For Information / Consideration	
Public/Non Public*	Public
Report to:	Joint Audit and Scrutiny Panel
Date of Meeting:	May 2021
Report of:	Chief Finance Officer
Report Author:	Charlotte Radford
Other Contacts:	Amanda Harlow
Agenda Item:	11

TREASURY MANAGEMENT YEAR END REPORT

1. Purpose of the Report

1.1 To provide members with details of compliance with the Treasury Management Strategy and prudential indicators for 2020-21.

2. Recommendations

2.1 Members are recommended to consider the report and the assurance it provides.

3. Reasons for Recommendations

3.1 This complies with good governance.

4. Summary of Key Points

4.1 The attached report details the Treasury Management activity for 2020-21 and how this compares with the approve treasury and prudential code indicators for the year.

4.2 Treasury Management is a significant activity within the finance function of the OPCC. It ensures that there are sufficient funds available to meet day to day expenditure such as paying creditors and salaries. It is also responsible for investing income from grants and precept to meet future expenditure requirements.

4.3 The Treasury Management Strategy is approved annually by the Police & Crime Commissioner and sets out the parameters within which the activity performs. The essential element of this is to protect the assets of the OPCC, with the ability to generate additional income secondary to this.

4.4 A key element to the performance of this activity is the completion of the capital programme. Unfortunately, capital projects by their nature are large and take time to complete as various factors can affect them (e.g. other partners involved in the project, planning permission, availability of staff). Any delay in capital projects can impact on when payments are made and when borrowing is actually needed. COVID has had some impact in 2020-21, but major projects have continued and the delay on completion is minimal.

4.5 Income from investments in the money markets has remained static and low for quite some time. This will continue as austerity continues and market returns remain low. However, compared to market averages the returns made from investments are relatively high. And investments have only been made with those organisations with an approved rating.

5. Financial Implications and Budget Provision

5.1 None as a direct result of this report.

6. Human Resources Implications

6.1 None as a direct result of this report.

7. Equality Implications

7.1 None as a direct result of this report.

8. Risk Management

8.1 None as a direct result of this report.

9. Policy Implications and links to the Police and Crime Plan Priorities

9.1 This report complies with good governance and financial regulations.

10. Changes in Legislation or other Legal Considerations

10.1 None

11. Details of outcome of consultation

11.1 Not applicable

12. Appendices

12.1 Appendix A – Treasury Management Report 2020-21

The Nottinghamshire Office of the Police & Crime Commissioner

Treasury Management

Annual Review

2020-21

1. Introduction

The Nottinghamshire Office of the Police and Crime Commissioner is required by regulation issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for the year. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities.

During 2020-21 the minimum reporting requirements were that the Commissioner should receive the following reports:

- an Annual Treasury Strategy in advance of the year (February 2020)
- a Mid-year Treasury Update report (November 2020)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

There is a continued requirement for scrutiny within the regulatory framework and this report is an important aspect including adherence to policies and performance against previously set indicators.

The Chief Financial Officer to the Commissioner also confirms that they have complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports prior to presentation. The Prudential Indicators for the year are attached as an addendum to this report.

2. Economic Background

The key quarterly Monetary Policy Report meeting of the Bank of England's Monetary Policy Committee kept Bank Rate and quantitative easing (QE) unchanged on 4th February, (as it also did at its 18th March meeting). However, it revised its economic forecasts to take account of a third national lockdown which started on 5th January, which is going to further delay economic recovery and do further damage to the economy. Although its short-term forecasts were cut for 2021 due to the start of a third lockdown in early January, the medium-term forecasts were more optimistic than in November, based on an assumption that the current lockdown will be gradually eased after Q1 as vaccines are gradually rolled out and life can then start to go back to some sort of normality.

COVID-19 vaccines. These have been the game changer which have enormously boosted confidence that life in the UK could largely return to normal during the second half of 2021 after a third wave of the virus threatened to overwhelm hospitals around the start of the year. With the household saving rate having been exceptionally high since the first lockdown in March 2020, there is plenty of pent-up demand and purchasing power stored up for services in the still-depressed sectors like restaurants, travel and hotels. The UK has made fast progress with giving a first jab to half of all adults and this programme should be completed in the second half of the year. The big question is whether mutations of the virus could develop which render current vaccines ineffective, as opposed to how quickly can vaccines be modified to deal with them and enhanced testing programmes be implemented to contain their spread.

The Budget on 3rd March increased fiscal support to the economy and employment during 2021 and 2022 followed by substantial tax rises in the following three years to help to pay the cost for the pandemic. This will help further to strengthen the economic recovery from the pandemic and to return the government's finances to a balanced budget on a current expenditure and income basis in 2025-26. This will stop the Debt to GDP ratio rising further from 100%. An area of concern, though, is that the government's debt is now twice as sensitive to interest rate rises as before the pandemic due to QE operations substituting fixed long-term debt for floating rate debt; there is, therefore, much incentive for the Government to promote Bank Rate staying low e.g. by using fiscal policy in conjunction with the monetary policy action by the Bank of England to keep inflation from rising too high, and/or by amending the Bank's policy mandate to allow for a higher target for inflation.

Brexit. The final agreement on 24th December 2020 eliminated a significant downside risk for the UK economy. The initial agreement only covered trade so there is further work to be done on the services sector where temporary equivalence has been granted in both directions between the UK and EU; that now needs to be formalised on a permanent basis. There was much disruption to trade in January as form filling has proved to be a formidable barrier to trade. This appears to have eased somewhat since then but is an area that needs further work to ease difficulties, which are still acute in some areas.

US. The Democrats won the presidential election in November 2020 and have control of both Congress and the Senate, although power is more limited in the latter. This enabled the Democrats to pass a $1.9trn (8.8% of GDP) stimulus package in March on top of the $900bn fiscal stimulus deal passed by Congress in late December. These, together with the vaccine rollout proceeding swiftly to hit the target of giving a first jab to over half of the population within the President's first 100 days, will promote a rapid easing of restrictions and strong economic recovery during 2021. The Democrats are also planning to pass a $2trn fiscal stimulus package aimed at renewing infrastructure over the next decade. Although this package is longer-term, if passed, it would also help economic recovery in the near-term.

EU. Both the roll out and take up of vaccines has been disappointingly slow in the EU, at a time when many countries are experiencing a sharp rise in cases which are threatening to overwhelm hospitals in some major countries; this has led to renewed severe restrictions or lockdowns during March. This will inevitably put back economic recovery after the economy had staged a rapid rebound from the first lockdowns in Q3 but contracted slightly in Q4 to end 2020 only 4.9% below its pre-pandemic level. Recovery will now be delayed until Q3 of 2021 and a return to pre-pandemic levels is expected in the second half of 2022.

China. After a concerted effort to get on top of the virus outbreak in Q1, economic recovery was strong in Q2 and then into Q3 and Q4; this has enabled China to recover all of the contraction in Q1. Policy makers have both quashed the virus and implemented a programme of monetary and fiscal support that has been particularly effective at stimulating short-term growth. After making a rapid recovery in 2020-21, growth is likely to be tepid in 2021-22.

Japan. A third round of fiscal stimulus in early December took total fresh fiscal spending in 2020 in response to the virus close to 12% of pre-virus GDP. That is huge by past standards, and one of the largest national fiscal responses. The budget deficit is now likely to reach 16% of GDP in 2020-21. Coupled with Japan's relative success in containing the virus without draconian measures so far, and the roll out of vaccines gathering momentum, the government's latest fiscal effort should help to ensure a strong recovery and to get back to pre-virus levels by Q3 2021 – around the same time as the US and much sooner than the Eurozone.

World growth. World growth was in recession in 2020. Inflation is unlikely to be a problem in most countries for some years due to the creation of excess production capacity and depressed demand caused by the coronavirus crisis.

Deglobalisation. Until recent years, world growth has been boosted by increasing globalisation i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last 30 years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy. In March 2021, western democracies implemented limited sanctions against a few officials in charge of government policy on the Uighurs in Xinjiang; this led to a much bigger retaliation by China and is likely to mean that the China/EU investment deal then being negotiated, will be torn up. After the pandemic exposed how frail extended supply lines were around the world, both factors are now likely to lead to a sharp retrenchment of economies into two blocs of western democracies v. autocracies. It is, therefore, likely that we are heading into a period where there will be a reversal of world globalisation and a decoupling of western countries from dependence on China to supply products and vice versa. This is likely to reduce world growth rates.

Central banks' monetary policy. During the pandemic, the governments of western countries have provided massive fiscal support to their economies which has resulted in a big increase in total government debt in each country. It is therefore very important that bond yields stay low while debt to GDP ratios slowly subside under the impact of economic growth. This provides governments with a good reason to amend the mandates given to central banks to allow higher average levels of inflation than we have generally seen over the last couple of decades. Both the Fed and Bank of England have already changed their policy towards implementing their existing mandates on inflation, (and full employment), to hitting an average level of inflation. Greater emphasis could also be placed on hitting subsidiary targets e.g. full employment before raising rates. Higher average rates of inflation would also help to erode the real value of government debt more quickly.

3. Overall Treasury Position as at 31 March 2021

Commissioner's treasury position in comparison to the previous financial year:

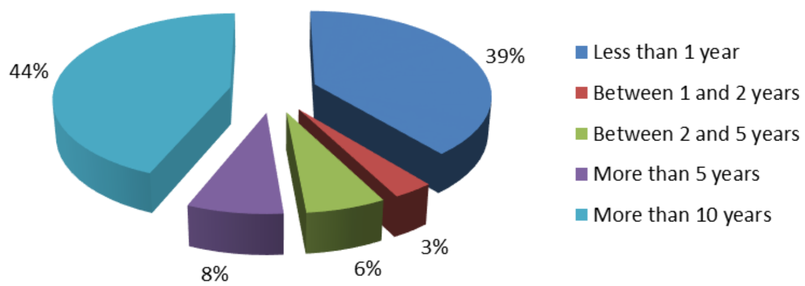
	31-03-20 £m	31-03-21 £m
Total Capital Debt	59.4	58.8
Capital Financing Requirement	70.2	79.8
Over/-Under borrowing	-10.8	-21.0
Total Investments	45.1	54.5
Net Capital Debt	14.3	4.3

4. Strategy - 2020-21

The Commissioner had maintained an under borrowed position throughout the year until March; meaning that the capital borrowing need (the Capital Financing Requirement) had not been fully funded through external borrowing, with reserve balances being utilised to finance the capital spend. This is a pragmatic and cautious approach at a time of high risk coupled with low return on investments. The CFO to the Commissioner has carefully monitored this situation, whereby investments continue to receive low returns compared to borrowing rates. The primary focus for investments continues to be security and liquidity over return.

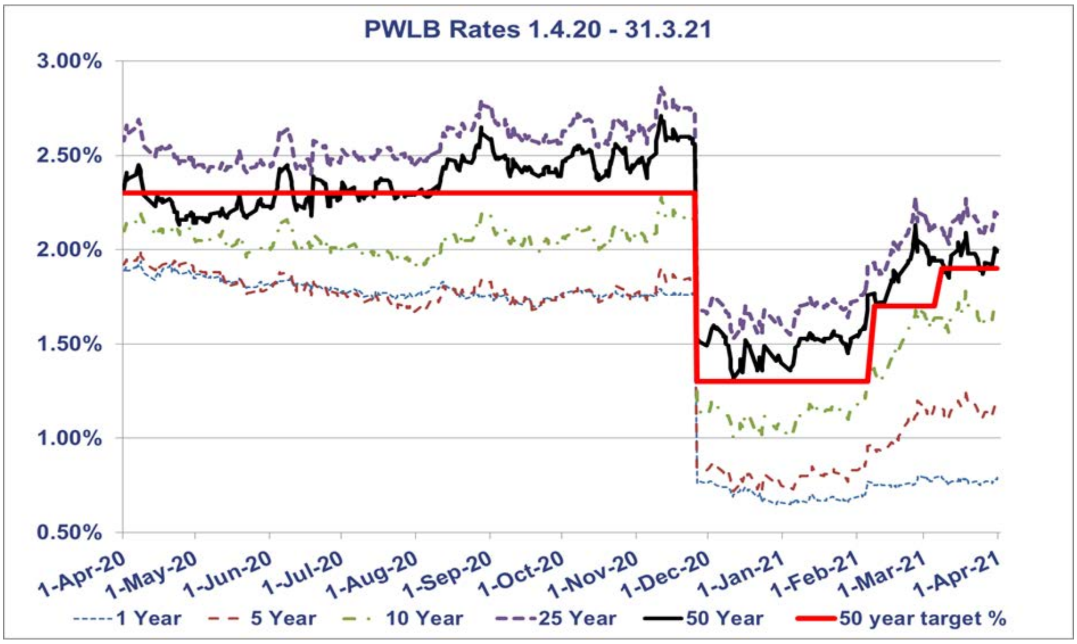
Short term borrowing from local authorities was utilised to maintain cash flow liquidity and fund short life asset purchases within the capital programme.

The borrowing maturity at the end of the year is illustrated below:



5. Borrowing Rates - 2020-21

The graph below shows PWLB maturity certainty rates throughout the year. The 50 year PWLB target certainty rate for new long-term borrowing was unchanged at 2.30% all year until the margin change on 25th November 2020 when it fell to 1.30%. It then rose to 1.70% in February 2021 and to 1.90% in March.



6. Borrowing Activity - 2020-21

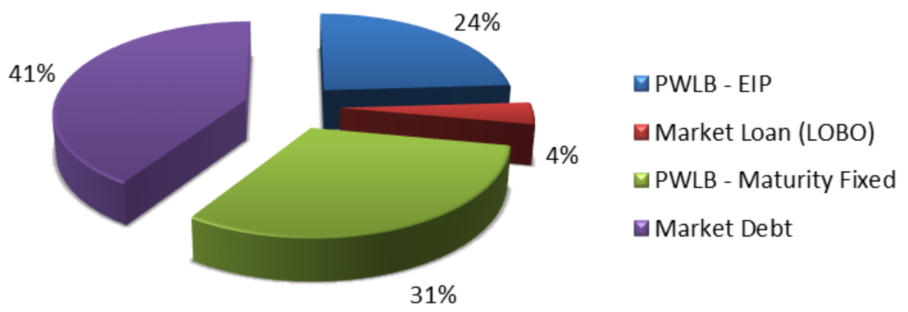
As per the Treasury Management Strategy up to £18.065m borrowing was authorised for the year, with £13m actually being borrowed. This includes borrowing in advance of need (£10m) which was undertaken in March 2020, when due to the coronavirus outbreak borrowing rates fell to a point where it was considered optimal to do so in order to finance capital expenditure which would be incurred within the time frame of the forward approved Capital Financing Requirement estimates. In taking this decision, careful consideration of achieving best value, the risk of having to borrow at higher rates at a later date, the carrying cost of the difference between interest paid on such debt and interest received from investing funds which would be surplus until used, and that the security of such funds placed on temporary investment could be ensured.

The budget for interest was £1.926m and savings of £0.074m were possible due to borrowing being available at a lower rate than initially estimated. Short term borrowing for cashflow purposes was obtained at the best rate available. There has been no opportunity for rescheduling debt for more advantageous rates during the year, although this has been considered on a regular basis.

The summary of borrowing activity is as follows:

	Position @ 01-04-20 £	Loans taken £	Loans repaid £	Position @ 31-03-21 £
Long Term Borrowing				
PWLB	53,894,681	0	(3,557,396)	50,337,285
LOBO	3,500,000	0	0	3,500,000
Local Authorities	2,000,000	3,000,000	0	5,000,000
Total Long Term Borrowing	59,394,681	3,000,000	(3,557,396)	58,837,285
Temporary Borrowing				
Local Authorities	10,000,000	93,500,000	(71,500,000)	32,000,000
Banks & Other Institutions	0	0	0	0
Total Temporary Borrowing	10,000,000	93,500,000	(71,500,000)	32,000,000
Total Borrowing	**69,394,681**	**96,500,000**	**(75,057,396)**	**90,837,285**

The borrowing (by loan type) at the end of the year is illustrated in the following pie chart:

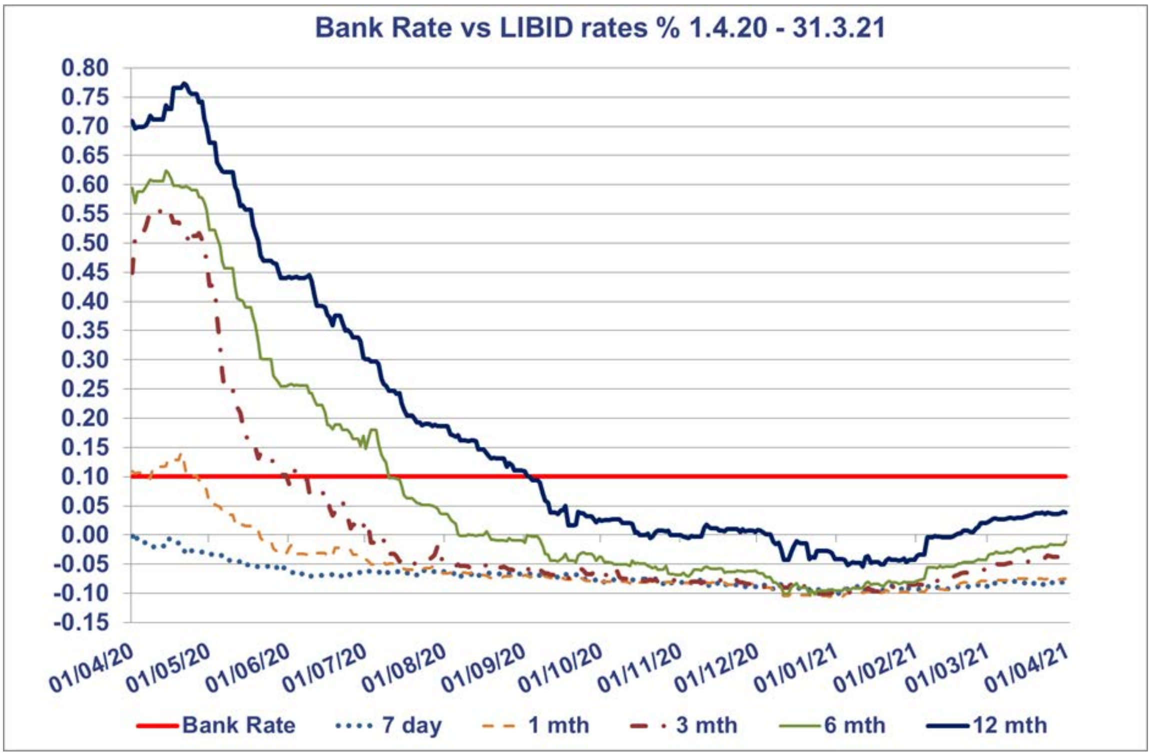


7. Minimum Revenue Provision (MRP) - 2020-21

The MRP policy has remained unchanged. There has been no additional revenue provision this year therefore the accumulated balance remains at £1m.

8. Investment Rates - 2020-21

Investment returns remained low during 2020-21. The coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its subsequent meetings, although some forecasters had suggested that a cut into negative territory could happen. However, the minutes of the Monetary Policy Committee in February 2021 made it clear that commercial banks could not implement negative rates within six months, and by that time the economy would be expected to be recovering strongly and so there would be no requirement for negative rates.



9. Investment Outturn - 2020-21

The Authority's investment policy is governed by the annual investment strategy incorporated within the Treasury Management 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.).

The investment activity during the year conformed to the approved strategy. There were no liquidity difficulties. The strategy has two levels of maximum investment allowable in Low Volatility Net Asset Values (LVNAVs) - successor of Money Market Funds - the general ceiling of £12m and an increased ceiling of £15m, which requires the authority of the CFO to the Commissioner to utilise. During the year there were 58 days which fell into the latter category. For clarity this is days per fund. On 53 days the increased ceiling of £15m was breached (with authority of the CFO to the Commissioner) when one of the LVNAVs dropped to a 0% return, the maximum held in one fund was £30m for 9 days. The average invested balance was £70.036m and earned 0.60% (£0.417m). This compares favourably to the average 7 day LIBID rate of -0.07%.

The following table gives information on the investments held at the start and end of the year:

	Position @ 01-04-20 £	Investments made £	Investments withdrawn £	Position @ 31-03-21 £
Temporary Investment				
Banks	(3,051,000)	(9,000,000)	8,023,000	(4,028,000)
Local Authorities	(30,000,000)	(85,000,000)	72,000,000	(43,000,000)
MMF	(12,090,000)	(334,760,000)	339,350,000	(7,500,000)
Total Investment	**(45,141,000)**	**(428,760,000)**	**419,373,000**	**(54,528,000)**

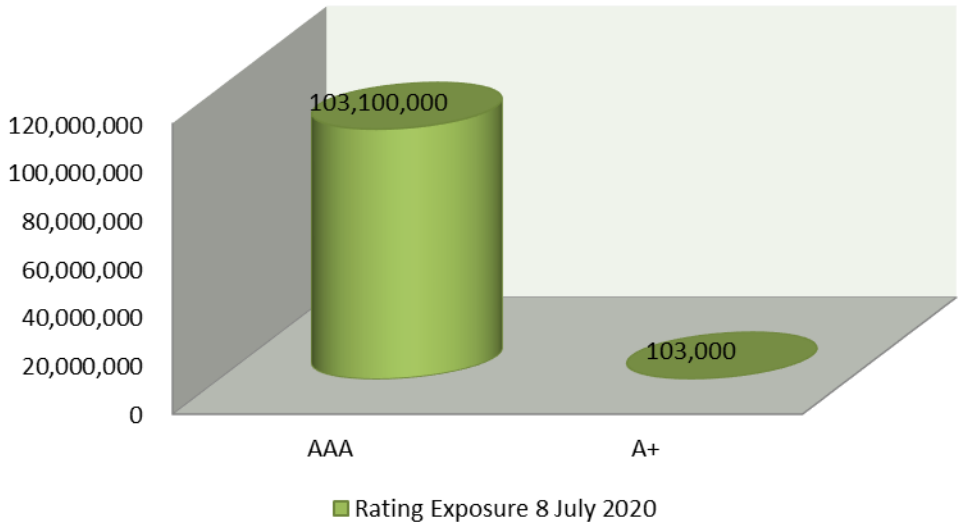
Investment:

	Position @ 01-04-20 £	Investments made £	Investments withdrawn £	Position @ 31-03-21 £
Fixed Term Investment	(30,000,000)	(90,000,000)	77,000,000	(43,000,000)
Variable Term Investment	(15,141,000)	(338,760,000)	342,373,000	(11,528,000)
	(45,141,000)	**(428,760,000)**	**419,373,000**	**(54,528,000)**

Proportion of Fixed Term Investment held	78.86%
Proportion of Variable Term Investment held	21.14%

10. Security of Investment

The quality of counterparties for investment is governed by the approved Treasury Management Strategy. This is monitored on a daily basis and an important part of this is the credit agency ratings. The maximum investment held during the year was £103.203m held on 08-07-20, when pension top up grant, other grants and precept had been received. The following graph shows the rating exposure on that day.



The majority of investments are made in LVNAVs which all carry a AAA rating, being the most secure available. The three being used by The Commissioner are as follows.

	Maximum Investment exposure 08-07-20 £m	Interest (Net 7 day yield) 08-07-20 %
LVNAVs		
Federated Investors	30.00	0.22
Aberdeen Liquidity	27.35	0.21
Black Rock	15.75	0.18

LVNAVs operate by spreading risk across a wide variety of counterparties many of which are not available to smaller investors. The impact of any counterparty failure is therefore minimised. It is also important that the Commissioner forms a minor part of the fund. At all times the PCC has formed less than 0.1 % of any fund.

11. Prudential and Treasury Indicators

During 2020-21 all legislative and regulatory requirements have been complied with.

The net borrowing and the Capital Financing Requirement (CFR) indicator ensures that borrowing levels are prudent over the medium term and that external borrowing, net of investments, must only be for a capital purpose. This essentially means that the borrowing cannot support revenue expenditure. In order to ensure this, the following key indicator of prudence is in place. External borrowing does not (except in the short term) exceed the total of CFR in the preceding year plus the estimates of any increases in CFR in the current and next two financial years.

The authorised limit is the “affordable borrowing limit” required by s3 of the Local Government Act 2003. It reflects a level of borrowing which, while not desired, could be afforded but may not be sustainable. The table below demonstrates that gross borrowing has remained within the authorised limit.

The operational boundary is based on expectations of the maximum external debt according to probable – not simply possible – events and is consist with the maximum level of external debt projected by the estimates. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit 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.

Prudential Indicator Monitoring 2020-21

	2018-19 Authority Approved Indicator	2018-19 Outturn @ 31 Mar 19	2019-20 Authority Approved Indicator	2019-20 Outturn @ 31 Mar 20	2020-21 Authority Approved Indicator	2020-21 Outturn @ 31 Mar 21
Section 1 - Indicators Based on Expected Outcomes						
Affordability:						
Ratio of Financing Costs to Net Revenue Stream	**2.1%**	**1.8%**	**2.0%**	**1.9%**	**2.1%**	**2.2%**
Incremental Impact of Capital Investment Decisions	**£1.20**	**-**	**£1.43**	**-**	**£1.17**	**-**
Capital Expenditure	**-**	**£9.653m**	**-**	**£8.850m**	**-**	**£30.369m**
Capital Financing Requirement	**£68.851m**	**£66.350m**	**£68.399m**	**£70.192m**	**£85.258m**	**£79.804m**
Section 2 - Indicators Based on Limits						
Affordability:						
Actual External Debt	**-**	**£51.349m**	**-**	**£69.395m**	**-**	**£90.837m**
External debt for Capital purposes		**£46.349m**		**£59.395m**		**£58.837m**
External Debt for Cashflow purposes		**£5.000m**		**£10.000m**		**£32.000m**
Authorised Limit for External Debt	**£80.000m**	**-**	**£85.000m**	**-**	**£95.000m**	**-**
Operational Boundary for External Debt	**£70.000m**	**-**	**£75.000m**	**-**	**£85.000m**	**-**
Prudence:						
Gross Debt & CFR	**£72.227m**	**£75.748m**	**£79.287m**	**£81.931m**	**£91.599m**	**£88.272m**