

APPENDIX A

SUMMARY OF TREASURY MANAGEMENT ACTIVITIES 2021-22 1 APRIL TO 30 SEPTEMBER 2021

1. External Debt and Investment Position

On 30 September 2021, the Council held £96.87 million of external long-term borrowing and £79.84 million of investments. The Council's external debt and investment position for 1 April to 30 September 2021 is shown below in Table 1; more detail is provided in section 3 - Borrowing Strategy and Outturn - and section 4 - Investment Strategy and Outturn:

Table 1: External debt and investment position 1 April 2021 to 30 September 2021

	Principal 01/04/2021 £m	Average Rate 01/04/2021 %	Principal 30/09/2021 £m	Average Rate 30/09/2021 %
External Long Term Borrowing:				
Public Works Loan Board	77.62	4.70	77.62	4.70
Lender's Option Borrower's Option	19.25	4.65	19.25	4.65
Total External Borrowing	96.87	4.69	96.87	4.69
Other Long Term Liabilities (LTL):				
Private Finance Initiative (PFI)*	15.56		15.16	
Other LTL	2.33		2.81	
Total Other Long Term Liabilities	17.89		17.97	
Total Gross External Debt	114.76		114.84	
Treasury Investments:				
Debt Management Office	0.00	0.00	15.34	0.01
Local Authorities	48.50	0.22	28.50	0.13
Banks	1.00	0.05	12.00	0.04
Money Market Fund***	2.05	0.02	24.00	0.01
Total Treasury Investments	51.55	0.21	79.84	0.06
Net Debt	63.21		35.00	

* (PFI) arrangement for the provision of a Secondary School in Maesteg 12.75 years remaining term

*** these funds provide instant access

Where a Council finances capital expenditure by debt, it must put aside revenue resources to repay that debt in later years and this amount charged to revenue is called the Minimum Revenue Provision (MRP). The Local Authority (Capital Finance and Accounting) (Amendment) (Wales) Regulations 2008 requires the Council to produce and approve an annual Minimum Revenue Provision (MRP) Statement before the start of the financial year that details the methodology for the MRP charge and this is detailed in the Council's Capital Strategy. The underlying need to borrow for capital purposes is measured by the Capital

Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to delay the need to borrow externally by temporarily using cash it holds for other purposes such as earmarked reserves. This is known as internal borrowing. This strategy is prudent as investment returns are low and counterparty risk is relatively high. The CFR is forecast to increase from 2020-21 levels due to the amount of prudential borrowing in the capital programme in future years. The Loans CFR is estimated to be £170.25 million as shown in table 2 below.

The liability benchmark measures the Council's projected net debt requirement plus a short-term liquidity allowance in the form of minimum cash and investment balances. The purpose of the benchmark is to set the level of risk which the Council regards as its balanced or normal position. The forecast liability benchmark, or level of debt, as at 31 March 2022 is £100.31 million, which is lower than the estimate within the TMS. The current level of long-term borrowing is £96.87 million. As the Council has available reserves it can use them to fund capital expenditure in the short term, which is a prudent approach to managing its cash resources. Table 2 below has been produced using estimates of capital spend and forecasts on usable reserves for the current financial year. The Loans CFR ignores cash balances and may be too high if the authority benefits from long term positive cash flows which this Council does benefit from. The benchmark assumes that cash and investment balances are kept to a minimum level of £10 million at each year-end to maintain sufficient liquidity but minimise credit risk.

Table 2: Liability benchmark

	2020-21 Actual	2021-22 Estimate TMS	2021-22 Projection
	£m	£m	£m
Loans Capital Financing Requirement	158.21	166.35	170.25
Less: Usable reserves	(114.43)	(49.11)	(79.94)
Plus: Actual/Minimum investments	10	10	10
Liability Benchmark	53.78	127.24	100.31

2. External Context

The Bank of England (BoE) has continued to hold the Bank Rate at 0.1% following the Monetary Policy Committee (MPC) voting unanimously for rates to remain unchanged at its meeting of 22 September 2021.

Annual CPI inflation rose to 2.1% in May and then again to 3.2% in August. As inflation rates during the pandemic remained low, small increases have a relatively large impact on the current inflation rate. In addition global cost pressures have continued to affect UK consumer goods prices. To a lesser degree, the reopening of the economy has led to a further increase in some

consumer services prices. Inflation expectations are currently being driven by rising oil prices and, in the UK, on-going signs of supply shortages. The HGV driver shortage and the higher wages being offered in that sector are likely symptomatic of the various effects of both Brexit and the pandemic.

The furlough scheme ended at the end of September with the Bank of England only expecting a small rise in unemployment. Since March 2020 when the pandemic began and the Coronavirus Job Retention Scheme was introduced, the furlough scheme has supported the wages of 11.6 million workers at a cost of over £68 billion. However, the impact of the ending of the scheme will only be known over the forthcoming months.

3. Borrowing Strategy and Outturn for 1 April to 30 September 2020

At 30 September 2021, the Council held £96.87 million of long-term loans as part of its strategy for funding previous years' capital programmes. The TMS 2021-22 forecast that the Council would need to borrow £30.37 million in 2021-22. Currently it is forecast that the Council will not need to take out new borrowing during the year, however this is dependent on the progress of the Capital Programme expenditure during the year and the use of available earmarked reserves during the year. More detail on forecast capital spend is provided in the Capital Strategy 2021-22 which was approved by Council on 24 February 2021 and the Quarter 2 Capital Monitoring report going to Council on 20 October 2021.

The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans, should the Council's long-term plans change, is a secondary objective. Therefore the major objectives to be followed in 2021-22 are:

- to minimise the revenue costs of debt
- to manage the Council's debt maturity profile i.e. to leave no one future year with a high level of repayments that could cause problems in re-borrowing
- to effect funding in any one year at the cheapest cost commensurate with future risk
- to monitor and review the level of variable interest rate loans in order to take greater advantage of interest rate movement
- to reschedule debt if appropriate, in order to take advantage of potential savings as interest rates change
- to optimise the use of all capital resources including borrowing, both supported and unsupported, usable capital receipts, revenue contributions to capital and grants and contributions

Given the impact of the Covid-19 pandemic on the economy and public finances in general, as well as on local government funding in particular, and the uncertainty going forward, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term

stability of the debt portfolio. The ever increasing uncertainty over future interest rates increases the risks associated with treasury activity. As a result the Council will take a cautious approach to its treasury strategy. With short-term interest rates currently much lower than long term rates, it is likely to be more cost effective in the short term to either use internal resources or take out short term loans instead.

The Council's primary objective for the management of its debt is to ensure its long term affordability. The majority of its loans have therefore been borrowed from the Public Works Loan Board (PWLB) at long term fixed rates of interest but we will also investigate other sources of finance, such as Welsh Government and local authority loans and bank loans that may be available at more favourable rates. Following the increase in the numbers of local authorities taking out PWLB loans to buy commercial properties for yield, following a UK government consultation HM Treasury issuing revised lending terms for PWLB borrowing by local authorities in November 2020. As a condition of accessing the PWLB, local authorities will be asked to confirm that there is no intention to buy investment assets primarily for yield in the current or next two financial years. Local authorities' Section 151 Officers, or equivalent, will be required to confirm that capital expenditure plans are current and that the plans are within acceptable use of the PWLB. Whilst this in itself does not preclude the Council from investing in commercial activities, investing in assets for yield would preclude the Council from accessing PWLB borrowing. Given the investment and borrowing requirement to support the Capital Programme, the Council is unlikely to consider any investments in commercial assets primarily for yield. CIPFA are also currently undertaking a consultation on proposed changes to the Prudential Code and Treasury Management Code of Practice. The outcome of this consultation will provide further clarification around what is commercial activity and investment and confirm that the purchase of property cannot lead to an increase in the capital financing requirement. It will also set out that it would not be considered prudent for a Local Authority to borrow to invest primarily for financial return, and therefore it must not do so.

The last time the Council took out long term borrowing was £5 million from the PWLB in March 2012. Should there be a need to borrow it is likely to be from the PWLB. For estimate purposes it has been assumed that this would be over 30 years. The Council may also take out short term loans (normally for up to one month) to cover unexpected cash flow shortages. Market conditions have meant that there has been no rescheduling of the Council's long term borrowing so far this year however, in conjunction with the Council's Treasury Management advisors Arlingclose, the loan portfolio will continue to be reviewed for any potential savings as a result of any loan rescheduling.

The £19.25 million in table 1 above relates to Lender's Option Borrower's Option (LOBO) loans which have a maturity date of 2054, however these may be re-scheduled in advance of this maturity date. The LOBO rate and term may vary in the future depending upon the prevailing market rates, the lender exercising their option to increase rates at one of the bi-annual trigger points (the trigger dates being July and January) and therefore, the Council being

given the option to accept the increase or to repay the loan without incurring a penalty. The lender did not exercise their option on 22 July 2021 and the next trigger point is 22 January 2022. The lender is unlikely to exercise their option in the current low interest rate environment, however, an element of refinancing risk remains. The Council would take the option to repay these loans at no cost if it has the opportunity to do so in the future. The current average interest rate for these LOBO's is 4.65% compared to the PWLB Loans average interest rate of 4.70%. The premiums payable to renegotiate the Council's Lender's Option Borrower's Option (LOBO) continues to be cost prohibitive.

The Treasury Management indicator shown in Table 3 below is for the Maturity Structure of Borrowing and is set for the forthcoming financial year to control the Council's exposure to refinancing risk with respect to the maturity of the Council's external borrowing and has been set to allow for the possible restructuring of long term debt where this is expected to lead to an overall saving or reduction in risk. It is the amount of projected borrowing maturing in each period as a percentage of total projected borrowing. The upper and lower limits on the maturity structure of borrowing set out in the TMS 2021-22 and the projections for 2021-22 are:

Table 3: Treasury Management Indicator Maturity Structure of Borrowing 2021-22

Refinancing rate risk indicator Maturity structure of borrowing 2020-21	TMS 2021-22 Upper limit %	TMS 2021-22 Lower limit %	Projection 31-3-22 %
Under 12 months	50	-	19.87
12 months and within 24 months	25	-	-
24 months and within 5 years	25	-	9.59
5 years and within 10 years	40	-	16.33
10 years and within 20 years	50	-	16.64
20 years and above	60	25	37.57

The 19.87% shown in Table 3 above relates to the £19.25 million LOBO loans which may be re-scheduled in advance of their maturity date of 2054, as detailed in the paragraph above. The CIPFA Code requires the maturity of LOBO loans to be shown as the earliest date on which the lender can require payment, i.e. the option/call dates in 2021-22, so the maturity date is actually uncertain but is shown in the "Under 12 months" category as per the Code.

4. Investment Strategy and Outturn 1 April to 30 September 2021

Both the CIPFA Code and the WG Guidance require the Council to invest its funds prudently and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, balancing the risk of incurring losses from defaults against receiving unsuitably low investment income.

The major objectives during 2021-22 were:-

- To maintain capital **security**

- To maintain **liquidity** so funds are available when expenditure is needed
- To achieve the **yield** on investments commensurate with the proper levels of security and liquidity

The Annual Investment Strategy incorporated in the Council's TMS 2021-22 includes the credit ratings defined for each category of investments and the liquidity of investments. The Council's investments have historically been placed in mainly short-term bank and building society unsecured deposits and local and central government. However, investments may be made with any public or private sector organisations that meet the minimum credit criteria and investment limits specified in the Investment Strategy. The majority of the Council's surplus cash is currently invested in Money Market Funds and with other local authorities, but the Council will continue to look at investment options in line with the limits detailed in the Investment Strategy. In the last 6 months Arlingclose has been constantly stress testing the financial institutions on its recommended counterparty list during the pandemic and, as a result, has removed a number from its recommended list for unsecured deposits and revised the credit rating, outlook and recommended deposit period for a number of others. This reflects the revised likely credit worthiness of the institutions from the economic and financial market implications of coronavirus. The Council takes into account updated advice from its advisors before making any investment decisions.

The Council holds surplus funds representing income received in advance of expenditure plus balances and reserves and as shown in Table 1 above, the balance on investments at 30 September 2021 was £79.84 million. Table 4 below details these investments by counterparty type. The average investment rate in the period 1 April to 30 September 2021 was 0.08% (Table 4) and was 0.06% at 30 September 2021 (Table 1 – Total Treasury Investments).

Table 4: Investments Profile 1 April to 30 September 2021

Investment Counterparty Category	Balance 01 April 2021 (A) £m	Investments raised (B) £m	Investments Repaid (C) £m	Balance 30 September 2021 (A+B-C) £m	Investment income received** Apr-Sept 2021 £'000	Average original duration of the Investment Days	Weighted average investment balance Apr-Sept 2021 £m	Weighted average interest rate Apr-Sept 21 %
Government DMO	-	173.50	158.16	15.34	0.63	12	10.63	0.01
Local Authorities	48.50	35.50	55.50	28.50	65.08	192	25.19	0.18
Banks (Fixed Maturity)	1.00	24.00	16.00	9.00	1.62	32	2.69	0.07
Banks Instant Access/Notice Period Account	-	3.00	-	3.00	0.09	-	5.90	0.03
Building Societies	-	-	-	-	-	-	-	-
Money Market Fund (Instant Access)	2.05	33.85	11.90	24.00	1.78	-	22.56	0.02
Total/Average	51.55	269.85	241.56	79.84	69.20	166	66.97	0.08

** actual income received in year excluding accruals

The Treasury Management indicator shown below in Table 5 is for Principal Sums Invested for periods longer than a year. Where the Council invests, or plans to invest, for periods longer than a year, an upper limit is set for each forward financial year period for the maturing of such investments. The purpose

of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of long-term investments. The limit on the long-term principal sum invested to final maturities beyond the period end are set out in the TMS 2021-22.

Table 5: Treasury Management Indicator Principal Sums Invested for periods longer than a year

Price risk indicator	TMS 2021-22 £m	Projection 31-3-22 £m
Limit on principal invested beyond financial year end	15	Nil

All investments longer than 365 days (non-specified) will be made with a cautious approach to cash flow requirements and advice from Arlingclose will be sought as necessary.

There were no long-term investments (original duration of 12 months or more) outstanding at 30 September 2021. All investments at 30 September 2021 were short term deposits including Government Debt Management Office (DMO), Money Market Funds, Local Authorities, instant access and notice accounts. Table 6 below details these investments by counterparty type based on the remaining maturity period as at 30 September 2021:

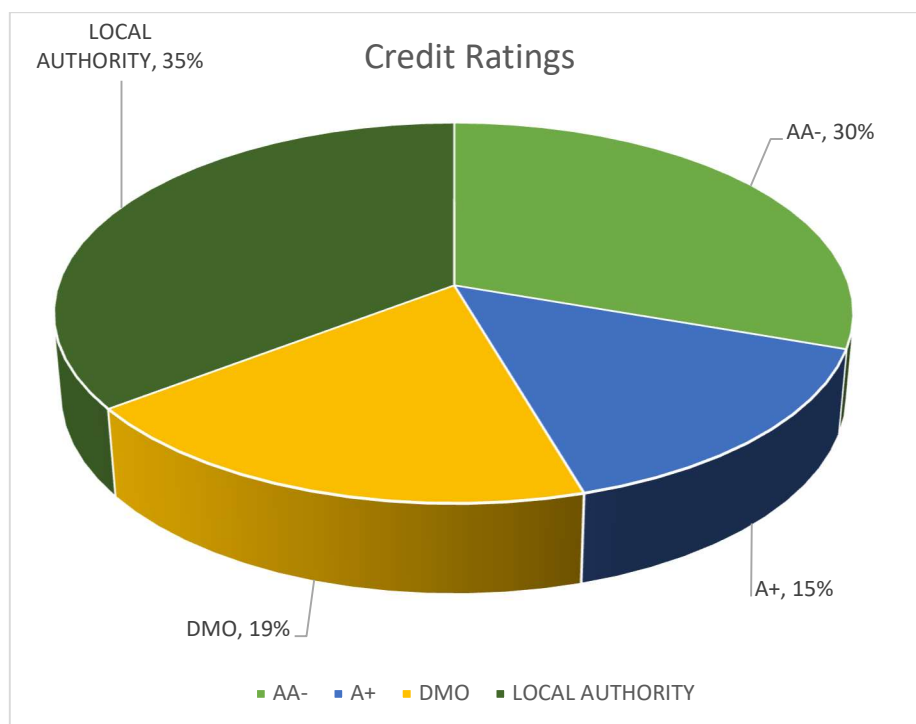
Table 6: Investments Outstanding Maturity Profile 30 September 2021

Counterparty Category	Instant Access £m	Deposits Maturing Within 1 Month £m	Deposits Maturing Within 2-3 Months £m	Deposits Maturing Within 4-12 Months £m	Total £m
Government DMO		15.34			15.34
Local Authorities			4.50	24.00	28.50
Banks	3.00	9.00			12.00
Building Societies					0.00
Money Market Funds	24.00				24.00
Total	27.00	24.34	4.50	24.00	79.84

Investment decisions are made by reference to the lowest published long-term credit rating from a selection of external rating agencies to ensure that this lies within the Council's agreed minimum credit rating. Where available the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account. **Appendix B** shows the equivalence table for credit ratings for three of the main rating agencies Fitch, Moody's and Standard & Poor's and explains the different investment grades. The Council defines high credit quality as organisations and securities having a

credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher.

The pie chart below summarises Table 6 by credit ratings and shows the £79.84 million investments at 30 September 2021 by percentage. Most Local Authorities do not have credit ratings and the £24 million invested with AA- rated MMF's were on an approved counterparty by Arlingclose, whilst the remainder of the investments all had a credit rating of A or above.



5. Interest Rate Exposures – Borrowing and Investments

The Council is exposed to interest rate movements on its borrowings and investments. Movements in interest rates have a complex impact on the Council depending on how variable and fixed interest rates move across differing financial instrument periods. Short term and variable rate loans expose the Council to the risk of short-term interest rate rises and are therefore subject to the Treasury Management indicator in Table 7 below to manage Interest Rate Exposures.

Table 7: Treasury Management Indicator Interest Rate Exposures

Interest rate risk indicator	Indicator £'000	As at 30-09-21 £'000
One year revenue impact of a 1% rise in interest rates	(273)	(573)
One year revenue impact of a 1% fall in interest rates	474	765

This has been set as an **indicator** (not a limit) to measure the net impact over one year on the revenue account of both a 1% rise and a 1% fall in all interest rates for borrowing net of treasury investments. This is calculated at a point in time on the assumption that maturing loans and investments will be replaced at rates 1% higher or lower than they would otherwise have been on their maturity dates and that the treasury investment and borrowing portfolios remain unchanged over the coming year. Interest rates can move by more than 1% over the course of a year, although such instances are rare.

The figures for the 1% fall in interest rates indicator are not the same figures as the 1% rise in interest rates (but reversed) as the borrowing relates to variable LOBO loans where it is assumed that the lender would not exercise their option if there was a fall in interest rates. All other borrowing does not have a rate reset in the next year and is with the PWLB at fixed rates

6. Review of the Treasury Management Strategy 2021-22

CIPFA's Code of Practice for Treasury Management requires all local authorities to conduct a mid-year review of its treasury management policies, practices and activities. The outcome of this review is that no changes to the TMS 2021-22 are required at this time.

APPENDIX B

Credit Rating Equivalence Table

	Description	Fitch		Moody's		Standard & Poor's	
		Long	Short	Long	Short	Long	Short
INVESTMENT GRADE	Extremely strong	AAA		Aaa		AAA	
	Very strong	AA+	F1+	Aa1	P-1	AA+	A-1+
		AA		Aa2		AA	
		AA-		Aa3		AA-	
	Strong	A+	F1	A1	P-2	A+	A-1
		A		A2		A	
	Adequate	A-	F2	A3	P-3	A-	A-2
		BBB+		Baa1		BBB+	
		BBB		Baa2		BBB	
	SPECULATIVE GRADE	Speculative	BBB-	F3	Baa3	Not Prime (NP)	BBB-
BB+			Ba1		BB+		
BB			Ba2		BB		
Very speculative		BB-	B	Ba3	Not Prime (NP)	BB-	B
		B+		B1		B+	
		B		B2		B	
Vulnerable		B-	C	B3	Not Prime (NP)	B-	C
		CCC+		Caa1		CCC+	
		CCC		Caa2		CCC	
		CCC-		Caa3		CCC-	
	CC	Ca		CC			
Defaulting	C				C		
	D	D	C		D	D	

Standard & Poor's (S&P), Moody's and Fitch are the three most significant rating agencies in the world. These agencies rate the creditworthiness of countries and private enterprises.

"AAA" or "Aaa" is the highest rating across all three rating agencies and indicates the highest level of creditworthiness. A "D" rating ("C" rating from Moody's) indicates poor creditworthiness of a company or government. A difference is made between short-term and long-term ratings.