CAMBRIDGESHIRE
& PETERBOROUGH
COMBINED AUTHORITY

Agenda Item No: 12

Treasury Management Strategy Update

To:	Audit and Governance Committee
Meeting Date:	26th November 2021
Public report:	Yes
From:	Robert Emery, Chief Accountant and Deputy S73 Officer
Key decision:	No
Forward Plan ref:	
Recommendations:	The Audit and Governance Committee is recommended to:

a) Note and review in year performance against the adopted prudential and treasury indicators.

Voting arrangements: No vote, noting item.

1. Purpose

1.1. The purpose of the report is for the Audit and Governance Committee to review the in year actual performance to 31st October 2021 against the prudential indicators included within the Treasury Management and Capital Strategies.

2. Background

2.1. According to its Terms of Reference, the Audit and Governance Committee shall "ensure there is effective scrutiny of the treasury management strategy and policies in accordance with CIPFA's Code of Practice".

2.2. The Treasury Management in the Public Services: Code of Practice 2017 recommends that Members receive regular reports on the authority's treasury management policies, practices and activities, including a mid-year review progress report.

Treasury Management Strategy Prudential Indicators

2.3. The Prudential Code underpins the system of capital finance. Prudential indicators are developed to ensure that:

(a) Capital investment plans are affordable;
(b) All external borrowing and other long-term liabilities are within prudent and sustainable levels; and
(c) Treasury management decisions are taken in accordance with professional good advice.

2.4. The current performance against the adopted Prudential Indicators is shown at appendix 1.

2.5. In previous reports, the indicator for Principal Sums Invested for Periods Longer than a year had been calculated to include all investments with maturities beyond the relevant year end date. Upon further investigation it has been confirmed that it should only include investments with an original duration of longer than a year.
This has the effect of significantly reducing our principal invested beyond year-end for the current year as this had previously shown all Treasury Management investments that would be in place on the 31st March 2022 and now only shows those investments which were made for longer than 12 months.

2.6. The Chief Accountant reports that, despite being increased for the 21/22 Treasury Management strategy, the Interest Rate Risk Exposure indicator has again been breached. This is due to higher levels of liquid funds being held to meet operational needs in the next 12 months. This position is expected to continue into 22/23 and is driven primarily by the delay in expenditure of the £79m grant fund on the Green Homes retrofit programme.

2.7. The level of short-term investments held, which drives this indicator, are dictated by the need to manage forecast cashflows to meet anticipated need. Where grant periods are due to complete the Combined Authority takes the prudent approach of assuming no extension will be granted until it is confirmed by the funder; as such we ensure sufficient cash is available to repay any unspent funds after the grant period concludes. Where we have large grants with short delivery windows, like the Green Homes retrofit programme for which the Combined Authority received £79m for delivery over 12 months, we cannot invest the funds significantly beyond the grant period and so this indicator is driven significantly higher. Given this position is expected to continue the appropriateness of this indicator for managing the Combined Authority's interest rate risk will be reviewed for the 22/23 Treasury Management Strategy.

Investment Activity

2.8. Surplus cash balances are held in accordance with the principles set out in the Treasury Management Strategy in order to support strategic investment decisions, the Capital Programme, and the Medium-Term Financial Plan (MTFP).

2.9. Forecast investment returns for 2021-22 are £374k against a budget of £231k. This is due to having higher than anticipated investment balances and to a number of multi-year deals which were made at a rate of interest significantly higher than that available for shorter term investments.

2.10. Table 1 below shows the treasury management position at 31st March 2021 and the position as at 31st October 2021. The CPCA has undertaken no borrowing in 2020-21 so there is no corresponding summary for debt.

Table 1: Treasury Management Summary

	As at 31.3.2021		**As at 31.10.2021**	
	Balance (£m)	**Average Rate**	**Balance (£m)**	**Average Rate**
Fixed Term Deposits				
Local Authority, time to maturity:				
Less than 3 months	40	0.33%	48	0.22%
3-6 months	45	0.32%	65	0.14%
7-9 months	43	0.26%	3	0.15%
10-12 months	50	0.20%	30	0.11%
Longer than 12 months	10	0.61%	10	0.61%
Total Local Authority	**188**	**0.29%**	**156**	**0.19%**
DMO*				
Less than 3 months	0	-	45	0.01%
3-6 months	0	-	5	0.07%
Immediate Access				
Call Account	11	0.00%	1	0.01%
Money Market Funds	32	0.01%	32	0.01%
Total investments	**231**	**0.24%**	**239**	**0.13%**

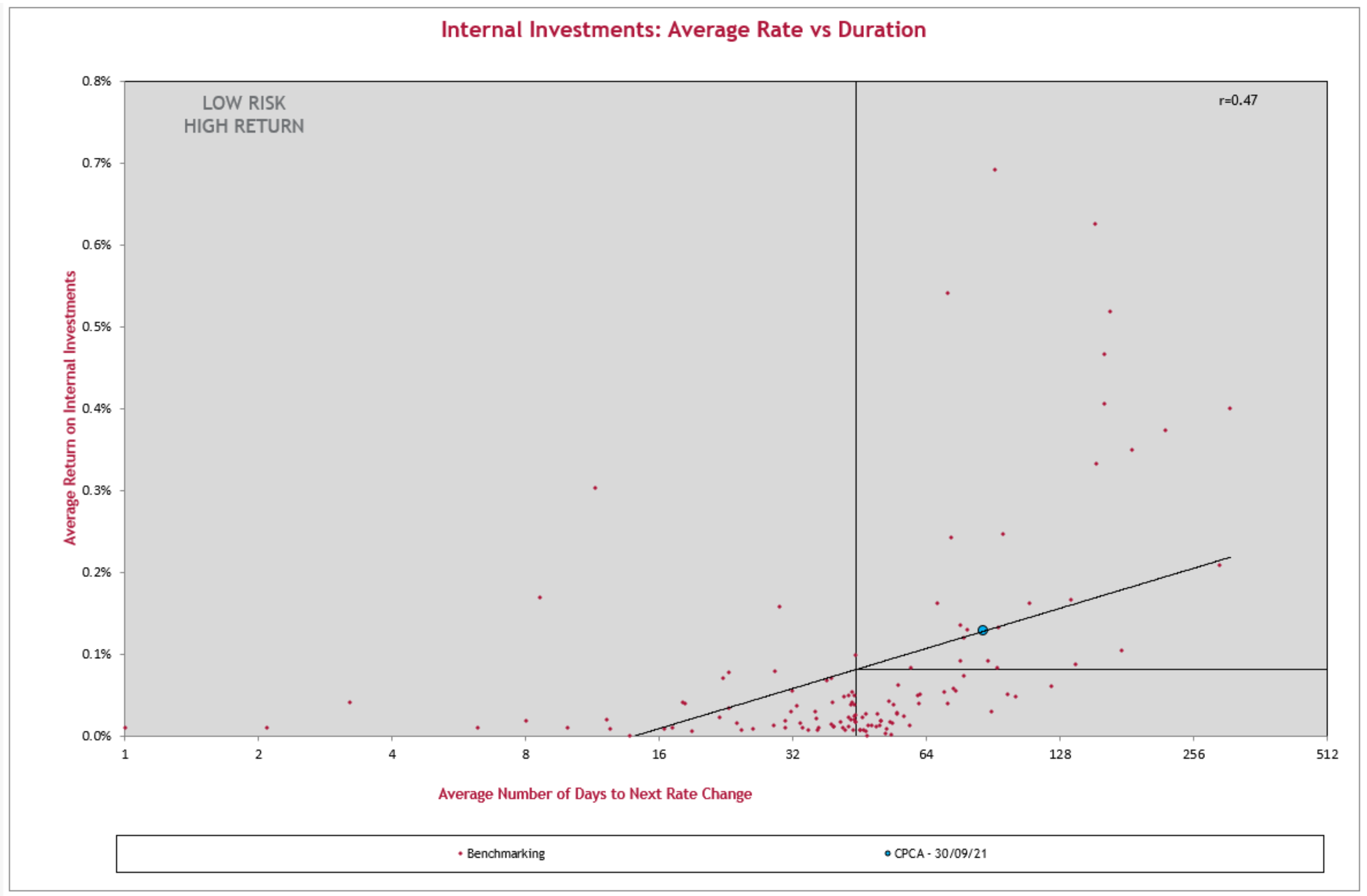
**DMO (formally the Debt Management Account Deposit Facility) is a government department which offers risk-free deposits for Local Authorities.*

2.11. In response to the global economic recession due to COVID the Bank of England, in line with many national and international institutions has reduced the cost of borrowing (the base rate) to historically low levels. The cost of debt from the Bank has a knock-on effect on lending rates across the country.

2.12. As we predominantly lend to other Local Authorities this reduction in the cost of debt is further exacerbated as Government has made substantial cash injections into the sector and projects have been put on hold, reducing the demand for borrowing and thus the rates achievable, although there are signs that the impact of this is starting to diminsh.

2.13. Interest rates expected to rise slowly over the next few quarters but still remain at historically low levels.

2.14. The investment portfolio compares as expected against benchmarking data for internal investments provided by our treasury management advisors, Arlingclose. The graph below shows average rate against the average remaining duration of investments. The Authority's portfolio sits on the trend line, at above both average rate and duration; this was a conscious decision to, where possible, take longer term deals in order to achieve an improved rate of return while maintaining required liquidity and security.

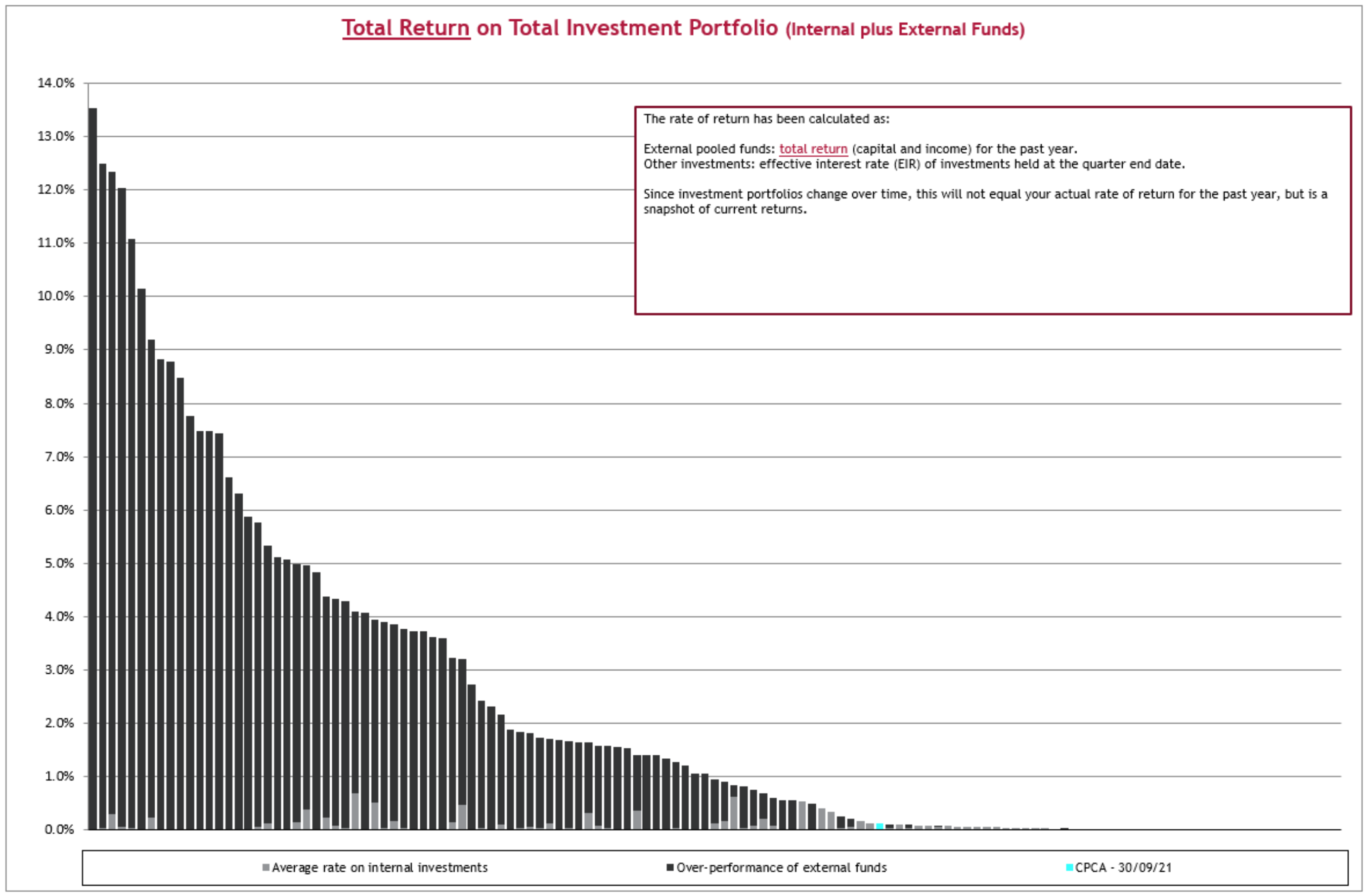


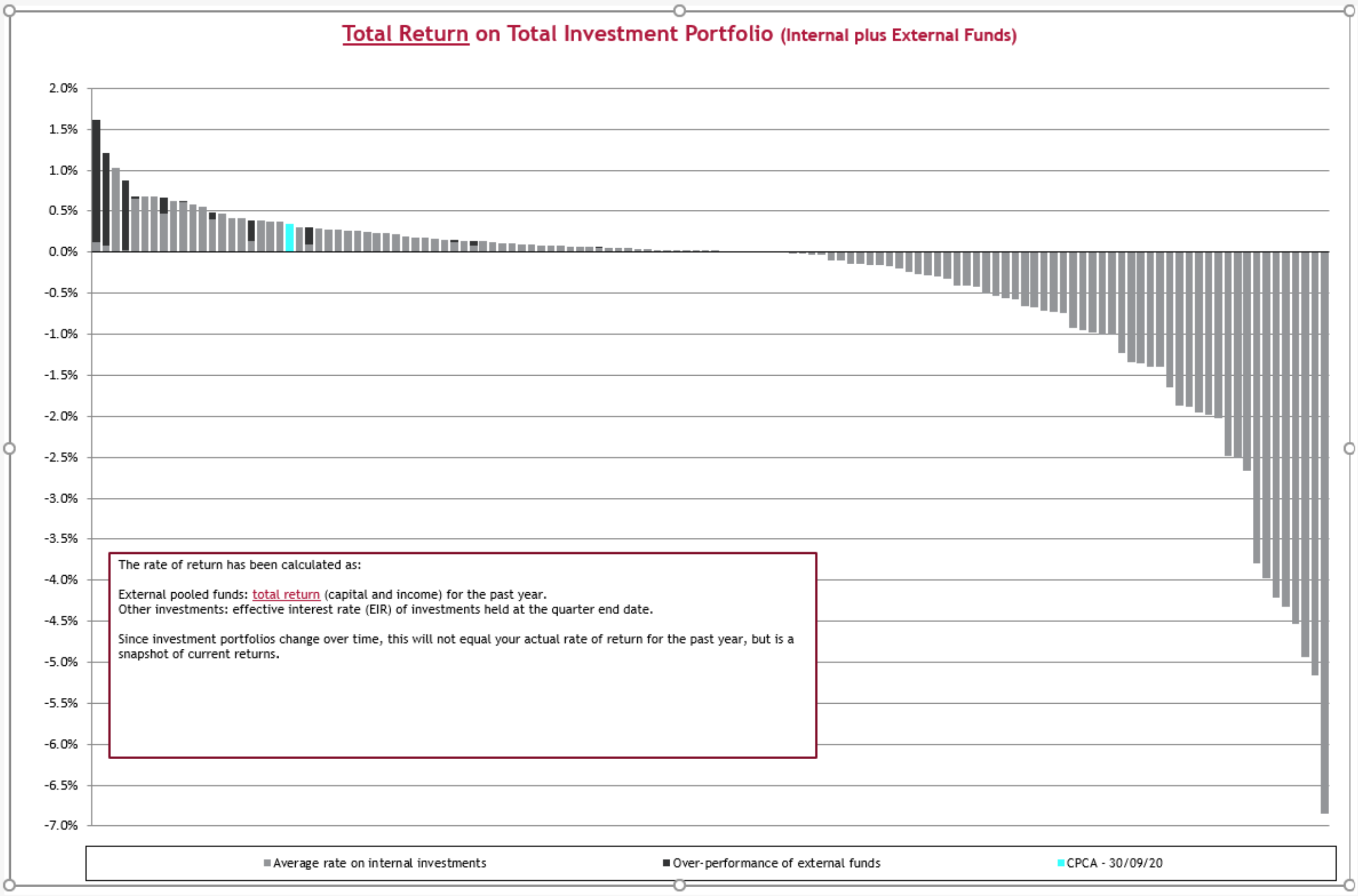
2.15. When compared against total returns against other Local Authorities, the portfolio compares less well as seen in the first graph below. For comparison, the second graph below shows that the portfolio compared favourably against total returns one year ago.

2.16. This is due to the inclusion of externally managed strategic investments where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and long-term price stability. Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years; but with the confidence that over a three- to five-year period total returns will exceed cash interest rates. Last year capital values were down due to the pandemic and thus the Combined Authority's portfolio compared favourably, as the market 'bounces back' capital values recover, and thus strategic funds are currently benefiting from higher returns. The Authority doesn't currently have any externally managed strategic investments.

2.17. The Authority's current Investment Strategy as set out in the Treasury Management Strategy is:
Given the increasing risk and very low returns from short-term unsecured bank investments, the Authority will continue to diversify into more secure and/or higher yielding asset classes during 2021/22. Due to current liquidity requirements, an increasing proportion of the Authority's surplus cash is currently invested in short-term unsecured bank deposits, and money market funds.

2.18. In line with the strategy, current market conditions and the Authority's long term cash flow forecast, officers are considering options for diversifying some balances available for longer term investments into higher yielding, more volatile asset classes.


Total Return on Total Investment Portfolio (Internal plus External Funds)
14.0%
13.0%
12.0%
11.0%
10.0%
9.0%
8.0%
7.0%
6.0%
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
The rate of return has been calculated as:
External pooled funds: total return (capital and income) for the past year.
Other investments: effective interest rate (EIR) of investments held at the quarter end date.
Since investment portfolios change over time, this will not equal your actual rate of return for the past year, but is a snapshot of current returns.
Average rate on internal investments
Over-performance of external funds
CPCA - 30/09/21


Total Return on Total Investment Portfolio (Internal plus External Funds)
2.0%
1.5%
1.0%
0.5%
0.0%
-0.5%
-1.0%
-1.5%
-2.0%
-2.5%
-3.0%
-3.5%
-4.0%
-4.5%
-5.0%
-5.5%
-6.0%
-6.5%
-7.0%
The rate of return has been calculated as:
External pooled funds: total return (capital and income) for the past year.
Other investments: effective interest rate (EIR) of investments held at the quarter end date.
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Average rate on internal investments
Over-performance of external funds
CPCA - 30/09/20

Significant Implications

3. Financial Implications

3.1. None other than those highlighted in the main body of the report.

4. Legal Implications

4.1. Treasury Management activities have to conform to the Local Government Act 2003, the Local Authorities (Capital; Finance and Accounting) (England) Regulations 2003 (SI 2003/3146), which specifies that the Council is required to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice and also the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (SI 2008/414), which clarifies the requirements of the Minimum Revenue Provision guidance.

5. Other Significant Implications

5.1. There are no significant implications not discussed above.

6. Appendices

6.1. Appendix 1: 21/22 Mid year Performance against Treasury Management and Capital Indicators and Limits

7. Background Papers

7.1. CPCA Capital Strategy: 24 March 2021 Combined Authority Board Item 2.2 App 1a

7.2. CPCA Treasury Management Strategy: 24 March 2021 Combined Authority Board Item 2.2 App 1b

Appendix 1 – 2021 Performance against Treasury Management and Capital Indicators and Limits

Treasury Management Indicators

The Authority measures and manages its exposures to treasury management risks using the following indicators, compliance has been indicated for each:

1. **Investment limits**: In order to minimise the risk of a single default against available reserves, the maximum that will be lent to any one organisation (other than the UK Government) will be £25m. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

		Cash limit per the 21-22 Treasury Management Strategy	Maximum balance held in 2021-22 financial year	Complied?
Any single organisation, except the UK Central Government		£25m each	£25m	Yes
UK Central Government		unlimited	£72m	Yes
Any group of organisations under the same ownership		£25m per group	£0	Yes
Any group of pooled funds under the same management		£50m per manager	£0	Yes
Negotiable instruments held in a broker's nominee account		£50m per broker	£0	Yes
Foreign countries		£25m per country	£0	Yes
Local authorities & other government entities	Counterparty limit	£25m	£25m	Yes
	Sector limit	Unlimited	£198m	Yes
Secured investments	Counterparty limit	£25m	£0	Yes
	Sector limit	Unlimited	£0	Yes
Operational bank account	Counterparty limit	£25m	£16m	Yes
Banks (unsecured), excluding operational account	Counterparty limit	£15m	£0	Yes
	Sector limit	Unlimited	£0	Yes
Building societies (unsecured)	Counterparty limit	£15m	£0	Yes
	Sector limit	£25m	£0	Yes
Registered providers (unsecured)	Counterparty limit	£15m	£0	Yes
	Sector limit	£50m	£0	Yes
Money market funds	Counterparty limit	£25m	£14m	Yes
	Sector limit	Unlimited	£32m	Yes
Strategic Pooled funds	Counterparty limit	£25m	£0	Yes
	Sector limit	£100m	£0	Yes

Real estate investment trusts	Counterparty limit	£25m	£0	Yes
	Sector limit	£50m	£0	Yes
Other investments	Counterparty limit	£15m	£0	Yes
	Sector limit	£25m	£0	Yes

2. **Security:** The Authority has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit score of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

	30.9.21 Actual	2021/22 Target	Complied?
Portfolio average credit score (lower is better)	4.40 (AA-)	6 (A)	Yes

This indicator is provided as at 30.09.21 as it is calculated by our Treasury Management advisors as part of our quarterly benchmarking. The credit rating of investments as at 31.10.2021 is not materially different from the position as at 30.09.2021

3. **Liquidity:** The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount cash available to meet unexpected payments within a rolling three month period, without additional borrowing.

	31.10.21 Actual	2021/22 Target	Complied?
Total cash available within 3 months	£81m	£50m	Yes

4. **Interest Rate Exposures**: This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interests was:

Interest rate risk indicator	31.3.21 Actual	2021/22 Limit	Complied?
Upper limit on one-year revenue impact of a 1% rise in interest rates	£1.64m	£1.5m	No
Upper limit on one-year revenue impact of a 1% fall in interest rates	£1.64m	£1.5m	No

The impact of a change in interest rates is calculated on the assumption that maturing loans and investment will be replaced at current rates.

5. **Principal Sums Invested for Periods Longer than a year:** The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end were:

	2021/22	2022/23	2023/24
Actual long term principal invested beyond year end	£10m	£0m	£0m
Limit on long term principal invested beyond year end	£160m	£50m	£50m
Complied?	Yes	Yes	Yes

Capital Strategy Indicators

1. **Capital Expenditure in £ millions.** The table shows the Combined Authority's capital expenditure for 2021/22, and the following two financial years based on the medium-term financial plan.

	2021/22 budget	2021/22 forecast	2022/23 budget	2023/24 budget
Capital investments	239.78	223.01	61.90	37.28
TOTAL	**239.78**	**223.01**	**61.90**	**37.28**

2. **Indicator 2 – Capital Financing in £ millions.** All capital expenditure must be financed, either from external sources (government grants and other contributions), the Authority's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing and Private Finance Initiative). The financing of the above expenditure is as follows:

	2021/22 budget	2021/22 forecast
Grant funding	210.76	196.37
Usable Capital Receipts	29.02	26.64
Debt	0	0
TOTAL	**239.78**	**223.01**

3. **Indicator 3 – Gross Debt and the Capital Financing Requirement in £ millions.** The Authority's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with Minimum Revenue Provision (MRP) and capital receipts used to replace debt. The Authority currently has no debt and therefore no CFR. Projected levels of the Authority's total outstanding debt which comprises borrowing, PFI liabilities and leases are shown below, compared with the capital financing requirement.

	31.3.2022 budget	31.3.2022 forecast
Debt (incl. PFI & leases)	0	0
Capital Financing Requirement	0	0

4. **Indicator 4 – Borrowing and the Liability Benchmark in £ millions.** To compare the Authority's actual borrowing against an alternative strategy, a liability benchmark is calculated showing the lowest risk level of borrowing. Given that there are no current plans to borrow, this benchmark is currently set at the existing debt cap, but will be kept under review.

	31.3.2022 budget	31.3.2022 forecast
Outstanding borrowing	0	0
Liability benchmark	84.61	0

5. **Indicators 5 and 6 - Authorised limit and operational boundary for external debt in £ millions.** The Authority is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year and to keep it under review. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

	2021/22 limit	2021/22 forecast
Authorised limit – total external debt	84.61	0
Operational boundary – total external debt	74.61	0