a temporary increase in cash balances; this would have incurred a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns.

The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years. However, this was kept under review to avoid incurring higher borrowing costs in the future when this authority may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

9.2 Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. The Chief Financial Officer therefore monitored interest rates in financial markets and adopted a pragmatic strategy based upon the following principles to manage interest rate risks

- if it had been felt that there was a significant risk of a sharp FALL in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings would have been postponed, and potential rescheduling from fixed rate funding into short term borrowing would have been considered.

- if it had been felt that there was a significant risk of a much sharper RISE in long and short term rates than initially expected, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would have been re-appraised. Most likely, fixed rate funding would have been drawn whilst interest rates were lower than they were projected to be in the next few years.

9.3 Interest rate forecasts expected only gradual rises in medium and longer term fixed borrowing rates during 2020/21 and the two subsequent financial years. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period.

Link Asset Services Interest Rate View														
	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25	1.25	1.25	1.25
3 Month LIBID	0.70	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.30	1.30
6 Month LIBID	0.80	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40	1.50	1.50	1.50	1.50
12 Month LIBID	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60	1.70	1.70	1.70	1.70
5yr PWLB Rate	2.30	2.40	2.40	2.50	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.10	3.20	3.20
10yr PWLB Rate	2.60	2.70	2.70	2.70	2.80	2.90	3.00	3.10	3.20	3.20	3.30	3.30	3.40	3.50
25yr PWLB Rate	3.20	3.30	3.40	3.40	3.50	3.60	3.70	3.70	3.80	3.90	4.00	4.00	4.10	4.10
50yr PWLB Rate	3.10	3.20	3.30	3.30	3.40	3.50	3.60	3.60	3.70	3.80	3.90	3.90	4.00	4.00

PWLB rates are based on, and are determined by, gilt (UK Government bonds) yields through H.M.Treasury determining a specified margin to add to gilt yields. The main influences on gilt yields are Bank Rate, inflation expectations and movements in US treasury yields. Inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation and the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years. We have seen over the last two years, many bond yields up to 10 years in the Eurozone turn negative on expectations that the EU would struggle to get growth rates and inflation up from low levels. In addition, there has, at times, been an investigation of bond yields in the US whereby 10 year yields have fallen below shorter term yields. In the past, this has been a precursor of a recession.

Gilt yields fell sharply from the start of 2020 and then spiked up during a financial markets melt down in March caused by the pandemic hitting western countries; this was rapidly countered by central banks flooding the markets with liquidity. While US treasury yields do exert influence on UK gilt yields so that the two often move in tandem, they have diverged during the first three quarters of 2020/21 but then converged in the final quarter. Expectations of economic recovery started earlier in the US than the UK but once the UK vaccination programme started making rapid progress in the new year of 2021, gilt yields and gilt yields and PWLB rates started rising sharply as confidence in economic recovery rebounded. Financial markets also expected Bank Rate to rise quicker than in the forecast tables in this report.

At the close of the day on 31 March 2021, all gilt yields from 1 to 5 years were between 0.19 – 0.58% while the 10-year and 25-year yields were at 1.11% and 1.59%.

HM Treasury imposed two changes of margins over gilt yields for PWLB rates in 2019/20 without any prior warning. The first took place on 9th October 2019, adding an additional 1% margin over gilts to all PWLB period rates. That increase was then, at least partially, reversed for some forms of borrowing on 11th March 2020, but not for mainstream non-HRA capital schemes. A consultation was then held with local authorities and on 25th November 2020, the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates; the standard and certainty margins were reduced by 1% but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three year capital programme. The new margins over gilt yields are as follows: -.

- PWLB Standard Rate is gilt plus 100 basis points (G+100bps)
- PWLB Certainty Rate is gilt plus 80 basis points (G+80bps)
- PWLB HRA Standard Rate is gilt plus 100 basis points (G+100bps)
- PWLB HRA Certainty Rate is gilt plus 80bps (G+80bps)
- Local Infrastructure Rate is gilt plus 60bps (G+60bps)

There is likely to be only a gentle rise in gilt yields and PWLB rates over the next three years as Bank Rate is not forecast to rise from 0.10% by March 2024 as the Bank of England has clearly stated that it will not raise rates until inflation is sustainably above its target of 2%; this sets a high bar for Bank Rate to start rising.

10. BORROWING OUTTURN

10.1 No debt was rescheduled during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

10.2 The following fixed interest rate loans were taken during the year:

Adur District Council

Lender	Principal	Purpose of Loan	Interest Rate	Maturity
PWLB	£2m	HRA refinancing	1.94%	25/03/2071
Rugby Council	£2m	HRA funding	1.70%	25/11/2022
Worthing Council	£2.5m	Capital expenditure & refinancing	1.00%	30/06/2022

Worthing Borough Council

Lender	Principal	Purpose of Loan	Interest Rate	Maturity
PWLB	£4m	Refinancing	1.94%	25/03/2071
Cornwall Council	£2m	Capital expenditure	0.60%	05/10/2022
East Sussex CC	£5m	Capital expenditure	0.65%	05/12/2022
Glos CC	£5m	Refinancing	1.00%	30/06/2022
Glos CC	£2m	Capital expenditure	0.80%	30/09/2022
Rugby CC	£2m	Refinancing	1.70%	25/11/2022

10.3 **Borrowing in advance of need**

The Councils have not borrowed more than, or in advance of their needs, purely in order to profit from the investment of the extra sums borrowed.

11. INVESTMENT OUTTURN

11.1 **Investment Policy**

The Councils' investment policy is governed by MHCLG investment guidance, which has been implemented in the annual investment strategy. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data, (such as rating outlooks, credit default swaps, bank share prices etc.).

11.2 **Use of Chief Executive's Urgency Powers**

As approved by JSC on 9th June 2020, the Chief Executive used his urgency powers to amend the counterparty investment limits from 1 April 2020 to 30 June 2020 to enable the Councils to manage the significant funding received from the Government to distribute as Business Grants. The duty to distribute the funds as quickly as possible necessitated that the funds were kept liquid and they could not be placed in fixed term investments. The limits were also breached on 1 July 2020 - this was reported to the JGC. The credit risk was mitigated by spreading the additional funds across counterparties with high credit ratings, using the usual criteria of “security, liquidity then yield” and no losses were incurred. The Treasury Management Strategy Statement counterparty limits applied after that period for the rest of 2020/21.

For Worthing Borough Council the investment limit was increased from £3m per counterparty to £6.5m per counterparty, with an overall total for money market funds of £26m. The limit for Lloyds Bank was increased to £7m.

For Adur District Council the investment limit was increased from £3m to £5m per counterparty with an overall total for money market funds of £20m. The limit for Lloyds Bank was increased to £6m.

11.3 Resources

The Councils’ cash balances comprise revenue and capital resources and cash flow monies. The Councils’ core cash resources comprised as follows:

Adur District Council

Balance Sheet Resources (£m)	31 March 2021	31 March 2020
General Fund Balances	(0.951)	(0.952)
HRA Balances	(7.816)	(6.362)
Earmarked reserves	(8.504)	(3.177)
Provisions	(0.862)	(0.600)
Usable capital receipts & grants	(6.339)	(5.567)
Total	(24.472)	(16.658)

Worthing Borough Council

Balance Sheet Resources (£m)	31 March 2021	31 March 2020
Balances	(1.543)	(1.543)
Earmarked reserves	(12.029)	(3.328)
Provisions	(0.516)	(0.185)
Usable capital receipts & grants	(6.360)	(5.432)
Total	(20.448)	(10.488)

11.4 **Investments held by the Councils**

Both Councils recorded a shortfall on investment income against budget, partly due to the use of “internal borrowing” - instead of borrowing externally to fund the capital programme, funds that could otherwise have been invested externally were used for capital expenditure. This approach was used due to the higher rates payable on borrowing compared to investing and resulted in an underspend on interest payable. Due to the Covid 19 pandemic, investment rates achievable in the market during the year were also lower than the original forecast.

Details of the income earned are shown below. A comparable performance indicator is the average 6 month London Interbank Bid Rate (the rate bid by banks on deposits), which was 0.07%.

Adur District Council:

Adur District Council maintained an average balance of £19.509m of internally managed short term investments, which earned an average rate of return of 0.35%. This excludes the £3m investment in the Local Authorities’ Property Fund, which returned an average of 3.90%, amounting to income of £117k.

The treasury investment returns included in the reported income of Adur Council for 2020/21, excluding the Local Authorities’ Property Fund investment, amounted to £69k, which under-achieved the budget by £197k, due to the reasons explained above. This shortfall was offset by compensating savings on the Council’s interest payments on borrowing, which were also at lower rates, resulting in an underspend of £240k.

Worthing Borough Council:

Worthing Borough Council maintained an average balance of £16.709m of internally managed short term investments, which earned an average rate of return of 0.21% and a long term investment of £2.5m which earned 1%. Those figures exclude:

- the £10m loan to Worthing Homes, which earned 0.70% above the rate at which the funds were borrowed from the PWLB, amounting to £70k;

- the £5m loan to GB Met College, which earned 2.00% above the rate at which the funds were borrowed from the PWLB, amounting to £103k;

- the investment in the Local Authorities’ Property Fund, which earned an average of 3.90%, amounting to £58.5k.

The Treasury investment returns included in the reported income of the Council for 2020/21 amounted to £54k, excluding the investments specified above, £57k under budget, due to the reasons explained above. This shortfall was offset by compensating savings on the Council’s interest payments on borrowing, which were also at lower rates, resulting in an underspend of £352k.

12. MINIMUM REVENUE PROVISIONS (MRP) FOR REPAYMENT OF DEBT

12.1 The Councils, in accordance with legislation, make a provision from revenue to enable the repayment of borrowing that has been undertaken to fund the capital programme. This provision is known as the Minimum Revenue Provision (MRP) and is charged to the General Fund Revenue Account each year. The Councils are also permitted to make a Voluntary Revenue Provision (VRP) which is additional to the MRP and can be used to reduce the MRP in future years.

12.2 For 2020/21 an amount of £2.222m of MRP, after an offset of £10k of VRP, has been provided in the Adur District Council General Fund. The VRP total balance at 31 March 2021 was £40k. No voluntary amount has been set aside for the HRA.

12.3 For 2020/21 an amount of £2.070m of MRP and a net £140k of VRP has been provided in the Worthing Borough Council revenue accounts. The VRP total balance at 31 March 2021 was £630k.

13. CURRENT PERIOD TREASURY MATTERS

13.1 Due to the Covid-19 virus, the government made substantial payments to both Councils to distribute as Business Grants to local businesses. On April 1st 2020 Adur District Council received £17.64m and Worthing Borough Council received £26.13m. Additional funding was also received to provide relief to the local community, support the additional costs that the Councils are incurring, and to compensate for the loss of income.

The Councils have been very successful in distributing the funds to support local businesses, However it was not possible to accept the grant funding and also adhere to the counterparty investment limits whilst managing these short term funds. Consequently the Chief Executive used his urgency powers to approve changes to the investment limits for three months (April - June 2020), which was approved by JSC on the 9th June 2020. The approval ended on the 30th June 2020, but unfortunately the counterparty limits were still exceeded on the 1st July 2021. All counterparty limits were met on the 2nd July 2021 and subsequently and there was no loss to either Council.

13.2 Following the consultation undertaken by the Ministry of Housing, Communities and Local Government, (MHCLG), on IFRS9, the Government has introduced a mandatory statutory override for local authorities to reverse out all unrealised fair value movements resulting from pooled investment funds. This will be effective from 1 April 2018. The statutory override applies for five years from this date. Local authorities are required to disclose the net impact of the unrealised fair value movements in a separate unusable reserve throughout the duration of the override in order for the Government to keep the override under review and to maintain a form of transparency. This applies to Adur and Worthing Councils in respect of the investments in the Local Authorities' Property Fund.

14. ENGAGEMENT AND COMMUNICATION

14.1 The Adur and Worthing Councils' treasury management team provides treasury services to Mid Sussex District Council through a shared services arrangement (SSA). The SSA is provided under a Service Level Agreement that was renewed from 18th October 2019, and which defines the respective roles of the client and provider authorities for a period of three years. The shared service also took on Treasury work for Arun District Council on the 1st March 2021 under a three year service level agreement.

14.2 Information and advice is supplied throughout the year by Link Asset Services Ltd, the professional consultants for the Councils' shared treasury management service.

15. FINANCIAL IMPLICATIONS

This report has no quantifiable additional financial implications to those outlined above. Interest payable and interest receivable arising from treasury management operations, and annual revenue provisions for repayment of debt, form part of the revenue budget.

16. LEGAL IMPLICATIONS

The presentation of the Annual Report is required by regulations issued under the Local Government Act 2003 to review the treasury management activities, the actual prudential indicators and the treasury related indicators for 2020/21.

Background Papers

Joint Treasury Management Strategy Statement and Annual Investment Strategy Report 2020/21 to 2022/23 – Joint Governance Committee 28 January 2020, Joint Strategic Committee 11 February 2020, Worthing Council 18 February 2020, Adur Council 20 February 2020

Joint Half-Year In-House Treasury Management Operations Report 1 April – 30 September 2020 for Adur District Council and Worthing Borough Council – Joint Governance Committee, 24 November 2020 and Joint Strategic Committee, 1 December 2020

Link Asset Services Annual Report Template 2020/21

CIPFA Code of Practice on Treasury Management and CIPFA Code for Capital Finance in Local Authorities

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SUSTAINABILITY & RISK ASSESSMENT

1. ECONOMIC

The treasury management function ensures that the Councils have sufficient liquidity to finance their day to day operations. Borrowing is arranged as required to fund the capital programmes. Available funds are invested according to the specified criteria to ensure security of the funds, liquidity and, after these considerations, to maximise the rate of return.

2. SOCIAL

2.1 Social Value

Matter considered and no issues identified.

2.2 Equality Issues

Matter considered and no issues identified.

2.3 Community Safety Issues (Section 17)

Matter considered and no issues identified.

2.4 Human Rights Issues

Matter considered and no issues identified.

3. ENVIRONMENTAL

Matter considered and no issues identified.

4. GOVERNANCE

4.1 The Councils' Treasury Management Strategy and Annual Investment Strategy place the security of investments as foremost in considering all treasury management dealing. By so doing it contributes towards the Councils' priorities contained in Platforms for our Places.

4.2 The operation of the treasury management function is as approved by the Councils' Treasury Management Strategy and Annual Investment Strategy 2020/21 - 2022/23, submitted and approved before the commencement of the 2020/21 financial year.

4.3 In the current economic climate the security of investments is paramount, the management of which includes regular monitoring of the credit ratings and other incidental information relating to credit-worthiness of the Councils' investment counterparties.