Mid-Year Monitoring Report 2021/22
Treasury Management and Prudential Indicators: 1 April 2021 to 31 October 2021

1. Introduction

1.1 The Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance:

- The Local Government in Scotland Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
- The Act permits the Scottish Ministers to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions have been made as yet during 2021/22).
- Statutory Instrument (SSI) 29 2004, requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities, and therefore to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services; and the treasury activity with regard to the CIPFA Code of Practice for Treasury Management in Local Authorities.
- Statutory Instrument (SSI) 123 2016, set out statutory arrangements for local authority borrowing and lending and the requirement to maintain a loans fund and replace the statutory arrangements set out in Schedule 3 of the Local Government (Scotland) Act 1975 (Schedule 3).

1.2 The regulatory framework of treasury management requires that the Council receive a mid-year treasury review, in addition to the forward looking annual treasury strategy and backward looking annual treasury report. This report meets that requirement and also incorporates the needs of the Prudential Code to ensure adequate monitoring of the capital expenditure plans and the Council's prudential indicators. The treasury strategy and prudential indicators were previously reported to Council on 3 March 2021. The current position is shown (where appropriate) and revisions to the 2021/22 estimate are provided where required.

1.3 In December 2017, the Chartered Institute of Public Finance and Accountancy, (CIPFA), issued revised Prudential and Treasury Management Codes. As from 2019/20, all local authorities require to prepare a Capital Strategy which provides the following:

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services;
- an overview of how the associated risk is managed; and
- the implications for future financial sustainability

The Council's Capital Strategy was reported to and agreed by Council on 3 March 2021.

1.4 This report sets out:

- Key changes to the Council's capital activity (the prudential indicators);
- An economic update for the first part of the 2021/22 financial year;
- The actual and proposed treasury management activity (borrowing and investment); and
- The risk approach to treasury management (the treasury management indicators).

2. Key Prudential Indicators

2.1 This part of the report is structured to update:

- The Council's capital expenditure plans and how these plans are being financed;
- The impact of the changes in the capital expenditure plans on the PIs and the underlying need to borrow;
- Compliance with the limits in place for borrowing activity; and
- Policy on the statutory repayment of loans fund advances

2.2 **Capital Expenditure** – Table A shows the current position and revised estimates for capital expenditure for 2021/22 only.

Table A:

£000	**2021/22 Original Estimate**	**Current Position**	**2021/22 Projected Outturn**
General Services	47,501	11,504	43,453
HRA	49,744	21,514	46,639
Capital Expenditure	**97,245**	**33,018**	**90,092**
Financed by:			
Capital receipts	7,077	2,153	3,532
Capital grants	12,765	2,708	17,289
Revenue / other	8,465	63	9,003
Net financing need for the year	**68,938**	**28,094**	**60,268**

2.2.1 The movement in the level of anticipated capital expenditure is mainly due to the inclusion of additional slippage following the year end; a reduction in anticipated capital receipts; an increase in spend related to external funding offset by slippage levels identified to date. The anticipated spends and resources are regularly reported to Members through budgetary control reports.

2.3 **Impact of changes in Capital Expenditure Plans** – Table B shows the CFR, which is the underlying external need to borrow for a capital purpose while Table C shows the expected debt position over the period.

Table B:

£000	2021/22 Original Estimate	2021/22 Projected Outturn
Opening CFR (1 April 2021)	**647,920**	**646,190**
New Borrowing	60,167	53,100
LTL repayment in year	(3,681)	(3,681)
Closing CFR (31/3/22)	**704,406**	**695,609**
movement in CFR	**56,486**	**49,419**
Net financing need for the year (Table A)	68,938	60,268
Loan repayments in year - excluding LTL (PPP)	(8,771)	(7,168)
New Borrowing - Movement in CFR (from previous year)	**60,167**	**53,100**

Table C:

£000	2021/22 Original Estimate	Current Position	2021/22 Projected Outturn
External Debt			
Estimated/Actual Debt at 1 April 2021	551,579	535,080	544,812
Maturing Debt	(221,628)	(200,192)	(262,677)
Movement in Borrowing			
New Borrowing - Maturing Debt	221,628	200,192	262,677
Borrowing adjustment in relation to over borrowing at year end	0	0	0
New Borrowing – CFR (Table B)	60,167	15,000	53,100
Debt at 31 March (1)	**611,746**	**563,080**	**597,912**
Long Term Liabilities (LTL) at 1 April	96,341	96,292	96,292
LTL repayment in year (Table B)	(3,681)	(1,339)	(3,677)
LTL at 31 March (2)	**92,660**	**94,954**	**92,615**
Actual Debt at 31 March (1) + (2)	**704,406**	**658,034**	**690,527**
CFR from Table B	**704,406**	**n/a**	**695,609**
Under/(Over) Borrowing	**0**	**n/a**	**5,082**

2.3.1 The external debt figures included within Table C now includes both short term and long term debt. This is due to the current strategy of using short term borrowing to fund long term capital investment enabling the Council to take advantage of lower interest rates. The reduction in the estimated external debt for 2021/22 is due to a reduction in the net capital financing need for the year.

2.3.2 The CFR is calculated on a year-end position based on the Council's balance sheet and therefore the current position is not shown. The CFR has reduced from the original estimate due to the forecast level of capital expenditure in 2021/22 being less than budgeted. The Chief Officer - Resources can report that the Council is currently on target to meet the 2021/22 revised estimates for both indicators.

2.3.3 Table C highlights that the borrowing of the Council is forecasting a minimal under-borrowed position against the CFR at 31 March 2022.

2.4 **Compliance with the limits in place for borrowing activity** – A key control over the treasury activity is a prudential indicator to ensure that over the medium term, gross borrowing will only be for a capital purpose.

Gross borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2021/22 and next two financial years. This allows some flexibility for limited early borrowing for future years.

The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent. The revised indicator is detailed in Table D and is illustrated by comparing the estimated gross debt as at 31 March 2021 with the CFR as at 31 March 2024. The Chief Officer - Resources reports that no difficulties are envisaged for the current year in complying with this prudential indicator.

Table D:

£000	2021/22 Original Estimate	2021/22 Projected Outturn
CFR at 31 March 2021		
2021/22 Estimate/Actual (From Table B above)	**647,920**	**646,190**
Estimated movement in CFR		
2021/22 (From Table B above)	56,486	49,419
2022/23	32,419	45,098
2023/24	56,027	56,027
Anticipated CFR at 31 March 2024	**792,852**	**796,735**
Gross Debt at 31 March 2022 (From C above)	**704,406**	**691,527**

2.4.1 The Operational Boundary is detailed in Table E below and is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

Table E:

£000	2021/22 Original Estimate	Current Position	2021/22 Projected Outturn
External Debt	774,848	658,034	760,680

2.4.2 A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which is detailed in Table F and represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Table F:

£000	2021/22 Original Estimate	Current Position	2021/22 Projected Outturn
External Debt	845,288	658,034	829,832

3. Economic Outlook

UK

3.1 The Monetary Policy Commission (MPC) voted to leave bank rate unchanged at 0.10% and made no changes to its programme of quantitative easing purchases due to finish by the end of 2021. Inflation recently announced at 4.2% which is the highest it has been in recent years. It is forecasted that by April 2022 the rate will be 5%.

3.2 Supply shortages, labour shortages, surging fuel prices and tax increases could have an effect on interest but these could be offset, at least partially, by the savings consumers have accumulated during the pandemic.

3.3 The UK economy is expected to grow stronger than anticipated in 2021 and 2022. It is anticipated that it will rise 6.5% this year and 6% in 2022.

Scotland

3.4 Since the start of the pandemic in March 2020 funding for COVID-19 has played an important role in the Scottish budget. This funding accounted for 17% of the 2020/21 Scottish budget and 10% of the 2021/22 budget. There isn’t the same guarantee of funding this year and the final level of funding should be confirmed early 2022. COVID 19 continues to have a profound effect on the economy but the outlook is better than originally anticipated.

3.5 Due to supports provided, the labour market performed better than anticipated during the pandemic. It is anticipated therefore that unemployment rates for quarter 4 will peak at 5.4% which is lower than initially anticipated. In 2020/21 the average Scottish house price was above £200,000. It is expected that they will stabilise at this value in 2021/22 but will continue to grow in future years. There are however, shortages in labour which may impact on the economy.

International update

3.6 In the US, shortages of goods and intermediate goods like semi-conductors, are fuelling increases in prices and reducing economic growth potential. There has been a sustained drop in the labour force which suggests the pandemic has had a longer-term effect in reducing potential GDP. Economic growth may therefore be reduced to between 2 and 3% in 2022 and 2023 while core inflation is likely to remain elevated at around 3% in both years instead of declining back to the Fed's 2% central target.

3.7 In the Eurozone the slow role out of vaccines initially delayed economic recovery in early 2021 but the vaccination rate then picked up sharply. After a contraction of -0.3% in Q1, Q2 came in with strong growth of 2%. With Q3 projected at 2.2%, the EU recovery is nearly complete although countries dependent on tourism are lagging. Recent sharp increases in gas and electricity prices have increased overall inflationary pressures but the European Central Bank is likely to see these as being only transitory after an initial burst through to around 4%, so is unlikely to be raising interest rates for a considerable time.

3.8 Based upon the above information, the Council's treasury advisor, Link Asset Services, has provided the following interest rate forecast. As at November 2021:

Table G:

Link Group Interest Rate View 8.11.21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00
3 month ave earnings	0.30	0.40	0.50	0.50	0.50	0.60	0.80	0.90	1.00	1.00
6 month ave earnings	0.40	0.50	0.60	0.60	0.70	0.80	0.90	1.00	1.10	1.10
12 month ave earnings	0.50	0.60	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20
5 yr PWLB	1.50	1.50	1.60	1.60	1.70	1.70	1.70	1.80	1.80	1.80
10 yr PWLB	1.80	1.90	1.90	2.00	2.00	2.10	2.10	2.20	2.20	2.20
25 yr PWLB	2.10	2.20	2.30	2.40	2.40	2.40	2.50	2.50	2.60	2.60
50 yr PWLB	1.90	2.00	2.10	2.20	2.20	2.20	2.30	2.30	2.40	2.40

Source:Link Treasury Management Advisors

3.9 Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- UK – COVID vaccines don't work as anticipated or as quickly as hoped;
- The pandemic leaves long term issues for the economy;
- The Government introduces austerity plans which stifle growth;
- The Montetary Policy Committee tightens monetary policy too early or late resulting in adverse effects on the economy;
- Major stock markets e.g. in the US, become increasingly judged as being over-valued and susceptible to major price corrections;
- Widespread political risk, for example: the German elections

3.10 Upside risks to current forecasts for UK gilt yields and PWLB rates are as follows:

- UK - stronger than currently expected recovery in UK economy.

4. Treasury Management Activity

4.1 This part of the report is structured to update:

- The Council's expected borrowing need and details of under/(over) borrowing;
- Debt rescheduling and new borrowing;
- Debt charges; and
- Investments

4.2 **The Expected Borrowing Need** – This was set out in Table C (above) and demonstrates that at 30 September 2021 Council is currently projecting and under-borrowed position to reduce risks in investments held and the cost of carry on investments. It should be noted that due to the recent announcement on PWLB interest rates, the borrowing rates are significantly different than in September 2021, when long term borrowing rates for periods greater than 25 years are currently between 1.96% to 1.57%, depending on length of term for borrowing. This introduces an element of interest rate risk, as longer term borrowing rates may rise; however, this position is being carefully monitored.

4.3 **Debt rescheduling and new borrowing** – The Council has not undertaken any debt rescheduling during the first half of 2021/22. In the year to date naturally maturing debt of £200.192m has been repaid which has been mainly funded by loans from other local authorities.

4.4 **Debt Charges** – The revised estimate for debt charges for both the General Fund and the HRA is shown in Table H.

Table H:

£000	**2021/22 Original Estimate**	**Current Position**	**2021/22 Revised Estimate**
Borrowing	20,925	10,463	20,925
Other Long Term Liabilities	10,547	5,274	10,547
Total	**31,472**	**15,736**	**31,472**

4.5 **Investments** – The objectives of the Council's investment strategy are to ensure the re-payment of the principal and interest of its investments on time with the level of investment return being a secondary objective. Following on from the economic background above, the current investment climate has one over-riding risk consideration which is the risk of default.

4.5.1 The Council held £16.341m of cash investments at 30 September 2021, and the constituent parts of the investment position are detailed in Table I:

Table I:

£000	Country	< 1 Year	1 – 2 Years	2 – 3 Years
Banks	UK	5,433	Nil	Nil
Money Market Fund	UK	10,908	Nil	Nil
Local Authorities	UK	0	Nil	Nil
Total	UK	16.341	Nil	Nil

4.5.2 Table J details the revised budget position for investment income. The original estimate has decreased by £0.011m due to ongoing interest rates.

Table J:

£000	2021/22 Original Estimate	Current Position	2021/22 Revised Estimate
Investment Income	75	32	64

4.5.3 A regulatory development to address risk is the consideration and approval of benchmarks relating to investment security, liquidity and the level of return. Benchmarks are currently widely used to assess the level of return and investment performance, however the application of security and liquidity benchmarks are more subjective in nature.

- **Security** - The Council's maximum security risk benchmark for the current portfolio in relation to investment periods of up to one year (when compared to historic default tables) was set at 0.00% and the Chief Officer - Resources can report that there have been no defaults of principal sums invested in the year to date.

Creditworthiness - Significant levels of downgrades to Short- and Long-Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. However, as economies are beginning to reopen, there have been some instances of previous lowering of Outlooks being reversed.

- **Liquidity** – The Chief Officer - Resources can report that liquidity arrangements were adequate during the year to date and that the liquidity facilities and benchmarks set by the Council as noted below were maintained:

    - Bank overdraft - £1.000m; and
    - Liquid short term deposits of at least £5.000m available on an overnight basis.

- **Return on Investments** – The Chief Officer - Resources can report that the investment return to date average 0.33%. Table K illustrates how this average return compares with the local benchmarks.

Table K:

Benchmark	Benchmark Return	Average Return
7 day LIBID rate	-0.08%	0.33%
1 month LIBID rate	-0.06%	0.33%
Council's Instant Access Account	0.10%	0.33%

5 Key Treasury Management Indicators

5.1 This part of the report is structured to update:

- Actual and estimates of the ratio of financing costs to net revenue stream;
- Upper limits on interest rate exposure:
- The maturity structure of borrowing; and
- Total principal sums invested.

5.2 **Actual and estimates of the ratio of financing costs to net revenue stream** – This indicator (as shown below in Table L) identifies the trend in the cost of capital (financing costs net of interest and investment income) against the net revenue stream.

Table L:

	2021/22 Original Estimate	2021/22 Revised Estimate
General Fund	8.53%	8.43%
HRA	28.07%	25.74%

5.3 **Upper Limits on Fixed and Variable Rate Exposure** – These indicators identify a maximum limit for fixed and variable interest rates based upon the debt position and were set at 100% and 50% respectively for 2021/22. The Chief Officer – Resources reports that the Council operates within these limits.

5.4 **Maturity Structures Of Borrowing** – These maximum limits are set to reduce the Council's exposure to large fixed rate loans (those instruments which carry a fixed interest rate for the duration of the instrument) which are due to naturally mature in any given period as detailed in Table M and show that the Council operates within limits set.

Table M:

Maturity Structure of Fixed Interest Rate Borrowing	2021/22 Original Limits	Current Position
Under 12 months	50%	44%
12 months to 2 years	50%	3%
2 years to 5 years	50%	5%
5 years to 10 years	50%	5%
10 years to 20 years	50%	4%
20 years to 30 years	50%	6%
30 years to 40 years	50%	3%
40 years to 50 years	100%	21%
50 years to 60 years	100%	9%
60 years to 70 years	100%	0%

5.5 **Total Principal Funds Invested** – These limits are set to reduce the need to temporarily borrow to cover any unexpected expenditure, and show limits to be placed on investments with final maturities beyond each year-end. The Council currently invests sums for periods greater than 365 days in Clydebank Property Company and hub West Scotland as detailed in Table N.

Table N:

	2021/22 Original Estimate	Current Position	2021/22 Revised Estimate
Principal sums invested > 365 days (maximum limit £7m)	£0.489m	£0.489m	£0.489m