London Borough of Barnet

Appendix A: Treasury Management Outturn Report

1 April 2021 to 31 March 2022

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1. INTRODUCTION

1.1 Background

The council is 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 2021/22. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

During 2021/22 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 2nd March 2021)
- a mid-year (minimum) treasury update report (Council 1st March 2022)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

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

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all the above treasury management reports by either the Policy and Resources Committee or the Performance and Contract Management Committee before they were reported to the full Council. Member training on treasury management issues was undertaken on 14th June 2022 to support members' scrutiny role.

2. SUMMARY

2.1 Debt

During the year 2021/22, additional long-term borrowing of £100m was taken from the Public Works Loans Board in two £50m loans taken in May and July of 2021. The average annualised interest on the additional borrowing was 1.97%, which is considerably lower than the 2.90% average cost of borrowing across the council's overall debt portfolio. Further to this, there was a small reduction of outstanding interest free loans to the council from Salix of £1.1m.

Gross debt increased by £98.9m to £589.1m. Capital expenditure requiring funding by debt/internal balances was £115.3 million, which was below the TMSS projection for 2020 / 21 of £134.6 million.

2.2 Investments

Investment balances increased through the year, in part due to the new borrowing being taken to protect the capital programme by securing favourable low rates rather than to generate returns. Investments held rose £38.4m to £192.3m at year end.

2.3 Current Portfolio Position

The overall treasury management portfolio as at 31 March 2021 and the position as at 31 March 2022 are shown below for both borrowing and investments.

Investments and Borrowing				
	31.03.2021		31.03.22	
	£'000	%	£'000	%
Treasury Investments				
Money Market Funds	94,500	61.4%	10,250	5.3%
Local Authorities	-	0.0%	-	0.0%
Banks UK	49,400	32.1%	39,962	20.8%
Banks Overseas *	-	0.0%	117,100	60.9%
Other investments	10,000	6.5%	25,000	13.0%
Total treasury investments	153,900	100.0%	192,312	100.0%
* Refers to Overseas banks that are domiciled within the UK with a UK branch and all deposits are in Sterling				
Borrowing				
PWLB	421,580	86.0%	521,580	88.5%
Bank borrowing - LOBO's	62,500	12.8%	62,500	10.6%
Total long-term debt	484,080		584,080	
Short-term local authority debt	-	0.0%	-	0.0%
Interest free loans - Salix	6,088	1.2%	5,013	0.9%
Total Treasury Borrowing	490,168	100.0%	589,093	100.0%
Net Treasury Investments / (Borrowing)	(336,268)		(396,781)	
Other long-term liabilities – PFI**	(14,320)		(13,619)	
Net Investments / (borrowing)	**(350,588)**		**(410,400)**	
** Refers to the joint Streetlighting PFI lease liability				

Note: The 2022 Treasury Management Strategy Statement estimated PWLB borrowing at 31 March 2022 of £321.58m and £3m Salix. Subsequent to the 2022 TMSS being prepared the council borrowed £50m in both February and March 2021 explaining why the PWLB borrowing at 31 March 2022 disclosed above is different to that stated in the 2022 TMSS.   In addition, the Salix balance at 31 March 2022 disclosed above allows for £3.088m drawn down between March 2020 and March 2021 which was not allowed for in the 2022 TMSS. This results in a Salix balance at 31 March 2022 of £6.088m.

There are multiple models that can be used to calculate the residual PFI lease liability which will apply different assumptions. The PFI lease liability at 31 March 2021 is aligned to the Statement of Accounts 20/21 whereas last year's outturn report for 2020/21 used a different method. The amount disclosed at 2021/22 is expected to be aligned to what will be disclosed within the 21/22 Statement of Accounts

2.4 Treasury Management Strategy Statement Limits

There were no breaches of limits set out within the 2021/22 Treasury Management Strategy Statement as agreed by Council on 1st March 2021 during the year to 31st March 2022.

However, note that the Commercial Limit set out within the TMSS is likely to be reviewed this financial period to better reflect the definitions of Commercial Income and Service Income which are set out in the 2021 Draft Prudential Code.

3. THE ECONOMY AND INTEREST RATES

3.1 Economic Summary

The coronavirus outbreak has had a significant impact on the global economy and has done huge economic damage to the UK and economies around the world. This led the Bank of England to take emergency action in March 2020 to cut the Base Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16th December 2021, 0.50% at its meeting of 4th February 2022 and then to 0.75% in March 2022. Into the first quarter of the 22/23 financial year, we have continued to see steep rate rises with a further 0.25% increase in each of May and June, with current base rate at 1.25% and forecast to continue to rise.

Throughout the coronavirus pandemic, large numbers of businesses were forced to close or to operate at significantly reduced levels due to restrictions and workforce illness. With most of the economy opened up and nearly back to business-as-usual, the GDP numbers have been robust (9% y/y Q1 2022) and sufficient for the MPC to focus on tackling the second-round effects of inflation. At the end of March 2022, the 12-month CPI rate was 7% indicating strong inflationary pressures. In the 12 months to May 2022, CPI rose by 9.1% and supply side shortages, labour shortages, commodity price inflation, the impact of Russia's invasion of Ukraine and subsequent Western sanctions all point to inflation being at elevated levels until well into 2023.

Gilt yields fell towards the back end of 2021, but despite the war in Ukraine gilt yields have shot higher in early 2022. At 31st March 2022, 1.38%, 2-year yields remain close to their recent 11-year high and 10-year yields of 1.65% are close to their recent six-year high. These rises have been part of a global trend as central banks have suggested they will continue to raise interest rates to contain inflation.

Historically, rises in US Treasury yields drag UK gilt yields higher; there is a strong correlation between the two factors. However, the squeeze on real household disposable incomes arising from the 54% leap in April utilities prices as well as rises in council tax, water prices and many phone contract prices, are strong headwinds for any economy to deal with. In addition, from 1st April 2022, employees also pay 1.25% more in National Insurance tax.

4 TREASURY POSITION AT 31 MARCH 2022

At the beginning and the end of 2021/22, the Council's treasury, including borrowing by PFI and finance leases, position was follows:

TABLE 1	31 March 2021 (£'000)	Average Rate	Average Life	31 March 2022 (£'000)	Average Rate	Average Life
Debt	490,168	3.08%	27.3 yrs	589,093	2.90%	27.9 yrs
Other long-term liabilities	14,320			13,619		
Total debt	**504,488**			**602,712**		
CFR	736,666			839,422		
Over / (under) borrowing	**(232,178)**			**(236,709)**		
Total investments	153,900	0.11%	163 days	192,312	0.43%	110 days
Net debt	**350,588**			**410,400**		

Note: Investments exclude loans to Saracens and Open Door Homes (as these are included within CFR).

Through taking on £100m of new 50 year borrowing from the PWLB at an average cost of 1.97% in 2021/22, the council's average life of debt has increased and average cost of borrowing has fallen from 3.08% to 2.9% across its total external debt portfolio.

5 THE STRATEGY FOR 2021/22

During 2021-22, the Council maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow was used as an interim measure. This strategy was prudent as investment returns were low 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 has been kept under review and due to the scale of the capital programme, the ability to take on debt at low rates against forecasts of Bank Rate increases in the future, and avoid incurring higher borrowing costs in the future, the council entered into £100m of new long-term borrowing.

Investment returns remained close to zero for much of 2021/22 although negative rates were avoided. The expectation for interest rates within the treasury management strategy for 2021/22 was that Bank Rate would remain at 0.10% until it was clear to the Bank of England that the emergency level of rates introduced at the start of the Covid-19 pandemic were no longer necessary.

The Bank of England and the Government also maintained various monetary and fiscal measures, supplying the banking system and the economy with massive amounts of cheap credit so that banks could help cash-starved businesses to survive the various lockdowns/negative impact on their cashflow. 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 remained low until towards the turn of the year when inflation concerns indicated central banks, not just the Bank of England, would need to lift interest rates to combat the second-round effects of growing levels of inflation (CPI was 9.1% in May).

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.

The strategy of minimising both new debt and investment balances was tempered in both 2021-22 and the prior year as new borrowings of £100 million were taken in both years. This reflected the five-year projected capital programme that required funding of £582.9 million from April 2021 and expectations that borrowing rates will increase from their historic lows. As a consequence, protecting the affordability of the capital programme took precedence over the short term cost of carrying additional debt.

Long-term interest rates have risen by around 100bps over the period from March 2022 to June 2022, with a risk that rates might increase further still. Given the under borrowed position of the Council, the Council is exploring opportunities to lock in interest rates further during 2021/22. Whether the Council takes on further borrowing will be economically accessed, including considering the impact on short-term revenue due to cost of carry, the potential viability of the capital programme should rates rise further still and the relative value of PWLB borrowing costs relative to what could be achieved via Private Placements.

6 BORROWING REQUIREMENT AND DEBT

The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR). The table below summarises the opening, projected and closing capital positions for both the HRA and General Fund.

	31-Mar-21 Actual	31-Mar-22 Budget	31-Mar-22 Actual
CFR General Fund (£'000)	494,861	542,971	554,977
CFR HRA (£'000)	241,805	316,488	285,145
Total CFR (£'000)	**736,666**	**859,459**	**840,122**

The council has operated within the Prudential Indicators with an emphasis on high quality relatively liquid investments to ensure that cash is available to meet expenditure requirements. The Local Government Act 2003 requires the council to set maximum limits on its total outstanding debt. During the period to 31 March 2022, there were no breaches of the Authorised Limit (maximum permitted debt) and the Operational Boundary (the value of debt considered affordable).

The total value of long-term loans as at 31st March 2021 was £490.168m[1]. In the period spanning February 2021 to July 2021, £200m of new 50-year borrowing was acquired from the PWLB, with £100m being taken in each of 2020/21 and 2021/22, while £1.1m of interest free loans from Salix Finance Limited acquired to fund environment friendly projects were repaid in April 2021. The average rate of interest on the new PWLB borrowing (since February 2021) is 1.83% (range 1.71% to 1.95%) compared with a previous average interest rate for the existing long-term borrowing of 3.63% (prior to February 2021). Plans for additional borrowing to support the five-year capital programme will be taken in conjunction with advice from treasury advisors. Cash balances are sufficient to support the capital programme in the next 12 months although additional borrowing will be required to support the longer-term capital plans and as discussed below the timing of new debt will factor is projections of changes in borrowing costs.

The Council did borrow in advance of need in May and July as borrowing rates fell to a point where it was considered optimal to do so to finance capital expenditure which would be incurred within the time frame of the forward approved Capital Financing Requirement estimates. In taking this decision, the Council carefully considered achieving best value, the risk of having to borrow at higher rates later, 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 Council could ensure the security of such funds placed on temporary investment.

As stated, the total loans outstanding has increased in the four months by £98.9m to £589.74m (31 March 2021: £490.135m). The authorised debt limits (absolute maximum permitted) is £962.6m and the Operational Boundary (maximum consistent with long term affordability) is £858.4m. These limits were created from borrowing requirements detailed in the capital programme in February 2021 and apply to the 2021/22 financial year as detailed in the 2021-22 TMS.

[1] This figure excluded accounting accruals for interest due at year end.

The CFR is the amount of debt outstanding that was taken to finance the acquisition of capital assets. The setting aside of MRP each year is earmarked for the repayment of debt as it falls due. As debt should only be for capital purposes, normally borrowing should be less than the CFR indicating that all borrowing is for capital purposes. The operational boundary for external debt is the expected debt level if capital expenditure plans are fully implemented. For the period 2021/22 the limits below applied.

Prudential Indicators	Outturn at 31 March 2022 £'000
Capital Financing Requirement (CFR)	
CFR – Non-housing	554,977
CFR – Housing	285,145
Total CFR	**840,123**
Operational Boundary for External Debt	
Borrowing	944,574
Other long-term liabilities	13,088
Total Debt	**957,662**

The upper limit for variable rate exposure (40%) allows for the use of variable rate debt to offset changes in short-term investment returns. Currently the only variable debt is LOBO loans (because of the interest options). These represent 16% of current borrowing.

Table 3: Upper limits for Interest rate exposure

	Limits for 2021/22 %
Upper Limit for Fixed Rate Exposure	100
Compliance with Limits:	Yes
Upper Limit for Variable Rate Exposure	40
Compliance with Limits:	Yes

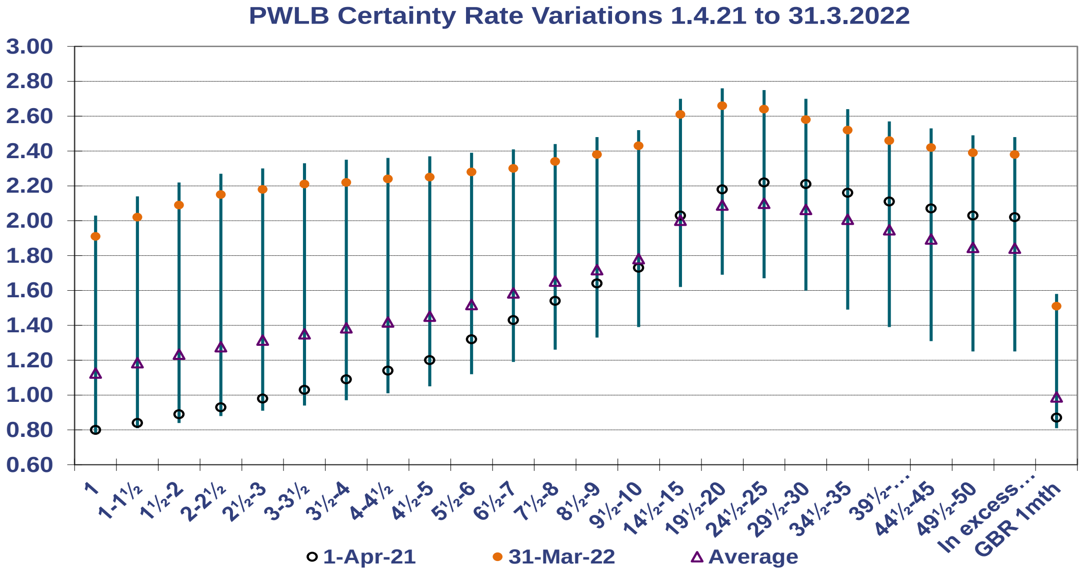
The below indicator is to limit large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates. Barnet debt is currently all long-term with no refinancing risk associated with short-term debt.

Table 4: Maturity Structure of Fixed Rate Borrowing

Maturity Structure of Fixed Rate Borrowing 31/03/22	Upper Limit %	Lower Limit %	Actual fixed Rate Borrowing £'000	Fixed Rate Borrowing Proportion %	Compliance with Set Limits?
Under 12 months	0	50	0	0.00%	Yes
12 months and within 24 months	0	50	2,000	0.34%	Yes
24 months and within 5 years	0	75	5,013	0.85%	Yes
5 years and within 10 years	0	75	91,032	15.45%	Yes
10 years and above	0	100	491,048	83.36%	Yes
Total			**589,093**	**100.00%**	

7 BORROWING RATES FOR 2021/22

The chart below represents the the PWLB certainty rate for different loan durations at 1st April 2021 (white circles), 31st March 2022 (orange circles), an average through 2021/22 (purple triangles) and the range through the year shown by the extremities of the horizontal bars.



PWLB rates are based on 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 inversion 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. Recently, yields have risen since the turn of the year on the back of global inflation concerns.

Gilt yields fell sharply from the spring of 2021 through to September and then spiked back up before falling again through December. However, by January sentiment had well and truly changed, as markets became focussed on the embedded nature of inflation, spurred on by a broader opening of economies post the pandemic, and rising commodity and food prices resulting from the Russian invasion of Ukraine.

At the close of the day on 31 March 2022, all gilt yields from 1 to 5 years were between 1.11% – 1.45% while the 10-year and 25-year yields were at 1.63% and 1.84%.

Regarding PWLB borrowing rates, margins attributed to their pricing are as follows: **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps), however as London Borough of Barnet sets out its capital expenditure plans to central government certifying no intention to invest for commercial income in their capital plans, it is possible to borrow by accessing the discounted **PWLB Certainty Rate** is gilt plus 80 basis points (G+80bps).

8 BORROWING OUTTURN FOR 2021/22

At 31 March 2022 the council had long-term borrowing totalling £521.58m from the Public Works Loans Board (PWLB) and Bank borrowing structured as Lender Option Borrower Option (LOBO) loans totalling £62.5m.

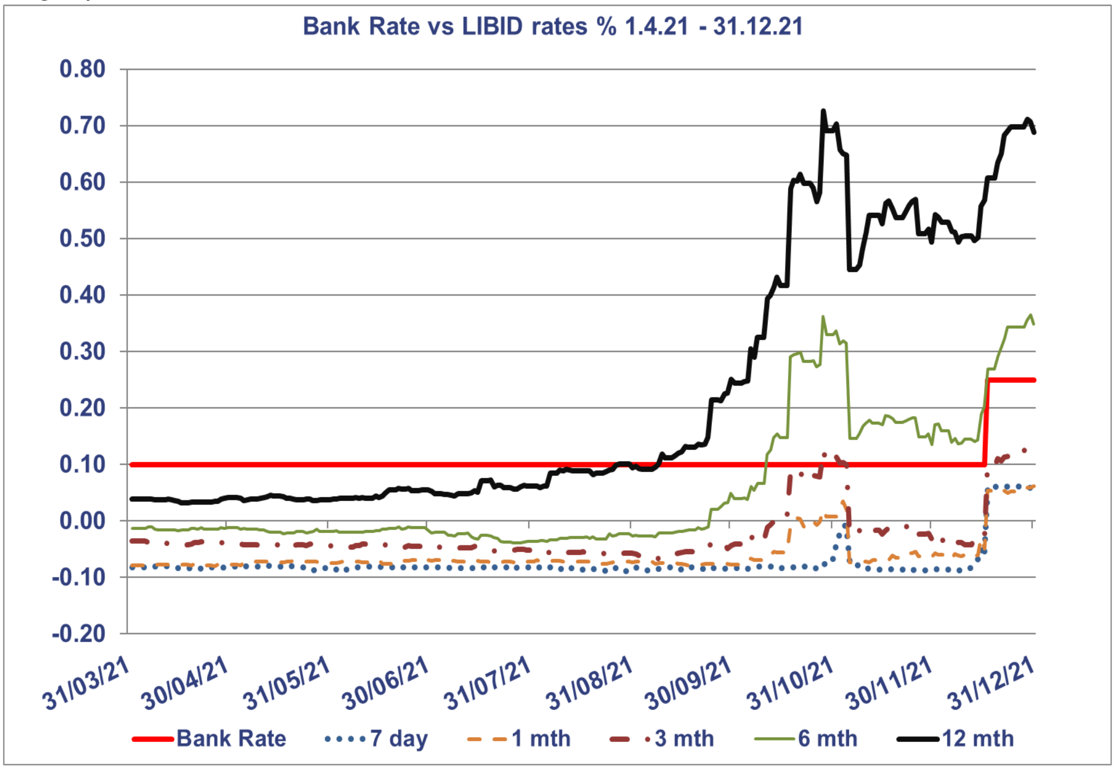
The council benefitted from the falling gilt yields and therefore PWLB rates during the year, undertaking £100m of new PWLB borrowing in 21/22, and is currently assessing options to agree forward rates of borrowing covering £180m of borrowing need between 23/24 and 25/26 to part fund its capital programme in order to remove the risk associated with the expected continuation of interest rises through 22/23 and beyond. These proactive measures to forward borrow are in line with the TMSS and seek to achieve a level of protection against rising Public Works Loans Board (PWLB) rates over the period where possible.

The council's LOBO loans next come under option in 2024, however given current long-term interest rates are lower than the rates being charged on these historical loans, lenders are unlikely to trigger their options to change the interest rates as this would give Barnet the opportunity to terminate the loans and seek to refinance at lower rates.

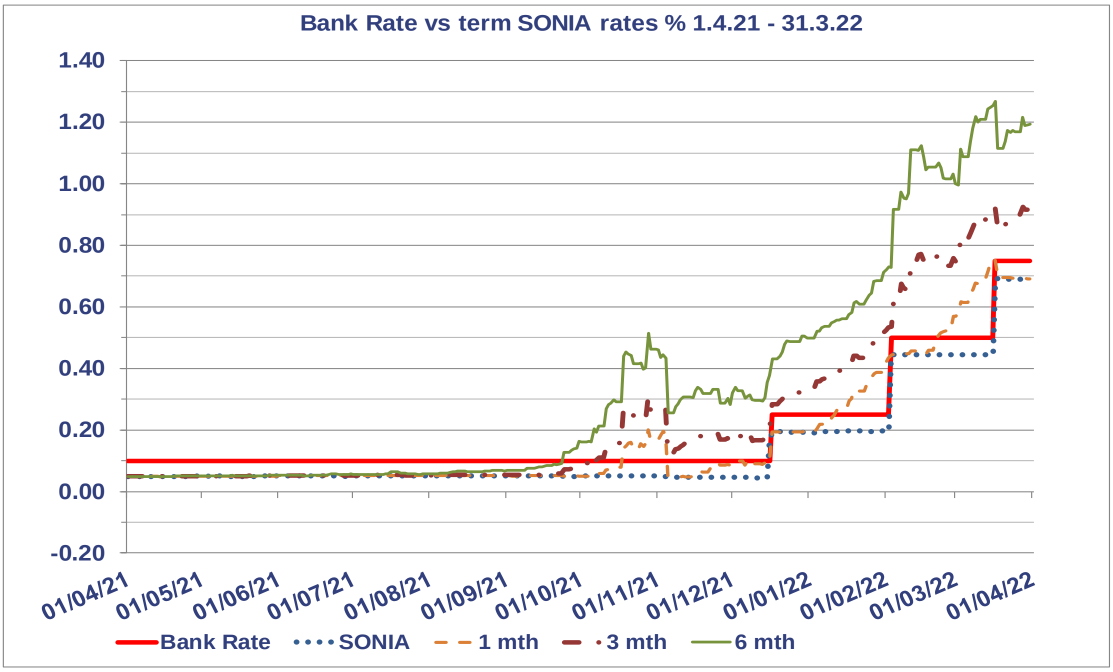
The council also has £5m of interest free loans from Salix.

9 INVESTMENT RATES FOR 2021/22

For consistency of comparison to previous rates, the below chart shows Bank Rate against the available data for LIBID rates which run to 31st December 2022 after which point it is no longer produced.



LIBID and LIBOR rates have both been phased out following recent issues with fixing and have been largely replaced by the Sterling Overnight Index Average (SONIA), which is shown below.



10 INVESTMENT OUTTURN FOR 2021/22

10.1 Investment Policy

The Council's investment policy, including timeframes and credit criteria for placing cash deposits, is governed by MHCLG guidance, which has been implemented in the annual investment strategy approved by the Council on 8th March 2021. 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 TMSS requires regular compliance reporting to include an analysis of deposits made during the period. This also reflects good practice and will serve to reassure that all current deposits for investment are in line with agreed principles as contained within the TMSS. A full list of the investments held by the council at 31st of March 2022 is in the table below.

The investment activity during the year conformed to the approved strategy, and the Council had retained sufficient cash balances to meet all its obligations on time.

10.2 Investments held by the council

Through improvements in cashflow reporting, the council has changed its mix of short-term investments to improve returns by investing over slightly longer periods with 37% of investments held beyond 3 months of 31 March 22. Short term investments are also benefitting from the uplift to the Bank of England base rates by the Monetary Policy Committee (MPC). These rates are currently at 1% with potential to rise further when the MPC next sits.

At 31 March 2022, the council held £192m in short-term liquid investments at an average rate of return of 0.43% (range from 0.17% to 1.51%) generating investment income of £0.657m for the financial year as detailed in the table below.

Counterparty	Principal (£'000)	Interest Rate (%)	Start Date	Maturity Date	Lowest long-term rating	Historic risk of Default (%)
Money Market Fund						
CCLA - The Public Sector Deposit Fund	9,850	0.39			AAA	0.04
Total Money Market	**9,850**					
Ultra Short-dated Bond Funds						
Aviva Investors Sterling Liquidity Plus Fund	400	0.17			AAA	0.04
Insight	24,962	-0.11			AAA	0.04
Total Ultra Short-dated Bond Funds	**25,362**					
Housing Associations (High credit quality)						
Southern Housing Group Ltd.	5,000	0.70	04-May-21	10-Aug-22	A-	0.05
Metropolitan Housing Trust Ltd.	10,000	0.90	10-Mar-22	11-Aug-22	A-	
Places for People Treasury PLC.	10,000	1.00	15-Mar-21	12-Aug-22	A-	0.05
Total Housing Associations	**25,000**					

Counterparty	Principal (£'000)	Interest Rate (%)	Start Date	Maturity Date	Lowest long-term rating	Historic risk of Default (%)
Banks						
Goldman Sachs International Bank	10,000	0.40	19-Apr-21	19-Apr-22	A+	0.05
Santander	10,000	0.35	19-May-21	19-May-22	A	0.05
Santander	15,000	0.35	26-Jul-21	26-Jul-22	A	0.05
ANZ Banking Group	7,500	0.17	26-Jul-21	26-Jul-22	A+	0.05
ANZ Banking Group	6,200	0.30	08-Oct-21	27-Jul-22	A+	0.05
Goldman Sachs International Bank	10,000	0.37	15-Oct-21	28-Jul-22	A+	0.05
Helaba Landesbank Hessen-Thuringen	5,000	0.30	03-Dec-21	29-Jul-22	A	0.05
ANZ Banking Group	8,200	0.53	05-Jan-22	30-Jul-22	A+	0.05
Helaba Landesbank Hessen-Thuringen	10,000	0.62	06-Jan-22	31-Jul-22	A	0.05
SMBC	6,000	0.48	20-Jan-22	01-Aug-22	A	0.05
Landesbank Baden Wurttemberg	10,000	0.41	21-Jan-22	02-Aug-22	A-	0.05
Landesbank Baden Wurttemberg	14,200	0.41	21-Jan-22	03-Aug-22	A-	0.05
Goldman Sachs International Bank	5,000	1.51	07-Feb-22	04-Aug-22	A	0.05
Close Brothers	10,000	0.45	01-Jul-21	05-Aug-22	A-	0.05
Close Brothers	5,000	0.55	30-Jul-21	07-Aug-22	A-	0.05
Total Banks	**132,100**					
Total Investments	**192,312**	**0.43**				**0.05**