

Epsom & Ewell Borough Council Treasury Management Training

1st December 2020

Presented by:
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Objectives for Today

- Gain an appreciation of what Treasury Management involves
- Gain an understanding of how Treasury Management is undertaken
- Understand the role of Officers and Members in Treasury Management decisions
- Understand the risks and opportunities in Treasury Management and how they should be managed
- Gain a broad appreciation of the impact of COVID-19 pandemic on the economic outlook and treasury management activities of the Council

Treasury Management Framework Overview

What is Treasury Management?

The management of the organisation's

- **Borrowing**
- **Investments**
- **Cash flows**
- **Banking**
- **Money market and capital market transactions**

– The **effective control of the risks** associated with those activities

– The **pursuit of optimum performance** consistent with those risks

Legal & Regulatory Requirements

Legislation



HM Government

- **Local Government Act 2003**

Statutory Guidance



Ministry of Housing,
Communities &
Local Government

- **Investment Guidance**
- **Minimum Revenue Provision Guidance**



- **Treasury Management Code of Practice**
- **Prudential Code**

Good Practice



BANK OF ENGLAND

- **UK Money Markets Code**

Legislation



Local Government Act 2003

CHAPTER ONE

S1 Power to Borrow

S2 Control of Borrowing

**S3 Affordable Borrowing
Limit**

S12 Power to Invest

**S15 Regard to Guidance
issued**

<http://www.legislation.gov.uk/ukpga/2003/26/contents>

Prudential Framework History

2004

2008

2017

FINANCIAL TIMES

Monday July 8 1991

Unrecorded deposits and loans were de

Secret bank in BCCI disguised large losses



Abu Dhabi

Lost in Iceland: £1 billion from councils, charities and police

- More than 100 public bodies had money in collapsed banks
- Brown accuses Icelandic authorities of acting illegally



▲ Iceland has failed to guarantee British savings in its failed banks. Photograph: Nordicphotos/Alamy

Gordon Brown last night branded Iceland's failure to guarantee British savings in its failed banks as "totally unacceptable and illegal", amid warnings that more than 100 local councils, police authorities and fire services have up to £1bn lost in its bankrupted system.

Councils bet billions on property purchases


Andrew Ellson
Consumer Affairs Correspondent

Britain's councils are making multi-billion-pound bets on commercial property as they try to replace revenue lost through government cuts, an investigation by *The Times* has found.

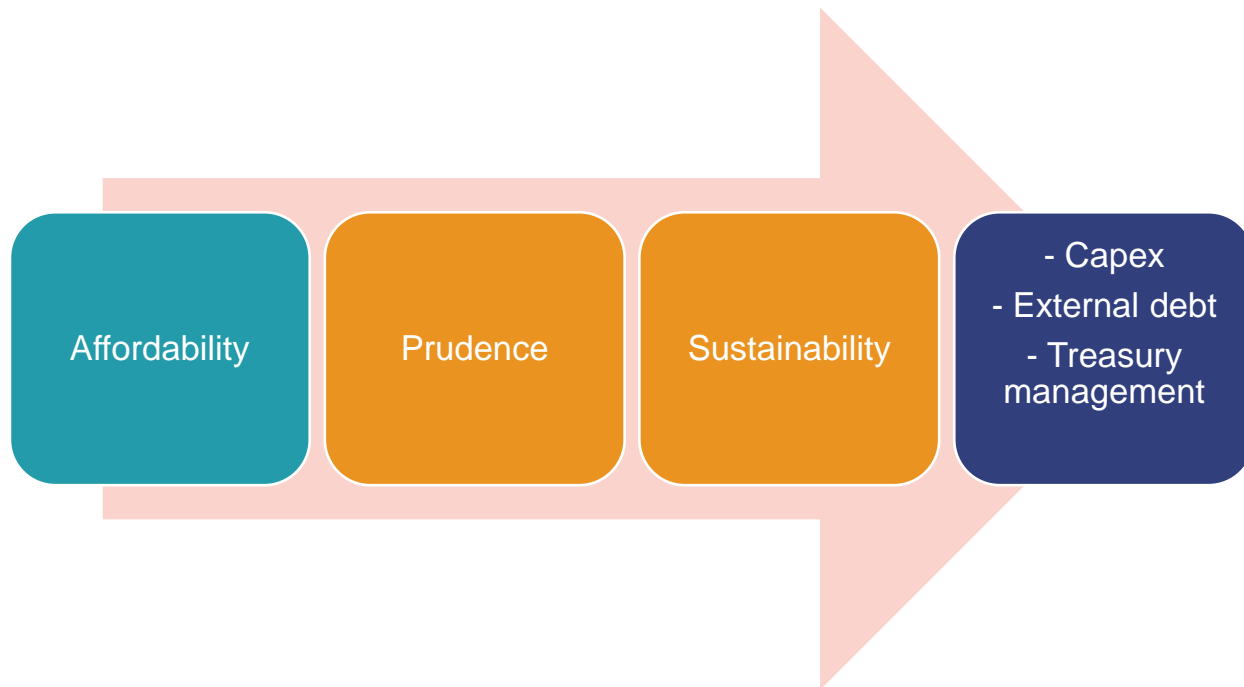
Local authorities are taking out loans to buy shop premises, offices and business parks despite having little or no investment experience, raising concerns that services will have to be reduced if the property bubble bursts.

Councils have paid £2.7 billion for commercial properties since 2015, up from £500 million over the previous

Prudential Code and Prudential Indicators

- 
- All local authorities must have regard to the Code
 - Code sets out Prudential Indicators
 - Approved by full Council / Authority meeting
 - Monitoring and reporting requirements
 - Code last refreshed 2017

What does the Prudential Indicators show?



Debt Management: Prudential Code...Key themes

Capital Financing Requirement

The CFR is the underlying need to borrow for capital purposes i.e. capital expenditure net of all capital receipts, grant, revenue contributions to capital outlay etc.

Operational Boundary

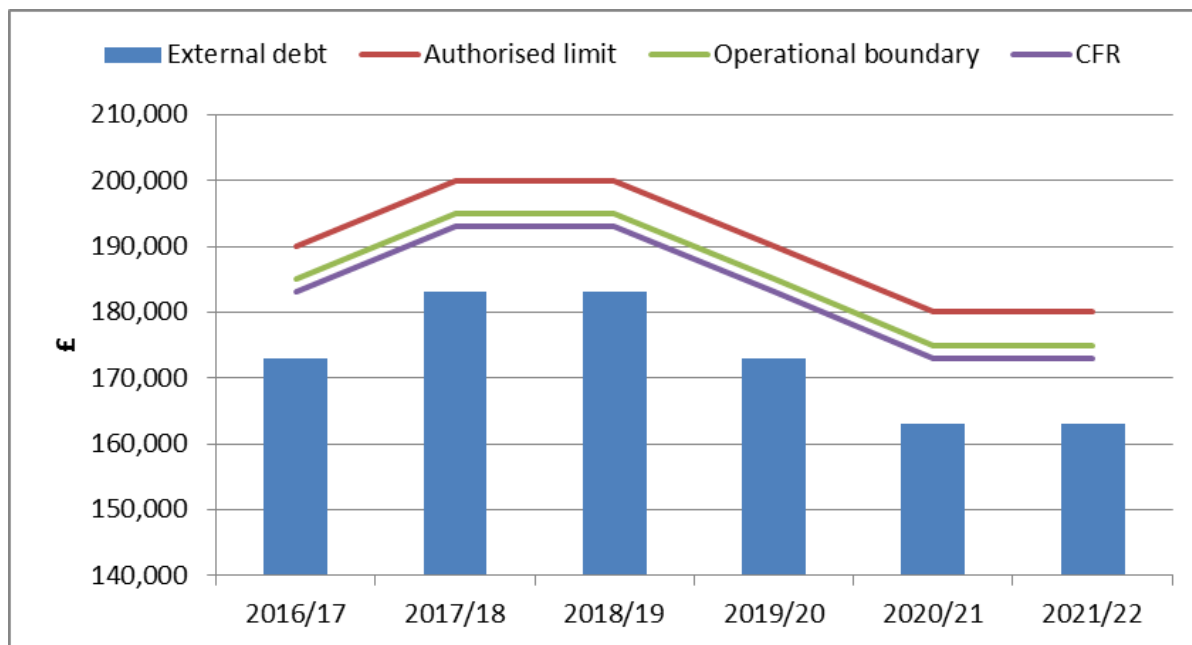
Total external debt – the most likely level – NOT worst case

Authorised Limit

Total external debt – the maximum permitted level i.e. “sufficient to allow for unusual cash movements”

Prudential Indicators can tell you what you need to do!

The gap between CFR and External Borrowing = Internal Borrowing



Internal vs. External Borrowing

First, why look to internally borrow (run down investments)?

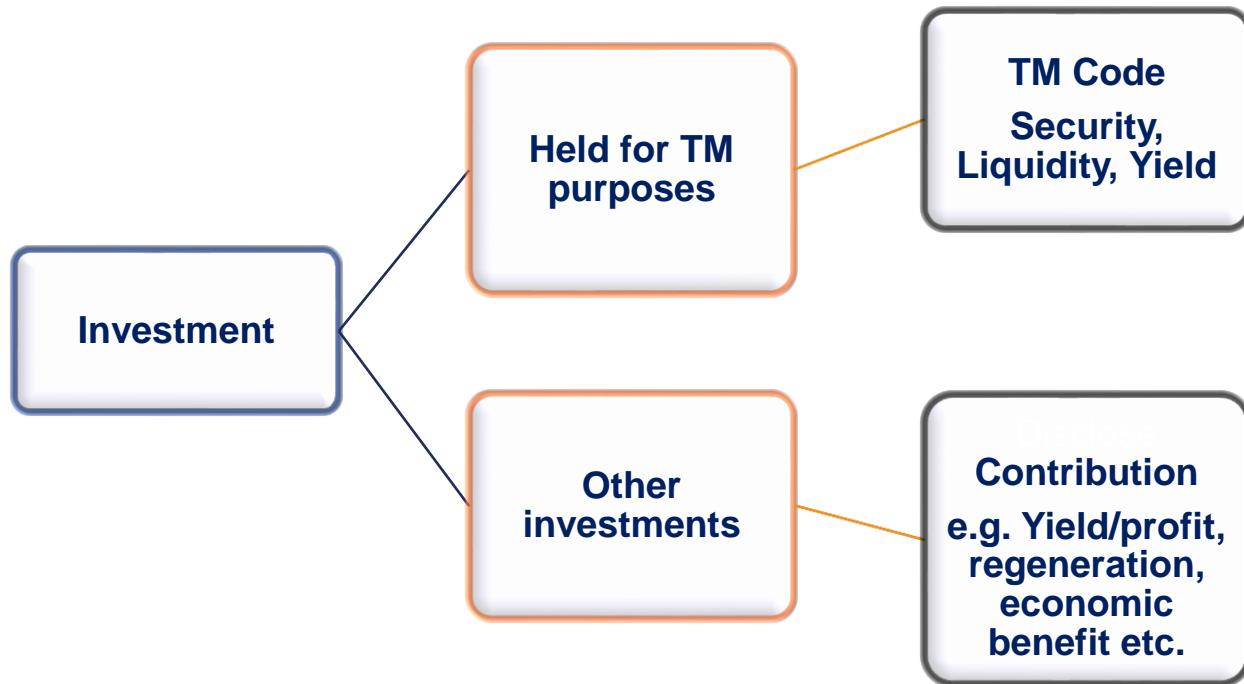


- Reduced counterparty risk
- Unattractive investment rates
- Avoid potential “cost of carry”



- Economic and political uncertainty
- How long can position be sustained...
- ...what is the need for certainty, usually driven by affordability criteria?

MHCLG Investment Guidance



Investments Not Part of TM Activity

- Section 8 of the TM Code introduces the **concept of proportionality** when an organisation supplements TM investment returns with investment returns from other financial assets and property
- An organisation should have robust procedures for **consideration of risk and return** and that these are applied to non-TM investment decisions. These must be included in your TM Practices
 - *How do you measure proportionality?*
 - *How do you apply Security, Liquidity, Yield concept to non-TM investments?*
- Any move away from this concept must be set out clearly in a **Member approved published schedule**

Remember “investment” in property, is capital spend, not placement of cash (Investment and SLY)

Reporting Requirements



Treasury Management Strategy Statement



Annual Investment Strategy



Capital Strategy



Annual Minimum Revenue Provision Statement



Mid-year report (as a minimum)



Annual Report (outturn report)

Summary

Legislation

Remember the legal & Regulatory background

TM Code

Covers Treasury & Non-Treasury Investments

Reporting

Understand minimum requirements

P.I's

Keep up to date!

Risk

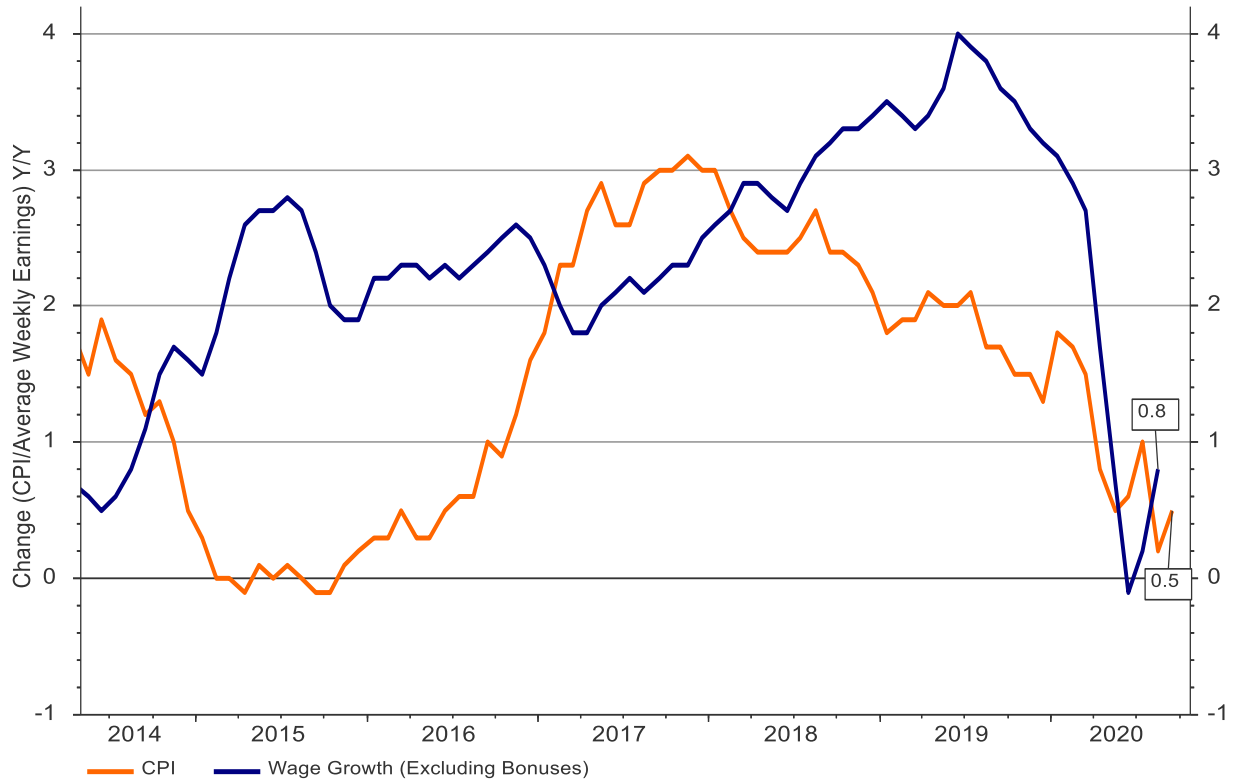
Responsibility lies with the organisation

Economic Outlook

Key Economic Indicators Comparison

	UK	EZ	US
Bank Rate	0.10%	0%	0%-0.25%
GDP	15.5%q/q (-9.6%y/y)	12.6%q/q (-4.4%y/y)	33.1% annual rate
Inflation	0.0%m/m (0.7%y/y)	0.2%m/m (-0.3%y/y)	1.2% annual rate
Unemployment Rate	4.8%	8.3%	6.9%

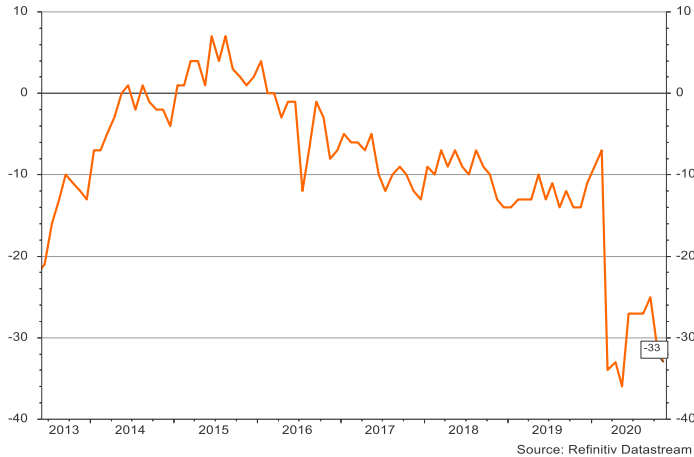
CPI Inflation v UK Wage Growth



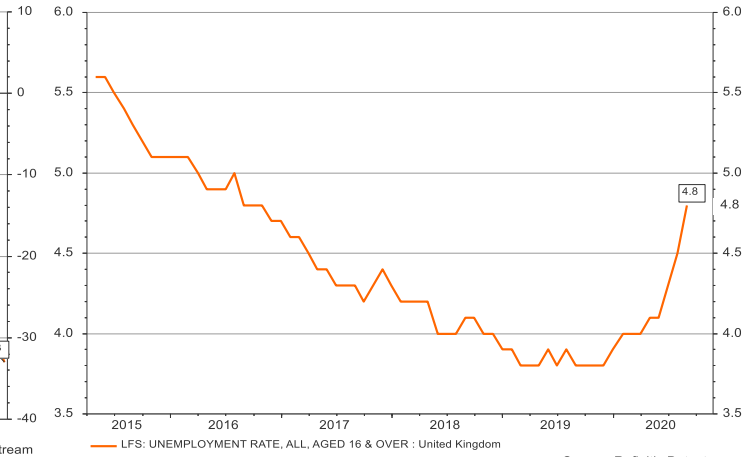
Source: Refinitiv Datastream

UK Employment and Consumer Confidence

GfK Consumer Confidence

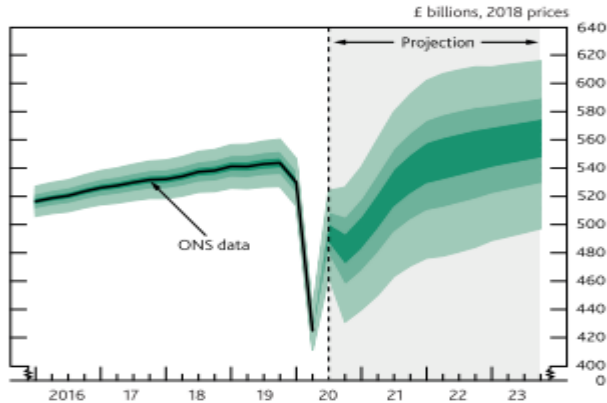


Unemployment

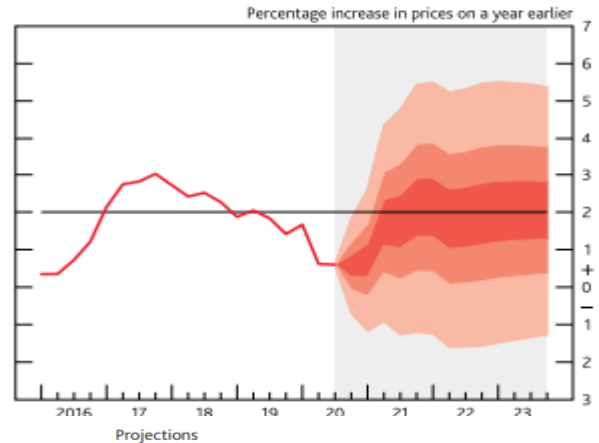


Bank of England Forecasts – November 2020

GDP



CPI



	2020 Q4	2021 Q4	2022 Q4	2023 Q4
GDP ^(c)	-11 (-5.4)	11 (6.2)	3.1 (2.3)	1.6
CPI inflation ^(d)	0.6 (0.3)	2.1 (1.8)	2.0 (2.1)	2.1
LFS unemployment rate	6.3 (7.5)	6.7 (5.9)	4.9 (4.5)	4.3
Excess supply/Excess demand ^(e)	-2¼ (-2¼)	-¼ (0)	+¼ (+¾)	+¼
Bank Rate ^(f)	0.1 (0.0)	-0.1 (-0.1)	-0.1 (-0.1)	0.0

UK Interest Rate Forecast

Bank Rate															
	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%
Capital Economics	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	-	-	-	-	-
5yr PWLB Rate															
	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	0.84%	0.80%	0.80%	0.80%	0.80%	0.80%	0.90%	0.90%	0.90%	0.90%	0.90%	1.00%	1.00%	1.00%	1.00%
Capital Economics	0.84%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	-	-	-	-	-
10yr PWLB Rate															
	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	1.14%	1.10%	1.10%	1.10%	1.10%	1.20%	1.20%	1.20%	1.30%	1.30%	1.30%	1.20%	1.30%	1.30%	1.30%
Capital Economics	1.14%	1.30%	1.30%	1.30%	1.30%	1.30%	1.30%	1.30%	1.30%	1.30%	-	-	-	-	-
25yr PWLB Rate															
	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	1.68%	1.50%	1.50%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.70%	1.80%	1.80%	1.80%	1.80%
Capital Economics	1.68%	1.80%	1.80%	1.80%	1.80%	1.80%	1.80%	1.80%	1.80%	1.80%	-	-	-	-	-
50yr PWLB Rate															
	NOW	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Link Group	1.51%	1.30%	1.30%	1.40%	1.40%	1.40%	1.40%	1.50%	1.50%	1.50%	1.50%	1.60%	1.60%	1.60%	1.60%
Capital Economics	1.51%	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	-	-	-	-	-

Please note – The current PWLB rates and forecast shown above have taken into account the 20 basis point certainty rate reduction from the new Standard Loan rate of 100bps over Gilts effective as of the 26th November 2020.

What does all this mean for Epsom & Ewell
BC?

Capital Financing and the Balance Sheet

Balance Sheet Review – Reserves & Balances

	2019	2020
Capital Financing Requirement	£86.9m	£91.7m
Less: Finance lease	(£3.4m)	(£3.0m)
Underlying Borrowing Requirement	£83.5m	£88.7m
External Borrowing	£64.4m	£64.4m
Internal Borrowing Position	£19.1m	£24.3m
Reserves & Balances	£28.9m	£32.1m
Working Capital Surplus	£3.8m	£7.4m
Investments	£13.6m	£15.2m

Capital Financing Requirement

	2019/20	2020/21	2021/22	2022/23
CFR	£91.7m	£139.9m	£138.0m	£136.0m

- 2020/21 CFR includes £55.6m of Commercial investment
- PWLB consultation has concluded with the following:
 - PWLB Certainty rate borrowing will revert back to October 2019 margins, gilt +80bpts
 - PWLB will not lend to any LA who has a debt to yield scheme in their capital programme

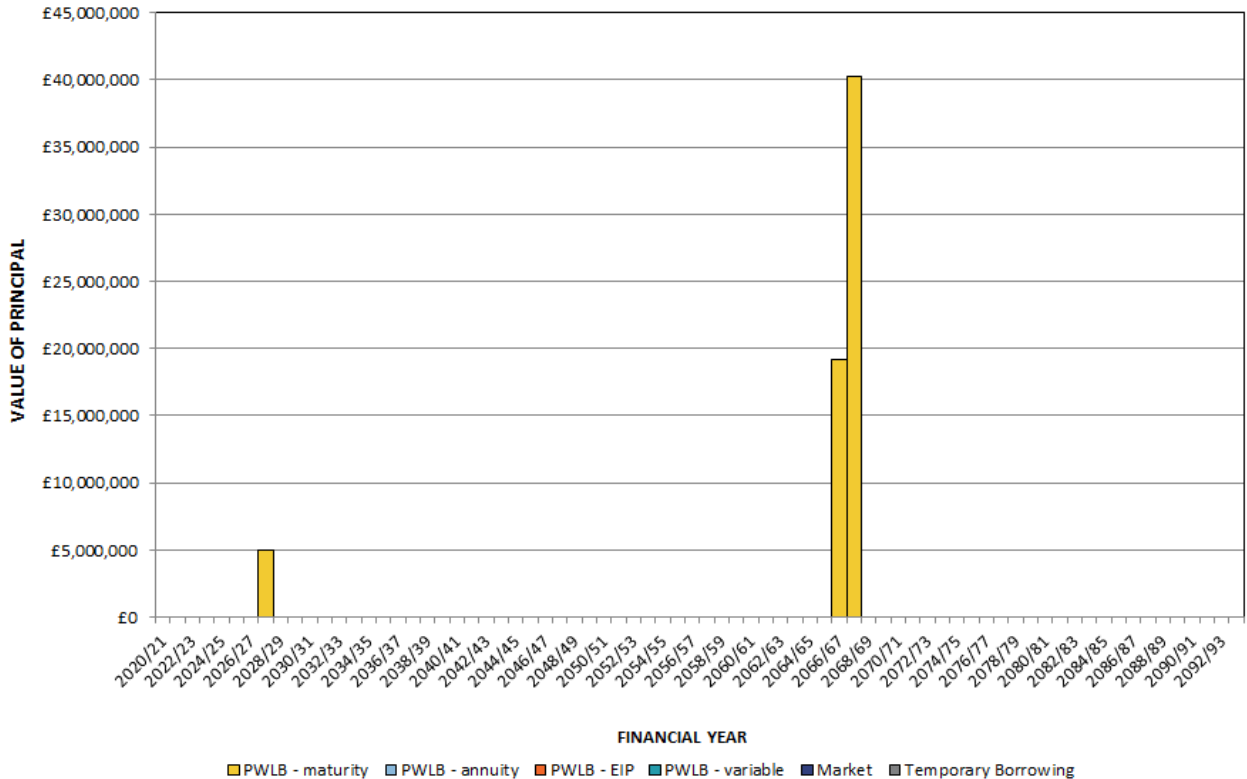
External Borrowing Considerations

- How much needs to be borrowed?
- Which type of borrowing (Internal / PWLB / market / temporary)
- How long to borrow for?
- What is your view on interest rates?
- Benchmark rate for borrowing?
- Fixed or variable rate borrowing?
- Loans fund repayments
- 3 year ahead time frame under the Prudential Code

Current Debt Portfolio

FIXED DEBT						
		Principal Outstanding	Discount	Premium	Average Rate	Average Life
PWLB	Maturity	£64,426,560	-	£47,036,825	2.523%	43.57 yr
	Annuity	-	-	-	-	-
	EIP	-	-	-	-	-
Total PWLB (fixed)		£64,426,560	-	£47,036,825	2.523%	43.57 yr
Market	Maturity	£0			-	-
	Annuity	£0			-	-
	Stock	£0			-	-
Total MARKET (fixed)		£0			0	0.00 yr
Total FIXED debt		£64,426,560	-	£47,036,825	2.523%	43.57 yr

Debt Maturity Profile



Investment Strategy

Why do you have investments?

What are the resources that back the investments?

- Provisions – cash put aside for a liability of uncertain timing or amount
- Grants and Contributions – cash received and yet to be spent
- Capital receipts – cash received and yet to be spent
- Earmarked reserves – cash put aside for specific purpose
- Balances – general cash not yet allocated
- Working Capital – debtors / creditors

Borrowing activity may impact upon the position as it will reduce / increase cash balances (and therefore investments)

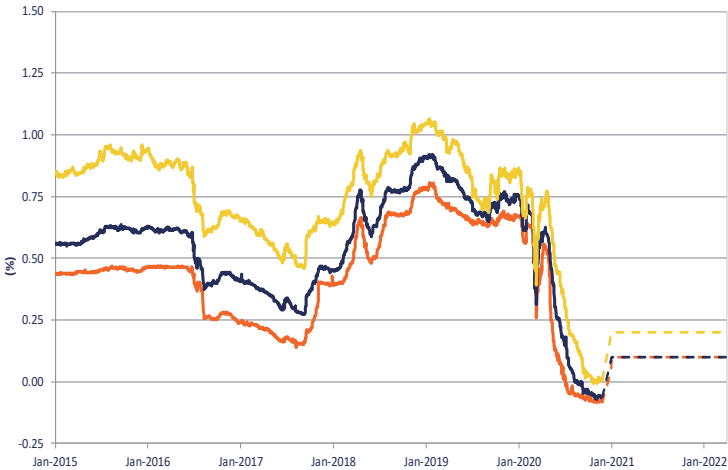
Investment Instruments

- **The UK's Debt Management Office (DMO)**
 - Fixed deposits up to 6 months
 - Risk versus reward trade off : exceptional credit quality versus low rate
- **Other Local Authorities**
- **Part-Nationalised Banks**
- UK Government Gilts / Treasury Bills
- **Banks** and Building Societies
- **Money Market Funds (MMFs)**
- Funds:
 - Property
 - Multi Asset
 - Bond
 - Equity

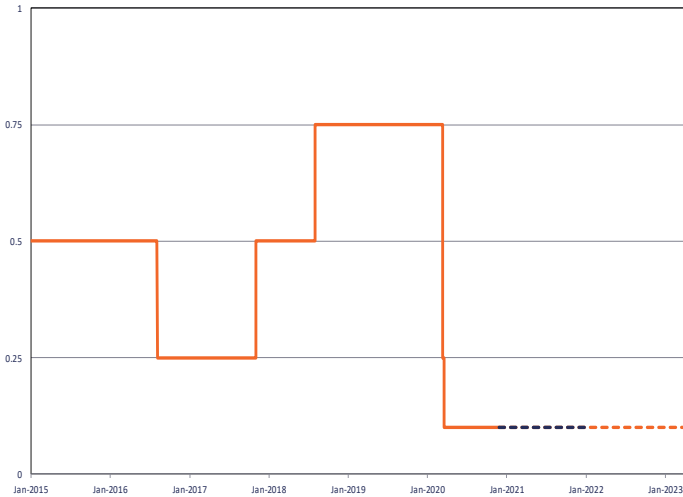
Current Investment Portfolio

Borrower	Principal (£)	Interest Rate	Start Date	Maturity Date	Lowest Long Term Rating	Historic Risk of Default
MMF Deutsche	5,000,000	0.01%		MMF	AAA	0.000%
MMF Goldman Sachs	5,000,000	0.01%		MMF	AAA	0.000%
MMF UBS	5,000,000	0.01%		MMF	AAA	0.000%
MMF SSgA	5,000,000	0.00%		MMF	AAA	0.000%
NatWest Markets Plc (NRFB)	900,000	0.01%		Call	BBB	0.000%
Total Investments	£20,900,000	0.01%				0.000%

UK Interest Rate Outlook



— 3m LIBID — 6m LIBID — 12m LIBID - - 3m LIBID Forecast - - 6m LIBID Forecast - - 12m LIBID Forecast



— Bank Rate - - Link Group Forecast - - CE Forecast

Link Group Interest Rate View

	Now	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
Bank Rate	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%
3 Month LIBID	-0.08%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%
6 Month LIBID	-0.06%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%
12 Month LIBID	0.01%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%

Summary

What does all this mean for Treasury Management?

- Significant uncertainty over direction of UK economy – Brexit/Covid-19
- Financial markets do not like uncertainty – can lead to market volatility
- Borrowing is very cheap...but, costs of carry remains a key consideration
- Limited movement expected in UK Bank Rate over next couple of years
- Investment Rates/Bank Rate could potentially turn negative next year.
- Counterparty risks in the financial markets have lessened, but not completely

Questions?

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