Agenda Item 11

Leicestershire County Council

CORPORATE GOVERNANCE COMMITTEE: 29TH January 2021

QUARTERLY TREASURY MANAGEMENT REPORT

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

Purpose of report

1. The purpose of this report is to update the Committee on the actions taken in respect of treasury management for the quarter ending 31 December 2020 (Quarter 3).

Policy Framework and Previous Decisions

2. The annual investment strategy forms part of the Council's medium term financial strategy (MTFS) and was approved by full council in February 2020.

3. An update in respect of Quarter 2 2020/21 was provided to the committee on 25th November 2020.

Background

4. Treasury Management is defined as:

   "The management of the organisation'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".

5. A quarterly report is produced for the Committee to provide an update on any significant events in treasury management.

Economic Background

6. The Council's treasury management adviser, Link Asset Management, provides a quarterly update outlining the global economic outlook and monetary policy positions. An extract from this report is attached as Appendix A to this report. The key points are summarised below.

7. The final quarter of 2020 is expected to see gross domestic product (GDP) contract by around 3.5% compared to the last quarter. The tightening of restrictions in October and subsequent lockdown will weigh heavily on the economy. However, the impact is not expected to be as severe as the first lockdown in March 2020 and the recent vaccine developments and subsequent commencement of roll-out offer an improved outlook going forwards.

8. Inflation is expected to remain below 2% into 2022, owing to spare capacity and weaker inflationary pressure. Food and clothing inflation accounted for an acceleration in the consumer price index (CPI) towards the end of last year, but the current lockdown and ongoing COVID restrictions are expected to keep inflation low in the coming months.

9. The role of central banks, and by extension monetary policy, is not expected to change in the short term as despite the recent vaccine developments it is anticipated that it will take several months to roll out inoculations, meaning restrictions are likely to be maintained for a while yet. Given this, the biggest risk facing central banks is that they act too quickly to pare back their support and ultimately damage economic recovery.

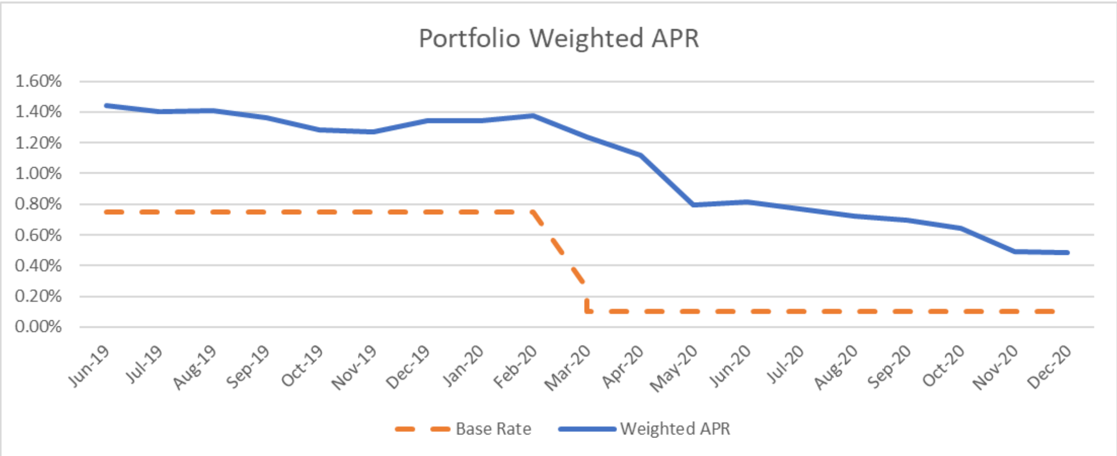
Action Taken During Quarter 3 to December 2020

10. The balance of the investment portfolio increased from £273.3m to £287.4m. Within the portfolio, £129.9m of investment loans matured at an average rate of 0.67% (excluding Private Debt), and £145.3m of new loans were placed, at an average rate of 0.24%. The Council also received capital receipts for the partners private debt investment totalling £1.3m.

11. To date the County Council has received four distributions from the private debt investment totalling £3.3m. Of this £2.9m represents return of invested capital, with the remaining £0.4m representing interest received. This means from an initial investment of £20m the council has £17.1m remaining capital committed. The private debt investment represents only a small portion of total portfolio, but, with a current internal rate of return (IRR) of 4.2%, is contributing significantly to the total portfolio annual percentage rate (APR). The APR including private debt is 0.48% versus a loans only APR of 0.25%.

12. The average rate achieved on new loans continues to fall short of the average rate of loans maturing. This was expected due to the reduction in base rates and the trend is likely to continue, as the markets do not foresee an increase in rates any time soon. As a result, the portfolio weighted APR reduced from 0.69% in Q2 20-21 to 0.48% in Q3 20-21.

13. The chart below shows the weighted APR achieved by the treasury portfolio compared to the Bank of England base rate:



14. The loan portfolio at the end of December was invested with the counterparties shown in the list below, shown by original investment date:

	£m	Maturity Date
Instant Access		
Money Market Funds	65.2	January 2021
6 Months		
HSBC	30.0	January 2021
Nationwide Building Society	10.0	January 2021
Santander	20.0	March 2021
Close Brothers	15.0	March 2021
Close Brothers	10.0	April 2021
Santander	5.0	May 2021
Goldman Sachs	25.0	May 2021
Nationwide Building Society	10.0	May 2021
Australia and New Zealand Bank	20.0	July 2021
12 Months		
HSBC	10.0	March 2021
National Westminster Bank Plc	10.0	August 2021
Lloyds (Bank of Scotland)	20.0	September 2021
National Westminster Bank Plc	10.0	November 2021
Beyond 12 Months		
Partners Group (Private Debt)	17.1	Estimated 2024
Danske Bank	10.0	September 2027
Total Portfolio Balance at 30 September 2020	**287.3**	

15. Market conditions remain challenging, as outlined in the last quarterly update, yields continue to fall and demand for capital has not picked up. The Council will continue its low risk approach to treasury management whilst trying to be mindful of rates earned.

16. Since the end of Q3 there have been some developments in the short end of the market and in particular, money market funds (MMFs). The Council primarily uses MMFs to store its working capital (the day to day funds required to pay for services). The key benefits to using MMFs is that they satisfy the need for capital protection (providing a level of diversification the Council would be unable to achieve on its own), whilst also remaining highly liquid – usually providing instant access.

17. Yields on MMFs have been falling rapidly since the reduction in the Bank of England (BoE) base rate in March 2020. In most funds, managers have lowered or waived fees to keep yields positive for investors. Despite this, the net yields in two of the four funds regularly used by the Council have fallen to 0%.

18. Given current market conditions, this fall to zero yield was not unexpected and in context only represents a reduction in income of 0.1%. However, given the availability of funds providing a positive yield the most prudent approach was deemed to be to temporarily restrict use of the zero yield funds whilst officers monitored the impact of the rate reduction on overall fund size and liquidity.

Loans to Counterparties that breached authorised lending list

19. There were no loans active during the period that breached the authorised counterparty list at the time that the loan was made.

Resource Implications

20. The interest earned on revenue balances and the interest paid on external debt will impact directly onto the resources available to the Council. For 2019/20 the interest generated by treasury management activities raised £2.5m. For 2020/21 the expected level of interest is expected to be significantly less than this at approx. £1.3m compared to a budget of £2.8m.

Recommendations

21. The Committee is asked to note this report

Background papers

22. None

Circulation under the Local Issues Alert Procedure

23. None

Equality and Human Rights Implications

24. There are no discernible equality and human rights implications.

Appendices

25. Appendix – Economic Overview (November 2020)

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