CHESHIRE FIRE AUTHORITY

MEETING OF:	**CHESHIRE FIRE AUTHORITY**
DATE:	**22 JUNE 2022**
REPORT OF:	**HEAD OF FINANCE**
AUTHOR:	**WENDY BEBBINGTON**

SUBJECT: **TREASURY MANAGEMENT ANNUAL REPORT 2021-22**

Purpose of Report

1. To present a review of the Authority's treasury management activities undertaken during 2021/22.

Recommended: That

[1] the report on treasury management activity for 2021-22 be noted; and

[2] the performance against the prudential and treasury management indicators be noted.

Background

2. The Chartered Institute of Public Finance and Accountancy (CIPFA) define treasury management as 'The management of the organisation's borrowing, investments and cash flows, including 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. The associated Code of Practice for Treasury Management recommends that those charged with governance are updated on treasury management activities regularly by way of a strategy at the start of the year, a mid-year review and an outturn report.

4. The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report provides Members with details of the treasury management activities undertaken in 2021/22. It also highlights compliance with the Authority's policies previously approved by Members.

5. This report includes details of:

    a. the Authority's loans portfolio position at 31 March 2022;
    b. the Authority's investment portfolio position at 31 March 2022;

c. a summary of performance for the year 2021/22;
d. the Authority’s performance in 2021/22 set against the key Prudential and Treasury Indicators

6. Members should be aware that all the 2021/22 figures in the report remain subject to audit.

The Economy and Interest Rates

7. Over the last two years, the Coronavirus Pandemic has done huge economic damage to the UK economy and to economies around the world. Investment returns remained close to zero for much of 2021/22. The expectation for interest rates within the treasury management strategy for 2021/22 was that the Bank Rate would remain at 0.1% until it was clear to the Bank of England that the emergency level of rates introduced at the start of the Pandemic were no longer necessitated and this proved to be the case. After the Bank of England took emergency action in March 2020 to cut the Bank Rate to 0.10%, it left the 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, 0.75% in March 2022 and then to 1% in May 2022.

8. The Bank of England and the Government also maintained various monetary and fiscal measures, supplying the banking system and the economy with cheap credit so that banks could help cash-starved businesses to survive the various lockdowns and 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. The consequent effect was that investment earnings rates remained low until towards the turn of the year when inflation concerns suggested that banks would need to lift interest rates to combat the second-round effects of growing levels of inflation (CPI was 6.2% in February 2022).

9. While the Authority has maintained 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 have been introduced over recent years. These requirements have provided a far stronger baseline 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.

10. Table 1 below provides a summary of the Public Works Loan Board (PWLB) maturity loan borrowing rates comparing the start of the year and the end of the year and provides a picture of how the rates moved throughout the year.

Table 1

	1 Year	5 Year	10 Year	25 Year	50 Year
01/04/2021	0.80%	1.20%	1.73%	2.22%	2.03%
31/03/2022	1.91%	2.25%	2.43%	2.64%	2.39%
Low	0.78%	1.05%	1.39%	1.67%	1.25%
Low date	08/04/2021	08/07/2021	05/08/2021	08/12/2021	09/12/2021
High	2.03%	2.37%	2.52%	2.75%	2.49%
High date	15/02/2022	28/03/2022	28/03/2022	23/03/2022	28/03/2022
Average	1.13%	1.45%	1.78%	2.10%	1.85%
Spread	1.25%	1.32%	1.13%	1.08%	1.24%

Outlook for 2022/23

11. In 2022/23, there is an expectation that higher inflation, rather than the rise in interest rates, will trigger an economic slowdown in the UK. Overall, markets are not forecasting a recession but with an anticipated negative impact on GDP from higher interest rate grown from Q2 of this year, there remains a risk that tighter monetary policy could tip the economy into recession.

12. The impact of the terms of trade disruption caused by the war in Ukraine, stronger than expected pipeline energy prices, and a tighter domestic labour market mean that inflation may be higher for longer than previously anticipated. Markets are expecting that CPI inflation may rise to a peak of 10% in October. Much of this further rise in inflation is due to the 54% jump in Ofgem's utility price cap introduced earlier this year, and markets anticipating an additional 30% price cap rise in October.

13. Even though a further surge in CPI inflation to a peak of 10% may take the economy to the brink of recession, the expectation is that the Bank of England (BoE) will raise interest rates further, from 1% now to a peak of 2.00% in Q1 (January – March) 2023.

14. The BoE struck a more dovish tone in early May after raising interest rates from 0.75% to a 13-year high of 1.00%, arguing that it won't make a decision until after August on whether to reduce its balance sheet faster by selling gilts. Although the BoE revised up its near-term forecast so that inflation rises from 7.0% in March 2022 to a peak of just over 10% in Q4 (October – December) 2022 or Q1 (January – March) 2023, rather than a peak of 8% in Q2 (April – June) 2022, it revised down its inflation forecast further ahead. Based on market expectations that interest rates will rise to up to 2.5%, CPI inflation is expected to be well below the 2% target in 2-3 years' time (1.30% in Q1 2025).

Portfolio Position at 31 March 2022

15. A summary of the Authority's long-term borrowing and investments at 31 March 2022 is shown in Table 2, including the equivalent position at 31 March 2021 for reference.

Table 2 – Portfolio Position		
	31 March 2021 £000	31 March 2022 £000
Long Term Borrowing	5,012	12,012
Treasury Investments	(13,804)	(18,646)
Net Borrowing / (Investments)	(8,792)	(6,634)

Note: All investments held relate to Treasury Management activities. The Authority has not engaged in any commercial investments and has no non-treasury investments.

16. Long-term borrowing as at 31 March 2022 is made up entirely of maturity loans from the Public Works Loans Board (PWLB). New PWLB loans totalling £7m towards the approved Capital Programme requirement were secured in July 2021 (£4m at 1.65%) and November 2021 (£3m at 1.63%).

17. Investment balances (including cash on deposit in Money Market Funds) have increased during 2021/22. This is due to both securing the remaining £7m of planned borrowing in respect of the Operational Training Centre project during 2021/22 and pausing the Fire Station Modernisation programme whilst a review is carried out, which is planned to be funded from cash reserves.

Treasury Management Performance 2021/22

Investments

18. In the current climate it remains impossible to generate significant levels of investment income. Investment income in 2021/22 is £41k, reduced from the £49k generated in 2020/21. This year-on-year decrease despite higher cash balances towards the end of the year is mainly due to available investment rates with suitable counterparties again being barely above zero for most of the year and lower than in 2020/21 when some higher medium term rates had already been secured prior to the Pandemic.

19. The Authority has continued with a cautious approach to its choice of counterparties. As at 31 March 2022, the Authority's investments are with Santander UK, Goldman Sachs PLC, Aberdeen Standard Liquidity Money Market Fund and in its National Westminster Bank Liquidity account, which

the Authority continues to use regularly to manage day to day cashflows. No other investment counterparties were used during 2021/22.

20. There have been no instances of non-compliance with Treasury Management Practices during the year.

Borrowing

21. The amount of borrowing as at 31 March 2022 is £12.012m. During 2021/22 interest rates have been monitored and no debt rescheduling took place during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unwise.

22. As previously reported to Members and in line with the currently approved Treasury Management Strategy, £11m of this current borrowing relates to the Training Centre which was initially deferred due to the temporarily high levels of reserves held which allowed some flexibility about the timing of the borrowing.

23. This borrowing was provisionally planned for early in 2021/22, however, due to an upward risk to borrowing rates towards the end of 2020/21, along with reducing cash balances, the Treasurer considered it prudent to secure the first £4m of this borrowing in February 2021 from PWLB at a favourable fixed long term interest rate of 1.99%. The situation was then kept under close review and following consultation between the appointed Treasury Management Advisors and the Authority's Treasurer, the remaining £7m of this approved borrowing has now been secured from PWLB during 2021/22, also at very favourably low fixed rates, in July 2021 (£4m at 1.65%) and November 2021 (£3m at 1.63%).

24. The Authority currently remains in an under-borrowed position, which means that historically decisions have been made to internally finance expenditure as opposed to borrowing. The current position is £4.1m under-borrowed and is in line with the approved Treasury Management Strategy. The strategy is to now increase internal borrowing over the period of major Estates projects delivery, through careful cashflow management, in order to minimise new long-term external borrowing.

25. The actual maturity structure for borrowing can be seen in Table 3. This indicator is designed to be a control over an authority having large concentrations of fixed rate debt which need to be replaced at times of uncertainty over interest rates. The limits set represent sensible boundaries and are intended to draw attention to potential issues before they arise. There are currently no potential issues.

Table 3 - Maturity Structure of Borrowing				
	Upper Limit %	**Lower Limit %**	**Actual %**	**Amount £000**
Under 12 months	25	0	0	0
12 months and within 24 months	25	0	3	426
24 months and within 5 years	50	0	5	586
5 years and 10 years	75	0	0	0
10 years and above	100	5	92	11,000
Total			100	12,012

Prudential and Treasury Indicators

26. The Authority must approve Prudential and Treasury Indicators annually, to reflect the impact of the capital programme on the Authority's financial position. Table 4 below shows performance in 2021/22 against the indicators, which were approved by the Authority in February 2021.

Table 4: Prudential and Treasury Indicators			
Prudential Indicators	2021/22 Indicator £000	2021/22 Outturn £000	Comment
Capital expenditure	8,228	4,967	Pause to review Fire Station Modernisation project and Crewe FS re-phasing, offset by vehicle replacement slippage from 2020/21.
Capital financing requirement Annual change in capital financing requirement	16,126 3,332	16,126 3,332	
Gross borrowing requirement: (Under) / Over borrowing	(4,114)	(4,114)	
Ratio of financing costs to net revenue stream	1.97%	1.77%	Lower than anticipated cost of new borrowing + Although interest on investments was low, it was higher than the approved budget

Table 4: Prudential and Treasury Indicators			
Treasury Indicators	2021/22 Indicator £000	2021/22 Outturn £000	
Authorised limit for external debt Operational boundary for external debt	14,212 12,212	14,212 12,212	Set 10/2/21, no change during 2021/22.
Actual external debt - Borrowing - Other long term liabilities Total	 12,012 0 12,012	 12,012 0 12,012	Approved borrowing now secured.
Upper limit of fixed interest rate exposure	100%	100%	
Upper limit of variable interest rate exposure	25%	Nil	No variable rate loans held or planned
Upper limit for principal sums invested for over 364 days	£5m	£nil	No longer term investments held or planned.

27. The above table shows that the Authority remained within both the authorised limit and operational boundary for external debt. These are limits on the amount of external debt permitted and include both loans and financial leases.

28. With the exception of some re-profiling of expenditure relating to both the Fire Station Modernisation Programme and the Crewe Fire Station replacement project, capital expenditure was broadly in line with anticipated spending levels.

Conclusion

29. Investment interest rates have remained very low throughout the year but are forecast to increase in the current financial year. Opportunities for seeking improved returns will continue to be pursued within the approved confines of the Annual Investment Strategy.

30. Borrowing levels remain sustainable. £11m of new borrowing has now been secured at very low fixed rates to finance the Training Centre. Further borrowing is required to finance the currently approved Capital Strategy and this will be secured at the optimum point taking into account available cash balances along with prevailing and forecast market rates.

Financial Implications

31. The report is in its nature financial and the implications are covered in the body of the report.

Legal Implications

32. All transactions between the Authority and counterparties are governed by the agreements between the two parties, and overseen by our Treasury Management partner Link Asset Services.

Equality and Diversity Implications

33. There are none.

Environmental Implications

34. There are none.

CONTACT: DONNA LINTON, GOVERNANCE AND CORPORATE PLANNING MANAGER
TEL [01606] 868804
BACKGROUND PAPERS: NONE